



# Budget Engagement Commission

*City of Arts & Innovation*

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**TO: HONORABLE COMMISSIONERS** **DATE: NOVEMBER 12, 2020**

**FROM: FINANCE DEPARTMENT** **WARDS: ALL**

**SUBJECT: FISCAL YEAR 2019/20 FINANCIAL UPDATE AND ADJUSTMENTS TO THE  
ADOPTED FISCAL YEAR 2020/21 EMERGENCY BUDGET**

## **ISSUES:**

That the Budget Engagement Commission receive the Fiscal Year 2019/20 financial update and adjustments to the adopted Fiscal Year 2020/21 Emergency Budget.

## **RECOMMENDATIONS:**

That the Budget Engagement Commission receive the Fiscal Year 2019/20 financial update and adjustments to the Adopted Fiscal Year 2020/21 Emergency Budget.

## **BACKGROUND:**

In March 2020, the Federal, State, County and City declared an emergency due to the COVID-19 pandemic. Subsequent State orders restricted human movement and caused the temporary closure of businesses. Staff immediately recognized that pandemic and related orders would likely have a significant and immediate impact on City finances and took immediate action to suspend recruitment for vacant positions and restrict spending to emergency and essential needs.

On June 16, 2020, the City Council adopted Resolution No. 23592 approving the Fiscal Year (FY) 2020-2021 (Emergency) Annual Budget. The adopted budget was the product of a truncated budget process prompted by the COVID-19 pandemic and Orders that limited the City's ability to receive the usual level of engagement in the budget process. Further, the impacts of the COVID-19 pandemic on City finances were largely unknown at the time of budget adoption due to the ongoing shut-down Order and uncertainty at all levels of the economy. As a part of the adoption of the emergency budget, staff committed to the City Council and the public that interim reports and recommendations to the adopted budget would be made as needed. On July 16, 2020, the Budget Engagement Commission (BEC) received a report on the FY 2020/21 Adopted Emergency Budget.

The City Council also received the FY 2019/20 Third Quarter Financial Report on June 16, 2020. In both reports, staff acknowledged the challenges in predicting the fiscal impacts of the pandemic on City finances while the Orders were still in place and with mixed economic news dominating the headlines. Staff estimated that FY 2019/20 General Fund revenues could fall short of budget projections by nearly 4%, particularly in sales tax due to business shutdowns, Transient

Occupancy Tax, and Non-Development Charges for Services (most notably, parks and recreation fees). Staff also noted in the FY 2020/21 emergency budget report that, while other Southern California cities were reducing General Fund revenue projections by as much as 25% and initiating drastic budget cuts, the revenue demographic of California cities is diverse, and staff believed a 10% contingency revenue reduction in the FY 2020/21 emergency budget was reasonable for the City – given Riverside’s diverse economy. Needed adjustments to the budget would be frequently brought forth as the economic landscape pivoted below our projections.

The Budget Engagement Commission (BEC) received the FY 2019/20 Third Quarter Financial Report on July 16, 2020.

On October 27, 2020 the City Council received a Fiscal Year 2019/20 financial update and recommended adjustments to the adopted FY 2020/21 Emergency Budget; this report to the BEC contains the same information presented to Council. There are no action items for the BEC resulting from this update.

## **DISCUSSION:**

As of the date of this report, fiscal year end processes and the external audit for FY 2019/20 are underway. A brief discussion of unaudited results and recent economic developments is included in this report; however, the final numbers are likely to be different from those presented in this report. It is anticipated that the final audited Comprehensive Annual Financial Report (CAFR) will be completed in December, after which the FY 2019/20 Fourth Quarter Financial Report will be presented to the BEC and City Council.

### **Economic Developments and Preliminary FY 2019/20 General Fund Results**

Since the onset of the COVID-19 pandemic in early spring and the various Executive Orders that followed, including the Governor’s shut-down order, the financial landscape of the City, region and State has continued to surprise experts. The temporary closure of businesses and high unemployment rate were just two factors that prompted economists’ dire warnings of economic fallout and staff’s Third Quarter analysis that projected a potential \$10 million shortfall in General Fund revenues.

Fortunately, the impact of the pandemic to the City’s budget has not been as drastic as originally expected. While there have been unfortunate impacts to the labor market and small business community, the impact to General Fund revenues has been relatively minimal. Overall, economists are proceeding with cautious optimism while acknowledging that the long-term effects of the pandemic will not be seen for some time. For example, the housing market has remained very active and favorable, but the impact of mortgage defaults and late rent payments due to high unemployment have yet to materialize and may likely occur in late FY 2020/21 if the pandemic continues into next calendar year.

Preliminary unaudited FY 2019/20 analysis indicates General Fund revenue results nearly in line with original projections, pre-COVID. In particular, sales tax revenue is one area where there was an expected decline in revenue due to the immediate shutdown of the economy and rapid loss of jobs. However, sales tax revenue for the FY2019/20 are projected to meet original budget targets. While there was a shift in sales tax revenue within the sales tax industry groups, the largest individual industry, Auto Sales and Transportation, performed well above pandemic projections, coming in just 1.8% below original pre-COVID projections. Some revenue shortfalls, particularly in Transient Occupancy Tax (\$1.2 million below projections) and Non-Development Charges for

Services (\$2.2 million below projections) are offset by outperforming revenues in Franchise Fees, Fines & Forfeitures, and others. However, significant expenditure impacts will be realized, including the General Fund subsidy of the Convention Center and Entertainment Fund operating losses totaling \$2.4 million above the budgeted subsidy for a total subsidy of approximately \$13.1 million inclusive of debt service of approximately \$6.7 million. The City's quick action in response to the pandemic to limit recruitment and spending to essential and emergency needs will offset those budget overages. With the additional benefit of savings generated by the City Manager's ongoing Managed Hiring initiative, significant one-year savings are anticipated for FY 2019/20, potentially achieving savings of approximately \$17 million (unaudited estimate). These savings will be critical to shore up City finances against the long-term fiscal impacts of COVID-19 on City finances as the impacts begin to materialize as well as other challenges and threats facing General Fund revenues.

Staff will return with the FY 2019/20 results following the conclusion of the financial audit, with recommendations related to General Fund savings. Prudent action will lead the City to review and reconsider some balancing measures adopted for FY 2020/21 (e.g. the withdrawal of Section 115 Pension Trust Funds) as well as potential areas of long-term fiscal risk that should be planned for.

### FY 2020/21 Emergency Budget Review

Due to the inability to predict the fiscal impact of COVID-19 at the time of budget adoption, only the General Fund and Measure Z were adjusted for potential COVID-19 impacts in the FY 2020/21 emergency budget, except for vacancy savings targets proposed in most funds.

### General Fund

The pre-pandemic proposed budget included a deficit of approximately \$11.5 million, largely attributable to rising personnel and retirement costs; \$1.4 million in one-time projected election costs; discontinuing budget balancing on unreliable one-time revenues such as sales of City property; and a 36% reduction of Measure Z support based on a 2017 five-year General Fund plan that projected strong revenue growth and significant one-time revenues. Public engagement and meetings with the Budget Engagement Commission and City Council would have resulted in specific direction as to how to close the budget gap, but these discussions did not occur due to the pandemic and stay-at-home order. As a result, staff recommended closing the initial budget gap with vacancy savings targets and the gap caused by the 10% contingency revenue reduction with other balancing measures. The City Council subsequently approved the following balancing measures in the General Fund budget:

- **Vacancy Savings Targets:** The General Fund has a total of 1,476.65 full-time equivalent (FTE) positions. A vacancy snapshot taken of the City's human resources system on March 13, 2020 showed 139.50 vacant positions across all General Fund departments. The budgeted value of these positions was quantified, and a vacancy savings target of approximately \$15.7 million was incorporated into the adopted budget as a balancing measure.
- **Pension Obligation Bond (POB) Issuance:** On June 11, 2020, the City completed a highly successful POB sale which results in a savings of at least \$7 million to the General Fund in FY 2020/21; this expenditure reduction has been included in the adopted budget as a savings target.
- **Maintain Measure Z FY 2019/20 Support Level:** Preserves the Measure Z contribution to the General Fund at the same level as FY 2019/20 (\$18.3 million) to help offset \$6.5

million of the deficit resulting from the COVID-19 revenue reduction.

- **Allocate Unspent Measure Z Contingency (2019-2021):** A total of \$6 million was programmed in the 2018-2023 Measure Z spending plan's Spending Contingency line item over three years from FY 2018/19 through FY 2020/21. The amount has not been expended and will be used to help offset General Fund revenue reductions resulting from COVID-19.
- **Section 115 Trust:** In 2019, the City Council approved the establishment of a Section 115 Pension Trust for the long-term management of pension costs. Approximately \$6.2 million of the \$9.4 million current value is budgeted as an interfund transfer to be allocated to the City's required CalPERS UAL payment in FY 2020/21.

### FY 2020/21 Budget Adjustments

During the months since budget adoption, staff has identified the need for several budget adjustments:

1. **Multiple Funds - Pension Obligation Bond (POB) Issuance:** On June 11, 2020, the City completed a highly successful POB sale which resulted in FY 2020/21 savings of \$11.1 million citywide and \$7.2 million savings to the General Fund. Required budget adjustments in relation to the sale include establishing the budget for the FY 2020/21 POB principal and interest payments totaling \$17.8 million and reducing and reallocating the budgeted UAL payment from \$46.1 million to \$17.1 million as a result of the paydown of the UAL.
2. **General Fund - Charter Amendments:** The adopted FY 2020/21 budget included an estimated expenditure of \$1.4 million for election and Charter amendment costs. On July 21, 2020, the City Council directed the City Clerk to place four measures on the November 3, 2020 ballot. The new estimate for fiscal year election costs is \$520,000 resulting in projected General Fund savings of \$880,000.
3. **General Fund - Festival of Lights:** On August 4, 2020, the City Council approved a modified Festival of Lights event for the current year, resulting in a reduction in General Fund revenues of \$364,160 and expenditure savings of \$517,500 to the General Fund. The net impact of the action is General Fund savings of \$153,340.
4. **General Fund - Cost Allocation Plan:** A budget error was identified wherein the allocation of internal service costs to be coded to Non-Departmental City Hall Occupancy was incorrectly coded to the Community & Economic Development Department Property Services. The correction is contained within the General Fund and has a net zero impact to the budget.
5. **Central Stores Fund:** Consistent with best practices, oversight of the Central Stores Fund is recommended to be returned to the Purchasing Division of the Finance Department. City Council approval of the interdepartmental transfer of personnel and budget from Riverside Public Utilities to the Finance Department is required, although the personnel and adopted budget will remain within the internal service fund with no General Fund impact. This adjustment is strictly an interdepartmental transfer with no net effect to the budget.

### FY 2020/21 Supplemental Appropriations

1. **Storm Drain Fund:** An amount of \$50,000 is requested for storm drain studies to maintain the City's drainage systems in order to facilitate a clean and healthy environment and to assist in

the prevention of flooding conditions. Funding for the studies comes from Development Impact Fees. There are sufficient Storm Drain fund reserves available for this supplemental request, with no impact to the General Fund.

2. **Measure A Fund:** Measure A funds come from a County of Riverside half-cent sales tax passed in 1988. The funds passed through to the City are required to be spent on local streets and roads. A supplemental appropriation of \$475,000 is requested for transportation planning (\$50,000), planning/investigations (\$300,000), and payment management systems (\$125,000), each of which were inadvertently excluded from the emergency budget. These are standard annual budget items that were overlooked in the development of the FY 2020/21 emergency budget. There are sufficient Measure A funds available for this supplemental request, with no impact to the General Fund.
3. **Electric Fund:** On June 16, 2020, the City Council received a report on the outcome of negotiations for the City's various insurance policies; however, the City's insurance brokers continued to negotiate with various insurance carriers and did not receive the final premium amounts until July 1, 2020. Increases in insurance policies paid by the City's self-insurance funds are allocated to City funds through the budget process and will be incorporated into the rates computed for the upcoming FY 2021/22 budget. However, direct insurance costs such as property insurance are paid directly by the applicable funds and departments. The FY 2020/21 cost of insurance to Riverside Public Utilities is \$606,600 higher than budgeted; therefore, staff recommends a supplemental appropriation from Electric reserves for this amount. There are sufficient Electric fund reserves available for this supplemental request.
4. **Special Districts Fund:** An annual contribution of \$30,000 is set aside in the Riverwalk Landscape Maintenance District (LMD) to accumulate funds for capital needs. A supplemental appropriation in the amount of \$175,262 was requested to replace fencing, gazebos, and play equipment within the Riverwalk LMD. Sufficient funds are available in the Riverwalk Landscape Maintenance District reserves, with no impact to the General Fund.

As we progress through the fiscal year, we expect continued financial impact of COVID-19 in certain areas, although we are unable to accurately project the potential impact at this time. Budget adjustments in these areas may be recommended in future reports to the City Council as the impact of the pandemic becomes clear. Additionally, FY 2019/20 fiscal year-end results may produce savings that can be carried over to FY 2020/21 to cover potential COVID-19 impacts.

### On the Horizon

The City, like a lot of government agencies, will continue to face mounting pressures due to the lasting impacts of COVID-19 on businesses and the psyche of people. The second quarter of the fiscal year is a critical time period for the City as the holiday season is when most local governments see the largest spike in yearly sales tax revenue. The challenges of COVID-19 are likely to be exacerbated by the lack of a continued federal stimulus which helped bolster FY 2019/20 spending.

The upcoming Presidential election in November and the uncertainty and timing of the election results are likely to stoke continued social unrest nationally and regionally the impact of which is unknown. Locally, the City continually faces ongoing threats to the General Fund Transfer. Any unsuccessful defense of these threats could have a significant impact on General Fund services. The City continues to be proactive in its approach to managing these issues; however, the significance and financial impact of current and potential future events cannot be understated.

**FISCAL IMPACT:**

The FY 2020/21 budgetary impact to City funds is a citywide increase in Revenue and Transfers-In of approximately \$12.8 million and increase in Expenditures and Transfers-Out of \$8.9 million (due largely to the increase of \$13.1 million in both Operating Transfers-In and Operating Transfers-Out related to the POB). The citywide adjusted FY 2020/21 Emergency Budget for all funds, inclusive of budget adjustments and supplemental appropriations, can be viewed in Attachment 1.

General Fund budget adjustments present a net savings of approximately \$1.3 million. On October 27, 2020, staff recommended to Council that these savings be used to reduce the budgeted \$6.2 million withdrawal of Section 115 Pension Trust funds to \$4.9 million, leaving a greater amount of the Trust's principal intact to fund future retirement costs as needed.

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availability of funds: Edward Enriquez, Chief Financial Officer/City Treasurer  
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Attachments:

1. Budget Adjustments
2. Presentation