



*City of Arts & Innovation*

# City Council Memorandum

**TO: HONORABLE MAYOR AND CITY COUNCIL** **DATE: MAY 24, 2016**

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

**SUBJECT: FISCAL YEAR 2015-16 THIRD QUARTER GENERAL FUND FINANCIAL UPDATE, INVESTMENT, AND DEBT REPORTS AND DELEGATION OF INVESTMENT RESPONSIBILITY – AS OF MARCH 2016 (THIRD QUARTER)**

## **ISSUES:**

The issue for City Council consideration is receipt of and input on the quarterly General Fund financial update, investment, and debt reports as of March 2016.

## **RECOMMENDATIONS:**

That the City Council:

1. Receive and provide input on the attached fiscal year (FY) 2015/16 quarterly General Fund financial, investment, and debt reports as of March 2016; and
2. Delegate investment responsibility to the City's Interim Chief Financial Officer/Treasurer for a period of up to one year.

## **BACKGROUND:**

On a quarterly basis, the Finance Department undertakes a comprehensive analysis of revenues and expenditures of the City's various funds, prepares year-end projections based on actuals to date, and as necessary, recommends adjustments to the budget in order to ensure fiscal stability of the City. This ongoing financial monitoring and review is an essential component of the City's strong fiscal management practices.

The attached FY 2015/16 General Fund Third Quarter Financial Report (Attachment A), summarizes the results of that analysis for the period from July 1, 2015 through March 31, 2016.

Also included are the Quarterly Investment Report (Attachment B) and the Quarterly Debt Report (Attachment C), which highlights the City's portfolio of investments and its outstanding debts, respectively. As in prior quarterly reports, financial status on all City funds is provided in Attachment B - a new practice instituted by the new administration.

**DISCUSSION:****Quarterly Financial Report Status – Focus on the General Fund***The Bottom Line*

In the **Mid-Year report** to the City Council (presented on March 8, 2016 and based on December 2015 actuals), staff anticipated an operational General Fund deficit of \$6.8 million, as a result of unrealistically high utility revenues included in the budget and omission of critical and real expenditures related to public safety. The Mid-Year report included balancing measures of nearly \$3.5 million to address a portion of the \$6.8 million deficit, projecting General Fund reserve draws of only \$3.3 million.

The **Third Quarter projection** for the General Fund, as described below, reflects a slightly larger operational deficit of \$7.2 million, up approximately \$430,000 from the Mid-Year projections. Importantly, both the Mid-Year projected deficit of \$6.8 million and the current projected deficit of \$7.2 million already assume that City departments have taken measures to curb spending, totaling approximately \$900,000. No additional measures beyond these already assumed savings are available to balance the shortfall – in other words, \$2.6 million of the \$3.5 million in recommended balancing measures assumed in the Mid-Year report are simply not real.

The process of actively engaging City departments in year-end financial projections is still relatively new to the City, and will require changes to the current culture. As the process unfolded during the preparation of the Mid-Year projections, the lack of communication between the Finance Department and all other City departments essentially led to an erroneous assumption of the majority of the \$3.5 million in savings – which, again, are not real.

The bottom line for the General Fund is that the entire \$7.2 million deficit may need to be balanced by the General Fund reserve. To alleviate the deficit to the extent possible, the City Manager, effective May 13, instituted a freeze on all General Fund hiring and non-essential purchases, to the extent permitted by existing contractual obligations including labor agreements. In addition to the freeze, the Finance Department will implement a FY 2015/16 financial year-end closing process, whereby all encumbered expenditures and requested carryovers are scrutinized and vetted for their applicability to essential City services, existing contractual/legal obligations, and consistency with City Council approved policy initiatives.

It must be noted that the \$7.2 million deficit currently projected for the General Fund reflects both one-time spending and savings measures. Accounting for these one-time items leads to the following calculation of a **Structural General Fund deficit**:

CURRENT:	\$7.2 million FY 15/16 Operational Shortfall
LESS:	\$800,000 in one-time costs related to police MOUs (retroactive FY 14/15 increases)
PLUS:	\$1 million in historical managed savings overages
PLUS:	\$900,000 in one-time savings measures implemented in FY 15/16
<b>EQUALS:</b>	<b>\$8.3 million structural shortfall for FY 15/16.</b>

### A. General Fund Revenues

In the Mid-Year report, revenue was projected to be \$2.25 million below budget. As of the Third Quarter, projected revenues have declined slightly to a total of \$2.5 million below budget as described below. The difference between the adopted budget estimates and third-quarter estimates proposed is approximately 1%.

In the **Taxes** category, total revenue is projected to be slightly below the budgeted target; however, some of the categories making up the total have variances that merit further comment.

- *Property taxes* are projected to exceed projections by approximately \$300,000. The former Redevelopment Agency (now Successor Agency) receipts are expected to be greater than budgeted by \$500,000 and the secured property tax receipts are expected to be \$300,000 greater than budgeted. The increases noted are offset by the Vehicle License Fee Backfill property tax that is now planned to be below budget by \$500,000.
- *Utility users tax (UUT)* revenues are projected to be approximately \$900,000 lower than anticipated, mainly because of higher than previously estimated electric and water conservation measures by City customers. Specifically, Water and Electric UUT revenue is projected to be under budget by \$500,000 and \$400,000, respectively.
- A positive variance exists in the *transient occupancy tax (TOT)*, which continues to show impressive growth due to the expanding demand for hotel room nights in the City. This is principally the result of the renovation and expansion of the Riverside Convention Center. TOT revenues are currently projected to be approximately \$575,000 above the original budget estimate.
- *Other miscellaneous tax revenue items* collectively reflect a minor negative variance of less than \$100,000 from the budget.

**Interfund Transfers** are projected to be approximately \$1.3 million below budget due to the lower than anticipated General Fund Transfer (GFT). The GFT is based on the final, audited prior year gross operating revenues of Riverside Public Utilities. A decline in Water Fund-related GFT was already anticipated in the budget, while further decline in Electric Fund revenues was not. The FY 2014-15 declining electric revenue amounts primarily account for the \$1.3 million GFT variance.

The **Charges, Licenses and Permits** category of revenues was projected to be \$1.15 million below the adopted budget estimate in the Mid-Year report. As of the third quarter, the projected amount is \$300,000 below the estimated budget. The change in projected revenue is primarily due to an increase in activity and estimated revenue associated with Live Nation and the Convention Center operations, which collectively account for a \$1.2 million increase. The revenue associated with fees and charges for services is projected to be \$1.5 million below budget due to the delay in approval of the City's user fee study and the subsequent stay of several key fee increases as they are being re-examined for process efficiencies.

**Other Revenues** were projected to be \$225,000 above budgeted revenues as of the Mid-Year report. As of the third quarter, however, there is a projected shortfall of approximately \$270,000. Other Revenues are largely made up of several items, including interest revenue, rentals leases, rebates/refunds, miscellaneous receipts, etc. One particular line item in the adopted FY 2015-16 Budget, miscellaneous receipts/one-time revenue, was budgeted for \$2.5 million. To date,

this account has not performed as planned causing the decrease from Mid-Year projections.

Finally, previously projected revenue for the **Fines and Forfeits** category has continued to decline. At Mid-Year, the shortfall was expected to be approximately \$375,000. As of third quarter, the shortfall amount has increased to approximately \$690,000. This decline is primarily due to a reduction in Code Enforcement revenue that is a result of an improving economy and the end of the foreclosure crisis. Also, the continued State drought legislation as well as City adopted conservation ordinance has prevented the City from assessing any fines related to brown/dry landscape. This was previously one of the primary case types and revenue generating violations for Code Enforcement.

### *B. General Fund Expenditures*

General Fund expenditures are currently projected to exceed the General Fund budget by \$5.7 million, which is approximately 2.2% of the Adopted Budget amount of \$256.6 million. The increase relates to two categories of additional expenditures:

1. Previously approved by the City Council supplemental appropriations from the General Fund reserve are approximately \$5.1 million. These appropriations include, but are not limited to \$3.9 million for known, but unbudgeted Police Department union contracts, approximately \$575,000 in Fire Department mutual aid reimbursable expenses, \$281,000 for the relocation of the City Attorney's Office, \$360,000 for emergency repairs and improvements to the Museum's storage facility, and \$109,120 associated with the audits of the Finance and Human Resources Departments.
2. For FY 2015/16, the adopted budget includes a Managed Savings target of \$6.1 million, which is budgeted at the fund level and tracked through departmental budget to actual analysis. Departmental expenditure projections currently indicate that they will collectively be short of the managed savings target in the adopted budget by approximately \$650,000. Within the overall departmental managed savings analysis, the Fire Department (\$575,000), Finance (\$161,000) and City Manager's Office (\$120,000) have the only projected over budget position.

The Finance Department and City Manager's Office are over budget due to the contractually obligated severance pay for the departed senior-level managers (Assistant City Manager, Finance Director/Treasurer, and Fiscal Resources Manager), related severance pay, and the need to fill those positions immediately.

In previous years, the Fire Department has been under budgeted/funded by upwards of \$1 million with respect to overtime; the current projected deficit of \$575,000 is a laudable improvement from previous years. Specifically, the deficit is related to a Memorandum of Understanding (MOU) provision that requires a staffing backfill for the majority of employees when they are not at work (vacation, sick, etc.), which causes the department to incur overtime costs; the Fire Department's discretionary overtime is actually relatively low. City Management will ensure the Fire Departments FY 2016-2018 Two-Year Budget is funded appropriately to avoid the structure overtime issues related to the need to backfill staff.

### *C. General Fund Reserves*

The impact of the variances in General Fund revenues and expenditures amount to a projected draw on the General Fund reserve of approximately \$7.2 million. **This effectively decreases**

**the projected reserve balance to \$32.9 million, representing only 12.8% and, therefore, falling below the City's 15% recommended reserve level.** As previously indicated, to alleviate the deficit to the extent possible, the City Manager, effective May 13, instituted a freeze on all General Fund hiring and non-essential purchases, to the extent permitted by existing agreements. In the FY 2016-2018 Two-Year Budget, the City's management team will recommend further actions to maintain the General Fund reserves at 15%.

### **Quarterly Investment Report Status**

Sound investment practices are an essential component of the City's strong fiscal management. The Finance Department is responsible for managing the City's investment portfolio, focusing first on the safety of investments, and then on liquidity and an appropriate rate of return. The investment results and portfolio composition are summarized and reported to the City Council each quarter. As of March 31, 2016, the City's pooled investment portfolio's market value was \$509 million, with the market value of investments held by fiscal agents (bond proceeds and reserve funds primarily) amounting to an additional \$311 million. The weighted average yield of the pooled investment portfolio continues to hold steady at 0.92%. Additionally, this report requests the continued approval of delegated authorization for the Chief Financial Officer/Treasurer to invest/reinvest funds and to sell or exchange purchased securities, consistent with the City's adopted investment policy. This is a requirement of State law.

Beginning with the First Quarter Investment Report, staff began including with the Investment Report a listing of cash balances by fund. This list is included in Attachment B. These cash balances reflect each fund's share of the City's pooled investment portfolio. Also shown are interfund loan receivables, which are treated as available cash due to the Finance Director/Treasurer's authorization to move loan receivables to other funds as needed.

All listed funds have a positive cash balance with the exception of the following funds:

1. The Public Parking Fund has a negative cash balance of approximately \$75,000 which is related to outstanding accounts receivable.
2. The Urban Areas Security Initiative (\$440,000), Housing Opportunities for Persons with Aids (\$390,000), NPDES Storm Drain (\$285,000), Capital Outlay (\$6.1 million), Transportation Projects (\$12,000), and Transportation Uniform Mitigation Fees Funds (\$3.5 million) all have a negative cash balance, which is fully offset by outstanding grant receivables.
3. The Liability Insurance Trust Fund has a negative cash balance of approximately \$4 million, but is consolidated with the positive cash balances of the Workers Compensation Insurance Trust Fund (\$16.8 million) and Unemployment Insurance Trust Fund (\$425,000) for financial reporting purposes. Staff is implementing a strategy to return the Liability Insurance Trust Fund to an improved financial condition (cash and fund balance levels) over the next five years. In the current year, the cash position was budgeted to improve by \$1 million, subject to the year's actual liability claim results.
4. The Central Stores Fund has a negative cash balance of \$350,000, which is fully offset by inventory assets.

## Quarterly Debt Report Status

The Finance Department is also charged with managing the City's debt portfolio, which includes issuing new debt and monitoring opportunities to refinance existing debt as opportunities to reduce interest costs arise. The Quarterly Debt Report (Attachment C) summarizes the composition of the City's debt portfolio, details the revenue sources utilized to pay the debt service associated with each outstanding debt, and provides detailed information regarding the total principal and interest payments due in the current fiscal year by Fund. There are no changes to the Quarterly Debt Report for this quarter.

## **FISCAL IMPACT:**

The Third Quarter Financial Report projects a \$7.2 million operational shortfall in the General Fund for FY 2015/16. To alleviate the deficit to the extent possible, the City Manager, effective May 13, instituted a freeze on all General Fund hiring and non-essential purchases, to the extent permitted by existing agreements. At this time, it will not be feasible to determine the financial impact the freeze will have. In addition to the freeze, the Finance Department will implement a FY 2015/16 financial closing, whereby all encumbered expenditures and requested carryovers are scrutinized and vetted for their applicability to essential City services, existing contractual/legal obligations, and consistency with City Council approved policy initiatives.

Prepared by: Adam Raymond, Assistant Finance Director  
Certified as to  
availability of funds: Scott Miller, Interim Finance Director/Treasurer  
Approved by: Marianna Marysheva-Martinez, Assistant City Manager  
Approved as to form: Gary G. Geuss, City Attorney

### Attachments:

1. Attachment A: Quarterly General Fund Financial Report
2. Attachment B: Quarterly Investment Report
3. Attachment C: Quarterly Debt Report
4. Presentation