



# CITY COUNCIL STAFF REPORT

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**TO:** Honorable Mayor and City Council      **DATE:** November 16, 2020  
**FROM:** Matthew Bronson City Manager  
**PREPARED BY:** Deanne Purcell, Administrative Services Director  
**SUBJECT:** FY 2019-20 Year-End and FY 2020-21 First Quarter Financial Review

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## RECOMMENDATION

Receive information on the FY 2019-20 Year-End and FY 2020-21 First Quarter Financial Review and provide comments to staff

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## BACKGROUND

### **FY 2019-20 Year End Financial Review**

On June 22, 2020, the Council adopted the FY 2020-21 budget which included estimates for the fiscal year ending June 30, 2020. This action followed a presentation provided to the Council on May 4, 2020 with initial projections of COVID-19 impacts to the City's financial outlook. Staff is working with the City's outside auditors to complete the FY 2019-20 annual audit which is anticipated to be completed in November and brought to the Council for approval in January. Following a site visit by the auditors in late October, staff has conducted an initial review of the year-end financial results of FY 2019-20 to provide a summary to the Council prior to the completion of the audit. The following summary represents preliminary information that will be shared in further detail as part of the audit process.

### General Fund

The General Fund is the City's primary fund. General City services including police, fire, and parks and recreation, and general administration are included in this fund. The General Fund is also where property tax, sales tax, and other general revenues are collected. Table 1 below shows the year-end estimates for FY 2019-20 provided to the City Council in June 2020 compared to the FY 2019-20 unaudited actuals:

Table 1

<b>GF Summary</b>	<b>FY 2019-20 Estimated</b>	<b>FY 2019-20 Unaudited Actuals</b>	<b>Difference</b>
Beginning Reserves	\$ 3,647,500	\$ 3,647,500	\$ -
Revenues/Transfers In	12,697,116	13,540,052	842,936
Expenditures/Transfers Out	12,405,846	12,482,739	76,893
<b>Annual Surplus</b>	<b>\$ 291,270</b>	<b>\$ 1,057,313</b>	<b>\$ 766,043</b>
Ending Reserves	\$ 3,938,770	\$ 4,704,813	\$ 766,043
% of Operating Expenditures	33%	39%	6%

FY 2019-20 actual revenues are higher than originally estimated as part of the FY 2020-21 budget process which identified a projected revenue shortfall of \$700,000 due to COVID-19 financial impacts. This information was preliminary after only two months into the pandemic with a strict shelter-at-home order in place along with related business closures. The initial impact of the pandemic on City finances was less than anticipated given early business reopening in May/June coupled with growth in cannabis business activity which led to cannabis tax revenues \$437,000 higher than budgeted and sales tax revenues \$381,000 higher than budgeted. While cannabis tax and sales tax revenues ultimately showed an increase for the year, transient occupancy tax (TOT) revenues declined for the year as projected though at a lower amount of \$140,000 compared with a projected \$200,000 reduction.

In summary, last year’s revenues overall did not show a decline as projected but rather were unexpectedly higher than budgeted by \$842,000 due to the one-time circumstance of early business reopening in late spring and continued growth of cannabis businesses. Expenditures shown in Table 1 are also approximately \$76,000 higher than originally estimated mainly attributed to additional costs for legal review on City projects and issues and higher costs for Public Works staff that are increasingly utilized for work on General Fund services compared with working on services in other funds as in past years. These increases were offset by lower than estimated training and education costs due to lack of travel to attend training and conferences given COVID restrictions.

As shown in Table 1, the FY 2019-20 General Fund estimated unaudited actual surplus is \$1.06 million though approximately \$285,000 of this amount represents carryover funds including \$110,000 in projects not completed by year-end and \$175,000 in remaining SB 1090 Diablo Canyon Settlement Funds for economic development work. Based on the remaining surplus amount of \$721,000, staff intends to carry out the \$500,000 pension cost paydown approved by Council last year that was put on hold given initial uncertainty at the beginning of the pandemic. This paydown will be made to CalPERS by December 31, 2020 and save approximately \$850,000 in lower pension costs over the next 16 years. Staff recommends holding off on additional expenditures at this time given continued uncertainty with public health restrictions given the worsening COVID-19 case numbers and the onset of winter weather conditions which could significantly affect local businesses. Staff will return to the Council with additional information about the City’s financial condition in February 2021 as part of the FY 2020-21 mid-year review and financial forecast that will be described further in this report.

Water Fund

The Water Fund is responsible for the maintenance and operation of City’s water system. This includes water lines, tanks, and wells. The Water Fund ended FY 2019-20 with \$1.7 million more than projected as shown below in Table 2:

Table 2

<b>Water Fund</b>	<b>FY 2019-20 Adopted</b>	<b>FY 2019-20 Unaudited Actuals</b>	<b>Difference</b>
Beginning Reserves	\$ 4,271,128	\$ 4,271,128	\$ -
Revenues/Transfers In	3,878,500	5,231,956	1,353,456
Expenditures/Transfers Out	3,696,586	3,346,323	(350,263)
<b>Annual Surplus</b>	<b>\$ 181,914</b>	<b>\$ 1,885,633</b>	<b>\$ 1,703,719</b>
Ending Reserves	\$ 4,453,042	\$ 6,156,761	\$ 1,703,719

Water revenues are higher than expected by approximately \$1.35 million, which is mainly due to a one-time transfer from the Community Development Block Grant (CDBG) Fund of \$1.15 million for the water main upgrade project that is being funded by CDBG along with higher interest income than budgeted of \$45,000 and higher water service charges of approximately \$130,000 than budgeted. Expenditures are lower than anticipated mainly due to CIP projects not completed by the end of the fiscal year of approximately \$454,000 offset by the cost of issuing debt (water revenue bond) of \$135,000.

Wastewater Fund

The Wastewater Fund is responsible for the City’s maintenance and operation of wastewater lines within the City and bills for and forwards funds collected to the South San Luis Obispo County Sanitation District. The Wastewater Fund is projected to end FY 2019-20 with approximately \$308,000 more than projected as shown in Table 3 below:

Table 3

<b>Wastewater Fund</b>	<b>FY 2019-20 Adopted</b>	<b>FY 2019-20 Unaudited Actuals</b>	<b>Difference</b>
Beginning Reserves	\$ 6,364,523	\$ 6,364,523	\$ -
Revenues/Transfers In	1,392,400	1,308,489	(83,911)
Expenditures/Transfers Out	1,801,584	1,409,354	(392,230)
<b>Annual Surplus</b>	<b>\$ (409,184)</b>	<b>\$ (100,865)</b>	<b>308,319</b>
Ending Reserves	\$ 5,955,339	\$ 6,263,658	\$ 308,319

Wastewater revenues are lower than expected due to the deferral of the broadband fiber loan repayment of \$143,000 from the General Fund. This was budgeted for FY 2019-20 as the first repayment of five payments but deferred due to COVID-19 pandemic and the need to preserve reserves in anticipation of a large revenue shortfall. Staff will incorporate this expenditure back to the Council as part of the upcoming FY 2020-21 mid-year review. This revenue deferral was offset by higher interest income of \$20,000 and higher wastewater fees of \$40,000. Expenditures are lower than anticipated mainly due to CIP projects that were not completed by the end of the fiscal year of approximately \$413,000.

**FY 2020-21 First Quarter Financial Review**

General Fund

The City Council adopted a FY 2020-21 General Fund budget of \$12,963,389 including \$12,396,131 in operating expenditures, \$166,258 in capital expenditures and debt service and transfers out of \$401,000. The General Fund budget assumed revenues and transfers in of \$12,999,906 which leads to an estimated surplus of \$36,517 producing reserves equivalent to 32% of operating expenditures.

Overall, revenues are performing as expected in the first quarter of FY 2020-21 from July through September using historical trends and the timing of when revenues are received. The FY 2020-21 budget took into account the projected impact of the pandemic on revenues, estimating a revenue shortfall for sales tax (\$300,000), cannabis tax (\$300,000) and TOT (\$200,000). These revenues are being monitored closely given the continued uncertainty and volatility of the

economic environment with COVID-19 restrictions. Overall, General Fund revenues are being received as anticipated for the first quarter of the year though there are some initial signs that the sales tax and cannabis tax impacts may be less significant than projected similar to the results of last fiscal year. However, it is still early in this fiscal year and economic conditions could worsen considerably as noted earlier. A more definitive estimate of revenues will be presented with the mid-year budget review and included in the updated financial forecast presented in 2021.

City staff has worked to keep expenditures on track as budgeted with first quarter expenditures listed below in Table 4:

Table 4

GF Department	Adopted	Q1 Actual	% of Budget
Administrative Services	\$ 485,411	\$ 117,305	24.17%
City Management	1,169,103	187,218	16.01%
Community Development	1,151,546	182,461	15.84%
Parks and Recreation	409,792	68,905	16.81%
Police	4,575,515	1,151,157	25.16%
Public Works	1,168,749	281,817	24.11%
Non-Departmental	3,902,583	1,534,305	39.32%
<b>Total GF Expenditures</b>	<b>\$ 12,862,699</b>	<b>\$ 3,523,168</b>	<b>27.39%</b>

Overall, expenditures should generally be approximately 25% of the budget at the end of the first quarter. The Administrative Services, City Management, Community Development, Parks and Recreation and Public Works departments are below 25% of budget for the first quarter. Actual expense for Police is reporting slightly higher than 25% for the first quarter mainly due to annual capital lease payments and annual maintenance agreements that were made at the beginning of the year. Non-Departmental is reporting 39% of its budget expended through the first quarter mainly due to annual payments made at the beginning of the fiscal year including insurance liability payments and the CalPERS unfunded liability payment. Two of the four payments have been made for the Five Cities Fire Authority contract as these are due at the beginning of each quarter. In addition, salaries of approximately \$25,000 are being tracked in Non-Departmental for COVID-19 reimbursement from FEMA.

Water Fund

Water Fund revenues are higher from this time in FY 2019-20 which is mainly due to the 6% rate increase enacted with the FY 2020-21 adopted budget. The City is on track to meet the revenue amounts in the adopted budget for this year. Operating expenditures for the Water Fund in the first quarter are tracking with expectations which includes an annual payment for insurance, a semi-annual payment made to the County for the Lopez Water contract, and debt service payment of the new water revenue bonds that will be used to fund water projects that total over \$3 million for the fiscal year. The Water Fund is more financially stable than in previous years and the Council will further discuss the future financial viability of the Fund with regards to system needs and long-term projects such as Central Coast Blue in early 2021.

Wastewater Fund

Wastewater Fund revenues appear to be on track with the adopted budget though expenditures are below budget for the first quarter with only 14% expended to date. The main reason is due to

capital projects that have not yet started and transfers-out that are reconciled and accounted for annually as a year-end adjustment. The Council's consideration of award of construction contract for the Highland Sewer project on the November 16<sup>th</sup> agenda is an example of these capital projects to improve the City's wastewater capacity. Similar to the Water Fund, the Wastewater Fund is in a relatively stable position and the Council will further discuss the future financial viability of the Fund with regards to system needs and long-term projects such as upgrading sewer capacity in early 2021.

### **Upcoming Budget Process**

Lastly, staff wished to update the Council on the upcoming budget development process planned for this fiscal year. Staff is intending to implement a new approach in developing a two-year operating budget for the next two fiscal years FY 2021-22 and FY 2022-23. This approach has been discussed with the Council in previous years and staff plans to move forward with the implementation in this upcoming budget development process. A two-year budget is common among cities including both neighboring Arroyo Grande and Pismo Beach and allows for improved planning and budgeting to meet future needs. This process also tracks with the Council's two-year goal-setting process which will commence in early 2021.

Similar to last year, staff is planning to update the City's long-range financial forecast internally versus contracting with an outside consultant to reduce costs and use staff capability in this work. This forecast will continue to be beneficial in identifying and refining key revenue and expenditure trends over the next several years including Measure F-20 revenues pending certification of election results. Staff is planning to present the mid-year budget review and updated long-term financial forecast to the Council in February 2021 as a starting point in the upcoming budget development process before the Council will hold a subsequent workshop to develop its list of 2021-23 Council Goals. This goal-setting process will involve community engagement to receive public input in this process. The mid-year review will also be an opportunity for staff to identify potential uses of one-time funding this fiscal year for the Council's consideration.

### **FISCAL IMPACT**

There is no fiscal impact from receiving this report.

### **ALTERNATIVES**

The Council has the following alternatives to consider:

1. Receive information on the FY 2019-20 Year-End and FY 2020-21 First Quarter Financial Review and provide comments to staff; or
2. Provide alternative direction to staff

### **PUBLIC NOTIFICATION**

The agenda was posted in accordance with the Brown Act.