FISCAL YEAR 2013-14 FOURTH QUARTER BUDGET STATUS UPDATE AND YEAR END PROJECTION

RECOMMENDATION

It is recommended that the City Council accept by motion this fourth quarter status report for Fiscal Year 2013-14 and adopt by resolution amendments to the Fiscal Year 2013-14 Annual Budget for the General Fund, Entertainment Venues, Neighborhood Stabilization Program 3 (NSP3), Low and Moderate Income Housing Fund, and Workers’ Compensation Internal Service Fund.

Summary

Staff has conducted an analysis of the fourth quarter financial activity and results for the Fiscal Year (FY) 2013-14, and developed year end projections (unaudited) for FY 2013-14. The year end projections for the fiscal year has prompted proposed budget amendments as described below. As reflected in Attachment A, the General Fund ending available balance is projected to be $16.4 million more than the $9.751 million fund balance projected in the Long Range Financial Plan (LRFP). The available fund balance is the result of budgeted reductions of $23.8 million to creditors, positive revenue results, and one-time savings from vacancies primarily in public safety departments and other operations. The increase of $16.4 million in the ending General Fund balance will be transferred to the Bankruptcy Fund in accordance with budget resolution 2014-06-24-1601, section 9.

In addition to the evaluation of the General Fund budget, an analysis has been conducted of other significant City operations to determine variances from budget or potential impacts to General Fund. The evaluations identified variances between budget and actual financial activity. Budget amendments are recommended to address current operational conditions for the General Fund, Entertainment Venues, Neighborhood Stabilization Program 3 (NSP3), Low and Moderate Income Housing Fund, and the Workers Compensation Internal Service Fund.

DISCUSSION

Background

Since 2008, the City Council has substantially reduced programs, staffing, services and employee compensation by enacting more than $90 million in ongoing General Fund budget cuts. Despite all the prior year reductions, the City was facing an additional deficit of $26 million going into FY 2012-13 that could only be addressed under protection of chapter 9 and adoption of a pendency plan budget. The City’s General Fund budget for FY 2013-14 was also balanced under continuing chapter 9 protection by making an additional $23.8 million in reductions to creditors and retirees under the pendency plan budget. This budget continued the General Fund Pendency Plan under chapter 9 protection of the federal bankruptcy code and reflected the expenditure priorities pending
confirmation of a plan of adjustment to exit bankruptcy.

The budgeted General Fund beginning available balance for FY 2013-14 was projected to be $0, with the entire available balance from FY 2012-13 transferred to the Bankruptcy Fund to pay associated costs for legal, project management and settlement expenses. Subsequently, Council action on February 25, 2014, retained $3.1 million in the FY 2012-13 General Fund Ending Available Fund Balance, reflecting a one-time settlement payment of County Property Tax Administration Fees and allocated this amount to start rebuilding General Fund reserves. In addition, the FY 2013-14 General Fund Beginning Available Fund Balance included prior year encumbrances of $1.6 million making the total $4.7 million. Encumbrances are purchase orders and contractual commitments approved by the City Manager and City Council.

Also on February 25, 2014, Council approved an amendment to the FY 2013-14 Annual Budget to increase revenues for Measure A by $6.8 million along with corresponding expenditures of $1.1 million for the first phase implementation of the Marshall Plan and related support. Council also accepted a first quarter FY 2013-14 budget status report and further amended the budgeted revenue by $987,000 to reflect an increased property tax estimate. These actions increased the FY 2013-14 General Fund Ending Available Fund Balance to a projected $9.8 million. Consistent with the LRFP, it is anticipated that these funds will be used to help rebuild the General Fund reserves to an acceptable level as recommended by Government Finance Officers Association (GFOA) which is 16.67% of annual City expenditures, to end the bankruptcy, and to restore City service including the funding of one-time mission critical needs.

On October 21, 2014 City Council accepted a budget status report on the General Fund results for the Second and Third Quarters with a year end projection based on nine months of activity. This status report identified a likely year end positive fund balance of $14.7 million more than the $9.751 million fund balance projected in the LRFP.

Present Situation

General Fund

As shown in Attachments A and B, staff has completed its review of General Fund expenditure and revenue results for the final quarter of FY 2013-14. Certain budget amendments are recommended as a result of these reviews as discussed below.

An examination of revenue recorded through June 2014 indicates that General Fund revenues are slightly above the amended budget (approximately $3.6 million or 2.2%). About half of this variance is the result of higher than budgeted revenues in Property Tax and Code Enforcement proceeds. The remaining variance is the offsetting results of over and under collections across the remaining accounts in the General Fund. These variances are explained in more detail in the next section of this report.

General Fund expenditures through the final quarter of the year continue to run below budgeted levels with total annual savings of approximately $12.8 million (7.9%) projected. A total of $1,964,200 of these savings represents unspent Contingency Reserve. By far the largest portion of the savings ($5.8 million) is the result of vacant positions throughout the City, primarily in the Police and Fire departments, but also in the City Attorney, Administrative Services, and Human Resources.
departments. The unusually high level of vacancy savings continues to be the result of the stress placed on the organization by the continued budget reductions, salary and benefit reductions and the long bankruptcy process. Recruiting and retaining staff under these uncertain conditions has proven to be a very challenging task. Recognizing the high levels of vacancies through the end of FY 2013-14, the FY 2014-15 Adopted Budget addressed this by increasing estimated vacancy savings. Despite prior projections, the one-time vacancy savings accumulated through the end of the year, resulted in higher than budgeted vacancy projection for FY 2013-14. Additional savings are also expected in labor relations and legal services ($2.7 million), reflecting lower costs in those areas due to the slower than anticipated progress of labor negotiations prior to the close of FY 2013-14.

Savings achieved in the last two years have increased the General Fund ending available balance, which currently provides one time funding primarily for the bankruptcy process including legal and related costs. Other uses of General Fund ending available fund balance that will be considered going forward are establishing reserves consistent with LRFP, mission critical spending, addressing deficits in other funds (i.e. Internal Service Funds), and resolving areas of service insolvency. These savings are not anticipated to be ongoing once staffing levels are achieved. As the organization emerges from bankruptcy and begins utilizing the additional Measure A sales tax to hire additional officers, improve safety and other City services, the employee recruiting and retention environment should improve significantly. The City’s LRFP assumes that transition.

Revenue

Based on current information, it is expected that General Fund revenues will end the year at $171.2 million ending the year at slightly more than ($3.6 million) the current budgeted revenue of $167.6 million. This includes one quarter of Measure A sales tax revenues ($6.6 million) as shown in Attachment B. Year end revenue projections are approximately $1.2 million greater than the third quarter projection presented to Council on October 21, 2014. A discussion of the variances by revenue category within the General Fund follows.

Property Tax revenues continue to recover in FY 2013-14 exceeding the amended budget by $1.1 million (2.4%) due to a one time recovery and supplemental taxes. In February, the City received $401,000 from the County for settlement of unpaid interest on the refund of one-time prior year settlement of Property Tax Administration Fees (PTAF). Last fiscal year, the City received $3.1
million in PTAF refunds for fiscal years 2006-07 through 2011-12 (those funds have been placed in reserve in the Ending Fund Balance). The amount received in FY 2013-14 is the final payment of a prior year settlement with San Joaquin County for these refunds. Going forward the Property Tax Administration fees have been budgeted at the newly calculated lower fee rate.

As noted in the First Quarter Fiscal Review, property values in the City of Stockton experienced a net taxable value increase of 2.8% over the prior year due to recovering residential property values. The FY 2013-14 General Fund Budget was amended by Council action as part of the First quarter Review, raising the Property Tax estimate by $987,000. Consistent with the amount reported in the Third Quarter report, property tax revenues are projected to exceed the amended budget by approximately $708,000 primarily due to receipt of supplemental taxes attributable to property sold after the FY 2013-14 tax roll values were determined.

Sales Tax revenues are expected to end the year $200,000 or 0.4% above the amended budget. Total sales tax revenues of $47.2 million include $6.6 million collected between April and June for the new Measure A transaction and use tax. Transaction and use tax revenues were 3% less than budget due to lower used auto sales, bulk fuel sales and business to business sales. In February 2014, the revenue budget was increased by $6.8 million reflecting one quarter of Measure A revenues.

Utility Users Taxes (UUT) revenues improved in the fourth quarter of FY 2013-14 exceeding third quarter projections by $370,000 primarily due to seasonal increases in electricity usage. This revenue category is projected to end the year 0.6% above budget by approximately $180,000. This reflects variances within the individual UUT tax categories. Water ($146,000), Electric and Gas ($529,000), and Cable UUT receipts ($151,000) are all running slightly ahead of the budgeted estimates. These overages, however, are expected to be more than offset by a projected shortfall in the Telecommunications UUT category ($647,000). This shortfall reflects the negative impact on City revenues stemming from the continued rapid changes in telephone and data delivery methods. Revenue collections from the Telecommunication UUT have fallen three years in a row. The telecommunication tax will continue to be monitored as the environment of telecommunication delivery methods evolves, further shrinking this revenue stream.

Franchise Tax proceeds are projected to exceed the budgeted level by $310,000 (2.7%) primarily due to an increase in waste hauler revenues. With a 2.2% increase over the prior year, residential collections are growing at a rate slightly greater than the 1.59% CIP rate adjustment that went into effect June 1, 2013. As the economy continues to improve, consumer spending and related waste will also increase.

Business License revenues in FY 2013-14 are projected to be $9.4 million, an increase of 2.2% compared to FY 2012-13. The adopted budget assumed no growth in this area but business activity exceeded expectations. Business License Tax proceeds are projected to end the year above the budgeted amount by approximately $380,000. With a focus on Economic Development, and an improving business climate in Stockton there was an increase in gross receipts from reported businesses by $1.2 billion as compared to the prior year. In addition, the internal and external business license audits should continue to drive these results in the future.

The Program Revenues category contains a collection of accounts which are related to recovering the costs of City programs. On an overall basis, this category is projected to end the year well above budget ($1.5 million). It is however the result of a number of offsetting over and under collections.
The largest projected overage in this category is for Code Enforcement revenues and cost recovery. Staff is currently projecting Code Enforcement revenues will exceed the budgeted amount by approximately $770,000. Self-certification fee revenues for the rental inspection program represent the largest increase within Code Enforcement. This revenue varies from year to year depending on the quadrant of the City inspected and Code Enforcement staffing. This is consistent with Council’s approval for additional code enforcement officers in FY 2012-13 that were anticipated to increase collections. During this fiscal year, the number of rental units has increased beyond what was anticipated in the current year budget. Several years ago the County discontinued reimbursing the City for accumulated code enforcement related liens on properties under what was called the “Teeter Plan”. Now reimbursements represent payments for liens actually received. The primary driver for the improved performance is due to an increase in the number of home sales and value of properties sold in the local area. As an individual property is sold, the associated liens are paid off which provides the code enforcement revenue and cost recovery to the City. This is now occurring at a higher rate than anticipated at the time the budget was established.

Other Program Revenues listed in Attachment B that are expected to exceed budget in this category are:

- Revenues from Other Agencies ($294,000), which reflects unanticipated prior year State and Federal Fire support reimbursements, higher State POST program reimbursements, and higher than anticipated RDA pass-through revenue.
- The adopted budget and LRFP also did not anticipate the sale of fixed assets identified during the bankruptcy process to sell until FY 2014-15 but some sales were complete in FY 2013-14 generating an additional $200,000 for the General Fund.

These favorable results are partially offset by:

- A shortfall in the Fire Contracts line item, representing a true-up of prior year fire district charges.
- Higher than expected fines and forfeiture payments brought on by increased collection activities in the final quarter of the year resulted in revenue receipts of $130,000 more than the $1.3 million budget.
- In addition, a change in the recording of accounts receivable not previously projected added $678,000 primarily due to parking citation revenue recognition to the Fines and Forfeitures category, bringing the total to just over $2.1 million. Based on past collection experience, the City also reduced the receivable by an allowance for uncollectible accounts of $723,000 reflected in the Misc. Other Revenues category. The net budget variance of Fines and Forfeitures ($810,000) offset by the allowance for uncollectible accounts ($723,000) within Misc. Other Revenues is insignificant.

Expenditures

The General Fund continued to experience savings in the fourth quarter of FY 2013-14 increasing the $12.2 million savings projected in the third quarter report to $12.8 million as presented in Attachment A. The majority of the General Fund expenditures are in support of the five departments in the Programs category which are anticipated to run a total of $5.7 million below budget. The bulk of those savings are in the Police and Fire Department, as mentioned above, where efforts to fill
positions were virtually offset by continuing departures of existing staff. As was reported in the quarterly status reports, significant amounts of one-time salary savings accumulated through the end of the year as a result of vacancies experienced. This reflects the difficulty the City is having filling positions and retaining personnel.

As of June 30, 2014, the Police Department still had 18 sworn vacancies and the Fire Department had 13 sworn vacancies. On February 24, 2014 the City Council appropriated just over $1 million for expenditures related to Measure A revenues that are included in the approved budget of $162.5 million. The Measure A transaction and use tax was not effective until April 1st, therefore the appropriation of expenditures occurred in the final quarter of the fiscal year which included the approval of the new positions. Due to the length of time to recruit Police Officers to these new positions, the majority of the $1 million in appropriations is expected to remain unspent at year end. Although Police and Fire Department personnel are being hired, it is expected that the overall filled positions at year end will remain approximately the same as third quarter.

As a result, the current General Fund year end projection will provide savings of approximately $12.8 million or 7.9% of the budgeted expenditures. Projections show that of this total, $1,964,000 will be the result of unspent Contingency Reserve funds and $2.7 million will be unspent labor and litigation funds.

The Peacekeepers Program is anticipated to exceed its budget by $24,000. The Peacekeeper program is funded with competitive grants as well as a General Fund allocation. Due to economic conditions, the grant funding of the program has decreased significantly in recent years. A budget amendment to cover the shortfall for this program is proposed from the unspent available Grant Match budget in the attached resolution.

In the Program Support for Other Funds category, the analysis indicates that most programs are on track to stay within the FY 2013-14 budgeted subsidy levels from the General Fund with three exceptions as follows:

- The amount budgeted to subsidize the RDA Successor Agency was $750,000. It appears that the required subsidy will be close to $450,000; less than budget by approximately $300,000. This savings is anticipated from lower than budgeted outside legal costs related to properties, litigation and agency administration.
- The amount budgeted annually for Grant Match funding ($400,000) is not being utilized as anticipated. This is a result of less grants being implemented that require matching funds. Year end savings are anticipated to be approximately $336,000 in this category. The proposed budget amendment for Peacekeepers will utilize $24,000 of these savings.
- The Entertainment Venues Fund is expected to need a higher subsidy than budgeted by approximately $267,000 (see Attachment C). An analysis of the performance of the four venues included in this fund (Arena, Bob Hope Theater, the Ballpark and Oak Park) indicates that the shortfall is primarily the result of lower than anticipated revenue at the Arena. The Bob Hope Theater was nearly self-supporting, whereas the Ball Park and Oak Park experienced losses though these losses were under the City’s expectations and budget. The review of the Entertainment Venue Fund revenue and expenditure projections from SMG indicates that the General Fund subsidy of $2.65 million will not be insufficient to cover operating shortages by year end. An additional $267,000 subsidy will be needed. There are
sufficient savings in Other Administration/Non-Departmental budget for this subsidy. The Arena attendance was down across the board for shows and for the hockey team. The number of events held at the Arena was actually only 3 less than last year, but attendance in total was down for all tickets by 33,000 and paid tickets were down 72,000 from the prior year. This economic condition has resulted in reductions in all categories of revenues, including concessions and merchandise. Due to this situation, the Arena Operator cut expenses including laying-off some staff and not filling a number of vacant positions. Even after these reduction efforts, the operator was unable to make up for the loss of revenue. The original budget for Arena revenues included an assumption that an improving economy would stabilize ticket sales. Entertainment Venues budget for FY 2014-15 has been evaluated and the General Fund support has been increased to take into account a slower recovery than anticipated in event sales.

All of the departments and categories in the Administration Program section are projected to end the year at or below budget. The largest amounts of savings are occurring in the City Attorney’s Office, Administrative Services and Human Resources Departments, Tax Collection and Election Expense and in Other Administration category and are described as follows.

- Similar to last year, the City Attorney’s Office is experiencing significant salary savings due to several vacancies which occurred early last fiscal year and were not filled due to workload uncertainties and due to the City’s bankruptcy filing. One of these vacancies was filled in November 2013 and another was filled in November of this year however an additional vacancy is expected to remain until the City exits bankruptcy. Litigation cases have declined during the City’s bankruptcy process but are expected to return to pre-bankruptcy levels sometime during FY 2014-15, at which time, the vacant Deputy City Attorney position will need to be filled. The overall expected savings in the City Attorney’s Office is $288,000 for FY 2013 -14.

- Administrative Services Department is projected to end the fiscal year with $563,000 in savings due to vacancies that remain unfilled. Although some positions were filled toward the end of the fiscal year, such as the Program Manager to the Chief Financial Officer, other positions remain vacant. Recruitment efforts are underway in various divisions within the department.

- The Human Resources Office is expending below budgeted levels ($622,000) due to the existence of several vacancies, minimal legal expenses incurred and a delay in training expenses during this fiscal year. Hiring efforts continue to be made to fill the staff vacancies, but progress has been slow. The Human Resources Department has also generated savings by conducting voice stress tests during recruitments instead of polygraph tests.

- Tax Collection and Election expenses are expected to end the year approximately $380,000 under budget. This is almost entirely the result of savings in the election expense category due to Measure A/B election costs being charged to the Bankruptcy Fund as these measures were designed to assist the City through the bankruptcy process and into recovery.

- The Other Administration category holds a variety of City-wide costs that are not attributable to an individual or specific group of programs or departments. As described above, $2.8 million of funding budgeted for potential labor legal and negotiation costs were not utilized in FY 2013 -14 due to the delayed schedule of bargaining group negotiations.

Debt Service Administration costs are distributed between Assessment Districts and City funds based
on the share of total bond issuances. The General Fund’s share of debt service administration expenses in FY 2013-14 exceeds the budget for debt service by $58,000. This overage is due to a late transfer from General Fund to the Debt Administration Fund to cover a prior year budget shortfall. This was authorized by Council Resolution 2014-02-25-1503. Because the correction was for prior year, FY 2013-14 does not require a budget amendment as there are available funds in the Debt Service Administration fund.

Available General Fund Balance

Actions taken by City Council earlier in the year have resulted in budgeted Available Beginning General Fund Balance anticipated at $9.8 million consistent with the LRFP. Based on projections, an additional $16.4 million is anticipated for the General Fund Ending Available Balance. Much of the expenditures savings, primarily from salary savings and slow labor negotiations, are one-time in nature, along with some of the additional revenue over budgets ($401,000 prior year property tax administrative fee adjustment and $200,000 sale of assets). Per Resolution 2014-06-24-1601, Section 9, all of the unencumbered ending available General Fund balance as of June 30, 2014 in excess of the Long Range Financial Plan amount of $9,751,000 will transferred for use in the Bankruptcy Fund ($16.4 million).

Other City Operating Funds

Neighborhood Stabilization Program 3 (NSP3) budget appropriations need to be amended by increasing revenue and expenditures due to loan payoffs coming in higher than budgeted and housing program costs anticipated to be higher by the same amount ($795,000).

Low and Moderate Income Housing Fund (former Stockton Redevelopment Agency) has received more revenue from property tax increment revenue from the Successor Agency. This fund receives a 20% set-aside under a reimbursement agreement that is pledged towards debt payments. This will necessitate an increase revenue and expenditure appropriations by $296,000.

Workers’ Compensation Internal Service Fund (ISF) budget appropriations for revenue and expenditures need to be amended to reflect an increase due to the settlement of several large workers’ compensation claims. The FY 2013-14 budget for workers compensation claims of $7.8 million is based on an annual actuary report that assumes an average amount of the total claim liability will be incurred during the fiscal year. The actuarial estimate takes into consideration that claims costs over $500,000 will be recovered through the City’s excess insurance through CSAC Excess Insurance Authority. In FY 2013-14, the City paid 11 claims over the $500,000 with subsequent reimbursement by the city's excess insurance provider. Reimbursement revenues are conservatively not recognized until they are probable of receipt. For FY 2013-14 reimbursements received were approximately $3.8 million above the budget appropriation of $745,000. Paid claims including those covered by excess insurance totaled $10.1 million and were over budget by $2.3 million. It is recommended that both the revenue and expenditure budgets be increased by $2.3 million.

FINANCIAL SUMMARY

Based on the current projections and unaudited FY 2013-14 year end data, it is estimated that the City's General Fund will end the FY 2013-14 with $9.751 million after $16.4 million is transferred to
the Bankruptcy Fund per Council direction. This information will continue to be updated as additional data becomes available and the audit of the City’s Comprehensive Annual Financial Report is complete.

The following budget amendments are recommended to address projected shortfalls in FY 2013-14 budgets.

**General Fund - Peacekeeper Program**
- Increase Peacekeeper expenditures 010-0138-530 $24,000
- Reduce Grant Match expenditures 010-0000-992 $24,000

**Entertainment Venues**
- Increase General Fund Subsidy 010-0000-992 $267,000
- Reduce General Fund Non-Departmental 010-0131-510 $267,000
- Decrease Revenues 086-3661-347 $267,000
- Increase Subsidy from General Fund 086-0000-492 $267,000

**Neighborhood Stabilization Program 3 (NSP3)**
- Increase Revenues 064-0000-369 $795,000
- Increase Expenses 064-8526-640 $795,000

**Low and Moderate Income Housing Fund**
- Increase Revenues 329-0000-492 $296,000
- Increase Expense 329-0000-992 $296,000

**Workers Compensations Fund**
- Increase Revenues 551-5620-366 $2,300,000
- Increase Expenses 551-5620-571 $2,300,000

Attachment A - 2013-14 Year End Budget Update - General Fund
Attachment B - 2013-14 Year End Revenues - General Fund
Attachment C - 2013-14 Entertainment Venues Budget Update