



STAFF REPORT TO THE CITY COUNCIL

DATE: Regular Meeting of February 14, 2023

TO: Mayor and Members of the City Council

VIA: Dante Hall, City Manager

SUBMITTED BY: Edwin Gato, Director of Finance

SUBJECT: FY 22-23 Midyear Budget Review and Recommended Midyear Budget Appropriations and Adjustments

RECOMMENDATION ACTION:

Receive a report on the FY 22-23 midyear budget review and adopt a resolution approving various midyear budget appropriations and adjustments, as summarized and detailed in attachment 2 and 3, respectively.

EXECUTIVE SUMMARY:

The Midyear Budget review allows the City to adjust the current fiscal year budget (FY 22-23) for changes in projected revenues and expenditures levels that may have occurred since the adoption of the Annual Budget on June 28, 2022. Those changes are contained in this report along with a detailed justification for each recommended change.

BACKGROUND:

This report updates the Fiscal Year 22-23 financial projections and proposes current year budget amendments for various City funds to reflect and respond to the City's current financial condition. Also, this report provides the City Council with updates on the financial status of the City's General Fund by comparing budget projections for revenues and expenditures to actual receipts and expenses as of December 31, 2022.

The discussion below is presented in the following sections:

- I. General Fund Revenues
- II. General Fund Expenditures
- III. General Fund Net Annual Results
- IV. General Fund Operating Reserve
- V. American Rescue Plan Act (ARPA) Fund
- VI. Non-General Fund Programs

ANALYSIS:

As part of the budget process, the City staff must report to the City Council at midyear, examining revenues and expenditures and adjustments if necessary. The process provides an opportunity to review the status of the Budget at midyear to make adjustments to the City's planned operations and Budget. This year's report is attached and includes the following:

- A summary of recommendations.
- Assessments of both operating and capital budgets.
- A schedule showing the recommended midyear budget adjustments for each fund.

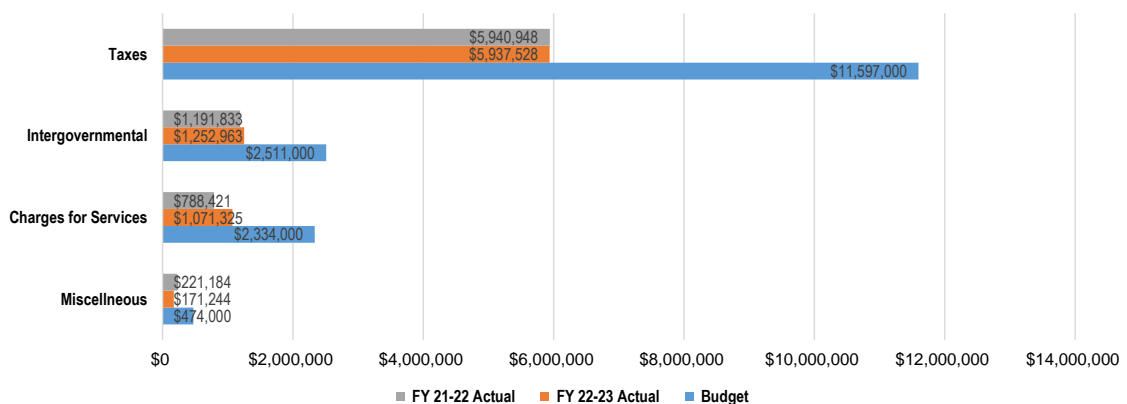
The Midyear Budget Review begins with the good news that at the six-month mark (December 31, 2022), most of the General Fund revenues are above 50%. Expenditures are slightly higher than the original budget due to the outcome of labor negotiations being 1.5% higher COLA than budgeted and upfront payments on insurance and debt service.

General Fund

In accordance with the City's Financial Policies, the annual operating budget was conservative when adopted. This was particularly true as we faced the many uncertainties created by the COVID-19 pandemic. The Policies also call for one-time, non-operating expenditures to be funded from one-time revenues. The City's practice of budgeting conservatively and living within our means remains effective at ensuring that we maintain good fiscal health, and the recommended changes in this Midyear Budget Review remain true to these practices.

I. General Fund Revenues

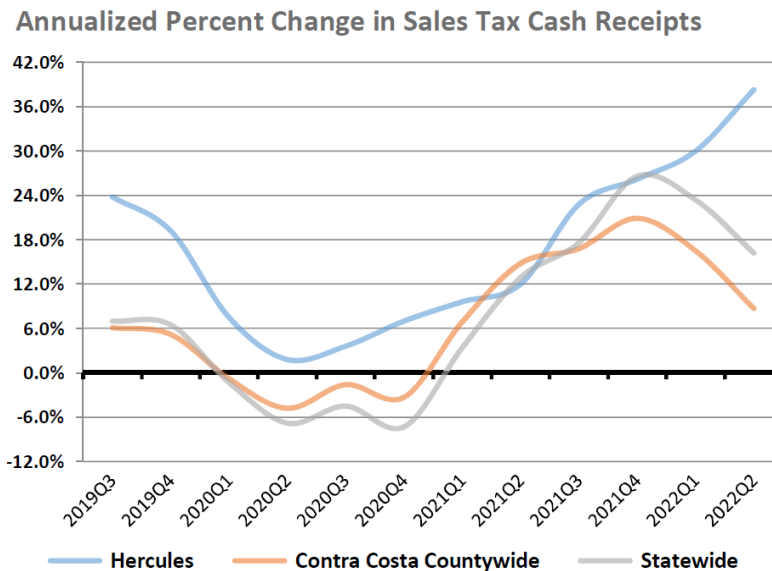
As of December 31, 2022, the General Fund operating revenues were \$8.4 million or 50% of the FY 22-23 adopted budget. Revenues from business licenses, franchise fees, and other taxes are received bi-annually and towards the end of the fiscal year. This accounts for why revenues are below 50% as of December 31, 2022. Also, the revenues received from program fees fluctuate each year. However, these revenues are offset by expenditures incurred by fees. The chart below represents revenue by source compared to the same period last year as of December 31 and how much was collected compared to the budget.



	FY 22-23			FY 21-22		% of Change Comped to PY
	Budget	Actual Receipts 12/31/2022	% Collected	Actual Receipts 12/31/2021	\$ Change Compared to PY	
Taxes						
Utility User Tax	\$3,589,000	\$1,754,196	49%	\$1,790,358	(\$36,162)	-2%
Sales Tax	4,998,000	2,908,360	58%	2,910,540	(2,180)	0%
Property Taxes	1,571,000	886,096	56%	822,033	64,063	8%
Franchise Fees	905,000	270,863	30%	281,963	(11,100)	-4%
Business Licenses	274,000	56,918	21%	48,415	8,503	18%
Transfer Tax	146,000	51,101	35%	80,591	(29,490)	-37%
Transient Occupancy Tax	114,000	9,994	9%	7,048	2,946	42%
Intergovernmental	2,511,000	1,252,963	50%	1,191,833	61,130	5%
Fines & Forefeitures	38,000	16,627	44%	18,325	(1,698)	-9%
Program Revenues						
Community Development	306,000	101,169	33%	111,896	(10,727)	-10%
Parks and Recreation	1,156,000	547,330	47%	294,282	253,048	86%
Police	139,000	50,903	37%	56,394	(5,491)	-10%
Public Works	38,000	25,194	66%	6,418	18,776	293%
Other	11,000	4,729	43%	3,253	1,476	45%
Use of Money & Property	286,000	79,617	28%	127,859	(48,242)	-38%
Cost allocated to other funds	684,000	342,000	50%	316,178	25,822	8%
Transfers In	150,000	75,000	50%	75,000	0	0%
Total, Revenues	\$16,916,000	\$8,433,060	50%	\$8,142,386	\$290,674	4%

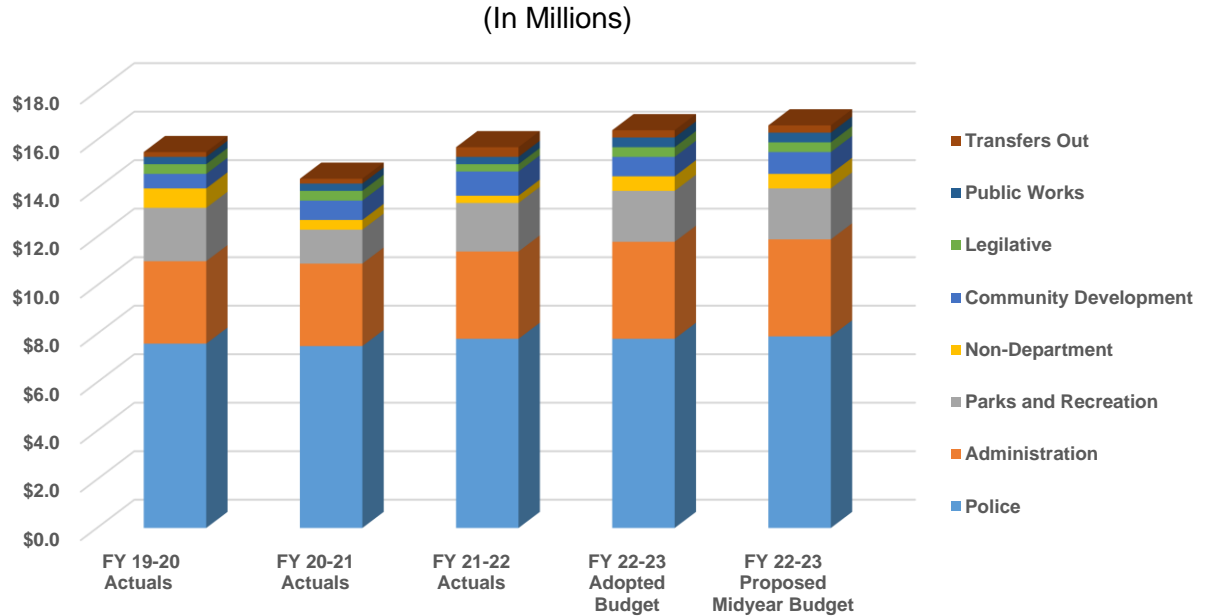
The following are the proposed midyear budget adjustments for the General Fund revenues:

- **Sales Tax:** The pandemic did lead to very conservative estimates for Sales Tax revenues with the adopted Budget. Sales Tax revenues continue to rebound in major tax groups. An annual reduction in general retail (-2%) is offset by growth in all other sectors, especially in Business to Business (22.9%) and Food Products (161%) based on the first quarter review of sales tax activities. Hercules's sales tax revenue is projected to increase by 38.3%. Based on the data analysis and conservatively estimated, based on the current economic climate, Sales Tax revenue is projected to exceed the original annual Budget by \$400,000.



II. General Fund Expenditures

A summary and year-to-date status of General Fund expenditures are presented in Attachment 3, as shown in the following graph. Payments on the insurance premium and debt service payment on equipment leases are due at the beginning of the fiscal year and due to the outcome of labor negotiation being 1.5% higher COLA than budgeted, which accounts for why expenditures are higher than 50% as of December 31, 2022.



Typically, the mid-year budget review and adjustments recommended are to make corrections to the adopted budget and to address required modifications. New initiatives or programs are not often contemplated unless necessary.

General Fund revenue and expenditure budget amendments are proposed to reflect the following adjustments and summarized and detailed in attachment 2 and 3, respectively:

	Increase in Revenues	Increase in Expenditures	Net Impact
Sales Tax	\$400,000		\$400,000
Salary and Benefits (COLA Adjustments) All Bargaining Groups		94,500	(94,500)
New Senior Planner Community Development		44,000	(44,000)
Implementation of Standby and Call Back Public Works		1,000	(1,000)
Pool Maintenance Contract Parks & Recreation		15,000	(15,000)
	\$400,000	\$154,500	\$245,500

III. General Fund Net Annual Results

The General Fund ended last fiscal year (FY21-22) with \$3.9 million in available cash, \$2.9 million better than projections. With the better-than-expected revenue at

the end of the FY 21-22, staff is assigning the available cash balance as follows based on the reserve policy, as amended by the City Council last fiscal year:

- \$977,256 – 25% to Pension Liability
- \$1,954,511 – 50% to Capital Reserve

This will reduce the beginning available cash balance to \$977,255.

The General Fund, excluding ARPA funds, Midyear review is projected to end FY 22-23 with a positive ending available balance of a little over \$900,000, which is \$180,000 better than projected in the adopted FY 22-23 budget. Most of the increase was attributed to the actual financial result of the audited FY 21-22 Financial Statements.

IV. General Fund Operating Reserve

Fiscal stability is an essential factor for all cities. Sound financial management includes the practice and discipline of maintaining adequate reserve funds for known and unknown contingencies. The City's operating reserve policy equals 16.66% of total operating expenditures, or two months equivalent. The General Fund operating reserve exceeded that requirement and maintained a \$4.2 million (including interest income earned) operating reserve equal to 26% of the total operating budget.

V. American Recovery Plan Act (ARPA)

To further assist government entities with the pandemic response and recovery, on March 11, 2021, the American Rescue Plan Act of 2021 (ARPA) was signed into law, making funding available through the State and Local Fiscal Recovery Funds (SLFRF) to assist states, tribal governments, and local governments. On May 10, 2021, the United States Department of Treasury released regulations and updated the local government allocation. As part of the \$1.9 trillion relief package, the City of Hercules became eligible for \$6,285,778 to be paid in two installments. The City received the first payment equal to one-half of the City of Hercules' allocation for \$3,142,889 was received on August 5, 2021. The second half was received on September 1, 2022. Effective April 1, 2022, the Secretary of the Treasury adopted a final interim rule. This rule implements the Coronavirus State Fiscal Recovery Fund and the Coronavirus Local Fiscal Recovery Fund established under the American Rescue Plan Act (ARPA). The following is the summary for the use of Fiscal Recovery Funds based on the final rule:

- General Fund Revenue Loss: The final rule offers a standard allowance for revenue loss of \$10 million. Hercules staff selected the standard allowance as permissible under the revenue loss category and may use the total amount allocated of \$6.2 million for government services.

Currently, the following summary represents the ending balance on ARPA funds:

ARPA funding received	\$3,142,889	\$3,142,889	\$6,285,778
Appropriated:			
Strategic Communication Plan	50,000		50,000
Willow/Palm Sidewalk Installation (Transit Center)	250,000		250,000
Refugio Tennis Court Tree Maintenance	6,000		6,000
Sidewalk and Safe Walkways	100,000		100,000
Community Swim Center Safety Fence Replacement	100,000		100,000
Community Swim Center Gym Floor Replacement & Other Building and Deferred Maintenance	250,000		250,000
Increase appropriation on All Abilities Swing Set	50,000		50,000
Reserve for COVID related expenses	50,000		50,000
E-Gift Card Program	65,000		65,000
HdL Contract - ARPA Administration	164,500		164,500
Building Facilities Plan	75,000		75,000
Parks Master Plan	150,000		150,000
Business Assistance Program	150,000		150,000
Business Rental Assistance Grants	150,000		150,000
			-
Total, Use of Fund	1,610,500	-	1,610,500
Ending Balance	\$1,532,389	\$3,142,889	\$4,675,278

A budget workshop is scheduled in mid-March to discuss Capital Improvement Plan and project priorities. Subsequently, staff will present a proposed ARPA spending plan to the Council for consideration during the FY 23-24 Budget.

VII. Non-General Fund Programs

These funds are driven by grants or other funding sources and are used for specific purposes, such as transportation, gas tax, Measure C “Street Fund,” etc. Such funding sources are restricted, requiring revenues and expenditures to be tracked differently from the City’s primary operating fund, the General Fund. There is sufficient funding to complete current projects or programs and fund the following proposed mid-year adjustments as summarized and detailed in attachment 2 and 3, respectively.

	Increase in Revenues	Increase in Expenditures	Net Impact
Salary and Benefits (COLA Adjustments) All Bargaining Groups		30,000	(30,000)
New Senior Planner			-
Implementation of Standby and Call Back		37,000	(37,000)
Pool Maintenance Contract			-
Uniform and Equipment for Special Response Team (SRT)		30,000	(30,000)
Additional Training		20,000	(20,000)
Pedestrian Sidewalk Improvement at Willow and Palm	1,058,000	1,058,000	-
	1,058,000	1,175,000	(117,000)

Next Step

Staff is currently in the process of preparing the FY 23-24 budget which will be introduced to the City Council on May 9, 2023.

The table below outlines key Council meeting dates at which budget information will be provided.

Date	Action/Topic
February 14, 2023	FY 22-23 Midyear Review & Budget Amendments
March 28, 2023	Budget Workshop to discuss the Five-Year CIP and project priorities, including recommendations for the ARPA funds spending plan
April 11, 2023	Budget Workshop to discuss the Preliminary draft of the FY 23-24 Sewer Enterprise and Internal Service Funds budgets
April 15, 2023	Budget Workshop to discuss the Preliminary draft of the FY 23-24 General Fund Operating budget and other funds (Special Revenues, Debt Service, Agency and Successor Agency) budget
May 9, 2023	Introduction and First Public Hearing of the FY 23-24 Budget and Five-Year Capital Improvement Plan (CIP), including the appropriation of ARPA funds
June 6, 2023	Second Public Hearing and Adoption of the FY 23-24 Budget and Five-Year Capital Improvement Plan (CIP), including the appropriation of ARPA funds

Budget Award

The City of Hercules FY 21-22 Budget was awarded the Distinguished Budget Presentation Award from the Government Finance Officers Association (GFOA) for the third time. This award is the highest form of recognition in government budgeting. Its attainment represents a significant achievement by the organization. Staff submitted the FY 22-23 Budget documents for award consideration.

FISCAL IMPACT:

The proposed budget amendment to the FY 22-23 Budget, as summarized and detailed in Attachment 2 and 3, respectively, will increase the General Fund revenue by \$400,000 on sales tax after the adoption of the FY 22-23 Budget and will increase General Fund expenditures by \$154,500. The General Fund also updated its beginning fund balance based on the year-end results to \$3.9 million and implemented the reserve policy adopted by the City Council last year. Also, as summarized and detailed in Attachments 2 and 3, the net impact of the proposed amendments on all other funds is a reduction in the available fund balance of \$117,000.

The following summarizes the Midyear Budget Adjustments:

	<u>Revenue</u>	<u>Expenditure</u>	<u>Net Impact</u>
General Fund	400,000	169,500	230,500
Non-General Fund	1,058,000	1,175,000	(117,000)
Total	1,458,000	1,344,500	113,500

ATTACHMENTS:

1. Budget Resolution
2. Proposed Budget Amendment
3. Budget Request Detail
4. General Fund Summary
5. Non-General Fund Summary