



STAFF REPORT TO THE FINANCE COMMISSION

DATE: Regular Meeting of March 21, 2019

TO: Members of the Finance Commission

SUBMITTED BY: David Biggs, City Manager
Edwin Gato, Finance Director

SUBJECT: Long-Term Financial Projection for the General Fund

RECOMMENDATION: Review and discuss the long-term financial projection for the General Fund. The report will be presented to the City Council on April 9, 2019.

FISCAL IMPACT OF RECOMMENDATION: There is no direct impact from the preparation and review of an updated long-term forecast. It is a planning tool that can be used to guide future fiscal decisions.

DISCUSSION: The City's finances are managed through four major efforts each year. The development and adoption of a budget for each fiscal which starts July 1st is generally considered the first point in the annual cycle. This is generally followed by the completion and the acceptance of the audit for the prior fiscal year with the goal of having that completed by December 31st or earlier. The completion of the annual audit typically sets the stage for the mid-year budget review in February or March and can include some adjustments or additional appropriations or designations of reserves. The preparation of an update to the long-term forecast would also be done in the March/April timeframe to set the stage for the development of the budget for the next fiscal year.

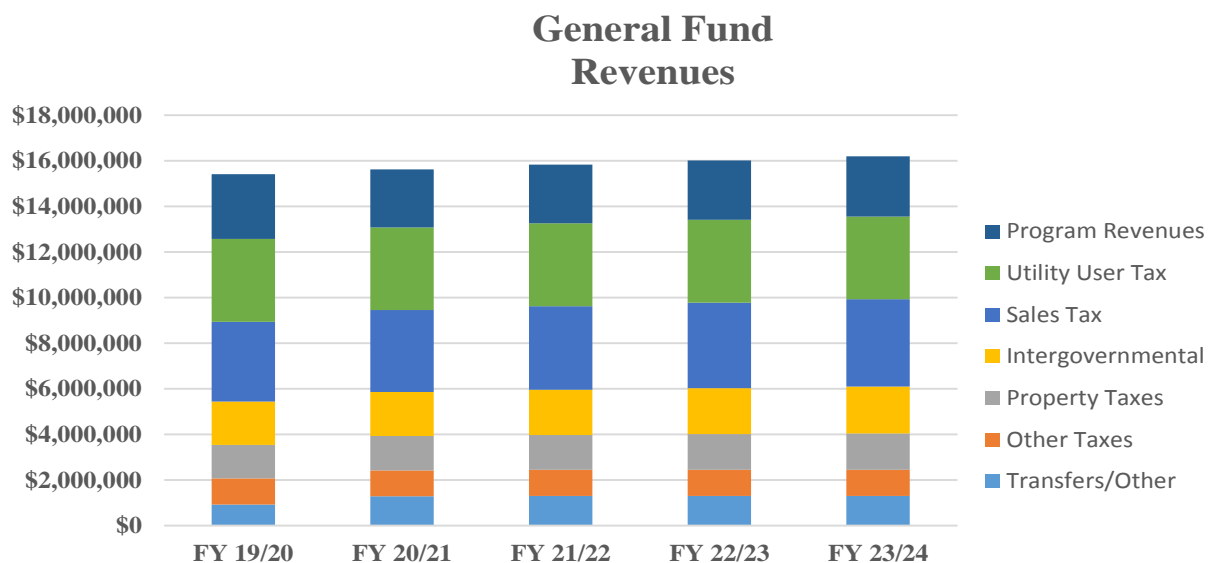
With the City Council having undertaken the mid-year review on February 26th, and with the audit having been received by the City Council on January 22nd, it is timely to review and update Long-Term Financial Projection. The forecast has been updated to reflect the FY 2017/18 audit results with the FY 2018/19 Year-End Projections indicated the mid-year review.

A long-term forecast was prepared for the General Fund for the time period from FY 2019-20 through FY 2023-24.

REVENUE PROJECTION AND ASSUMPTIONS USED:

The General Fund major revenue categories are summarized on page 1 of the Exhibit. The City derives a significant portion of its General Fund revenues from economically sensitive sources such as property taxes, sales taxes (1% Bradley-Burns), and utility users' taxes. When one or more of these key revenue sources deviates from projections, funding for future programs and services may be affected.

As shown in the following graph, General Fund revenues are projected to increase at the rate of 2% a year. Revenue projections for a 5-year forecast period through 2024 range from \$15 to 16 million. The following explains the major revenue assumptions used to estimate General Fund revenues.



- Sales Tax revenue is projected to increase at an average of 2% a year. Total Sales Tax revenue is highly concentrated within one major operator. Over 80% of the City's sales tax is generated by this one producer. The following chart depicts the source of the City's sales tax revenues by industry group. Hercules' sales tax revenue is substantially generated from business and industry sources.
- The City is realizing a stable property tax related revenue growth and assumed at 2% annual growth. Future growth in assessed values above the State Prop 13 annual 2% cap is limited to property turnover or new development entering the tax roll.

EXPENDITURE PROJECTION AND ASSUMPTIONS USED:

The following chart shows the growth in General Fund expenditures. The most significant cost in the General Fund is driven by its labor costs. Labor accounts for almost 60% of total expenditures. Below are significant assumptions used to estimate the cost of salaries and benefits.

1. Regular Salaries – Cost of living (COLA) increase by 2% per year.
2. PERS Miscellaneous and Public Safety Normal Cost rate applied are projected as follows based on CalPERS actuarial assumptions:

	<u>FY 19-20</u>	<u>FY 20-21</u>	<u>FY 21-22</u>	<u>FY 22-23</u>	<u>FY 23-24</u>
Police Classic	18.93%	20.30%	20.30%	20.30%	20.30%
Police 2nd-Tier	17.07%	18.30%	18.30%	18.30%	18.30%
Police PEPRA	10.03%	10.10%	10.10%	10.10%	10.10%
Misc Classic	6.68%	7.30%	7.30%	7.30%	7.30%
Misc PEPRA	3.99%	4.50%	4.50%	4.50%	4.50%

3. PERS Unfunded Accrued Liability (UAL) contribution rate are projected as follows based on CalPERS actuarial assumptions. The rate is calculated using projected payroll.

	<u>FY 19-20</u>	<u>FY 20-21</u>	<u>FY 21-22</u>	<u>FY 22-23</u>	<u>FY 23-24</u>
Police Classic	46.47%	50.49%	31.43%	34.85%	36.95%
Police 2nd-Tier	1.58%	1.15%	0.96%	0.80%	0.68%
Police PEPRA	0.38%	0.49%	0.63%	0.76%	0.54%
Misc Classic	21.22%	23.45%	26.19%	20.76%	21.90%
Misc PEPRA	0.20%	0.30%	0.40%	0.39%	0.47%

DISCUSSION:

Looking into the General Fund 5-year forecast, a deficit between revenues and expenditures for existing service levels is expected to return in FY 19-20 based upon current property, sales, and other general tax revenue trends. Expenditures assumed a projected overall increase at an average of 2% a year. The FY 19/20 projections will be further updated and refined during the adoption of the budget in June 2019. As the City plans its ongoing programs and services, it will need to balance its increasing cash flow requirements for legacy pension/OPEB obligation with commitment to maintain and enhance City services. As shown in Attachment 1, the City have sufficient available cash balance and set-aside operating reserve to cover the deficits.

ATTACHMENT:

1. City of Hercules – General Fund Long-Term Financial Forecast