



DATE: May 16, 2022

AGENDA ITEM # 4

TO: Financial Commission
FROM: John Furtado, Finance Director
SUBJECT: FY 23 Budget Update

RECOMMENDATION:

Provide a recommendation to the City Council to approve the revised budget for 2023

Attachment(s):

Attachment 1 – Capital Projects Final List FY 22-26
Attachment 2 -Revenue, Expenses, and Fund Balances Other Funds
Attachment 3 – General Fund Summary, Revenues, Expenditures, and Transfers Out
Attachment 4 – Staffing FTE by Department
Attachment 5 – GANN Limit Calculations

BACKGROUND

On June 1, 2021, the City Council approved the 2021-2023 Biennial Operating Budget, and as of April 30, 2022, 7 months of the 2021-23 budget cycle have been completed. Throughout the budget cycle, staff actively monitor actual revenues and expenditures and prepare a status update report to the Council at six-month intervals. These updates provide staff with opportunities to advise Council on major budget trends (revenue and expenditure) and propose changes where necessary to meet ongoing service demands or modifications related to economic or other factors. This report provides an informational update to the Finance Commission for the General Fund Operating Budget for Fiscal Year 2022-23, and outlines proposed budget adjustments for other funds. It is the norm of the City of Los Altos to adopt the second year of the biennial budget prior to June 30th of the first year.



SUBJECT: FY 22/23 Revised Budget

DISCUSSION

City Departments completed an in-depth review of their budgets in preparation for the FY 23 budget adoption by the City Council. Departments evaluated their revenues and expenditures, as well as operational trends, and recommended necessary adjustments. In addition, each department evaluated service-level needs and identified any adjustments necessary to respond to changes in the community's demand for services. On May 10th the Financial commission subcommittee met with City staff and discussed the proposed changes and agree with the report as presented below.

The Finance Department evaluated major non-departmental revenue sources (sales tax, property tax, real property transfer tax, business license tax, transient occupancy tax, etc.) to determine what, if any, mid-year adjustments are needed. Finance staff also evaluated any changes in compensation or cross-departmental expenses, such as medical costs or CalPERS rates, and recommend adjustments as needed.

Summary of General Fund Budget for FY 2023

Table 1 outlines projected changes in resources available and their proposed uses in the General Fund for FY2022-2023. These resources are classified into 3 relevant buckets as seen below

Table 1	
General Fund Summary (In millions)	
Projected revenue increase	Amount
Sales Tax	0.39
Property Tax	2.43
Documentary Transfer tax	0.02
Business License Tax	0.03
Transient Occupancy Tax	0.30
Interest Income	0.05
Community Development Fees	0.40
Total Revenue Increases	3.62
One time Items	
ARPA Balances	1.50
Total One Time Available Funds	1.50
Expenditure reductions	
Rosita Park COP *	0.17
Community Center loan*	0.62
Total Expense reductions	0.79
Total Available	5.92

*Funding will now come from the Park in Lieu Fund



SUBJECT: FY 22/23 Revised Budget

Revenues

General Fund revenue is monitored in several categories, including general revenue and departmental revenue. General revenue includes City-wide revenues such as sales and property taxes. Departmental revenue represents monies generated by the activities of operating departments. For example, in Community & Economic Development, revenue is generated through the issuance of building permits and hourly planner charges.

- **General Revenue**

- **Sales Tax** – Sales tax revenues are anticipated to increase by approximately \$0.39 million, based on the most recent estimates by HDL the City’s consultant, and are in line with growth projected at the mid-year update for FY 22.
- **Property Tax** –Property tax revenue is estimated to increase by \$2.43 million also based on our property tax consultants HDL as well as staff projects on the unsecured and ERAF rolls. These are projected to increase by 5.5% over the updated FY 22 Mid-year budget
- **Documentary Transfer Tax** – This category has been minimally adjusted to reflect historical trends and is increase by \$0.02M
- **Business license tax** –Is anticipated to increase over the original budget by \$0.03M
- **Transient Occupancy Tax (TOT)**– The FY 22 budget assumed a \$1 million in TOT, we are seeing stronger growth in this sector and the FY 22 actuals are anticipated to come in higher than projected. For FY 23 we have increased our projection by \$300K from \$1.31 million to \$1.61 million
- **Interest Income** – With a rising rate environment staff predicts that interest income will increase by 0.05M

- **Departmental Revenue**

Department revenues- The City has noticed a lot of development activity and applications for permits, based on staff analysis we are predicting an increase of \$0.4 million for community development. Other departmental revenues are expected to be on target with original projections.

Administrative Fees – The General Fund receives revenue amounting to \$918,500 related to staff costs incurred towards the Sewer and Solid waste Funds, historically these have been treated as revenue for the general fund, which is fundamentally wrong, these should be treated as an offset to costs that are already incurred in the General Fund, therefore staff is proposing to remove this revenue from the general fund and reduce expenditure by the same amount. Furthermore, as indicated in the FY22 final budget appropriations Consumer price index (CPI) has been applied to the Sewer and solid waste funds increasing the amounts by \$227,045 & \$25,120, respectively.



SUBJECT: FY 22/23 Revised Budget

One Time Items

The City will receive \$3.6 million in the second and final installment of the American Rescue Plan Act (ARPA) monies in FY 23. When the original budget was approved \$2.1 million of that was used to balance the budget while the balance of \$1.5 million was designated as a transfer to the ARPA fund. Considering the COVID uptick recently and uncertainty staff is proposing that this money remain unassigned in the General Fund, these funds can be reviewed at mid-year or close of FY 23 and be used to Fund The CIP

Expenditures

Staff performed a detailed analysis of the **Operating Budget**. Staff noticed that there were several errors in the compilation of the budget on the personnel side that resulted in over \$700K of required corrections, some examples were the Finance manager position was frozen in the FY 22 budget and the dollars were used for consultancy services as the position was vacant, however, in the FY 23 budget both the Finance manager budgeted dollars and the consultant dollars were removed causing a shortfall of \$240K. Another permit technician position was also frozen while the employee was, and is still working with the city and therefore requires a restoration of budget to the tune of \$150K, besides these issues the budget also failed to account for several hourly staff that were already employed with the city.

The FY 22-23 budgets had 6 positions vacant and unbudgeted the budgets erroneously removed the unfunded accrued liability (UAL) as well for these positions thereby underbudgeting UAL by over \$110K. The city had made a \$5 million prepayment to CalPERS that was anticipated to yield savings of \$0.33M, however, due to the prior errors the actual reduction made is only \$0.22M

Staff also scrubbed all the operating budgets and made significant reductions to the Litigation expenses for FY 23 which were reduced by \$600K.

The proposed expenses after the above corrections reflect current costs as well as the realignment and restoration of some positions into the budget based on business needs, and the compensation Philosophy adjustments that the council has approved. Total expenses are projected to increase by \$0.3M over the Original FY 23 budget, details can be seen in **attachment 3**

Staff also reviewed the **Capital projects list (Attachment 1)**, detailed listing of the changes is listed below and should be read in conjunction with Attachment 1 of this staff report.

Staff was able to identify projects that could be removed, reduced, or find alternative funding sources. This exercise resulted in \$728,126 of prior appropriations to be released. For the FY 22/23, CIP listings staff considered internal resources and ability to complete the projects and decided to prioritize accordingly, with some projects either eliminated, advanced, or moved to different years.



SUBJECT: FY 22/23 Revised Budget

Table 3 shows a summary of the details in attachment 1.

Table 3	
CIP General Fund Summary (In Millions)	
	Budget Amounts
Project Summary	
Estimated Prior Appropriated	6.13
Projected FY 2022 Expenditure	5.75
Projected FY 2023 Expenditure	4.03
Total Allocated	15.91
Funding Available	
CIP Reserves FY 22	12.16
CIP Cancelled projects	0.73
FY 22 Mid Year approved Transfers	2.92
Total Funding Available	15.81
Projected Excess/ (Shortfall) for FY 23	(0.10)

Key changes were made to CIP projects listed below

List of Projects changed, reduced, or eliminated (General Fund)

CD-01012 Annual Storm Drain Improvements– added cost of \$88,758 in FY 22/23 based on Engineers’ estimate of, \$350,000/- the contract has been awarded to the consultant.

CD-01017 First Street Streetscape Design Phase II – added cost in FY 21/22 based on Engineers’ estimate, \$88,758/- the contract has been awarded to the consultant.

CF-01003 Annual Civic Facilities Improvement - FY 2022/23 reduced by \$100,000 in FY 22/23 & FY 24-26 \$1,200,000 from each year removed as in the future we will bring specific projects related to improvements.

CF-01010 Annual ADA Improvements (Facilities)– Prior appropriations did not have identified projects and therefore prior appropriations of \$316,883 are removed, also the FY23-26 amounts of \$75,000 in each year are removed.

CF-01011 City Hall Emergency Backup Power Generator - \$150,000 moved from FY 22/23 to FY 23/24 as it is not anticipated to be completed in FY 22/23.

CF-01013 MSC Fuel-Dispensing Station Overhead Canopy- The project is not needed based on regulations therefore the FY 23/24 allocation of \$300,000 is removed.



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CF-01018 MSC Parking Lot Resurfacing – The project is not expected to commence in FY 22/23, therefore \$15,000 for design is moved to FY 23/24 & \$1,285,000 for construction is moved to FY 24/25

TS-01008 Annual ADA Improvements (Streets and Roadways) - Since prior appropriations exist (\$136,697) the FY 22/23 & FY 23/24 allocated amounts of \$200,000 each are removed.

TS-01013 Annual Transportation Enhancements – Since prior appropriations exist (\$216,313) the FY 22/23 & FY 23/24 allocated amounts of \$75,000 each are removed.

TS-01051 University Ave/Milverton Rd Sidewalk Gap Closure - The project needs for FY 22/23 are reduced by \$80,000 and \$500,000 is added to FY 23/24 to complete the construction phase of the project.

TS-01052 Annual Bicycle/Pedestrian Access Improvements - The FY 22/23 allocation of \$350,000 is removed as prior balances exist (\$313,712) and in FY 23/24 \$1,318,000 and 4,111,000 in FY 24/25 are added to account for the completion of the design and construction of the project.

TS-01055 Fremont Ave Pedestrian Bridge Rehabilitation – In FY 22/23 \$100,000 in added to meet the current Engineer’s estimate of construction.

New Projects

Carmel Terrace Sidewalk Gap Closure In FY 23/24 \$350,000 is added as this project was a prior council priority as well as a priority of the Complete Streets Master Plan.

Emergency Storm Drain Outfall Repair (Montclair Way)- FY 22/23 added \$65,000. The City maintains a 1-inch storm drain line that passes along the southerly side of the property located at 1266 Montclair Way and eventually outflows into Permanente Creek, which borders the westerly property line. The bottom portion of the storm drain pipe that outfalls into the creek has rusted away, causing the creek bank to erode. This project is to perform an interim repair to stop the bank erosion.

Emergency Retaining Wall Repair Along Path to Access the Windimer Ditch- FY 22/23, added \$132,000 The City maintains the storm drainage ditch located within a public utility easement along private properties behind Windimer Drive, Sierra Ventura Avenue, and Via Huerta. The City has observed safety concerns stemming from old, failed, short retaining walls in the existing access through the easement at the rear of one of the properties. The project includes the necessary repairs to address the tripping hazards.

999 Fremont- FY 22/23 \$10,000 is added for the setting up of a Police Substation at the location which is currently unused.



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Park in Lieu Funded Projects

CF-01019 Veterans Community Plaza Shade Structure- The Original project was downsized and completed in FY 20, therefore the prior appropriations of 45,476/- are being released

CF-01017 Annual Park Improvement Project- In prior Years the Park in Lieu projects were grouped under a General CIP project named the “Annual Park improvement project”, with remaining funds carried over each year, THE CIP currently has a prior appropriated balance of 334,396 and a further amount of \$750,000 in FY 21/22 of which only \$14,136 is spent and another \$13,189 is encumbered. As part of the new philosophy, the staff is advocating CIP projects would need to be specifically identified to the individual location level, therefore we have removed \$1,000,000 of prior appropriations and allocated the future years FY 23-26 on the individual projects listed on the sheet and below.

CF-01023 Grant Park Master Plan – Since we have received direction from council on the Grant Park and have allocated \$1,000,000 towards the same as seen below the \$150,000 reserved for the masterplan is not required at this time

New Project - Designated Picnic Areas - \$80,000 allocated in FY 22/23. This will meet a current need for reservable picnic areas as well as generate revenue. The city currently only has 2 reservable picnic areas, Patriots Corner at Shoup Park and Grant Park.

New Project- Naturescape - \$35,000 allocated in FY 22/23. Naturescape is a play/exploration area that is composed of all-natural features. Components such as tree stumps, downed trees, wood chips, and sticks of various sizes. It is located in the Redwood Grove Nature Preserve

New Project- Drainage and Drinking Fountains- \$180,000 allocated in FY 22/23. The funds will be used to install appropriate drainage systems and drinking fountain/hydration stations in identified park locations. Stations may include bottle fillers and dog dishes.

New Project- Park Shade-\$120,000 allocated in FY 22/23. Based on the 2012 Parks Master Plan Update, and will provide shade in parks where appropriate.

New Project- Hillview Dog Park- \$50,000 allocated in FY 22/23 & \$500,000 allocated in FY 23/24. These are estimated costs based on a full design of a fenced-in dog park.

New Project- McKenzie Dog Park- \$50,000 allocated in FY 23/24 & \$500,000 allocated in FY 24/25. These are estimated costs based on a full design of a fenced-in dog park.

New Project- Facilities Assessment- \$250,000 allocated in FY 22/23. This assessment will review the condition of all recreation facilities to determine future needs and help inform the prioritization process.

New Project- Grant Park Facility (Electrical, Hot Water, HVAC)- \$600,000 allocated in FY



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22/23 & \$400,000 allocated in FY 23/24. The scope of work is to upgrade electrical panels to increase load capability, provide HVAC to allow the facility to become a cooling center, and provide access to hot water.

New Project- Shoup Park Playground- \$207,000 allocated in FY 23/24 & \$828,000 allocated in FY 24/25. These are based upon the Park Master Plan Update, to replace the playground at Shoup Park as it is at the end of its expected lifespan. Pour-in-place rubber is recommended to reduce maintenance and increase safety and accessibility for children with disabilities.

New Project- Marymeade Playground- \$110,000 allocated in FY 24/25 & \$440,000 allocated in FY 25/26. These are based upon the Park Master Plan Update, to replace the playground at Shoup Park as it is at the end of its expected lifespan. Pour-in-place rubber is recommended to reduce maintenance and increase safety and accessibility for children with disabilities.

New Project- McKenzie Playground-\$145,000 allocated in FY 24/25 & \$580,000 allocated in FY 25/26. These are based upon the Park Master Plan Update, to replace the playground at Shoup Park as it is at the end of its expected lifespan. Pour-in-place rubber is recommended to reduce maintenance and increase safety and accessibility for children with disabilities.

New Project- Hillview Fitness Equipment-\$ 30,000 allocated in FY 25/26 based upon the Park Master Plan Update, replace adult fitness equipment at Hillview Park as it is at the end of its expected lifespan.

The projects listed below were originally in the General Fund under “Annual Facilities Improvements” and are now moved to the Park in Lieu as they are related to parks.

Moved Project - Garden house Upgrades- \$125,000 allocated in FY 23/24 to upgrade painting, flooring, kitchen, and fixtures to modernize and enhance the space to improve community experience and increase rentability.

Moved Project - San Antonio Club Upgrades- \$125,000 allocated in FY 23/24 to explore the feasibility of expanding classroom and teacher space, new windows and doors as well as improvements to outdoor space.

Moved Project - Rebuild Grant Park Basketball Court-\$150,000 allocated in FY 22/23. The Court is in bad shape and requires a complete rebuild.

Public Art Fund Projects

CD-01003 Annual Public Art Projects- added cost in FY 22/23 based on Public Arts commission’s unanimous recommendations, \$80,000/- was added to the prior budgeted amount of \$50,000, which will be sufficient to cover the commission’s plans after accounting for prior appropriated balances, which are listed below.

\$30,000 for maintenance of existing artwork

\$27,000 for the purchase of two existing artworks (T2 and Midnight Stomp Series)

\$15,000 for a Call for Art

\$7,000 for community engagement events and projects

\$75,000 for a new, commissioned gateway piece



SUBJECT: FY 22/23 Revised Budget

Infrastructure Technology Fund Projects

New – Financial system Project– added cost in FY 22/23 based on quotes received for new financial system implementation, \$350,000/-

Other Funds CIP Projects

No changes have been recommended to other CIP projects funded by the other funding sources.

Table 2 Outlines funding needs for the proposed FY 23 budget it is noteworthy to see that most of these listed are restoring items that were dropped without a plan when the original budget was adopted.

TABLE 2	
<u>Funding Needs (in millions)</u>	
Fund Name	FY 22
General Liability	1.00
Workers Compensation	0.86
Dental Fund	0.02
Equipment Replacement	0.30
Operating Reserve to 20%	1.08
Operating Budget Adjustments	0.53
CIP 23 Funding Required	0.10
Total Funding Needs	3.89
Available	2.52
<u>Proposed uses</u>	
CALPERS UAL Prepayments	1.00
Contingency Reserve	0.25
Unassigned Fund Balance	1.27
Total Proposed uses	2.52



SUBJECT: FY 22/23 Revised Budget

Staff worked with the Subcommittee of the Financial Commission to review a list of unfunded expenses in the original budget and the following was proposed.

The **General Liability Fund** General Liability coverage has increased exponentially for most cities in the bay area with premiums jumping over 40-60% over the last 3 years, the original budgets for FY22 & 23 provided funding of \$0.50 & \$0.81 million respectively, however, the General liability costs incurred in FY 21 have exceeded \$1 million and are expected to increase further in FY 23. In order to address this major cost escalation, staff has looked at claim history and decided to raise the Self-insurance Retention (SIR) from X to X. Staff is proposing that \$1 million, \$ 150K, and \$50K be transferred from the General Fund, Sewer Fund and Solid waste fund respectively.

The **Worker's Compensation Fund** was not funded in the original budget the latest actuary report from Bickmore Actuarial projects a need of \$.86M from the General Fund.

The **Dental Fund** received a transfer of \$100,000 in FY 22 to cover the negative fund balance, staff has reviewed based on current staff that at minimum another \$20K will be needed in the additional budget for the fund to meet its commitments for the year.

The **Equipment Replacement Fund** is projected to have a negative fund balance of \$4,873 by the end of FY 23, recently at the staff annual retreat one of the biggest concerns by city staff was the poor equipment, tools, and furniture such as chairs and tables that are in service today being outdated or dangerous. Staff currently recommends moving \$300K from the General Fund to the Equipment replacement fund to cover the immediate, replacement needs. City staff will have to create and implement a Fleet and Equipment Replacement plan to address the remaining unfunded needs.

The Financial policies for the City recommend a 20% **Operating Reserve** for the General Fund, based on the current level of expenditure the amount needed to bring the reserve to 20% would be \$1.03 million (based on FY 23 expenses). The operating reserve currently stands at 17.9%. The subcommittee discussed this in detail and based on their prior feedback recommended that we build the reserve back up to 20% with the available funding staff is currently recommending a transfer of \$1.03 million from the General Fund Unreserved fund balances be moved to the Operating reserve.

Operating Budget. The details are listed in the expenses section the total increase to the operating budget after all adjustments is \$0.3M.



SUBJECT: FY 22/23 Revised Budget

The Subcommittee also reviewed the **Capital projects** list for FY 23 and agreed to the recommendation to transfer the required shortfall to the CIP fund as shown in table 3 below.

Details of the CIP changes have already been presented separately in this report.

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Total Funding Available	15.81
Projected Excess/ (Shortfall) for FY 23	(0.10)

The Subcommittee also accepted the staff's proposed uses of the balance of \$2.52 million of available resources as listed below.

Setting up **Annual discretionary payments (ADP)** to CALPERS to reduce the unfunded liability, the committee felt that the \$1 million ask was reasonable.

Setting up a **Contingency Reserve** Staff has scrubbed the operating budgets of all departments as well as denied requests for budget increases, we also stopped the practice of departments holding on to operating budget contingencies for "What if" scenarios. The primary reason we were able to do that was to convince leadership that a centralized **City Manager Contingency Reserve** would be proposed. Staff recommends that we create this reserve and fund it at \$250K

The **unassigned fund balance** is projected to be \$1.5 million, given the uncertainty and uptick in COVID cases in recent days, while also considering that we have increased our projections on TOT we propose that the \$1.27 million remain unassigned at this time. We will review this amount at the FY 23 mid-year to identify if any adjustments need to be made. In any case, this unassigned balance can be allocated to the FY 24 CIP when we close the FY 23 books.



SUBJECT: FY 22/23 Revised Budget

Changes to Other Major Funds (Attachment 2)

Attachment 2 provides a listing of all other funds in the City; no major changes have been made to these except for the below. Changes in fund balances due to CIP allocations is covered with the CIP detail.

Park in Lieu Fund – The eligible costs of servicing the annual Debt for the Rosita Park (\$171.8K) and the community Center (\$622K) have been programmed to this fund.

Sewer Fund – The Sewer Fund staff have seen increased professional services costs and have requested a \$221,400 increase in the budget.

Staff has also in line with what was done if the final reconciliation for FY 22 applied the Consumer Price index (CPI) factor to the administrative fees charged to the Sewer Fund increasing the contribution to \$227,045.

Staff has noticed that the general liability contributions from the Sewer Fund were not made in the original budget therefore we propose a transfer of \$150,000 from the Sewer fund to the General Liability Fund.

For the Sewer Fund, the total of the required additional appropriations for FY 23 \$598,445; however additional budget appropriations are not currently required because when the original budget was produced \$801,803 of the Solid Waste Fund budget was also appropriated to the Sewer Fund in error.

Solid Waste Fund – The Solid Waste Fund staff have seen increased professional services costs and have requested a \$62,620 increase in the budget, staff also determined that other eligible solid waste costs related to trash receptacles of \$130,176 could be paid from the Solid Waste Fund.

Staff has also in line with what was done if the final reconciliation for FY 22 applied the Consumer Price Index (CPI) factor to the administrative fees charged to the Sewer fund increasing the contribution to \$25,120 and factored the undercharged amount of 36,500.

Staff has noticed that the general liability contributions from the solid fund were not made in the original budget therefore we propose a transfer of \$50,000 from the Solid Waste Fund to the General Liability fund.

On the Personnel side, the Solid Waste Fund supported one sustainability coordinator who has since left the city, part of the feedback gathered was that the work involved was too much for a single person, looking forward at the plans the city has developed this seems to be a true statement, therefore, we are proposing the addition of another position at the sustainability specialist level.

For the Solid Waste Fund, the total of the required additional appropriations for FY 23 is \$372,796.



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GANN Limit

Attachment 5 shows the GANN limit calculation for the city, The GANN Limit is a limit on the amount of tax money that state and local governments, including school districts, can legally spend. In November 1979, California voters approved the late Paul Gann's Proposition 4, which is called the Gann Limit.

Staff reviewed the calculations for the current year, the Gann limit builds on the prior year's data each year, and staff was unable to verify data beyond FY 2016. The current Gann limit for the city shows that we are at 97% of the limit which in effect means we will be unable to raise more taxes via a bond measure and if tax revenues come in excess of \$1.5M, we would be forced to return the funds to the taxpayers. Furthermore, since the limit is based on inflation and population a decrease in both factors will further shrink our limit.

We are unsure of the methods used to calculate the Limit each year in the past and the 97% current limit seems unlikely to be correct, we are recommending that a consultant be hired to review and compile the data from inception, most cities have Gann limits in the 50 -70% range.

Conclusion

As of the revised FY 23 update, revenue projections, including general revenue and department fees and charges, are trending higher than the original budget projections as adopted in May 2021, notwithstanding the proposed changes above. Overall, expenses have been adjusted as shown on this report. It is expected that the FY23 operating budget will continue to be balanced, largely due to the stimulus funding received via the American Rescue Plan. This funding has proved to be vital in helping the city navigate the FY 22 & 23 budget years by providing the much need bridge revenue as the economy opens and impacted revenues begin to recover. As mentioned at mid-year we see significant foreseeable challenges such as high inflation and an uptick in COVID cases these factors could impede our revenues and could cause unforeseen cost escalations across the board, some of these are already apparent with construction bids coming up 20 -30% over-engineer estimates.

We, therefore, restate the need to retain the balance of available funds as unassigned to meet these future uncertainties.