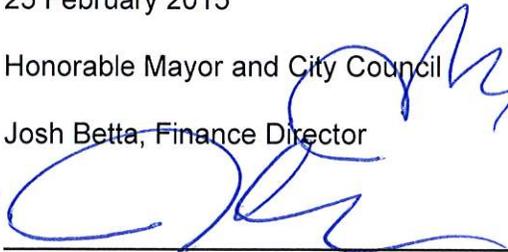


City of Bell Agenda Report

DATE: 25 February 2015

TO: Honorable Mayor and City Council

FROM: Josh Betta, Finance Director

APPROVED BY: 

 Doug Willmore, City Manager

SUBJECT: **Fiscal Year 2014-15 Midyear Financial Status Review**

Recommendation

Receive and file.

Background

Section 604 (d) of the City of Bell Charter stipulates that the Chief Administrative Officer shall “keep the City Council advised of the financial condition and future needs of the City and make such recommendations as my seem desirable.”

The Midyear Review focuses most attention on the condition of our General Fund, as the General Fund is the City’s largest fund, and thus provides the foundation for most service delivery in the City.

Adopted General Fund FY 2015 Budget – “Managed Structural Deficit” of \$1,481,029

Last year, during FY 2014, the City of Bell enjoyed an increase in net fund balance of \$22,248,048 owing to infusion of one-time revenues in the aftermath of the scandal. It resulted that during budget deliberations last Spring, deliberations that included five (5) public community meetings, considerable discussion was given to the inclusion of “expenditure items of above status quo budget” totaling \$1,489,203 in order to advance and improve the City organization – by creating new employment positions and establishing special projects.

The \$1,489,203 is comprised of \$780,803 in permanent, recurring costs and \$708,400 in one-time, non-recurring costs.

With its adoption of the FY 2015 Budget, the City Council approved and authorized all \$1,489,203 of expenditure items above status quo. In this manner, the City of Bell embarked upon a deliberate plan of “managed structural deficit” (that is, a deficiency of revenue to expenditure) totaling \$1,481,029. (See **Attachment 1** for City Manager’s discussion of managed structural deficit).

The additional spending was re-authorized by the City Council on October 22nd, at a regular Council meeting designed to reconsider the additional spending plan.

The additional spending is summarized by department/function below together with the corresponding percentage of the increase. The detailed listing of additional spending is included as **Attachment 2** to this report.

**FY 2015 Budget
Summary of Exceptional Expenditure Items**

City Council	150,831	10%
Human Resources	35,000	2%
City Clerk	60,000	4%
Finance Department	74,419	5%
Non-Department	119,000	8%
Community Services Department	589,619	40%
Police Department	316,381	21%
Community Development Department	143,953	10%
Total Exceptional Items	1,489,203	100%

With the addition of \$1,489,203 in expenditures above the status quo budget, the adopted General Fund deficit in FY 2015 is \$1,481,029.

Without the addition of the additional expenditures, a General Fund budget surplus \$8,174 would result.

On October 22, 2014, the City Council considered reducing these expenditure additions, but did not, in the end, act to reduce spending.

CalPERS Contribution Increase

The CalPERS retirement system suffered devastating portfolio losses during the Great Recession that spanned the years 2008 through 2010, depending on measurement criteria. Investment earnings are only now beginning to approximate the historical earnings enjoyed by the world's largest pension fund in prior years.

The effects of the Great Recession combined with vocal and widespread political support for "pension reform" created an environment in which CalPERS has been forced to require additional payment from member agencies that have large unfunded pension liabilities. The City of Bell, given its generous improvement of retirement plans just prior to the Great Recession as administered by the Rizzo regime, will be required to pay an approximate \$730,000 more toward unfunded liabilities each year going forward. We are stuck with the bill for Rizzo's actions to improve pension benefits, in other words.

The effects of these additional payments add to the City's structural budgetary deficit. A projection of estimated outcomes is discussed below.

The “Managed Structural Deficit” in Future Years

The premise behind the managed structural deficit is investment in future economic development and community aesthetic improvement.

Three potential future outcomes become apparent for the General Fund going forward.

Financial Projection Assuming Economic Development The General Fund financial projection of future outcomes, assuming accelerated economic development activities, is graphically depicted in **Attachment 3** to this report. This projection suggests that the City will maintain a managed deficit position of approximately \$1,523,000 next year, Fiscal Year 2016, and that the deficit will lower itself to \$1,086,000 in FY 2019. During the four-year period between FY 2016 and FY 2019, however, the General Fund deficit spending will average \$1.275 million per year, and an estimated total of \$5.1 million of deficit spending will be incurred.

Financial Projection Assuming No Notable Economic Development The General Fund financial projection of future outcomes, assuming no notable economic development activities, is graphically depicted in **Attachment 4** to this report. This projection suggests that the City will maintain a managed deficit position of approximately \$1,523,000 next year, Fiscal Year 2016, and that the deficit will only lower itself to \$1.221 million in FY 2019. However, during the four-year period between FY 2016 and FY 2019, the General Fund deficit spending will average \$1.3 million per year, and an estimated total of \$5.3 million of deficit spending will be incurred.

Financial Projection Assuming No Notable Economic Development and General Fund Assumption of Retirement Fund Shortfall The General Fund financial projection of future outcomes, assuming no notable economic development activities, and the assumption of \$880,000 in annual Retirement Fund deficits, is graphically depicted in **Attachment 5** to this report. This projection suggests that the City will maintain a managed deficit position of approximately \$2.4 million next year, Fiscal Year 2016, and that the deficit will only lower itself to \$2.1 million in FY 2019. However, during the four-year period between FY 2016 and FY 2019, the General Fund deficit spending will average \$2.2 million per year, and an estimated total of \$8.8 million of deficit spending will be incurred.

What if We Don’t Want a “Managed Structural Deficit” in Future Years?

Deficit spending, regardless of purpose, poses an obvious obstacle to other uses of the City’s FY 2014 revenue windfall.

Deficit spending will restrict the City’s ability to:

- (1) establish a Legacy Fund for economic development,
- (2) reduce the utility users tax,
- (3) establish an Other Post-Employment Benefits (OPEB) trust to pay down employment liabilities, or
- (4) transfer to the Retirement Fund to eliminate an accumulated Fund deficit (see discussion below).

Should the City Council desire reconsideration of its managed deficit spending plan, a first step would be to instruct its Interim City Manager to develop a FY 2016 Proposed

Budget that establishes a plan to balance available revenue and proposed expenditures. It is estimated at this writing, at a time before annual budget preparations have commenced, that the City's initial FY 2016 deficit position, given the three financial projections discussed above, ranges between \$1,523,000 and \$2,403,000.

If the Interim City Manager were instructed to propose a balanced budget, it is conceivable that the largest expenditure reductions would be considered in the areas that received the largest infusion of deficit budget spending. Reductions are easy to articulate in theory, but much harder to make in practical terms. The City has created meaningful service enhancements through the application of the deficit spending that would require great political will to reverse. Making matters more complicated, large portions of this deficit spending were focused on hiring additional staff – 3 new police positions, for example – and staffing reductions would likely result in meet-and-confer obligations with employee labor groups.

FY 2015 General Fund Estimated Outcome

As discussed above, the Adopted General Fund Budget is unbalanced by intent in order to apply one-time proceeds to important community objectives.

A summary of the originally adopted budget is provided as **Attachment 5** to this report. This attachment discreetly presents the additional expenditure plan above "status quo" expenditures.

There is, of course, always a difference between a budgetary plan and year-ending outcomes. All businesses confront unexpected budgetary events. In this light, **Attachment 6** to this report offers estimation of year-end outcomes based on unexpected events that either increased revenue, increased expenditures, or reduced expenditures.

With a net decrease in expenditures of \$316,045 in the FY 2015 Budget expected at this writing, it is projected that the total deficit at year end, as displayed in **Attachment 6**, will be \$1,164,984.

General Fund Reserves

City of Bell
General Fund Reserves

	Actual at June 30, 2011	Actual at June 30, 2012	Actual at June 30, 2013	Actual at June 30, 2014	Projected at June 30, 2015
Total Reserves	1,709,209	303,292	(1,486,331)	20,753,917	19,588,933
Total Expenditures	16,560,450	12,498,795	14,895,056	15,932,271	14,835,929
Reserves as % of Expenditures	10.3%	2.4%	-10.0%	130.3%	132.0%

The General Fund reserve position, given the one-time infusion of receipts in FY 2014, demonstrates that the City's financial turnaround is complete . A reserve position of -10% at

June 20, 2013 is now, following audit, 130% at June 30, 2014. The City's Budget and Fiscal Policies call for a 25% reserve ratio. Our reserve position is quite comfortable.

The reserve position could be altered dramatically by transfer out to create the Legacy Fund (for economic development), a reduction in the utility users tax, or a transfer out to cover the accumulated Retirement Fund deficit (see discussion below).

Continuation of a managed structural deficit will reduce reserves by an approximate \$1.5 to \$2.4 million per year.

The Retirement Fund

The City's Retirement Fund has a chronic pattern of deficit spending owing to increasing retirement and post-employment health care costs and debt service obligations. A pattern of transfers in from the General Fund has been necessitated in recent years to avoid Fund deficit.

In FY 2013, it came to our attention that we were experiencing a decline in revenue collections from this property tax assessment established in 1944. Similar decline became apparent in the other 11 cities in Los Angeles County that have authority to levy the tax. The exact amount of annual loss is difficult to determine with precision because the County not only collects the revenue for cities, but also distributes proceeds to cities according to its own formulas. It is a case of the fox guarding the hen house. Working from known base data in FY 2013, however, it appears the annual takeaway approximates \$660,000, but it could be higher.

The pension tax is being withheld due to the State Department of Finance's direction to Los Angeles County to withhold pension levy proceeds due to their unique (and disputed) interpretation of Redevelopment Dissolution law.

Although the City secured positive agreements with employee groups regarding self-payment of retirement contributions – estimated to save about \$411,000 annually beginning in FY 2015 -- continued revenue withholding and increasing costs have resulted in a deteriorating Retirement Fund financial position. The City has been seeking legislative remedy to date. If the City is not successful in the legislative arena or in any future litigation, continuing deep annual Fund deficits will result. Annual deficits will become the obligation of the General Fund.

Retirement Fund -- CalPERS Service Credit Reversal

Prior to public knowledge of the excessive salaries being fraudulently paid to former employees and City Councilmembers, the City was also making retirement contributions on behalf of these individuals. The contributions were made as a percentage of earnings according to levy rates in effect each fiscal year. Following the City's success in reducing pensionable earnings for these individuals, the City began collaboration with PERS representatives to reverse incorrect salaries reported and re-report allowable earnings.

This project continues via the efforts of Human Resources staff. At this writing, it is estimated that the City can expect a credit from PERS in the amount of \$727,000. It is a rare event for PERS to issue cash reimbursement to a member agency, so we hold no expectation of a cash reimbursement; rather, we expect that the credit will be applied to future actuarial contribution calculations.

Retirement Fund Reserves:

City of Bell
Retirement Fund Reserves

	Actual at June 30, 2011	Actual at June 30, 2012	Actual at June 30, 2013	Actual at June 30, 2014	Projected at June 30, 2015
Total Reserves	976,319	1,063,780	15,881	(881,652)	(2,187,419)
Total Expenditures	2,362,480	2,119,586	2,381,620	2,323,725	2,011,700
Reserves as % of Expenditures	41.3%	50.2%	0.7%	-37.9%	-108.7%

FY 2014 witnesses the first year-ending fund deficit in the Retirement Fund, as shown above. When the City’s budgetary plan for FY 2015 is inserted into the data, an estimated Retirement Fund deficit of \$2.2 million is expected at June 30, 2015.

It is highly likely that the General Fund will eventually be required to eliminate accumulated deficit in the Retirement Fund through transfers in. It is a question of timing that revolves around the success or lack of success in achieving remediation through legislative or legal means as conditioned by auditor opinion. In general, running a shorter-term deficit is not problematic if the auditor believes the agency possesses means to address the deficit in due course. Our auditors concur that the City of Bell’s General Fund reserves are robust enough to address the deficit when appropriate.

Other Post-Employment Benefits (OPEB):

The City, in accordance with contracts and agreements with employees, provides health care benefits to retired employees that are paid from the Retirement Fund. The actuarially determined annual contribution for FY 2014 was \$1,400,793, and the City made \$517,605 in contributions on a “pay as you go” basis during the year. A similar disparity exists in FY 2015 and will continue in future years.

The net OPEB obligation facing the City is \$8,830,402. The net obligation increased by \$883,188 during FY 2014, and will increase in future years in similar fashion.

Until the conclusion of FY 2014, the City of Bell has never been in a financial position to exercise its option to establish a trust for the purpose of funding and paying down the OPEB debt obligation. As the City ponders financial decisions in the future, the creation of an OPEB trust designed to pay down the \$8.8 million OPEB obligation should be considered.

Attachments:

- Attachment 1: City Manager’s Discussion of Managed Structural Deficit
- Attachment 2: Detail Listing of “Items Above Status Quo” that Create Managed Structural Deficit

Attachment 3: General Fund Financial Projection Assuming Economic Development
Attachment 4: General Fund Financial Projection Assuming No Notable Economic Development
Attachment 5: General Fund Financial Projection Assuming No Notable Economic Development
and General Fund Assumption of Retirement Fund Deficit
Attachment 6: FY 2014-15 Adopted General Fund Budget
Attachment 7: Projected FY 2014-15 General Fund Budget Outcomes

Attachment 1: City Manager's Discussion of Managed Structural Deficit

City of Bell
6330 Pine Avenue
Bell, California 90201
383-588-6211
383-771-9473 (fax)



Nestor E. Valencia, Mayor
Alicia Romero, Mayor Pro Tem
Violeta Alvarez, Council Member
Ana Maria Quintana, Council Member
Ali Saleh, Council Member

July 15, 2014

City Manager's Adopted Budget Message

Honorable Mayor and City Council,

While interested observers throughout the United States watch, the City of Bell – its City Council, citizens and staff – are creating the “New Bell.” The legal system has punished wrongdoers, a firm financial foundation has been established, and we now work to complete the phase of transforming the organization into a model of good government.

Fiscal Year 2015 marks our step into a new direction of financial and economic development planning. Only a few short months ago, the City collected \$5.7 million in legal settlements from those who did wrong to our community, \$4.8 million from the liquidation of an illegally-devised supplemental retirement program, and \$15.2 million from the sale of valuable land adjacent to Interstate 710. In all, this \$25.7 million one-time infusion of cash has created an enviable General Fund reserve position of approximately 188%.

With such an abundance of General Fund reserves, the City of Bell finds itself in a unique position of purchasing power that will likely never occur again. In this light, serious policy discussion took place during FY 2015 budget preparations concerning a spending plan supported by limited application of reserves. Guided by a desire to achieve a balance between re-investment in our City and the maintenance of a high-level of set-aside reserves, consensus was established to engage a three- to five-year period of “managed structural deficits.”

So it is that the FY 2015 Adopted Budget possesses a structural deficit (that is: an imbalance between income and disbursement) of \$1,481,029. The imbalance is attributable to permanent addition of \$633,803 in personnel costs owing to the expansion of staffing by 8 full-time positions and the permanent addition of \$147,000 in operating costs. At the same time, FY 2015 will see the application of \$708,400 in one-time expenditures for technology acquisition, capital improvements, and critical consultant assistance. (These one-time costs will be removed from the Budget in FY 2016).

Although we operate in relative financial freedom, the flip side to our expenditure plan is the commitment we have made to aggressive pursuit of economic development. The Rizzo administration ignored this obligation; their creativity was applied to schemes designed to enhance their pay and benefits.

Our economic development efforts, some of which are underway at this writing, seek to close the gap on the managed structural deficit within five years.

This a new departure for all involved. But continuation of a bare bones organization, one that offers little in the way of improved or enhanced services to our residents and visitors, and one that does not aggressively seek to grow the commercial tax base, is the lesser alternative. We cannot cut our way to future prosperity and service excellence. The only way out of the economic hole that the City is in is to grow our way out.

The General Fund Five-Year Financial Forecast (see Appendix) offers a model for our future. It demonstrates that deficit spending will be reduced from \$1,481,029 in FY 2015 to \$306,220 in FY 2019, a point at which the General Fund reserve position will be 158%.

We are beginning to come to terms with the new normal in the New Bell. Optimism is ours.

Respectfully submitted,



Doug Willmore
City Manager

Attachment 2: Detail Listing of “Items Above Status Quo” that Create Managed Structural Deficit

FY 2015 Budget

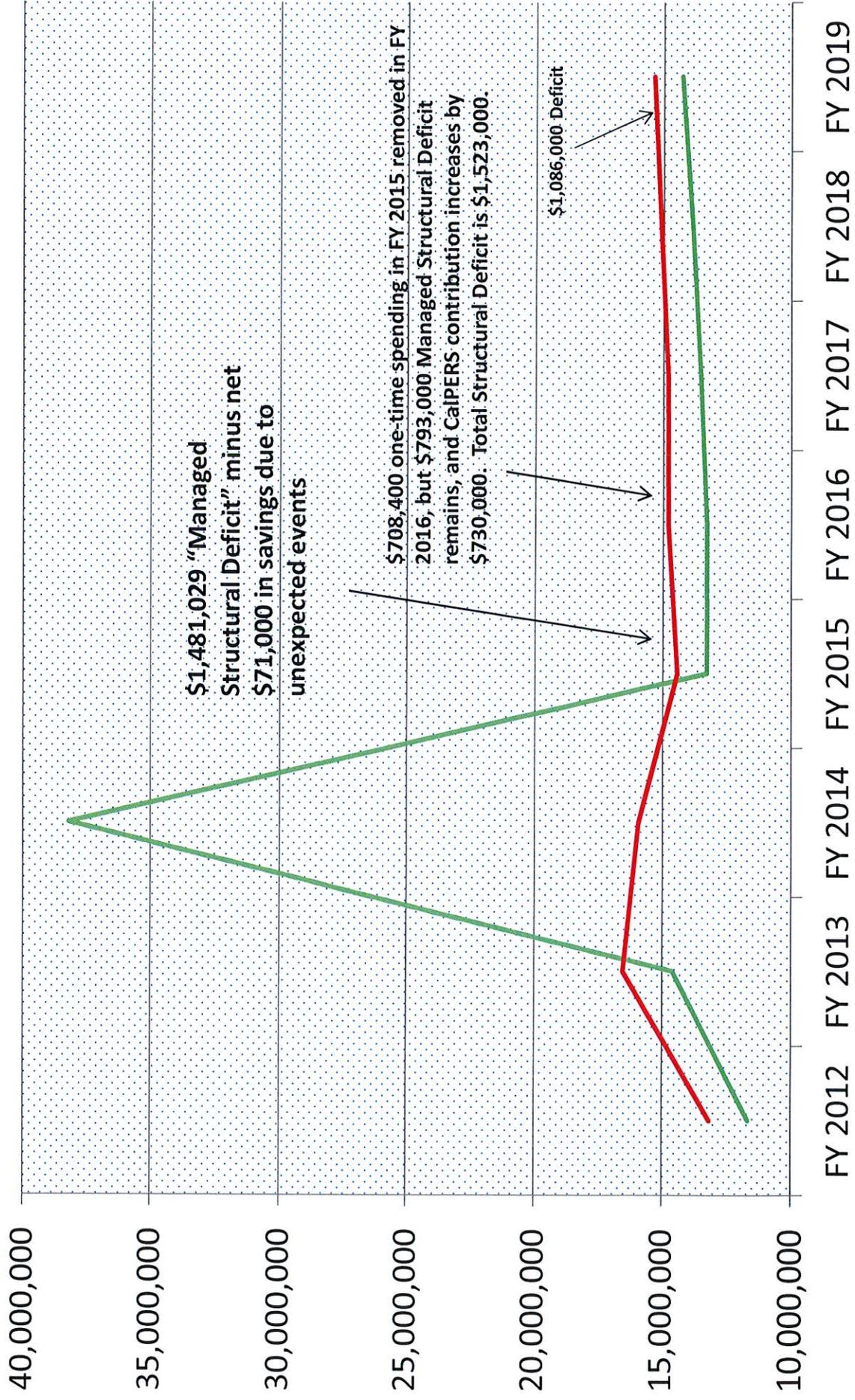
Exceptional Expenditure Items Above/Below Status Quo Budget

Description	Department	On-Going Costs		One-Time Costs	Total
		Personnel	Operations		
Technology	City Council	-	-	8,000	8,000
Professional Services	City Council	-	15,000	-	15,000
Add Administrative Specialist	City Council	77,831	-	-	77,831
Charter Reform Consultant	City Council	-	-	50,000	50,000
Citywide Employee Training	Human Resources	-	35,000	-	35,000
Automated Agenda Management Software	City Clerk	-	-	40,000	40,000
Microfiching Records Management	City Clerk	-	-	20,000	20,000
Infrastructure Inventory	Finance	-	-	25,000	25,000
Internal Audit Contract	Finance	-	25,000	-	25,000
Office Assistant to Full-Time	Finance	24,419	-	-	24,419
Master Schedule of Fees	Non-Departmental	-	-	19,000	19,000
Replace Telephone System	Non-Departmental	-	-	100,000	100,000
Debs Park Project	Community Services	-	-	250,000	250,000
Veterans Park Lighting Project	Community Services	-	-	175,000	175,000
Add Recreation Coordinator Position	Community Services	77,171	-	-	77,171
Add Recreation Coordinator Position	Community Services	(60,000)	-	-	(60,000)
Add Part-Time Staff	Community Services	51,029	-	-	51,029
Supplies: Youth Sports Program	Community Services	-	50,000	-	50,000
Supplies: Community Services Catalog	Community Services	-	22,000	-	22,000
Office Assistant to Full-Time	Community Services (City Commissions)	24,419	-	-	24,419
Add Police Sergeant	Police	152,427	-	-	152,427
Add Police Officer	Police	122,835	-	-	122,835
Add Motor Officer	Police	116,119	-	-	116,119
Add Motor Officer	Police	(75,000)	-	-	(75,000)
Add Code Enforcement Supervisor	Community Development	122,553	-	-	122,553
Code Enforcement Software/Hardware	Community Development	-	-	21,400	21,400
Total		633,803	147,000	708,400	1,489,203

Attachment 3: General Fund Financial Projection Assuming Economic Development

General Fund Projection

Revenue vs Expenditure Assuming Economic Development



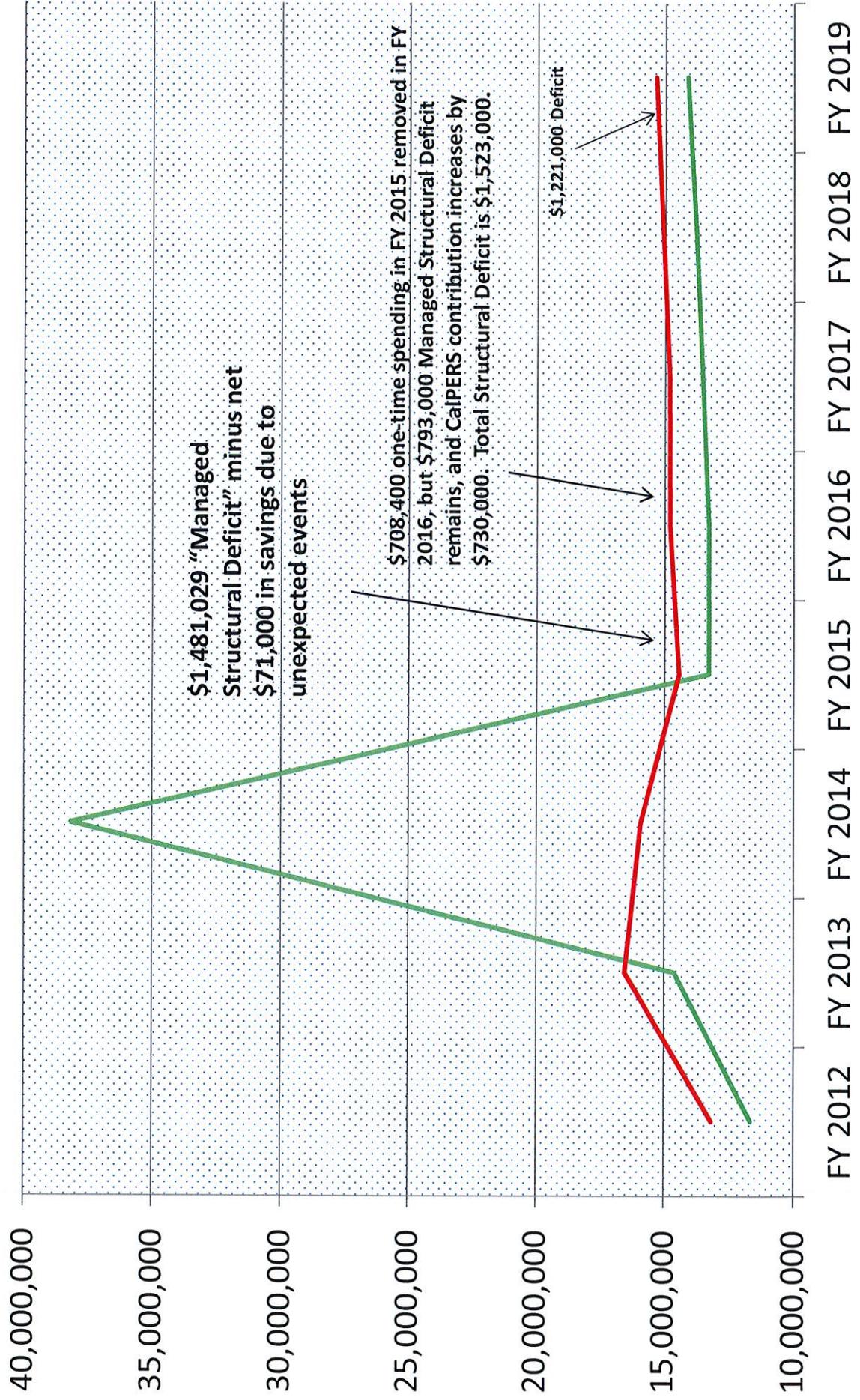
Projection Assumptions With Economic Development

	Revenue	Expenditure
FY 2016	2% Growth	(1) 2% Growth (2) \$708,400 One-Time Spending in FY 2015 Removed
FY 2017	2% Growth	2% Growth, and \$730,000 in additional CalPERS contributions added
FY 2018	2.5% Growth	2% Growth, and \$730,000 in additional CalPERS contributions added
FY 2019	3% Growth	2% Growth, and \$730,000 in additional CalPERS contributions added

Attachment 4: General Fund Financial Projection Assuming No Notable Economic Development

General Fund Projection

Revenue vs Expenditure Assuming No Economic Development



Projection Assumptions

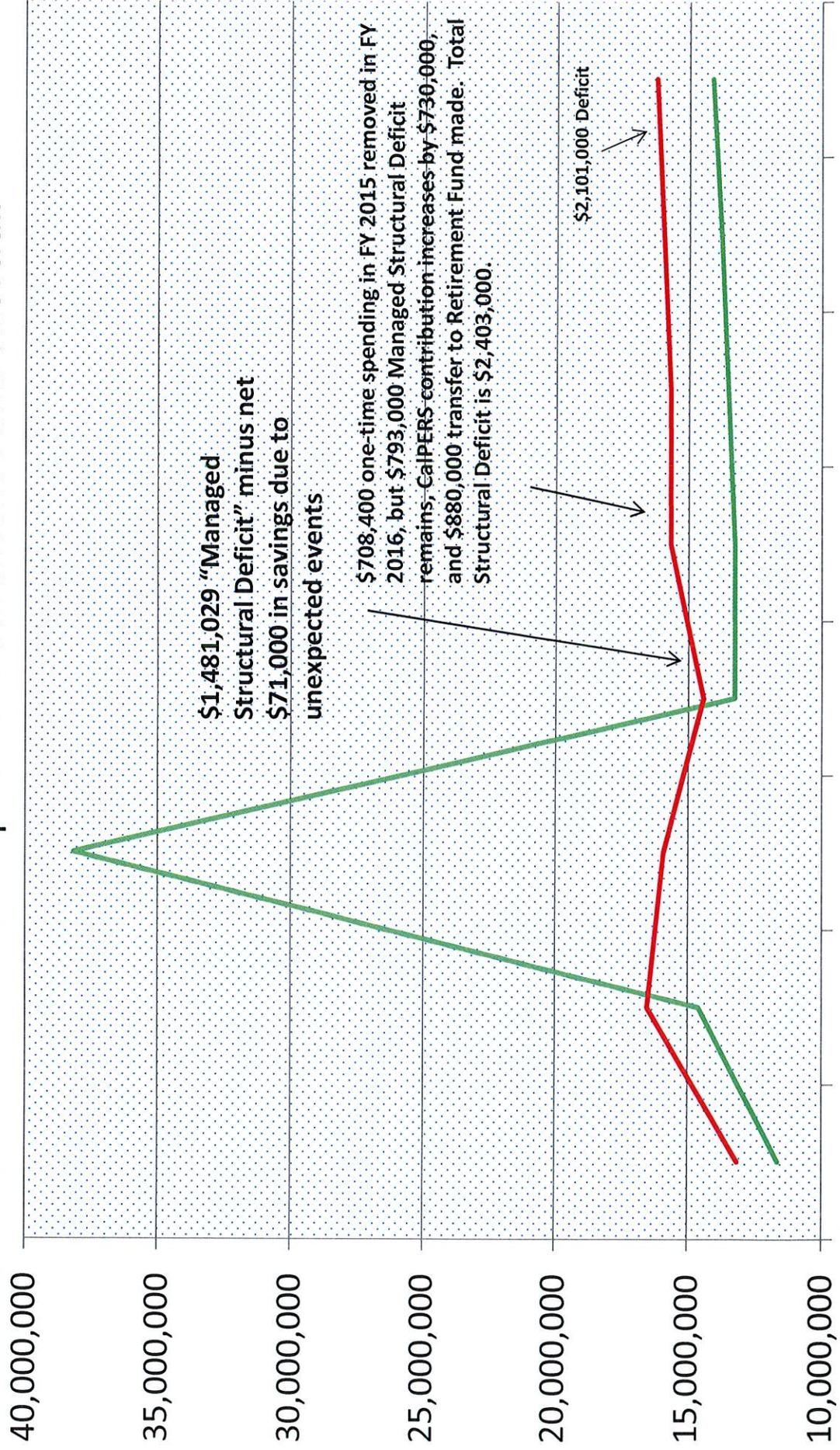
No Economic Development

	Revenue	Expenditure
FY 2016	2% Growth	(1) 2% Growth (2) \$708,400 One-Time Spending in FY 2015 Removed
FY 2017	2% Growth	2% Growth, and \$730,000 in additional CalPERS contributions added
FY 2018	2% Growth	2% Growth, and \$730,000 in additional CalPERS contributions added
FY 2019	2% Growth	2% Growth, and \$730,000 in additional CalPERS

Attachment 5: General Fund Financial
Projection Assuming No Notable Economic
Development and General Fund
Assumption of Retirement Fund Deficit

General Fund Projection

Revenue vs Expenditure Assuming No Economic Development and General Fund Assumption of Retirement Fund Shortfall



FY 2012 FY 2013 FY 2014 FY 2015 FY 2016 FY 2017 FY 2018 FY 2019

Projection Assumptions

No Economic Development and General Fund Assumes Retirement Fund Deficit

	Revenue	Expenditure
FY 2016	2% Growth	(1) 2% Growth (2) \$708,400 One-Time Spending in FY 2015 Removed (3) \$730,000 in additional CalPERS contributions added and, (4) \$880,000 in Retirement Fund deficit added
FY 2017	2% Growth	2% Growth, \$730,000 in additional CalPERS contributions added, and \$880,000 in Retirement Fund deficit added
FY 2018	2% Growth	2% Growth, \$730,000 in additional CalPERS contributions added, and \$880,000 in Retirement Fund deficit added
FY 2019	2% Growth	2% Growth, \$730,000 in additional CalPERS added, and \$880,000 in Retirement Fund deficit added

Attachment 6: FY 2014-15 Adopted General Fund Budget

FY 2014-15 Adopted General Fund Budget

Shown as Originally Adopted on June 25, 2014

General Fund Revenue

Revenue	12,730,531
Transfers In	<u>296,000</u>
Total Revenue	<u>13,026,531</u>

General Fund Expenditures

"Status Quo" Expenditures	11,743,487
Transfers Out	<u>1,274,870</u>
Total Expenditures	<u>13,018,357</u>

Subtotal "Status Quo" Budget Surplus/(Deficit) 8,174

Adopted Expenditures Above Status Quo Budget

City Council	150,831
Human Resources	35,000
City Clerk	60,000
Finance Department	74,419
Non-Department	119,000
Community Services Department	589,619
Police Department	316,381
Community Development Department	<u>143,953</u>
Total Expenditures Above Status Quo	<u>1,489,203</u>

Total Budget Surplus/(Deficit) (1,481,029)

Attachment 7: Projected FY 2014-15 General Fund Budget Outcomes

Projected FY 2014-15 General Fund Budget Outcome

Includes Unexpected Budget Events during FY 2014-15

General Fund Revenue

Revenue	12,730,531
Transfers In	<u>296,000</u>
Total Revenue	<u>13,026,531</u>

General Fund Expenditures

"Status Quo" Expenditures	11,743,487
Adopted Expenditures Above Status Quo	1,489,203
Transfers Out	<u>1,274,870</u>
Total Expenditures	<u>14,507,560</u>

Adopted General Fund Budget Contingency **(1,481,029)**

Projected Changes in General Fund Budget

Gas Tax Audit Findings	458,479
Administrative Specialist to Part-Time	(33,169)
Add Environmental Programs Manager	25,792
IRS Payment - 2007 GO Bonds	257,728
Dissolution of Bell/Cudahy JPA	192,980
Police EOP/COOP Disaster Plan	49,959
Four (4) HVAC Units	60,000
ICMA Restitution Payments	(244,814)
Citywide Personnel Savings (Vacancies)	(400,000)
MTA Transportation Audits Findings	-
City Council Technology	(8,000)
Charter Reform Consultant	(50,000)
Citywide HR Employee Training	(35,000)
Automated Agenda Management Software	(40,000)
Internal Audit Contract	(25,000)
Replace Telephone System	(100,000)
Debs Park Project	(250,000)
Veteran's Park Lighting Project	<u>(175,000)</u>
Total Projected Changes	<u>(316,045)</u>

Projected General Fund Excess/(Deficit) **(1,164,984)**