City of Culver City, California

City Council Agenda Item Report

Meeting Date: 01/22/08	Item Number: A-1
AGENDA ITEM: Presentation and Discussion of an Update of the Comprehensive Financial Master Plan.	
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Fiscal Impact: Yes [__] No [X]	General Fund: Yes [ ] No [X]
Public Hearing: [ ] Action Item: [ ]	Attachments: [X]
Public Notification: Master Notification List (01/16/08);	
Department Approval: Jeff Muir (01/08/08)	City Attorney Approval: Carol Schwab (by H. Baker) (01/08/08)
Fiscal Impact Review: Jeff Muir (01/08/08)	City Manager Approval: Jerry B. Fulwood (01/16/08)

RECOMMENDATION:

Staff recommends the City Council receive an update of the Comprehensive Financial Master Plan and discuss and direct staff as deemed appropriate.

BACKGROUND:

The Updated Comprehensive Financial Master Plan (Plan) being presented to the City Council tonight includes a five-year forecast of revenues and expenditures. The projections are based on updated assumptions and new events that have occurred since the Plan was previously presented. The Plan shows the trend of recurring expenditures out-pacing recurring revenues, as was presented in the last Plan.

The intent of the Plan is to provide a management tool that identifies short- and long-term financial issues. Based on the information provided in the plan, financing options and funding strategies can be developed for City Council's consideration and possible implementation. The Plan is intended to serve as a working document and will be updated at least annually or more frequently as needed.

This updated Plan utilizes a good deal of historical research originally done in preparation of the Plan presented to Council in 2007. This data was combined with updated financial information from the last two-year budget process and subsequent City Council approved appropriations mainly relating to capital improvement projects. The Plan was first introduced and presented to City Council on March 5, 2007. At that meeting, City Council directed staff to gather additional information on a number of the revenue enhancement options presented in the report. On June 18, 2007 staff presented the additional information to Council as requested. Due to the urgency of the issue, the City Council directed staff to pursue the option of modernizing the City's Utility User's Tax Ordinance to seek voters' support for maintaining and preserving the current City's UUT. The UUT issue is still a high-priority matter, but once resolved the focus must shift back to addressing the long-term structural deficit.

On December 3, 2007, the City Council was given a report addressing the current Fire Service level issue, which was originally presented as part of the Plan. The issue had re-surfaced as a result of outside factors that had come to fruition after the Council had considered revenue enhancing options on June 18, 2007. The City Council directed staff to seek consulting services to investigate forming a Special Tax District to potentially fund a third paramedic rescue unit. An RFP was released and responses were received on December 27, 2007 and are currently in the process of being reviewed. Staff will continue to keep the City Council informed of the progress of this item.

Land Use Planning and Density
A new concept being introduced with this update of the Plan is Land Use Planning and Density issues and how they may affect the City in the future, both from a development and financial standpoint. The areas and projects in which information has been analyzed are the Washington/National site, the Fox Hills area, commercial mixed use corridors, the proposed Entrada development, and Jefferson Blvd development. These areas/projects have been identified by the Community Development Department as underdeveloped areas that have significant land area with potential for development or large projects.

The Washington/National site is the location of the new Expo light-rail project, which is anticipated to open in 2010. Because of the unique circumstances inherent in this site as a station on the regional light-rail system, this area has been considered for transit oriented development. For the purposes of this update, some of the financial information from other recent documents prepared as part of the evaluation of this site has been used to demonstrate the potential financial impact of a development project of this scope.

The Fox Hills area has significant land area and several locations that are considered underdeveloped or underutilized and could potentially be redeveloped using the mixed-use development concept or redeveloped as new office-park development. There are a number of projects, including the construction of the Symantec office building and the remodel of the Westfield Mall, which may be catalysts for further redevelopment in the Fox Hills area. The Community Development Department provided information on potential build out scenarios in that area to demonstrate the potential for redevelopment. Based on that information, staff worked with Keyser Marston Associates to estimate the potential financial impact of that build out scenario.

There are also a number of underdeveloped and underutilized properties along the commercial mixed use corridors in the City that would benefit from redevelopment activities. Estimates were provided as to the amount of commercial/retail space and dwelling units that could be constructed, assuming a 5% build out. The low level of build out is attributed to the reduced level of investment in mixed use development that may occur as a result of the reduced densities proposed in the draft mixed use ordinance.

Lastly, there are a few larger commercial development projects that are currently being proposed and are in the beginning planning stages, including the Entrada building and Jefferson Blvd development. These projects have also been included in the Land Use Planning and Density projection.

It is important to note that a mid-year report will be coming to City Council in early February, which will include actual financial data through December 31, 2007. At that time, this report will also be included to reflect the updated 2007-08 adjusted budgeted amount plus any mid-year adjustments being recommended by staff.

DISCUSSION:

The updated Plan includes the adopted and approved appropriations for fiscal 2007-08 and 2008-09, adjusted budgetary information based on City Council approved actions for fiscal 2007-08, and detailed revenue and expenditure projections through fiscal 2012-13. This information was derived from historical trends for both revenues, which has been adjusted based on current economic trends, and expenditures, including MOU negotiated items such as COLAs for the City's six bargaining groups and known safety salary initiative increases. The City has been able to balance revenues with expenditures over the last few years due to higher than anticipated on-going revenues and some one-time revenues (including land sale proceeds). Based on current information, it is anticipated that the City will continue to show operational balance (or modest surpluses) through fiscal 2008-09.

The City has been diligent in ensuring that one-time revenues are only used to fund one-time expenditures. It is clear, though, that the underlying fundamental issue of recurring expenditures outpacing recurring revenues has not been solved in the long term projections. As shown in the Plan, beginning in FY 2009/2010, the projected deficit will continue to grow unless direct and decisive action is taken.

Preliminary figures do show the General Fund Reserve as having a healthy balance. However, it is important to realize that a good portion of the reserve is a result of one-time revenue receipts (such as proceeds from land sales), which have accumulated over time. This has enabled additional funding to be approved by City Council for significant capital improvement (one-time) projects, such as Fire Station #3 ($1,527,000), and the Public Safety Records Management System ($1,622,098), which otherwise might not have been funded. To help offset the additional funds appropriated for the additional construction costs of the new Fire Station #3, there is also one-time revenue of $1,000,000 in estimated land sale proceeds included in fiscal 2008-09 from the sale of land where the existing Fire Station #3 is located. Beginning in fiscal 2009-10, though, projections show the General Fund Reserve dropping below the 30% threshold established by City Council Policy.

Moving Forward

The City has been making positive progress through discussion and/or approved action on certain options and recommendations previously approved by City Council. These include:

- Placing a measure on the April 2008 ballot that asks Culver City voters to approve modernizing the City's Utility User's Tax Ordinance. The UUT currently generates revenue of approximately $13.5 million a year.
- Approval for a study of a Parcel Tax to help fund additional paramedics in order to maintain service levels. With the recent bankruptcy filing of Brotman Medical Center and increased medical calls for service received by the City's Fire Department, the need for additional paramedics has become an even higher priority for the City.
- Continue to implement Best Management Practices throughout City Departments.
- Finalized and implemented a full, in-depth Fees and Charges study in April 2007, which will generate approximately $715,000 of on-going General Fund revenue beginning in fiscal 2007-08.
- Created a team of staff to evaluate the feasibility of various options for healthcare cost containment including researching various healthcare providers (in process).
- Strategic Workforce Planning.

Current Economic Issues Facing the City

The current slowdown in the housing market is a concern for the City, although not as big as that for the State or other surrounding cities. Property Tax revenues for the City are approximately 3.8% of General Fund revenues. Revenue projections for

Property Tax and Real Property Transfer Tax over the next few years have taken into consideration the slowdown in the market and been kept at a very conservative growth rate. Culver City is also not experiencing the same significant declines in housing prices and sales as has been seen in other areas of Los Angeles County and surrounding counties (e.g. Riverside and San Bernardino counties).

The current Writers' Guild strike, which began on November 5, 2007, could potentially have a significant negative impact on Culver City, as well as the surrounding Los Angeles area economy. Culver City has two major studios, Sony Studios and The Culver Studios, both of which are major economic entities within the city. During the last strike in 1988, which lasted 22 weeks, it was estimated to cost the LA area economy approximately $500 million. If a strike were to last that long today, estimates put the loss to the area economy at approximately $1 billion.

The most visible sign of the strike for Culver City has been the less crowded restaurants/shops in downtown during the daytime hours. However, the most significant impact will be a slowdown of business-to-business activity as production of new movie and television episodes ceases. Business to business sales activity is a significant source of sales tax and business tax revenues for the City. Since major production has only recently started to slow, it is unknown at this time what specific impact the strike has had on the City's revenues. Staff will closely monitor this impact as the strike continues and as data becomes available.

Several weeks ago the State revealed an estimated $14 billion shortfall in its budget next year. In the State of the State address by the Governor, this was confirmed and the Governor revealed his plans to close the gap primarily through cuts to State programs in his proposed FY 2008/09 budget. There was immediate reaction from state legislative leaders against the proposed budget. Although the Governor's plans do not include diverting local government revenues or transportation monies, these items may be placed on the table as further budget discussions ensue between the parties. Proposition 1A does provide more protections to local governments than in the past, but the Governor has already declared a 'fiscal emergency' and with a two-thirds vote of the legislature the State can divert local funds twice in any ten year period with certain other conditions. Proposition 1A protections do not extend to redevelopment agencies. Staff will continue to monitor this situation closely and keep City Council informed of any new information.

<u>Future (Long-term) Issues Facing the City</u>

The City Council recently approved a contract with Aon Consulting to perform an actuarial study associated with the implementation of Governmental Accounting Standards Board (GASB) Statement No. 45. This study will assist the City with determining the long-term costs of the City's other post-employment benefits

(OPEB) such as medical insurance for retirees. The actuarial analysis should be completed in February and will be brought to City Council at that time for discussion of financing strategies.

While many cites throughout the nation have not yet implemented a strategy to address the issue of long-term heath care and pension liabilities, the City Council has taken the initial steps. Beginning in fiscal 2007-08, the City Council approved setting-aside $100,000 each fiscal year to start funding this long-term cost. However, it should be noted that this amount will be only a fraction of the amount to fully fund the expected actuary-recommended contribution. A little over one year ago an actuary performed a summary analysis of Culver City data and estimated an annual required contribution figure of $9.8 million. This figure would be inclusive of the current costs paid by the City for retiree medical of approximately $3.4 million, and would therefore result in an additional requirement of $6+ million per year. While GASB 45 does not require funding of the liability (it requires only including the liability on the City's financial statements), any difference between the actuarially computed contribution and the actual contribution will begin to reflect annually on the City's government-wide financial statements as a liability, which could affect its future credit rating and cost of borrowing.

Sufficient funding for deferred maintenance is an ongoing struggle for many cities, including Culver City. In fiscal 2007-08 and 2008-09, the City Council was able to appropriate funding from the General Fund Fund Balance for one-time capital improvement projects, but a long-term plan to fund outstanding deferred maintenance is still in process. A study was conducted earlier this year that identified how much the City will need to set-aside each year to enable it to meet future facility maintenance needs. It identified funding needs for routine costs, immediate repair costs, and annual reserve cost estimates. By utilizing data from this study, funds were appropriated in the fiscal 2007-08 Capital Improvement Budget in the I & A Fund for some immediate repairs using available fund balance from the General Fund reserve. This study is currently being finalized, and will be used as a planning tool for the upcoming budget review.

General Fund Scenarios in Updated Plan

There are four financial scenarios included in the Plan for the General Fund as follows:

Scenario A Summary

The first scenario takes a business as usual approach, with relatively conservative revenue and expenditure projections. Based on the current economic conditions, we must take this conservative approach. It includes information from the two-year budget process for 2007-08 and 2008-09, and other City Council actions approved since July 1, 2007. As can be seen on the worksheet, beginning in fiscal 2009-10, the General Fund Reserve percentage drops below 30% and is projected to continue on a downward trend from there. This scenario represents that even without factoring in costs for the OPEB contribution and deferred maintenance items there will be a deficit between on-going revenues and expenditures.

Scenario B Summary

The second scenario includes all information contained in Scenario A and adds one additional issue: the potential loss of a portion (Telecommunication) of the Utility User's Tax (UUT) revenues. Although the loss will not be immediate, the risk to the City of a permanent loss of this revenue will exist. The outcome of current legal challenges in other jurisdictions with similar language in their ordinances may set a legal precedent which would impact Culver City's revenue stream from this source. If the legal challenges from other jurisdictions (1) were applicable to Culver City and (2) were negative in their impact, it would result in a reduction of approximately $2.7 million in ongoing revenue.

On top of this, non-cellular (land-line) revenues from Telephone UUT have consistently been dropping (an average decrease of more than $100,000 per year since 2003-04) as more and more people have been moving towards wireless phones and similar media for communications. The loss of the wireless portion of the UUT ($2.7 million), coupled with the continuing decrease in land-line UUT equates to a potential loss of close to $3 million per year in UUT revenues.

Since it is not known when, or if, the City would potentially lose this revenue, a decision was made to show its loss in fiscal 2010-11. As can be seen from the worksheet, this would decrease the General Fund Reserve percentage by over 3% with further impacts in future fiscal years.

Scenario C Summary

The third scenario includes all information from Scenario A and adds additional information based on potential land use policies (i.e. height and density requirements) and economic development. Finance Department staff worked with Community Development Department staff and consultants from Keyser Marston Associates to identify areas with the greatest potential for development and to estimate the financial impacts of proposed developments. The financial impact included in the Plan represents the net difference between estimated increased revenues generated from the project area and estimated increased service costs from the resulting development. Please note that the estimates provided in Scenario C are simply meant to demonstrate the impact of development on the City's finances. These estimates are based on potential development as envisioned by staff based on current possibilities. The estimates do not necessarily represent actual proposed or planned projects.

Based on figures from the analysis, if the City and Redevelopment Agency aggressively pursued all of the potential developments identified, or substantially similar developments, the City could ultimately see approximately $2 million per year. While this does not fix the projected deficit problem, it does provide an avenue outside of reducing services or increasing taxes to improve on-going revenues. Substantial development is currently taking place outside the City along almost all the borders, and while Culver City doesn't see the positive economic impact from this we feel the impacts. Progressive cities need to attract quality development in order to see continued revenue growth. These projects would also likely generate fairly significant one-time revenues such as development and impact fees.

Scenario D Summary

The fourth scenario includes all information from Scenario A and adds an additional $2 million per year in costs to fund the required OPEB contribution beginning in fiscal 2008-09, $4 million in 2009-10 and $6 million in 2010-11. As stated earlier, the actuarial analysis will not be completed until February, so this figure is based on the previous **estimate** of a $9.8 million annual required contribution. This is a very real scenario, in that there is no question the City will be required to make a decision on how it will address this matter. Whether the choice is made to fully fund the required contribution or to 'ease' into the required amount over several years, this will have to become part of the City's upcoming operating budgets to fund retiree medical. Future negotiations to reduce retiree medical contributions by the City could result in lowering this number, but it will be calculated based on the current agreements.

Upcoming Decisions

The basic purpose of the updated Comprehensive Financial Plan is to show that the City's financial situation has been complicated by the various current economic factors locally, statewide and nationally. The City has made great strides in addressing a number of critical issues that will assist in the long-term financial viability of the City, but the structural deficit still exists and deferred maintenance and liability obligations have to be addressed. Quality development will assist the City in 'bridging the gap', but will not solve the problem.

The City Council has been presented with options previously that have sought to address the issue of closing the gap between recurring revenues and recurring expenditures. In basic terms, the solution to a structural deficit is to reduce costs, enhance revenues, or some combination of the two. The majority of the City's expenditure budget is for personnel costs that provide direct or indirect services for Culver City residents, businesses and visitors. Both the City Council and the Culver City community take pride in the high level of service provided by City employees. Given this pride and expectation, as well as reductions that have already been required in the past, further staff and service reductions are not desirable. One area that may need to be revisited is the budget enhancements approved in the two-year budget that includes fiscal year 2008-09. Based on refined projections from the mid-year budget review (which will be completed by early February), pulling back or delaying some of these enhancements could become necessary.

The other alternative is enhancing revenues. Aggressively pursuing continued ‘smart’ development opportunities is one avenue towards this, but further resources will be required. Within the upcoming months, the City Council will need to renew discussions on what direction staff should pursue in addressing the structural deficit. There are difficult decisions ahead, but Culver City is up to the challenge.

FISCAL ANALYSIS:

There is no additional fiscal impact associated with this staff report. If the City Council directs staff to bring back information related to options for revenue enhancements or cost reduction recommendations, there may be an associated fiscal impact at that time.

ATTACHMENTS:

1. Updated Comprehensive Financial Plan

MOTION:

That the City Council:

1. Receive and file the Updated Comprehensive Financial Master Plan; and

2. Direct staff as deemed appropriate.