



City of South San Francisco

P.O. Box 711
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South San Francisco, CA

Legislation Text

File#: 23-363

Agenda Date: 6/28/2023

Version: 1

Item #:

Report regarding the City of South San Francisco Operating Budget for Fiscal Year 2023-24 and approving the GANN Appropriation Limit. (*Karen Chang, Director of Finance*)

RECOMMENDATION

It is recommended that the City Council adopt a resolution that approves the City's Fiscal Year (FY) 2023-24 Operating Budget and the Gann Appropriations Limit.

BACKGROUND/DISCUSSION

In 2017, the City made the strategic shift away from a one-year operating budget cycle to a biennial operating budget cycle. FY 2019-21 was the last biennial operating budget, which was adopted by Council on June 26, 2019. Due to the extraordinary economic downturn stemming from the COVID-19 global pandemic, significant adjustments were made to the FY 2019-20, FY 2020-21, FY 2021-22 and FY 2022-23 budgets to react to the dynamically changing conditions. As a result, for FY 2023-24, staff is pursuing an annual budget, as opposed to a biennial budget for the upcoming fiscal year. The goal is to resume the two-year budget cycle once the economy shows signs of stabilization and longer-term recovery, as biennial budgeting generally requires a longer commitment of policy direction and funding levels.

The General Fund is the City's largest and core operational fund, where the bulk of the essential services delivered by departments such as Economic and Community Development, Fire, Library, Parks and Recreation, Police, Public Works and City Administration are budgeted.

The information included herein was presented at two public meetings:

- May 31, 2023 – Budget Standing Committee
- June 12, 2023 – Special City Council.

CITYWIDE OVERVIEW – EXECUTIVE SUMMARY

FY 2022-23 Budget update

While the current fiscal year has not yet closed, it is the expectation that this fiscal year will end with a slight deficit. When the Council adopted the FY 2022-23 budget, the expectation was that the General Fund would have a slight surplus of \$55,000.

The City of South San Francisco has shown resiliency during the COVID-19 pandemic. During the mid-year budget, the City has seen strong rebounds in some revenue categories particularly Transient Occupancy Tax (TOT), property tax, sales tax, and permit fees.

However, as revenues increase, there is often a commensurate increase in expenditure. During the FY 2022-23, the City has increased expenditure significantly especially in personnel costs as a result of labor negotiations, general operating costs to keep up with inflation and also in anticipation of opening of the Library, Parks and Recreation building.

During the mid-year budget cycle, staff anticipated closing the year with a surplus of about \$6 million. However, as we approach the year end, there was an unexpected loss due to a property sale at the PUC site for developing affordable housing, a childcare center, and public space amenities. Therefore, staff currently projected the City will close the year at a slight deficit of about \$17,000.

Should actual revenues prove to be stronger than expected or expenditures come in less than budget, this would translate into a smaller deficit, or a surplus which would boost the available General Fund unassigned fund balance.

FY 2022-23 Y/E Projections	
Revenues	\$ 132,954,510
Add: PO/CIP budget c/o	10,883,022
Less: Expenditures	<\$ 143,854,523>
Net Surplus/<Deficit>	\$ <16,991>

<i>Table 1: Projected City Reserves Summary as of 6-30-2023</i>	
General Reserves (20% set aside)	\$25,100,000
Pension Stabilization Reserves	\$5,600,000
Infrastructure Reserves	\$7,440,800
Total Reserve Levels	\$38,140,800
Available Unassigned GF Fund Balance ⁽¹⁾	6,060,000
Reserves & Surplus Fund Balance	\$44,200,800

⁽¹⁾ Est. balance after the \$6M set aside for ERP replacement during mid-year

A summary of City's General Fund revenue and expenditure as well as Reserves for FY 2019-2024 can be found in Attachment 1 of this report.

FY 2023-24 Proposed Budget

There are still looming economic uncertainties. Given that the Federal Reserve continues to raise interest rates to try to combat inflation, revenue projections remain uncertain. In particular, the projections are sensitive to changes in personal income, inflation, interest rates, and the extent to which workers return to offices. Nevertheless, the projections presented reflect the most up to date economic and financial data available.

The FY 2023-24 Operating Budget has been developed assuming many of the revenue categories would experience moderate to flat growth. On the expenditure side, the proposed payroll budget incorporates all

the positions added (19.61 FTE) during the FY 2022-23 mid-year review as well as all the budgeted impact as a result of FY 2022-23 labor negotiations.

The FY 2023-24 proposed budget includes approximately \$807,000 in personnel requests, \$3,298,900 in supplies and services requests, and \$45,000 for capital outlays. More detailed information about these requests can be found in Attachment 2 to this report.

After we incorporated all the revenue projections and expenditure requests for FY 2023-24, the expenditure has exceeded the revenue by approximately \$8 million.

To balance the FY 2023-24 budget, staff recommend an across-the-board attrition of \$3 million (approximately 2.8%) from each department's budget to help bridge the gap. Finance created an attrition saving line in each department's personnel budget to memorialize the amount needed. The attrition recommendation was based on historical information on vacancy savings. Of course, this approach will require discipline from each department to delay filling their vacant positions and continuing to be vigilant in their spending during FY 2023-24. Staff also recommends using the unspent revenue loss balance of \$4.987 million from American Rescue Plan Act's (ARPA) to cover the remaining shortfall.

In March 2021, the federal government passed the ARPA emergency stimulus package which included \$350 billion in aid for states, local and Tribal governments to support their responses to and recovery from the COVID-19 public health emergency. South San Francisco was awarded \$12.28 million – the two tranches of \$6.14 million received in June of 2021 and 2022. Ten million of the ARPA funds can be used to replace lost public sector revenue. The remaining portion of the ARPA funds were used or plan to be used to support critical social and community programs such as the Guaranteed Income Program, Youth Summer Internship Program, Food Voucher Program, Restaurant Grants, and City Broadband Expansion.

For FY 2023-24 proposed budget, the City projects operating revenues of \$140,162,500 (include the use of one-time ARPA fund), and \$140,153,300 in operating expenditures (includes the \$3 million attrition, but excludes any potential carry over purchase orders), giving a small net surplus of \$9,200 which would be added to the General Fund's unassigned fund balance.

FY2023-24 Proposed Budget	
Revenues	\$ 135,175,500
Add: ARPA Funds	4,987,000
Total Revenue & Resources	140,162,500
Expenditures	<\$ 140,153,300>
Net Surplus	\$ 9,200

1. FY 23-24 GENERAL FUND REVENUE PROJECTIONS

The revenue forecast (not including Measure W) for FY 2023-24 is shown below, set against FY 2022-23 budget and FY 2021-22 actuals:

Revenue Types	FY2021-22	FY2022-23		FY2023-24	
	Actuals	Adopted Budget	Adjusted Budget*	Proposed Budget	%age Change from FY2022-23
Taxes	90,813,357	80,849,791	88,049,791	93,191,500	15.2%
Property Tax	49,779,285	43,804,769	45,804,769	47,980,000	9.5%
Sales Tax	22,361,011	20,991,018	22,391,018	23,351,500	11.2%
Transient Occupancy Tax	12,135,638	11,160,752	14,160,752	14,190,000	27.1%
Other Tax	6,537,422	4,893,252	5,693,252	6,950,000	42.0%
Franchise Fees	4,863,076	4,600,000	4,600,000	4,600,000	0.0%
Licenses and Permits	14,062,472	15,500,000	19,425,400	16,962,894	9.4%
Fines & Forfeitures	700,960	710,824	710,824	700,000	-1.5%
Intergovernmental	3,196,346	2,844,618	4,231,054	3,139,827	10.3%
Charges for Services	9,747,605	8,799,097	8,265,097	9,709,257	10.3%
Planning	905,739	879,000	250,792	510,000	-41.9%
Fire	3,019,090	2,626,314	2,626,314	2,728,000	0.0%
Parks & Recreation	2,917,504	2,796,248	2,846,248	3,235,240	15.6%
Police	1,115,947	979,649	979,649	1,246,670	27.2%
City Admin & Other	1,789,325	1,517,886	1,562,094	1,989,347	31.0%
Money & Property	3,060,851	5,453,469	5,453,469	3,940,000	-27.7%
Other Revenues	514,996	259,383	263,903	337,826	30.2%
Transfers In	4,763,729	3,245,000	6,151,400	2,593,804	133.6%
ARPA				4,987,373	
TOTAL REVENUES	\$131,723,392	\$122,262,182	\$137,150,938	\$ 140,162,481	14.60%

*Adjusted budget includes approx. \$14.8 million revenue adjustments made throughout the fiscal year.

Property Tax remains the City's largest revenue component and is projected to be \$48.0 million in FY 2023-24. Property tax revenues have increased at an annual rate of 6% over the last five years from an economic boom along with robust developments. However, interest rate hikes throughout 2023 and a looming recession are expected to dampen the growth of the property valuation in this upcoming fiscal year. Staff has factored in such a slowdown in revenue growth for the FY 2023-24 budget. This revenue stream is also overshadowed by the risk of increasing Property Tax In-Lieu of Vehicle License Fees (VLF) shortfalls from declining numbers of non-basic aid schools. Following the previous practice, the County of San Mateo, on behalf of itself and all the municipalities within the County, will file a claim with the State of California in August 2023 for the \$70 million VLF shortfall, which the State will consider as a part of its 2024-25 budget for appropriation. It is currently unclear if any appropriations for the 2021-22 VLF county-wide shortfall of \$32.9 million (of which the City's share is \$1.3 million) will be included in the State's proposed 2023-24 budget. To be conservative, staff has realigned the projection for VLF for FY 2023-24 based on the latest information available.

Sales Tax revenues are expected to increase by 11.2% to \$23.3 million for FY 2023-24. Staff expects a decline in sales tax revenue in FY 2023-24. However, the decline is likely to be offset by elevated costs of goods and services due to inflation. Overall, staff believes sales tax revenue will remain relatively flat.

Transient Occupancy Tax (TOT) was hit the hardest during FY 2020-21 with collection dropping to an all-time low of \$6.7 million (40% of the pre-pandemic amount.) Since then, this revenue stream has demonstrated a strong recovery in the subsequent two years due to easing of traveling restriction and widespread vaccinations, reaching \$14.1 million for FY 2022-23 (projected). Staff anticipates a moderate increase in TOT next fiscal year due to resumed business travel.

Licenses and Permit revenues had been relatively stable prior to FY 2022-23 as construction and economic development throughout the City was strong. Rising interest rates triggered by untamed inflation starting in mid-2022, along with recent bank collapses, casts a shadow on the economy and presents a challenging environment for developers in FY 2023-24. Staff is cautiously optimistic about the development growth within city boundaries and projects a modest increase in revenues related to construction and economic development.

Charges for Services revenues experienced a significant downturn during the pandemic. In FY 2022-23, charges for services from fire, police and planning departments have mostly recovered to pre-pandemic levels while revenues from Parks & Recreation such as childcare programs, aquatic programs and facility rentals have yet to be fully restored. For FY 2023-24, we expect these Park and Recreation programs to continue to recover. Staff projects revenue from recreational activities to exceed the FY 2022-23 adjusted budget but remain below pre-pandemic levels. Total charges for services are projected to be \$9.7 million, which is \$910k or 10.3% higher than the FY 2022-23 adopted budget.

Use Money & Property is expected to be lower due to the sales of some properties (PUC site, 109 Longford Drive and 201 Baden Avenue) that occurred in FY 2022-23. Due to a higher interest rate environment, staff is not budgeting any property sales for FY 2023-24. However, interest earnings from investment are expected to be higher than FY 2022-23.

2. PROPOSED FY 2023-24 GENERAL FUND EXPENDITURES

The following table shows the proposed FY 2023-24 General Fund expenditure budgets by department.

Expenditure Type	FY2021-22	FY2022-23		FY2023-24	
	Actuals	Adopted Budget	Adjusted Budget	2024 Proposed	Percentage Change from FY2022-23 Adopted
City Council	252,677	258,749	260,649	269,486	4.1%
City Clerk	887,680	1,143,342	1,154,449	1,265,011	10.6%
City Treasurer	39,853	167,292	167,904	133,428	-20.2%
City Attorney	1,138,457	940,290	940,290	1,108,825	17.9%
City Manager	3,911,696	4,527,997	5,324,597	4,931,075	8.9%
Finance	3,148,918	3,892,875	4,405,085	3,992,281	2.6%
Non-Departmental	14,746,076	2,044,367	2,852,698	1,894,367	-7.3%
Human Resources	2,065,928	2,518,004	2,684,109	2,884,524	14.6%
Econ. & Comm. Development	11,006,918	8,907,770	15,609,630	8,499,933	-4.6%
Fire	32,560,465	31,313,293	33,424,717	32,761,869	4.6%
Police	33,281,487	32,957,662	34,450,023	36,838,240	11.8%
Public Works	6,294,565	7,120,654	8,603,705	11,954,045	67.9%
Library	6,495,266	6,706,110	7,273,745	8,044,806	20.0%
Parks & Recreation	18,092,525	19,608,365	22,869,652	24,675,441	25.8%
CIP	831,343	100,000	3,833,270	900,000	800.0%
TOTAL GENERAL FUND EXPENDITURES	134,753,855	122,206,770	143,854,522	140,153,329	14.7%
Information Technology (ISF)	3,404,272	4,311,906	5,241,804	4,443,433	3.1%

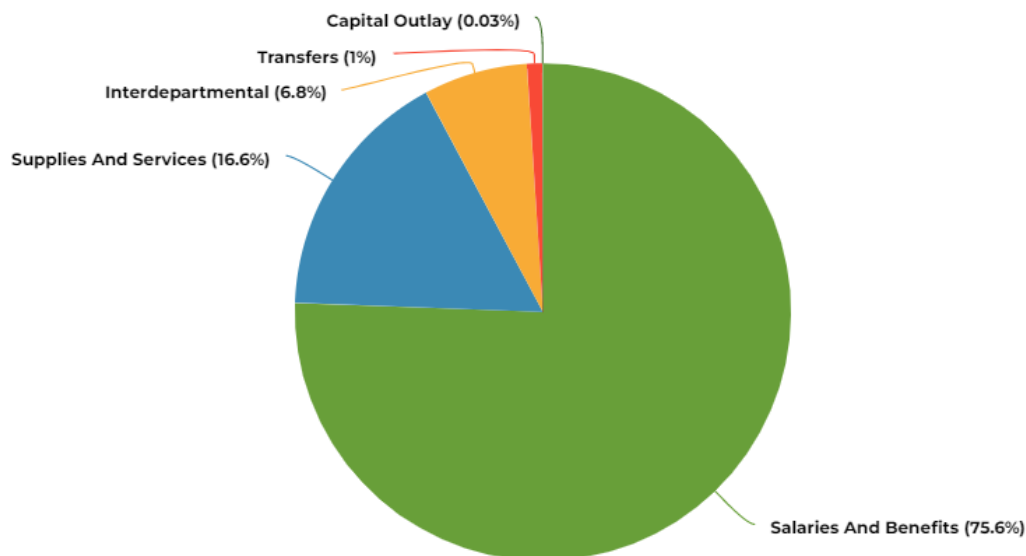
Attachment 2 of this report provides a summary of new budget requests for FY 2023-24.

In response to an inquiry from the Budget Sub-Committee, the following is a brief explanation of Economic & Community Development department's (ECD) FY 2022-23 adjusted budget. The FY 2023-24 ECD baseline budget is around \$8.5 million. The baseline is derived after removing the one-time expenditures from the previous year. The adjusted budget for FY 2022-23 was \$15,609,600 primarily due to rollover purchase orders pertaining to the Economic Advance Center (\$2.2M), Lindenville Specific Plan (\$1.2M) and General Plan (\$1.4M). There were also budget adjustments for the Façade and Tenant Improvement program and other labor costs adjustments.

The following provides additional information for each of the major expenditure categories.

Expenditures	FY 2022 Actual	FY 2023 Y/E	FY 2024 Proposed Budget
PAYROLL	\$ 95,445,374	\$ 100,377,916	\$ 105,942,584
SUPPLIES & SERVICES	21,887,485	30,756,837	23,261,011
CAPITAL OUTLAY	-	825,400	45,000
INTERDEPARTMENTAL CHARGES	7,387,247	7,361,099	9,504,735
TRANSFERS*	1,533,749	4,533,270	1,400,000
TOTAL	\$ 126,253,855	\$ 143,854,523	\$ 140,153,329
* Exclude the one-time transfer to Infrastructure Reserve			

The pie chart below shows the split of the General Fund expenditure budget between the different expense categories. Payroll accounts for three quarters of the proposed expenditure budget



Payroll:

- Total payroll costs, which includes salaries, wages, overtime, healthcare, pension, and other benefits, are projected to be \$106 million. The projected cost reflects negotiated increases in employee compensation, increases in cost of healthcare, increase in pension contributions.
- The payroll costs take into consideration the City's required annual Unfunded Accrued Liability (UAL) payment to CALPERS. The UAL payment is the City's obligation and is based on an amortization schedule provided by CALPERS. It is calculated based upon how much money is at CALPERS versus how much is required to pay pension benefits for all current and future retirees. The total UAL obligation for FY 2023-24 is \$17.4 million. This is a 1.6% decrease from

the FY2022-23 \$17.7 million UAL payment. The decrease was due to favorable investment returns at CalPERS during FY 2020-21, the cost will be much higher in FY 2024-25 when CalPERS investment loss of 7.5% in FY 2021-22 will be accounted for.

- There are 11.35 FTE requests for FY 2023-24 totaling \$0.8 million as can be seen in the table below. The proposed budget presented in Attachment 2 is inclusive of the position requests, re-classifications, and costing.

NEW PAYROLL REQUESTS			
Departments	FTE	Salaries and Benefits (General Fund)	Salaries and Benefits (Sewer Enterprise Fund)
Library	2.00	180,494.00	-
P&R	8.14	484,313.00	-
Police	(0.50)	(27,627.00)	-
PW	1.50	99,985.00	165,250.00
HR	-	40,000.00	-
Fire	0.21	30,650.00	-
Grand Total	11.35	807,815.00	165,250.00

- The department summaries in the budget book in **Attachment 3** have all positions listed for each department.

Supplies and Services:

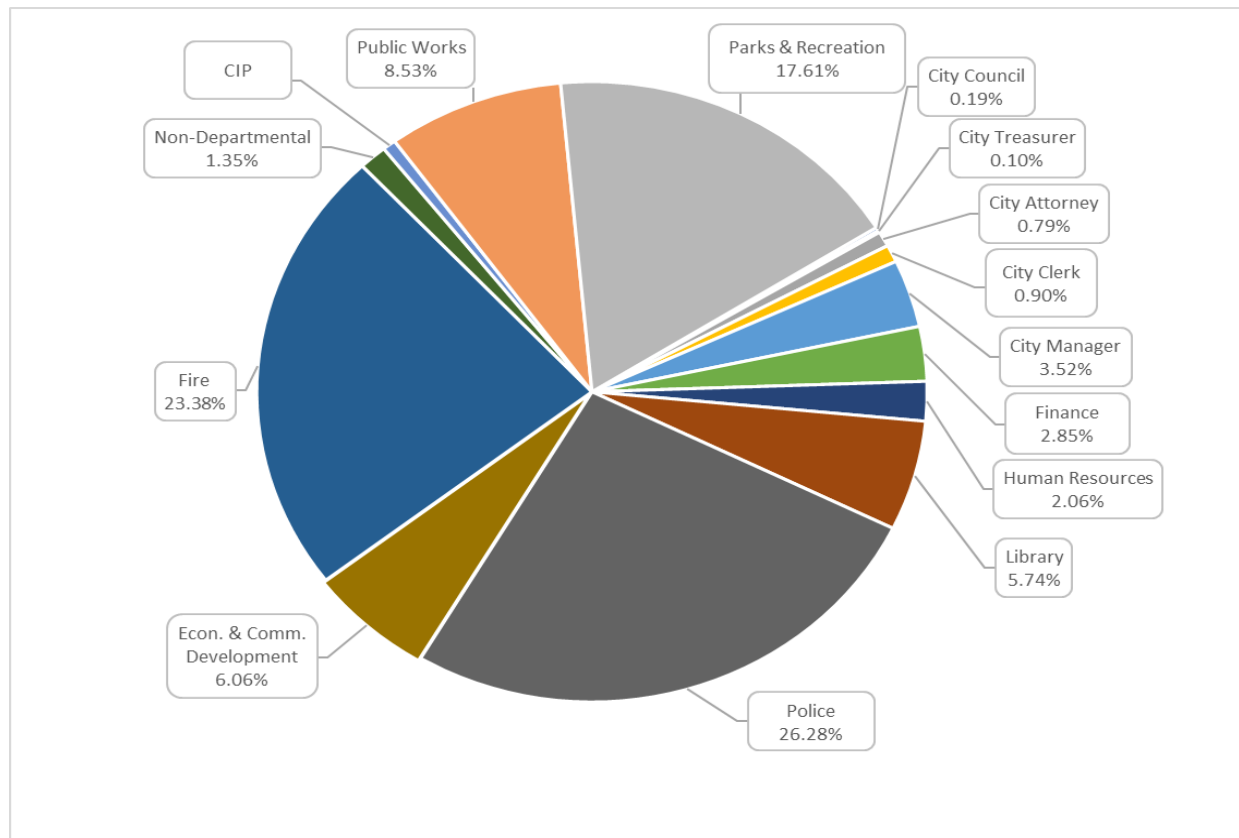
- The proposed budget includes all decision packages (new requests) submitted by departments that have been reviewed by the City Manager and are subject to Council approval. Total requests amount to \$3,343,910. These are shown in **Attachment 2**.

Interdepartmental Charges:

- Interdepartmental Charges are expenses that are accounted for in the General Fund (and other funds as necessary) and summarily transferred out to fund “internal services” and total \$9,504,735 in the proposed General Fund budget. The largest internal service fund is for the Information Technology (IT) department. In effect, the cost to fund IT services, as an example, is calculated and then “charged” to various funds of which the General Fund is the largest component.

The overall General Fund expenditure breakdown by department is shown visually below:

FY2023-24 Proposed General Fund Expenditures by Department*



3. PROPOSED FY 2023-24 GENERAL FUND BUDGET SUMMARY

The following is a summary of the proposed FY 2023-24 General Fund Budget.

FY2023-24 Proposed Budget	
Revenues	\$ 140,162,500
Expenditures	\$ 140,153,300
Net Surplus	\$ 9,200

**Does not include PO carryforwards.*

4. OTHER FUNDS

There are 61 funds that the City Finance Department manages outside of the General Fund. The notable fund budgets for FY 2023-24 are represented in **Attachment 3**. Many of the final budgets for these funds are contingent upon the adoption of the Capital Improvement Program (CIP) by the City Council. The numbers may change based upon Council's action related to the FY2023-24 CIP program.

The table below shows expenditures (including transfers) for all budgeted City funds summarized by fund type. City-wide appropriation requests for FY2023-24 total \$295,196,209.

Fund	FY2021-22 Actuals	FY2022-23 Adopted Budget	FY2022-23 Adjusted Budget	FY2023-24 Proposed Budget	FY2022-23 Adopted vs. FY2023-24 Proposed (%)
General Fund	\$134,753,855	\$122,206,770	\$143,911,381	\$140,153,329	14.7%
Measure W	\$11,481,647	\$13,143,072	\$24,031,115	\$8,762,385	-33.3%
Special Revenue Funds	\$26,650,774	\$36,566,097	\$92,647,831	\$23,689,812	-35.2%
Capital Improvement Funds	\$96,850,110	\$120,597,051	\$225,675,973	\$20,538,588	-83.0%
Debt Service Fund	\$8,287,833	\$8,289,450	\$8,289,450	\$11,525,338	39.0%
Proprietary Funds	\$28,783,384	\$38,840,406	\$76,879,067	\$59,448,973	53.1%
Internal Service Funds	\$28,234,916	\$33,547,775	\$36,939,745	\$31,077,784	-7.4%
TOTAL	\$335,042,519	\$373,190,622	\$608,374,562	\$295,196,209	-20.9%

5. RESERVES

The projected City's financial reserve funds as of June 30, 2024, are expected to be approximately \$40.2 million. The number is subject to change based on any additional requests during the year. A breakdown is shown below:

Financial Reserves FY 2023-24	
General Reserve	\$25,100,000
Infrastructure Reserve	3,390,800
CalPERS Stabilization Reserve	5,600,000
Unappropriated GF Balance	6,060,000
Total	\$ 40,150,800

The **General Reserve**, which represents 20 percent of the City's annual revenue budget excluding transfers in (General Fund), follows the best practices guidelines from the Government Finance Officers' Association (GFOA).

The **Infrastructure Reserve** is largely comprised of General Fund surpluses that were set aside over previous years in anticipation of the City's future infrastructure projects. The value shown is the unencumbered monies available that have not yet been designated toward a project. It should be noted

that within the proposed FY 2023-24 Capital Improvement Program, \$4.05million of direct capital project funding is requested from the Infrastructure Reserves. If approved, this would leave approximately \$3.4 million in the Infrastructure Reserves.

The *CalPERS Stabilization Reserve* was established through two separate Council actions in FY 2015-16 and FY 2017-18 totaling \$5.546 million. Finance took advantage of the higher interest environment and set up a separate investment account with the City's investment manager, Chandler, in December 2022 that yields a higher rate of return. As of April 2023, the balance has grown to \$5.6 million.

The *Unappropriated General Fund Balance* is the available fund balance remaining in the General Fund (as shown in the table in the summary section of this report) that has not been assigned for any particular purpose. This balance will change depending on the extent to which expenditures may exceed revenues (deficit) in FY 2022-23. It is important to note that the unassigned fund balance also acts as a buffer allowing for the natural ebb and flow within the General Fund that occurs during the year as a result of the mismatch between when revenues are received, and expenditures are incurred.

Although placed in different categories, the City Council by majority vote will be allowed to use the above reserve funds as necessary.

FISCAL IMPACT

For Fiscal Year 2023-24, the City's General Fund is projected to have operating revenues of \$135,175,108 with additional ARPA funding of \$4,987,373 for a combined total of \$140,162,500, and \$140,153,300 in expenditures net of any carryover purchase orders, resulting in a small net operating surplus of \$9,200.

RELATIONSHIP TO STRATEGIC PLAN

The budget is the City's spending plan that supports Priority Area 3, Financial Stability.

CONCLUSION

South San Francisco has weathered well during the pandemic and has since seen a steady recovery of revenue during the FY 2022-23. However, there are several trends that could adversely affect the City's fiscal health in subsequent years that will require prudent decision-making to maintain the current service levels. In terms of revenues, the level of revenue growth seen in previous years may slow down, as increases were largely fueled by the unprecedented level of federal stimulus funding. The City is expected to spend the remaining one-time American Rescue Plan Act (ARPA) funding of \$4.987 million in the current fiscal year. The City's expenditures are projected to increase at a slightly faster rate than the revenue growth in coming years. Particularly, increasing pension expenses and labor costs are putting pressure on the City's future budget.

In this upcoming budget, Staff recommends cautiously filling the vacant positions and approving the department requests to maintain the current services level to the community. Staff recommends the City Council use infrastructure reserves to fund critical infrastructure projects necessary throughout the City, and to maintain level spending to provide critical services to the community. Staff also recommends using

the one-time residual balance of American Rescue Plan Acts fund as the additional resource to bridge the shortfall between operating revenues and expenditures proposed in FY 2023-24. Staff intends to revisit the FY 2023-24 budget with City Council when the audit for the current fiscal year is available (likely February 2024) and adjust the budget as necessary based upon tax receipts and other economic data indicators available at that time.