

City Manager's Office

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May 30, 2014

Honorable Mayor and Members of the City Council:

Introduction

Presented for your consideration is the proposed Annual Budget for Fiscal Year 2014/2015, a period that covers July 1 through June 30. The Budget is the primary policy document adopted by the Council that establishes the service levels and capital projects to be provided to the community by its city government. It establishes the financial and human resources devoted to accomplishing community goals and objectives as reflected by the City Council. It provides a logical structure to organize its various programs, projects and other expenses. It provides a sound system for control of its revenues and expenses. Finally, it is a document that is widely available to the public and others interested in the operations of the city government.

The City began experiencing significant general fund budget problems in the latter half of last decade. Since then, the City has eliminated 110 positions, which represents almost 24% of the current workforce. Its effects may not always be evident to the public, but it is fair to say the City's service levels have been affected and the city's ability to fund capital expenses has also been diminished.

Even with the extreme attention applied to City finances the past several years, it is apparent that the improving economy is not going to solve the City's seemingly perpetual budget problem. This came into sharp focus with a December 17, 2013 staff report revealing that if the City continued its existing service levels with no significant new source of revenue, its general fund reserves would be completely extinguished by the end of the FY 14/15 budget year. The term used to describe this persistent deficit is "structural budget deficit," a situation that assumes that service levels and their cost structure remain fixed and there are no new significant revenue sources available. At that time, the structural budget deficit was estimated at about \$5 million. Allowing the reserve to be extinguished is unthinkable as it would negatively impact the City's credit rating; it would provide no margin for dealing with contingencies and emergencies; and it would result in more major reductions in FY15/16 and beyond.

On the topic of the budget, over the past five months there have been many public meetings and more than two dozen meetings with the community and business leaders. The general consensus is that the City needs to have a long-term financial strategy which would include, but not be limited to, continuing to pursue cost-control measures; investigating alternative

revenue sources; and supporting economic development activities which are compatible with community values.

After hearing from community and business leaders, City Council placed a ½ cent sales tax ordinance Measure O on the June ballot. If passed, Measure O would generate an estimated \$2.7 million in FY 14-15 and \$3.6 million annually, thereafter. Its status is not known at the time the Annual Budget is released, but it may be known shortly thereafter if the vote is decisive one way or another. Obviously this will have a material impact upon the forthcoming budget deliberations.

If Measure O fails to pass, the impact of not having the new sales tax revenue available will require significant expense reductions beyond those already identified within the proposed Budget will need to be considered immediately. At Council direction, staff is prepared to present budget reduction options.

This proposed Budget follows the direction given by the Council as discussed above, with emphasis on assuring the long-term fiscal stability of the city government. The following is a list of actions included in or related to the proposed FY14/15 Budget:

- **General fund reductions of \$1.2 million have been built into the proposed Budget.** In April, staff returned to Council with updated financial projections and reduction lists totaling \$5 million to address the structural imbalance. Of this amount \$1.2 million in cuts were recommended by staff, endorsed by the Council and included in the FY 14-15 Proposed Budget.
- **Additional ½ cent sales tax measure on June 2014 ballot.** Technically the proposed Budget has been constructed without including the \$2.7 million in revenue that would be available if Measure O is approved by the voters. The expenses have not been adjusted to include the reductions that would otherwise need to be recommended to avoid the reduction of nearly \$4 million of the general fund's reserve. Council previously gave general direction about the nature of the cuts that would be considered, but there was no direction to implement them commensurate with the approval of the Budget. In the event Measure O is defeated, staff will seek immediate guidance regarding the scope of the cuts that would be implemented in the first quarter of the fiscal year. The estimated target for the cuts is projected in the \$3-4 million range.
- **Growing revenues with economic development activities which are compatible with community values.** The revenue focus group and other community members indicated that it was important to pursue compatible economic development activities to provide a stable source of income for the City. Recently, the Council approved issuing a Request for Expressions of Interest in developing innovation center proposals. While achieving the economic goals and objectives is critical to achieve sustainability of City finances, this has a long-term impact that would roll out over time. The reality is that this will have little impact over the next several budget years. This is why the City is exploring alternative revenue sources in the meantime.

- **Update User Fees and Policies.** Funding is in the Budget to study user fees and identify the fees that could be adopted to achieve full cost recovery. It will be up to Council to approve any revised fees. Along with this effort will be a review of fee policies to determine whether any subsidies exist and in what cases subsidies may be in order. Given the fact that user fees haven't been thoroughly reviewed in many years it is likely that there are some significant subsidies being given, perhaps in areas where the Council would want to strive for full cost recovery, such as development processing fees. This is an important element for improving the City's revenue base and needs to be given high priority.
- **Proposed Legislative Changes.** Recently AB 2372 was introduced which, if adopted, will raise an estimated \$73 million statewide. It proposes to close a loophole in Proposition 13 which some corporations have used to avoid a reassessment when property changes hands. The fate of this is uncertain and the revenue impact in Davis is unknown, but if enacted it could be a positive revenue development.
- **OpenGov Launch.** Providing information about the City's finances and budget is important to enhancing transparency about City budgeting and finances. The release of OpenGov software, which is now available, will allow the community to see past expenditures as well as those that are planned. Also, this document contains more expenditure detail than in the past.
- **Street/Bike Lane Infrastructure Budget.** Council decided last fiscal year to include a \$500,000 allocation to fund a maintenance program for streets and bike lanes. In the proposed Budget, the allocation has been increased by \$2.5 million to \$3 million in General Fund support in the upcoming year. When combined with other funding, the City will be addressing a total \$4.7 million in street and bike lane improvements in the proposed Budget.
- **Water Conservation in Parks and Greenbelt Facilities.** Water costs have been budgeted at \$1.5 million with offsetting estimated revenues of \$600,000. To offset increasing water costs the sum of \$500,000 has been budgeted to continue the ongoing water conservation efforts to reduce consumption and to be more water efficient.
- **Measure P and the New Surface Water Treatment Facility.** Measure P proposes repealing the new water rate structure that was adopted to fund the joint water project with the City of Woodland. The proposed Budget assumes that the current rates stay in place, though recent Council action changed that direction and rates may be recalculated whether or not Measure P passes. This will affect water rate revenue by roughly \$1 million which will need to be made up in the recalculated rates. Staff is working with the Utility Rate Advisory Commission to consider revised rates. This may affect the Water Division's ability to secure financing whether it's low-interest loans or selling revenue bonds.
- **Wastewater Treatment Facility.** Construction will begin on this is design-build project. The project is funded by rates and will cost approximately \$101 million.

- **Funding for Publically-Owned Utility (POU).** At its May 13, 2014 meeting, the Council directed staff to remove the \$600,000 loan to the General Fund which had been set aside for the purpose of continuing work in pursuit of a city-owned electrical utility. This direction is reflected in the proposed Budget.
- **Technology Improvements.** As the City continues to make budget adjustments, automation is an important tool to maintain services levels and to stretch staff resources. Work will continue on replacing/updating the City's antiquated accounting system with \$100,000 that has been carried over for this purpose. The smart-phone and web-based Citizen Response Manager (CRM), a website redesign, evaluating e-bills/e-notification for utilities, and \$82,000 for the exploration new/updated functionality in the enterprise software are also included in the proposed Budget.
- **Medical Insurance Savings.** After the April update, the CalPERS Board of Administration voted to move Yolo County from the Bay Area health insurance rates and place it with Sacramento area. This change will be effective January 1, 2015 and save \$52,500 in the general fund for six months. In subsequent years, the annual savings across all funds will be approximately \$150,000.
- **Annual Full OPEB funding.** This marks the second full year of funding the Other Post-Employment Benefit (OPEB). This amount may change. Every two years, the OPEB amount has to be recalculated by an actuary and the City is currently awaiting the results which could change the contribution amount. If it does, staff will return to Council with recommendations.
- **Restoring negative fund balances.** Examining the City fund balances revealed that the Employee Benefits Fund and the Fleet Replacement Fund had shortfalls which needed to be addressed. The Employee Benefits Fund had a \$2.9 million deficit and Fleet replacement Fund had a \$1 Million shortfall. The FY 2014-15 Proposed Budget contains resources to begin repaying both funds over a seven-year period in the amount of \$305,000 and \$110,000 per year, respectively.
- **Updated Overhead Expense Plan.** The City's cost-allocation plan, which is a mechanism for recovery of General Fund overhead expenses, such as City Administration, City Attorney, Personnel Services, and Accounting, was evaluated and revised by an outside consultant. The overall analysis resulted in a reduction in billable expenses and general fund revenue of \$295,000. In part this is due to reduced staffing over the years which means there are less costs to recover.
- **Removal of Salary and Operations Savings factor.** In the past, the City has removed estimated savings from the Budget which may occur over the course of the year. It is approximately \$400,000 for vacancies and \$700,000 for operations. The problem is that over the past seven years with additional position cuts and expenditure reductions the savings became harder to realize. In FY 14-15, this savings was removed.

- **Updated Employee costs.** Employee services and benefits were calculated according to the terms of the Memoranda of Understanding (MOU). There was a 1% increase cost-of-living adjustment with offsets of a decrease in the amount of cash out in the cafeteria plan with employees picking up the final half-percent (0.5%) toward their retirement contributions, therefore paying their full share (8 % Miscellaneous and 9 % Public Safety).

In summation, the proposed FY 2014/2015 general fund Budget is increasing from the prior year, even with reductions and labor savings. More than half of it comes from the addition of another \$2.5 million to the infrastructure budget.

On an all-funds basis, the Budget reflects an overall decrease in appropriations of \$88 million dollars, of which \$76 million can be attributed to the Water and Sewer Capital projects (Surface Water Project, Water Tank & Wells Fargo Loan Repayments and Wastewater Treatment Plant).

FY 2014-15 Budget-Balancing Plan

In December 2013 and April 2014, the City reported that it had a \$5 million general fund structural imbalance and, absent any change, the reserves would be extinguished as noted previously. This is despite \$11.1 million overall in reductions over the past several years consisting of \$5.3 million in general fund labor concessions and \$5.8 million in position reductions. The proposed Budget does not contain any staff layoffs though a net of 5 positions are being eliminated.

With a goal of reducing the \$5 million structural imbalance when building the new Budget, departments were asked to develop General Fund reduction scenarios. This meant 12 percent reduction scenarios for all departments; and, up to 25 percent if Police and Fire were held harmless. These scenarios were presented to Council in December 2013 and in April 2014. The Council directed staff to include \$1.2 million of these reductions into the proposed Budget. The Council made no decisions on further cuts pending the outcome of Measure O.

If Measure O does not pass, the City will need to make additional expense reductions. The Council will need to decide the magnitude and services to be affected by the reductions. Pursuant to previous Council direction, such reductions would be effective October 1, 2014.

FY 2014/2015 Proposed Budget Department Highlights All Funds

City Council

- No proposed changes.

City Attorney

- Legal services budgeted at FY 2013/14 levels.

City Manager's Office

- **General Management**
 - One-time professional services contracts for the economic feasibility study to evaluate the City's options for electrical services were removed (\$471,000)
 - Reduction in Yolo County Office of Emergency Services (OES) funding (\$7,000). The City commitment has been reduced due to new County funding structure. New funding amount is \$33,000 which resulted in the savings.
 - Eliminate most of the funding for special projects/studies (\$80,000).
- **Cable and Media Services**
 - Various options for taping the City Council, Planning Commission and other meetings held in the Community Chambers will be explored in the upcoming year.
- **CDBG and Housing**
 - The sum of \$800,000 was removed in Special Projects funding and \$370,000 was added for funding of various organizations with Community Block Grant Funds. This is an annual process and will not be decided until later this summer.
- **City Clerk**
 - The staffing within the City Clerk's Office is proposed to be reorganized during the upcoming year.

Administrative Services

- **Administration**
 - No substantive changes.
- **Human Resources and Risk Management**
 - Reduce Professional Services by \$40,000. Most employee Memorandum of Understanding (MOU) contracts are effective through December 2015 which means this amount can be reduced.
 - General Office expenses were reduced by \$1,000 and Communications by \$1,600.
 - Recruitment Advertising was reduced in recognition of fewer positions result in less money being spent for recruitments. Also, as positions become vacant, they are being evaluated for possible elimination or reclassification prior to starting a recruitment (\$2,000).
- **Aquatics**
 - The Aquatics division was established in FY 14-15 to consolidate the Pool Maintenance which transferred from Public Works and activity programming from Community Services.
 - Civic Lap and dive pools are planned for re-plastering.
- **Child Care**
 - The Child Care Division obtains resources from federal and state grants and the amount of funding per year is dependent upon these funding sources.
 - In FY 2014-15, the City will be evaluating whether to continue to provide this service. State and Federal regulations prescribe the reimbursement the City receives and a nonprofit may be better able to more cost-effectively provide the services.

- Community Services and Parks
 - The Parks Division was transferred to Community Services from Public Works during FY 2013-14.
 - Continued efforts in Capital Improvements for water conservation measures in Parks and Greenbelts has been continued in the 2014-15 Budget (\$500,000).
 - Costs for city water and sewer have been included (\$1,532,420 and \$14,312, respectively).
 - A reduction in overtime by 50 percent (\$7,000). Over the last two years this line-item has decreased due, in part, to staffing reductions.
 - Reduce Parks Maintenance "Other Resources" expenditures (\$20,000). With reduced number of full-time and Temporary Part-Time employees, there will be less need for materials and supplies including fuel, pesticides, irrigation supplies, and safety and equipment stock.
 - Contract additional custodial services (\$55,746). The City has been switching to contract custodial services through attrition and a vacant custodial position will be eliminated.
 - Reduced other professional services in Community Services (\$10,000). This reduction will not affect the level of service.
- Information Systems
 - The City's accounting software is over 25 years old and the reporting needs of the City have changed. The process of determining whether to upgrade or replace the enterprise software began last year and will continue.
 - Funds have also been budgeted for "Click2Gov" software enhancement which will allow credit card processing in various programs such as utilities, Business License and Building Permits (\$82,000).
 - Reduce postage funding (\$31,721). Provides a minimal amount for postage and Departments will need to absorb additional postage costs.
 - Eliminate a portion of temporary part-time funding (\$1,096). Used to hire specialized IT help for application support.
 - Reduction in radio maintenance contract (\$14,783). Remove some Public Works and Public Safety Equipment from maintenance contract on the Radio Agreement.
- Budget and Fiscal Services
 - E-notification and e-billing will be pursued this year.
 - Contract Services - Business Licenses Eliminate contract service funding for Temporary Part Time assistance during Business License peak collections (January/February). Volunteers will be used instead (\$3,500).
 - Eliminate 50 percent of funding for Sales Tax contractual auditing by Muni Services (\$25,000). Muni Services has been auditing the City's Sales Tax base for approximately six years. Fewer errors in sales tax reporting are being found and which results in a lower annual cost for the service.
 - Reduction in Contract Services Reduce \$20,000 of the funding for the City's master fee schedule analysis. Part of the funding will be carried forward from the current fiscal year project.
 - Shift funding for Accountant 10 percent to Utilities (\$10,089). The new water and wastewater Capital Improvement Projects (CIPS) have presented a significant increase in workload for Finance. This shift has been discussed with the enterprises and it recognizes the additional workload for special

requirements related to Bond Disclosures, Bond Administration, Capitalization tracking, for new enterprise projects.

- Shift funding for Financial Supervisor 10 percent to Utilities (\$11,350). Shift in recognition of additional workload consumed for the purposes of monthly Utility Billing.
- Shift 2% of funding for Senior Accounting Assistant to Utilities (\$17,951). Shift in recognition of additional workload consumed for the purposes of monthly Utility Billing.
- Shift 20% of funding for Budget Manager in recognition of staff support for new major Enterprise Capital Projects (\$55,561). This has been discussed with the Enterprises and is related to the Alternative Water Supply, Wastewater Treatment Plant, Water Conservation & Roadway Rehabilitation projects.

Fire

- The overall department budget decreased about \$279,153 as a result of the implementation of the Management shared Services agreement with University of California Davis (\$64,702), strike team overtime (\$124,000) and the elimination of one-time costs.
- Operating expenditures have been increased to include \$180,000 for vehicle replacement charges, attributed to the replacement fund shortfall and building maintenance costs are increasing \$60,000 as a function of the re-distribution of the new cost allocation plan.

Police

- Code Enforcement (non-building) was transferred to the Police Department in FY 2013-14 from the Department of Community Services and Sustainability.
- Funds have been restored which were removed from the budget salary savings for unfilled Police Officer positions and factored into the budget through a staggered hiring process throughout the year as candidates become available.
- As part of an operations study the following recommendations are implemented in FY 2014-15: a Crime Analyst position was reclassified to a Police Intelligence and Resources Analyst; Public Safety Dispatch Supervisor was reclassified to a Records and Communications manager; and Administrative Services Manager was changed to a Public Safety Financial Analyst.
- Eliminate Vacant Assistant Chief position (\$267,708). Both Department bureaus would report to one Assistant Chief which will result in reduced administrative oversight over the department.

Community Development and Sustainability

- In FY 2014-15, the non-building Code Enforcement function was transferred to the Police Department.
- Eliminate General Fund Support for Sustainability Programs (\$131,681). The General Fund support for sustainability efforts will be eliminated and, instead, the program would be paid for with Enterprise and grant funds. Cool Davis or other similar program could also supplement sustainability services, upon successful grant funding. Reduced resources in support of local renewable energy efforts such as SB43 will result if grant funding cannot be secured.

- Eliminate paid planning internship (\$16,000). This reduction eliminates paid internships within Community Development Department and volunteer interns will be utilized.
- Reduce travel, training, memberships and subscriptions (\$5,000). This shift would reduce funds available for training for Planning Division staff.
- The Cannery project is starting in FY 2014-15, as well as other development projects, and positions to support the development have been added. The two Building Inspector positions are paid for by the Building Services Fund. A portion of the cost is offset by the elimination of contract inspectors.

Public Works

- Administration
 - An update to the citywide cost-allocation model is included in the FY14-15 Budget. This model updated and reallocated the overhead costs in the City based on the most recent budget and use data. This update allocated increased overhead to the administrative division of \$161,000.
- Transportation
 - Eliminate 5,000 Temporary Part-Time hours. (\$33,761)
- Wastewater
 - Capital expenditures are planned for 1,975,000.
 - Land-lease cost for utility on city property (\$86,767).
- Storm Water
 - One-time expenditures from FY 13-14 for repair services and construction costs were removed from the 14-15 Budget. All other expenditures remained relatively flat.
 - Land-lease cost for utility on city property (\$29,344).
- Water
 - Eliminate Utilities Manager Position (General Fund portion \$3,809). The duties for this position will be assumed internally.
 - Added \$124,516 for a Conservation Coordinator position.
 - Utility costs for Gas & Electric are projected to increase by \$56,000.
 - Land-lease cost (\$465,826). The other portion of the lease cost is contained in Wastewater (\$86,767) and Drainage (\$29,344).
- Engineering Services
 - Street Smarts—Safe Routes to School program (\$101,300) funded with grants.
 - Reallocate funding splits for Support Services Division Programs (\$16,600).
 - Reduces funding for printing and binding (\$3,700). Limited printing of various city atlas' (roads, address, utilities, etc.) Shift product to electronic medium.
- Solid Waste
 - Increase cost with Davis Waste Removal (\$178,000)
- Fleet
 - Capital expenditures for fleet replacement is budgeted based on an annual fleet replacement schedule. This total amount for FY 14-15 is \$1,555,514.

- Facilities
 - Eliminate vacant Facilities Manager position (\$157,102). Eliminating this position will have an impact on completing facility replacement projects. Asset Manager will assume primary Facilities Management role, with Facilities Supervisor assisting with project completion tasks.
 - Shift 40 percent of funding for Senior Office Assistant to Facilities (\$12,226). Required because of the restructuring of the Asset Management Division and the transfer of Parks & Open Space out of Public Works.
 - Shift 25 percent of funding for Parks/General Services Superintendent to Facilities (\$17,038). Same as above.
 - Facilities improvements have been budgeted at \$299,000.
 - Eliminate the facility replacement fund contribution for the City Fuel Facility with the intention to close and decommission the fuel facility in 2032 which is at the end of its useful life (\$19,303).

Summary

The past few years have been challenging for many cities, including Davis. Much has been done in Davis to control costs and look to the future. A ballot measure affecting finances is before the voters in June. If Measure O passes in June, it will help to stabilize the City's finances. If Measure O is unsuccessful, the City is prepared to make cuts. Due to the magnitude of the reductions, some service levels will be affected and this will take time to work through. The outcome of Measure P for water rates is another unknown but the City is prepared to recalculate rates. Another aspect of this is how the passage of Measure P may affect the water revenue and what consequences it will have on the City's ability to bond. It may impact the Water Division's ability to secure financing whether it is low-interest loans or selling revenue bonds.

Paring back the size of the organization and applying the skills learned in dealing with the existing economic reality continues to present challenges. These challenges include California Public Employees Retirement System (CalPERS) and Other-Post Employee Benefit (OPEB) cost increases, but it is encouraging that long-standing problems with the system are being acknowledged and addressed at least in part. Health care increases have outpaced inflation and it's helpful that CalPERS offered subscribers in Yolo County some relief. More savings may be possible down the road with the new health-care insurance exchange. The Council has been dealing with these cost drivers for several years and there is guarded optimism about the future.

The preparation of the Annual Budget, though routine, is an enormous task. Budget building is a team effort and this year has been particularly challenging. Special thanks to the Budget staff (Kelly Fletcher, Bob Blyth and Kathy McIntire), Dominique Sayer, Mary Morris and Pam Day who gave up weekends and evenings to produce the Budget. Department staff such as Jim Ivler and Stacy Winton worked after hours to quickly turn around sections of the Budget. Thanks to the department heads and executive management team (Herb Niederberger, Landy Black, Nate Trauernicht, Rob White, Mike Webb, Bob Clarke, Melissa Chaney, Kelly Stachowicz, Darren Pytel, Zoe Mirabile, Jason Best); the City Attorney, Harriet Steiner; the Finance staff and others too numerous to mention. The teamwork and effort is much appreciated.

This is a unique budget year insofar as the work behind it was peaking commensurate with the departure of the City Manager in late April. As a practical matter there hasn't been adequate opportunity for the Interim City Manager to have a significant role in the strategic decisions which shaped the proposed Budget. A report will be prepared by the Interim City Manager after this is published to update the Council on the implications of the Measure O election if known and provide additional recommendations about the proposed Budget.

Respectfully Submitted,



Yvonne Quiring
Assistant City Manager/Administrative Services Director

Approved by:



Gene Rogers
Interim City Manager

