Agenda Item #4.1
For Council Meeting of: October 21, 2025

CITY OF SANTA ROSA
CITY COUNCIL

TO: MAYOR AND CITY COUNCIL
FROM: SCOTT WAGNER, INTERIM CHIEF FINANCIAL OFFICER, FINANCE DEPARTMENT
SUBJECT: GENERAL FUND FINANCIAL UPDATE

AGENDA ACTION: STUDY SESSION

RECOMMENDATION

It is recommended by the Finance Department that the Council hold a Study Session to provide an update on the financial condition of the General Fund and present preliminary results for fiscal year (FY) 2024-25. This item is to provide an opportunity for City Council to receive information, ask questions and give general guidance for FY 2026-27 budget development. This item is for information only and no action is to be taken.

EXECUTIVE SUMMARY

This study session provides a preliminary overview of the FY 2024-25 General Fund results, comparing adopted budget figures to actual outcomes and an overview of budget actions over the past year. Staff will also present an updated Long Range Financial Forecast and analyze the status and projected utilization of reserves.

GOAL

This item relates to Council Goal #1 - Achieve and Maintain Budgeting Excellence and Fiscal Stability and presents an analysis of the preliminary FY 2024–25 results relative to the adopted budget and summarizes prior budget actions.

BACKGROUND/PRIOR COUNCIL REVIEW

On June 18, 2024, FY 2024-25 budget was initially approved with a General Fund deficit of $13.3 million. The City has been impacted by a structural deficit caused by increased costs for salaries, benefits, and services outpacing revenue growth. This structural deficit was projected to increase to $30.3 million by FY 2027-28 without intervention making the deficit unsustainable in the short term. (24-0452)

General Fund 5-Year Forecast Presented at FY 2024-25 Adoption 6/18/2024:

	FY 24-25	FY 25-26	FY 26-27	FY 27-28	FY 28-29
Revenues	$213.0	$218.1	$224.8	$230.0	$235.0
Transfers In	2.3	2.3	2.3	2.3	2.3
Total Revenues & TI	**$215.3**	**$220.4**	**$227.1**	**$232.3**	**$237.3**
Expenditures	220.2	227.0	238.5	252.3	263.8
Transfers Out	8.4	9.8	13.2	10.3	9.8
Total Expenditures & TO	**$228.6**	**$236.8**	**$251.7**	**$262.6**	**$273.7**
Budgeted Deficit	**($13.3)**	**($16.4)**	**($24.6)**	**($30.3)**	**($36.4)**

On August 6, 2024 the City Council introduced an ordinance to amend Chapter 3-28 of the Santa Rosa City Code to increase the Transient Occupancy Tax (TOT), paid by guests at hotels, motels, and other lodging establishments by two percent (2%), and approved a resolution ordering the submission of a ballot measure to seek voter approval of this ordinance at the November 5, 2024, General Municipal Election. (24-0573)

On August 6, 2024 the City Council introduced an ordinance to amend Chapter 6-04 of the City Code, entitled “General Business Tax” to increase the large business maximum tax to $10,000 annually, adjust business tax rates, and tax Short-Term Rental businesses, and approved a resolution ordering the submission of a ballot measure to seek voter approval of that ordinance at the November 5, 2024 General Municipal Election. (24-0574)

On November 5, 2024 voters passed ballot Measure EE to increase general business taxes and FF to increase the City’s TOT. The increased revenue from these changes resulted in actual collections exceeding the budgeted amount at adoption by $3.3 million for general business tax and $400,000 for the TOT.

On January 28, 2025, the City Council took mid-year actions to address the imbalance of the FY 2025-26 budget deficit of $13.3 million. Actions included reducing 13 full time equivalent (FTE) positions that had an ongoing budgetary savings of $4.0 million. Council additionally allocated $10.6 million in one-time funds from previously assigned projects to shore up reserves. (25-0061)

Prior to the FY 2025-26 budget development process, staff contracted with a firm, Alvarez & Marsal (A&M), to provide an independent validation of the City Long-Range Financial Forecast for the General Fund, and to evaluate the City’s annual budget process to provide insights on opportunities for improvement. A&M’s review found that the City’s General Fund financial model is a best practice and is more advanced than those used in other jurisdictions they have studied. Overall, the forecast methodology is sound; however, they noted that revenue forecasting should better align with actuals, notably that the City should lower its sales tax estimate to align with actual sales tax revenue.

On June 17, 2025, the City Council approved $11.4 million in budget reductions, which included eliminating 41 FTEs. Following these reductions, the Council adopted the FY 2025–26 budget with a remaining General Fund deficit of $8.4 million. (25-0429)

General Fund 5-Year Forecast after changes made during FY 2025-26 Adoption 6/17/2025:

	FY 25-26	FY 26-27	FY 27-28	FY 28-29	FY 29-30
Revenues	$215.1	$219.7	$224.5	$228.1	233.1
Transfers In	2.5	2.5	2.5	2.5	2.5
Total Revenues & TI	**$217.6**	**$222.2**	**$227.0**	**$230.6**	**235.6**
Expenditures	216.8	230.3	240.7	251.8	260.2
Transfers Out	9.2	9.3	9.5	9.0	9.2
Total Expenditures & TO	**$226.0**	**$239.6**	**$250.1**	**$260.8**	**269.3**
Surplus (Deficit)	**($8.4)**	**($17.3)**	**($23.1)**	**($30.1)**	**(33.7)**

ANALYSIS

The results presented are preliminary and unaudited, as the City's accounting staff is currently preparing the Annual Comprehensive Financial Report for FY 2024–25. While subject to change, no material modifications are anticipated at this time. The City's independent auditor, Macias Gini & O’Connell, is currently engaged in the annual financial audit. The audit's objective is to review the City's financial results and express an opinion on the fair presentation of the financial statements. Staff is collaborating with the auditors to ensure the timely completion of the review.

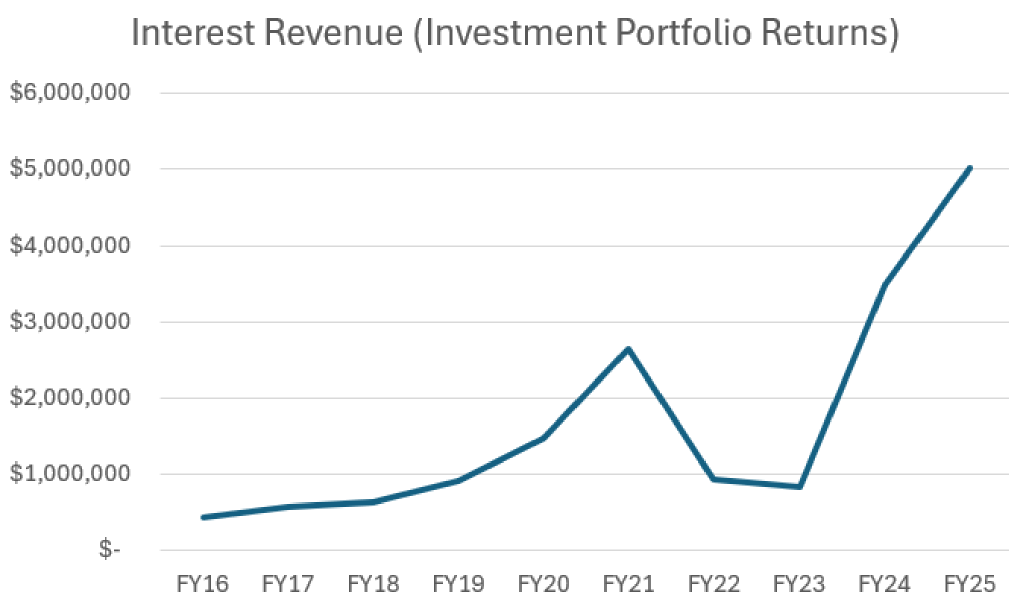
FY 2024-25 originally began with a $13.3 million budget deficit. During the year, the Council took action to address this shortfall. They approved $4.0 million in permanent budget reductions and released $10.4 million in one-time funding previously allocated to General Fund projects through PG&E settlement funds. Additionally, voter-approved enhanced revenue measures generated an extra $3.7 million for the General Fund from business and transient occupancy taxes. In total, these post-adoption measures amounted to $17.7 million in positive changes for the fiscal year.

Revenue Results FY 2024-25

The city's overall revenues surpassed the adopted budget by $3.1 million, which is a 1.4% increase when excluding changes to business and transient occupancy taxes. Despite this, several revenue categories showed variances. For example, sales tax revenue underperformed compared to budget by $6.8 million and was down $1.0 million versus the previous year. The final sales tax amount of $69.1 million for FY 2024-25 is also lower than the $71.2 million recorded in FY 2021-22. This decline is attributed to a decrease in consumer spending due to inflationary pressures, a shift in consumer behavior toward non-taxable goods and services, and continued growth in e-commerce. As sales tax is the city's largest revenue source, this stagnation in growth, which is not keeping pace with expenditure increases, is a primary factor in the General Fund's structural deficit. Property Tax revenue exceeded budget projections by $1.7 million due to sustained strength in local real estate market valuations. Charges for Services also posted a positive variance of $1.0 million, reflecting the continued rebound of recreation program participation.

The largest positive budget variance was recorded in investment earnings, which exceeded the budgeted amount by $4.4 million. The City’s long-standing practice is to budget a conservative, flat amount of $600 thousand for this line item, recognizing the inherent volatility of investment returns. This practice prioritizes budgetary stability by insulating operations from market fluctuations. However, the realized $4.4 million overage is substantially larger than historical results and indicates successful investment strategies. We are currently consulting with our investment advisor to analyze this performance trend and determine its reliability for integration into future revenue projections.

Without voter approved enhancements to business and transient occupancy taxes and investments outperforming historic norms, revenue would have been under budget by $1.3 million.



General Fund Revenues FY 2024-25

Revenue Source	FY 2024/25 Budget	FY 2024/25 Actual	Over (Under) Budget	% Difference
Interest	**$ 600,000**	**$ 5,022,393**	**$ 4,422,393**	**737.1%**
*** Interest is flat budgeted to $600K each year to insulate operations from gains and losses of the market**				

Revenue Source	FY 2024/25 Budget	FY 2024/25 Actual	Over (Under) Budget	% Difference
TOT	$ 7,000,000	$ 7,399,552	$ 399,552	5.7%
Business Taxes	$ 4,750,000	$ 8,018,506	$ 3,268,506	68.8%
Total	**$ 11,750,000**	**$ 15,418,058**	**$ 3,668,058**	**31.2%**
**** Voter approved changes occured after adoption and were not included in budget**				

Revenue Source	FY 2024/25 Budget	FY 2024/25 Actual	Over (Under) Budget	% Difference
Sales Taxes	**$ 75,866,735**	**$ 69,098,976**	**$ (6,767,759)**	**-8.9%**
Property Taxes	$ 39,068,300	$ 40,764,412	$ 1,696,112	4.3%
Other Taxes (net of BT and TOT)	$ 36,625,700	$ 37,290,883	$ 665,183	1.8%
Charges for Services	$ 26,727,653	$ 27,709,234	$ 981,581	3.7%
UUT	$ 14,200,000	$ 15,059,524	$ 859,524	6.1%
Contributions from Private Parties	$ 3,611,535	$ 3,408,160	$ (203,375)	-5.6%
Licenses and Permits	$ 3,181,000	$ 2,899,067	$ (281,933)	-8.9%
Miscellaneous	$ 2,116,360	$ 4,075,098	$ 1,958,738	92.6%
Intergovernmental Revenue	$ 1,991,493	$ 1,807,234	$ (184,259)	-9.3%
Fines and Forfeitures	$ 1,610,900	$ 1,613,965	$ 3,065	0.2%
Total	**$ 204,999,676**	**$ 203,726,554**	**$ (1,273,122)**	**0.6%**
		Total	**$ 6,817,330**	**3.1%**

Operating Expenditure Results FY 2024-25

The General Fund concluded FY 2024–25 with expenditures exceeding the final budget by $1.7 million or 0.8%. This net result includes the $4.0 million mid-year budget reduction approved by the City Council. Most City departments finished the fiscal year under budget, primarily due to a hiring freeze implemented by the City Manager. The Fire Department exceeded its budget by $1.7 million, driven by salaries and benefits, specifically overtime expenditures.

The significant annual budget "turnback" (underspending) experienced by the General Fund during and immediately following the COVID-19 pandemic did not occur in FY 2024–25. Staff do not anticipate the return of significant turnback in future years. This shift is due to the City no longer experiencing a high rate of position vacancies and budgets generally tightening as a result of recent reductions.

Department	Budget + Carryover + Changes	Actuals + Encumbrance* FY2024/25	(Over) Under Budget	% Difference
Police	80,571,388.43	80,416,648.74	154,739.69	-0.2%
Fire	57,748,948.87	61,016,048.74	(1,667,596.11)	2.9%
Public Works	26,219,989.03	26,662,201.05	(442,212.02)	1.7%
Planning, Economic Development	19,746,875.47	17,963,009.08	1,783,866.39	-9.0%
Recreation & Parks	18,558,194.14	18,601,762.18	(43,568.04)	0.2%
Finance	7,889,387.03	7,562,332.99	327,054.04	-4.1%
City Attorney	5,057,586.37	4,685,509.40	372,076.97	-7.4%
Human Resources	4,778,764.02	3,855,903.26	922,860.76	-19.3%
City Manager	3,318,991.46	2,846,157.40	472,834.06	-14.2%
CIRO	1,781,767.38	1,385,710.26	396,057.12	-22.2%
City Council	1,371,462.77	1,455,928.93	(84,466.16)	6.2%
Water	780,984.48	703,835.87	77,148.61	-9.9%
HCS	125,206.99	125,205.88	1.11	0.0%
Non Departmental (Vacancy Offset)	(9,587,042.42)	(7,228,312.53)	(2,358,729.89)	-24.6%
Total	**218,362,504.02**	**220,051,941.25**	**(1,689,437.23)**	**0.8%**

**Non Departmental contains the City's vacancy credit and creates a presentation of being over budget while realized savings is captured in operating department.*

Reserves Analysis and Projections

Preliminary results show a net increase of $9.5 million in General Fund Reserves. This achievement is significant given the fund began the fiscal year with a $13.3 million deficit.

The positive outcome was primarily driven by strategic mid-year financial adjustments, voter approved enhanced revenues, and the City's investment portfolio outperforming historical norms:

- One-Time Funding: Mid-year adjustments included the release of $10.4 million in one-time funds from PG&E settlement projects.
- Ongoing Reductions: $4.0 million in ongoing expenditure reductions were implemented.
- Voter-Approved Revenue: An additional $3.7 million was generated through voter-approved revenue enhancements, specifically increases to Business Taxes and the Transient Occupancy Tax (TOT).
- Investment returns outperforming budget by $4.4 million.

These factors, combined with the remaining revenues, operating expenditures, changes to encumbered contracts and project budgeting led to an additional $1.7 million on a budgetary basis, which directly contributed to the overall increase in reserves.

Without voter approved enhanced tax measures and the release of one-time funded projects reserves would have decreased by $5.0 million.

Despite the net increase in General Fund reserves projected for FY 2024-25, the remaining structural deficit poses a critical risk. Without intervention, reserves are projected to fall $3 million below mandated levels by the budget year under development (FY 2026-27), with only $8 million in total reserves remaining by FY 2027-28.

Current Total Reserves Usage Projection					
			Upcoming Budget Adoptions		
	FY2025	FY2026	FY2027	FY2028	FY2029
6/30/2024 Reserves	**$ 68,826,590**				
Adopted deficit	$ (13,300,000)				
Mid-year budget reduction	$ 4,000,000				
FY 25/26 results variance from budget	$ 4,300,000				
Results of Operating	**$ 63,826,590**				
Enhanced taxes	$ 3,700,000				
One-time projects released	$ 10,400,000				
6/30/2025 Preliminary Reserves	**$ 77,926,590**				
FY 26/27 Budget Deficit		$ (17,300,000)			
6/30/2026 Projected Reserves		**$ 60,626,590**			
FY 27/28 Budget Deficit			$ (23,100,000)		
6/30/2027 Projected Reserves			**$ 37,526,590**		
FY 28/29 Budget Deficit				$ (30,100,000)	
6/30/2028 Projected Reserves				**$ 7,426,590**	
FY 29/30 Budget Deficit					$ (33,700,000)
6/30/2029 Projected Reserves					**$ (26,273,410)**
* Council Mandated Reserve was $34.9M in FY2024, expected to be $40.6M in 2027					

Budget Reductions and Operational Data

Over the past year, the Council adopted $15.2 million in ongoing budget reductions. Departments were initially directed to propose 8% cuts to their budgets. Following review and Council direction, final department reductions varied from this target, as detailed in the following table.

Department	8% Target		Over (Under) Target	
Police	$	6,222,331	$	(3,217,329)
Fire Department	$	4,469,286	$	(2,342,286)
TPW	$	2,060,252	$	(165,647)
PED	$	1,400,261	$	109,929
Rec and Parks	$	1,369,611	$	(202,880)
Finance	$	640,292	$	1,114,610
HCS	$	392,022	$	1,186,978
Human Resources	$	371,420	$	148,015
City Attorney	$	367,459	$	(59,409)
City Manager	$	253,062	$	591,838
Comms and Intergovt.	$	145,580	$	298,788
Water	$	59,617	$	(2,617)

Staff is developing a tiered approach to proposing budget reductions for FY 2026-27. As part of this process, all departments are preparing financial presentations for the Long Range Financial Planning and Audit Subcommittee. These presentations are designed to get feedback and guidance for department-specific tiering of programs and services. The presentations started in September with a detailed look at the Housing and Community Services budget, including its composition, results, and services provided.

The Committee has requested that the Finance Department consistently provide more operational data, specifically General Fund spending changes as a percentage over time by function. This study session will present data categorized by public safety, operational, and administration departments and how the allocation of funding has changed over time.

Summary

Despite significant actions taken to shore up reserves in FY 2024-25 and ongoing budget reductions totaling $15.2 million, the General Fund remains in a structural deficit that necessitates further intervention. While one-time actions temporarily boosted reserves, the City continues to face a fundamental imbalance where expenditure increases outpace revenue growth.

Several factors have exacerbated the deficit, most notably the escalating costs associated with the California Public Employees' Retirement System (CalPERS) unfunded liability and lack of sales tax growth. General Fund payments toward the CalPERS unfunded liability are a major driver of the structural deficit, nearly doubling from $17.0 million in FY 2019-20 to a projected $34.5 million by FY 2026-27.The stagnation of sales tax growth is financially unsustainable. FY 2024-25 sales tax revenue is actually lower than it was three years ago, failing to keep pace with the rising cost of services.

Finance staff will continue to refine projections and budgets as information becomes available. The City's budgeting model continues to be sound. The increases in business and transient occupancy tax were included in the FY 2025-26 budget along with a reduced budget from sales tax to align with experience over the past three years.

In late January, we will run a projected payroll model for FY 2026-27 to gain a clear view of the potential deficit. Based on all current data, we do not anticipate a material difference from the $17.3 million deficit presented at the time of FY 2025-26 budget adoption. This will provide the basis for budget development guidelines that align with tiered priorities.

FISCAL IMPACT

This Study Session does not have a fiscal impact on the General Fund.

ENVIRONMENTAL IMPACT

Pursuant to CEQA Guidelines Section 15378, the recommended action is not a "project" subject to the California Environmental Quality Act (CEQA) because it does not have a potential for resulting in either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment. In the alternative, the recommended action is exempt from CEQA pursuant to CEQA Guidelines section 15061(b)(3) because it can be seen with certainty that there is no possibility that the recommended action may have a significant effect on the environment.

BOARD/COMMISSION/COMMITTEE REVIEW AND RECOMMENDATIONS

None.

NOTIFICATION

Not applicable.

ATTACHMENTS

None.

PRESENTER

Scott Wagner, Interim Chief Financial Officer