

City of Santa Rosa Update of Long-Range Financial Forecast

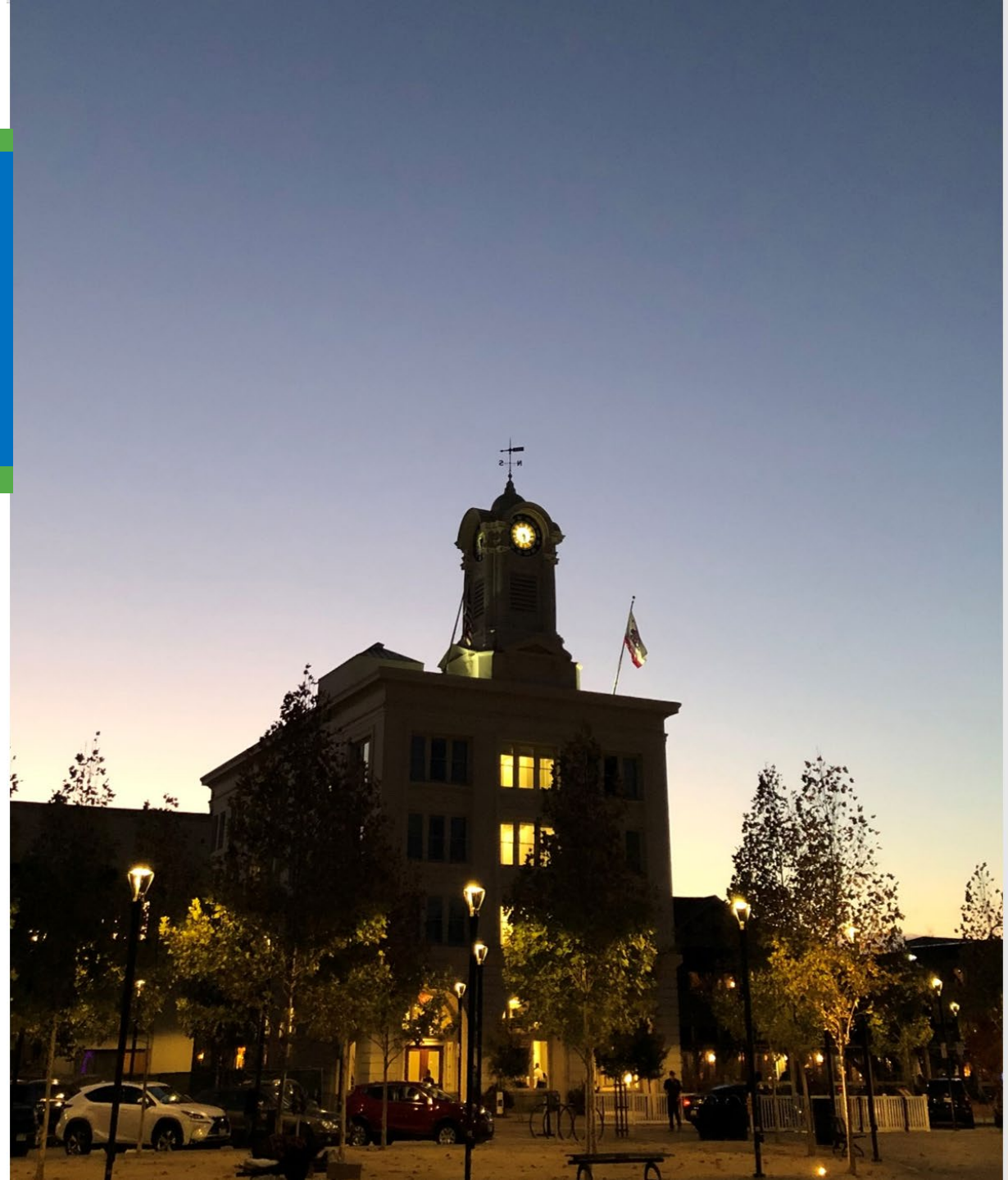
Presentation to City Council Study Session

Andy Belknap, Senior Vice President

Bob Leland, Special Advisor

April 6, 2021

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Partners



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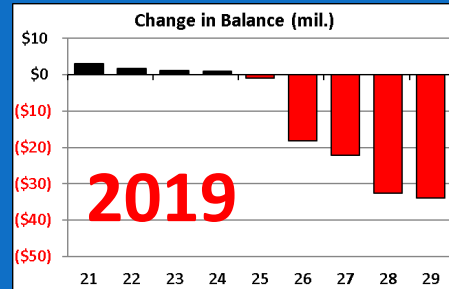
of California cities with more than 100,000 people
(53 of 59)

Our Services

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- Operations Improvement
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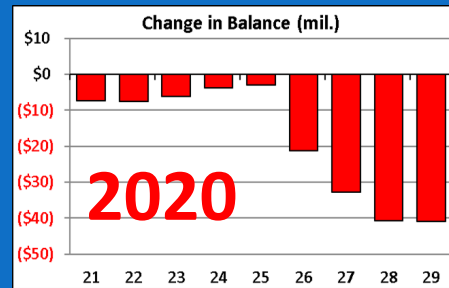
Consulting team has decades of forecasting experience, and has completed over 40 forecast models for local agencies in recent years

Project History



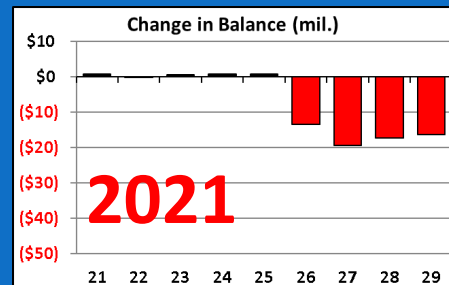
Created a long-range forecast model in Sep 2019

- Emphasis on rebuilding impacts, pension costs
- Model completed in Dec 2019



Fiscal model update for Covid-19

- Added pandemic revenue impacts in Apr 2020
- Budget strategies presented to Council in Sep 2020

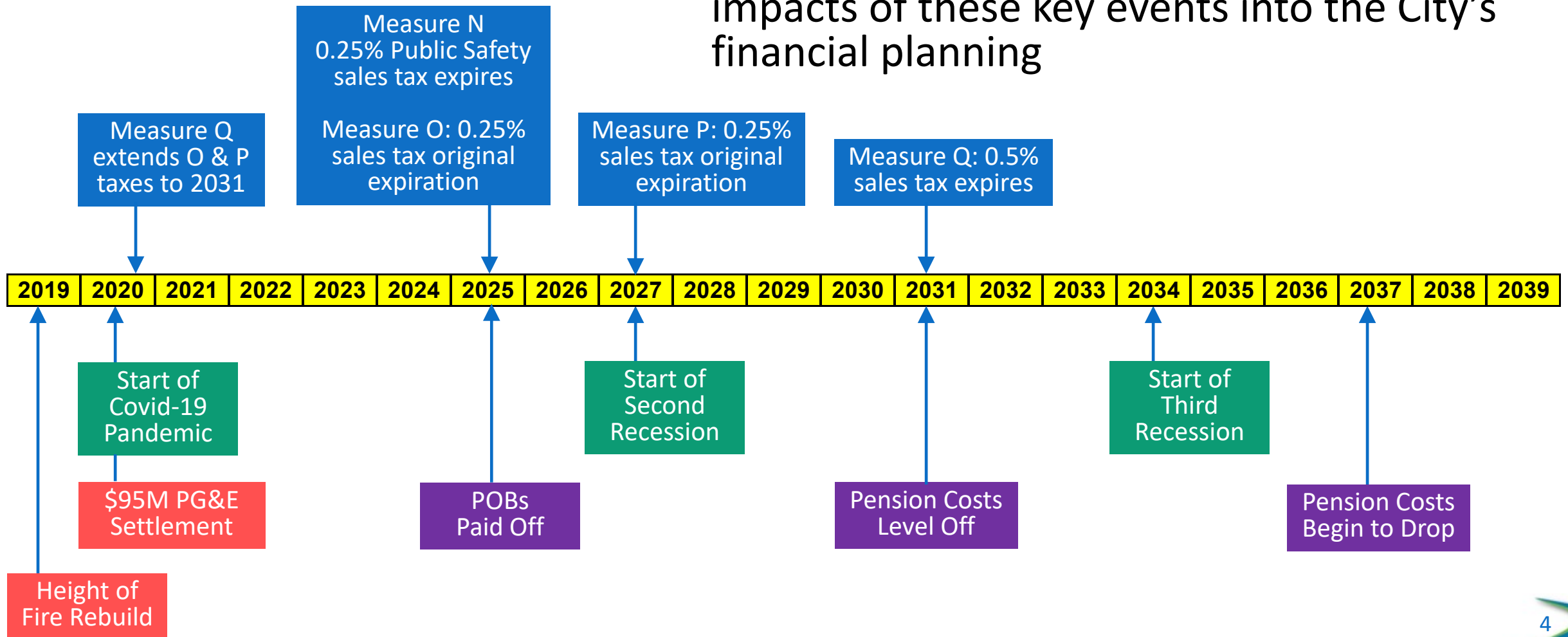


Fiscal model update in Feb 2021

- Revised pandemic revenue impacts
- Provides context for FY 2022 budget process
- Alternative scenarios for balanced long-term forecast

Timeline of Major Fiscal Events

- Long-term forecast is needed to incorporate impacts of these key events into the City's financial planning



Updated Baseline Forecast



Key Revenue Assumptions & Rationale

Economic Cycles

- **Pandemic recovery moved up from FY25 to FY24**
 - Sales Tax stronger per Avenu's 3Q20 forecast
 - TOT, rec/park fees slower to recover
- **Future moderate recessions starting in FY27 and FY34**
 - Historically recessions occur every 6-7 years
 - Including in forecast provides "stress test" for sustainability of reserves

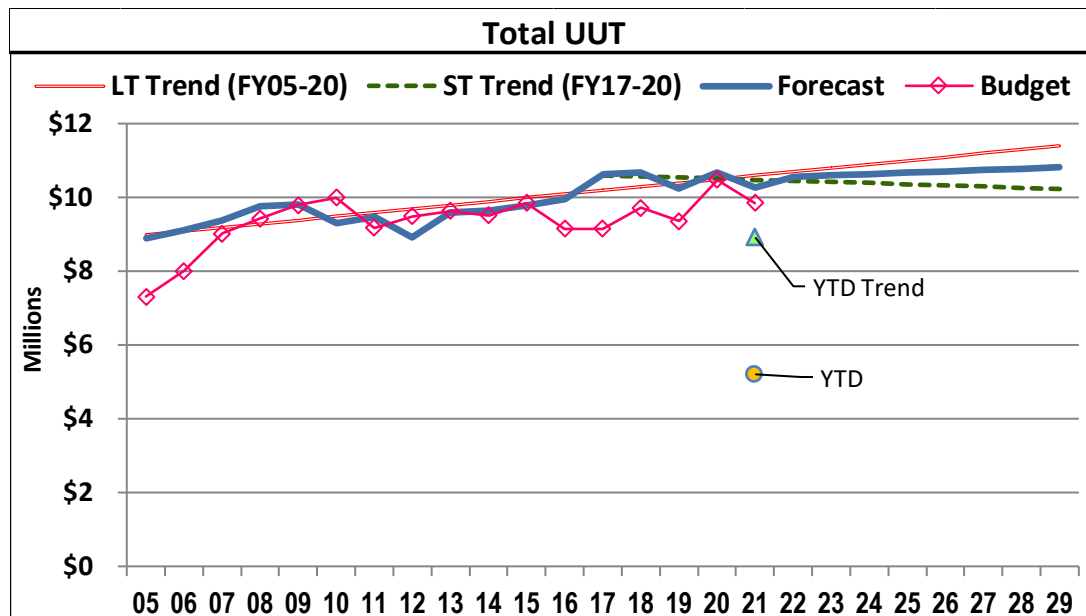
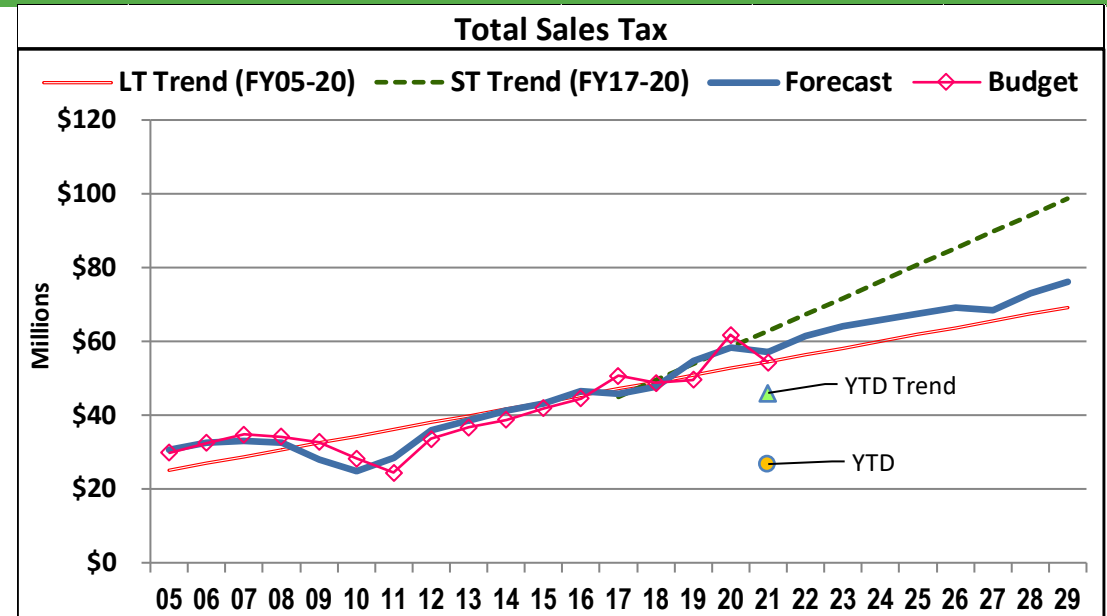
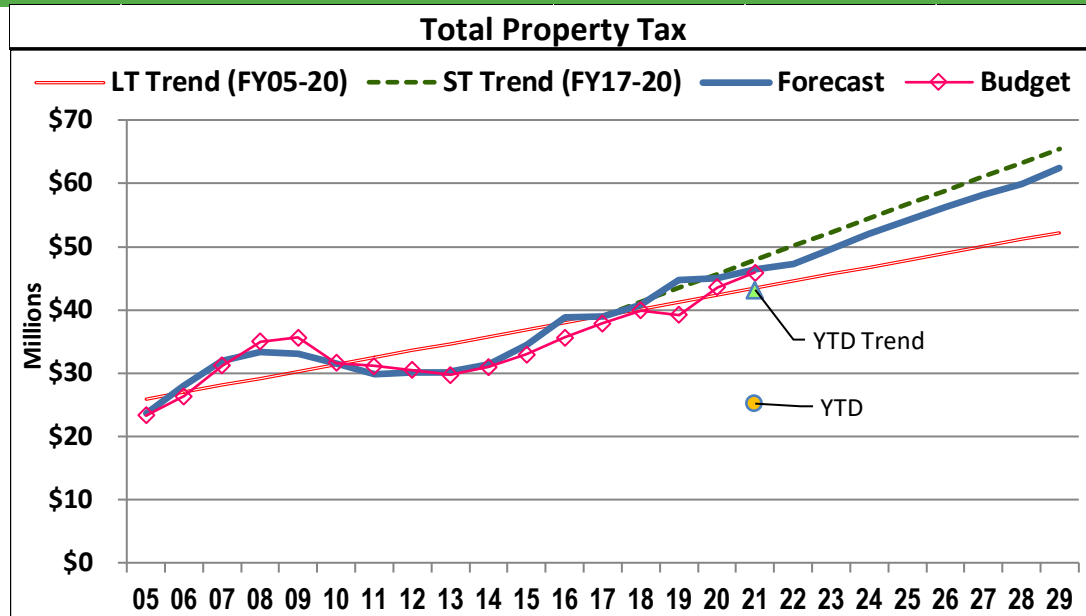
Local Sales Taxes

- **Measure O (0.25% public safety tax) expires in 2025, GF to backfill revenue loss**
 - Current measure sunsets without a 2/3rds vote to extend the tax
 - Public safety positions are a high priority service which will place pressure on GF to replace lost revenue if tax expires
- **Measure Q (0.5% general sales tax) expires 2031**
 - Current measure sunsets in 2031 without a majority vote to extend

One-Time Funding

- **PG&E settlement is excluded**
 - Best practice is to use for one-time, not ongoing expenses; however, Council has discussed using \$40M of the \$95M settlement to support operations, which buys time to restructure expenses
- **ARPA federal aid is excluded**
 - \$36.4M in aid, but only amounts replacing lost GF revenues or reimbursing past/budgeted costs should be counted in forecast
- **FEMA reimbursements (beyond estimated FY21) are excluded**
 - Staff has identified \$40.7M in potential outstanding reimbursements for the GF; timing of receipt uncertain

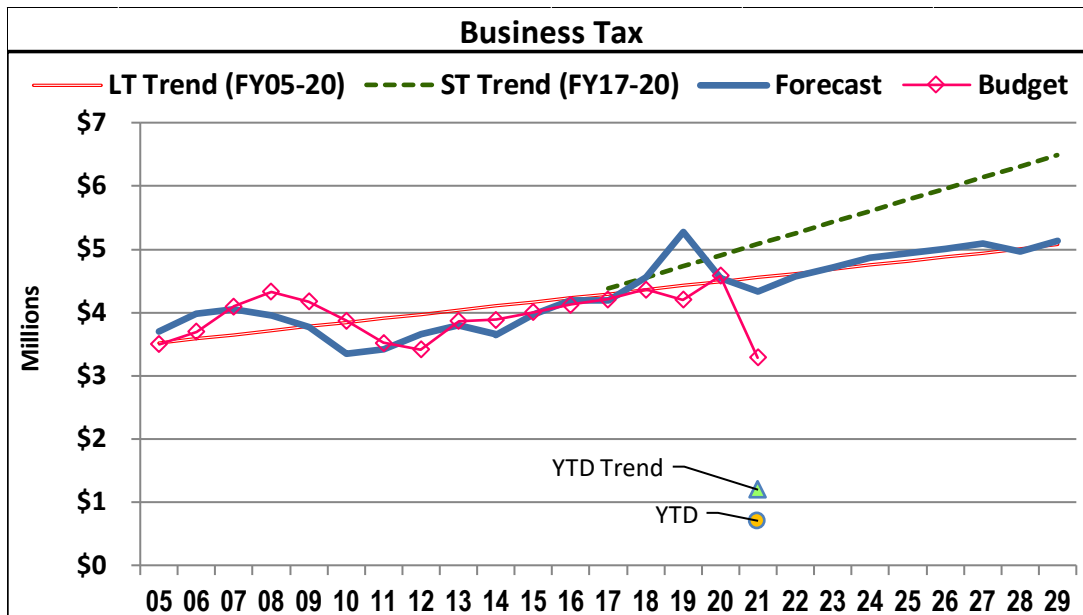
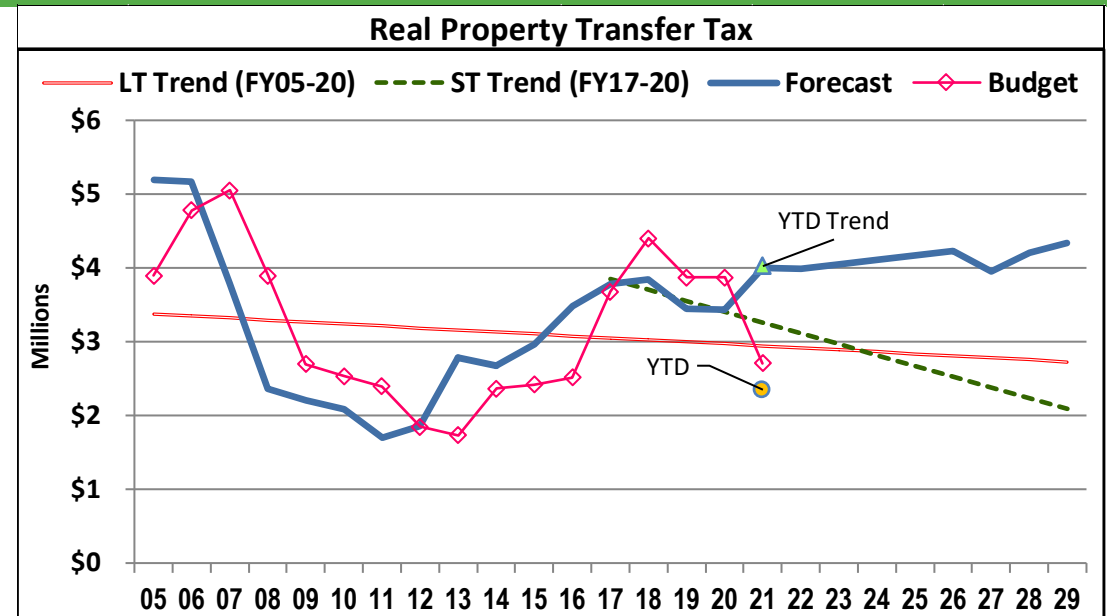
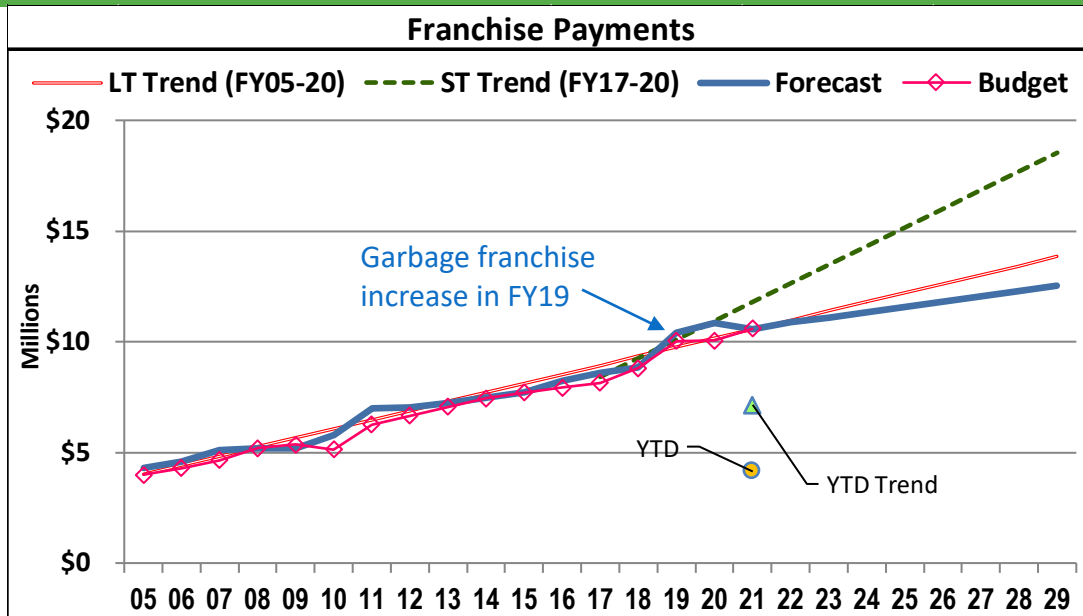
Largest GF Revenues are Relatively Stable



- Property tax has 1.036% inflator in FY22 (2% thereafter); home sale prices are strong; assumes all rebuilds by 2025 and 500 new units/year ongoing; follows short-term trend
- Sales taxes recovering more quickly than original estimates; uses Avenu 3Q20 forecast; follows long-term trend
- UUT growth splits long-term and short-term trends

Note that uneven cash flow means YTD Trend not always indicative of final amount for FY21

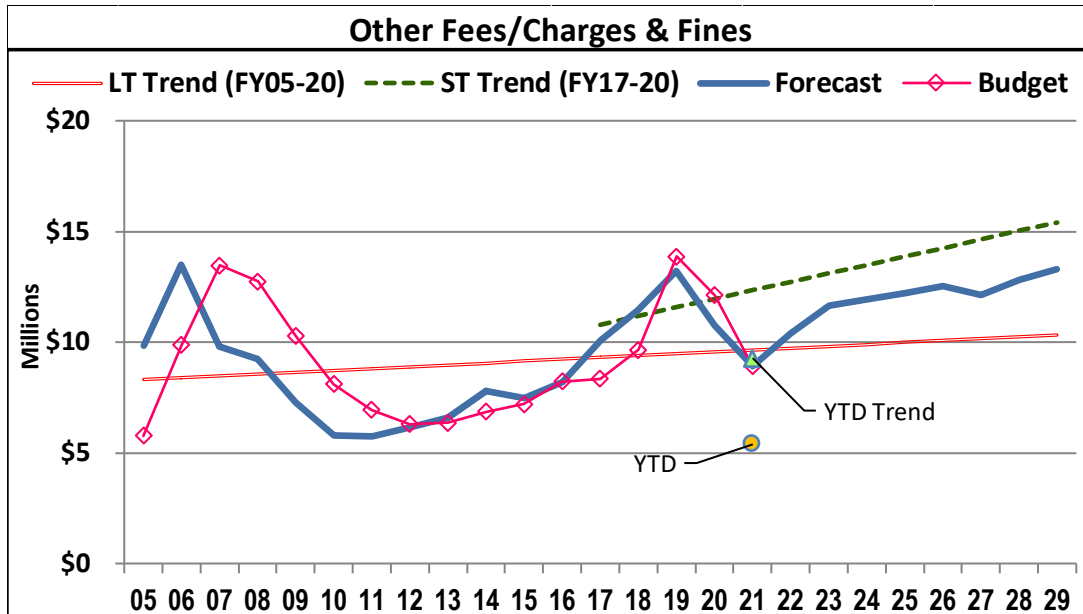
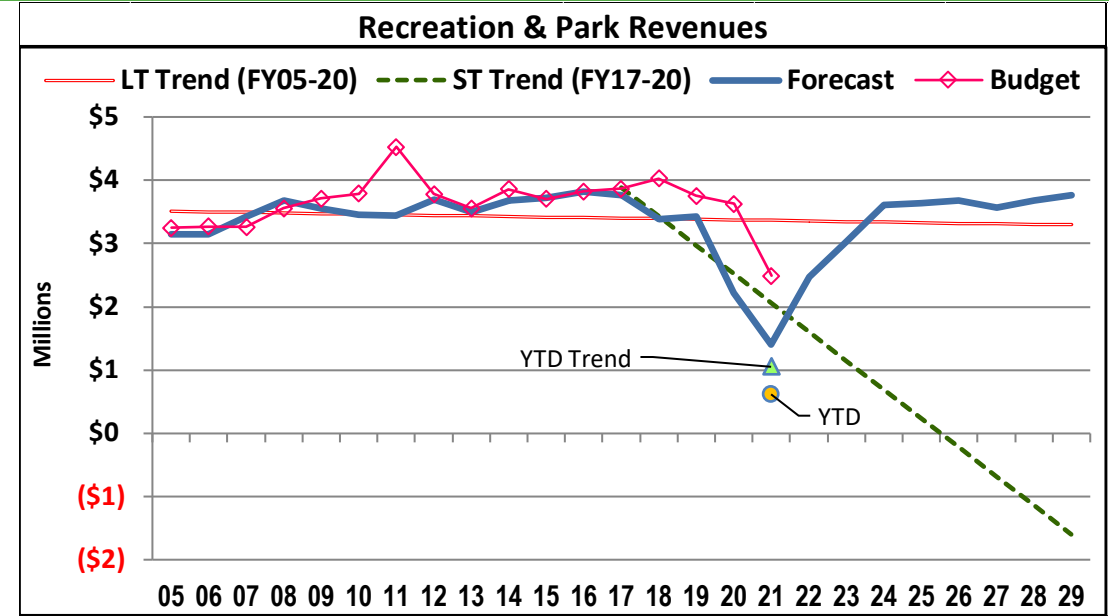
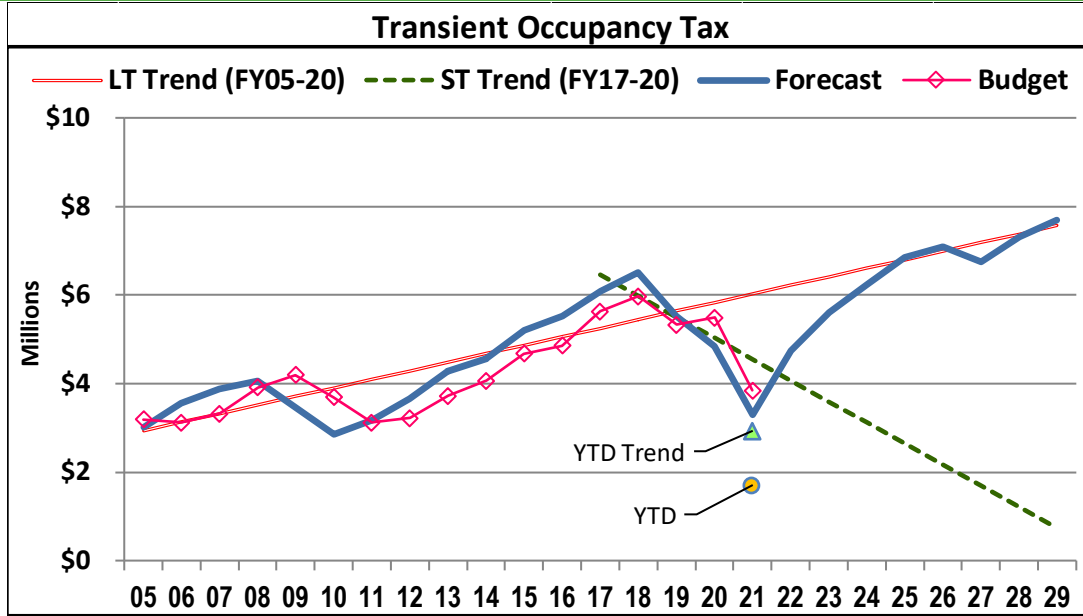
Other Taxes Have Varying Impacts



- Franchise payments have been historically stable; generally follows long-term trend
- RPTT is prone to volatility, but growing home sale prices have boosted FY21 revenues well over budget
- Business tax estimate anticipated lower FY21 revenues; forecast follows HdL projections for FY21 & FY22, then follows long-term trend

Note that uneven cash flow means YTD Trend not always indicative of final amount for FY21

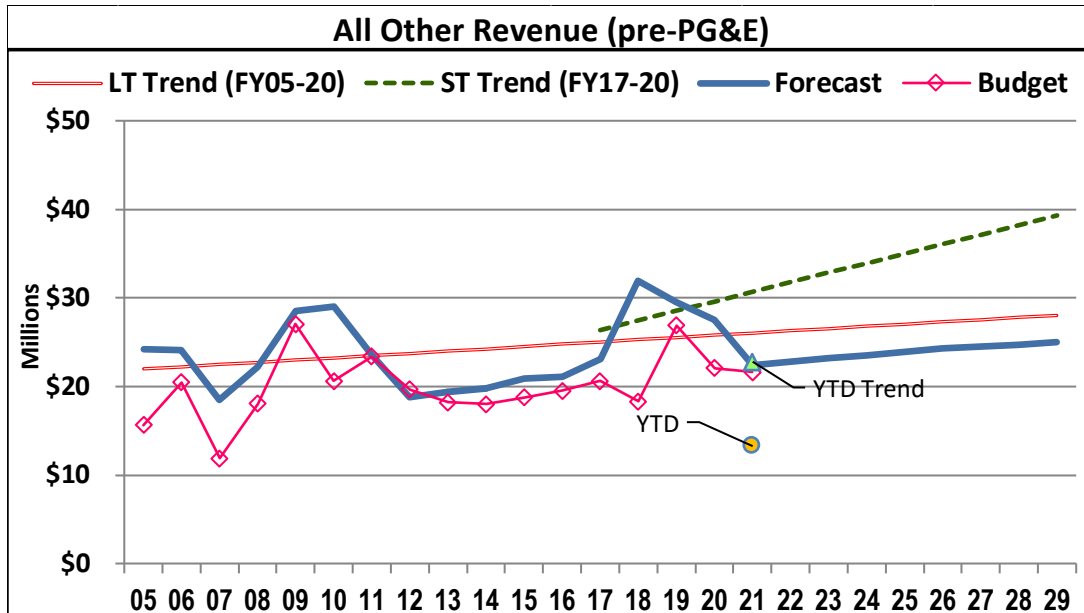
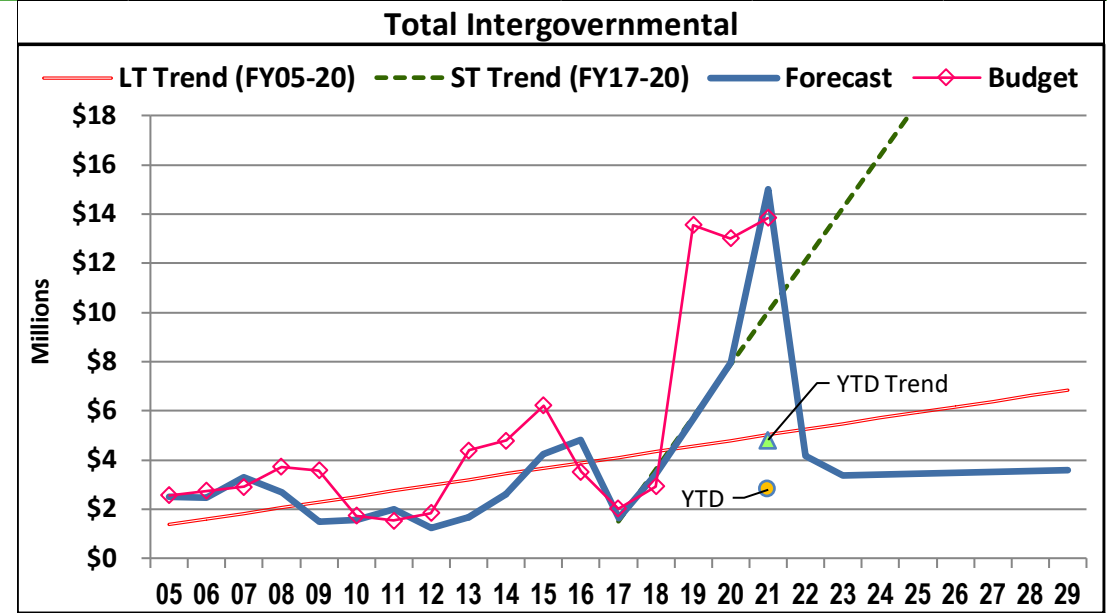
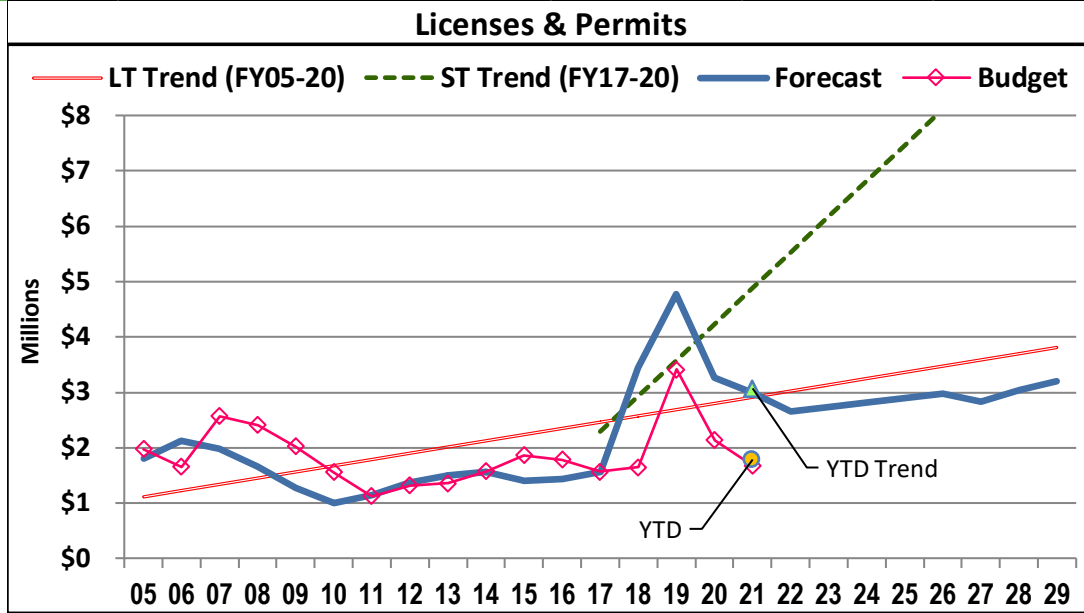
Revenues Most Severely Impacted by Pandemic



- TOT plunged in FY20 & FY21 due to pandemic impacts on travel, leisure and hospitality industries; recovery projected by FY25
- Rec & Park fees hurt by social distancing and event size limits; assumes recovery by FY24
- Other fees affected by lower activity levels in general, but still near long-term trend in FY21; assumes recovery by FY23

Note that uneven cash flow means YTD Trend not always indicative of final amount for FY21

Remaining Revenues Lower Than Recent Peaks



- Licenses & Permits peak in FY19 is from height of rebuild permits; forecast is nearer long-term trend
- Intergovernmental peaks in FY20-FY21 due to CARES Act and FEMA reimbursements; does not include potential new federal aid
- All Other Revenue peaks in FY18-FY19 due to insurance reimbursements, and in FY09-FY10 from transfers in; does not include PG&E settlement

Note that uneven cash flow means YTD Trend not always indicative of final amount for FY21

Key Expense Assumptions & Rationale

Sustainability

- **Positions frozen for 5 years, restored starting FY26**
 - Uncertainty over Measure N requires City to conserve fund balance to better position itself for potential loss of these funds
- **Add 2 FTE/year starting FY23**
 - Population/workload growth will create pressure to unfreeze positions and/or add new positions over time; responds to this need in graduated fashion
- **\$4M CIP transfer eff. FY22**
 - Ongoing needs for preventative maintenance and other projects; average of last 15 years

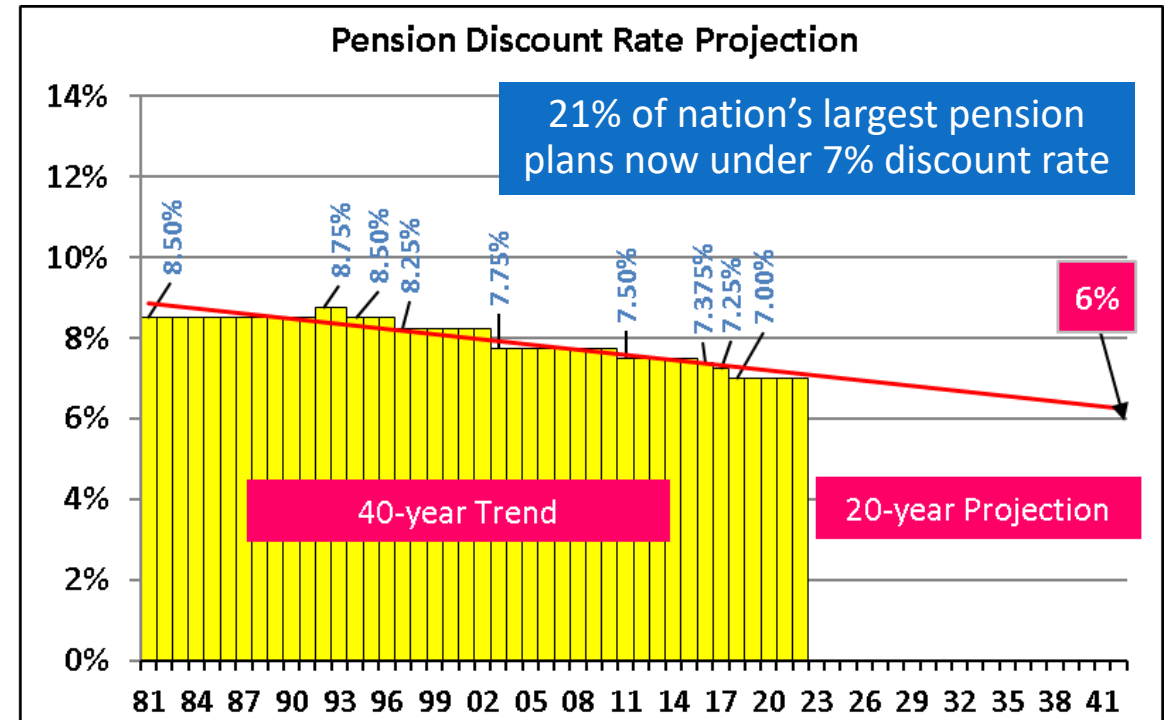
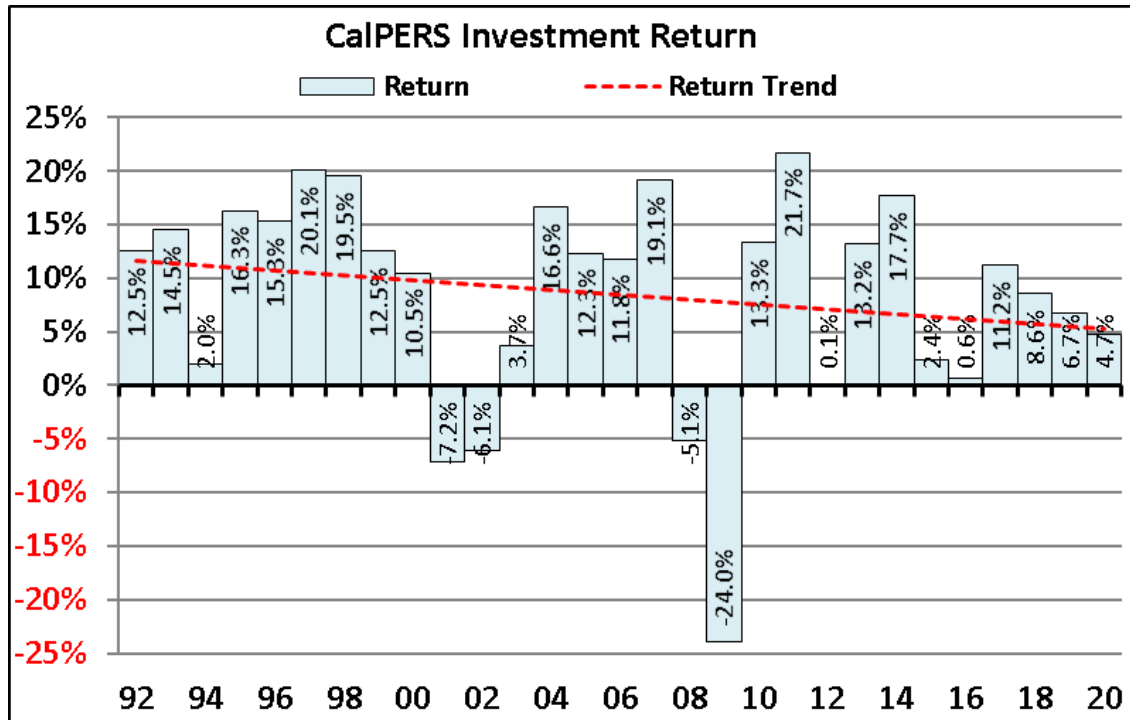
Cost Inflation

- **2% COLAs starting FY21**
 - MOUs have expired, but negotiations are ongoing; labor is largest expense and inflationary pressure must be included for forecast to be realistic
- **FY22 O&M/part-time/OT held to FY20 actuals**
 - Budget direction to departments is to hold these costs to the lesser of last year's actual or projected increase from FY21 budget; growth resumes in FY23 based on that FY22 level; cost of current positions would not be restricted
 - Reduces FY22 expense by \$6.4M (3.3%) compared to forecast model growth for FY22

Pensions

- **6.2% average returns**
 - Investment returns have been gradually falling for 30 years
 - Wilshire Associates estimated average annual return over next decade at 6.2%
- **6% discount rate phased in over 20 years**
 - CalPERS wants to decrease rate volatility and improve funded status, which means an eventual reduction in the discount rate
 - 6% supported by continuation of past 30 years of discount rate change

Pension Returns & Discount Rate

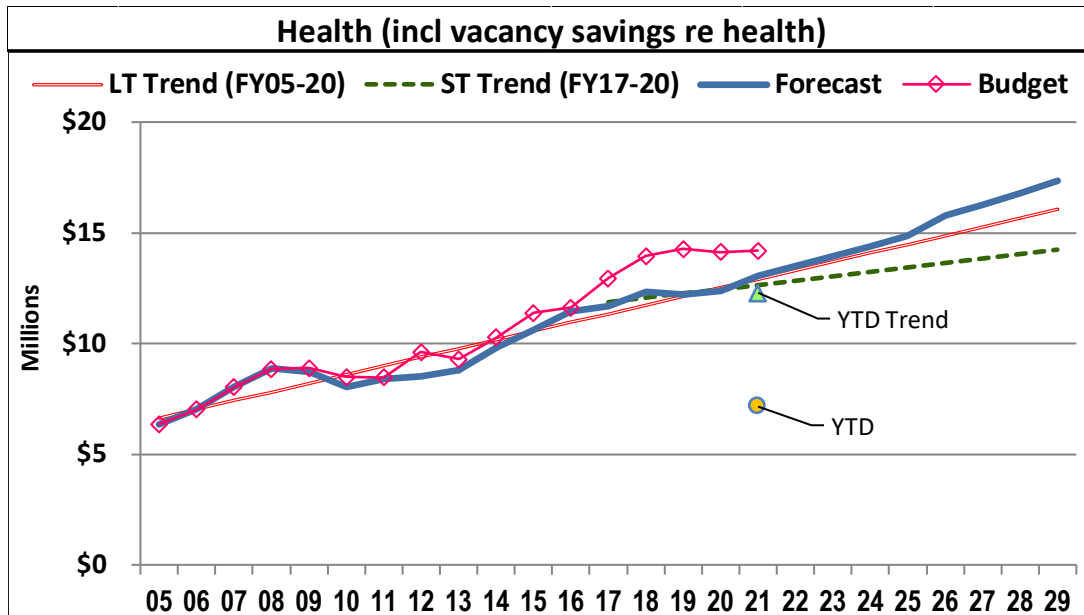
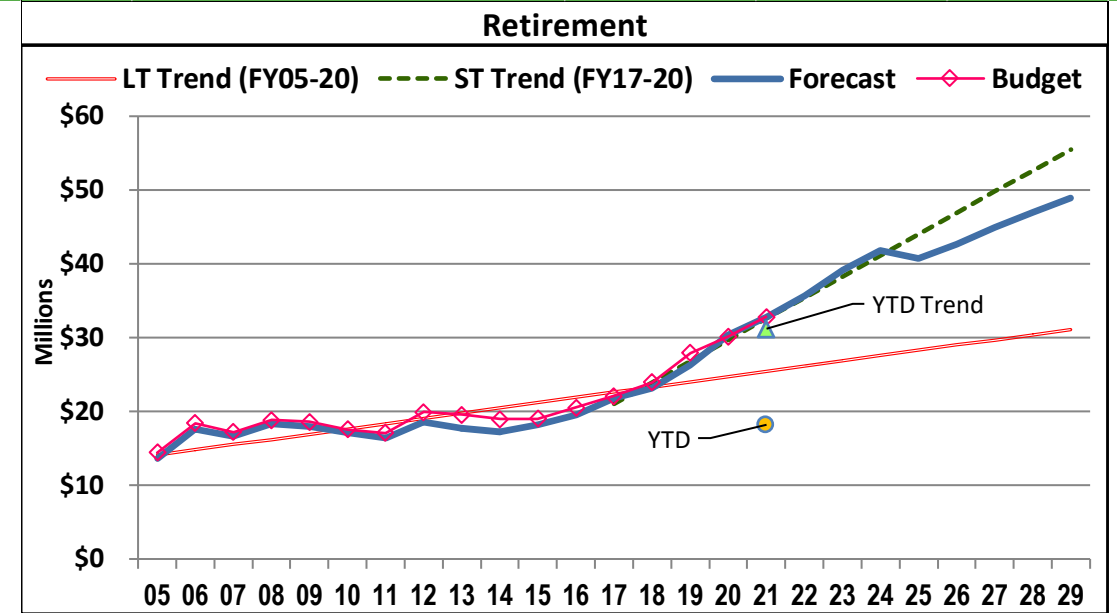
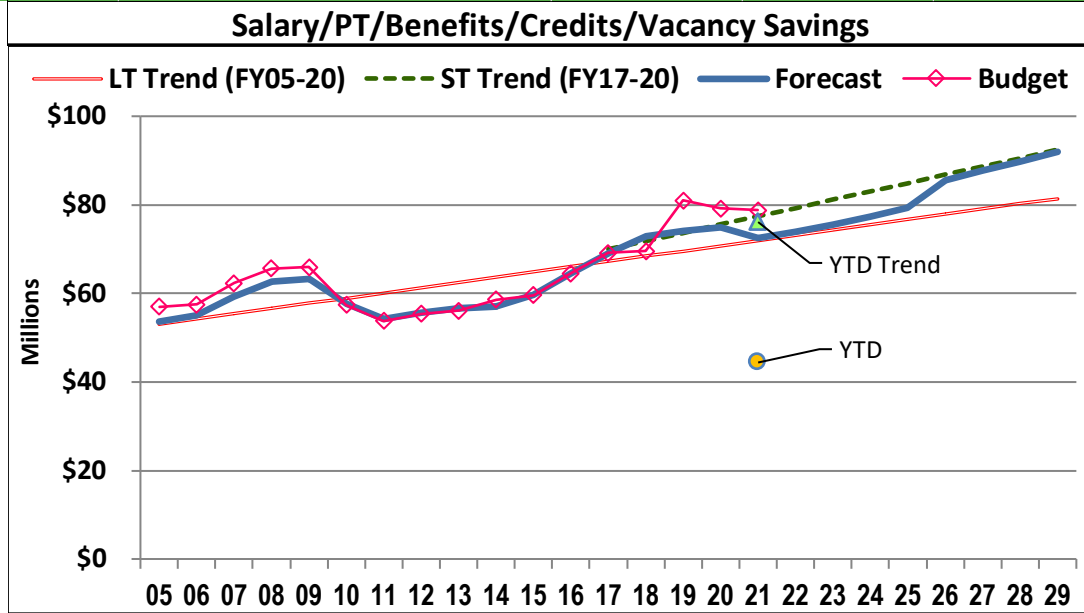


- Values above the pink line are years exceeding the discount rate and values below are years falling short of that level
- Slow downward trend in returns over the past 29 years

Average Returns	
6.67%	last 3
6.36%	last 5
8.69%	last 10
6.07%	last 20
8.43%	last 29

- Extending decline in discount rate over past 40 years hits just over 6% in 20 years
- CalPERS is reviewing its strategic asset allocation and discount rate in 2021; any change will be made in November to take effect 7/1/22

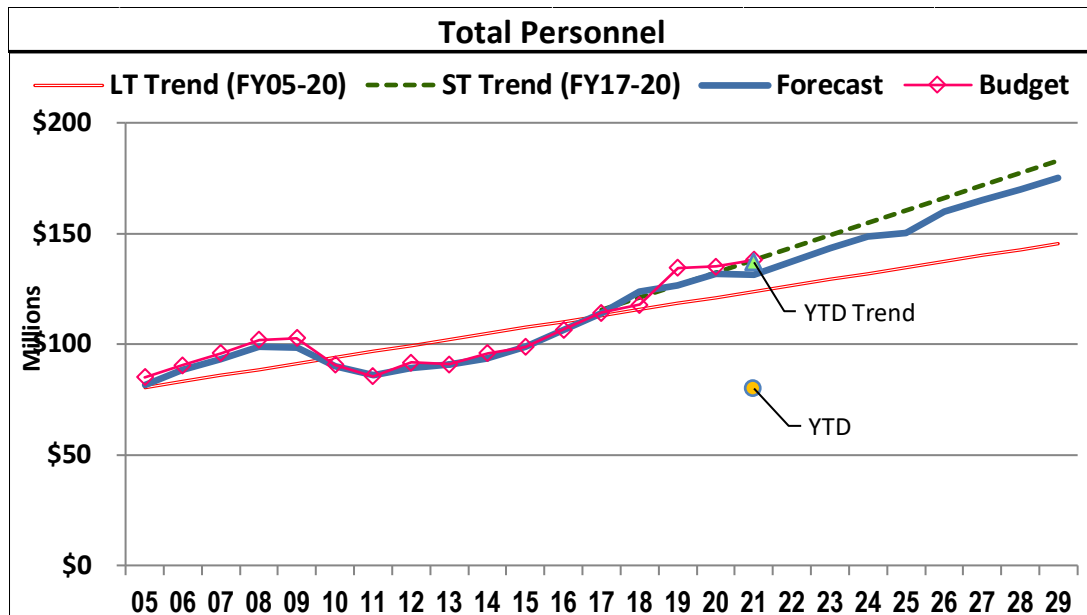
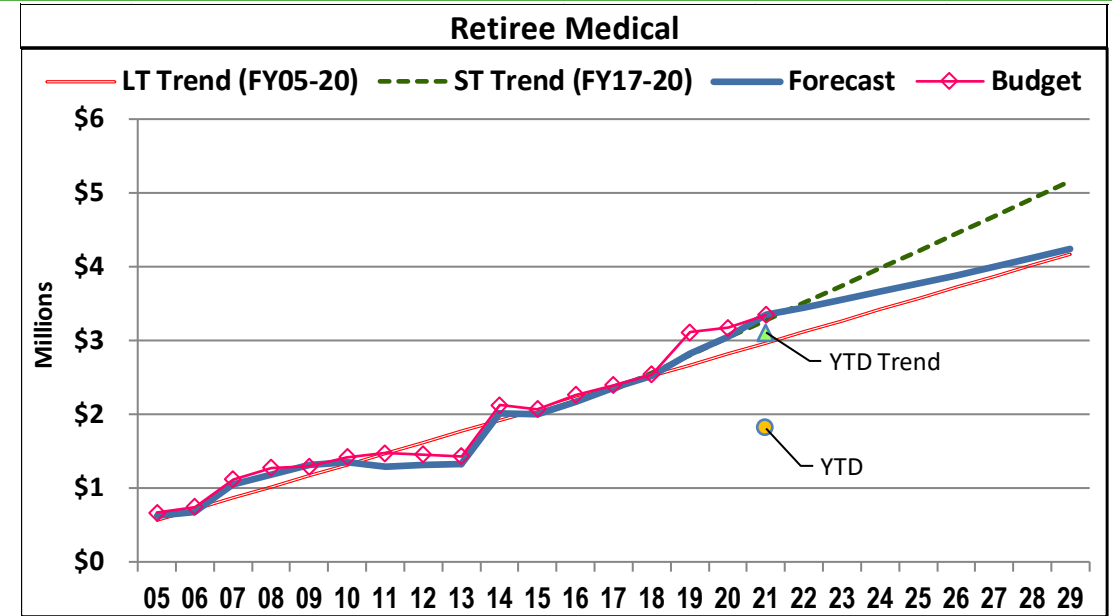
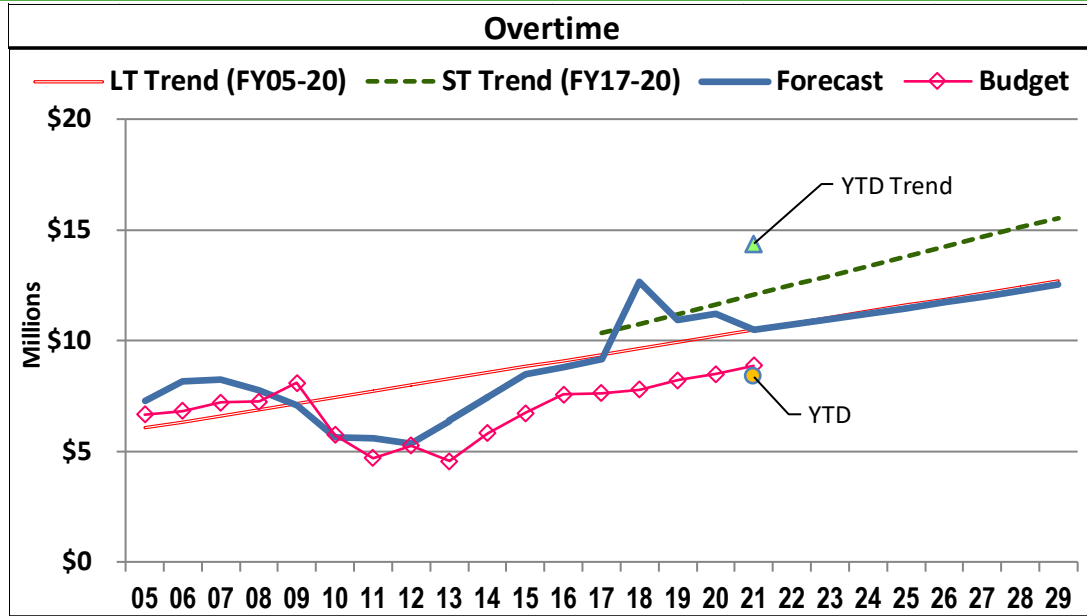
Personnel Expense Forecast



- Salaries/Benefits continue on short-term trend except for savings from 5yr position freeze (resulting vacancy rate is 4.5% for FY21-25, 1.5% after)
- Retirement costs use the lower returns and discount rate; projections follow short-term trend; reduction in FY25 is due to end of POB debt service
- Health at YTD trend for FY21, follows long-term trend thereafter (90% of position control calcs, including impact of vacancy savings on health costs)

Note that uneven cash flow means YTD Trend not always indicative of final amount for FY21

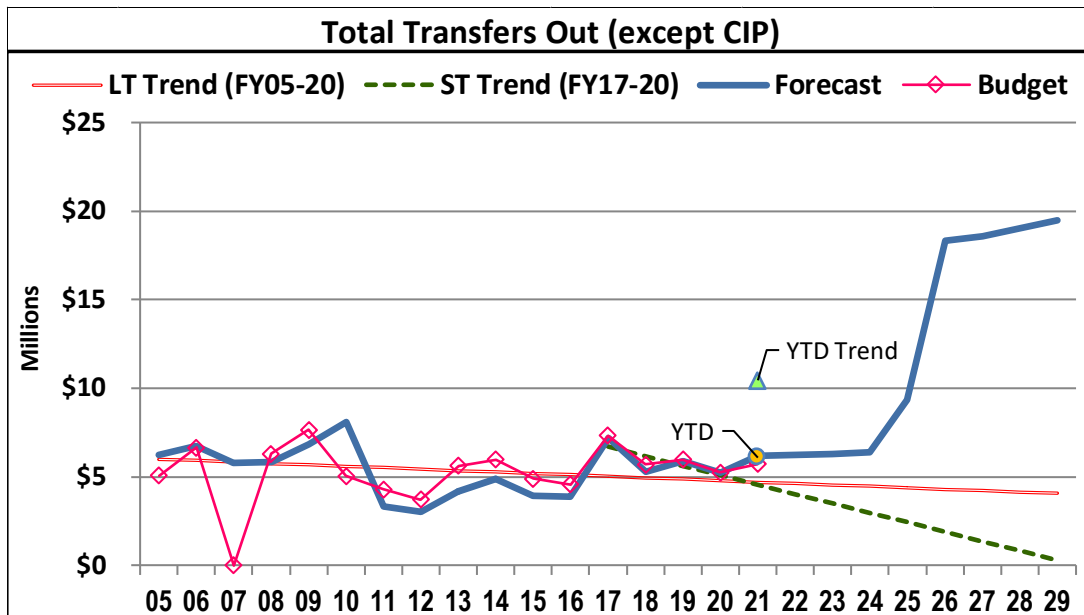
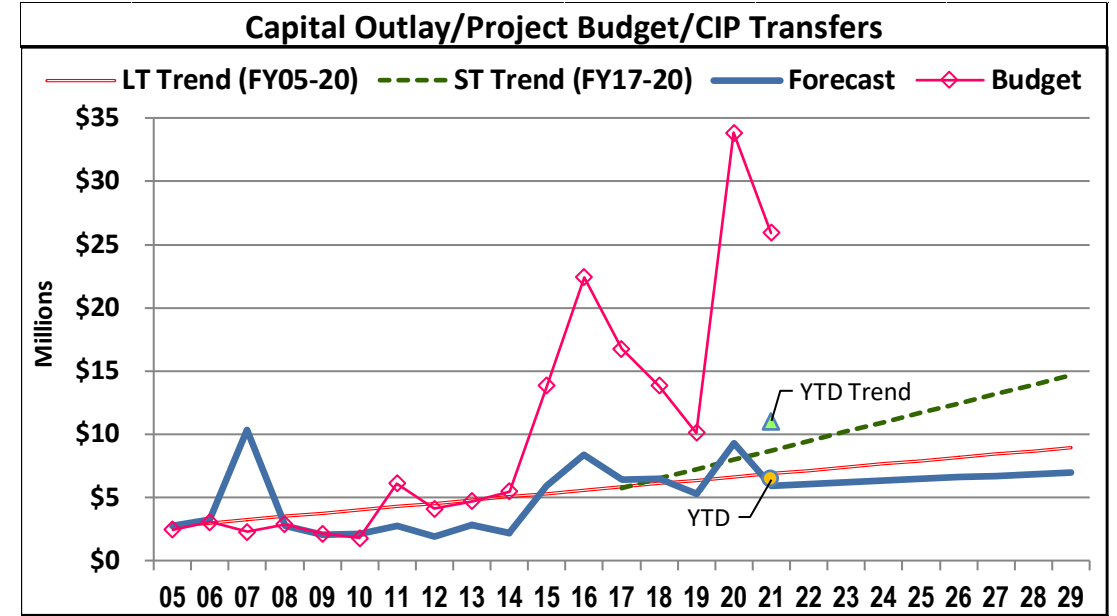
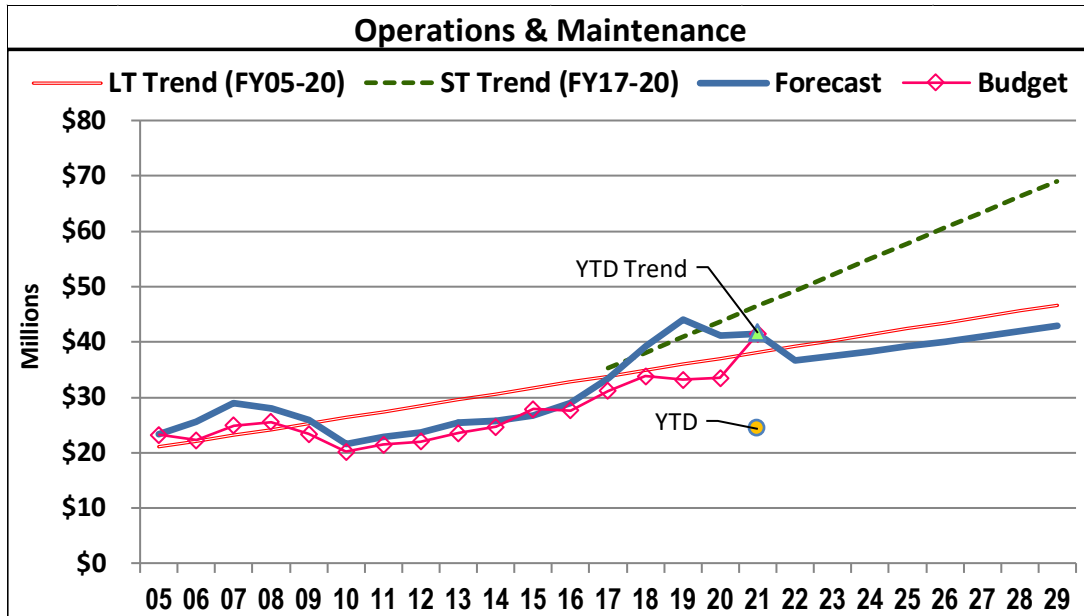
Personnel Expense Forecast



- Overtime in month 7 already near annual budget, forecast follows long-term trend
- Retiree medical forecast approaches long-term trend; need actuarial forecast for refined estimate
- Total personnel meets YTD trend & budget for FY21, then follows short-term trend

Note that uneven cash flow means YTD Trend not always indicative of final amount for FY21

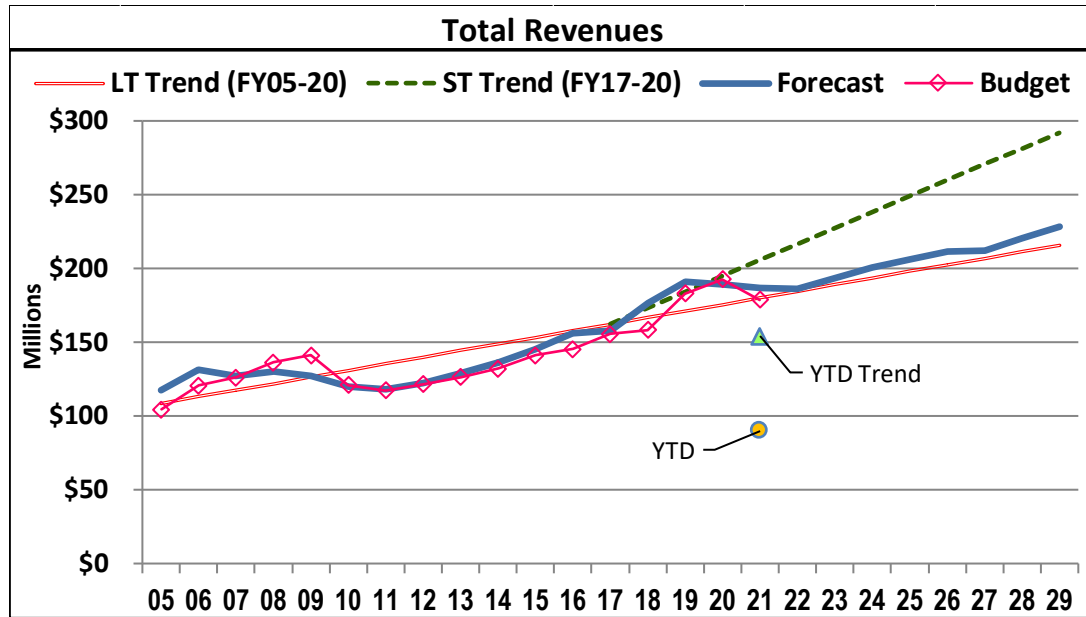
Non-Personnel Expense Forecast



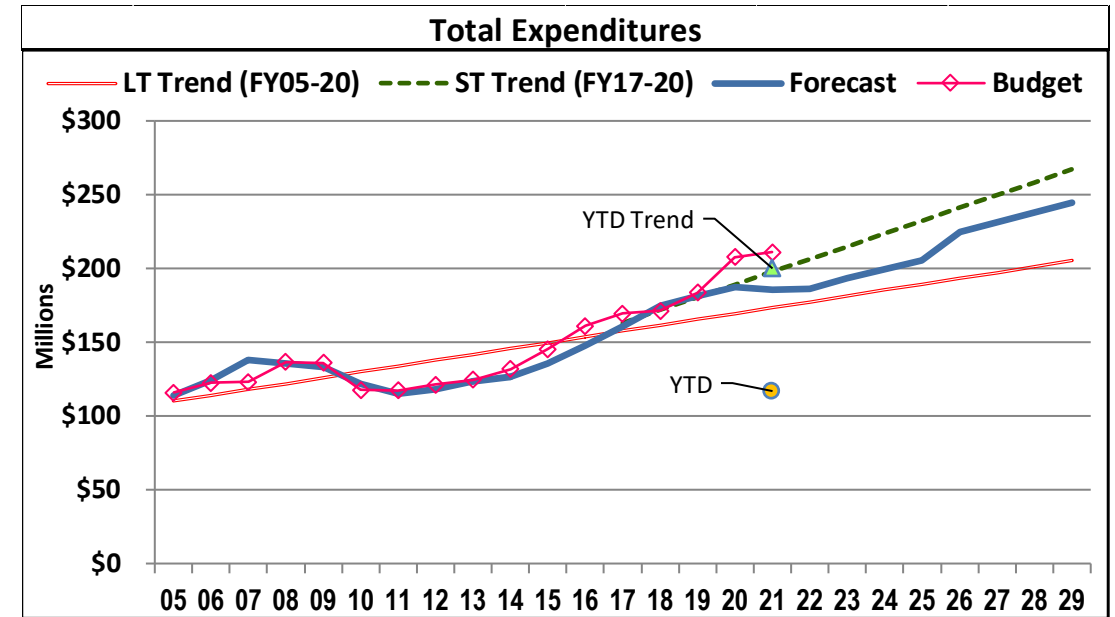
- O&M forecast at YTD trend & budget for FY21, parallels long-term trend thereafter
- Capital total is average of past 8 years (FY22 is \$4M CIP, \$2M project budget, \$100K capital outlay); CIP budget in recent years includes carryover for existing projects
- Transfers Out grow starting in FY25 with GF backfilling for assumed loss of Measure N tax

Note that uneven cash flow means YTD Trend not always indicative of final amount for FY21

Summary of Total Revenues & Expense



- Total revenue follows long-term trend starting in FY22
- FY22 lower than FY21 due to one-time CARES Act and FEMA revenues received

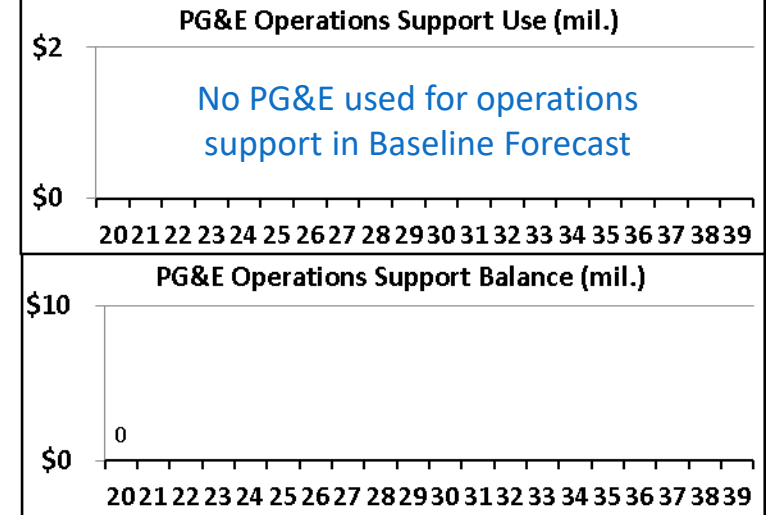
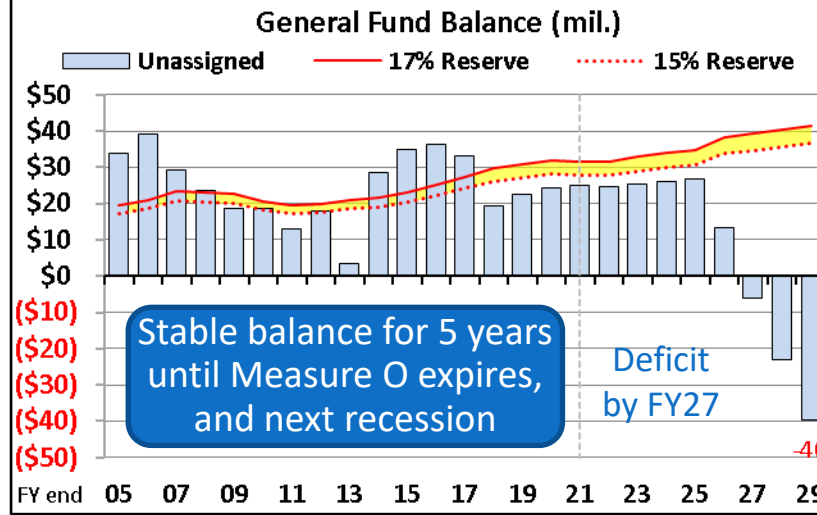
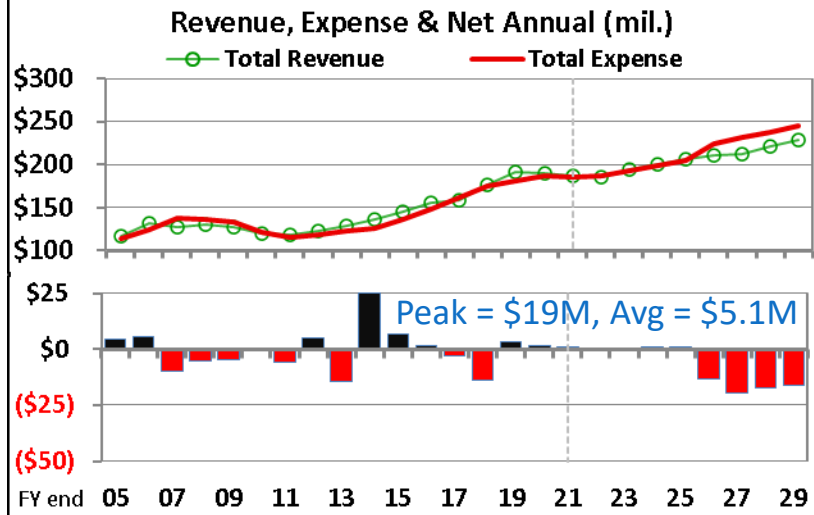


- Total expense YTD trend for FY21 is on the short-term trend line; projections thereafter split the two trends, and include the 5-year freeze of certain positions

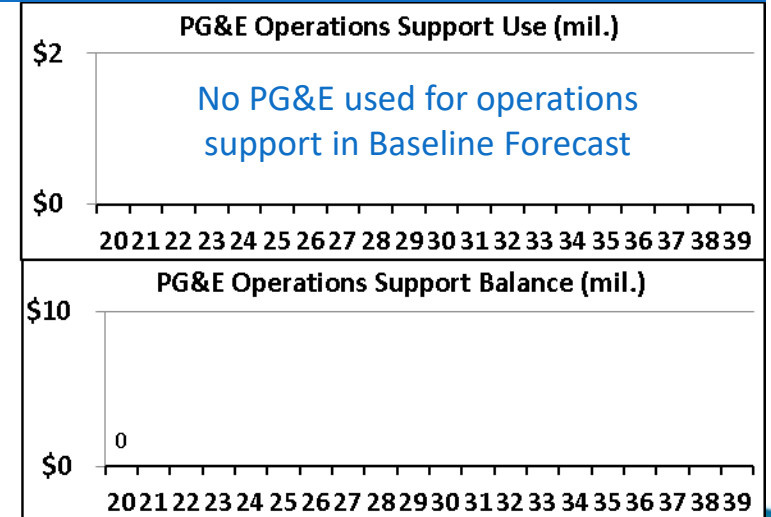
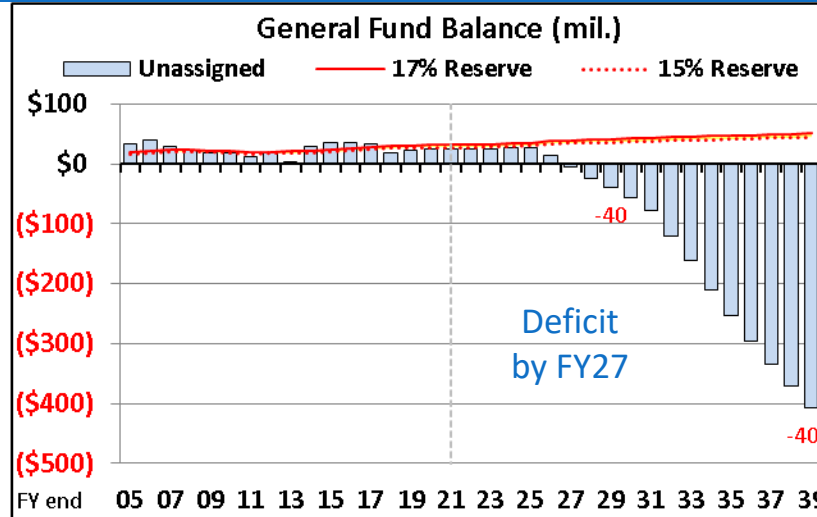
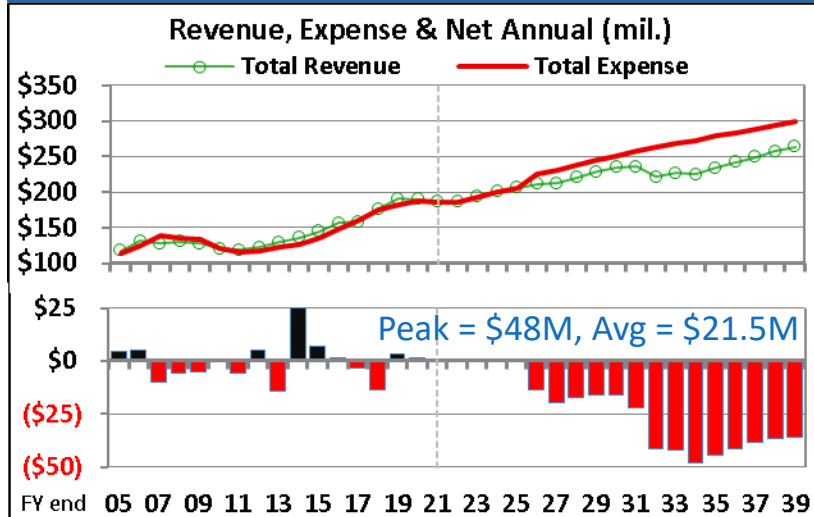
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Baseline Forecast

10-Year Forecast



20-Year Forecast

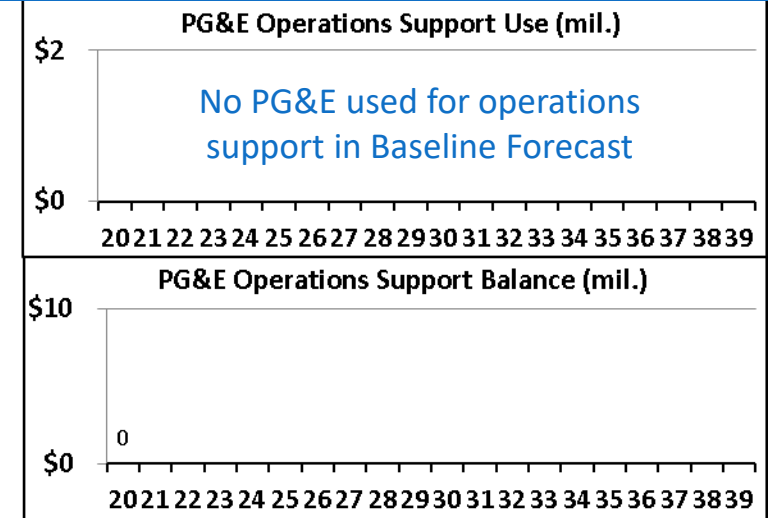
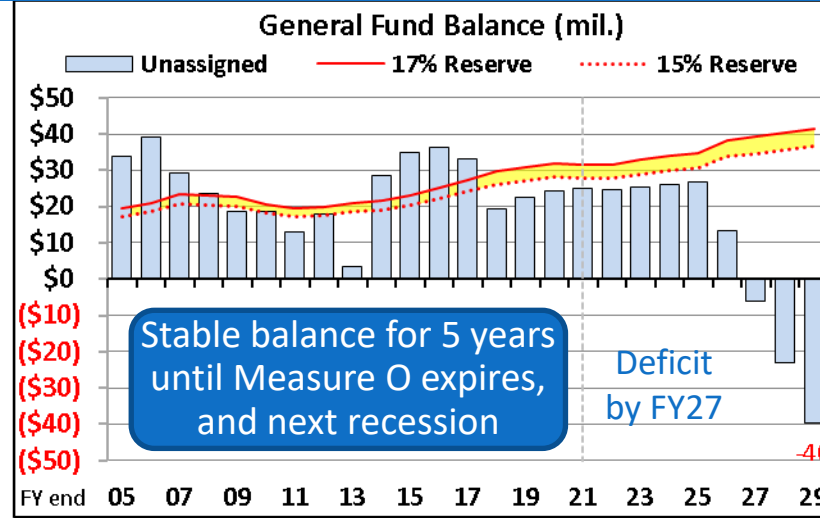
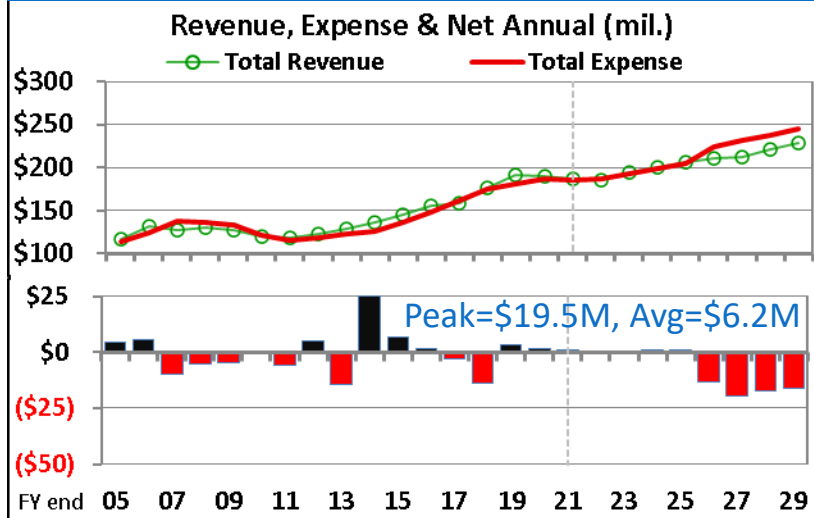


Major Forecast Variables

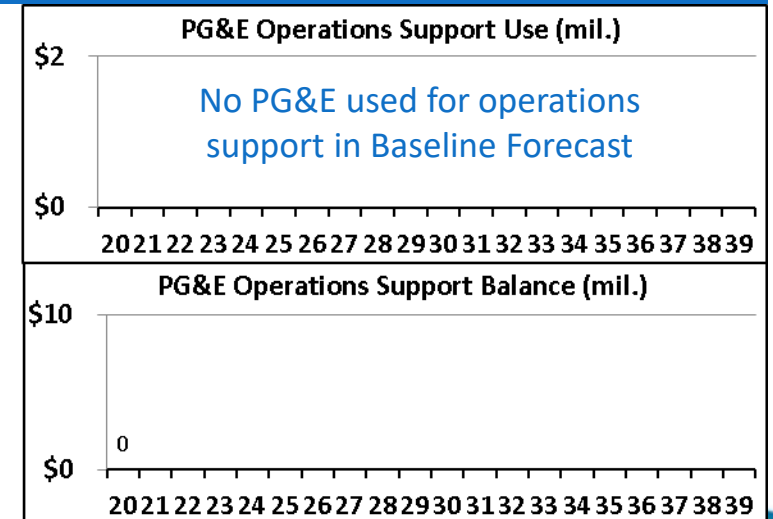
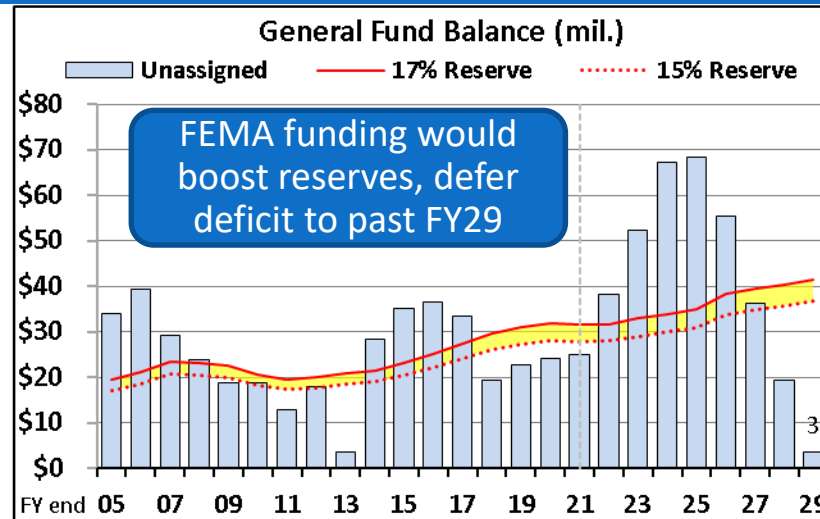
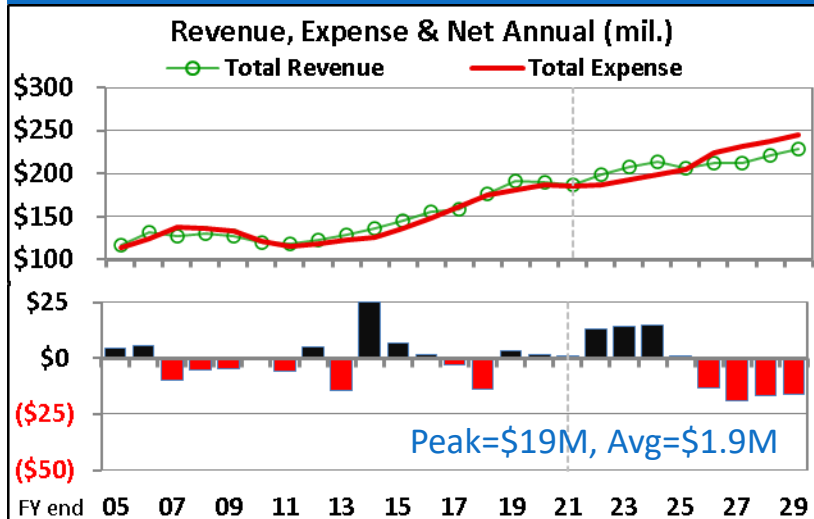
- **Vacancies**
 - Will be most likely reason for lower expense in near-term
- **Pay & Benefits**
 - Wage adjustments are subject to the meet & confer process, and if wage adjustments exceed the 2% in the forecast, these costs will compound into future years
- **Pension Costs**
 - Forecast assumes more conservative than CalPERS's current 7% returns and discount rate, but this is a realistic outcome; returns will be higher or lower every year, making pension forecast volatile in any event
- **Growth Related to Workload Increases**
 - Additions of 2 FTE and \$4M for CIP annually are budget decisions, and can be eliminated at City discretion, but are recommended for long-term sustainability of City services and infrastructure
- **One-Time Funding**
 - ARPA adds \$36.4M; GF benefits only to extent funds used to offset revenue losses or budgeted expenses
 - FEMA reimbursements not included in the forecast could be \$40.7M over the next few years, depending on the timing and level of payments approved; not all would go to the GF

Impact of FEMA Reimbursements

10-Year Forecast Excluding FEMA



10-Year Forecast Including \$40.7M Over Next 3 Years



Alternative Scenarios for Meeting Reserve Goal Using 20-Year Forecasts, Excluding FEMA Reimbursements



Summary of Alternative Scenarios

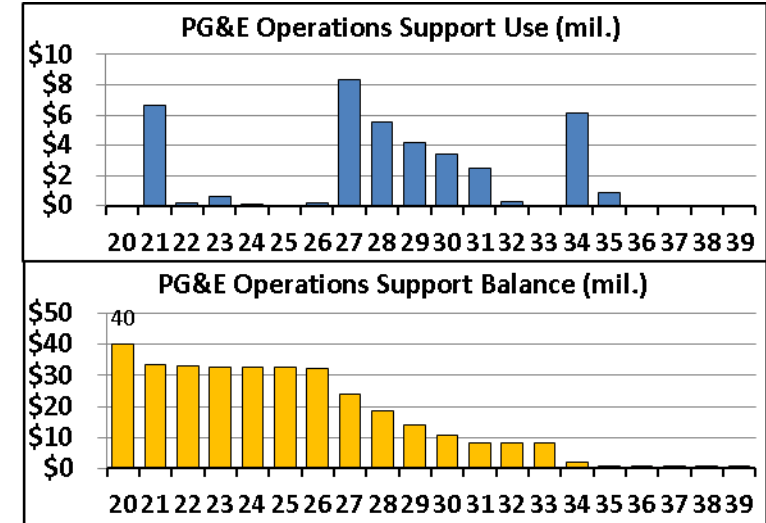
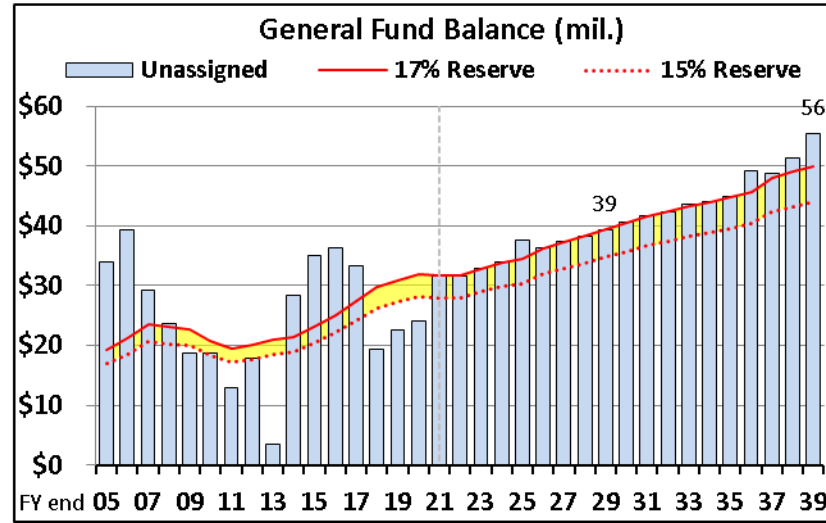
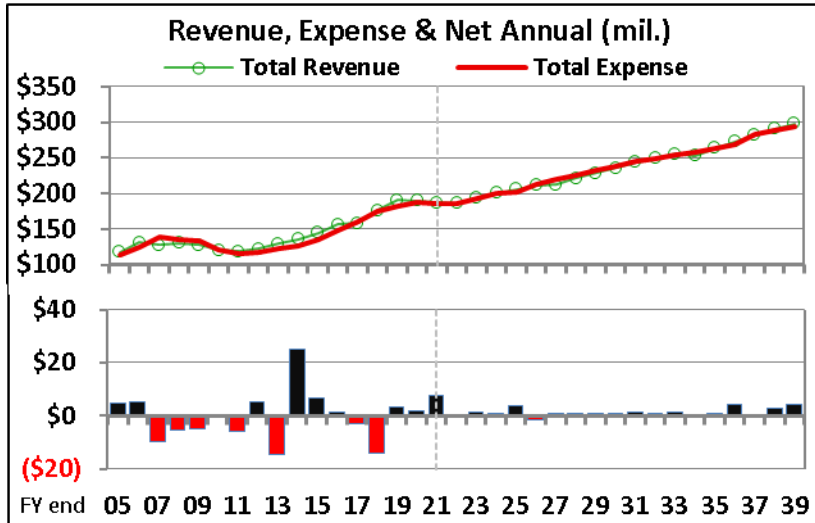
Budget Action	Baseline Forecast	Scenario A	Scenario B	Scenario C	Scenario D	Scenario E	Scenario F
PG&E settlement to support GF operations*	none	\$40M	\$40M	\$40M	none	none	none
FY22 Expense=FY20 for O&M/PT/OT	yes	yes	yes	no	yes	yes	no
Frozen FTE in effect	5 years	5 years	5 years	10 years	10 years	10 years	10 years
2 FTE growth/year	yes	yes	yes	no	no	no	no
Measures O (safety) and Q (general) sales taxes (requires voter approval)	O & Q both expire	O & Q renewed	O expires, Q renewed	O & Q renewed	O & Q renewed	O expires, Q renewed	O expires, Q renewed
Ongoing expense <u>decreases</u> (and/or revenue increases)**	none	none	\$11M in FY26	\$5M in FY27	none	\$12M in FY36	\$7M in FY22 & \$11M in FY25, 2yr phase
Ongoing expense <u>increases</u>	none	\$10M in FY37	\$6M in FY38	\$8M in FY37	\$12M in FY36	\$11M in FY36	\$10M in FY36

*drawdown as needed to maintain GF reserve goal

**Will be reduced to extent FEMA funding is received

Scenario A

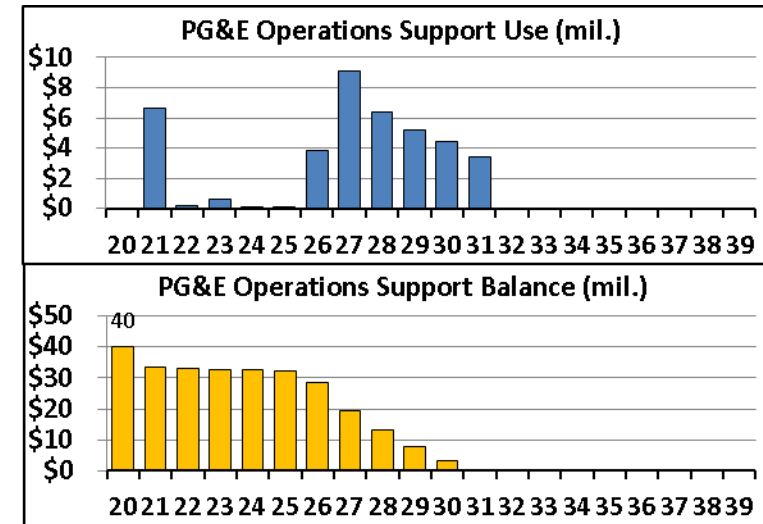
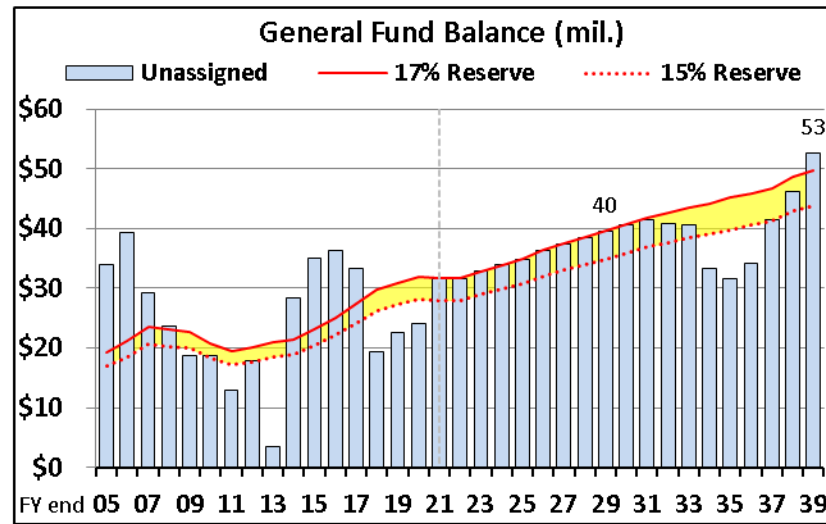
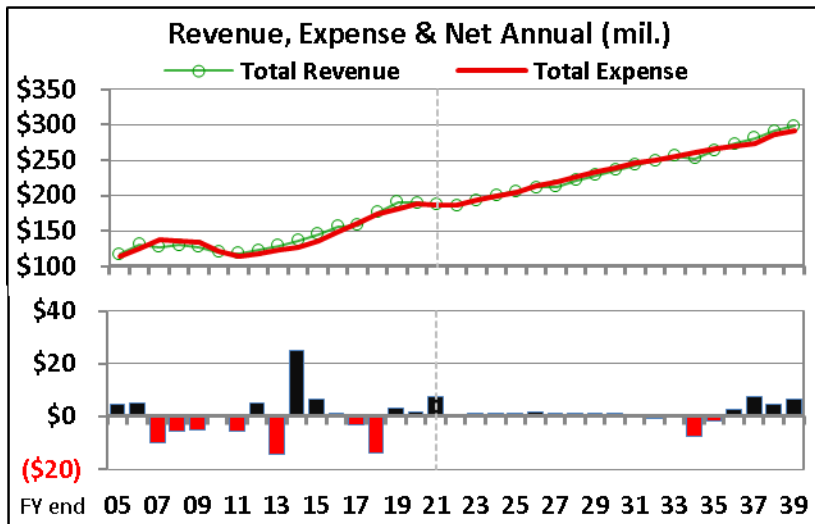
\$40M PG&E, FY22 Exp=FY20, Renew Both Taxes



- Revised Assumptions from Baseline:
 - Measure O (public safety) and Measure Q (general tax) are both renewed
- Budget actions required:
 - \$40M of PG&E settlement set aside to support operations, drawn down as needed to maintain GF reserve goal until funds are depleted
 - \$10M in ongoing expense increase starting FY37 (restored/augmented services)

Scenario B

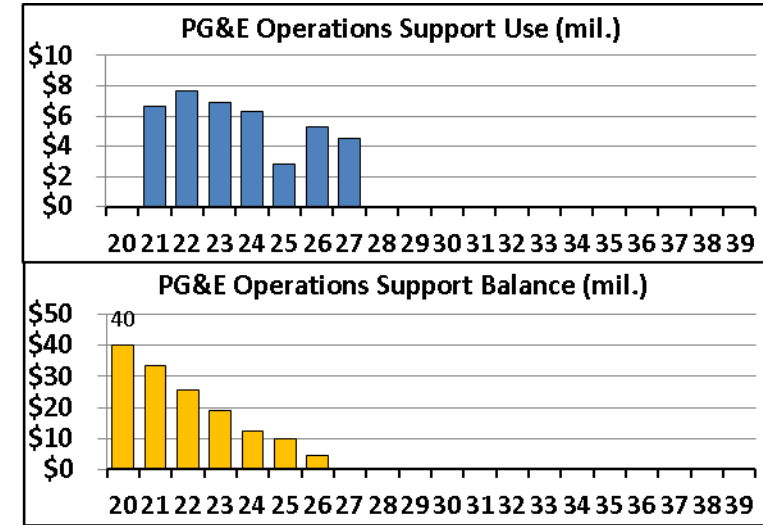
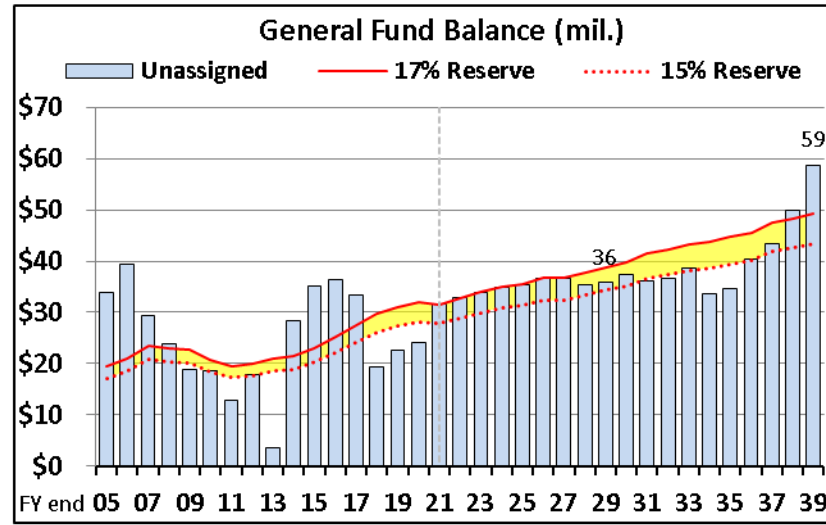
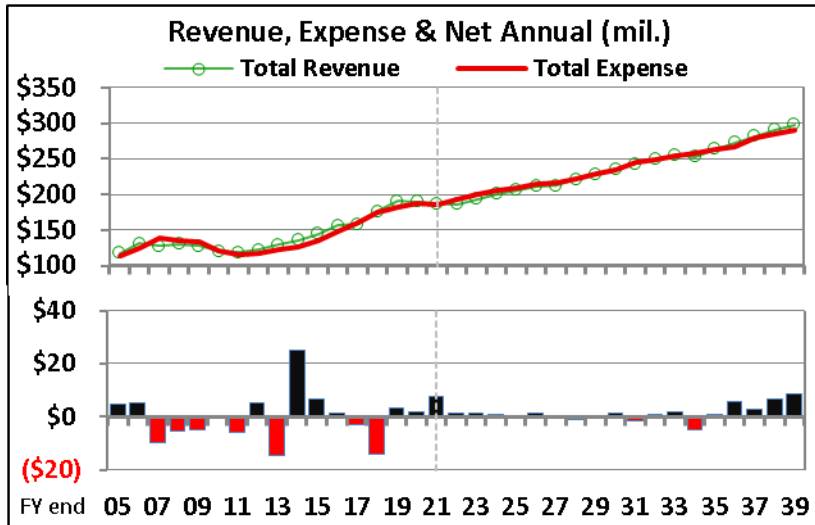
\$40M PG&E, FY22 Exp=FY20, Renew Q/Lose O



- Revised Assumptions from Baseline:
 - Measure Q (general tax) is renewed, but Measure O (public safety) expires
- Budget actions required:
 - \$40M of PG&E settlement set aside to support operations, drawn down as needed to maintain GF reserve goal until funds are depleted
 - \$11M in ongoing budget reduction (or revenue increase) starting FY26, and \$6M in ongoing expense increase starting FY38 (restoration of services)

Scenario C

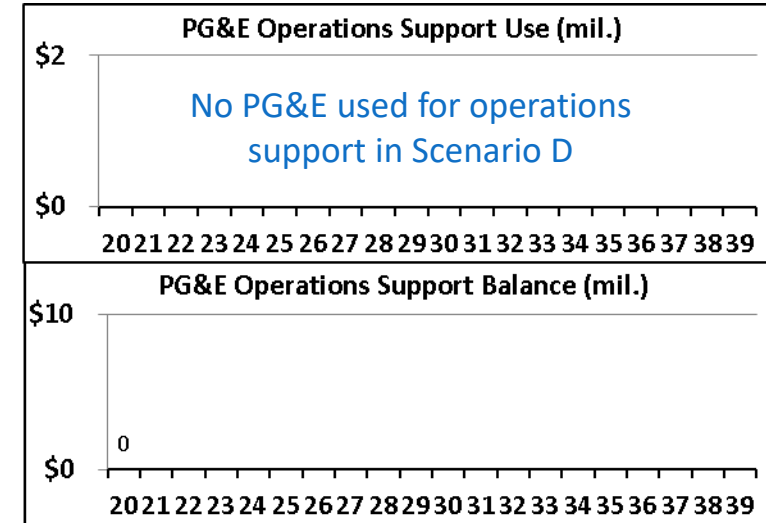
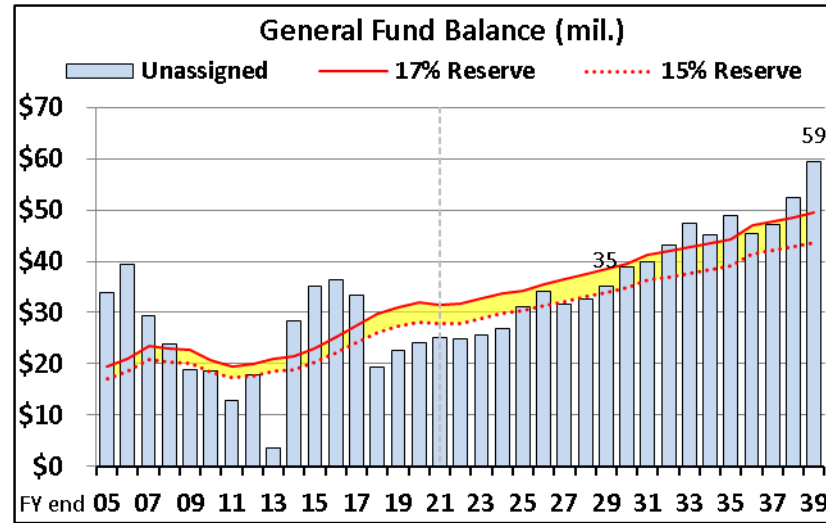
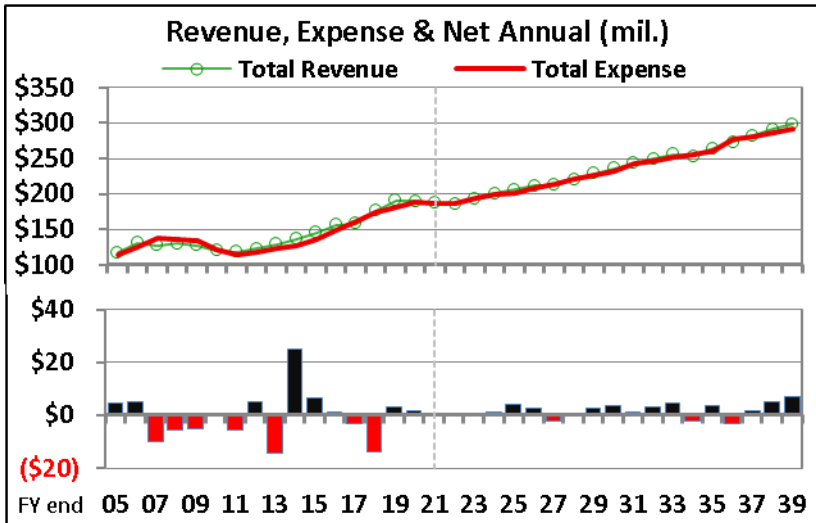
\$40M PG&E, No FY22 Exp=FY20, Both Taxes Renewed



- Revised Assumptions from Baseline:
 - FY22 O&M/PT/OT expense not held to FY20 levels
 - Measure O (public safety) and Measure Q (general tax) are both renewed
- Budget actions required:
 - \$40M of PG&E settlement set aside to support operations, drawn down as needed to maintain GF reserve goal until funds are depleted
 - Frozen FTE for 10 years and no annual FTE growth
 - \$5M in ongoing budget reduction and/or revenue increase starting FY27, and \$8M in ongoing expense increase starting FY37 (restoration/augmentation of services)

Scenario D

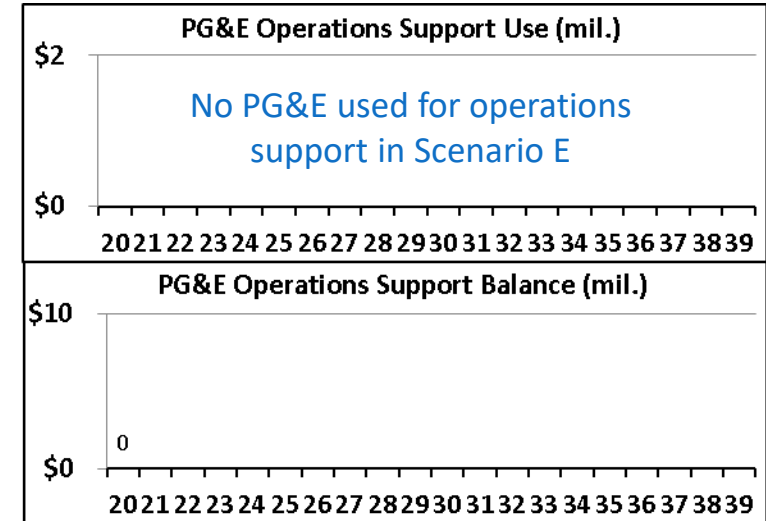
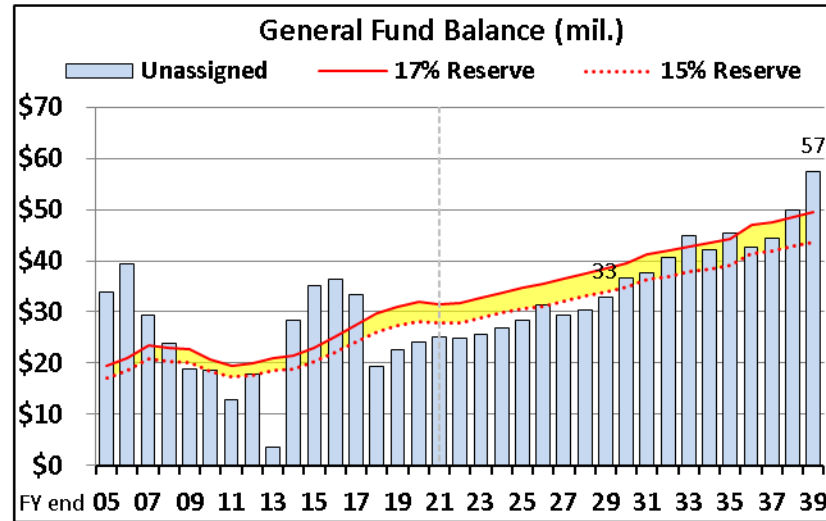
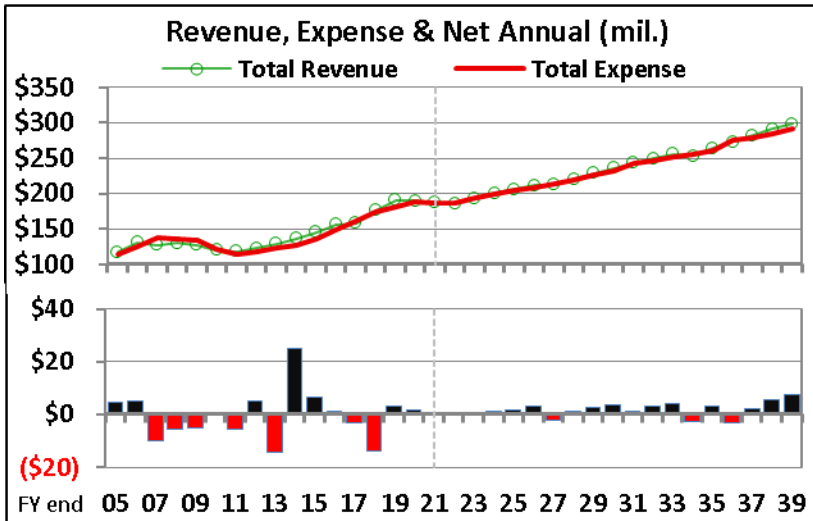
No PG&E, FY22 Exp=FY20, Both Taxes Renewed



- Revised Assumptions from Baseline:
 - Measure O (public safety) and Measure Q (general tax) are both renewed
- Budget Actions Required:
 - Frozen FTE for 10 years and no annual FTE growth
 - \$12M in ongoing budget increase starting FY36 (augmented services)

Scenario E

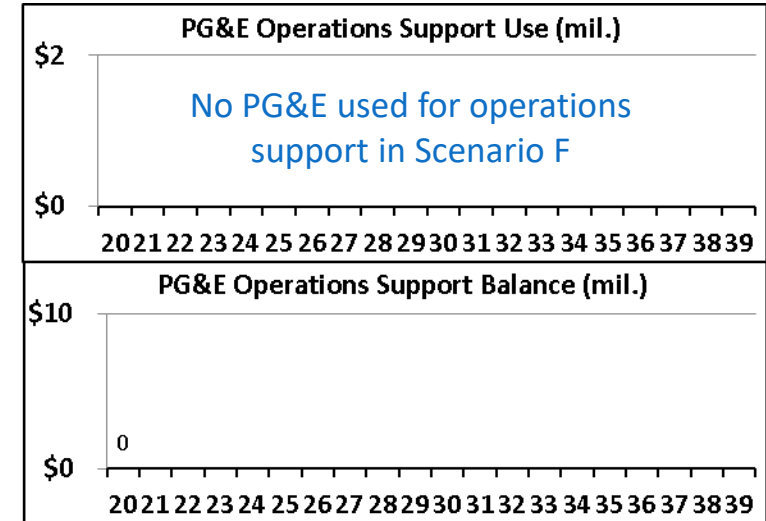
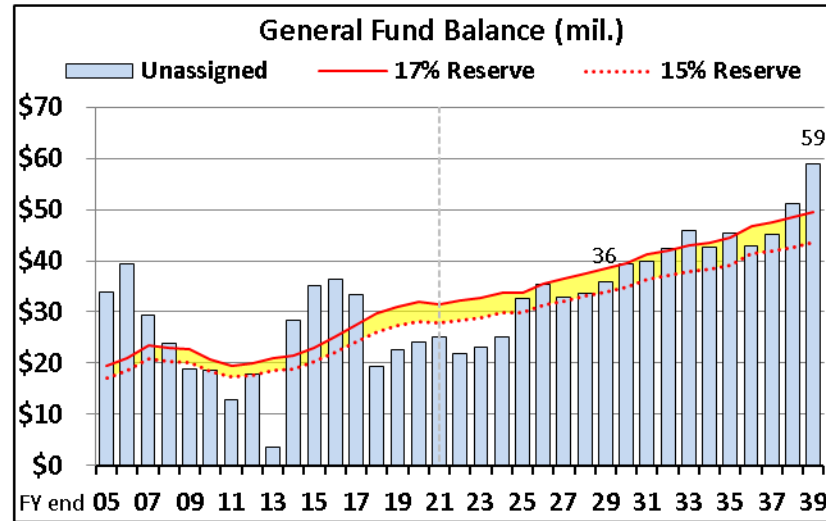
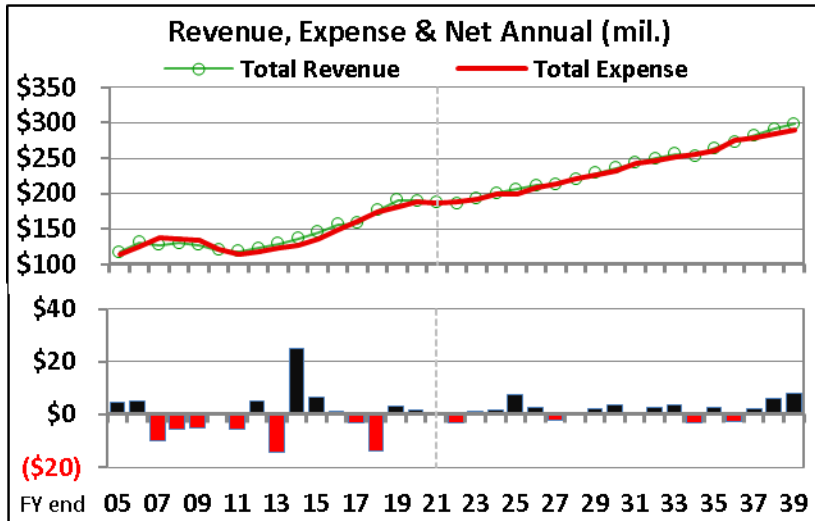
No PG&E, FY22 Exp=FY20, Keep Q/Lose O



- Revised Assumptions from Baseline:
 - Measure Q (general tax) renewed, but Measure O (public safety) expires
- Actions Required:
 - Frozen FTE for 10 years and no annual FTE growth
 - \$12M in ongoing budget decrease starts FY26, and \$11M in ongoing expense increase starts FY36 (restoration of services)

Scenario F

No PG&E, No FY22=FY20, Keep Q/Lose O



- Revised Assumptions from Baseline:
 - FY22 O&M/PT/OT expense not held to FY20 levels
 - Measure Q (general tax) renewed, but Measure O (public safety) expires
- Actions Required:
 - Frozen FTE for 10 years and no annual FTE growth
 - \$7M in ongoing expense reduction starting FY22 & \$11M additional expense reduction starting FY25 (both phased over 2 years), and \$10M in ongoing expense increase starting FY36 (restoration of services)



Thank You!

Questions?



Contact Information:

Bob Leland

rleland@managementpartners.com

530-219-5812