



DATE: December 5, 2018
TO: Council Budget and Finance Committee
FROM: Director of Finance
SUBJECT: Update on General Fund Long Range Financial Model

RECOMMENDATION

That the Council Budget and Finance Committee receives an update and provides comments on the City's General Fund Long Range Financial Model.

SUMMARY

This report provides an update of the City's General Fund Long Range Financial Model (Financial Forecast Model). Staff requests that the Committee reviews and provides feedback prior to presenting this update to the City Council in January 2019. This update includes the latest revenue and expenditure projections and shows the impact to the City's long-term financial outlook.

BACKGROUND

For several years, the City utilized a General Fund Ten-Year Plan Model previously developed in-house as a tool to understand the long-range financial implications of policy decisions. In early 2017, the City engaged Management Partners to develop a more comprehensive and agile financial model, which was presented to Council during a special work session in October 2017¹. That October presentation included a demonstration of the capabilities of the Financial Forecast Model, as well as Council participation in discussing a variety of hypothetical scenarios to illustrate the long-term fiscal implications. This Financial Forecast Model was again used to simulate the long-term financial forecast using the latest revenue and expenditure figures.

DISCUSSION

The proposed FY 2019 Operating Budget projected the use of \$5.5 million from the General Fund reserve to present a balanced budget. Implementation of one-time expenditure reduction and cost saving measures reduced the projected use of General Fund reserve by \$2.5 million. At the time of budget adoption, the Financial Forecast Model projected the

¹ City of Hayward City Council Meeting on October 17, 2017
<https://hayward.legistar.com/MeetingDetail.aspx?ID=568550&GUID=6855A6D8-73F8-422D-8F2B-D5E1FE091927&Options=info&Search=>

City's General Fund reserve levels would fall below the City's 20% policy level to 11.4% in FY 2020, and depletion of the City's General Fund reserve by FY 2022. Table 1 provides a summary of the previous FY 2019 Operating Budget General Fund projected fund balance through FY 2023, for background.

TABLE 1: FY 2019 GENERAL FUND FIVE-YEAR FORECAST ENDING FUND BALANCE PROJECTIONS (JULY 2018 PROJECTIONS)

GENERAL FUND FORECAST - FY 2019					
ADOPTED <i>in thousands</i>	FY 2019 Year 1	FY 2020 Year 2	FY 2021 Year 3	FY 2022 Year 4	FY 2023 Year 5
Revenues	\$159,748	\$162,798	\$166,525	\$172,813	\$179,454
Expenditures	162,790	170,074	179,193	188,805	194,780
Net Change in Reserve - Surplus / (Shortfall)	(3,042)	(7,276)	(12,668)	(15,991)	(15,326)
Beginning Balance	\$29,713	\$26,670	\$19,394	\$6,726	(\$9,265)
Net Change in Reserve - Surplus / (Shortfall)	(3,042)	(7,276)	(12,668)	(15,991)	(15,326)
Ending Balance	\$26,670	\$19,394	\$6,726	(\$9,265)	(\$24,591)
Target to maintain 20% GF Reserves in Operating Expenses	\$32,558	\$34,015	\$35,839	\$37,761	\$38,956
General Fund Reserve Level as % of Total Expenses	16.4%	11.4%	3.8%	-4.9%	-12.6%
Amount Above or (Below) Target 20%	(\$5,888)	(\$14,621)	(\$29,113)	(\$47,026)	(\$63,547)
Percentage Above or (Below) Target 20%	(18.1%)	(43.0%)	(81.2%)	(124.5%)	(163.1%)

Projected Impacts of Recent Changes to Financial Forecast:

In October 2017, City Council held a Fiscal Sustainability work session, where staff unveiled the updated Financial Forecast Model, and Council discussed various options in four categories to address the City's structural budget deficit, which included (1) revenue generating options, (2) cost shifting options, (3) expenditure control options, and (4) changes in provision of services that Council could implement to assist in closing the City's long-term structural budget gap. During that discussion, Council directed staff to primarily focus on one of the revenue generating options (placing a measure on the ballot to increase the City's Real Property Transfer Tax (RPTT)) and on continuing to partner with employees on cost sharing opportunities. On July 17, 2018, Council approved a resolution calling for a municipal election for an increase to the RPTT.² In November 2018, voters passed Measure T from its original rate of \$4.50 per \$1,000 of property value to \$8.50 per \$1,000 of property value. The RPTT is expected to generate an additional \$7.2 million annually, for total annual General Fund revenue of approximately \$15 million.

² City of Hayward City Council Meeting on July 17, 2018
<https://hayward.legistar.com/LegislationDetail.aspx?ID=3553050&GUID=5504B467-533C-4C23-9243-448F969C92EB&Options=&Search=>

In addition to the successful passage of Measure T this fall, the Council adopted labor agreements with all of employee labor groups resulting in equitable benefits for both the City and employees.

Table 2 below provides an update to the General Fund Five-Year Forecast that includes the adopted employee labor agreements and the increase in projected RPTT revenue, as well as, the latest projected revenue and expenditure calculations.

TABLE 2: DECEMBER 2018 UPDATED GENERAL FUND FIVE-YEAR PROJECTIONS

GENERAL FUND FORECAST - UPDATED <i>in thousands</i>	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
	Year 1	Year 2	Year 3	Year 4	Year 5
Revenues	\$164,357	\$169,796	\$173,160	\$179,325	\$185,446
Expenditures	163,805	168,098	178,634	188,298	194,336
Net Change in Reserve - Surplus / (Shortfall)	552	1,698	(5,474)	(8,974)	(8,890)
Beginning Balance	\$32,385	\$32,937	\$34,635	\$29,161	\$20,187
<i>Net Change in Reserve - Surplus / (Shortfall)</i>	552	1,698	(5,474)	(8,974)	(8,890)
Ending Balance	\$32,937	\$34,635	\$29,161	\$20,187	\$11,297
Target to maintain 20% GF Reserves in Operating Expenses	\$32,761	\$33,620	\$35,727	\$37,660	\$38,867
General Fund Reserve Level as % of Total Expenses	20.1%	20.6%	16.3%	10.7%	5.8%
Amount Above or (Below) Target 20%	\$176	\$1,015	(6,566)	(17,472)	(27,570)
Percentage Above or (Below) Target 20%	0.5%	3.0%	(18.4%)	(46.4%)	(70.9%)

Long-Term Financial Outlook

The updated Financial Forecast Model (Attachment II) provides a view of the City’s long-term outlook. A continued challenge is rising CalPERS rates and unfunded accrued liabilities that have a significant impact on the projected expenditures in future years.

Attachment III highlights key revenue and expenditure assumptions included in this updated Financial Forecast Model. For example, revenue projections in this updated five-year forecast include the additional \$7.2 million RPTT revenue anticipated with the passage of Measure T. The sales tax projections include a contraction in two fiscal years, one for the known departure of a top tax payer and the other for a recession scenario. The change for this revenue source ranges -2.2% to 4.4% in the fiscal years presented. For years after FY 2023, sales tax is calculated at 2.5% growth annually for subsequent years. The Cannabis Tax revenue is projected at \$750K in FY 2019, \$1M in FY 2020, \$1.25M in FY 2021 and 2% growth in subsequent years. Property tax projections include an assumed recession in 2020. Annual growth ranges from 0.03% in the projected recession year to 5.25%. Please note that the projected property tax revenue does not include increases to property tax expected from future developments. As the Committee is aware, in an effort to address the challenges

surrounding affordable housing and homelessness on October 2, 2018, the City Council authorized the appropriation and allocation of \$28.6 million of the City’s Affordable Housing Funds.³ In addition, the development of the former Route 238 CalTrans properties will also result in additional property tax revenues. These policy decisions are expected to have a positive impact on the property tax revenue projections moving forward. Staff does plan to adjust the expected property tax revenue from future developments when the timing of these property transactions and value of the properties become clearer. It is expected that these future developments will increase the property tax revenue projections significantly.

Please also note that these revenue projections do not include one-time revenue, such as expected proceeds from future 238 property sales or the prior period Utility Users Tax payments, both of which are being held in separate accounts.

Staff is currently updating the City’s cost allocation plan and completing a Fleet Utilization study to analyze the need for equipment and vehicles currently owned and maintained by the City. These two efforts are expected to reduce expenses slightly.

Proposed strategies and updates to the Financial Forecast Model will be provided to Council on an ongoing basis for their continued policy leadership in helping to ensure fiscal sustainability for the City while ensuring the highest level of service availability to the Hayward community.

Unfunded liabilities

TABLE 3: SUMMARY OF BENEFIT LIABILITIES (IN MILLIONS)

<i>(in millions)</i>	Actuarial Valuation Date	Accrued Liability	Value of Assets	Funded Ratio	Unfunded Liability (1)	Unfunded Ratio
CalPERS Police Safety Plan	6/30/2017	\$ 374.86	\$ 229.86	61.3%	\$ 145.00	38.7%
CalPERS Fire Safety Plan	6/30/2017	\$ 288.16	\$ 179.08	62.1%	\$ 109.07	37.9%
CalPERS Miscellaneous Plan	6/30/2017	\$ 440.24	\$ 290.12	65.9%	\$ 149.95	34.1%
Total Cal PERS		\$ 1,103.26	\$ 699.06	63.1%	\$ 404.02	36.9%
OPEB - Retiree Medical Police Officers	6/30/2017	\$ 33.64	\$ 2.02	6.0%	\$ 31.62	94.0%
OPEB - Retiree Medical Fightfigters	6/30/2017	\$ 15.24	\$ 0.92	6.0%	\$ 14.32	94.0%
OPEB - Retiree Medical Miscellaneous	6/30/2017	\$ 20.21	\$ 1.21	6.0%	\$ 19.00	94.0%
Total OPEB-Retiree Medical		\$ 69.09	\$ 4.15	6.0%	\$ 64.94	94.0%
Workers' Compensation	6/30/2017	\$ 16.64	\$ 8.63	51.9%	\$ 8.01	48.1%
Accrued Leave Payouts (1)	6/30/2017	7.89	0	0.0%	\$ 7.89	100%
TOTAL		\$ 1,196.87	\$ 711.84	59.5%	\$ 484.85	40.5%

As shown in Table 3 above, the City still has significant unfunded benefit liabilities that need to be addressed. The CalPERS retirement total unfunded accrued liability (UAL) is \$404 million, or 63.1% funded status. The City also faces challenges in funding its Other Post-

³ City of Hayward City Council Meeting on October 2, 2018
<https://hayward.legistar.com/LegislationDetail.aspx?ID=3690553&GUID=0F826B7B-CA03-44E1-AB73-06C8790A7D69&Options=&Search=>

Employment Benefits (OPEB) liabilities. According to the most recent actuarial report (for plan year 2017), the City's unfunded OPEB liability is \$64.9 million, or 6% funded status.

To address these challenges, staff is exploring ways to reduce the UAL to ultimately improve the City's balance sheet, decrease long-term payments, and increase benefit security for current and former employees. The options being explored are: 1) additional discretionary payments through a loan from an enterprise fund; 2) establishing a Section 115 Irrevocable Pension Trust; or 3) participation in CalPERS "Fresh Start"- re-amortizing the current UAL over a shorter period of time. On September 19, 2018, staff presented these options to the Council Budget and Finance Committee and will present to Council recommendations at a future date. For purposes of this discussion, staff did not include any potential savings as a result of the four funding options listed above until these are presented to Council and one is selected.

ECONOMIC IMPACT

There is no economic impact associated with this report as it is informational only.

FISCAL IMPACT

There is no fiscal impact associated with this report; however, staff will continue to refine and update the General Fund Long Range Financial Model as economic factors change.

PUBLIC CONTACT

The agenda for this item was posted in compliance with the California Brown Act.

NEXT STEPS

Staff will continue to update the Financial Forecast Model and provide regular updates to the Council as other strategies and options to help reduce the City's structural deficit are identified.

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