CITY OF YUBA CITY
STAFF REPORT

Date: February 18, 2020

To: Honorable Mayor & Members of the City Council

From: Finance/IT Department

Presentation By: Spencer Morrison, Finance Director

Summary

Subject: Financial Report for the Six Months Ended December 31, 2019

Recommendation: Note and File the December 31, 2019 Financial Report

Fiscal Impact: Informational item only

Purpose:

To provide City Council with a summary of the first six months of FY 2019-20 revenue and expenditures of the City's major operating funds.

Background:

Finance provides periodic Financial Reports to City Council to keep you apprised of the City's financial activities along with trends in revenues and expenditures.

Analysis:

The attached December 31, 2019 Financial Report has been prepared for City Council review.

Fiscal Impact:

Informational item only

Alternatives:

Not applicable

Recommendation:

Staff recommends that the City Council note and file the December 31, 2019 Financial Report.

Attachment:

1. Financial Report

Prepared By:

/s/ Spencer Morrison
Spencer Morrison
Finance Director

Submitted By:

/s/ Michael Rock
Michael Rock
City Manager

Reviewed By:

City Attorney

SLC by email

ATTACHMENT 1

FY 2019-20 Financial Report

For the Six Months Ending 12/31/19

February 18, 2020

OVERVIEW

As of July 1, 2019, the general fund had an unassigned fund balance of $6,836,022 as stated in the City's annual independent audit, the Comprehensive Annual Financial Report (also known as the CAFR). This amount meets the City's Fiscal Policy requirement of a 15% general fund reserve. The 15% Fiscal Policy minimum reserve level is a recommended best practice and is supported by the Government Finance Officers Association of the United States and Canada (GFOA). GFOA recommends that cities maintain a general fund reserve equal to 2 to 4 months of operating expenses. Yuba City has 1.9 months of operating expenses in reserve as of June 30, 2019.

It is difficult to determine when the next downturn in the economy will occur, the only certainty is that the next recession-causing event, such as the housing bubble, will eventually come. With this in mind, it is important for the City to maintain its 15% general fund reserve; ensure that both the water and wastewater enterprise fund revenues are sufficient to cover operating, debt service and infrastructure replacement costs; plan for infrastructure renewal and replacement; and to continue monitoring fiscal performance regularly.

Rather than lowering it further, the CalPERS Board voted in December, 2017, to maintain the lowered discount rate at 7.0% with the three-year phase-in over a period of several years. The CalPERS Board had been evaluating the possibility of lowering it even further. This would have had severe fiscal impacts on the City. As it is, the fiscal impact of a 7.0% discount rate is significant. The most recent projections based upon the June 30, 2018 CalPERS actuarial reports project that retirement costs will grow from $8.8 million in FY 19/20 to $11.3 million by FY 25/26. It will be a challenge for revenues to grow sufficiently to keep pace with this mandatory expenditure. This does not take into consideration growth in other expenditure categories or needs of the community such as infrastructure renewal and replacement, employee cost of living increases, or any other budget priorities. The City Council will be carefully prioritizing allocation of resources to cover increases in employee compensation and benefit costs, allocate funding towards unfunded pension liabilities, fund unmet facility and infrastructure needs related to parks and roads, cover the cost of providing police services to all City residents, and address deferred maintenance and improvements throughout the City. On a positive note, the City has a Pension Stabilization Trust Fund with $2.9 million dollars ($2.4 million after the February, 2020 payment) available that can be utilized to buy down a portion of future pension cost increases.

The City's financial model projects a balanced budget in the five-year financial forecast. Notably, the assumptions included in this model include positive revenue growth and very conservative expenditure growth. Staff retained the services of an independent financial consultant to, in essence, evaluate inputs of an economic downturn on the City's fiscal projections. This information was provided to City Council at the December 17, 2019 council meeting.

Finance evaluates employee vacancies on a quarterly basis to monitor the anticipated savings to the budget based on those vacancies. During the first half of the fiscal year, the vacancy rate remains near 11%. Finance anticipates that the City will end the fiscal year with a surplus larger than the $0.4 million contained in the original adopted budget due to normal employee turnover throughout the year. Notably, vacancy savings are usually partially offset by increased overtime for shift coverage in both the Police and Fire departments.

This report is prepared on a cash basis; therefore it describes the timing of cash flows as it relates to the City's revenues and expenditures.

Beginning Balances. The beginning fund and working capital balances presented in this report are final year end amounts from the previous year audit report and will not change.

Adjusted Budgets. The revenue projections and expenditure budgets shown in this report include adjustments for encumbrances, carryovers, and any supplemental revenue and expenditure appropriations made by the Council as of December 31, 2019.

GENERAL FUND

General Fund Financial Condition. With 50% of the year complete, General Fund revenues are at 24.8% of projections and expenditures are at exactly 46.9%.

General Fund

	Budget	YTD Actual	Percent
Balance, Start of Year	$ 6,836,022	$ 6,836,022	-
Revenues	45,764,420	11,370,399	24.8%
Expenditures	(46,693,230)	(21,891,081)	46.9%
Balance	**$ 5,907,212**	**$ (3,684,660)**	**-**

The budgeted expenditures shown above include encumbrance carryovers from FY 18/19 of $511,665. Encumbrance carryovers are outstanding purchase orders as of June 30th. Encumbrances are liquidated and paid from the beginning fund balance as prior year budget monies are used to pay for them (as opposed to current year revenues). In addition, budgeted expenditures include $641,666 added for public safety grant funded programs, $500,000 for the supplemental unfunded accrued liability (UAL) payment to CalPERS, $50,000 for professional services contracts and $36,700 for staffing changes in the Fire Department. Additionally, $837,700 was added for approved bargaining unit contracts, mixed between one-time and ongoing funds.

In the YTD Actual shown above, the ending fund balance is negative as of the end of the second quarter. The negative balance is an indication of the typical cash flow pattern for the general fund. This happens because general fund expenditures for payroll and vendor payments are incurred evenly throughout the fiscal year whereas our largest revenue sources of sales tax and property tax lag in receipt compared to the timing of when they are earned. Property tax is received in two large payments in February and May when property taxes are received from Sutter County. This is the City's second largest revenue source for the general fund and when it is received only two times per year, it causes the cash flows (and therefore fund balance) to go deficit until the first installment is received. The City receives two advance payments and a true-up payment for each quarter of sales tax revenue. However, there is a lag in time as to the end of the quarter of revenues and when the cash is received. For example, the advance payments for the Christmas quarter (October through December revenues) are received by the City in January and February with the true-up payment in mid-March. When additional sales tax is received from the State and property taxes are received from Sutter County, the negative fund balance will reverse and fund balance will end the fiscal year with a positive balance. The negative fund balance as of December 31, 2019, was compared to that of December 31, 2018, and the City is approximately $797,361 worse off (a larger negative) in 2019. Upon analyzing this change, half the difference is related to a decrease in sales tax receipts compared to the same months of the previous year. A large portion of the decrease is likely related to the ongoing software conversion issues the California Department of Tax and Fee Administration (CDTFA) is experiencing.

Revenues.

The City's top ten revenues account for approximately 94.5% of total General Fund revenues. As such, they provide a very good summary of our revenue position. Key revenues are performing as projected based on payment schedules and past trends for half way through the fiscal year. More detailed information is noted below.

Top Ten Revenues		Budget		YTD Actual	% Received
Property Taxes	$	13,742,700	$	-	0.0%
Sales Tax		14,125,000		5,215,248	36.9%
Business Licenses		1,084,300		85,508	7.9%
Franchise Fees		1,810,200		332,868	18.4%
Hotel/Motel Surcharge		1,274,600		361,506	28.4%
Building Permits		1,050,000		569,598	54.2%
Police Special Services		193,000		41,554	21.5%
CSA "G" Fire Contract		820,800		0	0.0%
Recreation Fees		904,100		310,701	34.4%
Operating Transfers		8,306,800		3,822,900	46.0%
Total	**$**	**43,311,500**	**$**	**10,739,883**	**24.8%**

▪ **Property Tax.** The first apportionment of FY 19/20 taxes will not occur until February, 2020. The FY 19/20 adopted budget projected a 4.3% increase in property taxes. Based upon the final assessed valuation reports from the Sutter County Auditor-Controller's Office, general fund secured and unsecured assessed values increased by 5.97%. Property tax revenues are expected to exceed budget projections by approximately $134,000 at the end of the fiscal year.

Five of the largest components of the change in assessed values are as follows:

- Properties were adjusted by a CPI factor of 2.0% between FY 18/19 and FY 19/20 (an increase of $65.0 million in assessed valuations), this accounted for 23% of all growth experienced in the City.
- Residential increased by 5.3% ($199.9 million).
- Unsecured increased by 5.78%.
- Industrial increased by 1.75% ($3.9 million).
- Commercial values increased 7.48% ($72.0 million) largely due to sales which added $42.0 million.

The City received the benefit of $287.4 million in assessed value increases during FY 19/20 attributable to an increase in market value compared to prior years when there had been decreases in assessed values pursuant to Proposition 8. The increase in Proposition 8 values included $36.5 million in residential (affecting a total of 1,733 residential parcels) and $10.8 million in non-residential. An additional 1,483 parcels remain under Proposition 8 status, with a total potential recapture of $98.6 million. The City will see these increases in assessed value translate to increases in property tax revenues if real estate sales prices continue to escalate. The potential recapture is eliminated when and if a home under Proposition 8 status is sold for less than the recapture value.

- **Sales Tax.** When the FY 19/20 revenue projections were developed, sales tax was projected to increase 2.0%. The most recent quarterly sales tax results decreased 9.6% on a cash basis and increased 0.5% on an adjusted basis (July - September, 2019 sales) and increased 14.5% on a cash basis and increased 2.0% on an adjusted basis (April - June, 2018). Sales tax continues to be unpredictable and volatile, but had shown overall increases until the CDTFA upgraded their software system and fell behind in processing incoming taxpayer returns in the third and fourth quarters of FY 17/18. Sales tax revenue remains volatile and we expect this to continue at least through FY 19/20. Finance expects sales tax revenues from new automobile sales to level off and subsequently decline, which we saw in the 2nd quarter of FY 19/20.

There is a lengthy lag time between the time that sales occur and when the City receives the information regarding the sales tax revenues in order to compare the data to the same quarter of the previous year. As of the date of this report, Finance staff is still waiting for the Christmas quarter results which will be available in mid-March, 2020. Finance continues to be cautiously optimistic because overall sales tax revenues have increased in 11 of the past 15 quarters on a cash basis (all 15 quarters have been positive on an adjusted basis).

As stated, the revenue data for the October through December quarter sales has not yet been released by the CDTFA. The revenue shown here represents the first quarter payments received from the State and advance payments received towards the second quarter revenues.

▪ **Business Licenses**. Business licenses are renewed in January of each year; therefore most of the revenues from business licenses are received during the third quarter of the fiscal year.

▪ **Franchise Fees**. The City receives franchise fees from PG&E, Recology, AT&T and Comcast; the fees are based upon a percentage of their revenues. The receipts for the second quarter of the fiscal year are not received until the end of January and PG&E pays theirs annually in April. Therefore, we would not expect franchise fees to be near the 50% mark during the first two quarters of the fiscal year.

- **Hotel/Motel Surcharge.** Surcharge revenues for the first quarter are included in the amount shown, but second quarter receipts are not due or paid until the end of January and are therefore not included here.

- **Construction Permit Fees.** Building Permits are right on track with budget expectations with 54.2% received half way through the fiscal year. This is an indication of the continued activity in construction and development.

- **CSA "G" Fire Contract.** The City receives these funds for fire services to the unincorporated area that was formerly served by the Walton Fire Protection District. Since revenues are property tax based, the first apportionment will be received in February, 2020.

- **Recreation Fees.** At 34.4% of budgeted revenues, service fees from recreation programs appear to be lower than anticipated halfway through the year. This is typical due to the seasonal nature of the programs offered.

- **Operating Transfers.** The General Fund receives reimbursement for operating costs associated with support services provided to the water and wastewater utilities as well as other fund transfers. Transfers are on track with budgetary expectations.

Expenditures. Operating costs are all within budgetary expectations with the exception of the Fire Department and City Attorney as summarized below. It appears that some departments exceed the 50% of budget expended half-way through the year, but this overage is attributable to the pre-payment of the City's unfunded actuarial liability for CalPERS that was made in July for the entire fiscal year in order to save interest charges from CalPERS. Additionally, the Fire Department appears to have the largest percent in excess of 50% of their budget expended. In their case, it is due to retirements and increased overtime costs related to injuries. Should the state send reimbursements for any strike team claims, the Fire Department's budget will be increased to account for the increase in overtime costs when the strike team revenue reimbursements are received from the State of California.

Expenditures	Budget	YTD Actual	% Expended
City Council	$ 120,498	$ 54,571	45.3%
City Attorney	250,000	185,921	74.4%
City Manager	737,453	342,647	46.5%
Finance/IT	3,008,739	1,343,829	44.7%
City Treasurer/City Clerk	59,550	9,262	15.6%
Human Resources	1,160,492	459,449	39.6%
Development Services	1,657,231	882,857	53.3%
Public Works	5,371,679	2,199,504	40.9%
Police	16,612,972	7,602,852	45.8%
Fire	11,967,670	6,384,884	53.4%
Animal Control Services	954,069	471,387	49.4%
Economic Development	343,807	62,451	18.2%
Contingency	110,965	17,314	15.6%
Non-Departmental Misc.	387,476	149,258	38.5%
Community Services	3,950,629	1,724,896	43.7%
Total General Fund	**$ 46,693,230**	**$ 21,891,081**	**46.9%**

ENTERPRISE FUNDS

The following summarizes year-to-date revenues, expenditures, and changes in current assets net of current liabilities for the enterprise funds. Depreciation is included as a footnote in the budget and is therefore not included below.

Water Fund

	Budget	YTD Actual	Percent
Balance, Start of Year	$ 21,894,220	$ 21,894,220	-
Revenues			
Operating	16,244,000	8,247,270	50.8%
Capital	577,700	242,634	42.0%
SRF Surcharge	689,800	324,047	47.0%
Grants	62,874	(31,618)	-50.3%
Sub-Total Revenues	17,574,374	8,782,334	50.0%
Expenditures			
Operating Programs	(10,366,774)	(4,415,473)	42.6%
Capital Equipment	(49,700)	(46,512)	93.6%
Debt Service	(3,483,806)	(1,146,233)	32.9%
Sub-Total Expenditures	(13,900,280)	(5,608,218)	40.3%
Balance	**$ 25,568,315**	**$ 25,068,337**	**-**
CIP Projects	**$ 14,485,460**	**$ 569,675**	**3.9%**

Water service revenue increases (10.0%) were last approved by City Council in June, 2018, in order to cover the operating cost of the Water utility, debt service costs and infrastructure renewal and replacement projects. Below is a summary of the total service revenues billed from July to September and then from October to December, comparing the total revenues billed, the consumption and the percentage of revenues billed changes from 2018 to 2019:

July 2018	July 2019	August 2018	August 2019	September 2018	September 2019
$ 1,553,002	$ 1,403,706	$ 1,666,133	$ 1,567,645	$ 1,610,081	$ 1,547,073
655,564	560,918	719,866	667,061	710,190	687,488
	-9.6%		-5.9%		-3.9%

October 2018	October 2019	November 2018	November 2019	December 2018	December 2019
$ 1,452,307	$ 1,395,977	$ 1,365,482	$ 1,335,544	$ 1,177,385	$ 1,188,438
585,922	560,645	487,741	508,370	396,516	407,803
	-3.9%		-2.2%		0.9%

Operating revenues in the water fund are at 50.8% of the amount budgeted and are on track to meet budget projections at the end of the fiscal year. At first glance halfway through the year, it would appear that we should have only approximately 50.0% of budgeted revenues as of December, 2019. However, this is somewhat misleading because the highest billing months occur in July, August and September. For comparison, in fiscal year 17/18, as of December 31st, operating revenues were at 58.6% of the amount budgeted, and at year end were at 110.4% of the total amount budgeted was received. Therefore, since operating revenues are at 50.8% mid-way through the year, it is likely that by the end of the fiscal year, operating revenues may be less than budgeted. Water consumption is heavily weather dependent. If we see an early and warm spring, customer consumption and therefore water revenues tend to increase. The reverse is also true.

Achieving targeted revenues is a fiscal priority as the City's bond covenants require the City to raise rates in order to continue meeting a 1.2% debt coverage ratio. Capital connection fee revenues are at 42.0% of the amount budgeted mid-way through the fiscal year.

Operating expenditures are at 42.6% at the mid-point of the fiscal year. There is savings in salaries and benefits due to 5.85 full-time equivalent vacant positions in the water utility, in addition to budgetary savings to date in operation and maintenance accounts.

Debt service expenditures are less than half for the first two quarters for both Water and Wastewater as they include only an interest payment because the payment that includes both principal and interest is not due until June 1st of each year.

Wastewater Fund

	Budget	YTD Actual	Percent
Balance, Start of Year	$ 22,231,813	$ 22,231,813	-
Revenues			
Operating	16,565,200	8,304,703	50.1%
Capital	693,200	114,347	16.5%
Sub-Total Revenues	17,258,400	8,419,050	48.8%
Expenditures			
Operating Programs	(12,092,234)	(5,166,703)	42.7%
Capital Equipment	(243,530)	(113,381)	46.6%
Debt Service	(3,353,257)	(988,674)	29.5%
Sub-Total Expenditures	(15,689,021)	(6,268,758)	40.0%
Balance	**$ 23,801,192**	**$ 24,382,105**	**-**
CIP Projects	**$ 12,019,434**	**$ 7,982,734**	**66.4%**

Wastewater operating revenues are at 50.1% of the amount budgeted and capital revenues are at 16.5%. Revenues through December 31st are closely on track with expectations. The most recent rate change happened on July 1, 2018; the City implemented an eight percent (8.0%) increase in wastewater service charges.

Wastewater operating expenses are slightly lower than anticipated halfway through the year at only 42.7% of budget. There is savings in salaries and benefits due to 5.35 full-time equivalent vacant positions in the wastewater utility, in addition to budgetary savings to date in operation and maintenance accounts. The most significant area where there are budgetary savings are in professional services. However, a significant amount of the unspent budget is encumbered (purchase orders have been issued but the actual expense has not yet been incurred).

Finance staff tracks and accounts for the operating funds and capital connection fee funds for both the Water and Wastewater operations separately. Debt service payments are allocated to the capital connection fee funds based upon how the debt proceeds were used to finance projects at the time the debt was issued. Repayments for bond principal and interest are charged accordingly. Public Works/Utilities advises Finance when a Water or Wastewater project is approved how much should be paid from operating funds versus capital connection fee funds. In recent years with the decline in development activities, City Council has been advised that at some point Finance staff will draw the connection fee fund reserves into a negative position in order to meet our bond covenant commitments and make debt service payments. Council concurred that this was an acceptable practice as long as Finance kept track of the funds separately, and replenished the cash flows as development activities increased. As of December 31, 2019, Finance reviewed the available cash balance in both the Water and Wastewater connection fee/capital funds and provides the following update:

		Water		**Wastewater**
Cash available @ 12/31/19	$	2,498,865	$	817,646
Annual D/S from connection fees	$	1,499,162	$	708,031
# of years of coverage available		1.67		1.15

This table indicates that the Water connection fee fund cash balance is deficit as of December 31, 2019. The table compares the amount of cash reserves available in each of the capital connection fee accounts to the total annual debt service currently being allocated to and paid from capital connection fees. Those two amounts are then compared to calculate a ratio of how long, in terms of years, the City will be able to pay debt service without drawing capital connection fee funds into a deficit position. Measured in terms of overage and shortage in dollars, the water fund currently has sufficient funds to meet the 1.20% requirement for debt coverage. However, the wastewater fund would need to provide $32 thousand of cash in order to meet the 1.20% requirement:

		Water		**Wastewater**
Required Ratio		1.2		1.2
Cash Reqd. to be at 1.2 Coverage	$	1,798,995	$	849,637
Cash Over(Short) @ 12/31/19	$	699,870	$	(31,991)

This calculation does not consider amounts used from capital connection fees for future capital projects or future revenues received; it is a snapshot in time of where the funds stand as of December 31, 2019. The water fund is in a better position to cover debt service than the wastewater fund, but without additional development to increase revenues, both will need to cover debt service from the operating funds as has been anticipated.