



**AGENDA ITEM
CITY COUNCIL MEETING DATE – MAY 5, 2020
BUSINESS ITEMS**

TO : City Manager

FROM : Finance Director

SUBJECT : **GENERAL FUND FINANCIAL FORECAST IN RESPONSE TO COVID-19 PANDEMIC**

EXECUTIVE SUMMARY:

Staff has reviewed the City’s General Fund budget and created an initial financial forecast in response to the novel coronavirus (COVID-19) and its estimated impacts on the City’s local economy. The forecast focuses primarily on the City’s revenues and incorporates information sourced from economic experts as well as financial trend analysis based on the City’s economic history. Due to the quick-changing nature of information and action from both the State and City in response to COVID-19, staff prepared this forecast to present a potential scenario based on the best available information available at the time it was prepared. The purpose of the forecast is to review and discuss the potential budgetary impacts, with the intent to adjust the budget when staff returns with a mid-cycle budget update in June 2020. There is no action or budget adjustment associated with this report.

RECOMMENDATION:

Move to accept the General Fund Financial Forecast for Fiscal Years 2019-2021 as shown in Attachment 1.

BUDGET INFORMATION:

This financial forecast provides an initial update to the General Fund revenues and expenses due to the sudden impact of the coronavirus pandemic on local revenues. At this time, the projected shortfall for the General Fund for 2019-20 is approximately \$2.5 million and for 2020-21 the projected shortfall is approximately \$8.5 million.

BACKGROUND:

GLOBAL PANDEMIC AND POTENTIAL RECESSION

In late 2019, the novel coronavirus (COVID-19) began to spread in China and throughout the world, causing a global pandemic. In response, as an effort to slow down the spread of the virus, national governments issued travel bans, prohibited mass assembly, and many local governments issued shelter-at-home orders, only allowing essential businesses to operate. On March 15, 2020,

Benicia City Manager issued a proclamation of local emergency in response to the COVID-19. The restriction of movement and commerce has affected the global economy and many experts and economists speculate that the long-term economic impact may result in an economic recession.

The swift reaction by consumers and businesses to the outbreak of COVID-19 in the United States has caused a massive decrease in spending on certain goods and services. The national and statewide response, combined with the uncertainty of how long the presence of the virus will disrupt the U.S. economy, has made forecasting local government revenues particularly challenging. On March 27, 2020, President Trump signed a \$2 trillion economic stimulus bill, the Coronavirus Aid, Relief, and Economic Security (CARES) Act, the largest such package in U.S. history. Although the stimulus package was released very quickly, the depth and duration of the negative economic impacts are unknown. Currently, the CARES Act does not provide direct assistance to local governments under 500,000 in population. Since then, additional stimulus funds have been released, but given the scale of the business disruption during the shelter-at-home order, the beneficial impact of the funds is not yet known.

To develop this updated forecast, City staff relied on the economic and financial recommendations provided by the Government Finance Officers Association (GFOA), financial consultants, HdL Companies, League of California Cities webinars and written materials, and articles written by many renowned economists and other experts.

Dr. Robert Eyler, the Sonoma State Professor who advises Solano Economic Development Corporation (EDC) and with whom the City of Benicia has contracted for assistance, described the expected financial impact as being equal to a combination of the Great Recession and 9/11 on various business sectors.

The assumptions relied upon for developing the COVID-19 forecast also assume a slow reopening of business activity and social interaction as described by Governor Newsom in late April and no second shelter-at-home order later this year or during the first half of next year.

GENERAL FUND FINANCIAL FORECAST: REVENUE

The two-year financial forecast included as Attachment 1 presents projected revenue in the General Fund at approximately \$41.1 million in FY 2019-2020 (a decrease of \$4.9 million from the revised budget presented at the March 3, 2020 meeting) and approximately \$36.6 million in FY 2020-2021. For the forecast revenue assumptions, the City applied guidance from various sources (including HdL Companies, the League of California Cities' financial expert Michael Coleman's and Dr. Eyler's outlooks), and in other cases applied only the fiscal trend experienced in the Great Recession to the forecast time period. The largest projected decrease comes in the form of sales tax revenue, but most other revenue categories are also negatively impacted. The following highlights the basis for the underlying assumptions for each of the City's revenue categories.

- ❖ **Property Taxes** – Although Governor Gavin Newsom made allowances for the postponement of property tax payment, Solano County did not defer the due date for

property taxes. Therefore, the City estimates receiving the budgeted property tax revenue for the remainder of this fiscal year, FY 2019-2020, but as the housing market slows down, the City anticipates a 4% decrease in the amount of approximately \$749,000 for FY 2020-2021.

- ❖ **Sales Tax** – The impact of this pandemic on sales tax to local revenues is immediate. The closure of non-essential businesses and the State’s deferral and loan program will impact the amount received by the City for the last two quarters of FY 2019-2020. The City applied the effects of the sales tax deferrals and the predicted industry losses by quarter for the remainder of FY 2019-2020 for a loss of approximately \$2 million. Also, the City applied the compounded effect of the Great Recession as well as the impact of 9/11 for an additional 24% decrease of approximately \$1.1 million for FY 2020-2021.
- ❖ **Measure C Sales Tax** – Similar to sales tax mentioned above, the impact of our local add-on sales tax to local revenues is immediate. HdL, the City’s sales tax consultant, assisted with estimates to include the deferrals and the predicted industry losses by the quarter for the remainder of FY 2019-2020 for a loss of \$1.8 million. Once again, the City applied the compounded effect of the Great Recession as well as the impact of 9/11 for an additional 24% decrease of approximately \$1 million for FY 2020-2021.
- ❖ **Utility User Tax (UUT)** – The FY 2019-2020 updated amount is approximately \$200,000 less than the revised mid-year budget based on expected payments. As more people continue to shift from cable plans to streaming services, the City estimates a 5% decrease in the amount of \$220,000 in FY 2020-2021.
- ❖ **Franchise Fee** – The changes to franchise fees for solid waste, gas, electric, and Valero will be temporary. Franchise fees for Valero is calculated over a 5-year average to eliminate any major spikes in operations such as this pandemic or a planned shut down for maintenance. Based on year-to-date actuals, the City estimates an 11% decrease in the amount of \$235,000 in FY 2019-2020 compared to the current budgeted amount. For FY 2020-2021 the City applied a 7% decrease in the amount of \$130,000 based on the trend the City is experiencing in varying industries, especially with cable.
- ❖ **Transient Occupancy Tax** – The impact to the transient occupancy tax will be felt immediately for the current quarter. Travel and social distancing restrictions will impact the hotels with a decline of 75% to 90% in the current quarter for a total decrease of \$130,000 or a 24% decrease in FY 2019-2020. Following the trend experienced during the Great Recession, the City applied an additional 3% decrease in the amount of \$12,300 in FY 2020-2021.
- ❖ **Business License Tax** – In an attempt to assist local businesses, the City has allowed for a deferral of business license tax until June 15. Due to the deferral, current trend has a decrease of revenues of 32% with a 25% decrease in number of business licenses filed to date compared to this time last year. Staff has reduced the revenues for FY 2019-2020 by 13.5% in the amount of \$74,400. Also, following the trend experienced in the Great Recession, the City applied an 8% decrease in the amount of \$38,000 for FY 2020-2021.
- ❖ **Other Taxes** – Other taxes includes property transfer taxes and cannabis taxes. City revenues will be impacted immediately for the loss of property transfer tax. Based on year-to-date actuals and expected receipts, the City anticipates receiving \$160,000 in FY

2019-2020. The City applied the trend experienced in the Great Recession for a slowing of housing and commercial property market, which is a 60% decrease in the amount of \$96,000 for FY 2020-2021.

- ❖ **Licenses and Permits/Charges for Services** – The impact to licenses/permits and charges for services will be felt immediately. As the stay-at-home order continues due to social distancing concerns, spring recreation programs have been cancelled with refunds for the cancelled programs being processed. Development applications are impacted by economic concerns and processing the plans and permits have slowed considerably due to social distancing concerns. Based on year-to-date actuals, the City estimates receiving \$2.7 million in FY 2019-2020, which is a decrease of approximately \$280,000 or 9%. For FY 2020-2021, another 9% decrease in the amount of \$252,600 is being projected.
- ❖ **Fines and Forfeitures** – City revenues for fines will be impacted within 60 to 120 days. Following the trend experienced in the Great Recession, the City applied a 10% decrease in the amount of \$16,880 for FY 2019-2020 and an 8% decrease in the amount of \$12,200 for FY 2020-2021.
- ❖ **Use of Money and Property** – In March 2020, the Federal Reserve made two emergency interest rate cuts totaling 1.5%, within two weeks, in an attempt to bolster financial markets. Also, the City estimates lower interest earnings due to potential fair market value adjustments. In FY 2019-2020, a decrease of \$371,800 or 41% is anticipated for the change in fair market value adjustment.
- ❖ **Other Agency/Other Revenues** - Based on year-to-date actuals and expected receipts from Valero for the temporary Fire Lieutenant position, administrative fees for business licenses, and the Maritime dispatch contract, the City anticipates receiving \$615,200 in FY 2019-2020 and the budget will remain flat for FY 2020-2021 when the position funding by Valero for the Fire Lieutenant will be updated in June 2020.

Financial losses associated with this unprecedented pandemic have been stark and immediate. The projected General Fund revenues, including transfers in and other previously approved funding sources, totals \$47.5 million for FY 2019-2020 and \$37.2 million for FY 2020-2021.

GENERAL FUND FINANCIAL FORECAST: EXPENDITURES

The two-year financial forecast also presents projected expenditures in the General Fund, including transfers out, at \$50.0 million in FY 2019-2020 and \$45.6 million in FY 2020-21. Although the analysis was primarily focused on the City's revenue sources and potential impacts, staff reviewed two key expenditure categories to provide a better understanding of year-end expenditures.

- ❖ **Salaries and Benefits** – Typically salaries and benefits expenses are budgeted assuming no vacancies—each position is assumed to be filled for the entire fiscal year even though that rarely occurs. For the 2019-20 forecast shown in Attachment 1, staff refined the salaries and benefits expenditures to reflect actual expectations. As a result, salary and benefit cost projections were reduced by \$1 million for Fiscal Year 2019-2020 only.

- ❖ **Expenditure Carryover** – Operating appropriations not spent during the fiscal year may be carried over for specific project purposes, as identified and approved during the City’s fiscal year end process. Staff sent out a preliminary list of open purchase orders for departments to review and determine if there were any purchase orders that could be closed now, as opposed to waiting until year-end. Based on each department’s analysis, staff closed several purchase orders which provided a better estimate of expenditures for FY 2019-2020. The reduction in carryover reduced the year-end expenditure estimate for FY 2019-2020 by approximately \$481,400, primarily related to the contracted services expenditure category.

As shown in Attachment 1, the two-year financial forecast presents an approximate shortfall in the General Fund of \$2.5 million for FY 2019-2020 and \$8.4 million for FY 2020-2021. This forecast is provided as a planning tool to begin navigating these challenges. Staff will incorporate potential solutions and strategies to cover the budgetary shortfall when the mid-cycle update is presented in June 2020. The majority of the “actuals expenditure” data for the two-year forecast was pulled in early April. Staff will have an additional two months of “actuals” data for the mid-cycle presentation, which will provide a more detailed analysis of any budgetary shortfalls.

GENERAL FUND FINANCIAL FORECAST: PRELIMINARY BUDGET BALANCING

The City of Benicia is in the fortunate position of having two reserves that total 20% of the General Fund, one designated for emergencies such as a major earthquake, and the other for economic uncertainty. There is also other funding that has accrued from budget savings in past years referred to as “unassigned fund balance”. On March 3, 2020, the Council assigned some of these funds, but little action has been taken to execute the allocations since then because of the City’s focus on responding to the pandemic. When staff returns in June with a mid-cycle budget adjustment report for 2019-20 and 2020-21, it will include recommendations for bringing both fiscal years into balance by drawing on these sources.

NEXT STEPS:

Return in June 2020 with a mid-cycle budget report for Fiscal Years 2019-21, which will allow refinement of the budgeted revenues in this unprecedented environment. In addition, staff expects to provide regular updates to the City Council on the City’s financial status.

ALTERNATIVE ACTIONS:

Provide alternative direction to staff related to the financial forecast.

General Plan	Goal 1: Creating a sustainable community in Benicia
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Priority Based Budgeting	Strategic City Result Impacted by this Agenda Item
	The City Council and community identified six (6) key “Results” that establish the key goals for which the City of Benicia aspires to achieve with our programs and services. Agenda Items often influence multiple Results, the primary Result impacted by this Agenda Item is (please check one):

	<ul style="list-style-type: none"> <input checked="" type="checkbox"/> Protect Community Health & Safety <input checked="" type="checkbox"/> Maintain & Enhance A High Quality of Life <input type="checkbox"/> Preserve & Enhance Infrastructure <input checked="" type="checkbox"/> Strengthen Economic & Fiscal Conditions <input type="checkbox"/> Protect & Enhance the Environment <input type="checkbox"/> High Performing Government <p style="text-align: center;">City Programs Impacted by This Agenda Item (Top 3):</p> <ol style="list-style-type: none"> 1. Emergency Operation System Management and Emergency Preparedness 2. Financial Planning <p style="text-align: center;">Priority Based Budgeting (PBB) Website:</p> <p>Coming soon in Spring 2020 will be a link to the City of Benicia’s PBB website to learn more about these programs and their costs.</p>
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<p>CEQA Analysis</p>	<p>The proposed amendments are exempt from the California Environmental Quality Act (CEQA) Guidelines Section 15061(b)(3), the “general rule” exemption that states that where it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment, the activity is exempt from CEQA. The City has determined that the proposed changes will not have an impact on the environment and therefore are exempt from CEQA under the general rule.</p>
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ATTACHMENT:

- 1) General Fund Financial Forecast

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