



DEPARTMENT OF FINANCE

April 18, 2011

TO: Honorable Mayor and City Council

FROM: Andy Green
Director of Finance

SUBJECT: Fiscal Year 2012 Budget Development Update

By request of the City Council, staff presents this general overview of the strategies and assumptions used to develop the FY 2012 budget recommendations. Budget documents relating to the operating budget hearings will be delivered to the City Council no later than May 2nd. A more detailed presentation will be provided at the May 9th joint Finance Committee and City Council budget kickoff meeting.

Although the recession of the last few years has technically ended, the City continues to face an ongoing structural deficit in the General Fund. The decline in City revenues appears to have abated, however, many revenue sources, including the three largest to the General Fund (property, sales, and utility user taxes), are not forecast to rebound significantly during FY 2012. Stagnate revenues coupled with cost increases such as PERS pension rates, employee health insurance, and other non-salary driven expenditures are contributing to the challenge of developing an operating budget consistent with the City's goal to eliminate the General Fund structural deficit by FY 2014.

Below is comparative financial information for the General Fund. One of the strategies used in developing the FY 2012 budget was to limit expense budgets to the adopted FY 2011 levels.

General Fund Financial Tread

2009 - 2011

| DESCRIPTION | FY2009 ACTUAL | FY2010 ACTUAL | FY2011 ADOPTED | FY2011 [1] FORECAST |
|---|------------------|------------------|-------------------|------------------------|
| Taxes | \$126,580,018 | \$118,346,236 | \$123,967,000 | \$122,351,084 |
| Other Revenues | \$89,376,311 | \$94,968,190 | \$87,769,757 | \$84,740,931 |
| Total Revenues | \$215,956,329 | \$213,314,426 | \$211,736,757 | \$207,092,015 |
| | | | | |
| Personnel | \$135,160,294 | \$132,052,367 | \$127,917,934 | \$125,362,073 |
| Other Expenses | \$89,943,651 | \$91,368,360 | \$89,361,753 | \$87,533,014 |
| | \$225,103,945 | \$223,420,727 | \$217,279,687 | \$212,895,087 |
| Excess/(Deficiency) of Revenues Over Expenses | (\$9,147,616) | (\$10,106,301) | (\$5,542,930) | (\$5,803,072) |

[1] Based on actual data through February 2011 and will likely change before the end of the fiscal year.

In October 2010, four community budget workshops were conducted to solicit input from City residents, business owners, and other community stakeholders regarding their priorities for public services. The workshops began with an overview of the City's budget and identified the fiscal challenges facing the City in continuing to provide high quality, public services. Participants were invited to ask questions and share comments and suggestions about reductions in City services. As a whole, police and fire services were most valued to the community with libraries trailing close behind. Residents were hard-pressed to identify what services to reduce or give up. The general consensus was to have reductions across the board rather than complete elimination of major services. A detailed, final Citizen Budget Workshop executive summary is attached and is posted on the City's website.

City departments began addressing the FY 2012 budget challenges in November 2010 when the City Manager directed all departments to propose reductions totaling five percent of their FY 2011 budget. These proposed reductions were to be made across all departments and all funds and were reviewed by the City Manager to determine which reductions would be accepted. On March 14, 2011, the City Council approved a mid-year budget revision that eliminated 34.9 FTEs resulting in an annual savings of \$3.9 million. These reductions and the related cost savings are reflected in the FY 2012 Recommended Budget. To ensure that the FY 2012 Recommended Budget stayed within the parameters of the FY 2014 financial plan, departments were instructed to make additional reductions. As a result, the FY 2012 Recommended

Budget includes additional personnel reductions, departmental reorganizations for improved efficiencies, and additional reductions to non-essential spending.

Revenue Assumptions

Though significant reductions to City revenues are not forecast to continue, FY 2012 revenues will remain below pre-recession levels. Tax revenues are forecast to experience modest increases in FY 2012 from the FY 2011 Adopted Budget. These increases, however, will be offset by projected decreases to non-tax revenues including investment income, building licenses and permits, and charges for services.

An additional concern for the FY 2012 budget is the potential impact from reductions in revenues from state and federal governments. While specific details are not finalized, the state and federal governments are expected to propose cost reductions that could negatively impact City revenues and corresponding services, especially in Economic Development, Housing, and Public Health.

Expense Assumptions

City departments were instructed to submit an FY 2012 operating budget that did not exceed their FY 2011 Adopted Budget. To accomplish this objective, departments made additional cost reductions to absorb increases in operating costs, including a significant increase to PERS pension rates and medical insurance. The PERS rate for Miscellaneous Employees in FY 2012 increased nearly 35 percent from the FY 2011 rate. Safety Employees' rate had an increase of 6 percent. The cost of employer provided medical insurance increased between 18 percent and 31 percent from FY 2011 to FY 2012 depending on the labor group and medical plan.

To offset additional labor-related cost increases that are beyond the City's control, departments included additional position reductions that will result in layoffs. These layoffs will impact labor groups, including, but not limited to, AFSCME, PMA, and Non-Represented. Continuing, and possibly expanding, reduced work hour schedules may be necessary to achieve expenditure targets. The City is working closely with representatives of each labor group to examine potential changes to labor agreements that would help mitigate impacts on the City's workforce and result in long-term savings. Where possible, departments have also been instructed to eliminate vacancies and under-filled positions (all positions should be budgeted at the appropriate level). Exploring opportunities to decrease or eliminate the City's portion of the employee PERS contribution as well as non-labor savings are also being explored.

Risks and Unknowns

There are risks that could have significant impacts on the FY 2012 Recommended Budget. Some economists are concerned about the potential for a double dip recession. The City will also be impacted by cost reductions at the state and federal level. There is uncertainty regarding redevelopment agencies and the allocation of tax increment revenues. Additionally, the City continues to struggle to identify sufficient resources for ongoing capital needs. As replacement cycles increase and capital improvements are deferred, there will be an impact on operating costs to maintain assets beyond their useful life. The City has absorbed significant employee benefit increases and it is likely that these costs will continue to grow, particularly those costs relating to unfunded liabilities for pension and retiree medical costs.

While some of these potential risks are a concern for the FY 2012 budget, there are long-term implications that will require close monitoring and frequent updates to financial forecast models.

Budget Adoption Schedule

A series of joint Finance Committee/City Council meetings are being scheduled to review the FY 2012 consolidated operating and capital budget in more detail. These meetings will be conducted in two phases; the first phase will focus on the Capital Improvement Plan (CIP); the second phase will focus on the operating budget. The approval of the combined operating and CIP budget will be recommended to City Council for adoption on June 6, 2011. The budget hearing schedule is attached.

Challenges for FY 2012

Balancing community needs and economic reality will continue to be the challenge in FY 2012. Although revenues appear to be stabilizing, costs beyond the City's control continue to add pressure to how future resources will be allocated. The FY 2014 General Fund financial plan initiated in FY 2009 began the operational changes needed to eliminate the structural deficit by FY 2014. The recommended FY 2012 budget will allow the City to strengthen core infrastructure such as technology, financial systems and processes, and human resources, and realize greater efficiencies and higher service levels despite a reduced workforce. The FY 2012 budget, as recommended, positions the City both organizationally and financially, to take advantage of future opportunities for FY 2015 and beyond. With the City Council's

continued support and staff's diligence in identifying ways to streamline and innovate, and with the cooperation of the City's labor groups, we will be better poised to invest in Pasadena's future.

Attachments:

Attachment 1: Fiscal Year 2012 Recommended Operating Budget Review and 2012-2015 Capital Improvement Program Schedule

Attachment 2: Executive Summary – Citizen Budget Workshops