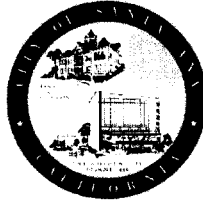


# REQUEST FOR COUNCIL ACTION



CITY COUNCIL MEETING DATE:

SEPTEMBER 19, 2011

TITLE:

## BUDGET STABILIZATION REPORT

A handwritten signature in black ink, appearing to read "Ken Waby".

CITY MANAGER

CLERK OF COUNCIL USE ONLY:

APPROVED

- As Recommended
- As Amended
- Ordinance on 1<sup>st</sup> Reading
- Ordinance on 2<sup>nd</sup> Reading
- Implementing Resolution
- Set Public Hearing For \_\_\_\_\_

CONTINUED TO \_\_\_\_\_

FILE NUMBER \_\_\_\_\_

## RECOMMENDED ACTION

Direct the City Manager to implement a budget stabilization plan based on the framework of a four-pronged approach that includes:

1. Negotiated compensation reductions
2. Outsourcing services
3. Restructuring and service reductions
4. Revenue increases

## DISCUSSION

Like many cities, Santa Ana has been severely affected by the economic recession. Major city revenues, including sales tax, property tax and the utility users' tax have declined. In addition, the State has balanced its budget by taking local government monies causing further decreases in the City's ongoing revenues. Further, the nationwide financial collapse has severely affected the City's PERS rates which have increased significantly over the last few years.

To respond to these revenue losses, the City has made reductions in its staffing levels and in employee compensation. Since 2009, the City reduced its staff by 390 positions through attrition, outsourcing, reorganizing and layoffs. The City also renegotiated its compensation agreements with its employees to eliminate or defer raises, and to increase employee contributions toward benefits and retirement. Work furloughs were also implemented. Despite these reductions, expenditures have continued to far exceed revenues.

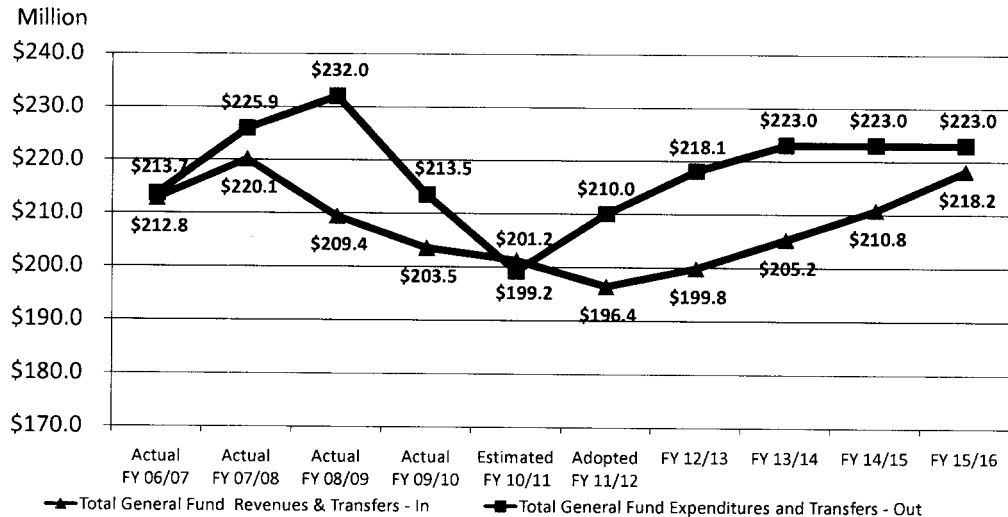
Management Partners was hired earlier this year to review the City's budget and to make recommendations for a budget stabilization plan. The purpose of the consulting firm's review was to identify ways to reduce costs and increase revenues to align the City's expenditures with its recurring revenues. This staff report incorporates some of the key findings of the study and presents staff's recommendations for implementation of a budget stabilization plan.

In June, the City adopted the FY 2011-12 budget that included a structural deficit of \$13.6 million between expected revenues and planned expenditures. This budget gap will be filled through a combination of: 1) projected savings from anticipated retirements, 2) departmental reductions and reduced purchases, and 3) the use of internal service funds that were above required levels in the City's liability and workers compensation funds. However, most of these strategies do not address the inherent structural deficit. The chart below shows that while reductions were made over the past several years, and have been planned for in FY 2011-12, they are not all structural in nature nor are they deep enough.

The following ten-year financial perspective illustrates the problem that the City has been experiencing over the past five years and the gap between revenues and expenditures in the current and coming years. The chart below was developed by Management Partners and was based on known information at the time the 2011-12 Budget was adopted. Since the adoption of the budget, new risks have emerged such as the elimination of vehicle license fees and the decline of utility user tax revenues.

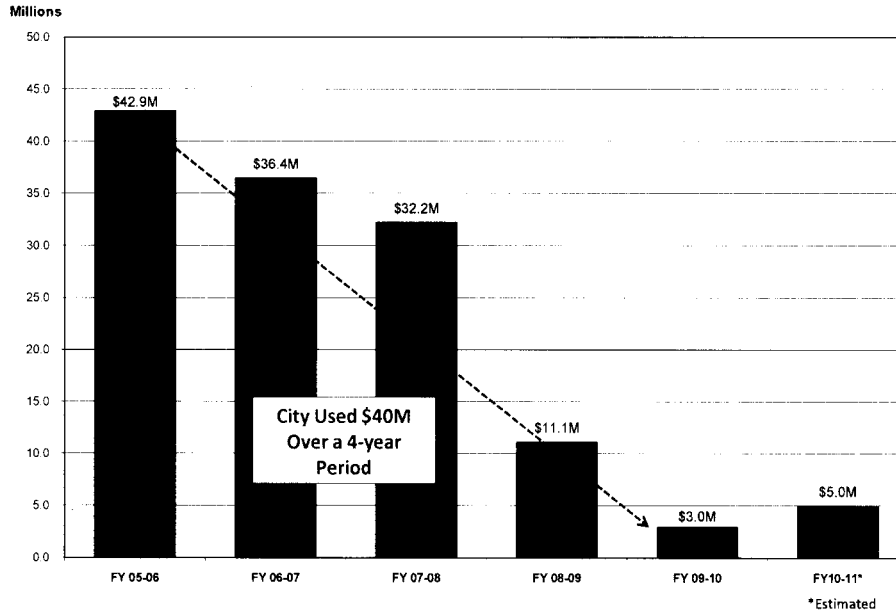
## Ten-Year Financial Perspective

(Based on FY2011-12 Adopted Budget Showing a \$13.6M Deficit)



To bridge the structural deficit, the City's unrestricted fund balance was used to maintain services. Currently it is estimated that there is only \$5 million in unrestricted funds remaining. The recommended reserve level by the Governmental Finance Officers Association is two months of operating expenses which for Santa Ana would be approximately \$35 million. The following chart illustrates the use of the City's unrestricted funds over the past five years.

**General Fund Unrestricted Balances**  
 (Savings were used to maintain operations)



Note: Economic recession began in late 2007

Looking to the FY 12/13 year, the deficit is projected to grow to an estimated \$30 million. This is due to ongoing declines in revenue associated with the economic recession, further takeaways from the State, increased costs from pre-negotiated compensation changes and increased pension costs.

**FY2012-13 Budget Forecast**

Base 2012-13 Forecast:

Revenues*	\$188.5M
Expenditure	\$218.1M
<b>Base Structural Deficit</b>	<b>\$29.6M**</b>

\*Includes loss of Vehicle License Fees and \$10M loss of UUT revenues.

\*\*Excludes additional potential revenue declines. Excludes impacts associated with the elimination of RDA estimated at \$0.5M to \$6M to the GF.

## **Recommended Approach**

To balance the City's budget, approximately \$30 million in structural changes must be in place by July 1, 2012. Budget adjustments need to begin by January 2012 to preserve the City's fund balance. The City's internal service funds need to be reserved for their intended purposes and not utilized to balance the budget.

Thus, over the past several months City staff has worked to create an action plan to stabilize the budget. A four-pronged approach is recommended to ensure that the City reduces its costs to match recurring revenues. The recommended four-pronged approach includes:

1. **Negotiated compensation reductions:** City needs to reduce salary and benefits provided to the workforce through a negotiated process. With closed contracts in place, this will require the collaboration of our bargaining units.
2. **Outsourcing:** City is obtaining requests for proposals from other service providers to preserve services to the community while obtaining them at a lower cost. Only through obtaining proposals will the City know what level of savings, if any, can be achieved.
  - Fire department services
  - Fire dispatch services
  - EMS ambulance service
  - Jail services
  - Police department services
  - Parking control and meter services
  - Animal control services
  - Fleet maintenance
  - Library services
  - Workers' comp administration
  - Zoo
  - Central stores
  - Street sweeping (sanitation fund)
  - Bowers Museum contract

Each proposal will need to be analyzed for its cost effectiveness and submitted to the Council for consideration. Implementation dates will be based on the complexity of the program, but are expected to begin in January 2012. In addition, when it makes economic and business sense the City will look at in-source opportunities.

3. **Restructuring and Service Reductions:** Departmental budget reductions including reorganizations and service reductions must be implemented. These reductions in services will depend on the dollars saved through negotiated compensation reductions and outsourcing.

4. **Revenue increases:** City will gather information to possibly seek voter approval for new and/or enhanced taxes. Staff is also working on full cost recovery for all City programs including the paramedic subscription and false alarm programs where opportunities exist to increase revenues.

Also, the City is looking into generating additional revenue from the utility franchise fee as well as from the marketing of City assets and potential sponsorships.

In addition to these four areas, I have implemented a series of expenditure control measures. These include: eliminating overtime unless pre-approved or warranted by contract, defer all major capital purchases that are not mission critical and maintain all vacancies and initiate a soft hiring freeze.

It is equally important to note that underlying this four-pronged approach are prudent fiscal principles, which not only stabilize the budget, but are critical as the City begins to build its financial health. These fundamental fiscal principles are:

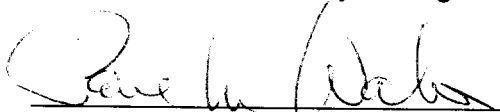
1. Fund ongoing expenditures with recurring revenues.
2. Preserve remaining unrestricted fund balance and build a general fund reserve.
3. Utilize internal service fund for intended uses, emergencies, contingencies, cash flow, and transition costs in service delivery.
4. Negotiate future compensation agreements that can be sustainable and affordable based on City's financial capacity.

To begin to implement these principles I have asked for the assistance of an outside financial consultant to review our budget and expenditure/revenue plan and have requested that bond counsel review our current portfolios. These actions are to ensure that Santa Ana proceeds forth in a prudent and responsible manner.

Throughout this process the City is committed to providing timely and relevant information to the public and to its employees. A new electronic newsletter to residents will be operational in October and the City's website and water bill inserts will be used to communicate to the public. An internal web page with budget updates has been made available for our employees with a portal site to gather their suggestions.

#### **FISCAL IMPACT**

The four-pronged approach identified above is designed to, enhance City revenues, reduce expenditures in the general fund by \$30 million, to bring expenditures in line with available revenues and to stabilize the City's budget.



Paul M. Walters  
Interim City Manager

