



REPORT TO MAYOR AND CITY COUNCIL

AGENDA ITEM

TO: THE HONORABLE MAYOR
AND CITY COUNCIL

DATE: December 11, 2007

SUBJECT: Consideration of Guiding Principles for the FY09 Budget and
10-Year Financial Plan

Report in Brief

On December 4, the City Council approved mid-year budget adjustments that addressed a \$2.658 million operating deficit generated by the current economic conditions and a structural problem wherein City expenditures and revenues are not balanced. The action approved by Council addressed the current deficit by not filling specific existing positions, deferring equipment purchases and similar “one-time” strategies. While the actions were significant and necessary, additional work is needed as part of the FY 2008-09 budget process in order to address the structural problem.

The City Council has provided staff with guidance in the development of the City’s annual budget for the past nine years. This guidance is especially critical this year as Woodland addresses extremely challenging fiscal conditions that will require staff and the City Council to review programs and adjust service levels. Staff has developed principles that are intended to guide the development of the FY 2008-09 budget and 10-year Financial Plan in a manner that meets the Council’s expectations. The purpose of this report is to summarize these principles for the City Council’s review and consideration.

Staff recommends that the City Council approve the guiding principles for the FY 2008-09 Budget and 10-year Financial Plan as described herein.

Background

On June 5, 2007, Council approved the FY 08 Operating Budget. The General Fund Budget was approved with a \$ 717,000 structural deficit to be funded with anticipated FY07 budgetary savings. The storm drain appropriations were restricted to the level of estimated annual revenues (approximately \$176,000); with Council to address additional requirements after resolution on the August 2007 vote for a storm drain rate increase. Funding toward the City’s OPEB liability was deferred for future and further discussion.

Unfortunately, the economic impacts related to the real estate market are significantly worse than originally predicted. The reductions in development activity realized in FY07 and projected for FY08 are approximately 50-60% lower than budgeted based on historic trends. Consistent with conditions across the United States, municipal revenues are being hit hard in the areas of permit fees, service charges, sales and property taxes, and development fee revenues. It is estimated that over \$2 million in General Fund revenue projected as part of the current year budget will not be collected. In addition, the defeat of the storm drain ballot measure adds an additional \$658,000 of expenses necessary to operate the program in compliance with state clean water mandates. As a result, the City Council reviewed and approved Mid-Year budget adjustments that reduced operating expenditures by over \$2.2 million and utilized a combination of unanticipated revenue and the General Fund Operating reserve to offset the revised revenue forecast.

The strategies used to reduce operating expenditures included not filling existing personnel vacancies, deferring equipment purchases and similar “one-time” strategies. While effective as a short term solution, these strategies will not resolve the current structural problem. The structural problem needs to be resolved by adjusting expenditures to be consistent with revenue assumptions. Most economists expect the current slump in the housing market to continue through 2009 and into 2010. Therefore, staff believes that the revised revenue estimates need to be factored into the City’s FY 2008-09 budget and 10-year Plan. In addition, challenges discussed as part of the FY 2008 budget process need to be revisited again, including the City’s Other Post Employee Benefit (OPEB) obligation and establishing adequate reserve funds.

It is important for the City Council to note that the City’s present fiscal condition and the future obligations described above may require an additional \$2 million reduction of General Fund expenditures over the \$2.2 million reduction generated by the Mid-Year Adjustments. It is critical that staff provide the City Council with several options to consider as part of the budget preparation process. The guiding principles developed for the City Council’s review are intended to provide these options.

Discussion

In order to meet the challenges described above, staff has developed several guiding principles. These principles should form the foundation of the budget process and need to be applied as an entire set; “selective” application of the principles will not be effective. The following guiding principles for the FY 2008-09 Budget and 10-year Plan are submitted for the City Council’s review:

- **Develop operating and capital budgets that have the minimum impact on public services:** The City’s first priority is providing responsive, efficient and effective public services. Therefore, the proposed FY 2008-09 budget needs to have the minimum impact on public services. Since it is highly likely that the preparation of a balanced budget will require some level of service reductions, it is staff’s responsibility to work toward mitigating these impacts through collaboration or other forms of alternative service delivery, develop alternative revenue sources to offset costs and present a prioritized list of service level reductions that will enable the City Council to review options.

- **Develop operating and capital budgets that have the minimum impact to employees:**
Woodland employees are the City's Number One asset. Without City employees, public infrastructure will not be maintained, critical buildings and programs are not adequately staffed and public safety needs unmet. Employees provide their skills, commitment and passion for public service to the City organization. In return, the City should provide a positive and productive work environment, fair compensation, 100% commitment to the current MOUs and open, direct and honest communication. The current status of the City's fiscal condition is a source of concern to City employees. Preparation of the City's budget during uncertain times needs to include assurances to employees that management will take every reasonable step to minimize the impact on the City's workforce. Since significant program and service reductions will likely include staffing reductions, City employees need to know that management will review options such as implementing a planned attrition program that seeks to reduce the workforce over time through retirements and voluntary separation. In turn, employees need to be flexible and consider accepting new work assignments in order to minimize the impact to public services. The development of the FY 2008-09 budget and 10-year Plan needs to include opportunities for employees, employee associations and work units to receive updates and status reports.

- **Develop the FY 2008-09 budget based on the FY 2007-08 Mid-Year Budget Adjustments:** The critical issues that generated the need to reduce the City's operating budget by \$2.658 million and the capital budget by \$12 million will remain in effect during FY 2008-09. Therefore, the upcoming budget needs to be prepared based on the conditions documented in the staff report reviewed by the City Council on December 4. Specifically, departments need to:
 - *Review existing vacancies approved with the Mid-Year Adjustments to determine if the loss of the positions can be absorbed with minimal service level impact;*
 - *Review the Mid-Year Adjustments in supplies, services, contracts, training and equipment to determine if those reductions can be absorbed with minimal impact;*
 - *Provide a prioritized list of activities with associated costs that will be discussed with the City Manager and City Council in order to consider alternatives for an additional \$2 million in General Fund expenditure reductions for FY 2008-09 over the Mid-Year Adjustments;*
 - *Consider other operating alternatives such as contractual services or community collaborations that would generate significant savings;*
 - *Consider utilizing other revenue sources to fund existing programs and services in order to reduce the impact on the General Fund;*
 - *Consider implementing new or expanded program fees for appropriate programs in order to mitigate reductions;*
 - *Consider reorganization and use of attrition to facilitate staffing reductions in a manner that reduces the impact to employees;*

- *Collaborate with the Finance Department by meeting all deadlines and reviewing potential cost saving or revenue generating scenarios with Finance staff prior to inclusion within the department's budget submittal.*
- **Present a capital and operating budget that is balanced over 10-years:** The City Manager and Senior Staff will work together in order to present a 10-year Financial Plan that is balanced over the entire planning period. This principle recognizes the potential for annual fluctuations and implements strategies to insure that an operating contingency and appropriate balance in all funds is maintained each year of the 10-year planning period.
- **Utilize the 10-year Plan as the basis for making long-term financial planning decisions:** All financial decisions, including the commitment to implement new programs and services, submission of grant applications with fixed-term funding commitments and employee compensation, will have long range impacts on the City's fiscal condition. These decisions need to be evaluated based on *short-term and long-term* impacts and factored into the 10-year Financial Plan.
- **Include resources required to maintain and operate all capital improvements commencing in the year the project is completed and continuing through the balance of the 10-year Plan:** All projects that require operating and maintenance funds need to have those funds factored into the 10-year Financial Plan *before* a commitment is made to fund the design and construction of the facility or improvement. These resources may include staff, equipment and annual contributions to reserve funds. If the resources are not available when the project is expected to be completed, consideration must be given to delay or cancel the project or reallocate future funds from another program for maintenance and operation.
- **Maintain essential services and existing facilities:** The City's investment in high priority services and established facilities needs to be factored into the 10-year Plan. Services evaluated by Senior Staff and the City Council as no longer essential should not be funded and resources reallocated to other higher priorities. Facilities that no longer meet community needs should be sold, transferred or appropriately disposed.
- **Commit to the future implementation of the Performance Based Budget:** Implementation of a Performance Based Budget will facilitate the City organization's commitment to outcomes and performance measures which will help guide program evaluation. As outlined in the Policy, Management and Leadership Initiatives staff report, the City's commitment to implementing a Performance Based Budget will be one of the primary factors in establishing a data driven, results oriented, customer focused and responsive local government organization.
- **Foster thriving and diverse residential and business communities:** The City's budget priorities need to provide adequate resources to community development activities. These

activities have a tremendous impact on the quality of life for all people who live, work, visit and conduct business in Woodland. The City's success in this area also helps to generate the resources that fund City services.

Staff believes the guiding principles described above will lay the foundation for developing the FY 2008-09 budget and 10-year Financial Plan for operating and capital programs in a responsible manner. Completing the FY 2008-09 budget will be challenging; however, it is a challenge that must be embraced as an opportunity to collaborate across departments and with the community in order to deliver the highest priority services.

Fiscal Impact

Based on staff's initial analysis of FY 2008-09 revenue/expenditure projections, reductions consistent with the Mid-Year Adjustments will be necessary to present a balanced budget. In order to address future obligations such as OPEB and the establishment of adequate reserves for facility component replacement and technology, additional reductions of approximately \$2 million may be necessary. The development of a 10-year Financial Plan may provide staff and the City Council with options for implementing the additional reductions over time through strategies such as staff attrition, property disposal and establishing a trust fund to address the OPEB liability. In any case, the Guiding Principles described herein will provide staff and the City Council with options for developing a budget in a responsible manner.

Public Contact

Posting of the City Council agenda. A copy of this report was sent to all employee associations.

Alternative Courses of Action

1. Approve the guiding principles for the FY 2008-09 Budget and 10-year Financial Plan as described herein.
2. Direct staff to implement alternative Guiding Principles based on Council discussion.

Recommendation for Action

Staff recommends that the City Council approve Alternative No. 1.

Reviewed by: Joan Drayton
Finance Director

Mark G. Deven
City Manager