

# FISCAL YEAR 2018

Fiscal Policies



The City of  
**SAN DIEGO**

## ADOPTED BUDGET

MAYOR KEVIN L. FAULCONER



# Fiscal Policies

The City of San Diego has established fiscal policies through the City Charter and Council Policies to guide responsible long-range fiscal planning, develop the adopted budget and establish reserves. The City continues to review existing policies and may adopt new policies as needed to foster responsible fiscal management. The Government Finance Officers Association (GFOA) recommends that local governments follow a financial planning process based upon established financial policies and strategies. Additionally, rating agencies such as Standard and Poor's, Moody's Investors Service, and Fitch Ratings consider fiscal policies which clearly delineate sound financial planning practices when evaluating credit ratings. The policies listed below describe the framework that the City has in place that guide fiscal decision-making.

The City's fiscal policies described below are, in most cases, summaries of the City Charter or Council Policy language. This list is not exhaustive and as policies are modified or adopted, they will be incorporated into future budget publications.

## **Legal Authority** *(Charter Section 69)*

The City Council will enact an annual Appropriation Ordinance which establishes the legal spending authority for each budgeted fund and/or department based upon the adopted budget.

## **Planning – Five-Year Financial Outlook** *(Council Policy 000-02)*

The practice of developing the Five-Year Financial Outlook (Outlook) on an annual basis for the City of San Diego began in Fiscal Year 2007, the first of which was released in November 2006. The most recent Outlook was updated and released in November 2016 and continues to present a comprehensive examination of the City's fiscal condition over the next five years. The Outlook focuses on the General Fund and is an important planning tool for the City. Beginning with Fiscal Year 2007, the Outlook has guided the City in developing the adopted budgets, and has served as the basis for the City's long-term fiscal decision-making. The Outlook communicates the City's fiscal priorities, strengths, and challenges in achieving a balanced General Fund budget.

## **Interim Financial Reporting** *(Charter Sections 39 and 89, Council Policy 000-02)*

The Chief Financial Officer provides monthly reports to the City Council detailing the fiscal status of the City with a comparison of actual revenues and expenditures to budgeted amounts.

Financial Management provides the City Council with quarterly reports forecasting the end-of-year status of the City's finances in relation to the Adopted Budget, the annual spending plan established at the onset of each fiscal year. Recommendations for appropriation adjustments necessary to maintain balanced revenue and expenses may be included.

## **Mid-Year Budget Adjustments** *(Municipal Code section 22.0229)*

During any fiscal year after the City has six months of actual budgetary data and the Mid-Year Budget Monitoring Report is projecting a surplus or a deficit relative to the Adopted General Fund Budget, the Mayor shall report such deficit or surplus to City Council and provide a recommendation to the City Council, and accompanying budget amendment resolution, to address the reported deficit or surplus. The Mayor may recommend budgeting all, none, or any portion of any projected surplus. The City Council may approve the Mayor's recommendation or modify such recommendation in whole or in part, up to the total amount recommended by the Mayor.

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Beginning in Fiscal Year 2017, Financial Management prepared the Mid-Year Budget Monitoring Report using five months of actual data as a streamlining effort for Financial Management and City departments. This allowed management and City Council to receive annual projections and recommend adjustments in a timelier manner, and allowed Financial Management to re-allocate staff resources with greater efficiency and save in overtime expenditures. As a result, Financial Management is currently reviewing the Municipal Code with the City Attorney and will be proposing recommendations to City Council to allow for flexibility in the number of months used to develop the Mid-Year Budget Monitoring Report going forward.

## **Budget Policy** *(Council Policy 000-02)*

The City adopted a Budgetary Policy in March 1962, which was amended by City Council in June 2016, to assist the City in achieving its current and future goals in a fiscally responsible and sustainable manner. The Policy guides the creation of the City's budget and outlines standards for revenue generation and the execution of operating and capital budget expenditures as recommended by the GFOA and the National Advisory Council on State and Local Budgeting (NACSLB). This document is reviewed on a regular basis to incorporate the highest standards of fiscal management and the City's budgetary goals and will be updated if changes to the Mid-Year Budget Monitoring process are approved.

## **Balanced Budget** *(Charter Section 69)*

A summary outlining the figures of the budget that describes the balance between the ensuing year's total expenditures and total revenues, contrasted with corresponding figures for the current year, is presented by the Mayor no later than April 15 of each year. The classification of the estimate shall be as nearly uniform as possible for the main divisions of all departments and shall furnish necessary detailed fiscal information.

## **Basis of Budgeting**

The City's budgets for Governmental Funds, such as the General Fund, Debt Service Funds, Special Revenue Funds, and Capital Project Funds, as well as Internal Service Funds, shall be prepared based on the modified accrual basis of accounting (revenues are recognized in the accounting period in which they become available and measurable, and expenditures are recognized in the accounting period in which the liability is incurred), except that the increase/decrease in reserve for advances and deposits to other funds and agencies shall be considered as additions/deductions of expenditures.

The City's Enterprise Funds shall be prepared on the full accrual basis of accounting (revenues are recognized when they are earned and expenses are recognize when the liability is incurred).

The City's operating budget shall exclude unrealized gains or losses resulting from the change in fair value of investments.

## **Community Projects, Programs, and Services** *(Council Policy 100-06)*

The City adopted a policy on July 7, 2011, and amended by City Council on December 8, 2011, to establish guidelines and uniform eligibility requirements for the annual appropriation and expenditure of funding for each City Council Office for community projects, programs, and services to be expended at the discretion of each Council member during the fiscal year. Annual funding levels are subject to budget priorities as established by City Council each year. Proposed funding levels for Community Projects, Programs, and Services for each Council Office is included each year in the Mayor's Proposed Budget. Proposed funding levels for the following fiscal year may be initially

determined based on estimated savings to be achieved related to the administration of each Council Office by the current fiscal year-end. Variances in actual savings from budgeted amounts may result in recommendations from the Mayor to the City Council to revise appropriations to reflect actual savings, as a mid-year budget adjustment, depending on financial circumstances and prior year results for the General Fund and reserves.

### **Capital Improvements Program (CIP) Prioritization** *(Council Policy 800-14)*

The City's Prioritizing Capital Improvement Program Projects Policy was adopted on January 16, 2007 and amended by City Council on November 13, 2013. This Policy establishes an objective process for evaluating CIP projects with respect to the overall needs of the City through the ranking of CIP projects. The ranking of projects is used to successfully allocate and maximize all available resources to ensure projects are completed effectively and efficiently, resulting in more projects delivered citywide.

### **CIP Transparency** *(Council Policy 000-31)*

The Capital Improvements Program Transparency Policy was adopted by City Council on April 5, 2012. This Policy establishes standard requirements for enhancing CIP transparency and improving access to publicly available information related to the CIP. It also establishes the framework for making the information readily available to the stakeholders by using a combination of presentations to the City Council, stakeholder meetings, and media including the City's website. This Policy was developed as part of the CIP streamlining process.

### **Proceeds of Sale of City-Owned Real Property** *(Charter Section 77)*

On June 7, 2016, the voters amended Charter Section 77, establishing that all proceeds received from the sale of City-owned real property shall be used exclusively for the acquisition and construction of permanent public improvements, including public buildings and such initial furnishings, equipment, supplies, inventory and stock as will establish the public improvement as a going concern. Proceeds may also be used to reimburse the General Fund for prior capital expenditures and for the financing costs, if any, associated with the acquisition and construction of such permanent public improvements. The funds may also be used for the replacement of permanent public improvements but not the repair or maintenance thereof.

### **Debt Management** *(City Debt Policy)*

The City's Debt Policy was adopted by the City Council in Fiscal Year 2008 and updated every other year with the last update on April 24, 2017 by Council Resolution 311057. The policy documents the procedures and goals for the use of various debt instruments to finance City needs and the sound management of the existing debt obligations.

The Debt Policy establishes guidelines to address the following: purpose and need for financing; credit ratings; types of financing instruments; debt ratios guidelines; structure and term of City indebtedness; method of issuance and sale; financing team role and selection process; refunding considerations; and post issuance compliance and administration. The Debt Policy addresses debt instruments issued by the joint powers authorities on behalf of the City including Lease Revenue Bonds, Revenue Bonds for Water and Sewer Systems and Conduit Financing Bonds.

Appendices to the Policy include specific policies for Special Districts. The Special Districts Formation and Financing Policy (Appendix A to the Debt Policy) provides uniform guidelines for the formation of Community Facilities District (CFD) and 1913/1915 Act Assessment Districts. Also

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included in the Debt Policy is the San Diego Housing Commission Policy Multifamily Mortgage Revenue Bond Program (Appendix B to the Debt Policy).

## **Infrastructure Fund** (*Charter Section 77.1*)

On June 7, 2016, voters approved Proposition H, requiring the City to dedicate specific sources of revenue to fund new General Fund infrastructure, such as streets, sidewalks, bridges, buildings, and the maintenance and repair of such infrastructure.

The calculations to fund the new Infrastructure Fund are based upon the following:

- Major Revenues Increment – amount equal to 50.0 percent of the year over year growth in property tax revenues, unrestricted General Fund TOT, and unrestricted franchise fees for Fiscal Year 2018 through Fiscal Year 2023
- Sales Tax Increment – an amount equal to the annual change in sales tax revenue when compared to the sales tax baseline of Fiscal Year 2016 actual receipts inflated by the lessor of California Consumer Price Index (CCPI) or two percent for Fiscal Year 2018 through Fiscal Year 2043
- General Fund Pension Cost Reduction – any amount if pension costs for any fiscal year are less than the base year of Fiscal Year 2016 for Fiscal Year 2018 through Fiscal Year 2043

## **Investment** (*City Treasurer's Investment Policy*)

The City Treasurer's Pooled Investment Fund is comprised of core and liquidity portfolios. The liquidity portfolio is designed to ensure that the projected expenditures and related demands for cash can be met over a six month period per California Government Code 53646 and the core portfolio is invested to allow for additional liquidity and longer term growth of principal. The investment process is governed by the City Treasurer's Investment Policy, which is based on the California Government Code and annually presented to the City Treasurer's Investment Advisory Committee for review. The City Treasurer's Investment Policy is finally reviewed and accepted annually by the City Council. The Investment Policy was last adopted on January 1, 2017.

## **Reserves Policy** (*Council Policy 100-20*)

The City Reserve Policy, adopted by Council on October 15, 2002 and most recently amended by City Council on February 21, 2017, defines the City's reserves and sets policy targets for reserves across City operations, including General Fund, risk management and enterprise operations. These reserves are intended to be the foundation for strong fiscal management guides future City decisions.

### **General Fund Reserves**

In February 2017, the City Council approved amendments to the City's Reserve Policy (Council Policy 100-20) to extend the funding schedule to achieve the 16.7 percent policy goal for the General Fund Reserve by Fiscal Year 2025. Prior to these amendments, the policy goal was to be achieved in Fiscal Year 2021. Total General Fund Reserves consist of the total of the Emergency Reserve and the Stability Reserve. The Emergency Reserve shall be set at a target level of 8.0 percent, and the Stability Reserve shall be set at a target level of 8.7 percent. The Fiscal Year 2018 Adopted Budget includes a total of \$17.4 million to the General Fund Reserve. This figure includes funding to achieve the Fiscal Year 2019 policy target level of 15.25%.

Total General Fund Reserves will be based on, and reconciled to, the General Fund fund



balance. The sum of the Emergency Reserve, Stability Reserve, and any amounts determined to be Excess Equity, shall equal the sum of unassigned fund balance and amounts restricted for the purpose of maintaining the Emergency Reserve.

### **Emergency Reserve**

An Emergency Reserve is to be maintained for the purpose of sustaining General Fund operations at the time of qualifying emergencies as declared by the Mayor and/or City Council and ultimately approved by City Council. The Emergency Reserve will not be accessed to meet operating shortfalls or to fund new programs or personnel. This reserve may be expended only if an event is determined to be a public emergency by a two-thirds vote of the City Council when such expenditures are necessary to ensure the safety of the City's residents and property. In the event this reserve is reduced below the amount established by this Policy, the Mayor shall prepare a plan as promptly as conditions warrant to replenish the Emergency Reserve balance to the Policy level.

### **Stability Reserve**

A Stability Reserve will be maintained to mitigate financial and service delivery risk due to unexpected revenue shortfalls or unanticipated critical expenditures. The purpose of this reserve is to provide budgetary stabilization and not serve as an alternative funding source for new programs. The Stability Reserve may be used as a source of one-time funding for critical capital or operating needs. Recommendations to appropriate from the Stability Reserve will be brought forward by the Mayor and will require approval by a majority of the City Council. In the event this reserve is reduced below the amount established by this Policy, the Mayor shall prepare a plan no later than one year from the reserve action to replenish the Stability Reserve balance to the policy level.

### **Excess Equity**

Excess Equity is spendable and unrestricted fund balance that is not otherwise assigned to General Fund Reserves and is available for appropriation. Excess Equity is most commonly a non-recurring source of revenue. Consistent with City Council Budget Policy (Policy No. 000-02) and the use of one-time and ongoing revenues, Excess Equity will be appropriated primarily for unanticipated circumstances, such as a General Fund revenue shortfall affecting programs included in the current year budget or for one-time priority expenditures. Recommendations for the use of Excess Equity may be brought forward by the Mayor and will require approval by a majority of the City Council.

### **Pension Payment Stabilization Reserve**

In April 2016, City Council adopted a Pension Payment Stabilization Reserve (Pension Reserve) as part of the City's Reserve Policy. As a result, a Pension Reserve will be maintained to mitigate service delivery risk due to the unanticipated increases in the annual pension payment, the Actuarially Determined Contribution (ADC).

The Pension Reserve shall only be used to supplement unanticipated increases in the ADC payment as calculated in the most recent Actuarial Valuation Report (Report) produced by the San Diego City Employee's Retirement System (SDCERS) actuary. Unanticipated increases are defined as the

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difference between the total change in the ADC and the expected change in the ADC as provided in the Change in ADC Table of the Report.

Recommendations to appropriate from the Pension Reserve may be brought forward by the Mayor in the annual budget process and will require approval by a majority of the City Council. During the adoption of the annual budget, the City Council has the authority to propose the use of the Pension Reserve consistent with the Pension Reserve Policy and the City Charter. In the event the Pension Reserve is reduced below the amount established by this Policy, the Mayor shall prepare a plan no later than one year from the reserve action to replenish the Pension Reserve balance to the Policy level. The Fiscal Year 2018 Adopted Budget includes the use of one-time funding of \$20.8 million to Citywide (\$16.0 million to the General Fund) from the Pension Payment Stabilization Reserve to offset the increase in the City's ADC to the pension system.

## **Workers' Compensation Fund Reserve**

In February 2017, City Council approved amendments to the City's Reserve Policy (Council Policy 100-20) to reduce the Workers' Compensation Reserve target from 25.0 percent to 12.0 percent of the three-year average of outstanding actuarial liabilities. As a result, there is \$19.7 million in excess Workers' Compensation reserves available for use in the General Fund. A total of \$14.1 million of these excess reserve funds will be used in Fiscal Year 2018, which includes a \$7.0 million contribution to the General Fund Reserve, a \$3.1 million contribution to the Public Liability Reserve, and a \$4.0 million reduction in Workers' Compensation operating expenses. The remaining excess Workers' Compensation reserves will be used to continue the reduction in Workers' Compensation operating expenses through Fiscal Year 2020.

## **Public Liability Fund Reserve**

The City shall maintain reserves equal to 50.0 percent of a three year average of the outstanding actuarial value of public liability claims. This reserve level recognizes that not all claims will be due and payable at one point in time and that not all claims will be awarded, yet there may be more than one large claim that could require an immediate payment. The Fiscal Year 2018 target is to reach 47.0 percent of the average actuarial liability valuation of the three most recent fiscal years. The Policy goal is to achieve 50.0 percent funding in Fiscal Year 2019.

## **Long-Term Disability Fund Reserve**

The Reserve Policy requires that the long-term disability fund reserves equal the average actuarial liability valuation of the three most recent fiscal years. The reserve is currently projected to be funded above the Policy level and \$2.1 million Citywide (\$1.4 million General Fund) excess reserves will be used to fund the pay-go requirement in Fiscal Year 2018. The Fiscal Year 2018 Adopted Budget does not include any additional contributions to this reserve.

## **User Fees** *(Council Policy 100-05)*

User fees are charged for services provided to residents and businesses in the City as a result of public need. Abiding by the standards and best practice guidelines established by the Government Finance Officers Association (GFOA) and the National Advisory Council on State and Local Budgeting (NACSLB), the City has formed a policy to identify factors to be considered in calculating the full cost of services in order to appropriately set fees.

The User Fee Policy requires that all fees be categorized according to the level of cost recovery (full or partial recovery or be considered as penalties which would not require a specific cost recovery level). Cost recovery rates shall be determined based upon direct and indirect costs.



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According to the Policy, a comprehensive user fee study and review of the Policy shall be conducted every three years. The City completed a comprehensive study on the General Fund user fees during Fiscal Year 2015 with implementation taking place with the commencement of Fiscal Year 2016. The next comprehensive study of General Fund user fees is scheduled to occur during Fiscal Year 2018 with implementation taking place with the commencement of Fiscal Year 2019.

Ongoing review of the City's fiscal policies will continue to support the City's continued efforts to improve financial transparency and improve the fiscal strength of the City.



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