THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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Review of the Fiscal Year 2012 First Quarter Budget Monitoring Report

OVERVIEW

On November 23, 2011, the Financial Management Department issued the Fiscal Year 2012 First Quarter Budget Monitoring Report ("Report"), which presents projections of year-end revenues and expenditures based on actual data for the first three months of the fiscal year (through September 30, 2011). The IBA has reviewed the Report and compared this information to the City Comptroller's Year-End Financial Performance Report in addition to the Mayor's FY 2013-2017 Five-Year Financial Outlook. The IBA could not compare the Report to first quarter performance in FY 2011 for possible continued trends due to issues that arose last year with SAP that prevented the report from being released.

The Fiscal Year 2012 First Quarter Budget Monitoring Report provides a detailed overview of General Fund performance for the first quarter of FY 2012 and contains few major issues. Performance of major revenues shows positive indications while total aggregate revenue exceeds budgeted levels. General Fund expenses have also increased due primarily to personnel expenses and fringe, which has resulted in a forecasted $2.6 million deficit in the Report. Additionally, current General Fund reserves estimates in the Report exceed forecasted levels on June 1, 2011 of a $94.1 million reserve total. The Report shows an estimated FY 2012 ending balance of $101.1 million, or 8.9 percent of forecasted revenue, which includes the forecasted $2.6 million projected deficit this fiscal year.

FISCALY/POLICY DISCUSSION

General Fund Revenues

General Fund revenues increased $6.1 million from the Adopted Budget, to $1.13 billion, due primarily to revised projections for the three largest major revenues: property tax, sales tax, and transient occupancy tax. Other revenues decreased by $4.7 million from the Adopted Budget due to revenue shortfalls in Police, Public Works – Engineering and Capital Projects, and the elimination of motor vehicle license fee (MVLF) revenue. The largest negative variations from budgeted amounts are from parking citation collections and lower than expected reimbursements for Public Works-Engineering and Capital Projects services.

The General Fund revenue projection is $3.4 million less than that projected for the FY 2012 base year that was utilized in the FY 2013-2017 Five-Year Financial Outlook. This variance is due to minor adjustments made to major General Fund revenue projections based on new current year performance data and revised departmental revenue projections that were not addressed in the Outlook.

Revenue Source	Fiscal Year 2011 Unaudited Actual	Fiscal Year 2012 Adopted Budget	Fiscal Year 2012 First Quarter Report	$ Change FY 12 Adopted Budget - FY 12 First Quarter	$ Change FY 11 Unaudited Actual - FY 12 First Quarter
Property Tax	$ 384,023,003	$ 380,908,544	$ 384,686,705	$ 3,778,161	$ 663,702
Sales Tax	209,122,393	211,589,835	217,596,602	6,006,767	8,474,209
Transient Occupancy Tax	73,398,622	74,787,161	76,128,190	1,341,029	2,729,568
Franchise Fees	65,546,321	67,688,948	67,520,239	(168,709)	1,973,918
Other Revenue	353,440,149	391,628,578	386,788,640	(4,839,938)	33,348,491
Total GF Revenue	**$ 1,085,530,488**	**$ 1,126,603,066**	**$ 1,132,720,376**	**$ 6,117,310**	**$ 47,189,888**

Major General Fund Revenues

The IBA has reviewed the projections for major revenues and assesses that they are appropriate based on current year performance trends and economic forecasts. The Report projects that the four largest major General Fund revenues (shown in table above) will exceed budgeted levels by $10.8 million, or 1.5 percent. The largest gain is from sales tax, accounting for over 50 percent of this total gain in major revenues. Consumer spending forecasts for sales tax and transient occupancy tax are consistent with current economic projections. The property tax revenue projection, the General Fund's largest revenue source, is consistent with assessed value information from the County of San Diego Assessor/Recorder/County Clerk's Office and the Report highlights potential risks with this revenue source.

Police Department

As outlined in the Report, due to State of California budget actions, MVLF revenue was eliminated this fiscal year. Projections included in the report reflect this elimination of $3.3 million in MVLF revenue. However, this revenue was to be partially offset by a projected $2.0 million booking fee relief from the State that is currently included in the Report under the Police Department expenditure budget. Additionally, an estimated $800,000 was forecasted to be received in citizen's option for public safety (COPS) grant from the State above budgeted amounts. After discussing with the Financial Management Department, this additional $800,000 noted in the report was not included in projections because these funds are currently being forecasted to be utilized outside of the General Fund for required helicopter maintenance.

Parking Citation Revenue

The FY 2011 Adopted Budget for parking citation revenue was $17.3 million and was increased to $21.5 million in budgeted revenue for FY 2012. The increase of $4.2 million above FY 2011 budgeted levels was due to two additions of revenue to the FY 2011 budgeted level: 1) $3.2 million of on-going revenue due to the pass-through of State mandated surcharges to offenders, and 2) $1.0 million in one-time revenues due to referral of delinquent parking citations to collections. As shown in the City Comptroller's Year-End Financial Performance Report, parking citation revenue projections for FY 2011 were $578,370 lower than budgeted revenues, which is a variance of 4.7 percent. However, as shown in the FY 2012 First Quarter Report, the variance from budgeted levels in FY 2012 is projected to be $3.0 million less than budget or approximately a 14.0 percent decline. In discussions with City Treasurer's Office, the $3.2 million in additional revenue included in the FY 2012 budget from the surcharge pass-through was based on a three year average of the number of parking citations issued multiplied by the surcharge amount. They also indicated that this program is operating properly and any variance in budgeted amounts would be due to the number of tickets issued in FY 2012 differing than the number of tickets estimated in the three year average.

The IBA also spoke with the Police Department regarding the cause for this variance from budgeted levels. Based on information provided to the IBA by the Police Department, the volume of parking citations written in FY 2012 as compared to FY 2011 is estimated to increase by 8.2% over FY 2012 based on the volume of citation activity in the first quarter. Additionally, in prior fiscal years, the Police Department attributed a negative variance in parking citation revenue to understaffing of parking enforcement officers; however, their staffing currently exceeds levels from the prior two fiscal years.

Based on the information received and reviewed by the IBA, the cause for the shortfall in parking citation revenue in FY 2012 has not yet been determined. We recommend that the Financial Management Department and the Police Department continue to research the cause for this revenue shortfall and report their findings in the FY 2012 Mid-Year Budget Monitoring Report.

Public Works – Engineering and Capital Projects

The Report identifies a projected $2.0 million revenue shortfall in E&CP due to "unknown reasons". After multiple conversations with the department, they have identified the variance is primarily due to lower reimbursements from other departments for engineering services. Our office has not been able to determine the specific causes for the reduction in reimbursements and the department is continuing to research the specific causes. This is a concern and will need to be explored further and reported in the Mid-Year Report.

<u>General Fund Expenditures</u>

General Fund expenditures increased $6.9 million from the Adopted Budget due primarily to personnel expenses, fringe expenditures, and supplies. Three departments primarily contribute to the overage in each individual area: Fire-Rescue, Police, and Public Works – Engineering and

Capital Projects. The IBA reviewed the expenditures outlined in the Report and are comfortable with the projected information presented.

Expenditure Category	Fiscal Year 2011 Unaudited Actual	Fiscal Year 2012 Adopted Budget	Fiscal Year 2012 First Quarter Report	$ Change FY 12 Adopted Budget - FY 12 First Quarter	$ Change FY 11 Unaudited Actual - FY 12 First Quarter
Personnel Expenditures	$ 490,118,457	$ 504,576,341	$ 507,436,024	$ 2,859,683	$ 17,317,567
Fringe Benefits	317,853,238	308,939,938	311,487,269	2,547,331	(6,365,969)
Contracts	160,220,858	174,522,415	174,284,512	(237,903)	14,063,654
Energy & Utilities	26,745,908	33,748,202	34,602,637	854,435	7,856,729
Information Technology	25,494,936	23,227,591	23,347,630	120,039	(2,147,306)
Supplies	18,433,908	17,872,193	19,929,459	2,057,266	1,495,551
Other Expenses	42,994,153	65,501,594	64,190,394	(1,311,200)	21,196,241
Total GF Expenses	**$ 1,081,861,458**	**$ 1,128,388,274**	**$ 1,135,277,925**	**$ 6,889,651**	**$ 53,416,467**

Library

The Library Department is projecting to end the fiscal year $849,000 under budgeted expenditures primarily due to vacant positions. Through the first quarter, the Library Department had 43 vacancies (out of 359 budgeted positions), but was actively working to fill these positions. As of the end of November 2011, the Library Department had filled 10 of these vacant positions and was in the interviewing/hiring process to address the remaining vacancies. Service levels have been maintained through the usage of hourly staffing and overtime, which will be reduced upon the filling of the vacant positions.

Park & Recreation

The Park and Recreation Department is projecting to end the fiscal year with $556,000 expenditures over budget primarily due to staffing for opening recreation centers beyond originally budgeted operating hours. However, the additional hours of operation are fully cost recoverable. These expenditures are recouped either through fees charged to organizations for their specific usage of the center when it would normally be closed or through donations which allow general public usage beyond the originally scheduled hours of operation. These additional charges and donations are also one of the causes for the anticipated $1.1 million excess revenue over the budgeted amount for the Park and Recreation Department.

Fire-Rescue

As referenced in the Report, the Fire-Rescue Department is projected to end the year $3.9 million over budget in personnel costs. This overage is due to $5.4 million in expenditure increases comprised of: $2.0 million in overtime, $1.5 million in additional expense associated with the filling of positions assumed in the department’s vacancy factor, $1.3 million in termination pay due to an increase in the expected number of retirements this year, $452,000 in vacation pay-in-lieu, and $218,000 in industrial leave. The additional expense of $1.5 million for filling of positions is the result of hiring 21 of 55 positions (the majority of which are sworn) that were assumed to be part of the department’s vacancy factor for FY 2012. The vacancy factor for FY 2013 may have to be reevaluated based on staffing patterns.

The total expenditure increase of $5.4 million is offset by $1.5 million in projected fringe savings due to the use of overtime to meet constant staffing needs instead of additional full-time positions.

Additional Expenditures

The Report mentions two potential increases in costs that are not currently reflected in projections, totaling $5.0 million: 1.) the projected termination pay expense of $3.3 million for DROP participants retiring in FY 2012 due to the change in retiree health benefits; 2.) and $1.7 million in increased costs for gasoline. The termination pay expense change was reflected as a savings in future fiscal years in the FY 2013-2017 Five-Year Financial Outlook, and identified the estimated cost mentioned in the Report. The IBA agrees that this expense should not be currently reflected in projections due to the currently unknown impact and difficulty in estimating the expenses, but an additional expense over budgeted amounts is reasonably expected to occur. An estimate for this expense should be included in the FY 2012 Mid-Year Budget Monitoring Report.

Gasoline costs are charged to General Fund departments by the Fleet Services Operating Fund in usage fees to recoup their costs expended for their purchase. The Fleet Services Operating Fund is noted in the Report as experiencing an increase in gasoline costs and, if trends are to continue, a shortfall of $2.3 million may occur due to the increase in gasoline and fuel costs. Additionally, there was a $1.2 million gasoline price increase reflected in the FY 2013-2017 Five-Year Financial Outlook in FY 2013. Based on current experience and previous forecasted increases in gasoline prices, the $1.7 million estimated increase in gasoline prices should be reflected in revised usage fees to be paid from General Fund departments in the FY 2012 Mid-Year Budget Monitoring Report.

General Fund Reserves

According to the Report, the General Fund ended FY 2011 with a fund balance of $103.3 million. It should be noted that approximately $1.6 million of that fund balance was due to savings in the FY 2011 Council District administrative budgets. These savings were subsequently budgeted in FY 2012 for Community Projects, Programs and Services (CPPS) in accordance with Council Policy 100-06, approved in June 2011.

Based on projected current year revenues and expenditures, and including the release of prior-year encumbrances, the General Fund is estimated to end FY 2012 with a fund balance of $101.1 million. This fund balance is approximately $10.2 million or 0.9 percent in excess of the 8.0 percent reserve target. This reserve projection also includes the $5.0 million in additional expenditures for early retirees based on changes to retiree healthcare and the increase in fuel costs, despite them not being included in operating projections in the Report. The estimated fund balance exceeds the $94.1 million fund balance published in the Supplemental May Revision on June 1, 2011 due to the performance of the General Fund in FY 2011. As detailed in the City Comptroller's Year-End Financial Performance Report, the General Fund ended with a $1.7 million deficit, which did not necessitate utilizing the $24.6 million in property tax set aside revenues and were retained in fund balance.

CONCLUSION

In summary, no budget adjustments are recommended at this time due to the forecasted deficit of only $2.6 million in the current fiscal year and reserves exceeding the target by $10.2 million. The IBA concurs with the revised revenue and expenditure projections for the current year that result in this forecasted deficit, with the exception of the few items noted in this report.

It is the IBA's recommendation the Mid-Year Budget Monitoring Report should reflect the increased gasoline prices of $1.7 million in usage fees for General Fund departments and include a projection for DROP participant leave liability figures due to the change in post retirement health benefits on April 1, 2012. Further research also needs to be undertaken to explain the reductions in parking citation revenue and reimbursements for engineering services, and addressed in the Mid-Year Budget Monitoring Report.

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