THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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FY 2013 First Quarter Budget Monitoring

OVERVIEW

The Financial Management Director issued the Fiscal Year 2013 First Quarter Budget Monitoring Report (1st Quarter Report) on November 21, 2012. The 1st Quarter Report describes the current status of revenues and expenditures and their year-end projections based on actual (unaudited) data from July 2012 through September 2012.

As noted in the 1st Quarter Report, overall projected revenue and expenditure variances from budgeted figures are minimal; however, certain individual revenue and expenditure projections are deviating from budgeted figures, but are generally offset with compensating changes in other General Fund projections. Our Office's report highlights the following:

- Additional detail for individual variances noted in the 1st Quarter Report
- Detail for items that have not been noted in the 1st Quarter Report that are projected to impact the General Fund
- Additional information on new revenue of note that has arisen since the issuance of the 1st Quarter Report that are known to impact General Fund projections
- Potential fiscal impacts due to the dissolution of the City's redevelopment agency

OFFICE OF THE INDEPENDENT BUDGET ANALYST
202 C STREET MS 3A SAN DIEGO, CA 92101
TEL (619) 236-6555 FAX (619)-236-6556

FISCAL/POLICY DISCUSSION

General Fund Revenues

General Fund projected revenues increased by approximately $0.5 million from the Adopted Budget primarily due to a small increase in major revenues. General Fund revenues are currently projected to be less than a 1.0 percent variance from budgeted figures. Additionally, the adjusted budget shown in the 1st Quarter Report reflects $4.5 million in revenues related to supporting the dissolution and unwinding activities of the former redevelopment agency.

Revenue Source (in millions)	FY 2013 Original Projections	FY 2013 1st Quarter Report	Variance
Property Tax	$ 387.1	$ 390.7	$ 3.6
Sales Tax	236.3	232.7	(3.6)
Transient Occupancy Tax	81.7	83.7	2.0
Franchise Fees	71.7	71.6	(0.1)
Departmental Revenue	374.4	373.0	(1.4)
TOTAL ADOPTED BUDGET	**$ 1,151.2**	**$ 1,151.7**	**$ 0.5**
Civic San Diego [1]	$ 4.5	$ 4.5	$ -
TOTAL ADJUSTED BUDGET	**$ 1,155.7**	**$ 1,156.2**	**$ 0.5**

1 - Authorized by R-307536

Major General Fund Revenues

The IBA has reviewed the projections included for the 1st Quarter Report for major General Fund revenues and believe they are appropriate based on current economic conditions and revenue distributions year-to-date. The General Fund's largest revenue source, property tax, is projected to exceed budgeted levels by approximately $3.6 million due to $4.8 million in projected revenue to be received from the Redevelopment Property Tax Trust fund (RPTTF) due to dissolution of the City's redevelopment agency. As noted in the 1st Quarter Report, this increase has been offset by a decline in assessed valuation from levels assumed in the FY 2013 Adopted Budget, which reduced property tax revenue by approximately $1.2 million prior to the inclusion of RPTTF revenue in current projections.

Consumer and business spending continue to increase, leading to an increase in both transient occupancy (TOT) and sales tax revenues from comparable prior periods. The $2.0 million growth in TOT is attributable to an increase in actual revenue above the FY 2012 year-end revenue estimate used to develop the FY 2013 budget. When using this updated base budget, estimated revenue for FY 2013 increases by $2.0 million.

As noted in the 1st Quarter Report, the decrease in sales tax revenue is primarily related to a lower than budgeted distribution of the "triple-flip" payment from the State of California, which is not indicative of current local taxable sales performance. This lower-than-forecasted distribution accounts for $3.4 million of the $3.6 million in the reduced sales tax projection.

Excluding this variance from the "triple-flip", sales tax revenue is close to budgeted levels for FY 2013.

Departmental Revenue Issues

Parking Citation Revenue

The FY 2014-2018 Five-Year Outlook (Outlook) assumed a $1.0 million increase to the $18.0 million parking citation base budget forecast for FY 2013. This increase was based on an assumed continuance of the improved performance in revenue experienced in FY 2012. However, the 1st Quarter Report does not reflect an increase in the year-end projections for parking citations previously assumed in the Outlook. While the Police Department anticipates that parking citation revenue will exceed budgeted expectations by approximately $600,000, this has not been reflected in the 1st Quarter Report given that it is too early to determine if current trends will continue based on one quarter of performance data. In contrast, the parking citation projection for the Transportation and Storm Water Department has been lowered in the 1st Quarter Report by approximately $200,000 based on current trends that are expected to continue. In total, based on current year-to-date revenue, parking citation revenue is expected to perform over budget by $400,000.

Fire-Rescue

It is anticipated that the Fire-Rescue Department will not achieve budgeted revenue levels for its Alarm Permit Fee program in FY 2013. Year-end projections for the program have been adjusted in the 1st Quarter Report to reflect an anticipated reduction in performance from budgeted levels of $910,000 to a revised year-end projection of $285,000, a reduction of $625,000. In FY 2012, the program yielded $204,095 in revenue, which was $705,905 under budgeted amounts. The program's under budget performance is primarily due to fewer permits being issued than initially expected and system processing issues undermining the department's ability to assess penalty billings. Fire-Rescue is currently working with the Police Department to prepare a Request for Proposal for a new alarm billing and tracking system that will remedy current billing issues. The new system is anticipated to be implemented by FY 2014.

Property Tax Administration Fee

Beginning in FY 2007, the County of Los Angeles began charging additional property tax administration fees to each city in the county based on legislative ambiguity associated with property taxes used to backfill city revenue associated with the "triple-flip" and "VLF swap". The County of San Diego also instituted this property tax administration fee calculation methodology starting in FY 2009.

In FY 2008, the City of Alhambra (et al.) filed a petition against the County of Los Angeles disputing the way in which the property tax administration fee calculation had recently been modified. After extensive litigation, the Supreme Court of California issued its opinion on the validity of the increase in property tax administration charges on November 16, 2012 ruling in favor of the City of Alhambra (et al.) and nullifying the increase in property tax administration charges.

Subsequently on December 5, 2012 (after release of the 1st Quarter Report), the City was informed that the County of San Diego would be returning this disputed excess property tax administration fee that the City paid from FY 2009 to FY 2012. The total amount collected in excess property tax administration fees for all cities in the County from FY 2009 to FY 2012 was $13.5 million; $6.9 million of which is due to be refunded to the City of San Diego in FY 2013.

Additionally, the County of San Diego is now returning to the methodology utilized prior to FY 2009 to calculate ongoing administration charges per fiscal year, starting in FY 2013. Based on the FY 2012 over-charge calculated by the County of San Diego, the actual charge the City would have paid is $3.7 million. Based on the similar level between actual FY 2012 property tax revenue and projected FY 2013 revenue[1], it is estimated that the FY 2013 administration charge will be similar to FY 2012, which represents an approximate $1.4 million in potential savings to the City from budgeted levels, as shown below.

Actual FY 2012 Administration Charge	$	5,597,018
County Calculated FY 2012 Overcharge		1,892,057
"Normalized" FY 2012 Admin Charge	**$**	**3,704,961**
Budgeted FY 2013 Administration Charge	$	5,102,711
"Normalized" FY 2012 Admin Charge		3,704,961
Estimated Savings for FY 2013	**$**	**1,397,750**

On December 6, 2012, Mayor Filner proposed to utilize the one-time $6.9 million in revenue to support new public safety expenditures. No further details are known at this time; however, any new proposed expenditure(s) would require City Council approval.

Corporate Partnership Program

Year-end revenue for the Office of the Chief Financial Officer (Corporate Partnership Program) is projected to be approximately 64% or $386,000 lower than the $600,000 budgeted in FY 2013. Although the Program has generated in-kind and other non-monetary benefits for the City in FY 2013, the lower revenue projection is in part attributable to unanticipated delays in certain partnerships (vending, water line insurance). The Program Director anticipates full implementation of these partnerships and realization of the associated revenue in FY 2014.

General Fund Expenses

General Fund expenditures increased by approximately $0.8 million from the Adopted Budget, which is attributable to a marginal increase in non-personnel expenditures. As with General Fund revenues, expenditures are currently projected to be less than a 1.0 percent variance from budgeted figures. Additionally, the adjusted budget reflects $4.5 million in expenditures (also included in revenues) related to support dissolution and unwinding activities of the former

[1] Excluding any redevelopment related property tax revenue in both fiscal years, which has an administration charge applied outside of the scope of this analysis.

redevelopment agency. The adjusted expenditure budget also includes $0.5 million to fund the Civic San Diego operating budget as approved by City Council.

Expenditure Category (in millions)	FY 2013 Original Projections	FY 2013 1st Quarter Report	Variance
Personnel Expenditures	$ 511.5	$ 511.8	$ 0.3
Fringe Benefits	321.1	320.5	(0.6)
Contracts	143.8	142.6	(1.2)
Energy & Utilities	42.7	42.9	0.2
Information Technology	42.9	42.8	(0.1)
Supplies	21.3	22.2	0.9
Other Expenditures	80.6	81.9	1.3
TOTAL ADOPTED BUDGET	**$ 1,163.9**	**$ 1,164.7**	**$ 0.8**
Civic San Diego [1]	$ 5.0	$ 5.0	$ -
TOTAL ADJUSTED BUDGET	**$ 1,168.9**	**$ 1,169.7**	**$ 0.8**

1 - Authorized by R-307536 & O-20185

Fire-Rescue Constant Staffing

In FY 2012, over budget personnel expenses, primarily related to overtime, prompted a mid-year adjustment to the Fire-Rescue Department budget. The over budget personnel costs highlighted a need to reevaluate the constant staffing budgeting methodology employed by the department. Projected expense overages in overtime, hourly wages, special pays, vacation pay in lieu, industrial leave, and other non-production time categories (e.g. vacation, sick leave, etc.) fell short of savings in salaried wages and fringe costs. In theory, in accordance with the constant staffing budgeting methodology, overtime and personnel expense overages are to be fully offset by savings in salary and fringe benefits. Financial Management and Fire-Rescue worked together to conduct an historical trend analysis to identify the cause of the over budget personnel expenses, which resulted in a recommended increase in the overtime budget for the department. As a result of this recommendation, the FY 2013 Adopted Budget includes the addition of $7.1 million in overtime expenses over the FY 2012 budget. The increase in the overtime budget is partially offset by a $1.5 million increase in the department's budgeted vacancy savings. Overall, the net adjustment in personnel expense for the Department totaled $5.7 million.

The personnel budget adjustments were intended to meet the department's true operational needs and reflect historical trends, as a part of a phased approach to addressing personnel budget overages. At the time, Fire-Rescue expressed that the increase in the overtime budget could possibly still not meet the actual overtime needs of the department in FY 2013, and that the coming fiscal year would provide an opportunity to see whether any additional adjustments are warranted. As was discussed in the 1st Quarter Report, the Fire-Rescue Department is currently projected to end the year at $2.0 million over budget in personnel expenses. The $2.0 million net overage is primarily related to a $4.0 million increase in overtime that is offset by savings of $2.0 million in salary and fringe costs. This indicates that additional adjustments to the department's personnel budget may be warranted.

Unrealized Managed Competition Savings

As noted in the First Quarter Report, $2.3 million of estimated General Fund savings from Fleet Maintenance managed competition are not expected to be realized during FY 2013. The delay in implementation of the Employee Proposal Team's (EPT) managed competition proposal is due to a longer than expected meet and confer process, and the subsequent time needed to put contracts in place for proposed outsourced work. Additionally, further negotiations are expected to take place regarding the outsourcing of heavy tire maintenance. Because of ongoing meet and confer work needed for the proposed outsourcing of this function, and the need for Council approval of the outsourced contracts included in the EPT proposal, implementation may not occur before the end of the fiscal year.

Implementation of Street Sweeping managed competition went live on December 1, 2012. The FY 2013 Adopted Budget included savings from this managed competition process of $560,000 based on a scheduled live date of July 1, 2012. Although some partial savings were realized in both personnel and non personnel expenditures during these months, the full annual savings estimate of approximately $560,000 is not expected to be realized for FY 2013 due to this delay.

Election Costs

Elections costs for FY 2013 were budgeted at $1.8 million, which included the cost for ballot measures and a number of elections that were not required due to candidate victories in June primaries. Due to this reduction in required costs for the November General Election, the 1st Quarter Report estimated election costs for FY 2013 at $250,000. However, subsequent to preparation of the 1st Quarter Report, it became known that a Special Election will need to be held for the District 4 Council seat due to the anticipated resignation of Councilmember Young at the end of December. Based on discussions with the City Clerk, a reasonable estimate for FY 2013 elections costs, which would include the District 4 Special Election, is $650,000. This would be $400,000 higher than the $250,000 estimated in the 1st Quarter Report.

Potential Impacts of Redevelopment Dissolution

The fiscal impact to the General Fund from the dissolution of the City's former Redevelopment Agency (RDA) is still unclear, but there is a high level of risk in FY 2013 which is discussed in the following sections.

Potential Expenditure Impacts

On October 19, 2012, the State Department of Finance (DOF) denied several items on the Recognized Obligation Payment Schedule (ROPS) 3 for the period January through June 2013. This includes debt service repayments between the City and the former RDA for improvements to Petco Park, the expansion of the Convention Center Phase II, and miscellaneous startup / general debt. Successor Agency staff went through the Meet and Confer appeal process on November 29th to provide justification for the disputed items and anticipate receiving a final ruling from DOF no later than December 18th. FY 2013 payments for the Convention Center and Petco Park were already made under ROPS 2 (July-December 2012) from Successor Agency reserve balances. However, if the DOF 's final determination invalidates the debt repayment agreements, the State Controller could exercise its right under the "claw-back" provision of AB

26 to order the City to reimburse the Successor Agency for any payments previously made under those agreements dating back to January 1, 2011. If this occurs, the City would have to rely on the General Fund to make the total $28.0 million payment to the County Auditor and Controller (CAC), likely in the April-June timeframe. This includes two annual payments made for the Convention Center Phase II expansion and Petco Park improvements in FY 2013 and FY 2012 totaling $4.5 million and $22.6 million, respectively. It also includes one payment of $867,407 that was made in FY 2012 under an agreement between the City and former RDA for repayment of startup/general debt. City has about $28.5 million available in the General Fund Reserve which could be used as a one-time source to mitigate the clawback.

Another potential impact to the General Fund in FY 2013 is related to the Successor Agency's administrative budget. Thus far, the budget has been funded with Redevelopment Property Tax Trust Fund (RPTTF) monies and unobligated reserve balances of the former RDA.

	ROPS 2 (July-Dec. 2012)	**ROPS 3** (Jan.-June 2013)	**TOTAL**
Total Budget (Successor Agency + City of San Diego	3,472,000	4,358,000	7,830,000
Revenues from RPTTF	318,461	647,757	966,218
Revenues from Reserves of Former RDA	3,153,539	3,710,243	6,863,782

Since the administrative cost allowance for the Successor Agency is 3 percent of enforceable obligations paid with RPTTF, the DOF's rejection of various line items in ROPS 3 has resulted in a corresponding reduction of $2.1 million to the RPTTF administrative allowance from about $2.8 million to $648,000. In addition, the DOF reclassified two items on the ROPS as administrative costs that must be paid from the administrative cost allowance. These items totaled $450,000, including $200,000 for the required annual audit of the Successor Agency's financial statements and $250,000 for the Oversight Board's legal counsel. If the DOF's objections are upheld and the DOF does not allow the Successor Agency to use non-RPTTF sources of funding for administrative costs, the City will have to make difficult decisions about providing supplemental funding for the administrative budget from the General Fund or further reducing Successor Agency staff. While the Successor Agency has relied on reserves to fund the majority of the administrative budget, as discussed below, it will be required to remit any unobligated reserve balances to the CAC following the completion of the non-LMIHF audit in late December.

Potential Revenue Impacts

The FY 2013 Approved Budget assumes that the City will receive a $2.4 pass-through payment from each of the CAC's RPTTF distributions (January 2nd and June 1st), which is considered General Fund property tax revenue. While the City received $2.4 million from the June 1, 2012 distribution, the CAC's RPTTF pass-through payment to the City for the period covering June through December 2012 is estimated to be about $1.6 million—$800,000 less than anticipated.

Per AB 1484, the Successor Agency retained the services of a licensed accountant to review unobligated Low and Moderate Income Housing Fund (LMIHF) and other reserve fund balances available for transfer to the CAC for distribution to local taxing entities. The audit of the LMIHF was issued on November 29th and concluded that no unobligated funds are available for remittance to CAC. In fact, the audit concluded that the Housing Successor Agency needs $10.2 million of RPTTF in the next few years in addition to funds currently on hand to pay all obligations. However, the LMIHF audit report is not considered final until it is approved by both the Oversight Board and DOF. In cases with other jurisdictions, the DOF has been asserting that the Successor Housing Agency owes a greater amount of unobligated housing balances to the CAC than reflected in the audit report, even when the report has been approved by the Oversight Board.

The audit of non-LMIHF balances is expected to be completed in December 2012. The amount that the City may receive could depend largely on whether the DOF ultimately approves several items in ROPS 3 that were expected to be paid from reserves, but which have been preliminarily challenged by the DOF. It is uncertain at this time how much money will be owed by the Successor Agency to the CAC as a result of this audit and whether the Successor Agency will possess adequate funds to make the required payment. If the Successor Agency has inadequate funds to make the payment, then it is expected that the City will need to make up any deficiency. AB 1484 allows the State to withhold sales and use taxes from the City or RPTTF distributions from the Successor Agency in order collect any underpayment or late payment of the unobligated balances.

CONCLUSION

In summary, the 1st Quarter Report does not highlight any significant areas of fiscal concern that could greatly impact General Fund projections for FY 2013. However, our Office has identified some additional items of note for departmental revenue and expenditures that should be monitored and potentially addressed in the Mid-Year Budget Monitoring Report, including Fire-Rescue overtime, parking citation revenue, and election costs, among others. Fiscal impacts on the City due to the elimination of the City's redevelopment agency should also be diligently monitored due to the potential significant affect on current year General Fund operations and the need to utilize reserves or reduce expenditures to offset any impact.

Seth Gates
Fiscal & Policy Analyst

Melinda A. Nickelberry

Melinda Nickelberry
Fiscal & Policy Analyst

Erin Noel
Fiscal & Policy Analyst

Lisa Byrne
Fiscal & Policy Analyst

Jeff Kawar
Fiscal & Policy Analyst

Nicole Nelson
Research Analyst

APPROVED: Andrea Tevlin
Independent Budget Analyst