

Financial Strategic Plan



Financial Strategic Plan

I. Background

The Financial Strategic Plan (Plan) is the City's long-range budget planning tool to project, and provide responses to, fluctuations in structural revenue and expense in the General Fund. Designed initially to recover from a projected structural deficit between the fiscal years 2004 – 2006, the Plan has now evolved to begin planning for fiscal years 2007 – 2009, as a three-year planning window allows for increased accuracy in projections based upon more concrete operational and financial assumptions. The Plan, as has been the case since its inception, will be updated each year to reassess the condition of the General Fund, address changes in the financial and service delivery environment, and to make appropriate adjustments to ensure it reflects the City Council's priorities and input from the community. This section of the budget book is designed to provide a brief synopsis of the Plan's history, detailed information on the Plan's direction for the Fiscal Year 2007 (FY 07) and an outlook for the subsequent two fiscal years.

II. Development of the Financial Strategic Plan

In September 2002, the Mayor and City Council directed City Staff to create a Plan to address the City's burgeoning structural deficit in the General Fund, which was projected to reach approximately \$102 million over the next three years if the City took no action. The Plan would eliminate the City's reliance on one-time revenues to balance its budget by rationally and responsibly bringing ongoing spending in line with ongoing revenues and restore structural balance to the General Fund budget. Seeking a reasoned approach within which the organization could make the necessary adjustments, the Mayor and City Council called for the development of the Plan to balance the budget.

The Plan was unveiled to the City Council on January 7, 2003. To ensure a broad base of support, the City Manager and his staff presented the proposed Plan to the City Council and held over 80 community meetings to brief community stakeholders on the Plan's approach to balancing the budget, discuss potential impacts and to answer questions and collect input for the City Council's consideration. After two months of intense review, the City Council officially endorsed the Plan on March 25, 2003.

Each spring and summer since the Plan was endorsed, the City has maintained the tradition of transparency and inclusiveness by conducting extensive outreach while updating the Plan's assumptions and proposals. Please see **Section V** below for a more detailed discussion of the City's community participation strategy through the Plan.

III. Plan Accomplishments FY 04 – FY 06

The City has made significant progress in its effort to reduce its General Fund structural deficit over the past three years through both strategic cost reductions and revenue increases. Under City Council leadership, Plan solutions were adopted with the annual budget each fiscal year, implementing \$92 million in structural deficit solutions from FY 04 – FY 06. Hundreds of difficult decisions were made in attacking the structural deficit, including \$62 million in cost reductions, e.g., the removal of over 250 vehicles from the City's fleet, elimination of more than 400 City positions, closing City Hall East and restructuring the City's operations to save money including Code Enforcement and the Workers' Compensation program. Other more difficult service reductions included Library hours cut by 20-30 percent, a 35 percent reduction in books, media and electronic materials available to customers, as well as deferred funding for facility maintenance in various departments.

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With these and other cost reductions, remaining employees were asked to “do more with less,” resulting in increased turnaround and response times for traditional customer service activities such as gas turn-ons/offers, tree trimming, street repair and facility maintenance. To avoid further service reductions, a total of \$26 million in annual revenue adjustments were made with increased return on assets and improved cost recovery through new and updated fees.

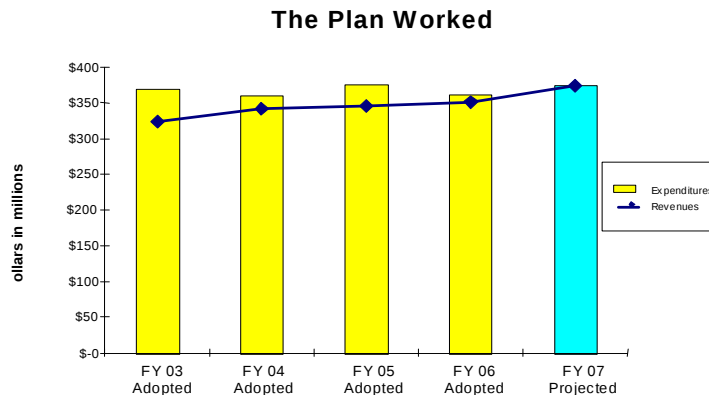
Given the level of reductions during a relatively short period of time, combined with the inability to achieve the level of negotiated employee concessions anticipated in the original Plan, a one-year extension to the Plan was endorsed by the City Council to allow time to develop alternate solutions to solve the remaining \$10 million of the projected \$102 million deficit. **Table 1** below reflects the success of the Plan in addressing the structural deficit from FY 04 – FY 06.

Table 1: Impact on the Structural Deficit FY 04 to FY 06

Beginning Projected General Fund Structural Deficit		\$102 million
Plan Year One: FY 04 Achieved Solutions	- \$41 million	
Plan Year Two: FY 05 Achieved Solutions	- \$29 million	
Plan Year Three: FY 06 Adopted Solutions	- \$22 million	
Total Structural Solutions: FY 04 – FY 06		\$92 million
Structural Deficit to be Solved FY 07		\$10 million

IV. Positioning for the Future: FY 07 – FY 09

The FY 07 Adopted Budget provides solutions to eliminate the last \$10 million of structural deficit. As projected, the Plan worked in its initial task of gradually aligning the General Fund's ongoing revenue with ongoing expenses.



In compliance with the City Council's Financial Policy on achieving and maintaining a *Structurally Balanced Budget*, the adopted General Fund budget is without a structural budget deficit for the first time in over two decades. While this may seem like a trivial distinction, it couldn't be any more significant. The City now has an equal amount of recurring revenue to support its critical recurring expenses for programs and services such as police, fire, libraries, recreation and public works. There is no longer an overarching threat that a core service would be cut because one-time revenues needed to fund such services did not materialize. Such fiscal stability not only places the City on a more sustainable service delivery and planning footing in the short-term, it allows the City to begin making long-term investments

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and utilizing long-term strategies to improve the quality of life for years to come. It also sends a clear sign to credit rating agencies and outside interests that Long Beach is a safe, responsible place to make investments. In fact, as a testament to the direct impact of the Plan, after years under a *negative watch* the City's credit rating was increased to *stable* in recent months.

The FY 07 Adopted Budget solves the \$10 million deficit using many of the same tools employed in previous years. As anticipated in the Plan, base revenues are showing natural growth now that the final Utility Users Tax reduction occurred in 2005. In addition, after three years of cuts to department budgets and services to the community, to eliminate the structural deficit the City Manager utilized a combination of: budget savings through optimization; appropriately allocated General Fund costs to other funds where the services are actually provided; increased cost recovery through new and adjusted fees; and savings generated by improvements in daily business practices. As promised to the City Council, no further library reductions are included in the FY 07 Adopted Budget. Specifically, the structural balance was achieved through:

- Budget savings through optimization (\$4.9 million)
 - o Improvement planned through optimization efforts including reprographics and helicopter maintenance
 - o Savings from the Employee Health Benefit optimization, generating savings while maintaining current health insurance services
- Appropriately allocated General Fund costs to other funds where the services are actually provided (\$3.7 million)
 - o Most Planning and Building functions were transferred to a new Development Services Fund, eliminating the traditional General Fund subsidy provided for the department's services
 - o Correctly assign Parks, Recreation and Marine administrative and management costs associated with Tidelands activities to the Tidelands Fund
 - o All appropriate Community Development administrative costs were allocated across its operations and funds
 - o Full cost allocation to enterprise funds for Police and Fire safety services
- Increased cost recovery through new and adjusted fees (\$1.4 million)
\$1.4 million in new and increased General Fund fee revenue were adopted

Table 2 below summarizes the deficit reduction solutions developed during the four years since the Plan was first endorsed by the City Council.

Table 2: Summary of Financial Strategic Plan Solutions – FY 04 – FY 07

	FY 04	FY 05	FY 06	FY 07
Structural Budget Gap	\$60	\$39	\$3	\$ -
Prior Year Deficit	-	19	29	10.0
Cost Reductions	28	22	16	7.4
Revenue Adjustments	13	7	6	2.6
Remaining Structural Deficit	\$19	\$29	\$10	\$ 0

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As a testament to the significance of what has been accomplished to date, the City's approach to long-range planning through the Plan has been highlighted as a best practice in an upcoming book being published by the Government Finance Officers' Association (GFOA) entitled, *Long-Term Financial Planning*. According to the GFOA:

"The elements of revenue and expenditure projection, fiscal environment analysis, gap identification, gap-closing strategy development, and cooperation and communication between a wide-range of stakeholder groups, including elected officials, staff, and citizens, are all hallmarks of successful long-term financial planning. Long Beach's story demonstrates the critical role that long-term financial planning can play in securing the financial position of a government. Long-term financial planning is not just a one-time event in response to crisis. Long Beach's experience illustrates this point, too."

Because the structural deficit is solved does not mean that the Plan is now obsolete. On the contrary, the Plan by design will now evolve into a tool to help manage and maintain the hard-earned structural balance as the City's financial and service delivery environments change over time, and plan for future investments. Thus, the Plan as presented below now incorporates FY 08 and FY 09 into its three-year outlook.

General Fund revenue projections over the next three years continue to show growth at a positive, steady pace. As expected, once the 5-year reduction to the Utility User Tax rate was complete, the City began to realize regular growth in annual revenue. Factoring in the recent indications that the national real estate market is seeing a cooling trend and the impact this might have on the City's property tax revenue, and impacts on the economy from historic cost of oil, it is estimated aggregate General Fund base recurring revenue will grow by \$8.3 million in FY 08 and an additional \$9.4 million in FY 09.

There are several changing financial conditions in the next few years that will have a definitive impact on the General Fund's standing for which the City must begin planning. Despite steady growth in recurring revenue sources, given the inevitability of emergent, unforeseen service needs and cost growth, these increasing expenses certainly have the potential of outpacing revenue growth if not closely monitored.

These include, but are not limited to:

- The City recently concluded negotiations with all of its employees, which included salary increases through FY 08 for all Fire sworn and Miscellaneous personnel, and police sworn through FY 09 (with civilian management only receiving performance-based increases, if at all). Over the two years combined, the impact of these negotiations on the General Fund is \$7.5 million for sworn personnel and an additional \$3.1 million for non-sworn employees.
- Starting in FY 08 in accordance with the City Council's Financial Policy on *Use on New Discretionary Revenue*, the City must make further investments in infrastructure equal to 10 percent of new, net general Fund structural revenue. According to current projections, this represents \$827,000 in FY 08 and an additional \$935,000 in FY 09, combined projected to be over \$1.7 million of ongoing infrastructure investment.
- General liability insurance costs continue to increase in the post-Katrina market. In FY 07, the City saw a 10.5 percent increase over FY 06, and it is projected that the City will face at least 8 percent annual increases (or approximately \$425,000 in FY 08 and \$458,000 in FY 09) over the next several years as the market recovers from the its recent significant losses.

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Table 3 below summarizes the structural budget projections for the General Fund from FY 07 – FY 09.

Table 3: Adopted/Projected Financial Strategic Plan – FY 07 – FY 09

(In structural increments, in millions)				
<u>Fiscal Year</u>	<u>FY 07</u>	<u>FY 08</u>	<u>FY 09</u>	
Adopted/Projected Structural Revenue	\$364.8	\$373.9	\$383.3	
Includes:				
<i>Secured Property Tax</i>		1.2	2.0	
<i>Sales Tax and In-Lieu Sales Tax (Backfill)</i>		1.3	1.7	
<i>Utility Users Tax</i>		1.2	.7	
<i>Vehicle License Fees and In-Lieu VLF (Backfill)</i>		.7	.8	
Adopted/Projected Structural Expenditures	\$364.7	\$372.4	\$376.3	
Includes:				
<i>Restoration of Library Services</i>	1.3			
<i>Police, Fire, Miscellaneous, Engineers and Other Negotiated Salary Increase (1)</i>		7.2	3.4	
<i>Debt Service</i>		(1.8)		
<i>PERS Costs</i>		(1.9)		
<i>10 percent New Discretionary Revenue Set Aside for Capital</i>		.8	.9	
Adopted/Estimated Structural Surplus/ (Deficit)	\$.1	\$ 1.5	\$ 7.0	
<u>Projected Potential Cost Increases on the Horizon</u>				
Estimated Police Department Longevity Pay Incentive			\$4.4	
Estimated Police Officers Adjustment to Median in FY 10			\$10-\$15	
Estimated Annual Debt Service on City Hall Seismic Retrofit			\$3.5	
Estimated Annual Set-aside to Fund GASB 45 Liabilities			\$2.5	
Fire and Misc. Employees Negotiations in FY 08/09 (cost per each 1% increase)			\$1.5	
<i>(1) This only includes the negotiated Police salary increases in FY 09; other Bargaining Unit agreements expire in FY 07 and FY08.</i>				

Despite several issues driving cost increases in the General Fund, the pace of growth in structural revenue will keep pace and maintain a structural balance during this next phase of the Plan. There are several additional costs however, that are not factored into the structural calculations, as they remain largely unknown. As noted at the bottom of the chart above, these include, but are not limited to:

- As recommended by the Mayor during the budget adoption process, the recently negotiated contract with the Police Officers Association was reopened and a 5 percent and 10 percent longevity incentive was granted for police officers with 10 and 15 years experience, respectively.
- Anticipated cost of the negotiated increase to the median for sworn police personnel. Taking into consideration pay increases at other agencies, the exact cost for this commitment could be as high as \$10 - \$15 million depending on where LBPD salaries rank amongst the ten comparable agencies on September 30, 2009.

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- Fire sworn and all other non-sworn employee agreements expire after FY 08. While the potential structural impact to the General Fund from future negotiated increases is impossible to predict, the cost for each 1 percent increase in salary for Fire sworn and Miscellaneous personnel is approximately \$687,000 and \$818,000, respectively. A cost of living increase of 3 percent alone would add \$4.5 million in structural expenses to the General Fund.
- City Hall must undergo a seismic retrofit to ensure the safety of the community and our workforce should a significant earthquake occur. The current estimated cost of the entire project likely exceeds \$40 million, bond funding for which would require annual debt service payments of about \$3.5 million over 30 years.
- The Government Accounting Standards Board (GASB) has issued a new standard (#45) that requires agencies to recognize projected retiree health care costs as a liability. The annual cost to fund this liability is still being evaluated, and as an example a 1 percent rate would cost the General Fund \$2.5 million.

With the specter of these potentially significant liabilities in our near future, the City must continue to take a fiscally prudent approach to the use of available General Fund resources. After several years of program constriction and deferment of critical projects, it will be difficult to resist the desire to immediately restore what has been lost and encumber resources that are available in the short-term. However, a key tenet of fiscal sustainability and prudence dictates that the City must maintain a long-term approach to ensure it does not compromise the fiscal stability it works so hard to attain.

V. Budget Summit and Community Involvement

On July 8, 2006 the City previewed the FY 07 Proposed Budget for the community at the fourth annual *Budget Summit: Community Voices and Budget Choices* workshop. This event was designed as an opportunity to inform the community on proposed changes to the budget before it was officially presented to the City Council in August, answer questions and solicit feedback. Over 100 members of the community and employees attended the workshop to discuss structural deficit elimination strategies in FY 07 Proposed Budget as well as learn about departments' significant issues, strategic objectives, programs and service. Community members also had the opportunity to ask direct one-on-one questions and to engage in a dialogue with department directors and City officials about a broad array of budgetary and services delivery issues.

The citywide Budget Summit was one component of the outreach efforts scheduled during the FY 07 budget process. Starting in January 2006, the City Council and the Budget Oversight Committee hold many public meetings to discuss implementation of FY 06 Plan solutions and the development of the FY 07 Proposed Budget in detail. In April, May and June, City Manager and Financial Management staff visited over 60 neighborhood, commission and committee meetings as well, in an effort to disseminate information about the budget and generate community input on possible solutions. The Mayor and City Council held additional public budget workshops and hearings throughout August and September to discuss the Plan's impacts, made recommendations and adopted final Plan solutions with the FY 07 Budget on September 12, 2006.