

NOTICE OF SPECIAL MEETING

Pursuant to Section 54956 of the Government Code of the State of California, a Special meeting of the **Tracy City Council** is hereby called for:

- Date/Time:** **Tuesday, April 4, 2023, 5:30 p.m.**
(or as soon thereafter as possible)
- Location:** **A quorum of City Council will be in attendance at:**
Tracy City Hall
333 Civic Center Plaza, Tracy, CA.
and
A Council Member will attend remotely at the following location:
Mardi Gras Hotel
3500 Paradise Road
Las Vegas, Nevada 89169

Government Code Section 54954.3 states that every public meeting shall provide an opportunity for the public to address the Tracy City Council on any item, before or during consideration of the item, however no action shall be taken on any item not on the agenda.

This meeting will be open to the public for in-person and remote participation pursuant to Government Code Section 54953(e)

For Remote Public Comment:

During the Items from the Audience, public comment will be accepted via the options listed below. If you would like to comment remotely, please follow the protocols below:

- *Comments via:*
 - **Online by visiting** <https://cityoftracyevents.webex.com> and using the following **Event Number: 2559 919 4332** and **Event Password: TracyCC**
 - ***If you would like to participate in the public comment anonymously***, you may submit your comment via phone or in WebEx by typing “Anonymous” when prompted to provide a First and Last Name and inserting Anonymous@example.com when prompted to provide an email address.
 - **Join by phone by dialing +1-408-418-9388**, enter 25599194332#8722922# Press *3 to raise the hand icon to speak on an item
- *Protocols for commenting via WebEx:*
 - *If you wish to comment under “Items from the Audience/Public Comment” portion of the agenda:*
 - *Listen for the Mayor to open “Items from the Audience/Public Comment”, then raise your hand to speak by clicking on the Hand icon on the Participants panel to the right of your screen.*
 - *If you no longer wish to comment, you may lower your hand by clicking on the Hand icon again.*
 - *Comments for the “Items from the Audience/Public Comment” will be accepted until the public comment period is closed.*

1. Call to Order
2. Actions, by Motion, of City Council pursuant to AB 2449, if any
3. Roll Call
4. ITEMS FROM THE AUDIENCE - *In accordance with Council Meeting Protocols and Rules of Procedure, adopted by Resolution No. 2019-240, and last amended by Resolution No. 2021-049, a five-minute maximum time limit per speaker will apply to all individuals speaking during "Items from the Audience/Public Comment". For non-agendized items, Council Members may briefly respond to statements made or questions posed by individuals during public comment; ask questions for clarification; direct the individual to the appropriate staff member; or request that the matter be placed on a future agenda or that staff provide additional information to Council.*
5. CITY COUNCIL CONDUCT A WORKSHOP TO REVIEW THE FIVE-YEAR FORECAST FOR THE CITY'S GENERAL FUND AND PROVIDE FEEDBACK REGARDING THE DEVELOPMENT OF THE FY2023/24 OPERATING AND CAPITAL BUDGET.
6. Council Items and Comments
7. Adjournment



Mayor

Posting Date: March 30, 2023

The City of Tracy is in compliance with the Americans with Disabilities Act and will make all reasonable accommodations for the disabled to participate in employment, programs and facilities. Persons requiring assistance or auxiliary aids in order to participate, should contact the City Manager's Office at (209) 831-6000 at least 24 hours prior to the meeting.

AGENDA ITEM 5

RECOMMENDATION

Staff recommends that the City Council conduct a workshop to review the Five-year forecast for the City's General Fund and provide feedback regarding the development of the FY2023/24 operating and capital budget.

EXECUTIVE SUMMARY

A financial forecast allows the creation of a sustainable financial vision for the City. A forecast does not remain static; it is a dynamic tool that allows for consideration of the most reasonable outcomes. The City's forecast will continue to be updated annually to allow the City to better anticipate future challenges and opportunities, thereby creating a solid foundation to make strategic decisions about the City's financial position. The forecast reflects economic estimations and assumptions based upon what is known today and provides guidance on what may be coming ahead. It should be used to provide guidance and policy direction to staff related to the development of the operating, capital, and liabilities budget. Following this discussion, staff will seek direction from the City Council on the City's preliminary FY 2023-24 Operating and Capital Budget.

BACKGROUND AND LEGISLATIVE HISTORY

The City Council of Tracy remains committed to maintaining fiscal sustainability while providing high quality public safety, public works, and community development to meet its existing and future needs. In 2020, the Council adopted a two-year Strategic Priority Work Plan and identified desired outcomes related to the City's social, economic, organizational, and environmental landscape. The Council adopted a governance strategy designed to retain and attract talent, enhance fiscal stability, improve the use of technology, and enhance transparency for the betterment of the community. In response, a set of strategic priorities, goals and objectives were adopted to carry out the vision of the City Council. The Council's strategic priorities, along with their goals and objectives, are the foundation for development of the budget and forecast. In a February 2023 Council workshop, Council began the process of setting the 2023-2023 Strategic Priorities. Staff expects to return to Council in April 2023 to adopt the 2023-2025 Strategic Priorities.

The City prepares a five-year fiscal plan annually as a tool for the Council to meet these strategic priorities and budget development. The City's fiscal strategy includes the creation of a financial forecast to evaluate current and future fiscal conditions and is to guide policy and programmatic decisions. As part of building the multi-year forecast, the City uses information based on past, current, and projected financial conditions and has developed and maintains several tools to provide analytic measurements of future fiscal impacts. First, the forecast includes two separate actuarial studies to analyze the impacts of employee retirement benefits on the City's finances over time. One is focused on the fiscal impacts of

pension and one on retiree medical costs. These reports are updated every 2-3 years based on Government Accounting Standards Board (GASB) rules. Secondly, the City has three separate studies on revenue forecasts based on economic trends surrounding short and long-term retail and housing markets. The City overlays each of these studies into the planning documents to create a multi-faceted approach to fiscal analysis and planning.

The goal of the City's annual Operating and Capital budget is to provide a plan that allocates resources to meet the needs and desires of Tracy's residents. It balances City revenues and costs with community priorities and requirements. In preparing the FY 2023/24 Operating and Capital Budget, City staff reviewed the FY 2022/23 amended budget and estimated the expenditures and revenues anticipated for the next year, FY 2023/24. These trends are then applied to the short term (first five years) to see projected outcomes. It reflects current market conditions both for revenues and expenditures. The long-term (5-year) forecast applies more conservative revenue and expenditure trends that are indicative of the restrictiveness of revenues while applying current spending to measure the City's ability to sustain a fiscally balanced budget.

In 2021 and the first half of 2022, the economy saw rising housing prices that bolstered property tax and diversification of commercial and retail growth that strengthened the City's sales tax, hotel, and business tax revenues. In mid-2022, rising inflation and interest rates led to the slowing of residential home sales and less discretionary spending by consumers. The result is an overall slowing in the rate of General Fund revenue growth. With that being said, the economy has natural growth and contractions that are outside of the City's control. Even with solid financial planning and long-term forecasting, not all future outcomes can be predicted. Knowing that, the City has positioned itself well by building financial reserves, adopting strong fiscal policies, and passing important revenue measures to support City services. However, even with these proactive steps, the City, like other agencies, will continue to be faced with unmet needs in an environment where resources are limited.

Creating a forecast has helped identify future revenue and expenditure trends that may have an immediate or long-term influence on government policies, strategic goals, funding obligations, or community services. The City uses the five-year financial forecast as a management tool to best anticipate inflows and outflows of City resources in the short-term, then projects out these trends into the longer five-year model to ensure budget sustainability. Modeling of long-term strategies also allows marginal shifts to occur over time to maintain healthy reserves while still actively improving services to the public. The forecast has become an integral part of the annual and mid-budget process.

General Fund Fiscal Challenges and Recovery:

Shortly after the adoption of the FY 2021/22 Operating and Capital Budget, the City received the January-March 2021 Sales Tax (Bradley Burns State Sales Tax) disbursement from the State of California Department of Tax Franchise Administration (CDTFA), which resulted in a significant change in the City's

estimated revenues. The result was due to a recent change in tax reporting by a predominant sales tax producer. This reporting change shifted the tax allocation from a statewide allocation through the County sales tax pool where the tax was distributed pro-rata throughout the State to a local sales tax allocation based upon the businesses' point-of-sale or fulfillment of the sale. The change has had a significant impact on the City's General Fund revenues; nearly doubling the Sales Tax revenues for the City.

However, this revenue is not guaranteed as there is significant interest to have these funds reallocated to other jurisdictions. The City Council's ad-hoc fiscal sustainability committee met to discuss the instability of the funds and ways to ensure fiscal sustainability in the future, should the sales tax allocation change.

On December 7, 2021, and March 22, 2022, the City Council's ad-hoc fiscal sustainability committee recommended strategies for use of the General Fund surplus to City Council, which included pre-funding of CalPERS and retiree medical, funding to cover deferred maintenance for streets and parks, and a 3% increase to City services and programs. These fiscal sustainability strategies were adopted with the FY2022/23 operating budget.

In the long-term forecast, all but the program increases will stop being funded in FY 2026/27, the same year the potential Sales Tax revenues could be reduced. As a result, the five-year forecast shows that the General Fund is fiscally sustainable with the revenue growth from other tax sources and reduction on one-time funding commitments.

Table 1: Council Adopted Fiscal Sustainability Strategies

On-Going Revenue	Estimated			
	% of Revenues	FY23/24	FY24/25	FY25/26
General Fund Revenues*		\$132	\$137	\$141
CalPERS Pre-funding	2%	\$2.6M	\$2.7M	\$2.8M
Retiree Medical Pre-funding	2%	\$2.6M	\$2.7M	\$2.8M
Road Improvements - Deferred Mtc.	3%	\$4.0M	\$4.1M	\$4.2M
Parks - Deferred Mtc.	2%	\$2.6M	\$2.7M	\$2.8M
City Services and Program Increase	3%	\$4.0M	\$4.1M	\$4.2M
Total		\$15.8M	\$16.3M	\$16.8M

*Revenues defined as total General Fund revenues less Measure-V Sales Tax and Transfers In

General Fund Fiscal Highlights:

Revenue Trends

Property Tax: New housing units being added to the assessor's roll, coupled with commercial developments in the community, and higher property values, have led to a steady increase in local property tax revenues over the last few fiscal years. Property Tax revenue increased in FY 2021/22 over FY 2020/21 by \$3.3M, approximately 12%. As interest rates have risen, the local real estate market has seen residential sales slow, both in volume and price, with drops to the average residential selling price over the last two quarters. Commercial and industrial real estate sales have continued to see moderate growth. As property tax revenue lags 12-18 months behind market conditions, the City estimates FY2023/24 will see slowing with an estimated increase of 2-3%. Property tax will begin to grow in FY2024/25 by 5-7% annually over the following 4 years based on market turnover and valuation growth. In the long-term (5-year term), the City will see property tax slow to the 2% cap as allowed under Proposition 13.

Sales Tax (Bradley Burns): As mentioned above, at the beginning of FY 2020/21, the City's forecast showed year over year decline in reserves. The City's expenses were outpacing revenues despite a thriving housing and commercial market. Fast forward one year to the last quarter of FY 2021/22, the City's Bradley Burns Sales Tax has increased nearly 100% from prior years and has resulted in a significant change in the City's estimated General Fund revenues. The rapid growth seen in prior fiscal years has begun to slow as rising interest rates and inflation have slowed consumer spending. FY 2023/24's growth is projected at 2%. FY 2024/25 and FY 2025/26 are projected to regain a moderate amount of growth in the 3-4% range.

Sales Tax from Bradley Burns is now more than 50% of the City's total General Fund revenues because of this recent taxpayer allocation change. The City is currently tracking a policy discussion occurring within the League of California Cities to consider supporting legislation that would modify the allocation of Bradley Burns (1% of State Sales Tax) for ecommerce businesses statewide. This has the potential to have a significant impact to the City's Sales Tax revenues and its long-term forecast. As a result, staff continues to recommend that the 5-year forecast only shows the current Bradley Burns Sales Tax revenues from ecommerce in the short-term, until FY2025/26. The forecast has a decline of \$20M in FY 2026/2027 to reflect the risk of the Sales Tax revenues being reduced. By placing this decline in the forecast, the City will have the flexibility to see the potential outcomes on a conservative basis to understand what these future impacts could generate.

Measure V Sales Tax (Local Sales Tax): In November 2016, the City Council and voters passed an additional ½ cent local sales tax (known as Measure V) that has

a twenty-year sunset (expires April 2037). Over the last five years, the City Council has adopted several resolutions, which prioritized Measure V Sales Tax to fund multiple amenities located in the City: The Aquatic Center, Multigenerational Recreation Center, Legacy Fields Sports Complex, Ritter Family Ball Park, and the Nature Park. These capital expenditures demonstrate the City Council's Strategic Priority for improved Quality of Life and Economic Development. (See report on capital improvement projects for more discussion on these and other CIPs.)

Business License and Cannabis Tax

In November 2022, voters approved the modernization of the Business License Tax. The updated tax goes into effect on July 1, 2023 and is anticipated to bring an additional \$3.5 M in revenue to the General Fund.

Additionally, cannabis tax is an overlay component of business license tax classifications. The City Council and voters approved a Cannabis Tax in 2020, which provided a gross receipts tax on retail, distribution, and manufacturing and a square foot tax on cultivation. This tax could potentially generate an additional \$1-2M annually in General Fund revenues.

Expenditure Trends & Assumptions

Because it takes people to provide services, the City's General Fund personnel costs are more than 50% of operating expenses. Drivers of cost as it relates to personnel expenses over the forecast horizon include but are not limited to changes in labor agreements, health care, and CalPERS normal cost and unfunded liability.

The General Fund forecast is based upon the assumption of full staffing levels. Although some attrition can be expected, it is difficult to rely upon personnel savings to reduce annual expenditures. In addition, it is uncertain when and where the vacancies may occur and their potential impact on service demands. It is not a good practice to rely upon salary savings as a permanent cost saving measure.

The General Fund forecast includes an inflation factor of 3% for expenses in the short term and flattens to 1-2% in the long-term. This factor is used to maintain the current buying power of the City. The trends for non-personnel may rise higher than the forecast of 3% due to steep rise in inflation and supply chain disruptions currently in the market. The inflation factor may result in the City's costs rising higher than the forecast and reducing the overall buying power. The City will continue to monitor the inflation rate on goods and services as it has historically outpaced the City's revenue growth due to regulatory restrictions on revenues. Staff will continue to monitor the costs of goods and services and their impacts on a quarterly basis.

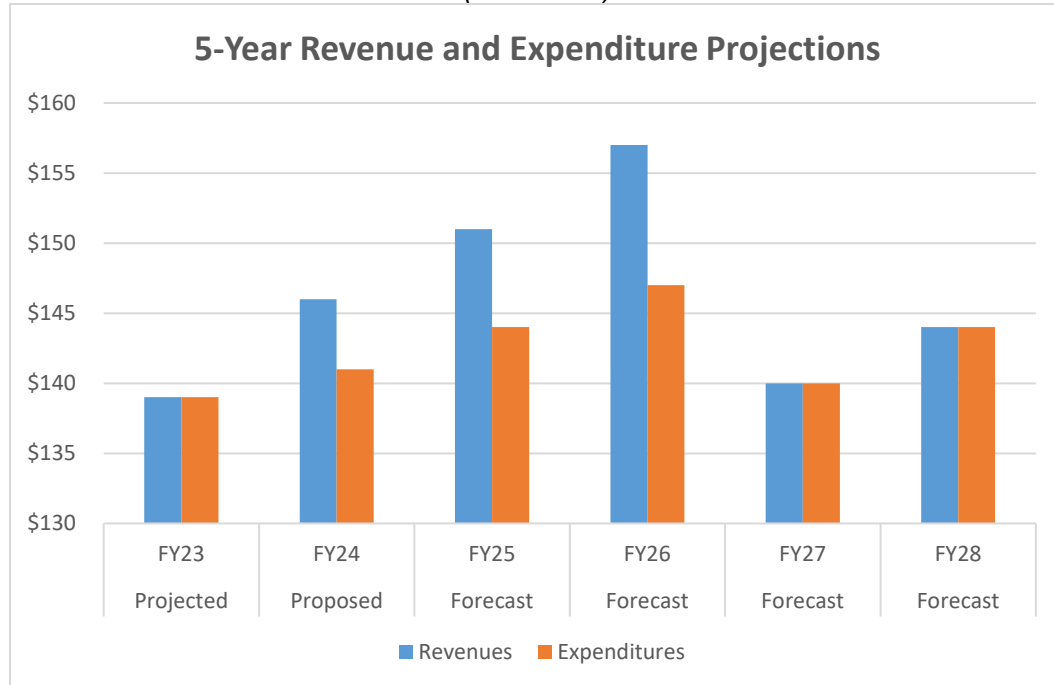
Table 2: 5-Year Forecast

(in Millions)

	Projected FY23	Proposed FY24	Forecast FY25	Forecast FY26	Forecast FY27	Forecast FY28
Revenues	\$139	\$146	\$151	\$157	\$140	\$144
Expenditures	\$139	\$141	\$144	\$147	\$140	\$144
Surplus/(Deficit)	\$0	\$5	\$7	\$10	\$0	\$0

Chart 1: 5-Year Revenue and Expenditure Projections

(In Millions)



GENERAL FUND RESERVES: The City’s General Fund is projected to have a surplus for the next three fiscal years, assuming the Sales Tax revenues collected today remain in place for the next three years.

**Table 3: 5-Year General Fund Uncommitted Reserves
 (In Millions)**

	Uncommitted Fund Balance	Cumulative Available for Future CIP
Actual FY 2022	\$7	\$7
Projected FY 2023	\$2	\$9
Proposed FY 2024	\$4	\$13
Forecast FY 2025	\$8	\$21
Forecast FY 2026	\$15	\$36
Forecast FY 2027	\$15	\$51
Forecast FY 2028	\$15	\$66

Pre-funding Pension/Medical Leave Liabilities: Adopted in the FY2022/23 budget, the City Council approved the recommendations from City Council’s Fiscal Sustainability Ad-Hoc Committee to begin setting aside funding for prefunding pension and retiree medical benefits, 2% of General Fund revenues, approximately \$2M each in the current fiscal year and is anticipated to equate to \$3M in future fiscal years. The prefunding drops off in FY 2027 when Sales Tax is projected to decline.

Deferred Maintenance and Capital Improvement Project: Included in the Forecast, is funding for deferred maintenance and capital improvement projects, such as road, building, and park improvement projects. Adopted fiscal sustainability strategies provide \$4M for road improvement deferred maintenance and \$3M for parks deferred maintenance. This funding drops off in FY 2027 when Sales Tax is projected to decline. It is estimated that the City could potentially set aside an additional \$66 million funding over the five-year period. These capital reserves could sustain the City’s deferred maintenance another 11 years at a spending rate of \$6M.

FISCAL IMPACT

There is no fiscal impact associated with this item. However, the five-year forecast is critical in establishing financial policy. The forecasted outcome has the potential to improve or worsen. Some potential outcomes that would improve the forecast would include higher employee vacancy rates (more vacant positions or vacancies for longer periods of time), delayed or weaker recessions, PERS investment gains, and stronger economic development activity beyond what is included in the forecast.

Potential outcomes that could worsen the forecast include: PERS investment losses (or additional discount rate cuts), weaker revenue growth, fewer new hotel rooms, delays, or closures in commercial activities, inflationary or recessionary losses, adjustment in labor COLAs, staffing beyond current levels assumed in the forecast, and unplanned, one-time expenditures.

STRATEGIC PLAN

This agenda item supports Governance Strategic Goal 3: Ensure Short and Long-term Financial Sustainability.

ACTION REQUESTED OF THE CITY COUNCIL

That the City Council conduct a workshop to review the five-year forecast for the City's General Fund and provide feedback regarding the development of the FY 2023/24 General Fund Operating and Capital Budget.

Prepared by: Sara Cowell, Director of Finance

Reviewed by: Karin Schnaider, Assistant City Manager
Nancy Ashjian, Assistant City Attorney

Approved by: Midori Lichtwardt, Acting City Manager

ATTACHMENTS

Attachment A – Five Year Forecast Power Point Presentation



**CITY COUNCIL WORKSHOP
FIVE-YEAR FORECAST
GENERAL FUND UPDATE FY 2023-2028**

April 4, 2023

Workshop Agenda

- Revenue and Expenditure Trends
- Use of Reserves
- Next Steps





Revenue and Expenditure Trends



Revenue Trends

- Property Tax
 - Short Term: 2-3% growth
 - Long Term: 4-5% growth
- Sales Tax
 - Short Term: 2% growth
 - Long Term: 3-4% growth in fiscal years 2024/25 and 2025/26
 - Estimated loss of \$20M in FY 2027 possible if ecommerce changes move forward
- Other Revenues
 - Business License modernization \$3.5M Increase
 - Adopted Fee Schedule Increases \$2M Increase
 - TOT (Hotel Tax) \$500k Increase

Expenditure Trends

- Salary and Benefits
 - Short Term: 2-3% growth
 - Long Term: 1-2% growth.
 - Only considers current employee contracts
 - Current employee contracts expire June 30, 2023
- Non-personnel
 - 3% growth for standard inflation
 - Current inflation rates are approximately 5%

Council Adopted Fiscal Sustainability Strategies

\$2M CalPERS (2% of revenues*)

\$2M Retiree Medical (2% of revenues*)

\$3M Deferred Maint. - Streets (3% of revenues*)

\$3M Deferred Maint. – Parks (2% of revenues*)

\$3M Program Increase (3% of revenues*)

\$12M budget increase FY23

*Revenues defined as total General Fund revenues less Measure V-Sales Tax and Transfers In



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Forecast of Fiscal Sustainability Strategies

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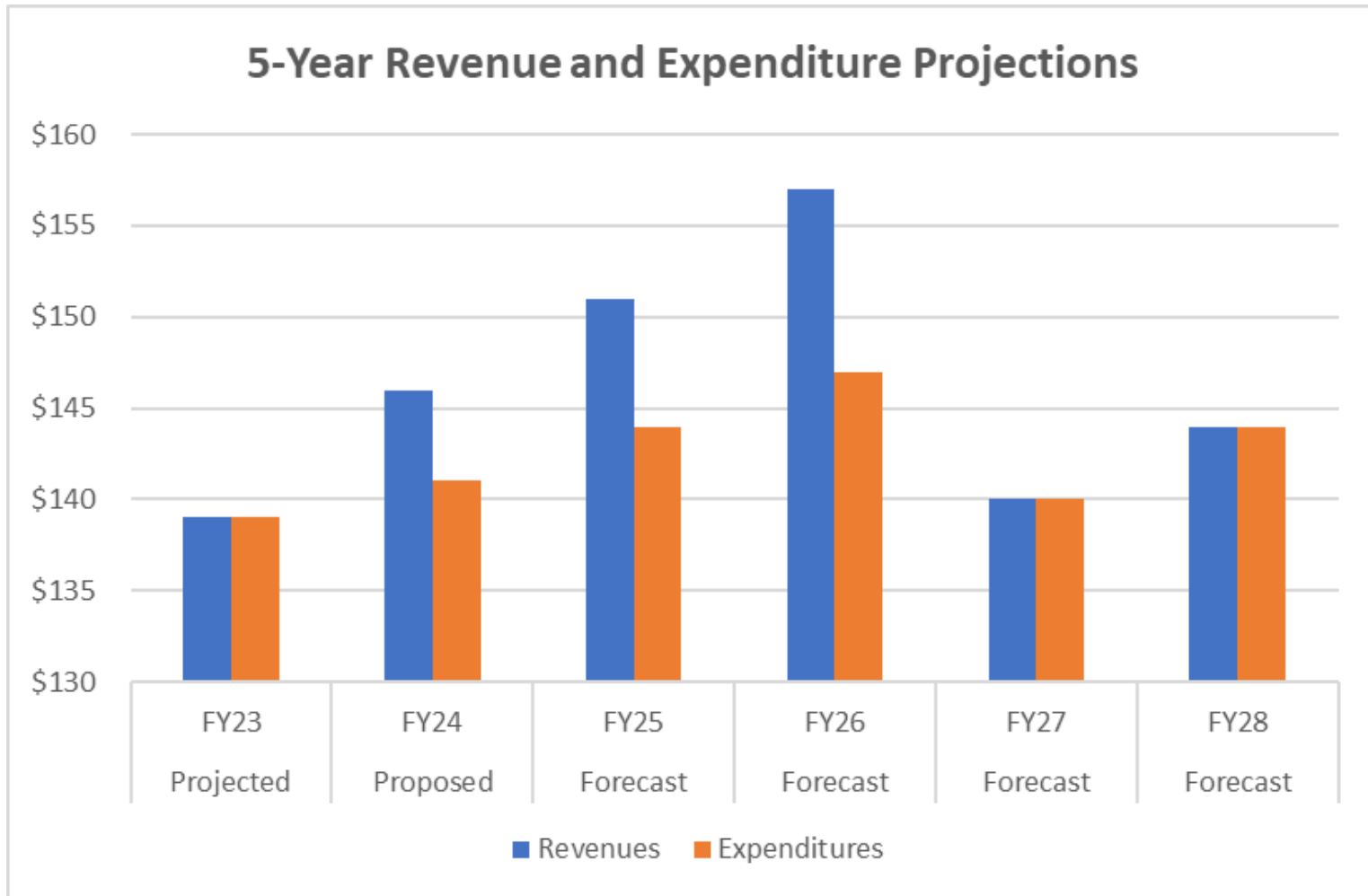


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General Fund 5-year Forecast FY 2023-2028

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General Fund 5-year Forecast FY 2023-2028

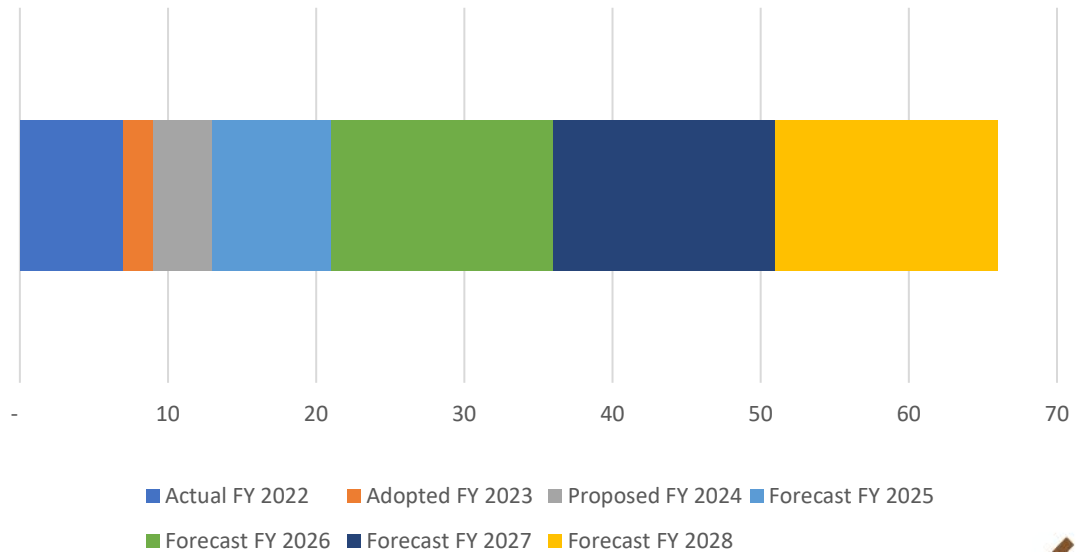


Think Inside the 'Triangle'



The City's General Fund is projected to have a surplus for the next three years, assuming the Sales Tax revenues collected today remain in place. The surplus could accumulate up to \$66M.

Uncommitted Fund Balance



Use of Forecast

- The forecast is meant to provide the City Council with potential impacts that could have a long-term impact of the fiscal sustainability of the General Fund.
- It provides indicators based on current trends and potential impacts as they are known today.



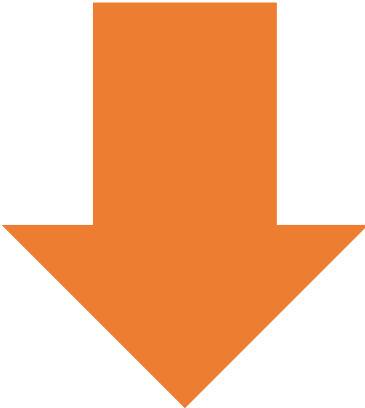


USE OF RESERVES





Use of Reserves: Offset Future Costs and Revenue Instability to Gain Fiscal Sustainability



Projected Revenues/Expenses

- 20M decrease in sales tax revenue expected FY27
- Expenses continue to rise



Prefunding Liabilities/New Revenue Sources

- Prefunding deferred maintenance
- Prefunding employee retiree benefits



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Next Steps





Next Steps

April 4, 2023

Staff will present the CIP Outlook and Measure V update during the regular Council meeting

April 19, 2023

Staff will present the proposed budget to the Finance Committee at its April 2023 meeting

June 6, 2023

Staff will return to Council on with the Proposed Operating and Capital Budget for FY 2023-24



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Q & A

