



Think Inside the Triangle™

## 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, March 5, 2024, 5:30 p.m.**  
(or as soon thereafter as possible)

**Location:** **Tracy City Hall**  
**333 Civic Center Plaza, Tracy, CA.**

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: 2555 063 6719** 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](mailto:Anonymous@example.com) when prompted to provide an email address.
  - Join by phone by dialing +1-408-418-9388, enter 25550636719#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 and Declaration of Conflicts
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. DISCUSSION ITEMS
  - 5.A The Tracy Finance Committee recommends that the City Council receive a report on the Five-year forecast for the City’s General Fund and provide direction regarding the City’s preliminary Fiscal Year 2024-25 Operating and Capital Budget.
6. Council Items and Comments
7. Adjournment

**Posting Date: February 29, 2024**

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.A

RECOMMENDATION

**The Tracy Finance Committee recommends that the City Council receive a report on the Five-year forecast for the City's General Fund and provide direction regarding the City's preliminary Fiscal Year 2024-25 Operating and Capital Budget.**

EXECUTIVE SUMMARY

This item is to provide a report on the five-year forecast for the City's General Fund. A financial forecast allows the creation of a sustainable financial vision for the City. A forecast 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.

In addition to providing the report, staff seeks direction on the City's preliminary Fiscal Year (FY) 2024-25 Operating and Capital Budget.

BACKGROUND AND LEGISLATIVE HISTORY

The City Council 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 2023, the City Council adopted a two-year Strategic Priority Work Plan and identified desired outcomes related to the City's social, economic, organizational, and environmental priorities. The City Council adopted a governance strategy designed to enhance fiscal stability, retain and attract new talent, improve the use of technology, and enhance transparency for the betterment of the Tracy 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 2023-2025 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 for the FY 2024/25 Operating and Capital Budget, City staff reviewed the FY 2023/24 amended budget and estimated the expenditures and revenues anticipated for the upcoming fiscal year, FY 2024/25. These trends are then applied to the short term (first year) 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.

### **Economic Outlook**

In 2022, the local economy saw housing prices continue to rise, which bolstered property tax and diversification of commercial and retail growth that strengthened the City's sales tax, hotel, and business tax revenues. In 2023, a shortage of homes for sale and high costs of borrowing had a negative impact on housing inventory and demand. With mortgage rates expected to decline over the next twelve months, it is expected the City will see a moderate increase in home prices.

The double-digit gains of the past two fiscal years have slowed in 2023 and consumer spending, while still positive, has slowed, with a focus on the balance between discretionary and demand spending. Rising consumer debt in auto loans are driving the reduction in discretionary spending by consumers. California's unemployment rate remains below 5%, while the San Joaquin County's unemployment rate has risen to 6.40%. The result of these factors is a continued 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-year 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. In 2022, CDTFA published a study related to sales tax specific to e-commerce, which reviewed the impacts of changing the method of sales tax allocation from the point of fulfillment to the point of delivery. The study showed that if this change occurred, the impact to the City would be 25% or greater from the City's current allocation. While no decision has been made, staff is tracking possible changes and their impacts. The forecast reflects a drop in sales tax beginning in FY2027-28.

With the 2022/23 operating budget, Council adopted a set of 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 continued with the FY2023/24 operating budget and are included in the short-term forecast through FY2026/27.

In the long-term forecast, all but the program increases will stop being funded in FY 2027/28, 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 in one-time funding commitments.

**Table 1: Council Adopted Fiscal Sustainability Strategies**

On-Going Revenue	Estimated			
	% of Revenues	FY24/25	FY25/26	FY26/27
General Fund Revenues*		\$135,308	\$138,612	\$142,343
CalPERS Pre-funding	2%	\$2.7M	\$2.8M	\$2.8M
Retiree Medical Pre-funding	2%	\$2.7M	\$2.8M	\$2.8M
Road Improvements - Deferred Mtc.	3%	\$4.0M	\$4.1M	\$4.2M
Parks - Deferred Mtc.	2%	\$2.7M	\$2.8M	\$2.8M
City Services and Program Increase	3%	\$4.0M	\$4.1M	\$4.2M
<b>Total</b>		<b>\$16.1M</b>	<b>\$16.6M</b>	<b>\$16.8M</b>

\*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. In 2023, continued interest hikes drove a reduction in the sale of existing homes, however, new construction continued to thrive in Tracy. In 2023, Tracy saw an increase in new home sales of 35%, from 322 in 2022 to 434 in 2023. This is largely due to the combination of a lack of inventory of existing homes and Tracy's affordability in comparison to bay area home prices. 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 FY2024/25 will see some slowing in the real estate market with an estimated increase of 2-3%. Property tax will begin to grow in FY2025/26 by 4-5% 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):** Over the last two fiscal years, the City's sales tax allocation from Bradley Burns rapidly increased as a result of changes from the CDTFA. The rapid growth seen in prior fiscal years has begun to slow as rising interest rates and inflation have slowed consumer spending. FY 2024/25's sales tax allocation is projected to decline by approximately 6%. FY 2025/26 is projected to regain a moderate amount of growth in the 2-3% range.

Sales Tax from Bradley Burns is now nearly 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 FY2026/27. The forecast has a phased decline of \$10M in FY 2027/2028, and a \$20M decline in FY 2028/29 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.

**Transient Occupancy Tax (TOT):** The Transient Occupancy Tax (TOT), is a tax collected on hotel stays within the City of Tracy. The TOT is currently 10%. With tourism statewide remaining strong, the City has seen TOT revenues remain steady. There are currently two new hotels under construction and three approved, but not yet constructed. The City is also in review of an additional four proposed hotels. It is expected that the two under construction will be completed in the upcoming fiscal year and as a result, the City can expect to see an increase in TOT revenue.

**Business License and Cannabis Tax:** In November 2022, voters approved the modernization of the Business License Tax. The updated tax went into effect on July 1, 2023 and is based upon a percentage of gross receipts varying from 0.1% - 0.3%, depending on business category. The updated tax increased Business Tax revenues by approximately \$6M and provides vital funding for community priorities, such as improving City streets and roads, public safety, and recreation programs.

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. In July 2023, Tracy's first Cannabis business opened. There are currently two Cannabis businesses open in Tracy. Like the Business Tax, Cannabis taxes are based on the gross receipts of the business. It is estimated that FY2023/24 Cannabis revenues will be \$500,000 and in the longer term, revenues are expected to increase as the number of Cannabis businesses open in the City.

### 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. Included in the forecast is a 3.5% increase in personnel costs associated with negotiated labor agreements.

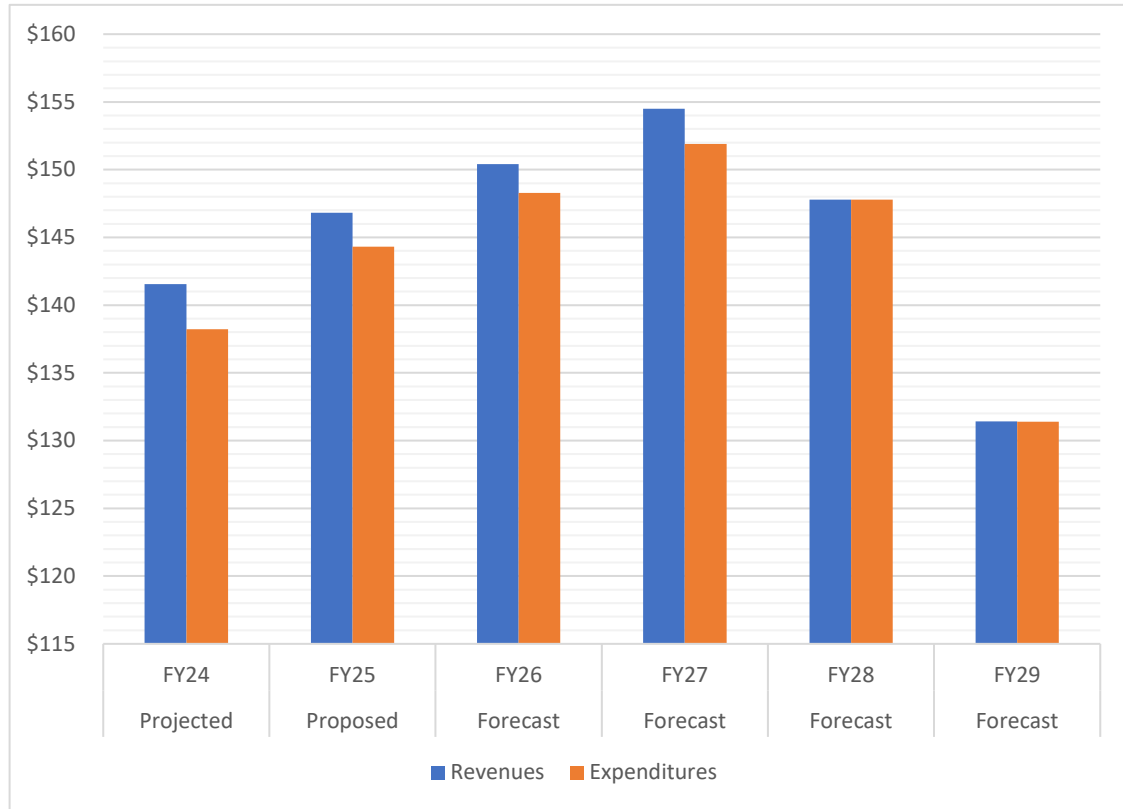
The General Fund forecast is based upon the assumption of full staffing levels. Although some attrition can be expected, it is difficult to rely upon personnel savings to reduce annual expenditures. In addition, it is uncertain when and where the vacancies may occur and their potential impact on service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

As a result of the COVID-19 pandemic, the Federal government issued the American Rescue Plan Act (ARPA). The City of Tracy received an allocation of \$14.8 million through ARPA. The City has used these funds towards various one-time and ongoing community priorities, such as, infrastructure repairs, economic development and homelessness. All ARPA funds must be committed or spent by December 31, 2023, resulting in a transition in funding from ARPA to the City's General Fund. Included in the forecast is \$1.5M in ongoing expenditures that will transition to the General Fund.

The General Fund forecast includes an inflation factor of 3% for non-personnel 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 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.



**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 2  
 5-Year Forecast**

(in Millions)

	Projected	Proposed	Forecast	Forecast	Forecast	Forecast
	FY24	FY25	FY26	FY27	FY28	FY29
Revenues	\$142	\$147	\$150	\$155	\$148	\$131
Expenditures	\$138	\$144	\$148	\$152	\$148	\$131
Surplus/Deficit	\$4	\$3	\$2	\$3	\$0	\$0

**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 \$4M each has been pre-funded to date and is anticipated to equate to \$3M in future fiscal years. The prefunding drops off in FY 2028 when Sales Tax is projected to decline.

**Deferred Maintenance and Capital Improvement Projects:** 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 2028 when Sales Tax is projected to decline.

### 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

The Tracy Finance Committee recommends that the City Council receive a report on the Five-year forecast for the City's General Fund and provide direction regarding the City's preliminary FY 2024-25 Operating and Capital Budget.

Prepared by: Sara Cowell, Director of Finance

Reviewed by: Bijal Patel, City Attorney  
Karin Schnaider, Assistant City Manager

Approved by: Midori Lichtwardt, City Manager

### ATTACHMENTS

Attachment A – Five Year Forecast Power Point Presentation



**CITY COUNCIL  
FIVE-YEAR FORECAST  
GENERAL FUND UPDATE FY 2024-2029**

MARCH 5, 2024

# Agenda

- Economic Outlook
- Revenue and Expenditure Trends
- Forecast
- Next Steps



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# Economic Outlook



# Economic Trends

- Tracy's local economy has remained stable despite rising interest rates and inflation.
- Home sales have remained steady
  - Low inventory of existing homes has bolstered new home sales.
  - Tracy housing remains more affordable than neighboring Bay Area homes.
- Consumer spending has begun to slow
  - Discretionary spending has slowed, as rising interest rates impact household budgets.





# 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 2025/26 and 2026/27
  - Estimated loss of \$10M in FY 2027 and \$20M in FY 2028 possible if ecommerce changes move forward



# Revenue Trends, Continued

- Other Revenues
  - Business License tax
    - Short Term: 3% growth
    - Long Term: 1-2% growth
  - TOT
    - Short Term: 10% growth
    - Long Term: 20% growth
  - Cannabis tax
    - Short Term: 50% growth
    - Long Term: 3% growth

# Expenditure Trends

- Salary and Benefits
  - Short Term: 3.5% growth
  - Long Term: 1-2% growth
  - Only considers current employee contracts, expiring June 30, 2025
- Non-personnel
  - Short Term: 3% growth for standard inflation
  - Long Term: 1-2% growth
    - Current inflation rates are approximately 3.1%

# Council Adopted Fiscal Sustainability Strategies

\$2.7M CalPERS (2% of revenues\*)

\$2.7M Retiree Medical (2% of revenues\*)

\$4.0M Deferred Maint. - Streets (3% of revenues\*)

\$2.7M Deferred Maint. – Parks (2% of revenues\*)

\$4.0M Program Increase (3% of revenues\*)

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\$16.1M budget increase FY25

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



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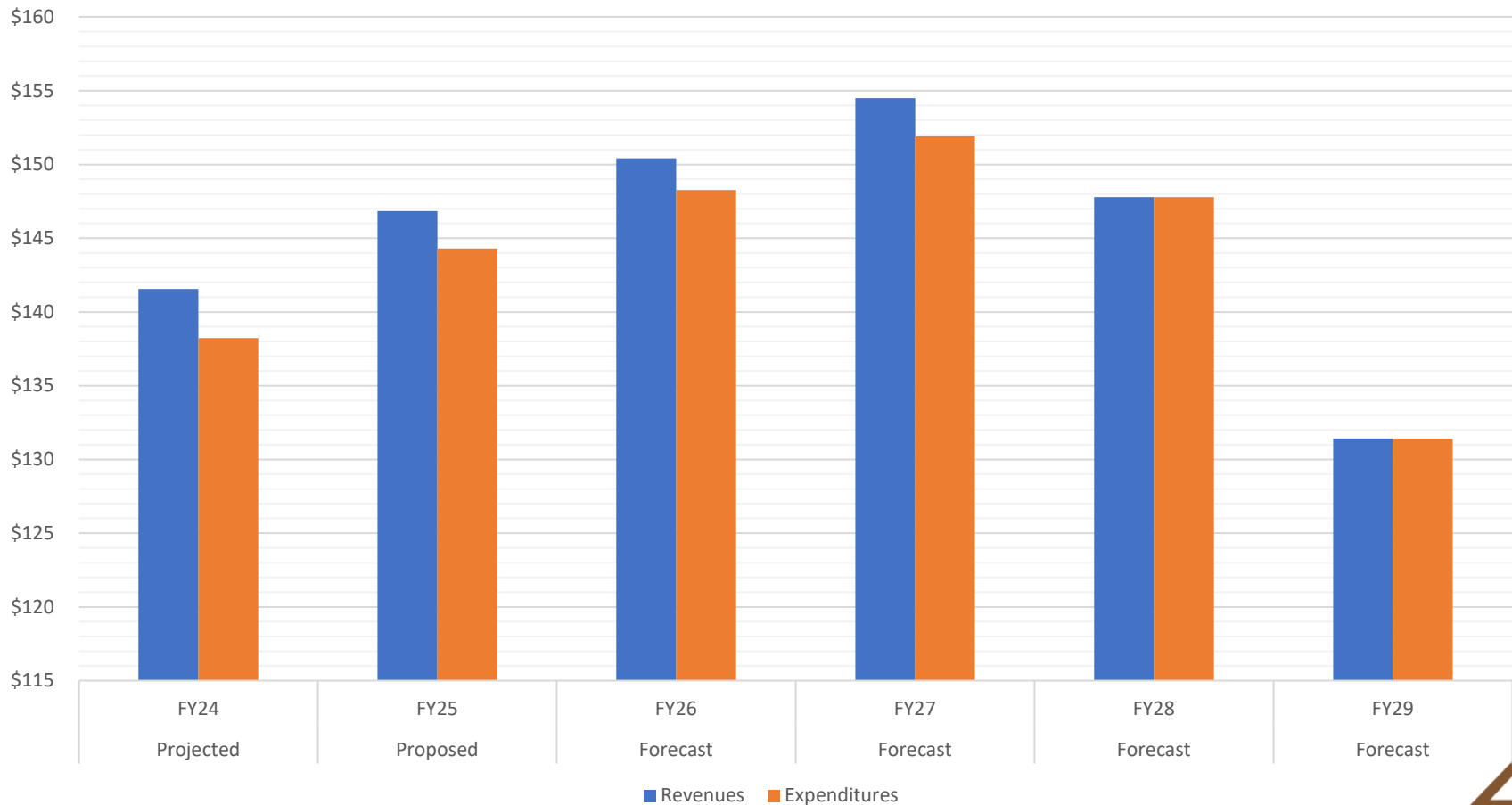
# Forecast of Fiscal Sustainability Strategies

On-Going Revenue	Estimated			
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# General Fund 5-year Forecast FY 2024-2029



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# General Fund 5-year Forecast FY 2023-2028

## 5-Year Forecast

(in Millions)

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Expenditures	\$138	\$144	\$148	\$152	\$148	\$131
Surplus/Deficit	\$4	\$3	\$2	\$3	\$0	\$0

The City's General Fund is projected to have a surplus for the next three fiscal years, assuming the Sales Tax revenue allocation method remains in place.



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# Sales Tax

- The City is tracking possible legislation change related to sales tax related to ecommerce.
- California Department of Tax and Fee Administration (CDTFA) studied changing the allocation method from point of fulfillment to point of delivery.
- The study showed that if such a change occurred, Tracy's allocation would be impacted by 25% or greater.



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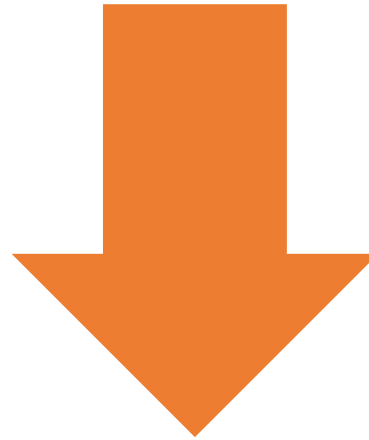
# Sales Tax, Continued

- Discussions are ongoing through the Cal Cities City Manager's Sales Tax Working group.
- Staff estimates any change to the sales tax allocation will occur in FY2027/28.
- The forecast reflects a \$10M decline in sales tax revenue in FY2027/28 and a \$20M decline in sales tax revenue in FY2028/29.





## Offset Future Costs and Revenue Instability to Gain Fiscal Sustainability



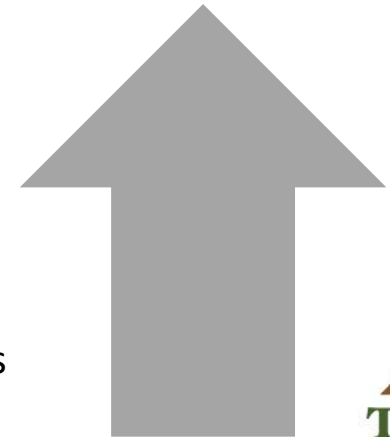
### Projected Revenues/Expenses

- 10M decrease in sales tax revenue expected FY28
- 20M decrease in sales tax revenue expected FY29
- Expenses continue to rise



### Prefunding Liabilities/New Revenue Sources

- Prefunding deferred maintenance
- Prefunding employee retiree benefits



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# 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.





# Next Steps



# Next Steps

March 26, 2024

Staff will present the CIP Outlook and Department Augmentation Requests to the Finance Committee.

April 2, 2024

Staff will present the CIP Outlook and Department Augmentation Requests to the City Council.

# Next Steps

May 28, 2024

Staff will present the FY 2024-25 proposed budget to the Finance Committee.

June 4, 2024

Staff will present the FY 2024-25 proposed budget to the City Council.



# Q & A

