

January 28, 2004

Honorable Mayor and Members of
the Hermosa Beach City Council

City Council Meeting of
February 10, 2004

MIDYEAR BUDGET REVIEW 2003-04

RECOMMENDATION:

It is recommended that the City Council:

1. Approve the revisions to estimated revenue, appropriations, budget transfers and fund balances as shown in the attached Budget Summary and Revenue Worksheet.
2. Approve a change to the year-end transfer of unspent funds to allocate amounts to the Compensated Absences Fund, the Capital Improvement Fund, the Insurance Fund and to a new Retirement Stabilization Fund. It is also recommended that we transfer any funds in excess of our goal in the Contingency Fund to the new Retirement Fund.

BACKGROUND:

The City has conducted a Midyear Budget Review annually since fiscal year 1981-82. The review is a good tool to ensure that assumptions and estimates originally used to prepare the budget ten months earlier remain realistic.

ANALYSIS:

Overview

The revenue changes recommended herein reflect small net increases in both the General Fund and Parking Fund. Significant line item changes are discussed below.

Revenue (see Revenue Worksheet)

The overall change in revenue in the General Fund is \$427,537 or 2.7%. Though the overall change is small, there are some notable changes.

Taxes

The tax category, overall, increases by 5.00%. Secured Property Taxes increase 9% over 2002-03, based on the actual levy, 3% over our original estimate. This increase is consistent with the past four years' history, given the increases in residential property values and the turnover rate.

Sales tax for the first two quarters is virtually flat compared to 02/03, which is good news! The Volkswagen dealership stayed at their site longer than originally anticipated and BMW new car sales have not moved to their new location yet. Even after adjusting for anticipated lower than normal supermarket sales due to the strike, the sales tax estimate is being increased by 5%.

The chart below compares sales tax on major accounts for the first half of this year to the first half of last year by the top ten categories.

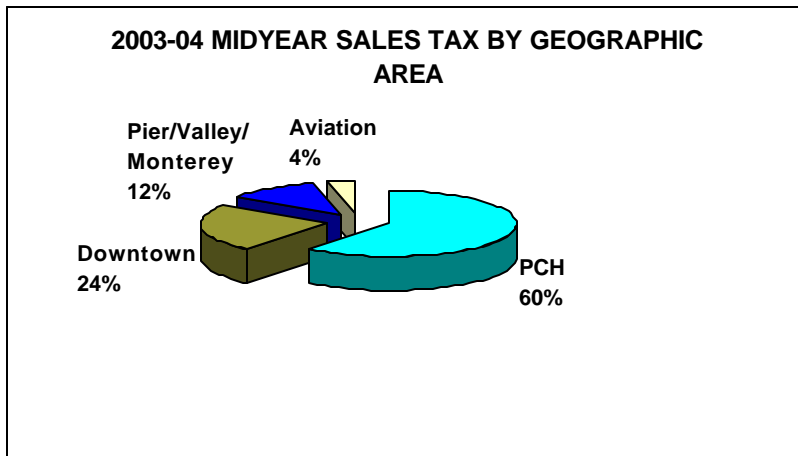
SALES TAX
Comparison of First Half of 2002/03 to 2003/04
Top Ten Categories

RANK/BUSINESS CLASS*	Sales Tax 2003-04	Inc./ (Dec.)	% of Change Prev. Yr.	Percent of Total
1. AUTO DEALERS	\$342,793	\$51,619	17.73%	31.54%
2. EATING/DRINKING PLACES	325,329	16,314	5.28	29.93
3. GROCERY STORES/LIQUOR STORES	102,429	(5,205)	-4.84	9.42
4. LUMBER/BUILDING MATERIALS	75,819	3,510	4.85	6.98
5. SPORTING GOODS/BICYCLES	61,211	6,858	12.62	5.63
6. AUTO LEASES	58,010	(9,961)	-14.65	5.34
7. SERVICE STATIONS	44,048	6,426	17.08	4.05
8. SPECIALTY STORES	31,434	2,700	9.40	2.89
9. HOUSEHOLD/HOME FURNISHINGS	30,893	4,406	16.63	2.84
10. AUTO REPAIR SHOPS	15,004	(1,965)	-11.58	1.38

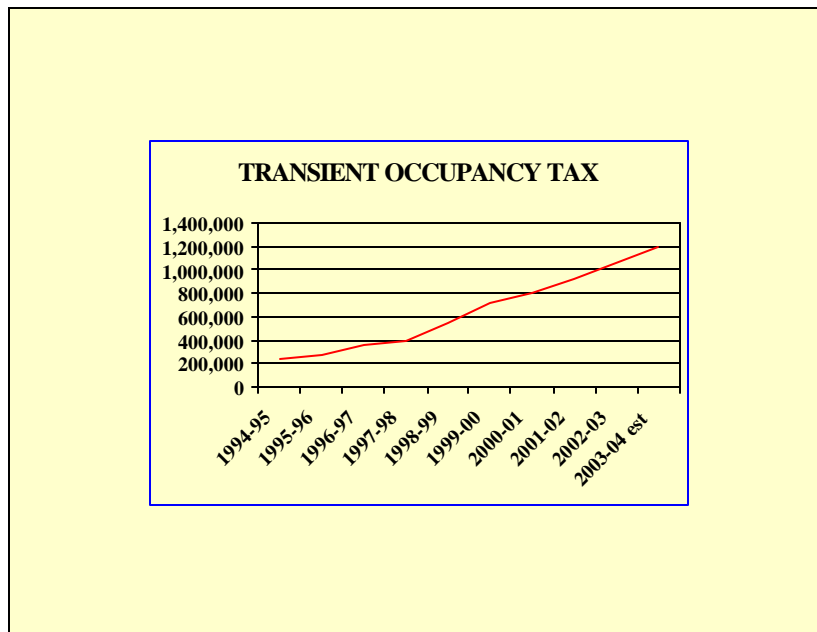
* Drug stores cannot be listed because there is only one

Sales Tax Comparison by Geographic Area

LOCATION	Revenue 2002-03	% OF Total	Percent Change	Revenue 2003-04	% Of Total
PCH	599,024	59%	10%	658,691	60%
Downtown	246,172	24%	4%	256,234	24%
Pier/Valley/Monterey	136,659	13%	-5%	130,477	12%
Aviation	39,909	4%	-2%	39,137	4%



Transient Occupancy Tax (TOT) is being adjusted up by approximately 9%. For the first half, the hotels are up by about that amount. (excluding the Hampton Inn, which had just opened in the second quarter of last year) As you can see below, the TOT revenue trend is very positive.



Utility User Tax revenue is being revised up to recognize higher revenue from both gas and wireless telephone providers.

Fines and Forfeitures

The estimate for Municipal Court Fines is increasing based on revenue for the first half. Revenue from the court for moving violations and other municipal code violations is up 10%. Revenue from misdemeanor court cases is up 74%.

Intergovernmental/State

The decline in revenue in this category is in the In Lieu Motor Vehicle Account, or the so-called “car tax”, “VLF” (vehicle license fees) that has been in the news so much lately. Our share of the \$1.3B reduction to local government, \$280,054, is the amount estimated for the League of California Cities.

A simplified history on why this reduction occurred:

When vehicle license fees (VLF) were reduced in 2001, the amount was fully backfilled by transfers from the state general fund, holding cities and counties harmless. In June of 2003, when the Governor declared that there were insufficient revenues to fund the backfill, higher rates went into effect, commencing with registrations due in October. Therefore the period between June and October constituted a “gap”, for which cities and counties would not receive these backfill funds. The reduction is supposedly a one-time reduction and is to be repaid by August 2006.

Additional Appropriations

The following additional appropriations are requested:

GENERAL FUND (001)

City Clerk Part-time/Temporary	\$5,184	Election premium was not included in original budget request.
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TOTAL GENERAL FUND **\$5,184**

PARKS/REC FACILITY TAX FUND (125)

Community Center Facilities Study Contract Services/Private	(\$25,000)	Reduction due to midyear revenue estimate.
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Public Works CIP 507 Valley Park Improvements Contract Services/Private	(\$21,471)	Project has been completed.
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Public Works CIP 630 Pier Renovation/Phase III Contract Services/Private	(\$7,702)	Reduction due to midyear revenue estimate.
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TOTAL PARKS/REC FACILITY TAX FUND **(\$54,173)**

PROPOSITION C FUND (146)

Public Works

CIP 174 Artesia Boulevard Rehabilitation Contract Services/Private	(\$39,885)	Project costs will be less than anticipated.
TOTAL PROPOSITION C FUND	(\$39,885)	
GRANT FUND (150)		
Public Works Sewers & Storm Drains (Beverage Recycling Grant) Contract Services/Private	\$2,542	Additional costs for grant administration.
Fire Assistance to Firefighters Grant Equipment more than \$1,000	\$47,700	Grant for diesel exhaust air cleaning system for Fire station.
TOTAL GRANT FUND	\$50,242	
OFFICE OF TRAFFIC SAFETY GRANT FUND (151)		
Be Street Smart Hermosa Grant Overtime Conference/Training	(\$2,356) (\$1,000)	Expended more in 2002-03 than anticipated.
Equipment less than \$1,000	\$797	OTS rearranged funding in 2003-04.
TOTAL OFFICE OF TRAFFIC SAFETY GRANT FUND	(\$2,559)	
SUPPLEMENTAL LAW ENFORCEMENT SERVICES (COPS) FUND (153)		
C.O.P.S. Program Equipment more than \$1,000	(\$60,000)	Document imaging system no longer needed due to change in records management system provider.
TOTAL SUPPLEMENTAL LAW ENFORCEMENT SERVICES FUND	(\$60,000)	
FIRE PROTECTION FUND (180)		
Public Works CIP 610 Fire Station Upstairs Remodel/Addition Contract Services/Private	(\$47,700)	Grant approved for diesel exhaust air cleaning system for fire station.
TOTAL FIRE PROTECTION FUND	(\$47,700)	
CAPITAL IMPROVEMENT FUND (301)		
Public Works CIP 189		

Street Improvements/Myrtle Area Contract Services/Private	(\$202,704)	Project costs will be less than anticipated.
CIP 507 Valley Park Improvements Contract Services/Private	(\$121,369)	Project has been completed.
CIP 622 City Hall Remodel Contract Services/Private	(\$1,386)	Project has been completed.
TOTAL CAPITAL IMPROVEMENT FUND	(\$325,459)	

**MYRTLE UNDERGROUND DISTRICT
IMPROVEMENT FUND (307)**

Utility Undergrounding/Myrtle Avenue Contract Services/Private	\$33	Actual cost higher than estimate. Adjust Budget to prevent expenditures in excess of appropriations at the fund level.
TOTAL MYRTLE UNDERGROUND DISTRICT IMPROVEMENT FUND	\$33	

Financial Policies

The City Council's adopted policies are:

General Fund - Any funds remaining unspent at year-end in the General Fund transfer equally to the Contingency Fund, Insurance Fund, Equipment Replacement Fund and the Capital Improvement Fund.

Contingency Fund – Goal of fund balance equal to 15% of the General Fund appropriations for economic uncertainties, unforeseen emergencies.

Insurance Fund – Goal of \$3,000,00 in retained earnings for claims reserves and catastrophic losses.

Equipment Replacement Fund – Goal of retained earnings equal to the accumulated amount calculated for all equipment, based on replacement cost and useful life of equipment.

Compensated Absences Fund – Goal of fund balance equal to 50% funding for accrued liabilities for employee vacation, sick and compensatory time.

For 2002-03, the transfer from the General Fund was changed, on a one-time basis, to transfer 1/3 each to the Contingency Fund, CIP Fund and the Insurance Fund.

Progress on Goals			
Fund Name	Goal	Balance	Over/Under Goal Amount
Compensated Absences Fund	\$448,271	\$184,192	(\$264,079)
	50.00%	20.54%	-29.46%
Contingency Fund	\$2,635,133	\$3,003,603	\$368,470
	15.0%	17.10%	2.10%
Insurance Fund	\$3,000,000	\$1,743,941	(\$1,256,059)
Equipment Replacement Fund	\$1,849,864	\$1,303,754	(\$546,110)

The Challenge for Next Year

Although the midyear review is positive, with a net increase to the General Fund fund balance of \$383,436, there are several factors affecting next year's budget that will make it more of a challenge to balance:

- The Governor's proposed budget would transfer \$1.3B in property tax from local government to the State. The impact to Hermosa Beach would be \$287,478. This number could change, of course, depending on what the Legislature does.
- Replacement of the Volkswagen dealership with a Savon Drug Store will produce less revenue.
- BMW new car sales, if not the entire dealership, will be moving to their new location.
- Retirement costs will increase by approximately 62%. 38% of the increase is due to changes in the rates and 24% is because the Miscellaneous Employee Plan is no longer superfunded (we were using these excess funds to pay PERS costs). The increase is estimated to be about \$1.2 million.
- Dispatching costs with the South Bay Regional Communications Center (RCC) increase next year by approximately \$80,000 (you will recall that we recognized substantial savings in 2003-04 by making the change to RCC). The increased costs for next year are still lower than they would have been had we not made the change).
- The balance in the Lighting and Landscaping District will be almost depleted by year-end, necessitating either a return to the voters for an increase in funding or a sizable reduction in services.

Some steps have already been taken to address the above. To name a few - some positions have been frozen, plans for reducing the fleet have been developed, and a user fee review is in the final stage. Staff has also started developing a list of other alternatives that could be implemented to address the shortfall.

Conclusion

We have reached our goal of 15% for the Contingency Fund. We are actually at 17%, with excess funds of \$368,470 projected. However, we are below our goal in the Compensated Absences Fund due to employees terminating or retiring. Recognizing the challenges we are facing for next year, it is

recommended that we transfer any funds available at year-end in the General Fund to the Compensated Absences Fund, the Capital Improvement Fund, the Insurance Fund and to a new Retirement Stabilization Fund. It is also recommended that we transfer any funds in excess of our goal in the Contingency Fund to the new Retirement Fund. Those funds could then be used to offset the increased retirement costs for next year.

2004-05 budget preparations begin immediately after the midyear revisions are approved.

Respectfully submitted,

Concur:

Viki Copeland
Finance Director

Stephen R. Burrell
City Manager