C I T Y O F S A N B E R N A R D I N O
CITY MANAGER'S OFFICE
INTEROFFICE MEMORANDUM

TO: Mayor and Common Council

FROM: Charles E. McNeely, City Manager

SUBJECT: Budget Balancing Strategy Options

DATE: April 19, 2010

COPIES: Department Directors

Over the last two and a half years, the historic downturn of the national economy has had a significant negative impact on the City's financial condition. To address these circumstances, the City has implemented numerous actions designed to constrain General Fund spending, including imposing a freeze on most hiring, asking vendors to take a voluntary 5% reduction in contract costs, placing restrictions on non-mandated travel and training, and reducing supply and material purchases to the extent practical. Additionally, significant reductions in budget allocations for facilities and public infrastructure maintenance were imposed, new revenue sources were identified, and personnel costs were reduced through employee granted wage concessions. Further, one-time revenue mechanisms, such as transferring funds from the City's reserves to operating accounts, were implemented. This is just a summary of the actions taken by the Mayor and Common Council to address a net General Fund shortfall of more than $59 million during the summer of 2008 through the current mid-year budget hearing. The budget reduction actions have had significant impacts on the City's ability to deliver services to its residential and business communities, as well as on the employees who continue to provide those services.

Despite this series of actions, the Finance Director projects a deficit of over $24 million for the next fiscal year with an estimated five-year cumulative deficit of $188 million. (See Exhibit 1, the financial projections from the Budget Workshop of March 11, 2010) In large part, this deficit is due to an anticipated continued decline in sales tax, utility user tax and property tax revenues, as well as increases in costs related to personnel compensation, retirement and other benefits. The combination of declining revenues and growing personnel and other costs has created a structural deficit; the City will continue to experience budget problems until its fiscal structure is corrected. Addressing this structural deficit will require a strategic, long-term approach that involves mechanisms designed to impact both major elements of the budget: increasing the revenues and decreasing the expenditures. To that end, the six key aspects of the strategy are: creating efficiencies; enhancing revenues; implementing entrepreneurial enterprises and consolidations, partnerships, or joint powers relationships with other governmental entities; conducting negotiations with labor groups; identifying program reductions; and performing economic development efforts.

The long-term outlook for the City's financial future can be a positive one, if the City addresses its fiscal challenges in a strategic manner. There are significant development opportunities, along with major transportation and transit improvements, on the horizon. Also, important progress has been made toward reducing the City's crime rate. Further, the federal stimulus plans continue to provide new investments in infrastructure. However, difficult decisions need to be made in the near future in order to position the City to recover financially in the coming years and to take advantage of these positive long-term opportunities.

Overview of Budget Balancing Strategy Options

At the direction of the City Manager, a team of representatives from a variety of departments was established to work with the Finance staff, other department heads, mid-managers and their staffs to develop a series of budget options. Employees throughout the organization were encouraged to submit ideas for review and consideration by the committee. The following is an overview of these budget balancing options. Each of the major aspects of the strategy has an attachment that provides details of its elements.

Creating Efficiencies Strategies

The attached matrix (Exhibit 2) details a number of efficiency measures that were identified in the organizational overview conducted by Management Partners in their 2007 report. These include a number of recommendations to consolidate internal City functions such as financial services, debt collection, human resources services and fleet operations. The anticipated outcome of these recommendations from Management Partners was two-fold: to become an efficient, well-aligned organization and to create cost savings through those efficiencies. As stated in that report,

> "The City of San Bernardino is at optimum size and complexity to take advantage of economies of scale in its overhead and management operations. Unfortunately, San Bernardino operates much differently from most other California cities, and this organizational structure frustrates potential efficiencies enjoyed by other organizations.
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> The most troublesome and by far largest contributor to this reality is the apparent creation of what are, in effect, several agencies with duplicated overhead. This structure works against the economy of scale advantage, and leads to inconsistency and frustration on many levels. Several City departments and agencies take on some of the functions that would otherwise be provided through central city support services."

Enhancing Revenues Strategies

Revenue Measures Requiring Voter Approval

The passage of Proposition 13 in 1978 and Proposition 218 in 1996 created important distinctions between types of taxes and the voter approval needed to enact such taxes, and imposed additional procedural requirements. The first major change created the distinction between general and special taxes. Since 1978, all local taxes fall into either one of these categories. A general tax refers to any tax imposed for general governmental purposes, while a special tax is imposed for specific purposes, such as benefit assessments or parcel taxes for public safety or parks.

There are a wide variety of general and special tax measures that could be levied subject to voter approval. Listed below are some of the larger and more common of these measures for the Mayor and Common Council to consider. The details of these options are provided in Exhibit 3.

Property Transfer Tax/Documentary Transfer Tax

The property transfer tax/documentary transfer tax is paid when real property is sold. Currently, San Bernardino has a documentary transfer tax rate of .55 cents per $1,000 sales value, which is the minimum dollar amount that cities collect. Only charter cities are allowed to establish a property transfer tax rate and a number of charter cities have imposed rates from $1.10 to $15.00 per $1,000 of assessed valuation. If the City establishes a property transfer tax, the documentary transfer tax will revert to the County. It is estimated that if the City, through voter approval, established a $5 per $1,000 property transfer tax, the increased revenue to the General Fund would generate an estimated $3 million annually.

Utility User Tax

The Utility User Tax (UUT) rate for San Bernardino is currently 7.75% and is charged on all gas, electric, and telecommunications services. Many cities also charge a UUT on other utilities such as refuse, water and sewer services. One option to consider is lowering the City's rate and expanding the base by applying the tax on refuse, sewer, and water services; this broadening of the applicable base would require voter approval.

Increasing Direct Charges to Enterprise Revenues

Currently the City's charter allows 10% of water revenues to be transferred to the General Fund. With voter approval, a percentage of the revenues of both the refuse and sewer enterprises could be transferred to the General Fund. A study would have to be conducted to ensure that there is adequate documentation and justification to allow this type of transfer under the provisions of Proposition 218. As this option is being reviewed, increasing the transfer amount to a maximum

of 15% should also be considered. The analysis of this strategy option should also identify its impact on the current utility rates.

Transient Lodging Tax, Warehouse Tax, Quarry Extraction Tax

The Transient Lodging Tax (TLT), Warehouse Tax and Quarry Extraction Tax are business-related taxes that are applied to the persons or entities for a specific activity or land use that impacts city services. Of these three taxes, the City currently collects only one, the TLT. Although the City's current TLT rate is 10%, which is the average for San Bernardino County, there are some cities that have slightly higher TLT rates such as Riverside (11%), Ontario (11.75%), and Barstow (12.5%).

On November 6, 2007 the voters of Redlands, approved a Warehouse License Tax by a margin of 71 to 29 percent. Through this vote, the citizens imposed a business license tax on distribution centers of $0.035 per square foot with an annual adjustment based on the Consumer Price Index (CPI). An exception was established for warehouses or distribution centers with a wholesale business within the City. A similar rate in the City of San Bernardino would generate approximately $300,000 per year.

Both the Lytle Creek Mine, which is operated by Robertson's Ready Mix Inc, and the Cajon Creek Mine, which is operated by Vulcan Industrial and Mining Corporation, are located within the City limits. The cities of Upland and Highland both have quarry taxes with an annual CPI adjustment. The City of Upland has a current rate of $0.1225 per ton. Highland has a current rate of $0.1719 per ton. The City of Irwindale has fixed quarry tax rates for general and special excavation and processing of materials. A quarry tax in San Bernardino may generate $200,000 annually.

Downtown and/or Airport Parking Tax

Several years ago, the City allowed the downtown-parking district to elapse. A parking district may take several forms, from installing meters on all public parking spaces to imposing a tax on the occupancy of off-street parking spaces. In the latter case, when the operator of a parking lot collects the fee from the parking patron for the space rental, the City's parking tax rate is incorporated into the amount collected. In addition to establishing a downtown parking district, the City has an option to initiate a parking district around the airport. Exploring this option would involve working with the Airport Authority to add a tax onto the proposed airport parking rate. If the initial tax rate is very low, for example $1 per day, the impact on airport operations should be minimal. A study by staff indicated that all major airports have some type of parking tax imposed on the airport parking fee.

911 Tax

With voter approval a small charge could be added to cellular and landline phones to generate revenue that would be appropriated to support the 911 operations in the City. If this tax were to be pursued, one recommendation would be to simultaneously reduce or modify the current paramedic user fee.

Parcel Tax for Library, Parks, or Other Services

A parcel tax is a non-*ad valorem* tax. In other words, it is levied as a flat fee on each parcel and is not based on the assessed value of the property. A parcel tax is a special tax that is usually designated for a specific purpose, such as libraries, parks, or public safety. In prior years the City has provided the voters with several opportunities to vote on the implementation of a parcel tax. The most recent example was in 2005 when the voters considered a parcel tax for libraries a majority, 55 percent, were in favor of this measure; however, it did not meet the 2/3 approval rate necessary to pass a special tax.

Benefit Assessment Districts

Benefit Assessment Districts are special tax districts formed by a vote of the property owners to assess properties for the improvements or services that specifically benefit the properties within the district. The City of San Bernardino used to have a citywide assessment district that generated revenue to cover the costs for street lighting, traffic signals, and street sweeping. In fiscal year 1997-98, the term of the district expired. The elimination of this district created a burden of several millions of dollars of costs on the General Fund. As the district generated $4.2 in the 1996-97 fiscal year, if its life had been extended and an annual CPI adjustment had been applied, the revenue from the district would have been approximately $6.0 million in the current fiscal year. Consideration needs to be given to re-establishing a citywide district that could generate additional revenues for current maintenance as well as the expansion of services such as street lighting, traffic signal maintenance, graffiti removal, parks maintenance, street maintenance, and tree trimming.

Unlike other options that require voter approval, this type of district requires property owner approval. A ballot mailed to each property owner would be required with approval for the district requiring a simple majority of those returning the ballots. The ballots are weighted in direct proportion to the assessment amount.

Revenue Measures Not Requiring Voter Approval

Fee Increases

The City currently has an approved Master Fee schedule. Staff is in the process of reviewing all fees for possible updates. Some options under consideration are increased Business Fire Inspection Fee and various technology fees for Departments.

Other Miscellaneous Ideas

In this section of the matrix are a number of miscellaneous ideas that have been raised by the departments; these include generating a one time revenue of $2.4 million by selling the convention center to the Economic Development Agency, instituting a business inspection program, and researching developing new fee-based programs or permits. A number of these suggestions would require additional research and analysis to determine the costs and benefits of the programs.

Joint Powers Authorities/Consolidations/Enterprise Strategies

The matrix on Joint Powers Authority, Consolidations and Enterprise options identifies areas of opportunities for partnerships with other public agencies or the private sector. (See Exhibit 4) The exploration of the strategy to develop a regional animal shelter is one that is currently underway. If the Mayor and Common Council provide direction to pursue one or more of the remaining strategies contained in this matrix, additional research and analysis of the costs and benefits of these options will need to be conducted.

Labor/MOU Negotiations Strategies

In conformance with the Brown Act, options for potential bargaining unit concessions will be explored in closed session. All employees are currently participating in concessions equivalent to a 10% salary reduction. (See Exhibit 5) These concessions expire on June 30, 2010.

Program Reductions Strategies

As the City of San Bernardino, and all municipalities, is a service organization, and its personnel provide those services, effectuating significant additional reductions in expenditures would require eliminating programs and positions. For example, a ten percent reduction in General Fund personnel costs would produce a savings of $10.7 million. Using an average annual salary and benefit rate of $83,200, this would equate to a staff reduction of approximately 129 full-time positions.

Economic Development Strategies

The final strategic area of additional business attraction and retention opportunities and efforts will be discussed as a component of the economic development strategy through the Economic Development Agency.

RECOMMENDATION AND NEXT STEPS

This report is provided for information and discussion purposes. Exhibit 6 provides a summary of the revenues or savings that would be generated if all of the budget balancing strategies were adopted and implemented.

It is recommended that the Mayor and Common Council review the budget balancing strategy options, identify any questions of the City Manager and staff, hear input from the public, and provide general direction to staff on the options that will require additional information or merit further consideration. Staff will present the selected options for further discussion and possible approval at the next budget meeting, which will be scheduled for May, 2010. It is important to note that the schedule for placing revenue measures on the 2010 November ballot requires the Mayor and Common Council to adopt a resolution calling for a special election and submit it to the County by August 6th.

I look forward to a productive discussion at the workshop and over the coming weeks to position the City for a secure financial future.