



# FINANCE COMMITTEE FINAL MINUTES

Special Meeting  
December 3, 2019

The Finance Committee of the City of Palo Alto met on this date in the Community Meeting Room at 6:02 P.M.

Present: Cormack, DuBois, Fine

## Oral Communications

None

## Agenda Items

1. First Quarter Fiscal Year (FY) 2020 Financial Report.

Kiely Nose, Director of Administrative Service and Chief Financial Officer introduced Ms. Lobo who presented the item to the Finance Committee (Committee).

Rima Lobo, Finance Manager reported that the First-Quarter Financial Report was for the General Fund and Enterprise Funds. For Fiscal Year (FY) 2020 the General Fund was 7 percent higher than FY 2019 in terms of revenues, but expenses were 3 percent higher than FY 2019. In terms of police overtime expenses, there was an increase of 6 percent compared to FY 2019. For fire overtime, it had decreased by 38 percent compared to FY 2019. For Enterprise Funds, the Water Fund had a change in net position with an increase of \$.7 million, the Electric Fund had a change in net position with a decrease of \$1.8 million, the Gas Fund had a change in net position with a decrease of \$.5 million, the Refuge Fund had a change in net position with a decrease of \$.4 million, and the Airport Fund had increased \$.3 million in net position. Staff recommended that the Finance Committee approve the Financial Report for the first quarter of FY 2020.

Council Member Cormack highlighted the average occupancy was declining for hotels and that City Council (Council) needed to pay attention to that. In terms of overtime for police and fire, she wanted to see the percentage of the total budget that was overtime and compare that. She wanted to know how an Enterprise Fund could be negative.

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Ms. Nose stated it had to do with cash flow for that quarter.

Council Member Cormack saw that there was 30 percent for expenditures for the first quarter and she wanted to know if there was seasonality in quarter expense reports.

Ms. Nose commented that Staff would investigate it and come back to her. One thing was that Community Service Department (CSD) had strong seasonality to their work and would often Staff up for spring and summer.

Michelle Poché Flaherty, Deputy City Manager confirmed that the Development Center often saw a spike in the summer months and then construction would taper off in the winter.

Council Member Cormack was impressed with the Fire Department's recruitment efforts to fill vacancies and their decrease in department disability days.

Vice Mayor Fine agreed with Council Member Cormack for overtime as a percentage of payroll or department expenses.

Chair DuBois asked for more information in terms of sales taxes.

Ms. Nose noted that the State implemented a new system and that was causing timing issues.

Chair DuBois predicted that next quarter Sales Tax revenue would go down.

Tarun Narayan, Manager of Treasury, Debt and Investments clarified that Staff was expecting Sales Tax to estimate about \$1.6 million higher than what was budgeted. It had to do with the timing of the new system and that new system coming online.

Chair DuBois wanted to know more about the Gas Fund revenue and long-term trend that the fund was likely to lose money.

Ms. Nose explained that the fund did look at rate base changes and because a large company went out of business that effected the Gas Fund.

Chair DuBois questioned if the Committee should be concerned about CSD services that were listed over 25 percent.

Ms. Nose announced that it was too early in the year to tell.

Chair DuBois requested what was in the Adjusted Budget column.

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Ms. Nose answered it was the Adopted Budget, any carryover in incumbencies and any budget amendments that the Council had approved.

Chair DuBois clarified that it did not include the Service Employee International Union Hourly Unit (SEIU) contract.

Ms. Nose confirmed that was correct.

Chair DuBois expressed that it was important to understand the hotel occupancy figures as well as the change in supply and how that impacted occupancy. He wanted to understand more about Airbnbs.

Council Member Cormack did not believe that Airbnbs were causing issues with hotels.

Vice Mayor Fine clarified that with more regulation's around Airbnbs, that would help the hotel market.

Chair DuBois emphasized that it was hard to tell what was happening with hotels when a large piece, such as Airbnbs, were not factored into the figures. He asked if Airbnb provided an average room rate along with their payments.

Ms. Nose acknowledged that Palo Alto (City) did have a contract with Airbnb but the terms were not publicly disclosed.

**MOTION:** Chair DuBois moved, seconded by Council Member Cormack to recommend the City Council review and approve the First Quarter Fiscal Year (FY) 2020 Financial Report.

**MOTION PASSED:** 3-0

2. Review and Recommend That Council Accept the FY 2021 - FY 2030 Long Range Financial Forecast and FY 2021 Budget Development Guidelines.

Steve Guagliardo, Interim Director of Office, Management and Budget presented the Fiscal Year (FY) 2021 – FY 2030 Long Range Financial Forecast to the Finance Committee (Committee). One highlight was that the forecast did project a surplus for FY 2021 with very minor deficits throughout the middle of the forecast. Palo Alto (City) was a service-driven organization and that the Long-Range Forecast was maintaining service levels that were already authorized by the City Council (Council). The forecast did include the Council approved 6.2 percent Discount Rate. Something new that was included in the forecast was Committed Additions which was maintenance costs for various Capital Improvement Projects (CIP). The Long Range Forecast did assume that the Budget Stabilization Reserve (BSR) was to be maintained at 18.5

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percent. Not included in the Long Range Forecast was new CIPs like the Junior Museum and Zoo Phase Two, the animal shelter rebuild, the Birch Street Property, future labor agreements, potential additional tax measures, and additional Pension costs.

Chair DuBois wanted to know why CIP projects were not included.

Mr. Guagliardo explained that it was hard to have strong estimates for future projects.

Chair DuBois noted that the Infrastructure Plan was included but not the cost increases.

Kiely Nose, Director of Administrative Services and Chief Financial Officer confirmed that the Infrastructure Plan was included based on current estimates.

Tarun Narayan, Manager of Treasury, Debt and Investments reported that the current and future FY revenue was predicted to grow. For FY 2022 and beyond, the growth was predicted at 4.4 percent.

Mr. Guagliardo continued with major expense projects which included salary and benefits expenses and non-salary expenses. Salary and benefits included the actual employee data that was consistent with Memorandum of Agreement (MOA), annual pension contributions by California Public Employees Retirement System (CalPERS) actuarial reports and a 2 percent General Wage increase model. Non-salary included models for a Consumer Price Index (CPI) of 2.7 percent based on the type of expense and current changes from August 2019 to August 2020 as well as any Committed Additions. Alternative forecast scenarios for one-time surpluses include Scenario A which was to pay CalPERS Pension Rates, Scenario B was a model for a recession, and Scenario C was to use the surplus for an additional 1 percent General Wage increase without MOAs. The FY 2021 Budget Development Guidelines included the develop of a structurally balanced budget that brought ongoing expenses into alignment over the short, medium and long term to maintain fiscal suitability, allocate one-time resources for one-time needs, examine appropriate uses of revenue surplus, ensure appropriate resources for Council's existing priorities, focus on internal business process redesign, explore alternative service delivery models, continue to analyze non-personal and equipment, explore the expansion of existing revenue sources and/or new revenue sources, and continue to analyze and prioritize resource augmentations. Staff recommended that the Committee review and recommend that the Council accept the FY 2020-2030 General Fund Financial Forecast and the Annual Budget Guiding Principles.

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Vice Mayor Fine wanted to include in the Annual Budget Guiding Principles a recognition that labor was the largest cost driver. He wanted to know if previous expense percentage growth and revenue growth figures were available.

Ms. Nose noted that all previous revenues and expenses were available on the Open Gov. platform.

Vice Mayor Fine suggested that it would be helpful to understand how confident Staff was in terms of expense and revenue growth as compared to previous years. He liked the addition of Committed Additions to the forecast.

Council Member Cormack commented that defining fiscal sustainability over different timeframes was an important Guiding Principle. In terms of the Infrastructure Plan, with an increase of 130 percent in construction costs, it was apparent that not everything was going to be achieved that was listed in the plan. She requested more clarification on property taxes for the Long Range Forecast.

Mr. Narayan explained that the County only forecasted for 1 year and so the information was limited.

Council Member Cormack predicted that the portfolio yield in earnings would increase more gradually than the market.

Mr. Narayan confirmed that was correct.

Council Member Cormack questioned if any of the Budget Guidelines were a new way of thinking.

Mr. Guagliardo highlighted that the exploration of finding new revenue options was something that did not focus on cutting expenses.

Chair DuBois believed that having the 2 percent baseline and Scenario C was good practice. He wanted to know why in the long term forecast there was always a major increase in surpluses.

Mr. Guagliardo explained that in the interest of sustainability, if ongoing funds were identified through the budget process those funds would be committed.

Ms. Nose added that most Staff were on stepped positions and the system only calculated up to five steps. So, after so long the system could not grow the salary anymore thus showing there to be a surplus in funds.

Chair DuBois acknowledged that though it may appear the City had a surplus in funds, those funds were used for CIPs mainly and there really was no

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surplus. In terms of the Retiree Medical Fund and Trust, he wanted clarification on why Staff believed funds could be moved out of that trust.

Mr. Guagliardo specified that the trust would meet a funded status level eventually and it was a policy question of if the City wanted to continue to fund the trust or pull funds from it. The Committee was going to see a report on the trust in the spring of 2020.

Chair DuBois asked if there was an unfunded liability including the trust.

Ms. Nose emphasized that there was a significant amount of unfunded liability and that the plan was less funded than pensions. Other Post Employee Benefit (OPEB) was an open plan and was funded less than 50 percent, but that was common for open plans.

Chair DuBois questioned if the City should be doing some long-term recession planning.

Ms. Nose affirmed that Staff was investigating that internally, but the City was already taking small steps in preparation for a recession.

Chair DuBois wanted to know if there was any discussion about increasing the BSR above the recommended amount.

Ms. Nose did not believe that the BSR needed to be increased but to be proactive to make sure it never fell below 18.5 percent.

Vice Mayor Fine stated he had the same question, should the BSR be elastic if there were recognized vulnerabilities. He requested how other Cities handled their reserves.

Ms. Nose answered that some Cities had Contingency Accounts for emergencies and then they started planning for long-term sustainability.

Vice Mayor Fine suggested to combine Scenarios B and C and have Staff come back with the figures on what would happen with those two scenarios combined.

Ms. Nose reported that a recession hitting and how to balance that in the budget was on her mind. She emphasized that Staff was already trying to put the City in financial readiness using small steps like setting the BSR at 18.5 percent or above.

Chair DuBois inquired if Scenario C was showing the City cutting back services.

Ms. Nose answered no.

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Michelle Poché Flaherty, Deputy City Manager plugged that it was easier for the community to accept major cuts in the budget if everyone was doing it.

Council Member Cormack declared that it was important to do scenario planning but did not believe it needed to be very detailed.

**MOTION:** Vice Mayor Fine moved, seconded by Council Member Cormack to recommend the City Council accept the Fiscal Year 2021 to 2030 General Fund Long Range Financial Forecast (Base Case), and the annual Budget Development Guiding Principles.

**MOTION PASSED:** 3-03. Review and Acceptance of City Services Guide.

Kiely Nose, Director of Administrative Services and Chief Financial Officer declared that the document was an all funds document and listed all the services that Palo Alto (City) provided each year.

Chair DuBois mentioned that it looked a lot like the Performance Indicator Report and wanted to know if the Finance Committee (Committee) would continue to receive that report as well.

Ms. Nose confirmed that was correct.

Council Member Cormack asked where the document was going to be for the public to review.

Ms. Nose explained that the document was to be modular and available to everyone.

Michelle Poché Flaherty, Deputy City Manager added that it was going to be integrated into an electronic document as well.

Council Member Cormack listed the visual nature of the document was something she liked and the explanation of taxes. The tree was hard to follow and suggested a pie chart, the descriptions of the department were not consistent, and she suggested more explanation on how to measure the data in terms of good and bad. She advised that Staff investigate how to share the document so that it be easy to find.

Vice Mayor Fine agreed that service levels compared to citizens would be helpful for all departments and he suggested to include what the City did and did not have responsibility for.

Chair DuBois liked the tree. He asked why all benefits were listed under Human Resources (HR).

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Ms. Nose explained that HR included the Special Revenue Fund in their budget and that was why benefits were only included in the HR section.

Chair DuBois advised clarifying that a little more in the document. He wanted Administrative Services Department (ASD) to work with all departments to determine what indicators were best to show the performance of the department. He wanted to see an internal project involving the Committee to do a deeper dive into each department.

Ms. Flaherty asked for more clarification.

Chair DuBois explained that there had been discussions about doing zero-based budgeting and part of that was to investigate the performance of a service to determine if that service was done efficiently.

Council Member Cormack did not believe that the Committee should be involved in a deeper dive into departments. She thought it might be perceived as intrusive.

Chair DuBois interjected that it was part of the budgeting process.

Vice Mayor Fine commented that the reason to do an investigation into a department needed to be clear.

Ms. Nose emphasized that the City was already doing the process of making sure that departments were efficient. The next step was to build off the document, look at benchmarks, and use the document to find places that could be cut if that needed to happen.

## **NO ACTION TAKEN.**

### 4. FY 2020 Budget Referrals Update.

Kiely Nose, Director of Administrative Services and Chief Financial Officer declared that the Finance Committee (Committee) had given Staff a referral to look at what was in the Stanford University Medical Center (SUMC) Fund. Staff's recommendation was to incorporate the balances that were discovered into the annual budget process and bring back to the Committee recommendations on what those funds could be used for. The fund was a one-time fund and was not intended for projects that were ongoing. The Junior Museum and Zoo was a project that Staff was reviewing and would present to the Committee in spring 2020. The 1 year phase-out of Project Safety Net and transitioning that to a legal 501C3 was also being discussed. In terms of Medic 61, Palo Alto (City) was working on setting up a meeting



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with Stanford to start discussions. For printing and mailing services, a discussion was happening on how to make that service more efficient.

Council Member Cormack loved the document.

Chair DuBois advised Staff to look back at what the prior Policy and Services Committee had recommended in terms of \$4 million for community health and safety.

Ms. Nose wanted to know when the policy was adopted.

Chair DuBois predicted in the year 2015-2016. He wanted to know about expansion cost mitigation and what it was for.

Ms. Nose announced that money could be used within the parameters that were set.

Vice Mayor Fine agreed that the document should be forwarded to the City Manager and full Council so that it be incorporated into the next budget process.

## **NO ACTION TAKEN.**

### Future Meetings and Agendas

Kiely Nose, Director of Administrative Services and Chief Financial Officer declared the next meeting was scheduled for December 17, 2019 to discuss ballot measures.

Adjournment: The meeting was adjourned at 8:09 P.M.