



MEMORANDUM

TO: City Council

FROM: Nicole Valentine, Administrative Services Director
Don Rhoads, Financial Consultant

SUBJECT: Consideration of General Fund Five-Year Financial Forecast

DATE: March 14, 2023

SUMMARY OF ACTION:

Review and discuss the General Fund Five-Year financial forecast.

IMPACT ON FINANCIAL AND PERSONNEL RESOURCES:

The forecast provides an analysis of the financial impact of revenue and expenditure changes in the current fiscal year and the following five years. Preparation of the forecast required several hours of staff time, with additional review and input provided by the City's financial consultant, Don Rhoads.

RECOMMENDATION:

Consider and receive the updated Five-Year Financial Forecast Report.

BACKGROUND:

The General Fund is the City's largest fund and is used to account for the revenues and expenditures that support most services commonly associated with local government, including police, fire, public works, community development, parks and recreation, and administration. The preparation of the Fiscal Year (FY) 2023-24 through FY 2027-28 Five-Year Financial Forecast Report (Forecast) is one of the first steps in the City's budget process.

The City of Arroyo Grande's Forecast is a long-range fiscal planning tool that will serve as the framework for the development of the upcoming FY 2023-24 and FY 2024-25 General Fund Biennial Budget. The Forecast will provide City Council, key stakeholders, and the public information about the City's financial resources to facilitate discussion and decision-making regarding the upcoming General Fund budget.

The Forecast is a fiscally conservative, yet realistic, point-in-time estimate of the capacity of the General Fund to pay for both ongoing services and capital needs for the next five years. Because the General Fund is the City's primary fund and is where most

Item 12.a.

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 2

discretionary funds reside, this Forecast does not include other City funds such as the water, sewer, transportation, and park development funds. The Forecast takes into account cost inflation over its five-year timeline while also implementing a “Status Quo” approach to staffing and program levels by projecting costs into the future with no material changes.

ANALYSIS OF ISSUES:

5-Year Financial Forecast Overview

As depicted in Table 1 below, expenditures are expected to exceed revenues by \$1.8 million in the current fiscal year (2022-23) due to a planned drawdown of reserves to support spending on streets, sidewalks, employee retention incentive program, and capital equipment. This expected deficit in FY 2022-23, however, is less than the originally planned reserve drawdown of \$2.4 million. This is mainly due to better-than-expected projections for property, sales, and transient occupancy taxes in the current fiscal year while budgeted expenditures are largely on target.

Table 1 General Fund Financial Forecast (In thousands)							
	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Beginning Fund Balance	\$7,999	\$10,500	\$8,662	\$8,506	\$8,356	\$7,804	\$7,173
Total Revenue	20,901	22,104	21,731	22,358	23,014	23,689	24,386
Total Expenditures	23,279	23,941	21,887	22,508	23,565	24,321	25,102
Surplus or (Deficit)	(2,378)	(1,838)	(157)	(150)	(552)	(631)	(716)
Ending Fund Balance	\$5,621	\$8,662	\$8,506	\$8,356	\$7,804	\$7,173	\$6,457
Fund Balance %	24.1%	36.2%	38.9%	37.1%	33.1%	29.5%	25.7%

Table 1 also shows that the City is expected to experience a budget deficit that reaches \$716,000 by FY 2027-28 if no adjustments are made to expenditures and no new revenue sources are developed. This trajectory would reduce the General Fund reserve from the current 36% of expenditures to just over 25% by FY 2027-28, approaching the policy level minimum reserve of 20%.

As shown in Table 2 below, revenues in FY 2023-24 are projected to dip slightly from FY 2022-23 due in part to non-recurring grant revenues in the current year, in part to a mild economic slowdown in sales tax receipts anticipated by the City’s sales tax consultant (HdL), and in another part to the discontinuation of some recreation programs (before and after school childcare). According to HdL, Gross Domestic Product (GDP) is expected to increase only 0.8% in FY 2022-23, rising to a modest 2.5% in the following year. Though HdL does not project that a recession is an inevitable outcome in the near future, they do expect some economic pullback in the near term and do not write off the possibility of a deeper recession depending on choices made by state and national policymakers in the

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 3

months ahead. Most revenues after the current fiscal year are, therefore, expected to increase modestly each year as will be described in more detail later in this report.

Table 2 Fiscal Year 2024-2028 Financial Forecast (In thousands)								
	FY 2021-22 Actual	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
REVENUE & OTHER SOURCES								
Taxes								
Property Tax	\$ 7,957	\$ 8,013	\$ 8,066	\$ 8,329	\$ 8,618	\$ 8,917	\$ 9,227	\$ 9,547
Sales Tax	5,389	4,730	5,377	5,318	5,469	5,633	5,802	5,976
Transient Occupancy Tax	1,477	1,300	1,500	1,545	1,591	1,639	1,688	1,739
Franchise Fees	782	704	780	796	812	828	844	861
Licenses & Permits	531	529	529	540	551	562	573	584
Charges for Services								
Community Development	411	354	354	361	368	375	383	391
Other Charges for Services	1,202	1,378	1,388	990	1,010	1,030	1,051	1,072
Other Revenue								
Fines & Forfeitures	61	47	47	48	49	50	51	52
Use of Money	402	537	537	548	558	570	581	593
Intergovernmental	193	296	513	120	120	120	120	120
Transfers	2,993	3,013	3,013	3,137	3,213	3,291	3,370	3,452
Total Revenues	\$ 21,398	\$ 20,901	\$ 22,104	\$ 21,731	\$ 22,358	\$ 23,014	\$ 23,689	\$ 24,386

EXPENDITURES & OTHER USES								
Salary & Benefits								
Salary & Taxes	\$ 6,783	\$ 7,679	\$ 7,736	\$ 8,006	\$ 8,286	\$ 8,576	\$ 8,876	\$ 9,187
Flexible benefits	1,157	1,430	1,430	1,496	1,564	1,636	1,711	1,789
Workers' Compensation	558	626	626	676	731	789	852	920
Employee retention	-	1,030	1,030	-	-	-	-	-
Pension Normal Cost	690	899	899	1,000	1,003	1,020	1,025	1,034
CalPERS Unfunded Liab	1,520	1,905	2,302	1,272	1,421	1,546	1,677	1,581
OPEB	143	235	235	235	235	235	235	235
Total Salary & Benefits	10,851	13,804	14,258	12,685	13,239	13,802	14,375	14,746
Services & Supplies								
Contractual Services	1,776	2,465	2,490	2,275	2,320	2,366	2,414	2,462
Five Cities Fire Services	2,052	2,052	2,052	3,114	3,012	3,328	3,323	3,536
Liability Insurance	653	622	622	684	752	827	910	1,001
Utility Charges	445	526	526	536	547	558	569	581
Other Operating Expense	1,529	1,534	1,662	1,567	1,598	1,630	1,663	1,696
Total Service & Supplies	6,455	7,199	7,351	8,175	8,229	8,710	8,879	9,276
Debt Service	128	286	286	286	286	286	286	286
Transfers	1399	1,536	1,591	641	654	667	680	694
Capital Purchases	13	454	454	100	100	100	100	100
Total Expenditures	\$ 18,846	\$ 23,279	\$ 23,941	\$ 21,887	\$ 22,508	\$ 23,565	\$ 24,321	\$ 25,102

General Fund (Shortfall)/Surplus	\$ 2,552	\$ (2,378)	\$ (1,838)	\$ (157)	\$ (150)	\$ (552)	\$ (631)	\$ (716)
----------------------------------	----------	------------	------------	----------	----------	----------	----------	----------

Item 12.a.

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 4

Table 2 above also shows that expenditures are expected to decline from the current fiscal year to the next, mostly due to the one-time nature of the employee retention incentive program and larger than normal expenditures related to streets, sidewalks, and capital equipment budgeted in FY 2022-23. Offsetting these expenditure decreases somewhat is an expected increase in the cost to provide fire services to our residents through the Five Cities Fire Authority. Unless otherwise noted, most expenditures are projected to increase modestly over time. More details on these projections are included later in this report.

General Fund Revenues

Property Tax

Property tax is the City's largest revenue source, representing 36% of all General Fund revenues based on the FY 2022-23 Projected Budget. The primary component of property tax is derived from levying an ad valorem tax imposed on real property (land and permanently attached improvements) and tangible personal property (movable property). Proposition 13 (1978) limits the real property tax rate to one dollar (\$1) per hundred dollars (\$100) of taxable value of all real property within the city limits. The amount of this tax is based on an annually determined assessed valuation calculated by the County Assessor's Office.

Also included in property tax revenue is Property Tax in Lieu of Vehicle License Fees, which is the result of the state reducing Vehicle License Fees for cities from 2.0% to 0.65% and offsetting this loss with property tax. A third type of revenue also included in the property tax projection is the property transfer tax that is levied on the sale of real property.

Property tax assessments on all properties are limited to an increase of no more than 2.0% per year unless there is new construction or a property has a change in ownership. When ownership changes or new construction is completed, the property is reassessed at market value and is added to the existing assessment. The City has generally, over time, experienced growth in home prices. However, due in part to rising mortgage rates, this growth has moderated recently to a median sale price of about \$750,000 according to Realtor.com and Redfin.com. Given continued demand for homes and the relatively restricted supply in Arroyo Grande and surrounding communities, home prices are expected to continue to show growth.

Forecast

The following Table 2.1 shows FY 2021-22 actual revenues, the FY 2022-23 Adopted Budget and revised property tax revenue projection and a five-year Forecast for FY 2023-24 through FY 2027-28. The FY 2022-23 and 2023-24 projections are based on recent estimates provided by the County Auditor-Controller's Office. In the outyears of the Forecast, property tax revenue are projected to increase 3.5% annually, reflecting the combination of the 2% inflator added each year to assessed values along with increases

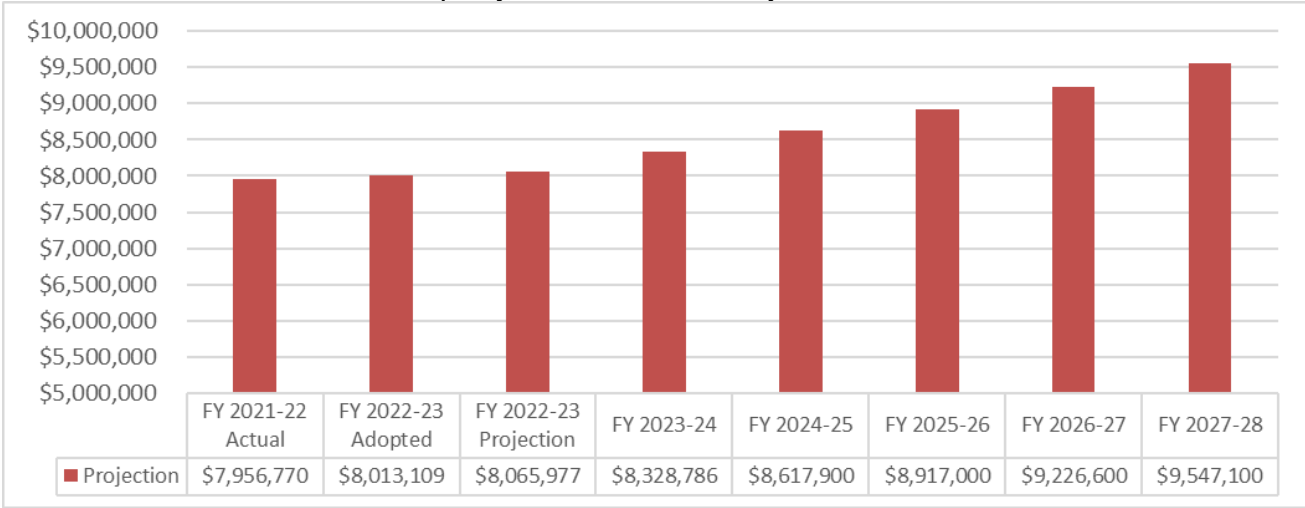
City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 5

resulting from the sale of existing properties at higher values than their current assessed valuations.

Table 2.1 Property Tax Five-Year Forecast								
	FY 2021-22	FY 2022-23	FY 2022-23	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
	Actual	Adopted	Projection					
Growth Rate		0.7%	1.4%	3.3%	3.5%	3.5%	3.5%	3.5%
Projection	\$7,956,770	\$8,013,109	\$8,065,977	\$8,328,786	\$8,617,900	\$8,917,000	\$9,226,600	\$9,547,100

Chart 2.1 shows the projected growth in property tax over the next five years using the 3.5% inflator noted above. It is advantageous to the City to have property tax as its largest General Fund revenue source given its relative stability over time. While property taxes can decrease during certain periods, as occurred during the 2008-09 recession, in general, property taxes weather economic changes better than the more volatile revenues such as sales tax and TOT.

Chart 2.1
Property Tax Revenue Projection



Sales Tax

The City’s second largest revenue source is sales tax which represents 24% of General Fund revenues based on the FY 2022-23 Projected Budget. Sales tax revenue includes both taxes collected at the point of sale as well as taxes collected from online sales. The City receives the basic local Bradley-Burns rate of 1.0% of the total City’s sales tax rate of 7.75% based on point-of-sale transactions within the City. Additionally, a half percent (0.50%) of the total sales tax is also paid to the City and is attributed to the Local Sales Tax measure approved in 2006. The majority of the Local Sales Tax is utilized for Capital Improvement Projects. However, a portion of the Local Sales Tax collected is used to support public safety programs, including payments to the Five Cities Fire Authority and the costs of a Senior Police Officer.

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 6

Forecast

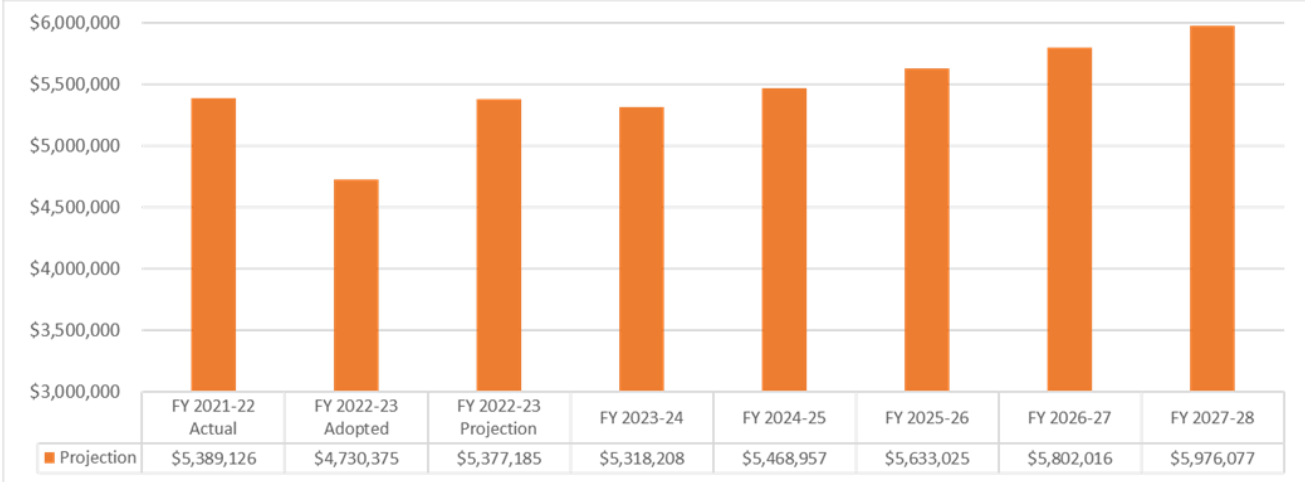
Economic drivers of the City’s sales tax revenue are unemployment rates, consumer confidence, consumer spending, and business retention and development. The unemployment rate in the region including and surrounding Arroyo Grande was 2.4% in December 2022, as published by the U.S. Bureau of Labor Statistics. This is a positive sign as it is less than half the unemployment rate of 5.5% two years earlier in the middle of the COVID-19 pandemic and lower than the national unemployment rate of 3.5%. Countering this good news, however, is a decline in the national index of consumer confidence, which measures consumers’ willingness to spend. This important measure declined for a second month in a row to 69.7% in February, which is more than 10 points below the confidence level that often signals a pending recession. Changes in consumer confidence, in part, account for the small decrease in sales tax revenues projected in FY 2023-24.

Table 2.2 shows HdL’s projected reduction in sales tax revenues of 0.2% in the current fiscal year and another 1.1% in FY 2023-24 due to the anticipated minor slowdown noted earlier. These projections reflect expected declines in categories like automobiles and transportation, fuel and service stations, and general consumer goods. The lower projections in these categories are the result of lower expected consumer demand in the short-term and, in the case of fuel, lower prices at the pump. In addition, the state and county pools sales tax category, which captures online sales, is projected to grow 14% this year, or \$92,000, over the original Adopted Budget. Categories that are expected to increase modestly over the next year include building and construction, restaurants and hotels, and receipts from the county sales tax pool. This pool is made up primarily of transactions that occur online rather than point of sale in Arroyo Grande and used automobile sales purchased outside the City.

Table 2.2 Sales Tax Five-Year Forecast								
	FY 2021-22 Actual	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		(12.2%)	(0.2%)	(1.1%)	2.8%	3.0%	3.0%	3.0%
Projection	\$ 5,389,126	\$ 4,730,375	\$ 5,377,185	\$ 5,318,208	\$ 5,468,957	\$ 5,633,025	\$ 5,802,016	\$ 5,976,077

The economic Forecast for sales tax revenue in the outyears assumes a 3% growth rate, which is in line with recommendations of the City’s sales tax consultant. Chart 2.2 below shows this trend in graphical form.

Chart 2.2
Sales Tax Revenue Projection



Transient Occupancy Tax (TOT)

TOT represents 7.0% of the General Fund revenues based on the FY 2022-23 Projected Budget. All lodging businesses (including vacation rentals, hotels, motels, bed and breakfasts, inns, etc.) must register for a City Business License and collect Transient Occupancy Tax (also called "bed tax" or "hotel tax") from their guests. A TOT tax is levied at 10 cents per dollar of taxable rent.

Forecast

The primary economic drivers of TOT revenues are lodging capacity, room rates, and occupancy. The following Table 2.3 shows that the original TOT projection of \$1.3 million for FY 2022-23 underestimated the rebound from previous pandemic related lows. Based on final numbers from FY 2021-22 of \$1.48 million, and after reviewing TOT receipts so far in FY 2022-23, this estimate has been revised to \$1.5 million, or a modest 1.6% increase over the previous fiscal year.

Table 2.3 Transient Occupancy Tax Five-Year Forecast								
	FY 2021-22 Actual	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		(12.0%)	1.6%	3.0%	3.0%	3.0%	3.0%	3.0%
Projection	\$1,476,939	\$ 1,300,000	\$ 1,500,000	\$ 1,545,000	\$ 1,591,350	\$ 1,639,091	\$ 1,688,263	\$ 1,738,911

The 5-year Forecast projects a modest but healthy increase of 3.0% year-over-year. The Forecast does not factor in any increase in the City’s current room capacity or the addition of new hotels within the City limits over the next five years. Nor does it factor in any efforts the City is making to increase TOT compliance with short-term rentals. Chart 2.3 provides a graphical representation of expected growth in TOT.

Chart 2.3
Transient Occupancy Tax Revenue Projection



License and Permit

The License and permit category includes revenue associated with regulating certain activities within the City, such as permits for building, encroachment, electrical, police, and fire. License and permit revenue represents 2.4% of General Fund revenues based on the FY 2022-23 Projected Budget.

The following Table 2.4 reflects license and permit revenue as flat for FY 2022-23 Adopted Budget with an expected 2.0% increase each year in the Forecast thereafter.

Table 2.4 License & Permit Five-Year Forecast								
	FY 2021-22 Actual	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		(0.3%)	(0.3%)	2.0%	2.0%	2.0%	2.0%	2.0%
Projection	\$ 530,599	\$ 529,100	\$ 529,100	\$ 539,700	\$ 550,500	\$ 561,500	\$ 572,700	\$ 584,200

Charges for Services

The City provides a variety of fee-based services that provide a benefit to an individual or group such as recreation programs, plan checking, and engineering inspections. Together, these charges for services represent 8% of General Fund revenues, so are an important part of the budget.

Forecast

As shown in Table 2.5 below, revenue from charges for services are on track for FY 2022-23 and did not change significantly from the original estimate. The 22.5% decrease in revenues projected for FY 2023-24 is due to the discontinuation of the before and after school childcare program in the Recreation Services Department, which is anticipated to be phased out by the City and provided, instead, by the YMCA in coordination with the Lucia Mar Unified School District. The corresponding Recreation Services Department

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 9

expenditures will be reduced as well. The Forecast includes a 2.0% increase per year in the outyears compared to FY 2023-24.

Table 2.5 Other Charges for Services Five-Year Forecast								
	FY 2021-22	FY 2022-23	FY 2022-23	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
	Actual	Adopted	Projection					
Growth Rate		7.4%	8.0%	(22.5%)	2.0%	2.0%	2.0%	2.0%
Projection	\$ 1,612,715	\$ 1,732,110	\$ 1,742,110	\$ 1,350,800	\$ 1,377,800	\$ 1,405,400	\$ 1,433,500	\$ 1,462,200
Community Developer	\$ 410,821	\$ 353,700	\$ 353,700	\$ 360,800	\$ 368,000	\$ 375,400	\$ 382,900	\$ 390,600
Recreation	827,286	822,610	822,610	412,900	421,200	429,600	438,200	447,000
Public Works/Other	374,608	555,800	565,800	577,100	588,600	600,400	612,400	624,600

General Fund Expenditures

Salaries and Taxes

Because municipalities are service entities, personnel costs are the largest category of expenditure, accounting for almost 60% of General Fund expenditures. The salaries and payroll taxes shown in Table 2.6 below represent all employee salaries (e.g. full-time, part-time, overtime, holiday, sick leave, etc.) and their associated payroll taxes. In addition to this, total personnel costs include employee benefits, workers’ compensation, and pension related expenses. These costs will be described later in this report.

The following Table 2.6 shows that Forecast includes a 3.5% inflator for the next five fiscal years based on current employee contracts and anticipated cost increases over the next few years.

Table 2.6 Salary & Payroll Taxes Five-Year Forecast									
	FY 2019-20	FY 2021-22	FY 2022-23	FY 2022-23	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
			Adopted	Projection					
Growth Rate			14.0%	14.9%	3.5%	3.5%	3.5%	3.5%	3.5%
Salary & Taxes	\$ 6,734,663	\$ 6,782,962	\$ 7,679,100	\$ 7,736,442	\$ 8,006,000	\$ 8,286,200	\$ 8,576,200	\$ 8,876,400	\$ 9,187,100

Employee Benefits

The City offers benefits to all eligible employees under a qualified benefits program that includes medical, dental, vision and basic life insurance plans. These benefits vary by recognized employee organization, working hours, years of service, and other factors.

As shown in Table 2.7 below, the FY 2022-23 Adopted Budget included \$1.4 million in flexible benefits, 85% of which is health insurance costs. The FY 2022-23 Projection for flexible benefits does not change from the Adopted Budget. The 23.6% jump from 2021-22 to the current fiscal year is due to a 10% increase in the cost of health insurance in FY 2022-23 and the addition of three new positions. The Forecast projects an approximate 4.6% increase year-over-year based on an average increase of actual health insurance over the previous five years.

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 10

Table 2.7 Flexible Benefits Five-Year Forecast								
	FY 2021-22	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		23.6%	23.6%	4.6%	4.6%	4.6%	4.6%	4.6%
Projection	\$ 1,157,075	\$ 1,430,435	\$ 1,430,435	\$ 1,495,600	\$ 1,563,900	\$ 1,635,500	\$ 1,710,600	\$ 1,789,300

Workers' Compensation

The City is a member of the California Joint Powers Insurance Authority (CJPIA) which manages the City's workers' compensation program. The CJPIA is composed of more than 100 California public entities and is organized under a Joint Powers Agreement.

As is reflected in Table 2.8, the FY 2022-23 Projected Budget includes workers' compensation costs of \$626,300, which is 12.2% above the previous fiscal year. For FY 2022-23 and beyond the Forecast includes projected increases of 8.0% in workers' compensation costs year-over-year based on the average actual increase of workers' compensation costs over the previous five years moderated by the fact that the growth rate has slowed somewhat in the last two years.

Table 2.8 Workers' Compensation Five-Year Forecast								
	FY 2021-22	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		12.2%	12.2%	8.0%	8.0%	8.0%	8.0%	8.0%
Projection	\$ 558,144	\$ 626,300	\$ 626,300	\$ 676,400	\$ 730,500	\$ 788,900	\$ 852,000	\$ 920,200

CalPERS Unfunded Liability

All qualified employees are eligible to participate in the City's Safety (Police) or Miscellaneous Employee Pension Plans. These two defined benefit plans are administered by the California Public Employees' Retirement System (CalPERS). The unfunded portion of the pension liability is the gap between the amount of future benefits a pension fund is expected to pay out and the assets presently in the pension fund.

The City is required by CalPERS to make annual payments towards the unfunded liability portion of the City's various retirement plans. The minimum amount the City is required to pay is calculated annually by CalPERS actuarial staff and invoiced to the City. The amount of the City's unfunded liability is based on a number of factors including investment returns, payroll growth, benefit eligibility, and the longevity of retirees. In 2021 CalPERS lowered their investment earnings assumption from 7.0% to 6.8% to better reflect expected long-term earnings. This change has resulted in increases to the City's unfunded liabilities in recent years.

The following Table 2.9 reflects a projection of the CalPERS unfunded liability payment the City will be required to pay through the period of this Forecast. The table reflects a significant decrease (44.7%) in the FY 2023-24 due to the fact that the current FY 2022-

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 11

23 budget includes \$982,000 as an estimated catch-up amount for unfunded liabilities of the Five Cities Fire Authority (FCFA) owed by the City. The FY 2022-23 Mid-Cycle Update included funding for a true-up payment to the FCFA totaling an estimated \$550,000 (\$50,000 per year for 10 years + \$50,000 for FY 2022-23) for the City’s share of accrued actuarial liability for employees who worked for the City before the FCFA was formed. No new CalPERS plan was created for the FCFA and instead all FCFA employees have been covered under the City of Arroyo Grande’s CalPERS pension plans. As a result, the City’s CalPERS plans include liabilities for employees and retirees of the City and of FCFA. Since the JPA was formed, FCFA has paid the full costs of the City’s Fire Safety CalPERS plans. The City will be required to pay back these amounts as part of the unwinding process contemplated in the Third Amendment to the JPA following the outcome of the OCSD’s 2022 ballot measure. The FCFA retained the actuarial firm Foster & Foster (formally Bartel & Associates) to calculate the actuarial accrued liability (AAL) for each person in the Fire Safety Classic tier, mirroring CalPERS actuarial valuation methods and assumptions. Foster & Foster has completed a detailed review of the past ten years to tally the City’s total amount owed, which is approximately \$982,000. A budget adjustment for this increased amount will be included in the FY 2022-23 Third Quarter Financial Status Report in May 2023. It is anticipated that funding for this adjustment will come from fund balance.

An additional estimate of \$100,000 is included in each year of the Forecast thereafter to fund the FCFA unfunded liability through the next five years. The estimates in this Forecast are provided by CalPERS and take into account the -6.1% investment return CaPERS experienced in FY 2021-22.

Table 2.9 CalPERS Retirement Unfunded Liability Five-Year Forecast								
	FY 2021-22	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		25.4%	51.5%	(44.7%)	11.7%	8.8%	8.4%	(5.7%)
Projection	\$ 1,519,503	\$ 1,904,700	\$ 2,301,691	\$ 1,271,885	\$ 1,420,835	\$ 1,546,399	\$ 1,676,816	\$ 1,580,980

Services and Supplies

Non-personnel expenditures include contractual and professional services, insurance, utilities, and other operating expenditures. These non-personnel related costs make up 38% of all General Fund expenditures. In addition, the portion of fire services contracted through the Five Cities Fire Authority (FCFA) and paid for with General Funds currently represents another 9% of total expenditures. The remaining portion of the City’s FCFA costs are paid from Fund 218, the City’s Local Sales Tax, Measure O-06 fund.

Fire Services - Five Cities Fire Authority (FCFA)

The City’s fire service and emergency response is provided through a Joint Exercise of Powers Agreement (JPA) combining fire department resources with the City of Grover Beach and Oceano Community Services District. Under current contract with FCFA, the current budget includes just over \$2 million for FCFA services as shown in Table 2.10.

Item 12.a.

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 12

Local sales tax dollars in the amount of \$645,000 in FY 2022-23 also contribute to pay for fire services but are not included as part of this General Fund analysis. An analysis funded by Arroyo Grande and Grover Beach is currently being completed to support the two cities' future decisions regarding staffing levels and costs to each of the member agencies. Based on the preliminary report provided by the consultant to the City Council on February 28, 2023, indications are that the cost to Arroyo Grande to maintain fire services will increase substantially as shown in Table 2.10 below. It should be noted that the \$3.1 million included in the Forecast for FY 2023-24 was based on the Baker Tilly Alternative Staffing plans Option A-4 from the PowerPoint presented at the February 28, 2023 City Council meeting (Attachment 1) and the amounts projected into the following years is a rough estimate at this point.

Table 2.10 Fire Services (FCFA) Five-Year Forecast								
	FY 2021-22	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		0.0%	0.0%	51.7%	(3.3%)	10.5%	(0.2%)	6.4%
Projection	\$ 2,052,061	\$ 2,052,061	\$ 2,052,061	\$ 3,114,000	\$ 3,012,000	\$ 3,328,000	\$ 3,323,000	\$ 3,536,000

Contractual Services

The City budgeted \$2.5 million for contractual and professional services in FY 2022-23. This category includes services provided by independent contractors for services such as legal, auditing, labor negotiations, police dispatch, landscaping, and professional and technical consulting and studies.

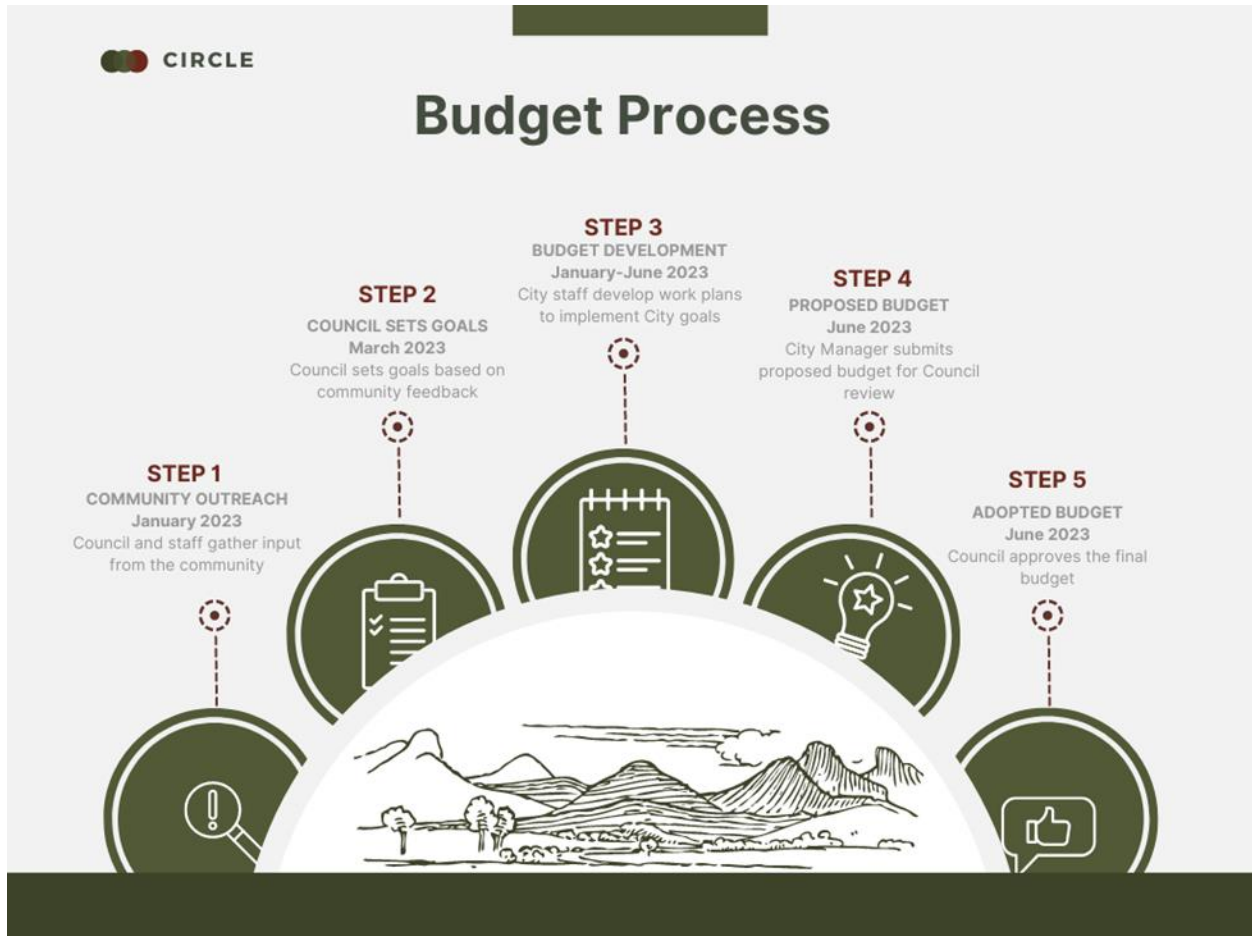
Table 2.11 Contractual Services Five-Year Forecast								
	FY 2021-22	FY 2022-23 Adopted	FY 2022-23 Projection	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
Growth Rate		38.8%	40.2%	(8.7%)	2.0%	2.0%	2.0%	2.0%
Projection	\$ 1,775,919	\$ 2,465,078	\$ 2,489,878	\$ 2,274,500	\$ 2,320,000	\$ 2,366,400	\$ 2,413,700	\$ 2,462,000

Forecast

Table 2.11 above reflects a large 40% increase from FY 2021-22 actual expenditures to the budgeted amount in FY 2022-23. The increase in the FY 2022-23 budget over the \$2.1 million in the FY 2021-22 budget was closer to 17% but some services expected to be encumbered that year were delayed and added to the FY 2022-23 budget. The increase in FY 2022-23, therefore, is largely due to several one-time contracts, such as services for a salary survey, a cost allocation, user fee, and development impact fee study, funding for the general plan update, consultant services in IT, and services related to new software products. Some of these projects were put on hold during the pandemic and are being completed now, which has temporarily inflated the budget for contractual services. These one-time items have been backed out of the forecast starting in FY 2023-24. Expenditures for contractual services are expected to increase by 2% thereafter.

Next Steps

The Five-Year Financial Forecast is part of a five step Budget Process as depicted in the timeline of the budget cycle below:



Steps 1 and 2:

Step 1 was completed through the Arroyo Grande Community Priorities Survey, which was published January 3rd and closed on February 20th. Results of the survey were presented to Council on March 2, 2023. Step 2 was completed on March 2, 2023, during the FY 2023-25 Goal Setting Study Session. The set of priorities developed during the study session will be used by staff to create work plans and a proposed biennial budget.

Step 3 includes:

- **March 2023 – Financial Forecast**
 - This report is the presentation to Council of the 5-year financial forecast with budget assumptions, challenges, goals, and strategies.

City Council
Consideration of General Fund Five-Year Financial Forecast
March 14, 2023
Page 14

- **Spring 2023 – Staff Develop Work Plans**
 - Staff will finalize operating and Capital Improvement Plan (CIP) preliminary budgets that reflect the established major City goals and the financial forecast.
- **May 2023 – Review of CIP**
 - Staff will present a proposed 5-year CIP for review and input from the City Council, and by the Planning Commission for determination of consistency with the General Plan.

Step 4 includes:

The proposed operating budgets, work plans, and CIP will be incorporated into a proposed FY 2023-25 Biennial Budget for discussion and consideration by Council in June 2023.

Step 5:

Adoption of the FY 2023-25 Biennial Budget will occur by the end of June 2023. Once Council approves the FY 2023-25 Biennial budget, FY 2023-24 funds will be appropriated on July 1, 2023.

ALTERNATIVES:

The following alternatives are provided for the Council's consideration:

1. Consider and receive the General Fund Five-Year Fiscal Forecast; or
2. Provide other direction to staff.

ADVANTAGES:

Receiving the Five-Year Financial Forecast Report will assist in informed discussions between the community, City Council, and staff about budgetary priorities as the City develops the upcoming FY 2023-25 Biennial Budget. In future budget cycles, this Report will be provided prior to the City Council's goal setting process.

DISADVANTAGES:

There are no disadvantages in relation to the recommended action.

ENVIRONMENTAL REVIEW:

No environmental review is required for this item.

PUBLIC NOTIFICATION AND COMMENTS:

The Agenda was posted at City Hall and on the City's website in accordance with Government Code Section 54954.2.

Attachments:

1. [February 28, 2023 Staff Report and Final Presentation](#)