CITY OF OAKLAND
BUDGET ADVISORY COMMISSION

Notice is hereby given that a **special meeting (date & time)** of the City of Oakland Budget Advisory Commission (BAC) is scheduled for **Wednesday, May 22, 2019** at **6:00 pm** In the **Hearing Room 4, City Hall, 2nd Floor**, at 1 Frank Ogawa Plaza.

Commission Members:

Lori Andrus, Jay Ashford, Ken Benson, Ed Gerber, Travis George, Geoffrey Johnson, Sarah Lee, Vincent Leung, Kasheica Mckinney, Caitlin Prendiville, Darin Ranahan, Brenda Roberts, Marchon Tatmon, Adam Van de Water, & Danny Wan

City's Representative:

Brad Johnson – *Finance Department*

Meeting Agenda:

1. Administrative Matters
   i. Welcome & Attendance

2. Discussion and possible action on submission to the City Council of a report regarding the FY 2019-21 budget and budget process. [90 minutes]

3. Possible scheduling of May 29 Special BAC Meeting [15 minutes]

4. June and July BAC Meeting Dates

5. Open Forum

6. Adjournment

<u>BAC 2019 – 2021 DRAFT Review of Mayor's Proposed Budget</u>

The BAC recommends the City Administrator confirm the General Purpose Fund Emergency Reserves were not appropriated during the year.

The City accumulated a reserve fund in accordance with the Reserve Fund Balance of 7.5% of the General Purpose Fund as of June 30, 2018. The policy requires approval of any appropriations of funds from the Emergency Reserves. Appropriations from the fund, if any, and reasons for appropriations made during the prior fiscal year should be included in Proposed Budget Policy under *Financial Summaries – Consistency with the Consolidation Fiscal Policy*, or a statement that no appropriations were made.

The BAC recommends the City conduct a further study of an appropriate revenue replacement for the Landscaping and Lighting Assessment District (LLAD)

Oakland property owners pay through property taxes into Oakland's LLAD fund. These property tax revenues support services for the more than 130 City parks, community centers and to maintain street lights and traffic signals. Established more than thirty years ago, LLAD revenues have not kept up with the increased costs to service these facilities as it never had a mechanism to adjust costs and payrolls as they increased over time. The City must identify a means to replace the LLAD to maintain existing service levels.

The BAC recommends that ongoing services not be funded with one-time funds.

The proposed FY 2019-21 budget uses one-time funding from the State Gas Tax fund to cover deficits in the Landscaping and Lighting Assessment District fund (LLAD) to balance the budget. . Using one-time funds is contrary to the City's Consolidated Fiscal Policy. The BAC memo of September 2017 included a recommendation that such one-time funds should not be used to fund continuing services.

The BAC recommends the City plan for anticipated costs and reasonably estimate revenues to retain balanced budgets.

The City's financial policies require a balanced budget that limits appropriations to the total of estimated revenues.

The Mayor's proposed 2019-21 Budget acknowledges the widening gap between sources of revenues within available funds and the growing rate of expenditures. The proposed budget starts out with a projected revenue shortfall of $49 million with $25 million within the General Fund (1010). The Mayor's proposal has two overarching goals to bridge this gap and to provide for a balance budget. First, the proposed budget includes no major increases in service levels without cost recovery or project funding. Second, every attempt was made to transfer funds from unhealthy funds to other useful or eligible sources and to only add personnel when secured by grant funding or with a cost recovery source.

Project Carryforwards and Encumbrances

No recommendation

Project carryforwards are financial obligations against reserves for current purchases that will be paid for in the following fiscal year. These adjustments should be limited. The City's Financial Policies require the Finance Department to review all proposed carryforwards and provide a recommendation to the City Administrator. The proposed budget presents fund balances reduced for carryforward amounts and total carryforward amounts are *not* shown in total.

2. The funding of the Capital Improvement Budget is substantially increased as compared to past budget. The review of this portion of the Budget has been assigned to the Affordable Housing and Infrastructure Bond Oversight Committee. Therefore, we will not have a comment on the Capital portion of the budget.

The BAC recommends that any performance management program include sufficient staff for implementation and that vacancy rates be considered as part of such a program.

We note in the Budget the proposal by CM Taylor to establish a Performance Management Program. We support this proposal which is consistent with our prior recommendations to include "comparative analytics." This program will place an added workload on staff. Such data should include continuing reports on vacancy rates. We therefore recommend that such a program include the provision of necessary staff. We further recommend that the Council consider the workload placed upon staff by its regular actions requiring additional reports on matters it is considering and provide necessary staff to meet this workload.

The BAC reiterates its recommendation that more time be spent exploring the revenue side of the budget.

Recognizing that the budget is both a revenue and expenditure program we have in the past recommended that significantly more time be spent on reviewing the revenue side of the budget. In our prior reports we have recommended seeking greater public engagement in revenue analysis and even year in depth examination of various revenue scenarios. Following is an extract from our prior report discussing this in more detail

> The BAC recommends that budget review and adoption place greater focus on revenues. The primary focus of the budget adoption process is often on proposed expenditures, whereas the equally critical revenue side of the ledger is less well understood by the public and subject to less external scrutiny. The most comprehensive review of city revenues is published by the City Administrator's Office in its biennial Five-Year Financial Forecast, which summarizes major revenues sources, reports prior and current year actual collections, and projects future revenue generation. City staff develops revenue forecasts, and the report notes that staff consult

with “independent budget and economic experts to confirm the soundness of the assumptions and analysis.”

To improve transparency and enable a broader understanding of the budget’s underlying revenue assumptions, the BAC recommends that such independent analyses of City revenue projections, be shared with the Council and the public. This could be achieved through an annual public forum at which relevant subject matter experts evaluate the performance of key City revenues, assess the validity and level of risk inherent in City staff projections and offer informed recommendations and fresh perspective to City staff and elected officials for consideration.

Additionally, the BAC recommends that the City Administrator’s Office implement a schedule for conducting deeper analysis of specific questions related to major revenue sources. Examples might include:

- A benchmarking study that compares Oakland’s tax rate structures (for, e.g., business tax, property transfer tax, impact fees) and the revenue they generate to other comparable jurisdictions
- Analysis of the pros and cons of moving from a flat real estate transfer tax to a split role for residential and commercial properties
- Thorough cost-recovery analysis of significant fees
- Inclusion of an analysis of impact fee revenues and expenditures in the Five Year Financial forecast
- Analysis of the foregone revenues and countervailing benefits that result from exempting owners of low and moderate-income housing from payment of the Business License Tax and Parcel Tax
- Scenario-based analysis of the City’s risk exposure as relates to its heavy reliance on property tax and real estate transfer tax revenues
- An equity assessment of who is impacted by the City's current revenue generating measures and any measures under consideration
- Analysis of novel revenue generation methods employed by other charter cities and their potential application in Oakland

Source BAC Report September 29, 2017.

In particular, the BAC recommends that additional revenue sources be explored for unfunded OPEB and pension costs.

The BAC commends the inclusion of Council member priorities.

We are pleased to note that this budget includes a statement of priorities by all Council members. The CFP invites "up to seven expenditure priorities in ranked and/or weighted order" including revenue suggestions. However priorities were not always included. We recommend the inclusion of priorities and revenue suggestions.

The BAC recommends that, to the extent feasible, the City assess and disclose private-sector and other governmental bodies' expenditures in Oakland on items that could be deemed municipal services, such as homeless services, in order to assess the full scope of resources directed at a problem.

Significant private sector and other government monies are being expended upon services required by Oakland residents in numerous program areas including homelessness. We recommend that the budget include a table of such expenditures to the extent feasible.

The BAC recommends that the budget document disclose its methodology for determining the full cost of services, such as how it determines overhead costs per FTE.

How to inform public discussions about the full costs of providing services? The line items for personnel includes direct salary plus various overhead costs. Where in the budget is this method described and the effects illustrated?

The BAC recommends that the budget clarify whether it is complying with the requirement to spend 25% of excess RETT on unfunded liabilities.

One concern with the MPB is how Excess Real Estate Transfer Tax (RETT) revenues are being used to fund OPEB. The MPB indicates that "it allocates several million dollars to the repayment of the City's OPEB unfunded obligation and thus complies with the use of excess RETT." *Id.* at 191. The OPEB Funding Policy requires that Excess RETT contributions be made on top of the 2.5% of payroll above pay-go mandatory contributions. The CFP requires that "[a]t least 25% [of RETT] shall be used to fund accelerated debt retirement and unfunded longterm obligations: including negative fund balances, to fund the Police and Fire Retirement System (PFRS) liability, to fund other unfunded retirement and pension liabilities, unfunded paid leave liabilities, to fund Other Post-Employment Retirement Benefits (OPEB)." CFP Part C.

The MPB estimates RETT of $401,760, meaning $100,440 should go to unfunded liabilities. MPB E-131. This is on top of the City's pay-go obligations for OPEB and its additional 2.5%

of payroll contribution toward OPEB. However, it is unclear from the summary if the use of RETT funds complies with this requirement, and the BAC was unable to determine from the face of the MPB whether it complies with this requirement.

The BAC recommend that the budget more clearly state whether or not it is complying with the RETT requirement, including providing all information necessary to determine whether it is in compliance, including the amount of mandatory payroll contributions, the total payroll for the City, the amount of RETT, and the total budgeted amount for OPEB and other unfunded liabilities.

The BAC commends the City for establishing and following its OPEB policy. However, it recommends that the budget document analyze the difference between the City's contributions under the OPEB policy and its actuarially determined OPEB contributions.

After passage of the FY 2017-19 budget in June 2017, the City took several steps toward addressing OPEB liability, culminating in the February 2019 adoption of an OPEB funding policy. *See* Resolution No. 87551. The City of Oakland Other Post-Employment Benefits (OPEB) Funding Policy (the "OPEB Funding Policy") provides that, "[b]eginning in FY2020, the City will contribute an additional 2.5% of payroll above pay-go into the OPEB Trust on an annual basis" until its promised OPEB benefits are fully funded. OPEB Funding Policy at 4. In addition, the City is to make further one-time contributions when Excess Real Estate Transfer Tax (RETT) thresholds are met. In addition, the City is to pursue periodic adjustments to benefits to ensure full funding and plan sustainability, with periodic assessments in advance of any rounds of collective bargaining. *Id.*

The Mayor's Proposed Budget ("MPB") notes that the City had an unfunded OPEB liability of $849 million as of July 1, 2017, an increase of nearly $20 million over its September 2017 estimate. MPB 187. It notes two major changes to address unfunded OPEB liability: (1) an agreement with its sworn public safety unions to cap retiree medical benefits for existing employees and retirees effective January 1, 2010 and new, lower-cost tiers for employees hired after January 1, 2019, which it estimates to reduce its unfunded OPEB liability by $175 million. *Id.* at 188. In addition, it purports to meet the 2.5% of payroll above pay-go contribution requirement in the OPEB Funding Policy. *Id.* at 189.

BAC commends the City for amending its Consolidated Fiscal Policy to set aside 2.5% of payroll ("Additional OPEB Payments") towards its unfunded OPEB obligations on top of its existing pay-as-you-go expenses. These additional OPEB Payments are projected to be $10 million in each of FY2019-20 and FY2020-21.

In a report prepared for the City on January 14, 2019 by PFM Group Consulting LLC, the

City’s pay-as-you-go expenses are projected to be $31.4M in FY2019-20 and $33.6M in FY2020-21. Meanwhile, the City’s actuarially determined OPEB contributions (“ADC”) are expected to be $83.5M for FY2019-20 and $87.9M for FY2020-2021. The ADC is the amount the City ought to pay to ensure sufficient funds for future benefits. It includes the City’s pay-as-you-go expense as well as an amortization payment towards its unfunded OPEB liability.

Even though the City recently negotiated benefit packages with its employees that will reduce its total unfunded OPEB liability in the long term, and even though $10M in Additional OPEB Payments in each of FY2019-20 and FY2020-21 are an improvement over previous longstanding City practices, such payments will not be sufficient to bridge the gap between the City’s ADC and pay-as-you-go expenses, which will be $52.1M in FY2019-20 and $54.3M in FY2020-21.

BAC also recommends that the City expand its OPEB discussion in the Proposed Budget to note that $10M in Additional OPEB Payments will still be insufficient to cover the City’s ADC in FY2019-20 and FY2020-21.

The BAC recommends that the City focus spending one-time revenues on paying down unfunded liabilities and clarify which spending is on CalPERS and which is on PFRS.

The MPB outlines unfunded CalPERS retirement benefits of $1.547 billion as of June 30, 2017, which includes $714 million in unfunded liability for the Public Safety Plan and $833 million in unfunded liability for the Miscellaneous Plan. MPB 187. As of June 30, 2016, those figures were $1.578 billion, $706 million, and $872 million, respectively. FY 2017-19 Budget E-131.

In addition, the MPB identifies $300 million in unfunded liabilities for the closed Police and Fire Retirement System (PFRS) as of June 30, 2017. MPB 187. That figure was $311 million as of July 1, 2016. FY 2017-19 Budget E-131.

The BAC is heartened to see these numbers trending in the right direction, notwithstanding policy changes at the state level putting an upward pressure on such unfunded liability, and understands that specific contribution amounts are set by CalPERS for the unfunded CalPERS retirement benefits. Nevertheless, the BAC urges the City to continue to invest one-time revenues in reducing unfunded retirement liabilities beyond the minimum mandatory contributions.

On page 187, the Proposed Budget notes that “the City’s estimated pension cost for FY2019-20 is $178 million.” On page 47 of the Five-Year Financial Forecast, meanwhile, the City’s assumed CalPERS unfunded actuarial liability is $102.6M for FY2019-20 and

$114.4M for FY2020-21.

BAC recommends that the Proposed Budget clarify whether the $178 million figure listed on page 187 is for all City pension expenses (including PFRS), or just for CalPERS. Moreover, BAC recommends that the Proposed Budget make clear whether such expenditures are from the General Purpose Fund or from other funds, and which departments are responsible for such expenditures.

Cheiron, an actuarial and financial consultancy firm, produced the most recent Actuarial Valuation Report for the Oakland Police and Fire Retirement System ("PFRS"). It shows that PFRS had an unfunded actuarial liability of $299.9 million as of July 1, 2018, and that its smoothed funded ratio, the ratio of actuarial assets over actuarial liability, was 53.7% as of June 30, 2018.

Historically, the City has relied on a number of measures to fund PFRS obligations:

- Tax revenues from Measure R, passed in 1976, and from Measure O, passed in 1988 (collectively, pension tax override revenues, or "PTOR")
- A New York Life annuity purchased in 1985
- Proceeds from multiple bond issues, of which series from 2001 and 2012 are currently outstanding ("POBs")
- Annual payments from the City ("Annual PFRS Payments")

PTOR last until 2026 and reflect a rate of 0.1575% on assessed property values. The Proposed Budget expects PTOR to be $112.9M in FY2019-20 and $118.1M in FY2020-21.

Meanwhile, POBs were historically structured so that their debt service would be adequately covered by PTOR. The Proposed Budget expects POB debt service of $67.0M in FY2019-20 and $68.4M in FY2020-21. Additionally, the City began Annual PFRS Payments in FY2017-18 to reduce its unfunded actuarial liability. Per Cheiron, these payments are projected to be $43.4M in FY2019-20 and $43.8M in FY2020-21. Together with the PTOR, they are designed to eliminate the City's unfunded PFRS liability by 2026, as directed by the City Charter.

This leaves expected excess PTOR, net of POB debt service and Annual PFRS Payments ("Excess PTOR"), of $2.5M in FY2019-20 and $5.9M in FY2020-21.

BAC acknowledges and commends the long-term work of City staff to plan and provide for the City's 2026 target for full PFRS funding. BAC, however, recommends that the City expand its PFRS disclosures in the Proposed Budget to reflect the following:

- Provide updated projections that show that PTOR are sufficient to fund POB obligations through 2025
- Provide an update on the City's progress towards eliminating its unfunded PFRS liability by 2026
- Confirm that the City's FY2019-20 and FY2020-21 contributions towards the unfunded PFRS liability come from PTOR
- Confirm that Excess PTOR are applied or dedicated towards the City's unfunded PFRS liability

Moreover, BAC recommends that the City explore whether tax measures similar to PTOR can be submitted for voter approval to fund the City's other unfunded liabilities, for example its CalPERS and OPEB obligations. Since current PTOR generate substantial revenues, and are a cost that Oakland taxpayers have been used to paying for decades, an ideal political opportunity exists in 2026 for a new ballot measure at that date. Given that the City's recent Five-Year Financial Forecast anticipates operating deficits over the next five years, however, due in no small part to rising obligations from pensions and other unfunded liabilities, the City may not have the luxury of waiting until 2026 to identify new revenue sources for the relief of its non-PFRS unfunded liabilities.

The BAC commends the City on its progress in addressing negative funds.

The MPB identifies negative funds in the amount of $60 million, $32.3 million with a repayment plan, $27.7 million of which are reimbursement funds, and $0.2 million of which are funds with no repayment plan. MPB E-127. For example, the Capital Improvements Reserve Bond Fund (Fund 5510) is a negative fund which is on a repayment schedule in the amount of $123,000 for retirement by 2028-29. These are trending downward from the FY2017-19 budget, which showed negative funds of $73 million, $26.9 million with a repayment plan, $31.8 million of which were reimbursement funds, and $14.2 million with no repayment plan; and accrued leave of $47.1 million. FY 2017-19 Budget E-131.

The BAC commends the City for making progress on these unfunded long-term liabilities, and refers the Council back to their _ 2019 recommendations for addressing negative fund balances.

The BAC recommends that the budget separate out sick and vacation leave liabilities.

The budget identifies as a liability accrued vacation and sick leave of more than $49 million as of June 30, 2018. MPB E-127. Regarding accrued vacation and sick leave, the BAC recommends breaking apart these two amounts in the budget document for transparency's purpose, given the different legal status of these respective liabilities (accrued vacation time being earned wages payable upon departure from employment and accrued sick leave being lost upon departure from employment).

The BAC notes that the proposed budget backslides from the 2017-19 budget in its use of one-time revenues to fund ongoing expenditures and recommends that the final budget explore ways to reduce or eliminate reliance on such revenues for ongoing expenditures, focusing one-time revenues on paying down unfunded liabilities.

In our September 2017 report, we recommended that future documents summarizing the adopted budget include an exhibit that clearly itemizes one-time sources and uses. *See* BAC's Report on the City of Oakland's Biennial 2017-19 Budget Cycle 4-5 (Sept. 2017). However, our May 2017 report faulted the Mayor's proposed budget as relying on one-time funding to support such ongoing services as the ASSETS program and park maintenance. *See* May 2017 Report at 2.

This year's MPB purports to "limit[] the use of one-time resources for ongoing expenditures . . . ." MPB at 11. However, it includes substantial reliance on one-time funding for ongoing expenditures. *See id.* at 191-92; *see, e.g.*, *id.* at 28 ("[a]ppropriate one-time funding of $100,000 in FY 2019-20 for Phase I of the Healthy Home Rental Inspection Program"); *id.* ("[a]ppropriate $480,000 in one-time funding ($240,000 per each fiscal year) for Last Saturday Free Dump Days"); *id.* at 29 ("[s]ustains funding for emergency medical supplies using one-time funds in Measure N"); *id.* at 68, 71, 73-74, 278, 281, 290, 296. This use of one-time funding for ongoing expenditures appears to outstrip the use of one-time funding for ongoing expenditures in the FY 2017-19 budget. *See* S. Landreth Transmission Letter, FY 2017-19 Adopted Policy Budget 1 (Oct. 2017).

The Consolidated Financial Policy ("CFP") notes that one-time revenues shall be used for one-time expenditures, debt retirement, or unfunded long-term obligations such as negative fund balances and PFRS/CalPERS/OPEB liabilities. It also recommends that any remaining one-time revenues remain as available fund balances. Other uses must be authorized by City Council resolutions that explain the need for using such one-time funds in contravention of CFP, and the plan to return to using such one-time funds in accordance with CFP.

The FY2019-2021 Proposed Policy Budget ("Proposed Budget") highlights two instances where one-time revenues are used to fund ongoing services. Moreover, in the May 7, 2019 City Council meeting, City staff ("Staff") presented two resolutions to enable these exceptions to the CFP.

In the first, $3.0M in annual funds for ongoing parks and recreation costs comes from a one-time source: the State Gas Tax Fund. The Proposed Budget also freezes 8.5 FTEs, yielding in $1.0M annual savings. Funding for parks and recreation services normally comes from Landscape & Lighting Assessment District ("LLAD") revenues, which have remained unchanged for over 30 years. To align with the CFP, Council Resolution [#___] authorizes and directs the City Administrator to pursue a ballot measure that will eliminate the use of such one-time funds in the future.

In the second, $0.2M in annual funds for medications used by the Oakland Fire Department ("OFD") in emergency medical services ("EMS") comes from Measure N. OFD is usually the first responder in EMS situations in Oakland which may require the use of medications. Alameda County's new Ambulance Contract no longer provides for County ambulances to replace medications used by local fire department paramedics in EMS situations. To align with the CFP, Council Resolution [#___] authorizes and directs the City Administrator to pursue revenue enhancements, negotiations with Alameda County, and additional fiscal adjustments to provide permanent and ongoing revenue for paramedic services.

BAC Process Ad-Hoc Committee - May 2019

Version 0.1 - 05/14/2019

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STRUCTURE:

Positive Feedback: this is the first budget cycle where ALL districts held budget forums. Forums were accessible to attendees, staff provided easy to read Powerpoint presentation, councilmembers were present at the forum, highly knowledgeable staff were present too, there was a mechanism in place to capture community feedback (including both open mic time and question card submission.)

Recommendation: include accommodations for non-native English speakers with language headsets for those who would want them. ~~Also~~, a few copies of translated handouts and literature.

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Recommendation: have a timer/facilitator in order to prevent run-on storytelling during open mic time. Establish and communicate ground rules at the beginning of the meeting (ideally by the councilmember) to respect the process, allow time for all participants to speak.

Recommendation: Come up with an approach for how to handle policy questions (i.e. council member vs staff).

Recommendation: what are additional foundational educational items to help citizens understand key budget concepts. (e.g. fund rigidity, general fund/GPF/restricted funds).

Recommendation: As an ongoing educational tool, council/staff to have the budget forums in the off-years when there is more time to go in depth.

Recommendation: Ensure maximum transparency around the Council budget team. Ensure that budget team deliberations are done in a public setting that is widely advertised.
During this budget cycle the Mayor used a Budget Ambassador program to increase budget literacy.
Recommendation: Develop a Budget Ambassador program which can be broadly and regularly used throughout the community to increase budget literacy.