
CITY MANAGER'S FISCAL YEAR 2020 BUDGET MESSAGE



To the Honorable Mayor and Members of the City Council:

With my great appreciation to the many City staff members who helped in its development, I submit to the City Council and Santa Cruz Community the Fiscal Year (FY) 2020 Budget. Building on our Fiscal Sustainability Plan, the objectives used in developing this budget were to present a balanced budget with prudent revenue and expenditure estimates; to do the best job possible of maintaining current excellent levels of service to the community; and to implement City Council's priorities in the City's Work Plan.

The FY 2020 Budget can be characterized as "proceed with caution." Thanks to both community support for Measure S last year and prudent and proactive financial planning, Santa Cruz is in better shape than many cities in California with the complexity of our needs.

However, the deficit we projected in our Fiscal Sustainability Plan is growing at a more accelerated pace than expected due to significant flattening in tax revenue (such as fewer taxable items and more nontaxable services purchased) unanticipated costs (such as those resulting from the Martin vs. Boise court decision on homelessness), as well as employee cost increases. The City's budget is within manageable parameters, but not strong enough to support unanticipated expenses, needed infrastructure repairs and maintenance, or to withstand significant emergency spending. As a result, reductions to City services will be necessary to balance the FY 2020 Budget.

The total budget for FY 2020 is \$263.3 million. This includes an operating budget of \$242.2 million and capital investment project (CIP) budget of \$21.1 million (of which none is for General Fund capital investment projects). The major operations included in the FY 2020 operating budget are the City's General Fund of \$107.0 million, which supports our day-to-day public safety, roads, traffic, and parks operations; and the operations and capital budgets of the Water Enterprise Fund (\$46.9 million); the Wastewater Enterprise Fund (\$23.4 million); and the Refuse Enterprise Fund (\$24.4 million).

Our Fiscal Sustainability Plan has served us well and thanks to City leadership and the support of our community, we have been able to recover from the worst recession in recent history, as well as to make significant progress to achieve the City's Strategic Vision and Work Plan.

Nonetheless, as I have reported in the last several budget messages, despite our achievements, there are dark clouds looming on the horizon for our General Fund that will require adjusting our fiscal strategy as well as making difficult decisions as the City continues to face growing budget deficits.



The overall economic trends reported in prior budget messages persist. While we continue in a period of positive economic activity with growing revenues, the foundation for those revenue sources is declining, particularly our sales tax, which has been a significant source of funding for the General Fund. Our voters approved a quarter-cent sales tax increase in June of 2018 with a passage rate of 72%, which was important for the preservation of City

services. However, in addition to flattening revenues, costs are increasing to the point of outpacing revenue growth. Employee costs are growing due to employee retirement system (PERS) rate increases passed on to cities from PERS investment shortfalls, increases to health insurance costs, and the challenge of providing salaries that are competitive enough to recruit, and as importantly, to retain employees. We continue to face a major deficit in our General Fund capital improvement investments, resulting in General Fund deferred maintenance growing at an unsustainable level. An economic slow-down is forecast in the coming years which will further strain the budget.

Our Fiscal Sustainability Plan calls for continued strategies to increase revenues, reduce expenditures, and implement best management fiscal practices and policies. Unfortunately, our most recent modeling, based upon the latest information on cost commitments and risk factors, points to a larger General Fund deficit for the coming budget year of \$3.1 to 3.2 million and potentially greater depending on upcoming decisions affecting revenues and expenditures. To maintain a balanced budget, the FY 2020 Budget must be adopted with changes to address this deficit.

Due to proactive efforts within our Fiscal Sustainability Plan, we have multiple strategies underway to balance the budget and address a previously anticipated \$1.6 million General Fund deficit as well as larger shortfalls in later years. These strategies include a second phase of the staff-led, award-winning Action Labs, reductions put forward by each department, and preparation for potential 2020 ballot measures.

However, I cannot emphasize enough the fact that the City's budget deficit has significantly increased beyond projections over the last several months which will require the City Council to make difficult decisions as part of the FY 2020 Budget deliberations, as well as potentially

making additional reductions in the fall of 2020, depending on the City Council adopted budget. The deficit has grown from \$1.6 Million to a range of \$3.1 to \$3.2 million, depending on Council actions.

We have therefore approached the FY 2020 Budget with more conservatism and caution. One step we are taking is to further restrain General Fund expenditures by including minimal new General Fund positions in the FY 2020 Budget; there are a few additions in the Enterprise Funds and the Library system which do not rely on the City's General Fund. Another step is recommending against new General Fund or related Public Trust Fund CIP projects. As I noted above, this is a disappointing turn as these projects are sorely needed and our infrastructure will only continue to degrade without investment. Additionally, the City Council, through a Revenue Subcommittee, is expected to explore revenue enhancements for upcoming special or regular elections. Although any measures put before the voters may not yield revenues for FY 2020, they would provide vital support in FY 2021 and beyond.



The FY 2020 Budget balancing undoubtedly will be difficult, but we are sharply focused on prudent and effective strategies to ensure fiscal sustainability while preserving our valuable services to the community.

I would like to extend my deepest appreciation to our budget development team including our Finance Director, Marcus Pimentel, his excellent budget staff, as well as all of the department budget leads and coordinators. They have improved the budget document and process every single year. We have more staff from all levels of the organization involved in providing input to decision making than ever before.

I would also be remiss if I didn't acknowledge the tremendous dedication and support of the City's Executive Team. They focus on the big picture and truly look beyond the boundaries of their department to contribute toward problem solving and the improvement of programs and services critical to the quality of life in our community.

Finally, I want to thank the City Council for commitment to the community. I look forward to your deliberations as we work to respond to our community's challenges.

Sincerely,

Martín Bernal
City Manager