

DATE ISSUED: February 2, 2005

REPORT NO. 05-032

ATTENTION: Honorable Mayor and City Council
Docket of February 8, 2005

SUBJECT: Council Policy 000-20 Review and Analysis

SUMMARY

Issue - Should the Mayor and City Council adopt the City Manager's recommendations on the amendment and implementation of Council Policy 000-20, "Annual Council Programming?"

Manager's Recommendation – Amend Council Policy 000-20, "Annual Council Programming," as described in the recommendations section of this report.

Other Recommendations – None.

Fiscal Impact – None.

BACKGROUND

During the City Council meeting of June 15, 2004, Councilmember Frye requested an analysis of Council Policy 000-20, "Annual Council Programming" (see Attachment "A"), and its applicability to the current budget hearing process. On June 21, 2004, Deputy Mayor Atkins presented a memorandum to the City Manager requesting full implementation of Council Policy 000-20 (see Attachment "B").

Council Policy 000-20 was first adopted 28 years ago in 1976. The purpose of the Policy as stated is to "increase the Council and citizen involvement in the formative stages of budget preparation and to establish a set of Citywide goals and objectives, and budget priorities on an annual basis."

The original policy described a schedule that would identify goals, objectives, and program priorities in early October of each year, almost nine months in advance of actual budget implementation.

Council Policy 000-20 was later amended for the first time in September, 1977 to identify goals, objectives and program priorities in late October of each year. The Policy was again amended in October, 1981 to perform these functions in late November of each year.

When Council Policy 000-20 was brought before the Rules Committee in 1981 and subsequently amended, the actual recommendation put forth to the Committee in a City Manager's Report by then-City Manager Ray T. Blair, Jr. was for the repeal of this policy. In that report, the City Manager indicated that "in actual practice, only two parts of this annual programming effort have been followed: the public hearing of citizen views and the City Manager's Report" (see Attachment "C"). From this statement it would appear that the Policy Committee was never convened prior to 1981, and there is no indication that the Committee was convened subsequent to that report. The Rules Committee voted in 1981 to approve one of the proffered alternatives in the report, which was to amend Council Policy 000-20, moving the dates for the City Manager's Report and the public discussion hearings from October to November and to keep the Council Policy in place. The Policy Committee as defined in the Council Policy consists of Council staff, a Legislative Analyst, committee consultants, and a City Manager representative.

Through several City administrations, it would appear that the process described in Council Policy 000-20 has evolved into the current Proposed Budget Process. As will become evident in the description of the current process, most aspects of Council Policy 000-20 remain intact, albeit in different time frames from those outlined in the Council Policy, with the primary exception being the convening of a Policy Committee.

It should also be mentioned that, in the process of researching this issue, Financial Management came across another Council Policy pertaining to budget development. Council Policy 000-02, "Budget Process," originated in 1991, called for the City Manager to begin preparation annually of a two-year budget proposal for City Council consideration. The policy also indicated that "No later than fiscal year 1996, [the two-year rolling budget] process will be reviewed by the City Manager and a report submitted for Council review containing a recommendation on what, if any, amendment to section 69 and/or 71 of the City Charter should be sought."

The two-year budget was abandoned after the publication of the Fiscal Year 1993 Proposed Budget due to the uncertainty of City revenues in light of the State of California's implementation of the ERAF. Financial Management has not yet determined whether a formal review of the two-year budget implementation ever occurred, and if so, the result thereof. The City Manager will present a separate report to the Mayor and City Council regarding this policy, its history and its feasibility.

Due to the timing of this report on Council Policy 000-20, the necessity of obtaining Mayor and

City Council direction on what the new budget process and timeline will be, and the desire to receive public input on this year's budget issues, this report does not include any actual discussions of budget priorities or policies for Fiscal Year 2006. Rather, the report illustrates both the current budget process and the process under the current Council Policy 000-20, and makes recommendations for an alternative budget timeline and process.

It is anticipated that for the Fiscal Year 2006 budget process, Mayor and City Council budget discussions, as well as public input, will take place at the February 28, 2005 City Council session. The Mid-Year Report and the City Manager's Five-Year Financial Plan, tentatively scheduled to be presented to the Mayor and City Council on February 14 and February 28, respectively, will serve as the bases for these budget discussions.

COUNCIL POLICY 000-20 vs. CURRENT PROCESS

[Please see attachment "E" for a visual comparison of the current budget process, the existing Council Policy 000-20, and the proposed amended Council Policy 000-20.]

Timeline – Council Policy 000-20

The requirements of the current Council Policy 000-20 include a report from the City Manager presented to the City Council in early November that would serve as the "basis for programming." This report would include current goals and objectives, a summary of allocated funds, forecasts of revenues and expenditures, and suggested service improvements and/or cutbacks.

Also in early November, but after the distribution of the City Manager's Report, a Policy Committee comprised of Council staff, (the) Legislative Analyst, committee consultants, and City Manager representative(s) would be convened. The Policy Committee would make recommendations to Council regarding policy guidelines, Citywide goals and objectives, and priority of community needs.

Additionally, Council Policy 000-20 indicates that the City Council is to conduct a public hearing in mid-November, and devote at least one meeting to formulating Citywide goals and objectives, program priorities, and other budget guidelines in late November. Once programming decisions have been determined by the Mayor and City Council through this process, the City Manager is to convey this direction to departments in late November, for consideration during the development of their respective budgets.

Council Policy 000-20 provides no further direction or chronology for the budget preparation process, but indicates that the "normal budget preparation and review process will ensue."

Timeline – Current Process

The current Proposed Budget Process incorporates many aspects of Council Policy 000-20, although not in the same time frame.

During the months of November and December, the Financial Management Department lays the initial groundwork for the development of the upcoming fiscal year's budget, based on Mayor and City Council direction, which usually occurs throughout the year, as well as City Manager direction. This includes a variety of essential preparatory activities, such as the collection of projections from responsible City departments for such non-discretionary items as utilities, information technology, and vehicle usage and assignment charges; compilation of information on expenses related to new facilities coming online; development of initial estimates for personnel-related expenses such as negotiated salary adjustments, workers' compensation and retirement contributions; completion of any departmental structural changes in the budget application; and development and publication of the Budget Reference Manual, a guide for operating and capital improvement program budget processes.

Generally within the first three months of each calendar year, the City Manager delivers to the Mayor and City Council a Financial Status and Forecast Report, commonly referred to as the Mid-Year Report. This report identifies the fiscal status of the current fiscal year, including revenue performance and expenditure status and projections, and also provides revenue forecasts and anticipated expenditure requirements for the upcoming fiscal year. This report raises issues or challenges regarding the upcoming fiscal year's budget and seeks direction and priorities from the Mayor and City Council. The report is typically presented with a discussion by the City Manager at a regularly scheduled City Council meeting, and parallels the "basis for programming" City Manager's Report referenced in Council Policy 000-20.

An additional component of Council Policy 000-20 that is included in the current Proposed Budget Process and exceeds the requirements of the Council Policy is the availability of Community Budget Forums in each council district, typically during the months of February and March. The Community Budget Forums, held jointly by the City Council Offices and the City Manager's Office, allow constituents the opportunity to discuss their specific council district needs and requirements during the development of the proposed budget. The convening of these forums within the respective communities also encourages greater attendance by citizens. In addition to the Community Budget Forums, the majority of the budget hearings held during May and June are also open for public comment and feedback. The Council Policy identifies only one public hearing to be held to solicit input from citizens.

While the background information of Council Policy 000-20 suggests that the initial stages of the budget development process occur absent citywide goals, objectives and priorities, there are numerous processes and forums that keep current City goals and priorities in the forefront. The

City's management is clear on these priorities and considers them while performing initial budget development activities.

Throughout the fiscal year, the City Manager, Mayor and City Council remain mindful of the core priorities of the City of San Diego. Funding of public safety needs has been and will remain paramount where General Fund expenditures are concerned. There are also several ‘yardsticks’ that City management uses to be reminded of established funding priorities, some static and some more dynamic. These include but are not limited to the Mayor’s Ten Goals, the Deferred Maintenance Report, the Mid-Year Report, and the recently released Fiscal Year 2004 Unfunded Needs Report, as well as ongoing guidance from the Mayor and City Council and Council Committees. These and other reports or policies provide a certain beneficial redundancy that keeps priority service needs at the forefront in the City’s budgetary prioritization and decision-making processes.

To augment these management tools, the City Manager is in the process of developing a five-year financial plan. This plan will utilize available information regarding funding needs and priorities, revenue projections, and revenue-generating opportunities to develop a comprehensive, five-year funding and budget plan. It will include a list of funding requirements, both operating and capital, and a plan to meet those requirements. Given the amount of unfunded needs facing the City, prioritization of needs as well as revenue generating opportunities will be explored.

ANALYSIS

The intent of Council Policy 000-20, that being to have earlier and more direct Mayor and City Council and public participation in the budget planning and prioritization process, is of benefit to the City of San Diego, and to City management in particular as it enables them to prepare annual budget submittals with a better understanding of the Mayor and City Council’s, as well as the public’s, funding priorities.

The process described in Council Policy 000-20 could be incorporated into the current budget process in its current state if the Mayor and City Council so agree. There are, however, some factors to consider when analyzing the implementation of the Council Policy.

Budgeting in the City of San Diego is a revenue-driven process. The amount of revenue estimated by the City determines the amount of expenditures that are appropriated and, consequently, the extent to which public service needs and priorities can be addressed. Therefore, while priority-setting discussions can take place at a conceptual level in November as stated in the Council Policy, the extent to which those priorities can be met, and the specific identification of funding amounts, may be better to occur at a point in time when there is sufficient information available to provide informed and reliable General Fund revenue projections.

Without accurate revenue forecasting, identification of specific funding levels for service improvements and/or cutbacks as described in the Council Policy may not be beneficial. The issuance of the Financial Status and Review Report by the City Manager in the first quarter of the calendar year is purposely timed to allow the compilation of six months of revenue history for the current fiscal year, which provides the basis for revenue forecasting in the subsequent fiscal year. This data allows more accurate forecasting of revenues due to the receipt of Property Taxes in

December and Sales Tax revenue from the holiday shopping season in January. Revenue forecasts prior to December would rely on less informed estimates of property tax and sales tax revenue, which comprise the majority of General Fund revenue.

The original Council Policy was written two years prior to the historic Proposition 13 passage, which severely limited the amount of Property Tax revenue that could be realized by the City. Additionally, the Council Policy also preceded actions at the State level that have impacted the amount of revenue the City receives. These two factors serve to compound the importance of accurately forecasting General Fund revenues prior to making specific budgetary decisions.

With the recent State actions, in fact, property tax now comprises approximately 35% of total General Fund revenue. A variance of as little as 1% in revenue projections could represent up to \$2.9 million for property tax and \$1.3 million for sales tax. Thus, the unavailability of sufficient data to project these revenue sources may impede the Mayor and City Council's ability to develop specific direction on funding levels for General Fund services in November or December, prior to availability of sufficient revenue data to formulate sound projections.

Similar issues apply to the projection of anticipated expenditure requirements for the upcoming fiscal year. While preliminary analysis and projection begins in the November-December time frame, sound estimates on upcoming expenditure obligations are not readily available until at least six months of current fiscal year expenditures have occurred and the data analyzed.

The issues pertaining to revenue and expenditure forecasting do not preclude the presentation of a report by the City Manager to the Mayor and City Council in November or December. It is suggested that the City Manager's Report to the Mayor and City Council at the end of the calendar year focus primarily on policy discussion and high-level priority-setting and on very preliminary revenue and expenditure projections in order to provide a clearer picture of available resources and expenditure obligations for the upcoming fiscal year. This report would serve as the platform for the Mayor and City Council's discussions of funding policies and priorities, or the "basis for programming" as referenced in Council Policy 000-20.

The release of the City Manager's Report would predate, by at least ten business days, the City Council meeting at which the City Manager's Report is presented to the Mayor and City Council and public input is solicited, allowing the public sufficient time to review and consider the content of the report prior to providing input to the Mayor and City Council. The discussion of budget priorities and objectives should also occur at the same City Council meeting at which the City Manager's Report is presented and public comment is received.

It would still be imperative to present the official City Manager's Financial Status and Forecast (Mid-Year) Report in the first quarter of the calendar year, when the City Manager would be in a position to provide more informed anticipated operational and capital expenditure requirements and revenue projections for the upcoming fiscal year. In addition to having sufficient data to provide better revenue estimates, such major funding obligations as pension fund contributions, negotiated

salary adjustments, new facility operational requirements, and various ordinance requirements such as the Library Ordinance could be reasonably estimated at that time. All estimates would, of course, be subject to adjustment as more information became available. This report would be in addition to the aforementioned City Manager's Report presented in November or December.

Finally, in order to ensure full representation of all City of San Diego residents in budget priority-setting, it is felt that any committee convened for the purpose of formulating Citywide goals and objectives, program priorities, and other budget policy guidelines should be comprised of the Mayor and the City Council in its entirety, as well as a representative of the City Manager's Office.

RECOMMENDATIONS

Based on the information provided in this analysis, in addition to the retention of the current Proposed Budget Process as described above, it is recommended that the Mayor and City Council consider the following amendments to Council Policy 000-20:

1. Amend Item #1 under "Schedule" to require the City Manager to provide a report to the Mayor and City Council no sooner than late November, but no later than the end of the calendar year. Amend the required contents of the report to include a discussion of current budgetary policies and priorities, a high-level forecast of revenue growth and expenditure requirements for the upcoming fiscal year, and recommendations for application of City resources.
2. Schedule the solicitation of public input and the Mayor and City Council's discussions of Citywide goals and objectives, program priorities, and other budget policy guidelines for the same meeting at which the City Manager's report is presented to the Mayor and City Council.
3. Remove the formation and convening of a Policy Committee as defined in Item #2 under "Schedule".
4. Amend Item #7 under "Schedule" to indicate that the City Manager is to present the Proposed Budget to the Mayor and City Council by the first Council Meeting in May, consistent with the City Charter.
5. Retain all activities and processes of the current Proposed Budget Process.

In Council Policy 000-20, "Schedule," item 2, the policy committee is to review public input, along with the Manager's "basis for programming," in early November, which is *prior to* the public hearing that is to take place in mid-November per item 3. This appears to be a logistical error that could be corrected via a Council Policy amendment as suggested in recommendation number two above.

Additionally, "Schedule," item 7, indicates that "The normal budget preparation and review process will ensue, with the City Manager submitting his proposed budget and six-year plan to Council at the first Council Meeting in March." However, per City Charter Article VII, § 69, "On or before

the first meeting in *May* [emphasis added] of each year the Manager shall prepare and submit to the Council a budget...for the ensuing fiscal year.” While these two directions are not necessarily contradictory in that Council Policy 000-20 merely exceeds but does not conflict with the City Charter requirement, the City Charter requirement is what the City Manager has historically adhered to and would more appropriately be considered the “normal budget process.” An amendment to clarify this section of Council Policy 000-20 is reflected in recommendation number four above.

If approved by the Mayor and City Council, any or all of the above recommendations would be memorialized through the amendment of Council Policy 000-20 (see draft proposed amended Council Policy 000-20, Attachment “D”). It should also be noted that Council Policy 000-20 may, in conjunction with all other Council Policies that relate to the responsibilities of the City Manager, require further revisions pursuant to the passage of the Strong Mayor Form of Governance Ordinance, which took place during the 2004 General Election. These amendments will be brought before the City Council well before the advent of the Fiscal Year 2007 Proposed Budget Process.

CONCLUSION

While there are several aspects to Council Policy 000-20 that have benefit to the City, the Policy calls for the recommendation of service enhancements or reductions by the City Manager at a point in the fiscal year when insufficient revenue or expenditure forecast data is available to provide sound revenue and expenditure projections for the ensuing fiscal year. The Council Policy would be more logical and beneficial were the recommended revisions to be enacted.

As indicated earlier in this report, budget discussions and public input for the Fiscal Year 2006 budget process are anticipated to occur at the City Council session of February 28, 2005, concurrent with the presentation of the Five-Year Financial Plan, with that plan and the Mid-Year Report serving as the bases for these discussions. The full implementation of Council Policy 000-20, in whatever form directed by the Mayor and City Council, would commence with the Fiscal Year 2007 budget process.

ALTERNATIVES

1. Direct the City Manager to implement selected amendments, either from the proffered changes or through alternate Mayor and City Council direction, to Council Policy 000-20.
2. Direct the City Manager to implement Council Policy 000-20 in its entirety, in its current state.
3. Rescind Council Policy 000-20 in its entirety and continue utilization of the Current Proposed Budget Process.

Respectfully submitted,

Mary Vattimo
Financial Management Director

Approved: Lisa Irvine
Deputy City Manager

Attachments: [Attachment "A" - Council Policy 000-20, CURRENT](#)
[Attachment "B" - Deputy Mayor Atkins' Memorandum](#)
[Attachment "C" - City Manager's Report to Rules Committee, Sept. 16, 1981](#)
[Attachment "D" - DRAFT Proposed Amended Council Policy 000-20](#)
[Attachment "E" – Budget Timetable - Comparison of Budget Processes](#)