LONG-TERM FISCAL SUSTAINABILITY

CITY OF IMPERIAL BEACH
CALIFORNIA

FINAL REPORT

MARCH 30, 2006

MAXIMUS, Inc. Sacramento, California

March 30, 2006

Mr. Gary R. Brown
City Manager
City of Imperial Beach
825 Imperial Beach Boulevard
Imperial Beach, CA 91932-2702

Re: Final Report

Dear Mr. Brown:

MAXIMUS, Inc. is pleased to present you with this final report of our review of the City's Long-Term Fiscal Sustainability. This report presents a summary of our findings, in bullet form, regarding the gap between the City's revenues and expenditures. Further, this report provides a brief review of associated items, such as the City's current Cost Allocation Plan (CAP). This final report incorporates the suggestions and concerns raised in the draft report.

We look forward to presenting our study to the City Council, and to assisting the City with its critical budgetary decisions. If we can be of any other service to you, please let us know.

Sincerely,

Brian A. Foster
Senior Manager

BACKGROUND

The City of Imperial Beach (City) contracted with MAXIMUS to conduct an independent review of the City's long-term fiscal stability. The purpose of this review was to determine whether the City needed to plan now for revenue and/or expenditure adjustments in future years, as the City is using approximately $0.6 million in one-time revenues to balance its current budget. Further, the City's revenue shortfall is expected to grow throughout most of the next decade, ultimately exceeding $1 million annually.

This growing shortfall is the result of cost increases outpacing revenue growth. While some of the City's major revenue rates are capped (e.g., property taxes), others are underperforming (e.g., sales tax), or of limited impact (e.g., transient occupancy tax). At the same time, the costs that the City incurs to maintain current service levels continues to grow at or above the regional inflationary rate. Most notably, personnel costs (including retirement and fringe benefits) are increasing faster than the consumer price index, as is the Sheriff's contract. The City of Imperial Beach is not alone in this dilemma, as many cities in California have, in recent years, addressed these matters.

In the first phase of this analysis, the City directed MAXIMUS to perform five tasks, as follows:

- Review and verify the City's current revenue projections.
- Identify any potential new revenues that the City may wish to collect, given full consideration of Proposition 218.
- Determine how well and completely the City is currently collecting the revenues it is already due to receive.
- Review the City's current Cost Allocation Plan (CAP) to determine whether a full revision is warranted.
- Review the City's current expenditure patterns and identify areas of possible reduction to balance the City's budget in future years, as needed.

Upon the conclusion of these tasks, MAXIMUS was to prepare a draft report in bullet form that highlights the findings of this review. This draft report presents those findings below.

STUDY METHODOLOGY

MAXIMUS met with the City Manager's staff, the Acting Finance Director, various members of the Administrative Services Department, the Community Development Department, and others, as needed to conduct this study. Among the primary documents reviewed were the City's current two-year budget, five years of revenue and expenditure reports, the two most recent Comprehensive Annual Financial Reports (CAFRs), and various redevelopment plans.

MAXIMUS focused on the budgetary data, and walked through the budget in line-item detail with the Acting Administrative Services Director. MAXIMUS then prepared worksheets of the City's financial data and compared that information to the City's budget projections. Those projections were adjusted for known or expected changes in the City's tax base, as primarily generated through redevelopment projects. The results of that review are presented in this report.

LIMITATIONS

Any long-range projection of revenues and expenditures is based on a series of assumptions regarding the state of the City and its myriad environmental influences. The further out those projections are made, the wider the scope of possibility for variance from those projections. Yet, a long-range projection has value when there are indicators that current course corrections could avert or shield against problems that are presently foreseeable.

In the City of Imperial Beach, there are additional limitations that add uncertainty to those projections. First, the City is in the process of recruiting its Administrative Services Manager. Until that process is complete, an interim Manager is in place and performing daily operations. Unfortunately, the prior incumbent was unavailable to assist with this project. Thus, the institutional memory of the City is limited.

Second, some of the supporting documents, such as future year budget models and detailed assumptions, are unavailable. They may exist with the City or on the City's computer servers, but they could not be located during the course of this study. This lack of information may be related to the current staff's unfamiliarity with where the prior Administrative Services Director maintained records and files.

Third, in prior years, the City maintained various reserves and/or funds for emergencies. In recent years, the City has used those funds and reserves in order to balance its budget. The City had use of those reserves only one time, and as each is exhausted, they are unavailable in the future to resolve the City's budget shortfalls. Last year (FY 2004-05), the City showed a new $3,738,100 fund balance reserve related to the City's loan to the Redevelopment Agency (RDA). The terms of the loan provide for the City to receive six percent interest on the $3,738,100 loan balance from the RDA, but the RDA is not expected to make payments on the principle balance next year. Thus, it is misleading to draw conclusions from a quick read of the figures appearing in the CAFR—they must be interpreted in context.

GUIDING PRINCIPLES

When reviewing the City's budget positions and policies, MAXIMUS relied upon commonly adopted budget and financial principles and guidelines—most of which are summarized and adopted by the Governmental Finance Officers Association (GFOA). Provided below is a summary of those primary principles and recommended practices. By undertaking this review, the City is acting responsibly to ensure that it is following as many of the suggested guidelines as practical.

APPROPRIATE LEVEL OF UNRESERVED FUND BALANCE IN THE GENERAL FUND

GFOA recommends that governments establish a formal policy on the level of unreserved fund balance that should be maintained in the general fund. GFOA also encourages the adoption of similar policies for other types of governmental funds. Such a guideline should be set by the appropriate policy body and should provide both a temporal framework and specific plans for increasing or decreasing the level of unreserved fund balance, if it is inconsistent with that policy.

The adequacy of unreserved fund balance in the general fund should be assessed based upon a government's own specific circumstances. Nevertheless, GFOA recommends, at a minimum, that general-purpose governments, regardless of size, maintain unreserved fund balance in their general fund of no less than five to 15 percent of regular general fund operating revenues, or of no less than one to two months of regular general fund operating expenditures. A government's particular situation may require levels of unreserved fund balance in the general fund significantly in excess of these recommended minimum levels. Furthermore, such measures should be applied within the context of long-term forecasting, thereby avoiding the risk of placing too much emphasis upon the level of unreserved fund balance in the general fund at any one time.

GFOA RECOMMENDED PRACTICES & NATIONAL ADVISORY COUNCIL ON STATE AND LOCAL BUDGETING (NACSLB) PRACTICES

The following principles derive from the GFOA's recommended practices, as coordinated with the National Advisory Council on State and Local Budgeting (NACSLB).

Element 4—Adopt Financial Policies: A government should develop a comprehensive set of financial policies. Financial policies should be consistent with broad government goals and should be the outcome of sound analysis. Policies also should be consistent with each other and relationships between policies should be identified. Financial policies should be an integral part of the development of service, capital, and financial plans and the budget. All other adopted budgetary practices of a government should be consistent with these policies.

Practice 4.1—Develop Policy on Stabilization Funds. A government should develop policies to guide the creation, maintenance, and use of resources for financial stabilization purposes.

Practice 4.2—Develop Policy on Fees and Charges. A government should adopt policies that identify the manner in which fees and charges are set and the extent to which they cover the cost of the service provided.

Practice 4.3—Develop Policy on Debt Issuance and Management. A government should adopt policies to guide the issuance and management of debt.

Practice 4.3a—Develop Policy on Debt Level and Capacity. A government should adopt a policy on the maximum amount of debt and debt service that should be outstanding at any one time.

Practice 4.4—Develop Policy on Use of One-Time Revenues. A government should adopt a policy limiting the use of one-time revenues for ongoing expenditures.

Practice 4.4a—Evaluate the Use of Unpredictable Revenues. A government should identify major revenue sources it considers unpredictable and define how these revenues may be used.

Practice 4.5—Develop Policy on Balancing the Operating Budget. A government should develop a policy that defines a balanced operating budget, encourages commitment to a balanced budget under normal circumstances, and provides for disclosure when a deviation from a balanced operating budget is planned or when it occurs.

Practice 4.6—Develop Policy on Revenue Diversification. A government should adopt a policy that encourages a diversity of revenue sources.

Practice 4.7—Develop Policy on Contingency Planning. A government should have a policy to guide the financial actions it will take in the event of emergencies, natural disasters, or other unexpected events.

Element 9—Develop and Evaluate Financial Options. A government should develop, update, and review long-range financial plans and projections. The information obtained from these plans and projections is used in determining the resource and expenditure options available for the budget period and the implications of those options. This element does not address decisions on a specific set of programs and services to be funded through the budget.

Practice 9.1—Conduct Long-Range Financial Planning. A government should have a financial planning process that assesses the long-term financial implications of current and proposed policies, programs, and assumptions and that develops appropriate strategies to achieve its goals.

Practice 9.2—Prepare Revenue Projections. A government should prepare multi-year projections of revenues and other resources.

Practice 9.2a—Analyze Major Revenues. A government should maintain an in-depth understanding of its major revenues.

Practice 9.2b—Evaluate the Effect of Changes to Revenue Source Rates and Bases. A government should evaluate and understand the effect of potential changes to revenue source rates and bases.

Practice 9.2c—Analyze Tax and Fee Exemptions. A government should periodically estimate the impacts and potential foregone revenue as a result of policies that exempt from payment, provide discounts and credits, or otherwise favor particular categories of taxpayers or service users.

Practice 9.2d—Achieve Consensus on a Revenue Forecast. A government should develop a process for achieving consensus on the forecast of revenues used to estimate available resources for a budget.

Practice 9.3—Document Revenue Sources in a Revenue Manual. A government should prepare and maintain a revenue manual that documents revenue sources and factors relevant to present and projected future levels of those revenues.

Practice 9.4—Prepare Expenditure Projections. Governments should prepare multi-year projections of expenditures for each fund and for existing and proposed new programs.

Practice 9.5—Evaluate Revenue and Expenditure Options. A government should evaluate revenue and expenditure options together, and consider the implications for other financial indicators prior to making specific choices with regard to the proposed budget.

Practice 9.6—Develop a Capital Improvement Plan. A government should develop a capital improvement plan that identifies its priorities and time frame for undertaking capital projects and provides a financing plan for those projects.

REVENUE & EXPENDITURE ANALYSIS

The City of Imperial Beach is fairly static in terms of its economic development, tax base, and financial support. The City is built out, and there is very little retail development activity taking place or planned, other than those stimulated by the Redevelopment Agency. The City wishes to maintain its character as more of a residential community nestled against the beach rather than a bustling business community.

As such, the revenue stream for the City of Imperial Beach is not very elastic to changes in the economy. With a shortage of retail sales and the relatively small tax base it provides, the City is not well insulated from the economic shocks that befall any city from time to time. When external, uncontrollable variables impact City finances, such as State takeaways in Vehicle License Fees (VLF), the City does not have many means to make up the difference, particular since the passage of Proposition 218, which essentially requires that all taxes and fees to go to a public vote for approval.

Yet, the citizenry of Imperial Beach desires the same level of service to which it has become accustomed over the years. Unfortunately, the City is not able to respond rapidly or easily to changes in community needs and financing mechanisms to support those needs.

Within this environment, the City is concerned that it is using one-time funds in order to balance its current operating budget. In fact, since FY 2003-04, the City has been operating a deficit in the General Fund (expenditures exceeded revenues). The City has operated a deficit by using its emergency reserves and other one-time funds. (The deficit figures are $302,468 in FY 2003-04, $376,021 in FY 2004-05, and $622,953 projected for FY 2005-06.) If the City continues to provide its current level of service while generating no new revenue streams, it is expected that the City will exhaust all of its reserves sometime before the end of FY 2008-09 (within the next three years).

Further, it is expected that the deficit would continue to grow over time. The tax and license revenue increases from the 9th & Palm development and the Seacoast Inn renovation will produce small bumps in future revenues, but those revenue increases will be insufficient to overcome the City's growing expenditure needs (holding service levels constant).

While the City has been using one-time revenue to balance its operating budget, it has in recent years incurred permanent revenue reductions that it must offset in all future years. First, the City is still adjusting to changes in Vehicle License Fee (VLF) funding (State takeaways). Second, in FY 2004-05, the City lost its share of the bridge revenues (approximately $166,000) when the toll to the Coronado bridge was eliminated. Even though these reductions occurred in prior years, the lost revenue needs to be made up in each succeeding year, and ultimately, not with one-time funds.

REVENUE & EXPENDITURE SCHEDULE

Table 1, below, presents the City's General Fund revenue and expenditure history, as reflected in the City's CAFR for the last ten years (FY 1994-95 to FY 2004-05). Further, this table presents financial projections from FY 2005-06 to FY 2015-16 for the City's General Fund. The figures beginning in FY 2005-06 have been adjusted from the City's revenue and expenditure detail reports to be consistent with prior year data appearing in the CAFRs (the internal charges and interfund transfers were adjusted out).

Table 1
Revenues & Expenditures
FY 1994-95 to FY 2015-16

Fiscal Year	Revenues	Expenditures & Net Transfers	Surplus/ (Deficit)	Undesig Balance
FY 94-95	$ 7,360,982	$ 6,557,104	$ 803,878	$2,314,210
FY 95-96	7,485,910	6,729,710	756,200	3,040,329
FY 96-97	7,654,944	7,192,875	462,069	3,403,049
FY 97-98	7,887,866	7,454,748	433,118	3,881,243
FY 98-99	8,340,760	8,793,897	(453,137)	2,701,923
FY 99-00	8,893,480	8,150,711	742,769	2,739,406
FY 00-01	10,181,983	8,344,541	1,837,442	3,650,000
FY 01-02	11,360,612	10,359,631	1,000,981	6,128,273
FY 02-03	11,046,641	10,446,713	599,928	7,309,956
FY 03-04	11,174,469	11,476,937	(302,468)	2,800,000
FY 04-05	12,432,112	12,808,133	(376,021)	2,473,167*
FY 05-06	**12,336,936**	**12,959,889**	**(622,953)**	**1,850,214**
FY 06-07	12,587,454	13,413,485	(826,032)	1,024,182
FY 07-08	13,056,280	13,950,025	(893,745)	130,437
FY 08-09	13,564,155	14,508,026	(943,871)	(813,434)
FY 09-10	14,382,631	15,160,887	(778,256)	(1,591,690)
FY 10-11	15,213,903	15,767,322	(553,419)	(2,145,110)
FY 11-12	15,817,405	16,555,689	(738,284)	(2,883,393)
FY 12-13	16,462,773	17,383,473	(920,700)	(3,804,093)
FY 13-14	17,133,006	18,078,812	(945,806)	(4,749,900)
FY 14-15	17,839,832	18,892,358	(1,052,526)	(5,802,426)
FY 15-16	18,583,165	19,836,976	(1,253,812)	(7,056,238)

*Note: In addition to the $2,473,167, the City has reserved $3,738,100 for the Redevelopment Agency loan.

Table 1 provides the following points of information:

- With the exception of FY 1998-99 and until FY 2003-04, the City has enjoyed budget surpluses of modest to significant size.

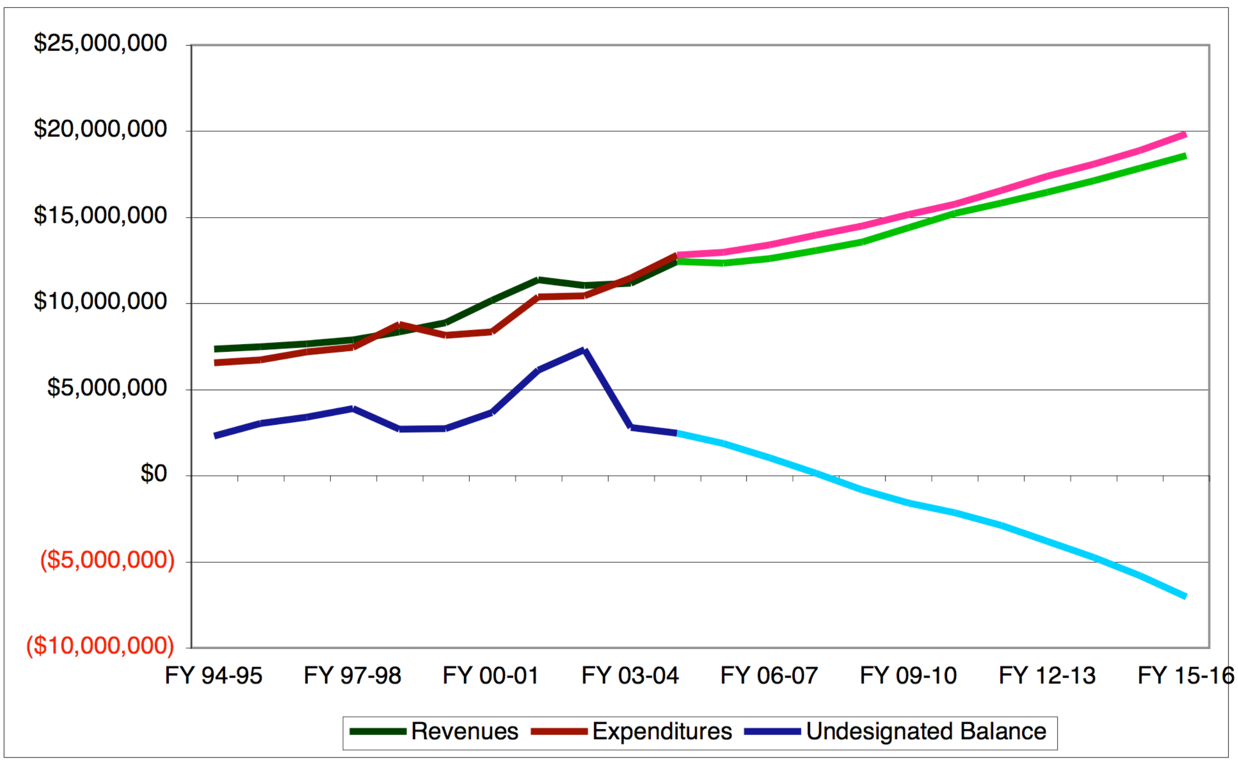
- In FY 2003-04, the City faced a $302, 468 General Fund deficit, which the City resolved with one-time funds.
- In FY 2004-05, the City's General Fund deficit was $376,021, which again was made whole with one-time funds.
- In the current fiscal year, FY 2005-06, the City's General Fund deficit is expected to exceed $600,000, even after the City undertook steps to increase revenues with user fees, storm water fees, and allowable Redevelopment Agency support.
- In the out years, the City is expected to incur significant General Fund deficits ranging from $500,000 to $1 million or more.
- The City's structural deficit has impacted the General Fund balance because revenues have not been increasing as quickly as expenditures. Most of the City's primary revenues, such as Property Tax, Sales Tax, and Transient Occupancy Tax have simply not kept up with inflation, much less the costs that have increased faster than inflation.
- The City's undesignated General Fund balance exceeded $7.3 million as recently as FY 2002-03. However, the current year undesignated General Fund balance is expected to be only $1.8 million—a precipitous decline in one-time funds.
- Sometime in FY 2008-09, the City's undesignated General Fund Balance is projected to be depleted, and absent expenditure reductions or revenue increases, the City would be at risk of fiscal insolvency.
- The City has an opportunity to act within the next two year to avoid fiscal crisis.
- It is projected that the 9th & Palm development will be completed and generating full tax and license revenue by FY 2009-2010. (Should this project be completed earlier, then the revenue increase will begin sooner; however, the revenue increase is insufficient to offset the City's growing costs of operation.) Also note that if this project does not succeed as planned, then revenues may not reach the levels targeted in current studies.
- Similarly, it is projected that the Seacoast Inn will be re-opened, fully operational, and generating tax and license revenue in FY 2010-11. (Should this project be completed earlier, then the revenue increase will begin sooner; however, the revenue increase is insufficient to offset the City's growing costs of operation.) Also, if patronage at the hotel and restaurant dose not materialize as planned, then revenues will need to be reduced from current estimates.
- The revenues incorporate assumptions for each major revenue item. For example, property taxes are expected to grow at slightly more than 2 percent per year, based on limitations imposed by Proposition 13. Transient Occupancy Tax revenues are fairly static, other than the adjustments for the Seacoast Inn (reduction during construction and increase once re-opened).

Other revenues are expected to rise and fall between about 3-5 percent per year, over time.

- The revenues do not include repayment of the loan from the Redevelopment Agency, as it is unclear when the Agency will be able to initiate repayments, and in what amounts.
- Similarly, the City's General Fund expenditures are expected to rise between 3-5 percent each year.
- For a detailed schedule of revenues and expenditures, see Attachments 1 and 2, respectively.

Figure 1, below, graphically depicts the relationship between the City's revenues, expenditures (and transfers), and undesignated fund balance over time.

Figure 1
Revenues, Expenditures & Fund Balance
FY 1994-95 to FY 2015-16



In Figure 1, above, the dark green line represents the City's revenues, as audited and appearing in the CAFR. The light green line indicates revenue projections. Similarly, the dark red line signifies audited expenditures, while the light red line shows expenditure projections. The dark blue line shows the size of the General Fund's Undesignated Fund Balance. The light blue line shows projections of the Undesignated Fund Balance.

These lines graphically depict the divergence of revenues and expenditures. The City's expenditures are outpacing revenues, and have done so since FY 2003-04. This funding gap is expected to continue for the foreseeable future, unless structural change is implemented.

It should be noted that the sales tax, transient occupancy tax, and business license tax for the Redevelopment Agency's to major projects are already incorporated into the revenue figures shown in Figure 1, above. Those two projects are the Seacoast Inn and 9th and Palm Street developments. While all revenue helps to support the City, their incremental additions do not make much of a noticeable change in the revenue line.

In short, in order for the City to balance its budget, it will need to undertake significant modifications to its expenditure patterns, revenue generation, or both. The City cannot develop its way out of this financial situation, absent the instant creation of thriving auto malls and big box stores.

FUND BALANCE POLICY

As noted above, the GFOA recommends that *at a minimum, [cities], regardless of size, maintain unreserved fund balance in their general fund of no less than five to 15 percent of regular general fund operating revenues, or of no less than one to two months of regular general fund operating expenditures*. This policy works well for most jurisdictions, but special consideration should be given to both size and local conditions.

In general, the smaller the city's size, the more difficult it is to adjust to fiscal challenges. Simply put, there are fewer opportunities or methods for small governments to adjust to fiscal challenges, such as the State's Vehicle License Fee (VLF) takeaways in recent years. Further, cities in California are limited in their ability to raise revenue, and to do so in a timely matter (due in large part to Proposition 218). Thus, the 15 percent recommended figure should be considered as a minimum for most small California cities, including Imperial Beach.

It is illustrative to review Imperial Beach's General Fund balance history against this recommended minimum level. Table 2, below, provides that comparison for Imperial Beach.

Table 2
General Fund Undesignated Fund Balance Review
FY 1994-95 to FY 2015-16

Fiscal Year	GFOA Recommend	City's Fund Balance	Difference
FY 94-95	1,104,147	2,314,210	1,210,063
FY 95-96	1,122,887	3,040,329	1,917,443
FY 96-97	1,148,242	3,403,049	2,254,807
FY 97-98	1,183,180	3,881,243	2,698,063
FY 98-99	1,251,114	2,701,923	1,450,809

FY 99-00	1,334,022	2,739,406	1,405,384
FY 00-01	1,527,297	3,650,000	2,122,703
FY 01-02	1,704,092	6,128,273	4,424,181
FY 02-03	1,656,996	7,309,956	5,652,960
FY 03-04	1,676,170	2,800,000	1,123,830
FY 04-05	1,864,817	2,473,167	608,350
FY 05-06	**1,850,540**	**1,850,214**	**(326)**
FY 06-07	1,888,118	1,024,182	(863,936)
FY 07-08	1,958,442	130,437	(1,828,005)
FY 08-09	2,034,623	(813,434)	(2,848,057)
FY 09-10	2,157,395	(1,591,690)	(3,749,085)
FY 10-11	2,282,085	(2,145,110)	(4,427,195)
FY 11-12	2,372,611	(2,883,393)	(5,256,004)
FY 12-13	2,469,416	(3,804,093)	(6,273,509)
FY 13-14	2,569,951	(4,749,900)	(7,319,850)
FY 14-15	2,675,975	(5,802,426)	(8,478,401)
FY 15-16	2,787,475	(7,056,238)	(9,843,712)

Table 2 shows that the City has a long history of maintaining a strong General Fund balance, and has maintained the amount in excess of the level recommended by the GFOA. This year, however, after a couple of years of declining balances, the City is experiencing less than the minimum recommended amount.

To some extent, the decline in the General Fund balance was accelerated due to the City's loan to the Redevelopment Agency and contributions to capital improvement projects. However, the City has also in recent years funded ongoing operations with its fund balance. Because of this structural deficit, the City is expected to slip further behind the recommended fund balance level in future years, absent increases in revenue or decreases in expenditure.

It is critical at this juncture that the City take steps to resolve the deepening fiscal problem. The City's leadership recognizes the importance of resolving this matter, and understands the lead time necessary to affect changes in either local revenues and expenditures.

EXPENDITURE COMPOSITION

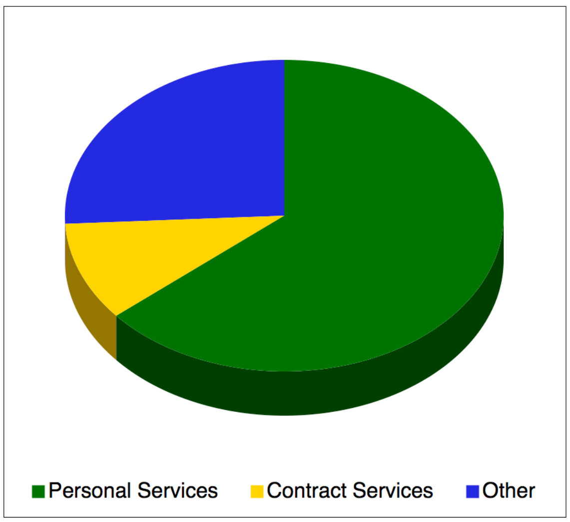
The City has compiled a series of options that may be employed to adjust the City's expenditures in future years. The City of Imperial Beach, like most cities in California, have experienced a series of fiscal challenges in recent years. As a result of that experience, cities have already reduced in many cases their service levels to minimal operations. For the most part, the City of Imperial Beach has done the same.

The scale of the City's operations is relatively small. Departments comprising only a few staff members are challenged to find means of cutting expenditures. In Imperial Beach, significant operations such as public safety are already contracted out, so there are fewer opportunities to develop synergies or economies of scale—the City has already exploited those.

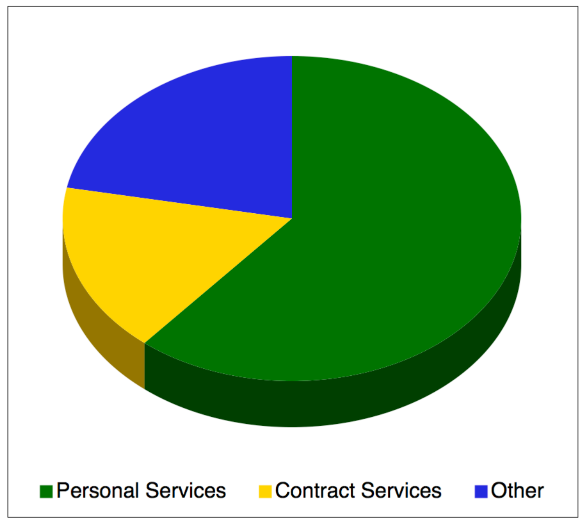
The City is now at a point where there are few easy options for reductions. Almost any significant reduction would impact salaried positions or completely eliminate functions. There simply are not many easy reduction targets left in the City's budget.

In order to understand where and how the City expends its General Fund dollars, the following series of pie charts indicates the funds spent on Personal Services (staff salaries and fringe benefits), Contract Services (such as Sheriff and Animal Control), and all other costs.

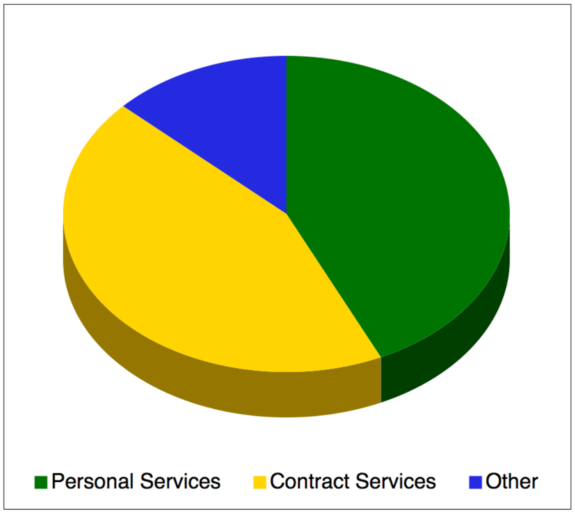
Legislative Department



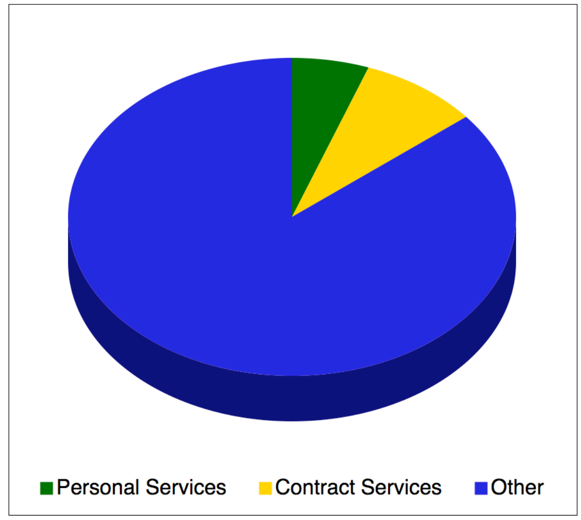
Executive Department



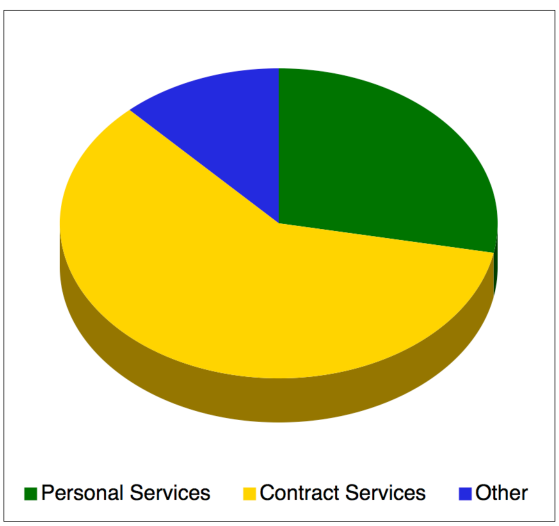
Administrative Department



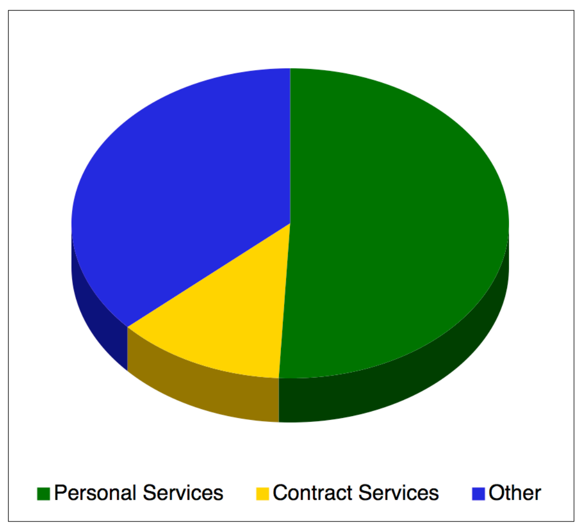
Miscellaneous Department



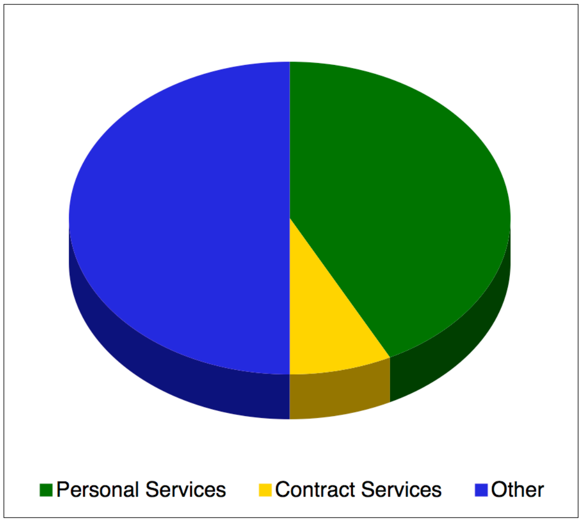
Public Safety Department



Public Works Department



Parks & Recreation Department



The pie charts above graphically depict that a majority of the City's General Fund dollars are spent on salaries and contracted services. There are very few options for the City to identify spending cuts that would not impact staff positions or contracted service levels. The only exceptions are in the Miscellaneous Department, but those "Other" expenditures are for a number of fixed, Citywide items. Public Works and Parks and Recreation also have significant "Other" expenditures. Those expenditures can be traced to materials costs, certain utility costs, internal service charges, etc.

While there may be opportunities to reduce expenditure levels in certain areas, often with measurable reductions in service levels, the City also has the option of considering new or increased revenue sources to address its Fund Balance problems. Revenue options are discussed in the next section of this report.

REVENUE OPTION ANALYSIS

The growing size of the fund balance gap identified above indicates that the City will need to undertake a significant policy change to resolve its structural deficit. Those changes could be made to expenditures, revenues, or a combination of the two. City staff are preparing a listing of expenditure options for consideration. In addition to those expenditure changes, the City could consider implementing the following changes to revenues:

- Implementing a Parcel Tax
- Shifting legitimate costs to the existing Landscape and Lighting Assessment District and increasing the amount of the assessment
- Implementing a Utility Users Tax
- Increasing Business License Taxes
- Increasing Franchise Fees
- Increasing User Fees

While increasing revenues is not always a popular proposition, some alternatives are better than others in a given situation. Each of the options above has it benefits and drawbacks, as shown in Table 3, below.

Table 3
Revenues Option Matrix

Item	Type of Vote	Time to Implement	Revenue Impact
Parcel Tax	Property Owners	Long-Term	High
LLAD	Property Owners	Long-Term	High
Utility Users Tax	Public	Long-Term	High
Business License Tax	Public	Long-Term	Medium
Franchise Fees	Council	Based on Contract	Medium
User Fees	Council	Short-Term	Small

Table 3 shows that of the options, all would require a vote under Proposition 218, although only a Council vote would be required on the last two options. Unfortunately, those two options provide the smallest change in revenues. Also, since User Fees were increased as recently as FY 2004-05, the potential revenue increase is small, and any additional increases might discourage the use of the service for which the fee is charged. (Disclaimer: MAXIMUS is an industry leader in the conduct of User Fee Studies.)

REVENUE COLLECTION EFFICIENCY

Another possible source of revenue is full enforcement of revenue collection efforts for those revenues that the City already has authority to claim. The City does use the services of an outside firm, Hinderliter de Llamas and Associates (HDL), to monitor its Sales Tax receipts; therefore, it is highly likely that the City is retaining all of the Sales Tax revenues to which it is due.

For other revenues, the City takes a rather passive role. The Administrative Services Department collects all revenue reported by taxpayers and ratepayers, but the City does not have an enforcement or audit mechanism to ensure that all tax and ratepayers are paying their fare share. The City's Code Enforcement Officer does check for valid Business License Certificates when reviewing business operations, but this effort does not constitute a concentrated effort to identify unlicensed operations.

There is a trade-off between expending time and resources to increase revenue collections through enforcement efforts, and it is not clear whether it would make sense to do so now. Yet, even a minimal audit effort typically returns revenues in amounts covering the expenses incurred.

For example, the City could conduct a targeted study of Business License taxpayers by performing field checks of businesses. In this scenario, staff would print out reports of current, licensed businesses and compare those lists in the field to existing storefronts. All added business would increase not only current revenue streams, but future ones as well.

While any compliance effort on the City's part increases revenues and promotes equity among tax and fee payers, it is not expected that increased enforcement is likely to yield significant revenue increases that would be necessary to materially improve the City's fund balance position. Thus, any revenue improvements that the City might enjoy from increased enforcement should be considered supplemental, not a major impact on the City's structural deficit.

COST ALLOCATION PLAN REVIEW

The City's Cost Allocation Plan (CAP) is maintained on a spreadsheet based on fiscal data from FY 2001-02. (Actually, the model is an adjustment from a model developed in FY 1999-00.) A cursory review of this model yields the following comments.

- The model is quite aggressive in its approach to allocating costs, and warrants further review to determine compliance with OMB Circular A-87.
- The original model is now six years old. During that time, there have been internal organizational changes that may merit the model outdated.
- The basis for allocation of costs is not always clear, as the bases are not always labeled.
- The model uses a complex matrix to spread costs among departments and across funds. Operationally, it is not clear whether the charges match the designed amounts.
- It is not known whether capital costs are fully reflected in the cost recovery model.

Given the questions and concerns noted above, the City might consider creating a new Cost Allocation Plan to fully, fairly, and appropriately spread administrative costs to other operations, especially to funds other than the General Fund. (Disclaimer: MAXIMUS is a national leader in the conduct of Cost Allocation Plans.)

CONCLUSION

The City of Imperial Beach faces the difficult tasks that many California cities have been facing in recent years: how to maintain fiscal stability. It is clear that the City is using one-time funds to maintain operations at their current level, and it is just as clear that the City cannot employ that model indefinitely. Based on current revenue and expenditure patterns, the City will face a fiscal crisis in FY 2008-09, where expenditures will exceed revenues, and there will be an insufficient General Fund balance to make up the difference.

The City has two options to thwart this growing fiscal crisis: decrease expenditures and/or raise additional revenue. Neither of these options is necessarily pleasant, yet the City is required to address this matter if it chooses to remain fiscally solvent. It must also be stated that the magnitude of the growing fiscal problems is not small. The City will need to implement significant expenditure reductions and/or revenue increases—the growing structural deficit cannot be fixed by "small tweaks."

It is also important to note that the longer the City delays in addressing this matter, the more severe the changes will need to be to make up for the structural gap. Course corrections made now will bring the revenue and expenditure lines closer together so that the gap does not continue to grow apart.

What is important is that the City recognizes its financial position now and is prepared to position the City for future fiscal stability. In order to achieve that stability, the City needs to act now with a plan to resolve the structural deficit. Given the long lead-time necessary to enact revenue measures, particularly those that require voter approval, and/or the difficult and sometimes lengthy debate associated with reduced service levels to the citizenry, the City needs to put in place now its plan for the future. The City is to be commended for facing these difficult choices at this critical juncture, before the City finds itself in a state of fiscal crisis.

MAXIMUS appreciates the opportunity to help the City of Imperial Beach with its budgetary analysis. The City's leadership has shown us its commitment to addressing its fiscal matters in a responsible and timely manner.

ATTACHMENT 1
GENERAL FUND
REVENUE SCHEDULE

Fiscal Year	Property Tax	Sales Tax	TOT	Franchise Tax	Other Taxes	Business License	Other Licenses	VLF	*continued*
FY 00-01	1,763,369	668,400	224,311	553,153	151,433	275,478	175,593	1,512,256	
FY 01-02	1,902,071	701,337	215,589	784,680	54,854	277,797	174,259	1,505,002	
FY 02-03	1,843,311	760,968	272,925	761,211	78,788	264,883	177,339	1,604,856	
FY 03-04	1,912,851	814,591	233,919	800,797	103,663	259,840	214,573	1,264,954	
FY 04-05	3,561,005	727,792	279,826	836,367	273,198	252,976	253,237	648,004	
FY 05-06	3,635,786	749,626	280,106	869,822	108,359	260,565	263,366	232,900	
FY 06-07	3,712,138	779,611	280,386	904,615	111,610	268,382	273,901	244,545	
FY 07-08	3,790,093	810,795	280,666	940,799	114,958	276,434	282,118	256,772	
FY 08-09	3,869,684	835,119	280,947	987,839	118,407	284,727	290,582	269,611	
FY 09-10	3,950,948	1,201,524	196,663	1,037,231	121,959	298,963	299,299	283,091	
FY 10-11	4,033,918	1,256,285	402,630	1,089,093	125,618	310,922	308,278	297,246	
FY 11-12	4,118,630	1,306,536	410,682	1,143,547	129,386	320,249	317,526	312,108	
FY 12-13	4,205,121	1,371,863	418,896	1,189,289	133,268	329,857	327,052	327,714	
FY 13-14	4,293,429	1,426,738	427,274	1,236,861	137,266	339,752	336,864	344,099	
FY 14-15	4,383,591	1,483,807	435,819	1,286,335	141,384	349,945	346,970	361,304	
FY 15-16	4,475,646	1,543,159	444,536	1,337,789	145,625	360,443	357,379	379,370	

Fiscal Year	Other Intergov	Charges for Service	Fines	Use of Money	Misc	Fund Transfers	Other	CAFR Adjustment	Total
FY 00-01	442,998	2,024,845	165,350	501,664	446,335	701,797	2,100,152	(1,525,152)	10,181,982
FY 01-02	305,062	2,598,262	260,402	517,673	294,823	1,951,800	822,051	(1,040,862)	11,324,800
FY 02-03	233,837	2,920,954	257,478	349,945	590,765	1,981,719	871,828	(1,924,166)	11,046,641
FY 03-04	399,094	2,902,130	333,032	365,250	525,243	2,196,602	864,004	(2,016,074)	11,174,469
FY 04-05	184,490	3,337,482	372,655	322,700	220,881	2,367,403	980,800	(2,186,704)	12,432,112
FY 05-06	191,870	3,537,731	398,741	306,565	234,134	2,509,447	1,010,224	(2,252,305)	12,336,936
FY 06-07	199,544	3,749,995	418,678	291,237	248,182	2,383,975	1,040,531	(2,319,874)	12,587,454
FY 07-08	207,526	3,974,994	439,612	232,989	263,073	2,503,174	1,071,747	(2,389,471)	13,056,280
FY 08-09	215,827	4,213,494	461,592	186,392	278,857	2,628,332	1,103,899	(2,461,155)	13,564,155
FY 09-10	224,460	4,466,304	484,672	149,113	295,589	2,759,749	1,148,055	(2,534,989)	14,382,631
FY 10-11	233,439	4,734,282	508,906	119,291	313,324	2,897,736	1,193,977	(2,611,039)	15,213,903
FY 11-12	242,776	4,970,996	534,351	83,503	332,123	3,042,623	1,241,736	(2,689,370)	15,817,405
FY 12-13	252,487	5,219,546	561,068	58,452	352,051	3,194,754	1,291,406	(2,770,051)	16,462,773
FY 13-14	262,587	5,480,523	589,122	40,917	373,174	3,354,492	1,343,062	(2,853,153)	17,133,006
FY 14-15	273,090	5,754,549	618,578	28,642	395,564	3,522,217	1,396,784	(2,938,747)	17,839,832
FY 15-16	284,014	6,042,277	649,507	20,049	419,298	3,698,327	1,452,656	(3,026,910)	18,583,165

ATTACHMENT 2
GENERAL FUND
EXPENDITURE SCHEDULE

Fiscal Year	Legislative[1]	Executive[2]	Admin[3]	Misc Dept[4]	Public Safety[5]	Public Works[6]	Parks & Recreation[7]	CAFR Adjustment	Total
FY 00-01	260,969	379,846	924,717	1,407,502	5,083,724	829,090	983,845	(872,551)	8,997,142
FY 01-02	277,488	462,100	1,030,821	822,365	6,079,270	1,416,785	1,275,852	(1,314,215)	10,050,466
FY 02-03	352,873	343,615	1,012,485	1,114,708	6,780,598	1,503,836	1,263,437	(1,868,162)	10,503,390
FY 03-04	301,052	488,837	1,279,944	2,077,776	7,562,357	1,519,641	1,190,814	(2,943,484)	11,476,937
FY 04-05	323,277	488,519	1,092,175	1,721,521	8,522,688	1,504,168	1,342,487	(2,533,403)	12,461,432
FY 05-06	336,208	508,060	1,135,862	1,790,382	8,863,596	1,564,335	1,396,186	(2,634,739)	12,959,889
FY 06-07	347,975	525,842	1,175,617	1,853,045	9,173,821	1,619,086	1,445,053	(2,726,955)	13,413,485
FY 07-08	361,894	546,876	1,222,642	1,927,167	9,540,774	1,683,850	1,502,855	(2,836,033)	13,950,025
FY 08-09	376,370	568,751	1,271,548	2,004,254	9,922,405	1,751,204	1,562,969	(2,949,475)	14,508,026
FY 09-10	393,307	594,344	1,328,767	2,094,445	10,368,913	1,830,008	1,633,303	(3,082,201)	15,160,887
FY 10-11	409,039	618,118	1,381,918	2,178,223	10,783,670	1,903,208	1,698,635	(3,205,489)	15,767,322
FY 11-12	429,491	649,024	1,451,014	2,287,134	11,322,853	1,998,369	1,783,567	(3,365,763)	16,555,689
FY 12-13	450,966	681,475	1,523,564	2,401,491	11,888,996	2,098,287	1,872,745	(3,534,052)	17,383,473
FY 13-14	469,004	708,734	1,584,507	2,497,550	12,364,556	2,182,219	1,947,655	(3,675,414)	18,078,812
FY 14-15	490,109	740,627	1,655,810	2,609,940	12,920,961	2,280,419	2,035,299	(3,840,807)	18,892,358
FY 15-16	514,615	777,659	1,738,600	2,740,437	13,567,009	2,394,440	2,137,064	(4,032,848)	19,836,976

[1]Includes: Mayor/City Council, and City Clerk

[2]Includes: City Manager, Economic Development, and Personnel

[3]Includes: Administrative Services, City Attorney, and Community Development

[4]Includes: Facilities Maintenance and Non-Departmental

[5]Includes: Law Enforcement Contract, Fire Protection, Ocean/Beach Safety, Building and Housing Inspection, Animal Control, Disaster Preparedness, Code Enforcement, and AVA

[6]Includes: Street Maintenance, Administration, Graffiti Removal, Solid Waste Management, and Storm Water

[7]Includes: Recreation, Park Maintenance, Senior Services, and Tidelands Maintenance