

**CITY OF NEWPORT BEACH
FINANCE COMMITTEE
MAY 21, 2020 MEETING MINUTES**

I. CALL MEETING TO ORDER

The meeting was called to order at 3:02 p.m. via teleconference.

II. ROLL CALL

PRESENT: Mayor Pro Tem/Chair Will O'Neill, Council Member Joy Brenner, Council Member Diane Dixon (attending remotely), Committee Member William Collopy, Committee Member John Reed, Committee Member Joe Stapleton, Committee Member Larry Tucker (attending remotely)

STAFF PRESENT: City Manager Grace K. Leung, Finance Director/Treasurer Dan Matusiewicz, Deputy Director/Finance Steve Montano, Senior Accountant Theresa Schweitzer, Budget Analyst Amy Lewis, Budget and Acting Budget Manager Shannon Espinoza, Administrative Specialist for Finance Director Caitlin McCourt

MEMBERS OF THE PUBLIC: Jim Mosher

III. PUBLIC COMMENTS

None

IV. CONSENT CALENDAR

MINUTES OF MAY 14, 2020
Recommended Action:
Approve and file.

MOTION: Committee Member Reed moved to approve the minutes, Committee Member Collopy seconded. The motion carried unanimously by acclamation.

V. CURRENT BUSINESS

A. INTERNAL AUDIT PROGRAM UPDATE

Summary:
Update on audit work performed to date by Moss Adams LLP (Moss Adams) that was retained to assess internal control risks, conduct performance audits and management consulting services.

Recommended Action:
Review the City Manager's proposed budget and give recommendations to the City Manager in advance of the budget's presentation to the City Council.

Deputy Director/Finance Steve Montano reported the City's Internal Control Auditor, Moss Adams recently completed its first draft of the Enterprise Risk Assessment which assessed the City's operating environment from a risk and performance perspective to develop the Internal Audit Plan. He advised that City Manager Grace Leung and staff would be meeting with Moss Adams to discuss the findings and determine next steps. He also reported Moss Adams is

reviewing the City's internal controls to identify opportunities for strengthening and will help form the City's long-term Audit Plan.

Deputy Director/Finance Montano advised this phase of the project began in May with expected completion of both the Risk Assessment and the Internal Controls review by the end of June. He advised that at once completed the Internal Audit Plan will be formulated and will guide the City's audit activities moving forward. He reported the project is on time and within budget and will continue to provide updates as work progresses.

City Manager Leung reported the first draft was delivered a month ago but was slowed by the COVID-19 response. She hopes to use Moss Adams to review the City's operating efficiencies and activities as the City moves into the next phase of the budgeting process.

In response to Committee Member Collopy's inquiry, Deputy Director/Finance Montano clarified the Enterprise Risk Assessment and Enterprise Internal Controls Assessment will be completed in June at which time work will begin to develop the Internal Audit Plan at the end of June.

In response to Committee Member Collopy's inquiry, Deputy Director/Finance Montano and City Manager Leung advised Moss Adams is setting up the framework of the actual Work Plan of the audit which will be ongoing and the size of the audit will vary.

In response to Committee Member Larry Tucker's inquiry, Director/Treasurer Dan Matusiewicz advised the Enterprise Risk Assessment was mostly high-level interviews with department heads and the subsequent phase consisted of high-level assessment on the internal controls. He hopes to receive a road map in June from Moss Adams that identifies the most vulnerable areas for review.

City Manager Leung reported Moss Adams is looking broadly at External Risk, Organizational Structure and Staffing, Risk Programs, Capital Resources, and Leadership to complete their assessment of the organization. Committee Member Tucker requested to see a more granular Internal Controls Plan once completed. He expressed his support for the assessment of the organizational structure.

Chair O'Neill opened public comments.

Jim Mosher inquired if the Moss Adams report would be made public at the June 11th meeting. City Manager Leung responded she hopes to deliver the document by June or shortly thereafter but could not promise a specific date.

Chair O'Neill closed public comments.

There was no further action taken on this item.

B. PROPOSED FY2020-21 BUDGET OVERVIEW

Summary:

Staff will provide an overview of the Proposed FY 2020-21 Operating Budget.

Recommended Action:

Receive and file.

Director/Treasurer Matusiewicz reported that COVID-19 dealt a significant blow to the global economy and the City is in the initial phases of administering financial first aid. He acknowledged the City was in a better financial position than other cities but stressed there is much work to be done if the pandemic persists beyond the next fiscal year.

Director/Treasurer Matusiewicz presented the Fiscal First Aid Roadmap which was developed by the Government Finance Officers Association (GFOA) after the last recession and reported the City is in the Bridging Stage where short-term generic solutions are used. He advised starting July 1, the City will need to look at long-term solutions for the COVID-19 Recovery stage.

Director/Treasurer Matusiewicz reported the City is still relying on strong Property Tax growth in this current year and continues to focus on the City's Quality of Life and Infrastructure. He reported the City is aggressively pursuing paying down its Unfunded Liability which represents a significant risk to the City's financial health. He provided a review of the budget in its totality including new Capital Improvement Plan (CIP).

Director/Treasurer Matusiewicz presented on the overall Revenue and reported the City is still looking at a 4.2% increase in Property Tax revenue and a 20% decrease in Sales Tax revenue. In response to Committee Member Collopy, Director/Treasurer Matusiewicz explained the budget was down \$1 million for FY 19/20 Property Tax and the City was accounting for potential additional Property Tax delinquencies but acknowledged that has not happened at this time. He advised there was a slowdown in the 7th installment of Property Taxes but hopes to make up the difference on the 8th installment. Senior Accountant Theresa Schweitzer confirmed the 8th installment is July 14th, 2020.

Director/Treasurer Matusiewicz reported Transient Occupancy Tax (TOT) shows an overall 63% decrease over the next four (4) quarters and confirmed future projections is an educated guess based on conversations with hoteliers.

Chair O'Neill clarified due the variances the TOT is down almost 75% which is significant and the same is true for Sales Tax which is down \$7 million. Chair O'Neill requested City Council be presented the variance numbers as compared to the original FY 19/20 Budget or the Actual FY 19/20 Budget as it shows the more severe drop. Committee Member Collopy suggested the variances be shown by Quarter.

Director/Treasurer Matusiewicz stated General Fund revenues were projected to be \$242 million but is now projected to be \$199 million. He reported a \$5 million transfer to the Capital Program and various transfers in and out of the General Fund left an approximately \$33 million shortfall but various short-term remedies have been used to close that gap.

Director/Treasurer Matusiewicz reported the budget includes built-in Internal Service Charges to set aside monies for future use. He reported it was initially thought \$10 million would need to be taken from Contingency Reserves but was lowered to \$2.3 million which includes the additional \$5 million payment to CalPERS. He reported the City is proposing to use \$2.3 million of the Contingency Reserve and there is another \$50 million available to bridge the gap or buy the City time if the pandemic continues into the future.

In response to Chair O'Neill's inquiry, Director/Treasurer Matusiewicz explained the \$52.4 million is 25% of the Operating Budget less the Discretionary Payments Fund and clarified how the \$52.4 million was calculated for Committee Member Tucker.

In response to Chair O'Neill's inquiry, Director/Treasurer Matusiewicz clarified the Contingency Reserved is based on the General Fund Operating Budget. Acting Budget Manager Shannon Espinoza clarified FY 20/21 General Fund Expenditures by Department is \$219.8 million. Chair O'Neill clarified the proposed General Fund Revenue is \$199.5 million but the proposed General Fund Expenditures is \$219.8 million but does not include transfers out to other Master Plans and requested clarification.

In response to Chair O'Neill's inquiry, Director/Treasurer Matusiewicz explained the \$20 million gap. He explained the proposed General Fund Revenue is \$199.5 million and if all of the

transfers and Internal Service Fund were included, General Fund Expenditures would be \$240 million. He reported the transfers have been reduced as well as some savings plans and in some cases money has been transferred back to the General Fund. Chair O'Neill noted he needs to be able to explain the \$20 million gap.

Director/Treasurer Matusiewicz reported on solutions for bridging the \$20 million gap which would include \$2.9 million netted from operating cuts in Tier 1, \$2 million in hiring freezes from Tier 2, and a \$21 million reduction in deferred Capital spending from Tier 3 which is almost \$25 million.

In response to Chair O'Neill's inquiry, Acting Budget Manager Espinoza clarified the \$219 million in General Fund Expenditures includes Tier 1, Tier 2 and Tier 3 already being reduced. She clarified the transfer's in and out on Page 45 of the Proposed Budget is included in the tiers Director/Treasurer Matusiewicz referenced to bridge the gap.

In response to Chair O'Neill's inquiry, Director/Treasurer Matusiewicz clarified \$5 million of funding to the General Fund Capital Projects Program was included and any transfers to the Master Plans are not included for the Operating Expenditures. Director/Treasurer Matusiewicz further clarified if Tier 1 through Tier 4 were combined and \$2.3 million was used from Tier 5, it would total \$32.3 million.

In response to Chair O'Neill's inquiry, Director/Treasurer Matusiewicz clarified the Operating Expenditures are deceiving because they do not include the traditional transfers to the Master Plans necessitating the \$33 million. Director/Treasurer Matusiewicz commented he would be working on developing a better plan.

Chair O'Neill explained when trying to bridge the gap between budgets the summary of all funds must be taken into account. Director/Treasurer Matusiewicz explained the confusion may be the transfers in and out as they show a net. He further explained the difference between Revenues and Operating Revenue is \$20 million and if the transfers to the other funds are included, it is an additional \$20 million.

Committee Member Tucker explained paying Operating Expenses is not optional. He explained the report is using margin for things that would normally be funded by the General Fund. Director/Treasurer Matusiewicz responded these are short-term savings and not long-term remedies. Committee Member Tucker hoped to better understand what the City's long-term sustainable numbers would be in the next couple of months.

Chair O'Neill commented the report shows FY 18/19 Revenues as \$229.8 million and the General Expenditures and \$208 million but knows there was not a \$21 million surplus for that year. Acting Budget Manager Espinoza clarified the \$229.8 million represents all funds and the \$208 million represents General Fund Only Expenditures. Committee Member Tucker agrees there is additional General Fund monies that were spent but are not in the report.

Budget Analyst Amy Lewis clarified Page 37 does not include the transfers, but Page 40 reflects like-for-like General Fund Revenue at \$214 million. Chair O'Neill commented the report needs a better break down which explains how the gap is broken down in detail. He advised this is the first time he has ever seen a Proposed General Fund Expenditure that is higher than the General Fund Revenue. Director/Treasurer Matusiewicz explained the target differential is \$30 million.

City Manager Leung explained FY 19/20 Actual General Fund Revenues were \$230 million and the proposed General Fund Revenue for FY 20/21 is \$200 million which leaves a \$30 million loss and the Operating Budget is only being cut by \$5 million. She explained it is being shored up by transfers until there is a full understanding of the financial impact.

Council Member Dixon suggested presenting two (2) different schedules; one that includes the transfers and one that does not. Chair O'Neill requested the Proposed Budget be made less difficult to interpret for the City Council and the public. Director/Treasurer Matusiewicz explained there are many moving parts with this Proposed Budget and will work to develop a better interpretation.

Director/Treasurer Matusiewicz presented the proposed Capital Project that would continue and be placed on hold until FY 21/22. In response to Committee Member Collopy's inquiry, Director/Treasurer Matusiewicz confirmed City Council has already reviewed the list of proposed CIPs. He explained the Proposed Budget includes transfers of \$1 million to the Facilities Maintenance Plan (FMP), zero allocation to the Facilities Financial Plan (FFP), \$5 million to Capital Improvement Program (CIP), and advised these transfers are not reflected as an operating expenditure.

Director/Treasurer Matusiewicz reported on Savings Reductions and noted Internal Service Charges are reflected in the Operating Budget. He reported \$5 million of the Savings Reduction would be returned to the General Fund. Lastly, he reported the Proposed Budget reflects \$50 million in Contingency Reserves which is within \$2.3 million of its target.

Director/Treasurer Matusiewicz reported on Department Expenditures has increased mainly due to the Flores vs. City of San Gabriel case which increased overtime. He reported an increase of one (1) Police Officer position is also reflected and happened in FY 19/20.

In response to Committee Member Collopy's inquiry, Director/Treasurer Matusiewicz reported the Police Department staffing level fluctuates every fiscal year. Acting Budget Manager Espinoza clarified there were many vacancies in FY 19/20 but the Police Department is now almost fully staffed.

In response to Committee Member Collopy inquiry, Acting Budget Manager Espinoza was unable to determine if there were 231 or 232 staffed positions in the Police Department and advised she will follow up with Human Resources. He suggested staffing below 100% given the current situation. Chair O'Neill clarified the Police Department is usually staffed at 100% but all vacancies are not always filled. Director/Treasurer Matusiewicz reported \$2 million in salary savings was included in the Proposed Budget.

City Manager Leung advised departments were beginning to prepare budgets when COVID-19 struck which resulted in a hard stop of the budget process in order to begin the enhancement process. She reviewed the required items in the Proposed Budget which includes adjustments for overtime pay due to the verdict in the Flores vs. City of San Gabriel case and Paramedic School for the Fire Department. She also explained there are some necessary positions that are part-time or funded through specialized funds and are required due to the nature of the work. Lastly, she reported a new 10-year Street Sweeping contract was included in the budget.

Director/Treasurer Matusiewicz reported there is still a robust Capital Improvement Program (CIP) in the proposed budget and recapped several projects included the construction of Fire Station 2 and Grant Howald Park. He advised Fire Station 2 will be financed to give the City much needed breathing room. Chair O'Neill reported City Council approved the concept of financing Fire Station 2 by a vote of 6-0.

Director/Treasurer Matusiewicz reported there were other funds which reflect reduced revenue estimates. He noted that some Master Plans had reduced revenues but also had reduced project expenditures. He reported the transfer into the Master Plans was decreased by \$1 million. He noted the graph reflects Master Plan funds pre- and post- COVID-19 and explained there is \$13 million more in Harbor and Beaches Master Plan than what is reflected in the report. He noted the budget is being balanced by reducing Capital funding and reducing Capital spending. Chair O'Neill requested a simplified report be prepared for City Council review.

Committee Member Collopy requested Director/Treasurer Matusiewicz develop a simplified report quickly so it can be reviewed.

Director/Treasurer Matusiewicz discussed the Additional Discretionary Payment (ADP) to CalPERS and explained the City likes to keep the payment below \$35 million and recapped discussions to use Surplus Revenue to pay down the debt. He hopes to send CalPERS the first \$5 million in the next six (6) months and revisit the additional payments down the road.

In response to Chair O'Neill's inquiry, Director/Treasurer Matusiewicz explained the \$5 million ADP will come from reserved funds but still requires City Council approval. Chair O'Neill recapped the report and noted the Proposed Budget shows expenditures of \$219.8 million and a \$5 million CIP transfer which is \$224.8 million. Director/Treasurer Matusiewicz explained how the \$5 million ADP and is entered in the Proposed Budget. Chair O'Neill requested Director/Treasurer Matusiewicz be prepared to explain he used Generally Accepted Accounting Principles (GAAP) properly when reconciling the \$5 million.

Committee Member Collopy suggested reporting on All Funds to make the report easier to understand. In response to Committee Member Collopy's inquiry, Director/Treasurer Matusiewicz reported the ADP in FY 19/20 is \$8.8 million based on an expected 7% rate of return for future years. He further explained the ADP in FY 20/21 is \$5.246 million to cover past liabilities and the \$5 million is anticipatory of future capital market losses. He advised CalPERS has projected investment returns for the next 10-years to be approximately 6%.

Director/Treasurer Matusiewicz clarified the outlook was discussed in a November Finance Committee meeting and it was agreed up to review annually but is based on a five (5) year outlook. He explained CalPERS new amortization assumes 20 years repayment starting three (3) years out.

In response to Committee Member Collopy's inquiry, \$5.3 million from the Proposed Budget is allocated to ADP payments and the additional \$5 million is being reserved. He clarified the ADP of \$10.3 million only includes \$2.5 million from actual reserves.

Director/Treasurer Matusiewicz recapped the next milestones which includes creating a new presentation by May 26, 2020 for City Council review. Chair O'Neill suggested rescheduling the next meeting to June 4th to allow additional time for Finance Committee to review the Proposed Budget and was agreed upon by all.

In response to Committee Member Stapleton, Director/Treasurer Matusiewicz explained the he is unsure if the COVID-19 pandemic will financially similarly to the Great Recession of 2008.

In response Committee Member Reed, Director/Treasurer Matusiewicz was unable to answer if City Council would provide any financial assistant to local small businesses.

In response to Council Member Dixon's inquiry, City Manager Leung reported COVID-19 related expenses are reimbursable from the Federal Emergency Management Agency (FEMA). She reported the Orange County Board of Supervisor allocated Coronavirus Aid, Relief, and Economic Security (CARES) Act funding to reimburse City's from that funding and are in current discussions to determine what would be reimbursable. She also explained any expense not reimbursed through FEMA or CARES would be an additional expense for the City.

Committee Member Tucker thanked staff for their report and is hopeful the next revision of the report is easier to follow.

Chair O'Neill opened public comments.

Jim Mosher commented it would be helpful to the public if the Finance Committee had explained the budget had been posted. He also reported the agenda overlooked public comments on non-agenda items and needs to be added into future agendas.

Chair O'Neill closed public comments.

There was no further action taken on this item.

C. WORKPLAN REVIEW

Summary:

Staff will review with the Committee the agenda topics scheduled for the remainder of the calendar year.

Recommended Action:

Receive and file.

Chair O'Neill reported there may be a Finance Committee on June 11th and 25th but is dependent on budget review.

Chair O'Neill opened public comments.

Mr. Mosher inquired if the Finance Committee will be taking their usual break during the summer given the review of the Revised Budget in July. Chair O'Neill responded that the topic will be discussed at the next Finance Committee.

Chair O'Neill closed public comments.

Chair O'Neill acknowledged there was no public comment period for non-agenda items and opened public comments.

Mr. Mosher commented the meeting was not live-streamed although he believed that was the original intention. He also commented there was confusion regarding the meeting location which was not noted on the agenda.

Chair O'Neill closed public comments.

There was no further action taken on this item.

VI. FINANCE COMMITTEE ANNOUNCEMENTS ON MATTERS WHICH MEMBERS WOULD LIKE PLACED ON A FUTURE AGENDA FOR DISCUSSION, ACTION OR REPORT (NON-DISCUSSION ITEM)

None

VII. ADJOURNMENT

The Finance Committee adjourned at 4:53 p.m. to the next regular meeting of the Finance Committee on June 4, 2020 at 4:00 p.m.

Filed with these minutes are copies of all materials distributed at the meeting.

The agenda for the Regular Meeting was posted on Thursday, May 14th, at 4:20 p.m., in the binder and on the City Hall Electronic Board located in the entrance of the Council Chambers at 100 Civic Center Drive.

Attest:

Will O'Neill, Chair
Finance Committee

Date

DRAFT