



Department: Finance
Cost Center: 2002
For Agenda of: 1/14/2025
Placement: Business
Estimated Time: 90 minutes

FROM: Emily Jackson, Finance Director
Prepared By: Riley Kuhn, Principal Budget Analyst

SUBJECT: 2025-27 BUDGET FOUNDATION

RECOMMENDATION

1. Provide staff with input on the 2025-27 Community Forum and Goal Setting Workshop; and
2. Provide staff with initial input relative to existing Major City Goals; and
3. Review and provide feedback on revised fiscal policies and recommended budget balancing strategies; and
4. Review and discuss the general economic outlook for the 2025-27 Financial Plan development; and
5. Review the long-range Capital Improvement Plan overview; and
6. Review information about CalPERS Additional Discretionary Payments (ADP) and direct staff to recommend allocation of FY 2023-24 unassigned fund balance to increase the ADP as part of the FY 2024-25 Second Quarter Budget Report.

REPORT-IN-BRIEF

Development of the 2025-27 Financial Plan officially began on December 10th, when staff presented the “Setting the Stage” budget item. That item included broad contextual information on year-to-date financial results, state legislation impacting cities, a report on macroeconomic conditions and how they influence the City’s finances, and a discussion on how the growth of the community impacts the budget.

This item continues the discussion from Setting the Stage and includes:

- A review of Community Survey results and the upcoming the goal setting process;
- Recommended changes to fiscal policies;
- Recommended Budget Balancing Strategies to provide further guidance to staff in development of the City’s annual budgets;
- A review of the long-term Capital Improvement Plan;
- A discussion of additional discretionary payments (ADPs) to CalPERS; and
- A curated package of third-party economic forecasting materials and a revisit of the City’s Long-Term Forecast for the General Fund to provide additional context for 2025-27 budget development.

POLICY CONTEXT

Development of the City's budget is required and guided by State law, the City's Municipal Code, City Charter, and the fiscal policies which are reviewed and reaffirmed by the City Council every two years.

California State Law

1. Article XIII B of the California Constitution and California Government Code Sec. 7910 requires that cities establish appropriations limits¹ by resolution annually. The City of San Luis Obispo complies with this requirement through adoption of its annual budget.
2. California Government Code Section 53901 requires each local agency to file its budget with the county auditor within 60 days after the beginning of its fiscal year.

City Charter

1. 801. Fiscal Year – establishes that the City's Fiscal Year commences on July 1 of each year.
2. 802. Annual Budget – requires that the City Manager shall provide the Council a careful estimate, in writing, of the amounts, specifying in detail the objects thereof required for the business and proper conduct of the various departments, offices, Boards and Commissions of the City, over which the office has control, during the next ensuing year.
3. 803. Public Hearing – sets forth the requirement for a public hearing to adopt the annual budget.
4. 804. Adoption of Budget – requires the Council to adopt the budget and allows that after adoption of the budget, the Council may amend or supplement the budget by motion adopted by a majority vote of the Council.

DISCUSSION

Two-year Financial Plan Process

The City has long used a two-year financial plan along with annual budgets. The benefits of the two-year plan include:

1. Reinforcing the importance of long-term thinking
2. Aligning resource allocation decisions with significant council directed priorities
3. Establishing realistic multiyear timeframes for achieving objectives

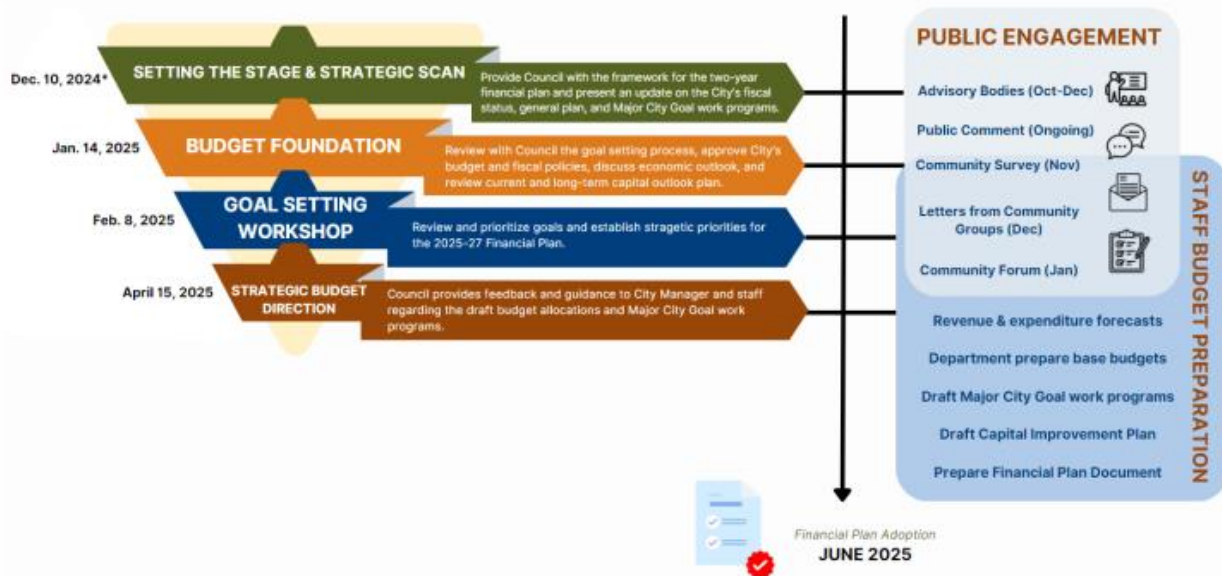
The fundamental purpose of the City's budget process is to link, through public engagement and strategic discussions, the priorities of the community to the available

¹ The City's appropriation limit is based on the Gann Spending Limit Initiative, a State constitutional amendment adopted by the voters on June 6, 1979 and amended in 1990 with Proposition 111. It is anchored in the State Constitution under Article XIII B. The limit restricts appropriations from tax revenues by State and local governments. Under its provisions, no local agency can appropriate proceeds of taxes in excess of its "appropriation limit". Excess funds may be carried over into the next year. However, any excess funds remaining after the second year must be returned to taxpayers by reducing tax rates or fees; a majority of the voters may approve an override to increase the limit.

resources in order to achieve the desired outcomes. The process allows the City Council to engage the community in identifying Major City Goals while also providing information regarding the City’s basic functions, including the day-to-day work programs and responsibilities carried out by City employees to support resident quality of life and community well-being.

Goal-Setting Process

A detailed Financial Plan Calendar was approved by the City Council on October 1, 2024 and is posted on the City’s [website](#). There are a variety of opportunities to provide input to the City Council as they work to establish Major City Goals with the community’s needs and interests in mind. These opportunities are highlighted in the following graphic:



Community engagement efforts began in October and are ongoing. In addition to this Budget Foundation item, which includes the results of the Community Survey and Advisory Body goals, the two principal elements of the City’s goal setting process are the Community Forum, to be held at the Ludwick Center on Thursday, January 23rd at 6:00 PM, and the Council Goal Setting Workshop, to be held at City Hall on Saturday, February 8th 2025.

Community Priorities Survey

The Community Priorities Survey was open for one month and closed on December 13th, 2024. Community members were notified with their utility bills in the mail or attached as a PDF for paperless customers. The City also notified the public with social media posts, on its website, at various advisory body meetings, and at the October 1st and December 10th City Council meetings.

The survey gathered input from 1,629 community members and will help guide discussions and decisions in the budget process. Participation increased by 25% compared to two years ago, reflecting strong community engagement. While not statistically representative, the survey results indicate that the community’s priorities for

the next two years align closely with the City's current priorities and work programs. Attachment A includes a summary of the results; for a deeper understanding of the community's perspectives, readers can reference all of the survey responses which are included as a [reading file](#). The top five priorities identified in the survey were homelessness, infrastructure maintenance, downtown vitality, housing supply and affordability, and open space. The survey also included an optional open-ended question for respondents to identify how the City might adjust funding current projects or services to accomplish any new priorities. Approximately 45% of respondents provided input to that question, with recurring suggestions for prioritizing basic services, addressing homelessness, improving cost efficiency, and balancing priorities.

Staff is not seeking specific direction regarding the community survey results at this time and are providing the results to begin informing future discussions regarding Major City Goals for the 2025-27 Financial Plan. For more information, please see Attachment A.

Community Forum

The Community Forum, scheduled for January 23, 2025, serves as a vital platform for community engagement, allowing residents, stakeholders, and City Councilmembers to collaboratively shape the City's Major City Goals for the 2025-27 Financial Plan. This interactive event invites participants to review and provide input on existing plans and policies while exploring new ideas. The forum also fulfills the requirements for the Revenue Enhancement Oversight Commission (REOC) to hold a Citizens' Oversight meeting for the use of the Local Revenue Measure funds. Attachment B includes details about the Community Forum, including the key topics for interactive stations and a draft agenda.

Insights from the forum will guide the City Council during their February 8, 2025 Goal-Setting Workshop, where they will refine long-term objectives and discuss how to prioritize the use of limited resources to align with the services most valued by the community. In early January, staff will provide Councilmembers with pre-work instructions to help prepare for the facilitated discussion on February 8.

Staff is seeking feedback regarding any requested changes to the Community Forum format, agenda, or identified topics for the interactive stations, which have been developed based on the outcome of the community survey. For more information, please see Attachment B.

Fiscal Policies

One purpose of the Financial Plan is to set clear fiscal policies that support sound financial decision making. The City's Fiscal Policies are typically included in the reference section of the Financial Plan and cover a broad range of fiscal topics, including:

1. General Revenue Management
2. User Fee Cost Recovery Goals
3. Enterprise Fund Fees and Rates
4. Revenue Distribution

5. Investments
6. Appropriation Limitations
7. CalPERS and Unfunded Liability Management
8. Capital Improvement Management
9. Debt Management
10. Human Resources Management
11. Contracting for Services
12. Productivity

With each financial plan, the City reviews its fiscal policies to determine if any updates are necessary. Changes are generally intended to create consistency amongst various City policies, reflect current practices, and create a system that is effective and efficient to administer.

Staff is seeking input from Council on the changes to the Fiscal Policies that are recommended as shown in Attachment C. The most significant changes to the Fiscal Policies reflect Council's action on July 2, 2024 to adopt a new user fee schedule. Other notable changes include clarification of Capital budgeting practices and modernizing the Human Resources Management policies to reflect current and best practices.

Budget Balancing Strategies

Staff has developed a set of Budget Balancing Strategies that are intended to serve as a playbook for sound fiscal management in both good times and bad. This document incorporates guidance included in other Council adopted documents including the Fiscal Health Contingency Plan, Financial Responsibility Philosophy, Fiscal Health Response Plan and Compensation Philosophy and provides strategies to operationalize many of the ideas in those plans. While development of the document was prompted by the deficit forecasted in later years of the current 5-year forecast, this document is flexible enough to provide guidance to staff not only in times of budget difficulty, but also in times of fiscal recovery and growth.

Staff is seeking input from Council on the proposed strategies provided in Attachment D.

Financial Plan Organization

The organization of the Financial Plan has been incrementally improved with each budget cycles and closely aligns with industry standards and best practices. Based on a careful review, staff is planning to make minimal changes to the organization of the document in order to improve readability and more effectively communicate the important information it contains.

Staff is seeking input from Council on other changes it would like to see to the structure and content of the Financial Plan document; for more information, please see Attachment E.

Economic Outlook

Macroeconomic conditions have always been difficult to predict and economists have had an even more difficult time forecasting the trajectory of the post-COVID economy. While economic developments can have a significant impact on the City's finances, staff hesitates to speculate about macroeconomic conditions and seeks to recommend budgets that are most prudent in an uncertain environment.

Attachment F to this report includes links to a number of reputable sources of economic materials including the Federal Reserve's Summary of Economic Projections, the Central Coast Economic Forecast materials presented by Beacon Economics, HdL's statewide sales tax analysis, and materials from the State of California's Legislative Office and Employment Development Department. These materials provide broad context for the current economic conditions nationally, statewide, and regionally.

The consensus of these reports is that despite numerous recession indicators including an inverted yield curve, increased unemployment rates, and ongoing geopolitical strife, a recession is no longer expected. This consensus points to a return to growth in cyclical revenues for the City including sales tax, transient occupancy tax, and development review fees.

This report also includes a revisit of the City's long-term forecast for the General Fund, which was previously presented to Council and projects deficits in future periods.

Staff is not seeking any guidance from Council on the Economic Outlook. For additional information, please see Attachment F.

CalPERS and the City's Unfunded Pension Liabilities

The City of San Luis Obispo, like many other California municipalities, is a participant in the California Public Employees' Retirement System (CalPERS) pension system, which provides retirement benefits to City employees. The City identified addressing unfunded pension liabilities as a priority with the Fiscal Year 2018-19 Supplemental Budget and the Fiscal Health Response Plan recommended Additional Discretionary Payments (ADPs) to reduce the City's unfunded liability. The most recent actuarial evaluation showed that the City's unfunded pension liabilities have continued to grow.

To address unfunded liabilities, the City has made at least \$2 million in annual discretionary payments to CalPERS from the General Fund and larger payments when resources allow. Unfortunately, the investment losses experienced by CalPERS have decreased the impact that the City's ADPs have had on the funded status of the City's pension plans. Attachment G to this report includes an analysis of how the \$2 million payment would need to increase in order to keep up with growth in staffing expenditures over time.

Staff is seeking guidance from Council on a recommended increase to the annual ADP amount. For the current year, staff recommends that Council direct staff to recommend

allocation of FY 2023-24 unassigned fund balance to increase the ADP with the FY 2024-25 Second Quarter Budget Report. For more information, please see Attachment G.

Long-range Capital Improvement Plan

Development of the Capital Improvement Plan (CIP) for the 2025-27 Financial Plan is in its early stages. The CIP serves as a critical roadmap for addressing the City's immediate and long-term infrastructure needs. This financial plan builds on lessons learned from past cycles and introduces significant process improvements to enhance clarity, transparency, and accountability in project prioritization and funding allocation.

For 2025-27 Financial Plan, the approach focuses on aligning resources with realistic project delivery timelines, ensuring fiscal responsibility, and maintaining the City's existing assets. This foundation is vital as the City navigates evolving challenges and opportunities in managing infrastructure investments.

One significant change for the 2025-27 Financial Plan is the shift to fully budgeting for out-years in the CIP, moving away from planning without clear resource constraints beyond the immediate financial plan. This change fosters more intentional long-term decision-making in response to escalating project costs and numerous infrastructure commitments. It also helps set clearer expectations for when projects can realistically be delivered, ensuring greater transparency and alignment between planning and execution.

Staff is not seeking any guidance from Council on the Long-Range Capital Improvement Plan. For more information, please see Attachment H.

Previous Council or Advisory Body Action

Various Advisory Bodies have submitted recommendations for Council's consideration in the 2025-27 goal setting process. These recommendations can be found in Attachment I, which are provided for consideration as part of the Major City Goal and work plan development process.

Public Engagement

Public engagement on this item can be provided to the City Council through written correspondence prior to the meeting and through public testimony at the meeting. This item continues the extensive public engagement processes to support development of the 2025-27 Financial Plan as discussed above.

CONCURRENCE

The City's internal Financial Plan Steering Committee concurs with the recommendations included in this report.

ENVIRONMENTAL REVIEW

The California Environmental Quality Act (CEQA) does not apply to the recommended action in this report because the action does not constitute a "Project" under CEQA Guidelines Sec. 15378.

FISCAL IMPACT

Budgeted: N/A
 Funding Identified: N/A

Budget Year: 2025-27

Fiscal Analysis:

Funding Sources	Total Budget Available	Current Funding Request	Remaining Balance	Annual Ongoing Cost
General Fund	\$	\$	\$	\$
State				
Federal				
Fees				
Other:				
Total	\$N/A	\$N/A	\$N/A	\$N/A

The recommendations included in this report have no immediate fiscal impact but are part of the financial planning process which is intended to ensure that the City is able to provide the maximum benefit to the community with the resources available.

ALTERNATIVES

1. **Council could direct staff to continue with Additional Discretionary Payments to CalPERS in the same amount as prior years.** This would provide flexibility to address other priorities, but would slow progress in paying down pension liabilities.
2. **Council could modify the proposed Goal Setting activities.** The Council could direct staff to pursue a different process for goal-setting. This action is not recommended because there is value to the community in conducting consistent processes year to year to ensure resident engagement. Should modifications to the Goal Setting activities be made, staff recommends incremental adjustments to the activities planned.
3. **Council could direct further changes to the recommended financial plan policies provided in Attachment C.** Council may direct modifications to the financial plan policies, which will be incorporated into the 2025-27 Financial Plan document.
4. **Council could direct further changes to the recommended budget balancing policies provided in Attachment D.** Council may direct modifications to the budget balancing policies, which will be incorporated into the 2025-27 Financial Plan document.
5. **Council could direct modifications to the Financial Plan Organization, described in Attachment E, or direct other changes to the financial plan.** Council may direct modifications to the financial plan organization or content, which will be incorporated into the 2025-27 Financial Plan document.

ATTACHMENTS

- A - Community Survey Responses
- B - Plans for Community Forum and Goal Setting
- C - Review of Financial Plan Policies
- D - Budget Balancing Strategies
- E - Review of Financial Plan Organization
- F - Review of Economic Conditions
- G - CalPERS Pension Plans and Funded Status
- H - Long-Range Capital Improvement Plan
- I - Advisory Body Goals