



Quarterly Financial Report  
As of June 30, 2012 - **UNAUDITED**

## Introduction

This report provides an analysis of the City's General Fund revenues and expenditures for the fourth quarter of the 2011-12 fiscal year. The numbers in this report are **PRELIMINARY ONLY**, as the year is not yet officially closed, and the annual Financial Audit is scheduled to begin October 29, 2012.

The Audited Financial Statements will be presented to the City Council in early 2013.

## Management's Overview

The City's two year budget for fiscal years 2011-12 and 2012-13 was adopted by the City Council on June 21, 2011. The purpose of the quarterly report is to provide regular updates and propose adjustments to the Council regarding revenue and expenditure trends to ensure the City Council has a strong understanding of the City's current financial condition. The 2011-12 first quarter report was presented to the City Council on November 15, 2011, and included increases to General Fund revenues of \$1.2 million, and increases to General Fund expenditures of \$0.3 million. The second quarter report was presented on February 7, 2012 and although it did not propose any adjustments to revenues or expenditures, the operating deficit was revised down to (\$3.2) million based on salary savings from departments with high vacancies (e.g. Public Safety). The third quarter report was presented on May 1, 2012, and included increases to General Fund revenues of \$0.9 million, and identified further departmental savings – reducing the Operating Deficit to (\$1.4) million.

As the following report will detail, the City of Napa is estimating closing FY 2011-12 in a positive position. This positive news is the combination of stronger than expected revenues (\$2.5 million over 3<sup>rd</sup> Quarter projections), and one-time savings from departments (\$0.2 million additional savings over 3<sup>rd</sup> Quarter projections).

Additionally, an overview of the City's Operating position and General Fund Undesignated Reserves will be provided, summarizing the City's recent reserve use / contribution.

Thirdly, although the focus of this report is the FY 2011-12 estimated revenues and expenditures, it is necessary to consider the FY2012-13 Budget and beyond to ensure long-range perspective when considering one-time (e.g. CIP Projects) or on-going (e.g. additional positions, benefits, programs) adjustments to the Budget.

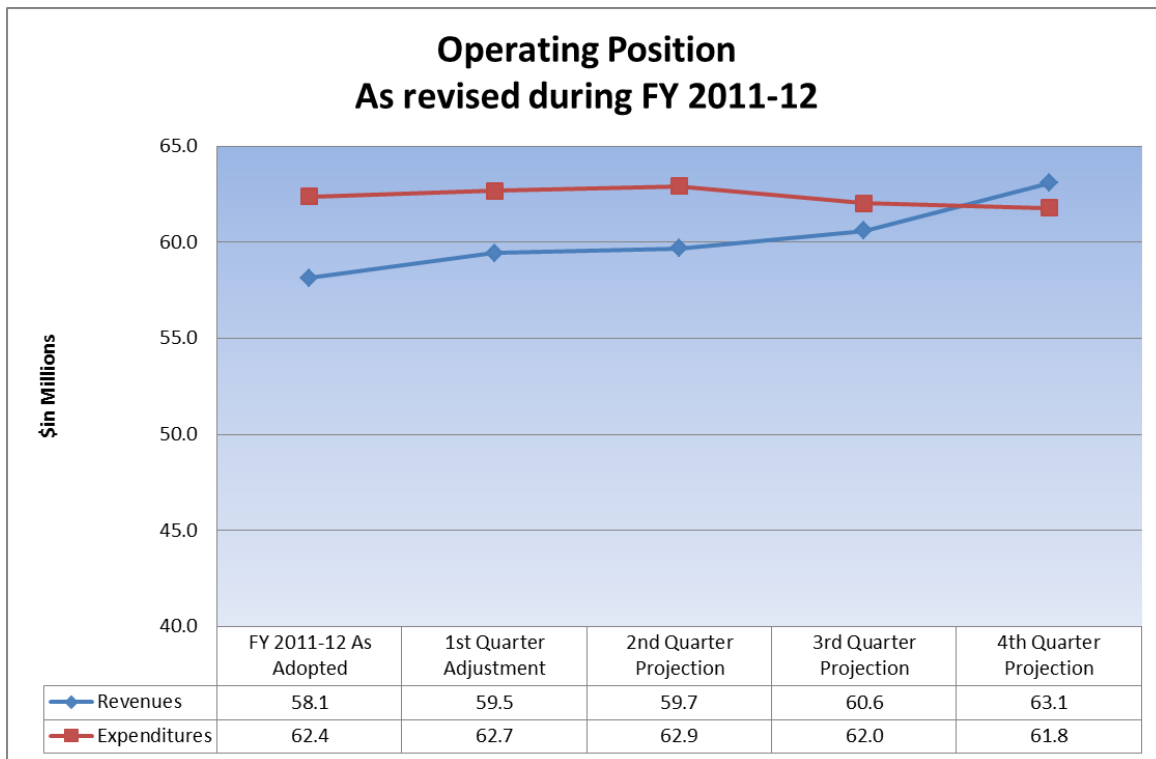
Finally, as in previous quarterly reports, the final section “What we are watching”, will provide a brief summary of the potential issues and impacts at the national, state and local levels.

### **FY 2011-12 Budget**

The FY 2011-12 budget as originally adopted estimated revenues of \$58.2 million to fund expenditures of \$62.4 million with the resulting \$4.2 million shortfall to be funded from operating reserves. The City’s General Fund Undesignated Reserve as of July 1, 2011 was \$6.29 million, and it was anticipated to be fully depleted by the end of the biennial budget June 30, 2013 to cover the structural imbalance in both FY 2011-12 and FY 2012-13.

As previously noted, the quarterly reports include proposed revisions to revenues and expenditures, as well as highlighting the resulting impact to operating position and General Fund Undesignated Reserve. The revenue increases in FY 2011-12 were based on an assessment of increased revenues that were expected to be sustainable over the long term, as well as “one-time” revenues (e.g. pent up demand in sales tax). The same assessment was done with estimated expenditures, with particular focus on the one-time savings resulting from vacant positions (especially in Public Safety).

Based on our current analysis, the budgeted operating *deficit* of \$4.2 million was eliminated over the course of the year through a combination of increased revenues and one-time departmental savings. The final operating position for the City will be finalized during the upcoming financial audit, however it is currently projected to result in a *positive* operating position of approximately \$1.3 million. The graph below reflects the changes in the FY 2011-12 operating position as reported to the Council during the quarterly reports.



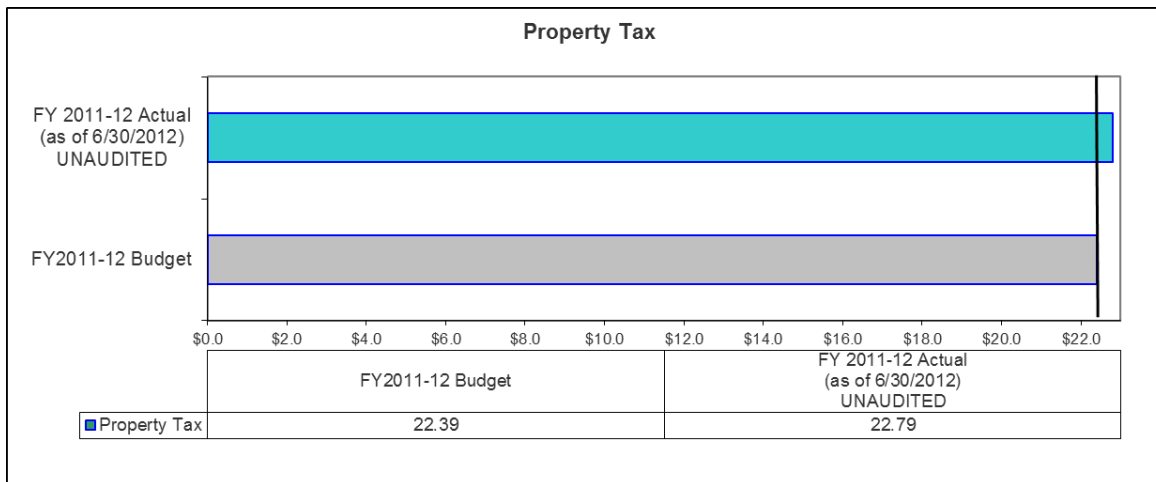
Although this is good news for the City, it is important to reinforce how the surplus was created by one-time elastic revenues (e.g. pent up demand), and one-time savings from vacant positions in Public Safety.

### **Major Revenues**

**Property Tax** - The City's major source of property tax revenue to the General Fund is residential property (77.6%), followed by commercial property (12.2%) and industrial property (5.1%).

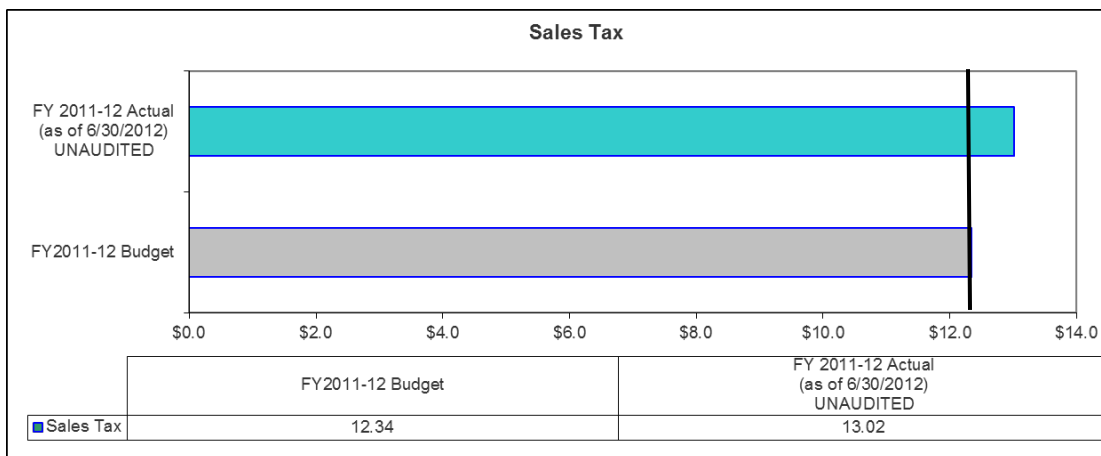
FY 2011-12 Property Tax receipts were originally budgeted at \$21.4 million, and adjusted upward by \$600,000 in the 1<sup>st</sup> Quarter Report to \$22.0 million to reflect a 0.27 percent increase in the City's assessed valuation for FY 2011-12 compared to FY 2010-11. Another \$400,000 upward adjustment was made in the 3<sup>rd</sup> Quarter Report to \$22.4 million.

*It is estimated that Property Tax revenues will end FY11/12 at \$22.8 million and exceed the budget by \$0.4 million, resulting from additional property tax receipts of approximately \$400,000 received from the County made available through the dissolution of the Redevelopment Agency on January 31, 2012.*



**Sales Tax** - FY 2011-12 Sales Tax was originally budgeted at \$12.0 million, but was adjusted upward in the 1<sup>st</sup> Quarter Report to \$12.3 million, to more accurately reflect the continued economic recovery. Specifically we have seen increases in General Retail (e.g. Department Stores), Food Products (e.g. Restaurants), Transportation (e.g. Car Sales, Service Stations) and Construction (e.g. Building Materials) sales tax receipts over the previous quarter.

*It is estimated that Sales Tax revenues will exceed the last budget adjustment by \$0.7 million, resulting from quicker than anticipated economic recovery and end FY11/12 at \$13.0 million. It is estimated that approximately \$500K of the FY 2011-12 sales tax revenue is related to pent-up demand (e.g. new car sales), increased construction activity, and increased tourism. Staff will be watching the FY 2012-13 Sales tax revenues very closely to further refine this estimate. The following graph tracks the Sales Tax on collections on sales through June 30, 2012.*

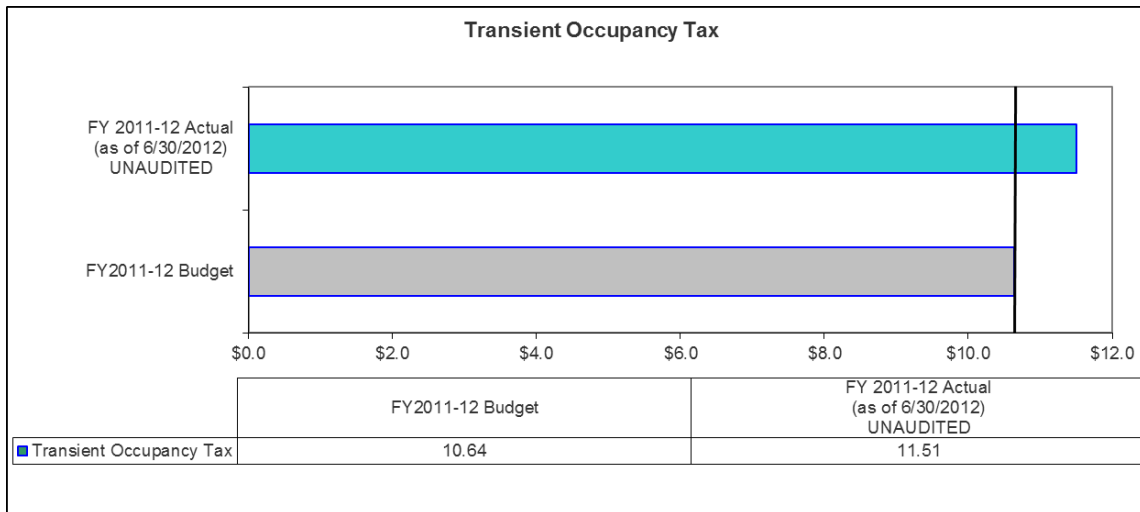


**Transient Occupancy Tax (TOT)** - There are currently 23 hotels, 18 bed and breakfast establishments and 38 vacation rentals generating transient occupancy tax revenue within the City.

FY 2011-12 TOT revenue was originally budgeted at \$9.4 million, but adjusted upward by \$500,000 to \$9.9 million in the 1<sup>st</sup> Quarter Report, and again adjusted upward by \$750,000 to \$10.6 million in the 3<sup>rd</sup> Quarter Report to reflect the

improvement in the City's tourism business. The City is experiencing continued high tourism as a result of destination council activities that have effectively extended Napa's tourism season well into fall. *It is estimated that Transient Occupancy Tax revenues will exceed the last budget adjustment by \$0.9 million and end FY11/12 at \$11.5 million, due to continued strong tourism throughout the year.*

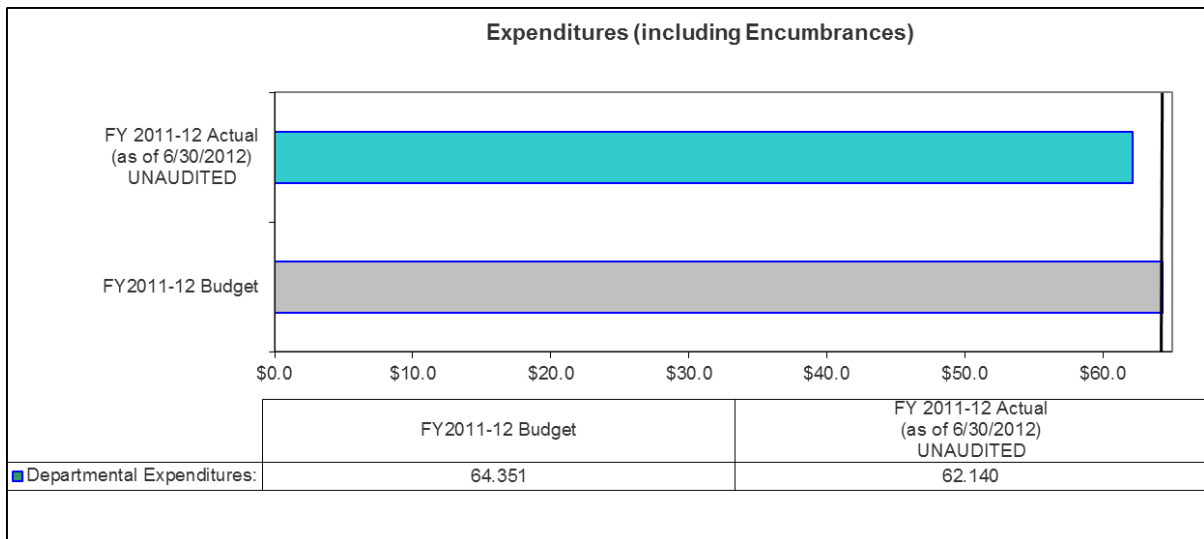
The following graph tracks the Transient Occupancy Tax (as remitted by hotels, inns, etc. based on receipts through June 30, 2012).



## **Expenditures**

Estimated June 30, 2012 expenditures anticipate all departments operating within their approved budgets. As stated earlier, the final operating budget for FY11/12 (which includes carry forward, budget resolutions and adjustments throughout the fiscal year) was \$64.4 million. It is estimated that FY11/12 actual expenditures will total \$61.8 million (including carry forwards), which is \$0.2 million less than the 3<sup>rd</sup> Quarter projection. As previously noted, a significant portion (50%) of the \$2.6 million difference between the FY2011-12 Budget (as of 6/30/2012) and projected expenditures are related to the high number of vacancies in Public Safety throughout the year. As these positions are filled and we reach fully staffed levels, this "savings" will be used to pay our new employees.

The following graph tracks the General Fund Expenditures as compared to the approved budget. Please note that the unaudited estimate as presented includes active encumbrances assuming these dollars will be carried forward. This assumption has been included to more accurately estimate the General Fund Undesignated Reserve balance available as of June 30, 2012.

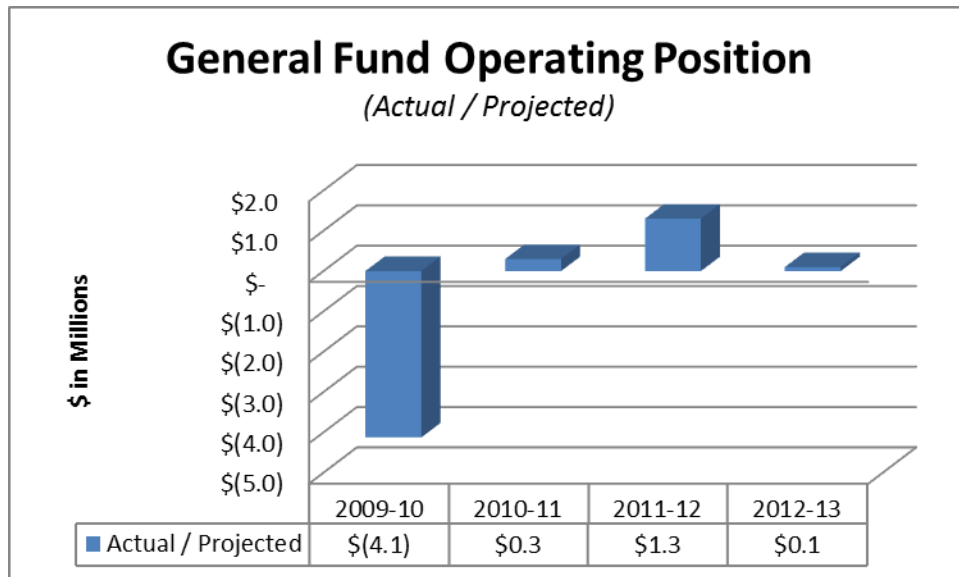


Additional analysis and details on expenditures will be provided upon completion of the FY2011-12 Financial Audit.

### **Operating Position & Reserves**

As of June 30, 2012, the FY 2011-12 General Fund is estimated to complete the year with a \$1.3 million positive impact to General Fund Undesignated Reserve, which is estimated to be \$4.5 million (or approximately 7% of the FY 2012-13 Operating Budget).

The following graph reflects the City's Operating position for FY 2009-10 through FY 2012-13.



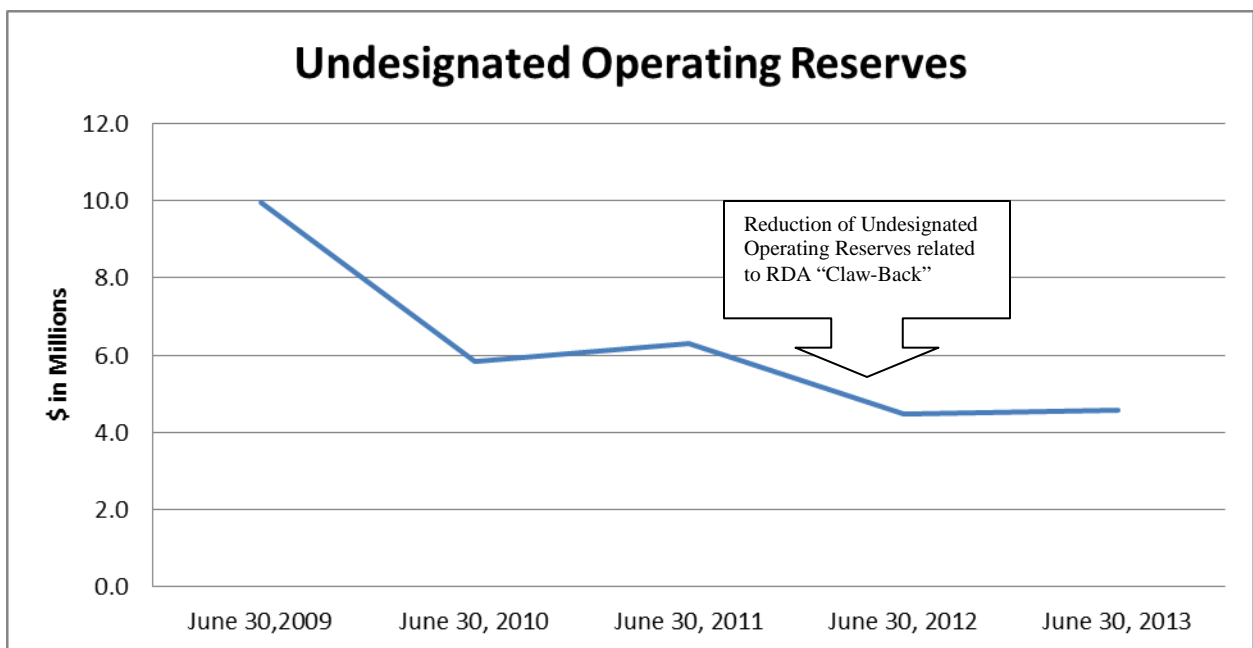
As shown in the graph above, FY2011-12 was the City's second year in a row with a positive operating position. The FY2011-12 budget as adopted on June 21, 2011 anticipated a negative operating position requiring the use of \$4.2 million in General Fund Undesignated Reserves, however throughout the year,

the combination of Increased revenues (\$2.5 million), Public Safety vacancies (\$1.3 million) and other departmental savings (\$1.7 million) combined to fully offset the negative, and provide the City with a \$1.3 million surplus.

(\$ in millions)		FY2011-12
Operating Position As Budgeted	\$	(4.2)
Increased Revenues		2.5
Salary Savings		1.3
Other Departmental Savings		1.7
Net Operating Position	\$	1.3

The next graph depicts the General Fund Undesignated Reserves from June 30, 2009 through June 30, 2013. The impact of the \$3.1 million RDA claw back reserve approved during the Mid Cycle review is reflected in the June 30, 2012 projected balance.

The estimated \$4.5 million General Fund Undesignated Reserve is approximately 7% of the FY 2012-13 budget. Per the approved Financial Policy the City will transfer Undesignated Reserves in excess of 5% of the operating budget to one time expenditure accounts like Reserves or Capital Projects as reviewed and approved by the Council. This transfer will be completed each year after the audit of the Financial Statements is complete (FY2011-12 Audited Financials will be presented in early 2013). At this time, it is estimated the City will be transferring \$1.4 million in excess reserves to the Capital Projects fund for currently unfunded projects (e.g. Construction of the Main Street Boat Dock).



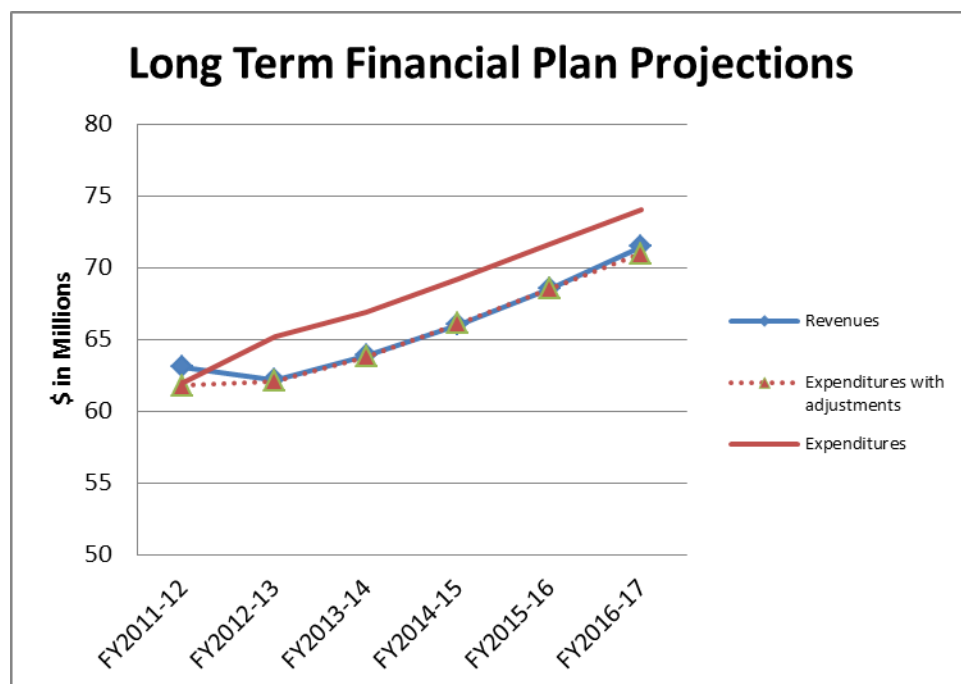
### **FY2012-13 Budget**

As part of the budget message in June, 2011, it was promised that adjustments to the FY2012-13 budget would be presented to the Council in Spring 2012 and would detail the reductions necessary to eliminate the use of \$3.9 million in undesignated reserves and bring the City budget into a balanced position for the first time in ten years. This was accomplished as a combination of an improving local economy (resulting in ongoing revenue increases of \$2.9 million) combined with prudent fiscal management from the City Council which included programmatic reductions by departments (savings of \$1.5 million) and concessions from the various bargaining groups (savings of \$1.6 million). Additionally, expenditure increases were included in the Mid Cycle Review (\$2.1 million) resulting in a net reduction of (\$1.0) million, and a positive operating position.

The graph below provides the estimated year end revenues and expenditures for FY 2011-12, and also projects the Revenues and Expenditures through FY 2016-17. The solid expenditure line reflects the projected expenditures prior to the FY 2012-13 Mid cycle adjustments which reduced expenditures by approximately \$3.1 million each year through a combination of departmental programmatic reductions (\$1.5 million) and concessions from the various bargaining groups (\$1.6 million). The dashed expenditure line represents the projected adjusted expenditures.

As shown in the graph below, one time revenues or expenditure savings may adjust a fiscal year “dot” up or down, but will not adjust subsequent years revenue or expenditure estimates. Only on-going, sustainable adjustments to revenue or expenditures will actually impact the City’s operating position in the long term.

*Please note: The Long Term Financial Plan is currently being updated, and will be presented to Council in January 2013.*





**What We Are Watching****Nationally:**

Although it is too soon to be overly optimistic for the future, it does appear recovery from the economic recession continues its slow steady progress. We still have concerns over the state of the national economy and its trickle down effects on state and local government. Napa is fortunate in that our revenues are remaining steady, or even showing slight gains, however the bleak national outlook reminds us that fiscal caution is still a necessity.

Lack of confidence in the real estate markets and the prolonged effects of high national unemployment continue to be major concerns for the nation, as well as continued turmoil in world financial and economic markets. These are all issues we will be watching to anticipate and hopefully lessen any impact to our local community.

**State:**

At the State level, California's economy continues to be fragile, with high unemployment and continuing impacts from unsteady global markets (e.g. China). The impacts of the November election, and specifically the tax initiatives, will most certainly impact local governments, as the success or failure of those plans will probably change the role and responsibilities of both the Counties and Cities.

We will continue to watch Sacramento to anticipate any revenue or expenditure impacts, and react and adjust to them as quickly and efficiently as possible.

**Local Economic Condition:**

During the recently completed fiscal year, the City of Napa saw real growth in its major taxes (Property, Sales and Transient Occupancy Tax). Although Sales Tax and Transient Occupancy Tax are both important revenue streams for the City, and had strong gains in FY 2011-12, they are considered "elastic" revenues as they tend to ebb and flow with the general economy. Property Tax, on the other hand, is "inelastic" in that it tends to be more consistent over time, regardless of the short term ups and downs. Although Property Tax has shown slow and steady growth over the past year, we need to continue to be "cautiously optimistic" in our revenue projections to ensure we rebound at a rate that can be supported and sustained by the local economy.

Additional good news includes the fact that unemployment in Napa is falling, (7.7% in July 2012, 1.3% lower than March 2012), and the average sales price of homes has increased. Tourism in the Napa Valley continues to grow, with many activities extending the tourism season well into late fall / early winter.

Although we have reason to feel positive about the future, we need to continue to be prudent in budgeting, and balance our Operating Expenditures with our Operating Revenues and use General Fund Undesignated Reserve balance to replenish reserves and/or one-time expenditures like capital projects. To use

General Fund Undesignated Reserves to increase operating expenditures (in anticipation of increasing revenues), especially if those revenues are one-time in nature, jeopardizes the budget cuts and concessions achieved in the fiscal year 2013 budget (and future budgets) that accomplished a structurally balanced budget (whereby current year expenditures equal current year revenues) for the first time in ten years.

**Recommendation**

Receive and file the Fourth Quarter Report for Fiscal Year 2011-2012.

**FY 2011-12 Financial Update - NOT CLOSED / NOT AUDITED**  
**General Fund**

	FY2011-12 Budget (as of 6/30/2012)	FY2011-12 3rd Quarter Projection	FY2011-12 YTD (as of 6/30/2012)	%
<b>Operating Revenues</b>				
Property Tax	22.4	22.4	22.8	101.80%
Sales Tax	12.3	12.3	13.0	105.48%
Transient Occupancy Tax	10.6	10.6	11.5	108.12%
Other Revenues	15.5	15.2	15.8	101.80%
<b>Total Operating Revenues</b>	<b>60.9</b>	<b>60.6</b>	<b>63.1</b>	<b>103.65%</b>
<b>Operating Expenditures</b>				
Estimated through 6/30/2012			60.2	
Carry forward for Police and Fire (effective 7/1/2012)			.6	
Carry Forward (Active Encumbrances & Contracts)			1.0	
<b>Total Operating Expenditures</b>	<b>64.4</b>	<b>62.0</b>	<b>61.8</b>	<b>96.10%</b>
<b>Net Impact of Operations to Fund Balance</b>	<b>(3.4)</b>	<b>(1.4)</b>	<b>1.3</b>	

	FY2011-12 Budget (as of 6/30/2012)	FY2011-12 YTD (as of 6/30/2012)
<b>Impact to Fund Balance</b>		
<b>Estimated 6/30/2012 Unrestricted Reserve Fund Balance</b>	<b>2.8</b>	<b>7.6</b>
<i>Claw-back for NCRA (effective 7/1/2012)</i>		-3.1
<b>Estimated 7/1/2012 Unrestricted Reserve Fund Balance</b>		<b>4.5</b>