



Office of the City Manager

ACTION CALENDAR  
December 13, 2022

To: Honorable Mayor and Members of the City Council

From: Dee William-Ridley, City Manager

Submitted by: Sharon Friedrichsen, Budget Manager

Subject: Status Report - Berkeley's Financial Condition (FY 2012 – FY 2021):  
Pension Liabilities and Infrastructure Need Attention

INTRODUCTION

On May 24, 2022, the City Auditor submitted a Financial Condition audit report<sup>1</sup> to City Council with recommendations to build on the City's financial strengths in order to: (1) help address the City's unfunded capital and deferred maintenance needs and pension liabilities; (2) help the City prepare for unforeseen economic challenges by assessing the risk of the reserves, and ensuring that enterprise funds can balance and avoid recurring shortfalls and (3) to update the City's debt policy to help strengthen the City's ability to assess its general obligation debt capacity.

The purpose of this information item is to update City Council on the status of implementation of the audit report's recommendations. This is the first status report regarding this audit.

CURRENT SITUATION AND ITS EFFECTS

The City Auditor's report included five recommendations. As of the writing of this report, two recommendations have been partly implemented and three recommendations have been started. Please see Attachment 1 for a detailed table of audit report recommendations and implementation progress. The next status report to Council is expected to be presented on June 6, 2023.

BACKGROUND

The audit provides a high-level overview of the City's financial condition over 10 fiscal years. By broadening the scope of financial reporting to incorporate long-term financial trends, financial condition analysis can introduce long-term considerations into the

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<sup>1</sup> Audit-Berkeley's Financial Condition (FY 2012 - FY 2021): Pension Liabilities and Infrastructure Need Attention: <https://berkeleyca.gov/sites/default/files/documents/2022-05-24%20Item%2018%20Berkeley%E2%80%99s%20Financial%20Condition.pdf>

budgeting process, clarify the City's fiscal strengths and weaknesses, and help highlight financial risks that the City needs to address including its unfunded capital and pension liabilities.

ENVIRONMENTAL SUSTAINABILITY AND CLIMATE IMPACT

There are no identifiable environmental effects or opportunities associated with the subject of this report.

POSSIBLE FUTURE ACTION

The City Manager's Office will continue to work on implementing the various recommendations, including conducting a risk assessment of the General Fund reserve and developing recommendations regarding fund balance for the various enterprise funds. The Finance Department will continue to assess the debt capacity threshold and update the debt management policy. In addition, the City Manager's Office will continue to assess Council fiscal policies and make recommendations regarding long-term funding strategies to address the City's pension and capital infrastructure liabilities.

FISCAL IMPACTS OF POSSIBLE FUTURE ACTIONS

The audit recommendations are intended to build on the City's financial strengths and help mitigate risks associated with the City's unfunded liabilities.

CONTACT PERSON

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Attachments:

1. Audit Findings, Recommendations, and Status Updates

Audit Title: Berkeley's Financial Condition (FY 2012 - FY 2021): Pension Liabilities and Infrastructure Need Attention				
Finding	Recommendation	Issue Date	Department	Status of Audit Recommendations, Corrective Plan, and Progress Summary
The COVID-19 pandemic slowed the City's progress toward its 2027 reserve funding goal.	1.1 To better prepare the City for unforeseen economic challenges, we recommend that the City Manager complete the risk assessment required by the City's reserve policy as scheduled and propose to the City Council a plan to replenish the Stability and Catastrophic Reserves based on the results of the assessment. This may include revising the funding goal for 2027 to align with the City's financial reality and projected risk level.	5/5/2022	City Manager	<u>Started:</u> City staff are in the process of consulting with the Government Finance Officers Association (GFOA) for technical assistance with the risk assessment.
The COVID-19 pandemic slowed the City's progress toward its 2027 reserve funding goal.	1.2 To ensure the City's enterprise funds can balance and avoid recurring annual shortfalls, we recommend the City Manager assess the appropriate fund balance for each of the City's enterprise funds, report findings to the City Council and explore financial policy options to manage enterprise fund balances.	5/5/2022	City Manager	<u>Started:</u> City staff have started to conduct research and are forming a working group to discuss current approaches utilized by departments and best practices as the first step in developing fund balance policies.
The City's limit for general obligation bond debt is set at 15 percent of total assessed property value.	2.1 To strengthen the City's debt management, we recommend that the Finance Department update the Debt Management Policy. The Finance Department may consider revising its current general obligation bond threshold of 15 percent of assessed property value or building upon the City's existing general obligation bond debt limit by considering additional debt capacity factors such as debt per capita, debt to personal income, and/or debt service payments as a proportion of General Fund revenues.	5/5/2022	Finance	<u>Started:</u> the Finance Department is working on updating the debt management policy.
The City has taken steps to increase pension funding.	3.1 To maximize the benefit of the Section 115 Trust, we recommend that the City Manager present a plan for adoption by the City Council to assure sufficient contributions to the Trust. This may include taking the steps proposed by the Budget and Finance Committee to increase contributions to the Trust. It may also include a strategy to ensure that the City is able to meet its yearly contribution goals, such as allocating contributions at the beginning of the budget cycle.	5/5/2022	City Manager	<u>Partly Implemented:</u> The City budgeted funds for the Section 115 Trust and adopted fiscal policies to fund the Section 115 Trust as part of the FY 2023/24 biennial budget process. Staff will be working with an actuary to review the target goal and will continue to explore additional funding options for Council's consideration to increase contributions to the Trust.

<p>The City reported \$1.2 billion in unfunded capital and deferred maintenance needs in FY 2021.</p>	<p>4.1</p>	<p>To address rising costs for unmet capital needs, we recommend that the City Manager collaborate with the Department of Public Works to implement a funding plan aimed at 1) reducing the City's unfunded capital and deferred maintenance needs, and 2) ensuring regular maintenance of city assets to prevent excessive deferred maintenance costs in the future. This may include prioritizing capital assets that generate the highest deferred maintenance costs.</p>	<p>5/5/2022</p>	<p>City Manager</p>	<p><u>Partly Implemented</u>: The City has updated its fiscal policies to increase funding for unfunded capital and deferred maintenance needs.</p>
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