



STUDY SESSION MEMORANDUM

TO: Mayor and Members of City Council

FROM: Nuria Rivera-Vandermyde, City Manager
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DATE: May 24, 2022

SUBJECT: Financial Update & Budget Outlook

EXECUTIVE SUMMARY

Each spring staff provides an update to council presenting the prior years' ending financial results, current and forecast economic conditions, and a budget outlook for the current and following year. This memorandum includes an overview of the city's financials since the beginning of the pandemic, summaries related to year-end 2021, and implications for 2023 budget development. This memo also discusses the differences between emergency reserves, fund balance, and related policy considerations. Finally, an overview of 2023 budget development process improvements are provided.

Overall, strategies taken by the city in extremely uncertain times, combined with faster recovering revenue outpacing projections, have resulted in a positive financial position for the city entering 2022 and the 2023 budget development. The more positive local revenue picture has allowed the organization to focus on continued recovery of services and organizational capacity while investing in key community priorities and the city workforce. The strength of 2022 YTD revenues will allow staff to discuss risk posture for 2023 revenue projections and 2022 budget flexibility while appreciating global and national headwinds that may impact local economic activity.

Questions for Council

- Does council have any questions regarding the 2021 preliminary, unaudited 2021 year-end financial results and the General Fund emergency reserves and fund balance?
- Does council have any questions regarding the 2022/2023 budget outlook?

- Does council have any questions about the 2023 budget process improvements and Boulder OpenGov?

BACKGROUND

The development of the 2023 Budget will represent the third budget year impacted by the pandemic. Reaction to the global shutdown included immediate steps in 2020 and led to cautious budgeting approaches in the subsequent annual budgets. The 2023 budget will represent continued recovery from the pandemic with many revenue sources return to or above pre-pandemic levels. While the revenue forecasts will provide some optimism about organizational recovery, there are other economic constraints to consider, including high inflation, continued supply chain issues, and international conflict. Despite potential headwinds, staff believes the steps taken to invest in community priorities in 2022 and within the upcoming 2023 budget will represent a road to recovery in Boulder. Below is an overview of the conditions and strategies that underpin the previous budget developments.

2020 Budget

The COVID-19 pandemic started late 2019 and spread throughout the world including the U.S. and Colorado in February and March 2020. With goals of flattening the curve and protecting lives, city facility closures began March 13, 2020, and state and local stay-at-home orders followed the following week. This caused a shock to many of the city's revenue sources – some abruptly down to zero or nearly zero, others were expected to decline somewhat or significantly. At that time, staff expected nearly 70% of revenue sources would be impacted during 2020.

At the [March 31, 2020 City Council meeting](#), and at this early stage in the crisis, macroeconomic forecasts varied wildly. May 2020, staff contracted with the University of Colorado Business Research Division to develop sales and use tax econometric models to forecast city revenue for 2020-2024 based upon Moody's Analytics macroeconomic and regional forecast scenarios.

Staff provided council with additional monthly financial updates through the summer of 2020. Over that period revenue forecasts grew more pessimistic and then later more optimistic. In response to the significant revenue disruption and uncertainty, the city reduced 2020 expenditures by \$18.3 million or roughly 10.4% of the 2020 approved budget. The details of 2020 actual results are detailed in full in the [April 27, 2021 Financial Update](#).

2021 Budget

In October 2020, City Council approved the 2021 Budget, only 6 months into the pandemic, during a time of tremendous uncertainty and with a consistent council and staff perspective to be conservative or cautious about the timing and strength of recovery.

On April 27, 2021, staff provided a financial update that provided preliminary 2020 financial results, which were more positive than expected, and an outlook for 2021/2022

that projected 2021 revenue to exceed adopted 2021 budget. In May 2021, council approved the first adjustment to base (ATB1) included ongoing funding to address critical funding needs and to begin rebuilding staff capacity. In September 2021, council approved a special supplemental appropriation, appropriating the first tranche of American Rescue Plan Act funding and again appropriating funding from revenue that was projected to exceed budget to restore some services that were cut due to COVID-19 and budget reductions and to appropriate funding for a one-time restorative payment to current employees who took unpaid extended holiday furlough days in 2020.

The 2021 budget was a total annual budget of \$341,743,592 including a General Fund budget of \$146,937,662. Due to the significantly reduced 2021 budget, many restorations were provided in adjustments throughout the year. The first adjustment-to-base in May 2021 was a total of \$37,043,443, including \$7,088,297 in General Fund, and \$29,955,146 in restricted funds. The total special adjustment was \$7,917,624, including an initial ARPA allocation of \$3,977,000. A final adjustment was made in November, bringing the final revised 2021 budget to \$405,200,583.

2022 Budget

In October 2021, City Council approved the 2022 Budget. The city's approved 2022 all funds budget (excluding transfers/internal service funds) was \$462.5 million. This represented a \$120.8 million or 35% increase over the 2021 Approved Budget. The budget was comprised of an operating budget of \$300.1 million, which represents a 10% increase, a capital budget of \$162.4 million, which represents a 134% increase, compared to 2021. The capital budget increase was primarily due to anticipated bond proceeds from a Utilities bond issuance in 2022, at the time estimated at \$92.3 million. The 2022 budget added 58.5 FTE – 28 new positions and 30.5 reinstated positions and extended 18 fixed-term positions.

ANALYSIS

2021 Financial Update

Below is an update on:

1. Preliminary 2021 results for the city's major revenue sources
2. Preliminary 2021 results for the General Fund
3. Discussion and history of General Fund - fund balance

1. Major Revenue Sources

2021 Sales and Use Taxes

Sales and use tax revenues comprise over one-third of total city revenue and nearly half of total city revenue excluding utilities (which are not supported through taxes). The city monitors and tracks these revenues monthly and presents the results in a [monthly revenue report](#). Sales and use taxes provide revenue for the following funds: General Fund, 0.25 Cent Sales Tax Fund (Parks and Recreation), Open Space and Mountain Parks Fund, Transportation Fund and the Community, Culture, and Safety Fund.

YTD December 2021 sales tax revenue (including audit revenue and the additional 3.5% recreational marijuana tax) increased by \$19,720,235 (or 19.0%) when compared to YTD December 2020. This increase, while significant compared to YTD December 2020, results in a compound annual growth rate of 4.4% compared to 2019. Much of this growth in sales tax is attributable to the adoption of the Marketplace Facilitator ordinance in October 2020, which resulted in over \$3.5 million of new revenue in 2021.

Sales tax revenue for most sectors continues to show growth, led by: Apparel Stores (up 39.6%), Consumer Electronics (up 33.2%), General Retail (up 32.3%), and Eating Places (up 36.9%). Only three categories declined when compared to YTD December 2020: Food stores declined by 5.9%, Medical Marijuana declined by 34.5%, and Recreational Marijuana declined by 5.6%. Retail and dining nodes are still showing strong growth compared to last year: Pearl Street Mall increased 68.7%, Downtown increased 36.3%, 29th Street Mall increased 20.6%, and The Hill increased 18.6%.

Business and construction use tax revenue was actually down for 2021 – down 5% and 22% respectively. As was discussed in the 2021 Financial Update, one of the reasons 2020 results were more positive than expected was because of unusually strong business and construction use tax, this proved out to be a spike as 2021 revenue from those sources actually declined. Because the city budgets conservatively for these volatile revenue sources, actual revenue did exceed budget.

2021 Property Tax

2021 property tax collections came in very close to budget. Property tax as a percent of total General Fund revenue has increased, particularly over the past 10 years as property values have increased. This increase has resulted in a more diversified portfolio of revenue for the General Fund which helped stabilize that fund during this economic crisis.

2021 Accommodations Tax

The travel and tourism industry began to recover during 2021 and accommodations tax revenue was approximately \$6.4 million which was an increase of \$3.1 million or 94% from 2020 and above budget. It is important to note that even with that strong growth, revenue remained below the 2019 level of approximately \$8.8 million.

2021 Other Taxes

Other taxes include admissions tax up \$80,000 or 48%, food service tax up \$175,000 or 38%, short-term rental tax up \$588,000 or 103%, sugar sweetened beverage tax up \$314,000 or 8%, and recreation marijuana excise tax up \$321,000 or 31%.

2021 Parking Changes and Fees

On-street parking revenues were up 17.6% over 2020 actuals. However, 2021 on-street revenue was still down 43.6% from pre-pandemic levels in 2019. This could be due to a combination of changing commuting habits, semi-permanent street closures, and continuing recovery of tourism.

2021 Other Revenue

Other revenue includes many miscellaneous revenue types including grant revenue. The 2021 adopted budget included the appropriation of CARES funding of \$3.7 million. These funds were setup as a reimbursement and, as reimbursements have been approved and remitted, are booked as a revenue with approximately \$3 million in 2021 revenues.

2. General Fund

The General Fund is the primary operating fund of the City and is a governmental fund as defined by the Governmental Accounting Standards Board (GASB). The focus of the city's governmental funds financial statements is to provide information on near-term inflows, outflows and balances of resources that are available for spending at the end of the fiscal year (fund balances).

2021 General Fund Results

During 2021, revenue continued to recover and exceed forecasts used to build the adopted budget and, as such, Council approved service restorations throughout the year as noted in the Background section above. Despite the continued investments, 2021 actual expenditures fell below projections due to vacancy savings and capacity restrictions. Expenditure savings combined with more robust than expected sales tax performance led to an increase to fund balance of approximately \$16.1 million.

Table 1: 2019-2021 General Fund Results

	2019	2020	2021	2022
	Actual	Actual	Actual	Adopted
Beginning Fund Balance	\$64,250,248	\$50,842,985	\$41,148,788	\$39,609,665
Total Sources	\$158,651,344	\$148,112,727	\$169,977,940	\$166,602,129
Total Uses	\$172,058,607	\$157,806,924	\$153,852,447	\$164,657,129
Total Reserves	\$34,703,601	\$38,832,991	\$38,710,195	\$39,559,367
Ending Fund Balance After Reserves	\$16,139,384	\$2,315,796	\$18,564,084	\$1,995,295

3. General Fund – Fund Balance

The city's practice in the "fund financials" contained in the annual budget document is to reflect:

- Total fund balance
- All amounts reserved for a specific purpose including emergency reserves

- Ending fund balance after reserves

Emergency reserves are in place to address emergencies, unexpected one-time costs or to temporarily support essential city services when revenues decline as a result of a shock or during a recession. Recognizing the importance of holding adequate reserves, the city accumulated General Fund emergency reserves such that the Original 2020 Budget planned for emergency reserves of 19.5% of the ongoing expenditure budget or \$28.2 million. At that time, one percentage of ongoing expenditures equaled approximately \$1.4 million.

While the city has been focused on the amounts held in emergency reserves, the General Fund has carried an ending fund balance after all reserves (including emergency reserves) that is available for major projects or opportunistic expenditures. In recent years, this has been used for costs related to the deconstruction of the hospital at Alpine-Balsam and the relocation for Fire Station No. 3.

As staff reacted to the severe decline in revenue due to the COVID-19 induced business and government service closures, staff recommended as a one-time source of funding drawing down the ending fund balance after reserves and using a portion of the emergency reserves to support essential city services. Staff did not recommend drawing down the emergency reserves below 15% as the city continues to remain vulnerable to other disasters which could require the use of reserves and must hold minimum balances to maintain a strong bond rating.

Below are details on the recent history/trends of General Fund total fund balance, emergency reserves and ending fund balance after reserves and a brief description of why those balances have changed and how those actual changes differed from expectations particularly during the pandemic which was and continues to be an extremely uncertain economic environment.

Fund balance History 2016-2020 Original Budget

From 2016 to 2018, total fund balance increased, both the emergency reserves as part of the strategy to build reserves to 20% by 2020 and total fund balance including fund balance after reserves to accumulate funds for projects or opportunistic investments. At the end of 2018, total fund balance was \$64.3 million including \$26.3 million in emergency reserves (18.3%), \$15.0 million in restricted reserves and \$23.0 million in ending fund balance after reserves.

In 2019, the city drew down ending fund balance after reserves by \$13.4 million, which was largely a planned draw of \$12.0 million toward deconstruction of the hospital at Alpine-Balsam and \$1.5 million toward the relocation/construction of Fire Station No. 3. At the end of 2019 total fund balance was \$50.8 million including \$25.6 million in emergency reserves (19%), \$15.0 million in restricted reserves and \$10.3 million in ending fund balance after reserves.

The original 2020 budget included an additional planned draw from ending fund balance after reserves of \$4.1 million - additional funding for the deconstruction of the hospital but planned emergency reserves of \$28.2 million (19.5%).

Table 2: General Fund - Fund Balances: 2016-2019 Actual & 2020 Original Budget

	2016 Actual	2017 Actual	2018 Actual	2019 Actual	2020 Original Budget
Emergency Reserves	\$220,925,806	\$24,754,628	\$26,279,201	\$25,614,678	\$28,197,573
Restricted Reserves	10,804,609,	15,144,599	14,949,144	14,973,923	10,185,233
Ending Fund Balance after Reserves	26,141,775	16,684,299	23,021,903	\$10,254,384	8,352,889
Total Ending Fund Balance	\$57,872,190	\$56,583,526	\$64,250,248	\$50,842,985	\$46,735,695
Emergency Reserves a % of Ongoing Expenditure Budget	16.2%	17.0%	18.0%	19.0%	19.5%

2020 Expenditure Saving Measures

With the sharp decline in revenue and extraordinary uncertainty, the city took action to swiftly reduce expenditures. During 2020, many of the expenditure savings actions were one time and included hiring holds on standard, nonessential vacant positions, delayed or cancelled hiring of seasonal and temporary positions, furloughs and layoffs of seasonal, temporary and standard staff, postponed capital/operating projects, six extended holiday furlough days (excluding emergency responders in Fire, Police and OSMP Rangers), and other one-time budget reductions.

Of the personnel expenditure savings strategies, many of the furloughs were related to facility closures or program/service suspensions. The staffing reductions included the following:

Standard employees:

- 56 layoffs including 7 that were in fixed-term positions that ended early
- 121 furloughs over 4 furlough periods between April 20 and September 20, 2020
- 103 vacancy holds
- 6 unpaid holiday closure furlough - all employees (except for emergency personnel in Fire, Police, OSMP Rangers). The salary lost was repaid to affected employees in 2021.

Non-standard (Seasonal, temporary or intern staff):

- 68 terminations
- 472 furloughs

Even with significant staff and service reductions (some reduced due to public health restrictions) staff projected a draw from fund balance of nearly \$19.8 million, drawing the ending fund balance after reserves to zero and drawing down emergency reserves by nearly \$4.5 million. However, the actual 2020 draw from fund balance of \$9.7 million

was less than expected because a number of revenue sources exceeded expectations including retail sales tax, construction use tax, business use tax and motor vehicle use tax.

2021 Fund Balance

As noted above, despite the continued investments, 2021 actual expenditures fell below projections due to vacancy savings and capacity restrictions. Expenditure savings combined with more robust than expected sales tax performance led to an increase to fund balance of approximately \$16.1 million.

Table 3: 2019-2021 General Fund - Fund Balances

	2019 Actual	2020 Original Budget	2020 Projected	2020 Actual	2021 Actual
Emergency Reserves	\$25,614,678	\$28,197,573	\$23,080,397	\$26,992,234	\$30,338,443
Restricted Reserves	14,973,923	10,185,233	7,925,520	11,840,757	7,273,251
Ending Fund Balance after Reserves	\$10,254,384	8,352,889	-	2,315,796	19,662,585
Total Ending Fund Balance	\$50,842,985	\$46,735,695	\$31,005,917	\$41,148,788	\$57,274,281
Emergency Reserves a % of Ongoing Expenditure Budget	19.0%	19.5%	15.8%	19.5%	19.5%

2022 & 2023 Budget Outlook

Economic Outlook

The economic outlook for the nation and the state has improved and the consensus forecast is for robust economic growth for 2021. The city contracted with the University of Colorado Business Research Division to forecast sales and use taxes and its forecast uses Moody's Analytics U.S. Macroeconomic Outlook forecasts for model inputs. For the current forecast, CU recommends using Moody's Scenario 2 forecast which is more conservative than the Baseline forecast. The Scenario 2 forecast assumes continued disruption from the COVID-19 pandemic, including continued supply chain issues, decline in stock prices, and increased inflation while accounting for a strong labor market, continued influence of federal investments, and larger personal savings driving strong consumer spending.

2022/2023 Major Revenue Sources Outlook

Significant revenue sources impacting the General Fund are retail sales tax, property tax and accommodations tax. Below is the current outlook for those sources.

Retail Sales Tax

There is a lag to receiving sales and use tax. These taxes that were paid by customers in March were due to the city by the vendor on April 20, then processed by the finance

department in the following weeks, with a revenue report released in May. The March 2022 Revenue Report is not available at the time of printing of this memo, but results will be incorporated into the May 24 presentation.

The most recent CU econometric model forecasts that 2022 retail sales tax revenue will be above the 2022 budget. The forecast range that staff has focused on is the medium (or most likely result) and the average of the medium and low (the low being one standard deviation below the medium). That range shows 2022 retail sales tax revenue could exceed the 2022 budget by \$3.5 to \$7.8 million and 2023 retail sales tax revenue could exceed the 2022 budget by \$8.5 to \$13.8 million.

Property Tax

2021 was a property reassessment year which impacts the 2022 and 2023 budget years. The 2021 property reassessment is based upon home sales from July 1, 2018, to June 30, 2020 with sales during that period age-adjusted to the June 30, 2020 appraisal date. Property taxes are collected in arrears so 2021 property taxes that are based upon the 2021 reassessment are paid and collected in 2022.

For 2022, the final abstract of assessment, total assessed values in the city are up 5.5%, with residential values increasing 12% and non-residential values increasing 1.0%. The final assessment was not significantly different than the preliminary assessment, upon which the 2022 budget was based, so we expect property tax revenue to be on track with budget.

For 2023 (and 2024), per SB21-293, there is a temporary reduction to the assessment rates for property classified as agricultural, renewable energy production, and residential. In off property reassessment years, staff assumes total assessed value will increase approximately 2% due to production including rehabilitation. That assumed increase, combined with the decrease in assessment rates for those classifications of property, staff is projecting an overall 0.5% increase in property tax revenue.

Accommodations Tax

The updated 2022 budget for accommodations tax is approximately \$7.0 million which is \$600,000 or 9% more than 2021 actual revenue. Preliminary information from the Boulder Convention and Visitors' Bureau indicates that overall, 2022 YTD occupancy is down approximately 5% from pre-pandemic level, but the average daily rate is up approximately 13% YTD over 2021. While confidence is still strong that occupancy levels will continue to rise towards pre-pandemic levels, there are a number of factors that are being monitored closely. Consumer pessimism related to inflation, especially travel prices, is growing and could have an impact on summer travel plans and local occupancy. BCVB is working towards a more comprehensive forecast in the coming months and will be shared out once developed.

Continued Organizational and Community Recovery

The revised 2022 budget projections include the two supplemental appropriations, the special adjustment in March and the proposed adjustment in May. With additional

expenditures and revenues, the revised projected ending fund balance for 2022 is \$13,801,173. The 2023 Recommended Budget (currently in development) will consider one-time and ongoing expenses to meet community needs and Council priorities and will reflect the opportunities related to the ending fund balance and potential investments with federal American Rescue Plan Act dollars (not included in the General Fund figures above). Council will review the 2023 Recommended Budget at a study session in September.

2023 Budget Process Improvements and Boulder OpenGov

A point of emphasis over the past several months has been to analyze and improve the overall budget process. In 2018, the city received a Department of Local Affairs grant to improve resilience through budgeting. The city retained a consultant to develop a framework to overhaul the budget process. The report, titled Budgeting for Community Resilience, provided several recommendations to improve the budget process with a focus on embedding measurements, or key performance indicators, within the budgeting process and budget performance analysis. The organization was able to partially implement some of the strategies; however, due to the pandemic many of the recommendations were set aside.

Staff has been working on a new budgeting process to fully implement the recommendations in the report and to adapt the recommendations to current organizational resources and needs in alignment with an overall direction towards more organizational strategic planning. There are four main elements of budget process improvements for 2023:

- Improved strategic decision-making
- Greater focus on outcomes of funding
- Greater organizational alignment
- Better transparency and accessibility

One key challenge was to adapt the strategy to the current organizational reality. It is important to note that the organization has budgeted in a certain way for a long period of time, so any change was likely to be resource intensive. The city has traditionally budgeted at the department level and made decisions aligned with department goals or master plans that may or may not be in alignment or prioritized in the context of other citywide goals. The previous budget process was also set up to only consider the budget requests or the incremental cost of adding to the base budget. This setup a process where executive budget team members were not given contextual information to make decisions and departments were not provided with adequate feedback during the process.

The changes made throughout the 2023 budget development process reflect a desire to become more oriented around citywide goals and the Sustainability, Equity and Resilience Framework, to better articulate our budget in terms of programs and projects and begin to develop how we measure success in terms of our intended outcomes. The first step that the organization took to improve our process was to first align our investments by programs. This alignment allowed us to inventory the various ways we

were investing our operating dollars and provided greater insight into the purpose of our investments by department and across departments. for the 2023 budget development, departments have been instructed to budget at their program level and provide detailed information on how the proposal influences the intended outcomes of the program in alignment and consideration of citywide goals, especially our racial equity and climate action goals.

Another major challenge in process improvement was the limitations of current budgeting software as a vehicle for transparency and accessibility and capability to provide city staff with a modern way to ensure best budgeting practices. To solve this challenge, the city purchased a new software, called OpenGov, which is an industry-leading budgeting software to assist with these process improvements. The city's entire 2023 budget and 2023-2028 capital improvements program is being developed within our new Boulder OpenGov platform.

An additional and equally important component of the process improvement is to improve the transparency and interaction of our annual budget creation within our community. While staff is extremely excited about the capability in terms of budget development, one of the best features of the software is the accessibility of information for council and the community. OpenGov has the ability to provide visualization of the recommended 2023 budget by program and project, and also provide historical and current year actual budget performance information in an easy-to-use online platform. This will greatly enhance the ability for public engagement in the budget process by making the information accessible and engaging. Additional engagement opportunities will be explored with OpenGov in the future as we continue to improve the city's budgeting process.

Staff is preparing for this budgeting improvement as a three-year project. While significant steps taken this year to improve, the process to accurately measure our intended outcomes and understand the true community impact of all our investments will continue over the next two or three budget cycles. Council is familiar with the organizational need for clear and centralized data collection and analysis especially as it relates to our equity goals. The work to modernize our data practices will coincide with and enhance our efforts to improve how we budget and hopefully the impact of our investments.

NEXT STEPS

- 2023 Budget Study Session - September 8
- Adoption of the 2023 Budget, first reading on October 6, second reading on October 20.