Written materials relating to an item on this agenda that are distributed to the legislative bodies within 24 hours before the item is to be considered at this special meeting will be made available for public inspection at the Library, 251 South "A" Street and the City Clerk's Office, 300 West Third Street, 4th Floor, during customary business hours. Any materials to be presented at this meeting will be made available electronically 24 hours prior to the meeting, at the end of this agenda. The agenda reports are on the City of Oxnard web site at www.oxnard.org.

CITY OF OXNARD CALIFORNIA

AGENDA

OXNARD CITY COUNCIL
Special Meeting
City Council Chambers, 305 West Third Street, Oxnard
October 27, 2016
5:00 P.M.

A. ROLL CALL/POSTING OF AGENDA

B. PUBLIC COMMENTS ON REPORTS

At this time, a person may address the legislative body only on matters appearing on Reports section of the agenda. The presiding officer shall limit public comments to three minutes.

C. REPORTS

FINANCE DEPARTMENT

1. SUBJECT: First Quarterly Financial Review: 10 Year Forecast and Status of Bond Rating, Letter of Credit, and Quality Control Review Report from State Controller's Office
   RECOMMENDATION: Receive and file an update to the City's 10-year financial forecast, State Controller's Report on its quality control review of the FY2014-15 external audit, a briefing on the City's current bond rating from S&P, discussion on the Letter of Credit (LOC) status with Union Bank, and the current situation with the City's failure to meet bond covenants related to debt coverage.
   Legislative Body: CC Contact Jim Throop Phone: 385-7475

D. ADJOURNMENT

In compliance with the Americans with Disabilities Act, if you require special assistance to participate in a meeting, please contact the City Clerk's Office at 385-7803. Notice at least 24 hours prior to the meeting will enable the City to reasonably arrange for your accessibility to the meeting.

City of Oxnard internet address: www.oxnard.org

CITY OF OXNARD CALIFORNIA	CITY COUNCIL AGENDA REPORT	TYPE OF ITEM: Report AGENDA ITEM NO.: 1

DATE: October 27, 2016

TO: City Council

THROUGH: Greg Nyhoff
City Manager

FROM: Jim Throop
Interim Chief Financial Officer

SUBJECT: First Quarterly Financial Review: 10 Year Forecast and Status of Bond Rating, Letter of Credit, and Quality Control Review Report from State Controller's Office

CONTACT: Jim Throop, Interim Chief Financial Officer
Jim.Throop@oxnard.org,

RECOMMENDATION:

Receive and file an update to the City's 10-year financial forecast, State Controller's Report on its quality control review of the FY2014-15 external audit, a briefing on the City's current bond rating from S&P, discussion on the Letter of Credit (LOC) status with Union Bank, and the current situation with the City's failure to meet bond covenants related to debt coverage.

BACKGROUND

Financial Systems and Compliance

This report includes information about important past, present, and future City financial issues. During the last two years, the City Council considered the issues related to finance that needed immediate review and action. In 2015, following turnover of senior accounting positions in the Finance Department, staff and subject matter experts working with the City identified significant problems with the City's compliance with laws regarding the pension tax override (known as the Carman Override), development impact fees and maintenance assessment districts. Other compliance issues relating to payroll and benefits for limited benefit employees were identified as well.

As the City's Fiscal Year 2015-16 budget was adopted in June 2015, estimated revenues were affected by overpayments of sales tax by the State, as well as continuing slow sales and property tax growth. In August 2015, the City's then new Chief Financial Officer identified more compliance issues, this time relating to storm water expenditures charged to the Wastewater fund.

The City's compliance issues required use of unspent Measure "O" funds to replenish deficit cash balances in multiple restricted funds. This use of Measure "O" funds resulted because use of the General Fund reserves would deplete the cash resources to a dangerously low level.

The discovery of compliance issues that had existed for years, inadequate accounting records, and the tepid economic recovery required a conservative approach to the budget. In addition, the end of the State's Triple Flip financing scheme, material overpayments of sales taxes by the State and County, which is to be repaid in the next two years, compounded budget expectations.

In addition, after the 2015 fiscal year was closed, the independent auditor, through initial audit field work on the Fiscal 2014-15 financial statements, identified a number of problem areas in the City's financial accounting systems including cash reconciliation, capital assets, year-end closing of Fiscal 2014, and reconciliation practices. Problems identified required significant subject matter expert support because of inadequate staffing and turnover in the Finance Department. During this effort, the City's Chief Financial Officer left City employment, and an unplanned leave sidelined the Budget Manager, which required subject matter experts and new staff with extensive budget experience in other agencies to lead the Fiscal Year 2016 budget effort.

The Fiscal Year budget 2016 was improved to reduce estimation risk by using professional subject matter expert services to analyze and estimate property and sales tax. Based on updated data in late April 2016, experts determined that property tax revenue estimates should be adjusted upward, staff asked a second subject matter expert to provide its own estimation. The second estimate supported the original estimate. Rapid improvement in AB 8 adjustments for property tax by the County, a strong real estate market, and new development combined to improve the forecast. Sales tax improved despite significant price reductions in gasoline. Staff also used independent estimates for sales tax and retirement costs to improve the accuracy of the forecasts. This more rigorous approach and improving economy, improved vacancy savings estimates, and stable estimates of employee compensation costs accounts for changes between the May 2015 five-year forecast and the current 10-year forecast.

The FY 2014-15 financial audit confirmed that there were structural budget imbalances and issues with the City's financial condition, reporting, and internal controls. The auditors' description of these issues prompted staff and the City Council to prioritize the process to correct past practices and create a stable financial base to plan for the future.

The challenges presented to the Council included the 111 audit findings, and 128 organizational assessment items identified by subject matter experts. Other ongoing studies related to the maintenance districts, cost allocation and fees, will most likely result in additional recommendations to Council. These sets of issues will take time to solve as many of the findings will require a review, updating of policies/procedures, and the training of city staff on these new policies. The effort to address these concerns is urgently important, but so complex that a rapid solution is not available. Staff plans to implement solutions based on the materiality and risks posed by each issue.

Financial Condition Problems

There is extreme concern involving the financial solvency for the Water and Wastewater funds. The recent studies of these two funds show that the user rates need to be adjusted in order to stabilize these funds. Without the new rate structure in place, these funds are forecast to be in a negative cash position within this current fiscal year. Funding would need to be provided by the General Fund to ensure public health and safety is maintained.

In addition, the Council and staff must work on new banking relationships for the Letter of Credit that is necessary to meet its debt/bond requirements for the Water and Wastewater funds. Without this letter of credit, there is a potential for immediate repayment of the outstanding debt, which could equate to $20 million for the Wastewater Fund. Given that the Wastewater fund has only a few months of cash on-hand for operations, funds for repayment would need to come from the General Fund, which is also in a stressed financial condition.

These challenges are not insurmountable, but will require continuous monitoring of the City's finances and continued work on correcting the audit and operational review findings in order to become financially stable.

Single Audit Findings

The City received the single-audit from the City's auditors, Edie & Payne, which listed 111 audit findings. These audit findings pertained to internal controls, policies & procedures, staffing levels, finance system deficiencies, management oversight, staff training, and more.

During this period of time, the SCO notified the City and the audit firm that there would a review of the audit papers and a peer review of the audit firm to ensure that all proper auditing guidelines were followed.

The City recently received written notification from the SCO that it had completed its review of both the City audit and the peer review for the audit firm and that it was in agreement with the findings and was closing its review. The SCO did request follow-up reports from the City on its progress in completing the work on the audit findings, both at six-month and one-year intervals.

Bond Rating, Letter of Credit, & Bond Insurer

The City was recently re-evaluated by the bond rating agency Standard & Poor's. The outcome of the rating moved the City in a positive manner. The rating for the City moved from an "A+ Negative" outlook to an "A+ Stable" outlook. This is a positive step forward for the City, as the rating agency took notice of the many management and financial changes that have been taking place in the City and continue to be made going forward.

Some of the noted changes from S&P were the stabilization of General funds, together with the ratification of labor contracts, and strong budgetary flexibility.

The Letter of Credit (LOC), currently with Union Bank/MUFG is in a situation such that the Bank would like to end its current relationship with the City. The City was currently granted a 90-day LOC extension, which will take the City to February 2017. The City's Financial Advisor is currently searching for a new bank to carry the LOC.

This change in relationship with Union Bank/MUFG could have negative potential financial issues for the City. Should the bank decide to not re-new or grant an extension in February, this would trigger a default situation and all $16.5M in bonds would be due immediately. In addition, should the swap holder, RBC, elect to terminate the agreement due to the lack of a LOC, there is a "make-whole" section in the agreement, such that the City would need to pay an additional $4M in lost interest payments to RBC.

In order to avoid the devastating financial situation, it is critical to improve the financial standing of the Wastewater fund, such that Union Bank would continue with the LOC, or the City must quickly find a replacement bank to back the LOC.

Forecast

The 10-year forecast is designed to provide transparency, fiscal discipline, 'forward-thinking', early warning, alternative outcomes, and in turn, use the forecast to recommend policies and corrective actions for Council.

The forecast covers a range of issues from a possible recession, inflationary factors, rising costs - including salaries/benefits, staffing levels, and more.

The forecast currently presents a favorable outcome at year 10 due to the recent adoption of the four MOUs by City Council. This is savings is due to city employees picking additional PERS pension costs. It is recommended that the remaining MOUs be negotiated quickly so that the new agreements may be combined into the forecast.

Two of the main revenue streams, Property tax and Sales tax, are forecasted to show positive growth throughout most the forecast period. There is a possibility shown in the forecast of a modest recession in FY2018-19.

In order to continue with the process of keeping a balanced budget, the remaining MOU negotiations will need to be completed, development of a plan to improve the financial performance of the PACC and Golf Course, and an analysis and re-organization for the LMDs.

In addition, this forecast should be updated annually, along with mid-year or quarterly budget status reports to City Council, and City Management.

STRATEGIC PRIORITIES

This agenda item supports the Organizational Effectiveness strategy. The purpose of the Organizational Effectiveness strategy is to strengthen and stabilize the organizational foundation of the City in the areas of Finance, Information Technology, and Human Resources, and to improve workforce quality while increasing transparency to the public. This item supports the following goals and objectives:

Goal 1. To help foster a healthy and accountable corporate foundation by strengthening the support functions of the organization, which include Finance, Information Technology and Human Resources.

Goal 2. Increase transparency with Council, community and staff related to the City's budget and financial management processes.

FINANCIAL IMPACT

There are no financial impacts in receiving and filing this report.