


CITY OF LOS ANGELES
INTER-DEPARTMENTAL CORRESPONDENCE

Date: *January 29, 2010*

To: The Honorable Mayor Antonio Villaraigosa
The Honorable Members of the City Council

From: Miguel Santana, City Administrative Officer 

Subject: **MID-YEAR FINANCIAL STATUS REPORT AND THREE-YEAR PLAN TO FISCAL SUSTAINABILITY**

The City is facing a budget crisis unlike any crisis that it has ever experienced. The recession which began in 2008 caused deeper revenue declines than any post-World War II recession. The recession was much deeper than anticipated in the budget and has greatly affected the majority of the City's revenue categories. Receipts are now projected to be \$110.6 million below the prior estimate for a total of \$185.6 million. We are seeing distress in almost every revenue category including property, sales, utility, business, and hotel taxes. In the recession of the early 1990s, it took five years for the major taxes to return to the pre-recession level and it took nine years for the City's most economy-sensitive revenue, the sales tax, to fully recover. This lag is because rising employment and higher consumer spending trail economic recovery and actual City receipt of tax revenue lags consumer spending. Simply stated, local government revenue cannot recover from a severe recession until well after the recession ends.

Accounting for the revenue shortfall, the overall projected deficit is now \$208.5 million. Mitigating measures such as position reductions, contract reductions of 10%, sweeping all available funds and other measures are proposed to reduce the deficit. However even with adoption of these mitigation efforts, the City will have to dip into the Reserve Fund to offset the remainder of the deficit. We anticipate that the Reserve Fund balance will grow to \$232 million although after offsetting the deficit, the balance at year-end would only be approximately \$24 million; far short of the City's goal of maintaining a five percent Reserve Fund balance.

The enormity of our current fiscal crisis forces the City to take swift action now and lay out a financial plan for the future. The January 20, 2010 letter from the Mayor and Council leadership instructed my Office to take appropriate steps in confronting the crisis and laid out three major goals:

- Balancing the budget in the current Fiscal Year;
- Strengthening the City's credit rating; and
- Restoring the City's long-term fiscal health and sustainability.

Immediate steps must be taken to achieve these goals in a meaningful way. Attached to this cover memorandum, are the Mid-Year Financial Status Report and the Three-Year Plan to Fiscal Sustainability. These documents provide an update of the City's current

financial position, steps needed to address the budget deficit and the goals outlined above, and provide a financial and policy roadmap for the next three years. Recommendations are provided that will be difficult to consider, much less approve. However, postponing approval of these recommendations or alternative solutions with tangible savings will continue to negatively impact the City's financial position and increasingly jeopardize its long-term fiscal health and sustainability.

It should be noted that that my Office has reopened dialogue with the City's labor partners and have communicated with them that the revenue threshold in the agreements has been triggered along with the City's election to maintain budget flexibility by effectuating the furlough and layoffs provision(s) of the labor agreements for this fiscal year. The Financial Status Report triggers the re-opener language for 2010-11.

Contained within the Financial Status Report are recommendations to eliminate 1,000 General Fund positions within the next three to six months. Although it should be noted that Executive Employee Relations Committee has directed my Office to identify an additional 500 position reductions. Five basic criteria were used to determine the layoff target for each department. These criteria excluded positions based on core functions and services:

- 100% Revenue generating positions
- 100% Non-General Fund positions
- Legally mandated functions
- Positions needed to protect the public's health and safety
- Positions needed to keep critical City operations intact

In order to achieve this target, the Personnel Department and all affected departments must begin the layoff process immediately. To the extent possible, employees facing immediate displacement will be placed into vacant special-funded position authorities to minimize the number of resulting job loses from the layoff process. It is estimated that the annual direct salary savings from the 1,000 position reduction would be approximately \$65 million. There is a financial and human cost for each day of delay. The daily cost of postponing 1,000 layoffs is approximately \$338,000, which equals four more positions that need to be eliminated to generate the targeted savings. Any position removed from the 1,000 list must be replaced with an equal number in another department.

The Three-Year Plan to Fiscal Sustainability addresses the immediate and long-term outlook of the City's fiscal situation. Four strategies have been developed that encompass various strategies in restoring the City's fiscal health. These strategies include workforce modernization, public-private partnerships, focus on core mission and responsible financial management. These strategies and the initiatives behind them are explained in the Plan. Without adoption of the strategies and related solutions, the City risks further deterioration of its financial situation and the services that are provide to its constituents.