



Understanding a Municipality's Fiscal Health

Understanding a City's financial health is as complex as it is important. Public financing and required reporting procedures are governed by state, local law and in some cases, federal law. Municipal finance can be difficult to understand and easy to misinterpret. However, a careful review of official documents and resources will help you navigate the basics of public financing.

Where to Look

The City of Brea is a fiscally conservative municipality. The City adopts a balanced budget every fiscal year. The City maintains healthy General Fund Reserves. In Brea, all of the Budget documents and related reports, such as Comprehensive Annual Financial Report CAFR, are readily available online.

[General Operating Fund Budget](#)

The General Fund Budget reports City operating revenues and expenditures. The General Fund provides the resources necessary to sustain the day-to-day activities and pays for all administrative and operating costs. It is required that General Fund Revenues exceed Expenditures. The Brea City Council requires that a minimum of 8-10% of the Operating Budget be held in Reserves.

[Capital Improvement Program \(CIP\)](#)

The CIP is a seven-year plan that identifies capital projects and equipment purchases, provides a planning schedule and identifies options for financing the plan.

[Comprehensive Annual Financial Report \(CAFR\)](#)

The CAFR is published once a year and is a set of financial statements that comply with the accounting requirements established by the Governmental Accounting Standards Board (GASB). The report is subject to review by the city's auditors to ensure that it is prepared in accordance with generally accepted accounting principles and that the amounts and disclosures are fairly presented in all material respects. The City Council receives and files the CAFR annually.

Evaluating a City's Fiscal Health

- **The CAFR**—The City's Fund Financial Statement which shows the balance sheet of governmental funds is contained in the CAFR. This document is the most accurate way to measure fiscal health. Brea's CAFR contains audited financial statements and a statistical section, as well as City management's discussion and analysis of the fiscal year reported.

- **A City's fiscal health is evaluated annually by bond agencies**, such as Standard & Poor's and Moody's. Their review is thorough and exacting. Bond agencies look at the level of debt. They look at the credit quality of the issuer; their ability and willingness to pay what they've promised. Agencies also study a city's economic base to analyze the economic future. They review its financial structure and how the place operates. Is it paying its bills? Meeting payroll? Paving the streets? Brea's Bond Rating is AA.

Indicators of a City's Fiscal Health include:

- Balanced General Fund Budget.
- Strong General Fund Reserve Fund.
- Ability to meet all financial obligations on time.
- Making required pension contributions on time.
- Public service levels meet or exceed standards of the community.
- Meets recognized standards of financial reporting determined by the Government Finance Officers Association (GFOA) and the Government Accounting Standards Board (GASB).*

What about Brea's Fiscal Health?

Brea is able to check of all of these indicators listed for good municipal fiscal health.

- ✓ Yes, Brea always balances its Budget.
- ✓ Brea maintains a strong General Fund Reserve Fund greater than the dictates of the City Council Policy.
- ✓ Brea meets all financial obligations on time.
- ✓ Brea makes regular pension fund contributions, and in fact, has the funds to make the required unfunded liability annual payment early in order to realize savings. (The savings for Fiscal Year 2018/19 is approximately \$270,000.)
- ✓ In addition, Brea is saving funds to offset the Pension Unfunded Liability.
- ✓ Brea offers enhanced public service levels that consistently meet or exceed standards of the community.
- ✓ Brea meets the standards of financial reporting and has earned achievement awards from the Government Finance Officers Association for excellence in financial reporting.

About the Pension Reform

- Like many California Cities, the City of Brea is a member of the CalPERS pension fund. CalPERS is the nation's largest public pension fund. California cities are facing a rising pension costs due to a number of factors including lower than expected returns, and catch up from the Great Recession increased longevity of retirees, and fewer new employees (as compared to the Baby Boomers) paying into the system.
- Pension reform has been identified as a top priorities by the Brea City Council.
- As this issue is impacting cities statewide, significant, long-term solutions must come from the State Legislature in Sacramento. Still, cities must do their part and stay on top of it. Brea officials are completely aware of the issue and are addressing it at the local, regional and state levels.

- There are no easy solutions to the Pension reform, as it is a complex issue, which makes it easy for the media and others to misunderstand the process.

Following are some important facts to keep in mind:

- The City of Brea makes bi-weekly payments to CalPERS for all active PERS employees. They are budgeted and accounted for in the General Fund budget.
- Brea also makes an annual contribution to CalPERS toward paying down the Unfunded Pension Liability.
- In addition, City Council in FY 2015-2016 set aside \$6 Million in a *Section 115 Irrevocable Pension Trust Fund*, under separate investment management, to be used as necessary to meet our pension obligations and is an asset on our balance. These funds have grown to approximately \$7.4 Million.
- A City's Unfunded Pension Liability refers to the total cost for future benefits that will be paid out through the retirement of the vested CalPERS employee, less the amount of assets held by CalPERS for these benefits. This obligation is meant to be paid regularly, over time similar to paying making a monthly mortgage payment to pay down the home loan debt.
- A City's Unfunded Pension Liability is sometimes used by the media to imply that Brea, and other cities, are not fiscally prudent, or are close to financial crisis. This is an unfair and inaccurate characterization for the City of Brea. Pension costs are definitely an important issue and one that Brea takes very seriously and as previously stated, is taking steps at the local and state level to address the issue.
- Cities that choose to have their own Fire and Police Departments, (like Brea) will show a larger pension liability than contract cities. (Cities that contract out its fire, police and/or other city services to another agency or county, do not carry the liability on the city's books.)
- The pension liability for contract cities is reported on the "contractor's" balance sheets. For example, if a city contracts for fire services with the Orange County Fire Authority, (OCFA), the pension liability will be carried on OCFA's financial records.
- These reasons are why using the Unfunded Pension Liability number, without the proper context and understanding can be confusing and misleading.

Pitfalls to Avoid When Reviewing City Financial Records

- **Taking budget numbers out of context.** A budget is a multi-faceted document and must be understood in the proper context. For example, as mentioned in the section above, "Pension Liability" is an often misused term. Likewise, a guest media opinion columnist erroneously used Cities' "Unrestricted Net Position" from the CAFR and divided it by the city's population and then ranked OC cities in an attempt to imply that the larger the negative per capita number is, the more financial trouble the city is facing. This was a disservice to the readers in a number of ways:

- Comparing cities in Orange County is like comparing apples to oranges. The County is made up of contract cities, full-service cities, general law and charter cities, which makes a difference in how finances are reported among many other things. Additionally, the level of service and quality of life differs greatly among the cities.
- The Unrestricted Net Position figure from the CAFR he refers to includes costs for governmental activities including net pension obligations for full-service cities. Contract cities do not report their pension obligations in the CAFR, therefore such comparisons are not accurate.
- Additionally, the per capita number he quotes for Brea does not reflect our service level of the larger population we serve during the day. The City of Brea has a population of 43,000+. However, it serves a population of over 100,000 people who come to work, and recreate.
- A city's Fund Financial Statement balance sheet is a better, more accurate way to measure fiscal health as it details all of a city's available funds: cash, investments and reserves.
- **Comparing the balance sheets of full-service cities to full or partial contract cities.** This is a mistake that the media often makes. Full-service Cities and contract cities differ greatly in how their revenues and expenditures are reported.
 - For example, a full-service City, like Brea, carries the pension liability on their financial records per GASB* 68. However, a contract City, who contracts with the county for Police and/or Fire services for instance, does not carry its pension liability for its police and/or fire services on its financial records. That figure is in the County's records.
 - Additionally, cities have different service levels and standards based on Community needs and desires. Comparing cities balance sheets without taking this into consideration, will not yield accurate results.
- **Relying on unofficial sources such as media soundbites, rumors, blogs or social media** in in order to understand complex municipal issues. For official information visit the *CityofBrea.net*.

*GASB—Government Accounting Standards Board. The Governmental Accounting Standards Board is the source of generally accepted accounting principles used by state and local governments in the United States. GASB 68 refers to accounting and financial reporting requirements on pensions.