



## Legislation Text

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### CITY COUNCIL AGENDA ITEM

#### **ACTION REQUESTED:**

Receive the September 2020 Financial Report

**DEPARTMENT:** Finance Department

**SUBMITTED BY:** Rachel Mayer, Finance Director

#### **BOARD/COMMISSION REVIEW:**

N/A

#### **BACKGROUND:**

The City, region, and nation continue to experience the ongoing economic effects of the COVID-19 pandemic that began in mid-March. To provide current data in order to make strategic financial decisions at the appropriate time, staff is presenting a financial report to the City Council at its second meeting of each month.

In August, Council approved the temporary removal of use restrictions on Food and Beverage and Home Rule Sales Tax revenues to move towards the goal of financial flexibility through 2020 and 2021. This followed Council direction to staff in July to develop actions as necessary to further the goal of financial flexibility and maintaining core services at current levels.

#### **DISCUSSION:**

##### ***New Information***

Ongoing developments continue to shape the pandemic's financial impact on the City. Since the August 18 Council meeting, the following new events occurred:

- **Will County mitigation measures required:** A COVID-19 positivity rate exceeding 8% for three consecutive days triggered additional state-mandated mitigation measures for Region 7, which includes the Will County portion of Naperville. The additional measures include the rollback of indoor restaurant and bar service and limiting gatherings to 25 people. These additional measures initially took effect on August 26 for 14 days; as of September 10, although the positivity rate has decreased, it does not meet the threshold to rollback the additional mitigation measures, which will continue to be in effect.
- **Electric cost increasing:** The Electric Utility is experiencing higher than budgeted power costs from the Illinois Municipal Electric Agency (IMEA) as electricity consumption across the agency is down and fixed costs are being spread over a lower number of kilowatt-hours. Revenue to fund this increase has been collected through the Purchased Power Adjustment (PPA) which was implemented with a base rate in 2016 and adjusted in 2019. The PPA collects revenues when power costs are over the base rate and refunds (credits) when below the base rate. The Electric Utility is entering the final year of its three-year rate study period,

with a 2% rate decrease programmed for 2021. While no immediate action is necessary, the Council may be asked to consider options to address this issue as part of the 2021 budget process.

- **CARES Act reimbursement:** Staff submitted the City's request for reimbursement of COVID-19 related expenses to Will County on September 8. The initial reimbursement request included public safety and other payroll costs that, if approved, would total the full amount of \$2,094,757 allocated to Naperville. The U.S. Treasury issued revised guidance on the use of CARES Act dollars on September 2 which aligns with the City's request. Based on the revised guidance, the City anticipates receiving its full allotment from Will County. A submission to DuPage County will be made in the coming weeks.

### **Revenues Update**

The City continues to monitor state and local revenues to gain a clearer understanding of the pandemic's fiscal impact. Each month, revenues are analyzed to identify trends that may be developing. September marks six months since the pandemic began impacting revenues; however, only three full months of data exists due to the delay in receiving some state shared revenues. Given the constantly evolving mitigation efforts that were occurring during the first four months of the pandemic, the City has seen significant fluctuations in revenues over the past several months. Although we have seen two consecutive months of improvement, consumer spending habits continue to change, and no clear trends have been established as to the pace of recovery over the second half of 2020 and into 2021.

### **State revenues**

Sales tax revenues improved significantly in September with state sales tax being 6.4% lower than original budget projections and home rule sales tax (HRST) being 13.0% lower. These revenues represent sales that occurred during June. For the first time since reporting pandemic-related sales tax impacts, Naperville outperformed the statewide average declines when making a year-over-year comparison. For September, Naperville declined 3.4% for sales tax and 12.5% for HRST while the statewide average declines were -5.7% and -15.5%, respectively. Staff will look to October sales tax numbers to determine whether a trend is being established as September and October represent collections from consecutive months with similar Phase 4 mitigation efforts in place (June and July).

September's state income tax revenue was 6% higher than original budget projections. This is the second consecutive month of better than expected revenues in this category. Similar to last month, September revenue likely benefited from the delayed income tax filing deadline. Although revenues have improved over the past two months, the Illinois Municipal League (IML) recently provided a forecast for CY2021 that shows state income tax revenue shared through the Local Government Distributive Fund (LGDF) will remain under pressure and is estimated to decrease by 10% from CY2020. These estimates will be reflected in the 2021 budget.

Local use tax continues to outperform budget projections due to the shift in consumer behavior to increased online shopping. September revenue was 45% higher than original budget projections. IML is forecasting continued strength in this category with 2021 revenues estimated to exceed 2020 revenues by 7.5%. Some of this increase is tied to the changes in sales tax laws that will take effect on January 1, 2021 that require most online marketplace retailers to remit sales tax based on the delivery location. This means the City will begin collecting HRST on these online purchases. IML has been cautious in forecasting how the tax law changes will impact municipal revenues other than to

predict that, in the long run, local use tax will decline in favor of much higher sales tax revenues. For 2021, it remains unclear how local use tax and state sales tax will balance with these changes.

State motor fuel tax (MFT) revenues, which include Transportation Renewal Funds (TRF), remained nearly 7% below budget projections in September. This marks three consecutive months of decline in the 5 to 7% range. IML’s recent revenue forecast indicates that MFT will grow by 5% in CY2021 and TRF will grow by 9% from CY2020 levels. Because the City did not include TRF or Rebuild Illinois funds in the 2020 budget, MFT related revenues should be an area of growth in the 2021 budget.

**September State Shared Taxes**

Revenue	Projection	Actual	Diff (\$)	Change (%)
Sales Tax	3,151,192	2,950,152	(201,045)	- 6.4
State Income Tax	1,068,381	1,132,744	64,360	6.0
Home Rule Sales Tax	1,288,341	1,120,302	(168,041)	-13.0
Motor Fuel Tax	544,993	508,714	(36,279)	-6.7
Local Use Tax	380,510	554,184	173,674	45.6
<b>Totals</b>	<b>6,433,426</b>	<b>6,266,096</b>	<b>(167,331)</b>	<b>-2.6%</b>

Year-to-date, actual revenues for the five major state collected revenue categories are now 12% below budget projections through September. It is important to note that not all these categories are allocated to the General Fund; MFT and HRST revenues are allocated to capital funds.

In July, staff reduced the projected revenue shortfall in the General Fund from \$18 million to \$12 million. Due to the continued uncertainty surrounding how the pandemic might progress as we enter the traditional cold and flu seasons, staff has not updated that projection. However, if revenues continue to improve or even hold steady over the remainder of 2020, the projected revenue shortfall may be much less than \$12 million. A revised projection will be included in the proposed 2021 budget.

Revenue	Projection (through Sept)	Actual (through Sept)	Diff (\$)
Sales Tax	26,245,376	24,108,239	(2,137,136)
State Income Tax	11,846,461	9,161,266	(2,685,195)
Home Rule Sales Tax	9,738,247	9,353,170	(385,078)
Motor Fuel Tax	4,104,274	3,169,141	(935,134)
Local Use Tax	3,438,944	3,823,904	384,959
<b>Totals</b>	<b>55,373,302</b>	<b>49,615,719</b>	<b>(5,757,583)</b>

**Local revenues**

Staff continues tracking overall taxable sales reported in several local revenue categories. Sales numbers for prior months are adjusted as delayed tax receipts are received. In July, food and beverage sales continued to show strong recovery, up 12% from June. Food and beverage sales remain 12% below pre-pandemic sales in February. Local gasoline sales improved 9% in July and are now 8% below February sales. Real estate sales in August continued to show strength,

increasing 3% from July. Closer analysis of tax stamp data for 2020 shows residential real estate outperforming and commercial real estate lagging as compared to 2019. Property tax collections continue to be in line with prior years. Through the first week of September, the City has recorded 90% of its budgeted property tax revenue.

Month	Food & Beverage	Hotel/Motel	Local Gas	Real Estate
January	34.63	0.85	5.38	66.11
February	34.10	0.93	5.27	67.11
March	22.74	0.48	4.26	89.48
April	15.89	7.38	2.39	71.07
May	22.32	0.06	3.39	107.41
June	27.21	0.12	4.40	135.77
July	30.51	2.71	4.85	149.88
August	-	-	-	153.78
<b>Totals</b>	<b>187.40</b>	<b>12.54</b>	<b>29.94</b>	<b>840.61</b>
<b>\$ in millions</b>				

**Risk Assessments**

Staff continues to review and update risk assessments for the various revenue categories identified as being at-risk at the outset of the pandemic. There are no changes to the risk assessments this month, and staff will continue to monitor for changing trends.

Revenue Source	Level of Risk	Reasoning
Hotel/Motel Taxes	High	Business and leisure travel continue to be limited by the pandemic.
Food and Beverage Taxes	Medium	Business limited by consumer demand, Phase 4 mandates, and Will County mitigation measures.
State & Home Rule Sales Taxes	Medium	Overall consumer spending lower as part of the broader economic slowdown; staff continuing to monitor for future trends that may show evolving consumer behavior patterns.
Income Taxes	Medium	Statewide unemployment in July declined to 11.3%.
State & Local Motor Fuel Taxes	Medium	Work-from-home economy and reduced leisure travel impact miles driven.
Commuter Parking Fees	Medium	Reduced rail commuter traffic due to telework impacting parking fees.

**Expenses Update**

Although spending has normalized in most categories, expenses overall remain below budget projections by \$17 million across all funds. More than half of that amount, \$9.5 million, is accounted for in capital outlay. The timing of those expenses is less predictable and project expenses may not

be realized until the third and fourth quarters of the year. Purchased electric and water also remain below budget by \$2.9 million combined. Insurance benefits and related claims remain \$3.5 million below projections. Salary and overtime are \$680,000 below budget projections, primarily due to lower overtime costs. Other categories experiencing notable spending reductions include operational services, equipment parts, fuel, and education and training.

### ***2021 Budget Discussion Preview and Timeline***

With 2021 budget creation underway, it is evident the City Council has positioned the City well over the past several months despite the volatility associated with the pandemic. Council's prior development of the financial principles and willingness to explore alternate financial options that were not envisioned at the beginning of 2020 has let the City develop a measured financial response that can be utilized as appropriate in the coming months. These actions are positioning the City to not just stay the course through the remainder of the year, but also as the City envisions a post-pandemic future.

Looking ahead, the unique environment the City finds itself in may require a departure from the traditional reliance on trends and data in financial forecasting. Understanding that no historical financial comparisons from a similar event exist within our lifetimes and that no definitive upward or downward trends have been identified with revenue streams at this point, along with the need to monitor evolving consumer spending patterns, staff continues to use flexibility as the driving force behind 2021 budget development.

The conversation around the 2021 budget will take place at three upcoming workshops on October 26 and November 9 and 23, with the publication of the draft 2021 budget scheduled for Friday, October 16. The conversation will be driven by the concept of the 2021 budget as an asset that will invest in Naperville both for the duration of the calendar year it covers as well as beyond the pandemic through supporting the ongoing stability and vitality of City services. Discussions will center around the four pillars of services, people, programs, and the local economy, with an emphasis on how appropriate investment in each of these areas positions the City for continued service levels throughout and following the pandemic's course.

### ***Next Steps***

Staff continues to closely monitor City finances to identify trends as we progress through the pandemic. These trends, along with Council direction provided during monthly reports, are informing the 2021 budget development process.

Staff is also finalizing the 2020 debt issuance, which includes approximately \$16 million in new borrowing. Additionally, three bonds from 2010 and 2011 are eligible for refunding. By refunding these bonds, the City is essentially refinancing debt at lower interest rates to achieve cost savings over the remaining life of the debt service. The bond issuance ordinance will be presented to Council on October 6.

### **FISCAL IMPACT:**

N/A