



MINUTES FINANCE COMMISSION

Wednesday, February 26, 2020 - 5:00 P.M.
City of Huntington Beach
Civic Center – Lower Level Conference Room #B-7
2000 Main Street
Huntington Beach, CA 92648-2702

Chair Lo Grasso called the meeting to order at 5:00 p.m. and led the Pledge of Allegiance.

MEMBERS PRESENT: Lo Grasso; Hudson; Sterud; Ray

MEMBERS ABSENT: Van Der Mark, Gledhill

STAFF PRESENT: Dahle Bulosan, Acting Chief Financial Officer
Sunny Rief, Acting Assistant Chief Financial Officer
Oliver Chi, City Manager
Travis Hopkins, Assistant City Manager
Behzad Zamanian, CIO, Information Services
Thuy Vi, Administrative Assistant, Finance
Linda Wine, Administrative Assistant, Finance

ORAL COMMUNICATIONS – None

MINUTES

Motion: Moved by Sterud and seconded by Lo Grasso to approve the Finance Commission Meeting Minutes dated January 29, 2020, as presented

Ayes: Lo Grasso; Hudson; Sterud; Ray

Noes: None

Absent: Van Der Mark, Gledhill

Approved: 4-0-2 (Van Der Mark, Gledhill-Absent)

DIRECTOR ITEMS – Acting Chief Financial Officer Dahle Bulosan recommended that the Dark Fiber Update Presentation be the first Discussion Item.

DISCUSSION ITEMS

Dark Fiber Update

Assistant City Manager Travis Hopkins gave a presentation on the Dark Fiber Update. He showed the Finance Commission the “Fiber Optic Master Plan and Implementation Roadmap,” which was presented to the City Council on October 7, 2019.

Hopkins noted at the Strategic Planning Session on February 7, 2019, Dark Fiber was presented as an option for funding a revenue source for the City. The City Council asked staff to develop and present a Broadband Master Plan for the installation of Fiber throughout the City. He provided the Finance Commission with City roadmaps identifying areas where an established City-owned Fiber network will assist in connecting City facilities and deploying “smart city” applications and technologies. He noted that fiber is the transport layer that enables high-speed connectivity.

Hopkins summarized the City’s Accomplishments: in 2015, the Broadband Strategic Plan was drafted, in 2016-2017, the Magellan Advisors were retained to assist the City, and in 2017, the internal

telecommunications team was launched and discussed forming a Broadband “Smart City” Ad Hoc Committee. He stated that the purpose of the Master Plan is to provide a guide on how to implement the Master Plan. The Plan was brought to the City Council with the current municipal communications infrastructure, as well as use for the future network expansion. Hopkins summarized City Fiber by the numbers. The City currently has 41 connected intersections, 27 connected facilities, ten miles of Fiber in the road, and the capacity of the Dark Fiber – unused fiber – is 50% of the 96 Strand Cable.

Hopkins explained that fiber is used throughout the City to transfer data and communicate with traffic signals and other City facilities – Fire Station, Joint Powers, Public Works Yard, Lifeguard Towers and Headquarters. Fiber is available for other agencies to use to transfer data quickly throughout the City, and fiber provides the opportunity for “smart city” technology for future data that can be collected, which requires fiber to deliver that information.

Hopkins listed the current Traffic Signal System projects, which include current construction of 9.25 miles of fiber and 24 new signals at Brookhurst, Magnolia, Newland, Center Ave, Main Street and Goldenwest. The funded projects include 4.25 miles of fiber and 13 new signals down Edinger and Warner. The existing Information Systems projects include the Murdy Park fiber connection back to City Hall, and the funded projects include connecting the Downtown Facilities. In design is the Joint Powers and Utilities to Goldenwest fiber system. He also noted that over 1,000 cities in the United States have Municipal Fiber Networks.

Chair Lo Grasso asked about the advantage of fiber on streetlights. Hopkins said that the City has a traffic management facility at City Hall, and traffic is managed through cameras on traffic signals. The cameras are run independently and talk to the system. Traffic signals can operate on timers, or when a vehicle triggers a sensor. Hopkins stated that fiber brings all the signals together so that we can operate them in conjunction. With cameras on traffic signals, traffic lights can be controlled from the office in the case of an emergency. Lo Grasso asked what percentage of the City is fiber connected, and Hopkins said there are 41 connected signals out of approximately 130 traffic signals.

Commissioner Sterud asked about a Dark Fiber Business Plan and potential revenue. Hopkins said that ten miles is not a large enough “backbone,” and funding for the required additional backbone would cost \$16M to \$20M. Sterud asked if the \$20M investment in Dark Fiber would be worth the return on the investment. City Manager Oliver Chi said that it would be unrealistic to expect that the City will have fiber down every major arterial, and to be an internet service provider, we would need to build infrastructure and invest billions in capital. Sterud noted that the Commission was informed that the City has ten miles of fiber that can be leveraged to generate revenue. Chi stated that this is not true. Sterud asked how we move forward.

Lo Grasso wanted to know how cost effective it would be for him to receive internet service at his office building via fiber from the nearby traffic signal. Hopkins said that it would not be cost effective because the service would require 24/7 maintenance. In that case, the City would go to other providers who would provide the service. The provider would lease the Dark Fiber from the City, connect and sell the service and bill the end user. Lo Grasso said that this does not sound financially feasible.

Commissioner Ray echoed Sterud’s question about a Dark Fiber Business Plan and potential revenue. Chi noted that Federal and State grants are available to fund the interconnecting of all signals and City facilities. Chi also noted that the City’s goal is to leverage the money we have to build what the City needs. Sterud said that the Finance Commission was told that buried cable can be sold for revenue and was misled. He noted that if Dark Fiber is not a revenue generator, it should not be an issue for the Finance Commission. Lo Grasso said that Dark Fiber should not have been presented as a revenue generating item.

Hopkins noted that spending the \$16M-\$20M to complete the interconnectivity on Brookhurst and on Warner could increase the City's revenue. Chi noted that the Dark Fiber connectivity speed needs to be 5G. Chi also said that Dark Fiber is an infrastructure project to better manage the City, not a revenue-generating project. Sterud asked if the City Council will be notified that Dark Fiber is not a revenue-generating project. Hopkins responded yes.

The Finance Commission thanked Hopkins for his presentation.

Large Real Estate Purchases

City Manager Oliver Chi gave a presentation on Large Real Estate Purchases. His presentation focused on the City's current Property Acquisition Process. He noted that the City Council approves property acquisition deal points via a Letter of Intent (LOI) or Memorandum of Understanding (MOU), and that upon City Council approval of deal terms, a series of due diligence processes are initiated. The steps include opening escrow by Real Estate staff; title report run and review by City Attorney's Office and Real Estate staff; Phase I Environmental Report for a cursory review of any environmental issues on the property coordinated by Real Estate staff with support from the City Attorney's Office; if any issues, Phase II Environmental Report for a more in depth study is initiated by Real Estate staff in coordination with Public Works, who typically has contracts with on-call environmental testing firms and purchase, then reviewed by Real Estate staff and the City Attorney's Office for any exceptions; and purchase and sales contract developed by the City Attorney's Office with support from Real Estate staff. Chi also noted that if any material issues are identified during the due diligence process, the deal would then need to be reassessed and possibly brought back for further City Council review, depending on any identified issues.

Lo Grasso asked how the City identifies the property it wants to purchase; whether the City looks for property on the market that fits the purpose, or property not on the market where the owner is approached. Chi said that this depends on the City's objective in the transaction. Chi noted that the City typically does not buy much property, but if there is a reason to purchase property for a specific purpose, that is where the dialogue begins. Chi said that the City is looking to acquire property on Cameron Lane because the City needed to spend restricted money for affordable housing. Cameron Lane was identified as a piece of property for an affordable housing site, and the property owner's broker approached the City. Chi said that he then met with the the City Council during closed session and received direction for negotiation, which formed the basis for dialogue with the property owner and the LOI that was ultimately brought to Council for consideration. Property purchase can be funding source driven or Council policy driven, which dictates what piece of property the City seeks to acquire. LoGrasso asked if the City looked for property that not is not on the market. Chi responded that it would be based on the context and Council direction. The City would work with real estate brokers, and also has access to real estate websites such as Loopnet.com for available commercial property.

Lo Grasso asked about the purchase of the property on Pipeline Lane. Chi said that the broker approached the City with the Pipeline deal. Lo Grasso asked how the City determines pricing. Chi stated that he was not involved in the discussions during the Pipeline purchase, but in a typical real estate transaction, the broker would approach the City with the asking price and the City would have an opportunity to counter. Lo Grasso was interested in knowing the asking price and purchase price. He said that the City spent \$2.75M on Pipeline, when it was listed at \$1.3M in 2008 and did not sell. Lo Grasso said that he had toured the property during the open house, and there have been no improvements that would have increased the value of Pipeline to 100% in 10 years. He wanted to know if Pipeline was officially appraised. Chi said that he did not know the basis by which the Pipeline purchase was determined to be a fair price, but the City was able to sell the property for the same price that it was purchased for. Chi noted that with the Cameron property, there was no formal appraisal when the City made a purchase offer, because an appraisal was done two months prior on a comparable property that helped determine the value of Cameron. Lo Grasso wanted to know whose idea it was to purchase

Pipeline and how the purchase price was determined. Sterud asked about the City's Real Estate staff. Chi stated that there are four full-time staff, one with a real estate background, who used to work for the Office of Business Development (OBD), which was previously under the direction of Kellee Fritzel. Currently, staff reports to Director Ursula Luna-Reynosa in Community Development. OBD has primarily a housing and Community Development Block Grant (CDBG) function, and the real estate components are managing lease concessions and contracts. Chi said that internal coordination is needed between OBD managing contracts and CDBG housing funds, and staff could have done a better job of this. Lo Grasso asked if the staff has a real estate license. Chi said a staff member has a real estate background. Lo Grasso questioned the lack of an appraisal on Pipeline and paying cash, without knowing its value, and said that the City is not performing its fiduciary duty and due diligence when purchasing properties. Sterud concurred. Chi said he does not agree that this applies to the Cameron property, and believes the City got a great, below market deal on the transaction. He said that two months ago, an appraisal was done on a property on Beach Boulevard, behind Denny's, and the City received an appraisal of \$3M. Chi said the Cameron property is similar in type and location, but superior to the appraised property. The City offered less than other buyers, and was accepted because there were no contingencies in the offer. Chi noted that with the Cameron purchase, the City solved multiple problems by preventing \$3M from being taken by the State, was fiscally responsible and met its obligation to handle the City's money in a responsible manner.

Lo Grasso stated that for a large real estate purchase, an appraisal takes two weeks, should be a matter of course and done on every transaction. Chi said that moving forward, appraisals will always be part of the purchase and sale agreement. Lo Grasso questioned how review of the title report on the Pipeline purchase was missed, and was not reviewed by the City Attorney's Office until after the purchase. Chi said that there was breakdown in the transactional process, and it is his responsibility to have processes in place where this never happens again. Lo Grasso said that the process doesn't work and our controls are shoddy. Chi acknowledged this comment and agreed that this should have never happened. He said that the City now has new procedures in place on how property is acquired. Sterud asked if the Property Acquisition Process was in place for the property purchases prior to Chi's arrival, and if the City Attorney's Office was part of that process. Chi said that he does not believe that the process was in place, and with the Pipeline transaction, the City Attorney's Office did not receive the title report. He acknowledged that part of the problem was that internally, the City had rules that were hard to understand and that staff could have done a better job. Ray asked if an itemized checklist could be instituted for the Property Acquisition Process and Procedures. Chi said yes, via a City Administrative Regulation on property transactions, which is not yet in place. Chi noted that with the Cameron purchase, the City is following the new guidelines and doing its due diligence.

Sterud said he was concerned that a non-City real estate representative was not involved in the Pipeline negotiation, and should have been retained to check on City staff and City officials. Chi noted that broker fees are required to be paid as part of the transaction, and that existing City staff should be able to perform the job. Sterud said that broker fees are 2.5%, and the City would have saved money. He said that it was inappropriate to have a sitting Councilperson's brother represent both the buyer and the seller for Pipeline. Sterud stated that the City Council member should have disclosed the conflict of interest, so that the Council could consider a seller or buyer representative. He stated that Chi is setting forth processes that would solve these issues, but does not think his concern about the Pipeline issue has been fully addressed. Sterud recommended retaining a real estate broker for property transactions, and Lo Grasso concurred. Chi noted that this would be a good recommendation for Council to consider. Lo Grasso said that the City Attorney should review all real estate documents. Ray recommended that staff obtain a real estate license. Chi thanked the Commissioners for their feedback, and Lo Grasso thanked Chi for his presentation.

Bulosan gave a presentation on the City of Huntington Beach Unfunded Pension Liability Policy, Part Two, based on the feedback from the Finance Commission at the January 2020 meeting.

He gave an overview of Pension Obligation Bonds (POBs) and noted that a POB would save the City an estimated \$173M, assuming CalPERS (PERS) earns a 7% discount rate and the City is able to get the POB at an approximately 3.4% rate. He noted PERS' Historical Returns: 1 year at 6.7%, 5 years at 5.8%, 10 years at 9.1%, 20 years at 5.8% (factoring in two recessions) and 30 years at 8.1%. Bulosan noted that bond market rates are at an all time low, and the City has an opportunity to refinance at approximately 3.4%.

Bulosan presented the Fiscal Year-Over-Year chart showing the \$173.1M savings. Fiscal Year 30/31 represents the peak of annual payment; a \$21.09M or 85% increase from what the City paid in FY18/19. He noted the proposed POB Debt Service would stay steady at \$27.6M per fiscal year. Bulosan stated that the POBs are a great idea, with a huge amount of savings and that the City should take advantage because of our unique situation.

He noted the Finance Commission's considerations from the January 29, 2020 meeting. The Finance Commission recommended to keep the Accelerated Payoff / Funding Schedule until the City's PERS funded status reaches 120%. Upon reaching that goal, the Accelerated Payoff / Funding Schedule would be replaced, and the new policy instituted would be to pay off any new Unfunded Accrued Liability (UAL) within one year, unless market factors dictate a different approach. This concept was advanced because PERS' returns below 7% could create new UAL amounts that may not be feasible to cover within one year. The Accelerated Payoff / Funding Schedule enables the City to address any new UAL without significantly impacting ongoing operations. The PERS payback timeframe is 20 years. The City is striving to pay off any new UAL using an Accelerated Schedule. Chi noted that the City's challenge would be paying off any new UAL within the year.

Bulosan reviewed Staff's Unfunded Pension Liability Policy Recommendation. To achieve the identified policy objective, the City would set aside 100% of POBs savings to offset future UAL – approximately \$5M annually. Chi stated that setting aside \$5M a year in perpetuity is a significant and responsible policy change to managing our finances. He noted that the FY 19/20 Library Department budget is \$5M per year, the FY 19/20 Finance Department budget is \$6M per year, and we are basically taking a department and saving that amount. Sterud recommended that inflation (CPI, Consumer Price Index) be factored in. Lo Grasso and Chi concurred. Bulosan noted that based on the Finance Commission recommendations, the City's Accelerated Payoff / Funding Schedule will stay in effect until the City reaches a pension plan funded status of 120%. He also said that the reserve level would be determined by the combined account balances of the following: CalPERS account balance, Section 115 Trust, and Pension Rate Stabilization Reserve.

Chi covered the City's Accelerated Payoff / Funding Schedule. Any new UALs under \$10M would be paid within 1-3 years, \$10M-\$20M would be paid within 4-6 years, \$20M-\$30M would be paid within 7-9 years, \$30M to \$40M would be paid within 10-12 years, \$40M-\$50M would be paid within 13-15 years, and over \$50M would be paid within 15-20 years.

Chi presented the City's Funding Policy Upon Reaching 120% Funded Status. Upon reaching 120% funded status, the Accelerated Payoff / Funding Schedule would be replaced, and the new policy instituted would be to pay off any new UAL within one year, unless market factors dictate a difference approach. Chi noted that CalPERS policy is a pay off of 20 years, whereas the new City Policy would be a pay off of any UALs within one year.

Bulosan talked about the Pension Savings Allocations. He noted that one of the top priorities in setting aside these funds is capital preservation and making sure we have liquidity during a "down" market, and a

balance of risk and return. Bulosan stated that one of the options is investing in a Pension Rate Stabilization Reserve, which includes a City pooled investment governed by California Governmental Regulations. He noted that the Rate Stabilization Reserve is very conservative, and the primary goals for those investments are ensuring safety, capital preservation and liquidity. Bulosan said that the other option is the Section 115 Trust, which is an investment mix of equity, fixed income and cash. He also noted that the City's Section 115 investment objectives range from conservative, moderately conservative, moderate, balanced and capital appreciation. He presented Staff's Pension Savings Allocation Recommendation. Staff recommends setting aside POB savings of approximately \$5M annually, which are first allocated to pay off any CalPERS UAL, and once there is no remaining CalPERS UAL, the POBs savings will be allocated to the following, based on market conditions: Pension Rate Stabilization Reserve (which is the primary option) and Section 115 Trust. Vice Chair Jay Hudson asked Sterud what the percentage split would be to best protect our resources. Sterud recommended a split of 70% Pension Rate Stabilization Reserve, and 30% Section 115 Trust, with the Section 115 Trust investments being conservative and moderately conservative, since it is taxpayer money that the City is investing. Chi concurred. He noted that the \$5M annually should be in perpetuity and until all POBs and Bonds are matured and paid off.

Chi and Bulosan spoke of additional fiscal policies being developed. To further enforce fiscal sustainability initiatives, staff has started working on additional fiscal policies to take effect in the event that the POB issuance is authorized. Some of the policy ideas include an adopted, certified General Fund Reserve Policy that mandates setting aside annually a sum of money until a General Fund threshold is reached. Chi noted that typical, best practices in government is 30%-50% of the annual General Fund operating budget. Chi said that the typical Government Finance Officers Association (GFOA) formula is two months of operating budget, which is 30% of the City's operating budget. Chi requested the Commission's direction to work on the policies and to bring back to the Commission next month. He noted that the UAL adoption policy and POB consideration goes in tandem as a package. The City will do the UAL payoff worth \$5M a year in pension savings, and the General Fund Reserve Policy set aside until a threshold is met. Chi noted that in planning for future staffing cost increases, Bulosan suggested that personnel costing be calculated by the fully burdened rate multiplied by 50% to set aside additional money in the reserve. Chi said that the City needs to look at reinvesting in people, staffing and service levels, and having a policy in place with this calculation will require the City to be fiscally responsible. Sterud and Lo Grasso agreed that the calculation is a great idea.

Chi suggested having a policy in place for surplus money that sets aside funding for playground equipment, which has no current funding. He noted that the City owns 78 parks, but the development impact fee section in the State statute states that new developers cannot be charged for ongoing maintenance activities, but can be charged for impacts to existing infrastructure associated with the development, like parks. Sterud stated that he is comfortable with 7.5% in park funds. This will be addressed during the City's Annual Park Review.

Lo Grasso asked if there is a possibility that the City Council would approve the POBs, but not the suggested policies. Chi stated that it will be up to the City Council, but if the policies are developed thoughtfully with safeguards, we will put the City in the best financial position. He stated that he would like to draft the three policies for the Commission's review and consideration, and ultimately for consideration by the City Council in April 2020.

Hudson spoke of Newport Beach's strategy towards homelessness. Chi noted that Huntington Beach will present its Homeless Response Strategy for discussion in March 2020.

Bulosan stated that he is working with the City's financial advisors and requested direction from the Finance Commission.

Motion: Moved by Sterud and seconded by Hudson to achieve the identified policy objective, the City would set-aside 100% of POB savings to offset future UAL, starting with [approximately] 100% of POB savings in Year One – approximately \$5M annually, plus Consumer Price Index (CPI). This policy would continue until maturity and will expire at maturity or pay off of POBs.

Ayes: Lo Grasso; Hudson; Sterud; Ray

Noes: None

Absent: Van Der Mark, Gledhill

Approved: 4-0-2 (Van Der Mark, Gledhill-Absent)

COMMISSIONER COMMENTS –

Lo Grasso thanked the Commission and the presenters. Hudson requested a future discussion regarding a fleet leasing program, noting that the cities of Westminster and Redlands have adopted this program.

ADJOURNMENT – There being no further business, the meeting adjourned at 6:58 p.m.

Submitted by:

Dahle Bulosan, Acting Chief Financial Officer

By: Thuy Vi, Administrative Assistant, Finance Department
Linda Wine, Administrative Assistant, Finance Department