COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER

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January 6, 2011

TO: Supervisor Michael D. Antonovich, Mayor
Supervisor Gloria Molina
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Don Knabe

FROM: Wendy L. Watanabe
Auditor-Controller

SUBJECT: **CITY OF BELL FINANCIAL CONDITION REVIEW**

On October 19, 2010, your Board instructed the Auditor-Controller to conduct a comprehensive review of the financial condition of the City of Bell (Bell or City). The request was based on issues raised by the media regarding City salaries, and the State Controller's findings of "serious and pervasive" deficiencies in the City's administrative and accounting controls. Your Board instructed us to report back on whether Bell has the resources needed to provide core public services, including a review of revenues, expenses, cash, bonds and other obligations.

This is our report on Bell's financial condition. Our review indicates that the City's projected General Fund expenses will exceed its projected revenue, resulting in a deficit of approximately $2.16 million, 14.5% of the City's General Fund expenditures, a year. However, if the City reduces its programs to only provide general government, public safety and public works, and eliminates its Community Services program, or achieves other equivalent savings, it is projected to have a deficit of approximately $424,000, or approximately 3.3% of the City's projected General Fund expenditures. The City will also have to pay approximately $1.26 million in one-time extraordinary expenses. These extraordinary expense may be partially paid with approximately $350,000 in one-time revenue the City is expected to receive this year.

The following is a detailed description of the City's projected General Fund revenues and expenses:

CITY OF BELL

GENERAL FUND
ESTIMATED REVENUE AND EXPENDITURES

	ALL CURRENT SERVICES	CORE SERVICES
REVENUE:		
PROPERTY TAXES	$ 2,230,629	$ 2,230,629
OTHER TAXES	4,736,302	4,736,302
LICENSES & PERMITS	576,006	576,006
FINES, FORFEITURES & PENALTIES	702,500	702,500
REVENUE FROM MONEY & PROPERTY	870,500	870,500
REVENUE FROM OTHER AGENCIES	3,052,400	3,052,400
CHARGES FOR CURRENT SERVICES	366,450	366,450
COMMUNITY SERVICES	205,100	-
OTHER REVENUE	10,000	10,000
TOTAL REVENUE	**$ 12,749,887**	**$ 12,544,787**
EXPENDITURES:		
GENERAL GOVERNMENT:		
SALARIES & EMPLOYEE BENEFITS[1] *(15 Full-time and 5 FTE[2] Part-time Employees)*	$ 1,886,191	$ 1,886,191
SERVICES & SUPPLIES	1,872,942	1,872,942
GENERAL GOVERNMENT TOTAL	**3,759,133**	**3,759,133**
PUBLIC SAFETY:		
SALARIES & EMPLOYEE BENEFITS (Sworn) *(33 Full-time)*	5,924,612	5,924,612
SALARIES & EMPLOYEE BENEFITS (Non-Sworn) *(12 Full-time and 1 FTE Part-time Employees)*	1,249,910	1,249,910
SERVICES & SUPPLIES	1,297,016	1,297,016
PUBLIC SAFETY TOTAL	**8,471,538**	**8,471,538**
COMMUNITY SERVICES:		
SALARIES & EMPLOYEE BENEFITS *(5 Full-time and 32 FTE Part-time Employees)*	1,513,570	-

SERVICES & SUPPLIES	525,554	102,189
COMMUNITY SERVICES TOTAL	**2,039,124**	**102,189**
PUBLIC WORKS:		
SALARIES & EMPLOYEE BENEFITS *(3 Full-time and 0 FTE Part-time Employees)*	222,426	222,426
SERVICES & SUPPLIES	413,341	413,341
PUBLIC WORKS TOTAL	**635,767**	**635,767**
TOTAL EXPENDITURES	**$ 14,905,562**	**$ 12,968,627**
DEFICIT	**$ (2,155,675)**	**$ (423,840)**

[1] Includes five City Council Members at a total annual cost of $70,789.
[2] Part-time employees were converted to Full-time Equivalents (FTE)

It should be noted that, as discussed later in this report, the City faces some significant uncertainties (e.g., future business license fee collections, future CALPERS pension obligations, and a number of potential legal claims and fees). These uncertainties could have a significant impact on the City's financial status and its ability to provide even core services to its residents.

Our analysis is based on reviewing the City's revenues and expenses for the last three years, and current revenue collections. We then met with available Bell fiscal staff to identify areas where the City's revenues and expenses may have been inappropriately over or under the "normal" amounts, or charged to incorrect funds. For example, we reduced the City's projected business license fees because of claims that businesses may have been required to pay higher than appropriate fees in the past. We then revised the revenues and expenses to estimate the amounts that may be realized/incurred in the future.

It should be noted that, because of the fiscal practices of the City's prior management and limited fiscal staff, our estimates are based on some significant assumptions about the City's revenues and expenses. As a result, the City's actual revenue and expense could be substantially higher or lower than our estimates. In addition, as discussed later, the City has some extraordinary expenses, and faces some potential liabilities and other issues that could significantly affect its financial viability.

Salary Changes

Our estimates eliminated the high salaries paid under the prior administration. For example:

	Prior Base Salaries	New Base Salaries
City Manager	$ 703,000	$ 250,000
Assistant City Manager	$ 343,000	Position Eliminated
Police Chief	$ 457,000	$ 200,000
Director of Admin. Services	$ 231,000	$ 160,000
Council Members	$ 97,000	$ 8,100

NOTE: Includes only base salaries. Employee benefits and other related payouts are excluded.

It should be noted that the City's total General Fund salaries and employee benefits in our estimates are higher than the prior year amounts, even though the City is eliminating some excessive salaries (e.g., the prior City manager's salary). This is because some of the prior high salaries and employee benefits were recorded under other City funds, not in the General Fund, and because the City had incorrectly recorded its employee benefit costs in prior years. For example, some of the former City manager and assistant City manager's salary and employee benefits were charged to another fund. After the proper realignment, eliminating the high salaries does not reduce the total projected General Fund expenses significantly.

The projected salaries used in our estimates were discussed with the current contract City management. Some of the amounts may be higher than actually needed to fill the positions (e.g., $250,000 for a city manager). However, we used those estimates to be conservative and ensure we did not understate the City's future costs.

Extraordinary Expenses and Revenues

As noted earlier, our analysis is based on the City's projected ongoing General Fund revenues and expenses. Our analysis does not include some significant extraordinary expenses the City is currently incurring. For example, Bell's current legal expenses are significantly more than they would normally incur. These extraordinary expenses, which are continuing to be incurred, are projected to total approximately $1.26 million for the year ending June 30, 2011. We excluded these expenses from our projections because they are expected to be one-time costs. However, the City will have to pay these expenses.

The City may be able to pay part of the extraordinary expenses with one-time revenue the City has or is expected to receive this year. Specifically, the City is attempting to

collect $350,000 from the City of Maywood for administrative assistance Bell provided to Maywood. If Bell collects all $350,000 of this one-time revenue and applies it to its extraordinary expenses, it will still have approximately $910,000 ($1.26 million - $350,000) in extraordinary expenses that will have to be paid.

Other Uncertainties

Bell also has to address a number of potential costs and claims that may affect its cash flow and its ability to pay its expenses. For example:

- The City faces allegations that it impounded vehicles improperly to increase impound fees, and overcharged for business license fees and other revenues in the past. If the City has to repay any prior collections from its General Fund, it will reduce the City's available resources and may affect the City's ability to continue to provide public services.

- The City has made retirement contributions for pensions based on high salaries paid to some prior City managers, elected officials and other employees. However, the California Public Employees Retirement System (CALPERS) has indicated that a substantial portion of these higher pensions may not be paid. This area will probably be the subject of legal challenges by the City, questioning the legality of the higher pensions, and by the prior officials, who will claim they are entitled to the higher amounts. If the higher pensions are not paid, the City may be entitled to a reduction in future pension costs. The impact on the City will not be known until the conclusion of the legal process.

- The City's prior attorney claims the City owes him approximately $300,000 in legal fees. Bell management also indicated the City owes an additional $150,000 to another attorney. Again, if the City has to pay these fees, it may affect the City's ability to provide services.

Because the impact these issues will have on the City's General Fund are unclear, we did not include these issues in our estimates.

General Fund Cash Balance and Cost Reductions

One of the resources government jurisdictions use to address operating deficits and/or extraordinary expenses is their available cash balance. The City of Bell has not reconciled their cash account in approximately six months. However, City management estimates the General Fund's cash balance to be approximately $300,000 as of December 13, 2010. If the City applies its available $300,000 cash balance to the estimated $2.16 million operating deficit, it will still have a $1.86 million deficit, plus the remaining balance of $910,000 in extraordinary expenses discussed earlier, resulting a total of $2.77 million ($1.86 million + $910,000) in unfunded costs.

Given the uncertainties facing the City, it seems unlikely that the City would be able to address its unfunded costs by raising taxes or borrowing. As a result, the City may be forced to reduce its programs or its costs to pay the $2.77 million. The City can reduce its expenses by reducing salaries and employee benefits, and/or services and supplies by across-the-board reductions, or reducing specific expenses. The City may also be able to reduce its cost by cutting back on some non-core services. Eliminating the Community Services program would save the City approximately $1.73 million. In addition, the City may be able to reduce its cost by contracting for some services.

Bonds and Related Debt

As discussed earlier, our review was intended to evaluate whether the City's General Fund has the resources to provide core public services. However, we also completed a limited review of the City's bonds (attachment).

We thank the staff at the City of Bell for their cooperation and assistance in our review. Please call me if you have any questions, or your staff may call Jim Schneiderman at (213) 253-0101.

WLW:MMO:JLS
Attachment

c: Oscar Hernandez, Mayor, City of Bell
Pedro Carillo, Interim City Manager, City of Bell
Jamie Casso, Interim City Attorney, City of Bell
William T Fujioka, Chief Executive Officer
Sachi A. Hamai, Executive Officer Board of Supervisors
Audit Committee

BONDS AND RELATED DEBT	ISSUED AMOUNT	PURPOSE	REMAINING PROCEEDS	DEBT SERVICE FY 2010-2011	EST. PLEDGED REVENUE FY 2010-2011	PLEDGED REVENUE SOURCE	
CITY OF BELL:							
GENERAL OBLIGATION BONDS (SERIES 2004)	$ 15,000,000	Improve the sports complex, community center, and other recreational facilities. Bond proceeds were also supposed to be used to build a new library, theater, and other City facilities.	$ -	$ 1,018,619	$ 1,729,900	DEBT SERVICE TAX	(1)
GENERAL OBLIGATION BONDS (SERIES 2007)	$ 35,000,000		$ 23,000,000	$ 1,718,250	$ -	DEBT SERVICE TAX	(1)
BELL PUBLIC FINANCING AUTHORITY:							
CERTIFICATES OF PARTICIPATION	$ 3,020,000	Improve City streets and renovate two ballfields.	$ -	$ 210,398	$ 2,717,200	UTILITY USERS TAXES	(5)
TAXABLE PENSION REVENUE BONDS	$ 9,225,000	Fund the City's unfunded pension liability for safety employees and pay off an older bond that was issued for the same purpose.	$ -	$ 895,379	$ 2,620,408	RETIREMENT TAX	(5)
TAXABLE LEASE REVENUE BONDS	$ 35,000,000	Pay off debt that was issued to purchase property from the United States General Services Administration. Bond proceeds were also supposed to be used to develop the property.	$ -	$ 35,619,500	$ -	LEASE REVENUE	(2)
BELL COMMUNITY REDEVELOPMENT AGENCY:							
TAX ALLOCATION REFUNDING BONDS	$ 27,925,000	Fund redevelopment projects and pay off an older bond that was issued for the same purpose. Bond proceeds were also supposed to be used to fund other projects that benefit low and moderate income housing.	$ -	$ 2,025,368	$ 2,662,018	TAX INCREMENT	
PROMISSORY NOTE	$ 4,600,000	Acquire property (former Western Auto).	$ -	$ 465,809	$ -	NONE	(3)
BELL COMMUNITY HOUSING AUTHORITY:							
LEASE REVENUE REFUNDING BONDS	$ 20,790,000	Acquire, construct, and rehabilitate rental housing properties, and pay off an older bond that was issued to acquire mobile home parks.	$ 798,200	$ 1,293,821	$ 1,404,400	VARIOUS SOURCES	(4)

NOTES:

(1) The City has issued two General Obligation bonds ($15 million in 2004 and $35 million in 2007). In accordance with these voter approved bonds, the City levies a tax to pay the debt service costs of the 2004 bonds. The amount received from taxes is more than the debt service costs. The City uses the excess to repay the General Fund for the debt services costs it incurred before the taxes were levied (fiscal years 2004-05 through 2008-09).

However, the City has not increased the tax to pay for the 2007 bonds, and is using bond proceeds to pay for the debt service costs. It appears that the City will likely have to increase the tax to pay for the debt service costs at some point in the future.

(2) The City's Public Financing Authority (PFA) issued $35 million in bonds to pay off an older note and develop real property for leasing. The note was issued to acquire the property from the United States General Services Administration. The PFA planned to use the lease revenue to pay interest until the bond matured. The PFA would then pay off the principal at maturity by issuing a new bond with a longer term, and pay all subsequent debt service costs (principal and interest) with lease revenue.

However, the property has not been leased, and the PFA has not made the last two interest payments or the $35 million principal payment that was due in November 2010. The City is currently negotiating with the bond holders. It is unclear how this issue will be resolved, and what impact this will have on the City's General Fund.

(3) The Bell Community Redevelopment Agency (CRA) issued a $4.6 million promissory note. The CRA pays the debt service costs using any additional tax increment revenue left over after paying Tax Allocation Refunding Bond debt service costs. The tax increment is a tax on the incremental increase in the assessed value of property located within the redevelopment project area from the assessed value in the base year.

(4) Pledged revenue sources include net operating revenue from the Bell Mobilehome Park, Florence Village, Deb's Field, and Clubhouse at Veterans Park.

(5) The excess of pledged revenue over debt service costs is included in our General Fund revenue estimates.