



August 29, 2019

To the Honorable Mayor, City Council, and Citizens of the City of Hesperia:

It is a pleasure to present the City of Hesperia’s Fiscal Year (FY) 2019-20 Adopted Budget for the City of Hesperia, Hesperia Community Development Commission, Hesperia Housing Authority, Hesperia Fire Protection District, and Hesperia Water District. This budget was developed with the guidance provided by the City Council to provide the highest level of service to the residents and business community within the City’s fiscal constraints.

The FY 2019-20 General Fund Budget is structurally balanced, with operational revenue funding operational expenditures and the difference between total resources (revenue, budgeted reserves, and transfers), and total expenditures resulting in a surplus. The City Council’s prudent fiscal management has provided for the efficient use of City funds, with an emphasis on the delivery of services to the community, while also maintaining the City’s fiscal health.

Local Economy

Over the past eight years, improvement has been observed in several of Hesperia’s local economic indicators, as the City has recovered from the “Great Recession”. This improvement has been very slow when compared to prior recoveries, but it is clear that the local economy in Hesperia has shown real progress. One measure of Hesperia’s improvement is its steady advancement in property values which has enabled Hesperia to regain and surpass its previous assessed valuation high of nearly \$6.0 billion, last seen in 2008. The most recent announcement from the San Bernardino County (County) Assessor’s office in July 2019 revealed a \$6.4 billion assessed valuation for Hesperia, which is a 6.2% increase over its 2018 assessment roll valuation.



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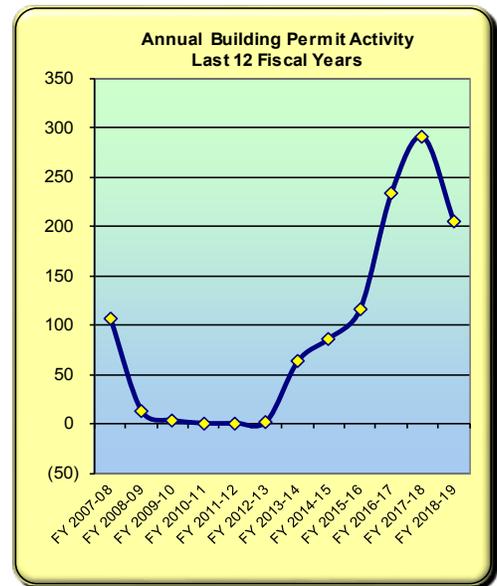
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Though welcomed, this restoration was not fully completed until the latter end of what is now being referred to as one of the longest expansion periods on record, occurring after the end of the 'Great Recession' in 2009. The City experienced four years of successive declines in assessed valuation, amounting to an overall deterioration of 28%. In the years following the 2012 bottom, however, assessed valuation has steadily increased. In all, it took ten years for Hesperia to go through the full effects of the recession and to slowly reclaim the same assessed valuation levels experienced prior to the recession. With the newly announced 6.2% increase for 2019, valuations are now 7.3% above the pre-recession high in 2008.

With respect to building permit activity, the chart to the right shows that the City has rebounded and continues to maintain single family residential (SFR) building permit levels that were seen prior to the recession. During the recession, the City experienced a 100% reduction in SFR permit activity, with two years of issuing no permits. Since that time, SFR permit activity has slowly returned, with 116 permits issued in FY 2015-16, 234 permits issued in FY 2016-17, 291 permits issued in FY 2017-18, and reducing to 205 permits issued in FY 2018-19. The FY 2019-20 Budget projects the issuance of 165 SFR building permits, reflecting a further reduction from the prior fiscal year, as a conservative projection resulting from concerns about an economic contraction amid a slowing global economy. Through July 2019, 15 SFR permits have been issued.



The City utilizes consultant-provided estimates for Sales Tax, Gas Tax, and Gas Tax Swap revenues (approximately \$12.1 million). Revenue estimates for Local Transportation Funds, Gas Tax Road Maintenance and Rehabilitation Account (RMRA) Funds, and various grants are obtained from other government agencies (approximately \$10.1 million). The remainder of the revenues are estimated by staff using trend analysis, examining development activity, property tax collection rates, water consumption by customer class, franchise fee statements, and hotel occupancy levels, which are then compared to amounts of prior years.

As displayed in the chart on the following page, Hesperia has seen a significant improvement in sales tax revenue in the years since the recession. As the largest General Fund revenue source, the City has experienced an increase in sales tax revenue of 87% from the economic downturn low of \$5.5 million in FY 2009-10 to \$10.3 million in FY 2018-19 (unaudited). The increases realized during this time are primarily attributed to fuel sales, as the largest sales tax producing sector of the City, as well as the addition of some large consumer retail stores that have opened in recent years, such as Super Target and Super Wal-Mart. Due to the loss of a large sales tax producer in February 2016, the FY 2016-17 actual dipped 8% from the prior fiscal year. However, the addition of new sales tax producing businesses, the growth in sales of existing businesses, as well as increases in the price of fuel contributed to a 13% increase in FY 2017-18 over the FY 2016-17.



Further, when compared to the FY 2006-07 pre-recession high of \$7.9 million, the City has experienced a 31% increase in sales tax revenue through FY 2018-19. This is due largely to the growth in business and rebounding fuel prices, but the FY 2018-19 results also include receipts that, due to State's change in reporting software, delayed the remittance of FY 2017-18 funds to FY 2018-19. As such, the FY 2019-20 Budget projects a 6% decrease from the FY 2018-19 unaudited actual of \$10.3 million due, in part, to the FY 2018-19 catch-up sales tax payments from the State of California caused by the implementation of the new State operating system; as well as conservative projections on fuel sales (price and consumption) in the coming year, which is a large component of Hesperia's sales tax revenue. Additional information about retail development is discussed later in this letter.

City Council Priorities

On February 11, 2014, the City Council hosted an agendaized Goal Setting Workshop where a consultant facilitated the integration of multiple goals into a list of the top six City Council Priorities. The goals, which were formally adopted by the Council on February 18, 2014, are as follows:

1. Public Safety – Ensure adequate public safety resources are available for our citizens, families, children, businesses, and visitors.
2. Financial Health – Hesperia will assure its financial health by continuing to provide structurally balanced budgets for its operating funds.
3. Future Development – Actively manage growth to ensure cohesive development including Industrial, Commercial, Residential, Freeway, Main Street and Ranchero Corridors.
4. Future Vision – Agree on a 'vision' of what Hesperia should be in 5, 15, and 25 years (revisit the 'vision' no sooner than once every 5 years).
5. Organizational Health – Establish and maintain a healthy and efficient organization to provide City services.
6. Capital Improvement – Create Capital Improvement Funding after Redevelopment's elimination.



Each year the City Council works with staff to establish planning goals within the framework of these six City Council Priorities which then, based upon funding availability, are incorporated into the annual budget process. For FY 2019-20, the specific projects noted below received funding in advancement of the City Council's Priorities:

- To advance the City Council's Financial Health Priority, the City's Reserve Policy was updated to require a minimum of two (2) months of the annual expenditures be held in cash, as recommended by the Government Finance Officers' Association (GFOA). The specific purpose of the reserves is to provide funding to meet operational appropriation requirements in the event of shortfalls in the level of anticipated revenues or unanticipated expenses. The FY 2019-20 General Fund Budget is balanced with 2.1 months of cash reserves, consistent with the City Council's Reserve Policy.
- To promote the City Council's Future Development Priority, funding in the amount of \$200,000 has been included in the FY 2019-20 Budget in order to complete the implementation of a Pavement Management System; a street assessment program to evaluate and rate the City-wide street infrastructure to determine the specific streets in most need of rehabilitation. This will enable the City to prepare a plan to focus funding on the streets most in need of repair, with the goal of augmenting reliable City infrastructure in order to foster future growth.

More information about the specific priorities for each division, as well as significant changes and expenditure information can be found in the F Section of this budget document.

Issues on the Horizon

Leveraging limited resources to derive the greatest benefit for the good of the entire community is at the heart of the City Council's commitment to conservative fiscal management. This prudent management philosophy made it possible for the City to maintain General Fund cash reserves through the most recent recession without the need for layoffs or furloughing of staff. With a local economy that is progressively improving, Hesperia has taken a cautiously optimistic approach in the preparation of the FY 2019-20 Budget. The noted revenue increases provide optimism that improvement continues, but the City's optimism is tempered with reasonable caution and fiscal conservatism. While proactive measures have been taken to successfully maintain the City's fiscal health, challenges still remain, such as:

Employee Retirement Costs – The City is a member of the California Public Employees' Retirement System (CalPERS), a cost-sharing multiple-employer public employee defined benefit pension plan for its personnel.

In anticipation of increased rates, based upon actions by the CalPERS Board to change its amortization and smoothing policies, the City Council gradually but purposefully moved away from the City bearing the cost of the full 8% employee contribution, to placing that cost reasonably with employees. Initiated well before the California Public Employees' Pension Reform Act of 2013, this funding shift began in FY 2007-08 and by FY 2012-13, employees were paying the full 8% employee contribution.



While this step was important, the City negotiated with employees to go even farther. To further advance the City Council's Financial Health Priority, in addition to paying the full CalPERS member contribution, employees also began paying 1% of reportable earnings as cost sharing of the City's normal costs starting in July 2015.

Despite these steps, CalPERS has announced additional policy changes which will increase the City's pension costs, in an effort to improve the plans' funded status, including reducing the amortization period from 30 to 20 years for future unfunded liabilities and reducing the discount rate from 7.25% for FY 2018-19 to 7.00% for FY 2019-20. CalPERS is attempting to find solutions to reduce its \$146 billion unfunded liability, of which the Hesperia unfunded liability, including the Hesperia Water District, is approximately \$22.4 million. As CalPERS continues to implement these changes, the annual funding requirements of the member agencies will increase over the next several years. Based upon 2019 CalPERS estimates, just the unfunded accrued liability (UAL) portion of the City's annual payment to CalPERS for the City and Water District's plans could reach as high as \$2.4 million by FY 2024-25, a 100% increase over the FY 2018-19 required contribution of \$1.2 million. For FY 2025-26, this amount is estimated to decrease to \$2.1 million, reflecting the complete phasing-in of the reduced amortization period.

In making the annual required contribution, CalPERS offers each agency the option of making monthly installment payments for the full required contribution amount, or an opportunity to make one lump sum payment at the beginning of each fiscal year for a discounted amount, enabling CalPERS to invest the full amount for nearly the entire fiscal year. By making the lump sum payment at the beginning of the fiscal year, for FY 2018-19 the City achieved a savings of approximately \$44,000 for the combined City and Water District plans, which is greater than what the City would have earned through its normal investing practices by making the full required contribution through monthly installment payments to CalPERS.

With respect to the CalPERS plans for the Hesperia Fire Protection District (HFPD), on November 1, 2018 the Local Agency Formation Commission (LAFCO) annexation process for the transfer of Fire District operations to San Bernardino County Fire (County Fire) was complete. As a result, County Fire assumed the responsibility for providing fire protection and ambulance services and the HFPD transferred all assets and liabilities to County Fire, with the exception of the HFPD's former personnel obligations. Hesperia will continue to satisfy the outstanding CalPERS obligations of the HFPD and the City will receive a new source of property taxes. For plans without active employees, such as the HFPD plans, CalPERS reduced the amortization period to 15 years. As such, recent CalPERS projections estimate that the HFPD UAL will level-off at \$1.0 million beginning FY 2020-21, which is an increase of approximately \$200,000 over the FY 2018-19 required contribution of \$797,783. Additional information about the annexation is discussed in the Significant Events of FY 2018-19 section of this document.

Currently, the CalPERS pension payments are a relatively small portion of the City's overall budget; however, with pension reform, changes to CalPERS' actuarial methodologies, and general effects of the economy, it is one of the more volatile expenditures that will have the potential to drastically increase in the future. Due to the projected impact upon future



budgets, the item will be brought before the City Council during FY 2019-20, for purposes of developing a plan to address the increases.

Other Postemployment Benefits (OPEB) – Governmental Accounting Standards Board (GASB) Statement No. 45 and its successor No. 75 require public-sector employers to recognize the cost of postemployment benefits, such as postemployment healthcare, over the active service life of their employees rather than on a pay-as-you-go basis and identify the methods and assumptions that are required to be used to project benefit payments. The resulting unfunded liability is reported in the Comprehensive Annual Financial Report (CAFR).

Hesperia Golf Course & Country Club – The Hesperia Golf Course & Country Club (Golf Course) is a 211 acre, 18-hole course that first opened in 1957 and was a tour stop for the PGA (Professional Golfers' Association). The Golf Course was privately owned until April 2010 when the City purchased it, in part to avoid the potential for blight due to the owner's desire to sell with an unknown outcome, but more importantly for the water rights associated with the property. At the time of the purchase, the City was aware of deferred maintenance of the course and clubhouse from the previous owners. Much of the infrastructure was the same as it was when it was originally constructed in 1957.

At the time of purchase, the City conducted an extensive public outreach program in order for the community to submit input regarding the long-term use of the property. The results of the outreach program indicated overwhelming support to continue to operate the regulated 18-hole golf course and the City entered into an agreement with the Hesperia Recreation and Park District (Park District) to operate and maintain the Golf Course.

Since 2010, the Park District has operated the Golf Course, and during that time annual losses were incurred, as expenditures for its operation have exceeded the revenue generated. While substantive improvements were needed to improve course infrastructure, the City was working through the effects of the Great Recession which had a significant impact upon City revenues and took many years to recover from. As such, some repairs were made, but funds were not available for investment in the course to make improvements. Recently, due to water conservation efforts in California, the Hesperia Water District (Water District) received partial grant funds to construct infrastructure and begin a reclaimed water distribution program. As a result, reclaimed water will be available to the Golf Course beginning in FY 2019-20.

With the Park District contract approaching its expiration date and the Park District expressing its intent not to extend, a Request for Proposal (RFP) was issued for the operation of the Golf Course. One respondent with extensive experience in golf course management was identified; however, start-up costs, needed repairs, projected operating losses, and fees to manage the course are projected to be \$1.2 million for FY 2019-20, with total costs to the City estimated at \$3.7 million over a 5-year period.

Due to the financial impact, on August 20, 2019 the City Council provided direction to staff to move forward with a contract with the golf course operator to avoid a disruption of service, while also conducting a feasibility study for a community facilities district (CFD) to explore the



potential of providing a funding mechanism for Golf Course operation and enhancements by the citizens who receive a direct benefit of living near the Golf Course. Upon receiving the results of the six-week feasibility study, the City Council will revisit the issue to determine the next steps in order to address this issue.

Significant Events of FY 2018-19

- In June 2019, the Hesperia City Council approved the FY 2019-20 Budget which provides an additional \$2,466,776 of funding for its annual Road Improvement Program. These funds are used to enhance streets throughout the City and are in addition to the ongoing Street Maintenance Program. Over the last nineteen years, this program has reconstructed over 317 miles of roads, with an additional 98 miles of slurry-sealed roads.
- On November 1, 2018 the Local Agency Formation Commission (LAFCO) annexation process for the transfer of Hesperia Fire Protection District (HFPD) operations to San Bernardino County Fire (County Fire) was completed. The HFPD had experienced years of ongoing revenue challenges to meet increasing fire protection costs.

Despite efforts to reduce expenditures wherever possible and reorganizing positions to minimize increases in the annual contract for fire protection services with the County of San Bernardino, reserves were depleted. A failed parcel tax measure in November 2011 resulted in the need to reduce the contract with San Bernardino County Fire Department by nine positions and the closure of Fire Station 301 in January 2012.

The City Council pursued multiple options to resolve the financial difficulties of the HFPD, including a two-year \$2 million Staffing for Adequate Fire & Emergency Response (SAFER) grant (which temporarily added 18 Limited Term Firefighter Paramedics) and a Joint Powers Authority (JPA) feasibility study with neighboring cities. Facing a lack of interest in pursuing the creation of a JPA and the ultimate conclusion of the SAFER grant, the City Council worked with County Fire to initiate an annexation process wherein County Fire would assume the fire protection and ambulatory services within Hesperia.

The annexation was approved by LAFCO board in May 2018 and on November 1, 2018 County Fire assumed the responsibility for providing fire protection and ambulance services and the HFPD transferred all assets and liabilities to County Fire, with the exception of the HFPD's former personnel obligations. Hesperia will continue to satisfy the outstanding CalPERS obligations of the HFPD and the City received a new source of property taxes.

- The City is proud to have been awarded more than \$5 million as a result of State and Federal grant programs. This funding will supplement City funds for much needed infrastructure improvements:
 - The City was awarded \$3.9 million as part of the California Transportation Commission's SB1 Local Partnership Program for the Rancho Widening Project, which will widen five miles of Rancho Road from two to four lanes and include



- features such as construction of a new bridge over the aqueduct, installation of signals and construction of a rail crossing.
- In December 2018, the City was awarded \$0.3 million as part of CalRecycle's Rubberized Pavement Grant Program to assist with repaving via rubberized asphalt. This rubberized asphalt mix will be used for approximately 1.2 miles on Main Street between La Junta Road and Escondido Avenue, as well as approximately five miles of Ranchero Road from Mariposa Road to Seventh Avenue.
 - The City received a federal Highway Safety Improvement Program grant for a traffic signal at the intersection of Main Street and Timberlane Avenue. The project will install a traffic signal, widen the roadway to accommodate left turn pockets, install sidewalks, crosswalks, and lighting. This intersection was identified as a safety priority by the City, with the cost of the project at \$1.2 million, supplemented with \$0.9 million of grant funding.
 - The City Council implemented a new program to assist non-profits in the City of Hesperia. The new Community Assistance Program (CAP) replaced the Housing and Urban Development (HUD) funded Community Development Block Grant (CDBG) sub-recipient program that the City previously used. The CAP, funded by the General Fund, was created to enable non-profits to spend more time helping Hesperia residents and less time on administrative paperwork. By utilizing this new program, CDBG funds are now being allocated for street improvement projects within the approved CDBG target areas.
 - The City hosted its 13th annual Youth in Government Day event for 20 high school seniors, which included presentations by senior management on departmental operations, City facility tours, questions and answers with the Mayor, and a mock City Council meeting.
 - Water conservation continues to be an important issue for California cities. In order to best utilize the community's water resources, the Hesperia Water District (Water District) is working with the Victor Valley Wastewater Reclamation Authority to bring a sub-regional recycled water facility to the community which will deliver tertiary treated water to recycled water customers in Hesperia. The Civic Center, as well as some parks and schools, have been fitted with purple pipe in order to take advantage of this resource. The Water District secured a \$2 million Proposition 84 Drought Relief Grant, as well as a \$4.7 million Proposition 1 Grant and a low interest loan through the California State Revolving Fund (SRF) Loan program to construct a storage reservoir, pump station, and approximately 8 miles of pipeline that will be used to transport recycled water to purple pipe locations such as the golf course, local schools, and parks. This will serve two important purposes; 1) reduce the flow of wastewater to the treatment plant and 2) lessen the demand on potable water for landscape irrigation purposes, thereby saving financial resources as well as precious water resources. Construction continued in FY 2018-19 and completion of the project is expected in January 2020.



- To recognize residents that have added to the charm of the community and enhanced their home's curb-appeal, the City implemented a Pride Enhancement Program. The program is aimed at beautifying Hesperia neighborhoods by creating a quarterly home beautification contest that recognizes homes that have been improved through enhanced landscaping, façade improvements and other upgrades that add to the appeal of the neighborhood. The goal of this program is to shine a light on the people in Hesperia that help to make our City a great place to live and work.
- Due in large part to a Mobile Source Emission Reduction Grant via the Mojave Desert Air Quality Management District, real-time adaptive traffic signal controllers are being installed at intersections along the Main Street corridor. These signal controllers utilize the latest technology to adjust signal timing based upon existing traffic at and approaching the intersection. Communication equipment was also installed, allowing the controllers to communicate with each other along the corridor, resulting in the efficient movement of traffic through the corridor. Phase I of this project installed real-time adaptive signal controller technology at eight intersections along the Main Street corridor from "I" Avenue to Eleventh Avenue, improving east/west travel. Phase II of the project will install the same type of system at an additional eight intersections from Escondido Avenue to Mesa Linda Avenue, with project completion anticipated in Spring 2020.
- In an effort to provide more efficient response times for small, non-structural modification projects, the City implemented an Over-The-Counter (OTC) plan review program. Minor construction projects such as residential rooftop solar, patio covers, swimming pools, HVAC change-outs, minor plan revisions, and tenant improvements are now being completed over the counter every Tuesday afternoon.
- In September 2018, the City, as Successor to the Former Hesperia Community Redevelopment Agency refinanced the Agency's former 2005 Series A Tax Allocation Bonds and its 2007 Series A (Tax Exempt) and Series B (Taxable) Revenue Bonds into Successor Agency 2018 Tax Allocation Refunding Bonds, achieving a \$19.0 million net present value savings which translates to an average annual savings of \$2.2 million. The underlying fundamentals of these bonds enabled the refinancing to secure a rating of A+ from Standard and Poor's. The savings achieved with this refinancing will result in additional pass-through revenue to taxing entities in the area, including an estimated annual \$1.3 million to Hesperia Unified School District and \$300,000 to Victor Valley Community College.
- Retail development continues in Hesperia:
 - In May 2019, Mama Carpino's, a foodie favorite of many residents in the High Desert, began construction on a restaurant in Hesperia, offering a great culinary option with a view of Civic Plaza Park.
 - Texas Roadhouse Grill, an 8,500 square foot restaurant hosting 200+ guests opened their first High Desert restaurant in April 2019.



City of Hesperia

- Culichi Town, specializing in Sinaloa style, Asian fusion dishes will also be making an entrance in 2019. Distinguished by the wide variety of seafood utilized in their recipes, from sushi to tacos to tostadas, Culichi Town aims to spice up Hesperia and the surrounding Victor Valley community with authentic Sinaloan flavors.
- Mexico Lindo, a family owned restaurant, known for their high-quality delectable cuisine, is now open on Main Street in Hesperia.
- Western International Gas opened escrow on eleven acres for their acetylene manufacturing plant near the "G" Avenue Rail Spur.
- Mag Bay Yachts began construction on their 78,000 square foot boat manufacturing facility.
- Kaiser submitted plans for their 55,000 square foot medical campus on 9.9 gross acres and construction will begin late 2019.
- Kahoots completed construction on their 15,000 square foot pet supply store and their official opening was held in August 2019.
- Plans were submitted for a shopping center in Hesperia located on Bear Valley Road, across from Victor Valley College. Aldi supermarket will anchor the center.

Conclusion

The Fiscal Year 2019-20 Budget continues to support services, maintenance, and infrastructure. Transportation projects remain a priority for Hesperia. Sustaining the momentum from the opening of the much anticipated Ranchero Road Interchange in FY 2014-15, progress continues with right-of-way acquisition for the Ranchero Road Widening and Aqueduct Crossing projects, in addition to funding for the installation of three traffic signals along the same essential thoroughfare.

Due to the continued strong, responsible leadership and prudent fiscal policy direction of the City Council, the City of Hesperia is well positioned to leverage federal and state grant funding, with City match requirements, to construct critical City infrastructure improvements for the benefit of the community; and I'd like to express my sincere appreciation to the Council, as well as the staff members and community partners who have contributed to this process.

Respectfully submitted,

Nils Bentsen
City Manager