



CITY OF OAKLAND FINANCIAL CONDITION FOR FISCAL YEARS 2012-13 TO 2018-19

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April 16, 2020

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April 16, 2020

HONORABLE MAYOR SCHAAF
HONORABLE CITY COUNCIL
INTERIM CITY ADMINISTRATOR
RESIDENTS OF OAKLAND
OAKLAND, CALIFORNIA

RE: CITY OF OAKLAND FINANCIAL CONDITION FOR FISCAL YEARS 2012-2013 TO 2018-2019

Dear Mayor Schaaf, President Kaplan, Members of the City Council, Interim City Administrator Falk, and Oakland Residents:

The attached audit report provides information on the City of Oakland's financial activities and its financial health prior to the COVID-19 pandemic. The impetus for this report was twofold: to provide the public and City leaders with an easily digestible account of the City's financial health and assist decision makers in visualizing the City's course, consider options, and make adjustments to improve the City's long-term financial condition. The current COVID-19 pandemic will likely dramatically compound the issues raised in this report.

As you read this report, I believe one theme will be prominent: Oakland does not rank favorably in most financial indicators, when compared to similar-sized California cities. This is not a new revelation—the State Auditor recently ranked Oakland as the 13th top city facing fiscal challenges in California.

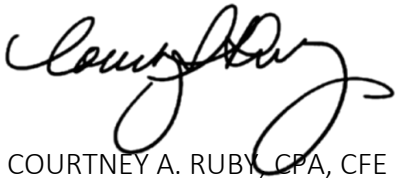
On a similar note, the United States Government Accountability Office affirmed in its *State and Local Government Fiscal Outlook: December 2018 Update* that the public sector fiscal challenges are not just cyclical, and few public employers will grow their way out of such pressures. In fact, the GAO predicts that closing the structural fiscal gap would require action

equivalent to a long-term 15% cut in state and local government spending. And, this was before the COVID-19 pandemic hit.

Consequently, state and local governments will need to rethink their fiscal strategies to survive. I believe City leaders must pause and reflect on two questions: 1) how will City officials move the needle quickly enough to place Oakland's financial future on solid footing in the midst of COVID-19, and 2) what are the opportunities COVID-19 affords us to work differently, more efficiently, and become more focused on the core government services our residents rely upon.

It is my sincere hope that we seize this moment as an opportunity to engage with stakeholders and innovators at every level of government. We must ask more thought provoking questions and harness our collective will to seek novel solutions to transform the City's financial future.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Courtney A. Ruby', with a stylized, flowing script.

COURTNEY A. RUBY, CPA, CFE
City Auditor

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INTRODUCTION

Audit Overview

This report provides residents and public officials with information on the City of Oakland's (City) financial health prior to the COVID-19 global pandemic (COVID-19). Our audit objective was to examine the City's financial well-being by calculating financial ratios, analyzing trends in the City's financial data over the past seven-year period, and comparing the results to other cities of similar size. We used information, primarily from the City's audited Comprehensive Annual Financial Reports (CAFR) to identify favorable and unfavorable financial trends at a high level.

For public officials and residents, independently assessing the City's financial health is a daunting task requiring an understanding of the City's CAFRs and Fiscal Year Budgets. These documents can be technical, lengthy, and not particularly designed for public consumption. Financial analysis, using financial ratios, can be used to draw meaning and give a voice to financial statements. Additionally, the City's financial statements reflect a single snap shot in time. This report focuses on historical trends over seven years and benchmarks the City with seven comparably sized cities in California.

Therefore, this report aims to 1) be an easily digestible account of the City of Oakland's financial activities and financial condition prior to COVID-19 and 2) assist decision makers visualize the City's course, consider options, and make adjustments to improve the City's long-term financial health.

The scope of this report covers Fiscal Years (FY) 2012-13 to FY 2018-2019, ending June 30, 2019. The report does not address the impact of the COVID-19 pandemic on the City's financial condition. This report, however, will provide a baseline for assessing the impact of the pandemic on the City's future financial condition. Therefore, we will issue a follow-up report next year, so the City may closely monitor the impacts of the COVID-19 pandemic on Oakland and other California cities included in this report.

Defining Financial Condition

Financial condition refers to a government's ability to (1) generate enough cash over thirty or sixty days to pay its bills, (2) generate enough revenues over its normal budgetary period to meet its expenditures, (3) pay all the costs of doing business in the long run, and (4) provide services required for the health, safety, and welfare of the community, and at the level and quality its residents desire.

Understanding the City's Financial Activities

Understanding the City's financial activities, provides insight into how the City's finances are managed. The City sets up procedures for keeping track of what is collected (revenues) and spent (expenses) by breaking them down into two major areas, as defined by Government Accounting Standards:

- **General governmental activities** are general programs and departments funded by residents and can be used by or for the benefit of anyone who lives and works in, or travels to Oakland. Some of these governmental activities include public safety, community services, community and economic development, public works and transportation. These activities are primarily supported by taxes and intergovernmental revenues.
- **Business-type activities** are City operated programs that do not receive general tax revenue to support their operation. In Oakland, this includes the sewer service system and some parks and recreation programs. These operations recover most of their costs through user fees and charges.

These activities are further classified into restricted and unrestricted funds. Restricted funds are established by local ordinances, the City Charter, federal and state laws, and grant agreements, specifying how the monies can be spent. Unrestricted funds can be used by City management as they wish for any lawful purpose.

Each year the City prepares its financial statements with the collected financial information for governmental and business-type activities. These are audited by an independent Certified Public Accountant and are made available to the public in the CAFR.

City budget documents also provide significant financial information to decision makers and the public. The City's budget serves as a financial plan and policy document describing how the City intends to use projected revenues to perform operations or provide services (expenditures) over a defined period. Oakland has a biennial budget cycle (occurring every two fiscal years) that begins on July 1 and ends on June 30.

Assessing Financial Condition

Several methods are available for assessing a local government's financial condition. We primarily used the financial and economic indicators included in the *International City/County Management Association's Evaluating Financial Condition Handbook for Local Government*. In this report, our assessments are organized around seven areas: (1) revenues, (2) expenditures, (3) long-term debt and liabilities, (4) pension and Other Post-Employment Benefit (OPEB) liabilities, (5) financial and operating position, (6) capital assets, and (7) demographic and economic indicators.

How is Oakland's Financial Health?

This report does not include information on the condition of the City's infrastructure, the citywide asset replacement value, or the funding gap for infrastructure needs because the City does not produce an annual citywide capital asset report.

Prior to the COVID-19 global pandemic, Oakland's financial health was relatively stable. Based on our financial analysis through FY 2018-19, revenues had increased, debt was down, the City had a balanced annual budget, and the City's liquidity and credit ratings were strong. This report prepared prior to COVID-19, however, illustrates the City needs to do more to address its increasing pension and OPEB liabilities, quantify its unmet infrastructure needs, and prepare for the future in which, according to the City's five-year forecast issued in March 2019, expenses are expected to outpace revenues. The City must now pivot to address the immediate and long-term effects of COVID-19, many of which remain unknown.

During our audit, we found the City's total net position, the difference between what a government owns and what it owes, has declined significantly. The primary reason for the decline is due to increasing liabilities related to pensions and OPEB. While these costs are not new, the requirements for state and local governments reporting¹ these costs have changed significantly during the seven-year period we audited. Additionally, we analyzed unrestricted net position, a more realistic and revealing long-range indicator of the City's financial condition. We found that the City's unrestricted net position remained negative over the entire seven-year period indicating the City's long-term commitments are greater than its available resources.

The City and State have taken steps to rein in pension expenses and the City has taken steps to fund more of its OPEB liability during the audit period. In 2013, the Public Employees' Pension Reform Act (PEPRA) became State Law, reducing long-term costs by restricting pension provisions and increasing flexibility for employee/employer cost sharing. In response, Oakland initiated its third pension tier for employees hired in or after 2013. Although PEPRA provides the City some long-term pension relief, the short-term benefits are minimal.

Additionally, in FY 2017-18 and FY 2018-19, the City agreed to contribute \$10 million annually to an OPEB Trust to pay for future OPEB benefits and approved an OPEB Funding Policy to close the funding gap by contributing an additional 2.5 percent of payroll beginning in FY 2019-20. The City will pay additional one-time

¹Government Accounting Standards Board (GASB) requires governments to disclose all unfunded pension (GASB 68) and other post-employment (GASB 75) benefits on their balance sheets.

contributions to the OPEB Trust when excess Real Estate Transfer Tax (RETT) thresholds are met. Additional long-term relief to the City's OPEB liability occurred in FY 2018-19, when the City reached an agreement with its sworn public safety employees (Fire and Police) to cap retiree medical benefits for existing employees and implement new, lower-cost OPEB tiers for employees hired after January 1, 2019.

While government reserves are the cornerstone of financial flexibility, the audit found that a higher level of unassigned funds and reserve balance is needed to protect residents and employees from unexpected changes in financial condition. The current COVID-19 crisis unfortunately illustrates this point as the City must continue to set aside reserves when the City needs additional cash.

Another area of financial exposure is the City's infrastructure, which are the City's assets such as streets, buildings, utility networks, and equipment. The audit was unable to include information on the condition of the City's infrastructure, citywide asset replacement value, or the funding gap for infrastructure needs because the City does not produce an annual city-wide capital asset report. Without quantifying these costs in one place, the City cannot begin to adequately determine the future monies it needs to address our future infrastructure needs.

Throughout the report, we have compared Oakland's financial indicators to California cities with similar population size and government services provided. It is important to note that in most cases Oakland ranks as the highest or the worst. Each city's circumstances are different, yet it is important to consider how these city's past financial choices can inform Oakland's future.

01

REVENUES

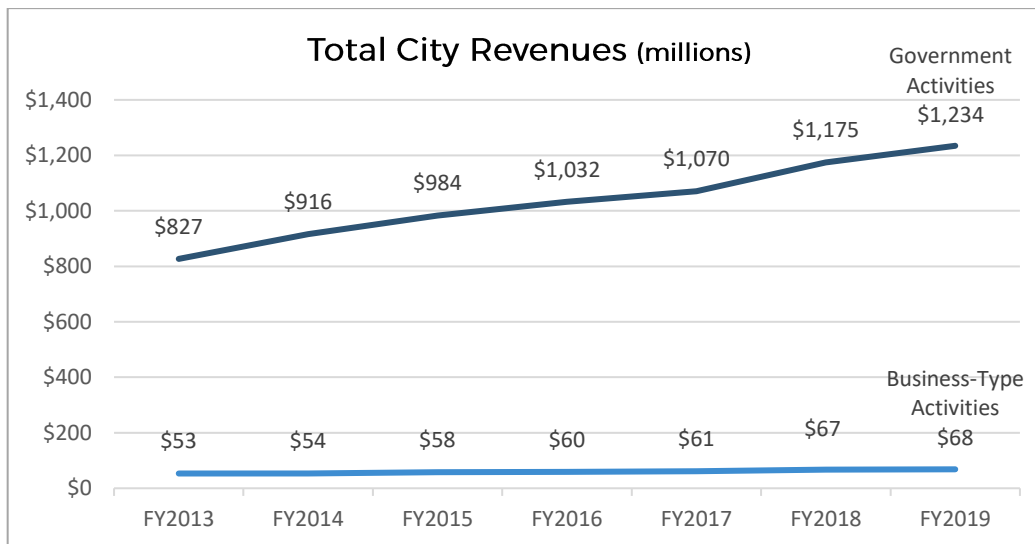
What Are Revenues?

Revenues determine the City's capacity to provide services. Diverse revenue sources can help the City withstand changes in the local or regional economy. Oakland's revenues are diversified and include property taxes, state taxes, other local taxes, charges for service, operating grants, one-time revenues,² contributions, and other revenues.

City Revenues

The City's total revenues (governmental activities + business-type activities) have increased from \$880 million in FY 2012-13 to \$1.303 billion (+48%) in FY 2018-19. Revenues related to governmental activities have grown from \$827 million in FY 2012-13 to \$1.234 billion (+49%) in FY 2018-19. Business-type activities increased by from \$53 million in FY 2012-13 to \$68 million (+28%) in FY 2018-19, mainly related to sewer-related activities.

Exhibit 1: City revenues for governmental and business-type activities from FY 2012-13 through FY 2018-19 (millions)

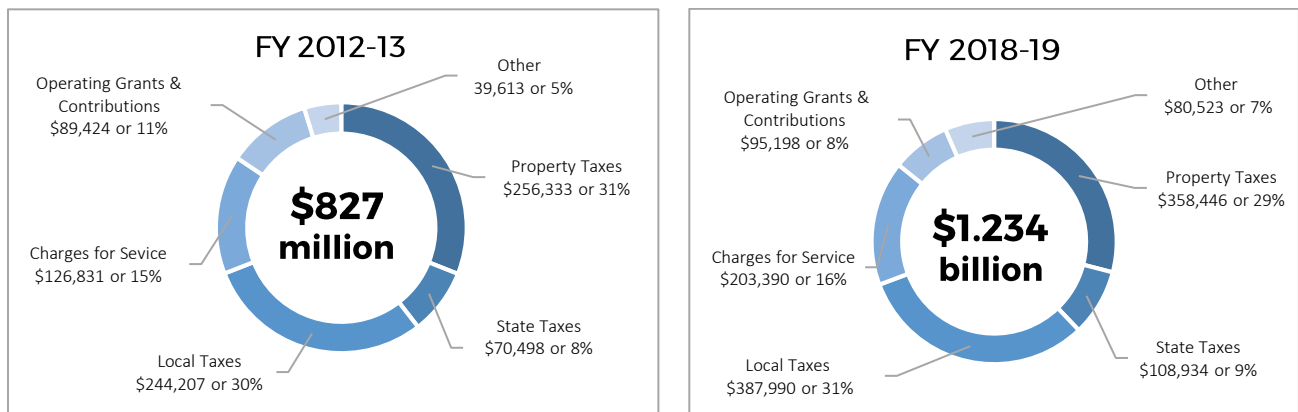


Source: Oakland CAFRs

² Financial proceeds that will not likely occur on an ongoing basis, such as sales of property or proceeds from the refinancing of debt. Fiscal prudence and conservancy require that one-time revenues not be used for recurring expenses as further detailed in the City's financial policy.

The City relies heavily on property, state and local taxes. Between FY 2012-13 and FY 2018-19, combined revenue from property, state and local taxes consistently accounted for about 70 percent of total revenues used to support governmental activities. Exhibit 2 shows the governmental activities revenue breakdown by revenue source.

Exhibit 2: City of Oakland revenues for governmental activities by source in FY 2012-13 and FY 2018-19 (thousands)



Source: Oakland CAFRs

While the City's FY 2018-19 governmental revenue is at a staggering \$1.2 billion, it is restricted from spending the majority of these funds. For example, tax revenues are largely unrestricted, while grant revenues are restricted by the grant agreement and often require matching contributions from other sources. Special revenues include voter-approved measures and are restricted for a specific purpose. Revenue from fines and penalties are largely unrestricted and result from enforcement activities.

Exhibit 2 shows that total governmental activities revenue increased by \$408 million, or 49 percent, between FY 2012-13 and FY 2018-19. Revenue growth has occurred in almost every revenue category (see Appendix A for a seven-year summary of revenues by type for governmental activities and percentage changes from FY 2012-13 through FY 2018-19). Some of these revenues are more susceptible to economic fluctuation, however revenue growth is primarily attributed to the increases in:

- **Real estate transfer tax (RETT)** which is a highly volatile revenue source and can increase and decrease rapidly with changing market conditions. RETT rate on residential and commercial sales was 1.61 percent of the value of each real estate transaction, until December 31, 2018.³ Oakland's share was 1.5 percent with Alameda County receiving the remaining 0.11 percent. The recent

³ On November 6, 2018, Oakland voters approved Measure X, establishing a progressive real estate transfer tax rate for the City. The new rates became effective on January 1, 2019 and are as follows: 1% up to \$300,000; 1.5% over \$300,000 to \$2 million; 1.75% over \$2 million to \$5 million; and 2.5% over \$5 million.

growth in RETT has been largely due to the sale of large commercial buildings and the City recently experiencing double digit year after year growth in home prices. Since FY 2012-13 revenue from RETT grew \$57 million, or 121 percent, but the increase was not a steady year after year increase.

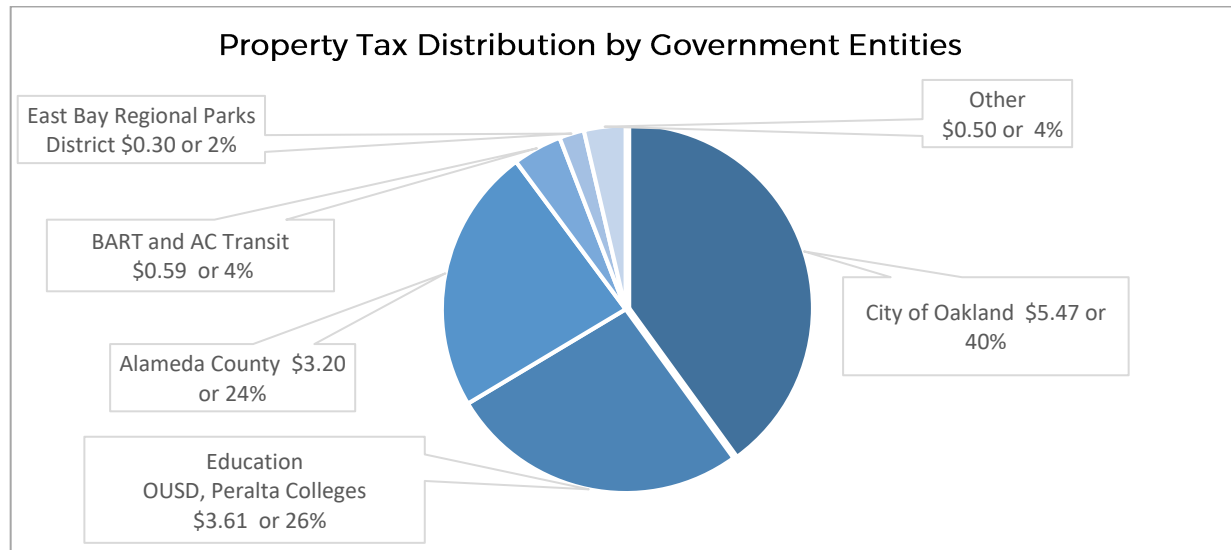
- **Sales and use taxes** apply to the retail sale or use of tangible personal property. The total sales tax percentage in the City of Oakland is 9.25 percent meaning on a \$1 taxable purchase, the sales tax paid is 9.25 cents. The City receives 1 percent of the total sales – meaning 1 cent on a \$1 purchase. The remaining 8.25 percent is allocated to the State and local taxing districts. Revenues from sales and use taxes increased by \$32 million, or 53 percent since FY 2012-13.
- **Business license tax (BLT)** has been a relatively steady and reliable revenue source for the City. However, BLT is impacted by the health of the economy as recessions considerably slow down business activities. BLT revenues grew by \$39 million, or 65 percent since FY 2012-13.
- **Property tax** is the largest single source of revenue for the City and has grown year after year, at an average pace of 5.9 percent. The growth for the period was accelerated by a rapid run-up in housing demand, new construction and development. Since FY 2012-13 it grew by \$102 million, or 40 percent.

Where Do Your Property Taxes Go?

As noted above, the City relies heavily on property taxes as a revenue stream. In the seven-year period beginning in FY 2012-13, property tax revenues grew by 40 percent. Property taxes are based on a property's assessed value. The County of Alameda is responsible for assessing, collecting, and distributing property taxes in accordance with enabling State law, and for remitting such amounts to the City.

The property tax rate in FY 2018-19 for the City of Oakland was \$13.67 per \$1,000 of assessed value. Property taxes are divided among several government entities as demonstrated in Exhibit 3. The City receives approximately \$5.47 or 40 percent of the total tax collected.⁴

⁴ The City receives approximately 40 percent of total tax collections that is broken down by: (1) Basic Rate (25.5%), (2) Debt Service Fund (3%), and 1981 Pension Liability (11.5%).

Exhibit 3: Property Tax Distribution by Government Entities

Source: Oakland CAFRs

Over the years, voters have approved special parcel taxes and special assessments that are part of the property owners' tax statement. Citywide, these special taxes include Measures Q, D, M, N, Z and the Landscape and Lighting Assessment District.⁵

Some of these local parcel taxes, such as the pension override tax, increase with assessed property values; some local parcel taxes, such as the landscape and lighting district and the vacant property tax, do not adjust. Some local parcel taxes, such as paramedic emergency services parcel tax (Measure N) adjust with the consumer price index (CPI). These various assessments fund important public services, such as libraries (Measures Q & D), violence prevention and public safety (Measure Z). In FY 2018-19 citywide, these special taxes added up to \$427/single residential household. Voters also approved parcel taxes that appear as an assessment on the local property tax bills of real property owners whose property falls within the boundary of the assessment district.

How FY 2018-19 Property Taxes, Special Taxes and Special Assessments Were Spent

In FY 2018-2019, the City received approximately \$408 million in property taxes, special parcel taxes and special assessments. These taxes paid for the following services and obligations:

- General purpose services such as police, fire and public works (49 percent),
- Pension bond payments for the Police and Fire Retirement System (26 percent),

⁵ Landscape and Lighting Assessment District (LLAD) is to raise funds to support improvements and maintenance of the City's park areas, landscaping areas, and street lighting. The assessments differ between residential and non-residential parcels in each benefit zone.

- Municipal services such as emergency medical services, paramedic services, library services, public safety and violence prevention services, homeless services (17 percent),
- Debt payments on general obligation bonds (7 percent), and
- Programs under the Affordable Housing Trust fund related to housing and human services (1 percent).

Exhibit 4 shows how these taxes were allocated in FY 2018-19.

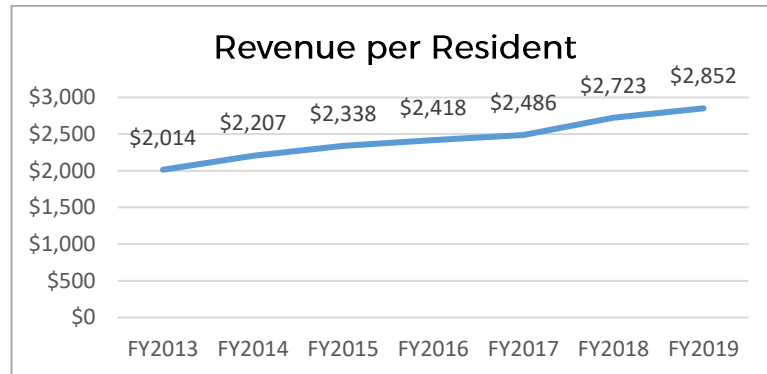
Exhibit 4: FY 2018-19 allocation of City property tax dollars (\$408 million)



Source: Oakland CAFRs and Oracle Reports

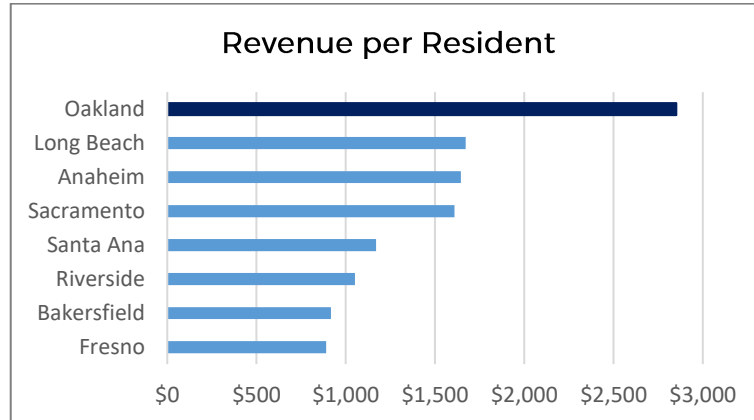
City Revenues Per Resident

Another way of reviewing revenues is on a per resident basis. Oakland's population grew by 5.45 percent over the last seven years. As population increases, revenues and the need for services may increase proportionately with population growth. If revenues decrease, the City may be unable to maintain existing service levels unless it finds new revenue sources or reduces costs. Over the last seven years, revenue per resident increased 42 percent, from \$2,014 to \$2,852 as Exhibit 5 below shows.

Exhibit 5: Seven-year summary of governmental activities revenue per resident

Source: Oakland CAFRs

Additionally, the revenue per resident was compared with California cities with similar population size and government provided service. As Exhibit 6 demonstrates, Oakland has the highest revenue per resident of the seven cities benchmarked. In FY 2018-19 Oakland's revenue per resident was \$2,852 while benchmarked cities revenues ranged from \$891 to \$1,671.

Exhibit 6: Revenues per resident for governmental activities and comparison between cities for FY 2018-19

Source: Oakland and other cities CAFRs

02

EXPENSES

What Are Expenses?

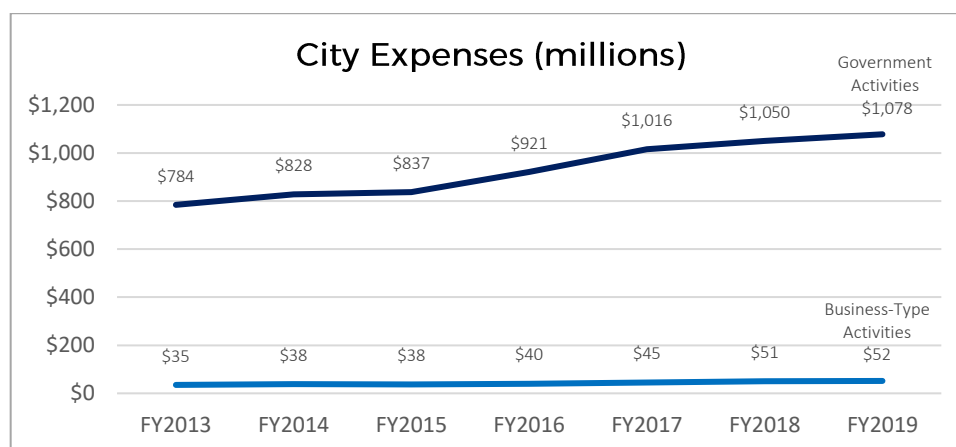
Expenses are the City's costs for providing services. Ideally, the City's expense growth rate will not exceed its revenue growth rate, and the City will have maximum flexibility to adjust spending. There are two key categories of expenditures: personnel and operations & maintenance (O&M). Personnel expenditures are used to pay for City employees to perform various functions and provide services to the public. These costs are expended via the City's payroll and benefits systems and include salaries, overtime, premiums, retirement, and healthcare costs. O&M expenditures are used to pay for anything other than City employees and are expended through the contracting, purchasing, and payables systems. O&M expenditures include contracts for services, supplies and materials, utilities, equipment purchases and debt payments.

City Expenses

As shown in Exhibit 7, the City spent \$1.08 billion in FY 2018-19, surpassing the previous peak of \$1.05 billion in expenditures the previous fiscal year. Expenses related to governmental activities increased 37 percent from FY 2012-13 through FY 2018-19.

Expenses related to business-type activities increased 47 percent during the same period. Business activities recover all or a significant portion of expenses through user fees and charges. Business activity revenues have exceeded expenses for the last seven years.

Exhibit 7: City expenses for governmental and business-type activities from FY 2012-13 through FY 2018-19 (millions)



Source: Oakland CAFRs

As shown in Exhibit 8, the City's expenses are categorized into the following service areas:

- General Government
- Public Safety
- Community Services
- Community and Economic Development
- Public Works and Transportation
- Interest on Long Term Debt

In FY 2018-19 general government expenses increased by \$89.2 million, or 80.7 percent, due to:

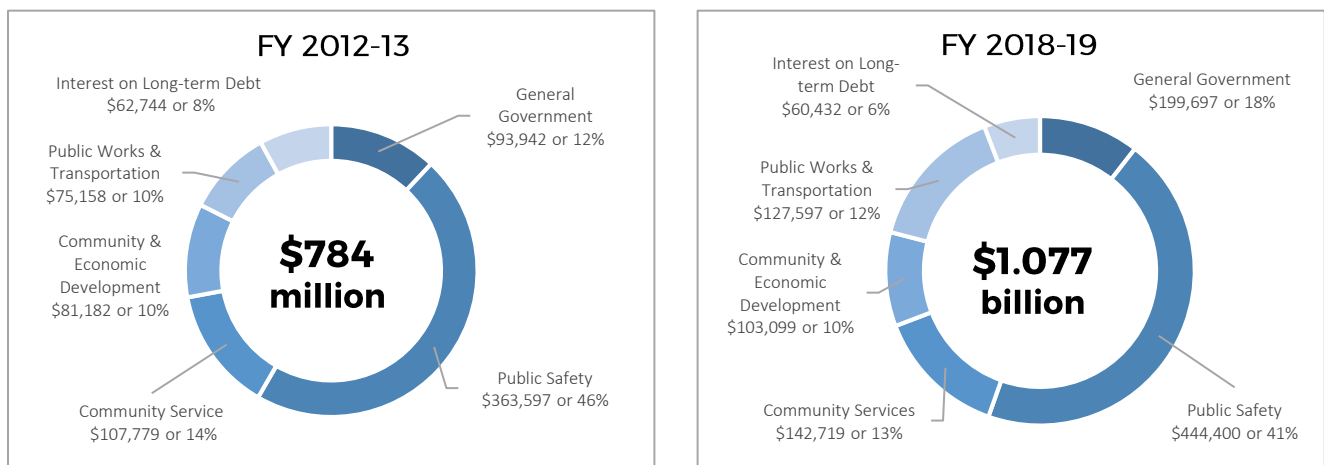
- Re-categorization of:
 - the Police and Fire Retirement System (PFRS) of \$44.9 million previously reflected in Public Safety,
 - capital improvement costs of \$31 million previously reflected in Public Works and Transportation, and
- PFRS contribution of \$6.6 million, and other personnel cost increases.

Public safety was the City's largest expense by service area for the last seven years. These expenses are related to the Police and Fire Departments and accounted for \$444.4 million, or 41 percent of all expenses in FY 2018-19.

The Public Works and Transportation Department accounted for one of highest growth in governmental expenses over the last seven years. The 70 percent increase is likely due to expenditures costs associated with the new Department of Transportation.

Interest on long term debt was the only area in which expenses decreased over the last seven years, decreasing from \$62.7 million in FY 2012-13 to \$60.4 million in FY 2018-19.

Exhibit 8: City of Oakland expenses for governmental activities by source in FY 2012-13 and FY 2018-19 (thousands)



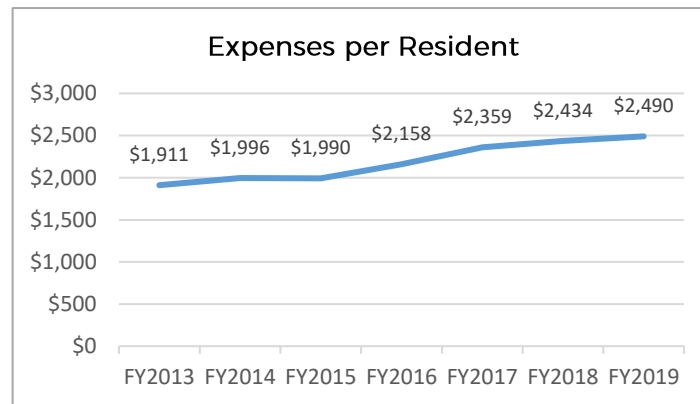
Source: Oakland CAFRs

City Expenses Per Resident

For a seven-year summary of expenses by type for governmental activities and percent change from FY 2012-13 through FY 2018-19 (thousands), see Appendix B.

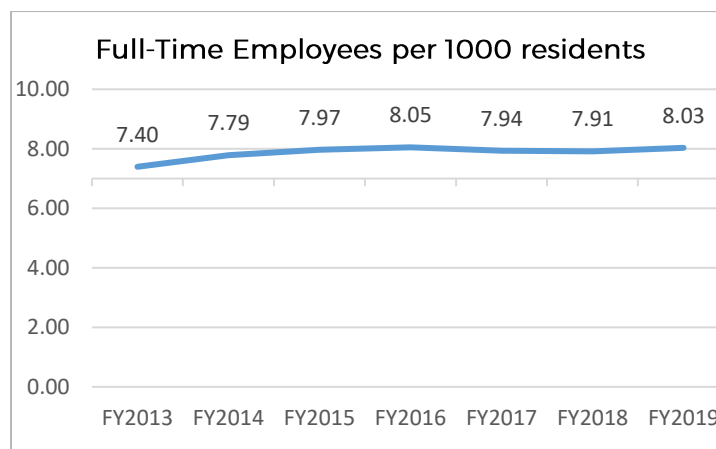
The City's expenses per resident, related to governmental activities, increased by 25 percent from \$1,911 in FY 2012-13 to \$2,490 in FY 2018-19, as seen in Exhibit 9. During the same period, the City's population grew 5.45 percent. Thus, the City's expense per resident grew nearly five times the rate of population growth. Furthermore, the number of full-time employees (FTEs)⁶ per 1000 residents had a modest increase from 7.4 to 8.03 from FY 2012-13 to FY 2018-19, as shown in Exhibit 10. Such an increase in expenses could indicate new services were added, and/or service delivery has become more expensive.

Exhibit 9: Seven-year summary of governmental funds expenses per resident



Source: Oakland CAFRs

Exhibit 10: City of Oakland full-time employees per 1,000 residents from FY 2012-13 through FY 2018-19

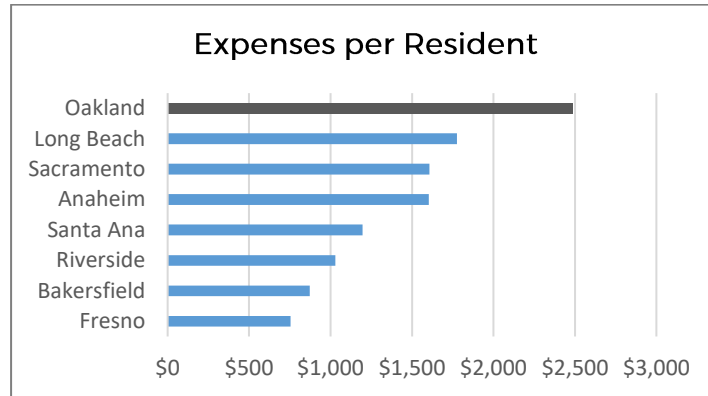


Source: Oakland CAFRs

⁶ An FTE is the hours worked by one employee on a full-time basis or the hours worked by several part-time employees added together into a full FTE.

As Exhibit 11 shows, Oakland has the highest expenses per resident of the benchmarked cities. In FY 2018-19 Oakland's expenses per resident was \$2,490, while the benchmarked cities expenses per resident ranged from \$755 to \$1,775.

Exhibit 11: Expenses per resident and comparison between cities for FY 2018-19

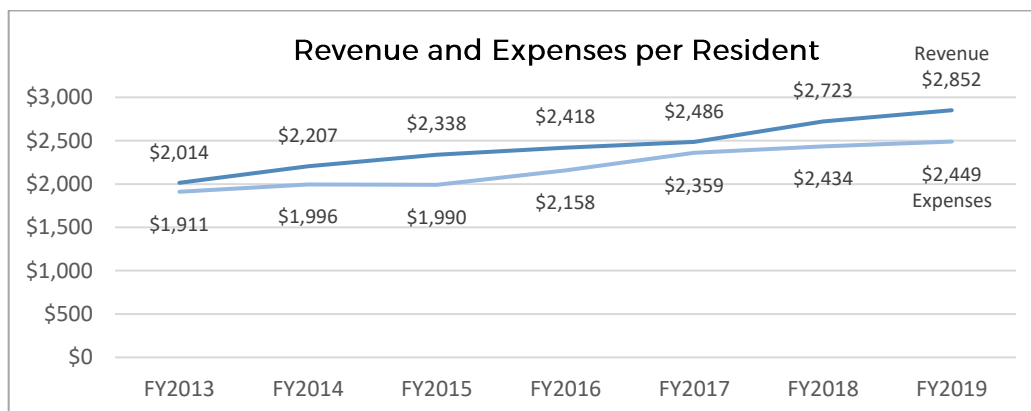


Source: Oakland and other cities CAFRs

Revenue related to governmental activities have exceeded expenses annually for the last 7 years as shown in Exhibit 12. The City's revenue per resident related to governmental activities increased by 42 percent from FY 2012-13 to FY 2018-19, while expenses per resident related to governmental activities increased by 30 percent during the same period. The trend in revenues exceeding expenses is in part due to the local economy that has experienced strong sales, business and property tax growth for the last couple of years.

While revenues per resident exceed expenses per resident, this analysis does not incorporate the portion of revenues that is restricted and not available to meet the annual operating expenses of the government. The net position analysis presented later in the report analyzes the resources available for the City to use for providing services after its debts are settled and its fund restrictions are factored in.

Exhibit 12: Revenue and expenses per resident for governmental activities between FY 2012-13 and FY 2018-19



Source: Oakland CAFRs

03

LONG-TERM DEBT and LIABILITIES (not including pension and OPEB)

What Is Long-Term Debt?

The City borrows money to pay for major capital improvements and long-term obligations. By borrowing money, the City can spread costs across many years. The majority of the City's long-term debt (not including pension and OPEB) comes from issuing bonds. A bond could be thought of as an I.O.U. between the lender and borrower that includes the details of the loan and its payments. To borrow money, the City issues four different types of bonds to fund governmental activities:

Exhibit 13: City of Oakland bond types as of FY 2018-19

Bond Type	Used to Support or Fund	Funded by
General obligation bonds	Infrastructure improvements (e.g. Measure KK, Measure DD, Measure G)	Property Taxes
Lease revenue bonds	Payment for improvements on the Oakland Administration Buildings	Lease payments made by the City's General Fund
Pension obligation bonds	A portion of the City's unfunded actuarial accrued liability for retirement benefits to members of the Police and Fire Retirement System (PFRS)	Primarily funded by property taxes
Special assessment district bonds	Improvements in specific assessment districts. (e.g. Underground street lighting in Piedmont Pines neighborhood)	Assessments levied on real property within specific assessment districts

How Much Long-Term Debt Does the City Have?

The City's total outstanding bond debt decreased 28 percent from \$1.044 billion in FY 2012-13 to \$751 million in FY 2018-19. Exhibit 14 shows the changes in the composition of the City's bonded debt from FY 2012-13 to FY 2018-19.

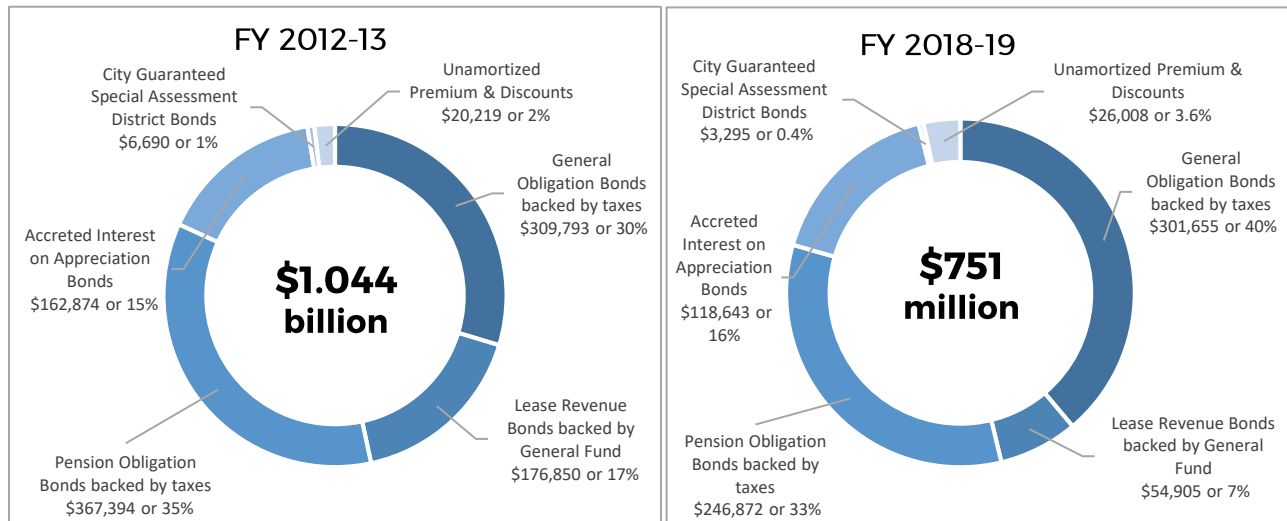
The composition of the bond debt and the changes over the last seven years are shown below:

- Debt from general obligation bonds decreased by 3 percent from \$310 million in FY 2012-13 to \$302 million in FY 2018-19. Although this debt decreased by 3 percent, the City issued \$118 million in general obligation bonds associated with Measure KK

(Infrastructure and Affordable Housing Bond) in FY 2017-18.

- Debt from pension obligation bonds decreased by 33 percent from \$367 million in FY 2012-13 to \$247 million in FY 2018-19.
- Debt from lease revenue bonds decreased by 69 percent from \$177 million in FY 2012-13 to \$55 million in FY 2018-19.

Exhibit 14: City of Oakland debt by type in FY 2012-13 and FY 2018-19 (thousands)



Source: Oakland CAFRs

Credit Ratings

Maintaining a strong credit rating reduces borrowing costs because investors consider the debt less risky. For the last seven years, the City had an Aa3 (Moody's) rating or higher on its bond obligations. This means the City is considered stable by the credit agencies. Exhibit 15 below shows the City's bond ratings as of FY 2018-19.

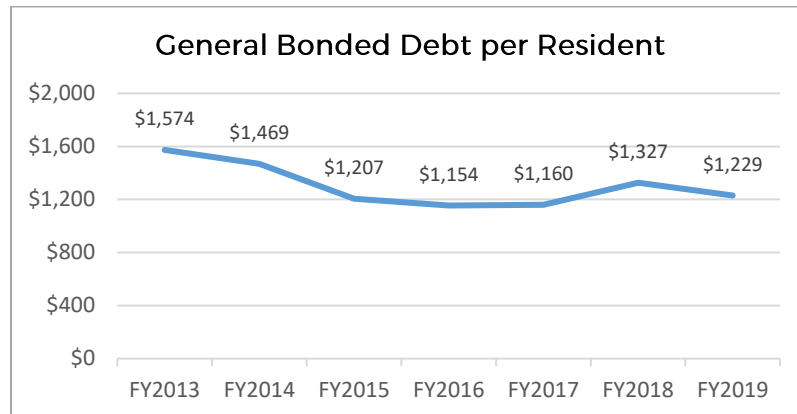
Exhibit 15: City of Oakland Bond Ratings as of FY 2018-19

Type	% of City Total	Moody's Rating	Credit Quality
General Obligation Bonds	49%	Aa2	Very Strong
Lease Revenue Bonds	9%	Aa3	Very Strong
Pension Obligation Bonds	42%	Aa3	Very Strong

City General Bonded Debt Per Resident

As Exhibit 16 shows, the City's debt backed by property taxes, including general obligation and pension obligation bonds (general bonded debt) per resident decreased by 22 percent, from \$1,574 in FY 2012-13 to \$1,229 in FY 2018-19.

Exhibit 16: Seven-year summary of debt per resident from FY 2012-13 through FY 2018-19



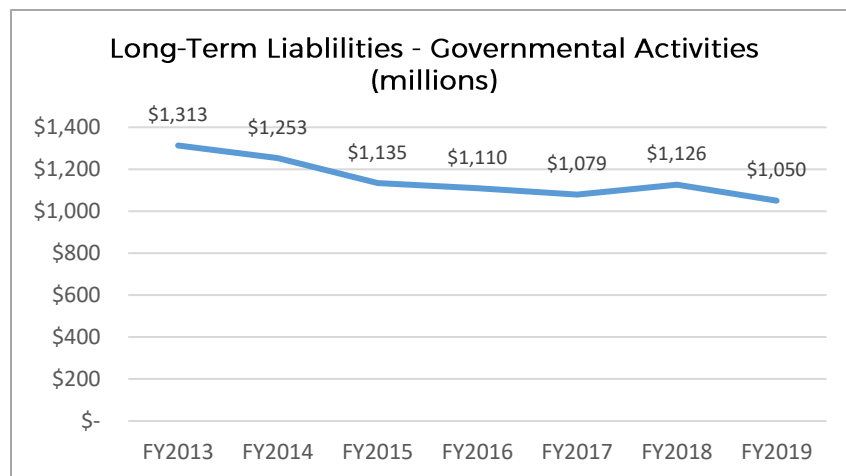
Source: Oakland CAFRs

In addition to bonds, the City has various other types of long-term liabilities. These include loans, capital leases, accrued vacation and sick leave, the City's self-insurance of workers' compensation, and the City's self-insurance of general liability.

The City has decreased its total long-term liabilities associated with governmental activities from \$1.31 billion in FY 2012-13 to \$1.05 billion in FY 2018-19, or 20 percent.

As Exhibit 17 shows, the City's long-term liabilities per resident were decreasing until FY 2018-19, when the City issued Measure KK bonds (the Infrastructure and Affordable Housing Bond).

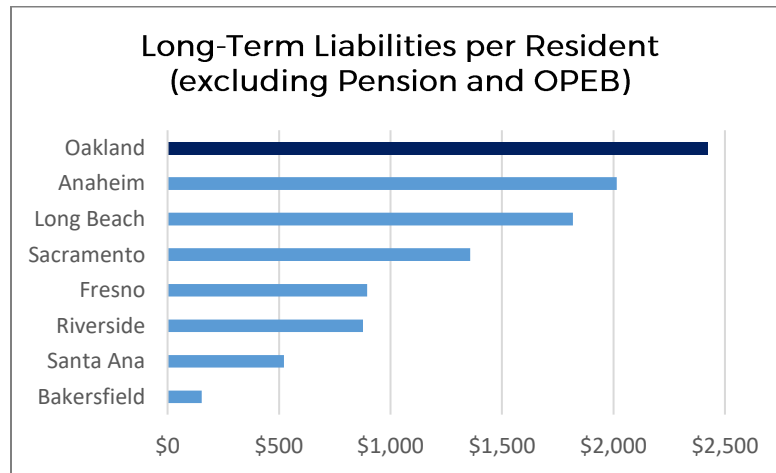
Exhibit 17: Seven-year summary of long-term liabilities for Governmental Activities



Source: Oakland CAFRs

Despite its strong bond ratings, the City's long-term liabilities per resident is higher than any of the benchmarked cities. Exhibit 18 indicates in FY 2018-19 Oakland's long-term liability was \$2,426 per resident, while the other benchmarked cities ranged from \$2,014 to \$153.

Exhibit 18: Long-Term Liabilities per resident (excluding pension and OPEB) and comparison between cities for FY 2018-19



Source: Oakland and other cities CAFRs

04

PENSION and OTHER POST-EMPLOYMENT BENEFITS LIABILITIES

This section describes the City's pension liabilities and OPEB costs and liabilities, which are significant long-term financial obligations for the City. The City has three defined benefit retirement plans:

- Oakland Police and Fire Retirement System (PFRS),⁷
- California Public Employees Retirement System (CalPERS) Miscellaneous Plan, and
- CalPERS Public Safety Plan (CalPERS).⁸

Defined benefit retirement plans are the pensions where workers and their employers agree to contribute to the pension funds over time for a guaranteed source of retirement income. The City's defined benefit plans guarantee a retirement income based on the employees' salary and years of service at retirement.

Recent accounting changes require the City to recognize unfunded pension obligations and OPEB in its net position calculation. Governmental Accounting Standards Board Statement 68 and Statement 75 (or GASB 68 and 75) requires government entities providing defined benefit plans to report the total long-term cost of these benefits as a liability in their annual financial reports. Prior to this requirement, plans only reported the yearly contributions required to cover benefits in annual reporting. In other words, the City is now required to quantify the future benefits to be paid and then compare this number to the current value of pension assets. It's like comparing the mortgage on your recently purchased home to your savings account.

Net Pension Liabilities

To determine whether the City has a pension liability, the benefits already earned by employees (total pension liability) need to be compared to the resources accumulated and held in trust to pay those benefits (fiduciary net position). The difference between the two amounts is the net pension liability (total pension liability - fiduciary net position = net pension liability). If the resources held in trust are less than the pension liability, a pension shortfall exists. In other words, the employer and employee contributions to the plan, combined with

⁷ PFRS is a closed single employer pension plan that covers public safety employees hired prior to July 1976. The City contributes, at a minimum, such amounts that are necessary, determined on an actuarial basis, to provide assets sufficient to meet benefits to be paid to PFRS members. The City is required to fund all liabilities for future benefits for all members by June 30, 2026.

⁸ All civilian City employees and sworn fire and police personnel hired after July 1976 are participants in the California Public Employees' Retirement System (CalPERS) Safety Plan and the CalPERS Miscellaneous Plan. These plans are funded on an actuarial determined basis each year pursuant to CalPERS requirements. The annual actuarial determined cost includes a percentage of payroll to account for the normal cost, and an additional fixed amount to fund the unfunded liability.

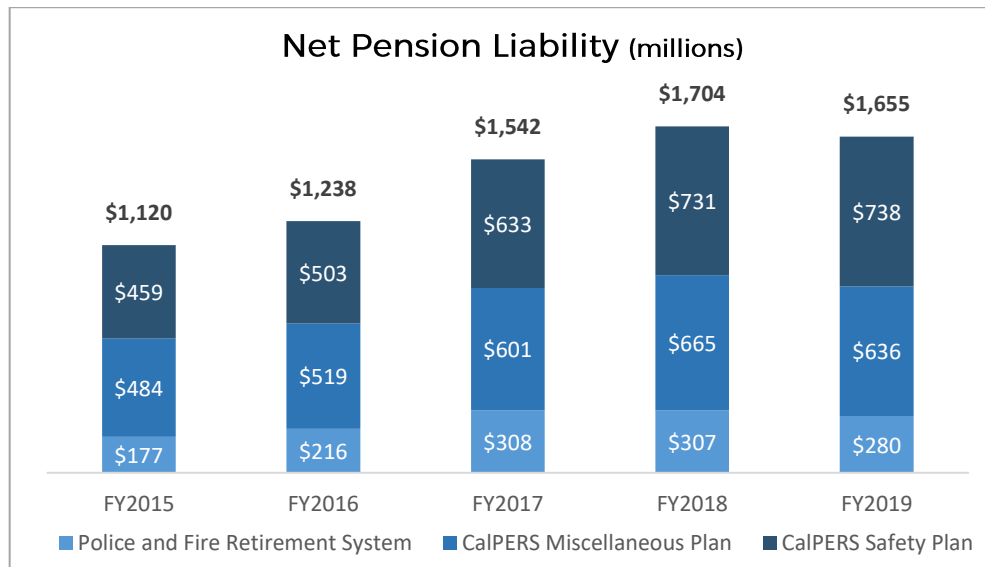
investment earnings, are not enough to cover the anticipated payments due retirees.

As of June 30, 2019, the total net pension liability was \$1.655 billion.⁹ The City's net pension liability was allocated as follows:

- PFRS - \$280 million
- CalPERS Miscellaneous plan - \$636 million
- CalPERS Safety plan - \$738 million

Exhibit 19 below shows the change in the net pension liability for PFRS, CalPERS Miscellaneous and Safety from FY 2014-15 through FY 2018-19.¹⁰ As Exhibit 19 shows, the City's total pension liability has grown by approximately \$535 million over the last five years.

Exhibit 19: Five-year summary of the City's net pension liability by pension plan from FY 2014-15 through FY 2018-19 (millions)



Source: Oakland CAFRs

Funded Ratio

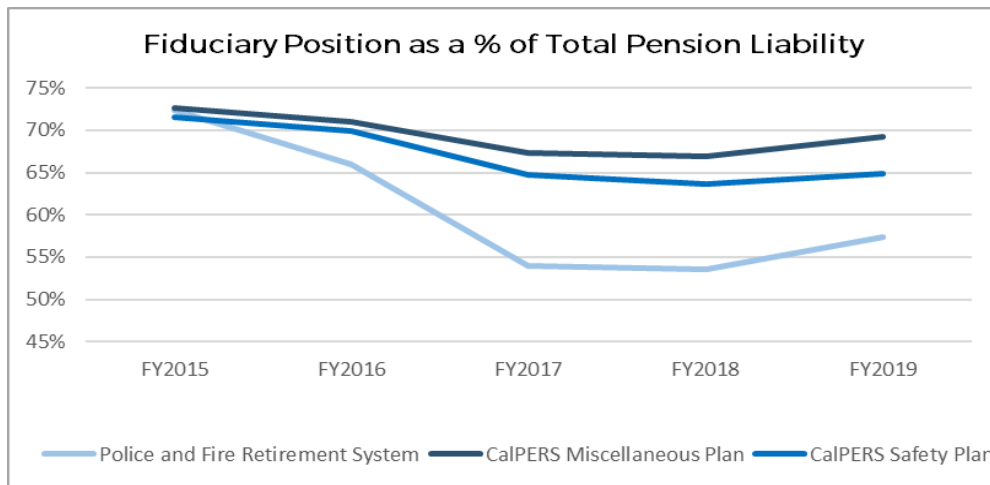
The funded ratio is another way to examine the financial health of a pension plan's status at a point in time. The funded ratio of a pension plan equals a value of assets in the plan divided by a measure of the pension obligation. Many experts consider a funded ratio of about 80 percent or better to be generally sound for government pensions. Additionally, a July 2012 Issue Brief published by the American Academy of Actuaries noted that pension plans should have a strategy in place to attain a funded status of 100 percent over a reasonable period of time.

⁹ Total Net Pension Liability excludes the Port of Oakland pensions.

¹⁰ Fiscal year ended June 30, 2015 was the first year of implementation of GASB Statement No. 68, therefore only five years of information is shown.

Since FY 2014-15, the funded ratio of each of the City's three pension funds has been decreasing each year as Exhibit 20 demonstrates. The PFRS funded percentage declined from 72 percent in FY 2014-15 to 57 percent in FY 2018-19. The CalPERS Miscellaneous and Safety plans followed similar paths, declining from 73 percent and 72 percent in FY 2014-15, respectively, to 69 percent and 65 percent in FY 2018-19.

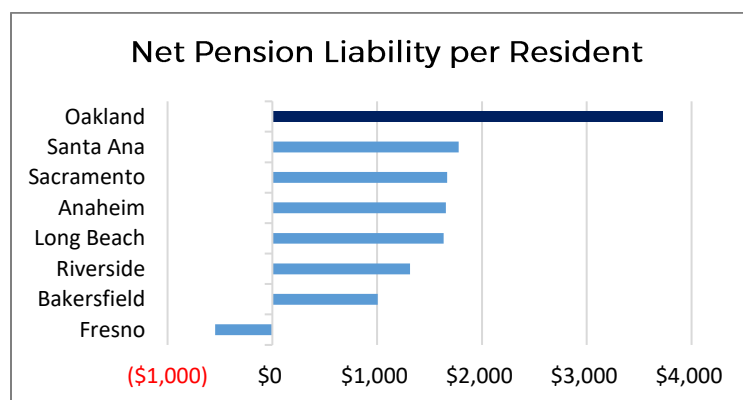
Exhibit 20: Five-year summary of funded ratio for pension plans from FY 2014-15 through FY 2018-19



Source: Oakland CAFRs

Exhibit 21 below shows the net pension liability per resident in FY 2018-19 for Oakland and the benchmarked cities. The City had a \$3,727 net pension liability per resident, which is the highest among the seven benchmark cities that range between (\$546) to \$1,777.

Exhibit 21: Net Pension Liability per resident and comparison between cities for FY 2018-19¹¹



Source: Oakland and other cities CAFRs

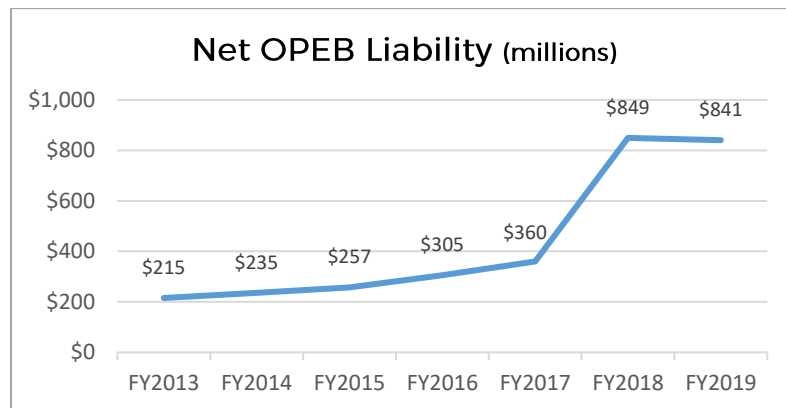
¹¹ The City of Fresno is the only city in our benchmark sample that does not have an active pension plan administered by CalPERS. Fresno's two pension plans are administered by independent retirement boards.

OPEB Liabilities

Other Post-Employment Benefits (OPEB) are benefits other than pensions that the City provides to its retired employees. The benefits include the opportunity to participate in regional health insurance plans offered through CalPERS, and covers a portion of the health insurance premiums, varying by job classifications. Traditionally, the City has paid OPEB benefits using a “pay-as-you-go” system. That is, the City has paid for the cost of these benefits from current revenues, instead of setting aside reserves to pay for future cost of these benefits.

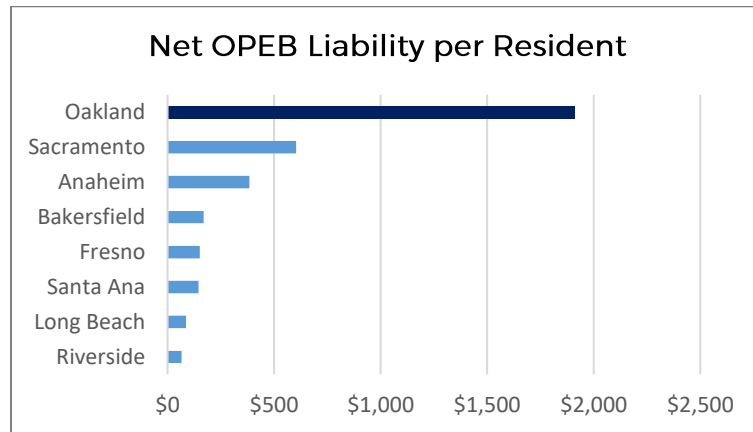
As Exhibit 22 shows, the City’s Net OPEB liability has increased from \$215 million in FY 2012-13 to \$841 million in FY 2018-19, a 291 percent increase. A substantial portion of this increase is due to GASB 75 changes which required OPEB liabilities (future benefit payments) to be included on the financial statements as of FY 2017-18. Additionally, the City’s OPEB liability is almost completely unfunded. As of FY 2018-19, the City’s funded ratio was 1.9 percent of the total OPEB liability.

Exhibit 22: Seven-year summary of net OPEB liability (millions)



Source: Oakland CAFRs

As Exhibit 23 shows Oakland has the highest OPEB liability per resident of the seven cities we benchmarked. In FY 2018-19 Oakland’s net OPEB liability per resident was \$1,913 and is significantly higher than the other benchmarked cities. The OPEB liability for the benchmarked cities ranged from \$66 to \$604 per resident. Some of the benchmarked cities like Bakersfield, Fresno, Long Beach and Riverside, have stopped offering this benefit to new employees, while others partially fund their plans.

Exhibit 23: Net OPEB Liability per resident and comparison between cities for FY 2018-19

Source: Oakland and other cities CAFRs

Recently the City has taken the following steps to start closing the funding gap:

- In FY 2017-18 and FY 2018-19 the City agreed to contribute \$10 million per year to the OPEB Trust through the California Employers' Retiree Benefit Trust (CERBT), a dedicated reserve to pay for future OPEB benefits. Additionally, in January 2019, the City approved a OPEB Funding Policy that would work to close the funding gap by contributing an additional 2.5 percent of payroll commencing in FY 2019-20 and further one-time contributions to the OPEB Trust consistent with the Consolidated Fiscal Policy, when excess Real Estate Transfer Tax (RETT) thresholds are met in addition to the "pay-as-you-go" amount.
- In FY 2018-19 the City reached agreement with its sworn public safety (Fire and Police) unions to cap retiree medical benefits for existing employees and implement new, lower-cost tiers for employees hired after January 1, 2019. These reforms provide significant, and much needed, long-term relief to the City's retiree medical program.

05

FINANCIAL and OPERATING POSITION

What is Financial and Operating Position?

Financial position, also known as net position, measures Oakland's financial standing at a point in time. Operating position indicators measure the City's ability to balance its budget on a current basis, maintain reserves for emergencies and have sufficient liquidity to pay its bills on time. Measures for net position, liquidity, and reserves are presented below.

Net Position

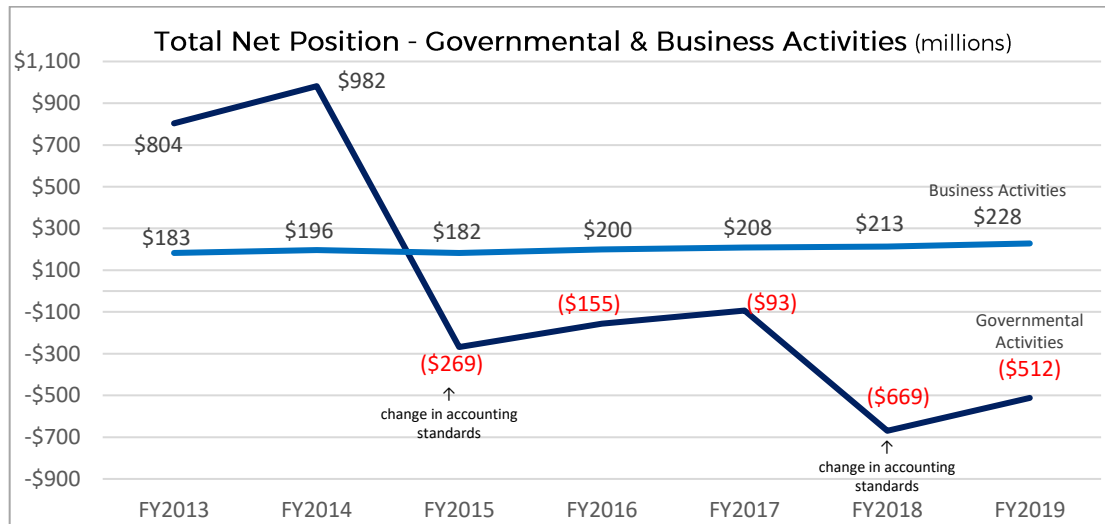
The statement of net position reports the City's assets, liabilities, and the difference in their totals at a specific point in time, usually at the last day of the fiscal year. The City's assets include resources owned by the City that are restricted to a specific purpose or are invested in capital assets such as buildings, roads, bridges, etc., and unrestricted assets. Liabilities are amounts owed to lenders, contractors, bond holders, and suppliers.

Net position represents the resources remaining for the City to use for providing services after its debts are settled. However, these resources are not always in a spendable form. There may be restrictions on how some of the resources can be used. To clarify these, we divided this section into total net position and unrestricted net position.

Total Net Position

Oakland's total net position (restricted and unrestricted) declined 164 percent from FY 2012-13 to FY 2018-19, from \$804 million to (\$512) million as shown in Exhibit 24. As mentioned earlier, changes in accounting practices required the City to recognize the unfunded pension obligations and Other Post Employment Benefits in its financial statements. These reporting changes significantly increased the City's total recorded liabilities and significantly decreased its total net position.

Exhibit 24: City of Oakland's total net position (governmental and business activities) between FY 2012-13 and FY 2018-19 (millions)

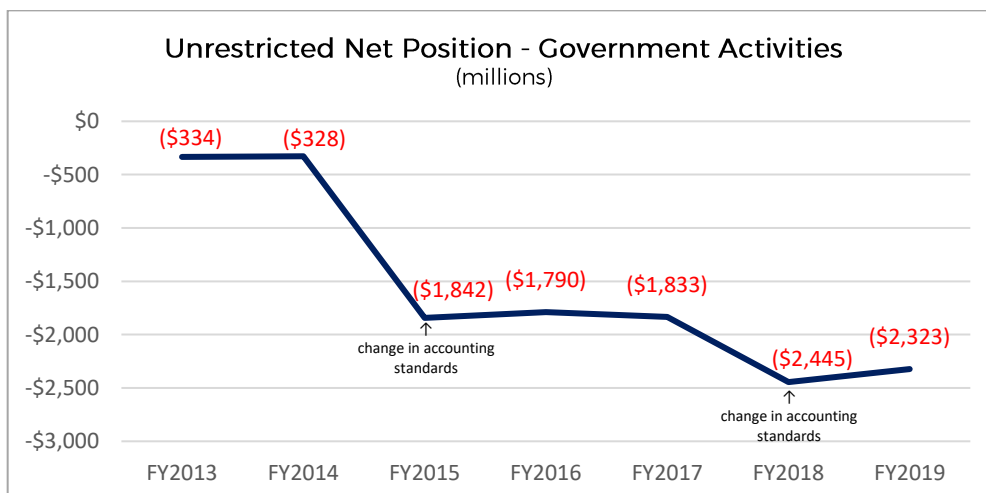


Source: Oakland CAFRs

Unrestricted Net Position

Unrestricted net position represents the City's financial position that is not restricted for any project or purpose; it is Oakland's ability to maintain governmental services when faced with unexpected expenses. Unrestricted net position is a more revealing, long range indicator of the City's financial condition. Exhibit 25 below shows the City's unrestricted net position's general trend over the audited seven-year period has always been negative. In addition, the amount of the deficit was significantly affected by the two accounting changes that took place in FY 2014-15 and FY 2017-18. This deficit does not mean that the City does not have resources available to pay its bills next year. Rather, it is the result of having long-term commitments that are greater than its available resources.

Exhibit 25: Unrestricted Net Position for governmental activities between FY 2012-13 and FY 2018-19 (millions)

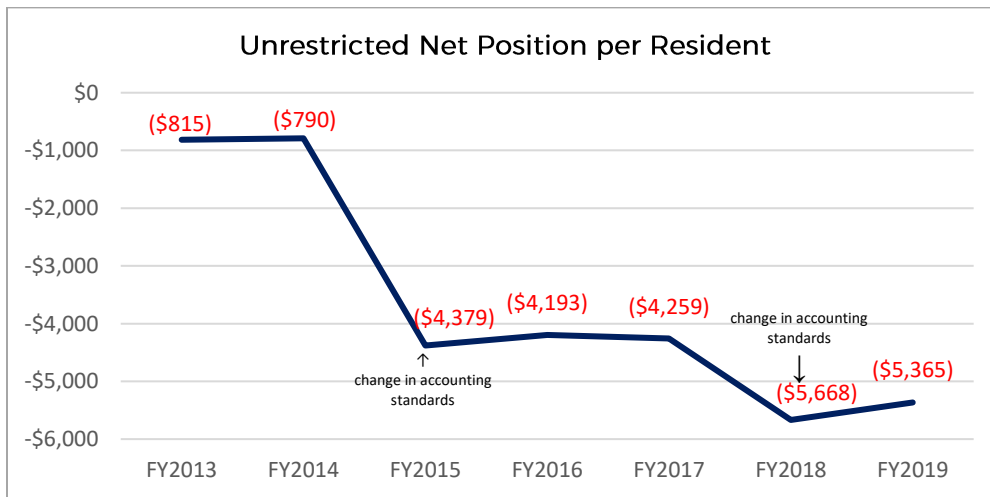


Source: Oakland CAFRs

Unrestricted Net Position Per Resident

One way of placing unrestricted net position in context is to calculate unrestricted net position per resident. The City's total unrestricted net position per resident for governmental activities decreased 559 percent from FY 2012-13 to FY 2018-19. The unrestricted net position per resident in FY 2013-14 was (\$815) and in FY 2018-19 was (\$5,365), as shown in Exhibit 26.

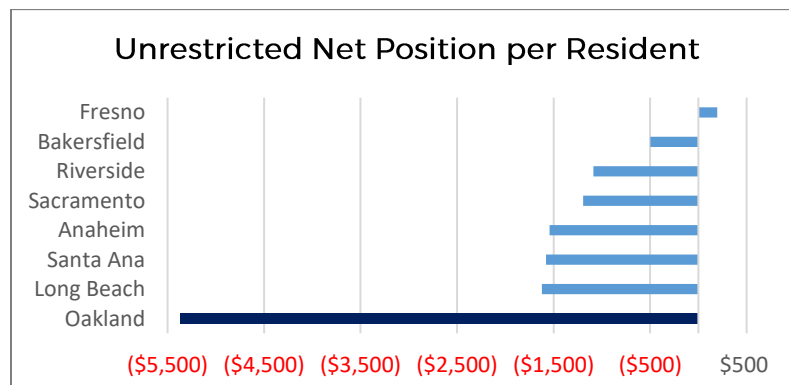
Exhibit 26: Seven-year summary of Unrestricted Net Position per resident for governmental activities from FY 2012-13 to FY 2018-19



Source: Oakland CAFRs

In FY 2018-19, Oakland's total unrestricted net position was (\$5,365) per resident. As Exhibit 27 below shows, Oakland had the worst net position per resident for governmental activities of the seven benchmarked cities. Oakland is not the only city with a negative unrestricted net position among the benchmark cities, however, Oakland's negative net position is over three times worse than the second lowest city on a per resident basis. The other benchmarked cities unrestricted net position ranged from \$197 to (\$1,623) per resident.

Exhibit 27: Unrestricted Net Position per resident and comparison between cities for FY 2018-19



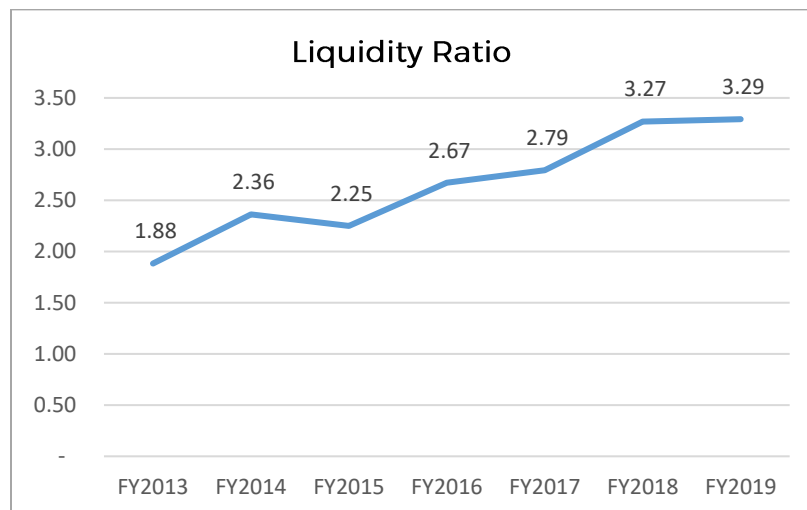
Source: Oakland and other cities CAFRs

Liquidity

Liquidity is the City's ability to pay its short-term obligations within a year. To measure liquidity the City's cash position (cash on hand, and other assets that can be easily converted to cash, short term investments and accounts receivables) is divided by the City's current liabilities (short-term debt, current portion of long-term debt, accounts payable, accrued and other current liabilities). Typically, a one-to-one ratio is the benchmark whether the City can meet its short-term obligations. A high liquidity ratio means that a City's current assets are higher than liabilities that are due within a year and is considered desirable. Thus, a low or declining ratio can indicate that a City's current liabilities are greater than the City's current assets, signifying greater difficulty for a City to pay its liabilities and/or the City has overextended itself in the long run.

As Exhibit 28 below shows, the City's liquidity ratio for governmental activities was above the ratio of 1:1 and increased from 1.88 to 3.29 during the seven-year period from FY 2012-13 through FY 2018-19.

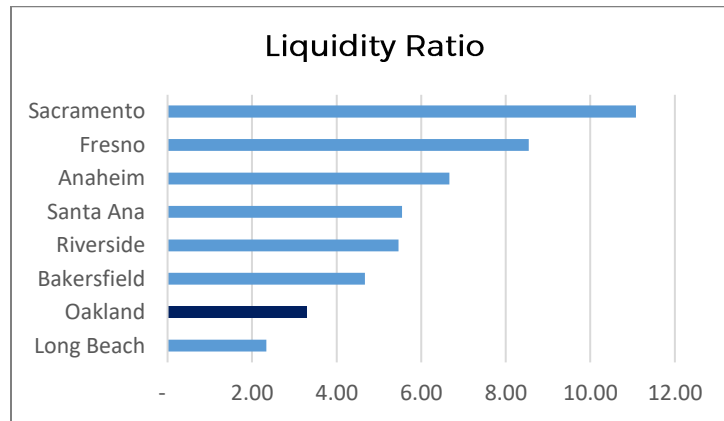
Exhibit 28: Seven-year summary of the City's liquidity ratio for Governmental Activities



Source: Oakland CAFRs

While Oakland's liquidity ratio rose to 3.29 in FY 2018-19, its liquidity ratio ranks seventh of the benchmarked cities that have ratios ranging from 4.67 to 11.08 as shown in Exhibit 29. Only one city, Long Beach, ranks below Oakland with a ratio of 2.34.

Exhibit 29: Liquidity ratio per resident for Governmental Activities and comparison between cities for FY 2018-19



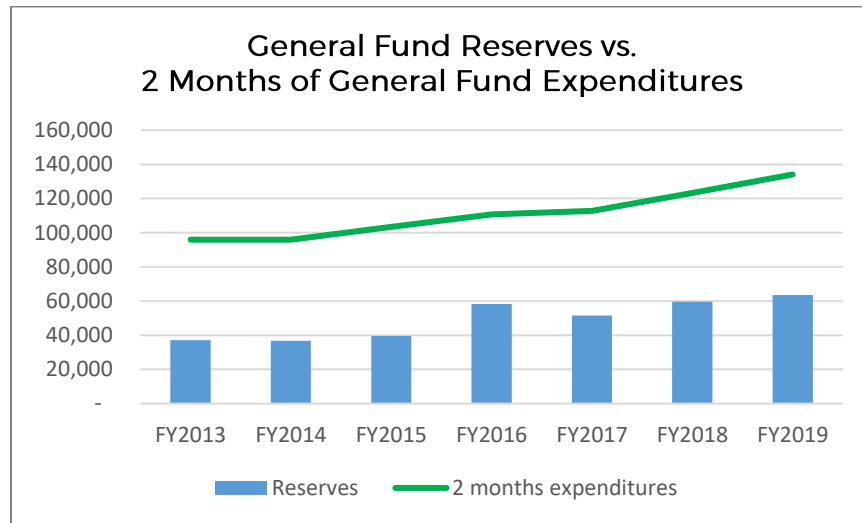
Source: Oakland and other cities CAFRs

Reserves

Reserves are the cornerstone of financial flexibility. Reserves help cities weather multi-year economic downturns, provide essential funding during natural disasters, provide for the support of essential City services, and reduces the financing costs through better credit ratings.

The Government Finance Officer Association (GFOA) has established a recommended reserve policy for governments. The GFOA recommends that governments, regardless of size, maintain an unrestricted budgetary general fund balance of no less than two months of general fund operating expenditures. Furthermore, it emphasizes that each government's situation is different, and governments may deem it appropriate to exclude from consideration resources that have been committed or assigned to some other purpose, focusing on unassigned fund balance, rather than on unrestricted fund balance.

As Exhibit 30 shows, the City's reserves have grown over the last seven years, but it has not met the GFOA reserves requirements. As of June 30, 2019, Oakland's reserves were equal to \$63.4 million, or \$70.6 million less than GFOA's recommended reserve. In other words, the City's reserves do not cover two months of general fund operating expenditures.

**Exhibit 30: Seven-year summary of general reserves
compared to two months of general fund expenditures**

Source: Oakland CAFRs

The City is vulnerable to natural disasters and is dependent on volatile revenue sources. A higher level of reserve balance could protect taxpayers and employees from unexpected changes in its financial condition. The City currently has two reserve policies, the General-Purpose Fund Reserve and the Vital Services Stabilization Reserve (Rainy Day Policy). Both reserves should be re-evaluated in the context of long-term forecasting and the City should consider a variety of factors (e.g., disasters, immediate capital needs, budget cuts) when determining the level of reserves needed. Additionally, these reserve policies do not ensure reserve levels consistent with the GFOA reserve policy.

06

CONDITION of CAPITAL ASSETS

What Are Capital Assets Indicators?

The City's wealth is invested in its physical assets such as streets, buildings, utility networks and equipment. Capital assets indicators evaluate the condition of the physical assets of the City. If these assets are not maintained, it can result in decreasing efficiency, increasing maintenance and replacement costs, creating large future obligations, and decreasing the attractiveness of the community as a place to live and do business.

Capital Assets

The City manages approximately \$1.7 billion (as of FY 2018-19) in total capital assets related to governmental and business type activities. These assets include land, museum collections, intangible assets, construction in progress, facilities and improvements, furniture, machinery and equipment, infrastructure (e.g., streets, streetlights, traffic signals, and parks), sewers, and storm drains. As assets age, their condition declines and the cost of restoring them increases. In the City, the current condition of capital assets varies by asset and bureau, and in some cases the condition is unknown.

This report does not include information on the condition of the City's infrastructure, the citywide asset replacement value, or the funding gap for infrastructure needs because the City does not produce an annual citywide capital assets report.

07

DEMOGRAPHIC and ECONOMIC INDICATORS

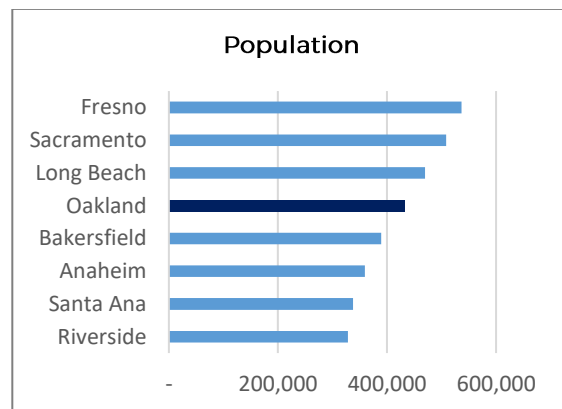
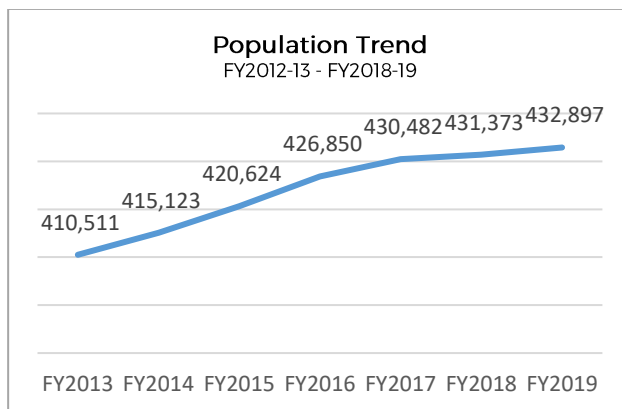
Why Are Demographic and Economic Indicators Important?

Demographic and economic indicators provide information about the needs and resources of the community. Changes in community needs and resources are interrelated in a continuous, cumulative cycle of cause and effect. For example, a decrease in population lowers the demand for housing and can cause a corresponding decline in the market value of housing, and a corresponding reduction in tax revenues. Also, a population decrease can negatively affect retail sales and personal income, causing local government revenues to drop even further. This section presents data on population, unemployment, and property values.

Population

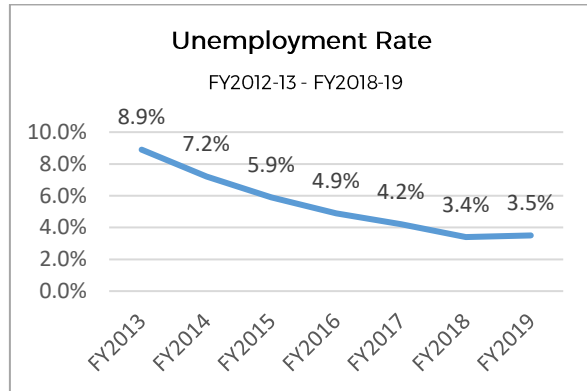
As Exhibit 31 shows, the City of Oakland's population increased by 5.45 percent from 2013 to 2019, from 410,511 to 432,897. In 2019, Oakland accounted for about 1.08 percent of California's total population, was the eighth largest city in California and ranks fourth highest in population of the benchmarked cities.

Exhibit 31: Seven-year trend for population trend and comparison between cities for FY 2018-19

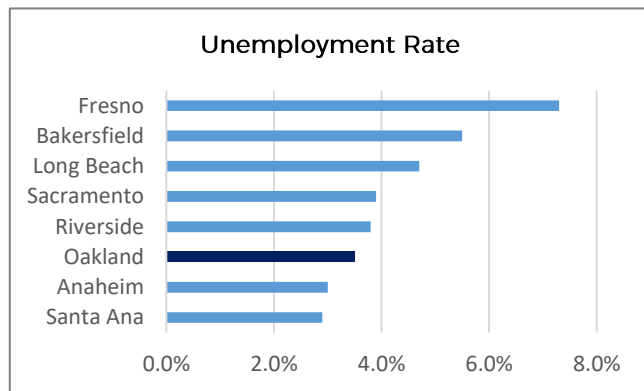


Unemployment

Exhibit 32 shows the City's unemployment rate decreased 61 percent from 8.9 percent in FY 2012-13 to 3.5 percent in FY 2018-19. The City had the third lowest unemployment rate of the benchmarked cities in FY 2018-19.

Exhibit 32: Seven-year trend for unemployment rate and comparison between cities for FY 2018-19

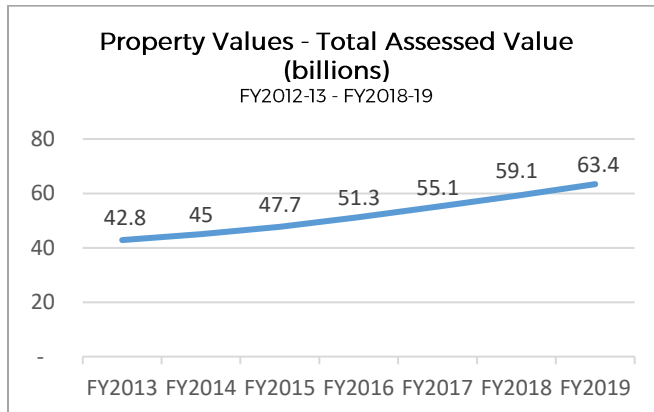
Source: Oakland CAFRs



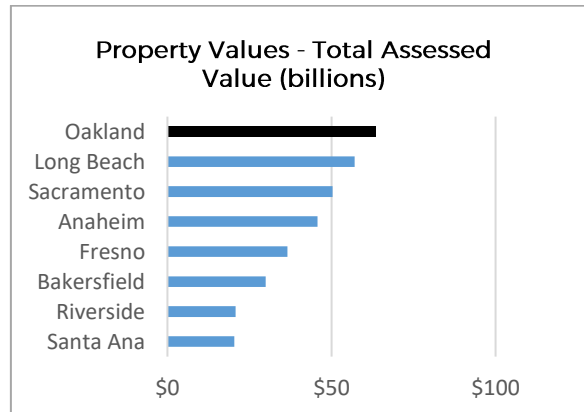
Source: Oakland and other cities CAFRs

Property Values

Assessed residential property values in the City of Oakland increased 48 percent from 2013 to 2019, from \$42.8 billion to \$63.4 billion, as shown in Exhibit 33 below. The assessed value of residential properties in Oakland is the highest of any of the benchmarked cities in California.

Exhibit 33: Seven-year trend for property values and comparison between cities for FY 2018-19

Source: Oakland CAFRs



Source: Oakland and other cities CAFRs

RECOMMENDATIONS

We recommend the following:

1. The City Council should do the following to address the City's unfunded pension and OPEB liabilities:
 - Convene a retirement advisory group to gather, evaluate, and organize information for a comprehensive solution to address Oakland's unfunded pension and OPEB liabilities. This Advisory Group will be tasked with designing a plan to impact retirement liabilities on three levels:
 - State/Federal — what legislative changes, if any, are needed to be proposed so that the municipalities may be in better control of their financial future as it relates to pensions.
 - CalPERS — does CalPERS serve the needs of all its member agencies and how can Oakland and other municipalities have a greater impact on CalPERS policies.
 - Oakland — what changes may be made now within the restrictions of CalPERS and State Law, and which of these changes can be agreed to by all stakeholders.

This process should be convened publicly and have clearly defined processes for stakeholder input, including citizens, unions and employees. The Advisory Group should be comprised of a broad cross section of stakeholders, for example, the City should strongly consider including:

 - Academia and pension/OPEB experts.
 - An independent financial consultant with no ties to the City to perform analysis on potential reforms as they are recommended by the Advisory Group.
 - An independent law firm with no ties to the City to evaluate the legality of potential reforms as they are recommended by the Advisory Group. - Form a coalition of cities to find common ground to support comprehensive solutions at the State level and CalPERS.
2. The City's Finance Department should provide the City Council with an annual analysis of how the City's long-term financial position could be strengthened.
 3. The City should develop a reserve policy that is consistent with the GFOA recommendations to maintain unrestricted budgetary general fund balance of no less than two months of general fund operating expenditures.
 4. The City should have a centralized report of fixed assets to be able to monitor changes in the condition of the assets and evaluate cost associated with maintaining and repairing them.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

The audit objective was to examine the City's financial well-being by calculating financial ratios, analyzing trends in the City's financial data over the past seven-year period, and comparing the results to other cities of similar size.

Scope and Methodology

We based our methodology for this report primarily on *Evaluating Financial Condition: A Handbook for Local Government by the International City/County Management Association*. We also reviewed background information on fiscal sustainability from the Governmental Accounting Standards Board.

Information for the report came mostly from the City's independently audited CAFR from Fiscal Year 2012-2013 to Fiscal Year 2018-2019. Other sources were also used. The primary sources for each area of the report are listed in the following table.

Data Sources

Indicators	Source(s)
Revenues <ul style="list-style-type: none"> City Revenues Revenues by Source Revenues per Resident Property Taxes 	City of Oakland Comprehensive Annual Financial Reports (CAFRs) <ul style="list-style-type: none"> Government-Wide Statement of Net Position Statement of Revenues, Expenditures, and Changes in Fund Balances Statistics – Schedule 8 Demographic and Economic Statistics City of Oakland Oracle system
Expenses <ul style="list-style-type: none"> City Expenses Expenses by Service Area Expenses per Resident City Employees 	City of Oakland Comprehensive Annual Financial Reports (CAFRs) <ul style="list-style-type: none"> Government-Wide Statement of Net Position Condensed Statement of Activities Demographic and Economic Statistics City of Oakland Oracle system
Debt <ul style="list-style-type: none"> City Debt Debt per Type Debt per Resident 	City of Oakland Comprehensive Annual Financial Reports (CAFRs) <ul style="list-style-type: none"> Notes to the Basic Financial Statements Ratios of General Bonded Debt Outstanding Demographic and Economic Statistics
Pension Obligations <ul style="list-style-type: none"> Pension Liabilities 	City of Oakland Comprehensive Annual Financial Reports (CAFRs)

<ul style="list-style-type: none"> • PERS Liability • OPEB Liabilities 	<ul style="list-style-type: none"> • Schedule of Changes in Net Pension Liability and Related Ratios • Schedule of Employer Pension Contributions • Schedule of Changes in Net OPEB Liability and Related Ratios • Schedule of Employer OPEB Contributions • Demographic and Economic Statistics
Financial and Operating Position <ul style="list-style-type: none"> • Citywide Net Position • City Liquidity • Reserves 	City of Oakland Comprehensive Annual Financial Reports (CAFRs) <ul style="list-style-type: none"> • Government-Wide Statement of Net Position • Balance Sheet • Statement of Revenues, Expenditures, and Changes in Fund Balances • Fund Balances, Governmental Funds • Demographic and Economic Statistics
Demographic and Economic <ul style="list-style-type: none"> • Population • Unemployment • Property Values 	City of Oakland Comprehensive Annual Financial Reports (CAFRs) <ul style="list-style-type: none"> • Demographic and Economic Statistics
Other City Comparisons <ul style="list-style-type: none"> • Revenue per Resident • Expense per Resident • Long-term Liabilities per Resident • Net Pension Liability per Resident • Net OPEB Liability per Resident • Unrestricted Net Position per Resident • Liquidity Ratio • Population • Unemployment Rate • Property Values 	City CAFRs and budget documents <ul style="list-style-type: none"> • Cities with fiscal years that begins on July 1 and end on June 30 – Anaheim, Bakersfield, Fresno, Sacramento, Santa Ana and Riverside • City with fiscal year that begins on October 1 and end on September 30 – Long Beach <p>* Long Beach's CAFR and budget documents are for FY 2017-18</p>

The audit did not review:

- Component units of Oakland, such as the Port activities. The government-wide financial statements include the primary government of the City and the Port of Oakland (Port), as a discrete component unit, however, financial information for the Port is reported separately from that presented for the primary government.
- Fiduciary Funds, which are comprised of private purpose and pension trust funds, because these funds are not included in the government-wide financial statements.

We reviewed information for reasonableness and consistency. We researched data that was not reasonable or needed additional explanation. We did not, however, audit the accuracy of source documents or the reliability of the data in computer-based systems. As nearly all financial information

presented is from the City's CAFRs, we relied on the work performed by the City's external financial auditors.

We chose comparison cities due to their similar population size and government services provided. These are the same jurisdictions used in various audit reports.

STATEMENT OF COMPLIANCE AND DISCLAIMER

Statement of Compliance

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Disclaimer

Our review of data was not intended to give absolute assurance that all information was free from error. Rather, our intent was to provide reasonable assurance that the reported information presented a fair picture of the City's financial health. In addition, while the report offers financial highlights, it does not thoroughly determine the reasons for negative or positive performance. More analysis may be needed to provide such explanations.

This report was independently developed by the Office of the City Auditor and is intended for the public as a high-level report. This report is the result of a performance audit and was not part of the City's annual financial audit on the City's financial statements. Expressions of opinion in the report are not intended to guide prospective investors in securities offered by the City and no decision to invest in such securities should be made without referencing the City's audited CAFRs and official disclosure documents relating to a specific security.

For additional information on the City of Oakland's finances, please visit the following website:
<https://www.oaklandca.gov/departments/finance-department>

APPENDIX A

Seven-year summary of revenues by type for governmental activities and percent change from FY 2012-13 through FY 2018-19 (thousands)

Revenue by Type		FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY2019	7 Year % Change
Local Taxes	Property Tax	256,333	240,779	267,534	279,764	312,078	340,573	358,446	40%
	Business License Tax	60,371	62,905	66,677	75,504	75,840	86,107	99,733	65%
	Utility Consumption Tax	50,752	50,422	50,594	51,006	52,618	52,047	49,599	-2%
	Real Estate Transfer Tax	47,406	59,060	62,665	89,594	79,070	77,663	104,905	121%
	Transient Occupancy Tax	15,831	18,468	21,569	25,671	29,049	30,039	33,005	108%
	Parking Tax	15,565	16,661	18,398	20,175	20,886	21,137	21,726	40%
	Voter Approved Taxes	38,247	38,835	37,443	37,793	37,962	50,469	59,682	56%
	Franchise Tax	16,035	16,666	18,150	18,609	18,763	19,124	19,340	21%
State Taxes	Motor Vehicles In-Lieu Tax	-	-	177	166	189	224	206	
	Gas Tax	10,004	13,085	12,030	8,653	7,974	10,867	16,409	64%
	Sales and Use Tax	60,494	58,912	63,718	77,365	79,866	85,500	92,319	53%
Program Revenues	Charges for Service	126,831	152,674	182,293	178,309	203,153	221,719	203,390	60%
	Operating Grants & Contributions	89,424	119,063	92,865	90,090	95,032	124,238	95,198	6%
	Capital Grants & Contributions	26,179	42,148	70,322	54,043	34,911	750	22,672	-13%
	Interest and Investment Income	6,358	6,653	6,362	4,596	3,046	11,762	26,394	315%
	Other	7,076	19,671	12,745	20,987	19,935	42,362	31,457	345%
Total		826,906	916,002	983,542	1,032,325	1,070,372	1,174,581	1,234,481	49%

Source: Oakland CAFRS

Property Tax: The property tax is ad valorem, which means that the tax paid on a property is proportional to the property's value. There are exemptions to certain portions of property values and certain types of properties that are regulated by the State and administered by the County, such as Proposition 13. The property tax assessed value (net after any exemption) is collected by the County and is distributed to various public entities in accordance with a complex formula.

Business License Tax: The business license tax is composed of three primary components: normal business gross receipts, gross receipts from construction activity, and business tax from the rental of residential and commercial property.

Utility Consumption Tax: This tax is imposed upon the consumption of telephone communication, alternative fuel, cable television, electric, and gas by the utility user. The utility company usually collects this tax as part of the regular customer billing procedures and remits the payment to the City.

Real Estate Transfer Tax (RETT): The RETT is assessed whenever there is a change in ownership of real property.

Transient Occupancy Tax (TOT): The transient occupancy tax (TOT) rate is 14 percent of the hotel rate and is paid by individuals who stay thirty days or less in a hotel located within the City of Oakland. This tax is collected and remitted by hotel operators.

Parking Tax: The parking tax is a tax imposed on the occupant of an off-street parking space. The tax rate is 18.5 percent and is collected by parking operators. 8.5 percent supports voter-approved Measure Z - Violence Prevention and Public Safety activities and is allocated to a separate fund.

Voter-Approved: Sugar-Sweetened Beverage Tax, Lighting and Landscaping Assessment Tax, Bedroom Tax, Measure M, Measure N, Measure Q, Measure D, Wildland Fire Prevention Assessment District, Rockridge Library Assessment District.

Franchise Tax: Franchise Tax revenue is derived from a fee paid to a municipality from a franchisee for “rental” or “toll” for the use of city streets and rights-of-way. These taxes apply to four utilities for the use of City rights of way: PG&E for gas and electric; Waste Management of Alameda County for garbage collection; East Bay Municipal Utility District for water; and Comcast for cable television.

Motor Vehicle In-Lieu: Since 2004, the State of California swapped additional property tax revenues in exchange for city and county vehicle license fee revenue (VLF). The property tax payment provided in-lieu of the VLF grows proportionally to a city’s assessed value.

Gas Tax: Under the provision of the Streets and Highways Code, the State gas tax revenues are restricted to uses related to local streets and highways and would include acquisitions of real property, construction and improvements, and repairs and maintenance of streets and highways.

Sales & Use Tax: The sales and use tax applies to the retail sale or use of tangible personal property.

Charges for Services: These are revenues that arise from charges to customers or applicants who purchase, use, or directly benefit from the goods, services, or privileges provided. Examples are rental fees for facilities, sewer service system charges, park and recreation program charges, and library fines.

Program-Specific Operating Grants and Contributions: These are revenues that occur from mandatory and voluntary nonexchange transactions with other governments, organizations, or individuals that are restricted for use in a program. An example is a business grant to provide a scholarship for staff training.

Program-Specific Capital Grants and Contributions: These are grants and contributions that consist of capital assets or resources that are restricted for capital purposes, such as purchasing, constructing, or renovating capital assets associated with a specific program. These revenues should be reported separately from grants and contributions that may be used either for operating or capital expenses. An example is a grant to purchase a fire engine.

Interest and Investment Income: Income that comes from interest payments, dividends, capital gains collected upon the sale of a security or other assets, and any other profit made through an investment vehicle of any kind.

Other: Miscellaneous revenue is primarily comprised of property sales, equipment financing, and litigation recoveries.

APPENDIX B

Seven-year summary of expenses by type for governmental activities and percent change from FY 2012-13 through FY 2018-19 (thousands)

Expenses by Type	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	7 Year % Change
General Government	93,942	79,806	82,493	99,183	127,344	110,486	199,697	113%
Public Safety	363,597	379,809	383,904	432,862	470,798	471,378	444,400	22%
Community Services	107,779	116,961	121,740	134,799	146,398	144,763	142,719	32%
Community and Economic Development	81,182	83,657	75,268	85,396	92,048	103,328	103,099	27%
Public Works and Transportation	75,158	109,177	105,619	114,597	122,540	158,610	127,597	70%
Interest on Long-Term Debt	62,744	59,026	68,033	54,335	56,471	61,505	60,432	-4%
Total	784,402	828,436	837,057	921,172	1,015,599	1,050,070	1,077,944	37%

Source: Oakland CAFRs

General Government: These expenses are attributed to the Mayor's Office, Council Offices, Attorney's Office, Auditor's Office, Administrator's Office, Clerk's Office, Finance Department, Human Resources Department, Information Technology Department, Contracting and Purchasing Department.

Public Safety: These expenses are attributed to the Police and Fire Departments.

Community Services: These expenses are related to Parks & Recreation, Library, Museum and Human Services Departments.

Community and Economic Development: These expenses are related to activities in Planning and Building, Economic and Workforce Development, and Housing and Community Development.

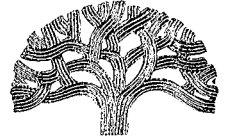
Public Works and Transportation: These expenses are attributed to Public Works, Department of Transportation, and interest on long-term debt.

Interest on Long-Term Debt: This expense includes the amount of interest on outstanding long-term debt issued.



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CITY OF OAKLAND



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Office of the City Administrator

March 10, 2020

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Honorable Courtney A. Ruby
Oakland City Auditor
1 Frank Ogawa Plaza, 4th Floor
Oakland, CA 94612

Re: City of Oakland Financial Condition Performance Audit

Dear City Auditor Ruby:

I am pleased to provide you with the City Administration's response to the City of Oakland Financial Condition Performance Audit. The Administration thanks the City Auditor and her staff for their work in developing this analysis. In general, the Administration concurs with your findings and recommendations.

As outlined in your report, the Administration has taken numerous actions in recent years to reduce the growth in unfunded retirement obligations for both pensions and Other Post-Employment Benefits (OPEB). In addition, the City Council adopted an OPEB Funding Policy that requires the set-aside of additional resources to ensure these benefits are available to City retirees in the future. We have a Consolidated Fiscal Policy ordinance that mandates an Economic Contingency reserve and Vital Services Stabilization Fund, that when fully funded will be equal to 22.5% of General Purpose Fund appropriations.

The Administration is committed to the continual evaluation of these ordinances and policies to improve the City's financial position over the long-term, and our efforts have paid off. In February 2020, Moody's upgraded the City's underlying credit rating from Aa2 to Aa1, the second highest rating available. S&P affirmed the City's underlying rating (AA), but improved the City's outlook from stable to positive.

Again, thank you and your staff for these efforts. I look forward to our continued partnership in being prudent stewards of the City's finances.

Sincerely,

A handwritten signature in black ink, appearing to read 'Sabrina B. Landreth', with a stylized, looping flourish at the end.

Sabrina B. Landreth
City Administrator

	City Auditor's Recommendations	Management Action Plan	Responsible Party	Target Date to Complete
1	<p>The City Council should do the following to address the City's unfunded pension and OPEB liabilities:</p> <ul style="list-style-type: none"> • Convene a Retirement Advisory Group to gather, evaluate, and organize information for a comprehensive solution to address Oakland's unfunded pension and OPEB liabilities. This Advisory Group will be tasked with designing a plan to impact retirement liabilities on three levels: <ul style="list-style-type: none"> ○ State/Federal— what legislative changes, if any, are needed to be proposed so that the municipalities may be in better control of their financial future as it relates to pensions. ○ CalPERS— does CalPERS serve the needs of all of its member agencies and how can Oakland and other municipalities have a greater impact on CalPERS policies. ○ Oakland — what changes may be made now within the restrictions of CalPERS and State Law, and which of these changes can be agreed to by all stakeholders. <p>This process should be convened publicly and have clearly defined processes for stakeholder input, including citizens, unions and employees. The Advisory Group should be</p>		City Council (to be discussed when report is presented to City Council).	



	<p>comprised of a broad cross section of stakeholders, for example, the City should strongly consider including:</p> <ul style="list-style-type: none">○ Academia and pension/OPEB experts.○ An independent financial consultant with no ties to the City to perform analysis on potential reforms as they are recommended by the Advisory Group.○ An independent law firm with no ties to the City to evaluate the legality of potential reforms as they are recommended by the Advisory Group. <ul style="list-style-type: none">● Form a coalition of cities to find common ground to support comprehensive solutions at the state and CalPERS levels.			
2	<p>The City's Finance Department should provide the City Council with an annual analysis of how the City's long-term financial position could be strengthened.</p>	<p>The Finance Department regularly reports to the City Council and/or publishes reports on the Finance Department's website on the financial condition of the City. These include quarterly reports on revenues and expenditures, quarterly cash and investment reports, and actuarial reports on pensions and OPEB.</p> <p>In addition, the Finance Department brings the Comprehensive Annual Financial Report (CAFR) to the City Council upon completion of the annual audit. While the CAFR presentation</p>	<p>Finance Department</p>	<p>This item will require annual, ongoing reporting. Staff anticipates discussing long-term strategies to strengthen the City's financial position when the CAFR is brought to the City Council each year (usually in</p>

		largely focuses on a summary of the year-end results, it can include a more detailed discussion of strategies for improving the City's long-term financial position.		January or February).
3	The City should have a centralized report of fixed assets to be able to monitor changes in the condition of the assets and evaluate cost associated with maintaining and repairing them.	Staff are currently exploring options, including the potential for a new software system, to monitor and track the conditions of fixed assets and long-term leases.	Finance Department / Oakland Public Works / Economic & Workforce Development	TBD. Staff anticipates that reporting will be ongoing.
4	The City should develop a reserve policy that is consistent with the GFOA recommendations to maintain unrestricted budgetary general fund balance of no less than two months of general fund operating expenditures.	The City currently has two General Purpose Fund (GPF) reserves: 1) the Economic Contingency Reserve; and 2) the Vital Services Stabilization Fund (VSSF). The Economic Contingency Reserve maintains a balance that is equal to 7.5% of GPF appropriations. The VSSF has a target balance of 15% of GPF appropriations and is funded through the City's use of "excess" real estate transfer tax revenues. Once the VSSF achieves its target balance of 15%, the City's total available reserves (22.5%) will exceed the GFO recommendation (16.7%).	Finance Department	Monitoring of reserves is ongoing. Staff anticipates bringing recommended CFP amendments in April 2020.



**CITY OF
OAKLAND**

Office of the City Auditor

**City of Oakland's Financial Condition
Performance Audit
Management's Response**

		<p>The Finance Department regularly reviews the Consolidated Fiscal Policy (CFP) ordinance and makes recommendations to the City Council on proposed amendments, including reserves policies and the use of excess real estate transfer taxes.</p>		
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