

**CITY OF NEWPORT BEACH
FINANCE COMMITTEE
AUGUST 13, 2015 MEETING MINUTES**

I. CALL MEETING TO ORDER

The meeting was called to order at 4:00 p.m. in the Newport Coast Conference Room, Bay 2E, 100 Civic Center Drive, Newport Beach, California 92660.

II. ROLL CALL

PRESENT: Council Member Keith Curry (Chair); Mayor Pro Tem Diane Dixon; Council Member Tony Petros; Committee Member William C. O'Neill; Committee Member Larry Tucker; and Committee Member John Warner

ABSENT: Committee Member Bill McCullough (Excused)

STAFF PRESENT: City Manager Dave Kiff; Finance Director Dan Matusiewicz; Deputy Finance Director Steve Montano; Administrative Specialist to the Finance Director Marlene Burns; Deputy City Manager/HR Director Terri Cassidy; Budget Manager Susan Giangrande; IT Manager Rob Houston; Municipal Operations Director George Murdoch; Senior Accountant Trevor Power; Municipal Operations Director Mike Pisani; Interim Assistant City Manager Carol Jacobs; General Services Operations Support Superintendent James Auger; and General Services Administrative Manager Cynthia Owens

MEMBER OF THE PUBLIC: Jim Mosher

OUTSIDE ENTITY: Jayson Schmitt, Chandler Asset Management

III. PUBLIC COMMENTS

Jim Mosher spoke on Council's upcoming review of the City's Master Fee Schedule noting that the fees are not only based on the cost of services rendered, but also multiplied by cost recovery factors. He opined that the cost recovery table is in need of a comprehensive review. He spoke about outsourcing street-light maintenance costs noting that Council recently approved a new contract with a new vendor and expressed concerns with the increased costs. He questioned whether the City can determine past costs for the same service.

Municipal Operations Director George Murdoch explained the actions taken in terms of the original contract for street-light maintenance, cost savings, and the RFP process. He added that the City provided materials under the old contract but, that in the new contract, the vendor supplies the needed materials. Additionally, the new contract includes payment of prevailing wages, which has doubled the City's costs. He added that employees' time is tracked daily, that the vendor who provided the lowest bid from the RFP process was chosen and that the City augmented the scope of work.

In response to an inquiry from Committee Member Tucker regarding prevailing wages, Municipal Operations Director Murdoch stated that the City was previously exempt from paying prevailing wages but it is no longer exempt.

IV. APPROVAL OF MINUTES

A. Summary:

Approval of the July 21, 2015, Finance Committee Minutes.

Recommended Action:

Approve and file.

Chair Curry reported corrections to the minutes were made by Committee Members Tucker and O'Neill.

Chair Curry opened public comments.

Jim Mosher offered additional corrections to the minutes.

With no further public comments, Chair Curry closed public comments.

Committee Member Tucker moved and Council Member Petros seconded, to approve the July 21, 2015, Finance Committee Minutes, as corrected. The motion carried with 5 ayes, 1 abstention (Committee Member Warner) and 1 absent (Committee Member McCullough).

V. CURRENT BUSINESS

A. ANNUAL INVESTMENT PORTFOLIO PERFORMANCE REVIEW

Summary:

A Staff and a City investment advisor will provide of brief fixed income market review of the past year and comment on the performance of the City's investment portfolio.

Recommended Action:

Receive and file.

Chair Curry introduced the item and deferred to staff for a report.

Finance Director Dan Matusiewicz reported that the City had outsourced the portfolio management function since 1992 and had a contractual relationship with as many as five investment advisors and five custody banks and added the City has now consolidated those relationships down to two investment advisors and an one custody bank in recent years.

Chair Curry provided a brief history of the City's investments and noted that the City was not materially affected by the Orange County bankruptcy.

At Mayor Pro Tem Dixon's request, Finance Director Matusiewicz addressed the selection of investment advisors and the contract terms.

Finance Director Matusiewicz continued addressing the core investment portfolio, the City's participation in the State liquidity pool, dual-approval requirements, the City's independent investment analytics software service, monitoring actions to ensure that the City stays within its risk parameters and identified that the complete monthly Treasury report can be found on the City's website.

Jayson Schmitt, Chandler Asset Management, provided a brief market overview. He addressed the likelihood of the Federal Reserve Board raising the Federal funds rate, impacts of global issues, volatility, decreases in the unemployment rate, labor participation and under-employment. He addressed retail sales, consumer credit and other market measures and economic indicators. Additionally, Mr. Schmitt reported on manufacturing, capacity utilization, Federal Reserve mandates, inflation, Consumer Price Index (CPI), revisions in the Gross Domestic Product (GDP), two-year Treasury Note rate and the three-month yield curve.

In response to Committee Member Warner's question, Mr. Schmitt commented that "core inflation" is a less volatile measure of inflation when food and energy are removed from the equation.

Mr. Schmitt reviewed the City's portfolio performance with respect to the City's investment objectives of safety, liquidity, and yield and compliance with the City's investment policy.

In reply to Council Member Petros's inquiry, Mr. Schmitt stated there have been no compliance issues within the last year.

Mr. Schmitt addressed the account profile versus benchmarks, and impacts of rising interest rates on the City's portfolio. He discussed average purchase yields, changing trends, security types owned by the City and investment issuers.

Responding to Committee Member Tucker's question, Finance Director Matusiewicz addressed investment advisor fees.

Mr. Schmitt commented on the Federal Government strengthening its balance sheet. He added that most mortgages, today, are purchased by Fannie Mae and Freddie Mac.

Brief discussion followed regarding supranationals.

Mr. Schmitt continued with his presentation addressing S&P ratings, range of distribution, investment performance, providers of fixed income indices and holdings. He summarized the City's universe of investments and provided highlights of same.

Finance Director Matusiewicz added that Newport Beach is generally more conservative than what the Government Code allows for investments.

Chair Curry opened public comments.

Jim Mosher commented on the Total Rate of Return and asked whether that number is before or after subtracting the management fee.

Mr. Schmitt reported that it is a gross number so that it is before subtracting management fees.

With no further public comments, Chair Curry closed public comments.

Council Member Petros moved, and Committee Member Warner seconded, to receive and file the report. The motion carried with 6 ayes, and 1 absent (Committee Member McCullough).

B. ANNUAL INVESTMENT POLICY REVIEW AND UPDATE

Summary:

In furtherance of Section K-2 of Council Policy F-1, Statement of Investment Policy (the Policy), the Finance Department has completed an annual review of the Policy to ensure its consistency with the overall objectives of preservation of principal, liquidity and return, and its relevance to current law and financial and economic trends. Staff is proposing two modifications to the Investment Policy as recommended by the City's investment advisors, Public Financial Management (PFM) and Chandler Asset Management (Chandler), and supported by the City's Finance Director/Treasurer.

Recommended Action:

Review, discuss, and approve or revise staff recommendations for Council approval.

Finance Director Matusiewicz provided details of the report addressing recommended changes.

Jayson Schmitt, Chandler Asset Management, provided details of supranationals and addressed the three organizations allowed to manage same. He explained that the organizations lend to different countries and that the loans are project-oriented in terms of social and environmental projects. He addressed the yield, AAA credit rating and support from a consortium of governments. He added that these are securities that would be beneficial to the portfolio in terms of safety, liquidity and diversification.

Brief discussion followed regarding donations and contributions to Greece.

Council Member Petros noted that Fannie Mae is backed by the U.S. Government, commented on other instruments being limited to individual institutions at 5 percent and on the uncertainty in international markets. He questioned whether investments should be made in a more conservative manner

Chair Curry noted that Fannie Mae and Freddie Mac are not guaranteed by the Government. He added that the quality of investment securities continues, at the highest level.

Mr. Schmitt added that these are not new organizations and that there has never been a default on those securities since the beginning. He addressed how the City might begin to invest in these securities and suggested a 10 percent allocation in two securities adding that the policy should reflect a broader type base to be available, moving forward.

Mr. Schmitt stated that these securities are very stable and close in quality to those of U.S. agencies. If these were risky investments, investors would demand more yield.

Mayor Pro Tem Dixon confirmed that the City will not be replacing the 26 percent in Fannie Mae and Freddie Mac but that changes will be very gradual.

In response to Committee Member Tucker regarding the yield difference, Mr. Schmitt stated it would be approximately 3 to 5 basis points above U.S. agencies. He added that focus should not be just on yield, but diversification and looking towards the future.

Committee Member O'Neill suggested setting the investment at 20 percent for three years, with the expectation that the matter would be revisited at that time.

Mr. Schmitt addressed consideration of flexibility and noted that this policy is reviewed on an annual basis.

Chair Curry opened public comments.

Jim Mosher commented on the City being more conservative in terms of investments policies versus being more liberal. He questioned whether there is other pending state legislation that may impact the City's investment policies in the coming year. He noted that the Committee can only make recommendations for Council action.

Chair Curry noted there is always pending legislation that would impact investment policy.

With no further public comments, Chair Curry closed public comments.

In response to an inquiry by Committee Member O'Neill, Mr. Schmitt stated that any changes, outside of the City's investment policies would be communicated to the City with an appropriate recommendation, almost immediately.

Committee Member O'Neill moved, and Council Member Petros seconded, to accept staff recommendations but changing the maximum portfolio allocation to supranational bond investments to 20 percent instead of 30 percent, with a review made on an annual basis and with

the ability to make changes, based on performance investment objectives. The motion carried with 6 ayes, and 1 absent (Committee Member McCullough).

Brief discussion followed regarding the City's independent advisors and independent data sources.

C. RECOMMENDATIONS FOR THE ANNUAL FINANCE COMMITTEE BUDGET REVIEW PROCESS

Summary:

During the July 21, 2015, Finance Committee meeting, members discussed the need for greater transparency and accountability during the annual budget development process. This report provides recommendations and associated action items to improve budget transparency and to increase the Finance Committee's involvement during the annual review of the City's budget.

Recommended Action:

Review, discuss, and approve or revise staff recommendations and action items for Council approval.

Finance Director Matusiewicz provided a PowerPoint presentation addressing the Committee's desire to be more involved in the budget-review process, including communicating budget priorities and principles, discussing budget assumptions and strategies prior to the development of the budget, providing for increased transparency and greater accountability, and better communicating the value of certain job functions. He addressed documentation reviewed during the process and a timeline for review of other elements within the budget. This will be done in order for the Committee to provide guidance in terms of budget priorities. He reported that there will be a review of the City's year-end financial results as scheduled on the Finance Committee Workplan. He addressed the need for pre-budget recommendations from the Finance Committee to Council to develop funding strategies and assumptions.

Committee Member Tucker suggested focusing on big budget categories rather than just larger percentage changes in categories, potential savings by outsourcing and increasing efficiency by potentially reducing staffing levels.

Finance Director Matusiewicz agreed and suggested those items should be considered prior to budget discussions. In addition, Finance Director Matusiewicz suggested having the Police and Fire Chief could provide a presentation on their operations for increased understanding of their respective departments.

Committee Member Tucker suggested that after staff takes a hard look at staffing levels, an independent consultant look at the City's organization, as a whole to determine possible staffing level reductions while maintaining the same level of service as presently exists. He noted that every dollar saved in the operation is a dollar that can be spent on infrastructure that redounds to the benefit of the entire community.

Mayor Pro Tem Dixon asked regarding the City's key performance indicators (KPIs) and Finance Director Matusiewicz reported that in municipalities, those are hard to establish, but added that some metrics could include customer satisfaction, response time and whether the City is delivering projects in a timely fashion.

City Manager Dave Kiff commented on developing benchmarks using those of other cities and suggested bringing these to the Finance Committee for review. He commented on the possibility of an outside review of City operations noting that it is good in principle, but harder in practice and explained potential challenges.

Council Member Petros recounted concerns regarding the previous budget adoption process, provided recommendations and cautioned against making comparisons between public agencies and private entities. He addressed customer surveys and noted that responses were 90 percent for every one of the benchmarks identified.

Mayor Pro Tem Dixon commented on levels of service and questioned if the City is striving for 100 percent satisfaction or less.

Council Member Petros commented on the City's reserves and noted that criticism was made that the City was hoarding money and that residents wanted money spent on capital projects. When the City does spend, criticism is made that the City overspends and that there is no way to tell whether the City is doing something correctly as the City is at the whim of human nature in politics. He cautioned against using metrics to measure satisfaction.

Committee Member Tucker reiterated the need to look for efficiencies in terms of staffing levels. He acknowledged that staffing levels may be appropriate currently but felt the Finance Committee ought to make an effort to look into this factor since personnel is the single biggest expense of the City's business.

Chair Curry offered that the City has already reduced its headcount and is in the process of refreshing its infrastructure while maintaining the highest reserves in the City's history. He noted that the City has a high bond rating but acknowledged there may be specific items to review that may provide further efficiencies and opportunities to do things differently for improved processes and for doing the things that people want. He commented on the importance of having an economically strong and viable plan for the future.

City Manager Kiff commented on in-house reviews by Department Heads, encouraged Committee Members to make suggestions for improvements and stated he liked the idea of looking at distinct functions for the entire City.

Discussion followed regarding location of the survey and results, upcoming surveys, the possibility of issuing shorter surveys on a more frequent and regular basis.

City Manager Kiff reported that the City's goal is issuing a survey every two years to determine residents' satisfaction with the City's performance.

Mayor Pro Tem Dixon noted the need to review each recommendation, perhaps at the next Finance Committee meeting and suggested providing suggestions for benchmarking in terms of quality of life goals and financial metrics.

Chair Curry opened public comments.

Jim Mosher commented positively on the quality of employees in the City and agreed that more thought needs to be given in terms of measuring the City's performance in the services it delivers. He added that he is skeptical of surveys.

With no further public comments, Chair Curry closed public comments.

D. WASTEWATER SERVICE IN NEWPORT BEACH

Summary:

The City Council has requested a review of the City's Wastewater Operation as part of the City's on-going effort to review operations for effectiveness, efficiency and cost. This report provides the roles and responsibilities of the Division.

Recommended Action:

Provide recommendation to the City Council considering the following options:

1. Keep the Wastewater Division as an in-house municipal function.
2. Engage a consultant to review the efficiency and effectiveness of the Division.
3. Consider outsourcing the maintenance function to a third party through a Request for Proposal Process (RFP).
4. Consider annexation of the system to another governmental entity such as a special district.

Municipal Operations Director George Murdoch provided a PowerPoint presentation addressing a detailed Wastewater Service Report, goals and objectives of the Wastewater Division, maintenance of laterals, number of structures services, pump stations, responding quickly to prevent property damage and spills, service overview, staff reductions, outsourcing and annual contributions to the General Fund. He addressed the wastewater budget, revenues, functions currently being outsourced, other outsourcing opportunities, and challenges in terms of finding a pump station operations provider. Municipal Operations Director Murdoch addressed proposals for cleaning operations and noted that it appears the City can perform this task less expensively than by outsourcing. He commented on lateral replacements, the City's hourly rates, including pensions, and other outsourcing options.

Council Member Petros pointed out that Costa Mesa Sanitary District recently raised its rates.

In response to Mayor Pro Tem Dixon's question regarding access to reclaimed water, Municipal Operations Director Murdoch reported that all of the recycled water lines in the City are owned and operated by the Orange County Water District. He added that they have agreed to expand the program beyond the recycled program, that the City does not have the appropriate infrastructure in place and commented on Proposition 84 funds.

Municipal Operations Director Murdoch addressed pros and cons.

Council Member Petros expressed appreciation to staff for the work and commented on getting a second opinion. He suggested getting a consultant to review this, holistically, to see if there are any other opportunities.

Council Member Petros departed the meeting at this juncture.

Municipal Operations Director Murdoch provided potential next steps and asked for the Committee's comments in terms of recommendations to forward on to Council.

Discussion followed regarding the time involved in hiring a consultant to review the operation, the possibility of issuing an informal RFP, obtaining guidance in terms of increasing rates, the importance of having control over the function, whether staff would be comfortable outsourcing specific functions, being able to respond to emergency situations, and budgeting.

Committee Member O'Neill sought clarification concerning the anticipated infrastructure spending of approximately \$1,000,000 per year. Municipal Operations Director Murdoch and City Manager Kiff addressed the City's adopted master infrastructure plan submitted to the County. City Manager Kiff noted stated that there are consequences if the City decides not to fund it.

Chair Curry opened public comments.

Jim Mosher addressed sewage spills in the City of Newport Beach compared with those in the City of Costa Mesa. He commented on the Costa Mesa Sanitary District conducting a Proposition 218 rate study and suggested discussions between them and City staff, especially in terms of annexing systems as they are currently discussing plans to move their headquarter buildings. Regarding outsourcing, he stated that Orange County Sanitary District outsourced 100

miles for cleaning and that they have decided to do it in-house, once again. Additionally, they have a different service model.

With no further public comments, Chair Curry closed public comments.

Discussion followed regarding after-hour calls, videoing services and key Division functions.

Chair Curry believed there is not enough current information to make recommendations to Council to contract out the entire Department and that the Committee should direct staff to continue providing services as they have been and outsource those functions that can be outsourced for increased efficiency. He expressed concerns regarding directing more and more consultant studies.

Committee Member Tucker summarized that three important considerations came out of the discussion: (i) Outsourcing all functions would mean that the City would have to rely on a third party which may not be positioned locally to respond to emergency spills, rather than City staff performing that critical function; (ii) Merger with another entity would mean the City Council would no longer control the rate charged to rate payers; and (iii) If the City determined to not raise rates, it may not be able to implement the adopted Master Plan, unless it identified other sources of funds or alternatively, amended the Master Plan to a plan that could be implemented with finances available. Committee Member Tucker suggested the Council should weigh in on the policy issues described before the Finance Committee could make a recommendation.

Mayor Pro Tem Dixon suggested letting Council know that staff has reviewed the matter fully to determine functions that should and should not be outsourced.

E. CITY COUNCIL POLICY F-9 CITY VEHICLE/EQUIPMENT GUIDELINES

Summary:

City Council Policy F-9 establishes the service life of vehicles and equipment and helps determine funding requirements for their replacement. At the request of City Council and due to a number of changes in operations, staff requests the Finance Committee to review and comment on the proposed changes.

Recommended Action:

Provide direction to staff on the proposed changes.

Interim Assistant City Manager Carol Jacobs provided a brief report addressing proposed revisions to City Council Policy F-9. She noted wanting to expand the number of years in which the City keeps vehicles. She noted the savings of approximately \$1 million to the internal service fund.

Discussion followed regarding Police patrol vehicles.

Chair Curry opened public comments.

Jim Mosher questioned some of the changes and made suggestions for additional changes and commented on the expected service life.

With no further public comments, Chair Curry closed public comments.

Committee Member O'Neill moved and Committee Member Warner seconded, to recommend staff forward the recommendation to the City Council. The motion carried with 5 ayes, and 2 absent (Committee Member McCullough and Council Member Petros).

F. ERP UPDATE

Summary:

ERP (Enterprise Resource Planning) software is a business management software system that integrates all of the City's core functional requirements for financials, human capital management, citizen services, and revenues. The ERP implementation is scheduled to take between 25 and 30 months and will consist of five major phases. The City has completed Phase 1 (Financials) and is currently implementing Phase 2 (HR/Payroll) and Phase 3 (Utility Billing/Revenue), each scheduled to be operational in January 2016 and May 2016, respectively. The software provider of the City's ERP is Tyler Technologies Inc. and this project is titled "eSAIL," short for ERP System Administration and Implementation Lineup.

Recommended Action:

Receive and file.

Deputy Finance Director Steve Montano provided an update on the City's Enterprise Resource Planning (ERP) software. He noted phases completed and noted that the City is on schedule to implement all phases of the ERP program by October 2016.

Brief discussion followed regarding costs.

Chair Curry opened public comments.

Chair Curry closed public comments.

G. FINANCE COMMITTEE SCHEDULE UPDATE

Summary:

The Finance Committee work plan represents the planned topics of discussion; however, is subject to change based on the availability of Committee members, information and the need to schedule other topics as they arise. This item allows Committee consideration of an update to the work plan schedule.

Recommended Action:

Discuss and confirm upcoming meeting dates.

Chair Curry noted a conflict with the next Finance Committee meeting of September 10, 2015, and suggested meeting either September 15 or 16.

There was consensus to direct staff to schedule the next Finance Committee on September 16, 2015, at 4:00 p.m.

VI. ADJOURNMENT

The Finance Committee adjourned at 6:30 p.m. to the next regular meeting of the Finance Committee on September 16, 2015, at 4:00 p.m.

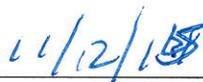
Filed with these minutes are copies of all materials distributed at the meeting.

The agenda for the Regular Meeting was posted on August 10, 2015, at 4:00 p.m., in the binder and on the City Hall Electronic Board located in the entrance of the Council Chambers at 100 Civic Center Drive.

Attest:



Keith Curry, Chair
Finance Committee Chair



Date