



CITY OF COSTA MESA CITY MANAGER'S OFFICE

June 3, 2025

To the Honorable Mayor, Members of the City Council, and Citizens of Costa Mesa:

It is my pleasure to present the City of Costa Mesa's Proposed Fiscal Year 2025-26 Operating and Capital Improvement Budget. City staff have carefully considered the City Council's priorities and goals during the budget development process to ensure the essential services and needs of the City are met. The current uncertainty regarding potential impacts of United States policies on global, domestic, and local economic conditions presents a challenging environment for both consumers and businesses. As a result, it is prudent to anticipate some slowdown in revenues leading into Fiscal Year 2025-26, particularly in Sales Tax and Transient Occupancy Tax, while Property Tax is expected to continue to experience modest growth. During the development of the Fiscal Year 2025-26 budget, the City diligently worked to balance the reduction in revenues due to economic uncertainties and the expected increase in cost for goods and services. However, you will find that, despite the decline in revenue and increase in costs, this carefully prepared budget ensures that services and programs will continue to be provided for its residents and business community.

The theme for the FY 2025-26 Proposed Budget is, "Focused. Efficient. Resilient." Staff will stay focused on the City's mission to serve its community; be efficient in all services delivered; while being resilient to the changing economic conditions. The dedication and collective efforts led by the City Council's leadership, of staff, residents, businesses, and the non-profit sector all working together to improve outcomes for all residents and visitors to Costa Mesa.

Guiding Principles

The guiding principles that shaped the FY 2025-26 Proposed Operating and Capital Improvement Budget were established when the City Council conducted a Strategic Planning workshop identifying key priorities, as well as the Mission Statement for Costa Mesa, as follows:

"The City of Costa Mesa serves our residents, businesses, and visitors by promoting a safe, inclusive, and vibrant community."

The City Council adopted five Strategic Plan Goals as outlined below:

- Strengthen the Public's Safety and Improve the Quality of Life;
- Achieve Long-Term Fiscal Sustainability;
- Recruit and Retain High Quality Staff;
- Diversify, Stabilize, and Increase Housing to Reflect Community Needs; and
- Advance Environmental Sustainability and Climate Resiliency.

In addition to the five goals, the City Council adopted six Core Values as part of their Strategic Plan:

- Integrity
- Sustainability
- Innovation
- Compassion
- Inclusion
- Collaboration

The recommendations in the FY 2025-26 Proposed Budget are rooted in the Strategic Plan Goals and Core Values created by the City Council for a safe, inclusive, and vibrant City. The FY 2025-26 Proposed Budget underwent a thorough review and in-depth analysis by multiple levels of staff. Funding requests contained herein to ensure both short-and-long term fiscal sustainability, while committing resources to achieve the City Council's goals.

Recommended budget adjustments in the Proposed Budget were carefully considered based on operational needs, the provision of essential core services to the community and the effective implementation of the City Council's stated Goals and Priorities.

Overview of FY 2025-26 Proposed All Funds Budget

The Fiscal Year 2025-26 Budget reflects the operating and capital spending plans for the General Fund, Special Revenue Funds, Capital Project Funds, and Internal Service Funds. The total proposed budget for all funds is \$224.4 million, a decrease of \$15.4 million, or 6 percent compared to the Fiscal Year 2024-25 Adopted Budget of \$239.8 million. Table 1 illustrates these amounts.

Table 1 – Proposed Budget – All Funds

| Expenditure Category | Adopted FY 2024-25 | Proposed FY 2025-26 | Increase/(Decrease) | | FY 2025-26 % of Total |
|----------------------|-----------------------|------------------------|---------------------|---------|--------------------------|
| | | | Amount | Percent | |
| Operating Budget | \$ 199,282,606 | \$ 204,133,821 | \$ 4,851,215 | 2% | 91% |
| Transfers Out | 12,631,498 | 3,547,836 | (9,083,662) | -72% | 2% |
| Capital Budget | 27,901,236 | 16,693,612 | (11,207,624) | -40% | 7% |
| Total | \$ 239,815,340 | \$ 224,375,269 | \$ (15,440,071) | -6% | 100% |

The All-Funds Budget for the City includes both governmental and proprietary funds. Governmental funds include the General Fund, Special Revenue funds and Capital Projects funds. The Special Revenue Funds are grants and other restricted funds designated for specific services and purposes provided by higher levels of government (i.e., Federal, State and County governments and agencies). Some of these funds receive ongoing revenue streams, while some are one-time competitive grants and require careful monitoring and record keeping. Proprietary funds are internal service funds that account for the City's equipment replacement, self-insurance and workers' compensation expenses, and information technology replacement costs.

In some instances, a fund can have available fund balances that have accumulated over time and are expended as the need arises and/or to complete specific projects within allotted timeframes. As such, the All-Funds Budget contains many funds that are separate entities with specific accounting and reporting requirements as per government regulations and in some cases, statutes.

The City's General Fund however, is not restricted and can be used to provide a broad array of public services and is comprised of multiple revenue sources including taxes (such as property, sales, and hotel taxes, among others), user fees, fines, facility rentals, and development related fees, to name a few.

Federal Funding

On January 27, 2025, President Trump signed an executive order freezing all federal funding, this provided recipients less than 24 hours before federal portals closed. City staff successfully secured over \$1.3 million in payments and continue to monitor policy changes to stay proactive of any changes to policy. The January 27th Executive Order on federal funding, and several subsequent Executive Orders, are currently frozen or suspended due to challenges within the courts. While policy shifts within the current Administration on spending, through the potential reduction of Federal grants, have yet to directly impact the City—these evolving changes could potentially thwart revenue sources to multiple departments within the City including, but not limited to the Police Department, Public Works, and Development Services.

Some of the Federally funded grants the City receives include Community Development Block Grant (CDBG), Home Investment Partnerships Program (HOME) Grant, and Local Action Early Plan (LEAP) Grant—all three of which are from the Department of Housing and Urban Development (HUD). Other Federal grants the City has been awarded include Justice Assistance Grant from the Department of Justice; Emergency Management Performance Grant (EPMG) from the Department of Homeland Security; and multiple road and safety grants provided by the US Department of Transportation.

Operating Budget

During the development of the Fiscal Year 2025-26 Proposed Budget, staff were directed to request only necessary budget increases that provide crucial services to the City. The proposed Operating Budget incorporated minimal growth of 2%, or \$4.9 million, in expenses to provide essential services. Leadership made a concerted effort to ensure a balanced All Funds budget of \$204.1 million in the FY 2025-26 Operating Budget.

Arts and Culture Master Plan Fund

The FY 2025-26 Proposed Budget includes the budget of year five of the Arts and Culture Master Plan Fund in the amount of \$416,990, of which \$227,472 is expected to be funded through the ½ cent Cannabis Measure Q tax allocation for the Arts. In the Arts and Culture Master Plan, \$141,000 is budgeted for various free art experiences for the community, such as ARTVenture, Art Crawl, Park Performances, and tickets for shows and performances.

Transfers Out

The proposed General Fund Transfers Out of \$2.8 million provides funding for the Information Technology Replacement Fund (Fund 603) to invest in the City's replacement of technology hardware and software. The overall transfers out decreased by \$6.9 million from the FY 2024-25 Adopted Budget due to the "Emergency Exception" clause of the Capital Asset Needs Ordinance under Section 2-209.2 (a)(2), Economic Downturn. City staff will be utilizing its Capital Improvement Program (Fund 401) fund balance to fund \$2.2 million in projects in the Proposed FY 2025-26 Capital Improvement Program, budget to ensure compliance with the required maintenance of effort (MOE).

Capital Assets Needs (CAN)

On March 3, 2020, the City Council updated the City's Financial and Budget Policies providing that the City allocates a minimum of five percent of General Fund revenues to fund capital expenditures and reallocate one and a half percent previously dedicated to the Capital Facilities Account to the City's Information Technology Needs. In the Proposed FY 2025-26 budget, staff is recommending a deferral of approximately \$6.9 million in General Fund contribution to the capital improvement fund.

Capital Budget

The FY 2025-26 Proposed CIP Budget was presented at the April 22, 2025, City Council Study Session. The focus of this fiscal year is to complete existing projects within the 5-Year Capital Improvement Plan list. The proposed All-Funds Capital Improvement Program (CIP) budget of \$16.7 million is a decrease of \$11.2 million, or 40 percent, from the Adopted FY 2024-25 budget. In addition to the \$16.7 million, the Capital Improvement Program includes \$12 million for the Fire Station #2 Reconstruction project that will be funded through future bond financing.

The \$16.7 million CIP budget consists of \$8.5 million in transportation projects, \$7.4 million in street improvement projects, \$250,000 in facilities improvement projects, and \$550,000 in park improvement projects. While the Operating Budget represents costs that are expected to be spent each year for City services and programs, the Capital Budget is by nature a multi-year expenditure plan where many of the projects are completed in phases over a multi-year period.

FY 2025-26 Proposed General Fund Budget Overview

The Proposed FY 2025-26 General Fund expenditure budget is a balanced budget and totals \$186.9 million. This reflects a decrease of \$3 million, or 2 percent, from the FY 2024-25 Adopted Budget of \$189.9 million. Table 2 is a summary of the FY 2025-26 General Fund Proposed Revenue and Expenditure Budget.

Table 2 – General Fund Revenue and Expenditure

| Revenue Source | Adopted FY 2024-25 | Proposed FY 2025-26 | Increase/(Decrease) | | FY 2025-26 % of Total |
|------------------------------|-----------------------|------------------------|-----------------------|------------|--------------------------|
| | | | Amount | Percent | |
| Taxes | \$ 163,213,634 | \$ 159,300,278 | \$ (3,913,356) | -2% | 85% |
| Licenses and Permits | 4,736,019 | 5,700,227 | 964,208 | 20% | 3% |
| Fines and Forfeitures | 1,302,091 | 1,302,091 | - | 0% | 1% |
| Use of Money and Property | 5,360,700 | 5,108,250 | (252,450) | -5% | 3% |
| Other Governmental Agencies | 896,086 | 959,207 | 63,121 | 7% | 1% |
| Fees and Charges for Service | 13,097,122 | 13,181,206 | 84,084 | 1% | 7% |
| Other Revenue | 1,288,507 | 1,304,347 | 15,840 | 1% | 1% |
| Total | <u>\$ 189,894,159</u> | <u>\$ 186,855,606</u> | <u>\$ (3,038,553)</u> | <u>-2%</u> | <u>100%</u> |

| Expenditure Category | Adopted FY 2024-25 | Proposed FY 2025-26 | Increase/(Decrease) | | FY 2025-26 % of Total |
|----------------------------|-----------------------|------------------------|-----------------------|------------|--------------------------|
| | | | Amount | Percent | |
| Salaries and Benefits | \$ 133,130,772 | \$ 137,367,315 | \$ 4,236,543 | 3% | 74% |
| Maintenance and Operations | 44,132,090 | 43,726,192 | (405,898) | -1% | 23% |
| Fixed Assets | 2,925,298 | 2,964,263 | 38,965 | 1% | 2% |
| Transfers Out | 9,705,994 | 2,797,836 | (6,908,158) | -71% | 1% |
| Total | <u>\$ 189,894,154</u> | <u>\$ 186,855,606</u> | <u>\$ (3,038,548)</u> | <u>-2%</u> | <u>100%</u> |

FY 2025-26 General Fund Revenue Highlights

The FY 2025-26 Proposed Budget for Total General Fund Revenues totals \$186.9 million, a reduction of \$3.0 million, or 2 percent decrease from the FY 2024-25 Adopted Budget. Economic and consumer challenges that impacted Sales Tax in FY 2023-24 and FY 2024-2025 continue to present potential headwinds in FY 2025-26 at the City, County, and State levels, and therefore have the biggest impact to overall City revenues. These funds typically are used to cover public safety, parks and community services, development services, and other activities and programs known to residents. The Fiscal Year commencing July 1, 2025, budget is balanced without the use of General Fund reserves.

Sales and Use Tax: Sales tax is the largest revenue category in Costa Mesa and is estimated at \$75.1 million for FY 2025-26, a reduction of \$6.5 million, or an 8 percent decrease from the FY 2024-25 Adopted Budget. General economic uncertainty due to the potential impact of tariffs on businesses and consumers, coupled with persistent inflation, and slower growth, could lead to a continued reduction in spending in such areas as automobiles, general consumer goods, and home renovations.

Property Tax: All combined Property Tax revenues are estimated at \$63.0 million, reflecting a 4 percent growth over the prior fiscal year budget. Despite continued higher

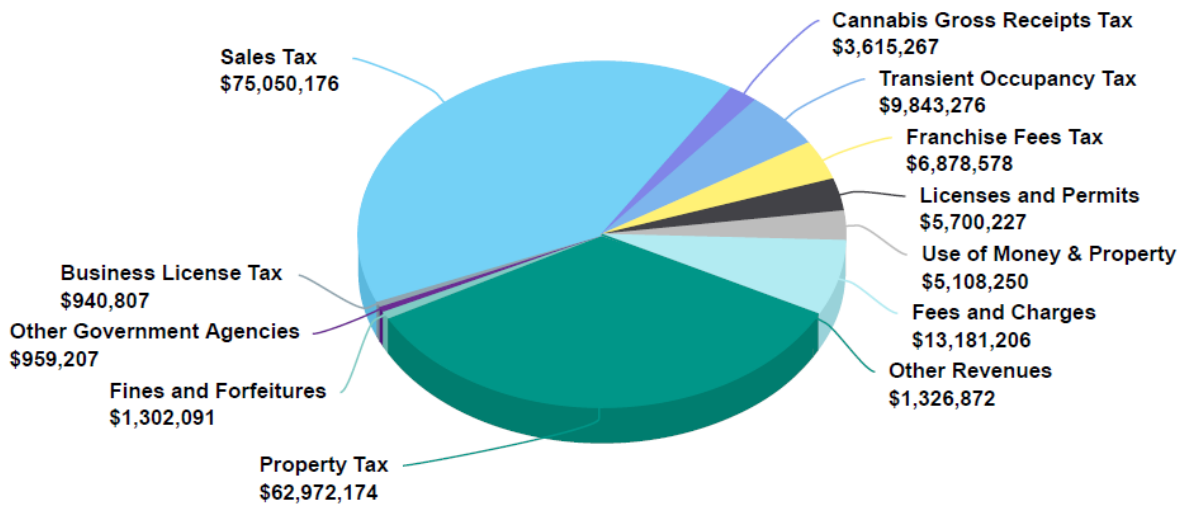
interest rates and limited supply, the competitiveness in the housing market continues to show resilience in terms of assessed values and number of home sales.

Transient Occupancy Tax (TOT): Hotel tax revenues are estimated at \$9.8 million next year, reflecting a 3 percent decrease to FY 2024-25 Adopted Budget. There is an anticipation of a potential slowdown in general consumer spending, and a reduction in international visitors to California. In addition, persistent inflation and economic uncertainty impact consumer confidence, discretionary income and savings levels, potentially impacting the travel and leisure segment of consumer spending.

Fees and Charges: Fees and Charges are estimated at \$13.2 million, a decrease of \$84,084, while Plan Check fee revenues are \$1.8 million in FY 2025-26. Staff is proposing a consumer price index (CPI) increase of 3.3% to certain fees and proposing a credit card processing fee of 2.7%. In addition, staff is proposing a Technology Enhancement Fee of 5% on all permit fees to recover costs of future development related technology enhancements and system replacement, as well as a General Plan Maintenance Fee of 5% for on all applicable building permit fees, to offset a portion of the periodic costs associated with General Plan and supporting document updates. Adopting a Technology Enhancement Fee and General Plan Maintenance Fee allows staff to reserve amounts collected and use them to offset the costs accordingly.

Measure Q Retail Cannabis Business Tax: On November 3, 2020, voters approved the “City of Costa Mesa Retail Cannabis Tax and Regulation” Measure, also known as Measure Q, which allows cannabis retail storefront and delivery uses. City Council voted to adopt a 7 percent tax on cannabis retail businesses. The FY 2025-26 Proposed Budget includes an estimated \$3.6 million in cannabis taxes, an increase of \$195,583, or 6 percent from FY 2024-25. To date the City has approved over 20 retail storefront and non-storefront businesses. Also, as previously approved by the City Council, the Proposed Budget has two restricted special revenue funds that are financed by the cannabis retail tax: The Arts and Culture Master Plan Fund (130) and First Time Homebuyers Fund (140).

Graph 1 – General Fund Revenue Estimates by Category



FY 2025-26 General Fund Budget Expenditure Highlights

The Proposed Operating General Fund Budget for FY 2025-26 reflects total expenditures of \$185.6 million. Of this amount, \$180.2 million in operating costs represents an increase of \$2.9 million, or 1.7 percent, compared to the current year's adopted operating budget of \$189.9 million. The General Fund will transfer \$2.4 million to the Information Technology Fund, as described earlier. With the economic uncertainties, the City funds must be prudently allocated to areas where they will provide the greatest impact. The FY 2025-26 Proposed Budget for expenditures includes the following significant items:

- Salaries and benefit increase of \$133,286 for a full-time Custody Officer in the Police Department.
- Includes \$30,000 for firefighter personal protective equipment and \$20,000 for training and supplies for the Emergency Operations Center and 9-1-1 Center in Fire and Rescue Department.
- A \$1.8 million increase in annual required CalPERS contributions.
- An additional \$2.3 million in compensation, as required per contractual MOU requirements.
- Continuation of the \$4.3 million vacancy factor (negative appropriation).
- No use of General Fund Reserves to balance the General Fund.

Graph 2 – General Fund Total Appropriation by Department

**Total Appropriations - General Fund - \$186.9 (includes Capital Improvement)
(in millions)**

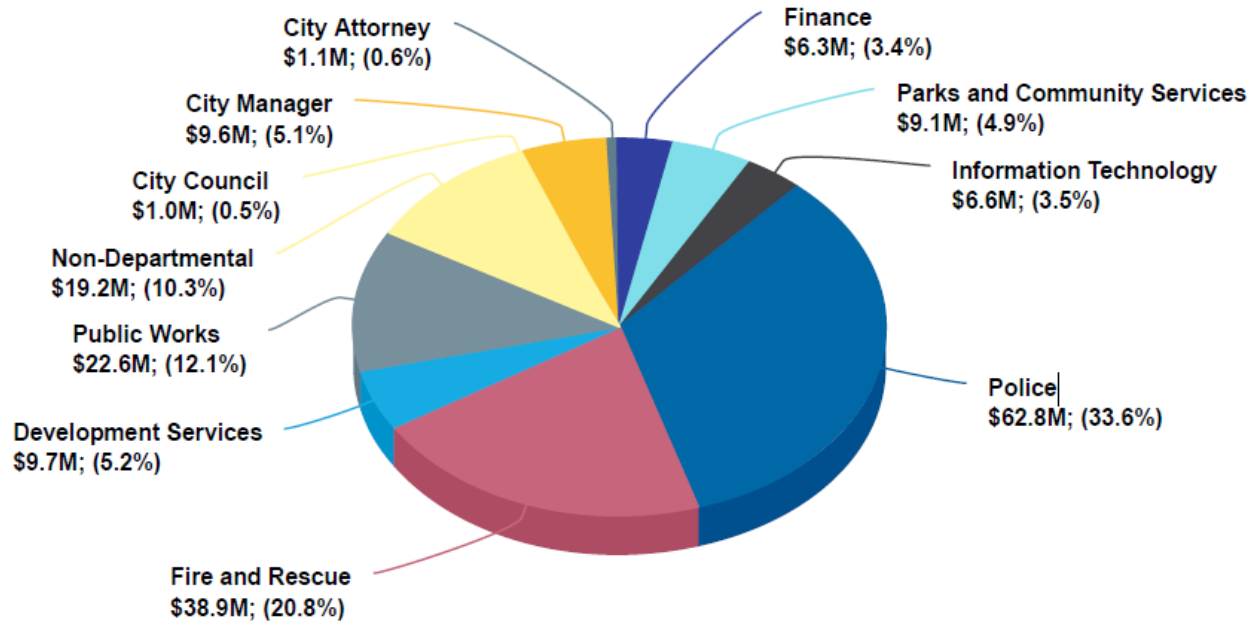


Table 3 – Breakdown of General Fund Appropriation by Department

| Department | FY 2020-21 Actual | FY 2021-22 Actuals | FY2022-23 Actual | FY 2023-24 Actual | FY 2024-25 Adopted | FY 2025-26 Proposed |
|---------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|------------------------|
| City Council | \$ 644,712 | \$ 867,909 | \$ 834,337 | \$ 750,577 | \$ 874,089 | \$ 954,143 |
| City Manager* | 6,068,680 | 6,505,480 | 7,573,363 | 8,902,755 | 9,594,377 | 9,613,230 |
| City Attorney | 968,029 | 958,775 | 988,108 | 977,061 | 1,086,750 | 1,123,700 |
| Finance | 4,485,375 | 3,811,155 | 4,271,188 | 4,416,583 | 6,073,764 | 6,296,502 |
| Parks and Community Services | 7,414,732 | 6,379,328 | 7,371,372 | 9,753,352 | 9,037,068 | 9,101,830 |
| Information Technology | 3,760,148 | 4,104,946 | 5,133,365 | 5,567,967 | 6,402,558 | 6,570,716 |
| Police | 48,905,944 | 53,504,411 | 55,874,470 | 62,005,909 | 61,919,751 | 62,820,471 |
| Fire and Rescue | 27,042,315 | 32,298,517 | 33,480,396 | 35,159,635 | 37,772,922 | 38,903,466 |
| Economic & Development Services | 6,325,666 | 7,522,770 | 8,229,755 | 9,082,786 | 9,911,803 | 9,695,734 |
| Public Works | 17,801,071 | 19,517,456 | 20,413,479 | 23,101,963 | 23,659,001 | 22,553,602 |
| Non-Departmental | 11,614,781 | 27,397,679 | 32,457,225 | 23,423,354 | 23,562,076 | 19,222,213 |
| Total | \$ 136,637,270 | \$ 162,868,426 | \$ 176,627,058 | \$ 183,141,942 | \$ 189,894,159 | \$ 186,855,607 |

*City Manager's Department includes City Clerk, Human Resources, and Risk Management

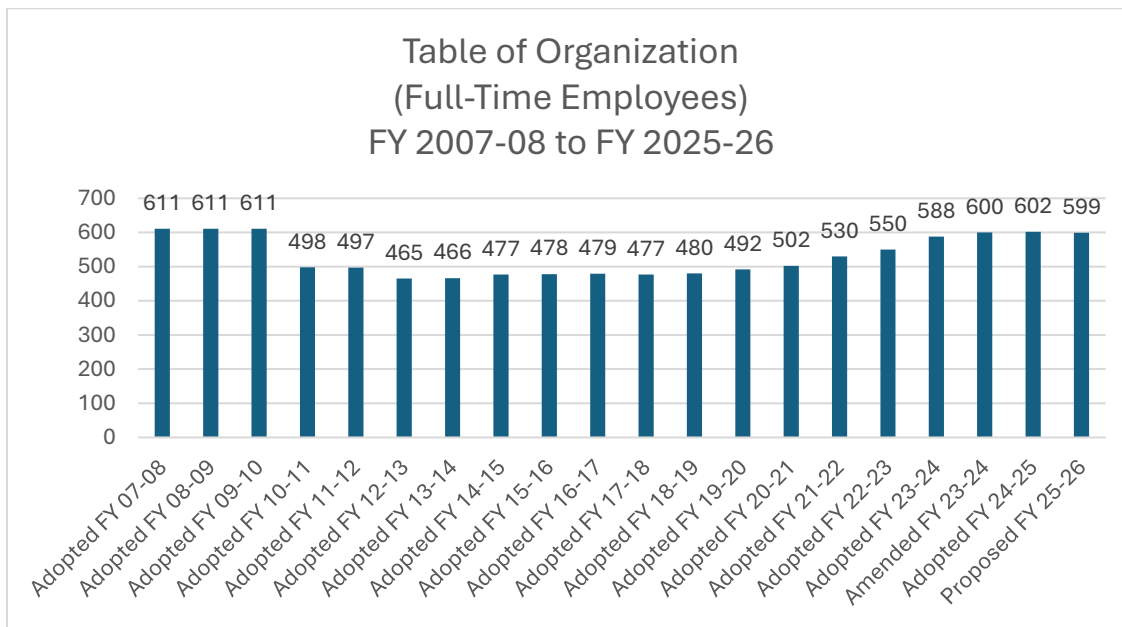
Staffing Levels

On April 1, 2025, the City implemented a soft hiring freeze of positions outside of public safety. The FY 2025-26 Proposed Budget includes 599 full-time employees, which reflects a net decrease of three (3) positions. Positions eliminated were in the City Manager's Department, which includes one (1) Human Resources Analyst, one (1) Programmer Analyst I, and one (1) Senior Management Analyst (CON) all funded by the General Fund. Additionally, one (1) Community Outreach Worker position was eliminated in the Housing Authority Fund (Fund 222). However, there is an increase of one (1) Custody Officer in the Police Department that is vital to managing the workload of the City's current jail staff. Custody Officers are needed for the transportation and booking of arrestees to the Orange County Jail. This one additional Custody Officer will alleviate staffing challenges, promote safety and wellness, and reduce overtime costs.

Table 4 – Change in Staffing Levels

| Department | Job Title | FTE |
|-------------------------------------|------------------------------|---------------|
| Other Funds | | |
| City Manager | Community Outreach Worker | (1.00) |
| Other Funds Total | | (1.00) |
| General Fund | | |
| City Manager | Human Resources Analyst | (1.00) |
| City Manager | Programmer Analyst I | (1.00) |
| City Manager | Sr. Management Analyst (CON) | (1.00) |
| Police Department | Custody Officer | 1.00 |
| General Fund Total | | (2.00) |
| Grand Total All Funds Impact | | (3.00) |

Table 5 - Budgeted Citywide Staffing Levels



The Table of Organization reflects 599 full-time employees, however, not included is the allocation of 107.48 part-time employees for a total of 706.48.

Strengthen the Public's Safety

The FY 2025-26 Proposed Budget allocates \$101.7 million as the City's commitment to public safety, comprising both the Police and Fire Departments. Public safety budgets account for more than 53 percent of the General Fund Proposed Budget, with 34 percent allocated to the Police Department and 21 percent to the Fire and Rescue Department. Of the 599 citywide full-time personnel, approximately 38 percent are sworn officers—consistent with funding levels prior to the Great Recession.

The Police Department budget includes 142 full-time sworn personnel. The Proposed Budget adds one new Custody Officer. Additionally, the Police Department manages the entire Animal Services and Enforcement Program.

The Police Department's salaries and benefits budget increased by a net of \$1.0 million, primarily due to labor contractual agreements and retirement benefits. As in prior years, and to balance the General Fund, the Department includes a vacancy factor of approximately \$3.7 million to account for its vacancy rate.

The Fire and Rescue Department consists of 85 full-time sworn personnel. Its salaries and benefits budget increased by a net of \$1.1 million, largely due to labor contractual agreements and retirement costs. The Fire and Rescue Department includes an increase of \$30,000 to fund additional firefighter personal protective equipment, and \$20,000 to fund training and miscellaneous supplies for the Emergency Operating Center and the Dispatch Communications Center (9-1-1 Center).

General Fund Reserves Overview

The City continues to demonstrate strong fiscal prudence and controls over spending. The combined commitment for emergency reserves including the declared disaster and economic reserves, is indicative of financial discipline. The General Fund reserves are currently at \$60.3 million and exceed the City Council policy of \$55.0 million by \$5.3 million.

Table 6 - General Fund Balance Overview

| Fund Balance Category | FY 2020-21 | FY 2021-22 | FY 2022-23 | FY 2023-24 | FY 2024-25 |
|-----------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| | Audited | Audited | Audited | Audited | Estimate |
| Committed | | | | | |
| Declared Disasters | \$14,125 | \$14,125 | \$14,125 | \$14,125 | \$14,125 |
| Self-Insurance | 2,000 | 2,000 | 2,000 | 2,000 | 2,000 |
| Economic Reserves | 9,000 | 9,000 | 9,000 | 9,000 | 9,000 |
| Assigned | | | | | |
| Compensated Absences | 5,920 | 5,584 | 6,210 | 5,982 | 5,982 |
| Police Retirement 1% Supplemental | 2,275 | 1,885 | 1,737 | 1,572 | 1,572 |
| Workers Compensation | | 1,000 | 2,000 | 2,000 | 2,000 |
| Facilities Reserve | | 2,000 | 2,000 | 2,000 | 2,000 |
| Strategic Plan Project | | 2,000 | 2,000 | 2,000 | 2,000 |
| Restricted | | | | | |
| Pension and OPEB | 1,778 | 3,061 | 3,178 | 3,367 | 3,367 |
| Non-spendable | 965 | 604 | 459 | 631 | 631 |
| Unassigned | 17,429 | 16,517 | 16,328 | 17,686 | 17,686 |
| Total Fund Balance | \$53,492 | \$57,776 | \$59,037 | \$60,363 | \$60,363 |

Conclusion

The Fiscal Year 2025-26 Proposed Budget reflects a strong commitment to the City Council, residents, and community partners by ensuring the delivery of high-quality core public services and fulfilling the City Council's highest goals and priorities.

We hope and believe that the FY 2025-26 Proposed Budget theme, "Focused. Efficient. Resilient." embodies the values of the City of Costa Mesa and serves to enhance the quality of life for all its residents, regardless of their circumstances.

I would like to extend my gratitude to the Finance Department and its Budget Team, as well as the Executive Team, their managers, and departmental budget liaisons, for their dedication in preparing the FY 2025-26 Proposed Operating and Capital Improvement Budget. Under the City Council's leadership, Costa Mesa will continue working alongside residents and community partners to ensure access to essential services and foster healthy, sustainable neighborhoods for everyone who calls Costa Mesa home.

Respectfully submitted,

Cecilia Gallardo-Daly
Acting City Manager
City of Costa Mesa