



CITY OF COSTA MESA

77 Fair Drive
Costa Mesa, CA 92626

Agenda Report

File #: 26-279

Meeting Date: 5/12/2026

TITLE:

FISCAL YEAR 2026-27 PROPOSED BUDGET STUDY SESSION

DEPARTMENT: FINANCE DEPARTMENT

PRESENTED BY: CECILIA GALLARDO DALY, CITY MANAGER,
MARK KHOU, BUDGET & PURCHASING MANAGER

CONTACT INFORMATION: MARK KHOU, BUDGET & PURCHASING MANAGER,
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RECOMMENDATION:

Conduct a Study Session on the Fiscal Year 2026-27 Proposed All Funds Budget of \$244.9 million, with a General Fund component of \$200.0 million, and provide feedback and direction to staff in advance of final adoption of the budget by June 30, 2026. City staff is presenting a FY 2026-27 Proposed Budget that is structurally balanced, ensuring ongoing revenues fully support expenditures while maintaining the City's commitment to long-term fiscal sustainability while continuing to provide the highest level of service.

BACKGROUND:

The Fiscal Year 2026-27 Proposed Budget includes collaboration efforts throughout all sectors, including public safety, parks, facilities, streets, and housing for the City of Costa Mesa residents, businesses, and visitors. Recommended budget adjustments contained in the Proposed Budget were carefully selected based on operational needs, the provision of essential core services to the community, and the implementation of the City Council's stated Goals and Priorities. The Fiscal Year 2026-27 Proposed Budget is balanced without the use of General Fund reserves. The City continues its commitment to strengthening the public's safety and improving the quality of life by dedicating 55% of the General Fund's budget to Public Safety. Furthermore, this Proposed Budget includes the full allocation and repayment of deferrals to both the Capital Asset Needs (CAN) and Information Technology Replacement Funds (ITRF) to support facility and infrastructure needs throughout the city.

While the City is presenting a structurally balanced FY 2026-27 Proposed Budget, it is important to recognize the broader uncertainty created by ongoing geopolitical tensions. Global supply chain disruptions, fluctuating energy markets, and volatility in international trade continue to pose risks that can ripple into the local economy. These external factors may influence revenue streams such as sales tax, tourism-related activities, and construction costs, all of which play a critical role in municipal operations.

The City is expecting modest increases in Sales Tax and Property Tax revenues. Transient Occupancy Tax is expected to grow but may soften if elevated fuel prices persist for a prolonged

period, which may affect travel patterns and consumer spending on travel activities. Development of the Fiscal Year 2026-27 Proposed Budget reflects a balancing of revenue projections with the expected increase in the cost of goods and services. Despite modest revenue growth and rising operational costs, the carefully crafted budget ensures that the City continues to deliver high-quality services and programs to our residents and business community. Staff will continue to closely monitor economic indicators and remain prepared to adjust revenue projections and expenditures as conditions evolve to maintain fiscal sustainability.

Guiding Principles

The guiding principles that inspired the recommendations for the FY 2026-27 Proposed Budget are based on the City Council's mission, goals, and priorities, which are as follows:

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

City Council Strategic Plan Goals:

- 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
- Advance Environmental Sustainability and Climate Resiliency
- Maintain and Enhance the City's Facilities, Technology, and Equipment

The recommendations contained in the FY 2026-27 Proposed Budget are rooted in the City Council's Strategic Plan Goals focused on fostering a safe, inclusive, and vibrant community.

ANALYSIS:

The theme for the FY 2026-27 Proposed Budget is "Measured Decisions. Meaningful Impact." Staff will remain focused on the City's mission to serve its community; be efficient in all services delivered, while being resilient to the changing economic conditions. This budget fully funds the Homeless and Behavioral Health Program, Capital Asset Needs, Information Technology Replacement Fund, Self-Insurance Fund, and Equipment Replacement Fund, enabling Departments to achieve shared goals in addressing our most pressing needs and concerns.

Funding requests contained in the FY 2026-27 Proposed Budget help to further stabilize or enhance critical City operations to better serve the public, and/or provide City employees with the essential technology, equipment, and overall tools to perform their public service effectively. The Proposed Budget helps ensure both short-and-long-term fiscal sustainability, while committing resources to achieve the Council's goals. As the cost of operating the City continues to rise, it was appropriate to anticipate that overall expenditures would begin to outpace revenues. Hence, the need to continue to explore new revenue opportunities. Forecasts indicated that the City's total expenditures were expected to exceed projected revenues.

To address and develop a balanced Budget for the Fiscal Year 2026-27, departments reviewed operational expenses and identified opportunities to defer or reduce expenditures without impacting core services. Following a comprehensive evaluation of departmental expenses, staff identified one-time savings that can be implemented without affecting the City’s primary services. At the same time, staff continue to evaluate long-term revenue strategies to ensure the City can sustainably meet its future operational needs. This includes assessing potential revenue enhancements, monitoring economic trends, and identifying opportunities to strengthen the City’s fiscal position. Together, these efforts support the City’s commitment to maintaining service levels, advancing Council priorities, and ensuring long-term financial resilience.

Overview of FY 2026-27 Proposed All Funds Budget

The Fiscal Year 2026-27 Proposed Budget is balanced and 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 \$244.9 million, an increase of \$19.9 million, or 9 percent, compared to the Fiscal Year 2025-26 Adopted Budget of \$224.9 million. Table 1 illustrates these amounts.

Table 1 - Proposed Budget - All Funds

Expenditure Category	Adopted	Proposed	Increase/(Decrease)		FY 2026-27
	FY 2025-26	FY 2026-27	Amount	Percent	% of Total
Operating Budget	\$ 202,433,823	\$ 211,466,653	\$ 9,032,830	4%	86%
Transfers Out	3,547,836	9,825,324	6,277,488	177%	4%
Capital Budget	18,957,631	23,585,595	4,627,964	24%	10%
Total	\$ 224,939,290	\$ 244,877,572	\$ 19,938,282	9%	100%

The All-Funds Budget for the City includes both governmental and proprietary funds. Governmental funds include the General Fund, Special Revenue Funds, Internal Services Funds and Capital Improvement Funds. Special Revenue Funds consist of grants and other restricted revenues designated for specific programs or services, typically provided through Federal, State, or County agencies. Some of these funds receive ongoing revenue streams, while others are awarded as one-time competitive grants that require careful monitoring, compliance, and record-keeping. Proprietary Funds include the City’s internal service operations, such as equipment replacement, self-insurance programs, and information technology replacement. These funds ensure that critical internal services are properly maintained and financially supported over time. Finally, Capital Improvement Funds support major capital projects that generally span multiple fiscal years.

In some cases, individual funds may carry accumulated fund balances that can be used as needs arise or to complete specific projects within required timeframes. As a result, the City’s All-Funds Budget is composed of numerous distinct funds, each with its own accounting and reporting requirements established by government regulations and, in some instances, by statute.

The General Fund is the City’s primary operating unrestricted fund and supports a broad range of public services. It is funded through multiple revenue sources, including property, sales, hotel and cannabis taxes, as well as user fees, fines, facility rentals, and development-related charges, among others.

For Fiscal Year 2026-27, the Proposed All-Funds Budget totals \$244.9 million, an increase of 9 percent from the previous adopted year and consists of an increase in all expenditure categories: operating, transfers out and capital budget.

Operating Budget

The FY 2026-27 total proposed operating budget for All Funds is \$211.5 million, an increase of \$9.0 million, or 4 percent, compared to the FY 2025-26 Adopted Budget of \$202.4 million. This includes realigning budgets to include year-over-year actuals in some areas. The FY 2026-27 All Funds Proposed Operating Budget is balanced and comprised of several items including:

General Fund

- \$250,000 increase in the City Manager Department's City Clerk Division for bi-annual elections.
- A salary and benefit budget decrease of \$158,442 in the Police Department for a full-time Park Ranger, and an overtime increase of \$122,000 for the City's jail operations.
- \$62,000 increase in the Police department Operating Budget to support the City's Animal Care services and security services for City Council meetings.
- Realignment resulting in an increase of \$79,321 for Part-Time positions in the Parks and Community Services Department.
- Adjustment resulting in an increase of \$70,968 due to CPI for the Parks and Community Services Department to support the lease agreement with Newport Mesa Unified and other operational needs.
- Reallocation of the Emergency Service Coordinator position to a sworn Battalion Chief with a net \$176,603 increase to the Fire Department Proposed Budget.
- A \$33,711 increase due to CPI for the City Attorney's annual contractual agreement.
- \$2.0 million increase to the annual CalPERS Unfunded Actuarial Liability (UAL) payment.
- Incorporates a citywide vacancy factor in the salary and benefits budget, calculated at 2% of the operating budget.

Other Funds

- \$220,000 increase in Measure M2 Fairshare (Fund 416) to utilize annual allocations towards City's traffic signal maintenance.
- The Gas Tax (Fund 201) has a \$350,000 budget increase to support tree trimming and maintenance along medians and public-right-of-way.
- \$508,693 increase in the Self Insurance Fund (602) for insurance premiums.
- \$66,000 one-time increase in Drainage Fund (Fund 209) to support legal advertising/filing fees.

Additionally, departments identified numerous temporary operational reductions totaling approximately \$1.7 million in savings to the Proposed FY 2026-27 General Fund Budget.

Transfers Out

Transfers Out from All funds totaled \$9.8 million, an increase of \$6.3 million. Ordinance No. 2020-06 requires the City to contribute 5% of annual General Fund revenues to the Capital Improvement Fund (Fund 401) and 1.5% to the Information Technology Replacement Fund (Fund 603). In the Proposed FY 2026-27 Budget, Transfers Out from the General Fund total \$9.8 million, with \$6.7 million allocated to Fund 401 and \$3.1 million allocated to Fund 603. This amount includes the repayment of previously deferred contributions to the Capital Asset Needs (CAN) program and the Information Technology Replacement Fund (ITRF), totaling \$717,047.

Information Technology Replacement Fund

This fund accounts for the accumulation of resources necessary to fund Information Technology Projects, including hardware and software replacements. As per the City's Municipal Code Section 2-209.4, 1.5% of General Fund revenues are allocated to the Information Technology Replacement Fund (ITRF) to provide funding for the City's immediate and future information technology needs, including those identified in the Information Technology Strategic Plan (ITSP). In FY 2026-27 Proposed Budget, \$3.1 million will be funded from the General Fund for the Citywide Computer Replacement Program, depreciation and staffing salaries and benefits related to the ITSP.

Self-Insurance Internal Service Fund

This fund accounts for the general liability premiums, and the City is proposing an increase of \$0.5M due to increasing insurance premiums.

Capital Budget

The proposed all-funds Capital Improvement Program (CIP) budget of \$22.0 million is an increase of \$3.0 million, or 8 percent, from the adopted FY 2025-26 budget. Of the City's \$22.0 million Proposed Capital Improvement Budget, \$15.9 million will be funded through various City funds and grants. A comprehensive detail of the Proposed CIP Budget was presented to the City Council at the March 31, 2026, Study Session and is contained in further detail in the CIP section of the FY 2026-27 Proposed Budget Book.

A few key capital projects include:

- Costa Mesa Skate Park Expansion
- Harper Park Playground Replacement
- Moon Park Playground Replacement
- Newport Boulevard Improvement (RMRA funds)
- Police Department Real Time Crime Center
- Police Department Chillers Replacement
- Adams Avenue Active Transportation Improvements - Multipurpose Trails

- Harbor Boulevard Rehabilitation Project (RMRA funds)
- Park Security Lighting Replacement
- Bicycle and Pedestrian Infrastructure Improvements
- Clean Mobility Options Program - On-Demand Transit Services
- Pedestrian Safety Festival
- Fire Station #2 Reconstruction

FY 2025-26 Proposed General Fund Budget Overview

The Proposed FY 2026-27 General Fund budget is balanced and totals \$200.0 million. This reflects an increase of \$13.1 million, or 7 percent, from the FY 2025-26 Adopted Budget of \$186.9 million.

Table 2 is a summary of the Proposed FY 2025-26 General Fund Operating Budget.

Expenditure Category	Adopted	Proposed	Increase/(Decrease)		FY 2026-27
	FY 2025-26	FY 2026-27	Amount	Percent	% of Total
Salaries and Benefits	\$ 137,367,317	\$ 146,171,618	\$ 8,804,301	6%	73%
Maintenance and Operations	43,726,192	41,165,570	(2,560,622)	-6%	21%
Fixed Assets	2,964,263	2,804,063	(160,200)	-5%	1%
Transfers Out	2,797,836	9,825,324	7,027,488	251%	5%
Total	\$ 186,855,608	\$ 199,966,575	\$ 13,110,967	7%	100%

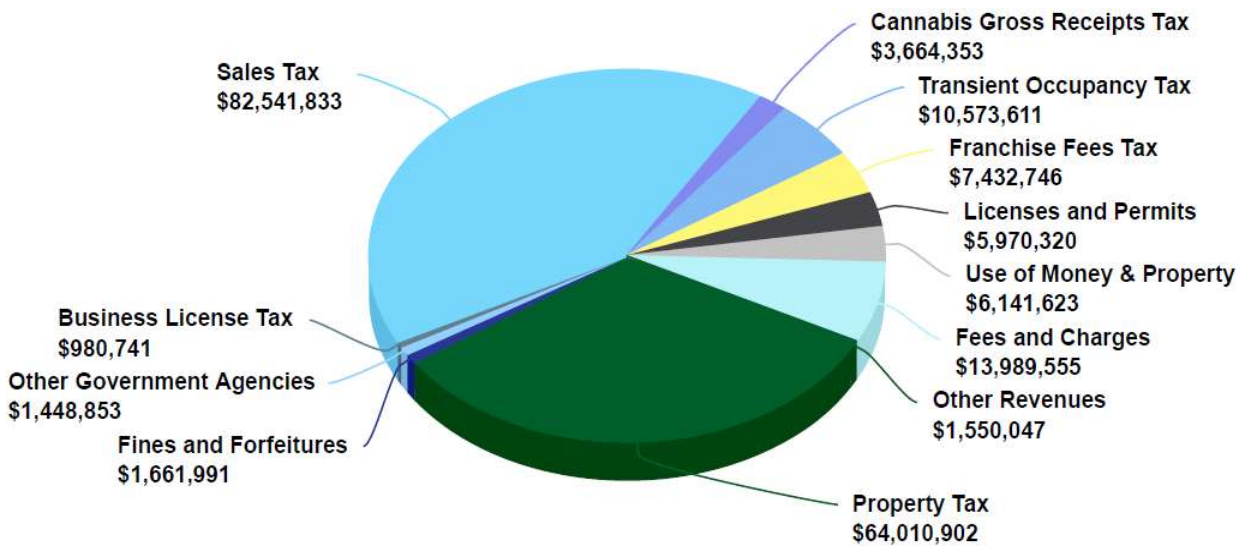
General Fund Revenue Highlights

The FY 2026-27 Proposed Budget for General Fund Revenues for all funds totals \$200.0 million, an increase of \$13.1 million, or 7 percent, from the FY 2025-26 Adopted Budget. Revenues are expected to have modest growth compared to the FY 2025-26 projected year-end of \$193.9 million. These funds are typically used to cover public safety, roads, parks and community services, development services, and other activities and programs for residents. In FY 2025-26. There were many uncertainties leading into the budget development process, including federal enforcement activity, changing tariff policies, and persistent inflation. These factors remain concerns; however, the City has seen modest revenue growth in certain categories. The fiscal year budget commencing July 1, 2026, will be balanced with projected revenues to offset expenses and without the use of reserves.

Table 3 - General Fund Revenue Estimates

Revenue Source	Adopted	Proposed	Increase/(Decrease)		FY 2026 27
	FY 2025 26	FY 2026 27	Amount	Percent	% of Total
Taxes	\$ 159,300,278	\$ 169,204,186	\$ 9,903,908	6%	85%
Licenses and Permits	5,700,227	5,970,320	270,093	5%	3%
Fines and Forfeitures	1,302,091	1,661,991	359,900	28%	1%
Use of Money and Property	5,108,250	6,141,623	1,033,373	20%	3%
Other Governmental Agencies	937,582	1,448,853	511,271	55%	1%
Fees and Charges for Service	13,181,206	13,989,555	808,349	6%	7%
Other Revenue	1,325,972	1,550,047	224,075	17%	1%
Operating Transfer In		-	-	100%	0%
Total	\$ 186,855,606	\$ 199,966,575	\$ 13,110,969	7%	100%

Graph 1 - General Fund Revenue Estimates by Category



Sales and Use Tax: Sales tax is the largest revenue category in Costa Mesa and is estimated at \$82.5 million for FY 2026-27, an increase of \$7.5 million, or a 10 percent increase from the FY 2025-26 Adopted Budget. The City continues to see growth in this category, despite the economic conditions that would typically dampen consumer spending.

Property Tax: All combined Property Tax revenues are estimated at \$64.0 million, reflecting a 2 percent growth over the prior fiscal year budget.

Transient Occupancy Tax (TOT): Transient Occupancy tax revenues are estimated at \$10.6 million next year, reflecting a 7 percent increase to FY 2026-27 Adopted Budget. The previously adopted revenue budget accounted for a potential slowdown in the travel and leisure segment of consumer

spending.

Fees and Charges: Fees and Charges are estimated at \$13.9 million, an increase of \$808,349, reflecting a 6 percent growth in FY 2026-27. In FY 2025-26, the City implemented credit card processing fee of 2.7 percent, which was previously paid by the City.

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 206-27 Proposed Budget includes an estimated \$3.7 million in cannabis taxes, an increase of \$49,086, or 1 percent from FY 2025-26. 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 the First Time Homebuyers Fund (140).

Business License Tax: Business License Tax was implemented over 40 years ago and the fees have not increased since its inception. The Business License Tax revenues are estimated at \$980,741 for FY 2026-27, a 4 percent increase from FY 2025-26.

FY 2026-27 General Fund Budget Expenditure Highlights

The Proposed General Fund Budget for FY 2026-27 reflects total expenditure of \$200 million. Of this amount, \$146.1 million is for salaries and benefits, which represents an increase of \$8.8 million, or 6 percent, from the FY 2025-26 adopted operating budget of \$137.4 million. The General Fund maintenance and operations and fixed assets budget will decrease to \$44.0 million from \$46.7 million. The decrease is due to the operating reduction requests from all departments to align expenditures with projected revenues. The remaining \$9.8 million represents the Transfers Out to the Information Technology Replacement Fund and Capital Asset Needs Fund as described earlier. The FY 2026-27 Proposed Budget for expenditures includes the following significant items:

- A \$3.1 million allocation to ensure compliance with the Information Technology Replacement Fund municipal code requirement of 1.5% of the General Fund revenue.
- A \$6.7 million allocation to ensure compliance with the Capital Asset Needs municipal code requirement of 5% of the General Fund revenue.
- A \$2.0 million increase in the annual required CalPERS UAL contribution.
- Adoption of a 2% vacancy factor.
- No use of General Fund Reserves to balance the General Fund.

Graph 2 - General Fund Total Appropriations by Department
Total Appropriations - General Fund - \$200.0 (includes Capital Improvement)
(in millions)

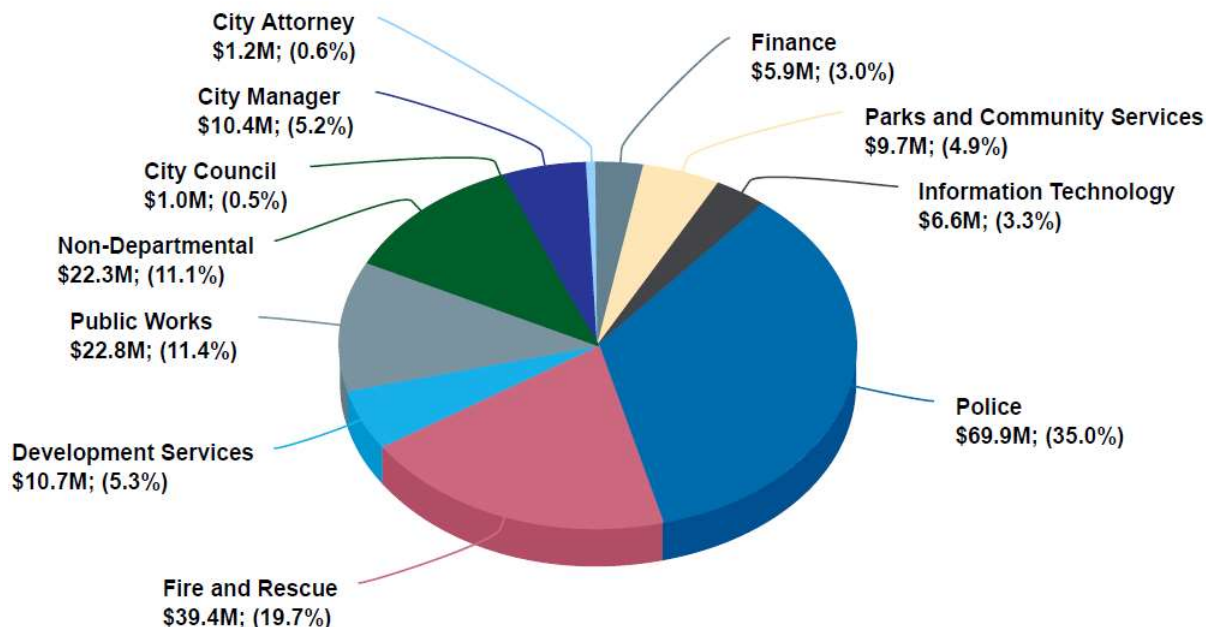


Table 3 - General Fund Budget by Department

Department	FY 2021-22 Actuals	FY 2022-23 Actual	FY 2023-24 Actual	FY 2024-25 Actual	FY 2025-26 Adopted	FY 2026-27 Proposed
City Council	\$ 867,909	\$ 834,337	\$ 750,577	\$ 797,518	\$ 954,143	\$ 968,834
City Manager*	6,505,480	7,573,363	8,902,755	9,900,304	9,613,230	10,430,048
City Attorney	958,775	988,108	977,061	1,107,716	1,123,700	1,157,411
Finance	3,811,155	4,271,188	4,416,583	5,057,429	6,296,502	5,933,378
Parks and Community Services	6,379,328	7,371,372	9,753,352	10,408,468	9,101,830	9,717,550
Information Technology	4,104,946	5,133,365	5,567,967	6,029,490	6,570,716	6,625,320
Police	53,504,411	55,874,470	62,005,909	66,702,742	62,820,471	69,922,839
Fire and Rescue	32,298,517	33,480,396	35,159,635	39,167,336	38,903,466	39,421,729
Economic & Development Services	7,522,770	8,229,755	9,082,786	9,571,371	9,695,734	10,651,781
Public Works	19,517,456	20,413,479	23,101,963	22,814,083	22,553,602	22,845,065
Non-Departmental	27,397,679	32,457,225	23,423,354	18,494,847	19,222,213	22,292,620
Total	\$ 162,868,426	\$ 176,627,058	\$ 183,141,942	\$ 190,051,304	\$ 186,855,607	\$ 199,966,575

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

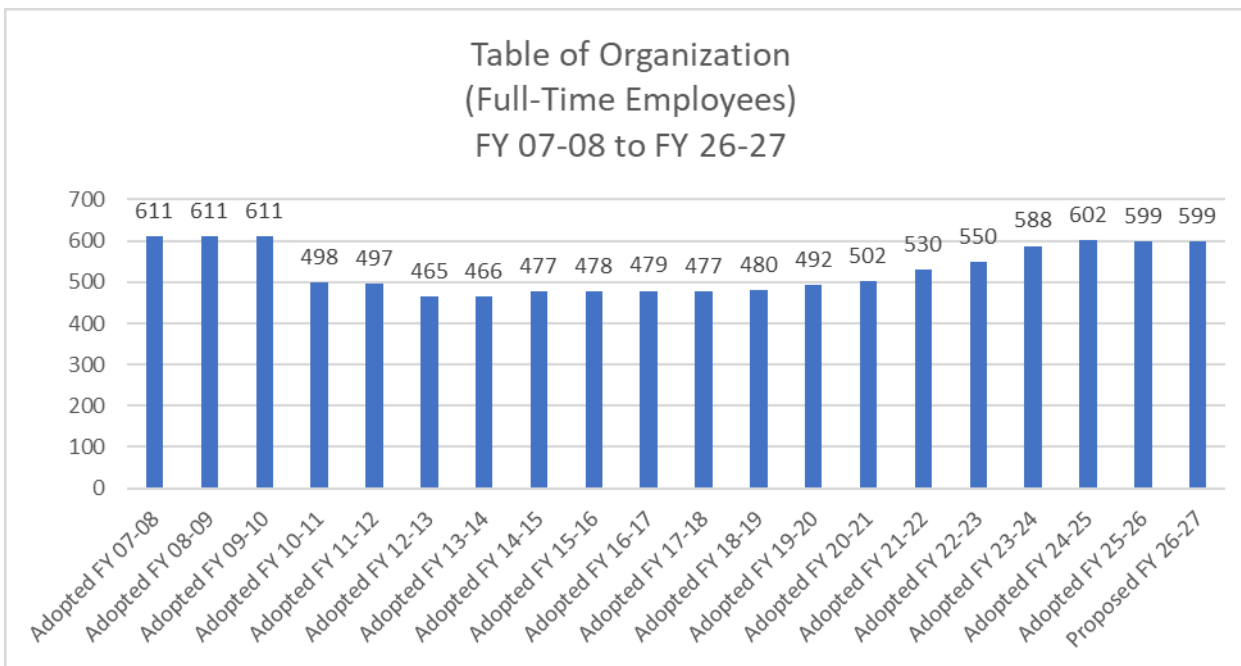
Commitment to the Arts and Culture

At the May 5, 2026, City Council meeting, the Arts Commission provided an update to City Council on the implementation of the five-year Cultural Arts Master Plan, and accomplishments to date, as well as next steps for developing the future five-year plan. As part of this discussion, the City Council provided direction to allocate funding for the City's arts and culture programs. The Fiscal Year 2026-27 Proposed Budget reflects the direction from the council.

Staffing Levels

As part of the City’s effort to ensure expenditure stays within the projected revenues, staffing levels were reviewed, and 13 vacant positions were identified and proposed to be frozen for the year. The FY 2026-27 Proposed Budget includes 599 full-time employees. On January 20, 2026, Council approved staff’s recommendation to utilize two part-time Concierge positions to convert to one full-time Office Specialist II position.

Table 4 - Budgeted Citywide Staffing Levels



The FY2026-27 Proposed Budget includes the reduction of 1.0 Park Ranger position in the Police Department. Also in the Police Department, is a reallocation of a Public Safety Dispatcher to a Public Safety Dispatch Supervisor to support training and operational needs.

The Development Services Department requests the reallocation of a Chief of Code Enforcement position to Senior Permit Technician to support building counter operations. The Department also intends to underfill an Assistant Planner position with a Planning Technician to provide needed support to the customer service counter.

The Proposed Budget will also include full funding for the Parks and Community Services Department Senior Center Community Outreach Worker.

Proposed Department Name Update

The Economic and Development Services Department is requesting a name change to “Community Development” to reflect their broader service base and purpose. This department performs a wide breadth of functions, manages all private-owned property in the City through the complete life cycle of the build environment. This includes reviewing new construction, managing land uses for new and

existing buildings, overseeing operational details, housing and community program assistance, ensuring property maintenance and code compliance, and finally, permitting demolition.

The name change to “Community Development” would reflect the broader service base and purpose that the department provides to the City of Costa Mesa.

Commitment to Public Safety

The FY 2026-27 Proposed Budget allocates \$109.3 million as the City’s commitment to public safety, comprising both the Police and Fire Departments. Public safety budgets account for approximately 55 percent of the General Fund Proposed Budget, with 35 percent allocated to the Police Department and 20 percent to the Fire and Rescue Department. Of the 599 citywide full-time personnel, approximately 38 percent are sworn positions.

The Police Department budget includes 142 full-time sworn personnel, with one new non-sworn Custody Officer in the proposed budget. Additionally, the Police Department manages the Animal Services and Enforcement Program. The Police Department’s salaries and benefits budget increased by a net of \$7.1 million, \$3.3 is attributed to labor contractual agreements and retirement benefits, \$122,000 in jail operations overtime, and \$3.7 million in the removal of the vacancy factor.

The Fire and Rescue Department consists of 86 full-time sworn personnel. Its salaries and benefits budget increased by a net of \$715,263, due to labor contractual agreements and retirement costs. The Department is requesting to reallocate a vacant Emergency Services Coordinator position to a Battalion Chief to address operational needs.

These are some of the proposed actions that demonstrate the City’s ongoing commitment to the public’s safety. The strong support of the City Council, along with the engagement of residents and community partners, continues to promote healthy, sustainable neighborhoods and balanced economic activity. Together, these efforts help maintain the high quality of services the City provides.

Finance and Pension Advisory Committee (FiPAC)

On May 7, 2026, Finance staff presented the FY 2026-27 Proposed Budget to FiPAC. The Committee commented on the proposed citywide vacancy factor and inquired about frozen positions and how they are accounted for in the vacancy factor. The Committee commented on whether additional funding was needed for the increasing cost of Utilities as the actual year-over-year expenditure has exceeded what has been budgeted in previous years. Further, the Committee inquired whether Police overtime has been budgeted to reflect actual historical costs. The Finance Department will return to FiPAC on May 13, 2026, for further discussion and recommendations to City Council.

ALTERNATIVES:

The City Council can provide alternative direction to staff on the FY 2026-27 Proposed Operating Budget.

FISCAL REVIEW:

Staff is requesting City Council provide feedback and direction in advance of final adoption of the FY 2026-27 Proposed Operating Budget. Staff will be bringing the FY 2026-27 Proposed Operating Budget forward to a Public Hearing on June 2, 2026, for additional feedback or final adoption. If needed, a second alternative final adoption date of Tuesday, June 16, 2026, is available.

LEGAL REVIEW:

The City Attorney's Office has reviewed and approved this report as to form.

CITY COUNCIL GOALS AND PRIORITIES:

This item supports the City Council goals:

- 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
- Advance Environmental Sustainability and Climate Resiliency
- Maintain and Enhance the City's Facilities, Technology and Equipment

CONCLUSION:

The overview of the Proposed Operating General Fund expenditure and revenue projections for FY 2026-27 was carefully evaluated with a cautious approach to any proposed increases. The FY 2026-27 Proposed Budget creates a solid foundation for "Measured Decision. Meaningful Impact."

Staff recommend that the City Council discuss and provide feedback on the FY 2026-27 Proposed balanced budget.