

BUDGET MESSAGE

FISCAL YEAR 2011-2012

July 1, 2011

Honorable Mayor and Members of the City Council:

INTRODUCTION

The Final FY 2011-2012 budget is the culmination of many hours of preparation. The City's Five-Year Financial Plan and Annual Budget documents are combined in one seamless document. We have done that by incorporating the City's Five-Year Financial Plan into the Financial and Personnel Summary section, as well as the individual department and non-department sections of this document.

The City's Five-Year Financial Plan is merely that – a five-year forecast of revenues and expenditures based upon the strategies and Policy Calendar adopted earlier this year. While the City Council will incorporate the Five-Year Financial Plan as part of this document, the City Council will only appropriate funds on an annual basis. Thus, the Annual Budget for FY 2011-2012 has been prepared.

The annual budget results in the actual appropriation of funds. Funding requests were carefully reviewed and considered prior to their inclusion in the recommended budget.

The budget is the primary policy document adopted by the City Council each year. It describes the City's goals and details how resources are allocated to achieve these goals. In addition, the budget serves as the annual financial plan, an operational guide and a communications tool.

ELEMENTS OF THE BUDGET

The budget document is organized as follows:

1. **Introductory Items**
 - Table of Contents
 - Mission Statement
 - City Government Organization Chart
 - Policy Calendar for 2011
2. **Budget Message:** Includes the letter of transmittal from the City Manager submitting the recommended budget to the City Council, major initiatives/issues, organizational changes addressed in the budget and the City's current and projected financial position.
3. **Budget Guide:** Includes a description of the annual budget process, a glossary of budget terminology and the structure of the City's finances.
4. **Five-Year Financial Plan:** Includes a City-wide look at expenditure and revenue trends affecting the City over the course of the next five years.
5. **Financial and Personnel Summaries:** Includes financial information on projected revenues, expenditures, fund balances and reserves, personnel resources, and a summary of funds as well as fund descriptions and information on all revenue sources and expenditure projections.
6. **Department Operating Budgets:** Operating department

sections include the departmental mission statement, personnel summaries, five-year strategic plan (including values, goals and objectives) of the organization, key initiatives completed, initiatives and service level expectations for FY 2011-2012, and changes in financial resources required to accomplish the department goals. The account summaries include the following five major categories of department appropriations:

Employee Services represents permanent full-time and part-time salary costs, overtime, holiday pay and fringe benefits.

Services and Supplies represents legal, consulting, and other professional services, contract repair and maintenance, utility charges, training and memberships, equipment rentals, insurance and employment services. This category also represents items purchased for repair and maintenance, operational activities such as publications, uniforms, recreation supplies and office supplies.

Internal Service Charges represents vehicle replacement charges, equipment replacement charges, self-insurance charges, information technology service charges, building maintenance charges, longevity recognition benefits funding, and PEMHCA benefits funding.

Capital Outlay represents expenditures for fixed assets in excess of \$1,000 including land, buildings, furniture, equipment, and City vehicles.

Reallocation represents reallocation of department operating expenses to non-General Fund budgets such as Special Revenue Funds and Enterprise Funds.

Behind the account summaries are the detailed line item expenditures.

7. **Non-Department Budgets:** Includes historical and proposed expenditures for non-department General Fund, special revenue, assessment district, enterprise and internal service fund budgets.
8. **Community Development Agency Budget:** Includes the personnel summaries, five-year strategic plan of the Agency, key initiatives completed, initiatives and service level expectations for FY 2011-2012, and changes in financial resources required to accomplish the Agency goals. This section also includes resource requirements by funds, revenue report, and Agency account summaries and detailed line item expenditures for each fund.
9. **Capital Improvements:** Includes various tables showing the proposed capital projects for the upcoming fiscal year and for a five-year period, along with detailed descriptions of capital improvement projects.

FINANCIAL OVERVIEW

The City/District/Community Development Agency funds are all in sound financial condition and will have reserves at the beginning and the end of the fiscal year that meet or exceed the Council defined minimum reserve levels. However, the City's five-year financial forecast shows that General Fund expenditures and transfers will exceed revenues in FY 2011-2012 by approximately \$2.5 million, and that a structural deficit of approximately \$2.8 million exists unless further adjustments (expenditure reductions and/or revenue enhancements) are implemented. The Community Development Agency Project Area One hit its \$170 million revenue cap in FY 2010-2011 and stopped receiving tax increment revenues. Consequently, the District is expected to see an increase in property tax revenues

of \$4.1 million in FY 2011-2012 and thereafter. The City has stopped direct allocation of personnel to the Community Development Agency, which has increased the expenditures in the General Fund.

Based on City Council direction, the General Fund minimum reserve level has been established at 33.3% of annual operating expenditures. The five-year forecast shows the City being able to stay above this reserve level in each of the successive 5 years through the implementation of an action plan to make the necessary balanced budget adjustments.

Key elements of the City's financial overview are summarized as follows:

- General Fund Reserves – An ongoing structural deficit of \$2.8 million, if not addressed by FY 2013-2014, would find General Fund reserves at the end of FY 2015-2016 at \$6.5 million, which is 19% of annual operating expenditures, or \$4.7 million under the minimum reserve threshold. The five-year analysis indicates that the City will need to make around \$2.8 million in a combination of ongoing expenditure reductions and/or ongoing revenue enhancements by FY 2013-2014, in order to balance the budget and maintain reserve levels above the 33.3% minimum.
- CDA Reallocations – As Project Area One has reached its tax increment cap, the City has determined to cease further personnel reallocations to the CDA. Nominal charges of less than \$5,000 are levied on the remaining two project areas in recognition of the administrative oversight provided by City personnel to those remaining project areas. In addition, nearly \$60,000 in charges are levied by the General Fund on the Foster City Affordable Housing Reimbursement Agreement funds in accordance with the provisions of that agreement. Prior year reallocations from

the City's General Fund to the CDA totaled \$804,000.

- Bargaining Units – Employees represented by the American Federation of State, County and Municipal Employees Local 829 (AFSCME) and employees covered by the terms of the Management Employees Compensation and Benefits Plan are in multi-year agreements that expire June 30, 2013. The Memoranda of Understanding with the Foster City Police Officers Association (FCPOA) and the International Association of Firefighters Local 2400 (IAFF) are one year agreements that expire June 30, 2012.
- Pension Costs – Employer contribution rates to the CalPERS pension plans for Miscellaneous and Public Safety plans are expected to be 16.642% and 28.437%, respectively. The Public Safety contributions have been reduced by 9.6% as a result of CalPERS' approval of the City's request to reamortize the side fund obligation over 30 years.
- Long-Term Capital Improvements Funding – The City's General Fund continues to transfer funds to the City Capital Investment Fund totaling \$1,342,000 to fund long-term capital improvement projects.
- Water and Wastewater Rates – Water revenue requirements will increase by 11% for FY 2011-2012 by maintaining fixed meter charges at current rates and requiring a 27% increase in the base consumption rate based upon a 38% increase in wholesale water rates charged by the San Francisco Public Utilities Commission. Wastewater rates will remain unchanged for FY 2011-2012.
- State Budget Assumptions – The Governor's May 2011 Revised Proposed Budget has formed the basis for the assumptions used in the City's budget. Income tax, sales tax, and vehicle license fees increases will lapse on June

30, 2011. The Legislature approved a budget on June 15, 2011 that was sent to the Governor, however the Governor vetoed the entire budget package on June 16, 2011 on the basis that the budget did not provide the long-term adjustments necessary to solve the State's ongoing budget deficit. The Governor's proposed tax extensions are still being met with opposition by Republican legislators. Unless a deal is worked out, it is likely that the referendum process will be used in an attempt to get those tax increases on the ballot in November 2011. Based upon the current budget proposals, SLESF/COPS grant funding is assumed to be eliminated, which previously provided \$100,000 per year to fund one partial Police Officer position and will negatively impact the General Fund by \$100,000. There are no assumptions relative to the Legislature's proposed elimination of redevelopment agencies incorporated into the budget as the bills that were approved have not been forwarded to the Governor for signature and face significant constitutional challenges.

HIGHLIGHTS FOR 2011-2012

As the nation, state, and region emerge from one of the worst economic recessions since the 1920's, recovery has been slow at best. With national unemployment at 9.1%, and California's unemployment rate at 11.9%, most economists believe that there will not be any significant economic recovery unless national unemployment falls below 7%, and California's unemployment falls below 8%. As we approach the start of a new fiscal year, the economy is showing renewed signs of stagnation. It is very likely that economic growth will remain below 2% for at least the next 4-5 years.

The State of California's fiscal status continues to be bleak. The State continues to wrestle with a structural deficit estimated at \$25.4 billion. The Legislature approved \$12 billion

in expenditure cuts for FY 2011-2012, yet legislators are at a stalemate on how to resolve the rest of the deficit (tax increases versus deeper spending cuts). The Governor has proposed the elimination of redevelopment agencies, and has proposed a ballot measure for the extension of various taxes that lapse on June 30, 2011. However, he has yet to garner the number of votes in the Legislature necessary to approve those initiatives.

The housing market in Foster City has softened in the past six months, with median housing prices falling by just over 1% from the prior year. The County Assessor's Office currently estimates assessed valuation growth of 2.12% for FY 2011-2012, yet there remains nearly \$616 million in assessed valuation at risk of reduction based on assessment appeals filed mainly by commercial property owners.

Sales tax revenues are expected to see modest growth of not more than 2% over the next several years, although local sales tax collections have increased over the past 6-9 months. Transient occupancy taxes have increased by 10% in the past year. Investment income remains at less than 1.5% yield with the lowest Treasury yields in well over 20 years.

The City has positioned itself well to weather this economic crisis, but will require prudent fiscal decisions over the coming years to meet the Council-adopted minimum General Fund reserves of at least 33.3% of annual budgeted operating expenditures. The General Fund starts FY 2011-2012 with a projected \$19.4 million in unrestricted reserves, nearly 63% of its annual operating expenditures. The City's General Fund will see an infusion of over \$4 million in property taxes that were formerly flowing directly to the Community Development Agency as a result of the Project Area One reaching its tax increment cap.

Significant development revenues are anticipated based upon

the agreements and approved project developments for the Pilgrim-Triton and Gilead Sciences Campus projects. However, development of the City-owned 15-acre site adjacent to City Hall has not occurred due to the current economic climate and the limited availability of financing for a project of this size. Therefore, no revenues that could be generated from this site are included in the five-year forecast. It should be noted that the City is currently marketing the site and, depending on the outcome of those efforts, it is possible for the City to realize revenues from this asset in the next five years.

The City has made approximately \$2 million in expenditure reductions and \$150,000 in revenue enhancements as part of the FY 2011-2012 proposed General Fund budget, yet still faces an ongoing structural deficit by FY 2013-2014 of nearly \$2.8 million per year. The City Council has established the goals of balancing the General Fund budget without the use of reserves by FY 2013-2014 and of maintaining reserves above the minimum level of 33.3% of annual budgeted operating expenditures. A detailed action plan to achieve these Council goals will need to be reviewed with a newly seated City Council starting in January 2012. Both expenditure reductions and revenue enhancements will be explored along with their associated service level impacts. The action plan will need to be reviewed with input from the community and from the employees and the labor groups who represent them. As an example of how to achieve these two goals, the five-year forecast shows ongoing budget adjustments of \$1.4 million per year in FY 2012-2013 and FY 2013-2014.

The proposed annual budget for FY 2011-2012 shows a net increase in General Fund expenditures of merely \$17,000 from the previous fiscal year. Significant changes in the FY 2011-2012 budget are presented in the following areas:

Community Development Agency

- Personnel reallocations from the City to the CDA have ceased given Project Area One reaching its tax increment cap
- Implementation of three agreements between the City and the Agency calling on the City to act on behalf of the Agency: 1) Public Improvements Reimbursement Agreement to construct various public improvements; 2) Affordable Housing Reimbursement Agreement to continue the affordable housing initiatives of the low- to moderate-income funds generated by the Agency; and, 3) Cooperative Services Agreement to allow the City to repay the Agency's obligation to the San Mateo Union High School District through FY 2015-2016

Community Development Department

- Elimination of one (1) Office Assistant II position, with duties reassigned primarily between the Building Permit Technician and the Management Assistant within the department

Fire Department

- Continued implementation of the Fire Command Shared Services Model with the City of San Mateo, including a 1/3 split of the Fire Chief position, the addition of a full-time Deputy Fire Chief, and the 1/3 split of one Battalion Chief position
- Increase of \$130,000 in training costs through the combining of training resources through the Central San Mateo County Training Division

Parks & Recreation Department

- Elimination of one (1) Parks Maintenance Worker II, utilizing the services of contractors and one part-time position and the successful implementation of synthetic

turf projects at Sea Cloud Park (S-3) and Port Royal Park

- Elimination of one (1) Recreation Coordinator as of December 31, 2011, reassigning duties amongst the remaining Recreation Coordinators, exploration of regionalized and shared services models for Adult Sports programs, outsourcing Youth Sports programs through contractors, and the reduction of other minor recreational programs
- Increase of \$101,000 in water charges as a result of the District's increased water consumption rates (see below)
- Increase of \$60,000 in diesel and gasoline fuel costs in the Vehicle Maintenance Internal Service Fund

Police Department

- Elimination of one (1) Police Corporal and two (2) Police Officer positions, realigning services within the Detective Bureau and the Patrol Division
- Elimination of one (1) Sr. Community Services Officer through a realignment of duties amongst the remaining Sr. CSO's
- Elimination of one (1) Police Records Specialist, reassigning duties amongst the remaining Police Records Specialists

Public Works

- Elimination of one (1) Senior Civil Engineer position in light of reduced engineering activities in the Engineering Division and reassignment and prioritization of engineering activities amongst the remaining Engineers

- Elimination of one (1) Public Works Superintendent position through the reallocation and streamlining of managerial functions in the Lagoons / Streets, Water and Wastewater Divisions
- Elimination of one (1) Public Works Maintenance Worker I/II position through reallocation and prioritization of workloads within the Lagoons / Streets Division

Support Departments (City Manager, City Clerk, Financial Services and Human Resources)

- Elimination of one (1) Office Assistant II position serving the Reception desk
- Elimination of one (1) Video Producer position, reducing FCTV service levels to include only productions of live City Council and Planning Commission meetings
- Elimination of one (1) part-time Clerical Assistant with duties reassigned to the remaining two (2) Clerical Assistants.
- Elimination of one (1) Transportation Intern, with reduced ongoing duties relative to transportation management reassigned to the Management Analyst.
- Reductions in replacement costs, extended useful lives, and technology changes that reduce total Information Technology internal service charges by \$232,000 in the Information Technology Internal Services Fund
- Use of excess reserves to reduce the Self-Insurance Internal Service Fund charges by \$150,000

Water Enterprise Operations

- The SFPUC is increasing its wholesale water rate by 38%, from \$1.90 / ccf to \$2.63 / ccf, with the potential to

increase it to \$2.72 / ccf in January 2012 depending upon water consumption patterns across the BAWSCA service area. These costs will be recovered through an increase in the base consumption rate that the District charges its customers to \$2.66 / ccf

- Expanded rebate programs will continue to be provided to customers in an effort to reduce water consumption by 20% by the year 2020
- Continued implementation of the radio read meter program for all water meters

Wastewater Enterprise Operations

- Reduction of \$200,000 in anticipated operational costs of the San Mateo Wastewater Treatment Plan, allowing the District to maintain its wastewater charges at current levels without the need for any increases

Shuttle Enterprise Operations

- Continued operation of the Blue and Red Lines with a fee of \$1 per ride or \$25 per month implemented for FY 2011-2012. Net of funding provided by C/CAG and San Mateo County Transportation Authority grants, the subsidy of \$99,000 for Shuttle operations will be provided from Measure M funds.

ORGANIZATIONAL CHANGES

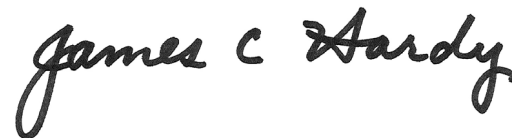
Based upon the organizational changes discussed in the preceding section, staffing levels as we enter FY 2011-2012 will be reduced by 12.5 full-time equivalents (FTE) from a total of 204 to a total of 191.5 FTE. This represents a 7% reduction from the FY 2010-2011 staffing level and a 10% reduction from the FY 2009-2010 staffing level of 213 FTE.

CONCLUSION

The City of Foster City, Estero Municipal Improvement District and Community Development Agency have been well managed and are in sound financial condition. This has served the City well in striving to maintain the highest service levels possible during these tough economic times. The City will need to exercise vigilance in its approach to the future beyond FY 2011-2012, and develop over the next several months a detailed action plan to address the structural budget deficit by FY 2013-2014. It is important to note that this City has a long history of being fiscally conservative, the result of wise policy decisions by current and former City Councils and excellent and talented staff that have committed themselves to the City's Mission and Values Statement to serving the community to the best of its ability.

On behalf of all the City employees, we look forward to providing the service levels funded in the Final Budget for FY 2011-2012.

Sincerely,



James C. Hardy
City/District Manager

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