

# BUDGET MESSAGE

## FISCAL YEAR 2010-2011

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**May 10, 2010**

Honorable Mayor and Members of the City Council:

### INTRODUCTION

The Preliminary FY 2010-2011 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 2010-2011 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 2010
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 2010-2011, 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, Enterprise Funds and the Community Development Agency.

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 2010-2011, and changes in financial resources required to accomplish the Agency goals. This section also includes resource requirements by funds, revenue report, Agency funded capital improvement program, 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.

#### HIGHLIGHTS FOR 2010-2011

The nation, state, and region are in the midst of an economic recession the likes of which have not been seen since the 1920's. Economists remain mixed as to whether or not we are at the early stages of recovery, with key indicators such as production indices and housing prices showing modest gains through the end of FY 2009-2010. Nevertheless, national unemployment is over 10%, and California's unemployment rate remains over 12%. Many economists believe that until unemployment rates fall below 9%, there will not be any significant economic recovery. It is very likely that we are still 12-18 months from seeing the bottom of this economic downturn, with modest economic growth thereafter.

The State of California's fiscal status continues to be bleak. The State has declared a fiscal emergency, has already made over \$60 billion in cuts to cure its deficits the past two years, and faces another \$20 billion deficit through FY 2010-2011.

The housing market in Foster City has stopped its decline, with median home prices staying relatively steady the past 6-12 months. Nevertheless, because statewide CPI was a negative 0.237% in 2009, and because home sales have not seen significant growth in price or volume, the County Tax Assessor's Office anticipates assessed valuation levels for the City will grow at only 0.8% in FY 2010-2011, which is 1.2% below the Proposition 13 cap of 2% and over 3% below the historical average growth of 4% per year. While property tax collections appear to be meeting predicted revenues in FY 2009-2010, property tax growth will be lower than previously forecasted.

Sales tax revenues are expected to remain at the same levels of FY 2009-2010 collections, which dropped 20% from the previous year. Transient occupancy taxes, however, fell nearly 25% from previous levels in FY 2009-2010, which lowers future projections. Investment income has fallen dramatically given 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 2010-2011 with a projected \$20 million in unrestricted reserves, nearly 68% of its annual operating expenditures. In FY 2010-2011, the City's General Fund will see the final paydown of the Community Development Agency's loan owed to the City, and tax increment revenue previously flowing to the Agency will once again begin to flow to the City/District when the Agency

reaches its tax increment cap. Significant development revenues are also anticipated based upon the agreements and approved project developments for the Pilgrim-Triton and Gilead Sciences Campus projects. However, development of the 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 are included in the five-year forecast.

The City faces an ongoing structural deficit by FY 2013-2014 of nearly \$1.9 million per year given the projected cost to maintain the current level of services and the lower projected revenues. 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 be developed by January 2011. Both expenditure reductions and revenue enhancements will be explored along with their associated service level impacts. The action plan will need to be developed 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 balanced budget adjustments of \$500,000 in FY 2011-2012, \$500,000 in FY 2012-2013, and \$875,000 in FY 2013-2014.

The proposed annual budget for FY 2010-2011 reduces General Fund expenditures by over \$500,000 from the previous fiscal year. These reductions were accomplished predominantly through two factors: 1) certain positions (e.g., Administrative Services Director and Executive Assistant to the City Manager) were eliminated, and others (e.g., Parks Maintenance Workers) were left vacant, unfilled and not budgeted for FY 2010-2011, as the City evaluates its service levels and the corresponding personnel requirements to

provide those services; and, 2) the reamortization of the unfunded actuarial liability related to Public Safety retirement costs.

There are a number of initiatives outlined in each departmental budget, highlights of which are provided here:

- Process the provisions of the developer agreements and planning / building permits for the proposed redevelopment of the commercial space in the Pilgrim / Triton area and the Gilead Sciences Campus.
- Commence construction of various roadway improvements, including residential street resurfacing and implementation of select Multi-Project Roadway Improvements as a result of development in the Pilgrim-Triton and Gilead Sciences project areas.
- Commence Phase II construction of the Levee Pedway Improvements project that will repair deficiencies and keep the pedway in good condition.
- Update the City's General Plan.
- Continued implementation of the action plan developed by the Ad Hoc Environmental Sustainability Committee in an effort to create a more environmentally sustainable community.
- Continued implementation of the action plan developed by the Ad Hoc Transportation Committee in an effort to create a comprehensive transportation system for Foster City.
- Implement conservation-based tiered water rates, online utility billing and monthly utility billing cycles, all in an effort to incent water conservation and manage water usage within the water supply allocation from the City and County of San Francisco.
- Continue discussions with the San Mateo-Foster City School District to address school overcrowding issues.
- Maintain an emphasis on emergency planning and

preparedness for the City, for the residents and for the business community.

### ORGANIZATIONAL CHANGES

The City previously reduced its budgeted full-time employees by 10% (from 237 FTE in FY 2001-2002 to 213 FTE in FY 2009-2010). Staffing levels as we enter FY 2010-2011 will be reduced by 7 FTE to a total of 206 FTE, accomplished through the elimination of certain positions and leaving other positions vacant, unfilled and unfunded pending an evaluation of service levels and personnel requirements to provide those services.

### 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 will exceed revenues in FY 2010-2011, and will continue as such throughout the five-year forecast if no balanced budget adjustments (expenditure reductions and/or revenue enhancements) are implemented. The Community Development Agency Project Area One will hit its \$170 million revenue cap in FY 2010-2011 and stop receiving tax increment revenues. However, the State is expected to take \$5.6 million from the Agency by the end of FY 2009-2010, which will delay reaching the cap and, as a result, delay the infusion of annual property tax revenues directly to the District. Accordingly, the District is expected to see an increase in property tax revenues of \$2.8 million in FY 2010-2011 and then an estimated \$4.8 million in FY 2011-2012 and thereafter.

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.

I would like to highlight a few of the significant items in the proposed FY 2010-2011 Annual Budget.

- The City will have sufficient reserves to maintain existing service levels enjoyed by the community in this budget. The proposed FY 2010-2011 General Fund budget indicates a deficit of \$2.4 million on a budget basis, and that reserve levels will finish the year at \$17.6 million, or 56% of annual operating expenditures. However, there will exist a structural deficit in an amount of ~ \$2.6 million through FY 2012-2013, and ~ \$1.9 million by FY 2013-2014 and beyond. If this structural deficit is not addressed, General Fund reserves would end FY 2014-2015 at \$8.8 million, which is 26% of annual operating expenditures, or \$2.6 million under the minimum reserve threshold. The five-year analysis indicates that the City will need to make around \$1.9 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.
- All employee groups are in multi-year agreements as we start FY 2010-2011. Management employees and those employees represented by the American Federation of State County and Municipal Employees (AFSCME) will be in the first year of three-year agreements. Employees represented by the International Association of Firefighters (IAFF) and the Foster City Police Officers' Association (FCPOA) will be in the last year of two-year agreements.
- Retirement contributions to the PERS retirement system for Miscellaneous Employees will increase by 1.1% in FY

2010-2011, while Public Safety retirement contributions will decrease by approximately 8% due to the reamortization of the unfunded accrued liability over 30 years.

- Water revenues are planned to be increased overall by 9% in FY 2010-2011 based upon a 10-year Rate Smoothing model adopted by the District Board in FY 2006-2007 and the funding of long-term capital improvements using a 10-year forecast. The rate-smoothing model was implemented to mitigate the impact of significant increases in water rates charged to EMID by the SFPUC resulting from the costs of significant capital improvements on the Hetch Hetchy System that supplies water to Foster City and much of the Peninsula. Conservation-based water rates in the form of tiered rates for single-family and multi-family residential customers, and a water budget based rate for irrigation customers, will be implemented for FY 2010-2011, with any excess revenues going to fund expanded rebate programs and conservation initiatives in a newly created Water Sustainability Fund.
- Wastewater rates are planned to be increased by 5% in FY 2010-2011 based upon a 10-year Rate Smoothing model adopted by the District Board in FY 2010-2011, which will smooth rates by no more than 5% increases through FY 2013-2014. Rate increases are based upon the capital improvement projects planned for FY 2010-2011 and 2011-2012, and the funding of long-term capital improvements using a 10-year forecast.
- The Final Budget has been prepared based on the Governor's proposed budget for FY 2010-2011. The State has closed its budget deficit in part through the takeaway of redevelopment agency funds. For Foster City, the State is expected to take \$5.6 million from the CDA in FY 2009-2010, and an additional \$1.275 million in FY 2010-2011. No

further local agency takeaways are currently in the budget proposal, but this will require close watch on the potential impacts to the City / District / Agency as the State addresses its shortfall.

- There is a 3% increase in the proposed Master Fee Schedule to reflect the increased cost of providing services.
- Funding for the Foster City Connections Shuttle for FY 2010-2011 in the amount of \$328,200 has been included based upon the assumed continued receipt of a 50% matching grant from the City/County Association of Governments (CCAG) under the "Local Transportation Services" component of the Countywide Congestion Relief Plan. The General Fund subsidy is expected to be \$164,100.
- We reviewed carefully all budget requests prior to their inclusion in the budget. The intent of this budget is to maintain the level of services currently being provided to the community.

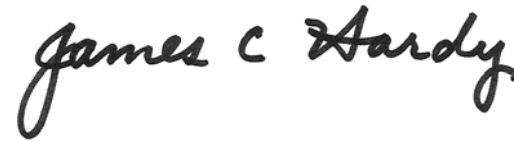
#### CONCLUSION

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 being able to maintain existing service levels to the fullest extent possible during these tough economic times. The City will need to exercise vigilance in its approach to the future beyond FY 2010-2011, 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 discussing with the City Council the Five-Year Financial Plan and the Preliminary Budget for FY 2010-2011.

Sincerely,

A handwritten signature in black ink that reads "James C. Hardy". The signature is written in a cursive, flowing style.

James C. Hardy  
City/District Manager