The past year has been one of the most fiscally complex years facing not only the City of Manteca, but the Nation and the State. Together we have faced a severe national recession that many have equated with the Great Depression. In the City of Manteca, we have faced unemployment levels nearing 20% and have been located in the epicenter of the mortgage crisis. When the City Council met with staff for an in-depth workshop in January 2009, the breadth of the fiscal challenges facing the City over the next five years was daunting. At that time, pro-forma projections for the General Fund calculated an estimated shortfall of $11.3 million in Fiscal Year 2009-10, growing to $14.2 million in Fiscal Year 2010-11.

Following the January workshop, Council formed a citizen's Budget Advisory Committee (BAC). On April 7, 2009, the BAC presented its findings to Council. The recommendations included freezing current vacant positions, approving suggested staff reorganizations, supporting staff maintenance of the Landscape Maintenance Districts, update of development fees, creation of a separate fund for Development Services, and to open up negotiations with all employee unions. The BAC also expressed strong opposition to the addition of any new revenue increases, such as a Utility Users's Tax. Each of these suggestions was implemented beginning with the Fiscal Year 2009-10 budget.

Working as a team, the City Council, management, and City employees joined together to execute salary and benefit strategies that would address the General Fund shortfalls through the end of Fiscal Year 2010-11. By putting into action the recommendations of the BAC and implementing negotiated employee salary and benefit packages, the City has reduced the projected General Fund shortfalls to an estimated $4.0 million for Fiscal Year 2009-10 and $3.4 million for Fiscal Year 2010-11. The Fiscal Year 2009-10 budget included the re-designation of reserves set aside for the over-sizing of infrastructure to general operating reserves. This action, combined with the use of existing operating reserves, will allow the City to bridge the General Fund gap through June 30, 2011 without the need for additional transfers of funds.

During the next 12 months, staff will closely monitor current economic conditions and proposed actions by the State to balance its own projected $19.1 billion deficit and any impact on the City's finances. Strategies will continue to be developed to further reduce the General Fund shortfall and to ensure fiscal stability in all funds.

Economic Conditions

Just as the Nation is beginning to show signs of recovery from one our most-severe national recessions, the prognosis for the City of Manteca's economy is beginning to improve. While cities in our region and throughout the State have continued to experience double-digit declines in sales tax, the expansion of the City's economic base including Costco, Bass Pro Shops, Best Buy, JC Penney and JM Equipment Company have resulted in a less-than-3% decline in the sales tax in our community during the past year. For the next 12 months, sales tax is projected to remain stable; however, we will closely monitor consumer spending trends in areas as such as car sales and construction to quickly identify any further deterioration in these economic sectors. Sales tax comprises 29% of General Fund revenues. This is second only to property tax, which makes up 38% of General Fund revenues.

Management staff has been in discussion with the County Assessor's Office regarding projected property assessments for Fiscal Year 2010-11. At this time, it is projected that residential property tax will remain flat with no further declines. However, commercial property tax is projected to decline by up to 15%. The majority of commercial property within the City is located in Redevelopment areas. The decline in commercial property tax should not impact the General Fund, but has been included in revenue projections for the Redevelopment Agency.

Project Budget, Capital Improvement Program, Budget and Fiscal Policies

In an effort to provide in-depth information regarding City operations, programs, activities and projects, the preliminary budget has been revised from a line-item budget to a project-based budget. Information regarding the proposed budget, use of requested funding, accomplishments and objectives have been provided for each operation and program throughout the City. Additionally, staff is moving toward performance-based management. During the first phase of implementation, performance measures have been developed for public safety, public works and risk management. Throughout the next year, staff will continue to develop and refine performance measures for all City operations. Through the employment of performance-based management, staff will be better able to assess the effectiveness of funded programs and to improve operational efficiencies.

The Fiscal Year 2010-11 Preliminary Budget also marks the first year that the City Council will be asked to approve a formalized Capital Improvement Program (CIP). The CIP represents staff's proposal for infrastructure and equipment needs for the next five years; however, Council is being asked to only approve funding for the upcoming fiscal year. All capital equipment requests and non-public-work capital projects in excess of $25,000 are included in the CIP. All public work capital improvement projects in excess of $100,000 are included in the CIP. All requests falling below these thresholds are included in the operating budget for approval.

The project-based budget, performance measures and development of a CIP encapsulate staff's goal to provide a greater level of awareness and information regarding the City's plan of action for the next fiscal year.

Budget policies have been revised and expanded in order to support the transition to a project-based budget. Additionally, policies and procedures regarding the CIP have been developed. Both sets of policies have been included in the budget document for approval and implementation beginning July 1, 2010.

Budget Overview and Highlights

The General Fund proposed budget for Fiscal Year 2010-11 is $29,717,753. This represents a 9.7% decrease over the adjusted budget of $32,921,524 for Fiscal Year 2009-10. The Citywide proposed budget, excluding the Redevelopment Agency, is $103,367,171. This includes new funding requests for capital improvement projects totaling $20,150,200.

The Redevelopment Agency proposed budget is $14,093,795, compared to the 2009-10 adopted budget of $26,019,235. A total of $5,834,110 in capital funding has been included in the CIP for carryover to complete projects that were included in the 2009-10 budget and will be continued in 2010-11. These projects include improvements to Library Park, the South Union Road/ Highway120 interchange project, the South Union Road Atherton project and the Milo Candini storm water basin project. Additionally, $1 million has been included for low/moderate-income projects, including down payment assistance and the senior rehabilitation housing program.

General Fund

The General Fund budget as presented projects an operating structural deficit of $3.6 million, compared to a projected $4.0 structural deficit for Fiscal Year 2009-10. Prior to implementing reduction strategies, the deficit for Fiscal Year 2010-11 was originally projected at $14.2 million. Reductions to the budget imbalance have been achieved through several measures, including:

1. In September 2009, Council again authorized management to offer two years additional PERS service credit for employees retiring by March 31, 2010. A total of 20 employees participated in this program. This was in addition to the 14 employees who participated in this program in January 2009.
2. A total of 57 vacant positions were frozen during Fiscal Year 2009-10 and will continue to remain unfilled.
3. A furlough program was instituted for all employees. This program will continue for all non-public safety employees through June 30, 2011.

4. The Parks Division assumed maintenance of all Landscape Maintenance Districts (LMDs). The team of 4 employees will continue to maintain the LMD's for additional General Fund savings.
5. Operational expenses for travel, training and supplies were again maintained at prior-year levels.
6. A Development Services Fund was established in 2009-10. The fund was established with a $1.7 million loan from the Redevelopment Agency in anticipation of adoption of revised development services-related fees. Through-out the past year, staff has been working with the residential development community regarding recommended fee structures. Staff will be including the updated fee schedule for adoption with the budget on July 6, 2010. Due to the delay in implementation of the revised fees, staff is requesting an additional $550,000 loan from the Redevelopment Agency to the Development Services Fund in order to phase in the new fee structure. The creation of the Development Services Fund allowed the revenues and expenditures for Community Development and Building Safety to be transferred from the General Fund to a Special Revenue Fund.
7. The use of the Information Technology Internal Service Fund was expanded in 2009-10 to include all capital and maintenance expenditures associated with providing technology to the City and its employees. This has been further expanded in 2010-11 to include all personnel costs. The full implementation of the Internal Service Fund allows for 100% cost recovery for all impacted funds, including the General Fund and Enterprise Funds.
8. Five of the City's six bargaining units negotiated revised salary and benefit packages, which included elimination of cost-of-living adjustments through December 31, 2011, elimination or reduction of deferred compensation, and additional employee contributions to the California Public Employees' Retirement System (PERS). Without the cooperation and support of our employees, the reduction to the City's structural deficit would not have been attained.

<u>Public Safety Sales Tax Fund</u>

In November 2006, the citizens of Manteca passed a one-half-cent sales tax for public safety. As part of the adoption of this sales tax measure, a Citizen's Oversight Committee was formed to ensure that all expenditures meet the guidelines as set forth in the adopted ordinance. When originally adopted, the five-year expenditure plan projected sales tax revenues of $4.6 million for Fiscal Year 2010-11. Due to declines in consumer spending, sales tax projections for the upcoming year are $3.6 million. In response to declining revenues, a revised staffing plan was approved in Fiscal Year 2009-10. As currently adopted, the Public Safety Sales Tax Fund provides funding for 11

Police protection personnel and 12 Fire protection personnel. No changes to staffing levels are projected over the next 12 month period in order to ensure the long-term fiscal stability of this fund. Staff will meet during the next year to provide an updated expenditure plan for review by the Citizen's Oversight Committee and approval by the City Council.

Golf Course Fund

The Golf Course faces the same challenges of decreased consumer disposable income that is impacting the General Fund. During the past five years, overall revenues have declined but appear to be stabilzing. The revenues continue to fall short of meeting five-year projections, and the fund continues to experience negative cash flow. The General Fund subsidizes the operations of the Golf Fund in three specific ways:

1. General administrative and overhead charges were suspended beginning in Fiscal Year 2007-08. This recommendation is continued for Fiscal Year 2010-11.
2. On average, $140,000 is loaned to the Golf Fund annually to meet cash flow obligations. The total cumulative amount due to the General Fund as of June 30, 2009 is $1.3 million.
3. In the past, the City Council has approved a contribution from the General Fund equal to the recreational benefit the Golf Course provides to the citizens of Manteca. The 2010-11 preliminary budget includes a poposed contribution of $155,000.

One of the primary challenges to achieving fiscal stability in the Golf Course Fund has been ongoing debt service related to the clubhouse. In prior years, the debt service represented 22% of all expenditures. As of June 30, 2010, the $2.2 million lease associated with the clubhouse expansion will be fully defeased. The remaining debt service payment to the expansion of the golf couse and construction the parking lot and tennis courts will be paid off in 2013.

With the retirement of the 1994 Capital Lease, debt service now comprises only 4.4% of all expenditures. Golf course revenues are anticipated to meet all operating expenditures, exclusive of major capital, beginning July 1, 2010.

In July 2009, the City Council approved an agreement with Economic Research Associates to perform and evaluation of the golf course operations. On February 16, 2010, Council was presented with the findings from the evaluation and directed staff to negotiate amendments to the professional services contract between the City and Alan Thomas. Administration has continued to meet with Mr. Thomas and anticipates bringing forward contract amendments in late July.

Areas of Consideration/Future Concerns

As a result of the collaborative efforts of Council, administration and employee bargaining units to control operating and personnel expenditures, the prognosis for the fiscal stability of the City is improving. Full recovery will be dependent on the City's ability to continue to contain expenditures, meet service level requirements and broaden our revenue base.

Complicating the City's ability to fully plan for the future are unknown impacts from the State. In August 2009, the State suspended Proposition 1A, and the City of Manteca was required to transfer nearly $1 million in property tax revenues back to the State in the form of a loan to be repaid in two years. With Council approval, staff securitized the loan via the California Communities Prop 1A Securitization Program and was able to avoid immediate cash shortfalls.

Additionally, in August 2009, the State required the transfer of a total of $8 million in property tax revenues from the Redevelopment Agency. The California Redevelopment Association (CRA) challenged the edict to transfer funds to the State. On May 4, 2010, the Sacramento Superior Court found that the $2.05 billion State take of Redevelopment funds did not violate the California Constitution. The CRA is pursuing an appeal of the adverse decision. As a result, on May 10, the Agency was required to forward $6.7 million to the State. The remaining $1.3 million has been programmed in the 2010-11 budget. Concern continues that with the Court decision, the State has been given carte blanche access to Redevelopment funds.

In March 2010 as part of a special study session called by the Governor, the Legislature passed ABx8 6 and ABx8 9, which contain provisions for a swap of sales taxes on gasoline for a gasoline excise tax. The new law goes into effect on July 1, 2010. The new law included expressed legislative intent to fully maintain local streets and roads funding to cities and counties. However, by swapping the sales tax to an excise tax, the key provision of Proposition 1A to protect local revenues is no longer applicable. In the future, the Legislature could reduce or eliminate this funding source. If that were to happen, the only source available to continue to fund street maintenance would be the General Fund.

In response to concerns regarding the State's use of local funds to balance its budget, a new ballot initiative is proposed for the November 2010 election. The measure known as the Local Taxpayer, Public Safety and Transportation Act of 2010 would close loopholes to prevent the State for further taking, diverting or borrowing local government, transportation, and public transit funds.

Conclusion

While the past 12 months have been challenging for the City, staff has continued to maintain service levels and meet Council goals and priorities, including:

- On May 6, 2010, the grand opening of the BMX track was held.
- Staff has worked with the development community to revise planning and permitting fees, and these will be presented for adoption in July.
- Staff continues to meet with the development community to review public infrastructure fees necessary to support future commercial, industrial and residential growth in our community.
- Entitled commercial projects include a 52.5-acre retail development know as Union Crossing; the CenterPoint 273-acre industrial project; and the completion of the Pacific Business Park Development, which is anticipated to provide five additional warehouse buildings.

In spite of the declines in the real estate market in our region, estimates from local builders indicate that residential construction will increase by 10-15 % over the next 12 months. Construction continues at the Woodbridge (Pulte Homes), Tesoro, Dutra Estates and Union Ranch East subdivisions. Manteca continues to lead the Valley in residential permits pulled. A total of 384 residential permits have been issued over the past 12 months.

During the next fiscal year, through enhanced economic development, staff will work to identify additional opportunities to both stabilize and expand our employment base. Meetings with our top employers will be conducted so we can ensure we are meeting their needs, and to develop successful partnerships between the business community and the City.

Measures have been adopted to lay the foundation for fiscal stability. Staff has developed a budget that strikes a balance of maintaining service levels within the limits of available resources, and continues to fund new projects to allow for future development and enhanced community amenities, while protecting our citizens from an uncertain financial outlook.

In preparing the Preliminary Budget, we have made our best efforts to balance these competing but equally important goals. Staff wishes to thank the Council for your leadership and support throughout the past year.

Steven J. Pinkerton, City Manager

Acknowledgements

Developing the Preliminary Budget is a team effort involving the time and talents of City employees, department managers, citizen's advisory groups, and staff members from the Finance Department. This year the extended budget development was interwoven with the ongoing demands of day-to-day operations.

Without the dedication of these City staff members, this budget would not have been possible. With Council's continued support of long-term planning and willingness to provide leadership in difficult circumstances, together we can develop a plan for the long-term financial stability of our City.