

NEW BUSINESS



AGENDA ITEM 15.4

August 23, 2011

TO: Mayor and City Council

FROM: Susan Mayer, Chief Financial Officer

SUBJECT: **FISCAL YEAR 2010-11 AND 2011-12 BUDGET UPDATES, AUTHORIZATION TO AMEND 2010-11 BUDGET, AND APPROVAL TO RECORD VARIOUS INTER-FUND TRANSFERS AND SETTLE INTER-FUND LOANS**

RECOMMENDATION

It is recommended that the City Council adopt a resolution amending the Fiscal Year 2010-11 budget and approving various inter-fund transfers and settlement of inter-fund loans to prepare for the closing of the City's general ledger for the fiscal year ended June 30, 2011.

Summary

The City Council has targeted "Fiscal Sustainability – Getting Our Fiscal House in Order" as one its four goals for 2011. One of the strategic initiatives developed to support this goal was a comprehensive business analysis of the City's funds and programs to assess current financial condition, liquidity, and program sustainability. This business analysis was a key process in the development of the 2011-12 budget and continues as the City prepares for the 2010-11 year-end close and publication of audited financial statements.

This report provides a budget update for 2010-11 and proposes a list of actions to address issues identified during the business analysis review of City programs. The City Manager made reference to the City's unfortunate past practice of complex inter-fund loans and deficit spending in his 2011-12 Budget Message and in his oral presentation to City Council during the 2011-12 budget workshop. Proposed actions in this report recognize and address programs with deficits, unwind a series of inter-fund loans, and consolidate unrestricted cash balances. This report takes actions to address these issues and continues positive, incremental steps to improve clarity about the overall fiscal condition of the City.

Moving forward into 2011-12, the City's budget condition continues to be impacted by external factors that challenge our ability to balance services within available revenues. This report updates the City Council on four significant events that have transpired since the adoption of the 2011-12 budget, including preliminary County Assessor results for the 2011-12 assessed property value tax base; the State's elimination of an important revenue allocation (Vehicle License Fee); further State action to eliminate redevelopment agencies; and the status of various employee labor contracts, including

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a recent fire arbitration ruling. Each of these four items put negative pressure on the City's General Fund budget. Despite these setbacks, the City remains committed to addressing challenges as they arise and recognizes its responsibility to continue to adjust service levels and costs as necessary to operate within available revenues.

DISCUSSION

Background

2010-11 Budget Update

The following General Fund 2010-11 budget update provides City Council with the status of this important source of discretionary funds and context for the following series of proposed financial transactions. It is still early in the 2010-11 year-end close process. Final tax and grant revenues are not expected until the end of September, 2011. We anticipate returning to City Council in November with an updated report on final 2010-11 results.

Overall, preliminary 2010-11 General Fund results indicate that operating costs have continued to exceed revenues. A series of one-time inter-fund transfers to and from the General Fund are identified with a net result of a June 30, 2011 General Fund balance that is currently estimated at \$722,000. This ending balance will continue to fluctuate as final tax revenues, grant reimbursements, and vendor payments are recorded. Prospectively, the City has implemented significant service and labor cost structure reductions for 2011-12 to balance its operations going forward. Staff is working on a plan to address the emerging issues impacting the recently adopted 2011-12 budget.

Revenue projections have improved by approximately \$700,000 to \$163 million since the last 2010-11 projection presented to City Council on May 17, 2011. Sales tax results for the quarter ending in March are an encouraging 3% above the comparable quarter in the prior year and have generated \$324,000 of this projection increase.

Program expenditures continue to track favorable to budget, but have eroded about \$300,000 since the last projection to \$167 million.

A series of one-time transactions are proposed to address uncollectible receivables and program deficits outside the General Fund. To cover these losses, with the assistance of outside counsel, we have identified a long-term liability that can be removed from the General Fund. This is a liability that is due from the General Fund to the Water and Wastewater Funds that is payable from future revenues and not from current resources.

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This liability is more appropriately recorded in the City's Debt Service Fund. With this change, the General Fund fund balance available for budgeting purposes will increase and better reflect the General Fund's current position. A detailed listing of proposed 2010-11 transactions are discussed in detail later in this report.

General Fund Projection 2010-11 As of 7-25-11	
Beginning Balance	<u>\$ 1,198,000</u>
Operating Activity	
Revenues	163,766,250
Expenditures	(167,169,900)
Encumbrance/other reserves	<u>1,112,907</u>
	(2,290,743)
One-time items	
Fire District Collection Risk	(1,047,000)
Transfer to Compensated Absence Fund	(4,000,000)
Transfers to cover other program deficits	(2,055,000)
Transfer MUD loan to debt service fund	8,417,000
Parking Fund loan repayment	<u>500,000</u>
	1,815,000
Net Annual Activity, including one-time items	<u>(475,743)</u>
Ending Balance	<u><u>\$ 722,257</u></u>

2011-12 Budget Update

Four significant events have transpired since City Council adopted its 2011-12 budget on June 21, 2011 that continue to challenge the City to maintain a balanced budget going forward into the new fiscal year.

1. Property Values and Related General Fund Property Tax Revenue

The County Assessor has released preliminary results for the January 2011 property valuations that are used to assess property taxes for the 2011-12 fiscal year. Results indicate a County-wide decline of 4% from the prior year. Results for the City of Stockton as a whole have declined 5.3% from the prior year. These results represent a fourth year of decline. The revenue impact to the City is shared between the Redevelopment Agency and the City's General Fund. Details on this split are not yet

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available from the County. However, the scope of this value decline is likely to have a significant impact on projected General Fund revenues. The 2011-12 property tax revenue budget had been developed with an assumption of stabilizing property values based upon projections provided by the City's contract tax consultant and from direct discussion with the County Assessor as recently as late April. These results have deteriorated from the last information available. It is likely that the General Fund budget will need to absorb a lower, revised revenue projection. A full loss of 5% in the General Fund would represent \$2 million in lower revenues. The final split between the Redevelopment Agency and the City is anticipated within the next month, at which time we can better measure the likely impact to the General Fund.

2. State Budget Impact – Vehicle License Fees and COPS Safety Grant

In the last hours before enacting its annual budget at the end of June, the State took unanticipated action to suspend local agency allocations of residual Vehicle License Fees that have been directed to cities and counties since 2004. The City's revenue budget loss from this elimination is \$1,047,000. This loss has been partially offset by restoration of the "COPS" public safety grant program that had just been cut in earlier state budget proposals. This new safety grant restores about half, or \$458,000, of restricted funds to the City. The City is exploring how it might use this grant to sustain its depleted Police Department budget.

3. Statewide Elimination of Redevelopment Agencies (or "Pay to Play")

The State has also passed legislation in conjunction with its annual budget to eliminate prospective Redevelopment activities. This legislation has been challenged in a lawsuit filed by the California Redevelopment Association and is unlikely to be resolved for some time. The City cannot at this point predict what impact the loss of its redevelopment agency would have on the General Fund of the City. A study session was held on August 16, 2011 presenting the City Council with details about the impact of this State action and options available to the Agency and City as a potential successor organization.

4. Status of Labor Contracts and Fire Arbitration Ruling

The City continues to negotiate with its employee organizations over salary and benefit concessions for the 2011-12 fiscal year. Voluntary agreements have now been ratified with all groups except Stockton Police Officers' Association (SPOA), Stockton City Employee's Association (SCEA), and Fire.

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The City reached a tentative agreement with the Fire and Fire Management groups that settled both 2010-11 and prospective compensation terms. The Fire Management group ratified and City Council approved their Memorandum of Understanding on August 9, 2011. Unfortunately the Fire (non-management) group failed to ratify. On August 9, 2011 Council approved implementation of the City's Last, Best and Final offer, effective August 1, 2011.

On July 22, 2011, the arbitrator in the dispute between the City and the Stockton Professional Firefighters Local 456 has ruled with a split decision about employee compensation during the 2010-11 Fiscal Year. The Arbitrator upheld the City's actions to close a truck company, concluding that there were "extraordinary circumstances" justifying the closure. However, the City did not prevail on a second point, in which the Arbitrator concluded that at the time of the Council decision not to grant union raises, the "emergency" was not "imminent" in June 2010 as he interpreted the labor contract. The Arbitrator did not impose any damages, but ordered the parties to attempt to resolve the issue of remedy. The City's rights under the Constitution are subject to parallel litigation that remains to be considered by the Superior Court. At this time, the City is unable to predict the total amount of one-time back pay that it may owe as a remedy in this dispute.

The City's initial estimate for the potential liability from the arbitrator's ruling was \$4 million in one-time retroactive 2010-11 compensation. Staff is working to refine this estimate now that final fiscal year 2010-2011 payroll costs are available. The ruling has no future impact to 2011-12, since the Fire contract expired June 30, 2011. Should the City exhaust its legal remedies and need to make this \$4 million payment, the Fire Department budget would anticipate further offsetting service reductions and additional negotiated labor cost reductions to continue to operate within its \$40 million annual budget.

Proposed 2010-11 Budget and Loan Actions

Returning to 2010-11, the following is a discussion of specific proposed 2010-11 actions.

1) Labor negotiations and related litigation costs

Labor negotiations and related litigation costs are expected to reach \$1.9 million for the 2010-11 fiscal year. Costs include negotiating efforts with 10 bargaining groups, essentially at the same time, to achieve the \$25 million in annual General Fund labor cost reductions incorporated into the 2011-12 budget in lieu of severe service

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reductions. Costs also include defense of City against of police and fire employee objections to the 2010-11 emergency measures, including a very expensive fire arbitration.

The proposed budget action approves the transfer of current 2010-11 appropriations from anticipated Police and Fire department savings into the Non-department budget account designated to track these labor litigation costs. The proposed action is a transfer of existing appropriations between departments and is not a net increase to expenditure authority.

The following is the proposed budget action:

General Fund #010 – Police and Fire Departments	
Transfer expenditure budget to non-department accounts, not to exceed realized 2010-11 savings	(\$1,900,000)
General Fund #010 - Non-Department	
Increase expenditure budget – Labor Litigation	\$1,900,000

2) Billing for Fire Services Provided to Independent Special Districts and Related Indirect Overhead Costs

The Fire Department provides services to several independent fire districts in the region (Eastside, Lincoln, Tuxedo Country Club and Boggs Tract). The fire districts are billed annually for a prorated share of the Fire Department's budget. The parties are in dispute over the basis of this calculation and the City has accumulated approximately \$2.3 million in uncollected accounts receivable balances due from these districts for the four year period from July 1, 2007 through June 30, 2011. The parties have discussed this issue over the years without resolution. Recent talks have reduced the accumulated dispute from \$2.3 million to \$1 million, and the parties have conceptually agreed to a new calculation going forward.

To minimize the amount at risk for 2010-11, a budget transfer is proposed to load the City's overhead cost onto the Fire Department budget in the same fashion in which overhead is allocated to other non-General Fund programs. This will provide the true cost of the fire department operations, including support cost such as the City's administrative functions including payroll and accounts payable. City Indirect cost allocations have not traditionally been formally recorded between the administrative and program departments in the General Fund since this effort would not change the total General Fund operating costs. Allocation of these costs to the Fire Department at this time, however, will increase the billable base budget to provide full cost recovery from

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the independent fire districts. The proposed indirect costs to be allocated to the Fire Department, as computed through the city-wide cost plan, totals \$1,608,000. Proration of this budget increment to the districts will reduce approximately \$147,000 of collection risk to the General Fund.

The following is the proposed budget action:

General Fund #010 - Fire Department	
Increase expenditure budget	\$1,608,000
General Fund #010 - Non-Department	
Decrease expenditure budget for allocated overhead	\$1,608,000

3) Golf Fund

City Council has received several reports on the operation of the City's two golf courses on April 13, 2010, May 19, 2010, May 25, 2011, and June 21, 2011. To address ongoing program deficits, City Council has authorized the award of a new management agreement with Kemper Golf on June 21, 2011. The 2011-12 Golf Fund budget has assumed that residual balances in the Recreation Special Revenue Fund will be used to fund both the accumulated 2010-11 Golf Fund operating shortfall and the projected 2011-12 shortfall pending implementation of the new contract. The proposed action will formally authorize use of recreation funds in 2010-11:

The following is the proposed budget action:

Recreation Special Revenue Fund #044	
Expenditure - Transfer Out	(\$498,000)
Golf Enterprise Fund #481	
Revenue - Transfer In	\$498,000

4) Public Facilities Administration Fund

The City administers over 20 Public Facilities Fee Districts and related zones. Public Facilities fees are collected to finance the infrastructure cost of development. An administration charge of 2.5% on all Public Facilities fees supports the supporting staff costs of administering the program. Administrative fee revenues have experienced the same sharp drop off as other development fees during this economic cycle and no longer support the prior level of supporting staff costs. While staff levels and allocations have been adjusted in the 2011-12 budget, in line with current revenue trends, a short

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fall has accumulated for 2010-11. The proposed action acknowledges this program loss and authorizes a backfill transfer from the General Fund.

The following is the proposed budget action:

General Fund #010	
Expenditure – Non-Department Transfer Out	(\$480,000)
Public Facilities Administration Fund #999	
Revenue - Transfer In	\$480,000

5) Debt Administration

The City administers approximately 50 bond issues and lease financing agreements. Seven of these bond issues are backed by the General Fund and have been issued since 2004. However, the methodology for the allocating the costs to support the debt program has not been updated to reflect the current debt structure. A treasury and debt administration pool has been established and appropriated in the 2011-12 budget. A new cost allocation methodology is under evaluation. The proposed action acknowledges and addresses the cost of General Fund participation in the City's debt program. The proposed action establishes a transfer to the debt service fund to fund these costs. The transfer will be recorded after actual charges are calculated and allocated to the various City debt programs. Without this change, the City would be vulnerable to a challenge on its cost allocation.

The following is the proposed budget action:

General Fund #010	
Expenditure – Non-Department Transfer Out	(\$250,000)
City Debt Service Fund #201	
Revenue - Transfer In	\$250,000

6) Compensated Absences

The City uses the Compensated Absences Internal Services Fund to accumulate resources to pay vacation, sick, and other leave balances due to employees upon retirement or separation from the City. Program departments contribute a percentage of their respective payroll costs annually to the Fund. However, budgeted contributions to the fund have not kept pace with disbursements.

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The fund has accumulated a significant cash deficit due to accelerated workforce reduction over the past three years. The fund deficit exceeded \$2 million at June 2010 and has escalated to over \$5 million at June 2011. The General Fund allocation of the projected June 2011 deficit is expected to reach \$4 million. This projection has increased by \$1 million from prior projections due to an increase in the number of retirements and of the early implementation of fire department workforce reductions which have accelerated costs from the 2011-12 fiscal year into 2010-11. As an aside, the General Fund's compensated absence liability has shed 11% during the past year. The General Fund remains exposed to a long-term liability of \$16 million at June, 2011.

For planning purposes, due to the significance of these Compensated Absence Fund deficits, budget action is proposed to amend the General Fund budget to provide for this anticipated shortfall and supplemental internal service fund contribution. The actual contribution will be recorded at the level necessary to zero the Compensated Absence Fund deficit, and may differ from this estimated level. Non-general fund programs will share in the deficit, but are not proposed for budget amendment at this time due to uncertainty of the final allocations.

The following is the proposed budget action:

General Fund #010	
Expenditure – Compensated Absence ISF charges -	
To be allocated to individual contributing departments	(\$4,000,000)
Compensated Absence Internal Service Fund #562	
Revenue – Charges for Services	\$4,000,000

7) Technology Funds

This item addresses both cash surplus and cash deficits in the Technology/Equipment Internal Service Funds. Although equipment rental charges to departments are intended to cover the cost of operations, over time imbalances have been created through savings or overruns in the various programs. The proposed action identifies surplus cash balances in two of the Technology/Equipment funds (Printing and Mailing Fund #508 - \$171,956; Telephone Equipment Fund #504 - \$330,000), covers a deficit in a third (Office Equipment Fund #550 - \$171,956), and consolidates the net available balance in the primary technology fund (Technology Fund #502 - \$330,000) for use in one-time projects in the 2011-12 budget. This consolidation of available funds into the Technology Equipment Fund (502) enhances the organizational capacity to leverage and focus these funds into technology projects prioritized for best city-wide benefit. The net result of this transaction will zero the balances in the Printing and Mailing Fund

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(508). As of July 1, 2011, the Printing and Mailing Fund (508) has been consolidated with the Office Equipment Fund (505).

The following is the proposed budget action:

Printing and Mailing #508	
Transfer In	\$171,956
Office Equipment #505	
Transfer Out	(\$171,956)
Telephone Equipment #504	
Transfer Out	(\$330,000)
Technology #502	
Transfer In	\$330,000

8) Development Services Fund Inter-fund Loans

The City's Development Services Fund carries a \$4.8 million loan receivable from the General Fund established to address a legal challenge over its fee structure. The Development Service Fund in turn has working capital loan obligations back to the General Fund and to the Workers Compensation Internal Service Fund to provide cash for current operations. The loan from the Workers Compensation Fund was approved as part of the 2009-10 budget. The loan from the General Fund was recorded as of June 30, 2010 to address the Development Service Fund's cash deficit. The three loans approximately offset within the Development Services Fund. The unwinding of these loans will improve transparency on the true liquidity of each of these funds and restores the cash balance of the Development Services Fund.

The following is the proposed 2010-11 accounting action:

General Fund	
Loan repayment to Development Services Fund	(\$4,849,481)
Development Services Fund #048	
Loan repayment from General Fund	\$4,849,481
Loan repayment to General Fund	(\$2,896,672)
Loan repayment to Workers Comp Fund	(\$1,650,000)

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9) Parking Fund Inter-fund Loans

The City's Parking Enterprise Fund carries inter-fund loan obligations to the General Fund (\$500,000), General Liability Internal Service Fund (\$530,000), and the Air Quality Public Facility Fee Fund (\$1,000,000). The loans from the General Fund and General Liability Funds were recorded to provide cash flow to settle legal challenges from property acquisition, including the acquisition of the Arena and its adjacent parking garage. The loan from the Public Facilities Fee Fund supplemented bond proceeds to finance construction of parking facilities. The Parking Fund has accumulated a cash balance sufficient to settle the General Fund loan at June 30, 2011. Should additional surplus cash be available, a portion of the other loans will also be evaluated for repayment. Ongoing Parking program revenues support the viability of ongoing annual amortization and repayment of these remaining loan balances.

The following is the proposed accounting action. The actual entry will include accumulated interest charges.

Parking #416	
Loan repayment to General Fund	(\$500,000)
General Fund #010	
Loan Repayment from Parking Fund #416	\$500,000

10) Marina and Redevelopment Loans

In 2008-09, City Council authorized a \$500,000 loan from the Redevelopment Agency's Waterfront Project Area to the Marina Fund in conjunction with its expansion project. This loan has two issues. First, the Waterfront project area is operating at a deficit and could benefit from the use of this loan to settle its own obligations to other funds, such as the Workers Compensation Fund. Second, the Marina Enterprise has not realized its revenue potential and carries sizable debt service through a State Department of Boating and Waterways loan that is separately supported through a General Fund operating contribution. Because the Marina does not have the demonstrated ability to repay this loan in the foreseeable future, the loan receivable on the Waterfront books is a collection risk. The proposed action unwinds this loan by transferring the obligation from the Marina to the Workers Compensation Fund, where it can offset a portion of another loan the Workers Compensation Fund has extended to the Waterfront Project area. The Workers Compensation fund advanced \$8 million in working capital funds to the Waterfront Project Area during 2009-10. The proposed action further backfills the Marina cash with a General Fund transfer funded by the collection of its Parking Fund loan in the same amount, discussed in Item #9 above.

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The following are the proposed accounting actions:

Marina Fund #460		
Transfer loan from Waterfront Fund to		
Workers Compensation Fund		(\$500,000)
Workers Compensation Fund #551		
Receive loan from Waterfront Fund from		
Marina Fund		\$500,000
Waterfront Fund #343		
Loan Repayment from Marina Fund		\$500,000
Loan Repayment to Workers Compensation Fund		(\$500,000)
General Fund #010		
Non-Department Expenditure – Transfer out - Marina		(\$500,000)
Marina Fund #460		
Revenue – Transfer In		\$500,000

Capital Improvement Program

The City's capital improvement program has been overcommitted in excess of \$20 million. This condition has evolved over time through reliance on optimistic development revenue projections and decentralized capital project management without sufficient budget monitoring processes to identify and address program deficits as the City's fast growing development revenue came to a halt. A portion of these deficits were authorized through inter-fund loans that were supportable with anticipated development revenue at the time of approval, but are no longer sustainable. Further, since four of the Public Facility Fee revenues were leveraged through a 2009 bond issue, future development revenues in these targeted fee areas are committed to pay debt service on the \$35 million of outstanding principal, and are not available to repay inter-fund loans in the foreseeable future.

Capital program commitments and identified deficits have been addressed by a cross-departmental team of Public Works, Community Development, Budget, and Accounting staff. City Council's action to merge four Street Improvement Public Facilities Fee zones on June 21, 2011 has addressed approximately \$6 million of this deficit. Another \$2 million has been addressed through replacement funding sources. \$7 million of projects have been deferred or cancelled as of June 30, 2011 and will not be carried over into the following fiscal year. Approximately \$2 million of unfunded interest charges are proposed for reallocation to other sources. Finally, about \$7 million of inter-

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fund loans in three Public Facilities Fees funds have not yet been addressed, and are further discussed below.

11) Capital Projects – Replacement Funding

The following changes are to correct a continuing problem where capital projects were approved based upon Public Facilities fee revenue projections that did not reflect the current economic downturn. For these projects, alternative replacement revenue sources have been identified. No changes are proposed to the size or scope of these projects. The only change is to update the revenue sources that pay for the project. Transfer of budget appropriations to these new revenue sources will help cure program deficits in the original source funds.

The following is the proposed budget action:

I-5 French Camp Project

Replace Citywide Street Fee revenue with Regional Transportation Fee revenue

Fund #915 – Public Facilities Fees (Citywide Street Fees)	
Increase expenditures – I-5 French Camp	\$1,418,692
Fund #917 – Public Facilities Fees (Regional Transportation)	
Decrease expenditures – I-5 French Camp	(\$1,418,692)

Street Improvement Projects, Zones 1&2

Replace Street Improvement Fee revenue with Area of Benefit revenues

Fund #304 – Capital Reimbursements (from project list below)	
Increase revenues and expenditures	\$945,742
Fund #911 – Public Facilities Fees (Street Zone 1&2)	
Decrease expenditures	(\$945,742)

Capital Reimbursement Project List

Lower Sacramento Road/Whistler Rd Traffic Signal	\$ 30,815
Hammer/West Lane Intersection	13,809
I-% Soundwalls Cal. River to 14 Mile Slough	120,999
Eight Mile Road/UPRR GS	707,791
Lorraine/hammer Lane Replace Traffic Signal	287
Morada/99 Overcross PSR	1,899
Whistler Way Extension	58,196
Davis Road Bridge Approaches	11,946
	<u>\$945,742</u>

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12) Grant Programs – Negative Interest

The City benefits from significant Federal, State, and local grant funding. Dedicated accounting funds have been set up to provide separate accountability for most grant programs outside of the General Fund. Most grant programs are operated on a reimbursement basis such that the City must first incur qualifying expenditures and then seek reimbursement based upon documented actual costs. The timing difference between City disbursements and the subsequent reimbursements creates cash borrowing from the City investment pool and associated interest charges. Unfortunately, interest charges exceeding \$2 million dollars have accumulated in the grant funds over the past 5 to 10 years without an eligible funding source. The proposed action acknowledges these unfunded costs and authorizes transfers from the Gas Tax Fund for shortages in the Transportation Program “SAFETEA” capital grant fund; from housing funds for shortages in the HUD program funds, including CDBG and HOME program funds; and from the General Fund for other grant programs in the multi-program capital grant fund. Prospectively, the underlying cause of this issue continues, as the City continues to leverage tens of millions of dollars annually through these successful grant programs. However, procedures have been revised to minimize negative grant interest charges. Grant billings will be prioritized, with a particular focus on large capital expenditures, to minimize the time lag between grant disbursement and reimbursement.

The following is the proposed budget action:

a) Transportation Programs	
Gas Tax Fund #030	
Expenditure – Transfer Out	(\$987,156)
SAFETEA Capital Grant Fund #038	
Revenue – Transfer In	\$987,156
b) Multi-fund Programs	
General Fund #010	
Expenditure – Non-Department - Transfer Out	(\$825,000)
Capital Grant Fund #304	
Revenue - Transfer In	825,000
c) Housing Programs	
Façade Fund #056	
Expenditure –Transfer Out	(\$243,697)

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HUD Funds – Transfers In	
CDBG #052	\$189,528
Special Grant & Loan Programs #053	\$17,000
CalHOME #060	\$30,431
Emergency Shelter Grant #057	\$6,738

13) Public Facilities Loans – Police, Fire, and Community Center Programs

The Police, Fire, and Community Center Public Facility Fee programs have constructed \$7 million in projects financed with loans from other Public Facility Fee Programs that are at risk for repayment in the foreseeable future. The improvement projects financed with these funds include the Teen Center, the Arena events center, the McNair Community Center, Fire Station #13, and the North Stockton police sub-station. The unified Street Improvement Public Facilities Fee is the primary source for these loans, which is owed \$5 million in principal.

Additional Public Facility Fee projects have also been financed by the City's \$35 million 2009 lease revenue bond issue. Because current and projected development fee revenues in the Police and Fire programs are committed to debt service on the 2009 Public Facilities Fee bonds, they are not available to repay these inter-fund loans in the foreseeable future. Further, the lending Public Facilities Fee programs have projects to schedule within the timelines required by State AB1600 that will require collection of these loans to finance project delivery. Even optimistic development revenue projections are unable to anticipate loan repayments within the next ten years.

Government Accounting Standards require an ongoing assessment of the realization of recorded receivables in the lending fund, and further require evidence of the ability and intent to repay inter-fund loans. These loans do not currently meet these criteria. Further, these inter-fund loans cannot simply be written off since the financed projects are not eligible expenditures of the funds from which the loans were made.

This report does not recommend corrective actions on these loan transactions at this time. However, a solution will be needed to complete the City's annual financial report. Staff will continue to compile actual year-end balances for the General and other unrestricted funds and return to City Council with a recommendation to further consolidate available balances and transfer these loans from restricted to unrestricted sources. This action will allow the restricted Public Facility Fee programs to complete the projects for which their fees were originally collected. The loans to the Police, Community Center, and Fire programs will be proposed to be held in the City's capital fund, offset by an allowance for doubtful accounts, until such time that development

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revenues are restored and repayment can be scheduled. To complete this proposal, \$7 million in unrestricted resources will need to be identified and transferred to the Capital Fund. This may require cancellation of additional projects or transfer of funds from other priority City programs but is a necessary step to openly address and measure the net unrestricted funds available to the City.

14) Measure K

The City receives Measure K transportation grant allocations for both capital and maintenance operating programs. For many years both capital and operating funds were administered in a consolidated fund. Beginning in 2010-11, activities were separated into the #80 Capital Fund and the #82 Operating Fund to improve budget and reporting accountability. The proposed action completes this segregation by finalizing the split of existing resources between funds according to their original Measure K source allocations. The following budget authorization is based upon program cash flow projections. The actual recorded transfer will be based upon actual 2010-11 receipts and expenditures.

The following is the proposed budget action:

Measure K – Capital Fund #80	
Expenditure - Transfer Out	(\$3,384,164)
Measure K – Operating Fund #82	
Revenue - Transfer In	\$3,384,164

15) Wastewater Public Facilities Fee Loan

The 2004-05 budget authorized a \$10 million working capital loan from the Wastewater Public Facilities Fee Fund to the Wastewater Operating Fund. The loan financed repairs at the Regional Wastewater Treatment Facility following OMI/Thames assumption of operations. The Operating Fund now holds sufficient cash to repay the loan with accrued interest. This repayment is proposed at this time to restore the Public Facility Fee cash position to facilitate development of its capital spending plan. In addition to the \$10 million principal balance, accrued interest will also be updated and charged. Some interest payments have been made over the years.

The following is principal balance of the proposed budget action:

Wastewater Operating Fund #431	
Loan repayment to Public Facilities Fee Fund	(\$10,000,000)

FISCAL YEAR 2010-11 AND 2011-12 BUDGET UPDATES, AUTHORIZATION TO AMEND 2010-11 BUDGET, AND APPROVAL TO RECORD VARIOUS INTER-FUND TRANSFERS AND SETTLE INTER-FUND LOANS

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Wastewater Public Facilities Fee Fund #434	
Loan repayment from Operating Fund	\$10,000,000

16) MUD/Jarvis Settlement

In 2009, the City entered into a legal settlement requiring the City's General Fund and General Capital Fund to repay the City's Water and Wastewater Funds for Proposition 218 violations. As of June 30, 2010, the balance due was \$20,016,000, payable in annual installments of \$1.1 million for thirty years. Consistent with Government Accounting Standards, this obligation has been reported as a loan payable in the City's fund financial statements.

Subsequent research indicates that as a judicial order, this obligation meets the State constitutional criteria for long-term debt that does not require voter approval, and is therefore not an obligation that restricts current resources. Further, the City's General Capital Projects fund has no substantive current revenue source other than annual General Fund contributions, and accordingly the substance of this loan is a General Fund obligation.

For these reasons, the proposed action transfers this inter-fund loan obligation from the General Fund and General Capital Projects Funds to the City's General Debt Service Fund #201 for amortization through annual debt service transfers similar to other long-term bonded debt obligations. This action will remove this long-term obligation from the General Fund balance sheet and free one-time resources to address the significant program deficits and supplemental appropriations described throughout this report. Prospectively, annual transfers from the General Fund to the Debt Service fund will provide the cash flow to continue the payment schedule to the Water and Wastewater Funds as required by the 2009 settlement agreement. The 2011-12 General Fund budget includes a \$1.1 million transfer for this purpose.

The following is the proposed budget action:

Debt Service Fund #201	
Loan from Water/Wastewater Funds	\$20,016,000
Expenditure – Transfer Out – General Fund #010	(\$8,417,000)
Expenditure – Transfer Out – Capital Fund #301	(\$11,599,000)
General Fund #010	
Revenue - Transfer In - Debt Service Fund #201	\$8,417,000
Loan from Water/Wastewater Funds #421/431	(\$8,417,000)

FISCAL YEAR 2010-11 AND 2011-12 BUDGET UPDATES, AUTHORIZATION TO AMEND 2010-11 BUDGET, AND APPROVAL TO RECORD VARIOUS INTER-FUND TRANSFERS AND SETTLE INTER-FUND LOANS

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General Capital Projects Fund #301	
Revenue - Transfer In – Debt Service Fund #201	\$11,599,000
Loan from Water/Wastewater Funds #421/431	(\$11,599,000)

Present Situation

The proposed 2010-11 actions support the City Council goal of “Fiscal Sustainability – Getting Our Fiscal House in Order” and make progress on the Business Analysis Strategic Initiative developed to support this goal. These actions continue to take positive, incremental steps to improve clarity about the overall fiscal condition of the City.

Final 2010-11 tax revenues and ending fund balances for all city funds will continue to be compiled and analyzed during the next two months. Concurrently, staff will be working on implementation plans to address emerging 2011-12 budget challenges from the anticipated additional loss of property tax revenues, elimination of state vehicle license fees, and the uncertain future of Redevelopment tax increment revenue. The Fire department is also developing contingency plans to address a potential arbitration budget impact through further service reductions or negotiated compensation reductions to maintain spending within its \$40 million annual operating budget.

The proposed resolutions amend the 2010-11 budget, approve transfers, and approve loan settlements as discussed above. Separate actions are proposed for the City and the Redevelopment Agency.

FINANCIAL SUMMARY

This report proposes actions that provide a path for the General Fund to end 2010-11 with a small surplus balance. As fund results are compiled, unrestricted surpluses in all City funds will be evaluated and considered for transfer to the City’s General Capital Project Fund to backfill \$7 million of inter-fund loans from restricted sources that currently carry repayment risk. Further, evolving challenges to the City’s 2011-12 budget plan may require implementation of additional service and labor cost reductions. Staff is working on the development of these plans.

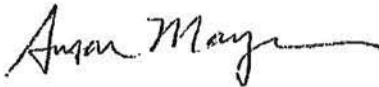
The entire City executive team recognizes the responsibility and the authority you have vested in us to take the actions necessary to maintain the City’s 2011-12 budget and to continue a path towards multi-year fiscal sustainability.

August 23, 2011

**FISCAL YEAR 2010-11 AND 2011-12 BUDGET UPDATES, AUTHORIZATION TO
AMEND 2010-11 BUDGET, AND APPROVAL TO RECORD VARIOUS INTER-FUND
TRANSFERS AND SETTLE INTER-FUND LOANS**

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Respectfully submitted,



SUSAN MAYER
CHIEF FINANCIAL OFFICER

APPROVED



LAURIE MONTES
DEPUTY CITY MANAGER

SM:jl

STOCKTON CITY COUNCIL

RESOLUTION OF THE CITY COUNCIL OF THE CITY OF STOCKTON APPROVING AMENDMENTS TO THE 2010-2011 ANNUAL BUDGET; APPROVING VARIOUS INTERFUND TRANSFERS; AND APPROVING SETTLEMENT OF INTERFUND LOANS

The City Council adopted the 2010-2011 Annual Budget on June 22, 2010; and

The City Council received updates on the 2010-2011 Budget on November 16, 2010, February 15, 2011, March 29, 2011, and May 17, 2011; and

Fiscal Sustainability is one of the City Council's 2011 goals; and

By the staff report accompanying this Resolution, the Council has been provided with additional information upon which the actions set forth in this Resolution are based; now, therefore,

BE IT RESOLVED BY THE CITY COUNCIL OF THE CITY OF STOCKTON, AS FOLLOWS:

1. The 2010-2011 Annual Budget is amended to include the adjustments, inter-fund transfers, and inter-fund loan repayments as outlined in Exhibit 1.
2. The City Manager is authorized and directed to take such actions as are appropriate to carry out the purpose and intent of this resolution.

PASSED, APPROVED, and ADOPTED August 23, 2011.

ANN JOHNSTON, Mayor
of the City of Stockton

ATTEST:

BONNIE PAIGE
City Clerk of the City of Stockton

City Atty
Review GOP
Date August 17, 2011

Exhibit 1
City of Stockton
Amendments to the 2010-2011 Annual Budget and Settlement of Inter-fund Loans
August 23, 2011

	<u>Amount</u>
1) <u>Labor Negotiation and related litigation costs</u>	
General Fund #010 Expenditures	
Police, Fire or other program department budget, not to exceed amount of realized budget savings	(1,900,000)
Non-Departmental - Labor Negotiation	1,900,000
2) <u>Billing for Fire Services Provided to Independent Special Districts and Related Indirect Overhead Costs</u>	
General Fund #010 Expenditures	
Non-Departmental	(1,608,000)
Fire Department - Indirect Costs	1,608,000
3) <u>Golf Fund</u>	
Transfer From:	
Recreation Fund #044	(498,000)
Transfer To:	
Golf Fund #481	498,000
4) <u>Public Facilities Administration Fund</u>	
Transfer From:	
General Fund #010	(480,000)
Transfer To:	
Public Facilities Administration Fund #990	480,000
5) <u>Debt Administration</u>	
Transfer From:	
General Fund #010	(250,000)
Transfer To:	
City Debt Service Fund #201	250,000
6) <u>Compensated Absences</u>	
Transfer From:	
General Fund #010	(4,000,000)
Transfer To:	
Compensated Absence Fund #562	4,000,000

Exhibit 1
 City of Stockton
 Amendments to the 2010-2011 Annual Budget and Settlement of Inter-fund Loans
 August 23, 2011

	<u>Amount</u>
<u>Continued</u>	
7) <u>Technology Funds</u>	
Transfer From:	
Office Equipment #505	(171,956)
Telephone Equipment #504	(330,000)
Transfer To:	
Printing and Mailing #508	171,956
Technology #502	330,000
8) <u>Development Services Fund Inter-fund Loans</u>	
Development Services Loan to General Fund	
General Fund #010 Repayment	(4,849,481)
Development Services #048	4,849,481
General Fund Loan to Development Services	
General Fund #010	2,896,672
Development Services #048 Repayment	(2,896,672)
Workers' Compensation Loan to Development Services	
Workers' Compensation #551	1,650,000
Development Services #048 Repayment	(1,650,000)
9) <u>Parking Fund Inter-fund Loans</u>	
Transfer From:	
Central Parking District Operating Fund #416	(500,000)
Transfer To:	
Central Parking District Capital Fund #417	500,000
General Fund Loan to Central Parking District	
Parking Capital Fund #417 Repayment	(500,000)
General Fund #010	500,000

Exhibit 1
City of Stockton
Amendments to the 2010-2011 Annual Budget and Settlement of Inter-fund Loans
August 23, 2011

	<u>Amount</u>
<u>Continued</u>	
10) <u>Marina and Redevelopment Loans</u>	
Marina Fund #460	
Transfer loan from Waterfront Fund to Workers Compensation Fund	(500,000)
Workers Compensation Fund #551	
Receive loan from Waterfront Fund from Marina Fund	500,000
Transfer From:	
General Fund #010	(500,000)
Transfer To:	
Marina Fund #460	500,000
11) <u>Capital Projects – Replacement Funding</u>	
Capital Expenditures	
Capital Reimbursements Fund #304	945,742
Public Facilities Fees Fund #911	(945,742)
Public Facilities (Citywide Street Fees) Fund #915	1,418,692
Public Facilities (Regional Transportation) Fund #917	(1,418,692)
12) <u>Grant Programs – Negative Interest</u>	
Transfer From:	
Gas Tax Fund #030	(987,156)
Transfer To:	
SAFETEA Capital Grant Fund #038	987,156
Transfer From:	
General Fund #010	(825,000)
Transfer To:	
Capital Grant Fund #304	825,000

Exhibit 1
City of Stockton
Amendments to the 2010-2011 Annual Budget and Settlement of Inter-fund Loans
August 23, 2011

	<u>Amount</u>
<u>Continued</u>	
12) <u>Grant Programs – Negative Interest</u>	
Transfer From:	
Façade Fund #056	(243,697)
Transfer To:	
CDBG #052	189,528
Special Grant & Loan Programs #053	17,000
CalHOME #060	30,431
Emergency Shelter Grant #057	6,738
14) <u>Measure K</u>	
Transfer From:	
Measure K – Capital Fund #80	(3,384,164)
Transfer To:	
Measure K – Operating Fund #82	3,384,164
15) <u>Wastewater Public Facilities Fee Loan</u>	
Wastewater Public Facilities Fee Fund Loan to Wastewater Operating Fund	
Wastewater Operating Fund #431 Repayment	(10,000,000)
Wastewater Public Facilities Fee Fund #434	10,000,000
16) <u>MUD/Jarvis Settlement</u>	
Debt Service Fund #201	
Loan from Water/Wastewater Funds	20,016,000
Expenditure – Transfer Out – General Fund #010	(8,417,000)
Expenditure – Transfer Out – Capital Fund #310	(11,599,000)
General Fund #010	
Revenue - Transfer In - Debt Service Fund #201	8,417,000
Loan from Water/Wastewater Funds #421/431	(8,417,000)
General Capital Projects Fund #301	
Revenue - Transfer In – Debt Service Fund #201	11,599,000
Loan from Water/Wastewater Funds #421/431	(11,599,000)