

Foster City Financial Update IQ 10/11

City of Foster City

For the Three Months Ended September 30, 2010

General Fund Revenues Likely to Fall \$1.5 Million Behind Original FY 2010-2011 Budget Projections

A reduction in the estimate of excess property taxes flowing from the Community Development Agency (CDA), the impact of assessment appeals granted on property tax revenues, and the likelihood of reduced sales tax revenues for businesses vacating Foster City will reduce the General Fund's revenue projections by \$1.5 million for FY 2010-2011 based upon known information at the end of the 1st Quarter.

As previously indicated in the 4Q 09/10 update, updated property tax projections and a correction in the property

tax increment analysis for the CDA's Project One Area will have a \$1.3 million negative impact on the revenue projections for the current year.

In addition, the County Controller's Office has provided the estimated property tax collection figures for FY 2010-2011, and it appears that property tax revenues will fall nearly \$600,000 short of the original projections as provided by the County Assessor's Office. Last minute assessment appeals granted prior to June 30, 2010, which reduced the value on which property tax would be assessed,

are the cause for the decrease. As an offset to these reductions, the County has indicated that a refund of prior ERAF funds taken from the City will total nearly \$400,000, which was not included in the original budget.

The other significant change is as a result of reduced sales tax revenues expected from companies relocating out of Foster City or going out of business. The net impact of those changes is expected to soften sales tax revenues by \$57,000, which is less than the \$115,000 anticipated in the last quarterly update.

Included in this report:

<i>General Fund Revenues Falling \$1.5 million short in FY 10-11</i>	1
<i>Water Rate Changes Impact Residential Customers</i>	1
<i>Key General Fund Revenue Trends in FY 10-11</i>	2
<i>Financial Trends Impacting FY 10-11</i>	3
<i>Status of Community Development Agency Fund</i>	4
<i>State Budget and Elections Update</i>	4

Highlights:

- General Fund Revenues may finish the year \$1.5 million behind projections.
- Water rate impacts are signaling the need for conservation.
- Sales tax, TOT and permit revenues are trending higher than last year, while recreation fees are lagging behind last year.
- Foster City will see little or no additional negative impact as a result of the State Budget and the November elections.

Water Rate Changes Impacting Residential Customers; Conservation Efforts Underway

The newly implemented tiered water rates are gaining the attention of the majority of the District's water customers. Financial Services staff reports a significant increase in phone calls and e-mails from residents complaining about the

new water rates, seeking to understand the rate structure, the reasons for the new rates, and ways to manage water consumption. As expected, the summer months are the times when residential customers use greater amounts of water

for irrigation and swimming pool usage. While overall water consumption is down by 4.3% from the same quarter in 2009, residents are now fully understanding the impact of the rates on their need to conserve

(Continued on page 3)



Key General Fund Revenue Trends in FY 2010-2011

There are 10 key revenue sources that have a significant impact on the City's General Fund. Here are the trends we are following in FY 2010-2011.

Property Taxes (\$12.8m)

As indicated on Page 1, Property Tax revenues will likely fall short by \$1.5 million (net of the ERAF refund) from original projections due to reduced assessed property valuations and reduced excess tax increment from the CDA. The first wave of tax collections will come in December, and will be analyzed in the next quarterly update.

Sales Tax (\$3.95m)

Sales tax revenues will be negatively impacted by businesses relocating to other cities and some business closures. Collections in IQ 10/11 were \$199k, which is normal for 1st Quarter. There were no collections in 2009 during the same period as the State had overadvanced the City of its sales tax revenues in early 2009. Most businesses pay sales tax to the State Board of Equalization on a quarterly basis, and so the 1st

quarterly installment relative to IQ 10/11 will not be received until the end of November.

Transient Occupancy Tax (\$1.16m)

TOT revenue collections in IQ were up by nearly 10% from the prior year due to higher occupancy rates, primarily at the Crowne Plaza.

Franchise Taxes (\$1.02m)

Franchise tax revenues are not received until 45 days after the end of the quarter. Franchise tax collections will be analyzed in the next quarterly update.

Vehicle License Fees (\$2.76m)

VLF fees are received as part of the property tax allocation (due to the Triple Flip). As such, the first collection will not occur until December.

Business License Taxes (\$612k)

Business license taxes are not collected until February of each year. Business license collection in IQ 10/11 represents late payers or new businesses. Such collections are up by over 200% from the prior year.

Building Permits / Planning Fees (\$931k)

Building permit activity in IQ 10/11 is up by 64% from prior year, due primarily to building activity with Visa and Gilead Sciences as expected.

Investment Income (\$239k)

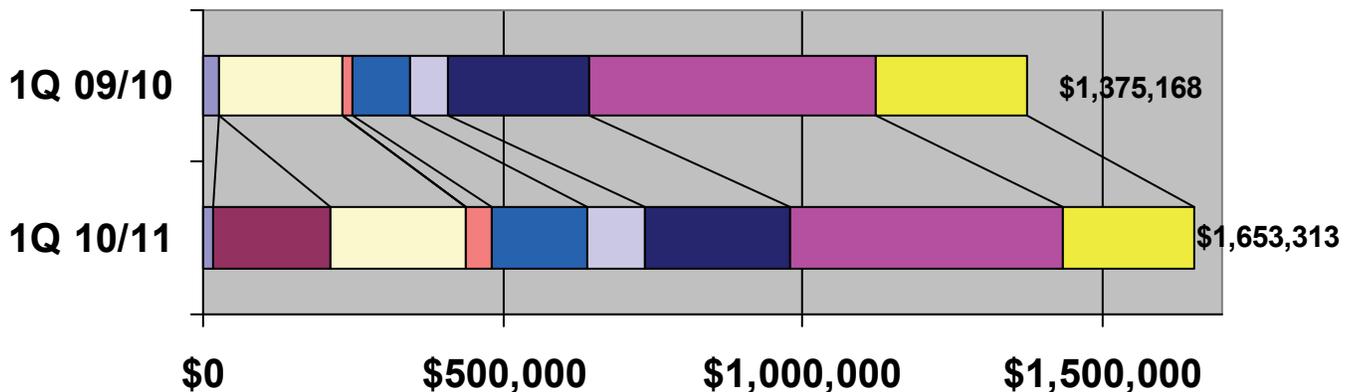
Interest rates continue to fall, however investment income is 50% greater than prior year primarily due to an increased investment in longer-term securities than in previous years that is providing greater yields. We expect interest rates to stay at record lows for some time.

Rental Income (\$789K)

Rental income is meeting budget projections in IQ 10/11.

Recreation Programs (\$1.11m)

Recreation program revenues were down by 5% when compared to prior quarter in all programs but Youth Contract Classes. We will be watching this trend as the Winter and Spring class enrollments begin.



Property Tax	Sales Tax	TOT	Franchise
VLF	Bus. Lic	Permits	Interest
Rent	Recreation	Other	



Water Rate Changes Providing Incentives for Water Conservation

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water. Most of the calls come from residents whose water usage pattern is 50-200% above the average for similar residential customers. Staff has worked with these customers to assist them in finding ways to reduce consumption, which was the goal of the tiered-rate structure.

As a result, total water revenues are up by almost 25% from the same period in 2009. Nearly \$100,000 of these revenues will be transferred into the newly created Sustainability Fund that will fund the City's various water rebate programs. There has been a slight increase in toilet rebates. Four (4) residents have had landscape audits performed on their properties to

learn ways of reducing water consumption. Customers have not indicated interest at this time in other rebate programs, but we anticipate that as Spring approaches and as the District expands its marketing efforts, customers may seek rebates for smart irrigation controllers as a means of reducing irrigation usage in the Spring.

Financial Trends Being Followed in FY 2010-2011

We are tracking the following trends in FY 2010-2011, including issues which have been made known to us in 2Q 10/11.

Surplus Property Tax Increment from CDA

As indicated earlier, when the CDA reaches its tax increment cap of \$170 million during the year, surplus property taxes will flow to EMID. Initial projections showed \$2.8 million flowing to the General Fund. Based on updated projections and correction of an error in the calculation, the figure will be \$1.5 million for FY 10-11. This is a one-time impact only. Ongoing revenues to the District beginning in FY 11-12 will be over \$4.8 million.

PERS Public Safety Rates Higher

CalPERS rejected the City's request, along with 8 other agencies, to reamortize the unfunded pension obligation for Public Safety. In August 2010, PERS revised its policies that would allow agencies to reapply if they met the updated criteria; however, any approvals would not go into effect until FY 2011-2012. The City has reviewed

the new policies and it appears the City would be eligible for a "Hardship Request". The City will file this request this December. Given PERS' rejection of the FY 10-11 request, this will impact the General Fund by \$800k in FY 10-11.

Lower Sales Tax Revenues Expected

Given the relocation timing and/or closure of various Foster City businesses that generate sales tax revenue, we have updated our projections for FY 10-11 and now estimate sales tax loss of ~ \$57k.

Property Tax Assessments Lowered by Assessor

As previously indicated, assessment appeals granted in June 2010 just prior to the closure of the tax rolls yielded a decline of approximately \$600,000 based on the County Controller's Office latest estimate of property tax collections for FY 10-11.

ERAF Refund

ERAF deductions from City property taxes are made each year based on conservative estimates of projected property values and tax status of school districts in the

County. Each year, the County Controller analyzes prior years' ERAF deductions and issues refunds to agencies for which excess ERAF has been withheld. Average ERAF refunds for the past 7 years have equaled \$580k. The current projections for the ERAF refund owed EMID is \$400k. These funds are not budgeted.

Employment Vacancies

There are currently 14 positions vacant, yet funded. Six (6) of these positions are in the Police Department, three (3) in Public Works, two (2) in Community Development, and one (1) position each in City Clerk, Fire, and Parks & Recreation. These positions are subject to the current hiring freeze. If these positions are not filled, salary and benefits savings totaling nearly \$1 million would be realized in the current year.

Opening Fund Balance

The fund balance for the General Fund started the year with \$22.1 million, which was over \$2.1 million greater than originally anticipated in the budget. The combination of the

(Continued on page 4)



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Status of Community Development Agency Funds

The County Controller's Office provided updated estimates on property tax increment collections for the Agency's three project areas.

- Project One Area - tax increment revenues will exceed projections by about \$100k. Since the Agency will reach its tax increment cap, this will positively impact the District and other taxing agencies as to excess tax increment.
- Marlin Cove - projected tax increment revenues will fall short by \$19k (2.5%) due to granted assessment appeals, however this project area has sufficient funds to meet its objectives.
- Hillsdale/Gull - tax increment revenues here will fall \$36k (or 20%) short of projections, but there are sufficient reserves to achieve the financial objectives in FY 2010-2011.

State Budget and November Elections Have Little Impact on Foster City

California legislators finally passed a State budget for FY 2010-2011 on October 8, nearly 100 days after the start of the fiscal year. The budget, which attempted to bridge a \$19 billion shortfall, comprised of nearly 70% of one-time savings by pushing expenditures beyond the fiscal year end date, temporary monies which may never materialize, and assumptions with respect to federal funding of Medicare and welfare programs which some experts are deeming unrealistic. The Legislative Analyst's Office says that California will face "sizeable

annual budget problems in FY 2011-2012 and beyond." Fortunately, none of the budget proposals took any additional monies from local government other than the \$350 million takeaway from redevelopment agencies that was approved in last year's budget. The Foster City Community Development Agency still plans on cutting a check to the State for about \$1.2 million in FY 2010-2011.

While the State will continue to wrestle with its budget woes, the passage of Proposition 22 by voters on November 2 will hopefully

stop any further raids on local government and transportation funds.

The passage of Proposition 26 is still be analyzed by the League of California Cities and City staff. The proposition was intended to prevent state and local government from passing along regulatory fees to various industries (the oil industry in particular), and now deems those type of fees as taxes. There are seven exemptions listed in the Proposition that exempt certain fees from the provisions of Prop 26. Some of those key exemptions in-

clude developers' fees, property related fees (water / sewer charges), fines and penalties, permits and inspection, lease or use of government property, and fees for services (e.g., recreation programs). Staff will continue to analyze the City's fees in relation to Prop 26, but initial review indicates that there may be little impact on the City's master fee schedule.

In all, Foster City was not significantly impacted by the State Budget and the recent Election results.

Trends Affecting FY 2010-2011

(Continued from page 3)

trends indicated above and the opening fund balance increase means that the General Fund could finish the year nearly \$750k above original projections.

Economic Trends



Staff is closely following key economic trends and their potential impact on Foster City. Those trends include:

- *Unemployment* - the California unemployment rate remains at 12.4%. Unemployment benefits were extended by Congress through November 30. Without another extension, consumer spending could cool off.
- *Real Estate Sales*—real estate sales have slowed in the past 90 days, and prices are softening slightly in Foster City.

- *Inflation* - inflation remains low at just under 1.0% for the SF Bay Area.
- *Financial Markets* - the Dow Jones Industrials gained 10.8% in 1Q 10/11 which if continued could help with PERS rates. However, 2-Year Treasury yields declined from 0.63% to 0.42%, which will negatively impact the City's investment yield on its portfolio.

The overall economy continues to lag. Economic data continues to be mixed, but there is greater consensus among economists that the economy is not expected to grow significantly in the next 12-24 months, particularly if unemployment benefits are not extended and if the Federal deficit continues to grow. Its effects on Bay Area unemployment could serve to keep housing prices and sales tax revenues low.