



Foster City Financial Update 2Q 12/13

City of Foster City

For the Six Months Ended December 31, 2012

General Fund Reserves Likely to Finish Year at \$16.4 million; Time Has Come to Solve Structural Deficit

With half of the fiscal year in the rear view mirror, the City now prepares to set its sights on FY 2013-2014, the final year of a three (3) year process to solve the General Fund structural deficit. While revenues appear to be on a positive trend, the next 18 months will be critical in setting the City's path towards fiscal sustainability.

The City now has a clearer picture of how its revenue streams may finish for FY 2012-2013 given the first six months of tax receipts. Four of the City's five primary tax revenue sources appear that they will finish higher than expectations, and the fifth meeting its targets. Overall, General Fund revenues are expected to finish the year \$500,000 (or 1.7%) stronger than originally projected, which if continued will provide a positive trend for the following year as the City looks to balance its budget.

The General Fund is expected to finish the year with \$16.4 million in General Fund reserves, or nearly 53% of annual operating expenditures. And while expenditures appear to stay within original appropriations, the City may likely still finish the year with a \$940,000 imbalance of expenditures and transfers exceeding revenues.

Significant trends noted at the 6-month curve are:

☺ Property Taxes—recovery from the reductions in assessed valuations during the economic recession portend revenues exceeding the original forecast by \$150,000.

☺ Sales Taxes—projections based on receipts and future estimates see Sales Taxes reaching \$61,000 over original budget, however the City must carefully monitor trends amongst its top 5 sales tax generators, which account for nearly 60% of total sales tax revenues. The loss of any of those companies could derail the City's efforts towards a balanced budget in FY 2013-2014.

☺ Franchise Taxes—franchise fees are expected to finish the year with an additional \$137,500 based upon City Council approval of an increase in the franchise fee to Recology effective January 1, 2013.

☺ Real Property Transfer—this revenue category will exceed original estimates by nearly \$140,000, due primarily to the one-time transfer tax received from the sale of the Electronics for Imaging properties to Gilead Sciences. However, median home prices are increasing as demand has increased over the past year, yet there remains relatively little inventory in homes on the market.

☺ Interest Income—interest rates continue to fall. This is good if you are a homebuyer, but not so good when investing a multi-million dollar investment portfolio in fixed income securities. The yield of the City's investment portfolio has dropped from ~ 1.5% to under 1.0% since July 2012 due to the drop in Treasury rates.

Included in this report:

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Highlights:

- General Fund revenues see positive trends while the City is poised to take on the structural deficit in FY 2013-2014.
- City dedicates “boomerang” housing funds toward Affordable Housing.
- Water consumption down 22% from 2009 due in part to positive response to conservation-based water rates and rebate programs
- Housing market rebounds ... will unemployment continue its steady decline?

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GF Reserves and Structural Deficit

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As such, the General Fund will likely miss its interest income targets by about \$60,000.

While these trends are overall positive, the time has come for the City to resolve its General fund structural deficit. That long-term deficit was originally projected at \$1.6 million as the City entered FY 2012-2013. The City Council has been committed to solving that structural deficit as the City enters FY 2013-2014. Battling against the positive revenue trends are expected cost increases for pension costs as a result of the projected investment markets. While the City and its labor groups have taken some steps to mitigate those costs, and the introduction of pension reform provided via state legislation effective January 1, 2013, the City will still need to carefully manage its employee costs

which represent nearly 80% of the annual operating budget. Moreover, as the economy begins to heat up, there is a likelihood that inflationary impacts may erode the City's purchasing power, particularly for capital improvement projects and in maintenance costs. The City Council will begin its deliberations in solving the structural deficit at its Budget Study Session on January 28, 2013.

Is the City in sound financial condition? Yes! Are the revenue trends we are seeing positive? Absolutely! Is the City out of the woods yet? Not in the least! The City must stay vigilant with its revenue streams (particularly sales tax) and make wise policy decisions to ensure that the community continues to enjoy Foster City as an ideal place to live, work and play while developing a fiscally sustainable approach to balancing its budget.

Funding Affordable Housing in a Post-Redevelopment Era

December 20, 2012 was a landmark day in the era of affordable housing in Foster City. That was the day that the City's former redevelopment agency wired \$12,731,687 to the State of California (through the County Controller), turning over virtually all of its affordable housing reserves that were intended to go towards much needed affordable housing projects in Foster City and, instead, were partially used by the State to solve its budget problems by offsetting its requirements to fund education from its General Fund.

Six days later, on December 26, 2012, the County Controller wired back to the City the sum of \$3,268,301, which represented the "boomerang" of those housing funds back to the City as one of the property tax entities in the former redevelopment area. The City Council knew that a portion of those once-dedicated funds were expected to be returned to the City, and on December 17 took a bold step in dedicating 100% of those funds back to affordable housing in Foster City. As it turns out, Foster City was one of the first agencies in San Mateo County to take this action and dedicate these funds towards affordable housing. While much of the other remaining funds would be returned to the State to offset its obligation to fund education, over \$3 million was also set to be given to

the County of San Mateo. Beyond its own action to set aside the City's returned funds for affordable housing needs, the Mayor sent a letter to the County and all other cities in the county urging that they follow Foster City's lead and dedicate 100% of their returned funds towards affordable housing needs in the County.

A recent publication by Mid-Pen Housing indicates that there was demand for over 100,000 living units by families at low- to moderate-income levels in San Mateo County, and yet the inventory in the County meets just over half of that need. Foster City has been a leader for years in providing affordable housing, using redevelopment funds to subsidize the availability of below-market rate units. Now that redevelopment agencies are a thing of the past, the shared problem of providing a stock of affordable living spaces for the teachers, EMT's, bank tellers, retail salespersons, and others that provide services and make a living in this county is more acute.

The City has dedicated these "boomerang funds" towards affordable housing, and it will now need to work closely with developers, employers, housing advocates, and other government agencies to address the issue of affordable housing and allow everyone to pursue the quality of life they desire in San Mateo County.



Update on the Sustainable Foster City Plan and Development

As the City begins to implement the priority tasks included in the Sustainable Foster City Plan that was mentioned in the last edition, a keen focus will be placed on the assessment of retail and commercial needs in the community. The City and Chamber of Commerce staff will be coordinating efforts to identify opportunities to provide the right mix of retail and commercial business offerings that support Foster City residents and prospective employees. The City will also be rolling out an Online Economic Dashboard in the upcoming quarter to provide metrics as to why Foster City is a great place to live, work and play.

In the meantime, development continues in Foster City. Here is a quick update on key projects:

- ◆ 15-Acre Site - The New Home Company, LLC and its partners continue to work through the planning process to develop a site plan and conduct the necessary environment impact analyses necessary to move forward with the project. The Planning Commission is working with Planning staff and the developer to review their plans, and key meetings will take place in the coming months as the developer closes in on processing the entitlements to purchase the property from the City.
- ◆ Pilgrim-Triton - the first tenants at “The Plaza at Triton Park” moved into their new homes in January 2013, and retail spaces will be leased out in the near future. The developer of Phase IV of the project known as “Triton Pointe” received City Council approval for its development agreement and are moving forward with the planning and building permitting process to start construction in 2013.
- ◆ Gilead Sciences - Gilead continues work towards the development of the master plan for what will eventually become a 2.5 million square foot campus in the Vintage Park area north of SR-92. The Environmental Impact Report is being scoped and the review will take place over the next several months.
- ◆ Chess-Hatch - the developer in the Chess-Hatch area immediately north of 92 has indicated renewed interest in developing this site, and is completing discussions with the City in terms of a development agreement and rezoning for an office project.
- ◆ Extended Stay Hotel - the developer of a proposed 115-unit extended stay hotel is working with Planning staff and the Planning Commission to bring forward this new hotel on the former Black Angus site.



Other City Funds Healthy; Water Conservation Efforts Working

The other funds outside of the General Fund remain healthy. Items of note in 2Q 12/13 include:

- ◆ Foster City Foundation - A grant by the Smart Family Foundation of over \$175,000 was accepted by the City Council that will fund improvements at the Windsurf location on E. Third Avenue.
- ◆ City Affordable Housing Fund - as indicated on page 2, the City Council dedicated the “boomerang funds” from the former redevelopment agency’s housing funds towards affordable housing needs in Foster City.
- ◆ Self-Insurance Fund - a settlement was reached in a case that provided over \$90,000 in reimbursement of expenses incurred by the City in defending the claim.
- ◆ Water and Wastewater Funds - water and wastewater revenues and expenditures are meeting expectations included in the rate models approved by the District Board last June.

The District has noted a significant decline in water consumption as a result of the conservation-based water rates implemented in July 2010. Water consumption as a community has declined 22% since 2009, and irrigation customers have reduced their overwatering by 47%. The City Parks & Recreation Department and various HOA’s and other multi-family residential customers are to be commended for their proactive reduction in irrigation uses while still maintaining healthy, attractive landscaping, and single-family customers are making great strides to reduce their consumption.



City of Foster City

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Sustainable Foster City:

*Sustaining and
 Enhancing the
 Quality of Life in
 Foster City*



Federal and State Budgets, Housing and Unemployment Dominate Economic News

Now that 2012 and the presidential election are behind us, the economic news in recent weeks has turned to the potential impacts of the federal and state budgets, a rebounding housing market, and unemployment.

Federal Budget - Fiscal Cliff Averted ... well, maybe...

Thanks to "12th Hour" negotiations on Capitol Hill, the so-called "fiscal cliff" - the combination of lapsing tax cuts (i.e., tax increases) and spending cuts necessary to reduce the federal deficit - was averted through a compromise bill approved by Congress and the President. The tax increases were averted, however the discussions regarding the debt ceiling and sequestration (spending cuts) were "kicked down the road" to March 3, and each passing week is causing economic markets to become "edgy" towards the cliff. Leaders from both houses and both sides of the aisle will be meeting in the coming weeks to attempt to wrestle with the debt ceiling and programs that will be cut if the ceiling is reached, decisions which will have significant impacts on the availability of credit, jobs in the public sector, and social services.

Governor Releases Preliminary Budget

Governor Brown released his proposed FY 2013-2014 budget in January, which projects a balanced budget with increased funding for education due to the passage of Proposition 30—the sales and income tax increase measure. The Governor's budget continues the process of realignment of state services pushed to the local level, the most significant of which is the impact on county jails. The education increases are overshadowed by a proposed change in the funding of schools that provide enhanced revenues to those schools that serve poorer, disabled, or non-English speaking students. The San Mateo-Foster City School District and, to a lesser extent, the San Mateo Union High School District may be negatively impacted if the Governor's proposal is passed without amendment. In addition, State Democrats realize they now have the supermajority required to pass the budget and tax increases, if necessary, without the need for compromise or voter approval.

Rebounding Housing Market

At all levels - nationally, statewide, regionally and right here in Foster City - the housing market is on the road to recovery. Housing starts are up, median home prices are rising (22.5% increase in the Bay Area, 6.5% in Foster City), and foreclosure activity has begun to subside. In Foster City, median home prices for single family homes have increased by 5%, and multi-family homes rose 7.6% in 2012., with the number of sales increasing by a combined 6%, according to Jim Minkey at Today Sotheby's International Realty. The average days on the market in 2012 was 34 days, which is back to pre-2007 levels. However, inventory (the number of homes on the market) is relatively low. The commercial market is also doing well in Foster City, with vacancy rates in Foster City at around 8%, and the average asking rental rate / square foot increasing from \$3.00 in 3Q 2011 to \$4.07 in 3Q 2012, according to Colliers International. Furthermore, City staff has seen a decrease in the number of assessment appeals by commercial property owners, and prior appeals being increased back up to Prop 13 basis levels. Economists believe that the housing market is rebounding, albeit at a slow pace that will not take the market back to pre-Recession levels for many years.

Mixed Unemployment Reactions

California's unemployment rate in December was 9.8%, down from 11.2% one year ago. Foster City's unemployment rate is estimated by the Bureau of Labor Statistics to be at 4.6%, down from 5.4% in 2011. Economists are watching the unemployment trends and are concerned that the national debt ceiling issue may have a negative impact on employment at a national level. A healthy job market will do more to help local government revenues than most other trends, and this will be followed closely in the months to come.