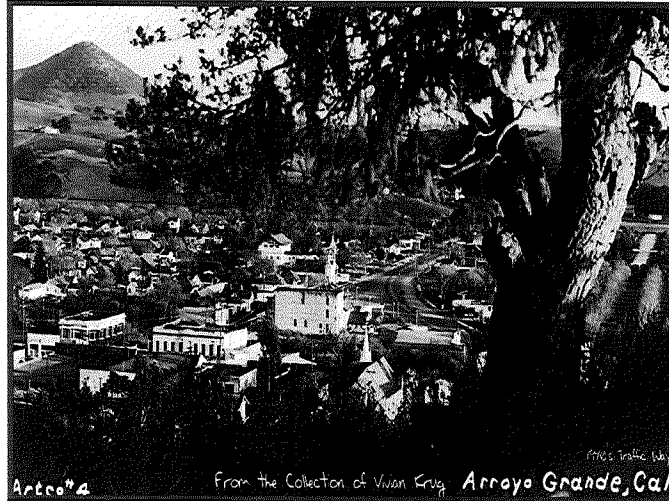


CITY OF ARROYO GRANDE



SECTION 1 *BUDGET MESSAGE*

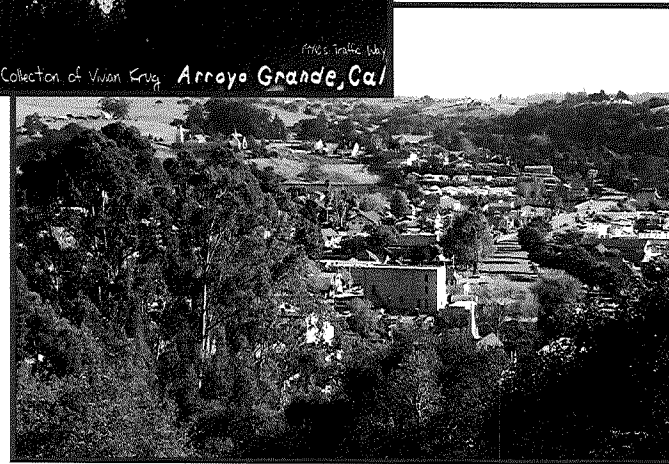
CITY OF ARROYO GRANDE



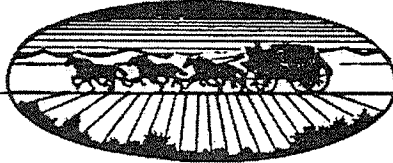
Arroyo #4

From the Collection of Vivian Krug Arroyo Grande, Cal

1910's Traffic Way



SECTION 1 BUDGET MESSAGE



July 2011

Honorable Mayor and Members of the City Council:

The staff of the City of Arroyo Grande is pleased to present the Biennial City Budget for FY 2011-12 and FY 2012-13. Budgets for all funds are incorporated into the document.

Like most cities throughout California and around the country, projected revenues for the City of Arroyo Grande have been significantly impacted by the economic downturn and employee benefit costs have dramatically increased. To address shortfalls in the prior budget, the City Council approved a comprehensive restructuring of the organization. This resulted in a decrease in positions, but maintained critical service levels through consolidation of operations and cross training of staff.

This left little ability to eliminate additional positions to address the current projected shortfall without impacting critical and basic services. Therefore, the City Council approved strategies to address the shortfall through a combination of use of reserves and employee

compensation concessions. The budget reflects the strategies approved.

Despite these operational funding constraints, the budget continues the City's commitment to utilize revenue from the 2006 Local Sales Tax Measure for the purposes intended, which primarily consist of capital improvements. In addition, the budget does not rely on any new or significant adjustment to fee revenues in recognition of the impact economic conditions have had on the community's residents and businesses.

As a result, the FY 2011-12 budget is balanced, will continue to fund high quality services provided to the community, and will invest in the future through capital improvements and maintenance activities. However, a projected deficit remains in the General Fund for FY 2012-13. As a result, the City Council was only requested to adopt the FY 2011-12 Annual Budget at this time. Staff will continue to develop recommendations for additional measures aimed at balancing the budget for the following year during the upcoming few months.

The recommended Citywide total budget for FY 2011-12 is \$22,935,373 and \$24,378,449 for FY 2012-13. Proposed expenditures for salaries, benefits, services and supplies provide the best indication of the City's management of its expenses. The total budgets for these categories for FY 2011-12 equal \$19,931,874, which represents a decrease of 4% over the prior year amended budget. Therefore, ongoing operational costs are being managed effectively and responsibly given revenue constraints.

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As part of the budget process, Departments were directed to maintain operational expenses at the same amounts budgeted in FY 2010-11. Only minor Service Level Change/Budget Amendment Requests were approved this year, primarily consisting of funding for new computer related services determined to be necessary.

One financial policy change has been proposed this year, which is to begin pre-funding retiree medical benefit costs. The budget includes funds to prepare an updated actuarial in FY 2011-12 to determine accurate long-term costs. FY 2012-13 includes an estimated expenditure amount to begin meeting this policy.

Concessions negotiated with the City's labor groups include a comprehensive reform of the City's retirement pension plan for all full-time employees. This includes a two-tiered system to reduce retirement benefits for new employees and an increase in employee payments for retirement benefit costs. Police sworn employees will pay the full employee share of these costs. Miscellaneous employees will pay all but one percent of the eight percent employee share. Three non-paid furlough days will be implemented in place of the remaining one percent.

The Biennial Budget uses the award-winning format that was initiated in FY 1997-1998. Of particular importance are the workload indicators for each department, which illustrates various activities conducted by the respective

departments and the cost and/or success of implementing those activities.

GENERAL FUND

The primary focus of budget deliberations is normally on the General Fund, which finances the majority of what are considered traditional government services. It is funded from tax revenue sources that tend to have the least flexibility to adjust funding levels to meet expenditure needs.

The budget process began with a projected shortfall of approximately \$760,000 for the General Fund in FY 2011-12. This was addressed primarily through approximately \$410,000 in negotiated reductions in employee pay and benefits and \$350,000 in use of reserves.

The total approved General Fund budget (without transfers) is \$13,428,698 for FY 2011-12. This represents a decrease of approximately 6% from the FY 2010-11 Amended Budget.

Revenues for the FY 2011-12 General Fund are estimated to meet budgeted expenditures. Revenue estimates are based upon reasonable and conservative projections, which are forecasted to be approximately \$698,270 based upon estimated actual revenues for FY 2010-11.

The two primary General Fund revenue sources, Property Tax and Sales Tax, are projected to decrease

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by 2% and increase by 3% respectively when compared to the estimated revenues for FY 2010-11. This represents a decrease of 1% in Property Tax and a 14% increase in Sales Tax from FY 2009-10. Another major impact has been to revenues generated from building activity. When combined, all building related permit fees are projected to be \$151,900, a 19% decrease from the 2010-11 amended budget.

Despite decreasing revenues, the fund balance for the City's General Fund has actually increased over the past year, which is the result of ongoing cost control measures. The projected June 30, 2012 Fund Balance of the General Fund is now \$2,887,205, which equals approximately 22% of General Fund appropriations, well above the City's minimum policy level of 15%.

The budget recommendations were prepared while the State debated the proposed elimination of redevelopment. Legislation was ultimately approved that provides the City with the option of eliminating the Redevelopment Agency or making a substantial payment to the City. Litigation has been initiated by the California Redevelopment Association. If unsuccessful, budget adjustments will become necessary since some of the Redevelopment Agency costs will need to be transferred to the General Fund.

HISTORICAL TRENDS

Staff has presented balanced budgets for the last 13 years. Given several years of financial challenges, the achievement of these balanced budgets is in large part

the result of the City Council's conservative fiscal policies, staff's adherence to those policies, and a commitment to implementing changes necessary to increase efficiency while maintaining service levels.

Over the past few years, the City has taken major steps to confront issues that could threaten long-term financial stability. These include reforming the City's retiree medical insurance program to control long-term benefit costs, approval of the local sales tax measure to fund long-term infrastructure and facility needs, joint fire operations to maintain the feasibility of a partial reserve force, economic development efforts to maintain the economic viability of the business community, and most recently reform of the City's employee retirement pension program.

However, the severity of the recession and related impacts has resulted in new challenges well beyond what was foreseen in the past. Staff is projecting sales tax to begin growing at a modest level, but to not return to former levels in the near future. A decline in property tax revenues is projected to continue. Little development activity is projected that would impact these revenue sources or reverse trends of decreasing building permit and development fee revenues.

The City's long-range financial plan, incorporated within the budget document, has been updated to reflect the current challenges. As a result, long-range projections indicate expenditures that exceed revenues and elimination of any fund balance. In reality, these

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numbers will not be accurate because they will not be allowed to exist. However, their purpose is to highlight the need to resolve existing financial trends. It will be necessary to do this either through further operational consolidation efforts with neighboring jurisdictions, additional employee concessions, and/or reductions in important services. Any approval of new commercial projects would be helpful.

SEWER FUND

Expenditures in the Sewer Fund exceed revenues in FY 2010-11, but will be balanced by FY 2011-12 due to adjustments included in the proposed budget. Fees are based on water usage. Therefore, the reduction in revenues has been closely linked to rainfall and water conservation efforts.

Total expenditures in FY 2011-12 for the Sewer Fund (Fund 612) are budgeted to be \$867,500 and projected revenues are \$928,800, leaving a projected ending fund balance of \$114,100. This is well below the City's policy goal of 60 days of operating expenses plus \$500,000. However, the fund balance is projected to gradually increase under the increases proposed and approved through the last rate study. A continued shortfall in revenues from the Sewer Facility Fund for capital projects due to decreasing development activity has added to the challenges faced by this fund to maintain adequate maintenance of the City's sewer system.

WATER FUND

Water Fund (Fund 640) revenues are estimated to be \$3,488,400 for FY 2011-12 and total expenditures are estimated to be \$3,217,411. The Ending Fund Balance for the Water Fund is expected to be \$11,129,367, well above the minimum policy goal. However, a significant amount of this funding is programmed to address needs in the 5-year Capital Improvement Program. In addition, substantial decreases in revenue due to rainfall and water conservation efforts have required adjustments in proposed expenditures, which could continue. The proposed goal is to maintain the fund balance at or above the minimum amount until the next rate study is prepared and can further assess revenue needs based upon the changing dynamics of the Water Fund.

CAPITAL IMPROVEMENT PROGRAM

The Capital Improvement Program (CIP) is funded from a wide range of revenue sources, including the General Fund, Sewer and Sewer Facility Funds, Water and Water Facility Funds, Park Improvement Fund and miscellaneous grants. While the Biennial Budget provides operational funding for a two-year period, the CIP programs project funding on a 5-year basis. Since the local sales tax measure was designed primarily to support long-term capital needs of the City, it has been the primary source of funding for general project needs. The CIP for FY 2011-12 consists of 44 new and continuing projects totaling \$10,226,153.

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Improvements to the Brisco Road-Halcyon Road Highway 101 Interchange continue to be one of the City's top priorities. Full funding is budgeted in FY 2011-12 to begin design if approval of the PA&ED and design exceptions is obtained from Caltrans on schedule. Additional funding is programmed in remaining years sufficient for debt service to finance the City's share of the project costs. The project construction schedule will be contingent upon additional funding from the State Transportation Improvement Plan (STIP).

Consistent with the priorities of the City's Critical Needs Action Plan, increases in major street projects and sidewalk repairs will continue. Reconstruction of El Camino Real and the Traffic Way extension will be completed in FY 2011-12. Recommendations of the pavement management program are fully funded in all five years of the CIP. Sidewalk repair funding is budgeted to meet the City's goal of eliminating all trip and fall hazards within the next three-year period.

Funding is programmed for debt service on the City Hall project, as well as to finance the proposed Police building project. Costs will not be determined until the feasibility study of the joint Police Building – Corporation Yard facility is completed. However, it is anticipated that additional funding will be needed from either Police consolidation savings or general obligation bonds, which would require another ballot measure.

Park projects primarily consist of lighting improvements at the Soto Sports Complex and completion of the

centralized citywide irrigation system. Continued use of Community Development Block Grant funds to complete Americans with Disabilities Act improvements is also proposed.

Given limited available resources, sewer capital project needs are proposed to be gradually phased over several years. Project priorities proposed for funding include replacement of Lift Station No. 3 and sewer improvements on the Pike, Crown Terrace, Le Point Street, and Ash Street.

Some of the proposed water projects were also phased in order to address decreases in revenues caused by the reduction in water usage. Major projects include Reservoir No. 6 construction, Oro Booster Station upgrade, Reservoir No. 7 construction, and water line upgrades on Bell Street, Faeh Street, Fair Oaks Avenue, Halcyon Road and Cornwall Street.

REDEVELOPMENT AGENCY

In August 1996, the City Council approved the formation of the Arroyo Grande Redevelopment Agency. Because sufficient tax increments were not available during the early years of the Agency, it has been necessary for the Agency to borrow funds for operational purposes. Debt has historically taken place from internal City funds.

In January 2001, the City Council approved a plan to address the Agency's operating shortfall within a 5-year period, which was successfully completed in FY 2005-06. The Redevelopment Agency's first issuance of tax

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allocation bonds was completed in FY 2006-07, which enabled the Agency to repay all internal debt and establish a positive fund balance.

The Redevelopment Agency is funding completion of the Le Point Street parking lot expansion, a portion of El Camino Real reconstruction costs, design of the proposed police building, and Peoples' Self Help Housing and Habitat for Humanity affordable housing projects. However, multiple transfers of this revenue to the State over the past few years have eliminated the ability to propose funding of any new projects.

If litigation to stop the State's proposed Redevelopment Agency elimination or payment is not successful, budget adjustments to this fund will be necessary. If litigation is successful, some modest revenue amounts may be available for future redevelopment activity.

SUMMARY

The following budget represents the professional expertise of the entire department director team for proposed City services, operations and programs. It reflects both the Fiscal Policy and budget priorities established by the City Council. The overall objective is to meet the community's needs and provide services in the most effective, efficient and responsive manner.

Staff does not recommend the budget be viewed as a plan to resolve long-term financial challenges currently facing the City due to the current nationwide economic condition. However, staff does believe strongly that it

represents the most effective and comprehensive approach to maintain financial solvency, adequate service levels, and progress in addressing long-term infrastructure and capital needs over the next year period while additional strategies can be developed and implemented.



STEVEN ADAMS
CITY MANAGER