

CITY OF ALBANY
FINANCIAL STATUS REPORT
REPORT OUTLINE
February 17, 2009

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FINANCIAL SEGMENTS

General Fund

The General Fund is the principal operating fund of the City and is used to account for all revenues that are not restricted or dedicated to specific activities. The General Fund accounts for the basic governmental services performed by the City, including:

- Public safety
- Building, planning and code enforcement
- Maintenance of public facilities and infrastructure
- Recreation, including senior and youth activities
- Administration and financial reporting

When we speak of operating or budget surpluses or deficits, it is usually in reference to the General Fund. The quarterly financial reports presented to the Council are limited to the General Fund.

At June 30, 2008, the total General Fund balance was \$4,779,000, of which \$3,209,000 was unreserved and undesignated. The unreserved-undesignated fund balance serves as an operating reserve, and as such, it is important that it is maintained at an appropriate level in relationship to annual operating expenditures.

Special Purpose Funds

The City maintains over 50 special purpose funds and, while these funds are an important segment of the City's total financial status, by definition these funds do not incur deficits. For this reason, no discussion of these funds is provided in this report.

Police & Fire Pension Fund

This fund is a fiduciary fund, which means the assets in the fund are held and managed by the City for the benefit of the participants of the Police and Fire Relief or Pension Fund. This plan is closed to new participants but as of June 30, 2008, there were 22 retired participants and 7 survivors with vested benefit in the plan. Because the City is committed to ensuring that the Fund maintains or obtains sufficient cash to pay all benefits to which the participants are entitled, the financial condition of the Fund is germane to the overall financial status of the City.

Reinvestment Agency

The Albany Community Reinvestment Agency is a separate legal entity and has the ability to issue debt independent of the City. However, the only debt incurred by the Agency is due to the City. Should the Agency's ability to repay its debt to the City become impaired, the financial status of the City would be affected. In addition to debt service payments to the City, the Agency passes to the City a portion of its tax increment revenue.

Tax increment revenue is the property tax collected on the increased assessed value of property in the redevelopment project area. This incremental revenue is retained by the agency to service the debt of the agency.

While a decline in revenue to the Agency would impact the ability of the agency to engage in economic development activity in the redevelopment area, and its ability to provide low & moderate income housing, there would not be a direct effect on the financial status of the City.

The major threat to the financial status of the Reinvestment Agency is the additional pre-emption of Agency revenues and fund balances by the State, as has been done with prior ERAF shifts of redevelopment fund to schools. In the latest ERAF shift the Albany Reinvestment Agency lost \$20,108.

Capital Improvement Plan

The Capital Improvement Plan refers to the approximately 35 capital improvement projects currently active in the City. Each project has specifically identified funding from bonds, grants, or special assessments, and, occasionally, minor General Fund revenues. There is a risk that should a project's costs exceed its funding, that the General Fund could be called upon to "bailout" the project.

GENERAL FUND BALANCE SHEET

City-wide Balance Sheet

Exhibit A – Statement of Net Assets, June 30, 2008 is taken from the June 30, 2008, audited, Comprehensive Annual Financial Report (CAFR). The objective of this statement is to provide the reader a picture of the combined assets and liabilities of the City's general fund, special funds and component agencies. It dispenses with the restriction placed upon the City's revenues and assets and combines everything in one statement, in much the same way that a public corporation presents its balance sheet.

The "Business-Type Activities" shown in a separate column, on the statement, represent the sanitary sewer system, an enterprise fund, for which the accounting rules parallel those of a commercial business, rather than those of a governmental organization.

The City of Albany balance sheet is a strong balance sheet showing net assets of \$53 million, an assets to liabilities ratio of 2.5 to 1.0, and unrestricted net assets of \$7.6 million. Of analytical significance, net assets increased 10.5% in fiscal 2008 over fiscal 2007. The recent decline in real estate and stock market values will not have a major effect on the Albany balance sheet, because the City's current assets are predominately cash or liquid securities, and the non-current assets are largely infrastructures, which are valued at cost and is not subject to market fluctuations in value.

General Fund Balance Sheet

Exhibit B – Balance Sheet – Governmental Funds, June 30, 2008 is taken from the June 30, 2008, audited, Comprehensive Annual Financial Report (CAFR). This statement provides a picture of the status of the General Fund, which is the City’s major operating fund. This is a strong balance sheet with a ratio of assets to liabilities of 5.1 to 1.0. A key financial measure on this statement is the undesignated General Fund Balance of \$3,209,486. This item is often referred to as operating reserves and the companion question is how much reserve should a City have. There is no simple answer to this question, as it is influenced by factors that include:

- size of the budget,
- volatility of primary revenues,
- liquidity of reserves, and
- officials’ tolerance for risk and uncertainty.

A broad rule-of-thumb would be that operating reserves should equal between 15% and 35% of the annual operating expenditures. The Albany reserves of \$3,209,486 are equal to 21% of the fiscal year 2007-08 General Fund expenditures of \$14,963,976.

In evaluating the City’s reserves, two reservations must be factored into the evaluation. First, although the General Fund assets are relatively liquid they are not 100% convertible to cash on short notice. Second, that from time to time informal advances are made to other funds such as capital projects, joint venture projects such as the Gilman Ballfields, Ocean View Park sports fields, repair of the Community Center tower, and reimbursement grants such as the fire aerial truck. In February 2008 the State delayed Highway Users Taxes of \$26,638 due the City for six months.

Unrecorded Liabilities

Often when entities experience financial difficulties, there comes to light unrecorded or unfunded liabilities that exacerbate the financial problems. Examples are accrued vacation, sick leave buy-back obligations, self-insurance reserves, pension contributions, termination benefits, and post employment benefits. We have followed a policy of recording and funding all determinable liabilities, and the City is not obligated for any post-employment benefits. While the unknown and unanticipated can never be eliminated, we are confident that the City has no significant unrecorded liabilities.

GENERAL FUND CHALLENGES

Declining Revenues

- Property Taxes are approximately 35% of the General Fund revenues and are the largest single revenue source in the City. In recent years we have experienced an annual growth in property tax revenue of approximately 8% per year. This growth in revenue has exceeded the inflationary growth in cost of living, which has been approximately 2% to 4%. As a result, the City has been able to balance its operating budget, fund reserve accounts, and initiate new activities and programs.

For Albany, the growth in property tax revenue has been a result of the maximum 2% annual increase in assessed value allowed by Prop 13, reassessment of property to market value when sold, and construction of new buildings.

We now face a situation where property values have declined and some properties have been reassessed at lower values. There were 167 transfers of title in fiscal 2007-08 - a decline of 20% from the 207 transfers in fiscal 2006-07. There have been no permits issued for major construction projects in the current fiscal year.

It is clear that growth in property tax revenue in fiscal years 2008-09 and 2009-10 will be significantly lower than in prior years. While some cities in Alameda and Contra Costa Counties may experience a decline in revenue, we believe that Albany will continue to have modest growth, and we have budgeted for increases of 2% in both 2008-09 and 2009-10.

- Property transfer taxes have been a major revenue source for the City, but unlike the annual ad valorem and parcel taxes, these taxes fluctuate significantly from year to year. The current tax rate is \$11.50 per \$1,000 of value; this rate was raised from \$8.50 in 2002. A ballot measure to raise the rate to \$14.50 failed in 2008.

The property transfer tax revenues for the last seven fiscal years were:

2001-02	\$ 810,357
2002-03	958,047
2003-04	1,813,666
2004-05	1,860,784
2005-06	1,559,959
2006-07	1,456,672
2007-08	1,184,635

We have budgeted revenue of \$921,375 for 2008-09 and \$1,000,000 for 2009-10.

- Sales tax revenue to the City was boosted significantly by the opening of the Target store in 2004, and revenues have remained relative stable through the current economic downturn. The sales tax revenues for the last seven fiscal years were:

2001-02	\$1,410,461
2002-03	1,339,720
2003-04	1,356,985
2004-05	1,599,449
2005-06	2,042,834
2006-07	2,242,377
2007-08	2,182,934

We have budgeted revenue of \$2,036,048 for 2008-09 and \$2,066,702 for 2009-10.

- Vehicle License Fees are received in two forms. Actual fees collected by the State are distributed to the Counties and Cities based on population. Fees received by the City of Albany in the last four years were:

2004-05	\$368,012
2005-06	109,565
2006-07	97,068
2007-08	74,425

The second portion of motor vehicle license fees is an in-lieu payment received from the State, in the form of property tax revenue. These revenues for the last four years were:

2004-05	\$ 898,304
2005-06	1,111,649
2006-07	1,147,174
2007-08	1,224,379

The future of these vehicle license fees is uncertain and will remain so until State budgetary problems are resolved. The revenue collected by the State in October and November was not sufficient to cover the State's administrative fees, resulting in zero distribution to the counties and cities. To date, in-lieu payments have been made as scheduled.

We have budgeted vehicle license fees payments of \$52,293 for both 2008-09 and 2009-10. We have budgeted in-lieu payments of \$1,280,211 for 2008-09 and \$1,305,815 for 2009-10.

- Earnings on Investment are a function of the amount of funds we have available to invest and the current interest rates. The City's reserves and temporary excess cash balances are invested in two pooled investment funds; the Local Agency Investment Fund administered by the State Treasurer, and CalTrust, a joint powers agency. These pooled funds may incur market losses, which will in turn reduce the earnings distributed to the depositing agencies. Current yield on our investments are approximately 2.5%, but we anticipate these yield falling in the near future.

In addition to the falling interest rate, the City will have less funds to invest than in recent years. General Fund earnings were \$480,579 in fiscal 2007-08. We have projected earnings of \$228,517 for 2008-09 and we have budgeted \$252,125 for fiscal 2009-10.

Increasing Revenues

- Race Track Tax revenue has been declining for the past several years as attendance at Golden Gate Fields races has declined. Having the race track in the City results in the City receiving revenue from racing events at the State Fair, county fairs and other thoroughbred race tracks in the state. The closing of Bay Meadows race track in San Mateo has resulted in the number of race days at

Golden Gate fields increasing from 127 days in calendar 2008, to 157 days in calendar 2009.

Race Track tax revenues for the last four fiscal years were:

2004-05	\$431,437
2005-06	429,032
2006-07	387,533
2007-08	357,457

We have budgeted revenues of \$399,886 for both 2008-09 and 2009-10.

- Tax Increment Pass-Through – Beginning in fiscal 2008-09 the Reinvestment Agency is required to pass through a portion of its tax increment revenue to agencies that levy taxes in the redevelopment area. This requirement results in less revenue for the City, all segments combined, but it also means additional unrestricted revenue to the General Fund. The additional revenue projected for 2009-10 is \$22,773.

Increasing Expenses

- Contractual wage and benefit increases set for firefighters in fiscal 2009-10 amount to approximately \$166,000 or 7% of Fire/Paramedic payroll, excluding overtime.
- Wage negotiations for employees represented by SEIU are scheduled to begin in March 2009. The current SEIU agreement expires March 31, 2009. The current agreement with the Albany Police Officers' Association expires October 31, 2009. The salaries of management personnel are customarily reviewed prior to the beginning of the fiscal year, July 1.
- PERS retirement contribution rates are scheduled to increase only modestly in 2009-10, and for some groups may decline, based on the latest communication from Cal PERS. However, Cal PERS has alerted member agencies that contribution rates for 2010-11 may increase as much as 2% to 5% of payroll. This equates to an increase in the contribution rate of as much as 17%.
- Medical insurance rates have continued to increase at double digit rates, and the City has implemented available cost savings measures such as reduction of the number of health plans available to members and increasing the member's co-pay per visit and for prescriptions. We have assumed a health insurance premium increase of 9% for 2009-10.
- Facility and fuel costs are largely uncontrollable by the City. These costs will increase modestly as a result of the expansion of facilities currently in progress, and the increase in the number of vehicles operated by the City.

- Infrastructure maintenance costs increase as the infrastructure assets age and as new requirements are imposed by various regulatory agencies.

New Discretionary Activities and Projects

- General Plan Update – The City is required to complete an update of its General Plan by December 31, 2010. While completion of the update is not optional, the City has significant discretion as regarding the resources employed in the update, and this will be a critical budgeting decision.
- Economic Development – In fiscal 2008-09 the City instituted activities, including the hiring of consultants, to formalize and increase its efforts to foster economic development in the City. As budgets are prepared, the City will have to decide whether to continue these activities, and the sources of funding for these activities.
- Urban Forestry Initiatives – This program began in fiscal 2006-07 and has proven to be a popular quality of life and sustainability activity for the City. As budgets are prepared, the City will have to decide on the level and sources of funding of this activity.
- Recycling Programs – In recent years the City has instituted programs and allocated staff time to expanding recycling in the City. These efforts have been largely funded by grants and have little impact on the General Fund. Our presumption, at this time, is that grant funding will continue to be available for these programs.
- Expanded Street Sweeping – In fiscal 2007-08 the City expanded its program of scheduled street sweeping by an outside contractor. Funding for this program comes from a trash collection surcharge collected by Waste Management and remitted to the City. In addition to the direct funding of the street sweeping, the institution of parking restrictions to facilitate the street sweeping has produced increased parking fines revenue. Staff has looked upon this revenue from parking fines as temporary bonus revenue that will decline as residents become accustomed to the restrictions.
- Community Organization – A community engagement specialist has been hired in the Police Department in a demonstration project for neighborhood organization and preparedness, utilizing the savings from approved but vacant positions in the Police Department. If there is a decision to continue this position beyond fiscal year 2008-09, either non-General Fund funding would have to be obtained or the General Fund budget would have to be revised.
- Public Art – In fiscal 2007-08, the City established a public arts permit fee for new construction. This activity requires some administrative staff time and requires the application of the arts permit fee to certain City capital projects.

- Integrated Pest Management. In 2008, the City Council adopted an ordinance establishing an integrated pest management program. While the City uses IPM policies and procedures, funds for the additional staffing envisioned in the program development are not contained in the 2008-09 or 2009-10 budgets.

GENERAL FUND FORECAST

- **Projection FY 2008-09** – Exhibit C is the Statement of Revenues, Expenditures and Changes in Fund Balances for the first six months of fiscal 2008-09, ended December 31, 2008. This statement contains a projection of revenues and expenditures for the full 2008-09 fiscal year. The projection was prepared by combining the actual results for six months with current estimates of revenues and expenditures for the last six months of the year.

The projection is for a positive bottom line of \$33,256. This net excess revenue exceeds that of the revised budget by \$19,981, and it exceeds the originally adopted budget net excess of \$4,625 by \$28,631. Both the projection and the revised budget reflect a reduction of previously approved transfer to Reserve Funds of \$25,000. If these transfers are restored, the projected net excess revenue will be \$8,256.

A positive net bottom line for the fiscal year is largely dependent upon receipt of revenues. Two volatile and difficult to forecast revenues are sales taxes and property transfer taxes. Sales taxes will decline as the local economy slows, but as noted in earlier discussion in this report, the largest sales tax revenue producers in the City have fared well during the economic downturn, and for the first half of the year produced revenues above the budget. Property transfer taxes are extremely difficult to forecast, and while they have dropped 29% from the first six months of fiscal 2007-08, they are only 1% below the budget for 2008-09, and may exceed the budget for the fiscal year.

A new full year projection will be made after completion of the third quarter, March 31, 2009, and at that time, additional modifications of expenditures and transfers will be recommended, as required.

- **Budget FY 2009-10** – Exhibit D is the original adopted budget for fiscal 2009-10, and the current projection for fiscal 2009-10. The bottom line of the projection is a negative \$656,612, which is \$440,498 greater than the adopted budget deficit of \$216,514.

The increase in the projected deficit is largely due to a decline in projected sales tax revenue of \$151,080 (7%), a decline in property transfer and other taxes of \$168,808 (4.6%), and a decline in earnings on investments of \$116,075 (31%). At the time the adopted budget was prepared, it was anticipated that there would be a turn around in the economy in 2009-10, but we are now anticipating no recovery of revenue streams in the first half of fiscal year 2009-10.

The Finance Department is exploring options to balance the 2009-10 budget. In addition, the City Administrator is recommending an organizational analysis to assist in developing recommendations for cost savings.

POLICE AND FIRE PENSION STATUS

Investment Losses

The market value of securities held in the Police and Fire Relief or Pension Fund are as chronicled below:

June 30, 2006	\$14,462,199
June 30, 2007	14,799,584
June 30, 2008	12,306,684
September 2008	10,939,280
November 2008	9,122,981
December 2008	9,595,725

The assets of the pension fund are invested in mutual funds managed by Dodge & Cox, Investment Bankers. The Dodge & Cox Equity funds have experienced losses exceeding 40% of their market value, in the last 12 months. The bond fund loss of value was less than 1%, but the quality ratings of securities held in the bond fund have declined. These losses are largely attributable to the general decline the market value of securities both national and internationally. However, the Dodge & Cox funds under-performed the market in 2008, in contrast to their 20-year history of consistently outperforming the market.

Contribution Requirement

Prior to June 30, 2008, the fund was fully funded on an actuarial basis, and no contributions were required to ensure the ability of the fund to pay all vested benefits. However, the investment losses of 2008 caused the Fund to have an unfunded liability of \$1,319,000 at June 30, 2008. Subsequent losses after June 30, 2008 will have increased the unfunded liability. As a result, the City will resume contributions to the plan from the Pension Property Tax Fund, with a contribution of \$500,000 in fiscal 2008-09. An actuarial study will be performed as of June 30, 2009, and this study will determine the annual contribution required to fund the unfunded liability over 15 years. We anticipate that the current pension property tax override will provide sufficient funds for the required contribution to the Fund.

REINVESTMENT AGENCY STATUS

Balance Sheet

Exhibit E – Statement of Net Assets, is the June 30, 2008 balance sheet of the Reinvestment Agency. The Agency is an independent entity whose assets are segregated from those of the City; however, the Agency is fully owned by the City and all of the debt of the Agency is owed to the City.

The financial status of the Agency is strong, with assets of \$1,408,889 and liabilities of \$798,875, it has unrestricted and uncommitted equity of \$610,014, as of June 30, 2008. The assets of the Agency are invested in LAIF, and have not suffered a major loss of value in the current economic crisis.

Investment Earnings

Because the assets of the Agency are invested in LAIF, and, as discussed earlier in this report, the LAIF yield is currently approximately 2.5% and expected to decline, investment earnings for the Agency will decline significantly in fiscal 2009. Earnings for fiscal 2008 were \$51,559.

Tax Increment

Tax increment revenue is a function of the change in assessed value of property in the redevelopment area. We expect the assessed value of property to remain stable until substantial property is sold or new developments are constructed. There are no active permits for substantial construction in the redevelopment area at this time.

Net tax increment revenue for fiscal 2008 was \$381,295. The Agency is required to pass through to taxing agencies 25% of the tax increment received. The City is one of the affected taxing agencies, and we have budgeted revenue \$22,773 for the City in fiscal 2009.

CAPITAL IMPROVEMENT PLAN

Capital Improvement Bonds

- Measures F&C – Measure F authorizing the issuance of \$14,500,000 of general obligation bonds to fund Park & Recreation projects, Street Projects and renovation of the Civic Center Complex, was approved in 2004. Bonds of \$8,000,000 were issued in 2004, and bonds of \$6,500,000 were issued in 2007. Exhibit F is a summary of the projects funded by these bonds, and the expenditures of funds through June 30, 2008. As of June 30, 2008, funds totaling \$706,805 remained in reserve for additional projects.

Funds of \$6,500,000 have been allocated for the Civic Center renovation, and an additional \$5,000,000 was allocated from general obligation bonds authorized by Measure C in 2006 and issued in 2007.

- **Measure R** – Measure R, approved in 1996, authorized the issuance of \$6,230,000 of special assessment district bonds for the acquisition of land to be held as open space, development of recreation fields, and creek restoration. Exhibit G is a summary of the expenditure of these funds from issuance of the bonds in February 1999 through December 2008. As of December 31, 2008, the remaining uncommitted funds were:

Open Space	\$1,358,087
Recreation Fields	274,798
Creek Restoration	447,858

Measure F 2006

Measure F 2006, approved in 2007, provides for a parcel tax of \$96.00 per equivalent residential unit (ERU), adjusted annually for inflation. The tax produces annual revenue of approximately \$800,000, which is to be used for storm drain improvements and repairs, and street pavement maintenance.

In 2008 a major storm drain project was begun to correct flooding on Neilson and Curtis Streets. The project is budgeted to cost \$2,887,543. Certificate of Participation bonds (COPs) will be issued to fund this project. Annual debt service will be approximately \$400,000, and Measure F parcel tax revenues will be pledged to cover the bond payments.

Suspension of committed funding

The State fiscal/budget crisis has resulted in the suspension of grant payments under the State's Park Bonds (Prop 12 & 40). These suspensions are presented by the State as temporary, but Albany City officials chose to advance up to \$94,000 for completion of the improvements to the Ocean View Sports Fields, from Measure R funds, so as not to delay completion of the project.

The Lower Codornices Creek restoration project is a joint project of the Cities of Albany and Berkeley, and the University of California. The budget for the project is \$5,424,067, of which \$2,100,000 is funded by a River Parkways Grant from the California Resource Agency. Disbursement of funds for the River Parkways Grant has been suspended due to the State fiscal/budget crisis. Work on the project has been suspended, but the City has advanced funds of approximately \$470,000 to the project, and these funds will not be reimbursed until grant payments are resumed.