

To: Mayor & City Council  
From: City Manager  
Date: May 29, 2007  
Subject: Fiscal Year 2007-08 Proposed Operating Budget

The City of Monterey, like nearly every other city, continues to face the dual challenge of increased competitiveness for qualified staff (“human infrastructure”), and increased need for renewal of our streets, sewer, storm drains and facilities (“capital infrastructure”). Past Council actions and the budget plan before you address these challenges in a variety of ways:

Human Infrastructure:

- ✓ Reclassify/salary adjustment of 39 miscellaneous employees in 2006;
- ✓ Significant increase in police salaries in 2006;
- ✓ Currently negotiating with firefighters;
- ✓ Second major reclassification/salary adjustment process currently underway;
- ✓ Reorganization of Public Works and Community Development Departments currently underway.

Capital Infrastructure

- ✓ Streets – implemented construction truck impact fee in 2006;
- ✓ Sewers – staff currently studying a possible revenue bond issuance with corresponding sewer rate increase;
- ✓ Facilities – budget includes \$900,000 set aside into facility renewal reserves for major City facilities.

Because of the financial impact of these challenges, the 2007-08 (FY 08) Proposed Operating Budget for the City of Monterey presented here is in a temporary deficit mode. In particular, the strategic decision to increase police salaries last Fall was the main factor creating a projected \$1.1 million dollar deficit in FY 08. However, Council was aware of this circumstance and decided this move was necessary from a public safety standpoint because staffing levels in the Police Department had dropped to unacceptably low levels.

In addition, we believe this approach was reasonable because it is expected that the new Cannery Hotel, scheduled to open in May 2008, will bring the City’s General Fund back into balance by FY 09. The proposed General Fund operating budget for FY 08 is summarized in the chart below.

**General Fund Proposed Operating Budget  
FY 2007-08**

(millions)

Operating revenues	\$51.45
Operating Expenditures (net)	(52.92)
Transfers (net)	0.36
<b>Net Operations</b>	<b>(\$1.11)</b>

The FY 08 budget proposes additional investment in several areas listed below. A detailed discussion of these and other items appears later in this report.

1. Extend overfill Police Lieutenant for COPPS	\$195,648
2. Increase Fire operations overtime budget	30,000
3. Additional greenbelt maintenance	18,500
4. Sr. Custodian position upgrade	6,657
5. Building maintenance projects	428,605
6. Library computer time management system	20,000
7. Heritage and cultural tourism supplies	12,500
8. Conference Center sales software	65,000
9. Additional funds for group sales, destination marketing and housing services	44,494
10. Lighthouse Ave. historic survey	20,000
11. Parking Attendant position upgrade	49,478
12. Capital Facilities Renewal Reserves	900,000
13. Economic Uncertainty Reserve	435,000

**General Fund Revenues**

General Fund revenues are estimated to be \$51.5 million in FY 08, which would be up 3.1%, or \$1.6 million over the current year's revised estimates. For all funds, operating revenues are estimated to be \$93.5 million, up 7% from the prior year. Following is a discussion of the major General Fund revenue sources.

**Transient Occupancy Tax**

The current fiscal year has shown fairly robust growth rates of 6.5% so far. This is above the projected 4.9% growth rate. However, we are not adjusting the estimate at this time due to a large remodeling project at a major hotel that is taking rooms offline for a time. A strong desire to travel, despite high gasoline prices, and additional tourism marketing dollars approved by Council have been important factors in this growth.

Transient Occupancy Tax is still the City's single largest revenue source making up 25% of the General Fund estimated revenue total for next year. As shown in the following

table (which includes both General Fund and Neighborhood Improvement Program portions), TOT is projected to increase 4% next year.

**TOT Growth**  
(General Fund and NIP)

Fiscal Year	Total TOT (millions)	Growth Rate
1999-00	\$14.3	10.8%
2000-01	14.6	1.4%
2001-02	12.9	-11.5%
2002-03	12.5	-2.7%
2003-04	12.8	2.4%
2004-05	13.6	6.1%
2005-06	14.2	4.1%
2006-07 est	14.9	4.9%
2007-08 est	15.5	4.0%

Sales Tax

Sales tax revenue in FY 08 is estimated to be \$7.5 million (not including Prop. 172 safety portion), making it the third largest General Fund operating revenue source after TOT and property tax (15% of projected revenues). This figure includes both sales tax revenues and the "Property tax in-lieu of Sales tax" revenue source created by the passage of Proposition 57, which reduced the City's sales tax by one-quarter and replaced it with a like amount of property tax revenues. This sales tax estimate represents an increase of 3.0% over the revised projection for the current year.

The Sales Tax estimate reflects fairly modest growth despite a number of new projects in the works such as PF Changs, Pottery Barn and Trader Joe's. We are being cautious with this growth estimate because this revenue source has not met expectations over the last couple of years. We believe part of this overall weakness in Sales Tax growth is due in part to leakage to both surrounding markets and the internet. This trend is likely to grow in the future. This makes it crucial that for major sales tax centers such as Del Monte Center and Cannery Row, careful economic development planning should take place.

### Sales Tax Growth

<b>Fiscal Year</b>	<b>Sales tax (millions)</b>	<b>Growth Rate</b>
1999-00	\$6.7	14.7%
2000-01	7.3	8.5%
2001-02	6.7	-7.7%
2002-03	6.3	-5.5%
2003-04	6.3	-0.7%
2004-05	* 6.9	9.4%
2005-06	* 7.0	1.6%
2006-07 est	* 7.3	3.8%
2007-08 est	* 7.5	3.0%

\* Includes Property Tax in Lieu of Sales Tax

### Property Tax

Property tax receipts have continued to increase, albeit at a slower pace. Based on receipts so far this fiscal year, we anticipate property tax receipts will be right on target with projections at \$7.5 million. For FY 08 property taxes are projected to increase another 4.9% to \$7.9 million. This modest projected growth rate is a reflection of the general slow-down in the real estate market. Property tax generates a little more than 15% of all General Fund revenues.

### Property Tax Growth

<b>Fiscal Year</b>	<b>Sales tax (millions)</b>	<b>Growth Rate</b>
1999-00	\$3.4	4.7%
2000-01	3.7	8.4%
2001-02	3.9	4.7%
2002-03	4.1	6.8%
2003-04	4.4	7.4%
2004-05	* 6.4	44.4%
2005-06	* 7.3	14.3%
2006-07 est	* 7.5	2.9%
2007-08 est	* 7.9	4.9%

\* Includes Property Tax in Lieu of VLF

## **General Fund Expenditures**

Overall for FY 08, proposed General Fund operating expenditures amount to \$55.2 million. This represents an increase of 5.3% from the FY 07 amended budget and a 6.9% increase over the original FY 07 budget. After allowing for estimated budget savings and one-time items paid for with non-operating money, the net operating expenditure budget is \$52.9 million. The total proposed FY 08 operating expenditures for all funds is \$94.8 million, which represents an increase of 3.5% from the FY 07 amended budget.

It is worth noting that a large number of position reclassifications and salary adjustments, and the Public Works/Community Development reorganization will be presented to Council over the next several months in separate staff reports from this budget proposal. However, an estimate of the funding necessary to implement these proposals is included in this budget package.

## **Budget Highlights**

The following discussion highlights some of the more significant programs and budget issues that are included in the proposed budget for 2007-08.

### **Police Department**

The Police Department is requesting \$195,648 to allow for a one-year extension of the Police Lieutenant overfill in order to manage and support the COPPS community policing program. This new program has been very successful as there has been more positive police/community interaction in the past year than ever before. Most importantly, through the COPPS program we have been able to make progress on dealing with issues that concern the community in ways that may not have been possible before.

Our original hope was that the COPPS program could get up and running within twelve to eighteen months, and that by then it would not need oversight at the management level. However, with the influx of new personnel into the Department, the Lieutenant position has continued to be very important to the long-term success of this program. Therefore, staff is recommending that the overfill of this Lieutenant position be extended one additional year.

### **Fire Department**

The proposed budget includes an additional \$30,000 for overtime expenses, bringing the total Fire operations overtime budget to \$432,500. Staff is currently analyzing Fire overtime usage however because it continues to increase, even with the restoration of two "frozen" firefighter positions and the recent addition of three captains. So it is possible that the amount budgeted for FY 08 overtime in the Fire Department may be low. After this matter has been studied in more

depth, staff will return to Council for a recommendation and/or budget adjustment if necessary at a later date.

This budget also includes \$34,000 for necessary fire fighting equipment such as portable radios (\$12,000); replacement jackets (\$3,000); and fire hose replacement and maintenance (\$6,000).

#### Assistance to Firefighters Grant

The City of Monterey Fire Dept and up to 23 other Monterey County fire agencies are eligible to receive radio communications equipment through an Assistance to Firefighters Grant award from the Dept of Homeland Security totaling \$918,250. This is included in the FY 08 budget in a special revenue fund for this program. The total grant award includes a federal share of \$734,600 (80%) plus \$183,650 (20%) in matching funds. As the host agency for this multi-jurisdictional grant, the City of Monterey will be exempted from the matching funds requirement, and therefore, will incur no expense. In exchange, Monterey will provide staff time to procure and distribute equipment and to administer receipt of funding and related payments.

### **Public Works Department**

#### Contract Greenbelt Maintenance

The budget proposal includes an additional \$18,500 for contract greenbelt maintenance to take care of projects such as trimming the eucalyptus trees at El Estero, pitch canker removals and an increase in the daily California Department of Forestry rates. This will bring the total contractual services account in the Forestry Division to \$195,000, which is still below what was spent in FY 03 and FY 04.

#### Senior Custodian position upgrade

The Public Works Department has requested the upgrade of one Custodian position to a Senior Custodian. This will help them address staffing oversight issues and manage the custodial function better. The cost of this upgrade is \$6,657.

#### Building Maintenance Projects

The proposed FY 08 budget includes \$428,605 in building maintenance projects related to a variety of City facilities. This amount is substantially higher than the "normal" range of approximately \$250,000-\$300,000 annually. Staff believes this level of funding is necessary because during the budget cutback years some maintenance items were deferred due to lack of funds. Some of the proposed projects include Library lighting upgrade for energy savings (\$29,300); painting of El Cuartel (\$45,000); and replacement of 1000 gallon hot water heater at the Sports Center (\$89,000).

## **Library & Museum Departments**

### **Public Computer Time & Print Management System**

The Library is requesting \$20,000 in one-time funds to upgrade and enhance their public computer time and print management system. This system will provide better customer service to the many library patrons who need access to a computer and printer and don't have one of their own. It is also expected to save Library and Information Resources staff time and money because the current system has been unstable and expensive to maintain.

### **Heritage and Cultural Tourism**

The Museum is requesting \$12,500 for supplies and services for brochures and staff travel expenses related to heritage tourism and the Preserve America program. Also included in this funding is a possible co-sponsorship of the California Cultural and Heritage Tourism Council, a live enactment of the 1849 California Constitutional Convention, and design and development of new exhibits in the Old Monterey Jail.

### **Preservation and Conservation**

Also included in this proposal is \$7,707 for supplies and conservation services to reestablish a program of evaluation, preservation and repair of the City's valuable art and historical artifact collection.

## **Public Facilities Department**

### **Conference Center**

This budget proposal includes several one-time items to enhance the Conference Center's programs and facilities including new software to better manage sales (\$65,000); new tradeshow booth displays (\$10,000); public area furniture and rug replacements (\$35,000); recycling containers for Serra Ballroom and public areas (\$10,500); Conference Center painting (\$25,000); and landscape maintenance (\$6,789). It is important that we maintain the Monterey Conference Center facility as a very high level so that we continue to be a premier conference destination.

At the April 17 Council meeting, the elimination of the Sales and Marketing Director position was approved. Oversight of this division was transferred to the Conference Center Manager. This budget proposal includes the upgrade of the renamed Conference Center General Manager to a level 4% above the Harbormaster and Parking Superintendent positions to recognize these additional responsibilities. The additional cost of this action (approximately \$21,300 annually) is more than paid for by the elimination of the Sales Manager position. The overall net savings is over \$100,000 annually.

### Visitor Marketing Program

Included in this budget proposal is a request for \$44,494 in additional “fair share” funding for the Monterey County Convention and Visitors Bureau’s (MCCVB) destination marketing, group sales and housing services programs. This would bring the City of Monterey’s total investment to \$850,819. Staff believes that much of the recent growth in TOT can be attributed to this increased investment. Fair share contributions from all participating agencies in the County to the MCCVB will be combined with the new tourism business improvement district “self-assessment”. This greater level of funding is expected to enable the MCCVB to better compete with other destination areas for valuable tourist dollars.

## **Community Development Department**

### Planning

Some of the items recommended for approval in the Planning Division budget include an increase in fees by the Department of Fish & Game for environmental review documents (\$9,250); mixed-use neighborhood design guidelines for N. Fremont Street (\$13,333 – 1/3 in General Fund, the other 2/3 in Housing Fund budget); and funds to complete the historic survey of Lighthouse Avenue and lower New Monterey (\$20,000).

### Building Safety

The Building Safety & Inspection Division is proposing a document conversion program for scanning its many plans and documents. This will save physical storage space and make these documents easier to retrieve. Staff proposes funding the projected \$29,340 cost of this conversion by assessing an archiving fee when plans are submitted for checking. The proposed fee is \$3 per plan sheet submitted.

## **General Government**

### Business Transformation

In 2005 the City Council authorized three contract positions so help implement the many business transformation projects that are planned to streamline and make processes more efficient. These position were originally three-year positions through June 30, 2008. One of these positions, the Systems Analyst, became vacant so at mid-year Council authorized the extension to 2010 to help with the recruitment process, and because while much has been accomplished, there is more to do.

Included in the proposed budget is a request for the extension of the other two contract positions (Assistant City Clerk and Systems Implementation Manager) as they also are critical to our business transformation program. The recommendation is to also extend these positions two additional years to June 30, 2010. These positions are critical because for example, while we will have

made enormous progress on our cost accounting and content management programs, we believe that they will not be fully deployed and integrated throughout the organization by June 2008. In addition, substantial work will remain related to the integration of our various data systems (easing access to data and eliminating redundant data entry, with the various problems that come with it) and the deployment of various electronic commerce and eGovernment tools. We will also want to make more progress on utilizing our existing human resources management system, further deploying the workflow support tools that will be embedded in the soon-to-be purchased electronic content management system, and purchasing/deploying a “business intelligence” platform that will help us mine the vast array of enterprise data that will be at our disposal. The total cost of these to positions is \$213,000 annually.

## **FINANCIAL OVERVIEW – OTHER FUNDS**

The City maintains a number of funds other than the General Fund to account for the revenues and expenditures of activities that are separate from the General Fund for either legal or accounting purposes. A brief overview of the FY 08 budget picture, and some of the proposals for some of the more significant of these funds follows.

### Presidio Public Works Authority Fund

The Presidio Public Works Authority Fund accounts for the operational activities, capital projects, and revenues associated with the municipal services contract between the City and the U.S. Army at the Presidio of Monterey. Services provided to the Army include maintenance of buildings, streets, sewers, storm drains and water systems and other special projects. The proposed FY 08 operating budget includes an estimated payment to the General Fund of \$750,000 for the overhead and administrative support the City provides to support this contract. This includes not only the normal operational budget for overhead, but also an additional estimated \$500,000 for Presidio projects expected above and beyond our regular maintenance contract.

### Storm Water Utility Fund

Projected revenues of \$1.1 million in the Storm Water Utility Fund fall short of the \$1.2 million in proposed operating expenditures in this fund for FY 08. So for the first time since the storm water utility fee was implemented, the General Fund will have to subsidize the operations of the Storm Water Fund by \$96,000. In addition, the Storm Water Fund has not been able to fund its capital projects for some years now. These projects have been funded with either General Fund or NIP monies as these funds are available. State and Federal requirements for public education, testing of storm water flows, and continued implementation of best management practices have significantly increased the budget in this fund, without a currently identified revenue stream to offset these new costs. Increasing the Storm Water Utility fee would require a vote of the people because

under Proposition 218 storm water fees are considered property-related fees, unlike water, sewer or refuse fees.

#### Sewer Line Maintenance Fund

The Sewer Line Maintenance Fund will generate an estimated \$1.4 million in FY 08 which exceeds the \$1.2 million in projected operating expenditures. In addition, the CIP budget includes \$400,000 for capital needs, which will come from this small surplus and reserves. In the past, Sewer Fund fees generated enough revenue to pay for operating costs as well our “pay-as-you-go” capital program. However, as costs have risen and the sewer maintenance fee has not, Sewer Fund revenues now pay for operations and only a small portion of capital maintenance.

To address this infrastructure funding shortfall, staff has begun to analyze the pros and cons of issuing sewer revenue bonds to implement a \$14 million sewer capital renewal/replacement program. While financing capital needs with debt requires careful consideration, given the size of the sewer renewal and replacement program, and the importance of minimizing the potential for sewer leaks, staff believes the current pay-as-you-go method is not getting the job done. In order to pay for the approximately \$1 million annual debt service, sewer fees would likely have to be increased. Currently the rate is 46.7% of the Monterey Regional Water Pollution Control Agency (MRWPCA) sewer fee, which generates most of the \$1.4 million in revenue mentioned above. Staff is still studying this matter and will return to Council in the future with options and a recommended course of action.

#### Cemetery Fund

Projected Cemetery revenues of \$249,600, and an operating budget of \$308,551 results in a \$59,000 operating shortfall that the General Fund will have to subsidize. This budget includes \$20,000 for the second phase of installing irrigation lines at the Cemetery that staff believes over time will produce operational efficiencies. In addition, the Cemetery Fund will require an advance from the General Fund of \$77,948 to cover the debt service payments on the columbarium. This amount will be recorded as an interfund loan as it is projected that over time sales of all niches from the columbarium will far exceed the total debt service costs. However, since the columbarium loan will be paid off more quickly than all niches will be sold, there will be a need for advances from the General Fund in the meantime.

#### Marina Fund

The Marina Fund's proposed budget of \$1.9 million includes debt service on state loans in the amount of \$468,627 and \$35,000 for a consultant to obtain all necessary permits for a future Marina dredging project. In addition, the Marina Fund will transfer \$136,591 to the General Fund next year to assist with the expense of maintaining Wharf II, and \$186,200 to the Parking Fund for parking

support. Total estimated revenues for FY 08 in the Marina Fund are expected to be \$2.1 million.

#### Parking Fund

The proposed \$5.8 million Parking Fund FY 08 budget includes \$966,557 in facility lease payments for the Cannery Row Parking Garage, \$124,181 for position changes as described below and \$24,268 for extended MST WAVE trolley service hours during the summer (to be reimbursed by the Monterey Bay Aquarium). In addition, \$200,904 will be transferred from the Parking Fund to the General Fund as reimbursement for custodial, parks and street maintenance services. Revenues are projected to be \$6.5 million.

#### Parking Attendant

The proposed Parking budget includes the upgrade of a part-time Parking Facility Worker position to a full-time Parking Attendant. It has become increasingly difficult to find qualified applicants for the existing part-time position. Converting to a full-time Parking Attendant position will enable us to recruit for higher caliber applicants who possess more appropriate work experience, and will give the off-street supervisor greater flexibility in scheduling the parking attendant workforce. The net cost of this upgrade is \$49,478 to be paid for by the Parking Fund.

#### Parking Management Positions

This budget package proposes: 1) creation of a one-half time contract Assistant Public Facilities Director; 2) upgrading the Parking Superintendent position back to full-time; and 3) banding of the Parking Superintendent position with the Harbormaster. The one-half time contract Assistant Public Facilities Director position would be responsible for providing administrative staff assistance to the Public Facilities Director (also one-half time) in the development, implementation and administration of Department policy, programs and operations. This position will also be responsible for assisting the Conference Center General Manager during the transition of the Sales Marketing program to the Monterey County Convention and Visitor's Bureau to ensure that the City's best interest is protected. The cost to the Parking Fund for these changes is \$74,703. However, there is a savings in the Marina Fund as noted above which brings the net cost down.

#### Parking Fund Land and Facility Lease Payments

Since the early 1990s, in response to the first property tax "grabs" by the State, the City has put much effort into ensuring that all costs that can be legitimately born by funds other than the General Fund be captured and allocated correctly. The first incarnation of this was the formalization of the debt agreement between the City and the Redevelopment Agency in 1993 for the many projects paid for by the City's General Fund in the early years of the Agency.

The City has implemented several other cost reimbursement arrangements with City special funds since then that generate hundreds of thousands of dollars for the General Fund each year. Examples include payments to the General Fund by the Parking Fund for administrative, custodial and street maintenance services, from the Marina Fund for administrative services and wharf maintenance, and from the Presidio Fund for administrative overhead.

Some City funds such as the Parking and Marina funds are classified as “enterprise” funds because the intent of that operation is to fully cover its operating and capital costs through its fee structure. In an effort to ensure that City enterprise funds are indeed capturing all their costs and are not being subsidized by the General Fund, staff is continually reviewing these operations and their relationship to the General Fund. For instance, Council approved a new reimbursement arrangement with the Parking Funds in the FY 07 budget whereby Parking pays the General Fund for its share of the cost of street maintenance services provided to the Parking Fund for upkeep of the many on-street metered and time-limited parking spaces. This will generate a reimbursement of \$100,154 to the General Fund in FY 08.

The next step in this attempt to ensure that the parking operation includes all costs is the proposed implementation of a land and facility lease agreement between the Parking Fund and the General Fund. The premise of this recommendation is that the City’s General Fund actually owns most, if not all, of the land upon which the various parking structures, lots and spaces reside. In any arms-length business arrangement, a private enterprise would pay rent for the use of that land. In fact the City generates over \$3 million annually leasing City land and facilities to private parties. Staff believes the General Fund should not be keeping parking rates artificially low by providing free rent.

Similarly, The Redevelopment Agency owns the City’s parking garages and the Parking Fund makes facility lease payments on these structures equal to the cost of the annual bond payments. Staff believes that in the case of the East and West Custom House garages, though the debt was recently paid off by the Agency, this does not change the fact that the parking operation has use of these structures and should continue to pay some level of facility rent.

Additional analysis, research and discussion still needs to take place in order to determine a fair level of rent for land and facilities used by the parking operation. And it is possible that one result of implementing this recommendation is that parking rates may have to be increased at some point. However, staff believes that after considering the annual gross receipts of the Parking Fund and lease rates charged on other City properties, land and facility rent could approach \$600,000 annually. A more precise analysis and recommended lease agreement will be brought back to council at a later time for discussion and adoption.

### Worker's Compensation Fund

Currently, the Workers Compensation Fund reserve is \$5.9 million. The most recent actuarial report states that the "expected level" of the reserve should be \$7.4 million. The "expected level" means that given our history and trends, there is an even chance that this reserve level will fully fund all worker's compensation losses, known and unknown. So it is possible this reserve is underfunded.

However, staff is still analyzing this report and talking to the actuary and our worker's compensation administrator to try to determine why there has been an increase in the projected reserve, especially since actual claims experience has been reasonably good and stable. Early indications are that the actuary does not credit the reimbursements from excess insurance coverage in the calculations for the reserve. This may be because the City must pay the claim and then seek reimbursement. So, in theory, the City is always liable for the claim, even though excess will reimburse the City for its cost. Staff is exploring the question of how much money needs to be on hand to meet our reserve obligations. Therefore, the proposed budget includes a \$100,000 increase in the reserve level, but we are not at this point recommending any additional transfers until questions about the actuarial report have been clarified. If additional reserve funding is necessary staff will return to Council with a full analysis at a later time.

## **General Fund Reserves**

### Economic Uncertainty

In FY 04, Council authorized a draw of \$1.5 million from the Reserve for Economic Uncertainty to balance the budget. The proposed FY 08 budget brings the reserve up to \$5.8 million, which is equivalent to 11% of General Fund net operating expenditures. However, Council fiscal policy sets the target reserve at 15%, which would require a reserve of \$7.9 million, leaving us \$2.1 million short. In the FY 07 budget, Council approved a five-year plan to gradually bring the Economic Uncertainty reserve back up to 15%. Because of budget changes in the current year, mostly related to increases in public safety salaries, staff now estimates that it will take an additional three years to fully re-establish this important reserve.

### Property Acquisition

This reserve started the year with \$2 million. To complete funding for the Mohr Motors property, \$200,000 was taken from the reserve earlier this year. An additional \$1,411,189 was subsequently transferred out of this reserve to the Monterey Conference Center HVAC CIP project account to fully fund that project. This is an instance of where a necessary capital replacement project on a key facility came up and we had only \$205,000 in reserve for Conference Center capital renewal. Far short of what was needed. So the property acquisition reserve had to be tapped. Due to other budget priorities, staff is not recommending funding this reserve in FY 08.

### Business Transformation

As Council is aware, the City is undergoing a number of technology-related transformation projects in order to obtain better management information for decision making and to make City operations more efficient. One such upcoming project is a new Police Records Management system. Staff is not at a point where we are ready to budget for these systems, but the Business Transformation Reserve contains \$352,775 for potential future acquisition of this software and other costs based on our best estimate of need at this point. Staff will return to Council, once a system is selected, with a request to award a contract along with an appropriate business case for the purchase.

### Capital Facilities Renewal

As mentioned earlier, setting aside enough money for the capital renewal of the City's facilities and infrastructure continues to be a major challenge. For the first time in many years, in FY 07 Council approved the funding of several capital renewal reserves for key facilities such as the Sports Center, Conference, Library and Wharves. Though these reserves were meant for projects "down the road", in the case of the Sports Center and Conference Center urgent projects came up that used up their reserves almost as soon as they were in place.

In order to recognize the importance of planning ahead for capital expenditures, and to exercise prudent stewardship of the City's facilities, staff is recommending in the FY 08 budget that \$1,295,000 be transferred from the Public Service Center Fund to the Capital Facility Renewal Reserves. As a starting point we are proposing setting aside 1% of the insured value of these properties each year for future use. Though staff believes this level of funding is not nearly enough, it will help keep some momentum going on the funding of these key reserves. This funding is on top of the regular ongoing General Fund Capital Improvement Program (CIP) budget which is proposed to be \$1,250,000 in FY 08.

### **LONG-TERM GENERAL FUND FORECAST**

As part of the recent FY 07 mid-year financial review, staff explained that we were already projecting FY 08 would be in a significant deficit position, but for the out-years we did not expect to be structurally out of balance. The short-term deficit came from the decision to substantially increase the salaries of police officers in order to attract qualified candidates for the many open positions we were not able to fill. We could not fill these positions because, simply put, our salaries were no longer competitive in the job marketplace.

Public safety is our highest priority, so the good news is that this strategy was very successful. The Police Department is now fully staffed with very well-qualified personnel. However, fiscally speaking, this came at a cost. Staff was comfortable recommending this approach, however, because starting with FY 09 the Cannery Row Hotel is scheduled to open and is expected to generate significant new revenue (upwards of \$2 million), enough to bring the budget back into balance.

In the proposed FY 08 budget, the projected operating deficit (i.e. ongoing inflows minus ongoing outflows) is \$1.1 million, which is very close to the FY 08 deficit projected at mid-year. This budget does however provide some funding for future capital facilities renewal and makes progress toward building the Reserve for Economic Uncertainty back up to policy levels. And in the end, we project that the General Fund Available Balance (i.e. unappropriated, unreserved fund balance) will be \$278,000.

#### Fiscal Year 2008-09

Looking past next fiscal year to FY 09, we project a General Fund operating budget that is structurally balanced, but just barely so. As we discussed during the mid-year review, new revenue generated by the Cannery Row Hotel are expected to bring the budget back into balance after the FY 08 deficit year. This will not leave a lot of latitude for program/expenditure growth given current projections. However, staff is exploring in more depth full cost reimbursement from the City's special funds, such as the Parking Fund as mentioned earlier. This may result in additional financial flexibility in the General Fund though it could begin to strain the Parking Fund's resources and may require a rate increase in the future.

Our early FY 09 projections show an operating surplus of approximately \$68,000. However, this does not include the annual set-aside of \$900,000 from the General Fund operating budget for renewal of our key facilities. The FY 08 proposed and FY 09 projected budgets do include this reserve set-aside from non-operating resources however. The ultimate goal is to fund these key capital renewal reserves from operating resources.

The FY 09 forecast includes the annual allocation to the Reserve for Economic Uncertainty for 15% of the growth in the expenditure budget, as well as a "catch-up" transfer of \$750,000 to begin bringing this reserve back to 15%. In line with the plan approved last year, staff proposes that non-operating resources be used to partially bring this reserve back to policy level over time. However, because of other budgetary changes this year, we now estimate that it will be FY 14 (rather than FY 11) before we are fully back to 15%.

As discussed earlier, employee recruitment and retention and capital infrastructure maintenance will continue to be significant issues in the years ahead. Nevertheless, through prudent financial planning and stewardship, and a dogged determination to live within our means over the long haul, the City of Monterey continues to be in a better financial condition than many other governmental organizations. I believe that even though we are projecting a deficit for FY 08, we fully understand why that is the case and that it is a short-term situation. Structurally, the City's General Fund remains balanced.



Fred Meurer  
City Manager