June 19, 2006

Honorable Mayor and City Council:

I am pleased to submit the fiscal year 2006-2007 City of Antioch budget. This has once again been an intense budget development period. The City Council and staff have worked hard to tackle difficult issues over the past few fiscal years. A deficit situation caused by several factors, including revenue taken away from the City by the State, was finally reversed in fiscal year 2005-2006. While the future remains challenging in the short run, we have taken this first step.

This budget includes implementation of the recently adopted cost allocation model. Cost allocation assures the City is accurately accounting for, and charging properly for, our complete overhead costs. We have also attempted to modify the internal service fund approach taken in previous budgets. This will give the Council a clearer accounting of Departmental budgets and costs. This is also the first budget completed for a number of the new Executive Management team members.

The budget positions the City to be in compliance with the recently discussed reserve policy, which will be presented to Council for adoption in August. The reserve policy will become an important part of the framework for financial planning for the City.

This part of the budget message is organized in the following major sections:

Budget Challenges
Economic Overview
General Fund Revenue Assumptions
General fund Expenditure Assumptions
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Conclusion

BUDGET CHALLENGES

Executive Management Team

Key City staff retired during Fiscal Year 2005-2006, creating opportunities to hire a new City Attorney, Finance Director, and Police Chief. A new Human Resources Director was brought on board and the City Council authorized funding for a new Economic Development Director who also joined the staff.

The State's Fiscal Condition

The "Triple-Flip" is in effect with the impacts described in a following discussion on revenue assumptions, but the potential impacts from the State's financial and budget situation requires careful monitoring. The provisions of State Proposition 1A, Protection of Local Government Revenues, passed by voters in November 2004, help ensure limits on the State's ability to raid local government resources such as portions of the property tax, sales tax and vehicle license fees.

Over the past two years, State payments extracted for the Educational Revenue Augmentation Fund (ERAF) from the City's General Fund and Redevelopment Agency totaled $2.6 million. Proposition 1A protects the General Fund from future takes unless the State determines a "fiscal hardship" exists. While Proposition 1A addresses General Fund tax revenue sources, it leaves Redevelopment Agencies vulnerable to future State raids. Any significant reduction in Redevelopment revenues will negatively impact the City's budget.

The State's financial issues continue to create uncertainties for local government. Current proposals such as those involving State and new Federal provisions on franchising of telecom services could impact local government's contract authority as well as revenues.

Other Post Employment Benefits (OPEB)

The rising costs of providing health benefits affecting both the State and communities such as Antioch, which provides paid health coverage as a retiree and current employee benefit. The provision of this benefit to future retirees establishes the further requirement under the new Governmental Accounting Standards Board (GASB) Statement No. 45 to report these future costs and the progress made toward funding these costs, in financial statements beginning in FY 2007-2008.

Other Post Employment Benefits (OPEB) (Continued)

The provision of paid retiree health coverage is considered an “Other Post Employment Benefit” (OPEB) by GASB. The new rule requires the provider agency to calculate the current estimated costs for the future benefit. The government entity then has the option to determine the method it will use to pay for this future benefit. The GASB requirement is to reflect the estimated costs, the resources allocated to fund this benefit, and to report the difference. If the amount currently set aside to fund the benefits is less than the need calculated, the difference is reflected in the financial statements as an “unfunded liability.” Many public agencies have routinely used the “pay-as-you-go” method of accounting for retiree medical costs.

The State’s unfunded liability for OPEB is estimated by the Legislative Analyst’s Office to approach $70 billion. The State’s lack of a plan to address a known obligation of this size creates fiscal uncertainty, and increases the likelihood that the State may look to others for resources it does not currently have.

The City of Antioch provides for the payment of a portion of the medical premiums for all employees who retire from service (either regular retirement or disability retirement), based on their respective MOU currently in effect. The City has been reporting the retiree medical liability and funding a portion of it annually in three Post Employment Medical Internal Service Funds.

In an effort to reduce future liabilities, the City has negotiated MOU’s to modify post retiree medical coverage for future hires. The unfunded liability is recalculated annually and will be adjusted to account for employees hired before January 10, 2005. This new approach to medical after retirement will both provide future employees with more flexibility and the City with more predictable expenses.

ECONOMIC OVERVIEW

The Federal government continues to work through many of the same concerns affecting the national economy that have been present for years, such as expanding Federal budget and trade deficits, the war in Iraq, high oil prices, and increasing interest rates. In spite of these economic challenges, the national economy continues to slowly grow. Local governments are faced with the reality that local programs such as the Community Development Block Grant

(CDBG) funding may be cut in an effort to bring balance to the larger Federal budget.

The State of California is experiencing unexpected increases in revenues that have resulted in earlier than expected pay backs to local governments of VLF funds. While some of the increases can be attributed to one-time revenues, the State's economic growth continues. While it can be expected that at least some of the State's deficit problems will resolve through growth, the structural budgetary problems that brought State and Local Governments to Proposition 1A remain. Key among them is the State's inability to bring operating revenue estimates in line with operating expenditures. While the State struggles with its own budget, the potential exists for future raids on local resources in spite of Proposition 1A.

While the Bay Area continues to pull out of the economic setback caused by the "dot.com" recession, permanent job creation is still a concern. Antioch's population has leveled off following years of steady growth. More than twenty thousand residents have been added to the population in the last eight years. Job creation has increased significantly in the last three years, while commercial square footage has also experienced steady growth over the same period.

Revenue projections for Fiscal Year 2006-2007 reflect cautious optimism with estimates based on known economic factors such as expected increases in property tax from the County Tax Assessor's office, and in sales tax projections with newer commercial areas such as Slatten Ranch in full operation.

GENERAL FUND REVENUE ASSUMPTIONS

Property Tax

Property Tax makes up 36.2% of estimated General Fund revenue in FY 2006-2007 when the City of Antioch anticipates receiving $15.7 million in property tax. Growth in property taxes has been projected at 7.5%, which is conservatively estimated based on higher projections from the County Tax Assessor.

Sales Tax

Sales tax is estimated to generate a total of $12.4 million in FY 2006-2007. This represents 29% of General Fund revenues. It is the second largest source of revenue in the General Fund and represents an expected increase of 8% over the revenue estimated for FY2005-2006. Projections are based upon analysts projections of most likely results based on projected retail sales for FY2006-2007. As reported, newer retail centers such as Slatten Ranch are now fully operational and other segments of the economy such as auto sales are also rising.

In addition to regular calculations of estimating revenues, the City must calculate the estimated sales tax revenue involved in reconciling the States “triple-flip” payments. Because the “triple-flip” changes the cash flow of sales tax, each year there will be a reconciling payment/reimbursement from/to the County of a “settle-up” from the prior year.

The “triple-flip” is the State’s mechanism to ensure that the bonds issued to deal with their budget deficit had a “new” funding source. While the City can be reasonably assured that all sales tax properly allocated to the City will be received, the timing of the cash flow is impacted by this program. As a result, estimated sales tax revenue is now developed by looking at the economic forecasts, and then determining the effect of the State’s “triple-flip.” This method of estimation will be required until the State’s deficit bonds are paid.

The City of Antioch currently contracts with MBIA MuniServices Company to perform sales tax analysis and monitor “triple-flip” tax receipts.

Franchise Fees

The City of Antioch is anticipating $2.4 million in franchise fees in FY 2006-2007. This represents 5.6% of total General Fund revenues. This amount represents a modest increase over expected FY2005-2006. Recent activity related to increasing competition in the Cable industry without the contractual requirement to pay local government a franchise fee places, a sizeable portion (estimated at $850 thousand in FY 2006-2007), of this revenue at risk. The legislative outcome of this issue is anticipated in the next few months.

Transfers of Funds and Interfund Charges

Transfers are made from the other funds such as Enterprise Funds, Special Revenue Funds, etc., to pay for the support provided by General Fund departments or to pay for specific purposes.. The FY 2006-2007 Budget includes $1.2 million in net transfers to the General Fund for services provided.

The FY 2006-2007 Budget also implements the recommendations of the City-wide cost allocation study conducted over the past two years. The cost allocation plan provides a methodology for calculating and distributing costs of providing departments or funds to receiving departments or funds. The net increase in the General Fund as a result of implementing the cost allocation plan in FY 2006-2007 is expected to be $2.2 million.

EXPENDITURE ASSUMPTIONS

All known labor agreement Memorandum of Understanding (MOU) adjustments are included in the preliminary appropriations, for each respective MOU. A vacancy factor has been included in the Police Department budgets based upon the expectation that eight positions will remain unfilled although recruitments continue.

ACKNOWLEDGEMENTS

The new budget team of Finance Director, Dee Brookshire, Assistant Finance Director, Dawn Merchant, and Administrative Analyst III, Janan Roybal deserves recognition and special thanks for the long hours and hard work dedicated to the implementation of the city-wide cost allocation plan and the development of the FY 2006-2007 Budget.

CONCLUSION

This year's operating budget focuses on implementing key capital projects and providing enhanced public services. During the coming year, the City will continue to expand its police department through staffing increases, continue long-term financial, program and project planning, and work closely with the community to improve the quality of life in Antioch.

Respectfully submitted,

JIM JAKEL
City Manager