

October 31, 2002

Mayor and City Council  
City of Modesto  
1010 Tenth Street  
Modesto, California 95354

**SUBJECT:** Adopted Budget for Fiscal Year 2003

Honorable Mayor and Members of the City Council:

I am pleased to present you with the Fiscal Year 2003 Adopted Budget. This budget totals \$232.9 million, with \$105.7 million in General Fund expenditures, \$27,829,000 million in Capital Improvement Programs. The budget was adopted on June 25, 2002. This budget represents our determination to continue towards our goals of achieving the Vision for our city.

Vision:

*“Modesto: A healthy, safe, attractive, economically vibrant, socially diverse and culturally rich city with a strong sense of identity and pride, a community engaged in the practice of citizenship with governance based on the principle of stewardship.”*

**Overview:**

The preparation of this budget has been one of the more difficult tasks we have faced in years. As we present this budget, there is major uncertainty concerning the impact on the City of the State’s economic and budgetary problems. The State’s budget deficit is projected in excess of \$23.6 billion. In addition, within the last several weeks we have had to find ways to absorb major increases in workers compensation and insurance costs as well as a costly ruling in arbitration process with our firefighters. As you know, we have been working since December to prepare ourselves for potentially large reductions in state aid or cost increases. That effort has been successful. I am pleased to inform you that I am presenting a balanced General Fund budget for Fiscal Year 2003. This enables us to maintain General fund reserves in excess of \$9 million and positions us well to be able to weather the expected losses of State aid.

Our success is based on two factors, the ability of our operating departments to identify service reductions and other savings that resulted in expenditure reductions of \$4.02 million in fiscal 2002 and 2003 and the continuing robust performance of our local economy. This, along with the prudent use of City cash reserves, has

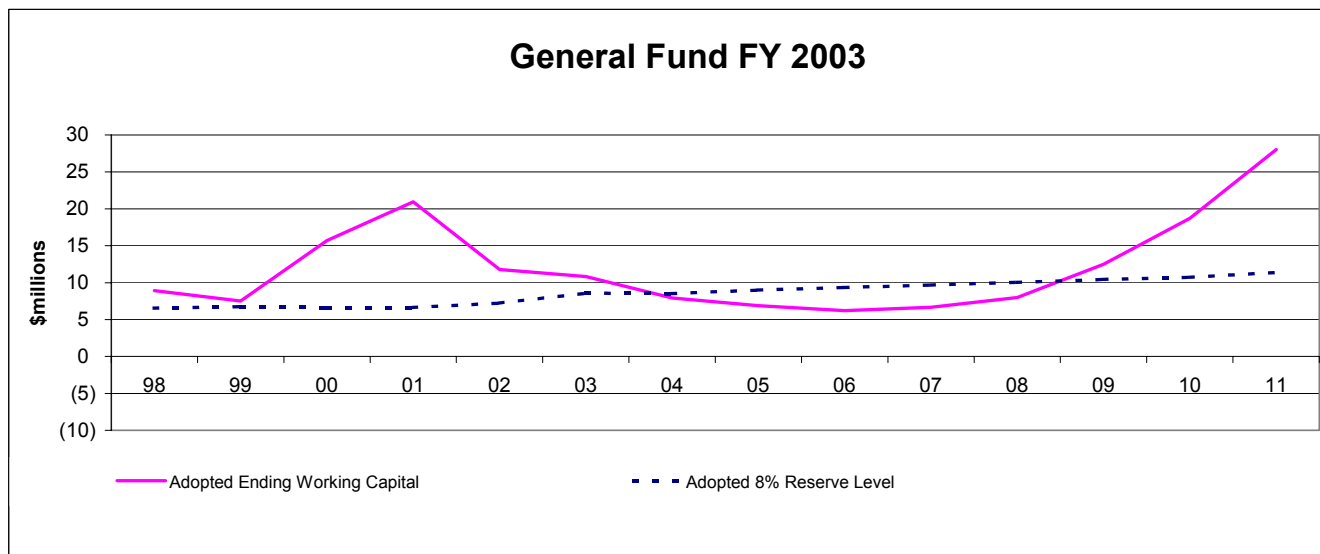
enabled us to maintain our commitment to public safety with larger than inflationary increases for both Police and Fire. This commitment is summarized below:

- Fire Station No. 11 construction \$1.16 million (\$ 660,000 funded in FY 03 and the remaining funding and staffing in FY 04)
- Fire Department net budget increase by \$ 3.3 million.
- Police Department net budget increase of \$1.8 million

We estimate the General Fund’s ending working capital for June 30, 2002 at \$10.6 million, which is \$0.8 m under the FY 2001-2002 Adopted Budget amount of \$11.4 million. The \$10.6 million includes a reserve for cable at \$990,000, therefore, the estimated ending working capital for FY 2003 budget is \$9.6 million. Outside of these figures includes \$3.2 million set aside for the Village One storm drain in FY 2002.

This budget represents continued support of public needs for a population growing over 200,000. We have changed the expenditure growth rate to reflect the increased CALPERS (California Public Employees Retirement System) costs associated with the Fire arbitration and Public Safety labor agreements approved by Council. We expect the revenue growth to continue into the next year, and our long-term revenue projections have been adjusted to many five-year averages. The resulting “smile curve”, below shows the estimated General Fund working capital is at 9% at the end of FY 2003, then slowly dropping to a 4% level in FY 2005 before it returns to the 8% level in FY 2008. The upward slope of the curve in the out years illustrates the point at which additional General Fund money can be spent on major capital improvement projects or increased staffing based on current revenue and expenditure assumptions.

The General Fund graph below is a tool for policy makers to evaluate decisions and impacts.



As we have discussed in the past, any long-term financial model is extremely sensitive to changes in the assumptions. In our model, we are projecting inflation to be slightly less than 3 %, that our

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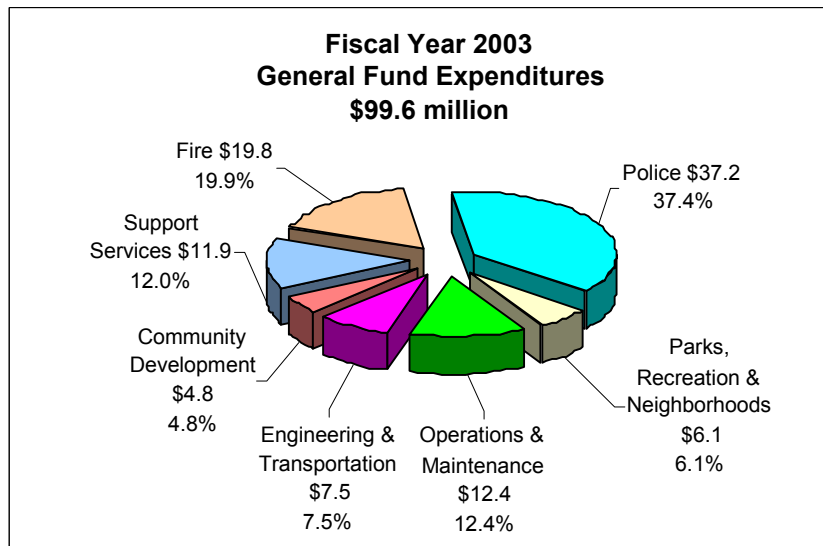
revenues will grow faster than that at approximately 3.9 %, and that we can keep expenditure growth to slightly less at 2.5 %. In addition, the model no longer assumes large unspent departmental expenditures.

**Reserves:**

In FY 2001, Council adopted a policy increasing the targeted General Fund reserve level to 8% in order to safeguard the City against economic downturn and improve our ability to respond to emergency needs. This policy gave us increased protection against the uncertain dynamics associated with the power crisis and stock market volatility, and will offer protection against the potential fiscal impacts of the State of California budget deficit and changes in the local economy. It is important to maintain the General Fund reserve target of 8% over the next couple of years. The 8% target assists us in retaining a good bond rating standing, which is currently rated at A3.

**Expenditures:**

General Fund expenditures are budgeted at \$99.6 million. General Fund expenditures for Public Safety represent the largest portion of the General Fund at 57.3% of the total budget. Of this amount, Police represents \$37.2 million (37.4%) and Fire represents \$19.8 million (19.9%). Other City Departments are Operation and Maintenance, 12.4%; Engineering and Transportation, 7.5%; Parks, Recreation and Neighborhoods, 6.1%; and Community Development, 4.8%. The Support Services area includes City Council, City Manager, City Attorney, City Clerk/Auditor, Personnel, Finance and non-departmental. These departments total 12.0%. Support Services also includes less than 1% for non-departmental usage.



Our goal is and will continue to be a commitment to give citizens a General Fund budget that balances operating expenditures with available operating revenues. In FY 2002, our budget for the first time balanced revenues with department expenditures. Because of a large fund balance, we increased the transfers out of the General Fund to fund important capital projects.

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<b>Operating Budget General Fund (millions)</b>		<b>FY 2003</b>
<b>Estimated Revenues</b>		<b>\$98.1</b>
<b>Operating transfer in</b>		<b>7.6</b>
<b>Total Revenues</b>		<b>\$105.7</b>
<b>Budgeted Expenditures</b>		<b>\$99.6</b>
<b>Operating transfers out</b>		<b>6.1</b>
<b>Total Expenditures</b>		<b>\$105.7</b>
<b>Projected Change in Working</b>		<b>0</b>

This year, our intent is to preserve our working capital and balance the budget including all transfers in and out as Total Revenue equals Total Expenditures. Transfers out of the General Fund were reduced to create a net of “0” dollars for Total Revenues less Total Expenditures. This allowed us to meet this vital objective of balancing the budget and protecting our working capital.

The major transfers into the General Fund come from the Special Gas Tax Fund, Local Transportation Fund and Traffic Safety Fund to provide for the daily operations in Streets Maintenance, Electrical, Community Forestry and Traffic Divisions. There have been no transfers from the Utility Funds since the Council eliminated them on September 21, 1999. Major transfers out of the General Fund include the one-time expenditures on capital items, the payment of Tenth Street debt service, subsidy for Centre Plaza, the transfers to the Redevelopment Agency and their portion of the Transient Occupancy Tax, and the loan to the Golf Fund.

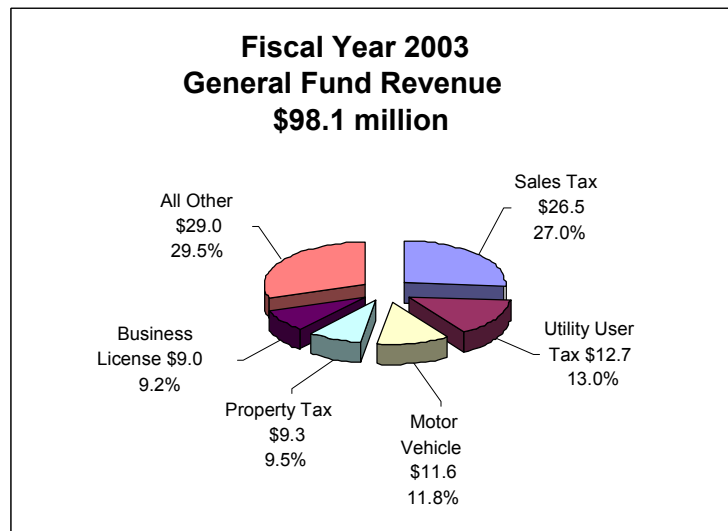
**Revenues:**

Fiscal Year 2003 General Fund revenues are projected at \$98.1 million with overall revenue growth in the General Fund projected at 3.3%. Major revenue sources are projected to grow by 4.9%. Our revenue assumptions for FY 2003 for Sales Tax and Motor Vehicles are set at five-year averages. Future growth assumptions for revenues have been increased to 4.9% overall. This represents a determination to pursue revenue-generating policies and cost savings measures. The chart below illustrates the General Fund’s major revenue sources.

<b>General Fund Revenues</b>					
(millions)					
	Actual FY 2001	Estimate FY 2002	FY 2003 Assumption	Budget FY 2003	Long-range Avg Assumption
Sales Tax	\$23.3	\$24.8	6.8%	\$26.5	6.0%
Utility Users Tax	14.4	12.3	3.5%	12.7	3.5%
Motor Vehicle	9.9	10.7	8.2%	11.6	7.0%
Property Taxes	8.2	9.0	3.1%	9.3	4.9%
Business License	8.0	8.5	6.6%	9.0	6.7%
Transient Occupancy	2.1	2.2	4.5%	2.3	4.5%
Franchise Fees	2.4	3.0	4.3%	3.1	5.1%
Investment Income	1.7	1.3	-50.0%	0.6	-16.1%
Indirect Cost Recovery	2.5	2.7	6.3%	2.8	3.0%
Construction Related	3.4	2.8	7.2%	3.0	3.5%
Major Revenues	75.8	77.2	4.9%	81.0	5.4%
Other Revenues	10.5	17.7	-3.7%	17.1	2.7%
<b>Total</b>	<b>86.3</b>	<b>94.9</b>	<b>3.3%</b>	<b>98.1</b>	<b>4.9%</b>

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The large drop in Utility Users Tax (UUT) simply recognizes that fiscal 2001, with its massive increases in energy prices were a one-time anomaly that will not reoccur. Unfortunately, this has an impact on our road maintenance expenditures. The reduction of UUT means that “excess” monies pledged toward road maintenance have disappeared and we will, therefore, be appropriating \$760,000 less in fiscal 2003. The large reduction in investment income reflects much lower cash balances as well as a slight reduction in interest rates. The FY 2002-2003 budget does not allocate any UUT revenue toward road maintenance. A preliminary report on street maintenance is included in the Policy Issues and Reports section and new reports will be issued in December 2002.



**Public Safety:**

Even in these difficult times, we have continued our commitment toward Public Safety. As noted earlier, we have increased the budgets of both the Police Department (5.6 %) and the Fire Department (22.5 %) much more than inflation while also continuing with plans to construct, equip and staff Fire Station No. 11 in Fiscal Year 2004. We substantially increased budgeted overtime and contractual expenses in Police and covered the full cost of the pension expenses in the Fire Department. Unfortunately, these large increases in labor costs, particularly in the Fire Department and in workers compensation and insurance costs for these departments has meant some reductions in staffing levels. In the Police Department we have not funded 8 sworn and 4 non-sworn positions, while the Fire Department was reduced by 4 support positions. The Police Department is aggressively pursuing grant funding for additional police officers. These officers will be assigned to patrol and will enhance public safety services to the community.

**Strategic Plan:**

The FY 2003 budget makes a managed effort to expend resources in areas that are closely tied to Council’s *Strategic Plan*. We must be mindful that achieving the goals listed in that plan require long-range planning and thoughtful implementation. Even significant revenue will not provide us with all of the resources needed to meet these goals and will require discipline, dedication and innovative approaches. The Strategic Plan and Department Performance Measures will become increasingly more important in light of the difficulties with balancing future year budgets and

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anticipated revenue loss because of the state deficit. During the FY 02 and 03 departmental reduction process, impacts were evaluated against strategic plan objectives. This process will be improved and continue as part of the city budget development and evaluation cycle.

**Information and Technology Services:**

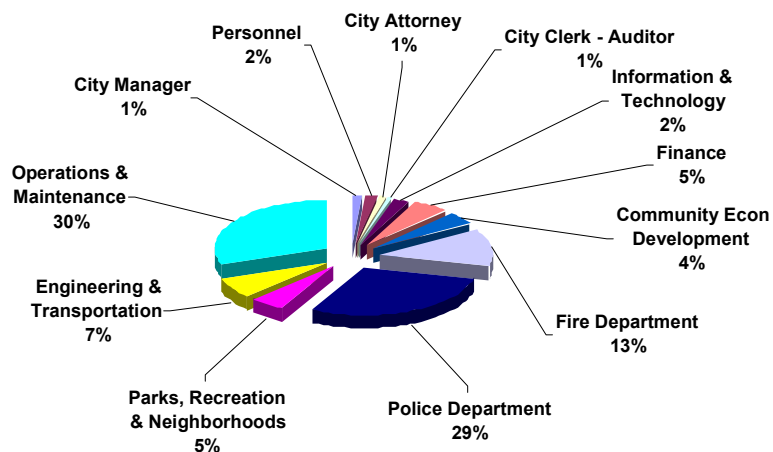
Investment in technology is critical to the successful operation of a City our size. The budget allocates an additional \$197,000 for technology, an increase of 5.9%, to improve our ability to provide essential technological services to departments and enhance our ability to implement an e-government strategy. This also provides for increases in software maintenance costs. In 2001, we have elevated this vital function to Department status, however, this department relies on internal service charges to other city departments for its budget. It is also expected that a Information Technology Director will be on board to direct mission critical services by the beginning of FY 2003. We expect that our investment in technology will offer improved services to both the public and city employees and can create an overall increase in productivity with a decrease in costs.

**Management and Administrative Services:**

This includes the City Council, Clerk/Auditor, City Manager’s Office, Finance, Personnel, City Attorney and Information and Technology support areas. A well-managed City must commit the resources necessary to conduct City business with professionalism. We have committed limited resources necessary to make improvements in our central services and systems because they support the decisions we make and the services we provide. One notable change is the function of CFD (Capital Fee Districts) moved from the City Attorney to the City Manager’s Department.

**Position Allocation:**

**FY02-03 Position Allocation by Department**



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**Staffing:**

The FY 2002 adopted budget included an increase of 54.4 full-time equivalent positions (FTEs) from 1,209. Of the 54.4 FTEs, 32.7 FTEs were in the General Fund and 22.5 positions represented conversion of part-time or contract positions to full-time status. The FY 2002-2003 budget eliminates the funding for 31.5 FTEs supported by the General Fund. The chart below compares staffing levels as well as the results of the FY 03 budget reductions.

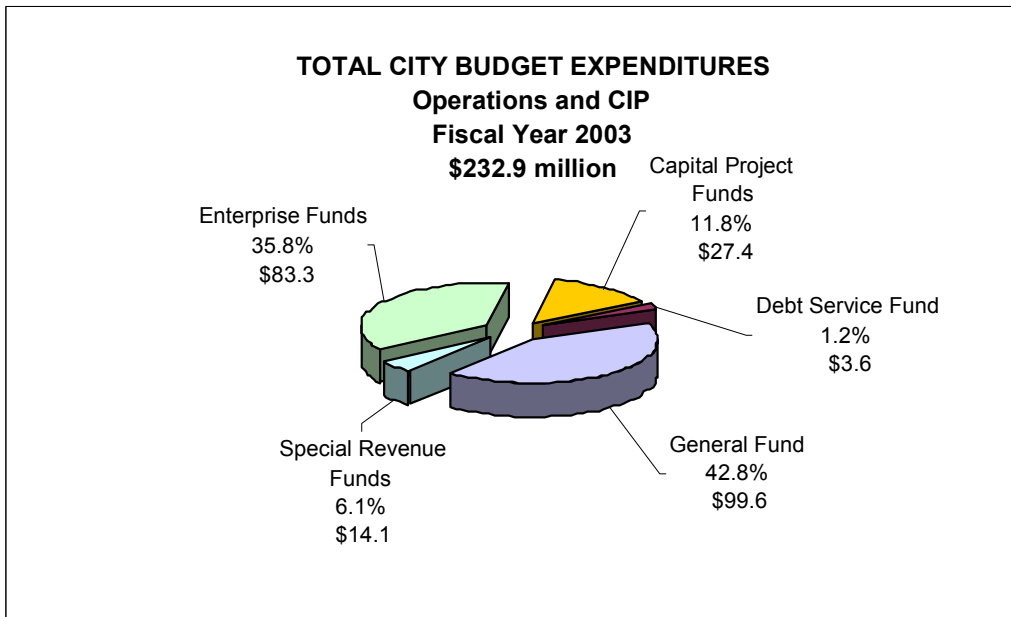
				<b>Authorized</b>	<b>Unfunded</b>	<b>Budgeted</b>
	<b>FY99-00</b>	<b>FY00-01</b>	<b>FY01-02</b>	<b>FY02-03</b>	<b>Budget</b>	<b>Budgeted</b>
<b>Department</b>	<b>Actual</b>	<b>Actual</b>	<b>Current</b>	<b>Proposed</b>	<b>Reduction</b>	<b>Adopted</b>
						<b>FY 02-03</b>
						<b>Budget</b>
City Manager	10	12	16	16	0	16
Personnel	18.125	20.125	21.125	21.125	0	21.125
City Attorney	15	18	17	17	0	17
City Clerk - Auditor	5	7	7	7	0	7
Information & Technology	13.75	17.75	23.75	26.75	0	26.75
Finance	57	58	64	66	-1	65
Community Econ Development	47	48	53	53	-2	51
Fire Department	155	155	159	159	-4	155
Police Department	356	364	367	367	-12	355
Parks, Recreation & Neighborhoods	55.75	52	62.5	63.25	-1	62.25
Engineering & Transportation	78.9	89.75	91.8	90.8	-2	88.8
Operations & Maintenance	348.5	367.5	384	383	-8.5	374.5
<b>Total</b>	<b>1160.025</b>	<b>1209.125</b>	<b>1266.175</b>	<b>1269.925</b>	<b>-30.5</b>	<b>1239.425</b>
General Fund	879.125	897.375	932.675	935.425	-31.5	903.925
Other Funds	280.9	311.75	333.5	334.5	1	335.5
<b>Total</b>	<b>1160.025</b>	<b>1209.125</b>	<b>1266.175</b>	<b>1269.925</b>	<b>-30.5</b>	<b>1239.425</b>
No. of FTEs to City Population (per 1,000)	6.10	6.15	6.37	6.23		6.08
City Population	190,100	196,679	198,633	203,718		203,718
Note: This table does not include the City Council						

Although, the population of the city continues to grow, the number of City employees per thousand based on the FY 2003 budget returns to a 1999 city staff to population ratio. City employees provide direct services to the citizens of Modesto and maintain the city infrastructure.

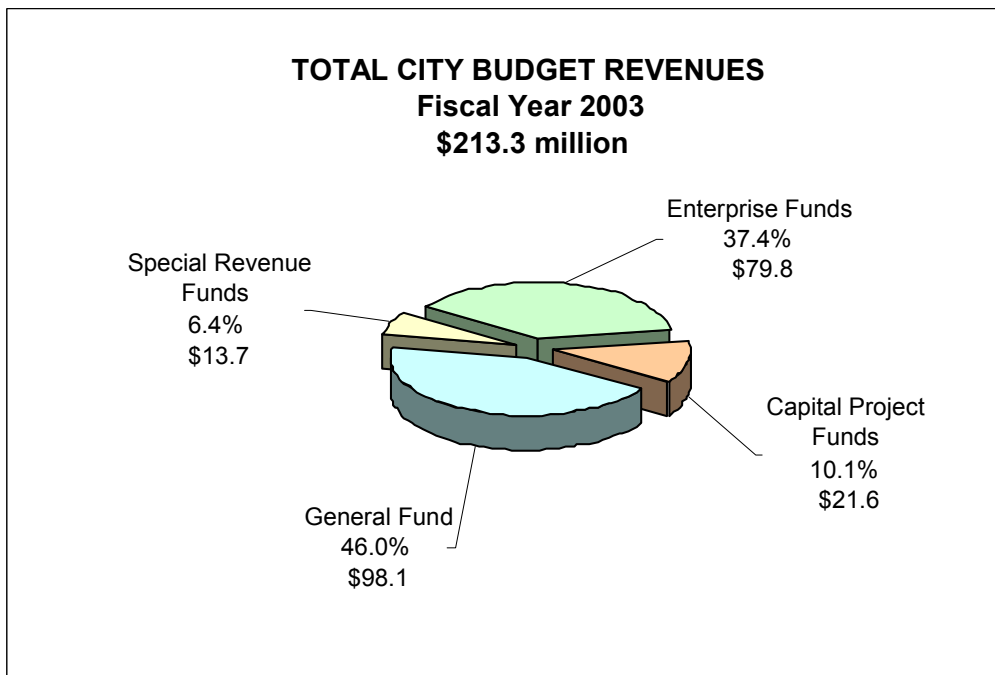
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**Fiscal Year 2003 Overall City Budget:**

The Fiscal Year 2003 overall budget totals \$232.9 million in expenditures and Capital Improvement Program (CIP) and \$213.3 million in revenues. For comparison, FY 2002 was \$220.3 million in expenditures and \$212.2 million in revenues at the adoption of the budget.



The chart below shows the overall City revenue forecast for Fiscal Year 2003. The revenue forecast is based on a careful analysis of past trends adjusted for the latest information from Departments.



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**Utility Rate Increases:**

In order to sustain adequate water, wastewater (sewer), and storm drainage facilities by improving existing deficiencies, the anticipated rate increases projected for the next ten years are shown in the following table:

Utility-Rate Increases	02/03	03/04	04/05	05/06	06/07	07/08	08/09	09/10	10/11	11/12
Water*		3%	4%	4%	3%					
Wastewater (Sewer)	4%	4%	3%	4%	3%	3%	3%	3%	3%	3%
Storm Drainage		To Be Determined after Completion of the Storm Drainage Master Plan								

\* Proposed increases for water Zones 1 and 2 only – no increases are currently planned for Zone 3.

**Storm Drain System:**

Due to the problems associated with our mail Proposition 218 ballot measure, no revenue increase has been forecast for the Storm Drain Fund for fiscal 2003. This loss of approximately \$400,000 will significantly impact the level of preventative maintenance performed in this area. We have, however, included monies in the budget for preparation of a comprehensive Storm Drain Master Plan. This plan will document infrastructure needs and financing alternatives.

The City Council established a storm drainage surcharge in June 1991, to pay for rockwell cleanings, rehabilitations, and replacements; monitoring storm water quality; street sweeping; annual leaf collections; storm drain repairs; and general capital improvements to the storm drainage system.

The City's use of a rockwell stormwater runoff retention system is highly dependent on preventative maintenance in order to function properly. While a number of repairs and improvements have been made over the past few years, the overall system is still deficient in its ability to convey stormwater runoff and minimize localized flooding in many areas of the City. This deficiency is largely due to a lack of adequate funding to perform necessary maintenance and repairs to the system in a timely manner, and since 1995, the storm drainage fees have remained unchanged but the rate of inflation has increased by over 15%. It is estimated that without a rate increase the Storm Drainage Enterprise will be depleted, requiring a reduction in maintenance and repair levels. Maintenance will become more oriented toward "stop gap" measures, reacting to problems in the system as they occur rather than preventative or proactive maintenance.

**Golf Fund:**

This fund continues to experience difficulties in making its revenues equal its costs. In fiscal in 2002, the General Fund will advance more than \$400,000 to the Golf Fund. Approximately 25 % of that amount was associated with the costs of drilling a well. For fiscal 2003, the General Fund impact will change from a "loan" status to a "subsidy" status. Revenue shortfalls will need to be constantly monitored. Additional analysis will be required to determine if this subsidy should be a set amount or continue as an adjustable dollar amount.

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**Projected Loan to the Redevelopment Agency:**

As we go to press, we still do not have the latest estimates for tax increment growth in the redevelopment area for fiscal 2003 and beyond from Keyser Marston & Associates, our redevelopment specialists. They are currently engaged to prepare new estimates of revenue growth. The Agency's budget therefore has been prepared based on their past estimates. At this time we do not expect significant changes in the budget or our estimate of the needed General Fund loan of \$337,000 in fiscal 2003. In addition, Governor Davis in the November Revision of the State budget for Fiscal Year 2003 has proposed that redevelopment agencies, among others, should also participate in the Education Revenue Augmentation Fund process. If enacted, this could have a significant effect on agency revenues.

The current budget proposes subsidizing the RDA with General Fund sales taxes and Transient Occupancy Taxes (TOT) in accordance with current Council policy.

<b>Redevelopment Loan Projection</b>			
<b>FY 2003</b>			
<b>(000's)</b>			
<b>Fiscal Year</b>	<b>FY 2001 Adopted</b>	<b>FY 2002 Adopted</b>	<b>FY 2003 Adopted</b>
2001	\$255	\$472	\$472
2002	521	931	776
2003	325	514	337
2004	33	273	64
2005	0	81	0
<b>Total</b>	<b>\$1,134</b>	<b>\$2,271</b>	<b>\$1,649</b>

**Capital Improvement Program:**

The Adopted CIP budget for Fiscal Year 2003 totals \$27,829,000 million as compared to \$28.857 million for Fiscal Year 2002. A major difference in the figures takes into effect the Federal and State grants not available in FY 2003. This year's CIP also represents another step in the City's overall strategy to address the infrastructure challenges of the Community. Our capital planning will continue to focus on meeting Council goals as stated in the Strategic Plan.

During the last couple of years, the General Fund's improved financial condition has allowed funding of several important capital projects. In FY 2002, General Fund Capital Improvement Project requests totaled \$1,940,000. For FY 2003, we are able to approve three requests for capital projects to be funded by General Fund monies totaling \$791,000. These three projects are the first three projects listed below followed by other projects of significant interest:

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- Fire Station 11 - a multi-year strategy to build, equip, and staff the new facility that will serve new development; proposed for FY 2003 is \$660,000 for the construction of the Fire Station. Additional funding in FY 2004 will allow for the completion and staffing of Fire Station 11.
- Fire Station 1 Rehabilitation – a multi year strategy to make improvements that will bring the building up to the Essential Building Act standards. Funding for FY 2003 is \$91,000.
- A Corps of Engineer Feasibility Study – Tuolumne River Flood Control at \$40,000.
- Coffee/Claratina Neighborhood Park/Basin at \$1.110 million
- Maddux Youth Center Improvements at \$524,000
- Orville Wright Neighborhood Park – All Phases at \$532,000
- Briggsmore- Oakdale to Roselle at \$1,900,000
- Claratina – Coffee to Oakdale at \$785,000
- CFF (signals and intersections) at \$2,568,000
- Bus Maintenance Facility at \$1,010,000
- Storm Drain Master Plan at \$450,000
- Cannery Segregation –Land Acquisition at \$1,200,000

In FY 2002, we revised our CIP definitions and moved annual maintenance costs out of the CIP and into the operating budgets in the appropriate departments. We believe this change more accurately reflects the ongoing maintenance needs of the City. We are currently researching all open CIP projects and accounting for all revenue sources. This effort will fold into a new and improved capital budgeting process that will be completed in FY 2003.

**Title Changes:**

In FY 2002 as part of the budget, names were changed for the following Department and Fund. Recreation and Neighborhoods Department was changed to **Parks, Recreation and Neighborhoods** to properly acknowledge the importance of Parks to our City as well as to better reflect the function of this department. In addition, the Strategic Planning Fund was changed to the **Economic Development and Strategic Planning Fund**. This change reflects the priority Council has placed on Economic Development.

In FY 2003, the name of the Community Development Department will be changed to **Community and Economic Development Department** to reflect the department's functions. The SLESF (Supplemental Law Enforcement Services Fund) will be called the **Operating Grants Fund**.

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**Conclusion:**

The City has many challenges ahead. The first step toward meeting those challenges is a budget that is responsible from a financial perspective and that reflects the Council's Vision Statement. I believe this budget passes both of these tests. It is fiscally responsible by balancing the General Fund and takes important strides toward meeting Council's goals.

In the coming year, our management team will continue to work with Council, the community, and staff to develop strategies to improve our infrastructure and meet the current and future needs of the community. Emphasis will be placed on financing infrastructure such as dual use drainage/park basins, parks, major transportation system improvements and "backbone" infrastructure, such as drainage in Village One. We will continue to pursue State and Federal grants to augment local resources and will perform master planning to develop financial strategies for the City's major infrastructure systems. These systems play a significant role in the City's economic health and enhance our ability to attract new industrial and commercial development. With this development comes jobs and a strong local economy.

As we strive for economic prosperity, we must ensure we maintain adequate police and fire protection, and a balance of other services to sustain a healthy and safe city where citizens feel protected and secure. Finally, we will turn our attention to developing cultural opportunities for our socially diverse community. We will also increase amenities to make Modesto an attractive place to live, work and play. The result will be an attractive, economically vibrant, healthy, safe, socially diverse and culturally rich community for our citizens.

Respectfully,

Jack R. Crist  
City Manager