



MEETING DATE: 10/15/07

ITEM NO: 11

## COUNCIL/AGENCY AGENDA REPORT

DATE: OCTOBER 15, 2007

TO: MAYOR AND TOWN COUNCIL/  
CHAIR AND MEMBERS OF THE REDEVELOPMENT AGENCY

FROM: PAMELA JACOBS, INTERIM TOWN MANAGER/EXECUTIVE DIRECTOR *P. Jacobs*

SUBJECT: FISCAL YEAR 2007/08 FIRST QUARTER BUDGET PERFORMANCE AND  
STATUS REPORT FOR THE PERIOD JULY 1, 2007 - SEPTEMBER 30, 2007

- A. ACCEPT 2007/08 FIRST QUARTER BUDGET PERFORMANCE STATUS REPORT.
- B. AUTHORIZE BUDGET ADJUSTMENTS AS RECOMMENDED IN THE ATTACHED FIRST QUARTER BUDGET PERFORMANCE REPORT.

### RECOMMENDATION:

1. Accept Fiscal Year 2007/08 first quarter budget performance and status report.
2. Authorize budget adjustments as recommended in the attached first quarter budget performance report.

### PURPOSE:

The purpose of this report has three primary goals. First, the report informs the Town Council on the status of the Town's FY 2007/08 Adopted Budget and status of the local economy at the first quarter. Second, staff provides the Town Council an update on the preliminary General Fund financial results (unaudited) as of June 30, 2007. Third, the report includes staff's most recent five year budget forecast which informs the evolving budget status for FY 2008/09 and beyond.

### BACKGROUND:

The attached Budget Performance Report covers the first three months of the fiscal year beginning July 1, 2007 and ending September 30, 2007. The report presents analysis and recommendations related to key General Fund revenues by category and expenditures by fund.

PREPARED BY:

*[Signature]*  
**STEPHEN D. CONWAY**  
Finance and Administrative Services Director

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Reviewed by: \_\_\_\_\_ Assistant Town Manager/Deputy Director OK Town Attorney/General  
Counsel \_\_\_\_\_ Clerk Administrator/Secretary SL Finance  
\_\_\_\_\_ Community Development

MAYOR AND TOWN COUNCIL/CHAIR AND MEMBERS OF THE REDEVELOPMENT AGENCY

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Staff provides to Town Council periodic updates on the status of the current year's adopted budget revenues and expenditures and the projected financial condition of Town funds, concentrating on the Town's General Fund. Though financial results are limited to the first three months, staff is able to provide an update based on early revenue trends for the current fiscal year, and to advise on potential future revenue and expenditure challenges which may materialize during the fiscal year.

DISCUSSION:

The attached first quarter budget report reflects a mix of positive news about last year's fiscal results, and a concern that the recovery in the Town's economically-sensitive operating revenues such as the sales tax, transient occupancy tax, and property tax will be negatively impacted from the effects of slowdowns in the local real estate market. In August 2007, the California Association of Realtors reported existing home sales were down 27.8 % statewide from the prior year. Average home prices decreased 5.1% from the year before. Economists point out that declines in housing prices tend to have a dampening effect on consumer spending. Any significant further rise in energy costs also has the potential to impact the Town's local economically-sensitive revenue base. National economists predict that as fuel prices rise, the buying power of consumers is eroded, leaving fewer dollars available for discretionary spending. If this occurs, the moderate recovery which appeared to be materializing in the Town's operating revenues last year and early this fiscal year may become stalled at some point.

**Service delivery in FY 2007/08**

In the FY 2007/08 "status quo" budget, staff conservatively forecasted continuing recoveries in local revenues and incorporated modest revenue growth in economically-sensitive revenues such as sales tax, franchise fees, business license and transient occupancy taxes. While avoiding another consecutive year of service level reductions in FY 2007/08, the reductions carried over from the prior year continue to have effects on operations overall. Holding vacancies and reducing staffing and overtime result in the current workforce absorbing more of the workload, thus affecting the capacity to deliver services and limiting the flexibility to respond to new ideas and/or increased service demands. Response times associated with non-public safety requests have increased. Parks and public works related maintenance cycles have been extended or reduced, as well. Over the longer-term, staff's goal of achieving the highest quality of service levels possible is constrained by available resources to fund them.

**FY 2008/09 and Beyond: Continuing Challenges Ahead**

Staff remains attentive to the goal of preserving the Town's economic vitality. The most recent update to the Town's Five-Year Financial Plan presented on the following page continues to project potential revenue shortfalls developing in future years. However, the current update indicates two important points: The first is that the efforts the Town has accomplished in the

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past four years have generated positive fiscal results in spite of a lingering soft local economy and the closing of three automobile dealerships in the past two fiscal years. Second, if recoveries continue in economically-sensitive revenues and service delivery costs are contained, the projected shortfalls will be reduced accordingly. However, downward adjustments to the Town's operating budget are expected to be necessary to avoid the future shortfalls forecast for FY 2010/11.

The updated Five-Year Financial Plan is based upon estimated costs of labor and benefits which represent approximately 70% of General Fund operating costs, and assumptions for modest increases in revenues associated with a gradual economic recovery from the downturns experienced in recent years. The plan currently projects revenue shortfalls ranging from \$574,000 to \$1.0M in future years that must be managed pro-actively by the Town. To address this, the Town is continuing its multi-prong efforts to achieve operational efficiencies, cost reductions, reductions in non-vital services, and revenue enhancement efforts. An analysis of fees for cost recovery levels will also be undertaken as in years past. As the budget tightens each fiscal year, the ability to reduce operational expenditures without service impacts becomes increasingly challenging.

The Five-Year Forecast assumes that the State property tax swap or "back-fill" of approximately \$1.2 million in Car Tax for local property tax will continue to be implemented permanently in each annual budget bill as promised by the State. Revenues are presented optimistically with varying growth rates, 5% on average for tax revenues and 3% for charges for services. Expenditures are derived from a database using actual costs and adjusting for future known increases in labor costs if multi-year labor agreements are in effect, and actuarial updates for retirement and other benefit costs as provided by PERS or other information sources available to the Town.

Each of the years presented in the plan assume that adjustments made to the budget to eliminate the revenue shortfall in FY 2007/08 and beyond are "permanent" adjustments, thereby reducing the level of shortfall in the following fiscal years. It is possible to make some adjustments through one-time solutions or prudent use of bridge funding on a year-to-year basis. The Revenue Stabilization Reserve is available for this purpose. However, problems that are truly structural should be addressed eventually with new revenue sources or reduced expenditures in an ongoing way.

## MAYOR AND TOWN COUNCIL/CHAIR AND MEMBERS OF THE REDEVELOPMENT AGENCY

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TOWN OF LOS GATOS - GENERAL FUND  
Five-Year Financial Plan FY 2007/08 Through FY 2011/12

	ACTUAL 2004-05	ACTUAL 2005-06	ACTUAL 2006-07	ADOPTED 2007-08	PROJECTED 2008-09	PROJECTED 2009-10	PROJECTED 2010-11	PROJECTED 2011-12
<b>Revenue Summary</b>								
Sales Tax	\$7,904,129	\$8,655,566	\$9,253,891	\$8,231,100	\$8,490,400	\$8,745,100	\$9,007,400	\$9,277,600
Property Tax	5,302,061	5,831,822	\$6,594,056	\$6,727,220	\$6,976,200	\$7,244,500	\$7,523,900	\$7,814,300
Charges for Services	2,920,356	3,006,634	\$3,967,735	\$3,371,470	\$3,026,000	\$3,060,300	\$3,097,100	\$3,136,100
Business Licenses	1,056,814	1,019,386	\$1,176,422	\$1,920,400	\$1,015,000	\$1,030,200	\$1,045,700	\$1,061,400
Car Tax/VLF Prop Tax Swap	1,554,932	2,096,704	\$2,003,271	\$2,030,360	\$2,069,900	\$2,111,300	\$2,153,500	\$2,218,100
Intergovernmental Rev.	2,316,962	2,606,356	\$2,252,682	\$2,168,025	\$2,234,085	\$2,273,563	\$2,319,650	\$2,367,575
Other Lic. and Permits	1,360,390	1,584,662	\$1,503,014	\$1,050,000	\$1,754,800	\$1,788,500	\$1,823,000	\$1,858,200
Investment Earnings	905,704	1,385,266	\$2,576,062	\$1,498,300	\$1,639,900	\$1,657,300	\$1,674,800	\$1,692,500
Franchise Tax	942,648	1,130,190	\$1,162,038	\$1,603,180	\$1,618,400	\$1,661,500	\$1,705,800	\$1,751,400
Hotel/Motel Tax	868,908	1,028,664	\$1,108,257	\$1,000,000	\$1,030,000	\$1,060,900	\$1,092,700	\$1,125,500
Fines & Forfeitures	580,937	210,888	\$214,565	\$525,405	\$465,300	\$473,800	\$482,500	\$491,500
Transfers & Use of Reserves	494,165	430,839	\$114,470	\$400,500	\$221,700	\$223,200	\$224,700	\$226,200
Miscellaneous	247,958	2,738,297	\$599,015	\$545,100	\$1,406,450	\$1,406,450	\$1,206,450	\$1,206,450
<b>Total Revenues</b>	<b>26,455,964</b>	<b>31,725,274</b>	<b>32,525,478</b>	<b>31,071,060</b>	<b>31,948,135</b>	<b>32,736,613</b>	<b>33,357,200</b>	<b>34,226,825</b>
<b>Town Expenditures</b>								
Salary	11,415,065	11,439,231	11,126,609	13,113,656	14,482,650	14,636,889	15,183,718	15,698,356
Elected Officials	22,590	23,340	23,340	23,200	23,340	23,340	23,340	23,340
Temporary Employees	353,871	437,250	674,865	465,193	496,579	513,959	531,948	550,566
Overtime	494,170	542,624	663,992	442,900	436,476	451,753	467,564	483,916
Other Salary	572,258	571,011	755,638	396,899	201,591	206,955	213,414	218,968
Benefits	4,101,626	4,764,717	4,698,961	5,560,532	5,855,647	6,222,903	6,626,042	7,094,757
Supplies, Materials, & Services	3,256,678	3,287,777	4,763,774	5,107,209	4,278,725	4,402,850	4,564,200	4,739,000
Grants & Awards	177,578	178,359	184,329	150,326	176,410	176,410	176,410	176,410
Utilities	409,610	428,744	458,385	200,522	370,600	386,960	404,200	422,410
Fixed Assets	-	192,343	46,556	-	-	-	-	-
Internal Service Charges	2,820,428	2,849,969	3,091,387	3,312,300	3,347,500	3,447,925	3,551,363	3,657,904
Debt Service	930,710	932,122	931,078	930,790	931,850	931,100	929,050	932,100
Operating Transfers Out	182,876	67,673	230,827	-	610,000	610,000	610,000	610,000
GFAR Capital Transfers Out	75,000	475,000	4,194,094	989,370	650,000	650,000	650,000	650,000
<b>Total Expenditures</b>	<b>24,812,461</b>	<b>26,190,160</b>	<b>31,843,835</b>	<b>30,692,897</b>	<b>31,861,368</b>	<b>32,661,044</b>	<b>33,931,249</b>	<b>35,257,727</b>
<b>Net Revenues Less Expenditures</b>	<b>1,643,503</b>	<b>5,535,114</b>	<b>681,643</b>	<b>378,163</b>	<b>86,767</b>	<b>75,569</b>	<b>(\$74,049)</b>	<b>(1,030,902)</b>

**Special Consideration - Governmental Accounting Standards Board Statement #45**

Effective FY 2008/09, the Town will be required to fully accrue its actuarial determined liability for the Town's contribution to retiree health care premiums under the provisions of the Governmental Accounting Standards Board (GASB) Statement #45-Other Post Employment Benefits. The Town has historically budgeted and expensed these benefits on a "pay-as-you-go" basis, a standard procedure for most local governments under generally accepted accounting principles.

Under GASB's new accounting standard, the Town is required to accrue a liability for the cost of post-retirement benefits, using actuarial methods to estimate expected future costs for a calculated portion of the current workforce that will retire under the Town's retirement benefit program. Assumptions will be made about the level of benefits and the number of eligible employees who will eventually retire from the Town. This will be offset by future accrued investment earnings expected to be earned in a separate irrevocable trust account that is usually recommended by actuarial consultants to be established by local governments to provide a funding account for these benefits.

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Since the actuarial study is not yet completed, the Five-Year Financial Plan does not reflect these benefit costs on an actuarially determined basis (the Town expects the study to be completed by December 2007). With the understanding there would be potentially significant increases in future years, a 25% annual retiree benefit cost increase was built into the Five-Year Forecast; however, until the study is completed true liability estimates are unknown. Although accrued expenses will increase, actual cash payments to retirees are expected to trend much as they have in the "pay-as-you-go" basis. The difference between the accrued annual expense and the actual cash payments made annually by the Town will likely be phased-in over a period of approximately 10 to 20 years until the full annual actuarial accrual of this expense is achieved. Until then, the difference between amounts set aside by the Town and the actuarial liability will be booked at year-end either as a liability or asset on the Town's financial statements. As a result of GASB 45, the future updates of the Five-Year Financial Plan will include potential increases to the annual expenditures for cash payments made to the post retirement trust account used to fund post retirement benefits.

**Conclusion**

The Town has managed very effectively through the budget challenges in recent years. Shortfalls were dealt with, priority services maintained, and General Fund contingency reserves are intact. However, with the most current update to the Town's Five-Year Financial Plan indicating projected shortfalls beginning in FY 20010/11, the need to remain fiscally aware continues to be a high priority for Town staff. Key goals are to minimize the impact on Town services, maintain the community's quality of life, and remain a competitive employer while sustaining the Town's fiscal health.

FORMAT OF THE REPORT

The attached Budget Performance Report includes a financial overview comprised of: a brief discussion of the Town's financial condition; the FY 2007/08 financial outlook; a summary of the performance of the Town's primary General Fund revenue sources and necessary budget adjustments; and a look ahead at the FY 2008/09 budget process.

ENVIRONMENTAL ASSESSMENT:

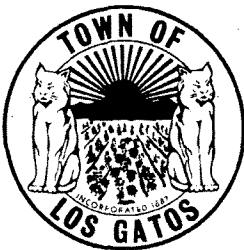
This budget report is not a project defined under CEQA, and no further action is required.

FISCAL IMPACT:

The attached First Quarter Budget Performance Report includes a section providing a detailed list of recommended expenditure and revenue budget adjustments recommended for the first quarter of FY 2007/08. Upon approval of the recommended budget adjustments by Town Council, the adopted appropriations for the fiscal year will be adjusted accordingly.

Attachments:

Budget Performance Report for the Three Months Ended September 30, 2007



# **TOWN OF LOS GATOS BUDGET PERFORMANCE REPORT FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2007**

October 15, 2007

## **FINANCIAL OVERVIEW – EXECUTIVE SUMMARY**

### **Status of FY 2007/08 Adopted Budget:**

First Quarter results are trending positively overall, with revenue collections on pace with amounts collected the prior year. Despite the loss in recent years of three automobile dealerships, sales tax receipts for the first quarter are trending slightly ahead of collections for the prior year. The chief reasons for this are the continued success of one internet commerce retailer and a solar energy retailer, whose continued growth has allowed the Town to sustain the loss of three of top ten businesses in the Town's portfolio of sales tax generators. Another favorable trend is the continued economic recovery of the downtown. Sales tax collections, excluding new car sales, for the quarter ending June 30, 2007 (the most recent quarter available) were up approximately 1.5 % for the prior year. Restaurant sales taxes for the period were the highest generated in the past two years, up 6.5 % from the prior year.

Department expenditure totals for the first quarter FY 2007/08 are also trending favorably, with spending at the end of the first quarter averaging 21% expended, or 4% below the 25% benchmark level used for three months of 12 months operations. With only three months of data available, it is difficult to predict revenues and expenditures for the whole year. The uncertainty of the economic effects of potential rises in energy costs or a more dramatic downturn in the local real estate market may impact consumer behavior. In light of this uncertainty and being fully aware that the local economy's recovery remains vulnerable, staff continues to be cautiously optimistic while monitoring fiscal developments very closely. Consequently, further adjustments may be necessary during the fiscal year. Any mid-year course corrections or budget adjustments necessary to balance operating revenue and expenditures will be brought to Town Council's attention at the earliest opportunity.

### **State Budget Fiscal Impacts to Town for FY 2007/08:**

Highlights from the FY 2007/08 state budget package are the following:

***No Additional State Property Tax Shifts Enacted -Proposition 1A and its Influence on the State Budget Process*** –With the successful passage in November 2004 of Proposition 1A restrictions exist on future legislative authority to reduce or reallocate local revenues from the sales tax, property tax, or vehicle license fee (VLF). Namely, the state is prevented from:

- Reducing local sales tax rates or altering the method of allocation
- Shifting property taxes from the Town to fund other state programs
- Decreasing VLF revenues without providing replacement funding
- Enforcing unreimbursed mandates (with certain exceptions)

Proposition 1A prohibits further state revenue "takes" from local government as itemized above. However, Proposition 1A contains provisions for additional state revenue "takes." Specifically, starting in FY 2008/09, in an emergency and by a vote of two-thirds of both houses of the Legislature and the approval of the Governor, the Town's share of property tax could be "taken" or shifted to state programs. It must be repaid, with interest, within three years. The state could also approve voluntary exchanges of sales and property tax revenues among local governments within a county. These transfers of taxes and funds would not need voter approval. With this in mind, it is important to note that currently the State is facing a projected \$3.4 billion shortfall for FY 2008/09 and another \$2.5 billion for FY 2009/10.

***Property Taxes Shift to K-14 District*** – While the FY 2006/07 state budget bill ended the two year \$1.3 billion property tax shifts from cities, counties, special districts, and redevelopment agencies to K-14 district schools for the fiscal benefit of the state, the FY 2007/08 budget was balanced without a recommended property tax shift. The state continues to project future budget deficits, so local government finance should never be considered immune from the potential of future state revenue takes.

***Status of Proposition 42 Transportation Funding*** – The FY 2007/08 state budget bill provides no Proposition 42 funds for local streets and roads because cities received funding in two prior fiscal years when other state transportation programs did not. On a positive note, beginning in FY 2008/09, cities and counties will receive approximately double their allocations if Proposition 42 is funded in the state budget. The Town's share is estimated to be approximately \$297,000 in FY 2008/09.

***State Mandates*** – The FY 2007/08 does not include funding for mandated claims incurred by the Town this fiscal year. However, a trailer bill was passed appropriating the full payable amount in the annual state budget for mandates for which costs were incurred in the prior year. Thus, claims for FY 2007/08 will be paid in the state FY 2008/09 budget. The cost reimbursements are for Town costs related to state mandated activities such as certain public safety regulations, investment reporting, and Open Meetings Act, among others.

***Restores Booking Fee Authority and Reimbursements*** – The State budget bill appropriated \$35 million for county sheriffs for local detention facilities and prohibits counties from charging jail booking fees to cities or other local agencies. Counties will have the authority to charge a new "jail access fee" for bookings in excess of an agency's three year average for low-level offenses.

#### **Effects of State Budget Package on FY 2007/08 Operating Revenues:**

The changes to Town revenue structure first implemented as budget adjustments in FY 2004/05 are recapped below for purposes of clarification and comparison:

**Sales Tax** – The Sales Tax revenue estimate is \$8.2 million for FY 2007/08. The state's Economic Recovery Bonds, approved by the voters in March 2004, were secured by a pledge of revenues from an increase in the state's share of the sales and use tax of one-quarter cent beginning July 1, 2004. The Town's one per cent local share of the tax was reduced by one quarter and, in exchange, the Town receives an equal amount of property shifted from state property tax collections during the term the one-quarter cent is being used by the State to pay off the bonds (estimated to be between 9 and 14 years). Effects on the current year budgeted amounts are shown below:

<b>Revenue Type</b>	<b>FY 2007/08 Adopted</b>	<b>FY 2007/08 Post State Budget After Implementation of "Triple Flip" Effective 7/1/2004</b>
Sales Tax	\$5,920,200	Rate of 1% of 8.25% changed under budget bill to (.75% of 8.25% sales tax rate) for a period of between 9 and 14 years.
Sales Tax Replaced With Property Tax	\$2,310,900	(.25% of 8.25% sales tax rate) This amount now is dedicated to the state, but the "triple flip" provisions of the state budget bill (SB 1096) replaces the lost Town sales tax with additional state property tax to make the Town "whole." The amounts are paid twice annually by County of Santa Clara with a final settlement paid in August following the fiscal year.
Totals	\$8,231,100	Total Sales Tax and Replacement Property Tax

**Motor Vehicle License Fees (VLF-"Car Tax")** –The budget package permanently replaces the Town's backfill revenues with an equal amount of property taxes paid out of the state General Fund.

<b>Revenue Type</b>	<b>FY 2007/08 Budgeted</b>	<b>FY 2007/08 Post State Budget After Implementation of "Triple Flip" Effective 7/1/2004</b>
Car Tax-Remaining Town Share	\$163,200	Rate reduced legislatively to 1/3 <sup>rd</sup> of the former rate (2.0%). This tax is constitutionally dedicated to local government. The Town continues to receive the tax collected, but at the reduced 1/3 <sup>rd</sup> level (.65%).
Car Tax Backfill Eliminated and Replaced By an Equal Amount of Property Tax	\$2,030,360	The budget package permanently replaces the Town's VLF backfill revenues with an equal amount of property taxes paid "in lieu" of car tax revenue out of the property taxes forwarded by the County to the State's General Fund.
Totals	\$2,193,560	Total VLF and Replacement Property Tax

**Prior Fiscal Year Closing Results:**

The FY 2006/07 closing financial results continue to affirm the positive effects of the Town's pro-active budgetary actions taken in response to the continuing flat revenue growth or downturns in key operating revenues the Town experienced since FY 2001/02. In developing the FY 2006/07 "status quo" budget, Town Council approved a combination of budgetary initiatives that held the line on service level delivery coupled with revenue adjustments in the Town's "Charges for Services" category. The bulk of these fees are to recover costs related to private development activity aligning fees charged for services with the current cost incurred by the Town. This strategy coupled with the effect of Town-wide expenditure reduction strategies continued from prior years and other revenue gains like continued strong performance by Netflix sales tax generated a favorable General Fund closing balance of approximately \$4.8 million of available revenues over expenditures at fiscal year end June 30, 2007. This balance was reduced by



approximately \$4.2 million to provide funding for approved capital projects, resulting in excess revenue above expenditures for FY 2006/07 of approximately \$680,000.

The Town's General Fund reserves closed the year (unaudited) at a total of approximately \$19.0 million (including the Town's Reserve for Economic Uncertainty intact at \$3,678,000), compared to \$18.1 million balance upon the close of the prior year, an increase of approximately \$900K in total General Fund reserves.

The following factors were key in contributing to the \$4.8 million in General Fund revenues above expenditures for the fiscal year, before this amount was reduced by \$4.2 million to fund approved capital projects:

- Sales tax revenue final collections exceeded mid-year estimates by approximately \$1.1 million due primarily to stronger than expected performance by Netflix.
- Plan check and building permit fees were approximately \$795,000 above estimates made at mid-year FY2006/07. Revenues collected last year for work to be performed in this fiscal year were recorded as unearned revenue, earmarked as such in the General Fund, and accordingly were not included in the determination of revenues available for reserve designation at fiscal year end.
- Investment earnings exceeded mid-year estimates by approximately \$935,000 largely due to increases in the overall interest yield market.
- General fund expenditures were approximately \$530,000 below the approved adjusted budget levels for FY 2006/07.
- Property taxes collected exceeded mid-year estimates by approximately \$125,000 due to continued turnover of Town properties and their attendant new valuations.

It should be emphasized that operating revenues for FY 2006/07 included \$300,000 in funds which had accumulated as a liability from prior years but were not used for PERS costs. These revenues were used to offset the large PERS increases which have occurred during the recent downturn in the economy. Currently the Town's strategy is to use these accumulated PERS rebate funds to establish a cost/revenue smoothing effect over the next 5 to 10 years.

In each fiscal year it is likely that the Town's cost of services will be impacted by scheduled labor and benefit cost increases and other operating expenditure increases. It is reasonable to anticipate these costs to trend upward in the future if for no other reason than inflationary pressures. This reality will continue to require strong performance in the Town's economically-sensitive revenues to offset the cost increases likely to occur. The Town's efforts over the past five years, including expenditure reductions, alignment of user fees to cost of service delivery, operational reviews and service level adjustments, along with ongoing efficiency efforts have allowed the Town's revenue base to keep pace with the cost of providing services and provide funding for much needed capital improvements such as road resurfacing, sidewalk repairs, retaining walls, and trail and park facility refurbishments.

#### **General Fund Reserve Status – June 30, 2007**

General Fund reserves are classified into two categories - Restricted and Designated. Restricted reserves are those which are restricted in use by accounting standards or legal agreements and are not considered as available for use for another purpose. Designated reserves are established by Council policy for an intended purpose. Currently Restricted Reserves in the General Fund are approximately \$4.7 million as presented below.

<b><i>Restricted General Fund Reserves:</i></b>	<b><i>Amount</i></b>
Reserved for RDA Loan	\$4,220,000
Reserved for LT Notes Receivable	512,394
Reserved for Grant Funds & Carryovers	(5,818)
<b>Total Restricted General Fund Reserves</b>	<b>\$4,726,576</b>

As stated earlier the total General Fund Reserves closed at a balance of approximately \$19.0 million at June 30, 2007. In addition to the approximate \$4.7 million of General Fund Reserves set aside for restricted purposes, the Town has approximately \$14.3 million in designated reserves established in accordance with Town financial policies and operating and capital budget requirements. The Designated Reserves presented below include the newly established Revenue Stabilization Reserve created by the Town upon the adoption of the FY 2005/06 budget.

<b><i>Designated Reserves:</i></b>	
Designated for Revenue Stabilization	\$4,817,445
Designated for Capital & Special Projects	4,325,011
Designated for Economic Uncertainty	3,678,001
Designated for Civic Center Improvements	663,086
Designated for Open Space	562,000
Designated for Mgr's Contingency & Prod.	200,000
Designated for Authorized Carryforwards	31,910
<b>Total Designated Reserves</b>	<b>\$14,277,453</b>

The Reserve for Capital and Special projects, whose source is derived from half of the annual available General Fund budget savings, serves as the primary source for replenishment to the Town's Capital Improvement Fund (GFAR) in addition to the annual budgeted transfer from the General Fund's operations of \$150,000. As such, it represents the source for a large number of unfunded needs identified during the annual capital improvement plan process. This reserve also functions as a potential funding source for new capital projects or augmentations to authorized projects funded through the Town's Five Year Capital Improvement Program (CIP). The Town continues to be challenged in identifying an ongoing source of funds to meet the annual \$1.5 million recommended for the street repair and maintenance program and other priority infrastructure improvements such as sidewalk repair and replacement.

The Revenue Stabilization Reserve was established to serve as a transitional or "bridge" funding source that could be used to mitigate or smooth out cyclical ups and downs in locally generated revenues due to temporary downturns in the local economy or "one-time" revenue losses where recovery of the revenue base is deemed likely to be restored in the near future.

In its public communications, staff refers to the \$14.3 million in Designated General Fund reserves as the Town's "reserves" since these are established by Council policy for their intended purpose. The availability of approximately \$14.3 million in Designated General Fund reserves provides the Town with resources to manage through future fiscal challenges and opportunities, mindful of the many competing priorities for resource allocation, ranging from restoration of core services to the community to a large amount of unfunded capital improvements.

## **GENERAL FUND - KEY REVENUE ANALYSIS FY 2007/08**

The following provides the status of significant General Fund revenue sources as of the first quarter ending September 30, 2007. Staff monitors each revenue source closely and at this time recommends certain revenue adjustments based on revenue actuals or state budget actions. Adjustments necessary (if any) will be brought forward to Town Council for approval at mid-year (approximately February 2008), when more revenue data is available.

### ◆ Sales Tax Revenue ◆

Los Gatos Sales Tax Revenue receipts are a result of a formula that allocates 1.0 cent of the 8.25 cents of local sales tax collected per \$1 dollar of sales by merchants on retail sales and taxable services transacted within the Town of Los Gatos.

Under the "triple flip" allocation now in effect, the State Board of Equalization reallocates .25 cents of the 1.0 cents share Los Gatos receives, and replaces it with an equal amount of property tax revenue. Sales Tax revenues are remitted to the Town on a monthly basis and placed in the General Fund for use in general operations.

#### Quarterly Analysis

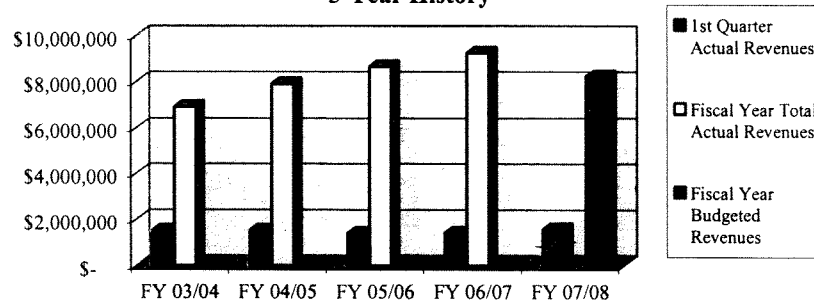
According to California's Department of Finance, California's economy is showing signs of slowing with the cooling of the housing market. A fall-off in real estate activity is expected to trickle down to decreases in the State's related labor and retail markets. In addition, the decrease in gasoline prices

since August is reflected in lower than expected receipts for the State. More data will become available as the fiscal year progresses.

First quarter Sales Tax revenues are slightly above last year's 1<sup>st</sup> quarter receipts, however as revenue timing is inconsistent from year to year, 1<sup>st</sup> quarter receipts do not provide sufficient data for annual revenue analysis. Because of strong performance by other tax generators like Netflix, this revenue category has absorbed the loss of three automobile dealers in recent years. However, this revenue continues to be vulnerable to the loss of other large Sales Tax generating businesses located in the Town.

To offset the vulnerability resulting from one vendor responsible for a sizeable portion of the Sales Tax Revenue, the Town should continue to seek a more balanced portfolio of business sectors to generate sales tax.

**Quarterly and Annual Revenues  
5-Year History**



	<u>FY 03/04</u>	<u>FY 04/05</u>	<u>FY 05/06</u>	<u>FY 06/07</u>	<u>FY 07/08</u>
1st Quarter Actual Revenues	\$ 1,515,570	\$ 1,514,045	\$ 1,392,150	\$ 1,407,997	\$ 1,568,805
Fiscal Year Total Actual Revenues	\$ 6,914,526	\$ 7,904,130	\$ 8,655,565	\$ 9,253,891	
Fiscal Year Budgeted Revenues					\$ 8,231,100

*FY 2004/05 forward will reflect the Sales Tax In Lieu paid by Santa Clara County*

1st Quarter Percent of Total	21.92%	19.16%	16.08%	15.22%	19.06%
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**Recommended Budget Revision**

**No Change**

### ◆ Property Tax Revenue ◆

Property Tax Revenue accounts for 21.7% of the Town's budgeted General Fund revenues for FY 2007/08. As Property Tax distributions are largely received in the third and fourth quarters of a fiscal year, the revenue receipts are not reflected proportionately in the chart below, by quarter.

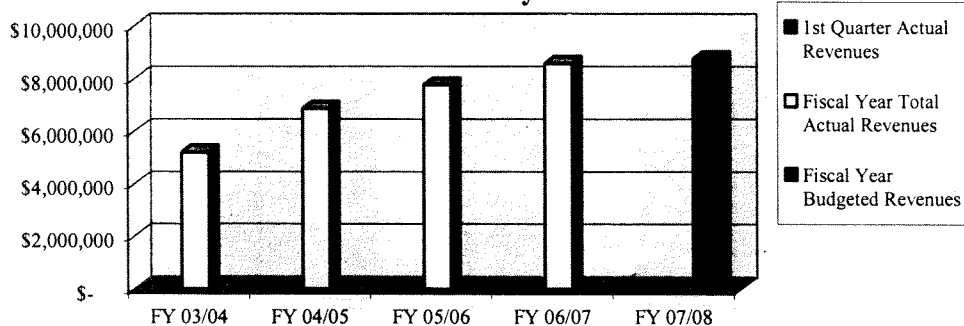
The passage of California's Proposition 13 in 1978 limited both the tax rate that can be levied on property to 1% rate of a property's assessed value (*plus voter approved bonds, service fees, improvement bonds, and special assessments*) and established a property's original tax base as its 1975/76 assessed value. The assessed value is subsequently adjusted by no more than a two percent inflation factor thereafter until the property changes hands or new construction occurs.

The Town currently receives approximately 9.5 cents of each dollar paid to the Assessor's Office. Once ownership changes, property is reassessed to its current market value, meaning real property values critically impact revenues.

#### Quarterly Analysis

First quarter tax receipts do not provide enough data for analysis as the majority of property tax revenues are received later in the fiscal year. Of note however, is that the Santa Clara County Assessor continues to provide a positive growth outlook in its FY2007/08 Annual Report, even with the expectation that the housing market is cooling. All cities continued to show positive growth over the last year, with Los Gatos experiencing an overall 8% increase in assessed value in FY 2006/7

**Quarterly and Annual Revenues  
5-Year History**



	FY 03/04	FY 04/05	FY 05/06	FY 06/07	FY 07/08
1st Quarter Actual Revenues	\$ 86,045	\$ 102,035	\$ 105,271	\$ 75,831	\$ 138,916
Fiscal Year Total Actual Revenues	\$ 5,207,381	\$ 6,856,993	\$ 7,755,200	\$ 8,584,612	
Fiscal Year Budgeted Revenues					\$ 8,757,580
<i>FY 2004/05 forward will reflect an increase in Property Tax due to "Permanent" Realignment of VLF</i>					
1st Quarter Percent of Total	1.65%	1.49%	1.36%	0.88%	1.59%

**Recommended Budget Revision**

**No Change**

### ◆ *Transient Occupancy Tax* ◆

The Town of Los Gatos levies a 10 per cent Transient Occupancy Tax (TOT) on hotel/motel rooms within Town limits as a funding source for Town services and infrastructure provided to transitory lodgers and visitors.

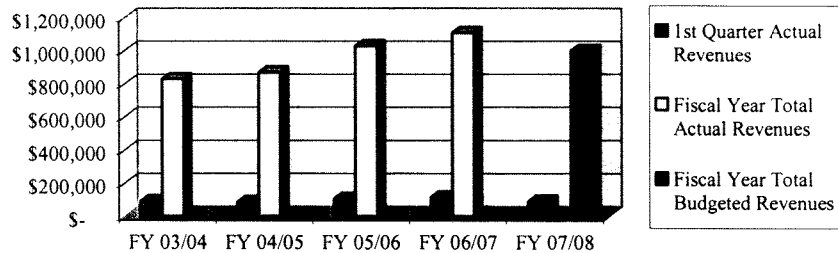
#### Quarterly Analysis

FY 2007/08 budget projections were decreased from the prior year due to the closure of two hoteliers in recent years (Village Inn and Villa Felice). Staff expects that TOT revenues will meet budgeted levels

by year end. FY 2006/07 year end results supports recent market research that both business and leisure travel continue to recover in California. Research data suggests high gas prices led more Californians to vacation closer to home during the summer months.

For the remainder of the fiscal year, the Town expects occupancy rates to remain as projected in line with seasonal changes.

**Quarterly and Annual Revenues  
5-Year History**



	<u>FY 03/04</u>	<u>FY 04/05</u>	<u>FY 05/06</u>	<u>FY 06/07</u>	<u>FY 07/08</u>
1st Quarter Actual Revenues	\$ 91,170	\$ 87,668	\$ 107,529	\$ 116,118	\$ 90,367
Fiscal Year Total Actual Revenues	\$ 829,025	\$ 868,908	\$ 1,028,664	\$ 1,108,257	
Fiscal Year Total Budgeted Revenues					\$ 1,000,000
1st Quarter Revenue Percent of Total	11.00%	10.09%	10.45%	10.48%	9.04%

<b>Recommended Budget Revision</b>	<b>No Change</b>
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◆ **Interest Income Revenue** ◆

The Town earns interest revenue through the investment of cash not immediately required for daily operations in various money market instruments. Investments are overseen by the Elected Town Treasurer, within parameters as stated in the Investment Policy approved by the Town Council. The Town's goal is to achieve a competitive rate of return while protecting the safety of those funds.

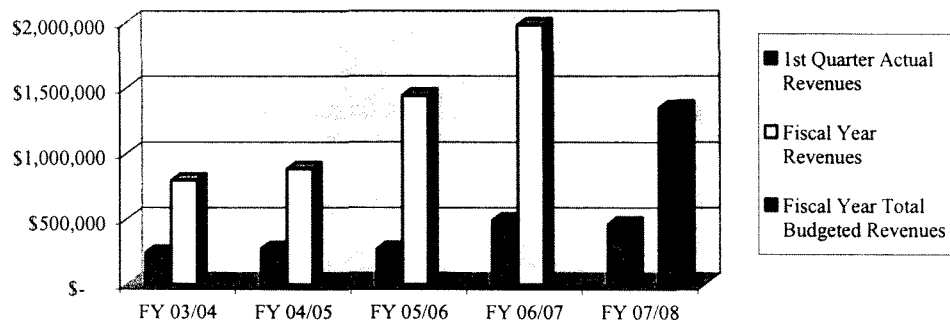
The Town's Interest Income revenue is primarily dependent upon two factors: the cash balance in the Town's investment portfolio, and the yield received on those funds.

**Quarterly Analysis**

Interest Income earnings have been impacted positively in recent years by both a significant increase in the Town's cash balances, and a general improvement in interest rates from investments.

Current year interest revenues reflect significantly higher first quarter earnings than in previous years due to increases in investment returns and the Local Agency Investment Fund (LAIF) rate. LAIF yields have risen to an average yield of 5.231% in September 2007, from 5.023% in September of last year, and from its record low of 1.42% in May 2004.

**Quarterly and Annual Revenues  
5-Year History**



	FY 03/04	FY 04/05	FY 05/06	FY 06/07	FY 07/08
1st Quarter Actual Revenues	\$ 242,485	\$ 276,278	\$ 272,325	\$ 489,730	\$ 461,635
Fiscal Year Revenues	\$ 795,488	\$ 884,203	\$ 1,439,685	\$ 1,977,233	
Fiscal Year Total Budgeted Revenues					\$ 1,348,300
1st Quarter Revenue Percent of Total	30.5%	31.2%	18.9%	24.8%	34.2%
<b>Recommended Budget Revision</b>	<b>No Change</b>				

◆ **Business License Tax Revenue** ◆

The Town of Los Gatos requires businesses to pay an annual Business License Tax if a business is located within Town limits, or if an agent of a business conducts operations within Town limits.

The Business License Tax fees are based on the type of business activity. Retail sales, wholesale, and manufacturing businesses are charged on a sliding scale based on their annual gross receipts, and comprise approximately 40% of the Business License Tax revenue. Other businesses, such as contractors, professionals, and services, are based on flat fees as set forth in the Town Code, and make up the remaining 60% of revenue.

Annual business license renewals are due and payable in advance on January 2<sup>nd</sup> of each year.

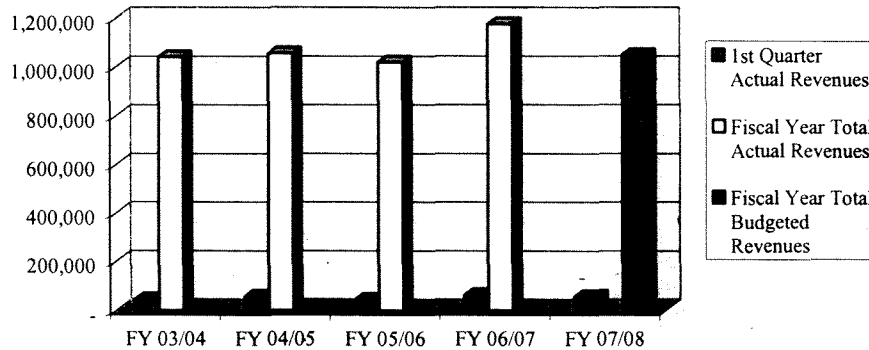
New business license applications for flat-fee based businesses are pro-rated by quarter, from the date of application to the end of the year.

**Quarterly Analysis**

The Business License Tax revenue received in the first quarter is largely comprised of prorated tax fees charged on new businesses, and assessments stemming from business tax audits. The majority of the business tax revenue comes from the annual renewals, which are primarily received in the second and third quarters of the fiscal year.

First quarter receipts are tracking comparably with the same period in the prior year. No significant deviations from annual projections are expected at this point.

**Quarterly and Annual Revenues  
5-Year History**



	FY 03/04	FY 04/05	FY 05/06	FY 06/07	FY 07/08
1st Quarter Actual Revenues	45,619	56,632	42,402	63,057	55,900
Fiscal Year Total Actual Revenues	\$ 1,041,865	\$ 1,056,814	\$ 1,019,386	\$ 1,176,422	
Fiscal Year Total Budgeted Revenues					\$ 1,050,000
1st Quarter Revenue Percent of Total	4.38%	5.36%	4.16%	5.36%	5.32%
<b>Recommended Budget Revision</b>					<b>No Change</b>



◆ **Franchise Fee** ◆

The Town collects franchise fees on privately owned utility companies for the privilege of using Town streets and right-of-ways, and as a fee in lieu of the business license tax. Franchise Fees are currently received from Comcast for cable television services, PG&E for gas and electric service, and Green Valley for solid waste collection services.

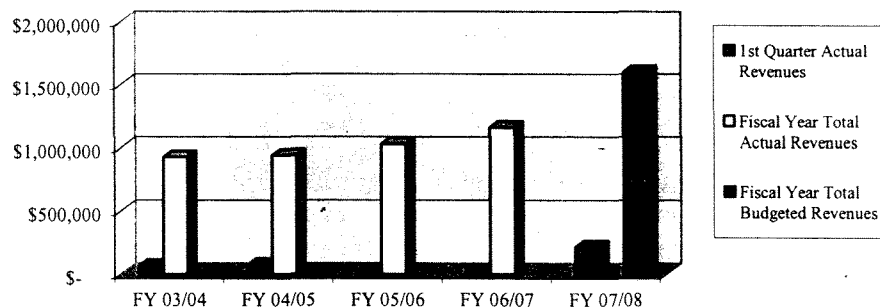
**Quarterly Analysis**

Franchise Fees revenues are received at varying times throughout the year. PG&E pays an annual fee in the 4<sup>th</sup> quarter, Comcast pays quarterly, with actual receipts received following quarter end, and Green Valley is scheduled to pay monthly. Receipts shown in this report are for the first two months, July and August and the September remittances will be received during October.

First quarter receipts reflect 11% increase over the same period last year. This increase is a result of a rate change for garbage. This increase was built in at the time the budget was developed. It does not represent additional or incremental revenue.

Future cable television franchise fees may be impacted as a result of the adoption of AB 2987, the Digital Infrastructure and Video Competition Act of 2006. This bill allows telephone and cable companies to enter into state franchise agreements in lieu of local agreements. Currently, local agencies are authorized to charge a local franchise fee of up to 5% of the cable operator's gross revenues as rent for the commercial use of the public right-of-way. AB 2897 replaces this local franchise fee with what is essentially a state tax that will be paid to local agencies (at least for the time being). The Town is working with AT&T who now has a small cable customer base in Town. The revenue from this segment is not expected to be significant in the short term. Comcast who is the Town's cable provider is yet to apply to the Public Utilities Commission for state franchise. Staff estimates that once a state franchise agreement is reached between the state and Comcast, the Town's franchise receipts will be reduced by at least \$30,000.

**Quarterly and Annual Revenues  
5-Year History**



	FY 03/04	FY 04/05	FY 05/06	FY 06/07	FY 07/08
1st Quarter Actual Revenues	\$ 66,174	\$ 74,273	\$ 22,702	\$ 28,661	\$ 215,985
Fiscal Year Total Actual Revenues	\$ 930,997	\$ 942,647	\$ 1,030,189	\$ 1,162,037	
Fiscal Year Total Budgeted Revenues					\$ 1,603,180
<i>FY 2005/06 Total Actual Revenues reflect increased revenue based on Audit for Prior Years performed by Town</i>					
1st Quarter Revenue Percent of Total	7.11%	7.88%	2.20%	2.47%	13.47%

**Recommended Budget Revision**

**No Change**

## **RECOMMENDED BUDGET ADJUSTMENTS**

### **FY 2007/08 Expenditure Appropriations Adjustments**

Budget adjustments are recommended for the following revenues and expenditures at the first quarter as described below:

#### *Financial Systems Upgrade Project (GFAR Fund) - \$50,000*

Staff is anticipating a spring 2008 implementation of a significant part of the Town's new financial system (Pentamation Plus). The project had been suspended during the vacancy of the Finance Manager position, but now is ready to begin again. To better serve the Town's customers, one of the primary goals is to provide a mechanism for e-business through the web. To facilitate this goal, Pentamation has advised staff to upgrade its current Pentamation servers. This upgrade was not a part of the original project budget. The recommended budget adjustment will be funded through a \$50,000 transfer of available fund balance in the Town's MIS fund.

#### *Finance Department: Finance System Upgrade Temporary Help (General Fund) - \$10,000*

To assist the implementation goals of this project, staff recommends an increase in temporary staff dollars to provide assistance during the financial system conversion. Temporary support will be utilized to provide a variety of support tasks, including counter coverage during staff training sessions on the new system, database setup, data conversion, and user training.

### **FY 2007/08 Estimated Revenues Recommended Adjustments:**

#### *Grants Fund Program (Grants Fund) - \$4,444*

Staff recommends grant revenues and the related grant expenditure budget be increased to recognize additional federal Homeland Security Grant Funds made available to the Town in FY 2007/08.

## **FINANCIAL SUMMARIES, PROJECTIONS AND RECOMMENDATIONS**

### *General Fund*

The following page presents the *Schedule of FY 07/08 General Fund Operating Revenues vs. Operating Expenditures* for the first quarter and comparison information from the prior year. In the last column, the Finance Department projects final balances for the fiscal year based upon the early trends observed through the first quarter.

**Town of Los Gatos**  
**Schedule of General Fund**  
**Operating Revenues vs. Operating Expenditures**  
**For the period ended September 30, 2007**

	Unaudited FY06/07 Final Balance	FY06/07 Adjusted Budget	FY06/07 1st Qtr Actuals	FY06/07 % YTD	FY07/08 Adopted Budget	FY07/08 Adjusted Budget	FY07/08 1st Qtr Actuals	FY07/08 % YTD	FY07/08 Finance Projection
<b>Revenues</b>									
General Property Tax	\$ 6,594,058	\$ 6,469,900	\$ 75,830	1%	\$ 6,727,220	\$ 6,727,220	\$ 138,917	2%	\$ 6,727,220
Prop Tax Car Tax Backfill	1,990,555	1,990,550	-	-	2,030,360	2,030,360	-	0%	\$ 2,030,360
Sales & Use Tax	9,253,891	8,100,140	1,407,996	17%	8,231,100	8,231,100	1,568,805	19%	\$ 8,231,100
Franchise Fees	1,162,038	1,238,940	28,661	2%	1,603,180	1,603,180	215,985	13%	\$ 1,603,180
Transient Occ Tax	1,108,257	1,000,000	116,118	12%	1,000,000	1,000,000	90,368	9%	\$ 1,000,000
Business License Tax	1,176,442	1,000,000	62,705	6%	1,050,000	1,050,000	55,900	5%	\$ 1,050,000
Licenses & Permits	1,541,302	1,616,000	959,973	59%	1,930,400	1,930,400	928,493	48%	\$ 1,930,400
Motor Vehicle In Lieu	194,104	152,700	80,110	52%	163,200	163,200	42,577	26%	\$ 163,200
Intergovernmental	2,058,576	2,062,432	305,127	15%	2,004,825	2,004,825	320,168	16%	\$ 2,004,825
Charges for Services	3,967,735	3,221,390	770,093	24%	3,371,470	3,371,470	675,772	20%	\$ 3,371,470
Fines & Forfeitures	561,665	455,900	96,280	21%	525,405	525,405	66,107	13%	\$ 525,405
Interest	2,127,234	1,705,700	467,731	27%	1,498,300	1,498,300	461,635	31%	\$ 1,498,300
GASB investment to market per audit	448,828	-	-	-	-	-	-	-	-
Miscellaneous Other	320,614	206,800	148,272	72%	267,230	267,230	164,953	62%	267,230
Fund Transfers	114,471	221,850	44,515	20%	184,110	184,110	37,793	-	184,110
<b>Total Revenues</b>	<b>\$ 32,619,770</b>	<b>\$ 29,442,302</b>	<b>\$ 4,563,411</b>	<b>15%</b>	<b>\$ 30,586,800</b>	<b>\$ 30,586,800</b>	<b>\$ 4,767,472</b>	<b>16%</b>	<b>\$ 30,586,800</b>
<b>Use of Other Funding Sources:</b>									
Reserves	4,179,094	-	318,710	-	525,000	525,000	525,000	-	525,000
PERS Liability Account	300,000	300,000	300,000	-	300,000	300,000	300,000	-	300,000
Use of Internal Service Reserves - Yr 3	-	-	-	-	-	-	-	-	-
<b>Total Other Funding Sources</b>	<b>4,479,094</b>	<b>300,000</b>	<b>618,710</b>		<b>825,000</b>	<b>825,000</b>	<b>825,000</b>		<b>825,000</b>
<b>Total Revenues plus Reserves</b>	<b>\$ 37,098,864</b>	<b>\$ 29,742,302</b>	<b>\$ 5,182,121</b>		<b>\$ 31,411,800</b>	<b>\$ 31,411,800</b>	<b>\$ 5,592,472</b>		<b>\$ 31,411,800</b>
<b>Expenditures (includes c/f but no encumbrances)</b>									
Mayor & Council	150,379	161,130	33,311	21%	169,500	169,500	34,541	20%	169,500
Treasurer	102,713	98,150	17,222	18%	106,650	106,650	20,735	19%	106,650
Attorney	234,828	245,450	52,972	22%	257,750	257,750	48,388	19%	257,750
Administrative Services	2,307,354	2,338,010	552,573	24%	2,442,300	2,442,300	542,155	22%	2,442,300
Comm Development	2,936,351	3,246,500	796,875	25%	3,656,585	3,656,585	574,651	16%	3,656,585
Police	11,628,108	11,625,576	2,836,257	24%	11,958,720	11,966,180	2,678,313	22%	11,966,180
Parks & Public Works	4,988,746	4,967,350	1,342,078	27%	5,255,750	5,255,750	1,118,653	21%	5,255,750
Community Services	1,943,843	982,065	190,213	19%	1,032,772	1,032,772	216,561	21%	1,032,772
Library	1,914,247	1,989,660	499,401	25%	2,056,810	2,066,260	460,138	22%	2,066,260
<b>Total Dept Expenses</b>	<b>\$ 26,206,569</b>	<b>\$ 25,653,891</b>	<b>\$ 6,320,901</b>	<b>25%</b>	<b>\$ 26,936,837</b>	<b>\$ 26,953,747</b>	<b>\$ 5,694,135</b>	<b>21%</b>	<b>\$ 26,953,747</b>
<b>Non-Dept Expenditures and other uses</b>									
General Government	6,031,556	6,659,148	812,085	12%	3,571,800	3,586,800	843,550	24%	3,586,800
<b>Total Non-Dept Expenses</b>	<b>\$ 6,031,556</b>	<b>\$ 6,659,148</b>	<b>\$ 812,085</b>	<b>12%</b>	<b>\$ 3,571,800</b>	<b>\$ 3,586,800</b>	<b>\$ 843,550</b>	<b>24%</b>	<b>\$ 3,586,800</b>
<b>Total Operating Expenditures</b>	<b>\$ 32,238,125</b>	<b>\$ 32,313,039</b>	<b>\$ 7,132,986</b>	<b>22%</b>	<b>\$ 30,508,637</b>	<b>\$ 30,540,547</b>	<b>\$ 6,537,685</b>	<b>21%</b>	<b>\$ 30,540,547</b>
<b>Net Operating Revenues Before Capital Trsfrs</b>									
<b>&amp; Budgeted Beg Fund Balance</b>	<b>\$ 4,860,739</b>	<b>\$ (2,570,737)</b>	<b>\$ (1,950,865)</b>		<b>\$ 903,163</b>	<b>\$ 871,253</b>	<b>\$ (945,213)</b>	<b>N/A</b>	<b>\$ 871,253</b>
<b>Authorized Use of Reserves</b>									
Capital Projects	4,179,094	-	318,710	-	525,000	525,000	525,000	-	525,000
<b>Total Budgeted Use of Reserves</b>	<b>4,179,094</b>	<b>-</b>	<b>318,710</b>	<b>-</b>	<b>525,000</b>	<b>525,000</b>	<b>525,000</b>	<b>-</b>	<b>525,000</b>
<b>Net Surplus or (Use) of Reserves</b>	<b>681,645</b>	<b>(2,570,737)</b>	<b>(2,269,575)</b>		<b>378,163</b>	<b>346,253</b>	<b>(1,470,213)</b>		<b>346,253</b>

**Guide to Presentation:**

Each of the following groups of financial summaries present data by governmental fund type - the types are Special Revenue Funds, Capital Projects Funds, Internal Service Funds, and Redevelopment Agency Funds. In each of the following projections a similar format is presented. The fund information starts with beginning fund balances and adds current year revenues and subtracts current year expenditures resulting in ending fund balance. Budget amounts are also provided for revenues and expenditures, useful for comparing actual amounts received or spent to date versus budget for FY 2007/08.

**Special Revenue Fund** – Special Revenue Funds, which account for the proceeds derived from specific revenue sources that are legally restricted or assigned to special purposes including the Town's Parking Fund, Solid Waste Fund, Community Development Block Grant Fund, Non Point Source Fund, Landscaping and Lighting District Funds, and the Operating Grants Fund.

Of special note, here is the Parking Fund, which continues to indicate revenue shortfalls wherein costs of parking administration and enforcement are exceeding citation revenues. Citation revenues have been reduced due to personnel injuries, other public safety support priorities which have pulled staffing off parking enforcement, and an unanticipated length of time to successfully fill a Parking Control Officer vacancy. The department expects revenue citation revenue to be restored to more normal levels in the near future. The budgeted General Fund subsidy for this program for the fiscal year is \$184,260 to balance operating revenues with operating expenditures. Staff is continuing to evaluate this program, as any shortfall in this fund must be covered at year-end with a transfer from the Town's General Fund.

Special Revenue Funds Budget to Actuals Comparisons						
	Parking Fund	Solid Waste	CDBG Grants	Non Point Source	LIDs	Operating Grants
Beginning Fund Balance (Pre-audit)	-	338,850	802,076	108,289	97,491	(5,818)
Budgeted Revenues	555,860	346,384	210,643	172,010	36,170	-
Actual Revenues - 1st Qtr	23,009	15,000	6,890	166,660	33,557	4,445
Budgeted Expenditures	555,860	396,384	421,293	180,940	43,290	-
Total Actual Expenditures - 1st Qtr	92,927	34,906	3,281	61,072	12,071	-
1st Quarter Ending Fund Balance	(69,918)	318,943	805,685	213,878	118,977	(1,373)

**Capital Projects Funds** – Capital Projects Funds are utilized to account for resources used for acquisition and construction of capital facilities by the Town. Funds included in this category are the GFAR Fund (General Fund Appropriated Reserve), Traffic Mitigation Fees Fund, Grant Funded CIP's Fund, Storm Drains Fund, Utility Undergrounding Fund, and the Gas Tax Fund. Capital Project Funds are tracking in accordance with the FY 2007/08 adopted budget. Staff is recommending no changes at this time.

If operating revenues will support it, the FY 2007/08 budget includes a General Fund's current year transfer of designated Future Year's Capital & Special Projects reserves in the amount of \$525,000 in support of the first year of the Town's adopted Five-Year Capital Improvement Plan.

The Grant Funded CIP fund displays a deficit balance because this grant fund expends Town dollars first, then provides documentation of these expenditures to the State of California or other granting agencies and is reimbursed for those costs, which eventually should result with the fund "breaking even" or a zero fund balance (Dollars expended equal dollars received back in grant reimbursements).

**Capital Project Funds  
Budget to Actuals Comparisons**

	<b>GFAR Fund</b>	<b>Traffic Mitigation</b>	<b>Grant Fund CIP's</b>	<b>Storm Drains</b>	<b>Utility Undergd</b>	<b>Gas Tax</b>
<b>Beginning Fund Balance</b>	<b>6,245,816</b>	<b>93,491</b>	<b>(141,453)</b>	<b>805,284</b>	<b>2,269,147</b>	<b>903,833</b>
Budgeted Revenues	1,210,240	50,000	3,864,244	132,470	140,220	565,710
<b>Actual Revenues - 1st Qtr</b>	<b>679,111</b>	<b>-</b>	<b>-</b>	<b>45,908</b>	<b>12,929</b>	<b>98,044</b>
Budgeted Expenditures	8,853,060	50,000	3,956,895	301,930	-	1,057,447
<b>Total Actual Expenditures - 1st Qtr</b>	<b>2,195,809</b>	<b>9,683</b>	<b>68,702</b>	<b>-</b>	<b>-</b>	<b>21,139</b>
<b>1st Quarter Ending Fund Balance</b>	<b>4,729,117</b>	<b>83,808</b>	<b>(210,155)</b>	<b>851,192</b>	<b>2,282,076</b>	<b>980,738</b>

**Internal Service Funds** - Internal Service Funds are used to finance and account for special activities and services performed by a designated Town department for other departments on a cost reimbursement basis. Included in this fund type are the Equipment Replacement Fund, Worker's Compensation Fund, General Liability Self Insurance Fund, Stores Fund, Management Information Systems Fund, Vehicle Maintenance Fund, and the Building Maintenance Fund.

Internal Service Funds are tracking in accordance with the adopted FY 2007/08 adopted budget. No revision to adopted revenues or expenditures is required at this time. Staff believes there is still some potential for further operating transfers in future years, if needed, from these funds as excess balances exist in amounts needed for funding in a number of these funds.

**Internal Service Funds  
Budget to Actuals Comparisons**

	<b>Equipment Replacemt</b>	<b>Workers Comp</b>	<b>Self Insurance</b>	<b>Office Stores</b>	<b>Mmgt Info Systems</b>	<b>Vehicle Maint.</b>	<b>Building Maint.</b>
<b>Beginning Fund Balance</b>	<b>3,161,526</b>	<b>2,393,460</b>	<b>2,125,032</b>	<b>241,342</b>	<b>2,085,760</b>	<b>190,878</b>	<b>738,656</b>
Budgeted Revenues	414,100	613,500	506,800	86,000	925,530	611,600	1,189,500
<b>Actual Revenues - 1st Qtr</b>	<b>101,740</b>	<b>165,447</b>	<b>145,078</b>	<b>14,498</b>	<b>228,656</b>	<b>152,900</b>	<b>292,699</b>
Budgeted Expenditures	641,910	604,440	541,400	84,600	1,381,800	597,050	1,179,600
<b>Total Actual Expenditures - 1st Qtr</b>	<b>161,089</b>	<b>185,743</b>	<b>328,750</b>	<b>12,482</b>	<b>230,463</b>	<b>117,533</b>	<b>205,237</b>
<b>1st Quarter Ending Fund Balance</b>	<b>3,102,176</b>	<b>2,373,165</b>	<b>1,941,359</b>	<b>243,359</b>	<b>2,083,953</b>	<b>226,245</b>	<b>826,118</b>

**Trust and Agency Funds** - Town Trust and Agency Funds have fund balances as of June 30, 2007 of \$319,716 for Parking District #88 and \$313,424 in the Library Trust Funds. No budget revisions are contemplated at this time for these funds.

**Redevelopment Agency** - The Agency's FY 07/08 and FY 2007-12 Capital Improvement Plan adopted budgets are incorporated into the Redevelopment Agency's financial statements and year-to-date actuals as presented below. The Capital Projects Fund balances include approximately \$372,000 dollars of remaining unexpended funds at September 30, 2007 from the Agency's \$10.7 million dollar 2002 COP issue. Approximately \$98,000 of the remaining proceeds are encumbered to be spent on the Elm Street Reconstruction project, and \$80,000 for

Almond Grove Concrete Rehabilitation Pilot project. The other remaining funds of approximately \$194,000 (including accrued interest earnings) are available for their planned purpose including eligible capital projects in the downtown project area such as the Santa Cruz Avenue/Wood Road Gateway design (\$65,000) and the North Santa Cruz Lighting Project (\$55,000).

**Redevelopment Agency Funds  
Budget to Actuals Comparisons**

	<b>Capital Projects</b>	<b>Debt Service</b>	<b>Low/Mod Housing</b>	<b>Total RDA Funds</b>
<b>Beginning Fund Balance</b>	<b>4,316,921</b>	<b>4,307,048</b>	<b>6,556,978</b>	<b>15,180,947</b>
Budgeted Revenues	600,000	6,597,990	1,676,800	8,874,790
<b>Actual Revenues - 1st Qtr</b>	<b>10,113</b>	<b>180,677</b>	<b>7,540</b>	<b>198,330</b>
Budgeted Expenditures	3,658,091	5,034,400	497,420	9,189,911
<b>Total Actual Expenditures - 1st Qtr</b>	<b>1,156,195</b>	<b>752,120</b>	<b>19,655</b>	<b>1,927,970</b>
<b>1st Quarter Ending Fund Balance</b>	<b>3,170,839</b>	<b>3,735,605</b>	<b>6,544,863</b>	<b>13,451,307</b>

Since 1992 redevelopment agencies across the state have been required to make Educational Revenue Augmentation Fund (ERAF) payments to the State. Last year's State budget In accordance with the State budget agreement, the ERAF payment was increased \$303,000 for FY 2004/05 & FY 2005/06. Since passage of the FY 2006/07 state budget, the increased ERAF payments have not been approved by the legislature, allowing the Agency to retain this amount of tax increments to be used for important future Agency projects.

Proposition 1A approved in 2004 does not contain specific protections for redevelopment agencies. They were not included because there are existing legal opinions that conclude that redevelopment agency tax increment revenue is constitutionally protected from state revenue takes.

It is important that the Town continue to monitor developments regarding Redevelopment Agencies to discourage the legislature from further State takes from Redevelopment Agency Tax Increment. Protecting Redevelopment Agency funds for all cities is also a strategic priority for the League of California cities. It is essential to preserve the Agency's tax increment revenue as any take from this source will reduce the annual revenue stream. If a larger revenue take is enacted, the lowered revenue stream will reduce the total amount of bonds the Agency can issue in the future.

### CONCLUSION

The financial results from the prior fiscal year coupled with the FY 2007/08 first quarter data point towards a cautious optimism that the Town's economically-sensitive revenues will continue their positive trends. This is especially important in light of the loss of three top ten sales tax providers in the past two years. Though the Five-Year Financial Plan continues to project future revenue shortfall challenges, these challenges will be made less so if the Town's economically-sensitive revenues can sustain their momentum and the cost core service delivery can be kept in check.

