General Fund

Operating Budget:	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
	Fiscal Year				
Revenue	$ 84,065,952	$ 79,468,394	$ 80,142,712	$ 80,142,712	$ 83,433,213
Expenditures	(80,547,164)	(80,875,801)	(83,446,913)	(80,615,040)	(87,179,436)
Operating surplus	3,518,788	(1,407,407)	(3,304,201)	(472,328)	(3,746,223)
Capital budget:					
Capital Grants	-	-	-	-	871,003
Capital budget	(4,543,676)	(1,015,150)	(1,015,150)	(1,015,150)	(1,298,403)
Net addition to (use of) reserves	$ (1,024,888)	$ (2,422,557)	$ (4,319,351)	$ (1,487,478)	$ (4,173,623)

BACKGROUND

The adopted fiscal year 2005 General Fund budget is a continuation of the process and approach begun in the middle of fiscal year 2002. The budget includes a combination of expenditure reductions, revenue enhancements, and the use of reserves in excess of policy requirements to balance the budget. The budget is also consistent with the City's multi-year General Fund financial plan to return to a balanced operating budget by fiscal year 2007. Although total expenditures are projected to increase (as discussed below), the fiscal year 2005 budget includes a reduction over fiscal year 2004 adopted amounts in discretionary supplies and services of 4.4% and a net reduction of almost 12 permanent, full-time equivalent positions.

After several years of historically strong revenue growth, a number of the City's key General Fund revenues began to reflect a weakening economy in the spring of 2001. Growth rates in these key revenues began to moderate significantly. The terrorist attacks of September 11th compounded this trend. In the wake of September 11th, revenues such as sales tax and transient occupancy tax (TOT) declined for the first time in more than four years. Although the City's key tax revenues are now growing once again, in some cases they have just returned to 2001 levels. During this same time, some of the City's costs have grown significantly, most of which were partially or completely beyond the City's control. In particular, insurance costs, including workers' compensation, property insurance and employee health insurance, have increased substantially in the last three years. In addition, due to the poor performance of financial markets over the last three years, the City's retirement contributions to the California Public Employees Retirement System (PERS) are increasing dramatically. These concurrent trends have combined to present the City with both significant budget challenges and opportunities.

In some ways, the current budget environment has been similar to the recession of the early 1990s. However, there are also fundamental and important differences. Like the previous recession, key General Fund revenues have been impacted. For example, in fiscal year 2002, two of the General Fund's most important and economically sensitive revenues declined. Sales tax declined 4.1% and transient occupancy tax declined 3.3% from fiscal year 2001 levels. Sales and transient occupancy taxes are two key revenue sources that are just now returning to the levels

General Fund

prior to September 11, 2001. Unlike the recession of the early 1990s, the current budget challenges are due more to increasing costs than declining or stagnant revenues. In fact, even had revenues continued to grow at historical levels, the City would still be facing budget challenges. The cost increases mentioned above (and discussed in further detail later in this overview) are a significant dimension that was not present in the recession of the 1990s.

Another similarity between the recession of the early 1990s and the current situation is the State's budget situation. In 1991, the State faced a sizeable budget deficit, which it solved in large part by taking funds from local governments. Through the use of the Educational Revenue Augmentation Fund (ERAF), the State shifted local property tax dollars to schools, thus enabling it to reduce its own obligation to school funding by an equal amount. The ERAF shift, which continues to grow each year, is now costing the Santa Barbara's General Fund over $2.5 million of property tax revenue annually. In fact, much of the state's budget surplus during the late 1990s was the result of the continuing ERAF shift that was never returned to local governments once the economy recovered.

In fiscal year 2004, the State once again raided local government revenue. This time, the State failed to honor a previous commitment when it diverted $1.3 billion of vehicle license fee (VLF) backfill revenue from cities and counties, using the funds instead to address a portion of its multi-billion dollar deficit. This $1.3 billion state budget action resulted in a loss to the City's General Fund of $1.7 million, representing over 2% of total revenue. The State considered this action a temporary loan from local governments to the State, promising that this "loan" will be repaid in 3 years. Since this action was taken after the adoption of the City's budget, the VLF revenue included in the City's adopted fiscal year 2004 budget did not reflect the $1.7 million estimated reduction in VLF payments from the State.

The State is facing another substantial budget deficit for fiscal year 2005. In May 2004, the Governor announced his proposed plan in connection with the "May Revise". Among other things, the proposed plan called for a $1.3 billion property tax shift from local governments in fiscal years 2005 and 2006. In return, the Governor agreed to support a ballot measure that would provide Constitutional protection of local revenues.

The proposal, supported by local government officials, was opposed by many democratic legislators who favored an alternative proposal that gave the State more flexibility to affect the allocation of revenues among local governments. However, on July 21, the Governor and State legislators finally reached an agreement, which preserved the protection of local revenues sought by the Governor and local governments. In addition, the agreement provides for the repayment of the $1.3 billion VLF loan in fiscal year 2007 as noted above.

The impact to the City will be a loss of property tax revenues through another ERAF shift of almost $1.3 million in each of the next two years. Although the loss of revenues is significant, the protection of local revenues is a major victory for cities, counties, and special districts across the State.

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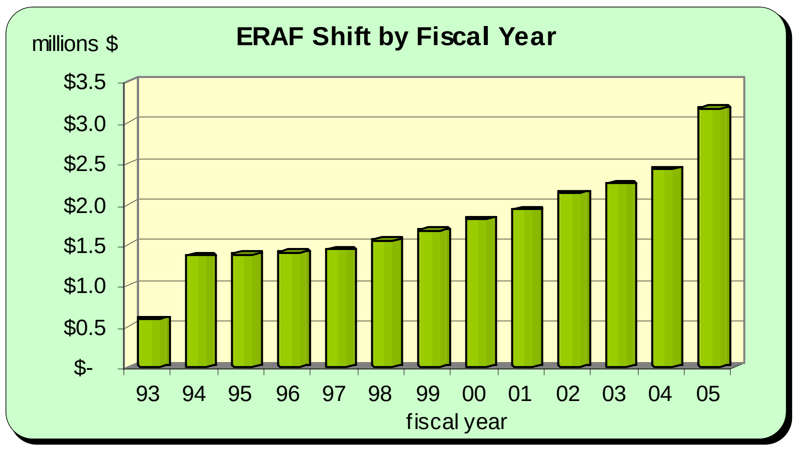
As mentioned on the previous page, the City's General Fund is already losing over $2.5 million per year to the ERAF. The chart below displays the City's property tax loss to the ERAF since it was created in fiscal year 1993. Estimated property tax revenue in the fiscal year 2005 adopted budget has been adjusted to reflect the Governor's January proposal only, since the recent agreement between the Governor and the State legislature was reached only after adoption of this budget.



Although revenues - including the impacts from the State budget - remain a concern, the current General Fund budget challenges are primarily expenditure-driven. Because there is no expectation that these cost pressures will abate in the short term, the City is not in a position to simply wait for an improved economic climate to grow revenues back to a balanced budget. For example, insurance costs including workers' compensation, and especially retirement costs, are all expected to grow in excess of the rate of inflation over the next two years. Therefore, to address the budget challenges, adjustments to both expenditures and revenues were required in developing the fiscal year 2005 budget.

The City's goal has been, and continues to be, to combine expenditure reductions, adjustments to the City's fees and service charges, and the judicious use the General Fund's accumulated reserves to permit a gradual and orderly transition to a smaller, more efficient organization. Often referred to as a "soft landing," the concept is to manage the return to a balanced budget while avoiding layoffs or other unnecessary disruptions to the organization. This is exactly the scenario for which the General Fund has accumulated reserves. For example, the adopted fiscal year 2003 General Fund budget contained approximately $2 million in expenditure reductions combined with the budgeted use of an equivalent amount of reserves. Although vacant positions were eliminated, the $2 million of reductions were accomplished without layoffs. The adopted fiscal year 2004 budget continued this approach. The adopted 2004 budget contained 27 fewer positions citywide than were authorized in the amended fiscal year 2003 budget.

Because of the City's conservative budgeting practices, invariably the use of reserves at fiscal year-end is considerably less than originally budgeted. For example, the adopted fiscal year 2003 budget included the use of $2.1 million of reserves to balance the operating budget. However, at the end of fiscal year 2003, not only was the General Fund balanced, the fund had generated an operating surplus of just over $1 million. This was the result of favorable budget variances of over $3 million. Similar results are expected for fiscal year 2004. It is this experience combined with

General Fund

the continued use of conservative budget assumptions that permits the City to maintain General Fund reserves at levels consistent with adopted policies, despite budgeting their use. Therefore, although the adopted budget for fiscal year 2005 shows the use of $3.75 million of reserves to balance the operating budget, the City's multi-year financial model projects a year-end use of reserves of only $2.2 million for operations.

SUMMARY OF ADOPTED FY 2005 BUDGET

As shown in the table at the top of the page D-1, the adopted fiscal year 2005 General Fund operating budget projects total revenue of $83.4 million combined with the use of almost $3.8 million of reserves to fund an operating budget of $87.2 million. The use of an additional $427,400 of reserves, plus grant revenue of $871,003, will fund a capital program of $1.3 million. Total use of reserves in the adopted budget for operating and capital is just under $4.2 million. The use of reserves for capital is in keeping with both past practice and the City Council policy, established in 1995, of using non-recurring revenue (reserves) to fund non-recurring costs (capital). It deserves a second mention that the final use of reserves for fiscal year 2004, based on past experience, will be at least $2 million less than the budgeted amount. This is due to conservative budgeting practices resulting in favorable year-end variances for both revenue and expenditures.

General Fund operating expenditures in the adopted budget are $87.2 million, an increase of $6 million (7.5%) over the adopted fiscal year 2004 budget. The entire increase is attributable to higher salary and benefit costs. Overall, salaries and benefits in the adopted budget are $6.6 million (11%) higher than the adopted fiscal year 2004 budget. What makes this increase remarkable is that the adopted budget does not contain any provision for future salary increases - despite the fact that all of the City's labor agreements expire between June 30 and December 31, 2004. The growth in personnel costs is a result of the dramatic increase in retirement costs. The General Fund's contribution to the California Public Employees' Retirement System (PERS) will increase by almost $4.8 million (59%), from $8.1 million to $12.9 million. This follows a 31% increase in fiscal year 2004. The following table details the City PERS rates by "contribution group."

PERS Contribution Rates by Contribution Group

Contribution Group	FY 2003	FY 2004	FY 2005	FY 2006*
Miscellaneous	7.000%	10.161%	17.352%	18.700%
Police	27.793%	32.665%	43.418%	46.100%
Fire	19.899%	30.549%	45.878%	49.600%

Rates stated as a percent of payroll | ** - CalPERS estimate*

The rates, stated as a percent of covered payroll, include both the employer rate and the City-paid employee rate. The fiscal year 2006 rate is a preliminary estimate provided by PERS.

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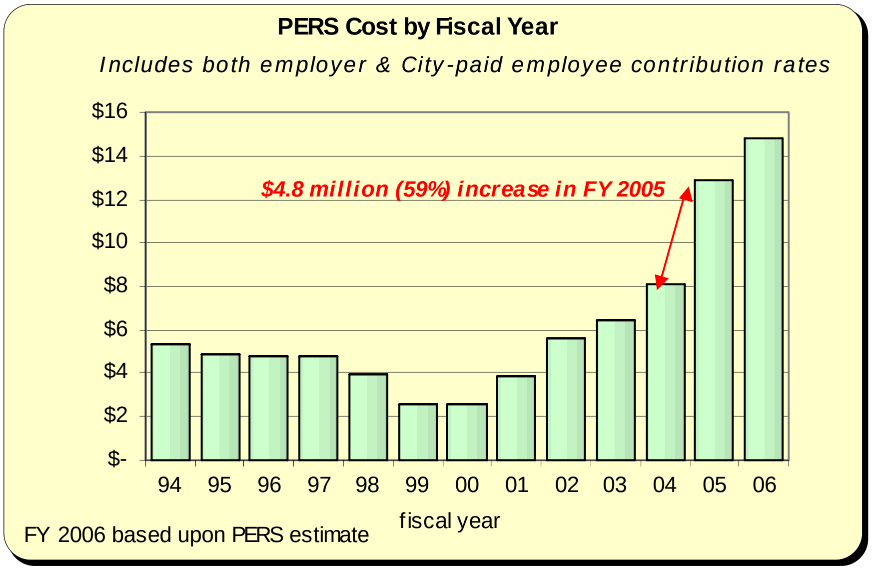
Although the 50% increase in police and fire retirement benefits that took effect in 2001 has certainly been a factor in the rate increases for those groups, the dramatic increase in retirement costs is primarily attributable to the investment losses suffered by PERS over the last several years. Whatever the cause, the increase in retirement costs is greater than the total budgeted use of reserves in the adopted budget. Therefore, all other things being equal, if fiscal year 2005 PERS costs had remained at fiscal year 2004 levels, the General Fund operating budget would have been balanced without the use of reserves.



The chart to the right displays the General Fund PERS costs by fiscal year since 1994. As the chart indicates, the fiscal year 2005 increase, although the largest, is just the latest increase since the General Fund's retirement costs hit a historical low in fiscal year 2000. The fact that the City's PERS costs hit an historical low in 2000 is further evidence of the impact of PERS' investment returns on the City's contribution rates. Contribution rates reached all-time lows on the strength of the "dot-com"-driven investment gains of the late 1990's.

Property and workers' compensation insurance costs have also increased over the last several years. The City is partially self-insured for workers' compensation. Since fiscal year 2001 the General Fund's workers' compensation costs have increased almost $1.2 million (102%). In addition, the City's self-insured retention (deductible) for workers' compensation has increased from $300,000 to $750,000 per occurrence. The City purchases commercial property insurance, including coverage for earthquake and flood. In fiscal year 2000, the City paid $461,000 for property insurance, including earthquake and flood coverage, with a basic deductible of $100,000 per occurrence. In fiscal year 2003, the City paid over $1.5 million for coverage with a $2 million deductible per occurrence. This represents a 225% increase in cost with a 20-fold increase in the deductible. The General Fund has absorbed a proportionate share of this increase. The City's property insurance premium for fiscal year 2005 is projected to be the same as in fiscal year 2004, just under $1.5 million with the same deductible limits.

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LONG-RANGE FINANCIAL PLANNING

For many years now, the City staff has used a multi-year forecasting model to project General Fund budgets several years into the future and assess the long-term impacts of current budget decisions and options. The model allows staff to perform "what-if" projections using different sets of assumptions for both revenues and expenditures. At least annually, a series of these projections are reviewed with the City Council Finance Committee. Particularly in unsettled budgetary times such as now, the model is an extremely useful tool in making decisions and projecting the impacts of those decisions up to four years into the future. The table below is a summary of the current version of the multi-year model. The table contains data for the prior year's actual year-end balances, year-end projections for fiscal year 2004, the adopted fiscal year 2005 budget adjusted for the impact of the recent agreement reached between the Governor and State legislators, and projections for three additional fiscal years.

City of Santa Barbara
Multi-Year Forecast
General Fund

	FY 2003 Actual	FY 2004 Projected	FY 2005 Adopted	FY 2006 Estimated	FY 2007 Estimated	FY 2008 Estimated
Total Revenues	$ 84,065,940	$ 80,048,022	$ 82,758,682	$ 86,069,029	$ 92,463,553	$ 94,394,096
Total Expenditures	82,869,262	81,615,040	87,179,436	90,728,759	93,464,788	96,288,858
Revenues Over (Under) Expend	1,196,678	(1,567,018)	(4,420,754)	(4,659,730)	(1,001,235)	(1,894,762)
Anticipated Year-End Variance	-	1,000,000	2,179,486	2,268,219	2,336,620	2,407,221
Operating Surplus (Deficit)	1,196,678	(567,018)	(2,241,268)	(2,391,511)	1,335,385	512,459
Cumulative Future Budget Adj.	-	-	-	500,000	500,000	500,000
Expected Oper. Surplus (Deficit)	1,196,678	(567,018)	(2,241,268)	(1,891,511)	1,835,385	1,012,459
Capital Program	(2,233,730)	(1,015,150)	(427,400)	(750,000)	(750,000)	(750,000)
Net Addition to (Use of) Reserves	(1,037,052)	(1,582,168)	(2,668,668)	(2,641,511)	1,085,385	262,459
Beginning Reserves Balance	30,441,123	29,404,071	27,821,903	25,153,235	22,511,724	23,597,109
Ending Reserves Balance	$ 29,404,071	$ 27,821,903	$ 25,153,235	$ 22,511,724	$ 23,597,109	$ 23,859,568
Required Reserves	$ 21,218,950	$ 22,794,859	$ 23,682,190	$ 24,303,697	$ 25,009,715	$ 25,731,880
Reserves Over (Under) Policy	8,185,121	5,027,044	1,471,045	(1,791,973)	(1,412,606)	(1,872,312)
Total Reserves	$ 29,404,071	$ 27,821,903	$ 25,153,235	$ 22,511,724	$ 23,597,109	$ 23,859,568

The projections of fiscal years 2006, 2007 and 2008 are based upon the assumptions in the table to the right. In each case, the percentage represents the annual growth assumed for that

	FY 2006	FY2007	FY 2008
Revenue growth	4%	4%	4%
Expenditures:			
Salaries	3%	3%	3%
Health insurance	5%	5%	5%
PERS	PERS estimate	3.5%	3.5%
Workers' Comp.	5%	5%	5%
Supplies & services	2%	2%	2%

General Fund

particular item. For example, the model assumes 4% annual revenue growth and 3% annual growth in salaries.

Using these assumptions, the model projects that, with another $500,000 of adjustments in fiscal year 2006, the General Fund will return to a balanced operating budget in fiscal year 2007 ("Expected Operating Surplus/(Deficit").

As mentioned above, because of conservative budgeting assumptions, the City invariably ends the year with a favorable variance (revenue over budget and expenditures under budget). The model reflects this experience by incorporating an "Anticipated Year-End Variance." The model assumes that the favorable year-end variance will be 2% of the operating budget.

The balance of the table projects the impact of both the operating results and the capital program on the General Fund's reserve balances. Based upon all of the assumptions listed and described above, the model projects that from fiscal year 2004 to the end of fiscal year 2008, the General Fund will use $5.5 million of reserves, of which $1.8 million will be to balance the operating budgets and the balance ($3.7 million) will be used for capital. As displayed on the very bottom line of the model above ("Reserves Over (Under) Policy"), at the end of fiscal year 2008 General Fund reserves will be approximately $1.9 million below the policy guideline established by City Council resolution. However, the policy reserves to be used will come from the "Budget Reserve," which was established specifically to be available during difficult budget and economic times. We strongly believe that the current situation qualifies as such.

Most importantly, despite the projected use of reserves, at the end of the planning horizon, the General Fund would still have $23.9 million of reserves, including a remaining balance in the "Budget Reserve" for economic contingencies of $8.1 million, a "Disaster Reserve" of over $14.8 million and a Capital Reserve of $1 million.

Clearly, the results projected by this version – or any version – of the model are only as good as the assumptions. Staff believes that the basic assumptions used in this version are reasonable based upon the current situation. The model is updated regularly as the situation changes and this allows staff to focus on the longer-term implications of both external impacts and potential policy decisions. It is an extremely useful tool; so much so, that virtually all of the City's Enterprise Funds now prepare and maintain a similar model for their own long-range planning.

The balance of this General Fund overview will focus on specific revenue and expenditure issues. Details on operating expenditures by department and program can be found in the department summaries and program narratives later in this document.

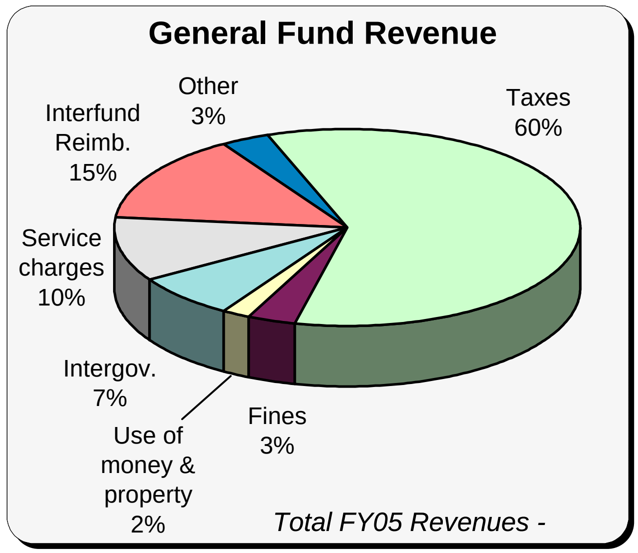
REVENUE

In total, fiscal year 2005 General Fund revenues are projected at $83.4 million. This represents an increase of almost $4 million (4.9%) from the adopted fiscal year 2004 budget.

General Fund

The chart below displays the General Fund's major revenue sources. As the chart indicates, taxes, at 60%, still constitute the largest source of General Fund revenue. Interfund Reimbursements, which represent payments to the General Fund from other City funds for various services provided to those funds, is the second largest category at 15%. Fees and service charges represent 10%, followed by intergovernmental (7%), fines (3%) and use of money and property (2%).

Overall, staff is projecting moderate growth in the General Fund's major tax revenues. Additional detail is presented below, but growth rates are projected to be between 2% and 7%, depending on the particular revenue.



The other factor affecting overall revenue projections are fee increases proposed by the various General Fund departments. Through a combination of anticipated growth in activity levels and the projected impact of fee increases contained in the adopted budget, total service charge revenue is expected to be approximately 10% in fiscal year 2005.

In summary, the revenue growth rate projections used to develop the adopted budget are consistent with recent experience and staff believes they are reasonable. However, if the City experiences a renewed economic slowdown with a corresponding impact on revenues, additional adjustments to the budget will be required. Additional detail on specific revenue sources is presented below.

Taxes

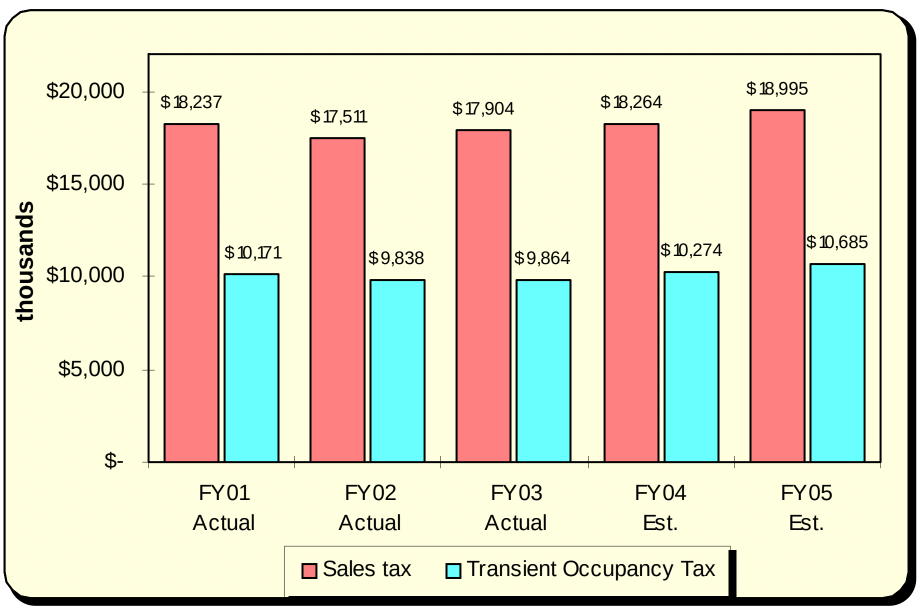
Overall, the adopted fiscal year 2005 tax revenue estimate is 3.7% above the estimated fiscal year-end amounts for fiscal year 2004. The table on the following page details the City's tax revenues with amounts presented for the adopted budget and projected fiscal year 2004 year-end actual amounts, and the fiscal year 2005 adopted budget. The "percentage growth" amounts compare the fiscal year 2004 estimated year-end amounts to the adopted fiscal year 2005 budget. This comparison presents a clearer picture of the growth rates staff is projecting for fiscal year 2005 and is consistent with the way staff develops the revenue estimates. Staff begins by evaluating fiscal year 2004 year-to-date amounts and projects estimated year-end balances. Then projections for the budget year are developed based upon the prior year, year-end estimates, less any adjustments for any structural changes.

General Fund

As the table below indicates, the City is projecting 4% growth in sales tax revenue. As the City's largest and most economically sensitive revenue source, staff tends to be somewhat conservative with sales tax projections. A negative variance of only 1% in the sales tax projection translates into a revenue loss of almost $190,000. In addition, sales tax is more difficult to project because of the significant delay in the state's reporting of actual results. In projecting sales tax growth rates, staff also considers projections developed by the State Franchise Tax Board and the City's sales tax auditor.

	Fiscal 2004 Budget	Fiscal 2004 Y/E Estimate	Fiscal 2005 Adopted	Percent Growth
Sales and use	$ 18,042,000	$ 18,264,267	$ 18,994,900	4.0%
Utility users	5,607,700	5,480,200	5,837,700	6.5%
Property	10,992,200	11,099,337	11,299,100	1.8%
Transient occupancy	10,273,900	10,273,900	10,684,900	4.0%
Business license	1,876,300	1,915,000	1,982,500	3.5%
Real property transfer	408,000	600,000	618,000	3.0%
Total taxes	$ 47,200,100	$ 47,632,704	$ 49,417,100	3.7%

As the chart below indicates, both sales tax and transient occupancy tax declined in fiscal year 2002, but were up very modestly in fiscal year 2003. Both are expected to finally return to fiscal year 1991 levels in fiscal year 2004 and both are budgeted to grow 4% next fiscal year. Unlike sales tax, the City receives TOT on a monthly basis and therefore it is somewhat more predictable.



Property tax continues to show strong growth. Staff is projecting 7% growth for next fiscal year. However, after adjusting for the Governor's proposed ERAF property tax shift ($577,232) in January, the projected growth rate is lowered to 1.8%.

Revenue from the City's 6% utility users tax (UUT) is split between the General

General Fund

Fund and the Streets Fund. Pursuant to the municipal code, 50% of the City's UUT is restricted to use for streets and roads and is budgeted in the Streets Fund. The other 50% is unrestricted and is budgeted in the General Fund. UUT is projected to increase 3% next year. However, adjusting for the impact of potential utility rate increases on UUT, the growth rate increases to 6.5%. The City's utility users tax revenue has been unusually volatile over the last two years as commodity prices for energy skyrocketed and then returned back to close to previous levels. However, staff feels that the revenue estimate is realistic for fiscal year 2005.

And finally, business license tax is projected to grow 3.5% over fiscal year 2004 and real property transfer tax is projected to grow 3%, as shown in the chart.

Fines and Forfeitures

This revenue category is projected to provide approximately $2.6 million in General Fund revenue (3%). This is approximately 2.4% ($63,000) higher than the amount budgeted in fiscal year 2004. The largest item in this group is parking fines, which is anticipated to generate $2.3 million of the $2.6 million total.

Use of Money and Property

This category, totaling $1.6 million (2% of General Fund revenue) is comprised of two items. The first, and smaller, is the rents and leases earned on General Fund properties, primarily the three Community Centers in the City. This provides approximately $480,000.

The more significant revenue in this category is investment income. The fiscal year 2005 budget for investment income is $1.15 million. This is up only very slightly from the fiscal year 2004 budget of $1.13 million. Even if interest rates increase over the next year, staff believes that investment income will remain at current levels because it will take time for the lower yielding investments in the City's portfolio to mature or be sold and replaced with higher yielding investments.

Intergovernmental

Intergovernmental revenues are projected to contribute approximately $6.2 million (7%) to the General Fund budget. This is virtually identical to the amount budgeted in fiscal year 2004. By far the most significant individual revenue in this category, budgeted at $5.8 million, is the vehicle license fee (VLF). This revenue is paid to the City by the State and, as mentioned earlier, the State retained 3 months of the fiscal year 2004 VLF backfill payments to cities to help balance its own budget. This action cost the City $1.7 million of its fiscal year 2004 VLF revenue. The adopted fiscal year 2005 budget assumes that the State will honor its commitment to continue the full VLF backfill during fiscal year 2005.

General Fund

Service Charges

After taxes and Interfund charges, this is the third largest revenue category in the General Fund. In total, service charges are projected to provide just over $8.7 million (10%) of General Fund revenue. As the table below indicates, the adopted fiscal year 2005 amount is approximately $1 million (13%) above the adopted fiscal year 2004 amount. In a number of cases, the total projected growth in revenue is due to a combination of increases in fees and anticipated activity levels.

	Fiscal 2003 Actual	Fiscal 2004 Adopted	Fiscal 2005 Adopted	Percent Change
Community Development	$ 3,225,910	$ 3,161,746	$ 4,145,951	31.13%
Finance	680,958	652,500	677,500	3.83%
Fire	50,128	130,200	187,379	43.92%
Library	582,910	603,036	648,241	7.50%
Parks and Recreation	2,165,931	2,396,050	2,129,856	-11.11%
Police	545,117	510,951	570,190	11.59%
Public Works	288,069	270,375	360,327	33.27%
Total	$ 7,539,023	$ 7,724,858	$ 8,719,444	12.88%

While there is always sensitivity to increased fees for government services, staff believes it is important that the City establish fee levels to recover a reasonable portion of the costs of providing those services. Service costs not recovered through program fees must be subsidized with tax revenue. While this may be appropriate in some cases, as a rule, staff believes that the users of the services ought to bear the costs of providing them. As has been discussed earlier in this document, the City will continue to work towards the goal of becoming a smaller and more efficient organization. Over time, this will lower the costs of providing services to the public. However, in many cases, the City's current fee levels still recover only a small fraction of the cost of providing the services. In conjunction with development of the adopted budget, the City conducted a General Fund fee study. The study defined the fully allocated costs of providing General Fund services as well as the percent of those costs recovered through the corresponding fees. The fee study will facilitate discussion of both the costs of providing services and the appropriate fee levels.

Interfund Charges and Reimbursements

This category of revenue represents reimbursements to the General Fund for services provided to the City's Enterprise and Special Revenue funds. The adopted fiscal year 2005 budget contains almost $12 million from this revenue source, representing 14% of total General Fund revenue. Four items account for over $10.1 million of the total.

General Fund

The General Fund's overhead allocation represents just less than $4.9 million. These are charges to the City's Enterprise and Special Revenue funds for administrative costs provided by the General Fund. Examples of the services provided include most of the payroll, accounts payable, accounting, human resources, legal, City Clerk and City Administrator support. Each administrative service is individually allocated based upon usage. For example, payroll costs are allocated based upon the number of paychecks issued for each fund.

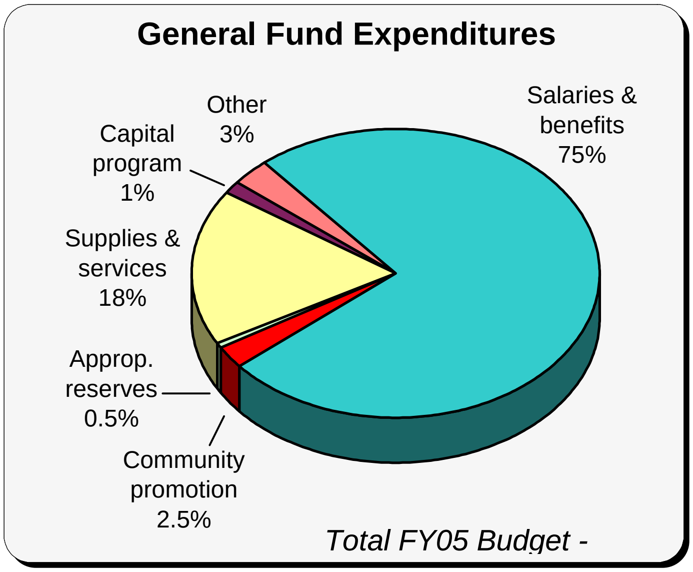
The Airport pays approximately $1.35 million to the General Fund for Fire Department staffing of the Airport Rescue and Firefighting (ARFF). This is the fire station at the Airport that provides FAA-mandated fire and rescue services. The Airport pays for the direct costs of the firefighters as well as all associated costs of maintaining the station and equipment and an allocated overhead.

Public Works generates $2.65 million from engineering charges to City projects. Virtually all of these charges are incurred from engineering support of capital projects. When the General Fund-paid engineering staff works on a capital project, the cost of their time is charged to that project.

The final notable item in this revenue category is payment from the City's Redevelopment Agency (RDA) for staffing of the Agency. The RDA has no staff. Under a contract between the City and the RDA, the City commits to providing staffing to the Agency, including legal services. This reimbursement totals approximately $1.1 million.

EXPENDITURES

As mentioned at the beginning of this section, overall General Fund operating expenditures in the adopted fiscal year 2005 budget are $87.2 million. Including capital, the total adopted General Fund budget is $88.6 million.



The adopted operating budget is $6 million (7.5%) greater than the adopted fiscal year 2004 budget. The budget also contains the elimination of just under 12 permanent full-time equivalent positions. In addition, as was described earlier, the operating budget has absorbed a significant increase in retirement costs. The adopted budget contains no provision for any salary increases for any bargaining unit beyond what is contained in existing labor agreements.

The chart to the right displays the adopted budget, including capital, by object of expenditure. As is always the case, salaries and benefits (75%)

General Fund

represent the largest portion of the General Fund budget.

Capital expenditures represent 1% of the General Fund budget. As indicated in the chart, the Community Promotion budget comprises approximately 2.5% of the budget. The Community Promotion program accounts for City contributions to various civic events such as the 4th of July celebration, Old Spanish Days and Summer Solstice, as well as to organizations such as the Chamber of Commerce and the Conference and Visitors Bureau.

The table below summarizes General Fund operating expenditures by department for the adopted fiscal year 2004 budget, the fiscal 2004 amended budget, and the adopted fiscal year 2005 budget. The percentage change column is based on the change from fiscal year 2004 amended budget to the adopted fiscal year 2005 budget.

General Fund Departments	Fiscal 2004		Fiscal 2005	FY04 Amended
	Adopted	Amended	Adopted	to FY2005
Administrative Services	$ 1,705,287	$ 1,761,857	$ 1,511,570	-14.2%
City Administrator	1,742,995	1,848,916	1,787,126	-3.3%
City Attorney	1,681,641	1,789,693	1,800,391	0.6%
Community Development	7,499,416	7,892,843	8,275,717	4.9%
Finance	4,306,500	4,526,500	4,488,332	-0.8%
Fire	14,037,658	14,495,746	16,257,299	12.2%
Library	3,687,342	3,920,491	3,906,441	-0.4%
Mayor and Council	556,099	592,084	529,158	-10.6%
Non-Departmental	3,881,547	3,602,457	3,557,793	-1.2%
Parks and Recreation	12,589,366	12,564,530	12,350,177	-1.7%
Police	24,601,638	25,746,742	27,761,429	7.8%
Public Works	4,586,312	4,705,052	4,954,003	5.3%
Total expenditures	$ 80,875,801	$ 83,446,911	$ 87,179,436	4.5%

As the table indicates, a number of the departmental budgets are below fiscal year 2004 levels, despite absorbing substantial increases in costs such as retirement. In large part due to the retirement cost increases, public safety is up a combined $3.8 million (9%) from the fiscal year 2004 amended budget and $5.4 million (14%) from the fiscal year 2004 budget as originally adopted. Public safety now represents 51% of the total General Fund operating budget.

SUMMARY

Overall, the City's General Fund remains in a strong financial position. With the support of the City Council and through prudent planning, the General Fund has accumulated considerable reserves. As planned, these reserves are now available to assist the General Fund as it transitions to a smaller and more efficient operation through attrition. Through long-range

General Fund

planning, a financial plan has been established to guide the City back to a balanced budget while maintaining the integrity of the reserves upon which the City relies. The adopted fiscal year 2005 operating budget is another step in a process that was begun during fiscal year 2002. The number of General Fund positions is being reduced over time while significant cost increases beyond the City's control have been absorbed. While the reductions and adjustments begun in fiscal year 2002, and continued through the budgets for fiscal years 2003, 2004 and now the adopted fiscal year 2005 budget, it is clear that substantial uncertainty remains. Depending on the impacts of the State's budget solutions and the performance of the local economy, additional adjustments may well be necessary over the next year or two.

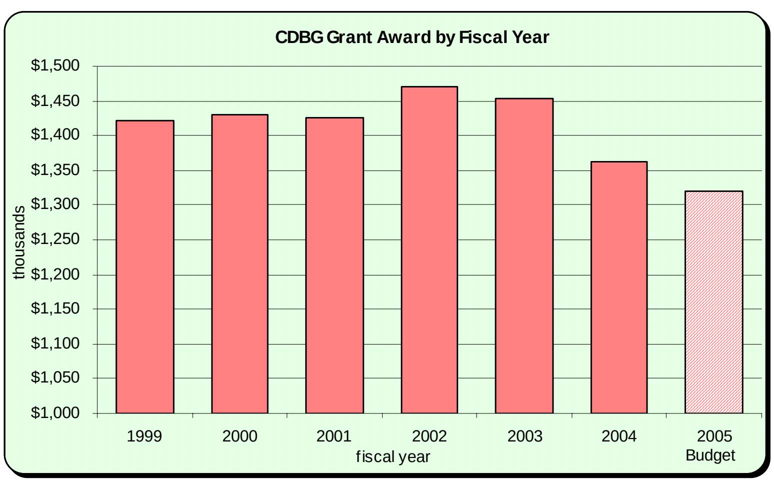
Special Revenue Funds

COMMUNITY DEVELOPMENT BLOCK GRANT FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue					
CDBG revenue	$ 1,236,190	$ 1,364,000	$ 1,364,000	$ 1,364,000	$ 1,319,000
Program income	662,620	450,000	450,000	750,000	650,000
Total revenue	1,898,810	1,814,000	1,814,000	2,114,000	1,969,000
Operating expenditures	1,898,810	1,814,000	1,814,000	1,814,000	1,969,000
Net addition to (use of) reserves	$ -	$ -	$ -	$ 300,000	$ -

The City's Community Development Block Grant (CDBG) Fund is used to account for the annual federal block grant received by the City from the U.S. Department of Housing and Urban Development. This annual grant supports programs including the City's Rental Housing Mediation Task Force, human service and community capital grants and a low and moderate-income housing rehabilitation loan program.

Over the last several years, federal budget actions have adversely impacted the City's annual CDBG award. The chart below indicates that since fiscal year 2002 the City's grant award has declined over $152,000 (10%) to a projected grant amount of just over $1.3 million for fiscal year 2005. Although the City's grant award has declined since the peak in fiscal year 2002, the City is still enjoying substantially greater CDBG funding than in the early 1990s when grant amounts were approximately $800,000. The City remains concerned that federal budget actions may continue to adversely affect the programs supported by the CDBG grant program.



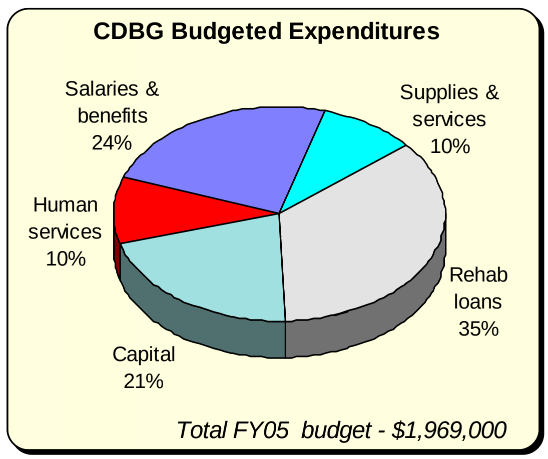
Besides the annual federal grant award, the other major source of revenue in this fund comes from repayments of the housing loans issued under the housing rehabilitation program.

As of June 30, 2003, the City had almost $7.5 million in outstanding CDBG funded housing rehabilitation loans. The City maintains a "revolving" loan fund so that as loan repayments are received the funds are re-appropriated and loaned again. As in past years, the adopted fiscal year 2005 budget includes an

Special Revenue Funds

estimated amount for loan repayments (also known as "program income"). The estimate is based upon an analysis of the scheduled monthly payments for all outstanding loans. Because the routine repayments are quite predictable, they are included in the budget. As indicated in the table at the top of the previous page, loan repayments for fiscal year 2005 are projected to be $650,000. In some years, loan repayments significantly exceed expectations. For example, in fiscal year 2004 loan repayments are projected to be approximately $750,000, $350,000 ahead of budget. The additional amounts represent unscheduled pre-payments of loan balances due to property sales or re-financings. Due to the indeterminate nature of these prepayments, no attempt is made to include them in the budget. In the event significant prepayments are received during the year, a supplemental appropriation will be requested.

The chart below displays the CDBG budget by category of expense. Human service grants (Including capital grants) and housing rehabilitation loans represent 66% of the budget.



The CDBG human services grants are allocated, along with the General Fund human services funding, based upon recommendations submitted to the City Council by the City's Community Development and Human Services Committee. The Committee's recommendations for fiscal year 2005 grant awards, to be funded from the adopted fiscal year 2005 budget, were recently submitted to and approved by the City Council.

All requests for housing rehabilitation loans are evaluated by program staff and are submitted to the City's Loan Committee for approval. The Loan Committee is comprised of the Assistant City Administrator, the Community Development Director and the Finance Director. The Loan Committee can approve loans up to $60,000. Loans of more than $60,000 require approval of City Council.

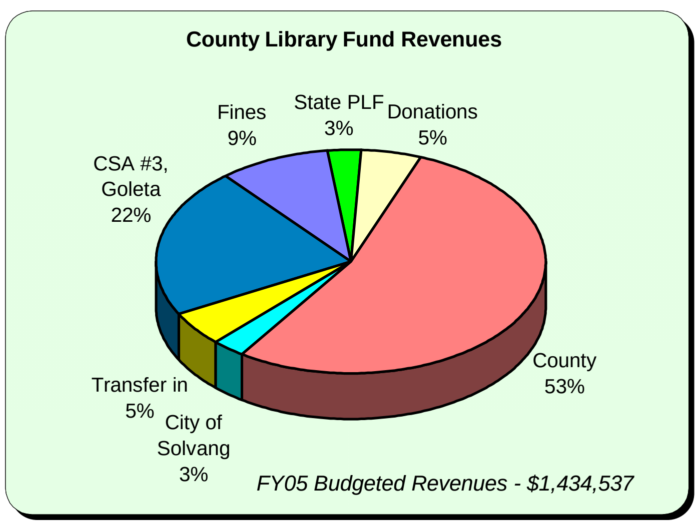
Special Revenue Funds

COUNTY LIBRARY FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 1,334,044	$ 1,228,193	$1,518,673	$1,405,000	$ 1,434,537
Operating expenditures	$ 1,401,019	$ 1,657,428	$2,079,108	$1,657,828	$ 1,632,289
Net addition to (use of) reserves	$ (66,975)	$ (429,235)	$ (560,435)	$ (252,828)	$ (197,752)

The County Library Fund accounts for the costs of providing a full range of library services to the residents of Solvang, Santa Ynez, Los Olivos, Carpinteria, Montecito, Goleta, under contract with the County of Santa Barbara. The chart below indicates that revenue to support these services comes from a variety of sources including the County, State Public Library Fund (PLF) Grant, the cities of Solvang and Carpinteria, fines, fees and donations. Additional funds for the Goleta library are provided by a special assessment (CSA #3). Although additional contributions from various "Friends of the Library" community groups are received occasionally, they are generally not budgeted because of the unpredictable nature of the donations. The budget does, however, include gifts from the Friends of Montecito and Carpinteria libraries used to support some program staffing at those libraries. No City of Santa Barbara funds are included in the County Library Fund budget.

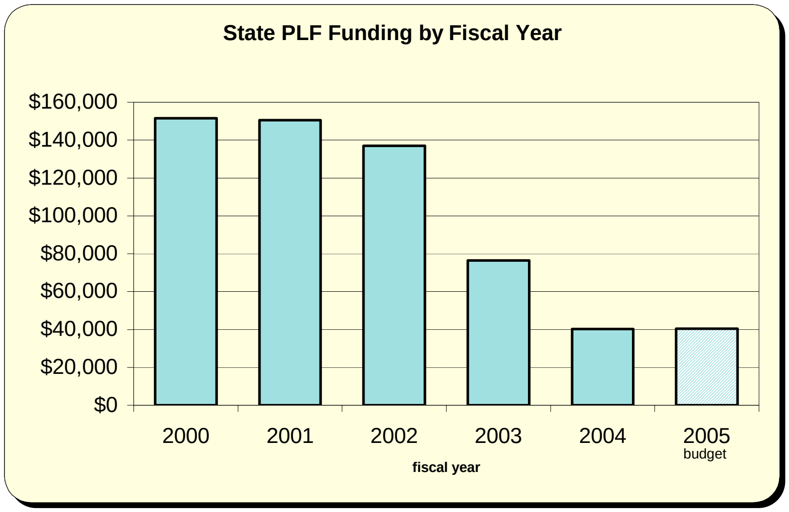
Under the terms of the agreement between the City and the County, the City is compensated for managing these County library services. The City's General Fund receives an administration fee amounting to 9% of the annual County appropriation for County (non-City) resident library services.



The adopted fiscal year 2005 budget is based upon staff's best estimates of next year's funding levels from both the County and the State. Changes in the level of either of these revenue sources will require corresponding program and expenditure adjustments. Given the grim budget outlook for both the State and counties, it is likely that the budget for these programs may have to be revised late in the fiscal year. Since neither the state nor the County generally adopt a budget prior to July 1st start of the fiscal year, such adjustments are usually brought before the Council in the autumn.

Special Revenue Funds

As with the City library system, the County Library Fund is under increasing fiscal pressure as the State continues to reduce funding to libraries statewide. State Public Library Fund (PLF) has been reduced several times in recent years. As the chart to the right indicates, the State PLF funding for the County Library System has declined over $110,000 (73%) from $150,000 as recently as fiscal year 2001 to a projected $40,000 in fiscal year 2005. Although the Governor's "May Revise" proposed fiscal year 2005 State budget does contain continued minimal PLF funding, there has been some discussion of a complete elimination of the PLF funding.



The adopted budget contains the use of approximately $198,000 in accumulated reserves to offset the impacts of other budget reductions. Most of the reserves will be used to fund $139,000 for the acquisition of collections materials. The balance of the reserves will be used to support various programs and activities.

Special Revenue Funds

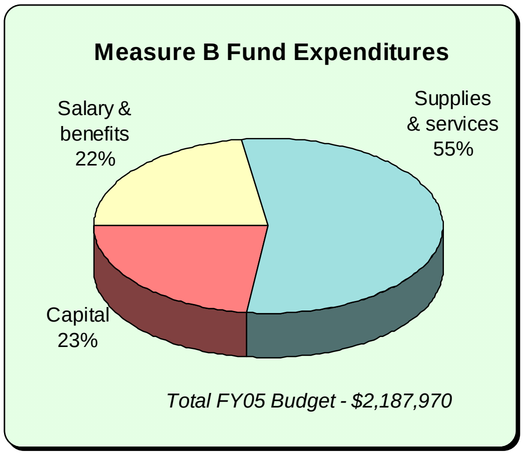
CREEKS RESTORATION & WATER QUALITY IMPROVEMENT (MEASURE B) FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 2,066,112	$ 2,104,780	$ 2,104,780	$ 2,145,880	$ 2,187,970
Operating expenses	905,033	1,653,511	1,803,090	1,509,670	1,687,970
Operating surplus	1,161,079	451,269	301,690	636,210	500,000
Capital budget	520,000	525,000	525,000	525,000	500,000
Net addition to (use of) reserves	$ 641,079	$ (73,731)	$ (223,310)	$ 111,210	$ -

In November 2000, the City's voters overwhelmingly approved Measure B, a two-percent increase in the City's transient occupancy tax effective January 1, 2001. Under the terms of the measure, all proceeds from the tax increase are restricted for use in the City's Creeks Restoration and Water Quality Improvement Program. In order to meet the intent of the measure, the City opened a Special Revenue Fund to account solely for all revenues and expenditures associated with this program.

The Creeks Restoration and Water Quality Improvement Program is managed by the City's Parks and Recreation Department. Under the direction of the Parks and Recreation Director, the Creeks Restoration and Water Quality Improvement Manager manages the program.

The adopted budget for fiscal year 2005 is approximately $2.2 million. $50,000 of the budgeted revenue is projected to come from investment income. The balance, just over $2.1 million, is projected to come from the two-percent transient occupancy tax (TOT). The $2.1 million TOT estimate for fiscal year 2005 is consistent with the assumptions used to budget the General Fund's TOT.

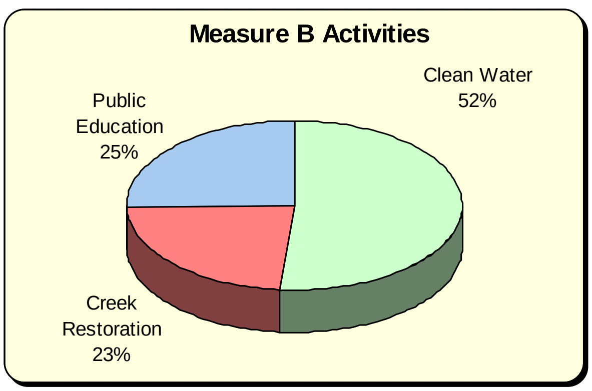


The chart on the right displays the expenditure budget by object of expenditure. As the chart indicates, 23% of the budget is dedicated to capital ($500,000). Projects include the beginning phases for the restoration of a city-owned six-acre parcel adjacent to Arroyo Burro Creek ($125,000); the enhancement of Old Mission Creek in the West Figueroa area ($125,000) and $200,000 for the restoration of the Arroyo Burro estuary. Although not included in the adopted budget, an ultra violet light water treatment facility will also be installed to improve water quality in Mission Creek pending receipt of $900,000 in State grant funds.

Special Revenue Funds

With salary and benefit costs representing only 22% of the budget, the Measure B Fund more closely resembles one of the City's Enterprise Funds rather than the General Fund. In addition to the five full-time positions, there is funding in the operating budget for program and technical support from the City's Public Works Department. These services include the in-school youth watershed education program, catch basin filter maintenance, and water quality capital project management. These funds (approximately $72,000) are budgeted in the supplies and services category (non-contractual services), but costs will only be charged based upon actual hours provided.

The chart below displays the adopted budget (operating and capital) by activity. Clean Water activities comprise approximately $1.1 million or 52% of the budget with specific focus on creek clean-ups ($150,000), water quality testing ($80,000), DNA microbial source tracking research ($50,000), and residential street sweeping ($153,000). A full-time Water Resources Specialist position provides storm water code enforcement, technical business assistance and storm drain monitoring.



Creek Restoration activities comprise 23% of the budget and include a full-time Restoration Planner position, maintenance of a native plant nursery and the restoration of Old Mission Creek at Bohnett Park ($30,000), neighborhood creek re-vegetation projects ($25,000) and management of three creek restoration and water quality capital projects, including the Arroyo Burro Estuary, Old Mission Creek restoration at West Figueroa and the restoration of the Las Positas Valley six-acre parcel.

Public Education activities comprise approximately $553,000 (25%) of the budget and include a full-time Outreach Coordinator position, youth education programs ($75,000), clean water business and neighborhood creek steward programs, as well as $100,000 for production and airing of bilingual radio and television educational campaigns. The adopted budget also includes public outreach activities through the monthly meetings of the Creeks Advisory Committee, community creek restoration and water quality events, collaborative projects with community organizations and other public agencies, and the development of educational materials.

In summary, the adopted fiscal year 2005 budget is balanced and includes a $500,000 capital program.

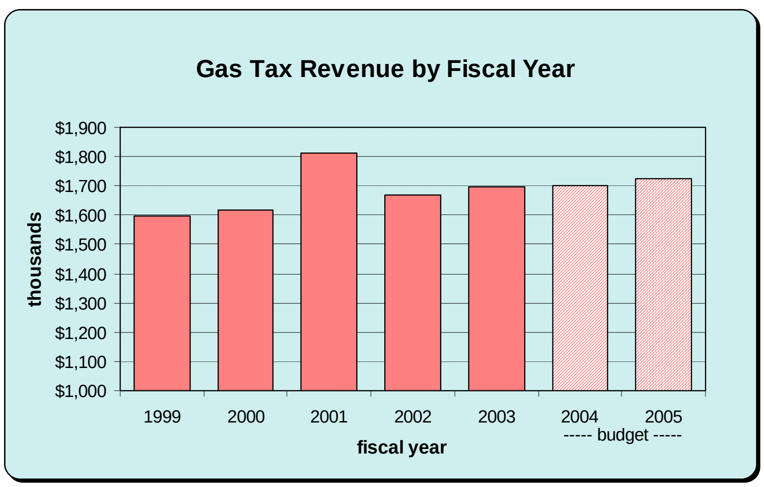
Special Revenue Funds

GAS TAX

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 1,698,393	$ 1,700,000	$ 1,700,000	$ 1,715,000	$ 1,725,000
Operating expenditures	1,698,393	1,700,000	1,700,000	1,715,000	1,725,000
Net addition to (use of) reserves	$ -	$ -	$ -	$ -	$ -

The Gas Tax revenue received by the City is a portion of the state's 18 cents per gallon tax on fuel used to propel a motor vehicle or aircraft. Article XIX of the California Constitution restricts the use of gas tax revenue to research, planning, construction, improvement, maintenance and operation of public streets and highways or public mass transit. The funds are distributed by the state on a per capita basis.

Paid to the City by the State, gas tax revenue is initially accounted for in the City's Gas Tax Special Revenue Fund. After receipt, all gas tax revenues are transferred to the City's Streets Fund for use in the City's street operations and maintenance activities. Each year, the City is audited by the State Controller's Office to ensure that the funds are used in accordance with state law.



The City anticipates receiving approximately $1.725 million in gas tax revenue in fiscal year 2005, which is approximately the same as the amount to be received in fiscal year 2004.

Special Revenue Funds

REDEVELOPMENT AGENCY (GENERAL) FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Total revenue	$ 10,670,837	$ 10,709,000	$ 10,709,000	$ 12,479,477	$ 11,199,000
Operating expenditures	12,047,408	10,709,000	11,893,863	10,069,388	11,257,500
Net addition to (use of) reserves	$ (1,376,571)	$ -	$ (1,184,863)	$ 2,410,089	$ (58,500)

The adopted fiscal year 2005 Redevelopment Agency (RDA) General Fund budget includes $11.2 million budgeted revenue, $11 million (98%) of which is from the incremental property tax ("tax increment") generated from within the Agency's one project area. Under State law, all redevelopment agencies are required to dedicate a minimum of twenty percent of total tax increment revenue to low and moderate housing programs. The remaining 80% of the tax increment may be used for any legally qualifying redevelopment activity, and represents the $11 million of tax increment budgeted in the RDA General Fund. The twenty percent of tax increment restricted to low and moderate housing programs is budgeted separately in the RDA Housing Fund. The balance of the RDA General Fund's budgeted revenue is from interest income ($175,000) and rental income on an Agency-owned property ($24,000).

With over 98% of its revenue coming from property taxes, the RDA is vulnerable to anything that impacts that revenue source. Over the last several years, the biggest threat to the Agency's revenue has come from the State's continual shifting of redevelopment agency property taxes to help address its own budget shortfall. Through the Educational Revenue Augmentation Fund (ERAF), the State has shifted property taxes from redevelopment agencies to schools, thus reducing its own obligation for school funding. The table on the right displays the amount of property tax lost to the State's ERAF shift. The fiscal year 2005 amount contained in the adopted budget is based upon the Governor's proposed budget (January 2004) and represents almost 6.5% of the Agency's total (non-housing) tax increment. However, the Governor's "May Revise" budget, if adopted, includes an additional ERAF shift, beyond what was proposed by the Governor in January, that would result in a total loss of over $1.3 million to the City's RDA. Unlike previous RDA ERAF shifts, which have been one-time, the Governor's proposed ERAF shift for fiscal year 2005 would be permanent and ongoing.

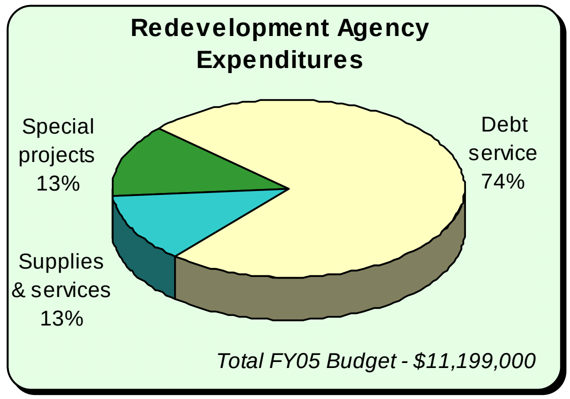
Fiscal Year	ERAF Shift
2003	$ 424,948
2004	704,140
2005	704,140

Like the revenues, the RDA expenditure budget is also straightforward. The RDA has no staff. Under a contract between the two legally separate entities, the City provides staffing for the Agency and bills the Agency for the costs. These costs are budgeted by the Agency as contractual services within the "supplies and services" category. The total supplies and services budget is approximately $1.4 million (13%). Of that amount, reimbursement to the City for direct

Special Revenue Funds

administrative and legal services totals approximately $745,000. In addition, pursuant to the results of a recently completed City cost allocation plan, the Agency reimburses the General Fund approximately $447,000 for administrative and management services provided by General Fund personnel (purchasing, accounting, auditing, etc.).

As displayed by the chart on the right, debt service consumes $8.3 million (74%) of the budget. The RDA has three outstanding tax allocation bonds. The table at the bottom of the page summarizes the three debt issues. In December 2003, the Agency issued what is likely to be its final (non-housing) bond issue. The Agency's only project area, the Central City Redevelopment Project Area, expires in 2012 and the Agency has already bonded against its projected future tax increment receipts.



The only other expenditure category, special projects, represents approximately $1.5 million (13%) of the budget. Specific expenditures include a contribution to the operation of the Downtown and Commuter Lot electric shuttles ($300,000). The contribution is a mitigation measure for the impacts of the downtown improvements financed by the Agency. The largest component of the special projects category is an unallocated $1.1 million. Normally, these funds would be available to fund Agency projects. However, because of the ERAF threat, the adopted budget preserves these funds as unallocated. As mentioned above, the ERAF shift contained in the Governor's proposed budget would cost the Agency approximately $704,000 of the unallocated $1.1 million.

Because a real possibility exists that the final ERAF amount could be even larger than the Governor's proposal, the Agency's adopted budget preserves the entire $1.1 million as unallocated until such time as the State adopts its budget.

Redevelopment Agency Debt

Issue	Original Amount	Outstanding at 1-Jan-04	FY 2005 Debt Service	Final Maturity
1995 Tax Allocation Bonds	$ 35,015,000	$ 14,130,000	$ 3,110,300	3/1/2008
2001 Tax Allocation Bonds	38,855,000	38,305,000	1,764,854	3/1/2019
2003 Tax Allocation Bonds	34,810,000	34,810,000	3,359,830	3/1/2019
Totals	$ 108,680,000	$ 87,245,000	$ 8,234,984	

Special Revenue Funds

REDEVELOPMENT AGENCY HOUSING FUND

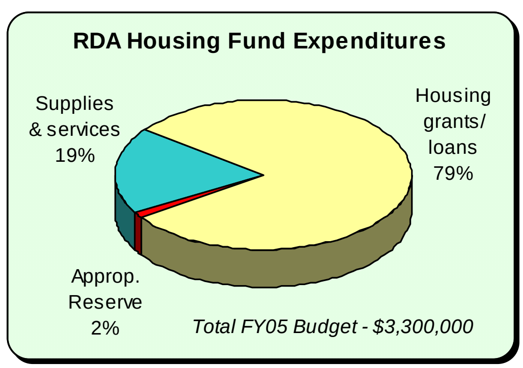
	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Total revenue	$ 3,181,251	$ 3,170,000	$ 3,170,000	$ 3,530,382	$ 3,300,000
Operating expenditures	5,143,900	3,170,000	7,481,905	1,558,044	3,300,000
Net addition to (use of) reserves	$ (1,962,649)	$ -	$ (4,311,905)	$ 1,972,338	$ -

The adopted fiscal year 2005 Redevelopment Agency (RDA) Housing Fund budget is balanced at $3.3 million.

Of the $3.3 million budgeted revenue, $2.75 million (83%) is from the incremental property tax ("tax increment") generated from within the Agency's one project area. Under State law, all redevelopment agencies are required to dedicate a minimum of twenty percent of total tax increment revenue to low and moderate housing programs. The remaining 80% of the tax increment may be used for any legally qualifying redevelopment activity. The $2.75 million of tax increment budgeted in the RDA Housing Fund meets the twenty percent state requirement.

The balance of the RDA Housing Fund's budgeted revenue is interest income on investments ($150,000) and on housing loans ($400,000). As of June 30, 2003, the Housing Fund had approximately $24 million of outstanding low and moderate-income housing loans.

The Agency's 20% tax increment that is restricted to low and moderate-income housing is not affected by the State's Educational Revenue Augmentation Fund (ERAF) property tax shift. In the past, the State has always prohibited redevelopment agencies from using any of their 20% housing set-aside funds to meet their ERAF obligation. That is unlikely to change in the future.



The chart on the right summarizes the Housing Fund's expenditures. The Housing Fund has no staff. Under a contract between the two legally separate entities, the City provides staffing for the Agency's Housing Fund and bills the Agency for the costs. These costs are budgeted in the Housing Fund as contractual services within the "supplies and services" category. The total supplies and services budget is approximately $611,000 (19%). Of that amount, reimbursement to the City for direct administrative and legal services totals approximately $400,000. In addition, pursuant to the results of a recently completed City cost allocation plan, the Agency Housing Fund reimburses the

Special Revenue Funds

General Fund approximately $60,000 for administrative and management services provided by General Fund personnel (purchasing, accounting, auditing, etc.).

As displayed by the chart on the previous page, funds for housing grants and loans comprise over $2.6 million (79%) of the budget. These housing funds are available to be loaned or granted by the Redevelopment Agency to meet the housing goals established by the Agency Board (City Council). A $50,000 appropriated reserve is also included in the adopted budget.

At over $3 million per year, the Redevelopment Agency's Housing Fund is able to direct significant resources towards what many consider to be the most pressing need facing the Santa Barbara area - developing and maintaining affordable housing.

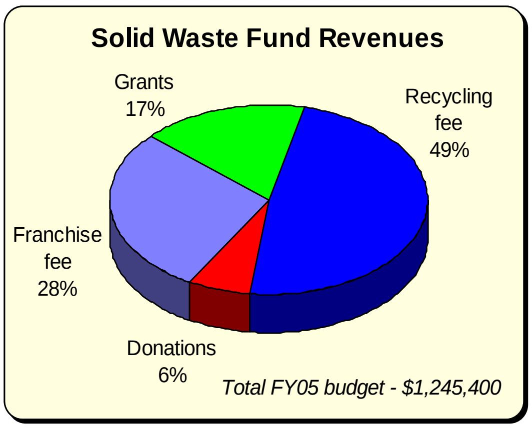
Special Revenue Funds

SOLID WASTE FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Total revenue	351,445	824,210	1,000,918	968,415	1,245,400
Operating expenditures	222,730	824,210	1,083,608	935,073	1,245,400
Net addition to (use of) reserves	$ 128,715	$ -	$ (82,690)	$ 33,342	$ -

The City's Solid Waste Fund was first established in fiscal year 2003. Prior to that time, solid waste activities were accounted for within the General Fund. Given the importance of the City's solid waste activities and the increasing and dedicated revenue sources supporting the solid waste activities, a separate special revenue fund was created with the adoption of the fiscal year 2003 budget.

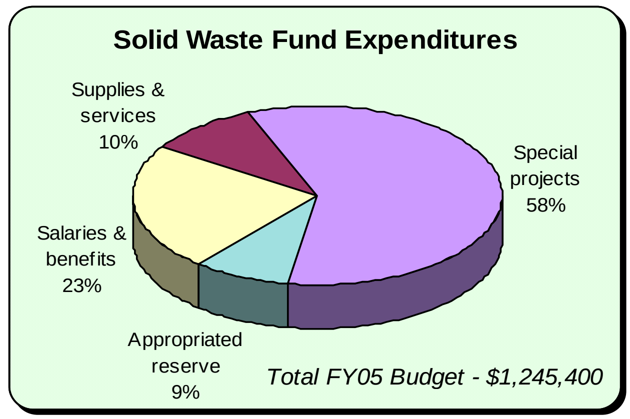
Funding for solid waste activities comes from several sources. The chart below details the projected solid waste revenue for fiscal year 2005. The largest source of revenue is a recycling fee ($600,900), which is generated from a 4% fee included in the trash collection rates. The franchise fee revenue ($352,500) is from a 2% franchise fee paid by the City's two contracted trash haulers. The balance of the revenue is from grants ($212,000) and donations from the City's two franchised haulers ($40,000 each). The donations are used for the Looking Good Santa Barbara program, dedicated to assisting the City with recycling outreach, beautification and graffiti abatement activities. Of the total grant revenue, $140,000 is from the State of California to support the City-run Antifreeze, Batteries, Oil and Paint (ABOP) recycling center, while $46,000 is to support the development of a public information campaign on refuse strategies.



The City has already made significant progress in meeting its recycling goals. The state-mandated goal of 50% diversion has been met. However, the City has established a goal to be the recycling leader in the state and achieve 70% diversion by 2010. The adopted fiscal year 2005 budget will further that goal by working towards higher recycling levels in the commercial and food-waste areas.

Special Revenue Funds

The chart on the right summarizes the adopted budget by object of expenditure. As the chart indicates, 58% of the total adopted budget will be used for special projects to further enhance the City's solid waste diversion. Only 33% of the budget is used for staffing and supplies and services. The only other component of the budget is an appropriated reserve ($107,703).



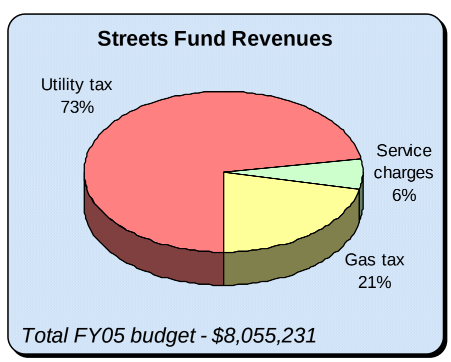
Special Revenue Funds

STREETS FUND

	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
	Fiscal Year				
Revenue	$ 4,867,878	$ 8,367,363	$ 11,284,305	$ 9,083,900	$ 8,055,231
Expenses:					
Operating	-	6,207,327	6,289,417	5,395,147	5,758,816
Capital	5,763,399	2,160,036	10,422,419	7,150,000	2,296,415
Total expenses	5,763,399	8,367,363	16,711,836	12,545,147	8,055,231
Net addition to (use of) reserves	$ (895,521)	$ -	$ (5,427,531)	$(3,461,247)	$ -

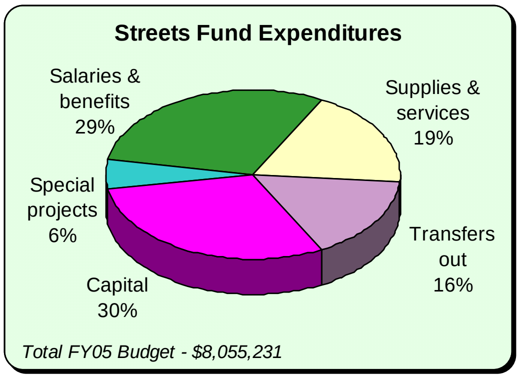
The Streets Fund accounts for all City-funded streets operations, maintenance and capital. Until fiscal year 2004, the Streets Fund was strictly a capital fund used to budget and account for streets capital projects. Prior to that time, all City-funded streets operations and maintenance activities were budgeted in the General Fund. However, because the streets operations and maintenance activities are funded almost entirely from restricted revenue, beginning with fiscal year 2004 they were moved out of the General Fund and into the Streets Fund. As a result of this budgeting and accounting change, the Streets Fund is now a special revenue fund and the budget has increased significantly. As the table above indicates, the Streets Fund budget has increased from approximately $5.8 million in fiscal year 2003, when it was capital only, to an adopted budget of approximately $8.1 million in fiscal year 2005.

The chart to the right summarizes the Streets Fund revenue sources. The single largest revenue source is utility users tax ($5.8 million). As required by City ordinance, fifty percent of the City's 6% utility users tax revenue is restricted to use for streets operations, maintenance and capital. Gas tax ($1.725 million) is the other significant revenue source. Paid to the City by the State, the City's gas tax revenue is first credited to a dedicated Gas Tax Fund. The total amount of gas tax revenue is then transferred into the Streets Fund for funding of qualifying streets expenditures. The final Streets Fund revenue source is service charges. Revenue associated with the City's downtown shuttles, which are operated for the City by the Metropolitan Transit District (MTD), include the fare revenue from the City's Downtown/Waterfront Shuttle ($125,000) and reimbursement from the City's Redevelopment Agency (RDA) for support of the commuter lot and Downtown/Waterfront shuttles ($300,000). The RDA's support of the shuttles is a mitigation obligation of the RDA as a result of the downtown projects funded by the Agency. Both of these revenues are used entirely and solely to pay for the costs of the shuttle operations.



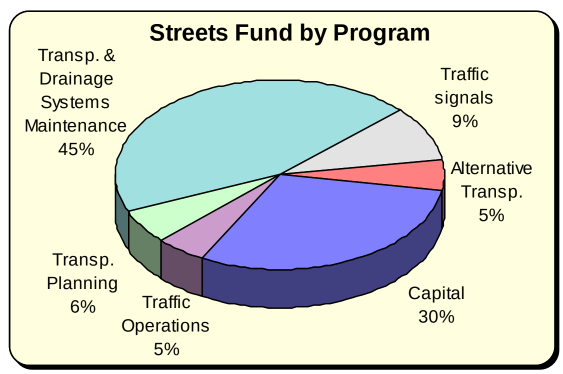
Special Revenue Funds

The chart below summarizes the Street Fund expenditures by object. The capital program ($2.4 million) constitutes 30% of the budget. For fiscal year 2005, the capital program includes the annual programs such as slurry seals and overlays ($851,661); street light installation and maintenance ($202,754) and the continuing replacement of the City's underground 6.6KVA power lines ($240,000). In addition, $677,000 is included as the City's share of the cost to replace and widen the bridge on Haley Street over Mission Creek. The balance of the project cost will be funded from a federal grant, estimated at $2.4 million.



Virtually the entire special projects category goes to the downtown and commuter lot shuttles ($425,000). As mentioned above, this entire amount is generated from fare revenue from the Downtown/Waterfront Shuttle ($125,000) and a contribution from the City's Redevelopment Agency ($300,000). The balance of the fund's budget supports streets operations and maintenance activities.

The chart on the right summarizes the Streets Fund expenditure budget by program activity. By far the largest activity is the Transportation and Drainage Systems Maintenance ($3.6 million). This activity includes maintenance and repair of streets, sidewalks, storm drains, traffic signage and markings and other infrastructure within the public right-of-way. The Alternative Transportation program is the shuttle bus activity discussed above.



In summary, the Streets Fund now accounts for all City-funded street operating, maintenance and capital activities, providing better accountability of the City's restricted street revenues.

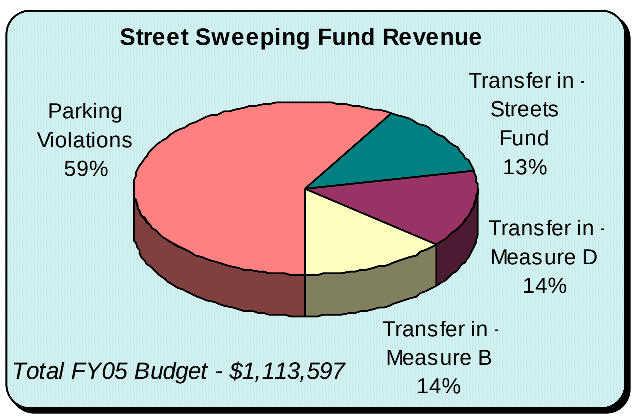
Special Revenue Funds

STREET SWEEPING FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	-	-	-	-	1,113,597
Operating expenditures	-	-	-	-	1,113,597
Net addition to (use of) reserves	$ -	$ -	$ -	$ -	$ -

The Street Sweeping Fund is a new fund established in fiscal year 2005. It consolidates all of the City's street sweeping operations into one dedicated fund.

As displayed in the chart below, there are two sources of street sweeping revenue. The largest revenue source is parking violations ($650,000). The parking tickets are issued to vehicles that are not moved off the streets during posted street sweeping times. The police department's parking enforcement officers have been issuing an average of 600 parking citation each week in support of the program. All revenue generated from these parking citations is returned to the Street Sweeping Fund. The balance of street sweeping revenue is transferred from other City funds. The transfers are from the Streets Fund ($150,000), the Transportation Sales Tax ("Measure D") Fund ($160,597) and the Creek Restoration/Water Quality ("Measure B") Fund ($153,000). The Measure B contribution is used to fund a portion of the expanded residential street sweeping program.

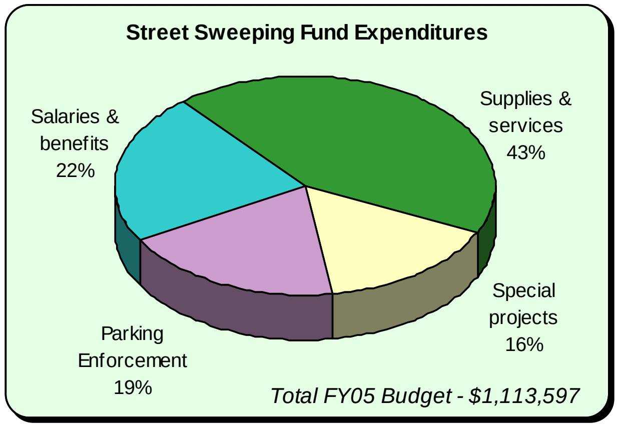


As recently as fiscal year 2000, the City's regular street sweeping was limited to the downtown commercial area. The residential street sweeping program was started as a pilot program on the Westside in October 2001 and was expanded to the Eastside on October 2003. The goal of the program is to improve the appearance of the City by reducing the amount of litter and contaminates from automobiles that flow into the storm drains and creeks. The City sweeps the residential areas on a weekly basis and removes approximately 53 cubic yards of debris each week. The goal is to eventually expand street sweeping coverage over time to the entire city.

The chart on the following page summarizes the fund's expenditures. Salaries and benefits constitute 22% of the fund's total budget. Currently, the street sweeping is handled through a combination of contract and in-house resources. The supplies and services category includes funds for the contract portion of the program ($359,000). The "special projects" category contains

Special Revenue Funds

approximately $179,000 that will be used for tree trimming and signage when street sweeping is expanded to additional areas of the City. The other expenditure category is for parking enforcement. Approximately $210,000 is reimbursed to the City's Police Department (General Fund) for the costs of enforcing the street sweeping-related parking restrictions. With anticipated parking citation revenue of $650,000 (see above), the net revenue to the Street Sweeping Fund from citations will be approximately $440,000.



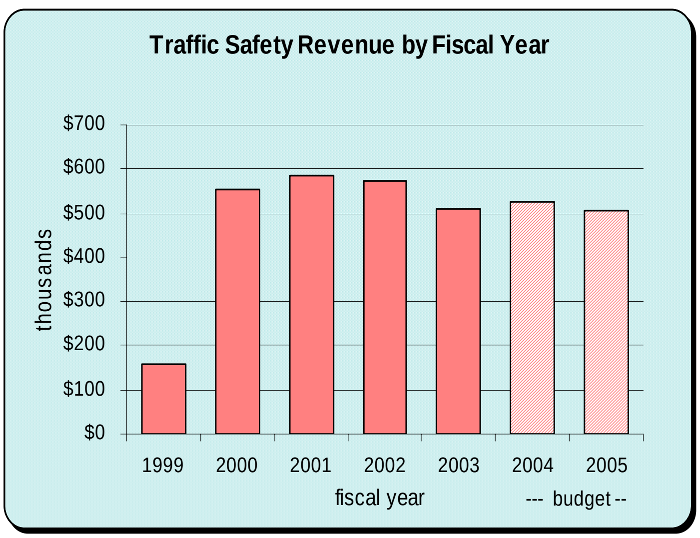
Special Revenue Funds

TRAFFIC SAFETY FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 511,685	$ 525,000	$ 525,000	$ 550,000	$ 505,000
Expenditures					
Operating	-	25,000	25,000	25,000	30,000
Transfers out	482,180	500,000	500,000	525,000	475,000
Total expenditures	482,180	525,000	525,000	550,000	505,000
Net addition to (use of) reserves	$ 29,505	$ -	$ -	$ -	$ -

Pursuant to state law, the City must deposit all fines and forfeitures received as a result of citations issued by City police officers for Vehicle Code violations into a special "Traffic Safety Fund." These funds may be used solely for traffic control devices, maintenance of equipment and supplies for traffic law enforcement, traffic accident prevention, the maintenance, improvement or construction of public streets, bridges or culverts and the compensation of school crossing guards who are not regular, full-time employees of the City's Police Department. The County pays these funds to the City. After being recorded in the City's Traffic Safety Fund as required by law, virtually the entire amount received is transferred to the General Fund and is expended by the Police Department for traffic law enforcement and school crossing guards. The small amount of operating expenditures recorded within the Traffic Safety Fund ($30,000) is payment for blood testing on individuals suspected of driving while intoxicated.

As the chart indicates, there was a substantial increase in the City's Traffic Safety revenue in fiscal year 2000. Effective with fiscal year 1999, State legislation changed the Vehicle Code to allocate to cities fees paid for "court supervised programs" (i.e., traffic schools) in lieu of base fines. The City began receiving this additional revenue in fiscal year 2000. Since this change in State law, the amounts received by the City have been fairly stable at around $500,000 or more. Based upon the actual amounts received in fiscal year 2003, budgeted revenue for fiscal year 2005 has been reduced to $505,000.

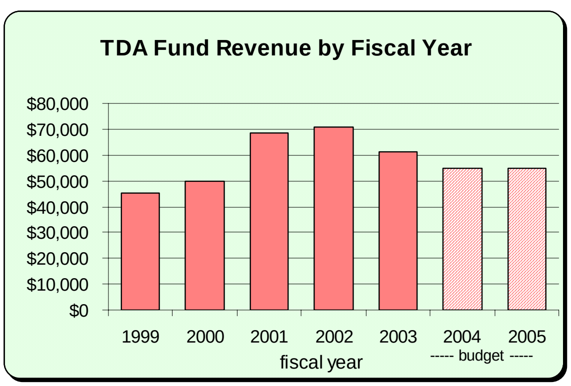


Special Revenue Funds

TRANSPORTATION DEVELOPMENT FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 61,296	$ 55,000	$ 55,000	$ 55,000	$ 55,000
Capital expenditures	158,862	55,000	55,000	55,000	55,000
Net addition to (use of) reserves	$ (97,566)	$ -	$ -	$ -	$ -

Transportation Development Act (TDA) funds are restricted for use in support of alternative transportation including sidewalks and bikeways. Each year, the City receives approximately $50,000 of TDA funds from the County. This revenue along with approximately $5,000 of annual interest income earned on accumulated balances is appropriated each year to the Street Capital Program. Because of the relatively small amount of TDA revenue received annually, the proceeds are often accumulated over multiple years in order to fund specific projects. For example, in fiscal year 2003, TDA fund expenditures included the use of over $97,000 of accumulated prior year balances for the Sidewalk In-Fill Program. Total expenditures of approximately $159,000 represented almost two years of accumulated TDA revenues. This accumulation of prior year amounts also generates additional revenue in the form of interest income.



As the chart on the left indicates, the City's annual TDA revenue has increased somewhat since 1999. Based upon this increase, the budget for TDA revenue was increased in fiscal year 1999 from $25,000 to $50,000 annually, with the balance of revenue budgeted each year attributable to interest income.

A summary list of the Streets Capital Program, which is funded in small part by TDA revenue, can be found in the next section of this document, Capital Program. Additional detail of the Streets Capital Program can be found within the Public Works section of the document. For fiscal year 2005, the TDA revenue will be used to continue the Sidewalk In-Fill Program.

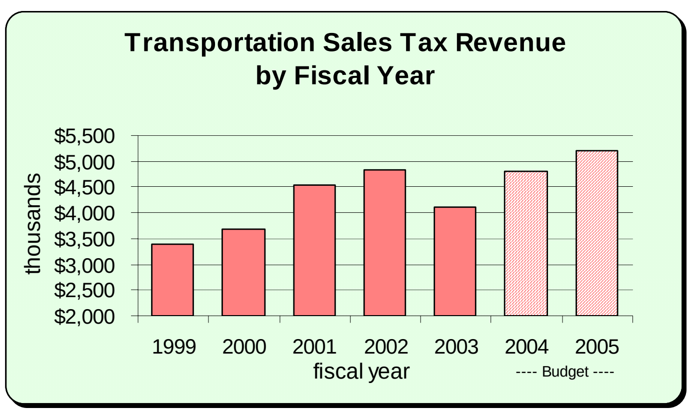
Special Revenue Funds

TRANSPORTATION SALES TAX (MEASURE D) FUND

	Fiscal Year				
Revenues	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Transportation sales tax	$ 4,120,382	$ 4,800,000	$ 4,800,000	$ 4,900,000	$ 5,200,000
Interest income	212,517	225,000	225,000	160,000	140,000
Total revenue	4,332,899	5,025,000	5,025,000	5,060,000	5,340,000
Operating expenditures	2,223,946	2,892,630	3,662,908	3,557,141	3,021,263
Operating surplus	2,108,953	2,132,370	1,362,092	1,502,859	2,318,737
Capital budget	2,373,143	2,609,020	6,029,769	4,500,000	2,318,737
Net addition to (use of) reserves	$ (264,190)	$ (476,650)	$(4,667,677)	$(2,997,141)	$ -

The Transportation Sales Tax fund is also known as the "Measure D" Fund after the designation of the ballot proposition approved by Santa Barbara County voters in November 1989. The ballot measure enacted a twenty-year, one-half cent sales tax, the proceeds of which are restricted for use in the City's streets and transportation programs. The revenue generated by this tax is subject to an annual "maintenance of effort" requirement to ensure that the proceeds of the sales tax will be used to supplement - not supplant - the City's existing streets programs. For any year in which the City fails to maintain its discretionary Streets program (operating and capital) at or above the base year (fiscal 1987) level of $2.7 million, the City is not entitled to the Measure D revenues. The City is audited each year to verify that the maintenance of effort has been met.

The adopted fiscal year 2005 Measure D budget is balanced at $5.34 million, including a capital program of just over $2.3 million. As indicated in the chart below, the City's Measure D sales tax revenue grew steadily through fiscal year 2002, but came in lower in fiscal year 2003 because of lower sales tax receipts and allocation adjustments.



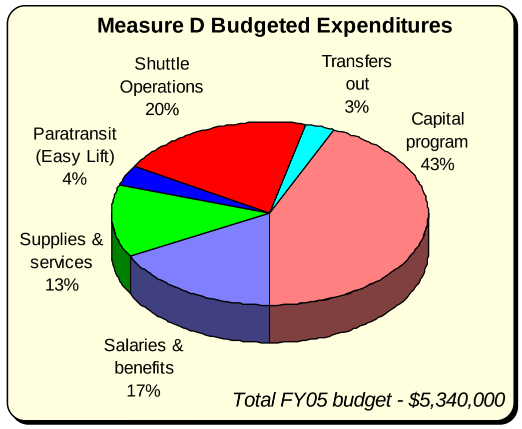
As in the past, the revenue estimate, and therefore the budget, is based upon an estimate provided by the Santa Barbara County Association of Governments (SBCAG). SBCAG is the agency that oversees the Measure D program on a countywide basis. Traditionally, the revenue estimate provided by SBCAG has been conservative. This has resulted in actual revenue exceeding budget, often leaving a fiscal year-end budget surplus. Although there was a decline in the sales tax revenue in fiscal year 2003 of almost $750,000 (15%) to $4.1 million, current fiscal year receipts are expected to meet the $4.8 million budgeted amount. The $5.2 million projection for fiscal year 2005 Measure D sales tax represents an 8%

Special Revenue Funds

increase over the current year and, if achieved, will be the first time this revenue source will surpass $5 million.

The Measure D Fund budget is developed based upon annual and five-year program of projects that is prepared by the City and submitted to SBCAG for approval. The adopted fiscal year 2005 budget is consistent with those plans.

As mentioned above, just over $2.3 million or 43% of the adopted fiscal year 2005 budget is dedicated to the Street Capital Program, including $1.2 million for the slurry seal program and $633,000 for sidewalk repairs and infill. The budget also includes almost $1.1 million (20%) for the Downtown and Cross-town Shuttle programs and $190,000 (4%) represents a transit grant to Easy Lift for para-transit services. The balance of the budget, approximately $1.75 million supports street maintenance activities.



With an adopted fiscal year 2005 budget totaling just over $5.3 million, Measure D has been, and continues to be, a critical component of the City's street operations and capital programs.

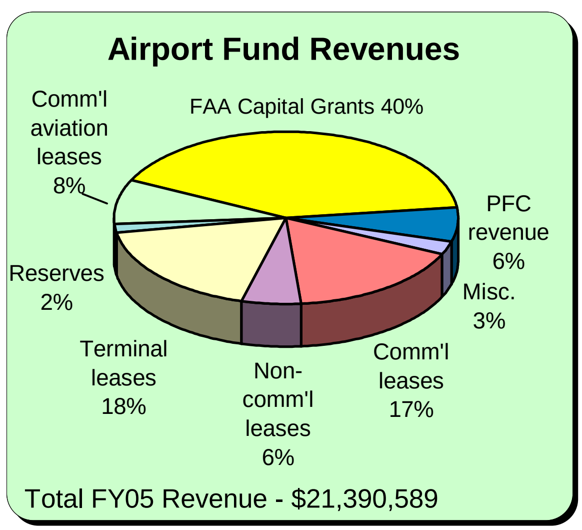
Enterprise Funds

AIRPORT FUND

	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
	Fiscal Year				
Operating budget					
Revenue	$ 10,712,159	$ 9,916,777	$ 9,916,777	$ 11,262,285	$ 10,948,274
Expenses	8,619,676	9,331,777	9,748,141	9,123,061	10,346,532
Operating surplus	$ 2,092,483	$ 585,000	$ 168,636	$ 2,139,224	$ 601,742
Capital budget					
FAA & capital grants	$ 1,596,184	$ 2,621,164	$ 21,864,396	$ 8,694,500	$ 8,694,500
PFC revenue	1,013,573	1,100,000	1,100,000	1,155,075	1,365,000
Capital expenses	3,076,145	3,206,164	24,694,963	3,100,000	11,044,057
Net addition to (use of) reserves	$ 1,626,095	$ 1,100,000	$ (1,561,931)	$ 8,888,799	$ (382,815)

The adopted fiscal year 2005 Airport Fund budget reflects an operating budget of $10.3 million and a capital program of just over $11 million.

The chart below displays total fiscal 2005 operating and capital revenues as contained in the adopted budget. As the chart indicates, virtually all of the Airport's operating revenue is derived from leases. Overall, fiscal year 2005 operating revenue is projected to be approximately $1 million (10%) higher than the revenue contained in the adopted fiscal 2004 budget. Over two thirds of the increase is projected to come from airline terminal operations. Commercial industrial leases are projected to grow approximately $436,000 (38%) and commercial aviation airline terminal facility leases are projected to grow approximately $198,000 (12%). Given the operating revenues realized in fiscal year 2003, staff feels that the revenues estimates for fiscal year 2005 are conservative and that actual revenue in fiscal year 2004 will likely exceed budget.



The most significant component of the adopted budget is the capital program. At $11 million, it is more than three times as large as the adopted fiscal year 2004 capital program because it contains a number of large projects from the Airport Facilities Master Plan. The implementation of this plan continues to be a top priority for the City.

Funding for the Airport's capital program comes from three sources. FAA capital grants continue to fund the largest portion of the Airport's capital program, including a significant portion of the work associated with the Airport Facilities Master Plan. As the table on the preceding page

Enterprise Funds

indicates, the Airport's FAA grants are estimated at almost $8.7 million for fiscal year 2005. In most cases, FAA grants fund 90% of approved project costs, with the Airport required to provide 10% matching funds. However, with the adoption of new FAA legislation, the Airport's matching share has been reduced to 5% effective with the 2004 federal grant. The City may use Passenger Facility Charge revenue to meet the matching funds requirement.

The Airport's second source for capital funding is the Passenger Facility Charge (PFC). With the approval of the FAA, on January 1, 1998, the Airport began to levy and collect a $3 PFC. Again with FAA approval, on November 1, 2003, the Airport's PFC was raised to $4.50. The PFC is a fee per airline passenger ticket with the proceeds restricted by federal law to approved capital improvements. It is estimated that the PFC will generate approximately $1.365 million in fiscal year 2005, all of which will be accumulated for future projects.

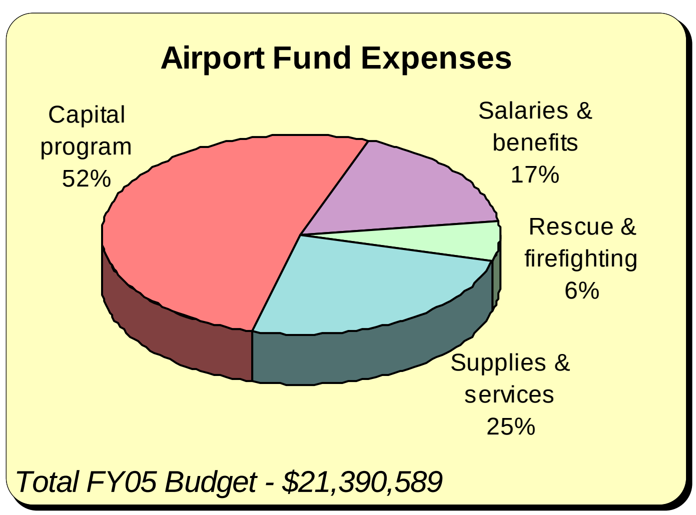
The third source for capital funding comes from Airport Fund operating revenue in excess of operating expenses. For fiscal year 2005, operating revenue is projected to contribute just over $600,000 to the capital program. In addition, approximately $1.7 million of accumulated Airport reserves will be used for capital. The table on the right summarizes the funding for the adopted capital budget.

FY 2005 Capital Budget

Funding Source	Amount
Operating Revenue	$ 601,742
Airport Fund Reserves	1,747,815
FAA Capital Grants	8,694,500
Total	$11,044,057

The chart below displays expenses in the adopted fiscal year 2005 Airport Fund budget by category. As discussed above, the capital program represents over half of the total budget (52%). The largest projects in the adopted capital budget include Phase 3 of the Runway 7-25 Safety Area Extension project ($6 million), the construction of new Taxiway M ($2.4 million) and Phase 2 of the North Taxiway B Relocation ($313,000). Additional details on the Airport's complete capital program may be found in the Capital Program section of this document.

In the operating budget, supplies and services (25%) represent a significant portion of the budget. The cost of Airport Rescue and Firefighting (ARFF) services represents 6% of the budget. ARFF services are provided to the Airport by the City's Fire Department with the Airport Fund reimbursing the City's General Fund for personnel costs. For fiscal year 2005, the Airport Fund budget contains almost $1.3 million for this required service. Over the last three years, the Airport Fund's operating costs have increased substantially. The



Enterprise Funds

largest portion of these cost increases is related to increased security requirements in the wake of the September 11, 2001 terrorist attacks. Five full-time security positions were added in February 2002 at a cost of almost $275,000. In addition, the adopted budget contains more than $250,000 for additional contract security services now required under federal regulations. The federal government has entered into a Memorandum of Agreement with the City to reimburse the Airport Fund for some or all of these costs.

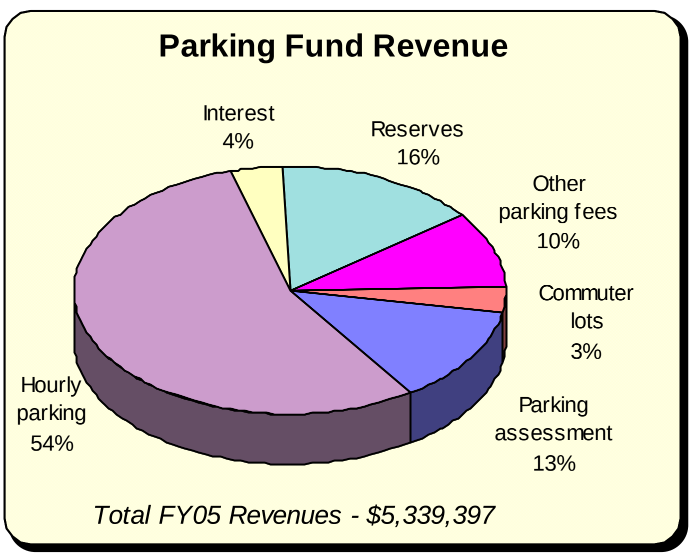
Enterprise Funds

DOWNTOWN PARKING FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 4,685,609	$ 4,850,000	$ 4,850,000	$ 4,845,000	$ 4,510,000
Operating expenses	4,621,132	4,294,747	4,471,096	4,294,153	4,694,395
Operating surplus	64,477	555,253	378,904	550,847	(184,395)
Capital budget	-	530,000	2,582,277	2,500,000	645,002
Net addition to (use of) reserves	$ 64,477	$ 25,253	$(2,203,373)	$(1,949,153)	$ (829,397)

The adopted fiscal year 2005 Parking Fund operating budget is $4.7 million with a capital program of $645,002. The budget relies on $184,395 of reserves to balance the operating budget and an additional $645,002 to fund the capital program. The use of reserves by an enterprise fund to balance the operating budget is generally contrary to City policy. However, as discussed below, the reserves will be used to backfill for the temporary loss of substantial parking fee revenue during construction of the Granada Garage. Because of the discrete, one-time nature of this revenue loss, the use of reserves is still within established city policy.

As the chart below indicates, the various parking user fees provide the bulk of the Parking Fund revenue. Combined, these fees represent 67% of total revenue. The commercial parking assessment (PBIA) that supports a portion of the seventy-five minute free parking period in the City's downtown lots is budgeted to provide $675,000 (13%) of total revenues. The only other Parking Fund revenue is interest income, budgeted at $200,000 (4%). As mentioned above, the revenue estimates for hourly parking have been reduced approximately $375,000 to reflect the anticipated loss of parking capacity during construction of the Granada Garage. Construction is expected to begin during the first half of fiscal year 2005. Given the unique and one-time nature of this revenue loss, the use of reserves to balance the operating budget is still within the City's established reserve policy.

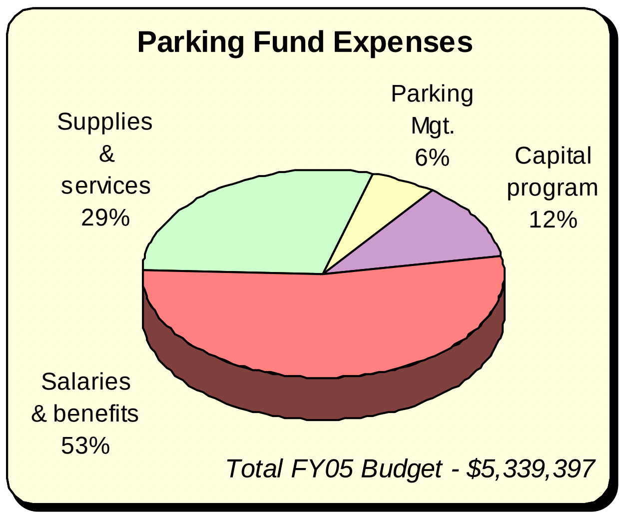


The Granada Garage project is still the

Enterprise Funds

most significant issue facing the Parking Fund at this time. As one of the largest capital projects ever undertaken by the City, the Granada Garage project will continue to be the top priority of the Parking Fund and the Public Works Department. Once construction does begin, Parking Fund staff will be responsible for implementing plans to mitigate the associated impacts on both the parking inventory and the neighboring businesses.

As the chart below indicates, the largest segment of the Parking Fund's expense budget is salaries and benefits (53%). Just less than half ($1.3 million) of the $2.9 million in salaries and benefits is temporary wages for staffing the City's various lots.



Several years ago, a new program, Parking Management, was added to the Parking Fund. The Parking Management Program is intended to reduce the demand for commuter parking in the downtown area by encouraging the use of alternative transportation. The program funds educational efforts and incentives to encourage commuters to choose alternative means of transportation. It also supports downtown transit services. The programs provide particular incentives to downtown workers to make use of alternative transportation. The adopted budget provides over $460,000 for the Parking Management Program activities, including alternative transportation programs and incentives, including $100,000 for the "My-Ride" free bus pass program.

The adopted capital program includes capital maintenance on the City's downtown lots ($295,000) and the set up and furnishing of parking staff offices, including installation of a high-speed communications link, in the soon-to-be constructed Granada Garage ($350,000).

The Parking Fund is in good financial condition with reserve balances well in excess of levels required by City policy. However, one of the issues facing the Parking Fund over the next several years will be increasing capital maintenance needs on the downtown parking facilities, especially the garages, as they begin to age. Staff expects that the annual capital program may need to double over the next several years in order to maintain the City's investments in these expensive assets. The extent and costs of the required capital maintenance will determine if and when future rate increases are necessary.

Enterprise Funds

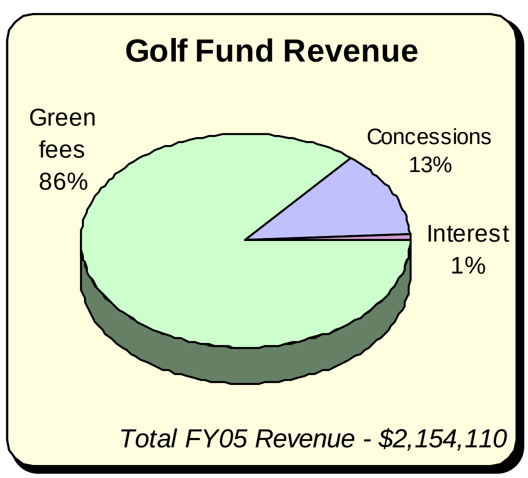
GOLF FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 2,001,412	$ 2,064,500	$ 2,064,500	$ 2,044,494	$ 2,154,110
Operating expenses	1,927,017	1,764,500	1,871,571	1,866,086	1,901,888
Operating surplus	74,395	300,000	192,929	178,408	252,222
Capital budget	365,065	300,000	379,917	379,917	252,222
Net addition to (use of) reserves	$ (290,670)	$ -	$ (186,988)	$ (201,509)	$ -

The Golf Fund adopted fiscal year 2005 budget contains operating revenue sufficient to support a $1.9 million operating budget and a capital program of $252,222. Operating revenue in the adopted budget reflects a modest 4% growth over the fiscal year 2004 adopted budget. The revenue estimate reflects the impact of modest increases to most of the Golf Fund's fees. Most of the green fees will increase by only $1.

Greens fees of various types comprise 86% ($1.85 million) of the revenue budget. The Golf Fund's fee structure currently offers discounts to residents of Santa Barbara County. Residents may purchase a resident card for a nominal $15 annual fee. The card entitles the holder to discounts of from $7 per round (weekday play) to $13 per round (weekend play). Additional discount programs are available for both weekday-only and full-week play. Staff is recommending an increase in the weekday-only discount from $50 to $75 and in the full-week discount from $75 to $100. The adopted budget also includes a proposal to expand the definition of "resident" to include Ventura County.

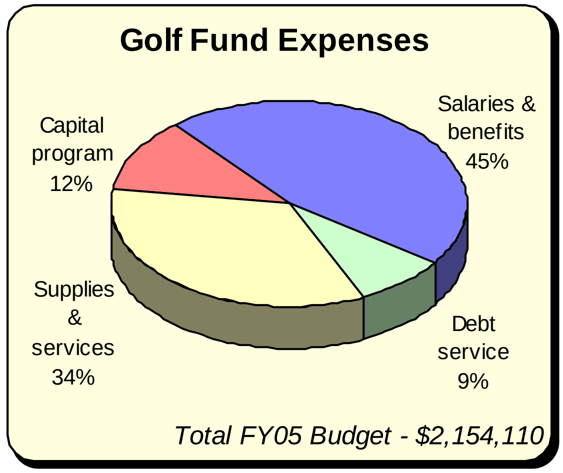
With the exception of a small amount of investment income, the balance of the Golf Fund revenue is from concession agreements with the golf professional and the clubhouse restaurant. Revenue from these agreements is budgeted at $275,000. Golf Fund staff perform all course maintenance but the golf professional provides management of course play, golf lessons and operation of the pro shop, under a concession agreement with the City. Food services are provided by a separate concession agreement.



Expenses in the adopted budget, including capital, total approximately $2.2 million. The chart on the following page summarizes the distribution of expenses. Salaries and benefits comprise 45% of the budget. Other than personnel costs, water is the Fund's single largest cost ($159,000). In terms of acre-feet consumed, the golf course is

Enterprise Funds

one of the largest water customers in the City's municipal water system. The adopted capital program ($252,222) includes the purchase of replacement power turf equipment ($90,000) and various improvements to tees, greens and cart paths ($162,222).



The fund's debt service, at just over $184,000, is principal and interest on the Golf Fund's share of the 2002 Municipal Refunding Certificates of Participation (COP). The 2002 certificates were issued to refund certificates originally sold in 1986 and previously refunded in 1993. The original proceeds were used to expand and renovate the clubhouse and to install a new irrigation system for the entire course. The 2002 refunding lowered the Fund's annual debt service by approximately $15,000. The principal balance currently outstanding is approximately $2 million. Final maturity of the certificates is in 2018.

Overall, the Golf Fund is in good financial condition. Operating revenues more than meet operating expenses and the Fund maintains reserve balances in accordance with the City's policy requirements.

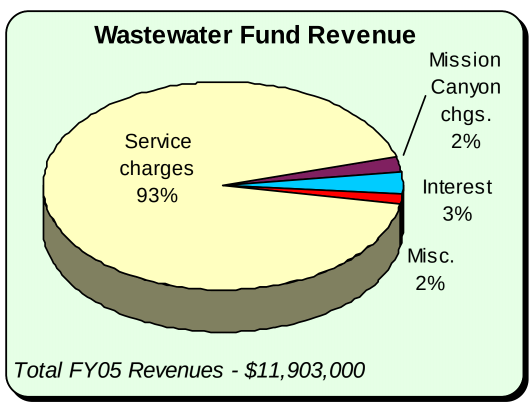
Enterprise Funds

WASTEWATER FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 9,994,460	$ 10,575,000	$ 10,575,000	$ 10,540,000	$ 11,903,000
Operating expenses	7,628,716	9,068,006	9,178,284	9,178,284	10,383,000
Operating surplus	2,365,744	1,506,994	1,396,716	1,361,716	1,520,000
Capital budget	2,629,814	3,954,000	3,954,000	3,954,000	1,520,000
Net addition to (use of) reserves	$ (264,070)	$ (2,447,006)	$ (2,557,284)	$ (2,592,284)	$ -

The adopted fiscal year 2005 Wastewater Fund budget projects enough revenue to fund all operating costs and a $1.5 million capital program.

The budget reflects a 16% wastewater service rate increase, effective July 1, 2004, as recommended by the City's Water Commission and adopted by City Council. It is estimated that the 16% across-the-board rate increase will generate an equal increase in overall service charge revenue to the Wastewater Fund. A portion of the rate increase will fund increasing operating costs, but it is current and future capital costs that are by far the largest reason for the significant rate increase. This increase is the third consecutive annual increase after almost a decade of no changes in wastewater rates. Despite the financial pressures of increasing capital needs, the fund continues to maintain a solid financial position. However, as discussed below, the increasing capital needs dictate the rate adjustment and may require additional, albeit much more modest, rate increases over the next several years.

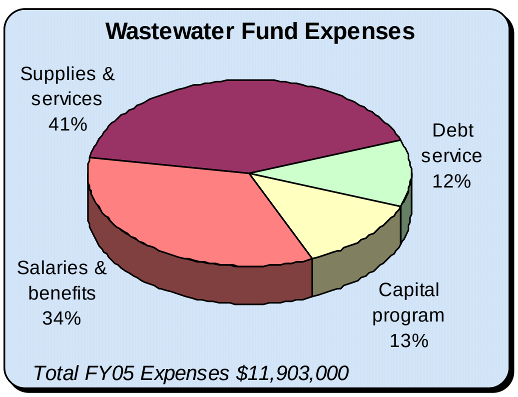


Wastewater Fund revenue is much more stable than revenue in the Water Fund. Wastewater revenues are comprised almost entirely of the regular, monthly service charges. Because these are based upon the customer's water usage in the lower rate blocks, they are more stable and less susceptible to variations than metered water sales. Service charges are projected to provide $11 million (93%) of the $11.9 million revenue total. Investment income, the second largest source of revenue for the fund, is budgeted at $375,000. This is a reduction of $150,000 from the current year budget due to the continuing low interest rate environment. The only other revenue of note is the $275,000 representing charges to Mission Canyon (non-city) residents.

Enterprise Funds

Wastewater Fund operating expenses are budgeted at just under $10.4 million and the adopted capital program is $1.5 million. As the chart below indicates, capital represents 13% the overall budget.

Debt service, at $1.4 million, represents 12% of the budget. At the time of adoption of this budget, the Wastewater Fund had no debt. However, in July 2004, only two weeks after the start of the fiscal year, the Wastewater Fund issued 25-year bonds for $20.41 million. The bond proceeds will generate $18.5 million of project funds of which $16.5 million will be used for major renovations at the El Estero Treatment Plant. The plant is now 25 years old and in need of significant rehabilitation. A recent independent evaluation of the facility identified a ten-year capital improvement program necessary to protect the City's massive investment and maintain compliance with the more stringent federal and state treatment standards. A total of $26.5 million in adopted capital improvements was identified over the ten-year horizon of the study. The proceeds of the debt issuance will allow those improvements to begin this year.



The remaining $2 million from the debt issue will be used to resolve some specific wet-weather capacity problems in the wastewater collection system. Because the bonds were issued in July, the adopted budget contains a full year of debt service.

Although the adopted capital program ($1.5 million) is less than prior years, when combined with the $18.5 million of capital debt proceeds discussed above the total capital program over the next two or three years will easily approach $25 million. Managing the projects, especially those at the El Estero Treatment Plant, will be a major focus of the Wastewater Fund (Public Works) staff. In addition, the capital budget contains almost 750,000 for lift station improvements, including the elimination or reconstruction of the San Marcos lift station ($650,000).

In large measure it is the necessary capital improvements that are driving the adopted rate increase. Although adopted rate increases will be kept to the minimum level necessary, maintenance of the El Estero Treatment Facility and the wastewater collection system is absolutely essential.

In summary, the Wastewater Fund operating budget is balanced and a substantial capital program is planned for fiscal year 2005.

Enterprise Funds

WATER FUND

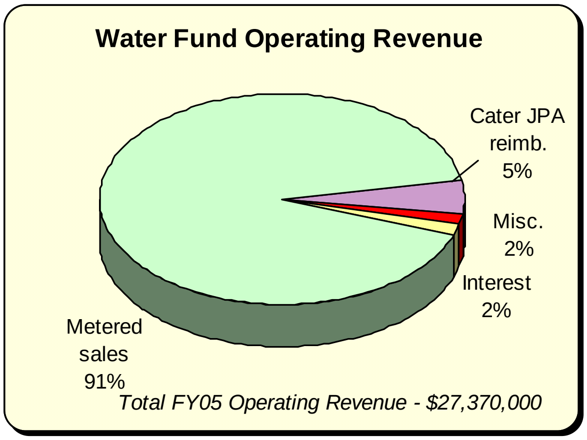
	Fiscal Year 2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 24,138,397	$ 24,641,937	$ 24,656,937	$ 24,788,946	$ 27,370,000
Operating expenses	18,707,702	21,923,471	22,258,244	21,973,400	22,817,000
Operating surplus	$ 5,430,695	$ 2,718,466	$ 2,398,693	$ 2,815,546	$ 4,553,000
Capital budget	6,089,980	6,412,497	6,412,497	4,931,000	4,553,000
Net addition to (use of) reserves	$ (659,285)	$ (3,694,031)	$ (4,013,804)	$ (2,115,454)	$ -

The adopted fiscal year 2005 Water Fund budget contains operating revenues sufficient to fund a $22.8 million operating budget and a $4.6 million capital program.

The adopted budget reflects a 4% rate increase for metered water sales, effective July 1, 2004, as recommended by the City's Water Commission and adopted by Council. It is estimated that, overall, the rate increase will generate an approximate 10% increase in metered sales revenue. A small portion of the rate increase will fund increasing operating costs, but it is current and future capital costs that are by far the largest reason for the increase.

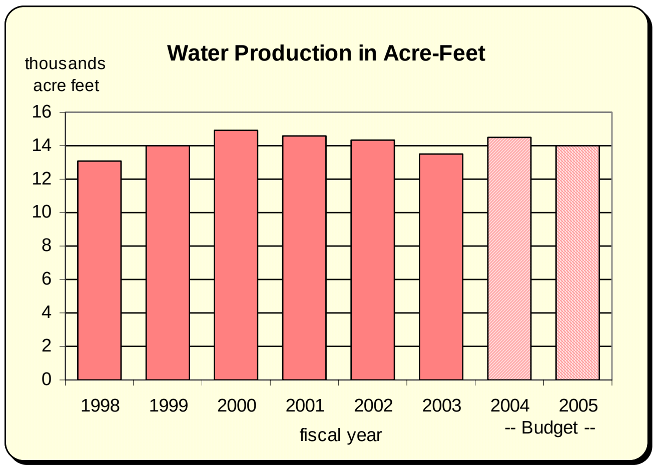
As the chart below indicates, the vast majority of estimated Water Fund revenue is provided by metered water sales ($25.1 million or 91%). Interest income, budgeted at $450,000, is derived from the investment of the Water Fund's capital and operating reserves. The estimate for investment income is approximately $250,000 below the amount budgeted in the current fiscal year due to the continued low interest rate environment as well as lower Water Fund reserve balances.

The other notable Water Fund revenue is a reimbursement from the Carpinteria and Montecito water districts. Under a joint powers authority agreement (JPA), the City treats all water for both districts at the City's Cater water treatment plant. Under the terms of the JPA, the districts pay their pro-rata share of the operating and capital costs of the Cater treatment facility. The districts' approximate 40% share (combined) is based upon an allocation of the Cater treatment capacity and is projected to result in $1.3 million of revenue in fiscal year 2005.



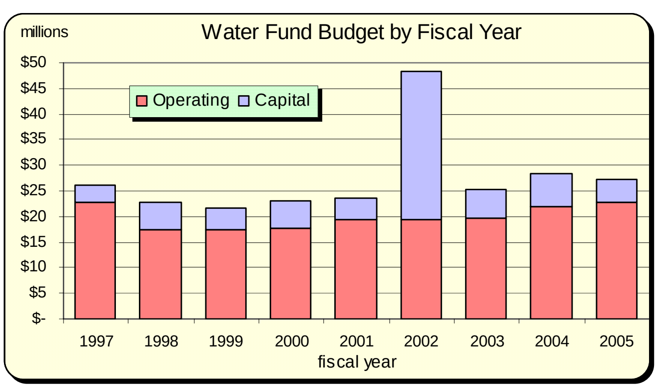
Enterprise Funds

With 91% of Water Fund revenue generated by metered water sales, the most important component of the revenue projection is the water sales estimate in acre-feet. As the chart to the right indicates, water sales have been essentially flat since 1999. In fact, since the most recent peak in fiscal year 2000, each year has reflected a year over year decline. Metered sales revenue for the adopted 2005 budget is based upon an estimate of 14,000 acre-feet, or five hundred acre-feet less than the budgeted estimate for fiscal year 2004. Because a large portion of the Water Fund's costs are fixed, declining or stagnant sales levels can have a significant impact on the overall financial health of the fund. City staff believes the fiscal year 2005 estimate is reasonably conservative. However, even if actual production and sales fall somewhat below the budgeted target, the Water Fund expenditure budget will be controlled to ensure that a balance is maintained.



The operating budget has been growing since fiscal year 2002 as a result of increasing costs for water purchases, energy and treatment supplies. Over that time the operating budget has grown just over $5 million (29%). The increasing trend in operating costs combined with significant capital needs and stagnant sales has led to the rate increase.

The adopted capital program is approximately $4.6 million. This is a $1.9 million (29%) decrease from the current fiscal year. Budgeted at $2.5 million, more than half of the capital program is for improvements to the City's groundwater facilities, including rehabilitation of the Ortega Groundwater Treatment Facility. Also included is almost $600,000 for pump station rehabilitation, including an upgrade to the Campanil pump station.



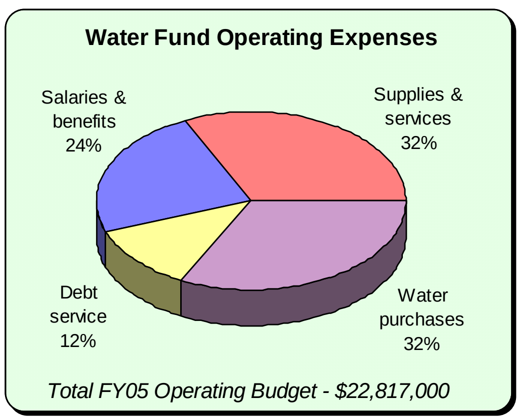
The chart on the left presents a ten-year history of the adopted Water Fund operating and capital budgets. The most noteworthy element of the entire ten-year period is the size of the fiscal year 2002 capital budget. At $29.1 million, it exceeded the total of the previous seven years' capital budgets combined. This is still relevant because the two major projects contained in that capital budget will continue to have significant workload impacts during fiscal year 2005. The Sheffield Reservoir Project ($22 million) will replace the existing open

Enterprise Funds

reservoir with underground reservoir tanks. The Cater Strategic Plan Implementation Project ($19.5 million) will renovate a number of major components at the Cater Treatment Plant, protecting the City's investment in that facility and enabling the plant to continue to meet more stringent water quality standards. Both projects are being funded with very low interest loans from the State Department of Water Resources. The cost of the Cater project is being shared with the Montecito and Carpinteria water districts. Under the joint powers agreement discussed above, the two water districts are responsible for their pro-rata share of the project. Each district will pay its share of the debt service on the 20-year low interest state loan.

The adopted operating budget is $22.8 million, an increase of approximately $900,000 (4%) over the adopted 2004 budget. As always, the largest individual cost item in the operating budget is water purchases (32%). Water is purchased from both the federal Cachuma Project ($3.2 million) and the State Water Project ($4.2 million).

As the chart below indicates, fixed costs, including water purchases and debt service, comprise 44% of Water Fund operating expenses. Because of the magnitude of these fixed costs, unlike most other City funds, salaries and benefits comprise only 24% of the Water Fund budget. Of the $7.3 million of supplies and services, $860,000 is for electricity, approximately $1.1 million is for facilities maintenance, $600,000 is for treatment chemicals, and an additional $1.5 million is paid to the General Fund for overhead allocation. Other significant items include over $443,000 for vehicle and equipment rents, and maintenance and fuel (paid to the City's Motorpool program) and $227,000 for insurance. These items combined amount to just over $4.7 million or 64% of the supplies and services budget.



The Water Fund has five outstanding debt obligations. As of June 30, 2003, the combined principal outstanding on these five debt issues totaled approximately $30.1 million. The debt issues include a 1994 revenue bond ($6.7 million), a 2002 Refunding Certificate of Participation ($15 million) and three loans from the State ($8.5 million). This does not include approximately $34.1 million in new debt for the additional state loans referenced above for the Cater and Sheffield projects. As of the end of fiscal year 2003, only $5.1 million of the total $19.2 million for the Cater loan had been drawn; and, to date, no amounts have been drawn on the $20 million Sheffield loan.

In summary, while the Water Fund continues to maintain a solid financial position, increasing operating costs and significant near term capital needs have resulted in an adopted rate increase for fiscal year 2005. The operational focus during the next fiscal year will be on completing the significant capital program, including the Cater and Sheffield projects.

Enterprise Funds

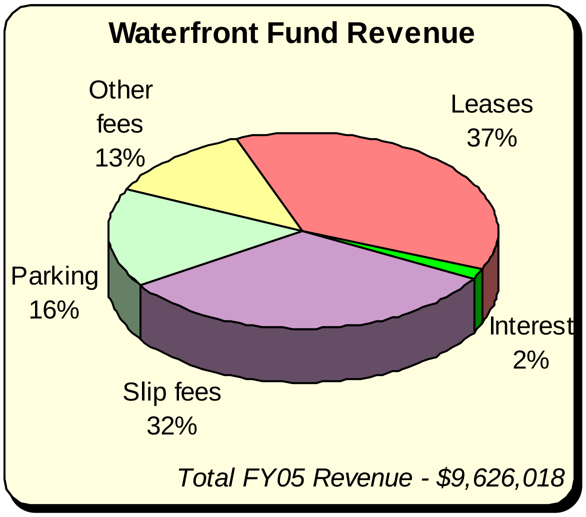
WATERFRONT FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 9,011,940	$ 9,301,230	$ 9,301,230	$ 9,615,930	$ 9,626,018
Operating expenses	7,409,286	8,836,345	8,834,345	8,812,352	9,129,106
Operating surplus	1,602,654	464,885	466,885	803,578	496,912
Capital budget	1,135,102	1,935,000	1,935,000	1,935,000	1,215,000
Net addition to (use of) reserves	$ 467,552	$(1,470,115)	$(1,468,115)	$(1,131,422)	$ (718,088)

The adopted Waterfront Fund budget for fiscal year 2005 contains sufficient operating revenue to fund all operating expenses and $496,912 of a $1.2 million capital program. The balance of the capital program ($718,088) will be funded from reserves.

The adopted $1.2 million capital program includes annual capital maintenance of Stearns Wharf ($300,000) and the Marina ($250,000). Also included is funding for breakwater repairs ($370,000).

As the chart below indicates, Waterfront revenues fall into three main categories. Leases of waterfront property provide approximately $3.6 million or 37% of total revenue. Most of the Waterfront leases are long-term agreements on a “percent of gross basis” under which the Waterfront receives a minimum base rent, or up to 11% of the tenant’s gross receipts, whichever is greater. The specific percent of gross receipts paid by the tenant varies from lease to lease. The Waterfront has a lease audit program to ensure that the City is receiving the percentage rent to which it is entitled. The Waterfront has realized substantial additional revenues as a result of this lease audit program. Because virtually all of the significant leases are long-term in nature, the Waterfront has little control over lease revenue in the short run.



The second category of Waterfront revenue is from parking. Parking in nine waterfront lots plus Stearns Wharf generates approximately $1.6 million, or 16% of total revenue. In addition, annual parking permits generate approximately $255,000. The adopted budget contains no increase in waterfront parking rates.

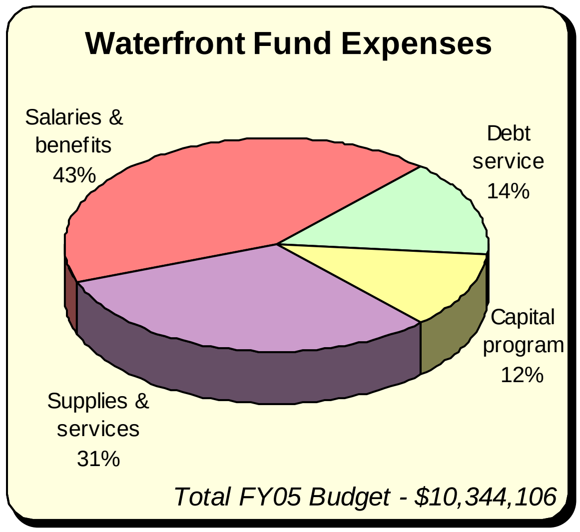
The third significant category of revenue is harbor fees, including slip fees. Slip fees are estimated to generate just over $3.1 million (32%) of total revenue in fiscal year 2005. Other fees include visitor fees ($370,000), slip transfer fees

Enterprise Funds

($390,000) and live-aboard fees ($190,000). The adopted budget includes increases in both the live-aboard fee (from $100 to $140 per month) and the slip transfer fee (from $100 to $125 per foot). The slip transfer and live-aboard fee increases are projected to generate an additional $54,400 and $45,000, respectively. The adopted budget contains no in slip fees.

Because the lease revenues are generally fixed in the short-term, the only revenue sources over which management can exercise near-term control are the parking and harbor-related fees.

The chart to the right displays the Waterfront Fund's expenses by category for fiscal 2005. The capital program (12%) and debt service (14%) combined represent 26% of the total budget.



The Waterfront Fund currently has two outstanding debt obligations. As of June 30, 2003, the total principal due on these two obligations totaled $20.5 million. The 2002 Refunding Waterfront Certificates of Participation ($19.4 million) represent a refinancing of debt originally issued in 1984 to fund repairs and capital improvements to Stearns Wharf and the harbor. The other obligation is a loan from the City General Fund ($1.8 million), the proceeds of which were used in the 1980s to make major repairs to Stearns Wharf. The Waterfront Fund is repaying the General Fund, without interest, at the rate of $100,000 per year. The loan will be fully repaid in 18 years. Although not yet executed, an additional $1.7 million General Fund loan has already been authorized to help pay for the Chandlery Remodel/Administrative Offices project.

Total operating expenses in the adopted budget are approximately $300,000 (3%) more than in the adopted fiscal year 2004 budget. The majority of the increase is in the salary and benefit category as a result of higher retirement costs.

In summary, the Waterfront Fund remains strong operationally with revenues exceeding operating expenses. Although it continues to be necessary to spend a portion of the fund's accumulated reserves for capital, including a portion of the Harbor Preservation Fund, the Waterfront Fund remains in solid financial condition.

Internal Service Funds

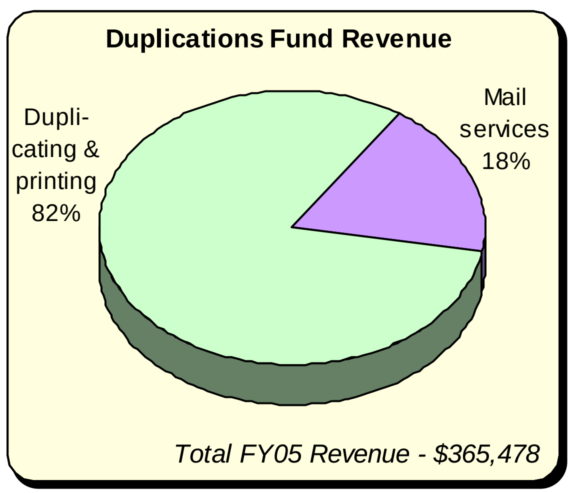
DUPLICATIONS FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 341,175	$ 375,978	$ 375,978	$ 330,978	$ 365,478
Operating expenses	315,433	399,191	399,226	397,838	365,478
Net addition to (use of) reserves	$ 25,742	$ (23,213)	$ (23,248)	$ (66,860)	$ -

The adopted fiscal year 2005 Duplications Fund budget is balanced at $365,478.

As an internal service fund (and part of the Finance Department), the fund's revenue is comprised of charges for services rendered to other City funds and departments. The revenues are derived from printing and copying (82%) as well as interoffice and external mail services (18%). The Duplications staff also processes and mails over 30,000 utility and accounts receivable billings monthly.

The entire budget is comprised of personnel costs (53%) and supplies and services (47%). The adopted budget is approximately $50,000 (16%) above the actual fiscal year 2003 expenditures. The increase is almost evenly split between salary and benefit costs and supplies and services. The salary and benefit increase is primarily due to the increase in retirement costs. The supplies and services increase is the result of higher allocated charges from the General Fund.



For the last several years the Duplications Fund has enjoyed a small operating surplus. This followed a number of years of small operating losses. While the use of reserves during that period was relatively small, staff was committed to making changes to improve the situation. Since that time, staff reduced some costs and implemented some nominal revenue enhancements. As a result of these changes and some significant billable projects the fund's situation has stabilized over the last two years.

The General Fund has provided an operating subsidy in each of the last several years. The adopted fiscal year 2005 budget continues this General Fund operating subsidy ($65,000). The intent of the subsidy, in part, is to allow the fund to accumulate enough resources to fund the replacement of required capital equipment.

Internal Service Funds

Sustaining a balanced budget will continue to be a challenge. Essentially, the Duplications Fund is, at best, a break-even operation. In the long run, the fund is unlikely to generate sufficient surplus to provide for capital replacement; thus, the rationale for the General Fund operating subsidy discussed above.

While virtually all of the services provided by the Duplications Fund can be obtained from the private sector, staff believes that, for the present, there is a significant value to having this capability in-house. In addition to cost considerations, issues such as timeliness, responsiveness and confidentiality are important factors.

Internal Service Funds

INFORMATION SYSTEMS FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ -	$ 1,909,387	$ 1,909,387	$ 1,909,387	$ 2,271,082
Operating expenses	-	1,909,387	1,940,779	1,665,583	1,949,062
Operating surplus	-	-	(31,392)	243,804	322,020
Capital budget	-	-	-	-	322,020
Net addition to (use of) reserves	$ -	$ -	$ (31,392)	$ 243,804	$ -

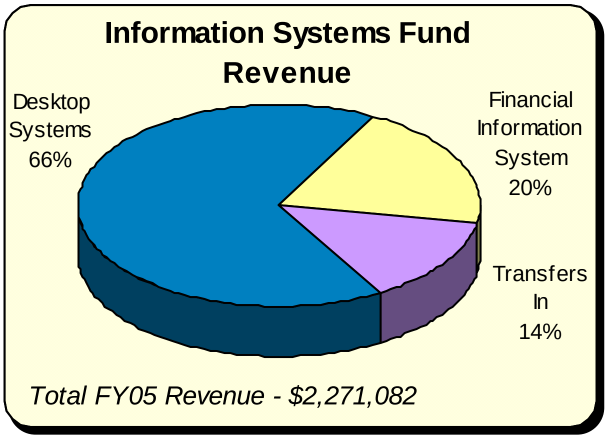
Information Systems was first established as an internal service fund in fiscal year 2004. Prior to that time, it was part of the General Fund. The adopted fiscal year 2005 budget is balanced at $2.3 million, including a capital program of $322,020. As an internal service fund, all of the revenue is from allocated charges to other City funds and departments.

Information Systems is comprised of two programs. The Desktop Information Systems program provides technical leadership, maintenance and user training and support for the City's 11 local area networks and over 630 desktop computers. The Financial Information Systems program provides programming, support and training for the City's 17 applications comprising the City's custom-developed financial management system.

The Desktop Systems program budget is approximately $1.5 million (66%) and the Financial Information Systems program budget is approximately 450,000 (20%). The balance of the fund's revenue is from a $315,000 transfer in from various other City funds to fund the Information Systems capital program.

The capital program includes funds for the implementation of a wireless technology foundation ($204,020) that will allow use of applications such as remote training at various fire stations as well as remote access to city data by field personnel. Also in the capital program is funding to begin implementation of an online payment system to allow City customers to make electronic Internet payments.

Overall, the Information Systems Fund generates sufficient revenue to fund all operating expenses and a modest capital program.



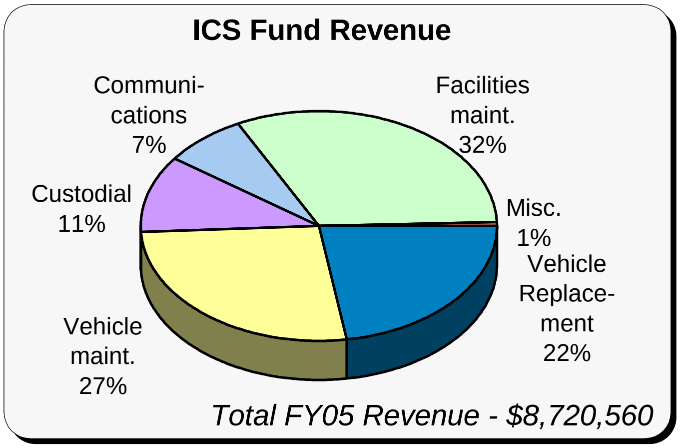
Internal Service Funds

INTRA-CITY SERVICE FUND

	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 7,482,805	$ 8,209,436	$ 8,309,436	$ 8,377,505	$ 8,720,560
Operating expenses	5,439,328	7,015,366	7,749,384	7,463,590	6,871,945
Operating surplus	2,043,477	1,194,070	560,052	913,915	1,848,615
Capital budget	1,725,912	1,733,479	1,854,496	1,800,000	1,989,415
Net addition to (use of) reserves	$ 317,565	$ (539,409)	$(1,294,444)	$ (886,085)	$ (140,800)

Fiscal Year

Part of the City's Public Works Department, the Intra-City Service (ICS) Fund is an internal service fund providing services to other City funds and departments. Revenue in the adopted fiscal year 2005 budget is sufficient to fund all operations and all but $140,800 of $2 million capital program. Beginning in fiscal year 2004, two operational areas that were previously part of the City's General Fund were moved into the ICS Fund. These two areas, Custodial Services and Communications Systems, were added to the Motor Pool and Facilities Maintenance functions that are already budgeted in the ICS Fund. Like the Motor Pool and Building Maintenance functions, both the Custodial Services and Communications Systems operations provide services exclusively to other City departments. Including these two operations in the ICS Fund ensures that the costs of providing the related services are properly borne by the other City operations benefiting from the services.



The Facilities Maintenance function provides on-call response for repairs and maintenance of facilities throughout the City, as well as managing the General Fund's annual planned maintenance program. The facilities maintenance program also provides management of small and medium-sized improvements to various City facilities. The Motor Pool program provides vehicle and equipment maintenance as well as managing the City's vehicle replacement program. The Communications Systems function provides management and maintenance of the City's radio, telephone and related communications systems. Custodial Services function provides custodial services to various City facilities.

Virtually the entire $2 million capital program is for the citywide vehicle replacement program ($1.95 million). The balance of the capital program ($50,000) is minor office and computer upgrades for the Building Maintenance operation.

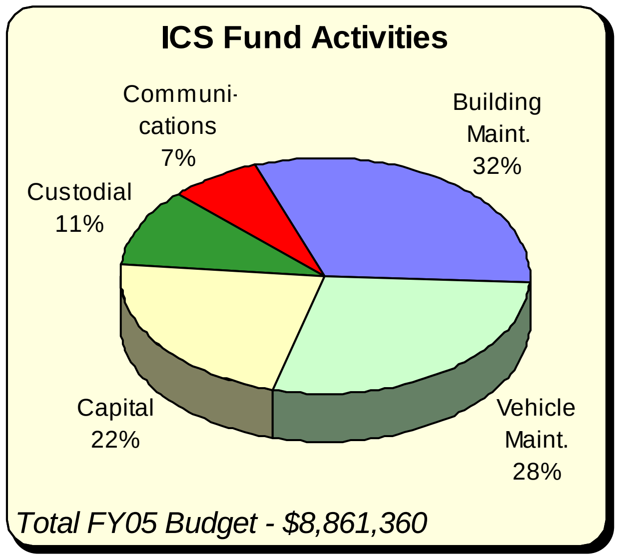
The chart on the previous page displays the various ICS Fund revenues for fiscal year 2005. Even with the addition of the Custodial Services and Communications Systems operations, the majority of the revenue is still generated from the Motor Pool and Facility Maintenance operations.

The building maintenance function operates on a work order system. Each job is tracked and billed to the customer department. Facilities maintenance staff handles repairs and call-out response. The planned maintenance program is handled almost exclusively by contract.

The Motor Pool charges an annual rental for each City vehicle in service. These rental payments are accumulated in a separate capital fund and used to replace vehicles in accordance with the City's vehicle replacement schedule. Each vehicle is also charged an annual maintenance fee, which covers all required maintenance and all repairs as needed. Since the maintenance charge is a flat annual fee, the ICS Fund can end up spending more on maintenance and repairs for individual vehicles than is recovered through the maintenance charge. On the whole however, sufficient funds are raised to keep the City's vehicles and equipment operating.

The chart on the right displays the ICS Fund expenses by program.

Overall, the ICS Fund continues to generate sufficient revenue to fund all operating expenses and a substantial vehicle replacement program.



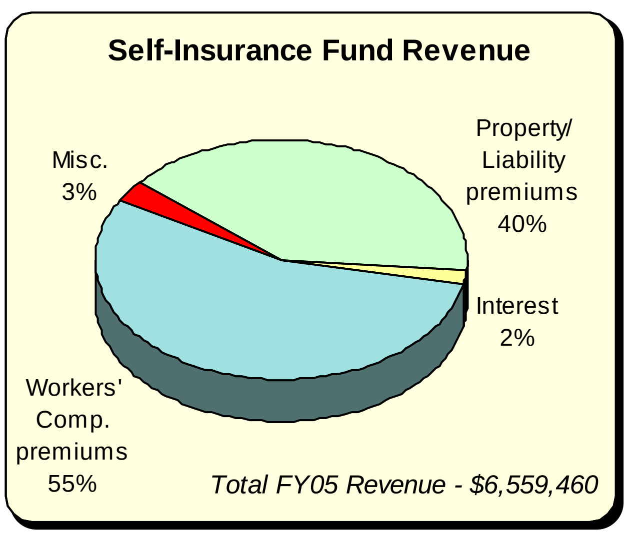
Internal Service Funds

SELF-INSURANCE FUND

	Fiscal Year				
	2003 Actual	2004 Adopted Budget	2004 Amended Budget	2004 Projected Actual	2005 Adopted Budget
Revenue	$ 6,213,695	$ 6,349,792	$ 6,349,792	$ 6,349,792	$ 6,559,460
Operating expenses	8,792,344	6,349,792	6,384,088	6,150,000	6,559,460
Net addition to (use of) reserves	$(2,578,649)	$ -	$ (34,296)	$ 199,792	$ -

The City is partially self-insured for both workers' compensation and liability. The City's self-insured retention (deductible) for workers' compensation is $750,000 per occurrence. A commercial excess workers' compensation policy provides additional coverage above the City's self-insured retention. For liability, the City is a member of the Authority of California Cities Excess Liability (ACCEL), a joint powers authority created to pool common municipal liability exposures such as general, automobile and public officials errors and omissions liability. There are currently a total of 11 California cities in ACCEL. Member entities share the cost of losses over an individual self-insured retention, and the City's self-insured retention is $1 million per occurrence. Shared losses are capped at $22 million. Because ACCEL is effectively a mutual insurance company, if the premiums the City pays are not needed to pay claims, they are returned to the City with interest, instead of becoming insurance company profits. Since the City has been in ACCEL, over $6 million in premium rebates have been returned to the City. This is an excellent indication that, to date, ACCEL has been a major success.

Insurable property is covered for all risks by commercial policies with a pooled aggregate limit of $750 million. Deductibles vary depending on peril and apply on a per occurrence basis. The City has separate limits of $50 million per occurrence for both flood and earthquake. The City's property insurance is purchased through a consortium of over 4,000 public entities that pool their purchasing power in order to better manage costs. The City currently has declared insured property values totaling $236 million.



The Self Insurance Fund acts as the City's own insurance company. As displayed in the chart on the right, the $6.6 million of total revenue contained in the adopted fiscal year 2005 budget is divided between workers' compensation premiums (55%), property and liability premiums (40%), and interest income

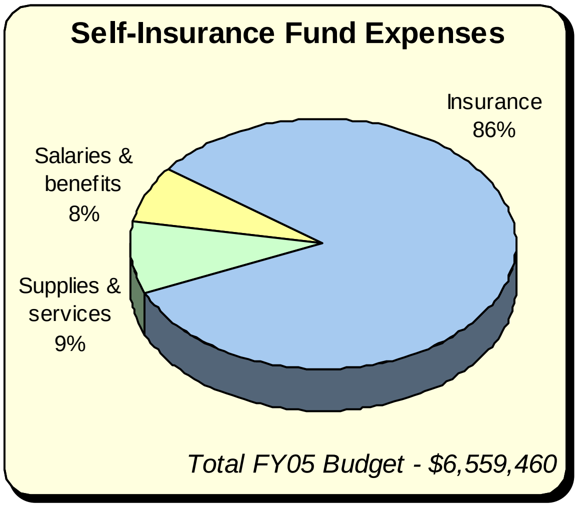
Internal Service Funds

(2%). As an internal service fund, the fund's revenue comes entirely from "premiums" charged to the City's other funds and departments for the coverage provided.

Like many entities, both public and private, the City has experienced dramatic increases in the cost for all lines of insurance over the last several years. In particular, both workers' compensation and property insurance costs have grown rapidly. As the table below indicates, as recently as fiscal year 2001, the total Self Insurance Fund "premiums" paid by the other City funds and departments totaled approximately $2.9 million. This has grown to $6.2 million in the adopted fiscal year 2005 budget. This is an increase of almost $3.4 million, or 118%, in just the last four years. This represents over $3 million that has been diverted from the actual programs and services provided by the City's departments to pay for increased insurance costs. And the premium increase only tells half the story. Over the same period, the City has had to accept significantly higher deductibles or premium increases would have been much larger. In the last four years, the City's deductible for workers' compensation has increased from $300,000 to $750,000 per occurrence and the property insurance deductible has increased from $100,000 to $2 million.

	Fiscal Year		FY 2005 Increase Over FY 2001	
	2001 Actual	2005 Recommended	Dollars	Percent
Workers' Compensation	$ 1,724,316	$ 3,599,460	$ 1,875,144	109%
Property / Liability	1,136,795	2,650,000	$ 1,513,205	133%
Total premiums	$ 2,861,111	$ 6,249,460	$ 3,388,349	118%

Every two years, in conjunction with the budget development process, the City contracts for an actuarial study on its self-insurance programs. The actuarial study recommends both how much the City should have in its self-insurance reserves and how much the City should budget for claims expense for each of the next two years. The actuarial study is based upon a combination of the City's specific loss history and certain industry standards. It has been the City's experience over the years that the actuarial study, because of its conservative assumptions, generally over-estimates the amount needed by the City for annual claims expense. This is due to the generally conservative nature of the study and the fact that the City's loss experience continues to be better than public agency industry standards. Based upon this experience, the City has traditionally set the premiums charged to the City's various funds significantly lower than the actuarial study recommends. Despite an increase in the cost of workers' compensation claims over the last several years,



Internal Service Funds

this is once again true with the most recent actuarial study and the adopted fiscal year 2005 budget.

The chart on the preceding page displays the Self-Insurance Fund's expense budget by category. Insurance costs represent a full 86% of the budget. Insurance costs include premiums paid for commercial insurance (property insurance, for example), as well as the claims budget for the City's self-insured exposures such as liability and workers' compensation.

In addition to managing the City's insurance portfolio, staff from the Self-Insurance Fund also provides occupational safety services to the City's various departments. This includes a significant training program, as well as accident investigation and working with departments to minimize the City's exposure to liability. The fact that the City's claims experience consistently runs below the actuarial projections is a testament to the effectiveness of the City's risk management program.

In summary, the costs of insurance have risen dramatically in the last several years and staff does not anticipate any significant change in this trend in the immediate future. At best, a stabilization of the premium increases can be expected.

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