



INTRODUCTION

City Administrator's Budget Message

OVERVIEW

Key Indicators Showing Local Economy is Getting Back on Track

After a difficult national recession and amid a continuing State budget crisis, the economic recovery that began last year appears to be holding steady. This is reflected in several key indicators of local economic health, many of which are tied to tourist and visitor counts.



One of the most favorable trends is the steady increase in airport passenger counts over the last two years. In fiscal year 2002, passenger counts fell to just under 700,000 from 781,000 due to the events of September 11, 2001. In fiscal year 2004, passenger counts reached 796,000, finally exceeding pre-September 11 levels. In May 2005, passenger counts were 9.9% above the same month last year, well above the national average of 4.7%. For fiscal year 2005, passenger counts are up 8.3% through

May 2005, representing strong overall growth in passenger volumes.

Another good measure of local economic health is the level of activity at local hotels. After a 3% decline in fiscal year 2002, transient occupancy tax (TOT) revenues remained flat in fiscal year 2003, but rebounded for a 5.1% increase in fiscal year 2004. Through May 2005, TOT revenues have grown 5.7%. 4.5% and 5% growth rates are projected for fiscal years 2006 and 2007, respectively.

And finally, we look to our sales tax revenues as a key indicator of local spending, which is heavily influenced by the number of visitors and tourists coming to the City. After several years of stellar performances, sales tax revenues declined 2.6% in fiscal year 2002, the first decline in approximately 10 years. Since then, sales tax revenues grew by 1% in fiscal year 2003 and 4.1% in fiscal year 2004. Through March 31, 2005, nine months into the fiscal year, sales tax revenues have increased 2.8%.

Proposition 1A Provides Measure of Relief

In connection with the State budget, the Governor and a coalition of local government officials reached an historic agreement, which led to placement of Proposition 1A on the November 2004 ballot. The measure, overwhelmingly approved by the voters, provides enhanced Constitutional protection to local government revenues, preventing the State from taking local



INTRODUCTION

City Administrator's Budget Message

government revenues in the future. The State would still be able to *borrow* property taxes from local governments, but only if: (1) the Governor proclaims a "significant State fiscal hardship," (2) the Legislature approves the borrowing with a 2/3 vote, and (3) the State repays any outstanding loans from local government, with interest.

In return for this protection of local revenues, the budget agreement calls for cities, counties, special districts, and redevelopment agencies to endure two years of revenues losses. Specifically, \$1.3 billion in local property tax revenues will be shifted to the State in the current fiscal year and next fiscal year (fiscal years 2005 and 2006). Statewide, cities will share in a \$350 million loss. The City of Santa Barbara's annual share of this shift is approximately \$1.25 million, and our Redevelopment Agency will lose approximately \$1.3 million. The adopted budget for fiscal year 2006 has been adjusted for these losses.



Despite this historic agreement, the \$105 billion fiscal year 2005 State budget continues to rely heavily on borrowing and does not resolve the State's continuing structural deficit. Although Proposition 1A provides significant protection against future raids on local revenues, it does not provide absolute protection. The State may find other ways to address their deficits that have an impact on local government.

Controlling Cost Still a Major Challenge

Over the last few years, the single biggest challenge facing most California cities has been the impacts of increased costs of health insurance, property and liability insurance, workers' compensation, and retirement. The most dramatic increase has been increased contributions to the Public Employee Retirement System (PERS). In large part due to the stock market losses from 2001 through 2003, required contributions for the General Fund increased by \$6.7 million from fiscal year 2003 to 2005. Another \$1.5 million increase is projected in fiscal year 2006.

In the General Fund, where salaries and benefits make up approximately 75% of total operating costs, recently negotiated and approved salary and benefit increases have added stress to the overall balancing of the fund. Although the City Council has expressed the importance of keeping salaries in line with the local market to ensure the City can attract and retain quality personnel, particularly in light of the extraordinary housing prices in the tri-County area, the challenge is finding a way to fund these additional costs when the General Fund is still facing budget deficits.



INTRODUCTION

City Administrator's Budget Message

Additional Reserves Needed to Balance General Fund Budget

Over the last three years, the City has budgeted for the use of reserves to balance the General Fund operating budget. This long-term strategy was developed to address the operating budget deficits created by the impacts of "9-11", the increases in costs, and the State's raid on local revenues. In addition to the use of reserves, the strategy included cuts to departmental budgets and adjustments to fees to keep pace with the cost of providing services. The goal was to minimize the impacts on the organization as it transitions to a smaller organization, and to resolve the structural imbalance by fiscal year 2009.

Although the use of reserves through fiscal year 2009 was contemplated when the strategy was developed several years ago, recently completed labor negotiations have increased the structural deficit and projected use of reserves beyond the amounts anticipated. As a result, City General Fund departments will be asked immediately in fiscal year 2006 to reduce operating expenditures by \$1 million. We will also immediately begin planning for additional adjustments totaling \$1.3 million for fiscal year 2007, for a total of \$2.3 million annually. It is critical we implement these additional changes to the General Fund in order to minimize the long-term use of General Fund reserves.

Forecast Shows General Fund Balanced by Fiscal Year 2009

In the development of the budget each year, staff updates the General Fund multi-year forecast, a financial planning document that plays a vital role in budgetary decisions. The forecast undergoes ongoing review by the Finance Committee and Council, and is updated several times throughout the budget development process.

The table on the following page is a summary version of the most current General Fund multi-year forecast. The forecast includes the expected results for fiscal year 2005 (current year); the adopted and proposed budgets for fiscal years 2006 and 2007; and projections for fiscal years 2008 and 2009.



INTRODUCTION

City Administrator's Budget Message

CITY OF SANTA BARBARA General Fund Multi-Year Forecast					
	Two-Year Financial Plan				
	FY 2005 Expected	FY 2006 Adopted	FY 2007 Proposed	FY 2008 Projected	FY 2009 Projected
Operating Revenues	\$ 84,438,876	\$ 88,510,646	\$ 93,587,465	\$97,121,623	\$100,937,869
Operating Expenses	<u>87,547,417</u>	<u>95,754,589</u>	<u>98,648,031</u>	<u>102,145,470</u>	<u>105,653,619</u>
Operating Gain (Loss)	(3,108,541)	(7,243,943)	(5,060,566)	(5,023,847)	(4,715,750)
Anticipated Year-End Variance	<u>2,626,423</u>	<u>2,872,638</u>	<u>2,959,441</u>	<u>3,064,364</u>	<u>3,169,609</u>
Net Operating Gain (Loss)	(482,118)	(4,371,305)	(2,101,125)	(1,959,483)	(1,546,141)
Capital Program	<u>(1,177,400)</u>	<u>(623,700)</u>	<u>(977,000)</u>	<u>(750,000)</u>	<u>(750,000)</u>
Total Projected Use of Reserves	(1,659,518)	(4,995,005)	(3,078,125)	(2,709,483)	(2,296,141)
Required Budgetary Adjustments	-	1,000,000	1,300,000	-	-
Cumulative Budgetary Adjustments	<u>-</u>	<u>1,000,000</u>	<u>2,300,000</u>	<u>2,300,000</u>	<u>2,300,000</u>
Adjusted Use of Reserves	<u>\$ (1,659,518)</u>	<u>\$ (3,995,005)</u>	<u>\$ (778,125)</u>	<u>\$ (409,483)</u>	<u>\$ 3,859</u>

As shown in the multi-year forecast above, operating revenues are insufficient to fund operating expenditures in each year of the forecast, resulting in operating deficits ranging from almost \$7.2 million in fiscal year 2006 to approximately \$4.7 million in fiscal year 2009. Because favorable year-end variances are typically realized each year, the forecast includes an "Anticipated Year-End Variance" amount, estimated at 3% of operating expenditures, in each year. Although unbudgeted, these anticipated year-end variances (i.e., revenues over budget and expenditures under budget) are important for financial planning purposes as they provide considerable relief, if realized, to the overall use of reserves. Thus, the "Net Operating Loss" for fiscal year 2006 drops to approximately \$4.4 million, and down to slightly over \$1.5 million by fiscal year 2009.

When capital program expenditures are included, however, the use of reserves increases each year by the estimated amount of the capital program. Therefore, the balance, shown as the "Total Projected Use of Reserves", represents total deficit of the General Fund. By fiscal year 2009, this total projected deficit decreases to approximately \$2.3 million, which is the amount established as the "structural deficit" that needs to be addressed.

Accordingly, the multi-year forecast identifies a total of \$2.3 million of adjustments (i.e., expenditure reductions or revenue enhancements) to be implemented in the next two fiscal



INTRODUCTION

City Administrator's Budget Message

years in order to bring the General Fund into balance by fiscal year 2009. It is anticipated that the majority of the adjustments will be in the form of expenditure reductions through the further downsizing of the City organization via attrition. Staff is committed to minimizing service delivery impacts whenever possible, but some service impacts are inevitable.

In accordance with Council-adopted policy, the General Fund should have 25% of its operating budget set aside in reserves: 10% designated to cover budgetary shortfalls, and 15% designated to respond to natural disasters. In addition, a fixed amount of \$1 million is designated as a capital reserve. The following table shows the reserves needed to fully fund General Fund reserves in accordance with City policy, and the projected reserve balances based on the multi-year forecast from fiscal year 2005 to 2009.

As shown in the table below, the first year that "policy reserves" are used is in fiscal year 2005, in the amount of \$655,822. Each year thereafter, the gap between the policy reserve balances and the actual reserve balances grows, reaching almost \$9.1 million in fiscal year 2009. However, with the structural deficit cured by this same year as forecasted, no additional reserves will be needed to balance the General Fund operating budget. Having "turned the corner", we expect, over time, to begin replenishing the reserves back to the policy levels over time.

**CITY OF SANTA BARBARA
Summary of Projected and Policy Reserves**

	<u>FY 2004</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>
Budget Reserve (10%)	\$ 8,754,742	\$ 9,575,459	\$ 9,814,803	\$ 10,099,547	\$ 10,405,983	\$ 10,767,323
Disaster Reserve (15%)	13,132,113	14,363,188	14,722,205	15,149,321	15,608,975	16,150,984
Capital	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Total Policy Reserves	22,886,855	24,938,647	25,537,008	26,248,868	27,014,958	27,918,307
Actual/Projected Reserves	25,942,343	24,282,825	20,150,155	19,234,366	18,824,883	18,828,741
Over (Under)	\$ 3,055,488	\$ (655,822)	\$ (5,386,853)	\$ (7,014,502)	\$ (8,190,075)	\$ (9,089,566)



INTRODUCTION

City Administrator's Budget Message

CITYWIDE GOALS AND PRIORITIES

Preserving the Quality of Life a Top Priority

We are fortunate to live in one of the most beautiful cities in the world. It is a city that boasts a breathtaking coastline, great beaches, and a mild climate, all within a picturesque setting



bordered by mountains to the north and the ocean to the south. It is a destination point for both domestic and international travelers, attracted by the exclusive shopping and dining, nearby wineries, cultural events and attractions, such as the Old Spanish Days and the Santa Barbara International Film Festival, and a relaxed beachfront atmosphere.

The preservation of this wonderful community has long been a priority of the City and its residents. The quality of life we enjoy encompasses the environment, the quality and safety of our neighborhoods, the economic vitality of the downtown and waterfront areas, and the cultural and recreational elements of the City.

City Continues Efforts to Improve the Environment

Some of the efforts aimed at improving the environment include restoration of local creeks that will help improve the overall quality of the waters flowing into local beaches. The concern over water quality led to the passage of Measure B in November of 2000, which increased the City's transient occupancy tax from 10% to 12%. Measure B has provided over \$2 million per year in revenues, supplemented by various federal and state grants, to address water quality issues.



Examples of such efforts include the restoration of Old Mission Creek and the Arroyo Burro estuary. The implementation of a watershed action plan is currently underway that will identify community priorities and long-term strategies for storm water and urban runoff reduction, and creek habitat and water quality capital improvement needs.

In terms of solid waste management, the City continues to implement strategies in order to reach its goal of diverting 70% of its solid waste from the local landfill. Some of the efforts aimed at reaching this goal have included introducing recycling bins in all City parks to convey the message that recycling is always a part of waste disposal - at home, at work, and at play. Trash cans in all City offices have also been replaced with a recycling/trash combo, with the trash container being significantly smaller than the recycling container.



INTRODUCTION

City Administrator's Budget Message

In this environmentally conscious community, waste diversion goes beyond basic recycling and green waste bins. The City has launched a public outreach program to give residents information on recycling, reuse, or proper disposal of commonly recycled items as well as non-traditional materials such as CD's, plastic bags, construction waste, electronic waste, hazardous wastes, appliances, and furniture. In an effort to reach out to all members of the community, the City has developed a Hispanic outreach program that features Spanish television commercials, recycling brochures in Spanish, and a bilingual newsletter that will premier on Earth Day.

On a larger scale, the City extended its contract to MarBorg Industries for waste disposal in order to help them finance a new state of the art recycling facility that will increase local waste diversion. The Public Work's Environmental Services Program is also completing a strategic plan that sets a road map for increasing diversion through food waste composting, diversion in schools, recycling of construction wastes, increased business and multi-family recycling, green building, and procurement of recycled products.

More Neighborhood Improvements Planned



Last year, the City implemented the Neighborhood Improvement Program in response to a growing awareness that the delivery of City services needed to be restructured to improve the safety and quality of life in our neighborhoods. The goals of the program include increasing the effectiveness and efficiency of services provided by City departments, creating more positive impacts in higher-density neighborhoods, engaging neighborhood residents and community groups to improve the quality of life in their neighborhoods, and increasing building and zoning enforcement efforts.

As a result of this program, a number of improvements and neighborhood clean-up efforts have been completed. For example, the City's Recreation Division Job Apprenticeship Program, with partial funding from Santa Barbara Beautiful, cleaned up a portion of Old Mission Creek. Youth apprentices worked all through August to clean up the site. Other efforts include:

- In September of 2004, City streets maintenance staff, along with the Police Department and Union Pacific Railroad, removed 18,000 pounds of trash from under the Las Positas Bridge at Highway 101. About 20 gallons of paint were used to cover graffiti on both sides of the underpass.



INTRODUCTION

City Administrator's Budget Message



- Renovation of the Community Gardens, including the Rancheria, Yanonali and Pilgrim Terrace Gardens, is scheduled for completion in June 2005. Garden plot borders have been installed at the three sites, storage sheds have been delivered and will be permanently located, irrigation systems are being repaired, and information kiosks have been ordered for installation.
- The City is eligible to receive up to \$473,500 from the State Street Workforce Incentive Grant Program for additional neighborhood improvement projects, including the Montecito Street Pedestrian Lighting Improvement Project; the Junipero Pedestrian Bridge Lighting Project; and Punta Gorda Street curbs, gutters, and sidewalks.
- On March 15, 2005, the City Council approved \$425,375 in funding from the Community Development Block Grant Program for five projects that are part of the Neighborhood Improvement Program. They include \$64,225 for Clean and Safe Neighborhoods; \$42,000 for the Franklin Center/Library; \$125,000 for the Coronel Pocket Park; \$85,000 for Ortega Park Improvements; and \$109,150 for Montecito Street Lighting.

Another major effort is the West Downtown Neighborhood Improvement Project, one of several projects funded by the Redevelopment Agency's 2003 Tax Allocation Bonds. Improvements will include upgrading pedestrian amenities, general landscaping improvements, and additional lighting where appropriate. Improvement of this area will strengthen the pedestrian connection between the west downtown and downtown.

Downtown and Waterfront Slated for Major Renovations

Maintaining the physical, cultural, and aesthetic features in the downtown and waterfront areas is critical to the economic vitality of the City. Over the last several years, the Redevelopment Agency (RDA) and business owners jointly funded the Downtown Sidewalk and Landscaping Project. The Project was broken up into phases, beginning with the 1000-1200 blocks, each carrying the same improvements further south on State Street. The goals of the Project are to improve pedestrian circulation and safety, improve business visibility, maintain and enhance landscape diversity, acknowledge significant architectural features of buildings, provide amenities for the comforts and





INTRODUCTION

City Administrator's Budget Message

convenience of pedestrians, and thereby provide a pedestrian friendly State Street Plaza. Phase IV of the Project, covering the 400-500 blocks, is scheduled to begin in January 2006.

While the majority of the development in the downtown has been focused on State Street over the last 30 years, Chapala Street is emerging as a focus of private redevelopment. Redevelopment Agency (RDA) staff, in collaboration with the Planning Division and Transportation Division of Public Works, recently completed a design guidelines process to develop a cohesive streetscape design theme to be used by both private developers and the City. The product of this process will be guidelines similar to the State Street Landscaping Guidelines, including text and renderings. The RDA has now funded \$835,000 for various improvements to Chapala Street in conformance with the Design Guidelines.



In the waterfront area, over \$5 million has been allocated towards sidewalk and other pedestrian improvements. The East Cabrillo Boulevard Sidewalk Improvement Project will repair and replace the existing sidewalk from Stearns Wharf to Milpas Street. The Project will also include landscaping enhancements where appropriate and the addition of pedestrian amenities. The West Side Pedestrian Improvements Project will provide sidewalk and landscaping improvements from Stearns Wharf to the Santa Barbara Harbor, and will

focus on improving the pedestrian connection between the wharf and harbor.

The Granada Garage, which is being built on Parking Lot No. 6 on Anacapa Street (between Anapamu and Victoria Streets), is now under construction. When completed, the Granada Garage will be a six-level parking structure with 575 parking spaces. The architecture of the garage is Mediterranean in style and the garage will feature new paseos and landscaping surrounding the structure. The garage will provide much needed parking in the Cultural District north of Carrillo, and help maintain the economic vitality of this important area.

Renovations to Cultural and Recreational Venues in the Works

A number of separate efforts are underway to develop or renovate major performing arts venues. One of the major efforts currently underway is the renovation of the historic Granada Theater. The Santa Barbara Center for the Performing Arts (SBCPA) has acquired the theater, with the goal of improving and expanding it to provide up to 1,600 seats. A major fundraising campaign is currently underway. The City's Redevelopment Agency will be providing a \$3 million grant towards construction, which is expected to begin in fiscal year 2006.



INTRODUCTION

City Administrator's Budget Message

The Ensemble Theater has also proposed a new theater in response to the Performing Arts Feasibility Study conducted by the Santa Barbara Center for Performing Arts and partially funded by the Redevelopment Agency (RDA). The RDA has allocated \$2.5 million in funding from the proceeds of the 2001 Tax Allocations Bonds for a potential grant or loan to Ensemble Theater for predevelopment or construction costs, as well as installation by the RDA of public paseos around the theater.

The Carrillo Recreation Center, located at the corner of Carrillo Boulevard and Anacapa Street, is scheduled for a \$3.5 million renovation next year. This heavily-used historic landmark will receive upgrades to its electrical and plumbing and aesthetic improvements.

Affordable Housing Receives Boost in Funding

For many years our City has made the provision of affordable housing a high priority. In partnership with the Santa Barbara Housing Authority and other non-profit housing developers, the City and Redevelopment Agency have provided funding for the development of many affordable units in the City. Currently, 12% of the City's housing stock is under restrictions to ensure its affordability.



The Redevelopment Agency (RDA) recently approved \$2.3 million in funding towards a project at 617 Garden Street for a Mental Health Association (MHA) administrative and program center, which will include 50 units of affordable housing. Twenty-five of the units would be for very-low-income MHA clients, and 25 for low-income, downtown workers. The RDA also recently allocated \$2 million for future affordable housing projects, and an additional \$4 million for property acquisition, some or all of which could be

used for acquiring property for housing.

In addition, the Redevelopment Agency provided approximately \$17 million in a combination of loans and grants toward the largest affordable housing development to be built on the South Coast. Mercy Housing California and St. Vincent's Institution are developing 75 low-income family apartments and 95 low-income senior apartments on the 19-acre St. Vincent's School campus at Highway 154 and Calle Real. The development is also financially supported by the County of Santa Barbara as a regional response to affordable housing needs.

City Focusing on Working Smarter

Over the last several years, the City has faced unprecedented financial challenges on many fronts, including the impacts of September 11, 2001, and the ensuing economic downturn on



INTRODUCTION

City Administrator's Budget Message

City revenues; the sharp rise in costs; and the raid on local revenues by the State. Because of these factors, the City has been forced to trim costs and reduce staffing through attrition.

Even with the staff reductions over the last several years, and the potential for further reductions over the next two years, the demand for City services has not diminished. Consequently, it has become more important than ever for the City to work more efficiently to ensure the quality services our residents and businesses currently enjoy are unaffected.

One of the initiatives designed to create a more efficient City government is the implementation of a performance measurement program two years ago, called the Paradise Performance Program (or "P³"). For each operating program, specific measurable objectives are created to better plan work efforts and identify results. Additionally, performance indicators have been developed for each program to measure both effectiveness and efficiency. Although still evolving, the P³ program has already made significant improvements in City operations.

One of the ongoing challenges affecting City operations is the high cost of living on the south coast, which has made it difficult to attract and retain quality staff. This will become even more acute as a large number of baby boomers reach retirement age in the next five years.

In response to this challenge, last year the City implemented a comprehensive training program for employees, called Learning for Excellence and Achievement Program ("LEAP"). Employees are provided training opportunities in a number of topics, ranging from employment law to improving communication skills. This is an important investment in our employees that will generate dividends on a long-term basis as we look to our own personnel to fill key management and supervisory positions.



Major Planning Efforts Underway

Next year staff will begin work to update the City's General Plan, which contains many important goals and policies for growth management and land use planning in our community. Measure E, which in 1989 amended the City's Charter that provides the basis for the City's Growth Management Strategies, has a 2010 expiration date. This effort will require considerable time and resources over the next 5 years. When complete, we will have the framework for land use decisions through 2030.



INTRODUCTION

City Administrator's Budget Message

Staff is currently working on Phase I of the General Plan Update (GPU). The primary objective of Phase I is to produce a series of background reports ("Conditions, Trends & Issues") for each of the key resource constraints to growth. These reports will serve as both the foundation for the community discussion and decision making in the next phases, as well as an educational tool.

Phase II, which will begin in early fiscal year 2006, will formally kick-off the public participation effort, the residential development analysis, as well as the environmental review. This process will develop and confirm the community's vision for future growth and development, as well as work through a set of specific growth scenarios, culminating in a single preferred growth option.

The focus of Phase III, scheduled to begin in fiscal year 2007, will be the development, analysis and community debate of the various growth options and their associated environmental impacts. In working towards a preferred growth option, formal environmental review will play a key role in framing the discussions and eventual decisions.

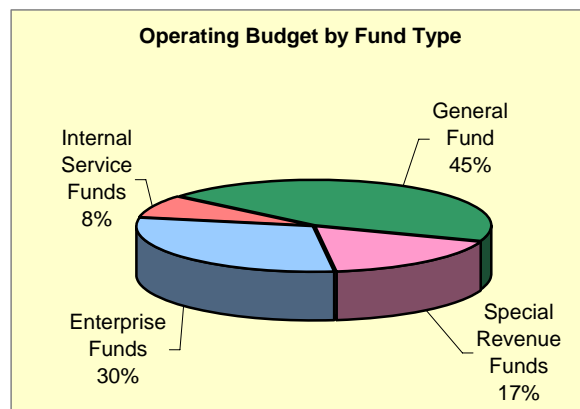
Phase IV will confirm the preferred option through a ballot measure, and will be followed by a series of General Plan Element and Zoning Ordinance implementation efforts.

BUDGET HIGHLIGHTS

City Continues to Provide Full Scope of Services

The City of Santa Barbara is a full service City providing a broad range of services, including police and fire protection, parks and recreation, library, planning, streets maintenance, water, wastewater and refuse, a regional airport, a harbor and waterfront.

The fiscal year 2006 adopted budget includes a total operating budget of approximately \$189.8 million and a citywide capital program of \$20.6 million. The General Fund, where services traditionally associated with local government are accounted for, includes a \$95.8 million operating budget and a \$623,700 capital program.





INTRODUCTION

City Administrator's Budget Message

In addition to the General Fund, the City has a number of other funds used to account for the many services and activities provided (see chart). Special revenue funds, totaling \$45.5 million (17%), are used to account for revenues legally restricted for a specific purpose. Internal service funds, totaling \$17.3 million (8%) are used to account for services provided internally to City departments and programs, such as Information Systems and Risk Management (i.e., Self-Insurance) services. Enterprise funds, totaling \$64.5 million (30%), are used to account for the activities of the City operated in a manner similar to the private sector.

The City's enterprise funds include the Water, Wastewater, Downtown Parking, Waterfront, Golf and Airport Funds. Each relies on a unique set of fees and charges to fund its operating and capital costs. As with the General Fund, they have been affected by the increased costs over the last several years in insurance and employee retirement costs. However, all of the enterprise funds are in good financial health and are balanced in fiscal years 2006 and 2007.

Key General Fund Revenues Reflect Moderate Growth

Key General Fund revenues are now posting increases consistent with historical growth averages. Between 1992 and 1995, the national, state and local economies suffered through an economic recession. City revenues at that time were flat and, in some cases declined. This period was then followed by one of the strongest periods of growth in recent history, which lasted through the last half of the decade and through 2000. Correspondingly, City tax revenues realized extraordinary growth, ranging from 6 to 9%. However, for the decade, total General Fund revenues realized an average growth of just 3.5%, and tax revenues (i.e., sales, property, transient occupancy, etc.) grew an average of just 4.3%.

These long-term growth averages give perspective and understanding to current growth trends of General Fund revenues and the projections for the next two years. The table below provides a summary of key General Fund revenues for fiscal year 2005 (estimated year-end projections), and budgeted estimates for fiscal years 2006 and 2007.

The largest growth has been, and continues to be, in property tax revenues. Between 1997 and 2004, property tax revenues grew an average of 9% per year. In the last three years, despite the impacts of the recession on other key revenues, property values appreciated considerably. For both fiscal year 2005 and 2006, as shown in the table, we estimate a 7% growth in property tax revenues; a 6% growth is projected for fiscal year 2007.



INTRODUCTION

City Administrator's Budget Message

CITY OF SANTA BARBARA Summary of Key General Fund Revenue Estimates

	<u>FY 2005 Projected</u>	<u>Est. Growth %</u>	<u>FY 2006 Estimate</u>	<u>Est. Growth %</u>	<u>FY 2007 Estimate</u>	<u>Est. Growth %</u>
Sales Tax *	\$ 18,629,754	3.0%	\$ 19,374,944	4.0%	\$20,149,942	4.0%
Property Tax *	11,981,583	7.0%	12,820,294	7.0%	13,589,512	6.0%
Transient Occupancy Tax	10,780,310	4.0%	11,504,200	6.7%	12,079,400	5.0%
Utility Users Tax	5,837,700	4.8%	6,071,200	4.0%	6,253,300	3.0%
Franchise Fees	2,074,964	1.0%	2,170,200	4.6%	2,275,100	4.8%
	<u>\$ 49,304,311</u>		<u>\$ 51,940,838</u>		<u>\$54,347,254</u>	

* Amounts do not include adjustments for recent change in allocation pursuant to State budget provisions:

- Sales tax does not include Prop. 172 1/2 cent sales tax.
- 25% of sales tax revenues replaced them with an equal amount of "property tax in-lieu".
- Replacement of approximately 90% of Vehicle License Fees with an equal amount of property taxes.
- State take away in both FY 2005 and 2006 of over \$1.2 million in property taxes ("ERAF shift").

As shown in the preceding table, sales tax, the largest General Fund revenue, is projected to grow 3% in fiscal year 2005, and 4% in fiscal years 2006 and 2007. Although the growth rates are consistent with historical averages, they are above the growth rates of the previous three years. The table to the right shows the actual growth rates for sales tax revenues since 1999 through 2004, and the estimates for fiscal years 2005 through 2007. The economic recovery of the late 1990's generated strong growth through fiscal year 2001. However, revenues *declined* in fiscal year 2002 by 4.1%, and grew less than 3% in fiscal years 2003 and 2004.

City of Santa Barbara Sales Tax Revenue Growth

<u>Fiscal Year</u>	<u>Actual Growth Rate</u>
1999	6.4%
2000	5.8%
2001	5.4%
2002	-4.1%
2003	2.2%
2004	2.8%
2005 (Est.)	3.0%
2006 (Est.)	4.0%
2007 (Est.)	4.0%

Our projected growth rate for fiscal years 2006 and 2007 of 4% essentially reflect an expectation that the economy will continue on this positive trend. This is consistent with economic indicators and general economic projections at both the state and national levels.

Through May 2005, transient occupancy tax revenues are 5.7% above last year, and are projected to continue at this rate through remainder of the fiscal year. A 6.7% increase is estimated for fiscal year 2006, which assumes a normal growth rate of 4.5% plus additional



INTRODUCTION

City Administrator's Budget Message

revenues due to the recent opening of the Andalucia Hotel. Based on recent trends, a 5% growth is estimated for fiscal year 2007.

As shown in the table below, growth in franchise fees has been fairly unstable over the last few years. This is due to a number of factors, including: (1) fluctuation in the prices of natural gas and electricity rate reductions; (2) overpayments of franchise fees on natural gas received in one year, adjusted in the subsequent year; a rebate to customers in fiscal year 2004 on electric charges; and a change in funding for public access and educational programming whereby the City received an additional 1.5% in franchise fees from the City's cable provider, offset by City contributions to the South Coast Community Media Access Center.

The table also shows the percentage change in franchise fee revenue from fiscal year 2002 through 2004, and the projections for fiscal years 2005 through 2007. Even with the volatility of the past few years, we are now seeing more stability. For fiscal year 2005, we expect revenues to grow just 1%. In fiscal years 2006 and 2007, the projected growth is 4.6% and 4.8%, respectively. The increases in fiscal year 2006 and 2007 are largely attributable to increases to cable franchise fees, from 4.5% to 5% approved by Council in May 2005. Although the effective date could be as early as end of July 2005, we have only factored in six months of additional revenues in fiscal year 2006, with the full impact of the fee increase reflected in fiscal year 2007 revenues.

City of Santa Barbara Franchise Fee Growth

<u>Fiscal Year</u>	<u>Amount</u>	<u>Actual Growth Rate</u>
2002	\$1,797,590	15.9%
2003	1,769,584	-1.6%
2004	2,055,864	16.2%
2005 (Est.)	2,074,964	1.0%
2006 (Est.)	2,170,200	4.6%
2007 (Est.)	2,275,100	4.8%

The City Council has also approved an increase in the electric franchise fee, from 1% to 2%. The fee increase could generate approximately \$600,000 of additional revenues, half of which will be restricted to fund undergrounding of electric power lines. The proposed increase has recently been approved by the Public Utilities Commission (PUC); however, the implementation date is still uncertain given the substantial effort required to effect this change. Therefore, no additional revenues have been included in this adopted two-year financial plan for the impacts of the increase in franchise fees.

Enterprise Funds Focusing on Major Capital Improvements

The Airport is moving forward with the expansion of the airline terminal. The growth in passenger volumes over the last ten years and the additional security needs have resulted in severe overcrowding and lack of space for airline and airport operations.

The Airline Terminal Improvement Project will be funded from a combination of federal grants, bond financing and airport revenues. A feasibility study determined that the Airport's financial



INTRODUCTION

City Administrator's Budget Message

capacity is \$55 million for the entire project, which includes the terminal expansion, roadway improvements, increased parking facilities, and an aircraft-parking ramp.

In February of 2005, Airport staff and the project management team initiated meetings with stakeholders. These "kick-off" meetings focused on the process of developing a Program Criteria Document (PCD), which will contain the key elements for design of a new Airline Terminal Complex. Over the next several months, additional meetings with a subcommittee of the stakeholders will be held to provide ongoing input to design elements. When complete, the PCD will set forth the project budget, the building size, all technical information on square footage, space for the various uses in the terminal, and parking gate layout. The PCD process enables the City Council, boards and commission members, and affected users to have their concerns and needs addressed prior to design. Completion of the PCD is expected for the fall of 2005.

The Golf Course is planning major capital improvements to address a number of safety issues and to improve the overall playability of the course. A Master Plan has been approved by the Golf Advisory Committee, the Parks and Recreation Commission, and City Council. The Master Plan will guide future capital improvement projects and will outline methods of improving the course in an orderly manner over the next few years.

The Downtown Parking Fund is currently evaluating alternative parking fee structures to fund an increase to its capital program for maintenance of the aging parking facilities. Although no additional parking structures are proposed, other than the Granada Garage, the aging facilities are demanding more maintenance efforts to ensure continued service to both shoppers and commuters.

In the Water Fund, major improvements to the William B. Cater Water Treatment Plant began two years ago and will continue over the next several years, at a total cost of approximately \$20 million. The plant, which was built in 1964, supplies water to the City of Santa Barbara, Montecito Water District and Carpinteria Valley Water District.



In the Wastewater Fund, a strategic plan for the rehabilitation of the El Estero Wastewater Treatment Plant was completed in January 2003. Nine projects costing \$18.5 million, identified as having the highest priority, began this fiscal year and will continue into the next two years. These projects will be funded through long-term debt issued in June 2004, which will be repaid over 25 years.



INTRODUCTION

City Administrator's Budget Message

The Sheffield Reservoir Project is nearing completion. The main elements of this project are the construction of two buried 6.5 million gallon capacity concrete reservoirs and conversion of the parcel to a passive open space. The existing open reservoir has been demolished, and construction of the new tanks has been completed, and the temporary above ground steel bolted tanks are being dismantled. The area around the water tanks is being backfilled for the planting of trees and plants this fall. In the last few months, work consisted of bringing the two buried tanks on line, beginning backfill and compacting operations, erecting the roof of the Filtration Building, and removal of the liner of the water main running under the Filtration Building and under Mountain Drive. The project is approximately 72% complete and is scheduled to be completed at the end of this calendar year.



CONCLUSION

Despite many difficult challenges ahead, the adopted two-year financial plan envisions a bright future for our community: improvements to protect our fragile environment, major enhancements to a multitude of facilities and our critical infrastructure, development of a new General Plan to guide future land use decisions, and the continued delivery of quality services to our residents. This truly is an exciting time to be a part of Santa Barbara City government.

Over the next two years we need to have the courage to address the financial issues our City faces. This issue is not complex and the budget shortfall we face is certainly less severe than other fiscal crises faced by Santa Barbara over the past 155 years. I am confident that our organization has the talent and the dedication to solve the problems we face and continue to move our City forward in a positive direction.

On behalf of the City staff, I would also like to express our appreciation to the City Council for your leadership and support as we implement the work envisioned in this budget. Our City is the type of community it is today because citizen leaders are willing to contribute their time and skills to make Santa Barbara special.

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