



City of Woodland

REPORT TO MAYOR AND CITY COUNCIL

AGENDA ITEM

TO: THE HONORABLE MAYOR
AND CITY COUNCIL

DATE: June 2, 2009

SUBJECT: Fiscal Year FY10 - FY19 Capital Improvement Program and FY10 –
FY 12 Capital Budget

Report in Brief

A capital improvement program (CIP) is a blueprint for planning a community's capital expenditures and is one of the most important responsibilities of local government officials. The purpose of a CIP is to provide a method through which the City can take a planned and programmed approach to utilizing its financial resources in the most responsive and efficient manner to meet its service and facility requirements. The City's CIP is a balanced ten-year spending plan which was developed through a joint effort with all City departments and is designed to be consistent with respective Master Plans, the Major Projects Financing Plan (MPFP), Measure E spending plan and other Council adopted plans. The proposed Capital Budget is the first three years of the CIP and identifies the projects for which three-year capital appropriations are requested.

Staff recommends that the City Council review the 10-year CIP, including capital projects, revenue assumptions and anticipated financing, and authorize expenditures for the three-year period beginning in FY09/10 and ending in FY11/12. Council's recommended changes, if any, will be brought back for final adoption on June 16, 2009.

Background

On December 11, 2007, City Council discussed the City Manager's Implementation of Policy, Leadership and Management Initiatives which included a commitment to creating a balanced and sustainable ten-year financial plan. Consistent with that commitment, Council adopted the City's first ten-year CIP on June 10, 2008 that included ten-year expenditures of over \$198 million, and appropriated \$78.3 million in the first three years.

The majority of the City's capital program is funded through a combination of development impact fees, Measure E and utility user fees. These revenue sources have been significantly impacted by the collapse of the housing market and subsequent financial crisis and economic recession. As a result, on January 20, 2009, Council acted to reduce the FY09-FY11 capital budget by \$20.3 million.

These reductions were necessary to account for (1) reduction in expected building permit activity; (2) reduction of the MPFP fees adopted by Council on December 16, 2008; and (3) implementation of a fee deferral program for development impact fees, effective January 1, 2009. Despite these significant reductions, economic conditions have continued to decline and revised development projections indicate that the funding situation for the capital program is even worse than anticipated in January.

In previous capital budgets, the City allocated resources based on a “pooled cash” approach, whereby project expenditures were covered by the pooled City-wide cash resources. Because the City implemented and expended money on various capital projects in advance of collecting the related development fees, several development fee funds reflect negative balances. These funds have internal loan repayment schedules that allocate future development fees collected from each respective fund back to the treasury over varying time periods. The more significant internal borrowing balances anticipated at June 30, 2009 is reflected below:

Sewer Development:	\$(10,288,731)
Police Development:	\$ (4,258,571)
Storm Drain Development:	\$ (1,052,403)
Road Development:	<u>\$ (4,378,978)</u>
Total	<u>\$(19,978,683)</u>

Given these large beginning deficits, substantial slowdown in development, and the magnitude of reduced development fee revenues, the City is not able to fund necessary projects without some level of continued pooled cash borrowing. However, staff is striving to minimize the use of pooled cash by aligning the commitment of funds with the receipt of the associated revenues; this goal is considered to the extent possible in the ten-year CIP.

In addition to internal borrowing between capital funds, the City issued a significant amount of debt between 2002 and 2007 to fund construction of the Community Senior Center and Sports Park, Fire Station 1 and expansion of the Wastewater Treatment Plant. Aggregate annual debt service payments for these bonds total \$5.39 million, of which \$4.1 million is required to be paid by development fees and the remaining \$1.2 million is an obligation of either Measure E or the sewer enterprise fund.

Even with relatively moderate development activity, meeting current debt service requirements will be challenging. Given the adopted reduction in development fees combined with the reduced level of development activity, the Park, Fire and Wastewater Development Funds will not generate sufficient revenue from residential development to meet minimum debt service requirements. Depending upon the level of non-residential development that may occur the City will likely need to rely, at least in the short-term, on pooled cash borrowing to make the annual payments. Staff is currently working with the City’s financial advisor to explore long-term options that may provide some relief from current debt service obligations; however, no final recommendations have been determined at this time.

In order to facilitate the City Council's review of the 10-year CIP, staff has developed a binder that includes detailed information regarding the entire capital program. Projects are summarized by fund source and the allocations from all funds are provided. Fund balance information on each categorical fund for the 10-year Plan period is also included. Finally, detailed information sheets are provided summarizing each project. These sheets are the basis for staff review of specific projects as they provide funding detail, operational costs and information that explain justification, service level and pertinent issues. The Council should note that presentation of the 10-year CIP in this manner is a "work in progress" and refinements are inevitable to improve the information. However, staff believes the 10-year CIP binder represents an improvement over the spread sheets with the small type that has been issued in the past.

Discussion

Revision of the CIP has been a time intensive and comprehensive effort involving all City departments. Staff has undertaken a thorough examination of all requested projects with regard to timing and availability of financial resources for both implementation/construction of the project as well as continued maintenance and operations. Achieving a balanced three year budget and 10- year Plan has been extremely difficult and has required delay of projects that are very important to the community and City staff. Staff will continue to evaluate the timing of projects and search for alternative funding sources during each update of the 10-year CIP.

The following assumptions were used in compiling the CIP:

Revenues

Development Fees: Based upon conversations with Spring Lake developers, the Departments of Finance and Community Development revised the development projections necessary to determine the amount of resources available for capital projects. These projections are conservative, take into consideration the significant slow-down in the housing market and related development. The 10-year Plan includes full build-out of the Spring Lake Specific Plan area and assumes some level of residential development in the Master Plan Remainder area during the last two years. Revenues have been calculated based on the development fees adopted December 16, 2008, and include an annual CPI escalation factor. Timing of residential development takes into consideration the fee deferral program that began on January 1, 2009. Given the constantly changing circumstances of both the economy and the active homebuilders, these projections will be revisited during each annual update of the CIP.

Enterprise Funds: The user fees for the Sewer Enterprise fund are based on the fees currently adopted by Council, adjusted annually by a CPI factor. The Water Enterprise fund assumptions include rate increases beginning in FY09/10. The City is currently in the process of completing a water rate study to allow for implementation of consumption based residential billing. This study will also include components of the Davis-Woodland Water Supply Project. In order to fund the projects submitted to the rate consultants and based on preliminary study results, staff has included estimated annual rate increases of 20% in FY10/11 through FY13/14, and 6% annually thereafter.

The Storm Drain Enterprise fund assumes the General Fund will continue to subsidize the difference between annual revenues and necessary operations through FY 10/11.

Bond Financing: Financing of capital projects through use of debt issuance (bonds) can be advantageous to the City and more appropriately spreads the cost of new improvements. One advantage of debt financing is that once the money is borrowed, there is a fixed repayment schedule that is spread over a number of years and repaid by dollars that are cumulatively deflating in value. Additionally and most importantly, capital improvements are generally long-term in nature. Bond financing spreads the cost of a facility over a period of time that more closely resembles its useful life. Those who require and will use the improvements being paid for with bonds will pay for the improvements as they use them over time rather than placing a significant expenditure burden on current customers.

Because of these reasons, bond proceeds have been included as one-time funding sources in both the Water and Sewer Enterprise funds. In FY09, Council approved issuance of up to \$18 million of water revenue bonds; however, because of turmoil in the financial market, the City was able to issue only \$9 million. Staff has assumed an additional \$9 million of bond proceeds will be received in FY10 to complete the original request of \$18 million. FY10 also includes \$11 million in debt financing from the Sewer Enterprise fund. Calculations by the City's financial advisor show that this financing would be well within both the bonding capacity of the Sewer fund and the current sewer rates approved by Council. These proceeds will be used to finance critical utility infrastructure that might otherwise be delayed. Should Council choose not to pursue these proposed financings, \$20 million of projects in the first year of the CIP will need to be cancelled and/or delayed. Additional financing has also been assumed related to the Davis-Woodland Water Supply Project, which is discussed in further detail within this report.

Grants: Awarded grant funds are included as one-time funding sources in the Capital Budget. In the event of possible defunding of grants by the State, the project will either be placed on hold or alternative funding sources will be identified.

Debt Service/Operating Appropriations

Consistent with previous years, annual debt service requirements have been programmed to receive the highest priority of available cash within the Capital Budget. Estimated debt service payments for the anticipated bond financings discussed above have been included in the 10-year Plan. Operating appropriations consistent with the ten-year plans for the major funds have been included in determining the amount of cash available for capital projects.

Capital Projects

Projects included in the CIP are consistent with the various Council adopted Master Plans, MPFP and Measure E spending plans. Each department prepared cost estimates for projects required by their respective programs, including phasing, timing and detailed project justifications and descriptions. The projects were reviewed by the City Manager, all senior staff members and various project proponents. The CIP assumes projects approved in the FY09 Capital Budget will fully spend approved appropriations and/or carry-over into future years.

Davis-Woodland Water Supply Project

The City Council has received a number of reports regarding the Davis-Woodland Water Supply Project including estimates of the City's share for funding the project which is nearly \$200 million. The magnitude of this project is such that funding strategies will need to be explored, including significant multiple debt financings and substantial adjustment to the current utility user fees. The CIP includes three years of requested appropriations totaling close to \$18 million, and the remainder of the project is currently unfunded pending further review. Staff has assumed financing will be pursued for these amounts and has included bond proceeds of \$16.9 million as well as the related annual debt service. As mentioned previously, staff has also assumed some level of utility user fee increases. Future development will also pay its fair share for this project; however, a development impact fee has yet to be calculated until additional information from the rate study is received. Therefore, development impact fee revenue has not been included for the project within the 10-year CIP. This information will be included in future updates.

Operating Budget Impacts

One of the many issues evaluated through the CIP process is the impact new projects may have on departmental operating budgets. These "hidden" costs can affect the ability to fully utilize the proposed facility and provide quality services. By addressing these costs at the outset of the process and including necessary enhancements in the operating budget, other important services will not be compromised in future years. Projects that were identified to have significant operating impacts that the City cannot currently afford were generally delayed and/or unfunded.

Unfunded Projects

As mentioned herein, the CIP attempts to maintain fund integrity and address future operating budget impacts. To meet these objectives, with particular focus on minimizing future General Fund burdens, certain projects have been moved "below the line" and are referred to as ZIP (Zero Impact Project) in the project detail sheets. These projects are not currently funded during the ten-year plan period pending further discussion, policy direction, or identification of alternative funding sources. These projects include some items funded in the Measure E Spending Plan. Scheduling these projects is problematic until the economic situation stabilizes and operating costs primarily supported by the General Fund can be identified. Given the high priorities associated with these projects, staff will need to develop alternatives for the City Council's consideration that will allow these projects to be moved up to a funded status in future annual CIP updates.

Fiscal Impact

If approved, the Capital Budget would appropriate approximately \$26.7 million in FY09/10, \$22.8 million in FY10/11 and \$28.7 million in FY11/12 for capital expenditures on projects identified in the attached schedules.

Public Contact

Posting of the City Council agenda.

Commission Recommendation

The ten-year CIP and Capital Budget were presented to the Planning Commission on May 21, 2009. The documents were found to be in conformance with the City's General Plan, per Government Code Section 65401.

Alternative Courses of Action

1. Approve the 10-year CIP, including capital projects, revenue assumptions and anticipated financing, and authorize expenditures for the three-year period beginning in FY09/10 and ending in FY11/12. Council's recommended changes, if any, will be brought for final adoption on June 16, 2009.
2. Approve the 10-year CIP with changes to revenues and/or bond financing assumptions; direct staff to reduce project expenditures by an equal amount of reduced revenues.

Recommendation for Action

Staff recommends that the City Council approve Alternative No. 1.

Prepared by: Kimberly McKinney
Senior Accountant

Lynn Gatie
Senior Management
Analyst, Engineering

Mark G. Deven
City Manager

Attachments