Budget Overview and Summary

This budget document is more than just numbers representing dollars to be spent in the upcoming fiscal year; it is the plan for the City operations, and the program details necessary to carry out this plan. This budget serves four distinct functions:

- A financial plan (as defined within each program);
- A policy document (as defined in the overview and within each program);
- An operations guide (as defined within each program); and
- A public education device (as defined within each program and supplemental information).

This document presents the Program and Financial Plan for 2007-08 as adopted by the governing bodies of the City of Lancaster and the Lancaster Redevelopment Agency on June 26, 2007. Yet it is more than a financial plan, it is a policy document that incorporates priorities set by the City Council and Lancaster Redevelopment Agency for the fiscal year. Key principles, which are reflected in the operations sections of this document, are:

- Maintain the fiscal integrity of the City;
- Emphasize economic development i.e., job creation and retail development;
- Public Safety: create a safe environment for our citizens to live, work and play;
- Provide an exceptional level of customer service to our taxpayers; and
- Manage growth and address the pressures to meet quality of life issues that emerge.

These principles are directly reflected in the allocations within the budget.

In addition, the 2020 Vision Plan, which establishes the vision for the City over the next 13 years, was the guiding document in recommending new programs and projects. The Vision Plan established the following priorities:

- Enhancing public safety;
- Improving infrastructure to meet growing needs;
- Bringing new jobs and economic vitality to the community;
- Encouraging responsible growth and development;
- Revitalizing neighborhoods and ensuring the availability of affordable housing;
- Continuing development of great parks and leisure time activities;
- Ensuring that needed health and human services are available locally.

City of Lancaster
Program/Performance Budget Preparation Process

The formal budget preparation process began in January with a budget team meeting to determine the budget process and schedule. In February, there was a budget kick-off meeting to distribute the Budget Guide and answer any questions. The Budget Guide provided the calendar, information on the process, and sample worksheets for use in development of the budget. Worksheets included a combined Year End Estimate and 5-Year Revenue History, and a Base Budget. The Finance Department prepared revenue projections for the upcoming year for major revenue sources. These revenue projections [see Revenue Source Definitions, (near the back), for basis of estimates], and subsequent expenditure projections, are on a modified accrual basis.

During the month of February, departments developed year-end estimates of revenues and expenditures for FY 2006-07 and revenue projections for FY 2007-08. Expenditure budgets, including base budget adjustments and decision packages for new programs, positions and services were due in Finance February 23.

During the month of March, the budget team and departments met to review their goals for the coming year and to discuss their budget submittals. The meetings were interactive and informative in making critical policy and funding decisions.

These meetings were followed by compilation of the total effect of all programs and the financial resources to fund those programs. Through a series of follow-up meetings and discussions, Finance balanced and finalized the budget for distribution to the City Council, the press, and the public at a special Council workshop scheduled for the middle of May.

Major budget policies include: maintaining a 10% fund balance reserve, maintaining a General Fund with no long-term debt, fully appropriating funding for each capital improvement project (to prevent shortfalls the following year), and conservatively projecting revenues (at the minimum that can be expected to be received) and expenditures (at the maximum to be spent).

A public hearing occurred on June 12 to take public input regarding the budget, and the final budget adoption date was June 26, 2007.
Timeline for the 2007-08 Budget Process

<table>
<thead>
<tr>
<th>Budget Team Meeting to determine budget process</th>
<th>Budget Kick-Off Meeting; Development of Year-End Estimates &amp; Revenue Estimates</th>
<th>Budget Packages Due to Finance &amp; Reviewed at Department Meetings</th>
<th>Final Budget Meeting &amp; Budget Compilation</th>
<th>City Manager Presents Proposed Budget to Council</th>
<th>Public Hearing; City Council Adopts Budget Effective July 1</th>
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</thead>
<tbody>
<tr>
<td>January</td>
<td>February</td>
<td>March</td>
<td>April</td>
<td>May</td>
<td>June</td>
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Basis of Budgeting

The City utilizes the modified accrual basis of budgeting for its general government fund type budgets; there are no enterprise funds. Simply stated, obligations of the City are budgeted as expenses, but revenues are recorded when we know how much to expect (measurable), and we receive the revenues within the time needed to make payments for costs incurred within the fiscal year. This differs from “generally accepted accounting principles”, GAAP, with outstanding purchase orders at the end of the year recorded as expenses. All annual appropriations (authorizations to expend funding) lapse at the end of the fiscal year unless there are outstanding encumbrances (commitments to pay for goods/services ordered through the utilization of a purchase order, a formal authorization of the City, or a contract).

The Comprehensive Annual Financial Report (CAFR) presents the City’s financial status based on “Generally Accepted Accounting Principles” (GAAP). In 1999, the Government Accounting Standards Board (GASB) published sweeping changes in state and local government financial reporting. This new reporting standard calls for financial statements prepared using full accrual accounting, rather than the modified accrual basis. The method of budgeting continues to be on a modified accrual basis.

Allocating the Cost of Services

The City allocates administrative costs among the services and funds that benefit from those activities. The allocation method is determined by the appropriate service unit. For example, accounts payable costs are allocated by the number of invoices generated by a department, payroll division expenses are allocated by the number of FTEs in a department. The cost allocation plan was updated during the past fiscal year and adopted in December 2006 to ensure utilization of the appropriate allocation amounts for distribution amongst those activities not funded by the General Fund.
Modification of the Budget after Adoption

The City holds a mid-year budget review workshop with the City Council each January to adapt the budget to the current economic climate. The Finance department prepares an economic analysis in early December, followed by departmental meetings with the budget committee, to prepare the recommended budget modifications. These modifications are then brought to the Council for adoption following the workshop.

The City Council receives supplemental appropriation requests as necessary. Because this is a program budget, the City Council adopts the program and appropriates the necessary funding. Changes that increase the total appropriation for the program must be approved by the City Council. The City Manager, Finance Director, and affected Department Heads, without returning to Council for approval, are responsible for making necessary modifications in line item budgets to best manage the operation of the program, as long as the total appropriation for that program does not increase during the fiscal year.
Revenue and Expenditure Estimates

Budgetary revenue estimates are prepared using a variety of methods. Certain revenue sources, such as Federal and State grants, and transportation funds, are relatively fixed and known. State subventions (Vehicle License Fees) and gas tax funds estimates are provided by the State. Other revenues, such as recreation fees, are stable and based on the number of programs planned, historical data, and current economic conditions.

The largest single source of revenue for the City's General Fund is sales tax. The City receives a 1% tax on purchases, excluding food and labor. Sales tax represents 35% of all General Fund revenues. This revenue source provides for the City's law enforcement efforts, our number one priority.

Vehicle License Fees and Property Taxes are up, reflective of the growth in population and assessed valuation that occurred during the past few years. The chart below shows the historical revenue amounts of these important General Fund sources. You can see the impact the triple flip has had on the makeup of the City’s revenue stream. Property tax has become much more significant, while Vehicle License Fees are much less important.

These important revenue sources are expected to be up slightly from FY 2006-07, with most of the growth coming in the form of property tax in lieu fees, due to the increases in assessed valuation the city has been experiencing over the past several years. This is expected to slow down with the slow down it the housing market, however, assessed valuation updates lag the market and as a result we continue to see increases.
Another significant portion of General Fund revenues is generated by developer fees, franchise fees, and interest income. These are projected through trend analysis, economic forecasts from state and national sources, and other information obtained from local builders, retail outlets, and franchisees. Developer fees are fairly easy to predict in the short run due to the long lead times of housing projects. For FY 2007-08 it is estimated that approximately 1,100 residential building permits will be issued. This is relatively flat from the expected 1,137 permits in the prior year.

The City also receives revenues that are restricted to specific purposes such as road construction, park improvement and expansions, utility/drainage improvements, and assessment districts. These dollars are programmed through Capital Improvements Projects or "Other Funds" included in this document.

Investment income, although minimal compared to a decade ago, still continues to be a source of income for the City. The City's policy is to invest all funds upon receipt in interest bearing accounts. The City continues to follow its policy of conservative investments. Safety of principal is the number one priority, followed by liquidity, the availability of cash to pay bills when needed. Yield on investment is a tertiary concern. In light of investment problems by various government agencies, it is good to know that the City of Lancaster does not chase unrealistic investment yields, nor does it invest in derivatives. We earn it “the old fashioned way”.

The City of Lancaster has no general obligation debt; however, bonded debt issued by other districts, such as Los Angeles County Sanitation District, Los Angeles County Water District, school districts, hospitals, and Los Angeles County General Fund are added to the general property tax levy. Other districts and entities (including the Lancaster Redevelopment Agency) have debt obligations that are funded by specific revenue sources, and are not added to the general levy. The City does administer a few special assessment districts and maintenance districts; these pay for themselves through scheduled annual assessments collected through the property tax roll.

During fiscal year 2006/07, revenues were lower than expected, necessitating a negative adjustment to development fees at mid-year. This was primarily due to the slowing housing market and inflationary pressures. We also experienced lower than expected sales tax revenue due to the slowing in automobile sales. We are not expecting any significant change in 2007/08, so we will need to find a reliable source of revenue to address unfunded liabilities and allow the City to maintain service levels over time.
Annual Appropriations Limit

The Appropriations Limit, established by the State of California per Article XIIIB of the California State Constitution, sets a limit for the annual appropriations of tax proceeds for all municipalities.

Article XIIIB was amended by Proposition 111 to change the method of calculating the annual appropriations limit. Prior to Proposition 111, the annual appropriations limit was adjusted annually by the change in the cost of living or by the change in California per capita personal income, whichever was less, and by the percentage change in the population of the City.

Under the new guidelines set forth by Proposition 111, the annual appropriations limit will not exceed a base year adjusted by the change in population of the City or the County combined with either the change in California per capita personal income or the change in the local assessment roll due to local nonresidential construction. Proposition 111 also changed the base year for all municipalities to 1986-87.

The following table compares the difference between Lancaster’s Appropriations Limit and the estimated proceeds of taxes that are subject to the limit. With a gap of $82,441,295 the City remains well below its Appropriations Limit of $129,150,360 for FY 2007-08.

<table>
<thead>
<tr>
<th>FISCAL YEAR</th>
<th>APPROPRIATIONS LIMIT</th>
<th>SUBJECT TO LIMIT</th>
<th>DIFFERENCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997-1998</td>
<td>$75,028,022</td>
<td>$19,254,097</td>
<td>$55,773,925</td>
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<tr>
<td>1998-1999</td>
<td>80,625,930</td>
<td>23,171,310</td>
<td>57,454,620</td>
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<tr>
<td>2001-2002</td>
<td>91,532,419</td>
<td>25,129,977</td>
<td>66,402,442</td>
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<tr>
<td>2002-2003</td>
<td>91,318,734</td>
<td>26,921,043</td>
<td>64,397,691</td>
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<tr>
<td>2003-2004</td>
<td>95,694,454</td>
<td>26,965,074</td>
<td>68,729,380</td>
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<tr>
<td>2004-2005</td>
<td>101,127,627</td>
<td>29,302,048</td>
<td>71,825,579</td>
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<tr>
<td>2005-2006</td>
<td>110,052,072</td>
<td>33,768,526</td>
<td>76,283,546</td>
</tr>
<tr>
<td>2006-2007</td>
<td>118,860,688</td>
<td>42,692,278</td>
<td>76,168,410</td>
</tr>
<tr>
<td><strong>2007-2008</strong></td>
<td><strong>129,150,360</strong></td>
<td><strong>46,709,065</strong></td>
<td><strong>82,441,295</strong></td>
</tr>
</tbody>
</table>
The 2007-08 Budget, Planning for the Future

We developed the 2007-08 budget with our future in mind. Even with all the effort, analysis, and thoughtful formulation that went into preparation of this financial plan, it remains a flexible document. Its relevance can only be measured by the extent to which it moves the community toward Council's goals and objectives. While it must facilitate progress toward long-range goals, it must also assure responsiveness to day-to-day needs, and be sufficiently flexible to accommodate the unanticipated. Insofar as budget projections necessarily look more than a year ahead of their actual preparation, it is essential that the budget process be viewed as a continuous one, not a "one shot" event. This is evident in our process of mid-year reviews.

Budgets are based on a set of assumptions for the upcoming year. These assumptions are developed well in advance of the actual start of the fiscal year, and as such, (unless you are a city with a long history of no growth or change) the budget must have the flexibility to guide the City without locking it into a strict control system. We all want to have full control of our futures, but realize that we do not. The Finance Department, as well as the operating departments, continually monitor the fiscal status of ‘actual versus budget’ through a ‘real-time’ financial and reporting system, and quarterly meetings with the City Manager, Finance Director and Department Heads. This, and the formalized midyear budget review, helps keep the City moving in a positive direction with the flexibility to deal with those economic bumps in the road.