



# Financial Section

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## INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and Members of the City Council  
City of Manhattan Beach, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Manhattan Beach, California, as of and for the year ended June 30, 2008, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Manhattan Beach's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Manhattan Beach as of June 30, 2008, and the respective changes in financial position and cash flows, where applicable, and the respective budgetary comparison for the General Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December, 18, 2008, on our consideration of the City of Manhattan Beach's internal control over financial reporting and our tests of its compliance with certain laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



To the Honorable Mayor and Members of the City Council  
Manhattan Beach, City Hall  
City of Manhattan Beach, California

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the City's basic financial statements. The accompanying introductory section, the combining and individual fund statements, schedules and statistical tables are presented for the purpose of additional analysis and are not a required part of the basic financial statements. The accompanying combining and individual nonmajor fund financial statements and schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The accompanying introductory section and statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

*Lance, Soll & Loughard, LLP*

December 18, 2008

## CITY OF MANHATTAN BEACH

### MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Manhattan Beach, we offer our readers of these financial statements this narrative overview and analysis of the financial activities of the City of Manhattan Beach for the fiscal year ended June 30, 2008. We encourage readers to consider this information in conjunction with additional information that we have furnished in our letter of transmittal, which can be found on pages i to xi of this report.

#### FINANCIAL HIGHLIGHTS

##### *Government Wide Financial Basis*

- As of June 30, 2008, the City's total net assets citywide (including all governmental and business type activities) totaled \$171,118,767. This is an increase from the prior fiscal year of \$1,065,337, or .6%.
  - Governmental net assets increased slightly by \$511,779 (.4%) to \$131,060,065.
  - Business type activity net assets increased by \$773,822 (2%) after restatement of beginning balance by negative \$220,264, largely due to investment earnings and rents of \$874,003.
- Unrestricted net assets, which may be used to meet the government's on-going obligations within certain parameters and requirements, totaled \$41,561,172. This is a decrease of \$1,641,998 (3.8%) from FY 2006-2007 levels. The decline is the result of the use of working capital to generate capital assets, and the payment of required actuarial contributions to meet GASB 45 (Other Post Employment Benefits, or OPEB) pronouncement.
- Citywide capital assets, net of depreciation, increased by \$1.2 million from the prior year, the result of infrastructure and water enterprise capital expenditures.
- The City's bonded debt decreased by \$1.78 million during FY 2007-2008. This decrease is attributable to the scheduled principal pay down of issued bonds and leases by both governmental activities and business type activities.
- Long term insurance claim reserves were increased by \$1.78 million primarily attributable to a high level of workers compensation claims activity. Employee leave reserve balances were marginally increased to keep pace with the value of wage increases.

##### *Fund Financial Basis*

- As of June 30, 2008, the General Fund balance was \$18,437,158. Fund expenditures exceeded revenues by \$2,358,950. The imbalance was primarily caused by the expenditure of \$4.72 million for advanced funding of the General Fund portion of Other Post Employment Benefits (OPEB) for future retiree medical benefits, which was mostly paid from reserves.
- Total Governmental Fund revenue totaled \$56,724,348, a decrease of 10.2% (\$6,446,962) from the prior year. One-time bond proceeds and prepayment revenues from property owners for underground assessment district construction in the prior year (which were not repeated in the current year) accounted for \$8.5 million in decreases. Offsetting that is revenue from the City's Pension Fund transferred to the General Fund (\$1.1 million) to contribute to the retiree medical benefits pre-payment, as well as \$423,301 from the Insurance Fund to reimburse the General Fund for salary continuation payments for employees out on injuries.
- Governmental Fund expenditures totaled \$60,509,915, down \$13,821,855 (18.6%) from FY 2006-2007. In the prior year, there were one-time expenditures of pension obligation bond proceeds (\$5,777,433), as well as disbursements from the underground assessment district funds (\$11,168,303) which account for the decrease.

- General Fund transfers-out totaled \$207,984 for the following purposes:
  - \$189,967 to the Street Lighting Fund to relieve a deficit from operations
  - \$18,017 to the Insurance Fund to maintain policy reserves.

## USING THIS ANNUAL REPORT

### Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements, which is comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

### Reporting on the City as a Whole

**Government-wide financial statements:** The *government-wide financial statements* are designed to provide readers with a broad overview of the City's finances in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of the City's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City of Manhattan Beach is improving or deteriorating.

The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs on a full-accrual basis, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

The government wide statement of activities has two components:

#### *Governmental Activities*

This is a consolidation of all governmental funds and includes the General Fund, Capital Projects Funds, Special Revenue Funds and Internal Service Funds. These funds are supported by taxes, intergovernmental revenues, grants, and charges for services. Expenses include materials and labor, depreciation, and amortization of prepaid pension obligations. Governmental fund expenditures for payment of principal on long debt and capital assets are excluded. All intra-governmental charges and expenses and transfers within governmental funds are eliminated.

All internal service fund expenses and depreciation on capital assets are fully allocated to each functional program. Expenses are classified among the following programs: general government, public safety, culture and recreation, and public works. Program activities that produce revenues or receive grant support are applied against program expenses to yield the net expenses. Revenues that cannot be attributed to a specific program, such as taxes and interest (e.g. General Revenues), are shown separately. The total of General Revenues, less net program expenses, generates the change in net assets. Total net assets of governmental activities differs from fund balances of governmental funds by long term assets (capital and prepaid pension), long term liabilities and the total of internal service fund net assets.

#### *Business Type Activities*

This includes all enterprise funds (Water, Waste Water, Storm Water, Refuse and Parking Funds). These activities have been traditionally presented as enterprise funds and tie directly to the *Statement of Revenues, Expenses, and Change in Net Assets – Proprietary Funds*, as shown in the Funds section of this report.

The government-wide financial statements can be found on pages 19 and 20 of this report.

## Reporting on the City's Most Significant Funds

**Fund financial statements:** A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Manhattan Beach, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds and fiduciary funds.

**Governmental funds:** *Governmental funds* are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spend-able resources, as well as on balances of spend-able resources available at the end of the fiscal year. In effect, the budgetary government fund statements are working capital flow of funds statements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Following the governmental funds *Balance Sheet*, and *Statement of Revenues, Expenditures and Changes in Fund Balances*, there are respective reconciliations of the fund balance to *Statement of Net Assets*, and *Net Change in Fund Balances* – total governmental funds to change in net assets of governmental activities. As discussed above, the reconciliations include treatment of capital expenditures, depreciation, changes in capital assets, long term debt, prepaid pension costs, full accrual versus modified accrual and change in net assets of internal service funds

The City of Manhattan Beach maintains 11 individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund and the Capital Projects fund, both of which are considered to be major funds. Data from the other 9 governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these *non-major* governmental funds is provided in the form of *combining statements* elsewhere in the fund financial statements section of this report.

The City of Manhattan Beach adopts an annual appropriated budget for each of its governmental funds. A budgetary comparison statement has been provided for each governmental fund to demonstrate compliance with this budget.

The basic governmental fund financial statements can be found on pages 23 to 38 of this report.

**Proprietary funds:** Proprietary funds account for goods and services provided to customers and for cost recovery via service charges. There are two types of proprietary funds: enterprise funds which provide services to outside users (residents and businesses of Manhattan Beach), and internal service funds, which provide services to City departments. The City uses internal service funds to account for its fleet of vehicles, computer systems, shared building and maintenance costs, and City-wide insurance costs. Because these services predominantly benefit the governmental function, they have been included within governmental activities in the government-wide financial statements and related intra-governmental charges and transfers have been eliminated accordingly, except for charges and transfers to the enterprise funds, which are quasi-internal transactions.

Proprietary fund financial statements provide the same type of information as the government-wide financial statements, only in more detail. All four internal service funds are combined into a single, aggregated presentation in the proprietary fund financial statements. Individual fund data for the internal

service funds is provided in the form of combining statements. Four of the City's seven enterprise funds are considered major funds and presented as such in the fund financial statements. The three non-major funds, Storm Water, County and State parking lots, are presented individually in the combining statements.

The combining statements referred to earlier in connection with non-major governmental funds, proprietary and internal service funds are presented immediately following the notes to the financial statements. Combining and individual fund statements and schedules can be found on pages 79 to 108 of this report.

**Notes to the financial statements:** The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 39 to 78 of this report.

### The City as Trustee

**Other information:** In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information* concerning the City's progress in funding its obligation to provide pension benefits to its employees and budget-to-actual financial comparisons for the General Fund. The City has elected to present this information within the basic financial statement and financial statement sections of the report. Note 9 provides detailed analysis of City retirement plans.

All of the City's fiduciary activities are reporting distinctly in a separate Statement of Fiduciary Assets and Liabilities. These figures are not combined with other financial statements because the City cannot use these assets to finance present or future operations. The City is responsible for ensuring that the assets reported in these funds are used for their intended purpose.

## GOVERNMENT-WIDE FINANCIAL STATEMENTS

As noted earlier, net assets (assets in excess of liabilities) may serve over time as a useful indicator of a government's financial position. In the case of the City of Manhattan Beach, net assets totaled \$171,118,767 at June 30, 2008.

By far, the largest portion of the City's net assets (88%) reflects its investment in capital assets (e.g., land, infrastructure, buildings and equipment). The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending.

### City of Manhattan Beach Net Assets

	Governmental Activities		Business Type Activities		Total	
	2008	2007	2008	2007	2008	2007
Current Assets	\$ 42,156,000	\$ 46,237,333	\$ 14,809,449	\$ 15,999,710	\$ 56,965,449	\$ 62,237,043
Non-Current Assets	\$ 132,435,624	127,995,339	\$ 42,861,242	41,673,414	175,296,866	169,668,753
<b>Total Assets</b>	<b>174,591,624</b>	<b>174,232,672</b>	<b>57,670,691</b>	<b>57,673,124</b>	<b>232,262,315</b>	<b>231,905,796</b>
Current Liabilities	\$ 11,183,912	10,402,897	\$ 1,900,163	2,081,125	13,084,075	12,484,022
Non-Current Liabilities	\$ 32,347,647	33,281,489	\$ 15,711,826	16,086,855	48,059,473	49,368,344
<b>Total Liabilities</b>	<b>43,531,559</b>	<b>43,684,386</b>	<b>17,611,989</b>	<b>18,167,980</b>	<b>61,143,548</b>	<b>61,852,366</b>
Invested in Capital Assets						
Net of Related Debt	\$ 94,464,084	93,644,407	\$ 24,736,570	23,447,692	119,200,654	117,092,099
Restricted	\$ 8,591,311	8,011,040	\$ 1,765,630	1,747,121	10,356,941	9,758,161
Unrestricted	\$ 28,004,670	28,892,839	\$ 13,556,502	14,310,331	41,561,172	43,203,170
<b>Total Net Assets</b>	<b>131,060,065</b>	<b>130,548,286</b>	<b>40,058,702</b>	<b>39,505,144</b>	<b>171,118,767</b>	<b>170,053,430</b>

Net assets of the City's *Governmental* activities amounted to \$131.06 million, an increase over the prior year of \$511,779. Of the \$131.06 million, \$94.46 million is invested in capital assets net of related debt such as land, buildings, machinery, infrastructure, equipment and other improvements; \$8.59 million is restricted for debt service or for Special Revenue Fund resources that are subject to external restrictions on use. The balance of unrestricted net assets (\$28.0 million) is investment in economic resources available to the City. A significant portion of this remaining balance is subject to capital project designations and policy reserves displayed in financial Note 8.

Net assets of the City's *Business-type* activities totaled \$40.06 million. This represents an increase from FY 2006-2007 of \$553,558. \$24.7 million is invested in capital assets (land, buildings, machinery, equipment, etc.) net of related debt, while \$1.77 million is reserved for debt service and for business improvement district use. \$13.56 million is investment in economic resources available to the City.

The City's total change in net assets amounts to \$1.285 million with respect to the beginning balance as restated. The following is the condensed Statement of Activities and Changes in Net Assets for the fiscal years ending June 30, 2007 and June 30, 2008:

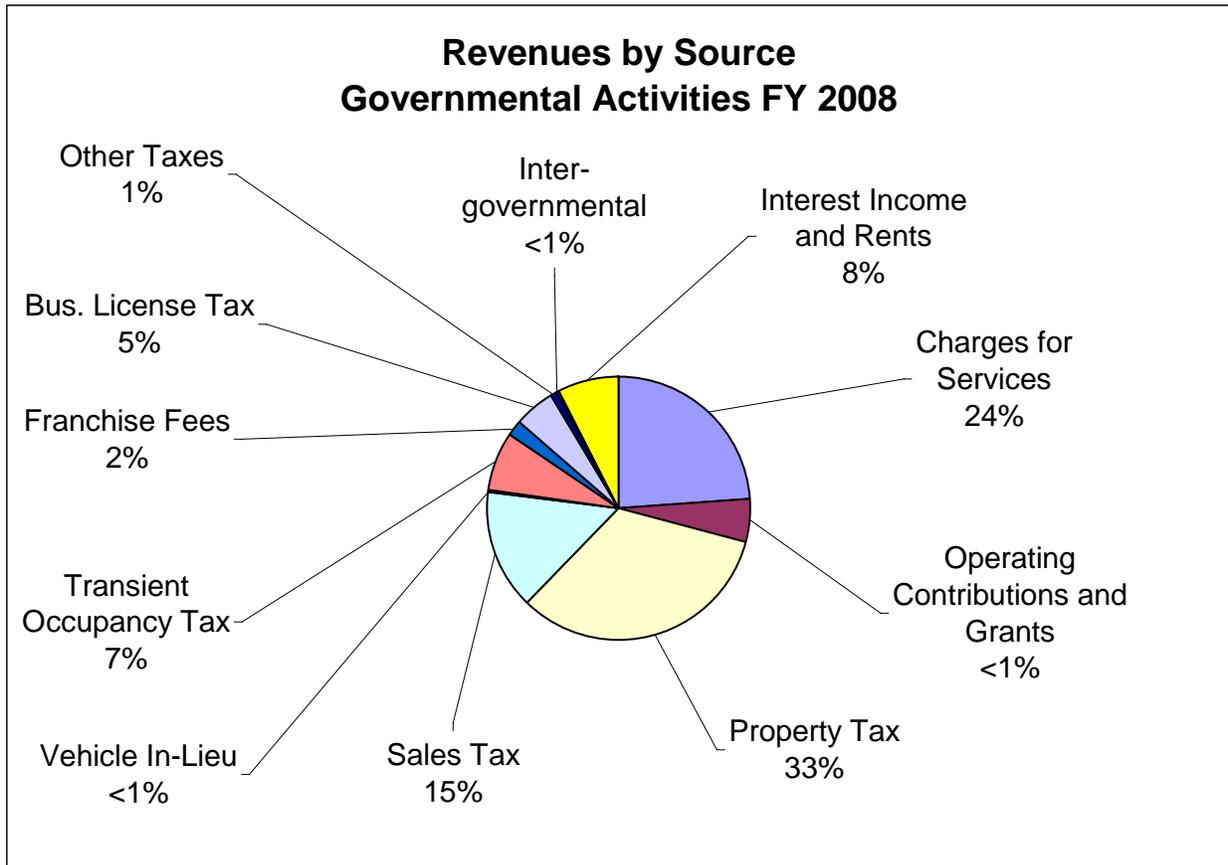
**City of Manhattan Beach Changes in Net Assets**

	Governmental Activities		Business -Type Activities		Total	
	2008	2007	2008	2007	2008	2007
<b>Program Revenues:</b>						
Charges for Services	\$ 13,491,412	\$ 12,904,269	\$ 14,357,640	\$ 14,889,212	\$ 27,849,052	\$ 27,793,481
Operating Contributions and Grants	2,250,606	1,933,403	90,853	10,861	2,341,459	1,944,264
Capital Contributions and Grants	679,865	10,923,007	900,000	-	1,579,865	10,923,007
<b>General Revenues:</b>						
Property Taxes	18,567,451	17,257,507	-	-	18,567,451	17,257,507
Other Taxes	16,580,383	16,223,609	-	-	16,580,383	16,223,609
Motor Vehicle in Lieu	157,143	245,008	-	-	157,143	245,008
Other	5,544,068	4,336,284	874,003	935,323	6,418,071	5,271,607
<b>Total Revenues</b>	<b>57,270,928</b>	<b>63,823,087</b>	<b>16,222,496</b>	<b>15,835,396</b>	<b>73,493,424</b>	<b>79,658,483</b>
<b>Expenses:</b>						
General Government	9,090,991	9,057,584	-	-	9,090,991	9,057,584
Public Safety	31,752,170	27,134,132	-	-	31,752,170	27,134,132
Public Works	8,675,214	19,721,241	-	-	8,675,214	19,721,241
Parks & Recreation	6,031,938	5,593,739	-	-	6,031,938	5,593,739
Interest on Long-Term debt	1,178,065	990,298	-	-	1,178,065	990,298
Water, Waste, Storm	-	-	9,198,028	8,894,850	9,198,028	8,894,850
Refuse	-	-	3,888,615	3,858,401	3,888,615	3,858,401
Parking	-	-	2,392,802	1,973,300	2,392,802	1,973,300
<b>Total Expenses</b>	<b>56,728,378</b>	<b>62,496,994</b>	<b>15,479,445</b>	<b>14,726,551</b>	<b>72,207,823</b>	<b>77,223,545</b>
<b>Revenues Over Expenses</b>	<b>542,550</b>	<b>1,326,093</b>	<b>743,051</b>	<b>1,108,845</b>	<b>1,285,601</b>	<b>2,434,938</b>
<b>Transfers In (Out)</b>	<b>(30,771)</b>	<b>26,000</b>	<b>30,771</b>	<b>(26,000)</b>	<b>-</b>	<b>-</b>
<b>Increase (Decrease) in Net Assets</b>	<b>511,779</b>	<b>1,352,093</b>	<b>773,822</b>	<b>1,082,845</b>	<b>1,285,601</b>	<b>2,434,938</b>
<b>Net Assets - Beginning Restatement</b>	<b>130,548,286</b>	<b>129,043,118</b>	<b>39,505,144</b>	<b>38,422,299</b>	<b>170,053,430</b>	<b>167,465,417</b>
<b>Net Assets - June 30 (Year End)</b>	<b>\$ 131,060,065</b>	<b>\$ 130,548,286</b>	<b>\$ 40,058,702</b>	<b>\$ 39,505,144</b>	<b>\$ 171,118,767</b>	<b>\$ 170,053,430</b>
<b>Total Change from Prior Year (Before restatement)</b>	<b>\$ 511,779</b>		<b>\$ 553,558</b>		<b>\$ 1,065,337</b>	

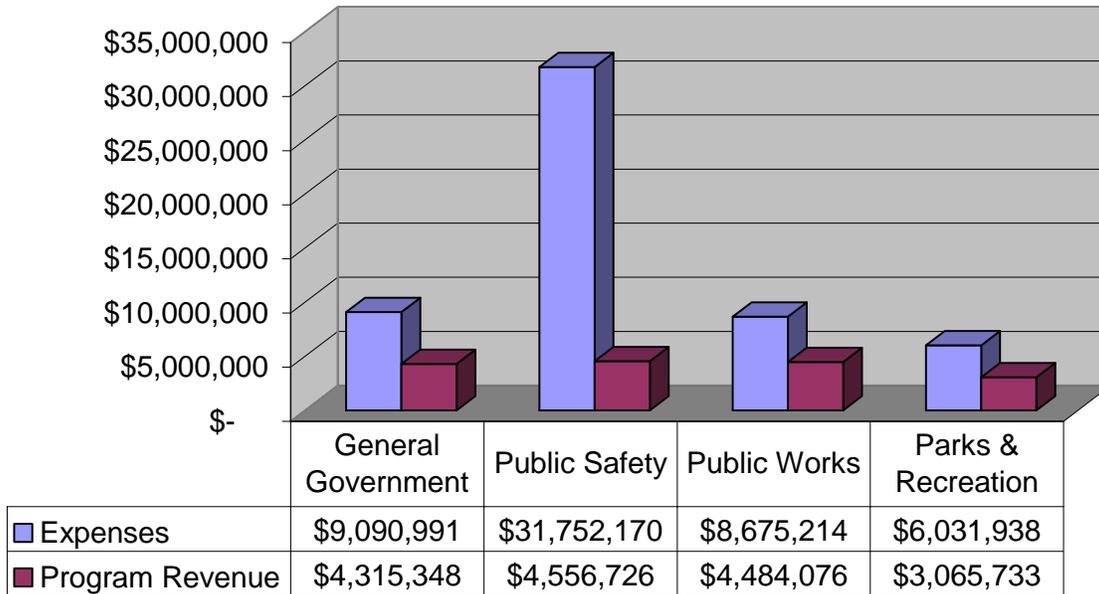
### Changes in Net Assets - Governmental Activities

The City's governmental activities in FY 2007-2008 increased net assets by \$511,779, which was a .4% increase from FY 2006-2007.

Total Governmental revenues of \$57,270,928 are broken-out as follows:



**Governmental Activities Revenue and Expenses  
by Function/Program  
Year Ended June 30, 2008**



Functional expenses (excluding interest on debt) for the years ending June 30, 2008 and 2007 were as follows:

	Total Cost of Services		Net Cost of Services	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
General Government	\$ 9,090,991	\$ 9,057,584	\$ (4,775,643)	\$ (4,521,629)
Public Safety	31,752,170	27,134,132	(27,195,444)	(22,983,178)
Public Works	8,675,214	19,721,241	(4,191,138)	(6,264,602)
Parks and Recreation	6,031,938	5,593,739	(2,966,205)	(1,976,608)
Total	<u>\$ 55,550,313</u>	<u>\$ 61,506,696</u>	<u>\$ (39,128,430)</u>	<u>\$ (35,746,017)</u>

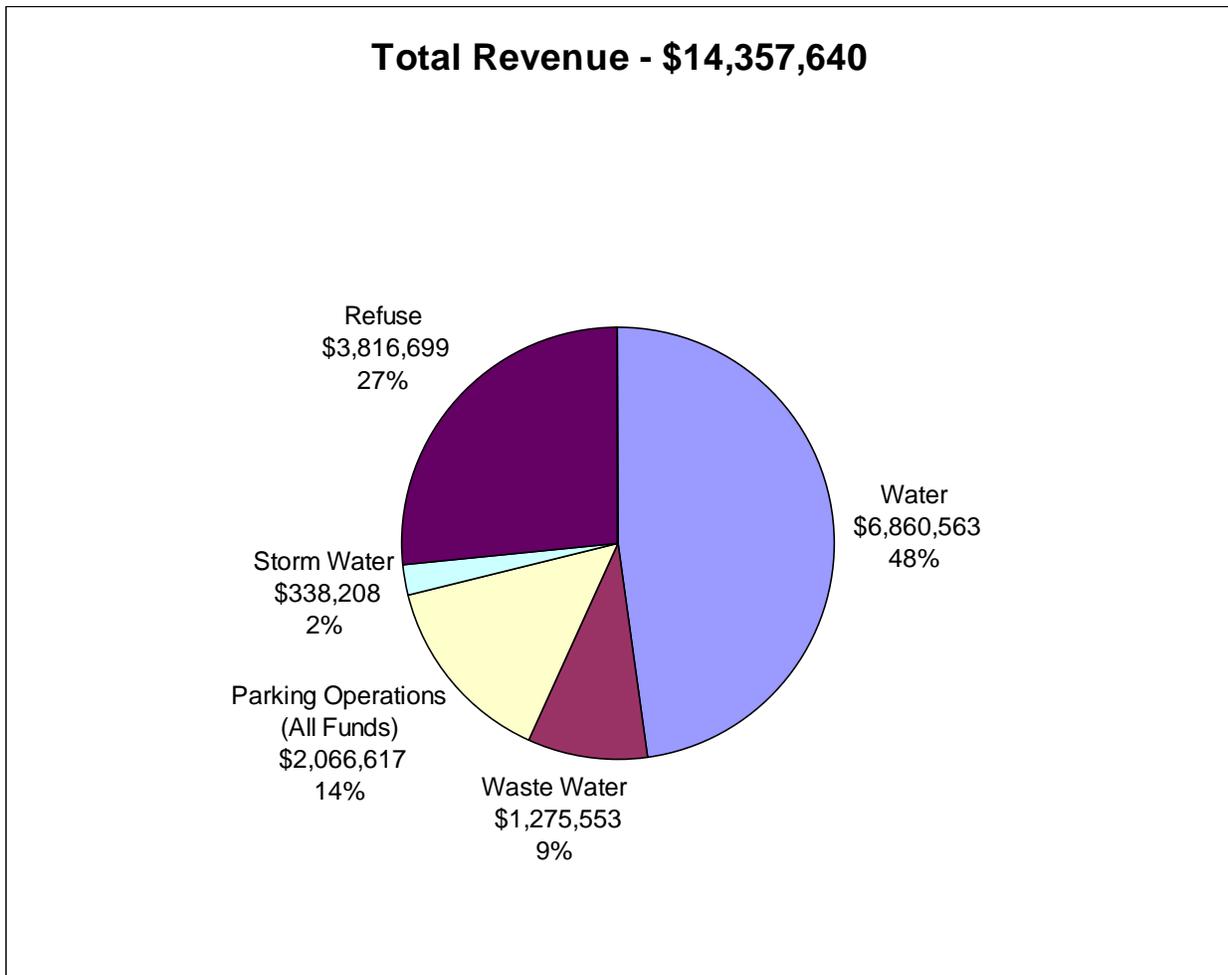
The total cost of services declined from the prior year by \$5.96 million (9.7%), while the net cost of services increased by \$3.38 million, or 9.5% from the prior year. Activities contributing to the change include:

- The one-time revenues and expenditures in 2007, and not repeated in 2008, for underground assessment district formation and construction (see Public Works above). These expenditures benefit the individual property owners and are not considered a City project, and therefore do not generate a City capital asset.
- Salary and benefit cost increases citywide
- The annual required contribution for OPEB

## Business Type Activities

In fiscal year 2007-2008, operating revenues for the City's business type activities amounted to \$14,357,640, while total operating expenses equaled \$14,663,437, for operating income of *negative* \$305,797.

### Operating Revenues by Source - Business Type Activities FY 2008

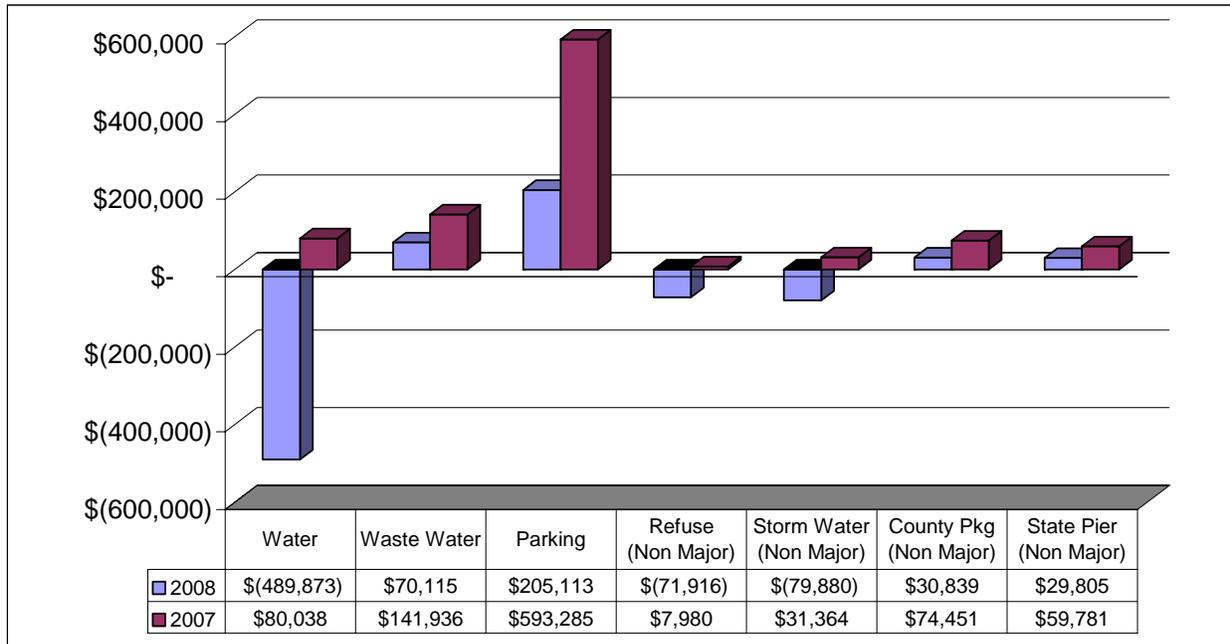


Non-operating revenues net of expenses was \$1,048,848, and consisted of a parking fund grant of \$900,000 for installation of pervious pavement in parking lots, investment income of \$874,853 and debt interest expense of \$816,003. Net income was \$743,822, however it should be noted that without grant revenue which is a nonrecurring event, net income would have been negative \$156,949. Subsequent to 2007-2008 year end, interest rates on investments declined dramatically. As a result, measures will need to be taken to bolster revenues to generate positive net income.

The beginning value of net assets was restated by negative \$220,264 resulting in an increase of net assets of \$773,822.

Operating Income varied across the business-type activities in FY 2008. A year-over-year comparison is presented below. Further analysis of the major funds is discussed later in this report.

**Net Operating Income/(Loss) for Business-Type Activities for 2007 & 2008**



**FUND FINANCIAL STATEMENTS**

**Governmental Funds**

As of the end of the 2008 fiscal year, the City's governmental funds ending fund balances totaled \$30.56 million, a decrease of \$3.83 million in comparison with the prior year. The use of resources totaling \$5,777,433 to fund accrued liability and the normal cost for Other Post Employment Benefits (OPEB) with a third party trustee is the primary cause for the decrease. Infrastructure improvements also contributed to the decrease.

Approximately 76% of the total Governmental Funds total, or \$23.2 million, constitutes unreserved fund balance. The remainder of the fund balance (\$7.35 million) is reserved, to indicate that it is not available for new spending because it has already been committed for on-going capital projects, purchase orders of the prior period, and for legally-required debt service reserves.

***It is important to note that City Council established fund designations in its financial policy requirements and budgetary capital planning initiatives.*** Components of fund balances are listed in Note 8 of these financial statements. Of the \$23.2 million unreserved governmental fund balance noted above, \$14.7 million has been designated by City Council actions. Considering these designations, \$8.5 million in governmental fund balances (General, Capital Improvement, and Special Revenue Funds) remain unreserved and undesignated.

## General Fund

The General Fund is the chief operating fund of the City of Manhattan Beach. At the end of the 2007-2008 fiscal year, unreserved fund balance of the General Fund was \$16.59 million, while total fund balance was \$18.44 million. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 31% (3.7 months) of total General Fund expenditures, while total fund balance represents 34% (4.1 months) of that same.

During the current fiscal year, General Fund expenditures exceeded revenues by approximately \$2.36 million. This imbalance is mainly the result of funding of the accrued OPEB liability and the normal cost in the amount of \$5,704,981. This expenditure was partially offset by revenue of \$1.1 million from the Pension Fund to the General Fund to assist in the pre-funding.

Net transfer activity in this fund totaled \$182,905, and included the following transfers:

- Funds totaling \$18,017 were transferred to the Insurance Reserve Fund to maintain policy reserve levels.
- The Street Lighting Fund received \$189,967 to relieve a deficit fund balance.
- \$25,079 of excess reserves from the County Lot Fund was transferred to the General Fund in line with the contract with the County of Los Angeles.

## Capital Improvement Fund

The Capital Improvement Fund serves to plan and manage the construction and maintenance of non-enterprise projects which are funded through dedicated revenue sources as well as General Fund surpluses which may arise from year to year. Along with its operating budget, the City adopts a five-year capital project plan on an annual basis in which City Council priorities are planned. The Capital Improvement Fund is one of the major funds covered in that City-wide plan.

At the end of the current fiscal year, the unreserved fund balance of the Capital Improvement Fund was \$3.6 million, while total fund balance was \$6.3 million. \$1 million of the unreserved balance has been specifically earmarked for the underground assessment district loan program, leaving \$2.6 million in undesignated fund balance at June 30, 2008 (please see Note 8 to these financial statements). Project reserves, which total \$1.81 million at year-end include:

- \$940,580 for Playground equipment
- \$280,000 for Live Oak and Manhattan Heights park fencing
- \$106,220 for City entryway signage
- \$75,000 for Live Oak Park retaining wall and landscaping
- \$40,000 for Creative Arts Center sound baffling

During Fiscal Year 2007-2008, the Capital Improvement Fund balance decreased by \$1.29 million. The decrease is the result of expenditures for a number of projects and purposes discussed below.

Dedicated revenues in this fund amounted to \$1.3 million in FY 2007-2008. These revenues are earmarked for funding general government capital improvement projects in the effort to maintain and enhance City infrastructure. A breakdown of these follows:

**Hotel Tax:** 15% of the Transient Occupancy Tax has been dedicated to funding CIP's. This has resulted in the generation of \$644,111 of revenue for the year. This is 19% above prior year levels marking a significant increase in general local tourism and patronage.

**Parking Meter Rates:** A twenty-five cent per hour increment of on-street parking meter rates, dedicated to capital improvements, generated revenue of \$536,140 this fiscal year. Actual revenues were consistent with budgetary estimates, and down slightly (3.6%) from last year's results.

**Parking Citation Rates:** Four dollars of most parking citations is dedicated to the CIP fund. For FY 2007-2008, revenue of \$122,216 was realized; a decrease of 4% over the prior year.

This fund realized \$185,849 in permits, interest and other revenue.

Capital Improvement Fund expenditures equaled \$2.7 million which included:

- \$814,574 for Police & Fire facility debt service
- \$700,500 for synthetic turf at the Manhattan Village Soccer Field
- \$185,350 for Strand Improvements
- \$196,600 for the Facilities Strategic Plan project
- \$162,400 for the Council Chambers remodeling project
- \$140,390 for Police & Fire Facility
- \$127,600 towards park playground equipment
- \$90,000 for Downtown Streetscape improvements
- \$51,000 for Polliwog Park exercise equipment
- \$44,000 towards entryway signage at the City's borders

### **Other Governmental Funds**

Other non major governmental funds include all Special Revenue funds used exclusively to account for intergovernmental and assessment proceeds which are restricted in use by law. This group of funds includes the Street Lighting Fund, Federal and State Grants Fund, Gas Tax Fund, Propositions A and C Funds, Asset Forfeiture Fund, Police Safety Grant Fund, the Air Quality Management Fund and Underground Assessment Fund. The majority of the dollars which flow through these funds are used for the maintenance of streets, parks, local transportation programs and the purchase of safety and fuel efficient equipment.

Combined fund balances at year-end approximated \$5.87 million, virtually unchanged from 2007. Gas Tax expenditures totaling \$1.8 million for sidewalk repair and street resurfacing caused the Gas Tax Fund balance to decline by \$413,468. However, accumulation of reserves for the future Sepulveda Bridge Widening project in the Proposition C Fund added \$569,373. Changes in fund balances for this group can be expected to fluctuate as capital projects are expended over time.

One fund in particular, the Street Lighting Fund, continues to run deficits each year. For FY 2007-2008, expenditures exceeded revenues by \$189,967. Because there is no fund balance to draw upon, the General Fund contributed the entire \$189,967 needed for continued operations. These contributions will be necessary until a Proposition 218 assessment vote is successful in raising the assessment rates and revenues.

### **Proprietary Funds**

The City's proprietary funds consist of enterprise funds and internal service funds. The enterprise funds include Water, Waste Water, Refuse and Parking Funds (major funds), as well as Storm Water, and both the County and State Parking Lot Funds (which are considered non-major). Internal service funds include Insurance Reserve, Information Systems, Fleet Management and Building Maintenance and Operations.

At year-end, total net assets of all enterprise funds amounted to \$40.1 million, of which \$13.6 million is unrestricted. Within the working capital of that amount, Council, by policy, has established certain designations for continuing CIP's and financial policy goals, which total \$5.29 million. The remaining restricted balance has been classified as such given the existence of legal reserve requirements for ongoing bonded capital projects, business improvement district funds and debt service requirements.

Overall, enterprise funds combined net income was \$743,051 before transfers. Net assets increased for all funds by \$773,822.

Several enterprise funds are worth noting this year. In each of these cases, operating expenses are rising at a greater pace than revenues, signifying the need for future rate increases to sustain the operations:

- Water Fund net income from operations has been declining for the past two years. In 2006 net income from operations totaled \$598,000, and in 2007 totaled \$80,000. In 2008, the net income from operations was negative \$489,873. This is the result of operating expenses (labor, materials, services, etc.) rising by 2.8%, while revenues actually declined by 5%.
- A similar situation exists in the Waste Water Fund, which had \$244,530 in net operating income in FY 2006, \$141,940 in 2007, and now \$70,115 in 2008. While operating expenses rose slightly by 1.2%, revenues declined by 4.4%.
- Storm Water Fund net operating income in FY 2008 was a negative \$79,880. This was the result of operating expenses increasing by 30% over 2007 levels to \$418,088, while revenues dropped 4.4% to \$338,208 from the prior year.

The reduction in net operating income in all three funds is mitigated somewhat from non-operating revenues (interest income).

Subsequent to the end of FY 2007-2008, the City Council approved water and waste water rate increases to support those funds. However, further rate increases will be necessary to maintain levels of service and fiscal integrity for those operations.

Storm Water revenues are based on property assessments which require a Proposition 218 vote to change. Increased costs from new governmental clean water standards, as well as labor and materials costs will eventually require such a vote to support this activity.

Parking Fund net income, before transfers, was \$627,453, while income from operations was \$205,113. Non operating income was \$422,340 with a major contribution from a one-time State grant of \$900,000. This grant was used to install pervious payment in city parking lots. It is important to note that while the fund had positive net income, the overall cash flow generated from parking operations of \$610,108 is insufficient to meet payment of bond principal of \$270,000 and interest of \$581,609, while still providing for future capital improvements. Subsequent to the end of the 2008 fiscal year, the City Council took steps to support this fund through meter rate increases, which is anticipated to improve the cash flow and profitability of this fund.

### *Internal Service Funds*

Unrestricted net assets of the internal service funds at the end of the year amounted to \$2.16 million with a net assets total of \$4.7 million. Net assets decreased by \$1,132,073 due to increasing claims cost in the Insurance Reserve Fund, primarily from Workers Compensation. FY 2007-2008 claims totaled \$3.5 million, up from \$2.96 million in 2007. The City continues to look for ways to proactively manage risk and reduce these costs.

## General Fund Budgetary Highlights

### Estimated Revenues

Actual revenues, which totaled \$51,911,105, exceeded the original budget by \$3.3 million. Taxes and Assessments exceeded budget by \$1.075 million, Charges for Services came in \$620,000 to the positive, and Use of Money (interest income) exceeded forecasts by \$507,000. Finally, Miscellaneous revenue included \$1.1 million transferred into the General Fund from the Pension Fund to pre-fund retiree medical benefits with a third party.

### Appropriations

The final amended budget reflects an increase of \$5,458,914 over the adopted appropriations.

Significant budget adjustments included:

- \$5,639,619 for funding of the OPEB normal cost and accrued liabilities
- \$422,224 in re-appropriations for open purchase orders from fiscal 2006-2007
- \$681,395 for an engineering analysis for underground assessment districts

The underground assessment district appropriation will be reimbursed to the City upon the successful formation of the specific districts.

## Capital Asset and Debt Administration

**Capital Assets:** The City's investment in capital assets government wide as of June 30, 2008, is \$158,225,662 (net of accumulated depreciation). This is an increase from the prior year of \$1.26 million, or .8%. This investment in capital assets includes land, buildings, park improvements, roadways, sewer, storm drains, vehicles, computer equipment, furniture and other equipment.

### City of Manhattan Beach Capital Assets (Net of depreciation)

	Governmental Activities		Business -Type Activities		Totals	
	2008	2007	2008	2007	2008	2007
Land	\$ 33,634,566	\$ 33,634,566	\$ 1,757,434	\$ 1,757,434	\$ 35,392,000	\$ 35,392,000
Buildings	39,733,862	40,595,968	16,141,008	15,529,973	\$ 55,874,870	\$ 55,905,677
Machinery & Equipment	2,397,549	2,567,276	354,113	312,971	\$ 2,751,662	\$ 2,880,247
Vehicles	2,920,572	3,123,711	-	-	\$ 2,920,572	\$ 3,123,711
Infrastructure	34,770,892	27,711,821	20,889,327	20,453,153	\$ 55,660,219	\$ 48,164,974
Invested in Joint Venture (RCC)	1,840,811	1,855,268			\$ 1,840,811	\$ 1,855,268
Work In Progress	2,175,840	7,863,987	1,609,688	1,563,900	\$ 3,785,528	\$ 9,427,887
<b>Total</b>	<b>\$117,474,092</b>	<b>\$ 117,352,597</b>	<b>\$ 40,751,570</b>	<b>\$ 39,617,431</b>	<b>\$ 158,225,662</b>	<b>\$ 156,970,028</b>

\*2007 Business Type Activities restated by (\$220,264)

During the current fiscal year, governmental capital assets increased by a net \$121,495 (.1%). The increase is the result of the following:

- \$1.87 million in street improvements
- \$926,500 in park improvements
- \$323,900 of machinery and equipment purchases
- \$415,975 in vehicle purchases

These additions were offset by the sale of surplus vehicles and assets, and by scheduled depreciation.

During the current fiscal year, \$913,875 in net additions to business type activity assets were realized, the bulk of which relates to a grant-funded pervious pavement projects totaling \$1.09 million in the parking funds.

Additional information on the City's capital assets can be found in Note 5 of this report.

**Liabilities:** Total liabilities citywide equal \$55,519,504, an increase of \$145,324 over fiscal 2006-2007. Governmental liabilities increased by \$497,737 (1.3%) while business type liabilities decreased by \$352,413 (2.1%).

### City of Manhattan Beach Outstanding Liabilities

	<u>Governmental Activities</u>		<u>Business Type Activities</u>		<u>Total</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
Marine Avenue COP's	\$ 8,375,000	\$ 8,580,000	\$ -	\$ -	\$ 8,375,000	\$ 8,580,000
Capital Equipment Lease	390,008	558,190	-	-	\$ 390,008	558,190
Police & Fire Facility COP's	12,495,000	12,740,000	-	-	\$ 12,495,000	12,740,000
Accrued Employee Leave & Benefits	2,362,213	2,226,775	104,166	81,579	\$ 2,466,379	2,308,354
Supplemental Leave	27,058	35,595	-	-	\$ 27,058	35,595
Water and Wastewater COP's	-	-	3,715,000	3,820,000	\$ 3,715,000	3,820,000
Metlox Parking COP's	-	-	12,300,000	12,570,000	\$ 12,300,000	12,570,000
Pension Obligation Bonds	6,095,000	6,800,000	-	-	\$ 6,095,000	6,800,000
So. Bay Communications (RCC)	1,750,000	1,830,000	-	-	\$ 1,750,000	1,830,000
Insurance Claim Reserves	7,744,193	5,963,069	-	-	\$ 7,744,193	5,963,069
Unamortized Bond Premium	161,866	168,972	-	-	\$ 161,866	168,972
<b>Total Liabilities</b>	<b>\$ 39,400,338</b>	<b>\$ 38,902,601</b>	<b>\$ 16,119,166</b>	<b>\$ 16,471,579</b>	<b>\$55,519,504</b>	<b>55,374,180</b>
<b>Current</b>	<b>\$ 7,052,691</b>	<b>\$ 5,621,112</b>	<b>\$ 407,340</b>	<b>\$ 384,724</b>	<b>7,460,031</b>	<b>6,005,836</b>
<b>Long Term Liabilities</b>	<b>\$ 32,347,647</b>	<b>\$ 33,281,489</b>	<b>\$ 15,711,826</b>	<b>\$ 16,086,855</b>	<b>\$48,059,473</b>	<b>\$49,368,344</b>

#### *Governmental*

Principal obligations for existing debt were reduced in accordance with existing debt service schedules. The total decrease in debt was \$1,419,060. This decrease was offset by increases in liabilities for compensated absences and insurance cases. As a result, the total governmental liabilities increased by \$497,737. The increase in insurance reserves (\$1.78 million) is due to workers compensation and general liability cases. The increase in compensated absences is due to increases in salary and accrued leave hours.

### *Business Type*

Liabilities decreased as a result of the reduction in bond principal of \$375,000 (\$105,000 in Water/Waste Water bonds and \$270,000 in Metlox Public Improvement bonds). This reduction was offset by an increase of \$22,587 in employee leave and benefits. No new debt was issued in FY 2007-2008.

For the details regarding components of long term liabilities refer to Note 6.

State statutes limit the amount of general obligation debt a governmental entity may issue to 3.75% of its total assessed valuation. The current debt limitation for the City of Manhattan Beach is \$407,300,625.

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGET**

The City Council adopted the FY 2008-2009 operating budget in June 2008. The budget, which included a planned use of reserves of \$520,000 in order to provide fiscal support for the Manhattan Beach Unified School District, estimates revenues at \$51,813,219 and expenditures of \$52,321,483. Factoring out the one-time support, expenditures are projected to be \$51,801,483.

The City's major General Fund revenue sources are beginning to show the affects of the recession and economic slowdown. Property Tax, the single biggest General Fund revenue source, which has had near double-digit growth rates for the past several years, is expected to have lower growth rates – the result of the decline in the housing market. As a result, the 2008-2009 budget projects property taxes to exceed 2007-2008 collections by 4% - a rate much lower than prior years. We expect to see further weakness in the housing market, and potentially lower annual growth rates in the near term.

By way of other revenues in the General Fund, Sales Tax is projected to increase by 1.72% over FY 2007-2008 results, while the Transient Occupancy Tax, which has seen strong growth in the past several years, is projected to be 10% above prior year receipts. In keeping with the housing slump, Building Permit and Plan Check Fees were budgeted below FY 2007-2008 actual levels by 3.9% and 3.7% respectively. Finally, Business License Tax revenue is expected to come in 7% below FY 2007-2008, reflective of the economic slowdown.

On the expenditure side of the equation, there are long term labor agreements in place with the three bargaining units (Police, Fire and Miscellaneous), with the first expiration date occurring in summer 2010. These agreements give us a measure of predictability in our labor costs, which equal nearly 70% of the General Fund expenditures. On a related note, the City is experiencing increased retiree medical liabilities with the passage in 2006 of State Assembly bill AB 2544. This legislation requires the City, as a subscriber to the CalPERS medical plans, to provide certain minimum cash contributions towards retirees' medical premiums, effective January 1, 2008. Those liabilities, as well as other negotiated retiree medical benefits (valued at \$5.7 million) have been recognized as required by GASB 45, and were pre-funded in its entirety during FY 2007-2008 with CalPERS' trust program.

The City completed the Facilities Strategic Plan during FY 2007-2008, which identified the needs for recreational and public facilities. While the ultimate plan is yet to be identified, construction of these facilities will likely require outside funding, the sources of which will need to be identified and evaluated.

Clearly, the recession and economic events of late 2008 will have material impacts on the City's finances. Lower interest rates will affect future investment income, the housing slowdown will continue to affect property taxes and construction-related revenues, and retail and tourism based revenues such as Sales Tax, Business License Tax and Transient Occupancy Tax will be weak.

Overall, the General Fund budget anticipates revenues and expenditures to increase 6.6% and 7.7% respectively over the prior year's budget. Excluding the one-time use of General Fund reserves (\$520,000) to support the school district, expenditures increased by 6.6% in line with revenue growth.

**Requests for Information**

This financial report is designed to provide a general overview of the financial position of the City of Manhattan Beach for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Department, 1400 Highland Avenue, Manhattan Beach, CA 90266.