



April 20, 2009

Honorable Mayor and City Commission
City of Bay City
301 Washington Avenue
Bay City, MI 48708

Re: City of Bay City Fiscal Year 2010 Budget for All City Funds

Dear Mayor Brunner, Commission President Shannon, and City Commissioners:

In accordance with the Uniform Budgeting and Accounting Act (Public Act 2 of 1968) as amended, Section 5.2.(d) and 8.2 of the City Charter, and Commissioner Davidson's July 12, 2004 resolution, I hereby submit to you a balanced budget for fiscal year 2010 (July 1, 2009 through June 30, 2010) totaling \$137,197,773.

Once again, my staff and I struggled in preparing a balanced budget while maintaining quality, core services to our residents, tax payers, and rate payers. The FY 2010 budget was difficult because of the financial services and housing market crises which has driven our country into a full fledged recession. I believe it is imperative for us to understand our environment to fully appreciate the City's continued success. The recommended FY 2010 City budget continues to successfully respond to our residents, tax payers and utility customers changing needs and expectations. The preparation of a balanced budget with only one proposed "reduction in force" and inclusion of several major infrastructure projects was no easy feat. This achievement was possible because of the continuous examination of all aspects of our operations, our commitment to innovation through partnerships, and participation of all stakeholders in moving the City forward while remaining true to the City's vision and mission.

THE BIG PICTURE ... NATIONAL AND STATE ECONOMY

According to the April 4-5, 2009 edition of the Wall Street Journal, "*U.S. employers shed 663,000 jobs in March, pushing the nation's unemployment rate to its highest level since 1983 and casting a shadow over recent signs of a stabilizing economy. The deepening labor market contraction brought job losses for the recession to 5.1 million, with two thirds of the cuts coming since*

November,” the Labor Department said. “The jobless rate jumped to 8.5% from 8.1% -- and many forecasters expect it to top 10% by later this year.”

The United States and the majority of the world is entangled in a recession of extraordinary proportions. In fact, the United States Congress authorized the American Recovery and Reinvestment Act of 2009, a \$787 billion stimulus plan, which is ...

... an unprecedented effort to jumpstart our economy, create or save millions of jobs, and put a down payment on addressing long-neglected challenges so our country can thrive in the 21st century. The Recovery and Reinvestment Act is an extraordinary response to a crisis unlike any since the Great Depression. With much at stake, the Act provides for unprecedented levels of transparency and accountability so that you will be able to know how, when, and where your tax dollars are being spent.
(Recovery.gov)

According to the Recovery.gov website, the American Recovery and Reinvestment Act is intended to:

- create or save more than 3.5 million jobs over the next two years;
- take a big step towards computerizing American’s health records, reducing medical errors, and saving billions in health care costs;
- revive the renewable energy industry and provide the capital over the next three years to eventually double domestic renewable energy capacity;
- undertake the largest weatherization program in history by modernizing 75% of federal buildings space and more than 1 million homes;
- increase college affordability for seven million students by funding the shortfall in Pell Grants, increasing the maximum award level by \$500, and providing a new higher education tax cut to nearly four million students;
- as part of the \$150 million investment in new infrastructure, enact the largest increase in funding of our nation’s roads, bridges, and mass transit systems since the creation of the national highway system in the 1950’s;
- provide an \$800 Making Work Pay tax credit for 129 million working households, and cut taxes for the families of millions of children through an expansion of the Child Tax Credit; and
- require unprecedented levels of transparency, oversight, and accountability.

Additionally, the federal government provided \$25 billion in an initial loan to the auto industries, specifically General Motors and Chrysler. Both car companies have sought additional financial support from the federal government. Recently, President Obama has demanded and received the resignation of Rick Wagoner, GM Chairman and CEO. Also, the White House Auto Task Force was charged

with overseeing the restructuring of General Motors which could result in bankruptcy – an uncertain process with as much uncertainty on the outcome.

On November 5, 2007, the City Commission unanimously approved a resolution under P.A. 328 of 1998 as amended, for 100% personal property, 50 year tax abatement for all new equipment purchased and brought on-line at the Bay City Powertrain Plant. In doing so, the City of Bay City sent a clear message to General Motors and Powertrain executives about the importance of the Bay City plant to our community. Additionally, the City has partnered with our state legislators (Senator Barcia and Representative Mayes), Bay County representatives, Bay Future and the Bay Area Chamber of Commerce to discuss additional ideas for retaining General Motors in our community.

Furthermore, the City Commission, at its March 2, 2009 meeting, approved membership in the Mayors & Municipalities Automotive Coalition, which joins other automotive communities in lobbying the federal government for assistance to the Automotive Industry.

The federal government, through the Troubled Assets Relief Program, authorized \$700 billion to assist financial institutions and insurance companies in removing “toxic assets” from their balance sheets. These “toxic assets” have severely hampered the credit market and caused troubled financial institutions to merge with larger banks. Banks inability, due to unprecedented financial losses, to make loans have frozen investments, forced businesses into bankruptcy, and driven up municipal bond market costs.

The City of Bay City, through its staff and elected officials, are working very closely with U.S. Senator Levin, U.S. Senator Stabenow, and Congressman Kildee to capitalize on the various stimulus funds available for infrastructure projects, energy efficiency programs and housing initiatives. In fact, City staff at the request of our federal legislators, Governor’s office, and the Michigan Municipal League, prepared project lists for road, water, sewer, electric, City facilities, airport, and cemetery. Our stimulus project list totaled an estimated \$194,192,050. Additionally, the City provided several requests to our federal legislators for inclusion in the FY 2010 federal budget. These projects were submitted by our delegation as appropriation requests, which would provide federal funding above and beyond the stimulus package.

The United States Congress is also considering legislative proposals involving the Family Medical Leave Act, the Americans with Disabilities Act, and others that may potentially have an adverse impact on the City by extending the length of leave or expanding areas of coverage.

Even though the United States formally acknowledged it was experiencing a recession, the State of Michigan has been struggling for several years. In fact, since 2002 the State of Michigan has struggled with its own fiscal challenges and budgetary constraints. The State of Michigan currently has an unemployment rate of 12.8%.

According to Stateline.org:

... the Great Lakes State has lost jobs for six consecutive years, Michigan's longest run of workplace shrinkages since the Great Depression. Automakers are laying off tens of thousands. Pharmaceutical giant Pfizer is closing up shop in Ann Arbor and Kalamazoo. The state ranks among the top three in the country for home foreclosures and mortgage delinquencies.

"The main reason for the sluggish economy is that the Big Three automakers – General Motors, Ford and Daimler-Chrysler – are losing ground in the U.S. market," said Dana Johnson, Chief Economist for Comerica. "Indeed, the domestic automakers claimed 53.7 percent of the market in 2006, compared to 73.7 percent in 1993. In the last six years, Michigan's vehicle production dropped 27 percent, enough to account for 120,000 lost jobs.

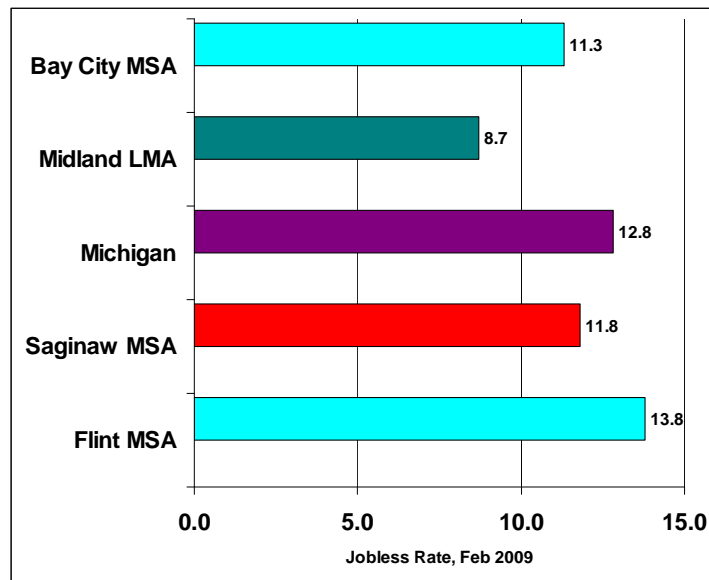
According to the Research Seminar in Quantitative Economics, at the University of Michigan,

The rainstorm that has been stationed over Michigan's economy for the past 8 years has now developed into a monsoon. From last October to this February the state has shed jobs at a rate of one percent a month, and we estimate that the first quarter of 2009 will come in at an annual rate of job loss just shy of 12 percent. The roots of the problem are evident: a national downturn that by our accounting will be the most severe of the post-war recessions; the domestic auto industry in a mess; and homebuilding activity operating at historic lows.

We are in for a rough ride for 2009 – a drop of 239,000 jobs during the year, the largest yearly decline since at least 1956. Although not a good year, 2010 will be a better one, with employment losses during the year dwindling to 12,500 and the economy holding its own by spring. This forward movement is predicated on a strengthening U.S. economy, a better functioning auto industry, and some pickup in local homebuilding.

According to the Bureau of Labor Market Information & Strategic Initiatives, of the Michigan Department of Labor, Energy, & Economic Growth,

In February, jobless rates for the three regional metropolitan areas declined moderately. ... The primary source of the unemployment reductions was worker recalls from temporary layoffs in the auto industry. Over the month, the Michigan jobless rate rose by 0.3 percentage points to 12.8 percent. Despite the monthly reduction, the Flint MSA jobless rate (13.8 percent) in February was one percentage point above the Michigan rate. Jobless rates for the Saginaw MSA (11.8 percent) and the Bay City MSA (11.3 percent) were below the state's rate.



The City of Bay City has been adversely impacted by the downturn of the Michigan economy, with reduction in state revenue sharing of \$1,219,775 since 2002, and a reduction of Act 51 revenue (Street Revenue) in the amount of \$102,827. Likewise, the City of Bay City has experienced 1,267 foreclosures since 2000, with 269 remaining vacant as of February 13, 2009.

According to Gerald J. Miller and James H. Svara in an article entitled Navigating the Fiscal Crisis: Tested Strategies for Local Leaders, *“The downturn in economic activity and rising unemployment reduce revenues and increase demands on social safety net.”*

The City has experienced increase demands on our social safety nets with increases in crime, increases in past due utility bills, and an increase in homelessness.

The financial crisis has forced the City of Bay City to reexamine its investment policy and practice. On March 30, 2009, Patti Fritz, City Treasurer, presented information to the City Commission on how the financial crisis required her, on behalf of the City of Bay City to modify her “SLY” principals of public fund investing. Ms. Fritz explained, her number one priority in this current financial crisis is “S” safety of our investment, she then evaluate its “L” liquidity and our ability to access funds when we need it. Finally, Ms. Fritz considers “Y” yield, which is the rate of return on our investments. Ms. Fritz explained that the investments currently held by the City of Bay City include government agencies; certificates of deposit, which is FDIC insured up to \$250,000/institution; certificates of deposits account registry service, which is insured by the FDIC up to \$50 million; money market, U.S. Treasury guaranteed program; and the 500 Index Fund (healthcare investment which mirrors investments made by Standard & Poors 500).

Ms. Fritz also explained actions she has taken to protect the principal of our investments by sweep access fund to governmental money market which are backed by the federal government; use of low interest “NOW” accounts 100% FDIC insured; safety number one priority over yield; and the purchase of CDARS for 100% FDIC insurance coverage. The City of Bay City currently invests \$56,556,912 of which \$55,750,317 is insured or guaranteed. By shifting our approach to safety over yield, our annual return on investment which is shown in various funds as interest earnings, has decreased significantly over the years.

The U.S. housing foreclosure crisis persists, and according to housing and banking experts, the foreclosure problem will become bigger. While the drivers of the crisis are complex, we know several things drawing on the assessment by Dr. Benton. J. Edwin Benton is a professor in the Department of Governmental and International Affairs at the University of South Florida. Dr. Benton wrote an article on Coping with Foreclosures.

First, the factors responsible for it predate and largely triggered the current economic downturn. Second, the recession likely will lead to another wave of foreclosures of a different nature and magnitude. Foreclosure began with subprime mortgages – those made to borrowers with a sketchy credit history or who provided limited documentation of their income or assets. The foreclosures now, contrary to similar past periods, are on higher-end properties, resulting in more severe bank losses. A third wave of foreclosures is likely to follow and conform to traditional patterns—those who live from paycheck to paycheck. The states with the highest foreclosure rates (in order of magnitude) are Nevada, Florida, Arizona, California, Colorado, Michigan, Ohio, and Georgia. These eight states along with eight others with rates over 1.5% account for almost four-fifths of all housing units in foreclosure in the country.

Ms. DeHaan-Legge, City Assessor, presented data to you at the January 12, 2009 Finance/Policy Committee meeting on the impact the housing crisis was having in Bay City. In fact, Ms. DeHaan-Legge reported that assessed values for 2008 declined .02% overall with personal property experiencing a .73% decrease, industrial with a slight increase of 2.19%, commercial properties experiencing a 0.12% decrease and residential experiencing a 0.06% percent decrease.

Ms. DeHaan-Legge explained that taxable values for 2008 increased overall 1.22% with personal property decreasing 1.62%, industrial increasing at 2.37%, commercial property increasing at 0.94% and residential property at 1.80%. The City of Bay City has experienced a decline in annual residential sales from a high of 779 sales in 2003 to a low of 545 sales in 2008, with average sale prices fluctuating widely with a high of \$88,696 (2006) to a low of \$69,514 (1999). The average sale price in 2008 was \$74,206. The City also has experienced an increase in foreclosures with a low of 46 in 2000 to a high of 243 foreclosures in 2008. Overall, we have experienced 1,267 foreclosures between 2000 and 2008.

Ms. DeHaan-Legge predicts the CPI changes, which affect the rate in which taxable values increase to be only 1.2% in 2010, 1.7% in 2011, 2.9% in 2012, and 3.1% in 2013. This slow rebound from the housing crisis demonstrates the fiscal constraint placed on property taxes which is an important revenue stream for both the General Fund and the Street Fund.

As a result of the housing market crisis, the City of Bay City millage rate will remain unchanged, with the exception of that portion of our levy dedicated to retiring the 1991 \$10.6 million Street Improvement Bond (Debt Sinking Fund). The Debt Sinking fund levy varies based on our annual payment of principal and interest. For the past several years as well as for FY 2010, the Debt Service Sinking Fund levy will remain unchanged.

The Wall Street Journal, April 15, 2009 edition contained a front page article entitled "*Banks Ramp Up Foreclosures.*" The article reported that J.P. Morgan, Chase & Co., Wells Fargo & Co., Fannie May and Freddie Mac were lifting their internal moratoriums or state imposed moratoriums on foreclosure efforts.

According to Dr. Benton, *When foreclosures are concentrated, property assessments decrease, and local governments' property tax collections are reduced. Sales taxes have slumped in part due to lower consumer spending brought on by the heavy debt load households assumed with home equity loans and second mortgages.*

The City of Bay City has felt the effects of the housing market crisis and subsequent foreclosures. This year's March Board of Review experienced a 14% increase in petitions requesting relief in property valuations. To relieve some of this increased pressure, the City Assessor offered for the first time an "Assessor Review." An "Assessor Review" allowed concerned tax payers to better understand what was driving the change to their assessed values and/or taxable values; and to hear their specific issues which could have resulted in an immediate adjustment to their assessment/taxable value and re-issuance of an assessment notice without the need of the Board of Review intervention.

Dr. Benton further states: On the spending side, foreclosed properties often result in public health issues, crime, and other social problems. State and local governments rely on borrowing in the municipal bond market to finance all sorts of capital projects. This market has been severely disrupted by the financial crisis, which leads to a disruption in capital financing and substantial increase in borrowing cost.

The FY 2010 budget includes proposed bond issues for water, sewer and streets (TIFA). Warren Creamer of R. W. Baird Inc., the City's financial advisor, indicates that the credit market is thawing, which will possibly result in lower costs of issuing new debt.

The financial crisis also hit public pension plans hard. At the end of the third quarter of 2007, state and local pension plans collectively held assets worth \$3.26 trillion, but the value of assets dropped to \$2.75 trillion by the end of the third quarter in 2008. How will this loss affect state and local government pension contributions? Two factors make the impact somewhat difficult to predict. First, pension contributions depend on how the stock market performs over the next six months, since most pension plans' fiscal year ends on June 30. Given the volatility in the current market, it is difficult to tell. The second factor is the smoothing technique used by pension plans in valuing assets. To avoid the volatility in asset value, plans use a multi-year smoothing technique to phase in asset gains or losses.

Pension Funds

At its annual meeting on March 10, 2009, the Bay City Police & Fire Retirement Board of Trustees received its actuarial valuation as of June 30, 2008 prepared by Sandra Rodwan of Rodwan Consulting. The actual valuation as of June 30, 2008 maintained the percentages of employer contributions required for fiscal year beginning July 1, 2009 (FY 2010). The employer contributions as a percentage of payroll for police patrol is 20.41%, for police command is 26.05%, and for fire is 31.88%. The City of Bay City Police & Fire Retirement System

funding level is at 80.1%. As of June 30, 2007, the Police & Fire Retirement System had a total market value of assets of \$55,490,980. As of June 30, 2008, the total market value of the assets decreased to \$50,263,830.

According to Ms. Rodwan, the overall experience of the retirement system during the year ended June 30, 2008 was more favorable than expected. The recognized rate of investment return on this smooth funding value of assets was the primary source of favorable experience 8.19% versus 7.5% assumed.

Ms. Rodwan further states, the overall funded condition of the retirement system improved during the year ending June 30, 2008. Continued improvement is dependent upon receipt of recommended employer contributions and the actual experience emerging in the future. The City of Bay City Police & Fire Retirement System utilizes a five year smoothing method. According to Ms. Rodwan, this method spreads market value gains and losses over five years. This method is unchanged from prior valuations. Because of the five year smoothing of valuations, the City will experience losses incurred in previous years and will not fully reap the benefits of any gains that have been made in current years until such time earlier losses are no longer calculated as part of the five year valuation.

The City of Bay City is also a member of the Municipal Employees Retirement System of Michigan (MERS) for its Defined Benefit Program which was discontinued in 1999. The City currently offers any employee hired after 1997 a Defined Contribution Program. MERS has reported a market valuation decrease of over 21%.

Highlights of the FY 2010 City Budget

General Fund

State Revenue Sharing – The 2010 budget reflects a slight decrease in state revenue sharing. The Michigan Department of Treasury continuously modifies their estimates based on the most accurate data available. As such, City staff relies on this information to establish revenue projections for FY 2010. With the economic downturn, State Revenue Sharing, which is reflective of actual sales tax captured, will be impacted by individual spending habits.

Reimbursement – Other Fund – this line item represents reimbursement from other funds through the Cost Allocation Plan. This amount represents services provided by Central Services (i.e. payroll/payables) to other funds for the period of July 1, 2007 to June 30, 2008.

Property Taxes – the City's General Fund largest revenue source reflects a decrease of .3% over 2009 budget. Also, industrial facilities tax/commercial facilities tax (IFT/CFT) decreased by 52% over 2009 because of existing tax abatements expiring. Typically, as tax abatements expire, value of personal property is transferred to the Ad valorem tax roll and reflected in property taxes. However, the City experienced a reduction in this transfer of IFT/CFT to property taxes because area businesses (i.e. General Motors) are idling their equipment, which is assessed at a lower value.

Payment In Lieu of Taxes – the City's General Fund fourth largest revenue source is the charge to utilities based on 4% of revenues and reflects a slight increase over FY 2009. Of course, the amount actually paid under the PILOT is based on audited financials at the end of the prior fiscal year.

Safe Streets Task Force – this line item reflects the FBI's reimbursement of the City's Police Department overtime associated with the Safe Streets Task Force, which was detailed in the Memorandum of Understanding dated March 29, 2007.

Fire Department Revenue – Reimbursement – Cost Recovery includes estimated revenues anticipated under the City's Cost Recovery Ordinance which was adopted on January 26, 2009. The primary revenue source is the \$500 charge to property owners' insurance for fire fighting services.

Economic Development Revenue – By-Ways Grant – Federal. This line item reflects grant proceeds awarded through the City for the Center Avenue Neighborhood Association. The City will receive \$71,600 in grant proceeds to implement a community-wide directional signage program, which is part of a total multi-year grant award of \$125,200.

Parks Department Revenue – State grants reflect proceeds from the Michigan Department of Natural Resources Trust Fund for Wenonah Park renovations Phase I and anticipated funding for improvements to Birney Park. At its March 16, 2009 meeting, the City Commission approved submittal of a grant application for Birney Park in the amount of \$146,000. Bay Area Housing, Inc. received a Michigan State Housing Development Authority grant, which is being used as the City's local share and leverage for this Michigan Department of Natural Resources Trust Fund Grant.

City Clerk Activity (101- 2150) includes \$22,248 for a part-time Special Events Coordinator whose responsibility will be processing special events applications and coordinating the City's review and services. Currently, the City Manager's office handles special event applications as one of many tasks undertaken. A part-time Special Events Coordinator will focus on enhancing our services especially with community pursuit of potential film industry opportunities. This

position would be funded, in part, by revenues generated from the Cass Avenue MetroPCS cell tower agreement. The agreement requires an initial fee of \$21,600.

City Hall & Grounds Professional Services – includes \$9,850 to install interior and exterior cameras. The cameras would increase security. The City of Bay City Police Department had assessed the current security features of City Hall and the Commission Chambers. The report recommends the installation of both an internal and external camera system as a means of reducing or preventing crime.

Police Support – Salary and Wages reflects a reduction due to the elimination of a clerical position. This position became vacant when the employee transferred to the Water Treatment Plant.

Post Employment Benefits – Retirement Paid MERS – the additional payment the City is making to reduce its MERS Defined Benefit unfunded liability, which was \$25.6 million as of December 31, 2005. This year's budget reduces our "additional" contribution by 50% because of the under performance of the markets. In fact, MERS reported their fund lost 21%. As such, the City is contributing an additional 2.5% of its General Fund allocation to the unfunded liability.

Post Employment Benefits – Hospitalization Retiree – this line item represents the City's obligations under GASB-45 Other Post Employee Benefits for retiree health care. The FY 2010 budget recommends a contribution of four percent (4%) of payroll to the City HealthCare Trust Fund. This four percent (4%) is a slight reduction of .25% from previous years.

Major Streets

State Grants – State Highway Maintenance – this line item represents the City's receipt of Act 51 Funds (Motor Vehicle Fuel Tax). The FY 2010 budget reflects a decrease in Act 51 funding. Act 51 funding is the primary funding source to maintain City Major Streets.

Engineering – Professional Services includes funding for Harrison Street Reconstruction Project, the Marquette Connector Reconstruction Project, and four (4) stimulus related road projects. Three of these road projects are for funding of engineers' designs to position the City for successful pursuit of future stimulus funding rounds. These three road projects include Johnson Street (Center Avenue to 11th Street); Trumbull Avenue (Center Avenue to Woodside Avenue); and Lincoln Street (22nd Street to Fremont Street). The fourth project involves joint repair on Truman Parkway intersection at Woodside.

Land Improvements include funding for Harrison Street; Marquette Connector, Center Avenue, and Truman Parkway joint repairs along with a possible future stimulus project.

Surface Maintenance and Improvements line item includes \$120,000 for LED traffic signal lighting. City staff is recommending that all the City's traffic signals be converted to LED lights for greater efficiency and reduced costs.

Local Streets – Revenue – Transfer from CDBG. This line item includes funding for local streets projects. As part of the federal stimulus package, the City of Bay City will be the recipient of approximately \$380,000 through the Community Development Block Grant R Program. The Community Development Block Grant "R" (Recovery) Program is a separate, one-time allocation of CDBG dollars within the American Recovery and Reinvestment Act of 2009. City staff is recommending that the allocation of the CDBG R program be dedicated to local street projects.

City Loans and Collections (Fund 223) is a new fund created to represent costs associated with pursuing outstanding loans under the previous POWER Fund Loan Program. This cost center includes attorney fees and fund balance reserve.

Solid Waste Fund

Solid Waste Management – Solid Waste – Revenue, Trash and Recycling Fee. The monthly trash fee remained unchanged; even though, the City Commission has approved a multi-year rate structure to address cost increases associated with our solid waste and recycling contracts. City staff had identified that those cost increases would result in a \$1.63/month increase by fiscal year 2012. However, City staff believes the Solid Waste Management Fund has sufficient revenues to avoid this year's scheduled increase. Also, the statewide tipping fee increase does not appear to be progressing.

The total Solid Waste, Trash Recycling Fee revenues for FY 2010 reflect a decrease due to a reduction of customers receiving service from the City of Bay City.

CDBG Fund

Community Development Block Grant includes the funding for the Woman's Center Rehabilitation, emergency home repair, low income sidewalks, 6th Ward Sidewalk Replacement Program, the City's Rehabilitation Program, demolition of unsafe structures, Bay Area Housing Development Corporation Housing

Rehabilitation, Mid-Michigan Dental Program, free Medical Clinic sponsored by Bay Regional Medical Center, Good Samaritan Rescue Mission, foreclosure prevention, other rehabilitation projects, Disability Resource Service Center, street tree planting, and various transfers to Major Streets, Local Streets, and Housing Rehabilitation Fund. Additionally, there is an allocation to the Fair Housing Council and administration of the CDBG Program as well as transfers to Fire Awareness and Community Policing.

Public Improvement Fund

Public Improvement Fund includes funding for the replacement of the City Hall Roof. The General Fund is being asked to transfer from the General Fund fund balance additional dollars needed to fund this project. The General Fund fund balance currently has \$1.3 million above the City-Commission established 15% reserve. I am proposing utilizing approximately \$500,000 of this excess General Fund fund balance to complete the replacement of the City Hall roof, and stimulate our local economy by contracting the project sooner than later..

According to Dr. Justin Marlowe, Assistant Professor in the Department of Public Administration at the University of Kansas, in the Navigating the Fiscal Crisis: Tested Strategies for Local Leaders, *“Leaders can mildly stimulate their local economies with several strategies: 1) increasing revenues or drawing down financial reserves to maintain or increase local government expenditures; and 2) expanding or accelerating local capital projects.”*

Building Inspection Fund

Building Inspection Department (Fund 249) reflects the reduction of one inspector. After having discussed the Building Inspection/Code Enforcement Department with Mr. Galford, I believe that the City is able to maintain adequate coverage to inspect rental units and building permits/property maintenance complaints with three code inspectors. Currently, the City has three code inspectors and one Code Official, who also inspects. Additionally, the City currently contracts with SCMCCI for inspection services in connection for electrical, mechanical, and plumbing permits.

The Mayor and City Commission have fully embraced the idea of neighborhood improvements through a targeted enforcement program and various incentives. To maintain quality neighborhoods, the City needs to be adequately staffed to enforce its current ordinances and encourage property maintenance/housing improvements.

Midland Street TIFA Fund

Midland Street TIFA #2 includes the design for reconstruction of Walnut Street between Vermont Street and Veteran's Memorial Bridge and reconstruction of Midland Street between Vermont and Dean Streets.

Marquette District TIFA Fund

The Marquette District TIFA #5 includes several projects under Land Improvements. The projects are Wilder Road drainage improvement in conjunction with the road commission's Wilder Road reconstruction project, signage replacement within the Marquette Industrial Center, and repairs to the Truman Parkway median.

Water Street DDA Fund

Water Street DDA #6 Land Improvements includes the Wenonah Park Redevelopment Project, Public Improvement-Wayfinding Signs, Streetscape Improvements along Washington Avenue between Second and Third Streets, and alley improvements within the district. The Downtown Development Authority Board of Directors maintains a cost sharing policy to assist district businesses who wish to improve their alley.

Economic Opportunities Fund

Economic Opportunities Fund includes in Land Improvements funding for the physical improvements to 1900 Broadway (roof, parapet, skylights, tuck pointing) to preserve the building. The City is talking with various developers who have expressed interest in acquiring the building from the City and renovating it for future use.

James Clements Airport Fund

Land Improvements includes monies for the construction of the sea plane improvement and design taxiway rehabilitation/reconstruction, and hangar taxi street rehabilitation project.

Electric Fund

The fiscal year 2010 Electric budget reflects no rate increase. However; there will be an Energy Efficiency Surcharge placed on customer bills. The rate surcharge will support the cost of the energy efficiency program.

As you may recall, Public Act 295 of 2008 requires all electric utilities in the State of Michigan to purchase 10% of their retail sales from renewable sources by 2015. The City of Bay City in partnership with the Michigan Public Power Association, entered into a contract with Granger to purchase power generated from methane gas, a by-product of Granger solid waste landfills. Specific projects under this contract are not expected to come on-line before the second half of 2010 and therefore will not affect the fiscal year 2010 budget. The contract stipulates the base cost at \$76.88/MWh plus project specific transmission and miscellaneous costs.

Additionally, Public Act 295 requires all electric utilities to reduce purchase power through energy efficiency programs. The City of Bay City in partnership with the Michigan Public Power Association, submitted its Energy Efficiency Plan to the Michigan Public Service Commission on May 31, 2009. This plan calls for the City to show energy savings programs based on a percentage of customer sales beginning at 0.3 percent of 2007 kilowatt-hour sales in 2009 and stepping up to one percent (1%) of 2011 kilowatt-hour sales for 2012 and succeeding years. Energy savings programs must be targeted to residential, commercial and industrial customers' requirements and must set aside a specific amount to low income residential customer programs especially weatherization. Even though our renewable portfolio and energy efficiency programs have an initial cost increase to implement, we will reduce our reliance on electric purchase and thus reduce costs long term, as well as improve the environment.

The FY 2010 Electric Fund recommends the use of appropriated fund balance (retained earnings) to cover costs associated with the purchase and installation of automatic metering infrastructure which is supported by the Governor and the Michigan Department of Labor, Energy, and Economic Growth as a means of improving our delivery responsiveness and efficiencies. In fact, the featured speaker at the Bay Future Inc. annual meeting was Stanley "Skip" Pruss, the Director of the Department of Labor, Energy, and Economic Growth. Mr. Pruss stressed, in his "Michigan's New Energy Economy" presentation, the importance of advance metering infrastructure to position Michigan in taking advantage of the new energy economy.

The Electric Service Building Capital includes funding for a new storage facility on-site. With the proposed relocation of the 46 Kv electric transmission line and the reconstruction of its Saginaw Street Substation as part of the Uptown at RiversEdge Redevelopment Project, the former Sears Automotive Garage is scheduled for demolition. Currently, the electric and other City departments utilize this building for storage. Since the building will be demolished to facilitate the relocation of the Saginaw Street Substation and the Consumers Energy switching station, City staff is recommending a new storage facility at the electric yard on Water Street.

The Electric Fund also represents costs associated with replacement of street lights in connection with the Center Avenue Reconstruction Project with ornamental light and the Harrison Street Reconstruction Project, and system-wide maintenance. The Center Avenue street lighting project is primarily grant funded.

Sewer Fund

The Sewer Fund, like Water, has experienced a decrease in consumption. The decrease in consumption coupled with system-wide maintenance and improvements has caused rates to increase. As such, the sewer rates for FY 2010 are proposed to increase by 6.8%. This increase results in the following charges; readiness to serve charge of \$9.77/month; billing charge of \$2.83/month; and a commodity charge of \$7.52/ccf or 748 gallons used. An average 7 ccf/month user will pay a \$65.06/month, which is 9.3% or \$5.56/month increase over last year. Of the 6.8% rate increase, 1.6% is for increased costs of operations and maintenance of the sewer system, and the remaining increase in rates of 5.2% is due to adjustments required for changes in consumption.

The Sewer Fund includes sewer maintenance, cleaning and improvement through the following projects: sewer rehabilitation project assessment and design, rehabilitation project construction, Center Avenue sewer project, Farragut Street sewer replacement, Harrison Street sewer repair, Marquette connector street sewer improvement, and sewer replacement on Linn Street, Walnut Street, and Midland Street.

Within the Sewer Fund, sewer plant operation and maintenance equipment line item in the FY 2010 budget recommends the basin screw rehabilitation project, miscellaneous equipment purchases, basin #4 flush pump which will be funded from the equipment replacement fund – a fund that is required under our State Revolving Fund Loan regulations. The State Revolving Fund requires the City to set aside \$735,444 next year to ensure adequate funding for equipment maintenance and replacement. This amount is reflective of the annual equipment depreciation schedule.

Water Fund

The Water Fund budget for FY 2010 reflects a rate increase of \$.22 per ccf or a \$1.50 per month for the average customer (using 7 ccf per month). Overall the in-City rate increases from \$2.68 per ccf to \$2.90 per ccf. The out-City commodity rate is proposed to increase by \$.10 per ccf from \$1.96 to \$2.06.

The Water Fund revenue also reflects appropriate fund balance usage to cover costs associated with the implementation of the Automatic Metering Infrastructure Program, and pursuit of loan/bond proceeds for various water main replacement projects as part of either street reconstruction or system improvements.

Water Purification Activity includes money in the professional services account for the disposal of residuals from water treatment process. This is the first year the City will remove residuals and dispose of them on an annual basis. When the North Lagoon Reclamation and Reconstruction Project was planned, the project was designed to construct three separate containment cells within the lagoon proper. Each containment cell allowed the City to dispose of residuals, a byproduct of the softening/treatment process, allowing them to dry to where we could start disposing of them on an annual basis. In essence, one cell would be full while the City was filling a subsequent cell, the first cell had ample time to dewater leaving the remaining solids to be removed and disposed. This methodology would prevent the need to fund a major reclamation and disposal project.

The Water Purification activity also includes equipment, upgrades or purchases, for the plant. These projects include the CO2 feed system, re-roofing the Water Treatment Plant in phases, and the phosphate feed system.

Information Systems Fund

Information Systems Budget (636) includes the purchase of a virtualization server which would better utilize the various servers in place throughout the City even at remote locations for enhanced storage capacity and speed/reliability.

Motor Equipment Revolving Fund

Motor Equipment Revolving Fund –MERF budget - (661) includes monies within the capital account for improvements to the building such as window replacement, door replacement, HVAC and other energy efficiency improvements. MERF also includes a list of vehicles and equipment scheduled for replacement during FY 2010.

Healthcare Fund

Healthcare Fund (683) includes the costs associated with attorney fees in a law suit against Blue Cross/Blue Shield for overcharges of access fees and an actuarial report required by GASB-45 for our other post employment benefits (OPEB) (i.e. retiree health care) obligations .

Additionally, the fiscal year 2010 budget proposes a four percent (4%) of payroll contribution to the Other Post Employment Benefit obligation (retiree healthcare), which as of December 31, 2006 actuarial valuation had an unfunded liability of approximately \$123 million. The FY 2010 budget also recommends a transition in healthcare administration for post 65 retirees from a fully funded Blue Cross/Blue Shield policy to a fully funded NEBCO/Willis policy. The NEBCO policy will cover the “gap” in coverage provided under Medicare. Under our collective bargaining agreements, post 65 retirees are covered by the Medicare Part A, B, and D Programs, which covers 80% of medical related expenses and prescription drug coverage. The NEBCO program covers the twenty percent gap. This new third party administrator will save the City approximately \$728,000 per year.

What does this all mean?

In conclusion, City staff was successful in preparing a balanced budget totaling \$137,197,773. The FY 2010 budget does not incorporate the 1% tax administrative fee proposal submitted to you by City Treasurer Fritz. The FY 2010 budget does reflect a \$.22/ccf increase for City water customers, a \$5.56/month for the average sewer customer, and an electric surcharge to implement its energy efficiency programs. The FY 2010 budget reflects healthcare savings of approximately \$728,000 incorporating a change in the third party administration from Blue Cross/Blue Shield to NEBCO/Willis, for post 65 retirees and post 65 eligible dependents.

The FY 2010 budget reflects \$22,347,265 in capital improvements for all City funds. FY 2010 budget does not reflect any rate increase or compensation adjustments except those currently under contract. City staff will be renegotiating collective bargaining agreements with seven of its eight unions and discussing possible changes to wages and health care coverage for the eighth unit which currently has a “reopener clause” in its contract.

The FY 2010 budget reflects the creation of a part-time position in the City Clerk’s Office to coordinate, process, and ensure better services for the City’s special events; elimination of a vacant clerical position in the Police Department; the layoff of an inspector in the Building Fund; and the creation of an Assistant Director for the Electric Department. I firmly believe the position scheduled to be laid off in the Building Fund may be absorbed in the City’s organization through transitions caused by retirement or separations from employment in other departments.

The FY 2010 budget reflects the challenges encountered as a result of financial markets, housing crises, and the overall recession. The City has lost revenue sharing, Act 51 revenue, and likewise experienced a decrease in interest

earnings. The City has been active in pursuing federal and state grant opportunities such as the By-Ways Grant and the Department of Natural Resources Trust Fund Grant, and Seaplane Improvement Grant for James Clements Airport. The City stands to receive stimulus funding for road projects. The FY 2010 budget includes monies for engineering design on additional road projects for future rounds under the stimulus plan. Additionally, the City's Community Development Block Grant Program is eligible for stimulus funding under CDBG R Program, the Homeless Prevention and Rapid ReHousing Program, and the CDBG Neighborhood Stabilization Program. The City submitted an application to the Michigan State Housing and Development Authority (MSHDA).

Finally, the FY 2010 budget continues to carry out the City's Vision, Mission and approved City Manager goals for FY 2008/2009. The City has been operating with five goals categories, which includes:

- Category Economic – to continue to improve the City's economic vitality and quality of life;
- Category Finance – to maintain financial stability of all City Funds while minimizing adverse impact on tax payers and rate payers;
- Category Infrastructure – to maintain or replace our infrastructure utilizing preventative maintenance techniques and long-range planning;
- Category Community Development – to share relevant information with all stakeholders; and
- Category Employee Relations – to improve employee relations through targeted program efforts and recognition efforts.

A copy of the City Manager's goals for fiscal year 2008/2009 as approved by the Mayor and City Commission at the December 15, 2008 regularly scheduled City Commission meeting, is included in this budget document.

The City of Bay City is faced with mounting unfunded liabilities and a rapidly deteriorating infrastructure. To address these issues, the fiscal year 2010 budget maintains a respectable contribution to our unfunded liabilities with a reduction from the additional 10% contribution to a 5% contribution (except for the General Fund and Street Fund which was reduced from 5% to 2.5%) for the Michigan Employees Retirement System (MERS) Defined Benefit unfunded liability, which in 2005 was approximately \$25.6 million.

With regards to the infrastructure, the City needs to invest greater resources at a more rapid pace to address the conditions of our streets, sewer collection system, and water treatment and distribution systems. This may require the City placing a question on an upcoming ballot to levy millage in support of an infrastructure bond issue similar to one past in 1991 for \$10.6 million and is the

current basis of our debt service sinking fund levy of approximately 2.5888 mills annually. The City of Bay City is not in a position to continue to ignore the conditions of our streets and water and sewer utility infrastructure. City staff has increased their maintenance efforts, but will be unable to reverse the current trend without significant investment.

I would like to thank all City employees who participated in this year's budget process. I would especially like to thank Cathy Szostak and her staff for their continued attention to detail; and Debbie Buck and Melody Roth for preparing and assembling the budget document. I am pleased to present this balanced budget for FY 2010. I look forward to our review and discussion of the initiatives, projects, and programs incorporated in this budget.

Sincerely,

Robert V. Belleman
City Manager

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