

2018-2019

ANNUAL

REPORT

TRANSMITTAL

MEMORANDUM

Memorandum

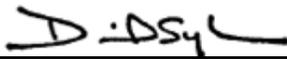
TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Jim Shannon

SUBJECT: 2018-2019 ANNUAL REPORT

DATE: September 30, 2019

Approved



Date

09/30/2019

RECOMMENDATION

It is recommended that the City Council:

- (a) Accept the 2018-2019 City Manager's Annual Report in compliance with City Charter Section 701 (F).
- (b) Adopt Appropriation Ordinance and Funding Sources Resolution amendments in various operating and capital funds to implement the 2018-2019 Annual Report recommendations, as detailed in Section IV (Recommended Budget Adjustments and Clean-Up/Rebudget Actions).
- (c) Approve the following position changes in the Information Technology Department:
 - (1) Add 6.0 Enterprise Supervising Technology Analyst.
- (d) Approve the following technical position corrections in the Parks, Recreation and Neighborhood Services Department to align with the 2019-2020 Adopted Budget:
 - (1) Add 2.75 Recreation Leader PT;
 - (2) Delete 1.0 Senior Geographic Information Systems Specialist;
 - (3) Delete 1.0 Senior Maintenance Worker;
 - (4) Delete 1.0 Parks Maintenance Repair Worker II;
 - (5) Delete 1.0 Office Specialist II;
 - (6) Delete 2.0 Maintenance Assistant; and
 - (7) Delete 2.0 Groundswoker.

OUTCOME

In accordance with Section 701 (F) of the San José City Charter, the 2018-2019 Annual Report describes the financial status of the City at the end of the 2018-2019 fiscal year. As specified in the City Charter, the focus of the City Manager's Annual Report is a comparison of actual revenue collections and expenditures to projections and appropriations included in the City's budget.

OUTCOME

The 2018-2019 Annual Report will provide the City Council with the information necessary to review the financial performance of all City funds. In addition, this report provides a comparison of the actual 2018-2019 Ending Fund Balance for each fund to the estimates used in the development of the 2019-2020 Adopted Budget as well as information on the status of the year-end reserve levels for each of the City's budgeted funds.

Approval of the recommended budget actions will implement required fund balance reconciliations and necessary rebudget and clean-up adjustments based on the final financial performance (unaudited) for 2018-2019. This report also includes actions that are necessary to: revise the 2019-2020 budget to align budgeted revenue and expenditures with the most current information; correct technical problems; recognize new or adjust existing grant, reimbursement, or fee activity revenues and expenditures; fund four urgent fiscal/program needs in the General Fund; reflect changes in project and program allocations based on revised cost estimates; and establish a limited number of new projects and programs in special and capital funds.

EXECUTIVE SUMMARY

The Administration proactively managed 120 budgeted funds in 2018-2019. Budget actions were brought forward during the year to ensure that revenues and expenditures remained in alignment with actual performance. Through this careful management, the various City funds generally ended the year with revenues close to the budgeted estimates and expenditures below the budgeted allocations.

With the local economy's sustained growth over the past several years, the City's budget again remained stable. Accordingly, the 2018-2019 Adopted Budget maintained and, in limited instances, enhanced existing service levels in alignment with direction provided in the City Council-approved Mayor's March and June Budget Messages for Fiscal Year 2018-2019 in the following areas: Homelessness and Housing, Public Safety, Environment, Innovation and Technology, Education and Our Youth, Community Engagement, and Saving and Improving Fiscal Sustainability. A small number of investments targeted improvements in City infrastructure, and the City continued its adherence to a multi-year approach to budgeting with one-time funding set aside in 2018-2019 to address a projected General Fund shortfall in 2019-2020. As always, the City will maintain its focus on rebuilding services within available resources to meet the needs of the San José community.

In the General Fund, both the revenues and expenditures ended the year very close to budgeted expectations. The 2018-2019 General Fund Ending Fund Balance of \$364.8 million exceeded the estimate of \$289.4 million used in the development of the 2019-2020 Adopted Budget by \$75.4 million. This variance represents 2.3% of the 2018-2019 Modified Budget total sources and uses. These funds are recommended to be allocated in the 2018-2019 Annual Report, as shown in the table on the following page.

EXECUTIVE SUMMARY

Recommended 2019-2020 General Fund Adjustments (\$000s)

Additional 2018-2019 Ending Fund Balance	\$75,387
Clean-Up Actions	
Development Fee Programs Reconciliation	(12,191)
Fire Training Center Replacement Reserve Rebudget	(36,835)
Other Rebudgets/Clean-Up Adjustments	1,032
Total Clean-Up Actions	(\$47,994)
Fund Balance Available After Clean-up Actions	\$27,393
Recommended Budget Adjustments	
Required Technical/Rebalancing Actions	(10,624)
Grants/Reimbursements/Fee Activities (Sources = \$3.6M; Uses = \$2.8M)	781
Urgent Fiscal/Program Needs	(7,550)
Total Recommended Budget Adjustments	(\$17,393)
Remaining Fund Balance After Clean-ups/Recommended Adjustments	\$10,000
Distribution of Remaining Fund Balance Per City Council Policy I-18	
Budget Stabilization Reserve	(\$5,000)
Unmet/Deferred Infrastructure: City Facilities Emergency Power Generation	(\$5,000)
Total Fund Balance Distributed Per Council Policy I-18	(\$10,000)

When bringing forward recommendations for the use of the additional 2018-2019 General Fund Ending Fund Balance, the Administration follows City Council policy and first considers clean-up actions associated with the close-out of the 2018-2019 fiscal year to be essentially non-discretionary and the highest priority. These clean-up actions result in a net decrease to the available fund balance of \$48.0 million and consist of changes to the Development Fee Programs reserves to reconcile actual 2018-2019 performance (decrease to fund balance of \$12.2 million); the rebudgeting of the Fire Training Center Replacement Reserve that was established June 18, 2019, subsequent to the City's receipt of sale proceeds of the existing Fire Training Center site (\$36.8 million); and the rebudgeting of other amounts carried over to 2019-2020 to complete projects and technical adjustments to other revenue and expenditure line items (net increase to fund balance of \$1.0 million).

The remaining fund balance of \$27.4 million is recommended to fund various required technical and rebalancing actions (\$10.6 million), actions associated with grant and fee activities (-\$781,000), and a limited number of urgent fiscal or programmatic needs of the City (\$7.6 million) that the Administration has deemed cannot or should not wait until the Annual Budget process. Notable adjustments in these categories include: an increase of \$4.0 million to the General Liability Claims appropriation based on an analysis of current and potential litigation settlements and claims awards against the City; an allocation of \$3.6 million to the Police Department for overtime and vehicle purchases to support the Guardian Rapid Response Program that enhances the City's ability to swiftly and effectively respond to active shooter incidents at schools and special events;

EXECUTIVE SUMMARY

an increase to the Transfer to the Municipal Golf Course Fund of \$2.3 million to accelerate the pay down of outstanding debt related to the Los Lagos golf course; as directed by City Council's approval of the Mayor's June Budget Message for Fiscal Year 2019-2020, an investment of \$1.9 million for Information Technology project managers and contractual support to implement the backlog of impactful technology projects throughout the City; and \$1.5 million to help operationalize Pillar 3 of the Community Plan to End Homelessness that focuses on improving quality of life for unsheltered individuals and creating healthy neighborhoods for all.

After these adjustments, the remaining fund balance of \$10.0 million is recommended to be distributed in accordance with City Council Policy I-18. These funds are recommended to increase the Budget Stabilization Reserve (\$5.0 million) from \$27.0 million to \$32.0 million to maintain a baseline level for General Purpose Reserves at 6.5% of General Fund operating expenditures, and support unmet/deferred infrastructure needs by allocating funds for City Facilities Emergency Generation (\$5.0 million). The recommended budget actions are summarized later in this message and described in *Section IV: Recommended Budget Adjustments and Clean-Up/Rebudget Actions*.

This report also addresses immediate needs in various special and capital funds, including procuring back-up generation equipment for five sanitary sewer pump stations and a fueling island; investments in pedestrian, bicycle and roadway safety improvements, including the Better Bikeways Program; allocating additional resources to strategize and prepare for the pre-cursor projects leading up to the next stage of development at the Airport; actions to allocate Public Art and program administration funding within the Measure T bond program; and reallocating funding within the Parks Flood Remediation Program to address updated project costs.

As the fiscal year progresses, the Administration will continue to monitor and report on the City's financial performance through Bi-Monthly Financial Reports that are agendaized four times a year for review by the Public Safety and Strategic Support City Council Committee, and the Mid-Year Budget Review that is heard by the full City Council in February. The financial results of 2018-2019 will also be factored into the development of the 2021-2025 General Fund Five-Year Forecast that will be released in February 2020.

BACKGROUND

Each year the City issues the Annual Report at the end of September, three months after the close of the fiscal year, as required by the City Charter. Following is a description of the various sections of the Annual Report document.

- **Transmittal Memorandum** – This section provides an overall summary of the 2018-2019 Annual Report.

BACKGROUND

- **Section I: Budget Performance Summary (All Funds)** – This section provides a comparison of the 2018-2019 budget to actual revenues received and expenditures incurred by fund as well as an explanation of revenue and/or expenditure variances of 10% or greater to the budget. This section also provides a comparison of the year-end actual 2018-2019 Ending Fund Balance by fund to the 2018-2019 Ending Fund Balance/2019-2020 Beginning Fund Balance estimate used in the development of the 2019-2020 Adopted Budget. In addition, a listing of the Earmarked and Contingency Reserves that were available at the end of 2018-2019 by fund is included.
- **Section II: General Fund Budget Performance** – This section provides a summary of the General Fund budget performance in 2018-2019, including the following: Results of Operations in the General Fund, Revenue Performance, and Expenditure Performance.
- **Section III: Selected Special/Capital Funds Budget Performance** – This section provides financial information on the 2018-2019 year-end performance for selected special and capital funds that represent major City operations. It includes a discussion of variances between actual and budgeted revenues and expenditures as well as a comparison between the actual ending fund balance and the fund balance estimated for 2018-2019 in the development of the 2019-2020 Adopted Budget.
- **Section IV: Recommended Budget Adjustments and Clean-Up/Rebudget Actions** – This section provides a description of the recommended budget adjustments and clean-up actions for City Council consideration. The proposed actions fall into three categories: (1) adjustments to the 2019-2020 Beginning Fund Balance amounts in various funds, including the General Fund, based on the final reconciliation of 2018-2019; (2) upward and downward adjustments to previously rebudgeted sums to ensure the appropriate amount of unexpended funds are carried over to 2019-2020 to complete projects; and (3) actions based on more recent information that are necessary to revise the 2019-2020 budget to align budgeted revenue and expenditures with the most current information, correct technical problems, recognize new or adjust grant, reimbursement or fee activity revenues and expenditures, fund one-time urgent fiscal/program need in the General Fund, and reflect changes in project and program allocations based on revised cost estimates as well as establish a limited number of new projects and programs in special and capital funds.
- **Section V: Financial Statements** – This section provides the financial results (unaudited), prepared by the Finance Department, for all budgeted fund groups for 2018-2019. It should be noted that audited financial results will be released later in the fall as part of the 2019 Comprehensive Annual Financial Report (CAFR) for Fiscal Year Ended June 30, 2019. Final fund balance reconciliations to the CAFR will be conducted for all funds and, while few adjustments are typically necessary, any final adjustments will be brought forward for City Council consideration as part of the 2019-2020 Mid-Year Budget Review.

ANALYSIS

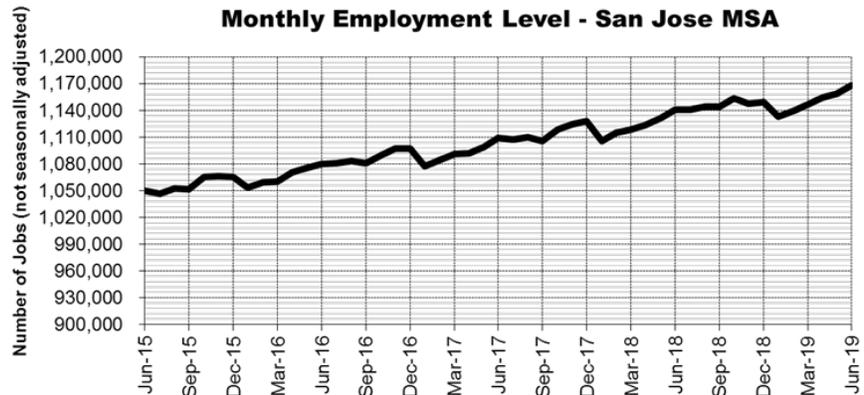
This Analysis section includes the following:

- an overview of the economic environment;
- a discussion of the 2018-2019 budget performance of all City funds;
- a discussion of the 2018-2019 budget performance for the General Fund;
- a discussion of the components of the 2018-2019 General Fund ending fund balance;
- an analysis of the impact of the General Fund performance on the 2019-2020 Adopted Budget; and
- a discussion of the 2018-2019 budget performance of selected special and capital funds.

Economic Environment

When the 2018-2019 Adopted Budget was developed, slow economic growth was expected to continue throughout the year. This assumption has proven true, with continued improvement in economic indicators and actual revenue performance during 2018-2019. Employment indicators, construction activity, median single-family home prices, and the number of days it took to sell these homes all performed well in 2018-2019.

The June 2019 employment level in the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (San José MSA) of 1.17 million was 2.4% higher than the June 2018 level of 1.14 million, representing an increase of 27,500 jobs. This includes 9,000 jobs in the information sector, 7,200



manufacturing jobs (primarily computer and electronic product manufacturing), 2,800 government jobs, 2,700 jobs in professional and business services, and 2,500 private education and health services jobs.¹

¹ State of California Employment Development Department Labor Market Information Division Press Release, July 19, 2019

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Economic Environment

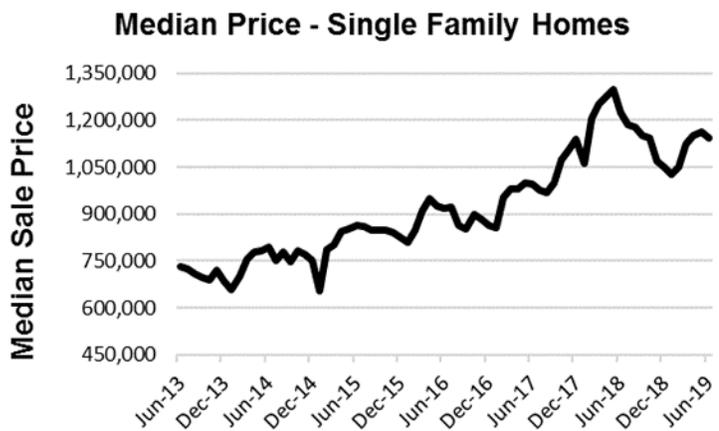
Unemployment Rate (Unadjusted)		
	June 2018	June 2019**
San José Metropolitan Statistical Area*	2.9%	2.7%
State of California	4.4%	4.1%
United States	4.2%	3.8%
* San Benito and Santa Clara Counties Source: California Employment Development Department. ** June 2019 estimates are preliminary and may be updated.		

The unemployment rates at the local, state, and national levels have all slightly decreased from the prior year. In June 2019, the unemployment rate for the San José Metropolitan Statistical Area of 2.7% is slightly higher than the 2.2% unemployment rate experienced in May 2019; however, it is marginally lower than the levels experienced in June 2018. In this region, the June 2019 unemployment rate continues to be lower than the unadjusted unemployment rate for the State (4.1%) and the nation (3.8%).

The total valuation of projects submitted in 2018-2019 was \$1.7 billion, 4.2% above the \$1.6 billion valuation of projects that were received in 2017-2018. The number of new residential dwelling units permits issued in 2018-2019 totaled 2,985, which was 7.9% below the prior year level of 3,241 permits issued. Residential valuation ended the year below the estimate while the valuations for the Commercial and Industrial land use categories ended the year above estimates.

Private construction activity is a driver for several development related taxes and fees and is an indicator of future activity for several other categories, such as storm and sanitary sewer system fees.

After seven years of year-over-year home price growth, the local real estate market is beginning to slow down. According to data from the Santa Clara County Association of Realtors, the single-family home price peaked at \$1.3 million in May 2018 (which represented a 30.0% increase from the May 2017 home price), but then began steadily decreasing. In addition, year-over-year median prices have steadily decreased each month since November 2018, with drops ranging from 3%-13% compared to the prior year level. In June 2019, the median single-family home price totaled \$1.1 million, which represents a 6.5% decrease from the June 2018 price of \$1.2 million, but is approximately 15% above the June 2017 price of \$996,000. In addition to the median home prices dropping, the number of property transfers (sales) has also continued to steadily decline. The total number of property transfers that occurred through June 2019 has dropped approximately 10%



ANALYSIS

Economic Environment

compared to the prior year. Lastly, while single-family and multi-family dwellings are continuing to sell quickly, they are on the market longer than the prior year. The average days-on-market for single-family and multi-family dwellings in June 2019 totaled 30 days, which is twice as long than the extremely low 15 days experienced in June 2018.

2018-2019 Budget Performance (All Funds)

As shown in Section I of this document, City revenues (excluding Beginning Fund Balances) totaled \$3.5 billion in 2018-2019, which was 2.6% (\$92.6 million) below the budgeted estimate of \$3.6 billion.

In 2018-2019, expenditures (excluding Reserves and Ending Fund Balances) totaled \$3.7 billion, which was \$613.1 million (14.3%) below the modified budget of \$4.3 billion. At the end of 2018-2019, the Contingency and Earmarked Reserves for all City funds totaled \$993.7 million, which represented 19.2% of the total 2018-2019 Modified Budget of \$5.2 billion (including interfund transfers, loans, and contributions). In the General Fund, Reserves totaled \$262.5 million.

The financial performance in 2018-2019 is used as the starting point for 2019-2020. The collective 2018-2019 Ending Fund Balances for all City funds totaled \$1.7 billion, which was \$182.9 million above the 2018-2019 Ending Fund Balance estimates of \$1.5 billion used in the development of the 2019-2020 Adopted Budget. After adjusting for additional rebudgets of \$54.3 million recommended in this report, the adjusted 2018-2019 Ending Fund Balance variance for all funds falls to \$128.7 million, or 2.5% of the 2018-2019 Modified Budget. The adjusted fund balance variance totaled \$27.4 million in the General Fund, \$30.2 million in the special funds, and \$71.1 million in the capital funds.

The City's General Fund ended the 2018-2019 fiscal year within budgeted levels. As shown in the chart below, the General Fund Ending Fund Balance of \$364.8 million was \$75.4 million (4.5% of the 2018-2019 Modified Budget total sources and uses) above the fund balance estimate assumed when the 2019-2020 Adopted Budget was developed. The following table summarizes the General Fund performance in 2018-2019, comparing the actual results to the modified budget and the estimates used to develop the 2019-2020 Adopted Budget.

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2018-2019 General Fund Budget Performance

**Table 1
 General Fund Year-End Status
 For the Year Ended June 30, 2019
 (\$000s)**

Sources	2018-2019 Modified Budget	2018-2018 Year-end Estimate	2018-2019. Budgetary Basis Actual	Actual to Budget Variance	Actual to Estimate Variance
<i>Beginning Fund Balance</i>	249,953	249,953	249,953	-	-
<i>Carryover Encumbrances</i>	35,250	35,250	35,250	-	-
<i>Liquidation of Carry- over Encumbrances</i>	-	3,306	3,217	3,217	(89)
<i>Revenue</i>	<u>1,385,490</u>	<u>1,390,489</u>	<u>1,394,877</u>	<u>9,387</u>	<u>4,388</u>
<i>Total Sources</i>	<u><u>1,670,693</u></u>	<u><u>1,678,998</u></u>	<u><u>1,683,297</u></u>	<u><u>12,604</u></u>	<u><u>4,299</u></u>
Uses					
<i>Expenditures/Transfers</i>	1,408,190	1,389,573	1,318,485	(89,705)	(71,088)
<i>Reserves</i>	<u>262,503</u>	-	-	<u>(262,503)</u>	-
<i>Total Uses</i>	<u><u>1,670,693</u></u>	<u><u>1,389,573</u></u>	<u><u>1,318,485</u></u>	<u><u>(352,208)</u></u>	<u><u>(71,088)</u></u>
<i>Ending Fund Balance</i>	<u><u>-</u></u>	<u><u>289,425</u></u>	<u><u>364,812</u></u>	<u><u>364,812</u></u>	<u><u>75,387</u></u>

Note: In the chart above, the General Fund excludes the Emergency Reserve Fund and the Cash Reserve Fund, which are budgeted as separate funds and reflected separately in this document. In the 2018-2019 Comprehensive Financial Report (CAFR), the Emergency Reserve Fund and Cash Reserve Fund will be displayed as part of the General Fund to comply with GASB 54 reporting requirements.

In 2018-2019, total revenue in the General Fund was \$1.3 billion, which was within 0.7%, or \$9.4 million, of the 2018-2019 Modified Budget, and \$4.4 million (0.3%) above the estimate used to develop the 2019-2020 Adopted Budget. The liquidation of prior year carryover encumbrances totaled \$3.2 million, which was slightly below the \$3.3 million estimate.

General Fund expenditures/transfers of \$1.3 billion were \$352.2 million (2.1%) below the 2018-2019 Modified Budget level of \$1.7 billion and \$71.1 million (5.0%) below the estimate used to develop the 2019-2020 Adopted Budget. Budgeted reserves of \$262.5 million remained unexpended at year-end as expected.

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2018-2019 General Fund Budget Performance

When comparing the actual revenue and expenditure performance to the estimates used to develop the 2019-2020 Adopted Budget, a portion of these variances is related to various grants and reimbursements that were not received in 2018-2019, but are expected to be received in 2019-2020. A total of \$4.2 million of grant and reimbursement revenues and expenditures were rebudgeted to 2019-2020 in the 2019-2020 Adopted Budget. This resulted in lower actual revenues and expenditures in 2018-2019, with no net impact to the General Fund. After factoring out the lower revenues and expenditures associated with these grants and reimbursements, revenues were \$8.6 million (0.6%) above the budgeted estimate and expenditures savings totaled \$66.9 million (4.0%). Further adjustments to these figures are necessary to account for the recommended clean-up and rebudget actions in the Annual Report.

In this Annual Report document, budget actions are recommended to distribute the additional fund balance of \$75.4 million. Per City Council Policy I-18, when determining the proposed distribution of these funds, the first priority is to complete clean-up actions associated with the final reconciliation of 2018-2019. Recommended clean-up actions result in net decrease of \$48.0 million to the amount of funding available to distribute to reflect reconciliation of the Development Fee Programs (\$12.2 million), the rebudgeting of the Fire Training Center Relocation Reserve (\$36.8 million) that was established June 18, 2019 only after sale proceeds were received by the City, and other required expenditure rebudgets and other clean-up adjustments to close-out 2018-2019 (net increase to fund balance of \$1.0 million). The adjusted figure of \$27.4 million in additional funding available to distribute was generated from net expenditure savings of \$16.1 million (0.9%) and higher than estimated revenues of \$11.3 million (0.7%), partially offset by a slightly lower than estimated liquidation of prior year encumbrances (-\$89,000).

Of the \$27.4 million available for distribution, \$17.4 million is recommended to be allocated to address various required technical and rebalancing actions (\$10.6 million) and urgent fiscal/program needs (\$7.6 million), with a net increase of \$781,000 resulting from actions related to grant reimbursements or fee program activity. The remaining balance of \$10.0 million is recommended to be allocated per City Council Policy I-18 to the Budget Stabilization Reserve (\$5.0 million) and to address unmet/deferred infrastructure needs by allocating funds for City Facilities Emergency Power Generation (\$5.0 million).

To identify revenue and expenditure trends, Table 2 below compares the City's budget performance in 2018-2019 with the budget performance of the prior year.

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2018-2019 General Fund Budget Performance

**Table 2
 General Fund
 Comparison of Year-End Actuals With Prior Year
 (\$000s)**

	2017-2018 Actuals	2018-2019 Actuals	Change	% Change
Source of Funds				
Beginning Fund Balance	241,173	249,953	8,780	3.6%
Revenues	1,297,251	1,394,877	97,626	7.5%
Total Source of Funds	1,538,424	1,644,830	106,406	6.9%
Use of Funds				
Personal Services	807,240	842,867	35,627	4.4%
Non-Personal/Equipment/Other	143,132	151,095	7,963	5.6%
City-Wide Expenses	305,844	240,080	(65,764)	-21.5%
Capital Contributions	47,457	36,611	(10,846)	-22.9%
Transfers	34,347	47,832	13,485	39.3%
Reserves	-	-	-	N/A
Total Use of Funds	1,338,020	1,318,485	(19,535)	-1.5%

As shown in Table 2, 2018-2019 General Fund revenues (excluding Beginning Fund Balance) of \$1.4 billion represent an increase of 7.5% from the 2017-2018 collection level of \$1.3 billion. The categories that experienced the largest increases included: Other Revenue, Sales Tax, Property Tax, Licenses and Permits, and Business Taxes. This increase was due to economic performance as well as other contributing factors such as the sale of multiple surplus properties (Fire Training Center, Coleman Avenue property, and seven previously owned SARA properties that the City received 14.14% of the sale price), and over-collection of Sales Tax due to processing issues experienced by the California Department of Tax and Fee Administration (CDTFA), which resulted in at least \$10 million of Sales Tax being received in 2018-2019 that was due to 2017-2018 activity. The largest revenue declines from the prior year were experienced in the Revenue from Local Agencies, Revenue from the Federal Government, and Franchise Fees categories.

General Fund expenditures of \$1.32 billion in 2018-2019 were 1.5% (\$19.5 million) below prior year expenditure levels of \$1.34 billion. This decrease is due to lower City-Wide Expenses (\$65.8 million) and Capital Contributions (\$10.8 million), partially offset by higher Personal Services (\$35.6 million), Transfers (\$13.5 million), and Non-Personal/Equipment/Other (\$8.0 million).

A detailed discussion of the General Fund revenue and expenditure performance is provided in Section I of this document.

ANALYSIS

2018-2019 General Fund Ending Fund Balance

The current budgeting practice of the City is to use the projected level of fund balance expected to remain in the General Fund at the end of any fiscal year as a funding source for the following year. The Ending Fund Balance estimate always contains two components: the portion of the fund balance that is rebudgeted for completing projects or retaining reserves; and the portion which is undesignated and available as a general funding source in the coming year. In the 2019-2020 Adopted Budget, a total fund balance estimate of \$289.4 million was included as a funding source. As discussed earlier, the 2018-2019 General Fund Ending Fund Balance of \$364.8 million was \$75.4 million above this estimate.

The components of the 2018-2019 General Fund Ending Fund Balance include additional funding sources, expenditure/transfer savings, and unexpended reserves as described below:

**2018-2019 General Fund
 Ending Fund Balance Components**

Fund Balance Component	\$ Amount (\$ in 000s)
Additional Funding Sources	12,604
Expenditure/Transfer Savings	89,706
Unexpended Reserves	262,503
TOTAL	\$ 364,813

The total Sources of Funds ended the year \$12.6 million above the modified budget as a result of higher revenues (\$9.4 million) and liquidation of carryover encumbrances (\$3.2 million). For the Uses of Funds, expenditure and transfer savings totaled \$89.7 million, while unexpended reserves totaled \$262.5 million, representing the largest component of the 2018-2019 Ending Fund Balance. Of the \$89.7 million in expenditure savings, a majority was rebudgeted in the 2018-2019 Adopted Budget (\$50.2 million) with additional funding being recommended for rebudget as part of this report (\$8.3 million).

General Fund Reserves, totaling \$262.5 million at the end of 2018-2019, include three categories: Earmarked Reserves (\$186.4 million) established to address specific needs per City Council direction; Ending Fund Balance Reserve (\$39.1 million) established to help ensure sufficient fund balance would be available at the end of 2018-2019 to meet the budgeted estimate used for the development of the 2019-2020 Adopted Budget, and the Contingency Reserve (\$37.0 million) set at a minimum of 3% of expenditures per City Council policy.

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2018-2019 General Fund Ending Fund Balance

Following is additional information regarding the two reserve categories.

- ***Earmarked Reserves (\$225.5 million)*** – At the end of 2018-2019, the most significant reserves included the following: 2018-2019 Ending Fund Balance Reserve (\$39.1 million); Fire Training Center Replacement Reserve (\$36.8 million); 2019-2020 Proposed Budget Planning Reserve (\$34.5); Building Development Fee Program Reserve (\$26.1 million); 2019-2020 Future Deficit Reserve (\$15.5 million); Workers Compensation/General Liability Catastrophic Reserve (\$15.0 million); Salaries and Benefits Reserve (\$9.2 million); Budget Stabilization Reserve (\$17.0 million); Fire Development Fee Program (\$7.2 million); Public Works Development Fee Program Reserve (\$5.6 million); Sick Leave Payments Upon Retirement Reserve (\$5.0 million); Cultural Facilities Capital Maintenance Reserve (\$3.1 million); and City Health Plan Restructuring Reserve (\$3.0 million). Most of the Earmarked Reserves were either approved for rebudget or used as a funding source in the 2019-2020 Adopted Budget.

The 2018-2019 Ending Fund Balance Reserve of \$39.1 million was proactively set aside to help ensure sufficient fund balance would be available at the end of 2018-2019 to meet the budgeted estimate used for the development of the 2019-2020 Adopted Budget. Annually, as part of the development of the General Fund Forecast and Adopted Budget for the following year, a certain amount of current year unrestricted ending fund balance is estimated to be available at the end of the year as a funding source for the following year's budget. This ending fund balance is expected to be generated from additional revenues above budgeted levels, expenditure savings, and the liquidation of carryover encumbrances during the year. In the 2019-2020 Adopted Budget, it was assumed that \$49.5 million would be generated from these sources. The establishment of the 2018-2019 Ending Fund Balance Reserve set aside a portion of this funding, projecting additional fund balance would be realized from a combination of excess revenues, expenditure savings and the liquidation of prior year carryover encumbrances.

- ***Contingency Reserve (\$37.0 million)*** – The City Council has established a budget policy of maintaining a minimum 3% Contingency Reserve in the General Fund. At the end of 2018-2019, the Contingency Reserve totaled \$37.0 million and remained unspent during the year. As part of the development of the 2019-2020 Adopted Budget, the full Contingency Reserve was rebudgeted to comply with the Council Policy of maintaining a minimum 3% Contingency Reserve in the General Fund. To align with the Modified Budget that will result from the recommended actions included in this report, an additional \$1.5 million is recommended in this report to comply with the 3% funding requirement that would bring the 2019-2020 Contingency Reserve to \$40.0 million. It is important to note, however, that if this Contingency Reserve is ever needed, it is only sufficient to cover General Fund payroll expenditures for approximately two weeks in the event of an emergency.

ANALYSIS

2018-2019 General Fund Ending Fund Balance

As discussed above, it was assumed that \$289.4 million would remain in the General Fund at the end of 2018-2019 and would be carried over to 2019-2020 as Beginning Fund Balance as part of the adoption of the 2019-2020 Budget. These funds, which were expected to be generated from unexpended reserves, unexpended funds that were rebudgeted to 2019-2020, additional revenue, expenditure savings, and the liquidation of carryover encumbrances, were programmed for use in the 2019-2020 Adopted Budget. The actual General Fund Ending Fund Balance was above the estimate used in the 2019-2020 Adopted Budget by \$75.4 million due to excess revenues and additional expenditure savings, of which nearly two thirds are recommended to be rebudgeted or incorporated into clean-up actions (e.g. Development Fee Program) as part of this report.

The following chart details the recommended uses of the \$75.4 million additional fund balance as well as other budget adjustments that are recommended as part of this report. Recommended clean-up actions will result in a decrease to the available fund balance of \$48 million, reflecting a downward adjustment of \$12.2 million to reconcile the actual performance of the Development Fee Programs and Small Cell Permit Fee Program in 2018-2019, as well as a net downward adjustment of \$35.8 million to account for additional rebudget and clean-up actions to close-out 2018-2019, including rebudgeting of the \$36.8 million Fire Training Center Replacement Reserve. Once these adjustments have been accounted for, the net available fund balance available for allocation totals \$27.4 million. This additional fund balance is proposed to be allocated to address required technical/rebalancing needs as well as a very limited number of urgent fiscal/program needs in the current year.

ANALYSIS

Impacts on the 2019-2020 General Fund Budget

RECOMMENDED 2019-2020 GENERAL FUND ADJUSTMENTS (\$000s)	
Additional 2018-2019 Ending Fund Balance	\$75,387
Clean-Up Actions	
Development Fee Program Reconciliation	(\$12,191)
Fire Training Center Replacement Reserve Rebudget	(\$36,835)
Rebudgets/Clean-Up Adjustments	\$1,032
Subtotal: Clean-Up Actions	(\$47,995)
Fund Balance Available After Clean-Up Actions	\$27,393
Recommended Budget Adjustments	
Required Technical/Rebalancing Actions	
General Liability Claims	(\$4,000)
Information Technology Department - Project Management (6.0 FTE and Contractual Support of \$1M)	(\$1,900)
City Attorney's Office Non-Personal/Equipment (Contractual Services for Litigation)	(\$1,500)
Contingency Reserve	(\$1,500)
Library Department Non-Personal/Equipment (San Jose State University Agreement - IT Baseline Costs)	(\$485)
Cultural Facilities Operations Support	(\$400)
Transfer to the Building and Structure Construction Tax Fund (North San José BCP)	(\$371)
3-1-1 Call Transition Reserve	(\$250)
Insurance Premiums	(\$185)
Fire Training Center Relocation (\$3.5 million, Offset by Reserve Reduction)	\$0
Transportation Department Electrical Services Support (Reallocate \$450,000 to Non-Personal/Equipment)	\$0
Miscellaneous Adjustments	(\$33)
Subtotal: Required Technical/Rebalancing Actions	(\$10,624)
Grants/Reimbursements (Sources = \$3.6 M; Uses = \$2.8 M)	\$781
Urgent Fiscal/Program Needs	
Police Department Guardian Rapid Response Program (Overtime, \$3.0 M; Vehicle Purchases, \$550,000)	(\$3,550)
Transfer to the Municipal Golf Course Fund (Los Lagos Golf Course Debt Pay Down)	(\$2,300)
Community Plan to End Homelessness – Quality of Life and Healthy Neighborhoods	(\$1,500)
City Facilities Safety Assessment	(\$200)
Subtotal: Urgent Fiscal/Program Needs	(\$7,550)
Subtotal: Recommended Budget Adjustments	(\$17,393)
Remaining Fund Balance After Recommended Adjustments	\$10,000
Recommended Distribution of Remaining Fund Balance in Accordance with City Council Policy (I-18)*	
Budget Stabilization Reserve	(\$5,000)
Unmet/Deferred Infrastructure Needs: City Facilities Emergency Power Generation	(\$5,000)
Total Recommended Fund Balance Distributed per City Council Policy I-18	(\$10,000)
Remaining Fund Balance After Recommended Adjustments	(\$0)

* These actions are reflected in the Recommended Budget Adjustments and Clean-Up/Rebudget Actions section of this report under Required Technical-Rebalancing Actions.

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Impacts on the 2019-2020 General Fund Budget

A summary of the significant adjustments by category is included below. More detail is provided in *Section IV: Recommended Budget Adjustments and Clean-Up/Rebudget Actions*.

Clean-Up Actions (-\$48 million)

- **Development Fee Programs Reconciliation (-\$12.2 million)** –Year-end reconciliations of the revenues and expenditures in the Development Fee Programs and Small Cell Permit Fee Program are conducted to determine if revenues exceeded or fell below costs. To ensure that all development fees will be used solely to support development fee activities, any excess revenues and interest earnings above actual costs are placed in Development Fee Program Reserves. Based on 2018-2019 results, \$12.2 million is recommended to be returned to the Development Fee (Building, Fire, Planning, and Public Works), Citywide Planning, and Small Cell Permitting Programs.
- **Rebudgets/Clean-Up Adjustments (-\$35.8 million)** – A series of adjustments are recommended to complete existing projects in 2019-2020 and to reflect any necessary technical budget adjustments or reconciliation actions. The Annual Report is the point in the budget process where action is required to rebudget unexpended funds from the prior year that were not anticipated when the Adopted Budget was approved, but are required to complete a project in the current year. The largest rebudget is for the Fire Training Center Replacement Reserve of (\$36.8 million), which was established on June 18, 2019 shortly after the proceeds were received from the sale of the existing Fire Training Center site. Also recommended are actions that reduce previous rebudgets to reflect instances where expenditures, for which rebudgets were approved for incorporation into the Adopted Budget, exceeded estimates for 2018-2019; therefore, the funds are not available for rebudget to 2019-2020. Other technical adjustments include the reconciliation of restricted program funding (e.g. 4th Street Garage Banquet Facility Maintenance and Operations, Artificial Turf Capital Replacement, Certified Access Specialist Program, Contractual Street Tree Planting, Digital Inclusion Program, Jet Fuel Sales Tax, and Government Access activities).

Recommended Budget Adjustments (-\$17.4 million)

A number of General Fund budget adjustments, with a total net cost of \$17.4 million are recommended and can be classified under three categories: 1) Required Technical/Rebalancing Actions (net cost of \$10.6 million) that align already approved revenue estimates and expenditure budgets with the most current tracking information, reallocate funding among appropriations based on updated needs, to correct technical problems in the 2019-2020 Adopted Budget, or comply with actions previously authorized by the City Council; 2) Grants/Reimbursement/Fee Activities actions (net increase of \$781,000) to recognize new or adjust grant, reimbursement, or fee activity revenue, and adjust the appropriations for these purposes as necessary; and 3) Urgent Fiscal/Program Needs (net cost of \$7.6 million) brought forward for City Council consideration

ANALYSIS

Impacts on the 2019-2020 General Fund Budget

as part of this report because the Administration has deemed the needs cannot, or should not, wait until later in the year.

- **Required Technical/Rebalancing Actions (-\$10.6 million)**

- ***General Liability Claims*** – increases funding for General Liability Claims payments by \$4.0 million per an analysis of current and potential litigation settlements and claims awards, bringing the total 2019-2020 budget to \$14.0 million. (-\$4.0 million)
- ***Information Technology Non-Personal/Equipment and Personal Services (Project Management)*** – increases the Information Technology Department’s Personal Services (\$900,000) and Non-Personal/Equipment (\$1.0 million) appropriations by \$1.9 million to add 6.0 Enterprise Supervising Technology Analyst positions that will provide additional product-project management support and capacity to maximize the success of City technology initiatives. This action responds to direction provided in the Mayor’s June Budget Message for Fiscal Year 2019-2020, as approved by City Council, to repurpose vacancies and vacancy savings to add at least a half dozen positions to implement IT projects throughout the City. Though the City continues to experience vacancy savings (including savings in the IT Department of \$1.7 million in 2018-2019), these savings are primarily generated by the high volume of hiring and separation across the City; even positions vacant for extended periods of time are typically backfilled with temporary staffing resources and cannot be eliminated on an ongoing basis without service delivery impacts. The Administration recommends adding these 6.0 positions ongoing, and will look to offset the ongoing cost as part of the 2020-2021 Proposed Budget. In addition to staffing support, this action adds one-time contractual support funding project management support and capacity-building for high-impact projects that require specialized expertise (as was used for the PeopleSoft upgrade in 2016). Focus areas for the increased project management capacity consist of emergency management technologies, development services transformation, data governance and business analytics, mobile and wireless communications, business process improvement and automation, and Internet-of-Things platforms and services. (-\$1.9 million)
- ***City Attorney’s Office Non-Personal/Equipment (Contractual Services for Litigation)*** – increases funding for contractual legal services due to higher than anticipated litigation activity, and for required subject matter expertise given the nature of the litigation. (-\$1.5 million)
- ***Contingency Reserve*** – increases the Contingency Reserve by \$1.5 million to comply with City Council Policy 1-18 to reserve a minimum of 3% of the General Fund operating budget to meet unexpected circumstances arising from financial and/or public emergencies that require immediate funding that cannot be met by any other means. This reserve level is sufficient to cover General Fund payroll expenditures for a couple of weeks in the event of an emergency. (-\$1.5 million)

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Impacts on the 2019-2020 General Fund Budget

- ***Library Department Non-Personal/Equipment (San José State University Agreement – IT Baseline Costs)*** – increases the Library Department’s Non-Personal/Equipment budget by \$485,000 to fund the payment of the Information Technology (IT) baseline services invoice from 2017-2018 per the cost-sharing agreement with San José State University (SJSU), and following engagement between the Library Department and SJSU throughout 2018-2019, to evaluate and update the shared IT baseline cost and shared obligation. Ongoing costs for 2019-2020 are already included in the Library Department’s Base Budget. (-\$485,000)
- ***Cultural Facilities Operations Support*** – as directed in the Mayor's June Budget Message for Fiscal Year 2019-2020, as approved by the City Council, increases by a total of \$400,000 for the annual operational support to the following major cultural organizations operating City facilities - the Tech Interactive (\$260,000), San Jose Museum of Art (\$50,000), Children's Discovery Museum (\$46,500), Hammer Theatre Center (\$30,000), and Escuela de Artes y Cultura at the Mexican Heritage Plaza (\$13,500) – that sustained large reductions in operational support during the Great Recession. This action restores previously reduced funding and the allocations in future years will align with inflation. (-\$400,000)
- ***Transfer to the Building and Structure Construction Tax Fund (North San José BCP)*** – transfers \$371,452 to the new North San José New Development (BCP) Reserve in the Building and Structure Construction Tax Fund in accordance with Mayor's June Budget Message for Fiscal Year 2014-2015 direction, as approved by the City Council (Manager's Budget Addendum #8), which dedicated sales tax collections from North San José construction activity as part of the Business Cooperation Program toward unfunded transportation needs in North San José. One company in the North San José Policy Area has participated in the Business Cooperation Program to date for a new construction project, resulting in the City receiving \$371,452 of sales tax revenue to be set aside per this policy direction. (-\$371,452)
- ***3-1-1 Call Transition Reserve*** – sets aside \$250,000 for potential funding needs with the transition of non-emergency call handling from Police Communications to the City Customer Contact Center. The 2019-2020 Adopted Operating Budget added 3.0 positions to the Customer Contact Center for the transition anticipated later this year, as well as contractual services to study the number and types of 3-1-1 and public safety calls to transition to the Customer Contact Center. This recommended action helps ensure that sufficient services are available for the transition by addressing any additional needs identified by the study or to deal with higher than anticipated call volumes. (-\$250,000)

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Impacts on the 2019-2020 General Fund Budget

- ***Insurance Premiums*** – increases the Insurance Premiums appropriation by \$186,000, to purchase a cyber liability insurance policy to mitigate potential liability and loss exposures resulting from the City's electronic data and commercial activities. Acquisition of cyber liability insurance coverage was recommended through the Finance Department's annual insurance renewal process, which analyzed the City's risk exposures, insurance market trends, product availability, and historical approach to insuring for losses. (-\$185,000)
- ***Fire Training Center Relocation*** – net-zero actions reduce the Fire Training Center Replacement Reserve and allocate funding (\$3.5 million) for the design of the new Fire Department Training Center, which is to be relocated from its current location in the Diridon Station Area to the City Central Service Yard at Senter Road. The existing Fire Training Center property was sold to Google on June 6, 2019, and the expected turnover of the property is June 2022. (\$0)
- ***Transportation Department Electrical Services Support (Reallocation from Personal Services to Non/Personal Equipment)*** – net-zero actions reallocate \$450,000 from the Department of Transportation's Personal Services appropriation to its Non-Personal/Equipment appropriation for contracted shift coverage for electrical services due to continued Electrician vacancies within the Department, resulting in limited in-house staff availability to cover mandatory graveyard and weekend on-call shifts to address emergency and safety electrical issues, such as signal outages or critical repair and/or removal of equipment damaged in a crash. (\$0)
- ***PRNS and PW Staffing Level Corrections*** – Several adjustments to correct staffing levels and attributable costs that were inadvertently omitted or incorrectly adjusted during development of the 2019-2020 Adopted Budget, including: add 2.75 Recreation Leader PT unbenefited positions in the Parks, Recreation and Neighborhood Services Department (PRNS) to provide staff support for the anticipated opening of the Arcadia Softball Sports Complex as originally anticipated in the 2018-2019 Adopted Budget and correct cost allocations in the Public Works (PW) Department related to the Public Works Development Fee Program and the Public Safety and Infrastructure Bond Fund. In addition, the position count within the Parks, Recreation and Neighborhood Services Department were incorrectly stated in the 2019-2020 Adopted Operating Budget, primarily due to the timing of limit-dated positions. Corrective actions to delete these overstated positions are recommended; however, the personal services budget available to PRNS remains unaffected. (-\$233,000)

ANALYSIS

Impacts on the 2019-2020 General Fund Budget

- ***Remaining Adjustments*** – A limited number of other adjustments make minor technical corrections or reallocations, including the recognition of additional late fee revenue received in 2018-2019 from the Water Utility Fund, shifting personal service resources to non-personal/equipment for Nurse Practitioner temporary staffing in the Human Resources Department, reduction to the Council District #10 and Office of the Mayor budgets that align with the deferral of the salary increase set by the Council Salary Setting Commission, correction to Local Sales Tax – My San José 2.0 to adjust for erroneous expenditures that were inadvertently charged in 2018-2019, adjustments to the Childcare Facilities and Training (Gardner Preschool) appropriation to accurately align the budget amount, adjustments between the operations support and capital maintenance funding allocations for the Mexican Heritage Plaza to align the Adopted Budget with the existing agreement, transfer to the Edward Byrne Memorial Justice Assistance Grant Trust Fund to ensure that the fund does not have a negative fund balance, funding of elections cost for Community Facilities District #8 serving Communications Hill residents as directed in the Mayor’s June Budget Message for Fiscal Year 2018-2019, and a liquidation of the Office of Equality Assurance Labor Compliance System Reserve to provide initial administrative support and temporary staffing for the system’s implementation and assistance with implementing City Council Policy Priorities related to labor compliance. (net -\$200,000)

- **Grants/Reimbursements/Fees (-\$781,000)**
 - A series of adjustments (net revenues of \$3.6 million offset by net expenditures of \$2.9 million) are recommended to recognize new and updated revenues and expenditures for ***Grants, Reimbursements, and/or Fees*** for the following Departments: Office of Economic Development (net-zero expenditure adjustment of \$1.0 million); Fire Department (net zero expenditure adjustment of \$370,000); Library Department (net zero expenditure adjustment of \$163,000); Mayor & City Council (net zero expenditure adjustment of \$164,000); Parks, Recreation and Neighborhood Services Department (net revenue increase of \$306,000); Planning, Building, and Code Enforcement Department (net expenditure increase of \$5,000); Police Department (net zero expenditure adjustment of \$809,000); Public Works Department (net expenditure decrease of \$515,000); and Transportation Department (net expenditure increase of \$35,000). These adjustments are further described in *Section IV. Recommended Budget Adjustments and Clean-Up/Rebudget Actions*. (\$781,000)

ANALYSIS

Impacts on the 2019-2020 General Fund Budget

- **Urgent Fiscal/Program Needs (\$7.55 million)**
 - ***Police Department Guardian Rapid Response Program*** – increases the Police Department's Personal Services (\$3.0 million) and Non-Personal/Equipment (\$550,000) appropriations by \$3.6 million for overtime costs and to purchase and equip nine patrol vehicles for the implementation the Guardian Rapid Response Program. The new Guardian Rapid Response Program is designed to enhance the state of readiness for an active shooter attack, and to focus efforts on enhancing the safety of all school campuses in the City of San José. Guardian Teams will consist of two-officer patrol vehicles in pre-designated zones to fulfill the dual roles of immediate active shooter response and strategic school campus safety patrols. The program may additionally deploy officers in the event of a known threat or an anticipated, unusually large crowd size. (-\$3.6 million)
 - ***Transfer to Municipal Golf Course Fund (Los Lagos Golf Course Debt Pay Down)*** – increases the transfer from the General Fund to the Municipal Golf Course Fund by \$2.3 million, from \$8.4 million to \$10.7 million, to pay down outstanding principal for debt related to the Los Lagos Golf Course. The direction provided in the Mayor's March and June Budget Messages for Fiscal Year 2019-2020, as approved by the City Council, prioritized the use of one-time resources to improve long-term fiscal sustainability by early retirement of debt obligations and allocated a total of \$6.2 million to both the elimination of Rancho Del Pueblo debt (\$3.4 million) and the early pay down of Los Lagos debt (\$2.8 million). The allocation of an additional \$2.3 million for Los Lagos debt pay down furthers this approach and, when combined with actions in the 2019-2020 Adopted Budget result in a cumulative annual debt service savings of approximately \$700,000 and shortens the debt retirement date by four years to 2026. (-\$2.3 million)
 - ***Community Plan to End Homelessness – Quality of Life and Healthy Neighborhoods*** – establishes a City-Wide appropriation in the amount of \$1.5 million to support inter-departmental efforts to operationalize a locally-tailored work-plan in support of Pillar 3 of the Community Plan to End Homelessness (Improving Quality of Life for Unsheltered Individuals and Creating Healthy Neighborhoods for All), and efforts to enhance service levels in pilot project areas, or where there are disproportionate impacts from unsheltered individuals. (-\$1.5 million)
 - ***City Facilities Safety Assessment*** – establishes funding of \$200,000 to conduct a security evaluation and threat assessment consistent with Homeland Security Best Practices for Antiterrorism, which will inform the development of potential security and operational improvements to protect City-owned facilities and the community and employees who use them. A separate allocation of \$207,000 in the Convention and Cultural Facilities Fund supports activities related to the Convention Center and various cultural facilities. (-\$200,000)

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Impacts on the 2019-2020 General Fund Budget

Recommended Distribution of Remaining Fund Balance per City Council Policy I-18 (-\$10.0 million)

Per Council Policy I-18, Operating Budget and Capital Improvement Program Policy, any ending fund balance that may be available after the close of the 2018-2019 fiscal year will be allocated 50% for unmet/deferred infrastructure and maintenance needs and 50% to offset any projected deficit for the following fiscal year. Based on the February 2019 Forecast, it is currently estimated that the General Fund will face a shortfall of approximately \$10.9 million in 2019-2020. To fully address this projected shortfall on a one-time basis, the 2019-2020 Adopted Budget sets aside an equivalent amount (\$10.9 million) in the 2020-2021 Future Deficit Reserve. Because this reserve is fully funded, remaining funds may be allocated to the following: Budget Stabilization Reserve and/or Contingency Reserve, unmet/deferred infrastructure and maintenance needs, and/or other one-time urgent funding needs. The remaining Ending Fund Balance of \$10.0 million is recommended to be allocated to unmet/deferred infrastructure needs and the Budget Stabilization Reserve, as follows:

- ***Unmet/Deferred Infrastructure Needs: City Facilities Emergency Power Generation*** – provides one-time funding of \$5.0 million to procure and install equipment to support the sustained operations of critical City facilities in the event of a planned or unplanned electrical power outage, as 32 critical City facilities do not have adequate levels of back-up electricity generation and would cease to function in the event of an outage. General Fund resources are also allocated to supply generators to fueling stations at the West Corporation Yard and the Police Substation, which currently do not have generators and are necessary for refueling emergency vehicles in the event of an outage, as well as for the procurement of two high capacity fuel storage trucks to provide needed service coverage and minimize generator downtime. Pacific Gas and Electric (PG&E) should be responsible for provision of back-up power generation or reimburse the City for expenses incurred to undertake mitigation measures for power generation according to California Public Utilities Commission (CPUC) guidance and rulemaking regarding Utility Public Safety Power Shutoff Programs. However, until the City receives the commitment from PG&E and due to the critical nature of these improvements, the City will advance this funding to ensure power generation is available in the event of an outage. Additional funding of \$600,000 is recommended from the Sewer Service and Use Charge Capital Fund (\$500,000) for back-up electricity generation at five sanitary sewer pump stations, and from the San José-Santa Clara Treatment Plant Capital Fund (\$100,000) for the fueling island at the Regional Wastewater Facility. (-\$5.0 million)

ANALYSIS

Impacts on the 2019-2020 General Fund Budget

- **Budget Stabilization Reserve** – increases the Budget Stabilization Reserve by \$5.0 million in accordance with City Council Policy 1-18 to maintain an adequate reserve level to provide budget stability when there are fluctuations that result in lower than projected revenues and/or higher than projected expenditures that cannot be re-balanced within existing budget resources in any given year. This action, along with the increase to the Contingency Reserve, maintains the level of General Purpose Reserves (the sum of the Budget Stabilization Reserve, the Contingency Reserve, and the Worker's Compensation General Liability Catastrophic Reserve) at 6.5% of General Fund operating expenditures, which is consistent with the level included in the 2019-2020 Proposed Operating Budget and consistent with the strategy identified in the Mayor's Budget Addendum #25, "General Fund Reserve Target Levels". (-\$5.0 million)

2018-2019 Selected Special/Capital Funds Budget Performance

Airport Operating Funds

The Airport served 14.9 million passengers in 2018-2019, which was an overall increase of 10.8% from 2017-2018. Moreover, the 11.0% growth in annual enplanements at the Airport in 2018-2019 far exceeded the estimated level of 3.0%. For 2019-2020, passenger growth is anticipated to increase 1.3% over the 14.9 million passengers in 2018-2019.



Additional airport activity categories that demonstrated growth as compared to last year include traffic operations, landed weights, gallons of aviation fuel sold, and ground transportation trips.

ANALYSIS

2018-2019 Selected Special/Capital Funds Budget Performance

Overall, revenue performance exceeded budget by \$3.1 million (1.8%). Airline Rates and Charges (combined total of landing fees and terminal rents) and all other operating categories, excluding transfers, ended the year at \$175.9 million, which was \$3.1 million above the budget of \$172.7 million. The positive variance is mainly attributed to the Parking & Roadway revenue category, which was above the budgeted estimate by \$8.7 million (15.7%) due to higher revenues from economy (long-term), daily, and hourly parking and ground transportation, as well as Terminal Building Concession revenue, which was above the budgeted estimate by \$3.3 million (16.3%) associated with increased passenger levels.

The Airport Customer Facility and Transportation Fee Fund had year-end expenditure savings of \$251,000 (1.2%) and Airport Maintenance and Operation Fund had a year-end expenditure overage of \$8.4 million (7.1%) compared to the budgeted levels of \$118.2 million. The overage is attributed to the Airline Funds Distribution payments (\$30.2 million), the result of entering into the 2019 Airline-Airport Lease and Operating Agreement prior to June 30, 2019 and recording the net remaining revenue 2018-2019 Fiscal Year financial performance. The impact of the expenditure overage was partially mitigated by personal services savings of \$1.4 million from position vacancies and \$2.6 million in non-personal/equipment savings from the reassessment and prioritization of airport needs.

Capital Fund Major Revenues

A number of taxes and fees levied on construction and property resale (conveyance) activity provide a large source of revenue to the City’s Capital program. Except for the Sanitary Sewer Connection Fee, the 2018-2019 actual collections in these capital revenue categories ended the year above budgeted estimates. The chart below provides a comparison of estimated revenues to actual revenues for these types of revenues, and a discussion of the three largest revenue sources follows.

Construction-Related Capital Program Revenues Comparison
 (\$ in Thousands)

	2018-2019 Estimate*	2018-2019 Actuals	% Variance
Construction and Conveyance Tax	\$42,000	\$47,187	12.4%
Building and Structure Construction Tax	\$16,000	\$22,530	40.8%
Construction Excise Tax	\$21,000	\$25,770	22.7%
Municipal Water System Fees	\$75	\$245	226.7%
Residential Construction Tax	\$200	\$322	61.1%
Sanitary Sewer Connection Fee	\$700	\$226	(67.7%)
Storm Drainage Connection Fee	\$200	\$237	18.6%

* Revenue estimate used in the development of the 2018-2019 Adopted Capital Budget.

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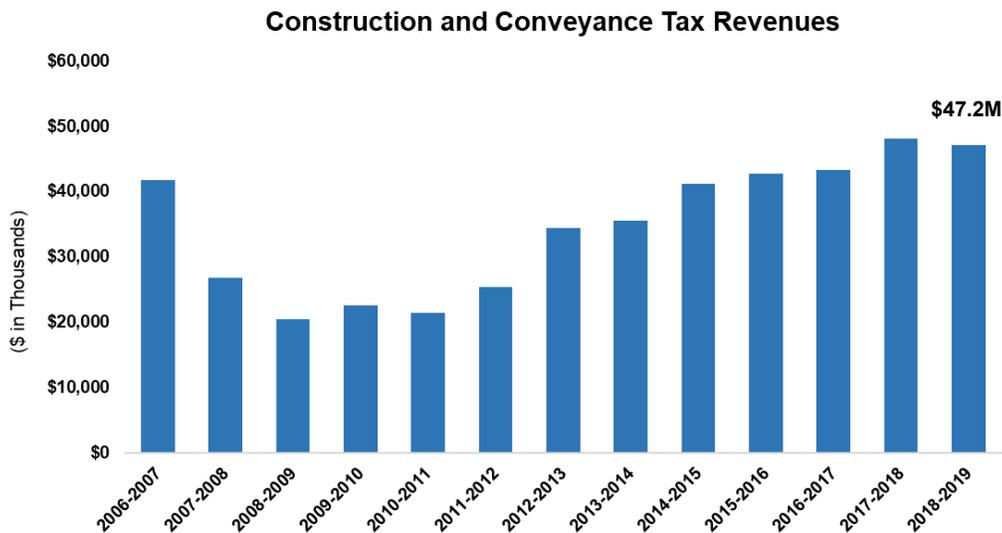
2018-2019 Selected Special/Capital Funds Budget Performance

Capital Fund Major Revenues

- **Construction and Conveyance Tax**

Real estate activity (primarily housing re-sales) determines the collection level of one of the major capital revenue sources, the Construction & Conveyance (C&C) Tax. Approximately 99% of C&C Tax is derived from a tax imposed upon each transfer of real property, with the remaining 1% generated from a construction tax levied on most types of construction. C&C Tax revenues, which are a significant source of funds for the Parks and Community Facilities Development, Library, Fire, Service Yards, and Communications capital programs, totaled \$47.2 million in 2018-2019. This collection level was marginally lower by \$900,000 (2%) from 2017-2018 collections of \$48.1 million, and \$5.2 million (12.4%) above the estimate of \$42.0 million that was assumed in the development of the 2019-2020 Adopted Capital Budget. The 2019-2020 Adopted Capital Budget was developed with the assumption that C&C tax receipts would total \$42.0 million in 2018-2019 and decrease to \$38.0 million in 2019-2020. With the stronger than anticipated performance in 2018-2019, the 2019-2020 C&C Tax revenue estimate allows for a 24.2% decline from 2018-2019 receipts. Collections in 2019-2020 will be closely monitored, and any necessary adjustment will be brought forward later in the fiscal year.

The following graph displays the history of Construction and Conveyance (C&C) Tax receipts.



After seven years of year-over-year home price growth, the local real estate market is slowing down. According to data from the Santa Clara County Association of Realtors, the single-family home price peaked at \$1.3 million in May 2018 (which represented a 30.0% increase from the May 2017 home price), but then began steadily decreasing.

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2018-2019 Selected Special/Capital Funds Budget Performance

Capital Fund Major Revenues

In addition, year-over-year median prices have steadily decreased each month since November 2018, with drops ranging from 3%-13% compared to the prior year level. In June 2019, the median single-family home price totaled \$1.1 million, which represents a 6.5% decrease from the June 2018 price of \$1.2 million, but is approximately 15% above the June 2017 price of \$996,000. In addition to the median home prices dropping, the number of property transfers (sales) has also continued to steadily decline. The total number of property transfers that occurred year-to-date through June 2019 has dropped approximately 10% compared to the prior year. Lastly, while single-family and multi-family dwellings are continuing to sell quickly, they are on the market longer than the prior year. The average days-on-market for single-family and multi-family dwellings in June 2019 totaled 30 days, which is twice as long than the extremely low 15 days experienced in June 2018.

- **Building and Structure Construction Tax and the Construction Excise Tax**

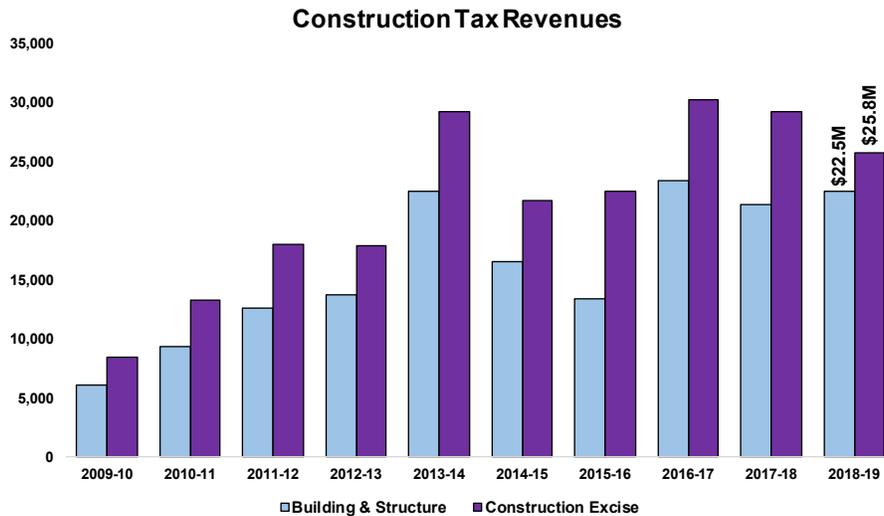
The Building and Structure Construction Tax and the Construction Excise Tax are major sources of funding for the Traffic Capital Program. Year-end collections in the Building and Structure Construction Tax category totaled \$22.5 million in 2018-2019. This collection level was 40.8% (\$6.5 million) above the revenue estimate of \$16.0 million used to develop the 2019-2020 Adopted Capital Budget and \$1.0 million higher than the \$21.4 million received in 2017-2018. Construction Excise Tax receipts for 2018-2019 totaled \$25.8 million, 22.7% (\$4.8 million) above the revenue estimate of \$21.0 million used to develop the 2019-2020 Adopted Capital Budget, representing a 12.2% (\$3.6 million) decrease from 2017-2018 collections of \$29.4 million.

ANALYSIS

2018-2019 Selected Special/Capital Funds Budget Performance

Capital Fund Major Revenues

The graph below displays the collection history of both the Building and Structure Construction Tax and Construction Excise Tax receipts. Valuation activity in 2016-2017 surpassed the historically high levels of 2013-2014, setting a new peak, but have been declining since in the last couple of years. The status of these volatile taxes will be closely monitored throughout 2019-2020 to determine if budget actions are necessary to revise the revenue estimates



Special and Capital Funds Budget Adjustments

Several budget adjustments for both special and capital funds are included in this report, including recognition of grants, net-zero transfers/reallocations, new allocations for a small number of high priority projects and programs, and required fund rebalancing activity.

In the Parks and Community Facilities Development Capital Program, in 2012-2013, \$3.5 million from the Santana Park Development Reserve (allocated in the Park Trust Fund) was used to front a State Proposition 84 grant that was awarded to Del Monte Park (allocated in the Park Trust Fund). As grant funding has been received over the last several years, the reserve has been replenished. The 2018-2019 Annual Report includes an action to allocate the final reimbursement (\$900,000), which is derived of grant revenue received in 2018-2019 (\$590,000) and Del Monte Park project savings (\$310,000).

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2018-2019 Selected Special/Capital Funds Budget Performance

Special and Capital Funds Budget Adjustments

In the Airport Capital Program, actions are recommended to reduce the budgets of several projects in the Airport Renewal and Replacement Fund to create available funding of \$1.0 million for the new Airport Program Management project. The following project budgets will be reduced or eliminated: Customs and Border Protection Process Improvements (\$600,000); Terminal Dynamic Curbside Signage (\$446,000); and Terminal A Baggage Make-Up Unit (\$150,000). The years of continual passenger growth has put a strain on the airport facilities. As a result, Airport has reset priorities to ensure they have sufficient resources to prepare for Phase II capital development.

Notable adjustments in the Traffic Capital Program include the establishment of the Better Bikeways Program to help implement a network of buffered bike lanes in the downtown (\$2.4 million), full funding of the Access and Mobility Plan (\$573,000), and the set aside of \$2.2 million to refund an overpayment of Building and Structure Construction Tax and Construction Excise Tax due to a portion of the Coleman Highline development changing its intended use from commercial to industrial, which is taxed at a lower rate.

The Public Safety and Infrastructure Bond Fund (Measure T) includes adjustments to clearly reallocate the financial and administrative costs in the Public Works Department from individual projects into a separate program administration appropriation, and the establishment of 1% Public Art funding based on eligible projects.

Finally, the rebudget of unexpended funds for projects and programs extending into 2019-2020 is recommended in this report. Details of these adjustments can be found in Section IV of this report.

NEXT STEPS

The results of the 2018-2019 Annual Report will provide an updated starting point for monitoring 2018-2019 financial performance, with the observed revenue and expenditure trends factored into the analysis of the General Fund and numerous special and capital funds. Information on the City's budget for 2018-2019 will be provided in the Bi-Monthly Financial Reports and the 2018-2019 Mid-Year Budget Review.

The 2018-2019 Annual Report results will also be factored into the 2019-2020 budget development process. The General Fund Five-Year Forecast is scheduled to be released in late February 2020. The 2020-2021 Proposed Capital and Operating Budgets are scheduled to be released on April 22, 2020 and May 1, 2020, respectively.

PUBLIC OUTREACH/INTEREST

This document is posted on the City's website for the October 8, 2019, City Council agenda.

COORDINATION

The City Manager's Budget Office coordinated with the Finance Department on the reconciliation of the City's funds and coordinated with all City Departments and City Council appointees, as applicable, on recommended budget adjustments that are brought forward in this document.

COMMISSION RECOMMENDATION/INPUT

No commission recommendation or input is associated with this action.

CONCLUSION

Through careful fiscal management, overall revenues for the various City funds ended the year close to estimated levels and expenditures were below budgeted allocations. When the 2018-2019 Adopted Budget was developed, it was assumed that economic growth would continue. Economic indicators and actual revenue performance supported this general assumption, with a number of revenue categories, such as Sales Tax, Property Tax, Licenses and Permits, and Business Taxes. Those revenue categories associated with private development and construction projects, such as development-related fees and taxes, again saw solid performance in 2018-2019.

In the General Fund, the additional fund balance at the end of 2018-2019 after considering clean-up adjustments totaled \$27.4 million. Recommendations are included in this report to allocate those funds to various required technical and rebalancing actions (\$10.6 million) and to address an several urgent fiscal/program needs (\$7.6 million). In addition, adjustments to various grants, reimbursements and fee activities are included that yield a positive balance of \$781,000 along with a series of technical adjustments. After these adjustments, the remaining fund balance of \$10.0 million is recommended to be distributed in accordance with City Council Policy I-18. These funds are recommended to increase the Budget Stabilization Reserve (\$5.0 million) from \$27.0 million to \$32.0 million and to support unmet/deferred infrastructure needs by allocating funds for City Facilities Emergency Power Generation (\$5.0 million).

The Administration will continue to monitor and report on the City's budget performance through the Bi-Monthly Financial Reports and the Mid-Year Budget Review. The financial results of 2018-2019, as well as the actual performance in 2019-2020, will be factored into the development of the 2020-2021 budget. The 2021-2025 General Fund Five-Year Forecast will be released in February 2020 for budget planning purposes.


Jim Shannon
Budget Director

CERTIFICATION OF FUNDS

I hereby certify that there will be available for appropriation in the designated funds and in the amounts as listed below in fiscal year 2019-2020 monies in excess of those heretofore appropriated therefrom:

General Fund	\$87,209,463
Airport Customer Facility and Transportation Fee Fund	\$234,495
Airport Fiscal Agent Fund	\$589,798
Airport Maintenance and Operation Fund	\$446,366
Airport Passenger Facility Charge Fund	\$3,746,312
Airport Renewal and Replacement Fund	\$4,743,086
Airport Surplus Revenue Fund	\$10,176,474
Benefit Funds – Dental Insurance Fund	\$238,438
Benefit Funds – Unemployment Insurance Fund	\$123,525
Branch Libraries Bond Projects Fund	\$35,104
Building and Structure Construction Tax Fund	\$17,867,469
Business Improvement District Fund	\$432,922
Cash Reserve Fund	\$26
City Hall Debt Service Fund	\$509,252
Community Development Block Grant Fund	\$1,833,409
Community Facilities District Fund #11	\$6,650
Community Facilities District Fund #17	\$37,629
Community Facilities District Fund #2 and #3	\$9,260
Community Facilities Revenue Fund	\$1,522,972
Construction and Conveyance Tax – Communications	\$320,170
Construction and Conveyance Tax – Fire	\$1,094,803
Construction and Conveyance Tax – Council District 1	\$1,068,455
Construction and Conveyance Tax – Council District 2	\$453,514
Construction and Conveyance Tax – Council District 3	\$647,706
Construction and Conveyance Tax – Council District 4	\$685,800
Construction and Conveyance Tax – Council District 5	\$544,456
Construction and Conveyance Tax – Council District 6	\$879,047
Construction and Conveyance Tax – Council District 7	\$2,702,436
Construction and Conveyance Tax – Council District 8	\$874,175
Construction and Conveyance Tax – Council District 9	\$620,564
Construction and Conveyance Tax – Council District 10	\$916,912
Construction and Conveyance Tax – Parks City-Wide	\$5,734,508
Construction and Conveyance Tax – Parks Yards	\$280,253
Construction and Conveyance Tax – Service Yards	\$614,024
Construction Excise Tax Fund	\$37,774,776

CERTIFICATION OF FUNDS

Contingent Lien District Fund	\$216,340
Convention and Cultural Affairs Fund	\$1,616,083
Convention Center Facilities District Revenue Fund	\$1,591,009
Downtown Property and Business Improvement District Fund	\$22,793
Economic Development Administration Loan Fund	\$40
Emergency Reserve Fund	\$103,704
Emma Prusch Fund	\$12,611
Federal Drug Forfeiture Fund	\$92,850
General Purpose Parking Fund	\$1,318,664
General Purpose Parking Capital Fund	\$21,132
Gift Trust Fund	\$1,075,263
Home Investment Partnership Program Fund	\$1,660,057
Housing Trust Fund	\$1,044,617
Ice Centre Revenue Fund	\$864,196
Improvement District Fund	\$54,121
Inclusionary Fee Fund	\$7,653,742
Integrated Waste Management Fund	\$2,630,991
Lake Cunningham Fund	\$134,990
Library Parcel Tax Fund	\$406,657
Library Parcel Tax Capital Fund	\$278,748
Low and Moderate Income Housing Asset Fund	\$27,228,540
Maintenance District Fund #1	\$15,482
Maintenance District Fund #18	\$5,945
Maintenance District Fund #21	\$1,927
Major Collectors and Arterials Fund	\$14,026
Major Facilities Fund	\$141,720
Multi-Source Housing Fund	\$8,944,384
Municipal Golf Course Fund	\$2,358,183
Neighborhood Security Bond Fund	\$95,493
Parks and Recreation Bond Projects Fund	\$908,732
Public Works Program Support Fund	\$358,223
Rental Stabilization Program Fee Fund	\$1,294,046
Residential Construction Tax Contribution Fund	\$782,458
San José Arena Capital Reserve Fund	\$4,018,068
San José Clean Energy Operating Fund	\$4,283,743
San José-Santa Clara Treatment Plant Capital Fund	\$6,096,184
San José-Santa Clara Treatment Plant Income Fund	\$94,941
San José-Santa Clara Treatment Plant Operating Fund	\$5,911,857
Sanitary Sewer Connection Fee Fund	\$563,881
Sewage Treatment Plant Connection Fee Fund	\$1,184,776
Sewer Service and Use Charge Fund	\$2,116,814
Sewer Service and Use Charge Capital Improvement Fund	\$8,777,994
South Bay Water Recycling Capital Fund	\$25,975
St. James Park Management District Fund	\$137,171

CERTIFICATION OF FUNDS

State Drug Forfeiture Fund	\$407,987
Storm Drainage Fee Fund	\$36,418
Storm Sewer Capital Fund	\$638,970
Storm Sewer Operating Fund	\$1,912,184
Subdivision Park Trust Fund	\$11,313,613
Supplemental Law Enforcement Services Fund	\$1,341,470
Transient Occupancy Tax Fund	\$3,103,162
Underground Utility Fund	\$1,676,490
Vehicle Maintenance and Operations Fund	\$704,784
Water Utility Fund	\$3,387,766
Water Utility Capital Fund	\$1,115,898



Jim Shannon
Budget Director