RECOMMENDATION
Staff recommends that the Finance Committee recommend to the City Council adoption of the attached Budget Amendment Ordinance (BAO) (Attachment 1), which includes:

   a. Proposed midyear adjustments to the 2004-05 Budget for the General Fund, Enterprise Funds, Special Revenue Funds, Internal Service Funds, Debt Service Fund, and Capital Improvement Fund (Exhibit A).
   b. New or amended 2004-05 Capital Improvement Program Project Descriptions (Exhibit B).
   c. Amendments to the 2004-05 Adopted Municipal Fee Schedule (Exhibit C).
   d. Amendments to the 2004-05 Table of Organization (Exhibit D).

The 2004-05 midyear Capital Improvement Program Projects Status Report is attached as an informational item (Attachment 2). A list of continuous projects follows this summary (Attachment 3). No action is required on these two items.

Staff also recommends the Finance Committee review and comment on the preliminary financial condition of the City as of December 31, 2004.

BACKGROUND
This report summarizes the changes to the 2004-05 Adopted Budget as part of the normal course of business through December 2004. Where possible, adjustments are held until this midyear report is brought to Council in an effort to streamline the BAO process year-round. This discussion is categorized by fund with a primary focus on major changes in the General Fund. Details of these changes, as well as all fund summaries, are included in Exhibit A. The midyear CIP project status report (Attachment 2) provides the Finance Committee with information on the status of the City’s CIP
projects as of December 31, 2004.

As recommended by the City Auditor, this report also provides the Finance Committee and City Council with preliminary insight into the financial condition of the City as of December 31, 2004. It is worth noting the second quarter totals are unaudited and are subject to change.

**DISCUSSION**

The following is a summary of major revenue and expenditure adjustments as detailed in Exhibit A.

**General Fund**

At midyear, General Fund operating revenues and expenditures are at 41 and 54 percent of budget respectively. The difference between these numbers reflects typical timing issues with the collection of tax revenues and contract encumbrances. As noted below, the State of California’s “triple flip” agreement with cities in fiscal 2004-05 and 2005-06 is resulting in later-than-normal payments as a significant portion of sales tax revenue is being paid as property tax. By year-end, total General Fund expense will be less than total revenues.

In the first half of 2004-05, the City witnessed stabilization in the local economy and a lessening in the rate of decline in its economically sensitive revenue sources. While this represents a positive turn for the City, the local job picture has not improved significantly. Consequently, staff does not foresee a major rebound in key revenue sources such as sales and transient occupancy taxes. State actions to solve its budget problems, however, do require a considerable adjustment to Vehicle License Fee revenue.

**Sales tax** revenues for 2004-05 are expected to roughly equal the $18.1 million realized in 2003-04. This requires a downward adjustment of $0.24 million at midyear. Sales taxes in the second and third calendar year 2004 quarters (which fall in fiscal year 2004-05) improved over prior year quarters by 3.0 percent and 4.3 percent, respectively. Due to several significant one-time receipts in the prior year, softness in automobile sales, and rising consumer debt, sales tax revenue is projected to remain flat in 2004-05 compared to the prior year.

**Property taxes** are being adjusted upward at midyear by $2.49 million to $16.09 million. As mentioned above, the State is paying a large part of the VLF via property tax remittances. Of the $2.59 million increase, $1.71 million is due to this change. The remaining $0.88 million is due to the increase in the property tax roll for 2004-05. The long-term lease transaction for the Stanford Shopping Center results in additional annual property taxes for the City.

**Transient Occupancy Taxes (TOT)** appear to be firming in 2004-05 with occupancy and room rates slowly rising. Although July through September results were flat, October and November 2004 occupancy and room rates were 4 percent higher than the prior year. Staff is cautiously optimistic that this trend will continue and has accordingly adjusted TOT revenue upward by $0.20 million.

**Other Taxes and Fines**

- **Documentary transfer tax** revenues are being raised by $0.28 million at midyear. Transfer taxes were exceptionally strong in 2003-04 as a result of the Stanford Shopping Center transaction. With a steady residential market and a potentially improving commercial market,
staff expects slightly higher 2004-05 revenues than originally budgeted.

- **Motor Vehicle License Fee (VLF)** revenue is being reduced by $3.3 million as a consequence of State actions to solve its deficit. As described in the Long Range Financial Plan (p. 10), the City is losing $1.5 million in annual VLF revenue in 2004-05 and in 2005-06; full payment will resume in fiscal 2006-07. Starting in 2004-05, most of the remaining VLF revenue will be paid via property tax remittances. A small part of the VLF will continue to be paid directly by the State, estimated at $0.3 million for 2004-05.

- **Parking citation** revenues are being reduced by $0.1 million (6 percent) due to the opening of the new public garages and the extension of free parking time limits from 2 to 3 hours.

**Charges for services** revenues are being reduced by $0.2 million (1 percent). Major components of this reduction include a $0.4 million (31 percent) reduction in Development Center plan check fees resulting from a slowdown in development-related activities; a $0.1 million (7 percent) reduction in paramedic revenues due to delayed implementation of the Basic Life Support (BLS) program and a revised Medicare reimbursement projection; offset by a $0.3 million increase in 2003-04 yearend Stanford University billings for fire services.

**Permits and licenses** revenues are being reduced by $0.3 million (11 percent) due to a reduction in Planning and Community Environment’s building permit fee revenue. Changes in Development Center activities have prompted a recommendation for a comprehensive cost recovery analysis as part of the 2005-07 budget process.

**Department expenditures** are being reduced by a net $0.7 million (1 percent) as a means of balancing the midyear revenue reductions and $0.25 million in additional expenditure appropriations mainly from grant-funded spending. Specifically, $1.0 million in salary and benefit savings is being removed from 8 department budgets related to 37 current vacant positions. Library Department grants include the State of California’s Library Fund allocation ($23,929) and a California State Library grant purchase of Chinese language books ($10,000). Police Department grants include a COPS grant for a bar coding system, purchase and upgrade of various public safety equipment ($100,000); an Office of Traffic Safety (OTS) grant for a seatbelt compliance campaign ($25,000); an OTS grant for police sobriety checkpoints ($11,245); and a Department of Alcoholic Beverage Control (ABC) grant for decoy operations ($10,433).

**General Fund Overtime Analysis:**

Overtime expense reached 79 percent of budget as of December 31, 2004. Specifically the Fire and Police Departments are exceeding anticipated spending levels in this area for the following reasons:

- **Fire Department** (111 percent of budget): The two primary factors contributing to this situation are disability leave and vacancies. There are eight personnel on disability leave and the general length of time for disability has increased (four on long-term leave). There are 6 vacancies but the new recruits from the April academy will not be on active duty until next fiscal year. There will be offset savings in the regular salary budget to fund this additional expense.

- **Police Department** (66 percent of budget): The main factors contributing to higher overtime spending include absences due to disability leave, staff vacancies, and newly hired officers assigned to the academy and patrol program. These absences create additional overtime expense due to mandated minimum staffing levels in Patrol. Overtime reimbursements of
approximately $85,000 are expected from activities related to Stanford University football games, sobriety checkpoints duties, seat belt enforcement and ABC decoy operations. Offset savings in regular salaries will fund this additional expense.

With these two departments removed from the analysis, General Fund overtime expense is at 45 percent of budget at midyear.

CITY OF PALO ALTO
2004-05 MIDYEAR FINANCIAL REPORT
GENERAL FUND OVERTIME
(in thousands of dollars)

<table>
<thead>
<tr>
<th>(as of 12/31/04)</th>
<th>Adopted Budget</th>
<th>Midyear Budget</th>
<th>Midyear Changes</th>
<th>Actual</th>
<th>% of Midyear Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>City Attorney</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>0%</td>
</tr>
<tr>
<td>City Auditor</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>0%</td>
</tr>
<tr>
<td>City Clerk</td>
<td>13</td>
<td>13</td>
<td>-</td>
<td>-</td>
<td>0%</td>
</tr>
<tr>
<td>City Council</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>0%</td>
</tr>
<tr>
<td>City Manager</td>
<td>4</td>
<td>4</td>
<td>-</td>
<td>-</td>
<td>0%</td>
</tr>
<tr>
<td>Administrative Services</td>
<td>52</td>
<td>52</td>
<td>-</td>
<td>7</td>
<td>13%</td>
</tr>
<tr>
<td>Community Services</td>
<td>199</td>
<td>199</td>
<td>-</td>
<td>110</td>
<td>55%</td>
</tr>
<tr>
<td>Fire</td>
<td>983</td>
<td>983</td>
<td>-</td>
<td>1,087</td>
<td>111%</td>
</tr>
<tr>
<td>Human Resources</td>
<td>2</td>
<td>2</td>
<td>-</td>
<td>1</td>
<td>50%</td>
</tr>
<tr>
<td>Library</td>
<td>59</td>
<td>59</td>
<td>-</td>
<td>24</td>
<td>41%</td>
</tr>
<tr>
<td>Planning and Community Environment</td>
<td>66</td>
<td>66</td>
<td>-</td>
<td>29</td>
<td>44%</td>
</tr>
<tr>
<td>Police</td>
<td>974</td>
<td>974</td>
<td>-</td>
<td>638</td>
<td>66%</td>
</tr>
<tr>
<td>Public Works</td>
<td>100</td>
<td>100</td>
<td>-</td>
<td>52</td>
<td>52%</td>
</tr>
<tr>
<td><strong>Total Overtime</strong></td>
<td><strong>2,452</strong></td>
<td><strong>2,452</strong></td>
<td>-</td>
<td><strong>1,948</strong></td>
<td><strong>79%</strong></td>
</tr>
<tr>
<td><strong>Total Overtime Excluding Public Safety</strong></td>
<td><strong>495</strong></td>
<td><strong>495</strong></td>
<td>-</td>
<td><strong>223</strong></td>
<td><strong>45%</strong></td>
</tr>
</tbody>
</table>

Enterprise Funds
Major operating fund issues are discussed below. Please refer to the detail fund summaries in Exhibit A for more information on these midyear changes and to the CIP section for a discussion of the changes in Enterprise CIP project funding.

- **Electric Fund** (Net reserve reduction of $0.5 million) An additional $475,000 in legal expenses is required due to ongoing litigation with Enron and PG&E. An additional $23,000 in contract services for line clearing is needed to encumber the full contract bid amount with Davey Tree. The remaining expenditure increase includes $50,000 for contract services with Canopy to administer the Right Tree in the Right Place Program, the cost of which the Utilities Department has agreed to cover in fiscal 2004-05.

- **Gas Fund** (Net reserve reduction of $0.2 million) An increase of $60,000 in legal fees is due to additional legal assistance needed in the Gas Accord III settlement. An increase of $53,000 in contract services is required to assist in regulatory matters. The remaining expenditure increase includes $53,876 for contract services with PG&E for mandated training.
Adjustments to the City’s 2004-05 Capital Plan are noted in Exhibit A, with specific project adjustments described in Exhibit B. All of the CIP changes fall into three basic categories: transfer of project management due to CIP streamlining process, projects requiring additional appropriations, and other adjustments such as reducing project appropriations.

- **Civic Center Infrastructure Project – CIP PF-01002** – Additional funding needed for construction/design phase (Capital Fund, $630,000 Infrastructure Reserve funding).

- **Photovoltaic Design and Installation – CIP PE-05001** – Increase funding by $406,600 and decrease funding by the same amount to **Animal Shelter – CIP PE-04014**; funding is transferred due to elimination of CIP PE-04014 Animal Shelter as a candidate project for grant funding (No additional funding required).

- **Main Library Space Reconfiguration – CIP PE-05002** (New project) Funding for space reconfiguration to provide space for youth services collection and program area. (Reduce funding for Library Automation CIP LB-94018 $140,000; reduce Library Department operating budget $36,392; Capital Fund $176,000 Infrastructure Reserve funding.) See informational report in this packet for fuller description.

- **University Parking Structure – CIP PE-95030** – Project already completed. $8,421,237 reduction in project appropriation, as well as a transfer of unused funding to Debt Service Fund ($3,434,695) and to University Avenue Parking Structure Fund ($425,000).

- **Downtown Urban Design Improvements – CIP PE-96008** – Relocation of one Decaux toilet from Lytton Plaza to the Caltrain Transit Center (Capital Project Fund: $40,000 Infrastructure Reserve Funding).

- **Sidewalk Repairs – CIP PO-89003** – Reduce funding by $500,000 to align budget with project annual expense. No significant change in project scope (Reduce transfer from General Fund $500,000).

- **Utilities CIS Study – CIP EL-05002** – (New Project) Study on CIS system integration with SAP (Electric Fund: $82,000; Transfer project funding from SAP Continuous Improvement Project CIP-TE-05001 in Technology Fund; no funding from stabilization reserve).

- **Wastewater Solids Disposal Project – CIP WQ-97070** – Additional funding needed to upgrade and rehabilitate two multiple hearth incinerators (Wastewater Treatment Fund: $72,000 reserve funding).

- **Mail Processing System – CIP AS-05000** – (New Project) Funding for purchase of mailing machine in accordance with United States Postal Service standard (Printing and Mailing Fund: $33,000).

- **Children’s Library Improvement – CIP PE-04010** – Change in project description. Addition of 610 square feet (south addition) is planned in partnership with the Palo Alto Library...
Foundation (PALF) and Friends of Palo Alto Library (FOPAL). The south wing will have office and storage space for Children’s Library staff.

Other Funds

Special Revenue Funds: Two changes are proposed for the City’s Special Revenue Funds: a transfer from the Parking District Funds to cover the cost of erecting signage for the new downtown parking garages ($13,000); a correcting entry reversing a transfer from the Community Development Block Grant (CDBG) Fund to the Capital Fund that is not needed ($628,440).

Business Improvement District (BID): Appropriation of funds to allow the processing of authorized expenditures from collected fees on BID-related activities through June 30, 2005 (Business Improvement District Fund, $68,857).

Amendments to the 2004-05 Adopted Municipal Fee Schedule

Staff is proposing to amend the 2004-05 Municipal Fee Schedule (Exhibit C) to include four new fees and fourteen existing fee adjustments. Future year annual revenue increases are expected to be $189,500 due to these changes.

The new fees are concentrated in the Fire Department’s paramedic services and include: ALS II which is the highest level of paramedic service; BLS Transport – Single which is for inter-facility transport; BLS-1 for Special Event Stand By, and ECG 12 Lead which is a new, more advanced defibrillator. The fee adjustments are in the Administrative Services Department (adjust the Returned Check Fee), Community Services Department (Mitchell Park Community Center hourly room rentals: Teen Center, Main Hall, and Mitchell Park Community Center Patio), Fire Department (increasing the fees for ALS, BLS, BLS Scheduled Transport, 911 ALS Transport Mileage, Inter-facility BLS Transport Mileage, Night, Oxygen), and the Library Department (eliminating the Replace Lost Library Card fee, increasing the Test Monitoring Fee).

Table of Organization Changes

The proposed adjustments to the Table of Organization (Exhibit D) include three new items and one correction to a previously submitted item.

- Administration Services Department: Reclassification of 1.0 Full Time Equivalent (FTE) Financial Analyst to Senior Financial Analyst in the Real Estate Division due to restructuring of duties related to the acquisition and disposition of property rights. The division eliminated a vacant Senior Financial Analyst position in fiscal 2003-04, and now must upgrade the Financial Analyst position to a Senior Analyst position to match job duties. The $9,430 in additional annual expense is funded with cost reductions elsewhere within the division.

- Community Services Department: Correction of an error in the department restructuring presentation (CMR:427:04 of October 25, 2004) requires the elimination of both a 0.5 FTE Facilities Assistant and 0.5 FTE Program Assistant to add 1.0 FTE Office Specialist as described in the staff report. Costs associated with this change have been included in Budget Amendment Ordinance No. 4850.

- Library Department: Reinstatement of Saturday hours at the Downtown library branch requires the addition of a 0.5 FTE Library Assistant, funded by a one-time $35,000 transfer from the City Manager Contingency fund. This expense will be incorporated into the department’s 2005-06 budget proposal as an ongoing expense. Additionally, a new 1.0 FTE Library Assistant will be created by eliminating a vacant 0.5 FTE Senior Librarian and
reallocating $19,212 from temporary to regular salaries. This position will be assigned to the Mitchell Park Library to better support the high level of circulation at that branch.

- Police Department: Addition of 1.0 FTE Communication Technician—this position was eliminated in the 2004-05 budget, however it was reinstated as a result of Summer 2004 contract negotiations with the Service Employees International Union. The department is funding this position with other vacancy savings in the current year, but the $118,400 in salary and benefit expense will be incorporated into the department’s 2005-06 budget proposal as an ongoing expense.

2004-05 Midyear Capital Improvement Program Projects Status Report:
This report provides the Finance Committee with information on the status of the City’s Capital Improvement Program (CIP) projects as of December 31, 2004. In the attached matrix (Attachment 2), all City departments have submitted information on their projects and commented on any issues that might cause a change in the scope or timing of the projects. Information in this report is intended to keep Council abreast of progress on all CIP projects that were open at the beginning of the 2004-05 fiscal year and on those projects, which were added or completed during the current year.

The attached matrix categorizes CIP projects into minor projects (projects which can be completed within a one-year period) and multi-year projects (projects which have multi-year budgets and/or complex implementation schedules with identifiable phases). The projects status portion of the matrix identifies the phase the project was in as of December 31, 2004. Information on phases is intended to give Council a perspective on how much progress was made on a project. Three distinct phases are utilized, as follows:

<table>
<thead>
<tr>
<th>Phase:</th>
<th>Activities:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-Design</td>
<td>• Preparation of a feasibility study</td>
</tr>
<tr>
<td></td>
<td>• Development of a master plan</td>
</tr>
<tr>
<td></td>
<td>• Definition of a project scope</td>
</tr>
<tr>
<td></td>
<td>• Preparation of an Environmental Impact Report</td>
</tr>
<tr>
<td>Design</td>
<td>• Hiring a design consultant</td>
</tr>
<tr>
<td></td>
<td>• Completion of project design</td>
</tr>
<tr>
<td></td>
<td>• Soliciting bids or proposals</td>
</tr>
<tr>
<td>Construction</td>
<td>• Acquisition of major equipment</td>
</tr>
<tr>
<td></td>
<td>• Installation</td>
</tr>
<tr>
<td></td>
<td>• Implementation of a project</td>
</tr>
</tbody>
</table>

The comment section of the matrix provides Council with information clarifying the status of certain projects.

In the attached matrix, projects are listed by department for the General Fund and by fund for the Enterprise and Internal Service Funds. The matrix also includes information on the total budget from inception for each project, the available budget as of the beginning of the fiscal year, the fiscal year expenditures through December 2004, including commitments (encumbrances), and the remaining balance in the project budget as of midyear.
The matrix does not include "continuous" projects. These projects, such as water meter replacement, have no definitive beginning or end dates and receive ongoing funding to reflect the continuing replacement cycles or commitments. During the first half of 2004-05, progress was made on all of the "continuous" projects (Attachment 3).

RESOURCE IMPACT
Adoption of the attached ordinance will allow for adjustments to the fiscal year 2004-05 budget, along with amendments to the Table of Organization, the Municipal Fee Schedule and five General Fund CIP projects. With the approval of this ordinance, the projected ending balance of the General Fund BSR is $21.2 million, a decrease of $0.7 million (17.6 percent of General Fund expense). The Capital Fund Infrastructure Reserve is projected to end with a balance of $30.1 million, a reduction of $0.6 million. The projected ending Rate Stabilization Reserve total for all Enterprise funds is decreasing by $0.8 million mainly due to increases in legal and capital expense.

POLICY IMPLICATIONS
These recommendations are consistent with existing City policies.

ENVIRONMENTAL ASSESSMENT
This is not a project for purposes of the California Environmental Quality Act (CEQA).

ATTACHMENTS
Attachment 1: Budget Amendment Ordinance with the following exhibits:
   Exhibit A  Fund Summaries and detail changes to the General Fund, Enterprise Funds, Special Revenue Funds, Internal Service Funds, Debt Service Fund and Capital Improvement Funds
   Exhibit B  CIP Project Descriptions
   Exhibit C  Amendments to the 2004-05 Adopted Municipal Fee Schedule
   Exhibit D  Amendments to the 2004-05 Table of Organization
Attachment 2: 2004-05 Midyear Capital Improvement Projects Status
Attachment 3: List of Continuous Capital Projects
PREPARED BY:  

CHARLES PERL  
Budget Manager

DEPARTMENT HEAD APPROVAL:  

CARL YEATS  
Director, Administrative Services

CITY MANAGER APPROVAL:  

EMILY HARRISON  
Assistant City Manager