City of Palo Alto (ID # 10101)

City Council Staff Report

Report Type: Action Items **Meeting Date: 3/4/2019**

Council Priority: Fiscal Sustainability

Summary Title: FY 2020 - FY 2029 Long Range Financial Forecast

Title: Acceptance of the Fiscal Year 2020 - Fiscal Year 2029 Long Range Financial Forecast

From: City Manager

Lead Department: Administrative Services

Recommendation

Finance Committee and staff recommend that the City Council accept the Fiscal Year 2020 – Fiscal Year 2029 Long Range Financial Forecast (Attachment A) (LRFF) and include deltas in the assumptions from the Long Range Financial Forecast when the budget is presented.

Executive Summary

The LRFF, which details the projected financial outlook through the Fiscal Year (FY) 2020 – FY 2029, was presented to the Finance Committee on November 28, 2018 (Attachment A, staff report 9764, www.cityofpaloalto.org/civicax/filebank/documents/67825). Action minutes of the Finance Committee meeting are attached as well for reference (Attachment B, www.cityofpaloalto.org/civicax/filebank/documents/68123). Of major note, for the first time, this LRFF incorporates direction from the City Council to budget pension costs more conservatively than CalPERS' projections. Detailed explanation and analysis of the LRFF and assumptions can be found in the original staff report presented to the Finance Committee.

The Finance Committee accepted the LRFF by a 3-1 vote (Chair Scharff, then-Vice Mayor Filseth, Councilmember Kou voted for; Councilmember Tanaka voted against) and directed that the LRFF be forwarded to the City Council for approval. In addition, the Committee directed staff to describe changes to the assumptions used in the LRFF as part of the annual budget process. There were motions to amend the recommendation, including changing the Compound Annual Growth Rate (CAGR), including the Unfunded Actuarial Liability (UAL) for both pension and retiree healthcare, and lowering the assumption about Property Tax revenue growth. These motions each failed due to lack of a second.

ATTACHMENT A: FY 2020 – FY 2029 Long Range Financial Forecast

The FY 2020 – FY 2029 Long Range Financial Forecast marks the beginning of the FY 2020 annual budget development process. It includes projected General Fund financials over the next ten years based on current City Council approved service levels as well as two alternative financial models. The current base case financial forecast projects a $2.8 million gap in the General Fund in FY 2020 and a range between annual gaps of up to $4.5 million to surpluses of $18.2 million in the final years of the forecast. The base case is intended to provide a launching point that can assist in measuring the impacts of major policy interventions against a likely 'status quo' version of the future. The forecast assumes that the City will continue to provide the same levels of service and that external events continue to unfold based on current expectations.

Attachment A to this report contains the full FY 2020 – FY 2029 LRFF as presented to the Finance Committee in November 2018. The LRFF discusses the financial climate of both the national and local economy and reviews the base case for the LRFF including revenue and expense modeling assumptions, as well as two alternative scenarios 1) Normal Cost calculated at CalPERS Discount Rate (phase-in to 7.0 percent by FY 2021) and 2) Major Tax Revenue Sensitivity Analysis. As discussed above, it is important to note that the FY 2020 – FY 2029 LRFF includes, for the first time, a lower rate of return for pension fund earnings (6.2%) than CalPERS' current projections (7.0%), for the calculation of a portion of pension contributions (normal cost only). This change in methodology is consistent with City Council direction and increases anticipated expenses by $3.9 million in FY 2020.

Looking forward, the City will face a number of pressures as it strives to ensure financial sustainability, one of its City Council approved priorities for 2019. The City will continue to proactively identify solutions to ensure cost-effective service delivery and the City's long-term financial sustainability. The FY 2019 Adopted Operating Budget the City reduced ongoing expenses by more than $2.3 million in the General Fund. Since budget adoption and in continuing discussion with the Finance Committee regarding fiscal sustainability, another $4.0 million in budget reductions, of which $0.6 million is ongoing, has been identified to close the General Fund gap in FY 2019. The City is also currently reviewing all City services as part of the strategic action approved by City Council on December 17, 2018 (see staff report 9925, https://www.cityofpaloalto.org/civicax/filebank/documents/68153).

Recognizing that the City will actively continue discussions with some of is bargaining units and with the Finance Committee surrounding the salary and benefit assumptions, staff has included a third alternative scenario with this report. This scenario is meant to help address questions from the Finance Committee regarding the variability seen year-over-year in salaries and benefits growth throughout the forecast. The scenario is meant to be used as a forecasting tool that models the impact of changes in the budgetary assumptions for salaries, not as a commitment to future negotiations. This additional scenario models the impact of a one percent change in budgetary assumptions for bargaining units beyond the term of the existing Memoranda of Agreements (MOAs) and is discussed in greater detail below.

Alternative Forecast #3: Change in Long Range Financial Forecast Assumptions Related to Salary for Bargaining Units Outside of MOA Terms

During the Finance Committee's discussion of the LRFF, there was conversation about the appropriate methodology for modeling salary and benefit increases year-over-year. The LRFF assumes two percent general wage adjustments in the forecast years beyond the terms of the existing MOAs (discussed in Attachment A). This is consistent with prior City Council direction to use the two percent figure as a forecasting assumption, not as a commitment for future negotiations. As part of the expense sensitivity analysis on the City's finances, a third alternative forecast is presented here that analyzes a general wage adjustment of three percent for all employees in years when MOAs have not yet been negotiated. As with the other models in the LRFF, this model is for forecasting purposes and is not a commitment to future labor negotiations.

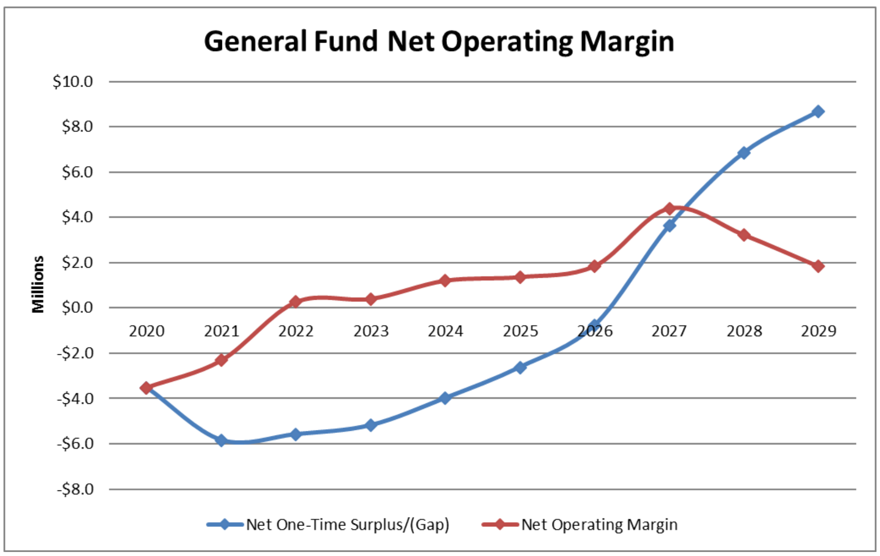
In this third alternative scenario, wider gaps between revenues and expenses in the initial years would occur, as expected. Through the ten years of the forecast, this change in the modeling assumptions would increase expenses significantly. In FY 2020 through FY 2022, expenses would increase by $715,000, $1.3 million, and $2.4 million, respectively. The City has MOAs in place with its safety units through the conclusion of FY 2021, therefore the budgetary impact of the one percent increase to these groups can first be seen in FY 2022: International Association of Fire Fighters (IAFF), Fire Chief's Association (FCA), Palo Alto Peace Officers' Association (PAPOA), and Police Management Association (PMA). FY 2022 illustrates the full cost of an additional one percent raise for the General Fund, as this is the first year of the forecast in which this change would impact all bargaining units.

Overall, the general trends of the base case continue even in this third alternative scenario. The base case projected that by FY 2024, the City would have a positive net one-time surplus; in this third alternative scenario the City does not generate a positive net one-time surplus until FY 2027. The City would maintain a nominal surplus beginning in FY 2022 if the gaps of FY 2020 and FY 2021 were solved in a structural (ongoing) manner.

Table 13: FY 2020 – FY 2029 Long Range Financial Forecast Alternative Forecast #3

	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Total Revenue	**$214,497**	**$227,108**	**$233,938**	**$241,315**	$248,921	$256,571	$264,392	$273,133	$281,311	$290,856	$299,948
		5.9%	*3.0%*	*3.2%*	*3.2%*	*3.1%*	*3.0%*	*3.3%*	*3.0%*	*3.4%*	*3.1%*
Total Expenditures	**$210,706**	**$230,631**	**$239,780**	**$246,901**	$254,108	$260,555	$267,014	$273,902	$277,681	$284,005	$291,272
		9.5%	*4.0%*	*3.0%*	*2.9%*	*2.5%*	*2.5%*	*2.6%*	*1.4%*	*2.3%*	*2.6%*
Net One-Time Surplus/(Gap)	$3,791	($3,522)	($5,842)	($5,586)	($5,187)	($3,984)	($2,621)	($768)	$3,630	$6,851	$8,677
Cumulative Net Operating Margin (One-Time)											-$8,354
Net Operating Margin		(3,522)	(2,320)	257	399	1,203	1,363	1,853	4,398	3,221	1,826
Cumulative Net Operating Margin											$8,677

Table 14: FY 2020 – FY 2029 Long Range Financial Forecast Net Operating Margin Alternative Forecast #3



Attachments:

- ATTACHMENT A: FY 2020 - FY 2029 Long Range Financial Forecast
- ATTACHMENT B: 11-28-2018 Finance Committee Action Minutes

City of Palo Alto (ID # 9764)

Finance Committee Staff Report

Report Type: Action Items **Meeting Date: 11/28/2018**

Summary Title: FY 2020 - FY 2029 Long Range Financial Forecast

Title: Review and Forward the FY 2020 - FY 2029 Long Range Financial Forecast

From: City Manager

Lead Department: Administrative Services

RECOMMENDATION

Staff recommends that the Finance Committee review, comment, and forward the Fiscal Year 2020 to 2029 General Fund Long Range Financial Forecast (Base Case) for City Council approval.

EXECUTIVE SUMMARY

The Fiscal Year (FY) 2020 to 2029 General Fund Long Range Financial Forecast (LRFF), marks the beginning of the FY 2020 annual budget process. It includes projected General Fund financials over the next ten years based on current City Council approved service levels as well as alternative financial models. The current Base Case financial forecast projects a gap in the General Fund of $2.8 million in FY 2020 and a range between annual gaps of up to $4.5 million to significant surpluses in the final years of the forecast. The Base Case provides a preliminary forecast that can assist in gauging effects of major policy interventions against a likely "status quo" version of the future. It assumes that the world continues to change and unfold in line with current expectations.

City staff will continue to review and refine these projections to establish the FY 2020 Base Budget and provide direction to Departments on the FY 2020 budget process. Based on this Forecast, it is anticipated that guidance to prioritize spending will again be critical to ensure financial stability.

Looking forward, the City continues to face several pressures from the 2014 Council approved Infrastructure Plan including a new public safety building, the growing costs of pension benefits, and the ongoing labor negotiations for many of the City's largest employee units. The policy direction from the City Council regarding proactively addressing the pension obligations, including the most recent direction to assume a lower discount rate in calculating pension costs, is contained in the base case forecast model. If this direction were excluded from the model, the General Fund would reflect the tough choices and the hard work of the City during the FY 2019 Budget process to structurally balance the budget. The City will continue to face critical choices in order to balance future financial challenges and any unforeseen program needs or an economic downturn. The review of this Long Range Financial Forecast and the planning that follows it will be critical since the City is facing many requests and has identified several key programs that the community would like to fund and complete.

Included in this report and subsequent documents are the following:

- Overview of the current financial status of the General Fund as of the FY 2019 Adopted Budget
- Discussion of the current financial climate of the United States to the City of Palo Alto
- Review of the Base Case for the Long Range Financial Forecast including Revenue and Expense modeling assumptions
- Alternative Scenarios including a) normal cost calculated at CalPERS Discount Rate (phase-in to 7.0 Percent by FY 2021) and b) an economic downturn modeled in FY 2022 of the forecast

BACKGROUND

Annually the Office of Management and Budget produces a ten-year Long Range Financial Forecast (LRFF). The LRFF reflects staff's best estimates on the projected revenues and expenditures over the next ten years based on the information currently available. It is important to note that the LRFF is a planning document and is separate and distinct from the development of the City's Adopted Operating Budget. There are assumptions and parameters modeled in the LRFF, but these assumptions are revised and refined as more information becomes available through the budget adoption process.

The LRFF does contain a comprehensive review of the costs to provide current City Council approved service levels, including looking at current contracts, updates to salaries and benefits based on the current population of employees and the current labor contracts in effect. The LRFF also reviews the status of the current economy and various economically sensitive revenues such as Sales Tax, Documentary Tax, Property Tax, and Transient Occupancy Tax to explain key trends in those areas. This Forecast allows staff and City Council to look at both the short-term and long-term financial status of current service levels in the General Fund and inform daily policy decisions and ongoing long-term goals and challenges.

Since the great recession, the City has approved many strategies to mitigate rising costs, especially the rising increase in salaries and benefits. Strategies that have been used include: a second pension tier, employees sharing in health plan cost increases, and ending the employer-paid member contributions for pensions. Negotiations with bargaining units have included employees not only paying their full portion of CalPERS contributions but also beginning a cost-sharing program wherein employees contribute a certain percentage of the City's required pension contribution.

The City Council continues to invest in the community and approved significant improvements in June 2014 with the Infrastructure Plan in the original amount of $125.8 million. However, other projects identified in the plan are estimated to cost substantially more due to updated designs, rising construction costs, and minimum and prevailing wage requirements. These changes have led to an anticipated funding gap of approximately $76 million for the Infrastructure Plan projects. Capital projects are one example of known items that are not fully included in this Forecast, both the capital cost to build as well as the operating and maintenance costs once these projects are completed and these new facilities are actively used will be refined as information becomes available.

Palo Alto serves a diverse community with a broad range of unique services that adds to the significant complexity of managing a balanced budget and healthy long-range financial outlook. The demands and conflicts emerging from our vibrant economy have heightened the intensity of the “Palo Alto Process” with new analyses and data generation demands and deep dives into complex problem solving within an engaged public process across a wide range of issues. These forecast figures present staff with the challenge of prioritizing the growing needs of the City with the long-term sustainability of these needs.

The Economy

The economy is healthy at a national level. As of the end of September, the national gross domestic product (GDP) increased 3.5 percent while the national consumer price index (CPI) has grown 2.3 percent. The economy has gained from a rebound in consumer spending, employment growth, and substantial tax cuts. The nation is operating at what is considered “full employment” levels, at 3.7 percent unemployment as of September 2018. At the same time, massive tax cuts have driven budget deficits and higher interest rates. It is anticipated that the national job market may slow and the make-up of the market may change as immigration decelerates and labor participation from the Baby-Boomer generation shrinks.

The local economy continues to outpace the unemployment rate at the state and national level. As of the end of September, California maintained 4.1 percent unemployment and the unemployment rate for the Bay Area region was lower at 2.5 percent. Despite local housing and transportation challenges, companies continue to plan expansion in Palo Alto and communities that surround our City. Compared to other regions in California, the Bay Area experienced the strongest job growth at 2.1 percent last quarter and is expected to slow in the short term. Although there is enough economic momentum to generate growth for the remainder of the year, reports from the Center for Continuing Study of the California Economy, UCLA’s Anderson School of Management, and Bank of the West Economics point to sharply lower economic growth in the short term and higher interest over the next two fiscal years. It is expected that GDP will fall to near 1 percent in the next 12 to 18 months. Regionally, demand for employees has driven the local real estate market so far up that, for some communities, it has become prohibitively expensive for businesses. Bay Area job growth is anticipated to decelerate from 2 percent in 2019 to 0.3 percent in 2020.

The foundations of the local economy – stable housing market, diverse and favorable mix of business segments, and academic and medical properties – provide the City a bulwark against an economic downturn in the medium term.

DISCUSSION

Included in this section are both the Base Case and alternative scenarios. As with all forecasts, there is uncertainty regarding the revenue and expenditure estimates contained in this document. For example, General Fund revenues may exceed or fall below expectations based on changes in economic or non-economic conditions. Various cost elements can also vary from year to year.

Base Case

The following table displays the projected General Fund revenues and expenditures over the next decade and the total cumulative surplus. In addition to the cumulative surplus, the incremental surplus or shortfall (assuming each preceding surplus or shortfall is addressed completely with ongoing solutions in the year it appears) for each year of the forecast is included. Because it is the City's goal to remain in balance on an ongoing basis, the incremental figure is useful in that it shows the additional surplus and/or shortfall attributed to a particular fiscal year. To the extent that a shortfall is not resolved, or a surplus is not expended on an ongoing basis, it is important to understand that the remaining budget gap or surplus will carry over to the following year. For example, in FY 2019, the City structurally balanced both FY 19 and FY 2020 with known variables at the time. This reduced expenses on an ongoing basis by more than $2.3 million. Had this discipline not been exercised and had reserves been used instead, the FY 2020 gap would be even larger, estimated to be at least $5.1 million.

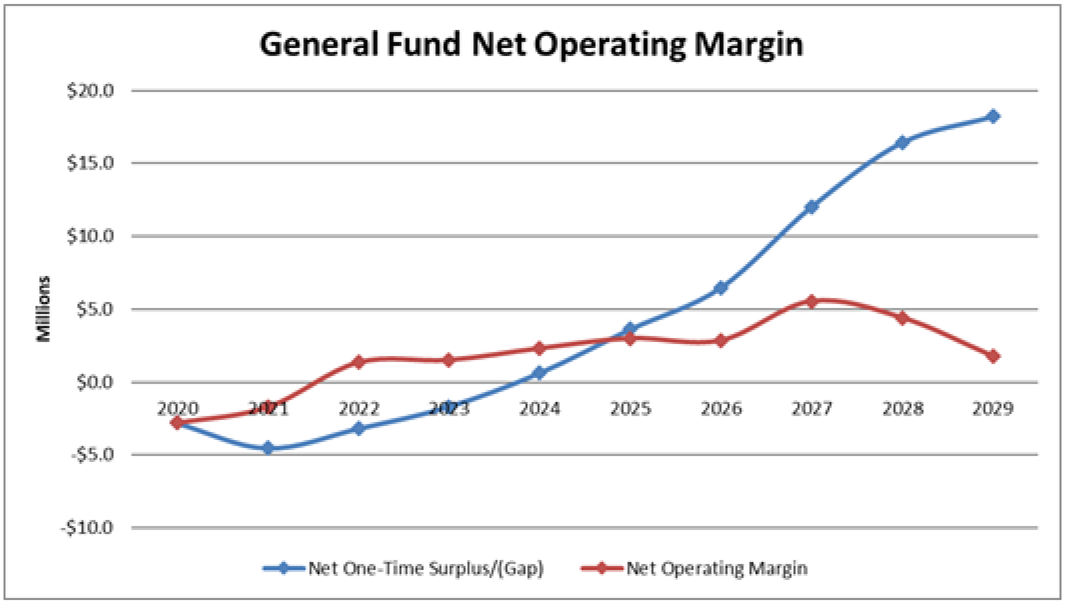
Instead, this FY 2020-2029 Long Range Financial Forecast anticipates smaller gaps ranging from $2.8 million in FY 2020 to a gap of $4.5 million in FY 2021 with surpluses beginning in FY 2024 at $0.8 million and increasing through the term of the forecast.

TABLE 1: FY 2020-2029 Long Range Financial Forecast
Base Case

	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Total Revenue	$214,497	$227,108	$233,938	$241,315	$248,921	$256,571	$264,392	$273,133	$281,311	$290,856	$299,948
		5.9%	*3.0%*	*3.2%*	*3.2%*	*3.1%*	*3.0%*	*3.3%*	*3.0%*	*3.4%*	*3.1%*
Total Expenditures	$210,706	$229,916	$238,472	$244,508	$250,606	$255,948	$260,771	$266,655	$269,292	$274,424	$281,731
		9.1%	*3.7%*	*2.5%*	*2.5%*	*2.1%*	*1.9%*	*2.3%*	*1.0%*	*1.9%*	*2.7%*
Net One-Time Surplus/(Gap)	$3,791	($2,807)	($4,534)	($3,193)	($1,685)	$623	$3,622	$6,478	$12,019	$16,432	$18,217
Cumulative Net Operating Margin (One-Time)											$45,171
Net Operating Margin		($2,807)	($1,727)	$1,341	$1,508	$2,308	$2,998	$2,857	$5,541	$4,413	$1,785
Cumulative Net Operating Margin											$18,217

Assumes that the annual shortfalls are solved with ongoing solutions and annual surpluses are spent for ongoing expenditures.

TABLE 2: FY 2020-2029 Long Range Financial Forecast Net Operating Margin Base Case



Revenue Assumptions

As discussed in the Economy section of this report, the Bay Area economy is anticipated to outperform the state and the nation. Despite a projected slowdown in Bay Area job growth, major expansion for Silicon Valley companies and a stable local housing market result in healthy and robust tax revenues for the City throughout the term of the forecast. Tax revenues constitute nearly 60 percent of General Fund resources. In FY 2020, the forecast projects a $9.1 million, or 7.2 percent, tax revenue increase compared to the levels in the Adopted FY 2019 Budget. In total, revenues are anticipated to increase by $12.6 million, or 5.9%, from the Adopted FY 2019 Budget of $214.5 million to $227.1 million in FY 2020.

TABLE 3: FY 2020 - 2029 General Fund Revenue Forecast
Base Case

Revenue & Other Sources	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	CAGR 10 Years
Sales Taxes	$31,246	$34,286	$35,754	$37,000	$38,154	$39,302	$40,426	$41,546	$42,759	$44,063	$45,498	3.8%
Property Taxes	45,332	48,193	51,181	54,231	57,235	60,285	63,426	67,289	71,508	76,078	80,970	6.0%
Transient Occupancy Tax- General Purpos	16,699	17,977	18,444	18,933	19,473	20,018	20,618	21,260	21,908	22,556	23,188	3.3%
Transient Occupancy Tax- Infrastructure	8,350	8,406	8,625	8,853	9,106	9,361	9,641	9,941	10,244	10,547	10,843	2.6%
Documentary Transfer Tax	7,434	8,359	8,631	8,905	9,174	9,484	9,851	10,188	10,547	10,928	11,325	4.3%
Utility Users Tax	16,092	17,026	17,519	18,024	18,407	18,768	19,109	19,497	19,811	20,168	20,526	2.5%
Other Taxes and Fines	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	0.0%
Subtotal: Taxes	127,185	136,279	142,186	147,978	153,581	159,250	165,103	171,753	178,809	186,372	194,382	4.3%
Charges for Services	20,630	22,057	22,870	23,551	24,230	24,788	25,323	25,955	26,010	26,464	26,534	2.5%
Stanford Fire & Dispatch Services	7,384	7,829	7,992	8,128	8,273	8,395	8,486	8,580	8,651	8,763	8,810	1.8%
Permits and Licenses	8,949	9,065	9,169	9,252	9,337	9,406	9,474	9,555	9,563	9,620	9,669	0.8%
Return on Investments	1,166	1,197	1,230	1,266	1,304	1,346	1,390	1,432	1,475	1,519	1,563	3.0%
Rental Income	15,807	16,120	15,272	14,766	15,153	15,551	15,961	16,384	16,819	17,267	17,729	1.2%
From Other Agencies	1,150	370	370	370	370	370	370	370	370	370	370	-10.7%
Charges to Other Funds	10,093	11,103	11,471	11,770	12,092	12,357	12,595	12,894	12,837	13,100	13,300	2.8%
Other Revenue	2,361	2,361	2,313	2,314	2,315	2,316	2,316	2,317	2,318	2,319	2,321	-0.2%
Total Non-Tax Revenue	67,540	70,102	70,688	71,418	73,073	74,528	75,915	77,487	78,043	79,422	80,296	1.7%
Operating Transfers-In	19,772	20,727	21,063	21,918	22,267	22,793	23,374	23,893	24,459	25,062	25,271	2.5%
BSR Contribution (One-Time)												
Golf Operating Loss Reserve Liquidation												
Total Source of Funds	$214,497	$227,108	$233,938	$241,315	$248,921	$256,571	$264,392	$273,133	$281,311	$290,856	$299,948	

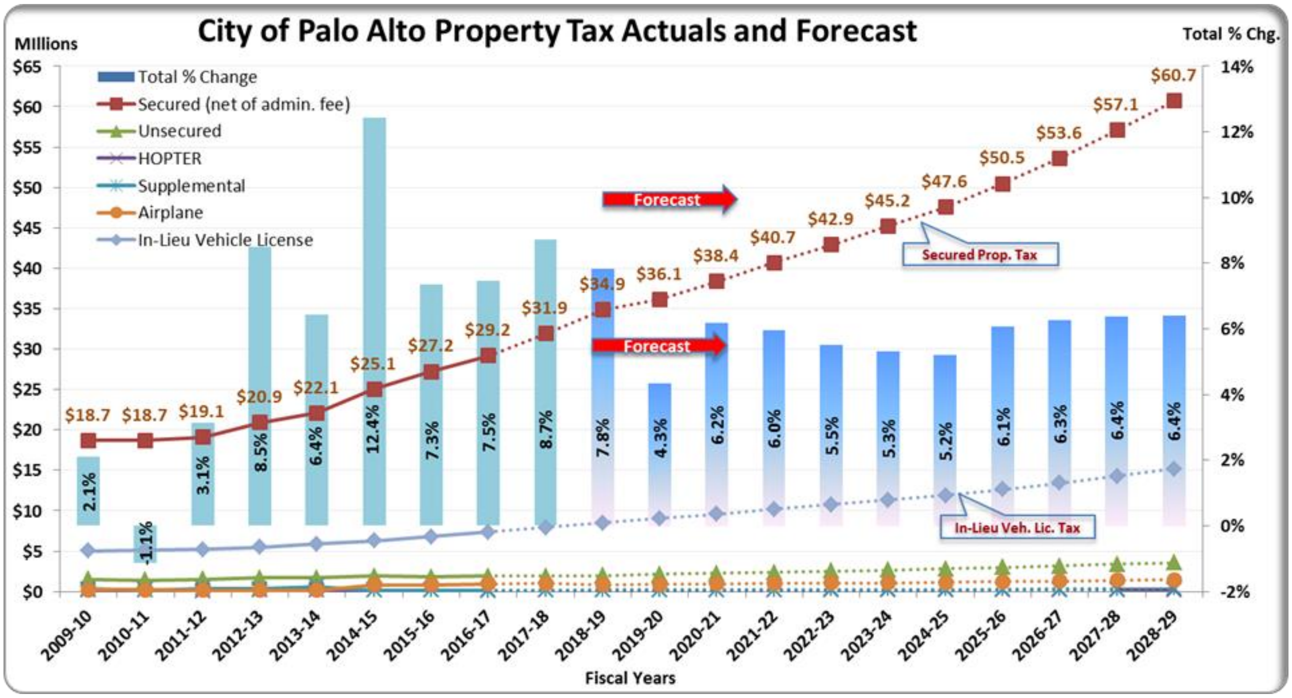
Sales Tax

The sales tax revenue forecast is driven by strong personal income and spending growth and a larger share of consumer spending online. New and innovative retail formats have helped revive physical retail presence. Stores that were once strictly online are now finding physical presence within communities. As the nation transitions from a shopping center country to online, a surge in online retail sales displace tax revenue from traditional industry segments to state and county pools. Based on activity and receipts for the recent quarter close, it is estimated that sales tax revenue will exceed the FY 2019 Adopted Budget by $1.2 million, or 3.9 percent, and will generate a total of $32.4 million by year-end. In FY 2020, sales tax is expected increase to $34.3 million, or 9.7 percent, above the FY 2019 Budget. This revenue category is currently tracking above budgeted levels in FY 2019 and it is anticipated that appropriate adjustments will be brought forward for the FY 2019 Budget through the mid-year budget process. Segments contributing to this growth include electronic equipment, restaurants, furniture/appliance, and auto leases. Department and drug store sales continue to experience declines. The FY 2020 – FY 2029 LRFF anticipates a compounded annual growth rate (CAGR) of 3.8% through the term of the forecast, with FY 2020's significant growth over FY 2019's Adopted Budget level tapering down through the out-years.

Property Tax

Property tax revenue is the General Fund's largest revenue source and represents 21 percent of total revenues. Over the last three-year period, property tax revenue has grown 17 percent, from $36.6 million in FY 2016 to $42.8 million (unaudited) in FY 2018. The FY 2019 Adopted Budget assumes $45.3 million in total property tax and is expected to grow to $46.2 million, or $0.9 million, by year-end. This trend continues in FY 2020, where property tax revenue is expected to increase by additional $2.0 million, or 4.2 percent, to total $48.2 million.

TABLE 4: City of Palo Alto Property Tax Actuals and Forecast through FY 2029



City staff meets with the County quarterly to obtain the latest assessed valuation and assessment roll data used to forecast of property tax revenues. The above graph displays nine years of actual revenue and 11 years of forecast, including the year-end projection for FY 2019. The forecast assumes the anticipated cooling of the housing market and an economic downturn that is spread over the length of the 10-year forecast. Over the 20-year period displayed, there has been some unpredictability in the revenue growth rate, from a negative 1.1 percent in FY 2011 to a high of 11.5 percent in FY 2015.

Meeting the property tax revenue forecast is contingent on maintaining property turn over and the median sales price. Data for the first four months of FY 2019 show that compared to the same time prior year, property sales volume is 7.3 percent lower while price is 9.8 percent higher. According to Zillow, as of November 2018, residential median sales price in Palo Alto is $3.3 million, an increase of 8.0 percent over the prior year.

Included in this revenue source category are excess Educational Revenue Augmentation Funds, or ERAF, which is not considered a permanent local revenue source. The FY 2019 forecast assumes $2.3 million in excess ERAF funds and this amount is reduced to $1.3 million in FY 2020 to reflect closer alignment with historical collection levels.

Transient Occupancy Tax (TOT)

In FY 2019, TOT revenue is expected to reach $25.5 million, $0.5 million or 2.2 percent above the FY 2018 unaudited revenue amount. Compared to the FY 2019 Adopted Budget, this is a slight increase of 1.7 percent, or $0.4 million. TOT realized double digit growth in FY's 2015 and 2016 due the 2 percent rate increase (from 12 percent to 14 percent tax rate), the recovering economy, and the addition of the three large hotels. Since then, TOT revenue has moderated therefore modest growth is anticipated for FY 2020 and beyond. FY 2020 is forecasted to be $0.9 million, or 3.6 percent, above the current FY 2019 estimate, totaling $26.4 million.

Average occupancy rates average 84.1 percent for the first two month of the fiscal year, compared to 81.7 percent in the same prior year period. At the same time, average room rates have increased from $265 to $272 per day, a 2.6 percent increase, compared to prior year. According to August 2019 TRENDS® in the Hotel Industry – Northern California Performance Report, the average daily room rate in Palo Alto is higher than that of the San Jose/Peninsula Area, while hotel occupancy is trending the same as the region.

TABLE 5: Northern California Hotel – Motel Business Trends as of August 2018

STATISTICS AND TRENDS OF HOTEL-MOTEL BUSINESS
NORTHERN CALIFORNIA MONTHLY TRENDS
MONTH OF AUGUST

REPORT OF ROOMS BUSINESS BY LOCATION

	AVERAGE DAILY ROOM RATE			OCCUPANCY PERCENT			REVENUE PER AVAILABLE ROOM		
	2018	2017	VAR	2018	2017	VAR	2018	2017	VAR
SAN FRANCISCO	$282.65	$275.93	2.4%	90.1%	92.8%	-2.9%	$254.59	$255.94	-0.5%
SAN FRANCISCO AIRPORT	209.04	212.64	-1.7%	91.9%	91.7%	0.2%	192.04	194.89	-1.5%
SAN JOSE/PENINSULA	220.18	211.51	4.1%	85.5%	86.6%	-1.3%	188.22	183.16	2.8%
OAKLAND/EAST BAY	178.95	171.32	4.5%	85.1%	86.0%	-1.1%	152.33	147.41	3.3%
MONTEREY/CARMEL	395.94	379.85	4.2%	88.6%	85.9%	3.2%	350.83	326.26	7.5%
CENTRAL VALLEY	108.36	104.15	4.0%	78.2%	80.8%	-3.2%	84.71	84.12	0.7%
SACRAMENTO	133.76	128.48	4.1%	82.5%	82.4%	0.1%	110.32	105.90	4.2%
MARIN COUNTY	203.63	195.59	4.1%	86.8%	88.2%	-1.6%	176.82	172.58	2.5%
NAPA COUNTY	294.34	294.56	-0.1%	82.7%	80.0%	3.3%	243.44	235.76	3.3%
SONOMA COUNTY	216.57	211.05	2.6%	84.8%	85.4%	-0.7%	183.66	180.31	1.9%
OTHER NORTHERN CALIFORNIA	136.03	129.08	5.4%	81.8%	82.4%	-0.7%	111.26	106.32	4.6%
OVERALL AVERAGE	$214.75	$208.57	3.0%	85.8%	86.8%	-1.2%	$184.18	$181.06	1.7%

Table source: TRENDS® in the Hotel Industry Northern California, compiled and produced by CBRE Hotels, Consulting

Recently, the voters approved an additional increase in the rate of Transient Occupancy Tax of 1.5 percentage points, from a tax rate of 14.0 percent to 15.5 percent. Due to the timing of this approval, no revenues anticipated as a result of this increase have been factored into this forecast. This rate increase is estimated to generate additional receipts of approximately $2.6 million annually.

<u>Utility User's Tax (UUT)</u>

The UUT is levied on electric, gas, and water consumption, as well as on telephone usage. In total, FY 2019 revenues were originally budgeted at $16.1 million and are currently estimated at $16.3 million in FY 2019 before rising to $17.0 million in FY 2020.

UUT telephone revenues rose from $5.5 million in FY 2017 to $6.0 million in FY 2018 (unaudited). This revenue has realized double digit growth and is forecasted to reach $6.3 million in FY 2020.

UUT revenue from Utility sales came in at $9.4 million in FY 2018 and is anticipated to reach nearly $10.1 million in FY 2019. Rate increases of 6.0 percent for electric, 4.0 percent for gas, and 3.0 percent for water consistent with the financial plans discussed in Spring 2018 with Finance Committee and City Council, are the primary drivers of this revenue growth. This revenue is expected to rise to $10.7 million in FY 2020.

<u>Documentary Transfer Tax</u>

In FY 2015, documentary transfer taxes peaked at $10.1 million. This milestone was a consequence of several large commercial transactions on Page Mill Road and in the Stanford Research Park. Since that time, transfer taxes have moderated somewhat, with $9.2 million earned in FY 2018. Given that revenue from July through October in FY 2019 is running nearly 9.8 percent above the same period in FY 2018, staff will likely modify the FY 2019 Adopted Budget at midyear from $7.4 million up to $8.3 million. For FY 2020, revenues are expected remain consistent with FY 2019 projected levels at $8.4 million.

As in past years, this revenue source is challenging to forecast since it is highly dependent on sales volume and the mix of commercial and residential sales. The transactions through October (217) are running lower than those through October of last year (234), however, the total value of these transactions has increased by 9.8 percent. The Palo Alto housing market remains stable despite the decline in number of transactions because the growth in total value is robust. Although pressure on the housing market and local economy will either drive or slow down property turnover, there is enough of a baseline trend in the Palo Alto housing market to signal a stable 3.1 to 3.9 percent growth in revenue over the length of this forecast.

Rental Income

Rental Income of $16.1 million primarily reflects rent from the City's Enterprise Funds and the Cubberley Community Center and reflects growth of approximately 2 percent from the FY 2019 Adopted Budget of $15.8 million. The declines at the beginning of the forecast in FY 2021 and FY 2022 represent the phase-out of payments from the Refuse Fund associated with the Landfill and the steady growth after that models a general 3.0 percent increase for this area partially offset by minor adjustments throughout the forecast. Rental revenue annual increase is typically based on a review of the change in the California Consumer Price Index (CCPI) in the San Francisco Bay Area from the December to December period. It is expected that revenues will be reviewed and revised subsequent to this forecast based on updated information.

Charges for Services and Permits and Licenses

Revenues in the 'Charges for Services' and the 'Permits and Licenses' categories are anticipated to be $22.1 million and $9.1 million, respectively, in Fiscal Year 2020. This represents growth from the Fiscal Year 2019 Adopted Budget levels of $20.6 million for 'Charges for Services' and $8.9 million for 'Permits and Licenses'. These increases in revenue estimates are primarily driven by the cost to provide services to the community, ranging from recreational activities to development activities. Therefore, revenues are impacted by personal service costs, the primary cost driver for providing these services, and are modeled to grow in line with the average increase in general salaries and benefits increases included in the Forecast. In the base case, the Normal Cost of pensions associated with the Discount Rate of 6.2% is not included in cost-recovery modeling in these categories. As part of the FY 2020 Budget and the municipal fee development process, the City will need to examine the implications of including this marginal cost in charges for services and permits and licenses. Additionally, this budget category includes revenues associated with the recently renovated Golf Course.

Stanford Fire and Dispatch Services

The City has two separate agreements with Stanford University to provide its response and emergency dispatch services. The City and Stanford have entered into a new agreement effective July 1, 2018 outlining both terms for service levels and a new cost allocation methodology as the baseline for the contract costs. The new fire agreement services contract extends through June 30, 2023 with a renewal through 2028 unless otherwise terminated.

As part of this new contract, a new staffing deployment model for suppression and medical services was approved by the City Council in October 2017 and deployed in January 2018. This forecast assumes this new staffing model and in accordance with the new contract, increases to this revenue from Stanford have been aligned with the average growth of the expenses in the Fire Department over the forecast period.

Charges to Other Funds

The main source of revenues in this category is General Fund administrative cost allocation plan charges to the Enterprise and Internal Service Funds. Internal support departments such as Administrative Services, Human Resources, and Council Appointees provide services to Enterprise and Internal Service Funds. The costs for these services are recovered through the administrative cost allocation plan charges. The FY 2020 estimate for Charges to Other Funds of $11.1 million reflects growth of 10.0 percent from the FY 2019 Adopted Budget of $10.1 million. This is attributed to the assumed increases in salary and benefits costs and the restoration of expenses such as workers' compensation and general liability that were subsidized by the respective Internal Service Fund on a one-time basis in FY 2019. After the first year of FY 2020, growth is more moderate ranging from 0 percent up to 3.3 percent annual increases throughout the forecast period.

Operating Transfers-in

Operating Transfers-in materialize as expenses in other funds throughout the City and as a revenue in the General Fund. This budget category includes the equity transfer from the Electric and Gas funds. In accordance with a methodology approved by the City Council in June 2009, the equity transfer is calculated by applying a rate of return on the capital asset base of the Electric and Gas funds. This rate of return is based on PG&E's rate of return on equity as approved by the California Public Utilities Commission (CPUC). Using the Utility Department's projections from the Electric and Gas Five Year Financial Forecasts, as approved by the City Council in spring 2018, the equity transfer from the Electric and Gas funds are projected to increase over the course of this forecast from $19.9 million in FY 2020 to $24.8 million in FY 2029. Overall, the Operating Transfers-in are estimated to increase slightly to $20.7 million in FY 2020, a 4.8 percent increase from the FY 2019 Adopted Budget level of $19.8 million.

Expense Assumptions

As part of developing the FY 2020 Forecast expenditure budget, the General Fund expense categories have been adjusted by removing FY 2019 Adopted Budget one-time expenses and updating major cost elements such as salary and benefits costs. The tables below display the expense forecast and when compared to the FY 2018 Adopted Budget, growth of 2.6 percent is expected in FY 2019, with growth ranging from 1.5 percent to 3.7 percent throughout the ten-year forecast.

TABLE 6: FY 2020-2029 General Fund Expense Forecast
Base Case

Expenditures & Other Uses	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	CAGR 10 Years
Salary	$ 70,469	$ 78,029	$ 80,751	$ 82,730	$ 84,835	$ 86,761	$ 88,548	$ 90,317	$ 92,083	$ 93,845	$ 95,607	3.1%
Benefits	54,935	60,378	62,416	64,366	66,295	67,733	68,771	70,277	69,192	70,141	71,278	2.6%
Subtotal: Salary & Benefits	125,404	138,408	143,167	147,097	151,130	154,494	157,318	160,594	161,275	163,986	166,884	2.9%
Contract Services	22,025	21,607	22,030	22,552	23,018	23,454	23,881	24,313	24,750	25,178	25,478	1.5%
Supplies & Material	3,521	3,558	3,628	3,697	3,767	3,837	3,907	3,977	4,046	4,116	4,189	1.8%
General Expense	6,183	10,454	10,726	11,005	11,289	11,580	11,877	12,682	12,901	13,531	14,364	8.8%
Debt Service	613	0	0	0	0	0	0	0	0	0	0	N/A
Rents & Leases	1,690	1,751	1,804	1,858	1,914	1,971	2,030	2,091	2,154	2,218	2,285	3.1%
Facilities & Equipment	522	532	543	553	564	574	584	595	605	616	628	1.9%
Allocated Charges	19,850	21,345	21,891	22,393	22,843	23,307	23,689	24,133	24,528	24,965	25,414	2.5%
Total Non Sal/Ben Before Transfers	54,404	59,247	60,621	62,059	63,395	64,723	65,968	67,790	68,984	70,624	72,357	2.9%
Operating Transfers-Out	5,725	4,869	4,899	4,955	5,039	5,033	5,092	5,156	5,182	5,212	5,271	-0.8%
Transfer to Infrastructure - Base/Cubb	16,823	18,987	21,161	21,545	21,937	22,339	22,752	23,175	23,609	24,055	24,512	3.8%
Transfer to Infrastructure - TOT	8,350	8,406	8,625	8,853	9,105	9,360	9,641	9,941	10,244	10,548	10,843	2.6%
Total Use of Funds	$210,706	$229,916	$238,472	$244,508	$250,606	$255,948	$260,771	$266,655	$269,292	$274,424	$279,867	2.9%

Salary and Benefits

The table above (also available in Attachment A) depicts the estimated General Fund salaries and benefits costs for the next decade. Over the forecast period, the salaries and benefits costs gradually increase in comparison to the total expenditure budget. In FY 2020, salaries and benefits costs represent approximately 60 percent of the General Fund budget expenditures and remain near that level of General Fund budget expenditures through FY 2029.

Salary

Consistent with the City's salary budget methodology for recent budgets, positions are budgeted at the actual rate of pay of employees including benefits as of Fall 2018. Then, by position, salary costs are updated in accordance with applicable Memorandum of Agreements (MOA) between the City and its labor groups and the Management and Professional Personnel and Council Appointees Compensation Plan(s). The safety (Police and Fire) bargaining units recently concluded bargaining with MOAs that continue through Fiscal Year 2022 as approved by the City Council. The main bargaining unit for miscellaneous employees in the General Fund, Service Employees International Union (SEIU), is currently in negotiations with the City. The SEIU MOA expires December 31, 2018.

The Forecast assumes step increases for employees in applicable positions, including SEIU, IAFF, and PAPOA and merit increases for Management and Professional employees. General wage adjustments of 2% are included in each year of the Forecast for all employees in years when there is not a MOA in effect. This is consistent with prior Council direction to use the 2 percent increase as a forecasting model, not as a commitment to future negotiations. If agreements are negotiated with salary increases greater than presumed in the forecast, then expenses will increase accordingly.

Benefits
<u>Pension:</u> The Forecast includes pension rates from CalPERS as of the June 30, 2017 valuation for the City's Miscellaneous and Safety plans for the first six years of the Forecast and modeled by the City for the final years of the Forecast. This methodology is necessary as CalPERS only provides projected pension rates for the next six years. CalPERS has implemented some changes with significant impacts to the City's pension liability lowering the discount rate from 7.5 percent to 7.0 percent over three years. For Fiscal Year 2020, the second year of this three-year phase in, CalPERS used a 7.25 percent discount rate.

CalPERS determines the City's total contributions for a given Fiscal Year as the sum of two factors: Normal Cost (NC) and Unfunded Accrued Liability (UAL). The Normal Cost (NC) is a variable cost that increases or decreases directly with the salary levels of the City and is sometimes referred to as a 'pay-go' cost. It represents the necessary funding for the City to pay for employees presuming that CalPERS makes its stated investment returns. However, in a year that CalPERS does not make its stated investment return, a loss in assets is realized. The accumulation of these losses represents the City's Unfunded Accrued Liability (UAL), which is calculated by CalPERS and is sometimes referred to as the 'catch-up' cost. The UAL is calculated over an amortized period with defined annual payments, similar to a mortgage. CalPERS then blends these payments into a percentage of payroll for reference.

For the miscellaneous plan, the projected pension contribution rate will increase from the current 32.6 percent in FY 2019 to 35.6 percent in FY 2020. This includes the continued phase-in of the lower discount rate for the unfunded accrued liability (UAL), which will be completed in FY 2021. The rate continues to increase to a peak of 43.1 percent of payroll in FY 2026 as a result of actuarial impacts before tapering down to 37.0 percent in FY 2029. This projection is consistent with prior actuarial assessments done by Bartel Associates which anticipated a slight decline in pension costs associated with various amortization factors including the pay-down of previously sustained losses.

The Safety plan follows a similar trend line, with the increases plateauing in the out years of the Forecast. In the first year, the safety plan is projected to grow to 59.4 percent of payroll from the current 55.6 percent of payroll and increase to 73.7 percent in FY 2025 before tapering down beginning in FY 2026. As with the miscellaneous plan, this initial growth is primarily driven by the phase-in of the 7.0 percent discount rate instead of the previous 7.5 percent discount rate. This growth stabilizes in the out years of the Forecast and returns to a lower level of 66.0 percent by FY 2029.

The table below shows CalPERS' projected FY 2019 – FY 2029 blended retirement rates. It should be noted that the numbers in FY 2026 are not provided by CalPERS (they only provide a forecast through FY 2025) but have been calculated by the City using a methodology consistent with CalPERS actuarial analysis. These rates are before the employee pick-ups of the employer share are factored in; that pick-up materializes as savings in the City's pension costs. The forecast does presume that employees in the miscellaneous plan will pick up 1% of the employer pension cost for miscellaneous plan members, and that safety plan members will pick up percentages consistent with their MOAs, ranging from the current 3% to 4% depending on the year and the unit.

TABLE 7: CalPERS' Projected FY 2019-2029 Blended Retirement Rates

(percentage of payroll)

	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029
Miscellaneous	32.6	35.6	38.2	40.0	41.4	41.9	42.5	43.1	38.5	37.9	37.0
Safety	55.6	59.4	64.1	68.0	71.1	72.7	73.7	70.0	68.9	67.5	66.0

On October 29, 2018 the City Council approved a significant change in assumptions for the development of financial planning, beginning with this base case for the Long-Range Financial Forecast. The City Council directed that staff include the NC for pension benefits in the budget assuming an equivalent of 6.2 percent discount rate and transfer additional funding beyond CalPERS actuarial determined contribution levels to the 115 Trust Fund. A preliminary calculation was done to capture the marginal increases associated with recognizing a 6.2 percent discount rate for the City's Normal Cost payments. The implication of this marginal increase is approximately $3.9 million in additional pension expenses in this Long-Range Financial Forecast beginning in FY 2020 compared to previous assumptions. These additional funds would be contributed directly to the City's IRS Section 115 irrevocable Pension Trust Fund and would augment the current principal deposits of $7.6 million. The City's Unfunded Accrued Liability (UAL), calculated by CalPERS, remains at the CalPERS discount rate assumption phasing down to 7.0 percent in FY 2021.

The marginal costs of the lower discount rates do taper as the forecast continues through to the end of the ten-year term. It is anticipated the City will spend a total of $32.3 million on pension costs in FY 2020, increasing to a peak of $35.6 million in FY 2026 before the downward trend starts at the end of the forecast. These expenses represent approximately 14% of the General Fund's total expenses. Alternative Forecast #1, contemplates how the Long Range Financial Forecast would change if the marginal costs associated with the lower discount rate were excluded from the forecast.

Retiree Medical: Retiree Medical is based on the most recent actuarial study prepared by Bartel Associates, which is completed every two years. The last actuarial study was done in FY 2018 and presented to the City Council as part of the Fiscal Year 2019 Adopted Budget. The table below details the cost to the General Fund for every year based on that actuarial study, excluding the implied subsidy. Consistent with City Council direction, as recommended by staff, the City continues to budget for the full payment of the Actuarial Determined Contribution (ADC) for retiree healthcare. Since CalPERS blends active employees with pre-Medicare retirees and charges the same medical premium, even though younger employees on average consume less healthcare and thereby subsidize older employees and retirees, there is an implied subsidy that effectively lowers the funding necessary to meet the ADC.

TABLE 8: FY 2020 – FY 2029 Retiree Medical General Fund Contributions

	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029
General Fund	$9.1M	$9.3M	$9.6M	$9.9M	$10.2M	$10.5M	$10.8M	$11.1M	$11.5M	$11.8M

The City's CERBT Trust, which contains prefunding for the City's Other Post Employment Benefit (OPEB) liabilities, maintains a very health fund balance. The CERBT Trust currently has over $100 million in assets. As the City continues through the next few years, there will be important impacts to examine associated with Retiree Medical as there may be opportunities over the course of this forecast to subsidize the City's ADC payments with withdrawals from the OPEB CERBT Trust. That savings could possibly be used for other competing priorities, such as prepaying an additional portion of the City's pension UAL.

Healthcare: Consistent with the most recent labor agreements between the City and its bargaining units in the General Fund, the City's contribution amounts towards medical costs for employees are based on a flat rate contribution from the City, with the employee contributing towards the remaining medical plan premium. Like salaries, healthcare costs are updated in accordance with applicable Memorandum of Agreements (MOA) between the City and its labor groups and the Management and Professional Personnel and Council Appointees Compensation Plan(s). This Forecast assumes an inflation factor of four percent on healthcare costs to the City in each year of the Forecast for all employees in years when there is not a MOA in effect. This forecast does presume lower growth than the four percent that has been modeled in the past for dental and vision costs. These costs underwent adjustments during CY 2018, including a downward adjustment for dental, and as a result of that increases of only two percent are modeled through this forecast.

Contract Services

This FY 2020 forecast assumes $21.6 million in contract services, a 1.9 percent decrease from the FY 2019 Adopted Budget of $22.0 million. This decrease is driven primarily by $780,000 in grant expenses that were recognized on a one-time basis as part of the FY 2019 Adopted Operating Budget. This budget category includes important contract increases for contractual obligations already approved by the City Council, including significant contracts such as tree maintenance, landscape maintenance, operations at the newly renovated Golf Course, and janitorial services. Throughout the Forecast, a 2.0 percent annual escalator was modeled to capture anticipated growth in this expense category beginning in FY 2020.

Supplies and Materials

The FY 2019 Adopted Budget for the General Fund included $3.5 million for Supplies and Materials, which is anticipated to grow modestly to $3.6 million in FY 2020. An escalator of 2.0 percent was applied to this expense category to capture anticipated growth over the course of the forecast.

General Expense
This category includes costs for travel and meetings, telephone and non-city utilities, contingency accounts, bank card service charges, and subsidies and grants provided through the Human Services Resource Allocation Program (HSRAP). The FY 2019 Adopted Budget of $6.2 million is somewhat understated because it includes the $4.0 million in General Fund expense reductions as directed by the City Council during the adoption of the FY 2019 Budget. The conversation between staff and the Finance Committee regarding that $4.0 million and where the lower expenses will be realized is ongoing. The FY 2020 forecast for this category does not continue that reduction, which is why this category increases to $10.5 million. Over the course of the forecast, increases of 2.0 percent were modeled. These figures do not include General Expenses for the Cubberley Lease, which is explained in further detail below.

General Expense - Cubberley Lease: In FY 2015, the City and Palo Alto Unified School District (PAUSD) agreed to an extension of the Cubberley Lease by five years starting January 1, 2015 and expiring December 31, 2019. As part of the lease agreement, the City Council approved creation of a fund for Cubberley infrastructure improvements. Based on the new lease, $1.9 million is transferred to the Cubberley Property Infrastructure Fund annually. Therefore, the $1.9 million is classified as an Operating Transfer Out which is discussed in further detail below. With the Cubberley infrastructure funds set aside, the FY 2019 Budget includes $6.3 million for Cubberley Lease payments. In accordance with the lease agreement, the Forecast assumes a 3.0 percent annual CPI increase for the lease payments to the PAUSD for the Cubberley facility. For planning purposes in this Forecast, it is assumed that the current agreement will continue during the entire Forecast period.

Rents and Leases
The Rents and Leases expense category for FY 2020 is estimated to increase by 3.6 percent from $1.7 million in FY 2019 to $1.8 million in FY 2020. This increase includes the lease for some of the Development Services Department staff at 526 Bryant Street. The growth throughout the forecast is projected at 3.0 percent due to the continued pressure on this expense category. It is important to note that if the City must continue renting space for operations of departments like Development Services and if the current rent environment persists, that this expense category could increase even more.

Facilities and Equipment
The Facilities and Equipment expense category is expected to experience a slight increase of 2.0 percent from $522,000 to $533,000, from FY 2019 to FY 2020. This budget category includes subscription payments for equipment like public safety radios as well as other non-capital equipment. Growth of approximately 2.0 percent is modeled through the forecast to capture anticipated increases.

Allocated Charges

Allocated Charges represent expense allocations by the City's Enterprise and Internal Service Funds for services and products they provide to General Fund departments. The FY 2019 Adopted Budget for the General Fund included $19.8 million for these expenses, including utilities usage, general liability insurance, technology costs, vehicle equipment maintenance and replacement costs and other charges. The allocated charges for general liability expenses and workers' compensation were subsidized on a one-time basis in FY 2019, which is not continued in the forecast in FY 2020. The FY 2020 allocated charges in the Forecast update the revenues and expenses for these various allocations based on the information available at the time of the Forecast development. FY 2020 is anticipated to experience an increase of 7.5 percent to a total of $21.3 million. This increase is driven primarily by the restoration of the full allocation of costs associated with the general liability expenses and workers' compensation funds.

Operating Transfers Out

Operating Transfers Out include transfers from the General Fund to the Debt Service Fund, the Technology Fund, and other funds. The transfer level for the FY 2019 Adopted Budget was $5.7 million; this included a one-time transfer of $1.2 million from the City's General Fund to its irrevocable Section 115 Trust Fund through the General Benefits Fund to prefund pension obligations. As a result of removing that transfer, the Operating Transfers Out are anticipated to be $4.9 million in FY 2020. (The costs associated with the lower discount rate and correspondingly higher Normal Cost, as directed by the City Council, are included in the Salary and Benefits category beginning in FY 2020.)

The main reason for the year-over-year increase in this category, even after adjusting for the one-time transfer to the benefits fund, is that the City shifted how it is paying for its debt service. Although no expenses are anticipated in the Debt Service category in the General Fund in FY 2020 budget, transfers to the debt service fund are included for the debt issued associated with the golf course. These payments continue throughout the term of the forecast.

Transfer to Infrastructure

In FY 2019, the adopted General Fund transfer to the Capital Improvement Fund is $25.2 million, which includes the base transfer of $16.8 million and $8.4 million from additional TOT proceeds generated through a two percentage point TOT increase as well as through the addition of new hotels. Incremental TOT increases from the rate increase and new hotels are dedicated to the Capital Improvement Fund to support the Infrastructure Plan, consistent with City Council direction. This transfer is anticipated to increase to $17.1 million for the base transfer in FY 2020 and an additional $8.4 million for the dedicated TOT funds per Council priorities. This budget category also includes the separate $1.9 million transfer to the Cubberley Property Infrastructure Fund, described earlier in this document. This transfer remains consistent throughout this Forecast despite the sunset date of the current lease terms for Cubberley to capture the anticipated costs.

The transfers to the Capital Improvement Fund are anticipated to remain generally consistent with the FY 2019 Adopted Budget for the next few years, with slight increases annually over the forecast period. Both the TOT and base transfers to the Capital Improvement Fund are anticipated to increase each year of the forecast period. The TOT transfer captures the growth anticipated from the construction of new hotels. Both the TOT transfer and the base transfer increase over the term of the forecast to capture anticipated CPI increases as well.

Budget Stabilization Reserve

The City's Budget Stabilization Reserve (BSR) serves as the primary General Fund reserve. By policy, the BSR is maintained in the range of 15 to 20 percent of General Fund operating expenditures, with a target of 18.5 percent. Any reduction to the reserve below 15 percent requires City Council approval. At the discretion of the City Manager, any BSR balance above 18.5 percent may be transferred to the Infrastructure Reserve (IR), which was established to provide funding for maintenance and rehabilitation of the City's capital assets. The BSR is used to fund unanticipated one-time costs as opposed to ongoing or recurring operating expenditures. The City's intent is to fund ongoing programs and services with ongoing dollars. This forecast assumes that the BSR meets or exceeds the City Council approved minimum of 15 percent of anticipated expenses in any given year.

The City has held a long-standing practice of maintaining a BSR balance of no less than 15 percent of General Fund operating expenses. At the close of Fiscal Year 2018, the BSR is anticipated to remain above the 18.5 percent target at $51.4 million. It should be noted that this includes the $4.0 million referral from City Council related to prefunding pension obligations. It is anticipated that other qualifications for the balance of the BSR will be further clarified through the Comprehensive Annual Financial Report and the Year-End process for FY 2018. Establishing sound fiscal reserve policies have been a strong factor in the City being rated AAA by rating agencies.

Assumptions NOT Included in Forecast

It should be noted that this Forecast does not include several potential impacts to the FY 2020 projected budget and the out years of the Forecast. Below is a list of a few items not included. This is not intended to be a comprehensive list or in any priority order.

Labor negotiations: Although the City has recently concluded negotiations with four safety units, these contracts only extend through the first few years of the forecast. These safety units are the Palo Alto Peace Officers Association (PAPOA), the International Association of Fire Fighters (IAFF), Fire Chiefs Association (FCA), and Police Management Association (PAPMA). Each of those contracts expire June 30, 2021. Additionally, the Service Employees International Union (SEIU) MOA expires at the conclusion of the 2018 calendar year. After an agreement is reached with SEIU, it will need to be incorporated into future budgets and forecasts, as applicable. Additionally, as discussed above, this Forecast models only modest increases to salaries in years where there is not a contract. This region's competition for a qualified workforce remains a significant pressure on the City's anticipated salary costs.

Capital Infrastructure Plan: As referenced earlier, the June 2014 Council approved Infrastructure Plan of $125.8 million in projects was based on construction and design costs with data from 2012. As construction costs have increased and the City is required to pay prevailing wages, the Plan's funding status has shifted. The FY 2019 Adopted Capital Budget anticipated that this Plan would cost $249.9 million. In addition, this Forecast does not assume ongoing operating and maintenance impacts as a result of the Infrastructure Plan, such as the operating costs associated with the new Public Safety building, but future forecasts will incorporate operating cost impacts as the specific projects are designed and implemented.

Grade Separation: The city is currently in the process of exploring four locations for grade separations. As the City continues the process of deciding not only how many locations will have grade separation but also what kind of grade separation will be pursued the financial impacts are difficult to define. Additionally, it may make sense to undertake a coordinated area plan for transit in the downtown area to synchronize with the grade separation process. Costs for these items are not included in this forecast.

Parks Master Plan: The Parks Master Plan was finalized in 2017, however, when approved it identified a need to develop a funding strategy. As such, this Forecast does not yet contemplate the necessary investments to execute this plan.

Junior Museum and Zoo: In November 2014, the City Council directed staff to negotiate a capital lease with the Friends of the Junior Museum and Zoo for the reconstruction of the Junior Museum and Zoo. This Forecast does not assume any additional capital or ongoing operating costs related to the renovated building and changes in programming as a result of the new building. This is an especially important variable to consider as future budgets are developed since the impacts will materialize at the beginning of the forecast and continue.

Other Capital Improvement Projects: A number of both assets and planned projects remain on the horizon, however, none have resulted in formalized capital improvement projects. Major improvements such as an update to the animal care shelter, rail grade separation, the former ITT site, and the acquisition of land or assets are not factored into the Forecast.

City owned assets operated by non-profit organizations: This Forecast does not include any additional capital investments for the Avenidas Senior Center (beyond the current $5 million pledge), the Palo Alto History Museum, the Ventura Child Care Center, the Junior Museum and Zoo, nor the Sea Scout Building.

Cubberley Community Center Master Plan: The City has started the process of designing a Cubberley Community Center Master Plan, however, costs to implement that master plan in excess of the dedicated Cubberley infrastructure funding as agreed to between the PAUSD and the City are not assumed in this Forecast. In addition, the lease agreement with the PAUSD is set to expire in December 2019.

Loans for special projects: From time to time the City's General Fund will assist other City operations with modest cash flow loans to bridge fiscal years. For example, the City has provided over $3 million in loans to the Airport Fund as it works to secure significant grant funding from the Federal Aviation Administration (FAA) for capital improvement costs. Other initiatives may need a similar type of short-term loan in order to fund the capital costs necessary to implement though none have been assumed in this forecast.

Cadillac Healthcare Federal Excise Tax: A 40 percent excise tax will be imposed on the value of health insurance benefits that exceed a certain threshold. CalPERS may be able to design healthcare premiums to stay below the threshold and discussions are in the preliminary stage. Congress did delay the implementation of this tax from calendar year 2020 to calendar year 2022. However, if the tax is implemented and applicable, the City may have to pay the tax.

Greater CalPERS City contribution increases: Currently, CalPERS assumes an annual investment return of 7.0 percent. Further, the CalPERS Board approved a gradual de-risking strategy, which is intended to reduce the assumed investment return to 6.5% over the next 20 years. This Forecast assumes that CalPERS will meet the annual investment return. However, staff and the Finance Committee continue to discuss the City's best options for addressing the unfunded pension liability. At the City Council's direction, this forecast does include the marginal costs associated with a lower discount rate on the normal cost. However, if CalPERS experiences investment returns lower than it has presumed in its actuarial model, it is anticipated that there may be even greater impacts on the City's finances.

Tax revenue alignment with updated Comprehensive Plan: The City Council recently completed updating its Comprehensive Plan, including the potential fiscal impact of various land use scenarios. The fiscal impact of this plan and various land use scenarios are not factored into this Forecast.

Changes in the local, regional, and national economy: This Forecast assumes a moderately growing local economy. Any changes may have positive or negative impacts on economically sensitive revenues such as Sales Tax and the Transient Occupancy Tax.

Alternative Forecast #1: Normal Cost calculated at CalPERS Discount Rate (phase-in to 7.0 percent by FY 2021)

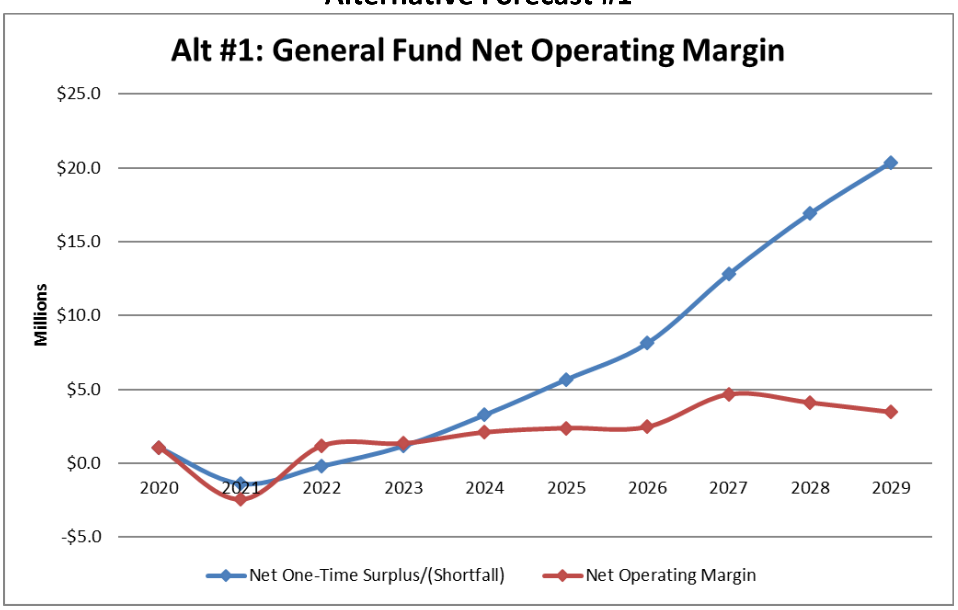
As discussed in the Salary and Benefits section above, the base forecast includes approximately $3.9 million in additional pension expenses in this Long-Range Financial Forecast. These costs capture the direction from City Council to budget the Normal Cost using a 6.2 percent discount rate to proactively prefund the City's pension liability. This assumption deviates from the current CalPERS actuarial assumptions for investment earnings; CalPERS currently assumes a phase-in to 7.0 percent discount rate by FY 2021. This alternative scenario models the impact of assuming CalPERS rates for both the NC and UAL portions of the City's annual pension contributions. The summary table for this alternative forecast and the Net Operating Margin graph for this alternative forecast are below. Additional discussion for this alternative follows these figures.

TABLE 9: FY 2020 – FY 2029 Long Range Financial Forecast
Alternative Forecast #1

	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Total Revenue	$207,042	$227,108	$233,938	$241,315	$248,921	$256,571	$264,392	$273,133	$281,311	$290,856	$299,948
		9.7%	*3.0%*	*3.2%*	*3.2%*	*3.1%*	*3.0%*	*3.3%*	*3.0%*	*3.4%*	*3.1%*
Total Expenditures	$210,426	$226,033	$235,292	$241,479	$247,736	$253,283	$258,718	$264,994	$268,506	$273,945	$279,573
		7.4%	*4.1%*	*2.6%*	*2.6%*	*2.2%*	*2.1%*	*2.4%*	*1.3%*	*2.0%*	*2.1%*
Net One-Time Surplus/(Shortfall)	($3,384)	$1,075	($1,354)	($164)	$1,185	$3,288	$5,675	$8,139	$12,805	$16,911	$20,376
Cumulative Net Operating Margin (One-Time)											$67,936
Net Operating Margin		$1,075	($2,430)	$1,190	$1,349	$2,103	$2,386	$2,465	$4,666	$4,106	$3,465
Cumulative Net Operating Margin											$20,376

Assumes that the annual shortfalls are solved with ongoing solutions and annual surpluses are spent for ongoing expenditures.

TABLE 10: FY 2020-2029 Long Range Financial Forecast Net Operating Margin
Alternative Forecast #1



The General Fund would run a slight surplus in the first year and then alternate between slight deficits and surpluses before trending to surpluses in FY 2024 in this scenario. However, no annual contribution to the City's Section 115 Pension Trust Fund is presumed in this model. This scenario represents the significant efforts the City has taken over the past few years to structurally balance the budget through reprioritization of work and reductions to the City's full-time staffing in order to help contain rising pension costs.

Alternative Forecast #2: Major Tax Revenue Sensitivity Analysis

This alternative scenario models the potential impact that might be seen if the economy contracted, for modeling purposes this is assumed to occur in FY 2022, and the growth that would be anticipated for the remainder of the forecast. The lower revenue estimates would continue through the forecast but would recover somewhat toward the final years of the forecast. These lower revenue estimates through first nine years of the forecast would significantly constrain the City's resources.

As discussed in the base case, FY 2020 total tax receipts account for nearly 60 percent of the General Fund's total revenues. The base case assumes that average tax receipts grow $9.1 million, or 7.2%, above the Fiscal Year 2019 Adopted Budget of $127.2 million to reach a total of $136.3 million in FY 2020. The growth tapers somewhat after that but remains between 4.3 percent and 3.5 percent over the ten years of the forecast. If tax revenue slowed, like patterns experienced by the City of Palo Alto during prior recessions, but all other assumptions remained constant, the loss in revenue would be approximately $15.3 million in FY 2022.

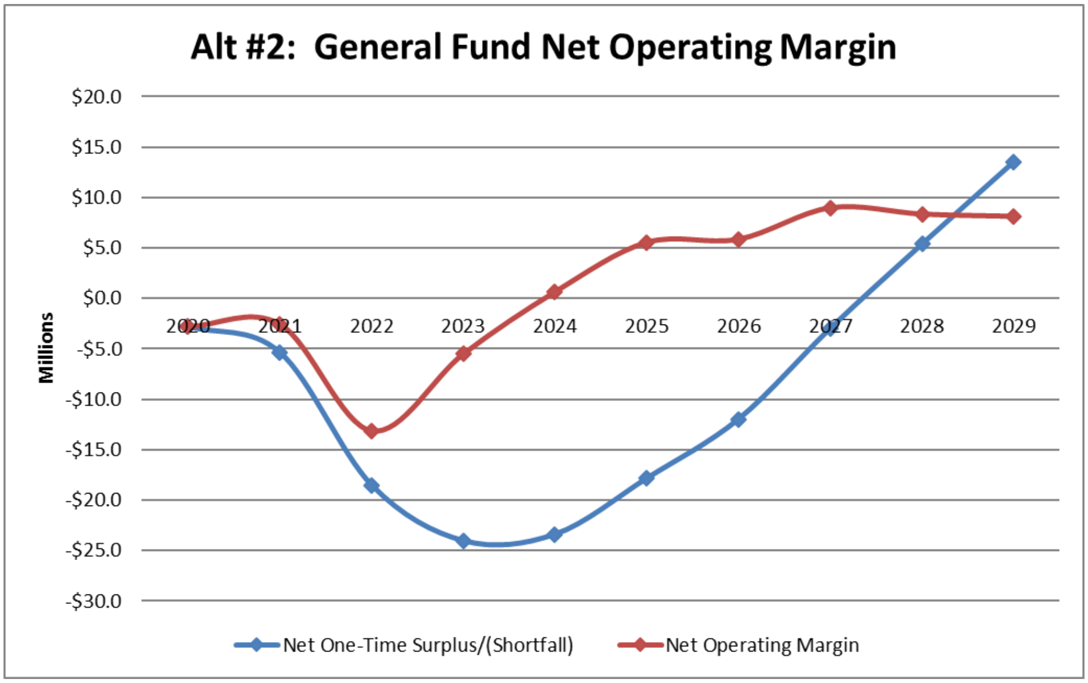
Under this alternative, the City's expenses would be projected to exceed revenues in all but the final two years of the forecast. The greatest one-time gap would be in Fiscal Year 2023, with $24.0 million more in expenses than revenues, before narrowing to $3.0 million more in expenses than revenues in FY 2027 and then closing in FY 2028. The summary table for this Alternative and the corresponding graph showing the Net Operating Margin are included below.

TABLE 11: FY 2020 – FY 2029 Long Range Financial Forecast
Alternative Forecast #2

	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Total Revenue	$207,042	$227,108	$233,100	$225,984	$226,565	$232,555	$242,938	$254,692	$266,323	$279,817	$293,398
		9.7%	*2.6%*	*-3.1%*	*0.3%*	*2.6%*	*4.5%*	*4.8%*	*4.6%*	*5.1%*	*4.9%*
Total Expenditures	$210,426	$229,916	$238,472	$244,508	$250,606	$255,948	$260,771	$266,655	$269,292	$274,424	$279,867
		9.3%	*3.7%*	*2.5%*	*2.5%*	*2.1%*	*1.9%*	*2.3%*	*1.0%*	*1.9%*	*2.0%*
Net One-Time Surplus/(Shortfall)	($3,384)	($2,807)	($5,372)	($18,524)	($24,041)	($23,393)	($17,832)	($11,964)	($2,970)	$5,393	$13,531
Cumulative Net Operating Margin (One-Time)											-$87,979
Net Operating Margin		($2,807)	($2,565)	($13,151)	($5,517)	$648	$5,560	$5,869	$8,994	$8,363	$8,138
Cumulative Net Operating Margin											$13,531

Assumes that the annual shortfalls are solved with ongoing solutions and annual surpluses are spent for ongoing expenditures.

TABLE 12: FY 2020-2029 Long Range Financial Forecast Net Operating Margin Alternative Forecast #2



Conclusion

The FY 2020 Long Range Financial Forecast puts in perspective the growing desires and the limited resources available to complete them all in a timely manner. The City structurally balanced with the adoption of the budget in FY 2019 and now needs to continue to exercise financial prudence in order to not only meet its obligations and demands on service delivery but also proactively prefund its pension liability. This balance will require extensive conversations with the community regarding what the City's priorities are and how that balance can best be achieved. Through these conversations, a continued scrutiny of the expansion and enhancement of existing services, the addition of new services, and the priorities of the community will be necessary. As the Committee and Council continue to discuss major projects such as pension, infrastructure, and grade separation the ability to manage expectations and implement innovative solutions will be critical. A prioritization of needs and ensuring that we operate within resources that are available are essential to preserving the City's sound financial future.

RESOURCE IMPACT

Financial implications from this report and input from the Finance Committee will be considered in the City Manager's development of the Proposed Fiscal Year 2020 budget.

ENVIRONMENTAL IMPACT

This report is not a project for the purposes of the California Environmental Quality Act. Environmental review is not required.

Attachments:

- Attachment A: Long Range Financial Report Base Case Revenue Tables
- Attachment B: Long Range Financial Report Base Case Expense Tables

FY 2020-2029 Long Range Financial Forecast Base Case Revenue Table

Revenue & Other Sources	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	CAGR 10 Years
Sales Taxes	$31,246	$34,286	$35,754	$37,000	$38,154	$39,302	$40,426	$41,546	$42,759	$44,063	$45,498	3.8%
Property Taxes	45,332	48,193	51,181	54,231	57,235	60,285	63,426	67,289	71,508	76,078	80,970	6.0%
Transient Occupancy Tax- General Purpose	16,699	17,977	18,444	18,933	19,473	20,018	20,618	21,260	21,908	22,556	23,188	3.3%
Transient Occupancy Tax- Infrastructure	8,350	8,406	8,625	8,853	9,106	9,361	9,641	9,941	10,244	10,547	10,843	2.6%
Documentary Transfer Tax	7,434	8,359	8,631	8,905	9,174	9,484	9,851	10,188	10,547	10,928	11,325	4.3%
Utility Users Tax	16,092	17,026	17,519	18,024	18,407	18,768	19,109	19,497	19,811	20,168	20,526	2.5%
Other Taxes and Fines	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	2,032	0.0%
Subtotal: Taxes	127,185	136,279	142,186	147,978	153,581	159,250	165,103	171,753	178,809	186,372	194,382	4.3%
Charges for Services	20,630	22,057	22,870	23,551	24,230	24,788	25,323	25,955	26,010	26,464	26,534	2.5%
Stanford Fire & Dispatch Services	7,384	7,829	7,992	8,128	8,273	8,395	8,486	8,580	8,651	8,763	8,810	1.8%
Permits and Licenses	8,949	9,065	9,169	9,252	9,337	9,406	9,474	9,555	9,563	9,620	9,669	0.8%
Return on Investments	1,166	1,197	1,230	1,266	1,304	1,346	1,390	1,432	1,475	1,519	1,563	3.0%
Rental Income	15,807	16,120	15,272	14,766	15,153	15,551	15,961	16,384	16,819	17,267	17,729	1.2%
From Other Agencies	1,150	370	370	370	370	370	370	370	370	370	370	-10.7%
Charges to Other Funds	10,093	11,103	11,471	11,770	12,092	12,357	12,595	12,894	12,837	13,100	13,300	2.8%
Other Revenue	2,361	2,361	2,313	2,314	2,315	2,316	2,316	2,317	2,318	2,319	2,321	-0.2%
Total Non-Tax Revenue	67,540	70,102	70,688	71,418	73,073	74,528	75,915	77,487	78,043	79,422	80,296	1.7%
Operating Transfers-In	19,772	20,727	21,063	21,918	22,267	22,793	23,374	23,893	24,459	25,062	25,271	2.5%
BSR Contribution (One-Time)												
Golf Operating Loss Reserve Liquidation												
Total Source of Funds	$214,497	$227,108	$233,938	$241,315	$248,921	$256,571	$264,392	$273,133	$281,311	$290,856	$299,948	3.4%

Revenue & Other Sources	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Sales Taxes	9.7%	4.3%	3.5%	3.1%	3.0%	2.9%	2.8%	2.9%	3.0%	3.3%
Property Taxes	6.3%	6.2%	6.0%	5.5%	5.3%	5.2%	6.1%	6.3%	6.4%	6.4%
Transient Occupancy Tax - General Purpose	7.7%	2.6%	2.7%	2.9%	2.8%	3.0%	3.1%	3.0%	3.0%	2.8%
Transient Occupancy Tax - Infrastructure	0.7%	2.6%	2.6%	2.9%	2.8%	3.0%	3.1%	3.0%	3.0%	2.8%
Documentary Transfer Tax	12.4%	3.3%	3.2%	3.0%	3.4%	3.9%	3.4%	3.5%	3.6%	3.6%
Utility Users Tax	5.8%	2.9%	2.9%	2.1%	2.0%	1.8%	2.0%	1.6%	1.8%	1.8%
Other Taxes and Fines	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Subtotal: Taxes	7.2%	4.3%	4.1%	3.8%	3.7%	3.7%	4.0%	4.1%	4.2%	4.3%
Charges for Services	6.9%	3.7%	3.0%	2.9%	2.3%	2.2%	2.5%	0.2%	1.7%	0.3%
Stanford Fire & Dispatch Services	6.9%	2.1%	1.7%	1.8%	1.5%	1.1%	1.1%	0.8%	1.3%	0.5%
Permits and Licenses	1.3%	1.1%	0.9%	0.9%	0.7%	0.7%	0.9%	0.1%	0.6%	0.5%
Return on Investments	2.7%	2.8%	2.9%	3.0%	3.2%	3.3%	3.0%	3.0%	3.0%	2.9%
Rental Income	2.0%	-5.3%	-3.3%	2.6%	2.6%	2.6%	2.6%	2.7%	2.7%	2.7%
From Other Agencies	-67.8%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Charges to Other Funds	10.0%	3.3%	2.6%	2.7%	2.2%	1.9%	2.4%	-0.4%	2.1%	1.5%
Other Revenue	0.0%	-2.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%
Total Non-Tax Revenue	3.8%	0.8%	1.0%	2.3%	2.0%	1.9%	2.1%	0.7%	1.8%	1.1%
Operating Transfers-In	4.8%	1.6%	4.1%	1.6%	2.4%	2.5%	2.2%	2.4%	2.5%	0.8%
BSR Contribution (One-Time)										
Golf Operating Loss Reserve Liquidation										
Total Source of Funds	5.9%	3.0%	3.2%	3.2%	3.1%	3.0%	3.3%	3.0%	3.4%	3.1%

ATTACHMENT B

FY 2019-2028 General Fund Long Range Financial Forecast Base Case
Expense Table

Expenditures & Other Uses	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	CAGR 10 Years
Salary	$ 70,469	$ 78,029	$ 80,751	$ 82,730	$ 84,835	$ 86,761	$ 88,548	$ 90,317	$ 92,083	$ 93,845	$ 95,607	3.1%
Benefits	54,935	60,378	62,416	64,366	66,295	67,733	68,771	70,277	69,192	70,141	71,278	2.6%
Subtotal: Salary & Benefits	125,404	138,408	143,167	147,097	151,130	154,494	157,318	160,594	161,275	163,986	166,884	2.9%
Contract Services	22,025	21,607	22,030	22,552	23,018	23,454	23,881	24,313	24,750	25,178	25,478	1.5%
Supplies & Material	3,521	3,558	3,628	3,697	3,767	3,837	3,907	3,977	4,046	4,116	4,189	1.8%
General Expense	6,183	10,454	10,726	11,005	11,289	11,580	11,877	12,682	12,901	13,531	14,364	8.8%
Debt Service	613	0	0	0	0	0	0	0	0	0	0	N/A
Rents & Leases	1,690	1,751	1,804	1,858	1,914	1,971	2,030	2,091	2,154	2,218	2,285	3.1%
Facilities & Equipment	522	532	543	553	564	574	584	595	605	616	628	1.9%
Allocated Charges	19,850	21,345	21,891	22,393	22,843	23,307	23,689	24,133	24,528	24,965	25,414	2.5%
Total Non Sal/Ben Before Transfers	54,404	59,247	60,621	62,059	63,395	64,723	65,968	67,790	68,984	70,624	72,357	2.9%
Operating Transfers-Out	5,725	4,869	4,899	4,955	5,039	5,033	5,092	5,156	5,182	5,212	5,271	-0.8%
Transfer to Infrastructure - Base/Cubb	16,823	18,987	21,161	21,545	21,937	22,339	22,752	23,175	23,609	24,055	24,512	3.8%
Transfer to Infrastructure - TOT	8,350	8,406	8,625	8,853	9,105	9,360	9,641	9,941	10,244	10,548	10,843	2.6%
Total Use of Funds	$210,706	$229,916	$238,472	$244,508	$250,606	$255,948	$260,771	$266,655	$269,292	$274,424	$279,867	2.9%

Expenditures & Other Uses	Adopted 2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Salary	N/A	10.7%	3.5%	2.5%	2.5%	2.3%	2.1%	2.0%	2.0%	1.9%	1.9%
Benefits	N/A	9.9%	3.4%	3.1%	3.0%	2.2%	1.5%	2.2%	-1.5%	1.4%	1.6%
Subtotal: Salary & Benefits	N/A	10.4%	3.4%	2.7%	2.7%	2.2%	1.8%	2.1%	0.4%	1.7%	1.8%
Contract Services	N/A	-1.9%	2.0%	2.4%	2.1%	1.9%	1.8%	1.8%	1.8%	1.7%	1.2%
Supplies & Material	N/A	1.0%	2.0%	1.9%	1.9%	1.9%	1.8%	1.8%	1.8%	1.7%	1.8%
General Expense	N/A	69.1%	2.6%	2.6%	2.6%	2.6%	2.6%	6.8%	1.7%	4.9%	6.2%
Debt Service	N/A	-100.0%	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Rents & Leases	N/A	3.6%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Facilities & Equipment	N/A	2.0%	2.0%	1.9%	1.9%	1.9%	1.8%	1.8%	1.8%	1.7%	2.0%
Allocated Charges	N/A	7.5%	2.6%	2.3%	2.0%	2.0%	1.6%	1.9%	1.6%	1.8%	1.8%
Total Non Sal/Ben Before Transfers	N/A	8.9%	2.3%	2.4%	2.2%	2.1%	1.9%	2.8%	1.8%	2.4%	2.5%
Operating Transfers-Out	N/A	-14.9%	0.6%	1.2%	1.7%	-0.1%	1.2%	1.3%	0.5%	0.6%	1.1%
Transfer to Infrastructure - Base/Cubb	N/A	12.9%	11.4%	1.8%	1.8%	1.8%	1.8%	1.9%	1.9%	1.9%	1.9%
Transfer to Infrastructure - TOT	N/A	0.7%	2.6%	2.6%	2.8%	2.8%	3.0%	3.1%	3.0%	3.0%	2.8%
Total Use of Funds	N/A	9.1%	3.7%	2.5%	2.5%	2.1%	1.9%	2.3%	1.0%	1.9%	2.0%

FINANCE COMMITTEE ACTION MINUTES

Special Meeting
November 28, 2018

Chairperson Scharff called the meeting to order at 6:36 P.M. in the Community Meeting Room, 250 Hamilton Avenue, Palo Alto, California.

Present: Filseth, Kou, Scharff, Tanaka

Agenda Items

1. Review Recommended $4 Million in General Fund Savings and Approve Corresponding Budget Amendments in Various Funds and the Table of Organization.

MOTION: Chair Scharff moved, seconded by Vice Mayor Filseth to recommend to the City Council to:

1. Amend the Fiscal Year 2019 Budget Appropriation for various funds;

2. Amend the Fiscal Year 2019 Table of Organization for the General Fund to:

    a. Eliminate 1.0 Performance Auditor I in the Office of the City Auditor; and

    b. Reduce 1.4 Building Serviceperson-Lead and reduce 0.75 Building Serviceperson positions; and

3. Amend the Fiscal Year Table of Organization for Other Funds to increase by 1.4 Building Serviceperson-Lead and increase by 0.75 Building Serviceperson.

MOTION PASSED: 4-0

2. Review and Forward the FY 2020 - FY 2029 Long Range Financial Forecast.

ACTION MINUTES

MOTION: Council Member Tanaka moved, seconded by Council Member XX recommend to the City Council that the Finance Committee review, comment, and forward the Fiscal Year 2020 to 2029 General Fund Long Range Financial Forecast (Base Case) for City Council approval and to make the following change: to change the Property Tax estimate to 5.5 percent.

MOTION RESTATED: Council Member Tanaka moved, seconded by Council Member xx to recommend to the City Council that the Finance Committee review, comment, and forward the Fiscal Year 2020 to 2029 General Fund Long Range Financial Forecast (Base Case) to City Council for approval, including the delta's for the budget, and to make the following changes:

1. Use a 5.25 percent increase for the Compound Annual Growth Rate; and

2. Include the Unfunded Actuarial Liability for Pension and Retiree Healthcare Trusts.

MOTION FAILED DUE TO LACK OF A SECOND

MOTION: Chair Scharff moved, seconded by Vice Mayor Filseth to recommend the City Council accept the Long-Range Financial Forecast and forward to the Council for approval.

INCORPORATED INTO THE MOTION WITH THE CONSENT OF THE MAKER AND SECONDER to include delta's in the Long-Range Financial Forecast.

MOTION RESTATED: Chair Scharff moved, seconded by Vice Mayor Filseth to recommend to the City Council to accept the Long-Range Financial Forecast and forward to the Council for approval and to include delta's in the Long Range Financial Forecast.

MOTION AS AMENDED PASSED: 3-1 Tanaka No

<u>Future Meetings and Agendas</u>

MOTION: Chair Scharf moved, seconded by Vice Mayor Filseth to hold the next Finance Committee Meeting at 2:00 PM on Tuesday, December 4, 2018.

MOTION PASSED: 4-0

ADJOURNMENT: Meeting was adjourned at 8:26 P.M.