



# Memorandum

**TO:** PUBLIC SAFETY, FINANCE, AND  
STRATEGIC SUPPORT COMMITTEE

**FROM:** Jim Shannon

**SUBJECT:** BI-MONTHLY FINANCIAL REPORT  
FOR JULY/AUGUST 2019

**DATE:** October 16, 2019

Approved

Date

10-16-19

## RECOMMENDATION

Accept the Bi-Monthly Financial Report on actual revenues and expenditures as compared to the 2019-2020 Budget for the two months ending August 2019.

## OVERVIEW

The Bi-Monthly Financial Report for July/August 2019 was jointly prepared by the City Manager's Budget Office and the Finance Department and is presented for the Public Safety, Finance and Strategic Support Committee's review. The City Manager's Budget Office has analyzed actual expenditures as compared to the 2019-2020 Modified Budget and the Finance Department has prepared a report that reflects the financial results for the two months ending August 2019.

Through the first two months of the fiscal year, revenues and expenditures were generally tracking within the budgeted estimates in the majority of City funds. The Administration will continue to closely monitor economic conditions and the performance in all City funds, bringing forward budget adjustments to the City Council during the year as appropriate. Following are key highlights in this report:

- While it is very early in the fiscal year, and there is minimal data, overall, General Fund revenues appear to be tracking within estimated levels in the General Fund.
- Overall, General Fund expenditures tracked within estimated levels through August. Expenditures will continue to be controlled and monitored to ensure appropriations stay within approved levels.
- Construction and Conveyance Tax, Building and Structure Construction Tax, and Construction Excise Tax collections are performing at anticipated levels. The Construction and Conveyance Tax is anticipated to end the year at budgeted levels. However, the Building and Structure Construction Tax and the Construction Excise Tax may exceed budgeted levels. These revenues will be closely monitored and, if necessary, budget adjustments may be brought forward for City Council consideration at a later date.

**OVERVIEW (CONT'D.)**

- Development-related revenues in the General Fund through August 2019 have generally grown from the same time period in the prior fiscal year and, with the exception of the Public Works Development Fee Program, are anticipated to meet budgeted levels by year-end. These revenues will continue to be monitored, and if necessary, budgetary actions may be brought forward later in the year to align the budget with anticipated levels.
- The Norman Y. Mineta San José International Airport (SJC) has enplaned and deplaned close to 3.0 million passengers through August, an increase of 10.0% from the figures reported through August of the prior year.
- In Silicon Valley, economic conditions remain positive, but economic indicators are continuing to moderate from the strong levels experienced in recent years. Overall, “sluggish” economic growth was anticipated and corresponding revenues have been budgeted accordingly. In addition, several economically sensitive revenues such as the Construction and Conveyance (C&C) Tax and the Transient Occupancy Tax (TOT), are experiencing declines from prior year levels. The drop in the C&C Tax was anticipated and is currently expected to meet budgeted levels; a decline in TOT was not anticipated. However, with only one month of data for TOT, it is generally too early to make a determination if revenues will fall below budgeted estimates. The Administration will continue to closely monitor the City’s economically sensitive revenues and will identify any changes in collection trends as appropriate.
- The Administration will continue to report to the City Council all significant developments through future Bi-Monthly Financial Reports and the 2018-2019 Mid-Year Budget Review.

**Economic Environment**

As mentioned above, while overall economic conditions in the Silicon Valley remain positive, the growth is continuing to moderate. The August 2019 employment level in the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (San José MSA) of 1.09 million was 1.2% above the August 2018 level of 1.08 million.





**OVERVIEW (CONT'D.)**

Between August 2018 and August 2019, employment in the San José MSA expanded by 28,800 jobs (2.5%). This growth includes an increase of 8,600 jobs in the information sector; 7,100 jobs in the professional and business industries; manufacturing up 6,400 jobs with computer and electronic product manufacturing (up 4,900 jobs) driving the job gains; and 5,300 jobs in the professional, scientific, and technical services sectors.<sup>1</sup>

The unemployment rates at the local, State, and national levels have continued to slightly drop compared to the prior year. In August 2019, the unemployment rate for the San José Metropolitan Statistical Area of 2.7% is marginally below the July 2019 and August 2018 unemployment rate of 2.8%. In this region, the August 2019 unemployment rate continues to be lower than the unadjusted unemployment rate for the State (4.2%) and the nation (3.8%).

<b>Unemployment Rate (Unadjusted)</b>			
	<b>August 2018</b>	<b>July 2019</b>	<b>August 2019**</b>
San Jose Metropolitan Statistical Area*	2.8%	2.8%	2.7%
State of California	4.3%	4.5%	4.2%
United States	3.9%	4.0%	3.8%

\* San Benito and Santa Clara Counties  
Source: California Employment Development Department.  
\*\* August 2019 estimates are preliminary and may be updated.

Overall construction activity through August 2019 has increased 176.7% from 2018-2019 levels. The increase was primarily due to the exceptional industrial activity in July 2019, setting a record of valuations over \$100 million. The 2019-2020 budget was developed with the expectation that private development activity would remain strong, though will likely moderate over the course of the year.

Through August, overall residential permit valuation increased from prior year levels. The number of residential units increased (490 new dwelling units in 2019-2020, compared to 296 in 2018-2019) and valuation was higher than prior year levels as well (\$89.4 million in 2019-2020, compared to \$72.6 million in 2018-2019). Valuation for alteration activity level increased from the prior year (\$31.8 million in 2019-2020, compared to \$20.4 million in 2018-2019). The 490 residential units through August 2019 included 396 multi-family units and 94 single family units. Significant residential projects for July and August included a permit issued for a three-story, 97-unit apartment building (located on North 7<sup>th</sup> Street between Jackson Street and East Empire Street) and a six-story, 299-unit apartment building (located on North 6<sup>th</sup> Street between East Taylor Street and Jackson Street).

<b>Private Sector Construction Activity (Valuation in \$ Millions)</b>			
	<b>YTD August 2018</b>	<b>YTD August 2019</b>	<b>% Change</b>
Residential	\$ 72.6	\$ 89.4	23.1%
Commercial	\$ 60.9	\$ 149.0	144.7%
Industrial	\$ 94.8	\$ 393.2	314.8%
<b>TOTAL</b>	<b>\$ 228.3</b>	<b>\$ 631.6</b>	<b>176.7%</b>

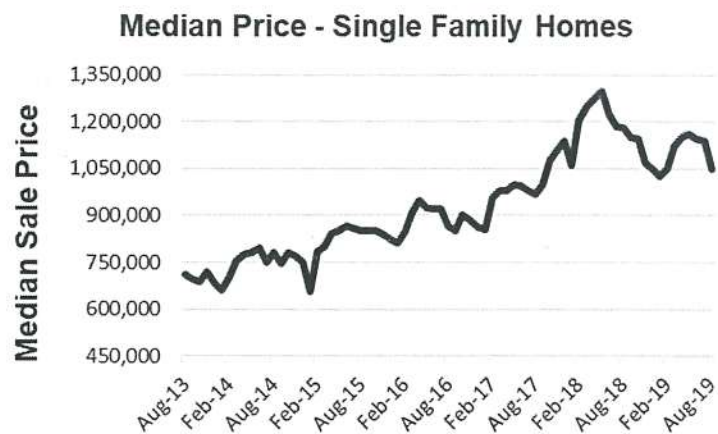
<sup>1</sup> State of California Employment Development: Labor Market Information Division Press Release, September 20, 2019

**OVERVIEW (CONT'D.)**

Commercial valuation through August 2019 is significantly higher than the 2018-2019 level (\$149.0 million in 2019-2020, compared to \$60.9 million in 2018-2019). New commercial construction activity and alteration activity are both higher than the prior year levels. A notable project for July and August includes a construction permit for a 9-story garage for two office buildings (located on Devcon Court between East Brokaw Road and Zanker Road).

Industrial construction valuation through August is also significantly higher than prior year levels (\$393.2 million in 2019-2020, compared to \$94.8 million in 2018-2019). As mentioned above, industrial activity was exceptionally high in July 2019 (\$386.0 million) with alterations only accounting for 6% of the activity (\$23.7 million). The activity dramatically dropped in August with alterations accounting for all of the activity (\$7.1 million). The notable project for July and August was a 5-story data center building with 238,000 square feet of space for the data center and 67,000 square feet of office space (located south of Highway 85 and west of Monterey Road).

Beginning in spring 2012, the median sale price for homes had consistently experienced year-over-year growth, which continued until 2018. Over the past year, however, Santa Clara County began to experience a slow down in the local real estate market, which included median sale prices dropping, the average days on market increasing, and the number of sales decreasing. According to data from the Santa Clara County Association of Realtors, the single-family home price peaked at \$1.3 million in May 2018 (which represented a 30.0% increase from the May 2017 home price), but then began steadily decreasing. In addition, year-over-year median prices have steadily decreased each month since November 2018, with drops ranging from 3%-13% compared to the prior year level. In August 2019, the median single-family home price totaled \$1.1 million, which represents a 11.0% decrease from the August 2018 price of \$1.2 million, but is almost 9% above the August 2017 price of \$967,000.



In addition to the median home prices dropping, the number of property transfers (sales) has also continued to steadily decline. The number of property transfers in August 2019 totaled 650, which represents a 4.0% drop from the 677 transfers that occurred in August 2018. In addition, while single-family and multi-family dwellings are continuing to sell relatively quickly, they are on the market significantly longer than the prior year. The average days-on-market for single-family and multi-family dwellings in August 2019 totaled 35 days, compared to 20 days experienced in August 2018. The increase in August 2019 represents growth of 75.0% from the extremely short number of days homes were active on the market in August 2018.



## OVERVIEW (CONT'D.)

On a national level, consumer confidence declined marginally in August, following a rebound in July. Lynn Franco, Senior Director of Economic Indicators at The Conference Board, stated “Consumer confidence was relatively unchanged in August, following July’s increase. Consumers’ assessment of current conditions improved further, and the Present Situation Index is now at its highest level in nearly 19 years (November 2000). Expectations cooled moderately, but overall remain strong. While other parts of the economy may show some weakening, consumers have remained confident and willing to spend. However, if the recent escalation in trade and tariff tensions persists, it could potentially dampen consumers’ optimism regarding the short-term economic outlook.”<sup>2</sup>

Economic conditions will continue to be closely monitored and will be factored into the assessment of the City’s performance in 2019-2020 as well as the development of the 2021-2025 General Fund Forecast that will be released in February 2020.

## GENERAL FUND

### REVENUES

General Fund revenues through August 2019 totaled \$99.5 million, which represents a decrease of \$92.7 million (48.2%) from the August 2018 level of \$192.1 million. This decrease is primarily attributable to the City no longer borrowing proceeds from the Tax and Revenue Anticipation Notes (TRANs), which were previously issued for cash flow purposes to facilitate the annual prefunding of employer retirement contributions for pension benefits. However, beginning in 2019-2020, this prefunding, which totaled \$150.0 million in 2018-2019, is no longer occurring. Excluding the TRANs revenue in 2018-2019, revenue in 2019-2020 has grown approximately \$57.3 million from the prior year. This increase is primarily due higher receipts in the Overhead Reimbursements category (\$37.5 million), as these reimbursements were not processed until later in the year in 2018-2019. In addition, several other categories are experiencing growth compared to prior year levels, including Utility Tax (\$5.5 million), Other Revenue (\$3.5 million), Licenses and Permits (\$2.3 million), and Revenue from Local Agencies (\$1.3 million). However, while most revenues are performing stronger than the prior year, there are several categories experiencing declines; including, Business Taxes, Franchise Fees, Telephone Line Tax, and Transient Occupancy Tax. The lower collections in these categories are primarily due to timing of payments. It is important to note that although these revenues may be lower than prior year receipts, only very preliminary information is currently known, therefore at this early point in the year the revenues are overall anticipated to meet the budgeted level by year-end.

The following discussion highlights General Fund revenue activities through August.

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<sup>2</sup> The Conference Board, Consumer Confidence Survey, August 27, 2019

<b>GENERAL FUND (CONT'D.)</b>
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**KEY GENERAL FUND REVENUES**

Revenue	2019-2020 Budget Estimate	YTD Actual	Prior YTD Collections
<b>Property Tax</b>	<b>\$ 354,000,000</b>	<b>\$ 566,352</b>	<b>\$ 271,564</b>

The Property Tax category consists of Secured Property Tax, Unsecured Property Tax, SB 813 Property Tax (retroactive collections back to the point of sale for reassessments of value due to property resale), Aircraft Property Tax, and Homeowner’s Property Tax Relief. In 2019-2020, Property Tax receipts are estimated at \$354.0 million, which reflects growth of 7.2% from the 2018-2019 collection level of \$330.2 million. The anticipated growth in Property Tax revenue is primarily attributed to Secured Property Tax, which is estimated at \$329.4 million in 2019-2020 (9.0% above the 2018-2019 collection level). Through August, Property Tax revenue of \$566,000 has been received, which is higher than the prior year receipts of \$272,000. However, a majority of the revenue in this category does not begin to be received until October of each year. At this early point in the year, Property Tax revenue is overall anticipated to meet budgeted levels. Additional information about each of the Property Tax sub-categories is provided on the following pages.

**Secured Property Taxes** represent over 90% of the revenue in the Property Tax category. The Secured Property Tax category includes general Secured Property Tax, Educational Revenue Augmentation Fund (ERAF) revenues, and Successor Agency to the Redevelopment Agency (SARA) Residual Property Tax. The 2019-2020 Secured Property Tax estimate of \$329.4 million was built on assumed growth of 5.5% for general Secured Property Tax receipts (\$293.6 million), estimated revenue of \$19.8 million for ERAF receipts, and \$16.0 million for SARA revenue. As anticipated, no Secured Property Tax receipts have been received through August due to the scheduled timing of these payments.

As mentioned above, the general Secured Property Tax estimate totals \$293.6 million in 2019-2020, which assumes growth of 5.5% from the 2018-2019 collection level. This growth primarily reflects an increase in assessed value due to the California Consumer Price Index (CCPI) increase of 2% and increased valuation due to changes in ownership or new construction. Under Proposition 13, assessed values of all real property adjust with the CCPI, with a 2% limit, unless there is a change in ownership, new construction, or a property has received a Proposition 8 adjustment. The preliminary general Secured Property Tax estimate provided by the County totals \$291.0 million, which is approximately 1% below the budgeted estimate. However, as it is still very early in the year, this estimate will likely change as additional information is known. The 2019-2020 estimated collection level will continue to be monitored and information will be included in future Bi-Monthly Financial Status Reports, the 2019-2020 Mid-Year Status Report, and the 2020-2021 budget process.



**GENERAL FUND (CONT'D.)**

Beginning in 1992, agencies have been required to reallocate a portion of property tax receipts to the ERAF, which offsets the State's General Fund contributions to school districts under Proposition 98. However, once there are sufficient funds in ERAF to fulfill obligations, the remainder of the funding is returned to the taxing entities that contributed to it, which generally occurs in March of each fiscal year. The 2019-2020 budget assumes the excess ERAF collections the City will receive in the current year will total \$19.8 million; however, the County provided preliminary information in August that a payment of approximately \$23.0 million may actually be received in the current year. The Administration will continue to monitor the distribution of ERAF receipts and may adjust the budget upward at a later date once further information is provided by the County.

As a result of the SARA bond refunding that occurred in December 2017, the City began receiving a residual property tax distribution. In 2017-2018, receipts totaled \$11.8 million, but dropped to \$8.2 million in 2018-2019. This decrease was due to outstanding Supplemental Education Revenue Augmentation Fund (SERAF) loans that were paid off in 2019. In 2019-2020, SARA residual property tax revenue is budgeted at \$16.0 million.

In the **Unsecured Property Tax** category, the largest payment is received in October of each year. The 2019-2020 Adopted Budget revenue estimate of \$15.0 million allows for an approximate 5% drop from the actual 2018-2019 collection level of \$15.8 million. The preliminary estimate from the County of Santa Clara for 2019-2020 totals \$14.8 million, which is slightly lower than the budgeted estimate.

For the **SB 813 Property Tax** category, collections totaled \$406,000 through August, while \$272,000 had been received last year at this time. The 2019-2020 Adopted Budget estimate of \$6.3 million is well below the 2018-2019 actual collection level of \$8.6 million as collections in this category ended 2018-2019 stronger than anticipated. However, the preliminary 2019-2020 estimate from the County for this category of \$6.0 million is approximately \$300,000 below the budgeted estimate.

**Aircraft Property Tax** receipts are typically received in October of each year. The 2019-2020 Adopted Budget estimate of \$2.4 million is consistent with the 2018-2019 receipts, and is slightly above the \$2.2 million estimated from the County of Santa Clara Assessor's Office.

In the **Homeowners Property Tax Relief** category, revenues in 2019-2020 are expected to be at the budgeted estimate of \$900,000, which is consistent with the 2018-2019 collection level.

**GENERAL FUND (CONT'D.)**

Revenue	2019-2020 Budget Estimate	YTD Actual	Prior YTD Collections
<b>Sales Tax</b>	<b>\$ 258,300,000</b>	<b>\$ 0</b>	<b>(\$ 3,872,949)</b>

The Sales Tax category includes General Sales Taxes, Local Sales Taxes, and Proposition 172 Sales Taxes. The 2019-2020 Adopted Budget for Sales Tax totals \$258.3 million, which allows for a 2.0% drop from the 2018-2019 collection level of \$263.5 million. The 2019-2020 Sales Tax estimate was derived from factoring in the following: reducing the 2018-2019 estimate by \$10 million, to account for the one-time overpayment in 2018-2019 from the California Department of Tax and Fee Administration (CDTFA) for 2017-2018 activity; estimated 2.5% underlying growth from the 2018-2019 estimate; and additional revenue of \$5.0 million anticipated for out-of-state internet sales as a result of the United States Supreme Court's ruling on South Dakota vs. Wayfair, Inc. The 2019-2020 Sales Tax estimate does not include any revenue related to the Revenue Capture Agreement between the City and eBay that was approved by the City Council on September 24, 2019. Any funding the City may receive as a result of the agreement would not be disbursed by the CDTFA until February 2020; and as there continues to be uncertainty regarding the revenue, a budget adjustment will not be recommended until the funds are received from the CDTFA.

Sales Tax payments are distributed from the CDTFA four times throughout the year. The first payment, which represents sales tax activity for July through September will not be received until November 2019. Therefore, at this time no additional information regarding Sales Tax receipts for 2019-2020 are known.

In June 2018, the United States Supreme Court made a historic ruling with the South Dakota vs. Wayfair, Inc., decision which provides states with the authority to require online retailers to collect sales tax even without a local presence in that state. The 2019-2020 budget was built on the assumption revenue totaling \$5.0 million would be received (\$4.0 million for General Sales Tax and \$1.0 million for Local Sales Tax) as a result of the Supreme Court's ruling. Out-of-state online retailers began complying with the new Sales Tax guidelines beginning in April 2019, however, marketplace facilitators did not begin complying until October 2019. The impact of the out-of-state online and marketplace facilitators is still unknown. Additional information is anticipated to be received and analyzed over the next several months and will be included in future Bi-Monthly Financial Reports and the 2019-2020 Mid-Year Budget Review.

Below is a discussion of the three Sales Tax sub-categories; General Sales Tax, Local Sales Tax, and Proposition 172 Sales Tax.

When the 2019-2020 Adopted Budget was developed, **General Sales Tax** was anticipated to total \$204.8 million in 2018-2019 and drop slightly to \$204.6 million in 2019-2020. The 2019-2020 estimate was the result of factoring out one-time adjustments related to the 2018-2019



**GENERAL FUND (CONT'D.)**

overpayment from the CDTFA attributable to 2017-2018 activity (\$9.0 million), assumed 2.5% underlying growth from the 2018-2019 estimate, and an estimated \$4.0 million anticipated to be received for out-of-state internet sales. However, since 2018-2019 receipts ended the year at \$209.8 million, the 2019-2020 budget allows for a 2.5% decline. Due to several uncertainties related to Sales Tax, such as the amount of revenue that will be received by out-of-state internet sales, and since revenue has not yet been received in the current year, it is too early to determine how General Sales Tax revenue will perform compared to budgeted levels.

On September 24, 2019 the City Council approved the Revenue Capture Agreement Between City of San José and eBay Inc. memorandum. As part of this memorandum, the City Council adopted a resolution authorizing the City Manager to negotiate and execute a Revenue Capture Agreement between the City and eBay, beginning in 2019 and ending in 2034. This agreement may result in the City receiving additional General Sales Tax ranging from \$5.0 million up to possibly \$29.5 million annually. As previously discussed, budget adjustments related to this revenue will not be brought forward for City Council consideration until the funds are distributed from the CDTFA (anticipated in February 2020).

In June 2016, San José voters approved a ¼ cent **Local Sales Tax**, which was implemented in October 2016. The 2019-2020 Local Sales Tax budget was built on the assumption 2018-2019 receipts would total \$47.7 million and drop slightly to \$47.0 million in 2019-2020. The 2019-2020 estimate was the result of factoring out one-time adjustments related to the 2018-2019 overpayment from the CDTFA attributable to 2017-2018 activity, assumed 2.5% underlying growth from the 2018-2019 estimate, and an estimated \$1.0 million anticipated to be received for out-of-state internet sales. As mentioned above, due to several uncertainties related to Sales Tax, such as the amount of revenue that will be received by out-of-state internet sales, and since revenue has not yet been received in the current year, it is too early to determine how Local Sales Tax revenue will perform compared to budgeted levels.

**Proposition 172 Sales Tax** collections represents the ½ cent tax that is allocated to counties and cities on an ongoing basis for funding public safety programs. The 2019-2020 budgeted estimate of \$6.7 million requires growth of approximately 2.5% from the 2018-2019 collection level of \$6.5 million. It is currently anticipated that collections will meet the budgeted estimate by year-end.

<b>GENERAL FUND (CONT'D.)</b>
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Revenue	2019-2020 Budget Estimate	YTD Actual	Prior YTD Collections
<b>Transient Occupancy Tax</b>	<b>\$ 22,500,000</b>	<b>\$ 1,073,665</b>	<b>\$ 1,294,157</b>

The 2019-2020 budget estimate for the General Fund **Transient Occupancy Tax** (TOT) allocation (40% of the total tax) is \$22.5 million, which was built assuming growth of approximately 7% from the 2018-2019 estimated collection level of \$21.0 million. However, since actual 2018-2019 receipts were below the revised estimated level (\$20.7 million) at \$20.5 million, growth of approximately 9.6% is needed to meet the 2019-2020 budget estimate. Year-to-date TOT receipts through August 2019 of \$1.1 million are 17% below the prior year collection level of \$1.3 million. This variance is primarily due to lower occupancy levels and room rates for July, which were lower compared to recent years, but consistent with the seasonality exhibited over summer months, and a relatively large negative accrual in July. Year-over-year revenues received in the month of August that excludes accruals are down 11%. Based on the increased room supply from the recent openings of three hotels in North San José (Fairfield Inn & Suites, Residence Inn, and Hyatt Place), and seasonality exhibited over preceding fiscal years, bookings and corresponding revenues are anticipated to begin rebounding through the next quarter.

Through August 2019, the average hotel occupancy rate reported for the San José market was 77.85%, a decrease of 5% over the same period in 2018-2019. Average room rates also decreased by 2.3%, from \$193.75 to \$189.20, and the year-to-date average revenue-per-available room (RevPAR) decreased 8.2%, from \$160.46 to \$147.28, relative to the same period in 2018-2019. Given the known seasonality, limited year-to-date activity, and recent supply changes, the Administration will continue to monitor TOT performance closely, and if necessary, will bring forward downward revenue adjustments at a later point.



**GENERAL FUND (CONT'D.)**

Revenue	2019-2020 Budget Estimate	YTD Actual	Prior YTD Collections
<b>Utility Tax</b>	<b>\$ 99,645,000</b>	<b>\$ 9,394,398</b>	<b>\$ 3,920,430</b>

The **Utility Tax** category includes the Electricity Utility Tax, Gas Utility Tax, Water Utility Tax, and the Telephone Utility Tax. Through August, Utility Tax receipts of \$9.4 million are significantly higher than the prior year level of \$3.9 million. The year-over-year increase is primarily due to higher Electricity Utility Tax receipts, which totaled \$5.6 million in August 2019 compared to only \$215,000 in August 2018, due to the timing of payments. The 2019-2020 Adopted Budget was built on the assumption that 2018-2019 Utility Tax revenue would end the year at \$99.0 million and grow less than 1% to \$99.6 million in 2018-2019. However, since 2018-2019 ended the year at \$99.3 million, growth of less than 0.5% is needed in 2019-2020 to meet the budgeted estimate. Based on historical collection trends and performance through this very early point in the year, it is anticipated overall Utility Taxes will meet budgeted levels by year-end.

In the **Electricity Utility Tax** category, collections through August totaled \$5.6 million, which is significantly above the \$215,000 received in the prior fiscal year, due to the timing of payments. The 2019-2020 Adopted Budget assumed that 2018-2019 receipts would total \$46.0 million, and grow approximately 2% to \$46.9 million in 2019-2020. However, since 2018-2019 ended the year slightly below budget (\$45.6 million), growth of almost 3% is needed to meet the budgeted estimate. Based on the preliminary information known at this very early point in the year, receipts are anticipated to meet or exceed the budgeted estimate by year-end.

In the **Gas Utility Tax** category, receipts through August totaled \$594,000, a significant increase from the previous year collection of \$76,000 due to the timing of payments. The 2019-2020 Adopted Budget estimate of \$10.4 million allows for an almost 7% decline from actual 2018-2019 collections (\$11.1 million) due to receipts performing stronger than anticipated at the end of 2018-2019. Based on the preliminary information known at this very early point in the year, receipts are anticipated to meet or exceed the budgeted estimate by year-end.

**Water Utility Tax** collections of \$1.3 million through August are 16.2% below the prior year level of \$1.5 million. The 2019-2020 Adopted Budget was built on the assumption that \$16.3 million would be received in 2018-2019, then grow approximately 2.5% to \$16.7 million in 2019-2020. However, since 2018-2019 receipts totaled \$16.6 million, growth of less than 1% is required to meet the 2019-2020 budgeted level. Based on the preliminary information known at this very early point in the year, receipts are anticipated to meet or fall below the budgeted estimate by year-end.

Collections in the **Telephone Utility Tax** category of \$1.9 million through August are 9.5% below the prior year collections of \$2.1 million. The 2019-2020 Adopted Budget estimate of \$25.6 million allows for a slight decline (1.2%) from the 2018-2019 actual collection level of \$26.0 million. Based on current collection trends, receipts in this category are anticipated to meet or fall below the budgeted estimate by year-end.



**GENERAL FUND (CONT'D.)**

Revenue	2019-2020 Budget Estimate	YTD Actual	Prior YTD Collections
<b>Business Taxes</b>	<b>\$ 72,200,000</b>	<b>\$ 9,895,996</b>	<b>\$ 11,074,300</b>

The Business Taxes category consists of the Cannabis Business Tax, Cardroom Tax, Disposal Facility Tax, and General Business Tax. Through August, overall collections of \$9.9 million are 10.6% below the prior year collection levels of \$11.1 million, primarily reflecting lower collections in the Disposal Facility Tax and General Business Tax categories. The 2019-2020 Adopted Budget estimate of \$72.2 million allows for a 3.6% decline from 2018-2019 levels as the result of revenues performing stronger than anticipated at the end of 2018-2019.

**Cannabis Business Tax** collections reflect cannabis business tax as well as cannabis business tax compliance revenues. Through August, receipts of \$1.0 million are 14.5% below prior year levels of \$1.2 million. In November 2016, the California Marijuana Legalization Initiative (Proposition 64) legalized recreational marijuana use in the State of California. As a result, the sale of recreational cannabis at the 16 licenses dispensaries in San José began in January 2018. The 2019-2020 Adopted Budget estimate of \$13.5 million allows for a 15.0% drop from 2018-2019 actual collection levels. This decrease was anticipated as a result of neighboring cities passing Cannabis taxes in the November 2018 election, which will provide competition for San José when the dispensaries are open in other jurisdictions. Although it is very early in the fiscal year, based on collections through August, it is anticipated revenue will meet the budgeted level by year end.

Through August, **Cardroom Tax** receipts of \$1.6 million are consistent with the prior year collections and are projected to meet the budgeted estimate of \$18.7 million. Because receipts in 2018-2019 slightly exceeded expectations, collections in the category can drop by approximately 1% in 2019-2020 and reach the budgeted estimate.

**Disposal Facility Tax** revenue of \$439,000 is significantly below the prior year level of \$1.0 million due to the timing of payments. The 2019-2020 budgeted estimate of \$12.0 million is fairly consistent with the 2018-2019 actual collection level of \$12.1 million. Based on the preliminary information known at this very early point in the year, receipts are anticipated to meet the budgeted estimate by year-end. Multiple factors impact collections including construction activity, population density, and the hauling of solid waste from outside the immediate area as other facilities might be farther away or costlier. Therefore, this revenue source can fluctuate from year to year.

Through August, **General Business Tax** receipts of \$6.8 million are 5.6% below prior year collection levels. The 2019-2020 budget estimate for General Business Tax revenue totals \$28.0 million, which is consistent with the 2018-2019 actual collection level. With the recent launch of the Business Tax Amnesty program, which runs through March 27, 2020 and is expected to increase receipts this year and ongoing, staff will continue to monitor and report on this revenue category.



**GENERAL FUND (CONT'D.)**

Revenue	2019-2020 Budget Estimate	YTD Actual	Prior YTD Collections
<b>Licenses and Permits</b>	<b>\$ 62,009,468</b>	<b>\$ 13,791,926</b>	<b>\$ 11,474,509</b>

The Licenses and Permits category contains fees and charges collected by various departments. The most significant revenue sources are development-related fees, which include Building Permits and Fire Permits. Through August, revenues of \$13.8 million are 20.2% above the prior year level of \$11.5 million. The 2019-2020 Adopted Budget estimate of \$62.0 million allows for a 5.0% drop from prior year collections of \$65.3 million. Based on activity through August, Licenses and Permits receipts are estimated to meet or exceed budgeted levels by year-end.

**Building Permit** revenues of \$6.8 million through August are 9.9% higher than the 2018-2019 collection level for the same period. The 2019-2020 Adopted Budget estimate of \$33.8 million allows for an 8.0% drop from the 2018-2019 actual collection level of \$36.7 million due to collections performing stronger than anticipated at the end of 2018-2019. It is currently anticipated revenues will meet or exceed the budgeted estimate by year-end.

All Building Permit categories are performing at expected levels with the exception of new residential permits in the building plan check, new residential building permits, new residential plumbing permits, new residential mechanical permits, new residential electrical permits, and permit processing fees, which are performing below anticipated levels.

As discussed in the Economic Impact section of this report, residential activity through August 2019 consisted of 396 multi-family units and 94 single-family units for a total of 490 units. Commercial activity through August amounted to a valuation of \$149.0 million (new construction of \$101.1 million, alterations of \$47.9 million). Industrial activity through August reached a valuation of \$393.2 million (new construction of \$362.4 million, alterations of \$30.8 million). Alteration activity accounted for all the industrial activity in August.

**Fire Permits**, which consist of development and non-development related permits, totaled \$4.1 million through August, which represents a 6.8% increase from the prior year collections. The 2019-2020 budget estimate of \$14.0 million is consistent with the actual 2018-2019 collection level. It is currently anticipated collections will meet or exceed the budgeted levels by year-end.

Development related receipts through August of \$1.6 million are \$150,000 higher than the prior year collections. The budgeted estimate of \$8.4 million is lower than the prior year collections of \$8.6 million and it is anticipated that receipts will meet or exceed the budget by year-end.

Non-Development receipts of \$2.6 million represents 45.7% of the budget and are 4.5% above revenues received through August 2018. This collection represents the first of four major billing cycles for non-development fire permits for this fiscal year. To meet the 2019-2020 budgeted estimate of \$5.6 million, growth of 3% from the 2018-2019 actual collection level of \$5.4 million is needed; at this point of the year, collections are anticipated to meet or exceed budgeted levels by year-end.



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**GENERAL FUND (CONT'D.)**

Revenue	2019-2020 Budget Estimate	YTD Actual	Prior YTD Collections
<b>Fees, Rates, and Charges</b>	<b>\$ 58,951,740</b>	<b>\$ 8,790,677</b>	<b>\$ 9,869,881</b>

The Fees, Rates, and Charges category contains various fees and charges levied to recover costs of services provided by several City departments, including Library; Parks, Recreation and Neighborhood Services; Planning, Building and Code Enforcement; Police; Public Works; and Transportation. Through August, revenues totaled \$8.8 million, which is 10.9% below the \$9.9 million received in the prior year. All departments within the Fees, Rates, and Charges category, with the exception of the Parks, Recreation and Neighborhood Services, Public Works, and Police Departments, demonstrated year-over-year increases compared to the prior year levels. The 2019-2020 budget estimate of \$59.0 million requires a 5.8% increase from the actual 2018-2019 collection level. At this early point in the year it is anticipated the overall Fees, Rates, and Charges category will meet or fall below budgeted levels by year-end.

Through August, **Planning Fee** revenues of \$1.1 million are 8.1% above the prior year collection level of \$1.0 million. Revenue was stable or strong for several fees, including residential General Plan amendments, non-residential conventional rezonings/rezonings, residential and non-residential environmental clearances, and single-family design review. Partially offsetting this growth in activity, are several fees that are performing below anticipated levels. These fees include non-residential tentative maps, public noticing, non-residential site development permits, and miscellaneous permits. Based on current collection trends, Planning Fee revenues are anticipated to meet or exceed the 2019-2020 budget revenue estimate of \$8.1 million. Revenues will continue to be monitored closely to determine if any actions need to take place during the year to align the budgeted estimate with actual revenues.

**Public Works** revenues through August of \$967,000 decreased 58.7% from the prior year level of \$2.3 million, which is primarily due to the timing of Small Cell Permitting fee payments. The Public Works Development total revenue collections through August 2019 are comprised of \$815,000 from the Development Services Fee Program and \$152,000 from the Utility Fee Program. No fees have been collected through August for Small Cell Permitting. Based on activity through August, collections in Public Works revenues are anticipated to meet the budgeted levels by year-end, which is primarily due to lower revenues in the Development Services Fee Program.

Development Services Fee Program revenues are below anticipated year-to-date levels, primarily due to lower activity levels in engineering residential and non-residential fees. In addition, Utility Fee collections are lower than anticipated at this point in the year. Based on current collections, Public Works' Development and Utility Fee revenues are anticipated to meet or fall slightly below the budgeted estimate. Revenues will continue to be monitored closely to determine if any actions need to take place during the year to align the budgeted estimate with actual revenues.



**GENERAL FUND (CONT'D.)****EXPENDITURES**

Through August, General Fund expenditures (without encumbrances) of \$203.4 million were 16.3% above the prior year level of \$174.9 million. Encumbrances of \$71.0 million were 12.5% above the prior year level of \$63.1 million. General Fund expenditures and encumbrances through August of \$274.4 million constitute 18.0% of the total budget including reserves, and 20.3% of the budget excluding reserves. Overall, expenditures are slightly exceeding estimated levels through August.

Through August, a small number of departments were performing slightly above the budgeted estimate in personal services expenditures, including the Public Works Department that had seasonal over-time hours, which caused their expenditures to track slightly high. Expenditures will continue to be controlled and monitored to ensure appropriations stay within approved levels. Following is a discussion of the performance of the Police and Fire Departments, the largest General Fund departments.

**KEY GENERAL FUND EXPENDITURES**

Department	2019-2020 Budget	YTD Actual	Prior YTD Actual
<b>Police</b>	<b>\$ 448,793,371</b>	<b>\$ 71,327,005</b>	<b>\$ 66,989,110</b>

Overall, the Police Department's expenditures are currently anticipated to end the year within budgeted levels. Personal services expenditures through August of \$62.5 million were 0.1% below the anticipated level at this point of the year (14.96% expended, compared to the par of 15.03%). Overtime expenditures of \$6.7 million reflect 23.43% of the total \$28.6 million budget. In addition, Non-personal/equipment expenditures of \$2.2 million are 41.3% lower than the prior year (due to the timing of payments), and are anticipated to end the year within budgeted levels.

As mentioned, personal services expenditures are within estimated levels at this point of the year. These expenditures include funding related to the Guardian Rapid Response Program that began in summer 2019, however, budgetary funds have not yet been allocated for the program. Included in the 2018-2019 Annual Report, which was released on September 30, 2019, is a recommendation to allocate \$3.0 million in overtime funding for this new program, which is designed to enhance the state of readiness for an active shooter attack at school campuses and at large special events. Through the first two months of the year, savings has enabled the Police Department to allocate resources for the Guardian Rapid Response Program without over-expending the personal services budget. This savings is primarily due to Hire Ahead program that began in 2019-2020 (provides \$7.0 million to hire new recruits in advance of pending retirements), but since backgrounding and recruiting is still underway, positions have not yet been filled. Provided that funding of \$3.0 million for the Guardian Rapid Response Program is approved by the City Council, at this early point in the year, expenditures are anticipated to end the year within budgeted levels; however,



**GENERAL FUND (CONT'D.)**

other factors such as anticipated recruit academies, special events, projected attrition, overtime trends, and compensatory time payouts, are subject to change. The Police Department has worked diligently to fill vacancies in both sworn and civilian positions, using vacancy savings in the meantime to pay for Police Academy Recruits as well as to backfill patrol and investigative positions on overtime. While the goal is to fill the vacancies and eliminate the need to backfill positions, academy and field training of new recruits takes 10-12 months, necessitating overtime to backfill until the new recruits are ready to serve as solo beat officers. Vacancy levels have also contributed to the build-up of compensatory time balances for sworn personnel. There is a limit of 480 hours of compensatory time balances after which sworn personnel are paid in overtime for any additional hours worked. Currently, 345 sworn personnel are at the 480-hour limit.

Overtime consists of overtime expenditures and compensatory time. The Memorandum of Agreement (MOA) with the Police Officer's Association (POA) limits how much overtime can be earned for pay versus compensatory time. The compensatory time balance at the end of August 2019 was 305,015 hours for sworn personnel. This represents an increase of 37,243 hours or 13.9% compared to the August 2018 balance of 267,772. As described above, 345 sworn personnel have reached the compensatory balance limit of 480 hours and all overtime worked by these employees is paid overtime. The Police Department is enforcing compensatory time reduction by requiring all sworn staff, outside of the Bureau of Field Patrol (BFO), to reduce compensatory time balances by the end of the calendar year or submit a request for an extension, per the MOA. Due to staffing levels needed to respond to calls for service, BFO is currently exempted until such time the Department reaches full street-ready sworn staffing (sworn who are fully trained and able to work as solo beat officers).

The table below provides a summary of sworn staffing vacancies and street-ready positions. While the vacancy level for sworn positions has decreased when compared against higher authorized sworn staffing levels, there is still a significant gap between filled positions and working street-ready positions. Though this gap is expected to decrease with the implementation of the Hire Ahead Program currently underway, it will fluctuate throughout the year due to the timing of pending retirements and the transition of academy recruits into officers. The Department expects only a minimum number of vacancies by fall 2020.

	<b>2018-2019 (as of 9/21/2018)</b>	<b>2019-2020 (as of 9/20/2019)</b>
<b>Authorized Sworn Staffing</b>	<b>1,110</b>	<b>1,151</b>
Vacancies	(38)	(40)
<b>Filled Sworn Staffing</b>	<b>1,072</b>	<b>1,111</b>
Field Training Officer/Recruits	(116)	(117)
<b>Street-Ready Sworn Positions Available</b>	<b>956</b>	<b>994</b>
Disability/Modified Duty/Other Leaves	(75)	(78)
<b>Street-Ready Sworn Positions Working</b>	<b>881</b>	<b>916</b>



**GENERAL FUND (CONT'D.)**

To fill the vacant sworn positions and put more Police Officers back on patrol, the Police Department will continue to conduct three Police Recruit Academies in 2019-2020: the first began in late June 2019 with 53 recruits; the second academy begins in October 2019 with a projected 50 recruits; and the third begins in February 2020 with an estimated 45 to 55 recruits. In addition, the academy that began in February 2019 completed in September 2019 with 37 recruits graduating.

A total of \$8.8 million (28.6%) of the Department's Non-Personal/Equipment budget (including carryover encumbrances) was expended or encumbered through August. Excluding the remaining balances for centrally-determined details, including electricity, gas, and vehicle operation and replacement, the Police Department has approximately \$12.9 million, or 64.8% of the non-centrally-determined appropriation available for the remainder of the fiscal year.

Department	2019-2020 Budget	YTD Actual	Prior YTD Actual
<b>Fire</b>	<b>\$ 242,918,817</b>	<b>\$ 37,999,197</b>	<b>\$ 37,401,317</b>

The Fire Department's budget totals \$242.9 million, which is comprised of \$232.4 million in personal services and \$10.5 million in non-personal/equipment. Overall, Fire Department expenditures are performing slightly above estimated levels through August. Personal services expenditures of \$35.0 million, or 15.07% of the Modified Budget, are slightly above the expected level of 15.03% at this point of the year. It is currently anticipated expenditures will end the year within budgeted levels. In addition, the Fire Department's non-personal/equipment budget of \$10.5 million was 28.4% expended or encumbered through August 2019 and is expected to end the year within budgeted levels.

Overall, the average sworn vacancy rate of 3.65% through August 2019 is lower than the vacancy rate of 6.6% experienced this time last year, though vacancies have been above the budgeted rate of 2.5%. The first full Firefighter Recruit Academy for 2019-2020 began in June 2019 and will conclude on October 4, 2019, with 21 graduates.

In accordance with the City Council's approval of a March 2010 report on annual vacancy and absence rates, the Fire Department has committed to limiting administrative assignments for sworn administrative personnel for overtime control purposes. As of the end of August, of the 32 current authorized staffing level, the Fire Department had 32 sworn personnel on administrative assignments.

**GENERAL FUND (CONT'D.)**

**CONTINGENCY RESERVE**

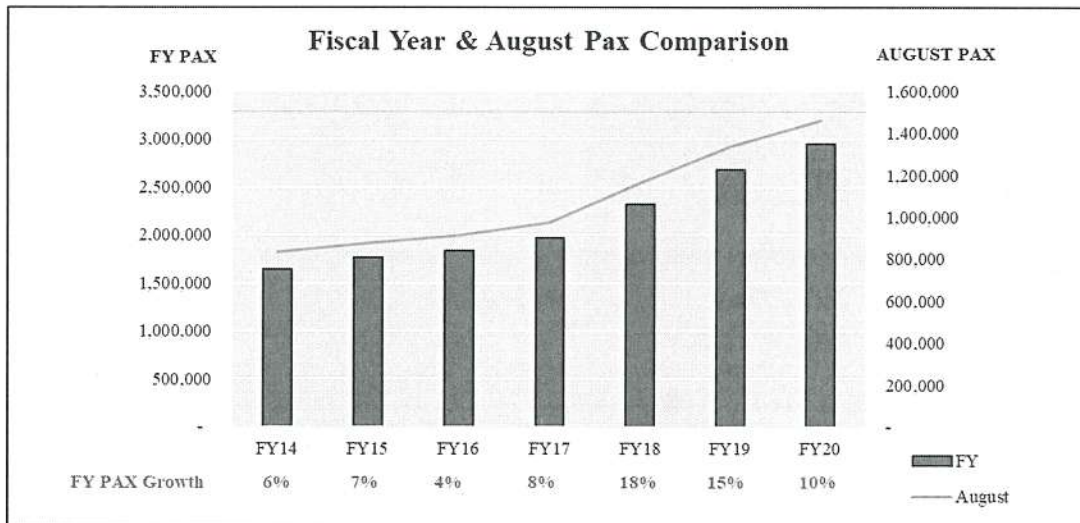
The General Fund Contingency Reserve remained at \$38.5 million through August, with no revisions through the first two months of the fiscal year. However, the 2018-2019 Annual Report, which was released on September 30, 2019 and will be brought forth for City Council consideration on October 22, 2019, includes a recommendation to increase the Contingency Reserve by \$1.5 million, to \$40.0 million. This reserve level complies with Council Policy 1-18, Operating Budget and Capital Improvement Program Policy, that requires the Contingency Reserve to be at a minimum of 3% of the operating budget.

**OTHER FUNDS**

**Airport Funds**

On a fiscal year-to-date basis, the Norman Y. Mineta San José International Airport (SJC) has enplaned and deplaned close to 3.0 million passengers, an increase of 10.0% from the figures reported through August of the prior year. International passengers have declined 24.7% year-to-date due to the discontinuation of service to Guadalajara and Mexico City by Aeromexico and to Frankfurt by Lufthansa. Domestic passengers increased 14.5%, boosted by the start of new service to Honolulu and Kahului by Southwest, Everett by Alaska, and Detroit by Delta. The chart below depicts the year-over-year change for the month of August and Fiscal Year-to-Date for the last seven years.

Fiscal year-to-date mail, freight and cargo totaled 18.1 million pounds, which represents a 10.1% decrease through August of the prior year. Revenue-generating activities posted increases over the same period of the prior fiscal year: Traffic Operations (landings and takeoffs) by 17.4%, Landed Weights by 7.5%, and Ground Transportation (taxicabs & TNC's) operations are 14.7% higher than the prior year. Parking exits are lower by 7.8% and gallons of aviation fuel sold decreased by 4.8%.





**OTHER FUNDS (CONT'D.)**

While year-to-date revenue primarily reflects just one month of receipts, it is currently expected that revenue will meet projections by year-end.

Through August, both the Airport Customer Facility and Transportation Fee Fund and Airport Maintenance and Operation Fund expenditures were tracking below budgeted levels. In the Maintenance and Operation Fund Personal Service expenditures were 13.6% of the budget (compared to the benchmark of 15.0%), while Non-Personal/Equipment expenditures were 6.0% of the budget (compared to the benchmark of 7.1%). Non-Personal/Equipment expenditures in the Customer Facility and Transportation Fee Fund were 7.5% of the budget compared to the straight-line benchmark of 16.7%.

The activity levels, revenues, and expenditure status of the Airport Funds will continue to be closely monitored throughout the fiscal year. In addition, the status of these funds will continue to be reported in each future Bi-Monthly Financial Report.

**Construction and Conveyance Tax Funds**

Through August 2019, Construction and Conveyance (C&C) Tax receipts totaled \$3.7 million, which represents 10.3% of the 2019-2020 Adopted Budget estimate (\$36.0 million). This amount is 23.7% below receipts through August 2018, which totaled \$4.8 million. In addition, the City has received the September Conveyance receipts from Santa Clara County, which total \$3.8 million, a 22.9% decrease from the September 2018 collection level. When taking into account total receipts through August and the estimated September collections, total C&C receipts in 2019-2020 total \$7.5 million, a 23.1% decline from the prior year collection level of \$9.8 million.

The 2019-2020 Adopted Capital Budget was built on the assumption that C&C Tax receipts in 2018-2019 would total \$42.0 million, then drop by almost 15% to \$36.0 million in 2019-2020. This drop was anticipated due to the slowdown in the local real estate market that began last year. However, since actual receipts in 2018-2019 totaled \$47.2 million, the 2019-2020 budget allows for a 23.7% decline in revenue. As mentioned above, through September C&C receipts have declined over 23% compared to the prior year. If this collection trend continues, receipts would end the year at the budgeted level of \$36 million. These economically sensitive taxes will continue to be closely monitored and updates will be provided in future Bi-Monthly Financial Reports.

Over 99% of the total Construction and Conveyance Taxes are comprised of conveyance receipts, a tax based on the value of property transfers (sales). As discussed in the Economic Environment section of this Bi-Monthly Financial Report, the local real estate market continues to experience declining single family median home prices coupled with declining sales activity. Since housing statistics are a key driver for the overall C&C collection levels, significant changes in the housing market will drastically affect the C&C Tax receipts. As mentioned, the slowdown in the market was anticipated and current year C&C receipts were budgeted accordingly. The local market will continue to be closely monitored, with updates provided in future Bi-Monthly Financial Reports.

**OTHER FUNDS (CONT'D.)****Other Construction-Related Revenues**

Revenues associated with construction activity are currently anticipated to meet or exceed their budgeted levels by year-end. As discussed below, the Construction Excise Tax and Building and Structure Construction Tax receipts through August are higher than prior year levels. Construction activities drive revenue collection in several categories, including the Construction Excise Tax and the Building and Structure Construction Tax that help fund the City's Traffic Capital Program, and are an indicator of future activity for several other categories, such as storm and sanitary sewer system fees.

Through August, the **Construction Excise Tax** collection level of \$4.0 million is 22.7% above the prior year receipts of \$3.3 million, primarily due to a high valuation level of commercial land use building permits. The year-to-date revenue represents 20.0% of the 2019-2020 Adopted Budget estimate of \$20.0 million. When the 2019-2020 Adopted Capital Budget was developed it was anticipated 2018-2019 Construction Excise Tax receipts would total \$21.0 million, then decrease by approximately 5% to \$20.0 million in 2019-2020. However, since 2018-2019 receipts ended the year at \$25.8 million, the 2019-2020 budget allows for a 22.4% decline from the prior year collection level. While this tax is extremely volatile, it is currently anticipated receipts will meet or exceed budgeted levels by year-end. This tax will continue to be closely monitored, and if necessary, budget adjustments may be brought forward at a future date to align revenues with anticipated collection levels.

Through August, the **Building and Structure Construction Tax** collection level of \$7.5 million is 154.0% above the prior year receipts of \$3.0 million, primarily due to both a high valuation level of commercial and industrial land use building permits. This revenue level represents 50.2% of the 2019-2020 Adopted Budget estimate of \$15.0 million. When the 2019-2020 Adopted Capital Budget was developed it was anticipated 2018-2019 Building and Structure Construction Tax receipts would total \$16.0 million, then decrease by approximately 6% to \$15.0 million in 2019-2020. However, since 2018-2019 receipts ended the year at \$22.5 million, the 2019-2020 budget allows for a 33.4% decline from the prior year collection level. While this tax is extremely volatile, it is currently anticipated receipts will meet or exceed budgeted levels by year-end. This tax will continue to be closely monitored, and if necessary, budget adjustments may be brought forward at a future date to align revenues with anticipated collection levels.



**CONCLUSION**

Overall, the City's funds appear to be performing within budgeted expectations through August. The City ended the 2018-2019 fiscal year in solid position as the starting point for 2019-2020. Although economic conditions remain positive, indicators are continuing to moderate from the strong levels experienced in recent years. This overall "sluggish" economic growth was anticipated and the corresponding revenues have been budgeted in 2019-2020 accordingly. More information about the state of the current local economy and anticipated revenue collection will be available for the Bi-Monthly Financial Report for September/October, which will be reviewed by the Public Safety, Finance, and Strategic Support Committee at its meeting on December 12, 2019. The Administration will continue to closely monitor economic conditions and the performance in all City funds, bringing forward budget adjustments to the City Council during the year as appropriate.

As always, staff will continue to report to the City Council significant developments through this and other budget reporting processes.



JIM SHANNON  
Budget Director