COUNCIL AGENDA: 12/5/2017
ITEM: 3.5 (17-393)

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Toni J. Taber, CMC
City Clerk

SUBJECT: **SEE BELOW**

DATE: November 22, 2017

SUBJECT: FIRST QUARTER FINANCIAL REPORTS FOR FISCAL YEAR 2017-2018

RECOMMENDATION: As recommended by the Public Safety, Finance and Strategic Support Committee on November 16, 2017, accept the following First Quarter (period ending September 30, 2017) Financial Reports for Fiscal Year 2016-2017 for the following programs:

(a) Debt Management Report.
(b) Investment Management Report.
(c) Revenue Collection Report.

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: PUBLIC SAFETY, FINANCE, AND STRATEGIC SUPPORT COMMITTEE

FROM: Julia H. Cooper

SUBJECT: **FIRST QUARTER FINANCIAL REPORTS FOR FISCAL YEAR 2017-2018**

DATE: October 31, 2017

Approved [signature] Date 11-8-17

RECOMMENDATION

(1) Accept the following First Quarter (period ending September 30, 2017) Financial Reports for Fiscal Year 2017-2018:
   (a) Debt Management Report
   (b) Investment Management Report
   (c) Revenue Collection Report; and

(2) Refer the First Quarter Financial Reports for Fiscal Year 2017-2018 to the December 5, 2017, City Council meeting for full adoption.

OUTCOME

Provide the quarterly update on debt management, investment management, and revenue collection work efforts.

BACKGROUND

The attached First Quarter Financial Reports for Fiscal Year 2017-2018 presents the Finance Department's quarterly activity for the City's Debt Management, Investment Management, and Revenue Collection programs (Attachment A). Additionally, the First Quarter Investment Report has been distributed to the City Council via email and is available on the Finance Department web page at http://www.sanjoseca.gov/index.aspx?NID=759. As part of the ongoing effort to streamline work efforts within the Finance Department, these three reports are combined in one single report for submission to the Public Safety, Finance, and Strategic Support Committee (the "PSFSS Committee") for its review and acceptance. A brief narrative discussion is provided below for all three components of this quarterly report.

ANALYSIS

This section of the report is divided into the following sections: Debt Management Program, Investment Management Program, and Revenue Collection Program which includes Marijuana Business Tax.

Debt Management Program

This First Quarter Debt Report focuses on the City's debt activities for the period ended September 30, 2017, and relates to the following elements of the City's Debt Management Program:

- Completed financings and current debt portfolio
- Debt issuance and management activities completed and anticipated to fiscal year end
- Current interest rate environments and credit ratings

The City's current general obligation bonds are rated Aa1/AA+/AA+ and lease revenue bonds are rated Aa2-Aa3[1]/AA/AA by the Moody's Investors Services Inc., Standard & Poor's Ratings Services, and Fitch Ratings, respectively. These ratings are based on the rating reviews through September 30, 2017.

Investment Management Program

A quarterly investment report for the period ended September 30, 2017, was distributed separately to the Mayor and City Council and is posted on the Finance Department website[2]. Pursuant to the City's Investment Policy, verbal presentations in addition to the written reports are provided to the PSFSS Committee for the Second and Fourth Quarter Reports. The materials that are presented in this consolidated report provide a "snapshot" of the investment portfolio. The report will be agendized for acceptance by the City Council pursuant to the Investment Policy.

Revenue Collection Program

The Revenue Collection report highlights the key aspects of the City's ongoing collection efforts. These efforts focus on reducing delinquent accounts receivable and enhanced revenue compliance in three primary collection programs: Business Tax, Accounts Receivable, and Revenue Compliance and Monitoring. This report provides the highlights of the Revenue Management Division's collection efforts and summarizes the progress towards meeting the annual collection target of $7.5 million. Actual collections through the first quarter of fiscal year 2017-18 are approximately $3.5 million which represents 46.4% of the annual collection target.

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[1] Moody's determines its lease revenue bond ratings in part based on "essentiality" of leased asset; bonds tied to an essential asset, like City Hall carries higher rating (Aa2) than bonds tied to a less essential asset such as Convention Center (Aa3)

[2] http://www.sanjoseca.gov/index.aspx?NID=759

Additionally, specific information is provided on Marijuana Business Tax collection and compliance efforts as well as the Business Tax changes that went into effect July 1, 2017.

Marijuana Business Tax ("MBT")

MBT Revenue Collection – The MBT revenue collected this fiscal year through September 2017 is approximately $1.97 million. This is 15.76% higher than the revenues collected through the same period in the prior fiscal year that totaled $1.7 million.

MBT Compliance – There are a total of 16 registered collectives in the City's Medical Marijuana regulatory program. All 16 are remitting MBT timely and are compliant with the MBT ordinance. As of September 30, 2017, there are seven non-registered MBT accounts which are delinquent and require further staff collection efforts. The summary of staff collection efforts related to the seven delinquent accounts are as follows:

- Six of the non-compliant store fronts have been closed through Code Enforcement action but one remains open.
- Four are actively being pursued by City staff for collection of taxes owed. One account remains with the City Attorney's Office for legal action. One account is currently in the settlement process with the City Attorney's Office. One newly identified non-registered store front has been contacted for audit and is currently being reviewed by Code Enforcement and the Police Department's marijuana regulatory office.

Business Tax Code Changes effective July 1, 2017

The City's Business Tax was first adopted on July 15, 1963. The methodology used for calculating the City's former Business Tax was adopted in 1984. The Business Tax Modernization Measure (Measure G) was approved by a majority of San José voters on November 8, 2016, went into effect July 1, 2017, and represents the first increase since 1986.

The voter-approved Business Tax Modernization changes require outreach to the business community through a variety of mediums. Staff from the Finance Department, Office of Economic Development, and City Manager's Office have provided various outreach efforts which are ongoing. Information regarding the changes to the tax will be found on the Finance Department's landing page (http://www.sanjoseca.gov/index.aspx?nid=5378). Specific examples of our ongoing outreach efforts are as follows:

- An advertisement was placed on the Silicon Valley Organization's website on October 5, 2017 to run through the end of November 2017 and can be viewed here: https://www.thesvo.com/about-commerce/.
- Additional advertisements will take place throughout October and November 2017 with KRTY/KLIV (Radio Stations), San Jose Mercury News, Metro Silicon Valley, and VTA buses.

- The Finance Department has commenced a letter campaign targeting residential landlords that are now required to register and remit the Business Tax with 8,400 letters mailed to date.

As of July 1, 2017 taxpayers can access an online payment portal to pay Business Tax and businesses can register online for Business Tax accounts at the Finance Department's website. Through September 30, 2017 a total of 1,695 new Business Tax account registrations were processed for a total billed amount of $357,567 as a result of the new online registration process. Of the 1,695 new accounts, 912 were Business Tax account registrations of residential landlords that contributed $181,760 to the above referenced billed amount.

EVALUATION AND FOLLOW-UP

The Finance Department prepares this report on a quarterly basis for review and approval by the PSFSS Committee. Finance Department staff will be available to answer questions on the First Quarter Financial Reports for Fiscal Year 2017-2018 at the PSFSS Committee meeting on November 16, 2017.

PUBLIC OUTREACH/INTEREST

This memorandum will be posted on the City's website for the November 16, 2017, PSFSS Committee meeting and the December 5, 2017, City Council meeting.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office and City Manager's Budget Office.

JULIA H. COOPER
Director of Finance

For questions, please contact Lisa Taitano, Assistant Director of Finance, at (408) 535-7041.

Attachment A: First Quarter Financial Reports for Fiscal Year 2017-2018

First Quarter Financial Report for Fiscal Year 2017-2018

Public Safety, Finance and Strategic Support Committee

Prepared by the Finance Department November 16, 2017

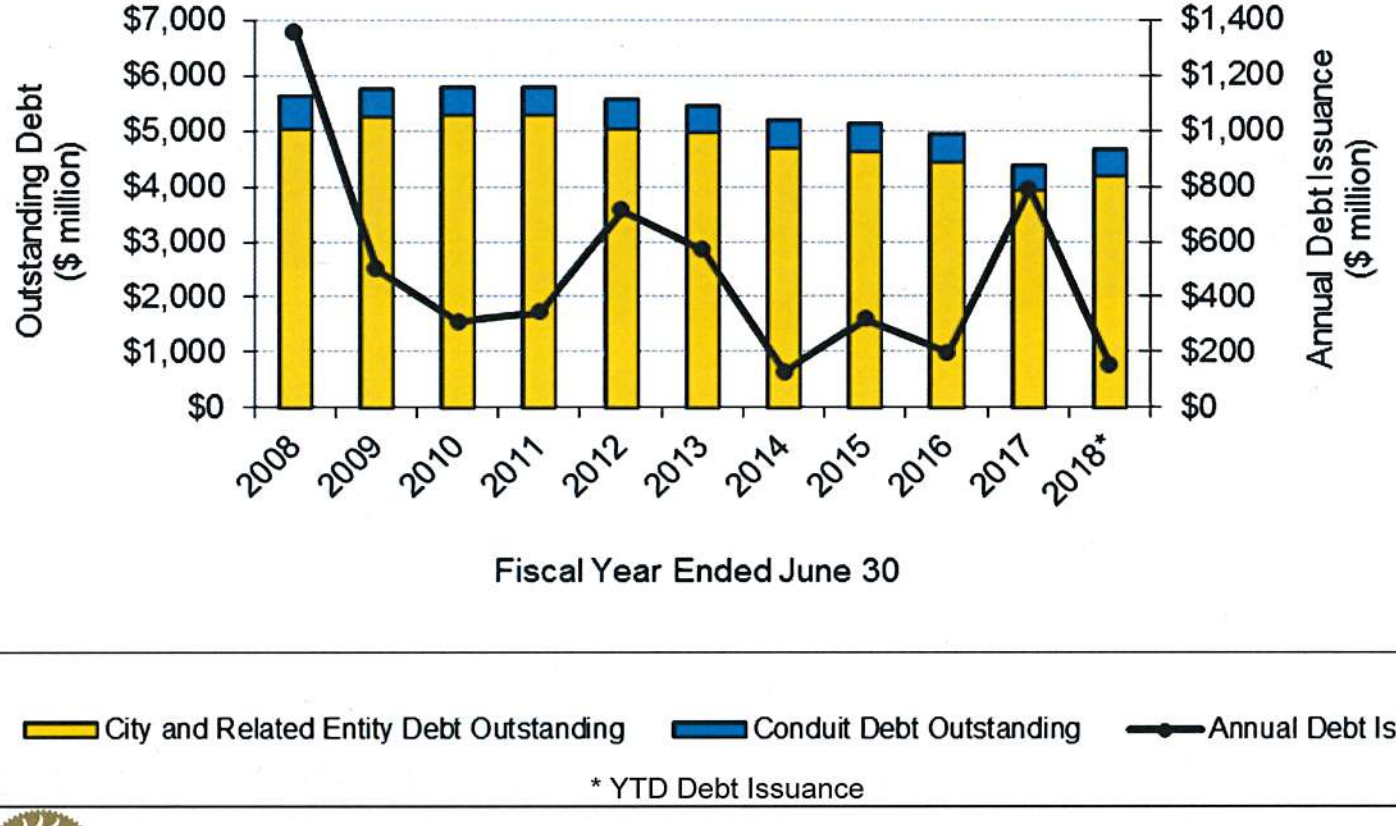
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First Quarter
Debt Management Report
for Fiscal Year 2017-2018

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Outstanding Debt Issued by All Agencies

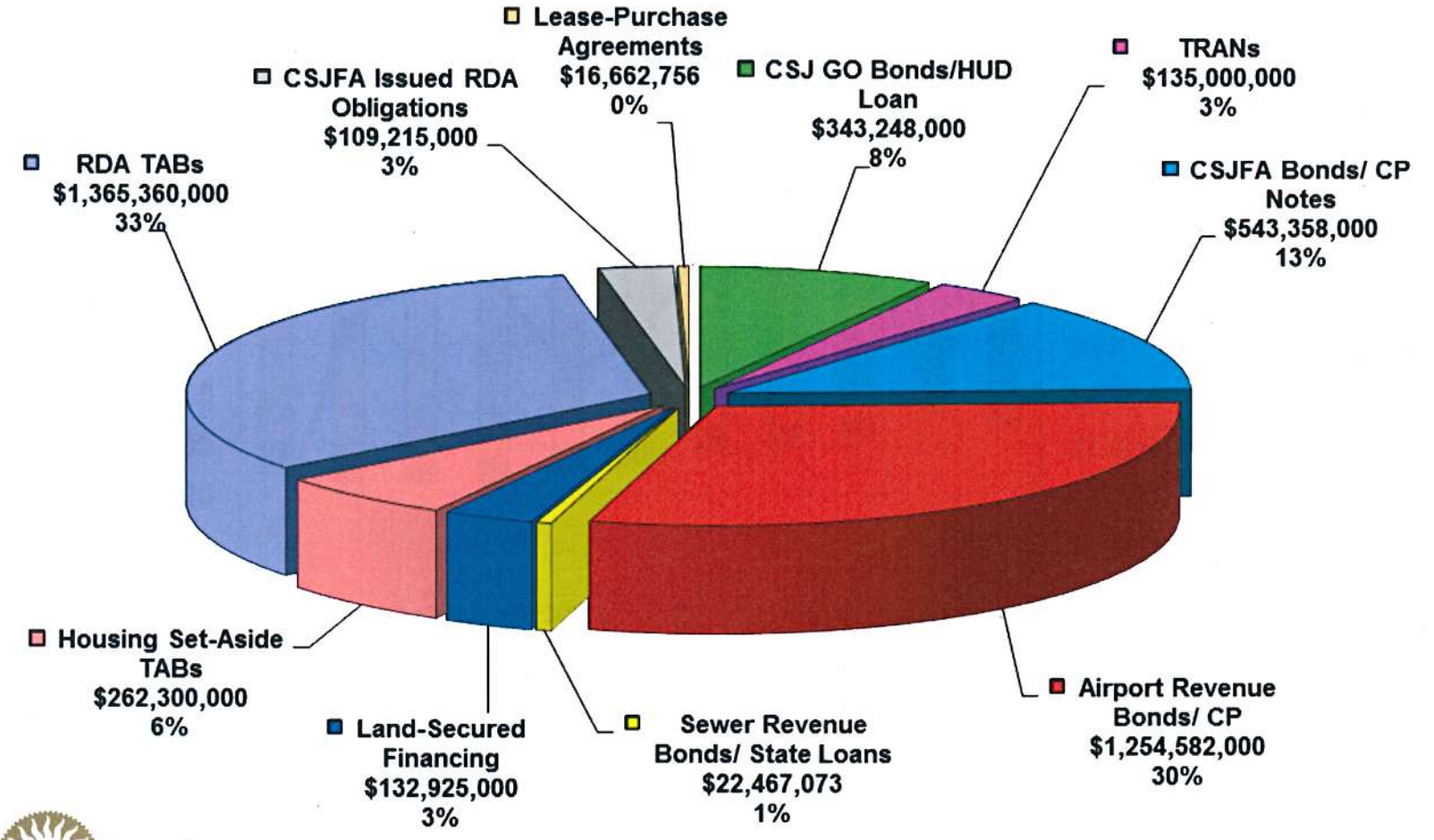
Outstanding Debt as of September 30, 2017: $4.6 Billion
FY 2017-18 Actual Debt Issuance: $150 Million



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Outstanding Debt Issued by All Agencies Excluding Multifamily Housing Revenue Bonds

Outstanding Debt as of September 30, 2017: $4,185,117,829*



* Excludes conduit debt, pension, OPEB, and other long-term liabilities of the City.

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Selected Debt Issuance and Debt Management Activities during 1st Quarter

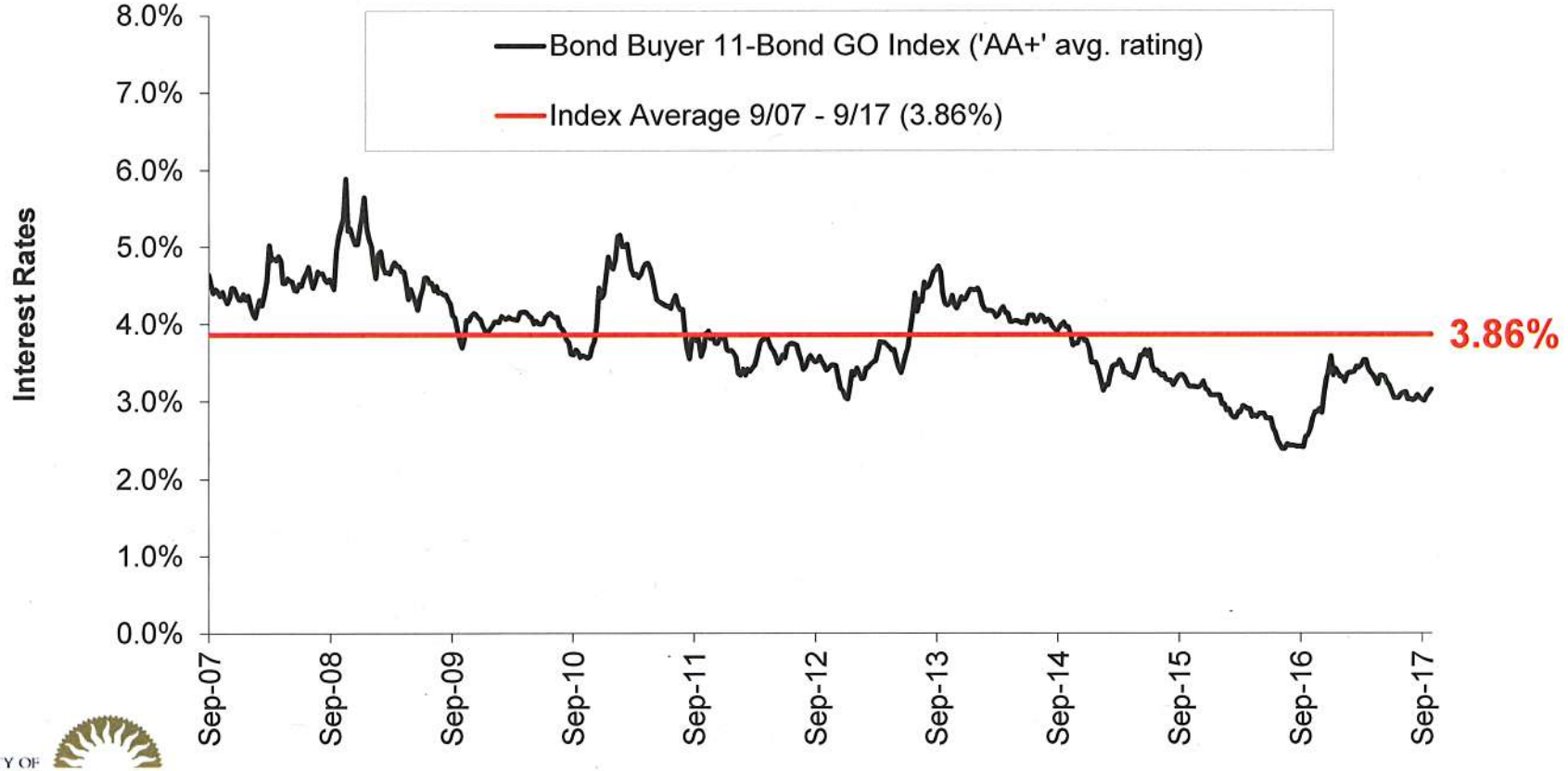
- Debt Issuance
  - ➢ $150 million Tax and Revenue Anticipation Note (2017 TRAN issued July 3, 2017)
  - ➢ Pre-issuance activities
    - Refinancing of Successor Agency of the Redevelopment Agency (SARA) debt
    - Short-term financing for Regional Wastewater Facility Capital Improvement Program
- Debt Management
  - ➢ Selection and Execution of Municipal Advisors contracts for General City, Airport, Multifamily, Wastewater Facilities, SARA and Land-Secured

Upcoming Debt Issuance and Management Through December 31, 2017

- Debt Issuance
  - ➢ $1.8 billion SARA RDA debt refinancing, issue date – December 2017
  - ➢ Multi-Family Housing Revenue Notes
    - Catalonia Apartments - $16.2 million, issued October 17, 2017
  - ➢ $300 million in Subordinate Wastewater Net System Revenue Notes to finance capital improvements at the San Jose-Santa Clara Regional Wastewater Facility (October 2017)
  - ➢ CSJFA lease revenue commercial paper notes for various projects include: San José Clean Energy startup costs ($10 million authorized); Convention Center exhibit hall ($15 million authorized); Energy Conservation equipment ($1,768,000 remaining authorization)
  - ➢ Pre-issuance
    - General Obligation and CSJFA lease revenue bond refinancings
- Debt Management
  - ➢ 2017 Comprehensive Annual Debt Report (CADR)
  - ➢ Annual Continuing Disclosure/Compliance Reporting

Ten-Year Tax-Exempt Market Index (Fixed Rate)

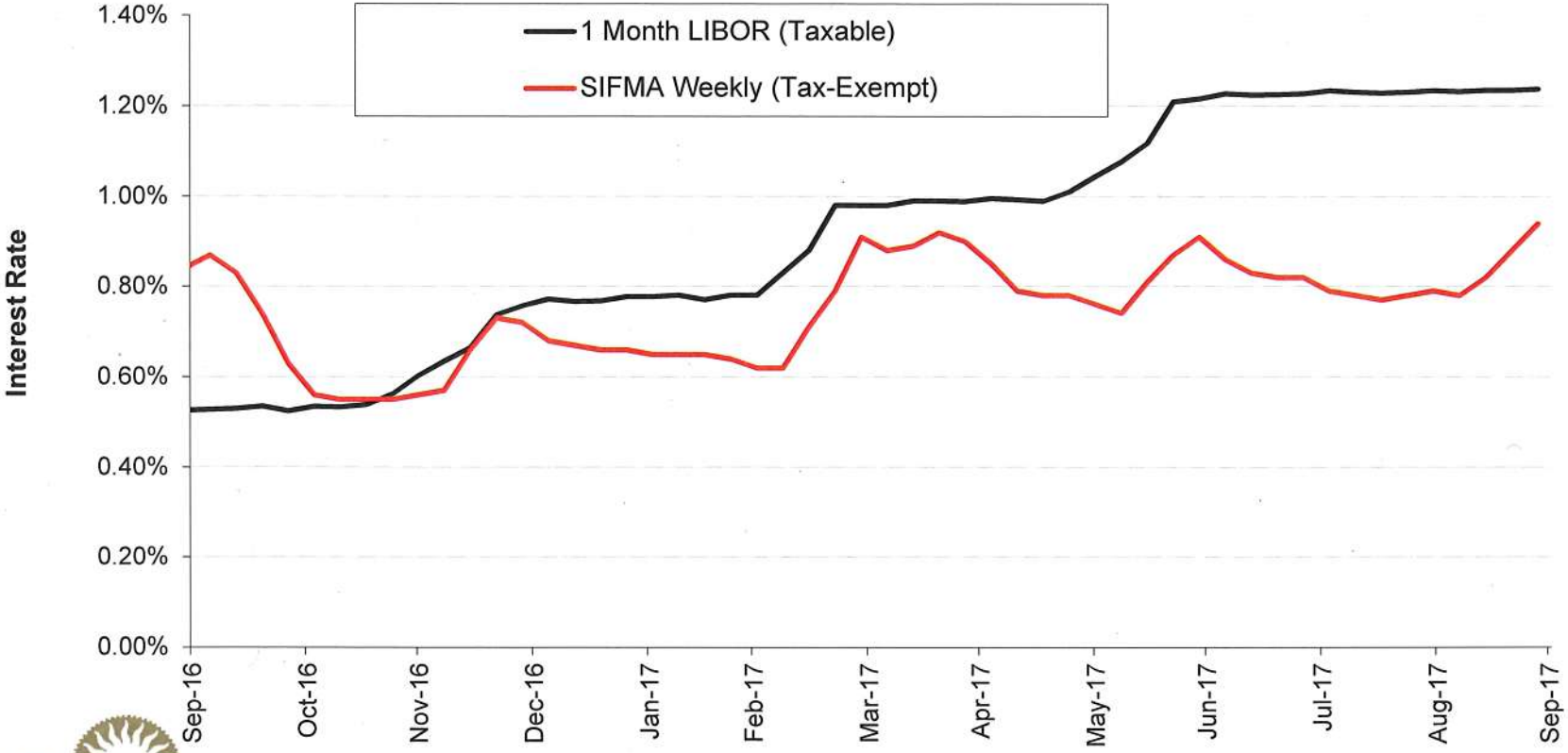
- 10-year historic tax-exempt long-term interest rates averaged around 3.86% and are currently at 3.16% (as of 10/26/17)



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Variable Taxable and Tax-Exempt Interest Rates

- Tax-Exempt SIFMA weekly interest rates paid by the City averaged 0.82% in Q1 and are currently at 0.92% (as of 10/25/2017)
- Taxable LIBOR monthly interest rates paid by the City averaged 1.23% in Q1 and are currently at 1.24% (as of 10/26/2017)



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City of San José – Credit Ratings[1]

- City continues to maintain high general obligation (G.O.) credit ratings of Aa1/AA+/AA+ and lease revenue bond ratings of Aa2-Aa3[2]/AA/AA
  - City G.O. bonds continue to be rated higher than State of California (Aa3/AA-/AA-)
  - Santa Clara County G.O. bonds are rated lower by Moody's (Aa2), higher by S&P (AAA), and the same by Fitch
- SJC Airport bonds are rated A2/A-/A-
- RDA non-Housing Tax Allocation Bonds are rated A2/AA-/A+
- RDA Housing Set-Aside Tax Allocation Bonds are rated A1/A/AA

[1] Ratings are listed in the following order by rating agency (unless noted otherwise): Moody's/S&P/Fitch.

[2] Moody's determines its lease revenue bond ratings, in part, based on "essentiality" of leased asset; bonds tied to an essential asset like City Hall carry a higher rating (Aa2) than bonds tied to a less essential asset like the Convention Center (Aa3).

First Quarter
Investment Management Report
for Fiscal Year 2017-2018

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Investment Policy (Council Policy 1-12)

- Conforms to the California Government Code Sections 53600 et seq.
- Authorized investments only include high grade fixed income securities. (Long-term rating A or higher; Short-term rating A1/P1/F1)
- Policy is reviewed annually and shall be adopted by resolution of the City Council
- Investment Program is audited semiannually for compliance purposes

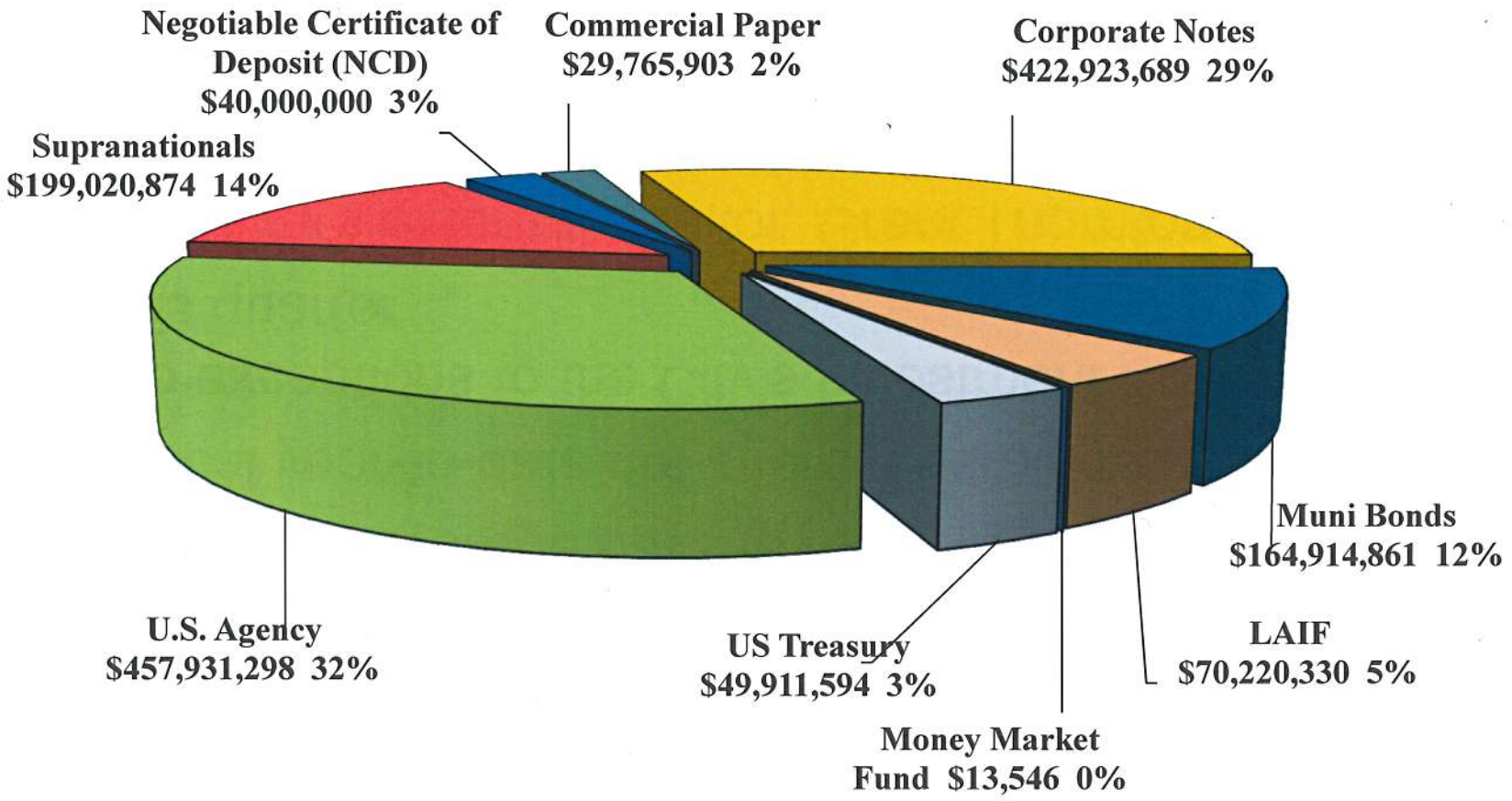
Investment Objectives & Reporting

- Manage investments to meet the City's objectives:
  - Safety
  - Liquidity
  - Yield
- Quarterly reports on-line and placed on PSF&SS Committee agenda

Summary of Portfolio Performance

- Size of total portfolio: $1,434,702,095
- Earned interest yield: 1.349%
- Weighted average days to maturity: 590 days
- Fiscal year-to-date net interest earnings: $5,150,061
- No exceptions to the City's Investment Policy during this quarter
- The City's external auditor, Grant Thornton LLP, evaluated the City's investment program for the year ended June 30, 2017. The report noted no exceptions.

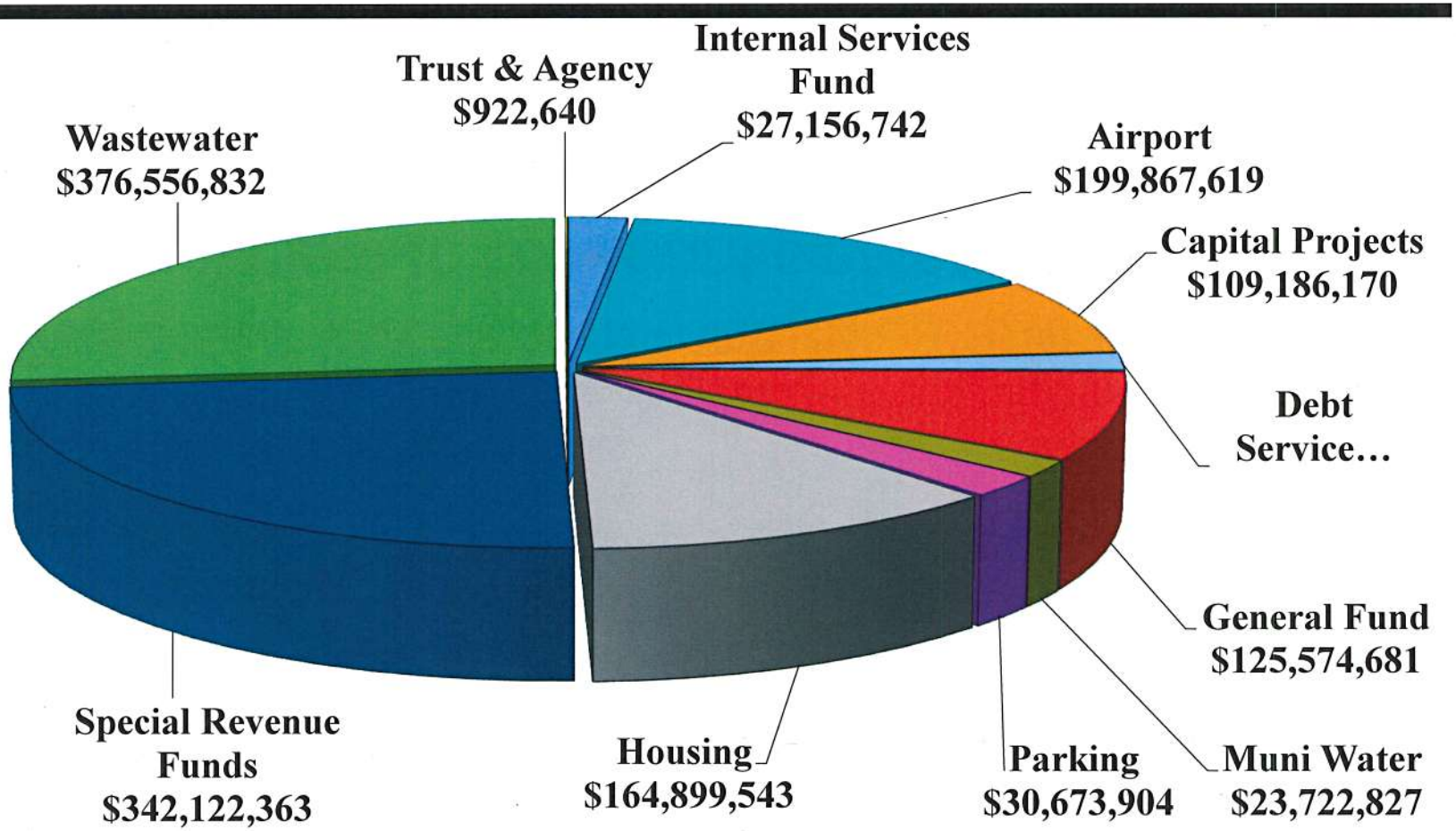
Portfolio Investment



Total Investment Portfolio = $1,434,702,095

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Investment by Fund



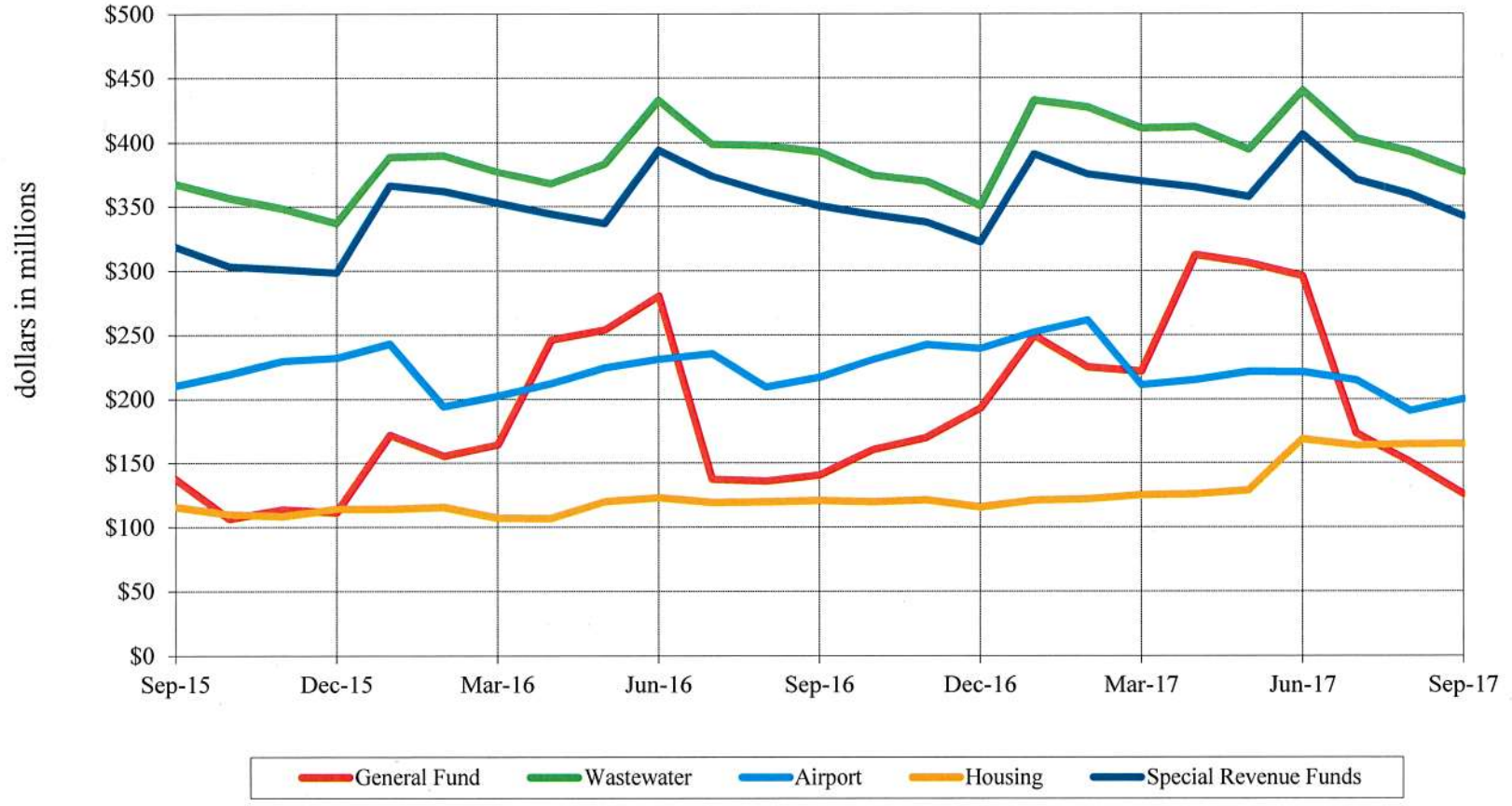
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General Fund Balances

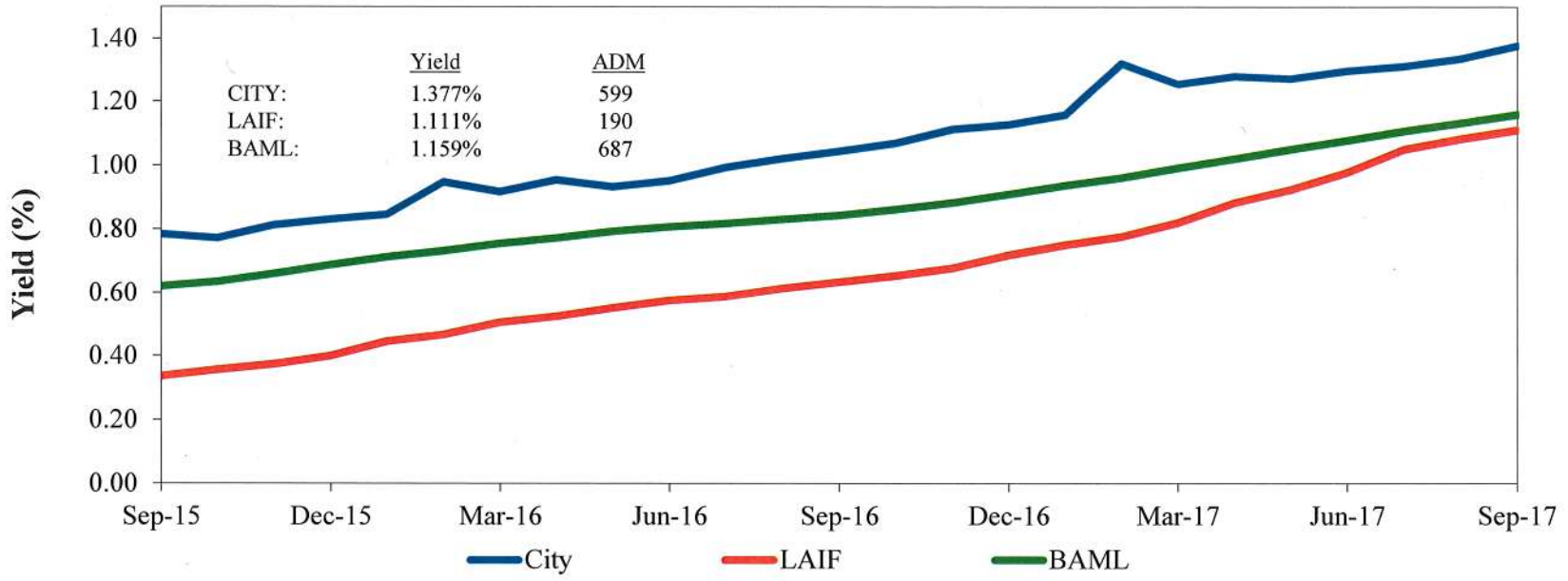
- General Fund balances decreased by approximated $170.1 million to $125.6 million this quarter, primarily due to retirement prefunding

- Projected investment maturities and revenue are sufficient to cover anticipated expenditures for the next six months

Comparison of Cash Balances by Select Funds



Benchmark Comparisons



Notes:

1. City refers to City's Fund 1 Portfolio, and the yield data are month end weighted average yields.
2. LAIF refers to the State of CA Local Agency Investment Fund and yield data are average monthly effective yields.
3. BAML refers to Bank of America Merrill Lynch 1-3 Year AAA-A US Corporate & Government Index and yield data are rolling 2-year effective yield

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Investment Strategy

- Continue matching investment maturities with known expenditures within the 24-month horizon
- Extend a portion of the portfolio beyond two-year term, when appropriate, to provide income and structure to the portfolio
- Maintain the diversification of the portfolio
- Focus on core mandate of safety, liquidity, and yield

First Quarter
Revenue Collection Report
for Fiscal Year 2017-2018

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Revenue Collection Program

- Finance Department revenue collection efforts focus on reducing delinquent accounts receivable and enhancing revenue compliance in three primary collection programs:
  - Business Tax
  - Accounts Receivable
  - Revenue Compliance and Monitoring
- Efforts may span several reporting periods, and actual collections are reported when funds are received by the City
- Revenue and compliance activities related to Marijuana Business Tax are reported separately

Revenue Collection Results – Quarter to Quarter Comparison

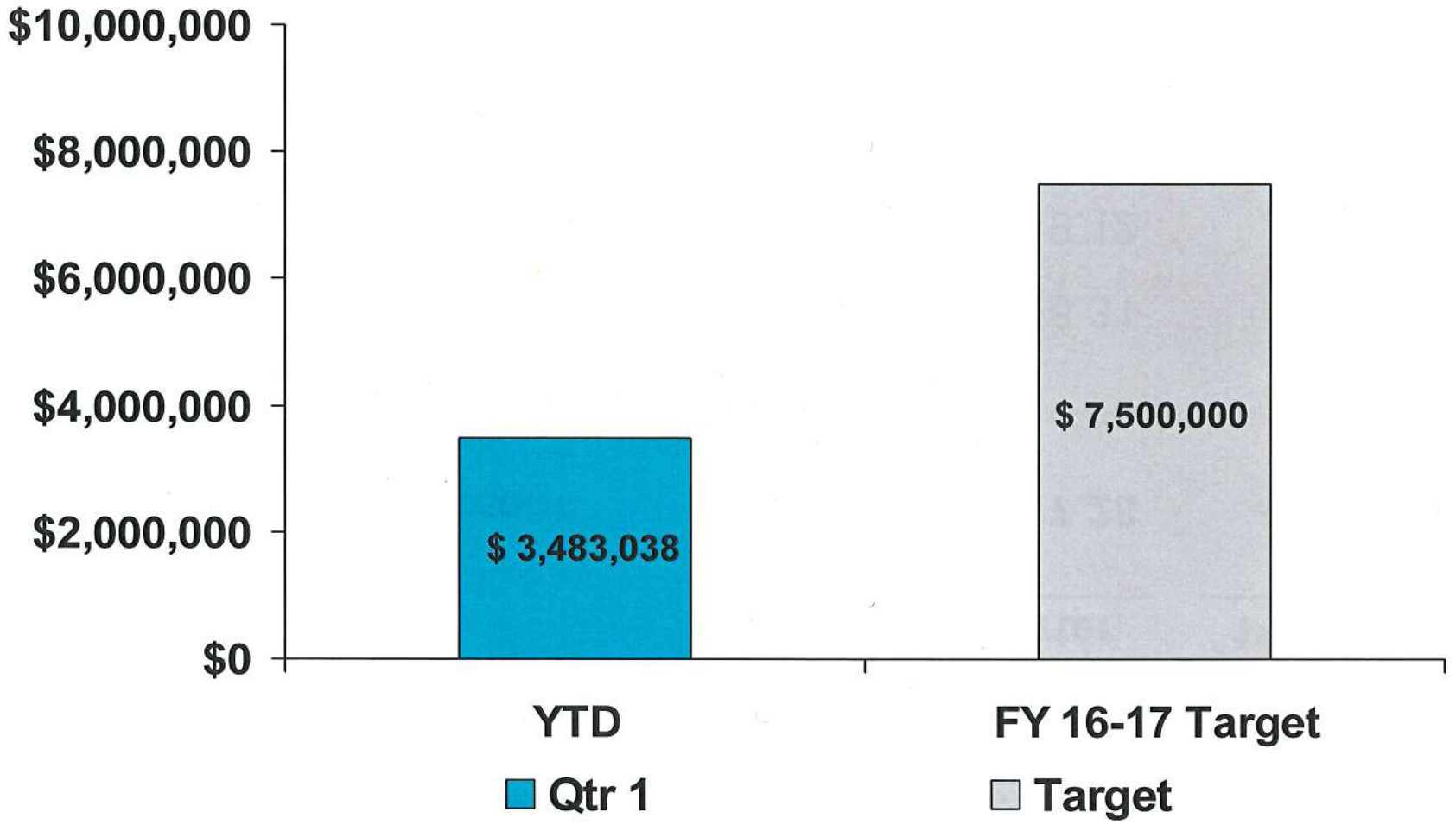
Collection Programs	FY 2017-18 1st Quarter	FY 2016-17 1st Quarter
Business Tax	$ 870,933	$ 746,699
Accounts Receivable	1,633,257	978,792
Revenue Compliance/Monitoring	978,848	389,597
Total Program Collections	**$ 3,483,038**	**$ 2,115,088**

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Return on Investment (ROI)
Quarter to Quarter Comparison

	FY 2017-18 1st Quarter	FY 2016-17 1st Quarter
Total Return on Investment	**7.28**	**5.36**
Return on Investment by Program		
Business Tax Delinquencies	6.31	5.31
Accounts Receivable Delinquencies	9.12	7.45
Revenue Compliance/Monitoring	6.08	3.17

FY 2017-18 YTD Revenue Collection Results: 46.4% of Annual Target



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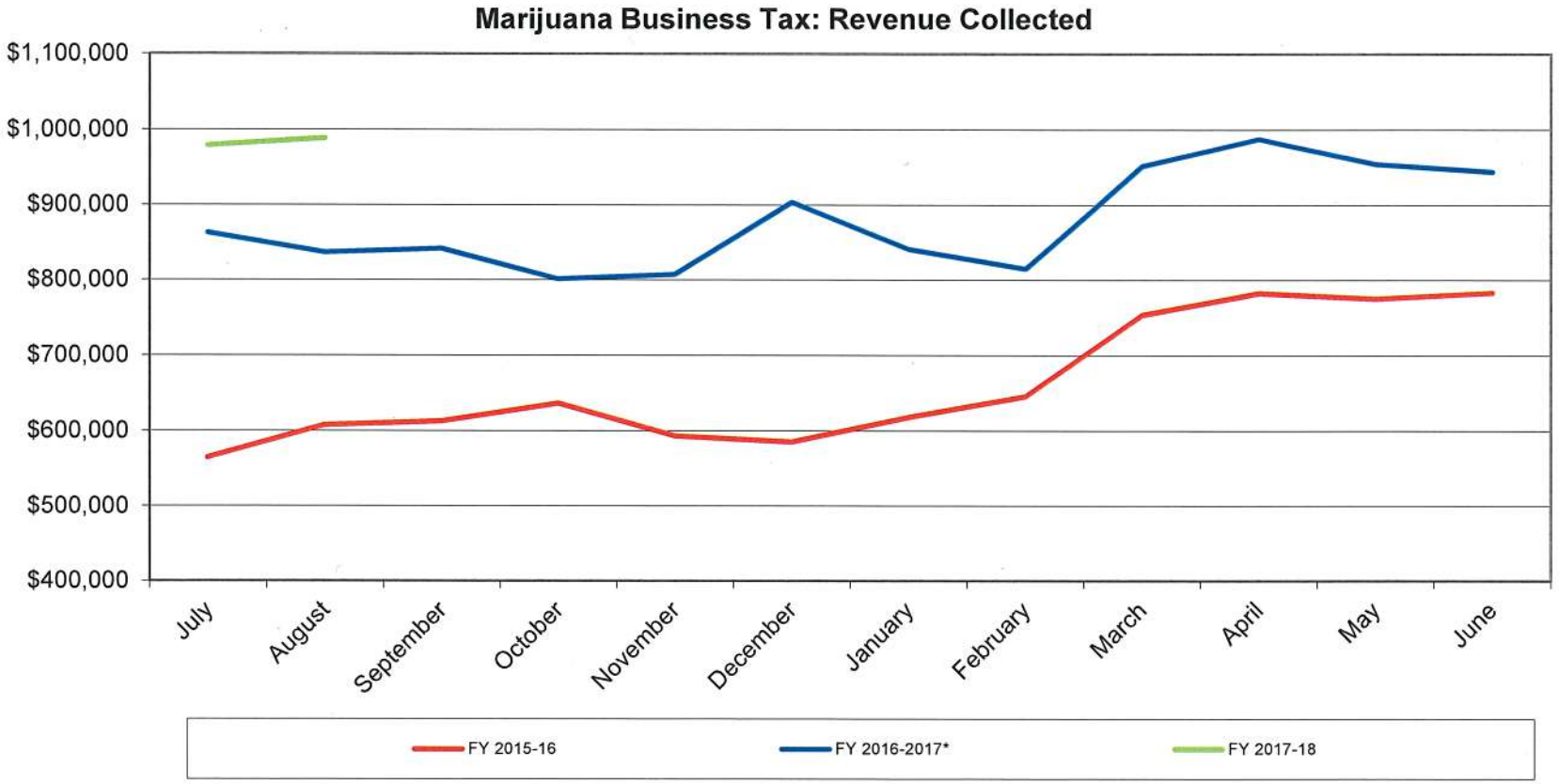
Accounts Receivable Balance

	As of Sept. 30, 2017	As of Sept. 30, 2016
Current Receivables		
0-60 Days	$ 4,964,532	$ 2,687,916
61-90 Days	1,269,193	8,837,713
Total Current Receivables	$ 6,233,725	$ 11,525,629
Delinquent Receivables		
91-365 Days	$ 5,245,425	$ 10,012,945
Over 1 Year	18,405,114	16,441,544
Total Delinquent Receivables	$ 23,650,539	$ 26,454,489
Total Accounts Receivable	**$ 29,884,264**	**$ 37,980,119**

- Delinquent Receivables include $5.0M in reserved MBT assessments under litigation/collections
- 77% of the receivable balance ending September 30, 2017 is General Fund
- 68% of the receivable balance ending September 30, 2016 is General Fund

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Marijuana Business Tax (MBT) Revenues



- Revenue in FY 17-18 has increased over FY 16-17 revenue as the collectives that remain open are taking in customers from non-tax remitting dispensaries that were closed due to Code Enforcement actions.

* Cash collected July through August 2017

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Billing System Online Functionality

Revenue Management is currently upgrading/implementing two new billing systems

	Take Payments & Provide Receipt	Update Contact Information	Accept New Account Applications
Business Tax System Implementation to be complete Spring 2018	★	★	★
Revenue Results Implemented October 2017	★	n/a	n/a

- Revenue Results is a delinquent invoice/tax collection system, not a registration/billing system.
- Beginning July 1, 2017 taxpayers can access an online payment portal on the Finance Department's website to pay the Business Tax.

Business Tax Code Change Outreach Efforts

- Changes effective July 1, 2017
- Advertisements to the public were placed with:
  - Silicon Valley Organization
  - KRTY & KLIV (Radio Stations)
  - San Jose Mercury News
  - Metro Silicon Valley
  - Valley Transit Authority (VTA)
- The Finance Department has mailed out approximately 8,400 letters to residential landlords now required to register and remit the Business Tax