



Memorandum

TO: PUBLIC SAFETY, FINANCE, AND
STRATEGIC SUPPORT COMMITTEE

FROM: Margaret McCahan

SUBJECT: BI-MONTHLY FINANCIAL REPORT
FOR JULY/AUGUST 2018

DATE: October 4, 2018

Approved

Date

10-4-18

RECOMMENDATION

Accept the Bi-Monthly Financial Report on actual revenues and expenditures as compared to the 2018-2019 Budget for the two months ending August 2018.

OVERVIEW

The Bi-Monthly Financial Report for July/August 2018 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 2018-2019 Modified Budget and the Finance Department has prepared a report that reflects the financial results for the two months ending August 2018.

Through the first two months of the fiscal year, revenues and expenditures were generally tracking within the budgeted estimates in the majority of the 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 if necessary. Following are key highlights in this report:

- While it is very early in the fiscal year, and there is minimal data, overall revenues appear to be tracking within estimated levels in the General Fund.
- Expenditures tracked slightly above 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. These revenues are all anticipated to meet or exceed the budgeted estimate by year-end

OVERVIEW (CONT'D.)

- Development-related revenues in the General Fund through August 2018 have generally grown from the same time period in the prior fiscal year. Revenues are anticipated to meet budgeted levels by year end, with the exception of Planning Fees that have grown, but are still performing lower than anticipated.
- The Norman Y. Mineta San José International Airport (SJC) has enplaned and deplaned 2.7 million passengers through August, an increase of 15.4% from the figures reported through August of the prior year. This follows extremely strong growth experienced over the last two years. In 2016-2017, annual passenger growth increased by 12.7% (8% growth experienced through August of that fiscal year), and annual passenger growth increased by 17.2% in 2017-2018 (18% growth experienced through August of that fiscal year).
- In Silicon Valley, general economic conditions remain positive, but some of the economic indicators are starting to moderate from the strong levels experienced in recent years. The Administration will closely monitor the City's economically sensitive revenues to 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

Silicon Valley continues to show positive economic performance. The August 2018 employment level in the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (San José MSA) of 1.09 million was approximately 1% above the August 2017 level of 1.08 million.



Between August 2017 and August 2018, employment in the San José MSA expanded by 33,500 jobs. This growth includes an increase of 10,900 jobs in the educational and health services industry, 6,600 job in the manufacturing sector, 6,000 jobs in the professional and business services industry, and 5,300 jobs in the information sector.¹

¹ State of California Employment Development: Labor Market Information Division Press Release, September 21, 2018

OVERVIEW (CONT'D.)

Unemployment Rate (Unadjusted)			
	August 2017	July 2018	August 2018**
San Jose Metropolitan Statistical Area*	3.5%	2.8%	2.7%
State of California	4.9%	4.4%	4.3%
United States	4.5%	4.1%	3.9%
<small>* San Benito and Santa Clara Counties Source: California Employment Development Department. ** August 2018 estimates are preliminary and may be updated.</small>			

The unemployment rates at the local, State, and national levels have continued to slightly drop compared to the prior year. In August 2018, the unemployment rate for the San José Metropolitan Statistical Area of 2.7% is below the July 2018 unemployment rate of 2.8% and the August 2017 rate of 3.5%. In this region, the August 2018 unemployment rate continues to be lower than the unadjusted unemployment rate for the State (4.3%) and the nation (3.9%).

Overall construction activity through August 2018 has decreased 3.4% from 2017-2018 levels. The 2018-2019 budget was developed with the expectation that private development activity would remain strong but would drop from the overall high levels experienced in 2017-2018.

Through August, overall residential permit valuation decreased from prior year levels. The number of residential units (296 new dwelling units in 2018-2019 vs. 253 in 2017-2018) was up, while the valuation was lower than prior year levels (\$72.6 million in 2018-2019 vs. \$88.0 million in 2017-2018). Valuation for alteration activity stayed level with the prior year (\$20.4 million in 2018-2019 vs. \$20.3 million in 2017-2018). The 296 residential units through August 2018 included 212 multi-family units and 84 single-family units. A significant residential project for August included a permit issued for the construction of a new 200 unit assisted living facility at the intersection of Almaden Expressway and Branham Lane.

Commercial valuation through August 2018 is lower than the 2017-2018 level (\$60.9 million in 2018-2019 vs \$90.1 million in 2017-2018). New commercial construction activity has decreased while alteration activity is slightly up compared to the prior year levels. Notable projects for July and August include a construction permit for a new Chick-Fil-A restaurant on Blossom Hill Road (west of the Almaden Expressway intersection) and foundation only permits for construction of a six story (194,205 square foot) office building and a five story (164,389 square foot) building located on Coleman Avenue, west of the San Jose Airport.

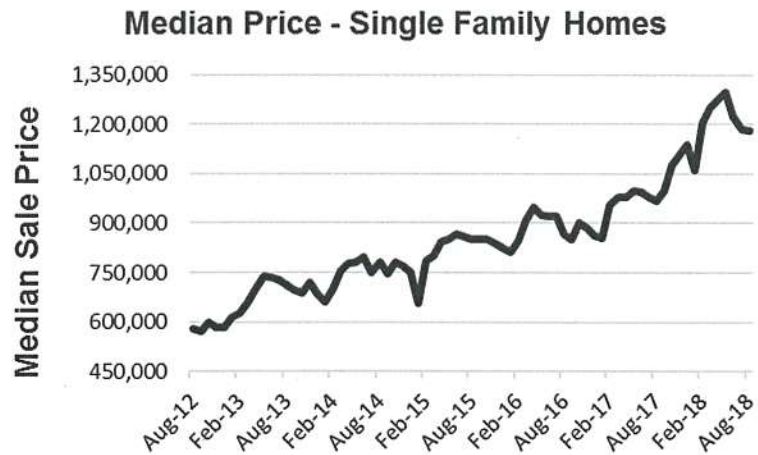
Private Sector Construction Activity (Valuation in \$ Millions)			
	YTD August 2017	YTD August 2018	% Increase
Residential	\$ 88.0	\$ 72.6	(17.6%)
Commercial	\$ 90.1	\$ 60.9	(32.5%)
Industrial	\$ 58.0	\$ 94.8	63.5%
TOTAL	\$ 236.1	\$ 228.3	(3.4%)

Industrial construction valuation through August 2018 is higher than prior year levels (\$94.8 million in 2018-2019 vs. \$58.0 million in 2017-2018). Both new industrial construction and alteration activity is higher compared to the prior year. A notable project for August included a permit issued for finished interior of a six story (215,000 square foot) office building, which is located north of Highway 237 on America Center Drive.

OVERVIEW (CONT'D.)

The local real estate market continues to experience strong growth in home prices compared to prior year levels, however, signs of the market slowing down may be appearing. According to data from the Santa Clara County Association of Realtors, the median single-family home price in August 2018 of \$1.18 million is up 22.0% from the August 2017 price of \$967,000. However, it

is important to note that this price is down from the historically high peak price of \$1.3 million experienced in May 2018. While the median home price has risen from the prior year level, the number of property transfers (sales) through August 2018 has dropped. The number of property transfers through August 2018 totaled 1,312, which represents a 14.8% drop from the 1,540 transfers that occurred through August 2017. The decrease in property sales compared to prior year levels is primarily attributable to the limited inventory available on the housing market coupled with the significantly high home prices. Homes continue to sell quickly, with the average days-on-market for the July-August two-month period totaling 19 days in both 2017 and 2018.



On a national level, consumer confidence increased in August, following a slight increase in July. Lynn Franco, Director of Economic Indicators at The Conference Board, stated "Consumer confidence increased to its highest level since October 2000, following a modest improvement in July. Consumers' assessment of current business and labor market conditions improved further. Expectations, which had declined in June and July, bounced back in August and continue to suggest solid economic growth for the remainder of 2018. Overall, these historically high confidence levels should continue to support healthy consumer spending in the near-term."²

Economic conditions will continue to be closely monitored and will be factored into the assessment of the City's performance in 2018-2019 as well as the development of the 2020-2024 General Fund Forecast that will be released in February 2019.

² The Conference Board, Consumer Confidence Survey, August 28, 2018

GENERAL FUND

REVENUES

General Fund revenues through August 2018 totaled \$192.1 million, which represents a decrease of \$19.5 million (9.2%) from the August 2017 level of \$211.7 million. This decrease is primarily due to declines in Licenses and Permits, Sales Tax, Transfers/Reimbursements, and Utility Tax, which are the result of timing differences of payments being processed and negative accrual adjustments. Though it is early in the fiscal year, General Fund revenues are generally tracking to meet or exceed budgeted estimates. The following discussion highlights General Fund revenue activities through August.

KEY GENERAL FUND REVENUES

Revenue	2018-2019 Estimate	YTD Actual	Prior YTD Collections
Property Tax	\$ 320,450,000	\$ 271,564	\$ 773,456

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 2018-2019, Property Tax receipts are estimated at \$320.5 million, which reflects growth of 5.2% over the estimated 2017-2018 collections (Secured Property Tax assumes 5.5% growth and the remaining categories range from 0%-3% growth). The 2018-2019 estimate reflects continued moderate growth as well as a 2.0% California Consumer Price Index increase that will be assumed in the Secured Property Tax category. Through August, \$272,000 in the SB 813 Property Tax category has been received, reflecting only 0.08% of the 2018-2019 budget for this category. The very preliminary estimate from the County of Santa Clara of \$323.2 million is slightly above the 2018-2019 Adopted Budget estimate by approximately \$2.8 million based on a higher projected Secured Property receipts of \$5.0 million, which consists of higher ERAF receipts (\$5.5 million) and regular Secured receipts (\$3.5 million), partially offset by lower SARA residual receipts (\$4.0 million). The higher overall Secured Property Tax receipts are partially offset by lower Unsecured Property Tax receipts (\$1.0 million) and SB813 receipts (\$1.0 million). Additional information about each of the Property Tax sub-categories is provided below.

Secured Property Taxes represent over 90% of the revenue in the Property Tax category. As anticipated, no Secured Property Tax receipts have been received through August due to the scheduled timing of these payments. For 2018-2019, the Adopted Budget estimate of \$295.5 million was based on assumed growth of 5.5% from the 2017-2018 estimated collection level for Secured Property Taxes. The 2018-2019 estimate includes \$275.1 million from general Secured Property Tax receipts, \$12.0 million from SARA residual Property Tax receipts, and \$8.4 million from the distribution of excess Education Revenue Augmentation Fund (ERAF) funds.

GENERAL FUND (CONT'D.)

The Adopted Budget assumed \$8.4 million from 2018-2019 excess ERAF funds, which is consistent with the 2017-2018 actual collection level. 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 is to be returned to the taxing entities that contributed to it. In August, the County provided preliminary information that a payment of approximately \$13.8 million may be received in March. The Administration will continue to monitor the distribution of ERAF receipts and may adjust the budget once further information is provided by the County.

As a result of the SARA bond refunding that occurred in December 2017, the City received an additional residual property tax distribution of \$11.8 million in 2017-2018. The Adopted 2018-2019 Budget assumed receipts would total \$12.0 million, which is fairly consistent with the prior year receipts. However, due to outstanding Supplemental Education Revenue Augmentation Fund (SERAF) loans anticipated to be paid off within the next year, the SARA residual property tax revenue will be reduced on a one-time basis to an estimated \$8.0 million in 2018-2019 and will increase in 2019-2020. The City is also expected to receive the SERAF loan repayment revenue in 2019-2020 due to the timing of payments.

In the **Unsecured Property Tax** category, the largest payment is received in October of each year. The 2018-2019 Adopted Budget revenue estimate of \$14.5 million requires growth of approximately 3% from actual 2017-2018 collection levels of \$14.0 million. The preliminary estimate from the County of Santa Clara for 2018-2019 of \$13.5 million falls approximately \$1.0 million below the budget estimate.

For the **SB 813 Property Tax** category, collections totaled \$272,000 through August, while \$463,000 had been received last year at this time. The 2018-2019 Adopted Budget estimate of \$6.9 million is well below the 2017-2018 actual collection level of \$7.4 million as collections in this category ended 2017-2018 stronger than anticipated. However, the preliminary 2018-2019 estimate from the County for this category of \$5.9 million is approximately \$1.0 million below the budgeted estimate.

Aircraft Property Tax receipts are typically received in October of each year. The 2018-2019 Adopted Budget estimate of \$2.7 million is consistent with the 2017-2018 receipts, and is slightly above the \$2.6 million estimated from the County of Santa Clara Assessor's Office.

In the **Homeowners Property Tax Relief** category, revenues in 2018-2019 are expected to be at the budgeted estimate of \$950,000, which is consistent with the 2017-2018 collection level.

GENERAL FUND (CONT'D.)

Revenue	2018-2019 Estimate	YTD Actual	Prior YTD Collections
Sales Tax	\$ 233,500,000	(\$ 3,872,949)	(\$ 855,060)

The Sales Tax category includes General Sales Tax, Local Sales Tax, and Proposition 172 Sales Tax. When the 2018-2019 Adopted Budget was developed, it was projected that Sales Tax receipts would end 2017-2018 at \$181.2 million and grow 1.7% to \$184.3 million. This increase reflected underlying quarterly growth of 2.0% as well as a downward adjustment of \$550,000 to account for a prior year accrual adjustment that occurred in 2017-2018. In 2017-2018 Sales Tax receipts, however, receipts ended the year at only \$177.4 million. This lower collection level was due to the under-distribution of sales tax revenue throughout the State. The California Department of Tax and Fee Administration (CDTFA), which is responsible for distributing Sales Tax revenue to jurisdictions in California, implemented a new automated system in May 2018, which has resulted in 3rd quarter and 4th quarter receipts not being fully disbursed to jurisdictions during the quarter in which the tax revenue was received. The CDTFA is processing the outstanding payments, and based on information received from the City's Sales Tax consultant, it is anticipated that the CDTFA will include the unallocated payments in the 1st and/or 2nd quarter 2018-2019 disbursements. It is estimated that at least \$5 million was not recognized in 2017-2018 due to this booking issue, and a \$5 million increase to the 2018-2019 Sales Tax revenue estimate is recommended in the 2017-2018 Annual Report to account for this underpayment.

Sales Tax receipts through August, which are negative \$3.9 million, primarily reflect accrual adjustments. Information on the first quarter collections of General Sales Tax and Local Sales Tax revenue is not received until November 2018, which will represent July-September activity.

General Sales Tax receipts in 2017-2018 of \$177.4 million grew 1.5% from the 2016-2017 collection level of \$174.7 million. If the outstanding 2017-2018 payments conservatively estimated at \$5 million had been received, collections would have ended the year at \$182.4 million, 4.4% above the prior year. The year-over-year growth is primarily driven by the 8.75% growth in the first quarter of 2017-2018. That quarter, however, is compared to a very low first quarter in 2016-2017 that resulted from a large negative correction associated with jet fuel sales tax revenues that were allocated to San José in 2015-2016 in error and therefore reversed in 2016-2017.

When the 2018-2019 Adopted Budget was developed, the General Sales Tax estimate of \$184.3 million reflected growth of 1.7% from the 2017-2018 estimate of \$181.2 million. This reflected underlying quarterly growth of 2.0% as well as a downward adjustment of \$550,000 to account for a prior year accrual adjustment that occurred in 2017-2018. Based on the actual 2017-2018 receipts of \$177.4 million plus an additional \$5 million in estimated underpayments, growth of approximately 1% is needed in 2018-2019 over the adjusted 2017-2018 receipts of \$182.4 million.

Starting in 2016-2017, the Sales Tax category includes **Local Sales Tax**. In June 2016, San José voters approved a ¼ cent local sales tax, which began implementation in October 2016. Receipts

GENERAL FUND (CONT'D.)

in 2017-2018 represented the first year of full implementation of the tax and totaled \$42.6 million, of which \$1.3 million is due to a prior year accrual adjustment that occurred in 2017-2018. When the 2018-2019 Adopted Budget was developed, the 2017-2018 Local Sales Tax was estimated at \$43.5 million, which is consistent with the actual performance level. In 2018-2019, revenue of \$43.0 million is estimated, which reflects underlying quarterly growth of 2.0% as well as a downward adjustment of \$1.3 million to account for the prior year accrual adjustment.

Similar to the General Sales Tax, 2017-2018 Local Sales Tax revenue is understated due to the CDTFa implementing a new automated system in May 2018 which has resulted in 3rd quarter and 4th quarter receipts not being fully disbursed to jurisdictions during the quarter in which the tax revenue was received. The CDTFa is processing the outstanding payments, and will include the missed payments in the 1st and/or 2nd quarter 2018-2019 disbursements. The Local Sales Tax receipts in 2017-2018 are likely understated by over \$1 million as a result of the unallocated payments. As necessary, adjustments to this category will be brought forward during 2018-2019 based on the final reconciliation of 2017-2018 and actual 2018-2019 performance.

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. Through August, the **Proposition 172 Sales Tax** receipts of \$648,000 were tracking significantly above 2017-2018 collections of \$75,000 through the same period, which is due to differences in the timing of payments. The 2018-2019 budgeted estimate of \$6.2 million allows for a 2.5% decrease from the 2017-2018 collection level of \$6.4 million. It is currently anticipated that collections will meet the budgeted estimate by year-end.

Revenue	2018-2019 Estimate	YTD Actual	Prior YTD Collections
Transient Occupancy Tax	\$ 19,700,000	\$ 1,294,157	\$ 1,378,872

The 2018-2019 budget estimate for the General Fund **Transient Occupancy Tax** (TOT) allocation (40% of the total tax) is \$19.7 million, which was built assuming growth of approximately 5% from the 2017-2018 estimated collection level of \$18.7 million. However, since 2017-2018 actual receipts came in above estimated levels at \$19.5 million, growth of less than 1% is needed to meet the 2018-2019 budget estimate. Year-to-date TOT receipts through August of \$1.3 million are 6.1% below the prior year collection level of \$1.4 million due to payment timing. However, based on year-to-date receipts and strong hotel occupancy and room rate performance through August, collections are anticipated to meet or slightly exceed the budgeted estimate by year end.

Through August, the average hotel occupancy rate at the 12 reporting major hotels was 80.9%, an increase of 1.1% from the 79.8% occupancy rate for the same period in 2017-2018. Average room rates also increased, from \$197.6 to \$216.1 (9.4%), as well as year-to-date average revenue-per-available room (RevPAR), from \$157.7 to \$174.8 (17.1%), relative to the same time period in 2017-2018.

GENERAL FUND (CONT'D.)

Revenue	2018-2019 Estimate	YTD Actual	Prior YTD Collections
Utility Tax	\$ 102,400,000	\$ 3,920,430	\$ 8,446,754

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 \$3.9 million are 53.6%, below the prior year collection level, which is primarily due to lower collections in the Gas and Electric Utility Tax categories. The majority of this variance, however, was due to differences in the timing of payments. The 2018-2019 Adopted Budget was built on the assumption that 2017-2018 Utility Tax revenue would end the year at \$101.3 million and grow 1.5% to \$102.4 million in 2018-2019. However, since 2017-2018 ended the year only at \$99.8 million, growth of almost 3% is needed in 2018-2019 to meet the budgeted estimate. It should be noted that Utility Tax receipts reflect a one-month lag, therefore, data for only one month of activity in 2018-2019 is available at this time. It is anticipated that revenue will meet or fall slightly below budgeted levels by year-end.

In the **Electricity Utility Tax** category, collections through August totaled \$215,000, which is significantly less than the \$4.5 million received during the same time period in the prior fiscal year and is attributed to differences in the timing of payments. The 2018-2019 Adopted Budget was built on the assumption that 2017-2018 receipts would total \$48.0 million, and grow approximately 2% to \$49.0 million in 2018-2019. However, since 2017-2018 ended the year at \$46.8 million, growth of almost 5% is needed to meet the budgeted estimate. Receipts may not meet this estimate, and any necessary adjustments will be brought forward later in the year.

In the **Gas Utility Tax** category, receipts through August totaled \$76,000, compared to previous year collections of \$481,000. The 2018-2019 Adopted Budget estimate of \$10.0 million assumed no growth from the 2017-2018 estimate of \$10.0 million. However, revenues in 2017-2018 ended the year at \$10.6 million, therefore the 2018-2019 estimate allows for an almost 5% drop from the prior year collections.

Water Utility Tax collections of \$1.5 million through August are 11.7% above the prior year level of \$1.3 million. The 2018-2019 Adopted Budget was built on the assumption that \$16.7 million would be received in 2017-2018, then grow approximately 3% to \$17.2 million in 2018-2019. However, since 2017-2018 receipts only totaled \$15.6 million, growth of 10.4% is required to meet the 2018-2019 budgeted level. Receipts in this category may also fall below the budget.

Collections in the **Telephone Utility Tax** category of \$2.1 million through August are consistent with the prior year level. Revenues in this category have been consistently decreasing in recent years, which reflects the competition between cellular carriers and the move from some cellular customers to VOIP and other services which are less expensive. The 2018-2019 Adopted Budget estimate of \$26.2 million allows for a 2.4% decrease from the 2017-2018 collection level of \$26.9 million.

GENERAL FUND (CONT'D.)

Revenue	2018-2019 Estimate	YTD Actual	Prior YTD Collections
Business Taxes	\$ 69,400,000	\$ 11,074,300	\$ 9,595,786

The Business Taxes category consists of the General Business Tax, Cardroom Tax, Marijuana Business Tax, and Disposal Facility Tax. Through August, overall collections of \$11.1 million are 15.4% above the prior year collection levels of \$9.6 million, primarily reflecting higher collections in the General Business Tax and Marijuana Business Tax categories. The 2018-2019 Adopted Budget estimate of \$69.4 million allows for almost 2% decline from 2017-2018 levels as the result of 2017-2018 ending the year approximately \$2.3 million above the estimated level.

Through August, **Cardroom Tax** receipts of \$1.6 million are consistent with the prior year levels. Because receipts in 2017-2018 slightly exceeded expectations, collections in the category can drop by 1% in 2018-2019 and reach the budgeted estimate of \$18.7 million.

Disposal Facility Tax revenue of \$1.0 million are significantly higher than receipts of \$388,000 received in the same time period in the prior fiscal year, due to the timing and recording of receipts. Actual landfill activity is only known for the first month of the fiscal year, which totaled \$1.0 million and represents an 8.5% increase from landfill activity in July 2017. The 2018-2019 Adopted Budget estimate of \$11.5 million allows for a 6% drop from the 2017-2018 actual receipts of \$12.3 million, due to higher than estimated receipts in the last quarter of 2017-2018.

Through August, **General Business Tax** receipts of \$7.2 million are slightly (\$663,000) above prior year collection levels. The 2018-2019 Adopted Budget assumed 2017-2018 collections would reach \$23.7 million, then grow to \$25.7 million in 2018-2019. This factored in 2% underlying growth for inflation adjustments from the 2017-2018 estimate, plus an additional \$1.5 million revenue as the result of the General Business Tax Amnesty Program, which was approved to be implemented in 2018-2019 and would encourage the enrollment of non-compliant businesses. Since 2017-2018 actual receipts totaled \$26.5 million, the 2018-2019 budgeted estimate allows for a 3% drop in receipts. Based on performance in the first two months of the fiscal year, it is anticipated receipts will end the year above budgeted levels.

Marijuana Business Tax collections reflect marijuana business tax as well as marijuana business tax compliance revenues. Through August, receipts of \$1.2 million are 12.0% above prior year levels of \$1.1 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 2018-2019 Adopted Budget estimate of \$13.5 million assumed growth of 5.5% from the 2017-2018 estimate of \$12.8 million based on the legalization of recreational marijuana usage. Since actual 2017-2018 receipts were slightly higher at \$13.0 million, growth of 3.7% is needed to meet the 2018-2019 budgeted estimate. Although it is very early in the fiscal year, based on collections through August, it is anticipated revenue will meet or exceed the budgeted level by year end.

GENERAL FUND (CONT'D.)

Revenue	2018-2019 Estimate	YTD Actual	Prior YTD Collections
Licenses and Permits	\$ 60,893,631	\$ 11,474,509	\$ 12,107,730

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 \$11.5 million are 5.2% below the prior year level of \$12.1 million. This decrease in revenue is primarily due to a timing difference with the receipt of the Cardroom Regulation Fee (\$2.0 million). The 2018-2019 Adopted Budget estimate of \$60.9 million requires growth of almost 1% from the 2017-2018 collection level of \$60.5 million. Based on current collections and historic collection trends, Licenses and Permits receipts are estimated to meet the budgeted levels by year end.

Building Permit revenues of \$6.2 million through August are 18.2% higher than the 2017-2018 collection level for the same period. The 2018-2019 Adopted Budget estimate of \$32.5 million assumed that receipts would remain at the estimated 2017-2018 levels of \$32.5 million. However, since actual 2017-2018 Building Permit revenues totaled \$33.5 million, receipts can drop 3.1% in 2018-2019 and still meet the revenue estimate.

All Building Permit categories are tracking above expected levels except for new residential permits in the building, mechanical, and electrical categories as well as all plumbing permits other than new residential. For 2018-2019, the Building Fee Program continued the phased implementation of the new fees and/or fee modifications recommended for the program as part of the City of San José Development Services Cost Recovery Analysis, Process Improvements, Calculation of Unearned Revenues, and Refund Processing Report accepted by the City Council in December 2016. However, these changes, implemented on August 13, 2018, had no net impact to the overall revenue estimate for 2018-2019 of \$32.5 million. It is currently anticipated Building Permit revenues will meet or exceed the 2018-2019 budget revenue estimate of \$32.5 million by year-end.

As discussed in the Economic Impact section of this report, residential activity through August 2018 consisted of 212 multi-family units and 84 single-family units for a total of 296 units. Commercial activity through August amounted to a valuation of \$60.9 million (new construction valuation of \$21.9 million and alterations of \$38.9 million). Alteration activity accounted for most of the commercial activity in both July and August. Industrial activity through August had a valuation of \$94.8 million (new construction valuation of \$40.0 million and alterations of \$54.8 million).

GENERAL FUND (CONT'D.)

Fire Permits, which consist of development and non-development related permits, totaled \$3.9 million through August 2017, which represents a 10.1% increase from the 2017-2018 collection level of \$3.5 million for the same time period. To meet the 2018-2019 budgeted revenue estimate of \$13.3 million, growth of less than 1% from the 2017-2018 actual collection level of \$13.2 million is needed; at this point of the year, collections are on pace to exceed budgeted levels by year-end.

Development related receipts through August 2018 of \$1.4 million are 20.1% above the 2017-2018 collection level of \$1.2 million. The budgeted estimate of \$8.1 million aligns with the prior year's actual collections of \$8.1 million, therefore, if current collection trends continue, it is anticipated that development-related receipts will exceed the budgeted estimate.

Non-Development receipts of \$2.4 million that have been received through August primarily represent the first of four major billing cycles for non-development fire permits for this fiscal year and represent a 4.66% increase the 2017-2018 collection levels. If current collection trends continue, it is anticipated that development-related receipts will exceed the budgeted estimate.

Revenue	2018-2019 Estimate	YTD Actual	Prior YTD Collections
Fees, Rates, and Charges	\$ 55,560,013	\$ 9,885,482	\$ 8,042,731

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; and Transportation. Through August, revenues totaled \$9.9 million, which is 22.9% above the \$8.0 million received during the same period in the prior year. All departments within the Fees, Rates, and Charges category, with the exception of the Police Department, demonstrated year-over-year increases compared to the prior year levels. The 2018-2019 Modified Budget estimate of \$55.6 million requires an almost 10% increase from the actual 2017-2018 collection level of \$50.7 million.

Through August, **Planning Fee** revenues of \$1.0 million were 7.2% above the prior year collection level of \$944,000. However, to meet the 2018-2019 Adopted Budget estimate of \$8.96 million, an increase of 36.8% is needed from the actual 2017-2018 collection level of \$6.6 million. The budgeted increase reflects City Council-approved fee changes that were implemented on August 13, 2018. Given the August implementation date for the fee increases, collections in the upcoming months are expected to reflect additional growth from the prior year. Revenue was strong for several of the Planning Fees, including preliminary review, public information services, and residential planned development rezonings/rezonings. However, partially offsetting these collections were lower than estimated revenues from several fees, including, residential conventional rezonings/rezonings, residential and non-residential planned development permits, and residential and non-residential site development permits. Based on current collection trends,

GENERAL FUND (CONT'D.)

Planning Fee revenues may end the year below the budgeted estimate. The revenue will be monitored closely to determine if any budgetary actions are needed to align the budgeted estimate with actual revenues.

Public Works revenues through August of \$2.3 million increased 54.1% from the prior year level of \$1.5 million, which is primarily due to the receipt of Small Cell Permitting revenue (\$700,000), which did not have receipts until June in the prior year. The Public Works revenue collections are comprised of \$1.2 million from the Development Services Fee Program, \$447,000 from the Utility Fee Program, and \$700,000 for Small Cell Permitting. Revenues received for Small Cell Permitting is for works-in-progress that will be spent through the remainder of the fiscal year. Revenues in most engineering residential and non-residential are within budget or slightly below estimated levels due to lower activity levels. However, this decrease is offset by higher collections in the utility excavation category. At this time, collections are projected to end the year at budgeted levels.

EXPENDITURES

Through August, General Fund expenditures (without encumbrances) of \$174.9 million were 12.7% above the prior year level of \$155.2 million. Encumbrances of \$63.1 million were 4.1% below the prior year level of \$65.8 million. General Fund expenditures and encumbrances through August of \$238.1 million constitute 15.7% of the total budget including reserves, and 17.5% of the budget excluding reserves. Overall, expenditures are tracking slightly above estimated levels through August.

Through August, a small number of departments were tracking slightly above the budgeted estimate in personal services expenditures, including the Fire, Public Works, and Environmental Services Departments. 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	2018-2019 Budget	YTD Actual	Prior YTD Actual
Police	\$ 411,404,321	\$ 66,989,110	\$ 48,359,060

Overall, through August the Police Department's expenditures are slightly above estimated levels through August. Personal services expenditures of \$58.8 million, or 15.4% of the Adopted Budget, are slightly higher than the expected levels of 15.3% at this point in the year. In addition, overtime expenditures of \$6.0 million, or 30.34% of the 2018-2019 Adopted Overtime Budget of \$19.6 million, are significantly higher than the expected levels of 15.3% at this point in the year.

GENERAL FUND (CONT'D.)

Based on current overtime trends, and taking into account three academies that will occur this fiscal year, the personal services expenditures are anticipated to exceed the budget by year-end. The Police Department has worked diligently to fill sworn and civilian vacant positions. Vacancy savings have been used to backfill positions in Patrol, however, as vacancies have been filled, this savings has decreased. While the goal is to fill the vacancies and eliminate the need to backfill positions, new recruits are in academy training and field training for 10-12 months. Until the new recruits are street-ready and are solo beat officers in Patrol, the Department continues to backfill these positions, incurring overtime. In anticipation of the high overtime expenditures that will be incurred in 2018-2019 until the new recruits are street-ready, the 2018-2019 Annual Report includes a recommendation to increase the Overtime Budget by \$4.0 million (from \$19.6 million to \$23.6 million).

Overtime consists of overtime expenditures and compensatory time. The Memorandum of Agreement 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 2018 was 267,772 hours for sworn personnel. This represents an increase of 19,798 hours or 8.0% compared to the August 2017 balance of 247,974.

The chart on below outlines current authorized sworn staffing levels and the number of street-ready sworn positions available this year compared to last year. Please note that an additional 41 sworn officers will be added effective June 2019 per the 2018-2019 Adopted Budget, which will increase the authorized sworn staffing level to 1,151.

	2017-2018 (as of 08/31/2017)	2018-2019 (as of 09/21/2018)
Authorized Sworn Staffing	1,109	1,110
Vacancies	(137)	(38)
Filled Sworn Staffing	972	1,072
Field Training Officer/Recruits	(107)	(116)
Street-Ready Sworn Positions Available	865	956
Disability/Modified Duty/Other Leaves	(75)	(75)
Street-Ready Sworn Positions Working	790	881

To fill the vacant sworn positions, the Department will conduct three Police Recruit Academies in 2018-2019, including academies that will begin October 2018 (50 expected recruits), February 2019 (65 expected recruits), and June 2019 (55 expected recruits). The academy staffing levels will be adjusted based on actual attrition and vacancies.

A total of \$8.2 million (27.2%) of the Department's Non-Personal/Equipment budget was expended or encumbered through August. Excluding the remaining balances for centrally-determined details, including electricity, gas, and vehicle operation and replacement, the Department has approximately \$14.2 million, or 68.5% of the non-centrally-determined appropriation available for the remainder of the fiscal year.

GENERAL FUND (CONT'D.)

Department	2018-2019 Budget	YTD Actual	Prior YTD Actual
Fire	\$ 222,063,027	\$ 37,401,317	\$ 28,129,444

Overall, Fire Department expenditures through August 2018 are tracking slightly higher than estimated levels. Personal services expenditures of \$33.4 million, or 15.8% of the Adopted Budget, are slightly higher than the expected level of 15.3% at this point of the year. The higher than estimated expenditures are partially due to expenditures incurred for Strike Team and Task Force 3 deployments, which will receive reimbursement funding from the State of California and Federal Emergency Management Agency and will be brought forward as part of the 2018-2019 Mid-Year Budget Review process. The Fire Department's Personal Services appropriation will continue to be carefully monitored by both the Budget Office and Fire Department to ensure overall expenditures remain within approved levels. The Fire Department's Non-Personal/Equipment budget of \$10.3 million was 38.73% expended or encumbered through August 2018 and is expected to end the year within budgeted levels.

Overall, the average vacancy rate of 6.6% is tracking above the 5.8% vacancy rate experienced this time last year; and vacancies continue to exceed the budgeted rate of 2.5%. The first 2018-2019 Firefighter Recruit Academy is set to start this fall consisting of 27 Firefighter Recruits and will reduce the number of sworn vacancies from 49 to 22.

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 28 sworn personnel on administrative assignments.

CONTINGENCY RESERVE

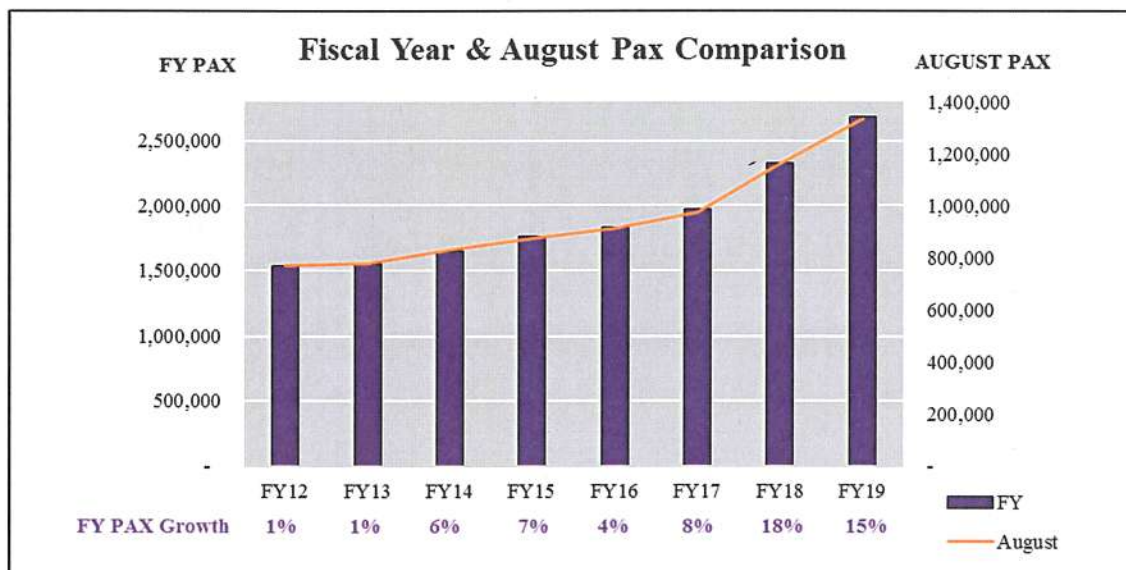
The General Fund Contingency Reserve remained at \$36.5 million through August, with no revisions through the first two months of the fiscal year. However, the 2017-2018 Annual Report, which will be brought forth for City Council consideration on October 16, 2018, includes a recommendation to increase the Contingency Reserve by \$500,000, to \$37.0 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 2.7 million passengers, an increase of 15.4% from the figures reported through August of the prior year. International passengers were boosted (up 20% this fiscal year) by the start of new service to Mexico City by Aeromexico, to Morelia and Zacatecas by Volaris, and to Cabo San Lucas by Southwest. Domestic passengers increased due to the start of new service to Houston, Orlando, and Spokane by Southwest as well as new service to Dallas, Los Angeles, and New York by Alaska. The chart below depicts the year-over-year change for the month of August and Fiscal Year-to-Date for the last eight years.

Year-to-date mail, freight and cargo totaled 20.2 million pounds, which represents a 1.0% decrease through August of the prior year. Many revenue-generating activities posted increases over the same period of the prior fiscal year: Traffic Operations (landings and takeoffs) by 12.0%; Landed Weights by 12.5%; Gallons of aviation fuel sold by 14.2%; Parking exits by 2.1%; and Ground Transportation (taxicabs & TNC's) operations are 142.0% higher than the prior year. The Ground Transportation increase is partially attributed to the municipal code change approved in June and became effective in October, which allowed for counting and charging for both TNC passenger drop-off and pick-up trips.



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 are below budgeted levels. In the Maintenance and Operation Fund Personal Service expenditures were 15.1% of budget compared to the

OTHER FUNDS (CONT'D.)

benchmark of 15.3%, while Non-personal/Equipment expenditures (without encumbrances) were 5.4% compared to the benchmark of 6.7%. Non-personal/Equipment expenditures in the Customer Facility and Transportation Fee Fund were 8.4% compared to the straight-line benchmark of 16.7%.

Construction and Conveyance Tax Funds

Through August 2018, Construction and Conveyance (C&C) Tax receipts of \$4.8 million are 38.7% higher than collections experienced through August 2017 of \$3.5 million. Collections through August 2018 represent 12.8% of the 2018-2019 Adopted Budget estimate of \$38.0 million. In addition, the City has also received September Conveyance receipts from Santa Clara County, which total \$4.9 million, a 22.2% increase from the \$4.0 million received in September 2017.

The 2018-2019 Adopted Capital Budget was built on the assumption that 2017-2018 receipts would total \$42.0 million, then drop by almost 10% to \$38.0 million in 2018-2019. However, due to stronger than anticipated performance in the last half of the fiscal year, 2017-2018 receipts totaled \$48.1 million. Therefore, the 2018-2019 revenue estimate of \$38.0 million allows for a 21% decline in tax revenue from the 2017-2018 actual tax collection.

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 strong 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. Local real estate information will therefore continue to be closely monitored.

Other Construction-Related Revenues

Revenues associated with construction activity are currently anticipated to meet their budgeted levels by year end. As discussed below, the Construction Excise Tax receipts through August are lower than prior year levels, however, the Building and Structure Construction Tax have grown compared to the prior year receipts. Construction activities drive revenue collection in several categories, including the Construction Excise Tax and the Building and Structure Construction Tax, 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 \$3.3 million is 14.3% below the prior year receipts of \$3.8 million. This revenue level represents 15.5% of the 2018-2019 Budget of \$21.0 million. When the 2018-2019 Adopted Capital Budget was developed it was assumed that high collection receipts experienced in 2016-2017 (\$30.2 million) and 2017-2018 (estimated at \$27.0 million) would not be sustainable, therefore, the 2018-2019 estimate was decreased by 22.2%, to \$21.0 million. However, since 2017-2018 receipts of \$29.4 million ended

OTHER FUNDS (CONT'D.)

the year above the estimated level, the 2018-2019 budgeted estimate allows for a 28.5% drop from the prior year collection level. While it is still very early in the fiscal year, and this tax is extremely volatile, it is currently anticipated receipts will meet or exceed budgeted levels. This revenue category will continue to be monitored throughout the year, and if necessary, budget adjustments may be brought forward at a later date.

Through August, the **Building and Structure Construction Tax** collection level of \$3.0 million is 4.2% above the prior year receipts of \$2.8 million. This revenue level represents 18.5% of the 2018-2019 Budget of \$16.0 million. When the 2018-2019 Adopted Capital Budget was developed it was assumed that high collection receipts experienced in 2016-2017 (\$23.3 million) and 2017-2018 (estimated at \$20.0 million) would not be sustainable, therefore, the 2018-2019 estimate was decreased by 20%, to \$16.0 million. However, since 2017-2018 receipts of \$21.5 million ended the year above estimated levels, the 2018-2019 budgeted estimate allows for a 25.5% drop from the prior year collection level. While it is still very early in the fiscal year, and this tax is extremely volatile, it is currently anticipated receipts will meet or exceed budgeted levels. Similar to the Construction Excise Tax, this revenue category will also continue to be monitored throughout the year, and if necessary, a budget adjustment may be brought forward at a later date.

CONCLUSION

Overall, the City's funds appear to be performing within budgeted expectations through August. The City ended the 2017-2018 fiscal year in solid position as the starting point for 2018-2019. 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 if necessary.

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



MARGARET MCCAHAH
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