

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Debra Figone

**SUBJECT: 2009-2010 CITY MANAGER'S
BUDGET REQUEST AND
2010-2014 FIVE-YEAR FORECAST**

DATE: February 27, 2009

INFORMATION ONLY

EXECUTIVE SUMMARY

In compliance with City Charter Section 1204, and the City Council's adopted budget process, this document provides both the 2009-2010 City Manager's Budget Request (Budget Balancing Strategy Guidelines) and the 2010-2014 Five-Year Forecast and Revenue Projections for the General Fund and Capital Improvement Program. In addition, the General Fund Structural Deficit Elimination Plan Update is included in this document per City Council direction. Following are the major highlights of this report:

- A significant General Fund base budget shortfall of \$61.2 million is projected for 2009-2010, representing almost 7% of the projected expenditures for next year. This shortfall reflects the projected cost of delivering existing services as well as the services for which the City has already committed, such as the operation of new facilities under construction and the addition of 25 police officers next year. The shortfall amount increases to \$67.1 million when adding the unmet/deferred infrastructure and maintenance needs that are included in the General Fund Structural Deficit definition. The base budget shortfall of \$61.2 million compares to a \$59.1 million base budget shortfall projected as part of the 2010-2014 General Fund Preliminary Forecast released in November 2008. Last year at this time (February 2008), a \$42.5 million shortfall was estimated for 2009-2010. Fiscal year 2009-2010 is the eighth consecutive year that budget actions will be necessary to address a General Fund shortfall.
- An additional base budget shortfall totaling \$36.7 million is projected in 2010-2011 bringing the total General Fund shortfall to almost \$100.0 million for the first two years of the forecast period. For 2010-2011, it is important to note that increases to the City's contributions to its two retirement systems are almost inevitable and will increase the shortfall that year, but the amount is unknown at this time. The extreme volatility and steep declines in the financial markets have negatively impacted performance in the plans. Actuarial analysis will be performed later this year and impacts should be known and incorporated into the 2011-2015 General Fund Preliminary Forecast to be released next fall.
- When compared to the November 2008 Forecast, the \$2.1 million increase to the 2009-2010 projected General Fund shortfall reflects the net impact of downward adjustments to revenue estimates of \$17.5 million and to expenditure budgets of \$15.4 million. The continued rapid deterioration of the economy has led to further reductions to the economically sensitive revenue categories. Expenditure adjustments reflect updated information and a more in-depth review of base costs.

EXECUTIVE SUMMARY (CONT'D.)

- Over the five-year forecast, the General Fund Forecast base operating budget shortfall totals \$86.2 million and the General Fund Structural Deficit totals \$115.7 million. The deep global recession is a major contributing factor to the size of the deficits projected for both 2009-2010 and 2010-2011. The variances in the last three years of the forecast are minimal, ranging from a deficit of \$4.9 million to a surplus of \$10.1 million in the last year of the Forecast. The improved budget situation displayed for the last three years of the Forecast reflects two important factors: fiscal conditions are expected to get better as the economy slowly recovers during that period, and no salary cost-of-living adjustments (COLAs) for any of the City's employees have been assumed in the last three years. There are currently no negotiated agreements that cover this time period. The consideration of salary increases is being treated in this Forecast as a resource allocation policy decision. This decision will need to be made in the context of what is affordable in light of the City's many service delivery priorities. At current rates, each 1% increase in salary has a General Fund price tag of \$5.5 million.
- As is customary in the Forecast, two alternative forecasts have been developed to model the range of financial scenarios possible under varying economic conditions. "Optimistic" and "Pessimistic" Cases have been created to model economic scenarios considered possible, but less likely to occur than the "Base Case". In 2009-2010, the projected deficits range from \$54 million to \$73 million, with the Base Case totaling \$61.2 million.
- It is also important to note what this preliminary base budget Forecast does not reflect: the impact of compensation increases resulting from outstanding negotiations if they exceed Forecast projections; changes in City contributions to the two retirement plans due to the significant losses suffered by those funds in recent months; funding for unmet/deferred infrastructure and maintenance needs; potential State budget actions; financial impacts associated with planned County annexations, the expansion of North San José; and potential impacts if the San Jose Redevelopment Agency reaches its tax increment revenue cap and is unable to continue to fund various eligible City support services. It also does not factor in one-time revenue sources, such as the 2009-2010 Future Deficit Reserve, or one-time expenditure needs.
- In approaching the 2009-2010 budget, the Administration proposes the use of the budget balancing strategy guidelines (2009-2010 City Manager's Budget Request) outlined in this memorandum. In addition, City Council priorities identified in prior policy sessions will guide the City's balancing strategy efforts. The Administration recommends City Council approval of the proposed City Manager's Budget Request (Budget Balancing Strategy Guidelines), with any desired revisions, as part of the Mayor's March Budget Message review process.
- The General Fund Structural Deficit Elimination Plan released in November 2008 and reviewed by the Mayor and City Council on December 5, 2008, outlined strategies to eliminate the General Fund structural deficit over the next five years. As directed by the City Council, this forecast document includes an update of the General Fund Structural Deficit Elimination Plan that factors in the most current forecast information. The strategies identified in the plan will serve as a blueprint to guide the 2009-2010 General Fund budget

EXECUTIVE SUMMARY (CONT'D.)

balancing efforts and will be refined in the future to reflect approved 2009-2010 budget actions, information, and further analysis. City staff will also start working on some of these major ideas to pave the way for future action, particularly for those items that have a longer implementation horizon.

- Capital Program-related revenues are projected to decline significantly from the estimates provided in the 2009-2013 Adopted Capital Improvement Program due to the steep declines in development activity and the drop in Construction and Conveyance Tax receipts.

BACKGROUND

The City Manager's Budget Request and Five-Year Forecast are key components of the City's annual budget process, and critical steps in the development of both the City's annual Operating and Capital Budgets and the Five-Year Capital Improvement Program (CIP). The General Fund Structural Deficit Elimination Plan Update outlines strategies that provide a roadmap for closing the City's General Fund structural deficit.

The City Manager's Budget Request includes budget balancing strategy guidelines that the Administration recommends be used in developing the 2009-2010 Proposed Budget. These guidelines are predicated on the most current projections for expenditure requirements and available revenue in the coming fiscal year. As the City's fiscal status for 2009-2010 is an integral part of the Administration's proposed approach to preparing next year's budget, a detailed discussion of the key economic, revenue, and expenditure assumptions for 2009-2010, and the subsequent four years, is provided as part of the 2010-2014 Five-Year Forecast and Revenue Projections section of this document.

ANALYSIS

This overview includes the following: a discussion of the 2009-2010 City Manager's Budget Request, including a description of the proposed budget balancing guidelines; an overview of the 2010-2014 Five-Year Forecast and Revenue Projections; an overview of the General Plan Structural Deficit Elimination Plan Update, a summary of the Capital Revenue Forecast; and a description of the next steps in the 2009-2010 budget process.

2009-2010 CITY MANAGER'S BUDGET REQUEST

This document provides a set of budget balancing strategy guidelines (these encompass the 2009-2010 City Manager's Budget Request) as well as financial projections recommended by the City Administration for use in preparing the 2009-2010 budgets for the General Fund and selected Capital Funds. The recommended guidelines contained in the 2009-2010 Manager's Budget Request have been formulated in the context of projections for an economy already in the grip of a deep recession that is continuing to contract in the early part of the forecast with slow recovery in the out years of the forecast period.

2009-2010 CITY MANAGER'S BUDGET REQUEST (CONT'D.)

It is currently assumed that the global recession and financial crisis will continue through at least 2009, and likely beyond. This will result in a significant drop-off in the City's economically sensitive revenues, particularly in 2009-2010 and 2010-2011. A slow economic recovery is expected in the later years of the Forecast, assuming that economic stimulus efforts are successful in pulling the economy out of one of the deepest recessions in a generation. The difficulty in this Forecast is projecting the depth and length of the current slowdown given the unprecedented nature of the turmoil in the global economy. It is also difficult to predict when and to what extent the various efforts underway to try to stabilize the situation will begin to show results. Until that time, the range of possible economic scenarios is staggering, from a modest recession lasting a year or two to a much more severe disruption with long-lasting outcomes.

With weak revenue growth, expenditure levels of existing General Fund programs are expected to exceed revenue sources in the first three years of this Forecast, with small surpluses in the last two years. It should be noted, however, that no cost-of-living salary increases for any employees have been assumed in the last three years of the Forecast, reflecting the fact that there are no negotiated agreements covering this period. Approval of any negotiated salary or benefit increases in those years, without any offsetting increase in revenues or reduction in costs, will have the effect of driving up the City's shortfall. The consideration of salary increases is being treated as a resource allocation policy decision. This decision will need to be made in the context of what is affordable in light of the City's many service delivery priorities.

This forecast updates the November 2008 Preliminary General Fund Forecast that projected a \$59.1 million shortfall next year. As discussed later in this Transmittal Memorandum and in greater detail in this document, these updated projections indicate a slightly larger General Fund base shortfall for 2009-2010 in the amount of \$61.2 million. Over the five-year forecast period, the General Fund base shortfalls are expected to total \$86 million. The City is required to address these shortfalls each year in order to develop a balanced budget. The base shortfall figures, however, do not include the unmet/deferred infrastructure and maintenance needs that are included in the broader General Fund Structural Deficit definition. Once those costs are added, the General Fund structural budget deficit climbs to \$115.7 million over the next five years. These additional costs, while not required to be addressed in the annual budget, represent a long-term unfunded need for the City.

Projections for the selected Capital Improvement Program (CIP) revenues included in this Forecast have also been adjusted downwards significantly from the last Forecast. For the major development-related capital budget revenues (which primarily support the Traffic Capital Budget), an overall decrease to the revenue estimates included in the prior CIP is forecasted, based on the dismal performance in these areas and the development activity projections provided by the Planning, Building and Code Enforcement Department. For the Construction and Conveyance (C&C) Tax, which supports a number of capital programs, it is anticipated that collections will continue to fall from the record setting levels experienced in recent years and will normalize at levels well below those assumed in the development of the last CIP.

2009-2010 CITY MANAGER'S BUDGET REQUEST (CONT'D.)

As noted above, the Administration proposes the use of the budget balancing strategy guidelines (2009-2010 City Manager's Budget Request) outlined on the following page to approach the 2009-2010 budget development process. As part of the 2009-2010 Mayor's March Budget Message, the Administration requests confirmation of these guidelines, with any desired revisions. These guidelines incorporate both short-term and long-term approaches to budget balancing efforts and reflect the City's sound fiscal principles.

The Proposed Budget Balancing Strategy Guidelines are similar to those adopted by the Mayor and City Council last year as part of the 2008-2009 Mayor's March Budget Message. A few modifications, however, have been incorporated into the proposed strategies to better position the City to address the significant General Fund shortfalls over the next few years. For example, a change to Budget Balancing Strategy Guideline #2 has been proposed to allow some flexibility on the use of one-time funds to close the General Fund budget shortfall in order to lessen the impact on the community. Given the severity of the economic downturn, it may be necessary to use one-time funds in the short-term to address a portion of the shortfall, allowing additional time to develop new budget balancing strategies and to determine whether the economy is recovering at a faster rate than currently anticipated.

In addition, modifications to Budget Balancing Strategy Guidelines #4 and #5 have been proposed to reflect General Fund Structural Deficit Elimination Plan efforts. Strategy #4 identifies the Structural Deficit Elimination Plan as the planning tool for pursuing new revenue sources or modifying existing revenue sources. In addition, Guideline #5 references the use of the Analytical Framework for Service Reductions/Eliminations to assist in service delivery optimizations or to identify those services that should be reduced or eliminated. This new framework was prepared in conjunction with the General Fund Structural Deficit Elimination Plan.

In addition to the budget balancing strategy guidelines, City Council priorities and goals identified in prior policy sessions will guide the City's budget balancing efforts. Input from the community through community surveys, various City Councilmember and stakeholder outreach activities, the San José Neighborhood Association Priority Setting Session, and the work to-date on eliminating the General Fund structural deficit will also serve as an important tool in this process. It is anticipated that feedback from these efforts will also be incorporated into the Mayor's March Budget Message.

2009-2010 CITY MANAGER'S BUDGET REQUEST (CONT'D.)

2009-2010 Budget Balancing Strategy Guidelines

1. Develop a budget that balances the City's delivery of essential services to the community, including building strong neighborhoods and supporting economic growth, with the resources available.
2. Every effort should be made to resolve the projected budget deficit with ongoing revenue and expenditure solutions to ensure no negative impact on future budgets to maintain the City's high standards of fiscal integrity and financial management. One-time funding sources, however, may be used to mitigate the impact on the community or to provide time for service delivery optimization efforts.
3. Use fee increases to assure that operating costs are fully covered by fee revenue and explore opportunities to establish new fees for services, where appropriate.
4. Explore expanding and/or re-directing existing revenue sources and/or adding new revenue sources for addressing both the General Fund structural deficit and unfunded needs as outlined in the General Fund Structural Deficit Elimination Plan.
5. Focus on protecting vital core City services for both the short- and long-term. Analyze all existing services and target service reductions or eliminations in those areas that are least essential. To the extent possible, use the Analytical Framework for Service Reductions/Eliminations to assist in service delivery optimization opportunities or identify services that should be eliminated.
6. Defer any new program commitments and initiatives or program expansions, unless those program commitments stimulate the local economy, job creation, new revenues, have a significant return on investment for the General Fund, and/or are funded through redeployment of existing resources.
7. Explore alternative service delivery mechanisms (e.g., appropriate community partnerships, public-private partnerships, working with other jurisdictions, outsourcing/in sourcing services delivered by City staff, etc.) to ensure no service overlap, reduce and/or share costs, and use our resources more efficiently and effectively.
8. Focus on business process redesign to improve employee productivity and business practices, including streamlining, innovating, and simplifying City operations (e.g., using technology) through employee engagement and empowerment so that services can be delivered with quality, flexibility, and lower cost.
9. Use the General Plan as a primary long-term fiscal planning tool and link ability to provide City services to development policy decisions.
10. Continue to make community and employee engagement a priority for budget balancing idea development.
11. Assuming positions are in the right program, make every effort to eliminate vacant positions, rather than filled positions, to minimize the number of employee layoffs. As programs are reduced or eliminated, ensure that management and administration are reevaluated accordingly.
12. Explore personal services cost savings, subject to the meet and confer process where applicable, by 1) considering further incorporation of total compensation bargaining concepts into the meet and confer process and focusing on all personal services cost changes (e.g., salary step increases, benefit cost increases), 2) civilianizing more sworn positions, 3) exploring alternate benefit structures for new employees, and 4) changing employee/retiree health care benefit plan designs.

2009-2010 CITY MANAGER'S BUDGET REQUEST (CONT'D.)

In light of the current forecasted budgetary situation, the Administration directed each of the six current City Service Areas (CSAs) (Community and Economic Development, Environmental and Utility Services, Neighborhood Services, Public Safety, Transportation and Aviation Services, and Strategic Support) to develop 2009-2010 budget proposals necessary to eliminate the projected General Fund shortfall using these guidelines. For planning purposes, budget reduction target ranges were set at 1% to 5% of General Fund Base Budget amounts (adjusted for reimbursement-related costs and costs beyond the control of the CSA) for the Public Safety CSA and 17% to 22% for the remaining five CSAs. These target ranges were set at levels to generate approximately \$40 million to \$65 million in General Fund proposals.

The Mayor is scheduled to issue a proposed March Budget Message in early March, which will then be discussed, amended if necessary, and adopted by the City Council. The contents of that Message will provide specific guidance for the preparation of the City Manager's 2009-2010 Proposed Capital and Operating Budgets currently scheduled to be submitted on April 20, 2009 and May 1, 2009, respectively. As required by City Charter, those Proposed Budgets will contain comprehensive plans for how the City organization will meet the City Council's priorities and community service needs while maintaining the fiscal integrity of the City.

After the release of the Proposed Budgets, there will be a series of Proposed Budget Study Sessions and Public Hearings to discuss the budget proposals and the associated impacts on performance measures and service delivery. The Administration will also work with the City Council to provide informational meetings on the Proposed Budget in the various Council Districts. Additional input by the City Council and community will be incorporated into the budget through these Proposed Budget Study Sessions, Public Hearings, and the Mayor's June Budget Message during the months of May and June 2009.

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS

The 2010-2014 Five-Year Forecast and Revenue Projections portion of this document is divided into five sections.

1. **Elements of the General Fund Forecast** – This section begins with a description of the overall economic outlook and the expected performance of the economy over the five-year period, followed by detailed descriptions of the assumptions made concerning each of the General Fund revenue and expenditure categories. The Elements of the General Fund Forecast section ends with information regarding the projected General Fund operating margin for each of the five years included in the forecast period.
2. **Base General Fund Forecast** – The forecast model is presented in this section. It includes projections for each of the General Fund revenue and expenditure categories. The expenditure summary is divided into two sections:

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

- *Base Case without Additions* – This section describes projections associated with existing expenditures only.
- *Base Case with Committed Additions* – This section describes the existing expenditures (Base Case) along with those expenditures to which the City is committed by previous Council direction and has less discretion, such as maintenance and operating costs for capital projects scheduled to come on-line during the next five years.

The Five-Year Forecast discussion is based on the Base Case with Committed Additions scenario, which is considered the most likely scenario for the upcoming year.

3. **Committed Additions to the Base General Fund Forecast** – This section describes the committed additions considered in the Forecast, including the financial impact in each year of the Five-Year Forecast. This section also includes a discussion of Budget Principle #8, which pertains to capital projects with General Fund operating and maintenance costs in excess of \$100,000.
4. **Alternative Forecast Scenarios** – Because all forecasts are burdened with a large degree of uncertainty, two plausible alternative forecast scenarios are presented – an Optimistic Case and a Pessimistic Case. These cases are compared with the Base Case, with committed additions, to show the range of growth rates for revenues and expenditures and the associated operating margins.
5. **General Fund Structural Deficit Elimination Plan Update** – The General Fund Structural Deficit Elimination Plan was released in November 2008. An update to that report is included in this document to align the Plan to the latest General Fund Five-Year Forecast.
6. **Capital Revenue Forecast** – This section describes the estimates for construction and real estate related revenues that are major sources of funding for the City's Five-Year Capital Improvement Program.

Two appendices are also included in this document. The first appendix, prepared by the Planning, Building and Code Enforcement Department, documents the basis for that department's five-year projections for construction activity. The second appendix provides descriptions of the City's major General Fund revenue categories.

2010-2014 Five-Year General Fund Forecast

The following table displays the projected General Fund revenues and expenditures over the next five years and the total cumulative shortfall. In addition to the cumulative shortfall, the incremental shortfall (assuming each preceding deficit is solved completely with ongoing solutions in the year it appears) for each year of the forecast is included. Because it is the City's goal to solve each deficit with ongoing solutions, the incremental shortfall figure is useful in that it shows the additional shortfall and/or surplus attributed to a particular fiscal year.

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

**2010-2014 GENERAL FUND FIVE-YEAR FORECAST
BASE BUDGET SHORTFALL
(\$ in Millions)**

	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014
Projected Revenues	\$ 824.9	\$ 834.3	\$ 863.1	\$ 890.0	\$ 921.1
Projected Expenditures	\$ 886.1	\$ 932.2	\$ 966.0	\$ 986.4	\$ 1,007.3
Total Cumulative Shortfall	(\$ 61.2)	(\$ 97.9)	(\$ 102.9)	(\$ 96.4)	(\$ 86.2)
Total Incremental Shortfall	(\$ 61.2)	(\$ 36.7)	(\$ 4.9)	\$ 6.5	\$ 10.1

The fiscal outlook for the City in years one and two of this Forecast is considerably worse when compared to both the preliminary 2010-2014 General Fund Forecast released in November 2008 and the final 2009-2013 General Fund Forecast that was issued in February 2008. The remaining years, on the other hand, are relatively unchanged or slightly improved due, in part, to methodology changes. The last three years in this Forecast do not presume cost-of-living salary increases. This is a change from the February 2008 Forecast that included anticipated salary adjustments, but is consistent with the November 2008 Preliminary Forecast.

Major changes to the assumptions for revenue and expenditure growth have been incorporated into the Forecast, reflecting the impact of the deep global recession and updated expenditure information. Through the first three quarters of 2008, the economy was very weak. The last quarter of 2008, however, was disastrous, and one of the most dismal periods in decades. The 6.2% drop in the Gross Domestic Product (GDP) in the fourth quarter of 2008 was the worst decline in 25 years. On a national level, total non-farm payroll jobs fell by 2.6 million in 2008, the largest job loss total since 1945. The majority of these job losses occurred in the last four months of the year. In the San José region, the number of jobs dropped by 11,000 in 2008, the largest decline since 2003. The unemployment rates at the national, State and local levels also increased by approximately 50% from December 2007 to December 2008. Homes prices also continued to fall sharply. In 2008, the median price for single family homes within San José dropped 35% from \$699,000 in December 2007 to \$452,000 in December 2008. Given the alarming deterioration of the economy at the end of the year, the Conference Board Consumer Confidence Index fell to a new all-time low in December 2008 (Index began in 1967).

In the first quarter of 2009, the news has continued to worsen as the economy continues its downward spiral. In January 2009, U.S. employment fell sharply with the loss of almost 600,000 jobs and an increase in the unemployment rate from 7.2% to 7.6%. The California unemployment rate reached double-digit levels of 10.1% in January 2009, the highest rate since June 1983. In the San José region, the median price for single family homes fell further to \$415,000, the lowest level since January 2000. At the end of February, the Dow Jones Industrial average was at its lowest point since May 1, 1997. The 11.7% decline in the Dow in February was the worst decline for that month since February 1933 during the Great Depression, which had a decline of 15.6%. The Conference Board Consumer Confidence Index also reached new all-time lows in both January and February 2009.

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

Given the bleak economic environment and the expectation that the severe recession will continue to impact this region through at least 2009 and probably beyond, the economically sensitive revenues have been adjusted downwards significantly. For example, the 2009-2010 Sales Tax projection of \$139.0 million is well below both the November 2008 Forecast estimate of \$141.9 million and the February 2008 Forecast estimate of \$158.1 million. The 2009-2010 Property Tax revenue estimate has also been revised downward over the last year from \$217.5 million in February 2008 to \$211.0 million in November 2008 and finally to \$207.8 million in this Forecast. Together, these downward revisions to the City's largest General Fund revenue categories total approximately \$29 million from the levels included in the February 2008 Forecast. Many of the other economically sensitive revenue categories are projected to experience significant declines, including Transient Occupancy Taxes, Motor Vehicle In-Lieu, and Use of Money and Property (interest earnings). The revenue decreases in these areas more than offset the additional revenue of \$20 million estimated to be generated from the November 2008 ballot measures that created a permanent Telephone Tax to replace the Emergency Communication System Support Fee and reduced and modernized the Telephone Utility Tax.

On the expenditure side, several upward and downward adjustments have been incorporated into this Forecast. The most significant changes include the addition of costs associated with the phase-in of the City's share of the General Fund annual required contribution for retiree health care benefits, the addition of 25 new Police Officer positions each year through 2011-2012 per City Council direction, slightly lower than anticipated cost-of-living adjustments, lower utility and fuel costs, and lower debt service costs for City hall and the Airport West properties.

It does need to be noted that the projected General Fund shortfall for 2009-2010 does not factor in impacts from the four Development Fee Programs (Building, Fire, Planning, and Public Works). These programs are designed to be 100% cost recovery and have been programmed to have a neutral impact on the Forecast by adjusting the revenue and costs to be equal. In three of these programs, Building, Public Works, and Fire, there are gaps between the projected revenues and expenditures. The Administration will be working with the development community to develop recommendations to close these gaps through a combination of fee adjustments and cost reductions.

One-time funding of \$4.0 million from the 2009-2010 Future Deficit Reserve that was established per City Council policy as part of the 2007-2008 Annual Report and \$2.3 million from the Airport West Proceeds Reserve that was established with Airport West option payments in 2008-2009 is available for use in the 2009-2010 budget process. In addition, as of this writing, the \$15.3 million Economic Uncertainty Reserve remains intact.

It is also very important to reiterate that this forecast uses an incremental approach to each year's projection. Under this approach it is assumed that the budget is completely balanced on an ongoing basis in each year. To the extent that a shortfall in any one year is closed using one-time measures such as the reserves referenced above, the shortfall in the following year would be increased by that amount.

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

The incremental changes in this Forecast range from a deficit of \$61.2 million in 2009-2010 to a surplus of \$10.1 million in 2013-2014. Consistent with prior forecasts, expenditure growth continues to outpace revenue growth. In the last three years of the Forecast, the incremental shortfalls or surpluses are relatively small given the size of the City's budget. For instance, the incremental shortfall of \$4.9 million in 2011-2012 of the Forecast reflects less than 1% of the projected expenditures in that year of almost \$1 billion.

Caution is in order, however, when considering the significance of out-year projections. Given the decreasing level of precision to be expected in the later years of a multi-year forecast, the significance of the projections in the out years is not so much in terms of their absolute amounts, but rather in the relative size of the decrease or increase from the prior year. This information should be used to provide a multi-year perspective to budgetary decision-making, rather than as a precise prediction of what will occur. This is particularly the case in this Forecast given the extreme level of uncertainty regarding future economic performance and the absence of projected salary cost-of-living adjustments in the final three years of the Forecast.

General Fund Committed Additions

Cost estimates for a number of specific "Committed Additions" that address previous City Council direction are included in this Forecast in the years that they are projected to be required. The Committed Additions category, summarized in the chart below, primarily reflects projected additional funding required for retiree healthcare benefits, additional Police Officers, and operating and maintenance costs for new capital projects in the 2009-2013 Adopted Capital Improvement Program. The costs of the additions, which total \$34 million by the end of the Forecast period, are obviously a significant component of the City's projected General Fund deficits during these years.

2010-2014 General Fund Committed Additions

	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014
Additional Police Officers (25 positions/year through 2011-2012)	1,754,000	5,019,000	8,460,000	10,325,000	10,849,000
Retiree Healthcare Benefits	199,000	1,819,000	3,527,000	5,186,000	6,846,000
County Pocket Annexations (Transportation)	298,000	478,000	478,000	478,000	478,000
New Parks and Recreation Facilities Maintenance & Operations	130,000	1,048,000	1,619,000	1,925,000	2,107,000
New Traffic Infrastructure Assets Maintenance & Operations	204,000	397,000	550,000	649,000	749,000
Measure O (Library) Maintenance & Operations	773,000	4,088,000	5,164,000	5,529,000	5,557,000
Measure P (Parks) Maintenance & Operations	889,000	2,251,000	2,734,000	2,723,000	2,786,000
Measure O (Public Safety) Maintenance & Operations: Fire	9,000	507,000	2,610,000	2,693,000	2,763,000
Measure O (Public Safety) Maintenance & Operations: Police	749,000	1,808,000	1,865,000	1,895,000	1,928,000
Total	5,005,000	17,415,000	27,007,000	31,403,000	34,063,000

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

Two new Committed Additions have been added when compared to the February 2008 Forecast. (These additions were, however, factored into the November 2008 Forecast.) As approved by the City Council in the 2008-2009 Adopted Operating Budget, the addition of 25 Police Officers annually through 2011-2012 (75 total) is included in this category. The cost of these positions is projected at \$1.8 million in 2009-2010 based on a January 2010 start date in the academy (\$3.1 million full year cost) and is expected to increase to \$10.8 million by 2013-2014. A new Retiree Healthcare Benefits line item has also been added to reflect the phase-in over five years of the City's share of the General Fund annual required contribution for retiree healthcare benefits for non-Police Officers' Association (POA) employees. In 2009-2010, the costs are \$199,000 and grow to \$6.8 million by the fifth year of the forecast period. In addition to these amounts, the Forecast includes \$9.9 million over the five-year period (\$2.4 million in 2009-2010) in the Personal Services category consistent with the recently negotiated funding agreement for this liability with the POA. In total, additional funding of \$16.7 million is included in this Forecast to bring retiree healthcare benefits to full funding in the General Fund.

Operating and maintenance costs related to currently budgeted capital projects are expected to total \$2.8 million in 2009-2010 and increase to \$15.9 million by 2013-2014. Some of the larger facilities expected to come on-line during this forecast period include the South San José Police Substation; Fire Station 37 (Silver Creek/Yerba Buena Road), East San José Carnegie Branch Library, Santa Teresa Branch Library, Seven Trees Community Center and Branch Library, Happy Hollow Park and Zoo, and Bascom Library and Community Center. A detailed listing of all capital project operating and maintenance costs included in this 2010-2014 Preliminary General Fund Forecast can be found in the Committed Additions Section of this document.

General Fund Capital Operating and Maintenance Costs/ Budget Principle #8

Budget Principle #8 states that Capital Improvement Projects shall not proceed for projects with annual operating and maintenance costs exceeding \$100,000 without City Council certification that funding will be made available in the applicable year of the cost impact. Consistent with that direction, this Forecast includes a detailed list and discussion of capital projects that are underway or were previously approved by the City Council with annual operating and maintenance costs in the General Fund greater than \$100,000. Funding for these projects have been included as part of approved Capital Improvement Programs or Redevelopment Agency Budgets. The majority of these costs are associated with the voter-approved General Obligation bonds for Park, Library, and Public Safety facilities. The operating and maintenance costs for these facilities are included in the figures presented in this General Fund Forecast. In total, by 2013-2014, the annualized costs to operate and maintain the City Council/Agency Board approved facilities with annual operating and maintenance costs in the General Fund greater than \$100,000 are projected at \$14.4 million annually.

Four potential projects where funding has not yet been approved through the City Capital Improvement Program or Redevelopment Agency Capital Budget are under preliminary development. These projects, if approved, are anticipated to have an annualized operating and maintenance impact of at least \$2.3 million by 2013-2014. Consistent with the direction

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

approved as part of Budget Principle #8, for purposes of this Forecast, these operating and maintenance costs are not included as part of the General Fund Five-Year Forecast "Committed Additions" category. Under the budget principle, certification for these projects and other identified projects that have not been approved by the City Council will be sought as part of the 2010-2014 Proposed Capital Improvement Program. If certified by the City Council, the operating and maintenance costs associated with these facilities would then be included in subsequent General Fund Five-Year Forecast documents.

Alternative Forecast Scenarios

In order to model the range of financial scenarios possible under varying economic conditions, two alternative forecasts have been developed. "Optimistic" and "Pessimistic" cases have been created to model economic scenarios considered possible, but less likely to occur than the "Base Case". These alternatives are presented to provide a framework that gives perspective to the Base Case. The Base Case Forecast is still considered, however, the most likely scenario and is being used for planning purposes for the 2009-2010 Proposed Budget Operating Budget. It should be noted that the expenditure assumptions remain constant in each of these alternative scenarios.

The Optimistic Case differs from the Base Case in that it is one in which general economic conditions are more favorable than those assumed by the Base Case. In the Optimistic Case it is assumed that the economic stimulus package recently passed by Congress and the banking aid measures being undertaken by the Federal Reserve and the Treasury are more successful than anticipated. This leads to a quicker and more robust recovery. When compared to the Base Case scenario, the overall Gross Domestic Product (GDP) increases substantially, more jobs are created, and the unemployment rate is significantly lower. This results in higher collections in the economically sensitive categories, such as Property Tax and Sales Tax. By the end of the five-year period, revenues under this scenario would be \$44.5 million higher than in the Base Case. In the Optimistic Case, the City would experience deficits in the first two years of the Forecast of \$53.7 million and \$26.2 million, but would then have surpluses ranging from \$2.1 million to \$18.3 million per year in the remaining three years.

The Pessimistic Case, alternatively, attempts to model the potential outcome of a deeper, longer lasting recession. Under this scenario, the economic stimulus efforts are not able to stop the economic decline. The City's revenues, particularly Property Tax and Sales Tax, would be more severely impacted by the high unemployment rates, very low consumer confidence, low inflation, and falling home prices. By the end of the five-year period, revenues under this scenario would be \$65.0 million lower than in the Base Case. In the Pessimistic Case, there are annual deficits in the first four years of the Forecast ranging from \$7.3 million to \$73.0 million. In the last year of the Forecast, there is a small surplus of \$2.7 million.

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

Revenues/Expenditures Not Reflected in Forecast Model

It is important to note that there are a number of significant factors that may well impact the City's General Fund condition during the five-year period that are not reflected in this forecast model. These include the following:

- *Negotiated Labor Agreements:* The Forecast does not assume that the City will incur significant additional costs resulting from negotiations with some of the City's bargaining groups that exceed projections included in the Forecast as mentioned previously. It also presumes no increases in the final three years.
- *Retirement Rate Changes:* The retirement rates are updated based on biannual actuarial calculations and are expected to be adjusted in 2010-2011. Consistent with past practice, the new rates are not factored into the forecast until they are approved by the two retirement boards. Given the current market performance, it is assumed that the retirement rates will be increasing, probably significantly during the forecast period, to compensate for the lower earnings on investments. However, it should be noted that the retirement plans invest for long term benefits. The actuarial studies "smooth" or average market gains or losses over five years.
- *Unmet/Deferred Infrastructure and Maintenance Needs:* The annual ongoing General Fund costs for annual unmet/deferred infrastructure and maintenance needs are expected to reach \$29.5 million over the five-year period. This figure does not include the one-time backlog of approximately \$825 million, of which \$457 million is in the General Fund. These needs are included in the General Fund Structural Deficit definition and will be considered as part of the planning efforts to reduce the structural deficit.
- *State Budget Actions:* The Forecast does not assume any financial impact from State budget balancing actions that may negatively impact the City.
- *County Annexations:* The impact on revenues and expenditures associated with the annexation of County properties into San José is not fully reflected in this Forecast model. The Forecast currently includes the transportation maintenance costs for the annexed areas.
- *North San José Expansion:* The overall impact on revenues and expenditures that may develop from the expansion of North San José are not reflected.
- *San Jose Redevelopment Agency Funding:* If the San Jose Redevelopment Agency reaches its funding cap and is no longer able to fund eligible City support services, the revenues and expenditures associated with these activities will be adjusted downward. Because it is unlikely that the City will be able to reduce all expenditures reimbursed by the Agency, such as funding for a portion of the Mayor and City Council and the Office of Economic Development, there could potentially be a net loss to the General Fund.
- *One-Time Revenues/Expenses:* Because the Forecast compares ongoing revenues and expenditures, it does not factor in one-time funding sources, such as the 2009-2010 Future Deficit Reserve, or one-time expenditure needs.

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

General Fund Structural Deficit Elimination Plan Update

At the direction of the City Council, the City Manager released the General Fund Structural Deficit Elimination Plan (Plan) in November 2008. This Plan outlined specific strategies and timelines to eliminate the General Fund structural budget deficit over a five year timeframe ending in fiscal year 2013-2014. The Plan was based on revenue and expenditure projections as of the November 2008 Preliminary General Fund Forecast and included input from the General Fund Structural Deficit Elimination Plan Stakeholder Group that convened in the summer of 2008. The original Plan, which described the projected shortfall and potential solutions, was discussed at a City Council Study Session on December 5, 2008.

In this document, the Plan has been updated to reflect revised revenue and expenditure projections in the final 2010-2014 General Fund Forecast. Based on these revised projections, the General Fund structural deficit is expected to total approximately \$116 million over a five-year period as shown in the table below:

2010-2014 General Fund Structural Deficit Projection (February 2009)
 (\$ in Millions)

	2009-2010	2010-2011	2011-2012*	2012-2013*	2013-2014*	Total
Projected Base Shortfall (Feb 2009 Forecast)**	(\$61.2)	(\$36.7)	(\$4.9)	\$6.5	\$10.1	(\$86.2)
Unmet/Deferred Infrastructure & Maintenance Needs***	(\$5.9)	(\$5.9)	(\$5.9)	(\$5.9)	(\$5.9)	(\$29.5)
Total Incremental Deficit	(\$67.1)	(\$42.6)	(\$10.8)	\$0.6	\$4.2	(\$115.7)
Total Cumulative Deficit	(\$67.1)	(\$109.7)	(\$120.5)	(\$119.9)	(\$115.7)	(\$115.7)

* Funding for cost-of-living salary increases not factored into the last three years of the Forecast. These increases are being treated as a resource allocation policy decision.

** Includes City's share of General Fund annual required contribution for retiree health care benefits and committed additions previously agreed upon by Council, such as addition of 25 officers annually through 2011-12 and operating and maintenance funding for capital projects coming on line.

*** Does not address one-time needs of \$457 million in the General Fund (\$825 million all funds).

A combination of cost savings strategies, revenue strategies, and service reductions/eliminations strategies has been identified to address the General Fund structural deficit. The existing strategies were refined based primarily on updated Forecast information and additional analysis. A number of new strategies have also been identified for incorporation into the 2009-2010 budget process or the November 2009 update to the General Fund Structural Deficit Elimination Plan, as appropriate.

These strategies identified in the plan will serve as a blueprint to guide the 2009-2010 General Fund budget balancing efforts and will be refined in the future to reflect the approved 2009-2010 budget actions, new information, and further analysis.

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

Capital Revenue Forecast

Section Five of this report describes the 2010-2014 Capital Budget Revenue Forecast that will be used to formulate several major elements of the Capital Improvement Program (CIP). As in past years, the construction-related revenue estimates included in this report are derived from construction activity projections provided by the Planning, Building and Code Enforcement (PBCE) Department and an analysis of actual collection patterns. The projections and their basis are described in a report prepared by PBCE, which is included as Appendix A of this document (Development Activity Highlights and Five-Year Forecast [2010-2014]). This activity forecast includes a review of specific projects that are in progress, as well as a general prediction of expected levels of new construction.

The following table compares the estimates for the economically sensitive capital revenue categories included in this Five-Year Forecast with those included in the 2009-2013 Adopted CIP. As can be seen, reflecting the current dismal financial conditions, revenue estimates are down significantly in all categories.

Forecast Comparison Summary
 (\$ in Thousands)

	2009-2013 CIP	2010-2014 Forecast	Difference	% Change
Construction and Conveyance (C&C) Tax	121,000	106,000	(15,000)	(12%)
Building and Structure Construction Tax	48,396	39,500	(8,896)	(18%)
Construction Excise Tax	70,026	43,000	(27,026)	(39%)
Residential Construction Tax	990	600	(390)	(39%)
Sanitary Sewer Connection Fee	5,599	3,750	(1,849)	(33%)
Storm Drainage Connection Fee	1,903	1,050	(853)	(45%)
TOTAL	247,914	193,900	(54,014)	(22%)

Real estate activity (primarily housing resales) determines the collection level of one of the major capital revenue sources, the Construction and Conveyance (C&C) Tax. The continued slowdown in the local and national real estate market continues to impact collections. While overall transactions have risen, the severe drop in the median home price continues to weigh on projected revenues in this category. Declines in Construction and Conveyance Tax revenues were predicted in the development of the 2009-2013 Forecast, however, recent information (December 2008 decline of 35% and January 2009 decline of 32%) indicates that collections have dropped even further than previously anticipated, and likely will not improve in the near-future. Through January 2009, collections have dropped in 30 of the past 33 months when comparing to collections in the same month of the prior year. As a result, in this Forecast, this category is projected to generate \$106 million over the next five years, a decrease of \$15 million from the estimates assumed in the 2009-2013 Adopted Capital Improvement Program (CIP). The average annual collection level of \$21.2 million projected in the 2010-2014 Forecast is also

2010-2014 FIVE-YEAR FORECAST AND REVENUE PROJECTIONS (CONT'D.)

well below the actual collection levels in recent years that reached a peak of \$49 million in 2005-2006, but is expected to drop to \$19 million in 2008-2009.

The remaining five economically sensitive capital revenue categories are directly linked to development activity. Based on projections provided by the Planning, Building and Code Enforcement Department, construction activity valuation is projected to drop considerably over the next couple of years and recover slightly to \$750 million. These assumptions are significantly reduced from the levels presented in the 2009-2013 Forecast. Construction activity peaked in 2000-2001 at \$1.9 billion, followed by a sharp decline that reached a low point of \$818 million in 2003-2004. From that low point, a modest recovery occurred in 2004-2005 with growth of 14% in that year. However, in 2005-2006, construction activity dipped again, to \$828 million, primarily due to a fall off of multi-family development to a ten-year low. A modest rebound driven primarily by commercial and industrial development and residential high rise construction in the downtown area occurred in 2006-2007. Due to a slowdown in residential construction, 2007-2008 experienced a 9% decline and is expected to decline an additional 8% in 2008-2009 with total projected valuation of \$775 million. This activity is then expected to bottom out at \$650 million in 2009-2010 and recover to \$725 million in 2010-2011 before flattening out in 2011-2012 at \$750 million. Based on the construction activity estimates and a review of revenue collection patterns, a decrease in construction-related taxes and fees of \$54 million, or 22%, is expected when comparing the 2010-2014 Forecast to the 2009-2013 Adopted CIP estimates.

NEXT STEPS

The next major steps in the budget development process include the following:

March 2009

- 2009-2010 Mayor's March Budget Message released with public hearing and amended/approved by City Council.

April 2009

- 2009-2010 Proposed Capital Budget and 2010-2014 Capital Improvement Program released.

May 2009

- 2009-2010 Proposed Operating Budget and 2009-2010 Proposed Fees and Charges released.
- City Council Study Sessions and initial Public Hearing on 2009-2010 Proposed Operating Budget, 2010-2014 Proposed Capital Budget and Capital Improvement Program, and 2009-2010 Proposed Fees and Charges.

June 2009

- 2009-2010 Mayor's June Budget Message released and amended/approved by City Council.
- 2009-2010 Operating Budget, 2009-2010 Capital Budget and 2010-2014 Capital Improvement Program, and 2009-2010 Fees and Charges adopted by City Council.

CONCLUSION

This document compares the projected revenues and expenditures for the General Fund over the next five years as well as provides estimates for some of the key revenues that support the City's Capital Program. The estimated 2009-2010 General Fund deficit of \$61 million is obviously significant and will clearly necessitate very difficult choices in order to bring projected revenues and expenditures into balance.

The Budget Request and Forecast are being released in the midst of one of the worst recessions in history and there are no signs of improvement. In fact, recent economic indicators continue to show further deterioration of the economy. It is anticipated that this deep and global recession will continue through all of 2009 and likely beyond. Some of the impacts of this recession will continue to impact City revenues well beyond that timeframe. In particular, the weakness in the real estate market is expected to impact Property Tax receipts for several years. There is also a significant amount of uncertainty regarding the length and depth of this recession, which makes long-term forecasting difficult.

The revenue and expenditure projections for the 2009-2010 fiscal year will continue to be refined over the next couple of months as additional information becomes available. This is particularly important in the areas of Sales Tax and Property Tax. Sales Tax data for the second quarter of 2008-2009, which covers the 2008 holiday period and will reflect the impacts of economic activity which nationally was down by the largest percentage (6.2%) seen in 25 years, will be received in March 2009. Based on this additional data, any necessary adjustments will be incorporated into the 2009-2010 Proposed Operating Budget. Similarly, based on the timing of the Property Tax data which will indicate the impact of the widespread re-examination of residential property values now being undertaken by the County Assessor, additional adjustments may also have to be factored into the 2009-2010 Adopted Operating Budget.

Given the scope of the fiscal challenges that the City faces, it is important that we remain committed to the sound fiscal policies and practices that have served the City well in the past. A combination of strong leadership from the Mayor and City Council, collaboration with the many stakeholders, and a strategic approach to determining how to scale back the organization based on the available resources will be necessary in order to prepare a 2009-2010 budget that will both preserve our fiscal integrity and meet the most critical needs of the residents and businesses we serve. Discipline and focus will be needed to align the City's limited resources with the highest value and priority needs.



Debra Figone
City Manager

ELEMENTS OF THE GENERAL FUND FORECAST

ASSUMPTIONS REGARDING THE ECONOMIC ENVIRONMENT

Overview

This document provides three alternative Five-Year Forecast scenarios for General Fund revenues and expenditures: Base Case, Optimistic Case, and Pessimistic Case. The Base Case is considered the most likely projection and that which the Administration recommends be used to formulate the 2009-2010 Proposed Operating Budget. Given the uncertainties inherent in any five-year forecast, however, two alternative case forecasts for the General Fund are also provided. These scenarios attempt to model the potential impact of more optimistic and pessimistic views of the future economic environment. Given the severity of the economic downturn and the volatility in the global economic conditions, it is obviously even more difficult than usual to predict economic performance in the coming year and certainly over the next five years.

- ❑ **Base Case** – The Base Case forecast is built on the assumption that the deep global recession will continue to impact economic performance through 2009. The impact on this region, however, is expected to be somewhat less severe than in other regions in California and the nation as a whole. In the out years of the Forecast, the economy is expected to slowly recover, resulting in slow growth in General Fund revenue collections over the forecast period.
- ❑ **Optimistic Case** – In the Optimistic Case, it is assumed that the economic stimulus package recently passed by Congress and the banking aid measures being undertaken by the Federal Reserve and the Treasury are more successful than anticipated. This leads to a quicker and more robust recovery. When compared to the Base Case scenario, the overall Gross Domestic Product (GDP) increases substantially, more jobs are created, and the unemployment rate is significantly lower. This results in higher collections in the economically sensitive categories, such as Property Tax and Sales Tax.
- ❑ **Pessimistic Case** – The Pessimistic Case, alternatively, attempts to model the potential outcome of an even deeper, longer lasting recession. Under this scenario, the economic stimulus efforts are not able stop the economic decline. The City’s revenues, particularly Property Tax and Sales Tax, would be more severely impacted by the high unemployment rates, very low consumer confidence, low inflation, and falling home prices.

Base Case Forecast

As with all forecasts, this one is based on a series of assumptions regarding the overall economic environment, now and in the future. These assumptions were reached after reviewing the projections included in a number of economic forecasts. The economic conditions and the projected impacts on City revenues will continue to be closely monitored and any new developments will be factored into the City Manager’s 2009-2010 Proposed Operating Budget, scheduled to be published on May 1, 2009.

ELEMENTS OF THE GENERAL FUND FORECAST

ASSUMPTIONS REGARDING THE ECONOMIC ENVIRONMENT (CONT'D.)

Base Case Forecast (Cont'd.)

The following is a discussion of both the national and local economic outlooks used to develop the revenue estimates for the Base Case Forecast. Various economic forecasts are reviewed in the development of the revenue estimates, including the national and State economic forecasts produced by the Anderson School of Management at UCLA. The City also uses an economic forecasting consultant to assist in the development of this forecast, particularly the modeling of the growth in the out years of the Forecast.

Current National Conditions

Currently, the U.S. economy is declining at an alarming rate. While the economic performance in the first three quarters of 2008 were already very weak, the last quarter of 2008 was one of the most dismal in decades. The 6.2% drop in the Gross Domestic Product (GDP) in the fourth quarter of 2008 was the worst decline in 25 years. On a national level, total non-farm payroll jobs fell by 2.6 million in 2008, the largest job loss total since 1945. The majority of these job losses occurred in the last four months of the year. (Source: Bureau of Labor Statistics). The unemployment rates at the national, State and local levels also increased by approximately 50% from December 2007 to December 2008. Given the alarming deterioration of the economy at the end of the year, the Conference Board Consumer Confidence Index fell to a new all-time low in December 2008 (Index began in 1967).

In the first quarter of 2009, the news continues to get worse as the economy continues its downward spiral. In January 2009, U.S. employment fell sharply with the loss of almost 600,000 jobs and an increase in the unemployment rate from 7.2% to 7.6%. The California unemployment rate reached double-digit levels in January of 10.1%, the highest rate since June 1983. At the end of February, the Dow Jones Industrial average was at its lowest point since May 1, 1997. The 11.7% decline in the Dow in February 2009 was the worst decline for that month since February 1933, which had a decline of 15.6%. The Conference Board Consumer Confidence Index also reached new all-time lows in both January and February 2009.

Prior to fall 2008, housing was the leading cause of the decline with home construction, resales, and prices falling at rates not seen since the end of World War II. In the fall of 2008, a new dimension was added to the crisis with the abrupt decline in the fortunes of major U.S. investment banks, JP Morgan, Morgan Stanley, Lehman Brothers and others. The world banking system has essentially frozen up with virtually no lending taking place. The unprecedented actions taken by American regulators and the Treasury Department seem to have averted for the moment a financial catastrophe. However, the loss to the American financial system has been significant. All of the large American investment banks are either out of business, part of another bank, or have transformed themselves from investment to commercial banks.

The recent decline in energy prices is one of the only positive trends in today's economy. The decline in the price of oil from the mid-\$100 dollar range to the current \$40-\$50 range is adding almost \$400 billion dollars of additional spending power to the American consumers. But even this extremely large increase in spending power has been overshadowed by spending drops

ELEMENTS OF THE GENERAL FUND FORECAST

ASSUMPTIONS REGARDING THE ECONOMIC ENVIRONMENT (CONT'D.)

Base Case Forecast (Cont'd.)

Current National Conditions (Cont'd.)

resulting from the onslaught of job losses, the loss of equity in real estate and equity investments, and the overall loss of consumer confidence.

The National Economic Outlook

The severe economic recession is expected to continue through at least 2009, with high unemployment, a decline in GDP, and extremely low consumer confidence levels. It is hoped that economic performance will show some signs of improvement in 2010, if the immense fiscal stimulus efforts begin yielding results. Many economists are beginning to worry, however, that the economic recession may linger well into 2010. As a consequence of the stimulus and accompanying decline in federal tax revenues, the federal budget deficit is expected to exceed \$1 trillion in 2009.

The unemployment rate is expected to remain high into 2010. From that point, the economy is expected to be on a path of recovery. However, the recovery will not be a fast one and the economy will remain weak for many years into the forecast period. In the later years of the Forecast, the U.S. GDP is projected to experience more historical rates of growth. Inflation is also expected to remain low through 2010, increasing only in the out years of the Forecast.

Energy prices are expected to remain moderate as the decline in demand for fuel brought on by the recession will help curb price increases. In the longer run, conservation programs, higher mileage and alternative fuel vehicles will help to moderate price increases as the economy begins to regain its footing.

Current Santa Clara County Economic Conditions

With the dot-com collapse in the last recession, Silicon Valley was one of the first and most deeply impacted regions in the nation. This has not been the case in this recession. Until the last quarter of 2008, Silicon Valley was somewhat less impacted than other areas in the State and the nation. However, this deep global recession has now enveloped this region as well, as evidenced by increasing job losses, rising unemployment, steep declines in home prices, rising foreclosures, and rising commercial vacancy rates.

In 2008, a total of 11,000 jobs were lost in the San José Metropolitan Statistical Area, the largest decline since the high-tech bubble crash in the early part of this decade. Several large high-tech companies have announced significant layoffs and more are expected in the upcoming months.

ELEMENTS OF THE GENERAL FUND FORECAST

ASSUMPTIONS REGARDING THE ECONOMIC ENVIRONMENT (CONT'D.)

Base Case Forecast (Cont'd.)

Current Santa Clara County Economic Conditions (Cont'd.)

Unemployment Rate (Unadjusted)

	Dec. 2007	Nov. 2008	Dec. 2008
San José Metropolitan Statistical Area	5.1%	7.2%	7.8%
State of California	5.9%	8.3%	9.1%
United States	4.8%	6.5%	7.1%

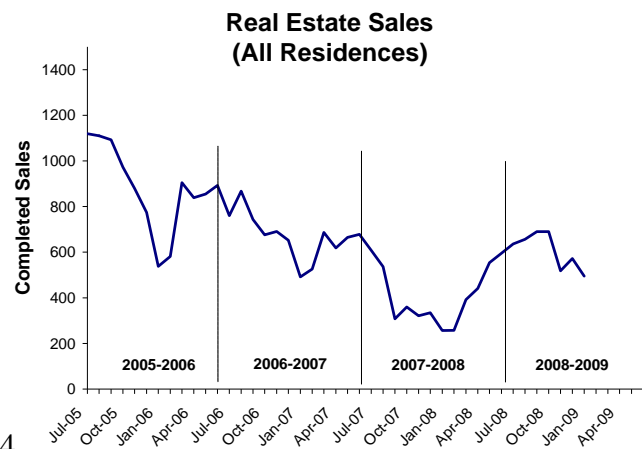
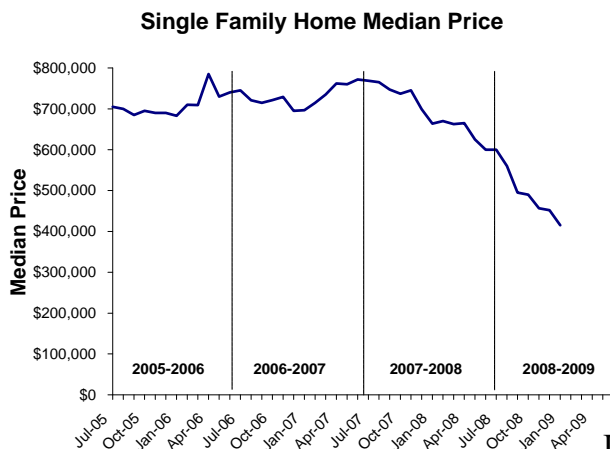
The unemployment rate in the San José metropolitan area continues to increase with a rate of 7.8% in December 2008. This figure is up significantly from 5.1% a year ago. When comparing the December 2008 unemployment rate in this region with the State and the nation, this area fares better than the State that had an

Source: California Employment Development Department

unadjusted unemployment rate of 9.1%, but is slightly worse than the nation, which had an unadjusted unemployment rate of 7.1%. As of this writing, January 2009 unemployment data for the nation and California has been released. The U.S. unemployment rate (not seasonally adjusted) increased again to 8.5% and the unadjusted rate for California reached double-digit levels at 10.6%.

Real estate performance in Santa Clara County remains extremely weak with a significant increase in the number of foreclosures. In the last quarter of 2008, approximately 3,000 San José homes received a new foreclosure filing. At this point, approximately 1.7% of the home ownership units are in some state of foreclosure. The vacancy rates for office space in San José also increased over 60%, from 10.8% in the fourth quarter of 2007 to 17.5% in the fourth quarter of 2008.

Following the nation-wide trend, local home prices have declined sharply over the last year. The median home price for single family homes within San José dropped an unprecedented 35% from \$699,000 in December 2007 to \$452,000 in December 2008. In January 2009, this figure fell further to \$415,000, the lowest level since January 2000. With the home prices dropping significantly, there has, however, been a corresponding increase in the number of sales. In January, the property transfers for all types of residences were up 92% from the extremely low level experienced in January 2008.



ELEMENTS OF THE GENERAL FUND FORECAST

ASSUMPTIONS REGARDING THE ECONOMIC ENVIRONMENT (CONT'D.)

Base Case Forecast (Cont'd.)

Santa Clara County Economic Outlook

The local economy is also expected to continue to face significant challenges through the remainder of the year. On an overall basis, this region's economy is expected to contract sharply in 2009.

For the near-term forecast period, local employment levels are expected to continue to decline in 2009 and the unemployment rate will continue to track well over 7%. After 2009, it is hoped that if the federal stimulus package has its intended effect and the general economy begins to recover, employment numbers would begin to grow again and the unemployment rate should start to decline. For most of the remainder of the forecast period, job growth in the County is expected to be lower than the historical norm, but will be positive.

Both consumer and business spending are also expected to be weak in 2009. The record lows in consumer confidence, the declines in real estate values, the volatility in the stock market, and the credit crunch in the financial markets are all factors that have and will continue to drive down spending. This region, however, does benefit greatly from the innovative nature of its companies, from the start-ups to the well-established businesses. While the County's high-tech companies have been impacted by the deep global recession, the products developed by these companies are expected to remain in demand over the forecast period. The world is also in the process of shifting to new "green" technologies and energy alternatives. Silicon Valley is potentially a leader in both of these fields.

In 2009, home prices are expected to continue to fall, significantly impacting the City's Property Tax receipts in the early years of the Forecast. Home prices are expected to begin to show some growth after 2009; but the rate of increase will be somewhat muted by an expected rise in interest rates that will make it a bit more difficult for prospective buyers to purchase a home. Still, home prices should continue to rise through the rest of the forecast horizon as both employment and incomes gain traction as we move through the forecast years.

In summary, the severe economic recession is expected to continue to impact economic performance in 2009-2010, with lingering impacts in 2010-2011. In the last three years of the Forecast, the resumption of modest revenue growth is anticipated.

Optimistic and Pessimistic Scenarios

As discussed above, all forecasts are burdened with a large degree of uncertainty, which increases going further into the future. As a result, in addition to the Base Case, two alternate, but plausible, revenue forecast scenarios are also presented in this document: an Optimistic Case and a Pessimistic Case. These alternatives were developed to display the range of possible outcomes over the next five years under varying economic conditions. The Base Case is, however, still considered the most likely outcome. Following is a discussion of these scenarios.

ELEMENTS OF THE GENERAL FUND FORECAST

ASSUMPTIONS REGARDING THE ECONOMIC ENVIRONMENT (CONT'D.)

Optimistic and Pessimistic Scenarios (Cont'd.)

Optimistic Case

In the Optimistic Case, the economic stimulus package recently passed by Congress and the banking aid measures being undertaken by the Federal Reserve and the Treasury are more successful than anticipated. With a more robust recovery, overall GDP will increase substantially above that of the Base Scenario. Along with it, many more jobs will be created and the unemployment rate will fall.

One slightly negative aspect of a more robust recovery is that it becomes more likely that inflation will be higher as well. With higher inflation, interest rates, particularly mortgage rates, will increase. For this scenario however, it is assumed that the increases in interest rates are not sufficient to derail the recovery. Interest rates are currently very low and there is sufficient room on the upside for them to increase in this scenario without unduly harming the recovery.

The real estate market improves significantly in this scenario. Both the quantity of home sales and the housing prices rise at a quicker rate than in the Base Case, resulting in higher Property Tax receipts. The number of homes reassessed downwards for Property Tax purposes under the Proposition 8 requirements also decline. In addition, the Proposition 13 mandated inflation adjustment reaches the maximum of 2% in all of the forecast years. With these adjustments, property taxes rise above the Base Scenario in all of the forecast years.

General increases in inflation, employment, and consumer attitudes promote increased spending, which generate Sales Tax for the City. Car sales could be expected to rebound from the dismal performance experienced in 2008. Development activity is also expected to improve. Higher energy prices increase Utility Taxes and Franchise Fees as well. By the end of the Forecast period, revenues are \$45 million above the Base Case.

Pessimistic Case

The Pessimistic Scenario is one in which the economic stimulus efforts are not able to curb the economic decline. The economy simply does not respond sufficiently to keep it from falling into an even deeper recession. This scenario would have an immediate and longer lasting negative impact on City revenues.

In this scenario, the economy is declining rapidly, which drives down inflation. For the first several years, prices for goods and services are actually forecast to fall before recovering very late in the forecast cycle. Home prices also continue to fall, resulting in significantly lower Property Tax receipts. The downward property reassessments under Proposition 8 continue to severely impact Property Tax collections. In addition, low inflation means that the Proposition 13 inflation adjustments fall below the 2% level. Property taxes fall for the first three years of this forecast before finally hitting the lowest point in the fourth year.

ELEMENTS OF THE GENERAL FUND FORECAST

ASSUMPTIONS REGARDING THE ECONOMIC ENVIRONMENT (CONT'D.)

Optimistic and Pessimistic Scenarios (Cont'd.)

Pessimistic Case (Cont'd.)

Sales Tax receipts are also significantly lower in this scenario. The very high unemployment rates and very low consumer confidence combine with falling prices to reduce Sales Taxes in the first two years of the Forecast. The other economically sensitive revenues are also expected to fall in this scenario. Gasoline Taxes, however, rise slightly because these per unit taxes are positively affected by the forecast for lower oil prices that result in higher gasoline consumption. By the end of the Forecast period, total revenues are \$65 million below the Base Case.

Impact of Forecasted Economic Conditions on Revenue Collections

The economic conditions discussed above are the primary drivers for the economically sensitive revenues, with the most significant impacts in the Sales Tax and Property Tax categories. Performance in other areas, however, is primarily driven by other factors. For example, the Utility Tax and Franchise Fee categories are more heavily impacted by utility rate changes and energy prices. Collections in the Fines, Forfeitures, and Penalties category remain relatively flat under all economic conditions, while collections from local, State, and federal agencies are primarily driven by the grant and reimbursement funding available from these agencies. As a result, the General Fund experiences no significant net gain or loss in times of an economic expansion or slowdown, respectively. Because these revenue sources do not track directly with the performance of the economy, the growth in these areas, even in times of economic strength, can hold down the City's overall revenue growth. Conversely, in an economic slowdown, these categories can act as a buffer, easing the impact of drops in the economically sensitive categories.

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST

An in-depth analysis of the General Fund revenue categories was completed to develop the 2009-2010 revenue estimates included in this Forecast. Over 500 revenue sources were examined to estimate the outcome in 2008-2009 and, building upon those projections, to develop the 2009-2010 revenue estimates. These revenue estimates will be closely examined and updated again during the preparation of the 2009-2010 Proposed Operating Budget.

As displayed in the Forecast, revenues (exclusive of Beginning Fund Balance) are shown to increase from \$774.5 million in 2009-2010 to \$862.5 million in 2013-2014, for an average growth rate of 2.84% per year. This is slightly above the average growth rate presented in the February 2008 Forecast (2.78%). It is important to note, however, that the relatively low growth rate in the last forecast was due, in part, to the scheduled sunseting of the Emergency Communications System Support (ECSS) Fee in 2009-2010. This is not, however, a factor in this forecast due to the replacement of the ECSS Fee with a voter-approved Telephone Tax. The low growth rate in this Forecast is due primarily to the low projected growth of only 1.34% in 2010-2011, reflecting the lingering impact of the economic downturn as well as the phase-out of a number of transfers and reimbursements.

Understanding the basis for the revenue estimates included in this Forecast requires discussion of the assumptions used for estimating each of the revenue categories. The following discussion focuses on estimates used for the 2009-2010 General Fund Forecast.

Property Tax

Property Tax receipts of \$207.9 million are projected for 2008-2009, which represents growth of 2.0% over the prior year. This growth reflects increases in both the Secured and Unsecured categories, offset by a decrease in the SB 813 (property resales) collection area. In 2009-2010, collections are expected to remain relatively flat with an estimate of \$207.8 million. Additional information about each of the Property Tax sub-categories is provided below.

Secured Property Taxes account for approximately 90% of the revenues in this category. In 2008-2009, Secured Property Tax receipts are expected to reach \$191.2 million, an increase of 4.2% over the prior year. These receipts are based on real estate activity through January 1, 2008. The 2009-2010 Secured Property Tax levy will be based on real estate activity through January 1, 2009. The residential real estate market experienced a significant slowdown in 2008, with a 35% drop in the median sales price. Based on the significant drop in home prices, the Santa Clara County Assessor's Office will be evaluating property sales that have occurred since 2000 for potential reassessment. This includes the review of almost 42,000 single family homes in San José, or 20% of the total. The impact of these reassessments is not yet known.

It is currently estimated that very low Secured Property Tax growth of only 1% will be realized in 2009-2010, bringing the estimate to \$193.1 million. It should be noted that final data on the actual tax levy for 2009-2010 is not available as adjustments are made through July 1, 2009. It is anticipated that initial information on the impacts of the Property Tax reassessments will not be available until May 2009, after the release of the 2009-2010 Proposed Operating Budget. If

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Property Tax (Cont'd.)

necessary, refinements to the Property Tax estimates will be brought forward in the Proposed Budget review process.

Unsecured Property Taxes are the second largest revenue source in this category. Growth in this category is driven primarily by increases in the value of personal property (e.g. equipment and machinery used by business and industry for manufacturing and production). During the last decade, performance in this category has been extremely volatile with annual growth or declines reaching double-digit levels based primarily on the strength of the local business sector. In 2008-2009 collections in this category are expected to reach \$11.1 million, which is consistent with 2007-2008 actual receipts. Given the severe economic downturn, collections are expected to decrease 10.0% in 2009-2010 to \$10.0 million.

SB 813 Property Taxes (supplemental taxes) represent payments for taxes owed on recent housing resales. With the significant drop in housing prices, SB 813 Property Tax receipts are expected to fall 45% from \$7.9 million in 2007-2008 to \$4.4 million in 2008-2009. Collections are projected to fall an additional 20% to \$3.5 million in 2009-2010 based on the assumption that the housing market will continue to experience steep declines through 2009-2010.

All other property taxes (Homeowners Property Tax Relief and Agricultural Tax Relief) are assumed to have little or no growth in 2009-2010, consistent with historical trends.

In the out years of the Forecast, annual Property Tax performance is expected to range from a decline of 1.5% in 2010-2011 to an increase of 5.0% in 2013-2014. These projected growth rates are far below those experienced in recent years and reflect the impact of the significant drop in housing prices. This is the first time in memory that Property Tax collections are projected to actually decline in one of the years of the Forecast.

Sales Tax

The Sales Tax category includes General Sales Taxes and Proposition 172 Sales Taxes. Overall, collections are expected to decrease 5.0% in 2008-2009 to \$146.3 million and an additional 5.0% in 2009-2010 to \$139.0 million.

The forecast for the General Sales Tax revenue estimate assumes collections of \$142.0 million in 2008-2009, a decrease of 5.0% over the 2007-2008 collection level of \$149.5 million. This reflects actual performance for the first quarter of 2008-2009 (decline of 0.4%) and the assumption that a decline 6.5% will be realized in each of the remaining three quarters of the fiscal year. The rapidly deteriorating economy is expected to negatively impact receipts through 2008-2009 and into next fiscal year.

Collections in all sectors are expected to be impacted. With the dismal holiday season, high unemployment, and record-setting lows in consumer confidence, the retail sector is expected to be very weak. The global economic recession and the lack of a credit market will affect the

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Sales Tax (Cont'd.)

business-to-business sector. Large declines are also projected in the transportation sector that has experienced a steep decline from automobile sales as well as the decline in gas prices. For 2009-2010, General Sales Tax receipts are expected to fall an additional 5.0% to \$134.9 million. It is assumed that the economy will continue to stall through the first half of the fiscal year and improve only slightly in the second half.

Proposition 172 Sales Tax collections (representing the one-half cent tax that is allocated to counties and cities on an ongoing basis for the use in funding public safety programs) are expected to total \$4.3 million in 2008-2009, which represents a decline of 5.0% from the actual 2007-2008 collections of \$4.5 million based on activity through the first seven months of 2008-2009. In 2009-2010, collections are projected to fall an additional 5.0% to \$4.1 million.

Through the remaining years of the Forecast, Sales Tax performance is expected to improve, with growth ranging from a low of 3.84% in 2010-2011 to a high of 4.85% in 2013-2014.

Departmental Charges and Other Licenses

The Departmental Charges and Other Licenses categories contain fees and charges collected by various departments. The most significant revenue sources are the construction and development-related fees. Revenue collection levels are projected based on City Council-approved cost-recovery policies with the goal of a net-zero impact on the General Fund.

When developing the forecast estimates for these categories, the revenues are generally set at the anticipated collection levels. For 2009-2010, the development-related revenues are expected to be very weak, continuing the dismal performance experienced in 2008-2009. In cases where the development-related revenues are projected to exceed costs, the impacted departments will need to develop budget proposals for incorporation into the 2009-2010 Proposed Operating Budget to increase resources to meet the service demands or to reduce fees. Conversely, if the projected revenues are not sufficient to cover the base costs, departments will be submitting proposals to reduce costs and/or increase fees to bring projected revenues and expenditures back in line for a net-zero General Fund impact. For 2009-2010, the Building, Public Works, and Fire Fee Program revenues are projected to be below the base costs, which will require budget actions to bring these programs in balance.

For the non-development-related fees and charges, the 2009-2010 estimates are based on current collection trends. In the out years of the forecast, both the Departmental Charges and Other Licenses categories are expected to experience growth of 3.4% in 2010-2011 and 1.4% in each of the remaining years of the Forecast. The growth rates in the out years are tied to the expected increases in costs for which the fees are designed to recover. It should be noted that cost-of-living salary adjustments have not been factored into the last three years of the Forecast. There are currently no negotiated agreements for that period.

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Business License Tax

This category includes General Business License Tax and Disposal Facility Tax. In 2008-2009 General Business Tax proceeds are expected to reach only \$12.3 million, which is well below the Adopted Budget estimate of \$13.3 million. The severe economic downturn has impacted the number of businesses as well as the staffing levels, which directly impact Business Tax receipts. In 2009-2010, collections are projected to drop to \$12.0 million to reflect the loss of revenue associated with the Business Discovery Program, which was funded on a one-time basis in 2008-2009.

In the Disposal Facility Tax category, collections are estimated at \$13.2 million in 2008-2009, a decrease of 5.3% from the 2007-2008 collection level. Receipts are expected to fall an additional 2.0% to \$12.9 million in 2009-2010 as a result of the economic downturn and continued recycling efforts.

In the remaining years of the Forecast, the Business License Taxes category is expected to experience very minimal growth of less than 1% per year.

Money and Property

This category consists primarily of interest income. The 2009-2010 estimate for interest earnings in the General Fund and for the other funds where earnings are transferred to the General Fund assumes an average interest rate of only 2.06%, applied to an average cash balance of approximately \$180 million for a total collection level of \$3.7 million. This forecast reflects a significant decline in both the average cash balance (down from \$240 million) and the average interest rate yield (down from 3.41%) adopted in 2008-2009. The decline in the cash balance is primarily the result of change approved in 2008-2009 to prepay the City's contribution to its two retirement plans at the beginning of each fiscal year in an effort to maximize the earnings from these plans and reduce the City's contribution rates to the system. The lower interest yield projection, which was provided by the Finance Department, reflects the impact of the current economic conditions.

Interest from other sources, such as capital and special funds, have been adjusted to reflect the various impacts of expected activity, fund balance levels, and interest rate yields in 2009-2010. Interest earnings from these sources are expected to generate \$3.2 million in 2009-2010. An additional \$1.0 million is expected to be generated from the remaining sources in this category, including subrogation recovery funds, and the rental of facilities. In the out years of the Forecast, increases ranging from 2.01% to 2.61% are projected.

Motor Vehicle In-Lieu

In 2008-2009, Motor Vehicle In-Lieu collections are expected to reach only \$3.0 million, a significant drop from the \$4.1 million received in 2007-2008. In 2009-2010, collections are expected to drop an additional 7.8% to \$2.8 million. This reflects the 23% drop in new car and light truck registrations experienced in 2009 and an additional 15% projected drop in 2009, with

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Motor Vehicle In-Lieu (Cont'd.)

some relief expected by 2010 (California Auto Outlook, January 2009). In the out years of the forecast, small changes ranging from a decrease of 0.33% in 2010-2011 to an increase of 0.90% in 2013-2014 are anticipated.

Federal Revenue

The Federal Revenue category consists of grant revenues. Two grants are anticipated in 2009-2010: the Senior Companion Program grant (\$130,000); and the Retired and Senior Volunteer Program (RSVP) grant (\$92,000).

Other State Revenue

The Other State Revenue category includes the Aircraft In-Lieu payments, State grant revenues, and other State reimbursements. The Aircraft In-Lieu payment is expected to reach \$4.6 million in 2008-2009, a decline 10.9% from the 2007-2008 receipts of \$5.2 million. In 2009-2010 collections are expected to decline an additional 10.0% to \$4.1 million as a result of the steep economic downturn.

The following State grants and reimbursements are expected in 2009-2010: Public Library Foundation (\$337,000); the California Library Literacy Service grant (\$50,000); the Waste Tire Enforcement grant (\$170,000); the Abandoned Vehicles Abatement Program (\$700,000); Auto Theft reimbursement (\$370,000); and the Highway Maintenance Charges reimbursement (\$287,000). The majority of these revenues are set at the 2008-2009 Adopted Budget level.

Growth of approximately 2% annually is projected in the out years of the Forecast.

Gas Tax

The Gas Tax estimate assumes that collections in 2008-2009 will drop 10.9% to \$16.7 million based on current tracking levels this year. In 2009-2010, an additional 2% decline is projected, bringing collections to \$16.4 million. These collection levels are below historical tracking patterns for this category and reflect the impact of volatile gas prices as well as the severe economic downturn. In the out years of the Forecast, growth of 0.5% annually is projected.

Transient Occupancy Tax

It is currently estimated that Transient Occupancy Tax receipts for 2008-2009 will total \$8.9 million, reflecting a decline of 6.7% from the 2007-2008 collection level. In 2009-2010, an additional decline of 14.2% from the 2008-2009 estimate is anticipated, reflecting the impact of the deep economic recession as well as the loss of business during the construction period for the Convention Center expansion. These revenue estimates were based on a study performed by an independent consultant Horwath HTL. In the remaining years of the Forecast, annual growth ranging from 2.7% to 9.1% is projected.

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Telephone Tax

In November 2008, voters approved a ballot measure that replaced the Emergency Communication System Support (ECSS) Fee with a Telephone Tax. The new tax was set at a rate 10% below the existing ECSS Fee. In 2009-2010, an estimated \$21.6 million will be generated from this new tax. In the out years of the Forecast, collections in this area are expected to increase 2% per year.

Utility Tax

Utility Taxes are imposed on electricity, gas, water, and telephone usage. Collections in 2008-2009 are anticipated to total \$84.5 million, representing an increase of 2.8% from the 2007-2008 collection level. In 2009-2010, Utility Tax collections are projected to increase less than 1% to \$85.0 million. In the Electricity category, a 4% increase is projected in 2009-2010 based on estimated rate increases. In the Gas category, it is assumed that collections will remain at the 2008-2009 level based on the assumption that Gas rates will experience declines in 2009 and will increase in 2010. Water Utility Tax receipts are also expected to remain at 2008-2009 levels as projected rate increases in this category of 5-10% are anticipated to be offset by lower consumption associated with potential water conservation efforts that may become mandatory. A decline of 4.2% in the Telephone Utility category is projected in 2009-2010. This decline reflects the impact of the ballot measure approved by the voters in November 2008 that lowered the tax rate by 10% and modernized the tax base, partially offset by the projected 2% increase in activity.

In the out years of the Forecast, growth ranging from 3.5% to 4.9% annually is expected in the Utility Tax category.

Franchise Fees

Franchise Fees are collected in the Electricity, Gas, Cable, Tow, Commercial Solid Waste, Water, and Nitrogen Gas Pipeline categories. Overall, collections are projected at \$41.3 million in 2008-2009, a slight increase over the 2007-2008 actual receipts of \$41.1 million. The growth in 2008-2009 was held down by the projected 6.1% decline in the Commercial Solid Waste category. In 2009-2010, Franchise Fees are expected remain essentially flat at \$41.2 million. In 2009-2010, growth is projected in the Electricity (4.0%), and Cable Television (2.0%) Franchise Fee categories. This growth, however, is offset by projected declines in the Commercial Solid Waste (down 2.7%) and Gas (down 10%) Franchise Fee categories. The decline in Commercial Solid Waste Franchise Fees reflects the impact of the severe economic downturn as well as recycling efforts. The Gas Franchise Fee category is also expected to decline based on the projected decline in gas prices in calendar year 2009. The remaining categories are expected to remain at the 2008-2009 estimated level for 2009-2010.

In the out years of the Forecast, Franchise Fee revenues are anticipated to increase from 3.4% to 4.8% annually.

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Fines, Forfeitures and Penalties

In 2008-2009, the Fines, Forfeitures and Penalties category is expected to generate \$15.1 million. This figure includes a penalty payment of \$539,000 from the Garden City Card Club as well as additional revenue of \$230,000 generated from the partial year implementation of a parking fine increase that was approved in February 2009. In 2009-2010, a total of \$15.5 million is projected and includes the final payment of \$45,000 from the Garden City Card Club as well as the full year implementation of the increase to the parking penalty fee. In the out years of the Forecast, growth ranging from 1.0% to 1.3% is projected annually.

Revenue from Local Agencies

In 2009-2010, revenue of \$47.7 million is projected from other local agencies, such as the Redevelopment Agency, the Central Fire District, and the County. The largest portion of the Revenue from Local Agencies category consists of reimbursements from the San José Redevelopment Agency (SJRA). The SJRA reimburses the General Fund for the Convention Center lease payment that is projected at \$14.7 million for 2009-2010. Estimated SJRA reimbursements for City service costs for 2009-2010 of \$18.5 million are based on the assumption that ongoing support will remain consistent with current levels. This figure includes SJRA reimbursements for eligible expenditures (which enable the City to fund the San José Best Program at \$4.0 million and to cover the annualized cost for eight Police Officer positions at \$1.0 million).

The City also receives reimbursement from the Central Fire District for the County areas covered by the San José Fire Department. These payments are based on the property tax assessments for fire services collected in those areas, which are passed on to the City. For 2008-2009, Central Fire District payments are expected to end the year at \$7.5 million. This includes a true-up payment from the prior year of \$900,000. In 2009-2010, collections are expected to drop to \$6.9 million. This assumes a minimal true-up payment in 2009-2010 and a 1% increase in Property Tax receipts.

In 2009-2010, payments from the County of Santa Clara for the first responder advanced life support program (Paramedic Program) are assumed at \$1.8 million as the receipts are based on the annual adjustments approved by the contract with the County. In addition, the City is expected to receive \$1.7 million from the County for the Adult Day Care and Senior Nutrition programs. Payments of \$1.8 million from other local agencies are expected to reimburse the City for the Police Department CAL-ID program.

No revenue is projected from Enterprise Fund In-Lieu payments from the Water Pollution Control Plant or the Municipal Water System. The \$2.4 million budgeted from this source in 2008-2009 was the last year of a two-year phase-out of this payment.

In the remaining years of the Forecast, the Revenue from Local Agencies category is projected to increase annually by 0.16% to 2.17%, based on the scheduled payments and cost-of-living adjustments for staff reimbursements.

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Other Revenue

The Other Revenue category consists of miscellaneous revenues received from a variety of sources, including proceeds from the Sale of Surplus Property, cost reimbursements for the Investment Program, Arena Rental, Suite, Parking, and Naming revenues, and reimbursements from the Airport to cover a portion of the Airport West property debt service payments.

Revenue estimates assume continuation of current year activity levels with revisions, where appropriate, for 2009-2010 costs or agreements. The proceeds from the Sale of Surplus Property category has been set at \$200,000 to assume that, at a minimum, a portion of costs of the Real Estate Division related to the sales process will be recovered. Airport reimbursement for the Airport West property of \$1.7 million is projected in 2009-2010. However, no Airport reimbursements for this property are projected in the out years of the Forecast based on the assumption that the Airport will no longer have a use for this property once the Airport expansion is complete.

The 2009-2010 estimate for Other Revenue is \$13.3 million. In 2010-2011, a decline of 11.3% is projected, primarily due to the elimination of the Airport reimbursement for the Airport West property. Increases of 1.9% are projected for both 2011-2012 and 2012-2013 followed by a slight decline of 0.20% in 2013-2014 to reflect changes in scheduled payments.

Overhead Reimbursements

The Overhead Reimbursements category includes overhead reimbursements from both operating and capital funds. In 2009-2010, a total of \$37.9 million is projected. This estimate is based on 2009-2010 overhead rates prepared by the Finance Department applied against the projected 2009-2010 salaries for those positions for which an overhead rate is applied. The overhead revenue estimate has been decreased to reflect the potential loss of overhead associated with positions that are likely to be eliminated in the 2009-2010 Budget, including positions at the Airport and the Convention Center.

In the remaining years of the forecast, annual increases ranging from 1.4% to 3.4% are assumed reflecting the anticipated salary and cost-of-living and adjustments. It should be noted that cost-of-living salary adjustments have not been factored into the last three years of the Forecast. There are currently no negotiated agreements for that period.

Transfers

The Transfers category is projected at \$24.5 million for 2009-2010. This reflects a drop from the 2008-2009 Adopted Budget estimate of \$51.7 million, primarily due to the elimination of the \$26.0 million transfer from the Emergency Communication System Support (ECSS) Fee Fund and the phase-out of the Municipal Water Rate-of-Return Transfer (\$445,000). Through the approval of a November 2008 ballot measure, the ECSS Fee has been replaced with a Telephone Tax effective April 2009 and is reflected in a separate category in this document.

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Transfers (Cont'd.)

Adjustments to the Airport Crash Fire Rescue and Airport Police Consolidation reimbursements have been assumed in 2009-2010 and the remaining four years of the Forecast to reflect updated salary and benefit costs and projected cost-of-living adjustments. The remaining transfers have been reflected at current year levels, with slight adjustments for costs or payment schedules as necessary.

In 2010-2011, the Transfers are expected to drop to \$23.6 million to reflect the scheduled phase-out of transfers from two special funds. In the remaining years of the Forecast, annual increases ranging from 0.9% to 1.8% are assumed.

Reimbursements for Services

The Reimbursements for Services category reimburses the City for actual costs associated with the Deferred Compensation Program and the Maintenance Assessment District Funds. These amounts have been set to recover costs in 2009-2010 of \$669,000, with increases ranging from 3.4% in 2010-2011 and dropping to 1.4% in the remaining of forecast to reflect salary and benefit adjustments.

Beginning Fund Balance

The forecast estimate for available Beginning Fund Balance in 2009-2010 of \$50.4 million is based on the following assumptions:

- A Contingency Reserve balance of \$28.7 million will remain uncommitted by year-end.
- A total of \$16.5 million will be achieved from a combination of excess revenue, expenditure savings, and the liquidation of prior-year carryover encumbrances. This figure is based on a review of actual revenue and expenditure performance in 2008-2009.
- A total of \$5.2 million will be provided from various Reserves for use in 2009-2010. The Forecast includes \$3.1 million from the Parks Maintenance Earmarked Reserve to support prior year General Fund balancing plans (\$1.6 million), Enhanced Parks Maintenance staffing (\$1.2 million), and Public-Private Partnership efforts (\$330,000). The Tully Branch Library Sunday Hours Reserve will provide \$60,000 to continue this activity in 2009-2010. The Wellness Reserve will provide \$311,000 to fund the Wellness Program and the Neighborhood Investment Reserve will provide \$316,000 to fund 3.0 Community Coordinator positions that support the Strong Neighborhoods Initiative. In addition, the Salary Reserve will provide \$1.4 million that is no longer necessary after the completion of salary and benefit calculations in 2008-2009.

The future year beginning fund balance estimates assume that excess revenues of 1% and expenditure savings of 1.5% - 2% would be generated annually. This would generate fund balance ranging from \$20.6 million in 2010-2011 to \$26.9 million in 2013-2014. The carried

ELEMENTS OF THE GENERAL FUND FORECAST

REVENUE FORECAST (CONT'D.)

Beginning Fund Balance (Cont'd.)

over Contingency Reserve portion is adjusted upward based on the Contingency Reserve allocation from the prior year.

One-Time Funding Available

Not included in the Forecast but available for Council consideration is the 2009-2010 Future Deficit Reserve of \$4.0 million that was established, per City Council policy, as part of the 2007-2008 Annual Report. This reserve was set aside to fund a portion of the shortfall that was projected for 2009-2010 in the February 2008 Forecast. This reserve is not assumed in the remaining forecast years. However, the amount of funding that has been set aside historically for future year deficits has ranged from a low of \$4.3 million in 2000-2001 to a high of \$18.4 million in 2005-2006. Per City Council policy, a portion of the remaining unallocated funds available at the close of each fiscal year is directed to be used to cover any projected shortfall in the following year based on the Five-Year General Fund Forecast.

In addition, the \$2.3 million Airport West Proceeds Reserve is available and could be used to offset a portion of the Airport West debt service costs for one year (2009-2010). The Reserve was established in 2008-2009 from option payments received for the Airport West property.

The Forecast does not assume the use of the \$15.3 million Economic Uncertainty Reserve that was established to address higher than anticipated declines in revenue resulting from the current economic downturn.

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST

Personal Services

As is our usual practice, the first year (2009-2010) projection for personal services costs in this Forecast has been calculated at a detailed level. An extract of payroll system information as of August 2008 was used as the starting point. This individual position-level information was then reviewed, corrected, and updated by each department to include current vacancies and filled positions, accurate salary step status, as well as any position reallocations. Also, 2008-2009 ongoing position reductions (cost savings) and additions (cost increases) were annualized, and projections for all categories of benefit costs in the coming year were made.

Personal services costs continue to account for approximately three-quarters of the General Fund's total costs. The Personal Services category has been broken down into its three major components (Salaries and Other Compensation, Retirement, and Health and Other Fringe Benefits). This display of personal services costs is intended to show how these different elements drive rising personnel costs. For example, even without any negotiated salary increases, growth in the other major personnel cost components (scheduled non-management step increases, retirement and health and other fringe benefits) impact personal services and, particularly in recent years, have been responsible for a growing element of the major increases in personnel costs. To provide historical context to the growth in this category, from 2000-2001 to 2008-2009, total average personal services costs grew by 59%, with average salary and other compensation increasing 43% over this period, while retirement costs increased 127% and health and other fringe benefit costs grew by 118%.

For 2009-2010, the total personal services preliminary estimate, as displayed in Section Two of this report, represents a decrease of approximately 0.6% (\$4.1 million) from the 2008-2009 Adopted Budget level. It should be noted, however, that the level of growth shown for personal services costs in the Forecast actually significantly understates the underlying personal services growth for 2009-2010 due to several reasons that are discussed below. Once the 2009-2010 personal services category has been adjusted for one-time items, the underlying growth of personal services is approximately 2.3% next year.

Specific factors impacting the elements of the personal services costs in the Forecast include:

- Approved salary compensation and benefit increases as negotiated with four of the thirteen bargaining/employee groups, including Police Officers Association (POA), City Association of Management Personnel (CAMP), Confidential Employees' Organization (CEO), and Municipal Employees' Federation (MEF);
- Forecasted new negotiated salary compensation and benefit increases with nine of the thirteen bargaining/employee groups, including International Association of Firefighters (IAFF), International Union of Operating Engineers, Local #3 (OE#3), International Brotherhood of Electrical Workers (IBEW), Association of Engineers and Architects, Units 41 and 42 (AEA), Association of Engineers and Architects, Units 43 (AEA), Association of Maintenance Supervisory Personnel (AMSP), Association of Building, Mechanical and Electrical Inspectors (ABMEI), Unrepresented Non-Management (Unit 82), and Executive Management (Unit 99);

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST (CONT'D.)

Personal Services (Cont'd.)

- Salary step increases for current non-management employees (an overall 1.3%, or \$7.1 million salary and benefit growth level for the category);
- The implementation of the retirement rates for both the Federated and Police/Fire Retirement plans for the pre-funding of the City's annual contribution which resulted in a net savings of \$4.1 million in the General Fund. This was one of the balancing strategies that the City approved for 2009-2010. These savings are partially offset by a loss of interest earnings revenue of approximately \$1.7 million;
- Forecasted health rate increases of 10%;
- The new inclusion of the five year phase-in plan to fully fund the City's share of the annual required contribution for retiree healthcare benefits for Police Officers' Association (POA) employees, as negotiated (\$2.4 million in 2009-2010 and increasing to \$9.9 million by 2013-2014). In addition to the Personal Services funding to cover the liability for POA employees, this Forecast includes \$8.3 million by the end of the five-year period to address the projected General Fund liability for non-POA employees, bringing the total retiree healthcare benefits funding in the General Fund to \$18.2 million. A portion of this ongoing General Fund funding (\$1.5 million) was set aside as an Earmarked Reserve in the 2008-2009 Adopted Budget. The remaining funding is reflected in the Committed Additions section of this document (\$0.2 million in 2009-2010 and increasing to \$6.8 million by 2013-2014);
- The impact of actions taken during 2008-2009 to rebalance the Development Fee Program with the elimination of 52 positions. The Planning and Building Fee Programs are by City Council policy required to achieve 100% cost recovery. Due to a steep decline in development activity, actions to address a revenue shortfall on an ongoing basis were necessary;
- The impact of deleting rebudgeted items in the Salary Reserve, primarily the funding for miscellaneous benefits and items previously carried over from prior years; and
- Elimination of two programs, Challenges and Choices and Summer Work Experience, that were approved by the City Council to be eliminated beginning in 2009-2010.

It is also important to note that not included in the Personal Services category are two large General Fund cost categories: Workers' Compensation Claims Payments and Sick Leave Payments Upon Retirement which are other significant components of the total costs of the City's workforce. These costs are included in the City-Wide Expenses category of this forecast. In 2009-2010, \$15.7 million for Workers' Compensation Claims Payments and \$9.3 million for Sick Leave Payments Upon Retirement have been included in this General Fund Forecast.

It should be further noted that due to the mechanism used to represent the desired outcome in fee programs, personal services expenditures in this forecast are understated by an additional \$4.1 million. The \$4.1 million represents the shortfall that would exist in the development-related fee programs in the Planning, Building and Code Enforcement, Fire and Public Works Departments

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST (CONT'D.)

Personal Services (Cont'd.)

if all costs were reflected. These fee programs are intended by the City Council to recover 100% of the cost of development review and inspection and, as a result, costs are reflected in this Forecast at the expected revenue collection level. The Public Works, Fire, and Building fee programs will be required to develop strategies that will address this \$4.1 million shortfall in the 2009-2010 Proposed Budget.

Retirement costs are calculated as a percentage of salary costs. In this Forecast, retirement costs have only been adjusted for the impact of the pre-funding of the City's contribution and step increases and cost-of-living adjustments (COLAs). It should be noted that every two years, an actuarial study is completed on the City's two retirement systems, Federated and Police and Fire. The next actuarial studies are scheduled to be completed in 2009-2010 for implementation in 2010-2011. Presently, the extreme volatility and steep declines in the U.S. financial markets are negatively impacting performance in the two retirement systems. The extent of that impact upon the contribution rates is not known at this time although the likelihood is for significant upward movement in rates and City costs to offset the investment losses. Due to the volatility of retirement rates, however, no specific predictions for the retirement rate contribution adjustments that will be required have been assumed in the out years of this Forecast.

As with past forecasts, personal services costs in years two through five of this Forecast have been projected on a more global basis, using the detailed costs calculated for the first year as a base, and then growing that base by an overall percentage factor representing expected growth from salary and benefit adjustments. For this Forecast, the out years were projected to inflate at a composite rate of approximately 2.8%. This projected rate of growth is well below the 4.3% presumed in the February 2008 forecast due entirely to a change in forecast methodology. In this Forecast, no cost-of-living salary increases for any employees in the last three years of the Forecast has been assumed reflecting the fact that there are no negotiated agreements covering this period. In past years, projected increases were built into the Forecast. Thus, the approval of any negotiated salary or benefit increases in those years, without any offsetting increase in revenues or reduction in costs, will have the effect of driving up the City's shortfall. In this regard, consideration of salary increases is being treated as a resource allocation policy decision and any decision will be made in the context of what is affordable in light of the City's many service delivery priorities.

Non-Personal/Equipment

Non-personal/equipment expenditures for the first year of the forecast have also been calculated at a detailed level. The process utilized by the Budget Office includes adjusting each department's current year budget to eliminate one-time cost allocations, annualizing all partial-year reductions or additions approved for 2008-2009, and including projected adjustments for specific large non-personal/equipment allocations (e.g., utilities, leases, contracted services, and Police Department vehicle replacement) as described later in greater detail. The resulting 2009-2010 estimates represent a decrease (\$2,613,000) from the current year level. Departmental gas and electricity funding for 2009-2010 has been slightly adjusted in this Forecast to reflect

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST (CONT'D.)

Non-Personal/Equipment (Cont'd.)

approved gas and electricity rates and projected consumption changes from new or expanded City facilities.

Other specific adjustments included in the 2009-2010 non-personal/equipment base include increases for the scheduled replacement of police vehicles (\$1.1 million), vehicle maintenance and operating costs (\$49,000) and contractually required cost of living increases to major contracts. An increase of \$1,147,000 from 2008-2009 for the scheduled replacement of the Police Department's marked, unmarked and covert fleet has been included. This is an increase of \$697,000 from what was assumed in the prior forecast due to higher vehicle usage. A major component of the City's vehicle maintenance and operating costs is fueling. Over the last eight months, fuel costs have fallen from the high costs that were being experienced last summer. This reduction in fuel costs almost entirely offsets increases to staffing costs needed to maintain the fleet. In addition to contractually required cost of living increases to major contracts, a 1.5% increase, which represents one-half of the San Francisco-Oakland-San José area consumer price index for the past 12 months, has been applied to eligible expenditures. Eligible expenditures in the non-personal/equipment category are non-centrally determined details, such as supplies, postage, and printing, and expenditures that have not already been inflated for negotiated contracts and agreements. For the out years of the forecast, a growth rate of 2.0% has been assumed from the 2009-2010 non-personal/equipment base level in each of the four years. This projection is unchanged from that assumed in recent forecasts.

Other Expenditures

The General Fund **Capital Projects** category includes debt service payments for Central Service Yard – Phase I (\$796,000 in 2009-2010). These payments increase to \$1,673,000 in the out years as a result of prior budget actions taken in 2008-2009 that impacted both 2008-2009 and 2009-2010. Also included in this category is the continuation of allocations for Arena repairs, unanticipated maintenance of City facilities, and fuel tanks and methane monitoring control and replacement.

As was the case in previous forecasts, continued capital funding for the Replacement of Fire Apparatus is carried in this Forecast. In 2009-2010, the level of funding is \$1.8 million and increases to \$3.2 million in 2012-2013 to fund the current Fire Vehicle Replacement Policy. This is consistent with the previous forecast.

The City-Wide Expenses program in the first year of the Forecast (2009-2010) represents a net reduction of \$45.4 million from the 2008-2009 level. This large reduction reflects the combined impact of deleting rebudgets (\$41.3 million) and other one-time items (\$16.9 million). This category also includes funding for debt service payments for several City facilities. The payments for the Convention Center and Airport West Property, which are reimbursed partially by Airport funds and Redevelopment Agency, have been adjusted by a net reduction of \$3.0 million to reflect the latest payment schedules. Workers' Compensation Claims payments in this forecast range from \$15.7 million in 2009-2010 to \$19.7 million in 2013-2014, which is an

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST (CONT'D.)

Other Expenditures (Cont'd.)

increase of \$2.1 million from the last forecast reflecting an increase in projections for growth in increased medical costs. Sick Leave Payments Upon Retirement expenditures have been included in this forecast at \$9.3 million for 2009-2010.

The **Earmarked Reserves** category includes a reserve for the Comprehensive General Plan Update (\$200,000) and for Retiree Healthcare Benefits (\$1.8 million, \$300,000 of which is offset by contributions from other funds). The General Plan Update Reserve is entirely offset by revenues collected from a surcharge on development permits. The Retiree Healthcare Reserve is an ongoing initial investment that was established in the 2008-2009 Adopted Operating Budget to begin to address the long-term liability associated with retiree healthcare. Two recent Governmental Accounting Standards Board accounting statements require changes in accounting and external reporting for post-employment benefits. Actuarial studies have been completed on the City's two retirement plans, Federated and Police and Fire, to calculate the liability under these new accounting standards. Based on the most recent analysis, the total liability is estimated at \$18.2 million annually for the City's General Fund share of the costs associated with retiree healthcare benefits. This liability figure will be updated as part of new studies to be completed in early 2009-2010. As discussed under the Personal Services category, this Forecast includes funding to fully address the projected General Fund liability by 2013-2014 in this Earmarked Reserve (\$1.5 million) as well as the Personal Services and Committed Additions sections (\$16.7 million).

The Forecast does not include a number of Earmarked Reserves that may remain unspent in 2008-2009, and be rebudgeted to 2009-2010. Some of the larger current Earmarked Reserves include the Development Fee Program Reserves, Workers' Compensation/General Liability Catastrophic Reserve, Enhanced Parks Maintenance Reserve, Salary and Benefits Reserve, Future Capital Projects (FF&E) Reserve, Neighborhood Investment Fund Reserve, and Economic Uncertainty Reserve.

As in previous years, the **Equipment** category includes a general equipment reserve of \$100,000 for subsequent allocation in the 2009-2010 Proposed Budget. Similarly, \$250,000 is assumed annually for computer equipment and automation projects also for subsequent allocation during the Proposed Budget process.

The Transfers category includes funding for Communications Center debt service as required under the terms of financing used for construction of this facility (final payment of \$2.4 million in 2009-2010); funding to cover a portion of the debt service payments for the Hayes Mansion Conference Center (\$4.1 million per year) and Rancho del Pueblo and Los Lagos Golf Courses (\$1.3 million per year); and payments in accordance with the San José Arena Management (\$1.5 million per year in years one through three) for Arena repairs and capital enhancements. All of the debt service and maintenance and operations costs for the Hayes Mansion Conference Center and golf courses are funded in the Community Facilities Revenue and Municipal Golf Course Funds, however, revenues in those funds are not projected to be sufficient to completely cover these costs. These transfers have been increased in this Forecast by \$200,000 and \$300,000,

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST (CONT'D.)

Other Expenditures (Cont'd.)

respectively, due to declining revenues. The payments for Arena repairs and capital enhancements are in compliance with the San José Arena Management Agreement Extension from 2009-2018. The first year of the Forecast (2009-2010) is the second year of these required payments, as assumed in prior forecasts. In 2012-2013, an additional \$1.25 million is necessary to pay for the City's share of the \$16.5 million of improvements at the Arena, as approved by City Council in May 2007. In addition, revenue offset payments for the Camden Lifetime Activities Center debt service (\$202,000 in 2009-2010), Fiber Optics loan repayment, and various Maintenance Assessment Districts for the General Fund's share of landscape services in those areas are included.

A **Vehicle Replacement/General Fleet** allocation (\$2.1 million in 2009-2010) is included to fund a vehicle replacement schedule for the General Fleet (\$1.6 million) and for the retrofit of diesel powered vehicles. State regulations necessitate the City to replace the City's diesel-powered vehicles throughout the forecast period, in order to comply with new regulations to reduce the use of fossil fuels and the release of harmful emissions. In this Forecast, costs range from \$482,000 in 2009-2010 to \$177,000 in 2012-2013.

In 2009-2010, **Vehicle Replacement/Police Fleet** funding is carried in the Non-Personal/Equipment category (\$3.9 million). Due to the large variation in funding levels necessary to fund the replacement of Police vehicles over the five-year period, the incremental costs necessary to ensure that replacement schedules for the marked, covert, and unmarked Police fleet are met are shown as a separate line item. In this Forecast, they range from an increased need resulting in additional costs of \$724,000 in 2011-2012 to a reduced need resulting in savings of \$2,175,000 in 2013-2014.

Contingency Reserve

Per City Council policy, the 2009-2010 Contingency Reserve is projected at the level necessary to comply with the City Council policy to maintain a 3% Contingency Reserve (\$28.7 million). Amounts necessary to remain in compliance with that policy are also included in each of the remaining four years of the Forecast.

Committed Additions to the Base General Fund Forecast

In this Forecast, projected additions to the base expenditure level have been included as **Committed Additions**. The **Committed Additions** are additional expenditures to which the City is considered to be committed by prior City Council action, such as the costs related to maintaining and operating capital projects previously approved by the City Council. The Forecast Base Case, considered most closely by the City Council, includes ongoing program costs plus committed additions.

The following committed additions, totaling \$5.0 million, are included in the 2010-2014 Forecast and explained in more detail in a later section of this document.

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST (CONT'D.)

Committed Additions to the Base General Fund Forecast (Cont'd.)

County Pocket Annexations costs (\$298,000 in 2009-2010) that would be required by the Department of Transportation have been included to maintain the approximately 40 miles of public streets and related infrastructure that will be annexed into the City from Unincorporated areas within the City of San José's Urban Service Area.

New Parks and Recreation Facilities Maintenance and Operations costs (\$130,000 in 2009-2010) are included at the levels necessary to support the additional costs of maintaining and operating new or expanded park facilities that were included in the City's latest Five-Year Capital Improvement Program and those that are being developed by other agencies. Examples of projects include Kirk Community Center Improvements in 2009-2010 and Edenvale Community Center in 2010-2011.

Increased costs from scheduled **New Traffic Infrastructure Assets Maintenance and Operations** (\$204,000 in 2009-2010) are included as a committed addition.

The approved bond measures from the elections of November 2000 and March 2002 will result in new and expanded library (**Measure O**), park (**Measure P**), and police and fire (**Measure O**) facilities and will require significant additional **Maintenance and Operations** funding (\$2,420,000 in 2009-2010). Some of the new facilities scheduled to open during this forecast period include: the South San José Police Substation, Fire Station 37 (Silver Creek/Yerba Buena Road), East San José Carnegie Branch, Santa Teresa Branch Library, Seven Trees Community Center and Library, Happy Hollow Park and Zoo, and Bascom Library and Community Center.

The hiring of **Additional Police Officers**, as directed by the City Council as part of the approval of the 2008-2009 Mayor's June Budget Message has been included in the forecast. The addition of 25 Police Officers annually through 2011-2012 is now included in this category. The cost of these positions is projected at \$1.8 million in 2009-2010 and expected to increase to \$10.8 million by 2013-2014.

A new item, **Retiree Healthcare Benefits**, has been included in the Forecast to reflect the five-year phase-in of the City's share of the General Fund annual required contribution for retiree healthcare benefits for non-POA employees. These costs increase from \$0.2 million in 2009-2010 to \$6.8 million in 2013-2014. As described previously, additional allocations for retiree healthcare benefits are displayed elsewhere in this document and include (1) Earmarked Reserves of \$1.8 million (\$1.5 million in the General Fund and \$300,000 in special funds) as those funds were added in 2008-2009 on an ongoing basis to begin to address the long-term liability of retiree healthcare benefits and (2) Personal Services funding increasing from \$2.4 million in 2009-2010 to \$9.9 million in 2013-2014 to cover the projected liability for POA employees, consistent with the recently negotiated funding agreement for this liability with the POA. In total, retiree healthcare benefits funding is increased to \$18.2 million annually by 2013-2014 to fully fund this liability.

ELEMENTS OF THE GENERAL FUND FORECAST

EXPENDITURE FORECAST (CONT'D.)

General Fund Capital Operating and Maintenance Costs/Budget Principle #8

Budget Principle #8 states that Capital Improvement Projects shall not proceed for projects with annual operating and maintenance costs exceeding \$100,000 without City Council certification that funding will be made available in the applicable year of the cost impact. Consistent with that direction, this Forecast includes a detailed list and discussion of capital projects that are underway or were previously approved by the City Council with annual operating and maintenance costs in the General Fund greater than \$100,000. Funding for these projects have been included as part of approved Capital Improvement Programs or Redevelopment Agency Budgets. The majority of these costs are associated with the voter-approved General Obligation bonds for Park, Library, and Public Safety facilities. The operating and maintenance costs for these facilities are included in the figures presented in this Preliminary General Fund Forecast. In addition, four potential projects where funding has not yet been approved through the City Capital Improvement Program or Redevelopment Agency Capital Budget are identified. These projects are under very preliminary development and if approved, are anticipated to have an annualized operating and maintenance impact of at least \$2.3 million by 2013-2014. Consistent with the direction approved as part of Budget Principle #8, for purposes of this Forecast, these operating and maintenance costs are not included as part of the General Fund Five-Year Forecast "Committed Additions" category. Certification for these projects and other identified projects that have not been approved by the City Council will be sought as part of the 2010-2014 Proposed Capital Improvement Program. If certified by the City Council, the operating and maintenance costs associated with these facilities would then be included in subsequent General Fund Five-Year Forecast documents.

ELEMENTS OF THE GENERAL FUND FORECAST

OPERATING MARGIN

The Base Case with Committed Additions General Fund Forecast projects a shortfall in the first year (2009-2010) of \$61.2 million. This is higher than both the November 2008 Preliminary Forecast shortfall estimate of \$59.1 million and the February 2008 Forecast shortfall of \$42.5 million for 2009-2010.

Base Case expenditures, including committed additions, increase from \$886.1 million in 2009-2010 to \$1.0 billion in 2013-2014, for an average growth rate each year of approximately 3.4%. This rate of expenditure growth outpaces the average increase in General Fund sources (including Beginning Fund Balance) of 2.9%. The sources of revenue total \$824.9 million in 2009-2010, and grow to \$921.1 million in 2013-2014.

The following table shows how the projected shortfall has changed in the most recent forecasts. The incremental shortfall assumes each preceding deficit is solved completely with ongoing solutions in the year it appears. Each of the four out years of the Forecast is shown in the table, along with a comparison with the increments projected for those years in the February 2008 Forecast and the preliminary 2009-2010 update provided to the City Council in November 2008.

2010-2014 General Fund Forecast Changes in Operating Margin (\$ in Millions)					
	<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
February 2008 Incremental Surplus/(Shortfall)	(\$42.52)	(\$5.49)	(\$4.73)	\$2.50	N/A
2008-2009 Adopted Budget Impact Incremental Surplus/(Shortfall)	(\$4.08)				
Revised Forecast	(\$46.60)	(\$5.49)	(\$4.73)	\$2.50	N/A
November 2008 Incremental Surplus/(Shortfall)	(\$59.14)	(\$26.95)	(\$0.11)	\$3.60	\$5.79
February 2009 Incremental Surplus/(Shortfall)	(\$61.19)	(\$36.74)	(\$4.92)	\$6.49	\$10.11
<i>One-time Funding Available</i>	\$6.30	N/A	N/A	N/A	N/A

In the February 2008 Forecast, an incremental shortfall of \$42.52 million for 2009-2010 was projected. This figure was based on the assumption that the entire 2008-2009 shortfall would be solved with ongoing actions. However, the 2008-2009 Adopted Budget included a combination

ELEMENTS OF THE GENERAL FUND FORECAST

OPERATING MARGIN (CONT'D.)

of ongoing and one-time solutions. The carryover impact of those one-time measures is reflected in the 2008-2009 Adopted Budget Impact incremental shortfall of \$4.08 million and, when combined with the previous shortfall anticipated for 2009-2010, would result in a deficit of approximately \$46.6 million in 2009-2010.

In November 2008, staff prepared a Preliminary Five-Year General Fund Forecast incorporating the final 2007-2008 actual performance and the first few months of activity in 2008-2009. In that Preliminary Forecast, the General Fund deficit for 2009-2010 was increased to \$59.1 million. This increase in the projected deficit was the net result of a number of upward and downward adjustments to the City's many General Fund revenue and expenditure categories. The most significant changes included: downward adjustments to the economically sensitive revenue estimates; the addition of costs associated with the phase-in of the City's share of the General Fund annual required contribution for retiree health care benefits and 25 new Police Officer positions per City Council direction; the addition of \$20 million in revenue as a result of the passage of the November 2008 ballot measures; and slightly lower than anticipated cost-of-living adjustments.

For the February 2009 Forecast, staff completed an in-depth review of anticipated revenues and expenditures for 2009-2010 and the remaining four years of the forecast period. Based on this updated information, a 2009-2010 General Fund shortfall of \$61.2 million is projected, a net increase of \$2.1 million from the November 2008 figure. This relatively small increase was the result of net downward expenditure adjustments of \$15.4 million that are more than offset by a net revenue reduction of \$17.5 million.

The projected drop in expenditures for 2009-2010 was primarily the result of lower debt service costs for City Hall and the Airport West properties, lower assumed costs to address the City's General Fund liability for retiree healthcare benefits; lower costs assumed for the development fee program to align with projected revenues; and lower utility and fuel costs. Other expenditure adjustments were based on a more in-depth review of base costs.

The downward adjustment of \$17.5 million to the General Fund revenue estimates primarily reflects the projected impact of the rapidly deteriorating economy on the City's revenues. The majority of the decline was the result of adjustments to the economically sensitive revenue categories, including Sales Tax, Property tax, Business Tax, Transient Occupancy Tax, and Use of Money and Property (interest earnings). The revenue estimates for the development-related fee programs are also significantly lower than the November 2008 figures based on actual performance through the first half of 2008-2009.

The second year of the Forecast (2010-2011) also has a sizeable General Fund deficit of \$36.7 million. While economic performance is expected to recover somewhat by 2010-2011, revenue growth is still projected to be very low in that year (1.13%). This is due, in part, to the small decline in Property Tax revenues projected for that year. Because Property Tax receipts in each fiscal year are based on activity in the prior calendar year, there is somewhat of a lag in realizing the gains and losses due to economic performance. The large declines in real estate prices

ELEMENTS OF THE GENERAL FUND FORECAST

OPERATING MARGIN (CONT'D.)

expected in 2009 will impact Property Tax receipts in 2010-2011. Projected expenditure growth in 2010-2011 of 5.2% significantly outpaces the minimal revenue growth. This overall expenditure growth is driven by personal services increases projected at 4.3% due, in part, to the continued phase-in of retiree healthcare costs and by changes in Committed Additions.

The variances in the three out years are minimal, ranging from a slight deficit of \$4.9 million in 2011-2012 to a surplus of \$10.1 million in the last year of the Forecast. It is important to note again, however, that no cost-of-living adjustments (COLAs) for any of the City's employees have been assumed in the last three years. There are currently no negotiated agreements that cover this time period. This is a methodology change that was first incorporated into the November 2008 Preliminary General Fund Forecast. With this change, the consideration of salary increases is being treated as a resource allocation policy decision. This decision will need to be made in the context of what is affordable in light of the many service delivery priorities. At current rates, each 1% increase in salary has a General Fund price tag of approximately \$5.5 million.

BASE CASE

February 2009 Forecast

REVENUE SUMMARY

	ADOPTED	FORECAST				
	<u>2008-2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
PROPERTY TAX	208,267,000	207,810,000	204,796,000	210,940,000	219,230,000	230,148,000
		(0.22%)	(1.45%)	3.00%	3.93%	4.98%
SALES TAX	152,536,000	138,987,000	144,324,000	150,544,000	157,153,000	164,775,000
		(8.88%)	3.84%	4.31%	4.39%	4.85%
DEPARTMENTAL CHARGES	30,863,305	28,301,000	29,263,000	29,673,000	30,088,000	30,510,000
		(8.30%)	3.40%	1.40%	1.40%	1.40%
BUSINESS LICENSE TAX	26,412,059	24,900,000	24,940,000	24,990,000	25,042,000	25,097,000
		(5.72%)	0.16%	0.20%	0.21%	0.22%
MONEY & PROPERTY	13,221,500	7,950,000	8,110,000	8,273,000	8,457,000	8,678,000
		(39.87%)	2.01%	2.01%	2.22%	2.61%
OTHER LICENSES	52,471,845	46,167,000	47,736,000	48,405,000	49,082,000	49,769,000
		(12.02%)	3.40%	1.40%	1.40%	1.40%
MOTOR VEHICLE IN LIEU	4,896,000	2,766,000	2,757,000	2,757,000	2,768,000	2,793,000
		(43.50%)	(0.33%)	0.00%	0.40%	0.90%
FEDERAL REVENUE	3,815,311	222,000	222,000	222,000	222,000	222,000
		(94.18%)	0.00%	0.00%	0.00%	0.00%
OTHER STATE REVENUE	5,369,304	6,054,000	6,175,000	6,299,000	6,425,000	6,553,000
		12.75%	2.00%	2.01%	2.00%	1.99%
GAS TAX	17,200,000	16,366,000	16,448,000	16,530,000	16,613,000	16,696,000
		(4.85%)	0.50%	0.50%	0.50%	0.50%
TRANSIENT OCCUPANCY TAX	9,972,000	7,651,000	7,858,000	8,573,000	9,269,000	10,003,000
		(23.28%)	2.71%	9.10%	8.12%	7.92%
TELEPHONE TAX	0	21,600,000	22,032,000	22,473,000	22,922,000	23,381,000
		N/A	2.00%	2.00%	2.00%	2.00%
UTILITY TAX	83,690,000	84,959,000	87,915,000	91,581,000	95,922,000	100,642,000
		1.52%	3.48%	4.17%	4.74%	4.92%
FRANCHISE FEES	41,621,000	41,172,000	42,563,000	44,274,000	46,293,000	48,506,000
		(1.08%)	3.38%	4.02%	4.56%	4.78%
FINES, FORFEITURES & PENALTIES	15,726,000	15,509,000	15,658,000	15,854,000	16,052,000	16,252,000
		(1.38%)	0.96%	1.25%	1.25%	1.25%
REVENUE FROM LOCAL AGENCIES	48,071,886	47,725,000	48,761,000	49,575,000	49,653,000	50,118,000
		(0.72%)	2.17%	1.67%	0.16%	0.94%
OTHER REVENUE	17,496,485	13,290,000	11,791,000	12,014,000	12,245,000	12,220,000
		(24.04%)	(11.28%)	1.89%	1.92%	(0.20%)
TOTAL GENERAL REVENUES	731,629,695	711,429,000	721,349,000	742,977,000	767,436,000	796,363,000
		(2.76%)	1.39%	3.00%	3.29%	3.77%

February 2009 Forecast
REVENUE SUMMARY

	ADOPTED	FORECAST				
	2008-2009	2010	2011	2012	2013	2014
TRANSFERS & REIMBURSEMENTS						
OVERHEAD REIMBURSEMENTS	34,253,745	37,936,000	39,226,000	39,775,000	40,332,000	40,897,000
TRANSFERS	51,717,001	24,485,000	23,630,000	24,047,000	24,272,000	24,499,000
REIMBURSEMENTS FOR SERVICES	617,796	669,000	695,000	720,000	745,000	771,000
TOTAL TRANSFERS & REIMBURSEMENTS	86,588,542	63,090,000	63,551,000	64,542,000	65,349,000	66,167,000
		(27.14%)	0.73%	1.56%	1.25%	1.25%
TOTAL GENERAL FUND REVENUES	818,218,237	774,519,000	784,900,000	807,519,000	832,785,000	862,530,000
		(5.34%)	1.34%	2.88%	3.13%	3.57%
BEGINNING FUND BALANCE	202,881,541	50,429,000	49,362,000	55,620,000	57,244,000	58,535,000
GRAND TOTAL SOURCES	1,021,099,778	824,948,000	834,262,000	863,139,000	890,029,000	921,065,000
		(19.21%)	1.13%	3.46%	3.12%	3.49%

February 2009 Forecast
EXPENDITURE SUMMARY

	ADOPTED 2008-2009	FORECAST 2010	2011	2012	2013	2014
PERSONAL SERVICES						
Salaries and Other Compensation	480,803,000	483,097,000	500,700,000	507,449,000	514,289,000	521,221,000
Retirement	113,106,000	107,180,000	112,703,000	116,147,000	119,517,000	122,841,000
Health and Other Fringe Benefits	59,974,000	59,477,000	64,295,000	69,503,000	75,133,000	81,219,000
TOTAL PERSONAL SERVICES	653,883,000	649,754,000	677,698,000	693,099,000	708,939,000	725,281,000
		(0.63%)	4.30%	2.27%	2.29%	2.31%
TOTAL NON-PERSONAL/EQUIPMENT	92,745,428	90,132,000	91,221,000	93,045,000	94,906,000	96,804,000
		(2.82%)	1.21%	2.00%	2.00%	2.00%
OTHER EXPENDITURES						
CAPITAL PROJECTS	33,662,749	3,296,000	4,623,000	4,821,000	5,625,000	5,620,000
CITY-WIDE EXPENSES	122,659,251	77,258,000	79,151,000	83,077,000	83,922,000	85,647,000
EARMARKED RESERVES	80,273,373	2,070,000	2,070,000	2,070,000	2,070,000	2,070,000
EQUIPMENT (INCLUDING COMPUTER)	0	350,000	350,000	350,000	350,000	350,000
TRANSFERS	32,812,459	27,470,000	27,826,000	28,697,000	26,216,000	25,633,000
VEHICLE REPLACEMENT/GENERAL FLEET	0	2,082,000	2,023,000	2,053,000	1,777,000	1,777,000
VEHICLE REPLACEMENT/POLICE FLEET	<i>Included in N/P</i>	<i>Included in N/P</i>	(244,000)	724,000	(458,000)	(2,175,000)
TOTAL OTHER EXPENDITURES	269,407,832	112,526,000	115,799,000	121,792,000	119,502,000	118,922,000
		(58.23%)	2.91%	5.18%	(1.88%)	(0.49%)
CONTINGENCY RESERVE	30,294,000	28,723,000	30,064,000	31,048,000	31,643,000	32,252,000
TOTAL BASE EXPENDITURES (w/o ADDITIONS)	1,046,330,260	881,135,000	914,782,000	938,984,000	954,990,000	973,259,000
		(15.79%)	3.82%	2.65%	1.70%	1.91%

OPERATING MARGIN

	ADOPTED 2008-2009	FORECAST 2010	2011	2012	2013	2014
BASE EXPENDITURES (w/o COMMITTED ADDITIONS)						
GRAND TOTAL REVENUE	1,021,099,778	824,948,000	834,262,000	863,139,000	890,029,000	921,065,000
GROWTH RATE		(19.21%)	1.13%	3.46%	3.12%	3.49%
TOTAL BASE EXPENDITURES (w/o COMMITTED ADDITIONS)	1,046,330,260	881,135,000	914,782,000	938,984,000	954,990,000	973,259,000
GROWTH RATE		(15.79%)	3.82%	2.65%	1.70%	1.91%
OPERATING MARGIN CHANGE		(56,187,000)	(24,333,000)	4,675,000	10,884,000	12,767,000
<i>From Prior Year</i>						

February 2009 Forecast
EXPENDITURE SUMMARY

	ADOPTED <u>2008-2009</u>	FORECAST <u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
COMMITTED ADDITIONS:						
Additional Police Officers (25 annually until 2011-2012)		1,754,000	5,019,000	8,460,000	10,325,000	10,849,000
County Pocket Annexations (Transportation)		298,000	478,000	478,000	478,000	478,000
New Parks and Recreation Facilities Maintenance and Operations		130,000	1,048,000	1,619,000	1,925,000	2,107,000
New Traffic Infrastructure Assets Maintenance and Operations		204,000	397,000	550,000	649,000	749,000
Measure O (Library) Maintenance and Operations		773,000	4,088,000	5,164,000	5,529,000	5,557,000
Measure P (Parks) Maintenance and Operations		889,000	2,251,000	2,734,000	2,723,000	2,786,000
Measure O (Public Safety) Maintenance and Operations: Fire		9,000	507,000	2,610,000	2,693,000	2,763,000
Measure O (Public Safety) Maintenance and Operations: Police		749,000	1,808,000	1,865,000	1,895,000	1,928,000
Retiree Healthcare Benefits		199,000	1,819,000	3,527,000	5,186,000	6,846,000
TOTAL COMMITTED ADDITIONS	0	5,005,000	17,415,000	27,007,000	31,403,000	34,063,000
TOTAL BASE EXPENDITURES (w/ COMMITTED ADDITIONS)	1,046,330,260	886,140,000	932,197,000	965,991,000	986,393,000	1,007,322,000
		(15.31%)	5.20%	3.63%	2.11%	2.12%

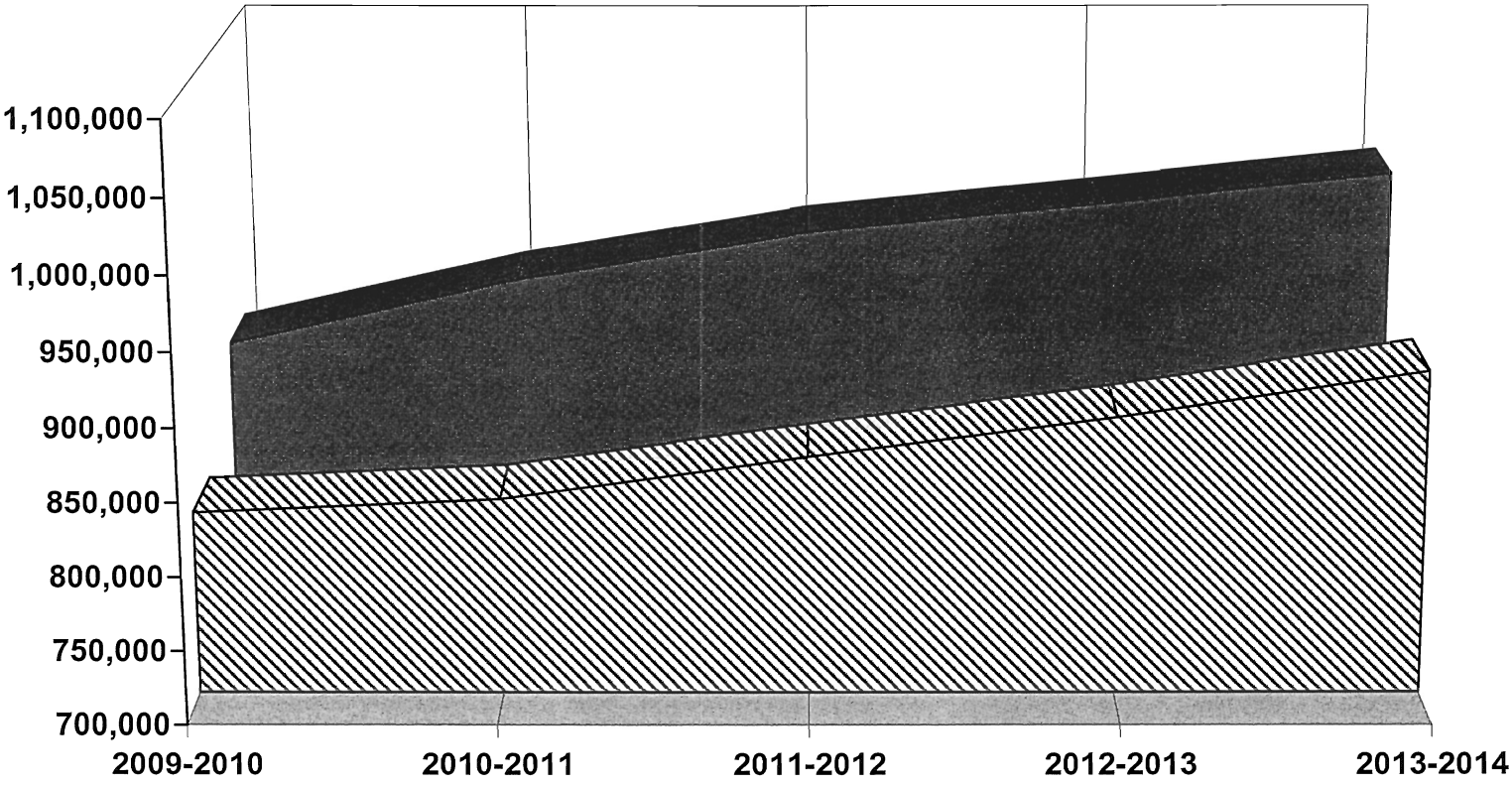
OPERATING MARGIN

	ADOPTED <u>2008-2009</u>	FORECAST <u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
BASE EXPENDITURES (w/ COMMITTED ADDITIONS)						
GRAND TOTAL REVENUE	1,021,099,778	824,948,000	834,262,000	863,139,000	890,029,000	921,065,000
GROWTH RATE		(19.21%)	1.13%	3.46%	3.12%	3.49%
TOTAL BASE EXPENDITURES (w/ COMMITTED ADDITIONS)	1,046,330,260	886,140,000	932,197,000	965,991,000	986,393,000	1,007,322,000
GROWTH RATE		(15.31%)	5.20%	3.63%	2.11%	2.12%
ONGOING OPERATING MARGIN CHANGE		(61,192,000)	(36,743,000)	(4,917,000)	6,488,000	10,107,000
<i>From Prior Year</i>						

ONE-TIME FUNDING AVAILABLE

2009-2010 Future Deficit Reserve	4,000,000
Airport West Proceeds Reserve	2,300,000
TOTAL ONE-TIME FUNDING	6,300,000

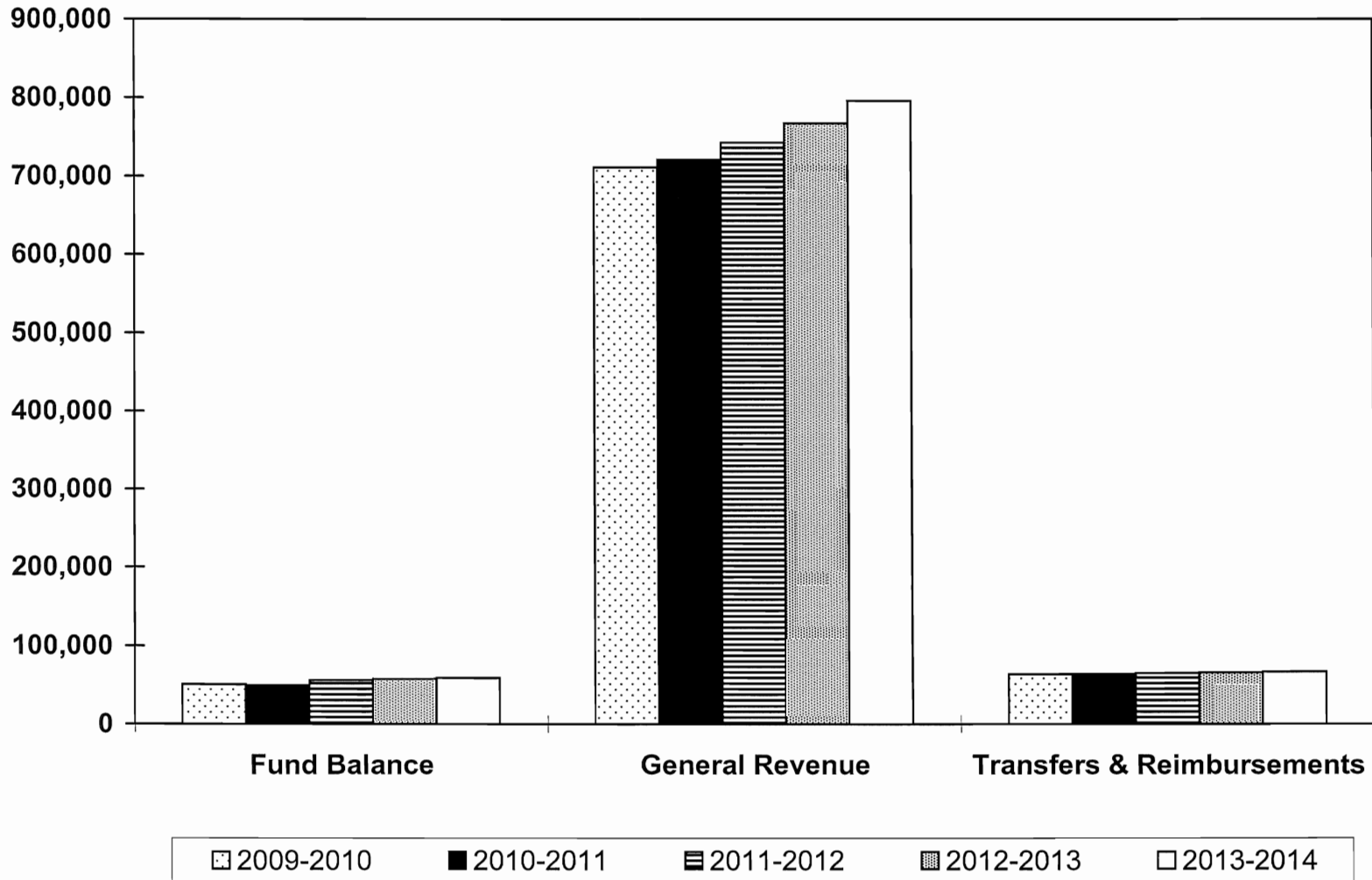
**2010-2014 General Fund Forecast
PROJECTED REVENUES AND EXPENDITURES
(\$ in thousands)**



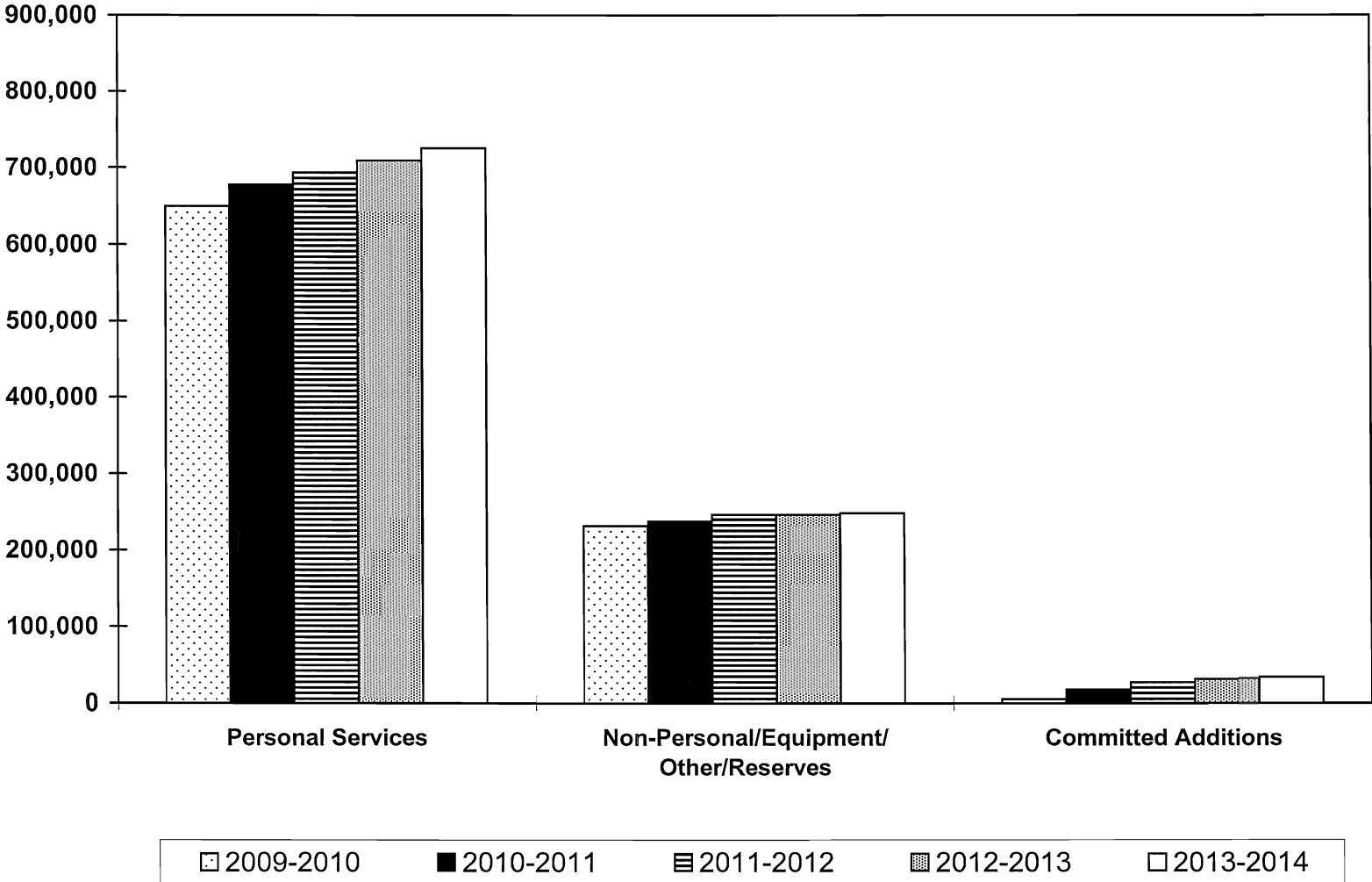
▨ BASE CASE REVENUES

■ BASE EXPENDITURES W/COMMITTED ADDS

**2010-2014 General Fund Forecast
FIVE-YEAR SOURCE OF FUNDS COMPARISON
(\$ in thousands)**



**2010-2014 General Fund Forecast
FIVE-YEAR USE OF FUNDS COMPARISON
(\$ in thousands)**



2010-2014 FORECAST
COMMITTED ADDITIONS TO THE BASE GENERAL FUND FORECAST

As has been our practice, potential future year program additional expenses in the General Fund considered virtually assured have been included in a “committed” additions section of the General Fund Forecast.

Committed additions involve expense changes that are deemed relatively unavoidable. The majority of items included in this category are additional maintenance and operating expenses that will be required to operate and maintain funded capital projects that will be completed within the five-year horizon of this forecast. This includes the expenses related to the hiring of 25 additional police officers each year until 2011-2012; county pocket annexations expenses; maintenance and operations of new street improvements, new parks and library facilities, and new community and public safety facilities; and retiree healthcare costs. It should be noted, however, that the projected costs included in this category have been submitted by the various departments involved, but have not yet been fully analyzed by the Budget Office. It can be anticipated that refinements of these estimates would be performed prior to bringing them forward for consideration by the City Council.

A summary of capital projects included in this Forecast is provided below and detailed in Chart A at the end of this section. In addition, based on the City Council’s adoption of Budget Principle #8 during the 2008-2009 budget process, a **General Fund Capital Operating and Maintenance/Budget Principle** discussion is included in this section. Capital projects with operating and maintenance costs over \$100,000 and included in approved Capital Improvement Program or Redevelopment Agency Budgets are identified in Chart B. However, there are four potential projects where funding has not yet been approved through the City Capital Improvement Program or Redevelopment Agency Capital Budget. Certification for these projects and other identified projects that have not been approved by the City Council will be sought as part of the 2010-2014 Proposed Capital Improvement Program. If certified by the City Council, the operating and maintenance costs associated with these facilities would then be included in subsequent General Fund Five-Year Forecast documents.

Following is a summary of Committed Additions included in the General Fund Five-Year Forecast. Projections factor in an inflation escalator for the out years of the forecast and are cumulative, not incremental.

COMMITTED ADDITIONS

Additional Police Officers (25 annually) – This item, new to the forecast, reflects the projected costs that will be necessary to fund 25 new police officers annually through 2011-2012 to help meet identified priorities, such as addressing the rise in property crimes and improving community policy and traffic calming as directed by the City Council’s approval of the Mayor’s 2008-2009 June Budget Message.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
1,754,000	5,019,000	8,460,000	10,325,000	10,849,000

2010-2014 FORECAST
COMMITTED ADDITIONS TO THE BASE GENERAL FUND FORECAST

COMMITTED ADDITIONS (CONT'D.)

County Pocket Annexations (Transportation) – This category provides funding necessary to maintain the properties that will be annexed into the City from unincorporated islands within the City of San José’s Urban Service Area. Approximately 40 miles of public streets and related infrastructure, such as streetlights, sidewalks, traffic signs, roadway markings, and trees will require ongoing maintenance, repair and rehabilitation work.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
298,000	478,000	478,000	478,000	478,000

New Parks and Recreation Facilities Maintenance and Operations – As detailed in Chart A, this category reflects the projected additional costs of maintaining and operating new parks and recreation facilities included in the City’s Five-Year Capital Improvement Program, including those that will be developed by other agencies such as the City’s Redevelopment Agency.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
130,000	1,048,000	1,619,000	1,925,000	2,107,000

New Traffic Infrastructure Assets Maintenance and Operations – As detailed in Chart A, this category reflects the projected additional costs that will be necessary to maintain new traffic signals, landscaping, and street lighting included in the City’s Five-Year Capital Improvement Program.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
204,000	397,000	550,000	649,000	749,000

Measure O (Library) Maintenance and Operations – As detailed in Chart A, this category reflects the projected additional maintenance and operations costs of new and expanded branch libraries that were approved in the November 2000 election. These include the East San José Carnegie, Seven Trees and the Santa Teresa branches in 2009-2010.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
773,000	4,088,000	5,164,000	5,529,000	5,557,000

2010-2014 FORECAST
COMMITTED ADDITIONS TO THE BASE GENERAL FUND FORECAST

COMMITTED ADDITIONS (CONT'D.)

Measure P (Parks) Maintenance and Operations – As detailed in Chart A, this category reflects the projected additional maintenance and operations costs of new and expanded parks and community facilities that were included as part of a bond measure approved in the November 2000 election. Some of the projects expected to be completed in 2009-2010 include the Happy Hollow Park and Zoo and Seven Trees Community Center.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
889,000	2,251,000	2,734,000	2,723,000	2,786,000

Measure O (Public Safety) Maintenance and Operations: Fire – As detailed in Chart A, this category reflects the projected additional maintenance and operations costs of new and expanded fire facilities that were included as part of a bond measure adopted by the voters in the March 2002 election. Included are the projected costs for new fire personnel that will be required. These include Fire Station 37 (South Willow Glen) in 2011-2012 and improvements to several other fire stations.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
9,000	507,000	2,610,000	2,693,000	2,763,000

Measure O (Public Safety) Maintenance and Operations: Police – As detailed in Chart A, this category reflects the projected additional maintenance and operations costs of new and expanded police facilities that were included as part of a bond measure adopted by the voters in the March 2002 election. Included are the projected costs for the South San José Substation and Emergency Communication (ECOMM) System Maintenance.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
749,000	1,808,000	1,865,000	1,895,000	1,928,000

**2010-2014 FORECAST
COMMITTED ADDITIONS TO THE BASE GENERAL FUND FORECAST**

COMMITTED ADDITIONS (CONT'D.)

Retiree Healthcare Benefits – This item, new to the forecast, is the phase-in over five years of the City’s share of the General Fund annual required contribution for retiree healthcare benefits for non-POA employees. In 2009-2010, the costs are \$199,000 and grow to \$6.8 million by the fifth year of the forecast period. In addition to these amounts, additional costs for retiree healthcare benefits are displayed elsewhere in this document and include \$2.4 million (in the first year and by inflated amounts in all out years) in the Personal Services category consistent with the recently negotiated funding agreement for this liability with the POA. In total, an additional \$16.7 million is required over the next five-year period to phase-in retiree healthcare benefits to full funding.

<u>2009-2010</u>	<u>2010-2011</u>	<u>2011-2012</u>	<u>2012-2013</u>	<u>2013-2014</u>
199,000	1,819,000	3,527,000	5,186,000	6,846,000

GENERAL FUND CAPITAL OPERATING AND MAINTENANCE/BUDGET PRINCIPLE #8

As part of the 2008-2009 budget process, the City Council adopted the Budget Principles recommended in the Mayor’s March 2008 Budget Message. Budget Principle #8 pertains to Capital Improvement Projects and directs that capital improvement projects with annual operating and maintenance costs “shall not proceed for projects with annual operating and maintenance costs exceeding \$100,000 in the General Fund without City Council certification that funding will be made available in the applicable year of the cost impact. Certification shall demonstrate that funding for the entire project, including operations and maintenance costs, will not require a decrease in existing basic neighborhood services.”

Chart A details a list of all project operations and maintenance costs assumed in this Forecast. In addition, a detailed list of projects is included in Chart B for capital projects that are underway or were previously approved by the City Council with annual operating and maintenance costs in the General Fund greater than \$100,000. Funding for these projects have been included as part of approved Capital Improvement Programs or Redevelopment Agency Budgets. The majority of these costs are associated with the voter-approved General Obligation bonds for Park, Library, and Public Safety facilities. The operating and maintenance costs for these facilities are included in the figures presented in this Preliminary General Fund Forecast. It should be noted that, by 2013-2014, the annualized costs to operate and maintain the City Council/Agency Board approved facilities with annual operating and maintenance costs in the General Fund greater than \$100,000 are projected at \$14.4 million annually. In total, all operating and maintenance costs for capital projects are forecasted to be \$15.9 million annually by the end of the five-year period.

All operating and maintenance costs for these facilities, however, will be evaluated on an annual basis for inclusion in subsequent Five-Year General Fund Forecasts. As part of this evaluation,

2010-2014 FORECAST
COMMITTED ADDITIONS TO THE BASE GENERAL FUND FORECAST

GENERAL FUND CAPITAL OPERATING AND MAINTENANCE/BUDGET
PRINCIPLE #8 (CONT'D.)

the costs and staffing necessary to operate and maintain these facilities may change as further analysis on the operational needs of each facility are conducted. Notably, further analysis may be required to determine the actual staffing of Fire Station 37. For purposes of this document, the operating and maintenance costs for Fire Station 37 – Willow Glen reflect the assumption that no staff would be relocated from Fire Station 6, and that a new Fire Engine (four additional duty positions) would staff that facility. This assumption is consistent with the “*City-Wide Policy for the Relocation/Closure and/or Selling Fire Stations and Removal of Fire Station 6 from the Budget,*” approved by the City Council on September 9, 2008. The additional annual General Fund operating and maintenance costs projected for this facility alone represents \$2.5 million in 2011-2012, the first full year of operations.

Additional operating and maintenance costs are identified for other (non-General Obligation Bond) City Council-approved projects. The General Fund costs associated to operate and maintain these facilities are projected at \$1.6 million annually in 2013-2014. These facilities include projects such as the Edenvale Community Center approved by the City Council on September 23, 2008 and a planned Hoffman/Via Monte Neighborhood Center included as part of the approved Redevelopment Agency Capital Budget.

Lastly, four potential projects where funding has not yet been approved through the City Capital Improvement Program or Redevelopment Agency Capital Budget are identified. These projects are under very preliminary development and if approved, are anticipated to have an annualized operating and maintenance impact of at least \$2.3 million by 2013-2014. Consistent with the direction approved as part of Budget Principle #8, for purposes of this Forecast, these operating and maintenance costs are not included as part of the General Fund Five-Year Forecast “Committed Additions” category. Consistent with the budget principle, certification for these projects and other identified projects that have not been approved by the City Council will be sought as part of the 2010-2014 Proposed Capital Improvement Program. If certified by the City Council, the operating and maintenance costs associated with these facilities would then be included in subsequent General Fund Five-Year Forecast documents.

**CHART A - 2010-2014 GENERAL FUND FORECAST
Operating Impact of Capital Programs**

	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014
NEW PARK AND RECREATION FACILITIES MAINTENANCE AND OPERATIONS					
Aborn Park Playground Improvements	0	5,000	5,000	5,000	6,000
Almaden Apartments Area Park	0	20,000	20,000	20,000	20,000
Carolyn Norris Turnkey Park	0	9,000	18,000	18,000	18,000
Chelmers Park Development	0	18,000	35,000	35,000	35,000
Kirk Community Center Renovation	53,000	84,000	83,000	84,000	84,000
Martial-Cottle Community Garden	0	0	20,000	41,000	41,000
Martin Park Expansion	0	61,000	74,000	75,000	76,000
Newhall Neighborhood Park	0	20,000	20,000	20,000	20,000
Nisich Park Development	0	8,000	15,000	15,000	15,000
Tamien Specific Plan Area Park	0	0	18,000	35,000	35,000
TRAIL: Albertson Parkway	33,000	34,000	35,000	35,000	36,000
Vietnamese Heritage Garden	19,000	0	0	0	127,000
Edenvale Community Center (RDA)	0	482,000	733,000	737,000	742,000
Hoffman/Via Monte Neighborhood Center (RDA)	0	0	0	199,000	200,000
Mabury Park/Commodore Children's Park	0	0	112,000	114,000	117,000
Mayfair Park (RDA)	0	0	0	20,000	21,000
TRAIL: Los Gatos Creek Reach 5a	19,000	19,000	20,000	20,000	21,000
TRAIL: Lower Silver Creek	0	17,000	24,000	32,000	41,000
TRAIL: Penitencia Creek Reach I	0	20,000	20,000	21,000	21,000
TRAIL: Penitencia Creek Reach VI	0	5,000	5,000	5,000	5,000
TRAIL: Willow Glen Spur Acquisition	0	0	66,000	67,000	69,000
TRAIL: Willow Glen Spur Reach V (Developer)	6,000	6,000	6,000	6,000	6,000
Scottish Rite Parksite (Venetian Terrace)	0	18,000	18,000	18,000	18,000
Watson Park Remediation	0	32,000	32,000	33,000	34,000
Baypointe Turnkey Park	0	24,000	24,000	24,000	24,000
Cadance Turnkey Park	0	5,000	5,000	5,000	5,000
Eden Court Housing	0	0	15,000	15,000	15,000
Goble Lane Turnkey Park and Tot Lot	0	25,000	25,000	25,000	25,000
Japantown Turnkey Park and Tot Lot	0	15,000	15,000	15,000	15,000
King/Dobbin Site Turnkey Park and Tot Lot	0	15,000	15,000	15,000	15,000
Legacy Turnkey Park	0	2,000	2,000	2,000	2,000
North San Pedro Turnkey Park and Tot Lot	0	15,000	15,000	15,000	15,000
Piercy/Tennant Site Tot Lot	0	8,000	15,000	15,000	15,000
River Oaks Turnkey Park	0	0	28,000	58,000	60,000
Riverview Turnkey Park	0	0	0	0	27,000
Vista Montana Turnkey Park and Tot Lot	0	81,000	81,000	81,000	81,000
TOTAL NEW PARK AND RECREATION FACILITIES MAINTENANCE AND OPERATIONS	130,000	1,048,000	1,619,000	1,925,000	2,107,000
NEW TRAFFIC INFRASTRUCTURE ASSET MAINTENANCE AND OPERATIONS					
Traffic Projects - Forecast	63,000	66,000	90,000	93,000	97,000
Traffic Light Synchronization Project	33,000	67,000	100,000	100,000	100,000
Landscape Maint - New Infra Assets and Op Costs	108,000	264,000	360,000	456,000	552,000
TOTAL NEW TRAFFIC INFRASTRUCTURE ASSET MAINTENANCE AND OPERATIONS	204,000	397,000	550,000	649,000	749,000
MEASURE O (LIBRARY) MAINTENANCE AND OPERATIONS					
Bascom Branch	0	1,308,000	1,396,000	1,401,000	1,405,000
Calabazas Branch	(28,000)	327,000	782,000	783,000	786,000
East San José Carnegie	153,000	157,000	160,000	162,000	165,000
Educational Park Branch	(34,000)	914,000	993,000	997,000	1,002,000
Santa Teresa Branch	288,000	315,000	318,000	322,000	327,000
Seven Trees Branch	394,000	1,067,000	1,072,000	1,074,000	1,079,000
Southeast	0	0	443,000	790,000	793,000
TOTAL MEASURE O (LIBRARY) MAINTENANCE AND OPERATIONS	773,000	4,088,000	5,164,000	5,529,000	5,557,000
MEASURE P (PARKS) MAINTENANCE AND OPERATIONS					
Bascom Community Center	53,000	735,000	744,000	746,000	747,000
Happy Hollow Park & Zoo	545,000	84,000	36,000	0	0
Soccer Complex	0	295,000	521,000	529,000	550,000
Softball Complex	0	380,000	670,000	679,000	713,000
Seven Trees Community Center	291,000	757,000	763,000	769,000	776,000
TOTAL MEASURE P (PARKS) MAINTENANCE AND OPERATIONS	889,000	2,251,000	2,734,000	2,723,000	2,786,000

**CHART A - 2010-2014 GENERAL FUND FORECAST
Operating Impact of Capital Programs**

	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014
MEASURE O (PUBLIC SAFETY) MAINTENANCE AND OPERATIONS: FIRE					
Fire Station 36 - Silver Creek/Yerba Buena - Maint/Util	0	44,000	69,000	70,000	71,000
Fire Station 19 - Maintenance and Utilities	9,000	21,000	22,000	22,000	23,000
Fire Station 21 - Maintenance and Utilities	0	0	14,000	21,000	22,000
Fire Station 37 - South Willow Glen - Staffing/NP	0	418,000	2,443,000	2,513,000	2,578,000
Fire Station 37 - South Willow Glen - Maint/Util	0	0	33,000	37,000	38,000
Fire Station 2 - Rebuild - Maintenance and Utilities	0	24,000	29,000	30,000	31,000
TOTAL MEASURE O (PUBLIC SAFETY) MAINTENANCE AND OPERATIONS: FIRE	9,000	507,000	2,610,000	2,693,000	2,763,000
MEASURE O (PUBLIC SAFETY) MAINTENANCE AND OPERATIONS: POLICE					
South San José Police Substation	627,000	1,564,000	1,582,000	1,600,000	1,619,000
E-COMM Public Safety System Maintenance	122,000	223,000	231,000	241,000	252,000
Driver Training Facility	0	21,000	52,000	54,000	57,000
TOTAL MEASURE O (PUBLIC SAFETY) MAINTENANCE AND OPERATIONS: POLICE	749,000	1,808,000	1,865,000	1,895,000	1,928,000
TOTAL OPERATING IMPACT OF CAPITAL PROGRAMS	2,754,000	10,099,000	14,542,000	15,414,000	15,890,000

CHART B - 2010-2014 GENERAL FUND FORECAST
Capital Projects - Operating and Maintenance Costs Greater than \$100,000 Annually

CITY COUNCIL-APPROVED GENERAL OBLIGATION BOND CAPITAL PROJECTS

PUBLIC SAFETY	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014
E-COMM Public Safety System Maintenance	122,000	223,000	231,000	241,000	252,000
Fire Station 37 - Willow Glen	0	418,000	2,476,000	2,550,000	2,616,000
South San José Police Substation	627,000	1,564,000	1,582,000	1,600,000	1,619,000
LIBRARY					
Bascom Branch	0	1,308,000	1,396,000	1,401,000	1,405,000
Calabazas Branch	(28,000)	327,000	782,000	783,000	786,000
East San José Carnegie Branch	153,000	157,000	160,000	162,000	165,000
Educational Park Branch	(34,000)	914,000	993,000	997,000	1,002,000
Santa Teresa Branch	288,000	315,000	318,000	322,000	327,000
Seven Trees Branch	394,000	1,067,000	1,072,000	1,074,000	1,079,000
Southeast Branch	0	0	443,000	790,000	793,000
PARKS					
Bascom Community Center	53,000	735,000	744,000	746,000	747,000
Happy Hollow Park and Zoo	545,000	84,000	36,000	0	0
Soccer Complex	0	295,000	521,000	529,000	550,000
Softball Complex	0	380,000	670,000	679,000	713,000
Seven Trees Community Center	291,000	757,000	763,000	769,000	776,000
Total O&M - City-Council Approved GO Bond Capital Projects	2,411,000	8,544,000	12,187,000	12,643,000	12,830,000

OTHER CITY COUNCIL-APPROVED CAPITAL PROJECTS

	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014
Edenvale Community Center	0	482,000	733,000	737,000	742,000
Mabury Park/Commodore Children's Park	0	0	112,000	114,000	117,000
Transporation Infrastructure - New Assets	108,000	264,000	360,000	456,000	552,000
Hoffman/Via Monte Neighborhood Center (RDA)	0	0	0	199,000	200,000
Total O&M - Other City-Council Approved Capital Projects	108,000	746,000	1,205,000	1,506,000	1,611,000

TOTAL - CAPITAL PROJECTS WITH OPERATING AND MAINTENANCE COSTS GREATER THAN \$100,000 ANNUALLY	2,519,000	9,290,000	13,392,000	14,149,000	14,441,000
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OTHER POTENTIAL FUTURE CAPITAL PROJECTS WITH OPERATING AND MAINTENANCE COSTS GREATER THAN \$100,000 ANNUALLY (NOT INCLUDED IN FORECAST)

Emma Prusch Park - Back Acreage Development			395,000	398,000	402,000
Festival Site (RDA)	TBD				
Future Trail Projects		55,000	175,000	297,000	421,000
Meadowfair Community Center (RDA)					1,484,000
Total O&M - Other Potential Future Capital Projects with Operating and Maintenance Costs Greater than \$100,000 Annually (Not Included in Forecast)	-	55,000	570,000	695,000	2,307,000

**2010-2014 General Fund Forecast
PROJECTED FIVE-YEAR OPERATING MARGINS
Alternate Forecast Scenarios**

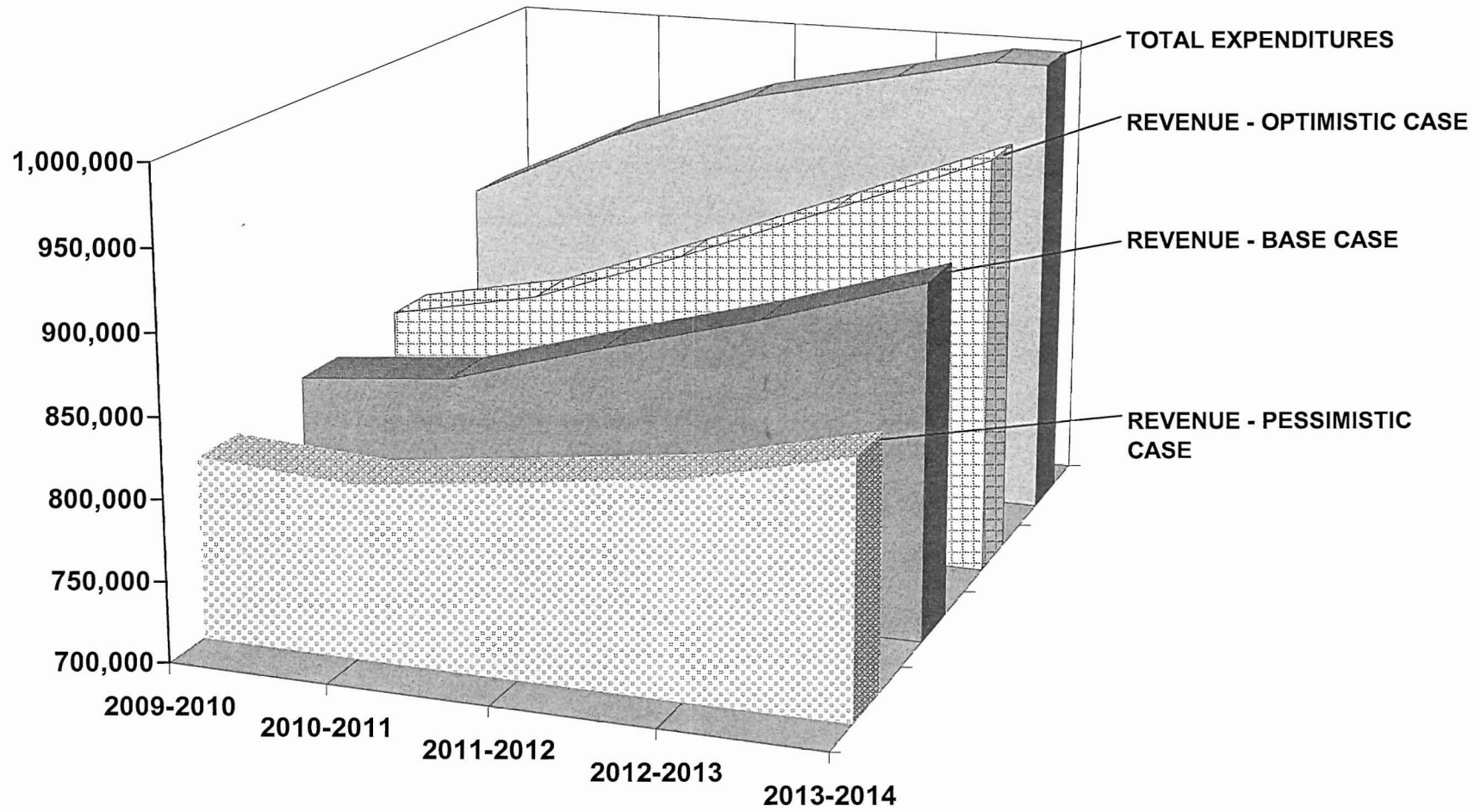
	BASE CASE				
	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
TOTAL REVENUES (\$)	824,948,000	834,262,000	863,139,000	890,029,000	921,065,000
GROWTH RATE		1.13%	3.46%	3.12%	3.49%
TOTAL EXPENDITURES (\$)	886,140,000	932,197,000	965,991,000	986,393,000	1,007,322,000
GROWTH RATE		5.20%	3.63%	2.11%	2.12%
OPERATING MARGIN - BASE	(61,192,000)	(36,743,000)	(4,917,000)	6,488,000	10,107,000

	OPTIMISTIC CASE				
	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
TOTAL REVENUES (\$)	832,403,000	852,274,000	888,149,000	926,866,000	965,603,000
GROWTH RATE		2.39%	4.21%	4.36%	4.18%
TOTAL EXPENDITURES (\$)	886,140,000	932,197,000	965,991,000	986,393,000	1,007,322,000
GROWTH RATE		5.20%	3.63%	2.11%	2.12%
OPERATING MARGIN - OPTIMISTIC	(53,737,000)	(26,186,000)	2,081,000	18,315,000	17,808,000

	PESSIMISTIC CASE				
	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
TOTAL REVENUES (\$)	813,097,000	807,056,000	819,377,000	832,430,000	856,056,000
GROWTH RATE		(0.74%)	1.53%	1.59%	2.84%
TOTAL EXPENDITURES (\$)	886,140,000	932,197,000	965,991,000	986,393,000	1,007,322,000
GROWTH RATE		5.20%	3.63%	2.11%	2.12%
OPERATING MARGIN - PESSIMISTIC	(73,043,000)	(52,098,000)	(21,473,000)	(7,349,000)	2,697,000

2010-2014 General Fund Forecast
FIVE-YEAR PROJECTION OF GENERAL FUND REVENUES AND EXPENDITURES
Alternate Forecast Scenarios
 (\$ in thousands)

IV - 2



GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

BACKGROUND

At the direction of the City Council, the City Manager released the General Fund Structural Deficit Elimination Plan (Plan) in November 2008. This Plan outlined specific strategies and timelines to eliminate the structural budget deficit over a five year timeframe ending in fiscal year 2013-2014. The Plan was based on revenue and expenditures projections as of the November 2008 Preliminary General Fund Forecast and included input from the General Fund Structural Deficit Elimination Plan Stakeholder Group that convened in the spring and summer of 2008. The Plan explains in full both the problem the City faces and the potential solutions outlined over a five year period. The document was discussed at a City Council Study Session on December 5, 2008 and is available online at:

www.sanjoseca.gov/budget/FY0809/GFStructuralDeficitEliminationPlan112008.pdf

The Plan serves as a policy guide and operational blueprint to assist the City Administration in closing the structural budget deficit while maintaining organizational sustainability. It offers the City options to best meet the fiscal needs of the City within each fiscal year. As conditions change in the greater economy and within the San José community, the Plan too can adapt to reach the end goal of closing the General Fund structural budget deficit.

In this report, the Plan has been updated to reflect revised five-year revenue and expenditure projections as outlined in the General Fund Forecast sections of this document. Based on these revised projections, the General Fund structural deficit is expected to total almost \$116 million over the next five years, with a shortfall of approximately \$67 million in 2009-2010. This reflects an increase from the total shortfall figure of \$106 million estimated in November 2008.

2010-2014 General Fund Structural Deficit Projection (February 2009) (\$ in Millions)

	2009-2010	2010-2011	2011-2012*	2012-2013*	2013-2014*	Total
Projected Base Shortfall (Feb 2009 Forecast)**	(\$61.2)	(\$36.7)	(\$4.9)	\$6.5	\$10.1	(\$86.2)
Unmet/Deferred Infrastructure & Maintenance Needs***	(\$5.9)	(\$5.9)	(\$5.9)	(\$5.9)	(\$5.9)	(\$29.5)
Total Incremental Deficit	(\$67.1)	(\$42.6)	(\$10.8)	\$0.6	\$4.2	(\$115.7)
Total Cumulative Deficit	(\$67.1)	(\$109.7)	(\$120.5)	(\$119.9)	(\$115.7)	(\$115.7)

* Funding for cost-of-living salary increases not factored into the last three years of the Forecast. These increases are being treated as a resource allocation policy decision.

** Includes City's share of General Fund annual required contribution for retiree health care benefits and committed additions previously agreed upon by Council, such as addition of 25 officers annually through 2011-12 and operating and maintenance funding for capital projects coming on line.

*** Does not address one-time needs of \$457 million in the General Fund (\$825 million all funds).

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

BACKGROUND (CONT'D.)

As forecasted revenues and expenditures change over time, the strategies set forth in the Plan will be modified to account for these changes. Although the underlying problem remains, outside economic conditions will make cost savings and revenue projections very volatile. The economic conditions may also impact implementation considerations and timing of strategies. As discussed below, the Plan will continue to be updated as additional information becomes available.

It is important to note that many strategies are being considered to resolve the General Fund shortfall as the Administration develops the 2009-2010 Proposed Operating Budget. The 2009-2010 portion of the Plan will be updated as numbers are further refined, strategy implementation feasibility is evaluated, and other departmental budget proposals are analyzed. These changes will be integrated into the 2009-2010 Proposed Operating Budget, to be released on May 1, 2009.

The below section outlines revisions to key strategies to reflect updated revenue and expenditure projections in this 2010-2014 General Fund Five-Year Forecast. A brief discussion of new strategies under consideration is also included.

EXISTING STRATEGIES UPDATE

Since the Elimination Plan release in November 2008, the City has been actively refining strategies and taking steps to implement those slated for specific fiscal years. All strategies outlined in the document are still under consideration by the City Administration. The estimated cost savings or revenue generation from specific strategies will be updated as current overall budget projections are adjusted. The table below highlights the updated potential cost savings/revenue by strategy category and fiscal year. These updated strategy estimates are discussed by category in the following sections.

Strategy Type	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	Five-Year Total
Cost Savings Strategies	\$2.5M	\$7.7M	\$7.6M	\$8.7M	\$10.1M	\$36.6M
Revenue Strategies	\$3.3M	\$6.3-12.0M	\$6.2-16.0M	\$4.0-8.0M	\$4.0-8.0M	\$23.8-47.3M
Service Reductions/ Eliminations	\$61.3M	\$22.9-29.6M	\$9.4M	\$0.0M	\$0.0M	\$93.6-100.3M
Total	\$67.1M	\$36.9-49.3M	\$23.2-33.0M	\$12.7-16.7M	\$14.1-18.1M	\$154.0-184.2M

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

EXISTING STRATEGIES UPDATE (CONT'D.)

Cost Savings Strategies

Initial optimization studies for City programs are currently underway to achieve cost savings in 2009-2010. For example, optimization studies for the School Crossing Guard program is in progress with results expected later in 2008-2009. As the initial Plan outlined, the City's efforts for optimization studies will increase over time with first investments producing smaller results. Greater results are expected in the later years as the City gains experience with these efforts. To that end, the City is identifying and then taking steps towards reviews of additional programs for the next fiscal year.

Another important strategy within the Cost Savings category is to reduce the rate of increase in personnel costs. Personnel cost savings will vary based on the outcome of contract negotiations with the various bargaining units and will occur according to the timeline of contract expirations. The annual budget will reflect the impacts of labor contracts as they are negotiated.

Revenue Strategies

The current economic climate has impacted the City's revenue projections as outlined in this Forecast and has also impacted the projected value of revenue strategies identified to address the General Fund structural deficit. These revenue strategies are now being developed at the bottom end of an economic cycle making the implementation of such strategies much more difficult. As economic conditions improve over time, these strategies are expected to generate additional revenue. In order to meet the goal of addressing the structural deficit over the next five years, however, it is necessary to use the most current, updated revenue projections as the basis for determining the projected benefits of the proposed revenue strategies. This methodology should be conservative and may understate the long-term impacts of these additional revenue sources.

As an example, since the release of the Plan in November, the deep global recession has resulted in downward revisions to some of the specific revenue generation projections. For instance, the strategy to increase Conveyance Tax was projected at \$11.4 million in the Plan based on the November 2008 Preliminary Forecast. Given the current projections, the same increase would now produce \$10.8 million, a drop of \$620,000. The affect on changes to the Business License Tax are less certain and dependent on the type of change pursued but the overall revenue from the existing tax is projected to be lower based on current collection trends. The revenue estimate for 2009-2010 has been adjusted downward from the November 2008 Preliminary Forecast by \$1.3 million, to approximately \$12 million.

The development of an asset management program has been an ongoing priority for the City. The community review process on 40 underutilized properties authorized by the City Council in October 2008 is nearing completion. Based on public input, staff will begin bringing property disposition recommendations to the City Council in April 2009. Staff will report further on actual revenues as sales are completed. As a conservative estimate, the City projects \$300,000 in new revenues from the asset management program in 2009-2010, bringing the total to \$500,000 in 2009-2010.

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

EXISTING STRATEGIES UPDATE (CONT'D.)

Revenue Strategies (Cont'd.)

The strategy related to fees and fines has produced more proposals in 2009-2010 than initially projected. City departments have been examining ways to raise existing fees to market rates and/or to develop new fees to recover City costs. These efforts include a Parks, Recreation and Neighborhood Services systematic fee restructuring, including extensive community outreach, to bring service fees closer to cost recovery and increases to existing fines and fees including library late material return fines, parking citation fines, and Police false alarm fines.

Service Reductions/Eliminations Strategies

The largest portion of the Plan's 2009-2010 strategies is in the area of service reductions/eliminations. To address the projected General Fund shortfall in 2009-2010, departments were directed to submit budget proposals that would reduce the reliance on the General Fund by 17.4% to 21.7% for non-public safety departments, and 1.0% to 5.0% for public safety departments. These reduction targets were set at levels sufficient to generate between \$60 million and \$65 million in budget proposals. These proposals, which include a significant amount of service reductions and eliminations strategies, are under consideration and analysis for inclusion in the 2009-2010 Proposed Operating Budget. Based on the difficulty of addressing this magnitude of a shortfall with ongoing service reductions and eliminations, the Proposed Operating Budget may include the use of a limited amount of one-time funds to bridge the gap in the first fiscal year. Use of those funds may reduce the need for implementing some of the most severe service eliminations/reductions until other cost savings and revenues strategies are implemented and can assist in balancing the budget.

To help plan for service reductions, City staff, in conjunction with Management Partners, developed an Analytical Framework for Service Reductions/Eliminations for both external services and internal support services. The intent of the Framework is to identify services which can be reduced or eliminated, to prioritize among competing demands, and to develop meaningful data that can be used to improve or optimize service delivery. In January, City staff was trained on the use of the Analytical Framework and a "Training Guide for Use of Analytical Framework" was distributed to Senior Staff.

Each Department was asked to pilot the Framework with two to three programs and present results as part of the 2009-2010 budget process. It is anticipated that the Framework will be appropriately modified after the pilot stage and will be incorporated into the yearly budget process going forward. Although each program does not have to be evaluated using the Framework for 2009-2010, it is expected that over the five year life of the Elimination Plan, each program provided by the City to either external or internal customers will be considered with the Framework.

NEW STRATEGIES UNDER CONSIDERATION

Through budget balancing ideas submitted by City departments and other ongoing analysis, several new ideas for revenue generation are under study. Three strategies with the most

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

NEW STRATEGIES UNDER CONSIDERATION (CONT'D.)

revenue potential are discussed briefly below and will be incorporated into the 2009-2010 budget process or the November 2009 update to the General Fund Structural Deficit Elimination Plan as appropriate.

Sales Tax: As a result of expressed support in the Annual Community Telephone Survey and from the January 24, 2009 Neighborhood Association and Youth Commission Priority Setting Association, the City has refocused consideration of an increase to the local Sales Tax rate first mentioned in the December 2007 report *Development of Strategies to Address the City's General Fund Structural Budget Deficit*. At that time, it was estimated that a one-quarter percent increase would generate additional Sales Tax for the City of approximately \$38 million. Given the current economic climate, the same raise is now expected to generate approximately \$34 million; while a one-eighth percent increase would produce an estimated \$17 million in new revenue annually. However, since the recent passage of the State budget that included a sales tax rate increase of 1%, bringing the Santa Clara County rate to 9.25%, additional analysis would be necessary before including a sales tax increase in the out year of the Plan.

Construction Excise Tax and Building and Structure Construction Tax: The Construction Excise Tax is assessed upon the construction, alteration, repair, or improvement of any building or structure which is for residential or commercial purposes or is associated with a mobile home. The Building and Structure Construction Tax is imposed upon the construction, repair, or improvement of any building or structure where a building permit is required. These taxes are calculated as a percentage of the building valuation. The Municipal Code stipulates the calculation based on valuation tables published by the International Conference of Building Officials (ICBO). The ICBO last published a table in 1997 and the International Code Council (ICC) is now the industry standard and publishes updated building valuation tables. Based on current projections, an initial estimate indicates that updating the valuation tables would generate an additional \$3.0-\$3.7 million annually. The additional revenue generated would be impacted by overall development activity. The increase would vary based on different types of construction. Changing the building valuation tables would require a Municipal Code revision, and although further legal analysis is needed, it is possible that a new ordinance would allow either the City Council or Building Official to update valuation tables according to industry standards. The additional Construction Excise Tax revenue of \$1.5-\$1.9 million could be used in part or in total as part of the General Fund budget balancing strategy. Revenue from the Building and Structure Construction Tax, however, is restricted to specific traffic capital program activities. New revenue of \$1.5-1.8 million from that tax would be available to support traffic capital projects.

Disposal Facility Tax: This strategy could both raise the Disposal Facility Tax (DFT) rate to partially adjust for the consumer price index (CPI) and broaden it by removing most "cover material" exemptions which have been added over time. By ordinance, the City established the DFT in 1987 and revised the tax in 1992 to its current rate of \$13 per ton of solid waste for disposal sites. The tax currently generates approximately \$13 million per year. The flat rate structure has not been adjusted with the CPI. The City estimates that for every dollar per ton

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

NEW STRATEGIES UNDER CONSIDERATION (CONT'D.)

Disposal Facility Tax: (Cont'd.)

the DFT is raised, new revenue of approximately \$1 million annually would be realized. If the DFT was also broadened to remove most of the exempt "cover material," each raise in dollar per ton would produce approximately \$1.3 million in new revenue. Using these estimates, raising the DFT from \$13 to \$15 per ton would generate an additional \$2.0-\$2.6 million annually. The revenue is subject to numerous factors including the continued use of City disposal sites and the level of waste produced. This modest raise remains below competitor municipalities. The higher tax rate would have a small effect on residential ratepayers but would primarily impact commercial waste haulers. Any DFT extension or increase, including raising or broadening, requires voter approval and, if included in a further Plan update, may be an option to consider for a future ballot measure.

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

General Fund Structural Deficit Elimination Plan							
Net Impact of Strategies on General Fund*							
COST SAVINGS STRATEGIES	Fiscal Year:	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	Total
<p>1. Optimization and Service Delivery Model Reviews</p> <p>Review service delivery models through example strategies below:</p> <ul style="list-style-type: none"> a. Business process redesign (through employee involvement and empowerment) b. Use of technology to achieve efficiencies c. Insourcing/outourcing d. Streamlining e. Third-party program auditing f. Charter agencies (concept only) g. Employee engagement and suggestion program h. Use of public safety civilian positions i. Modify minimum Fire staffing policies where appropriate based on Fire Strategic Plan <p style="text-align: right;"><i>(Budget Balancing Guideline #7, 8, 10)</i></p>		\$0.5M	\$1.8M	\$2.7M	\$3.9M	\$5.2M	\$14.1M
<p>2. Increase San Jose Redevelopment Agency (SJRDA) support to General Fund</p> <p>Example ideas where SJRDA could fund projects which General Fund would otherwise support:</p> <ul style="list-style-type: none"> a. Prioritize SJRDA Capital Funding for Economic Development Activities b. Retrofit to smart lights in SJRDA areas c. Modernize parking meters in SJRDA areas d. Shift additional economic development, code enforcement activities in SJRDA areas <p style="text-align: right;"><i>(Budget Balancing Guideline #4, 7)</i></p>		\$1.0M	\$1.0M	\$1.0M	\$1.0M	\$1.0M	\$5.0M

* Does not include one-time implementation costs

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

General Fund Structural Deficit Elimination Plan							
Net Impact of Strategies on General Fund*							
COST SAVINGS STRATEGIES	Fiscal Year:	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	Total
3. Shift Healthy Neighborhood Venture Fund Funding to General Fund Assumes \$10M annual funding remains; shifts forecasted increases of tobacco settlement funds <i>(Budget Balancing Guideline #4, 7)</i>		—	\$1.2M	\$0.2M	\$0.1M	\$0.2M	\$1.7M
4. Reduce Rate of Increase in Personnel Costs Reduce personnel costs annually through strategies below and/or ideas developed from negotiations: <ul style="list-style-type: none"> a. Increase time, amount and method to reach maximum compensation b. Implement sick leave payment modifications upon retirement c. Implement a two-tier retirement benefit d. Revise workers' compensation program e. Implement workers' compensation offset for public safety f. Revise overtime eligibility policies g. Implement healthcare insurance provider cost containment h. Reduce entry level compensation for positions for which the City receives many qualified applicants i. Implement health care plan modifications j. Modify binding interest arbitration** <i>(Budget Balancing Guideline #12)</i>		\$1.0M	\$3.7M	\$3.7M	\$3.7M	\$3.7M	\$15.8M
COST SAVINGS STRATEGIES SUB-TOTAL		\$2.5M	\$7.7M	\$7.6M	\$8.7M	\$10.1M	\$36.6M

* Does not include one-time implementation costs

**Requires voter approval

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

General Fund Structural Deficit Elimination Plan

Net Impact of Strategies on General Fund*

REVENUE STRATEGIES	Fiscal Year:	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	Total
5. Formalize and Implement a Rigorous Asset Management Program <i>(Budget Balancing Guideline #4)</i>		\$0.3M	\$1.0M	\$1.0–4.0M	\$1.0–4.0M	\$1.0–4.0M	\$4.3–13.3M
6. Ensure Current Fees Fully Cover All City Costs and Institute New Fees where Appropriate Develop new fees/fines and bring existing fees to full cost recovery where appropriate Examples include: a. Advance planning fee b. Parking fees/fines c. Entertainment Zone Policing Plan d. Parks, Recreation and Neighborhood Services fee structure e. Existing fee/fine increases <i>(Budget Balancing Guideline #3)</i>		\$3.0M	\$2.0M	\$2.0M	\$2.0M	\$2.0M	\$11.0M
7. Actively Pursue and Promote Economic Development Opportunities Examples include: a. Expansions of Santana Row and Valley Fair b. Business cooperative program c. Preparing retail development sites <i>(Budget Balancing Guideline #1, 4)</i>		—	\$1.0M	\$1.0–2.0M	\$1.0–2.0M	\$1.0–2.0M	\$4.0–7.0M
8. Restructure Business Tax Rates to Modernize and Reflect Current Business Profile** Examples include: a. Modernize rates by indexing to current consumer price index (CPI) and raising maximums b. Restructure business tax formula <i>(Budget Balancing Guideline #4)</i>		—	\$1.0–6.5M	\$1.0–6.5M	—	—	\$2.0–13.0M

* Does not include one-time implementation costs

**Requires voter approval

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

General Fund Structural Deficit Elimination Plan							
Net Impact of Strategies on General Fund*							
REVENUE STRATEGIES	Fiscal Year:	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	Total
9. Implement Landscape and Lighting District** Explore various landscape and lighting district options to cover costs related to the City's transportation infrastructure assets and operations <i>(Budget Balancing Guideline #4)</i>		—	\$1.3-1.5M	\$1.2-1.5M	—	—	\$2.5-3.0M
Library Parcel Tax Renewal** <i>Not a new strategy but will impact future ballot decisions; sunsets in 2014</i>							

* Does not include one-time implementation costs

**Requires voter approval; Landscape and Lighting District is mail-in ballot of property owners

**GENERAL FUND STRUCTURAL DEFICIT
ELIMINATION PLAN UPDATE**

General Fund Structural Deficit Elimination Plan						
Net Impact of Strategies on General Fund*						
OTHER REVENUE STRATEGIES (not included in subtotal below)						
Fiscal Year:	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	Total
10. Increase Revenues from Visitors Who Benefit from General Fund Services** a. Parking lot tax of 10% on City and SJRDA owned lots b. Parking lot tax of 10% on all public and private lots <i>(Budget Balancing Guideline #4)</i>	—	a) \$2.6M b) \$4.5M	a) \$2.6M b) \$4.5M	—	—	\$5.2-9.0M
11. Increase Conveyance Tax and/or Shift Construction and Conveyance Tax Funding from Capital Projects to Operations and Maintenance** Increase by 50%; with a shift of up to 40% of parks allocation to park maintenance and maintaining current allocation <i>(Budget Balancing Guideline #9)</i>	—	—	—	\$5.4M	\$5.4M	\$10.8M
12. Increase Card Room Tax, Increase Number of Tables, and/or Levy Tax on Card Room Bank Groups** a. Increase Card Room tax from 13% to 18% b. Increase number of tables per card room by nine and increase the tax to 18% c. Levy 18% Tax Card Room Bank Groups <i>(Budget Balancing Guideline #9)</i>	—	—	—	\$2.0-8.4M	\$2.0-8.4M	\$4.0-16.8M
REVENUE STRATEGIES SUB-TOTAL	\$3.3M	\$6.3-12.0M	\$6.2-16.0M	\$4.0-8.0M	\$4.0-8.0M	\$23.8-47.3M

* Does not include one-time implementation costs

**Requires voter approval

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

General Fund Structural Deficit Elimination Plan						
Net Impact of Strategies on General Fund*						
SERVICE REDUCTIONS/ELIMINATIONS STRATEGIES						
Fiscal Year:	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	Total
13. Service Reductions/Eliminations Service reductions and eliminations will be accomplished on an annual basis through the budget process which considers the goals of the City Council, and involves an outreach process within the City organization and in the community. In addition, the City will utilize the Analytical Framework for Service Reductions/Eliminations, when finalized, as discussed in this Plan. <i>(Budget Balancing Guideline #1, 5)</i>	\$61.3M	\$22.9-29.6M	\$9.4M	—	—	\$93.6-100.3M
SERVICES REDUCTIONS/ELIMINATIONS STRATEGIES SUB-TOTAL	\$61.3M	\$22.9-29.6M	\$9.4M	\$0.0M	\$0.0M	\$93.6-100.3M
All Strategies TOTAL	\$67.1M	\$36.9-49.3M	\$23.2-33.0M	\$12.7-16.7M	\$14.1-18.1M	\$154.0-184.2M
General Fund Structural Deficit Incremental Projections	\$(67.1M)	\$(42.6M)	\$ (10.8M)	\$ 0.6M	\$4.2M	\$(115.7M)
General Fund Structural Deficit Cumulative Total	\$(67.1M)	\$(109.7M)	\$(120.5M)	\$(119.9M)	\$(115.7M)	\$(115.7M)

*Does not include one-time implementation costs

GENERAL FUND STRUCTURAL DEFICIT ELIMINATION PLAN UPDATE

CONCLUSION

The General Fund Structural Deficit Elimination Plan is a working and evolving blueprint to eliminate the structural budget deficit. Although no strategies have been dropped from consideration since November 2008, many new ideas have been considered and some discussed above. The Plan will continue to evolve as strategies are fully developed and others are eliminated for various reasons. In addition, the Plan is dependent on the current City revenue and expenditure projections. As the City presents projections on a biannual basis, the Elimination Plan will also be updated twice a year. Plan updates will be provided until the General Fund structural budget deficit is closed.

CAPITAL REVENUE FORECAST

MAJOR CAPITAL REVENUES

Overview

The major revenues that support the City of San José's capital programs are bond proceeds, grants, transfers between funds, and a number of taxes levied on construction and property resale (conveyance) activity. This document provides a five-year forecast for the following taxes and fees: Construction and Conveyance Tax; Building and Structure Construction Tax; Construction Excise Tax; Residential Construction Tax; Sanitary Sewer Connection Fee; and the Storm Drainage Connection Fee.

As shown below, these revenues are expected to generate \$193.9 million over the next five years, which is a decrease of 22% over the 2009-2013 Adopted Capital Improvement Program (CIP) estimates. The large decline is the result of the economic recession resulting in reduced construction-related development and the drop in real estate prices. The Construction-Related Revenue chart included at the end of this section provides a year-by-year comparison of this forecast with the 2009-2013 Adopted CIP.

Forecast Comparison Summary

(\$ in Thousands)

	2009-2013 CIP	2010-2014 Forecast	Difference	Change
Construction and Conveyance Tax	121,000	106,000	(15,000)	(12%)
Building and Structure Construction Tax	48,396	39,500	(8,896)	(18%)
Construction Excise Tax	70,026	43,000	(27,026)	(39%)
Residential Construction Tax	990	600	(390)	(39%)
Sanitary Sewer Connection Fee	5,599	3,750	(1,849)	(33%)
Storm Drainage Connection Fee	1,903	1,050	(853)	(45%)
TOTAL	247,914	193,900	(54,014)	(22%)

For the Construction and Conveyance Tax, the Conveyance Tax portion (property transfers) account for 98% of the total collections. The continued slowdown in the local and national real estate market continues to negatively impact collections. While overall transactions have risen, the severe drop in the median home price continues to drive down projected revenues in this category. Declines in Construction and Conveyance Tax revenues were predicted in the development of the 2009-2013 Forecast, however, recent information (December 2008 decline of 35% and January 2009 decline of 32%) indicates that collections have dropped even further than previously anticipated, and likely will not improve in the near-future. Collections through January 2009 included drops in 30 of the past 33 months when comparing to collections in the same month of the prior year. As a result, in this Forecast, this category is projected to generate \$106 million over the next five-years, a decrease of \$15 million from the estimates assumed in the 2009-2013 Adopted Capital Improvement Program (CIP). The average annual collection level of \$21.2 million projected in the 2010-2014 Forecast is dramatically down from the actual

CAPITAL REVENUE FORECAST

MAJOR CAPITAL REVENUES (CONT'D.)

Overview (Cont'd.)

collection levels in recent years that reached a peak of \$49 million in 2005-2006, but is expected to drop to \$19 million in 2008-2009.

The capital revenue projections for the other taxes and fees described in this forecast are derived from construction activity estimates provided by the Planning, Building and Code Enforcement (PBCE) Department. Each year the PBCE Department provides projections of activity for each of the three types of development (residential, commercial, and industrial) from which the revenues are derived. A more complete discussion of these estimates is provided in a technical report prepared by that department entitled "Development Activity Highlights and Five-Year Forecast (2010-2014)", which is attached as an appendix to this document.

Over the forecast period, PBCE projects construction activity valuation to drop considerably over the next couple years and recover slightly to \$750 million. These assumptions are significantly reduced from the levels presented in the 2009-2013 Forecast. Construction activity peaked in 2000-2001 at \$1.9 billion, followed by a sharp decline that reached a low point of \$818 million in 2003-2004 (adjusted to 2008 dollars). From that low point, a modest recovery occurred in 2004-2005 with 14% growth in that year. However, in 2005-2006, construction activity dipped again, to \$828 million, primarily due to a fall off of multi-family development to a ten-year low. A modest rebound driven primarily by commercial and industrial development and residential high rise construction in the downtown area occurred in 2006-2007. Due to a marked slowdown in residential construction which has continued to this day, 2007-2008 experienced a 9% decline and is expected to decline an additional 8% in 2008-2009 with total projected valuation of \$775 million. In this forecast, activity is expected to bottom out at \$650 million in 2009-2010 and recover to \$725 million in 2010-2011 before flattening out in 2011-2012 at \$750 million. Based on the construction activity estimates and a review of revenue collection patterns, a decrease in construction-related taxes and fees of \$54 million, or 22%, is expected when comparing the 2010-2014 Forecast to the 2009-2013 Adopted CIP estimates.

Each of the six revenue categories along with a discussion of the major construction activity trends are discussed in more detail below.

CONSTRUCTION AND CONVEYANCE TAX

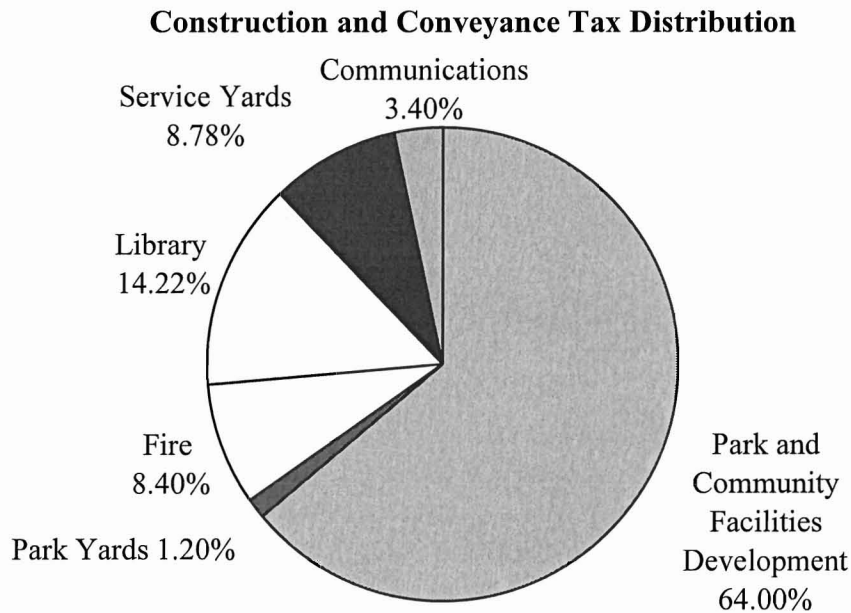
The Construction Tax portion of the Construction and Conveyance Tax category is levied on most types of construction. For residential construction, the tax rate is based upon the number of units constructed and ranges from \$75 per unit located in a building containing at least 20 dwelling units to \$150 for a single-family residence. The commercial and industrial rate is eight cents per square foot of floor area constructed. The Construction Tax accounts for approximately 2% of the total Construction and Conveyance Taxes collected.

CAPITAL REVENUE FORECAST

CONSTRUCTION AND CONVEYANCE TAX (CONT'D.)

The Conveyance Tax portion of the Construction and Conveyance Tax category is imposed upon each transfer of real property where the value of the property exceeds one hundred dollars. The tax is imposed at a rate of \$1.65 for each \$500 of the value of the property. The Conveyance Tax accounts for approximately 98% of the total Construction and Conveyance Taxes collected.

Construction and Conveyance Tax receipts are allocated using the following distribution to capital programs.



Under the current City ordinance, the combined proceeds from the Construction and Conveyance Tax may be used for facility acquisition, construction, equipment, furnishings, and limited operating and maintenance expenses.

Consistent with the Construction and Conveyance Tax Task Force recommendations adopted by the City Council in June 1989, the Park and Community Facilities Development portion of the estimated revenues, less non-construction costs and transfers to the General Fund, is allocated for all years of the forecast using a two-to-one ratio, with two-thirds of the proceeds going to neighborhood/district projects and one-third to city-wide projects. Per the current City Council policy, 20% of funds for neighborhood/district projects is set aside and equally allocated to meet special needs. The balance of the funds is then distributed based on a formula using the following criteria:

- neighborhood and community-serving park acres per 1,000 population;
- developed neighborhood and community-serving park acres per 1,000 population;
- square feet of neighborhood and community-serving center space per 1,000 population; and
- developed park acres and/or facilities in good condition per 1,000 population.

CAPITAL REVENUE FORECAST

CONSTRUCTION AND CONVEYANCE TAX (CONT'D.)

The five-year projection for Construction and Conveyance Tax revenue totals \$106 million, a decrease of \$15 million from the \$121 million estimated in the 2009-2013 CIP. The Construction and Conveyance Tax revenue projections are based upon: 1) a review of prior year collection trends; 2) a review of year-to-date residential sales activity in San José; 3) a review of year-to-date tax receipts; and 4) projections of the future strength of the San José real estate market.

- **Prior Year Collection Trends**

Historically, Construction and Conveyance Tax revenues have been very volatile, reflecting the impacts of the ups and downs of the local economy. In the late 1980's, collections of this tax were relatively strong, peaking at \$18 million in 1988-1989. In the first half of the 1990's, however, revenue fell precipitously with collections ranging from approximately \$9.3 million to \$11 million annually, reflecting the economic slowdown experienced at that time. In the latter half of the 1990's, healthy annual increases were again realized in this revenue category with growth skyrocketing from \$13.4 million in 1995-1996 to a peak of \$31.6 million in 2000-2001. This tremendous growth was indicative of the economic gains during that period, marked by stock market growth, low unemployment, and gains in personal income. As economic conditions began to worsen, tax receipts in this area again fell, experiencing a 17% decline in 2001-2002 to \$26.3 million and an additional 5.5% decline in 2002-2003 to \$24.8 million. Surprisingly, this drop-off did not continue, despite the general decline in economic conditions. Far exceeding our projections, collections grew to \$38.2 million in 2003-2004 and reached a record setting high of \$49 million in 2005-2006. Collections from that time however, have continually fallen as our forecasts have predicted, declining to \$41.8 million and \$26.8 million in 2006-2007 and 2007-2008 respectively following the recent real estate slowdown and sub-prime credit tightening.

- **2008-2009 Collections**

As projected in the 2009-2013 Forecast, the extreme distress in both the national and local real estate markets have seen collections of the Construction and Conveyance Tax plummet from the record peak levels three years ago. Collections received in January 2009 constituted the 30th out of the past 33 months where tax proceeds fell when comparing to collections in the same month of the prior year. Construction and Conveyance Tax collections in 2008-2009 of \$11.7 million through January 2009 decreased approximately 26% from the prior year. Data received in the most recent months (35% decline in December 2008 and 32% in January 2009) are particularly alarming as median home prices have dropped severely in recent months. The median single-family home price of \$415,000 in January 2009 represents a 38% decline compared to the \$664,000 figure in January 2008. It should be noted that this decrease has been partially offset by the increase in the number of property transfers for all types of residences in the city which rose by an astounding 56% through January 2009 when compared to the same period last fiscal year.

As a result of the extreme drop in the real estate market, a revision to 2008-2009 Construction and Conveyance Tax collections was approved in the 2008-2009 Mid-Year

CAPITAL REVENUE FORECAST

CONSTRUCTION AND CONVEYANCE TAX (CONT'D.)

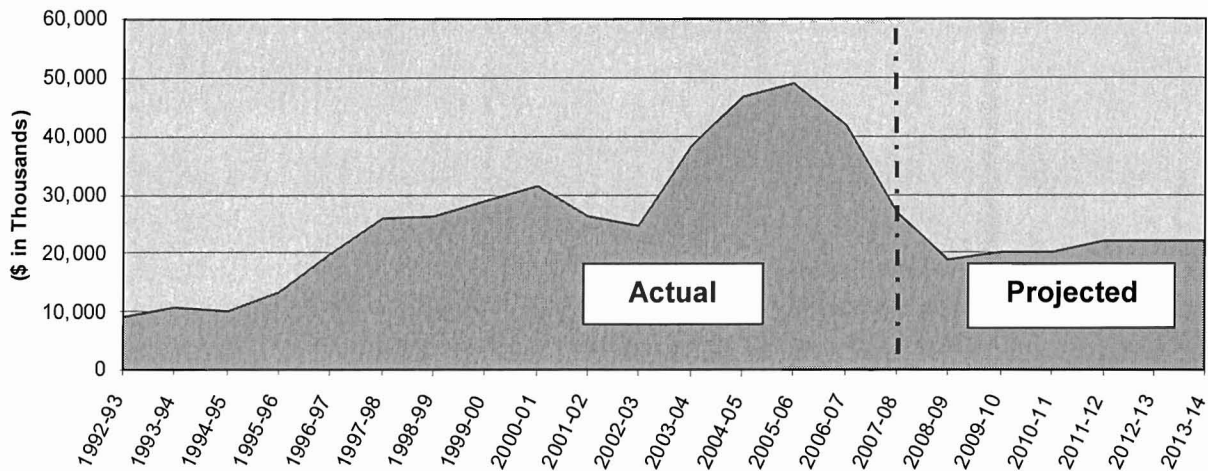
Budget Review, revising projected proceeds downward from \$23 million to \$19 million. The revised levels assume an approximate decline of 29% from the collection level of \$26.8 million received in 2007-2008.

- **2010-2014 Collections**

The 2010-2014 Construction and Conveyance Tax revenue forecast is built on the assumption that collections will bottom out in the current year, with collections increasing modestly and stabilizing at \$20 million in 2009-2010 and 2010-2011, and finally rising slightly to a collection level of \$22 million annually for the three remaining years of the forecast. This forecasted collection level reflects what is believed to be a more sustainable level of ongoing housing resale activity.

The following graph illustrates the volatility of this revenue source through a display of actual and projected revenues for the combined Construction and Conveyance Tax revenues over a 20 year period:

Construction and Conveyance Tax Revenues



CONSTRUCTION ACTIVITY PROJECTIONS

With the exception of the Construction and Conveyance Tax Fund, the capital revenues described in this forecast are construction-related taxes and fees. As described above, the PBCE Department has provided construction activity projections for each of the three types of development (residential, commercial, and industrial) from which the revenues are derived. These construction activity estimates are described in a report prepared by that department entitled “Development Activity Highlights and Five-Year Forecast (2010-2014)”, which is attached as an appendix to this document.

CAPITAL REVENUE FORECAST

CONSTRUCTION ACTIVITY PROJECTIONS (CONT'D.)

A summary of the PBCE Department construction activity projections and the corresponding revenue estimates are provided below. It should be noted that due to the highly volatile nature of the construction market, the reliability of the estimates can be expected to decline over the period of the forecast. The Department intends these to be interpreted as “ball park” estimates of the most likely state of the local economy based on current information. As new information becomes available, these estimates will be refined.

A. Residential Construction Activity

A significant portion of development-related revenue in San José has traditionally been generated by residential construction. Permit activity in 2007-2008 in this sector showed a sharp decline, with total construction valuation falling to its lowest level since 1982. When compared to the prior year, the number of building permits issued totaled 1,545 for new dwelling units. This represented a decrease of 52% from the 2006-2007 totals of 3,214 reflecting the national recession and the extreme distress in the real estate market. Significant declines in both multi-family and single-family construction activity were almost equal, with multi-family building permits declining by 51% from 2,669 units in 2006-2007 to 1,300 units in 2007-2008. A decline of 55% for single-family permits occurred with 545 units in 2006-2007 to 245 units in 2007-2008. In 2008-2009, the real estate slowdown is expected to continue to have a significant negative impact on the number of permits issued, with a decrease to an estimated 1,500 new units.

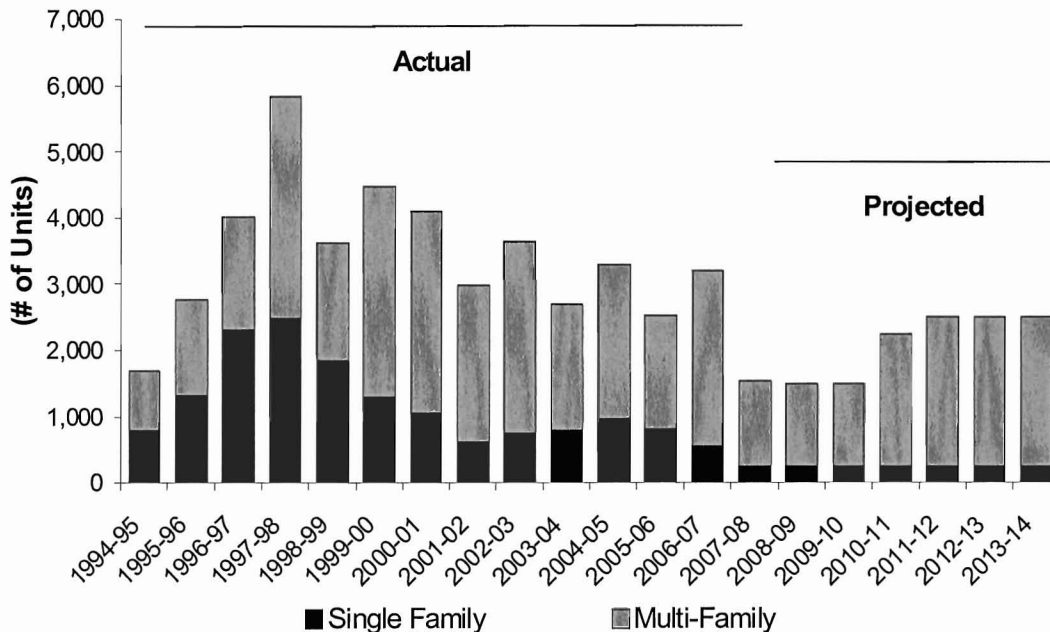
PBCE expects residential construction activity to generate a total of 11,250 units over the five-year period. This activity level represents a decline, driven by both multi-family and single-family markets, compared to the 14,500 units included in the 2009-2013 Forecast. This activity level represents a particularly significant decline from the actual levels experienced in peak years, which reached a high of 5,842 units in 1997-1998.

During the near term, residential activity is expected to remain weak as low builder and consumer confidence, falling home prices, rising unemployment, unsold inventory, and widespread foreclosures continue to outweigh demand. In this Forecast, a total of 10,000 multi-family units are expected reflecting the construction of higher density housing in the downtown area and North San José. Reflecting an expected decline in home prices, rising inventory, and credit tightening; only 1,000 new single-family dwellings are anticipated. This figure represents a 50% decrease from the 2,000 anticipated in the 2009-2013 Forecast and a significant decrease from the 1,500 anticipated in the 2008-2012 Forecast and 4,250 anticipated in the 2006-2010 and 2007-2011 Forecasts. The following chart shows the number of units, by housing type, anticipated in San José through 2013-2014.

CAPITAL REVENUE FORECAST

CONSTRUCTION ACTIVITY PROJECTIONS (CONT'D.)

Residential Construction Activity



B. Commercial Construction Activity

In 2007-2008, commercial construction activity totaled \$342 million, only a slight decrease from the 2006-2007 level of \$220 million (adjusted to 2008 dollars) but a huge drop (72%) from the peak reached in 2000-2001 of \$765 million. Planning staff expects commercial activity to experience a further decline in 2008-2009, with permit valuation estimated to reach \$250 million.

Over the forecast period, commercial construction is expected to decrease slightly to \$225 million in 2009-2010 and remain flat with anticipated valuations of \$225 million through the remainder of the five-year period represented in the forecast (see the chart on the following page). The total commercial valuation projected in this forecast is \$1.13 billion, which is significantly below the \$1.65 billion estimated in the previous five-year forecast. As discussed in the attached report provided by the PBCE Department, the outlook for commercial construction activity is expected to remain flat with declining sales revenues, rental rates, and occupancy rates weighing on demand for new space. The major expansion planned for Valley Fair Shopping Center is expected to continue at a slower pace. Some pending developments continue to remain in the pipeline. These include a proposed downtown grocery outlet, a new five story office building at Santana Row, and continuing construction of Vietnam Town Shopping Center on Story Road. It should be noted that recent information from the Office of Economic Development indicated that the San José commercial office vacancy rate was 14.3% and the commercial retail vacancies totaled 4.2%. The commercial retail vacancy figure, however, does not take into consideration large vacancies expected from larger stores such as the Mervyn's and Circuit City bankruptcies.

CAPITAL REVENUE FORECAST

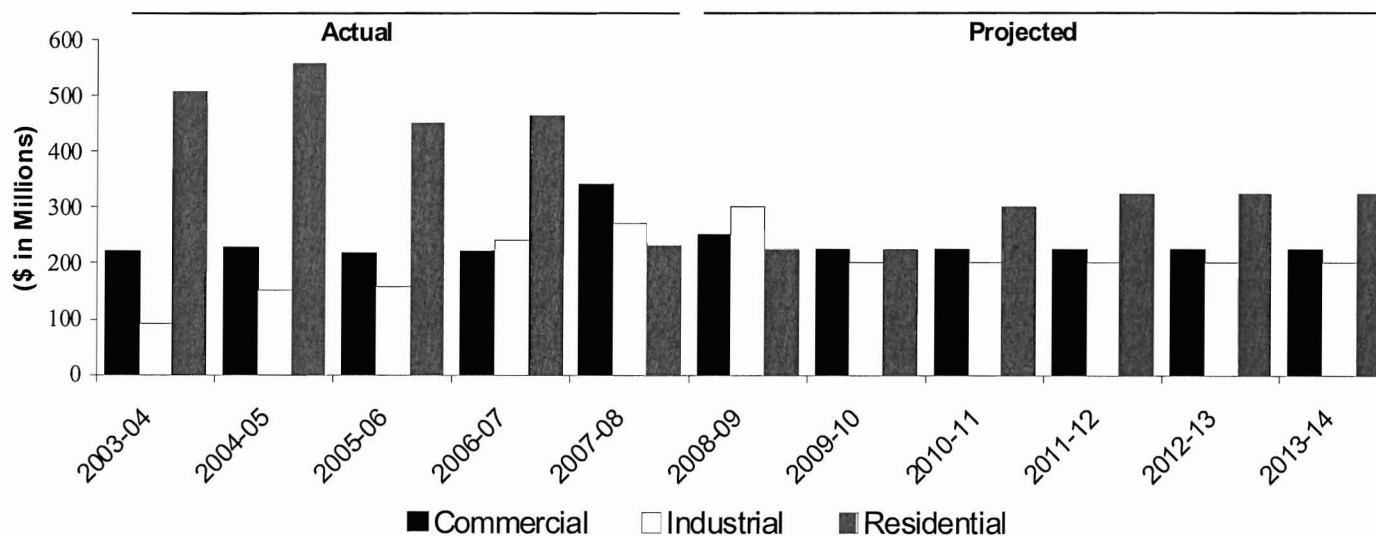
CONSTRUCTION ACTIVITY PROJECTIONS (CONT'D.)

C. Industrial Construction Activity

Industrial construction activity in San José has also experienced a dramatic decline since the peak in 2000-2001. In 2002-2003, permit valuation reached a low point of only \$82 million, a precipitous drop from the peak of \$531 million in 2000-2001. In 2004-2005, a slight recovery was experienced with permit valuation reaching \$152 million and continued to grow to \$242 million in 2006-2007 and \$272 million in 2007-2008. A slight increase is expected in 2008-2009, with permit valuation projected to reach \$300 million this year and then decreases to \$200 million throughout each of the five-years in the Forecast. The total industrial valuation over the forecast is estimated at \$1.0 billion, which is slightly below the \$1.1 billion estimated in the last forecast. As discussed in the attached report provided by the PBCE Department, activity in this area is expected to decrease over the forecast period from the moderate levels in the past two years. With the continued national recession, no new major groundbreakings are anticipated in the near term and permit valuation is expected to return to the low levels seen earlier in the decade. Recent information from the Office of Economic Development indicated that the San José vacancy rate for industrial space was 6.4%.

The following graph illustrates the level of projected construction activity by type (not including exemptions).

Projected Construction Valuation, by Type



CAPITAL REVENUE FORECAST

MAJOR DEVELOPMENT ACTIVITY DATA

As part of the attached Development Activity Highlights and Five-Year Forecast (2010-2014) document prepared by the PBCE Department, information is provided on development activity that serves as the foundation for their forecast. Data is provided on the major projects (residential projects greater than 50 units, commercial projects greater than 25,000 square feet, and industrial projects greater than 75,000 square feet) and is broken down by the three major land use categories – residential, commercial, and industrial. The projects are further subdivided into four categories based on their status (completed, under construction, approved but not yet commenced, and pending City approval). In addition, individual maps are provided for each of the 15 planning areas in the City that show the projects in all status categories submitted since January 1, 2005. These maps can be used in conjunction with the activity data to help analyze the rate, type and location of major development activity in San José.

BUILDING AND STRUCTURE CONSTRUCTION TAX

The Building and Structure Construction Tax is imposed upon the construction, repair or improvement of any building or structure where a building permit is required. Current rates are:

- 1) Residential - 1 ³/₄% of 88% of the Building Official's valuation.
- 2) Commercial - 1 ¹/₂% of the Building Official's valuation.
- 3) Industrial - 1% of the Building Official's valuation.

The proceeds from the Building and Structure Construction Tax are restricted by ordinance for use for traffic capital improvements on major arterials and collectors. These improvements can include the acquisition of land and interest in land and the construction, reconstruction, replacement, widening, modification and alteration (but not maintenance) of City streets. This tax revenue provides the Traffic Capital program with funds to complete major street infrastructure projects, particularly those that improve the Level of Service (LOS). LOS refers to the efficiency with which streets and roadways accommodate peak level traffic.

Based on the construction activity forecasts supplied by the PBCE Department and an analysis of actual collection patterns, the five-year projection for the Building and Structure Construction Tax collections totals \$39.5 million, with annual proceeds ranging from \$6.5 million to \$8.5 million. The five-year revenue projection represents a decrease of approximately \$8.9 million (18%) from the estimate included in the 2009-2013 Adopted CIP. While collections are expected to improve slightly over the forecast period, the lower projected activity levels reflect the national recession and real estate slowdown and are still well below the peak levels experienced a few years ago. For instance, the 2008-2009 revenue estimate of \$6.5 million for this tax is a drop of over 60% from the actual receipts in 2000-2001 of \$17.4 million.

A comparison of the five-year forecast with actual collections in previous years for the Building and Structure Construction Tax is shown in the chart in the following section.

CAPITAL REVENUE FORECAST

CONSTRUCTION EXCISE TAX

The Construction Excise Tax (also referred to as the Commercial-Residential-Mobile Home Park Building Tax) is imposed upon the construction, alteration, repair or improvement of any building or structure, which is for residential or commercial purposes or is associated with a mobile home. This general purpose tax may be used for any “usual current expenses” of the City. However, the City Council has historically used the majority of these funds for traffic improvements. The current rates are:

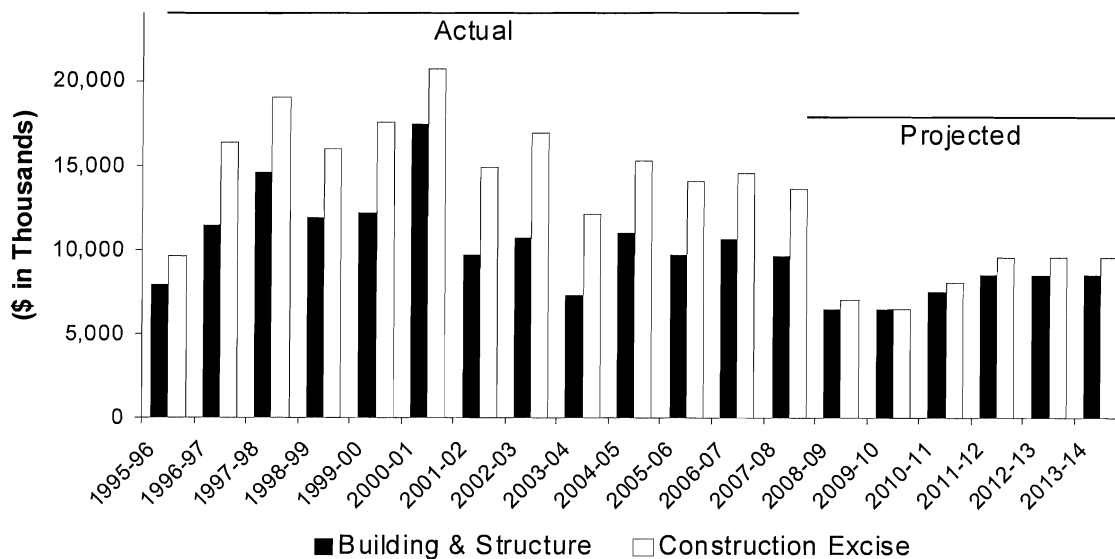
- 1) Residential - 2 3/4% of 88% of the Building Official’s valuation.
- 2) Commercial - 3% of the Building Official's valuation.

Unlike the Building and Structure Construction Tax, this tax does not apply to industrial development. As a result, changes in industrial building activity do not affect these tax receipts.

As mentioned above, this tax is a general fund tax that can be used for any purpose. The majority of the proceeds have generally been used for a variety of essential Traffic Capital projects that cannot be funded by the Building and Structure Construction Tax or grants. Typical projects funded with this tax include street maintenance and resurfacing, streetlights, bicycle and pedestrian facilities, and most strategic planning programs, which improve the City’s ability to obtain State and federal grants. A portion of these taxes have also been regularly used to help balance General Fund problems during times of financial stress on that fund.

Based upon the construction projections provided by the PBCE Department and actual collections on this tax, Construction Excise Tax collections are projected to total \$43.0 million over the five-year forecast period. This collection level represents a significant decrease of \$27.0 million (39%) from the 2009-2013 Adopted CIP. This decrease reflects the assumption that the recession and real estate slowdown will continue to impact development in the near-term, recovering slightly over the remainder of the forecast period.

Major Construction-Related Tax Revenues



CAPITAL REVENUE FORECAST

RESIDENTIAL CONSTRUCTION TAX

The Residential Construction Tax is imposed upon the construction of residential dwelling units and mobile home lots in the City. The rates are imposed on each dwelling unit and differ according to the number of units located in the building. Rates vary from \$90 for each dwelling unit in a multiple dwelling of at least 20 units to \$180 for a single-family residence.

This tax is collected and placed in the Residential Construction Tax Contribution Fund and is used to reimburse developers that have constructed a wider arterial street than their residential development required. The funds are also used to construct median island landscaping and other street improvements.

Based upon construction estimates by the PBCE Department and the actual collection pattern for this tax, \$600,000 in revenue is expected over the five-year period of this forecast. This amount is slightly below the 2009-2013 Adopted CIP revenue estimates of \$990,000.

SANITARY SEWER CONNECTION FEE

The Sanitary Sewer Connection Fee is charged for connecting to the City's sewer system. The fees collected may only be used for the construction and reconstruction, including land acquisition, of the San José sanitary sewer system. The fee is based on the number of single and multi-family residential units built and the acres developed on commercial and industrial properties.

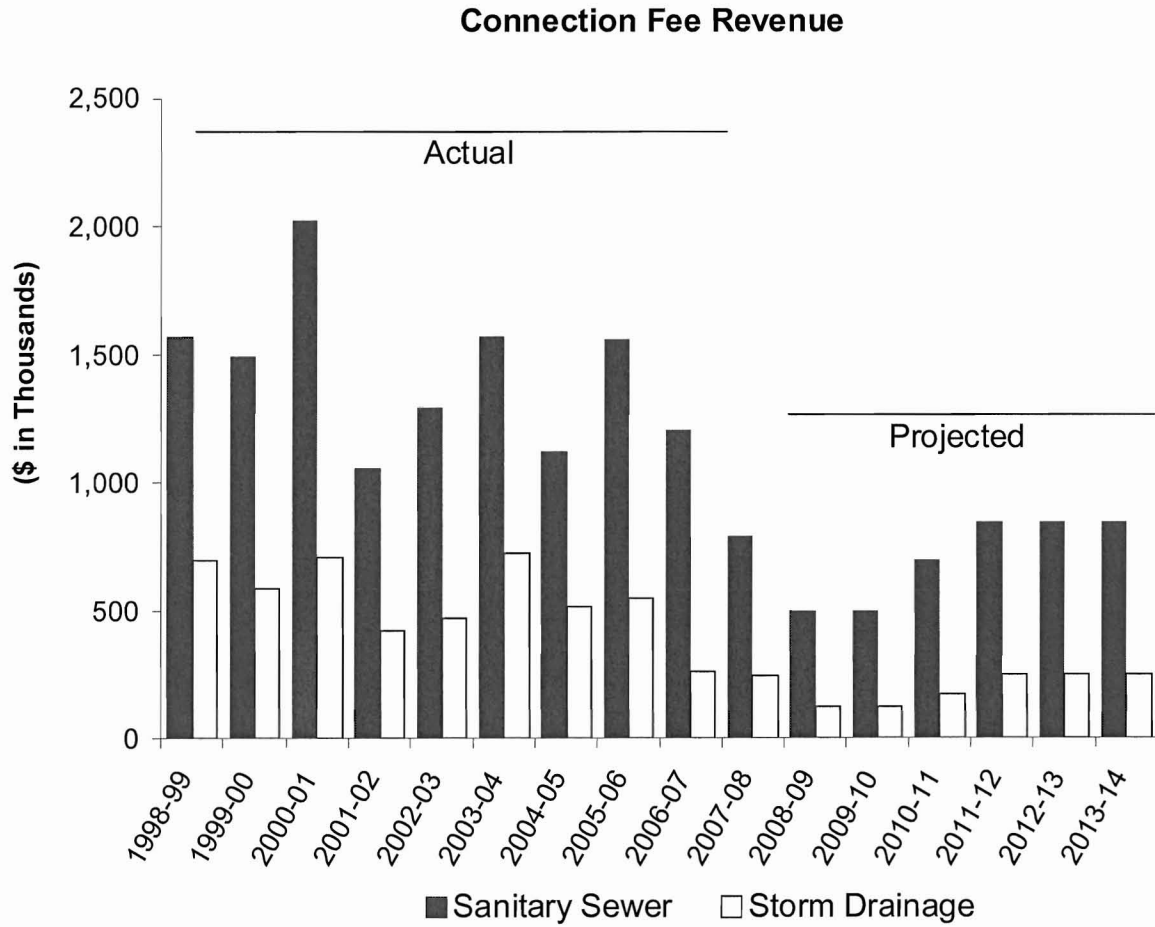
The 2010-2014 projection for this fee is \$3.8 million, which is a 33% overall decrease from the 2009-2013 CIP estimate of \$5.6 million. In addition to being affected by the lack of a significant rebound in development activity, this category is particularly impacted by a drop in the amount of projects involving undeveloped parcels for which these fees are assessed. Property that is being redeveloped typically is not subject to the fee.

STORM DRAINAGE CONNECTION FEE

The Storm Drainage Connection Fee is charged to the owner of any land that discharges storm water, surface water or ground water runoff into the City's storm drainage system. The fees are charged by acreage or lot and vary by land use and by the number of units located in the development. Storm Drainage Connection Fees may only be used for the construction, reconstruction, land acquisition and maintenance of the San José storm drainage system. The five-year forecast for Storm Drainage Connection Fees is \$1.1 million, which is a decrease from the estimate of \$1.9 million included in the 2009-2013 CIP. Over the five-year forecast period these fees are projected to rise from \$125,000 in the first year of the forecast period to \$250,000 in the fifth year.

CAPITAL REVENUE FORECAST

STORM DRAINAGE CONNECTION FEE (CONT'D.)



Construction-Related Revenue

2010 - 2014

(in \$ thousands)

	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	5 Yr Total
Construction and Conveyance Tax							
2009-2013 ADOPTED CIP	23,000	23,000	25,000	25,000	25,000	N/A	121,000
2010-2014 FORECAST	19,000	20,000	20,000	22,000	22,000	22,000	106,000
Difference	(4,000)	(3,000)	(5,000)	(3,000)	(3,000)	N/A	(15,000)
Building and Structure Construction Tax							
2009-2013 ADOPTED CIP	8,705	9,753	9,873	10,023	10,042	N/A	48,396
2010-2014 FORECAST	6,500	6,500	7,500	8,500	8,500	8,500	39,500
Difference	(2,205)	(3,253)	(2,373)	(1,523)	(1,542)	N/A	(8,896)
Construction Excise Tax							
2009-2013 ADOPTED CIP	12,975	13,974	14,223	14,415	14,439	N/A	70,026
2010-2014 FORECAST	7,000	6,500	8,000	9,500	9,500	9,500	43,000
Difference	(5,975)	(7,474)	(6,223)	(4,915)	(4,939)	N/A	(27,026)
Residential Construction Tax							
2009-2013 ADOPTED CIP	150	211	206	211	212	N/A	990
2010-2014 FORECAST	100	100	125	125	125	125	600
Difference	(50)	(111)	(81)	(86)	(87)	N/A	(390)
Sanitary Sewer Connection Fee							
2009-2013 ADOPTED CIP	907	972	1,167	1,257	1,296	N/A	5,599
2010-2014 FORECAST	500	500	700	850	850	850	3,750
Difference	(407)	(472)	(467)	(407)	(446)	N/A	(1,849)
Storm Drainage Connection Fee							
2009-2013 ADOPTED CIP	309	331	397	425	441	N/A	1,903
2010-2014 FORECAST	125	125	175	250	250	250	1,050
Difference	(184)	(206)	(222)	(175)	(191)	N/A	(853)
TOTAL							
2009-2013 ADOPTED CIP	46,046	48,241	50,866	51,331	51,430	N/A	247,914
2010-2014 FORECAST	33,225	33,725	36,500	41,225	41,225	41,225	193,900
Difference	(12,821)	(14,516)	(14,366)	(10,106)	(10,205)	N/A	(54,014)

Development Activity Highlights and Five-Year Forecast (2010-2014)



Prepared by:

**City of San Jose
Department of Planning, Building and Code Enforcement
February 2009**

Development Activity Highlights and Five-Year Forecast (2010-2014)

For more information, please contact:

**City of San Jose
Department of Planning, Building and Code Enforcement
Planning Division
200 East Santa Clara Street
San Jose, CA 95113
(408) 535-3555**

*This report and other information can be found
on the Planning Division web site at:*

<http://www.sanjoseca.gov/planning/data>

Development Activity Highlights and Five-Year Forecast (2010-2014)

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Development Activity Highlights and Five-Year Forecast (2010-2014)

I. PURPOSE

The *Development Activity Highlights and Five-Year Forecast (2010-2014)* is a report issued annually by the Department of Planning, Building and Code Enforcement. The report serves several functions. First, the report assists the Office of the City Manager in estimating future construction-related tax revenues that generate funds for the City's Capital Improvement Program. Second, the report provides City policymakers and staff with key data for periodic assessment of the rate, type, and location of development activity in San Jose. Lastly, the report is a tool for distributing information on major development projects to the general public.

II. SUMMARY

Development activity levels in San Jose are clearly being impacted by the severe recession currently gripping the global economy. Evidence of the downturn first appeared in residential construction, with a 50% decline in fiscal year 2007/08, which is now beginning to cascade into non-residential sectors. New commercial permit valuation is this year experiencing a similar rate of decline, while a comparable drop-off in industrial construction is expected next year. Fortunately, however, alterations activity—consisting of home remodeling and tenant improvements—remains remarkably steady, as in most cases “staying put” seems to present the most feasible and cost-effective strategy for owners and businesses to ride out this challenging economic storm. Regardless, the cascade effect of development hitting the across-the-board, proverbial “bottom” around 2010, provides an undeniably negative outlook, with permit valuation expected to decline to a 15-year low and remain at that or possibly lower levels throughout the five-year forecast period. The following summary discusses current development activity and trends for each major land use category (residential, commercial, and industrial), providing some insight as to what may occur over the forecast period (2010-2014).

Residential Development

- *New housing production in San Jose exceeded 4,000 dwelling units per year during the late-1990's, and then declined to an average of just over 3,000 units per year from 2001-2006. Since that time, however, activity has dropped off sharply, to approximately 2,000 units per year. In fact, total residential construction valuation in 2008 fell to its lowest level since 1982. For fiscal year 2007/08, building permits were issued for just 1,545 units, below the staff forecast (1,750 units).*

- *Staff forecasts that residential construction activity will remain very weak in the near term, as record low builder and consumer confidence, falling home prices and employment, unsold inventory, and widespread foreclosures outweigh demand stemming from improved affordability and low mortgage interest rates. As such, the number of new dwelling units is expected to reach just 1,500 units in fiscal year 2008/09—a modest decline from last year but also a 16-year low. On the other hand, home improvements (alterations) are holding up relatively well, showing little sign of deterioration and are expected to maintain current, moderate levels going forward.*
- *Following the present slowdown, staff anticipates that residential construction activity in San Jose will trend somewhat higher after 2010, albeit to levels well below long-term averages. Over the five-year forecast period, new construction is expected to sustain the moderate, post-2006 activity level of roughly 2,000 units per year. This outlook is based on a combination of factors, including the City’s commitment to construction of affordable housing, improving housing market fundamentals, and ultimate completion of numerous phased or otherwise temporarily stalled projects caught by the current economic slump. Future development will consist primarily of higher density housing in strategic infill locations, including the Greater Downtown area, North San Jose, and Specific Plan areas.*

Commercial Development

- *After a five-year-long boom in commercial construction activity that spanned the late-1990’s to early 2000’s, at which time total permit valuation averaged over \$500 million per year, activity from 2003-2007 consistently amounted to less than half that level. However, in fiscal year 2007/08, a resurgence primarily in office construction pushed activity to a six-year high of \$342 million, consistent with the staff forecast (\$350 million).*
- *Staff forecasts that commercial construction activity during fiscal year 2008/09 will return to the moderate levels of the 2003-2007 time period, with total permit valuation amounting to \$250 million. This activity will be driven by a combination of office and retail developments, which have in fact already pushed year-to-date valuation to roughly two-thirds of the forecast figure.*
- *For the five-year forecast period, commercial construction activity is expected to remain flat. Declining sales revenues, rental rates, and occupancy rates are dampening demand for new space. Even a major expansion of the highly successful Valley Fair Shopping Center, approved in late-2007, is now expected to proceed but at a slower pace. In any case, some bright spots remain, such as a proposed downtown grocery outlet (“The Market”) at one of San Jose’s several new high-rises, a new five-story office building at Santana Row, and*

recent resumption of construction (after a two-year delay) of the 300,000-square foot Vietnam Town Shopping Center on Story Road.

Industrial Development

- *Like its commercial counterpart, industrial construction activity nearly reached an astonishing \$500 million per year in permit valuation over the five-year period of 1997-2001. Since that time, however, activity has registered just a small fraction of that figure, reaching a low point under \$100 million per year in the two years immediately following the “dot com” bust. By comparison, the activity in fiscal year 2007/08, totaling \$272 million, was in a relatively moderate range, yet exceeded the staff forecast (\$225 million). At the same time, tenant improvements were quite robust, edging out last year’s respectable pace and setting a 7-year high.*
- *Staff forecasts that industrial construction activity will remain moderate during fiscal year 2008/09, with total permit valuation reaching \$300 million. In particular, new construction valuation in the first four months (July-October) already exceeded last year’s total, which surge was almost entirely attributed to several mid-rise office buildings underway for Brocade Communications Systems at the southeast corner of North 1st Street and Highway 237. On the other hand, tenant improvements are expected to weaken somewhat from their relatively high level over the past few years.*
- *Activity levels for industrial construction will be likely unable to sustain recent moderate levels over the forecast period. With no new major groundbreakings anticipated in the near term, permit valuation is expected to return to the low levels seen earlier in the decade. As such, tenant improvement activity, even though in decline, should manage to outpace new construction, a pattern common in recent years and typical of recessionary periods.*

III. FIVE-YEAR FORECAST (2010-2014)

The Department of Planning, Building and Code Enforcement’s five-year forecast of development activity is summarized in Tables 1 and 2 (next page). Construction valuation is expected to decline to a 15-year low of \$775 million during fiscal year 2008/09, and roughly remain at that or possibly lower levels throughout the forecast period.

Table 1
Construction Valuation: FY 03/04 to FY 13/14

Fiscal Year	03/04	04/05	05/06	06/07	07/08	08/09	09/10	10/11	11/12	12/13	13/14
	Actual Valuation¹ (in millions)					Projected Valuation (in millions)					
<u>New Construction</u>											
Residential	\$417	\$460	\$358	\$375	\$158	\$150	\$150	\$225	\$250	\$250	\$250
Commercial	\$82	\$86	\$105	\$85	\$185	\$100	\$100	\$100	\$100	\$100	\$100
Industrial	\$24	\$35	\$25	\$91	\$110	\$175	\$75	\$75	\$75	\$75	\$75
Subtotal	\$522	\$581	\$488	\$552	\$453	\$425	\$325	\$400	\$425	\$425	\$425
<u>Alterations</u>											
Residential	\$90	\$96	\$92	\$90	\$73	\$75	\$75	\$75	\$75	\$75	\$75
Commercial	\$140	\$143	\$114	\$135	\$157	\$150	\$125	\$125	\$125	\$125	\$125
Industrial	\$66	\$117	\$134	\$151	\$162	\$125	\$125	\$125	\$125	\$125	\$125
Subtotal	\$296	\$356	\$340	\$376	\$393	\$350	\$325	\$325	\$325	\$325	\$325
GRAND TOTAL	\$818	\$937	\$828	\$928	\$846	\$775	\$650	\$725	\$750	\$750	\$750
<u>Tax Exemptions</u>											
Residential	*	*	*	*	*	\$(25)	\$(25)	\$(25)	\$(25)	\$(25)	\$(25)
Commercial	*	*	*	*	*	\$(25)	\$(25)	\$(25)	\$(25)	\$(25)	\$(25)
Industrial	*	*	*	*	*	\$(25)	\$(25)	\$(25)	\$(25)	\$(25)	\$(25)
Net Total (Taxable)						\$700	\$575	\$650	\$675	\$675	\$675

*Note: Data on actual tax exemptions not available at the time of this report.

¹Valuation figures adjusted to 2008 dollars, per Bureau of Labor Statistics Consumer Price Index (CPI), San Jose-San Francisco-Oakland, all items index.

Table 2
Residential Units and Non-Residential Square Footage: FY 03/04 to FY 13/14

Fiscal Year	03/04	04/05	05/06	06/07	07/08	08/09	09/10	10/11	11/12	12/13	13/14
	Actual¹					Projected					
<u>Residential (Units)</u>											
Single-Family	782	962	814	545	245	250	250	250	250	250	250
Multi-Family	1,927	2,331	1,701	2,669	1,300	1,250	1,250	2,000	2,250	2,250	2,250
TOTAL	2,709	3,293	2,515	3,214	1,545	1,500	1,500	2,250	2,500	2,500	2,500
<u>Non-Residential (sq.ft., in thousands)</u>											
Commercial	500	750	750	1,000	1,250	750	750	750	750	750	750
Industrial	150	250	250	250	250	750	250	250	250	250	250
TOTAL	650	1,000	1,000	1,250	1,500	1,500	1,000	1,000	1,000	1,000	1,000

¹NOTE: Data on residential units based on the Building Division's *Permit Fee Activity Report*.

Data on non-residential square footage estimated based on construction valuation in the Building Division's *Permit Fee Activity Report*.

IV. CONSTRUCTION TAXES AND EXEMPTIONS

The City of San Jose imposes a series of construction-related taxes that are generally used to finance the construction and improvement of facilities and infrastructure systems that provide capacity beyond the needs attributed to a particular development. These taxes are in addition to cost-recovery fees charged for processing and reviewing applications for development approvals and permits. The largest construction-related tax revenue sources are described below.

Building and Structure Construction Tax

The Building and Structure Construction Tax is imposed upon the construction, repair, or improvement of any building or structure where a building permit is required (except for authorized exemptions- see below). The proceeds from this tax are restricted in use to the provision of traffic capital improvements on major arterials and collectors, the acquisition of lands and interest in land, and the construction, reconstruction, replacement, widening, modification and alteration (but not maintenance) of City streets.

Construction Excise Tax

The Construction Excise Tax is imposed upon construction, alteration, repair, or improvement of any residential or commercial structure (except for authorized exemptions- see below). The tax does not apply to industrial development. This is a general purpose tax that may be used for any “usual current expenses” of the City. The City Council has historically used the majority of these funds for traffic infrastructure improvements.

Residential Construction Tax

The Residential Construction Tax is imposed upon any construction of a one-family dwelling unit or multi-family units or any mobile home lot in the City. This tax is collected and placed in a fund used to reimburse private entities that have constructed a portion of an arterial street that is wider than what is normally required in connection with residential development. The funds are also used to construct median landscaping and other street improvements.

Exemptions

Certain construction-related tax exemptions are provided in San Jose. These exemptions apply only in certain areas and/or to certain types of land uses, and are generally designed to accomplish one of the following objectives:

1. Reduce the economic constraints involved in the development of housing in high risk areas and/or housing for very-low income households;

2. Implement a separately administered funding arrangement that finances infrastructure and public service needs in an area only with revenue generated by development in such area (e.g., Evergreen Specific Plan Area); and,
3. Provide exemptions required by State or Federal law (e.g., hospitals, churches).

Planning staff estimates that \$75 million in construction valuation will be exempted each year over the forecast period, or approximately 10% of total valuation during this time (see Table 1 on page 4).

V. MAJOR DEVELOPMENT ACTIVITY DATA

Planning staff has collected a significant amount of data on development activity, which is the foundation for the five-year forecast contained in Section III of this report. These data focus on recent “major” projects with the highest likelihood to have the most significant impact on the forecast. Major projects are defined as residential projects greater than 50 dwelling units, commercial projects greater than 25,000 square feet, and industrial projects greater than 75,000 square feet. This data collection effort has identified approximately 35,000 dwelling units and 15 million square feet of non-residential space submitted for Planning approval since January 1, 2005.

The development activity data on the following pages is first divided into three major land use categories-- residential, commercial, and industrial. Then, individual projects are divided into four subcategories based on project status-- projects completed, projects under construction, approved projects (construction not yet commenced), and projects pending City approval.

**Major Residential Development Activity
Projects of 50+ Dwelling Units, Submitted Since 1/1/05***

File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Housing Type	No. of Units	Proj. Mgr	Approval Date
<u>Projects Completed</u>									
PDA01-101-02	5/12/06	Santana Row (Parcel 7)	277-40-012	SE/c Winchester & Stevens Creek	West Valley	SF/MF	259	EM	6/23/06
PD05-011	2/4/05	Altura Townhomes	230-14-031	NE/c Newhall & Campbell	West Valley	SF	220	JR	6/9/05
PD05-005	1/25/05	Del Rosa at Miramonte	678-01-016	Nly side Metcalf, eby Hwy 101	Edenvale	SF	213	JR	12/8/05
HA04-038-01	7/18/05	The 88 Condos (Phase 1)	467-22-157	S/s E. San Fernando bet S. 2nd & S. 3rd	Central	MF	206	LX	9/7/05
PD05-013	2/8/05	Encanto Homes	230-14-007	N/s Campbell, 1000' wly Newhall	West Valley	SF	104	JR	9/6/05
PD05-084	11/14/05	Autumnvale Townhomes	244-31-011	SW/c N. Capitol & Autumnvale	Berryessa	SF	104	JR	3/1/06
PDA05-015-01	8/17/05	Montclair Townhomes	254-17-077	NW/c King & Mabury	Alum Rock	SF	91	SM	2/23/06
PD05-006	1/27/05	Autumn Terrace at Bonita	472-06-034	W/s Hwy 101, sly San Antonio	Central	SF	80	LX	6/15/05
HA03-002-01	2/8/06	The Globe Condos	467-22-134	Bet. S. 2nd & 3rd, 110' sly Santa Clara	Central	MF	76	LX	9/9/03
PD06-062	11/2/06	Siena at Montecito Vista	455-09-030	W/s Monterey, 300' sly Umbarger	South	SF	53	LM	7/3/06
PD05-074	10/20/05	Grandview Terrace Condos	592-06-020	NE/c N. Capitol & Grandview	Alum Rock	MF	45	SM	9/22/06
Total							1,451		
<u>Projects Under Construction</u>									
PD07-025	3/26/07	Race Street Housing (Phase 1)	264-09-043	E/s Race, nly UPRR tracks	Central	MF	385	RO	7/23/07
PD03-079	12/17/03	Monte Vista Condos	264-15-005	NE/c Auzerais & Sunol	Central	SF/MF	383	EM	2/15/06
PD04-074	9/29/04	The Villas/Courtyards Condos	244-20-025	SW/c Lundy & McKay	Berryessa	MF	304	MM	2/4/05
PD04-085	11/24/04	Fifty One Condos	261-33-038	SE/c The Alameda & Bush	Central	MF	265	EM	3/25/05
PDA07-026-01	2/6/08	Parkmoor Apts	264-09-051	NE/c Race & Parkmoor	Central	MF	243	MD	4/16/08
PD04-021	4/1/04	Skyline at Tamien Station	434-13-015	NE/c W. Alma & Hwy 87	Central	MF	240	CH	8/13/04
PD04-084	11/24/04	Paseo Senter Family Apts	477-20-050	E/s Senter, 600' sly Needles	South	MF	218	LM	3/18/05
HA05-037-01	9/27/06	Three Sixty Condos	264-29-053	NE/c Market & San Salvador	Central	MF	213	LX	11/22/06
PD05-041	6/7/05	Willow Glen Place	442-44-018	W/s Meridian, both sides Foxworthy	Willow Glen	MF	206	RB	9/19/05
PD05-082	11/2/05	Parkwood Homes	421-07-021	Bet. Hwy 85 & Samaritan, 1000' wly Union	Cambrian/Pioneer	SF/MF	202	SS	6/23/06
PDA03-006-01	5/23/07	Fairgrounds Senior Apts	497-38-020	S/s Tully, 750' wly Senter	South	MF	201	MD	11/30/07
PD05-032	5/2/05	Modern Ice Townhomes	249-68-001	NE/c Berryessa & Oakland	Central	SF	200	LX	7/27/05
PD05-075	10/20/05	Messina Gardens Condos ¹	254-06-037	SW/c N. Capitol & Mabury	Alum Rock	MF	199	SM	7/21/06
PD04-024	4/14/04	Venetian Terrace Condos	455-32-012	E/s Almaden Expwy, 500' sly Curtner	South	MF	170	EM	2/25/05
PD04-103	5/10/04	Fiesta Senior/Vista on San Carlos	274-14-142	NE/c W. San Carlos & Buena Vista	Central	SF/MF	127	EM	8/25/04
PD05-044	6/16/05	Hampton Park Townhomes	237-01-022	NW/c Oakland & Rock	Berryessa	SF	98	SM	12/22/05
PD06-070	12/15/06	Merrill Gardens Assisted Living	284-03-020	SW/c Meridian & Curci	Willow Glen	MF	95	RR	4/24/07
PD06-042	8/15/06	Village Square Condos	274-14-077	N/s W. San Carlos, 650' wly Meridian	Central	MF	95	SM	10/27/06
PD06-016	2/9/06	Fruitdale Apts	284-01-005	NE/c Southwest Expwy & Fruitdale	Willow Glen	MF	91	EM	9/1/06
PD05-078	10/24/05	Fairways at San Antonio Apts	481-46-010	E/s Hwy 101, wly term San Antonio	Alum Rock	MF	86	CH	6/29/06

**Major Residential Development Activity
Projects of 50+ Dwelling Units, Submitted Since 1/1/05***

File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Housing Type	No. of Units	Proj. Mgr	Approval Date
PD05-056	7/27/05	Crimson Townhomes	497-31-001	N/s Lewis, 1500' e ly Monterey	South	SF	80	LM	5/3/06
PD06-001	1/3/06	Monterey Family Apts	497-33-001	E/s Monterey, 600' sly Umbarger	South	MF	72	LM	4/12/06
PD06-047	9/11/06	Casa Feliz SRO	472-28-101	W/s S. 9th, 90' sly E. William	Central	MF	60	RE	11/14/06
PD07-042	5/1/07	Monta Vista Place Townhomes	359-35-008	NW/c S. De Anza & Hwy 85	West Valley	SF	57	MD	6/29/07
PD05-094	12/19/05	Almaden Walk Townhomes	455-31-023	E/s Almaden, opp Malone	South	SF	56	RR	6/7/06
PD05-089	11/28/05	Oakland Road Condos	237-01-011	W/s Oakland, 550' nly Rock	Berryessa	MF	53	SM	8/18/06

Total

4,399

Approved Projects (Construction Not Yet Commenced)

PD05-087	11/18/05	Hitachi Site Mixed Use	706-04-013	NE/c Cottle & Hwy 85	Edenvale	SF/MF	2,930	JR	6/2/06
PDC03-108	12/23/03	Flea Market Mixed Use	254-17-084	Both sides Berryessa, wly UP railroad	Berry./Alum Rock	SF/MF	2,818	RB	8/14/07
PDA07-006-03	12/12/08	Crescent Park Apts	097-33-113	SE/c Zanker & River Oaks	North	MF	1,750	MD	1/15/09
PD07-090	10/23/07	Riverview Mixed Use	097-06-038	W/s N. 1st, 450' sly Rio Robles	North	SF/MF	1,579	JB	4/4/08
PDC07-015	2/15/07	Newbury Park Mixed Use	254-04-076	NE/c N. King & Dobbin	Alum Rock	SF/MF	972	AB	12/18/07
PD06-062	11/2/06	Montecito Vista Mixed Use ²	455-09-030	W/s Monterey, 300' sly Umbarger	South	SF	783	LM	7/3/06
PD08-056	8/29/08	Seely Apts	097-15-026	SE/c River Oaks & Seeley	North	MF	777	ES	1/23/09
PD07-033	4/13/07	Northpointe Mixed Use	097-07-086	NW/c Zanker & Tasman	North	SF/MF	704	JB	11/30/07
PD07-091	10/11/07	Tasman Apts	097-52-013	B/s Vista Montana, bet Tasman & N. 1st	North	MF	554	ES	10/24/08
PDA06-048-01	11/8/07	Hyundai Site Mixed Use ³	097-06-055	N/s Montague, 550' wly N. 1st	North	MF	528	JB	12/14/07
PD07-043	5/7/07	Airport Parkway Condos	230-29-065	SE/c Airport & Hwy 101	North	MF	528	CB	4/21/08
PD07-082	9/20/07	Vista Montana Park	097-52-028	B/s Vista Montana, bet Tasman & N. 1st	North	MF	444	JB	3/21/08
PD08-001	1/7/08	Green Acres Mixed Use	254-15-072	SE/c Berryessa & Jackson	Alum Rock	SF	371	RM	10/10/08
PDC07-095	11/9/07	Santana Row	277-33-004	SE/c Winchester & Stevens Creek	West Valley	SF/MF	369	SM	5/13/08
H07-008	2/16/07	The Carlyle Condos	259-35-007	SW/c N. Almaden & W. St. John	Central	MF	347	MS	12/7/07
PDA08-036-01	11/4/08	River Oaks Housing	097-33-036	NE/c Zanker & River Oaks	North	MF	293	MD	12/19/08
PD08-053	8/19/08	Rosemary Housing	235-05-012	SE/c N. 1st & Rosemary	North	MF	290	RM	1/28/09
PD07-007	1/10/07	Fruitdale Station (Phase 2)	284-02-008	SE/c Southwest Expwy & Fruitdale	Willow Glen	SF	256	SM	3/21/08
PD07-088	10/9/07	Morrison Park Townhomes	261-01-054	SW/c Cinnabar & Stockton	Central	SF	250	LM	8/1/08
PD08-039	6/16/08	Campbell Avenue Housing	230-14-026	E/s Campbell, 2000' nwly Newhall	West Valley	SF/MF	248	ES	12/12/08
PD05-066	9/19/05	Santana Row (Parcel 8B)	277-46-001	SE/c Winchester & Stevens Creek	West Valley	SF/MF	238	EM	1/31/07
PD08-029	4/16/08	Virginia Terrace Condos	472-18-051	SW/c E. Virginia & S. 6th	Central	MF	238	RM	10/24/08
PD08-023	3/11/08	Baypointe Mixed Use	097-07-072	NE/c Baypointe & Tasman	North	SF	229	JB	8/1/08
PDC07-096	11/13/07	San Carlos Mixed Use	277-20-006	SW/c W. San Carlos & Meridian	Central	SF	218	ES	9/23/08
H05-029	6/21/05	Park View Towers	467-01-118	N/s St. James, bet N. 1st & N. 2nd	Central	MF	194	LB	5/23/08
PD07-099	11/19/07	Belovida Senior Apts	254-04-076	NE/c N. King & Dobbin	Alum Rock	MF	185	AB	8/29/08
PD07-036	4/13/07	Baypointe Housing	097-07-031	W/s Baypointe, 370' nly Tasman	North	SF	183	JB	11/30/07

**Major Residential Development Activity
Projects of 50+ Dwelling Units, Submitted Since 1/1/05***

File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Housing Type	No. of Units	Proj. Mgr	Approval Date
PD07-094	10/23/07	South 2nd Mixed Use	477-01-082	SE/c S. 2nd & Keyes	Central	MF	134	ES	11/14/08
PD07-067	7/23/07	Kings Crossing Apts/Shelter	254-04-076	NE/c N. King & Dobbin	Alum Rock	MF	130	AB	10/22/08
PDA05-057-01	12/19/07	Park Avenue Lofts	261-36-062	N/s Park, 450' ely Sunol	Central	SF	125	MD	4/21/08
PD06-011	4/11/06	Fourth Street Apts	235-04-005	E/s N. 4th, 600' nly Gish	North	MF	100	CB	6/29/07
PD04-071	11/17/04	Blackwell Condos	481-18-013	W/s McCreery, 230' sly Alum Rock	Alum Rock	MF	93	MD	9/9/08
PD05-045	6/22/05	Oakwood Apts (annex)	299-37-031	SE/c Saratoga & Blackford	West Valley	MF	84	RR	9/28/05
CP07-101	12/6/07	Bascom Senior Assisted Living	412-24-009	SW/c Bascom & Surrey	Willow Glen	MF	69	MD	6/11/08
PD07-013	2/9/07	22nd & William Housing	472-01-021	S/s William, 350' wly S. 24th	Central	SF	67	MS	6/29/07
PD07-097	11/13/07	Cornerstone at Japantown Condos	249-08-002	SW/c N. 10th & E. Hedding	Central	MF	53	LM	6/13/08

Total

19,131

Projects Pending City Approval

PDC08-049	8/29/08	Communications Hill Mixed Use	455-19-101	N/s Hillsdale bet Monterey & Hwy 87	South	SF/MF	2,389	MD	---
PDC07-098	11/21/07	iStar Site Housing	706-08-008	NW/c Monterey & Hwy 85	Edenvale	SF/MF	1,500	AT	---
PDC08-061	11/3/08	Ohlone Mixed Use	264-14-131	SW/c W. San Carlos & Sunol	Central	MF	825	LM	---
PDC07-010	1/25/07	Markovits & Fox Mixed Use	237-03-070	SW/c E. Brokaw & Oakland	Berryessa	SF	750	JB	---
PDC07-073	9/12/07	Corp Yard Mixed Use	249-39-039	NE/c Jackson & N. 6th	Central	SF	600	LM	---
PDC07-060	8/8/07	River Oaks Condos	097-33-102	N/s River Oaks, 200' ely Research	North	MF	490	JB	---
PD08-046	7/16/08	Century Center Mixed Use	230-29-022	SW/c N. 1st & Century Center	North	MF	460	CB	---
PDC05-101	10/14/05	Vendome Place	259-05-024	NW/c N. 1st & Taylor	Central	MF	433	ES	---
H06-040	8/29/06	City Front Square Condos	259-42-080	NE/c S. Market & E. San Carlos	Central	MF	414	RE	---
PDC08-036	6/20/08	Libitzky Mixed Use	249-09-001	NW/c N. 10th & E. Taylor	Central	MF	384	ES	---
H06-082	10/23/06	Market Street Mixed Use	259-40-093	SW/c Market & Santa Clara	Central	MF	309	LM	---
PDC06-116	10/25/06	Renaissance Housing	097-52-027	SW/c Renaissance & Vista Montana	North	SF	263	JB	---
H08-001	1/2/08	San Pedro Condos (Tower 1)	259-32-044	SW/c N. San Pedro & Bassett	Central	MF	240	ES	---
HA04-038-04	11/21/07	The 88 Condos (Phase 2)	467-22-156	S/s E. San Fernando bet S. 2nd & S. 3rd	Central	MF	204	ES	---
PDC06-069	6/29/06	North Tenth Street Housing	249-08-004	W/s N. 10th, bet Vestal & E. Mission	Central	SF	166	LM	---
PDC06-125	11/14/06	Delmas Place Condos	264-26-006	W/s Delmas, 300' sly W. San Carlos	Central	MF	164	ES	---
PDA04-076-01	3/14/08	Ajisai Gardens Condos	249-37-006	SE/c E. Taylor & N. 7th	Central	MF	126	ES	---
PDC08-034	6/18/08	Sunol Court SRO	261-39-009	N/s W. San Carlos, bet Sunol & McEvoy	Central	MF	123	MD	---
PD08-071	12/17/08	Santana Row (Parcel 6B)	277-40-011	NW/c Olin & Hatton	West Valley	SF/MF	118	ES	---
PDC06-117	10/31/06	Riverpark Condos	259-43-072	NE/c W. San Carlos & Hwy 87	Central	MF	99	LM	---
PDC08-067	12/23/08	Summerwind Apts (annex)	477-19-060	NW/c McLaughlin & Summerside	South	MF	91	MD	---
PDC08-010	2/11/08	Japantown Senior Apts	249-39-011	W/s N. 6th, 200' sly E. Taylor	Central	MF	85	ES	---
PD09-001	1/20/09	San Antonio Apts	472-05-032	S/s E. San Antonio, opp. S. 28th	Central	MF	84	LB	---
PDC06-121	11/3/06	Las Brisas Condos	481-19-003	S/s Alum Rock, 350' ely McCreery	Alum Rock	MF	79	AT	---

**Major Residential Development Activity
Projects of 50+ Dwelling Units, Submitted Since 1/1/05***

File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Housing Type	No. of Units	Proj. Mgr	Approval Date
PD07-089	10/10/07	Leigh Senior Housing	284-32-014	SE/c Southwest Expwy & Leigh	Willow Glen	MF	64	MD	---
PDC08-066	11/25/08	Westmount Square	249-09-009	SE/c E. Mission & N. 10th	Central	SF	62	ES	---
PDC07-017	5/19/08	Lincoln Avenue Condos	261-41-096	SW/c Lincoln & Pacific	Central	SF	53	BR	---
PDC08-035	6/23/08	Edwards Mixed Use	264-37-060	SW/c Edwards & S. 1st	Central	MF	50	LM	---
Total							10,625		
GRAND TOTAL							35,606		

Footnotes: (1) Includes PD06-029 (110 units)
(2) Includes PDA06-062-01 (743 units)
(3) Includes PD06-051 (104 units), PD06-052 (50 units), and PD06-068 (127 units).

File Number Prefixes: PDC= Planned Development Rezoning; PD= Planned Development Permit; H= Site Development Permit; CP= Conditional Use Permit

**Major Commercial Development Activity
Projects of 25,000+ Square Feet, Submitted Since 1/1/05**

File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Square Footage (approx.)	# of New Guest Rooms	Proj. Mgr	Approval Date
Projects Completed									
CP05-034	6/9/05	The Home Depot	484-33-057	NE/c Story & McGinness	Alum Rock	149,000		HL	3/22/06
CP05-046	7/29/05	Costco Wholesale	244-14-014	NW/c Hostetter & Automation	Berryessa	147,000		JR	5/24/06
CP06-062	11/9/06	Beshoff Infinity	491-04-046	SW/c Capitol & Tully	Evergreen	35,000		RM	2/12/07
PD05-065	9/9/05	Senter/Quinn Retail	477-73-039	E/s Senter, 200' nly Quinn	South	34,000		LM	6/9/06
PD05-024	3/21/05	Gold Street Office	015-34-063	SW/c Gold & Guadalupe River	Alviso	24,000		SM	7/6/05
PD06-060	11/1/06	Silver Creek Valley Retail	678-93-016	S/s Silver Creek Valley, 750' sly Hellyer	Edenvale	24,000		JR	4/27/07
Total						413,000	-		

Projects Under Construction

PD07-060	6/20/07	America Center	015-45-026	NW/c Hwy 237 & Gold	Alviso	981,000	176	CB	11/8/07
PD05-058	8/4/05	The Plant Shopping Center	455-05-011	NW/c Curtner & Monterey	South	646,000		RM	6/7/06
PD05-016	2/14/05	Vietnam Town Shopping Center	472-11-065	N/s Story, 700' swly McLaughlin	Central	300,000		LM	9/5/06
PD84-123	11/13/84	Riverpark Towers II	259-43-074	SE/c Park & Hwy 87	Central	293,000		JW	2/6/85
H07-025	7/2/07	Lowe's Home Improvement	237-05-053	SE/c Hwy 880 & Brokaw	Berryessa	195,000		JB	2/29/08
CPA02-048-01	11/16/06	Harker School (Upper Campus)	303-25-001	NE/c Saratoga & Hwy 280	West Valley	169,000		AB	4/11/07
CP07-072	9/18/07	Whole Foods Market	567-50-012	SW/c Blossom Hill & Almaden	Cambrian/Pioneer	81,000		ES	4/8/08
PD07-100	11/19/07	Santana Row (Office)	277-33-004	SE/c Winchester & Stevens Creek	West Valley	76,000		SM	4/11/08
H06-035	7/18/06	Lenfest Self Storage	254-02-037	SW/c Mabury & Lenfest	Alum Rock	60,000		LX	5/10/07
PD07-105	12/20/07	Bellarmino (Humanities Building)	261-11-005	NE/c Elm & Emory	Central	53,000		ES	7/11/08
HA04-038-01	7/18/05	The Market	467-22-157	S/s E. San Fernando bet S. 2nd & S. 3rd	Central	41,000		LX	9/7/05
CP06-011	2/7/06	Tully/Monterey Retail	477-22-017	NE/c Old Tully & Monterey	South	40,000		LM	9/13/06
H07-045	11/6/07	Umbarger Square	497-38-002	NE/c Monterey & Umbarger	South	29,000		ES	7/3/08
Total						2,964,000	176		

Approved Projects (Construction Not Yet Commenced)

H06-027	5/10/06	Valley Fair Shopping Center	274-43-035	NW/c Hwy 17 & Stevens Creek	West Valley	525,000		AB	11/19/07
PD05-087	11/18/05	Hitachi Site Mixed Use	706-04-013	NE/c Cottle & Hwy 85	Edenvale	460,000		JR	6/2/06
PD07-049	5/21/07	Lowe's Home Improvement	230-46-064	NW/c Coleman & Newhall	North	251,000		ME	5/2/08
PDC03-108	12/23/03	Flea Market Mixed Use	254-17-084	Both sides Berryessa, wly UP railroad	Berry./Alum Rock	245,000		RB	8/14/07
PD07-063	7/10/07	Lowe's Home Improvement	706-06-015	SE/c Monterey & Cottle	Edenvale	201,000		SS	9/19/08

**Major Commercial Development Activity
Projects of 25,000+ Square Feet, Submitted Since 1/1/05**

File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Square Footage (approx.)	# of New Guest Rooms	Proj. Mgr	Approval Date
PDC07-095	11/9/07	Santana Row	277-33-004	SE/c Winchester & Stevens Creek	West Valley	198,000		SM	5/13/08
PD05-095	12/22/05	Calif. Center for Health Care	678-07-029	SE/c Silver Creek Valley & Hwy 101	Edenvale	178,000		SS	9/21/07
PD07-001	1/3/07	Smythe European	296-38-012	SW/c Stevens Creek & Palace	West Valley	170,000		RR	6/15/07
H07-030	8/2/07	Extra Space Storage	455-07-012	NW/c Curtner & Stone	South	135,000		CB	6/6/08
CP08-071	8/29/08	Hotel Sierra	097-03-138	SE/c N. 1st & Hwy 237	North	116,000	160	CB	12/10/08
PDC06-059	5/31/06	Aborn Storage Center	670-13-002	NW/c Aborn & King	Evergreen	104,000		RM	1/9/07
CP08-057	6/26/08	Oakland/Brokaw Commercial	237-03-074	NW/c Oakland & Brokaw	Berryessa	100,000		ES	10/22/08
PDC07-072	9/7/07	Bellarmino College Preparatory	261-11-005	NE/c Elm & Emory	Central	83,000		ES	6/17/08
PDC06-019	3/16/06	Public Storage	462-19-013	N/s Capitol, 200' w Snell	South	83,000		LX	10/3/06
H07-053	5/25/07	Retail @ First	097-03-138	NE/c N. First & Headquarters	North	73,000		CB	4/4/08
PD07-071	8/21/07	Senter Office/Retail	477-73-043	E/s Senter, 1200' nly Tully	South	60,000		MD	11/30/07
PD08-018	2/20/08	Orchard Supply Hardware	447-05-018	E/s Yucca, bet Foxworthy & Hillsdale	Willow Glen	51,000		ES	8/15/08
PD07-090	10/23/07	Riverview Mixed Use	097-06-038	W/s N. 1st, 450' sly Rio Robles	North	45,000		JB	4/4/08
PD07-039	4/25/07	Whole Foods Market	261-01-098	NW/c The Alameda & Stockton	Central	44,000		HL	9/28/07
H05-006	2/7/05	Westgate West Shopping Center	381-36-012	NE/c Prospect & Lawrence	West Valley	42,000		RM	9/27/06
PD06-036	7/24/06	Evergreen Village Square	659-56-002	SW/c Ruby & Classico	Evergreen	37,000		RM	1/12/07
PD08-001	1/7/08	Green Acres Mixed Use	254-15-072	SE/c Berryessa & Jackson	Alum Rock	30,000		RM	10/10/08
PD08-040	7/1/08	Coleman Retail	230-46-068	NW/c Coleman & Newhall	North	25,000		ES	10/24/08
PD07-033	4/13/07	Northpointe Mixed Use	097-07-086	NW/c Zanker & Tasman	North	25,000		JB	11/30/07
PD07-007	1/10/07	Fruitdale Station (Phase 2)	284-02-008	SE/c Southwest Expwy & Fruitdale	Willow Glen	25,000		SM	3/21/08
PDC07-015	2/15/07	Newbury Park Mixed Use	254-04-076	NE/c N. King & Dobbin	Alum Rock	25,000		AB	12/18/07
Total						3,331,000	160		

Projects Pending City Approval

PDC08-037	6/23/08	Marriott Residence Inn	230-29-109	SW/c N. 1st & Skyport	North	216,000	321	JD	---
CP07-070	9/7/07	Target Stores	097-03-140	SE/c N. 1st & Hwy 237	North	165,000		SD	---
PDC06-089	8/9/06	Public Storage	670-41-007	SW/c E. Capitol & Quimby	Evergreen	128,000		RM	---
PD08-027	4/4/08	Flea Market Mixed Use (North)	254-17-084	Both sides Berryessa, wly UP railroad	Berry./Alum Rock	121,000		JB	---
PD08-054	8/12/08	Samaritan Medical Center	421-37-012	NE/c Samaritan & S. Bascom	Cambrian/Pioneer	75,000		ES	---
PDC08-049	8/29/08	Communications Hill Mixed Use	455-19-101	N/s Hillsdale bet Monterey & Hwy 87	South	65,000		MD	---
PD07-085	10/1/07	Silicon Valley Club	015-34-059	W/s Gold term El Dorado	Alviso	60,000		JD	---
PDC07-010	1/25/07	Markovits & Fox Mixed Use	237-03-070	SW/c E. Brokaw & Oakland	Berryessa	56,000		RB	---
PDC08-061	11/3/08	Ohlone Mixed Use	264-14-131	SW/c W. San Carlos & Sunol	Central	50,000		LM	---
H08-014	3/26/08	Stevens Creek Chrysler/Dodge	294-41-003	S/s Stevens Creek, 260' e ly Kiely	West Valley	50,000		ES	---
PDC08-056	9/30/08	Valley Christian Schools	684-05-019	Ely term. Skyway	Edenvale	45,000		SS	---

**Major Commercial Development Activity
Projects of 25,000+ Square Feet, Submitted Since 1/1/05**

File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Square Footage (approx.)	# of New Guest Rooms	Proj. Mgr	Approval Date
H06-040	8/29/06	City Front Square Condos	259-42-080	NE/c S. Market & E. San Carlos	Central	33,000		RE	---
PDC08-031	6/6/08	Morrill/Landess Commercial	092-20-008	SE/c Morrill & Landess	Berryessa	31,000		BR	---
PDC07-073	9/12/07	Corp Yard Mixed Use	249-39-039	NE/c Jackson & N. 6th	Central	30,000		LM	---
HA04-038-04	11/21/07	The 88 Condos (Phase 2)	467-22-156	S/s E. San Fernando bet S. 2nd & S. 3rd	Central	27,000		ES	---
H08-025	5/28/08	Stevens Creek Gateway	274-57-022	NE/c Stevens Creek & DiSalvo	Central	26,000		ES	---
H08-044	12/5/08	Askari Self Storage	241-12-012	E/s Oakland, 350' sly Service	Berryessa	25,000		SD	---
PDC08-015	3/7/08	Almaden Mixed Use	451-06-068	NW/c Almaden & Hillsdale	Willow Glen	25,000		MD	---
Total						1,228,000	321		
GRAND TOTAL						7,936,000	657		

Footnotes:

File Number Prefixes: H= Site Development Permit; CP= Conditional Use Permit; PDC= Planned Development Rezoning; PD= Planned Development Permit

**Major Industrial Development Activity
Projects of 75,000+ Square Feet, Submitted Since 1/1/05**

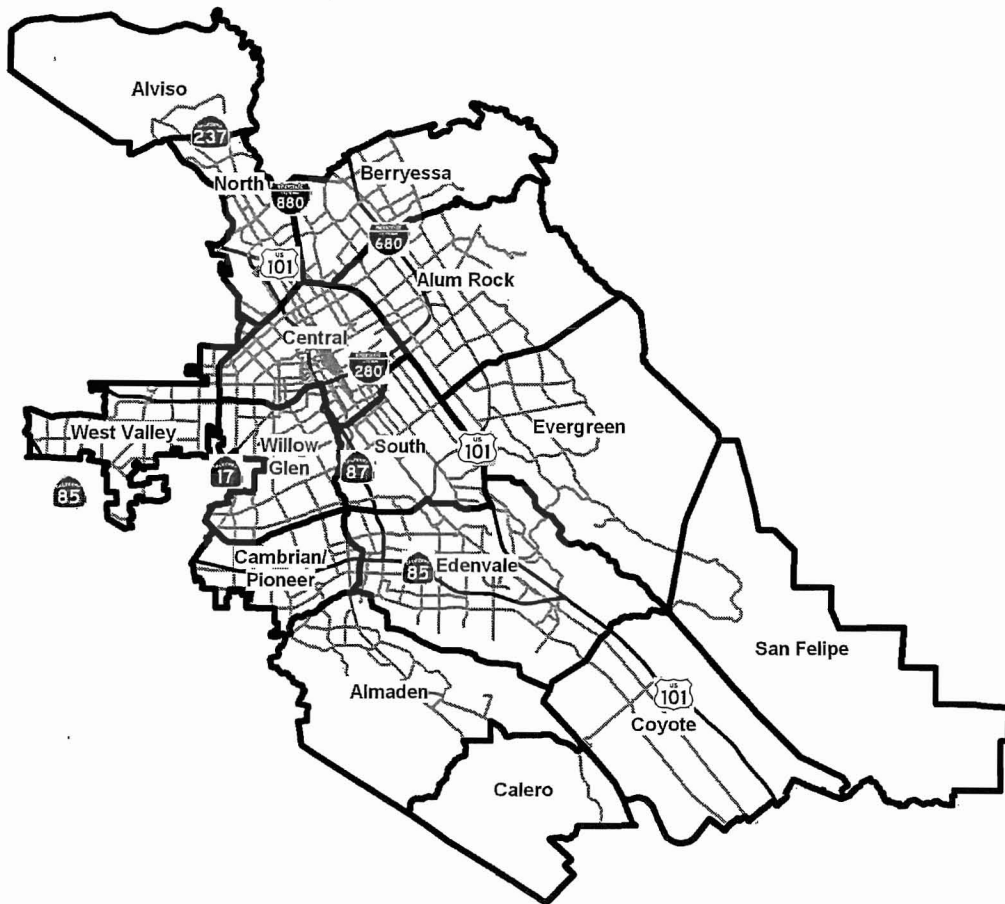
File Number	Filing Date	Project Name	Tracking APN	Street Location	Planning Area	Square Footage (approx.)	Proj. Mgr	Approval Date
<u>Projects Completed</u>								
SPA04-064-01	4/27/05	Hellyer Commons	678-08-038	SE/c Piercy & Hellyer	Edenvale	98,000	JR	7/1/05
Total						98,000		
<u>Projects Under Construction</u>								
H07-018	5/3/07	Brocade Communications	097-03-139	SE/c N. 1st & Hwy 237	North	889,000	CB	10/19/07
H05-053	10/28/05	Cadence Design Systems	097-66-005	N/s Montague at Trimble	North	208,000	JR	10/13/06
HA02-040-01	3/19/07	ACM Aviation Hangar/Office	230-46-042	SE/c Coleman & Aviation	North	78,000	CB	6/22/07
Total						1,175,000		
<u>Approved Projects (Construction Not Yet Commenced)</u>								
H03-039	7/3/03	eBay	101-04-005	SW/c N. 1st & Charcot	North	1,279,000	MM	12/12/03
PD08-030	4/22/08	Skyport Plaza (Phase 2)	230-29-056	W/s N. 1st bet Skyport & Sonora	North	558,000	JB	8/8/08
H08-002	1/8/08	Boston Properties (Zanker)	097-33-104	NE/c Zanker & Montague	North	533,000	CB	12/17/08
PD07-081	9/18/07	Legacy on 101 Office	101-02-015	W/s Orchard, 750' nly Charcot	North	398,000	JB	12/21/07
Total						2,768,000		
<u>Projects Pending City Approval</u>								
PD08-064	11/3/08	Campus @ North First	101-02-011	SW/c N. 1st & Component	North	2,800,000	JD	---
SP08-046	8/14/08	Equinix	706-09-102	NW/c Great Oaks & Hwy 85	Edenvale	160,000	SD	---
Total						2,960,000		
GRAND TOTAL						7,001,000		

File Number Prefixes: H= Site Development Permit; CP= Conditional Use Permit; PDC= Planned Development Rezoning; PD= Planned Development Permit

VI. MAJOR DEVELOPMENT ACTIVITY MAPS (PLANNING AREAS)

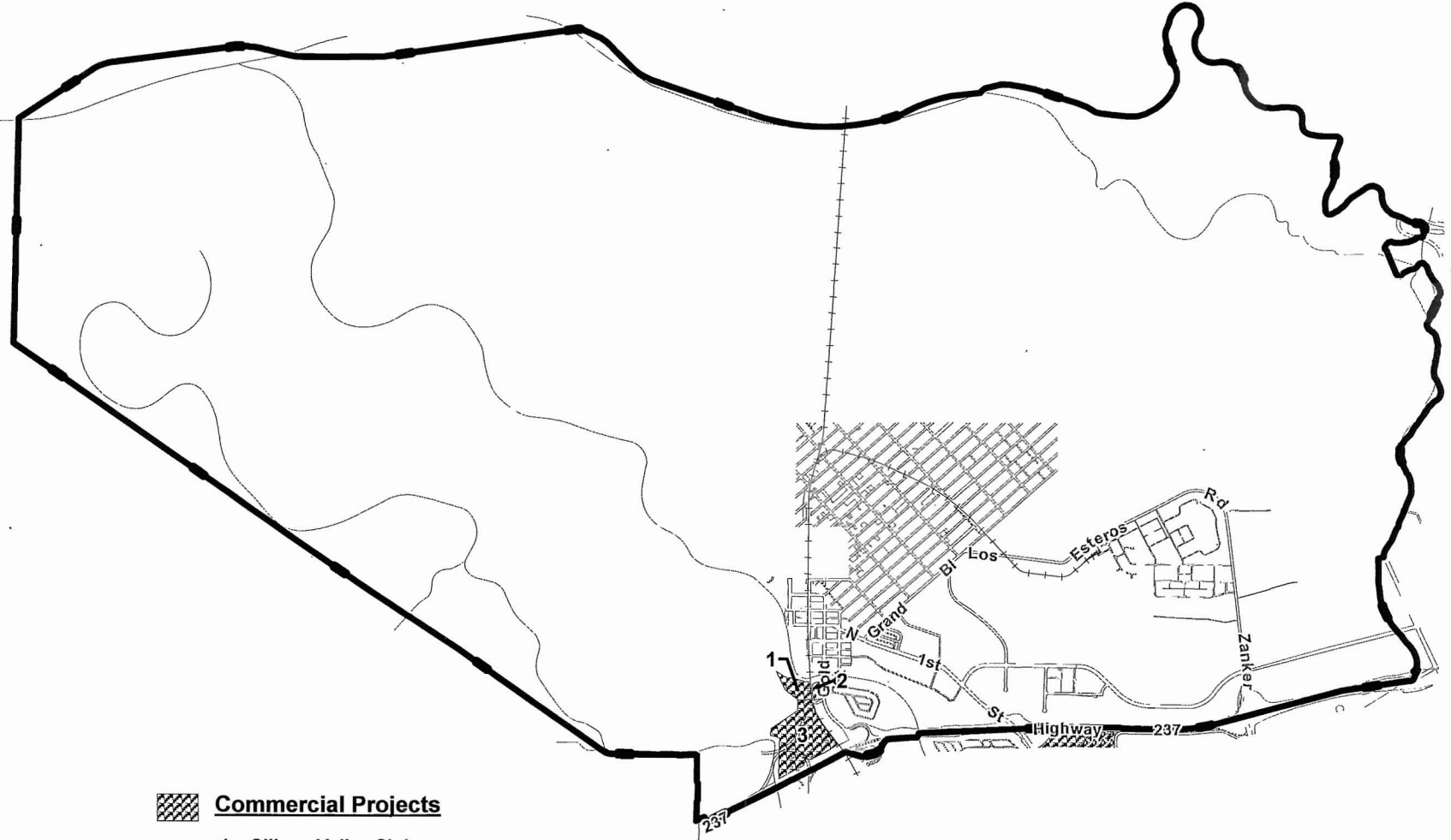
San Jose is divided into a total of fifteen (15) planning areas (see Figure 1, below). The individual planning area maps that follow include projects in all status categories submitted since January 1, 2005. These maps can be used in conjunction with the data contained in Section V of this report to allow closer analysis of the rate, type, and location of major development activity in the City. (Note: map exhibits are not provided for the Almaden, Calero, Coyote, or San Felipe planning areas, as no major development activity occurred there and/or these areas are outside the City's Urban Service Area and Urban Growth Boundary).

Figure 1: San Jose Planning Areas



Alviso Planning Area Major Development Activity

A-16



Commercial Projects

- 1 Silicon Valley Club
- 2 Gold Street Office
- 3 America Center

Total Commercial Sq.Ft.= 1,065,000

North Planning Area Major Development Activity

- Residential Projects**
- 1 Vista Montana Park
 - 2 Renaissance Housing
 - 3 Tasman Apts
 - 4 Baypointe Housing
 - 5 Baypointe Mixed Use
 - 6 Northpointe Mixed Use
 - 7 Riverview Mixed Use
 - 8 River Oaks Housing
 - 9 Crescent Park Apts
 - 10 River Oaks Condos
 - 11 Hyundai Site Mixed Use
 - 12 Seely Apts
 - 13 Airport Parkway Condos
 - 14 Century Center Mixed Use
 - 15 Fourth Street Apts
 - 16 Rosemary Housing

Total Dwelling Units= 9,172

- Commercial Projects**
- 17 Target Stores
 - 18 Retail @ First
 - 19 Hotel Sierra
 - 20 Northpointe Mixed Use
 - 21 Riverview Mixed Use
 - 22 Marriott Residence Inn
 - 23 Coleman Retail
 - 24 Lowe's Home Improvement

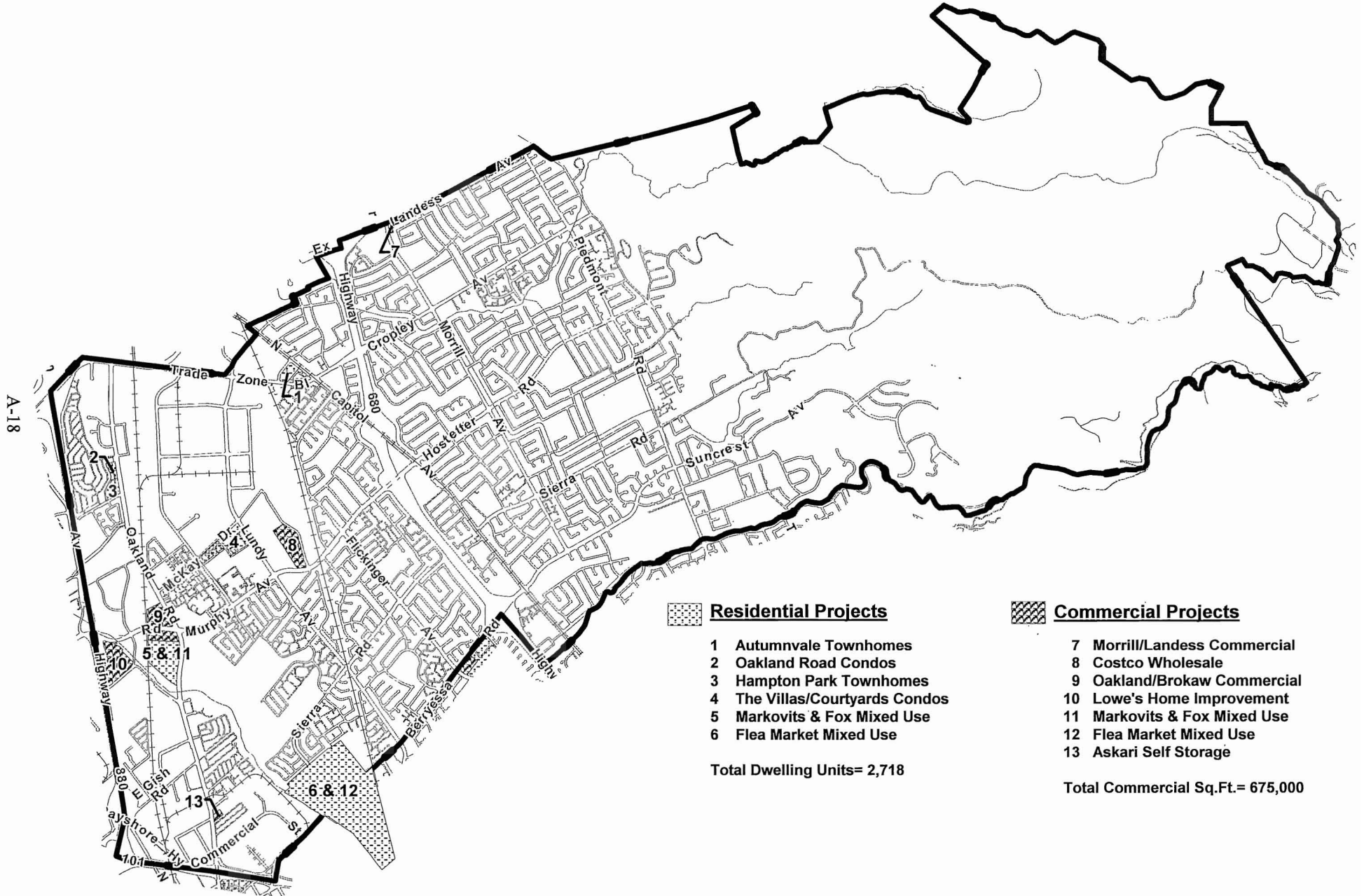
Total Commercial Sq.Ft.= 916,000

- Industrial Projects**
- 25 Brocade Communications
 - 26 Boston Properties (Zanker)
 - 27 Cadence Design Systems
 - 28 Campus @ North First
 - 29 Legacy on 101 Office
 - 30 eBay
 - 31 Skyport Plaza (Phase 2)
 - 32 ACM Aviation Hangar/Office

Total Industrial Sq.Ft.= 6,743,000



Berryessa Planning Area Major Development Activity



Central Planning Area Major Development Activity



 **Residential Projects**

- | | |
|------------------------------|--------------------------------------|
| 1 Modern Ice Townhomes | 21 San Antonio Apts |
| 2 Cornerstone at Japantown | 22 Autumn Terrace at Bonita |
| 3 North Tenth Street Housing | 23 22nd & William Housing |
| 4 Libitzky Mixed Use | 24 Fiesta Senior/Vista on San Carlos |
| 5 Westmount Square | 25 Village Square Condos |
| 6 Vendome Place | 26 San Carlos Mixed Use |
| 7 Japantown Senior Apts | 27 Fifty One Condos |
| 8 Corp Yard Mixed Use | 28 Park Avenue Lofts |
| 9 Ajisai Gardens Condos | 29 Delmas Place Condos |
| 10 San Pedro Condos | 30 Lincoln Avenue Condos |
| 11 Park View Towers | 31 Sunol Court SRO |
| 12 Morrison Park Condos | 32 Ohlone Mixed Use |
| 13 The Carlyle Condos | 33 Monte Vista Condos |
| 14 The Globe Condos | 34 Race Street Housing |
| 15 Market Street Mixed Use | 35 Parkmoor Apts |
| 16 The 88 Condos | 36 Virginia Terrace Condos |
| 17 City Front Square Condos | 37 Edwards Mixed Use |
| 18 Riverpark Condos | 38 South 2nd Mixed Use |
| 19 Three Sixty Condos | 39 Skyline at Tamien Station |
| 20 Casa Feliz SRO | |

Total Dwelling Units= 8,620

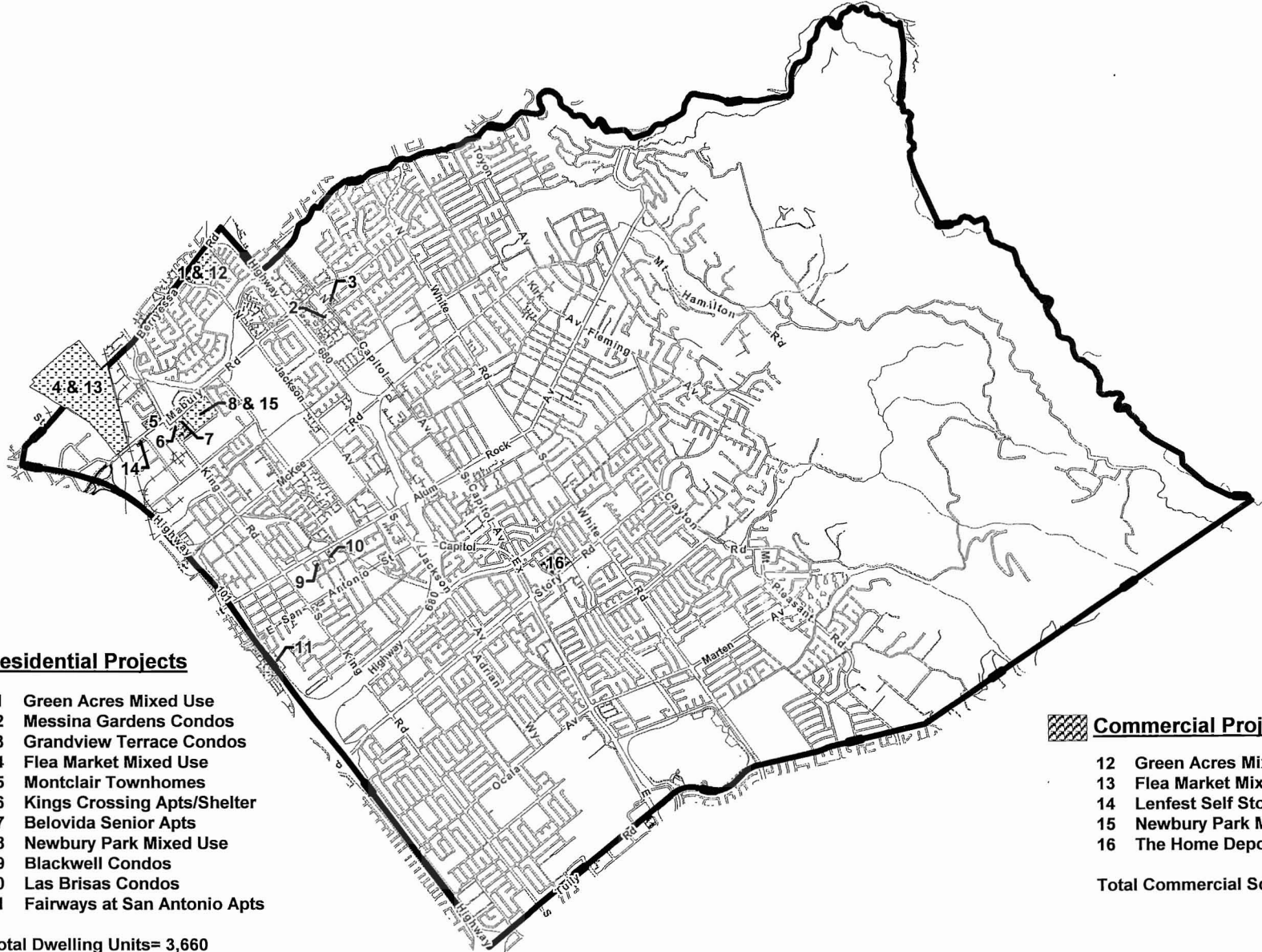
 **Commercial Projects**

- | |
|-----------------------------------|
| 40 Corp Yard Mixed Use |
| 41 Bellarmine College Preparatory |
| 42 Whole Foods Market |
| 43 The Market |
| 44 The 88 Condos |
| 45 City Front Square Condos |
| 46 Riverpark Towers II |
| 47 Vietnam Town Shopping Center |
| 48 Stevens Creek Gateway |
| 49 Ohlone Mixed Use |

Total Commercial Sq.Ft.= 980,000

Alum Rock Planning Area Major Development Activity

A-20



Residential Projects

- 1 Green Acres Mixed Use
- 2 Messina Gardens Condos
- 3 Grandview Terrace Condos
- 4 Flea Market Mixed Use
- 5 Montclair Townhomes
- 6 Kings Crossing Apts/Shelter
- 7 Belovida Senior Apts
- 8 Newbury Park Mixed Use
- 9 Blackwell Condos
- 10 Las Brisas Condos
- 11 Fairways at San Antonio Apts

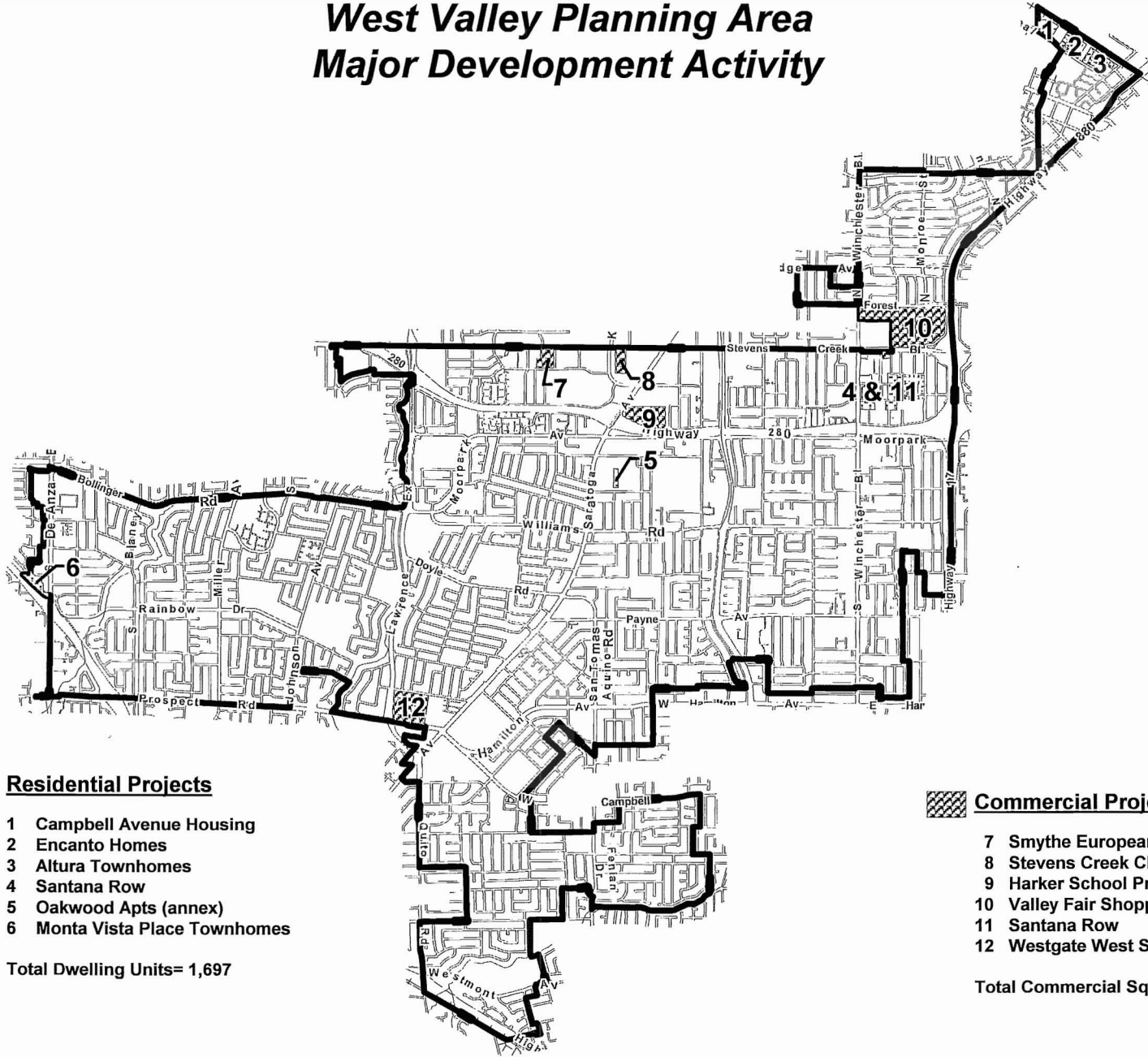
Total Dwelling Units= 3,660

Commercial Projects

- 12 Green Acres Mixed Use
- 13 Flea Market Mixed Use
- 14 Lenfest Self Storage
- 15 Newbury Park Mixed Use
- 16 The Home Depot

Total Commercial Sq.Ft.= 509,000

West Valley Planning Area Major Development Activity



Residential Projects

- 1 Campbell Avenue Housing
- 2 Encanto Homes
- 3 Altura Townhomes
- 4 Santana Row
- 5 Oakwood Apts (annex)
- 6 Monta Vista Place Townhomes

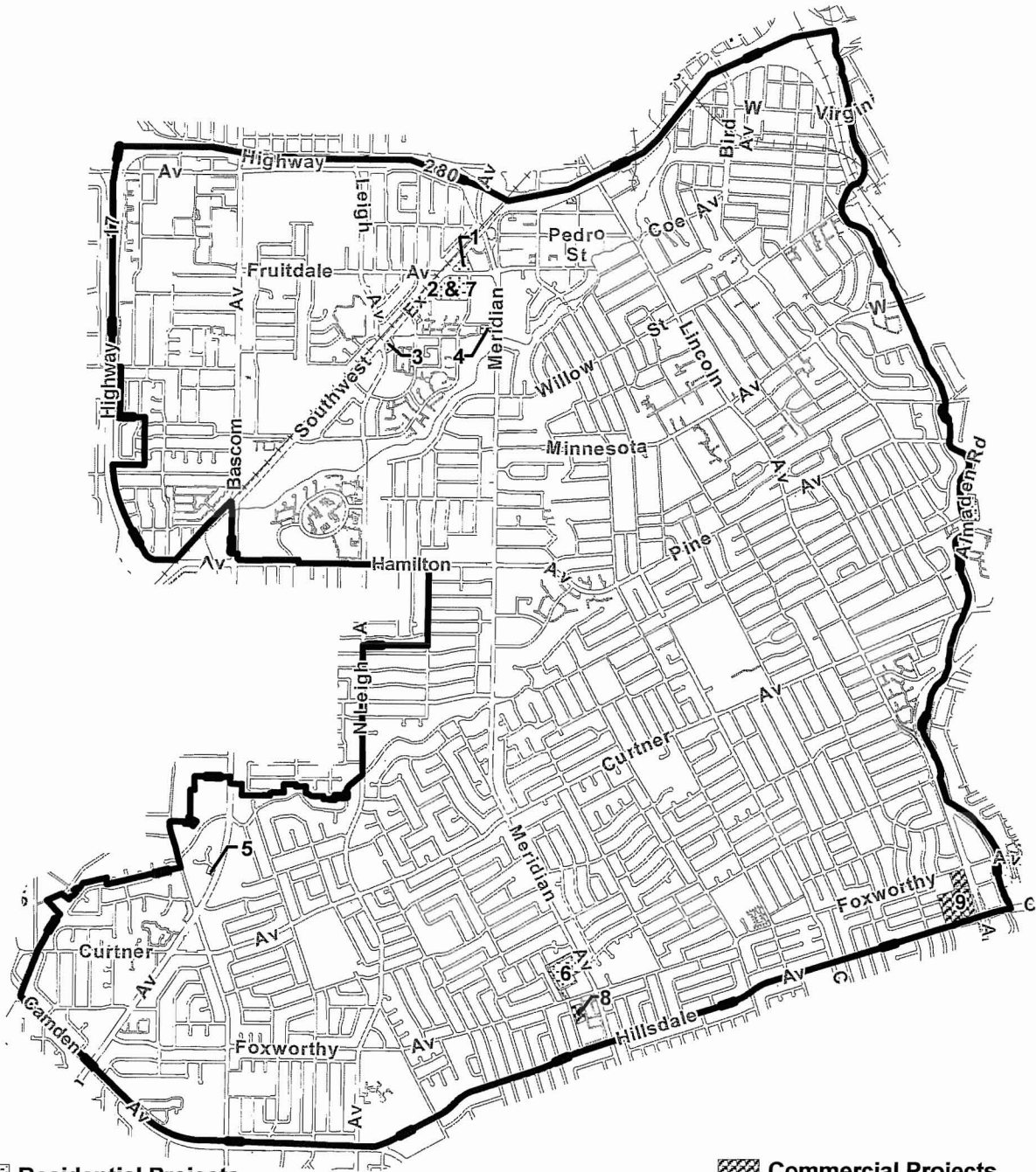
Total Dwelling Units= 1,697

Commercial Projects

- 7 Smythe European
- 8 Stevens Creek Chrysler/Dodge
- 9 Harker School Preparatory
- 10 Valley Fair Shopping Center
- 11 Santana Row
- 12 Westgate West Shopping Center

Total Commercial Sq.Ft.= 1,230,000

Willow Glen Planning Area Major Development Activity



 **Residential Projects**

- 1 Fruitdale Apts
- 2 Fruitdale Station (Phase 2)
- 3 Leigh Senior Housing
- 4 Merrill Gardens Assisted Living
- 5 Bascom Senior Assisted Living
- 6 Willow Glen Place

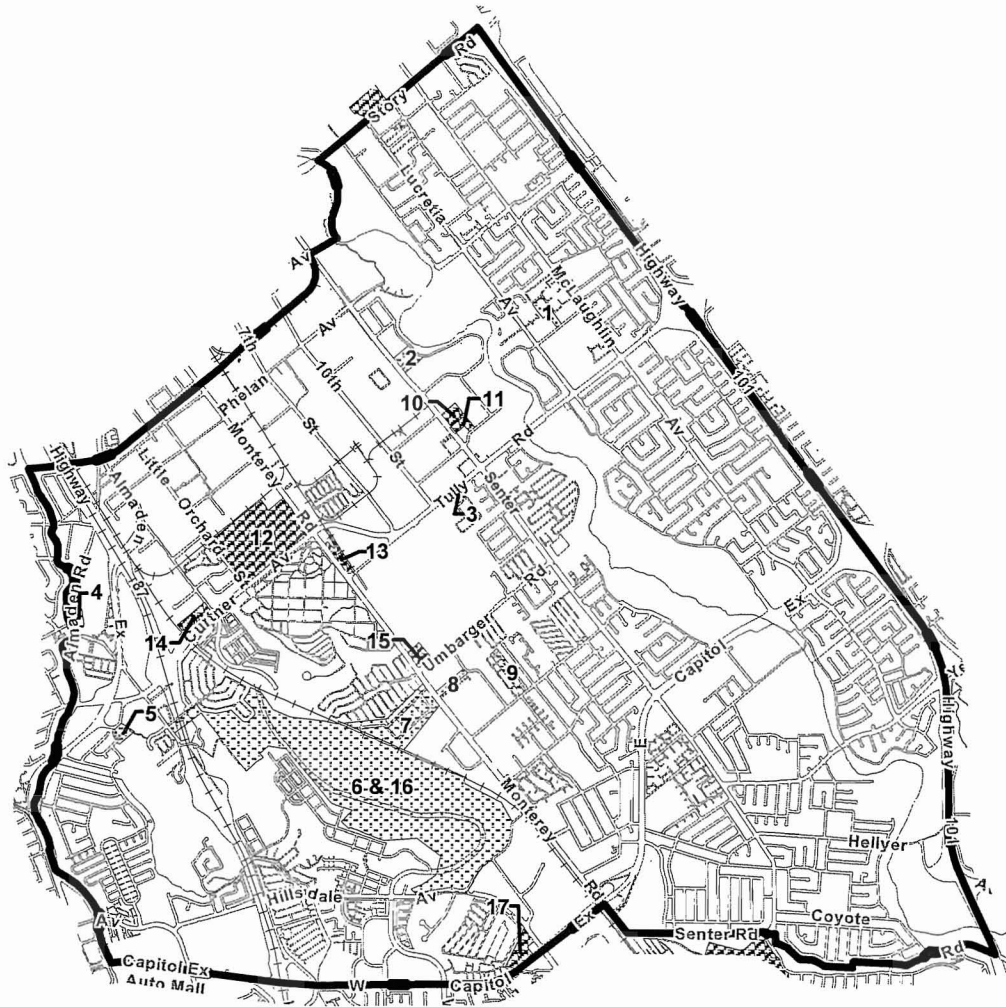
Total Dwelling Units= 781

 **Commercial Projects**

- 7 Fruitdale Station (Phase 2)
- 8 Orchard Supply Hardware
- 9 Almaden Mixed Use

Total Commercial Sq.Ft.= 101,000

South Planning Area Major Development Activity



Residential Projects

- 1 Summerwind Apts (annex)
- 2 Paseo Senter Family Apts
- 3 Fairgrounds Senior Apts
- 4 Almaden Walk Townhomes
- 5 Venetian Terrace Condos
- 6 Communications Hill Mixed Use
- 7 Montecito Vista Mixed Use
- 8 Monterey Family Apts
- 9 Crimson Townhomes

Total Dwelling Units= 4,113

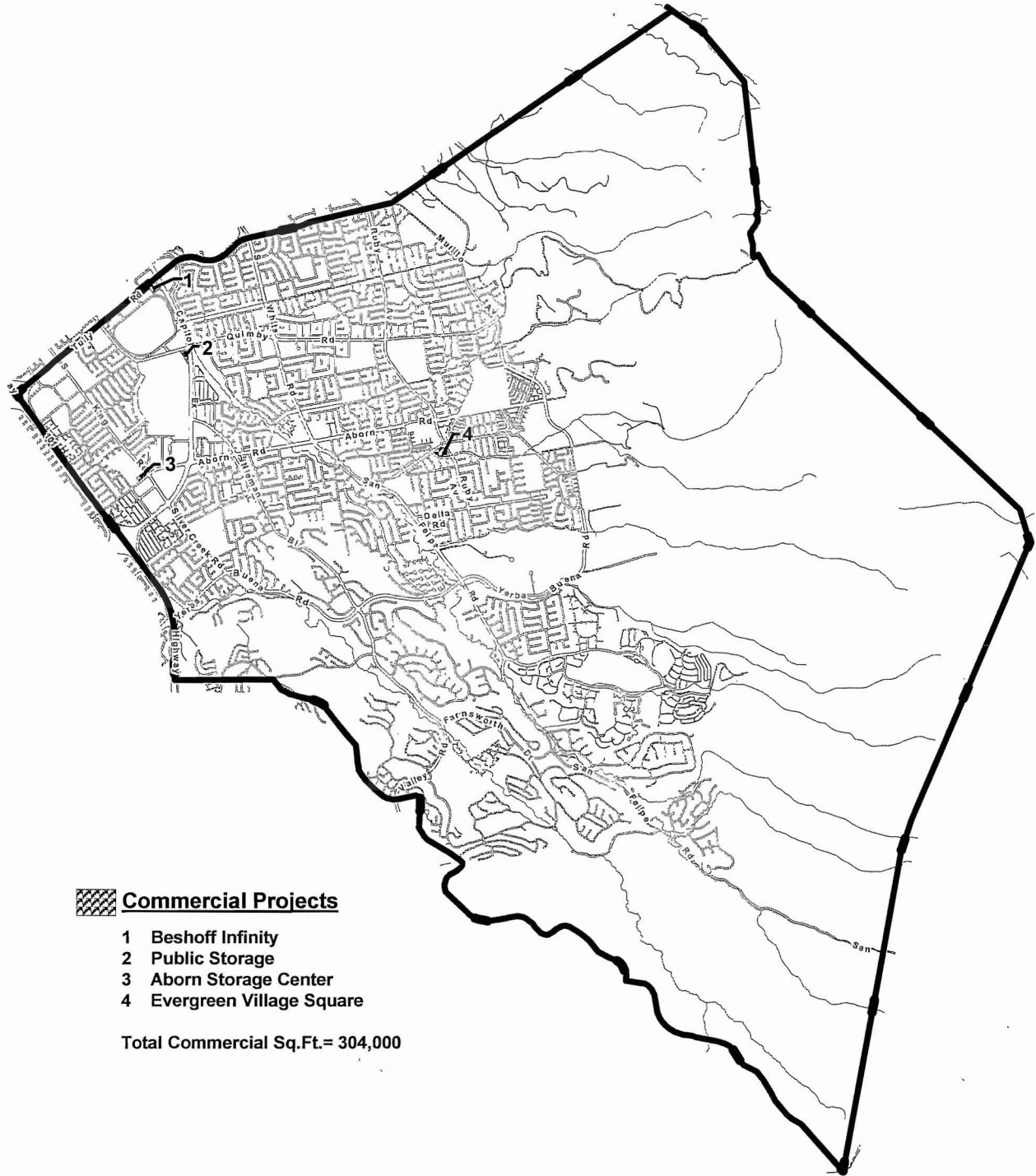


Commercial Projects

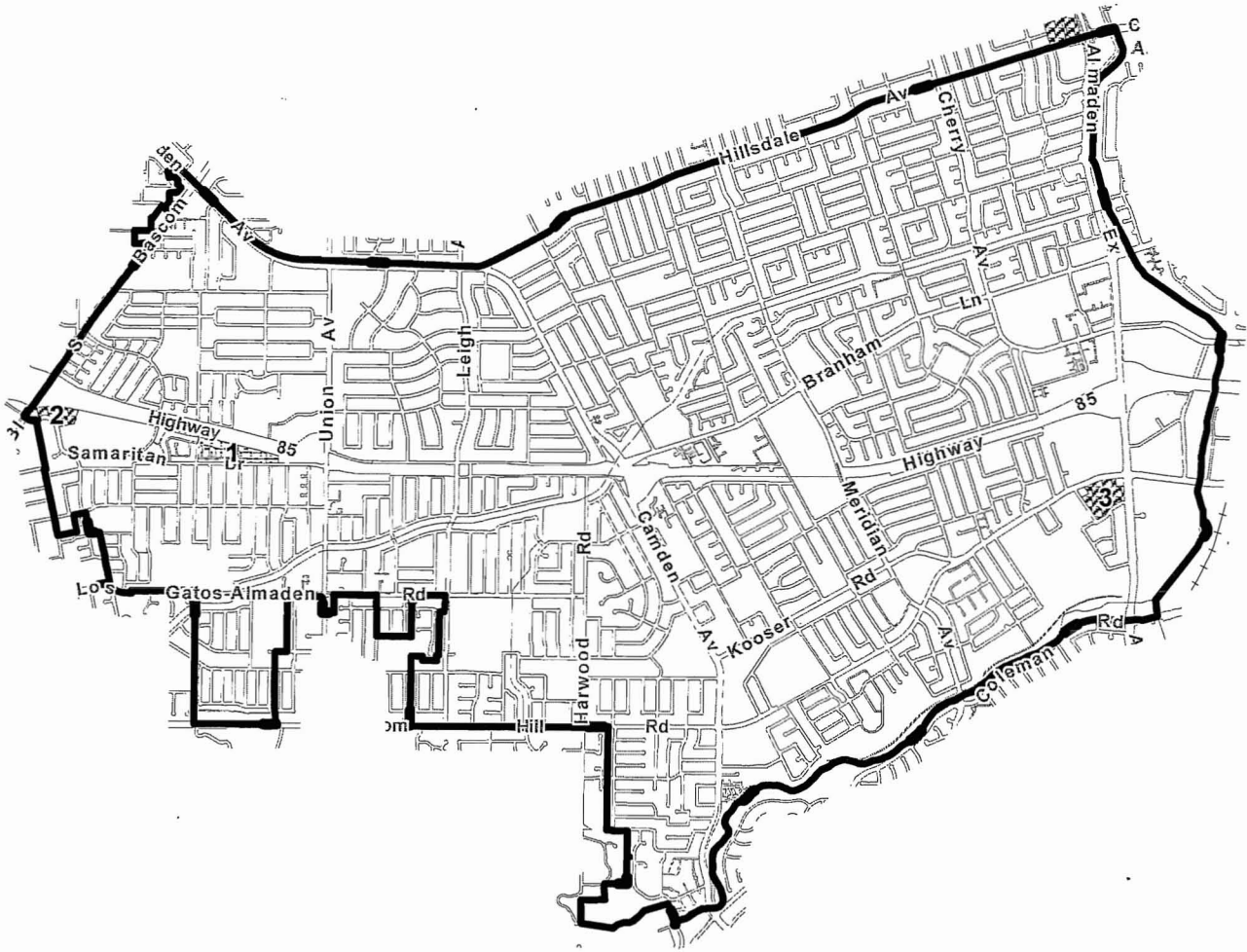
- 10 Senter Office/Retail
- 11 Senter/Quinn Retail
- 12 The Plant Shopping Center
- 13 Tully/Monterey Retail
- 14 Extra Space Storage
- 15 Umbarger Square
- 16 Communications Hill Mixed Use
- 17 Public Storage

Total Commercial Sq.Ft.= 1,092,000

Evergreen Planning Area Major Development Activity



Cambrian/Pioneer Planning Area Major Development Activity



 **Residential Projects**

1 Parkwood Homes

Total Dwelling Units= 202

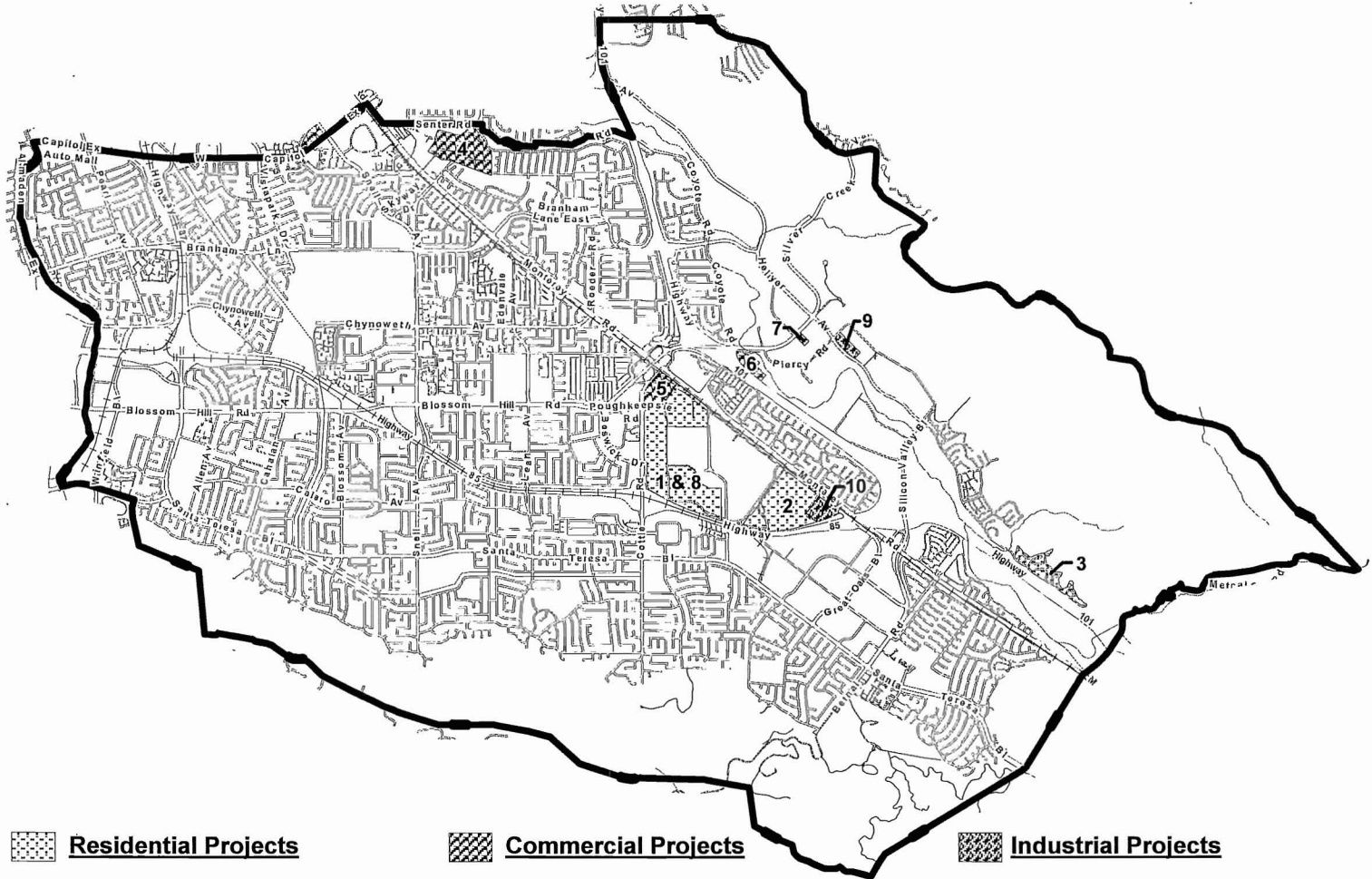
 **Commercial Projects**

2 Samaritan Medical Center

3 Whole Foods Market

Total Commercial Sq.Ft.= 156,000

Edenvale Planning Area Major Development Activity



A-26

Residential Projects

- 1 Hitachi Site Mixed Use
- 2 iStar Site Housing
- 3 Del Rosa at Miramonte

Total Dwelling Units= 4,643

Commercial Projects

- 4 Valley Christian Schools
- 5 Lowe's Home Improvement
- 6 Calif. Center for Health Care
- 7 Silver Creek Valley Retail
- 8 Hitachi Site Mixed Use

Total Commercial Sq.Ft.= 908,000

Industrial Projects

- 9 Hellyer Commons
- 10 Equinix

Total Industrial Sq.Ft.= 258,000

VII. APPENDIX: SOURCES

The Department of Planning, Building and Code Enforcement utilized a variety of information sources in the preparation of this report. These sources are described below.

Data Collection and Analysis

The Department's development project database was the primary initial resource for information on applications submitted to the City. Spreadsheets and Geographic Information Systems (GIS) were also used to manage and display this empirical information in a format that was more readily comprehended. Architectural drawings, aerial photographs, and fieldwork were also used to evaluate site-specific issues that could have affected the anticipated cost or timing of a project's construction.

Planning staff conducted and/or participated in a series of interviews/discussions with a variety of persons, including City staff processing development applications, developers or their representatives, and others working in the development industry or related fields, such as the City's Office of Economic Development and Redevelopment Agency. These discussions surfaced important information on specific development projects as well as provided a forum for review of the economic assumptions underlying the report's five-year forecast.

Review of Publications

Planning staff consulted several publications that made an important contribution to the preparation of this report, including: San Jose Business Journal and San Jose Mercury News (various articles), the Silicon Valley Leadership Group's *Projections 2009*, Joint Venture Silicon Valley Network's *2008 Index of Silicon Valley*, the Association of Bay Area Governments' (ABAG) *Projections 2009* (draft) and *Regional Economic Outlook 2009-10*, Beacon Economics' *2008 South Bay Economic Forecast*, Marcus & Millichap's *Market Research Reports* (periodic), and Commercial Property Service's (CPS) *RealNews* (quarterly).

GENERAL FUND REVENUE DESCRIPTIONS

Property Tax

Under current law, all taxable real and personal property is subject to a tax rate of one percent of the assessed value. (In June 1986, California voters approved a Constitutional Amendment, which provides for an exception to the one-percent limitation. The Amendment allows local governments and school districts to raise property taxes above one percent to finance general obligation bond sales. A tax increase can only occur if two-thirds of those voting in a local election approve the issuance of bonds.) The assessed value of real property that has not changed ownership increases by the change in the California Consumer Price Index or a maximum of two percent per year. Property which changes ownership, property which is substantially altered, newly-constructed property, State-assessed property, and personal property are assessed at the full market value in the first year and subject to the two percent cap, thereafter.

In 1979, in order to mitigate the loss of property tax revenues after approval of Proposition 13, the State legislature approved Assembly Bill 8 (AB 8). This action was approved to provide a permanent method for allocating the proceeds from the one percent property tax rate, by allocating revenues back to local governments based on their historic shares of property tax revenues. AB 8 shifted approximately \$772 million of school district property tax revenue to local governments and backfilled schools' lost revenue with subsidies from the State General Fund. Actions taken by the State in order to balance the 1992-1993 and 1993-1994 State budgets partially reversed the AB 8 formula. The 1992-1993 action reduced the City's Property Tax proceeds by nine percent, and shifted this funding to schools in order to reduce the amount of State backfill required. As part of the State's 1993-1994 Budget, the AB 8 formula was again altered requiring another ongoing shift in City Property Tax revenue to K-12 schools and community colleges.

In November 1993, the City Council elected to participate in the Teeter Plan, which is an alternative method for County property tax apportionment. Under this alternative method authorized by the State legislature in 1949, the County apportions property tax on the basis of the levy without regard for delinquencies. With the adoption of the Teeter Plan in 1993-1994, the City received a one-time buy out of all current, secured property tax delinquencies as of June 30, 1993, which totaled \$3.5 million. Under this system, the City's current secured tax payments are increased for amounts that typically were delinquent and flowed to the secured redemption roll, but it gave up all future penalties and interest revenue derived from the delinquencies.

In 2004-2005, the State budget included a permanent reduction of the Motor Vehicle In-Lieu (MVLIF) tax rate from 2% to 0.65% (its current effective rate). As part of the State budget action, the loss of MVLIF was approved to be replaced with a like amount of property tax revenue, on a dollar-for-dollar basis, and will now grow based on assessed valuations.

GENERAL FUND REVENUE DESCRIPTIONS

Sales and Use Tax

The Sales Tax is an excise tax imposed on retailers for the privilege of selling tangible personal property. The Use Tax is an excise tax imposed on a person for the storage, use, or other consumption of tangible personal property purchased from any retailer. The proceeds of sales and use taxes imposed within the boundaries of San José are distributed by the State to various agencies, with the City of San José receiving one percent.

As of April 1, 2009, the total sales tax rate for the County of Santa Clara will be 9.25%. In February 2009, a temporary 1% increase to the State sales tax rate was approved. This increase is scheduled to sunset in June 2011 or June 2012, with the longer period contingent on voter approval of the proposed Budget Stabilization constitutional amendment. The distribution of the sales tax proceeds is as follows:

Agency	Distribution Percentage
State of California	6.50%
City of San José*	1.00%
Santa Clara County	0.75%
Santa Clara County Transit District	0.50%
Public Safety Fund (Proposition 172)	<u>0.50%</u>
Total Sales Tax	9.25%

Major items, such as services, are exempt from the tax code. As part of a 1991-1992 legislative action, tax exemptions were removed from candy and snack foods, bottled water, newspapers and periodicals, and fuel and petroleum products sold to certain carriers. The removal of these exemptions became effective July 1991. On November 3, 1992, however, the voters approved Proposition 163, which partially repealed the prior action, re-establishing the exemption for snack food, candy, and bottled water effective December 1, 1992.

On November 2, 1993, Proposition 172 was approved allowing for the permanent extension of the half-cent state sales tax that was originally imposed on July 15, 1991, and was to sunset on June 30, 1993. (On July 1, 1993, a six month extension of the tax was granted by the State in order to provide a source of one-time funding for cities and counties to partially offset 1993-1994 ongoing property tax reductions.) The passage of the Proposition 172 legislation, effective January 1, 1994, required that the proceeds from the half-cent tax be diverted from the State to counties and cities on an ongoing basis for use in funding public safety programs.

The local Sales and Use Tax is collected and administered by the State Board of Equalization and is authorized by the Uniform Local Sales and Use Tax Law and the Bradley-Burns Uniform Local Sales and Use Tax Law.

*Note: As part of the Proposition 57 State fiscal recovery funding mechanism (passed by the voters in March 2004), starting July 1, 2004, 0.25% of the City's one percent Bradley-Burns sales tax has been temporarily suspended and replaced dollar-for-dollar with property tax revenue (primarily Educational Revenue Augmentation Funds). This action is to last only for the life of the bonds (currently estimated at five to ten years). The City will, however, continue to record the replacement property tax revenues as sales tax receipts because the growth formula for these receipts is tied to sales tax and because this action is considered to be temporary.

GENERAL FUND REVENUE DESCRIPTIONS

Transient Occupancy Tax

The Transient Occupancy Tax is assessed as a percentage of the rental price for transient lodging charged when the period of occupancy is 30 days or less. The tax rate is currently ten percent, six percent of which is placed in the Transient Occupancy Tax Fund and four percent of which is deposited in the General Fund. The tax is authorized by Municipal Code, Section 4.74, Ordinance number 21931.

The expenditure of the Transient Occupancy Tax Fund portion of the revenues (six percent of room rent) is restricted by Ordinance number 20563 to the following uses:

- 1) Funding for the Convention and Visitors Bureau, including a rental subsidy of City facilities for convention purposes.
- 2) Funding of the cultural grant program and fine arts division programs, including cultural grants, such as the San José Repertory Theatre and the San José Museum of Art, and the expenses of the fine arts division.
- 3) Funding for the City's operating subsidy to the Convention and Cultural Facilities.

The General Fund portion of the Transient Occupancy Tax was enacted as a general tax and cannot be legally dedicated to any specific purpose.

Franchise Fees

The City collects compensation from Pacific Gas and Electric Company (PG&E) for the use of City streets in the distribution of natural gas and electricity. PG&E is assessed two percent of the gross receipts representing its sale of electricity and natural gas within the City limits. Both fees are calculated on gross receipts for a calendar year. The taxes are authorized by Title 15 of the Municipal Code, Chapter 15.32, and no authorized exemptions exist.

From the sale of nitrogen gas, the City collects an annual fee of \$0.119/linear foot of gas-carrying pipe installed within public streets. In addition, each customer is required to pay an annual per connection fee of \$118.76 multiplied by the inside diameter of pipe expressed in inches at the property line. A minimum of \$1,000 total franchise fees per calendar year is required. The fee is authorized by City Ordinance number 20822, and there are no authorized exemptions.

On July 1, 1996, commercial solid waste collection franchise fees (CSW) were converted to a volume basis. This revision amended the previous structure (which had been in effect since January 1, 1995) that assessed a franchise fee equal to 28.28% of gross receipts in excess of \$250,000. With that change, fees were set at \$1.64 per cubic yard per collection for cubic yards in excess of 43,000 (the cubic yard basis is tripled if the waste has been compacted) in a fiscal year, and were assessed on any commercial business engaged in the collection, transportation, or disposal of garbage and/or rubbish (solid waste) accumulated or generated in the City of San José. In December 1997, the City

GENERAL FUND REVENUE DESCRIPTIONS

Franchise Fees (Cont'd.)

Council increased the rate to \$2.41 (excluding the first 29,200 cubic yards hauled in the fiscal year), effective on January 1, 1998. In 1999-2000, this fee was increased to \$2.84 per cubic yard. In 2002-2003, a three year gradual shift in the revenue distribution between the CSW and AB 939 fees (also known as the “commercial source reduction and recycling fee” collected and deposited in the Integrated Waste Management Fund) was approved, that increased the amount collected for CSW to \$3.34 per cubic yard in 2004-2005. In 2005-2006, the City Council increased the fee by 4.5% (\$0.15 per cubic yard) to \$3.49 per cubic yard. In 2006-2007, an additional 5% increase was approved by the City Council, which brings the fee to \$3.67 per cubic yard. The CSW is authorized by Title 9 of the Municipal Code, Chapter 9.08.

The City collects a Franchise Fee from any company that provides cable television (Ordinance number 22128). The current fee is five percent of gross receipts derived from subscriptions. Excluded from the gross receipts are amounts derived from installation, late charges, advertising, taxes, line extensions, and returned check charges.

The Water Franchise Fee was established in 1995-1996 (effective July 27, 1995, Title 15 of the Municipal Code, Section 15.40). The assessment of the fee is allowable under State law, which asserts that a city can collect a franchise fee from a water utility company for laying pipelines and operating them in public right-of-ways. The fee is equal to the greater of either: 1) two percent of the utility’s gross annual receipts arising from the use, operation, or possession of facilities located in public streets within the City limits established on or after October 10, 1911, or 2) one percent of all gross receipts derived from the sale of water within the City limits. Those portions of the water company’s system that are established in private right-of-ways or utility easements granted by private developers are exempted from the franchise fee assessment. It should be noted that the City is not assessing a Water Franchise Fee on the San Jose Water Company due to a Santa Clara Superior Court ruling that states San José cannot impose a franchise fee on that company.

Utility Tax

The Utility Tax is charged to all users of a given utility (electricity, gas, water, and telephone) other than the corporation providing the utility (e.g., a utility company’s consumption of all utilities used in the production or supply of their service is not taxed). For the electricity, gas, and water categories, consumers pay 5% of their utility charges to the utility company that acts as a collection agent for the City. For the telephone utility tax, consumers pay 4.5% on all intrastate, interstate, and international communication services regardless of the technology used to provide such services. Private communication services, voice mail, paging, and text messaging are treated the same as traditional telephone services. In November 2008, voters approved Measure K that reduced the telephone utility rate from 5% to 4.5% and broadened the base for the tax and the definition of technologies covered by the tax. The utility company collects the tax from consumers on a monthly basis and is required to remit that amount to the City by the 25th of the following month. The tax is not applicable to State, County, or City agencies. Also, per State regulations, insurance companies and banks are exempted from the tax. This tax is authorized by Title 4 of the Municipal Code, Section 4.68.

GENERAL FUND REVENUE DESCRIPTIONS

Telephone Tax

In November 2008, voters approved Measure J that replaced the Emergency Communication System Support (ECSS) Fee with a tax in an amount that is 10% less than the ECSS Fee. The tax amount is \$1.57 per telephone line per month and \$11.82 per commercial type trunk line. The City will cease collecting the fee and begin collecting the tax on April 1, 2009. The tax will be collected from telephone users on their phone bills. Exemptions to the tax include low-income seniors and disabled persons who receive lifeline telephone service.

Business Tax

The General Business Tax is assessed according to the following schedule:

Category	Annual Tax
1 – 8 Employees	\$150
9 – 1,388 Employees	\$150 plus \$18 per Employee
1,389 and over Employees	\$25,000

In addition to the rates listed above, City Ordinance number 21518 specifies the assessment of taxes by grouping taxed businesses (each at a different rate) in the following categories: Rental or Lease of Residential or Non-Residential property, Mobile Home Parks, and Water Companies. Rented or leased properties (if three or more residential rental units) are subject to the \$150 minimum tax, but are also assessed \$5/rental unit over 30 units for residential properties and \$0.01 per square foot in excess of 15,000 square feet for non-residential properties. Fees for both residential and non-residential properties are limited to a maximum of \$5,000. Mobile home parks are treated as residential properties. Water companies are assessed by a schedule that assigns an amount (from \$200 to \$20,000) depending on the number of active metered connections. In November 1996, the rates had been increased to reflect an annual inflation factor as part of the New Realities Task Force recommendations contingent on voter approval. Because the voters did not approve the continuation of the increase in November 1998, the rates (as reflected) have been returned to the levels prior to November 1996.

There are several exclusions (by federal or State regulations) or exemptions (by the City Council) from the General Business Tax. Among the major ones are banks and insurance companies, charitable and non-profit organizations, and interstate commerce. In addition, on June 8, 1993, City Council deleted the sunset provision of a business tax exemption for certain artists and craftpersons selling their wares at one location. The Business Tax is authorized by Title 4 of the Municipal Code, Chapter 4.76.

On May 26, 1987, the City Council enacted a new Disposal Facility Tax which became effective July 1, 1987. The rate structure is based on the weight of solid waste disposed. On July 1, 1992, City Council increased the Disposal Facility Tax from \$3.00 per ton of disposed waste to \$13.00 per ton. This tax is assessed on landfills located in the City of San José. Beginning 2002-2003, waste previously classified as alternate daily cover was made subject to the Disposal Facility Tax. However, after a legal challenge, the City reinstated the Alternate Daily Cover exemption in August 2005.

GENERAL FUND REVENUE DESCRIPTIONS

Business Tax (Cont'd.)

During 1991-1992, Council approved the establishment of a Cardroom Ordinance which contained the provision to tax gross receipts from cardrooms located in the City. On June 9, 1992, City Council approved an ordinance amending the San José Municipal Code that increased the tax rate schedule and expanded the permissible games authorized. A gross receipt monthly tax schedule was established with taxes ranging from 1% to 13% of gross receipts. In 1993-1994, Council approved a revision to the Cardroom Ordinance, instituting a flat 13% gross receipts tax for all cardrooms located in the City with annual gross revenues in excess of \$10,000.

Other Licenses and Permits

The City requires payment for the issuance of Building Permits, Fire Permits, and miscellaneous health and safety-related licenses and permits. For most licenses and permits, the various fees charged by a given department are based on full recovery of the estimated costs for providing each service. For example, the City requires fire safety inspections of all commercial property. The fee provides for inspection charges and a number of special charges. Authorized exceptions include the addition and/or alteration of under 20 sprinkler heads and the installation of portable fire extinguishers. The fee is authorized by Title 17 of the Municipal Code, Chapter 17.12.

Where appropriate, license and permit fees take into consideration approved exceptions to Council's full cost recovery policy, as well as applicable State laws. Specific prices and rates are determined by ordinance and each of the charges is fully explained in the City's Fees and Charges Report, which is released in May of each year.

Fines, Forfeitures, and Penalties

The City receives a portion of the fines collected in connection with violations of the State Vehicle Code on city streets. Various fines may be assessed in addition to those imposed by the Santa Clara County bail schedule and judges' sentences. The County court system collects the fines as authorized by the State Vehicle Code and makes monthly remittances to the City. Only "on call" emergency vehicles are exempt from Vehicle Code street laws. State legislative action in 1991-1992 reduced the amount (by approximately 50%) of vehicle code fine and forfeiture revenue forwarded to the City. On October 10, 1997, however, the Governor signed Assembly Bill 233 (AB 233) which was effective on July 1, 1998. AB 233 changes how the State and California counties and cities share in traffic citation fine revenues. This legislation essentially results in the doubling of the City's revenue collections in this area, reversing the impact of the 1991-1992 state legislative action.

The City receives fines and forfeitures of bail resulting from violation of State Health and Safety Codes and City Ordinances. These fees, authorized by the State Criminal Code and City Ordinances, are collected by the County and remitted to the City on a monthly basis. The City also receives revenue collected in connection with violations of the City's vehicle parking laws. These fines vary according to the nature of the violation. The City pays an agency to process and collect the fines. The only authorized exemption is for "on call" emergency vehicles.

GENERAL FUND REVENUE DESCRIPTIONS

Use of Money and Property

The City invests idle funds in order to earn interest. The total income varies with the market rates of interest and the funds available to invest. The City has established a formalized and conservative investment policy with objectives emphasizing safety and liquidity. This policy provides guidelines for type, size, maturity, percentage of portfolio, and size of security issuer (among others) of each investment. In addition, the policy statement outlines several responsibilities of the Council, Manager, Auditor, Finance Director, and Finance Department. These policy and monitoring units interact and produce investment performance reports and an annually updated investment policy. All reports and policies must be reviewed and approved by both the City Manager and Council. Investment of funds is authorized by the City Charter, Section 8066.

Revenue is also received from the rental of City-owned property and from the sale of agricultural products grown on City land. Exceptions are created by Council resolution. The fees are authorized in Title 2 of the Municipal Code, Section 2.04.1070.

Revenue from Local Agencies

This revenue category contains revenue received from a variety of other local government agencies. The five primary sources of revenue are the reimbursement for City staff and overhead costs from the Redevelopment Agency; the reimbursement from the Redevelopment Agency for payment of the Convention Center debt service; Enterprise Fund In-Lieu charges; payments from the Central Fire District for fire services provided to District residents by the San José Fire Department; and payments from the County for the Paramedic Program.

Revenue from the State of California

The City receives revenue from the State of California in a number of different forms. While the State provides the City with funds through grants and contracts for services, by far the largest source of funds is In-Lieu Taxation.

The Motor Vehicle In-Lieu (MVLFF) Tax revenues are license fees collected by the California Department of Motor Vehicles (DMV). Until 1998-1999, the annual license fee was two percent of the market value of the vehicle as determined by the DMV. In 1998-1999, the State reduced the license fees by 25%, but agreed to backfill local jurisdictions for the loss in revenue, which represented 67.5% of MVLFF revenues received by the City at the time. In 2004-2005, as part of State budget actions, the MVLFF rate was permanently reduced from 2% to 0.65% (the current effective rate) and all future receipts of the backfill were approved to be in the form of increased Property Tax receipts and is reflected in that category. Thus, the backfill amount due the City has permanently become property tax revenue that now grows based on assessed valuations.

GENERAL FUND REVENUE DESCRIPTIONS

Revenue from the State of California (Cont'd.)

The State withholds less than five percent of these fees for the support of the DMV. More than 95% of these fees are divided equally between counties and cities, and their aggregate shares are distributed in proportion to the respective populations of the cities and counties of the State. The exemptions authorized by the State Constitution, Article 13, include vehicles owned by insurance companies and banks, publicly owned vehicles, and vehicles owned by certain veterans with disabilities. The tax is authorized by the State Revenue and Taxation Code.

In-Lieu Taxes are also levied against airplanes. While the method of collection is similar, the distribution is different. Revenue is distributed according to the location of the aircraft, which is then allocated to cities, counties, and school districts. State legislative action in 1992-1993 eliminated local Trailer Coach In-Lieu Tax revenues. These funds were shifted to the State General Fund.

Revenue from the Federal Government

Federal grants account for the majority of federal revenues. Grant programs must be specifically outlined and proposed for federal sponsorship. Due to the grant process, the volume of grants and level of revenue has been and will be sporadic.

Departmental Charges

Departmental Charges are comprised of fees charged for services which are primarily provided by the following departments: Planning, Building and Code Enforcement; Police; Public Works; Transportation; Library; and Parks, Recreation and Neighborhood Services. The Parks, Recreation and Neighborhood Services Department, for example, charges specific fees for various recreational programs, such as aquatic and adult sports programs. The prices and rates are determined by ordinance, and each of the several hundred charges is fully explained in the City's Annual Fees and Charges Report.

GENERAL FUND REVENUE DESCRIPTIONS

State Gas Tax

A portion of the State Gas Tax is shared with cities and counties under separate sections of the Streets and Highways Code. The 1964 Gas Tax (Section 2106) provides for a \$0.0104 charge on every gallon of gasoline. Revenue is then allocated according to the following formula:

County Allocation : **a** No. of Registered Vehicles in County
 ÷ **b** No. of Registered Vehicles in State
 x c \$0.0104
 x d Gallons of Gas Sold

City Allocation: **a** Incorporated Assessed Value in County
 ÷ **b** Total Assessed Value in County
 x c County Allocation

Individual City Allocation: **a** Population in City
 ÷ **b** Population all Cities in County
 x c City Allocation

The 1943 Gas Tax (Section 2107) authorized a per gallon charge of \$0.00725. The State allocates part of these revenues for snow removal; the balance is distributed by calculating the portion of the State-incorporated population represented by the city's population.

As a result of the passage of Proposition 111, gas and diesel taxes were increased \$0.05 per gallon on August 1, 1990, and increased by \$0.01 per gallon each January 1 until January 1, 1994. For this 1990 Gas Tax (Section 2105), cities are apportioned a sum equal to the net revenues derived from 11.5% of highway users taxes in excess of \$0.09 per gallon in the proportion that the total city population bears to the total population of all cities in the State.

Other Revenue

This revenue category contains revenue received from a variety of miscellaneous sources. For several years, Solid Waste Program revenues comprised the majority of revenues in this category. However, as approved by the City Council on November 22, 1994, approximately \$55.77 million in budgeted Solid Waste revenues were removed from this category to reflect the implementation of the newly established Integrated Waste Management (IWM) Fund. Revenue categories appearing in the IWM Fund include: Recycle Plus charges (Residential and Commercial), Assembly Bill 939 (AB 939) fees, and lien revenues related to billings which took place after the creation of the new fund. Revenues that remained in the General Fund are related to the collection of solid waste enforcement fees. These fees are now reflected in the Departmental Charges category.

GENERAL FUND REVENUE DESCRIPTIONS

Other Revenue (Cont'd.)

Other significant sources of revenue in this category include the following components: cost reimbursements related to Finance Department staff in the Investment Program; and HP Pavilion rental, parking, suite, and naming revenues. The remainder of revenue collected represents one-time and/or varied levels of reimbursements, including sale of surplus property receipts and miscellaneous revenues associated with the Office of the City Attorney.

Transfers and Reimbursements

The Transfers and Reimbursements revenue category is used to account for funds received by the General Fund from other City funds through a combination of means, including operating and capital fund overhead charges, transfers, and reimbursements for services rendered.

Overhead charges are assessed to recover the estimated fair share of indirect General Fund support services costs (staff and materials) that benefit other City program and fund activities. Examples of support activities included in the charges are services provided by the following departments: Finance, Human Resources, Information Technology, the Office of the City Manager, and the Office of the City Attorney. Each year the charges are calculated using Finance Department developed overhead rates applied to projected salary costs in most City funds. The most significant source of overhead reimbursements is generated from the Treatment Plant Operating Fund, the Sewer Service and Use Charge Fund, the Airport Maintenance and Operation Fund, and the Integrated Waste Management Fund.

Transfers consist of both one-time and ongoing revenue sources to the General Fund. Ongoing transfers include Airport Maintenance and Operation Fund reimbursements for Airport Police and Fire services and capital fund transfers for maintenance and operating expenses incurred by the General Fund. One-time transfers occur on a sporadic basis and have included the disposition of uncommitted fund balances in several special funds and the transfer of monies to fund a variety of City projects. Reimbursements from other funds represent the cost to the General Fund for services provided on behalf of the other City funds.