PSFSS COMMITTEE: 6/17/2021
ITEM: (c) 1

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: PUBLIC SAFETY, FINANCE, AND STRATEGIC SUPPORT COMMITTEE

FROM: Jim Shannon

SUBJECT: **BI-MONTHLY FINANCIAL REPORT FOR MARCH/APRIL 2021**

DATE: June 10, 2021

Approved Jennifer A Maguire Date June 10, 2021

RECOMMENDATION

Accept the Bi-Monthly Financial Report on actual revenues and expenditures as compared to the 2020-2021 Budget for the ten months ending April 2021.

OVERVIEW

The Bi-Monthly Financial Report for March/April 2021 was jointly prepared by the City Manager's Budget Office and the Finance Department and is presented for the Public Safety, Finance and Strategic Support Committee's review. The City Manager's Budget Office has analyzed actual expenditures as compared to the 2020-2021 Modified Budget and the Finance Department has prepared a report that reflects the financial results for the ten months ending April 2021.

In Silicon Valley, economic conditions drastically changed due to the shelter-in-place order that was issued in Santa Clara County on March 17, 2020. To comply with the order, a significant portion of economic activity was severely restricted, which has had deep impacts to many of the economically sensitive revenues in the General Fund and other City funds. Conditions improved in the summer and early fall; however, due to second wave of coronavirus, conditions worsened again in the winter months, as stay-at-home orders were once again implemented. Fortunately, as caseloads continue to drop due to continued vaccine distribution, health restrictions are anticipated to continue easing, which should have positive impacts on economic conditions.

Through the first ten months of the fiscal year, revenues and expenditures were generally tracking within the revised budgeted estimates in the majority of City funds, with some exceptions as noted below. Additionally, the Administration continues to closely monitor economic conditions and the performance in all City funds, and will bring forward adjustments, as appropriate, to the City Council as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum, which will be reviewed at the June 22, 2021 City Council meeting. Following are key highlights in this report:

OVERVIEW (CONT'D.)

- Overall, General Fund revenues are anticipated to exceed budgeted levels by approximately $30 million. Budget adjustments are included in the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum to increase the Property Tax revenue estimate ($18 million) and the Real Property Transfer Tax revenue estimate ($10 million) to align the budgeted estimates with anticipated collections. Per City Council direction, the Real Property Transfer Tax revenue will be expended on homeless prevention and affordable housing projects and programs. The additional Property Tax revenue will be used to offset other recommendations in the memorandum and to establish the 2020-2021 Ending Fund Balance Reserve, which was assumed as part of the development of the 2021-2022 Proposed Budget.

- Overall, General Fund expenditures tracked within or slightly below estimated levels through April. Expenditures will continue to be controlled – including the continuation of the hiring freeze and exemption review process established back in March 2020 – to ensure appropriations stay within approved levels and generate vacancy savings to provide a cushion against future budgetary uncertainty.

- Downward budgetary adjustments were brought forward as part of the 2020-2021 Mid-Year Budget review for Convention and Cultural Affairs Fund, the Convention Center Facility District Revenue Fund, and the Transient Occupancy Tax Fund, to align the budget with estimate collection levels. As collections continue to be impacted by the pandemic, these revenues will be closely monitored. Contingent on activity levels for the final few months of the fiscal year, revenues may fall slightly below the revised estimates.

- Building and Structure Construction Tax and Construction Excise Tax collections began to experience significant slowdowns in activity beginning in February 2021 and are anticipated to fall below budgeted levels. Budget adjustments are included in the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum to decrease the revenue estimates to align with the anticipated collections. Construction and Conveyance Tax revenues remain strong and are expected to exceed budgeted levels.

- All Development Fee Programs are anticipated to end the year slightly above budgeted levels.

- The Norman Y. Mineta San José International Airport (SJC) has enplaned and deplaned 2.9 million passengers through April, a decrease of 73.9% from the figures reported through April of the prior year. This year-over-year drop is due to the ongoing effect the pandemic is having on air travel and was anticipated as part of the 2020-2021 Adopted Budget.

- San José Clean Energy (SJCE), whose operations are captured in the San José Clean Energy Fund is facing several challenges including increasing regulatory fees, a pandemic-related increase in non-payment from customers, change in load, and increasing energy costs. Additionally, as a result of the increasing Power Charge Indifference Adjustment (PCIA) fees, the Community Energy Department recommended a rate increase and new service offerings that were approved by City Council in May 2021 to mitigate the financial impacts to customers and the SJCE program. A more in-depth discussion regarding the challenges SJCE faces, and a recommendation to draw upon the City's commercial paper program to address near-term financial issues, will take place at the City Council meeting on June 22, 2021.

OVERVIEW (CONT'D.)

Economic Environment

Economic conditions in the Silicon Valley significantly changed in Spring 2020 as a result of the pandemic. Due to the steep rise in COVID-19 cases during the fall and winter months, the initially slow rollout of the vaccine, and ongoing social distancing requirements that will remain in place for nearly the entire fiscal year, economic conditions, including employment levels, are anticipated to continue to be suppressed during 2020-2021.

The April 2021 employment level in the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (San José MSA) of 1.08 million was 6.9% above the April 2020 level of 1.01 million. Between April 2020 and April 2021, employment in the San José MSA increased by 69,800 jobs. This increase includes leisure and hospitality jobs increasing by 14,600 jobs; construction jobs increasing by 14,200; the trade, transportation, and utilities sectors expanding by 12,800 jobs; and private educational and health services increasing by 10,100 jobs.[1]

After topping at 12.0% in April 2020, the local unemployment rate has significantly dropped. In February 2021, the local unemployment rate was 5.1%, which is significantly lower than April 2020 (12.0%) and July 2020 (9.5%). Additionally, while local unemployment figures have risen since the shelter-in-place began, the unadjusted rates continue to be lower than the State and the national levels.

Unemployment Rate (Unadjusted)

	Feb. 2020	April 2020	July 2020	April 2021**
San Jose Metropolitan Statistical Area*	2.6%	12.0%	9.5%	5.1%
State of California	4.3%	16.2%	13.9%	8.1%
United States	3.8%	14.4%	10.5%	5.7%

* San Benito and Santa Clara Counties Source: California Employment Development Department.
** April 2021 estimates are preliminary and may be updated.

[1] State of California Employment Development: Labor Market Information Division Press Release, May 21, 2021

OVERVIEW (CONT'D.)

Overall construction activity through April 2021 decreased 4.0% from 2019-2020 levels. The decrease is primarily due to declines in residential and industrial activity. Extremely strong commercial activity in the first quarter of this fiscal year is propping up the levels for this year and mitigating the year-over-year decrease. The 2020-2021 Adopted Budget was developed with the expectation that private development activity would be significantly weaker than previous years.

Private Sector Construction Activity (Valuation in $ Million)

	April 2020	April 2021	% Change
Residential	$337.6	$280.4	(16.9%)
Commercial	$762.5	$1,026.7	34.7%
Industrial	$634.4	$357.9	(44.6%)
TOTAL	**$1,734.4**	**$1,665.0**	**(4.0%)**

Through April, residential permit valuation has decreased 16.9% from prior year levels ($280.4 million in 2020-2021 compared to $337.5 million in 2019-2020). Residential activity through April included 726 multi-family units and 455 units of single-family construction for a total of 1,181 units. Major residential projects in April were permits issued for an 87-unit affordable housing project and a 46-unit affordable housing project.

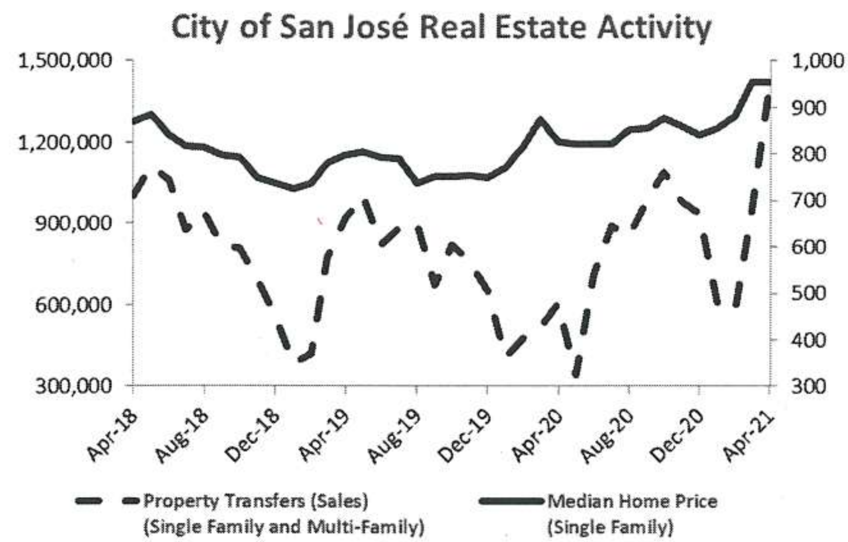
Commercial valuation through April 2021 was 34.7% higher than the 2019-2020 level ($1,026.7 million in 2020-2021 from $762.5 million in 2019-2020). Commercial activity in March and April was modest ($69.7 million) with additions/alterations accounting for most of the commercial activity for the two months ($49.3 million). A notable project for March included finished interior permits issued for a five-story, 162,000 square foot office building.

Industrial construction valuation through April was 44.6% lower than prior year levels, with receipts totaling $357.9 million in 2020-2021 and $634.4 million in 2019-2020, which was an historically high figure. Similar to the same period for last year, a spike in permit valuations in July has propped up the valuation level thru April of this fiscal year. Alterations accounted for all of the activity in March and April.

Real estate activity was anticipated to be sluggish in 2020-2021 due to to higher unemployment rates coupled with lower consumer confidence. According to data from the Santa Clara County Association of Realtors, the number of property transfers (sales) experienced year-over-year decreases (from the same time period in the prior year) ranging from -10% to -54% between the beginning of the shelter-in-place in March 2020 through June 2020. However, for 2020-2021, beginning in September, the local real estate market once again began to experience year-over-year gains. Through April, there were a total of 6,672 property transfers for all residences, which

OVERVIEW (CONT'D.)

represents growth of almost 30% from April 2020 levels. In addition, median single family home prices remain strong. As of April 2021, the median single family home price totaled $1.42 million, which represents an 18.3% increase from the April 2020 price of $1.20 million. Finally, it is taking significantly less time to sell these more expensive homes. The average days-on-market in April 2021 totaled 14 days, which is significantly below the average of 23 days experienced in April 2020.



On a national level, consumer confidence rose again in April, after a substantial gain in March. Lynn Franco, Senior Director of Economic Indicators at The Conference Board, stated "Consumer confidence has rebounded sharply over the last two months and is now at its highest level since February 2020. Consumers' assessment of current conditions improved significantly in April, suggesting the economic recovery strengthened further in early Q2. Consumers' optimism about the short-term outlook held steady this month. Consumers were more upbeat about their income prospects, perhaps due to the improving job market and the recent rebound of stimulus checks."[2]

As suggested by a number of economic indicators, the local economy appears to continue improving as vaccination rates increase and state and local restrictions continue to ease. These economic conditions were taken into consideration in the development of the 2021-2022 Proposed Budget, which was released May 4, 2021.

GENERAL FUND

REVENUES

General Fund revenues through April 2021 totaled $1.05 billion, which represents an increase of $159.2 million from the April 2020 level. This year-over-year increase is primarily attributable to the City receiving Tax and Revenue Anticipation Notes (TRANs) in the current year ($130.0 million) to facilitate the pre-payment of a portion of the City's 2020-2021 retirement contributions; retirement pre-payment did not occur in 2019-2020. Additionally, the Real Property Transfer Tax

[2] The Conference Board, Consumer Confidence Survey, April 27, 2021

GENERAL FUND (CONT'D.)

did not begin until July 2020, therefore no revenue was received in 2019-2020, compared to $32.7 million collected through April 2021. Partially offsetting the higher revenues is a significant year-over-year decrease related to the Development Fee Program. Revenue totaling $63.0 million was received through April 2020; however, revenue is no longer captured in the General Fund in 2020-2021 as these revenues (and associated expenditures) have been moved out of the General Fund and into specific Development Fee Program funds. After adjusting for these significant variances, revenue in 2020-2021 has increased approximately $59.5 million (7.2%) from the prior year.

Several revenue categories are experiencing growth compared to prior year levels, including Property Tax ($65.1 million), Sales Tax ($11.3 million), Transfers and Reimbursements ($8.4 million), Revenue from the State of California ($7.4 million), Revenue from Local Agencies ($3.1 million), and Utility Tax ($2.2 million). The higher collections for Property Tax and Utility Tax revenues are due to stronger performance than the prior year, and the higher collections for Sales Tax are primarily attributable to the Revenue Capture Agreement with eBay, which had partial collections in 2019-2020, but is annualized in 2020-2021. These categories are further described later in this report. Revenue from the State of California and Revenue from Local Agencies have higher collection levels than the prior year due to the timing of payments. Finally, Transfers and Reimbursements revenue is higher through April 2021 due to overhead reimbursement revenue related to the Development Fee Programs being captured in the General Fund beginning in 2020-2021. Partially offsetting this higher collection level, are year-over-year declines in several revenue categories, including Fees and Charges (excluding Development Fee Program revenue; (-$15.8 million); Transient Occupancy Tax (-$9.3 million), Fines, Forfeitures and Penalties (primarily Parking Fines; -$8.2 million), and Business Taxes (-$8.0 million). The lower collections for Fees and Charges (Parks, Recreation and Neighborhood Services Department fee revenue), Business Taxes (Cardroom Business Tax), Transient Occupancy Tax, and Fines Forfeitures and Penalties (Parking Fines) are primarily the result of impacts related to the COVID-19 pandemic and public health orders, much of which was anticipated and built into the revenue assumptions as part of the 2020-2021 Adopted Budget or modified as part of the 2019-2020 Annual Report or the 2020-2021 Mid-Year Budget Review.

General Fund revenues are anticipated to slightly exceed budgeted levels by approximately $30 million, which is due to variances in several revenue categories. Revenues that are anticipated to exceed their budgeted estimate include Property Tax ($18 million), Real Property Transfer Tax ($10 million), Sales Tax ($6.5 million), Business Taxes ($3 million), and Utility Tax ($3 million). However, partially offsetting these increased revenues, are several categories that are anticipated to end the year below the budgeted estimate, including Transfers and Reimbursements (-$2.5 million), Fees, Rates, and Charges (-$1.5 million), Other Revenue (-$1.5 million), and Fines, Forfeitures, and Penalties (-$1 million). Recommendations will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum to increase the Property Tax revenue estimate ($18 million) and the Real Property Transfer Tax revenue estimate ($10 million) to align with anticipated collection levels. The additional Property Tax

GENERAL FUND (CONT'D.)

revenue is recommended to offset actions in the memorandum and establish the 2020-2021 Ending Fund Balance Reserve that was assumed as part of the development of the 2021-2022 Proposed Operating Budget. Per City Council direction, additional Real Property Transfer Tax revenue will be expended on homeless prevention and affordable housing projects and programs. Additional information on these revenue categories as well as all other major General Fund revenue activity through April 2021 are highlighted on the following pages.

KEY GENERAL FUND REVENUES

Revenue	2020-2021 Budget Estimate	YTD Actual	Prior YTD Collections
Property Tax	**$ 361,500,000**	**$ 314,459,843**	**$ 249,361,965**

The Property Tax category consists of Secured Property Tax, Unsecured Property Tax, SB 813 Property Tax (retroactive collections back to the point of sale for reassessments of value due to property resale), Aircraft Property Tax, and Homeowner's Property Tax Relief. In 2020-2021, Property Tax receipts are estimated at $380 million, which reflects almost 3% growth from the 2019-2020 collection level of $369.5 million. Based on the most recent information provided by the State of California and the County of Santa Clara, Property Tax revenue may end the year approximately $18 million above the 2020-2021 Modified Budget estimate of $361.5 million. This growth is primarily due to higher Secured Property Tax receipts ($14 million), of which the largest component is the Educational Revenue Augmentation Fund (ERAF; $12 million), Unsecured Property Tax revenue ($2 million), and SB813 Property Tax receipts ($2 million), which are further discussed below. A recommendation to align the budget with the anticipated collection level will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum that will be reviewed by the City Council on June 22, 2021. Additional information about each of the Property Tax sub-categories is provided below.

Secured Property Taxes represent over 90% of the revenue in the Property Tax category. The Secured Property Tax category includes general Secured Property Tax, ERAF revenues, and Successor Agency to the Redevelopment Agency (SARA) Residual Property Tax.

The general Secured Property Tax budgeted estimate of $315.0 million in 2020-2021 assumes growth of approximately 5.5% from the 2019-2020 collection level. This growth primarily reflects an increase in assessed value due to the California Consumer Price Index (CCPI) increase of 2% and increased valuation due to changes in ownership or new construction. Under Proposition 13, assessed values of all real property adjust with the CCPI, with a 2% limit, unless there is a change in ownership, new construction, or a property has received a Proposition 8 adjustment. General Secured Property Tax receipts are anticipated to meet the budgeted estimate by year-end.

Beginning in 1992, agencies have been required to reallocate a portion of property tax receipts to the ERAF, which offsets the State's General Fund contributions to school districts under Proposition 98. However, once there are sufficient funds in ERAF to fulfill obligations, the

GENERAL FUND (CONT'D.)

remainder of the funding is returned to the taxing entities that contributed to it, which generally occurs in March of each fiscal year. In 2019-2020, the State of California notified counties (who oversee ERAF distribution) that changes were being considered to the calculation formula for ERAF distribution. As a result, the 2020-2021 budget was built on the assumption that 2020-2021 ERAF revenue would drop by approximately 50% from 2019-2020 actual collections, totaling $11.5 million. However, the State recently released the updated calculation instructions and 2020-2021 ERAF receipts are estimated at $23.6 million, which is consistent with 2019-2020 collections of $23.1 million. As a result, ERAF revenue is anticipated to exceed the budgeted estimate by approximately $12 million. A recommendation to align the budget with the anticipated collection level will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum that will be reviewed by the City Council on June 22, 2021.

As a result of the SARA bond refunding that occurred in December 2017, the City began receiving a residual property tax distribution in 2017-2018. The 2020-2021 Adopted Budget estimate totaled $21.0 million for SARA Property Tax revenue; however, as the result of a change in the residual property tax distribution formula due to a recent State Appellate Court decision, only $13.6 million is anticipated to be received. As part of the 2020-2021 Mid-Year Budget Review, the budget was reduced by $10.0 million (from $21.0 million to $11.0 million), which was the estimated revenue at that time. However, as revenue is now anticipated to be $13.6 million, a recommendation will be brought forward to increase the budget to align with the revised estimate as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum.

Unsecured Property Taxes are the second largest revenue source in the Property Tax category. Growth or declines in this category is driven by increases or decreases in the value of personal property (e.g. equipment and machinery used by business and industry for manufacturing and production). Based on the most recent information provided by Santa Clara County, 2020-2021 receipts of $16 million are anticipated, which is $2 million above the budgeted estimate. A recommendation to align the budget with the anticipated collection level will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021.

The **SB 813 Property Tax** category represents the retroactive taxes reassessed property valuation from the period of resale to the time that the Santa Clara County Assessor formally revalues the property. Based on the most recent information provided by Santa Clara County, 2020-2021 receipts of $8 million are anticipated, which is approximately $2 million above the budgeted estimate. A recommendation to align the budget with the anticipated collection level will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum that will be reviewed by the City Council in June 2021.

Aircraft Property Tax receipts are typically received in October of each year. Based on the most recent information provided by Santa Clara County, 2020-2021 receipts of $3.1 million are anticipated, which is consistent with the prior year collections and the budgeted estimate.

In the **Homeowners Property Tax Relief** category, revenues in 2020-2021 are expected to be at the budgeted estimate of $900,000, which is consistent with the 2019-2020 collection level.

GENERAL FUND (CONT'D.)

Revenue	2020-2021 Budget Estimate	YTD Actual	Prior YTD Collections
Sales Tax	**$ 262,500,000**	**$ 189,582,735**	**$ 178,281,553**

The Sales Tax category includes General Sales Taxes, Local Sales Taxes, and Proposition 172 Sales Taxes. In March 2020, as the COVID-19 pandemic rapidly accelerated, the County of Santa Clara instituted a shelter-in-place order, which severely restricted economic activity. The shelter-in-place and subsequent public health orders have impacted almost all sectors of Sales Tax revenue, including retail sales, transportation, and business-to-business. Information related to Sales Tax payments are distributed from the California Department of Tax and Fee Administration (CDTFA) four times throughout the year: November (representing July-September activity), February (representing October-December activity), May (representing January-March activity), and August (representing April-June activity). Based on information received through May 2021 (which reflects three quarters of Sales Tax activity; from July 2020 through March 2021), it is anticipated that 2020-2021 Sales Tax revenue will total $269.0 million, which is $6.5 million above the budgeted estimate of $262.5 million. Additionally, this collection level is approximately 3% above the 2019-2020 receipt level; however, it is important to note that 2019-2020 receipts only reflect three quarters of revenue associated with the Revenue Capture Agreement with eBay, Inc., as marketplace facilitators were not required to collect and remit sales tax until October 2020. When excluding collections associated with the Revenue Capture Agreement for both 2019-2020 and 2020-2021, collections are anticipated to drop approximately 2% from the prior year by year-end.

Additional information about each of the Sales Tax sub-categories is provided below.

General Sales Tax is the largest driver of the Sales Tax category and accounts for approximately 80% of all Sales Tax receipts. General Sales Tax receipts for the first three quarters (sales tax activity for July 2020-March 2021) were received in November 2020, February 2021, and May 2021. When excluding revenue associated with the Revenue Capture agreement with eBay, Inc. (which was not received in the first quarter of 2019-2020), receipts in 2020-2021 are consistent with the 2019-2020 collection level. However, 4th quarter receipts (April through June activity) are anticipated to experience growth of approximately 2% compared to 2019-2020 levels, which had declined significantly due to the strict shelter-in-place mandates that began in March 2020. While economic activity is increasing with the loosening of public health restrictions, it is anticipated that the 4th quarter distribution will include a large negative adjustment due to a previous quarter reporting error. Additionally, revenue collections are anticipated to be negatively affected by a recent CDTFA change in the sales tax distribution methodology for a large corporation, which will impact most cities within the State. As a result of the anticipated impacts to 4th receipts, year-over-year revenue growth is anticipated to be dampened. Based on these assumptions, General Sales Tax collections are anticipated to total $219.0 million in 2020-2021, which is $7.0 million above the budgeted estimate of $212.0 million (including the Revenue

GENERAL FUND (CONT'D.)

Capture Agreement). This collection level is fairly consistent with prior year receipts (excluding the Revenue Capture Agreement, which was only received in three quarters of 2019-2020).

Most General Sales Tax categories have experienced significant declines from the prior year, with the exception of the County Pool. The first and second quarters General Sales Tax payments reflected growth of 19.7% for the County Pool, while there was significant negative growth within the transportation, general retail, business-to-business, and food products sectors ranging from -14.4% to -31.4%. The County Pool's significant growth is attributable to the surge in online purchases during the pandemic, and facilitated by the South Dakota vs. Wayfair, Inc. Supreme Court decision in 2018, which provided states with the authority to require online retailers to collect sales tax even without a local presence in that State. The County Pool revenue is distributed to all cities within Santa Clara County based on a distribution formula administered by the CDTFA. This formula is based each quarter on each jurisdiction's total General Sales Tax receipts divided by the Total General Sales Tax receipts for the entire County. The City typically receives between 40% - 50% of the total County Pool.

In June 2016, San José voters approved a ¼ cent **Local Sales Tax**, which was implemented in October 2016. Local Sales Tax is generated based on the destination of the purchased product; therefore, all out-of-state online retailers (including marketplace facilitators) sales tax collections are directly distributed to the City of San José, versus the General Sales Tax revenue that is deposited in the County Pool, where the City only receives approximately 40% - 50% of the proceeds. Due to this distinction, Local Sales Tax revenue may not always experience the same growth and decline rates as General Sales Tax receipts.

Similar to General Sales Tax, Local Sales Tax receipts for the first three quarters (sales tax activity for July 2020-March 2021) were received in November 2020, February 2021, and May 2021. Receipts through the first three quarters reflect growth of approximately 2% from the prior year. Additionally, the 4th quarter payment (April through June activity) is anticipated to grow approximately 3.5% compared to 2019-2020 levels, which had significant declines due to the strict shelter-in-place mandates that began in March 2020. Based on these assumptions, Local Sales Tax collections are anticipated to total $44.0 million in 2020-2021, which is approximately $500,000 below the budgeted estimate, but approximately $1 million above the prior year collection level.

Proposition 172 Sales Tax collections represents the ½ cent tax that is allocated to counties and cities on an ongoing basis for funding public safety programs. The 2020-2021 budgeted estimate of $6.0 million allows for a 5.7% drop from the 2019-2020 collection level of $6.4 million. It is currently anticipated that Proposition 172 Sales Tax will end the year at budgeted levels.

GENERAL FUND (CONT'D.)

Revenue	2020-2021 Budget Estimate	YTD Actual	Prior YTD Collections
Transient Occupancy Tax	**$ 5,500,000**	**$ 3,659,666**	**$ 12,938,654**

The 2020-2021 budget estimate for the General Fund **Transient Occupancy Tax** (TOT) allocation (40% of the total tax) is $5.5 million, which was reduced from the Adopted Budget level of $9.0 million as part of the 2020-2021 Mid-Year Budget Review. This revised budget estimate represents a 39% decline from the Adopted Budget estimate, which already assumed a significant revenue decline of approximately 33% from the 2019-2020 estimated collection level of $13.5 million, attributable to the prolonged impact of the COVID-19 pandemic on the hospitality industry. Relative to actual 2019-2020 receipts, which exceeded the revised estimated level ($13.5 million) at $14.1 million, the current budget estimate represents an overall decrease of 61%.

Year-to-date revenues of $3.7 million are significantly underperforming relative to historical average performance due to the resurgence of COVID-19 during fall 2020 and winter 2020/2021 and corresponding impacts on business and leisure travel, convention activity and other public events. The adjusted TOT forecast already assumed low performance levels through the first three quarters of the fiscal year, with higher collection levels backloaded into 4th quarter of 2020-2021 based on the assumption of a slow recovery coinciding with vaccination progress and relaxation of public health restrictions for indoor gatherings. Overall, reported gross hotel revenues are performing at revised forecast expectations; however, non-remittances from hotels have resulted in lower than projected revenues to date. Of these non-remitting hotels, two have filed for bankruptcy, for which collection of past due tax remittances is uncertain.

Through April 2021, the average hotel occupancy rate reported for the San José market was 37.2%, a decrease of 25.6% over the same period in 2019-2020. Average room rates also decreased by 46.2%, from $188.32 to $101.31, and the year-to-date average revenue-per-available room (RevPAR) decreased 68.1%, from $118.24 to $37.69, relative to the same period in 2019-2020. However, hotel performance has consistently improved over the latter half of 2020-2021. Monthly revenue-per-available room, as a primary indicator of revenue trends, increased 10% from January 2021 to February 2021, 31% in March, and 6% in April. This incremental growth is expected to continue through May and June, currently at a 10% month-over-month pace.

As the number of vaccinated people continues to grow and restrictions are lifted, hotel activity is projected to moderately increase. While the pace of this rebound and success of current collection efforts remain uncertain, shifting conditions now indicate that revenues will fall short of budgeted levels due to lower than forecasted 4th quarter growth. This outlook extends to all impacted funds receiving hotel-generated taxes – General Fund, TOT Fund, and the Convention Center Facilities District Revenue Fund.

Given the considerable uncertainty in TOT activity, the Administration continues to closely collaborate with external consultants to monitor key performance indicators for hotel activity, and to revisit revenue assumptions. It is currently anticipated TOT receipts may total $5 million by year-end, which is approximately $500,000 below the budgeted estimate of $5.5 million.

GENERAL FUND (CONT'D.)

Revenue	2020-2021 Budget Estimate	YTD Actual	Prior YTD Collections
Utility Tax	**$ 95,800,000**	**$ 78,892,255**	**$ 76,724,421**

The Utility Tax category includes the Electricity Utility Tax, Gas Utility Tax, Water Utility Tax, and the Telephone Utility Tax. Through April, Utility Tax receipts of $78.9 million are approximately 3% above the prior year level. The 2020-2021 Adopted Budget was built on the assumption that 2019-2020 Utility Tax revenue would end the year at $96.1 million and then stay relatively flat at $95.8 million in 2020-2021. However, since 2019-2020 ended the year at $99.5 million, receipts can drop by 3.7% in 2020-2021 to meet the budgeted estimate. Based on historical collection trends and performance through April, it is anticipated overall Utility Taxes may exceed the budgeted level by approximately $3 - $4 million by year-end.

In the **Electricity Utility Tax** category, collections through April totaled $40.1 million, which is $1.6 million above the prior year receipts. The 2020-2021 Adopted Budget assumed that 2019-2020 receipts would total $46.5 million, and remain relatively flat at $46.6 million in 2020-2021. However, since 2019-2020 ended the year above estimated levels ($48.7 million), receipts can decline by 4.3% in 2020-2021 and meet the budgeted estimate. Based on historical collection trends and performance through April, collections are anticipated to end the year approximately $3 million above the budgeted estimate.

In the **Gas Utility Tax** category, receipts through April totaled $10.0 million, approximately $900,000 above the prior year collection level. The 2020-2021 Adopted Budget estimate of $11.3 million is fairly consistent with the 2019-2020 actual collection level of $11.23 million. Based on historical collection trends and performance through April, receipts are anticipated to end the year approximately $500,000 - $1 million above the budgeted estimate.

Water Utility Tax collections of $13.1 million through April are approximately $1.0 million above the prior year. The 2020-2021 Adopted Budget was built on the assumption that 2019-2020 collections would total $16.5 million and remain flat in 2020-2021. However, since 2019-2020 receipts totaled $16.9 million, receipts in 2020-2021 can decline by 2.4% and meet the budgeted estimate. Based on historical collection trends and performance through April, receipts are anticipated to end the year approximately $500,000 - $1 million above the budgeted estimate.

Collections in the **Telephone Utility Tax** category through April totaled $15.7 million, compared to prior year receipts of $17.0 million. The 2020-2021 Adopted Budget estimate of $21.4 million allows for a 5.7% drop from the 2019-2020 actual collection level of $22.7 million. The anticipated decline in this revenue category is the result of wireless consumers shifting to less expensive prepaid wireless plans, competition with cellular companies that keep prices down, and the shifting of wireless communications to increase reliance on data plans, which are not taxable. Based on current collection trends, receipts in this category are anticipated to end the year approximately $1 million below the budgeted estimate.

GENERAL FUND (CONT'D.)

Revenue	2020-2021 Budget Estimate	YTD Actual	Prior YTD Collections
Business Taxes	**$ 63,900,000**	**$ 53,764,930**	**$ 61,752,144**

The Business Taxes category consists of the Cannabis Business Tax, Cardroom Tax, Disposal Facility Tax, and General Business Tax. Through April, overall collections of $53.8 million are 12.9% below the prior year collection levels of $61.8 million, primarily reflecting lower collections in the Cardroom Tax and General Business Tax categories. The Business Taxes 2020-2021 Modified Budget estimate of $63.9 million allows for a 10% decline from the 2019-2020 actual collection level. Based on current collection trends, and an uptick in revenue over the spring months as health restrictions continue to ease, Business Taxes are now anticipated to end the year approximately $3 million above budgeted levels, which is primarily due to higher Cannabis Business Tax and Cardroom Business Tax receipts.

Cannabis Business Tax collections reflect cannabis business tax as well as cannabis business tax compliance revenues. Through April, receipts of $13.5 million are 18.7% above the prior year level of $11.4 million, which is primarily due to higher activity levels. In November 2016, the California Marijuana Legalization Initiative (Proposition 64) legalized recreational marijuana use in the State of California. As a result, the sale of recreational cannabis at the 16 licenses dispensaries in San José began in January 2018. The 2020-2021 Adopted Budget estimate of $17.0 million requires growth of 6.8% from 2019-2020 actual collection levels. Based on collections through April, it is anticipated that revenues will end the year approximately $1 million above the budgeted estimate.

Through April, **Cardroom Tax** receipts of $5.3 million have been received, which is significantly below the prior year level of $13.5 million. As a result of the shelter-in-place mandate, cardrooms suspended operations in March 2020 and remained closed through August 2020. In September, public health orders were modified to allow cardrooms to begin outdoor operations with social distancing requirements. However, cardrooms were only open for a limited period of time, before further health orders by Santa Clara County and then subsequently the State of California resulted in the closure of cardrooms from November 30, 2020 through January 27, 2021. Cardrooms are once again operational, under modified restrictions. Due to the continued easing of health restrictions and the increased taxes on cardroom operators that began in January 2021, it is now estimated that Cardroom Tax revenue will end the year approximately $1 - $2 million above the budgeted estimate.

Disposal Facility Tax (DFT) are business taxes received based on the tons of solid waste disposed at landfills within the City. DFT revenue through April totaled $10.5 million, which is 8.1% above the prior year level of $9.7 million. The 2020-2021 budget was built on the assumption that the pandemic would impact revenue collections in 2019-2020 with receipts to end the year at $12.3 million, with a further drop of in 2020-2021 of approximately 10% to $11.1 million. However, collections in 2019-2020 ended the year at $12.52 million and through the first few months of the

GENERAL FUND (CONT'D.)

fiscal year receipts were remaining stable compared to the prior year. Therefore, the 2019-2020 Annual Report, which was approved by the City Council on October 20, 2020, included an action to increase the DFT revenue by $1.5 million (from $11.1 million to $12.6 million), to align the 2020-2021 budget with estimated collection levels. Based on collections through April, it is anticipated revenue will end the year at the budgeted level.

Through April, **General Business Tax** receipts of $24.5 million are almost 10% below the prior year collection levels. The 2020-2021 Adopted Budget assumed that 2019-2020 receipts would total $28.0 million, and drop by approximately 8% to $25.7 million in 2020-2021. This decrease reflected a net increase of the 2% CPI adjustment that will be assessed in 2020-2021, offset by a 10% reduction to General Business Tax proceeds as a result of the pandemic's impact on local businesses. It is currently anticipated General Business Tax receipts will slightly exceed the budgeted estimate by year-end.

Revenue	2020-2021 Budget Estimate	YTD Actual	Prior YTD Collections
Real Property Transfer Tax	**$ 40,000,000**	**$ 32,692,006**	**N/A**

On March 3, 2020, San José voters approved Measure E, the Real Property Transfer Tax. This new tax, which became effective on July 1, 2020, is imposed at a tiered level for property transfers (sales) over $2.0 million. The 2020-2021 budgeted estimate totals $40.0 million for the Real Property Transfer Tax, however, based on year-to-date receipts, it is estimated receipts will total $50.0 million by year-end. These receipts will be expended on homeless prevention and affordable housing projects and programs, per City Council direction. A recommendation to align the budget with the anticipated collection level (and associated expenditure adjustments) will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum that will be reviewed by the City Council on June 22, 2021.

EXPENDITURES

Through April, General Fund expenditures (without encumbrances) of $1.12 billion were 15.3% above the prior year level of $972.2 million. However, after excluding TRANS debt service payments of $105.5 million (which was not used in 2019-2020) and factoring out costs related to the Development Fee Program that were expended through April 2020, but are not reflected in the General Fund in 2020-2021 as the Development Fee Program has been moved to individual special funds ($46.2 million), expenditures are approximately 10% above prior year levels. The 2020-2021 General Fund Budget assumes growth of 6% in expenditures from the prior year. Encumbrances of $83.6 million were 23.6% above the prior year level. General Fund expenditures and encumbrances through April of $1.2 billion constitute 68.4% of the total budget including reserves, and 76.2% of the budget excluding reserves. Overall, General Fund expenditures are anticipated to end the year at or below budgeted levels.

GENERAL FUND (CONT'D.)

Through April, departments are overall performing within estimated levels for personal services expenditures, with several exceptions, the largest of which includes the Police Department and Fire Department. Recommendations to increase budget allocations for these Departments as well as make adjustments to the Office of Economic Development, Human Resources Department, City Clerk's Office, and the City Attorney's Office will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum that will be reviewed by the City Council on June 22, 2021. While the causes of the overages in the Police and Fire Departments are discussed below, the overages for the other departments listed above are generally attributable to a combination of costs related to pandemic response that could not be reimbursed or allocated to the Coronavirus Relief Fund, lower than assumed vacancy rates and vacation payouts, and higher levels of actual payroll costs than assumed in the budget. Overall, expenditures will continue to be controlled and monitored – including the continuation of the hiring freeze and exemption review process established back in March 2020 – to ensure appropriations stay within approved levels to the extent possible, and generate vacancy savings to provide a cushion against future budgetary uncertainty. Following is a discussion of the performance of the Police and Fire Departments, the largest General Fund departments.

KEY GENERAL FUND EXPENDITURES

Department	2020-2021 Budget	YTD Actual	Prior YTD Actual
Police	**$ 458,182,548**	**$ 371,796,653**	**$ 358,073,350**

Police Department expenditures are tracking above estimated levels through April and are expected to exceed current budgeted levels. This overage is primarily due to Personal Services expenditures of $341.7 million (80.90% expended, compared to the par level of 79.75%) which are exceeding budgeted levels due to a lower than projected number of sworn vacancies that were used to determine the number of recruit positions that were hired as part of the Sworn Hire Ahead Program. This has led to higher regular salary, benefit, and retirement expenses in comparison to prior year levels (2.3%). In addition, the Department has experienced elevated sworn overtime usage and payouts. Year-to-date overtime expenditures of $35.7 million account for 130.9% of the Police Department's $27.3 million overtime budget, reflecting continued elevated levels of usage primarily used to backfill for vacant sworn street-ready positions. It is important to note, however, that overtime expenditures are tracking 3.3% below 2019-2020 levels, indicating incremental year-over-year progress with efforts to moderate the use of overtime. A portion of the higher Personal Services expenditures is also attributable to increased retirement contribution rates in the payroll system totaling $4.1 million that account for actuarial-assumed wage increases, which are not yet in the department's budget allocation, but have been instead budgeted in the Salaries and Benefits Reserve pending finalization of the new Memorandum of Agreement (MOA) with the Police Officers Association. The new MOA, effective July 1, 2021 through June 30, 2022, was approved by City Council on May 11, 2021 and provides for a 3.85% pensionable

GENERAL FUND (CONT'D.)

general wage increase as well as a one-time non-pensionable lump-sum payment of $2,000, effective May 16, 2021. The total estimated cost of these provisions is approximately $3.5 million for the remainder of the fiscal year, in addition to previously planned adjustments from the Salary and Benefits Reserve for retirement costs of $4.1 million.

After accounting for the budget adjustments necessary to account for MOA changes and related retirement costs, overall, Personal Services expenditures are on pace to exceed budgeted levels by approximately $4.4 million, or 1% of the Police Department's Personal Services Budget. This overage factors in the Police Department's cost containment measures related to overtime use as discussed below. Budget adjustments will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum to account for final estimated personal services costs.

A total of $30.1 million (84.03%) of the Department's Non-Personal/Equipment budget (including encumbrances) has been expended or encumbered through April. Excluding the remaining balances for centrally-determined details ($2.79 million), including electricity, gas, and vehicle operation and replacement, the Police Department has approximately $2.9 million, or 8.2%, of its total Non-Personal/Equipment appropriations available for the remainder of the fiscal year. Although Non-Personal/Equipment expenditures are tracking higher at this point of the fiscal year due to encumbrances of $5.8 million (19.3% of year-to-date activity), overall expenditures are expected to remain within budgeted levels as part of this encumbrance balance is expended for planned activities.

Overtime consists of overtime expenditures and compensatory time. The Memorandum of Agreement (MOA) with the Police Officer's Association (POA) limits how much overtime can be earned for pay versus compensatory time. The Police Department continues to diligently work to fill vacancies in both sworn and civilian positions, using vacancy savings and the $6.75 million in one-time funding from the Sworn Hire Ahead Program to pay for Police Academy Recruits. While the goal is to fill vacancies and eliminate the need for overtime to backfill positions, academy and field training of new recruits takes 10-12 months, necessitating overtime to backfill until the new recruits are ready to serve as solo beat officers. Vacancy levels have also contributed to the build-up of compensatory time balances for sworn personnel, for which there is a limit of 480 hours after which sworn personnel are paid in overtime for any additional hours worked.

As recommended in the City Auditor's March 2021 *Police Staffing, Expenditures, and Workload* audit report, the Bi-Monthly Financial Reports, Mid-Year Budget Reviews, and Annual Reports include: 1) the number of individuals who have reached the 480-hour limit (previously reported) and the 240-hour limit (newly reported; per the San José Police Officers' Association Memorandum of Agreement, a sworn employee who reaches 240 hours of compensatory time is responsible for bringing the balance below 240 hours prior to the end of the calendar year), 2) the total compensatory time liability (total hours were previously reported, total cost liability is newly reported), and 3) the amount of overtime expenses attributable to staff that have reached the 480-hour accrual limit (newly reported).

GENERAL FUND (CONT'D.)

As of April 2021, out of 1,013 street-ready sworn officers, 459 sworn personnel had reached the 480-hour limit, an increase of 24.7% compared to 368 sworn personnel as of April 2020. A total of 242 sworn personnel were between 240 hours and 480 hours, compared to the 273 sworn personnel as of April 2020.

The compensatory time balance at the end of April 2021 was 350,508 hours for sworn personnel ($24.7 million). This represents an increase of 29,380 hours or 9.1% compared to the April 2020 balance of 321,128 ($22.8 million). As described above, 459 sworn personnel have reached the compensatory balance limit of 480 hours and all overtime worked by these employees is paid as overtime.

Year-to-date overtime expenses attributable to staff that have reached the 480-hour compensatory accrual limit through April 2021 was $17.3 million (233,207 hours), compared to $12.7 million in April 2020 (169,183 hours), a 36% increase in expense. This increase is driven by backfilling recruits, unplanned overtime in response to protests, response to wildfires in the summer of 2020, preparations for demonstrations surrounding the contentious presidential election, increased investigations, and side show enforcement.

The Police Department is enforcing compensatory time controls by requiring all sworn staff, outside of the Bureau of Field Operations (BFO), to reduce compensatory time balances by the end of the calendar year, or to submit a request for an extension, per the POA MOA. The Police Department has implemented additional overtime and compensatory time approvals to slow, and eventually reduce, compensatory time balance growth, including revisions for BFO approvals to the extent possible.

As an example, the Chief of Police issued a department-wide memorandum in May placing additional controls on the use of overtime and compensatory time that include, but are not limited to: clarifying the definition of mandatory overtime as limited to work that must be completed immediately and cannot be done on an employee's regular shift or their next work shift; prohibiting the use of discretionary overtime unless approved by a Captain/Division Manager or higher rank; requiring that report-writing and follow-up overtime be approved by a Lieutenant or above and only when the action cannot be completed on duty or on the employee's next shift; and requiring Captains/Division Managers to submit a quarterly memorandum to the Department's Executive Officer justifying the use of overtime in their divisions.

Finally, an internal working group will be established – comprised of varying ranks of sworn personnel, fiscal personnel, and other civilian staff – tasked with identifying approaches to further increase the controls surrounding compensatory time liability. These actions, as well as the other recommendations included in the *Police Staffing, Expenditures, and Workload* audit report are intended to address, slow, and reverse the growth of overtime and compensatory time use.

GENERAL FUND (CONT'D.)

The table below provides a summary of sworn staffing vacancies and street-ready officers. While the sworn positions are almost completely filled, there is still a significant gap between filled positions and street-ready officers, with the Sworn Hire Ahead program squarely aimed at closing this gap and mitigating expected vacancies due to retirements and other separations. Of the 1,159 authorized sworn staff, 126 were in training (10.9%) as of April 2021, leaving 1,013 street ready sworn positions available (this includes sworn employees on disability/modified duty/other leaves) when also accounting for vacancies as shown in the chart below. Excluding sworn employees on disability/modified duty/other leaves, 952 sworn officers were actively deployed as of May 7, 2021.

	2019-2020 (as of 05/08/2020)	2020-2021 (as of 05/07/2021)
Authorized Sworn Positions	**1,151**	**1,159**
Vacancies	(10)	(20)
Filled Sworn Positions	**1,141**	**1,139**
Field Training Officer/Recruits	(135)	(126)
Street-Ready Sworn Officers Available	**1,006**	**1,013**
Disability/Modified Duty/Other Leaves	(70)	(61)
Street-Ready Sworn Officers Working	**936**	**952**

The Police Department completed or began several academies over the past year, including February/June 2020 (55 recruits), October 2020 (51 recruits) and February 2021 (42 recruits). Due to the pandemic, the February 2020 Academy was suspended in March 2020 and resumed in late June. This academy graduated in February 2021 and the October 2020 academy graduated in May 2021; the February 2021 academy is anticipated to graduate in September 2021 (42 recruits). To fill the vacant sworn positions and put more Police Officers back on patrol, the Department will continue with an additional Police Recruit Academy in 2020-2021, with the next beginning in June 2021 with an estimated 36 recruits.

GENERAL FUND (CONT'D.)

Department	2020-2021 Budget	YTD Actual	Prior YTD Actual
Fire	**$ 236,288,697**	**$ 190,430,439**	**$ 192,264,292**

The Fire Department's budget totals $236.3 million, which is comprised of $225.9 million in Personal Services and $10.4 million in Non-Personal/Equipment expenditures. Overall, Fire Department expenditures are performing slightly above estimated levels through April. Personal Services expenditures of $182.7 million, or 80.9% of the Modified Budget, are slightly above the expected level of 79.75% at this point of the year. The higher than estimated expenditures are due an active fire season in the summer and fall of 2020, the costs incurred from mutual aid, Strike Team, and Task Force 3 deployments, which will be reimbursed by the State of California and Federal Emergency Management Agency (approximately $3.7 million), and overtime to backfill sworn absences on the line due to the pandemic (approximately $1.1 million). The Fire Department's Non-Personal/Equipment budget of $10.4 million was 73.89% expended or encumbered through April 2021. Pending a final reconciliation, actions will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum that will be reviewed by the City Council on June 22, 2021, to recognize revenue from the State of California for mutual aid and Strike Team deployments State reimbursement and allocate it to the Fire Department's Personal Services and Non-Personal/Equipment budgets, as well as increase the Personal Services budget to account for sworn pandemic-caused absences.

Overall, the average sworn vacancy rate of 3.25% through April 2021 is slightly higher than the vacancy rate of 2.68% experienced this time last year, and above the budgeted rate of 2.5%. The current fire fighter academy for 2020-2021 began in April 2021 and will conclude in September 2021 with potentially 23 graduates.

In accordance with the City Council's approval of a March 2010 report on annual vacancy and absence rates, the Fire Department has committed to limiting administrative assignments for sworn administrative personnel for overtime control purposes. As of the end of April, of the 31 current authorized staffing level, the Fire Department had 31 sworn personnel on administrative assignments.

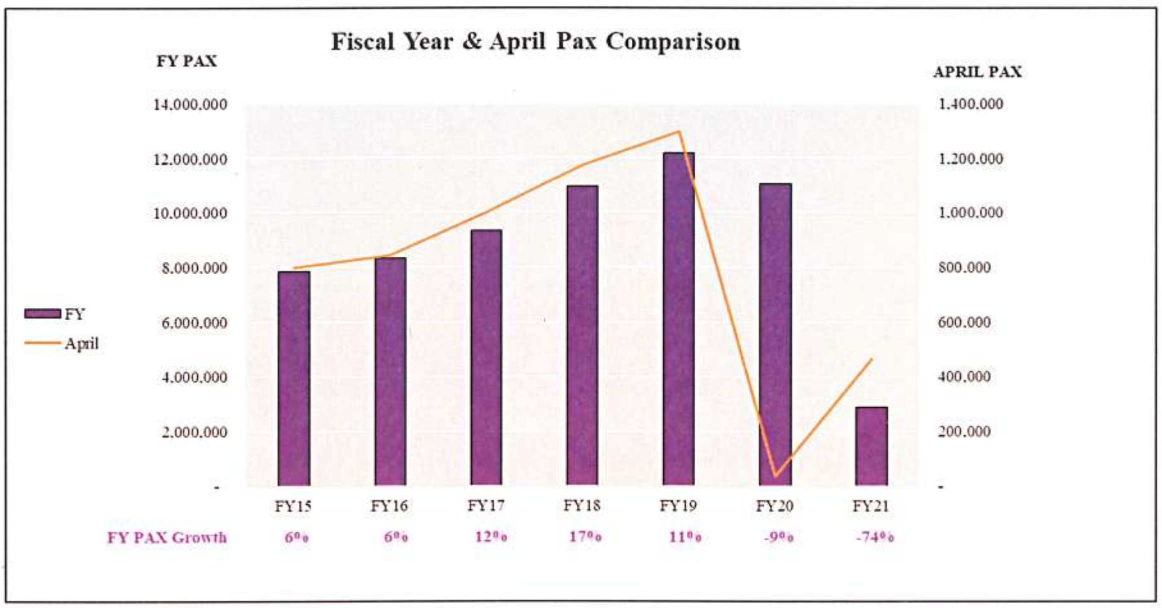
CONTINGENCY RESERVE

The General Fund Contingency Reserve remained at $40.0 million through April, with no revisions through the February. This reserve level complies with Council Policy 1-18, Operating Budget and Capital Improvement Program Policy, that requires the Contingency Reserve to be at a minimum of 3% of the operating budget.

OTHER FUNDS

Airport Funds

On a fiscal year-to-date basis, the Norman Y. Mineta San José International Airport (SJC) has enplaned and deplaned 2.9 million passengers, a decrease of 73.9% from the figures reported through April of the prior year. The month of April 2020 was a historic low number of passengers as it was the first full month of shelter in place orders. The chart below depicts the year-over-year change for the month of April and fiscal year-to-date for the last six years. Fiscal year-to-date mail, freight and cargo totaled 69.2 million pounds, which represents a 17.6% decrease over year-to-date April of 2020. All revenue-generating activities posted decreases over the same period of 2019-2020: Traffic Operations (landings and takeoffs) by 42.9%, Landed Weights by 57.8%, Ground Transportation by 84.2%, Gallons of Aviation Fuel sold by 63.9% and lastly Parking Exits decreased by 63.1%.



The County of Santa Clara moved to the Orange Tier on March 24, 2021 with changes to the travel policy and subsequently moved to the least restrictive Yellow Tier effective May 18, 2021. The month-to-date increase in passengers from April 2020 to April 2021 is 1,139.6% or 428,000; through April, passenger levels are 92% of the pro-rated 4.0 million estimated for 2020-2021.

Through April, overall revenue performance at the Airport tracked just 2.3% below the budgeted estimate, which was bolstered by CARES and Coronavirus Response and Relief Supplemental Appropriations (CRRSA) Act funding of $53.5 million received to-date – out of a total allocation of $65.6 million authorized – based on reimbursement of expenditure requests submitted to the FAA. Activity through April fell below the budgeted estimates for the following categories: Airfield revenues (-26.9%), Terminal Concessions (-28.8%), Parking & Roadway (-34.9%), and Airline Rates & Charges categories of Landing Fees (-13.9%) and

OTHER FUNDS (CONT'D.)

Terminal Rentals (-6.3%). General and Non-Aviation revenues tracked slightly above the benchmark at +3.8%. Airport revenue performance will continue to be closely managed and monitored through this fiscal year.

Through April, both the Airport Customer Facility and Transportation Fee Fund and Airport Maintenance and Operation Fund expenditures tracked below budgeted levels. In the Maintenance and Operation Fund, Personal Service expenditures were 79.9% of budget compared to the benchmark of 80.8%, while Non-personal/Equipment expenditures were 40.5% compared to the benchmark of 74.5%. Non-personal/Equipment expenditures in the Customer Facility and Transportation Fee Fund were 44.6% compared to the straight-line benchmark of 83.3%. The Administration will continue to closely monitor and report activity, revenue and expenditure status.

Construction and Conveyance Tax Funds

Through April 2021, Construction and Conveyance (C&C) Tax receipts totaled $34.0 million, which represents 85.0% of the 2020-2021 Modified Budget estimate ($40.0 million) and are expected to exceed budgeted levels. Year-to-date collections are 8.2% above receipts through April 2020, which totaled $31.4 million. In addition, the City has received the May Conveyance receipts from Santa Clara County, which total $6.3 million and represent a significant increase from the May 2020 collection level of $2.7 million. When taking into account receipts through April and the abnormally high May collections, C&C receipts in 2020-2021 total $40.3 million; it is anticipated that overall C&C receipts will exceed the budgeted estimate of $40 million by approximately $5 million - $10 million. A reconciliation of the C&C Tax revenue and the corresponding adjustments to C&C Capital Funds will be done as part of the 2020-2021 Annual Report, which will be released on September 30, 2021.

The 2020-2021 Adopted Capital Budget was built on the assumption that C&C Tax receipts would drop significantly in 2020-2021 due to the COVID-19 pandemic and uncertainty regarding its long-term effect on the local real estate market, which is the primary driver of this revenue source. In accordance with this expectation, C&C Tax receipts in 2020-2021 were initially budgeted at $30.0 million, which allows for a 27% drop from 2019-2020 actual collection level of $40.9 million. While collections were suppressed when the shelter-in-place began, receipts have since experienced year-over-year growth. Therefore, as part of the 2020-2021 Mid-Year Budget Review, the C&C budgeted estimate was increased by $10.0 million, from $30.0 million to $40.0 million. Based on the extremely high collections experienced in April and May 2021, C&C receipts are anticipated to exceed the Modified Budget level.

Over 99% of the total Construction and Conveyance Taxes are comprised of conveyance receipts, a tax based on the value of property transfers (sales). As discussed in the Economic Environment section of this Bi-Monthly Financial Report, the local real estate market has been experiencing strong growth compared to prior year levels. Since housing statistics are a key driver for the overall C&C collection levels, significant changes in the housing market will drastically affect the C&C Tax receipts.

OTHER FUNDS (CONT'D.)

Other Construction-Related Revenues

Capital revenues associated with construction activity are currently anticipated to fall below their budgeted estimates by year-end. As discussed below, the Construction Excise Tax and Building and Structure Construction Tax receipts through April are lower than prior year levels and recommendations to decrease the budgeted estimates will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum, which will be reviewed at the June 22, 2021 City Council meeting. Construction activities drive revenue collection in several categories, including the Construction Excise Tax and the Building and Structure Construction Tax that help fund the City's Traffic Capital Program, and are an indicator of future activity for several other categories, such as storm and sanitary sewer system fees.

Through April, the **Building and Structure Construction Tax** collection level of \$20.6 million is 30.0% below the prior year receipts of \$29.4 million and the **Construction Excise Tax** collection level of \$15.5 million is 15.0% below the prior year receipts of \$18.2 million. Through January, Building and Structure and Construction Excise Tax revenues were outpacing expectations, therefore the 2020-2021 Mid-Year Budget Review included an adjustment to increase the Building and Structure Construction Tax revenue estimate by \$6.0 million (from \$19.0 million to \$25.0 million), and Construction Excise Tax revenue estimate by \$7.0 million (from \$14.0 million to \$21.0 million). However, the pace of activity slowed considerably starting in February 2021. Due to this significant slowdown in activity, revenue collections are now anticipated to fall below the Modified Budget Estimate, therefore, recommendations will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum to decrease the Building and Construction Tax revenue estimate by \$3.0 million (from \$25.0 million to \$22.0 million) and the Construction Excise Tax revenue by \$4.0 million (from \$21.0 million to \$17.0 million).

Development Fee Program Funds

Development Fee Programs were previously captured in the General Fund; however, beginning in 2020-2021 all revenue and expenditures related to the Development Fee Programs have been allocated to specific Development Fee Program Funds. Development Fee Programs include the Building Development Fee Program, Citywide Planning Fee Program, Fire Development Fee Program, Planning Development Fee Program, Public Works Development Fee Program Fund, and the Small Cell Permitting Fee Program Fund. Currently, all Development Fee Programs are anticipated to meet or exceed budgeted estimates by year-end. Budget adjustments are included in the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum to increase the Building Development Fee Program, Planning Development Fee Program, Small Cell Permitting Fee Program, and Citywide Planning Fee Program to align the budgeted estimates with anticipated collections. Additional information about each of the Development Fee Program Funds is provided on the following pages.

OTHER FUNDS (CONT'D.)

The **Building Development Fee Program** issues building permits and oversees construction on private property. Building Permit revenues of $27.1 million through April are 15.1% lower than the 2019-2020 collection level for the same period. The 2020-2021 Adopted Budget estimate of $24.6 million allows for a 32.1% drop from the 2019-2020 actual collection level of $36.2 million due to the ongoing pandemic. Based on current collection trends, Building Fee revenues are anticipated to exceed the 2020-2021 budget revenue estimate of $24.6 million by at least $7.0 million.

The **Citywide Planning Fee Program** provides funding for the City's long-range planning projects, such as developing and updating the City's General Plan, to match the City's planning goals. The Citywide Planning Fee is an 11.97% fee applied to Entitlement, Building Permit Fees, and Building Plan Check Fee Categories. Through April, Citywide Planning Fee revenues of $2.7 million are 15.7% below the prior year collection level of $3.2 million. The 2020-2021 Adopted Budget estimate of $2.4 million allows for a 32.9% drop from the 2019-2020 actual collection level of $3.6 million due to the ongoing COVID-19 pandemic. Citywide Planning Fee revenues currently exceed the 2020-2021 budget revenue estimate of $2.4 million and if current collection trends continue, they will exceed the estimate by $750,000.

The **Fire Development Fee Program** provides operational and construction permits and inspections to ensure that development within San José meets the City's fire codes. Development-related receipts through April of $5.6 million are $2.1 million (31.5%) lower than prior year collections. The 2020-2021 Adopted Budget estimate of $6.2 million allows for 31.1% decrease from the 2019-2020 actual collection level of $9.0 million due to an anticipated decrease in fee activity as a result of the pandemic. Based on activity through April, Fire Development revenues are projected to meet or slightly exceed budgeted revenue estimate.

The **Planning Development Fee Program** processes land development applications for planning permits and services, such as zoning review, to match the City's planning goals. Through April, Planning Fee revenues of $6.5 million are 9.4% above the prior year collection level of $5.9 million. The 2020-2021 Modified Budget estimate of $6.4 million allows for a 6.5% drop from the 2019-2020 actual collection level of $6.8 million due to impacts associated with the COVID-19 pandemic. Planning Fee revenues currently exceed the 2020-2021 budget revenue estimate of $6.4 million and if the current collection trends continue, it will exceed the estimate by $700,000.

The **Public Works Development Fee Program** ensures that developments comply with regulations and provide appropriate public infrastructure, such as sidewalks, traffic signals, and streetlights. Revenues through April of $9.5 million are 2.2% above the prior year level of $9.3 million. The Public Works Development Fee Program total revenue collections are comprised of $5.4 million from the Development Services Fee Program and $4.0 million from the Utility Fee Program. The 2020-2021 Adopted Budget estimate of $10.9 million allows for a 9% decrease from the 2019-202 actual collection level of $11.9 million due to an anticipated in fee activity as a result of the pandemic. Based on activity through April, collections in Public Works revenues are projected to exceed budgeted levels by approximately $500,000 - $1.0 million.

OTHER FUNDS (CONT'D.)

The **Small Cell Permitting Fee Program** consists of review and approval of the installation of small cell and fiber optic telecommunication facilities on property owned by the city, including without limitation to, streetlights, traffic lights and rooftops. Revenues in this fund are generated primarily through fees, rates, and charges paid to the city by telecommunication companies in connection with the Department of Public Works' review and approval process. Through April, small cell permitting fee revenue collection totaled $6.3 million, whereas $2.3 million had been received through April 2020. The increased fee revenue is a direct result of increased permit submissions as telecommunication companies continue the expansion of fifth generation (5G) cellular networks throughout the City. The 2020-2021 Modified Budget estimate of $4.0 million allows for a 14.9% decrease from the 2019-2020 actual collection level of $4.7 million due to an anticipated decrease in fee activity as a result of the pandemic. Based on current collection trends, revenues are anticipated to exceed budgeted levels by approximately $2.5 million - $3 million.

San José Clean Energy Fund

The Community Energy Department operates San José Clean Energy (SJCE), suppling residents and businesses with cost competitive electricity with higher renewable content than PG&E. In November 2020, City Council approved SJCE's 2021 generation rates at 0.25% below PG&E's rates, inclusive of the Power Charge Indifference Adjustment (PCIA) and Franchise Fee Surcharge for all customers. The PCIA is a fee assessed by investor-owned utilities on all electric customers to cover above-market generation costs attributable to generation acquired prior to a customer's change in service provider. PG&E's PCIA has risen over 900% between 2013 and 2021, and 41% alone between 2020 and 2021. In 2021, SJCE customers will pay an extra $51.0 million in PCIA fees to PG&E for a total of $176 million in PG&E PCIA fees. Because the rate paid by customers to SJCE needed to be no greater than 0.25% below PG&E's rates, and because the rate paid by SJCE customers is inclusive of PCIA fees, which previously needed to be no greater than 0.25% below PG&E's rates, rising PCIA fees negatively affect SJCE's revenue and hamper the ability to maintain and build financial reserves.

As a result of the increasing PCIA fees, the Community Energy Department recommended a rate increase and new service offerings that were approved by City Council in May 2021 to mitigate the financial impacts to customers and to the SJCE program. This action included a rate increase of 8% above PG&E generation rates for SJCE's default product, GreenSource, and the addition of a new low-cost product called GreenValue, with rates set at parity with PG&E.

The following recent market events have impacted SJCE's financial operations and reduced cash levels for the enterprise:

- Delayed PG&E rate increase. Because SJCE rates are linked to PG&E rates, the delay in PG&E rate increases from March to September, and now a potential delay to December 2021 has an adverse impact on SJCE revenues and cash flow.

OTHER FUNDS (CONT'D.)

- Customer bad debt expense. The COVID-19 situation and constraints placed on utility shut-offs have increased bad debt expense three to five times, compared with pre-March 2020 levels. As with most industries, electric utilities have faced negative financial impacts due to the COVID-19 pandemic. SJCE customers' missed payments currently total approximately $9.6 million that are 90 days past due and continue to grow.

- High market prices: The energy market has experienced several disruptions which has increased forward prices. These are the main disruptions impacting the market:

  - The heat wave in August 2020 which impacted much of the Western U.S and led to rolling blackouts in California due to insufficient supply.
  - The extreme winter storm in Texas in 2021.
  - The Diablo Canyon and Palo Verde nuclear plants experienced operational issues this spring.
  - The drought has limited the supply of hydro-electric generation.

- Increased collateral requirements: Due to these recent events and increased market prices, some suppliers and the California Independent System Operator (CAISO) have increased SJCE's requirements for collateral and in some cases requested cash instead of a letter of credit.

The Community Energy Department, Finance Department, and the City Manager's Budget Office have been evaluating current financial conditions. A more in-depth discussion regarding the challenges SJCE faces, and a recommendation to draw upon the City's commercial paper program to address near-term financial issues, will take place at the City Council meeting on June 22, 2021.

Other Funds

Overall, the remaining Special and Capital funds are tracking within anticipated levels and are expected to end the year at revised budgeted levels. Due to continued impacts related to the pandemic, budgetary adjustments were brought forward as part of the 2020-2021 Mid-Year Budget Review to rebalance several funds, including the **Transient Occupancy Tax Fund**, the **Convention and Cultural Affairs Fund**, the **Convention Center Facility District Revenue Fund**, and the **General Purpose Parking Fund**. After accounting for the downward revenue adjustments approved by the City Council with the 2020-2021 Mid-Year Budget Review, it is anticipated that the funds will end the year close to budgeted levels. Depending on activity levels for the final few months of the fiscal year, the Transient Occupancy Tax Fund, Convention and Cultural Affairs Fund, and Convention Center Facility District Revenue Fund may fall slightly below the revised estimates. A full reconciliation of these funds will be done as part of the 2020-2021 Annual Report, which will be released on September 30, 2021.

CONCLUSION

As a result of the pandemic and the necessary response to protect community health and safety, economic activity was severely restricted beginning in March 2020. As anticipated, revenue sources across the City were significantly impacted. The 2020-2021 Adopted Budget was developed assuming that many of the General Fund and other economically sensitive City fund revenues would continue to be suppressed as public health orders and social distancing protocols are anticipated through much of the fiscal year. However, while some revenue categories are tracking to end the year below budgeted levels, several revenues are not being impacted as significantly as initially anticipated and are anticipated to end the year above budget.

Based on the available data through April, overall General Fund revenues are anticipated to end the year approximately $30 million above the budgeted level, which is due to positive variances in several revenue categories, primarily Property Tax, Real Property Transfer Tax, Sales Tax, Business Taxes, and Utility Taxes. However, partially offsetting these increased revenues are several categories that are anticipated to end the year below the budgeted estimate, including Transfers and Reimbursements, Fees, Rates, and Charges, Other Revenue and Fines, Forfeitures, and Penalties. Recommendations will be brought forward as part of the Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum to increase the Property Tax revenue estimate ($18 million) and the Real Property Transfer Tax revenue estimate ($10 million) to align estimates with anticipated collection levels. Per City Council direction, additional Real Property Transfer Tax revenue will be expended on homeless prevention and affordable housing projects and programs. The additional Property Tax revenue will be used to offset other recommended actions in the memorandum and to establish the 2020-2021 Ending Fund Balance Reserve as assumed in the development of the 2021-2022 Proposed Operating Budget.

Most other City funds are performing within expected levels, with some exceptions. Though Airport passenger activity is significantly down from prior year levels, revenues and expenditures are tracking within anticipated levels. As a result of continued Transient Occupancy Tax revenue and convention and cultural event-related activity declines, the Transient Occupancy Tax Fund, the Convention and Cultural Affairs Fund, and the Convention Center Facility District Revenue Fund remain heavily impacted. As a result, the 2020-2021 Mid-Year Budget Review rebalanced these funds to address the reduced revenues. However, revenue collections in these funds may still fall slightly below the revised estimates and will need to continue to be monitored closely. Additionally, as other economically sensitive City funds, such as the Building and Structure Construction Tax Fund and Construction Excise Tax Fund have experienced significant drops in activity levels and are anticipated to end the year below budgeted levels. The Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum includes recommendations to decrease the tax estimates to align revenues with estimated collection levels.

CONCLUSION (CONT'D.)

The Approval of Various Budget Actions for Fiscal Year 2020-2021 memorandum also includes recommendations to adjust both the General Fund and various Special and Capital Funds to align the budget with current estimates to avoid any overages in individual appropriations, and to recognize new revenues and associated expenditures and reserves. The final outcome of the 2020-2021 budget performance will be reported through the 2020-2021 Annual Report, scheduled to be released on September 30, 2021 and reviewed by the City Council in mid-October 2021.

Jim Shannon

JIM SHANNON
Budget Director

Attachment: Finance Department Monthly Financial Report