

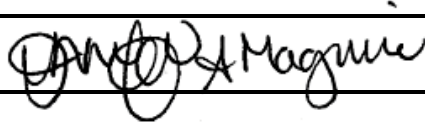
TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Jim Shannon

SUBJECT: 2020-2021 ANNUAL REPORT

DATE: September 30, 2021

Approved



Date

9/30/2021

RECOMMENDATION

It is recommended that the City Council:

- (a) Accept the 2020-2021 City Manager's Annual Report in compliance with City Charter Section 701 (F).
- (b) Adopt Appropriation Ordinance and Funding Sources Resolution amendments in various operating and capital funds to implement the 2020-2021 Annual Report recommendations, as detailed in Section IV (Recommended Budget Adjustments and Clean-Up/Rebudget Actions).

OUTCOME

In accordance with Section 701 (F) of the San José City Charter, the 2020-2021 Annual Report describes the financial status of the City at the end of the 2020-2021 fiscal year. As specified in the City Charter, the focus of the City Manager's Annual Report is a comparison of actual revenue collections and expenditures to projections and appropriations included in the City's budget.

The 2020-2021 Annual Report will provide the City Council with the information necessary to review the financial performance of all City funds. In addition, this report provides a comparison of the actual 2020-2021 Ending Fund Balance for each fund to the estimates used in the development of the 2021-2022 Adopted Budget as well as information on the status of the year-end reserve levels for each of the City's budgeted funds.

Approval of the recommended budget actions will implement required fund balance reconciliations and necessary rebudget and clean-up adjustments based on the final financial performance (unaudited) for 2020-2021. This report also includes actions that are necessary to: revise the 2021-2022 budget to align budgeted revenue and expenditures with the most current information; correct technical problems; recognize new or adjust existing grant, reimbursement, or fee activity revenues and expenditures; fund two urgent fiscal program needs in the General Fund; reflect changes in project and program allocations based on revised cost estimates; and establish a limited number of new projects and programs in special and capital funds.

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The Administration proactively managed 135 budgeted funds in 2020-2021. Budget actions were brought forward during the year to help ensure that revenues and expenditures remained in alignment with actual performance. Through this careful management, the various City funds generally ended the year with revenues close to the budgeted estimates and expenditures below the budgeted allocations.

The City Council approved the 2020-2021 Adopted Budget under the extraordinary circumstances of the early stages of the COVID-19 pandemic: limited historical precedent to understand the extent to which the pandemic would negatively impact the City's budget, a significant infusion of external funding to address the pandemic's impacts to the community – primarily from the Coronavirus Aid, Relief, and Economic Security Act – and an urgency that the City needed to quickly act to help our most vulnerable populations. The budget included actions to both address the anticipated negative revenue impacts to the General Fund and other City funds, such as the Transient Occupancy Tax Fund, General Purpose Parking Fund, and Airport funds, and allocate emergency response resources toward areas of homelessness sheltering and support, local assistance, food and necessities distribution, and direct staff support.

The 2020-2021 Adopted Budget was modified several times throughout the year as the City responded to new information regarding economic performance and persistence of COVID-19 cases. In the General Fund, actions were taken over the course of the year to decrease revenue estimates from business taxes, parking operations and citations, hotel activity, and parks and recreation-related fees. Significant revenue estimate increases included Sales Tax, Property Tax, and Real Property Transfer Tax (Measure E). As a result of these adjustments, as well as careful forecasting, monitoring, and management throughout all City funds, overall 2020-2021 revenues and expenditures ended the year very close to budgeted expectations. However, the fourth quarter of 2020-2021 saw an extremely strong surge of revenue growth in the General Fund, which contributed to a higher than anticipated level of year-end fund balance. The 2020-2021 General Fund Ending Fund Balance of \$369.2 million exceeded the estimate of \$321.2 million used in the development of the 2021-2022 Adopted Budget by \$48.0 million. This variance represents 2.7% of the 2020-2021 Modified Budget. These funds are recommended to be allocated in the 2020-2021 Annual Report, as shown in the table below.

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Recommended 2021-2022 General Fund Adjustments (\$000s)

Additional 2020-2021 Ending Fund Balance	\$47,992
Clean-Up Actions	\$13,621
<hr/>	
Fund Balance Available After Clean-up Actions	\$61,613
Recommended Budget Adjustments	
Required Technical/Rebalancing Actions	(\$19,036)
Grants/Reimbursements/Fee Activities (Sources = \$4.4M; Uses = \$4.6M)	(\$190)
Urgent Fiscal/Program Needs	(\$1,150)
Total Recommended Budget Adjustments	(\$20,376)
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Remaining Fund Balance After Clean-ups/Recommended Adjustments	\$41,237
Distribution of Remaining Fund Balance Per City Council Policy I-18	
2022-2023 Future Deficit Reserve	(\$28,300)
Budget Stabilization Reserve	(\$12,937)
Total Fund Balance Distributed Per Council Policy I-18	(\$41,237)

When bringing forward recommendations for the use of the additional 2020-2021 General Fund Ending Fund Balance, the Administration follows City Council Policy 1-18 and first considers clean-up actions associated with the close-out of the 2020-2021 fiscal year to be essentially non-discretionary and the highest priority. These clean-up actions result in a net increase to the available fund balance of \$13.6 million and consist of: 1) the rebudgeting of anticipated revenue from the commercial paper program to provide temporary encumbrance capacity to the Fire Training Center and Emergency Operations Center construction project in anticipation of the issuance of Measure T and Lease Revenue Bonds in 2021-2022 (increase of \$23.4 million); 2) the rebudgeting of prior year funding to 2021-2022 to complete various projects (decrease of \$7.7 million); 3) and technical adjustments to other revenues and expenditures (decrease of \$2.1 million).

The revised fund balance of \$61.6 million is recommended to fund various required technical and rebalancing actions (\$19.0 million), actions associated with grant and fee activities (net-zero expenditure adjustments of \$190,000), and two urgent fiscal and programmatic needs (\$1.2 million). Notable adjustments in these categories include: establishing a \$10.0 million reserve to offset pandemic related expenses that the Federal Emergency Management Agency (FEMA) may not deem to be reimbursable; providing a City match of \$2.5 million to the Berryessa Flea Market Vendor Business Transition Reserve; allocating a total of \$1.4 million to re-establish the Parks, Recreation and Neighborhood Services Department’s Pest and Turf Management Team through June 30, 2023; a reallocation of \$1.0 million from the Measure E – 35% Low Income Reserve to support the Quetzal Garden affordable housing project; establishing a City Facilities Security Improvements City-Wide Expenses appropriation to provide funding of \$750,000 for security

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enhancements at a variety of City facilities, including City Hall; increasing the Contingency Reserve by \$500,000 (from \$40.0 million to \$40.5 million) to ensure that the reserve totals 3% of General Fund operating expenditures per City Council Policy 1-18; the repurposing of \$500,000 of 2020-2021 savings within the San José BEST and Safe Summer Initiative appropriation to support enhanced accountability and oversight improvements for the program through June 30, 2023; and establishing a city-wide Customer Service Vision and Standards project as a focus area of the new City Manager (\$400,000).

After these adjustments, the remaining fund balance of \$41.2 million is recommended to be distributed in accordance with City Council Policy 1-18. These funds are recommended to fully fund the 2022-2023 General Fund shortfall as reflected in the 2021-2022 Adopted Operating Budget (\$28.3 million), and increase the Budget Stabilization Reserve (\$12.9 million) from \$33.6 million to \$46.5 million, which increases the level of General Purpose Reserves from 6.6% to 7.6% of General Fund operating expenditures, bringing the level closer to the policy target of 10.0%.

While fourth quarter economic performance indicates that revenue growth may be outpacing previous expectations, the Administration does not have the ability to update the shortfall figure until it completes a revised analysis of expected economic conditions and anticipated base budget expenditure costs, which will begin in October and be completed with the issuance of a new Five-Year Forecast at the end of February 2023. Should the City's budgetary position continue to improve, all or a portion of this reserve will be recommended for liquidation as part of the 2022-2023 Proposed Budget process for high-priority one-time uses. It is important to note that fully funding the \$28.3 million 2022-2023 Future Deficit Reserve has the practical implication of freeing up resources in the American Rescue Plan (ARP) Fund. As described in Manager's Budget Addendum #16, Community and Economic Recovery Budget, \$28.3 million of resources within the ARP Fund were contemplated to be set aside to help address potential future budgetary shortfalls. Fully funding the future deficit reserve and increasing the Budget Stabilization Reserve restores the responsibility for addressing future potential budgetary shortfalls within the General Fund, and simultaneously provides additional capacity to allocate more ARP resources to directly aid in the community's recovery, which the City Council will consider in November 2021.

This report also addresses immediate needs and circumstances in various special and capital funds, including the recognition of a separate stream of revenue from the American Rescue Plan Act in the Airport Revenue Fund for rent relief to Airport concessionaires and to assist with eligible Airport operating costs; recognition of commercial paper financing proceeds in the San José Clean Energy Fund to ensure sufficient cash flow through the fiscal year as previously authorized by the City Council; allocating greater than anticipated year-end Construction and Conveyance (C&C) Tax Proceeds into the C&C City-Wide Fund Infrastructure Backlog Reserve to be spent in future years on deferred infrastructure rehabilitation; and, within the Traffic Capital Program, restoring funding to the Transportation Grants Reserve and the City's local spending on pavement maintenance due to higher than anticipated year-end receipts from the Building and Structure Construction Tax and Construction Excise Tax. All recommended budget actions are summarized

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later in this message and described in *Section IV: Recommended Budget Adjustments and Clean-Up/Rebudget Actions*.

As the fiscal year progresses, the Administration will continue to monitor and report on the City's budgetary performance through Bi-Monthly Financial Reports that are agendaized four times a year for review by the Public Safety, Finance, and Strategic Support (PSFSS) Committee, and the Mid-Year Budget Review that is heard by the full City Council in February. The financial results of 2020-2021 will also be factored into the development of the 2023-2027 General Fund Five-Year Forecast that will be released at the end of February 2022.

BACKGROUND

Each year the City issues the Annual Report at the end of September, three months after the close of the fiscal year, as required by the City Charter. Following is a description of the various sections of the Annual Report document.

- **Transmittal Memorandum** – This section provides an overall summary of the 2020-2021 Annual Report.
- **Section I: Budget Performance Summary (All Funds)** – This section provides a comparison of the 2020-2021 budget to actual revenues received and expenditures incurred by fund as well as an explanation of revenue and/or expenditure variances of 10% or greater to the budget. This section also provides a comparison of the year-end actual 2020-2021 Ending Fund Balance by fund to the 2020-2021 Ending Fund Balance/2021-2022 Beginning Fund Balance estimate used in the development of the 2021-2022 Adopted Budget. In addition, a listing of the Earmarked and Contingency Reserves that were available at the end of 2020-2021 by fund is included.
- **Section II: General Fund Budget Performance** – This section provides a summary of the General Fund budget performance in 2020-2021, including the following: Results of Operations in the General Fund, Revenue Performance, and Expenditure Performance.
- **Section III: Selected Special/Capital Funds Budget Performance** – This section provides financial information on the 2020-2021 year-end performance for selected special and capital funds that represent major City operations. It includes a discussion of variances between actual and budgeted revenues and expenditures as well as a comparison between the actual ending fund balance and the fund balance estimated for 2020-2021 in the development of the 2021-2022 Adopted Budget.

BACKGROUND

- **Section IV: Recommended Budget Adjustments and Clean-Up/Rebudget Actions** – This section provides a description of the recommended budget adjustments and clean-up actions for City Council consideration. The proposed actions fall into three categories: (1) adjustments to the 2021-2022 Beginning Fund Balance amounts in various funds, including the General Fund, based on the final reconciliation of 2020-2021; (2) upward and downward adjustments to previously rebudgeted sums to ensure the appropriate amount of unexpended funds are carried over to 2021-2022 to complete projects; and (3) actions based on more recent information that are necessary to revise the 2021-2022 budget to align budgeted revenue and expenditures with the most current information, correct technical problems, recognize new or adjust grant, reimbursement or fee activity revenues and expenditures, fund one-time urgent fiscal/program needs in the General Fund, and reflect changes in project and program allocations based on revised cost estimates as well as establish a limited number of new projects and programs in special and capital funds.
- **Section V: Financial Statements** – This section provides the financial results (unaudited), prepared by the Finance Department, for all budgeted fund groups for 2020-2021. It should be noted that audited financial results will be released later in the fall as part of the 2021 Annual Comprehensive Financial Report for Fiscal Year Ended June 30, 2021. Final fund balance reconciliations to the Annual Comprehensive Financial Report will be conducted for all funds and, while few adjustments are typically necessary, any final adjustments will be brought forward for City Council consideration as part of the 2021-2022 Mid-Year Budget Review.

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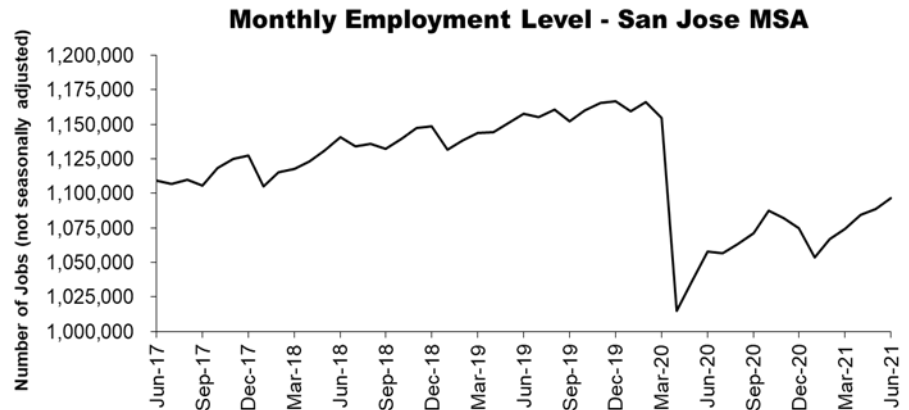
This Analysis section includes the following:

- an overview of the economic environment;
- a discussion of the 2020-2021 budget performance of all City funds;
- a discussion of the 2020-2021 budget performance for the General Fund;
- a discussion of the components of the 2020-2021 General Fund ending fund balance;
- an analysis of the impact of the General Fund performance on the 2021-2022 Adopted Budget; and
- a discussion of the 2020-2021 budget performance of selected special and capital funds.

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Economic Environment

The City of San José had been experiencing strong economic growth coupled with low unemployment levels for over a decade. However, the shelter-in-place mandate issued at the onset of the pandemic had an immediate impact to daily economic activity that was felt throughout 2020-2021.



California’s employment was significantly impacted when health orders in response to the pandemic severely curtailed halted economic activity. As can be seen from the chart above, after the immediate employment drop in April 2020, employment levels have progressively grown, with a smaller decline at the end of 2020 when the pandemic re-surfaced. Employment levels in spring and summer 2021 have continued to expand at a rapid pace, which is anticipated to continue until the end of the calendar year. Taner Osman, Research Manager at Beacon Economics and the UC Riverside Center for Forecasting, stated “Two major headwinds for the state’s economy have been eased: the declining spread of COVID-19 cases and the re-opening of schools. This paves the way for strong job gains through the end of this year.”¹

Prior to the COVID-19 pandemic, the unemployment rate for the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (San José MSA) had not exceeded 3.0% since August 2017. Further, between September 2017 and February 2020 the average local unemployment rate totaled 2.6%, which is considered full employment. However, as can be seen on the chart below, once the shelter-in-place mandate began, unemployment rates began to immediately rise, with the local rate hitting a high of 12.4% in April 2020.

¹ Beacon Economics, Beacon Employment Report, September 17, 2021

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Economic Environment

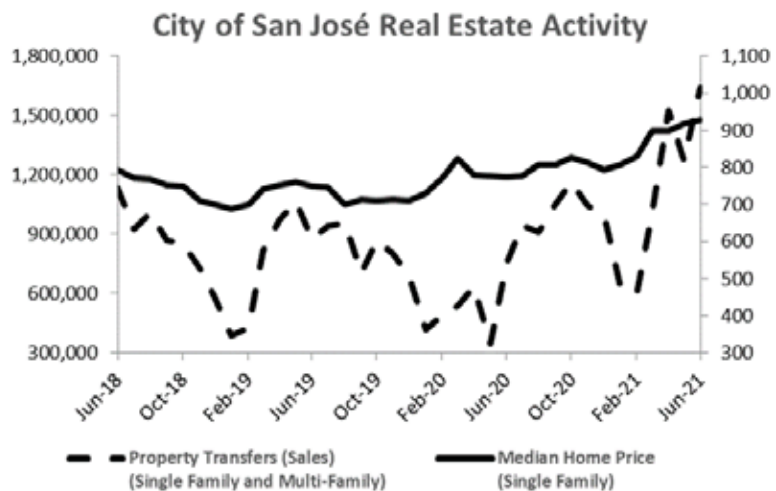
Unemployment Rate (Unadjusted)				
	Feb. 2020	April 2020	June 2020	June 2021**
San Jose Metropolitan Statistical Area*	2.6%	12.4%	10.4%	5.2%
State of California	4.3%	16.0%	14.1%	8.0%
United States	3.8%	14.4%	11.2%	6.1%
* San Benito and Santa Clara Counties Source: California Employment Development Department. ** June 2021 estimates are preliminary and may be updated.				

After topping over 12% near the beginning of the pandemic in April 2020, the local unemployment rate has significantly dropped. In June 2021, the local unemployment rate was 5.2%, which was drastically lower than the June 2020 rate of 10.4%. However, the unemployment rates remain significantly above the February 2020 pre-pandemic level of 2.6%. It is important to note though

that although local unemployment figures have risen since the shelter-in-place mandate began, the rates continue to be lower than the State and the national levels.

Construction permit valuation declined in 2020-2021 from 2019-2020 – which was a historically high year – primarily due to a drop off in industrial activity. The total valuation of projects submitted in 2020-2021 was \$1.9 billion, 23.8% below the \$2.5 billion valuation of projects that were received in 2019-2020. The number of new residential dwelling units permits issued in 2020-2021 totaled 1,975, which was 0.9% below the prior year level of 1,992 permits issued. Valuations for all the land use categories (residential, commercial, and industrial) ended the year slightly below the estimates.

Real estate activity was anticipated to be sluggish in 2020-2021 due 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 through June 2020. However, beginning in September 2020, the local real estate market once again began to experience year-over-year gains. Through June 2021 there were a total of 8,504 property transfers for all residences, which represents growth of approximately 41% from prior year levels. Median single family home prices grew sharply as well. As of June 2021, the median single family home price totaled \$1.48 million, which represents a 24.2% increase from the June 2020 price of \$1.19 million.



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2020-2021 Budget Performance (All Funds)

As shown in Section I of this document, City revenues (excluding Beginning Fund Balances) totaled \$4.2 billion in 2020-2021, which was 8.0% (\$370.4 million) below the budgeted estimate of \$4.6 billion.

In 2020-2021, expenditures (excluding Reserves and Ending Fund Balances) totaled \$4.8 billion, which was \$1.1 billion (18.6%) below the modified budget of \$5.9 billion. At the end of 2020-2021, the Contingency and Earmarked Reserves for all City funds totaled \$830.0 million, which represented 11.9% of the total 2020-2021 Modified Budget of \$7.0 billion (including interfund transfers, loans, and contributions). In the General Fund, Reserves totaled \$196.2 million.

The financial performance in 2020-2021 is used as the starting point for 2021-2022. The collective 2020-2021 Ending Fund Balances for all City funds totaled \$1.81 billion, which was \$44.0 million above the 2020-2021 Ending Fund Balance estimates of \$1.76 billion used in the development of the 2021-2022 Adopted Budget. After adjusting for a total net negative rebudget of \$128.8 million recommended in this report, the adjusted 2020-2021 Ending Fund Balance variance for all funds increases to \$172.8 million, or 2.5% of the 2020-2021 Modified Budget. The adjusted fund balance variance totaled \$61.6 million in the General Fund, \$32.5 million in the special funds, and \$78.7 million in the capital funds.

The City's General Fund ended the 2020-2021 fiscal year within budgeted levels. As shown in the chart below, the General Fund Ending Fund Balance of \$369.2 million was \$48.0 million (2.7% of the 2020-2021 Modified Budget) above the fund balance estimate assumed when the 2021-2022 Adopted Budget was developed. The following table summarizes the General Fund performance in 2020-2021, comparing the actual results to the modified budget and the estimates used to develop the 2021-2022 Adopted Budget.

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2020-2021 General Fund Budget Performance

**Table 1
 General Fund Year-End Status
 For the Year Ended June 30, 2021
 (\$000s)**

Sources	2020-2021 Modified Budget	2020-2021 Year-end Estimate	2020-2021 Budgetary Basis Actual	Actual to Budget Variance	Actual to Estimate Variance
<i>Beginning Fund Balance</i>	400,284	400,284	400,284	-	-
<i>Carryover Encumbrances</i>	46,448	46,448	46,448	-	-
<i>Liquidation of Carry- over Encumbrances</i>	-	-	458	458	458
<i>Revenue</i>	1,342,856	1,344,213	1,355,444	12,588	11,231
Total Sources	1,789,588	1,790,945	1,802,634	13,046	11,689
Uses					
<i>Expenditures/Transfers</i>	1,593,354	1,469,757	1,433,454	(159,900)	(36,303)
<i>Reserves</i>	196,234	-	-	(196,234)	-
Total Uses	1,789,588	1,469,757	1,433,454	(356,134)	(36,303)
<i>Ending Fund Balance</i>	-	321,188	369,180	369,180	47,992

Note: In the chart above, the General Fund excludes the Emergency Reserve Fund and the Cash Reserve Fund, which are budgeted as separate funds and reflected separately in this document. In the 2020-2021 Annual Comprehensive Financial Report, the Emergency Reserve Fund and Cash Reserve Fund will be displayed as part of the General Fund to comply with GASB 54 reporting requirements.

In 2020-2021, total revenue in the General Fund was \$1.4 billion, which was within 0.9%, or \$12.6 million, of the 2020-2021 Modified Budget, and \$11.2 million (0.8%) above the estimate used to develop the 2021-2022 Adopted Budget. The liquidation of prior year carryover encumbrances totaled \$458,000.

General Fund expenditures/transfers of \$1.4 billion were \$159.9 million (8.9%) below the 2020-2021 Modified Budget level of \$1.6 billion and \$36.3 million (2.5%) below the estimate used to develop the 2021-2022 Adopted Budget. Budgeted reserves of \$196.2 million remained unexpended at year-end as expected.

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2020-2021 General Fund Budget Performance

**Table 2
 General Fund
 Comparison of Year-End Actuals With Prior Year
 (\$000s)**

	2019-2020 Actuals	2020-2021 Actuals	Change	% Change
Source of Funds				
Beginning Fund Balance	364,813	400,284	35,471	9.7%
Revenues	1,204,729	1,355,444	150,715	12.5%
Total Source of Funds	1,569,542	1,755,728	186,186	11.9%
Use of Funds				
Personal Services	860,637	871,751	11,114	1.3%
Non-Personal/Equipment/Other	157,610	151,742	(5,868)	-3.7%
City-Wide Expenses	95,007	274,242	179,235	188.7%
Capital Contributions	53,593	54,893	1,300	2.4%
Transfers	48,967	80,826	31,859	65.1%
Reserves	-	-	-	N/A
Total Use of Funds	1,215,814	1,433,454	217,640	17.9%

As shown in Table 2, 2020-2021 General Fund revenues (excluding Beginning Fund Balance, which varies depending on the level of unspent funds carried into the following year) of \$1.4 billion represent an increase of 12.5% from the 2019-2020 collection level of \$1.2 billion. This year-over-year increase is primarily attributable to the City receiving Tax and Revenue Anticipation Notes (TRANs) in 2020-2021 (\$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 did not begin until July 2020, therefore no revenue was received in 2019-2020, compared to the \$50.5 million collected in 2020-2021. Partially offsetting the higher revenues is a significant year-over-year decrease related to the Development Fee Program. Revenue totaling \$71.1 million was received in 2019-2020; however, revenue was not captured in the General Fund in 2020-2021 as these revenues (and associated expenditures) were moved out of the General Fund and into specific Development Fee Program funds. After adjusting for these significant variances, revenue in 2020-2021 increased approximately \$41.2 million (3.6%) from the prior year.

General Fund expenditures of \$1.4 billion in 2020-2021 were 17.9% (\$217.6 million) above prior year expenditure levels of \$1.2 billion. This increase is due to higher City-Wide Expenses (\$179.2 million, primarily driven by the repayment of TRANs), Transfers (\$31.9 million), Personal Services (\$11.1 million), and Capital Contributions (\$1.3 million), partially offset by lower Non-Personal/Equipment/Other (\$5.9 million).

A detailed discussion of the General Fund revenue and expenditure performance is provided in Section II of this document.

ANALYSIS

2020-2021 General Fund Ending Fund Balance

The current budgeting practice of the City is to use the projected level of fund balance expected to remain in the General Fund at the end of any fiscal year as a funding source for the following year. The Ending Fund Balance estimate always contains two components: the portion of the fund balance that is rebudgeted for completing projects or retaining reserves; and the portion which is undesignated and available as a general funding source in the coming year. In the 2021-2022 Adopted Budget, a total fund balance estimate of \$321.2 million was included as a funding source. As discussed earlier, the actual 2020-2021 General Fund Ending Fund Balance of \$369.2 million was \$48.0 million above this estimate.

The components of the 2020-2021 General Fund Ending Fund Balance include additional funding sources, expenditure/transfer savings, and unexpended reserves as described below:

**2020-2021 General Fund
 Ending Fund Balance Components**

Fund Balance Component	\$ Amount (\$ in 000s)
Additional Funding Sources	13,045
Expenditure/Transfer Savings	159,901
Unexpended Reserves	196,234
TOTAL	\$ 369,180

The total Sources of Funds ended the year \$13.0 million above the modified budget as a result of higher revenues (\$12.6 million) and liquidation of carryover encumbrances (\$458,000). For the Uses of Funds, expenditure and transfer savings totaled \$159.9 million, while unexpended reserves totaled \$196.2 million, representing the largest component of the 2020-2021 Ending Fund Balance. Of the \$159.9 million in expenditure savings, a majority was rebudgeted in the 2021-2022 Adopted Budget (\$122.9 million) with additional funding being recommended for rebudget as part of this report (\$10.5 million).

General Fund Reserves, totaling \$196.2 million at the end of 2020-2021, include three categories: Earmarked Reserves (\$137.9 million) established to address specific needs per City Council direction; Ending Fund Balance Reserve (\$18.4 million) established to help ensure sufficient fund balance would be available at the end of 2020-2021 to meet the budgeted estimate used for the development of the 2020-2021 Adopted Budget, and the Contingency Reserve (\$40.0 million) set at a minimum of 3% of expenditures per City Council policy.

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2020-2021 General Fund Ending Fund Balance

As discussed above, it was assumed that \$321.2 million would remain in the General Fund at the end of 2020-2021 and would be carried over to 2021-2022 as Beginning Fund Balance as part of the adoption of the 2020-2021 Budget. These funds, which were expected to be generated from unexpended reserves, unexpended funds that were rebudgeted to 2021-2022, additional revenue, expenditure savings, and the liquidation of carryover encumbrances, were programmed for use in the 2021-2022 Adopted Budget. The actual General Fund Ending Fund Balance was above the estimate used in the 2021-2022 Adopted Budget by \$48.0 million due to revenue and expenditure savings that were above June 30, 2021 levels. Additional adjustments, through clean-up actions, program reconciliations, and the rebudgeting of prior year funding, increase this balance by \$13.6 million, to \$61.6 million.

The following chart details the recommended uses of the \$48.0 million of additional fund balance, as well as other budget adjustments that are proposed as part of this report. Recommended rebudgets and clean-up actions increase the available fund balance by \$13.6 million, inclusive of \$23.4 million of rebudgeted revenue of commercial paper proceeds related to the Fire Training Center and Emergency Operations Center construction project. Once these adjustments have been accounted for, the net available fund balance available for allocation totals \$61.6 million. This additional fund balance is proposed to be allocated to address required technical/rebalancing needs of \$19.0 million, grants and reimbursements totaling \$190,000, urgent fiscal/program needs of \$1.2 million, with the remaining \$41.2 million placed in the 2022-2023 Future Deficit Reserve (\$28.3 million) and Budget Stabilization Reserve (\$12.9 million) in accordance with City Council Policy 1-18.

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Impacts on the 2021-2022 General Fund Budget

RECOMMENDED 2021-2022 GENERAL FUND ADJUSTMENTS (\$000s)

(\$ in 000s)

2020-2021 Additional Fund Balance		\$47,992
• Rebudgets/Clean-Up Actions		\$13,621
Revenue Rebudgets/Clean-Ups	\$25,825	
City-Wide Expenses/Transfers/Reserves	(\$9,427)	
Departmental	(\$1,147)	
General Fund Capital	(\$1,630)	
Fund Balance Available After Clean-Up Actions		\$61,613
• Recommended Budget Adjustments		(\$20,376)
Required Technical/Rebalancing Actions		
FEMA Non-Reimbursable Expenses Reserve	(\$10,000)	
Berryessa Flea Market Vendor Business Transition Fund Reserve	(\$2,500)	
Parks, Recreation and Neighborhood Services (Pest and Turf Management Team)	(\$1,425)	
Measure E – Quetzal Garden	(\$1,000)	
Contingency Reserve	(\$500)	
Emergency Fire Equipment Reserve	(\$500)	
San Jose BEST Accountability and Oversight	(\$500)	
Diridon Station Area Development Planning	(\$450)	
Code Enforcement Permit System Reserve (Multiple Housing Program)	(\$400)	
Coyote Creek Patrol	(\$400)	
Solid Waste Code Enforcement Program Reserve	(\$400)	
Police Department Personal Services (Public Records Act Temporary Staffing)	(\$350)	
Insurance Premiums	(\$300)	
4 th of July Celebration	(\$250)	
Artificial Turf Capital Replacement Reserve	(\$200)	
City Attorney’s Office Outside Litigation Reserve	(\$190)	
Transfers and Reimbursements (CDDD Revenue)	(\$150)	
Fire Department Non-Personal/Equipment (Computer Aided Dispatch System)	(\$130)	
Police Department Non-Personal/Equipment (Recruiting/Marketing)	(\$125)	
Transfer to the Integrated Waste Management Fund (RAPID Equipment Reimb.)	(\$102)	
City Attorney’s Office Personal Services (Public Safety Initiatives)	(\$100)	
Measure E – 35% Low Income Reserve	\$1,000	
Transfers and Reimbursements (Transfer from Self-Insured Medical Fund)	\$447	
Remaining Adjustments	(\$511)	
Subtotal Required Technical/Rebalancing Actions	(\$19,036)	
Grants/Reimbursements (Sources = \$4.4M; Uses = \$4.6M)		(\$190)
Urgent Fiscal/Program Needs		
City Facilities Security Improvements	(\$750)	
Customer Service Vision and Standards	(\$400)	
Subtotal Urgent Fiscal/Program Needs	(\$1,150)	
Remaining Fund Balance Available After Clean-ups/Recommended Adjustments		\$41,237

Distribution of Remaining Fund Balance in Accordance with City Council Policy 1-18	
2022-2023 Future Deficit Reserve	(\$28,300)
Budget Stabilization Reserve	(\$12,937)
Subtotal Distribution per Policy 1-18	(\$41,237)

Remaining Fund Balance Available After All Recommended Actions..... \$0

A summary of the significant adjustments by category is included below. More detail is provided in *Section IV: Recommended Budget Adjustments and Clean-Up/Rebudget Actions*.

Clean-Up Actions (\$13.6 million)

- **Rebudgets/Clean-Up Adjustments (net \$13.6 million)** – A series of adjustments are recommended to complete existing projects in 2021-2022 and to reflect any necessary technical budget adjustments or reconciliation actions. The Annual Report is the point in the budget process where action is required to rebudget unexpended funds from the prior year that were not anticipated when the Adopted Budget was approved, but are required to complete a project in the current year. The largest rebudget actions are for the following appropriations: Other Revenue (Commercial Paper) (+\$23.4 million); Local Assistance (-\$2.1 million), Fire Training Center Relocation (-\$1.8 million), Government Access – Capital Expenditures (-\$1.5 million), and BeautifySJ – Illegal Dumping (-\$1.0 million). Also recommended are actions that reduce previous rebudgets to reflect instances where expenditures for which rebudgets were approved for incorporation into the Adopted Budget exceeded estimates for 2020-2021; therefore, the funds are not available for rebudget to 2021-2022. Other technical adjustments include net-zero shifts between departments and appropriations, as well as the reconciliation of restricted funding for multiple programs (e.g. Measure E reserves, Tree Mitigation, Licenses and Permits (Cardroom Fee), Certified Access Specialist Program, Contractual Street Tree Planting, and Government Access activities).

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Impacts on the 2021-2022 General Fund Budget

A number of General Fund budget adjustments, with a total net cost of \$20.4 million are recommended and can be classified under three categories: 1) Required Technical/Rebalancing Actions (net cost of \$19.0 million) that align already approved revenue estimates and expenditure budgets with the most current tracking information, reallocate funding among appropriations based on updated needs, correct technical problems in the 2021-2022 Adopted Budget, or comply with actions previously authorized by the City Council; 2) Grants/Reimbursement/Fee Activities (net cost of \$0.2 million) actions that recognize new or adjust grants, reimbursements, or fee activity revenues, and adjust the appropriations for these purposes as necessary; and 3) Urgent Fiscal/Program Needs (net cost of \$1.2 million) for emergent needs that the Administration has deemed should not wait until the annual budget process, but require authorization from City Council.

Notable actions under each category are outlined below.

Recommended Budget Adjustments (-\$20.4 million)

- **Required Technical/Rebalancing Actions (-\$19.0 million)**
 - ***FEMA Non-Reimbursable Expenses Reserve*** – establishes a FEMA Non-Reimbursable Expenses Reserve in the amount of \$10.0 million to set aside funding in the event that expenses incurred by the City in response to the COVID-19 pandemic, for which the City is actively pursuing reimbursement through the Federal Emergency Management Agency (FEMA), are later determined as ineligible for reimbursement. The City estimates that total amount eligible for FEMA reimbursement from 2019-2020 through 2021-2022 is \$37.4 million. However, it is common for FEMA to disallow portions of an agency’s submitted expenditures due to documentation and contractual issues, and nuanced interpretations of eligibility requirements. At \$10.0 million, the reserve represents the Administration’s conservative estimate of the City’s pandemic response efforts that may be deemed non-reimbursable by FEMA. The Administration anticipates a determination from FEMA on reimbursement in the second half of 2021-2022. (-\$10.0 million)
 - ***Berryessa Flea Market Vendor Business Transition Fund Reserve*** – provides a City match of \$2.5 million to the Berryessa Flea Market Vendor Business Transition Fund Reserve in accordance with direction received from the City Council at the conclusion of their meeting on June 29, 2021 regarding the Berryessa BART Urban Village Plan and Flea Market Rezoning. Separate memoranda from Mayor Liccardo and Councilmember Carrasco directed the City Manager to leverage funding from the American Rescue Plan Fund, if eligible, to match the commitment from the Developer in their establishment of the Transition Fund. After review of U.S. Treasury regulations, direct use of the American Rescue Plan Fund is likely not eligible for this purpose. As an alternative to pursuing eligible taxes generated from the development, which would likely otherwise be received in the General Fund or within the Traffic Capital Program, the Administration recommends reserving the match now in anticipation of the future contribution from the developer. (-\$2.5 million)

ANALYSIS

Impacts on the 2021-2022 General Fund Budget

- ***PRNS Pest and Turf Management Team Reserve*** – as directed in the Mayor’s June Budget Message for Fiscal Year 2021-2022, as approved by the City Council, this report includes actions to re-purpose 2020-2021 General Fund savings to reestablish the Parks, Recreation and Neighborhood Services (PRNS) Pest and Turf Management Team on a one-time basis. This team works to maintain turf conditions through the removal of pests from parks and fields in safe, humane, and environmentally friendly manner. Separate actions fund the team in 2021-2022 (\$425,000), and reserve funding to continue the team through 2022-2023 (\$1.0 million). (-\$1.4 million)
- ***Measure E – Quetzal Garden*** – establishes the Measure E - Quetzal Garden appropriation to the Housing Department in the amount of \$1.0 million to support the completion of the Quetzal Garden affordable housing project. The City Council previously approved the commitment of providing \$10.0 million in soft debt loan financing for this project. This funding will close the financing gap and fully fund the project. The funding specifically supports creating the community serving ground floor facility that will create a new home for Somos Mayfair, Excite Credit Union, and a small business incubator sponsored by the Latino Business Association. A corresponding decrease to the Measure E - 35% Low Income Reserve appropriation offsets this action. (-\$1.0 million)
- ***Contingency Reserve*** – increases the Contingency Reserve by \$500,000, from \$40.0 million to \$40.5 million, in accordance with Council Policy 1-18 which provides for the maintenance of a minimum 3% Contingency Reserve in the General Fund to meet unexpected circumstances arising from financial and/or public emergencies that require immediate funding that cannot be met by any other means. (-\$500,000)
- ***Emergency Fire Equipment Reserve*** – establishes the Emergency Fire Equipment Reserve in the amount of \$500,000 to set aside funding for emergency fire equipment replacement. Funding is anticipated to be needed in the current year to replace lifesaving medical equipment and radios that have reached the end of their useful life. Additionally, a reserve is being established in the Construction Tax and Property Conveyance Tax Fund: Fire Protection Purposes Fund in the amount of \$1.4 million for the same purpose. As costs and needs arise for these items, the Administration will recommend allocating all or a portion of this reserve as part of a future budget process. (-\$500,000)
- ***San José BEST Accountability and Oversight*** – as directed by City Council’s approval of the Mayor's June Budget Message for Fiscal Year 2021-2022, this action reallocates year-end San José Bringing Everyone’s Strengths Together (BEST) appropriation savings of \$500,000 to fund San José BEST Accountability and Oversight program through June 30, 2023 by establishing a City-Wide Expenses appropriation of \$170,000 for 2021-2022 and setting aside \$330,000 in a reserve to be spent in 2022-2023. Over an eighteen-month period, these resources will be focused on improving San José BEST contract management and accountability and expand the program’s evaluation design to include individual outcome assessments. A Senior Analyst would manage the existing team’s data sharing, collection and analysis efforts related to data-sharing partnerships with

ANALYSIS

Impacts on the 2021-2022 General Fund Budget

key stakeholder agencies; and lead the development, implementation, and management of 1) a content management system (CMS) system; and 2) further efforts to improve performance data collection tools. An Analyst would provide enhancements in day-to-day contract monitoring, grantee technical assistance, and accountability measures as well as assist with the grant application process, contract development and execution. The CMS will be used to collect and track activity and participant data that will be used to evaluate the San José BEST Grant Program's performance in terms of "direct impacts" to the community in areas such as academic performance, truancy/graduation rates, and arrest/incarceration rates. An evaluation of these one-time accountability and oversight enhancements will help inform the level of ongoing support that may be considered during the 2023-2024 budget development process. (-\$500,000)

- ***Diridon Station Area Development Planning*** – increases the Diridon Station Area Development Planning appropriation in the amount of \$449,543, reallocating funding provided by Google in prior years and consolidating previously separate appropriations to continue work on the next phase of development review for the Downtown West project and related Diridon Station Area plans. In addition to processing conformance review applications for Downtown West, temporary staff will work on: Infrastructure/Amenities Analysis, Diridon Financing Plan, District-wide Parking Plan, Diridon Station Area Amendments, CEQA process, and ongoing public outreach, including language services. (-\$449,543)
- ***Code Enforcement Permit System Reserve (Multiple Housing Program)*** – increases the Code Enforcement Permit System Reserve by \$400,000, from \$1.9 million to \$2.3 million, to set aside unspent fee revenue related to the Multiple Housing Program from 2020-2021 for a future software upgrade of the City's Code Enforcement Permit System for the Multiple Housing Program. (\$-400,000)
- ***Coyote Creek Patrol*** – establishes the Coyote Creek Trail Patrol City-Wide Expenses appropriation to the Police Department in the amount of \$400,000. City Council's approval of the Mayor's March Budget Message for Fiscal Year 2021-2022 prioritized funding for enhanced maintenance and safety of the Guadalupe River Park as well as the Coyote Creek Trail. This allocation provides matching funding for a pending agreement with the Santa Clara Valley Water District (SCVWD), which aligns with previous agreements the City has had with SCVWD over the years to fund safety-related programs. The one-year agreement is still under development, though both parties are anticipated to allocate \$400,000 for a total of \$800,000, providing police officers to maintain a law enforcement presence on the Coyote Creek Trail from William Street to Tully Road for 10 hours a day, 7 days per week to address potential criminal activity within waterways. This section of the Coyote Creek Trail is new and will likely have high usage. It is anticipated that the agreement and the corresponding budget adjustments related to the SCVWD's share will be brought forward for City Council approval as part of a future City Council agenda. (-\$400,000)

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Impacts on the 2021-2022 General Fund Budget

- ***Solid Waste Code Enforcement Program Reserve*** – establishes the Solid Waste Code Enforcement Program Reserve in the amount of \$400,000. The Solid Waste Code Enforcement Program is a full cost recovery program funded through fees, and the program ended 2020-2021 with expenditure savings totaling \$400,000. This funding will be set aside for future use by the Solid Waste Code Enforcement Program. (-\$400,000)
- ***Police Department Personal Services (Public Records Act Temporary Staffing)*** – increases the Police Department's Personal Services appropriation by \$350,000 to fund eight rehired retirees to address the workload associated with amendments to the California Public Records Act (CPRA) and the volume of records requests. This action increases the amount of staff supporting public records requests to 33, including 10 full-time personnel and 23 staff working part-time. Though currently, the Department is only budgeted for 9 positions to support this activity. Even with recent technology improvements to assist with video redaction, the backlog of requests remains high. These temporary staff will provide capacity for the processing, redaction, and production of video requests for body worn camera footage, as well as the establishment of departmental procedures, coordination with the Office of the City Attorney, compliance with policies, and the collection of applicable fees. (-\$350,000)
- ***Insurance Premiums*** – increases the Insurance Premiums City-Wide Expenses appropriation to the Finance Department by \$300,000, from \$1.52 million to \$1.82 million, to support additional costs for the City's insurance coverage and annual renewals as recently approved by the City Council. These additional costs are a result of coverage updates and premium increases for the City's overall insurance program, which includes property/casualty and flood excess insurance products and law enforcement professional liability insurance, for annual policy periods starting October 1, 2021. (-\$300,000)
- ***4th of July Celebration*** – as directed in the Mayor's June Budget Message for Fiscal Year 2021-2022, as approved by City Council, this action establishes the 4th of July Celebration City-Wide Expenses appropriation to the Office of Economic Development and Cultural Affairs in the amount of \$250,000 to support costs associated with a 4th of July pyrotechnic event at Discovery Meadow in July 2022. While the Administration may work with other groups to host the celebration, this allocation provides the estimated costs for a pyrotechnic contract, event production, marketing and communications, and City costs for traffic control, permits, and related City services. (-\$250,000)
- ***Artificial Turf Capital Replacement Reserve*** – increases the Artificial Turf Capital Replacement Reserve by \$200,000, from \$2.9 million to \$3.1 million, due to unused funds from the Smythe Sports Field Turf Replacement appropriation. Funding in this reserve will help fund future artificial turf replacements. (-\$200,000)

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Impacts on the 2021-2022 General Fund Budget

- ***City Attorney's Office Outside Litigation Reserve*** – increases the City Attorney's Office Outside Litigation Reserve by \$190,000, from \$810,000 to \$1.0 million, to ensure there is sufficient funding to support costs incurred for contracted litigation services and outside counsel, as needed by the City Attorney's Office. This action restores the reserve back to the initial amount as a portion of the reserve was used in Fiscal Year 2020-2021. (-\$190,000)
- ***Transfers and Reimbursements (CDDD Revenue)*** – decreases the estimate for revenue from Transfers and Reimbursements by \$150,000 to account for the elimination of the transfer from the Integrated Waste Management (IWM) Fund for Construction and Demolition Diversion Deposit (CDDD) revenue. Typically, any forfeited deposits are transferred to the General Fund after ensuring that all applicable expenses in the IWM Fund are met. However, a reconciliation of actual revenues and expenses for 2020-2021 has determined that these funds are needed by the CDDD program to ensure cost recovery in the IWM Fund. There is a corresponding action to decrease the Transfer to the General Fund - CDDD Revenue in the IWM Fund. (-\$150,000)
- ***Fire Department Non-Personal/Equipment (Computer Aided Dispatch System)*** – increases the Non-Personal/Equipment appropriation for the Fire Department by \$130,000. The County of Santa Clara will be updating their Communication Computer Aided Dispatch (CAD) System in April 2022. Currently, the County of Santa Clara and the San José Fire Department have compatible CAD systems to communicate with each other during emergency dispatch. With this updated CAD system, the Fire Department will need to update their own system to communicate with other agencies within the County Service Area. (-\$130,000)
- ***Police Department Non-Personal/Equipment (Recruiting/Marketing)*** – increases the Police Department's Non-Personal/Equipment appropriation by \$125,000 to fund contractual services to support job fairs and recruiting events; conduct targeted radio, print, and social media marketing; and conduct outreach in publications, at community colleges, and at military agencies. A contract for similar services lapsed in April 2021; afterward, the Police Department saw a drop in qualified applicants for police recruit academies. This funding ensures sufficient funding is in place to provide a similar level of service for future academies. The Police Department has approximately 60 vacant positions as of August 27, 2021 (including 12 sworn positions) and will continue their aggressive efforts to hire for the June Police Recruit Academy (the October Academy is set and the February Academy has begun background investigations), 9-1-1 Emergency Communications Center civilian positions, and other civilian position vacancies in the Department. (-\$125,000)

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Impacts on the 2021-2022 General Fund Budget

- ***Transfer to the Integrated Waste Management Fund (RAPID Equipment Reimbursement)*** – establishes a transfer from the General Fund in the amount of \$101,797 to reimburse the Integrated Waste Management (IWM) Fund for vehicles previously purchased for the Rapid Team, as adjusted for depreciation. The 2021-2022 Adopted Budget shifted the Rapid Team from the Environmental Services Department to the Parks Recreation and Neighborhood Services Department as part of the BeautifySJ management consolidation, including all non-personal/equipment funding for contractual services, supplies, and materials. This transfer from the General Fund appropriately compensates the IWM Fund for its previous investment in purchasing the vehicles. (-\$102,000)
- ***City Attorney's Office Personal Services (Public Safety Initiatives)*** – as directed in the Mayor's June Budget Message for Fiscal Year 2021-2022, as approved by City Council, this action increases the Office of the City Attorney's Personal Services appropriation by \$100,000, allocated from the Office of the Mayor's budget, to support costs for an Associate City Attorney working on gun violence restraining orders and criminal litigation. A corresponding decrease to the Office of the Mayor's budget offsets this action. (-\$100,000)
- ***Transfers and Reimbursements (Transfer from Self-Insured Medical Fund)*** – increases the revenue estimate for Transfers and Reimbursements by \$446,842 to recognize a transfer to the General Fund from the Self-Insured Medical Fund. The Self-Insured Medical Fund had received transfers from the General Fund in prior years to ensure fund solvency. This amount reflects the remaining balance in the fund that can be returned to the General Fund. A final reconciliation of this fund and a transfer of any remaining fund balance will be included as part of the 2021-2022 Mid-Year Budget Review. (\$447,000)
- ***Remaining Adjustments*** – Remaining actions include technical corrections or reallocations, and other smaller adjustments. These include the reallocation of funds for Learning and Development activities between appropriations and the reallocation of staffing costs between funds to align with actual levels of support. Additional actions increase departmental Non-Personal/Equipment funding for various activities, including: gaming background services; replacement of equipment/tools used by Fire academies; Aircraft Rescue/Fire Fighting Services; Microsoft licensing; Police Training Center maintenance and operations; Energy and Water Building Performance consultant services; and equipment to support the Pest and Turf Management Team. (-\$511,000)

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Impacts on the 2021-2022 General Fund Budget

- **Grants/Reimbursements/Fees (\$0.2 million)**
 - A series of adjustments - net revenues of \$4.4 million offset by net expenditures of \$4.6 million - are recommended to recognize new and updated revenues and expenditures for ***Grants, Reimbursements, and/or Fees***, primarily for the following Departments: Office of Economic Development and Cultural Affairs (net-zero adjustments of \$1.9 million); Parks, Recreation and Neighborhood Services Department (increase of \$187,000, with \$670,000 revenue-supported expenditure adjustments); Police Department (net-zero adjustments of \$512,000); Community Energy (net zero adjustments of \$483,000); and, the Library Department (net-zero adjustments of \$469,000). These adjustments are further described in *Section IV. Recommended Budget Adjustments and Clean-Up/Rebudget Actions*.

- **Urgent Fiscal/Program Needs (-\$1.2 million)**
 - ***City Facilities Security Improvements*** – establishes a City Facilities Security Improvements City-Wide Expenses appropriation in the Public Works Department in the amount of \$750,000. The safety of the public and employees is the highest priority for the City and this funding will allow the City to enhance security features and protocols in various facilities. These enhancements may include, but are not limited to, the installation and staffing of additional metal detectors at various entrances to City facilities, increased security patrols through a combination of sworn Police Officers and civilian Public Works Security Officers, and the installation of physical improvements such as security cameras and railings. As these improvements are implemented and evaluated over the course of the fiscal year, the Administration intends to bring forward a recommendation for ongoing funding as part of the 2022-2023 budget development process. (-\$750,000)

 - ***Customer Service Vision and Standards*** – establishes a Customer Service Vision and Standards City-Wide Expenses appropriation to the Office of the City Manager in the amount of \$400,000 for the Office of Civic Innovation, as a first step, to support the development of a city-wide customer service vision and standards project as a focus of the new City Manager. The Customer Service Vision and Standards project seeks to develop a set of standards that will serve as cornerstones of a multiyear transformation of the person-to-person customer service experience in the City of San José. The approach for this standard is to engage a consultant to conduct a discovery of the current customer service experience, challenges, and future opportunity areas. The current state of the customer service experience will be mapped by customer segments, personas, and journey maps, and a customer service vision and set of standards that represent the foundational building blocks of a transformation plan will then be formulated. The work will identify improvement opportunities and pilot initial ideas to deliver impact through testing and measuring early concepts. (-\$400,000)

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Impacts on the 2021-2022 General Fund Budget

Recommended Distribution of Remaining Fund Balance per City Council Policy 1-18 (-\$41.2 million)

Per Council Policy 1-18, Operating Budget and Capital Improvement Program Policy, after necessary appropriation adjustments to correct and update the current year budget, any remaining General Fund ending fund balance after the close of the fiscal year shall first be allocated to offset any projected deficit for the following fiscal year, with any excess allocated to: 1) the Budget Stabilization Reserve and/or Contingency Reserve; 2) Unmet/deferred infrastructure and maintenance needs; and, 3) Other one-time urgent funding needs. The Administration has identified two adjustments in accordance with this policy.

Two adjustments in accordance with this policy are outlined below.

2022-2023 Future Deficit Reserve – establishes the 2022-2023 Future Deficit Reserve in the amount of \$28.3 million. Of the \$38.3 million General Fund shortfall that was fully addressed in the 2021-2022 Adopted Operating Budget, only \$6.7 million was resolved on an ongoing basis. When combined with the \$35.0 million shortfall for 2022-2023 as estimated in the Five-Year Forecast released at the end of February 2021, the estimated General Fund shortfall for 2022-2023 stands at \$28.3 million. While fourth quarter performance indicates that revenue growth may be outpacing previous expectations, the Administration does not have the ability to update the shortfall figure until it completes a revised analysis of expected economic conditions and anticipated base budget expenditure costs, which will begin in October and complete with the issuance of a new Five-Year Forecast at the end of February 2022. (-\$28.3 million)

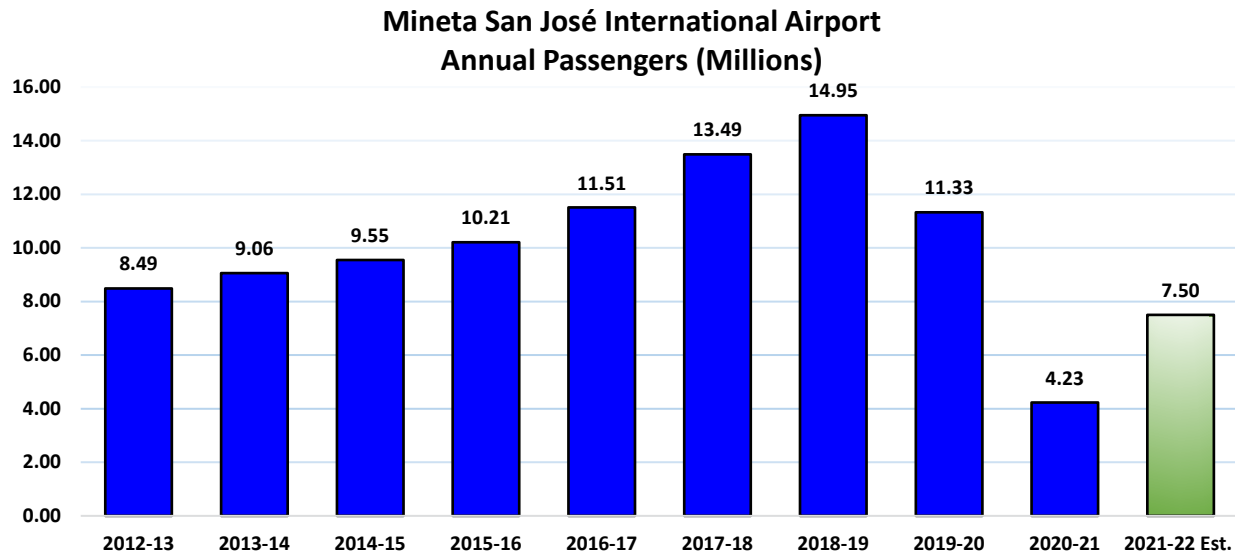
Budget Stabilization Reserve – increases the Budget Stabilization Reserve by \$12.9 million, from \$33.6 million to \$46.5 million, in accordance with City Council Policy 1-18 to maintain an adequate reserve level to provide budget stability when there are fluctuations that result in lower than projected revenues and/or higher than projected expenditures that cannot be re-balanced within existing budgeted resources in any given year. The Budget Stabilization Reserve is intended to provide a buffer, or bridge funding, to protect against reducing service levels when these fluctuations occur. This action, along with a separate action to increase the Contingency Reserve by \$500,000 to reach a level of \$40.5 million, and the existing budgeted funds for the Workers' Compensation/General Liability Catastrophic Reserve at \$15.0 million, brings the total General Purpose Reserve level to 7.6% of General Fund operating expenditures. The target set in City Council Policy 1-18 is 10%. (-\$12.9 million)

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2020-2021 Selected Special/Capital Funds Budget Performance

Airport Operating Funds

The Airport served 4.23 million passengers in 2020-2021, which was an overall decrease of 62.7% from 2019-2020. The COVID-19 pandemic continued to cause significant disruptions to domestic and international air travel. Passenger levels showed steady improvement from January through June 2021. Passenger levels are anticipated to recover gradually over several years given the ongoing uncertainty surrounding the COVID-19 pandemic and resulting impact to the general economy. For 2021-2022, projections reflect an approximately 75% increase from 2020-2021 levels, or 7.5 million passengers.



All airport activity categories demonstrated declines as compared to last year, including traffic operations, landed weights, gallons of aviation fuel sold, and ground transportation trips.

Overall, revenue performance was below budget by \$6.2 million (3.3%). Airline Rates and Charges (combined total of landing fees and terminal rents) and all other operating categories, excluding transfers and grant funding, ended the year at \$132.3 million, which was \$6.7 million below the budget of \$139.0 million. The negative variance is distributed across Landing Fees, Airfield, Parking and Roadway, Terminal Building Concessions, and Terminal Rental revenues, slightly offset by Miscellaneous and Petroleum revenues that finished the year slightly above the budget. The Airport worked with tenants to implement rent deferrals and relief where possible to support the long-term relationships and minimize economic impacts to the companies and their staff due to the pandemic. The partnership is important to continuing operations and service levels as passenger levels continue to increase.

ANALYSIS

2020-2021 Selected Special/Capital Funds Budget Performance

Airport Operating Funds

The Airport Customer Facility and Transportation Fee Fund had year-end expenditure savings of \$491,000 (2.2%) and Airport Maintenance and Operation Fund had a year-end expenditure savings of \$20.8 million (17.6%) compared to budgeted levels of \$118.3 million. The savings were primarily attributable to non-personal/equipment, the majority of which (\$19.2 million) resulted from reduced service levels and other expenditure reduction strategies implemented in response to the effects of COVID-19.

San José Clean Energy Fund

The San José Clean Energy Fund, managed by the Community Energy Department, facilitates the delivery of the San José Clean Energy program (SJCE), which provides residents and businesses of San José with cost competitive electricity and higher renewable content than PG&E. Total Energy Sales ended the year at \$280.4 million, or 3.0%, below the modified budgeted estimate of \$289.0 million. Additionally, the Cost of Energy expenditure ended the year 6.7% below the modified budget of \$295.0 million at \$275.2 million.

In November 2020, City Council approved SJCE's 2021 generation rates for its default GreenSource product at 0.25% below PG&E's rates, inclusive of the Power Charge Indifference Adjustment (PCIA) and Franchise Fee Surcharge for all customers. PG&E's PCIA has risen over 900% between 2013 and 2021, and 41% alone between 2020 and 2021. As a result of the increasing PCIA fees, the City Council approved in May 2021 a rate increase of 8% above PG&E generation rates, an increase to the renewable energy content of GreenSource to 55%, and the introduction of a new low-cost GreenValue product set to match PG&E rates.

However, rising PCIA fees together with a delayed PG&E rate increase, bad debt for unpaid customer bills due to the pandemic, high energy market prices, the effect of weather events, and facilities that experienced operational issues negatively affected SJCE's revenues and cash flow projections. In June 2021, City Council approved the issuance of \$15.0 million of Commercial Paper Notes to cover SJCE's identified cash flow shortage through June 2021, and approved a total Commercial Paper authorization of up to \$95.0 million. Consistent with the June 2021 Commercial Paper program authorization and corresponding baseline cash flow projections, this report recommends recognition of \$53.0 million of Commercial Paper proceeds in 2021-2022. In accordance with City Council direction, staff will return to the Transportation and Environment Committee in December 2021 with a report on SJCE's business plan and outlook for the next twelve months.

ANALYSIS

2020-2021 Selected Special/Capital Funds Budget Performance

Capital Fund Major Revenues

A number of taxes and fees levied on construction and property resale (conveyance) activity provide a large source of revenue to the City’s Capital program. The 2020-2021 actual collections in these capital revenue categories ended the year above budgeted estimates. The chart below provides a comparison of estimated revenues to actual revenues, and a discussion of the three largest revenue sources follows.

**Construction-Related Capital Program Revenues Comparison
 (\$ in Thousands)**

	2020-2021 Estimate*	2020-2021 Actuals	% Variance
Construction and Conveyance Tax	\$40,000	\$53,131	33%
Building and Structure Construction Tax	\$22,000	\$24,248	10%
Construction Excise Tax	\$17,000	\$20,083	18%
Municipal Water System Fees	\$75	\$54	(28%)
Residential Construction Tax	\$200	\$249	25%
Sanitary Sewer Connection Fee	\$500	\$514	3%
Storm Drainage Connection Fee	\$200	\$85	(58%)

* Revenue estimate used in the development of the 2021-2022 Adopted Capital Budget.

- **Construction and Conveyance Tax**

Real estate activity (primarily housing re-sales) determines the collection level of one of the major capital revenue sources, the Construction & Conveyance (C&C) Tax. Approximately 99% of C&C Tax is derived from a tax imposed upon each transfer of real property, with the remaining 1% generated from a construction tax levied on most types of construction. C&C Tax revenues, which are a significant source of funds for the Parks and Community Facilities Development, Library, Fire, Service Yards, and Communications capital programs, totaled \$53.1 million in 2020-2021 – an all-time record high for this revenue category. This collection level is \$13.1 million above the Modified Budget and the estimated collection level of \$40.0 million, and \$12.2 million (29.8%) higher than 2019-2020 receipts of \$40.9 million. For 2021-2022, \$38.0 million is budgeted, and will likely be recommended to increase later in the fiscal year as more information regarding local real estate activity is received. The following graph displays the history of Construction and Conveyance (C&C) Tax receipts.

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2020-2021 Selected Special/Capital Funds Budget Performance

Capital Fund Major Revenues



- **Building and Structure Construction Tax and the Construction Excise Tax**

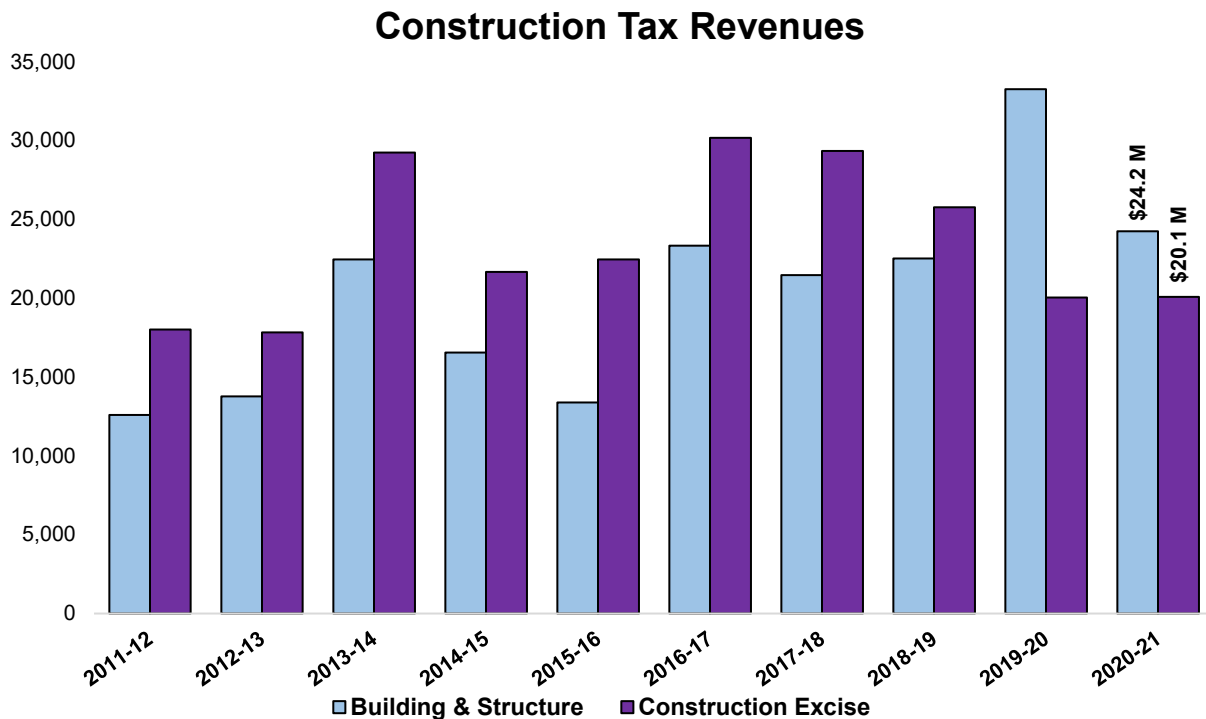
The Building and Structure Construction Tax and the Construction Excise Tax are major sources of funding for the Traffic Capital Program. Year-end collections in the Building and Structure Construction Tax category totaled \$24.2 million in 2020-2021. This collection level was 10.2% (\$2.2 million) above the modified budget estimate of \$22.0 million and \$4.2 million above the revenue estimate of \$20.0 million used to develop the 2021-2022 Adopted Capital Budget; however, the collection level was \$9.0 million less than the historically high amount of \$33.3 million received in 2019-2020. Construction Excise Tax receipts for 2020-2021 totaled \$20.08 million: 18.1% (\$3.1 million) above the modified budget estimate of \$17.0 million; \$2.1 million above the \$18.0 million used to develop the 2021-2022 Adopted Capital Budget; and a 0.2% (\$32,000) decrease from 2019-2020 collections of \$20.05 million.

The graph below displays the collection history of both the Building and Structure Construction Tax and Construction Excise Tax receipts. Valuation activity in 2019-2020 nearly reached the historically high levels of but declined in 2020-2021. The status of these volatile taxes will be closely monitored throughout 2021-2022 to determine if budget actions are necessary to revise the revenue estimates.

ANALYSIS

2020-2021 Selected Special/Capital Funds Budget Performance

Capital Fund Major Revenues



Special and Capital Funds Budget Adjustments

A number of budget adjustments for both special and capital funds are included in this report, including recognition of grants, net-zero transfers/reallocations, new allocations for a small number of high priority projects and programs, and required fund rebalancing activity.

In the Transient Occupancy Tax (TOT) Fund, \$1.9 million in net savings in the Cultural Grants (\$1.4 million) and Cultural Grants Administration (\$0.5 million) appropriations are recommended to be reallocated to a new Cultural Grants Reserve, pending future distribution as projections of TOT revenue performance for 2021-2022 are revisited later this fall during development of the 2022-2023 Preliminary Forecast. If TOT receipts meet budgeted expectations during the course of 2021-2022, this reserve will be recommended to fund additional cultural grants. If TOT receipts fall short, this reserve will buffer against offsetting reductions.

ANALYSIS

2020-2021 Selected Special/Capital Funds Budget Performance

Special and Capital Funds Budget Adjustments

Actions are included to decrease the Resident Relief - Food and Necessities Distribution appropriation in the American Rescue Plan Fund to reclassify \$3.6 million of eligible expenditures anticipated between July 2021 and December 2021 from the American Rescue Plan Fund to the Coronavirus Relief Fund, thereby optimizing the use of remaining federal CARES Act funds prior to their expiration in December 2021. This is an interim adjustment to align eligible COVID-19 response and recovery initiatives with eligible funding sources. However, at the November 2021 City Council meeting, the Administration will recommend a realignment of American Rescue Plan Act funding for community and economic recovery initiatives, which may include the extension of the Food and Necessities Distribution program beyond December 2021 and supplemental funding.

In the Airport Capital Program, actions are included in the Airport Renewal and Replacement Fund to increase the Airfield Geometric Implementation project appropriation by \$840,000, from \$2.6 million to \$3.5 million, to provide additional local share funding for an anticipated grant award from the Federal Aviation Administration (FAA). In order to apply for an Airport Improvement Program grant, the FAA requires demonstration of available funding with the grant application. A corresponding decrease to the Ending Fund Balance is recommended.

In the Parks and Facilities Development Capital Program, several adjustments are recommended in various funds. A couple of notable adjustments include an allocation of \$350,000 to establish the Trail: Five Wounds Trestle Study project in the Subdivision Park Trust Fund to assess the integrity of the trestle that was damaged by fire recently, and an action to increase the Infrastructure Backlog Reserve by \$2.5 million, from \$1.9 million to \$4.4 million, based on higher than anticipated Construction and Conveyance tax receipt in 2020-2021, to set aside funding for future infrastructure backlog needs.

It is important to note that this report includes actions to restore \$200,000 back to the Artificial Turf Capital Replacement Reserve in the General Fund due to the previous deferral of the Smythe Artificial Turf Field Replacement project. As directed in the Mayor's June Budget Message for Fiscal Year 2019-2020, staff was directed to return to City Council to present options for the Smythe Field rehabilitation and improvements and seek direction from the City Council. The initial estimate of \$1.2 million was included in the 2019-2020 Adopted Capital Budget with \$1.0 million from Council District 8 Construction and Conveyance (C&C) Tax and \$200,000 from the Artificial Turf Capital Replacement Reserve in the General Fund. At the time the field was built which was prior to 2010, the City had a contract with the Boys & Girls Club (Club) whereby the Club would pay half of the cost of the turf replacement. The Club is not able to provide that funding, and the City no longer has a contract for them to operate the field.

ANALYSIS

2020-2021 Selected Special/Capital Funds Budget Performance

Special and Capital Funds Budget Adjustments

Since the time the project was first identified as a capital need, the estimated cost for improvements has escalated to approximately \$4 million. Funding is not available from the Artificial Turf Capital Replacement Reserve to fund the full replacement; nor is additional funding available from Council District 8 C&C. This report includes budget adjustments to restore the \$200,000 back to the Artificial Turf Capital Replacement Reserve. No other budget actions are needed since the Council District 8's C&C funds were reallocated to other capital projects as part of the 2021-2022 Adopted Capital Budget. The field has been closed and is currently not available for public use. Staff recommends that the field remain closed while they investigate the potential to use Community Development Block Grant Funds for the field renovation.

In the Public Safety Capital Program, an allocation of \$1.4 million to establish the Emergency Fire Equipment Reserve in the Fire Construction and Conveyance Tax Fund is recommended, along with the \$500,000 allocated in the General Fund. Funding is anticipated to be needed in 2021-2022 to replace lifesaving medical equipment and radios that have reached the end of their useful life. As costs and needs arise for these items, the Administration will recommend allocating all or a portion of this reserve as part of a future budget process. A corresponding decrease to the Ending Fund Balance is recommended.

In the Traffic Capital Program, actions to increase the Transportation Grants Reserves in the Building and Structure Construction Tax Fund (\$2.0 million) and Construction Excise Tax Fund (\$3.0 million) are recommended. Actual construction tax revenue collections ended 2020-2021 higher than originally estimated and it is recommended that the additional funding be set aside in the Transportation Grants Reserves to provide City matching funds for grant funding opportunities. Additionally, City funds for pavement maintenance are recommended to be increased by \$1.0 million to restore funding that was decreased in the 2021-2026 Adopted Capital Improvement Plan as part of rebalancing actions for the Traffic Capital Program. This action will be funded by available fund balance in the Construction Excise Tax Fund as a result of various project savings that were generated at the end of 2020-2021.

Finally, the rebudget of unexpended funds for projects and programs extending into 2020-2021 is recommended in this report. Details of these adjustments can be found in Section IV of this report.

NEXT STEPS

The results of the 2020-2021 Annual Report will provide an updated starting point for monitoring 2021-2022 financial performance, with actual revenue and expenditure trends factored into the analysis of the General Fund and numerous special and capital funds. Information on the City's budget for 2021-2022 will be provided in the Bi-Monthly Financial Reports that are heard at the PSFSS Committee and the 2021-2022 Mid-Year Budget Review.

The 2020-2021 Annual Report results will also be factored into the 2022-2023 budget development process. The General Fund Five-Year Forecast is scheduled to be released in late February 2022. The 2022-2023 Proposed Capital and Operating Budgets are scheduled to be released by May 2, 2022.

PUBLIC OUTREACH

This document is posted on the City's website for the October 19, 2021, City Council agenda.

COORDINATION

The City Manager's Budget Office coordinated with the Finance Department on the reconciliation of the City's funds and coordinated with all City Departments and City Council appointees, as applicable, on recommended budget adjustments that are brought forward in this document.

COMMISSION RECOMMENDATION/INPUT

No commission recommendation or input is associated with this action.


CONCLUSION

Through careful fiscal management, overall revenues for the various City funds ended the year close to estimated levels and expenditures were below budgeted allocations. The City Council approved the 2020-2021 Adopted Budget under the extraordinary circumstances of the early stages of the COVID-19 pandemic. The budget was modified several times throughout the year as the City responded to new information regarding economic performance and persistence of COVID-19 cases. As a result of these adjustments, as well as careful forecasting, monitoring, and management throughout all City funds, 2020-2021 revenues and expenditures ended the year very close to budgeted expectations. However, the fourth quarter of 2020-2021 saw an extremely strong surge of revenue growth in the General Fund, which contributed to a higher than anticipated level of year-end fund balance.

In the General Fund, the additional fund balance at the end of 2020-2021 after considering clean-up actions totaled \$61.6 million. Along with a number of net-zero adjustments related to grants, reimbursements and fees, recommendations are included in this report to allocate \$19.2 million of the fund balance toward various required technical and rebalancing actions, \$1.2 million for two urgent fiscal and programmatic needs, as well as \$28.3 million to the 2022-2023 Future Deficit Reserve and \$12.9 million to the Budget Stabilization Reserve in accordance with City Council Policy 1-18.

CONCLUSION

The Administration will continue to monitor and report on the City's budget performance through the Bi-Monthly Financial Reports and the Mid-Year Budget Review. The financial results of 2020-2021, as well as the actual performance in 2021-2022, will be factored into the development of the 2022-2023 budget. The 2023-2027 General Fund Five-Year Forecast will be released at the end of February 2022 for budget planning purposes.


Jim Shannon
Budget Director

CERTIFICATION OF FUNDS

I hereby certify that there will be available for appropriation in the designated funds and in the amounts as listed below in fiscal year 2021-2022 monies in excess of those heretofore appropriated therefrom:

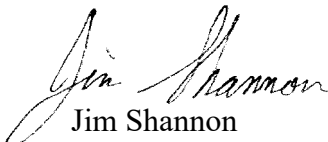
General Fund	\$74,326,016
Affordable Housing Impact Fee Fund	\$1,384,022
Airport Renewal and Replacement Fund	\$4,182,539
Airport Revenue Fund	\$50,126,009
Benefit Funds – Dental Insurance Fund	\$34,171
Benefits Funds - Life Insurance Fund	\$14,207
Benefits Funds - Self-Insured Medical Fund	\$342,534
Benefit Funds – Unemployment Insurance Fund	\$491,258
Branch Libraries Bond Projects Fund	\$6,630,517
Building and Structure Construction Tax Fund	\$9,262,047
Building Development Fee Program Fund	\$5,183,965
Cash Reserve Fund	\$14
City Hall Debt Service Fund	\$271,102
Citywide Planning Fee Program Fund	\$242,229
Community Facilities District Fund #1	\$135
Community Facilities District Fund #2 and #3	\$101,972
Community Facilities District Fund #8	\$53,049
Community Facilities District Fund #11	\$612
Community Facilities District Fund #13	\$20,016
Community Facilities District Fund #14	\$167,113
Community Facilities District Fund #16	\$47,693
Community Facilities District Fund #17	\$15,918
Community Facilities Revenue Fund	\$18,754
Construction and Conveyance Tax – Communications	\$737,813
Construction and Conveyance Tax – Council District 1	\$1,046,117
Construction and Conveyance Tax – Council District 2	\$464,093
Construction and Conveyance Tax – Council District 3	\$767,590
Construction and Conveyance Tax – Council District 5	\$933,431
Construction and Conveyance Tax – Council District 6	\$1,202,602
Construction and Conveyance Tax – Council District 7	\$2,047,463
Construction and Conveyance Tax – Council District 8	\$761,222
Construction and Conveyance Tax – Council District 9	\$1,148,030
Construction and Conveyance Tax – Council District 10	\$393,174

CERTIFICATION OF FUNDS

Construction and Conveyance Tax – Fire	\$1,570,073
Construction and Conveyance Tax – Library	\$10,063,683
Construction and Conveyance Tax – Parks Central	\$1,909,538
Construction and Conveyance Tax – Parks City-Wide	\$3,356,031
Construction and Conveyance Tax – Parks Yards	\$405,008
Construction and Conveyance Tax – Service Yards	\$1,259,440
Construction Excise Tax Fund	\$25,153,975
Contingent Lien District Fund	\$451,754
Convention and Cultural Affairs Capital Fund	\$622,910
Convention and Cultural Affairs Fund	\$511,988
Convention Center Facilities District Capital Fund	\$75,765
Convention Center Facilities District Revenue Fund	\$355,669
Edward Byrne Memorial Justice Assistance Grant Trust Fund	\$568
Emergency Reserve Fund	\$20,880,609
Emma Prusch Fund	\$33,730
Federal Drug Forfeiture Fund	\$215,355
Fire Development Fee Program Fund	\$1,354,376
General Purpose Parking Capital Fund	\$5,681,243
General Purpose Parking Fund	\$1,388,454
Gift Trust Fund	\$2,660,479
Homeless Housing, Assistance, and Prevention Fund	\$6,311,759
Housing Trust Fund	\$865,469
Ice Centre Expansion Bond Fund	\$14,086,620
Improvement District Fund	\$189
Inclusionary Fee Fund	\$357,984
Lake Cunningham Fund	\$149,413
Library Parcel Tax Capital Fund	\$764,099
Library Parcel Tax Fund	\$1,234,873
Low and Moderate Income Housing Asset Fund	\$9,466,566
Maintenance District Fund #1	\$72,785
Maintenance District Fund #5	\$17,434
Maintenance District Fund #11	\$104,477
Maintenance District Fund #13	\$2,107
Maintenance District Fund #15	\$74,515
Maintenance District Fund #18	\$57,230
Maintenance District Fund #20	\$8,967
Maintenance District Fund #21	\$6,396
Maintenance District Fund #22	\$335
Major Collectors and Arterials Fund	\$56,461
Measure T: Public Safety and Infrastructure Bond Fund	\$46,043,835
Multi-Source Housing Fund	\$11,466,819

CERTIFICATION OF FUNDS

Neighborhood Security Bond Fund	\$32,310
Parks and Recreation Bond Projects Fund	\$106,381
Planning Development Fee Program Fund	\$1,680,415
Public Works Development Fee Program Fund	\$1,392,060
Public Works Program Support Fund	\$1,110,702
Public Works Small Cell Permitting Fee Program	\$965,506
Residential Construction Tax Contribution Fund	\$408,556
San José Arena Capital Reserve Fund	\$4,001,748
San José Clean Energy Operating Fund	\$47,271,929
San José-Santa Clara Treatment Plant Capital Fund	\$5,141,177
San José-Santa Clara Treatment Plant Income Fund	\$35,704
Sanitary Sewer Connection Fee Fund	\$357,305
Sewage Treatment Plant Connection Fee Fund	\$250,859
Sewer Service and Use Charge Capital Improvement Fund	\$27,907,704
Sewer Service and Use Charge Fund	\$2,034,485
South Bay Water Recycling Capital Fund	\$12,471
South Bay Water Recycling Operating Fund	\$430,889
St. James Park Management District Fund	\$3,342,164
State Drug Forfeiture Fund	\$34,097
Storm Sewer Capital Fund	\$3,002,377
Storm Sewer Operating Fund	\$1,451,351
Subdivision Park Trust Fund	\$11,959,214
Supplemental Law Enforcement Services Fund	\$2,686,785
Transient Occupancy Tax Fund	\$1,675,578
Underground Utility Fund	\$1,208,872
Vehicle Maintenance and Operations Fund	\$371,042
Water Utility Capital Fund	\$1,213,179
Workforce Development Fund	\$323,563


Jim Shannon
Budget Director