



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Jennifer A. Maguire

**SUBJECT: UPDATES TO THE 2014-2015
PROPERTY TAX AND GENERAL
FUND BEGINNING FUND BALANCE
ESTIMATES**

DATE: May 29, 2014

Approved

Date 05-29-14

RECOMMENDATION

The following adjustments to the 2014-2015 Proposed Operating Budget of the General Fund are recommended:

1. Increase the Property Tax revenue estimate by \$5,400,000;
2. Increase the 2014-2015 Beginning Fund Balance estimate by \$3,000,000;
3. Eliminate the 2015-2016 Future Deficit Reserve in the amount of \$4,200,000;
4. Increase the Essential Services Earmarked Reserve by \$11,600,000; and
5. Increase the Contingency Reserve by \$1,000,000.

The following adjustments to the 2014-2015 Proposed Operating Budget of the General Purpose Parking Fund are recommended:

1. Increase the Estimate for Earned Revenue by \$3,363,151; and
2. Increase the Debt Service Payments Reserve by \$3,363,151.

BACKGROUND

The City Manager's Budget Office has continued to analyze and project funding sources for 2014-2015. Based on the updated information from the County of Santa Clara, received May 22, 2014, regarding property taxes and the latest analysis of projected fund balance at the end of 2013-2014, upward adjustments totaling \$8.4 million to the 2014-2015 Property Tax (\$5.4 million ongoing) revenue estimate and the 2014-2015 Beginning Fund Balance (\$3.0 million one-time) estimate are recommended. Budget actions are recommended to allocate these funds to the Essential Services Reserve and the Contingency Reserve. In addition, as part of these transactions, it is recommended that \$4.2 million of the ongoing Property Tax revenue be allocated on a one-time basis in 2014-2015, which would leave \$4.2 million ongoing starting in 2015-2016 to address the 2015-2016 General Fund shortfall projected in the 2015-2019 Five-Year Forecast issued in February 2014. This action would enable the elimination of the 2015-2016 Future Deficit Reserve of \$4.2 million that was included in the 2014-2015 Proposed Budget for this purpose. By eliminating this reserve, additional one-time funding of \$4.2 million would be available to allocate in 2014-2015, bringing the total amount of additional funds

May 29, 2014

Subject: Updates to the 2014-2015 Property Tax and General Fund Beginning Fund Balance Estimates

Page 2

available to \$12.6 million. In total, an increase to the Essential Services Reserve of \$11.6 million (\$1.2 million ongoing) and an increase of \$1.0 million to the Contingency Reserve are recommended as a result of these actions.

In addition, the 2014-2015 Proposed Operating Budget assumed that the Successor Agency to the Redevelopment Agency for the City of San José (“Successor Agency”) would have insufficient funds to complete the 4th/San Fernando debt service payment of \$3.4 million and the General Purpose Parking Fund would need to subsidize this payment. As outlined in the “Summary of the Successor Agency to the Redevelopment Agency Obligations and Risks to the City” section of the Proposed Operating Budget, beginning in 2012-2013, the City provided financial support to the Successor Agency as a result of insufficient redevelopment tax increment revenues that are eligible for either inter-year or intra-year reimbursements. Given the timing of the distribution of tax increment, the City may be required to provide cash flow loans as well as structural deficit loans in the event revenues are insufficient to cover all enforceable obligations.

With the updated information from the County of Santa Clara regarding the secured property roll growth for 2014-2015, an updated review of the Successor Agency projected 2014-2015 cash flow was completed. Based on this latest information, it is now projected that the Successor Agency will have sufficient tax increment to complete the debt service payment and the General Purpose Parking Fund will no longer need to provide a subsidy. Instead, the General Purpose Parking Fund will provide funding only for a cash flow loan with a reimbursement by the Successor Agency by the end of 2014-2015. This additional funding is recommended to be reserved in the Debt Service Payments Reserve.

ANALYSIS

General Fund

Following is additional detail regarding the proposed General Fund adjustments, including additional funding sources and the recommended use of those funds.

- **Property Tax** - On May 22, 2014, the City was provided the most recent Property Tax data from the County of Santa Clara Assessor’s Office regarding the 2014-2015 secured real property roll growth for the City of San José. Based on this latest information, secured property tax receipts in the City are projected to increase by approximately 6.2% in 2014-2015, which is up from the 3.5% growth assumed in the 2014-2015 Proposed Operating Budget based on previous information provided by the County. This new information will result in an increase in projected Secured Property Tax revenue of \$5.4 million (from \$209.8 million to \$215.2 million). Per the County, this additional growth reflects the continued full or partial restoration of property values that had previously been temporarily reassessed downwards under Proposition 8 due to declining market values, as well as continued growth in property values.

Proposition 8 provides that when the market value of a property declines below the previously established assessed value as of January 1 each year (lien date), the assessor is

required to proactively reduce the assessed value to reflect the lower market value. These most recent estimates reflect the programmatic update for the January 1, 2014 lien date for gross land and structural values only. Business personal property values and exemption values are based upon annual filings and are not available until roll closes on July 1 of each year and a number of residential and commercial properties will still require individual Proposition 8 review.

Approximately one-third of the properties in the City had received a Proposition 8 adjustment to their assessed value and continued to be under Proposition 8 valuation in 2012-2013. The County of Santa Clara Assessor's Office has been proactively reviewing and restoring, either partially or fully, the assessed value of properties that had received a Proposition 8 reduction. However, the impact of this work has not been available for property tax receipts until very late in the fiscal year as the work is in progress. For 2013-2014, over 30,000 properties were fully restored either due to the sale of the property or adjusted by the Assessor's Office resulting in the restoration of over \$5 billion to the City of San José's valuation. Additional restorations will occur again in 2014-2015, with an estimated restoration of \$2 billion to \$3 billion to the factored base year value in 2014-2015.

- **2013-2014 Ending Fund Balance/2014-2015 Beginning Fund Balance** - Based on the latest analysis of projected General Fund revenues and expenditures in 2013-2014, an upward adjustment of \$3.0 million to the 2014-2015 Beginning Fund Balance is recommended. Additional fund balance is available due to higher than estimated revenues in categories such as Property Tax, higher than estimated personal services savings in various departments as a result of continued vacancies, and additional small savings in various City-Wide Expenses appropriations.
- **2015-2016 Future Deficit Reserve** - The 2014-2015 Proposed Operating Budget recommended a one-time \$4.2 million 2015-2016 Future Deficit Reserve to temporarily address the projected ongoing shortfall outlined in the 2015-2019 General Fund Forecast issued in February 2014. As discussed above, it is recommended that \$4.2 million of the ongoing Property Tax revenue be allocated on a one-time basis in 2014-2015, which would leave \$4.2 million ongoing starting in 2015-2016 that is now recommended to address the 2015-2016 General Fund shortfall. This would resolve the shortfall ongoing rather than on a one-time basis, leaving the General Fund in a balanced position that year. This action would then enable the elimination of the 2015-2016 Future Deficit Reserve of \$4.2 million that was included in the 2014-2015 Proposed Budget for this purpose.
- **Essential Services Reserve** - An increase of \$11.6 million to the Essential Services Reserve, from \$2.0 million to \$13.6 million, is recommended and would be available for allocation by the City Council during the 2014-2015 budget process. Of this amount, \$1.2 million can be considered an ongoing funding source and includes the additional ongoing Property Tax revenue that was not set aside to address the projected 2015-2016 General Fund shortfall.
- **Contingency Reserve** - An increase of \$1.0 million to the Contingency Reserve, from \$31.5 million to \$32.5 million is recommended to ensure that the Contingency Reserve remains at

May 29, 2014

Subject: Updates to the 2014-2015 Property Tax and General Fund Beginning Fund Balance Estimates

Page 4

3% of the budget per City Council policy. With the projected increase in the 2014-2015 General Fund budget from additional funding sources and the rebudget of funds from 2013-2014 to 2014-2015 that were at a higher level than anticipated when the 2014-2015 Proposed Budget was developed, an increase to the General Fund Contingency Reserve is necessary.

General Purpose Parking Fund

Additional 2014-2015 actions in the General Purpose Parking Fund are recommended to reflect the revised property tax increment estimate for the Successor Agency per the most recent information provided by the County of Santa Clara Assessor's Office. As noted earlier, on May 22, 2014, the County of Santa Clara Assessor's Office issued updated estimates regarding the 2014-2015 secured real property growth for the Successor Agency, which are projected to increase by nearly 7% in 2014-2015. This figure is up from the 2.0% growth assumed in the development of the 2014-2015 Proposed Operating Budget. A revised cash flow of funds for 2014-2015 was completed for the Successor Agency, and should this higher growth be realized, it is estimated that only a cash flow loan will be necessary from the General Purpose Parking Fund as opposed to the current budgeted structural deficit subsidy. In order to reflect this change, an increase in the estimate for Earned Revenue is recommended for reimbursement from the Successor Agency by the end of 2014-2015, once sufficient tax increment revenues are received.

It should be noted that there are unknown factors related to the most recent projection from the County Assessor's Office that only reflects gross land and structural values for Secured Property Tax revenues. Business personal property values and exemption values are not included as they are based upon annual filing and are not available until July 1 of each year. Therefore, unsecured receipts are still unknown for former Redevelopment Agency property tax assessment regions and adjustments to the secured property tax assessed value continue to be evaluated through appeals and a number of both residential and commercial properties that require individual Proposition 8 review are still pending. In order to account for these uncertainties, the recommended reimbursement from the Successor Agency for the 4th/San Fernando debt service payment of \$3.4 million is recommended to be allocated to the Debt Service Payments Reserve in the event revised cash flow projections reflect insufficient revenues to cover this obligation.



JENNIFER A. MAGUIRE

Deputy City Manager/Budget Director