DATE: April 27, 2017

TO: Honorable Mayor and City Council

FROM: Patty J. Kong, Finance and Administrative Services Director
Daniel H. Rich, City Manager

TITLE: **Fiscal Year 2017-18 Narrative Budget Report**

STUDY SESSION MEMO

CITY OF MOUNTAIN VIEW

PURPOSE

This Study Session provides the City Council an opportunity to review and discuss the Fiscal Year 2017-18 Narrative Budget Report, which includes the City Manager's recommendations and is the foundation for the Proposed Budget. The Proposed Budget will be discussed by the City Council at public hearings on June 13 and June 20 and is scheduled for adoption after the public hearing on June 20, 2017.

The information in this report is for the following major funds: General Operating Fund (GOF), Development Services, Shoreline Golf Links, Shoreline Regional Park Community (Shoreline Community), Water, Wastewater, Solid Waste Management, and Reserves. For each fund, the report includes a current fiscal year status update of revenues, expenditures, and balance available, as well as budget recommendations for Fiscal Year 2017-18. To provide some context and assist with decisions that have longer-term implications, a Five-Year Financial Forecast (Forecast) for the GOF has been prepared and is included in this document.

BACKGROUND

The City is benefiting from the continued strong economy and high demand for development, resulting in significant property tax growth. The Assessed Value (AV) growth for the City is 12.0 percent year over year. This includes growth in property taxes resulting from new development being added to the tax role, as well as increases in AV from changes in ownership. Property Tax revenues for the City's General Operating Fund (GOF) are currently estimated to be 9.6 percent higher than the Fiscal Year 2016-17 adopted. Other revenue sources are also being fueled by the growing economy, unemployment continues to be very low, comparable to prior to the recession and lows for the past 50 years. Interest rates have remained at historical lows, with the Federal Reserve only taking recent actions to raise rates.

With that being said, the City's revenues are cyclical, and reflect the boom and bust of economic cycles. During the last recession, balancing the GOF was accomplished by strategically reducing expenditures, establishing more efficient operating models, and working closely with employee groups to contain employee compensation costs, as well as implementing limited revenue enhancements where appropriate. While the City has added positions back in recent years as the economy has improved, the City continues to operate with fewer staff than before the recession. Over the periods of retrenchment since Fiscal Year 2001-02, the City reduced approximately 70.0 positions or over 14.0 percent of its workforce in the GOF.

The City organization has found methods to improve efficiencies, to do more with less staff, but this has continued to place pressure on the organization. Therefore, to address some of the staffing needs within the City, there were a total of 22.5 positions, including limited-period positions, for all funds included in the Fiscal Year 2016-17 Adopted Budget; 4.0 of these are ongoing positions in the GOF.

Continuing to focus on adding resources where needed and to the extent the budget will allow, additional positions are recommended for Fiscal Year 2017-18. Several of the positions are currently limited-period positions that are being recommended to be ongoing. In some cases it has been difficult to recruit for limited-period positions, or limited-period employees leave the City for regular ongoing positions at other agencies. A Total of 10.75 net positions are recommended as ongoing positions and there are a net of 9.75 new personnel added. A summary of the positions recommended is as follows:

	GF	**Other Funds**	**Total Positions**
New Ongoing Regular	3.50	1.25	4.75
Limited-Period to Regular	1.00	5.00	6.00
Continuing Limited-Period	4.95	3.05	8.00[1]
New Limited-Period	2.00	3.00	5.00
Total	11.45	12.30	23.75[1]

[1] Does not include 2.0 FTE limited-period positions reimbursed by Google per the agreement that expires June 30, 2017.

The positions recommended are for almost all departments; however, about half of the resources being added or continued are development services related, for Community Development and Public Works, in response to the continued heavy workload.

The City is fortunate to be experiencing strong revenue growth; how long this will continue is unknown. Currently, local economists are not forecasting a downturn over the next 12 months, with certain caveats. However, recessions have generally occurred between 4 and 9 years in the past 5 decades, with the longest period of expansion lasting 11 years, from 1990 to 2001. It has been approximately 9.5 years since the beginning of the last recession and will be 11 years if the slowdown occurs in Fiscal Year 2018-19, when it is currently assumed in the City's Forecast.

The economic recovery is very extensive in the Bay Area, but the recovery is not prevalent everywhere in California or the rest of the country. Some would say the recovery has been very long and slow and, therefore, the next downturn could occur later. Although it is uncertain when the next economic slowdown will occur, based on history, it is certain there will be another recession sooner or later; therefore, it is assumed there will be a recession during the Forecast period.

EXECUTIVE SUMMARY

General Operating Fund

Fiscal Year 2016-17 revenues are estimated to exceed budget and expenditures are estimated below budget. This results in an estimated $18.9 million operating balance, prior to the contributions of $2.0 million each to the California Public Employees' Retirement System (CalPERS) and Retirees' Health Other Post-Employment Benefits (OPEB) to increase the funding status of these liabilities and transfers of $500,000 to the General Non-Operating Fund (GNOF) and $2.0 million to the Strategic Property Acquisition Reserve (SPAR). It is recommended the $12.4 million balance be used to fund limited-period expenditures, supplement reserves, and make additional contributions towards the City's unfunded liabilities.

It is fortunate the City is once again in a desirable position to be generating significant operating balances. It provides the opportunity to address some infrastructure needs and unfunded liabilities related to employee benefits, which were unable to be addressed during tough economic times. The overall funding status of CalPERS has declined over the past decade due to the CalPERS fund's investment losses, demographic assumption changes, etc., and CalPERS continues to work towards raising the funding level of pension benefits. However, this generally translates into higher rates for agencies. In light of the latest CalPERS reduction in the discount rate used for pension obligations, which will severely increase the City's contributions, staff is recommending a strategy to reduce the City's unfunded pension liability (see Attachment 1).

Fiscal Year 2017-18 revenues are projected to continue to rise to $128.0 million and expenditures are projected at $117.6 million (including recommendations). Revenues are at a level sufficient to fund expenditures and additional funding of $2.0 million each toward the OPEB liability and transfer to SPAR, with an additional $4.0 million contribution to CalPERS (for a total of $10.0 million, including the additional $6.0 million discussed in Attachment 1). There is a projected balance of $2.4 million. Recommendations include non-discretionary increases, as well as discretionary increases in high-priority areas. As in the past, $1.8 million of budget savings is built into the budget.

In the Forecast, revenues are projected to continue growing; however, the Forecast assumes a recession will occur during the five-year period. It is unknown exactly when a recession will occur, but staff has incorporated the impact of a recession beginning in Fiscal Year 2018-19 as that would match the longest economic expansion in decades. At that point, the projected operating balance declines and modest deficits are projected in Fiscal Years 2020-21 and 2021-22.

Items for City Council Discussion and Direction

In addition to the direction on the recommendations in this report, there are a few specific items staff would like direction on regarding whether these are items that should be included in the Fiscal Year 2017-18 Proposed Budget. This section can be found at the end of the General Operating Fund. Staff would also like direction from Council on the options related to additional funding towards the City's unfunded pension obligation, potential capital projects funding, and credit card processing fees (see Attachments 1 and 9).

Other Major Funds

- Development Services: Development activity for Fiscal Year 2016-17 remains strong and is anticipated to continue into the upcoming fiscal year. The Development Services Fund (DSF) is able to meet its current financial obligations, however, revenues are received in advance of the services provided; therefore, a significant balance should be maintained in the fund for these services and to continue operations during the next slowdown in development activity.

- Shoreline Golf Links (SGL): Course conditions continue to improve and both revenues and expenditures are below budget for Fiscal Year 2016-17. For Fiscal Year 2017-18, revenues are projected to be higher than the current fiscal year estimated and the surplus balance is projected at $125,000, $25,000 less than the current fiscal year.

- Shoreline Regional Park Community (Shoreline Community): Fiscal Year 2016-17 revenues are estimated to be $4.1 million higher than the Adopted Budget, primarily related to changes in ownership and new development added to the tax role. Fiscal Year 2016-17 estimated expenditures are essentially on target with budget. Fiscal Year 2017-18 operating revenues are projected with an increase over the current fiscal year adopted, but less than estimated as unsecured values and supplemental taxes are projected to decline. Fiscal Year 2017-18 operating expenditures are higher than the Fiscal Year 2016-17 adopted due to increases in operating expenses and projected intergovernmental payments, partially offset by lower debt payments. Future major capital projects related to transportation are proposed to be funded through the new development impact fee adopted by Council in February 2016 and the potential issuance of debt.

Utility Funds

- Water Fund: The financial position of this fund has been severely impacted by reduced water sales from conservation efforts due to the drought. However, for the current fiscal year, water usage is trending 7.0 percent higher. This is having a positive impact, but not enough to overcome the 30.0 percent reduction in usage in the prior two fiscal years. For the upcoming fiscal year, the San Francisco Public Utilities Commission (SFPUC) is currently proposing no wholesale water rate increase, and the Santa Clara Valley Water District (SCVWD) is proposing 9.0 percent and 9.9 percent increases for treated water and well water, respectively. **A 7.0 percent rate increase is recommended**, 1.0 percent to fund the increased cost of water and operating expenditures, and 6.0 percent because of the low water usage. The additional 6.0 percent was noticed and approved at the rate hearing on June 21, 2016.

- Wastewater Fund: The financial position of this fund has been severely impacted by unforeseen Palo Alto Regional Water Quality Control Plant (Treatment Plant) costs of $1.3 million in Fiscal Year 2015-16. This in addition to a 25.9 percent increase in Treatment Plant costs for Fiscal Year 2016-17 would have required a rate increase of 26.0 percent in order to bring revenues and expenditures into balance. Instead, staff recommended a 19.0 percent increase for Fiscal Year 2016-17, spreading the remaining increase needed over the following two fiscal years, 6.0 percent in each fiscal year, and using half of the rate stabilization reserve. For Fiscal Year 2016-17, revenues and expenditures are trending lower than budgeted, and the financial position has improved slightly.

  For Fiscal Year 2017-18, the Treatment Plant is currently proposing a 1.9 percent increase in treatment costs, which along with operating cost increases result in a 2.0 percent rate increase. This combined with the additional 6.0 percent and the additional 2.0 percent rate increase (the fourth year of 10 years) recommended to gradually increase rates to pay for major capital improvements at the Treatment Plant, both noticed and approved at the rate hearing on June 21, 2016, result in a

total rate increase recommended for Fiscal Year 2017-18 of 10.0 percent. Staff is also reviewing the major City infrastructure projects that are needed and the possible necessity of issuing debt.

- Solid Waste Management Fund: For Fiscal Year 2016-17, revenues are trending higher than budgeted and expenditures are trending less than the Adopted Budget. For Fiscal Year 2017-18, a 4.95 percent increase for Recology, no increase for the SMaRT® Station, as well as City operating cost increases and annual maintenance projects result in an overall 2.0 percent recommended increase to rates. In addition, the third and final year phase-in of cart rates resulting from the Cost of Service Study is recommended to be reduced to 8.0 percent, resulting in a **total recommended cart rate increase of 10.0 percent**. The residential food scraps program has been approved to be implemented in July 2017; however, the associated cart rate increase is recommended to be deferred until Fiscal Year 2018-19 in order to keep the cart rate as low as possible.

Non-Major Funds

There are recommendations for Non-Major funds and these are highlighted after the discussion of the Utility Funds, under the Other Major Funds Section.

Reserves

Most reserves are at their target or policy balance. Staff is recommending some reserve funds be considered towards addressing the City's pension obligation (see Attachment 1). It is recommended that $6.0 million from the Fiscal Year 2016-17 carryover and $4.0 million from the Fiscal Year 2017-18 GOF along with the proportionate share of Other Funds be contributed for a total of $12.3 million. Depending on which CalPERS funding option the Council directs, any remaining GOF carryover balance is recommended to be transferred to either the Capital Improvement Reserve or towards OPEB funding. Should the balance exceed the amount recommended, staff will return to Council for approval of the allocation of additional funds.

Next Steps

Based on the feedback provided by the City Council at the Narrative Budget Report (NBR) Study Session, staff will prepare the Proposed Budget to be presented to City Council at a public hearing on June 13, 2017. The Proposed Budget is scheduled for adoption after the public hearing on June 20, 2017.

DISCUSSION

GENERAL OPERATING FUND

The GOF is the single largest City fund and provides funding for core services, including Police, Fire, Parks, Recreation, Library, Planning, Public Works, and Administration. The City's financial health is shaped in large part by economic forces beyond our control. Revenues fluctuate with the economic climate of the Bay Area. During the dot-com boom, City revenues, especially Sales Tax revenue, increased significantly and just as significantly declined with the dot-com bust. During this past recession, due primarily to declines in Property Taxes, Sales Taxes, and Transient Occupancy Tax revenues, the GOF faced structural deficits (before corrective actions were taken) for four consecutive fiscal years. By addressing these structural deficits on an ongoing basis, the City was able to position itself for revenue growth with the economic recovery. In addition, the City's sound fiscal practices and budget discipline have allowed the City to maintain its AAA credit rating, a status few other California cities can claim.

Building on this strong financial foundation and with the continuation of revenue growth, this report provides the recommendations for the General Operating Fund budget for Fiscal Year 2017-18. The updated projections indicate continued strength in the economic environment throughout the Forecast. There is often a lag time from the time a development is completed, the property is placed onto the tax roll, and the City receives the associated property taxes.

Updated General Operating Fund Status for Fiscal Year 2016-17

Staff has continued to monitor General Operating Fund revenues and expenditures for the current fiscal year. As we progress through the fiscal year, estimates are refined and have a greater level of confidence, but the final numbers will not be available until after the close of the fiscal year. A comparison of estimated amounts to budget for the GOF follows (dollars in thousands):

	2016-17 Adopted Budget	2016-17 Adjusted Budget[1]	**2016-17 Estimated**	Variance of Estimated to Adopted Budget
Revenues	$118,718	119,262	**125,018**	6,300
Expenditures	(108,433)	(110,571)	**(106,108)**	2,325
Operating Balance	10,285	8,691	**18,910**	8,625
Transfer to GNOF	(500)	(500)	**(500)**	-0-
CalPERS Contribution	(2,000)	(2,000)	**(2,000)**	-0-
OPEB Contribution	(2,000)	(2,000)	**(2,000)**	-0-
Transfer to SPAR	(2,000)	(2,000)	**(2,000)**	-0-
Rebudgets	-0-	1,937	**-0-**	-0-
Ending Balance	$ 3,785	4,128	**12,410**	8,625

(1) The Adjusted Budget includes the Adopted Budget; any encumbrance and grant/donation carryovers from the prior fiscal year; increases for reimbursed expenditures, grants, and donations; and any budget changes approved through February by Council for the current fiscal year.

Overall, total revenues for Fiscal Year 2016-17 are currently estimated to be $6.3 million, or 5.3 percent higher than adopted revenues. Of the GOF major revenue sources, only Other Local Taxes and Licenses, Permits and Franchise Fees/Fines and Forfeitures are estimated below budget while all other revenue categories are estimated to be performing better than expected this fiscal year.

On the expenditure side, total operating expenditures for Fiscal Year 2016-17 are estimated to be $4.5 million, or 4.0 percent, lower than the Adjusted Budget and $2.3 million lower than the Adopted Budget. After accounting for higher revenues, the operating balance is estimated to be $12.4 million this fiscal year compared to the $3.8 million budgeted. This is a slight improvement in revenues from the estimates provided in the Midyear Report, where the operating balance was estimated at $12.1 million

Although we expect the City will end the current fiscal year with an operating balance greater than budgeted, it is important to note the carryover balance is the funding source for key organizational needs, such as limited-period expenditures, maintaining reserve levels, funding one-time capital projects, and when available contributions towards unfunded liabilities.

After the $2.0 million contribution each to CalPERS, OPEB, and SPAR included in the Fiscal Year 2016-17 Adopted Budget, the estimated Fiscal Year 2016-17 carryover balance of $12.4 million (subject to changes in assets and liabilities and grants/ donations carryovers) is available to fund a net $2.7 million of limited-period, $351,500 of capital outlay expenditures, and other recommendations.

It is recommended the City contribute an additional $6.0 million to CalPERS from the carryover and possibly other reserves, depending on Council direction, for a lump sum payment to CalPERS to pay down the City's unfunded pension liability (see Attachment 1). Any remaining carryover available, depending on the option chosen by Council, is recommended to supplement the Capital Improvement Reserve or as a contribution to the City's OPEB obligation. The final carryover available will be determined after the fiscal year-end close and audit of the City's financial records.

The Reserve Section of this report has additional information and detail related to Reserves.

General Operating Fund Projections for Fiscal Year 2017-18

In presenting the Preliminary GOF revenues and expenditures in the Midyear Budget Status Report on February 14, 2017, staff projected a $3.8 million surplus for Fiscal Year 2017-18. With additional information available on both revenues and expenditures as the fiscal year has progressed and the addition of budget recommendations, the updated projection is a surplus of $2.4 million or 1.9 percent of projected revenues. This surplus is after recommendations for expenditure increases, includes $1.8 million of budget savings, as well as additional contributions to CalPERS, OPEB, and SPAR. A brief discussion of revenues and expenditures for Fiscal Year 2017-18 follows.

Compared to the current Adopted Budget and including recommendations, total revenues are anticipated to grow by $9.3 million, or 7.8 percent, next fiscal year, and total expenditures are projected to increase $9.2 million or 8.5 percent.

Comprehensive information for revenues and expenditures is included in the GOF Five-Year Forecast Section included in this document. A comparison of the prior fiscal year audited, current fiscal year adopted and estimated, and the upcoming fiscal year recommended follows (dollars in thousands):

	2015-16 Audited	2016-17 Adopted Budget	2016-17 Estimated	**2017-18 Recommended**	Variance of 2017-18 Recom-mended to 2016-17 Adopted
Revenues	$115,911	118,718	125,018	**128,022**	9,304
Expenditures	(99,590)	(108,433)	(106,108)	**(117,626)**	(9,193)
Rebudgets[1]	(4,078)	-0-	-0-	**-0-**	-0-
Operating Balance	12,243	10,285	18,910	**10,396**	111
Transfer to GNOF	(6,995)	(500)	(500)	**-0-**	500
Transfer to General Fund Reserve	(2,248)	-0-	-0-	**-0-**	-0-
CalPERS Contribution	(2,000)	(2,000)	(2,000)	**(4,000)**	(2,000)
OPEB Contribution	(1,000)	(2,000)	(2,000)	**(2,000)**	-0-
Transfer to SPAR	-0-	(2,000)	(2,000)	**(2,000)**	-0-
Ending Balance	$ -0-	3,785	12,410	**2,396**	(1,389)

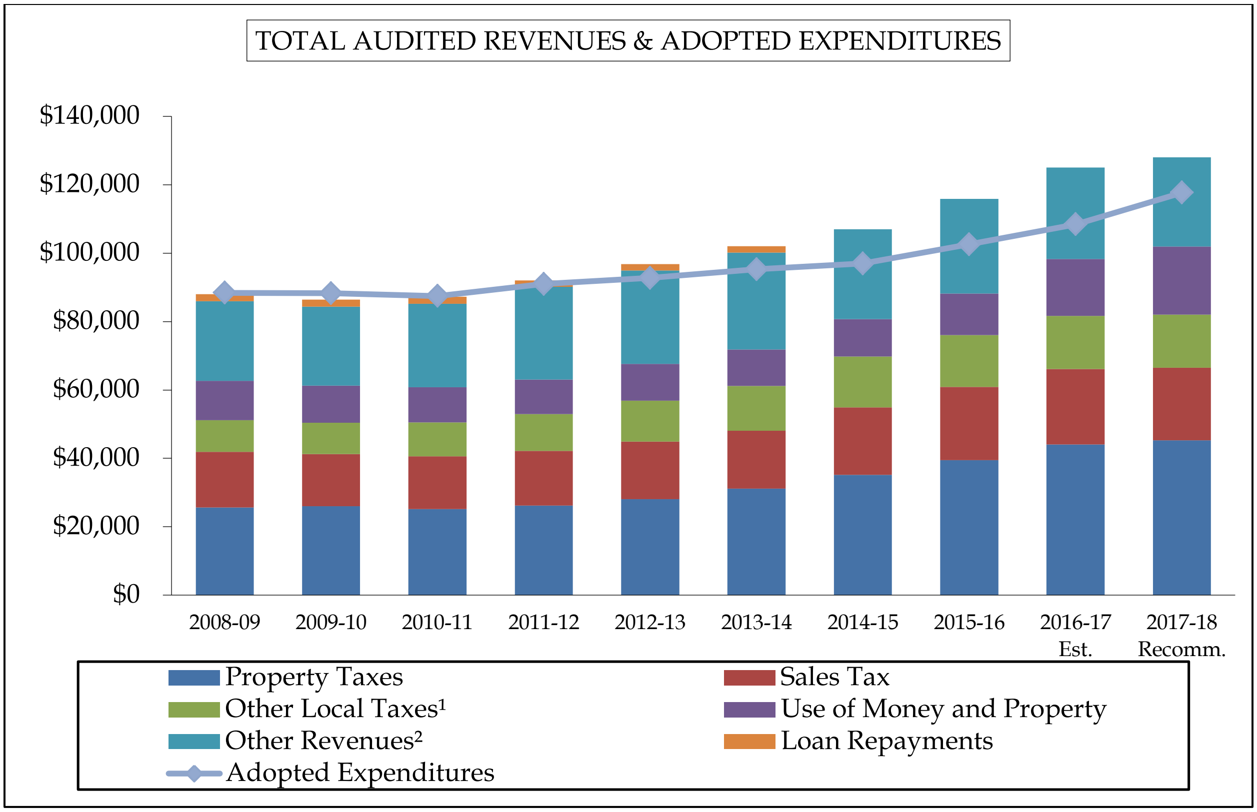
A summary of the Fiscal Year 2017-18 budget is as follows (dollars in thousands):

Total Revenues	$128,058
Total Net Expenditures	(115,362)
Recommendations:	
Non-Discretionary	(1,034)
Discretionary Increases	(1,230)
Revenue Changes	(36)
Operating Balance	10,396
CalPERS Funding	(4,000)
OPEB Funding	(2,000)
SPAR Funding	(2,000)
Net Balance	$ 2,396

Revenue Projections for Fiscal Year 2017-18

For Fiscal Year 2017-18, GOF revenues are projected to grow by 7.8 percent compared to the current fiscal year adopted, to $128.0 million, including recommendations. Most major categories of revenues (e.g., Property Tax, Sales Tax, etc.), are projected with increases. A few major revenue categories (Other Local Taxes and Miscellaneous Revenues), are projected comparable to, or slightly less than, the current fiscal year adopted revenues. More detail on each revenue source can be found in the Forecast.

The City's recent revenue history and estimated revenues for the current fiscal year and projected revenues for the upcoming fiscal year are as follows (dollars in thousands):



[1] Other Local Taxes is comprised of Transient Occupancy Tax, (TOT), Utility Users Tax (UUT), and Business Licenses.
[2] Other Revenues is comprised of Licenses, Permits & Franchise Fees, Fines & Forfeitures, Intergovernmental, Charges for Services, Miscellaneous, and Interfund Revenues/Transfers.

This table demonstrates the cyclical nature of the City's balance between revenues and expenditures. In recessionary years, small margins existed between GOF revenues and expenditures, while that gap widens during high-revenue-growth years as we are currently experiencing. The adopted expenditures in the table include the budget savings adopted; however, for Fiscal Years 2008-09 through 2010-11, the actual budget saving results were greater than adopted and were necessary to maintain a positive operating balance due to revenue shortfalls compared to budget. In comparison, for Fiscal Year 2011-12 through Fiscal Year 2014-15, actual budget savings have declined, but revenues have been greater than adopted.

Recommendations regarding new fees and increases to current fees are included with this report (see Attachment 2).

Expenditure Projections for Fiscal Year 2017-18

The recommended expenditures for Fiscal Year 2017-18 include the addition of $1.0 million of non-discretionary increases, which preserves current service levels, and $1.2 million discretionary additions for resources to meet demands and reduce some of the strain on staff.

While several new expenditure requests by departments are being recommended, there were more requests by departments for ongoing expenditure increases, many of which would be desirable and would ease more of the stress on staff. However, as can be seen in the Forecast and summarized below, although more expenditures could be afforded in the Fiscal Year 2017-18 Budget, it is recommended to only add expenditures that are generally sustainable through the next economic recession, when the GOF could be once again facing an operating deficit, requiring budget reductions to maintain a balanced GOF. To address heavy workloads, many current demands for resources are being addressed through limited-period funding.

Although service levels are generally not increasing, the City's costs are increasing. As a service organization, approximately 80.0 percent of expenditures are for personnel. Total costs of personnel are increasing $5.2 million. Although there were structural changes adopted Statewide with pension reform in 2012, retirement costs are still projected to increase by $1.6 million for Fiscal Year 2017-18 over the current fiscal year Adopted Budget. The changes resulting from pension reform will likely not be realized for 10 years or more, until there are a majority of employees under the new formula.

The categories of changes in costs from the Fiscal Year 2016-17 Adopted Budget to the Fiscal Year 2017-18 recommended budget are as follows (dollars in thousands):

Expenditure Changes:		
Compensation Changes	$1,481	
Retirement (CalPERS)	1,590	
Health and Other Benefits	820	
New Personnel Recommendations	1,274	
Total Changes Personnel Costs		5,165
Nonpersonnel Recommendations		990
Other Recommendations		3,038
Total Expenditure Increase		$9,193

All labor contracts and resolutions expire June 30, 2017, so precise personnel expenditures are not know at this time. As the City transitioned open enrollment for health care to a calendar year, new premiums are effective each January 1. The premiums budgeted for Fiscal Year 2017-18 are actual rates through December 2017 and assume an increase of 6.0 to 10.0 percent, depending on the plan for medical, and 2.0 percent for dental beginning January 2018. CalPERS rates are budgeted based on the actuarial rates provided by CalPERS.

Other recommendations of $3.0 million include increases to Capital Outlay, Equipment Replacement, Self-Insurance, Transfers, and Fleet. Most of this increase, $2.7 million, is for recommended transfers for additional funding to the Budget Contingency and Capital Improvement Reserves (See Reserves Section).

California Public Employees Retirement System (CalPERS) Rates

There has been attention focused on public-sector retirement costs in recent years; therefore, it is worth noting a few key points about Mountain View's approach to providing employee pension benefits. While in many cities the employer pays some or all of the employee contribution, Mountain View employees not only pay the employee contribution, but they also pay a portion of the employer contribution. For example, the amount paid by Safety employees ranges between 13.6 percent and 17.4 percent and for Miscellaneous employees ranges between 10.5 percent and 11.7 percent. This was an unusual and progressive arrangement when instituted in Mountain View and reflects the collaborative approach our employees have taken toward fiscal sustainability.

As a result of the significant financial losses to CalPERS during the recession and the resulting impacts to the financial sustainability of the pension plans, many changes in the way CalPERS rates are calculated have been adopted in the past several years, including the reduction in the discount rate from 7.75 percent to 7.50 percent and now to 7.0 percent, changes to the methodology for the amortization and smoothing of rates, and the changes in demographic assumptions, primarily related to life expectancy. All of these have an impact on the City's employer rates and there are increases projected in CalPERS rates throughout the Forecast period as discussed in more detail in the Forecast (see also Attachment 1).

Fiscal Year 2017-18 Budget Recommendations

The following is a discussion of non-discretionary and discretionary recommended expenditure increases. Departments have reviewed their programs, work levels, and preliminary goals for the upcoming fiscal year and developed their budget requests. Goals could be changing based on Council direction. The Citywide non-discretionary increase is primarily related to the City's minimum wage, information technology, contractual services, and utility cost increases. The discretionary items are based on requests made by departments that have been reviewed by the City Manager and are recommended for City Council consideration. These recommendations are included in the Fiscal Year 2017-18 numbers presented.

Non-Discretionary Increases

Non-discretionary increases totaling $1.0 million are recommended to fund existing and new required operational costs such as increases in the City's minimum wage, information technology costs, utility costs, PG&E, and contract services. Items recommended in the base budget, $25,000 and over, are as follows (see Attachment 3 for a complete listing, with descriptions, of non-discretionary items):

- **Microsoft Office/Email Licensing:** $220,000
- **City Utility Costs:** $200,000
- **Minimum Wage Impact 1/2-Year (Community Services):** $170,000
- **Janitorial Cost Increases for City Facilities:** $91,200
- **Microsoft Windows/SQL Server Licensing:** $80,000
- **PG&E Cost Increase:** $66,200
- **Information Technology Licenses and Maintenance:** $42,600
- **Annual Medical Surveillance Exams:** $36,000
- **Minimum Wage Impact 1/2-Year (Library Services):** $30,000
- **KMVT Contract:** $25,000

Discretionary Recommendations

New expenditures totaling $1.2 million are recommended for high-priority ongoing programs; $1.1 million is related to positions. A listing of recommended items, $25,000 and over, are as follows (see Attachment 4 for a complete listing, with descriptions, of discretionary items):

- **Information Technology Analyst I/II Position:** $169,000
- **Transportation Manager Position (0.75):** $149,600 (the salary for this position is subject to review)
- **Fire Overtime—Hiring Retention and Training:** $140,000
- **Tree Trimmer III Position:** $139,800
- **Reclassification of Six Firefighter Positions to Paramedic Level, Changing the Authorized Level of Paramedics from 21 to 27:** $116,100
- **Lead Public Safety Dispatcher Position (0.50):** $98,900
- **Silicon Valley Clean Energy (SVCE) 100 Percent Renewable Energy:** $80,000
- **Human Resources Technician Position (0.50):** $59,000
- **FASD Customer Service Representative Position (0.50):** $57,600
- **Geographic Information System (GIS) Data Conversion Services:** $(50,000) (offset by reduction in revenue of $50,000)
- **Library Materials:** $40,000
- **CMO Office Assistant Wages:** $36,800
- **Lease of Officer-Worn Cameras (44):** $35,000

Limited-Period Recommendations

Limited-period funding totaling $2.7 million ($2.8 million offset by $116,400 in revenue) is recommended; $1.9 million is related to positions, much of which is a continuation of current staffing. A listing of items recommended as limited-period expenditures

$25,000 and over are as follows (see Attachment 5 for a complete listing, with descriptions, of limited-period items):

- **Fire Special Operations Program:** $500,000 (see Attachment 6)
- **Police Officer Position (two year)—Community Outreach:** $221,300 (offset by $116,400 State grant)
- **Associate Civil Engineer—Capital Projects Section Position*:** $183,700
- **Human Resources Analyst I/II Position*:** $156,800
- **Firefighter Recruit Academy:** $150,000
- **Transfer to the Community Stabilization Fair Rent Act (CSFRA) Fund:** $150,000
- **ICMA Fellow Position*:** $134,600
- **Senior Deputy City Attorney Position (0.50):** $101,600
- **Associate Civil Engineer—Traffic Section Position (0.45)*:** $82,700
- **Employee Transportation Program:** $80,000
- **Human Resources Analyst Wages:** $80,000
- **Administrative Analyst I/II Position—Environmental Sustainability (0.50):** $76,600
- **Employee Engagement and Appreciation Program:** $75,000
- **Performing Arts Supervisor Position (0.50)*:** $69,500
- **IT Secretary Position (0.50)*:** $67,900
- **PW Program Assistant—Engineering Division Position (0.50)*:** $64,900
- **PW Hourly Staff to Support the Traffic Section:** $60,000
- **Pilot Program for Sidewalk Ramping and Grinding:** $46,000
- **Workplace Investigations:** $45,000

- **Hourly Staff to Support the Capital Projects Section:** $40,000

- **Labor Negotiations:** $35,000

- **Wellness Program:** $35,000

- **Sustainability Outreach and Engagement Program:** $30,000

- **Automatic Locks and Installation for Park Restrooms:** $28,000

- **Placeholder for New City Council Goal Related to Vulnerable Populations:** $25,000

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*represents a continuing limited-period position

Listings of Fiscal Year 2017-18 Recommended Capital Outlay and Equipment Replacement are included as Attachments 7 and 8, respectively.

Items for City Council Discussion and Direction

As discussed in this report, there are a few items staff is requesting Council direction on as follows:

- CalPERS Discount Rate Change Funding Strategy

  CalPERS has adopted a reduction in the discount rate used for the calculation of the City's pension obligation. This will result in projected increases being phased in the City's annual pension expense beginning in Fiscal Year 2018-19 of approximately $684,000 and projected to rise to $8.6 million annually after full implementation. Staff is recommending two strategies of payments to pay down this unfunded liability. The first strategy is a one-time payment of $10.0 million from the General Fund in Fiscal Year 2017-18 (see Attachment 1).

- Google Amphitheatre Parking Revenue

  Currently, Google subleases Parking Lots C and D from SFX (Live Nation) and this agreement ends mid-December 2017. In March 2017, the City Council approved Google's request for a three-year extension of the sublease through December 2020 for a $600,000 one-time payment to the City, which was received in early April 2017. The $600,000 is recommended to be transferred to the Capital Improvement

Reserve. It is anticipated the Certificate of Occupancy for the Charleston East development will be issued before the end of the three-year period and commencing no later than January 1, 2021, Google will begin a five-year lease of the parking lots starting at approximately $2.3 million annually (with 4.0 percent annual increases).

As this is limited period revenue, another recommended strategy to pay down the City's unfunded pension liability is to use $2.0 million annually of this revenue received from Google over the five years of the lease for an additional $10.0 million contribution to CalPERS (see Attachment 1).

- Credit Card Processing Fees

  At the February 14, 2017 Mid-Year Budget meeting, Council requested staff to review options for the costs associated with processing fees on credit card transactions. Staff has reviewed and evaluated options (see Attachment 9).

- Community Health Awareness Council (CHAC) Request:

  Staff has included a 3.0 percent increase for CHAC. CHAC has submitted a request for a 10.0 percent increase (see Attachment 10). The current funding of CHAC is $94,800.

- Council's Budget:

  The Council Procedures Committee (CPC) met on April 4, 2017 to discuss the Council's Budget in accordance with the revised Council Policy A-2. The CPC recommended the following:

  - An allowance of $70 per month for cell phone and data plans to be paid to Councilmembers on a semiannual basis. This would come from each Councilmember's existing communications budget.

  - Replacement of the table and chairs in the Committee Room. The table does not accommodate the full Council to sit at one time. Staff is estimating up to $3,000 for a new table and chairs.

SUMMARY

With the strong economic growth, combined with fiscally responsible actions taken in prior fiscal years, the City is poised to invest funds in needed areas such as additional staff, capital projects, CalPERS, and Retirees' Health. The growing economy has resulted in overall revenues projected to increase 7.8 percent over the Fiscal Year 2016-17 Adopted Budget. This results in the ability to include non-discretionary expenditure increases of $1.0 million and discretionary increases of $1.2 million of ongoing expenditures in the most needed areas, as well as a net $2.7 million in limited-period expenditures. The recommendations include 23.75 positions, and a net of 9.75 new staff.

The net result of the recommendations is a projected GOF surplus for Fiscal Year 2017-18 of $2.4 million after recommended contributions of $4.0 million to CalPERS, and $2.0 million each to OPEB and SPAR. Further ongoing expenditure increases are not recommended at this time, based on the assumption of a slowdown in the economy in later years, leading to modest deficit balances in the outer years.

OTHER MAJOR FUNDS

General Fund: Development Services Fund

Development Services is a General Fund program, separated from the GOF in order to facilitate better tracking and accounting. This separation was established to allow for an effective way to match revenues and expenditures. Initially created for Building Services, for Fiscal Year 2014-15 this definition was expanded to more fully encompass all development activity.

For the current fiscal year, development activity continues to remain strong. The revenue estimate for Fiscal Year 2016-17 is $15.3 million, $3.5 million higher than adopted and $1.1 million higher than the prior fiscal year audited. Development-related revenues are cyclical in nature and there is a timing difference for each project as plan check revenue is collected at the beginning of the development process and permit revenue just prior to construction; all services are provided subsequent to the payment of fees.

Operating expenditures for the current fiscal year are estimated at $13.5 million, $1.1 million (9.0 percent) higher than the Adopted Budget, primarily as a result of encumbrances carried over from the prior fiscal year. Included in operating expenditures is $1.6 million to reimburse the cost of administrative support by the GOF. In addition, Development Services contributed $754,000 for its share of the Retirees' Health unfunded actuarial accrued liability (UAAL), $239,000 to CalPERS, proportionate to the General Fund contributions, $66,000 to the Compensated Absences Fund, and funded capital projects of $552,000. The contribution to the Retirees' Health UAAL is less than budgeted due to the reevaluation of the contribution based on employees in the defined benefit versus the defined contribution plan. The fund is estimated to end the current fiscal year with a balance of $10.5 million and a Reserve for Land Use Documents of $4.5 million. The Land Use Document Fee was approved with the Fiscal Year 2015-16 Adopted Budget to establish this reserve for the purpose of accumulating costs associated with the update of Land Use Documents (e.g., General Plan, Precise Plans, Zoning Ordinance, etc.).

A comparison of the prior fiscal year audited, current fiscal year adopted and estimated, and the upcoming fiscal year recommended follows (dollars in thousands):

	2015-16 Audited	2016-17 Adopted	2016-17 Estimated	2017-18 Recommended
Revenues:				
Investment Earnings	$ 178	201	190	206
Permits	6,410	6,100	6,428	5,621
Charges for Services	7,551	5,424	8,663	6,353
Other	46	50	27	20
Total Revenues	14,185	11,775	15,308	12,200
Operating Expenditures	10,528	12,389	13,504	13,586
Operating Balance (Deficit)	3,657	(614)	1,804	(1,386)
Land Use Documents	523	840	818	800
CalPERS Contribution	(177)	(239)	(239)	(689)
Transfer to Workers' Comp	(15)	-0-	-0-	-0-
Transfer to Comp Absences	(12)	(66)	(66)	(22)
Retirees' Health UAAL	(2,748)	(1,754)	(754)	-0-
Capital Projects	(1,870)	(552)	(552)	(40)
Excess (Deficiency) of Revenues	(642)	(2,385)	1,011	(1,337)
Beginning Balance	14,588	13,946	13,946	14,957
Land Use Doc Reserve	(3,679)	(4,519)	(4,497)	(5,297)
Ending Balance	$10,267	7,042	10,460	8,323

The Fiscal Year 2017-18 recommendations total $2.3 million. There are no non-discretionary increases.

Discretionary Recommendations

New expenditures totaling $1.0 million are recommended for high-priority ongoing programs; $1.0 million is related to positions. A listing of recommended items, $25,000 and over, are as follows (see Attachment 4 for a complete listing, with descriptions, of discretionary items):

- **Senior Civil Engineer—Land Development Position*:** $199,400
- **Associate Civil Engineer—Construction Position*:** $183,700
- **Senior Planner Position*:** $176,500
- **Associate Planner Position*:** $163,000
- **Associate Planner Position:** $163,000
- **Associate Civil Engineer—Land Development Position (0.50)*:** $91,900
- **Digital Imaging of Building and Fire Permits:** $50,000 (offset by $50,000 in fees)

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*represents a position going from limited-period to ongoing

Limited-Period Recommendations

Limited-period funding totaling $1.3 million is recommended; $620,000 is related to positions; most is a continuation of current staffing. A listing of items recommended as limited-period expenditures $25,000 and over are as follows (see Attachment 5 for a complete listing, with descriptions, of limited-period items):

- **Consultants to Support Land Development Section:** $300,000
- **Consultants to Support Construction Section:** $200,000
- **Associate Civil Engineer—Construction Position*:** $183,700
- **Associate Planner Position:** $163,000

- **Consultants to Support Traffic Engineering Section:** $100,000
- **Two Associate Civil Engineer—Land Development Positions (0.40):** $73,500
- **Program Assistant—Engineering Division Position (0.50)*:** $64,900
- **Digital Imaging of Building Permits:** $60,000
- **Associate Civil Engineer—Traffic Section Position (0.30)*:** $55,100
- **Hourly Staff to Support the Land Development Section*:** $40,000
- **Hourly Staff to Support the Construction Section*:** $40,000
- **Cost of Service Study:** $40,000

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*represents a continuing limited-period position or hourly staff

Fiscal Year 2017-18 revenues are projected at $12.2 million, $425,000 higher than the current fiscal year Adopted Budget, and $3.1 million lower than the current fiscal year estimate. Development is projected to remain strong through Fiscal Year 2017-18, but the timing of project approvals and payment of fees is difficult to project. Fiscal Year 2017-18 operating expenditures are recommended at $13.6 million, $1.2 million more than the current fiscal year Adopted Budget. There are limited-period recommendations of $1.3 million and ongoing recommendations of $1.0 million (all primarily targeted to address workload during this high period of development activity) included for Fiscal Year 2017-18. In addition, there is a $689,000 contribution to the CalPERS liability proportionate to the General Fund contributions, $22,000 to the Compensated Absences Reserve, and $40,000 for capital projects.

The fund is projected to end the 2017-18 fiscal year, including recommendations of $2.3 million, with operating expenditures exceeding revenues by $1.4 million. After funding the additional CalPERS contribution, Compensated Absences, and capital projects, there is a projected ending balance of $8.3 million and a Reserve for Land Use Documents of $5.3 million. A balance in this fund is necessary to fund the expenditures that are incurred subsequent to payment of the associated fees.

<u>General Fund: Shoreline Golf Links Fund</u>

Shoreline Golf Links (SGL) is an 18-hole course designed by Robert Trent Jones II & Associates that was completed in 1983. The course is owned by the City and generally open to the public 364 days a year. After operating at a deficit for several years, Touchstone Golf, LLC (Touchstone), assumed management and operations of SGL (Pro Shop and maintenance) in January 2012. Although SGL is a General Fund program, it is tracked and reported separately for management information purposes and to provide a more comprehensive overview of its operations.

The Fiscal Year 2016-17 budget was adopted with a $150,000 net surplus which is budgeted as a revenue transfer to the GOF. For Fiscal Year 2016-17, total revenues are estimated at $2.4 million, $272,000 (10.2 percent) lower than the Adopted Budget, but $46,000 more than the prior fiscal year audited. After a record July 2016, the greens at the golf course caught a disease in August and September, which reduced their consistency and affected the number of rounds played. The issue was resolved in late September. Furthermore, the majority of the rain in October and November fell on weekends, which affects revenues at the golf course more than weekday rain. Due to the diseased greens, rainy weekends, and the impact of a rainy January, revenues for Shoreline Golf Links are not estimated to achieve the adopted revenues.

The Fiscal Year 2016-17 operating expenditures are estimated at $2.2 million, $295,000 (11.8 percent) less than the Adopted Budget of $2.5 million. Included in operating expenditures is the management fee of $102,000 to Touchstone, $76,000 to reimburse the cost of administrative support provided by the GOF, and annual funding of liability insurance and equipment replacement. The fund is estimated to end the current fiscal year with a sufficient operating balance to fund a transfer of $150,000 to the GOF.

A comparison of the prior fiscal year audited, current fiscal year adopted and estimated, and the upcoming fiscal year recommended follows (dollars in thousands):

	2015-16 Audited	2016-17 Adopted	2016-17 Estimated	2017-18 Recommended
Revenues:				
Green Fees	$1,534	1,758	1,555	1,665
Golf Cart/Other Rentals	354	377	360	395
Range Revenue	236	277	250	249
Retail Sales	167	200	185	181
Other	51	48	38	48
Total Revenues	2,342	2,660	2,388	2,538
Operating Expenditures	2,230	2,504	2,209	2,413
Operating Balance	112	156	179	125
CalPERS Contribution	(3)	(3)	(3)	-0-
Transfer to GOF	(109)	(150)	(150)	(125)
Excess (Deficiency) of Revenues	0	3	26	-0-
Beginning Balance	7	7	7	33
Ending Balance	$ 7	10	33	33

The Fiscal Year 2017-18 recommendations total a net reduction of $120,700. Those $25,000 and over are as follows (see Attachments 3 and 4 for complete listings with descriptions):

- **Minimum Wage Impact 1/2-Year (Shoreline Golf Links):** $64,900 (ongoing)

- **Net Miscellaneous:** $(185,600) (ongoing)

Projected revenue for Fiscal Year 2017-18 is $2.5 million, $150,000 higher than the current fiscal year estimate and $196,000 higher than Fiscal Year 2015-16 Audited. Touchstone continues to monitor the membership programs and incorporates adjustments as appropriate. A 3.0 percent increase is recommended to frequent player fees and a $1.00 per player increase to green fees and golf car rentals are also recommended. Tournament fees were not increased in previous fiscal years with other green fees, therefore a $1.00 to $3.00 increase to Tournament fees are recommended to bring them in line with the other green fees.

Projected expenditures by Touchstone and the City of $2.4 million are approximately $91,000 lower than the current fiscal year adopted. The operating costs reflect recommended decreases in funding for supplies and utilities offsetting minimum wage and other compensation increases. Included in the Fiscal Year 2017-18 recommended operating expenditures are contributions of $215,400 for annual equipment replacement and $76,800 for reimbursement of administrative support provided by the GOF. Fiscal Year 2017-18 is projected with an operating balance of $125,000 to be transferred to the General Operating Fund.

The course condition continues to improve. Revenues are projected with a net decrease compared to the Fiscal Year 2016-17 adopted, but a net increase compared to Fiscal Year 2016-17 estimated. Based on projected revenues and expenditures, management of the course by Touchstone will allow for a transfer of $125,000 net surplus to the City's GOF. If the City experiences another "wet" year that adversely impacts revenues at the golf course, Touchstone will save on personnel and water costs in order to achieve the $125,000 net allocation goal. Staff continues to work with Touchstone and meets quarterly to review the operations and financial status of the golf course. The second term of the operating agreement with Touchstone expires December 31, 2021

Shoreline Regional Park Community Fund

The Shoreline Regional Park Community (Shoreline Community) was created in 1969 by the Shoreline Regional Park Community Act (Act) for the development and support of the Shoreline Regional Park (Shoreline Park) and to economically and environmentally enhance the surrounding North Bayshore Area. The Act prescribes the powers of the Shoreline Community, including the construction and replacement of the infrastructure needed to serve the Shoreline Community such as streets, curbs, gutters, parking lots, sidewalks, water and sewer services, lighting, waste disposal, power and communications, housing and levees, as well as operations and maintenance of Shoreline Park. The Shoreline Community is a separate legal entity with its own budget and financial statements, but is considered a component unit of the City.

The primary source of revenues for the Shoreline Community is property taxes, which include the revenue generated from the Shoreline Community's 1.0 percent levy assessed on the incremental taxable value of real and personal property located within the Shoreline Community. The AV of secured real property that does not experience a change in ownership or is not subject to new construction is adjusted annually at a rate not to exceed the California Consumer Price Index (CCPI) or 2.0 percent, whichever is lower. However, if a property changes ownership, it is reassessed at the current market value and new construction is initially valued at the cost of the construction. Unsecured tax on personal property, such as computers and other equipment, is assessed on the value of the property as reported annually to the County by the owning business.

Property Taxes are estimated higher than budget, and investment earnings are estimated lower than budget resulting in total estimated revenues for the current fiscal year of $42.1 million, $4.1 million (10.8 percent) higher than budget. The property tax projection for Fiscal Year 2016-17 anticipated a net increase compared to the July 1, 2015 tax roll resulting from changes in ownership, the 1.525 percent annual CCPI, and resolution of appeals. The Fiscal Year 2016-17 estimated property tax exceeds budget as a result of increased AV from construction in progress inspections (on new development) and more changes in ownership.

Total expenditures for the current fiscal year are estimated at $27.5 million, $403,000 below the Fiscal Year 2016-17 Adopted Budget of $27.9 million primarily due to savings in salary and benefits, and supplies and services. This estimate includes the operations of the Shoreline Regional Park, landfill, and street maintenance, as well as the area’s share of costs for services such as Police and Fire protection, planning, and general administration.

The intergovernmental payments to the County, in accordance with the agreement authorized in December 2004, is estimated to be on target with budget, and contributions to the Mountain View Whisman School District (MVWSD) and the Mountain View Los Altos Union High School District (MVLAUHSD) have been made in accordance with the 10-year Joint Powers Agreement (JPA) approved in June 2013.

A $5.1 million North Bayshore Development Impact Fee was received for the development at 1625 Plymouth Street and will be held in the Development Impact Fees Reserve until a transportation project identified in the North Bayshore Development Impact Fee Nexus study is adopted.

A comparison of the prior fiscal year audited, current fiscal year adopted and estimated, and the upcoming fiscal year recommended follows (dollars in thousands):

	2015-16 Audited	2016-17 Adopted	2016-17 Estimated	2017-18 Recommended
Revenues:				
Property Taxes	$31,305	36,886	40,762	39,306
Investment Earnings	690	706	680	859
Other	471	360	625	359
Total Revenues	32,466	37,952	42,067	40,524
Expenditures:				
Operating	11,815	12,879	12,407	13,184
Intergovernmental Payments	7,659	8,493	8,563	9,994
Debt Service	6,406	6,514	6,513	4,980
Loan Payment	1,472	-0-	-0-	-0-
Total Expenditures	27,352	27,886	27,483	28,158
Operating Balance	5,114	10,066	14,584	12,366
CIP Refunds	51	-0-	-0-	-0-
Development Impact Fees	578	-0-	5,052	-0-
CalPERS Contribution	(87)	(112)	(112)	(302)
Transfer to Workers' Comp	(7)	-0-	-0-	-0-
Transfer to Comp Absences	(26)	(52)	(52)	(20)
Retirees' Health UAAL	(17)	(924)	(924)	(995)
Capital Projects	(9,139)	(2,762)	(5,062)	(28,422)
Excess (Deficiency) of Revenues	(3,533)	6,216	13,486	(17,373)
Beginning Balance	50,234	46,701	46,701	60,187
Reserve	(5,200)	(4,900)	(4,900)	(4,600)
Reserve for Landfill	(4,000)	(5,000)	(5,000)	(6,000)
Reserve for Dev Impact Fees	(1,472)	(1,472)	(6,441)	(6,536)
Ending Balance	$36,029	41,545	43,846	25,678

The Fiscal Year 2017-18 recommendations total $304,000. Those $25,000 and over are as follows (see Attachments 3, 4, and 5 for complete listings with descriptions):

- **Ranger Service Contract:** $82,000 (ongoing)

- **Two Associate Civil Engineer—Land Development Positions (0.40):** $73,500 (limited-period)

- **Transportation Planner (0.25):** $49,900 (ongoing)

- **Associate Civil Engineer—Traffic Section Position (0.25)*:** $45,900 (limited-period)

- **Associate Civil Engineer—Land Development Position (0.20)**:** $36,700 (ongoing)

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*represents a continuing limited-period position
**represents a position going from limited-period to ongoing

- Major Capital Projects:

  - Shoreline Boulevard Interim Bus Lane and Utility Improvements, Phase I Construction: $10,037,000

  - South Bay Salt Pond Restoration Project—Mountain View Ponds Components: $4,975,000

  - Shoreline Bus Lane Property Acquisition: $4,260,000

  - Lower Stevens Creek Trail Levee Improvements: $2,940,000

  - Shoreline Boulevard at Highway 101 Bicycle/Pedestrian Bridge, Preliminary Design (project amendment): $1,467,000

  - San Antonio and Bayshore Traffic Signal and Geometric Modifications: $805,000

  - Colony Connection to Permanente Creek Trail: $775,000

  - Police/Fire Training and Classroom Facility at Fire Station 5, Design: $644,000

— Rengstorff Avenue and Leghorn Street Traffic Signal and Geometric Modifications: $565,000

Projected revenues for Fiscal Year 2017-18 are $40.5 million, $2.6 million higher than the current fiscal year adopted and $8.1 million higher than Fiscal Year 2015-16 Audited. However, the 2.0 percent CCPI, changes in ownership, and reductions from resolved appeals result in a net decrease in property tax compared to Fiscal Year 2016-17 estimated property taxes. As of January 2017, the County has approximately 5,500 active appeals for properties throughout the County, including properties located in the Shoreline Community. The County has provided some information about pending appeals specific to each local agency, and the Fiscal Year 2017-18 revenue includes a projected tax loss based on historical resolution of resolved secured appeals. Unsecured AV is reported by the business owner and historically the change in unsecured AV does not track with the change in secured AV. Unsecured AV is projected with a decline as historically, fiscal years with a significant increase, such as the current fiscal year, are followed by fiscal years of significant decline. The anticipated decrease in Fiscal Year 2017-18 AV discussed above will result in a decrease in the intergovernmental payments to the County. However, the intergovernmental payment to the school districts is projected to increase as this calculation is based on a different methodology than the County and utilizes the percent change in total property tax received between the two prior fiscal years.

Fiscal Year 2017-18 expenditures are recommended at $28.2 million, $272,000 higher than the current fiscal year Adopted Budget which includes ongoing recommendations of $184,600 and limited-period recommendations of $119,400. In addition, there is a $1.0 million contribution to the Retirees' Health UAAL; $302,000 contribution to the CalPERS liability, proportionate to the General Fund contributions; $20,000 to the Compensated Absences Fund; and $28.4 million in capital projects. The capital projects total includes $15.8 million for transportation related projects.

The fund is projected to end the 2017-18 fiscal year, including recommendations, with an ending balance of $25.7 million and $17.1 million in Reserves. As previously discussed with City Council, there are significant capital projects anticipated in future years related to transportation, landfill, and sea level rise. The Council adopted the North Bayshore Development Impact Fee in February 2016 to assist with funding improvements detailed in the North Bayshore Development Impact Fee Nexus Study. The recently approved Charleston East project will be assessed this fee. It is anticipated debt will be issued in the near future to complement the fees to fund the transportation projects related to the North Bayshore Precise Plan.

UTILITY FUNDS
WATER, WASTEWATER, SOLID WASTE MANAGEMENT

The City's enterprise utility funds are fully funded by the rates charged to customers; there is no General Fund support to the utility funds. Utility rates charged by governmental entities for water, sewer, and trash and recycling services are considered property-related fees and are subject to the procedural requirements of Proposition 218, Article XIII, of the California Constitution. Proposition 218 requires governmental agencies to conduct a majority protest hearing prior to adopting any changes in utility rates. A notice is required to be mailed no later than 45 days prior to the public hearing and is required to include the proposed rate adjustment, the calculation methodology, and describe the process for submitting a protest vote. The legislation also provides for future rate increases within prescribed limits to be approved without holding a hearing each year for up to an additional four years.

A Proposition 218 hearing is not required for the recommended water, wastewater, and solid waste rate increases as all recommended increases for Fiscal Year 2017-18 are within the prescribed limits as noticed May 6, 2016 and approved at the June 21, 2016 public hearing (see more detail in each section below). Staff will be mailing a notification of the proposed rate changes on or before June 1.

Water Enterprise Fund

The Water Enterprise Fund is a utility fund accounting for the revenues and expenditures associated with the provision of retail water service to Mountain View residents and businesses. The City provides potable water service to approximately 96.0 percent of water customers within the City limits while California Water Service (a private company) provides service to the remaining 4.0 percent of water customers in a few previously unincorporated neighborhoods. Potable water for the City's system is obtained primarily from the San Francisco Public Utilities Commission (SFPUC) regional Hetch Hetchy water system (85.0 percent). Water is also purchased from the Santa Clara Valley Water District (SCVWD) (11.0 percent) and City well production (4.0 percent). The primary costs associated with water service are the purchase of water, staffing to operate and maintain the system, ongoing maintenance, and capital replacement and improvement projects. Charges for services are designed to fully fund ongoing annual costs and a base level of annual capital projects as well as to maintain adequate reserves in accordance with Council policy.

A 10.0 percent increase for the average cost of water and meter rates, and a 3.0 percent increase for recycled water rates were adopted for Fiscal Year 2016-17. Operating revenues for Fiscal Year 2016-17 are estimated at $30.8 million, approximately $2.6 million (9.4 percent) higher than budget. This fund has been significantly impacted by previous water conservation efforts due to the drought, an approximate 30.0 percent reduction in usage from the 2013 base year for measuring conservation through Fiscal Year 2015-16. Although the reduced water usage is positive from a conservation perspective, revenues were not being generated as budgeted and were insufficient to support required fixed costs. This resulted in higher rates required to generate sufficient revenues from lower units of water sales. Last fiscal year it was estimated an additional 9.0 percent rate increase would be needed due to the 30.0 percent reduction in water usage. It was recommended and approved for this increase to be divided over two fiscal years with 3.0 percent in Fiscal Year 2016-17 (included in the 10.0 percent rate increase) and 6.0 percent to be included in the Fiscal Year 2017-18 rate increase (as included in the Prop 218 notice). For Fiscal Year 2016-17, water usage through February is trending approximately 7.0 higher. This increase has a positive financial impact on the Water Fund; however, not enough to change the additional 6.0 percent increase previously recommended for Fiscal Year 2017-18.

Operating expenditures for Fiscal Year 2016-17 are estimated at $27.4 million, $2.0 million (6.8 percent) lower than the budget of $29.4 million. This is primarily the result of retail water costs lower than budgeted and savings in operations. The budget was based on 90.0 percent of the City's required minimum water purchase; however, the SFPUC notified the City in June the minimum purchase requirement would be waived for Fiscal Year 2016-17 due to their continued call for voluntary 10.0 percent conservation. With the increased rainfall, it is anticipated the SFPUC will no longer be waiving the City's minimum water purchase past the current fiscal year, and staff estimates water costs for Fiscal Year 2017-18 will increase over 20.0 percent as a result of the minimum purchase requirement. The final decision to waive the requirement will be based on the SFPUC's analysis of their water supply for the coming fiscal year and any State mandates for continued water conservation measures. Staff does not anticipate water usage to return to predrought conditions due to the ongoing impact of conservation programs and the gradually increasing use of recycled water. Staff is evaluating options to minimize or eliminate minimum purchase penalties and will provide updates to the Council as alternatives are further developed.

The estimated operating balance for Fiscal Year 2016-17 is $3.3 million, which is sufficient to fund the CalPERS contribution of $217,000, Retirees' Health UAAL of $635,000, and the current fiscal year's $2.1 million for capital projects.

Capacity fees were adopted by Council effective July 1, 2015. The Fiscal Year 2016-17 Adopted Budget includes fees of $2.4 million based on building permits projected to be issued during the fiscal year. The capacity fees are currently estimated at $1.5 million, sufficient to fund the $1.1 million in additional capital projects. Various Development Impact Fees have been adopted by Council, and for Fiscal Year 2016-17, $1.4 million has been received. These fees are designated for specific projects which will be identified in the Five-Year Capital Improvement Program (CIP). The Water Fund is estimated with a $7.3 million ending balance and $11.8 million in reserves.

A comparison of the prior fiscal year audited, current fiscal year adopted and estimated, and the upcoming fiscal year recommended follows (dollars in thousands):

	2015-16 Audited	2016-17 Adopted	2016-17 Estimated	2017-18 Recommended
Revenues:				
Investment Earnings	$ 337	246	316	397
Water Sales	24,018	26,106	28,462	30,454[1]
Recycled Water Sales	526	600	465	600
Other	1,676	1,189	1,537	1,196
Total Revenues	26,557	28,141	30,780	32,647
Expenditures:				
Operating	9,480	10,106	9,538	10,393
Water Purchases	14,862	18,411	16,977	20,768[2]
Loan Repayment—Recycled Water	300	300	300	300
Debt Service	629	634	634	634
Total Expenditures	25,271	29,451	27,449	32,095
Operating Balance (Deficit)	1,286	(1,310)	3,331	552
Capacity/Development Impact Fees	1,900	2,369	2,866	2,303
CalPERS Contribution	(177)	(217)	(217)	(590)
Transfer to Workers' Comp	(16)	-0-	-0-	-0-
Retirees' Health UAAL	-0-	(635)	(635)	(294)
Capital Projects from Fees	(1,848)	(1,079)	(1,079)	(2,287)
Capital Projects	(3,180)	(2,079)	(2,079)	(2,942)
Excess (Deficiency) of Revenues	(2,035)	(2,951)	2,187	(3,258)
Beginning Balance	18,931	16,896	16,896	19,083
Capacity/Dev Impact Fees Reserves	(45)	(1,335)	(1,832)	(1,848)
Reserves	(9,706)	(9,946)	(9,946)	(10,807)
Ending Balance	$ 7,145	2,664	7,305	3,170

(1) Based on the recommended 7.0 percent rate adjustment.

(2) Based on no increase in wholesale water costs proposed by the SFPUC at the minimum purchase requirement, and proposed 9.0 percent and 9.9 percent increases for treated water and groundwater (well production), respectively, by the SCVWD.

The Fiscal Year 2017-18 recommendations total $361,600. Those $25,000 and over are as follows (see Attachments 3, 4, and 5 for complete listings with descriptions):

- **Associate Civil Engineer—Engineering and Environmental Compliance Section Position*:** $169,600 (limited-period)

- **Two Associate Civil Engineer—Land Development Positions (0.40):** $73,500 (limited-period)

- **Utility Online Payment Processing:** $50,000 (ongoing) (see Attachment 9)

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*represents a continuing limited-period position

- Major Capital Projects:

  — Miscellaneous Water Main/Service Line Replacement: $2,533,000

  — Shoreline Boulevard Interim Bus Land and Utility Improvements, Phase I Construction: $1,500,000

  — Water System Improvements and Recycled Water System Improvements: $846,000

The major factors that influence rate setting for the Water Fund are: (1) the cost of wholesale water; (2) water consumption level; (3) annual operating costs; and (4) level of capital improvements. The cost of water purchases from the SFPUC and other water sources (approximately 65.0 percent of recommended expenditures) has been subject to major fluctuations for more than a decade and has caused the City's retail water rate adjustments to vary significantly. The SFPUC has proposed a zero rate increase effective July 1, 2017, and SCVWD is proposing 9.0 percent and 9.9 percent rate increases for treated water and well water, respectively, for Fiscal Year 2017-18. Final rates will not be approved by the SFPUC until May 9, 2017 and by SCVWD on April 25, 2017. Annual capital project funding of $2.9 million is included in the rate calculation as the three-year rolling average of annual projects.

The recycled water rate is set to recover the cost of the program which includes the loan repayment ($300,000) and recycled water program operating costs ($300,000). Staff will continue to convert customers from potable water to recycled water when possible.

For Fiscal Year 2017-18, a 7.0 percent rate increase is recommended for the average cost of water and meter rates and a 3.0 percent increase is recommended for the recycled water rate. The Uniform and Tier 2 rates reflect the average cost of water; Tier 1 is set at 75.0 percent and Tier 3 is set at 160.0 percent of the average cost of water. Meter rates are tied to the capacity ratios published by the American Water Works Association (AWWA). Because of these relationships, individual rate increases may be slightly more or less than the 7.0 percent stated. This 7.0 percent rate increase includes the additional 6.0 percent noticed and approved for Fiscal Year 2017-18 at the rate hearing on June 21, 2016. An additional 1.0 percent is for rate increases from providers and CPI as allowed and noticed at the same rate hearing.

Fiscal Year 2017-18 projected revenues, with the recommended rate adjustments and water consumption based on the current fiscal year trend, are $32.6 million and recommended expenditures are $32.1 million (after eliminating the budget effect of depreciation expense). Included in expenditures are the proposed rate adjustments to wholesale water costs. It is anticipated the SFPUC rate will be adopted at its meeting on May 9, 2017. Staff will provide an update to Council if there are any changes to the proposed rate increase with the Proposed Budget on June 13, 2017. Recommended fee modifications are included in Attachment 2, and a comparison of the current rates and the recommended rates are included in Attachment 11.

The recommendation results in an operating balance of $552,000. There are also capital projects of $2.9 million, contribution to CalPERS of $590,000, proportionate to the General Fund contributions, and funding for Retirees' Health UAAL of $294,000. This results in projected Fiscal Year 2017-18 reserves balance of $12.7 million and projected ending balance of $3.2 million.

Capacity fees are projected at $2.3 million for Fiscal Year 2017-18, funding $873,000 in additional capital projects. As noted above, these fees provide funding for additional capital projects and mitigate the need to fund these projects with rate increases. The balance available of Development Impact Fees of $1.4 million will partially fund a designated project identified in the Five-Year CIP for Fiscal Year 2017-18.

Future fiscal year rates are anticipated to be impacted by the continued projected rate increases for implementation of the SFPUC capital improvements to the Hetch Hetchy system. The SFPUC has provided estimated future water rate increases of 0.0 percent, 3.0 percent, 13.3 percent, and 10.8 percent for Fiscal Years 2018-19 to 2021-22, respectively.

<u>Wastewater Enterprise Fund</u>

The Wastewater Enterprise Fund is the utility fund that accounts for the costs and revenues associated with the collection, transportation, and treatment of wastewater generated from all residences and businesses in the City. Other associated functions included in this fund are the Hazardous Materials Permit Program and the Industrial Liquid Waste Management Program. Expenditures in the Wastewater Fund include the construction and maintenance of sanitary sewer lines, stormwater lines, and pump stations; the City's share of costs associated with the operation of the Treatment Plant; and personnel costs for the operation and maintenance of the system. This fund is affected by costs associated with stringent requirements for the Treatment Plant, stormwater discharges into San Francisco Bay, and fluctuations in water usage. Revenues are partially governed by the amount of water used by commercial dischargers in the City each fiscal year.

An overall 19.0 percent rate increase was adopted for Fiscal Year 2016-17. This includes a 17.0 percent rate increase for operations and a 2.0 percent rate increase for future Treatment Plant capital costs. As previously outlined, there are future capital expenditures forecasted for the Treatment Plant as the facility began operations in 1972 and is in need of major renovations. A cumulative rate increase of 20.0 percent is projected and Council approved a gradual phase-in of 2.0 percent annually for 10 years to fund these long-term capital costs, of which Fiscal Year 2016-17 is the third year.

Unforeseen Treatment Plant costs identified by Palo Alto in Fiscal Year 2015-16 caused the fund to be in a distressed financial condition. To fully fund the impact of the increases in Treatment Plant costs, the rate increase for Fiscal Year 2016-17 would have needed to be 26.0 percent. Council approved staff's recommendation to spread the increase needed to stabilize the financial position of this fund over three fiscal years and utilize half of the rate stabilization reserve for Fiscal Years 2016-17 and 2017-18 to balance the fund. To compensate for the increased costs, additional 6.0 percent rate increases were projected for Fiscal Years 2017-18 and 2018-19 to phase-in the rate increase needed. These rate increases were noticed and approved at the rate hearing on June 21, 2016.

Staff has also previously indicated there are major City sewer main replacement projects necessary, approximately $29.8 million is identified in the Proposed Five-Year CIP, approximately $5.8 million on the unscheduled CIP list, and possibly more identified in the update of the Sewer Master Plan in Fiscal Year 2019-20. The majority of the trunk main infrastructure was installed in the 1950s and 1960s. The possibility of issuing debt for these projects, with a corresponding recommendation to phase-in rate increases to fund the debt, was identified as an option. However, capacity fees were adopted by Council, and as funds are collected, these capacity fees are providing a source of funding and could reduce future rate increases or any debt required for these additional capital projects. Staff projected capacity fees based on projected building permits to be issued and development in the pipeline, but due to building permits not being deemed complete and issued for construction as quickly as anticipated, actual and estimated capacity fees for the current fiscal year are lower than originally projected.

Staff is reviewing the current major sewer capacity upgrades needed due to General Plan Update, Precise Plan adoptions, and Gatekeeper approvals. Staff is also reviewing the condition of existing sewer mains to plan ongoing replacements and will be presenting these to the City Council as part of the Five-Year CIP discussion (Fiscal Years 2017-18 through 2021-22). Staff will continue to monitor the amount of the fees collected and review if there will be a need to issue debt, and any potential associated rate increase necessary, for these additional capital projects.

Operating revenues for Fiscal Year 2016-17 are estimated at $19.3 million, $473,000 (2.4 percent) lower than the budget of $19.8 million, as wastewater service charges are trending lower than budget. Operating expenditures are estimated at $16.7 million, $1.0 million (5.7 percent) lower than the budget of $17.7 million. This is primarily due to Treatment Plant expenditures estimated approximately $560,000 lower than proposed, in addition to a $91,000 credit for prior year expenses and savings in operations.

Each fall, an annual reconciliation of the prior fiscal year's actual treatment costs (based on volume) is performed by the Treatment Plant staff, and an adjustment is provided to each member agency. The City's share of audited expenditures of the Treatment Plant for last fiscal year were $91,000 lower than budgeted, resulting in a credit that is applied towards the current fiscal year's treatment costs. The estimated operating balance of $2.6 million will fund the CalPERS contribution of $128,000, Retirees' Health UAAL of $387,000, and $1.8 million for capital projects.

The fund is estimated with a $2.8 million ending balance and $5.6 million in reserves, which includes the accumulation of the rate increases needed for future Treatment Plant capital expenditures, the borrowing of funds for the additional City capital projects until sufficient capacity fee revenues are received, and using half of the rate stabilization reserve.

Various Development Impact Fees have been adopted by Council and for Fiscal Year 2016-17, $328,000 has been received. These fees are designated for specific projects which will be identified in the Five-Year CIP.

A comparison of the prior fiscal year audited, current fiscal year adopted and estimated, and the upcoming fiscal year recommended follows (dollars in thousands):

	2015-16 Audited	2016-17 Adopted	2016-17 Estimated	2017-18 Recommended
Revenues:				
Hazardous Materials/ Fire Safety Permits	$ 496	425	446	425
Investment Earnings	188	151	177	290
Wastewater Service	16,388	19,172	18,653	20,519 (1)
Other	268	34	33	34
Total Revenues	17,340	19,782	19,309	21,268
Expenditures:				
Operating	5,835	6,723	6,356	7,106
Wastewater Treatment	10,100	11,036	10,385 (2)	10,668
Total Expenditures	15,935	17,759	16,741	17,774
Operating Balance	1,405	2,023	2,568	3,494
Capacity/Development Impact Fees	2,797	2,054	2,063	4,050
CalPERS Contribution	(111)	(128)	(128)	(349)
Transfer to Workers' Comp	(37)	-0-	-0-	-0-
Retirees' Health UAAL	-0-	(387)	(387)	(246)
Capital Projects from Fees	(4,271)	(1,520)	(1,520)	(627)
Capital Projects	(4,342)	(1,759)	(1,759)	(2,103)
Excess (Deficiency) of Revenues	(4,559)	283	837	4,219
Beginning Balance	12,070	7,511	7,511	8,348
Capacity/Dev Impact Fees Reserves	1,451	917	908	(2,515)
Treatment Plant Reserve	(891)	(891)	(891)	(2,077)
Reserves	(5,984)	(5,597) (3)	(5,597) (3)	(5,620) (3)
Ending Balance	$ 2,087	2,223	2,768	2,355

(1) Based on a recommended 10.0 percent rate increase.
(2) Includes $91,000 credit for the prior fiscal year.
(3) Includes borrowing 5.0 percent of the 10.0 rate stabilization reserve.

The Fiscal Year 2017-18 recommendations total $92,900. Those $25,000 and over are as follows (see Attachments 3, 4, and 5 for complete listings with descriptions):

- **Two Associate Civil Engineer—Land Development Positions (0.40):** $73,500 (limited-period)

- Major Capital Projects:

  - Miscellaneous Storm/Sanitary Sewer Main Replacement: $1,585,000

  - Shoreline Boulevard Interim Bus Land and Utility Improvements, Phase I Construction: $627,000

Costs for the Treatment Plant are proposed to increase 1.9 percent for Fiscal Year 2017-18, resulting in the cost of wastewater treatment to be approximately 60.0 percent of the total recommended operating expenditures. **A 10.0 percent overall rate increase is recommended for Fiscal Year 2017-18:** 2.0 percent is due to the increase from the Treatment Plant for Fiscal Year 2017-18 and operating cost increases up to the CPI, 2.0 percent is the fourth year of the phase-in of planned Treatment Plant capital costs, and 6.0 percent as noticed and approved for Fiscal Year 2017-18 at the rate hearing on June 21, 2016 for unanticipated Treatment Plant costs in Fiscal Year 2015-16. For rate-setting purposes, a $2.1 million base level of annual maintenance capital projects is assumed for Fiscal Year 2017-18. An additional 6.0 percent rate increase needed for Fiscal Year 2018-19 was also noticed and approved at the rate hearing on June 21, 2016.

Based on the recommended overall 10.0 percent rate increase, operating revenues for Fiscal Year 2017-18 are projected at $21.3 million and recommended operating expenditures are $17.8 million (after eliminating the budget effect of depreciation expense). The operating balance of $3.5 million will fund the contribution to CalPERS of $349,000, proportionate with the General Fund contributions, funding for Retirees' Health UAAL of $246,000, and $2.1 million for capital projects. This results in a reserve balance of $5.6 million, using half of the rate stabilization reserve, in addition to the Capacity/ Development Impact Fee and Treatment Plant reserves of $4.6 million. The projected ending balance for Fiscal Year 2017-18 is of $2.4 million.

Capacity fees are estimated at $4.1 million for Fiscal Year 2017-18, funding $358,000 in additional capital projects. As noted above, capacity fees are not being collected as quickly as originally projected; therefore, staff has deferred some projects until sufficient capacity fees can be collected. With the large number of projects in the 5-year CIP and capacity fees not being generated as quickly as previously estimated, staff is evaluating the need of issuing debt for the City's additional capital projects. If it is necessary to issue debt to fund the necessary City capital projects, staff will return to Council for approval and the estimated associated rate increase.

Development Impact Fees of $269,000, received in Fiscal Year 2016-17, will partially fund a designated project identified in the Five-Year CIP for Fiscal Year 2017-18.

<u>Solid Waste Management Enterprise Fund</u>

The Solid Waste Management Enterprise Fund is the utility fund that accounts for the revenues and expenditures of solid waste-related services, including trash collection and disposal, recycling services, street sweeping, and the maintenance of two of the City's three closed landfill sites.

Trash and recyclables generated in the City are transported to the SMaRT Station (in which the City is one of three partners) for removal of recyclables and the remaining trash is transported for final disposal at the Kirby Canyon Landfill in South San Jose. The City provides a variety of services through an outside contractor (Recology) for the collection of trash and recyclables. The City bills and collects all revenues for solid waste services.

A Cost of Service (COS) Study to review the rate structure to realign rates to reflect the true cost of collection and disposal was completed and the results were incorporated for Fiscal Year 2015-16, with the exception of the cart rate adjustment which was approved to be phased in over three years. For Fiscal Year 2016-17, a 10.0 percent rate increase was adopted for carts, incorporating the second year of the COS Study for phase-in of cart rates, but no increase for any other trash and recycling rates was adopted.

The City's Solid Waste Fund operating revenues for Fiscal Year 2016-17 are estimated at $13.9 million compared to the budget of $13.0 million. Trash and recycling service charges are trending $890,000 (7.0 percent) higher than budget, mainly due to higher debris box revenue associated with the high level of development activity. City operating expenditures are estimated at $12.0 million, $696,000 (5.5 percent) lower than the Adopted Budget of $12.7 million, as a result of savings in operations and lower SMaRT Station costs due to the prior fiscal year SMaRT Station reconciliation. The SMaRT Station performs an annual reconciliation of the prior fiscal year's costs and an adjustment is provided to each member agency. For Fiscal Year 2015-16, the City received a credit of $323,000, which has been applied against payments in the current fiscal year. Recology revenues and expenditures are not considered part of the City's budget as these are contractually passed through to Recology, but are shown for informational purposes.

Operating revenues are estimated higher than operating expenditures by $1.9 million. After funding the additional CalPERS contribution of $91,000 and the current fiscal year's $279,000 for capital projects, there is an estimated ending balance of $5.6 million and reserves of $3.2 million.

A comparison of the prior fiscal year audited, current fiscal year adopted and estimated, and the upcoming fiscal year recommended follows (dollars in thousands):

	2015-16 Audited	2016-17 Adopted	2016-17 Estimated	2017-18 Recommended
Revenues:				
Investment Earnings	$ 61	62	84	102
Trash and Recycling Service Charges	12,841	12,742	13,632	13,874[1]
Other	283	195	224	195
City Revenues	13,185	12,999	13,940	14,171
Recology Revenues[2]	14,152	14,683	14,342	15,052
Total Revenues	27,337	27,682	28,282	29,223
Expenditures:				
Operating	4,119	5,087	4,800	5,265
Disposal and SMaRT Station Charges	7,777	7,656	7,247[3]	7,245
City Expenditures	11,896	12,743	12,047	12,510
Recology Payments	14,152	14,683	14,342	15,052
Total Expenditures	26,048	27,426	26,389	27,562
Operating Balance	1,289	256	1,893	1,661
CalPERS Contribution	(75)	(91)	(91)	(241)
Transfer to Workers' Comp	(8)	-0-	-0-	-0-
Retirees' Health UAAL	-0-	-0-	-0-	(876)
Capital Projects	(323)	(279)	(279)	(338)
Excess (Deficiency) of Revenues	883	(114)	1,523	206
Beginning Balance	6,418	7,301	7,301	8,824
Reserves	(3,162)	(3,186)	(3,186)	(3,186)
Ending Balance	$ 4,139	4,001	5,638	5,844

(1) Based on a 2.0 percent rate adjustment recommended and the third (and final) year 8.0 percent phase-in for carts.
(2) Neither revenues nor expenditures are adopted for Recology.
(3) Includes $323,000 credit from SMaRT Station reconciliation for the prior fiscal year.

The Fiscal Year 2017-18 recommendations total $130,200. Those $25,000 and over are as follows (see Attachments 3, 4, and 5 for complete listings with descriptions):

- **Two Associate Civil Engineer—Land Development Positions (0.40):** $73,500 (limited-period)

- **Commercial Composting Processing Fee:** $35,000 (ongoing)

- Major Capital Improvements:

  — Shoreline Landfill Cap Maintenance and Repairs: $134,000

  — Landfill Gas/Leachate System Repairs and Improvements: $134,000

The agreement with Recology provides for an increase based on CPI. In addition, Council approved a residential food scraps collection program in December 2016 for which increased costs to Recology result in a 2.48 percent. The total increase to Recology for Fiscal Year 2017-18 is 4.95 percent. There is no increase in the City's share of SMaRT Station costs currently proposed. The Recology increase, as well as increases in the cost of City programs up to the CPI and the annual maintenance projects, requires an overall average 2.0 percent rate increase.

In addition, the cart rate increase includes the third-year phase-in of cart rate increases resulting from the COS Study. Results of the COS Study were implemented in Fiscal Year 2015-16 with a phase-in of the cart rate increase over three years; the final increase of 10.0 percent in Fiscal Year 2017-18 was noticed in last year's Proposition 218 letter and approved at the June 21, 2016 rate hearing. Staff is recommending this be reduced to 8.0 percent for a total cart rate increase of 10.0 percent.

For the new residential foods scraps program, the cost of the program Council approved was estimated to have a cart rate impact of 6.0 percent. Staff has refined the cart rate increase and 5.0 percent is determined to be sufficient. *However, staff is recommending deferring this increase to Fiscal Year 2018-19.*

Incorporating the final year COS Study phase-in for cart rates, for Fiscal Year 2017-18, **a 10.0 percent rate increase is recommended for carts, and a 2.0 percent rate increase for all other services is recommended**. With a 10.0 percent rate increase for carts, the rate for a 32-gallon cart will increase by $2.95 a month to $32.25 per month, which is still lower than our neighboring cities' rates. Attachment 2 includes recommended fee modifications and Attachment 11 includes a comparison of the current rates and the recommended rates. Revenues for Fiscal Year 2017-18, including the rate adjustments recommended, are projected to total $29.2 million (City revenues of $14.2 million) with total expenditures of $27.6 million (City expenditures of $12.5 million). There is also funding of $338,000 for capital projects and $876,000 for Retirees' Health UAAL. In addition, staff is recommending additional contributions to CalPERS of $241,000, proportionate with the General Fund contributions. The fund is projected to end the 2017-18 fiscal year with a reserve at the policy level of $3.2 million and a $5.8 million ending balance.

Non-Major Funds

The Fiscal Year 2017-18 recommendations ($25,000 and over) for nonmajor funds are as follows (see Attachments 3, 4, and 5 for complete listings with descriptions):

Child-Care Commitment Reserve

- **Low-Income Child-Care Subsidies: $100,000 (limited-period)**

Public Benefit Fund

- **Homeless Initiatives:** $477,000 (limited-period)

Below-Market-Rate (BMR) Housing Fund

- **Contract Services:** $30,000 (ongoing)
- **Fair Housing Assessment:** $30,000 (limited-period)
- **Consultant Services:** $30,000 (limited-Period)

Housing Impact Fund

- **Notice of Funding Availability (NOFA) Administration:** $25,000 (ongoing)

Community Stabilization and Fair Rent Act (CSFRA) Fund

- **Computer Equipment and Software:** $50,000 (limited-period)
- **General Office and Noticings:** $40,000 (limited-period)
- **Hearing Officer:** $30,000 (limited-period)

Successor Agency Fund

- **Housing and Services for Low-Income Residents:** $250,000 (limited-period)

Downtown Benefit Assessments Districts Fund

- **Redirect Third Parking Feasibility Study to Paid Parking Program:** $75,000 (limited-period)

- **Consultant Services:** $45,000 (limited-period)

- **Parking Structure—Interior Signage Improvements:** $25,000 (limited-period)

Tree Mitigation Fund

- **Street Trees and Arbor Days:** $50,000 (offset with $50,000 in revenue) (ongoing)

Workers' Compensation Fund

- **Workers' Compensation Excess Insurance:** $54,000 (ongoing)

RESERVES

The City has established reserves for various purposes in the General Fund, Shoreline Regional Park Community Fund, Utility funds, Internal Services funds, and other Special Revenue funds. Reserves are essential elements in maintaining financial stability, meeting long-term objectives, and providing the ability to respond to unanticipated situations. They are also a source of interest income that is used for operating needs or offsets other funding requirements. A factor considered by Standard & Poor's in reconfirming the City's AAA underlying credit rating is the structure and funding status of reserves. Most reserves are established pursuant to City Council Policy A-11, Section 4, Reserve Policies, and others have been approved, as needed, by the City Council. A discussion regarding the reserve classifications, estimated fiscal year-end reserve balances compared to policy, or target balances and the recommended allocations are described below.

Utility reserves are recorded in the Water, Wastewater, and Solid Waste Management Funds for emergencies, contingencies/rate stabilization, and capital improvements.

Reserve Classifications

Reserves can be classified as those uncommitted but designated for a specific purpose and those created to fund liabilities.

- Reserves uncommitted but designated for specific purposes:
  - General Fund
  - General Fund Budget Contingency
  - Earned Lease Revenue
  - Capital Improvements
  - Open Space Acquisition
  - Strategic Property Acquisition
  - Child-Care Center
- Reserves to fund liabilities:
  - Property Management
  - Graham Site Maintenance
  - Compensated Absences

- Equipment Replacement
- Workers' Compensation Self-Insurance
- Unemployment Self-Insurance
- Liability Self-Insurance
- Retirees' Health Insurance Program

Reserves in the first group are uncommitted but designated for a specific purpose and are funded entirely by the General Fund. Those in the second group have current or future liabilities offsetting all or most of the reserve balance and, with the exception of the Property Management and Graham Site Maintenance, receive transfers from multiple operating funds.

For the Retirees' Health Program, the City continues to accumulate funds toward this liability which is required to be recalculated every two years and will be updated during the next fiscal year, as of July 1, 2017. All funds, except the General Operating Fund, have contributed their full share of the liability. Fiscal Year 2016-17 includes funding from other funds to maintain full funding and an additional $2.0 million contribution from the General Operating Fund. The liability was last recalculated as of July 1, 2015 and the Fiscal Year 2017-18 budget includes recommended funding from other funds to maintain full funding of their share of the liability, an additional $2.0 million from the General Operating Fund, and additional funding from the estimated Fiscal Year 2016-17 carryover, depending on Council direction.

Background and Analysis

The table below details the estimated balance, recommended allocations, recommended balance, and policy/target balance for each reserve (dollars in thousands):

	6/30/17 Estimated Balance	Amount Recommended for Allocation	Other Funds	7/1/17 Recommended Balance	Policy/ Target Balance
Uncommitted but Designated for Specific Purpose:					
GF Reserve	$ 26,696	(3,171)[1]	-0-	23,525	23,525[1]
GF Budget Contingency	5,209	-0-	-0-	5,209	5,209
GF Earned Lease Revenue	3,591	-0-	-0-	3,591	3,500
GF Capital Improvements	14,818	3,970[2]	-0-	18,788[3]	8,217[3]
GF Open Space Acquisition	576	-0-	-0-	576	576
GF Strategic Property Acquisition	9,486	-0-	-0-	9,486	9,486
GF Child-Care Commitment	407	-0-	-0-	407	-0-
Subtotal	60,783	799	-0-	61,582	50,513
To Fund Liabilities:					
GF Property Management	1,560	-0-	-0-	1,560	1,560
Graham Site Maintenance	805	-0-	-0-	805	805
Compensated Absences[5]	6,900	550	42	7,492	7,450[4]
Equipment Replacement[5]	24,900	-0-	-0-	24,900	24,900
Workers' Compensation[5]	11,000	-0-	-0-	11,000	9,146[7]
Unemployment[6]	500	-0-	-0-	500	500
Liability Self-Insurance[5]	4,842	-0-	-0-	4,842	4,462[6]
Subtotal	50,507	550	42	51,099	48,823
Total	$111,290	1,349	42	112,681	99,336
Retirees' Health[7]	$107,900	2,000	-0-	109,900	137,405[8]

(1) Policy balance is recommended to be calculated as 20.0 percent of the General Operating Fund budget. This is subject to Council direction regarding a CalPERS funding strategy.
(2) Recommended up to $4.0 million, to be determined based on actual results for Fiscal Year 2016-17.
(3) Includes $3.2 million balance for prepaid lease from Downtown Family Housing Project.
(4) Based on the liability established as of June 30, 2016.
(5) Funding provided by the General Fund, Development Services, Shoreline Golf Links, Parking District, Community Development Block Grant (CDBG), Shoreline Regional Park Community, Enterprise Funds, and Fleet Maintenance, as applicable.
(6) Actuarial liability, in addition to reserve for catastrophic claims per policy, as applicable.
(7) Funds accumulated in the California Employers' Retiree Benefit Trust (CERBT).
(8) Based on the actuarial valuation as of July 1, 2015 for Fiscal Year 2017-18.

General Fund Reserve

Per Policy A-11, the General Fund Reserve has a policy balance of 25.0 percent of the GOF adopted expenditures. This reserve is the source of funding for necessary, but unanticipated, expenditures during the fiscal year, unanticipated revenue shortfalls, source for interfund loans, emergencies, and to generate ongoing interest earnings. In Fiscal Year 2009-10, up to $1.0 million in the General Fund Reserve was earmarked for the first-time homebuyers program. These loans would be considered as an investment alternative and would be included as funds toward the 25.0 percent policy balance. No loans have been issued to date.

For Fiscal Year 2017-18, staff is recommending to revise the policy balance to allow a range of between 20.0 to 25.0 percent of the GOF adopted expenditures, net of budget savings, as part of the CalPERS funding strategy to reduce the City's unfunded pension obligation. If this reserve were reduced to 20.0 percent, this would provide approximately $6.3 million that can be allocated to a one-time prepayment of $10.0 million to CalPERS (see Attachment 1). The final amount necessary will be calculated with the Adopted Budget. If there is any use of this reserve for the remainder of the current fiscal year, it will modify the amount available.

General Fund Budget Contingency Reserve

This reserve was created during the downturn in the economy in the early 2000s to position the City to adjust to anticipated lower revenues and provide financial flexibility in case revenue estimates were not met or State actions forced further budget reductions. In Fiscal Year 2006-07, the Council consolidated and eliminated what was believed at the time to be an unnecessary reserve as the economy and City revenues had improved. In Fiscal Year 2008-09, the economy plunged into the deepest recession since the Great Depression and this reserve was reestablished.

During this past recession, this reserve has been used for the transitioning of positions to be eliminated, the phasing out of certain expenditures, in addition to funding for the transitioning of employee benefit changes, transitioning Shoreline Golf Links to a new operating model, and the elimination of the City's redevelopment agency. The reserve is estimated with a balance of $5.2 million, as of June 30, 2017, before recommendations, and will be available for similar purposes during the next economic downturn.

Revenue from the Ameswell (Moffett Gateway) property is projected to begin in Fiscal Year 2017-18 and the full projected annual revenue after a few years of operations is estimated at over $4.0 million. The majority of this revenue is recommended to be earmarked for debt service related to the Police/Fire Administration Building Remodel and Expansion. Staff proposes the revenue received in the fiscal years prior to the beginning of debt service be used for a limited-period need. Fiscal Years 2017-18 and 2018-19 include transfers in the amount of $755,400 and $1.3 million, respectively to the Budget Contingency Reserve.

General Fund Earned Lease Revenue

In April 2011, the City leased the remaining portion of the Charleston East site to Google Inc. (Google) and Google prepaid $30.0 million as rent for the 53-year lease term that coincides with the lease term for the northern portion of the site. The initial $30.0 million was placed in a fiduciary fund for the benefit of Google. The annual rent of approximately $580,900 is recognized as it is earned and accumulated in this reserve with the intent the $30.0 million principal balance will be available at the end of the 53-year lease term. Based on an average 3.5 percent interest rate over the 53-year lease term, it was originally projected annual average interest earnings would be $1.1 million.

Beginning in Fiscal Year 2011-12, $1.1 million was transferred to the GOF from this reserve. However, due to the unprecedented low interest rate environment, the transfer was reduced to $750,000 for Fiscal Years 2012-13 and 2013-14 and in Fiscal Year 2014-15 transfers were ceased altogether. The estimated balance at the end of this fiscal year will be $3.6 million, slightly higher than the target balance of $3.5 million. Staff will reevaluate projected interest earnings, but at this point it is recommended that no transfers be made until interest rates rise more.

General Fund Capital Improvement Reserve

The City has a long-term policy to reserve a minimum of $5.0 million for unspecified capital projects in the General Fund Capital Improvement Reserve. This provides flexibility in the City's planning for capital projects, serves as a contingency fund for capital projects, generates ongoing investment earnings, and also serves as an emergency pool of funds for unanticipated high-priority capital needs.

As noted earlier, Google subleases Parking Lots C and D from SFX (LiveNation) and this agreement ends mid-December 2017. In March 2017, the City Council approved Google's request for a three-year extension of the sublease through December 2020 for a $600,000 one-time payment to the City, which was received in early April 2017. The $600,000 is recommended to be transferred to the Capital Improvement Reserve.

Additional contributions to the Capital Improvement Reserve are recommended from the funds set aside, identified as at risk, from the increases generated from the Google Leases revaluations. By the end of Fiscal Year 2017-18, the decennial revaluation process will have been completed for the three City-owned land leases between the City and Google. Based on the actual revaluation of two sites and an estimated revaluation of the third site, annualized rent payments are estimated to increase approximately $7.7 million. It is probable that during the time span before the next decennial adjustment in April 2026, there will be at least one economic downturn. If a downturn occurs when a revaluation occurs, the lease revenues to the City could decline. Staff reviewed the changes in AV for the past 13 years and identified a potential 15.0 percent loss in secured AV in the event of an economic downturn. Therefore, to reduce the dependency on these revenues in Fiscal Year 2017-18, the potential decline in revenues, calculated at $1.9 million, is recommended to be transferred to the Capital Improvement Reserve to fund projects in Fiscal Year 2018-19 or later.

This reserve generally receives an allocation from the General Fund carryover balance. The contribution from the Fiscal Year 2016-17 General Fund carryover depends on the direction received by Council on the CalPERS funding strategy.

In June 2009, $3.5 million was appropriated for the acquisition of the property at 263 Escuela Avenue (now The View Teen Center) and was repaid from the land lease prepayment for the Downtown Family Development Project in Fiscal Year 2011-12. However, these funds are considered unearned revenue and are available to be allocated as rent is earned. There is a remaining balance of $3.2 million of unearned revenue.

General Fund Open Space Acquisition Reserve

This reserve was established for the purpose of acquiring open space to meet the needs of the City. Council Policy A-11 provides the proceeds from sale of surplus property be allocated to this reserve if there is no other recommendation. These funds are designated to be available as supplemental funding to Park Land Dedication fees for open space acquisition. There is a balance of $576,000 in this fund.

General Fund Strategic Property Acquisition Reserve (SPAR)

This reserve was created in Fiscal Year 2000-01 for the purpose of setting aside specific funds for the City to use for the acquisition of strategic property(ies) in order to take advantage of economic development opportunities. This fund was used to purchase the Vector Control site (Ameswell/Moffett Gateway) which will provide ongoing revenue to the City. The proceeds from the sales of City-owned property have been placed in this reserve as one source for its funding.

During the current fiscal year, $3.0 million has been transferred to this fund ($2.0 million as part of the GOF and $1.0 million from the Fiscal Year 2015-16 carryover). This reserve has funded $5.0 million towards the capital improvements for the

Community Center. Additional activity in this reserve is the lease and sublease of the property on Villa and View Streets. The estimated balance available in this reserve is $9.5 million; however, a portion of this is an alternative source for the CalPERS funding strategy (see Attachment 1).

The City has had a positive history of leveraging City properties with long-term ground leases to generate ongoing revenues for the GOF. Long-term ground lease revenues are recession-resistant and are usually structured with inflationary increases. In order to provide resources for future properties that could be leased for future ongoing revenues, staff is recommending $2.0 million be transferred from the GOF to this reserve in Fiscal Year 2017-18.

General Fund Child-Care Commitment Reserve

This reserve was established for the repayment to the Packard Foundation for the financing of the Child-Care Center. The final payment to the Packard Foundation was made in January 2016. Community Gatepath was selected as the new operator of the Child-Care Center in 2015 and will continue to make the same annual payments of $201,000.

As the annual $201,000 lease payment from Community Gatepath is no longer needed for repayment of the loan, staff reviewed alternatives with Council at the April 19, 2016 Council meeting. Subsequently, staff returned to Council on December 6, 2016 with recommendations and Council approved using up to $100,000 per fiscal year for low-income subsidies through the initial term of the Operator Agreement with Community Gatepath. The Fiscal Year 2017-18 recommended budget includes $100,000 for the purpose approved by Council.

General Fund Property Management Reserve

This reserve was established in Fiscal Year 1995-96 to provide a source of funds for landlord obligations that could arise from the lease of City property in the North Bayshore Area. These obligations could include environmental testing, certain responsibilities identified in land leases, or other costs normally incurred by a lessor. There is a balance of $1.6 million in this reserve.

Graham Site Maintenance Reserve

This reserve was established in Fiscal Year 2004-05 to fund maintenance obligations for the Graham Sports Complex. In the agreement with the school district to construct the reservoir beneath the playing fields at Graham Middle School, the Water Fund contributes $220,000 per year to this reserve. The City agrees to maintain this site and the GOF is reimbursed from this reserve for the maintenance costs of the Graham Sports Complex. The reserve has an estimated balance of $805,000 to fund future maintenance or improvements to the site.

Compensated Absences Reserve

The Compensated Absences Reserve was established in Fiscal Year 1991-92 to fund the City's liability for the accrued vacation, comp time, and sick leave obligations of employees in all funds except the Enterprise and Internal Services Funds. The liabilities of the Enterprise and Internal Services Funds are recorded in those respective funds as required by governmental accounting standards. This reserve is drawn down for leave payoffs to separating and retiring employees (for accumulated vacation and sick leave, if applicable, under the City's Personnel Rules) and current employee vacation cash-out payments during the fiscal year. The leave liability is recalculated, in accordance with generally accepted accounting principles (GAAP), each fiscal year with the close of the City's financial records.

As of March 31 for the current fiscal year, $1.4 million has been paid out and an additional estimated $200,000 will be utilized by the end of the fiscal year. The calculated liability for this reserve has increased $624,000 from the prior fiscal year. The current estimated reserve balance of $6.9 million is below the calculated liability of $9.3 million as of June 30, 2016. Although it has been a long-standing policy to fund 100 percent of the liability in this reserve, 100 percent funding is unlikely to ever be required at any particular time. To bring the funding level to the current policy level of full funding would require $2.4 million of additional funding. The liability will be recalculated at the close of the current fiscal year.

As part of the CalPERS strategy to increase the funding of the City's pension obligation, staff is recommending to decrease the funding level to 80 percent for Compensated Absences. If this option is chosen by Council, this would require additional funding of $592,000—$550,000 from the General Fund carryover and $42,000 from other funds for their proportionate share—to bring the balance to 80.0 percent of the policy level. If this change is approved, staff would return with amendments to Council Policy A-11.

Equipment Replacement Reserve

The City established the Equipment Replacement Reserve in Fiscal Year 1991-92 to stabilize the annual funding needed for the replacement of certain City equipment. Level annual contributions are received from various funds and this reserve absorbs the large fluctuations in annual expenditures for equipment replacement from fiscal year to fiscal year. Only major categories of capital assets are included in the Equipment Replacement Fund. The assets included are all vehicles, information technology equipment (e.g., computers, printers, servers, etc.), Police and Fire radios, CAD/RMS system hardware, and Communications Center furniture and equipment. The equipment for the maintenance of Shoreline Golf Links is also separately accounted for in the Equipment Replacement Reserve. The annual contribution level is based on the cost or estimated replacement cost of the asset divided by the estimated useful life of the asset.

The annual funding level is projected at $3.8 million and the current estimated balance of $24.9 million is on target with the policy balance; however, the target balance is under review. Equipment replacements scheduled for Fiscal Year 2017-18 total $4.0 million, plus there is $703,000 recommended to be rebudgeted (from the $5.0 million budgeted in the current fiscal year) for a total of $4.7 million. Staff generally reviews all items before purchasing and will only replace those items necessary due to expected failure or that will provide improved efficiencies.

Workers' Compensation Self-Insurance Reserve

The Workers' Compensation Fund was established by Council resolution in 1975 to account for the City's self-insured obligations for Workers' Compensation liabilities to City employees injured while at work. The primary reasons to be self-insured are to control costs and pay claims as they are incurred to maximize cash flow and provide timely and better services. When insured, one pays the entire premium fees up front and then the insurance carrier manages the claim in hopes of incurring less cost.

Expenditures paid out of this fund include the cost for the City's third-party administrator (TPA), the insurance above our self-insurance retention of $750,000, claims, indemnity payments, and the State self-insurance fee.

In addition, the City budgets $200,000 a year to fund Public Safety employees' salaries while on Workers' Compensation. This is utilized when Police or Fire is required to backfill with overtime or other personnel for an employee out on Workers' Compensation and cannot absorb the cost of the employee's salary in the department's budget.

The required balance of this reserve is based on projected liabilities as determined by an actuarial valuation conducted every fiscal year. In addition, the reserve policy includes funding of $1.5 million for the potential of two catastrophic claims at the City's current level of self-insured retention of $750,000 per claim (i.e., deductible). The accrued liability is reviewed on an annual basis with the fiscal year-end close of the City's financial records.

The Reserve has an estimated balance of $11.0 million, which is higher than the $9.1 million policy level as of June 30, 2016. Staff is not recommending any reduction in this reserve at this time and will evaluate as needed.

Unemployment Self-Insurance Reserve

The Unemployment Self-Insurance Reserve was approved by Council in 1978. This program provides for the State-mandated unemployment insurance benefits for former employees. The City pays for unemployment claims on a pay-as-you-go basis and generally, contributions for the estimated payments are made annually. Annual expenditures will fluctuate in this fund and during the Great Recession higher unemployment and longer eligibility periods resulted in higher unemployment costs. However, with the economic recovery, unemployment claims have decreased. The balance in this reserve is approximately $500,000.

Liability Self-Insurance Reserve

The Liability Self-Insurance Reserve was approved by Council in 1980. The City currently self-insures for the first $1.0 million of liability exposure per occurrence. The City is a member of the Authority of California Cities Excess Liability (ACCEL) Program for the pooling of liability insurance above the $1.0 million self-insured retention. ACCEL began in 1986 as a pool for medium-sized cities and the City joined ACCEL in 1992. Other members of the pool are Anaheim, Bakersfield, Burbank, Modesto, Monterey, Ontario, Palo Alto, Santa Barbara, Santa Cruz, Santa Monica, and Visalia. ACCEL pools liability coverage and the City purchases additional coverage through ACCEL. Other expenditures funded from the Liability Fund are for outside legal counsel for defense against claims, insurance (e.g., property, automobile, flood, etc.), and payment for claims.

Council Policy A-11 specifies the policy level of this reserve to be $2.0 million for the self-insured exposure for two catastrophic incidents and an amount to fund estimated incurred claims. The estimated incurred claims are determined by an actuarial valuation performed every year and are reviewed on an annual basis with the close of the City's financial records. The actuarial valuation, last updated as of June 30, 2016, indicates a liability of $2.5 million, resulting in the policy level for this reserve at $4.5 million. The current estimated balance of $4.8 million is slightly higher than the policy level, but staff is recommending the surplus balance remain in the fund to offset potential future liability increases.

Retirees' Health Insurance Program Reserve

The City provides other postemployment benefits (OPEB) by contributing all or a percentage of the premium cost for its retired employees health care. The cost for current employees who will be eligible for this benefit in the future, as well as those already retired, represents an outstanding liability to the City.

The Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Post-Employment Benefits Other than Pensions* (Statement No. 45), became effective for the City with the fiscal year ending June 30, 2008. This statement requires the City to update its Retirees' Health valuation every two years. It was last updated as of July 1, 2015, and will be updated this next fiscal year as of July 1, 2017.

GASB Statement No. 75, *Accounting and Financial Reporting by Employers for Post-Employment Benefits Other than Pensions*, will be effective with the fiscal year ending June 30, 2018. The new OPEB standard parallels the pension standard issued with GASB Statement No. 68, *Financial Reporting for Pension Plans*, which essentially requires the City to report the unfunded liability on the face of the City's financial statements and enhances the note disclosures and required supplementary information (RSI) about our OPEB liability.

Major changes occurring with the latest valuation included the migration of Public Safety employees into the CalPERS health system (PEMHCA). As previously discussed with Council, it is anticipated the City's total actuarial accrued liability (AAL) will increase significantly by adding dependent coverage; however, the plan costs are lower and the employees are now contributing annually towards this liability. Other factors increasing this liability are the projected excise tax for high-cost plans under the Affordable Care Act, revised demographic assumptions, and the reduced discount rate from 7.00 percent to 6.73 percent. The City participates in the California Employers' Retiree Benefit Trust (CERBT or Trust) managed by CalPERS, which reduced the discount rate for all of its plans.

The City has made great strides toward funding the AAL of $137.4 million (projected for Fiscal Year 2017-18 as of July 1, 2015), with assets set aside of $107.9 million, or 78.5 percent funded (estimate as of June 30, 2017). All funds other than the GOF have fully funded their share of the unfunded AAL (UAAL). To reduce the GOF share of its UAAL, a total of $6.5 million additional funds have been budgeted and transferred to the CERBT since Fiscal Year 2014-15. An additional $2.0 million is recommended to be transferred from the current fiscal year carryover and staff is also recommending an additional $2.0 million in the Fiscal Year 2017-18 budget as well as $2.0 million for Fiscal Year 2018-19.

Reserve Recommendations

Staff has performed a preliminary review of reserve levels and included funding recommendations for specific reserve requirements. Alternatives to provide significant funds to contribute to CalPERS and reduce the City's unfunded pension obligation are being recommended. One option would modify the reserve levels for the General Fund Reserve from 25.0 percent to a range between 20.0 and 25.0 percent of GOF adopted expenditures, net of budget savings, and for the Compensated Absences Reserve from 100.0 percent funding to 80.0 percent. Other options include funding from SPAR or Capital Improvement Reserve. The reduction in the funding levels of reserves will contribute to the $10.0 million strategy to reduce the City's unfunded CalPERS pension liability. The remaining balance allocation is dependent upon Council direction provided on the CalPERS funding strategy. These recommendations will allow most reserves to meet policy levels.

CONCLUSION

Strong revenue growth has continued and the GOF is in a good financial position. For Fiscal Year 2017-18, the economy is anticipated to remain strong in most major categories (e.g., Property Tax, Sales Tax, Use of Money and Property, Charges for Services, etc.) and GOF revenues are projected to increase to $128.0 million, or 7.8 percent, compared to the current fiscal year adopted revenues. Including consideration of the budget recommendations, totaling $1.0 million in non-discretionary, $1.2 million in discretionary spending, which contributes to a 8.5 percentage total expenditure increase, the GOF is projected to have an operating balance of $2.4 million at the end of Fiscal Year 2017-18, 1.9 percent of projected revenues. Although there are other areas where additional resources could be added, more are not recommended at this time as the anticipated operating balance is relatively small and projections indicate it will decrease in the future. Additional net limited-period expenditures of $2.7 million are recommended to address additional staff resources.

The Development Services Fund revenues for the current fiscal year are estimated higher than budgeted as development activity remains strong. The Fund is estimated to end Fiscal Year 2016-17 with an available balance of $10.5 million and a reserve of $4.5 million. This balance is necessary due to the timing of development-related revenues and expenditures. Revenues for development activity are often collected well in advance of the performance of services and occurrence of the corresponding expenditure. Development activity is anticipated to continue at a high level for Fiscal Year 2017-18.

The condition of the Shoreline Golf Links continues to improve under the management of Touchstone. Fiscal Year 2016-17 revenues and expenditures are estimated less than budget, but still allowing for the full transfer to the GOF of $150,000. Continued improvement is projected for Fiscal Year 2017-18 with modest fee increases recommended.

The Shoreline Community's total Fiscal Year 2016-17 property taxes are estimated $3.9 million higher than budget due to new development and increases related to changes in ownership. Fiscal Year 2017-18 revenues are projected with an increase over the current fiscal year adopted but lower than estimated. Expenditures are higher due to operating increases and estimated interagency payments offset slightly by lower debt service payments.

The financial position of the Water Fund was severely impacted by reduced water sales from conservation efforts during the drought, resulting in approximately 30.0 percent less water usage. During the current fiscal year, water usage increased 7.0 percent over the prior fiscal year, which has resulted in an improved financial condition of the Water

Fund. For Fiscal Year 2017-18, the SFPUC is proposing no rate increase in wholesale water costs and SCVWD is currently proposing a 9.0 percent and 9.9 percent rate increase for treated water and well water, respectively. With the increased rainfall, it is anticipated the SFPUC will no longer be waiving the City's minimum water purchase past the current fiscal year. A 7.0 percent rate increase in the average cost of water and meter rates and a 3.0 percent increase in recycled water are recommended for Fiscal Year 2017-18 to fund the increased cost of water, City operational costs, and the impact of previous reduced water sales.

Wastewater Fund revenues and expenditures are trending lower than budget. Expenditures are below budget primarily due to savings in operating costs and the credit from the Treatment Plant from the prior fiscal year. A 10.0 percent rate increase is recommended for Fiscal Year 2017-18, 8.0 percent due to increases in Treatment Plant costs in the prior fiscal year being phased in over two years, as well as City operating costs and the additional 2.0 percent for the incremental phasing in of funding for capital replacements at the Treatment Plant (the fourth year of 10). The additional rate increase is needed to align operating revenues with expenditures, recommended to be phased in over Fiscal Years 2017-18 and 2018-19. Staff is also reviewing needed City capital infrastructure improvements as to whether debt will be required to fund those capital improvements.

Solid Waste Management Fund revenues are higher than budget and expenditures are less than budget. The Recology contract provides for a CPI 2.47 percent increase and with the implementation of the food scrap program, a total 4.95 percent increase is due to Recology. A 2.0 percent general rate increase is recommended and an additional 8.0 percent rate increase for carts, the third and final year from the Cost of Service Study. The food scraps program will be implemented in July 2017, but the 5.0 percent rate impact can be deferred until July 2018.

As all recommended rate increases are within those provided, noticed, and approved under Proposition 218 last fiscal year, no Proposition 218 hearing is required this fiscal year. The total average increase for a single-family residential customer as recommended for all three utilities is 8.5 percent, resulting in an estimated increase of $11.57 monthly. Rates will generally still be comparable, or lower, than our neighboring cities. A comparison of the current and the recommended rates is included in Attachment 11.

Most reserves are at or exceed their target or policy balance. Alternatives to provide funds for the CalPERS Funding Strategy are recommended to come from reserves. The funding from reserves will assist in the strategy to increase the funding level of the City's pension obligation. It is recommended $6.0 million from the estimated Fiscal Year 2016-17 and reserves be allocated to CalPERS and, depending on the strategy option selected, additional funding would be transferred from SPAR or the Capital Improvement Reserve, with any remaining carryover to be allocated to either OPEB or the Capital Improvements Reserve (see Attachment 1).

NEXT STEPS

Council input and direction are sought on the material in this report at the April 27, 2017 Study Session. Based on feedback from the City Council, the Fiscal Year 2017-18 Proposed Budget will be prepared for distribution to the City Council prior to budget hearings. The evening of June 13 is scheduled for the first public hearing and a second public hearing and final adoption is scheduled for the City Council Special Meeting of June 20, 2017.

PUBLIC NOTICING

Agenda posting, notice on social media, and notice published in the *San Jose Post Record* and the *Mountain View Voice*.

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Attachments:
1. CalPERS Discount Rate Change Funding Strategy
2. Fiscal Year 2017-18 Recommended Fee Modifications
3. Fiscal Year 2017-18 Recommended Non-Discretionary Ongoing Changes
4. Fiscal Year 2017-18 Recommended Discretionary Ongoing Changes
5. Fiscal Year 2017-18 Recommended Limited-Period Expenditures
6. Special Operations Program
7. Fiscal Year 2017-18 Recommended Capital Outlay
8. Fiscal Year 2017-18 Recommended Equipment Replacement
9. Credit Card Processing Fees-Update
10. CHAC Requested Increase
11. Comparison of Current and Recommended Utility Rates