



2019/2020 through 2028/29 Ten-Year Financial Plan

May 2018

ABOUT THIS REPORT

The purpose of the Ten-Year Financial Plan is to provide policy-makers and the public an updated assessment of the City's fiscal health that takes into account the latest economic developments. The report includes historical perspective on revenues and expenditures and a ten-year financial outlook beyond the adopted budget year. The value of this type of analysis is to give the City Council, staff, and the public a tool to assist with strategic decision-making as they work to adopt the budget for the coming year.

The Ten-Year Financial Plan is a collaborative effort between the City Manager's Office, Finance Department, and City departments. Individual projections of revenues and expenditures are developed based on trend analyses, input from available economic reports, consultant recommendations (e.g., our sales tax consultant MuniServices and property tax consultant HdL), and input from other subject matter experts. The most current information available is incorporated into the City's Plan and refined on a moving forward basis as part of the City's commitment to fiscal responsibility.

EXECUTIVE SUMMARY

The combination of an improved economy, careful management of limited resources, development and redevelopment projects happening throughout the City, and monies flowing to the City from events at Levi's Stadium have generated General Fund budget surpluses the last several years which have allowed the City to fully fund its Budget Stabilization Reserve (formerly Working Capital Reserve), make additional contributions to the Capital Projects Reserve which funded an increase in capital project funding, and allocate funding to the recently established Pension Trust Program to pre-fund pension obligations. Looking to fiscal year 2018/19 and beyond, the City is projecting that the regional economy will continue to grow at a moderate rate. However, due to rising pension costs it is projected that the City's expenditures will begin to outpace revenues in the next ten years.

As with any multi-year forecast, the accuracy of the results are only as good as the assumptions upon which they are based. While this Plan has been based on the primary assumption that the economy will continue to grow at a moderate rate, an appropriate amount of conservatism has been built into the projections given the typical amount of economic volatility in the local and regional economies. For example, although there are several large development projects currently under review that are likely to begin construction in the next couple of years, the forecast does not include the likely positive impact that these projects will have on General Fund tax collections.

ECONOMIC OUTLOOK

Summing up Silicon Valley's economy and community is not an easy task. On the positive side, Santa Clara has experienced strong revenue growth and development activity. Unemployment is at a historic low with job growth outpacing the rest of the state and the nation, with mixed opinions on the result of rising housing prices and a significant increase in commercial and residential development activity. Looking to 2018/19 and beyond, the City is projecting that the regional economy will continue to grow. However a word of caution, the probability of a change to the local economy resulting in an economic slowdown, or another recession, increases as this growth continues.

The U.S. Economy is in its ninth consecutive year of expansion and most economists believe that the economic recovery will continue for the next few years. The Department of Commerce records show that the nation's Gross Domestic Product (GDP), the broadest measure of economic activity, has continued to rise over the last four years. In addition soaring consumer confidence, a healthy job market and improving retail sales are giving the U.S. economy a further boost.

Over the last five years, job growth picked up significantly and unemployment rates have continued to decline to more healthy levels, particularly in Silicon Valley. According to data from the Bureau of Labor Statistics, the national unemployment rate peaked at 10.0% in October 2009, the first time the rate had been at 10% or above since 1983. Over the last 12 months, the U.S. unemployment rate has declined from 4.4% in April 2017 to 3.9% in April 2018.

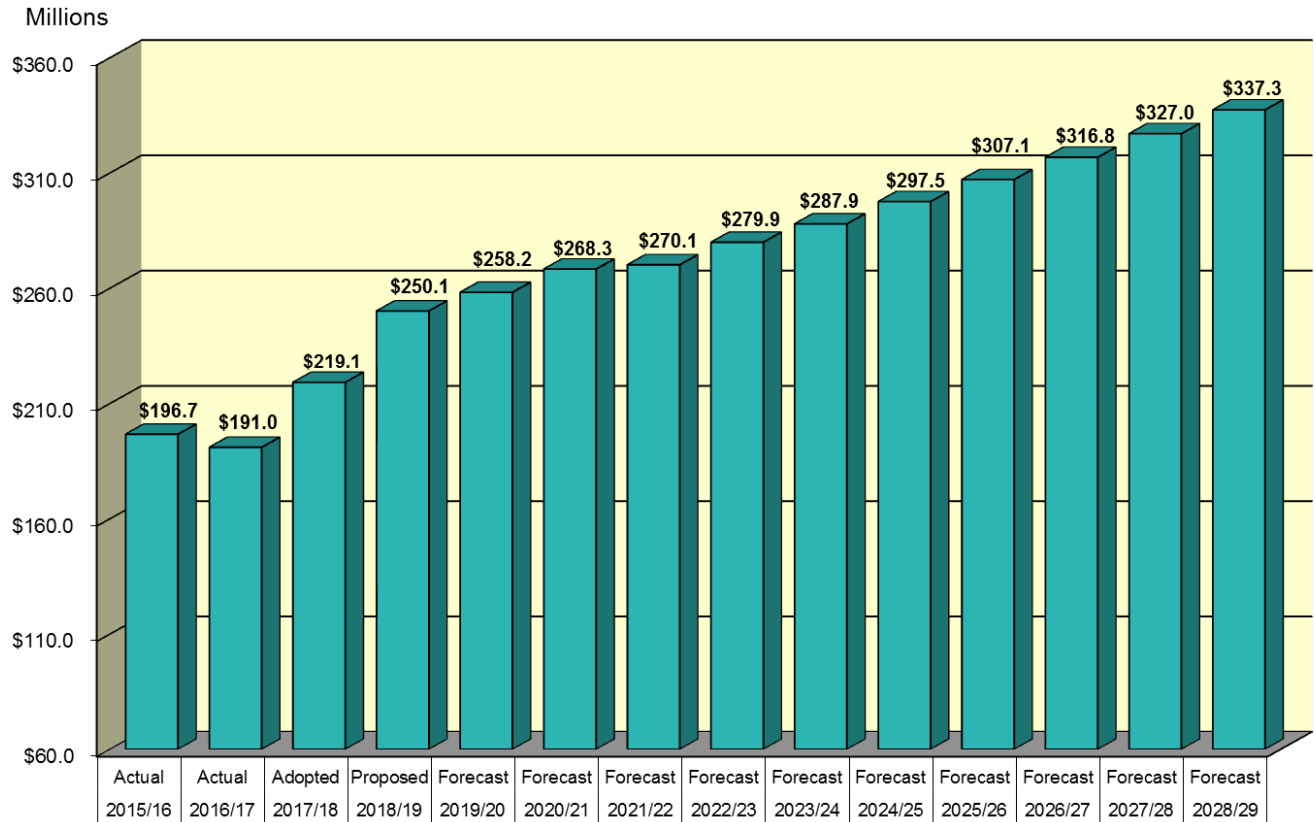
California's economy is projected to remain strong with continued job growth, pressure to raise salaries and hourly rates of pay, and a robust technology industry. The Employment Development Department reported California's unemployment rate rose past the 10% level in February 2009, reached a peak of 12.4% in early 2010, and began declining in late 2010. In the last year, the California unemployment rate declined from 5.2% in March 2017 to 4.3% in March 2018. Santa Clara County's and the City of Santa Clara's experience over the last year have been similar with March unemployment rates declining from 3.4% to 2.6% and 2.7% to 2.5% respectively.

CITY OF SANTA CLARA'S GENERAL FUND

Total General Fund resources are estimated at \$250.1 million in 2018/19, representing an increase of \$30.9 million or 14% when compared to the adopted 2017/18 budget (see Chart 1). The primary reason for this increase is due to a restructuring in budgeting the way transfers are shown in the 2018/19 budget; previously transfers were shown as net transfers in the revenue section of the budget. This budget reflects transfers-in as a revenue and transfers-out as an expenditure. In addition, there were increases in Property Tax due to rising home prices and in Contribution In-Lieu of Taxes received from Silicon Valley Power based on projected increase in customer services charges for electric usage.

As shown in Chart 1, General Fund resources are expected to grow at an average annual rate of 3% in the out years as moderate economic growth continues, reaching an estimated \$337.3 million by the end of the forecast period (i.e., 2028/29).

Chart 1
General Fund Resources



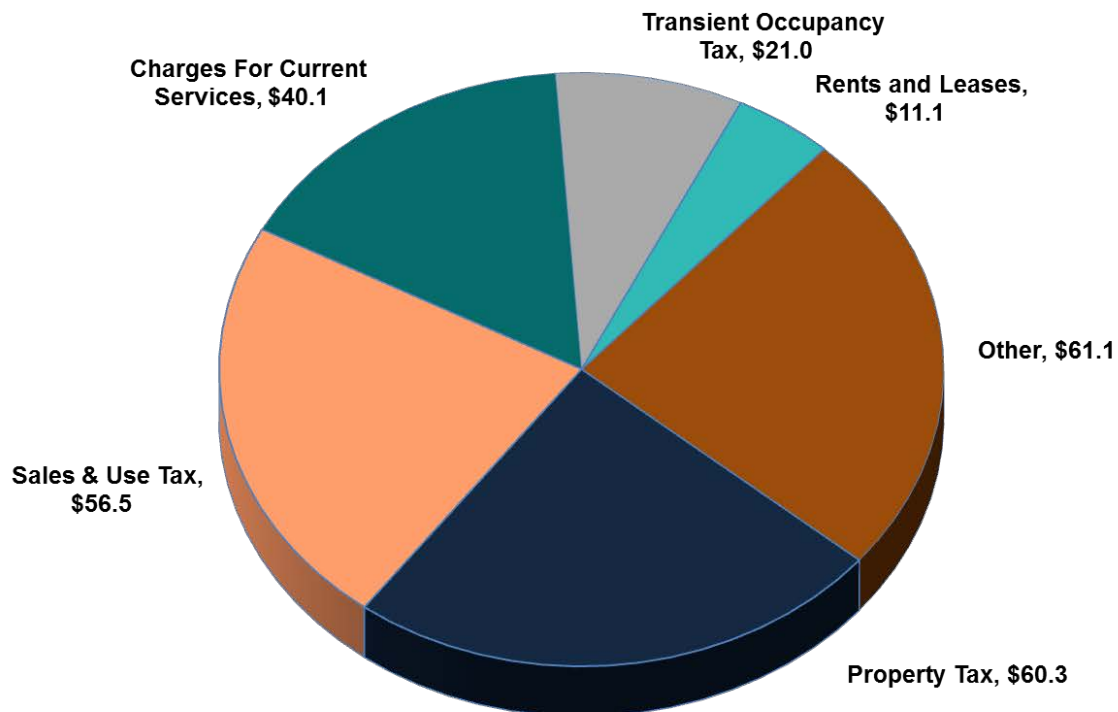
Note: Revenue for years 2018/19 through 2022/23 include transfers-in from the General Fund Capital Reserve Fund to fund projects listed in the City's five-year Capital Improvement Program (CIP) Budget.

Sources of General Fund Revenues

Major sources of revenue for the General Fund are shown in Chart 2. Sales tax and property tax comprise the largest sources of General Fund revenues, representing a combined \$116.8 million or 46.7% of the total. These and other major sources of revenue are described on the following pages.

Chart 2
2018/19 General Fund Resources

Total General Fund Resources = \$250.1 Million



Sales Tax

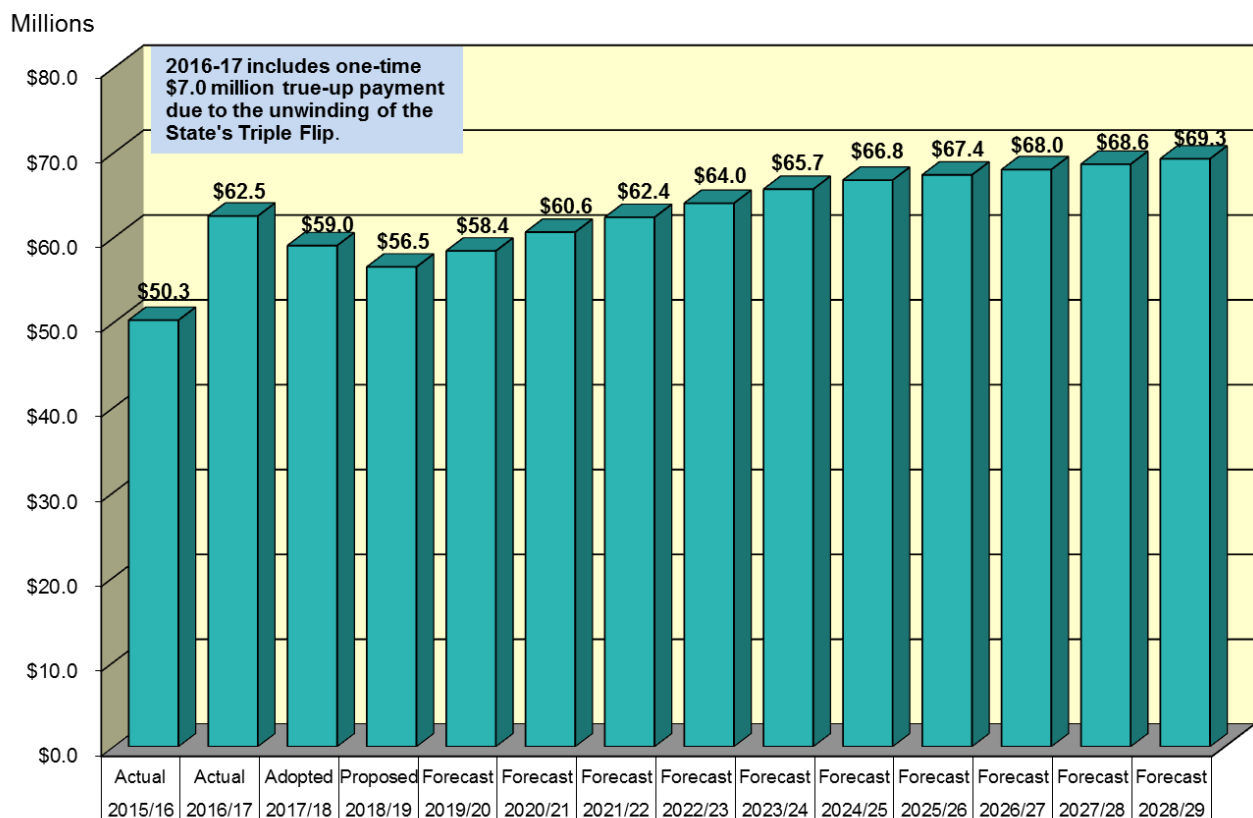
Santa Clara's sales tax collections are directly influenced by local, regional, national, and international economic and business cycles. Because of this, sales tax collections are one of the most economically sensitive General Fund revenue sources. As one of the City's largest revenue sources, sales tax collections reached a dot-com high of \$51.1 million in 2000/01. After falling almost \$17.0 million by 2002/03, collections rebounded to \$43.2 million by 2006/07 as rising home values and stock prices fueled consumer spending. Over the next three years, sales tax revenues fell \$13.1 million or 30% due to the impact of the Great Recession. Sales tax revenues began to grow again in 2010/11, and the strong growth in collections the last five fiscal years is expected to continue in 2018/19 (see Chart 3).

The 2016/17 fiscal year included a one-time \$7.0 million true-up payment due to the unwinding of the State's Triple Flip. The triple flip was due to the State's takeaway of $\frac{1}{4}$ of the local Bradley-Burns 1% sales tax rate which the State then used to guarantee their economic recovery bonds (flip 1). They then directed counties to backfill the loss to local agencies with property tax revenue from the County Education Revenue Augmentation Fund known as ERAF (flip 2). The shortfall in ERAF monies was then backfilled from the State General Fund (flip 3).

The 2018/19 projection of \$56.5 million is a decrease of \$2.5 million when compared to the prior year. This projection is based on information from the City's sales tax consultant, MuniServices. Their estimates are based on individual category/segment projections with adjustments for known individual business anomalies such as missed payments or misallocations.

Collections are expected to grow at an average annual rate of 2.1% over the ten-year forecast period. Based on these projections, annual collections will continue to surpass the 2000/01 all-time high of \$51.1 million.

Chart 3
General Fund Sales Tax Revenue



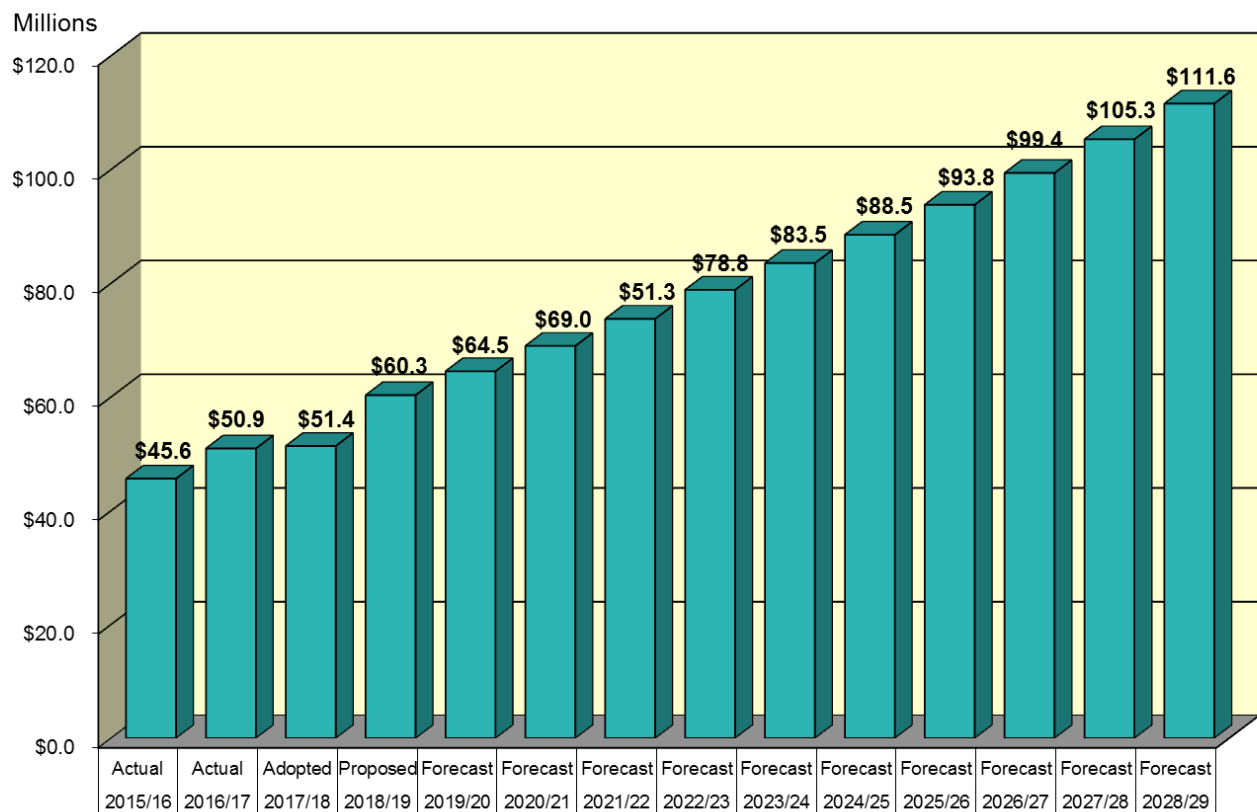
Property Tax

Under Proposition 13, the assessed valuation of properties held by the same owner from year-to-year is adjusted each year by the lesser of 2.0% or the percent change in the October to October California Consumer Price Index (CCPI). For 2018/19 the adjustment factor based on CCPI is 2.0%.

Property tax revenue for fiscal year 2018/19 is projected at \$60.3 million, a 17.4% or \$8.9 million increase from the 2017/18 Adopted Budget of \$51.4 million. Assessed valuation growth on secured property is projected at 2.4% based on rising home values and the value of new construction projects being added to the rolls (see Chart 4). The Property Tax projection is based on information provided to the City from our third party property tax consultant.

Note that these projections do not include new property tax collections for development projects that are either already entitled or currently under review. This Ten-Year Financial Plan only includes new development impacts once the projects are fully entitled and under construction. There are currently billions of dollars of construction projects in various stages of the development review process. Should any of these projects move forward, actual property tax collections should exceed the projections reflected below in Chart 4.

Chart 4
General Fund Property Tax Revenue



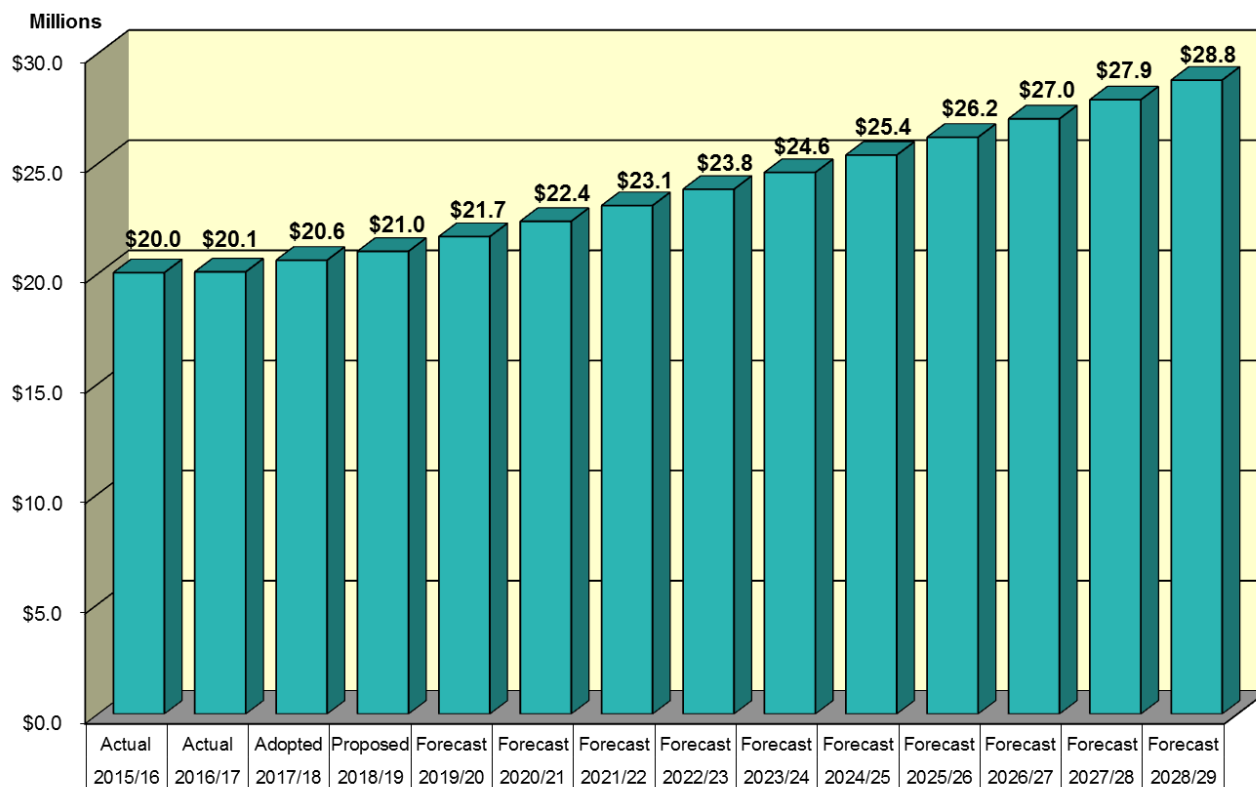
Transient Occupancy Tax

Transient occupancy tax (TOT), also known as hotel/motel tax, is another key revenue source for the General Fund. As with sales tax, TOT is sensitive to business cycles and therefore prone to volatility. After reaching a pre-recession peak of \$11.3 million in 2007/08, this revenue source fell to \$8.1 million in 2009/10. Collections began to grow again in 2010/11 due to the combination of higher occupancy levels and increases in the average daily rate (ADR) and strong growth occurred each year through 2017/18 with year-end collections expected to reach over \$20.0 million (influenced by high weekday demand from tech companies, Convention and Visitors Bureau bookings, and Levi's Stadium events).

Transient Occupancy Tax (TOT) is calculated as a percentage of City hotel/motel room charges. The City's current TOT rate is 9.5%. This revenue stream is extremely sensitive to changes in economic conditions and can vary greatly from year-to-year based on occupancy and room rates. TOT revenue is budgeted to remain relatively flat at \$21.0 million for 2018/19; this is slightly above the 2017/18 Adopted Budget of \$20.6 million (see Chart 5).

The forecast model projects that out-year TOT collections will grow at a rate of 3.2% per year from 2018/19 through the end of the Plan horizon in 2028/29. Although new hotels have been proposed in the Stadium area, they will not be included in the forecast until they start construction.

Chart 5
General Fund Transient Occupancy Tax Revenue



Charges for Current Services

Charges for current services are estimated at \$40.1 million in 2018/19, down by \$1.2 million or 2.8% over the 2017/18 budget of \$41.3 million. This decrease is primarily due to moving Fire prevention fee revenue from Charges for Services to Business Tax revenue to accurately reflect the correct revenue category.

Major sources of revenue within this category include charges for services provided to outside entities and other funds, such as the City's utility enterprise funds of (\$18.9 million), HazMat charges (\$2.9 million), planning and engineering fees (\$8.0 million), and various other customer service fees. The amount charged to outside entities and other funds also includes \$5.7 million to reimburse the General Fund for stadium-related services provided to the San Francisco 49ers and the Santa Clara Stadium Authority.

Contribution In-Lieu of Taxes

In accordance with the City's charter, Silicon Valley Power pays 5.0% of gross revenues to the General Fund as contribution-in-lieu of taxes (CLT). For 2018/19, CLT is projected to total \$23.9 million. The forecast is that CLT will increase to \$30.8 million by the end of the forecast period. The forecast is primarily driven by market projections for electric consumption and any rate increases assumed in the Electric Ten-Year Financial Plan.

Rents and Leases

In 2018/19, revenue recorded as rents and leases is estimated to total \$11.1 million. The amount projected for 2018/19 includes the ground lease with the Santa Clara Stadium Authority for the Levi's Stadium site (includes ground rent and performance rent totaling \$3.0 million), right-of-way rental fees charged to the water and sewer utilities (\$3.3 million), and other smaller leases (\$4.6 million). Growth projections for the Ten-Year Financial Plan are based on individual lease agreements.

Interest Income

The City invests all funds not needed for current cash requirements in accordance with the City Council approved Investment Policy. These funds are invested in securities having a maximum maturity of five years. The factors that directly influence General Fund interest income include prevailing interest rates, the size of the portfolio, and the relative percentage of the portfolio allocated to the General Fund. Over the last several fiscal years, the return on the City's portfolio declined from 4.92% in 2005/06 to a low of 0.68% in August 2014. These declines are primarily due to the extraordinary actions by the Federal Reserve to hold interest rates low. The City's portfolio return has increased over the last year with the April 2018 earnings return coming in at 1.55%. Based on the expectation that the Federal Reserve will gradually increase interest rates over the next couple of years, the General Fund is expected to receive \$4.0 million in interest in 2018/19.

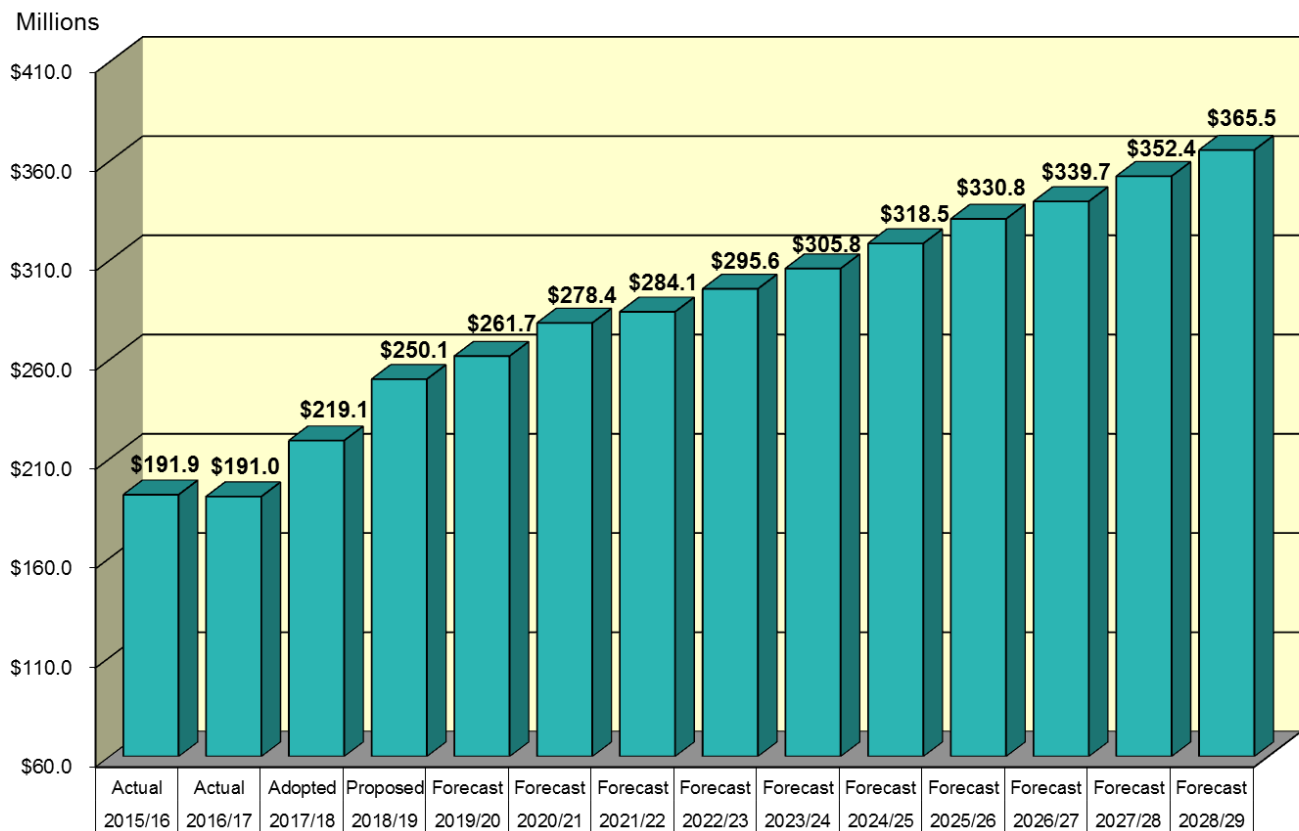
Expenditures

Chart 6 provides historic information on General Fund expenditures. Expenditures are projected to grow to \$250.1 million in 2018/19 and to \$365.5 million by the end of the forecast period. Despite actions to reduce expenditure growth, the primary growth driver continues to be increases in salary and benefit costs. On December 21, 2016, the CalPERS Board of Administration approved lowering the CalPERS discount rate assumption, the long-term rate of return, from 7.5% to 7.0% over the next three years. This will increase the City's contribution costs beginning in 2018/19. Lowering the discount rate means that the City will see increases in both the normal cost (the cost of pension benefits accruing in one year for active members) and the unfunded accrued liability.

Also of importance in this budget is the clear indication of transfers as transfers-in (revenue) and transfers-out (expenditure/expense) versus showing net transfers in the revenue section. This budget change accounts for \$12.8 million of the increase in General Fund expenditures from the Adopted 2017/18 Budget to the Proposed 2018/19 Budget.

Consistent with calendar year Memorandums of Understanding (MOUs), 2018/19 includes general salary adjustments and other benefit enhancements for bargaining groups that have current agreements with the City.

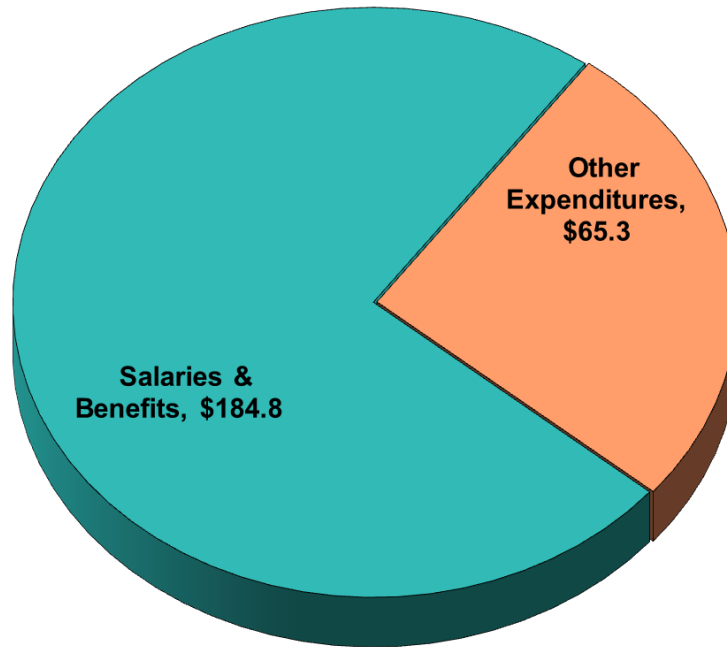
Chart 6
General Fund Expenditures



Note: Expenditures for years 2018/19 through 2022/23 include transfers-out from the General Fund Capital Reserve Fund to fund projects listed in the City's five-year Capital Improvement Program (CIP) Budget.

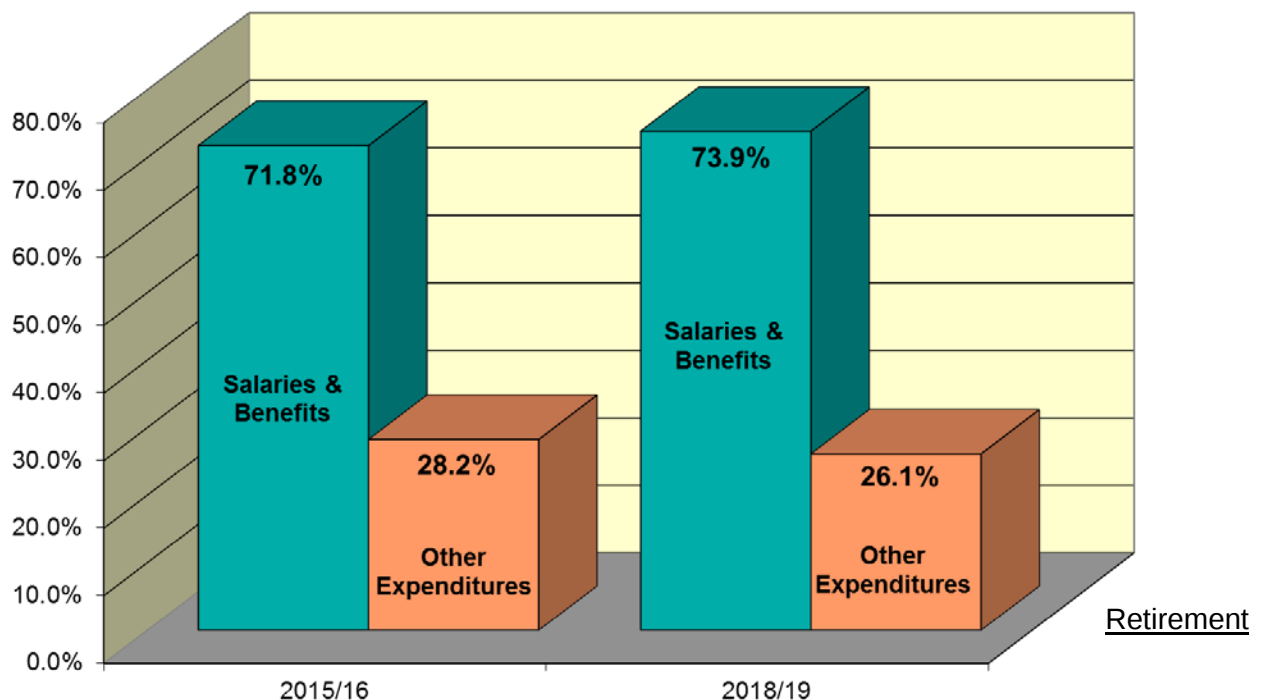
As shown in Charts 7 and 8, salary and benefits costs represent the majority (\$184.8 million) of budgeted 2018/19 operating expenditures.

Chart 8
2018/19 General Fund Expenditure Components
Total General Fund Expenditures = \$250.1 Million



Salary and benefits costs as a percentage of total operating expenditures grew from 72% in 2015/16 to 74% in 2018/19 (see Chart 9). Significant factors driving this growth include the addition of new funded positions, negotiated labor agreements, and rising pension costs.

Chart 9
Time Comparison of Major Expenditure Categories



Costs

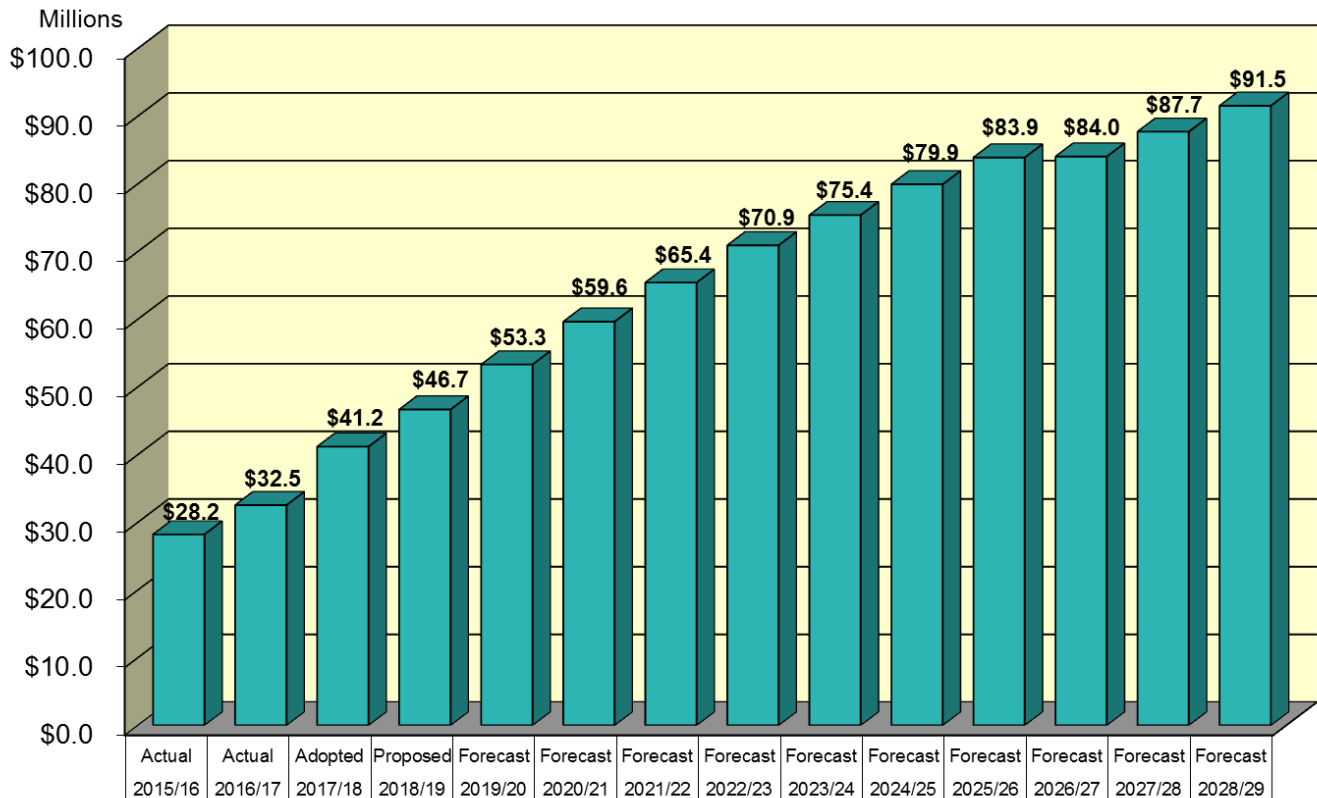
The City contributes to the California Public Employees Retirement System (CalPERS), which provides a defined benefit plan for participating public entities within the State of California. CalPERS offers a menu of benefit provisions that are established by State statutes within the Public Employee Retirement Law. The City selected its benefit provisions from the benefit menu by contract with CalPERS and adopted those benefits through local ordinance, following negotiations with employee bargaining groups.

The City's two defined benefit pension plans (Miscellaneous Plan and Safety Plan) with CalPERS provide retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefits for employees in the Miscellaneous Plan and Safety Plan vest after five years of CalPERS credited service. The retirement benefits under both plans are based on the retiree's age, years of CalPERS credited service, and a benefit factor of 2.7% at age 55 for Miscellaneous Plan members and 3.0% at age 50 for Safety Plan members.

In September 2012, the Governor signed AB 340, the Public Employees' Pension Reform Act of 2013 (PEPRA). This Act replaced existing pension benefit formulas for new hires with new lower benefit formulas for those new members who begin service January 1, 2013 or after. The City's PEPRA Miscellaneous Plan benefit formula is 2.0% at age 62 and the PEPRA Safety Plan benefit formula is 2.7% at age 57. Additionally, the salary basis for the retirement benefit is changed for all new hires from single highest year to highest average annual compensation over a three-year period. These changes are expected to slowly reduce rates over the next generation of employees.

CalPERS retirement costs rose sharply over the past decade as a result of the market losses in the early 2000s followed by benefit enhancements in the mid-2000s. In 2011/12, General Fund pension costs were \$18.9 million, seven years later; 2018/19 pension costs are projected to be \$46.7 million. As shown in Chart 10, retirement payments on behalf of employees are expected to rise dramatically as required employer rate increases are rolled in to make up for investment losses, a lower investment return assumption, shorter smoothing and amortization periods, and other demographic assumption changes including longer lifespans for retirees. These increases accelerated beginning in 2011/12, and continue to ramp up as CalPERS phases each of them in. By the end of the Ten-Year Financial Plan period, PERS expenditures are projected to reach an estimated \$91.5 million and consume an estimated 25% of General Fund revenues.

Chart 10
General Fund PERS Expenditures



The first major driver behind current and future rising retirement costs is the steep market losses experienced during the Great Recession. The CalPERS investment portfolio lost 4.9% in 2007/08 and 24.0% in 2008/09. CalPERS' actuarial assumption at that time was that it would earn a 7.75% annual investment return; this is the rate of growth needed to keep employer rates stable, all other things being equal. Given this assumption, CalPERS fell short of its actuarial estimate by 44.4% over this two year period, placing significant upward pressure on future rates. Rate increases to make up for these losses were phased in over three years beginning in 2011/12.

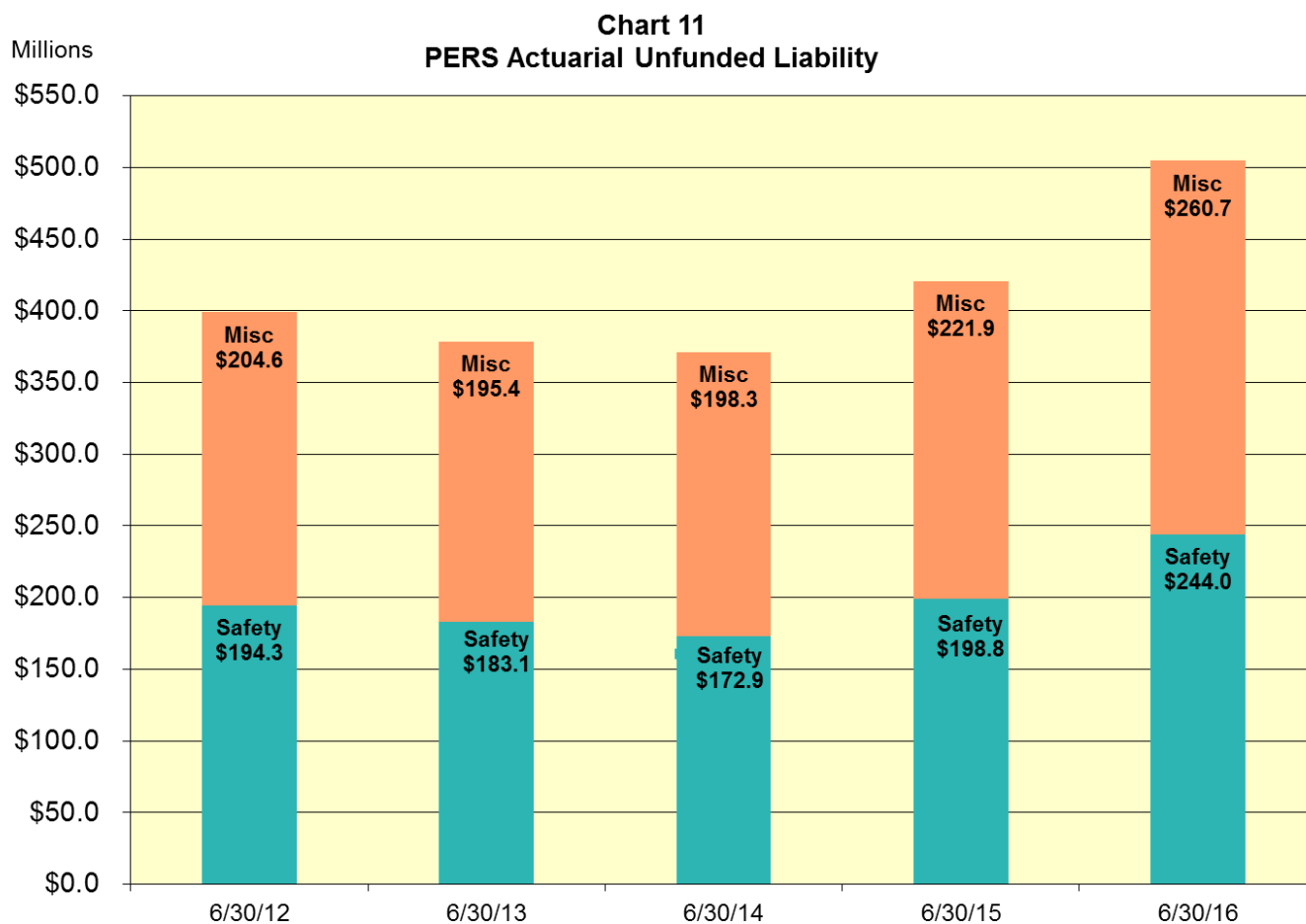
The second major driver behind pension rate increases are decisions made by the CalPERS Board. In 2012, the CalPERS Board revised their investment earnings assumption downward from 7.75% to 7.5% and in 2013 the Board modified smoothing policies from 15-year rolling average to five-year direct smoothing and changed the amortization period for investment gains and losses from a rolling to a fixed 30-year period. These changes were designed to help agencies move toward 100% funding faster than under the prior policies. The lower investment earnings assumption was incorporated into the calculation of rates beginning in 2014/15. The smoothing and amortization policy changes were implemented beginning in 2016/17. In 2014, the CalPERS Board approved new actuarial assumptions including mortality assumptions which show that retirees and their beneficiaries are expected to live longer than previously assumed, necessitating higher rates to fund higher lifetime pension payouts. These changes will be implemented over a five year period beginning in 2017/18. On December 21, 2016, the CalPERS Board approved lowering the investment earnings assumption (discount rate) downward 7.5% to 7.0% over the next three years. This change will increase rates beginning in Fiscal Year 2018/19. Most recently, in February 2018, the CalPERS Board approved shortening the period over which actuarial gains and losses are amortized from 30 years to 20 years for new pension liabilities. This policy will become effective as of the June 30, 2019 CalPERS actuarial valuations.

Year-by-year pension rate projections are shown below in Table 1.

Table 1
Projected CalPERS Employer Rates

Fiscal Year	<u>Percent of Salary:</u>	
	Miscellaneous Plan	Safety Plan
2015/16	29.562%	41.948%
2016/17	32.267%	44.431%
2017/18	33.430%	47.317%
2018/19	35.928%	51.438%
2019/20	40.100%	56.200%
2020/21	42.800%	60.300%
2021/22	45.000%	64.300%
2022/23	46.900%	67.300%
2023/24	48.000%	69.600%
2024/25	49.000%	71.500%
2025/26	49.600%	72.600%
2026/27	45.100%	73.400%
2027/28	45.400%	74.100%
2028/29	45.800%	74.700%

Chart 11 examines the City's unfunded PERS liability. In 2000/01, after years of double-digit returns on PERS investments, the value of the City's assets held by CalPERS actually exceeded projected liabilities, resulting in a super-funded scenario that allowed rates for the Miscellaneous Plan to drop to zero. However, due to investment losses, changes in actuarial assumptions, and benefit enhancements, by June 30, 2016 (the most recent actuarial valuation date) the unfunded liability increased to \$504.7 million with the funded status decreasing to 60.4% for the Miscellaneous Plan and 64.6% for the Safety Plan.



Budget Deficits Projected for the Forecast Horizon

The General Fund is reflecting a budget deficit beginning in 2019/20 and continuing to grow in the out years of the forecast (as shown in Chart 13). While revenues are anticipated to continue to grow at a moderate pace during the ten-year forecast, expenditures are projected to outpace revenues beginning in 2019/20. The primary drivers behind the higher growth rate for expenditures continue to be rising pension rates and increases in salary and other benefit costs.

The 2018/19 General Fund budget is balanced. However there was not sufficient funding to budget for transfers to the Budget Stabilization Fund (formerly the Working Capital Reserve) or to the Capital Projects Reserve. It is anticipated that staff will bring forward a recommendation to allocate funding towards these reserve funds if the FY 2017/18 General Fund includes a surplus at year-end.

It is important to note that revenue projections assume a moderately growing economy throughout the forecast period but do not include project specific revenues that may result from several large commercial and residential development projects currently under review or entitled but not yet under construction. If any of the development projects are completed and yield positive economic benefit, the outlook would improve. In addition, this forecast does not include a possible recession scenario.

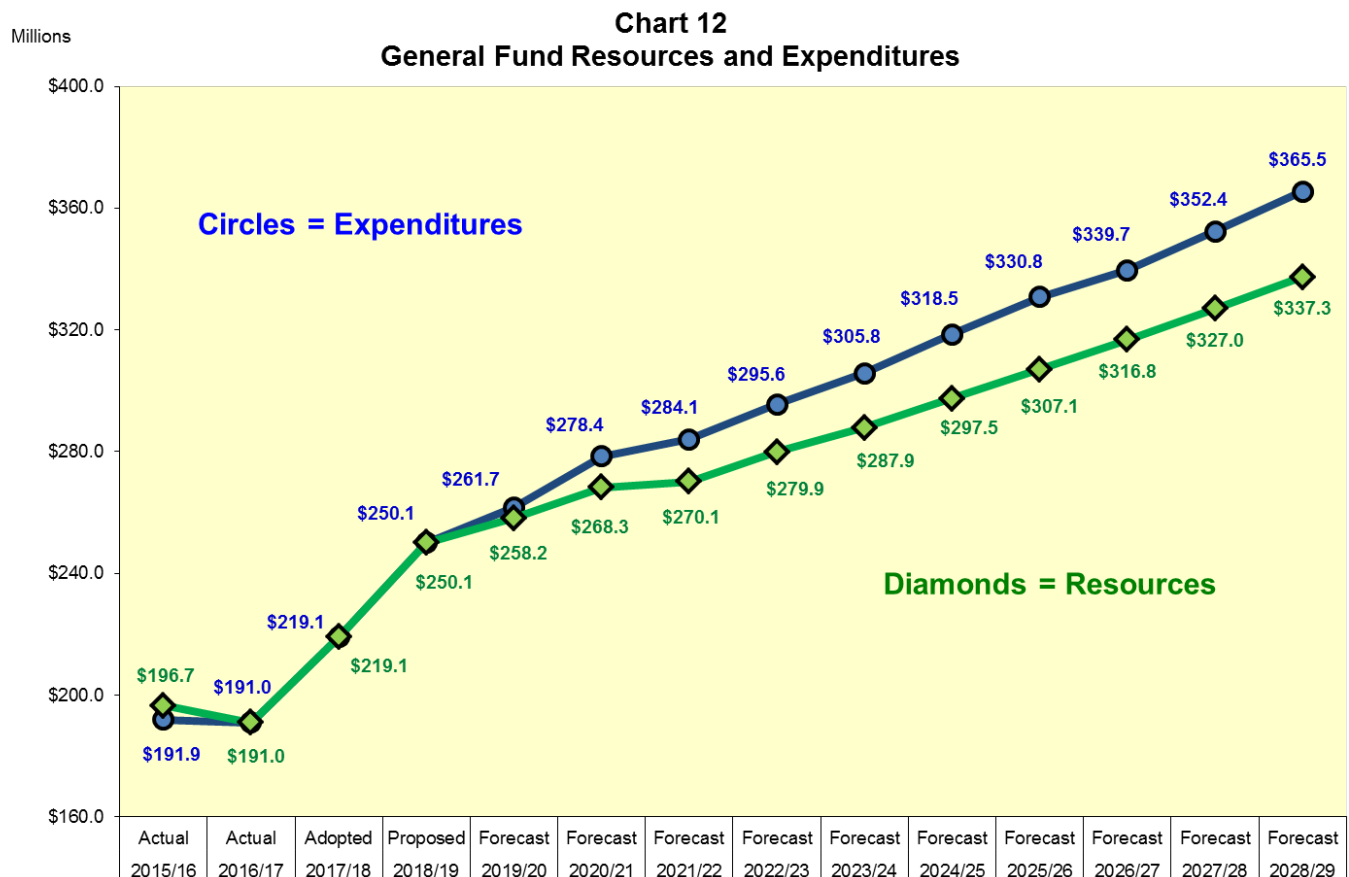
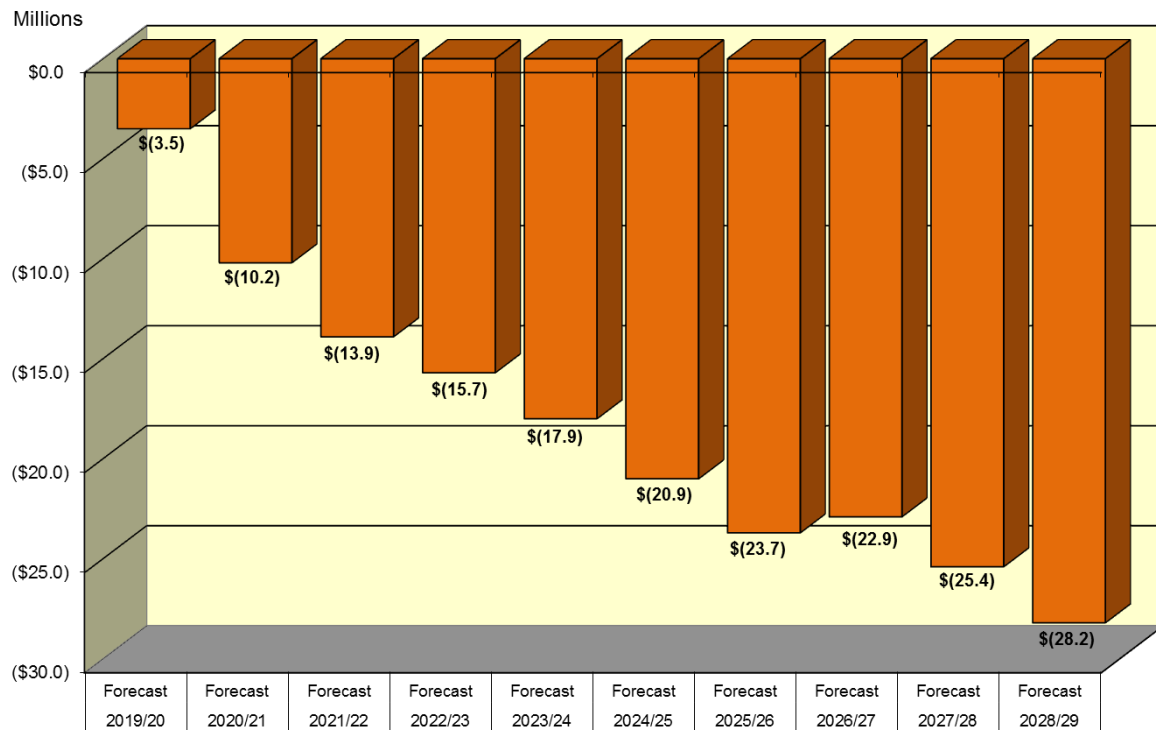
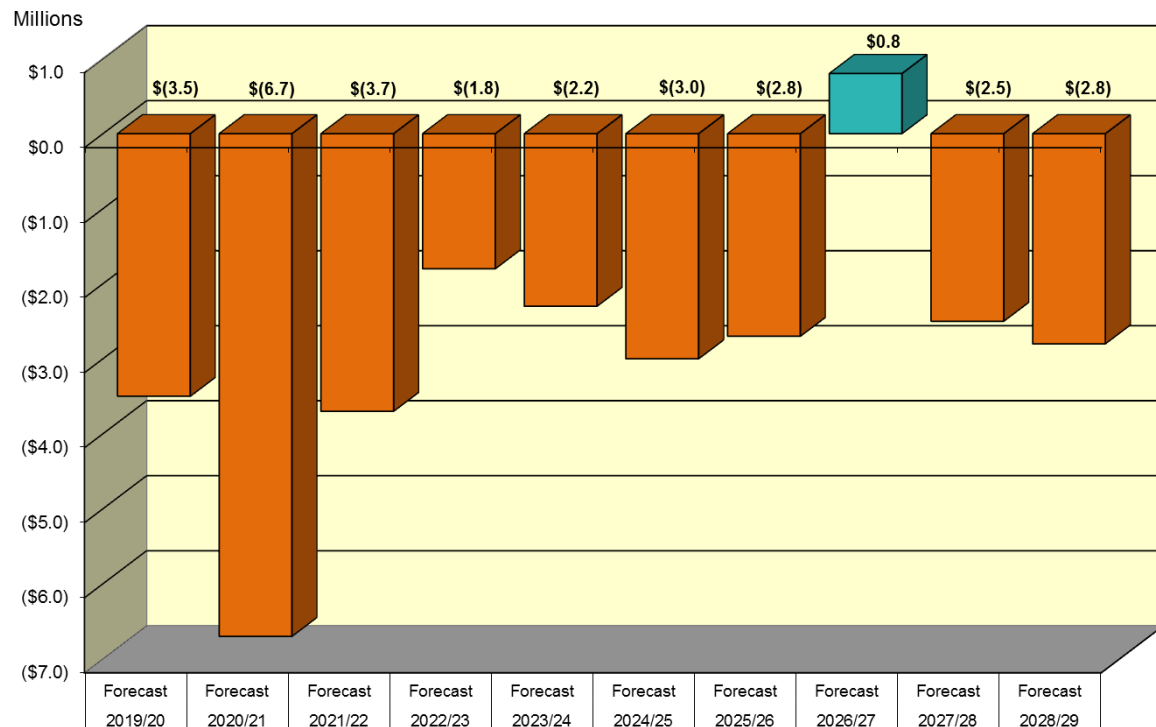


Chart 13
General Fund Operating Surplus/(Deficits)



By committing to correct the deficit each year through fiscal discipline and addressing the annual deficits with cost reductions, alternative service delivery options, or increasing revenue, the year-over-year deficits are forecasted to range between \$1.8 million to a high of \$6.7 million.

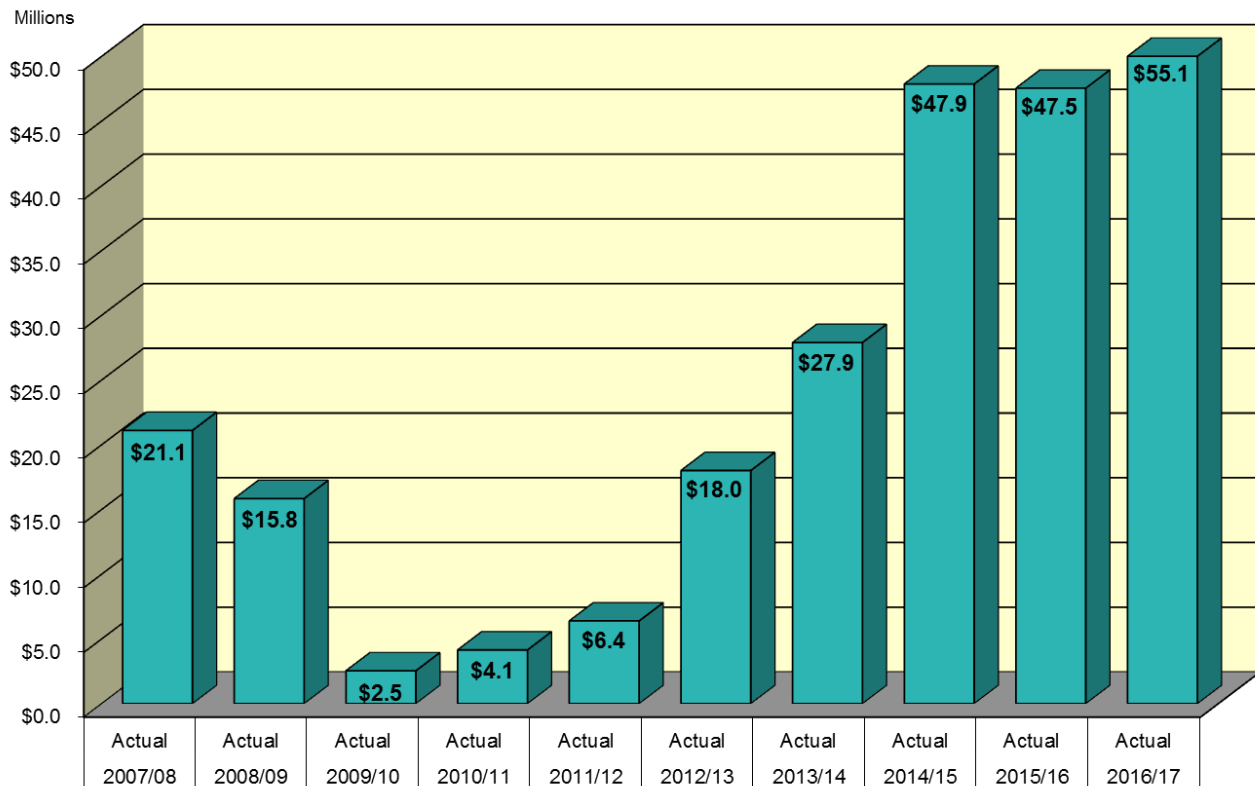
Chart 14
General Fund Net Operating Margin



Reserves

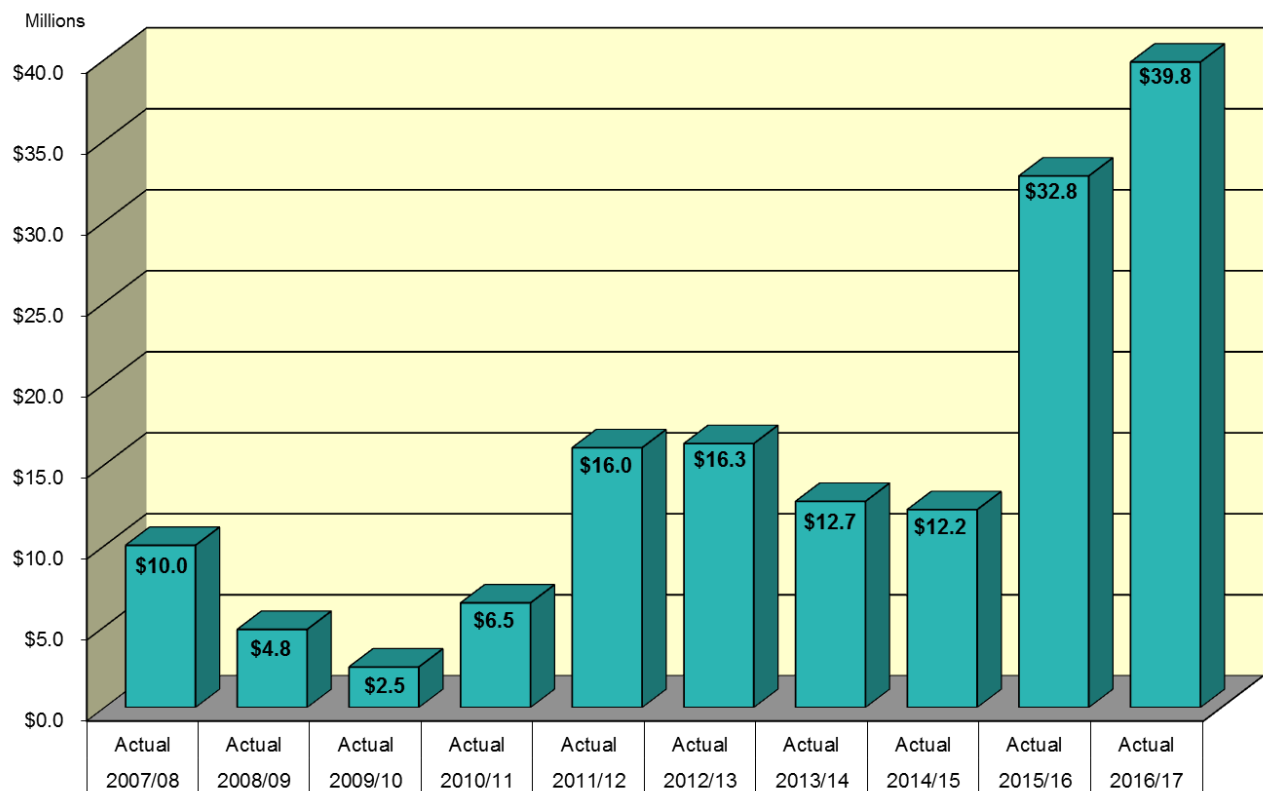
During 1985/86, the City Council established a policy regarding use of the City's General Contingency Reserve funds. Under that policy, two separate reserves were established: a *Working Capital Reserve* and a *Capital Projects Reserve*. To differentiate the Working Capital Reserve from the Capital Projects Reserve and to better reflect the purpose of this reserve, staff is recommending renaming the Working Capital Reserve to Budget Stabilization Reserve. The Budget Stabilization Reserve (BSR) is set aside to protect vital General Fund services through economic downturns, emergency financial crisis, or disaster situations. The reserve target is equal to the expenditures of the City's General Fund operations for three months (90-day or 25% of budgeted appropriations). The BSR reserve level for the end of FY 2017/18 is currently projected to be \$55.1 million. Per Council policy, the FY 2018/19 BSR level needs to be set at \$59.3 million, which is adjusted upward to reflect an increase in expenditures. To make up the shortfall of \$4.2 million, as part of closing the current fiscal year budget, staff will bring forward a recommendation to allocate \$4.2 million of the current estimated FY 2017/18 General Fund surplus of a projected \$7 million.

Chart 14
Working Capital Reserve Ending Balances



The Capital Projects Reserve is set aside to fund the portion of the City's capital spending program that has no other funding sources to support it. The projects funded from this critical reserve provide basic City infrastructure and quality facilities. The Council adopted a policy in 1996/97 to maintain a minimum of \$5.0 million in the Capital Projects Reserve. The Proposed FY 2018/19 & FY 2019/20 CIP Budget includes the expenditure of Capital Projects Reserves in the amount of \$9.9 million in FY 2018/19 and \$7.8 million in FY 2019/20. The remaining balance in the Capital Projects Reserve equals \$21 million and is allocated towards approved projects included in the Capital Improvement Program Budget. It is estimated that the Capital Projects Reserve will be depleted by the end of fiscal year 2022/23, if no additional action is taken by the City Council to replenish this fund. As with the Budget Stabilization Reserve, the Fiscal Year 2018/19 Proposed General Fund Operating budget does not anticipate any savings and/or surpluses; therefore, no transfer of funds have been included to the 2018/19 Capital Projects Reserve. However, as part of closing the FY 2017/18 Budget, the City Council may allocate a portion of the General Fund surplus to the Capital Projects Reserve.

Chart 15
Capital Projects Reserve Ending Balances



ENTERPRISE TYPE ACTIVITIES

The City owns and operates various enterprise type activities including the Electric, Water, and Sewer utilities, City Cemetery, and Solid Waste program. A five-year projection of major enterprise fund revenues and expenses is included in the attached schedules. The projections were prepared by the respective entities with underlying economic and other pertinent assumptions that may differ from those outlined in this plan. Presentation of enterprise fund information in this plan is designed to draw attention to their financial relationship to the City's General Fund.

Silicon Valley Power

Silicon Valley Power (SVP) provides electric power and services to over 55,000 City customer accounts. In calendar year 2017, the City of Santa Clara served approximately 1,660 industrial accounts that comprised 90% of the City's load and more than 88% of customer service revenues. The Electric Department provides diverse services including operating, maintaining and dispatching electric service, engineering, system design and planning, administrative and financial management, marketing, customer services, wholesale power trading, free outdoor Wi-Fi (powered by SVP Meter Connect) and dark fiber leasing services -- all of which makes Silicon Valley Power a successful and reliable resource for the City and its citizens. SVP owns power generation facilities, invests in joint ventures on generation and transmission projects, and trades wholesale power on the open market. Its primary goals are to provide safe, reliable service while remaining competitive in the marketplace and placing a premium on a high level of customer satisfaction. While the business environment has changed due to high-tech load growth, SVP remains dedicated to responsive, low cost and reliable customer service.

Over the next ten years, SVP will continue to build and expand its state-of-the-art power and communications infrastructure. SVP's mission is to be a progressive, service-oriented utility, and to offer reliable, competitively priced energy services for the benefit of Santa Clara and its customers. This means implementing energy efficiency programs, green technologies, ensuring reliable service, streamlining operations, and improving communications. SVP continually works with Santa Clara customers to enhance the value they receive from municipal ownership of their electric utility.

Also, over the coming years, SVP will take significant measures to proactively comply with continually increasing legislative and regulatory mandates such as California's Renewable Portfolio Standard (RPS) and the Cap-and-Trade Program. The State's RPS program requires electric service providers to increase procurement of eligible renewable resources to 33% of total procurement by 2020, and in 2015 the Governor signed Senate Bill 350 increasing that to 50% of total procurement by 2030. While SVP already exceeded state-wide RPS goals for Compliance Period 1 and 2 (2011-2016) and expects to fulfill the requirement for Compliance period 3 (2017-2020), the RPS requires the Utility to continue its support of this broad range of programs encouraging wise use of energy resources, especially renewable energy generation. The California Cap-and-Trade Program began in mid-2012 and intends to cap and reduce CO2 emissions by auctioning emission allowances and investing the proceeds in consumer benefits such as energy efficiency, renewable energy, and other clean energy technologies. At the Federal level, the North American Electric Reliability Corporation (NERC) has issued new reliability standards with mandatory requirements to ensure power system reliability throughout the country. SVP has established a framework to assure that the City is in and stays in compliance with NERC mandatory standards. Furthermore, Fitch Ratings upgraded the rating on SVP's revenue bonds to AA- from A+ and Standard and Poor's Global Ratings revised SVP's outlook to stable from negative, reinforcing the need to maintain a positive net income during normal operating years and keep Electric Utility reserves over the \$120 million target.

The cost of producing and procuring energy is projected to increase primarily due to higher electric transmission costs, increased gas transportation costs, and higher power purchase and generation expenses to serve the projected increase in retail load. Because the additional renewable resources were acquired to meet future state mandates and are not immediately needed for current period compliance, the higher costs are being partially offset by wholesale sales of the bundled renewable energy. Special

efforts are made to assure that costs for the procurement of natural gas and emissions allowances for carbon are properly projected.

To ensure safety and comply with reliability requirements, SVP continues its multi-year substation rebuilding projects. The forecast assumes capital expenditures including substation upgrades, equipment replacement, new technology deployment, and economic development projects. The Phase Shifting Transformer has been reducing the operating costs as well as improving the Utility's reliability. This project was funded by a short-term loan, which will be repaid through the operating cost savings.

In other ongoing capital projects, the Electric Department continues to improve, demonstrate, and implement new technologies to support tomorrow's power grid. Some key projects being deployed in this area are the continuing development of an Advanced Metering Infrastructure (AMI) Project; the SVP Meter Connect program (which powers the City's free outdoor Wi-Fi); the ongoing Operational and Technology Project, updating the power scheduling and back office systems required to schedule, track and settle power purchase and sales transactions; LED streetlight upgrade projects; and the improvement of the electric system cyber and physical security as required by mandatory federal reliability standards.

SVP continues to improve electric infrastructure to provide a reliable and low-cost business environment so Santa Clara's economy can grow and thrive. Rapid growth in energy demand, aging grids, communication technologies, and environmental impacts are driving change in how utilities do business and operate. New services, customer demand, and regulatory requirements continue to drive the need for advanced technology solutions to improve customer energy services.

The Electric Department's Ten-Year Financial Plan assumes a 2% rate increase in each of the next three fiscal years, 2018/19 through 2020/21, subject to further review and to City Council approval. The inflationary rate increase is needed to cover the increasing transmission and gas transportation costs. Additionally, it is important that we maintain our current reserve levels at the \$120 million target in the event there is a market disruption causing prices to increase beyond what was projected. Santa Clara's Electric Utility continues to offer among the lowest electric rates in the State of California while maintaining a strong balance sheet.

Water and Sewer Utilities

Water Utility expenditures are projected to increase by 14% between 2017/18 and 2018/19 and increase up to 7% per year over the ten-year planning period, primarily due to projected increases in the wholesale cost of water. Moderate increases are also projected in salaries and benefits, right-of-way fees, other operating expenditures, and Internal Service Fund allocations.

Sewer Utility expenditures are projected to increase 8% between 2017/18 and 2018/19 and approximately 3% per year for the duration of the ten-year forecast period. Increases are driven primarily by increases in operations and maintenance (O&M) costs for the San Jose/Santa Clara Regional Wastewater Facility (RWF), as well as moderate increases in salaries and benefits, right-of-way fees, and Internal Service allocations.

The exceptions to the 3% per year increase occur in Fiscal Years 2019/20 and 2021/22, during which there is an expected 15% increase in expenditures over the previous years. These increases are driven primarily by debt service payments on expected debt issuance in 2018/19 and 2020-21, respectively. This debt is being issued to keep rates from increasing significantly to cover capital expenditures at the San Jose/Santa Clara Regional Wastewater Facility (RWF), as well as to spread the cost of RWF improvements over a 25-year period.

Recycled Water Utility expenditures are projected to increase by 9% between 2017/18 and 2018/19, and by 8% per year over the remainder of the planning period. Increasing demand for and sale of, recycled

water, as well as wholesale purchase costs of recycled water, are the primary components of the projected increases.

Even with the projected increases in expenditures, the Utilities anticipate maintaining combined water, sewer, and recycled water rates at a competitive level that is affordable for residents and attractive for businesses.

Parks and Recreation Department Cemetery Division

In continuous operation since 1864, Mission City Memorial Park (MCMP) is a 25+ acre historic property, a place of reverence and peace. Parks and Recreation staff honors the Park's past and are positioning MCMP for the future.

Fees for interment rights and services are reviewed annually to ensure they are set appropriately. The inventory of available graves, niches, and crypts is managed to ensure residents have continued choices. Marketing strategies are employed to ensure Santa Clara residents are aware of MCMP as an excellent choice for their final resting place. Expenses are continuously evaluated to ensure resources are used efficiently and effectively, while maintaining MCMP in optimal condition.

In fiscal year 2016/17 a fee study was performed. As a result of the study some components of burial fees were reduced and/or combined in fiscal year 2017/18, resulting in greater affordability and a more clear process for the resident-customer. While the trend for the previous three years showed increased revenue of 5%, the near term forecast projects flat revenues, except for interment rights and perpetual care which will need to increase as a function of maintaining cost recovery levels.

The categories of sales (components of burial) are as follows:

1. Interment rights (facilities) are a one-time fee which reserves a person's space in a grave, niche, or crypt;
2. Perpetual care (endowment) is a one-time fee collected for each person interred and whose principal and growth is reserved and portion of interest on growth is used to support future maintenance of the grounds and buildings;
3. Materials sold include burial vaults, flower vases and rings, niche plaques, and mono-bars;
4. Marker setting fees include the permanent placement of a personalized stone marker onto a grave;
5. Site preparation (labor) includes staff time required to prepare a site for burial, it is collected only at time of need, and each time the site is accessed.

To assure funds are available to support the maintenance grounds and buildings, a 25% increase was applied to interment rights and perpetual care (endowment) in fiscal year 2018/19.

The Cemetery's salaries and benefits, other operating expenditures, and Internal Service Fund allocations are projected to increase by 4% per year over the ten-year planning period.

CONCLUSION

The Ten-Year Financial Plan provides policy-makers and the public an updated assessment of the City's financial condition that takes into account the latest projections of economic conditions. The benefit of the Ten-Year Financial Plan is to provide the City Council, staff, and community a clear assessment of the City's finances and facilitate an informed discussion during budget deliberations. The Plan serves as a starting point to provide perspective and analysis of what will happen if current financial decisions and operating practices continue into the future.