



## Agenda Report

21-43

Agenda Date: 2/23/2021

### REPORT TO COUNCIL

#### SUBJECT

FY 2020/21 Budget Rebalancing Actions to Address COVID-19 Pandemic Impacts

#### COUNCIL PILLAR

Enhance Community Engagement and Transparency

#### BACKGROUND

The FY 2020/21 budget was adopted during a time of unprecedented uncertainty with both a global public health and economic crisis as a result of the COVID-19 pandemic.

The pandemic suddenly altered the trajectory of the national economy and, while the long-lasting impacts are still not known, they have already been significant for residents, businesses, and the city. Prior to COVID-19, the City's financial forecast was manageable and well-planned; however, like many other cities, COVID-19 has had significant impacts on all facets of regular life and, likewise, is the source of these fiscal impacts presented in this report.

At a local level, several of the City's General Fund revenues have been impacted, with the largest declines in the transient occupancy tax and fees for services categories. When the budget was approved by the City Council in June 2020, the Budget Stabilization Reserve was used to close the projected General Fund deficit of \$22.7 million as a first step. The strategy of revisiting the City's fiscal condition during FY 2020/21 was put into place for the purpose of obtaining more economic data, evaluating the duration of COVID-19, and developing expenditure reduction proposals. As the year has progressed, the economic effects from the pandemic have continued, with more severe impacts on the City's revenues than originally anticipated. Through strong fiscal management efforts, the City has been able to develop proposals that suspend expenditures where appropriate due to COVID-19, minimize service delivery impacts, to the extent possible, and avoid employee layoffs.

This memorandum was originally scheduled for Council consideration on September 29, 2020 with subsequent follow-up in December 2020. However, this item was deferred to February 2021 to allow additional time for potential federal stimulus funding to be determined. While the federal stimulus package has not yet been finalized, this action is recommended to move forward at this time given that stimulus funding is not expected to be sufficient to address the current year shortfall and the FY 2021/22 deficit of \$41.7 million. Additional actions are planned to be brought forward as part of the FY 2021/22 and FY 2022/23 Biennial Operating Budget and could factor in any stimulus funding received.

An incremental approach to addressing the COVID-19 related shortfalls will continue to be used to allow time to evaluate the longer-term impacts of COVID-19, implement cost reduction strategies that start with those with moderate impacts and progressively move to those with more significant impacts, and to evaluate other balancing actions such as revenue solutions, the labor negotiations,

and the strategic use of reserves.

### **DISCUSSION**

Since the adoption of the budget, staff has continued to monitor COVID-19 economic impacts on the City's revenues. Many of the economic indicators experienced steep declines at the beginning of the pandemic but have continued to improve. On a national level, the U.S. unemployment rate was 6.7% in December 2020 and the number of unemployed persons totaled 10.7 million, which were well below the peak in April 2020 but remain well above the pre-pandemic levels in February 2020 (3.5% unemployment and 5.7 million unemployed). Significant impacts have also been experienced on the State and local level. The unadjusted unemployment rate in the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (MSA) was 6.0% in December 2020, up from a revised 5.2% in November 2020 and significantly higher than the December 2019 level of 2.3%. Between December 2019 and December 2020, employment in this region dropped by 80,300 jobs, or 6.9%.

Staff has continued to evaluate the impact of COVID-19 on the City's revenues. Unfortunately, based on the latest data available, the drop in revenues in FY 2020/21 is now expected to be greater than originally anticipated when the budget was adopted in June 2020. General Fund revenues are now tracking to fall \$20 million - \$25 million below the budgeted estimate. Budget actions to address \$17 million of this shortfall are included in this report. Additional downward adjustments may be necessary at year end, and the goal would be to offset these lower collections with expenditure savings to the extent possible. These impacts are in addition to the \$22.7 million budget shortfall addressed in June 2020 with the use of the Budget Stabilization Reserve. Of the \$17 million in budget balancing actions included in this report, 70% of the additional deficit is proposed to be closed with ongoing solutions. The remaining 30% reflects one-time cuts and savings from COVID-19 activities that are prohibited at this time.

### **February 2021 Budget Balancing Actions**

The budget actions recommended in this memorandum address the additional drop in revenues identified since the adoption of the budget. The table below summarizes the revenue and expenditure adjustments. The details associated with these revenue and expenditure actions are included in Attachments 1 and 2 to this memorandum.

**Table 1: February 2021 General Fund Budget Balancing**

<b>General Fund Adjustments</b>	<b>2020/21 Source of Funds</b>	<b>2020/21 Use of Funds</b>
Revenue Adjustments	(\$17.3 M)	
COVID-Related One-Time Expenditure Reductions		(\$5.2 M)
Other Expenditure Reductions		(\$12.1 M)
<b>Total Adjustments</b>	<b>(\$17.3 M)</b>	<b>(\$17.3 M)</b>

### **Revenue Adjustments**

The revenue adjustments recommended in this memorandum are summarized in the chart below and detailed in Attachment 1. The largest adjustment is to the transient occupancy tax (TOT) category that has been the most severely impacted by COVID-19. Other downward adjustments are recommended to the charges for services, interest earnings, and fines and penalties categories that have also been impacted this year. The FY 2022 - FY 2032 Ten-Year General Fund Forecast also

factored in these lower collection levels.

These downward adjustments are partially offset by the increases that are brought forward as budget balancing actions. These include reimbursements for staff costs associated with the Clean-Up Campaign and transfers from other funds.

**Table 2: Proposed General Fund Revenue Adjustments**

Category	FY 2020/21 Impact
Transient Occupancy Tax	(\$14.0 M)
Charges for Services	(\$2.2 M)
Interest Earnings	(\$1.1 M)
Fines and Penalties	(\$0.2 M)
Transfer from Other Funds	\$0.2 M
<b>Total Adjustments</b>	<b>(\$17.3 M)</b>

Additional revenue adjustments may be necessary at year end. State challenges to the Education Revenue Enhancement Fund (ERAF) property tax distribution and changes to the distribution of former Redevelopment Agency residual receipts may result in a property tax shortfall of up to \$4 million. Sales tax collections, which are trending better, may end the year slightly below budget.

#### Expenditure Adjustments

Budget actions are recommended in this memorandum to offset additional revenue declines. These actions, however, are not sufficient to restore the Budget Stabilization Reserve that was used to balance the FY 2020/21 budget in June.

The recommended proposals reduce costs by \$17.3 million in FY 2020/21 and \$12.3 million on an ongoing basis. Over \$5 million of these reductions in FY 2020/21 are possible due to the COVID-19 restrictions that have limited City operations, with the largest reductions in the Parks and Recreation Department. These proposals recognize the reduced level of staffing and services currently being provided.

The proposed General Fund expenditure reductions are broken down by department in the following table.

**Table 3: Proposed General Fund Expenditure Proposals by Department**

Department	Net Position Change	FY 2020/21	Ongoing
Mayor and City Council		(\$0.1 M)	(\$0.0 M)
City Attorney's Office	(1.00)	(\$0.2 M)	(\$0.2 M)
City Auditor's Office		(\$0.2 M)	(\$0.0 M)
City Clerk's Office	(1.00)	(\$0.2 M)	(\$0.2 M)
City Manager's Office/Non-Dept.	(4.00)	(\$2.3 M)	(\$2.0 M)

Community Development	(1.75)	(\$0.6 M)	(\$0.4 M)
Finance	(1.00)	(\$0.4 M)	(\$0.4 M)
Fire	(12.75)	(\$2.1 M)	(\$2.6 M)
Human Resources		(\$0.4 M)	(\$0.2 M)
Library		(\$0.7 M)	(\$0.3 M)
Parks and Recreation	(4.00)	(\$5.5 M)	(\$1.7 M)
Police	(15.00)	(\$3.6 M)	(\$3.6 M)
Public Works	(3.00)	(\$1.0 M)	(\$0.7 M)
<b>Total Adjustments</b>	<b>(43.50)</b>	<b>(\$17.3 M)</b>	<b>(\$12.3 M)</b>

Note: the figures above include reductions information technology services, fleet and vehicle replacement that are budgeted in internal services funds.

These proposals are detailed by department/office in Attachments 1 and 2 and are highlighted below.

- Police Department - eliminates vacant sworn and non-sworn positions that support various units and programs, including training, professional standards (recruiting and outreach), special events support, the drone program, parks patrol, records support, police officer field training program, community service officers, and the task force unit. Reductions are also proposed to non-personnel costs such as supplies and materials and contractual services.
- Fire Department - eliminates vacant positions, suspends the two supplemental ambulances, reduces minimum staffing overtime, and reduces the non-personnel budget for maintenance, supplies, training and conferences.
- Parks and Recreation Department - reduces staffing and non-personnel costs on a one-time basis to reflect COVID-19 related changes in services and programming, restructures special events programming and elements, reduces parks maintenance staffing, shifts eligible staffing costs to Quimby and Mitigation Fee Administration fees, eliminates Teen Center administrative staffing, reduces contributions to other agencies, and reduces conference, travel, and training funding for staff and commissions.
- Library Department - reduces staffing and non-personnel costs on a one-time basis to reflect COVID-19 related changes in services, reduces library materials funding including an unsustainable pay-per-use digital collection that would be implemented once the libraries are reopened, and reduces non-personnel costs for overtime, conference, training and travel as well as routine maintenance, supplies, events and activities, and marketing.
- Community Development Department - reduces staffing for Planning Division plan review and administration, reduces non-personnel funding for staff and commission training, and shifts eligible costs to CDBG funding for Emergency Rental Assistance Program administration.

- **Public Works** - eliminates vacant positions in the Design Division and the Traffic Division, reduces as-needed staffing support, reduces fleet operations and vehicle replacement funding (reflected as lower General Fund contributions to internal service funds), and reduces non-personnel funding for fountains at City Hall and Franklin Square, training and travel, operating supplies, contractual services, and facility maintenance.
- **City Manager's Office and Non-Departmental** - eliminates 1.0 vacant Assistant City Manager position and shifts funding for the City Librarian transition/recruitment, reduces the non-personnel budget for contractual services, conference, travel, and training, eliminates contingency funds for the City Manager's Office and reduces contingency funds for City Council, reduces community grants and special community groups funding on a one-time basis as a result of COVID-19, and reallocates the Risk Manager position to the Human Resources Department.
- **Strategic Support Departments** - reduces the Summer Internship Program, Leadership Program and employee recognition luncheon as a result of COVID-19, and reduces the non-personnel budget in the Human Resources Department; eliminates a vacant Deputy City Clerk position and reduces material, services, supplies and training in the Assistant City Clerk Office; reduces network infrastructure, security consultant staffing, contractual and consultant services, and Unisys staffing in the Information Technology Department (reflected as lower General Fund contributions to internal service funds); and eliminates administrative support, reduces the supplies and materials budget, and reorganizes the accounting and budget functions in the Finance Department.
- **Consideration of City Council and Council Appointees Proposals (Attachment 2)** - reduces as-needed staffing and conference, training, and travel funding for the City Council; eliminates a vacant Legal Office Specialist position and funding for materials, services, supplies and training in the City Attorney's Office; and recognizes one-time vacancy savings from the City Auditor position in the City Auditor's Office.

The recommended budget actions result in the net elimination of 43.5 positions. This includes four filled positions where employees would be reallocated to other departments and/or reallocated to perform different functions. These actions maintain the goal of preserving jobs and preventing layoffs.

#### General Fund Reserves

The General Fund has several reserves that may be considered for use as part of the budget balancing actions moving forward, including those identified in the table below:

**Table 4: Major General Fund Reserve Status**

<b>Reserve</b>	<b>2020/21 Balance</b>
General Fund Budget Stabilization Reserve	\$57.7 M
General Fund Capital Projects	\$5.4 M
Land Sale Reserve	\$23.7 M
Pension Trust (General Fund)	\$21.6 M

Any use of reserves would be considered one-time in nature and would only provide additional time to evaluate ongoing proposals or mitigate some of the service impacts that could result from future proposals. Budget balancing going forward must continue to contain ongoing expenditure reductions or additional ongoing revenues.

#### Employee Engagement

Online surveys and a suggestion drop box were provided as an opportunity for employees to submit cost-saving ideas. In addition, individual departments engaged employees for ideas that could achieve General Fund savings. Some of the themes of the suggestions include:

- Equity of pay reduction considerations
- Furloughs
- Early retirement program (CalPERS Golden Handshake)
- Reduced community services (e.g., fewer hours)
- Executive management pay cuts
- City Manager's Office position reductions
- Establishing new or increasing fees
- COVID-19 compliance fines

While a level of employee engagement took place, this process was also impacted by COVID-19 workplace restrictions. As such, departments were requested to work with their staff for departmental reduction proposals prior to submitting them to the Finance Department. Proposals were then evaluated based on mitigating service impacts, complying with labor agreements, and feasibility.

#### Moving Forward

The budget actions recommended in this memorandum are the first round of budget proposals to address the revenue shortfalls associated with current economic environment and COVID-19. These actions focus on expenditure reductions that are possible due to COVID-19 restrictions on service delivery as well as actions that avoid layoffs and major service delivery impacts.

In January 2021, staff prepared the Ten-Year General Fund Forecast that projects a shortfall of \$41.7 million in FY 2021/22. If the reductions proposed in this memorandum are approved, a General Fund shortfall of almost \$30 million will remain to be addressed in the FY 2021/22 and FY 2022/23 Biennial Operating Budget process as shown in the table below.

**Table 5: Ten-Year General Fund Forecast**

	<b>January 2020 Forecast</b>	<b>April 2020 Forecast</b>	<b>January 2021 Forecast</b>	<b>February 2021 (Assume Phase 1 Approved)</b>
General Fund Shortfall	(\$13 M)	(\$34 M)	(\$42 M)	(\$30 M)

The FY 2021/22 and FY 2022/23 Biennial Operating budget process will incorporate the continued refinement of the revenue estimates as well as budget actions that close the projected shortfalls with the goal of using ongoing solutions to the extent possible. The plan will also incorporate revenue solutions and use of reserves to balance the competing goals of aligning ongoing revenues and expenditures and minimizing the service delivery impacts to the community.

**COORDINATION**

This report has been coordinated with the City Attorney's Office and all city departments.

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall Council Chambers. A complete agenda packet is available on the City's website and in the City Clerk's Office at least 72 hours prior to a Regular Meeting and 24 hours prior to a Special Meeting. A hard copy of any agenda report may be requested by contacting the City Clerk's Office at (408) 615-2220, or email [clerk@santaclaraca.gov](mailto:clerk@santaclaraca.gov) <<mailto:clerk@santaclaraca.gov>>.

**RECOMMENDATION**

1. Approve the FY 2020/21 budget amendments detailed in Attachment 1 for all Departments and Offices, except the Mayor and Council and the City Auditor's Office and City Attorney's Office appointees, as recommended by the City Manager (five affirmative Council votes required for revenue actions only); and
2. Consider and approve the FY 2020/21 budget amendments detailed in Attachment 2 for the Mayor and Council, the City Auditor's Office, and City Attorney's Office appointees.

Reviewed by: Kenn Lee, Director of Finance

Approved by: Deanna J. Santana, City Manager

**ATTACHMENTS**

1. FY 2020/21 Budget Amendments
2. FY 2020/21 Budget Amendments for City Council and Appointees