



## Agenda Report

20-704

Agenda Date: 9/29/2020

### 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.

At a local level, several of the City's General Fund revenue have been impacted, with the largest declines in the transient occupancy tax, sales 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 in September and December 2020 was put into place for the purpose of obtaining more economic data, evaluating the duration of COVID-19, and developing expenditure reduction proposals. Through strong fiscal management efforts, the City has been able to develop proposals that maximize services, maintain our workforce, and suspend expenditures where appropriate due to COVID-19. The City's shortfall has been addressed with a combination of the following:

- One-time savings from cost control measures and other actions;
- Ongoing expenditure reductions;
- Potential labor negotiations (subject to meet and confer); and
- Potential ballot measures and other revenue generating actions.

This memorandum responds to the direction to reevaluate, in September, the City's fiscal condition and provide a further update to the budget based on COVID-19 impacts. Additional actions are planned to be brought forward in December 2020 and as part of the FY 2021/22 and FY 2022/23 Biennial Operating Budget. This incremental approach allows 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 and the labor negotiations.

To date, the City's strong fiscal management strategy has worked. The City has been able to manage COVID-19 significant budget impacts, within the past six months, while developing a strategic plan going forward over the next fiscal years. Prior to COVID-19, the City's financial forecast was manageable and well-planned: however, like many other cities, COVID-19 alone has had significant impacts on all facets of regular life and, likewise, is the sole source of these fiscal impacts

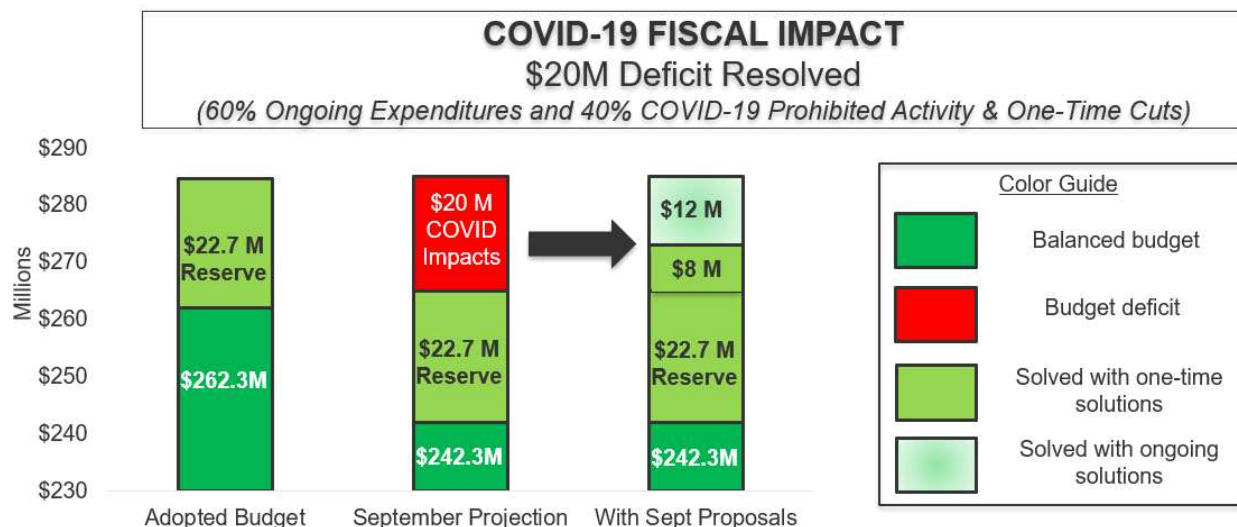
presented in this report.

## **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 continue to reflect the impacts of COVID-19, but some are showing some improvement. On a national level, the unemployment rate remains high at 8.4% in August 2020, which is below the record setting high of 14.7% in April 2020, but well above the 3.5% in February 2020. In the second quarter 2020, the Gross Domestic Product (GDP) declined by almost 32% as a result of the COVID-19 safety precautions, which is the largest contraction ever experienced. Significant impacts have also been experienced on the State and local level. After the State's largest increase in the unemployment rate in April 2020, the California unemployment rate has continued to improve to 13.3% by July 2020. The unadjusted unemployment rate in the San Jose-Sunnyvale-Santa Clara Metropolitan Statistical Area (MSA) was 9.4% in July 2020, down from a revised 10.8% in June 2020 but well above the July 2019 level of 2.8%.

Staff has continued to evaluate the impact of COVID-19 and the impacts 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. Additional downward revenue adjustments of approximately \$20 million are necessary to bring the budgeted estimates in line with the latest projections. These impacts are in addition to the \$22.7 million budget shortfall addressed in June 2020 with the use of the Budget Stabilization Reserve. With the actions included in this report, 60% of the additional deficit is proposed to be closed with ongoing solutions. The remaining 40% reflects one-time cuts and savings from COVID-19 activities that are prohibited at this time.

**Table 1: FY 2020/21 Budget - COVID-19 Fiscal Impacts and Solutions**



In evaluating the COVID-19 impacts, staff has also completed its FY 2019/20 year-end close analysis which resulted in a drop in General Fund revenues that were partially offset by expenditure savings as presented as a separate Council action on this Council agenda. The FY 2019/20 year-end close necessitates the use of the Budget Stabilization Reserve to address the shortfall of approximately \$3.5 million.

### September 2020 Budget Balancing Actions

The budget actions recommended in this memorandum are sufficient to address the additional drop in revenues identified since the adoption of the budget. These actions also provide capacity to address all of the shortfall resulting from the FY 2019/20 year-end close, without the need to draw down further from the Budget Stabilization Reserve.

The table below summarizes the revenue and expenditure adjustments recommended in this memorandum. The details associated with these revenue and expenditure actions are included in Attachment A to this memorandum.

**Table 2: September 2020 General Fund Budget Balancing**

General Fund Adjustments	2020/21 Source of Funds	2020/21 Use of Funds
Downward Revenue Adjustments	(\$19.7 M)	
Revenue Increases (Budget Solutions)	\$4.3 M	
COVID-Related One-Time Expenditure Reductions		(\$5.2 M)
Other Expenditure Reductions		(\$13.8 M)
Use for FY 2019/20 Balancing		\$3.6 M
<b>Total Adjustments</b>	<b>(\$15.4 M)</b>	<b>(\$15.4 M)</b>

### Revenue Adjustments

The revenue adjustments recommended in this memorandum are summarized in the chart below and detailed in Attachment 1. These include downward adjustments to some of the economically sensitive revenues, such as transient occupancy tax (TOT), sales tax, and property tax. The adjustments to TOT and sales tax reflect updated information about collections in these areas. The adjustment to the property tax estimate reflects the potential elimination of Education Revenue Augmentation Fund (ERAF) revenues as the State of California is challenging the distribution methodology for these receipts. Additional adjustments are also recommended in categories impacted by COVID-19, such as charges for services.

These downward adjustments are partially offset by the increases that are brought forward as budget balancing actions. These include the recognition of revenue associated with the close-out of old assessment districts as well as reimbursement for staff costs associated with the Clean-Up Campaign and transfers from other funds.

It remains difficult to project the longer-term impacts on the City's revenues associated with the current economic environment and COVID-19. Ongoing downward adjustments are included for a few of the revenue categories and reflect early projections on the potential impacts in FY 2021/22. These figures will be updated in the Ten-Year General Fund Forecast that will be updated in December 2020.

**Table 3: Proposed General Fund Revenue Adjustments**

Category	FY 2020/21 Impact	Ongoing Impact
<b>Downward Adjustments</b>		
Transient Occupancy Tax	(\$11.0 M)	(\$4.0 M)
Sales Tax	(\$5.0 M)	
Property Tax	(\$1.0 M)	(\$1.7 M)
Charges for Services	(\$2.4 M)	(\$0.4 M)
Fines and Penalties	(\$0.3 M)	
<b>Sub-Total Downward Adjustments</b>	<b>(\$19.7 M)</b>	<b>(\$6.1 M)</b>
<b>Upward Adjustments</b>		
Charges for Services	\$0.3 M	
Transfer from Other Funds	\$0.2 M	
Other Revenue (Fund Close-Out)	\$3.8 M	
<b>Sub-Total Upward Adjustments</b>	<b>\$4.3 M</b>	
<b>Total Adjustments</b>	<b>(\$15.4 M)</b>	<b>(\$6.1 M)</b>

Expenditure Adjustments

Budget actions are recommended in this memorandum to offset these 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 first round of proposals reduces costs by \$19.0 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 4: 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)	(\$3.8 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>(\$19.0 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, reorganizes fire administrative support, 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 as-needed 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, 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 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

Through strong fiscal management, the budget actions recommended in this memorandum are able



to cover the additional \$20 million impact from COVID-19 in FY 2020/21 as well as cover the actions that are being brought forward as part of the FY 2019/20 Budget Year-End Close (RTC 20-674). As a result, the balance for the Budget Stabilization reserve is projected to remain stable at \$57.8 million. This equates to approximately 20% of the budgeted expenditures in the General Fund.

The chart below details the changes in the major General Fund reserves taking into consideration the September 2020 and the FY 2019/20 Budget Year-End Close actions

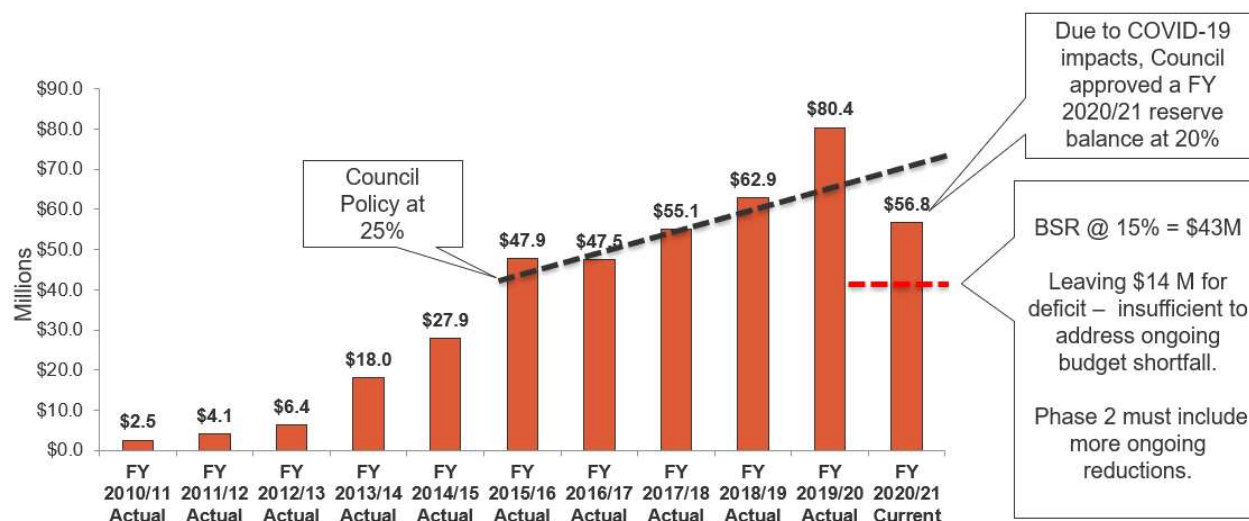
**Table 5: Major General Fund Reserves Status**

\$ In Millions		2020/21 Budget Adoption Change Reserves	2020/21 Revised Reserve Balance	FY 2019/20 Year-End Change in Reserves	Sept 2020 Balancing Change in Reserves	2020/21 Revised Reserve Balance
Reserve	July 1, 2020 Beginning Balance					
Budget Stabilization	\$ 80.4	\$ (22.7)	\$ 57.7	\$ (3.5)	\$ 3.6	\$ 57.8
Capital Projects	28.1	\$ (26.2)	1.9	3.5		5.4
Building Inspection	13.2	\$ (0.9)	12.3	5.7		18.0
Land Sale	23.2	\$ 0.7	23.9	(0.2)		23.7
Pension Trust	19.9		19.9	1.7		21.6
<b>Total</b>	<b>\$ 164.8</b>	<b>\$ (49.1)</b>	<b>\$ 115.7</b>	<b>\$ 7.2</b>	<b>\$ 3.6</b>	<b>\$ 126.5</b>

The chart below shows the General Fund Budget Stabilization Reserve history. Because of the impacts of COVID-19, staff recommends considering an exception to the policy to reduce the reserve level to 15% of operating expenses to maintain a minimum amount which would allow for additional flexibility to balance the budget going forward. Reducing the reserve would still provide \$43 million in reserves, or just slightly over a month and a half in operational reserves.

This would provide an additional \$14 million for use for future budget balancing; however, any use of the reserve 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. It is also recommended that this be the minimum level established as we continue to face multiple unknown challenges. Budget balancing going forward must continue to contain on-going expenditure reductions or increased on-going revenue levels (which is largely unlikely in this current economic environment caused by COVID-19).

### Chart 1: General Fund Budget Stabilization Reserve History



### 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

As described above, the September 2020 budget actions 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.

After the September 2020 budget actions, it is currently estimated that the General Fund shortfalls of \$28 million will remain to be addressed in the December 2020 process and the FY 2021/22 and FY 2022/23 Biennial Operating Budget process as shown in the chart below. This shortfall figure will be updated in the Ten-Year General Fund Forecast this will be released in December 2020.



**Table 6: Ten-Year General Fund Forecast**

	January 2020 Forecast	April 2020 Forecast	September 2020 (Assumes Phase 1 Approved)
<b>General Fund Shortfall</b>	(\$13 M)	(\$34 M)	Est. (\$28M)

If COVID-19 continues to have a negative impact of the City's fiscal condition, the next round of proposals will be brought forward in December 2020 and will take into account updated revenue projections from a revised Ten-Year General Fund Forecast, the results of the Transient Occupancy Tax ballot measure, and any impacts from labor negotiations. The reduction proposals brought forward at that point may have more significant impacts.

If the City's fiscal condition generally holds steady, then budget development instructions will be issued for FYs 2022 and 2023 with formal action planned by July 1, 2021. 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 at that point with the goal of using ongoing solutions to the extent possible.

### **COORDINATION**

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

### **PUBLIC CONTACT**

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;
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; and
3. Approve an exception to the Budget and Fiscal Policies and allow the Budget Stabilization Reserve to drop below 25% of the Operating Budget expenditures to 15%, or \$42,895,231, for consideration of future use of the Budget Stabilization Reserve for budget balancing purposes.

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 Appointees