

FINANCIAL FORECAST

Introduction

"Prediction is very difficult, especially if it's about the future."

--Nils Bohr, Nobel Laureate in Physics

Predicting future budgets is challenging because of the wide number of economic, demographic and policy variables involved. Many factors which drive the forecast are beyond the control of the City, such as inflation, employer pension rates, federal and state spending cuts, state-wide initiatives, short-term economic cycles, and emergencies. The City Council does influence salary and benefit costs through the labor negotiation process, and by the staffing levels set through the budget process. Revenues are largely controlled by other levels of government, or require voter approval, but the City can set fee levels to not exceed related costs, and can approve new development through the planning process. All of these factors cannot be known with certainty in advance, but one can make reasonable assumptions

The City has a history of forecasting, which is a best practice of the Government Finance Officers Association. What makes this year's Financial Forecast different is that the City retained Bob Leland of Management Partners to prepare a comprehensive and nimble forecasting model which can readily reflect a wide range of assumptions and forecast scenarios, and display an extensive dashboard of charts that update automatically as changes are made. Following the recommendation of the Finance and Budget Commission, which has reviewed the budget model, the City used it to produce a 20-year forecast, rather than the 5-year forecast of previous years. This longer time frame captures long-term changes in pension costs and is in line with the 20-30 year time frame of recent infrastructure studies.

The 20-year budget model and Financial Forecast serves as an important fiscal strategic planning tool. It provides a macro level view of General Fund revenues and expenditures to assist in evaluating the impact of policy choices made today on the long-term fiscal health of the City. By identifying developing trends and potential issues that may arise in the future, it will help ensure long-term stability for the organization by giving policy-makers improved information with which to craft prudent and timely budget solutions. The fact that there are restrictions imposed by the State that limit local governments in their discretion to raise revenues adds weight to the importance of longer term financial forecasting.

Forecasting is all about assumptions. This Financial Forecast focuses on what is likely to happen to the General Fund based on past experience and a realistic, versus conservative, assessment of what might happen in the future. This forecast is a snapshot in time, but the beauty of the budget model is that it is a "living" document which is constantly being updated with new information and can be adjusted as circumstances and trends begin to change. By being transparent about the assumptions that go into the forecast, and what is funded versus spending needs that are not funded, the City will promote better understanding of its financial condition and improve the credibility of its forecasting efforts.

General Fund Revenues

The amount of money available to fund services and programs through the General Fund is determined by the dollars generated by the City's economic base and the City's revenue structure. The General Fund provides the only discretionary revenue available to the Council and citizens to directly support local priorities. The General Fund provides most of the funding for services such as police and fire protection, parks, recreation, community development, as well as most of the administrative and support functions of City government.

There are five revenue sources that comprise 73% of total General Fund revenue: property tax (including the motor vehicle in-lieu amount), sales tax (including the Measure O local 1% tax), business license tax, transient occupancy tax (TOT), and municipal services tax. The City's ability to maintain General Fund revenue consistent with inflation and other increasing pressures on spending has been severely limited by various voter initiatives over the last 20 years. This trend began in 1979 with Proposition 13, and continued with Proposition 218. The effects these voter initiatives have had on the City's General Fund have been further compounded by the State's shift of local property tax revenues away from cities to school districts (Educational Revenue Augmentation Fund, or ERAF) and the State General Fund.

The projection of revenues into the future is based on past performance and analysis of actual current private and public sector activity. This includes such private sector activities as housing trends, property turnover and business growth; and public sector developments such as policy shifts at the local, state and federal levels. Revenue projections are inherently dependent on a number of assumptions, which vary by revenue source. The major assumptions used to project the General Fund revenues in the Financial Forecast are as follows:

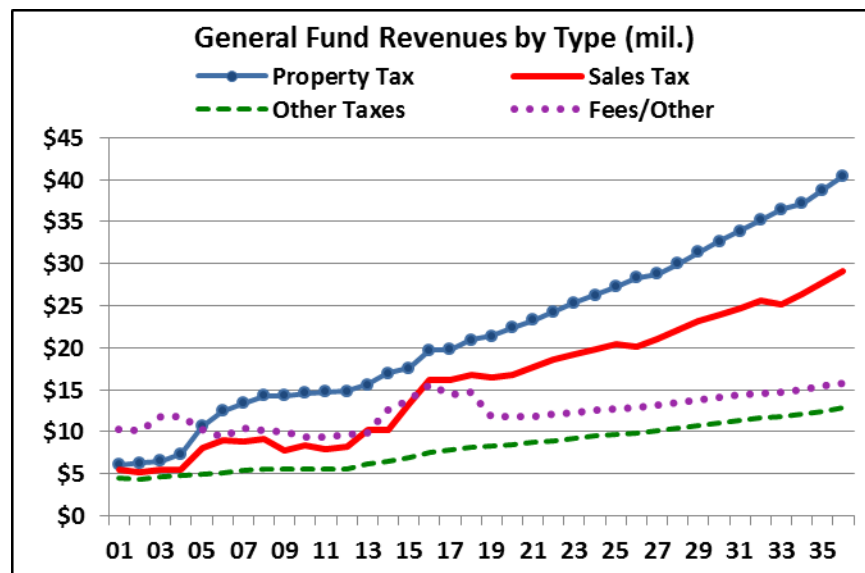
- *Tax Rates* – All tax rates are assumed to be maintained at current levels, although in the case of Measure O (sales tax) this will require voter approval. A local sales tax rate of 0.5% originally approved in 2004 was renewed by voters in June of 2010 and was set to expire in June 2016. In June 2014 voters approved Measure O, which increased the local rate to 1.0%. This tax expires on December 31, 2020, unless renewed prior to that time. The impact of retaining versus losing this tax will be shown below.
- *Recessions* – Modest recessions are assumed to occur every seven years (the average since the Great Depression) starting in 2019. They are projected to last one year with a recovery spread over the ensuing three years. The property tax will lose 2% of growth than would otherwise occur and the sales tax 5%. This level of reduction is much less than under the recent Great Recession, so a more pronounced economic downturn would result in lower revenues. The budget model allows staff to simulate a range of economic outcomes to test the sustainability of any given forecast.
- *Property Tax* – The State Constitution sets the base property tax rate at 1% of assessed value. Property values are limited to 2% growth except when property is transferred or newly constructed. The City receives approximately 18% of the property tax generated in Davis. Property tax growth is determined by the Proposition 13 inflator, changes in ownership, and new construction. It is assumed that 96% of existing parcels will grow at the 2% inflator, that 4% of parcels will change ownership and increase an average of 40%, and that new construction will occur as projected by the Community Development Department. A total of 960 new housing units, mostly multi-family, are projected to be permitted over the next three years, plus \$68 million in non-residential new construction, most of which involves three new hotels. Future growth assumes 40 housing units and \$10 million non-residential growth annually. The compound annual growth rate (CAGR) of the property tax from FY 16/17 through FY 35/36, including recessions, is 3.7%.
- *Sales Tax* – Revenues are derived from the tax imposed on sales of goods and services transacted within the City. Sales tax growth is based on a projection by MuniServices, the City's sales tax auditor, by economic sector through FY 21/22. The CAGR, including recessions, is 3.0%. With 39% of its sales tax from the transportation sector, compared to 26% statewide, Davis will always be subject to greater volatility in the sales tax during

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economic cycles. The continuing shift from taxable commodities to non-taxable services, and increasing internet purchases, are suppressing the rate of sales tax growth. Area incomes are not keeping up with inflation, which also adversely affects sales tax growth: in 1999 the median household income for zip code 95616 was \$42,110, and in 2015 it was \$44,417, a growth of only 5.5%, compared to the Bay Area inflation increase of 49.2% over that 16-year period.

- *Transient Occupancy Tax* – The TOT, or hotel tax, applies to rentals of less than 30 days at hotels, motels or short term rentals. The tax rate was increased from 10% to 12% by Measure B at the June 2016 election. The growth rate is 3% before the addition of three new hotels that have secured planning approvals from the City. These hotels will add a net of 327 rooms during fiscal years 18/19 and 19/20. Assuming nationwide average room rates for these chains, a 70% occupancy rate and a 10% substitution effect (loss of business from current hotels), these three establishments would add \$1.4 million in annual TOT revenue. Market forces may affect the timing and revenue generation from these new hotels.
- *Municipal Services Tax* – This tax was adopted by local voters in 1986. The tax paid by residential property owners is charged primarily per dwelling unit, and by commercial property owners primarily on building square footage. Revenue growth is projected at 3%.
- *Business License Tax* – This tax is imposed on gross receipts of businesses licensed to operate in the City. The tax rate varies depending on the business enterprise. Revenue growth is projected at 2%.
- *Other Revenue* – Other revenue sources include user fees, permits, fines, rentals, the property transfer tax, franchise payments, interest income and grants. Interest income assumes a 1% return on fund balance. Other revenues are generally projected to grow at the Consumer Price Index (CPI), which is projected to be 2%. The Bay Area index for All Urban Consumers has averaged 2.51% over the last 10 years, while a broader composite of US Cities, Western Urban and Bay Area inflation indices has averaged 1.87%. The Federal Reserve maintains 2% as their inflation goal.

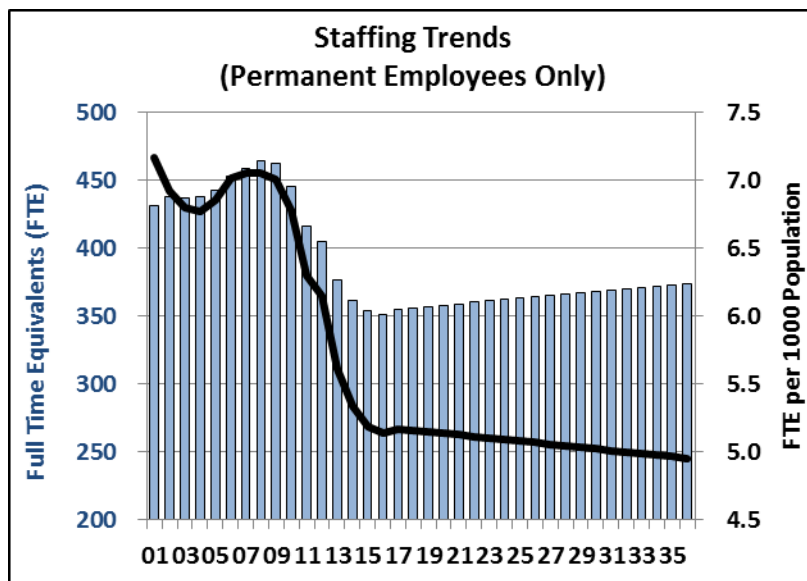
The following chart shows the historical and forecasted levels of the property tax, sales tax, other taxes (including the TOT) and fees/other revenue. The CAGR for all revenues is 2.6%, including recession impacts.



General Fund Expenditures

The expenditure baseline for the Forecast is the FY 16/17 Estimate, and the FY 17/18 Adopted Budget. The assumptions used to project the General Fund expenditures in future years are as follows:

- *Staffing Levels* - The baseline forecast starts with the staffing levels contained in the 17/18 Adopted Budget, using the current employees for filled positions and estimated costs of vacant positions. The forecast includes an allowance for the addition of one full time equivalent (FTE) position annually at the median total cost of a city position (currently \$141,577). The prior and forecasted level of staffing is shown in the following chart. After a slow increase through 2008, staffing cuts required by the Great Recession reduced permanent staffing levels by 119 FTE, or 24%. The gradual increase in FTE envisioned in the forecast will only restore one-sixth of that loss. It would take the addition of two FTE annually just to maintain a constant level of staffing (5.2 FTE) per 1000 population.

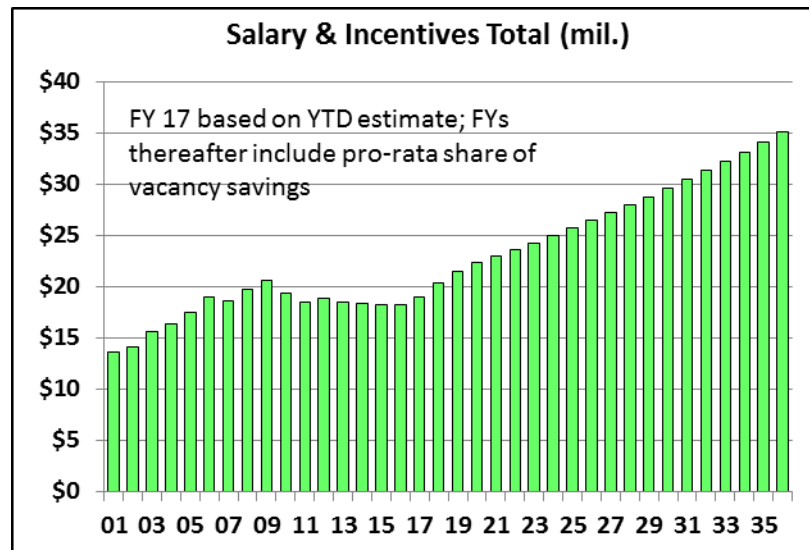


- *Wage Scale Increases* – The forecast assumes a 2% annual growth in wages, either in the form of across-the-board increases, or the equivalent in targeted increases based on recruiting, retention or equity considerations. Such wage changes are the result of the meet and confer process between the City and its labor groups, so the actual outcome of any given year may vary. It is prudent, however, to build such wage inflation into a forecast that includes anticipated growth in all other revenues and expenses. (The FY 17/18 Adopted Budget does not incorporate a cost of living adjustment into its personnel estimates, because labor negotiations are ongoing, but the forecast grows the baseline personnel expense by 2% for 18/19 and future year calculations as a contingency.)
- *Movement Within Wage Scale* – The forecast assumes a 0.5% average net increase which represents the combination of 5% step increases for eligible employees, and an assumed 8% rate of employee turnover with a resulting average savings of 12.5% from new employees hired at a lower pay range. This is an average: depending on the combination of employees leaving and those receiving step increases, the annual impact of movement within the wage scale may range from -0.3% to +0.8%.
- *Vacancy Savings* – The forecast (and City budget) now incorporate a vacancy savings factor to account for the estimated level of savings that will result from position left unfilled for a portion of the year. Such vacancies are a natural outgrowth of employee turnover, and by not accounting for this effect the City would always experience a “windfall” at the end of the year. In an effort to budget with the likely ultimate outcome in mind, the 17/18 budget

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contains a 5% vacancy savings factor, which drops to 4% in 18/19 and 3% thereafter. In normal times 3% has been the “industry standard”, but in recent years the high turnover of baby-boomers, hesitancy to fill vacancies as a budget savings strategy, and smaller staffs available to recruit and fill positions have led many agencies to experience vacancy rates of 5-10% or more. In the past year Davis experienced a vacancy rate of around 7%. The vacancy rate is computed on salaries and benefits, excluding the PERS unfunded liability, retiree medical payments, workers compensation, unemployment insurance, and leave payouts, which are fixed obligations.

The following chart shows the prior and forecasted level of salary and incentive payments. Note the accelerated rate of growth pre-recession (6.8% average annual growth), compared to the post-recession slide (-1.7% average annual growth). This is followed by a transition period where growth in salary costs is compounded due to the lowering of the vacancy savings assumption from 7% in FY 16/17 to 3% in FY 19/20. Thereafter, the growth rate is steady at 2.9% (and without the added 1.0 FTE annually the growth would be 2.5%).



- *Temporary Wages* – The growth rate of wages for temporary employees are based on an estimated impact of the minimum wage law which raises the minimum wage from the current \$10.50 to \$15 in annual increments through January 2022.
- *Overtime* – Only overtime that is anticipated to be required at the authorized staffing level is budgeted, because if overtime for police and fire jumps due to higher vacancy levels than budgeted, the City will experience additional savings from those vacancies that will offset the added overtime expense. Overtime resulting from fire strike teams is excluded (as is the reimbursement for such costs) due to the volatility of such activities, and the fact that the added expense and revenue will offset each other in any event.
- *Pension Costs* – Retirement rates are set annually by the California Public Employees’ Retirement System (CalPERS). Normal costs to pay for current accrued liability are recovered through a percent of payroll. Unfunded actuarial liability (UAL) is recovered through a fixed dollar payment. These are allocated proportionately by the City to the funds to which employees are charged.

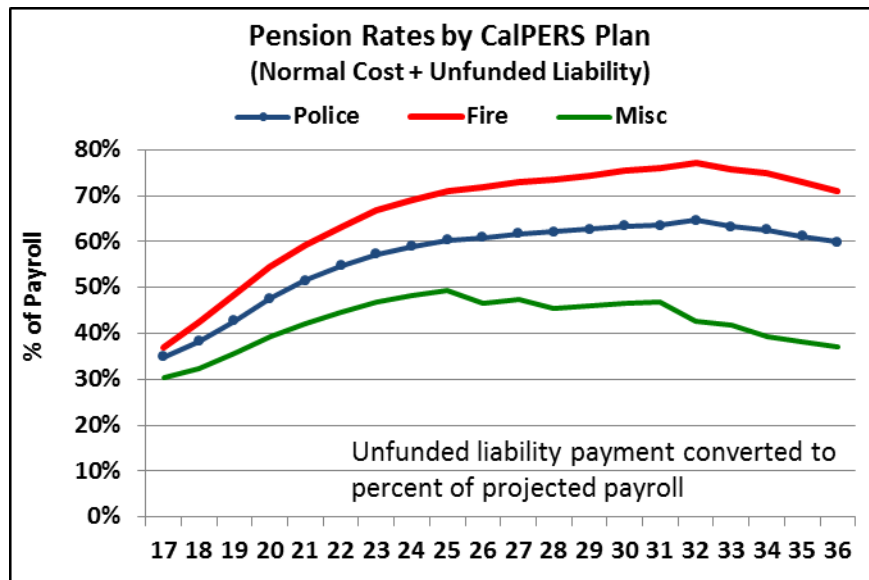
Pension costs are a major consideration in the budget planning for all government agencies. First, we are in the midst of a planned multi-year escalation in employer rates by CalPERS due to changes they have made in rate smoothing calculations, amortization of unfunded liability over fixed terms, and mortality improvements for beneficiaries, which extends through FY 22/23. This alone will double the City’s total UAL payments for all funds over the next six years, as shown in the following table:

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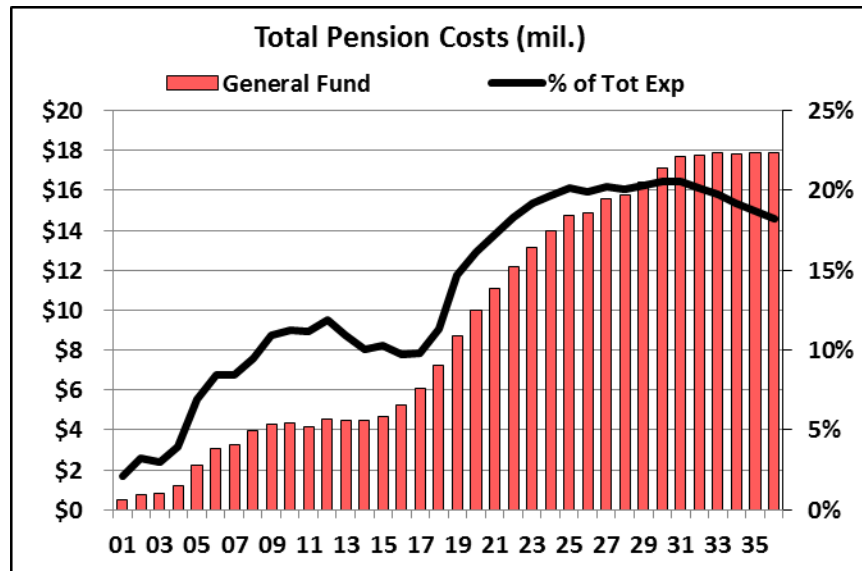
(\$ in mil.)	16/17	17/18	18/19	19/20	20/21	21/22	22/23
Police	0.98	1.19	1.47	1.76	1.93	2.09	2.23
Fire	0.88	1.07	1.32	1.58	1.72	1.87	1.98
Misc	3.78	4.24	4.88	5.55	5.96	6.41	6.77
Total	5.64	6.50	7.67	8.89	9.61	10.37	10.98

Second, CalPERS has approved a reduction in its discount rate (assumed investment return) from 7.5% to 7.0%, the effect of which will be phased in over seven years starting in FY 18/19. Since CalPERS receives 65% of its income through investments, and what it fails to make through investments must be made up by employers, reducing the discount rate results in significant cost increases to employers. This impact is in addition to the amounts shown above, and is a work in progress. Currently, CalPERS is giving statewide average impacts as guidance to local agencies. Their next annual valuation report due in July 2017 will fine-tune these estimates by agency. But this discount rate reduction to 7.0% will probably not be the last; CalPERS officials have been frank in stating that in February 2018 when this issue is next considered, the CalPERS board may well approve an additional discount rate reduction, which will likely be phased in as well.

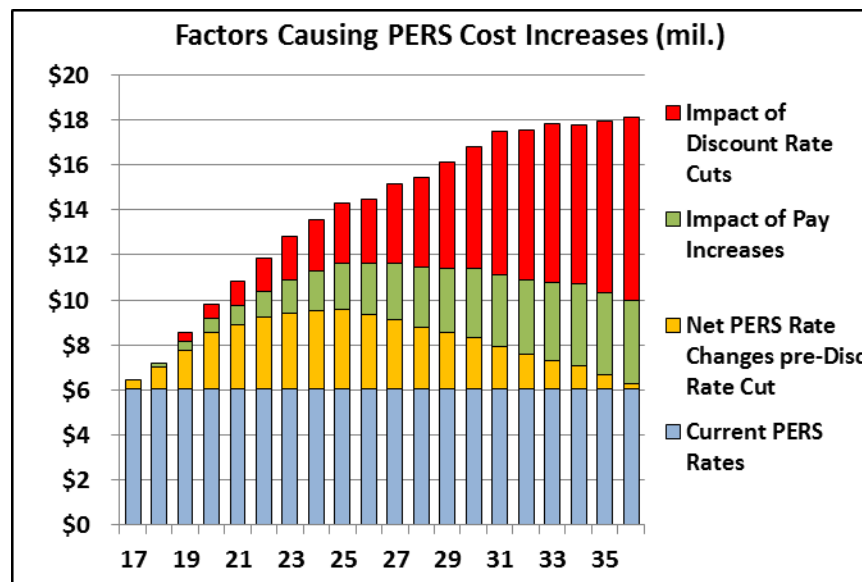
The City contracts with John Bartel Associates to prepare an independent evaluation of employer rates, which are used in the Financial Forecast. The Bartel projections assume a continued slow reduction in discount rate over time, hitting 6.0% in 2041. An ultimate decline to that level may require multiple actions by CalPERS, and may occur over a shorter period of time. The Bartel numbers also incorporate a continued transition of employees from higher-cost “classic” level of benefits to the lower benefits new hires receive under the Public Employees’ Pension Reform Act (PEPRA). The following chart shows the Bartel rates for the City’s safety, fire and miscellaneous employee plans.



Based on these rates, the following chart shows the evolution of the General Fund’s share of pension costs. Costs were under \$500,000 in FY 00/01 (back when CalPERS cut employer rates to near zero because of a “surplus” of funds) and have increased 12-fold since then. (Cost-sharing agreements reached with certain bargaining groups to date save the General Fund around \$250,000 annually, which reduce costs to the level shown.) In 20 years payments will peak at \$18 million, triple what they are today. The rapid growth in these costs will begin to abate as the various UAL amortization bases begin to be paid off. This will provide some budget relief, but not before the 2030’s. Pension costs will top out at just over 20% of total General Fund expenditures.



There are various reasons for the increase, as shown in the following chart. The chief culprit is the discount rate reductions, but a share is attributable to the pre-existing planned escalation of employer rates, and the impact of higher pay levels over time.



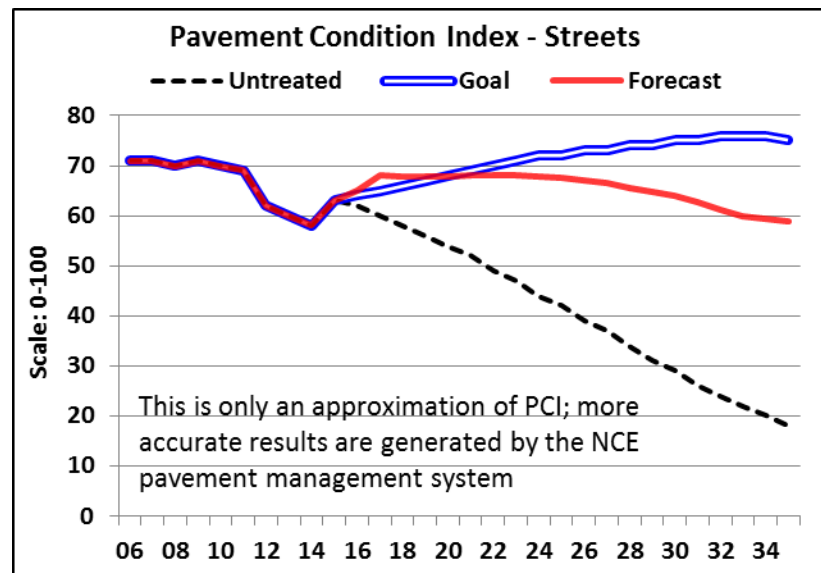
Suffice it to say that pension costs are very much on the City's budget radar, and will be closely watched on a continuous basis.

- *125 Plan Benefits* – Costs related to health, dental, and life insurance are assumed to grow at an annual rate of 2% throughout the forecast. With the implementation of the most recent MOU's, the City shares the cost of increases in medical insurance with the employee and the amount of cash that employee can take in lieu of benefits was decreased in January 2016 to a maximum of \$500 per month.
- *Other Post-Employment Benefits (OPEB)* – GASB 45 requires public agencies to evaluate and report in their annual financial statements the fully-funded cost of any post-employment benefits such as retiree healthcare. While GASB 45 does not require full pre-funding of post-employment benefits, it effectively highlights the difference between the actual cost of these benefits and the funds typically allocated on an annual pay-as-you-go basis. In this forecast OPEB costs are paid at the full annual required contribution (ARC), which is established in the actuarial reports by John Bartel Associates. This amount for all

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funds is \$6.125 million for FY 17/18, of which the General Fund pays \$4.39 million. The forecast assumes a continued slow reduction in discount rate over time, hitting 6.0% in 2041.

- *Other Expenses* – Non-personnel operation and maintenance costs generally grow at CPI (2%). Debt service costs are fixed at the 17/18 level.
- *Infrastructure Contributions* – The City has evaluated several areas of infrastructure investment to determine the recommended level of annual City maintenance funding to ensure these facilities stay in good condition over time. These include:
 - *Streets and Bike Paths* – Nichols Consulting Engineers (NCE) has prepared a pavement management system for the City (updated in 2016) and has recommended annual funding levels required to increase the pavement condition index (PCI) of City streets to the mid-70's on a scale of 0-100 with 70-100 being "good" condition. The need over 20 years is \$167 million or \$8.3 million annually (the actual amount varies by year based on a lifecycle analysis of streets). The NCE report identified \$25 million in bike path funding needs to average a PCI of 78. The forecast assumes that 66% of street costs and 65% of bike path costs, or nearly two-thirds of this need will be funded through a combination of sources: General Fund (\$3 million annually ramping up to \$5 million in the 2030's with 85% going to streets and 15% to bike paths), construction tax (\$130,000 annually), development fees (\$800,000 annually), and the new SB1 gas tax money (\$441,000 in 17/18 and \$1.56 million annually thereafter). The following chart shows street PCI, comparing the goal to the result if streets are untreated, and to the estimated result under the forecast. By the mid-2020's the projected PCI begins to gradually fall to about 60 by FY 35/36.



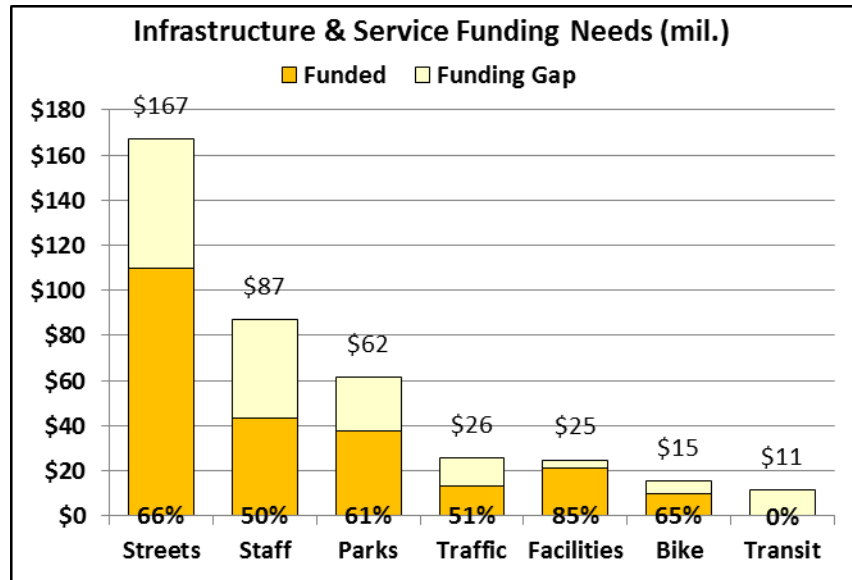
- *Facilities* – Kitchell CEM prepared a comprehensive facilities management plan that identified the costs of maintaining and ultimately replacing parks and buildings. They recommended \$25 million in maintenance costs over the next 20 years. The forecast projects that 85% of these costs will be met using \$1 million in annual General Fund contributions starting FY 18/19. (This does not include additional amounts that may be paid in future years from other funds.)
- *Park Maintenance* – This is a work in progress. Parks and Community Services staff has been updating the Kitchell study to better identify park facility needs. The forecast currently assumes an annual average unfunded need of \$555,000 for parks and structures, \$100,000 for pool equipment replacement, \$175,000 for park irrigation/conservation, \$250,000 for wildlife habitat maintenance and \$100,000 for

urban forestry, for a total of \$1.18 million. Assuming the park tax stays in effect at \$49/year it will continue to pay for \$1.4 million in other park-related costs annually, so the total annual need is \$2.58 million. If the General Fund adds \$200,000 annually to what the park tax pays for, starting in FY 18/19, then 61% of this \$62 million need over 20 years will be funded.

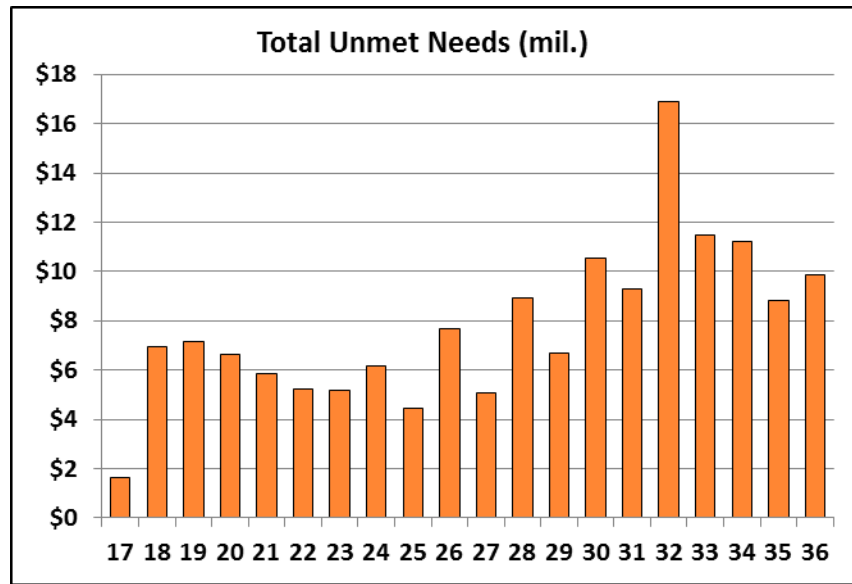
- *Traffic Maintenance* – The Public Works Department identified four areas of unfunded annual needs in December 2015: traffic signal maintenance (\$210,000), sidewalk/ADA ramps (\$400,000), striping maintenance (\$200,000), and neighborhood traffic calming (\$125,000). The forecast projects annual funding of \$450,000 starting in 18/19, which would address 51% of this \$26 million need over 20 years.
- *Transit* – This is also a work in progress. Recent indications are that transit operations may be under-funded by \$500,000 in future years due to insufficient resources in the transit-only Transportation Development Act (TDA) fund. The forecast does not include any General Fund contribution to transit operations, so absent the receipt of additional outside funding, none of this \$11 million need over the next 20 years would be addressed.

○ *Future Operating Workload* – In addition to infrastructure concerns, the City should endeavor to keep staffing levels per capita relatively constant so that workload increases caused by population growth and other service demands can be adequately addressed. This will avoid diminishing levels of service over time. Currently, most services are provided by City employees, but even if services were contracted for, additional funding will be required over time. The forecast funds one FTE increase a year, although two FTE would be required to hold staffing levels per capita constant over time. Thus, 50% of the \$87 million in service increase costs over the next 20 years would be funded.

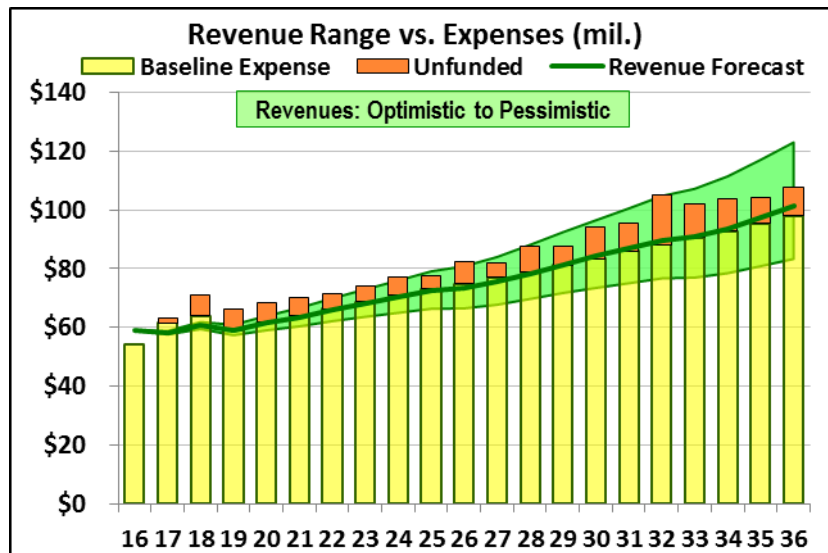
The following chart compares the funding levels as described above.



The annual shortfall in funding for all of the above infrastructure and service categories is shown in the chart below. The average annual shortfall in funding is \$7.8 million. In revenue terms, this amount is roughly equivalent to the current 1% Measure O sales tax, or to a 6.0% utility users tax on power, communications and water/sewer/sanitation services, or to a \$270 parcel tax.



To put this in another perspective, the following chart shows the unmet need compared to projected expenses, and to the projected revenues including a range of optimistic to pessimistic revenue growth.

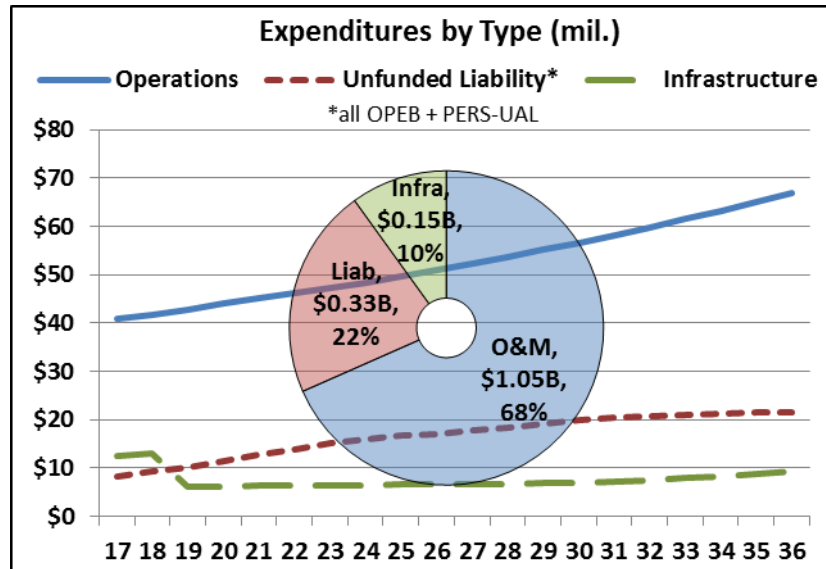


The first observation is that only under a sustained optimistic revenue scenario can a large portion of the unmet needs be funded. The revenue range widens over time with compounding, but in the near term little of the unmet needs would be funded. And if revenues are more in the pessimistic range, then not even the projected level of expenses can be sustained. Is not reasonable to assume that higher revenue growth will be able to fund these unmet needs. (Although performance in excess of the forecast in any given fiscal year could be directed into one-time infrastructure expenses.)

The second observation is that the unfunded portion averages 10% of the General Fund budget. Cutting existing budgets by 10% -- a significant amount -- to redirect funding to unmet needs, presupposes that the unmet needs are a higher priority than what the City is already doing, which is not likely. While costs can be evaluated over time to squeeze out some savings that could be redirected for this purpose, increased revenues remain the most feasible way of addressing the unmet needs while preserving current City service levels. The budget model can be used to run various forecast scenarios and levels of unmet needs that could be funded under a given proposal. This can be used to shape the combination of revenue increases and cost containment to be proposed.

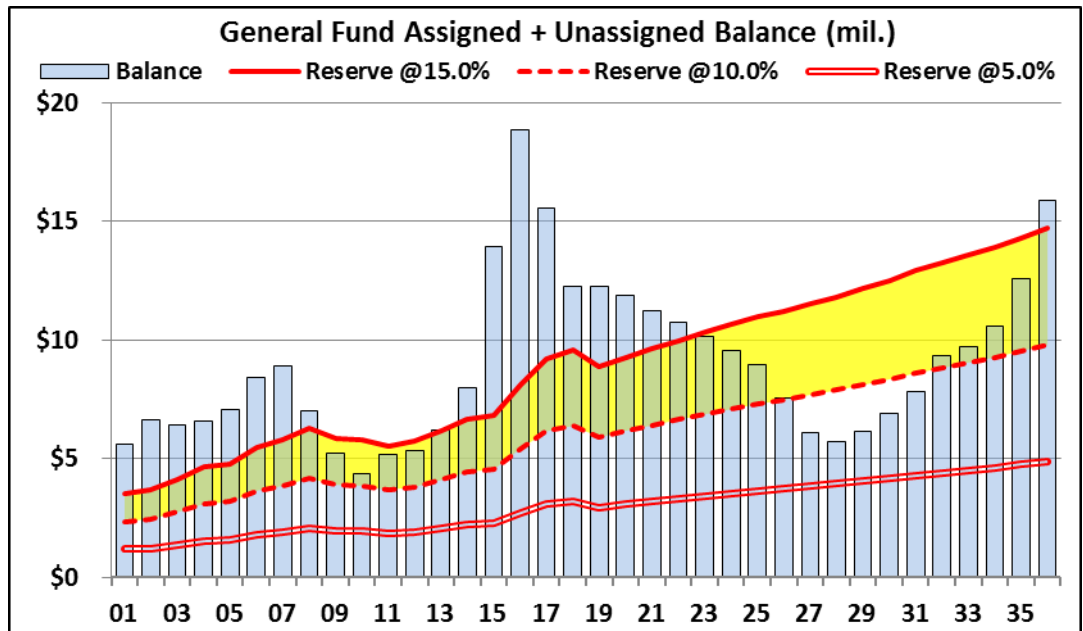
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The following chart shows the relative proportions of the three major categories of expense under the Financial Forecast: operations and maintenance, unfunded liabilities (OPEB and PERS UAL payments), and contributions to infrastructure.



General Fund Balance

The essence of a budget forecast is the fund balance. Budgets cannot run fund balance deficits, so the assumptions selected must result in a sustainable balance over time. This means a balance in the 10-15% of total expenditures, to buy time for well-thought out budget recovery plan in the event an economic downturn is greater than projected, or an emergency or other unanticipated expenditure needs exceeds the current budget. The following chart is at the center of the budget model, and compares the unassigned balance (total balance less non-spendable assets) to 5%, 10% and 15% reserve levels. (By the time balance falls to 5% an agency needs to put a recovery plan in place to staunch the budgetary bleeding prior to actual deficits resulting.)

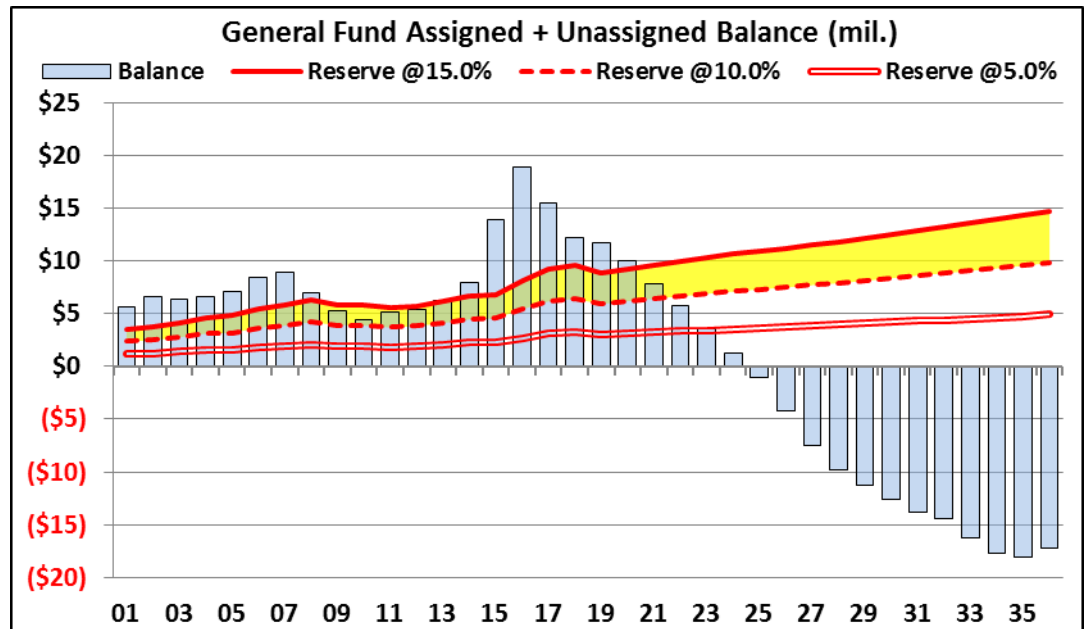


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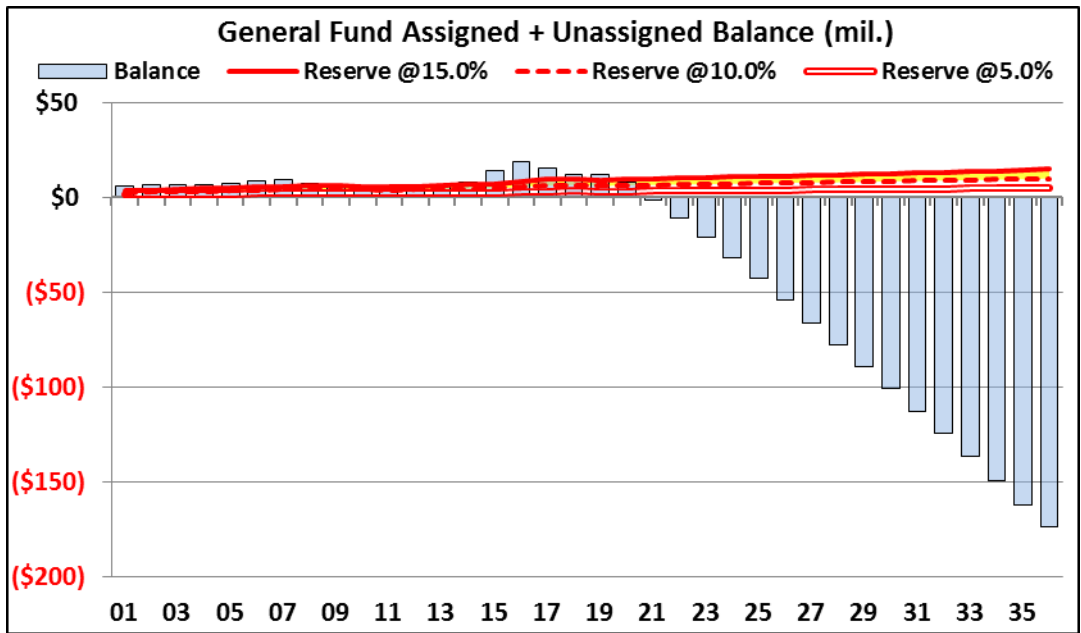
This chart shows a steady decline in balance due to the additional infrastructure investments and higher pension costs. Due to the high level of reserves starting in FY 15/16, the City has, assuming the timely completion of the new hotels, sufficient resources despite the continued decline in balance. The balance bottoms out in FY 27/28 as the rate of pension cost increase slows, and in subsequent years revenues are expected to begin exceeding expenses, thus allowing the balance to rebuild to the desired range. Maintaining an adequate reserve is the best defense against the uncertainty of pension and OPEB discount rate reductions, as well as other economic uncertainty.

Ideally, the balance/reserve should be no less than 15% in all years, but this forecast is itself a balance among competing needs: operations, infrastructure and unfunded liabilities. The unfunded liabilities are funded at 100% of annual obligations, and additional investments are proposed in infrastructure maintenance over time to avoid incurring even greater cost obligations for facilities in the long-run, if they lack adequate funding in the short and medium term.

The following chart depicts the first of two alternate revenue scenarios: no new hotel TOT revenues in the forecast.

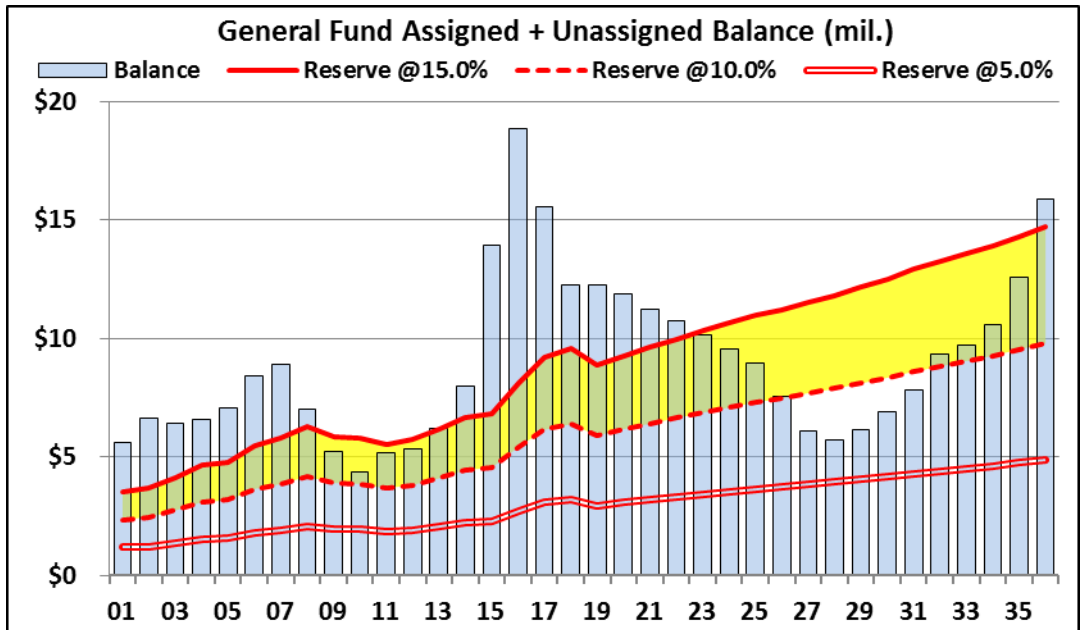


The next chart retains the new hotels, but the 1% Measure O local sales tax expires on 12/31/20, rather than remaining in effect.



Both of these present adverse outcomes, but the no Measure O scenario is ten-fold worse than the no new hotels scenario.

The following three pages provide a summary of the 20-year Financial Forecast (back to the forecast depicted in the chart below). Following that is a one-page recap of changes in this Forecast compared to the draft forecast previously discussed with the Finance and Budget Commission and Council, which was based on data prior to the preparation of the FY 17/18 Adopted Budget.



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First Ten Years of Financial Forecast

(\$ in Thousands)	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26
Property Tax	\$19,796	\$20,947	\$21,421	\$22,353	\$23,296	\$24,304	\$25,355	\$26,300	\$27,280	\$28,297
Sales Tax-Regular	7,818	8,068	7,981	8,414	8,869	9,345	9,710	10,066	10,409	10,223
Sales Tax-Measure O	8,320	8,716	8,526	8,427	8,804	9,202	9,483	9,775	10,079	9,893
Transient Occup Tax	1,607	1,752	2,252	3,263	3,385	3,512	3,618	3,726	3,838	3,857
Other Tax/Franchises	6,221	6,375	6,479	6,656	6,838	7,025	7,200	7,379	7,563	7,690
Permits & Fees	6,233	5,869	7,090	6,838	6,665	6,840	6,977	7,117	7,259	7,251
Other Revenue	8,212	8,912	5,351	5,464	5,578	5,694	5,806	5,921	6,038	6,135
Total Revenues	58,207	60,638	59,099	61,416	63,436	65,922	68,148	70,283	72,465	73,347
Salaries/Wages	18,026	20,358	21,115	21,723	22,349	22,992	23,654	24,334	25,034	25,753
Part Time (total)	1,246	1,526	1,557	1,611	1,671	1,738	1,812	1,848	1,885	1,923
Overtime	2,562	1,045	1,084	1,115	1,147	1,180	1,214	1,249	1,285	1,322
Retirement	6,057	7,257	8,714	9,969	11,095	12,159	13,171	13,978	14,753	14,874
Health/Cafeteria Plan	4,072	4,740	4,853	4,987	5,125	5,286	5,452	5,641	5,837	6,058
Retiree Medical	4,579	4,405	4,329	4,509	4,698	4,893	5,096	5,307	5,526	5,752
Other Benefits	2,275	2,986	3,095	3,184	3,276	3,371	3,468	3,570	3,674	3,782
Expense Credits	(5,030)	(5,373)	(5,682)	(5,981)	(6,268)	(6,555)	(6,840)	(7,102)	(7,364)	(7,551)
Vacancy Savings	-	(1,433)	(1,105)	(849)	(870)	(893)	(917)	(942)	(967)	(997)
Subtotal Personnel	33,787	35,510	37,959	40,269	42,223	44,172	46,110	47,884	49,662	50,916
Internal Services	9,557	7,537	8,688	8,861	9,038	9,219	9,404	9,592	9,784	9,979
Contract Services	10,528	6,436	6,122	6,244	6,369	6,497	6,627	6,759	6,894	7,032
Other O&M Expenses	5,827	5,331	5,178	5,282	5,388	5,495	5,605	5,717	5,832	5,948
Debt Service	268	245	245	245	245	245	245	245	245	245
Street Improvements	3,232	4,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000
Other Capital Outlay	5,118	7,616	700	714	728	743	758	773	788	804
Additions/(Reductions)	(915)	-	-	-	-	-	-	-	-	-
Subtotal O&M	33,615	31,165	23,933	24,346	24,768	25,199	25,638	26,086	26,543	27,009
Transfers	(3,390)	(2,710)	(2,764)	(2,819)	(2,876)	(2,933)	(2,992)	(3,052)	(3,113)	(3,175)
Total Expenditures	64,011	63,965	59,128	61,796	64,116	66,437	68,757	70,918	73,092	74,750
Net Annual	(5,804)	(3,327)	(28)	(381)	(680)	(516)	(609)	(634)	(627)	(1,403)
Beginning Balance	18,920	13,116	9,789	9,761	9,381	8,700	8,185	7,576	6,942	6,315
Ending Balance	13,116	9,789	9,761	9,381	8,700	8,185	7,576	6,942	6,315	4,912
Bal as % of Tot Exp	20.5%	15.3%	16.5%	15.2%	13.6%	12.3%	11.0%	9.8%	8.6%	6.6%
Infrastructure Funding Gaps:										
Street Needs (1)	7,300	7,800	7,500	7,400	6,800	7,100	7,300	7,600	5,900	8,600
Street Funding	7,626	6,391	5,043	5,043	5,043	5,043	5,043	5,043	5,043	5,043
Surplus(Shortfall)	326	(1,409)	(2,457)	(2,357)	(1,757)	(2,057)	(2,257)	(2,557)	(857)	(3,557)
Bike Path Needs (1)	4,200	1,900	1,800	1,200	800	1,000	500	900	600	800
Bike Path Funding	500	450	450	450	450	450	450	450	450	450
Surplus(Shortfall)	(3,700)	(1,450)	(1,350)	(750)	(350)	(550)	(50)	(450)	(150)	(350)
Facilities Needs (2)	1,204	2,063	2,063	2,063	2,063	687	687	687	687	687
Facilities Funding	3,044	-	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Surplus(Shortfall)	1,839	(2,063)	(1,063)	(1,063)	(1,063)	313	313	313	313	313
Park Needs (3)	2,536	2,587	2,639	2,692	2,746	2,800	2,856	2,914	2,972	3,031
Park Funding	1,356	1,583	1,615	1,647	1,680	1,714	1,748	1,783	1,819	1,855
Surplus(Shortfall)	(1,180)	(1,004)	(1,024)	(1,044)	(1,065)	(1,087)	(1,108)	(1,131)	(1,153)	(1,176)
Traffic Needs (4)	1,055	1,076	1,098	1,120	1,142	1,165	1,188	1,212	1,236	1,261
Traffic Funding	120	572	584	596	607	620	632	645	658	671
Surplus(Shortfall)	(935)	(504)	(514)	(524)	(535)	(545)	(556)	(567)	(579)	(590)
Total Surplus(Shortfall)	(3,650)	(6,430)	(6,408)	(5,739)	(4,770)	(3,926)	(3,659)	(4,392)	(2,426)	(5,361)
Other Funding Gaps:										
Staffing Level Gap (5)	-	(28)	(241)	(398)	(566)	(762)	(970)	(1,203)	(1,448)	(1,705)
Transit Funding Gap (6)	-	(500)	(510)	(520)	(531)	(541)	(552)	(563)	(574)	(586)
PERS Funding Gap (7)	-	-	-	-	-	-	-	-	-	-
OPEB Funding Gap (7)	2,000	-	-	-	-	-	-	-	-	-
Grand Total Gap	(1,650)	(6,958)	(7,159)	(6,657)	(5,867)	(5,229)	(5,180)	(6,158)	(4,449)	(7,652)

FINANCIAL FORECAST

Second Ten Years of Financial Forecast

(\$ in Thousands)	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32	2032-33	2033-34	2034-35	2035-36
Property Tax	\$28,785	\$30,034	\$31,337	\$32,698	\$33,920	\$35,189	\$36,506	\$37,139	\$38,756	\$40,444
Sales Tax-Regular	10,710	11,224	11,768	12,166	12,584	13,021	12,828	13,477	14,166	14,896
Sales Tax-Measure O	10,356	10,844	11,359	11,733	12,123	12,531	12,331	12,940	13,585	14,268
Transient Occup Tax	4,002	4,152	4,307	4,437	4,570	4,707	4,730	4,908	5,092	5,283
Other Tax/Franchises	7,901	8,118	8,340	8,549	8,764	8,984	9,139	9,391	9,649	9,914
Permits & Fees	7,441	7,637	7,837	7,994	8,154	8,317	8,308	8,526	8,750	8,980
Other Revenue	6,260	6,387	6,523	6,658	6,799	6,943	7,069	7,223	7,384	7,553
Total Revenues	75,455	78,396	81,473	84,236	86,913	89,691	90,911	93,604	97,381	101,339
Salaries/Wages	26,493	27,254	28,036	28,841	29,668	30,518	31,393	32,292	33,217	34,168
Part Time (total)	1,962	2,001	2,041	2,082	2,123	2,166	2,209	2,253	2,298	2,344
Overtime	1,360	1,399	1,439	1,480	1,523	1,566	1,611	1,657	1,705	1,753
Retirement	15,567	15,799	16,444	17,142	17,718	17,749	17,899	17,831	17,875	17,907
Health/Cafeteria Plan	6,288	6,544	6,810	7,104	7,410	7,747	8,097	8,479	8,877	9,309
Retiree Medical	5,989	6,235	6,490	6,755	7,030	7,317	7,616	7,926	8,248	8,582
Other Benefits	3,894	4,009	4,128	4,251	4,377	4,509	4,644	4,784	4,928	5,077
Expense Credits	(7,816)	(8,030)	(8,303)	(8,591)	(8,870)	(9,088)	(9,329)	(9,552)	(9,796)	(10,050)
Vacancy Savings	(1,026)	(1,057)	(1,088)	(1,120)	(1,154)	(1,192)	(1,230)	(1,271)	(1,312)	(1,355)
Subtotal Personnel	52,709	54,152	55,995	57,943	59,825	61,292	62,909	64,399	66,039	67,735
Internal Services	10,179	10,382	10,590	10,802	11,018	11,238	11,463	11,692	11,926	12,165
Contract Services	7,173	7,316	7,463	7,612	7,764	7,919	8,078	8,239	8,404	8,572
Other O&M Expenses	6,067	6,189	6,313	6,439	6,568	6,699	6,833	6,970	7,109	7,251
Debt Service	245	245	245	245	245	245	245	245	245	245
Street Improvements	3,000	3,000	3,000	3,000	3,250	3,500	3,750	4,000	4,500	5,000
Other Capital Outlay	820	837	853	870	888	906	924	942	961	980
Additions/(Reductions)	-	-	-	-	-	-	-	-	-	-
Subtotal O&M	27,484	27,969	28,463	28,967	29,732	30,507	31,292	32,088	33,145	34,213
Transfers	(3,238)	(3,303)	(3,369)	(3,437)	(3,505)	(3,575)	(3,647)	(3,720)	(3,794)	(3,870)
Total Expenditures	76,955	78,818	81,089	83,474	86,051	88,223	90,554	92,767	95,389	98,078
Net Annual	(1,500)	(422)	383	762	862	1,468	357	837	1,992	3,261
Beginning Balance	4,912	3,412	2,990	3,374	4,135	4,998	6,466	6,823	7,659	9,651
Ending Balance	3,412	2,990	3,374	4,135	4,998	6,466	6,823	7,659	9,651	12,912
Bal as % of Tot Exp	4.4%	3.8%	4.2%	5.0%	5.8%	7.3%	7.5%	8.3%	10.1%	13.2%

Infrastructure Funding Gaps:

Street Needs (1)	6,400	9,800	7,300	10,700	9,200	15,600	10,000	9,500	7,100	8,100
Street Funding	5,043	5,043	5,043	5,043	5,256	5,468	5,681	5,893	6,318	6,743
Surplus(Shortfall)	(1,357)	(4,757)	(2,257)	(5,657)	(3,945)	(10,132)	(4,320)	(3,607)	(782)	(1,357)
Bike Path Needs (1)	100	200	100	100	200	200	200	200	200	200
Bike Path Funding	450	450	450	450	488	525	563	600	675	750
Surplus(Shortfall)	350	250	350	350	288	325	363	400	475	550
Facilities Needs (2)	690	690	690	690	690	1,688	1,688	1,688	1,688	1,688
Facilities Funding	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Surplus(Shortfall)	310	310	310	310	310	(688)	(688)	(688)	(688)	(688)
Park Needs (3)	3,092	3,154	3,217	3,281	3,347	3,414	3,482	3,552	3,623	3,695
Park Funding	1,892	1,930	1,969	2,008	2,048	2,089	2,131	2,173	2,217	2,261
Surplus(Shortfall)	(1,200)	(1,224)	(1,248)	(1,273)	(1,299)	(1,325)	(1,351)	(1,378)	(1,406)	(1,434)
Traffic Needs (4)	1,286	1,312	1,338	1,365	1,392	1,420	1,448	1,477	1,507	1,537
Traffic Funding	684	698	712	726	740	755	770	786	801	818
Surplus(Shortfall)	(602)	(614)	(626)	(639)	(652)	(665)	(678)	(691)	(705)	(719)
Total Surplus(Shortfall)	(2,499)	(6,035)	(3,472)	(6,909)	(5,298)	(12,484)	(6,674)	(5,965)	(3,106)	(3,648)

Other Funding Gaps:

Staffing Level Gap (5)	(1,991)	(2,291)	(2,620)	(2,983)	(3,358)	(3,743)	(4,149)	(4,578)	(5,031)	(5,517)
Transit Funding Gap (6)	(598)	(609)	(622)	(634)	(647)	(660)	(673)	(686)	(700)	(714)
PERS Funding Gap (7)	-	-	-	-	-	-	-	-	-	-
OPEB Funding Gap (7)	-	-	-	-	-	-	-	-	-	-
Grand Total Gap	(5,087)	(8,936)	(6,713)	(10,526)	(9,303)	(16,887)	(11,496)	(11,229)	(8,837)	(9,880)

Footnotes:

(1) Street and bike path needs as identified in 2016 NCE report. Funding is \$3 million General Fund contribution plus \$130,000/year Construction Tax, \$800,000/year Developer Fees, \$1.56 million from SB1 gas tax and any grant/other funding as identified in the budget model.

(2) Facility maintenance needs as identified in 2016 Kitchell report (see Table 3). This does not include replacement costs. Funding is General Fund contribution of \$1 million starting FY 18/19.

(3) Park maintenance needs as identified by Parks staff (Dec 2015 staff report and updated Kitchell numbers). Funding is current \$49 parks tax (\$1.4 million/year) plus \$200,000 General Fund contribution starting FY 18/19.

(4) Traffic maintenance needs as identified in Dec 2015 staff report. Funding is existing General Fund support plus \$450,000 General Fund contribution starting FY 18/19.

(5) To maintain FTE/1000 population, City needs to add 2.0 FTE per year to theoretically address added workload from population growth and other needs. If this category is activated, deficit of this amount is reflected as shortfall, excess as surplus.

(6) Represents a shortfall in transit funds available for City's share of Unitrans costs. To maintain current service levels may ultimately require General Fund support.

(7) Funding in budget model compared to projected full funding obligation for each fiscal year. Both PERS and OPEB have long-term funding schedules to amortize unfunded liabilities. In FY 16/17 the City pre-funded \$2 million in OPEB obligations.

Changes to Draft Forecast

Based on the FY 17/18 Adopted Budget and new data on revenues and expenses, the forecast has been updated from the version previously discussed with the Finance and Budget Commission and Council. Net projected resource reductions of \$19 million over the period from FY 17/18 through FY 35/36 required \$15 million of reduced infrastructure contributions (out of \$116 million originally proposed) to balance the forecast with the desired reserve level. The table below gives a brief recap of changes to the 20-year forecast.

Revised Forecast Compared to Draft Forecast
Major Changes in Total Amounts Over Period of FY 17/18 Through 35/36
(\$ in Millions)

Revenues:

Property Tax	\$11	higher change in ownership values
Residual	(\$18)	lower amounts per County
Grants	(\$9)	excludes fire strike team reimbursement
Fees	\$0	planning fees up, fire down, other net changes offset
Other	\$3	net increase in revenues
Net Gain (Loss)	<u>(\$13)</u>	net reduction in revenue (mainly due to residual)

Personnel:

Salaries	(\$13)	add fire chief, FTE shifts to GF from other funds
Part-time	(\$2)	higher hours, wages
Overtime	\$39	lower based on full staffing, excludes strike team-related
Health	(\$15)	higher estimated costs
OPEB	(\$3)	adjustment in discount rate to match pension
Other Personnel	\$1	net cost reduction
Vacancy Savings	\$4	formula correction post-2027
Net Gain (Loss)	<u>\$11</u>	overall net savings (mainly due to lower overtime)

Non-Personnel:

Professional Services	(\$26)	incorrect exclusion of costs thought to be infrastructure
Other O&M	\$11	net reduction in costs
Projects/Capital Outlay	(\$2)	additional projects in 17/18
Net Gain (Loss)	<u>(\$17)</u>	net cost increase (mainly due to O&M contract costs omitted)
Total Before Corrections	<u>(\$19)</u>	net reduction in overall resources over 20 years
Infrastructure Contributions	<u>\$15</u>	reduction in streets/facilities contributions to balance forecast
Total After Corrections	<u><u>(\$4)</u></u>	resulting net reduction in resources

