



City of South San Francisco Legislation Text

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Item #:

Report regarding the City of South San Francisco Operating Budget for Fiscal Year 2025-26.
(Karen Chang, Director of Finance)

RECOMMENDATION

It is recommended that the Budget Standing Committee provide feedback in preparation for the City Council study session on June 11, 2025, related to the establishment of the City's Fiscal Year (FY) 2025-26 operating budget.

BACKGROUND/DISCUSSION

The City's budget process is an annual cycle that aligns financial planning with service delivery, policy goals, and community needs for the fiscal year beginning July 1 and ending June 30. It serves as both a financial plan and a policy document, guiding how City resources are allocated and managed.

Each year, the process begins with the development and refinement of City Council policy goals, typically occurring in the first quarter of the calendar year. These goals serve as a strategic foundation for budget development, providing direction for departmental priorities, new initiatives, and resource allocation. This early-stage policy discussion ensures that the budget reflects the long-term vision and evolving priorities of the City Council and the community.

Following this, departments prepare budget requests based on operational needs and policy alignment. These requests are reviewed by the Finance Director and City Manager, and department heads participate in individual meetings to evaluate and refine their proposals. Revenue forecasting is conducted primarily by the Finance Department for major tax categories, while departments contribute estimates for fees, permits, and other sources.

Capital improvement requests are managed separately by the Public Works Department and submitted via a dedicated staff report to ensure alignment with infrastructure planning and long-term capital needs.

The public component of the budget process begins with the Budget Standing Committee, which reviews preliminary recommendations and key assumptions. The proposed budget is then presented in a public City Council Study Session for discussion and feedback. A final version is adopted by the City Council in a regular meeting, completing a three-step public review and approval process.

The process is guided by best practices in fiscal management, emphasizing transparency, accountability, and the alignment of financial resources with strategic priorities.

CITYWIDE OVERVIEW – EXECUTIVE SUMMARY

While each fund, particularly the General Fund, face specific revenue-side concerns, the cost pressures affecting the City's budget are broad and largely universal across departments and funds.

A key driver of rising expenditures in the FY 2025–26 Proposed Budget is the continued growth in personnel costs. The budget currently includes a 3% cost-of-living adjustment (COLA), which adds approximately \$3.0 million to the City's payroll base. However, this projection may change, as contracts for all bargaining units will expire on June 30, 2025, and are currently being negotiated. In this context, the City must balance fiscal sustainability with the need to retain and attract a high-quality workforce.

Healthcare premiums continue to rise this year; however, the rate of increase has tapered off compared to last fiscal year's peak. Kaiser's premium, which rose 17% last year, shows no change this year, while Blue Shield's rates increased by 4%, and dental premium remain unchanged.

The City is also experiencing a sharp rise in its required pension contributions. The total Unfunded Accrued Liability (UAL) payment to CalPERS in FY 2025–26 is projected at \$23.6 million — a \$3.7 million or 19% increase over FY 2024–25.

These increases are primarily due to CalPERS' adjustments in actuarial assumptions—such as lower expected investment returns and changes in retiree longevity—as well as past investment losses that are now being amortized over time. Additionally, COLAs for salaries in South San Francisco have exceeded CalPERS' actuarial assumption of 2.8%¹ which further increases our UAL payment. Since pension liabilities are closely tied to employee compensation, this higher-than-expected wage growth has added upward pressure to the UAL. These impacts are compounded by CalPERS' structured amortization schedules. CalPERS uses a layered amortization approach to manage gains and losses over time, typically spreading each year's changes over 20 years. These schedules are deliberately backloaded: payments begin at lower amounts and ramp up over the first five years. While this method provides participating agencies with less pension contribution volatility, it does result in paying more interest than straight-line amortization of investment losses. The City is experiencing the ramp up period, and payments are rising in FY 2025–26 not only due to new liabilities, but also due to the natural progression of earlier amortization layers reaching their peak. This structured, escalating curve is intended to smooth volatility over time but presents near-term budget pressures for the City.

With respect to CalPERS' investment portfolio performance in the current fiscal year, while it experienced significant paper losses due to market volatility from federal government tariffs, through May 9, 2025, the market value of CalPERS investment portfolio is \$533.6 billion, which is a 6.1% year to date return on investment (ROI). Of note, it is the deviation between the discount rate (currently 6.8%) and the ROI that determines whether CalPERS amortizes an investment gain or loss for a fiscal year.

Other non-personnel operating costs are also rising. Mid-year adjustments to utility rates have been carried forward into the new budget, contributing to higher baseline expenses. In addition, ongoing

¹ <https://www.calpers.ca.gov/documents/jrs-actuarial-valuation-2024/download?inline>

inflation continues to drive up the cost of supplies, materials, and contracted services, placing added pressure on the City's operating budget. To help manage rising costs, the City Manager instructed departments to be highly selective in submitting new requests during the budget development process –especially those related to staffing. With limited exception, new position requests were discouraged in order to contain long-term cost growth and preserve budget flexibility. This directive reflects a strategic effort to align the City's service levels with available resources, ensuring fiscal sustainability while minimizing the accumulation of ongoing obligations in a challenging revenue environment.

Table 1 illustrates the citywide impact of these trends. While revenues are projected to increase slightly from FY 2024–25 to FY 2025–26, overall expenditures, particularly payroll and supplies and services, are rising more sharply, resulting in a projected **net deficit of \$6.0 million**:

Table 1. Citywide Operating Budget (in million)

Funds	Gen F	Meas W	Spec. Rev	Ent. Fund	ISF	Other	Total
Revenue	\$139.0	\$14.6	\$9.6	\$37.6	\$31.1	\$0.0	\$232.1
Transfers In	\$1.5	-	-	\$0.9	\$0.3	\$13.2	\$15.9
Payroll	(\$117.0)	(\$0.2)	(\$1.1)	(\$14.0)	(\$19.6)	(\$0.0)	(\$151.9)
Supplies & Svcs	(\$25.0)	-	(\$1.9)	(\$14.3)	(\$11.0)	(\$0.1)	(\$52.2)
Capital Purchases	(\$0.0)	-	(\$0.1)	(\$1.1)	(\$1.4)	-	(\$2.6)
Debt Service	-	-	-	(\$5.5)	-	(\$13.2)	(\$18.7)
Inter Dept	(\$10.2)	-	(\$0.0)	(\$2.3)	(\$0.1)	-	(\$12.6)
Transfers Out	(\$0.5)	(\$13.2)	(\$2.2)	-	-	-	(\$15.9)
Surplus/ (Deficit)	(\$12.2)	\$1.2	\$4.3	\$1.3	(\$0.6)	(\$0.1)	(\$6.0)

Table 1 highlights the growing gap between revenue growth and expenditure needs, a trend that without strategic action, could significantly constrain the City's ability to sustain existing service levels in the years ahead.

The remainder of the discussion of this report will be focused mainly on the General Fund operating budget. The General Fund is the City's largest and core operational fund, where all of the City's tax revenues and the bulk of the essential services are delivered by departments such as Economic and Community Development, Fire, Library, Parks and Recreation, Police, Public Works, and City Administration are budgeted and accounted for.

GENERAL FUND OVERVIEW – EXECUTIVE SUMMARY

City Council adopted the FY 2024-25 mid-year budget on February 12, 2025. At that time General Fund total revenues and resources were projected to be \$152.6 million, while expenditures were projected at \$159.5 million resulting in a General Fund deficit of approximately \$6.9 million.

FY 2024-25 Budget update

Since mid-year, additional updates have prompted revisions to the year-end projections.

As shown in Table 2, the projected net deficit has improved slightly, decreasing from \$6.9 million to \$5.8 million.

The adjustments following the mid-year, as shown in Table 2 are:

1. Following the mid-year adjustment, subsequent budget adjustments have resulted in a net reduction of \$2.7 million to the projected year-end available fund balance.
2. Further Adjustments represent additional adjustments by staff on the projected revenues and expenditures.
 - a. Revenues:
 - i. \$0.2 million in City Council authorized budget adjustments increasing revenue.
 - ii. \$1.4 million reduction in revenue due to the one-time billboard project being moved to the next fiscal year.
 - b. Expenses:
 - i. \$2.9 million in City Council authorized budget adjustments increasing expenditure authority.
 - ii. \$3 million reduction in projected payroll expenses due to additional anticipated vacancy savings.
 - iii. \$2.2 million reduction in Supplies and Services due to the closure of completed Purchase Orders with remaining balances.

Table 2. General Fund Year End Projection

	Mid-Year Projected FY 2024-25 Year End	Updated Projected FY 2024-25 Year End
Year Start Available Fund Balance	34.8	34.8
Adjustments to Fund Balance ¹	7.8	7.8
Revenues (inflows)	145.3	144.1
Expenditures	(159.9)	(157.6)
Change in Available Fund Balance	(6.9)	(5.8)
Projected Year-End Available Fund Balance	27.9	29.0

1. Adjustment to fund balance is the release of encumbered funds back into the available reserve.

Despite the projected available fund balance of \$29.0 million in the General Fund reflecting a 17 percent decrease when compared to the prior year, it remains at a fiscally sound level.

FY 2025-26 Proposed Budget

As the City begins development of the FY 2025–26 budget, it continues to monitor a range of national and state economic risks that may impact fiscal performance. At the national level, slower-than-expected economic growth, persistent core inflation, and the potential for prolonged high interest rates are creating uncertainty for both consumer behavior and municipal revenues. At the state level, ongoing budget deficits in California- unlikely to improve in near term- pose additional risks, particularly for local governments that rely on intergovernmental funding or economic activity linked to state-level policy. These factors present a greater risk to the City’s revenues than to its expenditure, as approximately 80 percent of General Fund spending is committed to

personnel costs, which tend to remain stable and are less immediately affected by economic fluctuations. These fiscal pressures provide important context for the City’s FY 2025–26 General Fund budget, which, as shown in Table 3, requires the use of \$12.2 million in General Fund available fund balance to close the budget gap, representing a 43 percent reduction in City’s General Fund’s available fund balance.

Table 3. General Fund Operating Budget

FY 2025-26 Proposed Budget (in millions)	
Beginning Available Fund Balance	\$29.0
Revenues	\$140.5
Less: Expenditure	152.7
Surplus/ (Deficit)	(12.2)
Use of General Fund Reserve	12.2
Net Surplus/(Deficit)	Balanced
Ending Available Fund Balance	\$16.8

The table above provides a high-level overview of the General Fund's projected revenues and expenditures for FY 2025–26. To better understand the factors driving the City’s financial position, the following sections provide additional detail, beginning with the revenue categories. Each revenue source is influenced by a range of economic, policy, and operational factors that shape the City’s ability to fund services and maintain fiscal stability.

1. FY 25-26 GENERAL FUND REVENUE PROJECTIONS

The FY 2025-26 Operating Budget has been developed, assuming many of the revenue categories would experience moderate to flat growth. Comparisons are generally made to the prior year adopted budget unless otherwise noted.

1. Property Tax revenue is projected to be higher based on historical information, but slightly lower than the mid-year update due to the assumption that the State of California will not appropriate funds to backfill the VLF shortfall
2. Sales Tax is expected to decrease from last year’s adopted but remain flat from the mid-year update.
3. Transient Occupancy Tax (TOT) revenue projected with modest increase.
4. Other Tax, which includes the voter-approved update to the Business License Tax, is projected to have a significant increase.
5. Franchise Fees remain flat
6. Permit Fee revenues are projected to decrease significantly.

The General Fund revenue forecast (excluding Measure W), Table 4 for FY 2025-26 is shown below, set against FY 2024-25 budget and FY 2023-24 actuals (in millions):

Table 4. General Fund Operating Revenue Budget

REVENUES <i>(in millions)</i>	FY 2023-24	FY 2024-25		FY 2025-26	
	Actual as of 6/30/2024	Adopted Budget	Adjusted Budget	Proposed Budget	Percent Change from FY 2024-25 Adopted
Taxes					
<i>Property Tax</i>	\$56.4	\$50.2	\$57.1	\$56.9	13.3%
<i>Sales Tax</i>	23.2	23.2	21.2	21.2	-8.6%
<i>Transient Occupancy Tax</i>	14.9	14.5	14.8	15.3	5.4%
<i>Other Tax</i>	7.1	6.7	7.7	9.0	34.6%
Franchise Fees	5.3	6.2	6.2	6.2	0.0%
License and Permits					
<i>Building</i>	8.3	9.0	8.0	5.7	-36.7%
<i>Fire</i>	3.8	2.3	2.9	2.7	15.7%
<i>Public Works</i>	1.6	1.8	2.7	2.3	25.7%
<i>Other</i>	0.2	0.0	0.0	0.1	700.0%
Fines & Forfeitures	0.5	0.9	0.9	0.9	0.1%
Intergovernmental	6.5	2.7	4.9	2.9	10.7%
Charges for Services					
<i>Planning</i>	0.7	0.4	0.4	0.8	86.5%
<i>Fire</i>	4.8	3.7	3.9	3.3	-9.5%
<i>Parks & Recreation</i>	4.2	3.4	3.4	3.5	2.7%
<i>Police</i>	1.2	1.1	1.1	1.0	-8.6%
<i>Other*</i>	0.1	0.0	0.0	0.0	4.9%
Inter-Fund Admin Charge	2.0	2.0	2.0	2.0	0.0%
Use of Money & Property	7.1	4.5	5.7	5.1	13.5%
Other Revenues	0.3	0.3	0.3	0.3	0.1%
Transfers In	6.3	1.7	2.3	1.5	-10.1%
PO/CIP Rollover			10.5		
Measure W	0.0	3.0	0.0	0.0	-100.0%
TOTAL REVENUES	\$154.6	\$137.4	\$156.0	\$140.5	2.2%
*Revenue appears as 0 due to rounding.					

Property Tax remains the City’s largest revenue source, projected at \$56.9 million in FY 2025-26. Over the past five years, property tax revenues grew at an average annual rate of 6%, fueled by a strong economy and significant development activity. This growth is reflected in the assessed value of properties in South San Francisco, which rose by 12% in 2023 and 9% in 2024.

However, in 2025, assessed value growth slowed sharply to just 2.23%. As a result, staff have projected only a modest increase in property tax revenue over the current year’s adjusted budget. While the growth rate is lower, staff have updated the forecasting methodology to use the adjusted budget as the baseline, rather than the prior year’s base budget as was previously done. Since the adjusted budget is significantly higher than the base, this change results in a notable increase over the prior base budget.

Growth in this revenue stream is further constrained by the increasing risk of Property Tax In-Lieu of Vehicle License Fee (VLF) shortfalls, driven by the declining number of non-basic aid schools. The State is expected to consider this claim for appropriation as part of its FY 2025-26 budget. However, Governor Newsom's proposed FY 2025-26 budget does not include any appropriations to cover the FY 2023-24 shortfall, of which the City's share is \$4.8 million. Although the State has consistently appropriated funding for San Mateo County's VLF shortfalls since FY 2019-20, these funds are now at significant risk due to mounting State budget pressures and the sharp increase in the shortfall over the past three years. The City has submitted a letter to its state representatives to address this matter. To be conservative, staff have not included the state backfill for the FY 2023-24 VLF shortfall in the proposed budget but will continue to monitor and update as needed.

Despite these issues, property tax revenues are projected to increase by \$6.7 million, a 13.3 percent increase over the FY 2024-25 adopted budget due to continued increase in the City's share, as a taxing entity, of property tax residual from the former Redevelopment Agency (RDA). Also, if the state backfills the FY 2023-24 VLF shortfall, the City's projected property tax revenue will increase by \$4.8M.

Sales Tax revenues in the City of South San Francisco have experienced fluctuations due to various economic factors. Since the adoption of the FY 2024-25 budget, the City's sales tax consultant has revised projections downward in response to factors such as rising unemployment, a shift in consumer spending from taxable goods to non-taxable services, and increasing costs in areas like housing, insurance, groceries, energy, healthcare, and education. At the end of 2024, only 6 of California's 58 counties reported positive sales tax growth, while 26 counties experienced year-over-year declines of at least 4% in the local 1% Bradley-Burns revenue. Statewide, sales tax revenues have declined in seven consecutive quarters, with an eighth projected.

Consumer sentiment remains one of the most significant drivers of sales tax revenue. Amid ongoing uncertainty related to tariffs and persistent inflationary pressures, consumer spending has slowed, contributing to the deceleration in sales tax growth and overall revenue performance.

Sales tax revenues in FY 2025-26 are expected to decrease by \$2 million, or 8.6 percent, compared to the FY 2024-25 adopted budget. As discussed during the FY 2024-25 Mid-Year budget meeting in February 2025. The City's sales tax revenue is particularly sensitive to gas prices as gasoline sales tax makes up a significant portion of the City's overall sales tax revenue, so any major changes in gas prices can directly affect our revenue performance. At mid-year, California was experiencing lower gasoline prices. With the planned closures of refineries in the East Bay, the impact on gasoline price remains to be seen. To reflect this change, and per the City's sales tax consultant, a FY 2024-25 mid-year adjustment was made to revise the sales tax forecast downward. For FY 2025-26, projected sales tax revenue is \$21.2 million. While this is \$2.0 million lower than the FY 2024-25 adopted budget, it is slightly above the revised mid-year estimate. This projection aligns with the updated trend and reflects a stabilization in revenue following the reclassification.

Transient Occupancy Tax (TOT) revenue has experienced a strong recovery since the pandemic, reflecting renewed domestic travel activity. However, recent declines in international tourism raise concerns, and the full extent of their impact on TOT revenue remains to be seen. In FY 2024-25, hotel occupancy reached 66 percent. For FY 2025-26, we project a 68% occupancy rate. Based on

this assumption, staff expects TOT revenue to increase by \$0.8 million, representing a 5.4% increase over last year's adopted budget.

Other Tax revenues, comprised primarily of the Business License Tax and Commercial Parking Tax, continue the upward trend projected at mid-year. At that time, Business License Tax revenue was revised upward by \$1 million. This additional increase results in a total of \$2 million above the prior year's adopted budget, driven by the voter-approved tax update. Staff have increased Commercial Parking Tax revenue to match current year actuals.

Franchise Fee revenues are expected to remain flat in FY 2025-26 compared to FY 2024-25. The total includes a one-time electronic billboard revenue of \$1.4 million originally budgeted for FY 2024-25. However, due to delays in receiving the funds, this amount is being carried forward into FY 2025-26. The revenue is not anticipated to recur in future years and should be treated as a one-time adjustment rather than ongoing income.

Licenses and Permit revenues remained relatively stable prior to FY 2022-23, supported by strong construction activity and robust economic development throughout the City. The City saw a surge in permits issued in FY 2022-23, when developers rushed to submit applications ahead of anticipated building code changes and fee increases, causing a temporary spike.

However, rising interest rates driven by persistent inflation beginning in mid-2022, combined with increased market uncertainty and regional bank failures, created a more challenging environment for developers in FY 2023-24. These conditions contributed to a slowdown in project activity.

Despite these challenges, staff remains cautiously optimistic about future development but continues to take a conservative approach to revenue projection. Permit revenues for FY 2024-25 were adopted at \$13.2 million and later adjusted upward to \$13.6 million at mid-year. However, for FY 2025-26, permit revenues are projected to decline further by \$2.5 million, bringing the total to \$10.7 million. This represents a significant decrease by the Building Division, partially offset by increases from the Fire and Public Works departments. The overall decline reflects continued softness in the development market, driven by persistently high interest rates and ongoing economic uncertainty.

Intergovernmental revenue primarily consists of grants and includes mutual aid cost recovery for the Fire Department's response to disasters outside the City. This revenue has been increased by \$400 thousand to align with the four-year historical trend. However, the traffic signal maintenance fee, previously budgeted at \$275 thousand, will no longer be recorded as intergovernmental revenue and has been reduced to \$0. The FY 2025-26 budget also includes the continuation of two multi-year library grants totaling \$232 thousand. As a result, the net projected increase in intergovernmental revenue of \$285 thousand, or 10.7%, when compared to the FY 2024-25 adopted budget.

Charges for Services for FY 2025-26, staff expect to see variable changes across different departments. Economic and Community Development (ECD) and Parks and Recreation (P&R) are projected to have increases of 86% and 3% relatively. ECD's increase is due to the expectation that more projects will start over next year. However, the City anticipates lower revenue from the Fire Department for their participation in the ambulance program of about \$350 thousand, a 9% decrease from the FY 2024-25 adopted budget.

Use Money & Property is budgeted at the same level as FY 2024–25. The primary source of revenue for this category is investment in the U.S. Treasuries and high-quality agency bonds, as required by statute. Given recent volatility in U.S. Treasury yields and other fixed-income markets, staff recommends maintaining a flat projection for now, but will monitor the market condition and provide an update during the mid-year review.

Transfers In are budgeted with a \$168 thousand reduction from FY 2024–25. This is due to the elimination of a budgeted transfer from the Developer Fee Fund from the prior year but the inclusion of two transfers from the Special Revenue Fund: \$60 thousand from Police Evidence Revolving account to offset Police recruiting expenses and \$72 thousand from the Opioid settlement to partially offset the cost of the Crisis Intervention Specialist.

2. PROPOSED FY 2025-26 GENERAL FUND EXPENDITURES

The following tables, Table 5 and Table 6, show the proposed FY 2024-25 General Fund expenditure budgets (in millions).

Table 5. General Fund Operating Expenditure Budget by Category (in millions)

EXPENDITURES (in millions)	FY 2023-24	FY 2024-25		FY 2025-26	
	Actual as of 6/30/2024	Adopted Budget	Adjusted Budget	Proposed Budget	Percent Change from FY 2024-25 Adopted
Salary and Benefits	\$106.1	\$113.4	\$114.4	\$117.0 ¹	3.2%
Supplies and Services	23.0	22.1	34.3	25.0	13.1%
Capital Outlay	0.2	0.0	0.7	0.0	0.0%
Debt Service	0.0	0.0	0.0	0.0	0.0%
Interdepartmental Charges	10.2	9.5	9.5	10.2	7.0%
Transfers - Operation	0.5	0.5	0.5	0.5	0.0%
Transfers - Capital Transfers	0.7	0.0	3.4	0.0	0.0%
TOTAL EXPENDITURES	\$140.8	\$145.4	\$162.8	\$152.7	5.0%

1. 2025-26 Salary and Benefits budget assumes \$8.0 million in vacancy savings.

Table 6. General Fund Operating Expenditure Budget by Department (in million)

EXPENDITURES (in millions)	FY 2023-24	FY 2024-25		FY 2025-26	
	Actual as of 6/30/2024	Adopted Budget	Adjusted Budget	Proposed Budget	Percent Change from FY 2024-25 Adopted
City Council	\$0.3	\$0.3	\$0.3	\$0.3	-14.5% ¹
City Clerk	1.0	1.3	1.4	1.4	6.6%
City Treasurer	0.2	0.2	0.2	0.2	26.7% ¹
City Attorney	1.7	1.5	2.3	1.5	4.0%
City Manager	3.4	3.9	4.3	4.8	24.3%
Finance	3.3	3.9	4.2	4.3	11.1%
Non expense/Dept	2.0	1.9	2.2	1.9	0.0%
Economic & Comm Develop	11.1	8.9	12.0	9.6	8.1%
Fire	36.7	36.4	38.1	40.2	10.4%
Police	37.1	38.2	38.4	42.3	10.8%
Public Works	10.1	11.1	14.4	12.6	13.4%
Library	7.7	8.9	9.1	9.3	5.5%
Parks and Recreation	22.9	26.3	29.6	29.1	10.4%
CIP	0.7	0.0	3.4	0.0	0.0%
Non expense/Dept	2.0	1.9	2.2	1.9	0.0%
Salary Savings	0.0	0.0	0.0	(8.0)	-
TOTAL EXPENDITURES	\$140.8	\$145.4	\$162.8	\$152.7	5.0%
Information Technology²	4.2	4.3	4.6	4.7	10.2%

1. Changes are due primarily to adjustments in optional City medical coverage.

2. Non-General Fund: budgeted as internal service fund in Fund 785

FY 2025-26 Expenditure Projection

Attachments 2 and 3 to this report provide a detailed explanation of each department's requests, along with the proposed funding budget breakdown of payroll, supplies and services.

The following provides additional information for each of the major expenditure categories.

Payroll:

- As noted above, the primary drivers of payroll costs are the 3% assumed COLA salary increase as well as the increase in the UAL and health benefit costs. While payroll request details for all funds are provided in **Attachment 2**, the following are the most impactful requests for the General Fund.
 - Police
 - **Change:** New Position Crisis intervention Specialist
 - Cost: \$230,000
 - Source: Opioid settlement for \$70,000, the remainder General Fund.
 - Parks and Recreation.
 - **Change:** Cultural Arts Positions
 - Cost: \$21,000
 - Source: Paid through the Arts-In-Lieu Fee no General Fund Impact.
 - **Change:** Aquatics Positions
 - Cost: \$520,000
 - Source: General Fund
 - **Change:** Senior Program
 - Cost: \$74,000
 - Source: General Fund
 - **Change:** Parks Program
 - Savings: \$(12,562)
 - Source: General Fund

Supplies and Services:

- The proposed budget includes all departmental decision packages (new requests) that have been reviewed by the City Manager and are to be submitted for City Council's approval. These requests are detailed in **Attachment 3** for all funds. However, overall, there are \$1.3 million in new requests for the General Fund. In particular:
 - \$560 thousand these requests are for contractors who support the City's permit and fee process, which means these costs are directly offset by increased projected revenue.
 - \$100 thousand are related to the increased operating costs for the new pool.
 - \$300 thousand from the City Manager's office.
 - \$200 thousand request is for contract service for Abandoned/Derelict Vessel Removal/Destruction at the Marina.
 - \$100 thousand for the biennial community survey.

Interdepartmental Charges:

- Interdepartmental Charges are expenses that are accounted for in the General Fund (and other funds as necessary) and then transferred out to support internal services functions. The largest internal service fund is the Information Technology (IT) Department. In effect, the cost of providing IT services is calculated and then “charged” to various City funds, with the General Fund bearing the majority of the charge.

3. OTHER FUNDS

There are other funds that the City Council oversees beyond the General Fund. The new requests from other funds can be found in *Attachment 3*. Many of the final budgets for these funds are contingent upon the adoption of the Capital Improvement Program (CIP) by City Council. The numbers may change based upon Council’s action related to the FY 2025-26 CIP program.

As noted in the Citywide section, the City’s Enterprise Funds are also experiencing pressure from rising costs. The three Enterprise Funds—Sewer, Parking District, and Stormwater, are summarized below in Table 7. Each fund follows a distinct process for adjusting revenues; however, due to statutory limitations in increasing Stormwater funding, this fund is currently heavily subsidized with transfers from the General Fund and Gas Tax revenues.

Table 7. Enterprise Funds Operating Budgets

Enterprise	Sewer	Parking	Storm
Revenue	\$36.1	\$1.0	\$0.5
Transfers In	-	-	\$0.9
Payroll	(\$12.1)	(\$0.5)	(\$1.5)
Supplies & Services	(\$13.2)	(\$0.8)	(\$0.3)
Capital Purchases	(\$1.1)	-	-
Debt Service	(\$5.5)	-	-
Inter Dept	(\$2.0)	(\$0.2)	(\$0.1)
Transfers Out	-	-	-
Surplus/ (Deficit)	\$2.2	(\$0.4)	(\$0.5)

4. OTHER REQUESTS NOT INCLUDED

Due to ongoing fiscal pressures, departments have opted not to include the following items in this year’s request. Some of these items were previously requested as one-time needs or are directly tied to Council priorities. While they are not part of the proposed budget, the requesting departments wish to bring them to the Sub-committee’s attention for transparency and potential discussion.

- Economic and Community Development
 - Bio Conference 2026 – \$100 thousand; opt for a different venue
 - Citywide Holiday Decorations – \$170 thousand
 - Promotores Social Service Navigators – \$165 thousand.

- Public Works
 - To effectuate the Council Priority of Traffic Management and Safety, a Traffic Engineer would provide the necessary expertise and leadership to implement effective solutions and will have authority over critical traffic control functions, including traffic signal timing implementation, optimization, and coordination and smart corridor traffic management – \$325 thousand.
 - To effectuate the Council Priority of Quality of Life / Implement Clean SSF, addition of four (4) PW Maintenance Workers are necessary to perform clean team operations to proactively address graffiti removal, illegal dumping, city property damage, etc. Additional personnel will enhance the City's ability to maintain clean and safe public spaces - \$600 thousand.

5. RESERVES

The City's financial reserve funds are expected to be approximately \$56.2 million. A breakdown is shown below:

Table 8. General Fund Reserves

Estimated Ending Financial Reserve for FY 2025-26 (in million)	
General Reserve	\$27.8
Infrastructure Reserve*	5.4
CalPERS Stabilization Reserve	6.2
Available GF Balance*	16.8
Total	\$56.2

The **General Reserve**, which represents 20 percent of the City's annual revenue budget, excluding transfers in (General Fund), follows the best practices guidelines from the Government Finance Officers' Association (GFOA).

The **Infrastructure Reserve** is largely comprised of General Fund surpluses that were set aside over previous years in anticipation of the City's future infrastructure projects. The value shown is the unencumbered monies available that have not yet been designated toward a project. It should be noted that within the proposed FY 2025-26 Capital Improvement Program, a net \$1.9 million of direct capital project funding is requested from the Infrastructure Reserves, which is reflected in the ending balance above.

The **CalPERS Stabilization Reserve** was established through two separate Council actions in FY 2015-16 and FY 2017-18 totaling \$5.5 million. Finance took advantage of the higher interest environment and set up a separate investment account with the City's investment manager, Chandler, in December 2022 that yields a higher rate of return. As of April 30, 2025, the balance of the account has grown to \$6.2 million.

The **Available General Fund Balance** is the available fund balance remaining in the General Fund (as shown in the table in the summary section of this report) that has not been assigned for any particular purpose. This balance will change depending on the extent to which expenditures may exceed revenues (deficit) in FY 2025-26. It is important to note that the available fund balance also acts as a buffer allowing for the natural ebb and flow within the General Fund that occurs

during the year as a result of the mismatch between when revenues are received, and expenditures are incurred.

Although placed in different categories, the City Council, by majority vote, is allowed to use the above reserve funds as necessary.

FISCAL IMPACT

For Fiscal Year 2025-26, the City's General Fund is projected to have operating revenues of \$140.5 million and use of General Fund Reserve of \$12.2 million for a total of available revenues and resources of \$152.7 million. Expenditures net of any carryover purchase orders are projected to be \$152.7 million, resulting in a balanced budget.

RELATIONSHIP TO STRATEGIC PLAN

The budget is the City's spending plan that supports Priority Area 3, Financial Stability.

CONCLUSION

The General Fund continues to experience a structural deficit, as revenue growth remains insufficient to keep pace with rising expenditures. Key cost drivers—including personnel expenses, healthcare costs, and inflation—are escalating at a faster rate than incoming revenues. Property tax revenue continues to increase but are anticipated to do so at a slower pace than in previous years. In light of increasing fiscal pressure from the State's own budget deficit, staff has adopted a more prudent approach by assuming that the State will not backfill the FY 2023-24 Property Tax in-lieu of Vehicle License Fees (VLF) shortfall. Should this funding materialize, it could reduce the FY 2025-26 budget deficit by approximately \$5 million. Staff will continue to monitor this and provide updates as new information becomes available.

Revenue sources such as sales taxes and TOT are subject to ongoing uncertainty due to tariffs and inflation. Additionally, permit fee revenues from developers have slowed, influenced by high interest rates and trade-related pressures. To help balance the long-term structural deficit, the City is evaluating potential revenue enhancement strategies. The proposed budget is structured to maintain current service levels, and no significant cuts are proposed at this time.

A key driver of rising expenditures in the FY 2025–26 Proposed Budget is the continued growth in personnel related costs. Since labor negotiations have not yet been finalized, the proposed budget assumes a 3% cost-of-living adjustment (COLA); any changes to this assumption will impact the projected deficit. On the other hand, since the City has experienced higher-than usual staff turnover, staff has included a 7% vacancy assumption, which is approximately \$8 million in personnel costs to account for the anticipated salary savings. Staff will continue to update the budget as more information becomes available.

This budget is prepared with a strategic effort to align the City's service levels with available resources, ensuring fiscal sustainability while minimizing the accumulation of ongoing obligations in a challenging revenue environment.

Staff welcomes feedback from the Budget Standing Committee related to the information contained herein.

Attachments:

Att 1 – General Fund Revenue and Expenditure Reports

Att 2 - New Request – Positions – GF and Other Funds

Att 3 – New Request – Supplies and Services – GF and Other Funds

Att 4 – Department Revenue Adjustments – GF and Other Funds