

July 1, 2019

Honorable Mayor and Members of the City Council:

I am pleased to present to you the fiscal year 2019-20 (FY 2020) operating and capital budgets. The adopted budget serves as a policy document, a financial plan, a communications device, and an operations guide, reflecting the policies, goals, programs and service priorities of the City Council and the community. It was developed based on direction provided by the City Council and feedback received from the Campbell community during the budget development process and recommendations made by each department that I've reviewed and approved.

In preparing the budget for FY 2020, staff conservatively estimated economically dependent revenues so as to not overcommit them to operational expenses should the economy experience a downturn. Additionally, staff continues to explore cost saving and revenue enhancement options to help minimize the need for reserves to be used. While the economic growth of the past ten years remains positive overall, there have been definite indicators that it has slowed down over the past two years and will likely continue to be flat in the near term. This, combined with ongoing expenditure commitments, presents fiscal challenges to the City and requires diligence and discipline in maintaining a balanced and sustainable budget while meeting service level demands. During any period of economic transition, it is difficult to know the exact timing of how and when the economy will begin to shift directions and to what degree it will begin to impact programs and services. Thus, staff has made a concerted effort in presenting a balanced budget that does not reduce services or programs to the greatest degree possible.

Some of the significant issues surrounding this year's operating budget include: keeping up with service level demands, increased pressure on retirement costs resulting from the CalPERS employer contributions, looking for ways to stimulate economic development, and converting most of the limited-term positions to permanent positions within the operating budget.

The budget is funded with a combination of ongoing operating revenue and reserves, primarily CIPR (Capital Improvement Plan Reserves), where appropriate, for expenditures considered to be one-time. Budgets in the prior years funded limited-term positions with CIPR funds. For the FY 2020 budget the limited-term positions are either converted to permanent positions funded within the operating budget, extended, or eliminated where appropriate. Limited-term positions are no longer funded with CIPR.

History has shown the economy operates in cycles of about 10 years on average with ups and downs being the norm. Since the recent recovery/expansion has been ongoing since 2009, prudence would suggest that precaution be taken into consideration during the City's strategic

planning process. Accordingly, a modest economic slowdown has been factored into future budgetary projections.

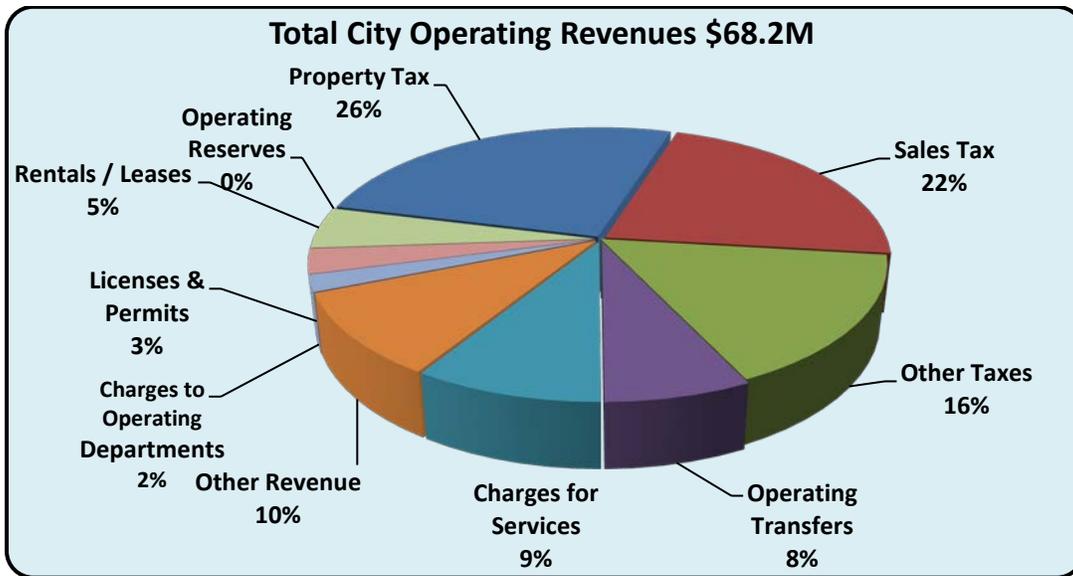
CalPERS rates will also continue to increase over the coming years. CalPERS' action to lower the discount rate used to calculate the City's required pension contribution amount took effect last fiscal year. This will increase the City's required contribution amount significantly over the ensuing seven years and beyond. While the City has accumulated \$2.5 million in reserves specifically for PERS and OPEB costs, this should be used judiciously. Staff continues to explore strategies to ensure that staffing and expenses can be sustained over the long term.

BUDGET SUMMARY

The combined FY 2020 operating and capital budgets total \$79.3 million including \$5.7 million in capital transfers. Related revenue sources total \$77.6 million. The net difference is a deficiency of \$1.7 million in revenues compared to expenditures; to be offset by using available fund balances. The following table depicts the total operating and capital budget for the City compared to the prior fiscal year:

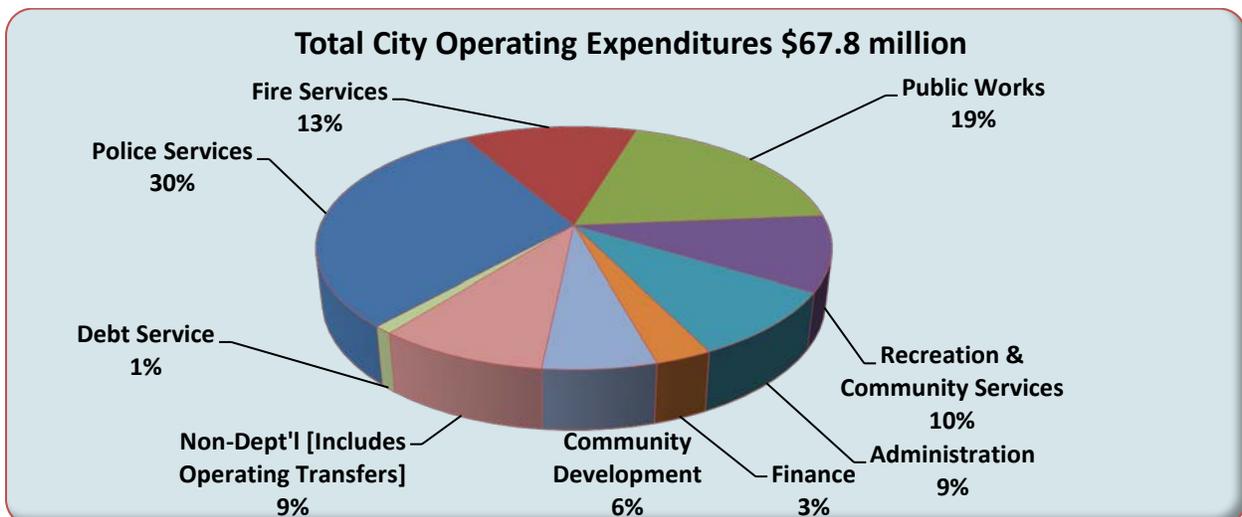
	FY 2019 - 20			FY 2018 - 19			Operating Budget Change	Percent Change
	Operating Budget	Capital Budget	Total Proposed Budget	Operating Budget	Capital Budget	Total Amended Budget		
Expenditures	\$ 62,827,076	\$ 5,805,450	\$ 68,632,526	\$ 59,799,732	\$ 3,061,039	\$ 62,860,771	\$ 3,027,344	5.1%
Transfers	4,960,601	5,745,450	10,706,051	4,900,165	3,061,039	7,961,204	60,436	1.2%
Total	\$ 67,787,677	\$ 11,550,900	\$ 79,338,577	\$ 64,699,897	\$ 6,122,078	\$ 70,821,975	\$ 3,087,780	4.8%

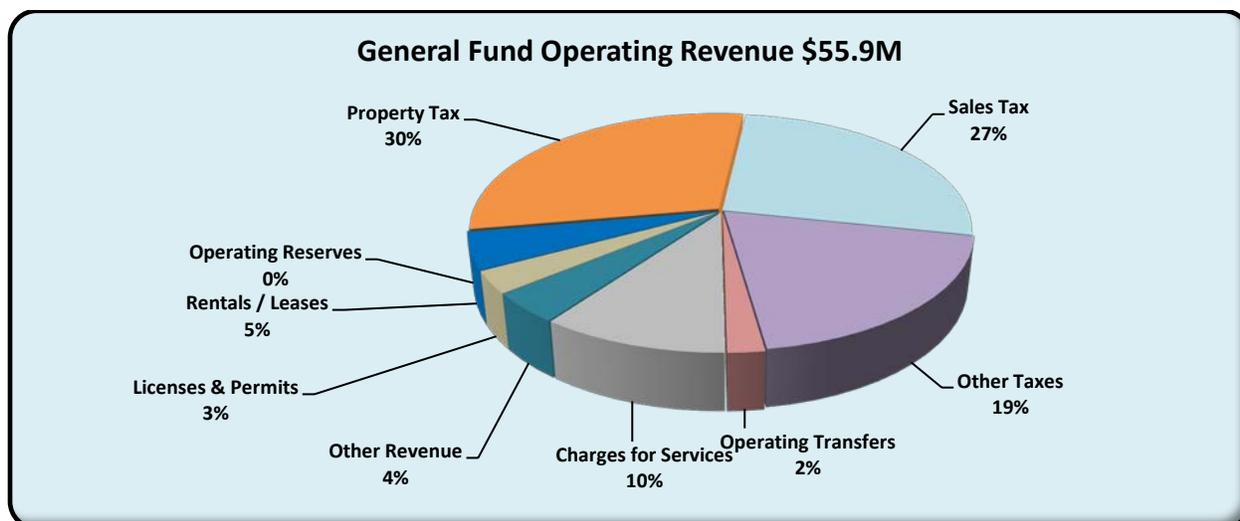
Operating Budget: Overall, the operating budget increased 4.8% from the previous year. The operating portion of the budget is \$67.8 million with related revenue sources of \$68.2 million; thereby resulting in an approximately \$400,000 excess of revenues over expenditures. The budget reflects expenditures that are expected to recur annually as well as those that may be non-recurring or one-time in nature.



The chart above illustrates the various revenue sources that are collected by the City. Property and sales taxes are the largest components and are critical to the City's fiscal health. However, these revenues are subject to fluctuations. While property tax is relatively stable, sales tax is more susceptible to market conditions and varies with the economy. Other taxes, such as franchise, transient occupancy and business license, comprise approximately 16% of all revenues. These, too, are impacted by the business climate and can vary from year-to-year.

The chart below illustrates how the City's revenues are spent. The largest percentage of the budget at 30% is spent on police and fire services. Public Works at 19% is the next largest component which includes engineering, land development and environmental services as well as parks and streets maintenance. Non-recurring or one-time expenditures are typically funded with a combination of one-time revenues, specific reserves and/or unreserved fund balances, all of which are revenue sources for purposes of presentation within this document. No use of the Economic Fluctuation Reserve (EFR) is contemplated in this budget but will be explored and discussed with Council in the future should the economy experience a significant downturn which would impact City service levels.





General Fund operating revenues and expenditures are budgeted at \$55.86 million and \$55.15 million, respectively, indicating an anticipated surplus of approximately \$700,000.

Capital Budget: The City's Capital Improvement Plan (CIP) is used both as a short and medium-range plan for the acquisition, improvement and/or renovation of City assets, infrastructure in particular. The CIP is reviewed and updated annually by a committee of senior management staff. It includes projects and equipment items valued in excess of \$25,000. Also included are studies or evaluations that will potentially lead to a capital project. Capital items with a value of less than \$25,000 are included in the operating budget in the appropriate capital outlay line item or as a building maintenance special project if related to facility improvements.

The CIP is presented on a five-year horizon in which project scheduling is dependent upon various factors including the urgency of need, availability of funding and staff workload to name a few. The first year of the CIP is incorporated within the operating / capital budget document, and formally appropriated by the City Council. The remaining years function as a project planning and budgeting tool. Any expected operating budget impacts resulting from the CIP are incorporated into the operating budget. The City has historically funded many of its capital projects with either General Fund CIPR or Federal, State and local grants. The value of all projects in this year's five-year CIP increased by \$1.7 million compared to the previous year resulting primarily from additional streets and signals, parks and open space, and public facility projects.

There are 11 capital projects requiring funding in FY 2020. Project expenditures of \$5.73 million plus related inter-fund transfers of an additional \$5.83 million total \$11.6 million in capital appropriations. The largest component of these projects is \$2.8 million for street maintenance projects and \$1.89 million for park and open space improvements at John D. Morgan Park. The full CIP, along with details of specific projects, can be found in the Capital Improvement Plan tab of this document.

REVENUES

The City has several key revenue sources on which it depends to provide funding for ongoing services to the community. The two sources, sales and property taxes, are driven by the economy and factors that are generally beyond the direct control of the City. Other revenue

sources are based on user fees and demand for specific City services. Together, they form a foundation that supports funding of basic City services. Program managers evaluate comparative historical data and factor in necessary adjustments for inflation, changes in assumptions for anticipated volume of activity, and any fee increases. Lastly, the most current economic outlook is taken into consideration to determine estimates for the upcoming year. Total budgeted revenue for FY 2020 is \$77.6 million, including capital funding sources of \$9.4 million. This reflects an increase of \$4.2 million (5.7%) from the previous estimated year-end actuals. In looking at just the operating budget component, total revenue is estimated at \$68.2 million, a slight decrease of \$70,000 (0.1%) from the previous estimated year-end actuals.

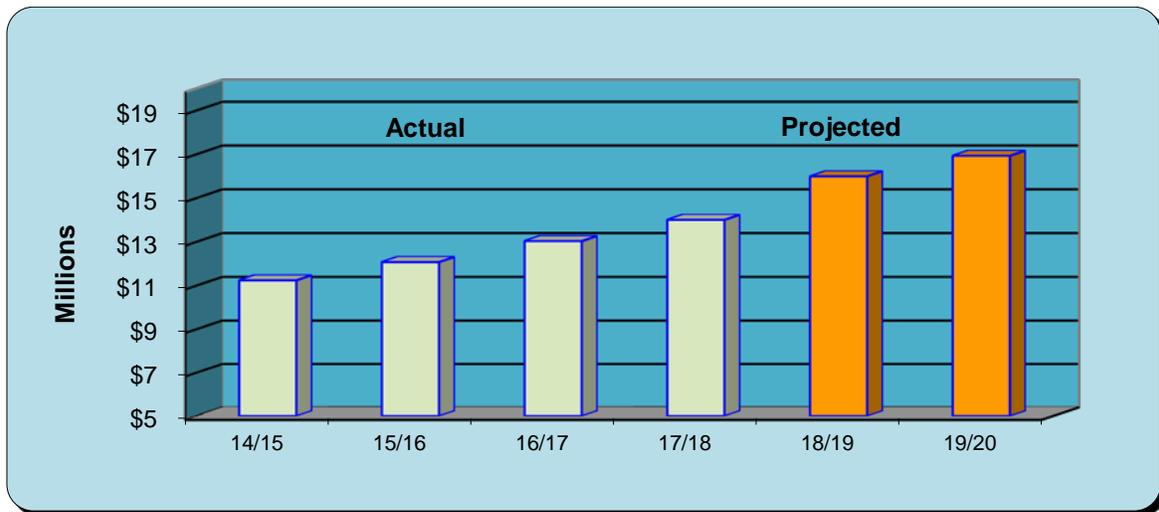
It should be noted that the capital project budget can fluctuate significantly from year to year depending upon the number and magnitude of projects that are approved. Capital projects are generally one-time in nature, and they are funded with non-operating revenue so there is generally no impact on the operating budget funding sources. The operating and capital budgets each contain transfers-in totaling \$5.83 million. Although this tends to make the budget appear higher in total than it actually is, the transfers-in on the revenue side are offset by transfers-out on the expenditure side. Including transfers in the City's adopted budget is done to readily demonstrate that budgets are balanced and match the internal budgeting system.

General Fund: Contained within the budget are a variety of funds, each with its own source(s) of revenue. The budget document is organized by operating department, then by program within the department. The General Fund is the City's largest single fund where the majority of services are budgeted. It funds general services such as police, fire, parks, streets, recreation and administration. Therefore, the focus of this section of the budget message is on this fund. General Fund operating revenue, excluding capital funding sources is estimated to be \$55.9 million, an increase of \$1.6 million (2.8%) from the previous estimated year-end actuals. Such growth was primarily driven by increases in property tax, sales tax, and charges for services revenue. All are indicative of a robust housing market, a strong economy, and low unemployment.

Property Tax: Property tax revenue in the General Fund for FY 2020 is projected at \$16.9 million, an increase of 5.9% over FY 2019 estimated actual revenue and is the largest single revenue source for the General Fund and one of the most stable over time. This represents approximately 30% of General Fund net operating revenue. Assessed values on secured residential and commercial properties continue to improve as a result of the strength of the job market and low unemployment that, together with low interest rates, continue the ongoing demand for housing. Development activity in the City has been brisk although the number of larger scale projects has diminished. Accordingly, related revenues are expected to continue, but at a reduced level compared with previous recent years. Nonetheless, the County base tax roll is expected to grow from the sales of pre-Proposition 13 homes whose values then increase to current market levels.

The primary factors used in the projection of revenues are historical growth in assessed valuation and new construction. The County Assessor provides periodic information and estimates of property values to the City upon which the revenue estimates are based. The following graph depicts the historical and projected FY 2020 property tax revenues in the General Fund.

Property Tax Trend - General Fund



Sales Tax: Sales tax, the second largest projected revenue source for the General Fund in FY 2020 at \$15.3 million, comprises approximately 27% of its net operating revenue base. Net revenues exclude reserves, which are not considered to be an on-going revenue source. This revenue base is comprised of approximately 5,200 diverse businesses throughout the City (although not all of these generate sales tax). While most of the largest sales tax producers can be considered stable businesses, they are still subject to the fluctuations from general and regional economic conditions which have a direct impact on the City's sales tax revenue base. During the past year, this critical revenue source saw some growth. However, the rate of growth has slowed down considerably the past couple of years and is expected to flatten further at approximately 2% over the next couple of years, absent a significant recession. Noteworthy contributors of sales tax revenue come from the food products, general retail, and business to business segments.

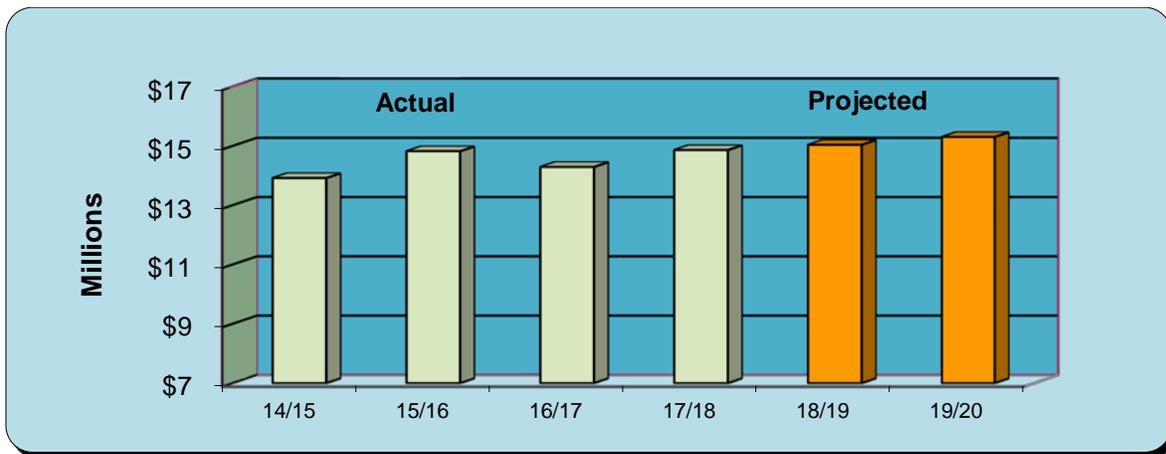
Growth in the sales tax base is challenging because the City is largely "built out" with limited space for additional significant retail development. Instead, the City must rely on "in-fill" projects of smaller scale and redevelopment of existing parcels. In addition, increased regional competition and the financial impact of electronic commerce have been impacting the revenues of some of the City's larger existing sales tax producers. By comparison, other Silicon Valley cities and the State overall have seen higher levels of sales tax growth, on average, due to their capacity to accommodate new retail business when the economy expands. Nevertheless, Campbell continues to enjoy a favorable reputation as a destination for many leisure activities such as shopping, dining and experiencing the many year-round festivals and events that occur throughout the City. This has played a significant role in bringing people into the City and continues to have a positive effect on the City's sales tax revenue.

A significant component of the total sales tax number above is the $\frac{1}{4}$ cent add-on that became effective in April 2009 resulting from the passage of Measure O by Campbell voters. This portion of the sales tax alone is estimated to generate \$2.9 million, or almost 19%, of the total sales tax revenue, in FY 2020.

Consequently, the FY 2020 Sales Tax revenue estimate of \$15.3 million is \$0.3 million (1.7%) higher than FY 2019 estimated actual revenue. The budget is based, in part, on recent performance and forecasts provided to the City by its sales tax consulting firm.

The graph below reflects sales tax performance for the past five fiscal years and projected FY 2020.

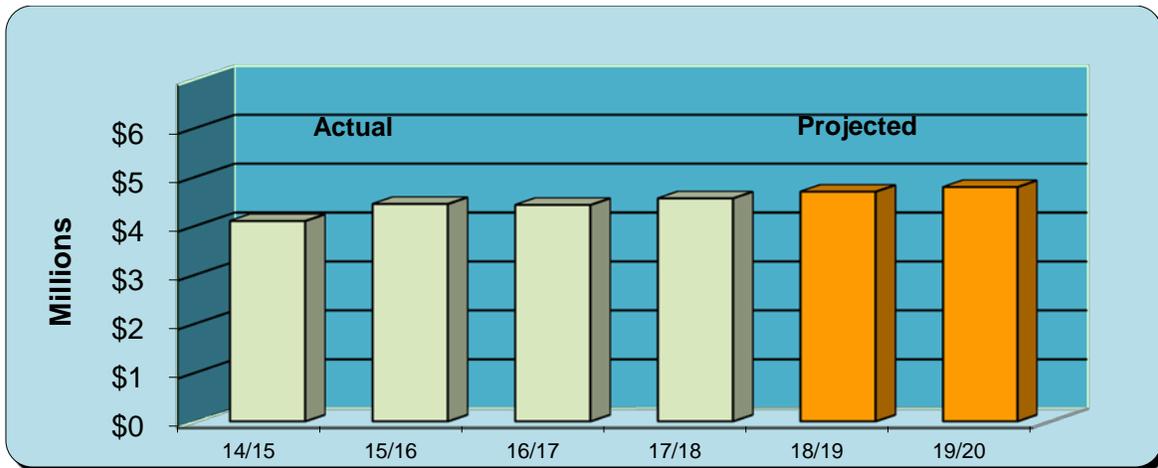
Sales Tax Trend - General Fund



Transient Occupancy Tax: This revenue source, more commonly referred to as hotel/motel tax, or simply TOT, is derived from a 12% surcharge that is applied to the room rates of the City's hotels/motels. TOT revenue in the General Fund for FY 2020 is budgeted at \$4.8 million, a \$0.09 million or 2.0% increase over estimated FY 2018 actual revenue, reflecting somewhat flat, but continued expected strength in the local travel and business sector. Despite the continued strength of corporate technology companies, occupancy and room rates have leveled off though indicating a relative flattening of this revenue for now and modest growth. This revenue comprises about 9.0% of net General Fund revenue in FY 2020.

Key factors in developing the revenue projections are such things as historical trends, the number of available rooms, the occupancy rate, exemptions, new rooms coming on-line, and the weighted average room rate. In recent years, Campbell hotels/motels have averaged occupancy rates of close to 90%. The next year is expected to level off and possibly see a slight decline in the near term as the transient population is expected to decline. The following chart depicts historical activity and projections for FY 2020.

Transient Occupancy Tax (TOT) Trend - General Fund

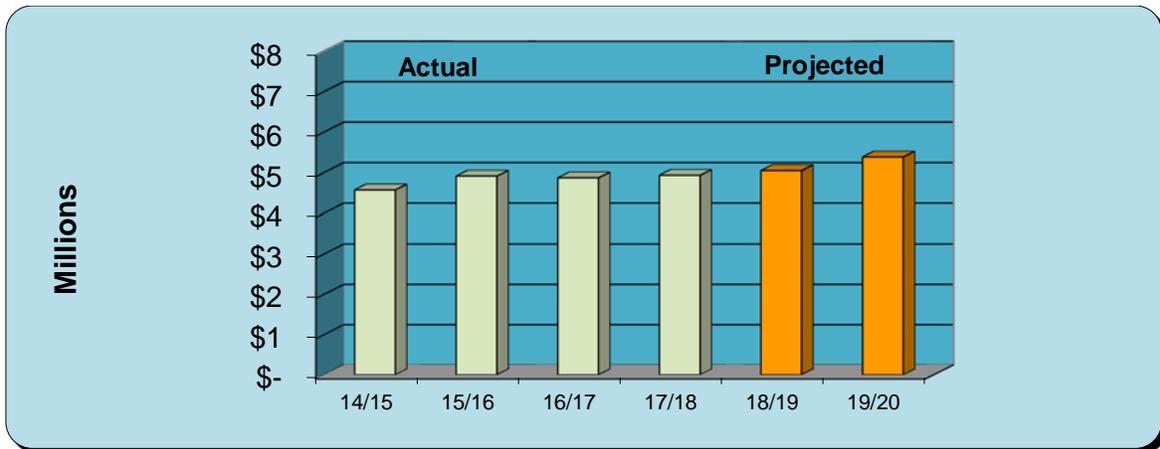


Charges for Services: Charges for services include revenues derived from a variety of sources, the largest being Recreation program fees that consist of classes/lessons, trips/tours, preschool and theater revenues. Other fees are charged for Police and Fire services; Engineering services; zoning review and business license processing.

The City maintains a cost allocation plan and user fee model that is updated periodically, and which serves as the basis for assessing and collecting fees and allocating indirect charges from operating departments. A Council approved User Fee Policy establishes a framework for cost recovery from which fee modifications are proposed and approved annually in conjunction with the budget process. Fees are increased to maintain recovery levels per the policy. The most recent User Fee study was performed in 2018 and 2019, with Council adoption occurring on May 7, 2019. All revised user fees are effective either July 1, 2019 or July 8, 2019.

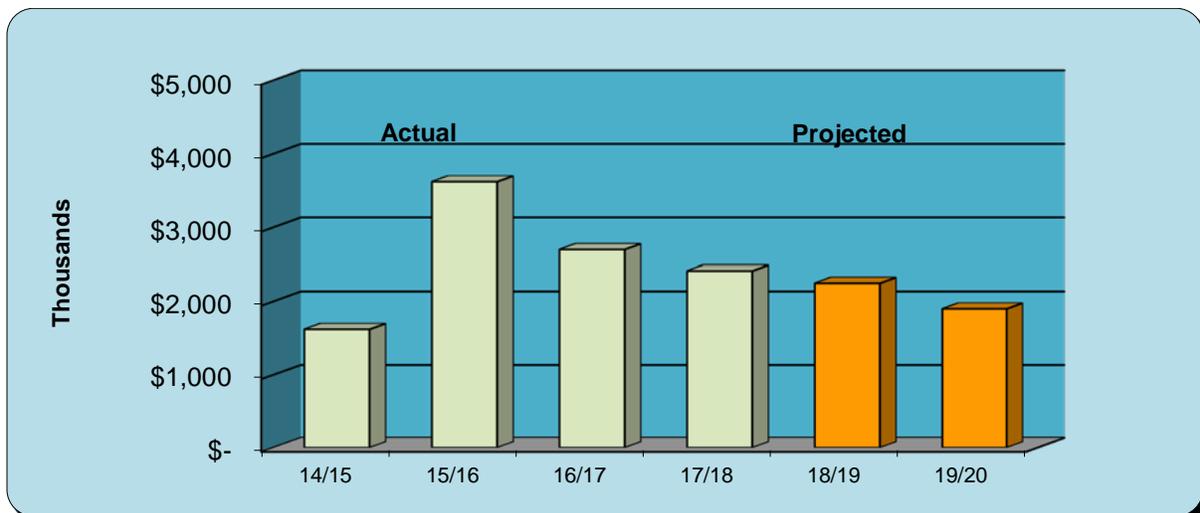
In addition to the cost of providing the service, other factors such as the allowable percentage of recovery, number of participants or attendees, inflationary factor, comparison to other agencies, and the historical trends are analyzed for nearly all fees and charges. The combined revenue for all user fees and charges is anticipated to generate \$5.4 million for the General Fund during FY 2020, which is \$0.3 million (6.6%) higher than FY 2019 estimated revenues. The following chart depicts historical activity and projections for FY 2020:

Charges for Services Trend - General Fund



Licenses & Permits: Revenues in this category are composed primarily of construction permits and advanced plan check fees. Also included are fire permits and other Building Division fee revenues. As can be seen from the chart below, revenues from this category fluctuate significantly with the level of development activity from year to year and can be difficult to estimate. The numbers, however, do serve as a measure of how the local economy is performing. Licenses and Permits revenue for FY 2020 is expected to be less than estimated FY 2019 revenue and equal approximately \$1.9 million; a \$0.3 million or 15% decrease from FY 2019. Building and development activity has been considerable over the past several years, in particular, FY 2016 which turned out to be an all-time peak year for collected revenues due to both the volume and magnitude of several large projects that were approved during this period of time. Un-audited, FY 2019 Licenses and Permits revenue is also strong, but staff expects this revenue source to see a reduction in FY 2020 as large scale, high value projects are replaced by an increasing volume of smaller value projects such as home remodels, still requiring considerable staff time. As such, while staff does not expect its overall workload to decrease, it does expect to generate lower overall revenue from this shift in the composition of building and development activity.

Licenses & Permits Trend - General Fund



Lease Rental Income: The City collects rental income from leasing out space to tenants at its Community Center as well as from rental of its Theatre and other Community Center buildings, in addition to a small amount from telecommunication antennas. Lease rental income represents approximately 3.0% of net General Fund operating revenues. FY 2020 revenue is budgeted to increase 2.5% from FY 2019 estimated actual revenue to \$2.9 million. Occupancy is expected to continue at or near capacity for the next year. The revenue projections are based on actual lease contracts and estimated market rates for available space.

Franchise Tax: Franchise tax revenue is derived from fees charged to various utilities for doing business within the City. The fee is generally computed as a percentage of the gross income of the utility. This revenue source is estimated to generate approximately \$3.7 million for FY 2020 an increase of 1.9% over estimated FY 2019 actuals. The estimate is developed from a combination of increased services/customers plus an inflationary factor averaging 2% on the historical amounts generated by utilities operating within the City limits, e.g. cable, water, garbage, gas and electric. Others are set contractually.

Other General Fund Revenues: The remaining significant General Fund revenue sources consist of operating transfers-in of \$1.3 million, representing reimbursements from other funds for services provided by the General Fund. Where appropriate, other revenue sources are projected to reflect modest inflationary increases and/or changes in activity levels.

Revenue - Other Funds

Various other funds are contained within the budget as discussed below. In summary, each fund's operating revenue meets or exceeds operating expenditures consistent with established financial policies. Exhibit A within each program budget provides a summary of that program's funding sources and all revenues monitored by that program. Narrative descriptions pertaining to the revenue sources can be found in the Financial Summaries section of this document. Charts and graphs for General Fund revenue as well as total City revenue, in addition to what is presented in this budget message, can also be found in the Financial Summaries section of the budget document. Because this budget is organized by program, funds other than the General Fund are included in the respective operating department's section of the budget along with the General Fund program. Each program is identified with the fund number at the beginning of each section.

Special Revenue Funds consist of Vehicle Impact Fees; Gas Tax; Lighting and Landscape District; Housing and Community Development; Environmental Services; Parkland Dedication; Asset Forfeiture; Supplemental Law Enforcement; Transportation Development Act (TDA); Other Grants and Other Special Revenues; Housing Trust; Community Facilities District #1 and Community Facilities District #2.

Gas Tax revenue is considered a State-shared revenue. Projections for this revenue source come directly from the State on an annual basis. Revenue in funds such as the Lighting and Landscape District and Environmental Services are based on rates that are assessed to individual properties depending upon type of service being provided or type of property. Total operating revenues for Special Revenue funds for FY 2020 are \$8.7 million, a decrease of \$0.2 million (2.2%) for estimated FY 2019 actuals.

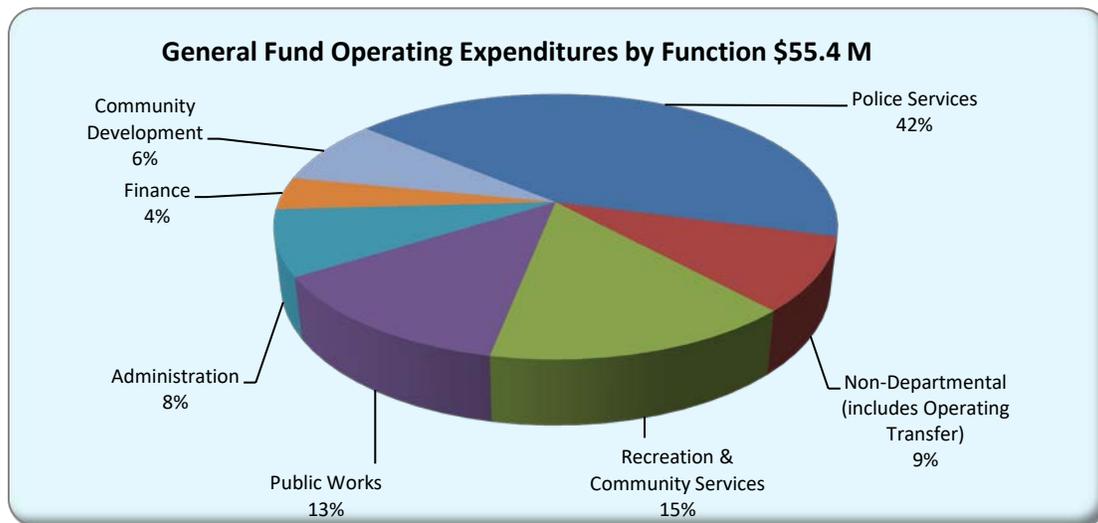
Debt Service Funds are incorporated within the budget due to various bond covenant requirements. The City refinanced most of its debt in FY 2017 to take advantage of lower interest rates. The resulting debt service was reduced through the remaining life of the new debt. Total funding sources for Debt Service funds for FY 2020 are \$0.8 million.

Three **Internal Service Funds** (Motor Vehicle, Information Technology and Workers' Compensation) are presented within the City's budget. Revenues in these funds are generated primarily through charge-backs to user departments depending upon the volume of assets and type of service provided by the specific fund. Costs that get recovered include staff time, repair, maintenance, claims payout and replacement of assets managed by the particular fund. Total revenues for Internal Service Funds for FY 2020 are \$3.6 million and are show flat growth from FY 2019 estimated actuals.

EXPENDITURES

As previously noted, the budget is composed of operating and capital expenditures totaling \$79.3 million. Operating expenditures alone total \$67.8 million.

The General Fund, which is the primary operating fund for the City, comprises approximately 82% of total City operating expenditures. Special Revenue funds comprise 11%, Internal Service funds comprise 5% and other funds make up the balance at 2% of the total. Operating expenditures in the General Fund are budgeted at \$55.1 million which is 3.6% higher than the prior estimated year-end actuals.



Employee Services: Personnel staffing represents a significant component of the City's annual operating budget. The combined number of budgeted permanent, permanent part-time, and limited-term FTE positions proposed in FY 2020 is approximately 173, a net increase of 2.6 FTEs from FY 2019. Changes to the budget from the prior year were minimal and include the following:

In the City Manager's Department, the conversion of the Administrative Analyst limited-term position (0.9 FTE) to a permanent Administrative Analyst (1.0 FTE) in the City Manager's

division, elimination of a limited-term position in the Information and Technology (IT) division, and the restructuring of IT positions results in the net reduction of one full time position. The budget also reflects the addition of a summer intern to be shared within the City Manager's Department. Additionally, the limited-term Communications and Public Engagement Coordinator position was previously funded 50% by the City Manager's program. This position was moved from the City Manager's program to the Public Safety program where its funding is allocated fully. Lastly, the City Manager's Department, in close coordination with the Public Works Department, will be taking one of the lead roles in advancing improvements at the Civic Center as defined by Measure O. A new position specifically for this purpose has been created. The new position, Senior Public Works Project Manager, will be dedicated to building consensus, assisting the City Council in defining the scope of the project and managing the project implementation. The position will be filled as a limited-term assignment with a term of four years. Employee and contractual costs relating to Measure O will be reimbursed to the City later by bond proceeds necessary to fund the Civic Center project. The issuance of the bond or multiple bonds, if necessary, up to \$50 million total was authorized by the successful passage of Measure O by Campbell voters in November 2018.

In the Recreation and Community Services Department, the conversion of a limited-term position to permanent is the only notable staffing change.

For the Finance Department, in the Accounting Services division a proposed restructuring of the accountant's responsibilities results in the proposal to eliminate the senior accountant position and add one additional accountant position to replace it.

The Community Development Department is also converting 5.0 FTE limited-term positions (Assistant/Associate Planner, Building Inspector, Economic Development Specialist, Planning Technician, and Senior Building Inspector) to 5.0 FTE permanent positions due to ongoing operational needs which are not expected to subside. Nevertheless, this results in no net FTE impact.

The Public Safety program requested the Communications and Public Engagement Coordinator position, which was approved in the FY 2018 budget as a two-year limited-term position and funded by both the Police Department (50%) and the City Manager's Office (50%), be converted to a permanent position that will be funded entirely by the Police Department. This position has proven to be extremely beneficial to both the Police Department and the City and the need for timely dissemination of information and social media engagement is continually growing. In the Field Services program, the Police Department is requested to convert 2 temporary Public Safety Assistant (PSA) positions to 2.0 FTE Community Services Officer (CSO) positions.

The Public Works Department has several noteworthy budget items. In the Public Works Administration Division indicates an increase in resources is needed to address issues related to both the West Valley Clean Water Program and the West Valley Solid Waste Management Program. Both programs will see increased regulatory constraints in the upcoming years and the participating cities will need to take on an increased role in meeting Clean Water requirements and implementing new organics regulations related to Solid Waste disposal. As such, Public Works is eliminating a 0.4 Executive Project Manager and replacing it with a 1.0 FTE Environmental Programs Coordinator. The Engineering Division is also converting 1.0 FTE Engineer Technician from limited-term to permanent and the continuing 1.0 FTE Assistant Civil Engineer limited-term position to meet current and projected workload demands related to current and proposed capital projects.

Salaries and Benefits: Salary and benefit summaries including charts can be found within the financial summaries section of this document, which can also be seen in the departmental budget summaries section, or on Exhibit B-1 of each program budget. These summaries reflect FTE's and budgeted expenditures for both permanent full-time, permanent part-time, and temporary staffing. Exhibit B in each program budget summarizes the various salary and benefit line-items contained within that program's budget.

The salaries and benefits category represent all personnel-related costs and makes up the largest component of City expenditures. In fact, personnel costs are approximately 56% of the total operating budget. This percentage is relatively low compared to many other cities because fire personnel are provided by contract with the County and, therefore, do not show up as City personnel costs. For FY 2020, salaries and benefits in the operating budget total \$37.7 million for all City funds, which is a \$3.0 million (8.9%) increase from FY 2019 estimated year-end actuals. The primary reasons for the growth were from modest employee wage and benefit increases including higher retirement contributions. Please note that in FY 2020, the City has also implemented a 2% salary/vacancy savings rate to account for natural attrition and vacancies occurring over the course of a fiscal year and to offset salaries budgeted at top step for all positions. This results in a salary and benefits appropriation reduction of approximately \$757,000 citywide at the 2% rate and is appropriate since not all positions will always be filled over the course of the fiscal year.

ECONOMIC AND FISCAL ISSUES FACING THE CITY

A top priority for the City is to maintain good fiscal health. By doing so, we preserve the City's ability to continue providing important programs and services for the community. Through past economic challenges, solutions were developed to address lost revenues while preserving vital services. The community played a critical role in helping the City to maintain desired services by supporting several revenue measures over the years. This was combined with expenditure reductions that reduced the City workforce and required shifting of priorities to maintain key services. These combined efforts provided a needed measure of stability to offset the decline in economic activity. Although revenues have improved considerably since then, cost containment efforts are still critical to ensure the future sustainability of important City programs and services, especially considering another potential economic downturn.

On a national level, Real Gross Domestic Product (GDP) in the United States grew at an annual rate of 3.1% in the first quarter of 2019, compared to 2.2% in the same quarter in 2018 and down from a four-year high of 4.2% in the second quarter of 2018. Corporate earnings during the first quarter of 2019, despite fears of a pending recession, have mostly been very favorable and have positively impacted the stock market (DJIA). The DJIA increased from 24,271 to 26,599 in the twelve months ending June 30, 2019, an increase of approximately 9.6%. However, the stock market has been marked by a very high level of volatility over the past year as the US intensifies trade disputes with China and other countries, investors react almost daily to the President's use of social media, and a high rate of automated high-volume trading persists. While US economic fundamentals remain largely intact, the Federal Reserve has become increasingly concerned about the downside risks to the economic outlook due to ongoing headwinds from slower global growth, persistently low global inflation rates, and trade disputes. At the same time, the housing market has continued to be largely healthy nationally and, especially, in the Bay Area, but there has been softening over the past year, with average home prices leveling off and month-to-month sales activity declining. Investment in residential

development expressed as a proportion of GDP also declined by 0.01% in 2018 and declined by an estimated 0.11% in the first quarter of 2019. A lowering of the discount rate by the Federal Reserve may bolster this sector over the next year, with further strength coming from continued low unemployment in the region, high housing demand, and a persistent scarcity of housing supply

The unemployment rate is an important economic statistic as to the state of the economy in general. It has shown that the State and local region continue to register historically low levels of unemployment which has helped boost the local economy. As of June 2019, the State seasonally adjusted unemployment rate was 4.2% compared to 4.2% the prior year. For Santa Clara County, the June unadjusted rate was 2.6%, a decrease from last year's rate of 2.8%. Campbell has historically trended better than both the County and the State in its unemployment rate. In fact, as of June 2019, Campbell's unemployment rate was just 2.3%, unadjusted, down from 2.6% in the prior year. While unemployment statistics represent only one measurement of the total economic landscape, they do provide a comparative indicator of how each area is doing relative to the prior year and over time.

Due to being "landlocked" on its borders, growth and new development within the City pose both opportunities as well as challenges. Campbell is essentially "built out", meaning that areas of undeveloped land in the City limits available for improvement are very limited. Therefore, "in-fill" projects, consisting of smaller individual parcels of land dispersed throughout the City or rebuilding of existing parcels whose current use may be enhanced by new development, is key to long-term success. The City's goal is to preserve the quality of life for Campbell residents and provide a variety of balanced land uses via established standards for residential, commercial and industrial development. Strategies include meeting with an economic development advisory committee and community business groups to obtain feedback on how best to approach various issues, maintaining a diversified and stable economic base, and marketing the community to targeted businesses. This year's budget maintains resources to continue the City's economic development efforts aimed at attracting new businesses and retaining existing ones.

With an increase in residential and commercial development activity, the City continues to address the overall impacts on the community of future development projects so that they remain manageable and environmentally balanced. While the current economic expansion has seen several large high-density development projects get approved, the City is committed to environmental sustainability and preservation, including the creation and enforcement of policies that are consistent with environmental standards. The City is a certified "Green" organization and continues to explore ways to promote this in the community. One example of this is the recent formation of the Silicon Valley Clean Energy Authority, a regional effort with numerous cities participating throughout Silicon Valley. The Authority allows participating residents in their community to receive their electric power from carbon free sources, primarily solar and wind generation, at competitive rates.

The City is also committed to providing reasonable health care coverage to both its active and retired employees. As the general population ages, more reliance is placed upon the health care system to provide comprehensive coverage for employees and their families. With the passage of the *Patient Protection and Affordable Care Act*, the City is also challenged with determining the impacts of providing affordable health care coverage to its full-time employees. The City, like all employers, has to consider how to balance the level of on-going benefits it can offer with the cost of providing them. The City began pre-funding its obligation to provide retiree health benefits 11 years ago and has budgeted \$0.6 million this year to continue its commitment to pre-funding

this obligation. In previous years, the City negotiated with several labor groups to eliminate a portion of these retiree obligations in exchange for other portable health spending accounts that provide more flexible arrangements for the employee while limiting the City's financial obligations after the employee retires.

Employer pension commitments are an additional challenge to the City's ongoing fiscal health. The recent reduction in the assumed discount rate used by the City's pension trustee, combined with changes in other assumptions used to calculate the City's contribution funding obligation, will result in additional rate increases beginning last year and continuing for at least six years. While pension reform efforts over past years help reduce costs in the long-run, in the short-term, there will be higher contributions for many employers. The City is planning to meet with labor groups to discuss solutions for addressing the increased costs.

Maintenance of the City's infrastructure, especially its streets, has been a challenge for many years. Approximately \$40 million dollars have been invested in the City's street infrastructure over the past two decades. While the overall condition of streets has been good for the past several years, a significant amount of resources is required to maintain a "good" condition rating on an on-going basis. Consistent funding for ongoing maintenance is a challenge as costs continue to increase from year to year. The City applies for various Federal and State grant funds annually to provide adequate funding. However, these are one-time funds that are not guaranteed each year. A vehicle impact fee was instituted several years ago to add a more stable source of funding. In FY 2017, the State approved legislation increasing the gasoline tax and allocating the proceeds for State and local road maintenance, thereby, providing another stable source of funds to help address these needs. In addition, the Santa Clara Valley Transportation Authority passed Measure B, a 30 year, half-cent Transactions and Use Tax devoted to transportation needs. Due to a lawsuit challenging the validity of the tax, local distribution of Measure B funds did not begin until January 2019. In FY 2018, the City began receiving annual allocations of funds for road maintenance from SB1, a State measure that was approved by voters. Combined, these two new funding sources are expected to improve the City's ability to properly maintain its network of roads. In FY 2020, the CIP five-year plan for street maintenance is \$13.6 million.

Lastly, keeping up with technology demands and replacement of aging infrastructure remains a constant issue. To maintain the City's current and proposed standards of performance, and to protect computer systems from ever increasing outside attacks, viruses and new vulnerabilities, additional resources are continually needed to ensure systems remain stable and reliable for all users and protected against data intrusion or loss. At the same time, improving efficiencies through use of new technologies, doing more for less cost, and reassessing how City services are delivered to the public are more important than ever.

LONG-TERM FINANCIAL PLANNING

The City incorporates long-term financial planning into its budget process in several ways. First, the City has established a set of financial policies to provide a basis for promoting and safeguarding the City's fiscal health by establishing requirements for budgeting revenues and expenditures, setting minimum or target levels for reserves, as well as guidelines for accounting, cash and debt management. Together, these policies ensure consistent management of the City's fiscal resources, establish criteria in which to evaluate the City's financial condition, create a sound financial basis for City operations, promote public confidence, and increase the City's credibility in the eyes of bond rating agencies and potential investors. These policies promote

budget stabilization by providing for various reserves that can buffer short-term economic downturns or emergencies. The policies are reviewed periodically and modified only when deemed necessary to maintain or improve the fiscal health of the City. The financial policies are detailed in Exhibit 2 of this budget message.

Second, the City strives to maintain five-year operating projections for revenues and expenditures that are revised during the year and shared with Council. These projections allow management to see what the longer-term future may look like given a set of assumptions and known information which then influence budget decisions of the current year. The current budget is evaluated in the context of whether decisions made now will be sustainable over the longer term given what may or may not occur down the road. Combined with the financial policies, the evaluation considers whether the City's fiscal health will continue over a 5-year period, not just a single year.

Lastly, the City also develops a five-year capital improvement plan (see CIP section of document) that serves as a strategic plan for meeting capital needs over a similar period of time. It incorporates information from the five-year operating projections into the model to know what internal funding sources may be available in each of the future years. This allows the City to plan and maintain flexibility in how and when capital projects will take place.

FY 2020 MAJOR WORK PLAN ITEMS

Departmental work plan items for the upcoming budget year were presented and discussed with the City Council at a study session on April 22 and approved on June 18, 2019. Major work plan items, in addition to a list of the on-going responsibilities of each department, can be found within the department program sections of the budget document.

FY 2019 SIGNIFICANT ACCOMPLISHMENTS

The City achieved a significant number of accomplishments during the past year. The key accomplishments, summarized by department, are shown in Exhibit 1 to this budget message.

STRATEGIC PLAN AND PERFORMANCE REPORTING

In addition to allocating necessary resources for the provision of ongoing services and work plan activities, the budget serves as the financial plan for accomplishment of the Strategic Plan vision and objectives, which are summarized within the City and Community Information section of the document.

At the beginning of each program budget section, the individual program mission statement and on-going and major work plan items are listed, and the total program budget is detailed by type of expenditure and by line item. Once the major work plan items have been identified, the departments proceed with development of budgetary resources necessary to accomplish the ongoing objectives and annual work plans. Many of the major work plan items are based on meeting Strategic Plan objectives and, therefore, are the link between the Strategic Plan and the annual budget.

Performance measures, which track and report work input and related outcomes, are located within each respective program budget section of the document and help the City Council, staff, and the community to assess trends and strive for continual improvement. Performance

reporting assists the City Council in establishing policies and priorities related to the quantity, quality and appropriateness of municipal services provided by the City of Campbell. Changes in resource levels can often also be articulated in terms of the impact on performance measures.

BASIS OF BUDGETING

The City budgets on a modified accrual basis for all funds except for its internal service funds which are budgeted on a full accrual basis. This is consistent with the City's basis of accounting as reported in its Comprehensive Annual Financial Report (CAFR). The City's *Governmental Funds* consist of the General Fund, special revenue funds, debt service funds, and capital project funds. To summarize, under this basis, revenues are estimated for the fiscal year if they are susceptible to accrual, e.g. amounts can be determined and will be collected within the current period. Principal and interest on general long-term debt are budgeted as expenditures when due, whereas other expenditures are budgeted for liabilities expected to be incurred during the current period or shortly thereafter to pay current liabilities.

Proprietary fund budgets are adopted using the full accrual basis of accounting whereby revenue projections are developed recognizing revenues expected to be earned in the period, and expenditure estimates are developed for all expenses anticipated to be incurred during the fiscal year. The City's proprietary fund type consists only of internal service funds, as the City has no municipally owned utilities or other enterprise activities.

Level of Budgetary Control: The City's budget is a working document that is utilized throughout the organization. Although the expenditure budget is legally adopted by resolution of the City Council at the total City budget level, it is important to note that the administrative level of accountability is at the line-item level within each program and fund. The City's financial policies authorize budget adjustments within the adopted budget up to \$10,000 or requiring transfers from reserves of less than \$5,000 to be approved by the City Manager. These are referred to as administrative budget adjustments. All budget adjustments that increase appropriations or any adjustments to capital projects must be approved by the City Council.

Budget Development: Development of the operating and capital budget is a process that takes place over six months and is summarized by the budget calendar located in the Budget Reference section of this document. The City's financial policies establish a process whereby a budget study session is held with the City Council during the annual budget development process. This meeting is generally held during March-May timeframe. Council is presented with an overview of the City's fiscal condition and proposed work plans for the upcoming year. A study session was held on May 7, 2019 to discuss the operating budget and capital improvement plan and the proposed budget was introduced on June 3 and adopted on June 18, 2019.

The City's budget presentation and format are intended to provide a document that is easy to read while functioning as a policy document, an operations guide, a communication tool, and a financial management instrument. It is a working tool that contains a considerable amount of information that is utilized at every level in the City organization throughout the year.

BUDGET AND FINANCIAL AWARDS

For the 26th consecutive year, the City's budget received national recognition by earning the Government Finance Officers Association (GFOA) "Distinguished Budget Award." To receive

the Distinguished Budget Presentation Award, a city must publish a budget document that serves as a policy document, a financial plan, a communications device, and an operations guide. We believe the FY 2020 budget conforms to GFOA program requirements. Additionally, this is the 21st year an award of “Excellence in Budgeting” has been received from the California Society of Municipal Finance Officers (CSMFO). Copies of both awards appear in the Budget Reference Materials section of this document. It also should be noted that the City’s Comprehensive Annual Financial Report has also been an award-winning document for excellence in financial reporting at both the State and national levels for many years.

CONCLUSION AND ACKNOWLEDGEMENTS

The development of the FY 2020 operating and capital budget was made possible through the knowledge and contribution of the City’s employees, input and support from our community, and direction of the City Council. The City has benefitted from a robust economy in recent years; however, an economic slowdown should be contemplated and planned for in advance. Consequently, the City will continue to be responsive to changes on the horizon, continue to prioritize what is important for the community and allocate available resources to those programs and services deemed to be most important while seeking more efficient processes for getting our work done. Our ability to manage scarce resources is a key reason Campbell remains a vibrant and desirable place to live and work.

I wish to thank everyone who participated in the budget process this year including the City Council and members of the Executive Team. Finally, I would like to recognize the Finance Department for their dedication and hard work that went into coordinating, developing, and publishing this budget document.

Respectfully submitted,



Brian Loventhal
City Manager