



**FY 2025 – FY 2034  
LONG RANGE  
FINANCIAL FORECAST**

City Council Item #12

**JANUARY 22, 2024**

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# OVERVIEW

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- Economy continues to demonstrate resiliency to formal recession
  - Forecast reflects stagnation offset by inflation
- LRFF consistent with FY 24 Adopted Budget, reflects near-term deficits
  - FY 2025 shortfalls resolved with Uncertainty Reserve
  - Consistent with FY 2024 Adopted Budget two-year strategy
  - Measure K (Business Tax) included for approved projects
  - Measure L (Equity Transfer) phased to 18% by FY 2027
- Expense projections based on current approved service levels
  - Assumes 20% BSR to mitigate uncertainty (typical target = 18.5%)
  - Cost of labor, inflation, and vacancies are key factors
- Estimated surplus in FY 2024 (\$3.4M) from Major Tax Revenue; to be reviewed at Mid-Year

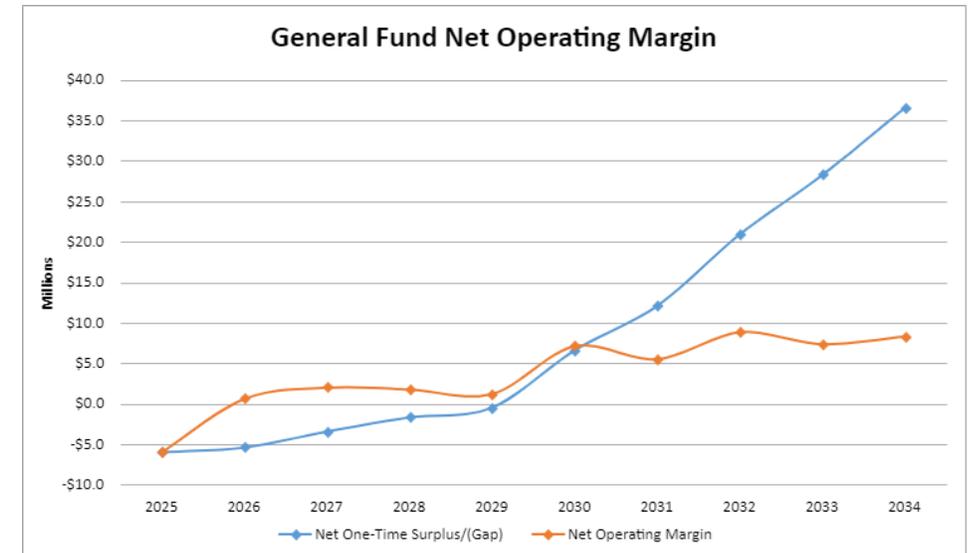
# FISCAL YEAR 2025 - 2034 BASE CASE FORECAST



	Actual 2023	Adopted 2024	Projected 2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
<b>Total Revenue</b>	\$254,799	\$261,141	\$264,281	275,889	\$289,060	\$301,025	\$312,564	\$325,208	\$339,684	\$353,085	\$365,820	\$379,944	\$394,026
<b>BSR Contribution (One-Time)</b>	-	\$3,440	\$3,440	-	-	-	-	-	-	-	-	-	-
<b>Reappropriated Funds (One-Time)</b>	-	\$15,000	\$15,000	-	-	-	-	-	-	-	-	-	-
<b>Total Source of Funds</b>	\$254,799	\$279,581	\$282,722	\$275,889	\$289,060	\$301,025	\$312,564	\$325,208	\$339,684	\$353,085	\$365,820	\$379,944	\$394,026
<i>Year over Year increase (revenue only)</i>				5.6%	4.8%	4.1%	3.8%	4.0%	4.5%	3.9%	3.6%	3.9%	3.7%
<b>Total Expenditures</b>	\$243,695	\$279,581	\$279,282	\$281,887	\$294,473	\$304,465	\$314,253	\$325,708	\$333,099	\$341,030	\$344,933	\$351,721	\$357,516
<b>Total Use of Funds</b>	\$243,695	\$279,581	\$279,282	\$281,887	\$294,473	\$304,465	\$314,253	\$325,708	\$333,099	\$341,030	\$344,933	\$351,721	\$357,516
<i>Year over Year increase</i>				0.8%	4.5%	3.4%	3.2%	3.6%	2.3%	2.4%	1.1%	2.0%	1.6%
<b>Net One-Time Surplus/(Gap)</b>	\$11,104	(\$0)	\$3,440	(\$5,998)	(\$5,414)	(\$3,440)	(\$1,689)	(\$500)	\$6,585	\$12,055	\$20,887	\$28,223	\$36,511
<b>Cumulative Net Operating Margin (One-Time)</b>													\$87,220
<b>Net Operating Margin</b>				(\$5,998)	\$585	\$1,974	\$1,751	\$1,189	\$7,085	\$5,470	\$8,832	\$7,336	\$8,288
<b>Forecasted One-Time Gap after Use of Uncertainty Reserve</b>				<b>(\$0)</b>									
<b>Cumulative Net Operating Margin</b>													\$36,511

Assumes that the annual shortfalls are solved with ongoing solutions and annual surpluses are spent for ongoing expenditures

- Revenues catch up to Expenses in FY 2030
- Mild economic stagnation through end of FY 2025
- Uncertainty Reserve offsets FY 2025 shortfall, consistent with 2-yr balancing strategy in prior year





## ASSUMPTIONS NOT INCLUDED IN FORECAST

- Labor Negotiations (contracts expire in Jan/June 2025); LRFF includes an estimated reserve for changes in vacancy rates, labor and benefit variability, and inflation
- Capital Improvements: Parks Master Plan, Railroad Grade Separation, Vehicle Fleet Electrification
- Cubberley Community Center Redevelopment
- Limited Term Programs:
  - Psychiatric Emergency Response Team (PERT)
  - PA Link
  - Downtown Streets Team
  - Project Homekey

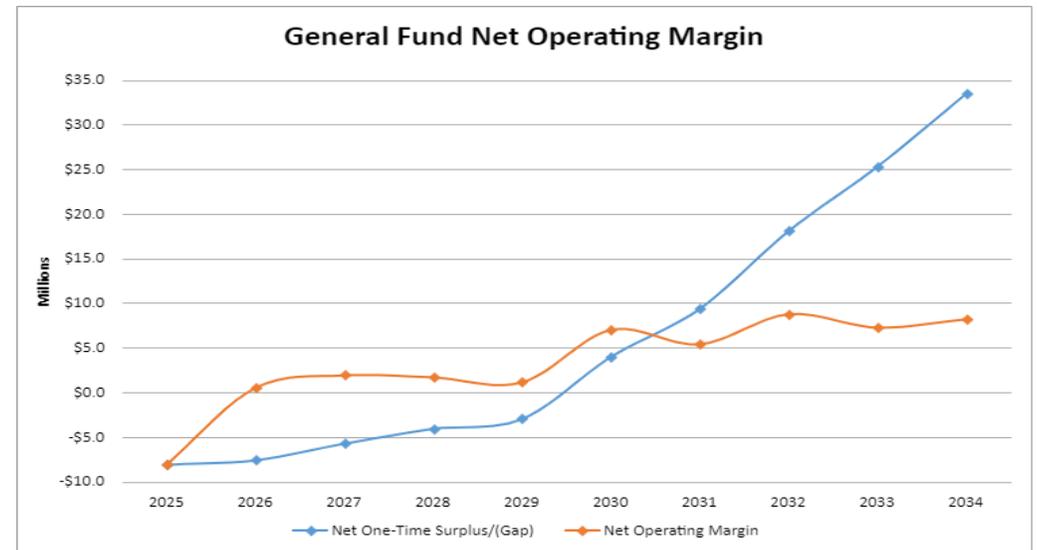
# ALT SCENARIO A: ECONOMICALLY SENSITIVE REVENUE IN FY25



	Actual 2023	Adopted 2024	Projected 2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
<b>Total Revenue</b>	\$254,799	\$261,141	\$264,281	273,760	286,825	298,692	310,138	322,682	337,041	350,335	362,971	376,979	390,943
<b>BSR Contribution (One-Time)</b>	-	\$3,440	\$3,440	-	-	-	-	-	-	-	-	-	-
<b>Reappropriated Funds (One-Time)</b>	-	\$15,000	\$15,000	-	-	-	-	-	-	-	-	-	-
<b>Total Source of Funds</b>	\$254,799	\$279,581	\$282,722	\$273,760	\$286,825	\$298,692	\$310,138	\$322,682	\$337,041	\$350,335	\$362,971	\$376,979	\$390,943
<i>Year over Year increase (revenue only)</i>				4.8%	4.8%	4.1%	3.8%	4.0%	4.4%	3.9%	3.6%	3.9%	3.7%
<b>Total Expenditures</b>	243,695	279,581	279,282	281,887	294,471	304,463	314,251	325,705	333,097	341,028	344,930	351,718	357,513
<b>Total Use of Funds</b>	\$243,695	\$279,581	\$279,282	\$281,887	\$294,471	\$304,463	\$314,251	\$325,705	\$333,097	\$341,028	\$344,930	\$351,718	\$357,513
<i>Year over Year increase</i>				0.8%	4.5%	3.4%	3.2%	3.6%	2.3%	2.4%	1.1%	2.0%	1.6%
<b>Net One-Time Surplus/(Gap)</b>	\$11,104	(\$0)	\$3,440	(8,128)	(\$7,646)	(\$5,771)	(\$4,112)	(\$3,023)	\$3,944	\$9,307	\$18,041	\$25,261	\$33,431
<b>Cumulative Net Operating Margin (One-Time)</b>													\$61,304
<b>Net Operating Margin</b>				(\$8,128)	\$481	\$1,876	\$1,658	\$1,089	\$6,968	\$5,363	\$8,733	\$7,221	\$8,169
<b>Cumulative Net Operating Margin</b>													\$33,431

Models the impact of a 1% loss in revenue from major taxes, charges for services, and permits and licenses

**Revenues decrease by \$2.1M in FY 2025 and increase projected shortfalls**

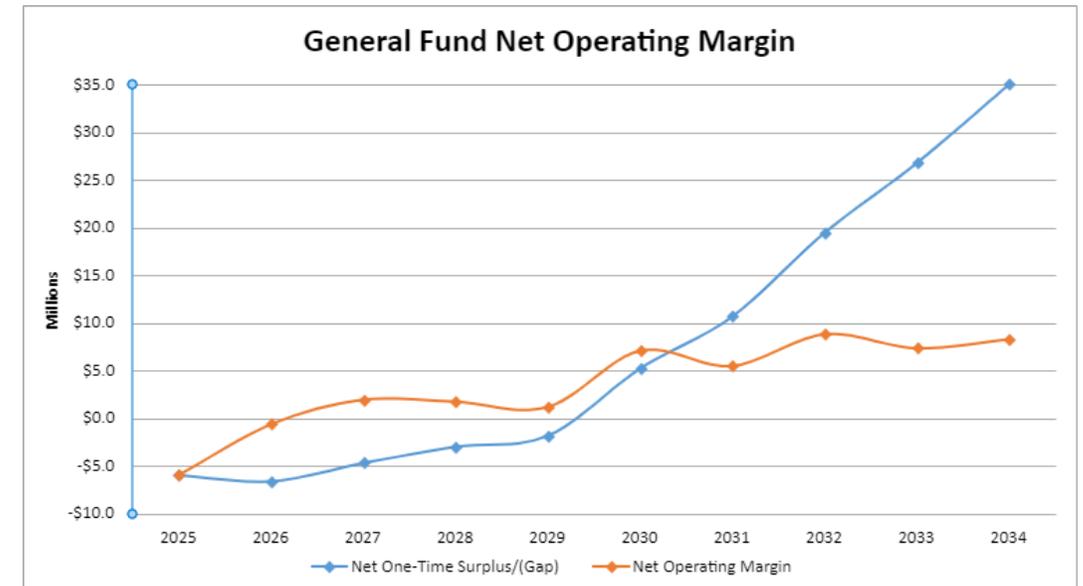


# ALT SCENARIO B: COMPENSATION ADJUSTMENT IN FY26

	Actual 2023	Adopted 2024	Projected 2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
<b>Total Revenue</b>	\$254,799	\$261,141	\$264,281	275,889	\$289,060	\$301,025	\$312,564	\$325,208	\$339,684	\$353,085	\$365,820	\$379,944	\$394,026
<b>BSR Contribution (One-Time)</b>	-	\$3,440	\$3,440	-	-	-	-	-	-	-	-	-	-
<b>Reappropriated Funds (One-Time)</b>	-	\$15,000	\$15,000	-	-	-	-	-	-	-	-	-	-
<b>Total Source of Funds</b>	\$254,799	\$279,581	\$282,722	\$275,889	\$289,060	\$301,025	\$312,564	\$325,208	\$339,684	\$353,085	\$365,820	\$379,944	\$394,026
<i>Year over Year increase (revenue only)</i>				5.6%	4.8%	4.1%	3.8%	4.0%	4.5%	3.9%	3.6%	3.9%	3.7%
<b>Total Expenditures</b>	243,695	279,581	279,282	281,887	295,719	305,761	315,587	327,082	334,501	342,460	346,392	353,208	359,033
<b>Total Use of Funds</b>	\$243,695	\$279,581	\$279,282	\$281,887	\$295,719	\$305,761	\$315,587	\$327,082	\$334,501	\$342,460	\$346,392	\$353,208	\$359,033
<i>Year over Year increase</i>				0.8%	4.9%	3.4%	3.2%	3.6%	2.3%	2.4%	1.1%	2.0%	1.6%
<b>Net One-Time Surplus/(Gap)</b>	\$11,104	(\$0)	\$3,440	(5,998)	(\$6,659)	(\$4,735)	(\$3,023)	(\$1,874)	\$5,183	\$10,625	\$19,429	\$26,736	\$34,993
<b>Cumulative Net Operating Margin (One-Time)</b>													\$74,676
<b>Net Operating Margin</b>				(\$5,998)	(\$661)	\$1,924	\$1,712	\$1,149	\$7,057	\$5,442	\$8,804	\$7,307	\$8,258
<b>Cumulative Net Operating Margin</b>													\$34,993

Models the impact of a 1% compensation adjustment once negotiated agreements sunset

**Expenses increase by \$1.2M in FY 2026 and increase projected shortfalls**



# FY 2025 BUDGET DEVELOPMENT GUIDELINES

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- Develop a structurally balanced budget to maintain fiscal sustainability
- Examine appropriate use of surpluses
- Review resource allocation for City Council's identified priorities
- Focus on business process redesign and explore alternative service delivery models
- Explore expansion of existing revenue sources or the addition of new revenue sources
- Continue to prioritize proactively funding long term liabilities

Council Referral: Consider pegging the Human Services Resource Allocation Process (HSRAP) budget allocations to a benchmark, such as percentage of General Fund budgeted expenditures.

## **Finance Committee recommends continuation of this item in February 2024**

- HSRAP funding averaged 0.26% of the General Fund budget from FY 2001 – FY 2024
- Total human services funding averaged 0.83%
- \$0.8M needed annually to increase total human services funding to 1% of the General Fund budget in FY 2025 – FY 2027 of the LRFF base case
- Human services funding never approved to be tied to the General Fund budget
- Prior to FY 2016 HSRAP included Avenidas & Palo Alto Community Childcare (PACCC), after FY 2016 these programs were funded through direct allocation separate from HSRAP

- Variability in LRFF Assumptions and Actual Results
  - Economic Advisory Report issued by Office of City Auditor (OCA) ([CMR 13915](#))
  - Actual results within 9% of original estimates
  - Long-term financial planning models and inputs align with the OCA’s considerations and best practices
  
- Historical Vacancy Analysis – General Fund
  - Up to \$1.7M savings in prior years, above budget assumptions for a 3% vacancy factor
  - Prior year actuals remained within 1.5% of budgeted levels
  - LRFF adjusts the vacancy factor to 5%, increasing potential savings by \$2M

	2019	2020*	2021*	2022	2023
<b>Total Savings/(Loss)</b> <i>actual salary and benefit costs vs. adjusted budget</i>	\$1.3M	\$1.3M	(\$1.7M)	\$1.6M	\$1.7M
<b>Annual Vacancy Rate</b>	12%	12%	15%	12%	13%
<b>Total Adjusted Budget</b> <i>net of vacancy factor</i>	\$123.3M	\$134.7M	\$124.1M	\$134.3M	\$148.4M
<b>Variance to Budget</b>	1.1%	1.0%	(1.4%)	1.2%	1.2%

\*FY20 and FY21 are anomaly years due to the pandemic

# INFO REQUESTED BY FINANCE COMMITTEE (ATTACHMENT C)

- Grants and Funding from Other Agencies

	2019	2020	2021	2022	2023
General Fund	\$0.8M	\$0.8M	\$1.1M	\$8.8M	\$12.1M
Capital Fund	\$12.4M	\$4.3M	\$12.6M	\$4.0M	\$17.0M

- The General Fund is supported by diverse external funding sources, with the most significant contributions coming from federal, state, and county funding, transportation initiatives, library partnerships, and emergency response.
- External revenues supporting capital improvement projects fall into three broad categories: local/regional grants (including Measure B), state grants, and federal grants, with local/regional grants comprising the largest source in three of the five years.

# CONCLUSION AND NEXT STEPS

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- Revenue trends indicate near term economic stagnation followed by return to growth
- 2025-2034 LRFF consistent with FY 2024 Adopted Budget two-year strategy
  - Focus on investing only in key areas of priority or urgent needs
  - Alternative scenarios increase projected shortfalls
  - Uncertainty Reserve and one-time surpluses are critical to manage the near-term fiscal stability and investments in priority initiatives
- FY 2024 Mid-Year will include recommendations for addition of key resources and appropriation of funds as directed by Council
  - Review of objectives deferred as outlined in FY 2024 Adopted Budget

## Next Steps Annual Budget Process

- *Feb 2024:* FY 2024 Mid-Year Budget
- *May 2024:* FY 2025 Proposed Budget
- *June 2024:* FY 2025 Budget Adoption

## RECOMMENDED ACTION

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The Finance Committee and Staff recommend that the City Council:

*Accept the Fiscal Year 2025 – 2034 Long Range Financial Forecast Base Case and the FY 2025 Budget Development Guidelines (Attachment B)*

*Direct staff to use this forecast as a starting point for the FY 2025 budget process*



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