



## City Council Staff Report

**From: City Manager**

**Report Type: ACTION ITEMS**

**Lead Department: Administrative Services**

**Meeting Date: June 17, 2024**

Report #:2406-3140

### **TITLE**

PUBLIC HEARING: Adoption of Budget Ordinance for Fiscal Year 2025, Including the Operating and Capital Budgets and Municipal Fee Schedule; Adoption of a Resolution determining the Appropriations Limit for Fiscal Year 2025; Acceptance of Updates to the Retiree Healthcare Actuarial Report; and Approval of Contributions for Retiree Healthcare Benefits

### **RECOMMENDATION**

The Finance Committee and Staff recommends that the City Council:

1. Adopt the Fiscal Year 2025 Budget Ordinance (Attachment A), which includes:
  - a. City Manager's Fiscal Year 2025 Proposed Operating and Capital Budgets, previously distributed at the May 6 City Council Meeting (Attachment A, Exhibit 1)
  - b. Amendments to the City Manager's Fiscal Year 2025 Proposed Operating Budget (Attachment A, Exhibit 2)
  - c. Amendments to the City Manager's Fiscal Year 2025 Proposed Capital Budget (Attachment A, Exhibit 3)
  - d. Fiscal Year 2025 City Table of Organization (Attachment A, Exhibit 4); and
  - e. Fiscal Year 2025 Municipal Fee Changes (Attachment A, Exhibit 5) including Impact and In-Lieu Fees (Exhibit 6)
2. Accept the Fiscal Year 2025 – 2029 Capital Improvement Plan
3. Adopt a Resolution determining the Appropriations Limit for Fiscal Year 2025 (Attachment B)
4. Accept the June 30, 2023 biennial actuarial valuation of Palo Alto's Retiree Healthcare Plan and approve funding of the Actuarial Determined Calculation (ADC) for Fiscal Year 2025 and Fiscal Year 2026 with a two-year phase-in of the adjusted assumptions using the staff recommended funding level of \$19.4 million and affirm the continued practice of transmitting amounts at a lower 5.75 percent discount rate as an additional discretionary payment to the City's California Employers' Retiree Benefit Trust (CERBT) Fund (Attachment D)

### **EXECUTIVE SUMMARY**

The FY 2025 Adopted Budget will be \$1.1 billion including the FY 2025 capital budget of \$441.8 million and \$1.7 billion over the 2025-2029 five-year Capital Improvement Plan (CIP). This is an

increase of approximately \$82.1 million over the proposed budget, mainly due to reappropriation of funding for continuing capital projects as well as funding added for Council Priorities as part of the budget review by the Finance Committee and Council. This budget recommends citywide staffing levels to increase by 29.00 full-time equivalent positions (FTE) from the FY 2024 adopted level for a total authorized staffing of 1,092.10 FTE in FY 2025. This is a net increase of 9.00 FTE from the proposed budget to address Council Priorities and associated administrative support.

This memorandum provides all necessary documents and transactions for the City Council adoption of the Fiscal Year (FY) 2025 Operating Budget, Capital Budget, and Municipal Fee schedule effective July 1, 2025, unless otherwise regulated. This action reflects two months of public dialogue by the Council and Finance Committee and provides a summary of all changes to the City Manager's FY 2025 Proposed Budget received by the Council on May 6, 2024. The necessary supporting documents for formal adoption by the City Council include the FY 2025 Budget Ordinance and the Table of Organization, and Resolution for Appropriations Limit for FY 2025.

On May 21<sup>st</sup> the Finance Committee "Committee" (CMR 2402-2664<sup>1</sup>) unanimously recommended the City Council adopt the FY 2025 budget inclusive of the Final Recommended Changes section of this memorandum. On June 4<sup>th</sup> the Finance Committee amended their recommendation to decrease the Real Property Investments Reserve by \$1.5 million to \$1.0 million in FY 2025 and ongoing; fund the Budget Stabilization Reserve at the 18.5% level of expenses in FY 2025; and increase the Uncertainty Reserve with remaining savings in FY 2025 for use in the FY 2026 Budget planning process.

All changes to the Proposed Budget recommended by the Finance Committee are detailed for the FY 2025 Operating Budget, by fund and by department, in Attachment A Exhibits 2 through 6.

Through the recommended budget actions, the community can expect continued high quality of services in Fiscal Year 2025, with a focus on building and strengthening services throughout the City. In addition, this budget invests in organizational resilience through continued workforce recruitment and retention efforts, furthers innovative service delivery and advances Council Priorities and related workplans.

The City continues to make infrastructure a priority through capital project investments in FY2025 and through the 2025-2029 Capital Improvement Plan (CIP). The FY 2025 budget includes projects to maintain current infrastructure such as streets, sidewalks, and facilities as well as enterprise funded capital needs such as electric, gas, and water distribution networks and

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<sup>1</sup> May 21, 2024, Finance Committee, *Discussion on the Fiscal Year (FY) 2025 Budget Wrap-Up and Recommended FY 2025 Budget including the FY 2025 Municipal Fee Schedule for City Council Adoption*;

<https://cityofpaloalto.primegov.com/api/compilemeetingattachmenthistory/historyattachment/?historyId=543c404f-2b05-4cbb-b9df-75ffb768545d>

substantial improvements at the Wastewater Quality Control Plant. The 2025-2029 CIP also includes projects to upgrade the City's infrastructure such as electric vehicle charging, electric grid modernization, and upgrading the fiber network to allow for Fiber to the Premises (FTTP).

To balance the budget for FY 2025, one-time funding from the Council appropriated Uncertainty Reserve, the Development Services Reserve, and the Budget Stabilization Reserve will be used to fund service priorities. A total of \$3.3 million in General Fund expenditures has been added to FY 2025 proposed funding levels to support a number of Council priority programs that are listed later in the report.

In addition, during the Budget Hearings, certain items did not require additional funding at the time of budget adoption but were recommended as part of staff's workplan for FY 2025. These items are listed later in the report and as a path forward staff will provide additional work throughout FY 2025, including the Ability Path request which will be considered during the FY 2025 Mid-Year Budget Review.

#### *FY 2025 Review Process: Segmentation of Certain Stanford-related Matters*

The California Political Reform Act (PRA) requires City officials to recuse themselves from matters where it is foreseeable that the City's decisions may have a material impact on a person or entity that is a "financial interest" to that official, and allows the City to segment multi-part items, such as the City's budget, so that the parts of the item that are the subject of the recusal are separated from the remaining parts of the item. This year, Council Member Veenker, who provides legal services to Stanford University on life sciences patent matters, will be recusing herself from certain Stanford-related elements of the budget. Those elements are listed in Attachment C. Council must consider and resolve the Attachment C items first. Once these items have been resolved, Council Member Veenker will rejoin and the Council will review and approve the remaining sections of the FY 2025 Operating and Capital Budgets and the Municipal Fee Schedule.

Also included in this staff report is the approval of the FY 2025 Appropriations (GANN) Limit that is required under Article XIII B to the California State Constitution, as amended by proposition 98 in 1988 and Proposition 111 in 1990 (Attachment B). The appropriations limit for Fiscal Year 2025 is \$219.74 million for funds subject to the appropriation limits. The City's Fiscal Year 2025 budgeted appropriations are estimated to be \$46.64 million under the limit (Attachment B, Exhibit 1).

Links to the meetings with the Finance Committee and the City Council, as well as the memoranda, presentations, and additional information provided for discussion can be found on the City's website under the FY 2025 Budget Process section.

#### **BACKGROUND**

Per the Municipal Code, the City Manager is charged with proposing a budget that provides a clear and complete financial plan for all City activities proposed for the coming budget cycle, or fiscal year. The FY 2025 Proposed Operating and Capital Budgets were released April 26, 2024 and transmitted to the City Council at their meeting on May 6, 2024. These documents represent

the planned expenditures and revenues for FY 2025 for the various fund types that constitute the City's Budget: General Fund, Capital Fund, Enterprise Funds, Internal Service Funds, Special Revenue Funds, and Debt Service Funds. The budget documents contain an overview section with descriptions of each of these fund types and detailed information of the revenues and expenses for each fund as well as for each individual department.

The FY 2025 Proposed Operating and Capital Budgets May 6, 2024 Council Study Session presentation provided an overview of the budget for review and discussion, including Citywide budget strategies, assumptions used in budget development, and a summary of service investments. As part of this discussion, the City Council provided guidance to the Finance Committee for their review of the budget documents during hearings on May 7, 8, 21, and June 4. The Finance Committee review of operating and capital budgets is structured around public hearings conducted prior to the City Council adoption to complete a detailed review of the budget documents and to incorporate opportunities for community input into the decision-making process. These meeting proceedings are organized by service area and include department presentations to highlight areas of emphasis for their respective department and fund(s). Department by department, the Finance Committee reviews individual budget sections for tentative approval of the budget, potential amendments, and requests for additional information to aid in their review. At the conclusion of these hearings (Budget Wrap-up), the Finance Committee is ultimately tasked to provide recommendations to amend the Proposed Operating and Capital Budgets and Municipal Fee Schedule for City Council consideration. These amendments, and additional information recommended for City Council review, are included in this adoption memorandum.

In addition to the regular schedule, staff held an additional study session on May 13 to check-in with the City Council for their feedback before the final budget wrap meetings on May 21 and June 4. In addition, a Community Information Session was held on May 15 to directly address questions from residents in the community.

The City Council adoption of the City Manager's FY 2025 Proposed Operating and Capital Budgets and FY 2025 Municipal Fee Schedule, including the amendments summarized in the Budget Wrap-up Memorandum on May 21, 2024 (CMR 2402-2664), will represent the ratification of the amendments that were approved by vote through the budget hearings. These amendments include all changes to the Municipal Fee Schedule and the Table of Organization. A comprehensive list of meeting materials issued during Finance Committee budget hearings is available on the City website<sup>2</sup>.

## **DISCUSSION**

The report is organized by the following sections:

- *Background and Discussion:* Summary of FY 2025 budget process and overall balancing strategies organized by fund type, including funding of Council Priorities and Objectives.

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<sup>2</sup> City's Budget Website: <https://www.cityofpaloalto.org/Departments/Administrative-Services/City-Budget>

- *FY 2025 Final Recommended Changes:* A summary of final direction given by the Finance Committee on May 21<sup>st</sup> and June 4<sup>th</sup> and additional recommended technical and staff adjustments organized by fund type.
- *Table of Organization:* A summary of additional changes to the Table of Organization because of adjustments made to the proposed budget that was released on May 6, 2024.
- *Municipal Fee Schedule:* A summary of the changes in the review and recommendations to Council for the FY 2025 Municipal Fee Schedule for incorporation in the FY 2025 Proposed Budget (CMR 2402-2587<sup>3</sup>).
- *FY 2025 Utility Rate Changes:* A brief overview of the rate changes reviewed by the Utilities Advisory Commission and Finance Committee and the final decision the City Council will make on June 17, 2024 (CMR 2404-2842); each of these rate changes are included in the FY 2025 budget assumptions.
- *Attachments:* Attached to this report are several documents as outlined and referenced throughout the recommendation language and the report. In addition, links to all the materials presented throughout the budget process to the City Council such as staff reports, At Places Memorandums, presentations made during the budget hearings, and transcripts from City Council Budget Hearings are included.

The FY 2025 Proposed Budget outlined a two-year budget balancing strategy, bringing financial planning through June 30, 2026 and recommends using one-time surpluses to bridge near-term shortfalls in FY 2025 and partially offset shortfalls in FY 2026 while investing in priority services, infrastructure, and saving for long-term liabilities. In addition, the strategy also recommends limiting ongoing costs to mitigate the potential for greater future deficits.

Overall, the enhancements reflected in this FY 2025 Budget will build and strengthen services throughout the City, support continued workforce recruitment and retention efforts, and advance City Council priority initiatives. While there are continued unknowns and uncertainties ahead, the FY 2025 Budget offers the Council, community, and staff reason for optimism that 2025 will continue progress to address community priorities and continue robust City services that the community expects through balanced financial strategies.

## **FY 2025 FINAL RECOMMENDED CHANGES**

This section reviews amendments to the FY 2025 Proposed Operating and Capital Budgets presented to the City Council on May 6, including final adjustments recommended by the Finance

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<sup>3</sup> May 8, 2024, Finance Committee, *FY 2025 Proposed Municipal Fee Schedule*;  
<https://cityofpaloalto.primegov.com/Portal/viewer?id=0&type=7&uid=bd4434c1-37fa-440d-8e01-71211721b2ed>

Committee and technical adjustments recommended by staff. A comprehensive list of these adjustments is included in Attachment A, Exhibit 2 for changes to the FY 2025 Operating Budget, and Attachment A, Exhibit 3 for changes to the FY 2025 Capital Budget. Changes to the Table of Organization are discussed later in this memorandum, and an updated Table of Organization is included in Attachment A, Exhibit 4.

Overall for operating and capital budgets, this reflects an \$84.5 million, or 8.2%, increase compared to the FY 2025 Proposed Budget. This includes an increase from the FY 2025 Proposed Budget of 9.00 FTE full-time staff (8.00 FTE in the General Fund and 1.00 FTE in Enterprise Funds) and a reduction of 0.96 FTE part-time staff (-1.92 FTE in the General Fund and +0.96 in the Enterprise Fund), resulting in an overall workforce of 1,092.10 full-time positions (602.57 FTE in the General Fund).

### **OPERATING BUDGET – General Fund**

Overall, the City's General Fund is recommended to have \$287.6 million in revenues and \$306.9 million in expenses. To balance the budget for FY 2025, one-time funding from the Council appropriated Uncertainty Reserve, the Development Services Reserve, and the Budget Stabilization Reserve will be used to fund service priorities. A total of \$3.3 million in expenditures has been added to FY 2025 proposed funding levels to support a number of Council priority programs that are listed below in Table 1.

#### *Uncertainty Reserve*

As part of the FY 2025 Proposed Budget, Staff recommended using \$6.9 million of the \$9.6 million Uncertainty Reserve to balance FY 2025, leaving \$4.7 million in the Uncertainty Reserve, including using \$2.0 million from the Budget Stabilization Reserve (BSR) to increase the Uncertainty Reserve for anticipated needs in FY 2026. As a result of actions taken by the Finance Committee, there are additional savings of \$1.5 million (including \$0.6 million from the BSR) that will be added back into the Uncertainty Reserve and bring it up to \$6.2 million. In total, \$2.6 million from the BSR will be used to set aside funding in the Uncertainty Reserve. The Uncertainty Reserve of \$6.2 million is recommended to fund the FY 2026 projected gross deficit of approximately \$11.0 million, leaving a projected net deficit of \$4.8 million.

#### *Budget Stabilization Reserve*

The FY 2025 Proposed Budget recommended using \$2.0 million from the BSR to provide additional funding in the Uncertainty Reserve, leaving the BSR at \$55.0 million or 18.8% of General Fund Expenditures for FY 2025. As part of the budget actions recommended for adoption by the Finance Committee, the BSR will be reduced by \$0.6 million to \$54.4 million or the 18.5% target level of the Council's recommended range of 15-20% of General Fund Expenditures. The BSR calculation excludes reserves such as the Uncertainty Reserve and the Utility Transfer Legal Cost Reserve to avoid unintentional inflation of BSR needs.

### Finance Committee Recommended Adjustments

Throughout budget hearings in May, the Finance Committee engaged in several meetings to review proposed budget documents and recommend tentative adjustments. Table 1 provides an overview of these adjustments at various touchpoints in the budget process.

**TABLE 1: FY 2025 General Fund Recommended Adjustments**

<b>Dept</b>	<b>FY 2025 General Fund Recommended Adjustments Description</b>	<b>FY 2025 Revenue or Savings/ (Cost)</b>	<b>Ongoing Revenue or Savings/ (Cost)</b>
<b>NON</b>	<b>Beginning Balance – City Council Priorities Reserve</b>	<b>\$-</b>	<b>\$-</b>
<b>NON</b>	Increase Gas Transfer to General Fund in FY25 to 14.5% (from 11.9%) & in FY26 to 18% (previously scheduled in FY27)	1,958,000	916,000
<b>NON</b>	Increase JMZ ticket prices from \$10 to \$14, during peak periods	350,000	350,000
<b>NON</b>	Use BSR to balance FY 2025 – Reduce BSR to 18.5%	605,000	-
<b>OOT</b>	Review an alternative service approach for PA Link with reduced net costs (proposed FY2025 budget funds \$0.9M)	223,000	60,000
<b>CSD</b>	Account for Los Altos & Los Altos Hills contribution for animal control services Report #2403-2827	198,000	198,000
<b>FIR</b>	Upstaff Fire Engine 62 with 3 Sworn Staff instead of Overtime	14,000	23,000
	<b>Subtotal Sources (Revenue)</b>	<b>\$3,347,000</b>	<b>\$1,547,000</b>
<b>NON</b>	Other Post Employment Benefit (OPEB) 2-Year Phase-In	(1,650,000)	(3,300,000)
<b>NON</b>	Increase Uncertainty Reserve to \$6.2M for Future Needs	(1,470,000)	-
<b>CSD</b>	JMZ additional staffing, new ticketing system and promotion	(509,000)	(702,000)
<b>CIP</b>	California Avenue Interim Improvements	(450,000)	-
<b>CIP</b>	Additional funding for Roth Building Rehabilitation (PF-23001) (revise terms and conditions of the tenant work letter)  \$1M total including \$0.2M interest earnings previously appropriated	(300,000)	(500,000)
<b>NON</b>	Establish Citywide Special Events & Programming (\$265k total program) [Requested UNAFF \$45k, 3 <sup>rd</sup> Thursdays \$40k, Neighbors Abroad \$30k (already in FY25 Proposed Budget), Magical Bridge \$150k, Environmental Volunteers Foothills Nature Preserve Program \$11k one-time]	(246,000)	(235,000)

<b>Dept</b>	<b>FY 2025 General Fund Recommended Adjustments Description</b>	<b>FY 2025 Revenue or Savings/ (Cost)</b>	<b>Ongoing Revenue or Savings/ (Cost)</b>
<b>NON</b>	Palo Alto Transportation Management Association (PATMA) increase to \$400,000 Citywide	(175,000)	(175,000)
<b>PWD</b>	Public Services Streets 311 Requests to support catch-up and keep-up	(100,000)	(107,000)
<b>FIR</b>	Upstaff Fire Engine 62 with 3 Sworn Staff instead of Overtime	(74,000)	(120,000)
<b>NON</b>	Car-free Streetscape Design for Ramona Street	(50,000)	-
<b>CSD</b>	Administrative Support for new Citywide Special Events & Programming (1 FTE)	-	(125,000)
<b>CIP</b>	Study of artificial turf replacement with grass at up to 4 fields (recommend use of current CIP to fund a study)	-	-
<b>OOT</b>	Review an alternative service approach for PA Link with reduced net costs (proposed FY2025 budget funds \$0.9M)	177,000	340,000
<b>NON</b>	Reduce Real Property Investment Reserve to \$1.0M Annually	1,500,000	1,500,000
	<b><i>Subtotal Uses (Expense)</i></b>	<b>(\$3,347,000)</b>	<b>(\$3,424,000)</b>
	<b>Potential Fund Remaining (Deficit)/Surplus</b>	<b>\$-</b>	<b>(\$1,877,000)</b>



## **OPERATING BUDGET – Enterprise Funds**

### **Electric Fund – Associate Sustainability Program Administrator**

This action adds 1.0 FTE Associate Sustainability Program Administrator to the Utilities Resource Management Division. Responsibilities of this position include tracking sales and marketing results, engaging in direct customer calls related to both sales and customer experience, and assisting with customer experience improvement for various programs, starting with the heat pump water heater program. This fulfills the Council's Climate Action priority by supporting programs to drive gas appliance conversion to electricity and electric vehicle adoption, both of which reduce emissions supporting the City's green electricity portfolio.

### **Gas Fund – Equity Transfer to General Fund and Rate Adjustments**

Consistent with Council direction, this action increases the Gas Fund equity transfer to the General Fund from 11.9% to 14.5%, an increase of \$2.0 million. This is accompanied by an increase to retail revenues by \$2.0 million, supported by an increase to the gas rate in FY 2025 from 9.0% in the proposed budget to 12.5%.

### **Water Fund – Water System Operations Staffing and Rate Adjustments**

Staff recommends removing the Water System Operations Staffing Proposal from the FY 2025 Proposed Budget to allow time for discussions with the Service Employee International Union (SEIU). The proposal sought to reclassify four Water System Operator II's and two Senior Water System Operators into four Utilities Install/Repairers and two Utility Install/Repairer Leads, respectively.

Staff also recommends a technical adjustment to retail revenues based on the FY 2025 Water Fund Financial Plan, which decreases overall target revenue to \$52.8 million. This target incorporates the SFPUC proposed rate of \$5.55 per CCF, which has since increased to \$5.67 per CCF. Due to this increase, staff originally proposed an increase of 10% to rates; however, the Finance Committee recommended a 9.5% increase instead with the remaining 0.5% rate to be offset by operations reserves.

## **OPERATING BUDGET – Other Funds**

### **Gas Tax Fund – Gas Tax Revenue Adjustment**

This action is a technical update to increase Gas Tax revenue estimates for Palo Alto based on the California Department of Finance's May 2024 updates for estimated Highway Users Tax Account (HUTA) and Road Maintenance and Rehabilitation Account (RMRA) taxes for FY 2025. This also increases the transfer to the Streets Maintenance capital project (PE-86070), which is discussed below in the Capital Budget section of this report.

### **General Benefits Fund – Healthcare and Pension Pass-through Expenses**

The General Benefits Fund acts as a pass-through to pay the City's pension and healthcare costs. These costs are allocated in the various funds across the City where staff are budgeted with the corresponding revenue budgeted in the General Benefits Fund. As staff were added to the budget as part of the FY 2025 Proposed Budget and actions recommended by Finance Committee, the costs were allocated to the funds across the City, but the corresponding revenue in the General Benefits Fund was not included. This net neutral technical action is usually done as part of the adoption memo in the General Benefits Fund and will increase the estimate for charges to other funds by \$1.6 million and increase expenses for pension and healthcare costs by \$1.6 million to keep the fund in alignment with staffing levels.

#### *Parks Development Impact Fee Fund – Transfer Adjustment*

A \$1,851 reduction in the transfer to the Capital Improvement Fund is recommended to align with recommended adjustments to capital project reappropriations from FY 2024 to FY 2025.

#### *Retiree Healthcare Fund – Other Post-Employment Benefits (OPEB) Actuarial Valuation*

On June 4, 2024, the Finance Committee unanimously recommended approval of the June 30, 2023 actuarial valuation of Palo Alto's Retiree Healthcare Plan (CMR 2402-2673) included in Attachment D. This report is completed biannually to provide an actuarial valuation detailing the latest status of the City of Palo Alto's Retiree Healthcare plans for employees and retirees. The analysis is used to determine the City's retiree healthcare liability and the annual Actuarial Determined Contribution (ADC) to the trust. In addition, the report details funding status, results of assumptions such as discount rate (DR), healthcare plan premiums, and projected future healthcare costs. During the June 4, 2024 meeting, the Finance Committee recommended a two-year phase-in of the financial impacts of the June 30, 2023 valuation. The Finance Committee also affirmed the continued practice of transmitting amounts at a lower 5.75 percent discount rate as an additional discretionary payment to the City's California Employers' Retiree Benefit Trust (CERBT) Fund. This recommendation supports financial flexibility for the provision of services citywide while continuing to proactively prefund long-term obligations in alignment with the City Council's Retiree Benefits Funding Policy. This action results in an FY 2025 Adjusted ADC of \$19.4 million citywide (approximately \$12.2 million in the General Fund), a \$2.6 million (\$1.7 million in the General Fund) increase from the \$16.8 million ADC from the June 30, 2021 valuation used to develop the FY 2025 Proposed Operating Budget. A detailed list of impacts by department and fund can be found in Attachment D, Exhibit 1.

#### *University Avenue Fund – Palo Alto Transportation Management Authority (PATMA)*

Finance Committee recommends \$200,000 in additional funding for the Palo Alto Transportation Management Association (PATMA), increasing the total funding allocation from \$200,000 to \$400,000, with \$25,000 funded by the University Avenue Parking Fund and \$175,000 supported by the General Fund, to maintain current service levels. This brings the funding level to \$200,000 from each fund. Previously, PATMA spent down reserves to maintain service levels and has exhausted those funds. Additional information can be found in the PATMA annual report (Report #2403-2761<sup>4</sup>).

## CAPITAL BUDGET

The City's Capital Improvement Plan reflects a \$441.8 million FY 2025 budget, and a \$1.7 billion plan over the five-year CIP (FY 2025-FY 2029). Of this, the Capital Improvement Fund FY 2025 budget reflects expected expense of \$124.7 million and \$845.8 million over the five-year CIP.

### Capital Reappropriations

The Municipal Code requires City Council authorization to reappropriate funds for capital projects from one fiscal year to the next. The FY 2025 budget process continues this procedure, and the FY 2025 Proposed Capital Budget included approximately \$147.1 million in reappropriated funds for project expenditures across all funds. In the time since the FY 2025 Proposed Budget figures, Staff refined the FY 2024 estimated project activity levels and provided further updates to increase the reappropriations by \$81.6 million, to \$228.7 million across all funds. The additional reappropriation adjustments are summarized in Attachment A, Exhibit 3.

### Other Capital Project Adjustments

In addition to the reappropriations from FY 2024 to FY 2025, several capital projects need to be adjusted based on updated information that became available after the release of the FY 2025 Proposed Capital Budget or as a result of actions recommended in this memorandum. These adjustments are discussed below and summarized in Attachment A, Exhibit 2.

### Capital Improvement Fund

- **Baylands Boardwalk Piling Repair (PE-24000)** – The FY 2025 Proposed Budget includes \$660,615. An additional \$203,000 is needed in FY 2025 because bids received in early May were higher than the engineer's estimate. A contract for repairs will be going to City Council on June 18, 2024, and if it is not awarded at the start of FY 2025, the Baylands Boardwalk will need to be closed.
- **California Avenue Streetscape Update (PL-23000)** – The California Avenue interim improvements are within the 2024 City Council Priority objectives. Description and funding are specified as part of Supplemental Report #2405-2969<sup>5</sup>. Finance Committee recommends a \$450,000 transfer from the General Fund to the Capital fund to support street paving adjustments, signage, planters, and site furniture.
- **Roth Building Rehabilitation (PF-23001)** – The Palo Alto Museum (PAM) requested reimbursement of \$1 million for inflationary cost increases. Because \$0.2 million of

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<sup>4</sup> April 24, 2024; Finance Committee; *Receive and Discuss the Palo Alto Transportation Management Association (PATMA) 2023 Annual Report, Strategic Plan, and Commute Survey*; <https://portal.laserfiche.com/Portal/DocView.aspx?id=71653&repo=r-704298fc&searchid=da277587-f6b6-4b90-aba4-da79874ca271>

<sup>5</sup> May 7, 2024; Finance Committee; *Supplemental Report: Additional Funding Proposal Options for FY 2025 Budget Process Consideration*; <https://portal.laserfiche.com/Portal/DocView.aspx?id=72129&repo=r-704298fc&searchid=f607c99c-a0b7-4c6e-9217-eeaeb21ee1d7>

interest earnings from Transfer Development Rights funding and other funding to support the project had already been allocated to the project in FY 2024 as part of the Mid-Year Review (Report #2311-2233<sup>6</sup>), Finance Committee recommends increased funding of \$0.8 million: \$0.3 million in FY 2025, funded by a transfer from the General Fund to the Capital Improvement Fund; and \$0.5 million in FY 2026.

- **Street Maintenance (PE-86070)** – The budget is recommended to be increased by \$79,378 annually to align with the California Department of Finance’s May 2024 estimates for FY 2024-25 Gas Tax revenue.

#### Gas Fund

- **Gas System, Customer Connections (GS-80017)** – The FY 2025 Proposed Budget included a technical error which added \$147,200 to the project. The recommended correction would reduce the cost of the project from \$847,200 to the appropriate amount of \$700,000.
- **Gas Main Replacements #25 (GS-15000)** – To mitigate further rate increases related to the increased Gas Fund equity transfer from 11.9% to 14.5%, and to maintain a sufficient reserve balance, staff recommends reducing the FY2025 budget for this project by \$0.7 million. There is an upcoming grant that will restore this capital project funding.

#### **TABLE OF ORGANIZATION**

During budget hearings and in subsequent City Council meetings, the Finance Committee and City Council recommended staffing adjustments of 9.00 FTE (net). A more detailed description of these actions is included in Attachment A, Exhibit 2, and an updated Table of Organization is included in Attachment A, Exhibit 4:

- Add 3.00 Fire Fighter EMTs to the Fire Department
- Add 1.00 Program Assistant I to the Community Services Department
- Add 4.00 Animal Caretakers to the Community Services Department
- Add 1.00 Associate Sustainability Program Administrator to the Utilities Department
- Add 4.00 Water System Operator II to the Utilities Department
- Add 2.00 Senior Water Systems Operator to the Utilities Department
- Delete 4.00 Utilities Install/Repair from the Utilities Department
- Delete 2.00 Utilities Install/Repair-Leads from the Utilities Department

#### **MUNICIPAL FEE SCHEDULE**

On May 8, 2024, the Finance Committee reviewed the FY 2025 Proposed Municipal Fee Schedule

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<sup>6</sup> February 12, 2024; City Council Item #11:

<https://cityofpaloalto.primegov.com/Portal/Meeting?meetingTemplateId=13351>

and recommended approval as outlined in CMR 2402-2587<sup>7</sup> and further amended on May 21, 2024 (CMR 2402-2664). Attachment A, Exhibit 5 provides a summary of all recommended changes as reviewed by the City Council on May 8, 2024. Additionally, Exhibit 6 provides a summary of changes to Impact and In-Lieu Fees.

#### *Affordable Housing Fee Waiver*

As part of this amendment, a new fee was introduced to waive City staff costs associated with processing one hundred percent (100%) affordable housing planning applications under the Housing Element Program Implementation 3.1 for Fee Waivers and Adjustments. The objective of the fee waiver is to support the production of affordable housing in Palo Alto. Approval of this fee is expected to reduce planning application costs by approximately \$5,000 to \$20,000 per affordable housing project that is processed for a planning entitlement. Due to the low volume of one hundred percent affordable housing applications, staff anticipates minimal revenue impact in FY 2025.

### **FISCAL YEAR 2025 RATE CHANGES**

An overview of the rate changes was reviewed and approved by the Utilities Advisory Commission (UAC) and Finance Committee in April 2024. These rate changes are included in the FY 2025 budget assumptions. This section references those changes for informational purposes only; a separate report recommending final rate changes will be considered by the City Council on June 17, 2024 (CMR 2404-2842).

- 9.0% rate change for Electric (recommended by UAC and Finance Committee);
- 2.6% CPI increase for Fiber (recommended by UAC and Finance Committee);
- 12.5% rate increase for Gas (recommended by UAC at 9% and Finance Committee at 12.5%);
- 0.0% rate change for Refuse;
- 2.6% CPI increase for Stormwater (recommended by UAC and Finance Committee);
- 15.0% rate change for Wastewater (recommended by UAC and Finance Committee); and
- 9.5% rate change for Water (recommended by UAC at 10% and Finance Committee at 9.5%)

The proposed rate changes will allow Palo Alto to invest in utility infrastructure, gradually increase reserves to guideline levels, and to support community goals. As utility infrastructure ages, investment is needed to maintain the reliability of the electric, gas, stormwater, wastewater, and water utilities. These rate increases will support the maintenance and replacement of infrastructure including rebuilding Palo Alto's wastewater treatment plant (Regional Water Quality Control Plant). Investment in modernizing the electric grid will allow the City to achieve the Council's Sustainability and Climate Action goals.

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<sup>7</sup> 5/8/2024, Finance Committee, FY 2025 Municipal Fee Schedule Amendments;  
<https://cityofpaloalto.primegov.com/Portal/viewer?id=2114&type=0>

The Finance Committee tentatively approved the rate changes listed above including the following modifications from the Proposed Budget: the 12.5% increase for Gas resulted from changing the Gas Equity Transfer to the General Fund from 11.9% to 14.5% of FY 2023 gross revenue; and lowering the distribution rate increase to maintain an overall expected bill impact of 9.5% percent increase for Water through the use of additional rate stabilization reserve funds in FY 2025. In addition, the Finance Committee tentatively approved the 9.0% increase for the median residential electric customer which is a result of a cost of service analysis (COSA) for the City's electric rates to ensure that electric rates continue to represent the Utility's cost to serve customers; the 15.0% increase for Wastewater Collection due to increasing Capital costs in Wastewater Collection and at the Regional Water Quality Control Plant; the 2.6% CPI increase for Fiber customers on the EDF-1 rate in accordance with the original dark fiber leasing agreement; and 2.6% CPI increase for Stormwater, consistent with the 2017 Storm Water Management Fee ballot measure, to keep fund revenues consistent with inflationary cost increases and to provide sufficient funds for planned Stormwater Management capital and operating expenditures.

## STAFF WORKPLAN

During the Budget Hearings, certain items did not require additional funding at the time of budget adoption but were recommended as part of staff's workplan for FY 2025. The list below is reflective of the items from the Budget Hearings that staff will provide additional work throughout FY 2025.

- *Ability Path (Request \$250,000)*

The Committee on June 4<sup>th</sup> requested that the Ability Path request be considered during the FY 2025 Mid-Year budget Review.

- *Analyze Fire Emergency Medical Response Fee Adjustments (Ongoing Revenue TBD)*

The Committee requested an analysis of Fire Emergency Medical Response Fees to offset the costs of City medical response costs. In FY 2025, the Citywide Cost Allocation Plan and Municipal Fee Study will be fully reviewed, including further analysis of Fire EMS response fees for appropriate alignment to cost recovery levels. Such draft fees will be presented to the Committee and Council for review and approval and take effect in July 2025.

- *Fire Emergency Medical Response; Supplemental Resources (Estimated costs: \$1,000,000 - \$4,000,000 Ongoing)*

The Committee requested staff analyze different EMS models and associated fiscal impacts that would improve the City's capacity to cover ambulance call volume during peak hours. During the budget hearings, the Committee reviewed this contract option, and recommended the consideration of two different model options to establish a supplemental ambulance unit. One model is an activation through staffing, which can be accomplished through either traditional sworn staffing (i.e. Firefighters) or civilian staffing (i.e. Single Role). This staffing approach would require labor discussions, includes staffing engines at Fire Stations 2 and 4, and with a multi-year phased-in implementation ultimately costing approximately \$3.2 million to \$4.0 million annually. The second model is an activation through third-party contract services, which would require a robust

procurement solicitation (i.e. RFP process), with an informal quotation of \$1.0 million annually. This is an essential service that needs to be implemented correctly, and accordingly, staff proposes to analyze this during FY 2025 and provide the Committee and Council with an in-depth analysis of the two models, fiscal impacts, and feasibility and implementation. Budgetary appropriation would follow such analysis and Council authorization.

- *Review Parks Restroom Prioritization (Specifically Pardee Park (Ongoing capital project costs TBD)*

The Committee requested staff to review parks restroom prioritization with a focus on Pardee Park. Several considerations influence the prioritization of park restroom projects. The Parks, Trails, Natural Open Space and Recreation Master Plan (2017) states, “The City will actively pursue adding park restrooms in parks that are approximately 2 acres or larger, have amenities that encourage visitors to stay in the park, have a high level of use and have no nearby restrooms.” Using those criteria, the following *potential* locations were included in the Master Plan: Bol Park, Bowden Park, Eleanor Pardee Park, Johnson Park, Ramos Park, Robles Park, and Terman Park. These are further prioritized by the level of community support, existing amenities in the park that may draw large crowds, timing with other projects in the same park, and other factors such as access to utilities. Additionally, restrooms in other parks may be prioritized above those identified in the Master Plan if a need arises due to an increase in park visitation from adding new amenities such as playgrounds or pickleball courts. The 2025-2029 Capital Improvement Plan includes funding in the Park Restroom Installation project (PG-19000) for the installation of restrooms in City parks every other year. A restroom at Mitchell Park is scheduled for installation in FY 2024, while specific parks have not yet been identified for restroom installations in FY 2026 and FY 2028. Staff recommends adding Eleanor Pardee Park to the workplan in FY 2026 and evaluating the workplan for FY 2028 in line with the Foothills Nature Preserve Restroom Replacement project (PE-26000) to align with staff workload capacity to install park restrooms. CSD staff can do some initial outreach starting in Fall 2024 for Eleanor Pardee Park given the previous opposition to restrooms at that location in 2007 and 2013, with the goal of funding it in the FY 2026 Capital budget.

- *Active Recruitment Digital Marketing Services (Contract Services)*

On May 7, 2024, the Committee directed staff to analyze a pilot recruitment digital marketing services for talent attraction to support organizational resilience. While the original estimate is \$250,000, later reduced to \$50,000 placeholder, staff at this time proposes this as an FY 2025 work plan item to analyze a pilot program in collaboration with city departments and contract vendor(s). No budget appropriation is requested at this time, but should a need arise, staff will update Council at FY 2025 mid-year.

- *Establish Organizational Development & Safety Division (\$135,000 Ongoing; 50% GF/50% ISF)*

On May 7, 2024, the Committee added 1.0 FTE focused on organizational development and safety division with Human Resources. Staff proposes this to be a FY 2025 work plan item to allow time to analyze and align with the risk function transition currently underway between Human Resources and Administrative Services. Funding for this position would be split equally between the General Fund and the General Liability Fund, but no appropriation is requested for FY 2025.

- *Explore financial, outreach, and policy processes for adding East Palo Alto to resident rates for the golf course (Ongoing revenue reduction TBD)*

The Committee directed staff to explore providing the discounted residents rates for Palo Alto golf to East Palo Alto (EPA) residents. Staff proposes this to be a FY 2025 work plan and estimates any fiscal impact, if significant, may be incorporated into the FY 2025 mid-year budget update.

- *Increasing Revenue-Generating CSD Programming to Meet Demand (Ongoing cost & revenue TBD)*

The Committee directed staff to analyze flexibility in increasing CSD classes to meet demand. This will likely entail a review of class demand, procurement, and facility capacity. Staff proposes this to be a FY 2025 work plan, and no budget adjustment is requested at this time.

## **APPROPRIATIONS LIMIT FOR FISCAL YEAR 2025**

California voters approved an initiative on November 6, 1979 that added Article XIII B to the State Constitution, as amended by Proposition 98 in 1988 and Proposition 111 in 1990. The provisions of this article place limits on the amount of revenue that can be appropriated by all entities of government. The appropriation limit is adjusted annually on the basis of population and per capita income changes provided annually by the California Department of Finance. Based on Article XIII B, the City of Palo Alto can use the larger of two measurements of population growth, (county or city population growth) in the appropriations limit calculation. For Fiscal Year 2025, the City is using the 2023-2024 percent change in population growth of the County of Santa Clara in the calculation. The City typically uses the highest factor in order to provide maximum appropriation flexibility.

The appropriations limit for Fiscal Year 2025 is \$219.74 million for funds subject to the appropriation limits. The City's Fiscal Year 2025 budgeted appropriations are estimated to be \$46.64 million under the limit (Attachment B, Exhibit 1). As required by State law, documentation used to compute the appropriations limit has been made available to the public at least fifteen days prior to the Council meeting at which the appropriations limit is being adopted, and notice was published of the availability of these materials.



## RESOURCE IMPACT

This report summarizes and seeks the City Council approval of the FY 2025 Operating and Capital Budgets, the supporting fee schedules, and table of organization in order to support the projections and appropriations included.

The approval of the City Manager's FY 2025 Capital and Operating Budget, as recommended to be amended in this report, would result in a projected General Fund Budget Stabilization Reserve of \$54.4 million. At recommended expense levels of \$294.2 million, after adjusting for reserves such as the Uncertainty Reserve and the Utility Transfer Legal Cost Reserve, the BSR is at 18.5%, the Council's target in the recommended range of 15-20% of General Fund Expenditures. Exclusion reserve funding has been done to avoid unintentional inflation of the BSR. The projected changes to the fund balance for all other funds including Enterprise Funds, Internal Services Funds, Special Revenue Funds, and Capital Funds are outlined in Attachment A and accompanying exhibits and impacts to fund balance summarized in Table 2.

**TABLE 2: Resource Impact (Non-General Funds with Fund Balance Change)**

<i><b>Fund Type</b></i>	<i><b>Fund Name</b></i>	<i><b>Fund Balance Change</b></i>
<i>Capital</i>	Capital Improvement Fund	-\$6.3M
	Cubberley Infrastructure Fund	-\$1.0M
<i>Enterprise</i>	Airport Fund	-\$12k
	Electric Fund	-\$9.2M
	Fiber Fund	-\$6.4M
	Gas Fund	-\$4.1M
	Refuse Fund	-\$48k
	Stormwater Management Fund	-\$5.9M
	Utilities Administration Fund	+\$3k
	Wastewater Collection Fund	+\$35k
	Wastewater Treatment Fund	-\$7.3M
	Water Fund	-\$6.0M
<i>Internal Service</i>	General Benefits Fund	+\$0.3M
	Printing and Mailing Fund	-\$5k
	Technology Fund	-\$1.3M
	Vehicle Fund	+\$0.3M
<i>Special Revenue</i>	California Avenue Parking Permit Fund	-\$1k
	Parks Development Impact Fee Fund	+\$2k
	Residential Parking Permit Fund	-\$1k
	University Avenue Parking Permit Fund	-\$27k

## **STAKEHOLDER ENGAGEMENT**

The budget process is structured around public hearings conducted before City Council adoption to complete a detailed review of the budget documents and incorporate opportunities for community input in the decision-making process. The community was encouraged to engage with the budget process through scheduled public meetings with the Finance Committee and City Council, a community informational session with City staff, and direct emails to the City Manager and City Council. Additionally, the City maintains a dedicated webpage for meeting materials and other budget information<sup>8</sup>.

## **ENVIRONMENTAL REVIEW**

Adoption of the City budget and associated actions is not a project under California Environmental Quality Act (CEQA) Guidelines Section 15378(b)(5) (organizational or administrative activities that will not result in direct or indirect physical changes in the environment).

### **Attachments:**

Attachment A - FY 2025 Budget Adoption Ordinance

Attachment A, Exhibit 1 - City Manager's Fiscal Year 2025 Proposed Operating & Capital Budgets & Municipal Fee

Attachment A, Exhibit 2 and 3 - Amendments to the City Manager's Fiscal Year 2025 Proposed Operating and Capital Budgets

Attachment A, Exhibit 4 - Table of Organization

Attachment A, Exhibit 5 - Fiscal Year 2025 Municipal Fee Changes

Attachment A, Exhibit 6 - Impact and In-Lieu Municipal Fees

Attachment B - FY 2025 City Appropriations Limit Resolution

Attachment B, Exhibit 1 - Appropriations Limit Calculation

Attachment C - FY 2025 Summary of Stanford Investments

Attachment D - June 30, 2023 OPEB Actuarial Valuation Report (CMR 2402-2673)

Attachment D, Exhibit 1 - Central OPEB Adjustments in Various Funds

Attachment E - Planning and Transportation Commission Letter of the 2025-2029 Capital Improvement Plan to the City's Comprehensive Plan

### **APPROVED BY:**

Lauren Lai, Administrative Services Director

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<sup>8</sup> City's Budget Website: [www.cityofpaloalto.org/budget](http://www.cityofpaloalto.org/budget)