

From: Phil Koen [REDACTED]
Sent: Monday, October 11, 2021 10:09 AM
To: Shelley Neis <sneis@losgatosca.gov>
Cc: Laurel Prevetti <LPrevetti@losgatosca.gov>; jvannada@losgatosca.gov [REDACTED] Rick Van Hoesen [REDACTED]
Subject: Re: Agenda item # 7 - Finance Commission

EXTERNAL SENDER

Thank you. Please include this note as well which corrects a typo found in the first sentence of the second paragraph. That sentence should read:

A more informative view of the FY 2018 - 19 general fund budget

Thank you.

Phil Koen

Sent from my iPhone

From: Phil Koen [REDACTED]
Sent: Sunday, October 10, 2021 6:30 PM
To: Ron Dickel [REDACTED]; Kyle Park [REDACTED]
loreen@losgatosca.gov [REDACTED] Rick Tinsley [REDACTED] stacey.del@losgatosca.gov [REDACTED]
Matthew Hudes <MHudes@losgatosca.gov>; Rob Rennie <RRennie@losgatosca.gov>
Cc: Laurel Prevetti <LPrevetti@losgatosca.gov>; jvannada@losgatosca.gov [REDACTED] Rick Van Hoesen [REDACTED]
[REDACTED]; Shelley Neis <sneis@losgatosca.gov>
Subject: Agenda item # 7 - Finance Commission

EXTERNAL SENDER

Dear Finance Commission,

Attached please find the land use fiscal analysis which was prepared as part of the 2040 General Plan background report. Table 2.2-1 present a "sources and uses" view of the 2018 general fund budget and includes a debt payment of \$1,909,073 that is eliminated when presenting GAAP financial statements. Because the budget includes general fund reserves as "revenue" this view shows an excess of \$726,807 in revenues and fund balance over expenditures and transfers out. It should be noted that Table 2.2-1 reflects the original approved budget and excludes \$1.5m in salary increases and other budget adjustments that were subsequently approved by the Town Council.

A more informative view of the 2108 general fund budget can be found in the second attachment, which is taken from the 2019 CAFR. Here you can see that total expenditures in the final budget have increased \$2,490,254 from the original adopted budget and there was a deficit of revenues over expenditures totaling \$4,152,589 as opposed to the \$726,807 surplus.

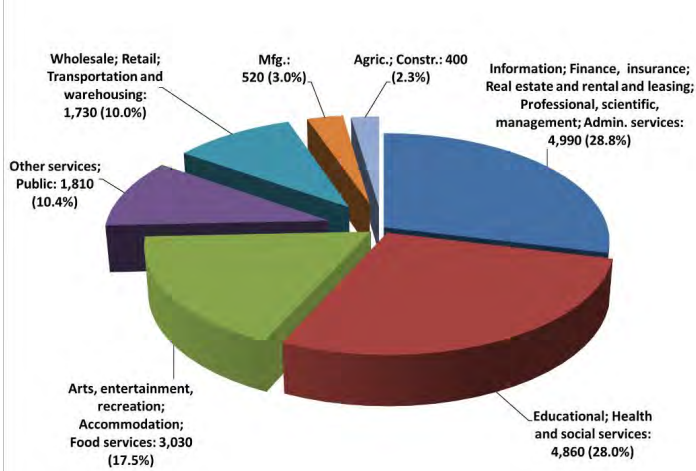
Because Table 2.2-1 does not reflect the final budget, includes general fund reserves as a source of revenue, as well as the debt payment the estimated annual revenues and costs by land use should not be relied upon. What we can conclude is the negative fiscal impact of residential land uses is far greater than what is shown in the table.

It is imperative that the Town prepare a fiscal impact analysis to understand the 20- year cumulative fiscal impact of land uses changes being proposed in the 2040 General Plan. The analysis presented in table 2.2-2 presents a one year view based on adopted land uses and population as of 2018 and is based on an incomplete 2018 budget. It is deeply flawed.

Thank you.

Los Gatos Community Alliance

Figure 2.1-6 In-Commuters by Broad Economic Sectors



Source: ADE, Inc.

Regulatory Setting

None.

2.2 Fiscal/Financial

This section describes municipal finances for the Town of Los Gatos. In addition to outlining the current budget and discussing recent staffing trends, this section discusses how different land uses contribute to the Town's tax base and demand for municipal services. As the General Plan update process goes forward, land use alternatives will be evaluated for their fiscal impact on the Town budget.

Major Findings

- The Town's General Fund supports about 70 percent of annual expenditures for Town services and facilities. The General Fund is mainly funded by taxes such as property taxes, sales taxes, and transient occupancy taxes. The other 30 percent of Town expenditures are supported by the Capital Improvements Fund and various Special Revenue Funds.
- The Town also maintains a number of Special Revenue Funds to support expenditures for capital improvements, pension and employee benefits obligations, information technology systems, and other purposes.
- In 2018, the Town adopted a balanced budget and maintained a minimum of 25 percent in reserves to cover fluctuations in economically sensitive revenues or unexpected expenses due to natural or other disasters.
- With two major recessions since the year 2000, Town staffing levels declined, reaching a low point in 2012. Since 2012, the Town has restored nine percent of its positions, but staffing remains below the level prior to the last recession in 2008.
- One major fiscal challenge for the Town, similar to many cities in California, is to fund future pensions and other post-employment benefits (OPEB) for its employees. Changes to actuarial assumptions and poor investment performance have led to increasing contribution requirements in the statewide CalPERS system. To date the Town has provided \$16.9 million in discretionary payments to the pension system and \$13.6 million to OPEB obligations. In addition, the Town has renegotiated some

of the provisions of its benefits program to reduce future obligations. However, the Town will need to continue to contribute toward these unfunded obligations for the foreseeable future.

- Residential uses generate most of the property taxes for the Town, but require a higher level of services than do commercial uses. Overall, existing residential uses are estimated to create a slight deficit in service costs over revenue. Commercial uses in the Town generate most of the sales taxes and require fewer services. Commercial uses generate a municipal revenue surplus that helps to balance the Town budget.

Existing Conditions

Town Budget

Los Gatos adopts an annual operating and capital budget, which also includes a rolling five-year General Fund projection. The General Fund supports about 70 percent of the Town's total expenditures, with the balance supported through additional funds, such as Capital Projects, Internal Services, Successor Agency, and others. For the current Fiscal Year (FY) 2018-19, which covers from July 1, 2018 to June 30, 2019, the Town has budgeted \$47.5 million in General Fund expenditures on \$48.3 million in annual revenues and use of reserves (Table 2.2-1). The largest single revenue source is property tax, which comprises 38 percent of the Town's operating revenue, when combined with property tax in lieu of vehicle license fees (VLF). The sales tax is the second largest source at \$7.7 million. The Town voters passed Measure G on the November 2018 ballot to add a local sales tax of 1/8 percent, which is estimated to increase sales tax revenues by \$700,000 per year.

In addition to annual recurring revenues, the FY 2018-19 budget includes use of several reserve funds to meet one-time expenditures as well as certain strategic goals of the Town. The Town will transfer \$2.3 million in Capital Projects Funds to support a number of road and facilities improvement projects. In addition, the Town has established additional funds to pay for its pension and OPEB obligations. Use of these reserves accounts (including the Town's General Reserve Fund) for another \$3.6 million in revenue for FY 2018-19.

For the General Fund, the largest single expenditure item is for police services, at nearly \$15 million per year. The General Government category in Table 2.2-1 consists of a number of Town offices and functions:

- Town Council
- Town Manager's Office
- Town Attorney
- Human Resources
- Finance
- Clerk Administrator
- Information Technology
- Non-Departmental

The Parks and Public Works Department has the second largest budget, at \$7.6 million, followed by Community Development at \$5.5 million. The Town does not provide fire protection services, which are instead provided by the Santa Clara County Central Fire Protection District (SCCFPD). The SCCFPD receives a property tax allocation to fund its services. For FY 2018-19, the Town estimates revenues received from Los Gatos tax payers totaled \$14.3 million.

Table 2.2-1: Los Gatos Town General Fund Budget, Fiscal Year 2018-19

Budget Categories	Annual Budget
REVENUES	
Taxes	
Property Tax	\$12,507,071
Property Tax in lieu of VLF	\$3,482,060
Sales Tax	\$7,744,208
Franchise Fees	\$2,386,910
Transient Occupancy Tax	\$2,272,500
Other taxes	\$1,657,000
Licenses and Permits	\$3,304,199
Intergovernmental	\$646,640
Town Services	\$4,457,258
Fines and Forfeitures	\$631,400
Interest Earnings and Rents	\$267,806
Other Sources	\$552,696
Debt Service Reimbursements	\$2,461,769
Transfers in	\$544,836
Use of Capital Project Funds Reserve	\$2,335,220
Use of Pension/OPEB Reserve	\$3,100,000
Use of Reserve	\$450,000
TOTAL REVENUES & RESERVE TRANSFER	\$48,248,887
EXPENDITURES	
General Government	\$12,085,478
Community Development Department	\$5,583,158
Police Department	\$14,976,514
Library	\$2,556,267
Parks and Public Works Department	\$7,626,360
Debt Payments	\$1,909,073
Transfers Out	\$2,785,220
TOTAL EXPENDITURES & ALLOCATIONS	\$47,522,070
NET REVENUES & RESERVE TRANSFERS LESS EXPENDITURES & ALLOCATIONS	\$726,807

Source: Town of Los Gatos, Operating Budget, FY 2018-2019

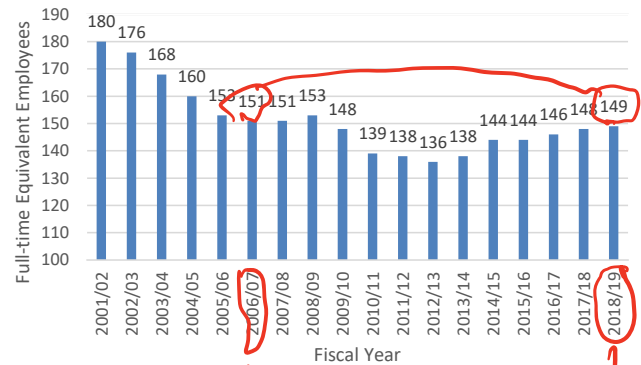
Salary increases \$1,484,487
(757,680)

Not after salary adj.

The FY 2018-19 budget has a net revenue surplus of more than \$800,000. However, with the use of the reserves as described, the overall General Fund Reserve is projected to decrease from \$27.1 million to \$20.9 million by the end of the year, of which \$10.1 million are for Catastrophic and Budget Stabilization Reserves. This complies with the Town budget reserve policy of maintaining 25 percent of operating expenditures in reserve. Over the next five years, the Town projects minimal increases in the General Fund Reserves.

Through the recessions in the early 2000's and in 2008-2009, the Town has needed to reduce costs to respond to declining revenues. As shown in Figure 2.2-1, the Town reduced its staffing from 180 positions in 2001 to 136 in 2012. The current level of 149 is well below previous peak periods.

Figure 2.2-1: Los Gatos Full-Time Equivalent Employees 2001- 2019

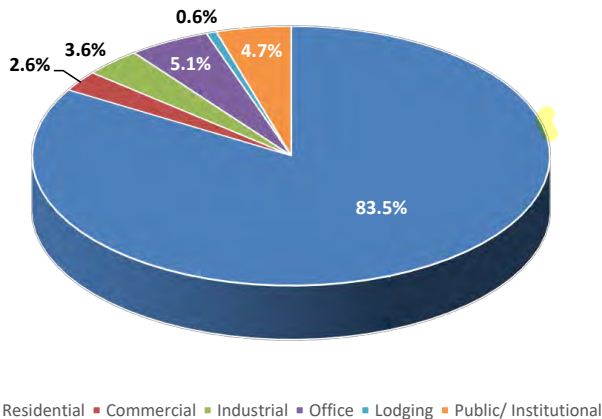


Source: Town of Los Gatos, FY 2018-19 Operating Budget, p. A-3.

Land Use Impacts on Town Budget

Residential and non-residential land uses affect Town revenues and costs differently. For example, most of the property in the Town is developed with residential uses, and in aggregate, housing produces more property taxes than non-residential development (Figure 2.2-2). Based on data published by the Santa Clara County Assessor, it is estimated that more than 80 percent of property tax in Los Gatos is paid by residential property owners. Among non-residential uses, industrial and institutional uses (including health care) are the highest property tax generators, in part because of the higher proportion of taxable equipment in those businesses.

Figure 2.2-2: Estimated Sources of Property Tax in Los Gatos, 2018



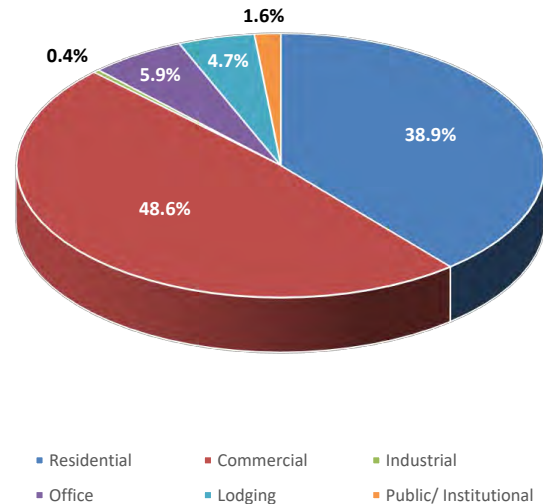
Source: ADE, Inc.

For sales tax, retail commercial uses are prominent (Figure 2.2-3). This is fundamental to how sales tax is allocated to cities in California, which is based on the point of sale (at a business location) rather than the residential location of the buyer. In Figure 2.2-3, residential uses are credited with taxable sales they make in Los Gatos, based on the retail market analysis presented later in this chapter. However, retail business in Los Gatos capture more sales than just from Los Gatos residents. The

analysis of retail supply and demand in Los Gatos indicates that residents of surrounding communities, including county unincorporated areas, spend significant dollars in Los Gatos. In addition, both day visitors and lodging visitors spend money on gas, in restaurants, and at retail establishments. Finally, the business community spends an estimated \$38.2 million on goods and services in Los Gatos.

Each of these spending sources are tracked to the corresponding land use in Figure 2.2-3, with the result that commercial uses generate about 49 percent of taxable sales, compared to 39 percent for Los Gatos households.

Figure 2.2-3: Estimated Sources of Sales Tax in Los Gatos, 2018



Source: ADE, Inc.

Municipal Service Costs

Residential uses tend to have a higher need for Town services. Residents typically have a greater number of calls for service for police protection and the use of other Town facilities (i.e., parks, libraries) than do workers who are in Town just during the workday. Many communities estimate that workers and the businesses where they are employed require approximately half the level of service as the residential population on a per capita basis. Using this factor, Table 2.2-2 estimates that residential land uses consume about 75 percent of the services the Town provides. Among non-residential uses, commercial businesses tend to be a higher target for crime while office, visitor-serving, and institutional uses generate higher levels of traffic and associated calls for service, thus requiring higher police services costs than office or industrial uses.

Table 2.2-2: Estimated Annual Revenues and Costs by Land Use in Los Gatos Fiscal Year 2018-19

Land Use	Revenues	Costs	Net
Total	\$39,968,992	(\$39,231,941)	\$737,051
Residential	\$26,891,996	(\$29,253,654)	(\$2,361,658)
Commercial	\$5,193,992	(\$4,067,888)	\$1,126,105
Industrial	\$854,080	(\$599,916)	\$254,164
Office	\$2,246,698	(\$2,241,099)	\$5,599
Lodging	\$2,802,725	(\$548,057)	\$2,254,669
Public/ Institutional	\$1,979,500	(\$2,521,328)	(\$541,828)

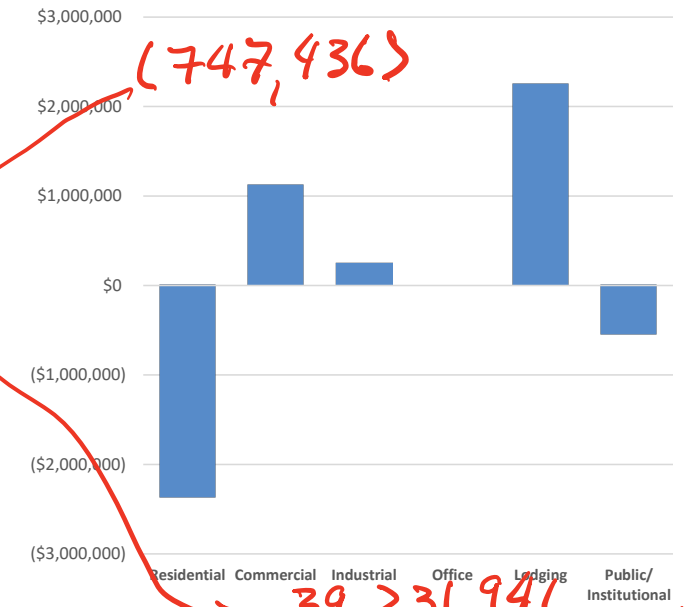
Source ADE, Inc.

Note: Totals do not add to budget totals for the Town as certain revenues and costs are not affected by land use.

The net fiscal impacts by land use are illustrated in Figure 2.2-4. This analysis reflects a balanced budget for the Town and only annually recurring costs. Use of the capital reserve and investments in the pension programs for the Town are not included. The outcome of the analysis is typical for many municipalities in California. Revenues from residential, which are more dependent on the property tax, often do not escalate with the cost of services due to the limitations on annual increases in assessments due to Proposition 13. The sales tax and the transient occupancy tax tend to follow increases in inflation more closely. The effect is that over time, residential uses do not generate enough revenue by themselves to pay the full cost of municipal services. However, in the current real estate market, new residential units often do generate

sufficient revenue, because their market values are much higher than older existing residences. The average assessed value per existing residential unit in Los Gatos is about \$700,000. For newer homes, assessed at \$825,000 or more, the cost/revenue ratio would be balanced. As it is, the retail and visitor-serving businesses in Town generate the extra revenue needed to balance the Town budget and provide the quality of services desired by Los Gatos residents.

Figure 2.2-4: Estimated Net Fiscal Impact by Land Use in Los Gatos, 2018



Source: ADE, Inc.

Handwritten calculations:

$$\begin{array}{r}
 39,231,941 \\
 1,484,487 \\
 \hline
 40,716,428
 \end{array}$$

Salaries w/c

**TOWN OF LOS GATOS
GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL (GAAP)
FOR THE FISCAL YEAR ENDED JUNE 30, 2019**

	Original Budget	Final Budget	Actual	Variance With Final Budget Positive (Negative)
REVENUES				
Property Taxes	\$ 15,989,131	\$ 16,718,348	\$ 17,321,344	\$ 602,996
Sales Taxes	7,744,208	7,629,879	8,158,152	528,273
Other Taxes	2,279,500	2,629,500	2,698,352	68,852
Franchise Fees	2,386,910	2,386,910	2,475,916	89,006
Licenses & Permits	4,961,199	4,961,199	4,586,788	(374,411)
Intergovernmental	685,759	845,718	950,380	104,662
Charges for Services	4,491,868	4,596,416	4,643,715	47,299
Fines and Forfeitures	631,400	631,400	510,266	(121,134)
Interest	267,806	267,806	1,682,347	1,414,541
Use of Property	31,959	31,959	32,960	1,001
Other	445,308	466,308	562,714	96,406
Total Revenues	<u>39,915,048</u>	<u>41,165,443</u>	<u>43,622,934</u>	<u>2,457,491</u>
EXPENDITURES				
Current:				
General Government:				
Town Council	223,036	230,280	205,903	24,377
Town Attorney	556,183	597,768	562,542	35,226
Administrative Services	4,290,959	4,641,901	3,931,807	710,094
Non-Departmental	7,015,300	7,043,251	3,304,002	3,739,249
Total General Government	<u>12,085,478</u>	<u>12,513,200</u>	<u>8,004,254</u>	<u>4,508,946</u>
Public Safety	14,976,514	15,713,469	14,945,407	768,062
Community Development	5,583,158	5,786,501	4,577,495	1,209,006
Parks & Public Works	7,626,361	8,619,883	7,934,869	685,014
Library Services	2,556,267	2,684,979	2,493,617	191,362
Capital Outlay	-	-	38,307	(38,307)
Total Expenditures	<u>42,827,778</u>	<u>45,318,032</u>	<u>37,993,949</u>	<u>7,324,083</u>
EXCESS (DEFICIT) OF REVENUES OVER EXPENDITURES	<u>(2,912,730)</u>	<u>(4,152,589)</u>	<u>5,628,985</u>	<u>9,781,574</u>
OTHER FINANCING SOURCES (USES)				
Proceeds from sale of assets	1,000	1,906,000	1,912,316	6,316
Transfers In	538,536	538,536	1,578,911	1,040,375
Transfers Out	(2,785,220)	(2,785,220)	(2,785,220)	-
Total Other Financing Sources (Uses)	<u>(2,246,684)</u>	<u>(2,246,684)</u>	<u>706,007</u>	<u>1,046,691</u>
NET CHANGES IN FUND BALANCES	<u>\$ (5,159,414)</u>	<u>\$ (6,399,273)</u>	<u>6,334,992</u>	<u>\$ 10,828,265</u>
BEGINNING FUND BALANCE			<u>31,635,535</u>	
ENDING FUND BALANCE			<u>\$ 37,970,527</u>	

The notes to the financial statements are an integral part of this statement.