



**TOWN OF LOS GATOS  
COUNCIL AGENDA REPORT**

MEETING DATE: 12/15/2020

ITEM NO: 10

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DATE: December 8, 2020  
TO: Mayor and Town Council  
FROM: Laurel Prevetti, Town Manager  
SUBJECT: Receive a Fiscal Year (FY) 2020/21 Revenue and Expense Update

**RECOMMENDATION:**

Receive a Fiscal Year (FY) 2020/21 Revenue and Expense update.

**BACKGROUND:**

On January 21, 2020, the Town Council received the initial Five-Year Forecast which became the basis of Strategic Priority planning and budgetary considerations. The development of that original forecast did not anticipate the unforeseen economic impacts associated with the local, national, and global effects of COVID-19.

On May 19, 2020, staff presented an updated Five-Year Forecast and the Proposed Operating Budget which included significant revisions to growth projections for the Town's primary revenues of property tax, sales tax, and transient occupancy tax (TOT). The revised revenue projections were made in close consultation with the Santa Clara County Assessor, Town sales tax consultant MuniServices, and a review of national and regional hospitality research. The following table contains the growth rates included in the Adopted Budget for the primary revenues of property tax, sales tax, and TOT.

FY 2020/21 Forecast	
Property Tax Growth Projection	2%
Sales Tax Growth Projection	MuniServices COVID-19 Scenario
Transient Occupancy Tax (TOT) Growth Projection	-15%

**PREPARED BY:** Arn Andrews  
Assistant Town manager

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Reviewed by: Town Manager, Town Attorney, and Finance Director

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BACKGROUND (continued):

Since the adoption of the FY 2020/21 budget, staff has continued to monitor revenue trends in relation to the Adopted Operating Budget and the unprecedented impacts of COVID-19.

DISCUSSION:

While staff does not normally try to extrapolate forward trends utilizing first quarter revenue/expense data, a review of current revenue/expense collections, disbursements, and projections is warranted given the significant events associated with COVID-19. The intent of this agenda item is to provide a snapshot of what is currently known for the fiscal year given the public interest surrounding the impacts of the COVID-19 related economic downturn.

In late February, the Council will receive the Mid-Year Budget Report (July 1, 2020 – December 31, 2020) which will provide an accounting of revenue and expenditure activity. At that time, the Council typically considers potential revenue and/or expenditure adjustments to the Adopted FY 2020/21 Operating Budget to align financial resources with Town needs for the remainder of the fiscal year.

**Revenues**

Following are summaries of major revenues to date and projections if available for property tax, sales tax, and TOT.

Property Tax

Property tax is the single largest revenue source for the Town and comprised approximately 28% of total Town projected revenues for FY 2020/21. Most property tax revenue is received in the second half of the year, so first quarter collections are not insightful.

The County of Santa Clara does provide updated projections throughout the year. The following table illustrates the most recent estimates relative to the Adopted FY 2020/21 Budget and 2019 actuals. The current County estimate indicates a modest deviation from budget of approximately \$300,000.

	FY 2019 Actual	FY 2020-21 Adopted Budget	November 6, 2020 County Estimate
Property Tax Revenue & Vehicle License Fee Backfill	\$18.4 M	\$18.7 M	\$18.4 M

DISCUSSION (continued):

It should be noted that the Town was recently informed that the County of Santa Clara intends on withholding approximately \$1.6 million over the next several fiscal years to recapture excess RDA residual property tax revenues distributed to the Town. County Counsel has advised the Auditor/Controller’s Office to “look back” three fiscal years to determine the total amount to be recaptured from the Town and paid back over two fiscal years. The immediate impact to the Town Budget will be an unanticipated withholding of approximately \$789K in FY 2020/21. The \$18.4 million November 6, 2020 County estimate reflects this reduction.

In addition, the Town is continuing to monitor developments regarding the distribution of excess Educational Revenue Augmentation Fund (ERAF) funds. A portion of property tax revenue goes to the ERAF to support local school districts. When the amount contributed to ERAF is more than the minimum cost of funding local schools, excess funds are returned to the county, cities, and special districts. Five counties, including Santa Clara, have been using a redistribution allocation formula that is being contested by the State. The Town's Adopted FY 2020/21 Budget had ERAF revenue estimated at \$433,000. The November 6, 2020 County property tax estimate includes \$1.8 million of ERAF funds. If the State is successful in contesting ERAF distribution the result would be a negative impact on budgeted revenues. The following table illustrates the potential impacts of ERAF distribution.

	County Estimate with ERAF	County Estimate 50% of ERAF	County Estimate No ERAF
Property Tax Revenue & VLF Backfill	\$18.4 M	\$17.5 M	\$16.6 M

While the aforementioned ERAF discussion does not pertain to COVID-19 impacts, it is a material potential revenue event the Town is monitoring.

Sales Tax

Sales tax is the second largest revenue source for the Town and comprised approximately 12% of total Town projected revenues for FY 2020-21. The following table illustrates the most recent projections from the Town’s sales tax consultant MuniServices relative to the Adopted FY 2020-21 budget and 2019 actuals.

	FY 2019/20 Actual	FY 2020/21 Adopted Budget	October 6, 2020 MuniServices Estimate
Sales Tax	\$7.5 M	\$8.0 M	\$7.3 M

DISCUSSION (continued):

The current estimate indicates a deviation from budget of approximately \$700,000; however, staff anticipates receiving the September 30, 2020 first quarter updated projection in mid-December and the estimate will likely change.

In addition, to the projection provided by MuniServices, the Town receives actual sales tax distributions throughout the year from the California Department of Tax and Fee Administration. As the table below illustrates, for the quarter ended September 30, 2020, the Town received \$2.15 million in sales tax distributions or 27% of annual budgeted revenues. It is important to note that while State distribution data is informative, due to the uneven nature of distribution, it often makes quarter to quarter comparisons difficult. Distribution data should be viewed in concert with MuniServices year-end estimates.

	FY 2018/19 Actual	FY 2019/20 Actual	FY 2020/21 Actual
Sales Tax			
1Q	\$1,940,462	\$2,151,795	\$2,150,494
2Q	1,872,921	2,372,516	
3Q	1,803,171	1,151,656	
4Q	2,541,598	1,855,458	
<b>Total</b>	<b>\$\$8,158,152</b>	<b>\$\$7,531,425</b>	<b>\$\$2,150,494</b>

Transient Occupancy Tax

TOT is a significant revenue source for the Town and comprised approximately 3.4% of total Town projected revenues of \$2.3 million for FY 2020-21. The following table illustrates TOT collections through September 30, 2020 relative to the Adopted FY 2020-21 budget, FY 2018/19 actuals, and FY 2019/20 actuals.

	FY 2018/19 Actual	FY 2019/20 Actual	FY 2020/21 Actual
TOT			
1Q	\$735,349	\$739,494	\$316,515
2Q	632,240	599,113	
3Q	608,902	434,493	
4Q	715,552	96,585	
<b>Total</b>	<b>\$2,692,043</b>	<b>\$1,869,685</b>	<b>\$316,515</b>

DISCUSSION (continued):

As the table illustrates, to date TOT has experienced the most significant percentage decline relative to budget at 57% quarter over quarter for the first quarter. In addition, on November 28, 2020, Santa Clara County issued new mandatory directives which included that hotels and other lodging facilities will be open only for essential travel and for use to facilitate isolation or quarantine. Staff anticipates that the current Health Order will further degrade TOT revenues in the second quarter relative to the prior year.

**Expenditures**

As illustrated in the table below, Total Department Expenditures in the first quarter of FY 2020/21 as a percentage of the Adopted Budget (25%) were comparable to the prior year first quarter of 26%.

	FY 2019/20 Actual	FY 2019/20 Q1	Q1% of 2019/20 Actuals	Q1% of 2020/21 Actuals	FY 2020/21 Q1	FY 2020/21 Adopted
<b>Expenditures</b>						
Mayor & Council	\$206,163	\$62,150	30.1%	21.4%	\$52,041	\$243,486
Attorney	559,010	164,678	29.5%	26.3%	169,822	645,303
Admin Services	4,380,504	1,297,422	29.6%	28.6%	1,421,711	4,974,616
Non-Departmental	7,878,468	627,652	8.0%	11.0%	379,044	3,452,007
Community Dev	4,473,790	1,240,383	27.7%	22.2%	1,223,829	5,517,030
Police	15,793,815	5,022,928	31.8%	27.8%	4,898,017	17,587,825
Parks & PWs	8,139,106	2,052,936	25.2%	26.6%	2,166,965	8,152,045
Library	2,700,802	844,265	31.3%	22.8%	671,597	2,946,509
Capital Outlay	138,384	-			-	-
<b>Total Department Expenditures</b>	<b>\$44,270,042</b>	<b>\$11,312,414</b>	<b>26%</b>	<b>25%</b>	<b>\$10,983,026</b>	<b>\$43,518,821</b>

CONCLUSION AND NEXT STEPS:

With the exception of TOT, the primary revenue sources of property tax and sales tax are currently trending in line with the Adopted Budget. In addition, currently departmental expenditures are consistent with prior disbursements relative to the Adopted Budget. Given current TOT collections and expectations for continued leisure and business travel constraints, staff anticipates recommending that the Council adjust the FY 2020/21 TOT revenue downward at the February Mid-Year review.

In addition to the Mid-Year review, the Council will be receiving an updated Five-Year Forecast in early 2021 as part of the FY 2021/22 Budget preparation. The Forecast is typically analyzed

CONCLUSION AND NEXT STEPS:

with optimistic and pessimistic scenarios to provide the Council and the public with information regarding how sensitive the forecast can be to changing assumptions and circumstances. As part of this discussion, the Council may also provide specific budget direction for certain assumptions, such as staff vacancy rates, budgeting at actual versus top salaries, etc.

COORDINATION:

This staff report was coordinated with the Town Manager, Town Attorney, and Director of Finance.

FISCAL IMPACT:

No fiscal impact at this time. Staff will continue to monitor revenues and expenses and bring forward any budget adjustment recommendations at Mid-Year.

ENVIRONMENTAL ASSESSMENT:

This is not a project defined under CEQA, and no further action is required.