Recommended 2005/2006 Budget
and
Ten-Year Resource Allocation Plan

City Manager's
Letter of Transmittal

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Honorable Mayor and Members of the City Council:

CITY MANAGER'S MESSAGE

EXECUTIVE SUMMARY

I am pleased to present for your review and consideration the recommended FY 2005/2006 Budget and accompanying Ten-Year Resource Allocation Plan (RAP). In addition, financial projections are provided for a second ten years, ensuring a full 20-year perspective for financial planning. In keeping with Council policy, each fund is balanced to the twentieth year when coupled with certain financial strategies and assumptions. While this has been a difficult task again this year for a number of reasons described below, significant progress has been made toward adjusting to the City's new fiscal realities.

FY 2005/2006 is the second year of the two-year operating budget cycle and the first year of the projects budget cycle. Most operating programs are not reviewed extensively the second year, allowing staff instead to perform a detailed review of all capital and special projects. Major revenue sources, personnel costs and enterprise activities are reviewed each year in order to ensure the accuracy of our long term projections. The process utilized in preparing the recommended FY 2005/2006 Budget is discussed in more detail later in Appendix A of this Transmittal Letter.

Sunnyvale and the rest of Silicon Valley continue to be challenged by a severe economic downturn exacerbated by increasing personnel costs and a severe State budget. In response to a $15 million budget shortfall in FY 2003/2004, Council took decisive action to reduce services and enhance revenues.

Unfortunately, the negative fiscal conditions continued through FY 2004/2005. Council utilized a new budget review process to identify service reductions and revenue enhancements totaling about $5 million in possible fiscal strategies. These service reductions were subsequently deferred, however, pending consideration in this FY 2005/2006 budget process.

Recommended FY 2005/2006 Budget

The recommended FY 2005/2006 Budget of $227 million for all City funds continues to acknowledge Sunnyvale's new fiscal reality. The level of services included reflects the reductions made in FY 2003/2004, with no further increases proposed. The service reductions approved in concept in FY 2004/2005 have not yet been included in the recommended budget. Assumptions for the City's major revenue sources reflect their specific business cycles. This means that with the recent downturn, the recommended budget is projecting marked growth to reflect the upside of the business cycles. On the expenditure side, the recommended budget assumes salaries and the cost of goods and services will increase modestly.

Even with aggressive revenue growth and conservative expenditure assumptions, $1.1 million in reductions or revenue enhancements will be required starting FY 2006/2007 to maintain this "bare bones" budget. In addition, reserve levels have been reduced to the minimum required by City policy. As a result, little flexibility remains for responding to unplanned conditions.

This year's focus on projects also reflects this "bare bones" approach. While over $21 million in projects citywide is recommended, the majority are needed to maintain the City's existing infrastructure. The FY 2005/2006 projects budget also expands last year's efforts to include projects that are anticipated in the second ten years of the City's Long Term Financial Plan. The projects budget for the twenty year planning period totals $259 million as compared to last year's twenty year total of $191 million. In addition to these projects, an unfunded projects list has also been developed, representing substantial future unfunded liabilities to the City.

Sunnyvale's new fiscal reality is most clearly felt in our General Fund. This fund accounts for our basic city services and is the one that is most affected by economic conditions. The recommended FY 2005/2006 Budget for the General Fund is $106 million. This reflects the previous FY 2003/2004 service reductions and contains no new increases. Nevertheless, a structural imbalance between revenues and expenditures continues to exist in this fund during the first ten years of the planning period. In order to balance the budget for FY 2005/2006, staff took several actions.

First, existing reserves were reduced to the minimum required by Council policy. The balances in the existing Land Acquisition and Non-Recurring Events Reserves were eliminated. The Service Level Stabilization Reserve, which had previously equaled 5% of Operations, was also eliminated. This latter reserve has been converted to a Service Level Set-Aside in the second ten years of the plan.

Second, staff strategically reviewed all areas supported by the General Fund to identify ongoing expenditures that could be more appropriately funded by other sources. As a result, Park Dedication Funds were programmed for all park-related infrastructure projects formerly paid for by the General Fund. Additional Gas Tax and Traffic Congestion Relief Program funds from the State were applied to the Public Works Pavement Operations program, again relieving the General Fund of these costs. The General Fund transfer to the Infrastructure Renovation and Rehabilitation Fund was reduced based on an updated schedule for replacement costs and timing.

Even with elimination of reserves and the shifting of expenses, the General Fund Long Term Financial Plan was unbalanced over the twenty years, largely due to rising costs in retirement contributions and medical insurance. An additional ongoing decrease in expenditures or increase in revenues of $1.1 million is needed in the first part of the planning period. Staff reflected this amount in the *Fiscal Strategies* line item of the plan through FY 2012/2013. The specific expenditure reductions or revenue enhancements will need to be identified and implemented by FY 2006/2007, the first year that the *Fiscal Strategies* line is reflected.

Financial Successes

The City has made considerable progress toward its goal of long term financial stability during this past year. Particularly noteworthy is our work to identify and fund our infrastructure renovation and rehabilitation needs, our efforts in affordable housing, and our continued refinement of the City's Planning and Management System.

Phase I of the Long Range Infrastructure Plan (LRIP), which incorporates General Fund-related assets, has been in place for some time. Original assumptions regarding cost and timing are in the process of being reviewed and updated. Staff has also been identifying and inventorying utility-related fixed assets and for the first time the recommended FY 2005/2006 Budget includes preliminary estimates for a full twenty year time frame. Work to refine the utility-related LRIP further will be completed in late 2005. Updates to both phases of the LRIP will be reflected in the budget for FY 2006/2007.

Sunnyvale has a number of sources of funds for affordable housing, including Housing Mitigation Funds, HOME grants, and Community Development Block Grants (CDBG). $14 million is programmed from Housing Mitigation Funds and HOME grants for affordable housing projects and programs over the twenty-year planning period. The City only budgets CDBG funds as they are allocated, because of the uncertainty of the funding, but the vast majority of the $1.4 million annual grant and the estimated $600,000 program income are focused on housing programs. With the impending redevelopment of the Town Center Mall, we have anticipated that the Redevelopment Agency's Low and Moderate Income Housing Fund will begin to collect funds for affordable housing in FY 2016/2017 and will have realized almost $17 million by the end of the 20-year planning period. In total, this represents a considerable level of funding for this important community need.

Sunnyvale's Planning and Management System provides the foundation upon which to make informed policy decisions in support of the City's core mission. During this past year staff has undertaken an ambitious program to update all administrative policies as well as our basic performance budgeting structure. Most of the administrative policies have been reviewed and updated. A review and analysis of the performance based budgeting system began early in FY 2004/2005 and is expected to be completed by the end of the fiscal year. Work included evaluation of the philosophy and intent of the system as well as the process. Recommended changes to the performance based system will be brought to Council in a study session format early in FY 2005/2006. Following approval of the revised system, staff will begin restructuring all programs into the revised format. This work will be completed during FY 2005/2006 and used to prepare the next two-year operating budget. This effort will also provide us a context within which to revisit the proposed budget reductions from FY 2004/2005.

Continuing Fiscal Pressures

During this year's budget process, staff sought to identify all items that could have a negative impact on the City's financial condition, in the short and long term. While

several concerns were identified, they are not funded in this budget because the scope and costs are not known at this time or because the funds are simply not available. Therefore, although the recommended FY 2005/2006 Budget is balanced, the City has several areas of vulnerability that are briefly discussed below:

- ***Library Facility and Programming*** – Several years ago, Council directed a study be conducted on potential expansion of the Library. Phase I of this study indicated that our Library facility and collection were not keeping up with the growing demand for our services and the Library facility is becoming inadequate to support even the current level of services. Rather than immediately moving to a project to expand the Library, a visioning exercise will be conducted during FY 2005/2006 to define the library of the future. The result of this effort could potentially identify substantial costs to maintain current service levels or new services and facilities.

- ***Community Recreation Fund Subsidy*** - The General Fund has provided a subsidy to the Community Recreation Fund since the Community Recreation Fund was created in FY 1991/1992. The subsidy level for FY 2005/2006 has been held to the same amount that it has been for the past two years. However, due to significant decreases in golf and recreation revenues and increase in personnel costs, there is a structural imbalance in the Fund. An increase in revenues and/or decrease in expenditures is required in order to prevent a further draw on the General Fund. Staff is conducting a comprehensive review of the purpose, quality and requirements of the Community Recreation programs, including prioritizing services and developing fiscal strategies. Staff will return to Council with options and recommendations in the fall to address the funding issue.

- ***Employee Costs*** - The cost for employees, both in salaries and benefits, has increased significantly in the last several years, outpacing revenue trends in the most recent years. Because labor costs are the largest component of operating expenditures, these increases are problematic for the long term financial picture. The recommended FY 2005/2006 Budget includes the increased costs for retirement and medical insurance and known adjustments related to the Memorandums of Understanding with our employee associations/unions. Growth in the number and cost for retiree medical insurance has also been factored in. Although identified, the increase in number of retirees over the twenty year planning period will be substantial and is not fully funded in this budget. The salary adjustments assume our comparator agencies will have modest increases in the next few years. If this assumption does not hold, the current recommended budget does not have the flexibility to handle unplanned increases.

- ***Unfunded Projects*** – As mentioned earlier, this year's project budget process identified all of the City's capital and infrastructure needs. Because this is a "bare bones" budget, an unfunded projects list was developed for those identified projects that are not the most critical or fully scoped at this time. The unfunded projects list totals $444 million in costs over the twenty years. While many of the project costs are preliminary estimates and most of the costs are anticipated in the second ten years, these projects represent substantial unfunded liabilities.

- ***Civic Center Replacement or Renovation*** – Due to functional obsolescence, the City will have to undertake a major renovation of City Hall, the Library, and the Public Safety Building sometime in the twenty year planning period. Included on the unfunded list is the reconstruction of the existing Civic Center campus. The total cost of improvements will be substantial, currently estimated to be more than $150 million with only modest increases from existing building size.
- ***Investment in the Organization*** – In order to maintain the quality of life that the community expects, we need to function as a high performing organization, leveraging opportunities as they arise and attracting and retaining top level employees. To be high performing, we need to invest in our human resources, providing opportunities for learning and developing skills. It is critical to create a culture that focuses on customer service, embracing innovation as a strategy for cost effectiveness and efficiency in service delivery. This must be coupled with instilling accountability throughout the organization but rewarding high performing employees. With our current "bare bones" budget, much of the investment in these areas has been eliminated. Restoring some of this flexibility when possible will be a smart investment in our future strength as an organization.
- ***Open Space*** – One of the most significant challenges facing the parks and recreation profession in urban environments today is that of trying to satisfy a seemingly unlimited demand for a very limited amount of open space. This has been at the heart of several controversial policy issues in Sunnyvale, including cricket play at Ortega Park, a park use and capacity study issue, dogs on/off leash, turf wars among and between youth sports groups for fields, and concerns regarding busloads of children accessing "neighborhood" playgrounds. As the City's population increases and demographics change, additional open spaces and/or changes to existing open spaces may be necessary. This is a subject that will be explored during pending revisions to the City's Recreation and Open Space Sub-elements.

Fiscal Strategies

Last year's budget included several fiscal strategies to address the structural deficit. These included a three pronged approach: continuous improvements within the organization, expenditure reductions, and revenue enhancements. First, various cost saving strategies were identified to be explored. These included a multi-year analysis designed to optimize staffing levels in each major City department and an emphasis on employing technology wherever possible to improve efficiency of City operations. A list of these and other cost savings strategies is included in *Appendix B* of this Transmittal Letter.

Second, service level reductions were proposed, based on Council priorities. As mentioned earlier, these proposed service level reductions have been deferred. Third, several potential revenue enhancements were considered. Council has provided policy direction to implement an Emergency 911 fee, pending resolution of legal issues. Additional Sales Tax revenue from the Town Center Mall redevelopment and a new rent charged for the SMaRT Station land have been included in the Long Term Financial Plan.

I am recommending that we continue to pursue all of the strategies identified last year. We have not included the revenues from the Emergency 911 Fee in the recommended FY 2005/2006 Budget because of the uncertain legal status. When the issues are resolved, implementation as per Council direction will provide approximately $2 million in needed new resources to the General Fund. The service level reductions proposed last year total $2.2 million. I will be reviewing and prioritizing these individually and will bring this analysis back to Council with the Mid-Year Review for consideration.

I am also recommending that the Council pursue two other possible revenue increases. The City's Transient Occupancy Tax and Business License Tax rates are lower than those of most of our surrounding communities. An increase in our Transient Occupancy Tax from 8.5% to the County average of 10% would generate about $900,000. The Business License Tax, which currently ranges from $10 to $325, is among the lowest in the County and is significantly lower than San Jose's high of $25,000. Raising this tax could provide $750,000 - $1 million in additional funds. These tax rate increases are not included in the recommended FY 2005/2006 Budget because they require voter approval for adoption. If approved, these two revenue increases would provide additional financial flexibility as the City addresses its future financial challenges. Council may also want to identify other potential revenue sources for consideration such as an admissions tax.

One additional fiscal strategy to consider which is also not included in the recommended Budget is the review of our land banking policies and sale of City land. During FY 2004/2005, Council provided preliminary direction to sell excess City land that is not tied to City development plans, such as plans for the downtown or the civic center. Significant one-time revenues can be generated from the sale of these excess City land parcels. However, it is recommended that the sale of land be held off pending updates to the City's Open Space and Fiscal Sub-elements, both of which will be revised during FY 2005/2006. It is important that clear policy direction underlie all decisions made, and these two policies will help us in our decisions relating to the use of City land and land proceeds as well as defining the long term view of what is desirable for our community and high quality of life.

Although most of these fiscal strategies are not needed to balance the FY 2005/2006 "bare bones" budget, they are the key for improving the City's financial position and ensuring long term financial stability that is responsive to community needs. I recommend we continue to pursue these fiscal strategies during FY 2005/2006 so we will be well positioned to meet the fiscal challenges ahead.

Conclusion

Two final points need to be made. First, Sunnyvale's planning and financial management systems provide the foundation on which we are building the solutions to the City's budget crisis. Without this foundation, we would have found ourselves unprepared to respond to a budget crisis of this magnitude, which requires that the City "change its lifestyle" to adjust to our new fiscal realities.

Second, although we have recommended ways to close the General Fund structural gap, our job is not over. A number of fiscal pressures have been identified that we must address in the coming years. Our economic condition continues to be evolving, and we will need to continue to pay close attention and make course corrections as necessary. Most of all, we will have to make courageous fiscal decisions while remaining responsive to community needs.

The City's approach to budgeting and long-term financial planning is complex, and highly valued in this organization and in our community. In preparing the recommended FY 2005/2006 Budget and Ten-Year Resource Allocation Plan, I am fortunate to have had the support and assistance of exceptional staff who continually go beyond the call of duty.

First, I would like to thank Deputy City Manager Chuck Schwabe for his efforts in coordinating the Council's new budget service review process. This process focuses on one-eighth of the City's operating programs. This year, the utility-related programs in Public Works and Finance were reviewed. Much staff work was undertaken by the directors and program managers in these two departments, particularly by Marvin Rose, Mary Bradley and Tim Kirby. I am grateful to them for their support and commitment to provide timely and complete information to the Council for consideration.

Of course, the budget would not have been prepared without the talented and dedicated budget team led by Mary Bradley, Director of Finance and Grace Kim, Finance Manager. These team members, including Mark Eyrich, Kurtis Mock, Charlene Sun and Tim Kirby, did a yeoman's job in putting the budget together and I greatly appreciate their dedication. My appreciation also goes to Assistant City Manager Robert Walker, who provided able assistance with the budget strategies and this budget message.

Finally, I would like to thank the Council for your leadership and support and your commitment of time in developing the new budget process, community outreach, and policy direction.

Respectfully Submitted,

Amy Chan
City Manager

May 13, 2005

FISCAL YEAR 2005/2006 BUDGET

OVERVIEW

I am pleased to present a balanced budget for this upcoming fiscal year. The Ten-Year Resource Allocation Plan and 20-year financial plan are in balance as well when coupled with the financial strategies that have been developed for Council's consideration as we address our ongoing structural imbalance between revenues and expenditures. In fact, if all of the financial strategies were successfully implemented, the long-term financial picture would provide the City financial flexibility in the second ten years.

Table I, below, is a summary of the recommended expenditures for all City funds. This table provides a comparison of the recommended FY 2005/2006 Budget with the revised FY 2004/2005 Budget and the actual expenditures for FY 2003/2004.

Table I Recommended Expenditures – Citywide*

Expenditure	2003/2004 Actual	2004/2005 Revised Budget	2005/2006 Proposed Budget	% Growth 2005/2006 over 2004/2005
Operating	146,962,524	160,341,500	170,093,184	6.08%
Projects**	24,061,857	68,168,356	21,159,682	-68.96%
Lease Payments***	1,216,661	1,554,330	1,849,908	19.02%
SMaRT Station Expenses****	17,452,500	17,610,787	16,776,843	-4.74%
Debt	6,845,819	6,823,666	6,813,408	-0.15%
SUB-TOTAL	**196,539,361**	**254,498,639**	**216,693,025**	**-14.85%**
Employment Development Grant Programs	12,347,229	9,992,785	10,126,301	1.34%
TOTAL	**208,886,590**	**264,491,424**	**226,819,326**	**-14.24%**

*This table excludes internal service funds, which are reflected as rental and additive rates in the Operating expenditure line.
**Projects excludes General Services projects but includes Project Administration costs
*** Lease Payments include the Parking Lease, SMaRT Station Long Term Lease and WPCP Rent.
****The SMaRT Station Expenses represent Mountain View and Palo Alto's shares of SMaRT Station expenses. Sunnyvale's share of expenses is represented in the Operating expenditure line.

The overall recommended FY 2005/2006 Budget is 14.24% below the revised FY 2004/2005 Budget. However, the inclusion of the Employment Development Grant programs and project-related expenditures can be misleading when making year-to-year comparisons.

The recommended FY 2005/2006 Budget for operating-related expenditures is 6.08% higher than the revised FY 2004/2005 Budget. In general, the increases are attributable to increases in the cost of personnel-related benefits including retirement contributions and medical insurance and certain services such the provision of contract refuse collection. Direct salary costs are budgeted to increase by 1.2%. The

individual components of the increases may vary for each fund and will be discussed the *Detailed Fund Reviews* section of this Transmittal Letter.

The project line item appears to have a dramatic decrease from the FY 2004/2005 revised Budget to the recommended FY 2005/2006 Budget. This type of yearly comparison is difficult to make because of the one-time nature of projects. The large apparent increase in the FY 2004/2005 Budget is due to the carryover of funds for projects that were budgeted in earlier years but not yet completed. Because projects are often multi-year in nature, project funds are carried over from year to year. This can be seen in the FY 2004/2005 revised Budget number of $68.1 million for projects. Of this amount, approximately $50.7 million represents carryover of funds for projects in progress from FY 2003/2004. When this is removed, the number for new projects funding in FY 2004/2005 is approximately $18.1 million. In this context, the recommended FY 2005/2006 Budget for projects represents an increase in funding over last year of 16.9%.

OVERVIEW OF GENERAL FUND AND GAS TAX FUND

Table II below outlines the recommended expenditures for the General Fund and Gas Tax Fund combined. Although these are separate funds, they are added together in Table II to better represent the proposed changes from one year to the next. It is in the interest of the City to expend Gas Tax Funds for eligible projects and operating activities before utilizing General Fund money. This results in increases and decreases from year to year regarding the amount of road maintenance operations that are funded by the Gas Tax Fund and General Fund respectively. By combining the two funds, a clearer picture results as to the year-to-year changes.

Table II Recommended Expenditures – General Fund and Gas Tax Fund Combined

Expenditure Character	2003/2004 Actual	2004/2005 Revised Budget	2005/2006 Proposed Budget	% Growth 2005/2006 over 2004/2005
Operating	90,438,754	100,022,782	106,527,270	6.50%
Project Operating	0	0	9,668	N/A
Projects	4,006,486	4,310,884	1,693,268	-60.72%
Debt	412,283	411,358	410,138	-0.30%
Lease Payments	1,216,661	1,220,728	1,219,558	-0.10%
Equipment	0	0	300,000	N/A
TOTAL	**96,074,184**	**105,965,752**	**110,159,902**	**3.96%**

As Table II indicates, the overall combined recommended expenditures of the General Fund and Gas Tax Fund for FY 2005/2006 are 3.96% above the revised FY 2004/2005 Budget. Because certain aspects of the budget can change dramatically from year to year, notably capital, infrastructure and special projects, a more precise understanding of the comparative budget is in the operating area. The operating portion of the recommended FY 2005/2006 Budget is 6.5% above the revised FY 2004/2005 Budget.

OVERVIEW OF PROPOSED CAPITAL AND SPECIAL PROJECTS BUDGET

In keeping with the separation of the operating and project budget cycles, FY 2005/2006 is the first year of a two-year capital and special projects budget. All projects proposed for the Ten-Year Resource Allocation Plan underwent a thorough review by the Projects Review Committee prior to being recommended to the City Manager. This process will be further described in *The Sunnyvale Approach to Budgeting* section that appears later. As a result of the project budget process this year, I am recommending $20,367,480 in capital and special projects in FY 2005/2006 and a total of $144,946,403 in projects over the ten-year planning period. Details of the projects budget are included in the *Major Project Efforts* section of this Transmittal Letter, in discussion of the individual funds, and in *Volume II Projects Budget* of the budget document.

Below is a table containing project appropriations by fund for FY 2005/2006 and the remainder of the long term planning period.

Table III Project Expenditures by Fund

Fund	2005/2006 Recommended Budget	2005/2006 to 2014/2015 Total	2015/2016 to 2024/2025 Total
Asset Forfeiture	253,400	761,162	0
Capital Projects	1,838,543	9,567,971	15,841,279
Community Development Block Grant	2,329,790	5,858,518	2,259,495
Community Recreation	10,500	63,199	0
Gas Tax	220,000	855,204	2,895,618
General Fund	1,361,654	10,639,494	10,691,089
General Services	780,005	2,371,444	682,191
Housing	1,806,400	5,806,771	1,980,593
Infrastructure Renovation & Replacement	2,724,593	24,891,450	28,470,468
Park Dedication	15,000	3,784,021	225,783
Parking District	52,500	508,240	618,899
Redevelopment Agency	265,000	1,727,792	73,519
SMaRT Station*	2,764,950	7,584,669	4,003,304
Utilities	5,945,145	70,526,468	46,453,218
TOTAL	**20,367,480**	**144,946,403**	**114,195,456**

*The SMaRT Station project costs represent Mountain View and Palo Alto's share. Sunnyvale's share is included in the Utilities project cost.

FUTURE FISCAL ISSUES

Midway through each fiscal year, a Council Study Session is held that identifies factors in the City's current environment and in the near-term that could impact our fiscal security. This year, the Study Session was held on January 31, 2005. The purpose of the Study Session was to:

- Provide Council with an update on the City's current financial condition, including revenue and expenditure patterns and give an economic forecast for the State in general and Silicon Valley in particular
- Identify the possible effect of the proposed FY 2005/2006 State budget on Sunnyvale
- Provide a status of the Fiscal Strategies identified in the City's FY 2004/2005 Budget
- Identify and briefly discuss three potential issues that may have a budgetary impact on the City over the near term
- Receive from Council issues, questions, and initial policy direction that will need to be incorporated into the annual budget.

Below are discussions of the major areas covered in the Fiscal Issues Study Session.

CURRENT ECONOMIC CONDITIONS AND OUTLOOK

The steep economic downturn that has so severely impacted the City's fiscal condition over the last several years appears to have given way to a moderate recovery, led by gains in consumer spending, large increases in business investment, and expanding exports. While economic growth is projected to continue into next year, the growth may slow somewhat. Further, there are a number of downside risks that could pose serious threats to the economy and its recovery.

The economic recovery in the Bay Area lagged significantly behind the state and nation, and employment in our region has not recovered. The California recession beginning in 2000 was concentrated in the Bay Area, which lost almost half a million jobs. However, the pace of job loss here appears to have slowed and there are indications that employment may be leveling out. Sales in the Bay Area also began to rise in the third quarter of 2003; prior to that time, our region suffered nine consecutive quarters of year-over-year declines. This recovery is currently reflected in a modest increase in Sunnyvale's receipts of Sales Tax and Transient Occupancy Tax so far this year.

National Economy

The national economy experienced solid economic growth in 2004. Gross domestic product (GDP), the measure of total goods and services production in the country, experienced an annual 4.4% growth rate in 2004.

Current economic projections are that the U.S. economy will expand at a solid though moderating pace in 2005, with economic growth as measured by the GDP slowing to approximately 3% in 2005 and accelerating modestly in 2006. Forecasts assume that business investment will continue to increase but the growth in consumer spending will slow.

Since the collapse from the euphoric "dot.com" era, consumer spending and residential investment have been the predominant drivers of the nation's economy. Consumer spending, which has fueled about two-thirds of U.S. economic activity since the downturn, has been buoyed by low interest rates. Since the beginning of the economic downturn in 2001, the Federal Reserve has reduced interest rates to stimulate investment and increasing spending. Consumers took advantage of historically low mortgage rates to either enter the real estate market or to refinance existing loans and use the funds for discretionary spending. However, the Federal Reserve has increased its short-term interest rate, the federal funds rate, eight times since June 2004 to 3% and signaled that it will keep raising this benchmark rate in the coming months to prevent inflation from increasing. Meanwhile, higher energy costs are leaving consumers with less money to spend on other good and services. The current increases in interest rates and increases in energy prices are forecast to have a dampening effect on consumer spending in the coming months..

Another important element of the current recovery is business investment. The continued rebound in business investment played a big role in the strong expansion of the national economy in 2004, with business investment nearly 14% higher in the first three quarters than in the corresponding quarters of 2003. In order to sustain future growth, business investment will have to increase to offset the potential decreases in consumer spending. However, just as there are impediments to sustained consumer spending, there are a variety of different factors that may hinder future growth in business investment for 2005. First, certain favorable tax provisions have recently expired. Second, due to higher energy costs and rising employee benefit costs, businesses are hesitant to make new commitments.

Finally, macro-economic issues such as geo-political uncertainties, the Nation's increasing trade deficit, and the growing federal budget deficit all represent risks to future economic growth over the later years of the planning period.

The California Economy

The California economy strengthened along with the national economy in 2004. Factors boosting economic growth over the past year have included the strong national rebound in business investment, the state's booming housing market, and a sharp increase in international exports.

Economists project that California's economic growth will continue in 2005, although at a more moderate pace than in 2004. On the positive side, the national outlook for continued strong business investment will boost manufacturing and technology in the state. However, the same negative forces that will have a dampening impact on the national economy, such as high energy costs and rising interest rates, will effect consumer spending and housing activity in the state.

The Bay Area Economy

While both the national and state economies appear to have stabilized in 2004, economic growth in the Bay Area continues to be sluggish, particularly in the Silicon Valley. Evidence in the form of our own Sales Tax and Transient Occupancy Tax receipts seems to indicate that our area reached the bottom and began a slow recovery in the third quarter of 2004. However, employment and the commercial real estate market still remain extremely problematic. The recovery in the Bay Area continues to be, in large measure, a "jobless recovery."

The Silicon Valley also continues to be plagued by extremely high vacancy rates in commercial and industrial properties. Recent estimates are that there is over 50 million square feet of office and research and development available for lease in the Silicon Valley. With an abundance of vacant space, businesses have sought to both upgrade their office locations and take advantage of reduced lease rates. The net result of these moves is to increase the vacancy in the "less desirable" office space. As an example of this trend, there have been recent reports of major investment in Sunnyvale corporate office buildings. The April 15, 2005 Silicon Valley Business Journal cites two large properties in the North Mathilda Avenue corridor in the Moffett Park district which have generated sales in excess of $400 per square foot. The same article reaffirms the fact that investors are pursuing top-quality offices while Class B and Class C buildings continue to struggle with considerable vacant offices that will not be quickly absorbed.

Consensus among economists is that our Bay Area economy will grow, but big problems remain for the region and the state. Challenges include the country and the state slipping deeply into debt, as well as the need for more funds for health care, education, and infrastructure.

Staff has taken the condition of the state and regional economy into consideration in preparing the recommended FY 2005/2006 Budget and long term projections for Council's consideration.

PROPOSED FY 2005/2006 STATE BUDGET

The Governor's Proposed FY 2005/2006 Budget issued in January contains program savings in the amount of $7.4 billion and the use of $1.7 billion in remaining deficit reduction bonds to close a projected budget gap of $8.6 billion and fund a reserve of $500 million. The major program savings occur in the areas of Proposition 98 Education (K-12 and community college education), Transportation, Health and Social

Services, Employee Compensation, and Mandated costs. Two of these areas, Transportation and Mandated Costs, will have fiscal effects on Sunnyvale.

First, in the area of transportation, the Budget proposed to suspend Proposition 42, the Transportation Congestion Improvement Act. Payments for FY 2003/2004 and FY 2004/2005 have already been deferred in prior budgets. Under the January proposal, the funds for FY 2005/2006 and FY 2006/2007 would again be suspended but would begin flowing to cities in FY 2007/2008 and beyond. Further, the Governor proposed to amend Proposition 42 to prohibit any suspension after FY 2006/2007. Staff has estimated that the total amount to be deferred over the four year period is about $2 million, and the budget proposes to repay this amount over 15 years beginning in FY 2007/2008 with no interest. This is different from the provisions of current law, which call for the suspended Proposition 42 amounts to be repaid plus interest by FY 2007/2008 and FY 2008/2009.

It should be noted that the Governor announced on May 12 that he intends to restore full funding for Proposition 42 in FY 2005/2006 due to an improved State revenue picture. If this proposal is ultimately approved by the Legislature, staff will program these funds into the City's adopted FY 2005/2006 Budget for Pavement Operations.

The second area of particular interest to Sunnyvale is mandates. The Budget would suspend most mandates on local programs for FY 2005/2006, with the suspended mandates repaid over a 15 year period, rather than the five year period that was contemplated in last year's budget agreement. These repayments would begin in FY 2006/2007. It is estimated that the total amount of mandated costs suspended to be repaid for Sunnyvale would be $500,000 for an annual repayment of $33,333.

The Governor's proposed FY 2005/2006 Budget reflects last year's budget agreement that resulted in the passage of Proposition 1A. Local governments will again contribute shifts in Property Tax to the Educational Revenue Augmentation Fund (ERAF) in the amounts previously agreed upon. This results in Sunnyvale losing $2.05 million in General Fund Property Tax and $269,398 in Redevelopment Tax Increment again in FY 2005/2006. These amounts were anticipated in our Long Term Financial Plans last year.

Other elements of the proposed Budget that have an impact on Sunnyvale include the anticipated elimination of the booking fee reimbursement, which has a net cost to us of $90,000. Supplemental Law Enforcement funding is maintained in the Proposed Budget at the existing level, which for Sunnyvale is about $193,000.

While the Governor's proposed FY 2005/2006 Budget is balanced for FY 2005/2006, the State will continue to experience a structural budget imbalance in future years absent ongoing corrective actions. The Budget therefore contemplates a number of reforms to the State's budgeting process, pensions, transportation funding, and Proposition 98 funding. The Governor has indicated that he will take constitutional amendments to the voters in the absence of legislative action on these issues. As of April, the Governor decided to not go forward with his constitutional amendment on pension reform for public employees, but indicated that he would bring it back as early as June 2006 absent corrective action at the legislative level. More discussion of this issue is contained later in the section on *Pension Reform*.

Other Budgetary Impacts for Cities in May Revise

On May 13, 2005 the Governor will release his May Budget Revision (the "May Revise"). This document updates the underlying revenue assumptions based on tax receipts as of April and contains any changes or "deals" made in the time since July. As was previously noted, the Governor has announced that he will be recommending full funding for the Traffic Congestion Relief Program (Proposition 42) in his revised budget. Staff will be reviewing the May Revise as soon as it is released and will brief Council on its contents and how it impacts our financial condition at the Budget Workshop.

LOCAL ISSUES IMPACTING THE CITY'S FINANCIAL CONDITION

At the Future Fiscal Issues Study Session in January, three current issues in addition to the items mentioned above were identified that may have a significant effect on the City's financial condition now and in the future. These issues are briefly described below and will also be discussed in later portions of this Letter of Transmittal.

Downtown Redevelopment

Although impeded by a number of developer–induced delays over the past year, the redevelopment of Town Center Mall now appears to be on track for construction (beginning with demolition) to commence this summer and for the retail portion of the project to open in the Fall of 2007. Macy's and Target will remain open throughout the construction period.

The Forum Development Group will completely redevelop the closed Town Center Mall into an open air shopping, office, and retail center and restore major portions of the original street grid. In addition to the existing Macy's and Target, Forum proposes to build 570,000 square feet of new shops, 275,000 square feet of office space, and 292 for-sale housing units. Once completed, the redevelopment of the Town Center Mall will protect existing revenue streams at the site and will result in increased Sales Taxes and Property Taxes.

The completed project is estimated to generate approximately $2 million per year in new Sales Tax for the City's General Fund. It is currently estimated that future costs for increased service demands related to the Mall development may total about $1 million. For purposes of our General Fund Long Term Financial Plan, we have included the increased Sales Tax revenue of $2 million net of these estimated costs. In FY 2007/2008 we are anticipating about half of the net revenue. Then, $1 million in Sales Tax net of the new costs is reflected beginning in FY 2008/2009 and forward, increasing by inflation.

The completed project should generate about $4 million per year in increased Property Taxes (tax increment payments) to the Redevelopment Agency. The Agency has agreed to return to the developer up to $4,050,000 per year, plus 50% of any tax receipts

above this amount, in return for the developer assuming all of the Agency's responsibility for providing parking for the project, constructing and maintaining all public streets and sidewalks, and placing at least 1,442 parking spaces underground.

The project will also pay major one-time fees as follows: construction tax of approximately $450,000; $1.5 million for construction plan check and inspection services; Traffic Impact Fees of $1.5 million; Park Dedication Fees of $1.5 million; and utility connection fees of $1.4 million.

The final piece of Downtown redevelopment will be the reconstruction of the Town and Country Shopping Center, which has not yet been included either in the Redevelopment Agency or General Fund Financial Plans because the scope of the project and the timing is not yet known.

Proposals for Pension Reform

Governor Schwarzenegger's proposed FY 2005/2006 State Budget includes the issue of pension reform as one of his major proposals for structural reform. To combat the State's rising retirement costs, the Governor proposed to bargain with employee unions to equalize the employee and employer share of the annual contribution to CalPERS as labor contracts come due. Further, in order to achieve overall pension reform, the Governor proposed a constitutional amendment that prohibits the State or any of its political subdivisions, including cities, from offering defined benefit retirement plans to new employees. In April, following concerns about certain provisions of the proposed amendment which would have a negative impact on public safety death and disability retirements, the Governor withdrew his support for the constitutional amendment to change public pensions from defined benefit to defined contribution and vowed to work with public agencies to effect positive changes to public retirement systems. He has indicated that he will be focusing on smoothing contribution rates, establishing a form of "rainy day fund" to offset rate increases, and limiting abuse in the disability retirement system.

At the national level, the social security reform package recommended by President Bush includes a suggestion that all government employees be covered by social security to offset some of the costs of the proposed provisions. Sunnyvale employees are currently not enrolled in social security, but are only in the California Public Employees Retirement System (CalPERS).

Each of the proposed pension reform plans mentioned above would have a long-term financial impact on Sunnyvale. In the case of the constitutional amendments which limit retirement plans or the City's portion of the cost, there would presumably be a substantial savings beginning in the later years of the Long Term Financial Plan. If mandatory social security were to be implemented for the City, our personnel costs would increase over the entire life of the Financial Plan depending upon how the social security interrelated with our CalPERS contract.

Threats to Telecommunications Taxes

Within the last several years, a complex array of technological advances has been emerging in the areas of data transmission, Internet access, telecommunications and video (cable) services. The convergence of these industries, each with disparate, multi-level governmental frameworks for taxation purposes, has blurred the lines between what is taxable/non-taxable, and has necessitated regulatory change that could have far-reaching negative implications for California cities. Depending upon the outcome of anticipated tax reforms, Sunnyvale could see an erosion of revenues associated with cable and telephone services, and even a loss of local control over cable franchise requirements.

Central to the debate are attempts by the telecommunications and cable industries to incorporate sweeping changes to a full range of local taxes and fees, including but not limited to Utility Users Tax, Franchise Fees, Sales Tax and 911 Fees and Surcharges.

Sunnyvale receives approximately $1.6 million annually in Utility Users Tax from telephone providers and approximately $900,000 in Franchise Fees from cable services. Any major erosion of these revenues as a result of changes in federal or state taxation laws would have a significant negative effect on the General Fund. As Sunnyvale is compensated for the cable provider's use of city-owned rights-of-way and also regulates certain cable services through a negotiated Franchise Agreement, any significant changes to federal law governing local franchising authority could put local control at risk.

FISCAL STRATEGIES

One of the most powerful aspects of multi-year budgeting and projection is the ability to plan for the future. Small changes made now can avert large problems later. As the City addresses the fiscal issues and challenges identified in the previous section, it is clear that a number of different strategies must be undertaken to help us deal with the structural imbalance between revenues and expenditures that has developed in our Long-Term Financial Plan.

A number of fiscal strategies were identified in last year's budget to position the City well to address the current imbalance so that quality services can be sustained in the years to come. These items generally fell into two categories: General Philosophies and Strategies. The General Philosophies reflected were as follows:

- **Ensure that we are good stewards of the City's infrastructure assets**
- **Don't sacrifice safety or quality of life**
- **Support diversity in all areas of the community**
- **Build and emphasize the connection between the community and business**
- **Support a quality work force**
- **Emphasize and build on the unique culture of Sunnyvale**
- **Stick to the knitting, focusing on issues that can make a difference**

To support these philosophies, a number of strategies and action items were identified to be explored during the coming year. Some of these were Citywide, while others related to a particular department or expenditure area. During the course of this fiscal year staff was reviewing and analyzing many of these ideas and good progress has been made on a number of them. The results of our efforts were reported to the Council during the Fiscal Issues Workshop and as part of the regular City Manager Informal Evaluation sessions. *Appendix A* of this Transmittal Letter contains an update on each item.

As staff was addressing the strategies that had been identified, it became clear that they fell into certain topic areas. Below are the major themes identified, the strategies that support these themes, and some action items that have been or will be employed in these areas:

Don't Make Matters Worse: This strategy speaks to our emphasis on Demand Management and Long-Term Planning. Action items in this area include:

- Pay close attention to the financial impact of policy decisions made throughout the year
- Think strategically by emphasizing the multi-year effects of key decisions
- Manage the City's "Life Style" so that we can live within our means

Continue to Emphasize Efficiency of Operations: This strategy speaks to Sunnyvale's long established emphasis on continuous improvement. Action items for this strategy are:

- Use cost-effective technologies to increase productivity, enhance customer service and/or reduce the cost of service
- Leverage and partner with community groups, non-profit organizations, and where appropriate the private sector to maintain services and lower costs
- Explore alternative service delivery methods including contracting out
- Work with employee associations to identify ways to more effectively utilize City resources
- Evaluate most effective and efficient organization structure to deliver services
- Manage/contain personnel costs
- Reduce or eliminate reserves that are not needed for prudent financial management

As noted earlier, staff has done a great deal of work this fiscal year on various action items related to these strategies, and these actions have had a positive impact on the City's financial condition. Nonetheless, if Council and staff are successful in the areas listed above and a structural imbalance in the City's budget still remains, two other major strategies will need to be considered. These are:

Investigate new and increased revenue sources: This strategy includes the City's existing taxes and fees and any opportunities for new taxes and fees to add to our ongoing revenue base. Action items in this area include:

- Review existing fees to ensure that full cost of the service is being recovered
- Evaluate the current level of the City's existing taxes for opportunities where our taxes are below the area norm
- Identify any new taxes or fees that might be appropriate to consider implementing

Reduce or eliminate services or modify service levels: This strategy focuses on adjusting the City's services and service levels to preserve essential core service but establish the most appropriate level for our fiscal circumstances. The service level review process that Council undertook in preparing the FY 2004/2005 Budget utilized this approach in prioritizing the City's services. As a result of the review, certain services or service levels were identified for potential reduction or modification. Actual implementation of these service reductions was deferred during FY 2004/2005 to allow time to more fully evaluate the City's long term financial position.

It is recommended that Council and staff continue to focus on these policies and strategies that will help the City close its structural imbalance and become a more effective, high performing organization. The updated list of strategies identified last year is shown in *Appendix A* of this Transmittal Letter.

MAJOR PROJECT EFFORTS

Sunnyvale's projects budget is a complex document involving four separate and distinct categories of projects: capital, infrastructure, special, and outside group funding. The projects themselves are budgeted and accounted for in various funds, most notably the General and Gas Tax Funds, the Capital Projects and Infrastructure Funds, and the Utility Funds.

Major initiatives and actions have added to this complexity. For example, the City's remarkable infrastructure planning and funding efforts led to the creation of long-term projects to fund major renovation and replacement efforts. The City's debt financing strategies are also reflected in this area.

Additionally, the past few years have seen a marked increase in various grants and special funding sources available for specific project categories, such as parks and streets and transportation. These revenue streams include the Santa Clara County half-cent Sales Tax for transportation (Measure B), Traffic Mitigation Fees and Traffic Impact Fees, State Park Grants (Proposition 12 and Proposition 40), and Park Dedication Fees. Unfortunately, with the State budget crisis the new transportation funding from the State has been put at risk. More discussion on this issue is contained in the section on *Traffic and Transportation Funding* below.

Along with the new initiatives and funding opportunities, the City also has a number of challenges in the projects area. As was discussed earlier, a major inventory of all funded and unfunded capital and special projects was undertaken in FY 2004/2005. This effort, led by the Public Works Department, identified approximately $200 million in unfunded projects over the ten-year Capital Improvement Plan. Building on this work, a major focus for this year's capital project process was to review our capital and infrastructure programs and revise the estimates as needed. This infrastructure effort is still underway and the full impact of the study will be included in the FY 2006/2007 Budget.

Staff also focused during this year's budget process to refine the unfunded projects inventory that was begun last year. This work has resulted in a full 20-year inventory of the City's unfunded projects. $49 million has been identified in the first ten years and $395 million in the second ten years, for a total of $444 million over the entire planning period.

The recommended FY 2005/2006 Budget includes funding for a total of 344 projects in all categories over the Ten-Year Plan. This section discusses some of the special funding sources and provides information on the status of major project initiatives. Highlights of recommended projects for each fund are included in the *Detailed Fund Review* section of this Transmittal Letter.

SPECIAL PARKS FUNDING

Proposition 12 Funds

The passage of the Safe Neighborhood Parks, Clean Water, Clean Air and Coastal Protection Bond Act of 2000 (Proposition 12) provided funds to cities on a per capital basis to be used for various local park and recreational lands and facilities. The City has already programmed about $1.3 million of these funds for a variety of park improvements through FY 2004/2005. The City is expected to receive an additional $406,581 in Proposition 12 grant monies in FY 2005/2006. $210,661 of these funds have been appropriated for the Park Buildings Rehabilitation project and $157,600 has been planned for the Playground Equipment Replacement project in the Infrastructure Fund. The remaining balance of the Proposition 12 allocation has not yet been programmed.

Proposition 40 Funds

The passage of a second bond measure under the California Clean Water, Clean Air, Safe Neighborhood Parks and Coastal Protection Act of 2002 (Proposition 40) made available to the City an additional $943,604 for park and open space projects beginning in FY 2003/2004. Council appropriated these monies to be used for the Plaza Del Sol project in downtown. Phase I of this project is now complete.

Park Dedication Fees

When developers of multi-family housing do not dedicate land for use as parks, the City collects a fee in lieu of the land dedication. These Park Dedication Fees are then used to pay for park facilities. These fees recently helped to pay for the Fair Oaks Skateboard Park and the Plaza del Sol in downtown Sunnyvale, and $500,000 of Park Dedication fees are programmed in FY 2004/2005 for the Sunnyvale Historical Museum.

The City is currently experiencing a marked increase in new housing developments that are subject to paying Park Dedication Fees, and an additional $10 million in fees are projected to be received over the next three years. The recommended FY 2005/2006 Budget proposes to use these anticipated fees to fund all park-related infrastructure projects in the 20-year planning period through a transfer to the Infrastructure Rehabilitation and Replacement Fund, thereby relieving the Community Recreation Fund and the General Fund of these essential expenses. Major infrastructure projects to be funded in the Twenty-Year Plan include replacement of the Community Center Building Roofs, Washington Pool Renovation, Golf Course Greens Renewal, Rehabilitation of Parks Buildings, and Golf Course Tee Grounds Renewal. In keeping with our long-term approach, we have also added a new project for routine rehabilitation of the just-completed Senior Center Buildings at the end of the twenty-year cycle.

Additionally, there are two new park projects recommended to be funded with Park

Dedication Funds in the first ten years of the Long Term Financial Plan. The first is $2.6 million for phase II of the Plaza del Sol, which is programmed in FY 2011/2012 and FY 2012/2013. The second is a Park Land Acquisition project in the amount of $1 million in FY 2007/2008.

More detail on the Park Dedication Fund can be found in this Transmittal Letter in the *Detailed Fund Reviews.*

TRAFFIC AND TRANSPORTATION FUNDING

State Traffic Congestion Relief Program and Proposition 42

The State Traffic Congestion Relief Program (TCRP) was passed as AB 2928 as part of the State's FY 2000/2001 Budget. Under this legislation, approximately $1 billion from the State portion of Sales Tax on gasoline sales was slated to go directly to cities and counties for preservation, maintenance and rehabilitation of local street and road systems for the period FY 2000/2001 through FY 2005/2006. These new funds were allocated on a per capita formula. AB 2928 funds impose a maintenance of effort requirement that obligates the City to maintain a level of expenditures for street, road, and highway purposes equivalent to the average expenditures for FY 1996/1997, FY 1997/1998 and FY 1998/1999. In addition, a "use it or lose it" provision requires that the City expend these funds by June 30th of the fiscal year following the one in which they were received. The legislation also requires that the monies be held and accounted for in the City's Gas Tax Fund.

When the legislation was first passed, it was projected that the City would receive approximately $3 million under AB 2928. In October 2000 the City received funds in the amount of $949,530 representing the first disbursement of AB 2928 monies for FY 2000/2001. AB 2928 funds in the amount of $333,586 were received in FY 2001/2002 and $345,684 was received in FY 2002/2003. All of these funds were appropriated and spent through FY 2003/2004 for a variety of traffic signals and other traffic improvements.

In March 2002, a constitutional amendment that permanently shifts the Sales Tax on gasoline from the State General Fund to the Transportation Investment Fund created by AB 2928 was approved by the voters as Proposition 42. The effect of this action was to indefinitely extend the allocation of Traffic Congestion Relief Program funds to cities, counties, and transit agencies beginning in FY 2008/2009.

Due to the ongoing State budget crisis, Traffic Congestion Relief Fund payments to cities were suspended beginning in FY 2003/2004 and again in FY 2004/2005. The Governor's proposed State budget for FY 2005/2006 issued in January assumed that these payments would be deferred again for the next two years. The total amount of deferred TCRP payments owed to the City of Sunnyvale would then be as follows:

Fiscal Year	Amount
2003/2004	$424,777
2004/2005	$399,083
2005/2006	$560,933
2006/2007	$600,000*
Total due	**$1,984,793**

*staff estimate

The January State Budget proposal also reflected a commitment to restore the dedication of Traffic Congestion Relief Funds to transportation, including repayment of the deferred amounts over a fifteen-year period (without interest) and constitutionally prohibiting any Proposition 42 suspensions after FY 2006/2007. The Long Term Financial Plan for the Traffic Congestion Relief Fund reflects the repayment of the deferred amounts beginning in FY 2007/2008 and receipt of Proposition 42 monies beginning in the same year. The Plan also assumes that these monies will be used for Public Works Pavement Maintenance operations on an ongoing basis.

Subsequent to preparation of our recommended FY 2005/2006 Budget the Governor announced that as part of his May Revised Budget he would be restoring Proposition 42 funds effective next fiscal year. If this proposal is approved by the Legislature, staff will reflect this change as part of the adopted budget.

Traffic Mitigation Fees and Traffic Impact Fees

The City Council has adopted a Transportation Strategic Program as part of the Revenue Sources for Major Transportation Capital Improvement Projects Study Issue. The Transportation Strategic Program establishes a comprehensive funding program of revenue sources for major transportation necessary to support the City's land use plans.

Prior to the adoption of the Transportation Strategic Program, an interim funding mechanism was implemented for transportation mitigation of major land development. Known as the Cumulative Traffic Mitigation Fee, this mechanism mitigates project-specific cumulative impacts of major approved land developments as they relate to the Land Use and Transportation Element of the General Plan, and offsets the potential revenue loss that would have resulted if the City waited until the Transportation Strategic Program was completed before implementing a fee or assessment. Cumulative mitigation funds are applied to capital projects that improve traffic capacity or alternative transportation facilities. Funds are allocated to projects of local or regional significance, depending upon the nature of traffic impacts identified in association with the land development.

The recommended FY 2005/2006 Budget includes approximately $5.5 million in projects to be funded by Traffic Mitigation Fees between FY 2005/2006 and FY 2014/2015. A new Future Traffic Signal Construction/Modification project is proposed that will fund one new traffic signal installation or major modification every other year, starting in FY 2006/2007. A project for engineering and environmental analysis for the Mary Avenue Extension is also proposed beginning in FY 2005/2006 in this fund.

Additionally, a transfer from the Traffic Mitigation Fund to the Capital Projects Fund in the amount of $1.6 million is included in the recommended FY 2005/2006 Budget for three projects. These include transfers for Washington Avenue and Mathilda Avenue Intersection Improvements ($948,000), the Borregas Avenue Bicycle Corridor ($492,000), and a Transportation Grant Matching Funds project ($165,000).

The City Council adopted the Transportation Strategic Program on November 11, 2003 and instituted a new Traffic Impact Fee to be applied to traffic-generating development citywide. This Traffic Impact Fee replaced the interim Cumulative Traffic Mitigation Fee. The City began collecting Traffic Impact Fees on new developments on January 1, 2004.

Approximately $3.4 million of these Traffic Impact Fees are programmed for two capital projects for the first ten years of the Long Term Financial Plan, and $15.1 million in the second ten years. The first, and smaller project, is the Transportation Model Update, which provides $50,000 to update to the City's computerized transportation model every five years starting FY 2005/2006. The second project, Transportation Strategic Program, represents all projects that were identified in this program as approved by the Council in November 2003. This project is intended to implement projects identified in the Land Use and Transportation Element of the General Plan. Implementation of the transportation projects is expected to begin in FY 2010/2011 when sufficient Traffic Impact Fee revenues are accumulated.

These funds are accounted for in the Traffic Mitigation Fees and Traffic Impact Fees Sub-funds of the Capital Projects Fund. More detail on the Traffic Mitigation and Traffic Impact Funds can be found in this Transmittal Letter in the *Detailed Fund Reviews* section.

MAJOR PROJECTS IN RECOMMENDED FY 2005/2006 BUDGET

Mathilda Avenue Railroad Overpass Replacement and Reconfiguration

The State of California Department of Transportation (Caltrans) inspects bridges throughout the state every other year for structural adequacy and functional operation. They have been doing this bi-annual inspection for many years and the reports are given to the City to address any corrective action that is documented. These reports are used as the basis for the City's maintenance efforts on bridges and included as part of the overall infrastructure management program.

As per the latest Caltrans inspection report, the current Mathilda Avenue Railroad Overpass bridge design does not meet bridge pier clearance standards, deceleration lane design standards, shoulder width standards, and bridge railing standards. These deficiencies create potential hazards to the public, and present a potential liability issue for the City.

City staff has successfully secured federal funds with 20% local match for removing the deficiencies and improving traffic circulation on the bridge. The proposed bridge improvements include reconfiguring the off ramp to Evelyn Avenue to allow full access

to Evelyn from southbound Mathilda Avenue. As an added benefit, this improvement can service the anticipated increase in traffic from southbound Mathilda Avenue to downtown Sunnyvale.

A conceptual layout of the improvement proposal with a preliminary cost estimate of $17.5 million for the project has been submitted to Caltrans for funding purposes. The requirement of 20% local match translates to a maximum federal share of $14 million with the City's share of $3.5 million. However, Caltrans has indicated to City staff that a limit of $10 million of Federal Highway Bridge Rehabilitation and Replacement funding is placed on this project at this time. This would require the City to commit to a match of $7.5 million, while only $3.5 million is currently budgeted. This would leave a funding shortfall of $4 million. Caltrans has also indicated to City staff that increased funding requests are considered on a case by case basis upon completion of project design. City staff is continuing to work with Caltrans to increase funding. If this additional outside funding is not forthcoming, staff would not recommend that the project go forward in its current form.

The recommended FY 2005/2006 Budget includes the Mathilda Avenue Railroad Overpass project unchanged at the $17.5 million project cost. As design work and negotiations with Caltrans continue, this project estimate will be modified to reflect the actual funding level and funding sources. As indicated above, additional City funds may be needed to fully construct this project. The project is currently undergoing environmental review. The level of environmental review is likely to be greater than originally anticipated in the project scope, which will delay the project and potentially increase cost.

Borregas Avenue Bicycle Corridor

This project involves the design and construction of new bicycle and pedestrian bridges on Borregas Avenue over US 101 and State Route 237. The construction of overcrossings will eliminate approximately two miles of detours that currently exist for bicyclists and pedestrians who wish to cross over the freeways. The total project cost is $6.5 million, funded by various grants from the Valley Transportation Authority (VTA) in the amount of $4.8 million, a Transportation Development Act grant of $400,000 and Traffic Mitigation Funds of $1.3 million.

The project is currently in the design and environmental clearance phase. Obtaining the necessary approvals from Caltrans for structures across two freeways has delayed the project due to lengthy Caltrans review times and staffing turnover at Caltrans. Design completion is scheduled for October 2006 and construction will take approximately two years.

It is possible that the project would require additional funding because material costs for concrete and steel have risen sharply due to increasing demand. Additional funding may be available from the VTA on an 80%/20% matching basis. As design work and negotiations with the VTA continue, this project estimate will be modified to reflect the actual funding level and funding sources.

Mathilda/237 Area Transportation Improvements/Mary Avenue Extension

The Mary Avenue Extension is a project to improve access to the Moffett Industrial Park north of State Route 237. The project extends Mary Avenue from its current terminous at Almanor Avenue over US 101 and State Route 237 and connects to the roadway network in and around the Lockheed Plant 1 area. This project has been in the planning stages since the late 1980s and was included in the General Plan when the Land Use and Transportation Element was revised in 1997. The project is a major element of the City's long-range Transportation Strategic Program.

In 2004 the City and the VTA completed an operations analysis of the Mathilda/237 area, including an updated examination of the Mary Avenue Extension. This study identified a Mathilda/237/101 freeway interchange reconfiguration project and the Mary Avenue Extension as a viable medium to long-range improvement to serve the City's north-south travel corridors and to support projected growth in the Moffett Industrial Park. As a result, these projects were included as priorities for outside funding in the Valley Transportation Plan 2030 regional plan for Santa Clara County. To continue transportation and land use planning and to facilitate future outside federal or state funding for these projects, the recommended FY 2005/2006 Budget includes a project to conduct conceptual engineering, environmental work, and Caltrans-required studies for these improvements. The intended outcome is the establishment of a plan line for the Mary Avenue Extension, program-level environmental clearance, and initial Caltrans approval of these projects. This work may be done in partnership with the Valley Transportation Authority.

Radar Speed Signs

In FY 2004/2005 the City completed a successful trial installation of semi-permanently mounted radar speed signs near critical facilities such as schools. This installation, funded with a State Office of Traffic Safety grant and City operating funds, demonstrated the efficacy of these signs at reducing travel speeds and garnered positive feedback from the public. As a result, the recommended FY 2005/2006 Budget includes a project to install 20 additional radar signs on collector and arterial streets near schools or other pedestrian traffic generators throughout the City at a cost of $200,000.

Capital Projects Planning and Unfunded Projects

In early 2004 the City Manager asked the Public Works Department to update the ten-year Capital Improvement Program (CIP). The purpose of this effort was to take a comprehensive look at both Capital Projects and Special Projects so that the City's future unfunded liabilities could be identified. Earlier versions of the CIP did not paint a complete picture because they incorporated only those projects for which funding had already been secured.

This update of the CIP required the City to assess its known future obligations and to identify new projects, both funded and unfunded. Some of these projects had been previously identified but had not been included in the ten-year CIP due to funding

constraints. Other projects had not been listed in the CIP because, while the obligation was known, the timing and scope of the project could not be easily defined. The update of the CIP was intended to include all projects even when funding was not yet identified or the final scope was indeterminate so that future obligations could be better projected.

The FY 2005/2006 CIP has updated and expanded last year's effort to also include projects that are anticipated in the second ten years of the City's Financial Plan. This effort was particularly beneficial in the case of utility infrastructure projects because it allowed utility rates to be projected based on a realistic assessment of what future capital funding needs were likely to be.

The complete list of unfunded projects that was developed by this effort is shown in this budget document in *Volume II Projects Budget* in the section titled *Unfunded Projects.* As indicated above, many of these costs are very rough estimates and are meant to portray a rough order of magnitude only. The total of these unfunded projects, approximately $444 million over the twenty-year period, represents a very significant potential unfunded liability of the City.

INFRASTRUCTURE RENOVATION AND REPLACEMENT

Sunnyvale has traditionally provided funding in its operating budgets for optimizing maintenance of City infrastructure. Staff believes this to be the most cost-effective, long-term way to approach asset management.

Nonetheless, even with this proactive maintenance approach, eventually every infrastructure element reaches a point where maintenance is no longer a cost-effective strategy, and significant renovation and replacement is required. Funding of the renovation and replacement of the City's estimated $1 billion in infrastructure assets is an enormous challenge, but it is critical to the long-term quality of life and financial condition of the City. The City has taken action on several fronts to deal with this challenge.

The City began development of a Long Range Infrastructure Plan (LRIP) several years ago. Phase I of the LRIP established the Infrastructure Renovation and Replacement Fund and incorporated full funding for the General/Gas Tax and Community Recreation Fund assets. The original assumptions included in Phase I now need to be reviewed and updated, and this work is underway. Phase II of the LRIP addresses fixed assets within the utility funds. Staff has been identifying and inventorying utility-related fixed assets and the recommended FY 2005/2006 Budget includes preliminary estimates for replacement costs and schedules.

The Water and Wastewater Funds have a large number of varied assets, including water mains, water valves, reservoirs, sewer collection systems, storm drains and the Water Pollution Control Plant. In order to provide more realistic estimates, staff has been collecting data on how these fixed assets perform in varied conditions. The Water Pollution Control Plant has also undertaken an engineering study to inventory, assess remaining useful life/failure potential, and identify the replacement cost for all Plant infrastructure. This work is expected to be completed in late 2005.

In the interim, the update of Phase I and the development of Phase II of the LRIP are ongoing. The work being done is, of necessity, a broad based approach that looks at categories of assets, their replacement costs and the annualized costs to upgrade or replace those assets over the next 40 years. It is expected that Public Works staff will complete this work effort the first part of FY 2005/2006 and more complete project descriptions and costs will be included in the budget for FY 2006/2007.

The recommended FY 2005/2006 Budget includes Infrastructure projects totaling $27.5 million for the Water Supply and Distribution Fund and $65.3 million for the Wastewater Management Fund over the twenty-year planning period.

INFORMATION TECHNOLOGY INVESTMENT FUND

The Department of Information Technology provides significant support in the selection, implementation and ongoing maintenance of major technology applications. This support was restricted as a result of substantial budget and resource reductions that were implemented in FY 2003/2004. Information Technology staff have focused their limited resources on major planned technology initiatives, such as the replacement of the City's Library and Payroll Systems, along with the provision of day-to-day support of existing mission critical software applications.

In response to similar funding reductions, other City departments attempted to identify technology solutions for streamlining their operations. This placed an additional demand on the Department of Information Technology for programming and project management that could not be met with existing funding and staffing levels. This has resulted in a delay in valuable technology projects.

To address this technology "gap", staff developed the concept of a flexible technology funding mechanism, called the Information Technology Investment Fund, to finance process improvement technology. This Fund has been established as a special project in the recommended FY 2005/2006 Budget.

Staff developed a systematic methodology to select projects that are eligible for process improvement through the use of technology. Each year, departments will be asked to prepare a business case that identifies the Value on Investment (VOI) for each proposed project based on the following criteria:

- Is required by legislation,
- Will enhance the protection of life and safety,
- Will result in process streamlining,
- Will aid in cost containment, and/or
- Will increase revenue.

While the administration and oversight of this Fund will be the responsibility of the Director of Information Technology, proposed initiatives will be systematically and objectively evaluated by an Information Technology Investment Fund committee. This committee will consist of a cross-departmental team of staff members, each bringing a unique perspective to the selection process.

Once the initiatives have been selected, the Information Technology Investment Fund will be used to procure software/hardware, development services, implementation services or project management services to address the technology need.

Staff has identified an initial appropriation of $285,076 to meet the short-term needs of the organization. This funding is available in the Information Technology Replacement Fund's reserves as the result of unanticipated expenditure savings realized in FY 2003/2004. It is our expectation that this funding source will be replenished through the capture of cost savings associated with the new technology, or with one time operating savings that will be contributed by each department benefiting from the approved project.

OUTSIDE GROUP FUNDING

Sunnyvale recognizes the need for human services and, within the limits of funding available for such activities, supports those services deemed necessary in the community that leverage resources and extend services for Sunnyvale citizens. Some Human services agencies in the City receive funding using the federal Community Development Block Grant program (CDBG) with additional support provided by the General Fund. CDBG support is limited by federal regulation to 15% of the City's total CDBG allocation plus program income. On January 31, 2005 the City Council approved a cap of $100,000 of General Funds to support human service agencies for FY 2005/2006.

Appendix C of this Transmittal Letter presents the recommended Outside Group Funding for FY 2005/2006. On May 20, 2005 Council approved the distribution of $350,000 of CDBG funds as shown. The recommended FY 2005/2006 Budget proposes $97,458 in General Funds to various outside groups as indicated. In addition, it proposed that one of the groups, Rebuilding Together Peninsula, be funded through the CDBG Housing Improvements Program in the amount of $6,250. All programs previously funded by the General Fund are recommended for full funding as requested, based upon their prior performance in achieving service level targets. New programs (Bill Wilson Center youth shelter programs, India Community Center, and Rebuilding Together Peninsula) are recommended at 50% funding based upon Council's Human Service Policy of providing "seed money" for new programs.

This is the first year of a two-year funding cycle for Outside Group Funding. During the second year of funding, the City will not solicit applications; rather, those agencies which have met or exceeded performance standards will be funded for a second year, with possible funding reduction in proportion to any reduction in available federal CDBG or General Fund support. Those agencies which do not meet performance standards, and all programs receiving one-year "seed money" will be reevaluated in the second year by the Housing and Human Services Commission and the Council for continued funding. Staff is committed to examine the entire Outside Group Funding process over the coming year and to recommend improvements which will make the process more objective and provide for better coordination between the two funding sources.

DETAILED FUND REVIEWS

While it is useful to understand the City's overall budget, it is important to underscore that the City's budget is comprised of multiple funds, with the real short-term and long-term position of the City contained in the respective position of each of these funds. This Transmittal Letter will discuss each fund in detail, but places emphasis on the General Fund.

The following review will provide strategic long-term, as well as important short-term, financial highlights for each individual fund.

GENERAL FUNDS

The General Fund is used by the City to account for all financial resources except those required by law or practice to be accounted for in another fund. Due to the fact that operation of the Gas Tax Fund is inextricably intertwined with the General Fund, it is included in the General Fund discussion.

General Fund

The General Fund supports many of the most visible and essential City services, such as police, fire, road maintenance, libraries, and parks and open space maintenance. General government support functions are also included in this fund, and their costs are apportioned through the use of in-lieu fees to other City funds. Because the General Fund receives the preponderance of its revenue from taxes, it has been the most affected by voter-approved initiatives and State legislative actions. As a result of such action over the past decade, revenues to the General Fund are significantly less than they would have otherwise been. Additionally, the state of the regional economy has a direct effect on the General Fund, as we can see from our current budget crisis.

The General Fund has a very close relationship with several other funds. Those funds are the Community Recreation Fund, the Youth and Neighborhood Services Fund, the Gas Tax Fund, the Internal Service Funds, the Capital Projects Fund, the Infrastructure Renovation and Replacement Fund, and the Redevelopment Agency Fund. In each case, the condition of these funds has a direct bearing on the General Fund due either to contractual relationships or because the General Fund is a primary or significant source of financial support. The relationship between these various funds, where appropriate, will be discussed as a part of the General Fund, as well as in the review of each of these individual funds.

General Fund Revenues

Revenue Estimation Methodology

All revenue assumptions and projections are reviewed and revised each fiscal year.

Further, considerable analysis is undertaken to identify the key elements that impact our major revenue sources so that the projection methodology is reliable over the long-term. Historical data underscores the fact that a significant swing in revenues can occur due to economic cycles. From a low in 1990 to the high in 2000, the economy has produced very different revenue yields to the City in a number of major categories. Projecting revenues based on the high point of the economic cycle could overstate the City's financial position significantly for future years and could result in spending patterns that cannot be sustained. Conversely, projecting revenues from the lowest point of the economic cycle could understate the long-term financial position of the City and cause unnecessary service reductions.

Each revenue source has its unique characteristics that have been used to make projections. In general, estimates of actual expected revenue for each major source are used to calculate FY 2005/2006 figures. For the balance of the financial plan, however, projections are based on a defined business cycle for each revenue modified for present circumstances. Because these projections are based on historic trends and assumed business cycles, they will need to be closely monitored and corrected to reflect any change in patterns or circumstances.

The on-going national recession has resulted in steep declines in the City's major revenues. It now appears that most of our key revenues have finally bottomed out and begun to grow slowly. Unfortunately, in many cases our revenues have stabilized at a new, lower base level. Additionally, several State initiatives have redefined or modified our revenue sources or the manner in which they are allocated. Most notable among these initiatives are the "Triple Flip," the Vehicle License Fee/Property Tax Swap, and "ERAF III".

The Triple Flip

In FY 2004/2005 the State issued "Economic Recovery Bonds" as part of the solution to its record budget deficit. These bonds are secured by a mechanism called the "Triple Flip" which swaps local Sales Tax for Property Tax while the bonds are outstanding. In short, the State moves money from cities and counties to the State by raising the State Sales Tax rate by ¼ cent and reducing the local Sales Tax rate by an equal amount. So that cities and counties aren't hurt, an equal amount of Property Tax is taken from the schools (the Educational Revenue Augmentation Fund) and given to the cities and counties. The State then makes up this loss by giving the schools an equal amount of money from the State's general fund.

When all of the flips are completed, everyone has the same amount of money as before, but a substantial amount of the State's money will now be in a special fund to pay debt service on the bonds instead of in the State's general fund.

The actual Triple Flip began in July 2004. The exchange mechanism will be in place as long as the Bonds are outstanding, and it unwinds automatically when the Bonds are paid off. Although the final maturity of the Bonds is 2023, it is expected that they will actually be fully repaid in nine to ten years because of certain provisions in the bond covenants and in the Proposition that authorized them.

The recommended FY 2005/2006 Budget for the General Fund reflects the Triple Flip mechanism over a ten-year period beginning July 1, 2004. Staff has reduced our Sales Tax projections each year by one-fourth and reflected it as a separate line on the General Fund Long Term Financial Plan called "*Triple Flip - Sales Tax Reduction.*" This same amount is then added to the Property Tax projections in a separate line entitled "*Triple Flip - Property Tax Increase*." In the Triple Flip, the Sales Tax/Property Tax swap is dollar for dollar based on the actual Sales Tax revenue collected and it does not actually increase the City's Property Tax base. There is no net fiscal impact to the City of the Triple Flip. The major effect of this mechanism on the City lies in the fact that Property Tax is essentially remitted to us twice a year while Sales Tax is remitted monthly; this causes a reduction in our interest earnings and a potential cash flow problem. We have taken this effect into consideration in our interest earnings projections for the General Fund.

Vehicle License Fee/ Property Tax Swap

Also included in the State Budget deal with local governments last year was a permanent redistribution of two of the City's revenue sources. Under this agreement, the Vehicle License Fee (VLF) rate will be permanently reduced from 2% to .65%. For FY 2004/2005, the VLF that the City would have gotten at the 2% rate will be calculated and this amount will be added to our Property Tax base through transfers from the Educational Revenue Augmentation Fund (ERAF). In the following years, we will receive our portion of VLF revenues at the now -permanent low rate and our increased Property Tax base will grow according to current economic conditions.

The VLF/Property Tax Swap was reflected in the General Fund Long Term Financial Plan as an increase in Property Tax and a corresponding decrease in VLF starting in FY 2004/2005. For FY 2004/2005 the numbers were developed by first taking our original VLF projection and reducing it by 67.5%. This number, approximately $5.4 million, was then added to the Property Tax projection. Subsequent to our using this methodology, staff from the League of California Cities learned that the State intended to distribute the remaining VLF base (the .65%) primarily to counties rather than cities to pay for county social services realignment costs. Revised numbers were developed for FY 2004/2005 for the actual VLF receipts and the amount that will be converted into Property Tax. The net result of this adjustment is that the total amount of funds will be the same, but our actual VLF revenues will be less and the Property Tax will be more. This newer, more accurate methodology has been reflected in the FY 2004/2005 actual projections and our estimates for FY 2005/2006.

In the years beginning FY 2006/2007, the new Property Tax base grows at our forecasted rates over the entire planning period. It should be noted that this permanent shift results in a financial loss to the City in two areas. First, since Property Tax is paid twice a year while VLF is paid monthly, there is a cash flow and interest earnings loss. Second, and most importantly, the Property Tax rate of growth that we have projected is lower than the growth rate of VLF revenues, and this has a negative impact on our Long Term Financial Plan overall. However, it should also be noted that the VLF is a relatively precarious revenue source that would probably be eliminated or reduced by popular demand in the near future. This new approach takes this risk away from cities and guarantees our revenues through Property Tax.

ERAF III

The final part of last year's State Budget agreement involved a two-year "contribution" of the City's Property Tax revenues to the State Educational Revenue Augmentation Fund (ERAF). Since this is the third time since 1990 that the State has dipped into our Property Taxes in this manner, the loss has been called "ERAF III." The amount of revenue that Sunnyvale will lose for FY 2004/2005 and FY 2005/2006 is $2,051,370 each year. The two years of loss are shown on the General Fund Long Term Financial Plan in the *Current Resources* section in the line item "*State Budget - Reductions*."

General Fund Major Revenue Sources

Five key sources generate nearly 80% of the City's General Fund revenues. They are: Sales Tax, Property Tax, Transient Occupancy Tax, Utility Users Tax/Franchise Fees, and construction-related taxes and fees. The current budget projected that revenues from many of these sources would moderately increase over the next few years as the economy began a slow but measured rebound. While receipts from Sales Tax and construction-related revenues have improved, during FY 2004/2005 we continued to experience decreases in our Property Tax revenues related to the commercial/industrial sector and Unsecured Property Tax. Our projections reflect modest increases over the next few years due to the high level of uncertainty surrounding the economy.

Table IV, below, reflects projected major sources of General Fund revenues for FY 2005/2006 and compares those sources with the FY 2004/2005 revised projections. FY 2003/2004 actuals are also included. Overall, our FY 2005/2006 revenues are forecast to be about .73%% higher than estimated FY 2004/2005 revenues. Comparisons of forecasts for specific revenue sources are difficult to make because of the reshuffling of VLF, Property Tax, and Sales Tax revenues through the Triple Flip and the Vehicle License Fee/Property Tax swap approved in last year's State budget.

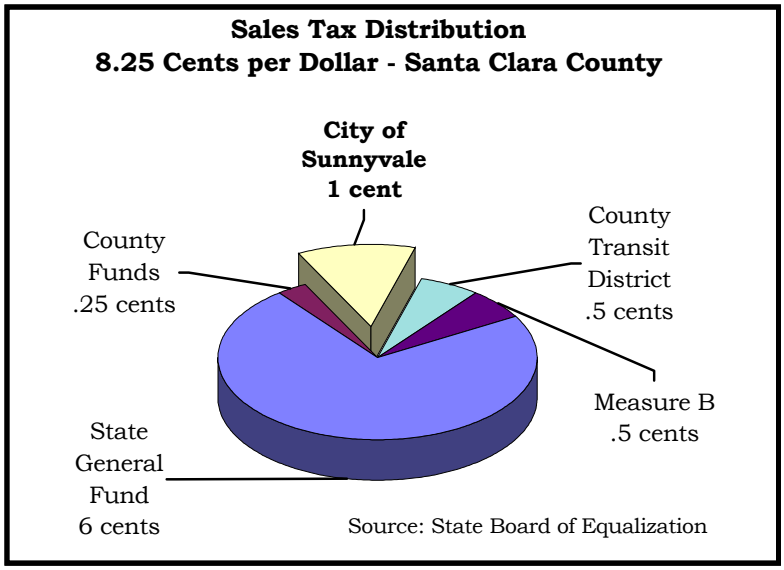
Table IV Recommended Revenues – General Fund					
Revenue Character	**2003/2004 Actual**	**2004/2005 Revised Projection**	**% Growth 2004/2005 over 2003/2004**	**2005/2006 Proposed Projection**	**% Growth 2005/2006 over 2004/2005**
Property Tax	23,580,170	23,369,331	-0.89%	23,967,319	2.56%
ERAF III	0	-2,051,370	N/A	-2,051,370	0%
Property Tax in Lieu of VLF	0	7,355,550	N/A	7,619,808	3.59%
Sales Tax	23,451,665	24,102,713	2.78%	24,916,650	3.38%
Utility Users Tax	5,876,966	5,833,746	-0.74%	6,015,416	3.11%
Franchises	5,520,536	5,334,051	-3.38%	5,455,378	2.27%
Transient Occupancy Tax	4,751,669	5,005,500	5.34%	5,250,225	4.89%
Permits and Licenses	4,251,724	4,509,759	6.07%	4,753,198	5.40%
Inter-Fund Revenues	2,977,816	4,394,663	47.58%	5,552,274	26.34%
State Shared	6,557,012	4,167,637	-36.44%	942,885	-77.38%
Service Fees	2,276,087	2,205,922	-3.08%	2,314,426	4.92%
Interest	2,796,249	2,562,500	-8.36%	2,693,844	5.13%
Other Taxes	1,868,826	1,963,680	5.08%	2,141,182	9.04%
Miscellaneous	857,848	1,895,639	120.98%	724,784	-61.77%
Rents and Concessions	977,993	1,325,897	35.57%	1,765,065	33.12%
Prop. 172 Sales Tax	1,147,392	1,155,437	0.70%	1,217,253	5.35%
Fines and Forfeitures	750,000	740,822	-1.22%	728,113	-1.72%
Real Property Sale	0	0	0%	550,000	100%
TOTAL	**87,641,953**	**93,871,477**	**7.11%**	**94,556,450**	**0.73%**

In the following section are detailed discussions of the City's five major revenue sources: Sales and Use Tax, Property Tax, Utility Users Tax/Franchise Fees, Transient Occupancy Tax, and construction-related revenues. This information will include explanations of the revenue forecasts for FY 2005/2006 and beyond. Following that section will be discussions of several other revenue sources of particular note.

Sales and Use Tax

Sales and Use Tax represents the second largest source of revenue to the General Fund, making up 26% of budgeted revenues in FY 2005/2006. In FY 2000/2001 Sales Tax represented the largest revenue source and constituted 32% of total revenue. Since FY 2000/2001 Sales Tax revenue has fallen at a dramatic rate of 35% or nearly $13 million. However, in FY 2003/2004 Sales Tax revenues increased from the prior year by $684,668. This marked the first time the City had seen a year-to-year increase since the peak of the "dot com" era.

The graph below shows how Sales Tax dollars are distributed within Santa Clara County. The State receives the largest share of the eight and one quarter cents per dollar of sales, while cities receive only one cent of the rate.

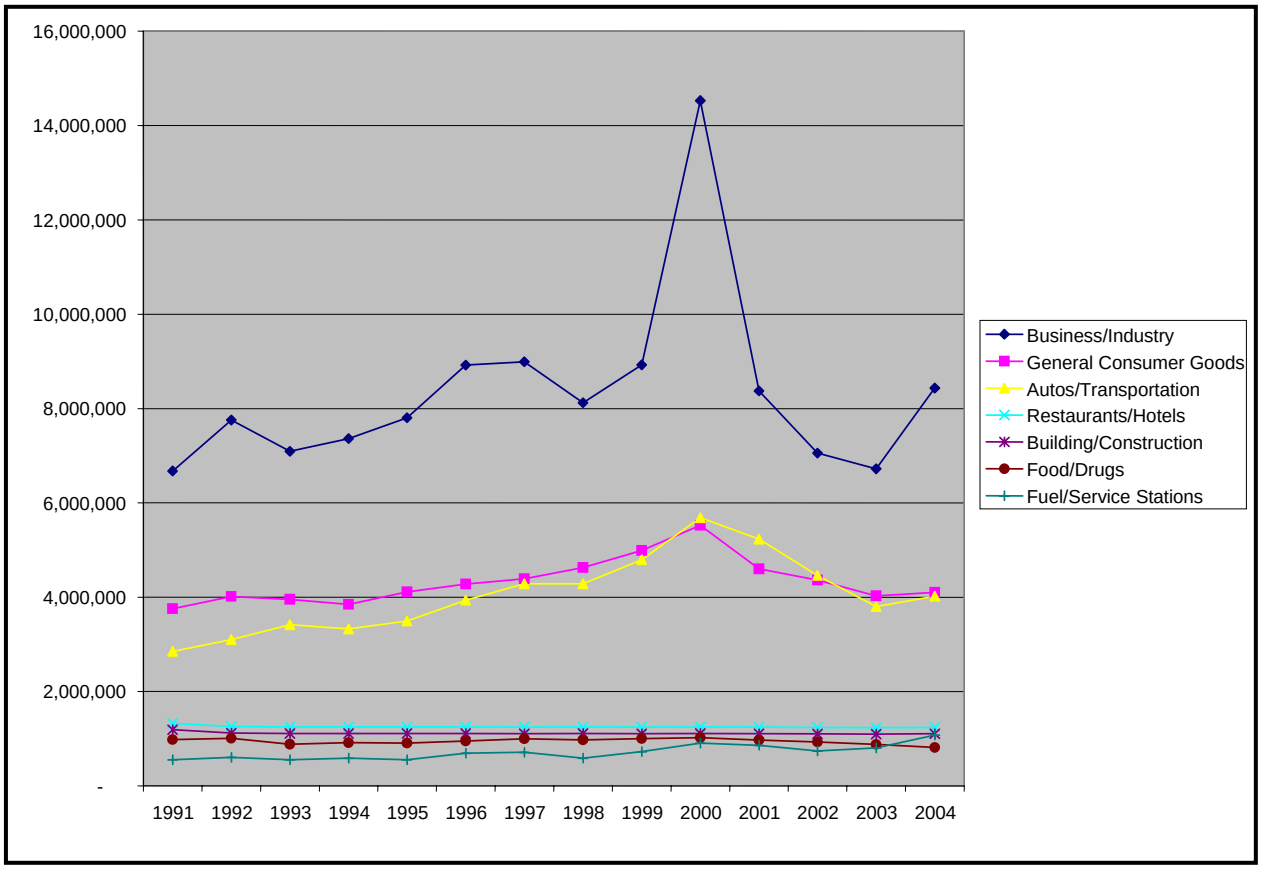


Sales and Use Tax is composed of two different types - general retail sales and business-to-business sales. In Sunnyvale, as well as some other Silicon Valley cities, an unusually high proportion of overall Sales Tax has traditionally been business-to-business in nature; this sector currently constitutes about 36% of our aggregate as opposed to the statewide average of 17%. This makes our Sales Tax much more complicated and difficult to predict because it is often one-time in nature.

Our revised Sales Tax estimate for FY 2004/2005 is $24.1 million. This is up approximately 3% or $650,000 compared to our actual receipts for FY 2003/2004, reflecting a continuing modest increase in our local economic base.

To develop our projections we divided Sales Tax receipts into four major categories that had similar economic characteristics: Business and Industry, General Consumer Goods, Autos and Transportation, and Other. As can be seen from the graph below, each category has a unique pattern:

City of Sunnyvale
Sales Tax Receipts by Major Sector
(Calendar Year 1991 – 2004)



In forecasting our Sales Tax revenues for the next two years and the balance of the financial plan, staff developed individual projections for each sector, and then assimilated the numbers into a single weighted aggregate forecast. Review of the historical data indicated that the Sales Tax had an eight-year economic cycle, which is reflected in our projections over the entire Long Term Financial Plan.

Projections for FY 2005/2006 are that the City's Sales Tax revenue will increase by approximately 3.4% above this current year, to $24.9 million. This is about $700,000 higher than the $24.2 projected for FY 2005/2006 last year. Forecasts for the following years reflect Sales Tax receipts increasing by 4.5% in FY 2006/2007 and moderately thereafter to FY 2008/2009, then slightly decreasing through FY 2012/2013 to reflect the business cycle. The forecast for the second ten years is an annual growth of 4.5% based on the average growth in the business cycle.

In developing our Sales Tax projections, staff took into account the known increases and decreases in companies in the City. Several significant business-to-business Sales Tax producers have recently relocated, with an annual loss of approximately $700,000. However, Council is aware of several new retail establishments that are

coming or are proposing to come to Sunnyvale in the near future. Staff has factored these new additions and identifiable losses into our long-term forecast.

The "Triple Flip" mechanism, implemented by the State beginning July 1, 2004, has also changed the way that Sales Tax is received and accounted for by the City. As discussed earlier, in the Triple Flip, 25% of the local portion of Sales Tax is swapped with Property Tax dollar for dollar based on actual sales collected. The County will estimate the amount of in-lieu Property Tax to be remitted to us based on last year's receipts, and then reconcile their remittances in January of the following year. This process makes it very difficult for us to measure and report our annual Sales Tax revenue because of the delay in accounting.

In summary, Sales Tax revenues have experienced wild swings over the last several years. Sunnyvale experienced unprecedented growth of about 20% per year in Sales Tax receipts in FY 1999/2000 and FY 2000/2001 due to a "boom" in high technology business. Unfortunately, this level of revenue was not sustainable. The current economic downturn was already impacting City revenues three years ago, as the stock market was undergoing dramatic declines and numerous companies across the nation were implementing cost saving measures that included reducing capital investment. We are now anticipating a mild recovery over the next several years to a more realistic on-going level.

Property Tax

Property Tax now represents the largest source of General Fund revenue. Property Tax is up considerably as a percent of General Fund revenues compared to the prior year as a result of the VLF/Property Tax Swap. Property Tax now represents 33% of all General Fund revenues.

Property Tax has also been the revenue most affected by voter initiatives and legislative actions. With approval of Proposition 13 more than 20 years ago, Property Tax revenues were reduced by two-thirds and thereafter limited to 2% annual increases or the CPI, whichever is less. In the early 1990s, the State legislature shifted a larger portion of the Property Tax to schools. This shift was made to the State's Educational Revenue Augmentation Fund ("ERAF") to backfill a portion of the State's obligation for school funding. This "ERAF shift" is now 3% of the Property Tax dollar, representing an annual loss to the City of Sunnyvale currently amounting to approximately $6.2 million. Cumulatively, the total ERAF shift from the beginning represents a loss of $63 million to Sunnyvale through FY 2004/2005.

Overall FY 2004/2005 Property Tax revenues are expected to be down approximately 1.0% when compared to FY 2003/2004. Despite robust residential valuation growth the City has experienced substantial declines in commercial, industrial, and unsecured valuations. Most notably, receipts received for unsecured property are down nearly 13%, or $299,288 from FY 2003/2004. This decline in Unsecured Property Tax reflects the continued vacancy in our research and development and commercial buildings, the departure of several manufacturing facilities, and the continued hesitancy of businesses to expand operations and purchase or replace capital equipment.

Revenue from Secured Property Tax, which represents about 85% of total Property Tax revenues, is projected to increase by approximately 3.5% next year. We anticipate continued growth associated with residential real estate and a stabilizing commercial and industry market.

For our future projections we developed a model similar to that used for our Sales Tax forecasts. For Secured Property Tax we isolated the assessed valuations for both Residential and Commercial/Industrial, as each segment represents different stages of the economic cycle. For FY 2005/2006 we have anticipated continued growth in residential valuations since the residential housing market remains strong. Assessed valuations associated with commercial and industrial properties are anticipated to remain flat for the next fiscal year as this sector continues to have historically high vacancy levels. In the following fiscal year, FY 2006/2007, we anticipated 6% growth in the residential sector and 2% for commercial and industrial properties. We then used the eight-year economic cycle to project revenues for the remainder of the financial plan. Projections are that residential property tax will remain strong for the first ten years of the planning period, with an average annual increase of 5%. Staff is also forecasting that the commercial sector will stay flat until FY 2007/2008 when it increases by an average of 4.4% through FY 2014/2015.

The Vehicle License Fee/Property Tax Swap that was part of the State budget last year has been reflected in our Property Tax projections beginning in FY 2004/2005. As discussed earlier, the Property Tax base has been increased in relationship to a reduction in Vehicle License Fee revenues. This increase will be permanent, and the new base will grow in the following years with the growth of Property Tax.

Utility Users Tax and Franchise Fees

Utility Users Tax (UUT) and Franchise Fees combined represent the third largest source of General Fund revenue, generating about 12% of the total. Historically, these two revenue categories have been combined because one of the primary sources of revenue for both is sale of electricity and gas.

The City's UUT revenues are based upon receipts from intrastate telephone, gas, and electric usage. Approximately 63% of UUT revenue is derived from the sale of electricity, 26% is related to intra-state telephone usage, and 11% is derived from the sale of gas.

As indicated in Table II, above, receipts from UUT are expected to remain flat in FY 2004/2005 compared to last year's receipts. UUT receipts are primarily driven by electric rates charged by Pacific Gas & Electric (PG&E). In February of this year PG&E announced that the California Public Utilities Commission (CPUC) had approved an average rate increase of approximately 3%. UUT revenues are projected to increase by 3% from FY 2005/2006 through FY 2014/2015 and 4% for the second ten years of the Long Term Financial Plan.

The City receives a one-time franchise payment from PG&E each year which represents about 41% of all Franchise Fee revenue. The City's other main franchise

agreements are with Comcast Cable and Specialty Garbage. We expect Franchise revenues to meet budgeted projections for FY 2004/2005. For FY 2005/2006 Franchise Fees are projected to increase by 2.27% over the current actual. Future year projections include an increase of 3% annually from FY 2006/2007 through FY 2014/2015 and 4% annually in the second ten years of the Plan.

Transient Occupancy Tax

Transient Occupancy Tax (TOT) represents the fourth largest revenue source of the General Fund, constituting about 5.5% of the total.

Beginning in approximately 1995, improved economic conditions led to higher occupancy rates and room charges, as well as the addition of several new hotel and motel properties. Our TOT rate was also increased from 8% to 8.5% in 1995. However, this revenue is particularly susceptible to economic cycles because both occupancy rates and room rates are closely linked to economic conditions. The bulk of our TOT revenue stems from weekday business travel. The Sunnyvale TOT rate, at 8.5%, is the lowest in Santa Clara County. Most cities are at 10%, with Santa Clara at 9.5%.

Since FY 2000/2001 TOT revenue has fallen at a dramatic rate of 55% or nearly $6 million. Based upon the most recent level of receipts, we are anticipating that TOT revenues have effectively bottomed out and are starting to show measured indications of growth. For FY 2004/2005 we anticipate that TOT revenue will exceed the prior year's amount by approximately 5%. We are forecasting a more robust recovery in FY 2005/2006 through FY 2008/2009, tempered by some adjustments as discussed below.

A number of changes in the City's hotel and motel properties have recently occurred or are scheduled to occur in the next year. One Best Western property on El Camino Real was purchased in March and is being demolished to be replaced by a retail establishment. The Woodfin Suites on El Camino Real was closed as of February and is being converted to residential. Finally, the Four Points Sheraton has shared plans with the City to demolish the existing hotel and replace it with a smaller, higher end hotel property and residential housing. These losses and changes in our hotel and motel businesses have been reflected in our TOT forecasts for FY 2005/2006 and beyond. As a result of the adjustments to the base forecast, we are projecting a 5.2% increase in TOT for FY 2005/2006 and a 2.2% increase in FY 2006/2007. In FY 2007/2008, we are forecasting a 14.5% increase to reflect the return of the Sheraton property to the base. Future year projections mirror the business cycle seen in the Business and Industry Sales Tax sector and average approximately 6% over the remainder of the planning period.

Construction-Related Revenue

Construction-related revenues represent about 5.7% of General Fund revenues in the current year. This category includes Construction Tax as well as receipts from the issuance of building, electrical and other permits. Plan Check Fees are also reflected

here. Due to a number of large commercial projects, as well as general increases in construction, these revenues showed extraordinarily large gains in FY 1999/2000 and FY 2000/2001. Clearly the economic downturn caused the levels of construction-related revenue to trend downward significantly in FY 2001/2002 and FY 2002/2003. Unusually high levels of residential development currently have caused the original projection for FY 2004/2005 to increase by approximately 6% when compared to the prior year.

Future years' projections have been based on a rolling eight-year economic cycle. The forecasts for FY 2005/2006 and FY 2006/2007 also take into account the effects of the Downtown Mall Redevelopment project, which is one of the largest developments that Sunnyvale has experienced. Projections call for growth of approximately 5.4% for Permits and Licenses in FY 2005/2006 and an increase of 34% for Construction Tax. In the following years construction-related revenue will grow at a slower pace until FY 2006/2007, and then decline until FY 2010/2011. The business cycle will then be repeated over the remainder of the planning period.

Other Revenue Highlights

The recommended FY 2005/2006 Budget includes certain other revenue sources which need some explanation.

State Shared Revenues/Vehicle License Fees (VLF)

In prior years VLF represented the General Fund's fourth largest revenue source. VLF is an annual fee on the ownership of a registered vehicle in California, levied in place of a property tax on vehicles. The State's adopted FY 2003/2004 Budget included a provision which permanently reduces the VLF rate from 2% to .65%, reduces corresponding revenues to local government and replaces these revenues with an equal amount of Property Tax.

As staff was reflecting this change in the FY 2004/2005 Budget, it was believed that the reduction in VLF revenues would correspond to the pro rata reduction in rate. Thus our projections were that the City would receive 32% of its prior VLF with the difference made up in Property Tax. It was subsequently discovered that the bulk of the remaining VLF monies for local government would be allocated to counties, with very little distributed to cities. Staff has therefore reflected this new situation in the recommended FY 2005/2006 Budget. It should be noted that the amount actually received in FY 2004/2005 is significantly higher than the budgeted amount for next year because of timing issues with the VLF distribution at the State level.

Also included in this category for FY 2004/2005 projected is $2.1 million that the City collected by participating in the VLF Loan Receivable Financing. This revenue is one-time only and represents early collection by the City of monies owed to us from the State.

Interfund Revenues

Interfund Revenues include repayment to the General Fund of various loans made to other funds. Also included here is the repayment by the Redevelopment Agency of the General Fund advance. This revenue source is projected to be up by 26% in FY 2005/2006, largely due to a higher repayment from the Redevelopment Agency.

Rents and Concessions

The category of Rents and Concessions includes two charges to the utilities for rent of General Fund land. The first is a charge to the Solid Waste Fund for use of the land that the SMaRT Station occupies. This charge, in the amount of $333,000 was new in FY 2004/2005. The second, a charge to the Wastewater Management Fund for the use of the land that the Water Pollution Control Plant occupies, is new for FY 2005/2006. The amount of the WPCP rent is $297,000. Both revenues continue through the 20-Year planning period, increased by inflation.

Library Audiovisual (DVD) Fees

As part of the City's budget reduction exercise for FY 2003/2004 the Library proposed a new few to cover rental of their DVD collection. Annual revenues from this source were estimated to be $300,000, with costs of $63,000. This program was scheduled to begin in FY 2004/2005. Experience to date indicates that the revenues realized will be in the range of $100,000. Therefore, the Library has revised the ongoing estimates and made reductions in their operating budget to make up the net difference. These new estimates have been reflected in the General Fund revenues and operating expenditures for FY 2005/2006 and beyond.

Real Property Sale

The recommended FY 2005/2006 Budget includes $550,000 in new revenue from the sale of a house on Charles Street owned by the General Fund. It is staff's recommendation that this house, which is currently rented as affordable housing, be transferred to the Housing Mitigation Fund, which has the primary responsibility for low and moderate income housing in the City. Currently the General Fund is receiving below-market rent for this property. The Budget also includes a modest reduction in rental income and maintenance costs due to the sale of this house.

Emergency 911 Fee

The FY 2004/2005 Long Term Financial Plan contemplated full implementation of an Emergency 911 Fee beginning in FY 2005/2006 as part of the Fiscal Strategies to balance the City's structural deficit. This fee was originally anticipated to begin in FY 2004/2005 but was delayed for one year to resolve certain legal issues that had arisen. In June 2004, the Council approved the fee in concept pending resolution of

the legal issues and challenges. This fee was forecast to recover a total of $2 million annually.

A number of cities in the Bay Area have enacted, or are considering the enactment of a cost recovery fee to help finance the operation of emergency 911 dispatching centers. Two municipalities, Stockton and Union City, enacted such ordinances last year and are currently involved in lawsuits sponsored by telecommunications providers. The lawsuits essentially allege that the fee is actually a tax and therefore has been enacted in violation of the voter approval requirements of Proposition 218.

Both lawsuits are still currently in progress and are at various stages. Meanwhile, the City of San Jose began collecting an Emergency 911 Fee in January 2005 and has not had legal challenge as of yet.

Based on the uncertain timing and outcome of the two existing lawsuits staff has removed the revenue from the Emergency 911 Fee from the General Fund Long Term Financial Plan. When and if a clear conclusion is reached, staff recommends that Council move forward with implementation of this new revenue to offset the continuing substantial costs of our emergency dispatch center.

Utility Infrastructure Fee

A new item that was included in the FY 2004/2005 Budget was the Municipal Utilities Infrastructure Fee. This fee was approved in concept in FY 2003/2004 and was scheduled to take effect in FY 2004/2005 in the amount of $645,000. The concept was that this fee would be collected from the City-owned Water and Wastewater utilities for their impact on General Fund assets. Currently the city charges a franchise fee to the private utilities that operate here, including the contractor that provides refuse collection services.

During the first part of FY 2004/2005 the Department of Finance engaged an expert to determine the impact of the Water and Wastewater utilities on the City's street system. This independent analysis ultimately revealed that the Utility Infrastructure Fee was not viable because of a number of recent legal rulings. For FY 2005/2006 and beyond we have removed this revenue source from the General Fund.

Additional Sales Tax from Redevelopment of Town Center Mall

Another revenue that was included in the Fiscal Strategies used to balance the FY 2004/2005 Budget was additional Sales Tax, net of any additional costs, to be generated from the redeveloped Town Center Mall. It is anticipated that this revenue will be approximately $1 million per year. The Long Term Financial Plan shows these funds beginning halfway through FY 2007/2008 in keeping with the current development schedule.

Traffic and Parking Fines

During preparation of the recommended FY 2005/2006 Budget staff discussed the forecasts for traffic and parking fines collected by the Department of Public Safety. Specifically, the formula for distribution of the fines collected by the courts was reviewed so that the City could understand if we were receiving all monies to which we were entitled.

It is interesting to note that most of the bail or fine monies for traffic citations go to the courts for support of the criminal justice system rather than being returned to DPS to support the cost of enforcement. Bail for Vehicle Code traffic offenses is established by the State Judicial Council and adopted annually by the Superior Court of Santa Clara County. Bail for specific offenses includes an established base fine and additional penalty assessments. Cities receive 74% of the base fine, with the County receiving the rest. The average base fine for the most common Vehicle Code offenses such as speeding or red light running, is $85. In Santa Clara County, penalty assessments totaling 235% of the base fine are added to the bail schedule. Local cities do not receive any funds associated with the penalty assessments.

For most parking violations, the City receives about 79% of the bail or fine amount. Bail for most parking violations is set at $32. Additional assessments totaling an average of $5 per citation are collected for various court purposes.

The distributions received by the City for traffic or parking citations have not been audited in the recent past. In FY 2005/2006 the Department of Public Safety and the Department of Finance will work together to audit these distributions and review any possibility for increased recovery.

General Fund Expenditures

Table V, below, outlines the recommended expenditures for the General Fund only. Looking at just the General Fund, the proposed operating expenditures for FY 2005/2006 are 4.7% above the revised FY 2004/2005 Budget. Total General Fund recommended expenditures, including projects, debt, and equipment, are 2.85% above the revised FY 2004/2005 Budget.

Table V Recommended Expenditures – General Fund

Expenditure Character	2003/2004 Actual	2004/2005 Revised Budget	2005/2006 Proposed Budget	% Growth 2005/2006 over 2004/2005
Operating	88,559,706	98,022,782	102,627,270	4.70%
Project Operating	0	0	9,668	N/A
Projects	3,405,116	3,421,372	1,450,329	-57.61%
Debt	412,283	411,358	410,138	-0.30%
Lease Payments	1,216,661	1,220,728	1,219,558	-0.10%
Equipment	0	0	300,000	N/A
TOTAL	**93,593,766**	**103,076,240**	**106,016,963**	**2.85%**

The major portion of the rise in operating costs for the General Fund in FY 2005/2006 is attributable to a major increase in CalPERS retirement costs, which are not under the City's control. The operating total reflected in the above table includes approximately $2.9 million in increased retirement costs for FY 2005/2006 above the current level. When these retirement increases are factored out of the calculation, the real increase in General Fund operations is 1.8%. The remaining portion of the increase in operating costs is due to salary increases programmed as part of the Public Safety Officers Association Memorandum of Understanding, and increases in other personnel-related costs such as health insurance and workers' compensation.

The recommended FY 2005/2006 Budget is built on several key salary and benefit assumptions. First, salary increases have been projected based on preliminary survey information from the Human Resources Department. The following table indicates assumptions for salary increases in the future:

Labor Unit	2005/2006	2006/2007	2007/2008 to 2014/2015	2015/2016 to 2024/2025
SEA/Confidential	0.00%	1.00%	3.00%	4.00%
PSOA	3.00%	1.00%	3.00%	4.00%
COA	3.00%	1.00%	3.00%	4.00%
SEIU	0.00%	1.00%	3.00%	4.00%
Management	0.00%	1.00%	3.00%	4.00%

In general, all employees saw significant salary increases as the result of our local labor market and the City's competitive compensation philosophy during the past several years. Our labor agreements for all of the four bargaining units are still in effect, as indicated in the following table:

Labor Unit	No. represented	MOU expiration date
SEA	530	June 30,2008
PSOA	215	June 30, 2006
COA	19	December 31, 2005
SEIU	57	June 30, 2005

As Council knows, these agreements contain formulas that determine what salary increases will be in the future. These formulas are based on market comparisons with predetermined comparable cities within our labor market. Our budget assumptions are that economic conditions will moderate future salary increases in our comparator cities.

Another major factor with significant fiscal implications for the General Fund is the rapid escalation that has been experienced in the cost of personnel benefits over the last several years. The recommended FY 2005/2006 Budget contains an increase of 10.6% in expenditures for the Employee Benefits Fund over this current year. The largest component of these increases by far is the cost of retirement contributions, which are continuing to rise as the effect of prior years' PERS investment losses are reflected in the new contribution rates. Detailed discussions of each of these costs are

included in the *Detailed Fund Reviews* section of this Transmittal Letter under *Employee Benefits and Insurance Fund*.

Several additional changes in the operations component of the General Fund are highlighted below:

- During FY 2004/2005 the Public Safety Department slowed recruiting efforts substantially because they were overstaffed in sworn officers. This will allow the department to save approximately $1.5 million in recruitment costs. These savings have been reflected as savings to the FY 2004/2005 Budget.

- It is projected that because of current overstaffing the Public Safety Department will not need to recruit during FY 2005/2006. This will result in one-time savings of $2.5 million which have been recognized in the General Fund.

- FY 2005/2006 is an on year for City elections. Therefore $170,000 is included in FY 2005/2006 for election-related costs.

- Each year the Gas Tax Fund supports a large portion of the Public Works Pavement Operations program. The amount that is used for this purpose varies each year depending upon funds available and project requirements. In FY 2004/2005 the Gas Tax support amounted to $2 million. For FY 2005/2006 the use of Gas Tax has been increased to $3.9 million. This accounts for the fact that the increase in operations for the Combined General Fund and Gas Tax Fund is 6.5% while General Fund alone is 4.7%. In essence, the Gas Tax Fund is defraying more of the General Fund street expenditures in FY 2005/2006.

Although the recommended FY 2005/2006 Budget for the General Fund shows an increase over the prior year, it must be emphasized that the level of service reflects the major reductions that occurred in FY 2003/2004.

Budget Supplements

Budget supplements are called out separately in the recommended budget to draw a distinction between the service levels provided in the baseline budget and recommended expansion or reduction of service levels. Supplements are normally presented to the City Manager by staff during the budget review process and then the City Manager makes a recommendation to Council. If a supplement is approved as part of the budget adoption in June, that particular activity is moved into the baseline budget and reflected as such in the adopted budget document.

This year, there are no budget supplements to be considered.

General Fund Projects

This is the first year of the two-year budgeting cycle for projects. Therefore, staff efforts were directed toward an extensive review of both currently existing projects and newly proposed projects. This Transmittal Letter focuses on newly developed or significantly revised projects. Descriptions and detailed financial information on all projects can be found in the budget document, *Volume II, Projects Budget*. There are two helpful indexes of all the City's projects, one by project name and the other by project number.

The recommended FY 2005/2006 Budget for the General Fund includes $50,000 in Capital Projects, $1,107,720 in Special Projects, and $203,934 in Outside Group Funding Projects. Additionally, General Fund-related projects are found in several places in the budget. They are in the General Fund, the Gas Tax Fund, the Capital Projects Fund, and the Infrastructure Renovation and Replacement Fund. In general, these categories are considered to be related to the General Fund because it is the ultimate source of financial support through contributions or transfers. The recommended FY 2005/2006 Budget includes $1,060,492 in transfers from the General Fund to the Infrastructure Renovation and Replacement Fund. *Volume II, Projects Budget* contains details on the projects included in the Infrastructure and Capital Projects Funds in the recommended FY 2005/2006 Budget.

Several major capital or special projects have been discussed earlier in this Transmittal Letter in the *Major Project Efforts* section. The following are additional projects affecting the General Fund which are either new or have changes in funding in the recommended FY 2005/2006 Budget:

- **Utility Underground Cost Sharing:** The Sunnyvale Municipal Code requires that developments underground overhead utilities. In some cases, the City is required to pay for portions of the undergrounding. This project provides funding for the City's required portion to underground overhead utilities. A budget of $50,000 per year, growing with inflation, has been established but may change pending completion of a study issue on undergrounding practices. This work was defunded in previous years due to budgetary constraints but has been restored to reflect the current Municipal Code requirements.

- **City Owned Properties - Downtown:** This project provides funds to maintain seven properties that the City owns in the downtown area. These properties include two single family residences, the Chamber of Commerce building, the bus depot, a duplex and two vacant lots. Changes to the project in FY 2005/2006 include a slight increase in cost and the extension of the project through FY 2008/2009. It is projected that the City will dispose of these properties in FY 2009/2010. The General Fund previously owned a third single family residence at 388 Charles Street, which is proposed to be transferred to the Housing Fund in FY 2005/2006. Therefore, the maintenance and rental revenues for that house are reflected in the Housing Fund for FY 2005/2006.

- **239/241 Commercial Street Property Maintenance:** This new project provides for the maintenance of the City's property at 239/241 Commercial Street. The City purchased this property in January 2003 for future expansion

of the City's Corporation Yard, which is next door. Due to the economic downturn, the expansion project has been deferred, and the property will continue to be leased to Sunnyvale Towing. The property is an older concrete tilt up building, and routine maintenance is required to maintain its marketability. Funds in FY 2005/2006 in the amount of $10,000 are programmed for work to the heating, ventilation and air conditioning (HVAC), plumbing, and electrical systems. Smaller amounts of approximately $5,000 growing with inflation are programmed for the remainder of the 20-Year Plan. Costs of the maintenance are fully covered by payments from the lessees of the building.

- **Update of Mandated General Plan Sub-elements:** This project funds the General Plan Sub-element updates that are mandated by the State or other federal or local regulations. Funds in the amount of $35,000 are budgeted in FY 2005/2006 to update the Housing Sub-element. Future funds are identified for the Noise, Land Use and Transportation, and Safety and Seismic Safety Sub-elements. Funding is estimated every two years for these required updates.

- **Updates of Non-Mandated General Plan Sub-elements:** This project provides for the updating of the 17 General Plan Sub-elements that are not mandated by the State. Funds are identified for the Arts, Public Safety Support Services, Socio-Economic, Community Design, and Air Quality Sub-elements in the first ten years. This project begins in FY 2006/2007 and continues every two years for the remainder of the plan.

- **Optimal Staffing Study for Public Works:** This project provides for a study to ensure that the City's Department of Public Works meets current service levels in the most cost effective manner. Funds in the amount of $100,000 are budgeted in FY 2005/2006, with $53,000 of this coming from transfers from the City's three utility funds.

General Fund Reserves and Set-Asides

One of the most powerful aspects of multi-year financial planning is its capability to recognize trends over time and begin at an early point to consider the necessary steps to alter the long-term forecasted position of a particular fund should that appear necessary. The reserves and set-asides contained in the General Fund's Long-Term Financial Plan play a pivotal role in the City's multi-year planning strategy.

The City has established five reserves in the General Fund that are restricted by prior policy or legal requirements to specific uses. Most of the City's reserves are established in accordance with policy adopted in the Fiscal Sub-Element of the General Plan. Policy 7.1B.8: states:

> "Reserves: Provide a prudent level of reserves for future unexpected expenses and revenue declines; to accumulate funds to support future planned capital improvements, and to level high and low expenditure years in the Ten-Year Resource Allocation Plan."

The General Fund currently has four reserves that are designed to be used according to the policy above. These reserves are contained in the General Fund's financial plan under the sub-heading, *Designated Reserves*.

The first is the *Contingencies Reserve* equal to 20% of the operating budget each year. This reserve is to be used only in case of emergency or disaster, and is not intended for normal unanticipated expenditures. In the Fiscal Sub-Element, the policy calls for this reserve to be 10% of operations, but Council policy adopted in FY 1992/1993 changed it to 20% of operations. This reserve changes each year as operations of the General Fund either increase or decrease.

In prior years the General Fund also has had an additional 5% of operating costs in the *Service Level Contingency Reserve.* This reserve was established in FY 1993/1994 to provide funds for increased service levels or costs in excess of inflation. Before FY 1993/1994, the Resource Allocation Plan contained an on-going set-aside called the "One Percent of Operations Set-aside" that provided the ability to handle revenues that did not perform as well as projected and expenditures that increased more than inflation. This set-aside was replaced by the *Service Level Contingency Reserve*. It is important to note that the reserve is one-time, and once drawn down it is gone. The set-aside, on the other hand, was available each year and accumulated if not used.

In the recommended FY 2005/2006 Budget the *Service Level Contingency Reserve* has been removed from the General Fund Long Term Financial Plan. Removing these monies will have an impact on interest earnings in the General Fund, since the Reserve's total of about $5 million is no longer in our cash portfolio. The elimination of the Reserve continues through FY 2016/2017, when *Current Resources* begin to exceed *Current Requirements.* In FY 2017/2018 we have reinstituted the on-going *Service Level Set-Aside* in the amount of $1 million. It should be noted that the Set-Aside grows significantly toward the latter part of the 20-year plan.

A third reserve that the General Fund has had in the past is the *Non-Recurring Events Reserve.* This reserve contains funds from FY 1997/1998 and FY 1998/1999 that resulted from greater than anticipated revenues and lesser than anticipated expenditures during the height of the dot.com boom. By Council action, these types of one-time funds resulting from the peak of the economic cycle were set aside for significant high-priority capital and special projects and not used to add recurring services. The balance of this reserve at the end of FY 2004/2005 is currently projected to be $163,506. In the recommended FY 2005/2006 Budget this reserve has been eliminated.

A fourth reserve in the General Fund is entitled the *20-Year Resource Allocation Plan (RAP) Reserve.* This reserve functions to levelize economic cycles from year to year. By letting this reserve vary each year, the fund can absorb the cyclical effects of the economy and specifically plan for project-related expenditures. In essence, this reserve grows during periods of economic growth and is drawn down during the low points of economic cycles to maintain stable service levels. The *20-Year RAP Reserve* functions very effectively to prevent us from adding services at the top of the economic cycle that cannot be sustained while allowing us to maintain Council-approved services levels during economic downturns. This is in sharp contrast to jurisdictions

like the State of California, which greatly increased spending during the boom and is now faced with making draconian expenditure reductions in the face of revenue shortfalls.

The function of the *20-Year RAP Reserve* and its strength has been particularly apparent in the last several years as the City has struggled with the rapid economic downturn in the region. In prior years when the City was experiencing strong economic growth, the reserve was building up over time to the $61 million level reached in FY 2002/2003. Then, as the effects of the economic downturn began to be fully felt, the reserve was available to provide a "cushion" to maintain City services at desired levels. In the recommended FY 2003/2004 Budget a structural imbalance between revenues and expenditures of $14-15 million was identified, and a plan consisting of a combination of service level/expenditure reductions and fee increases was implemented to bring the General Fund into balance over the twenty-year planning period. The recommended Long-Term Financial Plan shows the *20-Year RAP Reserve* being drawn down until FY 2011/2012 to reflect the structural imbalance the General Fund is experiencing in those years.

A detailed discussion of our current projections for the 20-Year RAP beginning in FY 2005/2006 is found in the section below entitled *General Fund Fiscal Position and Required Fiscal Strategies.*

Finally, the City has two reserves for specific purposes. The first, the *Land Acquisition Reserve,* was established in FY 1994/1995 for the purpose of purchasing land or property in the downtown area with an emphasis on future income generation through economic development. In the past, it has been used to purchase key parcels in the downtown area, and as the land is sold to the private sector, the reserve is replenished. For FY 2004/2005 the reserve balance is $3 million. However, in the recommended FY 2005/2006 Budget the reserve level is $550,000. This reflects the elimination of the $3 million current balance and the addition of proceeds from the land sale of a property on Charles Street to the Housing Mitigation Fund. This transaction is discussed in more detail in the section of this Transmittal Letter on *General Fund Revenues.*

The second restricted reserve is the Set Aside for the Historical Museum in the amount of $20,000. When Council approved an appropriation for construction of the Sunnyvale Historical Museum, an allocation of $20,000 was also approved to help defray operating expenses in the first few years. This money has been set aside pending actual construction and opening of the Museum.

In past years the General Plan Long Term Financial Plan has contained a planned expenditure called *Fiscal Uncertainties.* The *Fiscal Uncertainties* line item was contained within the *Expenditures* section of the financial plan, and it represents the on-going latitude that is available to increase service levels, add new annual programs, or address unexpected fiscal pressures.

For the recommended FY 2004/2005 Budget the *Fiscal Uncertainties* line item was zeroed out for the first nine years of the plan. In the recommended FY 2005/2006 Budget this line item has been eliminated.

General Fund Financial Position and Required Fiscal Strategies

The City has made considerable progress toward its goal of long term financial stability during this past year. Particularly noteworthy is our work to identify and fund our infrastructure renovation and rehabilitation needs and our continued refinement of the City's Planning and Management System.

Phase I of the Long Range Infrastructure Plan (LRIP), which incorporates General Fund-related assets, has been in place for some time. Revision of the original assumptions regarding cost and timing are in the process of being reviewed and updated. Staff has also been identifying and inventorying utility-related fixed assets and for the first time the recommended FY 2005/2006 includes preliminary estimates for a full twenty year time frame. Work to refine the utility-related LRIP further will be completed in late 2005. Updates to both phases of the LRIP will be reflected in the budget for FY 2006/2007.

Sunnyvale's Planning and Management System provides the foundation upon which to make informed policy decisions in support of the City's core mission. During this past year staff has undertaken an ambitious program to update all administrative policies as well as our basic performance budgeting structure. Most of the administrative policies have been reviewed and updated. A review and analysis of the performance based budgeting system began early in FY 2004/2005 and is expected to be completed by the end of the fiscal year. Work included evaluation of the philosophy and intent of the system as well as the process. Recommended changes to the performance based system will be brought to Council in a study session format early in FY 2005/2006. Following approval of the revised system, staff will begin an implementation stage to restructure all programs into the revised format. This work will be completed during FY 2005/2006 and used in preparing the next two-year operating budget.

Sunnyvale also faces a number of challenges to its long term financial stability. The continuing decline in Sunnyvale's General Fund revenues over the last several years and some sharp increases in personnel costs have led to a continuing structural imbalance between revenues and expenditures in the City's General Fund. For FY 2005/2006 we are projecting that revenues and expenditures will still be out of balance for the first portion of our planning period.

The General Fund Long Term Financial Plan contains a section underneath the *Fund Balance* information to display the *Total Current Resources*, *Total Current Requirements*, and the *Difference* between them. As can be seen from this information, a structural imbalance between revenues and expenditures exists for the first seven years of the plan, or through FY 2011/2012. In FY 2012/2013 the revenues and expenditures are essentially even and then revenues begin to be greater than expenditures by varying amounts.

The recommended FY 2005/2006 Budget for the General Fund continues to reflect Sunnyvale's new fiscal reality. The level of services included reflects the reductions made in FY 2003/2004 with no further increases proposed. In order to balance over the planning period, a number of reserves were reduced or eliminated. This provides

virtually no flexibility for responding to unplanned conditions or potential fiscal challenges.

It should be cautioned, as we discuss the fiscal health of the General Fund, that there are a number of pressures on the expenditure side that may pose fiscal challenges for the City in the upcoming years. These include: Library facilities and programming needs; an increasing Community Recreation Fund subsidy requirement; rising employee costs; unfunded projects; and the need for Civic Center replacement or renovation.

A recent study issue conducted in FY 2004/2005 indicates that our Library facility and collection are not keeping up with the growing demand for our services. A visioning exercise will be conducted during FY 2005/2006 to define the Library of the future. This may result in a need for substantial new services or facilities.

The status of the Community Recreation Fund, which currently projects a structural imbalance between desired program expenditures and revenues, also poses a fiscal risk to the General Fund. To the extent that the revenues generated in the Community Recreation Fund are insufficient to support all of the services that the community believes are important to our quality of life, Council will be faced with the choice of reducing programs or increasing the subsidy from the General Fund.

As mentioned earlier, the cost for employees, both in salaries and benefits, has increased significantly in the last several years. If our assumptions do not hold, the current budget does not have the flexibility to handle unplanned increases.

An additional challenge to the General Fund's long term fiscal health is the unfunded capital and infrastructure projects that have been identified this year which total about $444 million over the 20-year period. Of particular concern is the unfunded Civic Center project scheduled in FY 2019/2020 and FY 2020/2021. At that time, it will be necessary to reconstruct or renovate the existing City Hall, Library, and Public Safety Building due to functional obsolescence. It is estimated that the total cost of improvements will be $150 million.

Finally, in order to maintain the quality of life that the community expects, the City needs to function as a high performing organization, leveraging opportunities as they arise and attracting and retaining top level employees. In order to be high performing, we need to invest in our human resources, providing opportunities for learning and developing skills and the tools necessary to function at optimum levels.

Last year, the FY 2004/2005 Budget and Long Term Financial Plan for the General Fund includes several *Fiscal Strategies* that were designed to address the ongoing structural gap between revenues and expenditures. First, full implementation of the new Emergency 911 Fee was reflected starting in FY 2005/2006. This fee was estimated to generate approximately $2 million in new revenues.

Second, the additional Sales Tax that will be generated from redevelopment of the Town Center Mall was reflected in the plan starting in the second half of FY 2007/2008. This revenue has been estimated to add $1 million in new revenue annually net of potential additional City costs.

Although it appears that the additional Sales Tax from the Town Center Mall is still likely to be realized, the implementation of the Emergency 911 Fee has been delayed pending resolution of outstanding legal issues. To reflect this status, the recommended FY 2005/2006 Budget does not include receipt of the Emergency 911 Fee.

After the other fiscal strategies were considered, the General Fund Long Term Financial Plan still required an additional ongoing decrease in expenditures or increase in other revenues in order to balance over the first portion of the planning period. Staff reflected this amount in the line item *Fiscal Strategies* contained in the *Expenditures* section of the plan. It was forecast that about $2.3 million in strategies that would either reduce costs or increase revenues would need to be in place through FY 2011/2012. Last year Council participated in a comprehensive service level review process and identified service level reductions in the amount of $2.2 million. These reductions were deferred until December 2004 and then again until consideration of the FY 2005/2006 budget because of improving economic conditions.

It now appears that approximately $1.1 million in ongoing service reductions or revenue increases will be necessary in order to balance the Long Term Financial Plan and close the structural gap in the General Fund. This amount is shown on the *Fiscal Strategies* line item through FY 2012/2013.

In order to address the $1.1 million gap and provide some flexibility for dealing with future financial challenges, staff is recommending that a number of fiscal strategies be pursued. Some of these strategies involve revenue enhancement, and other involve reductions in cost.

First, staff has not included the revenues from the Emergency 911 Fee in the recommended FY 2005/2006 Budget because of the current legal questions. As soon as the legal issues are resolved, implementation in accordance with Council direction will provide approximately $2 million in needed new resources.

Second, staff is recommending that the Council pursue two other possible tax increases. The City's Transient Occupancy Tax and Business License Tax rates are lower than those of most of our surrounding communities. An increase in the Transient Occupancy Tax to the County average would generate about $900,000 and raising the Business License Tax could provide $750,000 - $1 million in additional funds. These tax rate increases are not included in the recommended FY 2005/2006 Budget pending Council consideration and subsequent voter approval. If approved, these two revenue increases would provide additional resources to address future challenges.

Meanwhile, staff is continuing to explore the cost saving strategies and ideas that were included in last year's budget. A list of these efforts is included as *Appendix B* to this Transmittal Letter. Finally, staff will be reviewing and prioritizing the $2.2 million in service reductions that have been identified and will bring back recommendations for Council consideration during the Mid-Year Review process.

Gas Tax Fund

The Gas Tax Fund is required by State law to account for gas taxes collected and allocated by the State. These taxes are levied on gasoline and other motor fuels in terms of cents per gallon, and these funds are then distributed to the State, cities and counties on a formula based on population. Revenue forecasts for this fund utilized year-to-date projected receipts increased by the Association of Bay Area Governments (ABAG) estimated population growth rate for Sunnyvale.

Beginning in FY 2001/2002 new state funding for streets and road systems, the State Traffic Congestion Relief Program (TCRP) has been held and accounted for in the Gas Tax Fund as required by state law. A complete discussion of this revenue source and the projects associated with it can be found in the *Major Project Efforts* section of this Transmittal Letter.

Gas Tax funds are spent on maintenance and capital related to public streets and highways. As noted in the previous discussion of the General Fund, the Gas Tax Fund works in tandem with the General Fund. Essentially, a level of Gas Tax funding for operations is established, with remaining funds used to cover Gas Tax-eligible capital projects.

Operating expenses programmed for street maintenance in this fund are $3.9 million for FY 2005/2006 and $2.2 million for FY 2006/2007. For the remainder of the first ten years, operating expenses vary from $2.05 million to $2.7 million each year. Operating expenses are slightly lower in the second ten years.

The recommended FY 2005/2006 Budget for the Gas Tax Fund has two capital projects totaling $220,000. The first is a continuing project in the amount of $20,000 annually plus inflation for the City's share of development costs associated with streets and roadways. The second is a new project in the amount of $200,000 for the installation of radar speed signs in schools areas.

The project administration expenditure in the Gas Tax Fund represents the in-lieu charge for Engineering Services that are expected to be utilized in supporting Gas Tax-funded capital projects. The cost is higher in the prior and current year of the Long Term Financial Plan because there were a number of larger projects that were programmed from Gas Tax revenues during that time period.

Finally, the recommended FY 2005/2006 Budget reflects a transfer to the Capital Projects Fund/Gas Tax Sub-fund of $170,956 to support the Roadway Rehabilitation on Various Streets project ($2,736) and provide $168,220 for the project administration costs associated with Gas Tax related projects in the Capital Projects Fund.

ENTERPRISE FUNDS

The Enterprise Funds of the City incorporate programs and activities that are either fully self-supporting by way of user charges and fees or partially self-supporting.

Those that are partially self-supporting require some level of transfer from the City's General Fund.

The City has three utilities that are fully self-supporting, including the Water Supply and Distribution Fund, Solid Waste Management Fund, and Wastewater Management Fund. Additionally, the SMaRT Station® Fund has been established to account for operations at the Sunnyvale Materials Recovery and Transfer Station, which is a partnership among the three cities of Sunnyvale, Mountain View and Palo Alto. This fund consists of two sub-funds, one used to account for SMaRT Station operations and the other used to account for equipment replacement needs.

In April 2005 Council approved the following rate changes as recommended by staff:

Utility	Rate Change
Wastewater	5.5%
Water	4.5%
Solid Waste	5.5%

Each rate increase and the factors contributing to the need for such increases are discussed in detail below. As a result of these increases, monthly costs associated with solid waste, water, and wastewater services for an average residential customer will increase by 5.2% overall. It is important to note that even with the rate changes, Sunnyvale residents enjoy utility rates that are approximately 30% lower than the average of surrounding communities. This amounts to annual savings of approximately $370 per household. Commercial customers also enjoy rates that are competitive with surrounding communities.

There is one enterprise fund that requires an annual transfer from the General Fund for operations because it is not fully sustaining. The Community Recreation Fund incorporates Leisure Services activities including golf, tennis, and recreation programs.

Water Supply and Distribution Fund

The Water Supply and Distribution Fund accounts for all revenues and expenses related to the City-operated water utility. Expenses include costs for wholesale water, project-related costs, debt service, and other operating costs. Revenues consist of service fees for water and recycled water, water-related public works and construction fees, and interest income. Once expenditure levels are developed, then water rates must be set to maintain the fund in a sustainable financial position. The fact that Sunnyvale utilizes long-range financial planning and sets utility rates every year helps minimize wild rate swings.

Sunnyvale currently receives water from four different sources. Approximately 42% comes from the San Francisco Public Utilities Commission (SFPUC), 45% from the Santa Clara Valley Water District (SCVWD), 5.5% from well water, and the remaining 7.5% from recycled water.

A significant portion (61.7%) of the Water Fund's direct expenditure budget is the cost of purchased water, so each year staff reviews the costs of wholesale water and the quantities planned to be purchased. The City currently purchases water from the two wholesalers at $492 per acre-foot for the SFPUC and $495 per acre-foot for the SCVWD. Our forecast anticipates a cost for FY 2005/2006 of $466 per acre-foot for SFPUC water and $510 per acre-foot for water purchased from SCVWD. As always, to the extent possible staff will attempt to purchase water from the least expensive source.

The City also receives charges in the form of a pump tax from the SCVWD for pumping ground water from City wells. The unit cost for well water is also influenced by the power costs associated with running the pumps. The projected well water total unit cost (tax plus power) for FY 2005/2006 is $503 per acre-foot.

Finally, the City's Water Pollution Control Plant (WPCP) provides recycled water as part of the Water Reclamation Project begun in 1993. Recycled water is wastewater that has been treated to very high standards. Recycled water currently provides landscaping water for the Sunnyvale Municipal Golf Course, Baylands Park, Twin Creeks softball complex, the SMaRT Station, and several commercial businesses in the Moffett Park area. The cost for recycled water is borne by both the Water Supply and Distribution Fund and the Wastewater Management Fund. The Water Fund distributes and sells recycled water and also benefits through reduced reliance on potable water sources. The Wastewater Fund benefits from the diversion of wastewater from discharge to the San Francisco Bay through reduced wastewater management regulatory requirements. In addition to these benefits, the City receives a $115 per acre-foot rebate from the SCVWD to encourage use of recycled water, which we are forecasting for the next five years in our financial plan.

Prior to preparing a Twenty-Year Water Forecast, staff obtains projections from each of the City's water wholesalers for next year and beyond. In general, each of the City's suppliers provides price projections for a one to ten year period. Staff then takes these numbers, factors in all known price increases, and projects water usage over the long-term plan to optimize the use of the least expensive sources of water within the terms of the contracts. Staff has received ten years of projections from SCVWD, five years from SFPUC, and an estimated additional five years of SFPUC rates from the Bay Area Water Supply and Conversation Agency (BAWSCA). BAWSCA is the agency which represents the "Suburban Users", a group of water retailers outside the City of San Francisco. Sunnyvale is one of 28 jurisdictions outside of the City of San Francisco who make up approximately 70% of the system's customers.

In March 2005, City staff received information from BAWSCA regarding a rate proposal from SFPUC for the next two years. In short, SFPUC had failed to complete scheduled capital improvements in a timely manner and therefore significantly overcharged the suburban users. In order to credit us for the overcharging, SFPUC was proposing to reduce our wholesale water rate by 9.8% effective April 2005 and hold the rate flat for FY 2006/2007. Sunnyvale and the other BAWSCA agencies agreed to implement this rate proposal which would avoid sharp rate fluctuations for our ratepayers. This approach has been reflected in our Long Term Financial Plan for the Water Fund.

The recommended FY 2005/2006 Budget assumes the proposed decrease of 9.8% for SFPUC and an increase of 3% for SCVWD. The Budget also includes the projections provided by SFPUC and BAWSCA through FY 2014/2015 and by SCVWD through FY 2011/2012. It should be noted that BAWSCA is projecting substantial rate increases for SFPUC in FY 2010/2011 through FY 2014/2015 to reflect completion of their ambitious Capital Plan. The projections provided by each agency are as follows:

	SFPUC	SCVWD
FY 2005/2006	-9.8%	3.0%
FY 2006/2007	0%	4.9%
FY 2007/2008	10.8%	2.8%
FY 2008/2009	6.3%	3.6%
FY 2009/2010	7.5%	5.3%
FY 2010/2011	34.3%	3.3%
FY 2011/2012	25.4%	3.2%
FY 2012/2013	20.4%	
FY 2013/2014	16.8%	
FY 2014/2015	14.5%	

Our experience tells us that the projections from the SFPUC are particularly unreliable, and subject to frequent change. Beyond the first ten years, the projections from SFPUC have been adjusted by staff to be no less than 6% to mitigate potential fluctuations in cost due to wildly varying SFPUC rates.

For the first five years of the Forecast, staff maximizes the use of SFPUC water to take advantage of the benefit provided by a rebate for recycled water. Starting in FY 2010/2011 the Forecast maximizes the use of well water, which is currently the City's most cost-effective source of water. However, the bulk of the water must still come from our wholesale suppliers as the wells are only able to generate a limited amount of acre feet. At this same point, the projected acre-feet taken from the SFPUC are essentially flattened for the remainder of the 20-year period. For this same period, there are slight increases in the use of SCVWD to meet the projected demand in FY 2024/2025.

In May 2002 the SFPUC approved a $3.6 billion Capital Improvement Program (CIP) and in November 2002, the San Francisco voters approved a $1.6 billion bond measure, the largest ever approved in city history, to fund the San Francisco portion of the project. The remaining portion of the CIP is to be funded by the Suburban Users.

Over the past few years, while the focus has been on the SFPUC capital improvement issues, Sunnyvale staff has been working to identify and scope projects to improve the City's own water supply and distribution system. In addition to the $3.4 million in capital and infrastructure projects included in the FY 2004/2005 Budget, the recommended FY 2005/2006 Budget proposes $27.5 million in water infrastructure projects and $8.8 million in water capital projects over the twenty year plan. Public Works staff have proposed a methodical and measured repair and rehabilitation plan

for the water supply facilities with the goal of extending infrastructure life by up to 100 years.

Following are some of the major capital and infrastructure projects included in the recommended FY 2005/2006 Budget and Long Term Financial Plan:

- **Refurbishment of Water Tanks at Wright Avenue:** This project provides $2,730,675 in funding to refurbish the two water tanks located at Wright Ave., inside and out, in accordance with a complete structural and coating evaluation done in 2004. Refurbishing the tanks is much more cost-efficient than replacing them, since the cost of replacing one tank can exceed several million dollars. Proper coating with the normal schedule of periodic tank maintenance should keep the tanks in useable condition for up to 40 years. For FY 2005/2006 the recommended funding is $1,540,000; an additional $1,190,675 is planned in FY 2009/2010 to complete the refurbishment of both water tanks.

- **Central Water Plant Building Reconstruction:** The Central Water Plant is a critical element of the City's water supply system. This project will provide $1,815,600 in funding during FY 2006/2007 and FY 2007/2008 to replace the existing structures and evaluate the existing equipment. Additionally, the project will provide funding to install a new propane generator, magnetic flow meter, and underground piping.

- **Equipment Replacement at Five Hetch Hetchy Connections:** This project provides $689,870 over three years for the replacement of pressure reducing valves, gate valves, limitorque valves and vaults and installation of magnetic meters at five connections (located at Lawrence, Fair Oaks, Borregas, Lockheed, Palomar, and Mary) to the Hetch-Hetchy water supply pipeline. The equipment is being replaced because of age and to provide upgrades allowing each facility to be connected to the City's Supervisory Control and Data Acquisition (SCADA) system. $111,000 is recommended for FY 2005/2006.

- **Earthquake Mitigation of Water Tanks:** The impact of tank failure during seismic activity is amplified by likely additional needs placed on the water system to protect public health and to provide fire suppression. This project will provide $1,986,000 to fund improvements to foundation connections by anchoring tanks to the ground and improve water inlet, outlet, and overflow connections by adding flexible couplets making them more reliable in seismic events. $150,000 is budgeted for FY 2005/2006 and the remainder the following year.

- **Pressure Reducing Valve Replacement and Relocation for SCADA:** Pressure reducting valves are an integral part of the water distribution system, providing balanced water pressure throughout the City. The valves are 40 to 50 years old, and the cost of preventive maintenance has begun to exceed replacement costs. This project provides $2,536,236 over twenty years starting in FY 2005/2006 to replace the City’s sixty existing pressure-reducing valves with new ones.

- **Hamilton Plant Emergency Generator and Mechanical Reconstruction:** This project provides $781,600 in funding to install an already-purchased emergency back up generator at the Hamilton Water Plant, including the pouring of a concrete pad base with electrical connections. $190,000 is programmed in FY 2005/2006 and $591,600 in FY 2006/2007.

- **City-Wide Water Line Replacement:** The integrity of the City's water supply system is critical to protect public health and safety. The success of these goals is dependent on the maintenance and eventual replacement of aged and worn infrastructure. Currently, many portions of the water system have exceeded their estimated life expectancy of 35 to 40 years. This project will provide $13,175,581 to begin the replacement of a total of 280 miles at a rate of 0.3 miles per year ramping up to 2 miles per year by 2011. Replacement will also upgrade pipes and fittings for seismic stability. $250,000 is budgeted in FY 2005/2006 for this project.

- **Interior Coating of Water Tanks:** This project funds $2,097,863 to remove the interior coal tar coating of five small water tanks and three large water tanks and will re-coat them to American Water Works Association standards. $581,400 is budgeted in FY 2006/2007 for the five small half-million gallon tanks, and the remainder of the project is scheduled in FY 2011/2012 through FY 2013/2014.

For FY 2004/2005 the City's method of accounting for capital and infrastructure projects in the utility funds was changed to reflect preferred practices, with capital projects and infrastructure projects are now reflected in the Water Fund Long Term Financial Plan directly. The transfer to the Infrastructure Fund has been reduced to reflect only those projects that are funded by multiple funds and therefore are properly reflected in another fund.

A new item on the Water Fund Long Term Financial Plan For FY 2004/2005 was the Municipal Utilities Infrastructure Fee. This is a new fee that was approved in concept in last year's budget process and was scheduled to take effect in FY 2004/2005. However, a study conducted during FY 2004/2005 by the Department of Finance found that it would be difficult to levy such a fee that would meet the legal requirements associated with Proposition 218. The recommended FY 2005/2006 Budget therefore removes this fee from the Long Term Financial Plans of the Water and Wastewater utilities. The study did conclude, however, that the direct charges to the utilities should be reviewed to ensure full cost recovery. Staff from Public Works and Finance are currently reviewing these charges.

The Water Supply and Distribution Fund carries a loan that was advanced from the General Fund for an original principal balance of $1,632,000. During FY 2002/2003 the City purchased property located at 239 Commercial Street to provide additional space for the Public Works Corporation Yard. The total purchase price of $2,530,000 was funded by the City's Water and Wastewater enterprise funds based on the number of staff located at the Corporation Yard. The Water Fund's share of the cost amounted to 64%, or $1,632,000. The Water Fund did not have sufficient funds for the purchase, and the General Fund loaned the Water Fund the total amount. The loan accrues interest of 6% starting in FY 2002/2003.

The recommended FY 2005/2006 Budget reflects an accelerated repayment schedule for the Interfund Loan. The revised schedule retains the same interest rate of 6% but accelerates repayment to only eight years. The repayment is now scheduled for FY 2007/2008 through FY 2014/2015. This change helps the Water Fund mitigate the impact of projected large increases in SFPUC water costs in the later years of the plan by bringing the loan payments forward and thereby freeing up rate revenue in the second ten years of the plan to absorb increased purchase water costs and keep rates stable.

The Fiscal Sub-Element of the City's General Plan calls for the Water Fund to maintain a Contingency Reserve of 25% of operations. This Contingency Reserve is to be used only in the event of disasters or other emergencies. The Water Fund also maintains a Rate Stabilization Reserve to smooth utility rates from year to year, levelize economic cycles and plan for project-related expenditures.

The rate increase approved by Council for water utility services for FY 2005/2006 is 4.5%, compared to the 5% anticipated last year. The projected rate increases anticipated over the remainder of the 20 years are shown at the bottom of the Water Fund Long Term Financial Plan. Also shown is the percent change in purchased water cost for each year. It is important to note that the water rate increases anticipated are in most cases significantly lower than the projected increases in the cost of purchased water.

Wastewater Management Fund

The Wastewater Management Fund accounts for the revenues and expenses related to the City-operated sewer collection and Water Pollution Control Plant (WPCP) services.

The City owns and operates an extensive system for management of wastewater (sewage) within City limits and in a small area in northern Cupertino. The system includes approximately 327 miles of sewer pipes and a 29.5 million gallon per day (MGD) Grade V Water Pollution Control Plant. Operations include the transport of sewage to the treatment plant, wastewater treatment, recycled water production, industrial discharge inspection and enforcement, and many other services related to wastewater. Although the WPCP has a 29.5 MGD capacity, it is currently processing about 15 MGD. One issue that will be explored in the coming years is whether it would be possible to make some of this capacity available to other nearby jurisdictions to help defray overhead and provide additional revenue to this fund.

Infrastructure maintenance and replacement has been and remains the largest issue for the Wastewater Management Fund. Portions of the treatment plant and collection system are approaching 50 years in age and are experiencing deterioration. For the past two years Public Works staff has worked to identify and isolate the cost and life span of the various pieces of infrastructure and schedule these into the Long Range Infrastructure Replacement plan. The recommended FY 2005/2006 Budget and Long Term Financial Plan reflects $65 million in infrastructure projects and $5.5 million in capital projects that have been identified for the 20-year planning period through this process.

The major infrastructure and capital projects in the Long Term Financial Plan are as follows:

- **Rehabilitation of Digesters and Replacement of Digester Lids**: Digesters at the WPCP are used to further degrade solid waste removed from the wastewater. The structural integrity of the digesters/lids must be maintained to prevent releases of potentially hazardous methane that could result in Bay Area Air Quality Management District (BAAQMD) violations. This project will provide a total of $9,365,735 for the design and construction of four replacement anaerobic digester covers and peripheral equipment. Construction costs are estimated at $1,750,000 per digester. Replacement will occur over the first five years of the plan.

- **Primary Sedimentation Basin Renovation Phase I**: WPCP primary treatment provides the removal of solids and floating material from the wastewater stream. The ten primary sedimentation basins that perform this task are old, the oldest of which were part of the original plant built in 1955. This project will provide for repair or replacement of the basins for a total project cost of $10,772,858. The work is scheduled beginning in FY 2007/2008 and ending in FY 2013/2014.

- **Air Floatation Tank Rehabilitation**: This project provides $3,375,048 in funds to rehabilitate and provide corrosion protection for the four Air Floatation Tanks at the WPCP. Air floatation tanks are used to remove the algae that grows during secondary treatment in the oxidation ponds. This project includes repair/replacement of the steel and mechanical portion of this structure, repair and/or replacement of the influent gates and coating of the concrete walls, extending their useful life for approximately 20 years. This project is scheduled over four years beginning in FY 2011/2012.

- **Fixed Growth Reactor Rehabilitation**: The fixed growth reactors at the Water Pollution Control Plant provide for the biological removal of ammonia from the wastewater stream. This project will provide funds to renovate the three fixed growth reactors. The project is scheduled to begin in FY 2014/2015 and will be completed in FY 2017/18. The total cost is budgeted at $6,921,685. The completion of this maintenance is expected to extend the life of the reactors another 20-25 years.

- **Replacement/Rehabilitation of Sanitary Manholes:** The sewer system infrastructure is on average 50 years old, with some parts considerably older. The system includes over 5,700 sewer manholes. This project provides $1,879,595 in funding to systematically replace or rehabilitate deficient manholes at a rate of about 10 manholes per year with an estimated cost of $7,500 per manhole. The project is expected start in FY 2005/2006 and be ongoing into the foreseeable future.

- **Replacement/Rehabilitation of Sewer Pipes:** The City has over 280 miles of sewer lines, in sizes from 6 inches to 36 inches in diameter. The value of these

lines is estimated to be in excess of $200 million. Many of these lines are 50 years old, or older. This project includes replacement or rehabilitation of approximately 3,000 feet per year at a total cost of $16,866,255 over twenty years. The project is scheduled to begin in FY 2005/2006 with a budget of $70,000.

- **Replacement/Rehabilitation of Storm Drain Pipes:** The storm system infrastructure is, on average, 50 years old. This project replaces or rehabilitates storm water pipes at an ongoing rate of 800 linear feet per year for a total cost of $1,141,140 over the second ten years of the project beginning in FY 2015/2016.

- **Storm Pump Station #1 Expansion:** Sunnyvale operates two storm pump stations to pump accumulated storm water into the San Francisco Bay. These are required for areas that are close to sea level and could suffer flooding, particularly during large storms and exceptionally high tides. The project budget consists of environmental permitting, engineering design, and dredging for a total cost of $1,892,277. This project is programmed to begin in FY 2012/2013.

- **Pond Sediment Removal:** The oxidation ponds provide secondary treatment using natural action of sun and wind to facilitate the growth of algae, which takes up dissolved waste from the wastewater. No solids have been removed from the ponds since the beginning of secondary treatment in the late 1960's. The current accumulation of solids is estimated at 35% to 45% of the pond volume. This project provides $11,960,699 over sixteen years beginning in FY 2005/2006, based on a recently completed pilot study, to remove sediment and improve pond capacity. $300,000 is budgeted for FY 2005/2006.

- **Sewer Lift Stations Rebuild:** The City currently operates five sewer lift stations which ensure proper flow of sewage through the sewer system. This project provides $1,033,248 in funding to overhaul pumps and rehabilitate wet wells, traffic covers, and electrical panels. The project is scheduled for FY 2010/2011 through FY 2014/2015. The next renovation should not be necessary for at least 10 to 20 years, with an appropriate level of maintenance.

The Wastewater Management Fund has two interfund loans that were advanced from the General Fund. The first loan was to finance the remodel of the primary facilities of the wastewater treatment plant, expanding the capacity from 22.5 million gallons per day to 29.5 million gallons per day. The loan was made by the General Fund in FY 1980/1981 for a total of $10.7 million at 7% interest. The original term was for 20 years. Payment of the loan began in FY 2004/2005.

The second loan from the General Fund was made to assist the Wastewater Management Fund with cash flow issues by providing needed cash to stabilize rates. The loan was advanced in FY 1995/1996 for a total of $2,453,635 at 7% interest. The term was for 20 years with ongoing payments on the loan deferred until FY 2004/2005.

The recommended FY 2005/2006 Budget reflects changes to the first loan, but no changes to the second loan. Payments on the first loan have been reduced for FY 2005/2006 and FY 2006/2007, deferred for FY 2007/2008 through FY 2009/2010, and increased for the remaining term of the loan. This change has mitigated the rate increases that would have been needed in the Wastewater Management Fund during the first ten years of the plan.

As with the Water Supply and Distribution Fund, the method of accounting for capital and infrastructure projects has changed beginning in FY 2004/2005. This change is reflected in the transfers in from the Capital Projects Fund and Infrastructure Fund of unexpended funds, and the capital and infrastructure projects that are shown directly in the Wastewater Fund starting in FY 2004/2005.

Environmental regulations continue to restrict numerous pollutants, requiring additional study and increased public outreach efforts to reduce the amount of pollutants reaching the San Francisco Bay. Staff is currently undertaking efforts to renew the City's discharge permit under these more stringent requirements. In prior years, three ongoing efforts related to our National Pollutant Discharge Elimination System (NPDES) permit and the control of non-point source discharges were shown in this fund as special projects. Since they are ongoing and are actually operational in nature, these projects were folded into operations for FY 2004/2005.

As with the Water Supply and Distribution Fund, the establishment of a Municipal Utilities Infrastructure Fee to the General Fund was projected starting in FY 2005/2006. Payment of this fee has been eliminated for reasons that have been discussed in more detail in the section of this Transmittal Letter dealing with the *Water Supply and Distribution Fund.*

One new cost reflected in the Wastewater Management Fund Long Term Financial Plan starting in FY 2005/2006 is a charge for rent for use of the land that the Water Pollution Control Plant occupies. The WPCP resides on approximately eight acres of land. Currently, the City's General Fund receives no revenue from the Wastewater Management Fund's use of this land, even though the Wastewater Fund receives a benefit for its use. Taking into consideration the location and values of comparable land in the Moffett Park industrial area, discounting for the proximity to and complications associated with the Sunnyvale Landfill and Sunnyvale Materials Recovery and Transfer Station, staff is recommending that the General Fund be reimbursed $12.17 per square foot for the use of the land, for a total payment of $296,748. This payment is reflected for the full term of the plan, adjusted for inflation.

The Wastewater Management Fund by policy maintains a Contingency Reserve of 25% of operations and a Rate Stabilization Reserve to levelize rates and provide for the effect of economic cycles.

The rate increase approved by Council for Wastewater services for FY 2005/2006 is 5.5%, half a percent higher than last year's projection. Annual rate increases for the remainder of the planning period are shown at the bottom of the Long Term Financial Plan.

Solid Waste Management Fund

The Solid Waste Management Fund accounts for the revenues and expenses related to collection, recycling, and disposal of solid waste generated within the City of Sunnyvale. A private company, Bay Counties Waste Services, doing business in Sunnyvale as Specialty Solid Waste & Recycling ("Specialty"), has been issued an exclusive franchise for collection of refuse and recyclable materials, and these contract costs are reflected here. Operations of the Sunnyvale Materials Recovery and Transfer Station and disposal of refuse at the Kirby Canyon Landfill are included in a separate fund, but the City's share of these activities is reflected in the Solid Waste Management Fund.

In budgeting for municipal solid waste management expenses, the most significant factor influencing revenues and expenses are tons of solid waste collected, transferred, and disposed. Staff begins preparation of the Solid Waste Long Term Financial Plan by projecting the amount of material that is anticipated to be delivered to the SMaRT Station. For forecasting purposes, staff has separately projected residential and commercial/industrial tonnage. Residential projections are based on new housing forecasts and are expected to remain relatively flat. The commercial/industrial forecast is based on the 8-year economic cycle of tonnage that is reflected in historical data for the Solid Waste Fund. These projections closely reflect the same economic cycle that has been used to forecast the City's Sales Tax, Property Tax, and construction-related fees. Revised tonnage projections for FY 2005/2006 are down slightly from last year's anticipated projections. As mentioned earlier, tons increase and decrease trending the assumed economic cycle.

One issue that was identified in last year's budget for the Solid Waste Fund was the proposed extension of the Specialty contract. In December 2004 Council awarded a contract extension to Specialty. The effects of this action are included in the recommended FY 2005/2006 Budget. Notably, a one-time accrued depreciation savings from Specialty in the amount of $907,389 is reflected in FY 2004/2005.

As mentioned earlier, the City contracts with Specialty for the collection of solid waste and recyclables throughout the City. Specialty is paid on a monthly basis, but their payment is determined once a year through a contractor payment review process. The contractor payment for the following fiscal year is driven primarily by actual expenditures from the prior year that are adjusted by various indexes as identified in the contract.

The projected FY 2005/2006 contractor payment is up $871,732, or 5.8%, from the prior year's projection. The largest increase occurs in labor costs which are up $630,000 due to increases in health care and worker's compensation costs. Total vehicle costs are up $180,648 due to increases in the cost of diesel and natural gas fuel. Finally, the Producer Price Index which is used to adjust the other miscellaneous costs rose by 8.8%. The total increase in contractor payment has been included in the recommended FY 2005/2006 Budget, but staff has flattened the projected contractor payment for FY 2006/2007 on the assumption that the increase in labor costs is largely due to a catch up period resulting from a payment methodology change under the new contract.

The recommended FY 2005/2006 Budget for the Solid Waste Fund includes increased costs for a project at the SMaRT Station to replace the two materials recovery lines. This project will be discussed more fully later in the section of this Transmittal Letter on the *SMaRT Station Fund.*

One new cost that was reflected in the Solid Waste Fund Long Term Financial Plan starting in FY 2004/2005 was a charge for rent for use of the land that the SMaRT Station occupies. The SMaRT Station is located on a parcel of land also occupied by the landfill that records indicate was originally purchased by the City with the intent of establishing a park. The facility resides on 9.5 acres of land. Previously the City's General Fund received no revenue from the Solid Waste Management Fund's use of this land, even though the Solid Waste Fund receives a benefit for its use. Taking into consideration the location and values of comparable land, a new charge was levied to reimburse the General Fund $11.25 per square foot for the use of the land. This payment is reflected for the full term of the plan, adjusted for inflation.

The Solid Waste Management Fund Long Term Financial Plan reflects two interfund loans from the General Fund. The first loan provided $3.68 million during 1985, 1988, and 1989 to construct a system to convert methane gas to a marketable form of energy. An additional $10.5 million was advanced for the purpose of stabilizing solid waste rates between FY 1994/1995 and FY 1998/1999. Both loans bear interest of 7%. The loans have since been combined and their original terms were to have them paid off over 29 years. Initial repayment began in the current fiscal year and continues through FY 2023/2024.

An additional loan was made from the Water Supply and Distribution Fund to the Solid Waste Management Fund in the amount of $1.7 million to fund a portion of the cost to close and place a final cover on the Sunnyvale Landfill. That loan will be paid off in FY 2004/2005.

By fiscal policy, the Solid Waste Fund maintains a Contingency Reserve of 10% of operations. This is less than the 25% required for the other two utility enterprises to reflect that fact that this operation has less risk for damage or disaster. The Fund also maintains a Rate Stabilization Reserve similar to the other utilities.

The rate increase adopted by Council for FY 2005/2006 is 5.5%, one percent higher than planned last year. The projected rate increases for the remainder of the planning period are reflected at the bottom of the Solid Waste Management Fund Long Term Financial Plan.

Sunnyvale Materials Recovery and Transfer (SMaRT) Station

The Sunnyvale Materials Recovery and Transfer Station Fund consists of two sub-funds. The SMaRT Station Fund accounts for operations at the SMaRT Station and receives its revenue from charges to the cities of Sunnyvale (Solid Waste Management Fund), Mountain View, and Palo Alto. Major operating cost components include the contract with Green Team/Zanker, the SMaRT Station operator, and disposal fees and taxes collected by the Kirby Canyon Landfill. The fund is designed so that annual

revenues and expenditures are in balance and that no fund balance is carried forward to the next year. Operating costs and revenues from the sale of recyclables are charged to or distributed to the cities based on the numbers of tons of solid waste each community brings to the SMaRT Station for materials recovery, transfer, and disposal.

The SMaRT Station Fund shows decreases in both revenues and expenditures over the planning period based on updated tonnage projections submitted by all three participating cities. SMaRT operations are affected by the same economic conditions that were discussed earlier in relationship to the City's Solid Waste program. Large swings in tonnage projections are anticipated to be seen in future SMaRT Station Fund Long-Term Financial Plans in response to economic cycles, the independent solid waste management strategies of the three cities, and other factors.

The SMaRT Station Replacement Sub-fund provides for the replacement of City-owned SMaRT Station equipment. The three participating cities contribute to these replacement efforts and to payment of debt service based on fixed percentages established by the SMaRT Station Memorandum of Understanding (MOU) among the cities.

For FY 2005/2006, the SMaRT Station Fund reflects the impacts of the recommended replacement of the two materials recovery lines at the SMaRT Station. Staff has scoped a project to replace both material recovery lines with new equipment, which are deteriorating due to age, that will meet the following goals:

- Update the facility with current materials recovery technology
- Reduce the amount of equipment downtime and repair
- Increase the diversion of recyclables from the waste stream
- Increase the revenues from the sale of recyclables
- Reduce landfill disposal costs
- Reduce operating (labor) costs

The project will take an initial investment from the three partner cities of $5,000,000. However upon completion, the project will reduce ongoing costs and increase revenues so as to save a net present value of approximately $11 million over the twenty years of the plan. This is reflected in the SMaRT Station Operating Sub-Fund's operating line items, and through the contributions to the SMaRT Station Replacement Sub-fund. Both reflect increases in the first ten years, and decreases in the second ten years which result in long term savings to the partner cities.

The recommended FY 2005/2006 SMaRT Station Long Term Financial Plan reflects debt service for the original cost of the facility through FY 2017/2018. The MOU with Palo Alto and Mountain View continues through October 2021. Staff projects that while most of the equipment can be maintained in good working order through the term of the MOU, there will come a point when major equipment and the structure itself will need replacement. In order to project the cost impact of this eventuality, staff has projected the debt service to continue at the existing level beyond the term of the MOU.

One issue that may have a significant fiscal impact on the SMaRT Station is the current status of the contract between the City and Green Team/Zanker, which requires the operator to pay its workers prevailing wages if a wage determination is made by the State Department of Industrial Relations (DIR). An initial wage determination is currently under reconsideration by DIR. Depending upon the outcome, operating costs at the SMaRT Station could increase by $2 to $2.5 million a year. This would equate to an additional rate increase to Sunnyvale refuse customers of 4.4% attributable to the prevailing wage issue. The SMaRT Station contract is due to expire at the end of 2007 and the impact of the DIR final determination will undoubtedly carry over to the next operating contract negotiations.

Community Recreation Fund

This fund, which was created in FY 1991/1992, contains the leisure service activities of the City, including the two City-operated golf courses, the tennis center, and recreation classes and services. Prior to the initiation of the Fund, leisure services were part of the General Fund. The creation of the Community Recreation Fund included the merger of the City's golf and Tennis Center operations with the remainder of all other leisure service activities, as well as the adoption of new, entrepreneurial approaches to service delivery. This approach resulted in a significant reduction in the General Fund subsidy that would have been required to support leisure services in Sunnyvale going forward.

The recommended FY 2005/2006 Budget for the Community Recreation Fund includes a number of key issues for Council consideration, as discussed below.

Golf Services

Golf operations continue to be the greatest single source of revenue for this Fund, providing over $1.6 million of direct net profit to the Fund in FY 2003/2004 to support other subsidized recreation services. Sunnyvale's golf courses are on track to again generate a substantial overall profit for FY 2004/2005. However, the general decline in the golf market place, as well as the local and state economy has continued to have a negative effect on planned golf revenues, and that will be reflected in year-end results. Staff estimates that the two courses will generate several hundred thousand dollars less in green fees than planned for this fiscal year. As a result of this decline in play, related revenue streams such as merchandise and golf car rentals will also finish the year below planned amounts. As approved in June 2004, golf green fees were increased and the first-ever Tournament Fees were implemented at each course on April 1, 2005. On May 1, 2005 the new Tournament Fee at Sunnyvale Golf Course was increased from $2.00 to $2.50 per player.

Future year projections of golf revenues take into account the changing market place for golf. As several new up-scale courses have been developed or renovated in this area and golf play as a whole has decreased, some of these up-scale courses are now competing for our market share. Future planning figures project a long-term decrease in golf rounds for both Sunnyvale golf courses as a result.

Since the peak in FY 1998/1999, the number of rounds at Sunnyvale golf courses has slowly but steadily decreased by approximately 16%. Staff had previously estimated that golf revenues would stabilize in FY 2004/2005 and begin to show measured signs of growth starting in FY 2005/2006. Staff now believes that a significant and consistent improvement over the life of the plan is unlikely. Based on current golf play statistics, staff projects a decrease in golf related revenues by an annual average of $500,000 throughout the remainder of the Long Term Financial Plan. This decrease in revenues means that less net profit is available to support other recreation programs.

Council's continued support of market-based golf fees regardless of residency or age (with the exception of monthly discounts for residents, seniors, youth and disabled golfers) remains a critical factor in maintaining this important revenue stream.

Senior Lunch Program

Early in FY 2004/2005 the City's Senior Lunch Program vendor (Bateman Senior Meals) notified the City of its intention to withdraw from our service contracts. To meet the service needs, Council approved temporary services through Bateman for the Senior Lunch Program. However, customer satisfaction was low and costs exceeded planned amounts. In March 2005 Council authorized a Budget Modification in the amount of $80,000 to cover costs to the end of the fiscal year and supplemental funding of $25,000 to fund the Program for a few months of FY 2005/2006. Council directed staff to consider short and long term solutions to this service including a Request for Proposals (RFP) process for a future service provider. The recommended FY 2005/2006 Budget reflects this action which results in a cost increase of $25,000 for senior lunch services. Upon completion of the RFP process, staff will return to Council for direction regarding the senior lunch program.

Fee Waiver Program

The fee waiver program is an important component of the City's delivery of leisure services. It allows the economically disadvantaged to participate in programs by defraying the established user fees. During FY 2004/2005 the program experienced increased costs in two areas – Participant use of Fee Waivers and Administrative Services for the Program.

Participant use of fee waivers increased well beyond planned amounts resulting in the need for Council action to avoid spending beyond approved budgets. In April 2005 Council authorized a $76,000 Budget Modification to continue the program for economically challenged residents through the end of the fiscal year. While fee waiver use and demand on the planned budget can fluctuate greatly from year to year, several related topics require more study and direction in the coming year to better understand the needs of the community and focus resources accordingly. An additional Study Issue covering these topics will be proposed for calendar year 2006, and would explore changes in eligibility for fee waivers as well as limitations on the types of programs to which fee waivers would apply.

New Administrative costs for the fee waiver program were incurred as Sunnyvale Community Services (SCS), the longtime non-profit administrator of the program,

experienced increasing operating costs. As a result, SCS was no longer able to administer the fee waiver program at no cost to the City as it had in previous years. Council approved a $10,000 payment to SCS for administration of this program for FY 2004/2005. Staff and SCS believe the collaborative relationship between the two parties should continue for the coming year. However, staff continues to examine potential for new technologies and/or organizational restructures that could allow cost-effective direct provision by the City of all or part of the administrative functions for participant eligibility, registration and activity participation. Council will review a separate report on administration of the Program before the current fiscal year-end.

Swirsky Youth Opportunity Fund Transfer

Beginning in FY 2004/2005 a portion of the interest generated by the Dorolou Swirsky Youth Opportunity Fund is being transferred to the Community Recreation Fund for supplementing the fee waiver program. In April 2005 Council approved the continuing use of 2/3 of the interest earnings by the Community Recreation Fund as recommended annually by the City Manager. More details on the Swirsky Fund and this transfer can be found later in this Transmittal Letter in the *Fiduciary Funds* section.

Infrastructure Projects

The City maintains and funds a planning system for repair and replacement of significant pieces of City infrastructure. To mention a few, items include roofs and heating/air conditioning systems, pool renovations and recreational equipment. Those projects and items relevant to the Community Recreation Fund have been listed in the *Current Requirements* section and, in past years have required several thousands of dollars of funding. As a part of the Capital Projects focus for this fiscal year, staff has reviewed funding sources for these infrastructure projects and has determined that infrastructure projects and equipment on park lands can and should be funded through the Park Dedication Fund. Therefore, future costs for infrastructure projects and equipment are no longer noted in the Community Recreation Fund.

General Fund Subsidy

The recommended FY 2005/2006 Budget provides $11 million worth of diverse leisure services to the community with a total subsidy from the General Fund of $3.2 million. Approximately $966,000 of this subsidy is returned to the General Fund to cover administrative in-lieu costs, making the net subsidy $2.2 million. The remaining $7.8 million of cost will be paid primarily by the direct beneficiaries of the programs in the form of user fees.

When the Community Recreation Fund was established in FY 1991/1992 the General Fund subsidy was approximately $2 million, with $91,000 returned to the General Fund for in-lieu charges. When converted to today's dollars, the same level of subsidy would be $3 million, and the in-lieu charges would be $138,000, for a net subsidy of $2.9 million. As this information indicates, over the intervening years the subsidy has held constant and in fact reduced slightly. This has occurred in spite of the fact that

the service level approved by the Council has increased (e.g. teen services, Fremont Pool, new Senior Center).

However, regardless of how well this Fund operates, the fact that it requires a subsidy and is dependent upon the General Fund necessitates that it be examined during times of fiscal crisis or retrenchment. A fundamental tenet of this Fund is that it can always reduce costs to the point of becoming self-sufficient by reducing or eliminating services. The dilemma, of course, is that the services that would need to be eliminated to achieve a reduction in the subsidy are those that are the least attractive to reduce from a public policy perspective. They are those that serve our youth, senior, disabled and low-income populations. Most other recreational programs pay for themselves or generate a slight profit.

Structural Imbalance

The recommended FY 2005/2006 Budget is balanced using a General Fund transfer of $3.2 million, the same level as projected last year. However, this is not sufficient to cover the full difference between revenues and expenditures in this fund.

As was the case in the previous year, staff has retained the General Fund subsidy at its previously projected levels, adjusting upward, as needed, the line for "*Fiscal Strategies*". This line notes $650,000 shown in the *Current Requirements* section and reflects the amount that the Community Recreation Fund will have to decrease its expenses (or increase its revenues) starting in FY 2006/2007 in order to continue to be in balance and not draw further on the General Fund. Staff anticipates that the Community Recreation Fund will end the current year with about $1.2 million in the 20-Year Resource Allocation Plan (RAP) Reserve due to operating savings related to unfilled positions in recreation services this year. Unfilled positions in this division are a significant concern, as the *Fiscal Strategies* and related service level adjustments have not yet been addressed formally.

Because Parks and Recreation staff are continuing to provide high levels of diverse services with reduced staff, they have been unable to quickly develop recommendations for more permanent plans. In the meantime however, those savings found through maintaining vacancies have helped to offset losses in golf and other recreation revenues. The budget proposal utilizes the 20-Year RAP Reserve to balance the Fund for FY 2005/2006. Staff is in the process of creating a plan of *Fiscal Strategies* to decrease expenses and maximize revenues by the needed amount.

As stated in the previous year, staff believes that this is possible by utilizing the following strategies:

- **Manage demand so as not to increase services unless they are self-sufficient**
- **Maximize Golf revenues**
- **Explore alternate ways of providing subsidized services at a lower cost**
- **Continue creative partnerships with outside groups to reduce costs**
- **Maximize other Community Recreation Fund revenues by charging market based fees wherever possible**

Staff will be looking at these strategies during FY 2005/2006 and will return to Council with recommendations designed to contain or reduce the General Fund subsidy. At that time staff will also present options for service level adjustments with potential reductions in highly-subsidized services to the City's youth, seniors, economically disadvantaged and disabled populations. With this information, Council may also evaluate the balance between recreational services provided to the community and the amount of General Fund subsidy that is needed to support those services.

The recommended FY 2005/2006 Budget and Ten-Year Resource Allocation Plan includes no new capital projects in the Community Recreation Fund. The Fund contains two small reserves. The first, *Co-op Sports Reserve*, reflects requirements of a contract that the City has with the Sunnyvale School District to administer the after school intra-mural sport league programs at Sunnyvale Middle School and Columbia Middle School. The reserve carries over funds for the Sunnyvale Middle School program, which generally brings in more revenue from participant fees than is needed to cover direct program costs. The reserve funds are used to purchase equipment and uniforms as needed by the school.

The second reserve is the 20-year Resource Allocation Plan (RAP) Reserve, which functions here as in other funds, to levelize expenses and revenues over the planning period. As stated earlier, we expect the 20-Year RAP Reserve to end FY 2004/2005 with $1.2 million that will be drawn down to maintain existing service levels in FY 2005/2006 while more permanent recommendations to balance the Fund are developed.

SPECIAL REVENUE FUNDS

Special Revenue Funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes.

Housing Fund

The Housing Fund is comprised primarily of revenues from federal HOME grants, housing mitigation funds, and Below-Market-Rate ("BMR") receipts. Expenditures are for capital and special projects targeted to achieve the goals of the City's Housing and Community Revitalization Sub-Element of the General Plan and the 2000-2005 Consolidated Plan. The Consolidated Plan is a five-year comprehensive planning document submitted to the federal government. It identifies a jurisdiction's overall needs for affordable housing and non-housing community development. The federal government requires the City to submit annual updates during the intervening years of the Consolidated Plan, and this is generally done in May of each year. Staff has prepared an updated Consolidated Plan for 2005-2010 which will be considered by the Council in May 2005.

Housing Mitigation Sub-Fund

Housing mitigation funds are maintained in a separate sub-fund, accruing interest solely for housing mitigation purposes as required by law. This fund shows receipts through FY 2004/2005, reflecting the final payment from Applied Materials for the fees on their Arques campus development. Housing Mitigation Fees are collected on certain high intensity industrial developments, and at this time staff does not anticipate any such new developments in the foreseeable future.

During the first ten years of the Long Term Financial Plan, the Housing Mitigation Sub-fund has two other specific sources of revenue. The first, Real Property Sale, represents the sale in FY 2009/2010 of an affordable housing unit in the downtown area that will be purchased by the Housing Mitigation Sub-fund from the General Fund in FY 2005/2006. The second, Housing Loan Repayment, reflects an estimate of repayments starting in FY 2009/2010 on the City/Public School/Child Care employees loan program discussed below.

Interest income on the reserve balances in this sub-fund continues to accrue and is available for programming to future housing mitigation projects.

Beginning in FY 2001/2002, Council appropriated Housing Mitigation funds for the Housing Assistance for Teachers and City Employees special project. The program consists of three components: Homebuyer Education, Security Deposit Loan Program and Down Payment Assistance Program. This project has a current budget of $2.5 million in FY 2004/2005. Staff has proposed to utilize these existing funds during FY 2005/2006 and then program an additional $200,000 annually for this project starting in FY 2006/2007.

Funds in the amount of $550,000 are identified for FY 2005/2006 for the purchase of one property suitable for affordable housing. This is a single family home at 388 Charles Street in downtown, currently owned by the General Fund. Although this house was purchased with General Funds, it is being rented to low and moderate income tenants. Therefore, staff believes that it is more appropriately owned by the Housing Mitigation Sub-fund. As indicated earlier, it is expected that this property will be sold in FY 2009/2010. The Charles Street property is expected to generate $16,200 in annual rental revenue and require $2,500 in annual maintenance costs until it is sold.

Following the proposed purchase in FY 2005/2006, the Housing Mitigation Sub-fund is projected to have a Housing Mitigation Reserve balance of approximately $6.7 million. These funds are available to be loaned to non-profit agencies for affordable housing projects in the City as they are identified.

HOME Sub-Fund

HOME funds are also maintained in a separate sub-fund of the Housing Fund. The City has been notified that its allocation of these monies for FY 2005/2006 totals $747,978. These funds are being recommended in FY 2005/2006 for the following activities: Operations ($74,798), Community Housing Development Organizations ("CHDO") Project ($112,197), and HOME projects ($560,983). In FY 2006/2007,

$615,081 is programmed for Future Home Projects. This is a placeholder for the remaining HOME monies that are not designated for specific projects but generally target the goals of the City's General Plan and the 2000-2005 Consolidated Plan.

Other Grant Supported Housing Sub-Fund

Finally, the Housing Fund has a third sub-fund that contains BMR and other grant-supported housing activities. Revenues in this sub-fund include housing monitoring fees, BMR processing fees, housing loan repayments, revenues from BMR code violations, and interest earnings. Expenditures are operating costs associated with maintenance and monitoring of the BMR program ($102,848) and two special projects ($580,720). One on-going special project in this sub-fund provides for the auditing of BMR participants to ensure compliance with program regulations. The second special project provides $540,000 each year through FY 2007/2008 for First-Time Homebuyer Support.

The Other Grant Supported Housing Sub-fund maintains two reserves. The first is the BMR In-Lieu Reserve which is to be used for BMR related activities. The second is the 20-year Resource Allocation Plan Reserve which is used here as in other funds to levelize spending or provide funds for capital expenditures.

Community Development Block Grant (CDBG) Fund

The Community Development Block Grant Fund consists of two sub-funds which account for revenues from Community Development Block Grants and the repayment of commercial and residential loans. Primary expenditures are for operations, housing opportunities, special projects, and most of the City's outside group funding efforts.

Community Development Block Grant Sub-Fund

This sub-fund accounts for Community Development Block Grants from the federal government. The Federal Government has notified the City that its FY 2005/2006 entitlement will be $1,418,817, which is 9.4% lower than the FY 2004/2005 allocation. Similar to the long-standing strategy used with all federally financed programs, future grant receipts are not shown beyond the fiscal year in which the entitlement amount is known.

Traditionally, CDBG funds are used primarily to address the City's affordable housing strategy. This includes support of housing and human service agencies; rehabilitation and retrofitting of the existing housing stock; and the acquisition, rehabilitation, and construction of affordable housing by non-profit developers. As in the Housing Fund, capital and special projects are targeted to achieve the goals of the City's Housing and Community Revitalization Sub-Element of the General Plan and the 2000-2005 Consolidated Plan. Additionally, by regulation, CDBG funds may be used for programs or projects that benefit groups with special needs such as senior and handicapped citizens or for targeted geographical areas that meet certain income requirements.

Expenditures programmed in FY 2005/2006 for the CDBG Sub-fund include $505,743 for operations and a transfer of $12,000 to the General Fund for update of the City's Housing Element of the General Plan.

The recommended FY 2005/2006 Budget includes $350,000 for Outside Group Funding of seventeen local agencies. Special projects are proposed in the amount of $352,800 for activities that include: the Home Access, Paint and Emergency Repair Program (($80,000), Fair Housing Services ($30,000), the City's ADA Curb Retrofit project ($150,000), Neighborhood Support/Education ($79,000), First Methodist Senior Nutrition Site Improvement ($6,000), and Analysis of Impediments Update ($7,800).

Two capital projects are proposed for FY 2005/2006 utilizing CDBG funds. The first appropriates $215,000 for Murphy/Evelyn Avenues Sewer Infrastructure Improvements to reline or replace sewer mains and service connections in the downtown area. The second provides $311,990 for the Manhole Reconditioning Project, which reconditions 34 sewer manholes in the area bounded by Mathilda, Washington, Sunset and Evelyn Avenues.

Details of the Special and Capital projects are included in *Volume II, Projects Budget.*

CDBG Revolving Loan Sub-Fund

The Revolving Loan Sub-fund was established by Council action in 2001 and separated for accounting purposes in FY 2003/2004. This revolving fund was created to provide a practical budgetary management tool to deal with program income from housing loans made with CDBG funds and to provide greater flexibility in the management of the City's housing assistance programs.

The Revolving Loan Sub-fund has two sources of revenue. The first is housing loan repayments, which consist of payouts of deferred loans and regularly scheduled monthly payments. These repayments are expected to total $600,000 in FY 2005/2006. The loan repayment projected out over the 20-year plan reflects staff's estimate of deferred and regularly scheduled payments based on the City's loan portfolio. The second source of revenue to this sub-fund is interest earnings on any available cash balances.

The recommended FY 2005/2006 Budget contains two special projects for the Revolving Loan Sub-fund. The first is Housing Rehabilitation Loans which are provided to existing rental properties that serve low-income households. Funds are budgeted in a total amount of $600,000 next fiscal year to provide approximately 15 loans in amounts varying from $20,000 to $60,000. This project continues each year throughout the financial plan in varying amounts.

The second special project is for Housing Acquisition projects by non-profit developers to maintain the City's stock of affordable housing units. $500,000 has been budgeted one-time in FY 2005/2006 with no ongoing appropriations. However, the 20-Year Resource Allocation Plan Reserve is projected to increase substantially as loans are repaid and staff anticipates that these funds will be used as high-priority projects become available.

Park Dedication Fund

The Park Dedication Fund was established to meet statutory requirements regarding the accounting for park dedication monies. In general, the City collects park in-lieu fees for multi-family residential projects that do not dedicate land for use as parks or open space. This fee is now calculated on an average fair market value per square foot as determined by the Community Development Department annually. These revenues are recognized in the Park Dedication Fund, and then available resources are appropriated here or transferred to the Capital Projects Funds for designated and approved park-related projects. Revenues in this Fund also include rental income from certain houses that the City purchased with Park Dedication Funds in anticipation of park expansion projects.

In past years, this fund was earmarked to help cover the costs of approved park-related projects, but because the amount of funds received was relatively small and unpredictable, the General Fund has funded the vast majority of past park projects, with the Park Dedication Fund simply an additional funding mechanism to periodically offset costs planned in the General Fund.

It is estimated that $1.2 million will be received by the end of FY 2004/2005. Staff from the Community Development Department project that residential development subject to the Park Dedication Fee will be high for the next three years, FY 2005/2006 through FY 2007/2008 and that about $10 million in fees will be received over that time period. A portion of this increase is attributable to the fact that the Park Dedication Fee rate is expected to rise from the current $55 per foot to $75 per foot starting July 2005.

Residential construction subject to Park Dedication Fees is projected to cease in FY 2008/2009 through FY 2012/2013 in keeping with the construction development cycle that the City has utilized to forecast its building related revenues. The cycle is expected to improve starting in FY 2012/2013, with revenues being received beginning in FY 2013/2014 at a much reduced level. The projection does not include any additional Park Dedication Fees in the later years of the plan.

The Park Dedication Fund also receives rental income from six houses that the City purchased in anticipation of expanding Murphy Park and Orchard Gardens Park. Currently, neither expansion project is funded in the Capital Improvement Program, and so the rental income has been included for the full twenty years of the planning period.

In the recommended FY 2005/2006 Budget one other small revenue is included in the Park Dedication Fund. This is $38,320 in Proposition 12 grant funds, which constitute the remaining funds not yet programmed. The balance of the City's Proposition 12 funds have been received and programmed in the Infrastructure Rehabilitation and Replacement Fund.

The Park Dedication Fund receives interest earnings on its unexpended fund balance. For FY 2005/2006 this is estimated to be $223,118.

To date, the largest single appropriation of Park Dedication Funds has been for the design and construction of the Plaza del Sol. A total of $4,424,405 was spent in support of that project from these fees. Park Dedication Funds have also been used for the Fair Oaks Skateboard Park and Playground Improvements at Ortega Park. Park Dedication Funds have also been appropriated to the Historical Society Museum Project in the amount of $500,000.

Recognizing the financial difficulty being experienced by the General Fund over the next several years, the recommended FY 2005/2006 Budget adopts a new fiscal strategy for the Park Dedication Fund. This strategy transfers the total responsibility for the City's Parks-related capital and infrastructure projects to the Park Dedication Fund, thereby relieving the General Fund of these costs. A total of $23.7 million in capital and special projects and transfers to the Community Recreation, Capital Projects and Infrastructure Rehabilitation and Replacement funds are programmed throughout the 20-Year Plan.

For FY 2005/2006, funds in the amount of $504,468 are projected to be transferred to the Infrastructure Rehabilitation and Replacement Fund for six projects. These include: Community Center Buildings Rehabilitation ($26,878), Park Furniture and Fixtures Replacement ($60,000), Park Building Roofs ($248,513), Raynor Activity Center Site Improvements ($37,577), Columbia Gym Wall Pads ($9,500), and Swim Pools Infrastructure ($122,000).

In addition to major infrastructure projects, there are two capital projects that are anticipated to be funded from Park Dedication Funds within the first ten years of the plan. The first is $1,040,400 programmed for Park Land Acquisition in FY 2007/2008. The second is $2.6 million of Plaza del Sol Phase II, which is scheduled for FY 2011/2012 and FY 2012/2013.

Details of the special and capital projects are included in *Volume II, Projects Budget*.

Asset Forfeiture Fund

The Asset Forfeiture Fund was established to account for monies received through drug and other law enforcement activities as allowed under Federal and State asset forfeiture guidelines. The purposes for which asset forfeiture can be used are limited, and funds are drawn down for new one-time expenses targeted for law enforcement services. As this is done, caution should be used to assure that these expenses are ones that fit into the City's priorities and that don't lead to unnecessary future liabilities.

It is expected that the Asset Forfeiture Fund will end FY 2004/2005 with about $1.6 million in reserves and it is not anticipated that any further funds will be received over the Long Term Financial Plan. The Fund does earn interest revenue on its unexpended balance. For FY 2005/2006 this is projected to be about $46,000.

The recommended FY 2005/2006 Budget includes one small operating expense in this Fund to cover allowable ongoing costs related to the yearly asset forfeiture audit. In

addition, it includes a continuing transfer to the General Fund to support juvenile diversion activities within Police Services. The City currently has an agreement with the County of Santa Clara to pay for the direct salary, not including benefits, of one Deputy Probation Officer. For FY 2005/2006 this amount is $83,622.

The recommended FY 2005/2006 Budget includes $173,000 for a capital project for Police Services Equipment Acquisition. In addition, $80,400 is programmed for two new special projects to be funded from the Asset Forfeiture Fund. These include: Public Safety Case Management System Implementation ($18,000) and Property and Evidence Purge Project ($62,400.) Also anticipated are two transfers to the General Services Fund Technology Sub-fund for the Storage Area Network project ($14,388) and the Network Security project ($10,260) for the Police Services pro rata portion of these efforts. Finally, a transfer to the Infrastructure Rehabilitation and Replacement Fund in the amount of $45,565 is programmed for the Police Services portion of the Security Access Control System Replacement project.

Assuming that no new asset forfeiture monies will be received in the future, the Asset Forfeiture Fund is projected to be depleted by FY 2014/2015.

Police Services Augmentation Fund

The Police Services Augmentation Fund accounts for two grant programs that provide monies for law enforcement purposes. The first is the Supplemental Law Enforcement Services ("SLES") program established by the State, and the second is a small Federal Local Law Enforcement Block Grant (LLEBG) from the Bureau of Justice Administration ("BJA").

The State SLES monies constitute the major portion of this Fund. The City first received the SLES grant in FY 1996/1997. Over the years, the amounts of both grants have decreased significantly, as shown in the table below:

	FY 96/97	FY 97/98	FY 98/99	FY 99/00	FY 00/01	FY 01/02	FY 02/03	FY 03/04	FY 04/05
SLES	293,461	297,886	295,694	295,117	289,000	267,997	263,782	197,376	193,370
BJA	63,935	68,768	70,158	52,915	41,718	41,198	33,685	25,997	11,528

As of FY 2005/2006 the Bureau of Justice Administration is replacing the LLEBG program with a different funding mechanism called a Justice Assistance Grant (JAG). This program is intended to simplify the administration process for grantees and now requires no General Fund match. In March 2005 the Council approved application for the JAG in the amount of $14,113 for FY 2005/2006. This new grant program is reflected in the Long Term Financial Plan.

Initially the Police Service Augmentation Fund monies were used to fund a full-time Domestic Violence Investigator, a Patrol Watch Commander, and participation in the State Bureau of Narcotic Enforcement's Bay Area Regional Narcotics Task Force. Beginning in FY 1999/2000 Council approved use of the SLES and BJA revenue to fund the Patrol Watch Commander and two Internal Affairs Investigators. Due to the continual decline of funding and increased personnel costs, by FY 2003/2004 the

grants were no longer able to support the three positions and funds were allocated to the Patrol Watch Commander and a portion of an Internal Affairs Investigator. The adopted FY 2004/2005 Budget supports only the Patrol Watch Commander with SLES/BJA funds. The Internal Affairs Investigator was moved to the General Fund operations of the Department of Public Safety.

The financial plan for the Police Services Augmentation Fund reflects revenue only for FY 2005/2006 because the grants are speculative in nature. During the State's budget crisis, the State SLES funds have been targeted as a possible reduction in funding to local governments but have never actually been eliminated. The State SLES grant is estimated at the same amount received in FY 2004/2005. Based on the combined funding from the SLES and BJA grants, reserves in the Fund will be totally depleted during FY 2005/2006 and available monies for the Patrol Watch Commander will be insufficient by about $24,000. The Public Safety Department has identified reductions in hours in that amount that can be charged to the SLES program for the Patrol Watch Commander.

If the grant funds go away or are reduced significantly, it is important to note that a Patrol Watch Commander position will be reduced accordingly from the Department of Public Safety Budget.

Employment Development Fund

The City of Sunnyvale, as administrative entity for the North Valley (NOVA) Job Training Consortium, is required by legislation and regulations to account for the use of various Federal and State funds and program revenues for the workforce development activities that are conducted for the consortium. The City has established the Employment Development Fund to fulfill this obligation.

NOVA, formed in 1983, serves the cities of Cupertino, Los Altos, Milpitas, Mountain View, Palo Alto, Santa Clara and Sunnyvale, and is administered by the Department of Employment Development of the City of Sunnyvale. NOVA has a wide variety of programs funded through various vehicles, with baseline funding originating from the Federal government and passing through the State of California. A significant amount of additional grant money is received from Federal and State sources, as well as the County of Santa Clara, local companies and foundations. Since July 1, 2000 the primary funding for the Department of Employment Development/NOVA has been allocated through the Federal Workforce Investment Act (WIA).

In FY 2004/2005 grant application success rate and anticipated funding met expectations and budget plans.

The WIA-allocated funds for NOVA for FY 2005/2006 have just been released by the State of California. The State of California received an allocation from the Federal government of approximately 3% less than in FY 2004/2005. Due to a decrease in NOVA's unemployment rate (although there was not a corresponding increase in the employment numbers), NOVA's allocation decreased by about 20%. To supplement these allocated funds, NOVA has a long history of being very competitive for additional Federal and State resources and has several grant applications in place. It is

projected that at least $5 million in supplemental funding will be secured during FY 2005/2006. As in the past, staff will monitor the actual expenditure/revenue rates on an on-going basis and make the required adjustments as needed.

For the purposes of the City's recommended FY 2005/2006 Budget, we have taken the total funds that were available in FY 2004/2005 and used these as a starting point for NOVA's FY 2005/2006 programs and service levels. It is important to note that the Department has not yet migrated to the outcome management format. As different grants come and go, various programs and activities have a relatively short lifespan relative to programs operated by other City departments. Therefore, the current listing of programs that have been operated by NOVA during the last several years are not included in this recommended Budget. Rather, a base funding level will be carried into the new fiscal year and the City Budget will be modified for planned activities, outcomes and expenditures during the course of the year as new funding is secured and new contract goals and obligations are agreed upon.

Volume II, Operating Budget, does contain descriptions of the significant NOVA programs and a summary table of the expenditures and budgets for these programs. The summary table presents three years of actual expenditures, the current budget, and the proposed budgets for FY 2005/2006. The proposed budgets include funds that were awarded in previous years but allocated over several years.

As in the past and in keeping with the City policy for grant-funded programs, the Employment Development Fund Long-Term Financial Plan reflects grant revenues only for the immediate planning period.

Parking District Fund

The Parking District Fund is a small fund that provides for the ongoing maintenance of downtown parking lots. Debt previously issued to purchase land and make improvements in the District was completely paid in FY 2003/2004.

The Downtown Parking District includes all public parking in the downtown area with the exception of the parking structure adjacent to the Sunnyvale Town Center, which is under ownership of the Redevelopment Agency and leased to the shopping mall.

The approval of Proposition 218 had a significant effect on the methodologies utilized to raise assessments to fund maintenance and operations within the Parking District. Proposition 218 not only deals with the approach and methodologies to be used for benefit assessments, but also the approval process. Essentially, after a method has been selected, a vote occurs by those who would be assessed, with votes weighted according to the amount of assessment. If this weighted majority does not approve the assessment, then it does not go forward.

This financial plan assumes that the District will approve two-year term assessments on an ongoing basis. It also assumes that the amount will remain the same as the base year of FY 2004/2005 plus costs to perform and implement the assessment. Since the assessment engineering and vote occurs every other year, this means that the assessment amount will be higher in one year and lower in the next.

The amount of the assessment generated in this manner will not be enough to pay actual operating expenses to maintain the District lots at the current level. The financial plan assumes that the 20-Year Resource Allocation Plan Reserve will be drawn down until FY 2011/2012 to sustain the existing level of service. At that time, operating expenses will be reduced to meet the available resources through the remainder of the planning period.

A new operating expense has been identified for the Parking District Fund for the recommended FY 2005/2006 Budget. A total of $35,000 has been programmed to pay for the insurance needed for the underground parking structure beneath the Mozart buildings and the Plaza del Sol. Although this parking structure is within the District boundaries, and was constructed with proceeds from the sale of District land, staff believes that the insurance is more properly a cost of the Mozart development since the Parking District members did not receive any new benefit or additional spaces beyond those that they had on the previously existing land. Therefore, a corresponding transfer is being made from the General Fund to cover these insurance costs.

This Fund has a continuing special project to pay for costs of calculating and implementing the annual assessments. Since the assessment is assumed to be a two-year process, the special project for FY 2005/2006 contains $17,500 for the assessment engineer and the charges by the County of Santa Clara for placing the assessment on the Property Tax roles. In FY 2006/2007 only the County charges are shown. This alternating pattern continues for the remainder of the financial plan.

In the near future, the various new developments now occurring or planned in the downtown area are likely to change the character of the parking assessment district. Once all of the various factors related to parking in the downtown are defined and stabilized, the Parking District may be reconfigured considerably.

It should be noted that the lot located on the corner of Charles Street and Evelyn Avenue is not included in the maintenance assessment and will not be maintained with Parking District Funds. Costs of maintaining this lot are currently reflected in the Public Works Department Public Parking Lot Maintenance program. Although this lot was acquired with parking district bonds, it was not effectively serving the properties within the parking district. Parking District property owners expressed concern that it was primarily used by CalTrain riders, and in FY 2001/2002 the costs of maintaining it were removed from the Parking Maintenance District Assessment.

Two issues regarding the Parking District Fund must be stressed. First, <u>the level of service in this area is set by the property owners, not by the City</u>. Depending upon their desire for various services and their willingness to pay, the Parking District members can have more or less services included in their assessment. The second important issue concerning the Downtown Parking District is the <u>continuing threat that the voters will not approve the assessments at some point in time</u>. If the assessment is not approved any time in the future, funds will not be available for continued operation of the District and it would be necessary for staff to explore other potential revenue raising possibilities. These possibilities include establishment of a Parking Improvement District or Business Improvement District or even paid parking.

Youth and Neighborhood Services Fund

The Youth and Neighborhood Services Fund accounts for the revenues and ongoing operating program expenditures associated with the management and maintenance of the Columbia Neighborhood Center ("CNC"). The Columbia Neighborhood Center was developed to meet the health, social, recreational, and education needs of North Sunnyvale residents through a coordinated network of services. The development of the Columbia Neighborhood Center was a collaborative effort between the City, the Sunnyvale School District, Advanced Micro Devices, and numerous community agencies that began in the fall of 1994. In FY 1996/1997, Council invested $500,000 as seed funding for the development of the Columbia Neighborhood Center. This was essentially the City's share of the Advanced Micro Devices contribution to Columbia Neighborhood Center. When this Fund was established, it carried with it a commitment to maintain this $500,000 to generate interest to help offset ongoing operating program expenditures. Also included in the ongoing fund balance were contributions made to the City in the amount of $6,658 on behalf of former employees that bring the current endowment total to $506,658.

At this time, only the operating program expenditures and Columbia Neighborhood Center related projects are in this fund along with the associated program revenues. As outlined in the partnership agreement with the Sunnyvale School District, a portion of the operating program expenditures are reimbursed for the youth services provided at the Columbia Middle School site. Other revenues to the Fund are Recreation Fees, Rental fees for the facilities, interest earnings on the endowment, and an annual subsidy from the General Fund. For FY 2004/2005 the subsidy was approximately $94,000 because the Center had reserves from which to draw. For FY 2005/2006, the subsidy is set at about $404,000 and it grows with inflation over the entire planning period.

In the recommended FY 2005/2006 Budget the operating costs of the facility are shown as separate components: the management and operations of the Columbia Neighborhood Center (under the jurisdiction of the Office of the City Manager), the Recreation programs being conducted at the Center, and the efforts of Public Safety in Juvenile Diversion and Neighborhood Safety.

Redevelopment Agency Fund

The Redevelopment Agency is a separate governmental and legal entity from the City. However, the Agency is a component unit of the City for which the City is financially responsible. Further, due to certain agreements between the Redevelopment Agency and the City, the General Fund of the City is inextricably tied to the financial condition of the Redevelopment Agency.

At the close of FY 2003/2004 the Redevelopment Agency had two outstanding loans due to the City General Fund totaling approximately $48.7 million. This is largely the result of the Redevelopment Agency's inability to raise sufficient tax increment revenue to repay the City for annual lease payments made by the City for the downtown

parking structure. The Agency entered into a First Amended Repayment Contract with the General Fund in 1977 to repay the debt associated with initial improvements to the Project Area and its inability to make payments on the parking structure. This Contract constitutes the "1977" loan. In 1986 certain State legislation imposed more stringent requirements on funds advanced by the General Fund to the Redevelopment Agency and a separate loan was created to account for costs subject to these restrictions. This loan is referred to as the "1986 loan."

Since the inception of the Redevelopment Project, the State has enacted several laws that placed revenue restrictions on redevelopment agencies. These include capping the time period for collection of tax increment for each redevelopment project area. For Sunnyvale's project area, the final year was originally 2025 but has been extended to 2026 due to recent enabling legislation resulting from the State's FY 2003/2004 Budget.

More important was the establishment of revenue limits for redevelopment agencies, referred to as Property Tax increment caps. The revenue limit/increment cap for the Sunnyvale Redevelopment Agency is $118 million.

When tax increment revenues from the downtown area as it originally existed were projected, the Agency reached its increment limit just before the time limit was reached in 2025. However, the recommended FY 2005/2006 Budget now reflects two major new developments which will cause the increment limit to be reached earlier.

The first new development is the completion of the 460,000 square foot Mozart office project at Mathilda and Washington. Because the buildings are complete, the City has begun to receive tax increment resulting from the project, and this new tax increment is now included in our revenue estimates.

The recommended FY 2005/2006 Budget for the Redevelopment Agency also includes the redevelopment of the Sunnyvale Town Center Mall by the Forum Development Group. This major project is scheduled to begin in FY 2005/2006 and be completed within the next two years. Projections of tax increment correspond to the latest development schedule, with approximately one-half of the total new value realized during FY 2007/2008 and the full value shown starting in FY 2008/2009. More information on the status of Downtown Redevelopment is included in this Transmittal Letter in the section on *Local Issues Impacting the City's Financial Condition.* In summary, the Agency has agreed to return to the developer up to $4,050,000 per year of Tax Increment plus 50% of any receipts above this amount, in return for construction by the developer of public streets and parking, including 1,442 underground parking spaces.

It is important to note that as the Town Center Mall is redeveloped and additional development occurs on the north of Washington block, more tax increment will be produced for the Agency, which will cause the City to reach its revenue limit or increment cap earlier. To address the issue of the Property Tax increment cap, the City is currently in the process of evaluating the feasibility of amending the Redevelopment Plan to increase the revenue limit. It is expected that a potential amendment to the Plan will be brought to Council for consideration in FY 2005/2006.

The primary source of revenues to the Redevelopment Agency is Property Tax increment, which is expected to total about $3.6 million in FY 2004/2005. However, the effect of the State budget is also shown here as a two-year reduction to the Property Tax through a shift to the Educational Revenue Augmentation Fund ("ERAF shift") starting at $264,116 in FY 2004/2005 and totaling $269,398 in FY 2005/2006.

As mentioned above, Property Tax increment for the redeveloped Town Center Mall will almost double this source of revenue in FY 2007/2008. To facilitate an understanding of the development deal with Forum, the Property Tax increment projected to be generated by the Town Center Mall has been identified separately from the base Property Tax increment. Under the terms of the Agency's Disposition and Development and Owner Participation Agreement (DDOPA) with the Forum Group, this new tax increment up to $4,050,000 will be returned to the developer in exchange for the construction of new parking facilities, streets, and other public facilities. Any increment above the $4,050,000 will be split between the Agency and the developer. This repayment to the developer is shown in the plan as an ongoing current requirement of the Agency.

The other major revenue source for this fund is a lease payment from the General Fund for the Mathilda Avenue Parking Structure in the amount of $1.2 million annually.

Administration of the Redevelopment Agency, which is managed by the Community Development Department, is reflected in the RDA Fund in the amount of $214,654 for FY 2005/2006.

Included in current requirements are debt service payments totaling $1.8 million for the Central Core Redevelopment Project Tax Allocation Bonds and the Parking Facility Certificates of Participation. It is now projected that the Parking Facility COPs will be repaid by FY 2016/2017 and the Central Core TABs will be repaid in FY 2022/2023.

The Long Term Financial Plan also includes a repayment to the City for its outstanding loans (as discussed above) in the amount of $2.6 million in FY 2005/2006 and $2.8 million in FY 2006/2007. The Resource Allocation Plan includes a total of $33.8 million in repayment to the General Fund over the first ten years and $37.7 million in the second ten years. The RDA Long Term Financial Plan assumes that funds available after paying debt service, projects and operating costs are used to pay the existing loan advanced by the City General Fund.

In FY 2001/2002 Council approved a capital project for improvements to the Downtown area in the amount of $1.5 million. These funds were originally generated from the sale of Parking District property for the Mozart development. In February 2005 the Council approved a program for utilizing these funds for four discrete projects:

- **Downtown Wayfinding System:** This project will develop a unified and clear signage program that directs the public within the downtown area as it is revitalized and evolves with new development and more uses. A coordinated signage program will improve the aesthetics and promote economic viability of the downtown. The total budget for this project is $300,000. $50,000 is

budgeted in FY 2005/2006 for the design and $250,000 is budgeted in FY 2006/2007 for construction.

- **Directional Signs to Downtown:** This program will provide directional signs to the downtown along major roadways such as Sunnyvale-Saratoga Road, Mathilda Avenue and El Camino Real that are consistent with the designs used for the Downtown Wayfinding System. The total budget for this project is $100,000 in FY 2007/2008. $25,000 is budgeted for design and $75,000 is for construction.

- **Murphy Avenue Enhancements, Phase I:** This project funds improvements to Murphy Avenue. The first action will include planning for the future of the 100 block of historic S. Murphy (through a study issue titled "Visual Streetscape Standards for Murphy Avenue). The idea behind the public improvements is to "freshen up" and enhance the streetscape along the frontage of the 100 block of S. Murphy Avenue, the north side of Washington from Frances to Sunnyvale Avenue, and on the south side of Evelyn from the parking lot exit to Murphy Avenue. The total budget for this project is $350,000, funded by $275,000 in RDA monies and $75,000 of Transportation for Livable Communities grant. $90,000 is budgeted in FY 2005/2006 for design and $260,000 is budgeted in FY 2006/2007 for construction.

- **Downtown Block 2 Completion:** This project provides funds to complete the segments of Block 2 that are not part of the historic Murphy Avenue or the Frances Street Transit enhancements. Four segments include Frances, Evelyn East and West of Murphy and Sunnyvale Ave. The total budget for this project is $695,000. $139,000 is budgeted for design, administration and contingencies, and $556,000 is budgeted for construction in FY 2006/2007.

A total of $1,370,000 is planned to be programmed in FY 2005/2006 through FY 2007/2008 for the four projects, to coincide with anticipated design and construction schedules. The remaining balance of $192,463 will be retained in the Downtown Public Improvements Project for unspecified downtown purposes, including possible matching funds.

Additional capital or special projects recommended for the Redevelopment Agency Fund in FY 2005/2006 are:

- **Redevelopment Plan Project Area Special Studies:** This project provides for the study and analysis of development-related issues to encourage or implement redevelopment projects in the downtown area. Efforts include but are not limited to: architectural studies and reviews, land planning, economic/market feasibility, parking analyses, and financial analyses to implement redevelopment in the downtown. $25,000 is budgeted for each year from FY 2005/2006 to FY 2007/2008 in anticipation of redevelopment of the Town Center and Town and Country Village areas.

- **Downtown Development Economic Analysis-Keyser Marston Associates:** This project will fund continuing economic analyses of potential downtown

development as needed. The project will fund the analysis of developer proformas and financing strategies and the negotiation of real estate transactions in the downtown area, such as the Town and Country site. The project has been programmed in the RDA Fund in the amount of $50,000 in FY 2005/2006.

- **Outside Counsel Services for RDA:** This project will fund needed outside legal services for the Redevelopment Agency over the next three years. Because of the increasingly complex nature of negotiations surrounding the downtown redevelopment, a special project was funded to track outside counsel services and costs. It is anticipated that significant outside legal services will be needed over the next two years to deal with the Town Center Mall project and other potential development projects in the downtown area. Future projects may involve assistance on relocation agreements for sites such as the Town and Country. The project has been programmed in the RDA Fund in the amount of $50,000 in FY 2005/2006, $25,500 in FY 2006/2007, and $26,010 in FY 2007/2008.

One final ongoing expenditure is programmed in the Redevelopment Agency Fund to pay the General Fund for the services of the Agency's Treasurer. These services are not charged directly to the RDA Fund, but rather are included in the General Fund.

The Redevelopment Agency Fund maintains one reserve that reflects Debt Service Reserve Funds held by the trustees for the two outstanding bond issues mentioned above. An additional reserve for Capital Projects accounts for funds that are programmed for various projects being completed over a multi-year period.

Finally, it should be noted that the Redevelopment Agency is currently unable to make payments of 20% of its tax increment revenues to the Low and Moderate Income Housing Fund because of preexisting debt obligations. Each year, the Agency calculates the contribution that should have been made and books it as a liability in its financial statements. It is currently estimated that when the tax increment cap is reached the liability will total approximately $19.2 million. State law allows the Agency to continue collecting tax increment after the Project time and increment limits are reached to fund its housing liability. Repayments of the Housing liability are anticipated to begin in FY 2027/2028.

The Redevelopment Agency will begin making deposits of 20% of Property Tax increment to the Low and Moderate Income Housing Fund beginning in FY 2016/2017. Annual deposits to this Fund will average $2 million, with a total of $16.8 million from FY 2016/2017 through FY 2024/2025. When combined with the repayment of the $19.2 million liability, the Low and Moderate Income Housing Fund will have a total of approximately $36 million to spend on affordable housing in the later years of the plan. Of course, if the Town and Country development, which is not currently reflected in the Long Term Financial Plan, goes forward this number will substantially increase.

Patent Library Fund

In the mid 1990s, the City and the United States Patent and Trademark Office (USPTO) formed a partnership with the City of Sunnyvale to create the Sunnyvale Center for Innovation, Invention and Ideas Sc[i]^3. Services and products designed and tailored to the needs of Silicon Valley inventors, intellectual property attorneys, corporate legal staff, researchers, patent agents and paralegal staff have been offered through Sc[i]^3 for the past ten years, and Sc[i]^3 has been recognized as an important contribution that the City of Sunnyvale has made to the economic development in the region, particularly during the technology boom of the late 1990s. Several years ago USPTO began to systematically make increasing amounts of patent and trademark information available electronically. This availability better addresses the preference of practitioners to work from their own offices, but has negatively affected Sc[i]^3 's revenue stream. Efforts to enhance revenue through other means such as the Friends of Sc[i]^3 Foundation or through support from the State of California have not been fruitful.

Sc[i]^3 was downsized, redesigned and relocated to the main library in January 2002. FY 2002/2003 was the first full year of operation with a streamlined budget and reduced services under which Sc[i]^3 was expected to be fully self supporting. At year-end the Program fell short of its goal by approximately $20,000. The operation is very lean with a very small staff. Some of the services offered are able to cover their own cost entirely while others operate without full cost recovery. The program is constrained from covering all costs in some cases because the federal government sets the fees. Performance in FY 2003/2004 resulted in a deficit of $34,000 and FY 2004/2005 appears to be on track for a deficit of $20,000.

Several factors contribute to the fact that Sc[i]^3 has a difficult time reaching full self sufficiency. First, Sc[i]^3 is required to pay a subscription fee of $30,000 to the USPTO. Repeated efforts by the City Council and staff to have this fee eliminated have been unsuccessful. Second, customer input indicates that the most valuable role Sc[i]^3 plays is that of liaison to the USPTO. In recent years this role has been virtually eliminated as evidenced by the lack of USPTO speaker visits, for example. Third, the USPTO is not always responsive to customer requests for training seminars on specific current topics. Fourth, very few customers take advantage of our services to provide access to the patent examiner database, EAST, or to conduct patent examinations or hearings using videoconferencing equipment. Due to this low level of use the services rarely cover their own costs.

For the reasons outlined above, there has been continuing risk for the City in the operation of Sc[i]^3.

At their October 19, 2004 meeting, Council voted to eliminate all specialized patent and trademark services, but to continue to provide free basic reference services through existing Adult Services resources. However, Council reconsidered that action and at the November 9, 2004 meeting voted to continue Sc[i]^3 through June 30, 2005, in order to give the Sc[i]^3 Advisory Board and supporters time to develop a funding alternative to close the funding gap.

Council considered the Sc[i]^3 program and funding alternatives at the March 29, 2005 meeting, including an alternative suggested by the Sc[i]^3 Foundation to move Sc[i]^3 to Cogswell College. Council voted to extend the Sc[i]^3 program to June 2005 and provide up to $53,000 to subsidize the program in FY 2005/2006. This action was taken in order to give the Sc[i]^3 Foundation and Cogswell College time to establish themselves in partnership with the USPTO in the hope that the USPTO would allow the transfer of Sc[i]^3 operations to the College.

The recommended FY 2005/2006 Long Term Financial Plan for the Patent Library Fund reflects the decision to phase out operations of Sc[i]^3 by the end of the fiscal year.

Transportation Development Act (TDA) Fund

In FY 2003/2004 a new, small special revenue fund was established to account for activities related to the Transportation Development Act (TDA) funds received from the State of California through the Metropolitan Transportation Commission. These funds are restricted for pedestrian and bicycle facilities and bicycle safety education programs and must be segregated for those purposes. In the past these funds were accounted for in the Gas Tax Fund. Although many of the projects using TDA monies are multi-funded by Gas Tax, TDA and other funding sources, they are completely different sources of funds and should not be reported in the same fund. In addition, the TDA, in accordance with Public Utilities Code Section 99245, must submit a report of a fiscal and compliance audit made by an independent auditor at the end of each fiscal year. In order to facilitate the audit and the issuance of the fiscal and compliance report, the City decided to segregate this fund into its own special revenue fund.

The recommended FY 2005/2006 Budget includes revenues of $496,198, $423,673 of which will be transferred to the Capital Projects Fund to partially fund two projects. The first is the Borregas Avenue Bicycle Corridor ($413,798), and the second is the Mary Avenue Route 280 Bicycle Footbridge ($9,875).

In addition, the financial plan includes revenues of approximately $80,000 annually from TDA funds based on staff's estimates using historical receipts. This revenue is included each year for the entire 20-year period, increased by inflation. The estimated new revenues are offset by an expenditure line item entitled "Future TDA Projects." When the funds are received, pedestrian and bicycle projects will be identified and funds will be appropriated. Examples of projects funded to date are Arques Avenue Bike Lanes, Sunnyvale Bicycle Network, Calabazas Creek Trail, and Countywide Bicycle Route 8 Bike Lanes.

CAPITAL PROJECT FUNDS

Capital Projects Funds are used for major capital acquisition, construction activities, and renovation or replacement of General City fixed assets. The City currently operates two of these funds: the Capital Projects Fund and the Infrastructure Renovation and Replacement Fund. Capital and Infrastructure projects related to the

Utility Enterprise Funds are budgeted and accounted for within each individual utility fund.

Capital Projects Fund

The Capital Projects Fund was established in FY 1997/1998 to account for capital projects that are funded by the General Fund and other governmental funds or that are funded by multiple sources. The Capital Projects Fund is divided into distinct sub-funds that receive direct transfers from the funds that are responsible for the particular projects. Each sub-fund records revenues, interest earnings, transfers and expenses separately.

The recommended FY 2005/2006 Budget includes four sub-funds of the Capital Projects Fund: the General Sub-fund, the Gas Tax Sub-fund, the Traffic Mitigation Sub-fund, and the Traffic Impact Sub-fund. In FY 2004/2005 staff changed the accounting method for capital projects related to the Utility Enterprise Funds to reflect best accounting practices. In keeping with this change, all monies that were held in the Capital Projects Fund for utility projects were transferred back to the Water Fund and the Wastewater Fund. All utility projects are now completely budgeted and accounted for within each Utility Enterprise Fund and the Capital Projects Fund will be used exclusively for the General Fund and other Governmental Funds. The only Utility Enterprise Funds that will still be budgeted here will be those that are relating to projects funded by more than one fund.

The Capital Projects Fund contains projects that are funded by federal and state granting agencies, developer contributions, and transfers from various City governmental funds. In FY 2003/2004 and FY 2004/2005, significant transfers were made from the Park Dedication Fund, primarily to support the Plaza del Sol Project.

Major project efforts included in the Capital Projects Fund are discussed throughout this Transmittal Letter under their applicable funding source. The table below is an overview of project appropriations by Sub-fund for FY 2005/2006.

Capital Projects Fund - Project Expenditures by Sub-fund

Sub-fund	**FY 2005/2006 Recommended Budget**
General Fund Assets	0
Gas Tax	1,738,543*
Traffic Mitigation	50,000
Traffic Impact	50,000
TOTAL	**1,838,543**

*The Long Term Financial Plan for the Gas Tax Sub-fund shows total capital projects budgeted of $3,488,543 in FY 2005/2006. This includes an anticipated carryover of the FY 2004/2005 budget for the Washington Ave. and Mathilda Ave. Intersection Improvement Project, which is on hold pending completion of the Mall redevelopment.

The appropriations for the Gas Tax Sub-Fund are comprised of one large project and two smaller projects. The large project is the Borregas Avenue Bicycle Corridor, budgeted at $1,405,798. The first smaller project is Roadway Rehabilitation on Various Streets, budgeted at $167,745. The second is the Transportation Grant Matching Project, budgeted at $165,000.

The Traffic Mitigation and Traffic Impact Sub-funds each have one new project budgeted for FY 2005/2006. The Traffic Mitigation Sub-fund includes the Mary Avenue Extension Engineering/Environmental Analysis Project, with funds of $50,000 in FY 2005/2006, and $500,000 in FY 2006/2007.

The Traffic Impact Sub-fund includes $50,000 for the Transportation Model Update in FY 2005/2006. This update is budgeted every five years through the life of the plan.

More detail on the Traffic Mitigation Fees, the Traffic Impact Fees, the Borregas Avenue Bicycle Corridor Project, and the Mary Avenue Extension Project is included in the *Major Project Efforts* section of this Transmittal Letter.

Infrastructure Renovation and Replacement Fund

The Infrastructure Renovation and Replacement Fund was introduced with the FY 1996/1997 Budget and Ten-Year Resource Allocation Plan. Its importance has grown with each subsequent year as staff identifies projects to address the City's need to fund the renovation and replacement of its extensive physical infrastructure. This growth will continue until staff completes the Long-Range Infrastructure Plan (LRIP).

Similar to the Capital Projects Fund, this fund is divided into distinct sub-funds that receive direct transfers from the funds that are responsible for the particular infrastructure projects. Each sub-fund records revenues, interest earnings, transfers and expenses separately. Currently the sub-funds are General, Community Recreation, General Services, and Multi-funded Assets. Infrastructure projects for the City's three utilities are budgeted and accounted for in each utility fund in accordance with governmental accounting principles.

Major projects contained in this fund are described throughout the Transmittal Letter. The following table contains project expenditures by sub-fund for FY 2005/2006.

Infrastructure Fund – Project Expenditures by Sub-fund

Sub-fund	**FY 2005/2006 Recommended Budget**
General Fund Assets	2,482,493
Community Recreation	222,100
General Services	0
Multi-Funded Assets	20,000
TOTAL	**2,724,593**

There are 21 projects in the various sub-funds consisting of such items as Corporation Yard Building HVAC repair and Traffic Signal Controller Replacement. The largest project is Security Access Control System Replacement for $531,296. Information on each of the projects is available in the *Volume II, Projects Budget*.

A complete discussion of the total Infrastructure Renovation and Replacement Program and its current status is contained earlier in this Transmittal Letter in the *Major Project Efforts* section.

INTERNAL SERVICE FUNDS

The City utilizes internal service funds to account for the financing of goods and services provided by one department or agency to other departments or agencies of the City. There are two such funds that operate on a cost reimbursement basis: the General Services Fund and the Employee Benefits and Insurance Fund. Both of these funds play an important role in the overall ability of the City to conduct business. Sunnyvale's full cost accounting methodology results in all of the costs of these funds being charged back to user activities on a rental rate or additive rate basis. Therefore, the total expenditures of these two funds are not added to the overall budget.

The City also has two additional internal service funds. One of the funds accounts for activities associated with the Sunnyvale Office Center and the other fund was created to separate property and liability insurance costs from the Employee Benefits and Insurance Fund.

General Services Fund

The General Services Fund provides a wide range of important support services to programs within the City. These services range from fleet, to building maintenance, technology and communication services. Funding for these services is recovered through rental rates charged to benefiting program operating budgets. The rental rates may include not only the cost of operations, but also the cost of replacement for depreciable equipment. This assures the availability of funds to replace equipment at the most cost-effective time.

Aggregate rental rate increases for General Services Fund activities are projected at 2.1% for FY 2005/2006 and an average of 3.1% over the remaining years of the financial plan. Rental rates are lower in the second ten years of the plan.

During the development of the FY 2005/2006 rental rates, budget staff identified potential savings from the reduction of some of the City's general service equipment. A number of these savings were incorporated into the Long Term Financial Plan this year. During the upcoming year staff will be conducting a comprehensive inventory of all general service equipment schedules.

There are a number of sub-funds within the General Services Fund in order to recognize distinct support service functions and establish appropriate rental rates for

each. Included in each section is a brief description of major items that effect the current resources, current requirements, or reserves of each plan.

Fleet Services Sub-fund

The Fleet Services program reflects the cost of ownership of City vehicles and equipment. A primary objective of Fleet Services is to provide rental rates that are competitive with those offered in the private sector.

The main source of funding within this Sub-fund is derived from Fleet Services rentals to other programs. However, other items that affect the current resources of this fund are also discussed below.

The Fleet Services rental is scheduled to increase by 3.6% for FY 2005/2006 or $113,277 above the current fiscal year. This increase is due in part to a significant rise in the cost of fuel. An average annual increase of approximately 3.2% is projected for the remainder of the plan.

The Sale of Property line item of the Financial Plan represents the sale of surplus or replaced vehicles or pieces of equipment. The actual revenue from this source was unusually high in FY 2003/2004 because of the sale of a number of vehicles that became surplused because of the budget reductions that occurred in that year. For the remainder of the plan a historical average of the sale of assets is used.

The Intrafund Loan Repayment represents scheduled payments from the Facilities Management Services Sub-fund. This loan was initially made in FY 1999/2000 to alleviate cash flow issues experienced by the Building Services Sub-fund. The initial terms of the loan were for a principal amount of $1.6 million to be repaid over 10 years with final payment scheduled for FY 2015/2016. The original terms of this loan have modified to accelerate payments whenever possible. The new repayment schedule includes a one-time payment in FY 2005/2006 and scheduled payments beginning in FY 2010/2011 through FY 2018/2019.

The multiple transfer line items found within the Current Resources section of the financial plan represent the funding mechanisms for a Capital Project Upgrading the City's Fuel Stations.

The two major current requirements deal with equipment replacement and operation of the Fleet Services Program.

The operations line reflects an increase of approximately $137,000 associated with substantial increases in costs for fuel.

The Equipment Replacement Reserve represents the accumulation of annual rental rates received from City programs, net of replacements purchased during the current fiscal year, for future replacement of vehicles and equipment. This reserve correlates with the *Equipment Replacement* line item under the *Current Requirements* section of the sub-fund. For example, when a large value item is scheduled to be replaced such as a street sweeper or a fire apparatus, the equipment replacement reserve will be

drawn down as the accumulated annual replacements fund within the reserve will be used to purchase the vehicle or apparatus.

The *20-Year RAP Reserve* functions in this fund, as in other funds, to levelize rates and plan for capital projects. The large reduction in this reserve from FY 2003/2004 to FY 2004/2005 is a result of increased fuel costs added to the operating budget per Council approved direction.

Facilities Management Services Sub-fund

The Facilities Management program reflects the cost of maintaining City facilities (including costs for electricity and water), free standing furniture, modular furniture, and building equipment.

The Facilities Management Services Sub-fund has two rental rate revenue items, one relating to space rental and the other relating to equipment. The space or Facilities rental is based upon the total square footage of building space throughout the City. This square footage is then divided amongst the various City programs. The equipment rental accounts for replacement costs associated with modular and freestanding furniture, carpet, and blinds, and building maintenance equipment. During the development of this year's rental rates staff performed a historical analysis of the Facilities Management Sub-fund and determined that the two rental rates for this fund were not correlated with the services actually provided. Due to extremely volatile energy costs experienced in recent year's the facilities rental rate had not generated sufficient funding to recover the cost of provided electricity to all of the City's buildings. This variance was then funded through lower than anticipated replacement activity and subsequent reductions in the sub-fund's equipment replacement reserve. Beginning with FY 2003/2004 the financial plan reflects the correct reserve levels associated with each service. The sub-fund is anticipated to fully mitigate the variance by FY 2007/2008.

For FY 2005/2006 the aggregate rental rate is scheduled to decrease by approximately 1% or $33,343 as compared to the current year. This decrease is due to a substantial reduction in rental for furniture replacement.

The major current requirements deal with equipment replacement and operation of the Facilities Management Services Program. The increase in planned operating costs for FY 2005/2006 is directly attributable to increase in costs associated with the provision of utilities for City facilities.

The Lease Payments line item in the financial plan represents a transfer of rental rate revenues received from City programs currently housed at the 505 W. Olive Sunnyvale Office Center. These funds are collected in this sub-fund and then transferred to the Sunnyvale Office Center Sub-fund to partially fund the facility management costs associated with that facility.

The Interfund Loan line item in the financial plan represents loan payments to the Fleet Services Sub-fund. As was mentioned in the *Fleet Services* section, this loan was made to alleviate cash flow constraints of the Facilities Management Sub-fund in FY

1999/2000. The original terms of the loan called for repayment over a 10-year period; however, staff has since accelerated the payment schedule to include a large one-time payment in FY 2005/2006 and regular payments beginning in FY 2010/2011 through FY 2018/2019.

The *Equipment Replacement Reserve* represents the accumulation of annual rental rates received from City programs, net of replacements purchased during the current fiscal year, for future replacement of office furniture, carpets and blinds, and building maintenance equipment. For FY 2005/2006 staff has recalibrated the reserve levels for this sub-fund to more accurately reflect the historical expenditure pattern related to the replacement of furniture and equipment.

The *20-Year RAP Reserve* functions in this fund, as in the other funds, to levelize rates and provide for planned capital projects. The *20-Year RAP Reserve* has been adjusted to reflect the increased costs previously absorbed by the fund's equipment replacement reserve.

Technology/Application Services Sub-fund

Beginning in FY 2004/2005 this sub-fund combined the two previous sub-funds associated with the City's Information Technology Department. These two sub-funds were combined for ease of administration as the department has completed an operating restructure to the outcome management budgeting system. As a result of the restructure both Technology and Communications equipment related charges and their associated operating costs are budgeted in one program. All software application related services have been incorporated into a separate program.

The rental revenue line items associated with the previous two sub-funds are listed separately for ease of comparison to previous years' financial plans. For FY 2005/2006 the aggregate rental rate is scheduled to increase by approximately 3.2% or $224,411 as compared to the current fiscal year. An average annual increase of approximately 3.1% is projected for the remainder of the plan

The Miscellaneous Revenue line item in the financial plan accounts for royalty revenue received from the City's SUNGIS software application.

The various transfers from the Asset Forfeiture, Utility, and General Service Funds represent the pro-rated portion of planned IT related projects such as a Network Security Project and a Storage Area Network Project. Transfers in FY 2010/2011 and FY 2011/2012 are for the planned replacement of the City's messaging and collaboration software. The on-going transfer from the General Fund represents funding for costs associated with management of the City's cable franchise agreement.

The two transfers from the Employee Benefits Fund in FY 2003/2004 represent funding donated by City employees to extend the timeframe of employment for those employees whose positions were eliminated as a result of the implementation of the service level reductions approved in the Adopted FY 2003/2004 Budget.

The major current requirements of this sub-fund deal with equipment replacement and operation of the Technology Services Programs. Staff has pro-actively reduced the Equipment Technology line by 10% on an on-going basis to reflect the continued decline in hardware acquisition costs and anticipated reductions in the level of equipment to be replaced in future years.

The $305,910 in the Capital Projects line item of the financial plan for FY 2005/2006 represents costs associated with the updating of the City's computer network and information security infrastructure. The resources under the Project Operating line item represent the ongoing costs that will be assimilated into the Technology Services Program upon completion of the program.

The General Fund Loan repayment line item of the financial plan represents the repayment schedule of a $2 million loan made to the former Technology Services Sub-fund in FY 1999/2000. This loan was made to fund a number of information technology initiatives including the City's geographical information system (GIS). The original term of the loan was 10 years with payments scheduled to begin in FY 2009/2010. Staff has accelerated the payment of this loan with two up-front payments scheduled in FY 2005/2006 and FY 2006/2007 and regular payments beginning in FY 2012/2013 through FY 2017/2018.

The equipment replacement reserve represents the accumulation of annual rental rates received from City programs, net of replacements purchased during the current fiscal year, for future replacement and maintenance of network infrastructure, central computer maintenance, desktop maintenance, training, development of equipment specifications and/or applications, administrative and support services, technology equipment replacement costs, communication equipment, office equipment, mail services, print shop services, and telecommunication franchise (all KSUN related equipment).

The *20-Year RAP Reserve* functions in this fund, as in other funds, to levelize rates and provide for planned capital improvements.

Sewer Equipment Sub-fund

The Sewer General Services program has responsibility for all equipment at the Water Pollution Control Plant and all equipment for the wastewater collection system. These rental rates are applied exclusively to the Wastewater Management Fund. For FY 2005/2006 the rental rate is scheduled to decrease by approximately 2% or $12,286 more than the current fiscal year. An average annual increase of approximately 3% is projected for the remainder of the plan.

The $3.3 million transfer to the City's Utility Fund represents adjustments made to the Wastewater Equipment Replacement schedule. These funds represent planned equipment purchases from prior years that were carried forward to the current year. Staff has determined that these funds are no longer necessary and therefore the funds were returned to the City's Wastewater Management Fund.

Public Safety Equipment Sub-fund

The Public Safety Department has responsibility for the General Services program that manages all fire and police service equipment. This equipment includes items such as guns, fire hose, and fire Self-Contained Breathing Apparatus (SCBA) units. (Fleet, radio, and computer equipment are all handled through the respective city-wide General Services program.) All rental rates are applied exclusively to Public Safety Programs within the General Fund. For FY 2005/2006 the rental rate is scheduled to increase by approximately 3.75% or $10,785 as compared to the current fiscal year. During the next fiscal year staff will be conducting a thorough inventory of all General Services equipment throughout the City and it is anticipated that this rental rate will decrease in the future. An average annual increase of approximately 0.3% is projected for the remainder of the plan.

The General Fund Loan repayment line item of the Long Term Financial Plan represents the repayment schedule of a $450,000 loan made in FY 2000/2001. This loan was made to help alleviate cash flow issues experienced by the sub-fund at that time; specifically, these funds were used for replacement purchases of SCBA units. The original term of the loan was 9 years of an annual payment of $20,000 starting in FY 2007/2008 through FY2011/2012 and $243,659 starting in FY 2012/2013 until FY 2015/2016. Staff has increased the dollar amount of the first portion of the loan repayment.

Parks and Recreation Equipment Sub-fund

The Parks and Recreation Department has responsibility for the General Services program that manages all leisure services equipment. Examples of this equipment include pool covers, theater lighting, gymnastic equipment, and theater staging equipment. All rental rates are applied exclusively to the Community Recreation Fund. For FY 2005/2006 the rental rate is scheduled to increase by approximately 2.5% or $1,059 more than the current fiscal year. An average annual increase of approximately 2.1% is projected for the remainder of the plan.

Project Management Sub-fund

This sub-fund represents project management services provided by staff within the Department of Public Works Engineering Service Program. These services are associated with the various capital and special projects currently incorporated within the City's Projects budget. The transfers into this fund represent the proportionate share of the current schedule of projects that the project management group is responsible for overseeing.

The FY 2003/2004 operating figure is uncharacteristically low due to the large number of Measure B projects that were administered by the Project Management program. Measure B grant regulations require that charges for services such as those provided by Project Management be charged <u>directly</u> to the Measure B funds rather

than charged to this general services account and then applied as overhead to the projects. This requirement causes the costs included in Project Management to be understated. Since Measure B funds were exhausted at the end of FY 2003/2004, this situation will not occur again.

Employee Benefits and Insurance Fund

The Employee Benefits and Insurance Fund provides a mechanism to cover expenditures related to pension costs, employee insurance plans, workers' compensation costs and leave time while applying the principles of full cost accounting. This is accomplished by charging an additive rate to staff salaries wherever personnel hours are budgeted and expended. To better track and analyze expenditures, the Fund is separated into four sub-funds: Leaves Benefit, Retirement Benefits, Workers' Compensation and Insurance and Other Benefits. Liability and property insurance, previously a part of the Employee Benefits and Insurance Fund, was broken out into its own fund because these costs are not related to salary expenditures, but instead are recovered on claims experience and building space usage.

The major driver of higher operating costs for FY 2004/2005, employee benefit costs, continue to increase for FY 2005/2006. Total expenditures in the combined fund are up by $5.2 million over the current budget, or a 10.6% increase. Last year, an increase of 9% was budgeted for FY 2005/2006. The increase is higher than budgeted primarily due to CalPERS retirement costs, which already increased significantly in the last year. With labor costs the largest component of operating expenditures, these increases, especially when they are outpacing revenue trends, are problematic for the long term financial picture. Details of the benefits increases are discussed in the sub-fund sections below.

Leaves Benefit Sub-fund

The Leaves Benefit program accounts for all City employees' leave time, including accrual of leave benefits. The additive rate is calculated by determining the amount of leave benefits to be accrued and adjusting for estimated salary increases. An additional adjustment was also calculated for the next three years to account for the filling of vacancies and higher leave accrual rates for long-term employees. It is anticipated that retirements will be delayed until the City's retirement plan is changed in FY 2007/2008. The change in retirement plan is discussed in more detail in the following section.

In prior years, the Leaves Sub-fund Financial Plan included a reserve for unused leave. Because the accrual of all earned leave is already reflected in the budget, presenting the unused leave as a reserve is redundant. Therefore, while the unused leave is properly accounted for as a liability in our General Ledger, the reserve line has been removed from the Financial Plan.

Retirement Benefits Sub-fund

The Retirement Benefits Sub-fund contains the costs for the City's retirement plan. Sunnyvale contributes to two California Public Employees Retirement System (CalPERS) plans for and on behalf of its employees: Safety (3% @ 50 Plan) and Miscellaneous (2% @ 55 Plan). The City pays the employee contribution as well as the employer contribution for these plans. While the employee contribution rate is set by law, the employer contribution rate is adjusted by CalPERS through an actuarial analysis and is impacted by its investment portfolio. The contribution rates are applied against employee salaries (PERSable earnings) in order to calculate the dollar amounts the City must contribute. Employer rates provided by CalPERS for FY 2005/2006 and projected by CalPERS for FY 2006/2007 are in the following table. Current and last year rates are also shown for reference.

CalPERS Plan Employer Rate	2003/2004 (actual)	2004/2005 (actual)	2005/2006 (actual)	2006/2007 (projected)
Safety (3% @ 50)	16.9%	29.6%	32.9%	32.5%
Miscellaneous (2% @ 55)	0.6%	6.6%	11.4%	11.2%

As the table indicates, the employer contribution rates have increased significantly. It is important to note that these rates are set by CalPERS using actuarial analysis that is two years old. Therefore, the FY 2005/2006 rates are now recognizing investment losses that were sustained in FY 2002/2003.

Because of the City's long term financial planning, staff worked with our consulting actuary last year to incorporate the projected FY 2006/2007 rates into the Long Term Financial Plan. Additionally, we reviewed the CalPERS actuarial analysis and adjusted it for increases in salaries. As a result, the most significant increases have been budgeted for. However, at the time the long range plan was developed last year, the investment results for FY 2002/2003 were not known, so the FY 2004/2005 rates were reflected for the remaining years of the planning period. Unfortunately, the investment losses continued for a historic third year, and the projected rates for FY 2005/2006 are higher than FY 2004/2005. These higher rates are now budgeted into the recommended budget.

As mentioned earlier, CalPERS experienced significant investment losses over the last three years. Long term contribution rates are based upon the assumption that investment earnings will equal 8.25% annually. In FY 2000/2001 CalPERS experienced a real loss of 7.2%, and in FY 2001/2002 a real loss of 6.1%. Results for FY 2002/2003 were an investment gain of 3.7%, 4.5% less than the actuarial assumption. These investment losses have had a dramatic impact on the assets in our employer account at CalPERS and therefore our contribution rates. Fortunately, FY 2003/2004 has seen a turnaround in the CalPERS portfolio, and market returns higher than the actuarial assumption will help to stabilize rates and prevent further increases. Returns for calendar year 2004 were 9.3%.

The effect of marked increases in CalPERS rates has been particularly noticeable in Public Safety additive rates. The change in the Public Safety plan from 2% @ 50 to 3% @ 50 in FY 2000/2001 represented a 50% increase in the value of the retirement

benefits for Public Safety members. This enhancement was made possible in large measure by the large surplus assets in the Public Safety plan, and an agreement between the City and the Public Safety Officers Association was made to split the estimated additional cost of the retirement enhancement equally between the City and the Association. The current and projected extraordinary losses in CalPERS assets have resulted in significant increases in public safety retirement costs and in the cost of the 3% @ 50 benefit. For FY 2005/2006 the additive rate for sworn personnel will be more than 100% of direct wages because of the higher CalPERS rates and increased workers compensation costs.

As negotiated in the current Memorandum of Understanding with SEA, the Miscellaneous Plan will also be enhanced effective FY 2007/2008. The benefit will increase from 2% @ 55 to 2.7% @55. The exact impact to the employer contribution rate is not known since the health of the investment portfolio at that time will have an effect on the rates. However, during negotiations, CalPERS provided the City what the rate would be if the enhanced benefit were to go into effect at that time. The employer contribution rate would increase by approximately 6%, essentially doubling the current rate of 6.6%. To pay for these increased costs, SEA took a 0% salary increase for FY 2004/2005 and agreed to a revised salary formula which is anticipated to result in lower salary increases than budgeted for the next two years. These budgeted salary savings have been transferred from all the various operating programs to the Retirement Benefits Sub-fund. It should be stressed that if either the actual employer contribution rate or the SEA salary adjustments are higher than projected, the fiscal impact to the City could be substantial.

The continuing increase in retirement costs has a significant impact on expenditures, particularly when reflected over the long-term financial planning period. For FY 2005/2006 the impact of the changes in CalPERS rates from FY 2004/2005 is about $20 million over the 20-year financial plan.

Workers' Compensation Sub-fund

The Worker's Compensation Sub-fund is funded through the use of an additive rate that is applied to all staff salaries. This additive rate is based upon actual usage of the City's Workers Compensation program. For this reason, the City charges a variable additive rate depending upon the classification of the employee. In other words, more high risk positions, such as a Public Safety Officer, are charged a higher rate than an administrative employee.

The City has experienced increased costs in the workers' compensation program over the past several years due to both controllable and non-controllable factors. Non-controllable factors include favorable legislation for injured workers and sharply rising medical costs. Staff is working to reduce costs of the controllable factors by focusing on injury prevention training, increased utilization of the light duty program and better management of and follow-up with employees out on workers' compensation. Through these efforts, staff's goal is to reduce workers' compensation costs by 25% in FY 2005/2006 and an additional 25% over the next five years, for a total of 50%. These reductions are reflected in the budget and in program measures for high risk

programs. Staff has also budgeted $100,000 annually for a wellness program to help Departments meet these goals.

The City currently is self-insured for workers' compensation costs but maintains excess insurance above what is known as the self-insured retention (SIR). The SIR level is at $500,000. All self-insured agencies must pay the State a self insurance assessment. The assessment was increased substantially for FY 2004/2005, increasing by 72% from the prior year, for a total assessment of $53,200. This higher assessment level has been budgeted for future years.

The Worker's Compensation Sub-fund reserve requirement is based upon an initial reserve provided through actuarial analysis. The estimated number of new claims and associated costs is added to this reserve. The ending reserve requirement assumes the total obligation of the initial reserve in addition to the anticipated number of claims net of estimated payments for the fiscal year. Based on the reductions targeted over the next six years, the reserve requirement has been reduced accordingly.

Insurance and Other Benefits Sub-fund

The Insurance and Other Benefits Program includes costs for all the employee insurance plans including medical, dental, vision and life insurance. This program also includes the costs of the City's incentives programs such as the Management Achievement Program, Disability Incentive Program and Service Awards. Expenditures also include the costs for administering these programs.

The largest cost in this Program is medical insurance for our employees. As anticipated, health premiums for the City increased significantly for calendar year 2005. The increase in premiums for the City's four healthcare plans ranged from 5.8% to 23.7%, with an average increase of 14.9%.

The ratio between the City's contribution for health premiums versus the employees' contribution has changed due to the recently adopted Memorandum of Understanding with the Sunnyvale Employees' Association. Prior to the new MOU, the citywide employees' contribution for healthcare costs was 14% of the total costs. The MOU increases the City's dollar contribution towards SEA employee healthcare costs so that the citywide employees' contribution has been reduced to 8%. In dollars, the City's costs have increased by approximately $450,000 annually. This fiscal impact was calculated during the MOU negotiations and is funded through projected savings in salaries.

The long range projections include 12% increases in medical costs for FY 2005/2006 and FY 2006/2007, 8% for the next five years, and then 5% for the remainder of the Long Term Financial Plan.

In the recommended budget, the medical insurance costs are broken out by active employees and retirees to reflect the significantly increasing costs for retirees. Although there are currently enough reserves to pay for the City's share of retiree medical costs, current additive rates cannot fully fund these costs over the long term. As a result, increased additive revenue in the amount of $2.2 million, growing

annually with inflation, is reflected in the last ten years of the financial plan. Without this additional revenue, medical costs are severely underfunded over the planning period. As part of the fiscal strategies, staff will be analyzing ways to contain medical costs for both active employees and retirees in the coming years.

Liability and Property Insurance Fund

This fund was established to separate out liability and property insurance costs from the Employee Benefits and Insurance Fund. Separating these costs into a separate fund provides better accountability of expenditures and allows the City to recover costs based on usage rather than on salary expenditures.

The Liability Property Insurance Fund is funded through transfers from its dependent funds rather than on an additive rate basis. This insurance coverage is applied to the maintenance of the City's infrastructure and covers the City against claims such as a Trip and Fall, Vehicle Damage, and damage caused by City trees.

Currently, the City participates in a risk pool administered by the California Joint Powers Risk Management Authority.

Reserve Levels in Employee Benefits and Insurance Fund

Reserves in the Employee Benefits and Insurance Fund have been set at amounts recently established by actuarial studies or staff analysis, as discussed above. The reserve levels as of June 30, 2005 are expected to be as follows:

Reserve Item	2004/2005 Year-End Amount
Workers' Compensation	$10,594,944
PERS RetirementVacation Leave	$1,296,994
Insurance and Other Benefits	$10,406,407
Liability and Property*	$1,104,707
Total Employee Benefits Fund Reserves	**$23,403,052**

*Liability and Property were separated into a new fund for FY 2002/2003.

Sunnyvale Office Center Fund

This fund accounts for the activities of the Sunnyvale Office Center located at 505 W. Olive Avenue, across from the main City Hall. The Sunnyvale Office Center was purchased in April 2001 by the issuance of variable rate Certificates of Participation ("COPs") to provide expansion opportunities for the Civic Center Complex. Activities included in this fund are maintenance and operations of the office facility, capital projects, and debt service. Revenues to this fund consist of rental from outside tenants and City operations, and interest on reserves.

When the fund was established, it was projected that the existing office buildings would be operated and leased through FY 2005/2006, when a long-term solution to the City's office space problem could be in place. Subsequently, plans for a new civic center complex have been put on hold because of the City's financial situation. The FY 2005/2006 Long Term Financial Plan therefore shows the complex being operated for the entire 20-year planning period. Increasing the length of operation causes the office complex to generate more net income than originally anticipated; this allows the Sunnyvale Office Center Fund to give a rebate to the General Fund of about $200,000 annually over the entire planning period.

Because of the age and general condition of the office buildings, it was necessary to propose capital improvements in the amount of $564,000 in the first ten years in order to keep the facility in working order for the additional years that it would be in operation. The capital improvements began in FY 2004/2005 and continue through FY 2007/2008. A similar set of capital improvements is proposed in the second ten years of the plan in order to maintain the facility as an earning resource.

Staff has also modified the interest rate assumptions to account for the likely increase in interest rates in the near future. Currently, the COPs weekly interest rate is less than 1%. However, given recent indications from the Federal Reserve's Federal Open Market Committee staff has increased the assumed interest rate to 3% beginning in FY 2005/2006. This interest rate represents the approximate historical average of the Bond Market Association's Municipal Swap Index.

FIDUCIARY FUNDS

Dorolou P. Swirsky Youth Opportunity Fund

In August 1993, City Council accepted Dorolou Swirsky's gift of an ongoing Youth Opportunity Fund to specifically address sports, recreational, social, cultural, and educational activities for disadvantaged youth living in Sunnyvale in the form of a Trust Estate.

The Dorolou Swirsky estate was donated to the City upon her death in March 2000. The estate consisted of a single family home located at 1133 Hollenbeck Road. Following the donation, the City established the Swirsky Youth Opportunity Fund to account for the proceeds. Ms. Swirsky had taken a reverse mortgage on the property which the City paid upon her death using General Fund monies. The property was rented out until August 2003 with net proceeds used to help pay back the General Fund for the reverse mortgage.

In November 2003 Council approved a resolution authorizing the sale of 1133 Hollenbeck Road. The house was subsequently sold, the remainder of the General Fund advance was paid, and an endowment of $526,635 was established. In accordance with Council's action, one-third of the interest generated each year by the endowment was to be used to provide summer recreational equipment and supplies to disadvantaged youth through an agreement with Sunnyvale Community Services. Council also asked the Arts Commission and the Parks and Recreation Commission to

explore how the City might grant the remaining two-thirds to outside agencies serving Sunnyvale's disadvantaged youth. However, given the current budget crisis and the costs involved with administering such a program, Council ultimately directed the City Manager to use these proceeds from the Swirsky Youth Opportunity Fund to supplement the City's Mobile Recreation Program or an equivalent City program rather than using the funds for grants to outside groups. The City Manager would include a recommendation for the use of funds (consistent with the Trust) with the budget submittal each year. It is recommended that funds for FY 2005/2006 be used to supplement the Mobile Recreation "Fun on the Run" Program.

Fremont Pool Endowment (Trust) Fund

The Fremont Pool Trust Fund was established by the City in FY 2002/2003 to account for the receipt of monies raised by The Friends of Fremont Pool, a group of residents who lobbied City Council regarding the need for a new pool in Sunnyvale. The Fund currently has an Endowment Reserve balance of $813,533. The basic premise of this fund is that the corpus, or principal, is never expended. Rather it is invested in a safe, interest-generating market. Each year the interest generated by this fund is transferred to the Community Recreation Fund to help offset the City's cost of operating the new, 50-meter pool constructed in partnership with the Fremont Union High School District at Fremont Union High School. The City has a contract with California Sports Center to program and operate the Fremont Pool on our behalf.

The City's cost is determined by adding 50% of the cost of maintaining the pool itself (performed by the School District, which subsequently bills the City), 100% of the City's cost of maintaining the public shower/locker facility, and staff costs related to oversight of the contract. The City's projected cost for Fremont Pool maintenance for FY 2005/2006, which is programmed in the Community Recreation Fund, is $119,902. Interest earnings on the Fremont Pool Trust Fund are projected to be $32,541. The Trust earnings pay approximately 27% of the City's annual costs, with a transfer from the General Fund making up the difference.

It should also be noted that while the corpus of this fund may grow a bit in future years (assuming continued contributions), it is not expected to increase markedly over time. As a result, it is not expected to keep up with inflation and the purchasing power of the interest it generates will likely erode over time. In this context, and the City's current budget crisis, it is critical to note the importance of allowing the California Sports Center (CSC) to charge market rates for use of the pool. The net revenue received by the City from CSC, and the interest generated by the Fremont Pool Trust Fund, are critical factors in allowing the pool to support itself financially.

APPENDIX A

THE SUNNYVALE APPROACH TO BUDGETING

In reviewing the recommended FY 2005/2006 Budget and Ten-Year Resource Allocation Plan, it is important to understand the key financial and planning systems that Sunnyvale uses to chart its future both in the good times and the bad times. Sunnyvale's approach to budget preparation is a central part of the City's Planning and Management System (PAMS). Key elements of the PAMS framework include:

- Long-range strategic planning (the General Plan Elements and Sub-Elements),
- Long-term financial planning (includes projections over a 20-year time frame for revenues, operations, projects, debt and reserves),
- Short-term allocation of resources (the two-year action budget),
- Performance measurement of service delivery,
- The Council Study Issues process,
- Performance "contracts" for Management,
- Annual performance reporting and evaluation, and
- Performance audits based on risk assessments.

This integrated framework has enabled the City, over time, to accomplish the long-range strategic goals established by Council in the General Plan Elements and Sub-Elements. PAMS has assisted the City in maintaining, and even expanding, services during times of numerous Federal/State mandates and revenue restrictions or reductions because the focus is on long-term fiscal management. PAMS has also served as a valuable tool in producing and capturing remarkable gains in efficiency and productivity.

The Fiscal Sub-Element of the General Plan requires that the City Manager annually propose a budget that is balanced not only for the budget year, but also for the Ten-Year Resource Allocation Plan. Since FY 1993/1994, Council has approved a financial plan that has been balanced to the twentieth year. The long-term nature of the City's financial planning system allows decision-makers to better understand the true effect of policy decisions. Because City practice has been to prepare a fully balanced 20-year financial plan, it effectively requires that decisions made today guarantee that the resources will be available to provide quality services in the future. The Ten-Year Resource Allocation Plan prevents wild swings in service levels during the upturns and downturns of economic cycles.

Annual budget review and approval is a sound business practice and is required by the City Charter. However, an understanding of the City's long-term financial picture is more important to the process than just looking at a one-year or two-year snapshot. Therefore, much of the discussion in this Transmittal Letter will focus on long-term strategic planning and fiscal issues.

PERFORMANCE BASED BUDGETING

The performance based management system is an important part of Sunnyvale's Planning and Management System (PAMS). The City began to implement this management concept in the late 1970's. Last year Council indicated that it would like to see staff complete a comprehensive review and analysis of the performance based management system. The review and analysis of the system began early in FY 2004/2005 and is expected to be complete by the end of the fiscal year. This work is being completed as part of a comprehensive overhaul of the City's Planning and Management System. Work this current year included evaluation of the philosophy and intent of the system as well as the processes that are followed to either establish a new or restructure an existing program to the performance based management system.

Recommended changes to the performance based management system will be brought to Council in a study session format early in FY 2005/2006. Following approval of the revised system, staff will enter into the implementation stage to undertake a major effort to restructure all programs into the revised format. This work will be completed during the first half of FY 2005/2006. This will allow for the revised system to be used in preparing the next two-year operating budget for FY 2006/2007.

OPERATING BUDGET PROCESS

Sunnyvale has practiced two-year budgeting for our operating programs for a number of years. This is in recognition of the tremendous effort needed to develop budgets, particularly with the City's sophisticated performance based budget system. In normal times, service levels remain relatively constant from year to year. By doing two-year budgeting, staff time is maximized and more in-depth review of each budget element can be accomplished. As indicated earlier, FY 2005/2006 is the second year of a two-year operating budget cycle. Therefore, most operating budgets were not reviewed. However, a number of other components of the operating budget were thoroughly analyzed and updated to reflect current conditions. Rental rates and additive rates for the internal service programs were reviewed, with new rates applied to recover costs. Current salary levels for City employees were adjusted based on existing Memoranda of Understanding or estimated salary trends. Employee benefit costs, especially retirement contributions and health insurance costs were reviewed. For enterprise funds, significant cost components were updated with current information and utility rates were adjusted as appropriate. Finally, major revenue sources were updated for all funds.

PROJECTS BUDGET PROCESS

In the City of Sunnyvale the term "project" refers to non-operating activities. Beginning in FY 1999/2000, the City segregated each project into one of four possible categories: Capital, Special, Infrastructure and Outside Group Funding. These categories are defined as follows:

Capital Projects are major expenditures related to construction, improvement or acquisition of capital assets. This category includes feasibility studies, preliminary plans and other projects that are related to design, construction, capital improvement or acquisition. The construction of a traffic signal would be a capital project. Other examples include adding a room to an existing facility (capital improvement) or purchasing a piece of property (acquisition).

Special Projects are one-time only in nature and are set up to eliminate the impact that such costs would have on unit costs in operating programs. This category includes studies and other projects that are not related to construction, capital improvements, renovation/ replacement or acquisition of a capital asset. For example, the preparation of a new sub-element of the General Plan would be a special project.

Infrastructure Projects are inherently related to capital projects. This category includes the renovation and/or replacement of a capital asset. After a capital project is complete, the City has an asset that must be maintained through the operating budget until the asset reaches a point where maintenance costs exceed renovation/ replacement costs. An infrastructure project is developed in order to provide future funds at the time that replacement or renovation is required. An example would be the replacement of major components of the Water Pollution Control Plant or the replacement of the Heating, Ventilation and Air Conditioning (HVAC) system in City Hall.

Outside Group Funding Projects are essentially special projects; however, they are established to identify contributions made to local community-based organizations.

Project Operating Costs are those on-going operating costs that will need to be included in future years upon the completion of a given project. These costs are reflected on each Long Term Financial Plan in the *Current Requirements* section under *Project Operating Costs*. Consideration of this information enables decision-makers to evaluate the complete cost of proposed actions. This prevents the City from adding assets or activities that are not sustainable over the long term.

COUNCIL BUDGET REVIEW PROCESS FOR FY 2005/2006

In FY 2003/2004, Council completed a comprehensive review of City services, service levels, and program budgets to address a continuing structural gap in the City's budget and long-term financial plan. Following this review, Council indicated that it should complete a service and budget review on a regular basis. Because of the resources and time needed to undertake these review, it was determined that one-eighth of all operating programs would be reviewed each year. This way, a councilmember serving two consecutive terms will have reviewed all the City's programs and services.

During April 2005 the City Council completed its first annual service and program budget review of selected City programs. At an all day special meeting, Council conducted an in-depth review of four programs - Water Supply and Distribution, Solid

Waste Management, Wastewater Management, and Utility Billing, Collection and Revenue Management. For each program, staff provided information on the program structure and services, program outcome statement and program measures, service delivery plans, and planned and actual budget costs.

The service and program review process is designed for several purposes:

- To inform Council and the public more completely about the services, service levels, costs and revenues that are associated with the selected City programs that are being reviewed;
- To provide Council with earlier involvement in the development of the City Manager's Recommended Budget and Long Term Financial Plan;
- To encourage more involvement and participation in the annual budget process by residents, business representatives, and community groups; and
- To give Council the opportunity to provide preliminary policy direction regarding services, levels of service, program costs, and the fees and charges associated with the programs under review.

Both the Council and the public indicated their satisfaction with the process used to review these programs. Additional programs will be selected for review at the Fiscal Issues Workshop that will be conducted in January 2006. All City programs will be reviewed by Council at least once every eight years through this process.

BUDGETARY INFLATION FACTOR

Inflation of purchased goods and services for the recommended Ten-Year Resource Allocation Plan and 20-year financial plan is assumed to be 1% for FY 2005/2006, 2% per year for the remainder of the first ten years, and 3% for the second ten years. Certain selected budget components, such as purchased water, gasoline, or electricity are increased (or decreased) according to their individual cost characteristics.

Salary projections are based on current memoranda of understanding (MOUs) with employee associations, with estimates for FY 2005/2006 provided by Human Resources staff after review of each respective salary formula. Assumptions for employees represented by the Public Safety Officers Association (PSOA) are that salaries will increase by 3% for FY 2005/2006, 1% for FY 2006/2007, 3% through FY 2014/2015, and then 4% thereafter. For Sunnyvale Employees Association (SEA) members and Management employees it has been assumed that salaries will increase 0% for FY 2005/2006, 1% for FY 2006/2007, 3% through FY 2014/2015, and 4% thereafter.

Projections for major revenues are based on detailed analyses of their unique characteristics and therefore they do not necessarily reflect a simple inflation pattern. The assumptions for each major revenue source will be detailed in the discussions of each appropriate fund.

The budgetary inflation assumptions mentioned above are particularly significant since the City utilizes multi-year financial planning over a twenty-year period. Small

changes can have a significant long-term effect. For example, a $1 million loss in revenue or a $1 million increase in operating expenses in an assumed 3% inflation environment amounts to a cumulative $26.87 million change in position over the entire planning period.

BUDGET FORMAT AND AWARDS

Sunnyvale has a thorough and detailed budget preparation, review and adoption process. Staff has traditionally presented to Council the City Manager's recommended Budget in the form of a workbook. This workbook is used to guide the Council through the budget workshop, the public hearing and finally the official adoption of the budget for the upcoming fiscal year.

The recommended Budget document is divided into three volumes. *Volume I* includes the *City Manager's Transmittal Letter*, *Budget Summary*, *Long-Term Financial Plans*, *Revenues*, and *User Fees. Volume I* is useful as a summary document, with more detailed information found in the other three volumes.

Volume II Projects Budget contains all of the City's capital, infrastructure, special and outside group funding efforts. This volume begins with a *Projects Budget Guide* that describes what a project is in the City of Sunnyvale and how projects are prioritized in the budget process. This volume receives detailed attention during the "on year" for projects, which is FY 2005/2006.

Volume III Operating Budget contains all of the City's programmatic efforts. This volume also begins with an *Operating Budget Guide* that describes Sunnyvale's unique Planning and Management System. The Operating Budget is organized around the seven elements of the General Plan. Each element contains the General Plan's Goals, Policies and Action Statements, Community Condition Indicators, and the budget of each operating program that is tied to that particular element. This volume receives detailed attention during the "on year" for operating, which was FY 2004/2005.

In prior years staff has received positive feedback from Council members and citizens regarding the Budget-in-Brief booklet. This is an effort to highlight the important aspects of the particularly large and complex recommended Budget document. This year, staff will again prepare this summary containing the City Manager's Transmittal Letter and Budget Summary.

In December 2004 the Department of Finance was notified that the City's adopted FY 2004/2005 Budget and Ten-Year Resource Allocation Plan had received the Distinguished Budget Presentation Award from the Government Finance Officers Association (GFOA), a national organization of finance professionals. This award program, established in 1984, "recognizes exemplary budget documentation by state, provincial and local government, as well as public universities and colleges." The City has received this award for 16 consecutive years. In addition to qualifying for the award this year, our Budget received "special performance measures" recognition because we were rated outstanding by all raters in the performance measures category.

APPENDIX B

STRATEGIES AND COST SAVING IDEAS TO BE EXPLORED IN 2004/2005

EMPHASIZE ECONOMIC DEVELOPMENT		
CDD	1.	Re-examine economic development strategies to ensure that short term and long term goals are achieved and deliverable, including explore incentives
USE TECHNOLOGY TO REDUCE COSTS		
CDD	2.	E-mail business newsletter rather than mail hard copy
CDD	4.	Continue roll-out of hand held units for field operations
ITD	7.	Establish investment fund to review and implement automation of processes citywide that are not currently automated
FIN/DPW/ITD	8.	Continue the deployment of remote meter reading technology
EXPLORE ALTERNATIVE SERVICE DELIVERY METHODS		
DPR	10.	Explore contracting out gymnastics classes
OCM	11.	Redesign Organizational Effectiveness program to focus on PAMS and cost containment practices
MANAGE/CONTAIN EMPLOYEE SALARIES AND BENEFITS		
HRD/DPW/ITD	13.	Utilize flexible schedules to reduce overtime needs
HRD/FIN/ITD	15.	Investigate tiered employee benefits for new hires
FIN	19.	Conduct audit of overtime usage citywide
HRD	20.	Explore alternate medical insurance plans
HRD	22.	Institute a vesting requirement for retiree medical benefits
HRD	23.	Investigate substituting a PTO program for disability where possible
HRD	28.	Review provisions of new workers' compensation law
HRD	30.	Reevaluate the disability leave incentive program
HRD	31.	Focus on reducing workers' compensation claims/costs

STREAMLINE CITY PROCESSES		
DPR	34.	Combine Parks and Recreation Commission with Arts Commission
OCM	35.	Consolidate/update administrative policies
MANAGE THE CITY'S "LIVESTYLE" AND EMPLOYEE EXPECTATIONS		
FIN	36.	Review level of items supplied by central stores to employees
DPS/DPW/FIN	38.	Reduce low use fire apparatus
EXPLORE REDUCING CITY HOURS OF OPERATION		
CDD/HRD/LIB	42.	Close City offices between Christmas and New Years with use of PTO or unpaid time
DPR/HRD/CDD	43.	Utilize different/shorter business hours for the public
EXAMINE WAYS TO MORE EFFECTIVELY USE CITY WORKFORCE		
DPR	46.	Eliminate one recreation Superintendent position, replace with lower position
HRD	47.	Explore expanded use of job sharing and allowing more part time employees
DPS	51.	Freeze vacant management positions in DPS during vacancy of Chief
DPS/FIN	52.	Change traditional backfill requirements in Fire when a short term (sick day, etc.) vacancy occurs
OCM/HRD	54.	Study Pay for Performance System
FIN/DPS	56.	Review practice of fire station staffing versus requirements in MOU
FIN/DPS	57.	Review patrol minimum staffing requirements in MOU
DPS/HRD	58.	Investigate use of part time Public Safety Officers and Public Safety retirees
FIN/DPS	59.	Review start times for Patrol schedule
FIN/DPS	60.	Evaluate need for Sworn/Non-Sworn Management positions in DPS
REVIEW FUND RESERVE POLICIES		
FIN/DPW/DPR/ITD	63.	Review all equipment replacement reserves

REVIEW CITY'S COST RECOVERY POLICY FOR FEES AND CHARGES		
FIN	66.	Explore full cost recovery of DPS permits for taxicabs, adult entertainment, pawn shops, massage parlors, and weapons
DPW/FIN/ ITD	67. & 76.	Revisit policy of keeping utility rates below average of surrounding cities and Update Phase I of the Long Range Infrastructure Plan and complete Phase II
FIN/DPR/LIB/CDD	68.	Update subsidy analysis of Community development, Recreation, and SCI3 programs
INVESTIGATE NEW AND INCREASED REVENUE SOURCES		
DPR	70.	Expand park picnic rental services, e.g. inflatable jumpers, etc.
FIN/OCA	72.	Explore increase in Business License Tax
FIN/OCA	73.	Explore increase in Transient Occupancy Tax
EVALUATE CITY'S POLICY REGARDING LAND HOLDINGS		
CDD/DPW/OCA	74.	Determine legal standing of Charles Street lot and responsibility for maintenance
MISCELLANEOUS		
DPR	77.	Evaluate recreation services fee waiver program and program admin
FIN/DPS	78.	Complete optimal staffing study for Public Safety Department
OCM	81.	Undertake comprehensive review and analysis of the outcome management system
OCM	82.	Develop and conduct PAMS training at all levels
DPW/FIN	83.	Perform complete update and review of Capital Improvement Program, including unfunded projects over 10-year plan
ADDED FROM ELT STRATEGY MEETING OF 5/27/04		
OCM/HRD/DPR	84.	Review all employee evaluation systems

JUST DO IT		
MANAGE/CONTAIN EMPLOYEE SALARIES AND BENEFITS		
OCA/HRD	29.	Review workers' compensation legal requirements as they relate to selection of physician and time off for workers' compensation medical appointments
EVALUATE CITY'S POLICY REGARDING LAND HOLDINGS		
DPW/DPR	75.	Analyze additional income potential of 505. W. Olive property

APPENDIX C

Human Services Recommendations-Outside Groups
General Fund and CDBG Fund

FY 2005/06

Outside Groups	2001	2002	2003	2004	2005 Request	HHSC Recommended		Staff Recommended	
CDBG SUPPORTED						**CDBG**	**GENERAL**	**CDBG**	**GENERAL**
Catholic Charities Shared Housing	16,170	16,170	16,500	11,000	15,000	10,000	0	10,000	0
Catholic Charities Ombudsman	11,195	13,641	13,060	12,407	13,212	13,212	0	13,212	0
Community Association for Rehabilitation	5,253	7,522	5,950	5,653	6,025	6,025	0	6,025	0
Cupertino Comm. Services	14,669	10,000	14,670	13,937	20,000	15,000	0	15,000	0
Emergency Housing Consort.	54,791	56,435	58,720	55,784	75,000	56,500	0	56,500	0
First United Methodist. Senior Nutrition	16,730	22,842	23,742	22,555	23,742	24,000	0	24,000	0
Project Match	8,685	8,685	11,193	10,833	14,000	14,000	0	14,000	0
Second Harvest Food Bank	5,100	7,211	5,610	5,330	5,490	5,490	0	5,490	0
Senior Adults Legal Assist.	10,398	10,710	11,030	10,479	10,479	10,479	0	10,479	0
Sunnyvale Comm. Services	61,407	65,360	77,533 (16,000)[1]	73,656 (20,000)[1]	98,339	65,552	32,787	65,552	32,787
Support Network For Battered Women	32,000	24,000	24,000	22,800	32,000	32,000	0	32,000	0
The Health Trust-Meals on Wheels	0	0	12,750	12,113	13,650	13,650	0	13,650	0
Friends For Youth-Mentoring	0	0	18,750	17,813	17,800	17,800	0	17,800	0
CDBG Prior Years [2]	271,478	269,772	306,016	283,193					
General Fund Supported									
Euphrat Art Program	12,298	12,298	12,298	12,300	12,298	0	12,298	0	12,298
Family and Child. Ser.	0	0	30,000	30,000	31,100	21,100	10,000	21,100	10,000
Junior Achievement	10,000	10,000	10,000	10,000	11,165	0	11,165	0	11,165
Leadership Sunnyvale	5,000	5,000	5,000	7,000	10,000	0	8,000	0	10,000
Live Oak/Adult Ser.		44,881 [5]	30,000	28,000	29,400	19,400	10,000	19,400	10,000
Bill Wilson Center	15,227	15,227	15,000	16,750	32,000	17,000	7,500	17,000	7,500
India Comm. Center	0	0	0	0	25,000	8,792	2,000	8,792	3,708
General Fund Prior Years [2]	81,000	85,000	118,000	124,000					
Total Outside Group Funded [2]	352,478	354,772	424,016	407,193	508,200 [4]	350,000	100,000	350,000	97,458
Rebuilding Together Peninsula	0	0	0	0	12,500	0	6,250	6,250 [3]	

TOTAL General Fund Recommendations FY 2005-06 **97,458**

[1] Sunnyvale Community Services received $20,000 General Fund FY 2004/05 and $16,000 General Fund FY 2003/04.
[2] Includes funding of agencies not currently receiving funds.
[3] Funding to be provided by CDBG Housing Improvement Program Funds.
[4] Includes request by Rebuilding Together Peninsula.
[5] 2002 funding from Special Funds.