



CITY OF
**PALO
ALTO**

City Council Staff Report

From: City Manager

Report Type: ACTION ITEMS

Lead Department: Administrative Services

Meeting Date: January 20, 2026

Report #:2512-5601

TITLE

Review the FY 2027-FY 2036 Long Range Financial Forecast (LRFF) and FY 2027 Budget Development Guidelines using the LRFF as the Baseline for Developing the FY 2027 Budget as Recommended by the Finance Committee, CEQA Status – Not a Project

RECOMMENDATION

The Finance Committee and staff recommend the City Council accept the Long Range Financial Forecast (LRFF) for Fiscal Year 2027-2036 (Attachment A) and the FY 2027 annual Budget Development Guidelines (Attachment B) and direct staff to use this forecast as the baseline for developing the FY 2027 budget.

EXECUTIVE SUMMARY

On December 2, 2025 the Finance Committee reviewed the FY 2027-2036 Long Range Financial Forecast (LRFF) (Attachment A) along with the annual Budget Development Guidelines (Attachment B) and unanimously recommended that it be forwarded to the City Council for acceptance¹. The Committee also reviewed major tax revenues and Section 115 Pension Trust on November 18, 2025 which were incorporated into this LRFF².

This preliminary forecast is based on the most current information available, actual revenues and expenses for FY 2025, and projected results through FY 2026 at the report was released. General Fund expenditures are based on current City Council approved service levels, including the recent expense reductions approved by the City Council on September 8, 2025.³The current outlook anticipates continued economic stagnation and uncertainty, which is reflected in this forecast.

¹ Finance Committee, December 2, 2025; Agenda Item #3; SR #2511-5473,
<https://cityofpaloalto.primegov.com/Portal/Meeting?meetingTemplateld=16338>

² Finance Committee, November 18, 2025; Agenda Item #2; SR # 2511-5392,
<https://portal.laserfiche.com/Portal/DocView.aspx?id=236317&repo=r-704298fc&searchid=a6cdeee1-f142-41c5-be56-9a6a512108b3>

³ City Council, September 8, 2025; Agenda Item #3; SR #2506-4818,
<https://portal.laserfiche.com/Portal/DocView.aspx?id=221264&repo=r-704298fc&searchid=95735611-6c94-45fd-9e08-5713bd4b0286>

The base case LRFF projects a shortfall of \$14.9 million in FY 2027, followed by shortfalls ranging from \$15.1 million in FY 2029 down to \$6.2 million in FY 2032. FY 2033 has a projected surplus of \$1.0 million which continues to grow through FY 2036. This forecast maintains current service levels approved in FY 2026 and should be used for planning purposes to assist in gauging effects of major policy interventions against a likely 'status quo' version of the future.

These amounts represent a larger than previously projected deficit. The projected \$14.9 million shortfall for FY 2027 is \$6.8 million greater than the \$8.1 million deficit forecasted for FY 2027 just seven months ago (May 2025) and \$7.0 million greater than the \$7.9 million projected in the December 2024 LRFF. This change is driven by a combination of lower projected revenue (most notably Property Tax and Sales Tax) and higher-than-anticipated expenditure growth (detailed in Attachments C and D). City staff will continue to review and refine these projections to establish the FY 2027 budget. Individual fiscal years will vary from this forecast as changes in revenue estimates or operating transfers occur.

Instead of modeling alternative budget scenarios, staff developed a menu of budget balancing strategies for the Council's consideration. This framework provides budget-balancing options, including revenue enhancements, expenditure reductions, and adjustments to pension and capital funding. The strategies are designed to facilitate a discussion on the trade-offs required to close the budget deficit in FY 2027 as well as the structural deficit in the out-years.

While the projections in the FY 2026 Adopted Budget included deficits in the LRFF, this revised LRFF reflects larger deficits in the near term primarily due to reduced property and sales tax revenue. The FY 2026 budget process addressed the projected shortfall with some ongoing budget cuts and dedicated one-time reserves. The City now faces the challenge of developing the FY 2027 budget and planning for the subsequent years, which will require strategic work over the next several months to balance the community's desired service levels with the financial resources projected.

BACKGROUND

Annually, the Office of Management and Budget produces a ten-year General Fund Long Range Financial Forecast (LRFF). The LRFF reflects staff's best estimates on the projected revenues and expenditures over the next ten years based on the information that is currently available. It is important to note that the LRFF is a planning document and is separate and distinct from the development of the City's annual Operating and Capital Budgets. There are assumptions and parameters modeled in the LRFF, and these assumptions are revised and refined as more information becomes available through the budget development process.

The LRFF contains a high-level comprehensive review of revenues and expenditures, especially costs to provide current City Council-approved service levels, including current contracts, updates to salaries and benefits based on the current employee population, and current labor contracts. This Forecast provides short-term and long-term financial status of current service

levels to inform policy decisions and evaluate long-term goals. The City Council last accepted the FY 2027-2036 Long Range Financial Forecast on January 13, 2025.⁷

Per City Council policy, items that are unanimously approved by the Finance Committee are placed as a consent agenda item for the City Council. Though this report was approved unanimously, staff and the Committee have placed this item on the City Council’s action agenda for deliberation of the full Council to acknowledge the importance for financial planning.

ANALYSIS

Finance Committee Review

The Finance Committee reviewed the FY 2027-2036 Long Range Financial Forecast (LRFF) on December 2, 2025. Following this review, staff updated the attached LRFF (Attachment A) to ensure the data aligns with the final presentation materials delivered to the Committee. These revisions specifically make minor adjustments in Table 1 Base Case and Table 5 Revenues. For the City Council's immediate reference, the updated Table 1: FY 2027-2036 Long Range Financial Forecast (Base Case) is provided below.

Revised Table 1: FY 2027-2036 Long Range Financial Forecast (Base Case)
(All figures in millions)

	FY 26 Adopted	FY 26 Projected	FY 27	FY 28	FY 29	FY 30	FY 31	FY 32	FY 33	FY 34	FY 35	FY 36
TOTAL REVENUE	\$307.2	\$298.0	\$305.1	\$316.9	\$327.2	\$340.4	\$353.0	\$365.2	\$378.4	\$390.3	\$404.6	\$418.8
Revenues	\$301.2	\$292.2										
Uncert Reserve	\$5.8	\$5.8										
TOTAL EXPENDITURES	\$307.0	\$307.0	\$320.0	\$329.7	\$342.5	\$354.6	\$363.7	\$371.6	\$377.4	\$386.0	\$393.3	\$405.6
SURPLUS/ (DEFICIT)	\$0	(\$9.0)	(\$14.9)	(\$12.8)	(\$15.3)	(\$14.2)	(\$10.7)	(\$6.4)	\$1.0	\$4.3	\$11.3	\$13.2

Revised Table 2: FY 2027-2032 Budget Balancing Strategies
(All figures in millions)

	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032
Revenues:						
Explore new/updated fees and other revenues	\$0.8	\$0.8	\$0.8	\$0.9	\$0.9	\$0.9
Budget Stabilization Reserve (BSR)	\$2.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Budget Reductions:						
FY 26 <i>Approved</i> Reductions thru FY 32 (\$6 m w/\$3.4 m on-going ~ \$2.4m GF + \$1 m CIP)	\$3.4 in base	\$3.4 in base	\$3.4	\$3.4	\$3.4	\$3.4
FY 27 <i>Additional</i> Reductions thru FY 32 (to be determined during FY 2027 budget development)	\$7.0	\$7.0	\$7.0	\$5.8	\$2.3	\$2.1

⁷ City Council, January 13, 2025, Agenda Item #12, SR #2412-3846,
<https://portal.laserfiche.com/Portal/DocView.aspx?id=125154&repo=r-704298fc&searchid=414f71d9-32af-44ed-a9e5-7e982f57164e>

	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032
CIP Reductions:						
FY 2027 <i>Additional</i> Reduction to Capital (to be determined during FY 2027 budget development)	\$1.0	\$1.0	\$0.0	\$0.0	\$0.0	\$0.0
Pension Cost:						
Reduce Additional Discretionary Payment (ADC)	\$3.6	\$3.6	\$3.6	\$3.6	\$3.6	\$0.0
Reduce Additional Discretionary Payment (ADP)	\$0.5	\$0.5	\$0.5	\$0.5	\$0.5	\$0.0
BUDGET STRATEGY TOTAL:	\$14.9	\$12.9	\$15.3	\$14.2	\$10.7	\$6.4
Remaining Surplus/(Deficit)	\$0.0	\$0.1	\$0.0	\$0.0	\$0.0	\$0.0

As part of the Committee’s review of the LRFF, several topics were discussed more in depth and staff has provided additional information for context and/or additional data points for reference to the City Council.

- Services/Programs and Council Priorities** – Committee acknowledged that given the General Fund deficit the Council would need to consider suspending or discontinuing City services/programs. The General Fund deficit would also impact funding for Council priorities and objectives. The budget balancing strategies include \$7 million in General Fund budget cuts and \$1 million in capital cuts (i.e. defer/reduce projects and/or fund balance). Staff will work with the Finance Committee and Council through the FY27 budget process; staff will continue identifying service efficiencies before reductions to minimize impacts to the community.
- Property Tax and Sales Tax Projections** – Committee discussed the downward projections for property tax and sales tax revenues. The reduced property tax revenue is based on a true-up to actual FY 2026 tax roll, which was lower than estimated and revised outlook to mid-4% growth from low-6% growth assumed in prior LRFF. This incorporates the current economic outlook and HdL property tax guidance. However, the forecast does not consider future housing growth (or its associated increased cost of city services), as timing and fiscal impacts are speculative. The City’s property tax, based on property value, mix is approximately 70% residential and 30% non-residential. As of the most recent County reporting for 2025 countywide property tax appeals, there were 5,659 appeals filed, of which 1,486 are active, totaling \$5.8 billion at risk countywide.⁹ This is an increase from the same period in 2024, with 4,582 appeals filed. For FY 2026, the county projects tax roll reduction correction totaling \$43.3 million (relative to Countywide total tax levy of \$6.9 billion) of which the City’s proportionate share is 0.7% (0.007) or \$0.3 million. The tax roll corrections are incorporated into the FY 2026 property tax projections and LRFF. The Committee was supportive of the revised property tax assumptions and forecast.

⁹ Cities Meeting, November 12, 2025,
<https://controller.santaclaracounty.gov/cities/cities-meetings>

The City continues to monitor pending litigation between Marin County and the California State Controller regarding the methodology used to calculate excess Educational Revenue Augmentation Fund (ERAF) distributions, which may affect Santa Clara County. A court hearing on this matter is expected to continue in March 2026. To mitigate potential impacts, the City has retained at-risk amounts in reserve and will update assumptions as new information becomes available.

The Finance Committee also discussed reduced expected sales tax revenue (previously reviewed by the Finance Committee on November 18) resulting from modified regulations used by the California Department of Tax and Fee Administration (CDTFA) in apportioning sales tax revenue from the leasing and new auto sectors. Staff continues to work with the State and business community on this matter. Furthermore, the Committee emphasized the importance of explaining that property tax and sales tax challenges worsened the City's finances.

- **Transient Occupancy Tax (TOT)** – Committee requested in-depth information regarding TOT drivers of trends and projections. TOT projections are based on historical revenue performance and hotel operating metrics, including average daily room rates and occupancy. The Q1 FY 2026 results reviewed by the Committee on December 2 were based on information available at the time of reporting and have since been updated. For the completed quarter, hotels reported an average daily room rate of \$272.19 and occupancy of 84.19% in Q1 FY 2026, compared to \$291.33 and 72.52% in Q1 FY 2025. While average room rates declined year over year, higher occupancy supported Q1 FY 2026 revenues of \$7.5 million, an increase of \$0.4 million or 5.5%, from the prior year.

Over the longer term, TOT has grown at a Compound Annual Growth Rate of 9.3% (five years) and 5.7% (10 years), respectively. This growth reflects the addition of three new hotels and approximately 400 hotel rooms since 2021, bringing total citywide inventory to approximately 2,500 rooms. The LRFF assumes ongoing TOT growth of approximately 4-5% annually over the forecast period, aligning more closely with long-term growth trends.

- **Vacancy Rate** – The LRFF includes 5% vacancy assumption, which Committee concurred after further review of current data. Available vacancy data reviewed:
 - October vacancy: 11.6% ~ as of Q1 FY 2026
 - General Fund vacancy rate: 9.6%
 - Enterprise Fund vacancy rate: 15%
 - General Fund vacancy rate (no public safety vacancies): 6.3%
- **2019 to current Trends** – Where multi-year trends are presented, Committee requested 2019 be included to reference pre-pandemic levels as baseline. Staff completed the historical summary of General Fund staffing by department since 2019

(Attachment B). Also, Staff will gradually incorporate with key charts with historical trends.

- **Known Unknowns** – Committee clarified that while the LRFF does not include funding from the General Fund for the projects/priorities within the Known Unknown listing, these projects may be funded by other funding source(s) (i.e. Measure B, Measure K, impact fees, etc).

FISCAL/RESOURCE IMPACT

Financial implications from this report and input from the City Council will be considered in the City Manager’s development of the Fiscal Year 2027 budget. Upcoming milestones related to the City’s fiscal standing and the FY 2027 Budget Process include:

- February (Council) – FY 2026 Mid-Year Budget Review and Second Quarter Financial Report
- March/April (Finance Committee and Utilities Advisory Commission or UAC) – Five Year Utility Financial Plans and FY 2026 Utility Rate Recommendations
- April/May (Finance Committee) – Citywide Cost Allocation Plan and Municipal Fee Study
- May (Council) – FY 2027 Proposed Operating and Capital Budgets Published
- May (Finance Committee) – FY 2027 Proposed Budget Hearings, including Utility Rates, Municipal Fees, and Five-Year Capital Improvement Plan
- June (Finance Committee) – FY 2026 Third Quarter Financial Report
- June (Council) – Adoption of the FY 2027 Operating and Capital Budgets, Utility Rates, and Municipal Fees.

STAKEHOLDER ENGAGEMENT

The preliminary forecast for FY 2026 represents the beginning of the fiscal year 2026 budget development process. As in previous years, City Council discussion of the LRFF will provide guidance to staff in the budget development process. It is anticipated that conversations with City Council and the community will occur through public budget hearings in Spring 2026, according to the standard budget adoption process. The community can track previous and upcoming FY 2027 budget discussions and information at www.cityofpaloalto.org/budget.

ENVIRONMENTAL REVIEW

Council action on this item is not a project as defined by the California Environmental Quality Act (CEQA) because accepting the LRFF and budget guidelines is fiscal activity which does not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment. CEQA Guidelines section 15378(b)(4).

ATTACHMENTS

Attachment A: FY 2027-2036 Long Range Financial Report (LRFF), CMR 2511-5473

Attachment B: Historical Staffing by Department – General Fund (adopted vs vacant)

APPROVED BY:

Lauren Lai, Administrative Services Director



CITY OF
**PALO
ALTO**

Finance Committee Staff Report

From: City Manager

Report Type: ACTION ITEMS

Lead Department: Administrative Services

Meeting Date: December 2, 2025

Revised Report #:2511-5473

TITLE

Review and Recommend the City Council Accept the FY 2027- 2036 Long Range Financial Forecast and FY 2027 Annual Budget Development Guidelines. CEQA Status—Not a Project.

RECOMMENDATION

Staff recommends that the Finance Committee review and recommend that the City Council accept the General Fund Long Range Financial Forecast (LRFF) for Fiscal Years 2027-2036 and the FY 2027 annual Budget Development Guidelines (Attachment A) and direct staff to use this forecast as the starting point for the FY 2027 budget process.

EXECUTIVE SUMMARY

Annually in December, the City presents a ten-year General Fund Long Range Financial Forecast (LRFF) that marks the beginning of the budget process. This preliminary forecast is based on the most current information available, actual revenues and expenses for FY 2025, and projected results through FY 2026. General Fund expenditures are based on current City Council-approved service levels. The current outlook anticipates continued economic stagnation and challenges.

The LRFF is a tool to model financial forecasting assuming resources and services are operating at the current authorized levels. City staff will continue to review and refine these projections to establish the FY 2027 budget. Individual fiscal years will vary from this forecast as changes in revenue estimates or operating transfers occur.

The Base Case LRFF projects a deficit of \$14.9 million in FY 2027, followed by deficits ranging from \$15.3 million in FY 2029 down to \$6.4 million in FY 2032. These deficits have doubled compared to prior forecasts, primarily due to the State's reallocation of local sales tax revenues. FY 2033 has a projected surplus of \$1.0 million which continues to grow through FY 2036.

These amounts represent a larger projected deficit than in prior projections. The projected \$14.9 million deficit for FY 2027 is \$6.8 million higher than the \$8.1 million deficit forecasted for FY 2027 just seven months ago (May 2025) and \$7.0 million higher than the \$7.9 million projected in the December 2024 LRFF. This change is primarily driven by a combination of lower revenues (most notably Sales Tax) and to a lesser extent, higher-than-anticipated expenditure growth. This

forecast (detailed in Attachments C and D) maintains current service levels approved in FY 2026 and should be used for planning purposes to assist in gauging the effects of major policy interventions.

Instead of modeling alternative scenarios for this LRFF, staff has developed a "Budget Balancing Sandbox" for Committee and Council consideration. This "Sandbox" provides a menu of potential budget-balancing options, including revenue enhancements, expenditure reductions, and adjustments to pension and capital funding. This framework is designed to facilitate a strategic discussion on the trade-offs required to close the budget deficit in FY 2027 as well as the structural deficit in the out-years. The Finance Committee reviewed major tax revenues and the retiree benefit funding policy, specifically for the Section 115 pension trust on November 18, 2025¹. The Finance Committee supported the Section 115 pension recommendations, and the sandbox incorporates that among its options for budget balancing.

Consistent with the projections in the FY 2026 Adopted Budget, this LRFF reflects deficits as revenues are outpaced by expenses. As part of the FY 2026 budget process, the projected deficit was addressed with budget reductions of \$6 million (approximately 2%) and using one-time reserves. In developing the FY 2027 budget and planning for the subsequent years, staff will continue the strategy of balancing increasingly constrained projected financial resources and the community's desired service levels.

Included in this report and subsequent attachments are the following:

- The Economy: discussion of the current financial climate (Attachment B)
- Summary Long Range Financial Forecast including Revenue and Expense assumptions in FY 2027-2036 (Attachments C and D)
- FY 2027 Budget Development Guidelines to inform the budget process (Attachment A)
- A summary of Assumptions Not Included in Forecast (Attachment E)

BACKGROUND

Annually, the Office of Management and Budget produces a ten-year General Fund Long Range Financial Forecast (LRFF). The LRFF reflects staff's best estimates on the projected revenues and expenditures over the next ten years based on the information that is currently available. It is important to note that the LRFF is a planning document and is separate and distinct from the development of the City's annual Operating and Capital Budgets. There are assumptions and parameters modeled in the LRFF, and these assumptions are revised and refined as more information becomes available through the budget development process.

The LRFF contains a high-level comprehensive review of the costs to provide current City Council-approved service levels, including current contracts, updates to salaries and benefits based on the current employee population, and current labor contracts. This Forecast allows staff and the Finance Committee to look at both the short-term and long-term financial status of current

¹ City Council, November 18, 2025; Agenda Item # 2:

<https://portal.laserfiche.com/Portal/DocView.aspx?id=236317&repo=r-704298fc&searchid=5d4c2a19-d8fb-4dc5-9540-dae614677957>

service levels to inform policy decisions and evaluate long-term goals. The City Council last accepted the FY 2026-2035 Long Range Financial Forecast on January 13, 2025.³

The Economy

At the national level, economic growth has shown significant strength through the third quarter of calendar year 2025, led by robust GDP (gross domestic product) growth. Consumer spending has remained resilient despite inflation rates that have ticked up from the prior year. As of September 2025, the Consumer Price Index (CPI), which measures changes in the prices paid by consumers for a basket of goods and services, was 3.0%. This is higher than the 2.6% CPI from a year ago. Assumptions in the LRFF report for general cost increases are using a CPI of 3% in FY 2026 and FY 2027 and 4% for FY 2028 and beyond. The national unemployment rate, as of August 2025, is 4.3%, a modest increase from 4.1% in October of the prior year, suggesting a labor market that is cooling but not contracting. This slowdown is consistent with the Federal Reserve's monetary policy intended to curb inflation without initiating a recession. Key factors to monitor include future Federal Reserve policy, ongoing geopolitical events, and the impact of tariffs on inflation.

The local economy, in contrast, is projected to experience a more sluggish recovery. The latest Fall 2025 UCLA Anderson outlook states that while the U.S. economic recovery may begin in mid-2026, "the California recovery will begin later, getting underway late next year and accelerating in 2027." The forecast notes that a rebound in the technology and aerospace sectors will be critical for this recovery, though this has yet to fully materialize. Locally, the unemployment rate for Santa Clara County was 4.7% in August 2025, tracking higher than the national average and indicating specific softness in the regional tech labor market. This in turn impacts local economic activity impacting major revenues, including property and sales taxes.

The erosion of purchasing power from inflation remains a key watch item; however, consumer spending remains resilient. Personal consumption expenditures (PCE) are the primary measure of consumer spending. According to the U.S. Bureau of Economic Analysis (BEA), the headline PCE price index rose 2.7% year-over-year as of August 2025. A key component, the core PCE price index (which excludes food and energy), rose 2.9% year-over-year. This core measure is the Federal Reserve's preferred inflation gauge, and its persistence well above the 2% target adds leeway for the Federal Reserve to hold interest rates at a restrictive level. Also, the United States consumer confidence for November 2025 dropped to 51, hovering near one of the lowest levels in the poll's history. This economic environment creates heightened complexity in financial forecasting. It is important to recognize that while the local economy within the City may exhibit trends similar to those at the state or national levels, its unique economic makeup will result in distinct variations. Staff is using the current available information to inform this forecast, which will change as new information becomes available and adjustments may be necessary to reflect evolving conditions. Additional details on economic statistics can be found in Attachment B.

³ City Council, January 13, 2025; Agenda Item #12;
<https://portal.laserfiche.com/Portal/DocView.aspx?id=125154&repo=r-704298fc&searchid=3269d775-c568-4189-bb60-a18f3c9899e8>

ANALYSIS

As with all forecasts, there is uncertainty regarding the revenue and expenditure estimates. This report is a continuation of the financial review presented to the Finance Committee on November 18, 2025, and provides the full ten-year forecast based on the updated revenue figures discussed at that meeting⁵. As noted in the Executive Summary, the Base Case forecast projects a structural deficit from FY 2027 through FY 2032. This deficit is primarily driven by the revenue projections, particularly for sales tax, that were reviewed on November 18. This is combined with a 4.3% expenditure growth (approximately \$13.1 million) from the FY 2026 Adopted Budget (\$306.9 million), driven by contractual and inflationary increases in salaries, benefits, and services.

Base Case

Table 1 displays the projected General Fund revenues and expenditures over ten years and the cumulative net operating margin. The operating margin reflects the variance between the projected General Fund revenues and expenditures for each year of the forecast or the annual surplus or deficit. The net operating margin is presented on a one-time basis (the "Surplus/(Deficit)" line). An incremental forecast (not shown in the table) assumes that each deficit is addressed completely with ongoing solutions in the year it appears and that each surplus is completely expended with ongoing expenditures. It is the City's goal to remain in balance on an ongoing basis. To the extent a deficit is not resolved, or a surplus is not expended on an ongoing basis, the remaining budget deficit or surplus will be pushed to the following year.

The Base Case financial forecast projects a deficit of \$14.9 million in FY 2027, followed by deficits ranging from \$6.4 million to \$15.3 million through FY 2032. A surplus is not projected until FY 2033.

Revised Table 1: FY 2027-2036 Long Range Financial Forecast (Base Case)

(All figures in millions)

	FY 26 Adopted	FY 26 Projected	FY 27	FY 28	FY 29	FY 30	FY 31	FY 32	FY 33	FY 34	FY 35	FY 36
TOTAL REVENUE	\$307.2	\$298.0	\$305.1	\$316.9	\$327.2	\$340.4	\$353.0	\$365.2	\$378.4	\$390.3	\$404.6	\$418.8
Revenues	\$301.2	\$292.2										
Uncert Reserve	\$5.8	\$5.8										
TOTAL EXPENDITURES	\$307.0	\$307.0	\$320.0	\$329.7	\$342.5	\$354.6	\$363.7	\$371.6	\$377.4	\$386.0	\$393.3	\$405.6
SURPLUS/ (DEFICIT)	\$0	(\$9.0)	(\$14.9)	(\$12.8)	(\$15.3)	(\$14.2)	(\$10.7)	(\$6.4)	\$1.0	\$4.3	\$11.3	\$13.2

⁵ Finance Committee, November 18, 2025; Agenda Item #2;

<https://portal.laserfiche.com/Portal/DocView.aspx?id=236317&repo=r-704298fc&searchid=fdc8782f-774d-4982-895c-a706c1bdb6a9>

Staff has developed a comprehensive Budget Balancing Sandbox as a critical step to proactively address the projected structural deficit, offering a menu of financial strategies that close a gap of \$14.9 million in FY 2027. These options illustrate the opportunities and trade-offs necessary to achieve immediate budget balance and systematically contribute to closing the structural deficit extending through FY 2032. The fundamental challenge remains in creating a responsible and strategic mix of one-time tools to fix the immediate FY 2027 problem and ongoing solutions required to address the structural imbalance over the next five years to achieve long-term fiscal stability.

Revised Table 2: FY 2027-2032 Balancing "Sandbox" Options
(All figures in millions)

	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032
Revenues						
Explore new/updated fees and other revenues	\$0.8	\$0.8	\$0.8	\$0.9	\$0.9	\$0.9
Budget Stabilization Reserve (BSR)						
Budget Stabilization Reserve (BSR)	\$2.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Budget Reductions						
FY 26 Approved Reductions thru FY 32 (<i>\$6 m w/\$3.4 m on-going ~ \$2.4m GF + \$1 m CIP</i>)	\$3.4M in base	\$3.4M in base	\$3.4	\$3.4	\$3.4	\$3.4
Budget Reductions						
FY 27 Additional Reductions thru FY 32	\$7.0	\$7.0	\$7.0	\$5.8	\$2.3	\$2.1
CIP Reductions						
FY 2027 Additional Reduction to Capital	\$1.0	\$1.0	\$0.0	\$0.0	\$0.0	\$0.0
Pension Cost						
Reduce Additional Discretionary Payment (ADC)	\$3.6	\$3.6	\$3.6	\$3.6	\$3.6	\$0.0
Pension Cost						
Reduce Additional Discretionary Payment (ADP)	\$0.5	\$0.5	\$0.5	\$0.5	\$0.5	\$0.0
BUDGET STRATEGY TOTAL:	\$14.9	\$12.9	\$15.3	\$14.2	\$10.7	\$6.4
Remaining Surplus/(Deficit)	\$0.0	\$0.1	\$0.0	\$0.0	\$0.0	\$0.0

Budget Balancing Sandbox for Consideration

The Budget Balancing Sandbox outlines a multifaceted and multi-year budget balancing strategy, includes reductions on top of FY 2026 reductions of \$6 million (or 2%), explores revenues, and service delivery efficiencies. It also charts a path forward for continued planning for reductions in pension liabilities, reinforcing the adopted Retiree Benefits Policy. Lastly, Staff strive to maintain the budget stabilization reserve at the 18.5% Council directed level. Together, these strategies will serve as a foundation for several Council actions coming to you soon including the Long-Range Financial Forecast, FY 2026 Mid-Year budget actions and the proposed FY 2027 budget.

Achieving structural balance requires a combination of options. A key challenge is distinguishing between one-time tools (i.e. BSR) that tackle the immediate FY 2027 problem, and ongoing solutions (i.e. revenues, cost reductions, and pension option 1 “ADC”) that address the structural imbalance over the next five years. An approximate balance of one-time and ongoing strategies is essential. A brief summary of each option follows the table.

Revised Table 3: FY 2027 Budget Balancing "Sandbox" Options
(All figures in millions. Projected FY 2027 Deficit: \$14.9M)

Option Category	Item	Strategy	Potential FY 2027 Impact
Revenue Enhancement (Ongoing)	Additional Revenue	Increase fees and/or other revenues	\$0.8
One-Time Funding	BSR Contribution	Utilize funds available above the 18.5% target	\$2.0
Ongoing Expenditure Reduction	General Fund Reductions	Target for permanent budget base reductions (ongoing)	\$7.0
Ongoing Expenditure Reduction	Reduction in Capital Contribution	Reduce General Fund Base Transfer to Capital Improvement Fund (CIF)	\$1.0
Long-term Cost & Liability Reductions	Pension Option 1 - NC/UAL	Reduce required payment to ADC level (for five years)	\$3.6
Long-Term Cost & Liability Reductions	Pension Option 2 - ADP	Reduce Additional Discretionary Payment (ADP) to Trust	\$0.5
Subtotal (Potential Solutions)			\$14.9
Remaining		<i>(Against \$14.9M Deficit)</i>	\$0

Revenue enhancement – (\$800,000) – explore new or updated fees and other revenues.

Ongoing expenditure reductions (\$8.0 million) - further reduce the General Fund operating budget and capital investments for the next five years, while exploring service efficiencies and aiming to minimize service impact to the community.

Long-term cost & liability reductions (\$4.1 million) – continue to implement the Retiree Benefit Funding Policy and make transfers from Section 115 pension trust to CalPERS to reduce employer costs (ADC) and unfunded liability (ADP). Funding the ADC over the next 5 years and ADP on-going will reduce the budget operating and capital cuts necessary to balance the budget. As reviewed with the Committee on November 18, the Section 115 pension trust funding transfers scenarios were financially analyzed, consistent with the City policy and the projected outcomes would achieve the City policy key objectives. This balances the City’s financial position, policy objectives and desirable service level of the community.

Budget Stabilization Reserve (BSR)

The City's Budget Stabilization Reserve (BSR) serves as the primary General Fund reserve. By policy, the BSR is maintained in the range of 15% to 20% of General Fund operating expenditures, with a target of 18.5%. Any reduction to the reserve below 15% requires City Council approval. At the discretion of the City Manager, any BSR balance above 18.5% may be transferred to the

Infrastructure Reserve (IR) in the Capital Improvement Fund and the City's Section 115 Pension Trust Fund, as outlined in the Retiree Benefit Policy. The BSR is used to fund unanticipated one-time costs as opposed to ongoing or recurring operating expenditures; the City's intent is to fund ongoing programs and services with ongoing dollars. Maintaining the BSR at or above the 18.5% target provides financial flexibility and has been a strong factor in the City maintaining a AAA credit rating.

The current BSR balance is projected to be above the 18.5% target for FY 2026. However, the projected \$14.9 million deficit in FY 2027 means that the BSR could be drawn upon or funds currently above the target could be allocated to bridge the gap. Utilizing a portion of the BSR (or transfers from above-target BSR funds) is presented as a potential one-time tool to solve the immediate operating deficit. Staff's approach prioritizes maintaining the target 18.5% BSR level for long-term fiscal stability, but the structural deficit requires consideration of all available strategic resources and as such, only \$6 million of the \$9 million projected FY 2026 incremental deficit is illustrated in this summary.

Table 4: Budget Stabilization Reserve (BSR) Summary (in millions)	
Budgeted FY 2025 Ending BSR	\$54.00
FY 2025 BSR Surplus Compared to Budget	\$4.9
Actual FY 2025 Ending BSR	\$58.9
Additional BSR (Included in FY 2026 Adopted Budget)	\$0.2
Use of BSR for FY 2026 Budget Amendments (BAOs)	-\$0.3
FY 2026 BSR Adjusted Balance	\$58.8
FY 2026 BSR 18.5% Target Level	\$56.8
Estimated Available BSR Above 18.5% Level	\$2.0
BSR Policy Analysis (PROJECTIONS):	
Table 4: Budget Stabilization Reserve (BSR) Summary (in millions)	
Recommend Roll Uncertainty Reserve/FY25 Surplus into BSR	\$6.0
BSR, FY 2026 Projected Ending Balance (before revenue decline)	\$64.8
Projected FY 2026 BSR Target Level	21.1%
Projected BSR Above FY 2026 18.5% Target	\$8.0
Projected Use of BSR:	
FY 2026 projected revenue decline (partial offset with BSR, while contingency one-time redistribution of sales tax may be funded by other resources, including Section 115 trust)	-\$6.0
FY 2026 Projected BSR, ending (minus revenue declines)	\$58.8
FY 2027 Projected BSR, use	-\$2.0
FY 2027 Projected BSR, ending	\$56.8
BSR as % of projected FY 2027 expenditures	18.5%

Revenue Assumptions

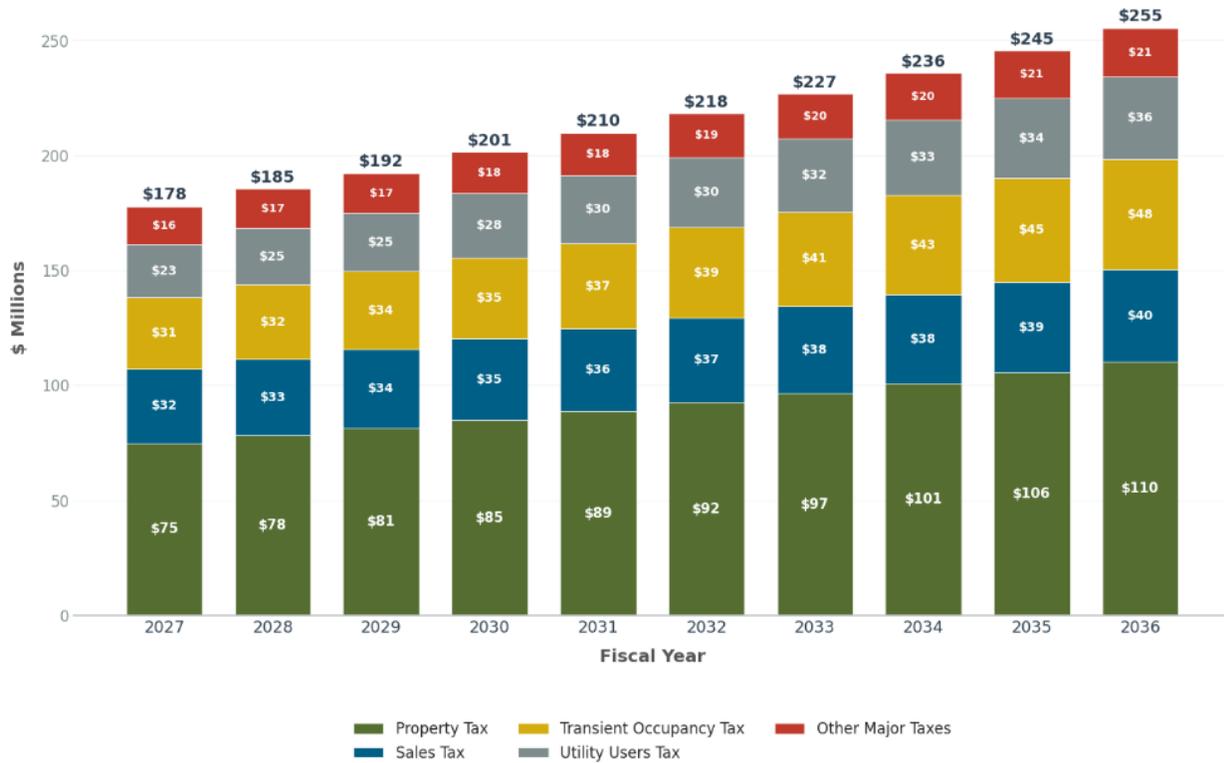
The FY 2025 Annual Comprehensive Financial Report (ACFR), scheduled for review by the Finance Committee, will report General Fund revenues as compared to the prior year. Major tax revenues have shown mixed results through the first quarter of FY 2026, indicating current fiscal volatility. Total General Fund revenues are projected to be \$305.1 million in FY 2027. As noted in the variance analysis provided to the Committee, this is approximately \$5.8 million lower than the forecast presented during the FY 2026 budget process. This significant downward revision is the primary driver of the structural deficit, highlighting the immediate need for budget balancing strategies. The change is largely attributable to a \$5.0 million reduction in the Sales Tax forecast, reflecting the steep decline in new auto sales and leasing sectors, with more detail in Attachment B. Property Tax was also revised down by \$1.5 million, to reflect the 10-year compound annual growth rate (CAGR) is projected at approximately 4.5%, which is a moderation from historical trends. Staff will continue to monitor revenues and provide an update during the FY 2026 Mid-Year Budget Review. A summary of key revenue assumptions are below; extensive information regarding each revenue category can be found in Attachment C.

Revised Table 5: General Fund Revenue Forecast (Base Case)

(All figures in millions)

Revenue & Other Sources	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
Sales Taxes	\$32.3	\$33.3	\$34.3	\$35.3	\$36.1	\$37.0	\$37.8	\$38.5	\$39.3	\$40.1
Property Taxes	\$74.9	\$78.1	\$81.4	\$84.9	\$88.6	\$92.5	\$96.6	\$100.9	\$105.5	\$110.3
Transient Occupancy Tax	\$31.0	\$32.3	\$33.8	\$35.4	\$37.1	\$39.1	\$41.1	\$43.3	\$45.5	\$47.9
Documentary Transfer Tax	\$9.0	\$9.3	\$9.5	\$9.8	\$10.2	\$10.5	\$10.9	\$11.3	\$11.7	\$12.1
Utility Users Tax	\$23.0	\$24.7	\$25.4	\$27.9	\$29.5	\$30.5	\$31.7	\$32.9	\$34.4	\$35.8
Business Tax	\$6.7	\$6.8	\$7.0	\$7.2	\$7.4	\$7.6	\$7.8	\$8.0	\$8.2	\$8.4
Other Taxes and Fines	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8
Subtotal: Taxes	\$177.7	\$185.3	\$192.2	\$201.3	\$209.7	\$218.0	\$226.7	\$235.7	\$245.4	\$255.4
Charges for Services	\$45.1	\$46.2	\$46.9	\$47.7	\$48.3	\$48.7	\$49.0	\$49.3	\$49.6	\$49.9
Permits and Licenses	\$11.8	\$12.0	\$12.1	\$12.3	\$12.5	\$12.7	\$12.7	\$12.8	\$13.0	\$13.1
Return on Investments	\$3.7	\$3.8	\$3.9	\$4.1	\$4.2	\$4.4	\$4.6	\$4.8	\$5.0	\$5.2
Rental Income	\$17.0	\$17.5	\$18.1	\$18.8	\$19.4	\$20.1	\$20.8	\$21.5	\$22.3	\$23.1
From Other Agencies	\$1.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1
Charges to Other Funds	\$15.8	\$16.2	\$16.7	\$17.0	\$17.4	\$17.5	\$17.8	\$17.9	\$18.0	\$18.0
Other Revenue	\$2.5	\$2.6	\$2.6	\$2.6	\$2.6	\$2.6	\$2.7	\$2.7	\$2.7	\$1.9
Subtotal: Non-Tax	\$97.0	\$98.3	\$100.5	\$102.6	\$104.5	\$106.1	\$107.7	\$109.1	\$110.6	\$111.3
Operating Transfers-In	\$30.4	\$33.2	\$34.6	\$36.7	\$38.8	\$41.2	\$44.1	\$45.7	\$48.6	\$51.4
TOTAL REVENUE	\$305.1	\$316.9	\$327.2	\$340.4	\$353.0	\$365.2	\$378.4	\$390.3	\$404.6	\$418.8

Graph 1: Major General Fund Revenues (\$ million)



Sales Tax: The FY 2026 Adopted Budget for Sales Tax was \$36.4 million. The new FY 2027 forecast is \$32.3 million. This represents a \$4.1 million (11.3%) decrease from the prior year's adopted budget and a significant \$5.1 million downward revision from the FY 2027 forecast included in the FY 2026 Adopted Budget. This structural reduction is the single largest driver of the projected deficit, as was discussed with the Committee on November 18, 2025.

This revision is based on current receipts and outlook for business-to-business sales (leasing) and new auto sales, reflecting local economic drivers. The "soft-landing" of the national economy has not fully translated to the Bay Area, which is projected to lag the U.S. recovery (Attachment B). The forecast assumes modest 2-3% growth in the out-years. Staff continues to monitor this critical revenue source.

Property Tax: Property tax revenue is the General Fund's largest revenue source, projected at \$74.9 million for FY 2027. This is a modest 1.8% increase over the FY 2026 Adopted Budget of \$73.6 million and a \$1.5 million reduction from the forecast included in the FY 2026 Adopted Budget. While the FY 2027 growth rate appears low at 1.8% due to technical re-baselining of FY 2026 actuals, the underlying assessed value growth assumption remains at approximately 4.4% to 4.8%. This reduction reflects a cooling in the real estate market and lower-than-anticipated assessed valuation (AV) growth. The 10-year compound annual growth rate (CAGR) is projected at approximately 4.5%, which is a moderation from historical trends.

This category also includes receipts for excess Educational Revenue Augmentation Fund (ERAF) distributions from the County of Santa Clara. ERAF is the fund used to collect and disburse

property taxes that are shifted to/from cities, the County, and special districts prior to their reallocation to K-14 school agencies. When the state shifts more local property tax than required to support schools, these funds are returned and known as excess ERAF. Staff continues to monitor potential legislative and legal challenges to the ERAF calculation and reserves funding in accordance with County guidance.

Utility Users Tax (UUT): The UUT is levied on electric, gas, and water consumption, as well as on telephone usage. Revenue in this category is projected at \$23.0 million for FY 2027, a 7.5% increase over the FY 2026 Adopted Budget. This is based on updated financial plans from the Utilities department, reflecting anticipated consumption and approved rate adjustments. Revenue in this category is expected to show steady growth over the forecast period, aligned with the Utilities' long-range financial plans.

Charges for Services and Permits and Licenses: Revenues in the Charges for Services and the Permits and Licenses categories are anticipated to be \$45.1 million and \$11.8 million, respectively, in FY 2027. Together, these amounts total \$56.9 million. These revenue sources are primarily driven by the cost of staff to provide services to the community. To ensure alignment with target cost recovery levels, the City has engaged a consulting firm to assist with a comprehensive cost allocation plan and municipal fee study during FY 2026, with implementation anticipated in FY 2027. Staff will evaluate and bring forward recommendations to align fees with target cost recovery levels to cover general salary and benefits increases and CPI trends. One exception to this is Development Services activities and related revenue. Development Services fees are intended to be fully cost-recoverable, and the department has been modeled as cost-neutral in this forecast. To the extent Council wishes to provide subsidies to development service permit fees to encourage activities such as electrification to reach sustainability goals, these subsidies would add to the forecasted General Fund deficit unless an alternative funding source is identified.

Expense Assumptions

As part of developing the FY 2027-2036 Forecast expenditure budget, the General Fund expense categories have been adjusted by removing one-time expenses from the prior year and updating major cost elements such as salary and benefits. Total General Fund expenditures are projected to be \$320.0 million in FY 2027. This represents a moderate 4.3% increase from the FY 2026 Adopted Budget of \$306.9 million. The overall annual growth is due mainly to increases in Salary and Benefits, Contractual Services, and Allocated Charges. A summary of expense assumptions is discussed here; extensive information regarding each expense category can be found in **Attachment D**.

Table 6: General Fund Expense Forecast
All figures in millions

Expenditures & Other Uses	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
Salary & Benefits	\$198.9	\$203.6	\$209.9	\$216.2	\$220.1	\$223.7	\$225.5	\$228.7	\$230.2	\$232.3
Contract Services	\$32.1	\$33.1	\$35.2	\$36.6	\$38.0	\$39.6	\$41.1	\$42.8	\$44.5	\$46.3
Supplies & Material	\$4.0	\$4.1	\$4.2	\$4.3	\$4.5	\$4.7	\$4.9	\$5.1	\$5.3	\$5.5
General Expense	\$10.5	\$10.8	\$11.1	\$11.5	\$11.9	\$12.3	\$12.7	\$13.1	\$13.6	\$14.6
Rents & Leases	\$1.5	\$1.6	\$1.7	\$1.7	\$1.8	\$1.8	\$1.8	\$1.9	\$1.9	\$0.2
Facilities & Equipment	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7
Allocated Charges	\$32.4	\$33.7	\$35.2	\$36.7	\$38.2	\$38.8	\$38.9	\$40.0	\$41.4	\$50.0
Subtotal: Non S&B	\$81.2	\$84.0	\$88.1	\$91.5	\$95.1	\$97.9	\$100.1	\$103.6	\$107.4	\$117.3
Operating Transfers-Out	\$6.3	\$6.3	\$6.4	\$6.4	\$6.7	\$6.6	\$6.8	\$7.0	\$7.2	\$5.6
Transfer to Infrastructure	\$33.6	\$35.8	\$38.1	\$40.5	\$41.8	\$43.4	\$45.0	\$46.7	\$48.5	\$50.4
TOTAL EXPENDITURES	\$320.0	\$329.7	\$342.5	\$354.6	\$363.7	\$371.6	\$377.4	\$386.0	\$393.3	\$405.6

Salary and Benefits: Consistent with prior years, the FY 2027 salaries and benefits costs represent approximately 62% of the General Fund budget expenditures. Salary and Benefits are projected to increase \$8.2 million or 4.3% from the prior year, from \$190.7 million (FY 2026 Adopted) to \$198.9 million (FY 2027 Forecast). Discussed in the following sections, this is primarily attributable to contractual increases in salaries, retiree healthcare costs, and pension costs.

- *Salary* costs are updated in accordance with Memorandum of Agreements (MOA's) between the City and its labor groups for contracts in effect. Then, a general wage adjustment of 2% is included for all employees starting in either January 2025 or July 2025 for all years of the forecast since no MOA's would be in effect at that time. A staff vacancy assumption of 5% is assumed, which is an increase from 3% assumption most recently a few years ago, creating a tighter budget forecast as the City continues to improve its actual vacancy rate through successful recruitment and retention programs.

- *Pension* are budgeted based on CalPERS determined rates as of the June 30, 2024, valuation for the City's miscellaneous and safety plans and additional contributions to Section 115 trust. In the General Fund, it is anticipated the City will spend a total of \$62.5 million on total pension costs in FY 2027, which includes \$53.7 million for the primary CalPERS contribution and \$8.8 million in supplemental Pension Trust (PARS) contributions. This total is approximately \$3.0 million higher than the prior year. These combined expenses represent approximately 19.5% of the General Fund's total expenses. This forecast does not reflect any strategies in the sandbox to transfer funds from Section 115 trust to CalPERS.

- *Retiree Healthcare/Other Post-Employment Benefits (OPEB)* - Retiree Medical is based on the June 30, 2024, actuarial study, which is completed every two years to inform the development of the FY 2027 and FY 2028 operating budgets. Consistent with City Council direction and the Retiree Benefit Funding Policy, this forecast continues the practice to budget the full payment of the Actuarial Determined Contribution (ADC) for retiree healthcare and the City Retiree Benefits Funding Policy prefunding to California Employers' Retiree Benefit Trust (CERBT) Fund.

Inflationary assumption in this long range is generally 3% annual inflation, with limited exception during the ten-year forecast to estimate cost increases for non-salary services and equipment.

Assumptions NOT Included in Forecast

It should be noted that the Base Case LRFF does not include several potential future impacts to the FY 2027-2036 General Fund outlook that are outlined in **Attachment E**. These items represent known priority projects or areas of planned investment that have not yet been fully developed in terms of costs, definitive funding sources, or finalized timelines. This is not intended to be a comprehensive list nor is it in any priority order.

FY 2027 Budget Development Guidelines

As discussed earlier in this document, this preliminary forecast represents the initial steps of the FY 2027 budget development process. Due to the clear overlap of projecting the City's fiscal condition and the need to shape service level expectations, the FY 2027 Budget Development Guidelines are incorporated into this discussion (**Attachment A**). These guidelines provide high-level budgetary direction to the entire organization.

Pairing the Budget Development Guidelines with the forecast at this time links the anticipated future fiscal condition of the organization with the necessary context regarding service delivery prioritization and resource allocation. This proactive linkage ensures that the City can address anticipated structural deficits, such as the \$14.9 million gap in FY 2027, using a comprehensive framework. The guidelines provide the financial mandate necessary to vet proposals against the structurally imbalanced General Fund, requiring staff to design budget solutions that not only solve the immediate deficit but also contribute to long-term alignment. This ensures that resource allocation is strategic, disciplined, and focused on maintaining financial sustainability rather than simply relying on one-time measures. The policy demands staff explore alternative revenue streams, optimize expenditures, and ensure all augmentations contribute positively to the overall structural balance.

Conclusion

This forecast maintains current service levels approved in FY 2026 but projects a structural deficit from FY 2027 through FY 2032. The primary driver of this imbalance is the \$14.9 million deficit in FY 2027, driven largely by downward revisions to Sales Tax projections. The Base Case assumes

a sluggish economic recovery, leading to continued revenue stagnation that is unable to keep pace with growth in expenditures. The Budget Balancing Sandbox offers a framework for the Committee to recommend ongoing solutions, such as \$8.0 million in structural General Fund reductions (operating and CIP) or adjustments to long-term liability payments, while leveraging one-time resources to bridge the immediate gap. Strategic planning and fiscal discipline are essential to maintain service levels and ensure long-term fiscal stability.

FISCAL/RESOURCE IMPACT

Financial implications from this report and input from the Finance Committee and City Council will be considered in the City Manager's development of the Fiscal Year 2027 budget.

STAKEHOLDER ENGAGEMENT

The preliminary forecast for FY 2027-2036 represents the beginning of the fiscal year 2027 budget development process. Information provided in this report will be discussed with the City Council after the Finance Committee reviews and provides recommendations. Those conversations will provide direction to staff in the budget development process. It is anticipated that conversations with City Council and the community will occur through public budget hearings in Spring 2026, according to the standard budget adoption process. The community can track previous and upcoming FY 2027 budget discussions and information at www.paloalto.gov/budget.

ENVIRONMENTAL REVIEW

This report is not a project for as defined by the California Environmental Quality Act because the review of the LRFF and budget policy guidelines are a fiscal activity which does not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment. CEQA Guidelines section 15378(b)(4)

ATTACHMENTS

Attachment A: FY 2027 Budget Policy Guidelines

Attachment B: The Economy

Attachment C: General Fund Base Case Revenue Assumptions

Attachment D: General Fund Base Case Expense Assumptions

Attachment E: Assumptions Not Included in Forecast

APPROVED BY: Lauren Lai, Administrative Services Director



FY 2027 Budget Development Guidelines

1. Structural Balance

Develop a structurally balanced budget that brings ongoing revenues and expenses into alignment. Develop a plan for any structural imbalance to ensure that the City maintains fiscal sustainability over the short, medium, and long-term.

2. One-Time Resources

Allocate one-time resources for one-time needs rather than committing one-time resources to ongoing services. Examine appropriate uses of revenue surpluses that exceed forecasted levels such as planning for recession needs, restoration needs, and strategic investments.

3. Council Priorities

Review resource allocation for the City Council's existing priorities and identify priority funding needs.

4. Process Redesign

Focus on business process redesign to enhance quality, flexibility, and cost-effectiveness of service delivery (include examining opportunities to streamline, simplify, reorganize, and reallocate resources to avoid duplication of effort).

5. Service Delivery Models

Explore alternative service delivery models (such as partnerships with non-profits or other public/private sector groups) to minimize overlap, maximize cost share, and effectively use resources.

6. Analyze Costs

Continue to thoroughly analyze non-personnel, equipment, other costs, such as contract services, for cost savings opportunities or realignment with current needs.

7. Revenue Expansion

Explore the expansion of existing revenue sources or the addition of new revenue sources, including the alignment of existing charges for services and the opportunity to establish new fees, when appropriate.

8. Augmentations

Continue to analyze and prioritize resource augmentations, seeking to offset augmentations with reductions elsewhere for net-zero impacts to the budget whenever possible; however, ensuring when resource augmentations are added, it is in alignment with one-time and ongoing forecasted sources.

9. Fund Long-Term Liabilities

Continue to prioritize proactively funding long term liabilities including but not limited to debt obligations, pension obligations, and capital infrastructure in accordance with City policies as approved by the City Council.

The Economy

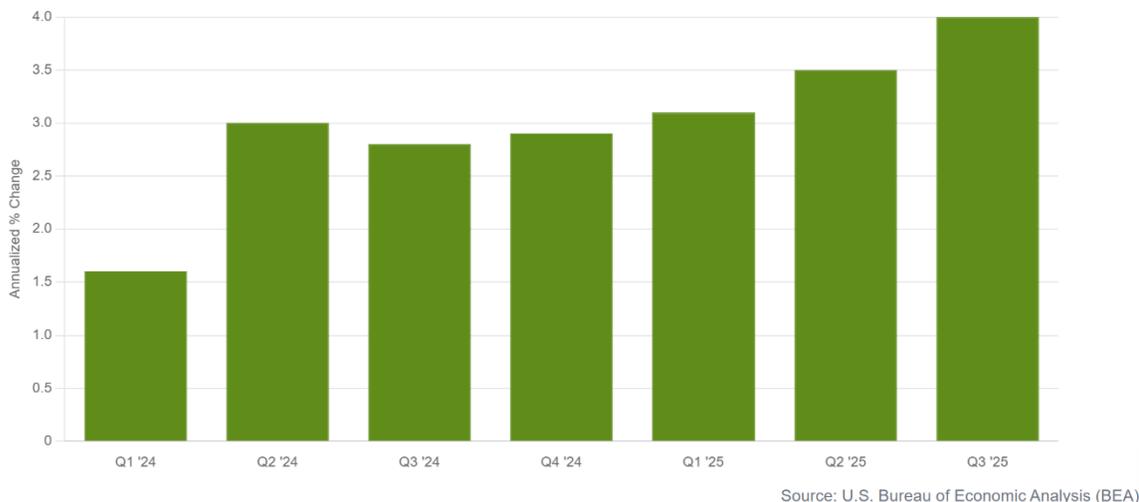
At the national level, economic growth has shown significant strength through the third quarter of calendar year 2025, led by robust GDP (gross domestic product) growth. Consumer spending has remained resilient despite inflation rates that have ticked up from the prior year. As of September 2025, the consumer price index (CPI), which measures changes in the prices paid by consumers for a basket of goods and services, was 3.0%. This is higher than the 2.6% CPI from a year ago. Assumptions in the LRFF report for general cost increases are using a CPI of 3% in FY 2026 and FY 2027 and 4% for FY2028 and beyond. The national unemployment rate, as of August 2025, is 4.3%, a modest increase from 4.1% in October of the prior year, suggesting a labor market that is cooling but not contracting. This slowdown is consistent with the Federal Reserve's monetary policy intended to curb inflation without initiating a recession. Key factors to monitor include future Federal Reserve policy, ongoing geopolitical events, and the impact of tariffs on inflation.

The local economy, in contrast, is projected to experience a more sluggish recovery. The latest Fall 2025 UCLA Anderson outlook states that while the U.S. economic recovery may begin in mid-2026, "the California recovery will begin later, getting underway late next year and accelerating in 2027." The forecast notes that a rebound in the technology and aerospace sectors will be necessary for California to resume its accustomed pace of growth. The risks to this forecast remain on the downside, tied to the performance of the tech sector, international trade, and the high cost of capital.

Table 1: National Gross Domestic Product (GDP)

National Gross Domestic Product (GDP)

Real GDP: Percent Change from Preceding Quarter



According to the U.S. Bureau of Economic Analysis (BEA), the US economy is estimated to have expanded at an annualized 4.0% in the third (calendar) quarter of 2025 (latest estimate), a significant acceleration from the growth seen in 2024. This robust growth was supported by a significant increase in personal spending, which increased at its fastest pace since 2023, boosted by consumption of both goods and services. Consumers showed strong spending on services related to travel, entertainment, and healthcare. Government consumption also rose,

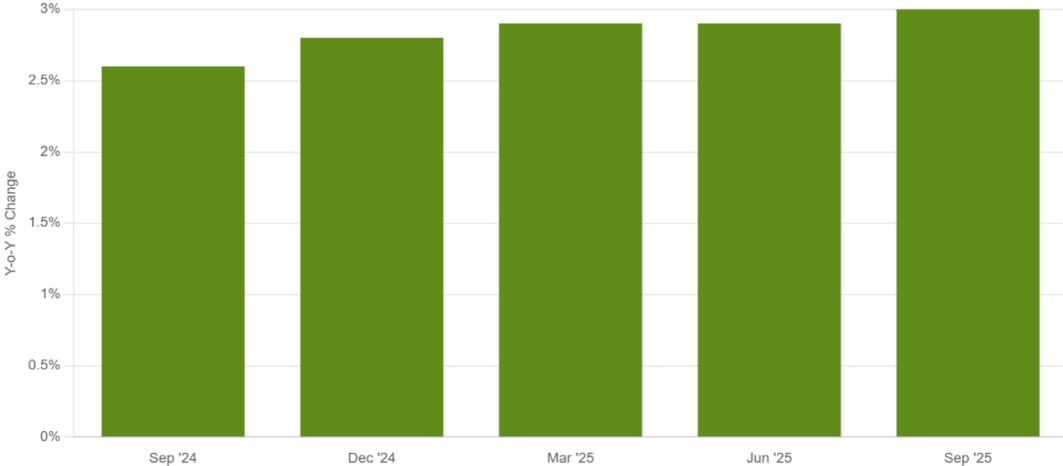
led by defense and state and local infrastructure spending. Business investment in equipment and intellectual property showed strength, offsetting a continued slowdown in fixed residential investment, which has struggled under higher interest rates. The contribution from net trade was positive, as exports of capital goods increased while imports held steady. This strong performance at the national level provides a crucial buffer against regional weaknesses and suggests underlying momentum in the economy.

The national inflation rate, as measured by the U.S. Bureau of Labor Statistics, rose to 3.0% (year-over-year) in September 2025, the highest rate since January 2025. This marks a continued upward trend from 2.9% in August. The increase was driven largely by a rise in energy prices, which rose 2.8% on the year, led by gasoline. Inflation for shelter, a major component of the index, also remained steady and elevated at 3.6%, continuing to pressure household budgets. On the other hand, a slowdown was seen in other areas, such as food (3.1%, down from 3.2% prior) and used cars and trucks (5.1%). On a monthly basis, the CPI increased 0.3%, which was below some market expectations. Core inflation (all items less food and energy), which is closely watched by the Federal Reserve, slowed slightly to 3.0% from 3.1% in the prior month, suggesting that underlying price pressures, while persistent, may be gradually easing.

Table 2: National Inflation Rate (CPI)

National Inflation Rate

National Inflation Rate (CPI): Year-Over-Year Percent Change



Source: U.S. Bureau of Labor Statistics (BLS)

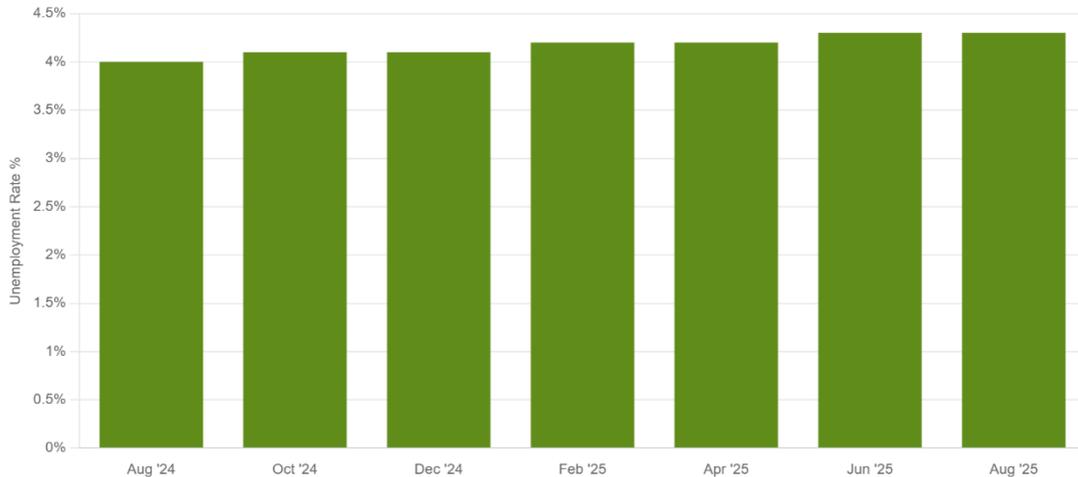
The nation's unemployment rate was 4.3% as of August 2025, with the number of unemployed persons at 7.4 million; these measures have changed little over the year. This rate, while low by historical standards, is slightly elevated from the beginning of the calendar year. Among those without employment, the number of long-term unemployed (those jobless for 27 weeks or more) was 1.9 million in August, accounting for 25.7% of all unemployed persons. In the meantime, the labor force participation rate held steady at 62.3%, which has declined by 0.4 percentage points over the year. Per the State of California's Employment Development Department (EDD), the state's unadjusted unemployment rate as of August 2025 is 5.8%, a notable increase from 5.3% in September of the prior year. The local region reflects this cooling trend. The unemployment rate for the San Jose-Sunnyvale-Santa Clara MSA was 4.7% in August 2025, with Santa Clara County at 4.6%. This is a measurable increase from the 4.1% county rate

seen a year prior, reflecting the sluggishness in the technology sector referenced by the UCLA forecast.

Table 3: U.S. Unemployment Rate

The Labor Market

U.S. Unemployment Rate: Monthly, Seasonally Adjusted



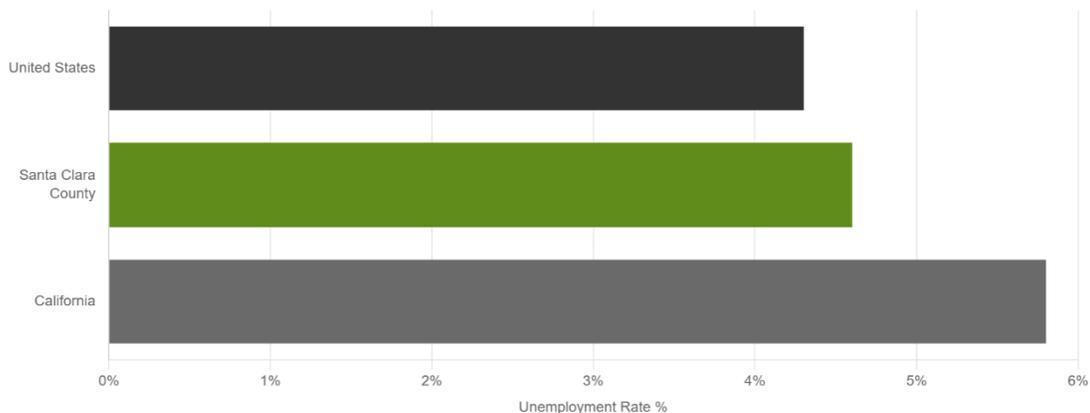
Source: U.S. Bureau of Labor Statistics (BLS)

The erosion of purchasing power from inflation remains a key watch item; however, consumer spending remains resilient. Personal consumption expenditures (PCE) are the primary measure of consumer spending on goods and services in the U.S. economy. It accounts for about two-thirds of domestic final spending, and thus it is one of the main factors that indicates future economic growth. Strength in PCE spending tends to prompt additional business spending. According to the U.S. Bureau of Economic Analysis (BEA), the headline PCE price index rose 2.7% year-over-year as of August 2025. A key component, the core PCE price index (which excludes food and energy), rose 2.9% year-over-year. This core measure is the Federal Reserve's preferred inflation gauge, and while it is an improvement from previous highs, its persistence well above the 2% target adds leeway for the Federal Reserve to hold interest rates at a restrictive level. This resilience in spending, particularly on services, continues to support economic growth but also poses a challenge to fully taming inflation.

Table 4: Unemployment Rate Comparison (August 2025)

Regional Unemployment

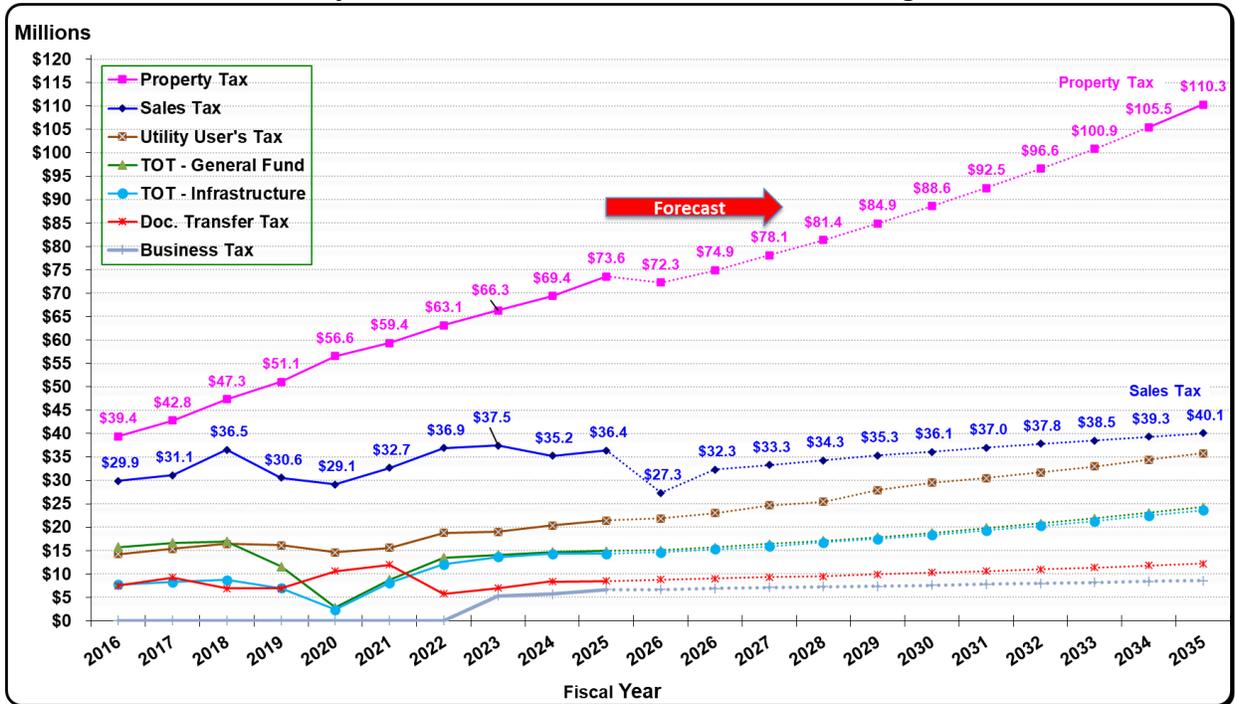
Unemployment Rate Comparison: Unadjusted Rates (August 2025)



Source: U.S. BLS, California EDD

General Fund Base Case Revenue Assumptions

Chart 1: General Fund Major Tax Revenue Actuals and Forecast through FY 2036



Property Tax

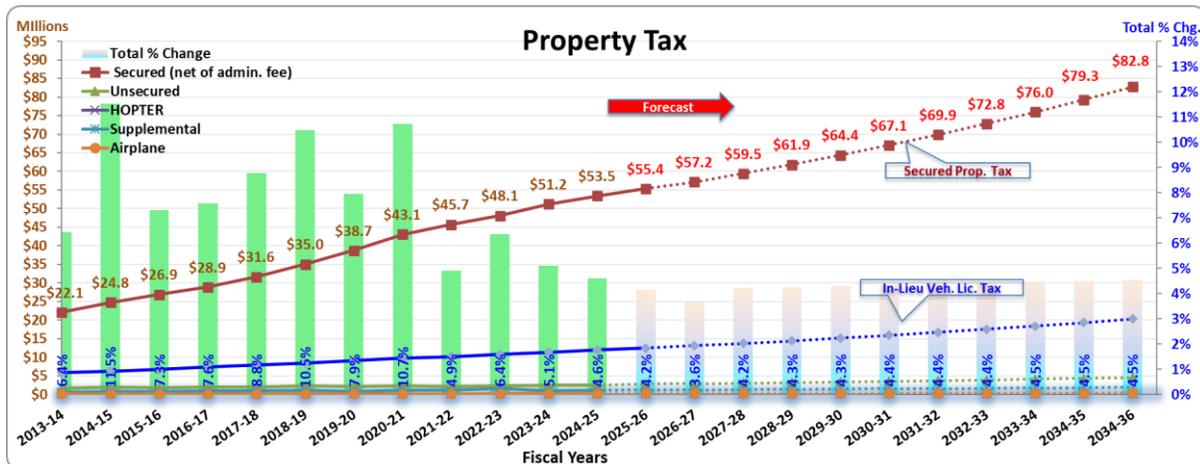
Property tax revenue is the General Fund’s largest revenue source and represents over 25% of the total General Fund revenues. Growth in this category has been steady over time, with the secured property tax 10-year compound annual growth rate (CAGR) ranging from a low of 5.8% in FY 2019 to a high of 7.25% in FY 2010, with the current 10-year CAGR of 6.9%. Although the City has realized a 10-year compound annual growth rate of 6.9% in property tax revenues, the FY 2027 forecast projects a moderated 1.8% growth rate, with revenues anticipated to increase from \$73.6 million in FY 2026 (adopted) to \$74.9 million in FY 2027 (projected). However, in FY 2026 it is likely that property taxes will be revised down to \$72.3 million which aligns with the County Tax roll for FY 2026. We therefore estimated a 4.8% increase from this revised FY 2026 property tax to project FY 2027, by using the actual assessed valuation growth from 2025.

Property tax performance typically lags economic conditions by about a year due to the assessment and collection timeline. This category also includes receipts for excess Educational Revenue Augmentation Fund (ERAF) distributions from the County of Santa Clara. ERAF is the fund used to collect and disburse property taxes that are shifted to/from cities, the County, and special districts prior to their reallocation to K-14 school agencies. When the state shifts more local property tax than required to support schools, these funds are returned and known as excess ERAF. As a result of the volatility of ERAF, it is not considered a permanent local revenue source even though it has performed strongly in the past decade.

ERAF Reserve: The City maintains an ERAF Reserve to address ongoing disputes related to the calculation of excess ERAF. Earlier challenges with the State and Santa Clara County, and with the State and California School Board Association, were resolved favorably, allowing the related reserves to be released. Currently, a State Controller’s Office audit finding against Marin County challenges the inclusion of former Redevelopment Agency funds in the excess ERAF calculation and remains under litigation. Approximately 18-22% of excess ERAF is considered at risk under this finding. Separately, there have been statewide discussions about extending ERAF eligibility to charter schools. Although no changes have been adopted at this time, this could introduce additional risk in the future.

To reflect this potential exposure, the City budgets excess ERAF on a net basis and reserves at-risk amounts when received. To date, a total of \$7.1 million has been set aside for prior-year at-risk amounts, with an additional contribution planned for FY 2026 once final amounts are known.

Chart 2: Property Tax Actuals and Forecast through FY 2036



Transfer of ownership is a significant driver of growth; however, that growth moderated in FY 2024 and is expected to continue in FY 2025 due to a higher interest rate environment and overall economic slowdown. Overall, median sales price of single family residential home increased 4.7%, where in the significantly low interest rate environment of 2021, the median price of a single family residential home increased by 18.26%.

The FY 2026 Adopted Budget for Property Tax is \$73.6 million, a \$5.0 million or 7.3% increase over the FY 2025 adopted revenue of \$68.6 million. In FY 2027, this revenue is anticipated to increase to \$74.9 million, a \$1.3 million or 1.8% increase over the FY 2026 Adopted Budget amount. The Base Case assumes approximately 2.0% to 4.5% growth over the length of the forecast.

Sales Tax

Sales Tax is the City’s second largest General Fund revenue source and represents approximately 13.5% of the total revenues. This revenue category continues to evolve based on

changes in consumer activity, including the growing influence of online purchasing and the modernization of retail operations. In the near term, these dynamics have been coupled with declines in the business-to-business (including car leases) and transportation sectors, consistent with trends in recent financial reporting and sales tax digests. These conditions, along with CDTFA adjustments and changes in the state’s allocation methodology, have resulted in lower receipts.

As a result, FY 2026 revenue is expected to fall by up to \$9.0 million below the adopted budget, decreasing from \$36.4 million to a projected \$27.3 million, due to a combination of potential one-time adjustments by the California Department of Tax and Fee Administration (CDTFA) and lower allocations to the City. The LRFF base case incorporates this lower starting point, with FY 2027 sales tax projected at \$32.3 million, roughly 11% below prior expectations due to an ongoing annual reduction of about \$5.1 million. In the out-years, sales tax is assumed to stabilize at this reduced level, with modest growth beginning in FY 2028 and returning to current budget levels by FY 2032.

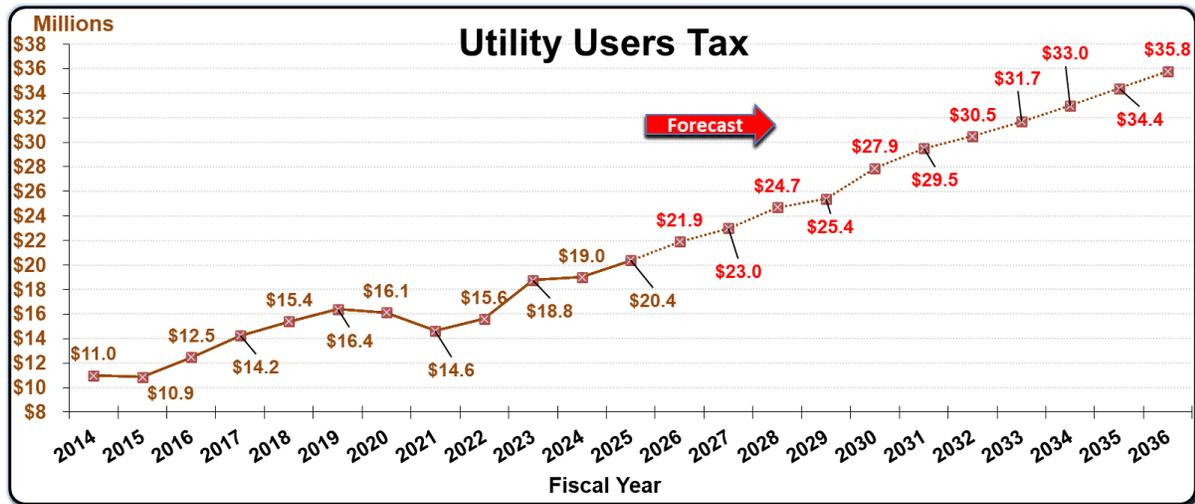
Chart 3: Sales Tax Actuals and Forecast through FY 2036



Utility User’s Tax (UUT)

The UUT is levied on electric, gas, and water consumption, as well as on telephone usage. Revenue in this category is impacted by consumption levels and has experienced reductions in prior periods due to water conservation programs and reduced workforces and business closures during the pandemic. This revenue has recovered as the local economy recovered and workers returned to the office in FY 2023. In addition, higher utility commodity costs and capital costs resulted in sizable utility rate increases and higher UUT revenues. The FY 2026 Adopted Budget for UUT is \$21.4 million, \$1.0 million or 5.1% higher than the FY 2025 actuals of \$20.4 million. In FY 2027, this revenue is anticipated to increase to \$23.0 million, a \$1.6 million or 7.5% increase over the FY 2026 budgeted amount. Revenue in this category is expected to grow between 3% to 10% over the length of the forecast, or a 10-year CAGR of 5.0%.

Chart 4: Utility Users Tax Actuals and Forecast through FY 2036



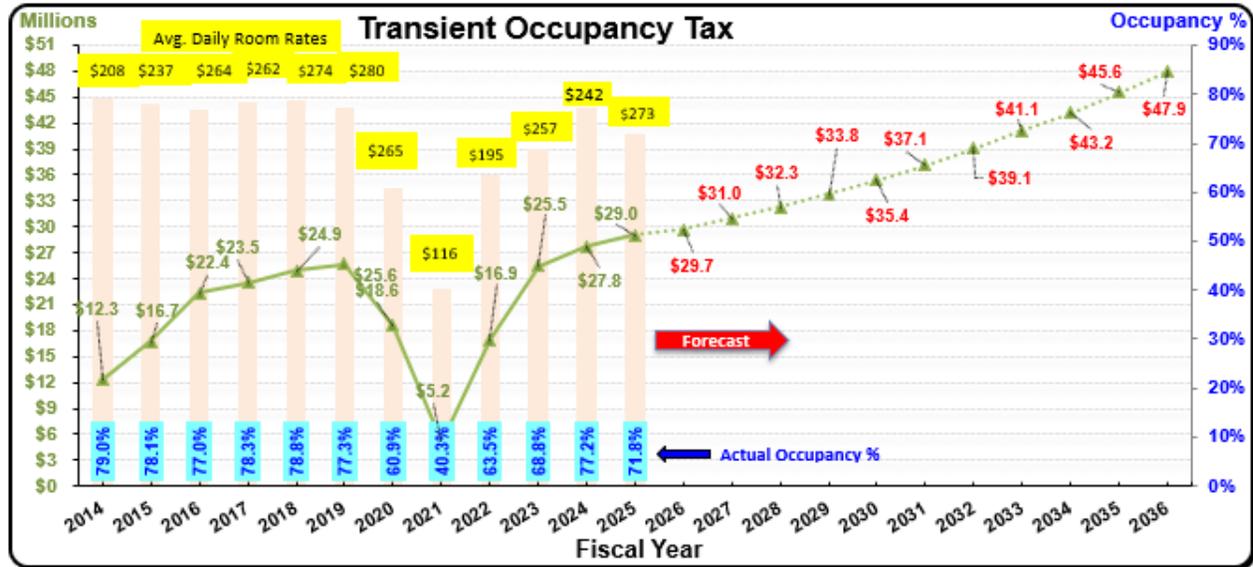
Transient Occupancy Tax (TOT)

The City’s TOT is applied at a rate of 15.5% on hotel and other short-term lodging stays and is impacted by business and other leisure travel activity. Consistent with policy, a portion of TOT receipts from new hotel developments is allocated to support infrastructure needs. In recent years, this has resulted in an overall distribution that is roughly split between the General Fund and Capital Improvement Fund. TOT revenues were significantly affected in FY 2020 and FY 2021 during the pandemic and have since stabilized as hotel activity recovered and new hotels added capacity.

The FY 2026 Adopted Budget for TOT revenue is \$29.1 million, a \$0.2 million or 0.6% increase over FY 2025 actuals of \$28.9 million. In FY 2027, this revenue is anticipated to increase to \$31.0 million. Of this amount, approximately \$16.7 million is allocated for general fund purposes and \$14.3 million is used to support capital infrastructure projects. This aligns with Council policy to direct a portion of TOT toward infrastructure investments.

During the first two months of the fiscal year, hotels reported an average daily room rate of \$225.86 and an occupancy rate of 82.3%, compared to \$238.76 and 70.2% in the same period in the prior fiscal year. TOT receipts have grown at a CAGR of 9.3% over the past five years and 5.7% over the past ten years, reflecting a rebound from pandemic lows and overall sustained recovery in the local hotel market. This LRFF assumes growth rates ranging from 1.3% to 5.3% over the forecast period.

Chart 4: Transient Occupancy Tax Actuals and Forecast through FY 2036



Note: January 2015, TOT Rate went from 12% to 14% April 2019, TOT Rate went from 14% to 15.5%

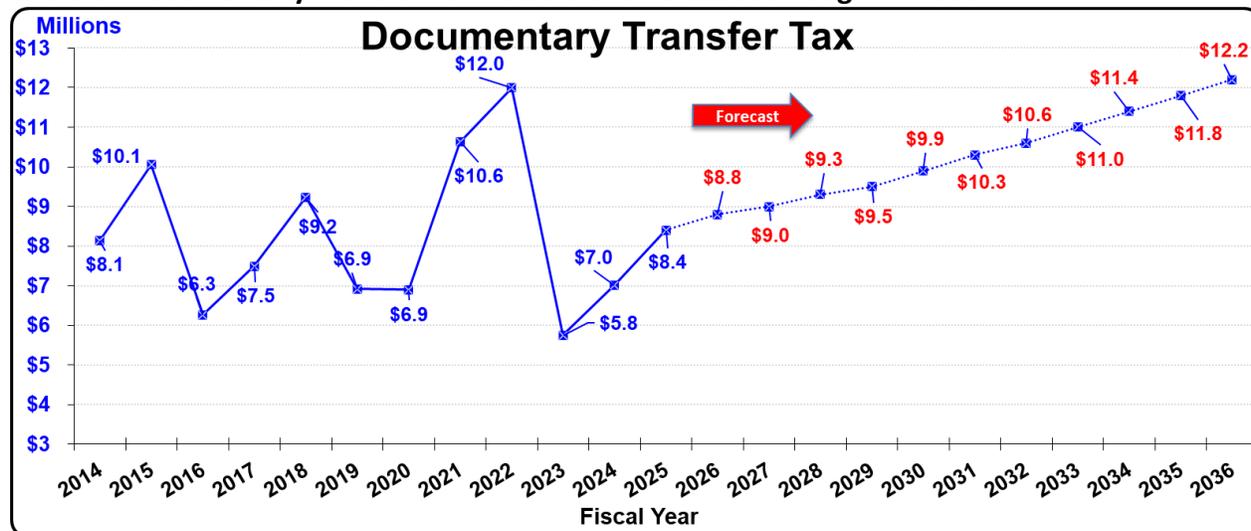
Documentary Transfer Tax (DTT)

Revenue in this category is highly volatile and depends on sales volume and the mix of commercial and residential sales. Activity can vary significantly year to year, making this a challenging category to forecast. Over the past 10 years, DTT receipts have averaged approximately \$8.0 million annually, with occasional spikes driven by large commercial transactions. FY 2021 and FY 2022 generated a record revenue of \$10.6 million and \$12.0 million due to several high-value commercial transactions, while lower activity contributed to a decline in receipts in FY 2023.

The FY 2026 Adopted Budget for DTT is \$8.5 million, a \$1.2 million or 16.4% increase from the FY 2025 adopted revenue of \$7.3 million. FY 2027 is forecast at \$9.0 million, with growth ranging from approximately 2.0% to 3.5% over the period.

The number of transactions through October 2025 (75) is 18.0% higher than the same period in the prior year, with the total revenue from these transactions increasing by 22.6%. Data from the first six months of the calendar year indicates that single family residential homes are selling for 1.5% less than in the previous calendar year, with number of sales being relatively flat. The median price for single family properties is \$3.3 million.

Chart 6: Documentary Transfer Tax Actuals and Forecast through FY 2036



Business Tax (BT)

In November 2022, voters approved Measure K (Business Tax) to provide additional funding for critical public safety needs, transportation safety improvements and grade separations, and affordable housing and unhoused services. The tax applies to non-exempt businesses above 10,000 square feet with an annual single business cap of \$500,000. The initial collection was based on a BT rate of 3.75 cents per square foot which increased to 7.5 per square foot starting on January 1, 2025. FY 2026 is the first fiscal year in which the full rate will be assessed. Both the rate and the cap will be increased annually by 2.5% beginning in FY 2027.

The FY 2026 Adopted Budget for BT is \$6.5 million, a \$1.0 million or 18.4% increase over the FY 2025 actuals of \$5.7 million. This increase reflects the first full fiscal year at the fully phased-in rate and continued registration activity from non-exempt businesses. In FY 2027, this revenue is projected to increase to \$6.7 million, supported by steady participation and the scheduled annual rate increase.

The BT program is still in its early stages and will continue to evolve as participation stabilizes and year-over-year data becomes more consistent. Staff will continue to monitor performance and will provide updated analysis and recommendations in future financial updates as more data becomes available.

Return on Investment

Investment income reflects interest earned on the City’s investment portfolio and liquid balances. In FY 2026, the City transitioned from managing its investment portfolio in-house to partnering with Chandler Asset Management for professional investment management services. The City’s current earnings reflect a combination of legacy holdings and new investments purchased under the revised portfolio strategy. As of the first quarter of FY 2026, the portfolio’s market yield was 4.01%.

Investment income is projected to generate approximately \$3.6 million in FY 2026 and increase

gradually to about \$5.2 million by FY 2036. The forecast assumes annual growth of roughly 2.0% to 4.0% over the forecast period, reflecting expected reinvestment of maturing securities and current market conditions. Staff continues to work with Chandler on developing forecasts that reflect the new strategy and expects to incorporate more refined projections in future financial updates.

Rental Income

Rental Income of \$16.4 million in FY 2026 primarily reflects rent paid to the General Fund from the City's Enterprise Funds and tenants at the Cubberley Community Center. Rental income is projected to remain flat compared to the FY 2025 Adopted Budget. This revenue category will be further reviewed and revised subsequent to this forecast, typically based on the December-to-December California Consumer Price Index (CCPI) in the San Francisco Bay Area.

Charges for Services and Permits and Licenses

Revenues in the Charges for Services and the Permits and Licenses categories are anticipated to be \$43.6 million and \$11.4 million, respectively, in FY 2026. Together, these amounts total \$55.0 million and are approximately \$5.7 million higher than the FY 2025 Adopted Budget of \$49.3 million. Increases in these categories are primarily due to revenue adjustments for the agreement with Stanford to provide Fire and Dispatch services, and higher forecasts for permit and plan review services processed through the Development Center.

The revenue estimates in these categories are based on current activity levels, and these revenue sources are primarily driven by the cost of staff to provide services to the community. To ensure alignment with target cost recovery levels, the City has engaged a consulting firm to assist with comprehensive cost allocation plan and municipal fee study during FY 2025, with implementation anticipated in FY 2026. Staff will evaluate and bring forward recommendations to align fees with target cost recovery levels to cover general salary and benefits increases and CPI trends. These efforts aim to improve fee transparency and ensure equitable cost distribution across City services. One exception to this is Development Services activities and related revenue. Development Services fees are fully cost-recoverable, and the department has been modeled as cost-neutral in this forecast.

Charges for Service – Stanford Fire and Dispatch Services

The City and Stanford have two separate agreements for the provision of fire response and emergency dispatch services. The fire response services agreement became effective in July 2018 and outlines service level terms and a new cost allocation methodology as the baseline for agreement costs. The term extended through June 2023, with annual renewals in effect through June 2028 unless otherwise terminated. The agreement includes a staffing deployment model for suppression and medical services, which was approved by The City Council in October 2017 and deployed in January 2018. This forecast aligns with the new staffing model; and, in accordance with the agreement, adjustments to revenue from Stanford have been aligned with the year-over-year changes to the operating expenses in the Fire Department over the forecast period. Similarly, changes to the revenue received for dispatching services have been aligned with the operating expenses in the Technical Services Division of the Police Department where the costs to provide these services are budgeted. The agreements for both fire and dispatch

services have termination dates that fall within the forecast period, and while the revenue forecast assumes continuation of the current agreement terms, new contracts will need to be executed. For fire and police revenue, additional adjustments may be applicable if new labor agreements are negotiated for the forecast period. Revenues for these services are based on current anticipated changes in salary and benefits costs within the Fire Department and Police Department Dispatch Unit.

Charges to Other Funds

The FY 2026 estimate for Charges to Other Funds of \$15.5 million remains flat compared to the FY 2025 budgeted amount. To ensure alignment with target cost recovery levels, the City has engaged a consulting firm to assist with a comprehensive cost allocation plan and municipal fee study in FY 2025, with targeted implementation in FY 2026. Staff will evaluate and bring forward cost allocation recommendations.

Operating Transfers-In

Overall, the Operating Transfers-in are estimated to be \$31.5 million for FY 2026. While this matches the total for FY 2025, the prior year included a one-time \$2.0 million transfer from the General Benefits Fund. This transfer was a refund of allocated charges paid by General Fund departments into the General Benefits Fund in prior years, which had accumulated in fund balance. Additionally, the Electric Fund equity transfer increased from \$15.1 million to \$18.3 million, while the Gas Fund equity transfer decreased from \$10.9 million to \$9.7 million, reflecting updated revenue forecasts for each fund.

In accordance with the methodology approved by the City Council in June 2009, the Electric Fund's equity transfer to the General Fund equity transfer has been calculated by applying a rate of return on the capital asset base of the Electric Fund. This rate of return is based on PG&E's rate of return on equity as approved by the California Public Utilities Commission (CPUC). The Gas Fund's equity transfer calculation was updated based on the passage of Measure L on the November 2022 ballot. As outlined in the ballot measure language, the Gas Fund equity transfer can be up to 18% of annual gross gas retail revenue. This LRFF increases the transfer to 18% in FY 2026, where it is projected to remain through 2036.

Other Revenue and Revenue from Other Agencies

Revenues in these two categories is projected at \$3.6 million in FY 2027, \$0.9 million lower than the FY 2025 adopted budget of \$4.5 million. These two revenue categories mainly account for grants or reimbursements from the federal and state governments or other local jurisdictions. Other Revenue decreased slightly by \$0.2 million in FY 2026 as a result of limited time funding in FY 2025 from LifeMoves, for reimbursement related to the Homekey Facility. Revenue from Other Agencies decreases by \$0.7 million in FY 2026, because FY 2025 is the last year of the Staffing for Adequate Fire and Emergency Response (SAFER) grant funding awarded to the City in FY 2022.

Table 1: General Fund Revenue Forecast (Year-to-Year Percentage Change)

Revenue & Other Sources	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
Sales Taxes	-11.3%	3.1%	3.0%	2.9%	2.3%	2.5%	2.2%	1.9%	2.1%	2.0%
Property Taxes	1.8%	4.3%	4.2%	4.3%	4.4%	4.4%	4.4%	4.5%	4.6%	4.5%
Transient Occupancy Tax	6.5%	4.2%	4.6%	4.7%	4.8%	5.4%	5.1%	5.4%	5.1%	5.3%
Documentary Transfer Tax	7.5%	7.4%	2.8%	9.8%	5.7%	3.4%	3.9%	3.8%	4.6%	4.1%
Utility Users Tax	5.9%	3.3%	2.2%	3.2%	4.1%	2.9%	3.8%	3.7%	3.5%	3.4%
Business Tax	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Other Taxes and Fines	3.1%	1.5%	2.9%	2.9%	2.8%	2.7%	2.6%	2.6%	2.5%	2.4%
Subtotal: Taxes	0.2%	4.3%	3.7%	4.7%	4.2%	4.0%	4.0%	4.0%	4.1%	4.1%
Charges for Services	3.4%	2.7%	1.3%	1.7%	1.3%	0.8%	0.6%	0.6%	0.6%	0.6%
Permits and Licenses	3.5%	1.7%	0.8%	1.7%	1.6%	1.6%	0.0%	0.8%	1.6%	0.8%
Return on Investments	0.0%	2.7%	2.6%	2.6%	5.0%	4.8%	4.5%	4.3%	4.2%	4.0%
Rental Income	3.0%	2.9%	3.4%	3.9%	3.2%	3.6%	3.5%	3.4%	3.7%	3.6%
From Other Agencies*	1000%	-90.9%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Charges to Other Funds	1.9%	2.5%	3.1%	1.8%	2.4%	0.6%	1.7%	0.6%	0.6%	0.0%
Other Revenue	0.0%	0.0%	4.0%	-3.8%	4.0%	-3.8%	4.0%	-3.8%	4.0%	0.0%
Subtotal: Non-Tax	4.0%	1.4%	2.0%	2.0%	2.1%	1.4%	1.5%	1.2%	1.6%	1.3%
Operating Transfers-In	-3.5%	9.2%	4.2%	6.1%	5.7%	6.2%	7.0%	3.6%	6.3%	5.8%
TOTAL REVENUE	1.3%	3.9%	3.3%	4.0%	3.7%	3.5%	3.6%	3.1%	3.7%	3.5%

General Fund Base Case Expense Assumptions

Salary and Benefits

Consistent with prior years, the FY 2027 salaries and benefits costs represent approximately 62% of the General Fund budget expenditures. Salary and Benefits are projected to increase \$8.3 million or 4.4% from the prior year. Discussed in the following sections, this is primarily attributable to increases in salaries (\$4.9 million), retiree healthcare costs (\$12.7 million total cost), and pension costs (\$45.1 million total cost).

Salary - Consistent with the City's salary budget methodology for recent budgets, positions are budgeted at the actual rate of pay of employees including benefit selections as of Fall 2025. Then, by position, salary costs are updated in accordance with applicable Memorandum of Agreements (MOA's) between the City and its labor groups and the Management and Professional Personnel and Council Appointees Compensation Plan(s).

In FY 2025, the City Council engaged with labor groups to negotiate new agreements for wages, benefits, and other terms and conditions of employment. These agreements extend through December 2027 (SEIU) and June 2028 (all other labor groups) for full-time staffing and include target market adjustments to align salaries with benchmark studies, Cost of Living Adjustments (COLAs), and other benefits such as a flexible compensation benefit.

The forecast assumes step increases for employees in applicable positions, including Service Employees International Union (SEIU), International Association of Fire Fighters (IAFF), and Palo Alto Peace Officers' Association (PAPOA), and merit increases for Management and Professional employees including Utilities Management & Professional Association of Palo Alto (UMPAPA). A general wage adjustment of 2% is included for all employees in the forecast when there is no MOA in effect. This is consistent with prior Council direction in previous LRFF reporting to use the 2% increase as a forecasting assumption, not as a commitment to future negotiations.

A reserve is included for potential changes to future labor costs including, changes in vacancy rates, labor and benefit rate variability, and inflation assumptions. Offering competitive compensation plans aligns with industry standards for attracting and retaining a skilled and motivated workforce and better positions the City of Palo Alto as an employer of choice. This level of funding is intended to offset potential future costs and may differ from actual outcomes. Negotiations for new labor agreements are anticipated to occur in FY 2028 for new terms beginning in FY 2028 and FY 2029.

Additionally, the budget includes vacancy savings that are expected to materialize as positions are vacated and new employees are hired through the normal course of business. As of the timing of this LRFF, the vacancy rate is approximately 11.6% (as of October 2025). Vacancy savings from public safety positions are typically exhausted by uses such as backfill, hire ahead programs, and overtime. Consistent with changes in the previous LRFF, this forecast assumes a General Fund vacancy rate of 5% in all years. This results in savings of approximately \$5.5 million in FY 2027 and increases annually over the forecast period in alignment with forecasted salary trends. Consistent with past practice, the vacancy assumption is lower than the actual vacancy rate to allow departmental

use of those savings for other staffing strategies, such as filling staffing gaps by contracting for professional services, hiring ahead to allow overlap and smooth transitions, piloting new technologies to increase efficiency in the absence of staff, and supporting a summer internship program.

Benefits - Pension: Pensions are budgeted based on CalPERS determined rates as of the June 30, 2024 valuation for the City's miscellaneous and safety plans. CalPERS determines the City's total contributions for a given Fiscal Year as the sum of two factors: Normal Cost (NC) and Unfunded Accrued Liability (UAL). Together the NC and the UAL expressed as a percentage of payroll is the 'blended rate' and is used to represent total costs in the discussion below.

The Normal Cost (NC) is expressed as a percentage of payroll and is paid as part of the payroll reporting process of active employees. Commonly referred to as the 'pay-go' cost, the NC is variable and increases or decreases directly with the salary levels of the City. It represents the necessary funding for the City to pay for employees presuming that CalPERS meets the current set of assumptions.

In a year that CalPERS does not meet assumptions, due to plan changes, assumption changes, method changes, or plan experience (including investment gains/losses), there is an increase or decrease to the Unfunded Accrued Liability (UAL). Commonly referred to as the 'catch-up' cost, the UAL is expressed as a dollar amount and is calculated over an amortized period with defined annual payments, similar to a mortgage. The contributions for UAL are billed as a flat dollar amount as opposed to a percentage of payroll due to potential funding issues that could arise from a declining payroll or number of active members in the plan. However, CalPERS provides an estimated percentage of payroll for UAL to allow a consistent comparison of total costs.

In the General Fund, it is anticipated the City will spend a total of \$45.1 million on total pension costs in FY 2027, including both CalPERS contributions and supplemental Pension Trust Fund contributions. This projection reflects the economic and demographic assumptions used in the annual CalPERS Valuation reports, including but not limited to investment returns. The CalPERS projected FY27-36 blended retirement rates are as of the June 30, 2024 valuation for plans and do not reflect any impacts of pension trust to CalPERS for additional discretionary payments (ADP). Should Council authorize, such impacts will be incorporated into the budget development.

Table 1: CalPERS’ Projected FY 2027-2036 Blended Retirement Rates (percentage of payroll)

	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036*
Miscellaneous	40.6%	41.0%	43.1%	42.7%	42.2%	38.7%	37.2%	34.5%	32.7%	31.5%
Safety	82.8%	83.3%	86.3%	85.4%	84.4%	80.2%	77.6%	72.3%	69.7%	67.5%

*FY 2036 projected based on amortization trends.

Retiree Healthcare/Other Post-Employment Benefits (OPEB): Retiree Medical is based on the June 30, 2023 actuarial study prepared by Foster & Foster (previously Bartel Associates), which is completed every two years. The most recent study was completed in June 2024 (CMR 2406-3140¹) to inform the development of the FY 2025 and FY 2026 operating budgets. This biannual actuarial study is anticipated to be updated in Spring 2026 and will be incorporated into FY 2027 budget development.

¹ City Council, June 17, 2024; Agenda Item #28; CMR# 2406-3140;
<https://portal.laserfiche.com/Portal/DocView.aspx?id=73983&repo=r-704298fc&searchid=004d1d0a-4344-4816-ab2d-c044073c40cb>

Consistent with City Council direction and the Retiree Benefit Funding Policy, this forecast continues the practice to budget the full payment of the Actuarial Determined Contribution (ADC) for retiree

healthcare and uses alternative assumptions, such as a more conservative 5.75% discount rate (6.25% assumption), to transmit amounts above the recommended payment as an additional discretionary payment ("prefunding") to the California Employers' Retiree Benefit Trust (CERBT) Fund.

CalPERS blends active employees with pre-Medicare retirees and charges the same medical premium, even though younger employees on average consume less healthcare. The higher premium to younger employees thereby subsidizes older employees and retirees who, on average, have higher claims and premiums. The LRFF estimates \$12.7 million in the General Fund in FY 2027 for ADC. The implied subsidy effectively lowers the funding necessary to meet the ADC.

Table 2: Retiree Medical General Fund Contributions (in millions)

FY 2025	FY 2026	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
\$10.5	\$12.4	\$12.7	\$13.1	\$13.5	\$13.8	\$14.2	\$14.6	\$15.0	\$15.4	\$16.0	\$16.7

Retiree Benefit Funding Policy (formerly “Pension Funding Policy”): The City has taken several proactive steps to address rising pension costs and long-term liabilities, including cost-sharing in labor agreements, establishing an irrevocable Section 115 Pension Trust (“Pension Trust”) and California Employers’ Retiree Benefit Trust (CERBT) Fund, and adopting a policy that guides financial planning of these benefits (CMR 11722 as modified by 2212-0513²).

The City initially contributed to the Pension Trust in FY 2017 on an ad-hoc basis, using one-time savings or excess revenues. Beginning in FY 2019, the City Council directed staff to use a more conservative discount rate as compared to CalPERS for the Normal Cost (NC) portion of the payment and transferring the supplemental funding beyond CalPERS required employer contributions to the Pension Trust. This practice was reinforced with Council approval of the Retiree Benefit Funding Policy, and as of FY 2024 the City’s NC discount rate is 5.3% as compared to CalPERS 6.8%. Additionally, one-time contributions continue to be made each year if excess revenues or unspent savings are available, subject to City Council approval. As part of policy goals, the City seeks to reach a 90% funded status by FY 2036.

Every four years, the City’s Retiree Benefit Funding Policy requires that staff consult with an actuary to inform the City Council of progress the City has made towards achieving a 90% funded status goal and assess and respond to changes impacting the City’s retiree benefit plans. This comprehensive review was most recently completed in FY 2023 and resulted in several policy revisions, most notably reducing the discount rate used to calculate supplemental contributions to the Pension Trust from 6.2% to 5.3% and extending actuary reporting from 3 to 4 years to align with the CalPERS ALM Study. Additionally, the title of the policy was revised from the Pension Policy to the Retiree Benefit Policy to recognize actions approved by the City Council to proactively plan for retiree healthcare plans in a similar manner

² City Council, November 30, 2020; Agenda Item #7; CMR 11722; <https://portal.laserfiche.com/Portal/DocView.aspx?id=105077&repo=r-704298fc>
 City Council, February 6, 2023; Agenda Item #3; CMR 2212-0513; <https://portal.laserfiche.com/Portal/DocView.aspx?id=61647&repo=r-704298fc&searchid=dfeb2c99-41c5-4b0f-87bb-b0704738eb9c>

to pensions, including the use of a lower 5.75% discount rate (CMR 2212-0513³). The most recent actuary analysis projects that the City will meet a 90% funded goal for pension plans by FY 2034 (miscellaneous plan) and FY 2036-37 (safety plan); the City's practice of transmitting excess one-time savings will help reach these goals sooner.

In this forecast, approximately \$8.8 million in the General Fund in supplemental contributions to the City's Pension Trust is assumed in FY 2027. Through FY 2026, a total of \$101.8 million (\$65.5 million in the General Fund) in principal contributions are expected to be made to the Pension Trust for pension benefits. Through FY 2026, it is expected that \$17.5 million in principal contributions will be made to the CERBT Fund for retiree healthcare benefits.

Healthcare: Consistent with the most recent labor agreements between the City and its bargaining units, the City's contribution amounts towards medical costs for employees are based on a flat rate contribution from the City, with the employee contributing towards the remaining medical plan premium. Like salaries, healthcare costs are updated in accordance with applicable Memorandum of Agreements (MOA) between the City and its labor groups and the Management and Professional Personnel and Council Appointees Compensation Plan(s). For FY 2027, Healthcare costs are projected at \$15.4 million.

Workers' Compensation: The budget appropriation for workers' compensation includes an estimate for claims incurred and reserves for current filings at an 85% confidence level, based on actuarial studies completed by Bickmore. Actuarial estimates completed in August 2024 informed FY 2027 budget levels. More recent actuary estimates completed in August 2025 project expense levels to increase, but the allocation between the General Fund and other funds to remain consistent. Staff will continue to monitor expenditures in the fund and bring forward adjustments as necessary. Estimates for workers' compensation increase in the forecast at rates consistent with general CPI increases.

Contract Services

This forecast assumes contract services of \$35.7 million in FY 2027, a 3.1% increase from the FY 2026 Adopted budget of \$34.6 million. This increase for FY 2027 is driven primarily by known contractual increases and a general 3% CPI cost increase on contracts that do not have defined annual increases, based on a review of the changes in the California Consumer Price Index (CCPI) in the San Francisco Bay Area from the August-to-August period. It is expected that the estimated CPI increases will be substituted with department base budget requests to adjust contract funding needs as part of the FY 2027 budget process.

Contract Services - Committed Additions

The Committed Additions included in this forecast account for anticipated operating and maintenance (O&M) costs in the General Fund for capital projects anticipated to come online within the ten-year forecast period. Costs for projects that came online in FY 2026 have been annualized into the ongoing General Fund operating budget as part of the LRFF. The preliminary total estimate is \$52,300 for costs associated with the following projects anticipated to come online in FY 2027: Dog Park Installation (PG-18001), Fire Station 4 (PE-18004), Library Automated Materials Handling (LB-21000), and Park Restroom Installation (PG-19000). Additional cost increases of 3.0% annually are included throughout

³ City Council, February 6, 2023; Agenda Item #3; CMR 2212-0513;
<https://portal.laserfiche.com/Portal/DocView.aspx?id=61647&repo=r-704298fc&searchid=dfeb2c99-41c5-4b0f-87bb-b0704738eb9c>

the ten-year forecast based on a review of the changes in the California Consumer Price Index (CCPI) in the San Francisco Bay Area from the August-to-August period. Timing and analysis of the funding needs for these projects will be evaluated as part of the FY 2027 Budget process and development of the 2027-2031 Capital Improvement Plan (CIP).

TABLE 3: FY 2027 – FY 2036 Committed Additions (Millions)

FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
\$0.05	\$0.05	\$0.07	\$0.11	\$0.12	\$0.12	\$0.14	\$0.14	\$0.16	\$0.17

Supplies and Materials

The FY 2026 Adopted Budget for the General Fund included \$3.6 million for Supplies and Materials, which is anticipated to increase by a 3.0% CPI cost increase in FY 2027 to \$3.7 million based on a review of the changes in the California Consumer Price Index (CCPI) in the San Francisco Bay Area from the August-to-August period. This annual increase is adjusted to 4% starting FY 2029 through the ten-year forecast period. It is expected that the estimated CPI increases will be substituted with department base budget requests to adjust funding for supplies and materials as part of the FY 2027 budget process.

General Expense

This category includes costs for travel and meetings, telephone and non-city utilities, contingency accounts and reserves, bank card service charges, and subsidies and grants provided through the Human Services Resource Allocation Program (HSRAP). The FY 2026 Adopted Budget of \$18.4 million is expected to decrease to \$15.5 million in FY 2027, primarily reflecting a planned year over year reduction in appropriations for settlement payouts and the anticipated use of the Budget Uncertainty Reserve to balance the FY 2027 budget. This reserve was partially used to balance the FY 2026 Adopted Budget (\$5.9 million), leaving funding to partially fund the anticipated gap in FY 2027 (\$14.9 million). The reduction is partially offset by a 3.0% annual CPI cost increase on smaller items that do not have a set annual budget, based on a review of the changes in the California Consumer Price Index (CCPI) in the San Francisco Bay Area from the August-to-August period. It is expected that the estimated CPI increases will be substituted with department base budget requests to adjust funding for general expense items as part of the FY 2027 budget process.

General Expense – Project Homekey

On September 27, 2021 the City Council directed staff to apply for Project Homekey funding in conjunction with LifeMoves to build an emergency shelter at the former Los Altos Treatment Plant (LATP) site (CMR 13595⁴). This project will deploy modular housing to provide interim housing opportunities for homeless individuals and families in the City of Palo Alto. Project Homekey is a program, funded by the State of California Department of Housing and Community Development, intended to provide grant funding and facilitate a partnership with the State to quickly acquire, rehabilitate, or master lease a variety of housing types. Once developed, these projects provide interim or permanent housing options for persons experiencing homelessness. The site will be operated for at

⁴ City Council, September 27, 2021; Agenda Item #10, Page 268; CMR 13595; <https://www.cityofpaloalto.org/files/assets/public/v/6/agendas-minutes-reports/agendas-minutes/city-council-agendas-minutes/2021/09-september/20210927/210927accsm-amended-final.pdf#page=268>

least fifteen years as interim housing per the program’s durational requirement. This project will utilize a combination of funding sources including the Project Homekey Program for capital expenses and donations, grant funds, and City support for ongoing operations expenses. This LRFF includes the City’s committed investment of \$7.0 million in operating expenses (\$1.0 million annually FY 2025 through FY 2031). Some operating funding support is expected from Project Homekey as well as the County of Santa Clara. Any remaining gaps in funding will need to be closed by fundraising, operating cost containment strategies, and/or grant funds.

General Expense - Cubberley Lease

The City and PAUSD adopted a tentative agreement between the City and PAUSD for land acquisition and amends the City’s leased portion of the Cubberley site. Although this agreement still needs to be approved by the City Council, this report assumes a lease costs for Cubberley of \$2.5 million, the current lease of \$2.0 million increases to \$2.5 million if PAUSD vacates its leases. Future lease costs and terms beyond current agreement are subject to renegotiation between the City and PAUSD.

Rents and Leases

The Rents and Leases expense category for FY 2027 is estimated to increase from the FY 2026 Adopted Budget level by approximately 2.7% to \$1.5 million. This is based on current lease terms that include previously negotiated lease increases. This category includes the lease agreement for Development Services staff at locations outside City Hall (285 Hamilton and 526 Bryant) as well as the lease with Stanford for El Camino Park. A new lease agreement was executed in December 2020 for the Development Services office location at 526 Bryant Street, limiting the space to the basement level (CMR 11426⁵). The lease was amended in September 2022 to extend the term initially for 12 months with the right to automatically extend for four successive 12-month periods, potentially through January 31, 2028 (CMR 14713⁶). In June 2021, the City entered into a seventh amendment for the Development Services office lease at 285 Hamilton Avenue to extend the term through January 2026 (CMR 12334⁷). As expenses for rent for Development Services are adjusted, a corresponding revenue adjustment will be made to ensure Development Services maintains cost recovery levels.

Facilities and Equipment

Along with funding for various equipment needs across departments, this budget category includes subscription payments for equipment like public safety radios. The Facilities and Equipment expense category is expected to increase from the FY 2026 Adopted level of \$536,000 to \$552,000 due to standard inflationary adjustments. It is expected that the estimated CPI increases will be substituted with department base budget requests to adjust funding for equipment needs as part of the FY 2027 budget process.

Allocated Charges

Allocated Charges represent expense allocations by the City’s Enterprise and Internal Service Funds for

⁵ City Council, December 14, 2020; Agenda Item #5; CMR 11426;
<https://www.cityofpaloalto.org/files/assets/public/v/1/agendas-minutes-reports/reports/city-manager-reports-cmrs/year-archive/2020-2/id-11426.pdf?t=59979.32>

⁶ City Council, September 27, 2022; Agenda Item #7; CMR 14713;
<https://portal.laserfiche.com/Portal/DocView.aspx?id=59256&repo=r-704298fc&searchid=583219cb-f413-40e9-9c79-1e429984be88>

⁷ City Council, June 21, 2021; Agenda Item #15; CMR 12334;
<https://www.cityofpaloalto.org/files/assets/public/v/1/agendas-minutes-reports/reports/city-manager-reports-cmrs/year-archive/2021/id-12334.pdf>

services and products they provide to other departments. The FY 2026 Adopted Budget for the General Fund included \$30.7 million for these expenses, including utilities usage, general liability insurance, technology costs, vehicle equipment maintenance and replacement costs, and other charges for services provided by other City departments and funds. The FY 2027 allocated charges in the LRFF update the revenues and expenses for these various allocations based on the information available at the time of the LRFF development. FY 2027 is anticipated to experience an increase of 3.8% to a total of \$32.4 million. This increase is primarily due to anticipated higher costs associated with technology services and utilities for City facilities such as water, electricity, and gas.

Operating Transfers Out

Operating Transfers Out include transfers from the General Fund to Debt Service Funds, the Technology Fund, and various other funds but excludes transfers to the Capital Improvement Fund, which are detailed in the following Transfer to Infrastructure section. The FY 2026 Adopted Budget included Operating Transfers Out of \$6.4 million. In FY 2027, Operating Transfers Out are anticipated to remain relatively flat of \$6.3 million to maintain the same service levels. Consistent with the FY 2026 Adopted Budget, a total of \$2.0 million across the University Avenue, California Avenue, and Residential Permit Parking Funds is factored into this LRFF.

Transfer to Infrastructure

The total General Fund transfer to the Capital Improvement Fund budgeted in FY 2026 is \$32.3 million compared to the \$30.2 million transferred in FY 2025. This is comprised of a \$14.0 million base transfer, interest earnings of \$1.1 million, \$14.3 million from TOT revenue generated through voter-approved rate increases and new hotels that is dedicated to the Capital Improvement Fund to support the 2014 Council Infrastructure Plan, and \$2.9 million of Utility User Tax (UUT) and Measure K Business Tax transferred directly into specific capital projects, consistent with City Council direction. Looking ahead, estimated transfers from TOT revenues in FY 2027 are projected to increase to \$14.9 million and the base transfer to increase to \$16.1 million, along with estimated interest earnings of \$1.1 million, and \$2.5 million of UUT and Measure K Business Tax transferred directly into specific capital projects, for a total \$34.7 million transfer to the Capital Improvement Fund. This forecast continues the goal established as part of the 2022-2026 Capital Improvement Plan (CIP) to restore the base portion of this transfer to pre-pandemic levels. This budget category also includes the separate \$1.9 million transfer to the Cubberley Property Infrastructure Fund. This transfer to the Cubberley Property Infrastructure Fund supports facility systems maintenance needs at the Cubberley Community Center facility as well as capital improvement projects to maintain and upkeep the facility.

Assumptions Not Included in Forecast

It should be noted that this forecast does not include several potential impacts to the FY 2027-2036 LRFF that are outlined below. These items are known projects or areas of investment that are priorities but have not been fully developed in terms of costs and timelines. This is not intended to be a comprehensive list nor in any priority order.

Project Homekey: Homekey Palo Alto, a modular interim housing shelter for unhoused individuals and families codeveloped by the City of Palo Alto and LifeMoves, continues to operate at the former Los Altos Treatment Plant (LATP) site. This LRFF incorporates the City's ongoing committed investment of \$7.0 million in operating expenses (\$1.0 million annually for seven years). While the City's direct costs for this project are currently programmed, future fluctuations could occur over the ten-year period. Potential offsets may be available through business tax revenue specifically designated for affordable housing and homeless services that has not yet been fully allocated. Upon the completion of the initial 7-year term, the source and structure of ongoing funding remain to be determined and will be evaluated in future forecast cycles.

Housing Growth Impacts: The City's certified FY 2023-31 Housing Element¹ outlines the condition of the City's current housing and future needs of its residents through citywide housing goals, objectives, and policies. The City is required to ensure adequate planning for its "fair share" of affordable and market rate housing, defined by its RHNA allocation of an additional 6,086 total units. The financial implications of this housing growth continue to evolve, increasing potential costs for land acquisition, planning and design, and construction, with potential offsets from new revenues such as sales tax and other economic benefits derived from more affordable housing. While significant planning has occurred, the full financial impacts, especially to the General Fund over the long term, have yet to be fully determined and incorporated into the LRFF.

Geng Road Safe Parking Program: The Geng Road program, launched in early 2021 in partnership with Santa Clara County, offers recreational vehicle (RV) dwellers a safe place to park, case management, and assistance with finding permanent homes. Following the City Council's approval to expand the site at 2000 Geng Road, the program's capacity has increased (CMR 2407-3274²). Staff continues to work on securing funding for operations through the California Department of Housing and Community Development's (HCD) Permanent Local Housing Allocation Program (PLHA). Even with grant funding, PLHA is not expected to fully fund the ongoing operations, and any balance of the costs may be funded by business tax revenue for affordable housing and homeless services that has not yet been fully allocated, or other sources as may be identified during the budget process.

Sustainability and Climate Action Plan (S/CAP): The City continues to implement its Sustainability and Climate Action Plan (S/CAP) to meet the goal of reducing greenhouse gas (GHG) emissions to 80 percent below 1990 levels by 2030 (the "80x30" goal). Investments

¹ City of Palo Alto FY 2023-31 Housing Element, <https://paloaltohousingelement.com/wp-content/uploads/2024/08/Palo-Alto-Housing-Element.pdf>

² City Council, August 19, 2024; Agenda Item #10; Staff Report #2407-3274, <https://portal.laserfiche.com/Portal/DocView.aspx?id=88920&repo=r-704298fc&searchid=1196faea-adb3-49fd-9006-dfb863754685>

continue across various City funds related to S/CAP, including grid modernization, infrastructure improvements, and electrification incentives. The S/CAP Work Plan provides a roadmap for these efforts, and the City has accounted for known capital projects and programmatic needs in its forecasts. However, uncertainties related to external factors, technological advancements, and the pace of adoption could impact the scope and scale of work needed to achieve the City's long-term sustainability goals. These unknowns are not fully reflected in this forecast.

Significant Code and Ordinance Updates: Updates to several significant programs, codes, and ordinances continue to be necessary. Key initiatives include Seismic Inventory Ordinance and Program Development, Historic Building Survey and Ordinance Development, Zoning Code Updates, and the implementation of the 2040 Comprehensive Plan. While some costs associated with these updates were included in the forecast, additional resources may be required depending on future Council direction and the extent and pace of implementation efforts.

Fee and Organizational Studies: The City regularly conducts comprehensive cost allocation plans and municipal fee studies to ensure fees align with cost recovery policies. Following the implementation of recommendations from the FY 2025 study, staff continues to evaluate and bring forward adjustments to align fees with target cost recovery levels to cover general salary and benefits increases and CPI trends. These efforts aim to improve fee transparency and ensure equitable cost distribution across City services. Future adjustments based on subsequent studies are not fully factored into the outer years of this forecast.

Labor Negotiations: In FY 2025, the City successfully negotiated new labor agreements with most bargaining units, extending terms through December 2027 (SEIU) and June 2028 (IAFF, UMPAPA). Consistent with Council direction in previous LRFFs, a general 2% assumption is included for all employees in the years following the expiration of these agreements for forecasting purposes; this is not a commitment to future negotiations. Additionally, this forecast includes a level of reserve for potential changes in employee compensation in future agreements for competitive wages and other terms of employment. Actual funding needs may differ, depending on outcomes of future labor negotiations.

Grade Separation: The grade separation project consists of at-grade crossings along the Caltrain corridor in the City of Palo Alto. The City continues to advance the project through the Preliminary Engineering and Environmental Documentation (PE&ED) Phase (CMR 2404-2861³). Currently, staff is working with the Valley Transportation Authority (VTA) and Caltrain to allocate Measure B funding. As Grade Separation funding requires matching local funds, additional funding sources will need to be identified to perform this work in upcoming years. Additional resources will need to be explored to plan and fund these grade separations, including City staff pursuing additional funding through grant opportunities and other financing mechanisms.

Parks Master Plan: The Parks, Trails, Natural Open Space and Recreation Master Plan⁴ presents a long-term vision for the system. While potential funding mechanisms have been identified for several high-priority projects and programs, a strategy to fund implementation of the entire

³ City Council, June 17, 2024; Staff Report #2404-2861,

<https://portal.laserfiche.com/Portal/DocView.aspx?id=73967&repo=r-704298fc&searchid=948efea6-f77f-4463-a371-dabd04cd097d>

⁴ The Parks, Trails, Natural Open Space and Recreation Master Plan, 2017;

<https://www.cityofpaloalto.org/files/assets/public/public-works/palo-alto-parks-master-plan.pdf>

plan has not been completed. As such, this forecast does not yet contemplate the necessary investments to fully execute this plan.

City-owned Assets Operated by Non-profit Organizations: This Forecast does not include any additional capital or operating investments for the Avenidas Senior Center, the Ventura Childcare Center, nor the Sea Scout Building. As costs around potential capital or operating investments for these assets solidify, staff will return to City Council to address them as appropriate. The Roth Building Rehabilitation continues to proceed under its funding strategy; however, if costs for rehabilitating the facility further increase, additional sources of funding would need to be identified.

Cubberley Community Center Redevelopment: Following the City Council's approval (CMR 2409-3500⁵) of the MOU with PAUSD for the Cubberley Site purchase and lease, the LRFF includes the revised lease financial terms and maintains the Real Estate Investment Reserve. This reserve funds critical professional service contracts (i.e., master plan, community outreach) and serves as a placeholder for future real estate investment appropriations. However, the LRFF does not reflect any potential General Obligation bond cashflow or future operating costs and repairs for a redeveloped site, as these fiscal impacts will be informed by the ongoing development of operational and financial models.

Loans for Special Projects: From time to time the City's General Fund will assist other City operations with modest cash flow loans to bridge fiscal years. As parking continues to be impacted by long-term shifts in demand, additional support or loans from the General Fund to the parking funds may be required. This LRFF assumes repayment revenue to the General Fund from previous parking loans in the outer years of the forecast. Staff will continue to review costs in the parking funds and revise funding needs and evaluate support as a loan or subsidy from the General Fund as part of the annual budget process.

Legislative Updates: Various actions at the state and federal level that could impact the City of Palo Alto have not been incorporated into this forecast due to the changing context and uncertainty of the quantitative impacts of potential legislative changes. As the potential impacts of various legislative initiatives are clarified, appropriate adjustments will be identified and brought forward as part of future budget development cycles.

Aging or Noncompliant Infrastructure: The City maintains indoor and outdoor facilities, many of which have been identified in the City's ADA transition plan and by the Infrastructure Blue Ribbon Commission as requiring capital project work to bring them up to full ADA compliance and/or sufficient conditions. Staff continues the program work needed in this area as part of the Americans with Disabilities Act Compliance capital project; however, the entire scope of work needed in this area exceeds current resources.

General Liability Umbrella Excess Premiums: The City's General Liability Program provides funding to cover various insurance policies for City-owned equipment and machinery. General Liability Umbrella Excess Premiums are anticipated to increase in future years due to significant national events and natural disasters. Staff will bring forward adjustments for these costs as part of future budget cycles as they become available.

Fire and Ambulance Service Expansion: Staff continues to analyze options for fire and

⁵ City Council, October 7, 2024; Agenda Item #AA1; Staff Report #2409-3500, <https://portal.laserfiche.com/Portal/DocView.aspx?id=98620&repo=r-704298fc&searchid=d8e93928-24cc-47b6-b45b-978951b272c4>

ambulance service expansion. Any funding, appropriation, and labor negotiation related to such expansion will be guided by future City Council direction, and as such is not incorporated into the LRFF at this time.

Fire Training Center: The City continues to evaluate options for the Fire Training Facility Replacement capital project, including identifying an appropriate site or partnering with other local jurisdictions. Funding for construction has not been fully appropriated, and additional resources will need to be identified in future budget cycles based on the results of ongoing studies and consultant engagements.

Limited Term Programs: There are several programs currently in progress that are funded on a limited term basis per Council approval. If these programs are recommended to continue through the ten-year forecast period, additional resources would be needed. These include the Psychiatric Emergency Response Team (PERT) program and the Palo Alto Link on-demand transit service, which rely on a mix of City funding, grants, and partner contributions that may require renewal or backfill in future years.

Vehicle Fleet Electrification: Currently the City's policy is to consider electric vehicles and then other alternative fuel vehicles when replacing existing vehicles. Transitioning the vehicle fleet to full Electric Vehicles (EVs) is part of the City's sustainability goals. It has been estimated that significant additional funding across all funds will be needed annually in order to replace all City vehicles with EVs.

Green Storm Infrastructure (GSI) Maintenance: The City is subject to the requirements of the Municipal Regional Stormwater National Pollutant Discharge Elimination System Permit. The City expects to have significantly more Green Stormwater Infrastructure (GSI) and associated maintenance in the coming years to comply with permit provisions. The long-term cost of this maintenance is still being quantified and is not fully reflected in this forecast.

Summary of Positions & Vacancy by Department

Attachment B

Source: FY 2019-2025 Adopted Operating Budget Books - Dept Org Charts,
At Place Memos - Vacancy Reports as of April of that Calendar Year

Department	Fiscal Year	Adopted FTE	Filled FTE	Vacant FTE Total	Footnote
City Attorney					
	2019	11.00	9.00	2.00	
	2020	11.00	11.00	-	
	2021	11.00	10.00	1.00	
	2022	11.00	11.00	-	
	2023	11.00	11.00	-	
	2024	13.00	11.00	2.00	
	2025	13.00	13.00	-	
City Auditor					
	2019	6.00	6.00	-	
	2020	5.00	4.00	1.00	
	2021	4.00	4.00	-	
	2022				1
	2023				
	2024				
	2025				
City Clerk					
	2019	5.00	5.00	-	
	2020	5.00	4.00	1.00	
	2021	5.00	4.00	1.00	
	2022	5.00	5.00	-	
	2023	5.00	4.00	1.00	
	2024	5.00	3.00	2.00	
	2025	5.00	5.00	-	
City Manager					
	2019	12.00	10.00	2.00	
	2020	10.75	7.75	3.00	
	2021	10.00	7.00	3.00	
	2022	9.00	4.00	5.00	
	2023	12.00	11.00	1.00	
	2024	13.00	12.25	0.75	
	2025	14.00	14.00	-	
Administrative Services					
	2019	58.50	54.30	4.20	
	2020	58.50	50.00	8.50	
	2021	59.50	52.00	7.50	
	2022	53.50	46.50	7.00	
	2023	55.50	46.50	9.00	
	2024	57.00	51.50	5.50	
	2025	60.00	51.50	8.50	
Community Services					
	2019	78.60	73.53	5.07	
	2020	78.60	74.60	4.00	

Department	Fiscal Year	Adopted FTE	Filled FTE	Vacant FTE Total	Footnote
	2021	78.60	74.95	3.65	
	2022	71.25	63.25	8.00	
	2023	74.35	70.60	3.75	
	2024	82.25	79.50	2.75	2
	2025	82.25	77.25	5.00	
Development Services					
	2019	20.00	20.00	-	
	2020				3
	2021				
	2022				
	2023				
	2024				
	2025				
Fire					
	2019	103.70	96.70	7.00	
	2020	103.50	99.50	4.00	
	2021	105.50	103.50	2.00	
	2022	94.50	89.50	5.00	
	2023	107.50	99.50	8.00	
	2024	110.50	92.50	18.00	4
	2025	113.50	103.50	10.00	
Human Resources					
	2019	17.00	16.00	1.00	
	2020	17.00	16.00	1.00	
	2021	17.00	16.25	0.75	
	2022	16.00	12.00	4.00	
	2023	17.00	14.00	3.00	
	2024	19.75	17.75	2.00	
	2025	19.75	18.75	1.00	
Information Technology					
	2019	33.00	31.00	2.00	
	2020	33.00	31.00	2.00	
	2021	33.00	33.00	-	
	2022	29.00	24.00	5.00	
	2023	31.00	29.00	2.00	
	2024	34.00	32.00	2.00	
	2025	35.00	31.00	4.00	
Library					
	2019	47.50	44.50	3.00	
	2020	46.50	43.50	3.00	
	2021	47.50	43.50	4.00	
	2022	40.50	32.00	8.50	
	2023	46.50	35.50	11.00	
	2024	49.00	39.00	10.00	
	2025	49.00	43.00	6.00	
Office of Emergency Services					

Department	Fiscal Year	Adopted FTE	Filled FTE	Vacant FTE Total	Footnote
	2019	3.00	3.00	-	
	2020	3.00	3.00	-	
	2021	3.00	3.00	-	
	2022	2.00	2.00	-	
	2023	2.00	2.00	-	
	2024	3.00	3.00	-	
	2025	3.00	3.00	-	
Office of Transportation					
	2019				6
	2020	15.00	15.00	-	
	2021	15.00	15.00	-	
	2022	15.00	13.00	2.00	
	2023	15.00	15.00	-	
	2024	17.00	15.00	2.00	
	2025	18.00	16.00	2.00	
Planning & Development Services					
	2019	42.46	28.96	13.50	7
	2020	51.00	33.50	17.50	
	2021	51.00	46.00	5.00	
	2022	45.00	41.00	4.00	
	2023	52.00	39.00	13.00	
	2024	56.00	47.00	9.00	
	2025	61.00	50.00	11.00	8
Police					
	2019	156.50	133.50	23.00	
	2020	150.50	128.50	22.00	
	2021	148.50	144.50	4.00	
	2022	125.50	116.50	9.00	
	2023	134.50	120.50	14.00	
	2024	140.50	124.50	16.00	9
	2025	140.50	131.50	9.00	
Public Works					
	2019	202.00	186.12	15.88	
	2020	199.50	181.50	18.00	
	2021	198.25	176.00	22.25	
	2022	193.25	158.00	35.25	
	2023	200.50	177.00	23.50	
	2024	207.00	179.00	28.00	
	2025	208.00	185.00	23.00	
Utilities					
	2019	244.50	206.40	38.10	
	2020	245.00	215.00	30.00	
	2021	245.00	212.00	33.00	
	2022	245.00	198.00	47.00	
	2023	253.50	199.50	54.00	
	2024	257.00	219.00	38.00	

Department	Fiscal Year	Adopted FTE	Filled FTE	Vacant FTE Total	Footnote
	2025	267.00	225.00	42.00	
Reconciling Difference (org chart vs total FTE)					
	2019	(0.59)			
	2020	(2.00)			
	2021	(3.00)			
	2022	(0.50)			
	2023	(0.50)			
	2024	0.90			
	2025	(3.10)			
Total for 2019		1,041.35	924.01	116.75	
Total for 2020		1,034.85	917.85	115.00	
Total for 2021		1,034.85	944.70	87.15	
Total for 2022		956.00	815.75	139.75	
Total for 2023		1,017.85	874.10	143.25	10
Total for 2024		1,063.10	926.00	138.00	11
Total for 2025		1,092.10	967.50	121.50	
Grand Total		7,240.10	6,369.91	861.40	

Department	Footnote	Description
City Auditor	1	After conducting a competitive process Council selected Baker Tilly as the City's Auditing firm. This function remains with Baker Tilly through the writing of this report.
Community Services	2	FY23 and FY24 CSD had significant position restorations including Assistant Director and Division Manager level classifications frozen during the pandemic. FY24 also saw small increases in services/positions within Art Center, JMZ, and Theaters.
Development Services	3	The Development Services Department was combined with the Planning and Community Environment Department in FY 2020 to form the Planning and Development Services Department.
Fire	4	The vacancy number reflects 18 vacancies but 8 of those were newly hired firefighters in the onboarding process and not yet reflected in the report. We typically hire more than 8 firefighters at a time.
Fire	5	Addition of 7.0 FTE positions to create the initial/pilot Single Role EMS Division of the Fire Department and 3.0 FTE Fire Captain positions to permanently cross staff Engine 64 and Medic 64 (per council directive in FY25).
Office of Transportation	6	In FY 2020 Office of Transportation was created within the City Manager's office, these positions were transferred from Planning and Community Environment.
Planning and Development Services	7	See footnote 3.
Planning and Development Services	8	In FY23 Planning underwent an organizational structure review and analysis resulting in changes to the structure and needed classification to meet increasing planning demands in long term planning and development services. These changes were implemented in FY24 consistent with this review and the recommendations.
Police	9	Restored various positions including 2.00 Public Safety Dispatchers to the Dispatching Servicing Team due to the high volume of calls for service and restored 2.00 Police Officers to the Traffic Enforcement Division due to increasing community concern regarding traffic safety around the City.
Total for 2023	10	FY 2022, the City Council approved amendments to realign the budget with a more optimistic economic outlook and proactively reinvest in activities that addressed the most immediate needs of the City and its residents into FY2023.
Total for 2024	11	FY 2024 Budget continues to invest in staffing resources that support City services and Council priorities.

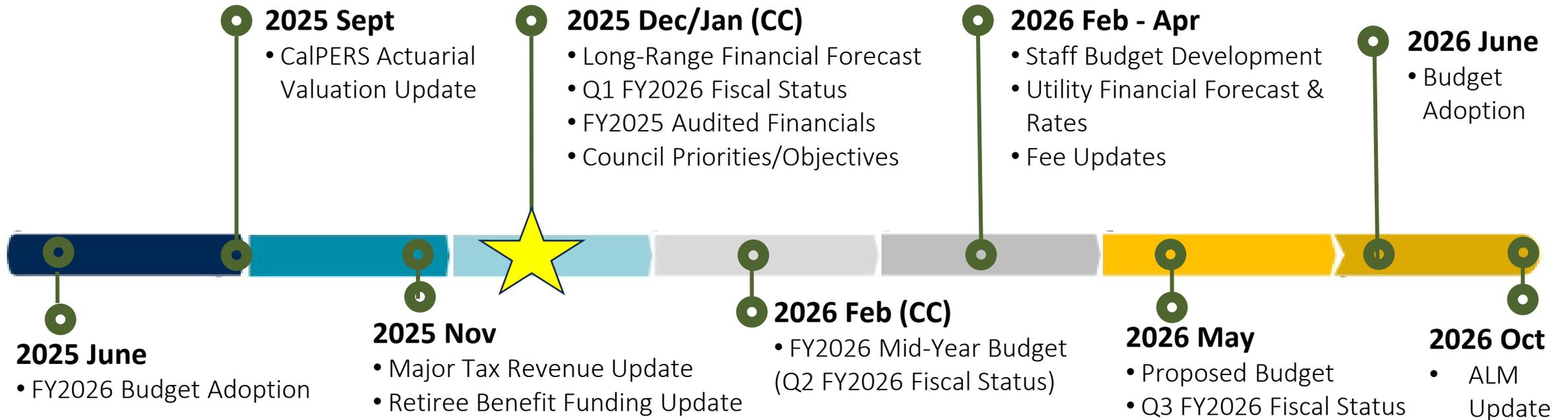


FY 2027 – FY 2036
**LONG RANGE
FINANCIAL FORECAST**

City Council Item #12

FINANCIAL PLANNING CYCLES & CONVERSATIONS

At the prior Finance Committee meeting, staff provided updates on Major Tax Revenues and Retiree Benefits. Today's presentation continues the discussion with the **Long-Range Financial Forecast**.





SUMMARY OVERVIEW

1. Finance Committee review and recommendation
2. The Economy
3. FY 2027 - 2036 Long-Range Financial Forecast (LRFF)
4. Budget Balancing Strategies
5. Budget Stabilization Reserve (BSR)
6. FY 2027 Budget Development Guidelines
7. Recommendation

Finance Committee & Staff recommend that the City Council review and approve the FY 2027 – 2036 Long-Range Financial Forecast (LRFF) and forward to the City Council and FY 2027 Annual Budget Development Guidelines and Using the LRFF as the Baseline for developing the FY2027 Budget.



FINANCE COMMITTEE REVIEW & RECOMMENDATION

December 2, 2025, Finance Committee reviewed and recommends the LRFF for Council approval, with additional consideration:

1. Services/Programs and Council Priorities – funding limitations
2. Property Tax & Sales Tax Projections – reduced revenues
3. TOT – primary drivers
4. Vacancy Rate
5. Historical trends 2019 onwards – Attachment B historical staffing
6. Known Unknowns – alternative funding sources

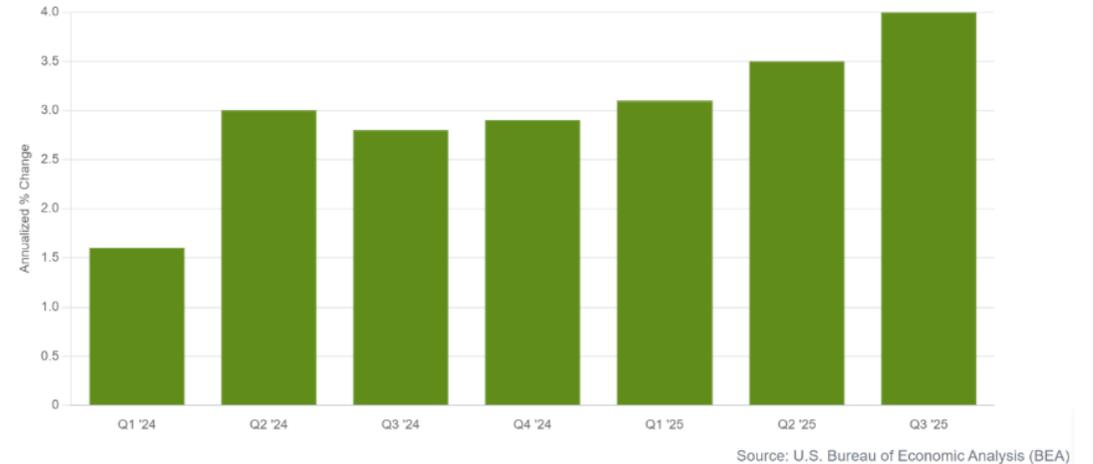
1. ECONOMY

While the national economy shows strength (GDP growth to 4.0%), the **local Bay Area economy is projected to experience a sluggish recovery**, indicating specific softness in the regional tech sector.

- Palo Alto's economy's recovery is projected to be sluggish, lagging national growth due to regional tech labor market softness,
- The *Fall 2025 UCLA Anderson Outlook* that expects a structural upturn for California only starting late 2026 and accelerating in 2027.

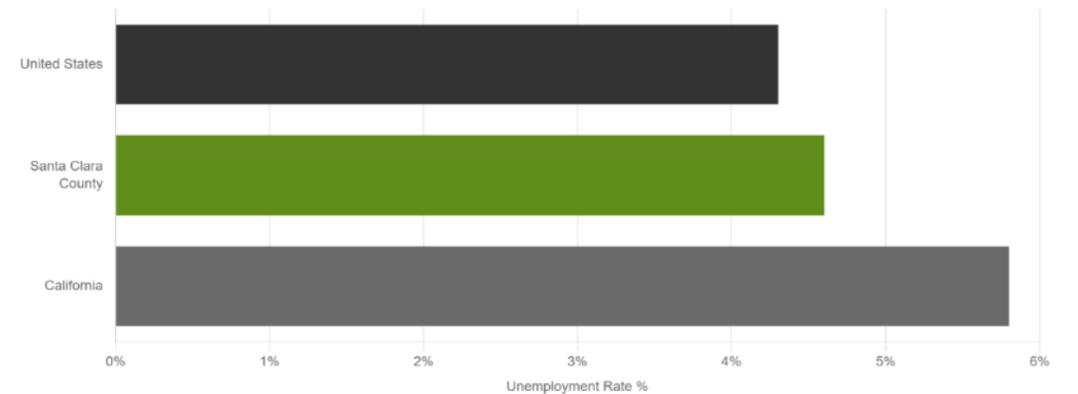
National Gross Domestic Product (GDP)

Real GDP: Percent Change from Preceding Quarter



Regional Unemployment

Unemployment Rate Comparison: Unadjusted Rates (August 2025)



Source: U.S. BLS, California EDD

2. FY 2027 – 2036 LONG RANGE FINANCIAL FORECAST (LRFF)

The forecast shows a **structural deficit beginning with a \$14.9 million gap in FY 2027**, driven by revenues that are structurally outpaced by rising expenditure costs.

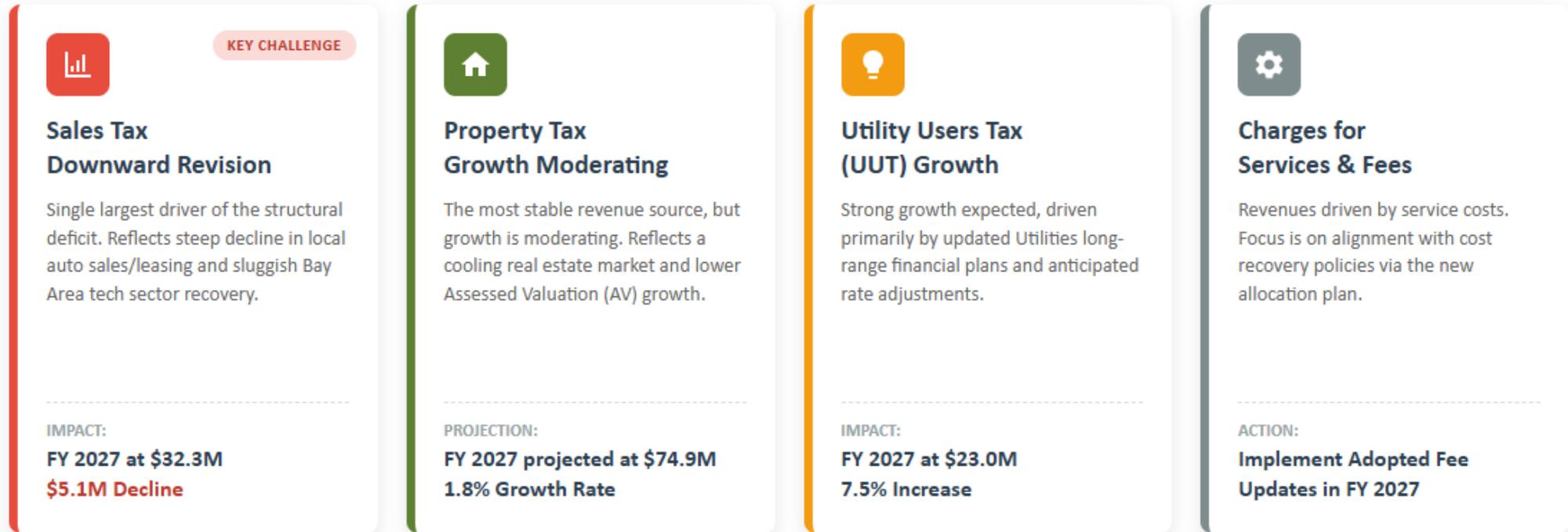
Metric (Millions)	FY 26 Adopted	FY 26 Projected	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
TOTAL REVENUES	\$307.0	\$298.0	\$305.1	\$316.9	\$327.2	\$340.4	\$353.0	\$365.2	\$378.4	\$390.3	\$404.6	\$418.8
<i>Revenues</i>	\$301.2	\$292.2	\$305.1	\$316.9	\$327.2	\$340.4	\$353.0	\$365.2	\$378.4	\$390.3	\$404.6	\$418.8
<i>Uncertainty Reserve</i>	\$5.8	\$5.8	-	-	-	-	-	-	-	-	-	-
TOTAL EXPENDITURES	\$307.0	\$307.0	\$320.0	\$329.7	\$342.5	\$354.6	\$363.7	\$371.6	\$377.4	\$386.0	\$393.3	\$405.6
SURPLUS / (DEFICIT)	\$0.0	(\$9.0)	(\$14.9)	(\$12.8)	(\$15.3)	(\$14.2)	(\$10.7)	(\$6.4)	\$1.0	\$4.3	\$11.3	\$13.2

Highlights

- Projected deficit from FY 26 – FY 32
- FY26 Revenue declines + slow recovery
- BSR reserve management

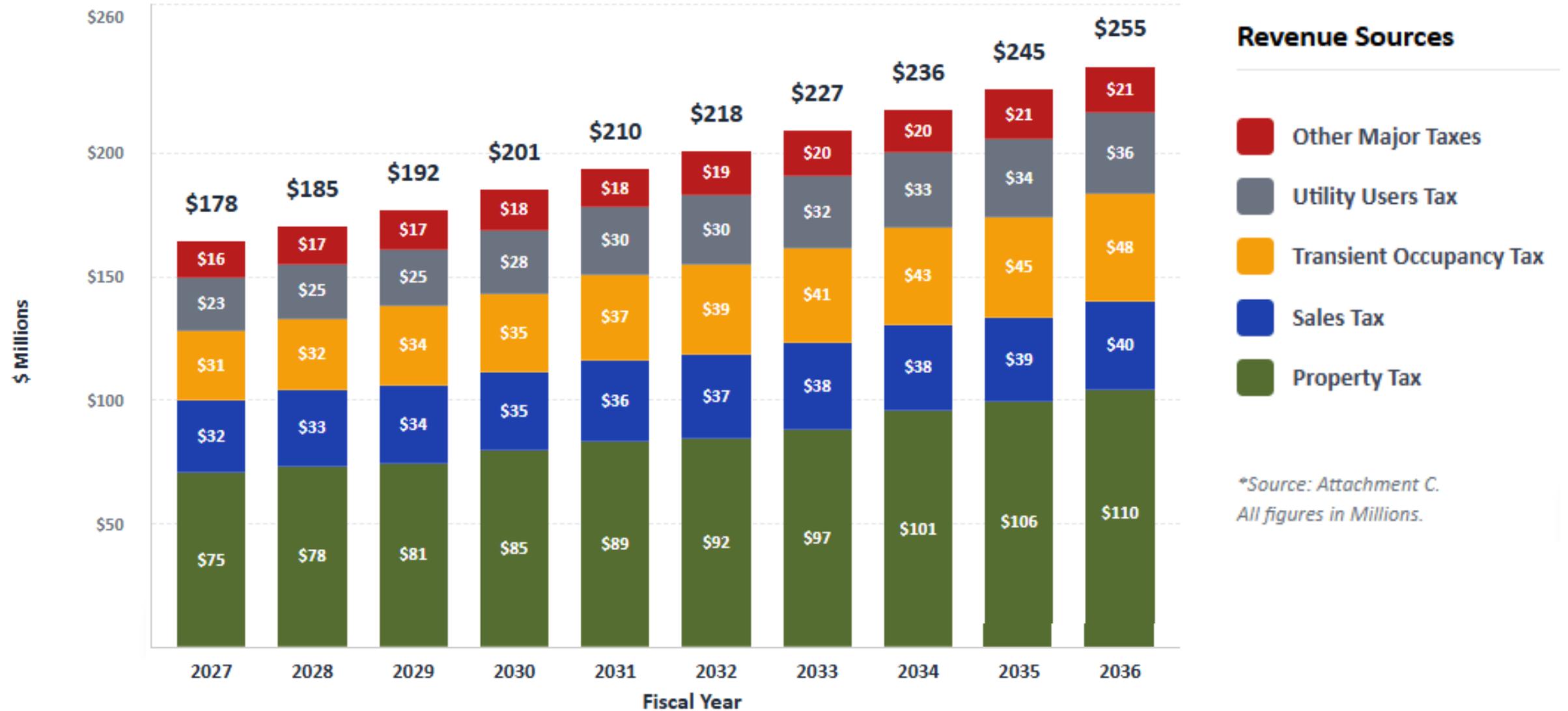
2A. LRFF REVENUES

The LRFF projects **total revenues of \$305.1M in FY 2027**, representing a \$1.9M reduction from the FY 2026 Adopted Budget (\$307.0M). This decline is primarily driven by the \$5.1M reduction in Sales Taxes, which necessitates advancing budget balancing strategies.



*Property Tax (6.9% CAGR) projects moderated 1.8% growth to \$74.9M (from \$73.6M adopted). This \$74.9M projection is based on a 4.8% increase from the revised \$72.3M FY 2026 baseline (per County Tax Roll) and assumes mid-4% in the long-term projections.

2A. REVENUE GROUPINGS – MAJOR TAX (\$ MILLION)



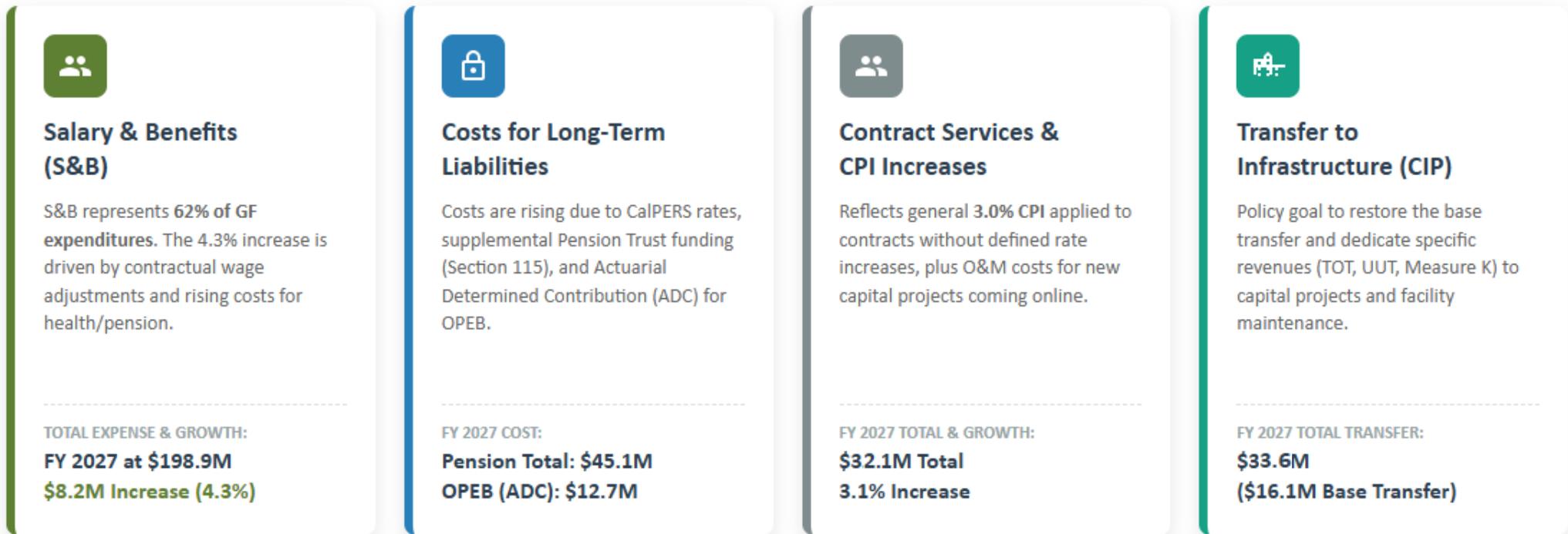
*Source: Attachment C.
All figures in Millions.

2A. LRFF REVENUE DETAILS (\$ MILLION)

Revenue & Other Sources	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
Sales Taxes	\$32.3	\$33.3	\$34.3	\$35.3	\$36.1	\$37.0	\$37.8	\$38.5	\$39.3	\$40.1
Property Taxes	\$74.9	\$78.1	\$81.4	\$84.9	\$88.6	\$92.5	\$96.6	\$100.9	\$105.5	\$110.3
Transient Occupancy Tax	\$31.0	\$32.3	\$33.8	\$35.4	\$37.1	\$39.1	\$41.1	\$43.3	\$45.5	\$47.9
Documentary Transfer Tax	\$9.0	\$9.3	\$9.5	\$9.8	\$10.2	\$10.5	\$10.9	\$11.3	\$11.7	\$12.1
Utility Users Tax	\$23.0	\$24.7	\$25.4	\$27.9	\$29.5	\$30.5	\$31.7	\$32.9	\$34.4	\$35.8
Business Tax	\$6.7	\$6.8	\$7.0	\$7.2	\$7.4	\$7.6	\$7.8	\$8.0	\$8.2	\$8.4
Other Taxes and Fines	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8	\$0.8
Subtotal: Taxes	\$177.7	\$185.3	\$192.2	\$201.3	\$209.7	\$218.0	\$226.7	\$235.7	\$245.4	\$255.4
Charges for Services	\$45.1	\$46.2	\$46.9	\$47.7	\$48.3	\$48.7	\$49.0	\$49.3	\$49.6	\$49.9
Permits and Licenses	\$11.8	\$12.0	\$12.1	\$12.3	\$12.5	\$12.7	\$12.7	\$12.8	\$13.0	\$13.1
Return on Investments	\$3.7	\$3.8	\$3.9	\$4.1	\$4.2	\$4.4	\$4.6	\$4.8	\$5.0	\$5.2
Rental Income	\$17.0	\$17.5	\$18.1	\$18.8	\$19.4	\$20.1	\$20.8	\$21.5	\$22.3	\$23.1
From Other Agencies	\$1.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1	\$0.1
Charges to Other Funds	\$15.8	\$16.2	\$16.7	\$17.0	\$17.4	\$17.5	\$17.8	\$17.9	\$18.0	\$18.0
Other Revenue	\$2.5	\$2.6	\$2.6	\$2.6	\$2.6	\$2.6	\$2.7	\$2.7	\$2.7	\$1.9
Subtotal: Non-Tax	\$97.0	\$98.3	\$100.5	\$102.6	\$104.5	\$106.1	\$107.7	\$109.1	\$110.6	\$111.3
Operating Transfers-In	\$30.4	\$33.2	\$34.6	\$36.7	\$38.8	\$41.2	\$44.1	\$45.7	\$48.6	\$51.4
TOTAL REVENUE	\$305.1	\$316.9	\$327.2	\$340.4	\$353.0	\$365.2	\$378.4	\$390.3	\$404.6	\$418.8

2B. LRFF EXPENDITURES

Total **expenditures are projected to grow 4.3% to \$320.0M in FY 2027**. This growth rate, driven by personnel costs and long-term liabilities, structurally outpaces the projected 1.3% revenue growth, leading to the projected deficit. Includes \$6m reduction in FY 26 - 28.



*Assumptions NOT INCLUDED in the expenditure forecast are included as Attachment E.

2B. LRFF EXPENDITURE DETAIL (\$ MILLION)

Expenditures & Other Uses	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032	FY 2033	FY 2034	FY 2035	FY 2036
Salary & Benefits	\$198.9	\$203.6	\$209.9	\$216.2	\$220.1	\$223.7	\$225.5	\$228.7	\$230.2	\$232.3
Contract Services	\$32.1	\$33.1	\$35.2	\$36.6	\$38.0	\$39.6	\$41.1	\$42.8	\$44.5	\$46.3
Supplies & Material	\$4.0	\$4.1	\$4.2	\$4.3	\$4.5	\$4.7	\$4.9	\$5.1	\$5.3	\$5.5
General Expense	\$10.5	\$10.8	\$11.1	\$11.5	\$11.9	\$12.3	\$12.7	\$13.1	\$13.6	\$14.6
Rents & Leases	\$1.5	\$1.6	\$1.7	\$1.7	\$1.8	\$1.8	\$1.8	\$1.9	\$1.9	\$0.2
Facilities & Equipment	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7	\$0.7
Allocated Charges	\$32.4	\$33.7	\$35.2	\$36.7	\$38.2	\$38.8	\$38.9	\$40.0	\$41.4	\$50.0
Subtotal: Non S&B	\$81.2	\$84.0	\$88.1	\$91.5	\$95.1	\$97.9	\$100.1	\$103.6	\$107.4	\$117.3
Operating Transfers-Out	\$6.3	\$6.3	\$6.4	\$6.4	\$6.7	\$6.6	\$6.8	\$7.0	\$7.2	\$5.6
Transfer to Infrastructure	\$33.6	\$35.8	\$38.1	\$40.5	\$41.8	\$43.4	\$45.0	\$46.7	\$48.5	\$50.4
TOTAL EXPENDITURES	\$320.0	\$329.7	\$342.5	\$354.6	\$363.7	\$371.6	\$377.4	\$386.0	\$393.3	\$405.6

3. BALANCING STRATEGY(\$ MILLION)

The options below provide the City Council with a strategy to eliminate the deficit in the **short** and long term.

	FY 2027
Revenues	
Explore new/updated fees and other revenues	\$0.8
Budget Stabilization Reserve (BSR)	\$2.0
Budget Reductions	
FY 26 <i>Approved</i> Reductions thru FY 32 (<i>\$6 m w/\$3.4 m on-going ~ \$2.4m GF + \$1 m CIP</i>)	\$3.4M in base
Budget Reductions	
FY 27 <i>Additional</i> Reductions thru FY 32 (To be determined during FY27 Budget Development)	\$7.0
CIP Reductions	
FY 2027 <i>Additional</i> Reduction to Capital (To be determined during FY27 Budget Development)	\$1.0
Pension Cost	
Reduce Additional Discretionary Payment (ADC)	\$3.6
Pension Cost	
Reduce Additional Discretionary Payment (ADP)	\$0.5
BUDGET STRATEGY TOTAL:	\$14.9
Remaining Surplus/(Deficit)	\$0.0

3. BALANCING STRATEGY(\$ MILLION)

The options below provide the City Council with a strategy to eliminate the deficit in the short and **long term**.

	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	FY 2032
Revenues						
Explore new/updated fees and other revenues	\$0.8	\$0.8	\$0.8	\$0.9	\$0.9	\$0.9
Budget Stabilization Reserve (BSR)	\$2.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Budget Reductions						
FY 26 <i>Approved</i> Reductions thru FY 32 (\$6 m w/\$3.4 m on-going ~ \$2.4m GF + \$1 m CIP)	\$3.4M in base	\$3.4M in base	\$3.4	\$3.4	\$3.4	\$3.4
Budget Reductions						
FY 27 <i>Additional</i> Reductions thru FY 32	\$7.0	\$7.0	\$7.0	\$5.8	\$2.3	\$2.1
CIP Reductions						
FY 2027 <i>Additional</i> Reduction to Capital	\$1.0	\$1.0	\$0.0	\$0.0	\$0.0	\$0.0
Pension Cost						
Reduce Additional Discretionary Payment (ADC)	\$3.6	\$3.6	\$3.6	\$3.6	\$3.6	\$0.0
Pension Cost						
Reduce Additional Discretionary Payment (ADP)	\$0.5	\$0.5	\$0.5	\$0.5	\$0.5	\$0.0
BUDGET STRATEGY TOTAL:	\$14.9	\$12.9	\$15.3	\$14.2	\$10.7	\$6.4
Remaining Surplus/(Deficit)	\$0.0	\$0.1	\$0.0	\$0.0	\$0.0	\$0.0

4. BUDGET STABILIZATION RESERVE (BSR) (\$ MILLION)

BSR - Projected Ending	Amount (\$million)
FY 2026, Actual Ending BSR	\$58.9
Additional BSR (Adopted FY26 Budget) \$0.2M	\$0.2
Use of BSR FY26 Budget Amendments	-\$0.3
FY 2026, Adjusted BSR	\$58.8
BSR – Policy Analysis (Projections):	
Recommend Roll Uncertainty Reserve (UR) into BSR	\$6.0M
FY 2026, BSR Projected Ending Balance (before revenue decline)	\$64.8
Projected Use of BSR: FY 2026 revenue decline (partial offset with BSR) – <i>one-time sales tax contingency may need other resources including Section 115 trust</i>	-\$6.0
Projected use of BSR: FY 2027	-\$2.0
FY 2027, Project BSR ending (June 2026)	\$56.8M (18.5%)

5. FY 2027 BUDGET DEVELOPMENT GUIDELINES (Attachment A)



1. Structural Balance

Develop a budget that brings ongoing revenues and expenses into alignment for fiscal sustainability over the short, medium, and long-term.



2. One-Time Resources

Allocate one-time resources for **one-time needs only** (e.g., restoration, strategic investments), avoiding commitment to ongoing services.



3. Council Priorities

Review and identify funding needs that directly align with the City Council's existing priorities.



4. Process Redesign

Focus on business process redesign to enhance quality, flexibility, and cost-effectiveness (streamlining, simplifying, reallocating resources).



5. Service Delivery Models

Explore alternative service delivery models, such as partnerships with non-profits or public/private sector groups, to minimize overlap.



6. Analyze Costs

Continue to thoroughly analyze non-personnel, equipment, and contract service costs for **savings opportunities** or realignment with current needs.



7. Revenue Expansion

Explore expansion of existing revenue sources or the addition of new ones, including alignment of existing charges for services and establishing new fees.



8. Augmentations (Net-Zero)

Prioritize resource augmentations, seeking to offset them with reductions elsewhere for **net-zero impacts** whenever possible.



9. Fund Long-Term Liabilities

Continue to prioritize proactively funding long-term liabilities: debt, pension obligations, and **capital infrastructure** in accordance with City policies.



6. RECOMMENDATION

The Finance Committee and Staff recommend the City Council:

Accept the General Fund Long Range Financial Forecast (LRFF) for Fiscal Year 2027-2036 (Attachment A) and the FY 2027 annual Budget Development Guidelines (Attachment B) and direct staff to use this forecast as the starting point for the initiation of the FY 2027 budget.

Next Steps Annual Budget Process

- *Feb 2026:* FY 2026 Mid-Year Budget
- *May 2026:* FY 2027 Proposed Budget



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