

City Manager's Budget Message

May 2, 2023

FY 2023/24 Recommended Budget

Dear Honorable Mayor, Councilmembers, and Sunnyvale Community,

I am pleased to present the FY 2023/24 Recommended Budget and Resource Allocation Plan. The Recommended Budget is balanced in the short and long term and reflects continued strong investments in the City's infrastructure. On the whole, the City's finances are moving in the right direction as the impacts from the COVID-19 pandemic subside. Virtually all revenues have returned or are returning to pre-pandemic levels. Some, including the largest General Fund revenue source, property tax, continue to exceed growth expectations. On the expenditure side, challenges continue as persistent inflation is driving up costs for goods, services, and salaries and benefits. However, strong revenue growth enables the targeted investments in infrastructure necessary to maintain the City's core services for many years to come.

Legal and Policy and Framework

The Recommended Budget and Twenty-Year Resource Allocation Plan reflects the Council's public policies and the related resources needed to implement them. Unlike many other public agencies, Sunnyvale is relatively unique in that it does not budget year-to-year.

Sunnyvale's reputation of strong financial management rests in the community's values expressed through the City Charter and long-established City Council Policies that together require the City to remain fiscally strategic and sustainable. These disciplined laws and policies promote fiscal solvency over the long term, for example:

- 10 Year Balanced Budget Mandate – Sunnyvale voters have mandated a City Charter provision requiring “At least thirty-five days prior to the beginning of each fiscal year, the City Manager shall submit to the City Council the proposed budget as prepared by him/her. Said budget shall be a balanced ten-year budget, reflect a minimum of ten years long-range financial planning” (Article1302);
- 20 Year Resource Allocation Plan Requirement – In addition to voter mandates, City Council Policy 7.1.1 requires decision making focused on long-range implications of current budgeting decisions, with specific focus on the following:
 - A.1.3 A balanced Twenty-Year Resource Allocation Plan shall be presented to the City Council annually.
 - A.2.1 The City shall maintain a long-term fiscal perspective by annually preparing a Twenty-Year Long-Term Financial Plan for each fund. Those funds which account for intergovernmental grants will only include known entitlements.
 - A.2.2 Major financial decisions should be made in the context of the Twenty- Year Long Term Financial Plan.
 - A.2.3 Long term financial planning should enable the current service level provided to be sustained over time through the strategic use of reserves.
 - A.2.4 The Long-Term Financial Plans should be used to communicate the fiscal impact of City decisions to all stakeholders whenever possible.

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- Budget Stabilization Fund Threshold Requirement – City Council Policy 7.1.1 (E.1.4) requires that:

The General Fund Budget Stabilization Fund will be a minimum of 15% of projected revenues for the first two years of the 20-year planning period. Beyond year two, the Budget Stabilization Fund will always have a balance of at least zero.

Although the focus is on the long-term financial picture, ultimately the Council will approve legal appropriations for only the following fiscal year. For FY 2023/24, the Recommended Budget totals \$607.9 M across all funds (\$581.1 M in expenditures, \$26.8 M in contributions to reserves). This includes \$607.9 M in revenues, a \$334.5 M operating budget (8.5% overall increase), and \$170.0 M in projects. Also included is a total of \$26.8 M in contributions to various reserves. The contributions to reserves come primarily from impact fee revenue that is being reserved for future projects, but major tax revenue sources such as property tax and sales tax are outperforming estimates and also contributing to the reserve balance. Additional detail on various funding sources, expenditures, and the use of reserves is included in the Budget Summary section.

The FY 2023/24 Recommended Budget strives to balance the distribution of resources and use of reserves to sustain core operations and important projects. The City alternates years between the operating budget and the projects budget with this year being a projects budget year. One of Sunnyvale's many strengths is the practice of focusing on maintaining a high level of service to our community. Keeping Sunnyvale as a desirable place to live by delivering high quality services that keep us safe and healthy, and provide opportunities to work, learn, and play requires modern and community-responsive infrastructure. The projects included in this Recommended Budget are based on a planning approach that includes detailed and thoughtful facilities master planning, and distribution across ten and twenty years to ensure project delivery resources are sufficient and project completion will be timely.

These investments include:

- Maintaining \$40.8 million in funding for a new Fire Station 2 including a new training center included in the current budget, with the design process currently underway.
- Adding \$15.4 million for the sequential renovation of the remaining fire stations, with the first to begin design in FY 2025/26 and completion of all four by FY 2035/36.
- New funding of the first phase of the Corporation Yard Master Plan with design scheduled to begin in FY 2026/27 and construction in FY 2028/29 for a total of \$21.5 million.
- Setting aside \$15 million to support the construction phase of Civic Center Phase 2 – Main Library.
- An additional \$262.2 million for the Sunnyvale Clean Water Program, with current and increased funding provided through a combination of Federal and State low-interest loans and future anticipated issuance of revenue bonds. This includes \$58 million to complete design and fund construction of the new Clean Water Center building which had been deferred in previous budgets.
- \$8.5 million for the rehabilitation of pond levees at the Water Pollution Control Plant.
- \$65.4 million over twenty years set aside for golf infrastructure renovations funded by Park Dedication Fund revenues in addition to \$2.6 million for golf and greens renovation and \$5.5 million for golf irrigation.

While the Recommended Budget focuses on projects, some operating changes were made to reflect council priorities, and there are many projects that are operating in nature but better captured as projects. Some of these highlights include:

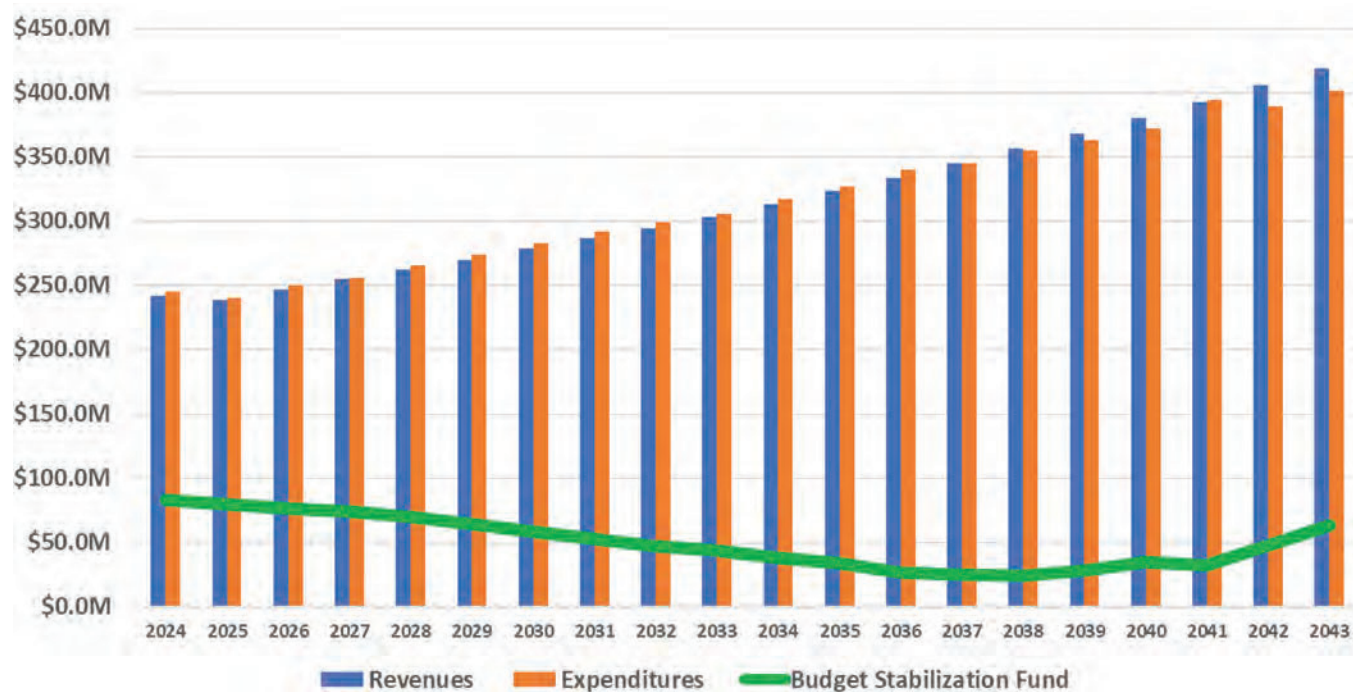
- Funding for the recruitment and training of 72 new public safety officers over the first 10 years of the General Fund, thirty of which come in the first four years. The total allocation increased by \$13.4 million over that period for a new total of \$72.3 million.
- An additional \$1.4 million per year in costs for chemicals at the water pollution control plant. This additional cost is to address recent algal blooms that are impacting the treatment processes.
- One new Civil Engineer to the Special Projects team for delivery of the Clean Water Program and Civic Center Phase II.

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- Establishment of a New Special Projects team dedicated to the delivery of parks projects funded by Park Dedication Fees. The team consists of one Senior Engineer, one Civil Engineer, and \$65,000 per year to provide support for procurement and bidding.

The City's largest fund, the General Fund, is balanced in the first 10 years of the Twenty-Year Plan. However, balancing the General Fund requires the use of reserves until the latter half of the Twenty-Year Plan. This is consistent with the City's past practice and reflects known increased retirement costs in the mid-term, which stabilize over the long term. It is important to note that until retirement costs stabilize, volatility in those costs will continue to be a challenge to manage. The near term addition of just \$1 million in ongoing costs would draw down Budget Stabilization Fund by \$24.2 million by FY 2037/38, the current low point, leaving only \$5.5 million available that year. Therefore, continued fiscal discipline is warranted. The following graph summarizes revenues, expenditures, and the Budget Stabilization Fund Balance.

General Fund Revenues, Expenditures, and Budget Stabilization Fund



Council's Policy Priorities

The Council revisits their priorities annually at the [Council Strategic Planning Workshop](#) to help guide the development of the Recommended Budget. Below is a summary of how this Recommended Budget supports Council's six priorities:

- 1. Civic Center Campus Modernization** – With Civic Center Phase 1 nearing completion, the Recommended Budget includes funding for Phase 2, which involves the Main Library. The Civic Center Master Plan as adopted by Council in September 2018 included a new or renovated Main Library as Phase 2. The proposed library is 118,000 square feet and has an estimated (2017) cost of \$135 million. Work is currently underway on a Feasibility Study, Conceptual Design, and community outreach process. Based on City Council's discussion at the February 2019 Council Strategic Session, this project is targeting the 2024 Election for a potential ballot measure to provide funding.

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- 2. Ability of Infrastructure to Support Development and Traffic** – This budget funds significant traffic and transportation projects over the twenty year plan. \$218 million is planned for pavement rehabilitation and slurry seal, \$4 million for pedestrian lighted crosswalk rehabilitation and replacement, and \$63 million for sidewalk, curbs and gutters.
- 3. Downtown Sunnyvale** – This budget anticipates the benefit of additional Sales Tax revenue from downtown development. The City began seeing some base Sales Tax increases starting in FY 2020/21. The old Macy's site is under construction, which will bring 500,000 square feet of office and 479 apartments over ground floor retail space. Additionally, annual funding of \$40,000 is provided to the Downtown Association through FY 2023/24. This funding is used to supplement other funding sources to support special events downtown.
- 4. Accelerating Climate Action, the Active Transportation Plan and Vision Zero Plan** – Investments are continued for the implementation of the Climate Action Plan, with the total budget for implementation of \$2.3 million. \$1.9 million is also included for new green stormwater infrastructure. Additionally, the new net zero City Hall and the installation of solar facilities at the corporation yard and the SMaRT Station continue to reduce the impact of city facilities on the climate. Projects related to Active Transportation include \$1.8 million for update of the Active Transportation Plan, \$1.6 million for periodic bicycle improvement studies, \$4.1 million for the Evelyn Avenue Multi-use Trail, \$100,000 per year for bicycle and pedestrian education and encouragement, \$7 million for design and permitting work on the Stevens Creek Trail Extension, and \$2.8 million for the East Channel Trail Study.
- 5. Support the Unhoused Community** – This policy priority was during during the 2023 Strategic Planning Workshop. The Recommended Budget begins to address this issue through the addition of a new management position for managing homeless services, as well as an additional \$500,000 in funding to extend the pilot program to provide case management, shelter beds, and encampment cleanups. Over the next year, staff will recruit for the new manager and begin to evaluate options for addressing this issue.
- 6. Equity, Access, and Inclusion** – The Recommended Budget continues funding for this council priority as well as adding new additional resources. These include three years of funding for continuing a series of Sunnyvale Unity events at \$15,000 per year, \$75,000 to conduct an equity, access, and inclusion, community needs assessment, and \$65,000 per year over three years to continue staff training. The City's Sunnyvale Employees for Equity and Diversity (SEED) team has been developing an equity framework and strategic plan which is expected to guide programs for the coming years.

We continuously evaluate our level of investment in these Council priorities and will use creative, low-cost approaches to address them when possible.

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Budget Supplements

For the FY 2023/24 Recommended Budget, five budget supplements are presented for Council consideration. A complete description of each budget supplement is included in Volume I of the FY 2023/24 Budget. Budget Supplement No. 1 provides funding for the Study Issues adopted by Council and placed above the line by the City Manager

Budget Supplement No. 2 outlines potential additions or savings above (or below) what is included in the FY 2023/24 Recommended Budget. This practice was initiated during the FY 2021/22 budget cycle in response to the COVID-19 Pandemic. This year's list, which is shorter than the past few years, includes budget proposals that are not recommended for funding as well as other unfunded programs or projects. It should be noted that any additions should be offset by a corresponding reduction to maintain a balanced budget.

The remaining Budget Supplements reflect the Budget Proposals that were referred to the Recommended Budget by Council at the Study Issues/Budget Proposals workshop.

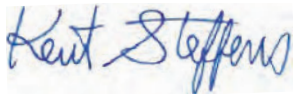
Closing

The past three years have been challenging for our community. However, the strength of our long-term planning and our disciplined practice of maintaining strong reserve balances allowed us to continue delivering core services through the impacts of the pandemic.

The work of Sunnyvale staff continues to be a source of pride. Staff consistently and professionally respond to changing conditions, maintain excellent services, and build community trust. I opened this message by sharing my optimism and excitement about the investments we make in this budget. It strategically rebuilds the infrastructure that our world class services so heavily rely upon. And it completes another year of Sunnyvale's long tradition of thoughtful long-term planning.

In the following pages, the FY 2023/24 Recommended Budget Summary provides greater detail on key components of this budget. For further information, *Volume I: Summary and Operating Budget* includes the 20-year financial plans for all funds as well as operating budgets by department and *Volume II: Projects Budget* presents specific project detail by category.

Sincerely,

A handwritten signature in blue ink that reads "Kent Steffens". The signature is written in a cursive, flowing style.

Kent Steffens
City Manager

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FY 2023/24 Budget Summary Highlights

The FY 2023/24 Recommended Budget totals \$607.9 million and includes all City operations and project expenditures, as well as withdrawals and contributions to the City's reserves. Citywide budgeted expenditures are funded from multiple sources including general taxes and revenues (General Fund), fee supported Enterprise Funds (Water, Wastewater, Solid Waste, Development Enterprise and Golf and Tennis), restricted Special Revenue Funds (Housing, Park Dedication and Gas Tax), grant funding, which includes transportation related grants for capital projects and federal and state workforce grants for employment development, and significant loans and debt proceeds related to the Sunnyvale Cleanwater Program and Civic Center Modernization. Restricted funds make up over half of the budget.

Sunnyvale is a full-service city, providing a host of essential services to the community. Many traditional services (public safety, library, parks, streets, trees) are funded through general taxes from the City's General Fund. The General Fund, which accounts for about 40% of the budget, has proposed expenditures of \$245.2 million in FY 2023/24. The General Fund is balanced over the twenty-year financial plan.

In developing the budget, the City performs a detailed review of operations and projects in alternating years. For the FY 2023/24 Recommended Budget, the focus is on the projects budget. City staff completed a detailed review of existing projects and each department was given the opportunity to propose new projects. More detail about the project budget process is included at the beginning of Volume 2 of this Recommended Budget.

The 2023/24 operating budget for all funds totals \$334.5 million, up \$26.1 million from FY 2022/23. Additionally, the FY 2023/24 Recommended Budget includes several Budget Supplements. Budget Supplements are proposals to supplement services or add new initiatives that require specific Council approval. All Budget Supplements are considered with the City Manager's Recommended Budget. More detail is provided in the "Budget Supplements" section below.

The budget document is organized into two volumes. Volume 1 – Summary and Operating Budget, includes the City Manager's message, the Budget Summary and Overview, Budget Supplements, twenty-year financial plans for each of the City's funds, and the City's Department Operating Budgets. Each of the sections for the twenty-year financial plans is preceded by a narrative that describes each plan. Each Department Operating Budget contains a narrative about the overall services the department provides, major budget highlights, and performance indicators tied to the City's General Plan goals. Volume 2 – Projects Budget, contains the City's projects. This volume is organized into sections by project category (e.g. Traffic and Transportation Projects). Each project section is preceded by a narrative and highlights of major projects in the section. Additionally, each project information sheet includes a project scope, fiscal impact, and the relevant General Plan goals.

City's Budget and Resource Allocation Plan

There are three (3) key elements to the City's budget and resource allocation plan that provide the financial picture of the City for both the short and long term: revenues, expenditures, and reserves. The following sections discuss the highlights, key assumptions and changes included in this Adopted budget for each of these elements. It is important to note these elements are budgeted into specific funds, such as the Park Dedication Fund and the Gas Tax Fund, primarily to ensure that revenues restricted to specific purposes can transparently be tracked as spent for those purposes. While the discussion here is not organized by fund, this important structure is reflected in the budget document with the presentation of twenty-year financial plans for each of the City's funds. Detailed discussions about revenues, expenditures, and reserves by specific fund are included at the beginning of each financial plan section.

I. City Revenues and Resources

The City relies on many sources of revenues and the strategic use of reserves to fund services to the community at a stable and sustainable level. The largest revenue categories are taxes and service fees, followed by federal and state revenues (e.g., gas tax) as well as bond and loan proceeds being used to fund the Sunnyvale Cleanwater Program.

Taxes

Taxes, imposed by a government for the purpose of raising revenue to support governmental activities, are distinct from fees in that a tax does not need to be levied in proportion to the specific benefit received by a person or property. Almost all of the City's tax revenues are general taxes received by the General Fund, the primary general purpose fund of the City. There are several significant exceptions, specifically in relation to transportation funding, which are discussed in greater detail in this overview. Taxes account for about 85% of revenues in the General Fund, supporting many of the City's most visible and essential services such as police, fire, road maintenance, libraries, and parks maintenance. Figure 1 presents recent revenues received and projections for the top tax revenues.

Figure 1 – Top Tax Revenues

Revenue Source	2020/21 Actual	2021/22 Actual	2022/23 Budget	2022/23 Revised Projection	2023/24 Proposed Projection
Property Tax	\$101,296,792	\$113,499,852	\$110,227,140	\$114,315,019	\$117,633,140
Sales Tax	26,089,903	35,801,316	29,876,069	34,915,338	34,286,478
Transient Occupancy Tax	5,192,090	10,584,492	11,893,731	14,125,965	17,390,205
Utility Users Tax	8,590,351	8,594,301	9,021,519	9,500,000	9,697,950
Gas Tax	3,400,604	3,608,091	4,447,916	3,975,339	3,975,310
RMRA Funds ¹	2,901,337	3,109,280	3,506,434	3,388,440	3,761,168
Measure B Funds ²	2,281,526	1,873,207	3,511,869	13,181,216	3,511,869
Construction Tax	2,454,170	5,548,089	4,072,154	4,072,154	4,333,550
Total Top Tax Revenues	\$152,206,773	\$182,618,628	\$176,556,832	\$197,473,471	\$194,589,670

1. Road Maintenance and Rehabilitation Funds (Senate Bill 1)
2. Measure B is a half cent County-Wide sales tax for transportation funding.

The current year's projections are also updated during budget development. Based on year-to-date figures, FY 2022/23 General Fund revenue (excluding the sale of property) will increase by approximately \$14.9 million over the prior fiscal year as a result of the recovering local economy and strong property value growth.

Property Tax revenue has experienced significant growth over the past three fiscal years. Despite a drop from the peak valuation in the second quarter of 2022, the median Sunnyvale home sale price remained strong at \$2.1 million as of the first quarter of 2023 and the overall assessed property value increased 8.3% for FY 2022/23, which is reflected in the FY 2023/24 forecast. For FY 2023/24, the assessed property value is currently projected to increase by 3.3%. However, the rise of interest rates have begun to temper growth and will continue to be monitored closely.

The City is also the recipient of excess Educational Revenue Augmentation Funds (ERAF). ERAF is local property tax revenue that is shifted to public school systems in each county to ensure a baseline level of funding. When the county auditors determine that the fund has enough money to meet the minimum state funding requirements for its public schools and community colleges, the remaining funds are returned to local governments. In both FY 2022/23 and FY 2023/24, the City is projecting \$7.1 million based on the County's estimate.

Sales Tax, the City's second largest tax revenue source, has continued to recover and is approaching pre-pandemic levels. The largest segment of activity in the City's sales tax base is business-to-business sales, which have been highly volatile. However, due to high inflation and post-pandemic retail recovery, FY 2023/24 Sales Tax revenue forecast at \$34.3 million. The City projects Sales Tax to continue to grow slowly each year with some of the anticipated growth as a result of the CityLine project development.

Transient Occupancy Tax (TOT) revenue is the City's third largest revenue sources of the General Fund. In 2018, voters approved Measure K, which updated the TOT ordinance and increased the TOT from 10.5% to 12.5% as of January 1, 2019. This change brought in strong TOT returns through the third quarter of FY 2019/20 before the COVID-19 Pandemic hit. Since then, TOT revenue has been significantly impacted. As a result, the TOT projection is \$17.4 million in FY 2023/24 and is still substantially lower than the peak of \$21.2 million received in FY 2018/19. Since the hotel industry continues to experience some of the deepest economic impacts, TOT is expected to recover slowly over several years and as such, staff has adjusted the timing of projected new hotels to reflect only developments actively under construction due to this economic uncertainty.

Short-term rentals are also subject to TOT and saw a decline due to the Pandemic. The City received almost \$700,000 in the short-term rental revenues in FY 2018/19, which dropped to about \$265,000 in FY 2020/21. While this segment is also recovering, this relatively new industry and the evolution of related policy and legislation results in a moderated revenue estimate of \$559,000 in FY 2023/24.

Utility Users Tax (UUT) revenue, generated from the sale of electricity, telecom services and gas, is forecasted for slow growth over the long-term. UUT has shown stagnation over the past several years. While the City's modernization of its UUT ordinance in November 2016 resulted in revenue growth, it has been offset by decreases in UUT revenue from telecom services. This is primarily due to the increasing popularity of streaming services, which are not subject to UUT. Additionally, although development activity is growing the base, this growth has been substantially offset by increases in energy efficiency, resulting in modest growth in revenue for gas, and electricity usage.

Gas Tax comes from gasoline exercise taxes, levied as a flat rate per gallon sold. The tax is largely based on volume sold and not on the price of gasoline. While fuel consumption was suppressed due to a sharp reduction in commuting during the Pandemic, gas sales have rebounded again and the City is projected to receive \$4.0 million in FY 2023/24. Fuel taxes are collected each month for sales occurring in the prior month and then allocated according to statute.

RMRA funds come from the Road Repair and Accountability Act (SBI) passed by the State in 2017. This allocates 50% of a new gas tax to cities and counties, after a series of specific program cost appropriations. City apportionments are based on population. These funds must be used for projects that include: road maintenance and rehabilitation, safety projects, railroad grade separations, traffic control devices, complete street components, active transportation purposes, pedestrian and bicycle safety projects, transit facilities, and drainage and stormwater capture projects in conjunction with any other allowable project. If a city or county has an average Pavement Condition Index that meets or exceeds 80, the city or county may spend its RMRA funds on transportation priorities other than these types of projects discussed above. For FY 2023/24, an apportionment of \$3.8 million is projected, though it is anticipated that this projection will need to be updated based upon estimates in the release of the State's revised budget in May.

2016 Measure B is a 30-year half-cent countywide sales tax to enhance investment in transit, highways, expressways and active transportation. Measure B funds are restricted for transportation purposes. Funds are distributed based on population through a reimbursement basis and also to specific projects. The Recommended Budget includes an estimated \$3.5 million in baseline Measure B funds for FY 2023/24. While unspent amounts from prior years may be carried over to future years, the City plans to use the funds for current projects when possible.

Construction Tax revenues resumed along with the strong development activity in the City beginning in FY 2021/22, after slowing in FY 2020/21 due to the pandemic that stalled or cancelled some development. To that end, the FY 2023/24 Budget estimate is \$4.3 million and assumes that new development activity will continue the growth experienced in the current year.

Service Fees

Service fees are the City's largest source of revenue. A diverse set of fees are charged to recover all or a portion of the City's costs for providing a service or access to public property, or for mitigating the impacts of the fee payer's activities on the community. Intended for cost recovery, a fee may not exceed the estimated reasonable cost of providing the service for which the fee is charged. Due to this requirement and legal restrictions related to their expenditure, many of the City's fees are accounted for in separate funds. By far, the largest source of fee revenue comes from the provision of water, wastewater, and solid waste collection services. The proposed increases in utility rates are discussed below, as well as highlights in other fee categories.

Figure 2 – Top Service Fee Revenues

Revenue Source	2020/21 Actual	2021/22 Actual	2022/23 Budget	2022/23 Revised Projection	2023/24 Proposed Projection
Golf Fees	4,295,471	4,540,101	4,421,031	4,239,777	4,358,450
Development Enterprise Fees	14,470,190	23,903,835	19,049,929	23,323,535	21,596,949
Solid Waste Fees	49,741,885	52,351,916	55,658,742	54,720,188	58,320,364
Wastewater Fees	44,654,833	47,393,693	47,228,819	48,904,704	53,306,127
Water Fees	57,379,901	54,004,985	54,236,788	52,542,740	55,535,602
Total Top Tax Revenues	170,542,280	182,194,530	180,595,309	183,730,944	193,117,492

Golf Fees support the Golf and Tennis Fund, and after years of operating at a deficit, is currently a self-supporting enterprise fund. This has been a strategic focus for Council, and staff has made progress in restructuring activities to reduce expenditures. During the pandemic, golf was one of the few activities that was allowed under the safety restrictions, resulting in higher than anticipated revenues. While staff continues to monitor progress, transfers from the General Fund to the Golf and Tennis Operations Fund will be required until a permanent plan is in place.

Utility Rates provide funding for the City's three self-supporting utility funds: The Water Supply and Distribution Fund, the Solid Waste Management Fund, and the Wastewater Management Fund. Each year, staff analyzes the current condition and long-term outlook for all three funds. The analysis includes a review of fund balances; state and federal environmental requirements; revenues; anticipated capital, infrastructure, and operational requirements; and a detailed inspection of significant expenditure areas. The results of this analysis lead to proposed adjustments to rates that will generate the revenues necessary to meet planned expenditures. Through the long-term planning model, staff attempts to keep utility rates as stable as possible with modest increases annually. The drought conditions over the previous decade have been impacting water rates, and plan to draw on reserves to moderate the rate increase. Wastewater rates are increasing to support the replacement of the City's aging Water Pollution Control Plant (WPCP). Solid waste rates are increasing due to an increase in new services to maintain compliance with SB1383. The overall recommended increase for FY 2023/24 is shown below, in Figure 3, with a comparison to the original projection made in the FY 2022/23 Adopted Budget:

Figure 3 – Utility Rates

Utility	Original Projection	Adopted FY 2023/24	Change in Percentage Points
Water	4.0%	4.0%	0.0%
Wastewater	3.0%	9.0%	6.0%
Solid Waste	5.5%	6.0%	0.5%

Each of the utility enterprises has its own unique pressures that drive rate adjustments. As the FY 2023/24 Adopted Budget is a capital budget cycle, each utility updated operating budgets for the two-year budget cycle in the prior fiscal year.

In the water utility, the two drivers affecting rates are purchased water and increased infrastructure needs. Extended drought conditions are resulting in increased wholesale water rates and lower water sales. The long-term plan anticipates changes to rates charged by the City's wholesalers, which account for most of the water supplied to the City. The San Francisco Public Utilities Commission (SFPUC) rates will increase 11.6% in FY 2023/24, and Valley Water (formerly Santa Clara Valley Water District) plans an increase of 15%. The financial plan calls for using the rate stabilization reserve to moderate rate increases over the next ten years, enabling the fund to absorb larger than usual rate increases from the wholesale water providers.

As with all utilities, there are fixed costs to operate the water system that are not based on the volume of water delivered. These include large capital needs in the fund, mainly associated with pipe, tank, and well replacements and rehabilitation, but the age of the system also required modest requests for additional equipment and contract services needed to maintain the system. The Recommended Budget includes projects over twenty years, the most significant of which is for water pipe and main replacements.

Wastewater rates are rising, driven primarily by costs associated with planned improvements to the City's wastewater collection and treatment system, and stricter regulatory requirements. The main driver of rates in the Wastewater Management Fund is the need to replace the City's aging wastewater treatment plant, which will cost approximately \$1.1 billion over twenty years. The rates take into account the debt that the City has and will issue to fund the project over many years. Annual debt service is projected to be \$8.4 million in FY 2023/24 and will increase as debt is matured over the twenty-year financial plan. By the end of the twenty-year plan, about \$37.3 million in annual debt service costs are expected. It is notable that the City received \$429 million in State Clean Water Revolving funds and up to \$220.6 million in Water Infrastructure Finance Innovation Act (WIFIA) funds for the project, which both came at a significantly lower rate than traditional municipal bonds.

Solid waste rates are increasing for FY 2023/24 due to numerous service additions, such as the expansion of food scraps and yard waste recycling to additional customers. These costs were included in the franchise agreement with Bay Counties Waste Services (dba Specialty Solid Waste & Recycling). These service changes are necessary to meet diversion goals and maintain compliance with SB 1383. Larger than average increases will be seen annually in the short term as more services are added. Solid waste rates also include the costs of operating and maintaining the Sunnyvale Materials Recovery and Transfer Station (SMaRT Station®). These costs are shared with Mountain View proportionally by the amount of recyclable material processed. Palo Alto is no longer a partner in the SMaRT Station® as of January 1, 2022. As a result, the proportional share of expenses has increased for the two remaining partners.

Development-Related Fees include revenue from the majority of fees related to development activity (e.g. plan check fees, inspection fees and permit application fees). A separate fund called the Development Enterprise Fund accounts for these fees and related expenditures. In addition to ensuring full cost recovery, the fund allows for the segregation of these revenues with the ability to build and draw from the reserve. This is especially important as development-related fee revenues are highly volatile and, as large development projects take many years to complete, expenditures related to specific fees can occur in later fiscal years than when the revenue was collected.

Development related revenues are projected to be stable in FY 2023/24 and for the foreseeable future. Development-related activity will be closely monitored, and projections will be re-assessed each fiscal year.

Development Impact Fees are imposed to mitigate the impact of a development on the community. These four (4) fees include: Housing Mitigation Fees, Park Dedication fees, Sense of Place fees, and Transportation Impact fees. Impact fees have strict requirements, set by state government code, that require fees to be roughly proportional to the impacts of the project and imposed for purposes related to the impacts of the project. Therefore, each of these fees is accounted for separately in its own fund or sub-fund. With development activity in the City at high levels, revenue from these fees has been significant.

Figure 4 – Top Impact Fee Revenues

Revenue Source	2020/21 Actual	2021/22 Actual	2022/23 Budget	2022/23 Revised Projection	2023/24 Proposed Projection
Housing Mitigation Fees	38,304	37,666,107	27,586,461	3,509,180	15,550,264
Park Dedication Fees	4,203,104	21,785,663	25,437,302	37,170,085	12,872,241
Sense of Place Fees	1,821,552	1,058,384	457,239	4,038	1,132,395
Transportation Impact Fees	(146,192)	10,481,569	5,802,208	2,461,028	4,677,569
Total Top Impact Fee Revenues	5,916,769	70,991,723	59,283,210	43,144,331	34,232,469

Based on year-to-date figures and approved projects, staff estimates collecting \$43.1 million in FY 2022/23 and projects \$34.2 million in FY 2023/24. Moving forward, development activity will be closely monitored, and projections will be revised in following fiscal years based on the City's future economic outlook for development. The revenue projected above last year's budget is primarily appropriated in projects or reflected as increases to fund reserves that will be dedicated to projects.

Other Revenue Sources

The remaining revenue sources are varied, including franchises, federal and state grants, rents, fines, licenses, and interest income. There are also one-time revenues in this category such as bond proceeds, and sale of property. Highlights of other revenue sources are discussed below.

Debt Financing is a tool for managing cash flow when large, one-time outlays are required, generally for large infrastructure projects.

The City currently carries debt for both the Water and Wastewater Systems, and the Civic Center Phase 1 project. All of the currently held debt is funded by rate revenues or lease payments paid by various funds. The City does not maintain any general obligation debt (commonly called "GO Bonds") and continues to maintain the highest issuer credit rating issued by Standard & Poor's (AAA) and Moody's (Aaa). The City also has two State Revolving Fund loans totaling approximately \$429 million for the Sunnyvale CleanWater Program and a Water Infrastructure Financing and Innovation Act loan with the Federal Environmental Protection Agency. These loans provide cost effective funding for the first two significant phases of the project, construction of new primary treatment facilities and headworks and construction of secondary treatment facilities.

Federal and state grants are important sources of funding for many of the City's services. The Workforce Innovation and Opportunity Act grant serves as the main source of funding for NOVA, which offers job placement and training services for Santa Clara and San Mateo Counties. The City also receives an annual allocation of Community Development Block Grant (CDBG) and HOME grant funds, which are used to help support affordable housing and rental assistance programs. The FY 2023/24 Recommended Budget projects \$13.2 million in federal and state grants, but the City will likely receive significantly more in competitive grants not included in the budget due to uncertainty.

Sale of Property includes one-time proceeds from the sale of property. These revenues go to the fund that owned or purchased the property. By City policy, one-time revenues are spent on one-time expenditures. As such, in the General Fund, sale of property revenue is placed in the Capital Improvement Reserve or transferred to the Infrastructure fund. There are no plans for sale of property in FY 2023/24.

II. City Expenditures

City expenditures fall into three broad categories: operating, projects and equipment, and debt service.

Operating Expenditures

City departments are extremely integrated and highly reliant on each other to deliver services and achieve the goals and results established by the City Council. The departments are:

- Office of the City Attorney
- Office of the City Manager
- Community Development Department
- Environmental Services Department
- Finance Department
- Human Resources Department
- Information Technology Department
- Library and Recreation Services Department
- NOVA Workforce Services Department
- Department of Public Safety
- Department of Public Works

Citywide Operations

Employee Compensation

As a service delivery organization, the majority of operating expenditures are related to salaries and benefits costs for personnel. Managing total compensation costs is a key component of long-term financial sustainability.

The Recommended Budget addresses this in several ways. The City accounts for pension costs in a separate Employee Payroll & Benefits Fund. In FY 2020/21 CalPERS achieved a 21.3% return on its investments, significantly exceeding its goals. However, in FY 2021/22 CalPERS experienced a 7.5% loss, well short of its stated goal of 6.8% growth and therefore virtually eliminating all of the prior year gain. Due to this volatility, the City is closely monitoring current year returns. The FY 2023/24 Recommended Budget assumes returns short of the 6.8% goal for the current fiscal year and that longer term pension costs will reflect this shortfall.

Additionally, the City holds a pension trust within a subfund in the Employee Payroll & Benefits Fund to account for its activities. Because those funds will grow at a higher projected earnings rate than regular City reserves, which are restricted by law as to how they can be invested, over time the additional funds can help stabilize or fund future pension cost increases. The City works with the City's actuary to refine the funding level and the timing of transfers into and out of the trust fund that would be most advantageous to reduce the unfunded pension liability and create budget stabilization. The City contributed \$10.0 million to the trust fund as of June 30, 2022 and will contribute another \$3.5 million by June 30, 2023. In the FY 2023/24 Recommended Budget, an annual funding commitment of \$1 million is budgeted for the next five years. The City is anticipated to start using the pension trust fund to offset pension payments starting FY 2028/29 and estimated to have \$31.4 million from the trust to pay for pension liabilities.

The Recommended Budget also includes updated assumptions on health and other insurance costs and salaries. A tightened and highly competitive labor market is creating stiff competition for talent. Just as the City doesn't project revenues under the assumption of a peak economy, annual increases in salaries are not projected at peak levels. This budget includes resources to maintain competitiveness in the short term, while moderating salary growth in the long term.

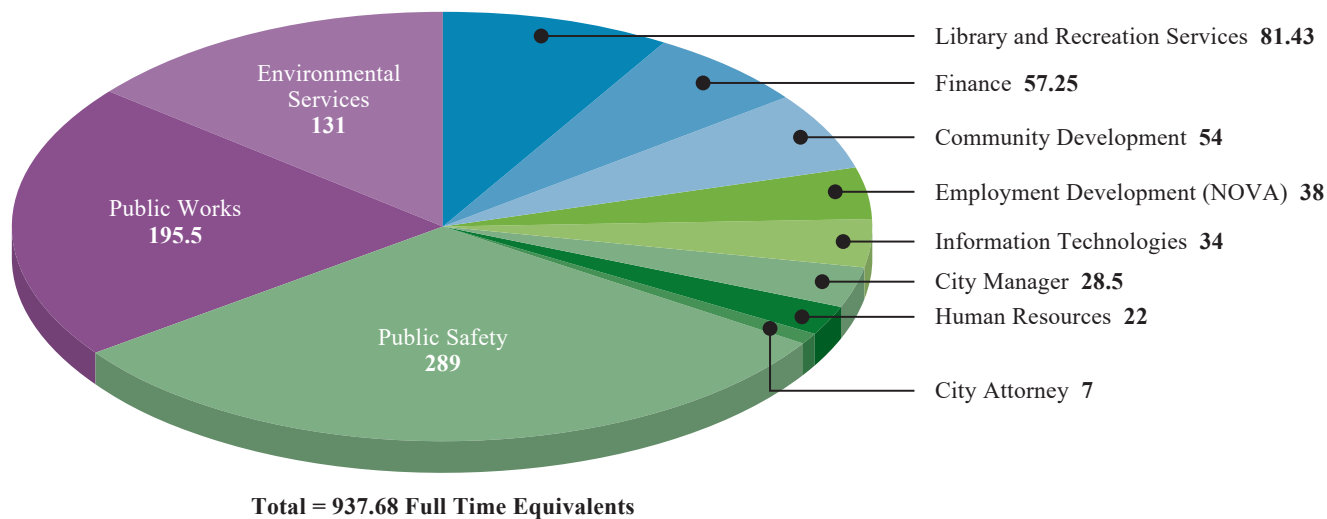
Changing demographics have reduced health insurance costs in prior years. Fewer employees are insuring families as younger employees take advantage of multiple household members' insurance plans and have fewer dependents. However, insurance rates are expected to increase sharply over the next three years. Similar to pensions, the City carries reserves for insurance rate volatility and uncertainty.

Total compensation in the General Fund (salaries, pensions, and insurance costs) is projected to rise by approximately 8.0% or \$13.0 million in FY 2023/24 when compared against the FY 2022/23 Budget, primarily due to negotiated wage and benefit increases. The City will be closely monitoring total compensation costs in the coming years, with an emphasis on providing competitive compensation while managing long-term liabilities and maintaining a structurally balanced budget.

The Recommended Budget includes 937.68 Full Time Equivalent (FTE) Employees. Since adoption of the FY 2022/23 Budget, the City has increased the number of FTEs by a net of 1.5 positions.

Figure 5 summarizes the changes in the budget for each department:

Figure 5. Full-Time Equivalents*



As this year is the second year of an operating budget cycle, minimal changes have been made to non-personnel costs in the budget. Significant operating changes are noted in the Budget Highlights section of each Department's narrative.

Projects Budget

This year is the second year of the two-year budget cycle, so the primary focus is on capital projects. The City categorizes projects into three broad categories: Capital, Infrastructure, and Special. Capital projects are efforts to construct new or expanded facilities or infrastructure. Infrastructure projects rehabilitate existing infrastructure. Special projects are efforts like special studies or initiatives. In this projects budget cycle, we reviewed all current projects, and proposed a group of new projects to support the City's infrastructure efforts.

Sunnyvale's projects budget is a complex document involving four separate and distinct categories of projects: capital, infrastructure, special, and outside group funding. Totaling over \$2.2 billion over twenty years, the projects themselves are budgeted and accounted for in various funds, most notably the General and Gas Tax Funds, the Capital Projects and Infrastructure Funds, and the Utility Funds. These projects are separated in this Recommended Budget into fourteen categories:

- Traffic and Transportation
- Downtown
- Housing
- Water
- Governance and Community Engagement
- Outside Group Funding
- Wastewater
- Clean Water Program
- Public Safety
- Community Development Block Grant (CDBG)
- Parks and Recreation
- Library
- Solid Waste
- Administrative Facilities

Each of these categories carries a portfolio of projects that address the subject area. As part of the annual budget preparation process, City staff reviewed and updated all projects, and identified new projects for inclusion.

Figure 6 shows the year over year change of the total 20 year project budget by fund.

Figure 6. Twenty Year Project Budget Change by Fund

Fund	FY 2022/23	FY 2023/24	Increase/Decrease
General Fund	200,100,565	238,360,802	38,260,237
Combined Housing Fund	1,133,572	16,891,065	15,757,494
HOME Fund	2,000,000	–	(2,000,000)
Redevelopment Housing Fund	2,500,000	2,250,000	(250,000)
CDBG Fund	7,399,177	6,094,703	(1,304,474)
Gas Tax Fund	63,296,604	62,768,806	(527,798)
Capital Projects Fund	34,274,444	25,587,069	(8,687,374)
Water Fund	125,029,071	117,828,343	(7,200,728)
Wastewater Fund	731,206,265	1,016,599,099	285,392,834
Solid Waste Fund	53,883,803	36,734,540	(17,149,263)
General Services Fund	12,184,267	23,767,453	11,583,185
Infrastructure Fund	41,423,322	88,666,705	47,243,383
Parking District	1,395,910	1,403,058	7,148
Park Dedication Fund	178,467,460	160,917,707	(17,549,752)
Road Maintenance & Rehab Account Fund	71,986,140	101,063,993	29,077,853
VRF Local Road Improvement Program Fund	23,431,995	18,969,620	(4,462,375)
Measure B Fund	78,233,911	275,915,972	197,682,060
Total*	1,627,946,504	2,193,818,935	565,872,431

* Totals as of April 2023

Projects Budget Highlights

Sunnyvale Clean Water Program

The Sunnyvale Clean Water Program will renovate the City's aging Wastewater Pollution Control Plant, which serves residents, businesses and industries in the City of Sunnyvale. It includes the renovation of existing facilities, as well as construction of some new facilities to replace existing infrastructure that is in too poor of a condition to rehabilitate. The program is planned as a series of design and construction projects over the next twenty years in various phases, and some project expenditures beyond the twenty-year horizon. The first two phases are fully underway. The Program is budgeted across multiple projects with a total cost of over \$1.1 billion over the twenty-year planning period, which includes an additional \$262.2 million added in the FY 2023/24 Recommended Budget.

To fund these projects, the City was able to secure up to \$220.6 million in Water Infrastructure Finance Innovation Act (WIFIA) loans through the Environmental Protection Agency and a total of up to \$429.2 million in funding from the Clean Water State Revolving Fund (CWSRF) through the California State Water Resources Control Board. Both of these programs offer interest rates and repayment terms that are more favorable to the City than other financing sources. Financial risks remain from potential unbudgeted increases in the cost of construction, as well as stricter regulatory requirements and rapidly aging infrastructure that may fail early.

Civic Center Modernization/Administrative Facilities Projects

The City has been actively planning to modernize the Civic Center campus since early 2015. Buildings at the Civic Center are in need of renovation or replacement. Phase 1, which includes City Hall and a Public Safety Emergency Operations Center Addition and Renovation, is nearing completion. The new City Hall, a modern and innovative 119,874 square foot, four story building, was completed in March 2023. It was designed to be Net Zero in energy use and Certified LEED Platinum. The two-story, 15,002 square foot Emergency Operations Center is LEED Gold and all electric (except for back-up generators). The final steps in Phase 1 involve the demolition of the old buildings and the conversion of approximately 6 acres of open park space, including a Civic plaza and outdoor amphitheater, with estimated completion scheduled for FY 2023/24.

Phase 2 of the Civic Center Master Plan adopted by the City Council in September 2018 includes a new Main Library building. The FY 2023/24 Recommended Budget sets aside \$15 million to support this phase of the project.

Additionally, while not part of the main Civic Center campus, the budget also funds a total of \$21.5 million for the first phase of the Corporation Yard Master Plan with design scheduled to begin in FY 2026/27 and construction beginning in FY 2026/27. The FY 2023/24 Recommended Budget maintains \$40.8 million in funding to build a new Fire Station 2, which includes a new training center, and also adds \$15.4 million for the sequential renovation of the remaining fire stations, with the first to begin design in FY 2025/26.

Parks and Recreation Projects

Parks and Recreation projects are funded by Park Dedication Fees. These fees may be used to pay for developing new or rehabilitating existing neighborhood or community parks or recreational facilities. The FY 2023/24 Projects Budget reflects a continuation of park projects with updated labor and construction costs. The Recommended Budget has \$162.2 million in park and recreation projects, which includes an aggregate of \$74.3 million in various projects over the next twenty years for golf infrastructure renovation.

Traffic and Transportation Projects

Maintaining and improving our transportation infrastructure is critical to ensuring livable local communities, balancing housing and jobs, and supporting economic development. Much of Sunnyvale's transportation infrastructure is old and requires rehabilitation and modernization. The City has made significant progress over the last several years addressing traffic and transportation needs. We are actively involved in countywide planning efforts. We also leverage federal and state funds, where possible, to fund many of these very expensive projects.

This Recommended Budget includes \$132.3 million in funding for the Caltrain Grade Separation at Mary and \$43.3 million for Sunnyvale Avenue as well as \$10 million for the Bernardo Avenue Undercrossing. The City also continued its investment in both pavement and sidewalk, curb, and gutter rehabilitation. Sunnyvale is leveraging Measure B funds, SB1 Funds, and traditional General Fund, Gas Tax, and Vehicle Registration Fee funding sources for a total investment of \$549.1 million over twenty years.

Water Distribution and Sewer Collection Infrastructure

In addition to the Sunnyvale Clean Water Program, the City also has projects to maintain and rehabilitate our aging water distribution and sewer collection infrastructure. Funded by revenues from utility rates, these projects ensure that our community receives a clean and reliable water supply. They also ensure that our sewer system safely and sustainably transports sewage to the Water Pollution Control Plant. The Recommended Budget includes \$142 million over twenty years in water system projects and \$96.8 million in wastewater system projects not related to the Sunnyvale Clean Water Program.

Public Safety

With this Recommended Budget, the City continues significant investments in public safety. The budget includes funding for the recruitment and training of 72 new public safety officers over the first 10 years of the General Fund, thirty of which come in the first four years. The total allocation increased by \$13.4 million over that period for a new total of \$72.3 million.

Budget Supplements

There are eleven Study Issues included in Budget Supplement No.1 totalling \$1,188,000 to be considered for funding. Nine of the eleven Study Issues are funded by the General Fund for a total impact of \$990,000, with the remaining two funded by the Technology and Communications Services Sub-Fund of the General Services Internal Service Fund.

Budget Supplement No. 2 outlines potential additions or savings above what is included in the FY 2023/24 Recommended Budget. While no action was required, the City Council will discuss these items during the Budget Workshop on May 18, 2023.

Budget Supplements 3, 4, and 5 reflect Budget Proposals that were referred to the Recommended Budget by Council.

Unfunded Needs

The list of unfunded needs is intended to assist the City in establishing funding priorities in a larger and long-term context. The following list enumerates known areas that are unfunded or underfunded. These issues all require additional scoping to identify. It is important to note this list is dynamic and will change with each budget cycle and as the City identifies new needs or funds items on the list. Progress has been made, most significantly the Recommended Budget includes funding for the renovation or replacement of all fire stations as well as the first phase of the corporation yard renovation.

Unfunded Projects Listing

Short Description
Community, Economic & Workforce Development
Transportation, Streets and Infrastructure
Transportation Strategic Plan Projects
Active Transportation Plan
Traffic Signal Infrastructure Replacement
Implementation Sidewalk Repair
Street Maintenance (additional to maintain PCI)
Environment and Sustainability
Climate Action Plan Program Funding
Water Infrastructure
Wastewater Collection Infrastructure
Stormwater Collection Infrastructure
Stormwater Program Funding
Library, Community Services & Public Facilities
Civic Center Modernization
Corporation Yard Modernization
Golf Building Replacements
Golf Course Infrastructure
Work order and Asset Management Systems
Evidence Storage

III. City Reserves

The backbone of the City's financial planning process is the Twenty-Year Resource Allocation Plan. This planning document provides the framework to maintain a structurally balanced budget by requiring financial discipline in making policy and service level decisions. Reserves are a key component of the financial plans. Various reserves are maintained within each plan consistent with best practices. While many organizations have reserves, the City's strategic and disciplined use of reserves is unique and more active than a typical city. The City maintains reserves for different purposes; some are restricted in use while others are available for a variety of priorities. Examples of restricted reserves include debt service reserves or reserves of special revenues. Unrestricted reserves are used strategically over the twenty-year planning period to balance each fund. The City plans to increase or decrease reserve levels as business and economic cycles pass, allowing stable and consistent levels of service. This is especially critical in periods of revenue volatility. Reviewing reserves over a long period forces policymakers, staff, and the community to think carefully before adding services that must be sustained through growing and recessionary economic periods.

In the General Fund, the unrestricted reserve is the Budget Stabilization Fund. Disciplined and strategic use of this reserve allowed the City to weather the great recession and the COVID-19 Pandemic and is helping to strategically restore services in a planned way to ensure sustainability over the long run. Most significantly, in the past several years, the reserve helped manage the significant increase in projected pension costs. In this Recommended Budget, the reserve is stable across the twenty-year plan reaching a low point of \$24.2 million in FY 2037/38 and then growing over the remainder of the twenty-year plan.

In the utility funds, the use of the Rate Stabilization Reserves allows for the measured increase of rates to cover increasing costs, such as wholesale water costs and tightening regulations on wastewater discharge. This reserve also allows the City to incrementally increase rates to the level needed to support the replacement of the WPCP.

Each major fund also carries large contingency reserves for emergencies such as natural disasters. Reserves also allow the City to undertake projects that may be more expensive than estimated or absorb unanticipated operating costs. In all cases, reserves are one of the City's most critical tools to achieve and maintain financial sustainability.

IV. Public Engagement on the Budget

The City Council engages the public on budget development through several avenues. The most significant is the Council's Strategic Workshop each year to discuss Council Policy Priorities. Currently, the Council Policy Priorities are:

- Civic Center Campus Modernization
- Ability of Infrastructure to Support Development and Traffic
- Accelerating Climate Action, the Active Transportation Plan and Vision Zero Plan
- Support the Unhoused Community
- Downtown Sunnyvale
- Equity, Access, and Inclusion

Early in the calendar year, Council receives an update on the current status of staff's progress on Council Policy.

Priorities and provides further direction. In that meeting, public input is sought and direction is given that affects resourcing of each of the Council's priorities.

The Study Issues and Budget Proposals process is another key piece of public engagement on the City's budget. A study issue is a topic of concern that may result in new or revised city policy. City Council and staff use a formal study issue process to identify, prioritize and manage the review of these topics during each calendar year. A budget proposal is a proposal to add a new service, eliminate a service or change the level of an existing City service, including possible service reduction or elimination. Council holds an annual workshop to discuss Study Issues and Budget Proposals, and makes a decision on how to move forward and if they should be referred to the Recommended Budget for funding consideration.

Lastly, the budget itself goes through a public and transparent process. First, after delivery of the Recommended Budget the City Council holds an all day workshop to go through a detailed review of the Recommended Budget. At the workshop, there is a public comment period, and the Council has the opportunity to make changes to the budget prior to the official public hearing. Prior to the workshop, many of the City's boards and commissions review the Recommended Budget to provide feedback to Council as well. In early June, the City Council holds a noticed official public hearing on the

Recommended Budget. No action is taken, but additional changes may be made. Then, a final public hearing is held to adopt the budget. At both these hearings, the public has opportunity to provide input.

Conclusion

The City's continued discipline in crafting balanced budgets enables us to anticipate and respond to the evolving needs of our community. We are strategic in advancing the City Council's goals and the services so highly valued by residents, all while safeguarding the City's long-term financial health. While more work is ahead of us in the coming years, we are confident this budget sets us on a sustainable path to respond to future needs.

In closing, we would like to thank our City Council for its dedication to advancing the strategic priorities which guide our budget development process. The preparation of this budget was also made possible by the collaborative efforts of our Executive Leadership Team and City staff. Thank you all for your commitment and hard work in preparing this budget.