

2016-2017 MID-YEAR BUDGET REVIEW

STATUS OF GENERAL FUND EXPENDITURES

OVERVIEW

General Fund expenditures through December totaled \$516.3 million, or 37.3% of the total 2016-2017 Modified Budget. This represents a decrease of \$10.7 million, or 2.0%, from the December 2015 level of \$527.0 million. Encumbrances totaling \$55.5 million were \$3.9 million (7.5%) below the December 2015 level of \$51.7 million. Expenditures and encumbrances through December of \$571.8 million constituted 41.3% of the total Modified Budget (including reserves) of \$1.4 billion; without reserves of \$137.3 million, expenditures and encumbrances constituted 45.8% of the total Modified Budget. The following chart displays the year-to-date expenditures (excluding encumbrances) compared to the prior year, by category.

2016-2017 General Fund Expenditures through December (\$ in Thousands)

Category	Current Budget	YTD Actual	% of Budget	Prior Year % of Budget
Departmental Expenditures				
Personal Services	\$ 738,935	\$ 339,152	45.9%	46.8%
Non-Personal/Equipment	119,908	40,950	34.2%	34.8%
Other Departmental	22,737	10,561	46.4%	42.9%
<i>Subtotal Departmental Expenditures</i>	<u>881,580</u>	<u>390,663</u>	<u>44.3%</u>	<u>45.1%</u>
Non-Departmental Expenditures				
City-Wide Expenses	\$ 256,126	\$ 87,009	34.0%	41.3%
Capital Contributions	82,878	10,589	12.8%	18.7%
Transfers	28,051	28,051	100.0%	100.0%
Reserves	137,305	-	0.0%	0.0%
<i>Subtotal Non-Departmental</i>	<u>504,360</u>	<u>125,649</u>	<u>24.9%</u>	<u>30.1%</u>
Total	\$ 1,385,940	\$ 516,312	37.3%	39.6%

Overall, General Fund expenditures are tracking below anticipated levels and are expected to end the year with savings of approximately \$10.0 million to assist in meeting the 2016-2017 ending fund balance estimate that will be used as a funding source in the Five-Year General Fund Forecast and the 2017-2018 Proposed Budget. The majority of savings is anticipated to be generated from Personal Services and City-Wide expenditure appropriations.

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Recommended Adjustments

Various budget adjustments are recommended in this document to accomplish the following major urgent and required items:

- Address two urgent fiscal/program needs, including: adding \$75,000 to the Office of Immigrant Affairs City-Wide Expenses appropriation to support the Capacity Building Streamlining Legal Defense for Families and Youth program that will provide immigrant service delivery coordination and fill a service gap that exists until County programs are in place; and establishing a Cyber Security City-Wide appropriation in the amount of \$275,000 to perform an audit, address penalties the City has incurred, purchase equipment and software, provide a Payment Card Industry (PCI) awareness training, and add firewalls.
- Implement required technical and rebalancing actions including:
 - Reallocating funding of \$4.0 million within the Fire Department Personal Services appropriation from the salaries and benefits line items to the overtime line item to account for higher than anticipated overtime costs to backfill for staff absences and vacancies, offset by vacancy savings;
 - Reallocating funding from the Parks, Recreation and Neighborhoods Services (PRNS) Personal Services appropriation to the PRNS Non-Personal/Equipment appropriation in the amount of \$1.1 million to provide funding for higher than anticipated parks water costs;
 - Increasing the Homeless Response Team City-Wide Expenses appropriation by \$100,000, offset by current year savings in the Homeless Rapid Rehousing City-Wide Expenses appropriation;
 - Reallocating funding from the Council District 02 Office to a City-Wide Expenses appropriation in the amount of \$75,000 for the Council District 02 participatory budgeting program; and
 - Addressing updated cost estimates, funding needs, and technical adjustments, including additional funding the Business Tax System Replacement (\$100,000), and the Transfer to the Downtown Property and Business Improvement District Fund (\$17,000).

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- Appropriate additional grant, reimbursement, and/or fee related funds (\$2.4 million) including but not limited to:
 - Increasing the Fire Department Personal Services appropriation in the amount of \$699,000, offset by a reimbursement from the State, for Strike Teams deployed to assist with fires in Kern, Santa Cruz, Contra Costa, San Bernadino, Eastern Humboldt, and Santa Clara (Loma Prieta) counties;
 - Increasing the Parks, Recreation, and Neighborhood Services Department Fee Activities appropriation in the amount of \$465,000, offset by fee revenue, due to increased activity from the preschool program, the Recreation of City Kids (R.O.C.K) program, which is after school programming for kids provided at school sites, and camps;
 - Establishing a California Gang Reduction, Intervention and Prevention (CALGRIP) Grant appropriation to the Parks, Recreation and Neighborhood Services Department, offset by State revenue in the amount of \$474,000, to target gang-impacted youth through the implementation of proven intervention, substance abuse, and remedial (GED)/vocational education strategies with the intent to reduce gang and youth violence; and
 - Increasing the Emergency Street Tree Services appropriation by \$300,000, offset by property owner reimbursements, for contractor maintenance of street trees which are the responsibility of adjacent property owners.

- Implement clean-up actions, such as adjustments that increase Personal Services appropriations, where needed, for Management Pay for Performance Program increases (\$1.3 million) and Health Benefit increases (\$821,000), offset by the Salaries and Benefits Reserve, and reallocate between Personal Services and Non-Personal/Equipment appropriations to fill vacant positions through temporary staffing resources.

In total, adjustments recommended in this document result in a net increase of \$2.8 million to General Fund expenditures. Additional information on these adjustments can be found in *Section III. Recommended Budget Adjustments and Clean-Up Actions* of this document. The following discussion highlights major General Fund expenditure activities through December.

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DEPARTMENTAL EXPENDITURES

Departmental expenditures include personal services (salaries, overtime, retirement, health, and other fringe benefit costs), non-personal/equipment, and other departmental expenses. Personal services costs represent the largest single General Fund expense category for the City. These costs accounted for 65.7% of the General Fund expenditures to date.

Through December, personal services expenditures for all City departments totaled 45.9% of the current Modified Budget, which is slightly below expectations (46.4%) at this point of the year. This expenditure level was slightly below the 46.8% expended through December last year. Overall, Personal Services expenditures are tracking to end the year with several million in savings. As of January 4, 2017, the City had 850 vacancies city-wide (all funds) compared to 678 vacancies in the prior year, representing a vacancy factor of over 10%. Although some of these vacancies are backfilled with temporary staffing resources, vacancy savings have been accumulating throughout the organization. As described in Section III of this document, reallocations of Personal Services appropriation savings to Non-Personal/Equipment appropriations in the Finance, Information Technology, and Parks, Recreation and Community Services Departments are recommended to reflect the use of temporary staffing or contractual services until vacancies are filled and/or to address other expenditure needs. In addition, budget actions are recommended to reallocate salary and benefit savings to overtime for the Fire Department.

Non-Personal/Equipment expenditures of \$41.0 million are also tracking below anticipated levels with 34.2% expended through December, slightly below prior year levels of 34.8% in December 2015. In addition to expenditures, \$28.6 million was encumbered, bringing the total amount of funding committed to \$69.5 million, or 58.0% of the \$119.9 million budget. Overall, these expenditures are expected to remain within budget for all departments with some savings generated by year-end. As a result of the high vacancy levels, as discussed above, many departments have needed to backfill with temporary staffing or contractual services to continue service delivery. As discussed above and described in Section III of this document, reallocations from Personal Services appropriations to Non-Personal/Equipment appropriations are recommended to align departmental budgets with anticipated spending by category.

The Other Departmental category includes the budget for the Mayor and City Council, Library Grants, and Parks, Recreation and Neighborhood Services Fee Activities. Other Departmental expenditures totaled \$10.6 million (46.4%) of the \$22.7 million budget through December, above prior year levels of \$8.6 million (42.9%) in December 2015. Expenditures in this category are expected to remain within budget.

Following is a discussion of the Fire, Parks, Recreation and Neighborhood Services, and Police Departments as well as non-departmental expenditures.

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DISCUSSION OF SELECTED GENERAL FUND DEPARTMENTS

Expenditure Status (\$ in thousands)			
<u>Department</u>	<u>2016-2017 Budget</u>	<u>YTD Actual</u>	<u>Prior YTD Actual</u>
Fire	\$203,968	\$95,674	\$93,651

Overall, Fire Department expenditures are tracking slightly below estimated levels after factoring in the recommended mid-year budget actions recommended in this report. Through December, Personal Services expenditures of \$87.8 million are tracking at 46.6%, which is slightly above the par level of 46.4%.

The Fire Department’s Non-Personal/Equipment budget of \$9.6 million was 54% expended or encumbered through December 2016. Non-personal/equipment expenditures are expected to end the year with some savings as encumbrances will be expended during the remainder of the year.

Through December, overtime expenditures of approximately \$7.0 million are tracking significantly above anticipated levels with approximately 74% expended. Higher overtime expenditures were incurred to backfill for sworn vacancies and absences in line duty positions (vacation, strike team deployments, modified duty, sick leave, disability, and other absences) to maintain minimum staffing requirements on Fire apparatus and to staff strike teams that were deployed to fight wildland fires. The Department has requested and will receive reimbursements from the State of California for costs associated with strike team deployments, and actions are being brought forward in this report to recognize and allocate these funds during 2016-2017 (\$699,000). Factoring in reimbursements from the State as well as some reimbursements from the federal government for training, the Department’s overtime expenditures continue to track above budgeted levels. To bring the overtime budget in line with projected expenditures, this report recommends reallocating \$4.0 million from salary and benefits savings to the overtime budget, increasing the department’s overtime budget from \$9.5 million to \$13.5 million.

Overall, the average vacancy rate of 5.8% is 2% higher than the vacancy rate at this time last year; however, vacancies continue to exceed the budgeted rate of 2.8%. In December, the Department completed the preliminary oral board interview of 554 candidates for the Firefighter Recruit Academy. Selection interviews with the Fire Chief occurred in January 2017. It is anticipated that the recruitment and selection of 25 candidates will be completed in March for an April 2017 Firefighter Recruit Academy.

Personal services expenditures in the Development Fee Program of \$2.7 million are tracking at estimated levels with 46.2% expended. To meet service commitments to the Development community, the Department has used temporary resources for peak workload demand and to temporarily fill vacancies.

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DISCUSSION OF SELECTED GENERAL FUND DEPARTMENTS

In accordance with the City Council’s approval of a March 2010 report on annual vacancy and absence rates, the Fire Department has committed to limiting administrative assignments for sworn administrative personnel for overtime control purposes. As of the end of December, of the 32 current authorized staffing level, the Fire Department had 29 sworn personnel on administrative assignments.

Expenditure Status (\$ in thousands)

<u>Department</u>	<u>2016-2017 Budget</u>	<u>YTD Actual</u>	<u>Prior YTD Actual</u>
Parks, Recreation & Neighborhood Services	\$68,936	\$37,216	\$33,196

Overall, Parks, Recreation and Neighborhood Services (PRNS) expenditures are tracking above estimated levels through December due to higher non-personal/equipment expenditures, partially offset by lower personal services expenditures. PRNS’ personal services are tracked on a seasonal basis instead of a straight line basis since seasonal activity better represents the department's expenditure trends. Through December, PRNS has spent \$37.2 million, or 45.0% of their personal services budget. Current tracking indicates the department will end the year with savings of \$1.4 million, primarily due to vacancy savings.

PRNS non-personal/equipment expenditures are tracking significantly above benchmark levels; year-to-date non-personal/equipment expenditures and encumbrances of \$13.4 million are at 70.7% of budget. A large increase in water costs is the main driver for the higher non-personal/equipment expenditures. Specifically, through December, PRNS has expended 84.1% of its budget for water utility, compared to 60.0% in the prior year.

PRNS attributes the higher expenditure rate to the water rate increases and increased usage in response to reduced conservation targets and community feedback that turf and sports fields are in poor condition. The increased water usage was also partially due to water leaks identified in the system for one account in May, June, and July 2016 where PRNS will be refunded for the expenses incurred. In addition, the higher than anticipated water rates, drought surcharges, and true-up charges of previous bills contributed to the increased costs. PRNS is currently evaluating and analyzing the increased water usage and billings from the San Jose Water Company and working to address the issue.

Due to the increased water usage and costs, the department is currently tracking to exceed budgeted levels by approximately \$2 million. PRNS is evaluating potential strategies to mitigate this impact. PRNS will be entering in their annual period where watering is kept to a minimum to prevent deterioration of irrigation systems. In addition, a reallocation of \$1.1 million from the Personal Services appropriation to the Non-Personal/Equipment appropriation to fund the increased costs is recommended as part of this report.

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DISCUSSION OF SELECTED GENERAL FUND DEPARTMENTS

Expenditure Status (\$ in thousands)

<u>Department</u>	<u>2016-2017 Budget</u>	<u>YTD Actual</u>	<u>Prior YTD Actual</u>
Police	\$346,516	\$160,307	\$160,716

On an overall basis, the Police Department’s expenditures are tracking slightly below estimated levels.

Personal services expenditures of \$146.9 million through December are tracking slightly below anticipated levels (46.0% compared to the par of 46.4%). Overtime expenditures of \$18.2 million are tracking higher than anticipated levels with 50.9% expended of the current \$35.7 million budget. Overtime is used primarily to backfill for sworn and non-sworn vacant positions as well as to conduct investigations and maintain targeted enforcement of high crime activity through suppression cars, specifically related to gang enforcement, prostitution, and graffiti. Based on current trends, personal services expenditures are tracking to end the year with savings of approximately \$2 - \$3 million, which represents less than 1% of the personal services budget. Although the Police Department is conducting regular police officer recruit academies to hire for sworn vacancies and continues to review strategies to improve the rate of sworn hiring and training, the Department is anticipated to begin 2017-2018 with approximately 132 sworn vacancies based on current attrition rates.

Overtime consists of overtime expenditures and compensatory time. The Memorandum of Agreement with the Police Officer’s Association (POA) limits how much overtime can be earned for pay versus compensatory time. The compensatory time balance at the end of December 2016 was 228,150 hours for sworn personnel. This represents an increase of 33,183 hours or 17.0% compared to the December 2015 balance of 194,967. The Police Department is in the process of implementing changes to the compensatory time usage to reduce the balance, including the implementation of special pay cars to minimize compensatory time accrual; recent implementation of the Overtime Staffing Plan to backfill positions in patrol with paid overtime; and moving sworn staff throughout the department into Patrol to minimize vacancies. In addition, the Department is looking at the feasibility of having staff, which are over the maximum compensatory time balance of 240 hours, use compensatory time first when taking time off and exploring other ways to reduce the compensatory time liability by year-end.

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DISCUSSION OF SELECTED GENERAL FUND DEPARTMENTS

The chart below outlines current authorized sworn staffing levels and the number of street-ready sworn positions available at work:

	2015-2016 (as of 1/26/16)	2016-2017 (as of 1/13/17)
Authorized Sworn Staffing	1,109	1,109
Vacancies	(193)	(184)
Filled Sworn Staffing	916	925
Field Training Officer/Recruits	(45)	(51)
Street-Ready Sworn Positions Available	871	874
Disability/Modified Duty/Other Leaves	(54)	(73)
Street-Ready Sworn Positions Working	817	801

In order to fill the vacant sworn positions and put more Police Officers back on patrol, the Department will conduct three Police Recruit Academies in 2016-2017 with one that began in October 2016. Each academy has the capacity to host between 45 - 60 recruits. The October Academy currently has 34 recruits, with the next academy beginning in February 2017 with 31 recruits, and a third academy anticipated in June 2017.

A total of \$13.4 million (49.6%) of the Department's Non-Personal/Equipment budget was expended or encumbered through December, and expenditures are expected to remain within budget. Excluding the remaining balances for centrally-determined details, including electricity, gas, and vehicle operation and replacement, the Department has approximately \$7.2 million, or 43.0% of the non-centrally-determined appropriation available for the remainder of the fiscal year.

NON-DEPARTMENTAL EXPENDITURES

With a Modified Budget of \$504.4 million, Non-Departmental Expenditures include City-Wide Expenses, Capital Contributions, Transfers, and Reserves.

Through December, City-Wide Expenses totaled \$87.0 million, or 34.0% of the Modified Budget of \$256.1 million. When expenditures and encumbrances of \$19.9 million are combined, the total amount of funding committed (\$106.9 million) was 41.7% of the budget. In total, City-Wide expenditures are tracking to end the year slightly below budgeted levels.

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NON-DEPARTMENTAL EXPENDITURES

2016-2017 City-Wide Expenses
Expenditures by City Service Area
(\$ in Thousands)

City Service Area	Current Budget	YTD Actual	% of Budget	Prior Year Actual	Prior Year % of Budget
Community & Economic Development	\$ 43,255	\$ 8,018	18.5%	\$ 16,272	46.0%
Environmental & Utility Services	4,326	729	16.9%	533	17.6%
Neighborhood Services	10,510	3,582	34.1%	5,603	45.2%
Public Safety	23,024	8,934	38.8%	8,582	39.2%
Transportation & Aviation Services	6,798	2,855	42.0%	2,791	46.1%
Strategic Support	168,213	62,891	37.4%	71,263	40.5%
TOTAL	256,126	87,009	34.0%	105,044	41.3%

The expenditure tracking for City-Wide Expenses can vary significantly depending on payment schedules and the timing of projects. For example, in 2016-2017, no payment has been booked through December for the Convention Center Lease Payments; however, in 2015-2016, \$9.8 million had been booked for this purpose, which accounts for the major difference in expenditures from year to year for the Community and Economic Development City Service Area (CSA) in the chart above. In some instances, the appropriations will not be fully expended by year-end because of the multi-year nature of some larger projects. As needed, recommendations will likely be brought forward at the end of the year to rebudget any savings to 2017-2018 to complete projects in progress.

Adjustments to City-Wide Expenses appropriations are recommended in this report to align the budget with the year-end expenditure projections. Additional details on these actions can be found in *Section III. Recommended Budget Adjustments and Clean-Up Actions* of this 2016-2017 Mid-Year Budget Review.

Key actions recommended in this report include:

- Increasing the California Gang Reduction, Intervention and Prevention (CALGRIP) Grant appropriation and corresponding revenue from the State of California in the amount of \$474,000. The CALGRIP grant is a collaborative effort to help reduce gang and youth violence through intervention, substance abuse, and remedial (GED)/vocational education.
- Establishing new appropriations to the Police Department for the following three grants: 2016 County Victim Services Program (\$142,000); 2016 Internet Crimes Against Children (ICAC) Task Force (\$38,000); and 2016 Sex Offender Registration and Notification (25,000), and recognizing total grant revenue in the amount of \$205,000.

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- Increasing the Emergency Street Tree Services appropriation and corresponding revenue or payment from property owners in the amount of \$300,000. This program currently has a backlog of pending tree work and this additional funding will enable the City to provide contractor maintenance of street trees, which are the responsibility of adjacent property owners.

In total, adjustments recommended in this report result in a net increase of \$1.3 million to City-Wide Expenses. Additional information on these adjustments can be found in Section III of this report.

The following highlights key appropriations in City-Wide Expenses across the five different CSAs:

- In July 2016, the City issued \$100 million in Tax and Revenue Anticipation Notes (TRANs) for cash flow purposes. The \$100.4 million **Tax and Revenue Anticipation Notes** Debt Service appropriation is used for repayment of these TRANs, including issuance, principal, and interest costs; \$45.4 million or approximately 45% of the budget was expended through December. This appropriation constitutes the largest allocation in the Strategic Support CSA.
- **Workers' Compensation Claims** appropriations totaling \$21.5 million are budgeted in four of the six CSAs with total expenditures of \$9.7 million through December 2016, or approximately 45% of the Modified Budget. This expenditure level is approximately 3% above the \$9.4 million expended through December 2015; the budget of \$21.5 million, however, is approximately 18% above the prior year actual expenditures of \$18.2 million. Overall, Workers' Compensation claim payments are currently tracking below budget, although some adjustments will need to be made to specific departmental City-Wide appropriations to redistribute funding based on projected needs. The Fire Department's appropriation is anticipated to have approximately \$1.9 million of savings from its \$9.2 million budget, while the Workers' Compensation Claims appropriation for the Department of Public Works is projected to exceed their budget of \$500,000 by \$300,000. A portion of the savings from the Fire Department Workers' Compensation Claims appropriation is recommended to be redistributed to the Workers' Compensation appropriation for the Department of Public Works.
- In the Strategic Support CSA, the **General Liability Claims** appropriation totals \$21.1 million, of which approximately 6.0% is expended or encumbered through December 2016, as compared to 29.0% expended or encumbered through December 2015. Claims expenditures can significantly vary from year to year.

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- Also in the Strategic Support CSA, **Sick Leave Payment Upon Retirement** expenditures of \$1.3 million through December reflect 25.4% of the total 2016-2017 budget of \$5.0 million. Year-to-date expenditures for these payouts are below the prior year level of \$1.7 million through December 2015 (2015-2016 year-end expenditures totaled \$4.0 million). Expenditures in this category are currently tracking to end the year at or below the budget. It is important to note, however, that the majority of expenditures in this appropriation typically occur in the second half of the year.
- In the Community and Economic Development CSA, the **Homeless Rapid Rehousing** and **Homeless Response Team** appropriations have expended or encumbered 32.2% and 75.9% of their respective budgets. These two appropriations provide funding for critical resources to address the City's ongoing efforts related to homelessness. This report includes an action to reallocate \$100,000 from the Homeless Rapid Rehousing appropriation to the Homeless Response Team appropriation to provide funding for anticipated expenditures associated with additional encampment cleanups in response to community and business concerns.
- In the Neighborhood Services CSA, the **San José BEST and Safe Summer Initiative Programs** appropriation has year-to-date expenditures of \$2.4 million with an additional \$1.9 million encumbered, reflecting 63.5% of the total budget of \$6.8 million committed. This appropriation supports gang prevention and intervention efforts across the City.
- In Strategic Support CSA, there are two large system upgrade projects underway, including the **Human Resources/Payroll/Budget Systems Upgrade** project and the **Business Tax System Replacement** project. The budget for both of these projects combined totals \$4.8 million; each project has expended or encumbered 71.0% and 68.3% of their respective budgets.

Through December, **General Fund Capital** expenditures total \$10.6 million and encumbrances total \$7.0 million, bringing the amount committed to \$17.6 million, or 21.3% of the \$82.9 million budget. Overall, minimal General Fund Capital expenditure savings are anticipated as the rebudget of unspent funds to 2017-2018 will be recommended to complete projects. No budget action is recommended to the General Fund Capital expenditures in this report.

Transfers of \$28.1 million are 100.0% expended through December as anticipated. All of the transfers from the General Fund are processed at the beginning of the year and have been completed. A recommended increase to the transfer to the Downtown Property and Business Improvement District (PBID) Fund of \$17,000 is included in this report to align the assessment rates for 2016-2017 used to calculate the transfer amount with the assessment rates adopted by the PBID Committee in June 2016 (the General Fund pays the assessment for City-owned facilities).

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There are no expenditures against the **Reserves** budget of \$101.8 million because expenditures cannot be charged directly to a reserve (to use Reserve funding, budget actions are necessary to move funding from a Reserve to an expenditure appropriation). The largest reserves include the Budget Stabilization Reserve (\$16.3 million), Development Fee Program Reserves (Building, \$16.5 million; Fire, \$5.9 million; Public Works, \$5.2 million, and Planning, \$2.3 million), Workers' Compensation/General Liability Catastrophic Reserve (\$15.0 million), Salaries and Benefits Reserve (\$8.1 million), Retiree Healthcare Solutions Reserve (\$6.1 million), Sick Leave Upon Retirement Reserve (\$6.0 million), and Cultural Facilities Capital Maintenance Reserve (\$5.9 million).

Several budget actions are recommended in this report that impact General Fund Reserves. The major actions are described below.

- Liquidation of a portion of the Salary and Benefits Reserve for health plan rate increases of 4.9%, effective January 1, 2017, for distribution to departmental budgets that are not tracking to generate sufficient vacancy savings to absorb these additional costs;
- Liquidation of a portion of the Salary and Benefits Reserve for the management pay-for-performance program (\$1.3 million) that is set aside in the 2016-2017 Adopted Budget. This is offset by the distribution of \$1.2 million to those departments with insufficient vacancy savings to cover these increase costs and a return of \$140,000 to the Development Fee Program Earmarked Reserves for savings identified in those programs;

No budget action is recommended for the **Contingency Reserve**, which currently totals \$35.5 million and complies with the City Council policy to set aside 3% of expenditures.