CITY OF MENLO PARK

STAFF REPORT

City Council
Meeting Date: **4/14/2026**
Staff Report Number: **26-055-CC**

Regular Business: **Approve fiscal year 2026-27 budget principles**

Recommendation
Staff recommends City Council approve budget principles for fiscal year 2026-27 (Attachment A).

Policy Issues
Menlo Park Municipal Code Section 2.08.080 (8) provides that the city manager must "prepare and submit to the City Council the annual budget." The city manager's proposed budget is built on foundational budget principles set by the City Council.

Background
The City Council held a priority-setting workshop March 21 to help set the stage for budget development. At the workshop, the fiscal year 2025-26 budget principles were shared for reference. The high-level priorities of the City Council will inform the development of the City's fiscal year 2026-27 budget. In addition to priorities, the City Council also approves budget principles, which continues the City's public input process for the annual budget.

Analysis
<u>Proposed budget principles</u>
To ensure the city manager's proposed budget reflects the City Council's foundational fiscal values, staff present the proposed budget principles for fiscal year 2026-27. Staff are proposing adding two new principles (1H and 3D), expanding on six existing principles to add context and/or methods for prioritizing limited resources (1A, 1C, 1G, 2D, 3B and 3C), rewording the Section 3 title for consistency, and simplifying the wording of two existing principles (2C and 2E; see Attachment A for the red-lined and clean versions). These proposed changes build upon and refine the principles adopted for fiscal year 2025-26 to align with the City's continued focus on achieving long-term fiscal sustainability and addressing the General Fund's structural imbalance, discussed in the General Fund five-year forecast section below. Staff may propose revisions to the General Fund reserve policy during the budget process to reflect the updated budget principles.

<u>Budget development calendar</u>
The following budget calendar outlines approximate dates for actions leading up to the adoption of the fiscal year 2026-27 budget. The City is required to adopt its budget before July 1 of each year.

Table 1: Fiscal year 2026-27 budget development calendar	
Date	**Description**
April 14	City Council reviews and approves budget principles; Update on capital improvement plan (CIP)
April 28	Master Fee Schedule public hearing and adoption; City Council workshop final report
May 12	CIP study session
May 20 (tentative)	Budget portal open to public
May 28	Public budget workshop
June 9	Budget public hearing
June 23	Budget adoption

Five-year capital improvement plan (CIP)
The City Council adopts the five-year CIP annually as part of the budget adoption process. The proposed CIP incorporates priorities identified through the City Council's annual priority setting workshop. At a future meeting, the City Council may provide additional direction regarding the five-year CIP by reviewing the criteria for identifying and prioritizing projects, the ranking of project priorities, and new project requests through the budget adoption process and mid-year budget review.

General Fund five-year forecast
The General Fund five-year forecast reflects the City Council's adopted budget principles and serves as a key tool to inform long-term strategic decision-making for the City's largest operating fund. The forecast identifies an ongoing structural imbalance between revenues and expenditures, highlighting the importance of continued fiscal planning to maintain long-term sustainability. Developed using the most current assumptions and best available data from a variety of sources, the five-year outlook provides the City Council with a comprehensive projection of revenues and expenditures over the next five years.

Revenue assumptions
The forecast assumes moderate growth in the City's three largest tax revenue sources property tax, transient occupancy tax (TOT) and sales tax, while remaining cautious due to an uncertain economic environment, including reduced consumer spending and persistent inflation. Federal policy changes under HR 1, the One Big Beautiful Bill Act, signed into law in July 2025, including reductions to healthcare funding, are expected to place additional pressure on local government resources. However, some fiscal relief is anticipated with the payoff of the Successor Agency of the Former City of Menlo Park Redevelopment Agency debt Dec. 31, 2029. At that time, approximately $5 million in property tax revenue currently allocated to debt service will be returned to the County distribution, resulting in an estimated $0.9 million in additional annual revenue for the City.

The City Council received preliminary information on the five-year forecast update during the March 21 workshop, where key assumptions and trends were presented for initial review. Since that time, the forecast has been updated to reflect the latest available information. The decrease of Vehicle License Fee (VLF) backfill revenue of $2 million represents the primary assumption revised in this update, along with a $0.8 million increase to Transient Occupancy Tax (TOT) to align with current trends, and other minor updates totaling an additional $0.5 million in revenue increases. In the earlier version of the forecast, the VLF backfill was not fully removed as the City was continuing to assess evolving State budget information and potential implications for this funding source. The Governor's 2026–27 budget proposal eliminates the VLF backfill for

San Mateo County. As a result, this forecast removes the previously projected $2 million in VLF backfill revenue and assumes no allocation in future fiscal years to align with best budgeting practices and reflect a cautious and realistic revenue outlook. As of fiscal year 2025-26, the City has already experienced a $3.8 million shortfall in VLF backfill revenue. With future year projections now revised to zero, the cumulative impact is estimated at a total loss of approximately $14.4 million over the next five years.

Other revenue assumptions include fee revenue based on current fee schedules and existing activity levels, pending potential updates resulting from the completion of the comprehensive costs of services study and adoption of the updated Master Fee Schedule.

Expenditure assumptions
On the expenditure side, assumptions include a 10% vacancy and turnover factor in fiscal year 2026–27, declining by 2% annually to a steady-state 6%, and 3% annual growth in personnel costs. The forecast also removes the non-spendable operating factor to align with best practices and improve budget transparency, incorporates a $1.7 million annual contribution to the Vehicle Internal Service Fund, and maintains a flat General Fund contribution to the capital improvement program.

<u>Budget strategies</u>
Overall, the forecast indicates an average structural deficit of $9 million per year, which is not fiscally sustainable, as General Fund reserves are projected to be fully depleted within the next three fiscal years. To address this, staff presented budget balancing strategies during the March 21 financial update at the City Council priority workshop. Immediate strategies include increasing revenue by updating user fees to align with cost recovery and budget principles, implementing an updated enterprise overhead allocation, enhancing business license tax compliance and reducing expenditures through lower General Fund contributions to capital improvement projects and targeted department budget reduction.

Maintaining alignment between user fees and the cost of providing services is a key part of maintaining long-term fiscal sustainability of the General Fund. With an update to the Master Fee Schedule and the corresponding, projected revenue to the General Fund, additional budget strategies are still needed including a recommended $1.5 million in total departmental budget reductions. Staff are continuing to work with departments to identify legally required and essential services to help guide these decisions.

As shown in Table 2, the Master Fee Schedule public hearing is scheduled for April 28, with the staff report and proposed Master Fee Schedule to be released in advance on April 13. As the final adopted user fees will directly influence projected fee revenue incorporated into the proposed budget for fiscal year 2026–27, staff may need to return to City Council to present options to produce a balanced budget.

Table 2: Master Fee Schedule calendar

Date	Description
April 13	Early release staff report in advance of public hearing
April 28	Master Fee Schedule public hearing and adoption
May 2	Deadline for approving Master Fee Schedule
June 9	Budget public hearing incorporating approved fee revenue projections
June 23	Budget adoption
July 1	New Master Fee Schedule takes effect

Longer term budget strategies include potential revenue-generating measures, such as a business license tax update or a sales tax measure, that could provide significant revenue in future years to help address the structural deficit.

Impact on City Resources

Preparation of the fiscal year 2026-27 annual budget is part of the City's baseline services. There is no impact to City resources at this time.

Environmental Review

This action is not a project within the meaning of the California Environmental Quality Act (CEQA) Guidelines §§15378 and 15061(b)(3) as it will not result in any direct or indirect physical change in the environment.

Public Notice

Public notification was achieved by posting the agenda, with the agenda items being listed, at least 72 hours prior to the meeting.

Attachments

A. Proposed fiscal year 2026-27 budget principles (red-lined and clean versions)

Report prepared by:
Katie Lee, Management Analyst II

Report reviewed by:
Fenny Lei, Assistant Administrative Services Director

PROPOSED FISCAL YEAR 2026-27 BUDGET PRINCIPLES

City Council
701 Laurel St., Menlo Park, CA 94025
tel 650-330-6620

1. Promote the City's long-term fiscal sustainability

A. Continue to fund the strategic pension reserve when financially feasible and utilize it as a tool for rate stabilization. Annual payments toward the CalPERS Net Pension Liability will be based on the required contributions identified in the actuarial reports, maintaining progress toward reducing the unfunded accrued liability (UAL). ~~Implement the annual payment necessary in the budget to achieve amortization of the CalPERS Net Pension Liability in accordance with the actuarial 15-year amortization schedule. This is consistent with the City Council's previously adopted budget principle to plan for an accelerated reduction of the unfunded accrued liability (UAL).~~

B. Invest in technologies that minimize low value-add processes, increase transparency in communications and most efficiently utilize our talented staff.

C. Strive to achieve City Council cost recovery goals for fee-based services, including implementing annual fee updates as necessary to reflect changes in the cost of providing services, including the Consumer Price Index (CPI), personnel costs, or other relevant cost indices.

D. Continue to evaluate the most cost-effective method to provide services at a specified level that provides the City with flexibility in all economic conditions, including the use of contracted services, shared services, and regular and limited-term employees.

E. Proactively manage the loss of institutional knowledge by documenting procedures, practices and processes and succession planning efforts including the ability to provide for overlap in critical positions at the discretion of the city manager.

F. Incorporate programs and initiatives that strengthen Menlo Park's standing as an employer of choice to retain highly qualified personnel.

G. Address the City's structural imbalance between revenues and expenditures through immediate and ongoing actions to stabilize the General Fund reserve and restore long-term fiscal sustainability. ~~Evaluate the long-term structural balance of revenues and expenditures to maintain a sustainable General Fund.~~

H. Focus available resources on essential and legally mandated services, while regularly assessing other programs for alignment with City priorities, service levels, and fiscal capacity.

2. Provide city services and infrastructure that contribute to quality of life in Menlo Park

A. Implement ordinances and City Council adopted initiatives and strategies to contribute to the quality of life in Menlo Park now and in the future.

B. Proactively maintain and improve existing infrastructure to minimize maintenance costs, decrease the City's greenhouse gas emissions, and increase the City's long-term disaster and climate resilience.

C. Strive to balance the resources and requirements of each area of the city in an equitable manner ~~through the use of~~ using equitable tools and ongoing collaboration with the Countywide Equity Working Group.

D. Evaluate one-time revenues for their highest and best use, prioritizing investments for long-term gains in financial sustainability and enhancing quality of life for the community. ~~Evaluate one-time revenues for highest and best investment recognizing the benefit of leveraging near term investments for long-term gains in financial sustainability and/or quality of life.~~

E. Commit to continuous improvement in the communication of City financial information through a variety of media acknowledging that the City's professional staff and consultants are obligated to conform to accounting and reporting standards ~~in order~~ to provide balanced financial information that informs policymakers.

F. Strategically identify and align financial resources to implement City Council-identified top goals.

3. Manage r~~R~~evenue sources and grant accounting

A. State the fund's surplus/(deficit) balance to show annual results and use of fund balance.

B. Limit budget appropriations for capital projects to those with secured funding. Appropriations shall not exceed available funding and will be adjusted if funding is reduced. ~~Identify revenue sources for the initial year of all capital projects.~~

C. Prioritize adoption of balanced budgets to maintain the fiscal integrity of all funds. Use of fund balance is permitted only to the extent that the year-end balance remains positive. ~~Ensure a fund's fiscal year-end balance estimate is positive.~~

D. One-time revenues should be used for one-time expenditures and not for ongoing commitments, to minimize the risk of creating or exacerbating structural deficits.

PROPOSED FISCAL YEAR 2026-27 BUDGET PRINCIPLES

City Council
701 Laurel St., Menlo Park, CA 94025
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1.	**Promote the City's long-term fiscal sustainability**
A.	Continue to fund the strategic pension reserve when financially feasible and utilize it as a tool for rate stabilization. Annual payments toward the CalPERS Net Pension Liability will be based on the required contributions identified in the actuarial reports, maintaining progress toward reducing the unfunded accrued liability (UAL).
B.	Invest in technologies that minimize low value-add processes, increase transparency in communications and most efficiently utilize our talented staff.
C.	Strive to achieve City Council cost recovery goals for fee-based services, including implementing annual fee updates as necessary to reflect changes in the cost of providing services, including the Consumer Price Index (CPI), personnel costs, or other relevant cost indices.
D.	Continue to evaluate the most cost-effective method to provide services at a specified level that provides the City with flexibility in all economic conditions, including the use of contracted services, shared services, and regular and limited-term employees.
E.	Proactively manage the loss of institutional knowledge by documenting procedures, practices and processes and succession planning efforts including the ability to provide for overlap in critical positions at the discretion of the city manager.
F.	Incorporate programs and initiatives that strengthen Menlo Park's standing as an employer of choice to retain highly qualified personnel.
G.	Address the City's structural imbalance between revenues and expenditures through immediate and ongoing actions to stabilize the General Fund reserve and restore long-term fiscal sustainability.
H.	Focus available resources on essential and legally mandated services, while regularly assessing other programs for alignment with City priorities, service levels, and fiscal capacity.
2.	**Provide city services and infrastructure that contribute to quality of life in Menlo Park**
A.	Implement ordinances and City Council adopted initiatives and strategies to contribute to the quality of life in Menlo Park now and in the future.
B.	Proactively maintain and improve existing infrastructure to minimize maintenance costs, decrease the City's greenhouse gas emissions, and increase the City's long-term disaster and climate resilience.
C.	Strive to balance the resources and requirements of each area of the city in an equitable manner using equitable tools and ongoing collaboration with the Countywide Equity Working Group.
D.	Evaluate one-time revenues for their highest and best use, prioritizing investments that leverage near-term resources for long-term financial sustainability and/or community quality of life. One-time revenues should be used for one-time expenditures and not for ongoing commitments, to minimize the risk of creating or exacerbating structural deficits.
E.	Commit to continuous improvement in the communication of City financial information through a variety of media acknowledging that the City's professional staff and consultants are obligated to conform to accounting and reporting standards to provide balanced financial information that informs policymakers.
F.	Strategically identify and align financial resources to implement City Council-identified top goals.
3.	**Manage revenue sources and grant accounting**
A.	State the fund's surplus/(deficit) balance to show annual results and use of fund balance.
B.	Limit budget appropriations for capital projects to those with awarded grants or secured funding sources. Appropriations shall not exceed available funding, and will be adjusted proportionally in the event that funding sources are reduced.
C.	Prioritize adoption of balanced budgets to maintain the fiscal integrity of all funds. Use of fund balance is permitted only to the extent that the year-end balance remains positive.