



## STAFF REPORT TO THE FINANCE COMMISSION

**DATE:** Regular Meeting of February 18, 2026

**TO:** Members of the Finance Commission

**SUBMITTED BY:** Edwin Gato, Director of Finance

**SUBJECT:** Adoption of a Resolution Amending the Fiscal Year (FY) 2025-26 Operating and Capital Budgets to Reflect the Recommended Mid-year Adjustments

### RECOMMENDED ACTION

The staff recommends that the City Council receive the FY 2025-26 Mid-Year Financial Summary Report and adopt a resolution to amend the FY 2025-26 operating and capital budgets to reflect the proposed mid-year adjustments.

### EXECUTIVE SUMMARY

The Midyear Budget Review provides a comprehensive assessment of the City's financial position halfway through the fiscal year. This review enables necessary adjustments to the current FY 2025-26 budget, reflecting any changes in expected revenues and expenditures since the Annual Budget was adopted on June 10, 2025.

### BACKGROUND

This report offers an analysis of the financial status of the City halfway through the fiscal year. It provides a comprehensive assessment of the City's General Fund and other non-general funds. The analysis compares projected revenues and expenditures with the actual receipts and expenses recorded as of December 31, 2025. This comparison provides a clear, insightful view of the City's fiscal performance, highlighting significant developments in the first half of the fiscal year.

### ANALYSIS

As part of the budget process, City staff are required to deliver a midyear report to the City Council. This report will evaluate revenues and expenditures and propose any necessary adjustments. The midyear review provides a valuable opportunity to assess the Budget's status and make informed adjustments to the City's planned operations and capital projects as needed.

The annual operating budget has been adopted through a careful, responsible process that aligns with the City’s financial policies. This method is particularly crucial given the uncertainties arising from unprecedented inflation and national instability. The City has effectively maintained its fiscal health by adhering to conservative budgeting practices and remaining within its financial capabilities.

This year, the staff is proposing several budget modifications in response to unforeseen financial circumstances. These adjustments aim to address the challenges while upholding the City’s commitment to sound financial management. The table below summarizes the proposed budget amendments:

Title	Proposed Funding Source	Budget Impact		
		General Fu	Other Fun	Total
Beechnut Park Project	General Fund Capital Reserve	\$98,000		\$98,000
Clean Water Program Support	Stormwater Fund		\$23,000	\$23,000
Animal Control	General Fund	\$76,000		\$76,000
Grant Writing	General Fund	\$50,000		\$50,000
	<b>Total</b>	<b>\$224,000</b>	<b>\$23,000</b>	<b>\$247,000</b>

The following section presents an analysis of the City's financial resources, beginning with an overview of the General Fund. The General Fund is the City's primary operating fund, supporting essential services such as law enforcement, public works, parks and recreation, and community development, as well as vital administrative functions.

**General Fund**

The General Fund is a crucial financial resource for the city, drawing on a diverse array of taxes, fees, and general revenue sources. This comprehensive funding structure enables effective allocation of resources across a wide range of essential expenses. As a result, the General Fund provides substantial flexibility in financial planning, allowing city officials to direct funds toward pressing community needs rather than confining them to specific, predefined projects. This strategic approach to resource allocation is vital for the efficient management of city services and resources, reflecting the government’s commitment to addressing the diverse needs of its residents.

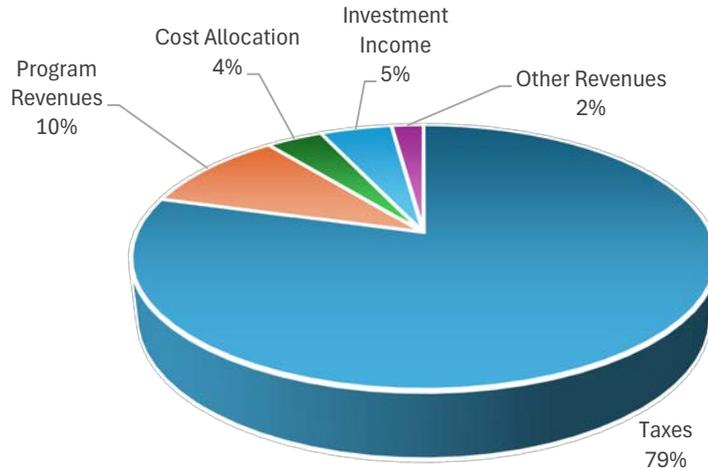
The Midyear Budget Review indicates that, as of December 31, 2025, the majority of General Fund revenues have achieved 49% of the estimated amount, while expenditures have reached 53%, slightly exceeding the original budget projections. This minor overage is anticipated to self-correct as the fiscal year progresses, primarily due to the reconciliation and payment of several expenses during the initial six months. As we approach year-end, we expect this preliminary overrun to stabilize, which reflects the adaptive and practical nature of our budget management practices.

- I. General Fund Revenues
 

As of December 31, 2025, the General Fund's operating revenues totaled \$9.5 million, representing 49% of the adopted budget for FY 2025-26. It is essential to recognize that most revenue from vehicle license fees and business licenses is received after this date, as vehicle license fee revenue is not remitted to the City until February, and the deadline for business license renewals is January 31. This

timeframe explains the observation of revenues falling below 50% at the end of December. Additionally, program-fee revenues often fluctuate annually; however, these variations are offset by the corresponding program expenditures.

Below is a chart of General Fund revenues, followed by an analysis of the major General Fund revenues:



Approximately 79% of the General Fund's revenues are derived from various general taxes. This substantial funding is heavily reliant on economically sensitive sources, such as sales taxes and utility user taxes. The stability of these key revenue streams is closely linked to the overall economic climate. As a result, any shortfall or fluctuations in these areas could have serious implications for the financing of future programs and essential services. Therefore, it is imperative to ensure a consistent flow of funds from these sources to maintain the City's financial health and effectively address community needs.

➤ **Utility Users Tax (UUT)**

The City imposes a utility users' tax (UUT) on the consumption of various utility services, including electricity, gas, water, telephone, and cable. The City determines the tax rate. Currently, the UUT rate in Hercules stands at 8%, which is crucial to funding essential City services and accounts for approximately 20% of General Fund revenues.

As of December 31, 2025, the City has collected \$2.1 million, representing 51% of the estimated fiscal-year revenue. These funds are remitted to the City monthly. Given the collections achieved to date, estimated revenue from UUT is on track to meet projected targets.

➤ Sales Tax

The City collects a tax on the sale of certain goods and services. This tax is the largest source of revenue for the General Fund, accounting for 28% of its total revenues. It is remitted to the City by the State every month.

As of December 31, 2025, the City has collected \$3.2 million, representing 54% of the estimated fiscal-year revenue. This collection suggests that sales tax revenue is on track to meet its targets. It is important to note that sales tax revenues are concentrated among a few major operators and are primarily derived from business-to-business transactions. The top three contributors account for over 50% of the City's total sales tax revenue. If any of these key revenue sources fall short of projections, it could negatively impact funding for future programs and services.

➤ Property Taxes

As of December 31, 2025, the City has collected approximately \$1.2 million, representing 69% of projected revenue. Property taxes in Hercules are relatively low in comparison to many neighboring Bay Area cities, primarily due to a historical and permanent reduction in revenue allocation resulting from Proposition 13, enacted in 1978. Importantly, the City's share of the base 1% property tax rate remains below that of many other jurisdictions, accounting for just over 5% of Hercules's total base property taxes.

➤ Vehicle License Fee (VLF)

In addition to the standard allocation of property taxes, cities and counties receive property tax revenues in lieu of Vehicle License Fees (VLF). In 2004, the Legislature implemented a permanent reduction in the VLF rate from 2 percent to 0.65 percent, offsetting the revenue loss to cities and counties with an equivalent dollar-for-dollar increase in property tax allocations. Each agency's property tax allocation in place of VLF is adjusted annually in accordance with the growth in gross assessed valuation within that specific city or county.

The City receives this allocation from the County biannually, in February and June. According to our consultant's estimates, the City is expected to receive approximately \$2.6 million by the end of this fiscal year.

➤ Business License Fees

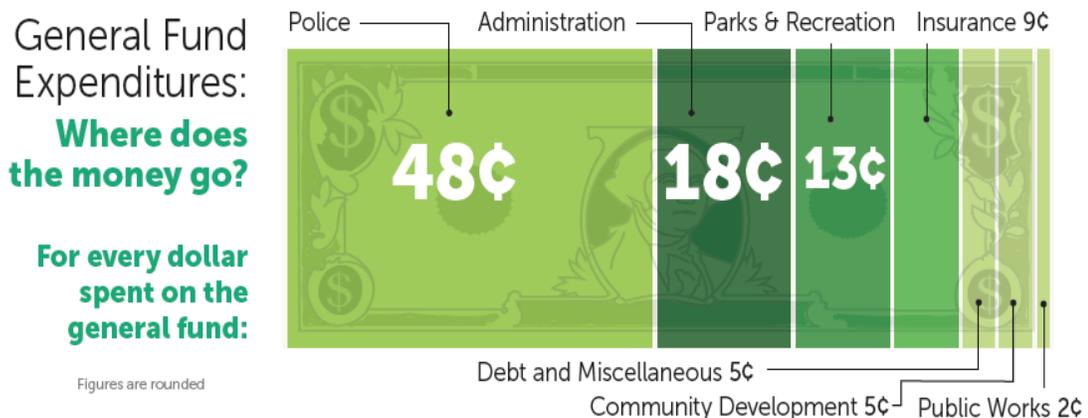
A business license fee is an annual tax mandated by the city for the legal operation of a business. In Hercules, this tax is determined by the industry's specific nature. Existing businesses must renew their licenses each year. Payments are generally due by January 1st, with a grace period extending until January 31st. The fee structure typically consists of a base amount plus a state-mandated \$4 fee.

➤ Other taxes and revenues

The summary indicates that several revenue streams are currently collecting less than 50% of their expected revenue, primarily due to the timing of receipt. However, a review of month-to-month trends from the previous year shows that overall General Fund revenues are aligning with our fiscal targets for this year. This outcome suggests a positive trajectory and a stable financial outlook, despite some areas underperforming at midyear.

II. General Fund Expenditures

The General Fund allocates its annual resources to a range of essential services vital to the community's functioning and improvement. These services include public safety provided by the police department, recreational opportunities and green spaces through the parks and recreation department, urban and community development initiatives, and infrastructure maintenance and enhancement through public works. Additionally, it supports the administrative functions required for effective governance. These allocations help create a safe, vibrant, and well-organized community environment.



As of December 31, 2025, the operating expenditures of the General Fund have reached \$11 million, accounting for 53% of the adopted budget for fiscal year 2025-26. It is important to highlight that insurance premiums for General Liability and Workers' Compensation are due at the start of the fiscal year. Furthermore, park and recreation expenses are primarily driven by the number of activities offered in each program and are seasonal. As a result, expenditures in these specific categories have surpassed 50% as of December 31, 2025.

The mid-year budget review provides an opportunity to suggest necessary changes to the adopted budget and implement required modifications. Generally, introducing new initiatives or programs during this review is discouraged unless deemed essential, ensuring that resources are allocated prudently. Details of the proposed budget adjustments are in Attachment 2.

III. General Fund Operating Reserve

Fiscal stability is a fundamental aspect of effective city management. Responsible financial stewardship includes the practice of maintaining adequate reserve funds to address both anticipated and unforeseen circumstances. The City has established a policy requiring operating reserves equal to 25% of total operating expenditures. Consequently, the General Fund complies with this standard, ensuring that the operating reserve represents 25% of the total operating budget.

**Non-General Fund Programs**

Funding for essential initiatives, such as transportation improvements, the gas tax, and the Measure C "Street Fund," is secured through various grants and dedicated funding streams. Each of these funding sources is subject to specific restrictions that necessitate meticulous tracking of revenues and expenditures. This process ensures that the funds are maintained separately from the City's primary operating fund, the General Fund. For a comprehensive summary of non-general fund financials as of December 31, 2025, please refer to Attachment 4.

Currently, funds and appropriations are available to support the ongoing development of projects and programs. This financial stability also enables the implementation of the proposed mid-year adjustments detailed in Attachment 2.

It is essential to note that the Victoria by the Bay Lighting and Landscaping Assessment District (LLAD) is designed to carry a deficit for 10 years, as established by the voter-approved assessment increase. As of December 31, 2025, the accumulated deficit reported for the Victoria by the Bay LLAD is approximately \$900,000.

**Next Step**

Staff are preparing the FY 2026-27 budget with a series of recommended budget workshops. The table below outlines the tentative Council meeting dates on which budget information will be provided.

Date	Action/Topic
March 24, 2026	Budget Workshop: 10-Year Capital Improvement Projects (CIP)
May 12, 2026	Budget Workshop: Preliminary draft of the Proposed FY 2026-27 Annual Operating Budget
June 9, 2026	First Public Hearing and Introduction of the FY 2026-27 Annual Budget and 10-Year CIP
June 23, 2026	Second Public Hearing and Adoption of the FY 2026-27 Annual Budget and 10-Year CIP

## **Budget Award**

The City of Hercules is proud to announce that its Fiscal Year 2025-2026 Budget has received the Distinguished Budget Presentation Award from the Government Finance Officers Association (GFOA) and Operating Budget Excellence Award from the California Society of Municipal Finance Officers (CSMFO) for the fifth consecutive year. These prestigious awards signify the highest level of recognition in government budgeting and underscore the City's commitment to transparency, accountability, and excellence in financial planning. This achievement is a testament to the hard work and dedication of the entire organization.

## **FISCAL IMPACT**

The proposed budget amendment for the fiscal year 2025-26, detailed in Attachment 2, is expected to have a financial impact of \$224,000 on the General Fund and \$23,000 on the Stormwater Fund. It is important to note that both funds possess sufficient resources to accommodate these expenditures. This amendment is strategically designed to enhance our financial planning while ensuring the continued provision of essential services and the advancement of infrastructure initiatives.

## **ATTACHMENTS**

1. Budget Resolution
2. Budget Request Detail
3. General Fund Summary
4. Non-General Fund Summary