

IBA Review of the Mayor's FY 2021-2025 Five-Year Financial Outlook

City Council, Item 201

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Independent Budget Analyst



Role of the Outlook in the Budget Process

- The Mayor's Five-Year Outlook is the first look at what the Mayor considers to be the next year's budget issues.
- It also includes what the Mayor considers to be critical strategic expenditures – identified as high priority, but not funded in the Baseline.
- These priorities may or may not be the same as the Council's.
- The Outlook allows the Council to begin identifying its top budget priorities & developing a strategy for achieving a balanced budget in FY 2021.

IBA Annual Review of Mayor's Outlook

The IBA's report on the Outlook includes:

- An overview of Baseline revenues & expenditures reported in the Outlook
- A recession scenario & its impact on City revenue
- An analysis of Mayor's Critical Strategic Expenditures included in the Outlook
- A review of potential future funding needs not included in the Outlook
- A discussion of future financial challenges
- A discussion of potential options to address shortfalls



Mayor's Five-Year Outlook

The Outlook projects deficits in the first four years, followed by one year of surplus after taking into account the Mayor's Critical Strategic Expenditures.

Mayor's FY 2021-2025 Financial Outlook					
in millions	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
Baseline (Shortfall)/Surplus	\$ (21.2)	\$ 21.6	\$ 69.6	\$ 108.6	\$ 148.7
Critical Strategic Expenditures	62.5	88.1	103.2	116.2	123.1
(Amount to be Mitigated)/Available Resources	\$ (83.7)	\$ (66.6)	\$ (33.6)	\$ (7.6)	\$ 25.5

General Fund Baseline Revenues

General Fund revenues are projected to grow throughout the Outlook; however, at a lower rate than the growth of recent years

- FY 2021 is projected at \$46.5M, or 3.0% higher than the First Quarter projection.
- Our Office supports the Department of Finance's (DoF) revenue assumptions in the Outlook.
- Revenue assumptions in the Outlook do not include assumption of a recession.



General Fund Baseline Revenues cont'd

Recession Scenario & Analysis

Recession Analysis: Potential Impact (in millions)					
	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
Outlook (Shortfall)/Surplus	\$ (83.7)	\$ (66.6)	\$ (33.6)	\$ (7.6)	\$ 25.5
<i>Potential Recession Impact</i>					
Property Tax	\$ -	\$ (9.5)	\$ (19.8)	\$ (20.7)	\$ (21.5)
Sales Tax	(22.5)	(37.7)	(38.3)	(38.8)	(39.3)
Transient Occupancy Tax	(12.0)	(21.0)	(21.8)	(22.6)	(23.3)
<i>Subtotal Potential Recession Impact</i>	<i>\$ (34.6)</i>	<i>\$ (68.3)</i>	<i>\$ (79.9)</i>	<i>\$ (82.0)</i>	<i>\$ (84.2)</i>
Total Recession (Shortfall)/Surplus	\$ (118.3)	\$ (134.9)	\$ (113.5)	\$ (89.6)	\$ (58.7)

- At Council’s request, our Office developed a scenario to demonstrate the potential impact of a recession in FY 2021.
- Growth rates for the main three revenues most impacted by a recession were reduced in line with consultant input & historical trends.

General Fund Baseline Revenues cont'd

Recession Scenario & Analysis

- This is only one potential scenario, & is subject to change based on the actual experience of a recession, including timing, severity, & duration.
- This scenario is also not our Office's prediction for a recession, but was developed to demonstrate a potential worst-case scenario as far as timing is concerned.
- While some economists are warning of a potential recession in the next five years, they are not currently including a recession prediction in their forecasts.

“Historically, the best that forecasters have been able to do consistently is recognize that we’re in a recession once we’re in one.”
-Tara Sinclair, Economist, George Washington University

General Fund Baseline Revenues cont'd

Cannabis Business Tax (CBT) Revenue Projection

- FY 2020 CBT revenue is \$4.8M higher than the FY 2020 Adopted Budget of \$12.2M.
- Outlook projects a positive annual average growth of \$2.5M taking into account a steady increase in the amount of outlets & marijuana production facilities (cultivation, manufacturing, distribution).



General Fund Baseline Revenues cont'd

Potential Stadium Impacts to Baseline

Stadium Operating Funds Relief from Sale					
	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
Operating Savings to General Fund	\$ 7,594,525	\$ 3,183,420	\$ -	\$ -	\$ -
Operating Savings to TOT Fund	-	388,244	618,000	636,540	655,636
Debt Service Payment Savings	4,047,349	4,046,336	4,045,371	4,045,097	4,041,248
Total Potential Operating Savings	\$ 11,641,874	\$ 7,618,000	\$ 4,663,371	\$ 4,681,637	\$ 4,696,884
Capital Outlay Fund ¹	\$ 18,133,545	\$ -	\$ -	\$ -	\$ -

¹ Assumes that, from a total distribution of \$47.3 million, \$29.2 million is held for debt service payments.

- The Outlook assumed no sale of the Stadium Site, & funded operations until the end of the current lease in December 2020.
- The table provides for an alternative scenario whereby the current deal with SDSU is approved in time for the university to take over the Stadium July 1, 2020, & pay the offered price of \$86.2M for the site.



General Fund Baseline Expenditures

Increase: FY 2020 Adopted Budget to FY 2021 Baseline Projection	
FY 2020 Adopted Budget	\$1,590.0
Personnel-Related Expenditure Changes	17.4
Non-Personnel Expenditure (NPE) Changes	28.2
Removal of FY 2020 One-Time NPEs	<u>(18.7)</u>
FY 2021 Outlook Baseline Projection	<u><u>\$1,616.9</u></u>
Total Increase to FY 2021 Baseline (1.7%)	\$ 26.9

Dollars in millions



General Fund Baseline Expenditures cont'd

Largest Cost Increases: from FY 2020 Adopted Budget to FY 2021	
<i>Personnel-Related Expenditures</i>	
Net Compensation Increases from Labor Agreements and Compensation Schedule Adjustments	\$8.7
Actuarially Determined Contribution (ADC) - Retirement Payment Increase	\$3.8
Step Increases for Salaries and Wages	\$2.3
<i>Non-Personnel Expenditures (NPE)</i>	
IT Increases (including \$2.9M help desk; \$2.4M voice/data network; \$2.0M data center)	\$8.7
Contracts - 3.89% Annual Growth Rate	\$7.5
Public Liability Insurance Premium Increase	\$3.4

Dollars in millions

General Fund Baseline Expenditures cont'd

Compensation Issues

- MOUs for all employee organizations expire FY 2020.
- FY 2021 contract negotiations are currently underway.
 - The Outlook does not include estimates for any potential new negotiated compensation increases.
 - DoF's General Fund cost estimate for a 1% salary increase for City employees is about \$6.0M.
- Funding will need to be identified in order for negotiated compensation increases to be effective.
 - If there are not additional revenues, expenditures (other programs & services) would need to be reprioritized to provide funding.

General Fund Baseline Expenditures cont'd

Compensation Issues cont'd

- Staffing challenges:
 - Annual *actual* vacancy savings has been significantly higher than *budgeted* vacancy savings.
 - Council has discussed concerns about *causes & effects* of the higher vacancy savings, for example hiring difficulties & staffing level deficiencies.

Mayor’s Critical Strategic Expenditures

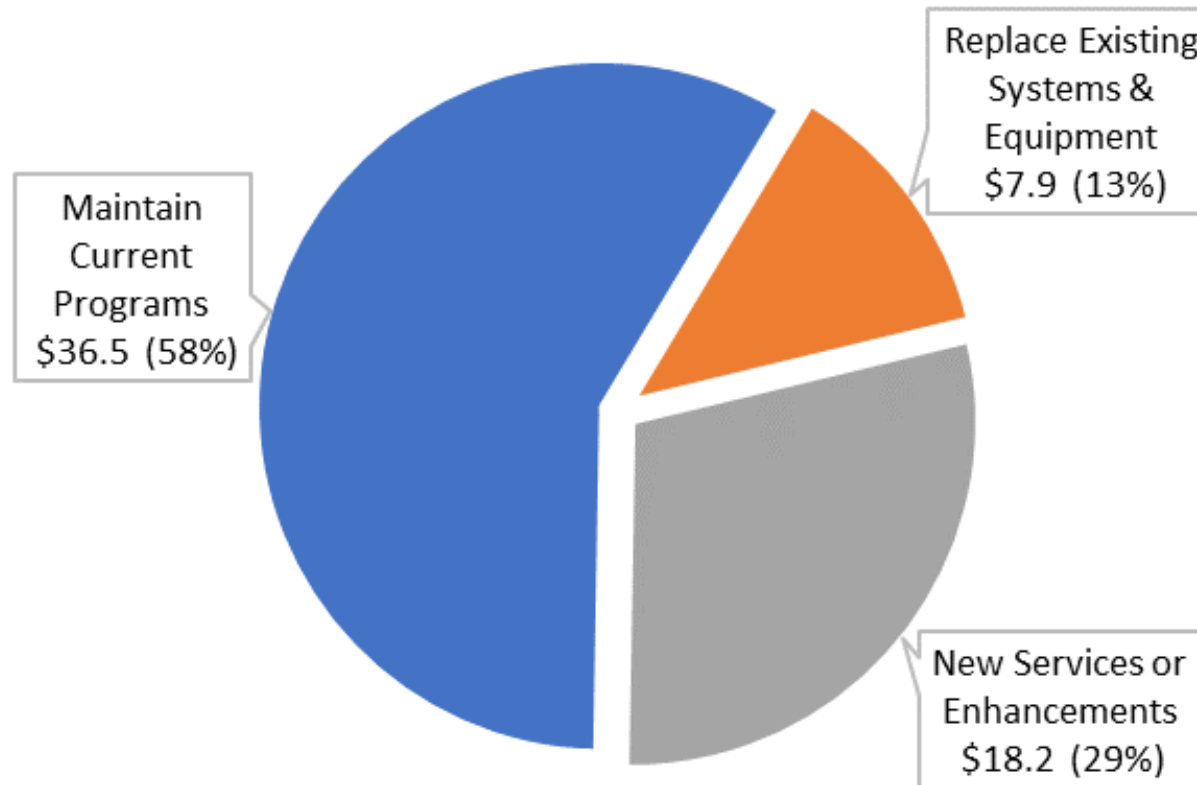
- The Mayor defines his Critical Strategic Expenditures as *“potential critical needs for the City”* that are *“necessary for meeting core service levels”*.

(in millions)	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
Critical Strategic Expenditures	\$ 62.5	\$ 88.1	\$ 103.2	\$ 116.2	\$ 123.1

- At this time, these are the Mayor’s highest priority items for consideration as City begins developing FY 2021 Proposed Budget.
- When added to the Baseline, these Critical Strategic Expenditures increase the Outlook’s projected deficit for FY 2021 from \$21.2M to \$83.7M.

Mayor's FY 2021 Critical Strategic Expenditures

We have grouped into three broad categories to provide context for prioritization



Mayor's FY 2021 Critical Strategic Expenditures cont'd

Projected Budget Gap	
(in millions)	FY 2021
Baseline Shortfall	\$ 21.2
Current Programs	36.5
Systems & Equip.	7.9
New/Expanded	18.2
Outlook Deficit	\$ 83.7

- When the Critical Strategic Expenditures are added to the Baseline shortfall, the deficit for FY 2021 increases from \$21.2M to \$83.7M



Mayor's FY 2021 Critical Strategic Expenditures cont'd

Funding Needed to Continue Existing Programs: \$36.5M

Funding Needed to Maintain Current Programs	FY 2021
Temporary Bridge Shelters	\$ 15.9
Neighborhood Policing Overtime	4.3
Arts, Culture, & Community Festivals Funding	3.9
CleanSD Overtime in Police	3.5
Continuing CleanSD Expansion in Environmental Services	2.9
Smart Streetlights	2.3
Transitional Storage Facilities	2.1
Safe Parking Program - Mission Valley	0.5
Security Guards at Central Library	0.3
Wheels of Change	0.3
Police Marketing & Recruitment Campaign	0.2
Dockless Mobility Enforcement by Police	0.2
Total	\$ 36.5

Review of Select Critical Strategic Expenditures: Funding Needed to Continue Existing Programs

- **Homeless Programs & Services**

- Outlook identifies \$18.8M for FY 2021, & \$22.2M ongoing to continue the City's homelessness programs that are funded with other one-time sources in FY 2020
- Recognizes the need for ongoing funding to support the ongoing Bridge Shelter & Storage Connect Center programs
- Signals the continuation of most programs allocated one-time State Homeless Emergency Aid Program (HEAP) funds
- Would add \$250k for Wheels of Change, currently funded through CleanSD

Review of Select Critical Strategic Expenditures: Funding Needed to Continue Existing Programs cont'd

- **Police Department**
 - Ongoing funding for overtime to maintain service levels funded by one-time resources in FY 2020
 - Neighborhood Policing - \$4.3M
 - CleanSD - \$3.5M
 - Mobility Enforcement - \$170k
- **Citywide Program Expenditures: Restoration of Arts & Culture Funding**
 - Restoration of \$3.9M in ongoing funding to maintain funding at FY 2020 levels
 - One-time transfers have been utilized for the past three consecutive fiscal years

Review of Select Critical Strategic Expenditures: Funding Needed to Continue Existing Programs cont'd

- **Environmental Services Department**

- \$2.9M in ongoing support for CleanSD to maintain expanded services levels funded with one-time resources in FY 2020

- **Sustainability Department**

- \$2.3M in additional support for the smart streetlights program, including ongoing maintenance funding & additional installation expenses

- **Library Department**

- \$457k in additional funding for Library Security to upgrade guards at the Central Library & increase overall security coverage across branch locations
- Upgrade to armed guards at Central Library has been in effect since early FY 2020 given current security needs



Mayor’s FY 2021 Critical Strategic Expenditures

Funding Needed to Replace Existing Systems & Equipment to Maintain Operations: \$7.9M

Funding Needed to Replace Existing Systems & Equipment	FY 2021
General Fund Vehicle Replacements	\$ 4.3
Public Safety Radio Equipment Replacement & Service Contracts	2.6
Replace Legacy Delinquent Accounts System & Services	0.6
Replacement of Council Electronic Voting & Audio-Visual Systems	0.3
Centralized Payment Processing Solution	0.2
Total	\$ 7.9

- The Outlook represents these items having reached the end of their useful life & funding is needed to maintain current departmental operations.
- These items need further review during budget process to assess criticality.



Mayor's FY 2021 Critical Strategic Expenditures cont'd

Funding Needed for New Services or Enhancements: \$18.2M

Funding Recommended for New Services or Enhancements	FY 2021
New Parks & Recreation Facilities	\$ 6.0
Sidewalk Repair & Replacement	3.6
Storm Water Pipe Repair Team & Street Sweeping	3.3
Peak Hour Fire Engines	2.2
New North University City Fire Station	1.4
SDG&E Franchise Consultant	1.0
Climate Action Plan	0.8
EAM Phase II	0.5
Street Resurfacing	0.3
New Pacific Highlands Ranch Branch Library	0.2
Asbestos Remediation	0.2
Enhanced Police Officer Recruiting Efforts	0.1
Security Guards for Branch Libraries	0.2
Fire-Rescue Staffing Model & Relief Pool	(0.5)
Maintenance Savings from Police Helicopter Fleet Replacement	(1.2)
<i>Total</i>	<i>\$ 18.2</i>

Review of Select Critical Strategic Expenditures: Funding Recommended for New Services or Enhancements

- **Parks & Recreation Department**
 - 14 new/expanded parks & 24 new Joint Use Facilities to open during the Outlook period
 - Expenses total \$6.2M in FY 2021, increasing to \$7.0M in FY 2025
- **Transportation & Storm Water Department**
 - New Storm Water Pipe Repair Team in response to June 2018 audit finding (net spending of \$3.5M)
 - New Sidewalk Repair & Replacement Teams, as well as additional sidewalk slicing contract funding, to reduce sidewalk maintenance backlog (net spending of \$3.6M)

Review of Select Critical Strategic Expenditures: Funding Recommended for New Services or Enhancements cont'd

- **Fire-Rescue Department**

- Continues to add Firefighter positions to build up the Relief Pool established in FY 2020 (37 FTEs, savings of \$451k in FY 2021)
- Four new fire stations in North University City (FY 2021, \$1.4M), Black Mountain Ranch (FY 2022, \$1.8M), Fairmont Avenue (FY 2024, \$2.0M), Paradise Hills (FY 2025, \$3.9M)
- Six Peak-Hour Engines – two each in FY 2021, FY 2022, & FY 2023 (total spending of \$6.6M in FY 2023)

- **Sustainability Department**

- Additional funding & positions for the Climate Resiliency Plan(\$442k) & for CAP Implementation (\$358k)

Review of Select Critical Strategic Expenditures: Funding Recommended for New Services or Enhancements cont'd

- **Information Technology**
 - Enterprise Asset Management (EAM) Phase II – \$529k in FY 2021 increasing to \$1.4M in FY 2025 for upgrades towards system improvements to support the rollout of additional departments in the EAM system
- **Library Department**
 - \$206k in FY 2021 in preparation for new Pacific Highlands Ranch branch library anticipated to open in February 2022 (FY 2022)
 - 9.5 FTEs & \$854k beginning in the first full year of operations
- **Police Department**
 - Addition of sworn positions beginning in FY 2022; 85.00 total FTEs to reach staffing goal at FY 2009 levels
 - Expenses total \$3.5M in FY 2022, increasing to \$12.7M in FY 2025

Prioritization of Critical Strategic Expenditures

Thoughtful Prioritization is Necessary

- Due to the size of the projected deficit, scrutinizing & prioritizing all of the Mayor's Critical Strategic Expenditures is essential.
- Our report breaks down the Mayor's Critical Strategic Expenditures into categories to clearly identify funding proposed for existing services versus new & expanded services.

Prioritization of Critical Strategic Expenditures cont'd

- Significant investments have been made in the implementation of existing homelessness & public safety services with the intent for them to be ongoing.
 - These services are important to the community & to those who benefit from them.
 - Nearly \$30M in new funding needs to be identified to continue homelessness & public safety services beyond FY 2020.
- Proposed new & expanded services, which require \$18.2M in new funding in FY 2021, are important to residents as well.
- If resources are limited, identifying ongoing funds to continue existing homeless & public safety programs should be a priority over new or expanded programs.

Potential Funding Needs Not Included in the Outlook

- **Citywide Program Expenditures: Companion Unit Fee Waiver**
 - The Companion Unit Fee Waiver is a popular existing program. As of November 2019, the full \$800k waiver allocation for FY 2020 has been spent in the first four months, which translates to more than 200 units
- **Environmental Services Department**
 - AB 939 fee increases are anticipated to address impacts from China's National Sword Policy; ongoing General fund impacts expected to be \$600k in FY 2021 & an additional \$600k in FY 2022

Potential Funding Needs Not Included in the Outlook cont'd

- **Employee Compensation – Negotiations with Labor Organizations**
 - FY 2021 contract negotiations are currently underway.
 - DoF's General Fund cost estimate for a 1% salary increase for City employees is about \$6.0M.
- **Fleet Department**
 - Kearny Mesa Repair Facility initiated with \$1.0M in FY 2020 but previous cost estimates ranged \$6.5M-17.0M
 - Also need funding for replacement/repairs of car/truck washes & shop equipment (\$7.6M General Fund)
 - Considered for Capital Infrastructure Planning Outlook
- **Homeless programs & services**
 - To the extent Council approves an expansion to the Women & Families Shelter, \$1.9M will be needed to continue the program beyond FY 2020
 - Updated HEAP expenditure projections suggest an additional \$1.2M is needed in FY 2021 to continuously fund HEAP-supported programs

Potential Funding Needs Not Included in the Outlook cont'd

- **Purchasing & Contracting Department**
 - Disparity study fully funded in FY 2020
 - If disparities identified, could require new program or changes to existing EOC program Plus repeating disparity study every 2-3 years to support ongoing program
- **Real Estate Assets**
 - Facility maintenance of emergency generators totaling \$194k & \$700k annually in rehab projects
- **Infrastructure**
 - \$1.5M for pavement condition assessments, & \$250k in facilities condition assessments

Future Financial Challenges

Potential challenges during the Outlook period

- Funding will need to be identified for future MOUs negotiated with employee organizations
- Latest estimate of General Fund infrastructure shortfall is \$1.86B
- Existing homeless programs & services need to be funded
- Potential pension issues - lower investment earnings or assumption changes; Proposition B
- Recession impacts on City revenue could be significant, timing unknown
- Projected Storm Water compliance needs (operational & capital) exceed current spending levels
- Vacancies, attrition, & recruitment difficulties continue as a trend

Potential Mitigation Measures

Possible actions & alternatives to address the projected deficit

- Budget reduction proposals (4% = \$63.6M)
 - Not all will be accepted, FY 2020 reductions were \$13.8M
- Alternative housing & homelessness funding
 - Homeless Housing, Assistance, & Prevention Program (HHAP) HHAP – Estimated \$20M one-time
 - Building Homes & Jobs Act – Estimated \$4.6M ongoing
 - Affordable Housing Fund – \$4.1M one-time
- Use of General Fund excess equity - \$22.1M of one time

Potential Mitigation Measures cont'd

- March 2020 Ballot Measure: “For a Better San Diego”
 - Estimated \$137M of TOT to address homelessness over the Outlook
 - Estimated \$8M for street repairs in FY 2025
 - Estimated \$10M to \$15M of new General Fund revenue once Convention Center expansion is opened (maybe FY 2025)
- Utilization of \$3.8M of the FY 2021 \$4.5M Pension Payment Stabilization Reserve contribution to pay for the General Fund increase to the ADC consistent with City Reserve Policy
- Paid refuse collection (Repeal of People’s Ordinance)
 - Collection service to single family homes represents \$34.5M annually that could be freed up for General Fund programs

Potential Mitigation Measures cont'd

- Redevelopment Property Tax Trust Fund (RPTTF) Lawsuit
 - The City could receive an estimated \$35M-40M in revenue pending the outcome of a lawsuit which is expected to be heard sometime in 2020.
- Stadium Revenue
 - Potential for \$7.6M in operating savings to the General Fund for FY 2021, & \$4.7M in ongoing Transient Occupancy Tax (TOT) Fund relief if sale proceeds are used for debt service, if purchase & sale agreement is complete by July 1, 2020.
- Storm Water fee increase
 - The City could raise approximately \$6M for each \$1.00 (charged per parcel per month) that the fee is increased (current fee is \$0.95 per parcel per month).

Summary & Conclusions

The Outlook, as well as this Report, allows the Council to begin identifying its top budget priorities & develop a strategy for achieving a balanced budget in FY 2021

Summarized below are some key guidelines that emerged from our Office's review of the Mayor's FY 2021-2025 Five-Year Financial Outlook for Council's consideration during the FY 2021 budget process:

- Some mitigation actions for addressing the deficit are available but are likely not sufficient.
- Existing, unfunded priority services versus new, expanded services need to be carefully prioritized.
- Efforts should be made to identify ongoing funding for existing unfunded services that are determined to be a priority.

Summary & Conclusions cont'd

- Not considered in the Outlook are any estimates for potential FY 2021 compensation increases for employee organizations, negotiations are underway & funding will need to be identified for the outcomes.
- Delaying or cutting back of proposed new/expanded services will likely need to be considered.
- The timing of a potential recession is an unknown but should be kept in mind when making future expenditure decisions.
- Sources for new or increased ongoing revenues should be considered within the Outlook period.