EXECUTIVE SUMMARY

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

Date Issued: December 8, 2015 **IBA Report Number:** 15-43

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Item Number: TBD

IBA'S REVIEW OF THE MAYOR'S FY 2017-2021 FIVE-YEAR FINANCIAL OUTLOOK

This report provides a thorough review of the FY 2017-2021 Five-Year Financial Outlook (Outlook) and includes an analysis of the Outlook's five years of General Fund revenue and expenditure projections, General Fund and Risk Management reserves, department operating and capital requests (those that were included in the Outlook in support of the Mayor's four priority initiatives, as well as requests submitted but not accepted), and a summary of known, likely, or possible impacts to the projections included in the Outlook.

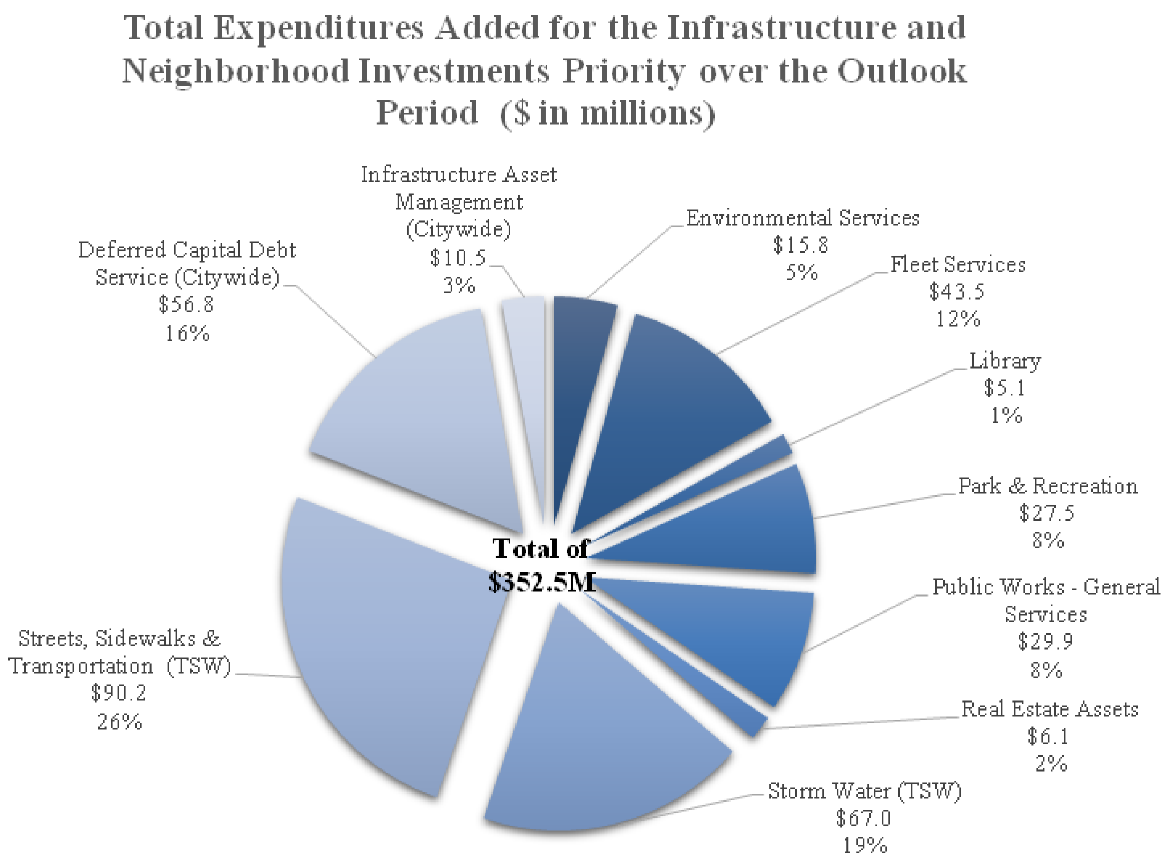
The Outlook projects revenues in excess of baseline expenditures in each year, ranging from $49.1 million in FY 2017 to $184.9 million in FY 2021. Growth in year-over-year revenues is mostly due to projected increases in major General Fund revenues; total baseline revenue in the Outlook grows from $1.31 billion in FY 2017 to $1.50 billion in FY 2021. This represents growth of 3.7% over last year's FY 2016-2020 Outlook. General Fund expenditures in this year's Outlook have also increased over last year's: expenditures in FY 2020 increased by $66.1 million, or 5.3%.

($ in millions)	FY 2017 Outlook	FY 2018 Outlook	FY 2019 Outlook	FY 2020 Outlook	FY 2021 Outlook
Baseline General Fund Revenues	$ 1,309.1	$ 1,356.2	$ 1,406.	$ 1,455.7	$ 1,501.9
Baseline General Fund Expenditures	1,260.0	1,278.4	1,292.3	1,306.2	1,317.0
Baseline Revenues in Excess of Expenditures	**49.1**	**77.9**	**113.8**	**149.5**	**184.9**
Priority Initiatives General Fund Revenues	2.0	2.1	1.5	1.6	1.6
Priority Initiatives General Fund Expenditures	50.8	72.1	90.2	104.7	112.8
Total Revenues in Excess of Expenditures	**$ 0.2**	**$ 7.9**	**$ 25.1**	**$ 46.4**	**$ 73.7**

The Mayor also identified $430.6 million in new expenditures over the Outlook period to address his four priority initiatives:

- Infrastructure and Neighborhood Investment
- Public Safety
- Technology Improvements
- Customer Service and Open Government

Funding for the Infrastructure and Neighborhood Investment priority initiative more than doubles from $41.6 million in FY 2017 to $94.0 million in FY 2021, and fulfills the Mayor's goal of pledging 50% of new revenues to investments in infrastructure. Total new investment in this initiative over the Outlook period is $352.5 million, an increase of $113.2 million or 47.3% over last year's Outlook. A significant portion of this increase is explained by the inclusion of $43.5 million in expenses for the Fleet Services Division's planned vehicle and equipment purchases, although other large infrastructure expenditures include deferred capital debt service, and various streets and storm water projects in the Transportation & Storm Water Department. The following chart provides a breakout of the various categories of expense within the Infrastructure and Neighborhood Investment Priority Initiative as identified in the Outlook:



New funding for the other three priority initiatives over the Outlook is significantly less than in the Infrastructure and Neighborhood Investments priority: Public Safety - $58.8 million, Technology Improvements - $13.3 million, and Customer Service and Open Government - $6.0 million.

In this report we discuss items that the Mayor funded as part of his priority initiatives, but we also note that important requests submitted by departments totaling $498.8 million were not funded in the Outlook. Of these submissions, $418.1 million was requested by the Transportation & Storm Water Department (TSW) primarily for flood risk management and storm water quality capital needs. Our Office notes the underfunding of TSW as a concern and considers it likely that additional storm water funding will be required over the period of the Outlook.

Finally, our report identifies a number of "known," "likely," and "possible" expenditure and revenue issues that could impact the Mayor's Outlook projections. We consider "known" items to be those where an action has occurred causing the impact, although the amount of the impact identified could vary due to other factors; "likely" items have a reasonable chance of occurring based on historical experience or the criticality of the issue; and "possible" items could occur if required actions take place or in some cases, if economic conditions change. The following sections discuss impacts to the Outlook and are included in greater detail in the body of our report.

"KNOWN," "LIKELY," OR "POSSIBLE" IMPACTS TO THE OUTLOOK

<u>Impacts on Revenue Projections</u>

Overstated Redevelopment Property Tax Trust Fund (RPTTF) Payments (Known)

The Outlook includes RPTTF tax sharing/pass-through and residual payments (formerly tax increment) associated with each Recognized Obligation Payments Schedule (ROPS) period. We believe both sets of payments in the Outlook are overstated, largely because the Outlook was released prior to the State's implementation of SB 107. The table below shows the possible effects on the Outlook's RPTTF projections after adjustments to pass-through payments and residual distributions are made.

($ in millions)	**FY 2016**	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Pass-Through (Outlook)	$4.4	$4.4	$4.6	$4.8	$4.9	$5.1
Residual RPTTF (Outlook)	9.4	15.1	18.5	21.1	24.0	25.2
Total Outlook	**13.8**	**19.5**	**23.1**	**25.9**	**28.9**	**30.3**
Pass-Through (Adjusted)	3.4	3.4	3.5	3.7	3.8	4.0
Residual RPTTF (Adjusted)	9.3	14.3	17.5	20.0	22.7	23.7
Total Adjusted[1]	**12.7**	**17.6**	**21.1**	**23.7**	**26.5**	**27.7**
Difference	**($1.1)**	**($1.9)**	**($2.0)**	**($2.2)**	**($2.4)**	**($2.6)**

[1] Pass-through and residual RPTTF amounts reflect adjusted tax-sharing and assume a $5.0 million increase in each future ROPS

Risk Scenarios for Property Tax and TOT Projections (Possible)

While we are comfortable with the Outlook's overall revenue projections, we believe that the "risk" scenarios to the property tax and TOT projections presented in the Outlook should be carefully considered. Economic indicators surrounding these projections remain positive, though some slowdown risks exist, and are detailed in our report.

Impacts on Expenditure Projections

Estimated ADC Increases Due to Lower than Assumed Investment Returns (Known)

The Outlook's defined benefit pension forecasts through FY 2021 are based on the most recently provided Actuarially Determined Contribution (ADC) projections from the San Diego City Employees' Retirement System's (SDCERS) June 30, 2014 actuarial valuation. However, the FY 2014 valuation ADC figures are expected to be impacted by subsequent events including the FY 2015 investment return of 3.3%, which is lower than the 7.25% return assumed in the FY 2014 report. Other positive and negative impacts to the Outlook's ADC figures related to demographic assumptions have not yet been determined. Because of the complexity of the pension system variables, the total of all effects on the ADC is unknown at this time. The table below shows preliminary estimated increases to the Outlook's expenditures for the lower investment return.

($ in millions)	**FY2017**	**FY2018**	**FY2019**	**FY 2020**	**FY 2021**
Investment Changes	$ 4.4	$ 8.2	$ 11.4	$ 14.2	$ 16.5

Estimated ADC Increase Due to Economic Assumption Changes (Known)

In November 2015, the SDCERS Board made changes to economic assumptions that will be included in the calculations of the FY 2017 ADC. Changes were made to both the discount rate and the wage inflation rate assumptions. The Board approved a 0.125 reduction for both factors for the FY 2015 and FY 2016 valuations. The table below shows preliminary estimated increases to the Outlook's expenditures.

($ in millions)	**FY2017**	**FY2018**	**FY2019**	**FY 2020**	**FY 2021**
Changes to Economic Assumptions	$ 4.4	$ 9.1	$ 9.8	$ 10.5	$ 11.2

Labor Agreement Reopeners for Employee Organizations (Likely at Some Level)

The City recently reached multiple-year labor agreements (ending FY 2020) with the San Diego Police Officers Association (POA) and the San Diego Municipal Employees Association (MEA), the related costs of which are reflected in the Outlook. The current five-year agreements with the City's four other employee organizations include reopeners which allow for negotiation over non-pensionable compensation for FY 2017 and FY 2018. If a labor agreement is negotiated that extends beyond FY 2018, pensionable salaries may be considered. Though the Outlook appropriately does not anticipate any related impact, each 1% compensation increase would total approximately $1.8 million for the General Fund. The table on the following page reflects the five-year impact on expenditures for each 1% annual increase. Actual results of labor negotiations are unknown at this time and could be higher.

Illustrative Cost for Employees Other Than POA & MEA					
($ in millions)	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Estimated Cost for Each 1% Annual Compensation Increase	$ 1.8	$ 3.6	$ 5.4	$ 7.2	$ 9.0

Note that the estimated figures above do not include San Diego City Employees Retirement System (SDCERS) pension impacts that may be applicable, or any compounding effects that may occur.

Police Department Overtime - Anticipated Expenditures in Excess of Outlook (Likely)

We note that the Police Department is projected to exceed budgeted overtime expenditures by $5.0 million for a total of $23.0 million in FY 2016, which lines up with actual expenditures of $23.1 million in the prior year. While not included in the Outlook projections, we anticipate that the Department's base budget for personnel expenditures will exceed Outlook assumptions by a range of $3-$5 million for each year of the Outlook as shown in the table below. This is based on our review of past overtime expenditures as well as the Department's current focus on extension-of-shift activities, a need which we do not see changing significantly over the next five years. The table below shows the projected impact on the Outlook.

($ in millions)	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Projected Overtime Expenditures	**$3.0-5.0**	**$3.0-5.0**	**$3.0-5.0**	**$3.0-5.0**	**$3.0-5.0**

Storm Water Additional Funding Needs (Likely at Some Level)

The Municipal Storm Water Permit adopted by the Regional Water Quality Controls Board (RWQCB) in May 2013 established stringent water quality with deadlines that begin in 2018. The Storm Water Division uses a Watershed Asset Management Plan (WAMP) to estimate funding requirements for both operating and capital needs. The City will incur significant penalties if it is unable to meet storm water regulations by 2018. While the Outlook fully funds Storm Water operations and maintenance, a gap remains in capital funding for storm water projects. No other major funding source exists for these critical projects outside of the General Fund. Even after successful negotiations with the RWQCB to reduce overall compliance costs (which are reflected in the Outlook), these costs remain high. The table below shows the total costs identified in the WAMP, the funding included in the Outlook, and the resulting funding gap.

($ in millions)	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Total Need	$120.6	$127.9	$142.4	$149.5	$156.1
Funding Included in Outlook	75.0	75.1	83.1	66.5	66.9
Funding Gap	**$45.6**	**$52.8**	**$59.3**	**$83.0**	**$89.1**

Unmet Funding of Prior Council Actions

Penny for the Arts Blueprint and Library Appropriation Ordinance (Possible)

The City Council has adopted plans that commit to providing ongoing funding that represents a fixed percentage of revenues and expenditures for the City's libraries and arts programs. Historically, the City has not allocated the full amounts prescribed under those plans, and instead provided budgets for those programs based on their needs each year.

We note that the Outlook continues this practice, and does not provide funding at levels consistent with the Blueprint and Ordinance; additional discussion of these programs is included in our report.

Departmental Requests, Other Items Not Funded in Outlook (Likely at Some Level)

The Outlook provides a list of unfunded departmental requests which total approximately $430.6 million over the five-year period. Of this, $418.1 million or 84.7% of the funding was requested by the Storm Water Division as discussed above. Typically a sizable number of the requests not included in the Outlook are ultimately funded in annual budgets as more information is gathered regarding their importance. Our Office notes that requests not included in the Outlook that may be of interest to the Council and community, include additional Fire brush management staff, increased library service hours at Central Library and the branches, expanded hours at recreation centers, additional sworn and civilian positions based on the Department's Five-Year Plan, and Public Works' contract specialist staff to support CIP contracts, to name a few.

Significant Policy Initiatives Under Consideration that Could Impact the Outlook Period and Beyond

Potential General Fund Reserve Options Being Considered

There have been discussions over the past several months about modifying the City's Reserve Policy to set aside additional reserve funds beyond those currently required, in order to better prepare for unanticipated increases in the City's annual pension payments. The following sections discuss the alternative proposals being considered to address this matter. Both alternatives would have an impact on the Outlook projections if enacted, and are planned to be considered by the full City Council in January.

New Pension Payment Stabilization Reserve (Possible)
The Mayor has proposed creating a separate Pension Reserve Fund to mitigate pension payment volatility arising from unanticipated increases to the City's ADC. The proposal sets aside $16.3 million in General Fund Excess Equity and $4.9 million from Enterprise Funds for this purpose. The Pension Reserve would only be used to fund unanticipated pension payment increases. The table on the following page shows the impact on the Outlook of establishing this new reserve, which reduces FY 2016 Excess Equity.

Projected Amount Available for Additional City Services After Five-Year Outlook Baseline Expenditures, Priority Initiatives, and Pension Reserve Funding						
($ in millions)	**FY 2016***	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Available Amount Per Outlook*	$ 31.3	$ 0.2	$ 7.9	$ 25.1	$ 46.4	$ 73.7
Amount for New Pension Reserve	(16.3)	-	-	-	-	-
Amount Available for City Services	**$ 15.0**	**$ 0.2**	**$ 7.9**	**$ 25.1**	**$ 46.4**	**$ 73.7**

*For FY 2016, the "Available Amount per Outlook" is the projected ending Excess Equity in the First Quarter Budget Monitoring Report (adjusted to incorporate updated revenue figures from the Office of the City Comptroller). The FY 2016 "Amount Available for City Services" is the adjusted ending Excess Equity amount remaining after funding the new Pension Reserve.

Increasing the Existing General Fund Stability Reserve from 14% to 16% (Possible)

The Budget and Government Efficiency Committee (B&GE) recently considered an alternative to establishing a separate Pension Fund Reserve, and that would increase the existing General Fund Reserve from 14% to 16% of operating revenues. This increase would be accomplished by maintaining the Emergency Reserve at 8% and increasing the Stability Reserve from 6% to 8%. The Stability Reserve could be earmarked for unanticipated pension payment increases in addition to other purposes restricted per existing Council policy. Increasing the General Fund Reserve in this manner requires $22.7 million in General Fund Excess Equity to be transferred to the Stability Reserve. The table below depicts the estimated impact on the Outlook as a result of reducing FY 2016 Excess Equity to grow the reserve to 16%.

Projected Amount Available for Additional City Services After Five-Year Outlook Baseline Expenditures, Priority Initiatives, and 16% Reserve Funding						
($ in millions)	**FY 2016***	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Available Amount Per Outlook*	$ 31.3	$ 0.2	$ 7.9	$ 25.1	$ 46.4	$ 73.7
Amount for 14% Reserve Maintenance	-	(4.6)	(2.2)	(5.8)	(5.9)	(6.7)
Additional Amount for 16% Reserve	(22.7)	(0.7)	(0.3)	(0.8)	(0.8)	(1.0)
Amount Available for City Services	**$ 8.6**	**$ (5.0)**	**$ 5.3**	**$ 18.4**	**$ 39.6**	**$ 66.0**

*For FY 2016, the "Available Amount per Outlook" is the projected ending Excess Equity in the First Quarter Budget Monitoring Report (adjusted to incorporate updated revenue figures from the Office of the City Comptroller). The FY 2016 "Amount Available for City Services" is the adjusted ending Excess Equity amount remaining after funding the General Fund reserve to a 16% level.

The Stability Reserve option requires $22.7 million in Excess Equity compared to the Pension Reserve which requires $16.3 million, a difference of $6.4 million.

Proposed "Firehouse Bond" (Possible)

A potential future impact to the Outlook is the current conceptual proposal for a "Firehouse Bond" in November of 2016. The proposal, developed by Council President Pro Tem Emerald, calls for a $200 million general obligation bond supported by a property tax increase, to fund design, land acquisition, construction, and apparatus purchases for 17 new fire stations. This dedicated funding source would complete all Citygate-recommended fire stations.

It is difficult to predict the specific General Fund impacts of a successful Firehouse Bond until a construction schedule has been determined and operating budget impacts analyzed. However, the known impacts to this Outlook and future Outlooks would include costs associated with staffing and operating the stations. Each new fire station would require ongoing General Fund expenditures of $2.2 million annually to support 12.00 FTE firefighters and related equipment. Total annual operating costs for all 17 fire stations are estimated at $37.4 million upon full build out, which would be staggered over a number of years that are yet to be determined. Additionally, expenditures for ongoing maintenance and repair would be necessary.

"Rebuild San Diego": Shift Sales Tax Growth, Pension Payment Savings for Infrastructure (Possible)

On December 2, 2015 Councilmember Kersey announced a conceptual ballot proposal for June of 2016 that would capture a portion of General Fund revenue growth and any pension payment savings over FY 2016 amounts over a 30-year period, and dedicate it to infrastructure-related expenditures. While specifics of the proposal are still being developed, if sales tax revenue growth over 1% were to be set aside for infrastructure-related items an estimated $81.0 million over the Outlook period would be dedicated to this specific purpose. A majority of the Mayor's $430.6 million in new funding for his Priority Initiatives during this period are identified as infrastructure-related expenses and would likely be eligible for this funding. However, other non-infrastructure programmatic and service priorities, whether in the Outlook or not, would be ineligible.

Environmental Growth Fund Charter Revisions (Possible)

The Charter Review and Environment Committees have discussed possible revisions to the Charter to clarify eligible uses of the Environment Growth Fund (EGF). Currently, two-thirds of the EGF is to be utilized solely for the purpose of acquiring open space lands; however, if anticipated revenues in any given year are insufficient to maintain existing City services related to the environment, this rule can be suspended. The City has suspended the expenditure rule for several years, and today it primarily uses EGF funds for maintenance expenses in the City's Developed Regional Parks and Open Space Parks. At the Charter Review Committee meeting on December 3, 2015, the Committee decided against amending the Charter's EGF provisions, and instead expressed interest in reducing or eliminating the ability to suspend the two-thirds requirement.

Approximately $10.8 million in EGF revenue was budgeted in the FY 2016 Adopted Budget for the two-thirds portion of the EGF, and allocated for Park & Recreation park maintenance expenses. If the City's ability to use this revenue for park maintenance expenses is reduced or eliminated and existing service levels are to be maintained, up to $10.8 million would need to be identified in other sources (potentially including the General Fund).

Summary of Known, Likely, and Possible Impacts to the Outlook

The table on the following page summarizes potential impacts to the Outlook for the items we have identified in our report, where funding impacts could be determined.

($ in millions)	FY 2017 Outlook	FY 2018 Outlook	FY 2019 Outlook	FY 2020 Outlook	FY 2021 Outlook
Outlook Projected Revenues in Excess of Expenditures after Funding Initiatives[1]	**$ 0.2**	**$ 7.9**	**$ 25.1**	**$ 46.4**	**$ 73.7**
Summary of Known Impacts to the Outlook					
RPTTF Payments Overstated	1.9	2.0	2.2	2.4	2.6
ADC - Investment Changes[2]	4.4	8.2	11.4	14.2	16.5
ADC - Changes to Economic Assumptions[2]	4.4	9.1	9.8	10.5	11.2
Sub-total Known Impacts	**$10.7**	**$19.4**	**$23.4**	**$27.**	**$30.4**
Summary of Likely Impacts to the Outlook					
Police Department Overtime	3.0-5.0	3.0-5.0	3.0-5.0	3.0-5.0	3.0-5.0
Storm Water Additional Funding Needs	45.6	52.8	59.3	83.0	89.1
Labor Agreement Reopeners for Employee Organizations[3]	1.8	3.6	5.4	7.2	9.0
Sub-total Likely Impacts	**$50.4-52.4**	**$59.4-61.4**	**$67.7-70.7**	**$93.2-95.2**	**$101.1-103.1**
Summary of Possible Impacts to the Outlook					
Risk Scenario for Property Tax	-	-	15.5	21.4	27.5
Risk Scenario for TOT	-	-	3.4	4.8	6.3
Penny for the Arts	6.4	6.8	7.1	7.5	7.8
Library Ordinance	29.3	31.4	3.2	33.4	34.9
Proposed Firehouse Bond	TBD	TBD	TBD	TBD	TBD
"Rebuild San Diego": Sales Tax Growth, Pension Payment Savings to Infrastructure	TBD	TBD	TBD	TBD	TBD
Potential Environmental Growth Fund Charter Revisions	TBD	TBD	TBD	TBD	TBD
Sub-total Possible Impacts	**$35.8**	**$38.2**	**$29.4**	**$67.1**	**$76.5**

[1]Amounts remaining after accounting for the Baseline Expenditures and Priority Initiatives.

[2]Other positive or negative impacts to the Outlook's ADC figures that are related to demographic assumptions have not yet been determined. Because of the complexity of the pension system variables, the total of all effects on the ADCs is unknown at this time. The preliminary estimates above are only presented as a conservative approach to considering the reliability of any projected Outlook revenues in excess of expenditures.

[3]Amounts represent estimates for 1% annual compensation increases for the four employee organizations other than POA and MEA. Actual results of negotiations are unknown at this time and could be higher.

CONCLUSION

The Mayor's Five-Year Outlook provides an accurate overview of the City's expected revenues, municipal services, and the Mayor's own goals and priorities. Revenue projections and economic growth assumptions in the Outlook are largely appropriate and reasonable, though some changes to RPTTF revenue figures may be necessary.

As is noted in the Outlook itself, the Outlook is not a budget, but is instead a plan that helps the City guide its long-range fiscal planning efforts, while serving as the framework for development of the City's FY 2017 Proposed Budget. It is nevertheless important to recognize that the City has many priorities, programs, and needs that all compete for funding, even in improved economic times. As examples of programmatic needs and policy commitments, the City's storm water program, Library Ordinance, and Penny for the Arts program all have additional funding needs beyond what is included in the Outlook.

If full funding for existing programs and commitments were included in the Outlook, the surpluses currently projected would turn into deficits. It is reasonable and appropriate to project increased revenues in future years, but decisions regarding what programs should receive additional funding still need to be made. Council and community input will continue to be critically important in making those decisions.

THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

Date Issued: December 8, 2015 **IBA Report Number:** 15-43
City Council Docket Date: December 14, 2015
Item Number: TBD

IBA's Review of the Mayor's FY 2017-2021 Five-Year Financial Outlook

OVERVIEW

On November 13, 2015 Mayor Faulconer released his Five-Year Financial Outlook (Outlook) for FY 2017-2021. To arrive at projected revenues in excess of expenditures (surplus) for each year of the Outlook, the Mayor established the baseline projection for current operations for FY 2017-2021, and then identified his Priority Initiatives and the costs associated with carrying out those initiatives over the Outlook period. The Priority Initiatives identified in the Outlook are Infrastructure and Neighborhood Investment, Public Safety, Technology Improvements, and Customer Service and Open Government. The Customer Service and Open Government priority initiative is the only change from the prior year's Outlook; it replaces last year's Transparency and Open Data initiative.

The Outlook projects revenues in excess of baseline expenditures in each year, ranging from $49.1 million in FY 2017 to $184.9 million in FY 2021, mostly due to projected increases in major General Fund revenues. Total baseline revenue in the Outlook grows from $1.31 billion in FY 2017 to $1.50 billion in FY 2021—an increase of 3.7% over last year's FY 2016-2020 Outlook. General Fund expenditures in this year's Outlook have also increased over last year's: expenditures in FY 2020 increased by $66.1 million, or 5.3%.

This year's Outlook allocates the majority of its projected surpluses (revenue projection minus baseline expenditures) to the Infrastructure and Neighborhood Investment priority initiative—approximately $41.6 million in expenditures or 81.9% of FY 2017 Priority Initiative spending, with substantial increases up to $94.0 million projected in FY 2021. Public Safety support is increased by $4.9 million in the first year of the Outlook and this number nearly triples in FY 2018 to $13.4 million. The last two initiatives are allocated a total of approximately $4.3 million in FY 2017: $3.0 million for Technology Improvements and $1.3 million for Customer Service and Open Government.

In this report we provide a review of the surpluses reported in the Outlook, an analysis of the items that are funded and unfunded over the five-year period, and a discussion of other real or potential impacts to the Outlook. We also review the General Fund revenue and baseline expenditure projections included in the Outlook, General Fund and Risk Management reserves, City programs and services allocated funding as part of the Mayor's Priority Initiatives, and some of the funding requests submitted by departments that were not included in the Outlook. We conclude with a review of whether these items will have a known, likely, or possible impact upon the General Fund over the next five years, and consider other issues not included in the Outlook—such as changes to the City's Actuarially Defined Contribution (ADC), potential future labor negotiations, or changes to the General Fund reserves.

REVIEW OF GENERAL FUND REVENUES

Economic Overview

The economic downturn or 'Great Recession' that occurred in and around 2008, resulted in major investment losses for the City, as well as the reduction of the City's major General Fund revenues. Faced with rising costs and declining revenue, the Mayor and City Council made difficult decisions about what City services to reduce in order to maintain a balanced budget, balancing concerns voiced by residents, mandated City services, public safety needs, and other priorities. City revenues have increased since that time, and the current Mayor and City Council have utilized recent budget surpluses and projected revenue increases to restore services, increase City reserves, boost employee compensation, and address needed investments in infrastructure. The FY 2017-2021 Five-Year Forecast projects additional surpluses over the next five years as the economy continues its post-recession recovery and stabilizes at lower rates of growth.

As noted in the Outlook, over the next five years Major General Fund revenues are projected to maintain current positive growth trends based upon a number of variables including continued increases in property value, low unemployment figures, and higher consumer confidence. Current positive revenue trends cool in the outer years of the Outlook as growth rates normalize to reflect a more stable economy as opposed to an economy in recovery. The Outlook also includes alternative scenarios that suggest risks to revenue projections: concerns include rising interest rates that may affect home and major consumer purchases, a reduction in leisure and business travel, and an increase in the unemployment rate.

Our Office notes that in addition to the risks outlined in the Outlook the recovery from the Great Recession in San Diego, as in the rest of the country, has been positive but inconsistent. For instance, while there have been increases in home prices and sales as well as in consumer confidence, there have also been sustained declines in the monthly Index of Leading Economic Indicators for San Diego County[1], and concerns that housing prices are rising to a level that is increasingly inaccessible to many San Diego residents[2]. Differences in the trajectory of economic indicators can lead to conflicting analyses between economists and make it more challenging to project future changes in revenue.

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[1] USD Index of Leading Economic Indicators: September 2015, August 2015, and July 2015. http://home.sandiego.edu/~agin/usdlei/

[2] Molnar, Phillip "Priced out? Home prices marginally creep up" The San Diego Union-Tribune. November 24, 2015. http://www.sandiegouniontribune.com/news/2015/nov/24/home-prices-up-september/

The sometimes contradictory nature of current economic indicators make economic forecasting more difficult and we appreciate the nuanced approach to revenue projections in the Outlook. While our Office believes that the positive revenue projections included in the Outlook are generally appropriate—including the slowdown in projected revenue growth in the outer years—we also discuss the possibility in the outer years of the Outlook, of the alternative scenarios for property tax and transient occupancy tax (TOT) that were included in the Outlook's major General Fund revenue discussions.

General Fund Revenues

In FY 2016, the major General Fund revenues of property tax, sales tax, TOT, and franchise fees make up approximately 73.2% of all General Fund revenues. Any changes, positive or negative, to the growth rate of any of these revenues can result in an increase or deficit of millions of dollars in General Fund revenues that support the majority of the City's services. Due to the potential for changes in economic variables when projecting major General Fund revenue growth over a period of five years, the Outlook includes alternative scenarios to its revenue projections that identify risks to growth and corresponding reduced growth rates. The table below displays the difference between the Outlook's current and alternative scenario for each of the major General Fund revenues discussed in this section. The differences (decreased revenues) between the two scenarios are discussed in greater detail in the sections below.

Difference Between Major General Fund Revenue Scenarios ($ in millions)

		FY 2017		FY 2018		FY 2019		FY 2020		FY 2021		
	Scenario	**Growth Rate**	**Projection**	**Growth Rate**	**Projection**	**Growth Rate**	**Projection**	**Growth Rate**	**Projection**	**Growth Rate**	**Projection**	**Total**
Property Tax	**Current**	5%	$498.3	4.5%	$523.1	4%	$545.7	3.5%	$566.8	3%	$584.2	
	Alternative	4%	493.5	3.5%	513.1	3%	530.1	2.5%	545.4	2%	556.7	
Difference			4.8		10.0		15.5		21.4		27.5	79.2
Property Transfer Tax	**Current**	3%	9.5	3%	9.7	2.5%	10.	2.5%	10.2	2.5%	10.5	
	Alternative	2%	9.4	2%	9.5	1.5%	9.7	1.5%	9.8	1.5%	10.0	
Difference			0.1		0.2		0.3		0.4		0.5	1.5
Sales Tax	**Current**	4%	278.8	4%	289.9	3.5%	299.8	3.5%	310.2	3%	319.2	
	Alternative	3%	275.5	3%	283.8	2.5%	290.5	2.5%	297.8	2%	303.4	
Difference			3.3		6.2		9.2		12.5		15.8	46.9
TOT	**Current**	6%	110.3	5.5%	116.4	5%	122.2	5%	128.3	4.5%	134.1	
	Alternative	5%	109.3	4.5%	114.2	4%	118.7	4%	123.5	3.5%	127.8	
Difference			1.0		2.2		3.4		4.8		6.3	17.7
Franchise Fees	**Current SDG&E**	3.3%	82.5	3%	84.2	3%	85.9	3.3%	87.7	3%	89.5	
	Current Cable	0%		0%		0%		0.0%		0%		
	Alternative SDG&E	2.3%	81.9	2.3%	82.8	2.3%	83.8	2.3%	84.8	2.3%	85.9	
	Alternative Cable	-1%		-1%		-1%		-1%		-1%		
Difference			0.7		1.4		2.1		2.9		3.6	10.6
TOTAL DIFFERENCE			**$9.9**		**$19.9**		**$30.6**		**$41.9**		**$53.7**	**$156.0**

Property Tax

The Outlook includes the property tax year-end projection of approximately $470.4 million included in the First Quarter Budget Monitoring Report (First Quarter Report) as the basis for its projection. A number of assumptions are included in the baseline calculation, including:

- An approximate 1.6% increase in the California Consumer Price Index (CCPI) in October 2015
- Continued positive growth of the City's assessed valuation

Since the release of the Outlook an updated CCPI of 1.5% has become available, which is very close to the 1.6% assumed in the Outlook. The Case-Shiller home-price index for September has also been released and includes a 6.6% increase in San Diego County home prices over the previous year, an increase over the 5.9% reported in the Outlook for August. However, these positive indicators are tempered somewhat by speculation that the Federal Reserve will raise interest rates before the end of the year thereby potentially cooling the housing market, as well as concerns that rising home prices in San Diego will mean a slow-down in purchases as homes become priced out of reach of residents. The Outlook reflects these risks as it assumes that there will be a slowing of property tax revenue growth in the outer years. While it is possible that an increase in interest rates or a reduction in market activity will result in a reduction in revenue growth, it is unlikely that changes would affect the FY 2017 projection. It is difficult to predict, however, whether the projected slowdown in the outer years will more closely follow the Outlook's baseline scenario or the more conservative alternative scenario. If the real estate market cools during the last three years of the Outlook to the levels projected in the alternative scenario, Property Tax revenues would be reduced by a total of approximately $64.5 million: $15.5 million in FY 2019, $21.4 million in FY 2020, and $27.5 million in FY 2021.

Our Office notes that there are changes to the property tax projection for the next fiscal year due to changes to Redevelopment Property Tax Trust Fund (RPTTF) projections that were identified after the Outlook was released; these changes are detailed in the following section.

Property Tax - RPTTF

Per the dissolution of California redevelopment agencies (RDAs) in February 2012, the City receives additional property tax revenue from the RPTTF, including both tax sharing/pass-through payments and residual payments associated with each Recognized Obligation Payment Schedule (ROPS) period. The Five-Year Outlook includes the following tax sharing/pass-through payments: $4.4 million in FY 2017, $4.6 million in FY 2018, $4.8 million in FY 2019, $4.9 million in FY 2020, and $5.1 million in FY 2021. The Outlook also includes residual distributions based on anticipated ROPS periods. Distributions are anticipated to increase over time as various enforceable obligations are paid off and the total assessed property values in the redevelopment project areas are increased. The Outlook includes $15.1 million in residual payments in FY 2017, $18.5 million in FY 2018, $21.1 million in FY 2019, $24.0 million in FY 2020, and $25.2 million in FY 2021.

Both sets of RPTTF payments—those associated with tax sharing/pass-through payments and residual distributions may be overstated, as discussed below:

<u>Tax Sharing/Pass-Through Payments</u>
In October, the Council rescinded the suspension of the City's receipt of revenues from the City Heights Redevelopment Project Area. This should have the effect of reinstating a pass-through agreement for the City Heights area, and increase anticipated redevelopment pass-through payments by $1.0 million each fiscal year. However, the San Diego County Auditor and Controller is responsible for making pass-through payments and has not recognized this reinstatement; City staff is currently working with the County to ensure recognition of the

reinstated pass-through agreement. Until an agreement with the County has been reached, however, it may be appropriate to exclude associated revenues from the Outlook.

Residual RPTTF Payments

As noted in the Outlook, passage of SB 107 allowed the City to include enforceable obligations on future ROPS that had been denied in the past. As Residual RPTTF payments are made from property tax increment funding that remains after enforceable obligations have been paid, increased enforceable obligations leads to decreased residual payments.

The Outlook's calculations for RPTTF included a number of reinstated agreements that were included in the latest ROPS submitted to the State, but did not include a reinstatement of the long-term miscellaneous debt repayment agreement due to the State's long-standing denial of this obligation. However, the State has indicated that, due to the passage of SB 107, it will begin to recognize this as an enforceable obligation.

Civic San Diego requested $500,000 related to the long-term miscellaneous debt agreement in the most recent ROPS, which covered the first six months of 2016. If a similar amount is included in each future ROPS, this will increase funding dedicated to enforceable obligations by $1 million each year, and decrease the pool of residual RPTTF by the same amount. However, it is likely that the funding requested in future ROPS will exceed $1 million, as the total outstanding long-term miscellaneous debt as of FY 2016 is $151.5 million. If $5 million were included in ROPS for this purpose each year, the total balance would be paid off in approximately 30 years.

The first table below indicates projections included in the Outlook. The second and third tables contain projections based on increasing future ROPS by $1 million and $5 million respectively.

Pass-Through and RPTTF Revenue as Included in Five-Year Outlook (*$ in millions*)

	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021
Pass-Through	$4.4	$4.4	$4.6	$4.8	$4.9	$5.1
Residual RPTTF	9.4	15.1	18.5	21.1	24.0	25.2
Total	**$13.8**	**$19.5**	**$23.1**	**$25.9**	**$28.9**	**$30.3**

Pass-Through and RPTTF Revenue with Adjusted Tax-Sharing and $1M Increase in Each Future ROPS (*$ in millions*)

	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021
Pass-Through	$3.4	$3.4	$3.5	$3.7	$3.8	$4.
Residual RPTTF	9.3	15.0	18.2	20.7	23.4	24.4
Total	**$12.7**	**$18.3**	**$21.8**	**$24.4**	**$27.2**	**$28.4**

Pass-Through and RPTTF Revenue with Adjusted Tax-Sharing and $5M Increase in Each Future ROPS (*$ in millions*)						
	FY 2016	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Pass-Through	$3.4	$3.4	$3.5	$3.7	$3.8	$4.
Residual RPTTF	9.3	14.3	17.5	20.0	22.7	23.7
Total	**$12.7**	**$17.6**	**$21.1**	**$23.7**	**$26.5**	**$27.7**

Property Transfer Tax

The First Quarter Report includes an approximately $807,000 increase in Property Transfer Tax over the FY 2016 Adopted Budget, and the projected year-end revenue of $9.2 million was included in the Outlook as part of the General Fund base revenue. The Outlook projects five years of (diminishing) positive growth for Property Transfer Tax, based on the same economic indicators discussed in the Property Tax section above.

Property Transfer Tax shares the same risks as Property Tax, but because this revenue source is based upon volume of transactions (properties sold within a year) as opposed to ongoing assessed valuation, any sudden changes in the variables assumed in the Outlook—such as an increase in the federal interest rate—could produce significant changes to the FY 2016 year-end projection and require updates to the Outlook for this revenue before the FY 2017 budget is proposed. Our Office notes, however, that absent any sudden changes to the variables assumed in the Outlook, the current scenario is appropriate as it reflects a gradual increase in interest rates and a corresponding slight slow-down in growth of property sales. And although the potential for a cooling of the real estate market to levels below those projected in the Outlook exists, the difference between the current and alternative revenue scenarios included in the Outlook is relatively small—approximately $1.5 million over the five years of the Outlook.

Sales Tax

The Outlook projects that sales tax revenues will grow by 4% in FY 2017 and FY 2018, 3.5% in FY 2019 and FY 2020, and 3% in FY 2021. The Outlook assumes a continuing decrease in unemployment and a corresponding increase in consumer confidence over its five years.

These assumptions are supported by outside forecasts for regional employment and improving market conditions. Beacon Economics is forecasting that unemployment in San Diego County will steadily fall from its current rate of 5.3% to 4.2% in 2020. Personal income is also projected to increase by roughly 5% per year in FYs 2017-2020. San Diego's population is expected to increase by roughly 1.5% per year in FYs 2016-2019. These projections are sufficient to support a growth in taxable sales.

The Outlook's anticipated growth rates are also consistent with projections for increased taxable sales in the region performed by Beacon Economics and the City's sales tax consultant HDL. Beacon projects taxable sales to increase by 5.6% per year through FY 2019. HDL's projections of likely growth are more conservative, at 4.3% growth each year through FY 2020.

We also note that the Outlook's sales tax projections include the end of the 'triple flip,' which was enacted by the State in FY 2005. Due to the City's accrual practices, the elimination of the triple-flip generates a one-time increase in sales tax revenue recognized in 2016 of $12.7 million. Because that one-time increase is not included in FY 2017 sales tax projections, the projected 4.0% growth in taxable sales is more than offset by the removal of the $12.7 million one-time revenues, resulting in a decline in overall sales tax revenues in FY 2017.

Transient Occupancy Tax

The Outlook continues the previous year's projected healthy 6% TOT revenue growth in FY 2017, and then gradually reduces the projected rate of TOT growth in FY 2018 to 5.5% and finally to a low of 4.5% in FY 2021. The Outlook notes several positive TOT indicators including:

- San Diego Tourism Authority (SDTA) projected growth through CY 2020 and the continuation of its marketing efforts to support San Diego as a prime tourist destination
- San Diego Convention Center projections of increased room night production for CY 2016 and 2017
- New hotel projects anticipated over the next several years
- San Diego will host the 87th annual Major League Baseball All-Star Game at Petco Park in 2016

While these positive indicators point to sustained healthy growth in TOT, the Outlook also recognizes that any slow-down in the economy may reduce leisure and business travel spending, and that the uncertainty surrounding the expansion of the Convention Center has the potential to limit or reduce future bookings of large conventions such as Comic-Con.

Our Office notes that the current scenario for TOT included in the Outlook appropriately reflects a slight reduction in revenue growth in the outer years of the Outlook, as the attempt is made to balance current healthy TOT growth with unknown future risks. However, we also note that San Diego will be facing increased competition for overnight hotel stays as investments are being made in other California cities in an attempt to attract more business and tourist travel dollars to those locales[3]. These considerations were not discussed in the Outlook, and have the potential to further reduce TOT projections to levels closer to the alternative scenario, especially in the outer years. A reduction in growth rates from the current to the alternative scenario over the last three years of the Outlook would mean a reduction in projected revenue of approximately $14.5 million: $3.4 million in FY 2019, $4.8 million in FY 2020, and $6.3 million in FY 2021. Our Office supports continued close monitoring of TOT revenues in order to determine if these factors are affecting San Diego's TOT collections, and if any additional reduction in projected revenue growth is warranted.

[3]Competition for tourist travel dollars may come when Universal Studios in Hollywood opens The Wizarding World of Harry Potter in Spring 2016. Universal Studios opened an original 'Wizarding World' in Orlando in 2010, and a second one in Japan. San Diego might also have to compete with Anaheim for business travel dollars when its convention center expansion is completed in the summer of 2017.

Franchise Fees

Franchise fees in the Five-Year Outlook consist mainly of payments from San Diego Gas and Electric (SDG&E), cable providers, and refuse haulers. Overall, all combined franchise fees are expected to increase slightly each year of the Outlook. Individual rates are discussed in detail below.

Cable Franchise Fees

Cable franchise fees currently constitute 23% of all franchise fees received by the City. The Outlook assumes no growth or decline in cable franchise fees in each of the five years. The Outlook notes that increasing demands for internet and cable-based phone services offset declining television subscriptions, which is consistent with current trends. In FY 2011, cable franchise revenue growth was 2.8%. This declined to 1.1% in FY 2012, and 0.5% in FY 2013. FY 2014 experienced declines in overall cable franchise fee revenue, before increasing slightly in FY 2015.

SDG&E Franchise Fees

Franchise fees paid by SDG&E currently represent 60% of the total franchise fees received by the City. Projected revenue increases for SDG&E franchise fees are 3.3% for each year of the Outlook. This is based on energy cost forecasts provided by the US Energy Information Administration.

SDG&E franchise fee revenue is ultimately determined by erratic commodity rates and sales in the City. It is difficult to accurately predict any given year's revenue variance – in the past, these revenues have seen large single year increases (21.3% in FY 2016) and decreases (12.3% in FY 2010). While the projected growth in San Diego's population size and the consumer price index suggest likely increased demand and energy purchases, the volatility of this revenue source suggests that a conservative projected growth rate should be used, as reflected in the Outlook.

Refuse Hauler Franchise Fees

Franchise fees paid by refuse haulers and tip fees at the Sycamore Landfill total 12% of all franchise revenues collected by the City. The Five-Year Outlook projects revenues from refuse hauler franchise fees to remain flat. Historically, growth and reductions in refuse disposal have broadly tracked overall economic conditions; forecasts by Beacon Economics and HDL for the San Diego region suggest a local economy that continues to improve, but not at rates experienced during the rebound from the recent recession. These indicators largely support the projections included in the Outlook.

Other General Fund Revenues

Bayside Fire Station $5.0 Million Transfer in FY 2017

The FY 2017-2021 Five-Year Outlook includes a $5.0 million transfer to the General Fund from the Bayside Fire Station CIP in FY 2017. In the FY 2016 Adopted Budget, $5.0 million was budgeted from Excess Equity to fully fund the CIP for this project, which is primarily funded by the Successor Agency to the former Redevelopment Agency. Since the time the FY 2016 budget was adopted by the City Council, other eligible funding from previously unallocated bond proceeds has been identified. The Semi-Annual CIP Report, which the Council is expected to consider on December 14, includes a recommendation to replace $5.0 million in General Fund contributions to the project with $5.0 million from these unallocated bond proceeds. If approved, $5.0 million in General Fund contributions would likely return to fund balance in FY 2016. The Five-Year Outlook includes this amount as a $5.0 million transfer to the General Fund in FY 2017.

REVIEW OF GENERAL FUND EXPENDITURES

The Outlook's Baseline Projection shows a ***net*** $29.0 million General Fund expenditure increase (or 2.3%) from the FY 2016 Adopted Budget through the five-year forecast period. Note that this $29.0 million increase includes the removal of $45.4 million in FY 2016 one-time expenditures. Without including adjustments for the FY 2016 one-time expenditures, the increase in expenditures over the Outlook period is $74.4 million.

Increases/(Decreases) from the FY 2016 Adopted Budget to the FY 2021 Outlook Baseline Projection *($ in millions)*		
FY 2016 Adopted Budget	**$1,288.0**	
Salaries & Wages		
Step Increases		1.4
Termination Pay (for Annual Leave)		2.1
POA and MEA Increases in Labor Agreements		23.0
Reversal of One-Time Expenditures		(0.7)
Subtotal Salaries & Wages	**25.7**	**25.7**
Fringe Benefits		
Pension/SDCERS ADC		(20.1)
Other Post-Employment Benefits (2.5% Annual Increases)		5.1
Workers' Compensation		3.8
POA and MEA Flexible Benefits in Labor Agreements		9.4
Other Adjustments to Fringe Benefits		0.1
Subtotal Fringe Benefits	**(1.7)**	**(1.7)**
Supplies		
3.5% Annual Growth Rate Over the Five-Year Outlook		4.5
POA and MEA Uniform/Equipment Allowance in Labor Agreements		(0.4)
Reversal of One-Time Expenditures		(1.8)
Subtotal Supplies	**2.3**	**2.3**
Contracts		
3.5% Annual Growth Rate Over the Five-Year Outlook		39.4
Adjustment for Contracts not Increasing by 3.5% (Largely Fleet Charges & Rent)		(2.1)
Reversal of One-Time Expenditures		(10.6)
Subtotal Contracts	**26.7**	**26.7**
Information Technology	**0.2**	
Energy & Utilities		
3.3% Annual Growth Rate Over the Five-Year Outlook		8.3
Net Adjustment for Water Charges - Includes Projected Conservation Savings		(2.8)
Subtotal Energy & Utilities	**5.5**	**5.5**
Other Expenditures		
Transfer to Park Improvements Funds		2.8
Supplemental COLA		(0.4)
MEA Parking Subsidy Benefit in Labor Agreement		0.2
Reversal of One-Time Expenditures		(32.3)
Subtotal Other Expenditures	**(29.6)**	**(29.6)**
FY 2021 Outlook Baseline Projection	**$ 1,317.0**	
Change: FY 2016 Adopted Budget to FY 2021 Outlook Baseline Projection	**$ 29.0**	

This projected $74.4 million increase in General Fund expenditures is largely due to the following:

- A $32.2 million increase related to compensation increases in the recently negotiated POA and MEA labor agreements;
- A $37.3 million increase in contracts, largely due to a 3.5% assumed annual growth rate;

- A $5.1 million increase for annual 2.5% increases to Other Post-Employment Benefits (OPEB);
- A $3.8 million increase in workers' compensation expenditures;
- A $5.5 million increase in energy and utilities, largely due to a 3.3% assumed annual growth rate; and
- A $4.5 million increase in supplies, due to a 3.5% assumed annual growth rate.

The increases listed above are partially offset over the five-year period by $20.1 million in reductions for the pension Actuarially Determined Contribution (ADC).

Additional expenditures above the baseline projections are listed in the Priority Initiatives section of the Outlook. All five Outlook years show projected revenues in excess of expenditures, which are net of the Priority Initiatives. Additional departmental requests are included in Attachment 3 of the Outlook report, but these operational needs are not included in the calculation of the Outlook's excess revenues over expenditures. See the following table for the total amounts included for each year in the Outlook.

Outlook Revenues in Excess of Expenditures						
General Fund Amounts *($ in millions)*	**FY 2016***	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Baseline General Fund Revenues	$ 1,281.9	$ 1,309.1	$ 1,356.2	$ 1,406.0	$ 1,455.7	$ 1,501.9
Baseline General Fund Expenditures	(1,288.0)	(1,260.0)	(1,278.4)	(1,292.3)	(1,306.2)	(1,317.0)
Subtotal: Revenues in Excess of Expenditures	**(6.2)**	**49.1**	**77.9**	**113.8**	**149.5**	**184.9**
Net Priority Initiatives	N/A	(48.8)	(70.0)	(88.7)	(103.1)	(111.2)
Revenues in Excess of Expenditures	**(6.2)**	**0.2**	**7.9**	**25.1**	**46.4**	**73.7**
Additional Departmental Requests not Included in the Outlook Figures	N/A	$ 94.1	$ 93.3	$ 98.8	$ 103.3	$ 108.9

*FY 2016 budgeted amount

Although there are revenues in excess of expenditures projected for each year of the Outlook, these are based on the City's funding needs with respect to the current baseline of City services, with additions for the Mayoral Priority Initiatives only. The City still has many unfunded needs, including infrastructure, as well as service level enhancements for the Police, Park & Recreation, and other departments, that have been reduced during the last decade and have not been brought back to previous levels. Furthermore, the following issues could further reduce funding available for City services. Potential impacts for each of these issues are summarized in the Executive Summary and discussed in detail elsewhere in this report. The following paragraphs discuss some additional areas of note concerning the General Fund expenditures portion of the Outlook.

Salaries and Wages

The Outlook baseline projection reflects a $2.8 million increase in salaries and wages over the five-year forecast period, excluding the impact of the recent multi-year agreements with POA and MEA, which are discussed in the next section. This increase results from the following items: a $1.4 million increase for salary "step increases", a $2.1 million increase in the termination pay estimate (which is based on DROP participants' exit dates), and a $0.7 million decrease due to one-time expenditure adjustments.

Vacation Pay-in-Lieu
Over the past six completed fiscal years (FY 2010 through FY 2015), pay-in-lieu of annual leave expenditures have averaged approximately $7.0 million and have been overbudget in each of those years. The FY 2016 budget for vacation pay-in-lieu is $5.1 million, and actual expenditures through October are $3.4 million. It seems likely that FY 2016 expenditures could be overbudget as well. We understand that pay-in-lieu of annual leave is a difficult expenditure type to forecast, but we continue to recommend that the City examine potential methodologies for estimating pay-in-lieu, so that a more accurate budget for those expenditures can be established.

New FTE Positions Added in the Five-Year Outlook
Attachment 1 to this report presents the General Fund positions added in each year of the Outlook. All position additions are found in the Priority Initiatives portion of the Five-Year Outlook. There are 136.76 FTE additions in FY 2017, increasing by 280.66 FTEs to 417.42 FTE additions in FY 2021. The largest increases include the following, with FY 2021 FTE increases:

- Streets, sidewalks, and transportation (24.00 FTEs)
- Storm water – flood risk management (32.00 FTEs)
- Storm water – water quality improvement projects (27.00 FTEs)
- Park & Recreation – new and enhanced facilities (51.25 FTEs)
- Expanded recreation center hours (23.00 FTEs)
- Zero waste (18 FTEs)
- Industry standard/CIP infrastructure maintenance (105.00 FTEs)
- New fire station facilities (72.00 FTEs)
- Police sworn and civilian positions (40.00 FTEs)

<u>Five-Year Employee Organization Agreements</u>

One impact to the Outlook's baseline forecast is due to the recent labor agreements between the City and two of its employee organizations. Related increases in compensation are non-pensionable for FY 2017 and 2018, and include 3.3% pensionable increases for FY 2019 and FY 2020. The increases included in the Outlook's forecasted expenditures are shown in the table below.

Costs Included in the Outlook for Labor Agreements (*$ in millions)*					
Employee Organization	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Police Officers Association (POA)	$ 13.1	$ 19.8	$ 22.7	$ 25.2	$ 27.5
Municipal Employees Association (MEA)	3.3	6.6	11.6	15.8	15.8
TOTAL	**$ 16.4**	**$ 26.4**	**$ 34.3**	**$ 41.0**	**$ 43.3**

In the current five-year agreements with the City's other four employee organizations, there are reopeners allowing for negotiations over additional non-pensionable compensation for FY 2017 and FY 2018. As the outcome of potential negotiations is unknown, the Outlook does not forecast any related impacts. The potential for additional impacts to the Outlook related to anticipated negotiations with other employee organizations is discussed elsewhere in this report.

Retirement

Pension/SDCERS

The Outlook's defined benefit pension forecasts through FY 2021 are based on the most recently provided Actuarially Determined Contribution (ADC) projections from the San Diego City Employees' Retirement System's (SDCERS) actuary, Cheiron, from the June 30, 2014 actuarial valuation. The estimated ADC for FY 2017 is $248.1 million citywide ($182.7 million for the General Fund). The annual ADC estimates included in the baseline projections decrease each year by an average of $5.5 million, with an estimated citywide ADC of $227.6 million for FY 2021 ($167.6 million General Fund portion).

These ADC figures are ***not*** adjusted for events that occurred subsequent to the FY 2014 valuation, including FY 2015 investment returns being lower than projected and actuarial assumption changes approved by the SDCERS Board in November 2015. We concur with this approach for the Outlook. Cheiron has not completed the FY 2015 valuation, which will provide the FY 2017 ADC and subsequent years' ADC projections. There may be other factors which impact the projected ADCs. Because of the complexity of the pension system variables, the total of all effects on the ADCs is unknown at this time.

However, if estimates do not change significantly, the events occurring subsequent to the FY 2014 valuation could cause the ADCs in the Outlook to increase each year, rather than decrease as currently forecasted. With that in mind we provide further discussion on the estimated impacts in the "Other Issues and Potential Impacts" section of this report.

Defined Contribution Plan

City employees hired on or after July 20, 2012, except sworn police officers, are no longer eligible to participate in the defined benefit (DB) pension plan. Instead they participate in the Supplemental Pension Savings Plan H (SPSP-H), which was previously for hourly employees but was modified to include these new participants. Both the City and employees contribute 9.2% and 11.0% of eligible compensation for general members and safety members, respectively.

There are no SPSP-H increases in the Outlook for turnover that occurs during the five-year period. Such turnover will lead to an increasing number of SPSP-H members, specifically new-hires who are not eligible to participate in the defined benefit pension plan. With these new SPSP-H members and no budget increase, there could be a potential SPSP-H shortfall of upwards of a million dollars for each year of the Outlook (depending on the extent of turnover and vacancies that will occur).

REVIEW OF RESERVES IN OUTLOOK

General Fund Reserve

As outlined in our review of the FY 2016 First Quarter Report (IBA Report 15-44), the projected FY 2016 year-end General Fund reserve is $190.3 million. Of this amount, $159.0 million is projected to be required to meet the City's 14% reserve requirement, leaving $31.3 million in

Excess Equity. The City's 14% reserve requirement is based on the past three fiscal years' General Fund operating revenues[4]. The three-year average and corresponding 14% reserve requirement are shown in the following table for each fiscal year of the Outlook.

Projected 14% Reserve Requirement						
($ in millions)	**FY 2016**	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
3-Year Average Revenues	$ 1,136.1	$ 1,168.7	$ 1,184.7	$ 1,226.4	$ 1,268.6	$ 1,316.6
14% of Average Revenues	$ 159.0	$ 163.6	$ 165.9	$ 171.7	$ 177.6	$ 184.3

Over the past few months, there have been discussions regarding modifying the City's Reserve Policy to set aside additional reserves, beyond those required in the current Reserve Policy. The potential impacts are discussed in the "Other Issues and Potential Impacts" section of this report.

Risk Management Reserves

Public Liability Reserve

The goal for the Public Liability Reserve, per the City Reserve Policy, is that the overall reserve target of 50% of the outstanding actuarial liability be reached by FY 2019. Currently, these estimates are based on the average value of annual actuarial liabilities for the three fiscal years ending in 2015, which equals $91.8 million. The target amount of 50% of the outstanding liability is $45.9 million.

The Outlook includes $9.3 million in reserve contributions, and is on track to meet the Reserve Policy goal with $2.8 million, $3.7 million, and $2.8 million anticipated to be contributed in FY 2017, FY 2018, and FY 2019. Note that the Public Liability Reserve is paid entirely from General Fund contributions. The Public Liability fund can be very volatile and will continued to be monitored throughout the year.

Workers' Compensation Reserve

For FY 2015, the Workers' Compensation (WC) Reserve had met the overall target level of 25% of the outstanding liability for WC. The outstanding liability is based on the average of the annual actuarial liabilities for the most recent three fiscal years. For FY 2015, that liability was $193.7 million (based on the average of liabilities for FY 2012 through 2014). The corresponding 25% target was $48.4 million.

With the June 30, 2015 valuation completed, the average of the outstanding liabilities for the three fiscal years 2013 through 2015 has increased to $218.1 million. Thus, the 25% reserve target has now increased to $54.5 million. The current reserve balance is approximately $48.4 million, or $6.1 million less than the target. The FY 2016 First Quarter Report indicates that the City will increase FY 2016 contributions to the WC Fund, which will provide the $6.1 million needed to bring the WC Reserve to the 25% reserve target.

WC Reserve contributions are forecasted for each year of the Outlook, at an average of $1.7 million added each year, to reach a Reserve of $63.0 million in FY 2021. Amounts are also included each year in the Outlook for increases in ongoing WC expenditures, which are

[4] Note: the FY 2016 reserve requirement is slightly higher than the $158.6 million shown in the First Quarter Report, per updated figures for the Office of the City Comptroller.

projected to increase by 2.4% annually.

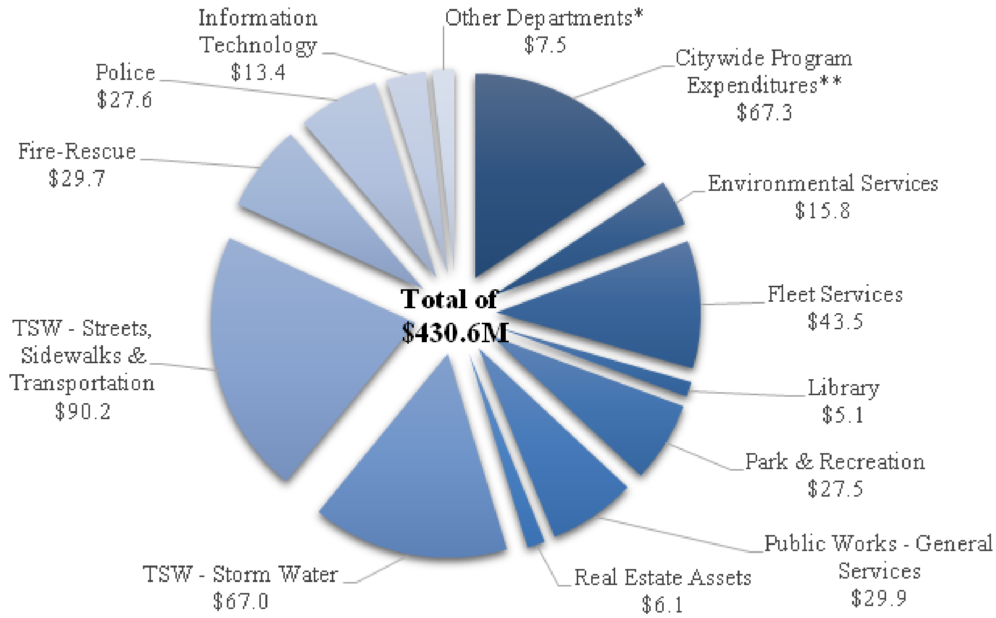
Long-Term Disability Reserve (LTD)
For FY 2015, the Long-Term Disability Reserve (LTD) had also met the overall target level, which is 100% of the outstanding liability for LTD. The outstanding liability is based on the average of the annual actuarial liabilities for the most recent three fiscal years. For FY 2015, that liability was $18.3 million (based on the average of liabilities for FY 2012 through 2014).

With the June 30, 2015 valuation completed, the average of the outstanding LTD liabilities for the three fiscal years 2013 through 2015 has decreased by $3.4 million, to $14.9 million. With the current reserve balance at approximately $18.4 million, the target is currently exceeded, and no contributions to the LTD fund are forecasted in the Outlook.

REVIEW OF MAYOR'S PRIORITY INITIATIVE EXPENDITURES

The General Fund revenue increases projected in the Outlook total approximately $430.6 million over five years and are allocated to projects and programs requested by departments and that were approved as being part of one of the Mayor's four priority initiatives: Infrastructure and Neighborhood Investment, Public Safety, Technology Improvements, and Customer Service and Open Government. The Infrastructure and Neighborhood Investment initiative received the largest portion of the allocation over the span of the Outlook with increases in resources projected for Citywide Program Expenditures, the Transportation & Storm Water Department's Street and Storm Water divisions, branch library expansions, a number of Park & Recreation Department projects, Environmental Services Department projects such as the Zero Waste initiative, and additional allotments to the Fleet Services Division, Real Estate Assets Department, and Public Works–General Services Division. Each department's allocation of priority initiative funding is included in the chart on the following page and we provide additional details and analyses in the subsequent sections.

FY 2017-FY 2021 Outlook Priority Initiatives Funding By Department ($ in millions)



*Other Departments include the Office of Homeland Security, City Clerk, City Comptroller, City Treasurer, Development Services, Personnel, Planning, and Economic Development, all of which received less than $3.0 million in expenditure adjustments in the Outlook.
**Citywide Program Expenditures includes Deferred Capital Debt Service, and Infrastructure Asset Management (IAM)

<u>Priority Initiative: Infrastructure and Neighborhood Investment – CIP Funding Overview</u>

Bonding Portion of the Capital Investment Plan in the Outlook

The Outlook includes debt service for three more deferred capital lease revenue bonds to be issued in FY 2017, FY 2018, and FY 2019. The planned amount for each of these bonds is $90.0 million.

On March 20, 2012, the Council took a significant step towards providing infrastructure funding when it approved a multi-year capital expenditure plan known as Enhanced Option B. The expenditure plan was designed to slow the rate of deterioration of streets, facilities, and storm drains, so that infrastructure would only deteriorate by 5 to 10 percent. Enhanced Option B called for the annual issuance of lease revenue bonds to fund capital projects totaling $494.0 million, as well as to provide annual maintenance and repair expenditures totaling $370.0 million over a six year period through FY 2017.

Excluding the first deferred capital bond that was issued in FY 2010, the table below compares deferred capital bonds issued since FY 2012 and bonds planned in the Outlook with the Enhanced Option B plan adopted by the City Council. Although unanticipated delays caused the timeframe to be delayed by two years, total deferred capital bonds will exceed the total bond amount presented in Enhanced Option B by approximately $6 million in FY 2019.

Fiscal Year	Bonds Already Issued* or Planned in Outlook *($ in millions)*	Planned Bonds in Enhanced Option B *($ in millions)*
FY 2012	$75	$75
FY 2013	$35	$80
FY 2014	$0	$81
FY 2015	$120	$90
FY 2016	$0	$84
FY 2017	$90	$84
FY 2018	$90	$0
FY 2019	$90	$0
FY 2020	$0	$0
FY 2021	$0	$0
Total:	**$500**	**$494**

*Bonds already issued are shaded in gray

Expenditure Status of Outstanding Deferred Capital Bonds

Between FY 2009 and FY 2015, the City issued four lease revenue bonds totaling $333.3 million to address deferred capital needs in the City. These bonds are known as DC 1 ($103.3 million), DC 2 ($75.0 million), DC 2A ($35.0 million) and DC 3 ($120.0 million). As of December 1, 2015, all of the DC1 and most of the DC 2 & 2A proceeds have been expended. As shown in the table below, approximately $112.8 million has yet to be committed to specific capital projects.

Expenditure Status of Deferred Capital Bonds					
Bond	**Year Issued**	**Bond Amount**	**Proceeds Expended**	**Proceeds Encumbered**	**Available Proceeds**
DC1	FY 2010	$103,300,000	$103,300,000	$0	$0
DC2	FY 2012	75,000,000	72,294,125	1,809,402	896,473
DC2A	FY 2013	35,000,000	15,318,268	16,073,574	3,608,158
DC3	FY 2015	120,000,000	1,172,736	10,490,043	108,337,221
	Total	**$333,300,000**	**$192,085,129**	**$28,373,019**	**$112,841,852**

Mayor's Commitment to Allocate 50% of New Major Revenue Growth to Infrastructure

Beginning with the FY 2015 Budget, the Mayor committed to allocate at least half of new revenue growth to infrastructure and neighborhood repair efforts. The minimum amount of this commitment is determined by taking 50% of the growth in the City's four major General Fund revenues: property tax, sales tax, TOT, and franchise fees. Based on current projections, the minimum amount of this commitment over the Outlook period is $94.2 million as shown in the table on the following page.

Mayor's Commitment to Allocate 50% of New Revenue Growth to Infrastructure						
$ in millions	FY 2017 Outlook	FY 2018 Outlook	FY 2019 Outlook	FY 2020 Outlook	FY 2021 Outlook	TOTAL
Projection in Outlook - 50% Major Revenue Growth	$15.6	$21.8	$20.0	$19.8	$17.0	$94.2

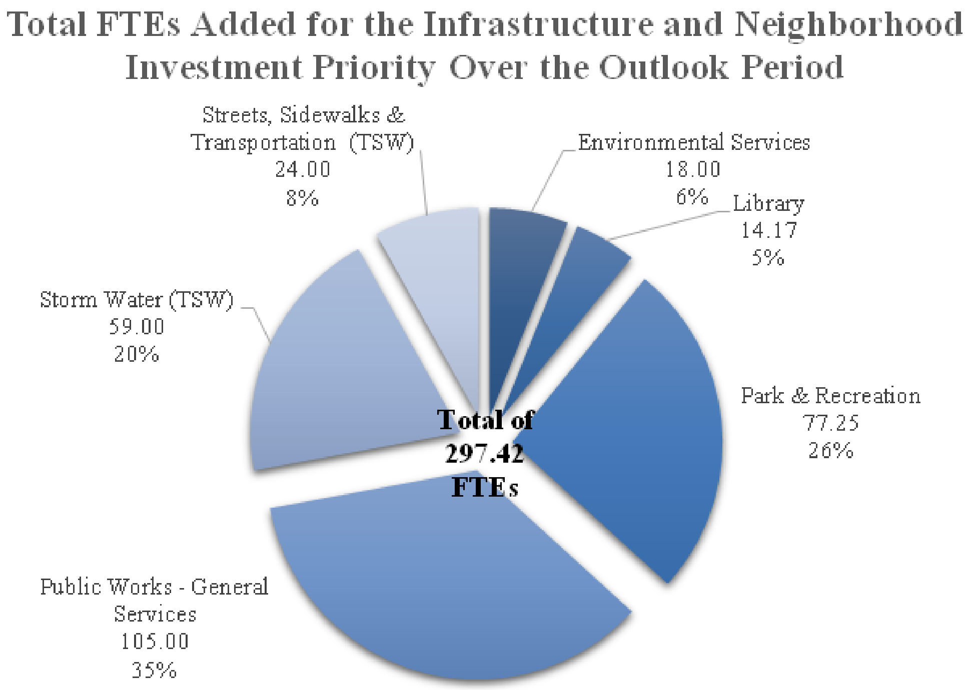
In an effort to demonstrate the Mayor's plan to spend at least 50% of the projected revenue above, page 6 of the Outlook presents a table showing $203.7 million (over the Outlook period) of planned Priority Initiative expenditures for Infrastructure that exceed the projected minimum 50% of major revenue growth commitment. The expenses in this table are largely a subset of the expense table for total Infrastructure and Neighborhood Investment on page 48 of the Outlook.

The major expenditures listed in the table on page 6 of the Outlook period include: personnel expense (PE) and non-personnel expense (NPE) related to street, sidewalk, and transportation projects (43%); debt service for $270 million of deferred capital bonds planned in the Outlook (28%); PE and NPE needed for the upkeep and preventative maintenance of facilities (14%); PE and NPE for storm water projects (8%); and implementation costs for the Infrastructure Asset Management (IAM) system (5%).

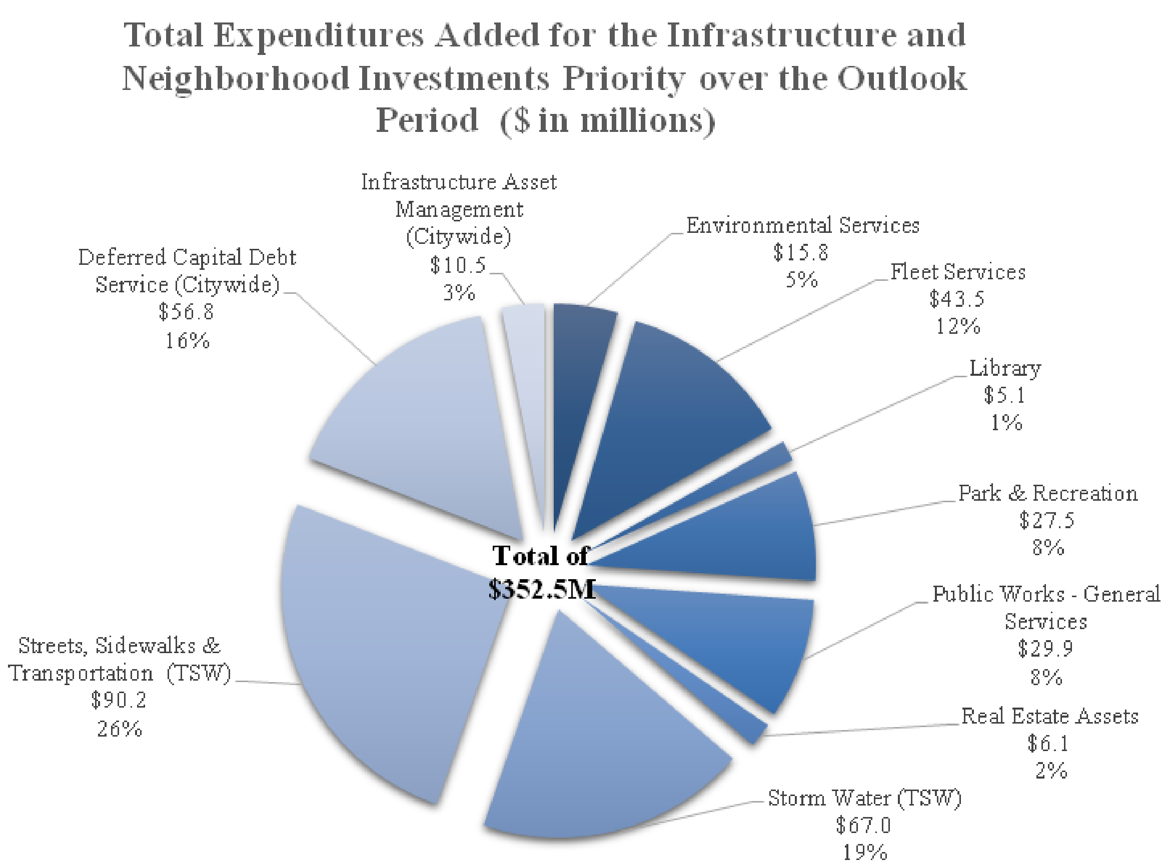
While some of the above expenses (e.g., maintenance, NPE, or IAM) are not directly related to specific infrastructure projects, they are investments in resources that will either support project administration or help the City effectively plan to maintain its capital assets going forward, and are generally appropriate for including with infrastructure totals.

Funding for Infrastructure and Neighborhood Investment

The charts on the following page provide a percentage breakout of FTE positions and categories of expense within the Infrastructure and Neighborhood Investment Priority Initiative as identified in the Outlook.



Note: The 18.00 FTE positions in Environmental Services represent a transfer of funding responsibility from the Environmental Services Department Enterprise Fund to the General Fund.



Planned annual expenditures in Infrastructure and Neighborhood Investment will more than double from $41.6 million in FY 2017 to $94.0 million in FY 2021 as the Mayor has stated. Total investment in the Infrastructure and Neighborhood Investment priority over the Outlook period is $352.5 million, an increase of $113.2 million over the $239.3 million total in last year's Outlook. A significant portion of this increase is explained by the addition of $43.5 million of expense for Fleet Services (planned vehicle and equipment purchases). Fleet Services and other expenditure categories of note within Infrastructure and Neighborhood Investment are discussed below.

Fleet Services

The addition of $43.5 million for Fleet Services accounts for 12% of all Infrastructure and Neighborhood Investment over the Outlook period. As explained on page 62 of Outlook, this reflects planned expenditures to replace active City vehicles operating beyond their expected useful life, and to acquire new automotive equipment. The plan is to first utilize vehicle replacement fund balances before consideration is given to increasing assignment fees[5] to benefitting General Fund departments. Vehicles and equipment will either be cash purchased or financed depending on available funds. According to the Financial Management Department, planned Fleet Service expenditures are included in this priority initiative because they represent investment in capital assets (e.g., street sweepers) that support neighborhood services.

Streets, Sidewalks, and Transportation

The largest portion (26%) of all Infrastructure and Neighborhood Investment in the Outlook is for new streets, sidewalks, and transportation-related projects. The expenditure plan calls for the addition of $90.2 million and 24.00 FTE positions over the Outlook period to address street repairs, sidewalk repair/replacement, streetlights, and traffic mitigation projects throughout the City.

Deferred Capital Debt Service

The Outlook includes $56.8 million of debt service for three $90 million deferred capital bonds (DC 4, DC 5, and DC 6) planned for FY 2017, FY 2018, and FY 2019. This debt service constitutes 16% of total Infrastructure and Neighborhood Investment spending in the Outlook. Given that debt service facilitates the accelerated receipt of capital for infrastructure projects, it is appropriately included in this priority initiative.

It is important to note that the City will be paying an additional $105.5 million in debt service during the Outlook period for $333.3 million of bonds (DC 1, DC 2, DC 2A, and DC 3) already issued to fund infrastructure projects. Since debt service payments for these bonds began prior to the Outlook period, the expense has been included in the Other Expenditures line item of the Baseline Projections in the Outlook.

Infrastructure Asset Management (IAM)

The Outlook includes $10.5 million of General Fund implementation and software maintenance costs for the development of an IAM system: $7.0 million in FY 2017 and $3.5 million in FY 2018. It is expected that a System Integrator consultant will be hired early in 2016 to help

[5] Assignment Fees are annual fees set aside to replace vehicles when they become more expensive to repair than to replace.

develop the IAM system over the next two or three years. Once implemented, IAM will provide a process to effectively and sustainably manage City infrastructure assets at a desired level of service.

Asset management incorporates two broad concepts: a business practice for making decisions on infrastructure based on quality data, and a software system for optimizing asset maintenance, repair, rehabilitation, and replacement (also referred to as Enterprise Asset Management). IAM will provide key data and information on assets so that decision makers can identify the most effective maintenance and CIP investment strategies. As noted in the Outlook, IAM is expected to increase operational efficiencies while reducing annual software maintenance expenses. Making sound and informed decisions regarding infrastructure investment is particularly important for the City given valid and competing priorities for limited resources.

<u>Maintenance and Repair</u>

The Outlook plans for a significant investment in additional personnel to maintain and repair (M&R) streets, sidewalks, and facilities. Most notably, the Public Works Department (PWD) plans to add 105.00 FTE positions over the Outlook period for upkeep and preventive maintenance of City facilities. The Outlook justifies the significant FTE increase by indicating that there will be an infrastructure investment of approximately $100.0 million in each fiscal year. PWD, in part, used an industry standard (suggesting 2% of the total value of new facilities be allocated for M&R) to develop its request for increased staffing; however, the plan is to develop Facilities Condition Index (FCI) goals for different categories of public facilities and use those FCI goals to determine the need for additional staffing.

The Street Division of the Transportation & Storm Water Department plans to add 24.00 FTE positions and $90.2 million over the Outlook period. These additional resources will be largely dedicated to street and sidewalk repairs. The planned investment in street repairs should help the City further the Mayor's goal of achieving an Overall Condition Index (OCI) of 70 by 2025. The Park & Recreation Department plans to add 3.00 FTE positions in FY 2017 to repair and replace playground equipment and rubberized surfaces that are nearing the end of their useful life. All of the aforementioned investments should help improve the City's M&R efforts which are critically important to the development of an effective infrastructure management program.

<u>Condition Assessments</u>

The Outlook includes $1.25 million ($250,000 annually) for consultants to perform facilities condition assessments. Following the release of a comprehensive facilities assessment in January 2016, the plan is to develop a rotating schedule to assess the condition of 25% of the City's facilities each year going forward. The goal is to continually assess the condition of General Fund facilities to maintain a current inventory, and to better plan for the appropriate maintenance and operation of those facilities.

The City recently completed a citywide street assessment and the results are anticipated to be released in a report early in 2016. The Street Division of the Transportation & Storm Water Department received $550,000 in the FY 2016 Adopted Budget to complete this condition assessment.

The FY 2016 Adopted Budget also included $300,000 for the Park and Recreation Department to continue park condition assessments. The Outlook continues annual funding in this amount as a baseline expense through FY 2021. The Department anticipates 30 to 50 parks can be assessed on an annual basis, depending upon the size and amenities of each park.

<u>Developing Project Delivery Resources to Support Increased Infrastructure Investment</u>

As the City continues to better assess the condition of its existing infrastructure assets and develop new funding sources to address an increasing array of priority needs, it will be critically important to develop staff and external project delivery resources (consultants/contractors) to effectively manage the increased annual volume of infrastructure projects in the Outlook. The City notably increased personnel and related expenses in the FY 2015 and FY 2016 budgets to sufficiently grow its internal project management capacity for the anticipated project volume in FY 2016 and FY 2017; however, the volume of projects planned in the Outlook and the Fiscal Year 2017-2021 Five-Year Capital Infrastructure Planning Outlook (Capital Outlook) continues to grow significantly. Additionally, there has been considerable discussion about pursuing new sources of revenue for new infrastructure projects such as the convention center expansion, fire stations, and a football stadium.

The planned and potential growth in infrastructure projects intensifies the City's need to develop and monitor project delivery resources going forward. Even though significant funding for additional personnel dedicated to infrastructure projects was added in the FY 2015 and FY 2016 budgets, staff will be challenged to quickly and efficiently spend existing funds (such as available bond proceeds) and future committed funds (such as 50% of major revenue growth) for expenditures identified in the Outlook period due to project design and construction management capacity limitations. Noteworthy cash management process improvements described in the first Semi-Annual CIP Budget Monitoring Report will save staff time and make additional funds available for infrastructure projects. The City also plans to borrow $270 million by issuing three new deferred capital bonds by FY 2019. Considering the aforementioned funding sources, it is clear the City will need to have sufficient project delivery resources (internal staff and design/construction management contractors) to efficiently use available funds and address the planned infrastructure spending detailed in the Outlook and Capital Outlook.

The City's Public Works and Personnel departments are to be commended for their efforts to quickly hire an unprecedented number of staff in an effort to increase project management capacity. It is important to note that it requires considerable time and senior staff resources to hire, acclimate, and train hundreds of new employees. There are also many other factors and challenges associated with developing project delivery resources. In the bullet points below, we identify some of the internal and external challenges that City staff may already be encountering or need to plan for, in order to develop sufficient project delivery resources:

<u>Internal Considerations</u>

- Hiring and training new staff requires senior staff participation which diminishes project management capacity in the near term
- New positions are often filled by existing staff which necessitates additional hiring processes to backfill vacated positions
- Project management experience/capabilities may decline when so large numbers of new staff are hired in a short period of time

- The time required to complete infrastructure projects often depends on required processes and staff in supporting City departments (financial, legislative, personnel, etc.)
- A significant amount of additional office space is required for new staff and needs to be coordinated expeditiously
- As the City takes on more projects, extra planning is required to avoid project conflicts within the City's right-of-way (e.g., street resurfacing, utilities undergrounding and water line replacement projects on the same street)
- Project delivery capabilities improve if the City is able to bid larger projects; however, moving in this direction may run counter to other City policy objectives (e.g., opportunities for small and local contractors)
- The City will need to hire more project design and construction management contractors in order to complete the infrastructure work discussed in the Outlook and the Capital Outlook while simultaneously training City staff in these skill sets in order to decrease reliance on outside contractors

External Considerations

- Market demand (private and public) for qualified engineers and project managers is high, which makes it more challenging to recruit good candidates
- The City competes with other major entities (County, Metropolitan Transit System, Airport Authority, Navy, etc.) for quality contractors
- Capable contractors are more likely to bid City jobs when they know we have a steady pipeline of projects and reliable funding sources to support those projects

Priority Initiative: Infrastructure and Neighborhood Investment – Department Funding Overview

Environmental Services (ESD)

Compressed Natural Gas (CNG) Fueling Station

The Outlook includes General Fund funding requests totaling approximately $1.2 million, for the CNG Fueling Station from FY 2017 to FY 2019, with the project anticipated to be completed and fully operational by FY 2020. The requests presented in the Outlook will fully fund the fueling station. The FY 2016–2020 Outlook projected the completion of the project by FY 2019; however, due to delays in the issuance of the Request for Proposal to award a design-build contract for this project, the project is anticipated to be completed one year later than originally anticipated.

In conjunction with the construction of the fueling station, the Department plans to replace the entire fleet of low sulphur diesel refuse and recycling packers in a phased approach. ESD projects the replacement of approximately 20 vehicles on an annual basis as the vehicles reach the end of their useful life cycles. The Department uses a seven year life cycle for the packer vehicles. As the replacement of these vehicles is addressed within the annual budget request, these expenses are not identified within the Outlook. Expediting the acquisition of the replacement vehicles would result in not fully utilizing the current vehicles and may not match the phased capacity of the fueling station.

In discussion with the department, the delivery of the new CNG vehicles from the vendor is anticipated to take one year from the order date. ESD anticipates ordering the first CNG replacement vehicles in FY 2017 for delivery in FY 2018. As the CNG fueling station is being constructed in phases, it is anticipated that the portion of the fueling station completed by FY 2018 will be able to accommodate the fueling needs of the new vehicles. With approximately 130 vehicles in their fleet and the initial replacement vehicles going into service in FY 2018, the entire fleet is projected to be replaced by FY 2024. The reduced expenditures starting in FY 2020 reflect the anticipated savings from the fully operational fueling station and the replacement vehicles coming into service.

Zero Waste

In July 2015, the City Council approved the Zero Waste Plan (ZWP). The ZWP is a framework of potential sustainable diversion strategies that would be implemented in steps to achieve the goal of diverting 75% of waste generated in the City from landfill disposal by 2020, achieving a 90% diversion rate by the 2035 goal (currently proposed in the City's draft Climate Action Plan), and sets the foundations for programs to support the goal of Zero Waste by 2040.

The Outlook includes the multiple proposed actions presented in the ZWP that will impact the General Fund. These items include:

- Removal of exemptions from the franchise haulers fees to include the collection of certain types of waste, including source separated recyclable waste. This action would increase the amount of materials on which fees could be charged, resulting in a positive revenue impact of approximately $1.7 million annually to the General Fund during the Outlook period.
- An increase to the franchise fees charged by $1 per ton in FY 2020. This would result in a positive revenue impact of approximately $700,000 in FY 2020 and FY 2021.
- A change in the rate charged for fibrous greens deposited at the Miramar Landfill is anticipated to result in an annual revenue reduction of approximately $100,000 throughout the Outlook period.
- A transfer of funding responsibilities for the Citywide Solid Waste Code Enforcement Program from the Refuse Disposal Fund to the General Fund. This action is an effort to better align expenses with the appropriate programs and will result in an increase in General Fund expenditures of $1.5 million in each of FY 2017 and FY 2018, $1.8 million in FY 2019, and $2.1 million in each of FY 2020 and FY 2021.
- An increase in the AB 939 Fees in FY 2019 and FY 2020. This action is projected to result in an increase in General Fund expenditures of approximately $338,000 in FY 2019, and $676,000 in each of FY 2020 and FY 2021.

Notable action items which were approved for consideration as part of the ZWP and not represented in the Outlook are the implementation of additional educational and outreach programs (proposed for FY 2017) and the development of a resource recovery center (proposed for FY 2019). While these items may be considered by the City Council as separate future items during the Outlook period, the costs associated with these items will be borne by ESD's Enterprise Funds and therefore not reflected in the Outlook.

Actions to support ESD's Five-Year Outlook

The Outlook reflects two actions highlighted in the FY 2016–2020 Outlook and approved in the FY 2016 Adopted Budget; and a scheduled rate increase described in ESD's Five-Year Outlook which was approved by the City Council in November 2012. The actions and impact to the General Fund are described below.

- Transfer of revenue received from the Sycamore Canyon Landfill Facility Franchise Agreement from the General Fund to ESD's Recycling Fund over a five-year period. The transfer was approved as part of the FY 2016 Adopted Budget with FY 2016 being the first year of the five year transfer (to be completed in FY 2020). The Outlook includes the incremental increases in the transfer amounts from the FY 2016 Adopted Budget.
- The FY 2016 Adopted Budget included the phased elimination of the $5 per ton tipping fee discount to City forces over a three-year period. The scheduled reduction of the discount included a $2 per ton reduction in FY 2016 (projected $616,000 impact), $2 per ton reduction in FY 2017 (projected $616,000 impact), and $1 per ton reduction in FY 2018 (projected $308,000 impact) to completely eliminate the discount. The Outlook includes the incremental increase in expenditures to the General Fund over the projected first year impact amount in FY 2016.
- ESD's Five-Year Outlook included planned increases of $1 per ton to the disposal fees at Miramar Landfill in FY 2018 and FY 2020. Each rate increase is anticipated to result in an increase of $308,000 in expenses to the General Fund. The Outlook reflects the increases in FY 2018 and FY 2020.

Library

Expansion/Replacement of Three Branch Libraries

The Department anticipates completing the expansion/replacement of three branch libraries during the Outlook period. These libraries are the Skyline Branch library anticipated to be completed in FY 2018, and the Mission Hills and San Ysidro Branch libraries anticipated to be completed in FY 2019. The Outlook includes 5.67 FTE positions and approximately $804,000 in additional operating costs associated with the expansion/replacement of these facilities. Full capital funding from various sources including the third DC bond issuance and private donations, has been identified for these facilities.

The projected completion of these facilities includes two adjustments from the FY 2016–2020 Outlook. The adjustments include the completion of the Skyline Branch library in FY 2018 compared to FY 2017, and the inclusion of the completion of the San Ysidro Branch library. The San Ysidro Branch library had previously been anticipated to be completed in FY 2019, however due to uncertainty about the project timeline and exact location, the facility was excluded from the FY 2016–2020 Outlook. As the issues related to the San Ysidro Branch library have been addressed, the expansion is now included for financial planning purposes.

New Branch Library

The Outlook includes 8.50 FTE positions and approximately $805,000 in operating costs for the Pacific Highlands Ranch Branch library, which will be the first new (not an expansion or replacement of an existing facility) branch library since the Mission Valley Branch library in 2007. This facility is planned as part of the increased development within the Pacific Highland Ranch community and will serve the entire North City Future Urbanizing Area (NCFUA). It is currently anticipated that this project will be funded solely through Facility Benefit Assessment (FBA) funds. The financial schedules have been updated for the programmed FBA funds for the contributing communities in Black Mountain Ranch, Del Mar Mesa, Pacific Highlands Ranch, and Torrey Highlands Ranch. This facility was not included in the FY 2016–2020 Outlook.

Park & Recreation

New and Enhanced Facilities

The Department has identified new parks and planned park enhancements projected to open and/or occur during the Outlook period. Planned park enhancements include the addition of acreage to existing parks and additions to services/maintenance programs. The Outlook allocates an increasing amount of funding from $2.6 million in FY 2017 to approximately $4.5 million in FY 2021 to address the operational expenses related to the new parks and planned enhancements. A list of the planned new parks and enhancements, which includes the fiscal year in which the park/enhancement is anticipated to open/occur and the costs and staffing related to each park/enhancement, is provided in Attachment 2.

Playground Outlay and Rubberized Surfacing

The Outlook includes approximately $352,000 in annual expenses plus a one-time vehicle expense of $120,000 in FY 2017 to create a program to repair and replace playground equipment and rubberized surfaces at park facilities. The proposed funding will provide a specialized crew to perform the routine maintenance and to complete the work required to comply with warranty requirements for playground equipment. The Department indentified the establishment of this program as a priority and has developed a list of facilities to be addressed based upon various factors such as equipment life cycle, staff evaluations, and input from park patrons. The list of facilities is anticipated to be adjusted during the Outlook period as additional information about park facilities is collected and high priority health and safety issues are identified.

Expanded Hours at Recreation Centers

One of the unfunded items presented in the FY 2016–2020 Outlook, was the Department's phased plan to add five hours per week to each recreation center throughout the City. The Department identified the need to add 53 Assistant Recreation Center Director positions (ARCDs) in order to increase the service hours for each recreation center from 45 to 50 hours per week.

The FY 2016 Adopted Budget included the addition of 45.00 FTE positions (36.00 ARCDs and 9.00 Recreation Center Leader 1s) as the first phase of the plan to add additional service hours to each recreation center. The additional positions increased the service hours at 36 recreation centers from 45 to 60 hours per week. The 36.00 ARCD positions added five hours to each recreation center and the 9.00 Recreation Leader 1s added 10 additional service hours to the 36 recreation centers that received the additional ARCD positions. The ARCD positions added in the first phase of additions were placed at the largest recreations centers within the City.

The Outlook continues the phased plan of adding additional ARCD positions to increase the service levels at the remaining recreation centers throughout the City. The Outlook projects the addition of 23.00 ARCD positions and approximately $1.0 million in operating expenses by FY

2019. The additional positions would ensure that each recreation center would have core service hours of at least 50 hours per week.

Transportation & Storm Water – Street Division

The Outlook contains expenditures consistent with those discussed in the Mayor's five-year street pavement repair program as it was presented to the City Council in April, 2015. In our review of the program, we noted that the goal of repairing 1,000 miles of streets was obtainable, but that additional funding would need to be identified to ensure that the Overall Condition Index (OCI) of City streets could be improved to 70 by 2020.

In our review of that program, we noted that funding was anticipated to come from dedicating two-thirds of future lease-revenue bond issuances to street repair, and that such dedications would leave the following gaps in funding required:

FY 2016-2020 Asphalt Overlay Funding Needed vs. Proposed *($ in millions)*						
	FY 2016	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**Total**
Need[1]	$83.1	$83.1	$83.1	$83.1	$83.1	**$415.5**
Proposed Lease Revenue Bonds[2]	$44.4	$65.0	$60.0	$60.0	-	**$229.4**
Shortfall	**$38.7**	**$18.1**	**$23.1**	**$23.1**	**$83.1**	**$186.1**

[1]Includes asphalt overlay, reconstruction, and concrete.

[2]Lease revenue bonds issued in FY 2015 will be largely expended in FY 2016; FY 2017 includes $5 million of carryover lease revenue bond funds; FYs 2017, 2018, and 2019 each include "up to" $60 million annually for streets from new $90 million bond issuances.

The Outlook continues to include two-thirds of future lease-revenue bonds as sources to meet the street repair commitment. Additional expenditures in the Outlook are projected to support streets, sidewalks, and other transportation projects in the following amounts:

Additional Expenses for Streets, Sidewalks, and Transportation in Outlook *($ in millions)*				
FY 2017	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
$7.3	$10.9	$21.1	$22.6	$28.5

This additional funding is not entirely dedicated to the street repair program, though a portion of it is anticipated to be used for street repairs.

The TSW Department has been conducting a condition assessment of all the City's streets this year. Results are expected to be released in early 2016, and will include an updated OCI and an inventory of City streets and the conditions of each street. That information will be used to develop future repair plans. The last full condition assessment for City streets was conducted in 2011, and showed an OCI of 54.6. Any increase in the OCI discovered in the most recent condition assessment would reduce the funding necessary to reach an OCI of 70 by 2020.

Public Safety Priority Initiative

Fire-Rescue

Fire Academies

The FY 2017-2021 Five-Year Financial Outlook includes $599,000 of funding annually for one additional fire academy over the Outlook period as a Priority Initiative. This would bring the total number of Fire academies to two per year, as one is already included in the baseline. We note that last year's FY 2016-2020 Five-Year Financial Outlook included funding for a total of three Fire academies per year. The Department has indicated that two academies per year will be sufficient to meet its staffing needs over the Outlook period.

New Fire Stations – Operations

The Outlook includes a total of approximately $16.3 million in increased funding and the addition of 72.00 FTEs over the Outlook period to support the operation of five new fire stations. Operational expenses include personnel expenditures and non-personnel expenditures such as new fire engines and/or trucks and related equipment. It is important to note that although the Fire-Rescue Department may anticipate these stations becoming operational by FY 2021, capital funding has not yet been identified to fully fund the design, land acquisition, and construction costs associated with all of these facilities. A detailed discussion of the capital needs for fire stations is included later in this report.

The five new fire stations included in the Outlook generally follow the recommendations of the Citygate Implementation Plan, which outlines the Fire-Rescue Department's future facilities needs and was approved by the City Council in 2011. The most recent update to the plan was presented to the Public Safety and Livable Neighborhoods Committee in January 2015, and is expected to be updated again in February 2016. The table below provides a comparison of the remaining items from the first four years of the Citygate Implementation Plan and the corresponding resources included in the FY 2017-2021 Five-Year Financial Outlook.

Citygate Implementation Plan - Status of Remaining Items in Outlook	
Identified Needs	**Status**
Design and planning for Home Ave. Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Funding for one Battalion Chief Unit	Does not appear in Outlook.
Construction of Home Ave. Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Purchase of fire engine for Home Ave Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Design and planning for Paradise Hills Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Staffing of Home Ave. Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Construction of Paradise Hills Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Purchase of fire engine for Paradise Hills Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Purchase of ladder truck for Paradise Hills Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Funding for land, design, and planning of College Ave. Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Staffing of Paradise Hills Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Construction of College Ave. Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Purchase of fire engine for College Ave. Fire Station	Operating costs included as a Priority Initiative in FY 2021. See table of capital needs.
Funding for design and planning of Skyline Hills Fire Station	Temporary fire station opened in August 2015; Permanent station does not appear in Outlook.
Funding for additional fire academy	One additonal fire academy included annually as a Priority Initiative in FY 2017-2021.

Lifeguard Division – Fire-Rescue Department

Advanced Lifeguard Academy

The Five-Year Outlook includes $252,000 in expenditures annually in FY 2017, FY 2018, and FY 2020 to support an Advanced Lifeguard Academy. The FY 2016 Adopted Budget included $232,000 for this purpose. While the Advanced Lifeguard Academy was not included in the Lifeguard Division Five-Year Needs Assessment approved by the City Council in March 2014, the Department has indicated that it serves an essential operational need. A comparison of remaining needs identified in the Division's Five Year Needs Assessment and initiatives included in the Outlook is provided in the following table.

Lifeguard Division Five-Year Needs Assessment - Remaining Needs through FY 2019	
Identified Needs	**Status in Outlook**
Year 1 - FY 2015	
Addition of 1.00 Senior Management Analyst	Does not appear in Outlook.
Lifeguard Vessel Replacement Plan	Funded in FY 2016; Included in Outlook as a baseline expenditure in FY 2017-2021.
Planning for Jr. Lifeguard Headquarters and Aquatic Safety Education Center	Does not appear in Outlook.
Year 2 - FY 2016	
Addition of 1.00 Special Operations Sergeant	Does not appear in Outlook.
Addition of 1.00 Clerical Assistant II position	Does not appear in Outlook.
Addition of 2.00 lifeguard positions at Ocean Beach	Does not appear in Outlook.
Year 3 - FY 2017	
River Rescue Team expansion	Does not appear in Outlook.
Lifeguard Dive Team expansion	Does not appear in Outlook.
Addition of 1.00 lifeguard position for training at Mission Bay	Does not appear in Outlook.
Addition of 1.00 lifeguard position for South Mission Beach in summer months and relief guard in non-summer months	Does not appear in Outlook.
Conversion of Boating Safety Unit to Specialty Team	Does not appear in Outlook.
Addition of lifeguard overtime for training	Does not appear in Outlook.
Increase seasonal lifeguard hours	Does not appear in Outlook.
Evaluate Paramedic Battalion Medical Officer Program	Does not appear in Outlook.
Construction of Jr. Lifeguard Headquarters and Safety Education Center	Does not appear in Outlook.
Year 4 - FY 2018	
Evaluate assigning Lifeguard Paramedics in Operations	Does not appear in Outlook.
Year 5 - FY 2019	
Evaluate expanding Lifeguard Heaquarters to create Mission Bay maritime public safety hub	Does not appear in Outlook.
Addition of second fire boat	Does not appear in Outlook.

Police

Body Worn Cameras

The FY 2017-2021 Five-Year Financial Outlook includes a total of $1.5 million during the Outlook period for 500 additional body worn cameras. A contract extension with Taser International, Inc., for the purchase of additional cameras was approved by the Public Safety and Livable Neighborhoods Committee on November 12, 2015 and is anticipated to be considered by the full City Council on December 8, 2015. If approved by Council, the contract extension will allow for the expenditure of $478,000 of COPS grant funds in the current fiscal year for 144 additional cameras for the canine unit and academy graduates. The contract also includes an option to spend up to $1.4 million in FY 2017-2020, contingent on approval of future years' budgets. The Department indicates that 1,000 cameras have already been deployed using the original $4.0 million budgeted since FY 2014. The new contract, if all options are exercised, will add up to approximately 900 more cameras.

Maintenance of Existing Facilities and Headquarters Facility Improvements

The Outlook includes the addition of $3.0 million in expenditures in FY 2017-2020 for the maintenance of existing Police Department facilities. In addition, $250,000 is included in FY 2017 for a feasibility study for improvements to the headquarters facility, plus $2.5 million in FY 2018 for the improvements themselves. The Department has indicated that planned improvements to the headquarters include new elevators and replacement of the energy management system, which works in conjunction with the heating, ventilation, and air conditioning (HVAC) system. The feasibility study is intended to assess these two major projects.

The Department has indicated that the $3.0 million intended for maintenance of existing facilities will address deferred maintenance needs at all facilities. This includes the Traffic Division facility, which our office reported on at the request of the Public Safety and Livable Neighborhoods Committee chair. However, this does not include the $250,000 recommended in that report for a feasibility study for a replacement permanent facility for Traffic Division. In conjunction with its update to the Police Department Five-Year Plan, the Department is expected to present a report on its facilities priorities to the Public Safety and Livable Neighborhoods Committee in February 2016.

Sworn and Civilian Positions

The Outlook includes the addition of 25.00 sworn and 15.00 civilian positions over the Outlook period. This addition partially fulfills the needs identified by the Department in its Five-Year Plan, most recently updated and approved by the City Council in 2013. While it is important to continue to focus on funding the Department's staffing goals as outlined by the Five-Year Plan, the metric of budgeted positions does not fully explain the current state of filled positions, particularly for sworn officers. As mentioned earlier in this report's discussion of Police overtime expenditures, sworn attrition rates continue to exceed budgeted assumptions. As a result, the number of vacant sworn positions in the Police Department is more than sufficient to absorb new recruits. As of November 30, 2015, the Department reported a sworn strength of 1,868 filled positions out of 2,036 budgeted positions.

A comparison of the Five-Year Plan and the initiatives included in the Outlook is provided in the table on the following page. The current plan runs only through FY 2018. It is important to note that the Police Department is expected to present an updated plan to the Public Safety and Livable Neighborhoods Committee in February 2016.

Police Department Five-Year Plan Identified Needs for FY 2017-2018	
Identified Needs	**Status in Outlook**
FY 2017	
Addition of 35.00 Sworn Positions	Continued expanded academies included as baseline expenditures; 5.00 FTE sworn positions included as a Priority Initiative.
Addition of 24.00 Civilian Positions	Continued expanded academies included as baseline expenditures; 3.00 FTE civilian positions included as a Priority Initiative.
New Recruit Equipment	Included as part of Priority Initiative for Sworn Positions and Equipment.
New Police Vehicles	Does not appear in Outlook.
Restoration of ABLE and Canine Hours	Identified need of $365,000; not funded in Outlook.
Replace Outdated Equipment	Identified need of $750,000; not funded in Outlook.
CAD Replacement Project	Included and fully funded as a Priority Initiative (debt service and maintenance).
Maintenance of Existing Facilities	Included as a Priority Initiative; $750,000 identified need fully funded.
FY 2018	
Addition of 35.00 Sworn Positions	Continued expanded academies included as baseline expenditures; 5.00 FTE sworn positions included as a Priority Initiative.
Addition of 24.00 Civilian Positions	Continued expanded academies included as baseline expenditures; 3.00 FTE civilian positions included as a Priority Initiative.
New Recruit Equipment	Included as part of Priority Initiative for Sworn Positions and Equipment.
New Police Vehicles	Does not appear in Outlook.
Restoration of ABLE and Canine Hours	Identified need of $370,000; not funded in Outlook.
Replace Outdated Equipment	Identified need of $500,000; not funded in Outlook.
CAD Replacement Project	Included and fully funded as a Priority Initiative (debt service and maintenance).
Maintenance of Existing Facilities	Included as a Priority Initiative; $750,000 identified need fully funded.

Technology Improvements Priority Initiative

Department of Information Technology

For FY 2017, the Outlook includes a transfer from the General Fund of approximately $789,000 to the Information Technology (IT) Fund, and a transfer of approximately $2.3 million to the OneSD Support Fund, which is an increase of approximately $308,000 or 11.3% over what was included in last year's Outlook for the Department in FY 2016. Over the entire five year period, the Outlook includes a transfer of approximately $3.8 million from the General Fund to the IT Fund and $9.6 million to the OneSD Fund, for a total of $13.4 million. This is a decrease of approximately $242,000 or 5.9% for the IT Fund and an increase of approximately $7.1 million or 298.1% for the OneSD Fund, when compared to the amount included over five years in last year's Outlook.

As part of the Technology Improvements priorities, the Outlook includes funding for the IT Fund-related items displayed in the table on the following page.

Information Technology Fund					
Item	FY 2017 Outlook	FY 2018 Outlook	FY 2019 Outlook	FY 2020 Outlook	FY 2021 Outlook
Cyber Security Continuous Monitoring System	382,000	382,000	382,000	382,000	382,000
Email Archive/e-Discovery	145,000	145,000	145,000	145,000	145,000
Support for IT Cyber-Security Team	159,322	159,322	159,322	159,322	159,322
Program Manager (FTE)	1.00	1.00	1.00	1.00	1.00
IT Consulting Services	200,000	200,000	200,000	200,000	200,000
Data Loss Prevention Upgrade	100,000	28,000	28,000	28,000	28,000
Remote Access Upgrade	100,000	(33,000)	(33,000)	(33,000)	(33,000)
Cyber-Security Consulting	100,000	100,000	100,000	100,000	100,000
Windows Server Software Upgrade	200,000	200,000	200,000	200,000	200,000
Desktop Operating System Windows 10 Upgrade	-	300,000	-	-	300,000
Other Items	100,000	300,000	-	-	100,000
Total FTE	**1.00**	**1.00**	**1.00**	**1.00**	**1.00**
Total IT Fund Requirements in Outlook	**1,486,322**	**1,781,322**	**1,181,322**	**1,181,322**	**1,581,322**
General Fund Portion (53.1%)	***789,237***	***945,882***	***627,282***	***627,282***	***839,682***

Of note, the Outlook includes:

- $200,000 each year for IT Consulting Services – The Department of IT is proposing to use these consulting services for a number of contracts, including the City's evaluation of its IT sourcing strategy. Currently, the City contracts with Atos and CGI to provide a variety of major IT services for the City. These five-year contracts will end in FY 2017 and FY 2018, and have two-year renewal options. However, the Outlook does not include one-time transition costs that would be necessary if the City chooses to issue an RFP, and transition from these contracts.[6]
- Support for IT Cyber-Security Team (1.00 FTE Program Manager) – The Outlook includes the addition of a Program Manager to lead the Cyber-Security Continuous Monitoring Operations Center[7]. The Department originally requested an additional program manager for its Payment Card Industry (PCI) compliance efforts (requirements the City must comply with in order to be certified to handle credit card information), but the position was not included in the Outlook. The Department has indicated that it will shift its internal resources to cover the anticipated workload for mandated PCI compliance requirements, and will reevaluate its personnel needs at the end of FY 2016. However, if the Department determines that an additional position is needed, it could require an additional $110,000 each year in personnel expenses (not including fringe benefits), which are not currently included in the Outlook.

Other Technology Improvements items in the Outlook are budgeted in the OneSD Fund and include upgrades to the Purchasing & Contracting module as recommended in the Huron Report, and a citywide document storage solution for SAP and non-SAP software that will allow users to retrieve their data more quickly and efficiently. The table on the following page provides additional details on all items included in the Outlook and budgeted within the OneSD Fund.

[6] If the City exercises its two-year renewal options, potential transition costs would be deferred for 3-4 years.
[7] The Cyber-Security Continuous Monitoring Operations Center supports the City's Payment Card Industry (PCI) compliance program, and addresses real-time cyber-security threats to the City.

OneSD Fund					
Item	FY 2017 Outlook	FY 2018 Outlook	FY 2019 Outlook	FY 2020 Outlook	FY 2021 Outlook
SAP Purchasing & Contracting module upgrade	$ 3,020,000	$ 2,900,000	$ 1,940,000	$ 1,500,000	$ 1,500,000
Training Support	146,576	146,576	146,576	146,576	146,576
Program Coordinator (FTE)	1.00	1.00	1.00	1.00	1.00
Document Storage Solution	969,621	1,096,889	1,096,889	1,096,889	227,268
PBF Module Upgrade	-	800,000	-	-	-
SuccessFactors Upgrades - Performance Evaluation module	-	154,000	319,000	119,000	119,000
Total FTE	**1.00**	**1.00**	**1.00**	**1.00**	**1.00**
Total OneSD Fund Additions in Outlook	**$ 4,136,198**	**$ 5,097,466**	**$ 3,502,466**	**$ 2,862,466**	**$ 1,992,845**
General Fund Portion (54.4%)	***$ 2,250,091***	***$ 2,773,021***	***$ 1,905,341***	***$ 1,557,181***	***$ 1,084,107***

Additional information on the items listed above and other citywide projects, department priorities, and associated costs for the OneSD Fund will be presented to the Budget and Government Efficiency Committee early in calendar year 2016.

Customer Service and Open Government Priority Initiative

Planning

Citywide Parks Master Plan

The Park Master Plan (PMP) is anticipated to be comprised of several components including a comprehensive review of the needs of the current park system, identification of emerging trends and benchmarks from comparable agencies, public outreach, proposal of an equitable citywide distribution of park and recreation facilities, identification of high priority sites for parks, and development of strategic actions for implementing the plan. The Department has indicated that the complexity of the PMP will be based upon the funding available. The Outlook includes $200,000 annually from FY 2017 to FY 2019 for a total of $600,000 in funding to develop the PMP at a strategic level. The Department has indicated that they will continue to seek grant funding to supplement any potential General Fund support.

Potential Impacts of the draft Climate Action Plan (CAP)

The City’s draft CAP identifies five potential strategies for reducing greenhouse gas (GHG) emissions and preparing for climate change. These strategies include:

- Energy and Water Efficient Buildings
- Clean and Renewable Energy
- Bicycling, Walking, Transit, and Land Use
- Zero Waste
- Climate Resiliency

Components of the Zero Waste and Climate Resiliency strategies are included in the Outlook. The Zero Waste strategy is discussed in the ESD requests in an earlier section of this report. The Climate Adaptation Plan component of the Climate Resiliency strategy is discussed in the following section.

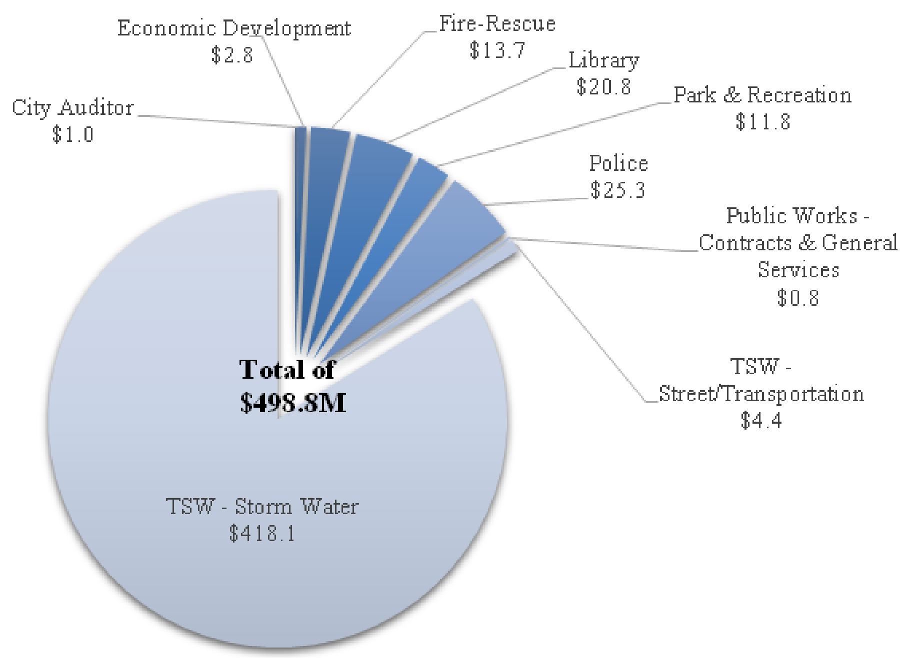
Support for the Climate Adaptation Plan

One of the strategies proposed with the City's draft Climate Action Plan (CAP) is Climate Resiliency. The Outlook proposes at total of $325,000 from FY 2018 to FY 2020 in support for the Climate Adaptation Plan (also known as resiliency planning) which is expected to aid the City in being better prepared for anticipated climate change impacts. According to the department, the objectives of the CAP are to identify areas most vulnerable to climate change impacts (such as water supply, fire preparedness, sea level rise), develop risk reduction strategies that protect resources, evaluate capital improvement projects to address potential impacts of climate change, and engage the public and decision-makers in a range of actions. The Department is working with other agencies to pursue grant funding to supplement any General Fund support.

DEPARTMENT REQUESTS: EXPENDITURES NOT FUNDED IN OUTLOOK

While approximately $430.6 million (over five years) of requests submitted by departments for inclusion in the Outlook were approved as part of the Mayor's priority expenditures, there was an additional $498.8 million (over five years) submitted by departments that was not accepted. As displayed in the chart below, the bulk of these requests were submitted by the Transportation & Storm Water Department (TSW); a discussion of TSW's unfunded requests and other significant department submissions and their potential impact on the Outlook are outlined in the following sections.

FY 2017-FY 2021 Five-Year Total of Departmental Funding Requests Not Included in the Outlook ($ in millions)



Library

Expansion of Library Service Hours

The Department provided a request to add 65.50 FTEs and approximately $4.0 million in annual costs to increase the core operation hours at all library facilities to 65 hours per week. This request would increase the Central Library operational hours by 4 hours per week from 61 to 65 hours, and the branch libraries core operational hours by 9.5 hours per week from 55.5 to 65 hours. The goal of the Department is to have every library facility open for the same operating hours per week. The Department has indicated that it has been able to incrementally add hours with the existing staffing structure, but any additional increase in operating hours would require changing the current structure to establish a second shift of staffing. The need to establish a second shift is the contributing factor to the large number of needed FTE positions and the total increase in annual costs.

Radio Frequency Identification (RFID) Conversion

The RFID technology has demonstrated that it offers enhanced security, increases automation and self-service capabilities, expedites inventory tasks, and allows staff to provide increased customer service to library patrons. Identified as a component of the new Central Library project, this technology has been implemented at the new Central Library. Remaining funding originally allocated for the implementation of this technology at the new Central Library is being used to initiate this program throughout the branch library system. Branches with the largest circulation levels will be the top priorities.

The FY 2016–2020 Outlook projected the available funding for this program to be fully expended in FY 2016, and requested a total of $950,000 in additional funding from FY 2017 to FY 2019 to continue this program. However, the conversion process and spend down of remaining funding is taking longer than originally expected. Due to the uncertainty related to the timing for additional funding to continue this program, the previous funding request was removed from the Outlook. As funding needs for this program become better defined, the Department has indicated that it will provide a request for funding consideration in a future financial outlook.

Park & Recreation

Additional Staffing for Recreation Centers

The FY 2016 Adopted Budget included the addition of 36.00 ARCD positions to increase service hours from 45 hours per week to 50 hours per week for the 36 recreation centers. Additionally, the FY 2016 Adopted Budget included 9.00 additional Recreation Center Leader 1 FTEs to further increase the hours at these locations from 50 hours per week to 60 hours per week. While the Outlook includes the addition of 23.00 ARCDs to increase core service levels at all recreation centers to 50 hours per week, should the City desire to increase services hours at all the recreation centers to 60 hours per week, an additional 5.75 Recreation Center Leader 1 FTEs and approximately $337,000 would need to be added during the Outlook period.

Brush Management

The Department provided a request to add 5.00 FTEs and up to approximately $1.4 million annually by the end of the Outlook period to support several brush management programs. Below are brief descriptions of the brush management programs and the projected financial impact of each for the Outlook period.

- Adjustments to the Open Space Brush Management Agreement: In January 2015, the City entered into an agreement with a new brush management vendor to clear 250 acres per year of Open Space areas. The agreement established a base fee for FY 2016 and allowed for annual cost increases based upon a cost index (capped at five % annually). The request from the Department represents the potential maximum increase per the agreement. The request increases from approximately $92,000 in FY 2017 to approximately $509,000 in FY 2021.

- Non-Open Space Brush Management: Mandated brush thinning in the San Diego Municipal Code for non-open space park parcels near and within developed parks is currently unfunded. The Department request is for 5.00 FTEs and approximately $578,000 in annual costs, with the one-time expense of approximately $143,000 for vehicle costs in FY 2017. Cost estimates may change as acres are identified.

- Undeveloped (Paper) Streets Program: Assumption of brush management responsibility for approximately 40 acres within paper streets for unused public rights-of-way adjacent to City-owned open space. The Department projects approximately $272,000 in annual costs for this program.

The following table reflects the unfunded brush management requests from the Department.

Requested Brush Management Programs										
Program	FY 2017		FY 2018		FY 2019		FY 2020		FY 2021	
Open Space Brush Management Agreement	0.00 FTEs	$92,175	0.00 FTEs	$188,959	0.00 FTEs	$290,582	0.00 FTEs	$397,286	0.00 FTEs	$509,325
Non-Open Space Brush Management	5.00 FTEs	$722,230	5.00 FTEs	$578,830	5.00 FTEs	$578,830	5.00 FTEs	$578,830	5.00 FTEs	$578,830
Paper Streets	0.00 FTEs	$271,780	0.00 FTEs	$271,780	0.00 FTEs	$271,780	0.00 FTEs	$271,780	0.00 FTEs	$271,780
Total	**5.00 FTEs**	**$1,086,185**	**5.00 FTEs**	**$1,039,569**	**5.00 FTEs**	**$1,141,192**	**5.00 FTEs**	**$1,247,896**	**5.00 FTEs**	**$1,359,935**

Penny for the Arts

On October 22, 2012, the City Council adopted the Penny for the Arts Five-Year Blueprint (Blueprint) with the goal of restoring arts, culture, and community festivals funding to FY 2002 funding levels, or approximately 9.5% of the City's annual projected TOT revenue. The full Blueprint goal of 9.5% of projected TOT was proposed to be realized in FY 2017, the first year of the recently released Outlook. The Blueprint funding level included in the Outlook for FY 2017 is 6.44%, which is the level of funding approved by Council in FY 2016 and is an increase over the Mayor's original FY 2016 proposed funding level of 5.7% of TOT, but below the FY 2016 Blueprint goal of 8.55%.

As noted in the Outlook, although the Blueprint funding level is held constant over the five years, the funds allocated to the program increase year-over-year due to projected annual increases in TOT revenue. While the Blueprint funding in the Outlook varies significantly from the Blueprint funding goals over the same timeframe (a difference of approximately $6.4 million in FY 2017 growing to a difference of $7.8 million in FY 2021), this Outlook represents an improvement over previous years as it maintains the increased funding level approved by the City Council in the FY 2016 Adopted Budget.

Transportation & Storm Water – Storm Water Projects

As noted in the Outlook and in IBA Report 13-44, the Municipal Storm Water Permit adopted by the Regional Water Quality Control Board (RWQCB) in May 2013 established more stringent water quality mandates and regulations that the City is required to meet. The Storm Water Division prepared and uses a Watershed Asset Management Plan (WAMP) to estimate funding needs for both operating and capital needs in order to address permit compliance, flood risk management, and the deferred capital storm drain assets. Costs necessary to ensure compliance are high.

Further, the first compliance deadlines associated with the new permit come in 2018. Significant increases in both operating and capital expenditures throughout the outlook period are necessary if the City is to ensure that it complies with storm water regulations.

While requirements for operations and maintenance in the Outlook are fully funded, capital costs for storm water projects are not. The table below shows the total costs identified in the WAMP, the total funding for storm water included in the Outlook, and the funding gaps each year.

Storm Water Funding Needs and Expenditure Projections					
	FY 2017	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Total Need	$ 120,621,658	$ 127,912,465	$ 142,381,899	$ 149,539,603	$ 156,081,847
Funding included in Outlook	75,005,124	75,074,621	83,056,202	66,542,437	66,944,918
Funding Gap	$ 45,616,534	$ 52,837,844	$ 59,325,697	$ 82,997,166	$ 89,136,929

As our Office has noted in past reports, and as is noted in the Outlook itself, the City will incur significant penalties if it is unable to meet the required storm water regulations by 2018. *Regulatory penalties include fees of $10,000 per day for violations from the RWQCB and $27,500 per day in federal EPA penalties*. If the City does not comply with the storm water permit requirements, it will also face a significantly increased risk of third party lawsuits.

It is becoming increasingly important for the City to identify funding sources necessary to comply with the new storm water permit. At present, the City collects a storm drain fee from water and sewer utility customers for the purpose of partially reimbursing the General Fund for storm water activities. That fee, however, only provides $5.7 million annually, which is well short of the total capital and ongoing needs of the storm water program: the total unfunded needs over the five years of the Outlook total $329.8 million. IBA reports #10-29, #13-44, and #14-43 all discuss the possibility of a storm drain fee increase, though before any increase could go forward, the City would need to prepare a cost of service study detailing the calculations necessary to determine an appropriate fee level.

The Outlook does note that the City is currently working with the RWQCB and the State Water Board to encourage reasonable implementation of storm water regulations, which could reduce projected compliance needs. The City has had success in working with the RWQCB to reduce the overall costs of compliance – these successes are included in the anticipated funding needs in this year's Outlook. However, even after successful negotiations, costs remain high.

To provide context, the following table shows the funding needs and anticipated expenditures that were projected in last year's Outlook, and the updated needs and expenditures that are included in this year's Outlook. The funding necessary for compliance has decreased substantially, while the projected expenditures have decreased in FYs 2017-18 and increased in FYs 2019-20.

Storm Water Funding – FY 2016-2020 Outlook and FY 2017-2021 Outlook				
($ in millions)	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**
FY 16-20 Outlook Compliance Funding Needs	$ 194.4	$ 233.0	$ 254.6	$ 215.1
FY 16-20 Outlook Projected Expenditures	87.2	83.9	60.1	62.1
FY 17-21 Outlook Compliance Funding Needs	120.6	127.9	142.4	149.5
FY 17-21 Outlook Projected Expenditures	$ 75.0	$ 75.1	$ 83.1	$ 66.5

While negotiations between TSW staff and the RWQCB have resulted in significant reductions in compliance costs, and while negotiations continue to be ongoing, given the magnitude of the funding gaps the City is facing, it is almost certain that significant amounts of additional funding beyond those included in the Outlook will be necessary to ensure compliance.

Fire-Rescue – Brush Management Program

The Outlook lists as an operational need, but does not fund, the addition of 8.00 FTE positions for a Fire-Rescue brush management program. The positions include 7.00 Code Compliance Officers and 1.00 Fire Prevention Supervisor. The Department has indicated that these positions would inspect parcels subject to brush management regulation. The Department has further indicated that of the items requested but not funded in the Outlook, the brush management program is its highest priority. This item is in addition to a separate request by the Park & Recreation Department for expanded brush management activities.

Police – Unfunded Items from the Department Five-Year Plan

The Outlook includes funding for the Police Department based on the Department's Five-Year Plan to the extent possible given limited resources. In addition, several items from the Plan were listed as operational needs but were not funded in the Outlook. Most of the requested items are part of the Five-Year Plan. A comparison of the Five-Year Plan and the initiatives included in the Outlook is provided in a table earlier in this report.

OTHER ISSUES AND POTENTIAL IMPACTS

In our review of the Outlook, we identified several items ***not*** submitted by departments for funding, but that may need to be addressed within the Outlook's five year timeframe.

Retirement ADC Considerations

The Outlook's defined benefit pension forecasts through FY 2021 are based on the most recently provided Actuarially Determined Contribution (ADC) projections from SDCERS' actuary, Cheiron, from the June 30, 2014 actuarial valuation. However, the ADC figures that were projected in the FY 2014 valuation are anticipated to be impacted by subsequent events as described in the following paragraphs.

First, the FY 2015 investment return of 3.3% was lower than the 7.25% returned assumed in the FY 2014 valuation. The impact of the lower investment return is a projected increase to the previously estimated FY 2017 General Fund ADC of roughly $4.4 million ($6.0 million for all funds). Accordingly, this lower return produced an investment experience loss.

Estimates for ADC impacts due to this experience loss have not been factored into the Outlook's pension figures. We concur with this approach as other experience gains and losses in the June 30, 2015 valuation have not been determined. However, for purposes of considering risks to the Outlook figures, we have included preliminary estimates related to the FY 2015 lower investment return in the table below.

Estimated ADC Increases Due to Lower than Assumed Investment Return					
($ in millions)	**FY2017**	**FY2018**	**FY2019**	**FY 2020**	**FY 2021**
Citywide	$ 6.0	$ 11.2	$ 15.5	$ 19.2	$ 22.5
General Fund	$ 4.4	$ 8.2	$ 11.4	$ 14.2	$ 16.5

Secondly, in November 2015 the SDCERS Board considered various options for changes to economic assumptions that will be included in the calculation of the FY 2017 ADC. Changes were made to both the discount rate and the wage inflation rate assumptions (which for the FY 2014 valuation were 7.25% and 3.3%, respectively). The Board approved reducing both the discount rate and the wage inflation rate assumptions by 0.125% for the FY 2015 valuation, and again by 0.125% for the FY 2016 valuation. The estimated increase to the FY 2017 General Fund ADC related to these changes is also approximately $4.4 million ($6.0 million all funds). The table below shows preliminary estimated impacts related to these assumption changes for all Outlook years.

Estimated ADC Increases Due to Economic Assumption Changes					
($ in millions)	**FY2017**	**FY2018**	**FY2019**	**FY 2020**	**FY 2021**
Citywide	$ 6.0	$ 12.4	$ 13.3	$ 14.3	$ 15.3
General Fund	$ 4.4	$ 9.1	$ 9.8	$ 10.5	$ 11.2

Other positive or negative impacts to the FY 2017 ADC that are related to demographic assumptions (for example those related to turnover, retirement, death, and disability) have not been determined. Because of the complexity of the pension system variables, the total of all effects on the ADC is unknown at this time; and the preliminary estimates above are only presented as a conservative approach to considering the reliability of projected Outlook surpluses.

The complete June 30, 2015 valuation that incorporates the economic assumption changes discussed above, the FY 2015 investment results, and all other FY 2015 experience gains and losses are expected to be available in January 2016. In addition to providing the FY 2017 ADC, the FY 2015 valuation is also anticipated to include updated ADC estimates for FY 2018-2021.

Lastly, the SDCERS actuary will be completing an "experience study" for Board review next summer. The experience study involves historical analysis of pension plan assumptions, including the rate of investment return, wage inflation, and retirement and mortality rates. The experience study and related analysis will be the basis for Cheiron's recommended changes in the plan's actuarial assumptions. The Board will consider any recommended assumption changes, and any approved changes would be included in the calculation of the FY 2018 ADC. Any such changes would affect estimated ADCs in future Outlook years as well. It is anticipated by Cheiron that there could be a "meaningful cost increase (2% to 6%)" related to assumptions regarding mortality.

Labor Agreement Reopeners for Employee Organizations

The City recently reached multiple-year labor agreements (ending FY 2020) with two of its employee organizations: the Police Officers Association (POA) and the Municipal Employees Association (MEA). General Fund cost increases due to increased compensation in these agreements are included in the Outlook's baseline forecast and total $16.4 million for FY 2017, rising to $43.3 million in FY 2021.

In the current five-year agreements with the City's four other employee organizations, there are reopeners allowing for negotiations over additional non-pensionable compensation for FY 2017 and FY 2018. Non-pensionable compensation increases would include flexible benefits increases, rather than salary increases. If the case arises where a labor agreement is negotiated that extends beyond FY 2018, pensionable salaries may be considered.

Though the Outlook does not anticipate any impacts due to these pending negotiations, for reference, each 1% compensation increase would total approximately $1.8 million for the General Fund. Note that this estimate also includes impacts related to employees who are not represented by an employee organization. The estimated impact of an annual 1% increase in compensation for all Outlook years is outlined in the table below.

Illustrative Cost for Employees Other Than POA & MEA					
($ in millions)	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Estimated Cost for Each 1% Annual Compensation Increase	$ 1.8	$ 3.6	$ 5.4	$ 7.2	$ 9.0

Note that the estimated figures above do not include San Diego City Employees Retirement System (SDCERS) pension impacts that may be applicable, or any compounding effects that may occur.

Additionally, a separate reopener in employee contracts pertains to death and disability benefits for employees who are members of the interim defined contribution plan (those not eligible for the defined benefit pension). The City is developing a plan for these benefits, which will be discussed with the employee organizations. Since negotiations are pending, the impact to the Outlook has not yet been determined.

Police Overtime

In our Office's review of the FY 2016 First Quarter Budget Monitoring Report (IBA Report 15-44), we note that the Police Department is projected to exceed budgeted overtime expenditures by $5.0 million, for a total of $23.0 million in FY 2016. In that report, we provide a detailed description of the causes of the overage and note that the projection is consistent with our predictions on the topic in previous reports. An overview of the Department's budgeted and actual overtime expenditures for the past five years is provided in the table below.

Police Department Overtime – Prior Years			
Fiscal Year	**Adopted Budget**	**Current Budget**	**Actuals**
FY 2016	$18.0 million	$18.0 million	$23.0 million (projected)
FY 2015	$11.1 million	$19.0 million	$23.1 million
FY 2014	$11.8 million	$13.8 million	$17.8 million
FY 2013	$17.1 million	$17.1 million	$19.7 million
FY 2012	$17.1 million	$17.2 million	$19.3 million

The FY 2016 overtime projection for the Police Department is essentially unchanged from the actual expenditures for FY 2015 at approximately $23.0 million. However, overtime expenditures included in the FY 2016 Adopted Budget were only $18.0 million—significantly less than the prior-year actuals. During the Budget and Government Efficiency Committee's consideration of the FY 2016 First Quarter Report, Financial Management indicated that the Police Department overtime budget was not adjusted to reflect prior-year actuals due to an assumption that sworn attrition rates would decrease and staffing levels would improve. In fact, this has not been the case.

As of November 30, 2015, the Department was experiencing a sworn attrition rate of 14 departures per month. In contrast, the FY 2015 and FY 2016 Adopted Budgets assumed an attrition rate of 9 departures per month. The effect of this persistently high attrition in excess of levels assumed in the budget is significant. In the current fiscal year, the Department has the budget authority to hire 172 new recruits by holding four expanded police academies of 43 recruits each. With an assumed attrition rate of 9 departures per month, the Department would be expected to lose 108 officers while gaining 172, for a net increase of 64. Should the current attrition rate of 14 departures per month continue for the remainder of the fiscal year, the Department will lose 168 officers while gaining 172, for a net increase of only four filled sworn positions. Attrition in excess of levels assumed in the budget has contributed to a higher-than-expected reliance on overtime for backfilling to meet recommended staffing levels.

Additionally, the Police Department has indicated that it has expanded its use of overtime in the form of extension-of-shift activities. This overtime is attributed to a number of factors, including increased neighborhood policing efforts, increased training by allowing more experienced officers to work alongside new officers, calls taking longer to resolve, and issues related to understaffing.

In light of significant overages in projected and prior-year actual expenditures on Police overtime, we note that Outlook projections do not include the likely scenario that these overages will continue. We anticipate that the Department's overtime expenditures will exceed Outlook assumptions by a range of $3.0 to $5.0 million across the five years of the Outlook period. This is based on our review of past overtime expenditures as well as the Department's current focus on extension-of-shift activities, the need for which we do not anticipate will change significantly over the next five years. While we estimate that gross overtime expenditures will continue to exceed current budget by $5.0 million each year, it is possible that a portion of that amount (up to $2.0 million) may be offset by unbudgeted revenue in the form of reimbursements. Therefore, we provide a range of $3.0 to $5.0 million.

Police Department Overtime – Anticipated Expenditures in Excess of Outlook Projections					
FTE/Rev/Exp	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
FTE	-	-	-	-	-
Revenue	$ -	$ -	$ -	$ -	$ -
Expense	$3.0-5.0M	$3.0-5.0M	$3.0-5.0M	$3.0-5.0M	$3.0-5.0M

Library Ordinance

The Library Appropriation Ordinance approved by the City Council in 2002 requires the Library Department budget to equal six percent of the General Fund's budget each fiscal year. Based upon the FY 2016 Adopted Budget, the funding for the Library Department represents approximately 3.85% of the General Fund Budget. While the Outlook continues modest contributions to the Library Department budget, the Library Budget as a percentage of the General Fund Budget continues to decline throughout the Outlook period. The following table illustrates the declining percentages based upon projections within the Outlook. The projections for the Outlook period for the Library Department budget would require the waiver of the Library Appropriation Ordinance throughout the Outlook period.

Library Appropriations Ordinance: Funding Shortfall					
($ in millions)	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Outlook	$1,310.8	$1,350.5	$1,382.5	$1,410.9	$1,429.8
Library Budget	49.3	49.6	50.5	51.3	50.9
Library Appropriation Ordinance Requirement (6% of General Fund)	78.6	81.0	83.0	84.7	85.8
Funding Shortfall	**$29.3**	**$31.4**	**$32.5**	**$33.4**	**$34.9**

Reserve Policy Discussions

Over the past few months, there have been discussions regarding modifying the City's Reserve Policy to set aside additional reserves, beyond those required in the current Reserve Policy. In October, the City's Chief Financial Officer (CFO) presented the Budget and Government Efficiency (B&GE) Committee with a proposal for setting aside a portion of Excess Equity (approximately $16.3 million) in a separate reserve that could be used to mitigate pension payment volatility arising from unanticipated increases to the City's Actuarially Determined

Contribution (ADC). This separate Pension Reserve would also include $4.9 million from Enterprise Funds for a total of $21.2 million.

A majority of B&GE Committee members at the October meeting raised concerns about the narrow use of the proposed reserve for unexpected pension payments only. They noted that the proposed reserve, as defined, lacked flexibility and that the proposed amount was not associated with any benchmarks or professional standards. They also questioned whether a separate pension reserve should be created, or alternatively should the City's General Fund Reserve be increased. Committee members approved a motion that directed staff and our Office to research the option of increasing the City's currently established General Fund Stability Reserve and to present the findings at a subsequent B&GE meeting.

Addressing the Committee's direction, our Office prepared IBA Report 15-41, "Options for Increasing the City's General Fund Reserve". Based on best practices mentioned in our report, we suggested that if the Committee is interested in increasing the General Fund Stability Reserve, an increase from 14% to 16% would be a suitable option. We also noted in our report that both methods—either increasing the General Fund Stability Reserve or creating a new pension reserve—are prudent. Both would achieve the intended purpose of identifying a source of funding for unanticipated increases in the City's pension ADC payment, while helping to avoid service reductions, and both would likely be favorably viewed by the rating agencies.

The B&GE Committee discussed IBA Report 15-41 on November 9, 2015, and forwarded the proposal to increase the General Fund Stability Reserve to the full City Council, without recommendation. This issue is anticipated to be heard at Council in January 2016.

On November 19, 2015 the B&GE Committee held another meeting, during which the Five-Year Outlook was presented. During discussions, Councilmember Alvarez requested information regarding the impact to the Outlook for both proposals discussed above. The table below shows the projected reserve requirements for an increased General Fund Stability Reserve (to 16% of operating revenues).

Projected 16% Reserve Requirement						
($ in millions)	**FY 2016**	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
3-Year Average Revenues	$ 1,136.1	$ 1,168.7	$ 1,184.7	$ 1,226.4	$ 1,268.6	$ 1,316.6
14% of Average Revenues	$ 159.0	$ 163.6	$ 165.9	$ 171.7	$ 177.6	$ 184.3
Increase in Requirement (14% to 16%)	$ 22.7	$ 23.4	$ 23.7	$ 24.5	$ 25.4	$ 26.3
16% of Average Revenues	**$ 181.8**	**$ 187.0**	**$ 189.6**	**$ 196.2**	**$ 203.0**	**$ 210.6**

The next table shows the projected amounts that would be available in the Outlook years for additional City services if the funding requirement for the Stability Reserve were to increase to 16% of operating revenues. The first line shows the available amounts for City services, per the Five-Year Outlook, after funding the Baseline Expenditures and Priority Initiatives. The next two lines show the reserve funding additions that would be needed as operating revenues increase over time. This additional funding is split into two components: the amount needed each year to fund the existing 14% reserve level and the additional amount to bring the reserve up to the 16% level.

The last line shows the remaining projected balance available for additional City services after accounting for the Outlook's Baseline Expenditures, Priority Initiatives, and 16% Reserve funding. This scenario assumes that all available funds are utilized in the year they become available, and are not carried forward to the next year as Excess Equity.

Projected Amount Available for Additional City Services After Five-Year Outlook Baseline Expenditures, Priority Initiatives, and 16% Reserve Funding						
($ in millions)	**FY 2016***	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Available Amount Per Outlook*	$ 31.3	$ 0.2	$ 7.9	$ 25.1	$ 46.4	$ 73.7
Amount for 14% Reserve Maintenance	-	(4.6)	(2.2)	(5.8)	(5.9)	(6.7)
Additional Amount for 16% Reserve	(22.7)	(0.7)	(0.3)	(0.8)	(0.8)	(1.0)
Amount Available for City Services	**$ 8.6**	**$ (5.0)**	**$ 5.3**	**$ 18.4**	**$ 39.6**	**$ 66.0**

*For FY 2016, the "Available Amount per Outlook" is the projected ending Excess Equity in the First Quarter Budget Monitoring Report (adjusted to incorporate updated revenue figures from the Office of the City Comptroller). The FY 2016 "Amount Available for City Services" is the adjusted ending Excess Equity amount remaining after funding the General Fund reserve to a 16% level.

With respect to the Pension Reserve alternative, the table below shows the projected amounts that would be available for additional City services if a new Pension Reserve were to be created. This scenario also assumes that all available funds are utilized in the year they become available, and are not carried forward to the next year as Excess Equity.

Projected Amount Available for Additional City Services After Five-Year Outlook Baseline Expenditures, Priority Initiatives, and Pension Reserve Funding						
($ in millions)	**FY 2016***	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**
Available Amount Per Outlook*	$ 31.3	$ 0.2	$ 7.9	$ 25.1	$ 46.4	$ 73.7
Amount for New Pension Reserve	(16.3)	-	-	-	-	-
Amount Available for City Services	**$ 15.0**	**$ 0.2**	**$ 7.9**	**$ 25.1**	**$ 46.4**	**$ 73.7**

*For FY 2016, the "Available Amount per Outlook" is the projected ending Excess Equity in the First Quarter Budget Monitoring Report (adjusted to incorporate updated revenue figures from the Office of the City Comptroller). The FY 2016 "Amount Available for City Services" is the adjusted ending Excess Equity amount remaining after funding the new Pension Reserve.

Mayor's Street Repair Goals

The Outlook contains expenditures consistent with those discussed in the Mayor's five-year street pavement repair program as it was presented to the Council in April, 2015. In our review of the program, we noted that the goal of repairing 1,000 miles of streets was obtainable, but that additional funding would need to be identified to ensure that the Overall Condition Index (OCI) of City streets could be improved to 70 by 2020.

The bulk of funding identified for the street repair program continues to come through dedication of two-thirds of future lease-revenue bond issuances to street repair. As lease-revenue bonds are not projected to continue throughout the five-year period of the Outlook, funding gaps for the street repair program exist in outer years. Per the Five-Year Financial Outlook and the Five-Year Capital Infrastructure Planning Outlook, the street repair commitment is fully funded through FY 2019, though additional funding will need to be identified in FY 2020 and 2021.

FY 2017-2021 Pavement Program Funding Needed vs. Projected						
$ in millions	**FY 2017**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**	**Total**
Need	$ 83.1	$ 83.1	$ 83.1	$ 83.1	$ 83.1	$415.5
Projected Expenditures	$ 83.1	$ 83.1	$ 83.1	$ 29.6	$ 35.8	$314.7
Shortfall	**$ -**	**$ -**	**$ -**	**$ 53.5**	**$ 47.3**	**$100.8**

Additional expenditures in the Outlook are projected to support streets, sidewalks, and other transportation projects in the following amounts:

Additional Expenditures for Streets, Sidewalks, and Transportation in Outlook *($ in millions)*				
FY 2017	**FY 2018**	**FY 2019**	**FY2020**	**FY 2021**
$ 7.3	$ 10.9	$ 21.1	$ 22.6	$ 28.5

This additional funding is not entirely dedicated to the street repair program, though a portion of it is anticipated to be used for street repairs.

The TSW Department has been conducting a condition assessment of all the City's streets this year. Results are expected to be released in early 2016, and will include an updated OCI and an inventory of City streets and the conditions of each street. That information will be used to develop future repair plans. The last full condition assessment for City streets was conducted in 2011, and showed an OCI of 54.6. Any increase in the OCI discovered in the most recent condition assessment would reduce the funding necessary to reach an OCI of 70 by 2020.

New Fire Stations – Operations Funded without Identified Capital Funding for Facilities

The Five Year Outlook includes a total of approximately $16.3 million in increased funding and the addition of 72.00 FTEs over the Outlook period to support the operation of five new fire stations. Operational expenses include personnel expenditures and non-personnel expenditures such as new fire engines and/or trucks and related equipment. These expenses are included as Priority Initiatives.

It is important to note that although the Fire-Rescue Department anticipates these stations will become operational by FY 2021, capital funding has not yet been identified to fully fund the design, land acquisition, and construction costs associated with these facilities. One exception is Bayside Fire Station (FS 2), which is anticipated to be fully funded by the Successor Agency to the former Redevelopment Agency. For the remaining four stations, it is unusual to include operational funds prior to capital funding being identified and completion schedules being determined. Remaining capital needs could be funded by future deferred capital debt issuances or new alternative sources of capital funding in future fiscal years. Details are provided in the table on the following page for new fire stations with operational funding included in the Outlook, according to their assumed operation year.

Capital Needs for Fire Stations Included as Priority Initiatives in Outlook		
Fire Station Name	**Remaining Capital Needs ($ in millions)**	**Status**
FY 2018		
Bayside Fire Station (FS 2)	$0.0	Construction costs fully funded by DIF and the Successor Agency to the former Redevelopment Agency. Construction is estimated to begin in January 2016, with completion anticipated in mid-2017.
FY 2021		
College Avenue Fire Station	$11.7	$270,000 in DIF funds identified for planning report and feasibility study; no additional funding. Total project cost $12.0 million.
Home Avenue Fire Station	$10.0	$2.0 million, primarily DC3 bond funds, identified for land and design. Total project cost $12.0 million.
Paradise Hills Fire Station (FS 54)	$11.1	No funding identified in CIP. Total project cost $11.1 million.
North University City Fire Station (FS 50)	$0.0	Project costs expected to be fully funded by FBA, including apparatus.
Total Remaining Capital Needs	**$32.8**	

CONCLUSION

The Mayor's Five-Year Outlook provides an accurate overview of the City's expected revenues, municipal services, and the Mayor's own goals and priorities. Revenue projections and economic growth assumptions in the Outlook are largely appropriate and reasonable, though some changes to RPTTF revenue figures may be necessary.

As is noted in the Outlook itself, the Outlook is not a budget, but is instead a plan that helps guide the City's long-range fiscal planning efforts, and serves as the framework for development of City's the FY 2017 budget. It is nevertheless important to recognize that the City has many priorities, programs, and needs that all compete for funding, even in improved economic times. As examples of programmatic needs and policy commitments, the City's storm water program, Library Ordinance, and Penny for the Arts program all have additional funding needs beyond what is included in the Outlook.

If full funding for existing programs and commitments were included in the Outlook, the surpluses currently projected would turn into deficits—a summary of known, likely, and possible impacts discussed in this report is reflected in the table on the following page.

It is reasonable and appropriate to project increased revenues in future years, but decisions regarding what programs should receive additional funding still need to be made. Council and community input will continue to be critically important in making those decisions.

($ in millions)	FY 2017 Outlook	FY 2018 Outlook	FY 2019 Outlook	FY 2020 Outlook	FY 2021 Outlook
Outlook Projected Revenues in Excess of Expenditures after Funding Initiatives[1]	**$ 0.2**	**$ 7.9**	**$ 25.1**	**$ 46.4**	**$ 73.7**
Summary of Known Impacts to the Outlook					
RPTTF Payments Overstated	1.9	2.0	2.2	2.4	2.6
ADC - Investment Changes[2]	4.4	8.2	11.4	14.2	16.5
ADC - Changes to Economic Assumptions[2]	4.4	9.1	9.8	10.5	11.2
Sub-total Known Impacts	**$10.7**	**$19.4**	**$23.4**	**$27.**	**$30.4**
Summary of Likely Impacts to the Outlook					
Police Department Overtime	3.0-5.0	3.0-5.0	3.0-5.0	3.0-5.0	3.0-5.0
Storm Water Additional Funding Needs	45.6	52.8	59.3	83.0	89.1
Labor Agreement Reopeners for Employee Organizations[3]	1.8	3.6	5.4	7.2	9.0
Sub-total Likely Impacts	**$50.4-52.4**	**$59.4-61.4**	**$67.7-70.7**	**$93.2-95.2**	**$101.1-103.1**
Summary of Possible Impacts to the Outlook					
Risk Scenario for Property Tax	-	-	15.5	21.4	27.5
Risk Scenario for TOT	-	-	3.4	4.8	6.3
Penny for the Arts	6.4	6.8	7.1	7.5	7.8
Library Ordinance	29.3	31.4	3.2	33.4	34.9
Proposed Firehouse Bond	TBD	TBD	TBD	TBD	TBD
"Rebuild San Diego": Sales Tax Growth, Pension Payment Savings to Infrastructure	TBD	TBD	TBD	TBD	TBD
Potential Environmental Growth Fund Charter Revisions	TBD	TBD	TBD	TBD	TBD
Sub-total Possible Impacts	**$35.8**	**$38.2**	**$29.4**	**$67.1**	**$76.5**

[1]Amounts remaining after accounting for the Baseline Expenditures and Priority Initiatives.

[2]Other positive or negative impacts to the Outlook's ADC figures that are related to demographic assumptions have not yet been determined. Because of the complexity of the pension system variables, the total of all effects on the ADCs is unknown at this time. The preliminary estimates above are only presented as a conservative approach to considering the reliability of any projected Outlook revenues in excess of expenditures.

[3]Amounts represent estimates for 1% annual compensation increases for the four employee organizations other than POA and MEA. Actual results of negotiations are unknown at this time and could be higher.

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Attachments: 1. FY 2017-2021 Five-Year Outlook: General Fund Position Additions
2. New/Enhanced Facilities Annual Costs

FY 2017-2021 Five-Year Outlook: General Fund Position Additions					
	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021
Streets, Sidewalks, and Active & Other Transportation	18.00	24.00	24.00	24.00	24.00
Storm Water - Flood Risk Management	14.00	26.00	30.00	30.00	32.00
Storm Water - Water Quality Improvement Projects	14.00	20.00	23.00	27.00	27.00
Library - Branch Expansions	0.00	2.00	5.67	5.67	5.67
New Pacific Highlands Ranch Library	0.00	0.00	0.00	8.50	8.50
Park & Recreation - New and Enhanced Facilities	20.88	32.98	44.05	50.25	51.25
Playground Outlay and Rubberized Surfacing	3.00	3.00	3.00	3.00	3.00
Expanded Hours at Recreation Centers	9.00	14.00	23.00	23.00	23.00
Zero Waste	18.00	18.00	18.00	18.00	18.00
Industry Standard/CIP Infrastructure Maintenance	21.00	42.00	63.00	84.00	105.00
New Fire Station Facilities	0.00	12.00	12.00	12.00	72.00
Advanced Lifeguard Academy	2.88	2.88	0.00	2.88	0.00
Urban Area Security Initiative (UASI) Improvement	3.00	3.00	3.00	3.00	3.00
Police Sworn Positions	5.00	10.00	15.00	20.00	25.00
Police Civilian Positions	3.00	6.00	9.00	12.00	15.00
Office of the Comptroller - Document Retention	1.00	1.00	1.00	1.00	1.00
City Treasurer - Revenue Auditor Positions	2.00	2.00	2.00	2.00	2.00
Redevelopment Successor Agency	2.00	2.00	2.00	2.00	2.00
TOTAL	**136.76**	**220.86**	**277.72**	**328.3**	**417.42**

NEW/ENHANCED FACILITIES ANNUAL COSTS

Department	Facility	Location of Facility (District)	FTE	First Year Annual Expense[1]	FY 2016 - 2020 Outlook
Fiscal Year 2017					
Park and Recreation	Angier Elementary School Joint Use Park[2]	7	0.30	$38,157	FY 2017
Park and Recreation	Black Mountain Ranch Community Park	5	2.30	279,919	FY 2017
Park and Recreation	Canyonside Community Park[2]	6	0.20	23,553	FY 2017
Park and Recreation	Civita Central Park	7	0.00	180,899	FY 2017
Park and Recreation	Del Mar Mesa Neighborhood Park[2]	1	0.90	98,433	FY 2017
Park and Recreation	Del Sur Neighborhood Park[2]	5	1.00	111,034	FY 2017
Park and Recreation	Mira Mesa Community Park Expansion - Phase 1[(2)]	6	1.30	154,002	FY 2017
Park and Recreation	Southcrest Trails Mini Park	9	0.50	57,066	FY 2017
Park and Recreation	Torrey Meadows Neighborhood Park[2]	5	0.80	94,510	FY 2017
Park and Recreation	Old San Ysidro Fire Station Park	8	0.05	5,932	New
Park and Recreation	Phyllis Place Park[2]	7	0.33	39,974	FY 2016
Park and Recreation	Wightman Street Neighborhood Park	9	0.20	19,986	FY 2016
Park and Recreation	Area Manager Support for New Facilities	Citywide	2.00	116,022	New
Park and Recreation	Citywide Maintenance Support[2]	Citywide	7.00	714,401	New
Park and Recreation	Staff for additional Open Space Acreage[2]	Citywide	4.00	386,437	FY 2017
Total Fiscal Year 2017			**20.88**	**$2,320,325**	

Department	Facility	Location of Facility (District)	FTE	First Year Annual Expense	FY 2016 - 2020 Outlook
Fiscal Year 2018					
Park and Recreation	Carmel Valley Neighborhood Park[2]	1	0.40	$51,568	FY 2018
Park and Recreation	Pacific Breezes Community Park[2]	8	2.00	259,514	FY 2018
Park and Recreation	Salk Neighborhood Park and Joint Use[2]	6	1.00	118,767	FY 2018
Park and Recreation	Linda Vista Skate Park	7	0.50	22,591	FY 2017
Park and Recreation	Pacific Highlands Ranch Community Park - CIP S10079[(2)]	1	5.50	429,792	FY 2020
Park and Recreation	Park de la Cruz Skate Park	9	0.50	33,516	New
Park and Recreation	Valencia Park	4	0.20	16,486	FY 2017
Park and Recreation	Citywide Maintenance Support[2]	Citywide	1.00	56,617	New
Park and Recreation	Staff for additional Open Space Acreage[2]	Citywide	1.00	45,302	FY 2018
Library	Skyline Branch	4	2.00	250,941	FY 2017
Fire-Rescue	Bayside Fire Station[3]	3	12.00	1,298,805	FY 2017
Total Fiscal Year 2018			**26.10**	**$2,583,899**	

Fiscal Year 2019					
Department	**Facility**	**Location of Facility (District)**	**FTE**	**First Year Annual Expense**	**FY 2016 - 2020 Outlook**
Park and Recreation	Canyon Hills Resource Park Improvements[2]	6	1.10	$152,321	FY 2019
Park and Recreation	Treena Mesa Sports Field Joint Use[2]	5	0.50	74,301	FY 2019
Park and Recreation	Cannon Street Mini Park[2]	2	0.10	7,328	New
Park and Recreation	Creative Performing & Media Arts JU[2]	6	0.60	85,566	New
Park and Recreation	Franklin Ridge Pocket Park	7	0.00	2,534	FY 2018
Park and Recreation	East Village Greens[2]	7	4.87	344,729	New
Park and Recreation	Fairbrook Neighborhood Park - CIP S01083[(2)]	5	0.20	28,013	FY 2018
Park and Recreation	North Park Mini Park	3	0.10	13,663	FY 2017
Park and Recreation	Riviera Del Sol NP	8	0.60	62,479	New
Park and Recreation	Citywide Maintenance Support[2]	Citywide	2.00	75,938	New
Park and Recreation	Staff for additional Open Space Acreage[2]	Citywide	1.00	45,302	FY 2019
Library	Mission Hills Branch	3	1.60	256,089	FY 2019
Library	San Ysidro Branch	8	2.10	235,026	New
Total Fiscal Year 2019			**14.77**	**$1,383,289**	

Fiscal Year 2020					
Department	**Facility**	**Location of Facility (District)**	**FTE**	**First Year Annual Expense**	**FY 2016 - 2020 Outlook**
Park and Recreation	Cubberley Elementary Joint Use[2]	6	0.40	$49,726	New
Park and Recreation	Dennery Ranch NP[2]	8	1.50	170,498	New
Park and Recreation	Gage Elementary Joint Use[2]	7	0.60	81,487	New
Park and Recreation	Hidden Trails NP	8	0.40	41,403	New
Park and Recreation	Wangenheim Joint Use Facility - CIP S15007[(2)]	6	0.30	38,507	FY 2019
Park and Recreation	Citywide Maintenance Support[2]	Citywide	2.00	85,638	New
Park and Recreation	Staff for additional Open Space Acreage[2]	Citywide	1.00	45,302	FY2020
Library	Pacific Highlands Ranch Branch	1	8.50	805,111	New
Total Fiscal Year 2020			**14.70**	**$1,317,672**	

Fiscal Year 2021					
Department	**Facility**	**Location of Facility (District)**	**FTE**	**First Year Annual Expense**	**FY 2016 - 2020 Outlook**
Park and Recreation	Staff for additional Open Space Acreage[2]	Citywide	1.00	45,302	New
Fire-Rescue	College Avenue Fire Station[3]	9	12.00	1,272,806	FY 2020
Fire-Rescue	Home Avenue Fire Station[3]	4/9	12.00	1,272,806	FY 2019
Fire-Rescue	Paradise Hills Fire Station[3]	4	24.00	2,545,612	FY 2019
Fire-Rescue	North University City Fire Station[3]	1	12.00	1,272,806	New
Total Fiscal Year 2021			**61.00**	**$6,409,332**	

[1]Figures do not include fringe expense on personnel expenses unless otherwise noted.
[2]Includes one-time expense for items such as vehicles in the first year of operation. One-time expenses eliminated from subsequent years operating costs.
[3]Figures include fringe expense for personnel costs.