



# IBA Review of the Mayor's Five-Year Financial Outlook for FY 2012-2016

Meeting of the Budget and Finance Committee

February 9, 2011



## Overview

- Mayor's Five-Year Outlook for FY 2012-2016 is 5<sup>th</sup> update in series of long-term outlooks
- Annual deficits range from \$56.7 million in FY 2012 improving to \$8.8 million deficit in FY 2016
- Annual deficits are lessened compared to prior Outlooks



## Overview

- Mayor is committed to bringing the Five-Year Outlook into balance by FY 2013
- Status of ten fiscal reforms provided
- Not all reforms can be completed in time to achieve deficit reduction for FY 2012 budget
- Some Council priorities not addressed



## Overview

- IBA review and analysis typically relies on comparisons with prior year actual results, and current year projections
- Neither were available during the review; should be forthcoming in the weeks ahead
- Unavailability of this data hampered review and reasonableness checks



## State Budget Impacts

- Outlook notes elimination of redevelopment agencies could have negative impact on General Fund by eliminating tax-sharing agreements and discouraging investment that could strengthen sales tax and TOT
- However, Outlook ignores positive impacts to General Fund due to allocation of tax increment revenues back to local agencies beginning in FY 2013



## State Budget Impacts

- Recommend that Financial Management work with the IBA to determine the potential increase in property tax revenues to City as more details of the Governor's proposal become available



# General Fund Revenue

- Most revenue categories consistent with previous versions of Outlook
- Given available data and current economic indicators and forecasts, most projections are appropriate
- Concern regarding Property Tax
- Highlight other large revenue changes



## Property Tax

- Varying factors will impact Property Tax, leading to possible negative growth in FY 2012, and a slower than forecasted recovery in outer years of the forecast
- The “pessimistic” forecast for Property Tax in the Outlook may be more appropriate
- Using pessimistic forecast, deficit could increase by \$3.8 million in FY 2012, and additional \$21 million in FY 2016





## Property Tax

- The California Consumer Price Index (CCPI) that is applied as assessed valuation growth for properties that have not changed ownership or had structural improvements in the past year is 0.753 for the FY 2012 property tax roll
- Improved from FY 2011 CPI of negative 0.2; likely not enough to offset other negative factors



## Property Tax

- Properties that received Prop 8 temporary reassessments to reflect market conditions may not increase in value due to relative flat growth in market values since the reassessments were conducted
- Recent information from the County Assessor's Office shows refunded amounts resulting from assessment appeals will increase in FY 2011, even though number of appeals has declined



## Sales Tax

- Sales Tax current performance exceeding projections thus far in the fiscal year
- Current base year projection for sales tax reflects 2.0% growth over previous year performance for the remainder of the fiscal year; most recent quarter receipts demonstrate growth of 4.3% over prior year (reflecting sales activity July –September 2010)



## Fines, Forfeitures and Penalties

- In November 2010, Council authorized increase in parking citation fees for State-mandated surcharges previously paid by General Fund
- Estimated to save General Fund \$1.75 million in FY 2011 mid-year, and \$3.5 million in FY 2012 and beyond
- Now reduced to \$3.2 million annually; under review by Police Department



## Interest Earnings

- Interest earnings projected to grow by 360% from \$1.7 million in FY 2012 to \$6.1 million in FY 2014
- Increase based on expected recovery of financial markets and anticipation that yields will increase to historical long-term average over next few years
- Reasonable to expect interest earnings will increase as pool becomes reinvested at higher rates (Yield on pooled assets fell to approx 1% in Dec 2010)



# General Fund Expenditures

- Expenditures increase \$81.8 million over five year period
- Largest area of increase is Retirement/Pension of \$63 million (over 77% of total)
- Next largest increase is due to two planned bond issuances for deferred capital projects (\$14.8 million) in the Other category



## Salaries & Wages

- No salary increases or restoral of 6% reduction for next five years
- **Vacancy Savings** – no longer separate line item
  - Adjusted \$1.7 million to correct 2011 amount
  - Cannot evaluate with limited information
- **Annual Leave Liability**
  - Estimated costs for accrued leave as employees depart City; significantly reduced from \$16 million to \$6.3 million in FY 2014



## Pension

- June 30, 2010 UAL is \$2.15 billion
  - Up from \$2.11 billion at June 30, 2009
- FY 2012 ARC estimated at \$231.2 million
  - Increase of \$2.1 million from \$229.1 million in FY 2011
  - General Fund contribution of \$179.2 million, up \$1.6M
- Reduction of \$21.2 million for FY 2012 since prior Outlook for General Fund





## OPEB – Retiree Health

- According to the City’s Budget Policy, the Outlook should “include the following amounts for each of the forecast’s five years for retiree health care: the Annual Required Contribution (ARC); pay-as-you-go costs; and the unfunded liability, based on the following two scenarios:
  1. Based on current funding strategy of pay-as-you-go amount plus some additional amount for pre-funding future liability for retiree health (lower than the ARC).
  2. Based on payment of the full ARC each year.”



## OPEB – Retiree Health

- City is preparing for negotiations with all labor unions regarding the appropriate level of retiree health benefits
- It is anticipated that there will be an agreement on a new benefit level to be effective July 1, 2011
- \$57.8 million has been included for each year of the Outlook, matching FY 2011 amount



## OPEB – Retiree Health

- Payment of the full Annual Required Contribution (ARC) for retiree health care costs is not legally required
- Guiding Principle #10 calls for a plan to fully fund the Retiree Health Care ARC
- Additional amounts needed for full ARC without reforms:

	<u>City-wide</u>	<u>General Fund</u>
FY 2012 OPEB ARC without reforms:	\$98.5 million	\$68.5 million
Current Amount in Outlook:	<u>\$57.8 million</u>	<u>\$40.2 million</u>
Additional needed to fund ARC	\$40.7 million	\$28.3 million



## OPEB – Retiree Health

- Inclusion of the additional funding need of \$28.3 million for payment of full ARC without reform would bring the FY 2012 General Fund deficit to \$85.0 million
- Retiree health care reform key to permanently lowering annual retiree health care costs



# Non-Personnel Expenditures

- **Supplies; Contracts; Information Technology**
  - 0% annual growth for these categories
  - Includes \$ for elections, removal of one-times
  - No savings estimated for IT competition
- Though not described, funding for **Community Plan Updates** has been increased from \$800K annually to:
  - \$1.2 million in FY2012
  - \$2.8 million in FY2013
  - \$2.15 million in FY2014
  - \$250K in FY2015



# Non-Personnel Expenditures

- Energy & Utilities – 5% growth
  - Consistent with prior Outlooks
- “Other” category includes transfers, debt payments; this includes Mission Bay Lease Revenues, some transfers to Reserves



# Mission Bay Lease Revenues

- Mission Bay lease revenues are projected to grow by two percent annually
- Proposition C, approved November 2008, amended City Charter to establish a threshold amount of Mission Bay lease revenue deposited in General Fund, and specifies how excess funds shall be allocated



## Mission Bay Lease Revenues

- From FY 2010 to FY2014 the General Fund threshold is \$23 million; in FY 2015 and continuing thereafter, the threshold is lowered to \$20 million
- Excess Mission Bay lease revenues are allocated to the Mission Bay Park and Regional Park Improvement Funds according to formula; increasing transfers are reflected in the Outlook reaching \$9.1 million in FY 2016





## Reserves

- Outlook includes funding to meet reserve policy goals, consistent with revised policy currently awaiting approval
- Total of \$14.1 million required in FY 2012, declining to \$12.0 million in FY 2016
- General Fund policy goal to reach 8% by FY 2013; Public Liability & Workers' Comp. policy goal to reach 50% of claims by FY 2014



## New Facilities

- List not provided in Outlook as in past
- In response to questions, IBA learned:
  - Various Park and Recreation locations coming on-line in each fiscal year, including:
    - W Lewis & Falcon St
    - Linda Vista Terrace
    - Del Mar Mesa
    - Treena Mesa
    - Pacific Breezes Community Park
  - Bayside Fire Station starting in FY 2013



## New Facilities - Main Library

- No changes since last version
- Scheduled to open in FY 2014
- Outlook assumes no net General Fund impact
- Additional operating costs anticipated to be offset with private donations and new revenue



## Storm Water Compliance

- Outlook includes \$35.2 million per year for Storm Water compliance
  - No increase from FY11 Budget; expect to comply with current Municipal Permit
- New permit to become effective during Outlook may result in additional regulations
- Staff indicated during last budget review that Cost of Service Study was underway; results were expected in December 2010



## Fire-Rescue Restorations

- At the January 26, 2010 PS&NS Committee meeting, Mayor's Office indicated there are no plans to restore rolling brownouts in FY 2011
- For FY 2012 and beyond, Mayor's Office working with Fire-Rescue Department on strategy to phase-in the restoration of overtime
- Details of phase-in not yet available



## Fire-Rescue Restorations

- Any level of restorations will add to the deficit in the years of the phase-in
- FY 2011 reduction due to implementation of rolling brownouts was \$11.5 million total
- Full-year restoration of each browned-out engine company requires an additional \$1.4 million
- Council priority not addressed in Outlook



## Civic Center

- Prior Outlook included specific line item of \$5.5 million for CAB Fire Sprinklers, and described four scenarios for Civic Center:
  - Two for new construction; two for continued occupancy
- CAB Sprinklers funding eliminated in FY 2011
- CAB needs and Civic Center plans not explicitly addressed in new Outlook



## Civic Center

- At 2/7 Council meeting, COO indicated that:
  - Civic Center project no longer being pursued
  - CAB sprinklers are planned to come forward for Council action in Fall 2011
  - Funding for CAB sprinklers of \$4 million will come from bond proceeds for deferred capital
- Previous Outlook had indicated that sprinkler costs not eligible for deferred capital bonds
- This issue needs to be resolved





## Deferred Capital

- Outlook includes debt service payments for the first March 2009 issuance; proposes two additional \$100 million issuances in FYs 2012 and 2015
- Prior Five-Year Outlook projected two additional bond issuances in FYs 2011 and 2013; bond issuances now postponed



## Deferred Capital

- Current backlog of deferred capital/infrastructure projects is still estimated to be \$800-\$900 million
- Long-term plan to address full backlog is not discussed in Outlook
- Not yet in line with Guiding Principle #11 which calls for plan to fund needs to reduce backlog and adequately fund capital needs



## Deferred Capital

- In IBA review of FY2011 Proposed Budget, staff estimated “catch-up” funding to a “high level of service” for Streets, Facilities, and Storm Drains would require \$564 million
- Funding is also required for “On-Going” maintenance of City’s Capital assets at a specified level



## Deferred Capital

- IBA review of FY2011 Proposed Budget, staff estimated current budget includes \$86.9 million for the maintenance of the three main asset classes (Streets, Facilities, and Storm Drains)
- FY 2011 funding for Streets not sufficient to prevent backlog from increasing; other assets may have same situation
- Once policy is developed, Outlook should reflect annual requirements



## Potential Solutions

- Managed Competition
  - May result in savings over Outlook period
- Pension & Benefit Reforms
  - Significant potential savings
- New Revenues
  - Previously discussed, but little political support; require voter approval
- User Fee Reviews and Adjustments
  - Status uncertain; potential for Police/Fire fees



## Potential Solutions

- Third Amendment to Ballpark Cooperation Agreement approved by City Council and Redevelopment Agency on February 8, 2011 will mitigate \$11.3 million annually in Fiscal Years 2014, 2015 and 2016, and is not currently shown in the Outlook
- Agreement will extend until 2032



## Conclusion

- Many past actions have been taken to move City toward financial health
- Without these accomplishments, fiscal challenges would be even more daunting
- Largely concur with Outlook projections
- Additional detail and actual prior year results needed to review properly



## Conclusion

- Annual deficits of \$56.7 million to \$8.8 million over five years of Outlook:
  - Does not reflect possible “pessimistic” property tax outlook
  - Does not assume any increases in service levels
  - Does not include any restoration of Fire-Rescue rolling brownouts
  - Assumes retiree health care reform to reduce costs, or continuing practice of not paying full ARC for retiree health
  - Assumes no salary increases for five years





## Conclusion

- Few viable budget solutions available other than deep budget reductions and service cuts
- Reforms will assist in elimination of long-term structural deficit



## Conclusion

- Council adopted eleven Guiding Principles for Structural Budget Deficit Elimination in February 2010
- Principle #4 states *“prepare a 5-year Outlook each year and provide numeric values for alternative budget balancing options based on input from City Council, Mayor and IBA; be prepared each year to discuss alternative budget balancing options with the Budget Committee or City Council should the Outlook suggest an ongoing structural deficit.”*



## Conclusion

- The Budget Committee and/or the City Council may wish to discuss reasonable requests to be made of the Mayor to incorporate specific budget balancing options in the Five-Year Outlook, as agreed to in the Principles, and present them at future meeting
- IBA intends to prepare written report for Council meeting of 2/14