



IBA Review of the Mayor's Five-Year Financial Outlook for FY 2014-FY 2018

November 26, 2012

IBA Revised Outlook FY 2014-2018



- The IBA agrees with the underlying revenue and expenditure assumptions in the baseline forecast of the Mayor's Outlook
- However, our review identifies significant risks and pending policy issues, the impacts of which have not been reflected in the Mayor's projections

IBA Revised Outlook FY 2014-2018



- None of these issues are surprises, they have all been publicly vetted numerous times by Council Committees and full Council over the past 18 months
- Because they are not surprises and they carry significant financial impact, it is important to discuss them in the context of the Five-Year Outlook

IBA Revised Outlook FY 2014-2018



- We have incorporated the potential financial impact of these items into our IBA Revised Outlook
- This shifts the Outlook from five years of surpluses to five years of potential deficits if some or all of these events were to occur
- It is important for the City Council and the public to be fully aware of the financial challenges and difficult choices that lie ahead

Risks to the Mayor's Outlook



- We have identified three categories of risks to the Mayor's Outlook:
 1. Non-Discretionary Expenditures
 2. Discretionary Expenditures
 3. Revenue Sensitivity

Risks to the Mayor's Outlook



- *Non-discretionary Expenditures:*
 - Fall into two separate categories:
 1. Events that are uncertain whether they will occur, but the financial impacts must be addressed if they do occur
 2. Events that have occurred but their impact is still being analyzed

Risks to the Mayor's Outlook



- *Non-Discretionary Expenditure Additions to the Outlook Include:*
 1. Redevelopment Dissolution
 2. Lower than Assumed Investment Return for Pension Plan
 3. Pension Changes and Proposition B

Risks to the Mayor's Outlook



- *Discretionary Expenditures:*
 - These are significant programmatic needs, not included in the Mayor's Outlook that have been identified as priorities for future funding through recent Council Committee deliberations or City Council action

Risks to the Mayor's Outlook



- *Discretionary Expenditure* Additions to the Outlook Include:
 4. Deferred Capital “Enhanced Option B” vs. “Status Quo”
 5. Penny for the Arts Blueprint
 6. Full Funding for 35 Member Police Academies

Risks to the Mayor's Outlook



- *Revenue Sensitivity:*
 - While we believe the revenue assumptions in the Mayor's Outlook are appropriate, we address the possibility of fluctuations by including the impact of more modest sales tax and property tax revenue projections than what are shown in the Mayor's Outlook

Risks to the Mayor's Outlook



- *Revenue Scenario* Additions to the Outlook Include:
 7. More Modest Sales Tax Projections
 8. More Modest Property Tax Projections

Non-Discretionary Expenditures:



1) GF Impact of Redevelopment Dissolution

- Debt service payments for Petco Park and Convention Center Phase II in ROPS 3 may be denied by the California DOF - \$14.3 million has been added to the Revised Outlook in FY 2014 increasing to \$16.3 million in FY 2018
- State Controller could also exercise “Clawback” provision for FY 2012 and FY 2013 payments which could impact the General Fund by an additional \$28 million
- Our Revised Outlook does not include this additional \$28 million impact, which would likely have to be paid in FY 2013

Millions of Dollars

	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Petco Park Improvements	\$ 11.3	\$ 11.3	\$ 11.3	\$ 11.3	\$ 11.3
Convention Center Phase II Expansion	3.0	3.5	4.0	4.5	5.0
Total	\$ 14.3	\$ 14.8	\$ 15.3	\$ 15.8	\$ 16.3

Non-Discretionary Expenditures:



2) Pension Plan Investment Experience Loss

- SDCERS assumed a FY 2012 pension plan investment return of 7.5%
- Latest estimates from SDCERS of the impact of lower than assumed investment return is not included in the Mayor's Outlook. SDCERS now reports investment return at 0.9%, revised from earlier reports of 0.3%

Estimated ARC Increases Due to Lower than Assumed Investment Return

(in millions)	FY 2014 Forecast	FY 2015 Forecast	FY 2016 Forecast	FY 2017 Forecast	FY 2018 Forecast
Citywide	\$ 7.8	\$ 14.5	\$ 20.2	\$ 25.0	\$ 29.2
General Fund	\$ 6.0	\$ 11.2	\$ 15.6	\$ 19.3	\$ 22.7

Non-Discretionary Expenditures:



3) Pension Plan Change – Proposition B

- The following table shows the estimated cost increases to the ARC due to a change in the UAL payment methodology – per the Proposition B fiscal analysis
 - It is now uncertain as to whether this methodology will be used to calculate the FY 2014 ARC (and future ARC estimates)
 - SDCERS is in the process of analyzing whether and how new GASB standards will apply to the FY 2012 valuation/FY 2014 ARC

Estimated ARC Increases Due to UAL Payment Change

(in millions)	FY 2014 Forecast	FY 2015 Forecast	FY 2016 Forecast	FY 2017 Forecast	FY 2018 Forecast
Citywide	\$ 27.7	\$ 22.7	\$ 17.6	\$ 12.5	\$ 7.2
General Fund	\$ 21.6	\$ 17.7	\$ 13.7	\$ 9.7	\$ 5.6

Non-Discretionary Expenditures



COMPARISON OF MAYOR'S OUTLOOK TO IBA REVISED OUTLOOK SCENARIO

<i>\$ in millions</i>	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Mayor's Five-Year Outlook "Baseline"	\$ 4.9	\$ 6.1	\$ 32.2	\$ 62.0	\$ 94.2
IBA Adjustments					
<u>Non-Discretionary Adjustments</u>					
1.) Redevelopment Impacts	\$ (14.3)	\$ (14.8)	\$ (15.3)	\$ (15.8)	\$ (16.3)
2.) Pension Plan Investment Experience Loss	(6.0)	(11.2)	(15.6)	(19.3)	(22.7)
3.) Pension Change - Proposition B	(21.6)	(17.7)	(13.7)	(9.7)	(5.6)
Sub-Total Non-Discretionary Adjustments	\$ (41.9)	\$ (43.7)	\$ (44.6)	\$ (44.8)	\$ (44.6)
Revised Outlook - "Baseline" + Non-Discretionary	\$ (37.0)	\$ (37.6)	\$ (12.4)	\$ 17.2	\$ 49.6

Discretionary Expenditures:



4) Deferred Capital – “Enhanced Option B” vs. “Status Quo”

- Achieving “Status Quo” requires a higher level of funding in order to prevent further deterioration of our assets
- Due to staff capacity and resource constraints, Council adopted “Enhanced Option B” funding plan, which was determined to be achievable and affordable and was recommended by our office and also supported by the Mayor’s Office
- While it is an aggressive and achievable funding plan, it is estimated slow deterioration to 5-10% over the five-year period
- B&FC requested to know the impact on the Outlook of achieving the higher “Status Quo” funding level. Long term financing rather than cash funding should also be evaluated

Discretionary Expenditures:



4) Deferred Capital – “Enhanced Option B” vs. “Status Quo”

Deferred Capital – Difference in Funding

\$ in millions	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	Total
Status Quo/Preventing Further Deterioration						
Operations and Maintenance	53.8	54.9	56.0	57.1	58.2	280.0
Net Bond (for Capital Projects)	105.2	105.2	105.2	105.2	105.2	526.0
Total	159.0	160.1	161.2	162.3	163.4	806.0
Enhanced Option B						
Operations and Maintenance	54.1	50.0	62.0	66.0	79.0	311.1
Net Bond (for Capital Projects)	75.0	80.0	81.0	90.0	84.2	410.2
Total	129.1	130.0	143.0	156.0	163.2	721.3
<i>Difference</i>	<i>(29.9)</i>	<i>(30.1)</i>	<i>(18.2)</i>	<i>(6.3)</i>	<i>(0.2)</i>	<i>(84.7)</i>
New Issuance of CIP Bonds	25.0	-	-	-	-	25.0
<i>Difference</i>	<i>(4.9)</i>	<i>(30.1)</i>	<i>(18.2)</i>	<i>(6.3)</i>	<i>(0.2)</i>	<i>(59.7)</i>

Discretionary Expenditures:



5) Penny for the Arts Blueprint

- On October 22, 2012 City Council approved the Penny for the Arts Blueprint proposal to increase arts and culture funds from \$7.8 million in FY 2013 to \$17.9 million in FY 2017
- This item was approved shortly after the Mayor's Outlook was released, and was supported by the Mayor
- This proposal contemplated using growth in TOT revenues to fund these increases. However, the Mayor's Outlook assumed this revenue growth would be used for other eligible expenses
- Therefore, implementing the Blueprint could require additional resources or impact other TOT funded programs

Discretionary Expenditures:

5) Penny for the Arts Blueprint



Impact of the Implementation of the Penny for the Arts Five-Year Blueprint on Five-Year Outlook (in millions)

Arts, Culture, and Festivals Allocation	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Five-Year Outlook	\$ 7.8	\$ 7.8	\$ 7.8	\$ 7.8	\$ 7.8
Penny for the Arts Blueprint	11.6	13.8	15.4	17.9	17.9
Increase Over Outlook Assumption	\$ 3.8	\$ 6.0	\$ 7.6	\$ 10.1	\$ 10.1

* Calculation may reflect rounding.



Discretionary Expenditures:

6) Full Funding for 35 Member Police Recruit Academies

- The Mayor's Outlook states that funding has been included to increase academy classes from 30 to 35 recruits for four academies per year
- The \$500,084 in funding included in the Mayor's Outlook to support 20 additional recruits annually will not fully fund related personnel costs
- Available salary savings from vacancies will be absorbed with larger academies in FY 2014 and beyond
- The Outlook does not adjust the department's budgeted salary savings to allow for an additional 20 recruits annually

Funding for 35 Recruit Academy Personnel Costs (in millions)

	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Five-Year Outlook	\$ 0.5	\$ 0.5	\$ 0.5	\$ 0.5	\$ 0.5
IBA Estimated Incremental Increase	8.2	13.5	18.9	24.3	29.6
Estimated Additional Costs	\$ 7.7	\$ 13.0	\$ 18.4	\$ 23.8	\$ 29.1

Discretionary Expenditures



COMPARISON OF MAYOR'S OUTLOOK TO IBA REVISED OUTLOOK SCENARIO

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IBA Adjustments					
<u>Non-Discretionary Adjustments</u>					
1.) Redevelopment Impacts	\$ (14.3)	\$ (14.8)	\$ (15.3)	\$ (15.8)	\$ (16.3)
2.) Pension Plan Investment Experience Loss	(6.0)	(11.2)	(15.6)	(19.3)	(22.7)
3.) Pension Change - Proposition B	(21.6)	(17.7)	(13.7)	(9.7)	(5.6)
Sub-Total Non-Discretionary Adjustments	\$ (41.9)	\$ (43.7)	\$ (44.6)	\$ (44.8)	\$ (44.6)
Revised Outlook - "Baseline" + Non-Discretionary	\$ (37.0)	\$ (37.6)	\$ (12.4)	\$ 17.2	\$ 49.6
<u>Discretionary Adjustments</u>					
4.) Deferred Capital "Enhanced Option B" vs. "Status Quo"	\$ (30.1)	\$ (18.2)	\$ (6.3)	\$ (0.2)	\$ 1.1
5.) Penny for the Arts Blueprint	(3.8)	(6.0)	(7.6)	(10.1)	(10.1)
6.) Full Funding for 35 Member Police Recruit Academies	(7.7)	(13.0)	(18.4)	(23.8)	(29.1)
Sub-Total Discretionary Adjustments	\$ (41.6)	\$ (37.2)	\$ (32.3)	\$ (34.1)	\$ (38.1)
Revised Outlook - "Baseline" + Non-Discretionary + Discretionary	\$ (78.6)	\$ (74.8)	\$ (44.7)	\$ (16.9)	\$ 11.5

Revenue Sensitivity Analysis:



7) Sales Tax

- The Outlook's annual sales tax growth projections are more optimistic than that of the City's sales tax consultant MuniServices, LLC
- More modest sales tax projections, in line with the City's consultant, would lower projections significantly
- Despite vulnerability, we support the Outlook's current projections, but show the impact if sales tax performance is lower than expected

Impact of More Modest Sales Tax Growth Projections on Five-Year Outlook Forecast

Forecast	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
MuniServices	5.8%	2.4%	3.4%	3.7%	3.6%
Five-Year Outlook	5.5%	5.5%	6.0%	6.0%	6.0%
\$ Impact on Outlook	\$ (0.2)	\$ (8.3)	\$ (14.9)	\$ (22.7)	\$ (30.9)

Revenue Sensitivity Analysis:



8) Property Tax

- Based on the Office of the County Assessor's preliminary assessment, assessed valuation growth impacting FY 2014 collections will likely range from 0 to less than 1 percent
- Gradual growth should be anticipated over the years of the Outlook
- The IBA Scenario shows the potential impact of more modest property tax growth assumptions

Impact of More Modest Property Tax Growth Projections on Five-Year Outlook Forecast
(in millions)

Forecast	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Five-Year Outlook	\$ 393.9	\$ 405.3	\$ 420.4	\$ 440.2	\$ 460.8
<i>Growth Rate</i>	<i>1.5%</i>	<i>2.5%</i>	<i>3.5%</i>	<i>4.5%</i>	<i>4.5%</i>
IBA Scenario	\$ 388.5	\$ 394.3	\$ 404.2	\$ 418.3	\$ 437.2
<i>Growth Rate</i>	<i>0.5%</i>	<i>1.5%</i>	<i>2.5%</i>	<i>3.5%</i>	<i>4.5%</i>
\$ Impact on Outlook	\$ (5.4)	\$ (10.9)	\$ (16.2)	\$ (21.9)	\$ (23.7)

**Property tax totals do not include the RDA pass-through.*

IBA Revised Outlook FY 2014-2018



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Revised Outlook - "Baseline" + Non-Discretionary + Discretionary	\$ (78.6)	\$ (74.8)	\$ (44.7)	\$ (16.9)	\$ 11.5
<u>Revenue Sensitivity Analysis</u>					
7.) Sales Tax Sensitivity	\$ (0.2)	\$ (8.3)	\$ (14.9)	\$ (22.7)	\$ (30.9)
8.) Property Tax Sensitivity	(5.4)	(10.9)	(16.2)	(21.9)	(23.7)
Sub-Total Revenue Sensitivity Analysis	\$ (5.6)	\$ (19.2)	\$ (31.1)	\$ (44.6)	\$ (54.6)
Revised Outlook: "Baseline" + Non-Discretionary + Discretionary + Revenue Sensitivity	\$ (84.2)	\$ (94.0)	\$ (75.8)	\$ (61.5)	\$ (43.1)

Resources Potentially Available



- \$28.5 million was set aside in the FY 2013 General Fund Reserve to help mitigate potential impacts of redevelopment dissolution
- This \$28.5 million is part of the \$153.4 million in General Fund reserves, which equals 13.3% of revenues, in excess of the 8% policy goal
- Use of reserves should be exercised with extreme caution; however, this \$28.5 million was set aside for this very purpose

Resources Potentially Available



- If it is necessary to use the full \$28.5 million to address redevelopment impacts, the reserve would still stand at \$125.3 million or 10.8% of revenues & still exceed the 8% policy requirement
- Additionally, \$10.7 million TOT fund balance remains available as well to help address redevelopment or other issues

Other Outstanding Expenditure Issues (not included in either Outlook)



- *Implementation of the Fire-Rescue Citygate Report*
 - \$53.3 million of identified needs remain including \$39.2 million to fund costs associated with 4 new fire stations
 - Funding sources to support long term bond financing will likely need to be identified for these stations
 - Future outlooks will need to incorporate related staffing costs for new stations estimated at a minimum of \$2.2 million per station annually

Other Outstanding Expenditure Issues (not included in either Outlook)



- *Additional Public Safety Expenditures Proposed by Mayor-elect Filner*
 - On November 15, 2012, Mayor-elect Filner announced plans to fund an additional \$21.6 million in public safety expenditures

DESCRIPTION	COST	
Police Department		
Replacement of Public Safety CAD System	\$	8.0
Refurbishment of Firing Range		2.0
Sub-Total	\$	10.0
Fire-Rescue Department		
Home Avenue Fire Station Design, Construction, and Engine	\$	9.5
Paradise Hills Fire Station Design		0.8
Mission Valley Fire Station Engine		0.8
Cliff-Rescue Vehicle		0.5
Sub-Total	\$	11.6
TOTAL EXPENDITURE	\$	21.6

Other Outstanding Expenditure Issues (not included in either Outlook)



- *Additional Public Safety Expenditures Proposed by Mayor-elect Filner*
 - If approved by Council, operating costs associated with the Home Avenue and Mission Valley fire stations would add approximately \$4.4 million per fiscal year to the Outlook and CAD funding would need to be advanced
 - It is our understanding that a realistic implementation timeline for CAD is 3-5 years, which is consistent with the Mayor's Outlook. It is unclear whether funds could be expended any sooner as recently proposed

Other Outstanding Expenditure Issues (not included in either Outlook)



- *Potential Need to Replace Funding for Public Liability Fund Reserve*
 - Mayor-elect Filner proposes to fund an additional \$21.6 million in public safety expenditures from the Public Liability Fund
 - This would necessitate increased annual contributions to the Fund of approximately \$3.6 million in each year of the Mayor's Outlook in order to meet the Fund's reserve target by FY 2019

Other Outstanding Expenditure Issues (not included in either Outlook)



- *Restoration of Service Levels*
 - The Mayor’s Outlook assumes current service levels for operating departments with the exception of the Storm Water Division, which will face new regulatory requirements
 - Significant service reductions have taken place in recent years during budget cutbacks (i.e. in 2001 recreation centers were open 62 hours per week compared to current service levels of 45 hours per week)
 - Mayor and Council have recently restored several detrimental reductions by eliminating Fire engine “brown-outs” and restoring some library and recreation center hours

Other Outstanding Expenditure Issues (not included in either Outlook)



- *Additional Impacts of Redevelopment Dissolution*
 - Our Revised Outlook only includes the potential impacts of the California DOF continuing to deny the inclusion of Petco Park and Convention Center Phase II payments in the City's ROPS 3
 - Other ROPS 3 items have also been denied by the DOF, which could impact the General Fund, but this has not been determined as of yet

Other Outstanding Expenditure Issues (not included in either Outlook)



- *Restoration of 6 Percent Salary Reductions*
 - Last year in the IBA Revised Outlook, we included a scenario to begin to restore the City's 6% salary and benefit reduction
 - This scenario included 2% general salary increases in both FY 2015 and FY 2017. Each 2% adds an additional ongoing \$11.1 million
 - We did not include this in our Revised Outlook in consideration of Proposition B; however, there may be a desire for considering these costs in order to address retention and morale issues

Other Outstanding Cost Saving Issues (not included in either Outlook)



- *Managed Competition*

- Completed processes for publishing, street sweeping, fleet maintenance, and streets and sidewalks are estimated to save the General Fund \$4.5 million annually
- Storm water, Utilities customer service, traffic engineering, CIP delivery, and solid waste collection are in various stages of this process
- Several of the Preliminary Statements of Work (PSOWs) are being prepared for Rules Committee and Council consideration following the holiday recess
- Cost savings estimates are difficult to project for future competitions, but could help offset future expenditures

Conclusion



- Our Outlook shows the potential for significant deficits as illustrated in the following chart:

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Sub-Total Discretionary Adjustments	\$ (41.6)	\$ (37.2)	\$ (32.3)	\$ (34.1)	\$ (38.1)
Revised Outlook - "Baseline" + Non-Discretionary + Discretionary	\$ (78.6)	\$ (74.8)	\$ (44.7)	\$ (16.9)	\$ 11.5
Sub-Total Revenue Sensitivity Analysis	\$ (5.6)	\$ (19.2)	\$ (31.1)	\$ (44.6)	\$ (54.6)
Revised Outlook: "Baseline" + Non-Discretionary + Discretionary + Revenue Sensitivity	\$ (84.2)	\$ (94.0)	\$ (75.8)	\$ (61.5)	\$ (43.1)

Conclusion



- These Revised Outlook projections reflect the estimated financial impacts of a number of uncertainties facing the City that could significantly impact the Mayor's Financial Outlook
- Given these fiscal challenges and the uncertainty of the economy, it is important to remain fiscally cautious and committed to the “Structural Budget Deficit Principles” adopted by Council in February of 2010