OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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Review of Five-Year Financial Outlook and Budget Balancing Scenarios

Introduction

In November 2008 the Mayor released an updated version of the Five-Year Financial Outlook for Fiscal Years 2010-2014. Building on the FY 2009 budget, the Outlook lays out a picture of the City's financial landscape. General Fund revenue and expenditure projections provide a foundation for the Outlook, and are based largely on historical trends, the economic outlook, and certain committed department expenditures. In addition, the Outlook continues to address the Mayor's Eight Significant Areas.

Overall, the Five-Year Financial Outlook presents a sobering view of the City's financial situation, with significant General Fund deficits projected for each of the next five years. Solving these deficits will require substantial and timely corrective action. While we commend the Mayor for providing an Outlook that identifies projected deficits facing the City over the next several years, such an Outlook should be the basis for a comprehensive, multi-year plan for financial mitigation. In that vein, this report breaks from our review in prior years by providing several scenarios by which the projected budget deficits may be balanced.

This report begins with a review of the Five-Year Outlook baseline revenue and expenditure projections. Several revisions are then made to the baseline in order to arrive at a more accurate and consistent deficit projection. A number of potential corrective actions are then discussed for consideration in addressing the projected shortfalls. Finally, we present the budget balancing scenarios to illustrate the types of corrective actions that may need to be employed to resolve deficits of such significant magnitude.

General Fund Revenue

The Five-Year Financial Outlook projects General Fund revenue to increase by $130.5 million over the forecast period, from a revised $1.14 billion estimated in FY 2009 to $1.27 billion in FY 2014. The majority of this growth is driven by the City's four major General Fund revenues, property tax, sales tax, transient occupancy tax, and franchise fees. While these revenues account for approximately 68% of total General Fund revenue, they account for over 84% of the total revenue growth over the five-year period. The table below summarizes the projections and growth rates for total General Fund revenue and the major revenues.

General Fund Revenue Projections, in Millions

	FY08[1]	FY09[2]	FY10	FY11	FY12	FY13	FY14
General Fund	$ 1,091.7	$ 1,144.5	$ 1,139.6	$ 1,166.8	$ 1,200.8	$ 1,238.1	$ 1,275.0
% Growth	*3.60%*	*4.84%*	*-0.43%*	*2.39%*	*2.92%*	*3.11%*	*2.98%*
Major Revenues	$ 760.7	$ 763.2	$ 773.8	$ 792.4	$ 815.7	$ 844.4	$ 873.1
% Growth	*3.92%*	*0.34%*	*1.38%*	*2.41%*	*2.94%*	*3.51%*	*3.40%*

1. Unaudited actual
2. Year-end projected

Major General Fund Revenues

Overall, the Five-Year Outlook employs generally conservative growth assumptions for the major revenues, consistent with the current economic climate. Growth rates for the major revenues were lowered in the FY 2009 budget to reflect the weakening economy, and were lowered again more significantly (in some cases going negative) in the revised first quarter projections as economic conditions deteriorated more rapidly and actual receipts came in lower than expected. The Five-Year Outlook incorporates these declines by using the revised FY 2009 projections as the baseline from which future growth is applied.

As reflected in the table above, aggregate growth for the major revenues is projected to bottom out in the current fiscal year, and then slowly recover beginning in FY 2010. For the most part, growth projections are the most conservative in the early years of the Outlook, and then become slightly more aggressive toward the outlying years as economic conditions are projected to improve. However, not all of the major revenue growth rates move in tandem. Property tax, the largest General Fund revenue source, is projected to maintain weak growth through FY 2012, before slowly beginning to recover in FY 2013. While the Outlook assumes that the housing market will begin to rebound toward the end of calendar year 2009, the long lag time between market activity and the receipt of property tax revenues is expected to result in several more years of tepid growth.

In contrast, sales tax revenue is projected to decline significantly in the current fiscal year, hold steady in FY 2010, and then begin to recover more rapidly in the years following. This makes certain sense: consumer spending tends to react more quickly to changing economic conditions, and therefore would be expected to recover as the economy recovered. The sales tax projection assumes that the economy will begin to recover toward the end of calendar year 2009. While generally conservative, the projection has a few notable downside risks. First, if job losses and credit market constraints continue well into 2009, then sales tax revenue may continue to decline in FY 2010 instead of stabilizing. Secondly, even once the economic recovery begins, consumers may increase spending more modestly than in the past, resulting in a more gradual increase in sales tax growth.

Transient occupancy tax (TOT), with arguably the most optimistic growth scenario of all the major revenues, is projected to resume moderate growth of 4% in FY 2010 after a year-end estimated decline of nearly 2% in FY 2009. While TOT has experienced exceptional growth over the last several years, reaching annual growth rates of greater than 12% at its peak, we are concerned that the growth projections in the Five-Year Outlook may be overly aggressive, particularly in the early years of the forecast period. According to San Diego Convention and Visitors Bureau Quarterly Travel Forecast, released in December 2008, both hotel room demand and the average daily room rate are projected to decline significantly throughout calendar year 2009, which are likely to have a negative impact on TOT revenue in FY 2010. While TOT revenue weathered the previous economic downturn, and rebounded quickly from the slowdown in travel following the September 11, 2001 attacks, we feel that the consumer-led nature of the current recession may warrant lower growth projections in the near term.

Franchise fees, which consists of franchise revenue from SDG&E, Cox and Time-Warner Cable, and refuse hauler franchise fees, are generally the major revenue source least affected by economic fluctuations. The Five-Year Outlook projects franchise fees to grow by a combined rate of around 5.4% annually. While growth in franchise revenue has fluctuated greatly in the last several years, growth over the last 10 years has averaged greater than 7.4% per year, making the Outlook projections well in line with historical trends.

Other General Fund Revenues

Aside from the four major General Fund revenues, the Outlook includes projections for revenue sources such as property transfer tax, safety sales tax, and vehicle license fees; as well as for other broad revenue categories including Licenses & Permits; Fines, Forfeitures and Penalties; Revenue from Money & Property; Revenue from Other Agencies; Charges for Current Services and Transfers from Other Funds. Projections for these revenues, which account for less than 15% of total revenue growth over the five year period, were largely based on historical trends. We note the following with regard to these other General Fund revenues:

- Property transfer tax is projected to remain flat in FY 2010 following two years of significant declines, before slowly beginning to recover in FY 2011. Property transfer tax does not have the same lag time as property tax, and thus is expected to rebound more rapidly as the housing market begins to recover.

- Interest earnings are projected to increase significantly over the forecast period, from $4.5 million in FY 2010 to $12.2 million in FY 2014. This is due to an increase in expected earnings on the investment pool from a low of 2.1% in FY 2010 to 5.0% in FY 2013-14. The investment pool is assumed to grow at the same rate of General Fund revenue growth.

- The one-cent of discretionary TOT revenue from the TOT Fund is assumed to be transferred to the General Fund in each year of the Outlook. In the FY 2009 budget, an additional $7.5 million was allocated from the TOT Fund for promotion-related expenditures within the General Fund. The Outlook assumes that these allocations will be maintained as part of the baseline projections. Furthermore, the Outlook employs additional TOT allocations for General Fund promotion-related expenditures as a corrective action. These transfers will be discussed in greater detail in the section on Special Promotional Programs.

- In the FY 2009 budget, $11.7 million was transferred to the General Fund from the Environmental Growth Fund (EGF) to fund park maintenance. The Five-Year Outlook assumes that this transfer will continue and increase by 5% annually, consistent with the projected growth of SDG&E franchise fees**.** However, the IBA has recently noted that the EGF has become overcommitted so it is unclear if General Fund reimbursements can continue, and increase in later years, as the Outlook currently projects.

Sensitivity Analysis

A new element in the Five-Year Outlook is the inclusion of a sensitivity analysis for property tax, sales tax and TOT, in which a low and high growth scenario is presented in addition to the base scenario used in the Outlook. This analysis illustrates how different assumptions regarding the economic outlook and revenue growth could impact the Outlook, and we commend the Mayor and the Financial Management Department for including this type of analysis. The table below demonstrates the range of outcomes and significant financial impact that may be realized based on economic factors.

General Fund Revenue Projections, In Millions

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
Baseline Projection	$ 1,139.6	$ 1,166.8	$ 1,200.8	$ 1,238.1	$ 1,275.0
Low Growth Scenario	$ 1,127.6	$ 1,139.9	$ 1,158.8	$ 1,180.7	$ 1,205.6
Change from Base	*$ (12.0)*	*$ (26.9)*	*$ (42.0)*	*$ (57.4)*	*$ (69.4)*
High Growth Scenario	$ 1,153.6	$ 1,187.7	$ 1,228.6	$ 1,275.2	$ 1,323.4
Change from Base	*$ 14.0*	*$ 20.9*	*$ 27.8*	*$ 37.1*	*$ 48.4*

Overall, the baseline General Fund revenue projections provide a reasonable foundation for the Five-Year Financial Outlook. The growth assumptions are generally conservative and in line with current economic conditions. While we feel that the growth projection for TOT may be overly optimistic in the early years of the Outlook, we hesitate to recommend a lower growth forecast as any negative variance may be offset by positive variances in other major revenues, such as property tax. It should be emphasized that General Fund revenue projections are highly dynamic, and should be subject to frequent revision as new economic data and actual revenue receipts become available.

General Fund Expenditures

In this section, we review and provide comments on the baseline assumptions for the various expenditure categories as discussed in the Five-Year Outlook.

The table below reflects annual percentage changes for each expenditure category. The shaded years reflect the term of the Outlook period, while prior years reflect previous adopted budgets. The figures in the table are further described in the sections that follow.

Annual Percentage Change by General Fund Expenditure Category

Fiscal Year	Salaries and Wages	Fringe Benefits	Supplies & Services	Information Technology	Energy/ Utilities	Equipment Outlay	Total
2006	1.71%	22.37%	-0.52%	4.16%	0.23%	-22.86%	5.81%
2007	10.17%	6.05%	60.74%	50.25%	44.41%	12.42%	18.05%
2008	0.67%	7.41%	29.45%	25.03%	-0.16%	-26.15%	8.35%
2009	8.52%	4.54%	11.79%	-1.02%	7.80%	-8.84%	7.81%
2010	0.11%	2.90%	1.95%	11.47%	4.88%	3.99%	1.72%
2011	0.22%	11.23%	1.41%	2.20%	5.17%	2.94%	3.37%
2012	0.11%	4.15%	2.08%	1.67%	4.92%	2.86%	1.83%
2013	0.13%	4.19%	1.97%	0.70%	5.00%	2.78%	1.82%
2014	-0.06%	4.25%	2.06%	0.93%	5.06%	2.70%	1.82%

Salaries and Wages
The Five-Year Outlook maintains the assumption that no new salary increases are projected for City employees throughout the FY 2010-2014 time period. The Outlook also identifies as a significant risk to the projections, the potential for additional costs associated with salary increases reached via the collective bargaining process. In total, it is estimated that if City employees (represented by a labor union) received a 1% salary increase of their FY 2009 salary, this would add $6.2 million annually to the projections.

On July 1, 2008, both sworn police officers and firefighters received a general salary increase of 3%. Furthermore, on September 1, 2008, firefighters received an additional 2% salary increase and police officers received an additional 3% effective December 27, 2008. The annualization of these salary increases is accounted for in the projections.

As depicted in the above table, the Outlook projects minimal increases in the category; however, these changes are a reflection of the decrease in the vacancy factor for future fiscal years. The most significant change in the vacancy factor for the General Fund is the reduction in police academy attendance to 25 recruits as proposed and approved in the FY 2009 first-quarter budget amendments. The Outlook assumes this action will be carried through FY 2014. The IBA has previously expressed concerns about the significant impact this may have on recruitment and retention in the Police Department and Council sought confirmation that this action was a "temporary" solution and should be reinstated for FY 2011 and beyond. Conversely, although a similar action occurred for fire academies, there is no discussion in the Outlook on how this action will impact vacancy factor in future fiscal years.

Fringe Benefits
This expenditure category includes costs to provide employee benefits. A significant portion of the expenses in this category are fixed, including those costs for pension, OPEB/retiree health, and workers compensation. As depicted in the table on page 5, the largest projected percentage change is anticipated to occur in FY 2011. This is attributed to the anticipated increase in pension costs. The following highlights our comments on specific components in the Fringe Benefits category.

<u>Flexible Benefits</u>
The Outlook projects no increases to the flexible benefit amount allocated to employees. In May 2008, the City's consultant (Buck Consultants) provided an actuarial analysis on OPEB/retiree health costs. As part of their assumptions, they included a Health Care Cost and Expense Trend to incorporate projected inflation in health care, anticipated changes in health care utilization or delivery patterns, advances in technology, and changes in the health status of plan participants. The trend rates utilized in the analysis begin at 9% in FY 2010 and reduce by 0.5% each year thereafter.

The Outlook does not discuss why the projections are not consistent with the actuarial analysis. If it is assumed that costs will increase, but the City does not increase these expenses, it could be interpreted to mean that these cost increases in health care will be borne by the employee. Whether the City will pick up this increase or pass these increases onto the employee will be part of the collective bargaining process.

Although the IBA does not recommend a revision to the baseline assumptions for Flexible Benefits, the IBA does recommend that this be identified as a risk to the projections. The following chart calculates the flexible benefit costs, if the assumptions used for retiree health are applied:

Flexible Benefits	**FY 2010 Forecast**	**FY 2011 Forecast**	**FY 2012 Forecast**	**FY 2013 Forecast**	**FY 2014 Forecast**
Percent	9.0%	8.5%	8.0%	7.5%	7.0%
General Fund	$ 43.7	$ 47.5	$ 51.3	$ 55.1	$ 59.0
Annual Increase	$ 3.6	$ 3.7	$ 3.8	$ 3.8	$ 3.9

Retiree Health

As described in the Outlook, the OPEB (Other Post Employment Benefit) payment comprises a pay-as-you-go (PAYGO) portion (for employees already retired), and a pre-funding portion (for the future payment of benefits being accrued now). The PAYGO portion is projected using information from the report produced for the City by Buck Consultants showing the annual payments for retiree health that year. Mayoral staff used the percentage growth in those payments, applied to the FY 2009 budget for PAYGO.

For the pre-funding portion, the IBA would note a significant change in policy from the Mayor's prior Outlooks. The Mayor's first Outlook proposed to pay the ARC in full for OPEB starting in 2010. The current Outlook foregoes the original proposal to pay the ARC beginning in FY 2010 and into the future. Instead, the pre-funding portion grows at the same rate as the PAYGO portion. However, it does not appear that the increase in pre-funding is enough to achieve payment of the full OPEB ARC during the Outlook time horizon. The chart below breaks the OPEB payment shown in the Outlook into PAYGO and pre-funding portions.

OPEB Payment	**FY 2009 Budget**	**FY 2010 Forecast**	**FY 2011 Forecast**	**FY 2012 Forecast**	**FY 2013 Forecast**	**FY 2014 Forecast**
Rate of Growth	N/A	14.2%	13.0%	12.2%	11.5%	11.5%
PAYGO	$ 23.9	$ 27.3	$ 30.8	$ 34.6	$ 38.6	$ 43.0
Pre-Funding	$ 26.1	$ 29.8	$ 33.7	$ 37.8	$ 42.1	$ 47.0
Total Citywide	**$ 50.0**	**$ 57.1**	**$ 64.5**	**$ 72.4**	**$ 80.7**	**$ 90.0**

This is a significant shift in Mayoral policy; yet because payment of the full OPEB ARC is not legally required and with the large projected deficit in each year, the IBA agrees that payment of the full ARC, in the near-term, may not be the most urgent use of scarce City funds. We continue to note that the City's efforts at pre-funding are ambitious and in-line with comments made by industry analysts and professional organizations.

Funding for Terminal Leave

This expense item, referred to as funding of "Deferred Retirement Option Plan (DROP) participant leave balances" in the Outlook, represents the cost for annual leave that an employee has accrued and must be paid upon their departure from the City. Terminal leave reflects this "pay out" for all forms of departure, including termination, resignation, retirement, and/or retirement of DROP participants.

Past practice had departments absorbing this expense when it occurred. However, as projected in the 2008 Outlook, the General Fund budgeted $3.2 million for this expense in FY 2009. In the 2008 Outlook, the IBA questioned the acceleration of these costs in future fiscal years, as summarized in the following table. The 2009 Outlook projects significantly lower calculations (see following table), which the IBA supports.

Terminal Leave	FY 2009 Forecast	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
2008-2013 Outlook	$ 5.6	$ 11.0	$ 11.4	$ 13.0	$ 13.0	$ -
2009-2014 Outlook	$ -	$ 5.0	$ 5.3	$ 6.1	$ 7.6	$ 7.6
Increase/(Decrease)	*n/a*	*$ (6.0)*	*$ (6.1)*	*$ (6.9)*	*$ (5.4)*	*n/a*

The Outlook's outlying numbers in this area still seem high, but additional experience will provide more insight. The IBA also questions how the current and future economy will impact the number of retirees and whether those individuals who were previously anticipating to retire in the upcoming years may hold off on this decision until the economy stabilizes.

Supplies and Services

The revised Outlook maintains the annual inflationary growth of 2.0% for the Supplies and Services expenditure category, in addition to changes related to departmental expenditures. As shown in the chart on page 5, past budgets have reflected annual increases in this category well in excess of this amount.

For FY 2008, $248.9 million was expended in the Supplies and Services category, and $291.4 million was initially budgeted for 2009. Recent increases in Supplies and Services are attributable to the Mayor's Eight Significant Areas, including allocations made for reserve purposes, funding increases for Storm Water programs, and deferred maintenance and street repair. For the forecast period of the Outlook, increased requirements for reserves are accounted for separately and are in addition to the amounts and percentage increases reflected in the summary table. Supplies and Services total $298.4 million for FY 2010 in the Outlook.

Many of the committed/departmental expenditures detailed in the revised Outlook would affect the Supplies and Services expenditure category, including $4 million in new funding for the ERP project, $2.3 million related to the New Mission Bay charter change, and $1.2 million associated with Property Tax Administration and $2.1 million for bookings fees, both of which are payments to the County of San Diego.

Information Technology
Information Technology costs include data processing, network, hardware, and software costs. The annual inflationary growth rate has been reduced to 1.0% from the prior Outlook's 4.0%. Recent past budgets reflect significant increases each year, in excess of the annual increases which have been included in the Outlook, as shown in the chart on page 5. General Fund IT expenditures for Fiscal Year 2008 totaled $35.2 million. Committed expenditures for FY 2010 include additional funds of $1.9 million required by the Office of the CIO to replace fund balance used last year, as a cost saving measure. This addition does not entirely explain the sharp growth of $4.2 million in FY 2010, which amounts to an 11.5% increase over the prior year.

Energy/Utilities
The Energy/Utilities expenditure category of the Outlook maintains the annual inflationary growth of 5%. FY 2008 actual expenditures in the area totaled $26.7 million for the General Fund, and the FY 2009 budget for Energy totals $27.6 million. Previously contributing to large year-to-year increases in the prior Outlook was additional funding for increased fuel costs in the amount of $1.365 million in each year of the five year period. The effect of changing fuel costs impacts the City's Equipment Division, which typically factors these impacts into the motive equipment usage rates charged to its customer departments. It is possible that recently reduced gasoline rates were factored in here, resulting in annual savings in the revised Outlook, though that is not specifically described.

Equipment Outlay
The revised Outlook maintains the annual inflation growth of 3.0% for equipment outlay, in addition to increased costs for departmental expenditures, as in previous Outlook versions. Recent past budgets have reflected large reductions from year-to-year in this category. The previous Outlook showed a significant increase of 17% for equipment in FY 2009 attributable to funds to be budgeted for compliance with emissions regulations of the California Air Resources Board, totaling $1.35 million. However, the final adopted budget for FY 2009 totals $9.86 million in this category, which helps to clarify the lower level of equipment funding shown in the revised Outlook for 2010 and beyond.

These recent changes result in an annual savings to the forecast of over $3 million. Further scrutiny in this area may be warranted, given that actual expenditures in this category totaled just $6.8 million for FY 2008. We have raised questions about this level of equipment outlay funding in prior reports, including the First Quarter 2009 report based on actual expenditures. As previously discussed, purchases in this area should be one-time in nature, and are not necessarily required each year.

Equipment Outlay	FY 2009 Forecast	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
2008-2013 Outlook	$ 12.6	$ 13.2	$ 13.7	$ 14.3	$ 14.4	$ -
2009-2014 Outlook	$ -	$ 10.2	$ 10.5	$ 10.8	$ 11.1	$ 11.4
Increase/(Decrease)	*n/a*	*$ (3.0)*	*$ (3.2)*	*$ (3.5)*	*$ (3.3)*	*n/a*

General Fund Reserve
The City's Reserve Policy calls for General Fund reserves to reach 6.5% of the total General Fund budget for FY 2009, increasing to 8% by FY 2012. The reserve calculation includes the Emergency Reserve, the Appropriated Reserve, and the Unappropriated Reserve.

According to the First Quarter Report prepared by Financial Management in November 2008, "based on current revenue projections and the City Reserve Policy (O-19679), the 6.5% reserve goal for FY 2009 is $74.3 million. The current estimated combined reserves balance, including the Appropriated and Emergency Reserves, is $74.6 million which exceeds the reserve goal for this fiscal year." Because of this, the FY 2009 budgeted contribution to the reserve of $3.7 million was considered to no longer be needed, and was eliminated as part of the Council-approved budget amendments as a cost-saving measure. Based on the CFO's methodology for determining the reserves, it will not be known until the end of FY 2009 whether the goal of 6.5% can be achieved without this contribution.

When comparing the revised Outlook to its predecessor, it is clear that the estimated total size of the General Fund has been reduced, primarily due to lower expectations related to major revenues because of economic conditions. This also results in lower reserve requirements, which are determined as a percentage of General Fund revenues. Based on the projected General Fund revenues and annual reserve policy goals, the amounts reflected in the revised Outlook will ensure that the City meets the targets outlined in the reserve policy, and will achieve the 8% General Fund reserve by FY 2012 based on current methodology.

It is important to also consider that increases to the General Fund, which may occur during budget development each year, will also trigger corresponding reserve increases, if reserve policy goals are to be maintained.

Workers' Compensation Reserve
The City's Reserve Policy establishes a goal of increasing funding the Workers' Compensation Reserve to reach 50% of outstanding claims by FY 2014. This funding is in addition to funds needed to pay annual claims and administrative costs. As stated in the Outlook, it is planned that the Mayor's Proposed Budget for FY 2010 will include no

contribution to the Workers' Compensation Reserve, with annual contributions of $4.1 million in FY 2011 and annually thereafter. Assuming the City's current level of claims is $161 million, the reserve target of 15% for FY 2009 would require a total of $24.2 million be maintained on hand.

The revised Outlook states that the Workers' Compensation reserve may reach $35 million, due to lower claims payments and the release of encumbrances. This is well in excess of the current reserve goal. While it may appear that excess funds could be utilized for other purposes, the escalating reserve requirement would necessitate funding be returned in the next few years, and there may be no prospect of identifying additional available revenues. However, if the City were to experience serious financial or other difficulties in the short-term, consideration could be given to access this overfunded source.

Assuming the City contributes only $4.1 million to the reserve each year, it would take until FY 2020 to reach the reserve goal of 50% of outstanding claims (or $80 million). At present, the City's reserve policy states that this goal should be achieved in FY 2014.

Public Liability Reserve

The City's Reserve Policy establishes an increasing goal of funding the Public Liability Reserve to reach 50% of outstanding claims by FY 2014. As stated in the Outlook, it is planned that the annual contributions of $5 million will be made to the Public Liability Reserve, beginning in FY 2010 and through the forecast period. This reflects a reduction from a $10 million annual contribution in the previous Outlook. Assuming the City's current level of claims is $114 million, the reserve target of 15% for FY 2009 would require $11.4 million be maintained on hand. Currently $10 million is reserved for this purpose. Assuming the City contributes only $5 million each year, it would take until FY 2019 to reach the reserve goal of 50% of outstanding claims (or $57 million), well beyond the current policy goal of FY 2014.

Deferred Maintenance

The Five-Year Financial Outlook proposes to continue the use of a combination of funding mechanisms to chip away at the City's estimated $800-$900 million in deferred maintenance/capital improvement needs (excluding Water and Wastewater). These funding mechanisms include Proposition 1B funding, land sales, and bond financing. The following table outlines the proposed funding for deferred maintenance through FY 2014:

Funding Source	FY 2009 Budget	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast	Total by Source
Proposition 1B	$ 21.2	$ 20.0	$ -	$ -	$ -	$ -	**$ 41.2**
Land Sales	$ 6.8	$ 11.8	$ -	$ -	$ -	$ -	**$ 18.6**
Bond Funding	$ 102.3	$ -	$ 102.3	$ -	$ 102.3	$ -	**$ 306.9**
Total by Fiscal Year	***$ 130.3***	***$ 31.8***	***$ 102.3***	***$ -***	***$ 102.3***	***$ -***	***$ 366.7***

As the chart above details, the significant funding source to address the City's deferred maintenance needs is from the issuance of multiple bond financings. The total expected proceeds from the three bond financings is $306.9 million. Debt service payments related to the bond financings will come from the City's General Fund. The following table details the estimated annual debt service payments for each of the anticipated Deferred Maintenance bond financings.

Deferred Maintenance Debt Service Payments	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
FY 2009 Issuance	$ 3.6	$ 3.6	$ 3.6	$ 3.6	$ 3.6
FY 2011 Issuance	$ -	$ -	$ 3.6	$ 3.6	$ 3.6
FY 2013 Issuance	$ -	$ -	$ -	$ -	$ 3.6
Total Annual Payment	***$ 3.6***	***$ 3.6***	***$ 7.2***	***$ 7.2***	***$ 10.8***

Storm Water

Storm Water Permit compliance continues to be one of the Mayor's Eight Significant Areas. Over the past several years, funding for storm water compliance activities has increased significantly, from approximately $12.9 million in FY 2006 to $48.8 million in FY 2009. Much of this increase has resulted from new regulations under the Municipal Storm Water Permit, which was revised and updated in January 2007.

In FY 2009, various storm water-related activities were consolidated into a single department, including storm water pollution prevention, street sweeping and storm drain infrastructure. The table below shows how funding has increased for each of these components over the last several years.

Activity	FY 2006 Budget	FY 2007 Budget	FY 2008 Budget	FY 2009 Budget
Storm Water	$ 2.7	$ 13.6	$ 23.0	$ 24.6
Street Sweeping	$ 3.1	$ 3.7	$ 5.8	$ 4.1
Storm Drains	$ 7.1	$ 7.1	$ 14.2	$ 20.1
TOTAL	**$ 12.9**	**$ 24.4**	**$ 43.0**	**$ 48.8**

The current Five-Year Outlook assumes flat funding for the Storm Water Department over the next five years. This represents a significant policy shift from the funding plans included in previous versions of the Outlook. In the previous Outlook, it was assumed that funding for Storm Water compliance would reach approximately $61 million by FY 2010, and hold flat thereafter.

In addition, it should be noted that the Storm Water Department was subject to nearly $5.7 million in budget reductions in the FY 2009 First Quarter Adjustment. As these reductions are assumed to be carried forward throughout the Five-Year Outlook, total funding for the Storm Water Department is projected to be $43.1 million per year.

Despite these reductions in funding, the Storm Water Department has indicated that the City will remain in compliance with the Municipal Storm Water Permit. However, storm water funding should continue to be closely monitored, as any future reductions may jeopardize the City's compliance with the Municipal Permit.

FY 2009 First Quarter Corrective Actions

Financial Management presented its FY 2009 Budget Amendment Report to a joint special meeting of the Budget and Finance Committee and the City Council Committee of the Whole on November 12, 2008. This report was intended as a first quarter financial review, including recommendations for budget changes to bring General Fund expenditures in line with reduced revenues, and was provided concurrently with the Five-Year Outlook.

The Budget Amendment Report recommended budget adjustments totaling $40.9 million to both revenues and expenditures, with major General Fund revenues reduced by $43.5 million. These reductions included the elimination of over 200 positions, and major service impacts, including the closure of seven branch libraries, the closure of nine recreation centers and one gymnasium, a rolling service reduction of one fire engine or truck company per day, and reductions to the number and/or size of the police and fire recruit academies.

Following public hearings and the receipt of additional information regarding potential options and alternatives to the reduction proposals, the City Council approved the vast majority (90%) of the Mayor's recommended reductions, totaling a net reduction to the General Fund of $36.9 million. Revisions to the proposal included the identification of funding to allow all branch libraries, recreation centers and fire stations to remain open and staffed as previously planned through the end of the current fiscal year, at a cost of approximately $4 million.

As the Council changes to the Mayor's proposal occurred following the release of the Outlook, it is not expected that the Outlook would reflect these revisions. The Outlook reflects an annual adjustment of $34.5 million in FY 2010 through 2014 as a result of the budget amendments (as originally proposed) during FY 2009. Because of these adjustments, it is important to note that the service impacts that were proposed are projected to continue for the term of the Outlook, including closures of city library and recreation facilities, and reduced fire staffing and reduced number and/or size of police and fire academies through FY 2014, although policy direction was given to restore funding for fire staffing in FY 2010 and police academies by FY 2011.

Revisions to Outlook Baseline

This section highlights the IBA's recommended changes to the baseline revenue and expenditure projections in the Five-Year Outlook. In this context, the term "baseline" refers to any underlying revenue or expenditure projection that is used to develop the overall General Fund surplus or deficit outlook. In other words, the baseline represents a starting point, from which future corrective actions and other policy decisions will be considered.

Pension Contribution

Since the publication of the Outlook, the June 30, 2008 valuation for the City's retirement plan has been published. While it was presented at the December meeting, it has not yet been adopted by the SDCERS Board. They are slated to take action on this item at their January meeting.

In the valuation, the actuary has calculated the annual required contribution (ARC) of $154 million for the City of San Diego in FY 2010, $12 million less than anticipated in the Outlook. The IBA has made this correction in our base case, with the General Fund share of the ARC projected at $120.9 million, or 78.5% of the total ARC (consistent with the Outlook).

For future years, the Outlook presented two possible scenarios for the City's ARC payments. However, the IBA has elected to show just one pension scenario in order to highlight potential outcomes of other variables in our analysis. This scenario will use the median of the two Outlook scenarios, which were developed by the SDCERS actuary and represent a broad range of potential outcomes based on discussions with Mayoral staff. The IBA's scenario is shown in the table below:

Baseline Pension Payment	FY 2009 Budget	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Citywide ARC	$ 161.7	$ 154.0	$ 217.5	$ 231.5	$ 245.6	$ 257.4
General Fund ARC	$ 126.9	$ 120.9	$ 170.7	$ 181.7	$ 192.8	$ 202.1

The difference between the pension scenarios in the Five-Year Outlook and the payments used in the IBA baseline are illustrated below:

Pension Payment - General Fund	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	$ 130.3	$ 156.2	$ 162.5	$ 169.0	$ 175.7
IBA	$ 120.9	$ 170.7	$ 181.7	$ 192.8	$ 202.1
Difference	*$ (9.4)*	*$ 14.5*	*$ 19.2*	*$ 23.8*	*$ 26.4*

New Funding for ERP

Included in the Outlook's committed expenditures for FY 2010 is $4 million identified as a new requirement for the ERP system (also known as OneSD, the City's Enterprise Resource Planning comprehensive computer upgrade project). In reports to the City Council in January and April 2007, annual costs related to the purchase, implementation and financing for the ERP Core project were outlined through 2016. The January 2007 report stated that the ongoing fiscal requirements for the ERP system will be offset through the elimination of the legacy systems and through efficiencies that will be gained through business process reengineering and by adopting best practices, and both reports mentioned that costs had already been included in the Five-Year Outlook. Based on this, the justification for an additional $4 million for FY 2010 is unclear and presumptuous.

The IBA opts to remove this new $4 million requirement from the baseline scenario, as any increased funding needs for this project are a policy decision deserving City Council review and approval, which has not yet occurred and should not be assumed. Many changes have taken place over the past several months related to the ERP project, both in terms of City leadership and consultant support, which may result in delays to the project schedule and/or revisions to its scope. The City Council should be provided a comprehensive update on these issues, and fiscal impacts, including possible additional funding needs, should be presented.

New Funding For ERP	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	$ 4.0	$ -	$ -	$ -	$ -
IBA	$ -	$ -	$ -	$ -	$ -
Difference	*$ (4.0)*	*$ -*	*$ -*	*$ -*	*$ -*

Special Promotion/TOT Transfer

The City of San Diego currently levies a transient occupancy tax (TOT) at a rate of 10.5 cents per dollar on the daily room rate charged by lodging facilities within the City. Of the 10.5 cent levy, 5.5 cents are deposited directly in the General Fund, and 5.0 cents are deposited in the TOT Fund and allocated via the Special Promotional Programs budget. Per the Municipal Code, of the 5 cents deposited in the TOT Fund, 4 cents are required to be used "solely for the purpose of promoting the City", while the remaining 1 cent may be used for discretionary purposes. Beginning in FY 2009, the full 1 cent of discretionary TOT has been transferred to the General Fund, and this approach has been assumed throughout the Five-Year Outlook.

Also in FY 2009, as part of the 4 cents required to be used for promotion, $7.5 million was allocated to the General Fund for certain "promotion-related" expenditures, including street and facility maintenance, and park programs, and certain police services. As part of the baseline revenue projections, the Five-Year Outlook assumes that this $7.5 million will continue to be allocated to the General Fund. Furthermore, the Outlook assumes that additional TOT funds will be allocated for other promotion-related expenditures in the General Fund as surplus TOT funding becomes available. While this measure has been identified as a potential corrective action, it is assumed in the baseline Outlook projections. All of the TOT transfers to the General Fund assumed in the Outlook are shown in table below.

5-Year Outlook TOT Transfers/Allocations	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
1 Cent Discretionary	$ 15.3	$ 16.1	$ 17.1	$ 18.1	$ 19.2
Existing Promo-Related	$ 7.5	$ 7.5	$ 7.5	$ 7.5	$ 7.5
Add'l Promo-Related*	$ 1.0	$ 6.6	$ 10.8	$ 16.8	$ 20.4
TOTAL	**$ 23.8**	**$ 30.2**	**$ 35.4**	**$ 42.4**	**$ 47.1**

** Identified in Outlook as a potential corrective action*

While we support continuing to transfer the 1 cent of discretionary TOT to the General Fund, we feel that continuing to allocate TOT funding for General Fund promotion-related expenditures, particularly at a sharply increasing rate, is a policy decision that should not be assumed in the baseline projections. This is reflected in the table below.

Total TOT Transfer to General Fund	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	$ 23.8	$ 30.2	$ 35.4	$ 42.4	$ 47.1
IBA	$ 15.3	$ 16.1	$ 17.1	$ 18.1	$ 19.2
Difference	*$ (8.5)*	*$ (14.1)*	*$ (18.3)*	*$ (24.3)*	*$ (27.9)*

While this will have the effect in increasing the baseline deficit, several options for the use of TOT promotion funds can still be considered as a corrective action. These options are discussed in greater detail in the Corrective Actions sections of this report.

New Facilities

The City has a multi-year Capital Improvement Program (CIP). As most capital projects span several years in order to plan, design, acquire property (when necessary) and construct, the CIP provides a preview of city facilities and improvements that are expected to be completed during the term of the Outlook. When complete, new city facilities often will require added resources for operations and maintenance. When additional resources are not available, the costs associated with new facilities often become a trade-off, requiring reduced service levels for existing facilities and/or programs.

Each year, City departments are asked to provide an estimate of operations and maintenance costs associated with new facilities to be completed. For the past two Outlooks, these estimates were included in the forecast to provide a realistic picture of known and expected costs on the horizon. In a change from past practice, these estimates were not included in the revised Outlook. The IBA reviewed departmental submittals and summarized the information about projected new facilities.

Beginning in FY 2010, costs associated with new facilities could require over $11.7 million, growing to $40.5 million in FY 2014. Project schedules in later years are certainly subject to change, and estimates for future years are dependent on project funding availability, and City Council approvals that may be needed during this time. However, for FY 2010, projects are under construction with firm completion dates, resulting in known increased costs if the facilities open as currently planned. By including this information, the IBA does not necessarily recommend that all capital projects continue and operate as estimated or planned. The City Council may desire to more fully discuss the implications of planned projects, and the options to delay, cancel, or change the scope of projects to mitigate budgetary impacts. The table below summarizes annual costs associated with new facilities. A detailed description of these planned new facilities is provided in Attachment 1.

Departmental New Facilities	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	$ -	$ -	$ -	$ -	$ -
IBA	$ 11.7	$ 20.2	$ 34.3	$ 37.4	$ 40.5
Difference	*$ 11.7*	*$ 20.2*	*$ 34.3*	*$ 37.4*	*$ 40.5*

Salary Increases

As discussed in the section on Salaries and Wages on page 6, the Five-Year Outlook maintains the assumption that no new salary increases will be given throughout the five year period. While the IBA does not believe that a baseline revision to account for potential future salary increases is appropriate or necessary, the outcome of labor negotiations in future years cannot be known with any certainty. Any new salary increases would impact baseline expenditure projections. As discussed in the Outlook, each 1% salary increase for classified employees is estimated to result in annual expenditure increases of approximately $6.2 million.

Summary of Revisions to Outlook Baseline

The tables below summarize the IBA's adjustments to the Five-Year Outlook's baseline revenue and expenditure projections.

Baseline Revenue Projections	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	$ 1,139.6	$ 1,166.8	$ 1,200.8	$ 1,238.1	$ 1,275.0
TOT Transfer	$ (8.5)	$ (14.1)	$ (18.3)	$ (24.3)	$ (27.9)
Revised Revenues	***$ 1,131.1***	***$ 1,152.7***	***$ 1,182.5***	***$ 1,213.8***	***$ 1,247.1***

Baseline Expenditure Projections	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	$ 1,183.5	$ 1,235.1	$ 1,258.9	$ 1,271.9	$ 1,295.6
Pension	$ (9.4)	$ 14.5	$ 19.2	$ 23.8	$ 26.4
ERP Maintenance	$ (4.0)	$ -	$ -	$ -	$ -
New Facilities	$ 11.7	$ 20.2	$ 34.3	$ 37.4	$ 40.5
Salary Increases*	tbd	tbd	tbd	tbd	tbd
Revised Expenditures	***$ 1,181.8***	***$ 1,269.8***	***$ 1,312.4***	***$ 1,333.1***	***$ 1,362.5***

PROJECTED DEFICIT	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	**$ (44.0)**	**$ (68.3)**	**$ (58.1)**	**$ (33.8)**	**$ (20.6)**
IBA Revised	**$ (50.7)**	**$ (117.1)**	**$ (129.9)**	**$ (119.3)**	**$ (115.4)**

** Each 1% salary increase for classified employees is equivalent to $6.2 million*

As these tables show, the IBA adjustments increase the projected deficits significantly in all years of the Outlook. However, we believe that these adjustments present a more accurate and consistent baseline against which budget balancing decisions must be made.

Corrective Actions

This section presents a number of potential corrective actions that may be considered as part of a comprehensive plan to address the projected future budget deficits. In general, the actions discussed in this section represent options that are commonly used by other cities, that may provide significant budgetary relief, and/or that may be quickly implemented. However, we wish to emphasize that while we have attempted to identify a broad range of potential actions, this section is not intended to be exhaustive or all-inclusive. Finally, it should be noted that all of these potential corrective actions may require further financial and legal analysis prior to implementation.

Service Reductions/Freeze New Facilities

In the Budget Balancing Scenarios shown in the next section, service reductions remain a necessary option in addressing the projected shortfalls, although they can be minimized significantly by carrying out a variety of other corrective actions. It is also important to note that all service reductions made in prior years remain throughout the entire period of the Outlook. Per the Outlook, the City will not be in a position to restore any prior service level cuts and will need to make further reductions in order to achieve a balanced budget. The Budget and Finance Committee has scheduled a series of community forums for the month of February to solicit input from residents on City services and priorities in advance of the FY 2010 budget process. Attachment II presents a preliminary listing of key City services that will be discussed and prioritized at these forums.

Before reducing current services, serious consideration should be given to whether it serves the community to continue to open new facilities at the same time that we are cutting existing services, an issue that we have raised in the past three budget cycles. As we indicated in the "New Facilities" section of this report, new park and recreation, fire and library facilities scheduled to come on line in FY 2010 add $11.7 million in new operating costs to the projected deficit. This number grows to $40 million over the Outlook period based on new projects currently in the planning stages, the capital costs of which are expected to be provided through donations, redevelopment funding, Developer Impact Fees, or Facilities Benefit Assessments. Options presented in this report include halting the construction of facilities just begun or those not started, as well as not staffing facilities which are complete or nearly complete. Consideration for changing construction and/or opening schedules of new facilities should be reviewed in conjunction with a comprehensive facility plan which the IBA recommended and the City Council requested be developed at the time of the FY 2009 first quarter financial report and budget amendments.

In a break from past practice, the projected costs for new facilities were not included in the Five-Year Outlook. To be consistent with prior versions of the Outlook, and to provide a more complete picture of future costs, we have incorporated these costs in to our baseline revisions. A policy decision to not open any new facilities over the period of the Outlook would result in the operating cost savings shown in the table below. For every new facility that moves forward, either reductions to existing services will need to take place or additional revenue will need to be raised.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Freeze Planned New Facilities	$ 11.7	$ 20.2	$ 34.3	$ 37.4	$ 40.5

Managed Competition

On November 7, 2006 San Diego voters approved Proposition C, which amended the City Charter to allow the contracting out of non-Public Safety services typically provided by Civil Service employees utilizing a "managed competition" method, which allows public employees to compete with the private sector to provide a given City service. On January 9, 2007 the City Council approved the Implementation Ordinance establishing the guidelines by which managed competition would be implemented and executed. The Mayor established an ambitious timeframe with the goal of issuing the first Request for Proposal for a managed competition process by summer 2007.

Since then Managed Competition efforts have been delayed by numerous issues and obstacles including a recent Public Employee Relations Board (PERB) ruling that the Managed Competition Guide, which had taken over a year to complete, must be met and conferred on with the City's unions. That process is currently underway, and it is uncertain when the managed competition process will be able to move forward.

Managed competition has been shown to be cost effective in certain service areas such as residential trash collection when guided by clear procedures and operating principles as well as strong monitoring and oversight. Cities such as Charlotte, Indianapolis and Phoenix have had long running programs and have experienced success with managed competition through the realization of cost savings and operating efficiencies, including City employees successfully competing for the service.

Employee Suggestions

In the Fall the Mayor called for City employees to submit ideas they had for addressing the City's budget challenges. Almost 400 employee suggestions were submitted for trimming department budgets or generating new revenues. City departments are currently in the process of analyzing these suggestions for their feasibility, potential for cost savings /revenue generation, and possible incorporation into the FY 2010 budget. The City Council may want to request that the Mayor share the original employee submissions to learn what City employees are thinking and to assist in generating other budget balancing ideas.

User Fee Increases

In IBA Report 08-20 "Need for Comprehensive Annual User Fee Review Process As Part of the Annual Budget" presented to the Budget and Finance Committee in February 2008, we discussed the need for the City to:

- Identify the full cost of service for activities that charge users fees
- Determine current cost recovery rates for these activities
- Develop "target" cost recovery policies
- Propose recommendations to Council for achieving these targets

In an April 15, 2008 memorandum to the Chair of the Budget and Finance Committee, the Mayor indicated that "a policy on cost-recovery for City fees will be developed and presented to the Budget and Finance Committee and City Council by the fall of 2008." In June 2008 the City Auditor completed a "User Fee Study: Best Practices, Methodologies and Guidelines" to provide Financial Management with best practices to facilitate efforts here in our City. Financial Management initiated a user fee review this summer which remains underway. No recommendations for user fee increases were included in the Mayor's Outlook although it was noted that "a policy would be coming to Council in January 2009 and upon its adoption, current user fees would be updated for Consumer Price Index (CPI) as well as cost recovery."

An estimated range of $2.0 million to $5.0 million in new revenues for the CPI alone was presented in the Outlook, however, no revenue increase was included in the corrective actions. The IBA Corrective Action has assumed a conservative $2.0 million revenue increase for FY 2010, increasing by 5% each year thereafter as shown in the table below. This represents an inflationary increase only and does not begin to address the issue of full cost recovery which is expected to be determined as part of the user fee study.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
User Fees	$ 2.0	$ 2.1	$ 2.2	$ 2.3	$ 2.4

Mandatory Furlough

Although not considered a long term solution for the City's structural budget deficit, a mandatory furlough could be considered to help close the anticipated General Fund budget deficit for FY 2010 and longer if needed. A furlough is a common strategy used by cities and states across the country due to its potential for significant savings. The implementation of a mandatory furlough would require meeting and conferring with the City's labor unions.

The following chart includes the possible savings options related to a mandatory one week or one day per month furlough. This information is based on actual expenditure activity and assumes that 75% of fringe benefits remain a fixed cost due to the Annual Required Contribution to the Retirement System and Retiree Health costs. The anticipated savings includes a reduction of $1.1 million that is related to General Fund employees already participating in the City's Voluntary Furlough Program in Fiscal Year 2009. The Five-Year Financial Outlook anticipates that the $1.1 million in savings from the Voluntary Furlough Program will continue in Fiscal Year 2010.

Mandatory Furlough Impacted Departments	One Week (40 hours)	One Day per Month (96 hours)
All General Fund Departments	$10.4 million	$24.9 million
All GF (Police & Fire Exempt)	$3.0 million	$7.3 million
All GF (Police, Fire, City Attorney, NCC, Refuse Collection, Street Exempt)	$2.0 million	$4.9 million*
Estimated Percent Employee Salary Reduction	1.92%	4.60%

** This option is reflected in the Budget Balancing Scenarios*

It is important to note that the estimated savings from a mandatory furlough could be less if additional staff reductions are made to balance the FY 2010 budget. In addition, the City's Labor Relations department has indicated that requiring unclassified employees to take a mandatory furlough could violate the Fair Labor Standards Act (FLSA). However, the City's unclassified employees could be required to take a salary reduction equal to that of the Classified personnel as a result of the furlough.

If the City of San Diego decided to implement a mandatory furlough for FY 2010, we would join many cities from across the nation that have implemented some form of a furlough in the last year. These cities include Sacramento, Chicago, Oakland, and Louisville. Jurisdictions that are currently considering a mandatory furlough include the cities of Denver and San Francisco, and the states of California and Maryland.

Although a mandatory furlough is a short term solution, the savings and operational impacts from the furlough could be analyzed over the fiscal year to determine if any long- term savings could result from a permanent change in operational hours or increased efficiencies. For example, the State of Utah is currently testing a four day work schedule that has resulted in savings and increased efficiencies. A December 2008 Governing Magazine article on alternative work schedules included the following initial results from Utah's four day work schedule:

> "The state already is seeing big results. Energy consumption is down, on track to meet Utah's prediction of $3 million in saving over the first year. Employee sick leave is down, now that workers have a built-in day for doctor appointments and other necessary errands. Absenteeism is down 6 percent from a year ago, which could translate into $13 million annually in productivity savings."

Other possible savings that could be achieved through a modified work week include fewer security and maintenance issues, and a reduction of information technology service calls. The table below shows the potential savings if a mandatory furlough is imposed over a two-year period.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Mandatory Furlough (1 day per month)*	$ 4.9	$ 4.9	$ -	$ -	$ -

** Police, Fire, City Attorney, NCC, Refuse Collection and Street Division exempt*

Consolidation of Debt Stabilization Reserves

The City has a longstanding internal practice to set aside funds or reserves for lease-revenue financings which are to be repaid by the General Fund (TOT). These set-aside funds are referred to as internal stabilization funds. The set-aside practice is equal to one-half of the annual debt service requirement on these financings. Approximately $17.8 million was set aside in FY 2009 and it is estimated that $15.7 million will be set aside in FY 2010. Funds are discretionarily budgeted annually and provide the General Fund a cushion in the event that TOT receipts are lower than expected. This practice currently applies to six outstanding City financings:

- Convention Center Expansion
- Petco Park Bonds
- Balboa Park/Mission Bay Improvements (1996A, 1996B, 2003)
- Old Town Trolley Extension
- Bayside Trolley Extension

Funding is appropriated annually for debt service payments on the TOT-backed lease-revenue financings. As with all City financings, the City is required to establish a debt service reserve fund (generally sized to equal maximum annual debt service). In the event that the City did not, or could not, make the annual appropriation for debt service, bondholders are assured that a debt service reserve fund has been established to cover a year of debt service. However, the City's internal stabilization funds are in addition to the debt service reserve fund. The City's internal stabilization funds are not pledged to repay the debt.

There are no bond documents requiring or referencing the City's practice to set aside internal stabilization reserves. The City does make the rating agencies aware of our internal fund set-aside practice for these lease-revenue financings. Rating agencies generally view this as a conservative and favorable practice; however, they understand that these are discretionary City funds that provide some insulation for TOT shortfalls without any requirement for debt service repayment.

These set-aside funds are not discussed or contemplated in the City's Reserve Policy, nor are they counted toward the City's reserve target of 6.5% for FY 2009. As a potential corrective action, these internal stabilization funds could be used to accelerate the policy objective of an 8% reserve for the City's General Fund. The City's Reserve Policy calls for General Fund reserves to grow from 6.5% in FY 2009 to 8% in FY 2012. The Outlook includes funding to meet the increasing reserve requirement each year and achieves the 8% goal by FY 2012, based on projected General Fund revenue.

Consolidating internal stabilization funds into the City's General Fund reserve would 1) bring the City's General Fund reserve to approximately 8% beginning in FY 2010 and 2) allow the City to save $17.8 million of planned contributions to the General Fund reserve from FY 2010 through FY 2012 as noted in the tables below.

FY09 Estimated GF Reserve	$ 74.6
Internal Stabilization Funds (ISF)	$ 17.8
Consolidated Reserves	**$ 92.4**

Consolidate ISF into General Fund Reserves	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook GF Revenue	$ 1,139.6	$ 1,166.8	$ 1,200.8	$ 1,238.1	$ 1,275.0
Reserve Including ISF	$ 92.4	$ 92.4	$ 96.1	$ 99.1	$ 102.0
Baseline Percentage	8.1%	7.9%	8.0%	8.0%	8.0%
Required Contribution	**$ -**	**$ -**	**$ 3.7**	**$ 3.0**	**$ 2.9**

Corrective Action - Reserve Contributions	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook Contribution	$ 5.2	$ 7.7	$ 8.6	$ 3.0	$ 3.0
Contribution w/ISF	$ -	$ -	$ 3.7	$ 3.0	$ 3.0
General Fund Savings	**$ 5.2**	**$ 7.7**	**$ 4.9**	**$ -**	**$ -**

It should be noted that total General Fund reserves, upon which the reserve percentage is calculated, include the Emergency Reserve, the Appropriated Reserve, and the Unappropriated Reserve.

Redevelopment Agency Revenue – Petco Park Debt Service

The FY 2009 Budget included $7.5 million in revenue from the Redevelopment Agency to support the $11.3 million annual debt service payment on the Petco Park bonds. The Outlook projects the current $7.5 million funding level to continue through FY 2012 and then increase to $10.0 million for FY 2013-2014.

The IBA had previously expressed questions on the mechanism and timing of this payment. Multiple scenarios were being explored, including whether this would be a repayment of outstanding loans by the Centre City project area or whether the Agency would make findings to mitigate the City's financial constraints and provide funding for the debt service.

On January 7, 2009 the Budget/Finance and Administration Committee of CCDC approved multiple actions impacting this item, including:

- Amending the Ballpark Cooperation Agreement and make certain findings relating to additional payments by the Agency to the City associated with debt service on bonds used to finance Petco Park. Payments of $11.3 annually would be made over a five-year period, beginning in FY 2009 through FY 2013.
- Approving a repayment agreement for the Centre City Redevelopment Project Area. Currently, the project area owes the City $116.3 million, primarily in Community Development Block Grant (CDBG) funds. The repayment agreement identifies annual payments of $10 million to commence in FY 2014 and continue for the first five years; increasing to $15 million in FY 2019; $20 million in FY 2020; and the final payment of $31.3 million in FY 2021.

Upon approval by the Agency and the City Council, these actions will differ from the scenario in the Outlook as illustrated below:

Redevelopment Debt Svc. Payment	FY 2009 Budget	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Outlook	$ 7.5	$ 7.5	$ 7.5	$ 7.5	$ 10.0	$ 10.0
IBA	$ 11.3	$ 11.3	$ 11.3	$ 11.3	$ 11.3	$ -
Difference	*$ 3.8*	*$ 3.8*	*$ 3.8*	*$ 3.8*	*$ 1.3*	*$ (10.0)*

Although the repayment of outstanding loans is scheduled to commence in FY 2014, these funds are restricted to CDBG eligible expenses and thus can not be used to pay the Petco Park Debt Service.

Transient Occupancy Tax Reallocation

As discussed in the section on Special Promotional Programs on page 15, the Municipal Code requires that 4 cents of the City's 10.5 cent TOT levy be used "solely for the purpose of promoting the City." In the FY 2009 Budget, this was equivalent to approximately $65.9 million. Of that amount, $7.5 million was used to fund "promotion-related" expenditures within the General Fund. As discussed in the aforementioned section, we feel that these General Fund "promotion-related" allocations should not be assumed in the baseline forecast until a broader policy decision regarding the use of TOT revenue is made. As a potential corrective action, there are two general options:

> Option 1: Amend the Municipal Code and Council Policy 100-03 to more clearly define the term "promotion". This definition could include current and/or future General Fund expenditures that have a nexus with promotion and tourism, such as beach and park maintenance, lifeguard and police services, etc.
>
> Option 2: Amend the Municipal Code and Council Policy 100-03 to reduce the amount of TOT that is required to be used for the purpose of promoting the City.

The table below shows the maximum potential benefit to the General Fund under either option, given existing TOT allocations and commitments. It should be noted that this assumes no new or additional allocations are made, such as for Arts & Culture.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
TOT Reallocation	$ 9.2	$ 11.8	$ 18.6	$ 22.1	$ 18.3

Lease City Box Suites

The Mayor issued a memo to the Council on January 12, 2009 indicating that in preparation for the FY 2010 budget he plans to bring forward options to maximize revenues including the potential sale or lease of the City's stadium guest boxes. This is a revenue generating option that the Mayor considered but did not propose as part of the FY 2009 first-quarter budget adjustments. Preliminary estimates show that this action could generate $500,000 annually to the General Fund.

Sales Tax Increase

The City may impose a sales tax increase, subject to voter approval. State Senate Bill 566 (2003), outlines the following requirements:

- The tax must be imposed at a rate of 0.25%, or a multiple thereof,
- The governing body must approve proposing the tax by a 2/3 majority,

- General purpose taxes must be approved by a majority (50% + 1) vote,
- Specific taxes must be approved by a 2/3 vote and
- An increase may not exceed 2%, which includes any supplemental tax that the county previously imposed

The table below shows a breakdown of the current statewide sales tax rate of 7.25 percent:

Rate	Jurisdiction
5.00%	State (General Fund)
0.25%	State (Fiscal Recovery Fund)
0.50%	State (Local Revenue Fund)
0.50%	State (Local Public Safety Fund)
1.00%	Local (County/City) 0.25% County Transportation 0.75% City Operations
7.25%	**Total Statewide Sales Tax**

In addition to the statewide rate, San Diego County currently collects a half-cent sales tax, which is used towards financing the transportation improvement program, TransNet. Because this half-cent increase counts against the 2% maximum that is allowed, the City would be able to impose a supplemental sales tax up to 1.5 cents.

In November 2008, the City of El Cajon passed Proposition J, a ballot measure that raised sales tax by a half-cent in order to preserve funding for general city services within the city. The passage of Proposition J increased El Cajon's tax rate to 8.75% and the revenue was used for general use purposes. A majority (50% + 1) vote was necessary and it received 51.77% of the vote.

The next scheduled ballot election is June 2010 and if a sales tax proposal was placed at that time and approved by voters, the revenue would start being generated in Fiscal Year 2011. Based on the revenue projections in the Five-Year Outlook, the table below reflects the potential additional revenue that could be generated if the City implemented a 0.25% sales tax increase:

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Sales Tax Increase (0.25%)	$ -	$ 55.5	$ 58.0	$ 60.6	$ 63.0

Transient Occupancy Tax Increase
The City of San Diego levies a transient occupancy tax (TOT) on the daily room rate charged by lodging facilities within the city. The City's TOT rate is currently 10.5%, and

is projected to generate $156.9 million in FY 2009. Council Policy 100-03 stipulates that the City's TOT rate shall not be greater than the average rate of 15 major cities as specified in the Policy. The average rate among these cities (discarding the highest and lowest rate per Council Policy instruction) is approximately 13.5%. Increasing the TOT rate would require majority voter approval. Based on the revenue projection in the Five-Year Outlook, the table below shows the potential additional revenue that could be generated if the TOT rate were increased from 10.5% to 11.5%.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
TOT Increase (1%)	$ -	$ 16.3	$ 17.3	$ 18.3	$ 19.4

Utility User Tax

The utility users tax (UUT) is a tax imposed on the consumption of public utilities. A UUT can be imposed on the consumption of electricity, gas, cable television, water or telephone. Almost all major cities in California charge taxes on electricity and natural gas consumption. A report from the Center on Policy Initiatives in 2005 entitled "The Bottom Line" showed that the average UUT for the cities of Los Angeles, San Jose, San Francisco, Sacramento and Oakland is approximately $111 per capita annually.

Although a UUT is considered to be a regressive tax in that lower income residents are forced to pay a larger portion of their income, it is a tax that is widely used by large California cities and can generate a significant amount of revenue for General Fund services. If the City were to levy a UUT over various utilities that equated to $15 per capita annually, it would generate approximately $20.2 million a year for General Fund services.

A UUT would require majority voter approval (50% + 1) and the next regularly scheduled election is not until June 2010. The table below reflects the additional $20.2 million (based on City population of 1,348,000 and a UUT equal to approximately $15 per capita annually) beginning in FY 2011 and assumes rapid implementation.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Utility User Tax	$ -	$ 20.2	$ 20.2	$ 20.2	$ 20.2

Parking Tax

A Parking Tax is levied on the gross receipts from all financial transactions involving the parking or storing of automobiles or other motor vehicles in outdoor or indoor parking lots and garages. Parking facility operators are responsible for issuing the claim check to the operator of the vehicle, collecting the tax and then remitting the revenue to the city. According to a 2005 Manager's Report, a Parking Tax is considered a Business Tax and is thus treated as a General Tax, which means that implementing this levy requires a simple majority vote (50% + 1).

The city of Los Angeles currently charges a 10% tax on each parking transaction and in Fiscal Year 2009 this tax was projected to raise nearly $94.5 million in General Fund revenue. The next scheduled ballot election is June 2010 and if a Parking Tax proposal was placed at that time and approved by voters, the revenue would start being generated in Fiscal Year 2011. Based on a 2005 City Manager's Report, a 10% Parking Tax would generate $19.6 million in additional General Fund revenue for the City of San Diego:

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Parking Tax (10%)	$ -	$ 19.6	$ 19.6	$ 19.6	$ 19.6

Property Transfer Tax Increase

Property transfer tax is levied on the sale price of any real property that is sold or transferred. The City of San Diego levies a tax rate of $0.55 per $1,000 of sale price. In conformance with State law, this rate is credited against the County's rate of $1.10 per $1,000, for a total charge of $1.10 per $1,000. Under this "conforming" tax rate, both the city and the county receive $0.55 per $1,000 of the sale price. Some cities levy a "non-conforming" property transfer tax at a rate above $0.55 per $1,000. In these cases, the county receives the full share of the $1.10 per $1,000, and the city receives the amount generated from its own tax rate. Several major California cities levy non-conforming property transfer tax rates that are significantly higher than that levied by San Diego, including Oakland ($15 per $1,000), Los Angeles ($4.50 per $1,000) and San Jose ($3.00 per $1,000). Increasing the Property Transfer Tax rate would require majority voter approval. Based on the revenue projection in the Five-Year Outlook, the table below shows the potential revenue from a $1 increase in the property transfer tax.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Property Transfer Tax Increase ($1)	$ -	$ 12.2	$ 12.4	$ 12.8	$ 13.2

Business License Tax Increase

Business license taxes (BLT) are charged to businesses for the privilege of conducting operations within a city's boundaries. These taxes are levied in many different ways, most commonly as a percentage of gross receipts or a fixed charge per employee. Often, rates are tiered depending on the size of the business or number of employees. Different rates are often charged to different types of businesses.

The City of San Diego currently levies an annual BLT of $34 for small businesses (12 or fewer employees). Larger businesses (13 or more employees) pay $125 plus $5 for every employee annually. Additionally, the City charges a processing fee of $25 for each new business applicant and $15 per business for annual renewals of the BLT. This BLT structure yields approximately $11 million annually for the City's General Fund.

Although the City has the third-highest gross receipts from businesses in California, we receive comparatively little BLT revenue as compared with other cities in the state. A report from the Center on Policy Initiatives in 2005 entitled “The Bottom Line” indicated that San Diego’s businesses pay the lowest business license fees, in proportion to gross business receipts, of the ten largest cities in the state. Comparative data compiled by the Office of the City Treasurer for FY 2007 (below) shows average tax revenue (including business rental tax receipts) received for each business license issued:

City	# of Bus.Licenses	Total Revenue	Ave. Revenue per Bus. License
San Francisco	93,576	$279 million	$2,983
Los Angeles	285,000	$365 million	$1,281
Oakland	65,000	$ 50 million	$ 774
Sacramento	22,000	$ 5 million	$ 227
San Jose	60,000	$ 14 million	$ 225
San Diego	**135,000**	**$ 11 million**	**$ 81**

If the City were to double their BLT it would generate approximately $11 million a year for General Fund services. As a BLT increase would require majority voter approval (50% + 1) and the next regularly scheduled election is not until June 2010, the table below reflects the additional $11 million (based on simply doubling the BLT structure that is in place for small, large and rental businesses) beginning in FY 2011. If approved by the voters, a new tax structure could be quickly implemented.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Business License Tax Increase	$ -	$ 11.0	$ 11.0	$ 11.0	$ 11.0

Storm Water Fee

Over the past several years, the General Fund budget for storm water pollution prevention and storm drain infrastructure has grown significantly, from $12.9 million in FY 2006 to $48.8 million in FY 2009. Much of this increase has resulted from new regulations under the Municipal Storm Water Permit. Currently, the City charges a monthly storm drain fee of $0.95 for single-family residences, and $0.0647 per hundred cubic feet for commercial properties. In FY 2009, the storm drain fee is projected to generate roughly $6 million, of which $5 million is allocated to the Storm Water Department. In the past, the IBA has advocated for a dedicated source of funding for Storm Water Permit compliance, and the Storm Water Department has been researching various options. As discussed in the Storm Water section on page 12, the Five-Year Outlook assumes that funding for the Storm Water Department will be held flat at $43.1 million per year. A storm drain fee could be structured to recover all or part of these costs not currently funded by the existing storm drain fee. Recent court rulings have held that storm drain fees are subject to the voter approval requirements under Proposition 218. The table below reflects the potential benefit to the General Fund of a full cost recovery storm water fee, based on the expenditure projection in the Five-Year Outlook.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Storm Water Fee	$ -	$ 38.1	$ 38.1	$ 38.1	$ 38.1

Refuse Collection Fee
The People's Ordinance, approved by voters in 1919, prohibits the City from imposing a fee or charge for residential refuse collection. As a result, San Diego is the only major California city that does not recover at least a portion of its refuse collection expenses, leaving the General Fund to bear the full burden of funding trash collection services. In FY 2009, $37.1 million was budgeted for residential refuse collection services; however, this likely understates the true cost as it does not account for legal, financial, and other citywide administrative support expenses. If the City implemented a refuse collection fee to recover the full cost of providing residential refuse collection services, the total benefit to the General Fund could be as high as $40 million. Based on an estimated 315,000 residential and small business customers, $40 million would translate into a monthly fee of approximately $10.60.

State law specifically exempts refuse collection fees from voter approval requirements, but instead requires that any implemented or increased fees follow a Proposition 218 notification process, much like increases in water and sewer rates. However, majority voter approval would be needed to amend the People's Ordinance before any refuse collection fee could be implemented in San Diego. A refuse collection fee could be structured to recover all or a portion of the cost of providing refuse collection services. The table below reflects potential full cost recovery from a refuse collection fee.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast*	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Refuse Collection Fee	$ -	$ 20.0	$ 40.0	$ 40.0	$ 40.0

** Assumes only half-year due to required Prop. 218 notification process*

Refuse Hauler Franchise Fees
The City currently levies franchise fees from refuse haulers at a rate of $11/ton for Class I haulers (those hauling less than 75,000 tons per year), and $12/ton for Tier II haulers (75,000 tons or more per year). As discussed in the Five-Year Outlook, a $2/ton increase in the refuse hauler franchise fee would generate approximately $1.5 million per year in additional General Fund revenue. It should be noted that since refuse hauler franchise fees are collected quarterly in arrears, any increase would need to be approved by April 1, 2009 in order to generate the full amount of additional revenue for FY 2010. The table below shows the potential additional revenue from a $2/ton increase in the refuse hauler franchise fee if it were fully implemented for FY 2010.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Refuse Hauler Franchise Fee Increase ($2/ton)	$ 1.5	$ 1.5	$ 1.5	$ 1.5	$ 1.5

General Obligation Bonds/Property Tax

General obligation bonds are typically issued to finance government improvements benefiting the community as a whole. These bonds are secured by the taxing authority of the issuer. The issuer pledges to levy the necessary taxes (typically ad valorem property taxes) on all assessable property within its jurisdiction to provide the timely repayment of debt. Due to the strength of this security pledge, general obligation bonds typically provide issuers with the lowest borrowing costs, typically do not require funding a reserve fund, and are readily accepted by investors in the municipal marketplace.

Deferred maintenance projects that involve the replacement of major systems or building components can be financed with general obligation bonds; however, ongoing maintenance of public facilities cannot be financed with general obligation bonds.

General obligation bonds require two-thirds voter approval, which can be difficult to achieve. Because of this, cities in California have chosen to look at other financing methods to fund their needs. A December 31, 2008 Los Angeles Times article on municipal debt pointed out that “of the more than 10,000 bonds and other debt vehicles issued between 1998 and 2007, fewer than 700 went to a public vote, according to the state treasurer’s office.” However, the article also pointed out the that “nontraditional debt vehicles cost more over the long run because they are considered riskier than general-obligation bonds, which governments stand fully behind. Investors therefore demand higher interest rates.”

A well thought-out process can lead to the passage of a General Obligation Bond measure in the San Diego region. For their successful 2008 bond measure, the San Diego Unified School District (SDUSD) created an ad hoc task force composed of a wide range of external and internal stakeholders. Over a four month time period the task force met multiple times to review the district’s Long-Range Facilities Master Plan, tour school facilities, and met with community members via the schools clusters groups to obtain feedback and discuss needs in each area. From the various Task Force meetings, values and principles were identified as important factors to consider when deciding where and how bond proceeds should be allocated. From these values and principles, four themes were developed that formed the foundation of their work.

The values, principles, and themes developed by the task force enabled the SDUSD to educate the electorate on how their proceeds would be used and the ultimate benefit to students and the overall community. Another important outcome from the overall process was the development of a comprehensive list of projects by facility that the bond proceeds would fund. This list was made available to the community for review on the district's website.

If the City of San Diego chose to move forward with putting a General Obligation Bond on the ballot and it was approved by the voters, a significant benefit would be the ability to have a dedicated funding source available to address the City's $800 - $900 million Deferred Maintenance backlog. The Mayor's Deferred Maintenance Plan uses a combination of funding sources that totals $367 million over five years. However, even with the $367 million in projected revenue, the City will still need to identify an additional funding source for the $400 - $500 million shortfall. In addition, the use of Lease Revenue Bonds will require the City to pay the debt service for the three bond offerings from the General Fund. With significant deficits projected in FY 2011 – 2014, the City would need to reduce service levels or find other revenue sources to fund the debt service for additional Lease Revenue bonds. Funding for a General Obligation Bond would come from additional Property Tax assessments to the City of San Diego property owners, resulting in no impact to the General Fund.

The benefit of a General Obligation Bond to the region could be substantial, especially as an economic stimulus in a down economy. In addition, as the SDUSD put an emphasis on modernizing school facilities to meet 21st century curriculum, a General Obligation Bond could be used to fuel the growth of green technology in the San Diego region. This could include partnering with local firms to incorporate new technology in City facilities that are being rehabilitated. A November 6, 2008 Forbes Magazine article states that the "green economy could soon become the nation's fastest-growing job segment, accounting for roughly 10 percent of new jobs over the next 20 years." In addition, the article identified San Diego as one of the "hottest" places for Green Jobs in the U.S.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Lease-Revenue Bond*	$ -	$ -	$ 7.2	$ 7.2	$ 10.8
G.O. Bond**	$ -	$ -	$ 3.6	$ 3.6	$ 3.6
Savings to General Fund	*$ -*	*$ -*	*$ 3.6*	*$ 3.6*	*$ 7.2*

**The Five-Year Outlook includes $3.6 million in debt service payments for FY 2010 and 2011 for the 2009 Lease Revenue Bonds in the baseline expenditure projections.*

***Assumes placement of a General Obligation Bond on the November 2010 Ballot backed by a supplemental property tax rate.*

Facility Use Fee

A facility use fee, or admissions tax, could be levied on events for which admission is charged, such as sporting events or concerts. Revenue from this fee would be used to partially offset the cost of parking, traffic and law enforcement, as well as facility maintenance. This tax is generally based on either a flat rate per ticket, a percentage of the admission price, or on a sliding scale. Cities may also impose these taxes on specific events or more broadly. For example, in the City of Pasadena, an admissions tax is implemented only to Rose Bowl events while the City of Santa Cruz charges an admissions fee to all events within city limits.

The City should caution against a broader implementation of this tax, as First Amendment issues have been raised by the City Attorney's Office. According to a September 21, 1992 Memorandum of Law, an admission tax may violate the First Amendment if it falls disproportionately on businesses engaged in free or protected speech, such as movie theaters. A more narrow application would be to levy a facility use fee on admission to events in Qualcomm Stadium, PETCO Park and the San Diego Sports Arena.

It is unclear whether implementation of a facility use fee requires voter approval. Assuming that it does and a proposal was placed on the June 2010 ballot, revenue would begin to be generated in FY 2011, as shown in the table below. Based on a 2003 report by the City Manager it is estimated that a 5% facility use fee would generate approximately $4.9 million.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Facility Use Fee	$ -	$ 4.9	$ 4.9	$ 4.9	$ 4.9

911 Surcharge

IBA Report 07-36 considered a 911 fee to help support the City's emergency response and dispatch system. In 2006 an assumed $3.00 monthly fee added to land lines was estimated to generate approximately $16 million annually. Since the release of this report, a California state appeals court ruled in a Union City case that a city needs two-thirds voter approval before charging phone customers a monthly fee for accessing the 911 system. According to the court's decision, a 911 fee imposed by elected officials amounted to a special tax that requires voter approval. Following this decision, Santa Cruz County and the City of Watsonville placed a 911 surcharge on the November 2008 ballot. Santa Cruz Measure T proposed a monthly tax of $3.49 per land and cellular line. Watsonville Measure C proposed a $2.05 per line per month. Both measures failed.

Also, in November 2008 the City of San Francisco passed Proposition O, which replaced the Emergency Response Fee with an Access Line Tax with a low-income user exemption. The replacement tax maintains the previous $2.75 per month per phone line tax. This tax generates approximately $42 million annually and the new tax is expected to generate the same amount of general fund revenue. Additionally, this proposition also updates the San Francisco's telephone users tax, which at 7.5% of the cost of services billed, exempting residential customers, generated approximately $40 million annually. This tax is aimed specifically to new and future technologies, such as non-residential voice over internet protocol.

In February 2008, the City of Ventura revised its 911 fee and offered its residents two options: a monthly $1.49 per phone line fee or pay a per-call fee of $17.88, which is equal to the annualized cost of the monthly fee. Additionally, each household signed up for the per-call option would get a free first call and would be allowed to enroll in the monthly plan in lieu of paying the one-time $17.88 charge. The table below shows the potential revenue that could be generated with a $3 monthly fee on land lines.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
911 Surcharge	$ 16.0	$ 16.0	$ 16.0	$ 16.0	$ 16.0

Pension Reform

Continued pension reform may be an avenue to yield further savings. While the City established a new retirement plan for new employees beginning July 1, 2009, additional plans that reduce benefits further for future employees can be established if it is the desire of the Mayor and City Council and after collective bargaining. The IBA continues to recommend that any revision to employee benefits be considered in light of the whole compensation package, to include salary & wages, health care, retirement and other ancillary benefits.

There have been some efforts, although unsuccessful to-date, to reduce the benefits of current City employees as well, which could yield large savings, depending on the scale of reduction and type of benefits reduced (i.e. DROP, Purchase of Service Credits, Retiree Health, the Preservation of Benefits Plan, etc.).

Pension Obligation Bonds (POBs) are another option to pursue potential savings for the City. Savings could only be achieved if the rate on the bonds was lower than that being paid on the City's UAAL. The City has capacity for debt such as this and it may be worth exploring. However, POBs can be more complex than the standard debt issuance and the IBA would recommend thorough research on contemporary issues surrounding POBs. If the City Council is interested in pursuing this alternative, we recommend convening a team comprised of staff from Debt Management, the City Attorney's Office, and the IBA, to explore options.

The IBA also notes that these and other efforts surrounding the issue of pension could result in direct savings to the City, and may also build the confidence necessary for the citizenry to consider revenue options such as those discussed in this report. As we have stated, eliminating the structural budget deficit must be done through a multi-pronged approach and likely cannot be effectively achieved through cost cutting or service reductions alone. Savings discussed in this section are unquantifiable at this time due to the varied options presented.

Summary of Potential Corrective Actions
The table below provides a summary of the potential corrective actions that have been identified in this section.

Potential Corrective Action	FY 2010 Forecast	FY 2011 Forecast	FY 2012 Forecast	FY 2013 Forecast	FY 2014 Forecast
Service Reductions	tbd	tbd	tbd	tbd	tbd
Employee Suggestions	tbd	tbd	tbd	tbd	tbd
Managed Competition	tbd	tbd	tbd	tbd	tbd
Freeze New Planned Facilities	$ 11.7	$ 20.2	$ 34.3	$ 37.4	$ 40.5
User Fee Increases	2.0	2.1	2.2	2.3	2.4
Mandatory Furlough	4.9	4.9	-	-	-
Lease City Box Suites	0.4	0.4	0.4	0.4	0.4
Internal Stabilization Funds	5.2	7.7	4.9	-	-
Redevelopment Debt Service	3.8	3.8	3.8	1.3	-
TOT Reallocation	9.2	11.8	18.6	22.1	18.3
Major Revenue Increases	-	192.9	216.6	220.6	224.5
Sales Tax	-	*55.5*	*58.0*	*60.6*	*63.0*
TOT	-	*16.3*	*17.3*	*18.3*	*19.4*
Utility User Tax	-	*20.2*	*20.2*	*20.2*	*20.2*
Parking Tax	-	*19.6*	*19.6*	*19.6*	*19.6*
Property Transfer Tax	-	*12.2*	*12.4*	*12.8*	*13.2*
Business License Tax	-	*11.0*	*11.0*	*11.0*	*11.0*
Storm Drain Fee	-	*38.1*	*38.1*	*38.1*	*38.1*
Refuse Collection Fee	-	*20.0*	*40.0*	*40.0*	*40.0*
Other Revenue Increases	1.5	22.4	26.0	26.0	29.6
Refuse Hauler Franchise Fee	*1.5*	*1.5*	*1.5*	*1.5*	*1.5*
G.O. Bond for Deferred Maint.	-	-	*3.6*	*3.6*	*7.2*
Facility Use Fee	-	*4.9*	*4.9*	*4.9*	*4.9*
911 Surcharge	-	*16.0*	*16.0*	*16.0*	*16.0*
TOTAL CORRECTIVE ACTIONS	**$ 38.7**	**$ 266.2**	**$ 306.8**	**$ 310.1**	**$ 315.7**

Budget Balancing Scenarios

This section presents several scenarios that illustrate ways in which the corrective actions described in the previous section could be employed as part of a comprehensive budget balancing solution. The goal in developing these scenarios was to present potential solutions for balancing the FY 2010 and FY 2011 shortfalls. As such, our choice of corrective actions was dictated somewhat by the options that are immediately available, particularly for FY 2010. For example, it is assumed that any revenue options which require voter approval will not be available until FY 2011 at the earliest, following the next regularly scheduled election in June 2010. However, we wish to emphasize that these scenarios do not constitute an endorsement of any particular corrective action; they have been constructed simply to illustrate the types of corrective actions that may need to be employed to resolve shortfalls of this magnitude.

Scenario 1

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
Adjusted Deficit	**(50.7)**	**(117.1)**	**(129.9)**	**(119.3)**	**(115.4)**
Corrective Actions - Scenario 1					
Service Reductions - FY 2010	11.9	11.9	11.9	11.9	11.9
Service Reductions - FY 2011	-	14.6	14.6	14.6	14.6
Freeze Planned New Facilities	11.7	20.2	34.3	37.4	40.5
User Fees	2.0	2.1	2.2	2.3	2.4
Mandatory Furlough	4.9	4.9	-	-	-
Redevelop. Loan Repayment	3.8	3.8	3.8	1.3	-
TOT Reallocation	9.2	11.8	18.6	22.1	18.3
Lease City Box Suites	0.5	0.5	0.5	0.5	0.5
Refuse Hauler Franchise Fee	1.5	1.5	1.5	1.5	1.5
Consolidate Debt Reserves	5.2	7.7	4.9	-	-
Storm Water Fee	-	38.1	38.1	38.1	38.1
Managed Competition	tbd	tbd	tbd	tbd	tbd
Employee Suggestions	tbd	tbd	tbd	tbd	tbd
Subtotal Corrective Actions	***50.7***	***117.1***	***130.4***	***129.7***	***127.8***
Remaining Surplus/(Deficit)	**-**	**-**	**0.5**	**10.4**	**12.4**

This scenario employs a mixture of service reductions, a freeze of planned new facilities, minor revenue enhancements, and other actions in order to balance the projected FY 2010 deficit. Further service reductions, as well as the implementation of the full-cost recovery storm water fee are employed in FY 2011. Construction of new facilities is assumed to be frozen throughout the five year period. It should be noted that all service reductions are assumed to carry forward in all future years.

Scenario 2

Adjusted Deficit	**(50.7)**	**(117.1)**	**(129.9)**	**(119.3)**	**(115.4)**
Corrective Actions - Scenario 2					
Service Reductions - FY 2010	23.6	23.6	23.6	23.6	23.6
Service Reductions - FY 2011	-	3.1	3.1	3.1	3.1
User Fees	2.0	2.1	2.2	2.3	2.4
Mandatory Furlough	4.9	4.9	-	-	-
Redevelop. Loan Repayment	3.8	3.8	3.8	1.3	-
TOT Reallocation	9.2	11.8	18.6	22.1	18.3
Lease City Box Suites	0.5	0.5	0.5	0.5	0.5
Refuse Hauler Franchise Fee	1.5	1.5	1.5	1.5	1.5
Consolidate Debt Reserves	5.2	7.7	4.9	-	-
Storm Water Fee	-	38.1	38.1	38.1	38.1
Refuse Collection Fee	-	20.0	40.0	40.0	40.0
Managed Competition	tbd	tbd	tbd	tbd	tbd
Employee Suggestions	tbd	tbd	tbd	tbd	tbd
Subtotal Corrective Actions	***50.7***	***117.1***	***136.3***	***132.5***	***127.5***
Remaining Surplus/(Deficit)	**-**	**-**	**6.4**	**13.2**	**12.1**

Under this scenario, construction and operation of all new facilities is assumed to proceed as planned. As a result, more significant service reductions are needed to balance the projected deficit in FY 2010. Even with these greater service reductions carrying through to future years, both a full-cost recovery storm drain fee and refuse collection fee are needed to balance FY 2011.

Scenario 3

Adjusted Deficit	**(50.7)**	**(117.1)**	**(129.9)**	**(119.3)**	**(115.4)**
Corrective Actions - Scenario 3					
Service Reductions - FY 2010	11.9	11.9	11.9	11.9	11.9
Service Reductions - FY 2011	-	52.7	52.7	52.7	52.7
Freeze Planned New Facilities	11.7	20.2	34.3	37.4	40.5
User Fees	2.0	2.1	2.2	2.3	2.4
Mandatory Furlough	4.9	4.9	-	-	-
Redevelop. Loan Repayment	3.8	3.8	3.8	1.3	-
TOT Reallocation	9.2	11.8	18.6	22.1	18.3
Lease City Box Suites	0.5	0.5	0.5	0.5	0.5
Refuse Hauler Franchise Fee	1.5	1.5	1.5	1.5	1.5
Consolidate Debt Reserves	5.2	7.7	4.9	-	-
Managed Competition	tbd	tbd	tbd	tbd	tbd
Employee Suggestions	tbd	tbd	tbd	tbd	tbd
Subtotal Corrective Actions	***50.7***	***117.1***	***130.4***	***129.7***	***127.8***
Remaining Surplus/(Deficit)	**-**	**-**	**0.5**	**10.4**	**12.4**

This scenario assumes no major revenue increases over the five year period. While the magnitude of the service reductions needed to balance FY 2010 are the same as in Scenario 1, significantly greater services reductions are be needed in FY 2011. In addition, all planned new facilities are frozen.

Conclusion

The Mayor's Five-Year Financial Outlook for FY 2010-2014 presents a sobering view of the City's financial situation, projecting significant General Fund deficits in each of the next five years. The IBA has reviewed the Five-Year Outlook, and in a break from our review in prior years, we implement a series of revisions to the baseline revenue and expenditure projections. While these revisions result in significant increases to the projected deficits in all years of the outlook, we feel that they present a more accurate and consistent baseline against which budget balancing decisions must be made.

Looking forward, solving these projected deficits will require substantial and timely corrective action. This report aims to assist in the development of a comprehensive, multi-year plan for financial mitigation by identifying a number of potential corrective actions, and presenting various scenarios for how these corrective actions may be used to address the future budgetary shortfalls. While the budget balancing scenarios presented in this report are merely hypothetical examples, and the corrective actions are by no means intended to be comprehensive, it is our hope that this report will provide some perspective on the seriousness of the situation, and the significant steps that will need to be taken to restore long-term financial health for the City of San Diego.

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Attachment I: Details on Planned New City Facilities 2010-2014
Attachment II: Prioritizing City Services