THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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

OVERVIEW

On November 6, 2019, Mayor Faulconer released the Fiscal Year 2021-2025 Five-Year Financial Outlook (Outlook), one of the City's annual financial planning tools. The Outlook is an integral part of the budget development process and is described in the City's Budget Policy as "the basis for determining the coming year's operating budget allocations."

The City's Budget Policy states that the Outlook "shall… include projections for committed expenditures which are defined as the operational costs for new facilities, contractual obligations, federal and State legal mandates, and adopted City Council policies." This year's Outlook includes General Fund Baseline revenue and expenditure projections as well as future critical expenditures identified by the Mayor, in conformance with the Budget Policy.

This year's Outlook projects a Baseline deficit in the first year of the Outlook period, followed by four years of surpluses. After taking into account the cost of the Mayor's Critical Strategic Expenditures, which are above and beyond the Baseline, the Outlook projects deficits in the first four years followed by one year of surplus. For FY 2021, the Outlook's projected deficit (after including Critical Strategic Expenditures) is $83.7 million, as reflected in the table below.

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

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In this report, we review the information presented in the Outlook as well as additional items identified by our Office, including:

- An overview of Baseline revenues and expenditures reported in the Outlook,
- A recession scenario showing the potential impacts on City revenue projections,
- An analysis of Critical Strategic Expenditures included in the Outlook,
- A review of potential future funding needs not included in the Outlook,
- A discussion of future financial challenges, and
- A discussion of potential mitigation measures to address shortfalls.

The Outlook and our Office's review of the Outlook are tools that the City Council can use to consider alternative expenditure priorities for the FY 2021 budget, as well as deficit mitigation strategies. Council may also wish to consider including alternative priorities or deficit mitigation strategies in their City Council Budget Priorities memoranda due to our Office in January 2020.

REVIEW OF BASELINE GENERAL FUND REVENUES

Major General Fund Revenues

The Outlook forecasts growth in General Fund revenues for each of the next five years; however, at a lower rate than the growth of recent years. The table below summarizes the projections from the Outlook, as well as the growth rates applied to the four largest revenue sources. Property tax, sales tax, Transient Occupancy Tax (TOT) and franchise fees make up over 72% of the General Fund's revenues in FY 2020.

Baseline General Fund Revenues (in millions)							
	FY 2019 Unaudited Actual[1]	**FY 2020 Projection[2]**	**FY 2021 Forecast**	**FY 2022 Forecast**	**FY 2023 Forecast**	**FY 2024 Forecast**	**FY 2025 Forecast**
Property Tax	$ 570.6	$ 604.7	$ 636.1	$ 666.5	$ 696.7	$ 726.6	$ 755.9
Property Tax Growth Rate		*5.25%*	*5.00%*	*4.75%*	*4.50%*	*4.25%*	*4.00%*
Sales Tax	304.4	300.6	311.1	321.1	331.0	340.9	350.8
Sales Tax Growth Rate		*3.9%*	*3.4%*	*3.2%*	*3.1%*	*3.0%*	*2.9%*
Transient Occupancy Tax	131.9	136.6	141.8	146.9	152.2	157.6	163.1
TOT Growth Rate		*3.0%*	*3.8%*	*3.6%*	*3.6%*	*3.6%*	*3.5%*
Franchise Fees[3]	78.9	79.8	82.0	83.9	85.8	87.5	89.3
SDG&E Electricity Growth Rate		*4.3%*	*3.9%*	*3.9%*	*3.9%*	*3.2%*	*3.2%*
Cable Growth Rate		*-2.0%*	*-2.5%*	*-2.8%*	*-2.8%*	*-2.8%*	*-2.2%*
Cannabis Business Tax	8.2	17.0	19.7	22.8	24.5	26.6	29.7
Other Revenues, incl departmental	397.6	410.5	405.0	413.9	423.1	424.3	430.5
Total General Fund Revenue	**$ 1,491.6**	**$ 1,549.2**	**$ 1,595.7**	**$ 1,655.1**	**$ 1,713.3**	**$ 1,763.5**	**$ 1,819.3**
Increase over Prior Year		***$ 57.6***	***$ 46.5***	***$ 59.4***	***$ 58.2***	***$ 50.2***	***$ 55.8***
Overall Growth %		***3.9%***	***3.0%***	***3.7%***	***3.5%***	***2.9%***	***3.2%***

[1] FY 2019 Unaudited Actuals from the FY 2019 Year-End Financial Performance Report.

[2] FY 2020 Projection from the FY 2020 First Quarter Budget Monitoring Report, except for Other Revenues which is projected at budget.

[3] Franchise Fees in the FY 2021-2025 Five-Year Financial Outlook include departmental franchise fees. These have been moved to the Other Revenues in the table above for comparison to FY 2019 Unaudited Actual and FY 2020 Projection.

Note: Growth Rate is applied by Department of Finance to majority of revenue within each category, then additional adjustments are applied based on known information.

Generally, our Office agrees with the slowing growth rates applied to revenues. As noted in the Outlook, the economy has seen steady improvements since 2009. A recession could occur during this Outlook period but is not reflected in the projections. Rather, the projections reflect slowing growth rates based on trends and the most recent information available. Following are some items of note regarding the projections in the Outlook.

- Property tax remains strong despite a slow-down in property sales due to the values of those properties remaining high. The Outlook projects 5.0% growth in property tax for FY 2021, slowing to 4.0% growth by FY 2025.

- Actual sales tax received in FY 2019 was high due to the change in the State's system which resulted in FY 2018 sales tax earnings being received in FY 2019. This was accounted for when the FY 2020 sales tax budget was developed and is why we see a dip in sales tax revenue from FY 2019 to FY 2020 in the table on the previous page. Sales tax projections for FY 2020 reflect 3.9% growth; however, the Outlook reduces those growth rates from 3.4% in FY 2021 down to 2.9% by FY 2025 to reflect the continued slowing of the economy and the shift of sales from brick and mortar stores to online purchases, which results in a smaller portion of sales tax to the City.

- The Outlook projects TOT revenue to grow by 3.8% in FY 2021 due to an expected increase in the average daily room rate and the supply of rooms available. This is then assumed to taper off slightly in the following years; however, still remaining steady throughout the Outlook period.

- SDG&E makes up over 60% of franchise fee revenue. The projections in the Outlook are based on the current franchise agreement with SDG&E. Meanwhile, revenue from the cable companies is expected to continue to decline but is offset by steady 2% growth projected from the refuse haulers franchise fee.

Overall, General Fund revenues are projected to grow by $46.5 million, or 3.0%, in FY 2021, as compared to the FY 2020 First Quarter projection. Revenue growth reaches a high of $59.4 million, or 3.7%, in FY 2022, with more moderate revenue growth in the following years. However, it is worth noting that these projections assume we do not experience a recession during this timeframe. Additional information on the current performance of General Fund revenues will be available in the FY 2019 Mid-Year Budget Monitoring Report (Mid-Year Report) and with the development of the FY 2020 Budget. Our Office will continue to monitor those trends.

Recession Scenario and Analysis

As previously mentioned, the revenue assumptions contained in the Outlook do not include the assumption of a recession at any time during the Outlook. The revenue projections contained in the Outlook are based on actual trends and are consistent with information received from the various consultants and economic indices that the City uses to develop the revenue projection. For now, while some consultants and economists are warning of a possible recession, most, if not all, are not including a recession prediction in their forecasts. However, there is always the chance that a recession could be right around the corner, and as such our Office was asked to do a recession analysis showing the gap in revenues that could reasonably be foreseen.

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

We should note that no one reasonably knows when a recession might occur, or what type of recession we may have. The previous recession, for example, hit the real estate market extremely hard, and as such drove a large decline in the property tax revenues for the City. However, previous recessions had, for the most part, only slowed the growth in property taxes. Again, it is not known what this next recession will look like, or how it will hit. The actual impact of a recession on the major revenues could be drastically different depending on a variety of factors, including various triggers, severity, duration, and timing.

The following scenario represents the best estimate for a recession that our Office could put together in the relatively short time frame of the request. For the purposes of this analysis, we only made changes to the three major revenues that are most affected by a recession: property tax, sales tax, and TOT. We did not include any assumptions for franchise fees as they tend to not be as severely impacted by recessions, nor did we assume any impact for other departmental general fund revenues.

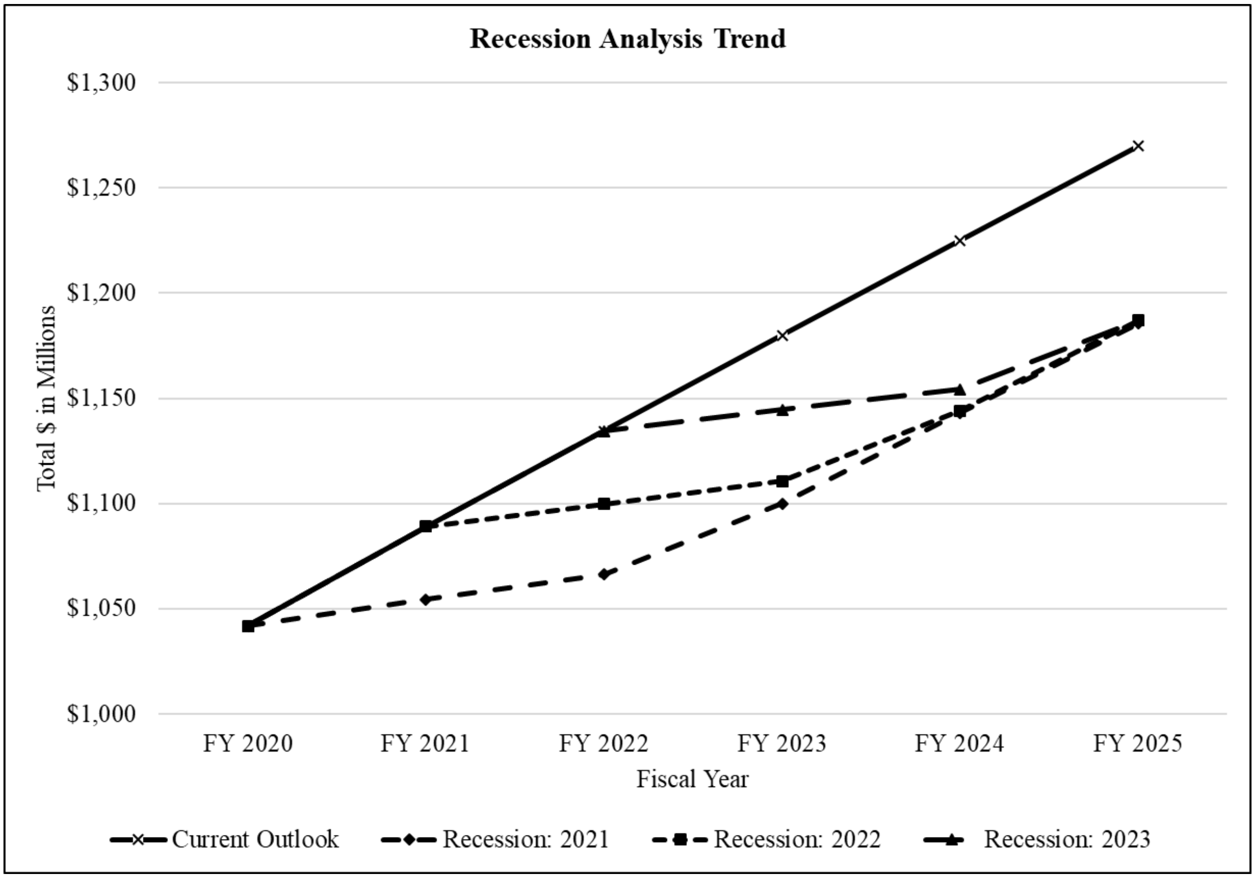
Recession Analysis: Potential Impact (in millions)					
	FY 2021	**FY 2022**	**FY 2023**	**FY 2024**	**FY 2025**
Outlook (Shortfall)/Surplus	$ (83.7)	$ (66.6)	$ (33.6)	$ (7.6)	$ 25.5
Potential Recession Impact					
Property Tax	$ -	$ (9.5)	$ (19.8)	$ (20.7)	$ (21.5)
Sales Tax	(22.5)	(37.7)	(38.3)	(38.8)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

For our analysis, we assumed that the bulk of the recessionary period takes place in FY 2021, which would be a potential worst-case scenario as far as timing of the recessionary period. Assuming this is the case, and based on historical activity, the two revenue sources that take the largest and most immediate decline are the sales tax and TOT.

- For the sales tax, total revenue would decrease by 4.0% in FY 2021, and an additional 1.8% in FY 2022, before rebounding back to historic growth levels.
- For TOT, the decline occurs in roughly the same fashion, but historically the decline has been even steeper. Our analysis predicts a 5.0% decline in total TOT revenue for FY 2021 and a 3.0% decline for FY 2022.
- For property taxes, the impact to revenues has historically been about one year after the decline in sales and TOT. For this analysis, we subtracted 2.0 percentage points from the otherwise projected growth in property taxes for FY 2022 and FY 2023.

As you can see in the table above, this worsens the Outlook deficit by $34.6 million in FY 2021, increasing the Outlook deficit from $83.7 million to $118.3 million. This gap continues to widen, reaching $84.2 million by FY 2025.

Further, due to the unpredictability of the recession timing, our Office decided to start the recession in numerous years to see the overall impact. While the decline in growth is delayed, the overall impact in FY 2025 remains fairly constant, as displayed in the graph below. This is due to the fact that our analysis only returns revenue growth to those rates that would have otherwise occurred. This is based on the trends following the last recession in 2009 where revenues only increased at a modest rate once the recession is over. Should this trend continue again no matter when the recession happens, it will portend a permanent decrease in the revenue base for the City.



Cannabis Business Tax

The Outlook includes projected revenue from the City's non-medical cannabis business tax (CBT). It estimates CBT revenue of $17.0 million in FY 2020, which is $4.8 million higher than the FY 2020 Adopted Budget of $12.2 million. The Outlook's revenue projection shows an average annual increase of $2.5 million through FY 2025 when the revenue is anticipated to be $29.7 million.

The increase in the CBT projection is attributable to FY 2020 being the first full year that the medical exemption will only apply to purchases made by patients with a State Issued Medical Marijuana Identification Card, as well as CBT applying to all ancillary items being sold by the outlets. Additionally, growth in CBT revenue in the Outlook's projection includes an increase in the number of outlets remitting taxes from 14 to 16 outlets in FY 2020. As a result, the Outlook's projection of CBT revenue takes a more aggressive approach because it includes an increase in the number of outlets as well as permitted cannabis businesses such as cultivators, manufacturers, and distributors.

Our Office will continue to review the CBT revenue throughout the FY 2021 budget development process as the cannabis business continues to develop with the advent of additional cannabis outlets and dispensaries, as well as the addition of potential changes to State, Federal, and local regulations.

Potential Stadium Impacts to Baseline

One area that has potential revenue impacts is the operations of SDCCU stadium. While the General Fund does not directly support the operations of the stadium, which is paid for by the Stadium Operations Fund, there is a significant amount of support provided by the Special Promotional Programs Fund for stadium operations.

Currently, the Baseline assumes that the City would continue to operate the stadium through the end of the current lease agreements, which end after December 2020, and that significant costs would only be incurred through the end of Fiscal 2021, with basic security services provided thereafter. The current Baseline thus assumes $7.6 million in FY 2021 and $3.6 million in FY 2022 would come from the Special Promotional Programs Fund for stadium support.

Currently, the City is negotiating with San Diego State University (SDSU) to sell the stadium site. The current offer most recently considered by Council included a provision that, if the sale is not completed by June 30, 2020, SDSU would lease the stadium from the City and take over operations of the facility. If the lease and/or deal are approved by the City Council prior to July 1, 2020, the Special Promotional Programs Fund would no longer have to support the stadium operations, and these funds could be reallocated to provide General Fund relief for tourism-related activities. For more information, see our section on Potential Mitigation measures.

REVIEW OF BASELINE GENERAL FUND EXPENDITURES

As shown in the table on the following page, the Outlook's FY 2021 General Fund Baseline projection is increasing by a ***net*** $26.9 million (or 1.7%) from the FY 2020 Adopted Budget.

The largest cost ***increases*** shown in the table include:

- $8.7 million for compensation increases (including variable fringe) primarily based on agreements with the City's recognized employee organizations,
- $3.8 million for the Actuarially Determined Contribution (ADC) pension payment increase,
- $2.3 million for impacts of step increases on salaries and wages,
- $8.7 million for information technology (IT) increases (including $2.9 million for help desk support, $2.4 million for voice/data network, and $2.0 million for data center expenses),
- $7.5 million for the 3.89% annual increase in costs for contracts, and
- $3.4 million for Public Liability insurance premium increase.

Additionally, the table on the following page shows certain expenditure increases related to FY 2020 use of one-time resources to cover various costs. These FY 2020 resources, which temporarily reduced overall expenditures by $9.1 million, included $4.0 million of Charter Section 77.1 Infrastructure Funds, $2.6 million in excess Public Liability Reserves, and $2.5 million of Capital Outlay Funds.

Increases/(Decreases) from the FY 2020 Adopted Budget to the FY 2021 Outlook Baseline Projection (in millions)		
FY 2020 Adopted Budget		**$ 1,590.0**
Personnel-Related Expenditure Changes		**17.4**
Net Compensation Increases from Labor Agreements, Compensation Schedule Adjustments [1]	$ 8.7	
Actuarially Determined Contribution (ADC) - Retirement Payment Increase	3.8	
Step Increases for Salaries and Wages	2.3	
Workers' Compensation Increased Contributions	2.1	
Long-term Disability (LTD) - (FY 2020 fully funded with excess LTD reserves)	1.9	
Termination Pay (for Annual Leave) Increase	1.2	
Other Post-Employment Benefits (OPEB) - 2.5% Annual Increase	1.1	
Net Salaries and Wages and Fringe Benefits Changes (other than those separately listed)	0.4	
Police Overtime Decrease - Clean SD ($3.5M) & Other Neighborhood Policing ($447,000) [2]	(4.0)	
Non-Personnel Expenditure (NPE) Changes		**28.2**
IT Increases (including $2.9M help desk; $2.4M voice/data network; $2.0M data center)	8.7	
Contracts - 3.89% Annual Growth Rate	7.5	
Public Liability Insurance Premium Increase	3.4	
Energy and Utilities - Various Growth Rates (electric, fuel, water, other)	1.7	
San Diego Humane Society Contract	1.6	
Charter Section 77.1 - Infrastructure Fund Transfer Increase	1.4	
Supplies - 4.58% Annual Growth Rate	1.4	
General Fund Reserve Contribution Increase	0.9	
Net Other NPE Changes (other than those separately listed)	1.7	
Removal of FY 2020 One-Time NPEs (see Five-Year Outlook, Attachment 2) [3]		**(18.7)**
Transfers to CIP	(5.6)	
Commission for Arts & Culture Funding	(3.9)	
Clean SD NPE (there is also $3.5M in Police overtime related to Clean SD)	(2.7)	
Animal Control and Services Program (one-time portion of budgeted expenditures)	(2.2)	
Companion Unit Fee Waiver Program ($800,000); Various IT Expenditures ($788,000)	(1.6)	
Community Projects, Programs, and Services	(1.5)	
Consultants - Energy Franchise Agreement Negotiations ($1.0M) & Disparity Study ($1.0M)	(2.0)	
NPEs for Two Fire Academies	(0.9)	
Use of Capital Outlay Fund for Deferred Capital Bond Debt Service	2.5	
Use of Excess Public Liability Reserve	2.6	
Use of Charter Section 77.1 Infrastructure Funds for Right of Way Maintenance	4.0	
Additional One-Time Expenditures (other than those separately listed)	$ (7.5)	
FY 2021 Outlook Baseline Projection		**$ 1,616.9**
Total Increase: FY 2020 Adopted Budget to FY 2021 Outlook Baseline (1.7% Increase)		**$ 26.9**

Note: Table may not total due to rounding.

[1] The net compensation increases line is primarily due to agreements with employee organizations (includes variable fringe costs).

[2] FY 2020 also includes an additional $3.9M for neighborhood policing overtime budgeted in the Seized Assets Fund, which for FY 2021 is included in the General Fund's Critical Strategic Expenditures.

[3] Attachment 2 to the Five-Year Outlook includes one-time expenditures of $60.1M - only $18.7M of which is shown in the "Removal of FY 2020 One-Time NPEs" section of this table. The remaining FY 2020 one-time expenditures are addressed among other components of this table and include: $24.1M Infrastructure Fund transfer; $11.9M in General Fund Reserve contributions; $4.3M Pension Payment Stabilization Reserve contribution; $4.0M Police overtime; and $3.2M related to FY 2020 use of excess Workers' Compensation and Long-term Disability Reserves.

Baseline increases are partially offset with a number of expenditure ***decreases***. The largest shown in the previous table include:

- $5.6 million for one-time FY 2020 transfers to CIP,
- $4.0 million for one-time FY 2020 Police overtime (including $3.5 million for CleanSD and $447,000 for other neighborhood policing),
- $3.9 million for one-time FY 2020 transfers to support the Penny for the Arts program, and
- $2.7 million for one-time FY 2020 CleanSD litter removal and abatement contract costs.

There are no increases related to new programs in the General Fund Baseline expenditures projection. New and expanded programs, and existing programs requiring new funding sources recommended by the Mayor, are included in the Critical Strategic Expenditures portion of the Outlook, which are discussed later in this report. More detailed components of Baseline expenditures are discussed below.

Personnel-Related Expenditures in the Outlook Baseline

Compensation Increases from Labor Agreements and Compensation Schedule Adjustments
General Fund compensation increases related to agreements with the City's employee organizations, or memorandums of understanding (MOUs), and compensation schedule adjustments total $8.7 million for the FY 2021 Baseline (including variable fringe). This $8.7 million rises further, by $794,000 over the remaining Outlook years (an average of 2.3% per year), bringing these compensation increases to $9.5 million in FY 2025. The largest component of the additional $794,000 is related to increased salaries for elected officials in accordance with the November 2018 Measure L (at $575,000).

FY 2021's ***net*** $8.7 million Baseline impact for these compensation adjustments is shown in the table on the following page and includes $10.7 million of increases:

- $8.7 million for Police Officers Association (POA) employees,
- $1.4 million for annualization of Municipal Employees Association (MEA) special salary adjustments (SSAs) and special assignment pays (add-on pays) that began in FY 2020,
- $339,000 related to elected officials' salary increases resulting from the passage of the November 2018 Measure L, and
- $227,000 for other SSA annualizations.

An offsetting $2.0 million compensation decrease includes amounts for Firefighters' overtime ($1.7 million) and annual leave ($277,000), related to required reductions in accumulated annual leave over accrual caps.

Net Compensation Increases from Labor Agreements & Compensation Schedule Adjustments General Fund Impacts (in millions)	FY 2021 Increase
Police Officers Association (POA)	
Annualization of FY 2020 Pay Increases (including $727,000 for Police Overtime)	$ 5.8
Police Officers' Holiday Credit on Days Off	2.9
Subtotal POA	*$ 8.7*
Annualization of FY 2020 MEA [1] Special Salary Adjustments (SSAs) & Special Assignment Pays	1.4
Increases to Elected Officials' Salaries - November 2018 Measure L	0.3
Annualizations of Other FY 2020 SSAs ($90,000 for Local 127 [2]; $137,000 for Unrepresented Employees)	0.2
Decreases to Firefighters' Annual Leave (AL) and Overtime - Related to Accumulated AL Over Accrual Caps	(2.0)
Net Increase Over FY 2020	**$ 8.7**

[1] Municipal Employees Association

[2] American Federation of State, County and Municipal Employees (AFSCME) Local 127

The FY 2021 estimated compensation increases shown in the table above can be grouped into a few categories: annualization of FY 2020 pay increases, Police Officers' holiday credit on days off, and increases to elected officials' salaries. The next sections cover the Baseline increases for annualizations and holiday credit on days off, as well as the $2.0 million decrease for Firefighters' annual leave and overtime related to required reductions in accumulated annual leave over accrual caps.

Annualization of FY 2020 Pay Increases

The following "across-the-board" pensionable pay increases have taken place or will in FY 2020.

- 3.3% negotiated increases for four of the six recognized employee organizations (beginning July 2019),
- 3.3% increases for unrepresented employees (beginning July 2019),
- 7.5% or 8.5% negotiated increases for Deputy City Attorneys Association (DCAA) employees, depending on job classification (beginning July 2019), and
- 7.3% and 5.0% increases scheduled for July 2019 and January 2020, respectively, that were negotiated with the POA.

Annualization of FY 2020 pay increases in FY 2021 is the result of pay increases that will be in effect for less a full year in FY 2020. All across-the-board increases mentioned above will be in effect for the whole of FY 2020 except the POA's January 2020 increase, which is the largest contributor to the annualization of FY 2020 pay increases. The POA's $5.8 million annualization includes over $4.8 million for the 5% across-the-board increase in January 2020, $727,000 for overtime, and $215,000 related to a negotiated 5% pensionable add-on pay for Officers with 20 or more years of sworn service. This add-on became effective July 2019, but the number of eligible Officers is anticipated to increase in FY 2021.

Other annualizations in FY 2021 include $1.4 million for MEA employees, $137,000 for unrepresented employees, and $90,000 for American Federation of State, County and Municipal Employees (AFSCME) Local 127 employees. These annualizations primarily relate to pensionable SSAs and add-on pays that will become effective in January or April of 2020.

Police Officers' Holiday Credit on Days Off

In accordance with the POA MOU, a Police Officer is currently not compensated for a holiday which falls on his or her regularly scheduled day off. The elimination of this "holiday credit on a day off" was a negotiated contract term that went into effect for FY 2014. The reason for elimination of this holiday credit is that the City and POA agreed to convert certain holiday compensation to increased flexible benefits.

With the current POA contract, the elimination of the "holiday credit on a day off" stays in effect until June 30, 2020, at which time holiday credit for days off will again be compensated. Officers will receive straight-time pay or an equal amount of compensatory time (comp time) for such holidays. For the FY 2021 Baseline, the Department of Finance has estimated the cost of the "holiday credit on a day off" to be $2.9 million.

This cost is difficult to predict due to variations in behaviors. For example, an Officer could choose to receive comp time, rather than straight time pay. When that comp time is utilized as a day off, there is the potential for overtime to be incurred by another Officer "backfilling" for the absent Officer. The overtime cost for backfilling an Officer would be at a rate of time and a half, rather than straight-time pay. It is also possible that an absent Officer's shift will not need to be backfilled, resulting in no cost.

Decreases to Firefighters' Annual Leave and Overtime – Related to Required Reductions in Accumulated Annual Leave Over Accrual Caps

The table on page 9 includes a $2.0 million decrease for Firefighters' annual leave and overtime related to annual leave over accrual caps ($277,000 and $1.7 million respectively). The current MOU with International Association of Fire Fighters Local 145 includes caps on Firefighters' annual leave accruals and requirements for reducing balances above the caps. Effective FY 2020, Firefighters who have not reduced their annual leave balances below the allowable maximum accrual will cease to accrue annual leave.

Mandatory payments for annual leave balances above accrual caps have taken place over the past several years, and are required until each employee's annual leave balance is below the maximum allowable accumulation. Department of Finance has determined there are only a handful of employees with high enough leave balances to require mandatory payouts, and such payouts will be nominal. Thus, the Baseline includes a reduction of $277,000 for associated pay-in-lieu costs.

In addition to receiving mandatory payouts of excess annual leave amounts as prescribed in the MOU, Firefighters have been taking more leave time to reduce their balances. When a Firefighter takes leave time, in his/her absence, another Firefighter will be requested to backfill the absent Firefighter's post to keep the constant staffing model operational. This backfilling has been causing substitute Firefighters to exceed (or further exceed) the 212-hour overtime threshold. Because annual leave above the caps is anticipated to be paid down by FY 2021, the overtime cost of such backfilling is estimated to decrease by $1.7 million for FY 2021.

Future MOU Considerations

> ***The Outlook does not contain estimates for any potential new negotiated compensation increases for FY 2021.***

MOUs for all employee organizations run through FY 2020; and FY 2021 contract negotiations are currently underway. The Outlook does not contain estimates for any potential new negotiated compensation increases for FY 2021 (and through the remainder of the Outlook). The Department of Finance estimates a 1% salary increase for City employees would be about $6.0 million for the General Fund.

Vacancy Savings

The annual Adopted Budget includes a listing of full-time equivalent (FTE) positions that are authorized to be filled; however, it does not provide funding for all authorized positions due to the vacancy factor. The budget removes funding for some positions to account for savings that routinely occur due to turnover, leaves of absence, and when newly hired employees fill vacancies at lower salaries than budgeted. The amount of funding removed from the budget for these occurrences, known as vacancy savings, reduces overall budgeted salaries and wages.[1]

Over the past several years actual vacancy savings has been significantly higher than vacancy savings included in each annual budget. As discussed in IBA Report 19-26 (IBA Review of the FY 2019 Year-End Financial Performance Report), there has been a recurring trend where additional vacancy savings beyond the budgeted amount has been used as a funding source for overages in the other wage types (including special pays, overtime, hourly wages, vacation pay-in-lieu, and termination pay).[2]

The City could consider increasing FY 2021 budgeted vacancy savings, or alternatively eliminate funded vacant positions, to free up budget for other program areas. However, we caution that these actions would likely leave less of a cushion for other salaries and wages overages should they continue the trend of exceeding budget. Ensuring that all other salaries and wages expenditures (overtime, special pays, hourly wages, vacation pay-in-lieu, termination pay) have sufficient funding levels will be important if salaries are reduced through eliminations of funded vacant positions, or increases in vacancy savings. The FY 2020 Mid-Year Report will provide useful information on how vacancy savings and other salary and wage types are trending.

Pension Payment – ADC

The ADC is the retirement payment made by the City for its defined benefit pension. The Outlook's citywide ADC estimate for FY 2021 is $355.5 million. Of this amount, $268.6 million is for the General Fund, an increase of $3.8 million from FY 2020. The annual citywide ADC projections for the remaining Outlook years average about $350.0 million (about $265.0 million General Fund).

The Outlook's ADC forecasts are based on the most recently provided estimates from the San Diego City Employees' Retirement System's (SDCERS) actuary, Cheiron, in the FY 2018

[1] Leaving the unfunded positions in the budget keeps the authorized positions transparent.

[2] The condition where excess vacancy savings covers over-budget amounts for other wages types (or vice versa) can be a natural occurrence in a dynamic organization. For example, in a constant staffing model such as for fire suppression, overtime may be needed when the existing staffing levels are insufficient to meet required staffing levels. With increases in vacancies there may be times when more overtime is needed than was originally expected.

actuarial valuation. These latest projections include an investment rate reduction from 6.75% for FY 2018 to 6.5% for FY 2019 and later years. They also include estimated impacts for Police Officers' pensionable pay increases that were approved in December 2017.

Subsequent to the completion of the latest ADC projections, the actual FY 2019 investment return was determined to be 7%. This is 0.5% higher than the 6.5% previously assumed, which will produce an investment "experience gain" and correspondingly, future reductions to ADCs. However, offsetting such ADC reductions will be impacts of pensionable pay increases that were not incorporated into the latest ADC projections, including FY 2019 SSAs and add-ons.

Because of the complexity of the pension system variables, the total of ***all*** impacts to the ADC will not be known until the FY 2019 valuation has been completed. The FY 2019 valuation, which will incorporate not only the FY 2019 investment results and certain pensionable pay increases, but all FY 2019 experience gains and losses, is anticipated to be available in January 2020. This valuation will determine the FY 2021 ADC, and it is anticipated to include updated ADC estimates for FY 2022-2025.

Future ADC Considerations

First, we would note that a significant stock market correction is possible in the next five years. In such a case, if investment earnings are lower than assumed in the actuarial valuation, future ADCs could be increased.

Second, there is the possibility of changes in assumptions used to produce the actuarial valuation. For an example of a potential assumption change, the SDCERS Board has previously discussed further reducing the discount rate assumption. Assumption changes are scheduled to be discussed with the "experience study" that includes the June 30, 2019 actuarial valuation (anticipated for the spring of 2020). Any assumption changes subsequently implemented in the FY 2020 valuation would impact the ADC for FY 2022.

Non-Personnel Expenditures (NPE) in the Outlook Baseline

The Outlook discusses Baseline NPE expenditures for the following categories: supplies, contracts, information technology, and energy and utilities. The table on page 7 provides a summary of major NPE changes from the FY 2020 Adopted Budget to the FY 2021 Outlook Baseline projection. Two NPE areas are further discussed below: contracts and information technology.

Contracts

Contracts are increasing from $246.9 million in the FY 2020 Adopted Budget to $247.9 million in the FY 2021 Baseline (an increase of $916,000) due to a number of offsetting increases and decreases. The largest increases are listed below:

- $7.5 million increase for the 3.89% growth rate applied to contracts,
- $3.4 million increase for Public Liability insurance premiums, and
- $1.6 million increase for the San Diego Humane Society animal services contract.

These increases are partially offset with $11.3 million in decreases due to removing FY 2020 one-time contracts expenditures, including $2.7 million in CleanSD litter removal and abatement costs; $2.2 million for one-time animal services costs; $1.0 million for energy franchise agreement negotiation costs; and $1.0 million for disparity study costs.

Subsequent growth in contracts over the remaining four Outlook years (which incorporates the 3.89% growth rate) is $43.8 million, for a total contracts projection of $291.6 million in FY 2025. The actual contracts spending level will be based on contracts in place and terms of those contracts, as well as the City's payment schedules. Service needs may vary from year to year, and the contracts spending category can include significant one-time expenditures. Spending for contracts over the past few years is shown in the following table.

General Fund Contracts - Past Expenditures				
(in millions)	FY 2016	FY 2017	FY 2018	FY 2019
Actual Expenditures	$ 229.3	$ 240.3	$ 232.4	$ 233.4

The average contract expenditures over the previous four fiscal years was $233.9 million. Contracts can vary significantly from year-to-year. However, based on recent spending levels, the 3.89% contracts growth rate may be projecting Outlook expenditures that are higher than necessary.

Information Technology

The Baseline reflects increases in information technology (IT) expenses to the General Fund of $7.9 million for FY 2021. This is more than 20% over the General Fund's FY 2020 Adopted IT budget. About a third of the total IT costs are inflated by forecasted consumer price index of 3.0% for FY 2021. The remaining two-thirds of the IT category are adjusted based on specific and anticipated needs and cost inflations. The largest increases anticipated for FY 2021 are:

- Help desk and desktop support $2.9 million
- Voice/data network $2.4 million
- Data center $2.0 million

Approximately $3.1 million of the projected increase in General Fund IT expenses for FY 2021 is related to anticipated costs associated with transitioning help desk and desktop support, as well as the data center to new vendors. Existing contracts are reaching the end of their term and Request for Proposals will be going out in calendar year 2020 to seek bids for these services. Included in the projections are one-time costs of transitioning the services to new vendors (depending on who wins the bids) and cost inflation since industry IT costs have risen significantly since the existing contracts were issued seven or more years ago.

Also included in the IT projections for FY 2021 are costs to address physical infrastructure for the City's voice/data network and data center. Approximately $1.7 million is needed from the General Fund to refresh and/or upgrade network hardware that is reaching the end of its useful life. Another estimated $1.1 million is needed to upgrade the data center's infrastructure to successfully migrate the City to a hybrid cloud environment. Other items of note in the projected General Fund IT cost increase for FY 2021 include modernizing network bandwidth to keep up with the City's growing use of cloud-based applications and an anticipated 15% increase in license costs for Microsoft.

Risk Management Reserves

The FY 2020 Adopted Budget included the use of excess Risk Management Reserves to help balance the budget. The use of Risk Management Reserves' funds in FY 2020 was expected to substantively eliminate excess Reserve balances. Excess Reserves utilized for the General Fund portion of the budget included the following:

- $4.8 million in Long-Term Disability (LTD) Reserves transferred to the General Fund as revenue,
- $2.6 million in Public Liability (PL) Reserves utilized to cover FY 2020 PL operating costs,
- $2.0 million in LTD Reserves utilized to cover FY 2020 LTD operating costs, and
- $1.2 million in Workers' Compensation (WC) Reserves to cover FY 2020 WC operating costs.

Subsequent to the release of the Outlook, the Risk Management Reserves' FY 2019 actuarial valuations were completed. Based on these valuations, the LTD and WC Reserve requirement changes are minimal. However, with the latest PL valuation, the FY 2020 PL Reserve requirement has increased by $1.7 million to $33.8 million. Whether additional FY 2020 General Funds (potentially Excess Equity) will be needed to support the updated PL Reserve requirement will depend on the PL operating balance. If there is enough of a balance to absorb the $1.7 million increase to the Reserve requirement, additional General Fund expenditures will not be needed in FY 2020. The FY 2020 PL Reserve requirement remains the Reserve requirement estimate for future Outlook years until updated by the results of future actuarial valuations.

REVIEW OF CRITICAL STRATEGIC EXPENDITURES

The Mayor's Outlook includes $62.5 million of Critical Strategic Expenditures for FY 2021, growing to $123.1 million for FY 2025 (expenditures net of revenue). These are defined in the Outlook as "potential critical needs for the City" that are "necessary for meeting core service levels". These are the Mayor's highest priority items for consideration as the City begins developing the FY 2021 Proposed Budget. Adding these expenditures to the Baseline projected shortfall, brings the total projected deficit in the Outlook for FY 2021 to $83.7 million.

To provide context, we have grouped the FY 2021 Critical Strategic Expenditures into three broad categories:

- **Funding needed to maintain current programs** which are either funded with one-time General Funds or other funding sources in FY 2020, or are overbudget in FY 2020, totaling $36.5 million,
- **Funding needed to replace existing systems and equipment** that have reached the end of their useful life and are necessary for ongoing operations, totaling $7.9 million, and
- **Funding recommended for new services or enhancements** above and beyond what is currently being provided in FY 2020, totaling $18.2 million.

Specific line items from the Outlook are grouped into these categories in the table on the following page.

Mayor's FY 2021 Critical Strategic Expenditures (in millions)		
Item		**FY 2021 Amount**
Funding Needed to Maintain Current Programs		
Temporary Bridge Shelters	$	15.9
Neighborhood Policing Overtime		4.3
Arts, Culture, & Community Festivals Funding		3.9
CleanSD Overtime in Police		3.5
Continuing CleanSD Expansion in Environmental Services		2.9
Smart Streetlights		2.3
Transitional Storage Facilities		2.1
Safe Parking Program - Mission Valley		0.5
Security Guards at Central Library		0.3
Wheels of Change		0.3
Police Marketing & Recruitment Campaign		0.2
Dockless Mobility Enforcement by Police		0.2
Commercial Paper Borrowing Costs (beginning in FY 2022)		-
Total to Maintain Current Programs	*$*	*36.5*
Funding Needed to Replace Existing Systems & Equipment		
General Fund Vehicle Replacements		4.3
Public Safety Radio Equipment Replacement & Service Contracts		2.6
Replace Legacy Delinquent Accounts System & Services		0.6
Replacement of Council Electronic Voting & Audio-Visual Systems		0.3
Centralized Payment Processing Solution		0.2
Total to Replace Existing Systems & Equipment	*$*	*7.9*
Funding Recommended for New Services or Enhancements		(net of revenue)
New Parks & Recreation Facilities		6.0
Sidewalk Repair & Replacement		3.6
Storm Water Pipe Repair Team & Street Sweeping		3.3
Peak Hour Fire Engines		2.2
New North University City Fire Station		1.4
SDG&E Franchise Consultant		1.0
Climate Action Plan		0.8
EAM Phase II		0.5
Street Resurfacing		0.3
New Pacific Highlands Ranch Branch Library		0.2
Asbestos Remediation		0.2
Enhanced Police Officer Recruiting Efforts		0.1
Security Guards for Branch Libraries		0.2
Fire-Rescue Staffing Model & Relief Pool		(0.5)
Maintenance Savings from Police Helicopter Fleet Replacement		(1.2)
Total for New Services or Enhancements	*$*	*18.2*
Total Mayor's Critical Strategic Expenditures for FY 2021	**$**	**62.5**

The Baseline projected shortfall for FY 2021 in the Outlook is $21.2 million. Within the Critical Strategic Expenditures, approximately $36.5 million is funding needed to **maintain current priority programs**. These are services such as the *temporary bridge shelters, transitional storage facilities, safe parking and other homeless programs and services; CleanSD and neighborhood policing; security guards at the Central Library; arts, culture and community festivals funding; smart streetlights; and enforcement of dockless mobility devices.*

Projected Budget Gap		
(in millions)		**FY 2021**
Baseline Shortfall	$	21.2
Current Programs		36.5
Systems & Equip.		7.9
Subtotal Current	*$*	*65.5*
New/Expanded		18.2
Outlook Deficit	$	83.7

The next category we have identified is funding needed to **replace existing systems and equipment**, such as replacement of General Fund vehicles, the public safety radio equipment, delinquent account collection and payment processing systems and the electronic voting system used by City Council. These account for $7.9 million of the Critical Strategic Expenditures projected in the Outlook. When combined, the Baseline shortfall, plus funding to maintain current programs and replace existing systems and equipment, brings the projected deficit for FY 2021 to $65.5 million, as shown on the table.

Of the total Critical Strategic Expenditures included in the Outlook for FY 2021, only approximately $18.2 million, reflecting roughly 22% of the total Outlook deficit of $83.7 million, is for **new services or enhancements** recommended by the Mayor. These include funding for new facilities coming online or needing resources in FY 2021 - parks, a fire station and a library, increased sidewalk, storm water and street repairs, adding peak hour fire engines, the consultant to assist with SDG&E franchise negotiations, and climate action plan implementation.

Other programs recommended in the Fire-Rescue and Police Departments will result in budgetary savings of $1.7 million which are grouped into the new services and enhancements category. These are Fire-Rescue's staffing model and relief pool, which will result in a reduction in overtime, and a reduction of maintenance costs in Police from the purchase of replacement helicopters.

Review of Select Critical Strategic Expenditures: Funding Needed to Maintain Current Programs

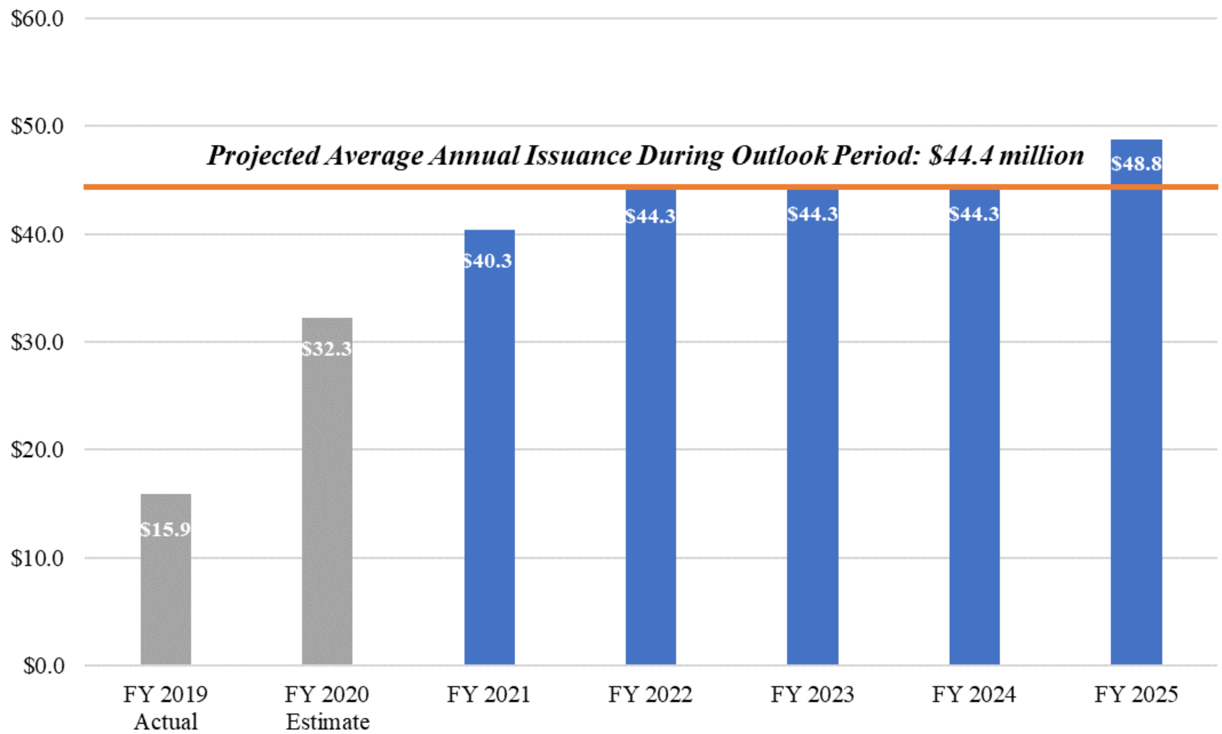
Citywide Program Expenditures: Borrowing Costs to fund General Fund Capital Projects

The Outlook includes $48.5 million to cover estimated borrowing costs for a $270.0 million financing plan for General Fund capital projects. The financing plan involves three $88.5 million phases of commercial paper borrowing, with an additional $4.5 million added to the last phase bringing total capital borrowing to $270.0 million (the first commercial paper borrowing began in FY 2019). When each phase of commercial borrowing reaches the $88.5 million authorization limit, the financing plan calls for replacing the outstanding short-term commercial paper notes with long-term bonds which are expected to be issued in June of 2021, 2023, and 2025. Therefore, the $48.5 million included in the Outlook is comprised of a combination of debt service expense for commercial paper notes and long-term bonds over the Outlook period.

With respect to the projected annual borrowing costs in the Outlook, $1.5 million of commercial paper debt service expense in FY 2021 has been included as a Baseline expenditure. Thereafter, annual borrowing costs are shown as Critical Strategic Expenditures. Additionally, we have confirmed that $5.9 million of debt service expense was mistakenly included in FY 2023. Correcting for this reduces the projected FY 2023 Outlook shortfall (factoring in Critical Strategic Expenditures) from $33.6 million to $27.7 million.

As shown in the chart below, the Outlook assumes the City will use commercial paper to borrow an average of $44.4 million per year, or $221.8 million over the entire Outlook period. This borrowing plan represents a significant increase in annual borrowing when compared to $15.9 million borrowed in FY 2019 and $32.3 million projected to be borrowed in FY 2020. Without improved project prioritization and expenditure planning, it may be difficult to spend $44.4 million of commercial paper proceeds a year considering that this represents an annual spending increase of approximately $28.5 million over FY 2019.

Commercial Paper Borrowing Plan - $270.0 million
(in millions)



It is important to note that the most recent five-year Capital Outlook identifies a $1.86 billion shortfall in which identified General Fund capital needs exceed the anticipated funding available. The shortfall represents funding needed *in addition to* the $270 million borrowing plan. Our Office believes that a critical part of any plan to identify additional revenue to mitigate the $1.86 billion shortfall must first endeavor to improve the City's ability to efficiently spend existing fund sources. This likely requires improved prioritization based on readiness to spend on project needs.

Citywide Program Expenditures: Restoration of Arts and Culture Funding

The FY 2020 Adopted Budget for Arts and Culture totals $14.2 million, including a one-time transfer of $3.9 million which supplements the $10.3 million base budget. This is the third consecutive year that a one-time transfer from the General Fund has been used in order to return funding levels to near FY 2017 levels. Restoration of $3.9 million in ongoing funding is included in the Outlook beginning in FY 2021 which would maintain funding for Arts and Culture at FY 2020 levels throughout the Outlook period.

Environmental Services: Ongoing Support for CleanSD
The Outlook recommends funding of $2.9 million annually throughout the Outlook period to continue CleanSD service levels that were expanded in FY 2020 with one-time funds. The expanded service levels that are expected to continue include litter removal 24 hours per day, seven days per week, and an additional waste abatement shift which primarily addresses homeless encampments. The total Environmental Services budget for the CleanSD Program is $6.7 million funded by the General Fund.

Homeless Programs and Services
The Outlook has identified $18.8 million for FY 2021, and $22.2 million for each year thereafter that is needed to continue homelessness programs that are funded with other one-time sources in FY 2020. The Outlook 1) reflects recognition of the ongoing funding need to support the ongoing Bridge Shelter Program and Storage Connect Center; and 2) signals the continuation of programs developed with one-time state funds called Homeless Emergency Aid Program (HEAP). Outside of these broader categories, we note that the Outlook includes $250,000 to support a program called Wheels of Change which the City began contributing to in FY 2020 through its CleanSD program. This program employs individuals residing at the Single Adults Bridge Shelter to provide community clean ups.

<u>Recognizes Need for Ongoing Funding</u>
The Outlook reflects the need for ongoing funding to support the Bridge Shelter Program at a cost of $15.9 million and the Storage Connect Center located in Sherman Heights at a cost of $1.4 million throughout the Outlook period. These programs have largely been funded with San Diego Housing Commission reserves as well as other one-time City resources. The bridge shelters serving the following populations are included as Critical Strategic Expenditures:

- Single adults (324 beds)
- Veterans (200 beds)
- Women and families (141 beds)
- Flexible population (128 beds)

<u>Continues Most Programs Supported by HEAP Funds</u>
The Outlook also generally continues the programs that were allocated one-time HEAP funds, except for the flexible spending pool and outreach activities. Staff indicates that the flexible spending pool will undergo further review during the budget process. In addition, though $1.6 million was initially allocated to expand outreach activities when HEAP programs were approved, and then reallocated to the Bridge Shelter Program, no request was made to fund outreach over the next five years. According to staff, outreach is currently embedded in the bridge shelters, storage facilities, and Housing Navigation Center programs.

Provisions for HEAP funds require the City to set aside $706,000 for youth-focused programs to be spent over multiple fiscal years, through FY 2021. Beginning in FY 2022, the Outlook assumes continuation of youth programs at half this amount, or $353,000 per year, though these programs have yet to be established. However, there is a pending request that the Housing Authority and Council approve fully expending the $706,000 set aside in FY 2020 to partially fund an expansion of the Women and Families Bridge Shelter by 138 beds to additionally serve transitionally aged youth (ages 18 to 24). Therefore, the plan for youth-focused programs during the Outlook period is currently evolving. The shelter expansion is discussed further in the "Future Funding Needs Not Included in the Outlook" section of this report.

Library: Security

The Outlook includes $457,000 in additional ongoing funding for expanded library security services which would increase the total Library Department security budget to nearly $2.0 million. The additional funding is split between the Central Library, receiving $301,000 primarily to upgrade all security guards to armed guards, and branch libraries, receiving $156,000 to increase overall security coverage across library branches as needs necessitate.

The upgrade to armed guards at the Central Library, which the Police Department supports, has been in effect as of early FY 2020 given the current security needs at the facility. As a result, the FY 2020 budget for security services is currently estimated to be over budget by approximately $300,000. The Department will evaluate the need for an appropriation adjustment during the Mid-Year budget monitoring process.

Police: Ongoing Funding for Overtime to Maintain Service Levels

The Outlook includes ongoing funding for police overtime, totaling $8.0 million annually throughout the Outlook period, to maintain existing Neighborhood Policing, CleanSD, and Mobility Enforcement service levels that were funded in FY 2020 with one-time funds.

<u>Neighborhood Policing ($4.3 million)</u>

Neighborhood Policing overtime was funded in FY 2020 by $3.9 million in Seized Asset Funds and $447,000 from the General Fund to address homeless outreach and public safety needs related to the transitional storage facility in Sherman Heights, the Housing Navigation Center, operations around the San Diego Riverbed, and general Neighborhood Policing Division Support. The Outlook contemplates the full $4.3 million expense to be fully funded by the General Fund on an ongoing basis.

Our Office notes that the recently adopted Community Action Plan on Homelessness calls for the elimination of SDPD's role as first responders with respect to homeless outreach citing an undue pressure on limited law enforcement resources and increased confusion and anxiety felt by people experiencing homelessness under the current approach. Until such time that this recommendation is implemented, the Department expects a continuation of these service levels.

<u>CleanSD ($3.5 million)</u>

CleanSD activities, as described by the Department, differs from Neighborhood Policing work in that it involves Police Officers working together with ESD employees as they perform CleanSD functions. Officers report areas needing cleaning or sanitization to ESD, and accompany ESD employees during abatement of unattended property for security. These activities as assumed to continue at the same service level in the Outlook.

Mobility Enforcement ($170,000)
The FY 2020 Adopted budget included $150,000 in one-time funding for the Department's Dockless Mobility Enforcement Program. Under the program, a weekly detail, including one Sergeant and two to four officers, conduct enforcement activities related to shared mobility devices on an overtime basis. These activities as assumed to continue at the same service level in the Outlook. We note that the Outlook includes a slight increase in funding from $150,000 in FY 2020 to $170,000 over the Outlook Period.

Sustainability: Ongoing Smart Streetlights Program
The Outlook's Critical Strategic Expenditures include additional funding for the General Fund portion of the Smart Streetlights Program, including $2.3 million in FY 2021, which increases to $3.0 million in FY 2024 before decreasing to $2.0 million in FY 2025. These costs include funding necessary to increase the back-haul capabilities of the streetlights, as well as the ongoing operational costs of operating the Smart Streetlight Program.

Previously, the budget only contained funding for the installation of the smart streetlight modules, with the financing payments for the installation offset by the energy savings that would accrue from the switch to the LED lights. During FY 2019, the speed of the installations slowed as the City discovered that not all of the streetlights slated for installation had the necessary infrastructure and capacity to power the smart modules, also known as "back-haul". This funding allotment will include one-time funding to increase the back-haul necessary to operate the smart modules, as well as ongoing maintenance costs associated with data transfer from the modules. We note that these costs will not be covered by the additional energy savings from the installation of the LED lights, as that money will still be necessary to pay for the financing payments on the installation charges.

Also, our Office would note that the FY 2020 budget did not include funding for the maintenance costs for those smart streetlights that have already been installed, even though the City is currently incurring those costs. This may require an appropriation adjustment request in the Mid-Year Budget Monitoring Report.

Review of Select Critical Strategic Expenditures: Funding Needed to Replace Existing Systems and Equipment

Information Technology: Public Safety Radio
The Outlook includes funding increases for the City's public safety radio system that range from $2.6 million in FY 2021 to nearly $6.8 million in FY 2024 and FY 2025. Over the five years, these projections include expenses for the contract with Motorola, decommissioning old radio sites, adding new radio repeater sites and replacing all public safety radios to newer models. These expenses are considered critical in order to keep the City's emergency radio and dispatch system operational, maintain FCC licensing and be eligible for grant funding.

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

Fire-Rescue: New Fire Stations Opening within the Outlook Period
The Outlook's Critical Strategic Expenditures include funding for operational expenses for four new fire stations projected to open within the Outlook period. These expenses are phased in over five years and total approximately $9.6 million in FY 2025, including the addition of 60.00 FTEs. Operational expenses include personnel expenditures and non-personnel expenditures such as equipment and supplies. Costs for items that may be considered capital in nature, like fire engines and ladder trucks, are routinely financed through the City's Equipment and Vehicle Financing Program (EVFP).

The four new fire stations identified in the Outlook as requiring operational funding over the next five years are listed below according to their expected opening date:

FY 2021 – North University City (developer funded)
FY 2022 – Black Mountain Ranch (developer funded)
FY 2024 – Fairmont Avenue (land purchased; lacks capital funding for construction)
FY 2025 – Paradise Hills (no land; lacks capital funding)

We note that all four stations were identified as high-priority sites by the 2017 Citygate Report, which recommended the addition of up to 12 new fire stations as well as other increased services such as Peak Hour Engines (discussed later in this report) in order to improve the Fire-Rescue Department's ability to meet its response time standards.

As noted in the list, the first two stations already have full funding identified for capital construction costs. The final two stations, Fairmont Avenue and Paradise Hills, do not have full funding identified for construction at this time. Further, all four of these fire stations were included in the Fiscal Year 2020-2024 Outlook as well, with the notable exception that the Fairmont Avenue and Paradise Hills stations were included one year earlier (in FY 2023 and FY 2024, respectively), than they are in the current Outlook. We also note that the Paradise Hills Fire Station is planned to be a double-house station, which will require the addition of 24.00 FTEs as opposed to the standard 12.00 FTEs normally needed to staff a fire station. The schedule for constructing and staffing all four stations will be impacted by the available capital funds for construction and General Funds available for adding 60.00 new FTE positions. A list of expenses for each station anticipated to open or become operational within the Outlook period is attached to this report.

Fire-Rescue: Staffing Model and Relief Pool to Reduce Overtime Costs
The current Outlook includes continued staffing for the Fire-Rescue relief pool, which was included in the previous Outlook, as well as implemented in the FY 2020 Adopted Budget. This Critical Strategic Expenditure will continue to add 37.00 additional FTE Firefighters in FY 2021 and FY 2022, until the total relief pool is up to 111.00 FTEs (37.00 FTEs were added with the FY 2020 Adopted Budget). The program is anticipated to increase expenditures for personnel and academy costs, but these costs are projected to be more than offset by overtime savings within the department.

Fire-Rescue Relief Pool Costs					
	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
Additional FTEs	37.00	74.00	74.00	74.00	74.00
Personnel Expenditures (PE)	$ 4,349,604	$ 8,699,208	$ 8,699,208	$ 8,699,208	$ 8,699,208
Overtime Offset	(5,232,029)	(10,464,058)	(10,464,058)	(10,464,058)	(10,464,058)
Subtotal – Net PE Savings	*$ (882,425)*	*$ (1,764,850)*	*$ (1,764,850)*	*$ (1,764,850)*	*$ (1,764,850)*
Academy Cost to Build Relief Pool (short-term)	431,324	431,324	-	-	-
Total Cost	**$ (451,101)**	**$ (1,333,526)**	**$ (1,764,850)**	**$ (1,764,850)**	**$ (1,764,850)**

By hiring more polkics to staff a relief pool, the Department anticipates achieving net savings in personnel expenditures by shifting costs from overtime (premium pay) to salaries (straight pay). The table above illustrates the various components of establishing a relief pool included in the Outlook, including the cost of running additional fire academies and supporting added personnel, as well as the overall net savings achieved due to reduced overtime. We would note that the relief pool is now showing a net savings in FY 2021 as opposed to a net spend as projected in the previous Outlook due to the addition of 9.00 FTEs for full-time academy instructors in FY 2020, which has lowered the incremental costs of additional academies in future years.

In previous reports, our Office has raised concerns about Fire-Rescue exceeding its overtime budget by significant amounts over the past several fiscal years. The proposed Relief Pool Critical Strategic Expenditure is intended to bring the Department's staffing levels into greater balance and reduce the Department's dependence on overtime to achieve constant staffing. While our Office is supportive of the relief pool in concept, should it continue to be funded and implemented, close monitoring of personnel expenditures relative to overtime will be required in FY 2020 and beyond to verify whether anticipated net savings actually occur as planned.

Fire-Rescue: Peak Hour Engines

The Outlook once again contains Critical Strategic Expenditures for the buildup of the Peak Hour Engines (PHEs). This includes 48.00 FTEs Firefighter positions, phased in over three years, and total expenditures of $6.6 million by FY 2023. This item was included in the previous Outlook; however, it was not funded in the FY 2020 Adopted Budget.

PHEs are fire engines that do not operate out of a fire station but are instead flexibly deployed in various areas based on need for 12 hours per day. Like traditional fire stations, PHEs are staffed by four-person crews. Due to the nature of Firefighters' shifts, the budgetary impact of staffing one 12-hour PHE is 8.00 FTE Firefighter positions.

PHEs are a new deployment concept that has not yet been utilized by the San Diego Fire-Rescue Department. PHEs were a key recommendation of the 2017 Citygate Report, which identified several geographic service gap areas contributing to performance challenges and offered several recommendations to improve response times. The Department has indicated that its intention with the PHE concept is to supplement rather than replace fire stations and existing Fast Response Squad (FRS) units. PHEs are anticipated to be implemented by deploying existing reserve fire engines and would not require any significant capital investment.

Following the release of the 2017 Citygate Report, which outlined the PHE concept, our Office worked with the Fire-Rescue Department to develop an implementation scenario in which the Department would pursue the Citygate priorities concurrently if funding is available. The addition of six PHEs, along with the completion of new fire stations, are expected to make significant advances in achieving the Citygate recommendations for improved emergency response in the City.

Without the funding included in the FY 2020 Adopted Budget, the current Outlook contains a new schedule for the staffing of the PHEs. Instead of adding all six PHEs by FY 2021, the new Outlook would add two PHEs in each of FY 2021, FY 2022, and FY 2023. This would place the full staffing component two years behind the initial schedule.

Information Technology: Enterprise Asset Management (EAM) Phase II

The Enterprise Asset Management system (EAM) is a software solution with Phase I implementation completed in FY 2018. The system allows staff to obtain information on City assets such as cost, schedule, maintenance history, and geographic location. This data allows staff to determine if a project or replacement of an existing asset is necessary and allows the Asset Managing Departments (AMD) to categorize work as a priority or non-priority. Assets included in the system in Phase I include wastewater mains, water distribution mains, water transmission mains, streets, bridges, facilities, storm drain pipes, and pressure regulating valves. The following facility types were also recently included as part of Phase I facilities data: Library, Police, Park & Recreation buildings, and Fire-Rescue. The AMD is responsible for providing and updating their asset data in the system.

The Outlook includes a request of approximately $5.7 million from the Department of Information Technology (IT) for implementation of EAM Phase II to the following departments: Police, Environmental Services, Library, Information Technology, Fire, and Parks & Recreation which would allow for additional asset types to be added to the system. The funds will also be used to support system updates that each new department will bring to the EAM solution. This includes several systematic updates including but not limited to the interfacing of the remaining systems and integration with external systems such as Get-It-Done. The Department of IT has noted that they will work with management from each of the participating departments in developing a project schedule, milestones, and identifying resource needs consistent with City standards as the additional departments make the transition to the EAM system. The sequence in which the remaining departments will rollout into Phase II will be dependent upon the need for EAM to replace the pre-existing legacy systems which would eventually need to be upgraded to ensure that they are secure for cyber security purposes.

These requests indicate that the system may require supplementary support if the rollout of EAM continues into Phase II. This may include additional FTE or consultant support for each individual department to handle EAM related tasks and maintenance which should be taken into consideration. Phase I is also in a support period with the Department of IT providing minor enhancement and fixes to the system for the participating departments as needed. If Phase II is not funded, the remaining departments not included in the system would continue to use the existing asset maintenance and management systems and the financial information integrated into these systems may not be readily available for future planning purposes. Should there be interest in expanding the use of the EAM system, Council could consider delaying funding for this until a concrete outline is created establishing a timeline for each of the remaining departments projected to be in the system.

Library: New Branch Library (Pacific Highlands Ranch)
The Outlook identifies 9.50 FTEs and approximately $854,000 in new ongoing annual operational costs for the Pacific Highlands Ranch branch library which is currently anticipated to open in FY 2022. Leading up to the completion of construction, the Outlook attempts to best match the need for the positions with the anticipated opening date of February 2022. In FY 2021, 2.00 FTEs and $206,000 are assumed in preparation for the branch opening, with full staffing (9.50 FTEs) and $554,045 in FY 2022. Thereafter, $854,000 in expenses are projected for the first full year of operations and beyond. This library is included in the list of General Fund facilities anticipated to open or become operational within the Outlook period that is attached to this report.

Parks & Recreation: New Parks and Joint Use Agreements
The Department expects 14 new/expanded parks to open, and 24 new Joint Use Agreements (Agreements) with local school districts, to become effective during the Outlook period[3]. The Outlook projects expenses for the new parks and the Agreements to be approximately $6.2 million in FY 2021 and increasing to an aggregate expense of approximately $7.0 million in FY 2025 once all the new parks and Agreements have come on-line. The projected operating costs include the addition of 60.82 FTEs throughout the Outlook period to maintain the new parks and playgrounds. The positions include the addition of 21.00 FTEs in FY 2021 of which 17.00 FTEs consist of various citywide park maintenance staff (e.g., Grounds Maintenance Workers, Swimming Pool Managers, Equipment Operators, etc.) given the new park openings. The remaining positions include:

- 1.00 Program Manager to manage the Department's Capital Improvements Program (CIP), this position is anticipated to be CIP reimbursable,
- 1.00 Program Manager intended to bring New Facilities forward and ensure the timely progression of parks improvement projects,
- 1.00 Associate Management Analyst to assist with the Department's CIP, as well as manage its grant portfolio and apply for new grants, and
- 1.00 Payroll Specialist to support the addition of new staff.

In conducting our review, we note that variances were found relating to FY 2022 and FY 2023 expenses due to the double accounting of certain costs which over stated total costs in these fiscal years in the Outlook by $243,000 and $57,000, respectively. These variances are reflected in the table below.

Parks & Recreation: New Facilities					
	FY 2021	**FY 2022**	**FY 2023**	**FY 2024**	**FY 2025**
Outlook	$ 6,173,222	$ 6,926,913	$ 7,010,925	$ 7,063,646	$ 7,027,646
Corrected	6,173,222	6,684,320	6,954,241	7,063,646	7,027,646
Variance	**$ -**	**$ 242,593**	**$ 56,684**	**$ -**	**$ -**

[3] The Outlook incorrectly states that the number of new parks (16) and Joint Use Agreements (28).

Detailed expenses for each facility anticipated to open or become operational within the Outlook period are attached to this report.

Police: Addition of Sworn Positions
The Outlook includes the addition of 85.00 FTE sworn officer positions over the Outlook period, including 21.00 FTEs per year in FY 2022 through FY 2024, and an additional 22.00 FTEs in FY 2025. These additions are intended to increase the total number of budgeted sworn officer, from the current level of 2,043 FTEs up to 2,128 FTEs, which was the sworn staffing level maintained in 2009. This staffing goal has previously been referred to as the Police Department's "Five-Year Plan" which was first presented to Council in FY 2013. Since that time, the Department has not significantly increased its budgeted number of sworn positions, and instead has focused on filling its existing positions. While the Outlook projects the need for added positions beginning in FY 2022, the Department has indicated that it does not anticipate a need for new positions until an appropriate number of existing vacancies have been filled. As of November 18, 2019, the Department had 1,864 of 2,043 budget sworn positions filled (175 vacancies).

Addition of Sworn Positions					
	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
FTEs per year	-	21.00	21.00	21.00	22.00
Cumulative FTEs	-	21.00	42.00	63.00	85.00
Total Expense	**$ -**	**$ 3,465,444**	**$ 6,479,301**	**$9,493,158**	**$12,672,037**

Sustainability: Climate Action Plan
The Outlook's Critical Strategic Expenditures include two items related to the Climate Action Plan (CAP), one for climate adaptation and resiliency support and another to further general CAP implementation.

The first item totals approximately $443,000 and 1.00 FTE for climate adaptation and resiliency support. This item was funded on a one-time basis in FY 2020 for $300,000. These expenditures will support the ongoing implementation of the City's Resiliency Plan. Previously, the Department had indicated that they would be potentially seeking grants for this purpose.

The second item includes approximately $358,000 for CAP implementation. This includes the addition of 1.00 FTE ($108,000), which will be a transportation/mobility equity specialist that will specifically monitor the CAP's mobility strategy as well as work to bring more transportation opportunities to communities of concern.

The additional $250,000 in non-personnel funding is included for surveys, consulting, and other specialized analysis to update the CAP and enhance the City's climate equity reporting and monitoring. This funding would be in addition to the $100,000 for this purpose which was included in the FY 2020 Adopted Budget.

Transportation & Storm Water: Pipe Repair Teams
The Outlook includes funding for a pipe repair team, including 24.00 FTEs and $5.7 million in ongoing operating expenditures beginning in FY 2021, with an additional $1.3 million in one-time costs in FY 2021. This in-house pipe repair team was recommended in the June 2018 audit for the

Storm Water Division. Funding this team would also be a major step towards meeting the full operational needs for the Storm Water Division, as outlined in the Watershed Asset Management Plan. However, there is a $6.7 million operating funding gap in FY 2021 for storm water. There is more detail on the future financial challenges related to storm water later in this report.

Our Office would also note that this item also includes approximately $3.8 million worth of revenue in each year of the Outlook for the pipe repair teams. This revenue would be generated when the repair teams do capital-related work, and thus would be derived from the CIP. However, the most recent Capital Outlook did not contain this level of support for drainage and other storm water projects. Thus, in order for these teams to generate this level of revenue support, additional funding may be required in the CIP.

Transportation & Storm Water: Sidewalk Repair and Replacement Teams
The Outlook includes funding, under the Critical Strategic Expenditures, to support sidewalk repair and replacement teams. This includes a total of 23.00 FTEs (21.00 in FY 2021, with the additional 2.00 in FY 2022) and ongoing costs of $2.9 million, beginning in FY 2021. There are also one-time costs of $1.6 million included in FY 2021. According to the Department, the City has received an average increase of approximately 40% in customer generated sidewalk repair requests through FY 2019 since the implementation of the Get-It-Done application. This has impacted the amount of time it has taken the Department to address reported sidewalk hazards. In FY 2019, the average time was approximately 50 days, with a target of 20 days.

The request is composed of various items, the largest of which is a 13-person concrete crew, which would perform new sidewalk installations and other maintenance. This includes $991,000 of personnel costs as well as one-time startup costs of $1.4 million. This crew would receive 50% offsetting revenue for the installations of new sidewalks. Additionally, the item also includes 2.00 FTEs and related vehicles to address the increase in sidewalk ramping requests and to mitigate sidewalk deficiencies efficiently. This would cost $537,000 in FY 2021, with ongoing costs of $292,000.

The request would also add $1.1 million to execute and manage a new sidewalk slicing contract, as well as 3.00 FTEs and $403,000 to manage the work. Finally, it is anticipated that the increased repairs would also result in an increase in Notice of Liability issuances and cost share participation. 2.00 FTEs and $137,000 are thus added in FY 2022 in order to keep up with the demand.

PRIORITIZATION OF CRITICAL STRATEGIC EXPENDITURES

Our report breaks the Critical Strategic Expenditures into three categories to emphasize that a majority of the funding is necessary to continue existing popular programs beyond FY 2020. Typically, expenditures for continuing existing programs and services would be accounted for within the Baseline Expenditures. However, as noted in the previous section, in FY 2020 $36.5 million in existing priority services, which are intended to be ongoing throughout the Outlook, were funded with one-time General Funds or other one-time funding sources. These services include CleanSD, Neighborhood Policing, temporary bridge shelters, transition storage facilities, and the Safe Parking Program. The General Fund one-time costs were appropriately removed from the FY 2021 Baseline and moved to Critical Strategic Expenditures, as new funding must be identified for these important services to continue beyond FY 2020. An additional $7.9 million is also required to replace existing systems and equipment to maintain existing department service levels.

Critical Strategic Expenditures are generally funding proposals for desired new or expanded services, and funding is considered based on the criticality of need and the availability of funding. Over $30.0 million of the FY 2021 expenditure proposals in this year's Outlook is needed just to continue existing critical homelessness and public safety programs. These programs are of utmost importance to the community and to those who are benefiting from their services. Additionally, significant investments have been made in their implementation with the intention of these programs being sustained in the future. Identifying ongoing funding to continue these services should be the highest priority for funding over new or expanded programs.

Identifying ongoing funding to continue existing homelessness and public safety programs should be the highest priority over new or expanded programs.

The third category of Critical Expenditures in the Outlook, which totals $18.2 million, is proposed for new or enhanced services such as Phase II of EAM, peak hour fire engines, the climate action plan, operational costs for new parks and recreation facilities, sidewalk replacement, street resurfacing, and storm water pipe repair, and will need to be prioritized amongst the funding needed to continue existing homelessness and public safety programs. Capital funds may be available for streets, sidewalks and pipe repairs. Other new/expanded programs may need to be reconsidered, reduced or delayed to help ensure that other existing, essential services, as discussed above, are maintained.

POTENTIAL FUTURE FUNDING NEEDS NOT INCLUDED IN THE OUTLOOK

Potential Future Funding Needs Not Included in Outlook
• Companion Unit Fee Waiver • Impacts from AB 939 Fee Increases • Fleet Repair Facility Needs • Homeless Programs & Services • Infrastructure Condition Assessments • Potential New Disparity Program • Facility Maintenance Needs

Citywide Program Expenditures: Companion Unit Fee Waiver

The FY 2020 Adopted Budget included $800,000 in one-time funds for the Companion Unit Fee Waiver Program which is not included the Outlook. The funding for this program is utilized to reimburse the Public Utilities Department for water and sewer capacity fees that cannot be waived and that otherwise would need to be paid by companion unit permittees, should the program not be continued. We note that this has been a popular program; as of November 8, 2019, the full $800,000 waiver allowance for FY 2020 has been spent down less than half way through the fiscal year. This has translated to more than 200 units benefitting from the program.

The Companion Unit Fee Waiver is a popular existing program. As of November 2019, the full $800,000 waiver allocation for FY 2020 has been spent, in the first four months.

Environmental Services: General Fund Impacts from AB 939 Fee Increases
In July 2019, the City Council approved new contracts for the processing and marketing of residential curbside recyclable materials. Historically, the City had received net revenues under past contracts for these services; however, given the impact China's National Sword Policy has had on the recyclables market, the new contracts now require payment from the City's Recycling Fund in order to process, market, and ultimately find a destination for these materials. Estimated costs under the new contract over the Outlook period ranges from $4.6 million in FY 2021 to $7.1 million in FY 2025. To support these costs to the Recycling Fund, the Department anticipates seeking AB 939 fee increases of $2 per ton in FY 2021 and an additional $2 per ton in FY 2022. Each $2 per ton rate increase would generate an additional $2.8 million in revenue. Given that the City collects more than 300,000 tons of materials annually that are subject to AB 939 fees, the impact to the General Fund would be increased costs of $600,000 in FY 2021 and an additional $600,000 in FY 2022 on an ongoing basis. These additional General Fund costs are not included in the Outlook.

Fleet: Kearny Mesa Repair Facility and Other Facility Needs
The FY 2020 Adopted Budget includes $1.0 million for design and permitting of the Kearny Mesa Repair Facility (CIP project P20000) on Othello Avenue which is being converted to a fire fleet repair facility. Additional funding will be needed in FY 2021 for construction; however, a cost estimate is not available. Previous cost estimates ranged from $6.5 to 17.0 million. In addition, the Fleet Department has requested funding for replacement and/or repairs of the City's car and truck washes ($4.0 million from the General Fund for FY 2021). They also requested funding for capital deferred maintenance and replacement of obsolete or inoperable shop equipment at various repair facilities, including repairing roofs, roll-up doors, shop floors and replacing damaged/missing rain gutters ($3.6 million from the General Fund over five years).

Because these are all capital repairs, the Department of Finance indicated that these items will be evaluated for inclusion in the FY 2021-2025 Five-Year Capital Infrastructure Planning Outlook. However, it should be noted that barring an outside funding source, Fleet facility needs are funded by the Fleet Operations Operating Fund, which is approximately 72% supported by the General Fund. The car washes and deferred maintenance alone could cost the General Fund $7.6 million over the next five years and the estimate for the Kearny Mesa Repair Facility is still unknown.

Homeless Programs and Services

<u>Expansion of Women and Families Shelter</u>
The Outlook includes funding needs for the existing four bridge shelters. However, on November 15, 2019 the San Diego Housing Commission recommended that on December 10, 2019 Council and the Housing Authority approve an expansion of the Women and Families Shelter by 138 beds to also serve transitionally aged youth. If approved, an additional $1.9 million will be needed to continue this expansion beyond FY 2020, which is not included in the Outlook. A request was submitted for the Outlook, but it is being deferred for consideration in the budget process.

We note that staff is recommending to partially fund the shelter expansion in FY 2020 with anticipated savings of $951,000 in ongoing General Funds coming from funds budgeted for equipment rented for the existing Bride Shelter Program. Use of ongoing General Funds would decrease the funding needed to support the shelter expansion on an ongoing basis to $926,000.

Critical Strategic Expenditures Related to HEAP Programs

As reflected in the Outlook, many programs funded by HEAP have funding needs beginning in FY 2022, instead of FY 2021 due to projected carry forward budgets. However, according to updated HEAP expenditure projections, our Office has learned that several of these programs have funding gaps in FY 2021 which was not anticipated at the time the Outlook was developed.

If current HEAP projections hold, and the shelter expansion is approved, these costs would add to the list of Critical Strategic Expenditures needed to maintain current programs in FY 2021 as reflected on the table on page 15 titled "Mayor's FY 2021 Critical Strategic Expenditures". The table below provides a summary of funding needed *in addition* to what is reflected in the Outlook for homelessness Critical Strategic Expenditures, as well as deferred requests. These funding needs will be reviewed during the budget process.

Summary of Homelessness Program Funding Needs not Included in the Outlook		
Program	**FY 2021**	**Ongoing**
Critical Strategic Expenditures		
Family Reunification	$ 450,000	$ 225,000
Safe Parking (Aero Dr. & Balboa Ave.)	411,000	-
Housing Commission Diversion	170,000	-
PLEADS[1]	100,000	-
Landlord Engagement	80,000	-
Think Dignity Storage Facility	35,000	-
Total	**$ 1,246,000**	**$ 225,000**
Requests Deferred to Budget Process		
Women and Families Shelter Expansion[2]	1,877,000	1,877,000
Homelessness Strategies Personnel (5)	649,000	649,000
Flexible Spending Pool	-	1,000,000
Total	**$ 2,526,000**	**$ 3,526,000**

[1] Prosecution and Law Enforcement Assisted Diversion Services criminal diversion program

[2] If Council approves the shelter expansion on December 10, 2019, continued use of $951,000 in the General Fund would offset the ongoing need for this program.

Infrastructure: Condition Assessments

In this year's Outlook, condition assessments are not included as a Critical Strategic Expenditure as they were in last year's report. Transportation & Storm Water requested $1.5 million in FY 2021 for a pavement condition assessment to assess the results of the City's significant investment in street repair and to update its inventory of other right-of-way assets. Facilities requested $250,000 in FY 2021 for a facilities condition assessment for facilities that were not captured in the condition assessments conducted from FY 2014 to FY 2016.

Purchasing and Contracting: Potential New Disparity Program
The disparity study is fully funded in FY 2020 for analysis of diversity in the City's contracting for services, goods, consulting and public works projects. Should any disparities be identified, the study will include recommendations on how to remediate those gaps. At this time, it is unknown if a new program would be needed to address any diversity gaps or what a program might cost. In addition, a disparity study would need to be conducted every two to three years to support an ongoing program. These potential yet unknown costs are not included in the Outlook.

Real Estate Assets–Facility Maintenance
Facilities submitted requests for the following items that were included in last year's Outlook but not included in the FY 2020 Adopted Budget or this year's Outlook:

- Support to maintain emergency generators for Fire, Police, and Communications ($194,000, of which $95,000 is one-time), and
- Rehabilitation projects ($700,000 annually).

Though Facilities staff does not have a list of specific facilities that need rehabilitation, they indicate that the types of projects would include HVAC replacements, plumbing replacements, and smaller renovations. These items will be considered further during the budget process.

FUTURE FINANCIAL CHALLENGES

Future Financial Challenges
• Future MOUs with Employee Organizations • General Fund Infrastructure Shortfall • Homeless Programs & Services • Pension Issues • Deficits Impact Existing Programs & Services • Recession • Storm Water • Vacancies, Attrition & Recruitment

Future MOUs With Employee Organizations
MOUs for the six City employee organizations run through FY 2020; and FY 2021 contract negotiations are currently underway. The Outlook does not contain estimates for any potential new negotiated compensation increases for FY 2021 (and through the remainder of the Outlook). The Department of Finance estimates a 1% salary increase for City employees would be about $6.0 million for the General Fund, which is not considered in the Outlook.

General Fund Infrastructure Shortfall
The most recent Five-Year Capital Infrastructure Planning Outlook released January 2019 identified a $1.86 billion funding gap between capital needs and anticipated funding sources available for FY 2020 through FY 2024. The gap is attributed to City assets that do not have a dedicated funding source. The greatest contributor to the funding gap is storm water, accounting for 38.7%.

The funding shortfall is in addition to the $270 million commercial paper borrowing plan which was authorized in FY 2018 and continues through FY 2025 to address General Fund capital needs. The Outlook assumes the City will issue an average of $44.4 million in commercial paper per year to reach $270 million by FY 2025. However, we believe it will be difficult to spend proceeds at this pace when only $15.9 million was borrowed in FY 2019. As previously discussed in our report, our Office believes that a critical part of any plan to identify additional revenue to mitigate the

$1.86 billion shortfall is to improve the City's ability to efficiently spend existing funding sources. This likely requires improved prioritization based on readiness to spend on project needs.

Homeless Programs and Services

The City continues to struggle to identify ongoing resources to support its recent expansion of homelessness efforts. However, this year's Outlook appropriately reflects the funding needs to continue these programs. Stable funding is a critical component of successfully implementing the recently adopted Community Action Plan on Homelessness. As the City may be faced with a recession in coming years, we caution the City further expanding homelessness programs and services with one-time resources unless they are intended to be temporary or there is a future ongoing funding plan.

In addition to funding existing programs, the City will work to address recommendations included in Community Action Plan on Homelessness adopted by City Council on October 14, 2019. Specifically, it recommends a $1.94 billion investment over ten years in permanent solutions to homelessness such as supportive housing with services, rental assistance, and diverting households from homelessness. It also recommends a limited increase in temporary crisis response solutions, such as shelter beds, to meet immediate needs of unsheltered individuals.

In the short term, one of the most important immediate actions identified by the plan is to establish a Leadership Council that allows for cross-agency collaboration and planning between the City, San Diego Housing Commission, the Regional Task Force on the Homeless, and the County. The composition of the Leadership Council was communicated to Council via memorandum dated November 15, 2019. The plan recommends evaluating staff resources at each entity as soon as possible so that adequate resources can be provided to ensure that the plan is implemented. Our Office anticipates related requests to be considered during the upcoming budget process.

A discussion on possible revenue options that could support these financial challenges are included under the "Mitigation Measures" section of this report.

Pension Issues

<u>Future Defined Benefit Pension Payments</u>

Any substantial increases to the City's defined benefit pension payment, or ADC, would negatively impact the Outlook. For example, a significant stock market correction is possible in the next five years. In such a case, if investment earnings are significantly lower than assumed in the actuarial valuation, future ADCs could be increased.

There is also the possibility of changes in assumptions used to produce the actuarial valuation. For an example of a potential assumption change, the SDCERS Board has previously discussed further reducing the discount rate assumption. Assumption changes are scheduled to be discussed with the "experience study" that includes the June 30, 2019 actuarial valuation (anticipated for the spring of 2020). Any assumption changes subsequently implemented in the FY 2020 valuation would impact the ADC for FY 2022.

Proposition B

Lastly, there are ongoing challenges to Proposition B, which was approved by voters in June 2012. Proposition B was challenged by four of the City's recognized employee organizations (Unions), alleging a violation of the Meyers-Milias-Brown Act (MMBA) – the State law that governs collective bargaining for public agency employers, like the City.

Heeding a related California Supreme Court decision on August 2, 2018, the California Court of Appeal directed the City "to meet and confer over the effects of the [Proposition B] Initiative and to pay the affected current and former employees represented by the Unions the difference, plus seven percent annual interest, between the compensation, including retirement benefits, the employees would have received before the Initiative became effective and the compensation the employees received after the Initiative became effective." Additionally, the City is ordered "to cease and desist from refusing to meet and confer with the Unions and, instead, to meet and confer with the Unions upon the Unions' request before placing a charter amendment on the ballot that is advanced by the City and affects employee pension benefits and/or other negotiable subjects."

However, despite the Court of Appeal directives, Proposition B is still part of the San Diego City Charter. To remove Proposition B from the City Charter, the Unions have pursued a *quo warranto* process. The State Attorney General granted authority for the Unions to sue on August 15, 2019; and the complaint in *quo warranto* was filed on September 27, 2019. Pursuant to Council direction, on November 18, 2019 the City Attorney's Office response to the Unions' complaint in *quo warranto* included language supporting a judgement that invalidates and removes Proposition B amendments from the City Charter.

The ultimate cost for resolution of the Proposition B legal challenges is dependent upon the pending negotiations with the Unions and compliance with federal tax laws and regulations with respect to retirement plans. The issues are not expected to be resolved for several years.

Projected Deficits Could Impact Existing Priority Programs and Services

The Outlook includes two components, the Baseline projection and the Critical Strategic Expenditures. The FY 2021 Baseline projection, which includes staffing, program, and service levels existing at FY 2020 is showing a deficit of $21.2 million. Adding, $62.5 million in Critical Strategic Expenditures yields a total FY 2021 projected deficit of $83.7 million.

There are a number of Critical Strategic Expenditures that are currently existing services, funded in FY 2020 as one-time expenditures, the largest of which include:

- Homeless Programs and Services ($18.5 million largely funded by the Housing Commission),
- CleanSD expansion ($6.5 million, including $3.5 million for Police overtime),
- Additional neighborhood policing ($4.3 million, of which $3.9 million is budgeted in the Seized Assets Fund), and
- Commission for Arts & Culture Funding ($3.9 million).

Further, there are new FY 2021 Critical Strategic Expenditures needed to maintain existing service levels, such as:

- Vehicle replacements ($4.3 million),
- Public safety radio replacements and related service contracts ($2.6 million), and
- Smart Streetlights Program ($2.3 million).

Based on the Outlook projections, in the absence of any ***new*** programs and services, the continuation of these existing programs would yield a deficit in both FY 2021 and FY 2022. In FY 2023, increases in projected revenues overtake the portion of the Outlook deficit that relates to existing services.

Potential Impacts of a Recession

The Outlook does not account for the potential impacts of a recession, which are difficult to predict. However, for the purposes of discussion, our Office has prepared a scenario that is presented in the Review of Baseline General Fund Revenues section earlier in this report. We analyzed the three major revenue sources: property tax, sales tax and Transient Occupancy Tax and provide a projection that could increase the shortfall by $34.6 million in FY 2021 and continuing to increase the gap each year after. Please see the Recession Analysis section earlier in this report.

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

Storm Water

In May 2013, the San Diego Regional Water Quality Control Board (Regional Board) adopted a new municipal storm water permit for San Diego. That permit mandates strict storm water quality requirements, and compliance with that permit will require significant increases in funding. The Transportation and Storm Water Department completed a Watershed Asset Management Plan (WAMP) in 2014 that notes activities and projects necessary to support flood risk management activities and compliance with the Regional Board's storm water permit. The WAMP, which was recently updated in October 2018, projects that funding needs total $3.1 billion through FY 2035. Penalties for not complying with storm water permits and requirements are up to $10,000 per day per violation.

Storm water permit compliance efforts have significant operational and capital needs which are higher compared to current spending levels. The FY 2020 Adopted Budget included a total of $52.0 million for storm water efforts. While the Outlook includes 24.00 new FTE positions and $5.7 million in expenses for increased storm drain pipe maintenance and repair, other significant projected storm water needs that are identified in the WAMP were not included in the Outlook's Baseline or included as Critical Strategic Expenditures. The table on the following page shows total operational needs of $53.3 million over the five-year period, above the FY 2020 base budget that are not included in the Outlook.

The majority of the projected storm water needs requested by the department and identified in the WAMP, including $53.3 million of operating needs over five years, are not included in the Outlook.

Projected Operating Costs to Meet Permit Compliance (in millions)					
	FY 2021	**FY 2022**	**FY 2023**	**FY 2024**	**FY 2025**
Operations/Maintenance[1]	$ 6.7	$ 15.3	$ 12.3	$ 9.6	$ 9.4

[1] Reflects necessary operating expenditures identified in the WAMP, net of the Storm Water Division's FY 2021 base budget ($51.5 million) and storm water related Critical

For capital needs, the Outlook notes that storm water flood risk management and water quality improvement projects have been identified, but the Outlook itself neither details those needs nor includes any of the projected costs for those needs. They are expected to be discussed in the Five-Year Infrastructure Planning Outlook, which staff plans to release in January 2020.

While future deferred capital bonds and commercial paper issuances may support some of the capital needs, they will not be sufficient to meet all storm water capital costs identified in the WAMP and other City CIP needs. The City continues to lack a dedicated funding source that provides revenues sufficient to address all storm water permit and mandate needs.

The City does have a Storm Drain Fee that is paid by water and sewer users. That fee collects 95 cents per month from single family residences and $0.0647 per hundred cubic feet of water use from multi-family and commercial water customers. In total, that fee brings in approximately $5.7 million per year.[4]

The Storm Water Fee rates have remained unchanged since the passage and implementation of California Proposition 218 in 1996. Proposition 218 allowed local governments to adjust water, sewer, and trash fees through a vote of the local legislative body (in the City of San Diego, this body is the City Council), but required other fee increases to be put to a public vote. This had the effect of making any increase in the storm drain fee subject to a two-thirds vote of City voters in a city-wide election, or majority vote of City property owners in a mail-out election. As the City became subject to increasingly stringent storm water quality mandates and permits, Proposition 218 has constrained its ability to adjust its Storm Drain Fee to compensate for those increased costs.

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[4] San Diego's storm drain fee is low compared to other coastal cities; Los Angeles' corresponding fee is $2.25 per month; Santa Cruz's is $9.08 per month; Santa Monica's is $7.25 per month.

However, various jurisdictions have been able to increase their storm water fees through the Proposition 218 process. In 2018, the City of Berkeley increased the storm water fee by $3.57 per month per customer through the mail-out election process, while Los Angeles County passed a parcel tax of 2.5 cents per acre of impervious surface through a general election vote, which will flow though property tax bills and generate an increase of approximately $6.92 per month per property owner. The City of Del Mar is also currently considering an increase through the mail-out election process which would increase the fee by approximately $2.00 per month, from $18.64 to $20.64, for the average single-family residence.

In 2017, the California Legislature passed SB 231, which clarified the interpretation of Proposition 218 to include storm drains and storm water systems under the overall definition of sewers, and thereby allows local governing bodies to adjust storm water and storm drain fees without putting the issue to a public vote. An increase of $1.00 per parcel per month would generate an additional $6 million per year; as an example, an increase in the fee to $5.00 per parcel per month would generate an additional $30 million per year to fund storm water needs.

Vacancies, Attrition, and Recruitment

As discussed in the General Fund Baseline section of this report, budgeted vacancy savings has been significantly lower than the actual vacancy savings which accumulates over a fiscal year. For FY 2019 there was $22.2 million in additional vacancy savings above the budgeted $33.2 million, for a total vacancy savings of $55.4 million. This is a continuation of a trend that has been discussed over the past several years. Causes and effects of such additional vacancy savings, for example hiring difficulties and staffing level deficiencies, have been discussed by Council. In December, the City Auditor's Office plans to release part one of a two-part report on human capital management, which will address some of these issues; and a Request for Proposal has been released related to a pay equity study, which may have some bearing. Additionally, the City intends to explore these issues via a working group, at the request of the Budget and Government Efficiency Committee.

POTENTIAL MITIGATION MEASURES

Potential Mitigation Measures
• General Fund Excess Equity
• 4% Budget Reductions
• Pension Payment Stabilization Reserve
• Alternative Housing/Homelessness Funding
• Stadium Revenue – Sale to SDSU
• March Ballot Measure
• RPTTF Lawsuit
• Storm Water Fee Increase
• People's Ordinance – Paid Refuse Collection

General Fund Excess Equity

The City could consider the use of any available Excess Equity for FY 2021 one-time needs. The amount that may be available is uncertain because the current $22.1 million estimate is not based on comprehensive projections for FY 2020, but rather the FY 2020 Adopted Budget amounts. The FY 2020 projections that will be included in the Mid-Year Report (expected to be released at the end of January 2020) will provide a more updated sense of potentially available FY 2020 Excess Equity.

4% Budget Reduction Proposals

In November 2019, the Chief Operating Officer released a memorandum directing departments to submit 4% budget reduction proposals as part of the FY 2021 budget development process. The memoranda further noted that departments "are required to **suspend all nonessential discretionary expenditures in Fiscal Year 2020**". At present, it is likely that not all department reductions submitted will be accepted and implemented due to potential operational impacts. The adopted budgets over the past three fiscal years (FY 2018, 2019 and 2020) include a total of $45.7 million in similar departmental reductions, making the potential for operational impacts more of a concern. We note several other options to address shortfalls in the discussion that follows.

Pension Payment Stabilization Reserve

The General Fund portion of the Pension Payment Stabilization Reserve (PPSR) is scheduled to reach $7.9 million in FY 2020.[5] The Outlook proposes to add $4.5 million, $4.7 million, and $4.3 million in FY 2021, FY 2022, and FY 2023, respectively, at which point the General Fund portion of the PPSR is expected to be fully funded at $21.4 million, in accordance with the City's Reserve Policy (Council Policy 100-20).

To assist with the deficit and help maintain existing services, consideration could be given to using $3.8 million of the FY 2021 $4.5 million PPSR contribution to cover the estimated General Fund increase in the City's FY 2021 ADC which is consistent with the City's Reserve Policy. Per the Policy, the intent of the PPSR is to "mitigate service delivery risk due to increases in the annual pension payment", or ADC. The Policy also states that the purpose of the PPSR is to provide a source of funding for the ADC when the ADC has increased year over year. The FY 2020 General Fund portion of the ADC was $264.8 million, while the FY 2021 amount is projected to be $268.6 million, an increase of $3.8 million year over year. This action would free up $3.8 million in one-time General Fund monies which could be used to help maintain critical services.

Alternative Housing and Homelessness Funding

As discussed earlier in this report, the Outlook identified $18.8 million in FY 2021, and $22.2 million in each year thereafter that is needed to continue existing homelessness programs for which a dedicated funding source has not been identified. In the sections below, we describe one-time and ongoing sources that will be available to the City that could temporarily address, or mitigate these funding needs, while also pointing out associated tradeoffs. Aside from those described below, an additional potential new ongoing revenue source for homelessness could become available which is discussed in our section entitled "March Ballot Measure".

<u>Homeless Housing, Assistance, and Prevention Program (HHAP) – Estimated $20 million one-time</u>

The Outlook identifies HHAP as a one-time revenue source to offset homeless program costs. HHAP was approved in the state budget for FY 2020 and provides jurisdictions funding to support regional coordination and expand or develop local capacity to address immediate homelessness challenges. The City is estimated to receive $20 million, but funding estimates are not yet finalized. We note that though this is a significant investment, it is one-time funding.

HHAP funds can be used to support many of the programs reflected in the Critical Strategic Expenditures for homelessness. A Notice of Funding Availability (NOFA) is expected to be released by December 2019 with applications for funding due February 15, 2020. Council will be

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[5] The General Fund PPSR contribution for FY 2019 ($3.6 million) and planned contribution for FY 2020 ($4.3 million) total $7.9 million.

asked to approve allocations. Awards are expected to be made by April 1, 2020 and funds must be fully spent by June 2025.

Building Homes and Jobs Act – Estimated $4.6 million ongoing
In 2017, Governor Brown signed Senate Bill 2 which created the Building Homes and Jobs Act establishing a $75 recording fee on real estate documents. In the first year of funding, planning grants were made available to local governments to streamline housing production, in which the City received $625,000. Beginning January 2019 and going forward, local governments will receive 70% of revenue collected through the Permanent Local Housing Allocation, creating an ongoing funding source to address unmet housing needs.

Preliminary estimates indicate that the City will receive $4.6 million, with future allocations likely to fluctuate. However, 20% of funding received statewide must go towards affordable owner-occupied workforce housing. Though not required of each jurisdiction, if the City provides 20% for purpose, about $3.7 million would be available for other eligible activities. These include: increasing the supply of affordable housing for lower- and moderate-income households and to support those who are homeless or at-risk of being homelessness through new or existing activities, such as emergency shelters. Though this funding could mitigate several of the homelessness Critical Strategic Expenditures on an ongoing basis, the tradeoff would be less funding available to increase the affordable housing stock.

The state is expected to issue a NOFA in February 2020 which will include the allocations for which local governments are eligible. Council must approve a five-year plan describing how funds will be used and submit it within the City's application. Awards are expected to be made beginning August 2020.

Affordable Housing Fund – $4.1 million one-time
On June 10, 2019 Council approved the FY 2020 Affordable Housing Fund Annual Plan. At that time, our Office highlighted that $4.1 million was not budgeted for any purpose since it is program income restricted for use on old programs that, according to the San Diego Housing Commission, ended between 1992 and 1997. To free up funds to support current priorities, the Commission would need to seek Council approval. These one-time funds could be used to support homelessness Critical Strategic Expenditures such as: the Bridge Shelter Program; rapid rehousing, landlord engagement, homelessness prevention and diversion, and family reunification. We note that this presents a tradeoff in that funds could also be used to increase the supply of affordable housing.

Stadium Revenue – Implications for Sale to SDSU
As previously mentioned in this report, the Outlook does not include any revenue or expenditure assumptions that consider the City's current negotiations with San Diego State University (SDSU) for the sale of the SDCCU Stadium site, per the terms of Measure G. The Outlook, as currently constructed, assumes that operations would continue at the stadium through the end of the current operating lease with SDSU, which expires in December 2020. Following the expiration of that lease, the stadium would then be shuttered, and only ongoing security services costs of approximately $600,000, as well as the remaining debt service payments of approximately $4.0 million, would be paid from the TOT Fund for special promotions and tourism related activities.

On November 18, the City Council considered an offer to purchase the site from SDSU, and during that meeting directed the City Attorney and Mayoral Staff to develop a Purchase and Sale Agreement (PSA) that incorporated most of the deal points contained in the updated offer. Should the PSA be finalized and the property close within the timeframe outlined by SDSU (they set a preferred closing date of March 27, 2020), the City could realize both a significant inflow of one-time revenue as well as realize significant operating cost savings from the deal. For more detail on the offer itself, please refer to IBA Report No. 19-27 "Analysis of the Updated Offer for the SDCCU Stadium Site in Mission Valley."

As stated in the offer, SDSU would seek to close on the property by March 2020. However, even if the full transaction is not able to close by that date, there is another component of the offer that states that SDSU would seek to lease the property, beginning July 1, 2020, until the offer does come to a close. Assuming that the PSA and this lease provision are approved prior to the end of FY 2020, the City would no longer have to pay ongoing operating costs for the stadium beginning in FY 2021. This would result in an immediate savings to the General Fund of $7.6 million in FY 2021 and $3.2 million in FY 2022. These savings would backfill reimbursements from the TOT Fund to the General Fund that were covered by one-time revenue in FY 2020. After FY 2022, additional savings from stadium operations would accrue to the TOT Fund balance.

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

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

If the stadium deal does close by March 2020, or even prior to July 1, 2020, then based on the purchase price offered the Capital Outlay Fund would receive $47.3 million. One potential way to secure additional operating fund relief would be to set aside $29.2 million from the purchase price to repay the existing bonds on the stadium. This would reduce expenditures by $4.0 million per year, which could be used to offset additional tourism related costs supported by the General Fund, such as the Critical Strategic Expenditure for the restoration of Commission for Arts & Culture Funding.

March Ballot Measure

A ballot measure entitled "FOR A BETTER SAN DIEGO" will be on the March 3, 2020 ballot. If approved by City voters, this measure would increase the City's transient occupancy tax (TOT) to expand the Convention Center, address homelessness, and, beginning in FY 2025, fund road repairs.

Between FY 2021 and FY 2024, 41% of the resulting new tax proceeds would be used for a broad array of eligible expenditures to address homelessness in the City (the allocation drops to 31% beginning in FY 2025). It is estimated that $137 million of tax proceeds will be received to address homelessness over the Outlook period. Among other eligible expenditures, these tax proceeds could be used to fund any of the homeless programs or services currently being provided by the City and/or to address recommendations included in the recently adopted Community Action Plan on Homelessness.

Beginning in FY 2025, 10% of the resulting new tax proceeds would be used for a broad array of eligible street repairs and other street-related infrastructure. It is estimated that $8 million of tax proceeds will be received to address street repairs in the last year of the Outlook period (FY 2025).

Additionally, an expanded Convention Center is expected to attract additional visitors who will make taxable expenditures while visiting the City. It is estimated that these expenditures will increase General Fund tax revenue by approximate $10.0 to $15.0 million annually beginning in FY 2025 when the expanded Convention Center would be expected to open.

Redevelopment Property Tax Trust Fund (RPTTF) Lawsuit
The City could receive an estimated $35-40 million in revenue pending the outcome of the City of Chula Vista, et al. v. County of San Diego (Sandoval) lawsuit. Local cities are challenging how the County allocates the RPTTF. A ruling is expected sometime in 2020; however, even if the cities prevail, the timing of receiving payment would still need to be determined.

Storm Water Fee Increase
As we noted in the "Future Financial Challenges" section of this report, an increase to the City's Storm Drain Fee is an option that the City Council may wish to explore to help address storm water permit compliance funding needs. The amount of revenue that could be generated roughly equates to $6 million for each $1.00 (charged per parcel per month) the fee is increased. The City currently charges 95 cents per parcel per month.

People's Ordinance – Paid Refuse Collection
The People's Ordinance establishes the trash collection of single family homes as a responsibility of the City for no fee, but does not include multi-family homes. As a result, City residents that live in multi-family homes normally contract with a third-party collection service and pay for trash collection.

Providing refuse collection services to single family homes represents approximately $34.5 million in ongoing General Fund expenses to which no revenue is collected. In addition to this, $20.2 million is funded by the Recycling Fund for collection of recyclable materials. The City is the only large city to continue to provide free collection services to single family homes. Monthly fees charged by other large cities in California (top 10) for comparable services ranges between $23–132 per month. Given the City's current costs, the monthly charge to the roughly 285,000 single family home residents currently served would be approximately $16 per month.

Should the City wish to re-evaluate free collection service, the Department would be able to develop more detailed fee estimates based upon current and/or desired service levels. Transferring this cost to single family home residents would alleviate the General Fund of approximately $34.5 million in annual expenditures. The repeal of the People's Ordinance would require a simple majority approval by voters.

SUMMARY AND CONCLUSION

This year's Outlook identifies shortfalls in the first four years of the Outlook period after considering projected Baseline revenues and expenditures and the addition of the Mayor's Critical Strategic Expenditures. For FY 2021, the Outlook's projected deficit (after including Critical Strategic Expenditures) is $83.7 million. Our review of the Outlook analyzes and discusses the Baseline, Critical Strategic Expenditures, potential funding needs not included in the Outlook, and future financial challenges, and potential options to address identified shortfalls. In addition, we provide a recession scenario and discuss the potential impacts to City revenue projections.

The information provided in the Outlook, as well as in our review of the Outlook, allows the Council to begin identifying its top budget priorities and develop a strategy for achieving a balanced budget in FY 2021. In February 2020, the Council will adopt its City Council Budget Priorities Resolution which will provide early input for the Mayor's consideration regarding prioritization of various expenditures as well as mitigation strategies for ensuring a balanced budget.

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

- Some mitigating actions for addressing the deficit are available but are likely not sufficient.
- Funding for existing, unfunded priority services versus new, expanded services needs to be carefully prioritized.
- Efforts should be made to identify ongoing funding for maintaining unfunded existing priority services beyond FY 2020.
- Delaying or cutting back of proposed new/expanded services will likely need to be considered.
- Not considered in the Outlook are any estimates for potential FY 2021 compensation increases for employee organizations which are currently being negotiated.
- The timing of a potential recession is an unknown but should be kept in mind when making future expenditure decisions.
- Sources for new or increased ongoing revenues should be considered within the Outlook period.

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Attachment: New Facilities and Joint Use Agreement Annual Costs

NEW FACILITIES AND JOINT USE AGREEMENT ANNUAL COSTS

Fiscal Year 2021 Department	Facility	Location of Facility (District)	FTE	First Year Annual Expense
Park and Recreation	14th Street Promenade[1]	3	0.50	$71,027
Park and Recreation	Bay Terrace Recreation and Senior Center[1]	4	2.50	$214,050
Park and Recreation	Canon Street Pocket Park[1]	2	0.50	$52,060
Park and Recreation	Children's Park Enhancement[1]	3	0.50	$228,359
Park and Recreation	Franklin Ridge Pocket Park	7	0.00	$2,348
Park and Recreation	Harriet Tubman Charter Elementary Joint Use Agreement	9	0.50	$57,539
Park and Recreation	Hickman Elementary Joint Use Agreement[1]	6	0.50	$101,558
Park and Recreation	Johnson Elementary Joint Use Agreement[1]	4	0.50	$105,336
Park and Recreation	La Paz Mini Park	4	0.50	$52,965
Park and Recreation	Lafayette Elementary Joint Use Agreement[1]	6	0.50	$128,560
Park and Recreation	Marie Curie Elementary Joint Use Agreement[1]	1	0.50	$113,298
Park and Recreation	Pacific Beach Elementary School Joint Use Agreement[1]	2	0.50	$69,274
Park and Recreation	Rolando Park Elementary Joint Use Agreement	9	0.50	$64,231
Park and Recreation	Rowan Elementary Joint Use Agreement[1]	9	0.50	$101,814
Park and Recreation	Salk Neighborhood Park & Joint Use Development[1]	6	1.00	$215,773
Park and Recreation	Sequoia Elementary Joint Use Agreement[1]	6	0.50	$124,451
Park and Recreation	Standley Middle School Joint Use Agreement[1]	1	0.50	$82,305
Park and Recreation	Standley Middle (Pool) Joint Use Agreement	1	5.82	$378,691
Park and Recreation	Taft Middle Joint Use Agreement[1]	7	0.50	$125,038
Park and Recreation	Wangenheim Middle School Joint Use Agreement[1]	6	0.50	$108,602
Park and Recreation	Citywide Park Maintenance[1]	Citywide	17.00	$3,308,197
Park and Recreation	New Facility Administration Staff	Citywide	4.00	$620,544
Fire-Rescue	North University City Fire Station	1	9.00	$1,380,472
Total Fiscal Year 2021			**47.32**	**$7,706,485**

Fiscal Year 2022 Department	Facility	Location of Facility (District)	FTE	First Year Annual Expense
Park and Recreation	Benchley / Weinberger Elementary Joint Use Agreement[1]	7	0.50	$96,275
Park and Recreation	Dennery Ranch Neighborhood Park[1]	8	1.50	$270,540
Park and Recreation	East Village Green[1]	3	7.5	$1,327,441
Park and Recreation	Fairbrook Neighborhood Park[1]	5	0.50	$83,992
Park and Recreation	Hawthorne Elementary Joint Use Agreement[1]	6	0.50	$109,189
Park and Recreation	Jones Elementary Joint Use Agreement[1]	7	0.50	$114,472
Park and Recreation	King Chavez Elementary Joint Use Agreement	8	0.50	$62,000
Park and Recreation	NTC Building 619	2	2.50	$224,358
Park and Recreation	Olive Street Mini Park	3	0.50	$48,034
Park and Recreation	Pacific View Elementary Joint Use Agreement[1]	4	0.50	$106,862
Park and Recreation	Riviera Del Sol Neighborhood Park[1]	8	1.00	$195,927
Fire-Rescue	Black Mountain Ranch Fire Station	5	12.00	$1,840,628
Library	Pacific Highlands Ranch Branch[2]	1	9.50	$427,173
Total Fiscal Year 2022			**37.50**	**$4,906,891**

Fiscal Year 2023 Department	Facility	Location of Facility (District)	FTE	First Year Annual Expense
Park and Recreation	Dewey Elementary Joint Use Agreement[1]	2	0.50	$71,622
Park and Recreation	Florence Elementary School Joint Use Agreement	3	0.50	$50,144
Park and Recreation	Hidden Trails Neighborhood Park[1]	8	0.50	$126,121
Park and Recreation	Mira Mesa Community Park (Phase III)[1]	6	3.50	$323,964
Park and Recreation	Toler Elementary Joint Use Agreement[1]	2	0.50	$82,070
Total Fiscal Year 2023			**5.50**	**$653,921**

Fiscal Year 2024 Department	Facility	Location of Facility (District)	FTE	First Year Annual Expense
Park and Recreation	Lindbergh-Schweitzer Elementary Joint Use Agreement[1]	6	0.50	$105,315
Park and Recreation	Spreckels Elementary Joint Use Agreement[1]	1	0.50	$93,106
Fire-Rescue	Fairmont Avenue Fire Station	9	12.00	$1,981,432
Total Fiscal Year 2024			**13**	**$2,179,853**

Fiscal Year 2025 Department	Facility	Location of Facility (District)	FTE	First Year Annual Expense
Fire-Rescue	Paradise Hills Fire Station	4	24.00	$3,889,947
Total Fiscal Year 2025			**24.00**	**$3,889,947**

1. Includes one-time expense for items such as vehicles in the first year of operation. One-time expenses eliminated from subsequent years operating costs.
2. The Outlook reflects new ongoing annual operational costs beginning in FY 2021; however, based on the latest estimate for construction, the Pacific Highlands Ranch Branch library is not anticipated to open until February 2022 (FY 2022).