THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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IBA Review of the Mayor's FY 2027-2031 Five-Year Financial Outlook

OVERVIEW

Importance of the City's Outlook

On November 7, 2025, Mayor Gloria released his *Fiscal Year 2027-2031 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 *Council Policy 000-02: Budget Policies* as *"the basis for determining the coming year's operating budget allocations."* Former Mayor Sanders initiated the Five-Year Financial Outlook process in 2006 which was continued by subsequent Mayors. In 2015, the City Council initiated a Charter Review process with a focus on greater clarity of the budget process including the requirement for the Mayor to issue a multi-year financial outlook annually. In June 2016, with a vote of the people, Section 69 of the City's Charter was amended to require the Mayor to prepare a multi-year financial outlook for the General Fund annually.

"The Mayor shall annually prepare a multi-year financial outlook for the general fund projecting anticipated revenues and expenditures in future years as a fiscal planning document and basis for the proposed budget."

The City's Budget Policy was also amended to state 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 Council policies." While the Outlook should not be interpreted as a budget, it provides the Council and the public with a longer-term financial perspective and a preliminary indication of the Mayor's budget priorities. Each year many Council priorities will overlap with the Mayor's, but Council has final authority in the budget process to determine the City's budget priorities for the next fiscal year.

While the Council cannot change the Mayor's Outlook, the Council remains the ultimate budget authority and can make changes to the budget following Mayor Gloria's release of the FY 2027 Proposed Budget. In doing so, the budget must stay balanced through identification of alternate budget reductions or new resources, delaying new facilities, consolidating or eliminating other programs, or other mitigation tools.

IBA Review and Analysis of Significant Annual Budget Reports & Council Budget Priorities

The release of the Outlook is the first forecast of the next fiscal year's overall budget issues and whether there is an anticipated surplus or shortfall in the General Fund. While the Executive Branch develops the Outlook, the Office of the Independent Budget Analyst (IBA) is charged with providing the City Council and the public with a comprehensive review and analysis of the annual Outlook as well as major budget reports – such as Quarterly Budget Monitoring Reports (including the First Quarter, Mid-Year and Third Quarter Reports); the Mayor's Proposed Budget; the Mayor's May Revision to the Proposed Budget; and the Five-Year Capital Infrastructure Planning Outlook.

Each fiscal year the Office of the IBA also develops the Council's Budget Priorities Resolution based on individual Councilmembers' priorities memoranda, which is provided to the Mayor to help inform Mayoral budget priorities. The Council's initial Budget Priorities Resolution for FY 2027 was approved on November 18, 2025.[1]

"Councilmembers shall . . . communicate their budget priorities to the IBA, who will analyze and consolidate the priorities into a proposed Council budget priorities resolution"

Implications in the Mayor's Outlook

The Outlook projects significant General Fund deficits through each of the next five years, starting with nearly $90.0 million in FY 2027, over $100.0 million in FY 2028, before dropping in half in FY 2029, largely due to an anticipated decrease in the City's pension payment. As the City is required by law to adopt balanced budgets on an annual basis, these deficits will have to be closed, either through the identification of additional revenues and resources, the reduction of existing or new expenditures, or both. Over the last year, the City implemented several new revenues, including a solid waste collection fee, increased Transient Occupancy Tax associated with implementation of Measure C, and various parking initiatives, among others. Looking to FY 2027, there are

[1] Council will also have the opportunity to update its initial FY 2027 Budget Priorities Resolution in February 2026; to start that process, a call memorandum will be issued mid-December 2025 for Councilmembers' updates to their budget priorities memoranda. Those priorities memoranda are due to our Office on January 9, 2026 and will be released on January 27 as part of an IBA report on updated Council priorities.

limited additional near-term revenue options available that can be implemented without voter approval at a Citywide election, which means expenditure reductions will need to be considered, including various ongoing reductions that could meaningfully impact current service levels.

While the City's annual budgets over the past several years were balanced, they were not structurally balanced and relied heavily on one-time resources. While the use of the federal American Rescue Plan Act (ARPA) and other one-time resources was necessary to maintain City services during the COVID-19 pandemic and its aftermath, our Office continually noted that this resource was projected to be exhausted, and that the City would be faced with a significant budget deficit if the structural imbalance was not addressed. Last year's Outlook, released December 2024, projected a budget shortfall of $258.2 million for FY 2026. In response, the Mayor implemented various expenditure mitigations over the following months, including a strategic hiring freeze, suspension of non-essential spending, consolidation of several departments, and the related reduction of budgeted staffing levels. Departments were also directed to propose budget reductions for FY 2026. At the same time, the Council and the administration moved to implement various revenue measures that helped reduce – but not eliminate – the need for expenditure cuts.

Balancing the FY 2026 Budget proved particularly challenging; it was developed with the aim of striking a balance between stabilizing the City's General Fund finances and sustaining investments in key priorities such as public safety, homelessness and housing, and infrastructure. To balance the FY 2026 Budget, the City again employed one-time resources, while scaling back funding for various programs and operations and identifying new ongoing revenue sources.

Although a significant portion of the structural deficit was reduced in FY 2026, the continued deficits projected over the Outlook are still large and will need to be addressed. Moving forward, the City should work to keep its ongoing operating expenses in balance with its ongoing revenues to achieve structurally balanced budgets. Continued use of significant one-time funds for ongoing expenditures invites challenges in future fiscal years. As the City works to balance its budget, it will also need to keep an eye on economic uncertainties – like tariffs, inflation, and potential drops in consumer confidence or job growth – that could affect future financial planning.

This report includes several sections, which are highlighted in the Report Summary on the next page. Additional details and discussions are included in the body of our report. Our Office thanks staff from the Department of Finance and other City departments for responding to our questions in preparing this report.

REPORT SUMMARY

Overall fiscal considerations

- Projected structural budget deficits persist throughout the Outlook period that must be addressed. Structural budget deficits occur when ongoing and sustainable revenue sources are insufficient to support ongoing expenses.

Review and analysis of General Fund baseline revenues and assumptions in the Outlook

- We find that while major General Fund revenue projections in the Outlook are reasonable, some revenue estimates for the upcoming fiscal year included in the Outlook may be too optimistic given current year actuals and anticipated economic headwinds.

Review and analysis of baseline General Fund expenditures

- We identify changes from the FY 2026 Adopted Budget to the FY 2027 Outlook baseline expenditures, which maintain service levels with no new initiatives.
- We discuss personnel-related expenditure increases for FY 2027, which are largely related to estimated compensation increases for members of the City's Recognized Employee Organizations.
- We also discuss select Non-Personnel Expenditures, including debt financing and the information technology ERP modernization project.

Review and analysis of additional Outlook priorities beyond baseline expenditures

- We discuss operating needs for anticipated new or expanded parks, libraries, and fire stations. Given the likelihood for service-level reductions during upcoming budget cycles, we note that the City should consider deferring the opening of new facilities if existing services, programs, and facilities are determined to be a higher priority.
- We also review funding needs for homelessness programs and services and note that for FY 2027 available resources may be insufficient to fund the City's planned efforts. Council may wish to re-evaluate existing homeless programs and strategize homelessness priorities given the limited available resource.

Review and analysis of potential funding needs not included in the Outlook

- Many of the City's unfunded priorities would require significant additional resources beyond what has been identified in the Outlook.
- We provide additional context on infrastructure needs discussed in the Outlook, as well as solid waste management considerations. We also provide a review of two priorities not funded in the Outlook to full Council policy or priority level: arts & culture and SD Access4All.

IBA discussion of potential resource and mitigation options

- We outline several considerations for FY 2027 resources, along with potential measures to mitigate the projected baseline budget deficits beyond FY 2027. Without a new major ongoing revenue source, significant budget cuts to programs and services will be needed to address the City's structural budget deficit.

OVERALL FISCAL CONSIDERATIONS

The General Fund Outlook "baseline" is comprised of ongoing revenues and expenditures; ongoing baseline expenditures are associated with maintaining, rather than expanding, current City service levels. Although baseline revenue projections over the Outlook increase steadily, as shown in the first row of the following table, they are insufficient to cover projected baseline expenditures. The resulting "Baseline Revenue Shortfall," or structural budget deficit, is shown in the third row of the table. A structural budget deficit occurs when ongoing revenue sources are not enough to support ongoing expenses.

Based on the FY 2026 Adopted Budget, the City is beginning the Outlook period with a General Fund baseline shortfall of $37.3 million – shown in the FY 2026 column.[2] Unlike in last year's Outlook, contributions to the General Fund and Risk Management reserves are not included in baseline shortfall amounts. For FY 2026, including the $66.4 million in reserve contributions that would otherwise be necessary to bring reserves to targeted levels would bring the baseline shortfall to $103.6 million (not shown in the table); this higher shortfall would be consistent with the methodology used in last year's Outlook. However, the City is in the process of revising its Reserve Policy, and consequently no contributions are currently included in the Outlook's baseline expenditures.

The Outlook's General Fund baseline shortfall increases in FY 2027 to $88.8 million – $51.6 million more than the $37.3 million baseline shortfall in FY 2026. This change is the result of projected expenditures outpacing revenues, with the largest expenditure increases projected in employee compensation, fleet fees, and debt financing for capital infrastructure.

Revised Outlook Shortfall *($ in millions)*						
	FY 2026 [a]	**FY 2027 Outlook**	**FY 2028 Outlook**	**FY 2029 Outlook**	**FY 2030 Outlook**	**FY 2031 Outlook**
Baseline Revenues	$ 2,137.9	$ 2,195.5	$ 2,255.7	$ 2,337.7	$ 2,406.3	$ 2,493.4
Baseline Expenditures	2,175.2	2,284.3	2,362.6	2,390.1	2,461.6	2,550.3
Baseline Revenue Shortfall	***$ (37.3)***	***$ (88.8)***	***$ (106.9)***	***$ (52.4)***	***$ (55.3)***	***$ (57.0)***
Adopted Budget: One-time Expenditure Priorities	(11.6)	-	-	-	-	-
Adopted Budget: Use of One-Time Resources	48.8	-	-	-	-	-
Outlook: Additional Priorities Beyond Baseline [b]	-	(21.8)	(32.1)	(39.1)	(39.7)	(47.4)
Revised Outlook Shortfall	**$ (0.0)**	**$ (110.6)**	**$ (139.0)**	**$ (91.5)**	**$ (95.0)**	**$ (104.4)**

Note: Table may not total due to rounding.
[a] FY 2026 includes the FY 2026 Adopted Budget as modified to remove one-time revenue and expenditure adjustments.
[b] Includes additional funding for homelessness programs and support for new and expanded facilities.

As shown in the "Revised Outlook Shortfall" line in the table, the FY 2026 General Fund Adopted Budget also included $11.6 million in one-time expenditure priorities *beyond* the Baseline Revenue Shortfall. To mitigate the resulting shortfall, the FY 2026 Budget was balanced with $48.8

[2] The FY 2026 base includes the FY 2026 Adopted Budget as modified to include one-time revenue and expenditure adjustments, for consistency with treatment of these areas in the Outlook years (FY 2027 through FY 2031).

million in one-time resources, including $19.3 million in expenditure reductions and $29.5 million in increased revenues – largely from reliance on grants and non-general fund monies. Thus, the FY 2026 Budget was balanced in accordance with City Charter requirements.

However, using one-time resources for ongoing expenditures creates challenges in future fiscal years. The City has limited one-time resources remaining. Grant funds have been considerably reduced since federal COVID relief funding was exhausted; the General Fund Reserve is underfunded as compared to the City's current Reserve Policy; and General Fund Excess Equity (available General Fund monies beyond the General Fund Reserve) is anticipated to be completely exhausted in FY 2025 [3].

Moving forward, operational deficits will need to be covered through reductions to programs and services provided by the City, and/or newly identified revenues. The City lacks the ongoing resources required to maintain its existing service levels and to address a growing capital backlog of critical infrastructure projects. The City's persistent structural imbalance must be addressed. As mentioned previously, there are limited significant near-term revenue options available, which necessitates the difficult consideration of expenditure reductions which will likely involve painful ongoing reductions that will meaningfully affect service levels.

Moreover, future service expansions expected by the public or needed for compliance with various laws or for health and safety reasons cannot occur without adequate funding. As shown in the second-to-last row of the preceding table, the Outlook incorporates additional priorities beyond the baseline, including additional funding for homelessness programs and support for new and expanded facilities. With these additional priorities, projected shortfalls – that need to be mitigated – grow larger, as shown in the bottom line of the table. For FY 2027, the projected shortfall increases to $110.6 million.

There are also other budget priorities that are not included in the Outlook's projected shortfalls, such as unfunded infrastructure needs and other Council priorities.[4] We further note that the Outlook is based on information known at this time; unpredictable events such as an economic recession could significantly alter projections.

[3] The depletion of Excess Equity is based on FY 2025 *unaudited* actual activity; year-end amounts are not considered final until completion of the audit of the City's FY 2025 financial statements – anticipated in December.

[4] Notably, the Outlook *does not include the full funding of capital infrastructure projects that were identified in the City's most recent Five-Year CIP Outlook.* Given the City's lack of sufficient resources to address those needs, it is reasonable to exclude those amounts from this Financial Outlook, but it should also be acknowledged that additional infrastructure priorities for which the City lacks funding continue to exist, as will be discussed later in this report.

To provide additional context on the City's fiscal condition, the following table provides a summary of the City's conformance with select financial policies and how they are handled in the Outlook.

Conformance with Financial Policies		
City Financial Policies		**Mayor's Outlook**
Select Principles included in the annual Statement of Budgetary Principles	Elimination of the General Fund structural budget deficit	Does Not Conform: The structural budget deficit projection for the FY 2027 Outlook is $88.8 million (at FY 2026 service levels); and a structural deficit persists throughout the Outlook period.
	Active pursuit of alternative service delivery methods for efficiency	In Process: The Outlook indicates that departments will conduct a strategic review of their programs to identify potential savings by implementing operational efficiencies; they will also evaluate potential service reductions.
	Prioritization for City services based on Charter requirements, public input, benchmarking, departmental goals, performance data, and equitable provision of services	In Process: Funding is included to support City Charter requirements, applicable laws, best practices, departmental goals, and public input that has been considered during budget development and adoption. In the Outlook the Mayor has identified additional services above baseline that he considers to be critical priorities. Priorities will be further considered during the upcoming budget development process.
	Identification of funding for ongoing expenses when considering new facilities or programs	Conforms: The Outlook identifies ongoing expenses for new facilities included in the Outlook.
	Achievement of 100% cost recovery for programs that intend full cost recovery through fees	Conforms: The City regularly reviews and adjusts user fees in accordance with its User Fee Policy; cost recovery levels are set upon approval of fees; and estimated fee revenues are included in baseline revenues.
	Fully fund the annual required defined benefit pension contribution	Conforms: The City has fully funded the annual required defined benefit pension contribution since FY 2006; estimated full funding is included in baseline expenditures.
	Fund the City's retiree healthcare costs in a manner that meets obligations to eligible members while keeping the related CalPERS fund solvent over the applicable benefit years	Conforms: This retirement benefit is also known as an Other Post-Employment Benefit, or OPEB. OPEB is funded in the Outlook in accordance with this long-term funding strategy, which was implemented in FY 2024.
	Develop a plan to fund deferred capital infrastructure and maintenance	Does Not Conform: The City's most recent Capital Improvements Program Outlook shows a $6.51 billion funding gap for infrastructure projects for which resources have not been identified. One future resource the City could consider is the use of General Obligation bonds, though they would require voter approval – see page 35 of this report for additional information.

Conformance with Financial Policies *(con't)*		
City Financial Policies		**Mayor's Outlook**
Debt Policy	The City's Debt Policy provides that the City shall strive to maintain certain General Fund debt ratios including: under 10% debt ratio (debt service/lease payments as a percent of total available revenues); below 25% debt ratio when combining debt service with pension and OPEB contributions.	Conforms: The City's debt ratios are projected to remain within Debt Policy parameters after accounting for projected debt service costs that are assumed to be incurred by the General Fund during the Outlook period. See page 17 for additional information.
General Fund (GF) Reserve	Under the current City Reserve Policy, the goal is to incrementally increase the GF Reserve to 16.7% of GF operating revenues by FY 2030. The FY 2026 Reserve target is 14.1%, which is estimated to be $262.9 million.	Does Not Conform: The Reserve is currently projected to be short of its FY 2026 target by $55.8 million; and the Outlook assumes no GF Reserve contributions will be made throughout the Outlook period. The Department of Finance is working to revise the Reserve Policy to better align with the City's current fiscal situation – anticipated to be presented early next calendar year. See page 31 for additional information.
Risk Management (RM) Reserves	These Reserves include Workers' Compensation (WC), Public Liability (PL), and Long-term Disability (LTD) Reserves, for which the goal is to maintain a balance equal to 12%, 50%, and 100% of outstanding claims, respectively, based on the most recent three-year average of actuarial liabilities.	Does Not Conform: RM Reserves are also currently projected to be underfunded in FY 2026 – WC by $12.7 million, PL by $8.3 million (not including an outstanding loan to the Sewer Fund – see our review of the First Quarter Report for more information), and LTD by $1.6 million. The Outlook assumes no contributions will be made to these Reserves throughout the Outlook period. As mentioned, a revised Reserve Policy is anticipated early next calendar year.
Infrastructure Fund	City Charter section 77.1 requires a transfer of designated revenues from the General Fund to the Infrastructure Fund. Allowable uses of these funds include acquisition of real property, construction, reconstruction, rehabilitation, and repair and maintenance of General Fund infrastructure, as well as associated financing costs.	Conforms: The Outlook assumes no Infrastructure Fund contributions will be made throughout the Outlook period. Based on current calculations, no such contributions are required.
Penny for the Arts	On October 22, 2012, the City Council approved a "Penny for the Arts" funding blueprint. The goal is to increase arts and culture funding from the City's Transient Occupancy Tax (TOT) to equate to 1¢ of the 10.5¢ TOT, or 9.52% of such TOT revenues.	Does Not Conform: The Outlook includes $14.4 million in Penny for the Arts funding for FY 2027, or 4.5% of the total 10.5¢ TOT revenues. The $14.4 million allocation is projected to remain relatively unchanged, while overall TOT revenues are projected to increase on-average by 2.1% annually over the Outlook period. Thus, the FY 2031 Penny for the Arts funding is only projected to be 4.1% of total TOT revenues. See page 28 for additional information.
Library Ordinance	The Library Appropriation Ordinance (Library Ordinance, San Diego Municipal Code section 22.0228), requires that the Library Department budget be equal to 6% of the General Fund budget each fiscal year.	Does Not Conform: For FY 2026 the Library Department budget is equal to 3.5% of the adopted General Fund budget; and the Library Ordinance provisions were waived. Funding in accordance with the Library Ordinance is not included in the Outlook.

REVIEW OF BASELINE GENERAL FUND REVENUES

Review of Baseline Revenues
• Property Tax • Sales Tax • Transient Occupancy Tax • Franchise Fees • Cannabis Business Tax • On-Street Parking Meter Revenue • Balboa Park Parking Revenue • Emergency Medical Services (EMS) Fund Transfer

The table below reflects baseline General Fund revenues for the FY 2027 to FY 2031 Outlook period and includes the FY 2026 Adopted Budget revenues and updated FY 2026 revenue projections included in the First Quarter Report. Total revenue for FY 2027 in the Outlook anticipates a growth rate of 1.4%, or $30.3 million, above the FY 2026 projected revenue in the First Quarter Report of $2.17 billion. Overall baseline revenues increase steadily for the remaining four years of the Outlook, with growth averaging about 3.2% per year. Notably, this growth rate is lower than the average annual rate of inflation over the prior five fiscal years (FY 2021-2025) of 6.2%, suggesting a continued slowdown in the growth of both economic activity and major General Fund revenues.[5]

Additionally, our Office believes that some FY 2027 revenue estimates in the Outlook may be too optimistic at this time given how revenue actuals performed in FY 2024, FY 2025, and FY 2026 to-date in addition to the economic headwinds that are expected in the short term; those headwinds were summarized in the September 2025 UCLA Anderson Economic Forecast, which stated:

> *Even if a recession is avoided, the current pivot towards monetary easing sets the stage for what we anticipate will be a "stagflation-lite" regime, marking a period where both inflation and unemployment remain modestly elevated.*[6]

Economic impacts and fiscal considerations for each revenue source are discussed in their respective sections below.

General Fund Revenues *($ in millions)*							
Source of Revenue	**FY 2026 Adopted**	**FY 2026 Projection**	**FY 2027 Outlook**	**FY 2028 Outlook**	**FY 2029 Outlook**	**FY 2030 Outlook**	**FY 2031 Outlook**
Property Tax	$ 844.6	$ 846.1	$ 883.8	$ 914.1	$ 952.4	$ 992.2	$ 1,033.6
Sales Tax	374.5	374.1	383.6	395.1	407.7	420.7	434.2
Transient Occupancy Tax	170.3	167.4	170.9	174.3	177.7	181.3	185.8
Franchise Fees	106.5	106.5	99.2	100.9	102.8	104.7	114.0
All Other Revenue Categories [a]	671.6	671.1	658.2	671.4	697.1	707.3	725.8
Total	**$ 2,167.4**	**$ 2,165.2**	**$ 2,195.5**	**$ 2,255.7**	**$ 2,337.7**	**$ 2,406.3**	**$ 2,493.4**

Note: Figures may not total due to rounding.

[a] Includes Transfers In, Charges for Services, Special Promotional Programs reimbursements, etc.

Property Tax

Property tax revenue in FY 2027 is forecasted to grow 4.5% above the FY 2026 year-end projection across all property tax sources and have an average annualized growth rate during the five-

[5] Inflation is measured by the Consumer Price Index (CPI) for all urban consumers in the San Diego-Carlsbad, CA Metropolitan Statistical Area (MSA).

[6] UCLA Anderson Forecast, "Fall 2025 Economic Forecast", September 2025, pp. 11, http://www.uclaforecast.com/uploads/forecasts/2025/Oct/uclaforecast_Fall2025.pdf.

year Outlook period of 4.1%. The FY 2027 growth rates for the portion of property tax revenue from 1% Proposition 13 and in-lieu Motor Vehicle Licensing Fee are expected to be 3.7% and 4.0% respectively.

These growth rates are the lowest since FY 2022, which suffered from poor real estate activity in calendar year 2020 during Covid. The FY 2027 forecast reflects a declining number of home sales in calendar year 2025, a modestly declining median home price, and limited new supply of housing.

In addition to the 1% Proposition 13 property tax and in-lieu Motor Vehicle Licensing Fee, the City receives property tax revenue from the Redevelopment Property Tax Trust Fund (RPTTF) via pass-through tax sharing payments and residual property tax payments after the City, as the Successor Agency for the former Redevelopment Agency (RDA), pays its annual Recognized Obligation Payment Schedule (ROPS). Similarly, the City received a portion of the proceeds of the sale of property formerly owned by the RDA.

The FY 2027 Outlook year includes $5.8 million in one-time property tax revenue coming to the City because of the sale of the Tailgate Park property. Given the timing constraints with resolving pending litigation and closing escrow on the property, our Office believe it may be a risk to include revenue from the sale of Tailgate Park, or any other RDA properties, in Outlook revenue assumptions. Without this revenue the FY 2027 property tax revenue would total $877.9 million.

Sales Tax

The First Quarter Report projects sales tax revenue to end the year at $347.1 million, representing 0.5% growth from FY 2025 unaudited actuals. In the Outlook, sales tax revenue in FY 2027 is projected to increase by 2.5% above the FY 2026 year-end projection as of the First Quarter Report, then increase by 3.0% in FY 2028, and 3.2% in the outer years. These growth rate projections are in line with estimates from the City's sales tax consultant prepared in October 2025.

The stable sales tax growth in the Outlook is reasonable, though we note it does not factor in any potential near-term recession. However, the near-term growth rate in sales tax, while buoyed by reliably strong online retail sales, is heavily reliant on industry specific growth for restaurants & hotels and business & industry which differs from recent actual data and consumer and business confidence surveys.

While the Outlook predicts a sales tax growth will rebound in FY 2027, which is somewhat evident already in FY 2026, the UCLA Anderson Forecast anticipates real taxable sales being closer to 1.8% in FY 2027 as compared to the 2.5% in the Outlook. A 1.8% growth rate would generate $2.6 million less than forecasted in the Outlook for FY 2027.

Transient Occupancy Tax

Transient Occupancy Taxes (TOT), or hotel taxes, are taxes on short-term lodgings at a rate of 11.75%, 12.75%, or 13.75% depending on which of three zones the lodging property is located in the City. The table on the following page shows the TOT amounts allocated to the General Fund, the TOT Fund, and three special Measure C related TOT funds. TOT is projected to grow by 1.8% in FY 2027 above FY 2026 across all sources of TOT revenue and maintain a 1.8% growth rate throughout the Outlook period.

Transient Occupancy Tax Revenue *($ in millions)*							
TOT Allocation	**FY 2026 Adopted**	**FY 2026 Projection**	**FY 2027 Outlook**	**FY 2028 Outlook**	**FY 2029 Outlook**	**FY 2030 Outlook**	**FY 2031 Outlook**
General Fund Allocation (5.5%)	$ 170.3	$ 167.4	$ 170.9	$ 174.3	$ 177.7	$ 181.3	$ 185.8
Special Promotional Programs (4.0%)	122.7	120.6	123.2	125.6	128.2	130.7	134.0
Council Discretionary (1.0%)	30.7	30.2	30.8	31.4	32.0	32.7	33.5
Subtotal - General Fund and TOT Fund	**$ 323.6**	**$ 318.1**	**$ 324.8**	**$ 331.3**	**$ 337.9**	**$ 344.7**	**$ 353.3**
TOT Homelessness Fund	32.6	31.5	32.2	32.8	33.5	34.2	26.5
TOT Street Repair Fund	0.0	0.0	0.0	0.0	0.0	0.0	8.5
TOT Convension Center Fund	47.7	47.7	47.7	47.7	47.7	47.7	47.7
Subtotal - Measure C	**$ 80.3**	**$ 79.2**	**$ 79.9**	**$ 80.5**	**$ 81.2**	**$ 81.8**	**$ 82.7**
Total	**$ 403.9**	**$ 397.3**	**$ 404.7**	**$ 411.8**	**$ 419.1**	**$ 426.5**	**$ 436.0**

A November 2025 report from the San Diego Tourism Authority (SDTA) of hotel's quarterly revenue actuals from calendar year 2023 to 2025 shows hotel revenue and City TOT revenue closely mirroring one another. It is reasonable to infer that an accurate SDTA hotel forecast for calendar years 2026 and 2027 would also closely mirror current City revenue forecasts, which they do. Our Office believes the TOT revenue assumptions in the Outlook are reasonable.

Franchise Fees

Overall Franchise Fees in the Outlook are projected to decrease by $7.3 million, -6.9%, from the FY 2026 year-end projection to FY 2027.

The FY 2027 decrease in Franchise Fee revenue to the General Fund is primarily due to an $8.0 million decrease in the pre-negotiated annual SDG&E electrical franchise bid payments. The annual electrical bid payments were front-loaded in the first five years of the 10-year agreement. Two additional bid payments in the initial 10-year contract term are anticipated in FY 2031 and FY 2032, but only if an additional 10-year extension option is exercised for FY 2032 to FY 2041.

The Outlook also projects a $0.7 million decline in cable franchise fee revenue in FY 2027 due to continued declines in cable revenue. The electric bid payment and cable franchise fee decreases are partially offset by increases in the SDG&E franchise fee payments for electricity and gas, increased refuse hauler tonnage, and police towing fees. We note that proposed changes to Council Policy 500-03, Policy Requested Towing, related to towing of vehicles with expired registrations of more than six-months may reduce the police towing fees revenue by up to $1.4 million, of which $0.9 million goes to the police towing franchise fee; however, this reduction might be mitigated by towing those vehicles for other reasons or increased fines for violations.

Overall, we believe the Franchise Fee revenue projections in the Outlook are reasonable, but note that significant changes are possible due to unpredictable fluctuations in the SDG&E franchise fee payment amounts. The City will receive an annual clean-up payment in February 2026, after which, we will have a clearer understanding of what total Franchise Fee revenue will look like in FY 2027.

SDG&E Franchise Fees Supporting Council-Established Funds

There are two fund transfers that are directly tied to SDG&E franchise fees, which were suspended in FY 2026, but are projected to resume in the Outlook. These transfers support the Council-established Energy Independence Fund (EIF) and Climate Equity Fund (CEF). The General Fund impact of these transfers is shown in the following table.

Transfer of Franchise Fee Revenue to Climate-Related Funds					
	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Climate Equity Fund	$ 6,711,000	$ 6,904,000	$ 7,111,000	$ 7,325,000	$ 7,544,000
Energy Independence Fund	117,000	120,000	124,000	127,000	2,739,000
Total Impact to General Fund	**$ 6,828,000**	**$ 7,024,000**	**$ 7,235,000**	**$ 7,452,000**	**$ 10,283,000**

Note that as part of the electric franchise agreement, SDG&E chose to pay their minimum bid proceeds, totaling $70.0 million, in installments, which included $10.0 million payments with interest in FY 2022 through FY 2026, and then the final two payments in FY 2031 and 2032.[7] As noted, this accounts for an $8.0 million decrease in franchise fee revenue from FY 2026 to FY 2027, as well as a $7.2 million increase in revenue from FY 2030 to FY 2031. As EIF payments are tied to bid proceeds, these payments also follow this trend.

Cannabis Business Tax

The Outlook includes projected revenue from the City's non-medical cannabis business tax (CBT). The tax applies to cannabis-related business activities such as transporting, manufacturing, packaging, and retail sales. Retail outlets are taxed at a rate of 10.0% while other activities, including cannabis production facilities (CPFs), are taxed at 2.0%.

The Outlook estimates total FY 2027 CBT revenue to be $20.6 million, which is $704,000 lower than the FY 2026 Adopted Budget of $21.3 million but $827,000 above the FY 2026 first quarter projection of $19.7 million. The Outlook assumes updated year-end CBT revenue based on the First Quarter Report and incorporates the actual number of new locations opened in prior fiscal years to forecast the number of outlets and CPFs through FY 2031.[8] The Outlook also assumes a 3.5% annual decline in taxable gross receipts from retail outlets to reflect increased competition from the illicit market over the outlook period.

Although it may be reasonable to factor in an annual decline in taxable gross receipts, the assumed -3.5% reflected in the Outlook is more optimistic than actual year-over-year declines. For instance, the average annual growth rate in taxable gross receipts from retail outlets over the past four fiscal years (FY 2022 – FY 2026) is -9.6%. If this rate was applied, all things being equal, FY 2027 CBT forecasted revenue would be $19.3 million, which is $1.2 million less than what is projected in the Outlook.

[7] Per the City Charter, all revenue derived from gas and electric franchise agreements, including bid proceeds must be split 75% to the General Fund and 25% to the Environmental Growth Funds.

[8] The number of retail outlets is anticipated to increase from 31 in FY 2027 to 36 in FY 2031, while the CPFs are projected to grow from 36 to 41 over the same Outlook period.

That noted, the Outlook also does not consider efforts that may help increase CBT revenue by targeting the illicit market. These include an early proposal from Councilmember Campillo's Office to require out-of-town delivery-only cannabis retailers to obtain permits with the City and increase fines for illegal operations. Additionally, the State has enacted legislation that limits the sale of intoxicating cannabinoids, which currently compete with the legal cannabis market, exclusively to licensed cannabis dispensaries beginning in January 2026, while the federal government is set to ban most intoxicating and synthesized hemp products for consumption beginning in November 2026. While the fiscal impact of these efforts is difficult to quantify at this time, our Office will continue to monitor CBT revenue trends.

On-Street Parking Meter Revenue

Revenue generated from City-owned on-street parking meters are used to support parking-related activities, including the collection of meter coins, the maintenance and enforcement of parking spaces, as well as certain transportation-related infrastructure improvements, such as streetlight repair. This revenue may be allocated to eligible expenditures, including those within the General Fund.

For FY 2027, the Outlook assumes the General Fund will receive \$22.0 million from the Parking Meter Operations (PMO) Fund and "loss-of-revenue" fees.[9] Although this projection still includes a 15% contribution of net parking meter revenue to Community Parking Districts (CPDs) per Council Policy 100-18, Council's action in October 2025 waived this contribution through FY 2027. With this waiver in place, the General Fund is anticipated to receive \$25.9 million in parking meter revenue, which is \$4.6 million above the FY 2026 Adopted Budget amount of \$21.4 million.

In addition to the Council policy waiver, the increase is also driven by various items including \$10.1 million in meter expansion activities at existing parking districts and \$2.2 million from the annualization of expanded hours and Sunday enforcement. These gains are partially offset by \$3.5 million in reduced parking meter revenue due to a smaller-than-anticipated implementation area for event-based pricing around Petco Park area and \$3.3 million in reduced revenue from existing parking meters prior to FY 2026. Additionally, PMO Fund-related expenses have increased, including a \$3.0 million increase in the City's parking meter contract due to the purchase and replacement of parking meters and \$291,000 for the addition of 2.00 Parking Meter Technicians and 1.00 Senior Parking Meter Technician within the PMO Fund.

We will continue to monitor parking meter revenues as additional initiatives are implemented and more actual revenue data becomes available.

Balboa Park Parking Revenue

The Outlook's baseline includes \$11.0 million in total revenues assumed to be generated annually from Balboa Park parking over the Outlook period. This includes \$8.0 million annually from the City's implementation of the Balboa Park Paid Parking Program and \$3.0 million annually from the San Diego Zoo. While these estimates are largely in line with our Office's current projections,

[9] "Loss-of-revenue" fees include fees paid by hotels, restaurants, and other businesses who utilize parking meters spots as valet zones, as well as fees related to construction projects encroaching into metered spaces.

actual revenue will vary depending on the behavioral changes of park visitors after the paid parking program is implemented beginning January 5, 2026. Additionally, negotiations with the San Diego Zoo concerning a long-term lease extension and Zoo parking lot revenue sharing, among other lease amendments, are still underway and the outcome is unknown.

Emergency Medical Services (EMS) Fund Transfer

Since the implementation of the Alliance Model in October 2023, EMS revenue has consistently exceeded projections, allowing excess fund balance to mitigate General Fund budget deficits. The FY 2026 Adopted Budget includes a transfer of $11.5 million from the EMS Fund to the General Fund, of which $11.2 million is ongoing and assumed to continue annually throughout the Outlook period. The Fire-Rescue Department's projections indicate that the EMS Fund can sustain this level of transfer activity assuming the current EMS ambulance transport system continues. However, should the City's EMS delivery method change following the completion of the next RFP process for the EMS system, financial projections could be impacted. Additionally, recent Medicaid reforms enacted under the One Big Beautiful Bill Act (OBBBA) could potentially impact EMS revenue going forward by shifting a greater portion of EMS patient populations from insured to uninsured and reducing supplemental reimbursement payments under the Public Provider Ground Emergency Transportation Inter-Governmental Transfer (PP-GEMT IGT) Program. The actual impacts from OBBBA are still unknown and the Department is in frequent communication with State and federal agencies for information and guidance.

REVIEW OF BASELINE GENERAL FUND EXPENDITURES

General Fund baseline expenditures support existing service levels; therefore, there are no increases related to new programs in the Outlook's baseline. However, we note that decision-makers may ultimately determine that continuation of certain baseline services may not be possible given the City's structural deficit: some service levels could be reduced or eliminated in order to fund other needs and priorities determined to be more important. The City Council is the ultimate budget authority and can fund services that are different than those proposed by the Mayor.

Our review of General Fund baseline expenditures addresses changes from the FY 2026 Adopted Budget to the FY 2027 Outlook baseline. As shown in the table on the next page, the Outlook's FY 2027 General Fund baseline expenditure projection represents a net increase of $116.9 million, or 5.4%, from the FY 2026 Adopted Budget.

The largest expenditure increases shown in the table include:

- $29.2 million for an assumed 2.94% general wage increase
- $18.6 million for Lease Revenue Bond (LRB) debt service for CIP, largely to bring payments for the FY 2025 LRB issuance to a full-year amount
- $17.1 million for fleet fee increases, including vehicle replacement and usage charges
- $9.9 million for Workers' Compensation, partially related to FY 2026 expenses being projected higher than budgeted

- $6.7 million for the restoration of the annual Climate Equity Fund contribution
- $5.8 million for contract cost increases based on a 3.2% growth rate
- $4.9 million for the Actuarially Determined Contribution (ADC) pension payment increase

Several baseline expenditure changes are discussed in the sections following the table.

Increases/(Decreases) from the FY 2026 Adopted Budget to the FY 2027 Outlook Baseline Projection *($ in millions)*		
FY 2026 Adopted Budget		**$ 2,167.4**
Personnel Expenditure (PE) and Fringe Benefit Changes		**51.1**
Assumed 2.94% General Wage Increase	$ 29.2	
Workers' Compensation Expense Increase	9.9	
Actuarially Determined Contribution (ADC) - Defined Benefit Pension Payment Increase	4.9	
Wage Step Increases	4.2	
Increases from Labor Agreements (wage annualizations ($3.0m) & flexible benefits ($1.0m))	4.0	
Net Other PE Changes	(1.1)	
Non-Personnel Expenditure (NPE) Changes		**65.8**
Increased Lease Revenue Bond Debt Service for CIP	18.6	
Fleet Fees Increase: Vehicle Replacement ($13.6m) and Vehicle Usage ($3.5m)	17.1	
Climate Equity Fund Restoration	6.7	
Contracts - 3.2% Annual Growth Rate	5.8	
Energy & Utilities - Including Water Service Increases ($2.2m)	4.0	
Information Technology (IT) [a]	3.7	
Elections Cost Increase	2.5	
Animal Services Contract Increase	2.5	
General Fund Payment for SAP Modernization	2.1	
Add Back FY25 One-Time Reduction in General Fund Support for Shelter Operations	1.9	
Increase in Parks Improvement Funds Transfer	1.5	
Supplies - 3.2% Annual Growth Rate	1.2	
Net Other NPE Changes (incl. reductions of FY25 one-time expenses that are $750k or less)	(1.8)	
FY 2027 Outlook Baseline Projection		**$ 2,284.3**
Overall Increase: FY 2026 Budget to FY 2027 Outlook Baseline (5.4% Increase)		**$ 116.9**

Note: Table may not total due to rounding.

[a] Includes a $2.2 million increase in IT Voice/Data Network services due to contract with current provider is set to expire in June 2026. Additional funding to support the disentanglement from the incumbent provider, onboarding and integration of a new vendor, and any service continuity costs necessary to ensure a seamless and secure transition of IT operations is needed.

PERSONNEL-RELATED EXPENDITURES IN THE OUTLOOK BASELINE

In its *Potential Impacts to the Outlook* section, the Outlook mentions two less predictable areas in the expenditures forecast, both of which are personnel related.

Review of Baseline Personnel Expenditures

- Employee Compensation

The first is the ADC pension payment, for which projections can vary year-to-year due to actual experience being different than what was assumed in initial ADC projections. Differences that could cause changes to ADC projections include higher investment returns or higher salaries than previously assumed, both of which are anticipated to be incorporated in the upcoming FY 2025 actuarial valuation that will include the FY 2027 ADC. A higher FY 2025 investment return than anticipated will have a decreasing effect on the FY 2027 ADC, and higher salaries will have an increasing effect. Additionally, any assumption changes that might be implemented in upcoming valuations could impact ADC amounts.[10] Because of the complexity of pension system variables, the total of all impacts to the FY 2027 ADC (as well as outyear projections) will not be known until the FY 2025 valuation is completed and approved in early 2026.

The other personnel-related area identified in the Outlook as potentially changing from current assumptions involves future compensation increases, which are discussed in the following section.

Employee Compensation

Employee compensation is largely based on labor agreements, or Memoranda of Understanding (MOUs), with the City's six Recognized Employee Organizations (REOs). Current MOUs for all REOs expire at the end of FY 2026 (June 30, 2026); and negotiations for FY 2027 MOUs are underway.

The Outlook's estimates for compensation increases in FY 2027 and the remaining Outlook years are largely based on an assumed annual 2.94% general wage increase for members of all REOs, as well as unrepresented employees – whose recent general wage increases have been consistent with those approved for the Municipal Employees Association. The 2.94% annual wage increase assumed for FY 2027 and the remaining Outlook years is equivalent to the average annual Consumer Price Index growth for the San Diego-Carlsbad region over the last fifteen years, which our Office finds reasonable. However, compensation increases negotiated with each of the City's REOs may end up higher or lower than assumed in the Outlook. For reference, as of FY 2026, a 1.0% wage increase for General Fund employees is estimated to cost $9.9 million ($8.9 million before adding estimated overtime impacts) – note that this estimate does not include lagging increases to the ADC.

Components of FY 2027 compensation increase estimates are highlighted below:

- $29.2 million for the assumed 2.94% general wage increase discussed above [11]
- $4.2 million for "step increases" to eligible civil service employees' wages, based on performance and time in a position

[10] Economic and demographic assumptions are anticipated to be reviewed by the actuary and San Diego City Employees' Retirement System (SDCERS) Board every three years through an "experience study". An experience study involves historical analysis of pension plan assumptions and a consideration of future expectations and trends, including the rate of investment returns, wage inflation, and retirement and mortality rates. The plan experience study is the basis for the actuary's recommended changes to the plan's actuarial assumptions. *The next experience study is expected to include data through FY 2025. SDCERS anticipates that any resulting recommendations from the study would be included in the FY 2026 valuation and impact the FY 2028 ADC payment.*

[11] The $29.2 million estimate for the assumed 2.94% general wage increase includes estimated overtime impacts but not lagging increases to the ADC.

- $4.0 million for annualizations based on MOUs – including those for certain wage increases ($3.0 million) and flexible benefits increases ($966,000), which both begin mid-FY 2026

The Outlook, beginning on page 68, provides an overview of compensation issues, including discussion regarding the City's Compensation Philosophy and the City's goal of positioning itself to attract and retain talent that can effectively deliver services to its citizens. This has been an important consideration in recent negotiation cycles with the City's REOs. Over the past several years, the City has made significant progress in increasing compensation to more competitive levels for many job classifications. The City endeavors to pay at least the market median compensation for comparably situated public employees.[12] Any budget mitigation efforts that involve failing to keep pace with market wages could help address the General Fund revenue shortfall, but could also move the City backwards in its ability to attract and retain talent. This area will need to be weighed with other competing priorities during the budget development process.

NON-PERSONNEL EXPENDITURES (NPE) IN THE OUTLOOK BASELINE

As part of our analysis, the table on page 15 of this report includes major NPE changes from the FY 2026 Adopted Budget to the FY 2027 baseline projections included in the Outlook. Select NPE areas are also discussed in more detail, including debt financing and the information technology ERP modernization project.

Review of Baseline Non-Personnel Expenditures
• Debt Financing
• Information Technology – ERP Modernization Project

Debt Financing

The Outlook's baseline includes projected debt service costs associated with $677.7 million in proceeds from two new General Fund-backed Lease Revenue Bond (LRB) issuances assumed over the course of the Outlook. These debt proceeds are assumed to provide a total of $650.9 million for the General Fund Capital Improvement Program (CIP), including $190.4 million which will be needed meet the EPA's matching funds requirement for the City's Water Infrastructure Finance and Innovation Act (WIFIA) Loan to fund Stormwater improvements. The remaining $26.8 million is assumed for non-CIP purposes to finance the General Fund's portion of estimated costs related to the modernization of the City's SAP system. The LRB issuances are assumed to occur in FY 2028 ($406.3 million to fund spending in FY 2027-2029) and FY 2030 ($271.4 million to fund spending in FY 2030-2031), as shown in the table below.

[12] As part of the current negotiations process with the REOs over the FY 2027 MOUs, the City plans to use an upcoming compensation survey that will provide information on the City's relative standing with respect to market median compensation levels for positions in comparable jurisdictions.

Assumed Use/Spending of Lease Revenue Bond (LRB) Proceeds by Fiscal Year *($ in millions)*						
LRB Issuance Year	**FY 2028**			**FY 2030**		**Total**
LRB Proceeds ($)	$406.3			$271.4		**$677.7**
Use / Spending Year	**FY 2027***	**FY 2028**	**FY 2029**	**FY 2030**	**FY 2031**	**Total**
Capital Improvement Program	$9.0	$120.0	$110.5	$110.5	$110.5	**$460.5**
WIFIA Match	-	71.4	71.4	47.6	-	**190.4**
SAP Modernization	-	13.5	10.5	2.8	-	**26.8**
Total	**$9.0**	**$204.9**	**$192.4**	**$160.9**	**$110.5**	**$677.7**

* Approximately $200.5 million in additional expenditures are projected in FY 2027 utilizing funding from previously issued lease revenue bonds (Series 2025A), including $47.6 million for support the WIFIA match and $8.9 million for SAP Modernization.

The amount assumed for the CIP ($460.5 million excluding WIFIA projects) does not represent the funding needed for any specific project(s) or asset types within the CIP; rather, this amount reflects the City's anticipated capacity to issue debt for infrastructure projects over the next five years, which is based on Engineering & Capital Project's (E&CP) projected spending rate ($9-12 million per month or $110-120 million per year).

Short-term borrowings anticipated over the Outlook period are also included in the Outlook's projections. These consist of Equipment and Vehicle Financing Program (EVFP) financing costs for the replacement of one Police helicopter and one Fire-Rescue helicopter, as well as General Fund PC replacement needs.

Review of Debt Appropriations and Debt Ratios

As reflected in the adjacent table, there are currently $110.7 million in existing Council-approved debt appropriations which require funding from future financing proceeds.

Existing Appropriations Requiring Future Debt	
EXISTING APPROPRIATIONS	
CIP Appropriations	$ 892,462,362
Capital Equipment and Vehicle Appropriations	158,616,337
Total	**$ 1,051,078,699**
(LESS) EXISTING DEBT PROCEEDS	
Debt Issued and Expended	$ (500,942,882)
Unexpended Debt Available for Appropriations	(439,427,151)
Total	**$ (940,370,033)**
Remaining Balance	**$ 110,708,666**

In addition to this, the Department of Finance anticipates seeking future Council action to approve additional debt appropriations for remaining Stormwater WIFIA matching funds (estimated at $57.0 million) and the General Fund's SAP modernization costs (estimated at $35.7 million). Assuming these actions occur, overall debt appropriations will total $203.4 million. This compares against $677.7 million of debt assumed to

General Fund Debt and Appropriation Summary	
Existing Appropriations Requiring Future Debt	$ 110,708,666
Anticipated Remaining Stormwater WIFIA Match	57,028,143
Anticipated SAP Modernization	35,689,000
Total Existing and Anticipated Appropriations [A]	**$ 203,425,809**
Assumed New Debt Proceeds (FY 2027-2031) [B]	**$ 677,700,000**
Additional Debt Capacity [B] - [A]	**$ 474,274,191**

be issued over the Outlook period, which leaves $474.3 million in additional debt capacity to potentially support additional capital projects, as summarized in the table above.

Recent updates to the City's Debt Policy require that a capacity analysis be undertaken for inclusion in the Outlook to project the impact new debt issuances will have on the City's debt ratios. Our Office worked with the Department of Finance's Debt Management Division to prepare the following table which reflects the additional debt service costs (i.e., principal and interest) that are assumed to be incurred by the General Fund during the Outlook period, as well as the associated impacts to the City's debt ratios. As reflected in the table below, the City's debt ratios are projected to remain within Debt Policy parameters after accounting for projected debt service costs that are assumed to be incurred by the General Fund during the Outlook period.

General Fund-Backed Debt Service *($ in millions)*					
	Forecast FY 2027	**Forecast FY 2028**	**Forecast FY 2029**	**Forecast FY 2030**	**Forecast FY 2031**
Existing Debt Service (Short-Term)	$ 21.2	$ 19.8	$ 14.9	$ 12.8	$ 10.3
Existing Debt Service (Long-Term)	88.8	88.9	76.9	76.9	78.6
FY 2028 Proj. LRB Issuance ($406.3M)	-	9.1	24.9	24.9	24.9
FY 2030 Proj. LRB Issuance ($271.4M)	-	-	-	6.1	16.7
Stormwater WIFIA Loan ($359.2M)	2.3	4.1	6.4	9.0	15.1
New Short-term Debt Service [1]	5.8	10.8	16.6	24.0	32.1
Totals	**$ 118.2**	**$ 132.9**	**$ 139.7**	**$ 153.8**	**$ 177.7**
Pension and OPEB Costs	$ 413.5	$ 424.1	$ 369.2	$ 367.0	$ 366.8
General Fund Revenue [2]	$ 2,217.4	$ 2,277.6	$ 2,347.5	$ 2,416.1	$ 2,503.2
Debt Ratios					
10% Benchmark	**5.3%**	**5.8%**	**6.0%**	**6.4%**	**7.1%**
Inc. Pension/OPEB - 25% Benchmark	**24.0%**	**24.5%**	**21.7%**	**21.6%**	**21.8%**

[1] Short-term debt primerily consists of General Fund-backed Equipment and Vehicle Financing Program (EVFP) leases.

[2] Includes other operating funds currently being used for existing debt service (e.g. non-General Fund TOT).

Information Technology – Enterprise Resource Planning (ERP) Modernization

The City is planning to proceed with the replacement of its current SAP ERP system, which is anticipated to reach end of life on December 31, 2027. General Fund costs for this replacement total $60.8 million over the Outlook period, all of which are included in baseline expenditures.[13] The majority of this project is assumed to be debt financed, which is allowable because ERP systems are treated as essential public infrastructure projects that provide long-term public benefits, similar to physical assets. Another $17.7 million, however, is assumed to cover contractual licensing costs which are not eligible for debt financing, beginning with a $2.1 million expense in FY 2027 as noted on the table on the following page.[14]

[13] Note that this represents 44% of ERP Modernization costs; the remaining 56% will be borne by non-General Fund departments. The total cost for ERP Modernization over the Outlook period is projected to be $138.0 million.

[14] $17.7 million is the General Fund portion of these costs; non-General Fund costs are anticipated to total $48.9 million.

ERP Modernization Project - General Fund Portion Expenditures over the Outlook Period						
	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031	Total
Contracts and Services						
Ongoing Budget	$ 1.3	$ 1.3	$ 1.3	$ 1.3	$ 1.3	$ 6.5
Software as a Service Cloud Licensing	2.1	3.2	3.6	4.1	4.7	17.7
Total Contracts and Services	**3.4**	**4.5**	**4.9**	**5.4**	**6.0**	**24.2**
Debt Financing	8.9	13.5	10.5	2.8	0.9	36.6
Project Total	**$ 12.2**	**$ 18.0**	**$ 15.5**	**$ 8.2**	**$ 6.9**	**$ 60.8**

Specifically related to the General Fund, the table above shows $36.6 million being financed over the Outlook period; debt service costs for the project are discussed in the *Debt Financing* section above. Note, the debt financed amount in that section for FY 2031 differs from this, which reflects the most recent projections from the Department of IT.

OUTLOOK PRIORITIES BEYOND BASELINE EXPENDITURES

NEW FACILITIES

New Facilities
• Library • Parks and Recreation • Fire Stations

The Outlook includes forecasted funding for new Library, Parks and Recreation, and Fire-Rescue facilities assumed to open during the Outlook period. Opening dates for new facilities in the Outlook are not certain as timelines can be impacted by project delays. Furthermore, **given the likelihood for service-level reductions during upcoming budget cycles, the impacts of moving forward with new facilities while at the same time cutting or eliminating services at existing facilities will need to be taken into consideration**. If existing services, programs, and facilities are determined to be a higher priority, deferring the opening of new facilities should be considered.

A list of expenses for new facilities anticipated to open or become operational within the Outlook period is included in Attachment 1 to this report.

Library

The Library Department anticipates the completion of three library expansion/replacement projects during the Outlook Period: the City Heights Library Annex in FY 2027, the Ocean Beach Library expansion in FY 2028 and the replacement of the Oak Park Library in FY 2028. Given that these new facilities will replace/expand existing library branches, no new staffing is assumed; new costs for these facilities in the Outlook instead include increases in NPE, including energy and other utilities, janitorial services, and landscaping. Total projected annual costs are $8,500 beginning in FY 2027 and increase to $163,000 in FY 2031.

Our Office includes additional updates for these Library facilities:

- *FY 2027 – City Heights Library Annex Expansion*: Project is fully funded, and construction is currently underway on phase 1; phase 2 is anticipated to begin in early-2026 and be completed in March/April 2026. The facility is anticipated to open by Summer 2026.
- *FY 2028 – Ocean Beach Library Expansion*: Project is fully funded; design build contract is anticipated to be awarded in Spring 2026, with groundbreaking in July 2026 and project completion in FY 2028.
- *FY 2028 – Oak Park Library (Replacement)*: Project is fully funded; design build contract has been awarded. Project design is anticipated to be finalized in FY 2026 and construction completion in FY 2028.

Parks and Recreation

The Parks and Recreation Department anticipates 20 new or expanded parks to open, and 14 new Joint Use facilities with local school districts allowing shared use of various recreation facilities. The Outlook projects new expenses for park facilities to total $6.8 million in FY 2027, which increases to an aggregate expense of $10.4 million in FY 2031; included in this aggregated expense is the addition of 63.00 FTE positions in total over the Outlook period to maintain the new parks and playgrounds. We note that most of the required positions (42.00 FTES) are needed in FY 2027 when 12 new parks and four Joint Use facilities are assumed to open. Staff indicate that the opening dates of new parks and joint use facilities will be reevaluated as the budget process approaches.

Fire Stations

The Outlook assumes funding for operational expenses at two new fire stations assumed to open during the Outlook period. Total assumed staffing needs and annual costs include 12.00 FTEs and $2.6 million beginning in FY 2028, increasing to 39.00 FTEs and $9.1 million in FY 2031. The two new fire stations identified in the Outlook are listed below:

- *FY 2028 – Fire Station 48: Black Mountain Ranch (primarily developer funded):* Project is currently in design and construction is anticipated to be completed in FY 2028, with the station opening around June 2028. The current funding gap for the project is estimated to be approximately $1.0 million given increased obligations related to a required water line relocation and the environmental permitting for the project.
- *FY 2029 – Fire Station 49: Otay Mesa:* Project is nearing the end of an environmental analysis phase to determine CEQA compliance and is anticipated to move to bid and award in early-2026; construction is anticipated to be completed in FY 2030, opening around October 2029. The funding gap for this project is currently projected at $33.9 million; however, an engineering cost estimate will be procured as soon as CEQA compliance is determined to provide a more accurate funding need. Tax increment revenue from the Otay Mesa Enhanced Infrastructure Financing District (EIFD) is anticipated to fund design and finance construction costs.

HOMELESSNESS PROGRAMS AND SERVICES

The Outlook includes anticipated funding needs to support existing homelessness services and programs as priorities beyond baseline expenditures. In the FY 2026 Adopted Budget, the $53.8 million Homelessness Strategies and Solutions Department (HSSD) budget is primarily funded through $32.6 million from Measure C revenue, $17.0 million from TOT reimbursements, $3.0 million from Opioid Settlement Funds, and $611,000 from grant reimbursements – with only $632,000 in direct General Fund support.

The Outlook incorporates projections for these revenues and reimbursements, as well as additional one-time County, State, and federal grant funds the City expects to receive during the outlook period. However, in contrast to past outlooks, additional State Homeless Housing, Assistance and Prevention Program (HHAP) grants are not anticipated after FY 2028 given uncertain future State funding. Due to an anticipated reduction in the next round of State HHAP funds along with changes in projected TOT reimbursements and Measure C revenue, the Outlook identifies the need for $15.0 million (in FY 2027) to $27.9 million (by FY 2031) in additional resources to maintain current service levels during the outlook period.

Regarding revenues, the Outlook assumes the use of one-time Measure C funds that is subject to change. As discussed in the FY 2026 First Quarter Budget Monitoring Report, the City began proactively collecting Measure C funds on May 1, 2025. Due to a delay in the resolution of pending litigation on Measure C into FY 2026, $5.9 million in Measure C revenue collected in FY 2025 will be available to support eligible FY 2026 expenditures. These one-time Measure C funds could help address a probable General Fund revenue shortfall in FY 2026, including from declining TOT revenue, or mitigate a homelessness funding gap due to HHAP funding reductions in FY 2027. The Outlook assumes the latter option.

Specifically, the Outlook assumes the addition of $5.9 million in one-time Measure C revenue for homelessness services in FY 2026 along with a corresponding reduction of $4.2 million in the use of State HHAP funds and the remaining difference offsetting a reduction in projected FY 2026 Measure C revenue ($1.1 million) and General Fund support ($632,000). As reflected in the table below, the Outlook anticipates less carryover HHAP funding from prior rounds, reductions in the next HHAP funding round (HHAP Round 7) anticipated in FY 2028, and no future State homelessness funding. The use of the $5.9 million from Measure C to primarily offset State HHAP funding in FY 2026 would preserve more HHAP funding for use in FY 2027, when such funds will be more limited. This approach avoids an otherwise larger homelessness funding gap in FY 2027.

Five-Year Outlook Projected State HHAP Fund Availability ***(in millions)***

State Grant	Total Funds	FY 2026	FY 2027	FY 2028	FY 2029-FY 2031
HHAP Round 1-4	$ 83.1	$ 1.2	$ -	$ -	$ -
HHAP Round 5	29.9	12.9	-	-	-
HHAP Round 6	25.8	6.1	19.7	-	-
HHAP Round 7 *(estimated)*	12.9	-	-	12.9	-
	Total	**$ 20.2**	**$ 19.7**	**$ 12.9**	**$ -**

However, the Department of Finance indicated the use of one-time Measure C funds to offset State HHAP is subject to change. For instance, the $4.2 million in the Outlook's planned reduction of FY 2026 HHAP use could instead offset $4.2 million in TOT reimbursements budgeted for homelessness that could be reallocated to reimburse other eligible General Fund expenditures in FY 2026, to the extent such TOT funding is available. As the $5.9 million in one-time Measure C funds are already being partially used to offset lower FY 2026 Measure C revenue projections ($1.1 million) and General Fund support ($632,000) in the Outlook, only $4.2 million may be available to help reimburse other eligible General Fund expenditures in this manner.

As a result, use of HHAP funds would then be increased by $4.2 million from $20.2 million to $24.4 million in FY 2026, reducing the amount of HHAP funds available in FY 2027 by the same amount. Under this scenario, the FY 2027 homelessness funding gap would grow to $19.2 million as less HHAP funding would be available, as seen in the table below, but the General Fund revenue shortfall in FY 2026 would be lessened. Our Office will continue to monitor General Fund revenues and expects more clarity on the use of the one-time Measure C funds by the Mid-Year Report.

Use of Measure C Funds Affects Homelessness Funding Gap

	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
Five-Year Outlook: Measure C Offset HHAP Decline	$ (15.0)	$ (21.2)	$ (21.4)	$ (20.8)	$ (27.9)
Alt. Scenario: Measure C Offset General Fund Shortfall	$ (19.2)	$ (21.2)	$ (21.4)	$ (20.8)	$ (27.9)

The Outlook also incorporates a planned reduction in Measure C revenue for homelessness starting in FY 2031, as the measure provides 41% of Measure C revenue to homelessness for the first four years of tax collection, after which homelessness would receive 31% and street repair would receive 10%. This corresponds to a $7.7 million year-over-year drop in projected Measure C revenue and contributes to a $7.1 million increase in the homelessness funding gap in FY 2031.

Regarding expenditures, there are some pending program changes that could affect FY 2027 planned expenditures. We note that $1.3 million included for homelessness diversion in the HHAP Round 6 Funding Plan, approved by Council on July 14, 2025 and budgeted for FY 2026 and FY 2027, remains in development as the Department and the San Diego Housing Commission (SDHC) continue discussions on program scope. Should the diversion program consist of entirely new expenditures without offsetting existing expenditures or new revenue, the homelessness funding gap in FY 2026 and FY 2027 would increase by a corresponding amount. Additionally, a second year of funding for the Safe Parking at the Old Central Elementary site is not reflected in the Outlook, because of uncertainty over the development timeline at the site. The first year of site operations[15] was funded through Council action in the FY 2026 Adopted Budget. SDHC staff anticipate requesting funding, likely not to exceed $375,000, to operate the site through June 2027 as part of FY 2027 budget development. Separately, according to Department staff, no shelter relocations or closures are currently anticipated, but moving forward, replacement beds for any shelter relocations would likely be subject to the availability of funds.

The table on the following page shows the anticipated expenditures associated with existing homelessness services in FY 2027 by the General Fund, as well as State and federal grant funds. The anticipated expenditures needed for existing programs and planned commitments totals $85.8 million. Only $70.8 million has been identified to support these expenditures, leaving a shortfall of $15.0 million. The identified resources include $32.2 million from Measure C revenue, $14.2 million from TOT, $2.5 million from Opioid Settlement Funds, $1.6 million from various non-HHAP grant funds, and $611,000 from grant funded General Fund reimbursements. Additionally, the City anticipates receiving drawing down $19.7 million remaining from HHAP Round 6 in FY 2027 and exhausting the full allocation of HHAP Round 7 estimated to be $12.9 million in FY 2028. The projected funding need for these programs may change depending on how much State grant funding awarded in previous years can be carried forward into FY 2027 and the possibility of future State HHAP funds.

[15] For reference, the contract for Safe Parking at Central Elementary runs from November 17, 2025 through November 16, 2026 and allocates a total of $593,000 (including admin), of which $343,000 is from the Regional Taskforce on Homelessness and the remaining $250,000 from City General Fund.

Breakout of FY 2027 Homelessness Planned Commitments *(Subject to Change)*			
System Component	**Programs**	**Unit Count**	**Anticipated Funding Needs**
Housing & Services[1] **$7.1 million**	Housing Instability Prevention Program	300 households	$ 5,984,000
	Diversion - Family Reunification		861,000
	Prevention Program - EDD		271,000
Crisis Response & Stabilization **$60.2 million**	Shelters		
	Bridge Shelter - 16th and Newton	326 beds	7,794,000
	Women and Family Shelter	210 beds	5,790,000
	Bridge Shelter - 17th and Imperial	140 beds	4,181,000
	Single Adult & Senior Interim Shelter (VVSD)	130 beds	3,727,000
	Domestic Violence Shelter	160 beds	3,000,000
	Family Non-Congregate Shelter	168 beds	2,447,000
	Youth Case Management & Shelter	67 beds	2,442,000
	LGBTQ+ Youth Services and Shelter	43 beds	2,075,000
	Connections Interim Housing	70 beds	2,056,000
	Veterans Interim Shelter (VVSD)	40 beds	1,118,000
	South County Lighthouse Interim Shelter	37 beds	1,012,000
	Family Semi-Congregate Shelter	93 beds	737,000
	Bishops Shelter	28 beds	665,000
	System-wide Shelter Ancillary		605,000
	Substance Use Disorder Shelters & Services		
	Harm Reduction Interim Shelter	44 beds	2,241,000
	Alcohol Use Disorder Interim Shelter	56 beds	772,000
	Safe Haven	22 beds	453,000
	Safe Sleeping		
	Safe Sleeping Ancillary		7,451,000
	20th and B Street Lot	189 tents	5,210,000
	"O" Lot at Balboa Park	581 tents	2,219,000
	Safe Parking Programs		
	Safe Parking Programs (incl. H-Barracks)	295 spaces	4,127,000
	Safe Parking Ancillary		103,000
Engagement Services **$9.8 million**	Outreach		
	Coordinated Street Outreach		3,611,000
	Downtown Street Outreach		1,218,000
	Community CARE Events & Outreach HUB		26,000
	Storage		
	Storage Connect Center I	500 bins	1,635,000
	Think Dignity Storage Facility	400 bins	251,000
	Other		
	Homelessness Response Center		1,064,000
	Day Center for Homeless Adults		978,000
	Public Restrooms		774,000
	Coordinated Shelter Intake Program		243,000
Administration **$8.7 million**	HSSD Administration[2]		7,645,000
	SDHC Administration		1,024,000
	HMIS Set Aside		31,000
		Total Expenses	**$ 85,842,000**
		Projected Grant and Ongoing General Fund Revenue Available	**$ 70,805,000**
		Funding Gap	**$ (15,036,000)**

Notes: Table only includes programs in the Homelessness Strategies and Solutions Department Budget.

[1] Eviction Prevention Program is funded under the Economic Development Department (EDD) budget.

[2] Of the total, $3.3 million supports HSSD staffing/coordination of City services, $3.2 million for non-discretionary expenses primarily shelter and Safe Storage leases, $1.1 million for supplies, and $14,000 for training and travel.

As Council thinks about the upcoming budget process as it relates to addressing homelessness, it is important to keep in mind how the City's existing programs advance the ambitious goals of the Community Action Plan on Homelessness Update (Update), heard by Council on May 20, 2025. This perspective is especially important given the limited budget resources and the anticipated shortfall for homelessness programs in the Outlook. Because there is a severe lack of funding to fully fund the Update's strategies, prioritization is needed to determine what goals are feasible with limited budget resources. For instance, the Update identified that for every one new shelter bed, on average, there should be around seven new prevention and diversion resources and eleven new permanent housing resources – suggesting that resource allocations across available funding sources should prioritize prevention, diversion, and permanent housing resources. However, most appropriately and efficiently targeting such resources to households where intervention would make a significant difference in preventing homelessness also requires careful consideration.

In preparation for upcoming budget decisions in FY 2027, Council may wish to re-evaluate existing homelessness programs and identify key strategic homelessness priorities for the limited available resources, as well as opportunities to either increase non-General Fund resources or reduce expenditures – for instance, through further program consolidation or cuts – while still considering program outcomes. Our Office will continue exploring options and compiling program outcome data for the Council to consider.

ADDITIONAL FUNDING NEEDS NOT INCLUDED IN OUTLOOK

The Outlook also includes sections on *Future Fiscal Considerations* and *General Fund Infrastructure Needs*. These sections cover certain City policies, programs, and requirements that could have a potential impact on City expenditures which are not currently included in the Outlook's projections. For this report, we provide additional context on specific areas of impact noted in the Outlook, as well as review of two specific Council priorities that are not discussed in the Outlook.

OPERATING NEEDS

The Outlook discusses numerous financial and operational issues related to the delivery of services provided by the City. This includes many items that are also Council budget priorities, including Climate Action Plan implementation, the Zero Emissions in Municipal Buildings and Operations Policy (ZEMBOP) and Fleet Electrification, improving and preparing a current condition assessment of City facilities, and the City's Compensation Philosophy. City staff is developing strategies to address many of these issues without the need for additional funds, including building electrification and rehabilitation projects through Energy Savings Performance Contracts, integrating Climate Action policies into already existing procedures, and seeking outside funding and grants for various upfront costs for EV chargers, electrification and charging upgrades, tree planting, and other work. As staff continues to work on these areas, it will be important to track future budget considerations and needs since, as our report discusses, the City currently lacks sufficient resources to maintain its current operations.

Beyond these initiatives, our report provides additional detail on two items of concern: continued General Fund impacts from City collection services activities, and two Council priorities that are not discussed in the Outlook report.

<u>Solid Waste Management – General Fund Impacts</u>

The Outlook notes potential General Fund impacts due to Solid Waste Management activities from three sources: 1) costs incurred for eligible customers receiving increased service levels in FY 2026, 2) costs incurred from ineligible customers that have not transitioned to private haulers, and 3) funding for a financial assistance program.

The first two sources should be one-time impacts, and they should largely impact FY 2026 as opposed to subsequent years. As noted in the Outlook, the costs incurred for eligible customers receiving increased service levels was already anticipated to require a one-time General Fund payment anticipated in FY 2026 of $10.0 million in order to prevent the Solid Waste Management Fund from ending the year with a significant negative fund balance.

For costs incurred from ineligible customers that have not transitioned to private haulers, our understanding is that this number continues to decline, with fewer than 5,000 properties still needing to transition. While there is an anticipated cost of $5.0 million for services in FY 2026, this number could potentially decline as fines begin to be levied against properties that have yet to transition. These fines are anticipated to be levied soon, and should be set as such to ensure that the City is recovering its costs to provide service to these properties. At a minimum, fines for properties that fail to transition should be set to prevent the need for a General Fund subsidy of the Solid Waste Management Fund, though ideally, they should be set at an amount that actively encourages properties to complete the transition to private haulers. **Our Office recommends that the Department of Finance include these amounts when developing projections for the Mid-Year Report.**

Finally, the Outlook assumes an ongoing appropriation of $3.0 million in General Fund dollars for a financial assistance program, equal to the amount budgeted in FY 2026. Two important considerations remain. First, the actual program has not been fully developed and approved by the Council, and it is unknown whether this level of funding is sufficient to match the Council's subsidy goals. Second, once those subsidy goals are set, maintaining the funding at a flat dollar amount will result in declining levels of support for recipients relative to collection fees which increase in outer years to account for increasing costs and expanded services. Unless the General Fund amounts grow at a similar rate, the level of subsidy or the number of recipients would need to decrease.

Other Council Priorities

While many of the recent budget priorities conveyed to the Mayor by the City Council focused on the maintenance of services currently rendered, there were some priorities that will require additional funds beyond what is included in the Outlook. While these remain priorities of the Council, it should be noted that increasing financial resources towards unfunded or underfunded priorities will require reductions in other expenditures in FY 2027. Two priorities not funded in the Outlook to full Council policy or priority level are discussed below.

Arts and Culture

The Outlook assumes an increase of $500,000 in funding for arts and culture from the FY 2026 funding level of $13.9 million. In their initial FY 2027 budget priorities memoranda, six Councilmembers expressed various levels of support for funding arts and culture programs. Information on the various funding levels is in IBA Report 25-32 REV.

The Outlook projects funding for arts and culture in FY 2027 to be $14.4 million, 4.5% of total projected TOT revenue, which is $0.2 million more than the figure ultimately approved by the full Council as part of the FY 2027 Budget Priorities Resolution. However, to fully fund the Penny for the Arts goal in FY 2027, which was supported by two Councilmembers in their budget priorities memoranda, an additional $16.3 million in arts and culture expenditures would be required above what is included in the Outlook.

The table on the following page reflects the projected funding level for arts and culture programs over the Outlook period. We note that the dollar amount allocated to arts and culture program funding in the five-year Outlook period remains flat, except for annual 2.0% increases to the Cultural Affairs Division's administrative costs. Since overall TOT revenue is projected to increase on-average by 2.1% annually over the Outlook period, the annual funding gap to reach the Penny for the Arts goal gradually increases over time as well.

Arts and Culture Funding Levels *($ in millions)*										
	FY 2027		FY 2028		FY 2029		FY 2030		FY 2031	
Total Citywide TOT Projection [a]	$322.1		$329.8		$336.4		$343.2		$351.8	
A&C Funding Level in Outlook	$14.4		$14.4		$14.4		$14.5		$14.5	
A&C Funding Level % of TOT [b]	4.5%		4.4%		4.3%		4.2%		4.1%	
Funding Target Scenarios (%)	**6.5%**	**9.5%**	**6.5%**	**9.5%**	**6.5%**	**9.5%**	**6.5%**	**9.5%**	**6.5%**	**9.5%**
Funding Target Scenarios ($)	$20.9	$30.7	$21.4	$31.4	$21.9	$32.0	$22.3	$32.7	$22.9	$33.5
Funding Gap	**($6.6)**	**($16.3)**	**($7.0)**	**($17.0)**	**($7.4)**	**($17.6)**	**($7.8)**	**($18.2)**	**($8.3)**	**($19.0)**

[a] Excludes revenue from RV parks as that goes directly into the General Fund.

[b] To meet the Penny for the Arts blueprint goal of 1¢ of the City's 10.5¢ TOT rate, the target percentage is 9.5%

SD Access4All

Council's Budget Priorities Resolution supported funding SD Access 4 All, which provides public WiFi access in City parks and libraries, a mobile hotspot lending program (through public libraries), digital literacy and navigation services, and public outreach activities. $1.3 million for these services is included in Outlook's baseline. While all core SD Access 4 All services now have dedicated ongoing funding, the mobile hotspot program was reduced from $875,000 in the FY 2025 budget to $336,000 in FY 2026, which decreased the mobile hotspots available for lending by 50% from 4,000 to 2,000 units. The reduction during the FY 2026 budget process assumed the City would be awarded E-rate grant funding for this purpose. However, on September 30, 2025, the Federal Communications Commission determined E-rate grants could not be used for mobile hotspot lending services.

$464,000 is the most recent estimated cost to add 2,000 units to restore the prior core service level of 4,000 mobile hotspots. The 2,000 existing units are currently distributed to all 37 libraries, with branches in high priority areas receiving a larger allocation of hotspots.[16]

INFRASTRUCTURE NEEDS – DEFERRED MAINTENANCE AND CIP

The Outlook discusses long-term structural challenges associated with the City's major General Fund-supported infrastructure assets – including its transportation network, stormwater systems, and facilities. The costs associated with maintaining and upgrading these systems are substantial and continue to grow each year. These pressures reflect not only deferred maintenance accumulated over decades, but also increasing regulatory requirements, aging and obsolete infrastructure, and the rising cost of materials and construction.

Across all General Fund asset types, funding levels remain far below what is needed to maintain a state of good repair. Streets require sustained operations, maintenance, and capital investment simply to prevent further deterioration. Streetlights face significant pressures due to aging electrical circuits and State-mandated Underground Locate responsibilities. Sidewalk repair and replacement needs continue to expand, including the existing backlog of temporary fixes and ADA obligations. Stormwater infrastructure has the largest funding gap, with billions in unfunded mandates tied to flood control and water quality compliance. Facilities lack updated condition assessments, and the backlog of repairs may now exceed $1 billion.

[16] To allocate hotspots, Library assessed circulation trends and community demand and generally provides higher allocations in Communities of Concern including Council Districts 4, 8, and 9.

Collectively, these needs represent a structural deficit that extends beyond the City's operational shortfalls. The most recent Five-Year Capital Infrastructure Planning Outlook (CIP Outlook) identified a $6.51 billion General Fund capital infrastructure gap, a 281% increase since FY 2016 that underscores the fact that the City is facing a long-term infrastructure funding challenge that cannot be addressed through existing revenue sources, one-time allocations, or current debt capacity. The General Fund's limited capacity to fund capital through issuances of debt that are still insufficient to close the capital funding gap will also further constrain resources available for core operating services.

Further, not addressing these issues will also lead to additional emergency spending in both the near and long term. Emergency spending on stormwater projects has tripled in the past three years, and failure to properly maintain facilities in a state of good repair already results in significant spending, such as emergency repairs to lifeguard stations to keep them operational, requiring already limited resources to have to be redeployed to these costly endeavors. Without a concerted effort to improve the City's infrastructure, additional failures will occur, requiring facility closures, costly emergency repairs, and other diversions of limited resources to support emergencies.

RESOURCE AND MITIGATION CONSIDERATIONS

CONSIDERATIONS FOR FY 2027

Given the Outlook's first year serves as a preview of what is anticipated for the FY 2027 budget, the Outlook's projected $88.8 million deficit for FY 2027 clearly demonstrates the need for mitigation measures. To adopt a balanced budget for the *current* year, FY 2026, the City implemented a number of significant additional revenues to help reduce expenditure cuts needed to close the FY 2026 deficit. Additional actions will be required to bring FY 2027 into balance; while some resource mitigations may be available for FY 2026, it will be necessary to lean more heavily on budget cuts to close the projected FY 2027 deficit. The City lacks the revenues necessary to maintain its current service levels and to address its infrastructure needs.

This section discusses potential mitigations for FY 2027. We begin by noting that existing amounts relied on or contemplated in the past, such as reserves and excess equity, will be limited or unavailable, then discuss some potential limited revenue options; and finally discuss the need for expenditure reductions.

General Fund Reserve and Excess Equity

General Fund Reserve (contributions already discounted from the Outlook and balance is lower than policy target)

The City's General Fund Reserve is currently funded at $207.1 million, which is below the FY 2026 Reserve target of $262.9 million (or 14.1% of the most recent three-year average of operating revenues).[17] The City elected to waive General Fund Reserve contributions in FYs 2024, 2025, and 2026 in order to fund other critical expenditures – resulting in this $55.8 million shortfall.

Unlike prior Outlooks, the current Five-Year Financial Outlook does not assume contributions to the General Fund Reserve (or Risk Management reserves) in its baseline expenditures, as the Department of Finance is working to revise the City's Reserve Policy, which calls for an ultimate goal of reserves funded at 16.7% of operating revenues, to better align with the City's current fiscal situation. Under the revised policy, contribution amounts may not be required annually and would therefore be excluded from the ongoing baseline. That noted, had the Outlook included a General Fund Reserve contribution pursuant to the City's current Reserve Policy, consistent with the approach in prior Outlooks, the deficit for FY 2027 would have been significantly higher.

The City's General Fund Reserve should not be used as an *ongoing* resource, though there can be times when it is appropriate to use reserves to provide for continuity of service, such as during temporary revenue dips, after which revenues can recover or expenditures can be restructured. Notably, forgoing Reserve contributions in FY 2024-2026 was essentially the equivalent of using the Reserve to support City operations in those years.

[17] The current Reserve balance and FY 2026 Reserve target amounts are based in part on FY 2025 unaudited actuals; as such they are pending completion of the audit of the City's FY 2025 financial statements – anticipated in December.

We anticipate the revisions to the City's Reserve Policy will take into account times when steady contributions to the Reserve may not be achievable. However, we stress the importance of maintaining a healthy General Fund Reserve to allow the City to better weather economic headwinds and to improve the overall fiscal health of the City. As such, we recommend the City not draw from the General Fund Reserve while also forgoing Reserve contributions.

Based on the Reserve Policy in place today, and revenue estimates included in the Outlook, forgoing a Reserve contribution in FY 2027 will increase the Reserve shortfall to an estimated $80.4 million, and its funding level will drop to 10.6% of operating revenues.

General Fund Excess Equity (none currently available)
In previous years, General Fund Excess Equity[18] was often a resource used to close budgetary shortfalls, but none is currently anticipated to be available in FY 2027 – though this could change with the Mid-Year Report projections. Although it was anticipated that FY 2025 would only require use of $84.4 million in available Excess Equity, the fiscal year closed out requiring the full $105.0 million[19] available, leaving nothing for FY 2026 should revenue fall short, or expenditures exceed projections.

The potential for Excess Equity to be generated in FY 2026 through mitigating actions or higher than anticipated revenues exists, though the First Quarter Report reflects both lower-than-budgeted revenues and higher-than-budgeted expenditures in select departments. If savings do materialize, they could be used to mitigate the FY 2027 projected shortfall, though at this time they should not be relied on. The first comprehensive projections of the City's current-year finances will not be available until the Mid-Year Report is released in January.

Near-Term Revenue Options are Limited
The City has made progress towards reducing the structural budget deficit in its current-year budget, but a nearly $90.0 million shortfall is still projected in FY 2027, even when assuming no new programs or program expansions. The FY 2026 budget included implementation of several new or expanded revenues, including a solid waste collection fee, increasing the Transient Occupancy Tax consistent with 2020's Measure C, user fee adjustments, and various parking initiatives. Looking to FY 2027, near-term revenue options available are significantly more limited. Two potential resources are discussed below, though we strongly caution against relying on either until and unless final actions are taken to fully implement them.

Beach and Bay Parking (timeline could possibly extend past FY 2027)
Several Councilmembers have discussed paid beach and bay parking, particularly for non-City residents, as a new budget resource to explore. Given the need for legal review and the need to obtain Coastal Commission approval prior to implementation, it is unknown whether this revenue

[18] General Fund Excess Equity is described as "Unassigned Fund Balance that is not otherwise designated as General Fund Reserves and is available for appropriation" which generally results from unexpected increases to General Fund revenues or decreases in expenditures during any given fiscal year.
[19] The depletion of Excess Equity is based on FY 2025 *unaudited* actual activity; year-end amounts are not considered final until completion of the audit of the City's FY 2025 financial statements – anticipated in December.

source would be available for FY 2027, though it could benefit future years. Given the timeline involved, this revenue source is unlikely to generate a significant amount of funds relative to projected FY 2027 deficit. **Finally, if this revenue option is pursued, we recommend against budgeting revenue prior to adoption of a Council-approved policy**.

Grants – State or Federal Funding (one-time)
The City regularly applies for grant funding, and grants have been an important source of funds for City projects in the past. In FY 2025, the City applied for 111 grants valued at almost $600 million, an 80% increase in the dollar value of applications from FY 2024, and was awarded 36 grants valued at $164.2 million. Grant awards range across a broad spectrum, including homelessness and housing, public safety and emergency services, environmental sustainability, transportation, and infrastructure. While the current federal Administration has implemented several changes resulting in reductions in federal funding for grants, the City Grants Team has provided departments with informal guidance on applying for federal grants in the current environment and continues to actively pursue federal and State grants.

As grants are typically one-time funding sources and vary from year to year, their use should be targeted for one-time expenditures, and not the ongoing baseline expenditures included in the Outlook.

<u>Focus on Expenditure Cuts</u>
Given the limitations of near-term revenue options, balancing FY 2027 will require reductions to existing expenditures and service levels. This section covers both budget reductions and mitigations that have already been requested by the Mayor, as well as a discussion of aligning the City's programs and services with the resources it has to provide those services.

Budget Reductions (ongoing)
On November 14th, the Mayor released a memorandum requesting City departments prepare budget reduction proposals for FY 2027 as options for consideration, and noting the implementation of mitigating actions for the current year. All General Fund departments were provided target reductions of 7%, except for Police, Fire, Office of Emergency Services, HSSD, and Transportation, which were given a reduction target of 3.5%. Departments were instructed that "[a]ny program or function deemed non-critical, in the context of the City's limited resources, must be entered into the City's budget system as a budget reduction proposal." The administration indicated that its aim is to first focus on eliminating or reducing non-core and non-mandated services. Additional key parameters include:

- Developing long-term solutions to address the City's structural budget deficit that extend beyond FY 2027
- Limiting budget additions only to mandated requirements

The memorandum also reinstated several mitigation measures with the aim of generating savings to offset the projected current year revenue shortfall or to use in FY 2027. These actions include:

- Reinstating the Request to Fill process

- Suspension of discretionary spending and non-essential overtime
- Zero-based review of external contracts

This direction continues several years of budget reduction requests. While not all reduction proposals will be taken, some will be unavoidable if the City is to close its deficit; when contemplating which reductions to implement, we encourage the administration to consider impacts to City residents, employees, and stakeholders, and to use clear metrics – including equity metrics – to inform decisions. In FY 2024, all City departments were directed to find 2% efficiency reductions in their FY 2024 budgets, and to include those reductions in their FY 2025 budget requests. Per the FY 2026 Adopted Budget publication, budget reductions totaled $114.7 million and 194.52 FTE positions were reduced.

Continued Need for Structural Realignment

The City made progress towards reducing its structural budget deficit in FY 2026, but closing the budget deficit in FY 2027 will require additional ongoing reductions, and it will be progressively more difficult for departments to identify one-time solutions that have not already been exhausted. Although the Outlook shows the deficit dropping considerably in FY 2029, even then there is still a baseline deficit of over $50 million. This ongoing gap underscores the need for multi-year, structural realignment of expenditures with ongoing sustainable resources.

As the City considers this realignment, we encourage it to *identify and prioritize those programs and services that are particularly critical*, and to fund departments that provide those services at levels that allow for success. This exercise will also require identifying reductions in non-essential services, and should consider potential disparate impacts of those reductions. While cuts to existing services will be difficult, it is likely the City will ultimately be better served by providing fewer services well than more services poorly.

Beyond this, the City should work to mitigate ongoing expenditure increases that would be partially supported by one-time solutions. Given the reality that budget cuts will be required in FY 2027, and that any expenditure increases in one area will require further offsetting cuts in other areas, Council should also **carefully consider the 2.94% wage increase** (translating to an estimated $29.2 million) assumed in the Outlook, and also consider areas where services can be aligned with anticipated available resources such as **examining and reprioritizing existing homelessness programs informed by program outcomes and reassessing the timing of new facilities**.

It is critical the City be open and transparent about the insufficiency of its existing resources to provide existing programs and services, especially if it elects to pursue future revenue measures, which will be discussed in the next section. In the absence of major new sources of revenue, it is equally important to align ongoing expenditures with ongoing resources so that if and when new revenue sources *do* materialize through increased taxes or fees, residents see a commensurate higher level of service.

POTENTIAL RESOURCE OPTIONS AFTER FY 2027

Looking beyond FY 2027, various revenue and resource options exist that could support needed or expanded City services. Some of those options are discussed in this section, though it should be noted that all would be subject to voter approval.

Potential Resource Options: After FY 2027
• Future Sales Tax Measure
• Future General Obligation Bonds
• Future Stormwater Fee Increase
• Future Property Transfer Tax Increase
• Future Vacation Home Tax

Potential Future Sales Tax Measure (ongoing)
The sales tax rate in the City is 7.75%, of which 1.0% goes to the City. If a 1.0% sales tax rate increase in the City to 8.75% was effective in FY 2027, it would generate an additional $360 million to $400 million in revenue for the General Fund.

The City put forward a one-cent sales tax measure on the November 2024 ballot that narrowly failed. The potential to put another sales tax increase measure on a future ballot exists, and if passed, it would have the potential to generate significant additional revenue to support core City services and infrastructure, though the City's existing structural budget deficit will have to be addressed in the short-term.

Potential Future General Obligation (GO) Bonds (one-time)
A General Obligation (GO) bond program could provide a dedicated funding source to help address the City's $6.5 billion deferred capital backlog and free up other funding sources for operations and maintenance. GO Bonds offer access to relatively low-cost borrowing and can establish a long-term funding stream outside of the General Fund. Many other large cities use GO Bonds to finance infrastructure projects such as streets, drainage, libraries, parks, housing and shelters, and public safety facilities. In recent years, GO Bond programs in cities like San Francisco, CA, Phoenix, AZ, and San Antonio, TX, have provided $390.0 million to $1.2 billion for these projects.

GO bonds generally include specific projects to be implemented with the bond funds, and public committees can be used to identify priority projects and provide oversight and accountability to ensure funds are spent on these projects as intended. In California, GO bonds require two-thirds voter approval because they are paid through additional levies on property taxes. For reference, issuing $100 million in GO bonds would increase annual property taxes by approximately $1.50-$1.75 per $100,000 of assessed value.

Potential Future Stormwater Fee Increase (ongoing)
The City has long discussed a potential stormwater fee to address operational and capital needs. In January 2021, the Stormwater Department proposed a Funding Strategy outlining stormwater needs and funding options, leading to a draft ballot measure in February 2022. This measure proposed a 4 to 5 cent per square foot impervious surface tax, which would have generated $74.0 to $93.0 million annually and cost single-family homes $10 to $14 a month. However, it was not pursued due to the requirement for two-thirds voter approval and polling that indicated insufficient support.

After the January 2024 storms, Council's Rules Committee revisited the issue, and considered a similar measure with a 7 cent per square foot tax which was estimated to generate $129.6 million annually. Again, the measure was dropped due to the high voter threshold.

An alternative under Proposition 218 allows for a property-related stormwater fee via a mail ballot to property owners, requiring a simple majority approval. This approach, used by some other cities, requires a cost-of-service study to ensure fees align with service costs. Implementing this method, however, would still require a public vote, and would require additional time, research, and resources. For more information on stormwater fees and the fee approval process, please refer to IBA Report 21-04 *Analysis of the Stormwater Division Funding Strategy Report*.

Potential Future Property Transfer Tax Increase (ongoing)
Property transfer taxes, also known as real estate transfer taxes or documentary transfer taxes, are levied on any real property that is sold or transferred. In San Diego, the county and city each receive $0.55 per $1,000 of the sale price of the property.

Increases to property transfer taxes are possible through a vote of the people (a simple majority for general use or a two-thirds vote for specific uses). Several other California cities have adopted property transfer tax rates that increase progressively with the sale-price of properties. Cities with similar median home prices to San Diego who have adopted progressive transfers taxes, include San Francisco[20] ($5.00 to $60.00 per $1,000), Culver City[21] ($0.45 to $4.00 per $1,000), Los Angeles[22] ($0.45 to $5.95 per $1,000), and San Jose[23] ($0.75 to $1.50 per $1,000).

In FY 2026, the revenue from the existing property transfer tax of $0.55 per $1,000 of property value is projected to generate $11.5 million for the General Fund. A voter-approved increase to $1.10 per $1,000 could double this amount to $23.0 million.

Potential Future Vacation Home Tax (ongoing)
The City currently has a one-time application fee and an ongoing licensing fee for permitted Short-Term Residential Occupancy (STRO) listing in the City of San Diego. There is currently no fee on vacation homes/second homes.[24]

[20] "Transfer Tax." *City & County of San Francisco Office of the Assessor-Recorder.* www.sfassessor.org/recorder-information/recording-document/transfer-tax. Accessed January 6, 2025.

[21] "Real Property Transfer Tax." *City of Culver City.* www.culvercity.org/Services/Make-a-Payment/Real-Property-Transfer-Tax. Accessed January 6, 2025.

[22] "Real Property Transfer Tax and Measure ULA FAQ." *City of Los Angeles Office of Finance*. finance.lacity.gov/faq/measure-ula. Accessed January 6, 2025.

[23] "Measure E." *City of San José City Clerk.* www.sanjoseca.gov/your-government/appointees/city-clerk/elections/2020-elections/measure-e. Accessed January 6, 2025.

[24] Vacation homes/second homes are defined as properties that certify they are exempt from paying the City's Rental Unit Business Tax (RUBT) because the property is not available for rent any part of the tax year and not reported on any tax forms as an income generating property. This is one of ten potential RUBT exemptions.

At an October 22, 2025 Rules Committee meeting, a proposal by Councilmember Elo-Rivera regarding a tax on STROs and vacation/rentals was considered, and the Committee, by a 3-1 vote (with one member absent) requested the City Attorney's Office return to the Rules Committee with ballot measure language to tax Tier 3 and 4 STROs and vacation homes/second homes. The proposal will need to be passed by the Rules Committee and City Council to be placed on the ballot for voters.

As of August 2025, there were 5,648 Tier 3 and 4 STROs with a total of 14,085 bedrooms and 4,996 second homes with a total of 12,485 bedrooms. Since the ballot proposal has not been finalized for consideration by City Council or the public, our Office is not yet able to provide an estimated amount of revenue the measure could generate.

CONCLUSION

The FY 2027–2031 Five-Year Financial Outlook underscores the City's ongoing structural imbalance and the gap between the cost of maintaining existing service levels and the revenues that are available to support them. While the City has taken meaningful steps over the last year to stabilize its finances – including implementing new revenue measures and making expenditure cuts in the current year's budget – a substantial gap remains between the City's ongoing revenues and the ongoing expenses associated with maintaining current service levels.

Our report highlights several drivers of the projected shortfalls. Revenue growth is expected to remain modest, with some FY 2027 estimates appearing optimistic in light of current performance and economic headwinds. Key sources such as property tax, sales tax, and franchise fees show slowing growth or increased volatility, while cannabis tax receipts and parking revenues carry notable uncertainty. On the expenditure side, personnel costs – including estimated wage increases – represent significant upward pressure; non-personnel costs also show increases, largely due to debt service for planned capital improvements, fleet replacement needs, and operational expenses for new and expanded facilities. Additionally, homelessness programs face growing funding gaps due to declining State support and shifting revenue streams.

While the Outlook projects the City's fiscal condition will improve over the next five years, it nevertheless shows baseline deficits in each of the next five years, which indicates that the City cannot sustain current service levels without corrective action. Near-term revenue opportunities are limited, and one-time solutions the City has relied on in recent years to balance its budget are no longer available. Departments have been directed to propose significant reductions for FY 2027, and the City should reassess the timing of new facilities, prioritize essential services, and evaluate program effectiveness – particularly in areas dependent on unstable or declining revenues. Moving forward, it remains critical to align ongoing expenditures with ongoing revenues to eliminate the structural deficit.

Lisa Byrne
Principal Fiscal and Policy Analyst

Jordan More
Principal Fiscal and Policy Analyst

Amy Li
Senior Fiscal and Policy Analyst

Donny Nguyen
Senior Fiscal and Policy Analyst

Erin Noel
Senior Fiscal and Policy Analyst

Baku Patel
Senior Fiscal and Policy Analyst

Noah Fleishman
Fiscal and Policy Analyst

Sergio Alcalde
Associate Fiscal and Policy Analyst

Jillian Andolina
Deputy Director

Charles Modica
Independent Budget Analyst

Attachment 1: New Facilities and Joint Use Agreement Annual Costs

NEW FACILITIES AND JOINT USE AGREEMENT ANNUAL COSTS

Department	Facility	Council District	FTE	First Year Expense
	Fiscal Year 2027			
Parks and Recreation	East Village Green	3	1.00	$ 383,018
Parks and Recreation	Bruce Brown Memorial Park	6	4.00	749,719
Parks and Recreation	Eastbourne Neighborhood Park	5	1.00	156,746
Parks and Recreation	Federal Boulevard Pocket Park	9	0.50	67,952
Parks and Recreation	Hickman Elementary Joint Use	6	1.00	146,137
Parks and Recreation	Hickman Field	6	1.00	144,681
Parks and Recreation	Mira Mesa Aquatic Center	6	8.00	944,509
Parks and Recreation	Pacific Beach Elementary Joint Use	1	1.00	113,168
Parks and Recreation	Rowan Elementary Joint Use	9	0.50	90,886
Parks and Recreation	Hidden Trails Neighborhood Park	8	3.00	468,514
Parks and Recreation	Beyer Park Phase 1	8	1.00	173,136
Parks and Recreation	Junipers Park	5	1.00	161,661
Parks and Recreation	Walden Neighborhood Park	5	-	37,664
Parks and Recreation	Mira Mesa Community Park	1	1.00	339,785
Parks and Recreation	Perry Elementary Joint Use	4	0.50	86,061
Parks and Recreation	Shoal Creek Neighborhood Park	5	0.50	120,027
Parks and Recreation	Citywide Facility Maintenance (New Facilities)	Citywide	16.00	2,544,250
Parks and Recreation	Payroll Support for New Facilities	Citywide	1.00	107,373
Library	City Heights Annex Expansion	9	-	8,520
Total Fiscal Year 2027			**42.00**	**$ 6,843,807**
	Fiscal Year 2028			
Parks and Recreation	Black Mountain Ranch Park Phase 2	5	3.00	$ 567,133
Parks and Recreation	Jones Elementary Joint Use	7	0.50	133,428
Parks and Recreation	Grove Neighborhood Park	8	2.00	389,916
Parks and Recreation	Beyer Park Phase 2	8	2.00	281,995
Parks and Recreation	North Central Square Park	3	0.50	61,496
Parks and Recreation	Solterra Vista Neighborhood Park	6	1.00	187,863
Parks and Recreation	Citywide Facility Maintenance (New Facilities)	Citywide	2.00	711,142
Library	Ocean Beach Library Expansion	2	-	34,885
Library	Oak Park Library	4	-	107,424
Fire-Rescue	Black Mountain Ranch Fire Station	6	12.00	2,563,185
Total Fiscal Year 2028			**23.00**	**$ 5,038,468**
	Fiscal Year 2029			
Parks and Recreation	Sefton Field	7	2.00	$ 290,087
Parks and Recreation	Toler Elementary Joint Use	2	0.50	81,824
Parks and Recreation	Lafayette Elementary Joint Use	2	0.50	129,778
Parks and Recreation	Emerald Hills Neighborhood Park	4	0.50	122,090
Parks and Recreation	Citywide Facility maintenance (New Facilities)	Citywide	2.00	492,032
Fire-Rescue	Otay Mesa Fire Station	8	27.00	5,922,325
Total Fiscal Year 2029			**32.50**	**$ 7,038,135**
	Fiscal Year 2030			
Parks and Recreation	Dennery Ranch Neighborhood Park	8	3.00	$ 523,447
Parks and Recreation	Foster Elementary Joint Use	7	0.50	86,600
Parks and Recreation	Ross Elementary Joint Use	2	0.50	71,859
Parks and Recreation	Johnson Elementary Joint Use	4	0.50	90,204
Parks and Recreation	Field Elementary Joint Use	2	0.50	86,600
Total Fiscal Year 2030			**5.00**	**$ 858,708**
	Fiscal Year 2031			
Parks and Recreation	Florence Elementary Joint Use	3	0.50	$ 76,366
Parks and Recreation	Benchley-Weinberger Elementary Joint Use	7	0.50	87,813
Parks and Recreation	Perkins Elementary Joint Use	8	0.50	74,366
Total Fiscal Year 2031			**1.50**	**$ 238,545**

Note: Facilities include one-time expenses for items such as vehicles in the first year of operation. One-time expenses are eliminated from subsequent years operating costs.