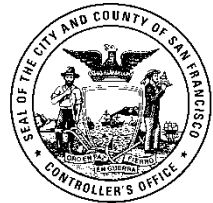


City and County of San Francisco

Controller, Mayor, Board of Supervisors' Budget Analyst

Five Year Financial Plan Update for General Fund Supported Operations FY 2018-19 through FY 2021-22

**Joint Report by the Controller's
Office, Mayor's Office, and
Board of Supervisors' Budget
Analyst**



December 21, 2017



City and County of San Francisco

Five Year Financial Plan Update for General Fund Supported Operations

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Summary

San Francisco Administrative Code Section 3.6(b) requires that by March 1 of each even-numbered year, the Mayor, Board of Supervisors Budget Analyst, and Controller submit an updated estimated summary budget for the remaining four years of the City's Five Year Financial Plan. This report provides updated expenditure and revenue projections for Fiscal Years (FY) 2018-19, FY 2019-20, FY 2020-21 and FY 2021-22, assuming no changes to current policies and staffing levels. The next full update of the City's Five Year Financial Plan will be submitted in December 2018.

Table 1 summarizes the projected changes in General Fund supported revenues and expenditures over the next four years. As shown in Table 1, this report projects shortfalls of \$88.2 million in FY 2018-19, \$173.4 million in FY 2019-21, \$561.2 million in FY 2020-21, and \$709.3 million in FY 2021-22.

Table 1. Summary of General Fund Supported Operations Projected Budgetary Surplus / (Shortfall) (\$ Millions)

| | <u>FY 18-19</u> | <u>FY 19-20</u> | <u>FY 20-21</u> | <u>FY 21-22</u> | <u>% of Uses</u> |
|---|-----------------|-----------------|-----------------|------------------|------------------|
| Total - Sources | 189.9 | 450.7 | 330.3 | 436.8 | |
| Uses | | | | | |
| Baselines & Reserves | (78.2) | (117.0) | (158.1) | (180.3) | 16% |
| Salaries & Benefits | (132.7) | (290.8) | (437.8) | (559.0) | 49% |
| Citywide Operating Budget Costs | (50.6) | (152.5) | (208.8) | (282.0) | 25% |
| Departmental Costs | (16.6) | (63.8) | (86.8) | (124.9) | 11% |
| Subtotal - Uses | (278.1) | (624.1) | (891.4) | (1,146.0) | 100% |
| Projected Cumulative Surplus / (Shortfall) | (88.2) | (173.4) | (561.2) | (709.3) | |

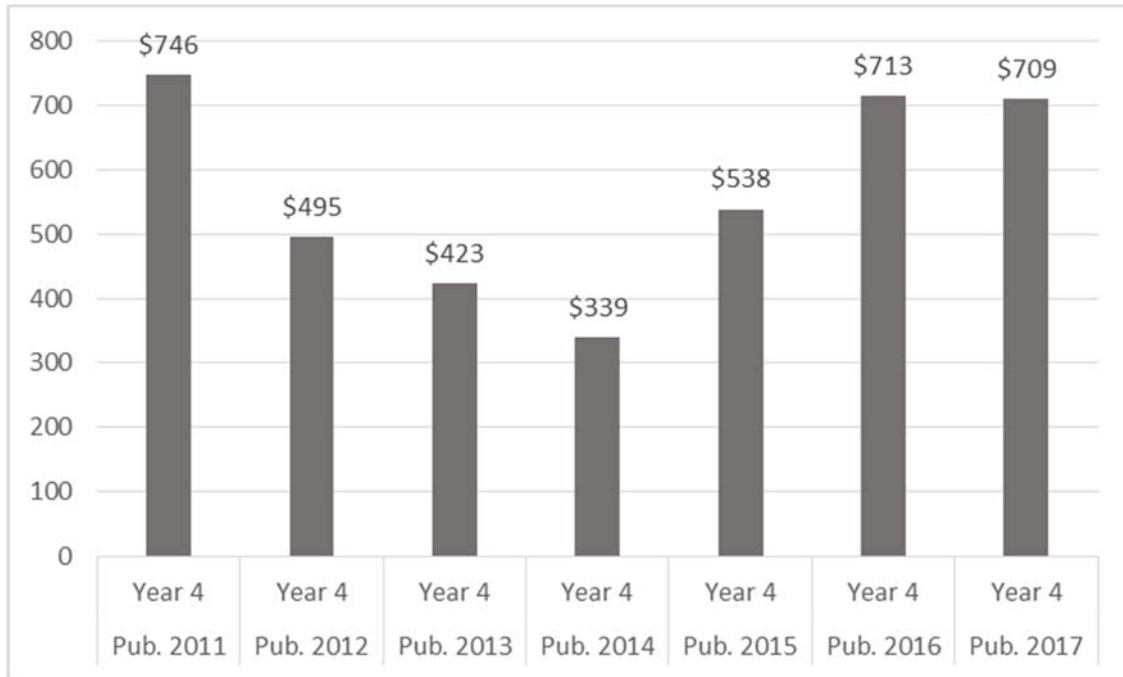
This projection demonstrates that although revenues are growing each year, they are not growing fast enough to keep pace with the projected increase in expenditures. As a result, a gap remains despite continued economic growth. The City currently projects revenue growth of \$436.8 million, or 8.5% over the four year period of this Plan, and expenditure growth of \$1.2 billion, or 22.3%.

In the short-term, the City's two-year deficit for FY 2018-19 and FY 2019-20 is \$262 million, roughly the same as the March 2017 projection of \$287.6 million. The two year deficit is largely the same as the last projection, despite rising costs driven by salary and benefit costs, overall cost inflation, and mandated baseline and set-aside contributions, due to increases in one-time revenue. However, over the long-term the City's structural deficit has increased in recent years.

Increasing Structural Deficits – Areas of Concern

The City made steady progress from 2011 to 2014 to better align long-term expenditure and revenue growth, steadily bringing down the projected structural deficit. However, since the projected deficit of \$339 million in the final year of the Joint Report published in 2014, the City’s long-term deficit has more than doubled, reaching \$709 million in the final year of this Report.

Figure 1. Fourth Year Deficit as Projected in Past Long-term Financial Plans (\$ Millions)

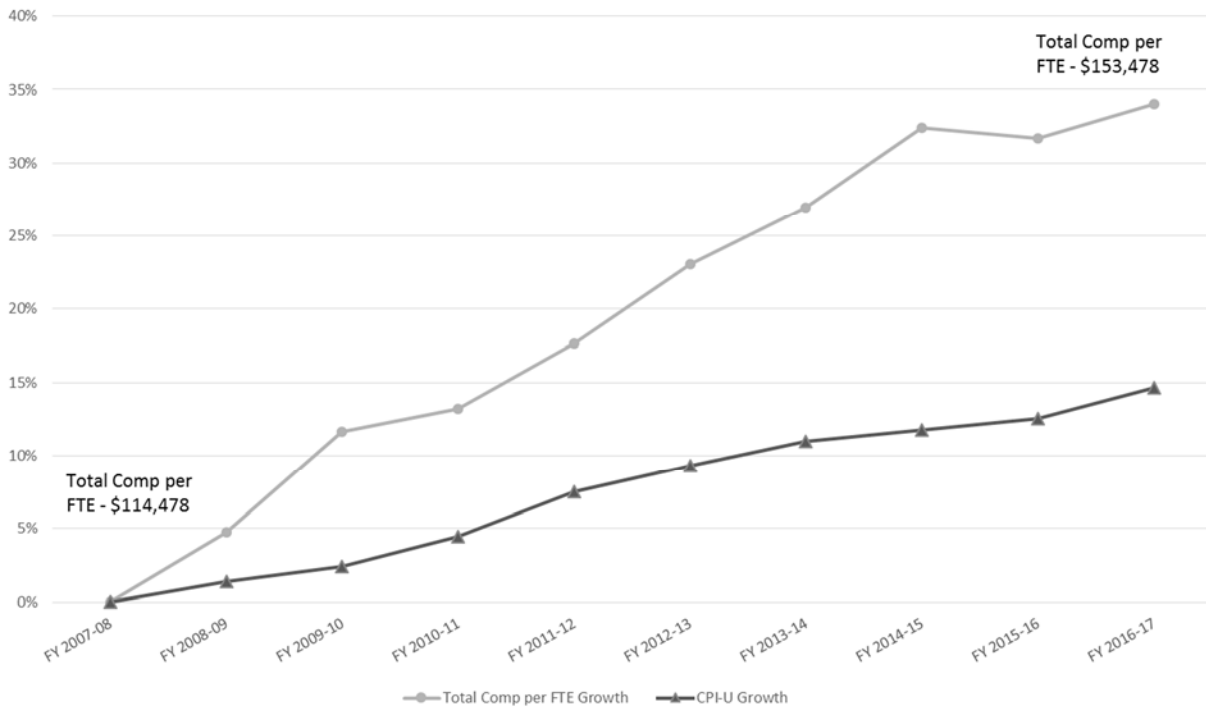


This escalation in the projected structural deficit is largely due to increases related to employee salary and benefit costs, including the projected employer contribution rates for the City’s retirement system and increases to health coverage rates; and voter-approved baselines and set-asides with spending requirements. A more detailed description of these two factors follow, which together make up approximately 65 percent of the projected shortfall in FY 2021-22.

Increased wages and health care coverage costs: Total salary and benefit cost projections make up 49 percent of the growth in the final year of this report. For the purposes of projections this report assumes that wage growth will increase at the rate of inflation. Figure 2, highlights that over the last decade total compensation, which includes employer contributions for pension and health care for employees, has far outpaced inflation.

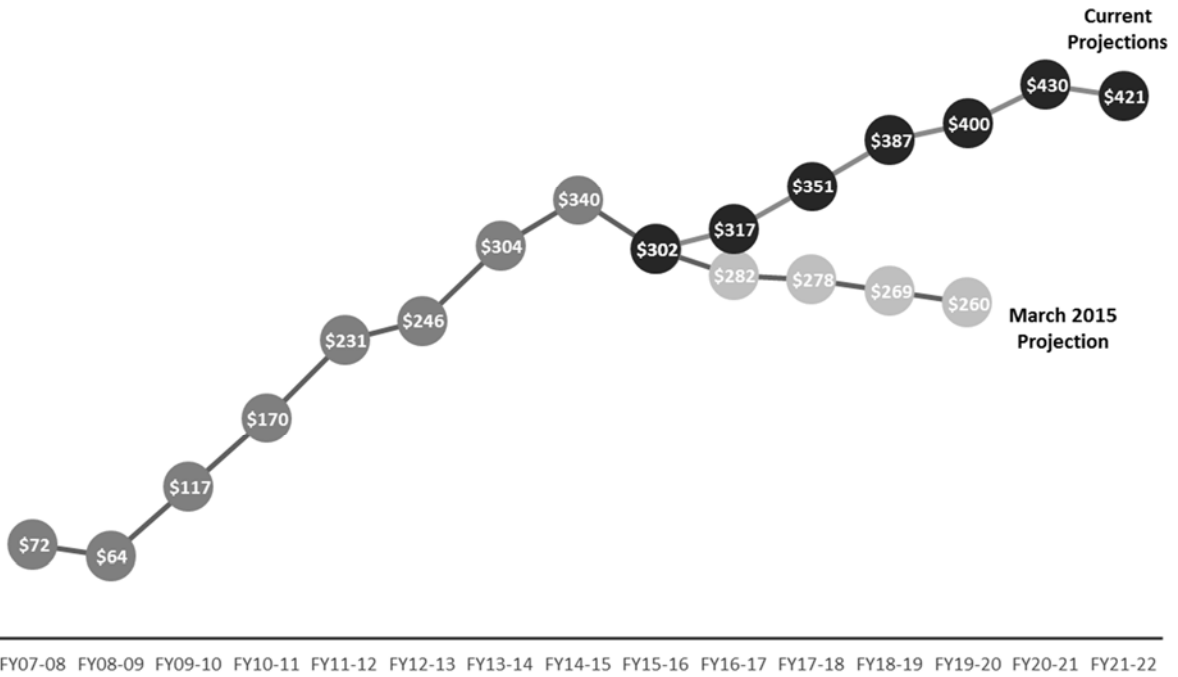
Both employer pension contribution and health rate increases have, in recent years, grown at a rate that exceeds inflation. This report assumes that the employer share of health and dental insurance costs for active employees will increase by 6% in FY 2018-19 and 8% each year in the remaining three years of the plan. It also assumes retiree health costs will increase by 9% in each year of this four year projection. These increases outstrip inflation, and are a significant increase from 2014 projections that anticipated approximately 5% growth in the employer share of health and dental rates.

Figure 2. Total Compensation per FTE FY 2007-08 to FY 2016-17



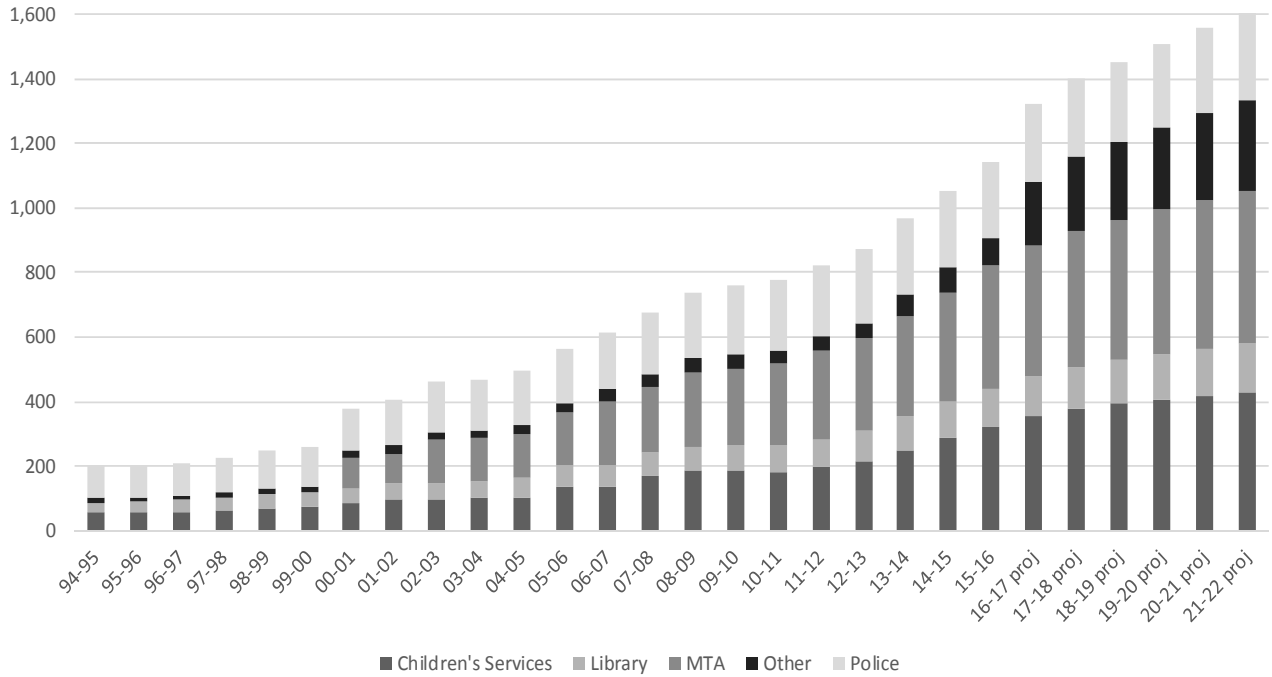
Steep increases in retirement plan employer contribution rates: Retirement plan employer contribution rates have risen significantly in recent years, substantially reversing prior year downward cost projections. As shown in Figure 3, at the time of March 2015 projections the City expected to see a decline in employer contributions to employee pensions. However, this trend was reversed significantly starting in 2016 due to the loss of the supplemental COLA lawsuit, employees living longer, and lower than expected investment returns in 2015 and 2016. This report also reflects that despite 2017 investment returns exceeding projected levels, the City’s contribution rates increase in the near term due to an additional on-going supplemental COLA to certain retirees triggered by the one-time better than expected returns. Over the last decade, the City’s General Fund expenditures related to employer contribution has gone from 2.5% of General Fund spending to over 7% of General Fund spending.

Figure 3. Projected Employer General Fund Pension Contribution Cost (\$ Millions)



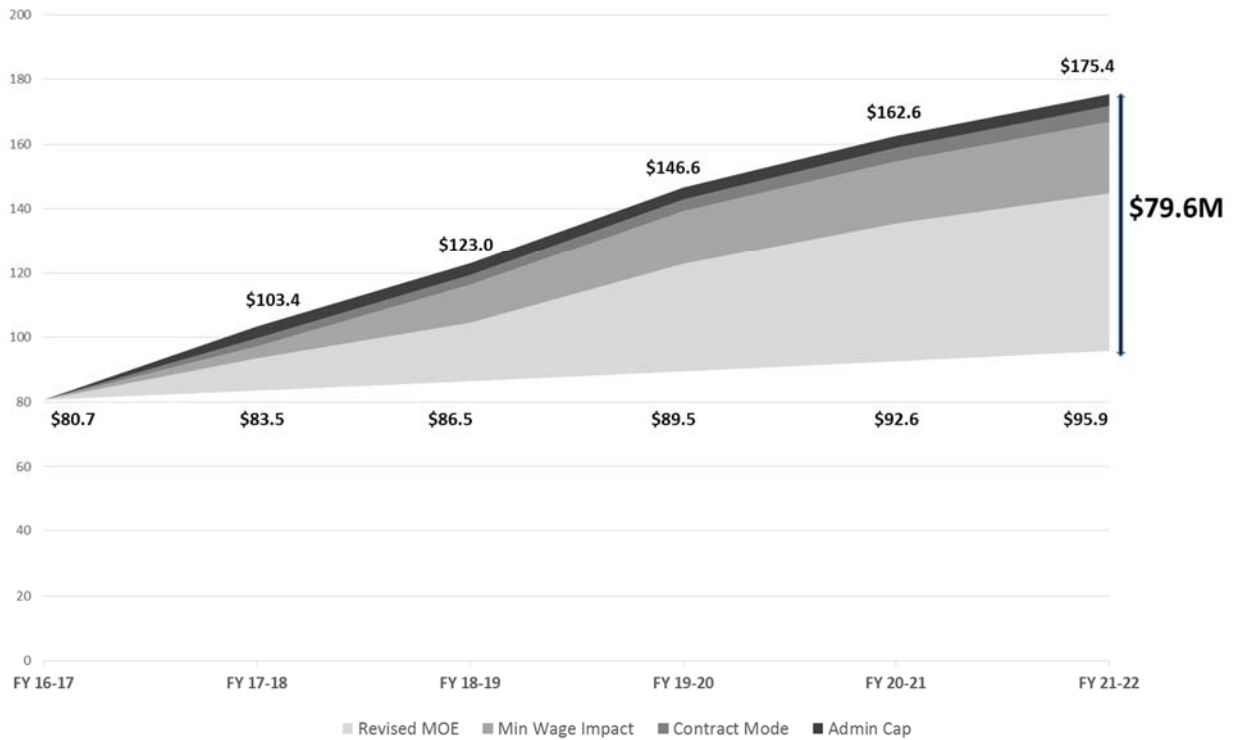
Increasing Cost of Baselines and Set-Asides: The number of voter-mandated baselines and set-asides has grown significantly over the last decade. In FY 1994-95 there were six baselines and now there are 19 spending and service mandates. Commensurately, spending on baselines and set-asides has grown dramatically from approximately \$200 million in FY 1994-95, to a projected \$1.6 billion in FY 2021-22. Baselines limit the financial flexibility of the City to make choices between service areas, especially in recessionary periods. As voter-mandated spending requirements have grown, financial pressures – whether to respond to a new service need or an economic slowdown – fall on a smaller portion of the budget. The portion of the budget mandated by voter-action has more than doubled since FY 1994-95, from 15% to 30% of the General Fund.

Figure 4. Baseline Spending Levels by Category FY 1994-95 to FY 2021-22 (\$ millions)



In-Home Support Services (IHSS) cost shift from the State: IHSS is an entitlement program which provides homecare services to 22,000 elderly and disabled San Franciscans, allowing them to stay in their homes rather than move into more costly nursing facilities or other programs. It is funded by federal, state, and county sources. Due to changes in the state budget, which are discussed in greater detail on p XX of this report, significant costs for this program were shifted from the state to counties. At the time of the Mayor’s last budget submission, the complete legislative language and regulations implementing the change had not yet been released. Based on the best estimates of the limited information available at the time, the FY 2017-18 and FY 2018-19 budget assumed significant cost increases of \$11.1 million in FY 2017-18 and \$16.9million in FY 2018-19, as compared to prior budget projections. As more detail has been released the Human Services Agency revised projections to add an additional cost of \$8.8 million in the FY 2017-18 budget, bringing the total cost growth in that year to \$19.9 million above prior budget projections. As Figure 5 shows, the cost shift continues to grow in FY 2018-19 and beyond, leading to an annual new cost to San Francisco of nearly \$80 million in FY 2021-22 as compared to prior projections.

Figure 5. Cost Growth in San Francisco Share of IHSS Program (\$ millions)

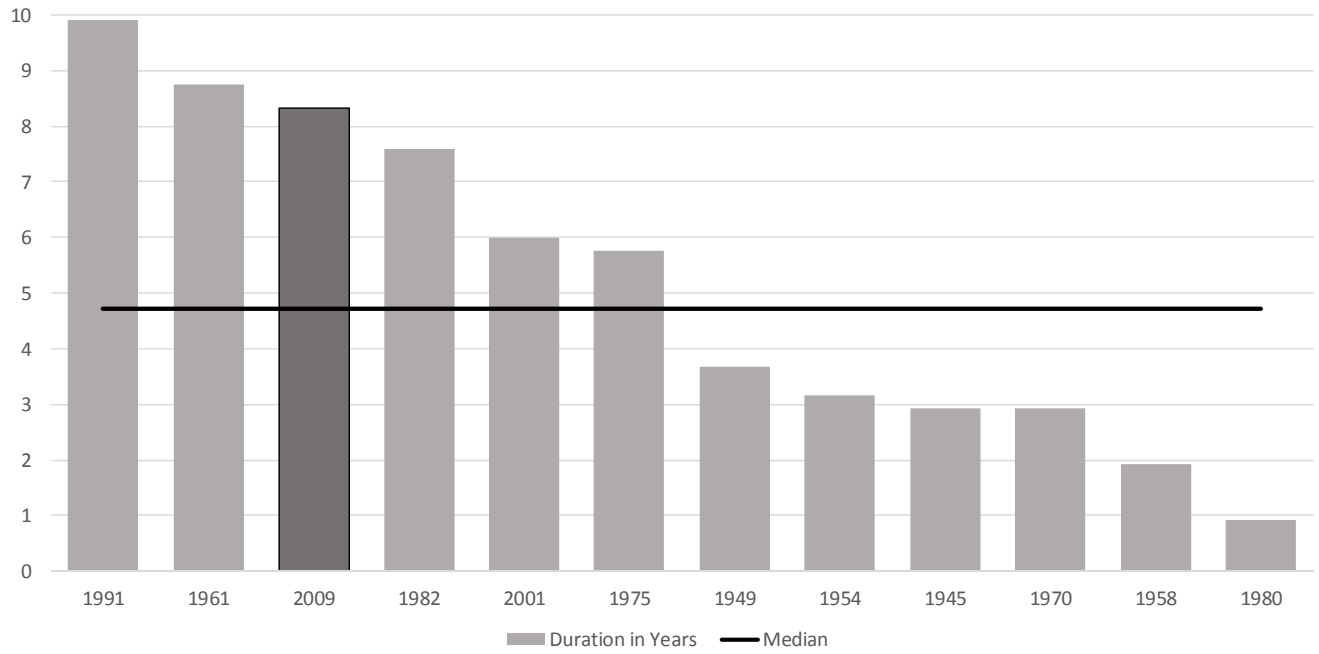


Volatile Revenue Sources - Areas of Growing Uncertainty and Risk

The projected deficit, already dramatically increased by growth of the City’s salary and benefits costs, as well as voter-mandated baselines and set-asides and IHSS increases, would be further exacerbated by a change in the overall economy or changes in policy at the federal level. These items are not assumed in the City’s Joint Report, but are discussed here due to their growing risk to the City’s fiscal picture:

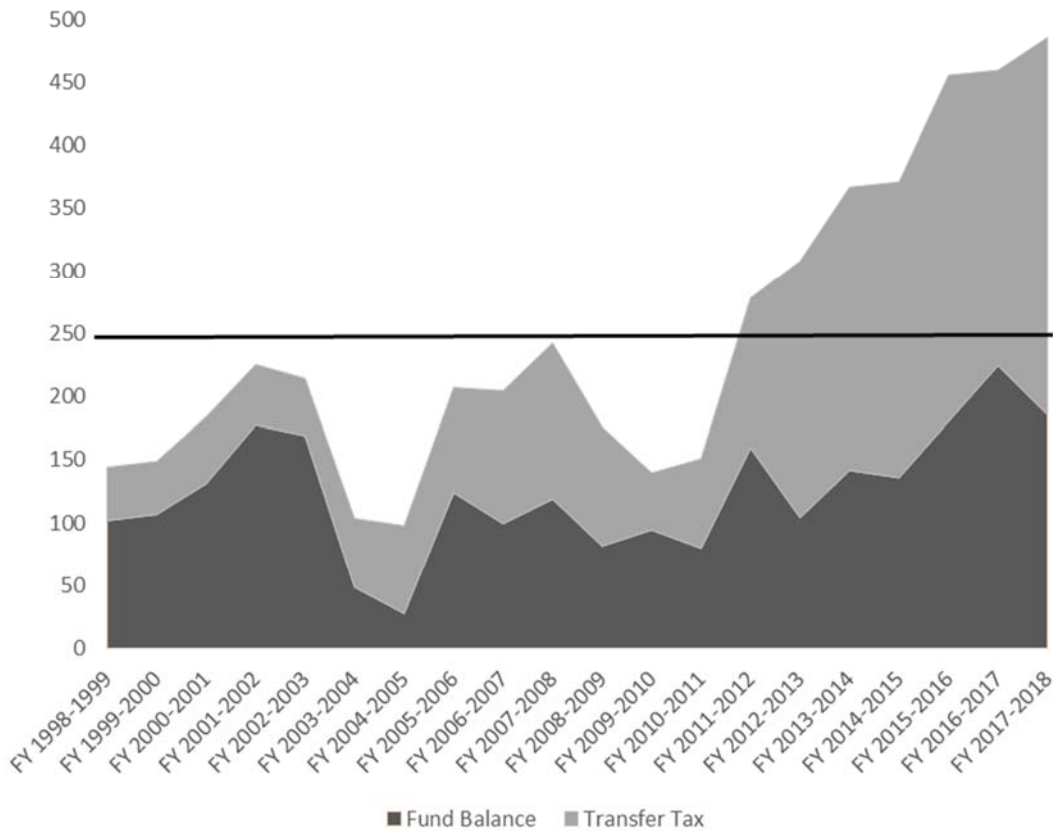
Length of Current Economic Expansion: Historically, periods of economic expansion are followed by economic contraction, or recession. Since the end of the Great Depression economic expansions have a median length of approximately 5 years. The current economic expansion, which began in 2009, has already lasted over eight years. As noted in Figure 6, the U.S. economy is experiencing the third longest economic expansion since 1945. It would be an historic anomaly to not experience a recession within the projection period of this report. While this report assumes that economy continues to grow, albeit at a slowing rate, it does not project a recession in this period. If a recession were to occur it would negatively impact this forecast.

Figure 6. Number of Years of Economic Expansion in the U.S. from Start Year (1945 to Present)



An example of how an economic recession could affect the City’s fiscal picture is shown by reviewing the amount of fund balance and transfer tax assumed in the FY 2017-18 budget as compared to past years as shown in Figure 7.

Figure 7. Budgeted Fund Balance and Transfer Tax (\$ Millions)



Fund balance, generally consisting of unexpectedly strong revenues and unexpended funds from the prior budget year, has played an increasing role in balancing the General Fund budget in recent years. In the FY 2012-13 and 2013-14 budget, \$229 million in fund balance was used. In comparison, the FY 2017-18 and 2018-19 budget used \$476 million of fund balance.

Additionally, transfer tax, the City’s most volatile revenue source, is generated from the transfer of ownership of real property from one person (or entity) to another. It is one of the City’s most economically sensitive and volatile sources of revenue. Real property transfers can decline significantly, greatly reducing revenue within a single fiscal year. In the last downturn, FY 2008-09, transfer tax was budgeted at \$94 million but actuals came in at nearly half of that, \$49 million. This unexpected revenue loss- among other unanticipated revenue losses- contributed to a need for mid-year expenditure reductions.

Additionally, high-value (largely commercial) properties generate a large portion of transfer tax; revenue is determined by a small number of individual transactions. For example, in FY 2016-17 almost 75% of transfer tax revenue came from the sale of properties valued in excess of \$10 million, which was less than 2% of all transfers. There are a finite number of properties of this value and there has been a high volume of these transactions in recent years.

The risk of an economic recession could greatly impact these two revenue sources, which are assumed at \$486 million in the FY 2017-18 budget and have been as low as \$98 million in past downturns.

Risk and Uncertainty from the Federal government: A multitude of potential policy changes at the federal level are cause for great uncertainty at the local level. The most prominent risks known at this time are posed by tax reform, changes to elements of the Affordable Care Act (ACA), and potential changes to the federal budget:

- **Tax reform:** The tax overhaul approved by Congress on December 20th, 2017 was developed in a short time period with little public review. Therefore, its impacts on the San Francisco local economy are not clear at this time. However, the local economy would certainly be impacted by some of the following policies included in the legislation passed by Congress: 1) the reduction of the State and Local Tax exemption (SALT) from an unlimited deduction to a cap of \$10,000 deduction, which would increase residents' total tax liability and could lead to a slowing of the local and state economy by depressing spending; 2) repeal of the individual health insurance mandate under the Affordable Care Act (ACA); and 3) the reduction in the mortgage interest tax deduction.
- **Affordable Care Act and other healthcare changes:** While explicit repeal and replace efforts related to the ACA have been unsuccessful at the federal level to date, the threat to Medi-Cal and the overall program remains. Efforts to convert Medicaid funds to a block grant or a per capita cap remain a risk, threatening vital revenue to the City. Additionally, as noted above, the tax reform legislation approved by Congress repeals the individual mandate, which could result in millions uninsured nationwide, leading to market uncertainty and higher premiums that could impact the City. Lastly, the federal government's failure to renew the Children's Health Insurance Program will result in a significant funding shortfall if action is not taken at the state or federal level.
- **Federal Budget:** Additionally, a Federal "budget shut down" due to Congress failing to pass a budget or a continuing resolution could impact San Francisco services and residents; for instance, issuance of new Social Security and Medicare cards would cease, as would enrollments in the Supplemental Nutrition Assistance Program (SNAP). Child welfare services, school lunch programs, Head Start, Community Service Block Grants, and funding for the San Francisco Housing Authority could also all potentially be affected.

The Mayor's Office, Budget Analyst's Office and the Controller's Office are closely monitoring these risks and will provide an update on these items to the Board of Supervisors Federal Select Committee as hearings are called, as well as when the update to the Joint Report is issued in March 2018.

Key Assumptions

Key assumptions affecting the FY 2018-19 through FY 2021-22 projections:

- **No major changes to service levels and number of employees:** This projection assumes no major changes to policies, service levels, or the number of employees from previously adopted FY 2017-18 and FY 2018-19 budgeted levels unless specified below.
- **Continued economic recovery:** This projection assumes the economic recovery and expansion that began in FY 2009-10 will continue through the forecast period and will be reflected in tax revenue increases. The rapid rates of growth experienced in the early part of the recovery have slowed, and lower rates of growth are expected to persist in the forecast period. Economic growth, and the revenue derived from it, is heavily dependent on changes in employment, business activity, and tourism. Physical and financial constraints are expected to limit this growth. This report does not assume any economic downturns or large changes in macroeconomic conditions; however, the median length of a period of economic expansion since 1945 is under five years. The current expansion is currently in its eighth year.
- **State and federal budget and policy impacts:** The FY 2017-18 budget included \$10 million for an unknown state and federal impacts reserve. A supplemental was introduced by the Mayor's Office on November 28, 2017 to appropriate \$9.6 million of the one-time \$10 million reserve. On-going costs related to IHSS and HIV/AIDS programming are assumed in this forecast. The \$50 million ACA reserve that was also assumed in the FY 2017-18 and FY 2018-19 budget remains unappropriated at this time, and the City will continue to closely monitor any potential changes to the ACA.

Aside from changes covered by the state and federal impacts reserve, this report does not assume other significant changes in funding at the state and federal levels, although many uncertainties exist.

- **Assumes inflationary increases for most employees in line with CPI:** Police officers and firefighter unions have open contracts starting in FY 2018-19 and will enter negotiations for Memoranda of Understanding (MOUs) with the City in the spring of 2018. Therefore beginning in FY 2018-19 the plan projects negotiated salary increases equal to the change in the Consumer Price Index (CPI) using the average projection of the California Department of Finance San Francisco Area CPI and Moody's SF Metropolitan Statistical Area CPI. This corresponds to 3.27% for FY 2018-19, 3.33% for FY 2019-20, 3.11% for FY 2020-21 and 3.04% for FY 2021-22. For the majority of miscellaneous employee unions the report assumes negotiated rates of 3% through FY 2018-19 and increases of CPI, as noted above, thereafter. Importantly, these assumptions do not indicate a willingness or ability to negotiate wage increases at these levels but rather are used for projection purposes. Final negotiated increases will increase or decrease projected shortfalls.
- **Retirement plan employer contribution rates continue to increase:** This report assumes updated 2017 year-end return on assets which were 13.5%, 6.0% above the actuarially assumed rate of return of 7.5% per year. One-time returns that exceed the 7.5% actuarially assumed rate trigger an on-going supplemental cost-of-living adjustment (COLA) payment to certain retirees. Employer and employee contribution rates assumed in this report are shown on page 33 of this report.

- **Health and dental insurance cost increases:** This projection assumes that the employer share of health and dental insurance costs for active employees will increase by 6% in FY 2018-19 and 8% each year in the remaining three years of the plan. The Health Service System anticipates negotiating rates for calendar year 2019 in late spring 2018, to be adopted by July 2018. For retiree health benefits, this report assumes that the City will continue its pay-as-you-go practice of funding the amounts currently due for retirees. Retiree health costs are assumed to grow 9% per year in each year of the plan.
- **Inflationary increase on non-personnel operating costs:** This projection assumes that the cost of materials and supplies, professional services, contracts with community-based organizations, and other non-personnel operating costs will increase by the CPI rate, as projected by the California Department of Finance and Moody's, 3.33% for FY 2019-20, 3.11% for FY 2020-21 and 3.04% for FY 2021-22. The projection reflects the adopted FY 2018-19 budget, which included a 2.5% cost-of-doing business increase for General Fund nonprofit contracts.
- **Ten-Year Capital Plan, Five-Year ICT Plan, and inflationary increases on equipment:** This projection assumes the adopted FY 2018-19 funding level for capital, equipment, and information technology. For capital, this means the Capital Plan level of funding in FY 2018-19 since the capital budget was fully funded for the first time ever in the FY 2017-18 and FY 2018-19 budget. In the remaining three out years, the report assumes funding will increase by 7% annually, as is described in the City's FY 2018-27 Ten-Year Capital Plan, which was released in March 2017.

The Information Technology investment projection assumes partial funding of annual projects in the City's Information and Communications Technology (ICT) Plan in FY 2018-19 in accordance with the most recent budget, and full funding in accordance with the ICT Plan in FY 2019-20 through FY 2021-22. This report also assumes full funding for major city IT projects in accordance with the ICT Plan through FY 2021-22.

For equipment, the plan assumes the budgeted level of funding in FY 2018-19. In the subsequent three fiscal years, the report assumes that the equipment budget will increase by CPI each year.

- **Hall of Justice Exit Plan:** This report assumes that the City will be undertaking a number of initiatives in order to empty and close the seismically deficient and functionally obsolete Hall of Justice. The fiscal impact that will result from these initiatives is assumed in this report and is detailed in the citywide costs section.
- **Deposits and withdrawals from reserves:** This projection makes several key assumptions regarding deposits to and withdrawals from major General Fund reserves. First, given the base case revenue projections, no deposits to or withdrawals from the Rainy Day Reserve are assumed. Consistent with the financial policies adopted by the Board of Supervisors in December 2014 and codified in Administrative Code Section 10.60(b), the General Reserve value will increase from 2.25% of General Fund revenues in FY 2017-18 to 3% in FY 2020-21. Lastly, various reserves allocated for particular one-time uses are assumed drawn down for those uses, as detailed later in the base case.

Key Factors That Could Affect These Forecasts

As with all projections, uncertainties exist regarding key factors that could affect the City's financial condition. These include:

- **Economy:** Because of the difficulty of projecting the timing of a recession, this report assumes slower rates of growth, rather than declines, in revenue in the final three years of the report. However, it is important for the City to closely monitor economic conditions over the coming years as noted above.
- **State and federal budget efforts and policy changes:** At the time of report issuance, state and federal budget deliberations have not yet begun. Thus, uncertainty remains around the local impacts of state and federal budget-balancing efforts, as noted earlier in this report.
- **Collective bargaining agreement negotiations:** Other than approved wage increases in collective bargaining agreements and inflation on open contracts in FY 2018-19 through FY 2021-22, this report does not assume any contract changes due to labor negotiations. Wage or benefit changes above or below these assumptions would increase or decrease the City's projected deficit.
- **Pending or proposed legislation – potential fee or departmental revenue increases:** Fee increases may be proposed to the Board of Supervisors before the end of the year or as part of the FY 2018-19 and FY 2019-20 budget. No increases above those budgeted in the adopted FY 2017-18 and FY 2018-19 budget are assumed in this projection.
- **Planning for growth:** The City is currently experiencing growth in both employment and population. As the City's population increases, there may be a need for additional services for the public such as more parks, transportation, first responders, health care providers, and street infrastructure improvements to accommodate more users of the public right-of-way. This report does not assume increased costs to specifically address future growth; however, this represents a risk and could increase projected deficits in the future.
- **Deficits will differ if new budget commitments are made:** If voters approve additional increases to existing baselines, set-asides, or other mandatory spending increases without commensurate revenue increases from new funding sources, this will grow the projected deficits shown in this report. A recent California Supreme Court decision, *California Cannabis Coalition Vs. City of Upland*, may increase the likelihood of new mandatory spending increases. According to an opinion by the City Attorney, one result of the *California Cannabis Coalition vs. City of Upland* decision is to lower the threshold needed to pass voter-initiated dedicated taxes from a 2/3 majority to a simple majority. This lower threshold also applies to voter-initiated ballot measures that would dedicate existing general taxes to specific purposes. The new 50% majority makes these measures much more likely to pass and thus increases the risk of a new spending commitment growing the deficit.

The appendices of this report show much greater detail on projected expenditure and revenue over the next four years.

Schedule of Upcoming Reports Containing Budget Projections

- **Early February - Controller’s Six-Month Budget Status Report:** This report will provide updated revenue, expenditure, and ending fund balance projections for FY 2017-18.
- **Mid-March – Update to the Joint Report:** This report will update the revenue and expenditure forecasts for FY 2018-19 through FY 2021-22.
- **Mid-June - Controller’s Discussion of the Mayor’s Fiscal Year 2018-19 and 2019-20 Proposed Budget (“Revenue Letter”):** This report will provide the Controller’s opinion regarding the reasonableness of the revenue estimates in the Mayor’s Proposed Budget.

Appendix: Projected Changes to General Fund Supported Revenues and Expenditures

| | |
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Appendix: Projected Changes to General Fund Supported Revenues and Expenditures

Table A-1. Key Changes to General Fund Supported Sources and Uses (Incremental)

| SOURCES Increase / (Decrease) | 2018-19 | 2019-20 | 2020-21 | 2021-22 |
|---|----------------|----------------|----------------|----------------|
| General Fund Taxes, Revenues and Transfers net of items below | 219.7 | 114.5 | 103.2 | 91.5 |
| Change in One-Time Sources | (62.6) | 119.2 | (238.5) | - |
| Children's Fund Property Tax Setaside Revenue | 12.7 | 3.5 | 3.6 | 3.5 |
| Department of Public Health Revenues | (5.0) | 14.9 | 6.7 | 7.0 |
| Other General Fund Support | 25.2 | 8.7 | 4.4 | 4.5 |
| TOTAL CHANGES TO SOURCES | 189.9 | 260.9 | (120.5) | 106.5 |
| USES Decrease / (Increase) | | | | |
| Baselines & Reserves | | | | |
| Municipal Transportation Agency (MTA) Baselines | (29.9) | (14.5) | (13.0) | (12.0) |
| MTA New Central Subway | - | (10.7) | (3.6) | (0.4) |
| Children's Fund and Public Education Enrichment Fund | (20.6) | (12.8) | (11.6) | (10.5) |
| Housing Trust Fund | (2.8) | (2.8) | (2.8) | (2.8) |
| Dignity Fund | (3.0) | (3.0) | (3.0) | (3.0) |
| Recreation and Parks Baseline | (3.0) | (3.0) | (3.0) | (3.0) |
| All Other Baselines | (7.0) | (4.0) | (3.5) | (3.1) |
| Deposits to General Reserve | 0.8 | 2.2 | (0.3) | 13.1 |
| Other Contributions to Reserves | (12.8) | 9.8 | (0.5) | (0.5) |
| Subtotal Baselines & Reserves | (78.2) | (38.8) | (41.1) | (22.1) |
| Salaries & Benefits | | | | |
| Annualization of Partial Year Positions | (3.9) | - | - | - |
| Previously Negotiated Closed Labor Agreements | (57.1) | - | - | - |
| Projected Costs of Open Labor Agreements | (17.5) | (100.8) | (98.1) | (98.3) |
| Health & Dental Benefits - Current & Retired Employees | (28.4) | (33.2) | (36.1) | (39.0) |
| Retirement Benefits - Employer Contribution Rates | (25.9) | (4.2) | (22.0) | 17.2 |
| Other Salaries and Benefits Savings / (Costs) | - | (20.0) | 9.1 | (1.0) |
| Subtotal Salaries & Benefits | (132.7) | (158.1) | (147.0) | (121.2) |
| Citywide Operating Budget Costs | | | | |
| Minimum Wage | (10.0) | (3.2) | (0.6) | (0.6) |
| Capital, Equipment, & Technology | (3.2) | (44.8) | (3.8) | (14.5) |
| Inflation on non-personnel costs and grants to non-profits | (12.8) | (36.3) | (35.0) | (35.3) |
| Debt Service & Real Estate | (12.6) | (16.2) | (31.6) | (14.8) |
| Sewer, Water, and Power Rates | (1.9) | (1.9) | (1.8) | (1.9) |
| Hall of Justice Exit | (8.0) | 3.0 | 19.0 | (3.6) |
| Other Citywide Costs | (2.0) | (2.4) | (2.4) | (2.4) |
| Subtotal Citywide Operating Budget Costs | (50.6) | (101.9) | (56.3) | (73.2) |
| Departmental Costs | | | | |
| City Administrator's Office - Convention Facilities Subsidy | 1.0 | 9.6 | (0.5) | (0.2) |
| Elections - Number of Scheduled Elections | 0.8 | (5.9) | 5.4 | (0.2) |
| Ethics Commission - Public Financing of Elections | (0.5) | (1.1) | (0.0) | (0.0) |
| Free City College | (2.2) | (3.1) | - | - |
| Golden State Warriors Event Center | (0.1) | (7.3) | (0.2) | (0.2) |
| Mayor's Office of Housing - HOPE SF and Local Operating Subsidy | (5.2) | (3.3) | (8.6) | (8.1) |
| Human Services Agency - Aid | 1.1 | (1.4) | (0.1) | 0.0 |
| Human Services Agency - IHSS | (28.4) | (23.6) | (15.9) | (12.9) |
| Public Health - Operating and one-time costs for capital projects | 20.4 | (10.2) | 0.0 | (16.3) |
| All Other Departmental Savings / (Costs) | (3.5) | (1.0) | (3.1) | (0.2) |
| Subtotal Departmental Costs | (16.6) | (47.2) | (22.9) | (38.1) |
| TOTAL CHANGES TO USES | (278.1) | (346.1) | (267.3) | (254.6) |
| Projected Surplus (Shortfall) vs. Prior Year | (88.2) | (85.2) | (387.8) | (148.1) |
| Cumulative Projected Surplus (Shortfall) | (88.2) | (173.4) | (561.2) | (709.3) |

Table A-2. Key Changes to General Fund Supported Sources and Uses (Cumulative)

| SOURCES Increase / (Decrease) | 2018-19 | 2019-20 | 2020-21 | 2021-22 |
|---|----------------|----------------|----------------|------------------|
| General Fund Taxes, Revenues and Transfers net of items below | 219.7 | 334.2 | 437.4 | 528.9 |
| Change in One-Time Sources | (62.6) | 56.6 | (181.8) | (181.8) |
| Children's Fund Property Tax Setaside Revenue | 12.7 | 16.2 | 19.8 | 23.3 |
| Department of Public Health Revenues | (5.0) | 9.9 | 16.6 | 23.6 |
| Other General Fund Support | 25.2 | 33.8 | 38.2 | 42.8 |
| TOTAL CHANGES TO SOURCES | 189.9 | 450.7 | 330.3 | 436.8 |
| USES Decrease / (Increase) | | | | |
| Baselines & Reserves | | | | |
| Municipal Transportation Agency (MTA) Baselines | (29.9) | (44.4) | (57.4) | (69.3) |
| MTA New Central Subway | - | (10.7) | (14.3) | (14.7) |
| Children's Fund and Public Education Enrichment Fund | (20.6) | (33.3) | (44.9) | (55.4) |
| Housing Trust Fund | (2.8) | (5.6) | (8.4) | (11.2) |
| Dignity Fund | (3.0) | (6.0) | (9.0) | (12.0) |
| Recreation and Parks Baseline | (3.0) | (6.0) | (9.0) | (12.0) |
| All Other Baselines | (7.0) | (11.0) | (14.5) | (17.6) |
| Deposits to General Reserve | 0.8 | 3.0 | 2.8 | 15.9 |
| Other Contributions to Reserves | (12.8) | (3.0) | (3.4) | (3.9) |
| Subtotal Baselines & Reserves | (78.2) | (117.0) | (158.1) | (180.3) |
| Salaries & Benefits | | | | |
| Annualization of Partial Year Positions | (3.9) | (3.9) | (3.9) | (3.9) |
| Previously Negotiated Closed Labor Agreements | (57.1) | (57.1) | (57.1) | (57.1) |
| Projected Costs of Open Labor Agreements | (17.5) | (118.2) | (216.3) | (314.6) |
| Health & Dental Benefits - Current & Retired Employees | (28.4) | (61.6) | (97.6) | (136.6) |
| Retirement Benefits - Employer Contribution Rates | (25.9) | (30.1) | (52.0) | (34.9) |
| Other Salaries and Benefits Savings / (Costs) | - | (20.0) | (10.8) | (11.9) |
| Subtotal Salaries & Benefits | (132.7) | (290.8) | (437.8) | (559.0) |
| Citywide Operating Budget Costs | | | | |
| Minimum Wage | (10.0) | (13.2) | (13.8) | (14.4) |
| Capital, Equipment, & Technology | (3.2) | (48.0) | (51.8) | (66.3) |
| Inflation on non-personnel costs and grants to non-profits | (12.8) | (49.1) | (84.1) | (119.5) |
| Debt Service & Real Estate | (12.6) | (28.8) | (60.5) | (75.3) |
| Sewer, Water, and Power Rates | (1.9) | (3.9) | (5.7) | (7.5) |
| Hall of Justice Exit | (8.0) | (5.0) | 14.0 | 10.4 |
| Other Citywide Costs | (2.0) | (4.5) | (6.9) | (9.3) |
| Subtotal Citywide Operating Budget Costs | (50.6) | (152.5) | (208.8) | (282.0) |
| Departmental Costs | | | | |
| City Administrator's Office - Convention Facilities Subsidy | 1.0 | 10.7 | 10.2 | 10.0 |
| Elections - Number of Scheduled Elections | 0.8 | (5.1) | 0.3 | 0.1 |
| Ethics Commission - Public Financing of Elections | (0.5) | (1.6) | (1.6) | (1.6) |
| Free City College | (2.2) | (5.4) | (5.4) | (5.4) |
| Golden State Warriors Event Center | (0.1) | (7.3) | (7.5) | (7.7) |
| Mayor's Office of Housing - HOPE SF and Local Operating Subsidy | (5.2) | (8.5) | (17.1) | (25.2) |
| Human Services Agency - Aid | 1.1 | (0.3) | (0.4) | (0.4) |
| Human Services Agency - IHSS | (28.4) | (52.0) | (67.9) | (80.8) |
| Public Health - Operating and one-time costs for capital projects | 20.4 | 10.2 | 10.2 | (6.1) |
| All Other Departmental Savings / (Costs) | (3.5) | (4.5) | (7.5) | (7.7) |
| Subtotal Departmental Costs | (16.6) | (63.8) | (86.8) | (124.9) |
| TOTAL CHANGES TO USES | (278.1) | (624.1) | (891.4) | (1,146.0) |
| Cumulative Projected Surplus (Shortfall) | (88.2) | (173.4) | (561.2) | (709.3) |

Notes to Tables A-1 and A-2

The preceding two tables display the key changes to General Fund sources and uses. Table A-1 provides an incremental view of changes—change from prior year; Table A-2 provides a cumulative view of changes—changes combined as compared to FY 2017-18.

SOURCES – Revenues and Transfers In

General Context Underlying Revenue Estimates

As referenced earlier in this document, San Francisco is in the 8th year of a national economic expansion. This plan assumes continued revenue growth—stronger in the next two year period, with slowing growth in the outer years. The near-term growth assumes robust business and property tax returns, partially offset assumed continued weakness in hotel, parking, and sales tax. Slowing growth is consistent with San Francisco’s housing and infrastructure constraints and reflective of the current length of economic expansion. While there are many risks at the federal level and the potential for an economic downturn, this report does not assume an economic recession.

National Economy

Nationally, economic indicators reflect continued growth with no signs of a recession. Gross Domestic Product (GDP) continues to grow, unemployment is low, and inflation is near the Federal Reserve’s target rate.

Since the end of the Great Depression, there have been 13 recessions, or approximately one every six years on average. Since the official end of the recession in June 2009, the national economy has expanded for more than eight consecutive years. Because of the difficulty of projecting recessions, this report does not assume one. However, if one did not occur during this time period this would mean the current economic expansion lasts for 13 years, the longest period of expansion on record.

Local Economy

San Francisco’s labor market continues to be strong, with seasonally-adjusted unemployment hovering around 3% for the past two years. Since 2010, San Francisco has added on average 26,000 jobs per year, with nearly every sector of the City’s economy contributing to this growth. However, technology has an out-sized role, contributing more than 30% of job growth in 2016. Additionally, employment in the technology industry has increased as a percentage of private employment from less than 2% in 1990 to roughly 13% in 2016; as a share of payroll, it has increased from less than 2% in 1990 to almost 20% in 2016. In the past year, there has been a notable slowdown in technology and private employment job growth rates, as the local economy nears full employment. Technology startup activity has also slowed, with a decline in the number of new firms forming since 2013 and a decline in number of venture capital deals since 2015. The slowdown in technology creates a particular risk for San Francisco, given its importance in the local economy. Due to the favorable macroeconomic conditions assumed in this report, we do not anticipate any technology-driven downturn, particularly in the early years of the forecast period.

In the near term, strong housing prices, tourism, and wage growth will support growth in tax revenues. As mentioned earlier, projected rates of revenue growth are higher in the first year of the plan period to reflect near-term strength in the national and local economies. In the last three years of the plan, growth is projected to slow, to reflect a slowing local technology industry, housing and infrastructure constraints on growth, underperformance in hotel, parking and sales taxes in recent years, and an increased risk of recession.

Property Tax

General Fund property tax revenues are expected to grow from a budget of \$1,557 million in FY 2017-18 to an estimated \$1,851 million in FY 2021-22. General Fund property tax revenue assumptions include:

- **Roll growth:** The locally assessed secured roll grows based upon an annual statewide inflation factor capped at 2% and new base year property value assessments triggered by changes in ownership or new construction. The change in the California CPI (measured October-to-October of the previous two years) is assumed at the maximum 2% for this report's four years through FY 2021-22. For changes in ownership and new construction, it is assumed that an additional 2% of secured roll growth occurs at minimum each fiscal year. An additional 3% of secured roll growth above the 2% is anticipated for FY 2018-19 for a total of 7% including California CPI.

The state assessed board roll and the unsecured roll comprise about 7.5% of overall taxable property values in San Francisco and tend to change in less predictable manners. In this Plan, the board roll value is assumed to remain at the FY 2017-18 value of \$3.5 billion, and the unsecured roll is assumed to grow at an annual rate of 1% from the FY 2017-18 value of \$14.0 billion through FY 2021-22.

- **Supplemental and escape assessments:** Supplemental assessments capture changes in value for the portion of the tax year remaining following a trigger date that results in a change in the base year assessed value of a property. The escape assessment captures a full year's increase in assessed value up to four years after the trigger date occurred. This Plan assumes supplemental and escape assessment revenue of \$104.9 million in FY 2018-19, declining about 10% per year through FY 2021-22 as the volume and size of such assessments is expected to decrease. Supplemental and escape assessments have traditionally been a significant source of variance in property tax revenues.
- **Change in San Francisco Children's Fund property tax allocation factor:** San Francisco voters approved Proposition C on November 4, 2014, which renewed and increased the property tax set aside for the Children's Fund. As a result, the Children's Fund allocation factor increased from \$0.0300 in FY 2014-15 to \$0.0325 in FY 2015-16. The Children's Fund allocation factor will subsequently increase to \$0.0350 in FY 2016-17, to \$0.0375 in FY 2017-18, and to \$0.0400 in FY 2018-19 on each \$100.00 valuation of taxable property. The allocation of property taxes to the General Fund decreases each year by the same incremental change to the Children's Fund factor.

Business Taxes

Business tax is expected to grow from a projected \$800.4 million in FY 2017-18 to \$940.5 million by FY 2021-22. Business taxes include payroll, business registration fees, and gross receipts taxes. Revenues from business taxes and registration fees follow economic conditions in the City and grew strongly from FY 2010-11 to FY 2016-17 reflecting underlying gains in employment and wages during the period. Business tax revenues are sensitive to changes in the economic condition of the City. The business tax projections reflect expectations of continued strong economic growth, particularly in wages, for the first year of the forecast. The last three years of the forecast project a slowdown partially due to constrained regional housing and transportation capacity and to reflect the risk of recession or a technology industry slowdown.

In November 2012, Proposition E was passed to replace a 1.5% payroll tax on businesses with a tax on a business's gross receipts at rates that vary by size and type of business. During this five-year period, the new tax structure is being phased-in as the payroll tax is phased out. The phase-in is designed to adjust

tax rates in order to generate the same amount of revenue as the original 1.5% payroll tax. The gross receipts tax applies only to businesses with \$1 million or more in gross receipts. Revenue collected from gross receipts tax varies based on implementation factors and any policy changes. The City is beginning to implement a new and far more complex tax structure and revenues may be sensitive to the administrative burdens of the new system. The underlying economic growth rate is projected to be 5.0% in FY 2018-19, 2.5% in FY2019-20, 2.0% in FY 2020-21, and 1.0% in FY 2021-22.

Sales Tax

Sales tax is expected to grow from a projected \$191.7 million in FY 2017-18 to \$202.2 million by FY 2021-22. As shown in Figure A-1, growth rates have declined, from highs above 8% per quarter in FY 2013-14 to three negative quarters in FY 2016-17. The projections anticipate lower growth rates between 1-3% to persist due to a combination of factors including: the expectation that job and housing markets are near full capacity; possible negative impacts on the county pool revenues caused by increased online sales; weakness in purchases of general consumer goods at brick and mortar stores; and a decline in luxury goods sales, which has historically been one of the major sources of local sales tax revenues.

**Figure A-1. Change in Local Sales Tax Revenues from Same Quarter Prior Year
FY 2012-13 through FY 2021-22**



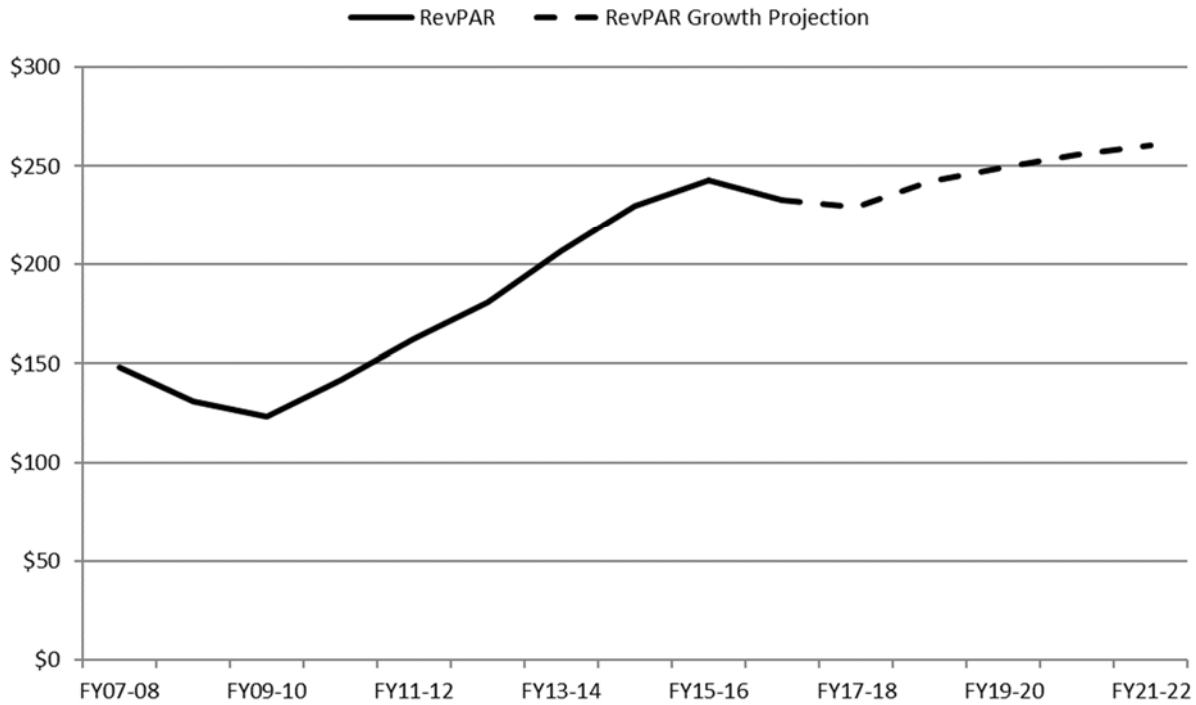
Note: Data is adjusted for corrections and misallocations by the California Department of Tax and Fee Administration (former Board of Equalization).

Hotel Tax

Hotel tax is expected to grow from a projected \$364.8 million in FY 2017-18 to \$417.3 million by FY 2021-22. Hotel tax is projected to decline in FY 2017-18 and then return to prior levels in FY 2018-19, followed by slower growth in the out years. Hotel tax revenue is influenced by three factors – average daily room rates (ADR), occupancy rate, and supply of available rooms – represented by revenue per available room (RevPAR). RevPAR is projected to grow slowly compared to the past six years. In FY 2016-17, hotel tax revenue fell as a result of the Moscone Convention Center closure, which hosts some of San Francisco’s largest conventions. The Moscone closure also affects the first three months of FY 2017-18. While the Moscone closure is a major factor in the recent decline of hotel revenues, modest declines in RevPAR began before the closure, and this trend is expected to continue in FY 2017-18. In FY

2018-19, revenue is expected to return to previous higher rates with Moscone open for the full year. RevPAR between FY 2019-20 and FY 2021-22 is expected to grow, but at a slowing pace, and hotel revenue is expected to follow this trend. Figure A-2 provides a recent history of RevPAR levels and projections for the five-year period.

**Figure A-2. San Francisco Revenue Per Available Room (RevPAR)
FY 2007-08 to FY 2021-22 Actual and Projected**



Source: CBRE PKF Hospitality Research, projections are Controller estimates

Real Property Transfer Tax

Real property transfer tax (RPTT) revenue is projected to decrease from a projected level of \$260.0 million in FY 2017-18 to \$245.0 million for the following five years. RPTT is one of the most volatile of all revenue sources and is highly sensitive to economic cycles and interest rates. A primary reason for the volatility is that transfer taxes are assessed at different rates according to the amount of the transaction, with higher value properties paying a higher tax rate.

In November 2016, voters approved Proposition W, which increased the real property transfer tax rate on properties over \$5.0 million, affecting the last half of FY 2016-17. This contributed to record high transfer tax collections of \$410.6 million in FY 2016-17. With Proposition W, the highest tier is 3% of transaction value for transactions of more than \$25.0 million. While the number of transactions in this tax tier is very small (<1% of transactions in the last six months of FY 2016-17), the proportion of total transfer tax revenue they generate is quite large (62% in the last six months of FY 2016-17). These high-value transactions are the primary reason for revenue volatility.

The projection assumes that transactions of large properties will taper off and that revenue will fall to average annual collections over the last ten years. Recent growth in RPTT revenue has largely been a function of the lack of more attractive alternative investment opportunities, as demonstrated by historically low U.S. Treasury Bond rates. However, in the second quarter of 2017, capitalization rates

have held steady, suggesting that the market may no longer be expanding. Capitalization rates are the returns on a capital investment. In addition, in a recent Korpacz survey, investors expect capitalization rates to increase or hold steady. The recent increase in office supply has pushed vacancy rates higher and has caused slight declines in overall asking rental rates. The combination of steady or declining rental rates and increasing capitalization rates signal that investors are expecting commercial property valuations to fall. With a commercial real estate market that is expected to slow down, real property transfer tax revenue is projected to decline in FY 2017-18 and then fall to the ten-year policy adjusted average beginning in FY 2018-19.

**Table A-3a. Summary of General Fund Supported Operating Revenues and Transfers in
FY 2016-22 (\$ millions)**

| | FY2016-17 | FY 2017-18 | FY 2018-19 | FY 2019-20 | FY 2020-21 | FY 2021-22 |
|---|------------------------|--------------------|----------------|----------------|----------------|----------------|
| | Year-End Pre- Audit | Original Budget | Projection | Projection | Projection | Projection |
| Property Taxes | \$ 1,481.1 | \$ 1,557.0 | \$ 1,668.0 | \$ 1,730.0 | \$ 1,791.0 | \$ 1,851.0 |
| Business Taxes | 700.5 | 750.8 | 884.0 | 908.0 | 928.9 | 940.5 |
| Sales Tax | 189.5 | 199.9 | 196.3 | 198.2 | 200.2 | 202.2 |
| Hotel Room Tax | 370.3 | 372.3 | 385.7 | 398.9 | 409.0 | 417.3 |
| Utility Users Tax | 101.2 | 99.7 | 101.7 | 102.7 | 103.8 | 105.0 |
| Parking Tax | 84.3 | 82.2 | 84.3 | 84.3 | 84.3 | 84.3 |
| Real Property Transfer Tax | 410.6 | 300.0 | 245.0 | 245.0 | 245.0 | 245.0 |
| Sugar Sweetened Beverage Tax | - | 7.5 | 15.0 | 15.0 | 15.0 | 15.0 |
| Stadium Admission Tax | 1.2 | 1.4 | 1.2 | 5.5 | 5.5 | 5.5 |
| Access Line Tax | 46.5 | 49.6 | 49.2 | 50.9 | 52.4 | 54.0 |
| Subtotal - Local Tax Revenues | 3,385.3 | 3,420.4 | 3,630.4 | 3,738.4 | 3,835.1 | 3,919.8 |
| Licenses, Permits & Franchises | 29.3 | 30.0 | 30.5 | 30.7 | 30.8 | 31.0 |
| Fines, Forfeitures & Penalties | 2.7 | 4.6 | 4.6 | 4.6 | 4.6 | 4.6 |
| Interest & Investment Income | 24.2 | 18.2 | 24.7 | 24.9 | 25.2 | 25.4 |
| Rents & Concessions | 15.6 | 14.1 | 15.0 | 15.0 | 15.0 | 15.0 |
| Subtotal - Licenses, Fines, Interest, Rent | 71.8 | 66.8 | 74.7 | 75.1 | 75.6 | 76.0 |
| Social Service Subventions | 238.8 | 257.2 | 261.9 | 261.9 | 261.9 | 261.9 |
| Other Grants & Subventions | (8.5) | 7.3 | 8.6 | 8.6 | 8.6 | 8.6 |
| Subtotal - Federal Subventions | 230.2 | 264.5 | 270.5 | 270.5 | 270.5 | 270.5 |
| Social Service Subventions | 209.9 | 225.1 | 227.3 | 230.9 | 226.3 | 221.7 |
| Health & Welfare Realignment - Sales Tax | 154.0 | 156.3 | 158.8 | 162.2 | 165.7 | 169.2 |
| Health & Welfare Realignment - VLF | 38.1 | 32.3 | 43.8 | 44.2 | 44.6 | 45.0 |
| Health & Welfare Realignment - CalWORKs | 14.9 | 21.6 | 21.6 | 21.6 | 21.6 | 21.6 |
| Health/Mental Health Subventions | 148.9 | 159.3 | 148.6 | 148.6 | 148.6 | 148.6 |
| Public Safety Sales Tax | 100.4 | 101.6 | 103.3 | 104.9 | 106.4 | 108.0 |
| Motor Vehicle In-Lieu (County & City) | 0.7 | - | - | - | - | - |
| Public Safety Realignment (AB109) | 35.5 | 41.3 | 36.0 | 36.7 | 37.4 | 38.2 |
| Other Grants & Subventions | 22.4 | 14.0 | 14.3 | 14.3 | 14.3 | 14.3 |
| Subtotal - State Subventions | 724.8 | 751.7 | 753.9 | 763.5 | 765.0 | 766.7 |
| General Government Service Charges | 65.1 | 67.5 | 65.9 | 65.9 | 65.9 | 65.9 |
| Public Safety Service Charges | 46.2 | 43.3 | 43.3 | 43.3 | 43.3 | 43.3 |
| Recreation Charges - Rec/Park | 20.8 | 20.3 | 20.5 | 20.5 | 20.5 | 20.5 |
| MediCal, MediCare & Health Svc. Chgs. | 62.4 | 84.1 | 83.6 | 83.6 | 83.6 | 83.6 |
| Other Service Charges | 17.2 | 17.7 | 18.8 | 18.8 | 18.8 | 18.8 |
| Subtotal - Charges for Services | 211.7 | 232.9 | 232.1 | 232.1 | 232.1 | 232.1 |
| Recovery of General Government Costs | 10.9 | 9.9 | 9.4 | 9.4 | 9.4 | 9.4 |
| Other General Fund Revenues | 37.8 | 43.4 | 44.1 | 44.1 | 44.1 | 44.1 |
| TOTAL REVENUES | 4,672.5 | 4,789.6 | 5,015.1 | 5,133.1 | 5,231.8 | 5,318.6 |
| Transfers in to General Fund | | | | | | |
| Airport | 45.0 | 45.6 | 45.5 | 50.6 | 52.2 | 53.9 |
| Other Transfers | 201.7 | 125.5 | 122.8 | 122.8 | 122.8 | 122.8 |
| Total Transfers-In | 246.8 | 171.1 | 168.3 | 173.4 | 175.0 | 176.8 |
| TOTAL GF Revenues and Transfers-In | 4,919.3 | 4,960.7 | 5,183.4 | 5,306.6 | 5,406.8 | 5,495.4 |

Table A-3b shows the percent change in General Fund revenues projected over the next four years.

Table A-3b. Growth Factors for General Fund Revenue Projections FY 2018-22

| | FY 2018-19 | FY 2019-20 | FY 2020-21 | FY 2021-22 |
|---|--|--|--|--|
| | % Chg from FY 2017-18 Original Budget | % Chg from FY 2018-19 Projection | % Chg from FY 2019-20 Projection | % Chg from FY 2020-21 Projection |
| Property Taxes | 7.1% | 3.7% | 3.5% | 3.4% |
| Business Taxes | 17.7% | 2.7% | 2.3% | 1.3% |
| Sales Tax | -1.8% | 1.0% | 1.0% | 1.0% |
| Hotel Room Tax | 3.6% | 3.4% | 2.5% | 2.0% |
| Utility Users Tax | 2.0% | 0.9% | 1.1% | 1.2% |
| Parking Tax | 2.6% | 0.0% | 0.0% | 0.0% |
| Real Property Transfer Tax | -18.3% | 0.0% | 0.0% | 0.0% |
| Sugar Sweetened Beverage Tax | 100.0% | 0.0% | 0.0% | 0.0% |
| Stadium Admission Tax | -11.8% | 358.3% | 0.0% | 0.0% |
| Access Line Tax | -0.7% | 3.3% | 3.1% | 3.0% |
| Subtotal - Tax Revenues | 6.1% | 3.0% | 2.6% | 2.2% |
| Licenses, Permits & Franchises | 1.8% | 0.6% | 0.6% | 0.6% |
| Fines, Forfeitures & Penalties | 0.0% | 0.0% | 0.0% | 0.0% |
| Interest & Investment Income | 35.7% | 1.0% | 1.0% | 1.0% |
| Rents & Concessions | 6.4% | 0.0% | 0.0% | 0.0% |
| Subtotal - Licenses, Fines, Interest, Rent | 11.8% | 0.6% | 0.6% | 0.6% |
| Social Service Subventions | 1.8% | 0.0% | 0.0% | 0.0% |
| Other Grants & Subventions | 17.8% | 0.0% | 0.0% | 0.0% |
| Subtotal - Federal Subventions | 2.3% | 0.0% | 0.0% | 0.0% |
| Social Service Subventions | 1.0% | 1.6% | -2.0% | -2.0% |
| Health & Welfare Realignment - Sales Tax | 1.6% | 2.1% | 2.1% | 2.1% |
| Health & Welfare Realignment - VLF | 35.7% | 0.9% | 0.9% | 0.9% |
| Health & Welfare Realignment - CaWORKs MOE | -0.1% | 0.0% | 0.0% | 0.0% |
| Health/Mental Health Subventions | -6.7% | 0.0% | 0.0% | 0.0% |
| Public Safety Sales Tax | 1.6% | 1.5% | 1.5% | 1.5% |
| Motor Vehicle In-Lieu (County & City) | 0.0% | 0.0% | 0.0% | 0.0% |
| Public Safety Realignment (AB 109) | -12.9% | 2.0% | 2.0% | 2.0% |
| Other Grants & Subventions | 2.1% | 0.0% | 0.0% | 0.0% |
| Subtotal - State Subventions | 0.3% | 1.3% | 0.2% | 0.2% |
| General Government Service Charges | -2.2% | 0.0% | 0.0% | 0.0% |
| Public Safety Service Charges | -0.1% | 0.0% | 0.0% | 0.0% |
| Recreation Charges - Rec/Park | 0.7% | 0.0% | 0.0% | 0.0% |
| MediCal, MediCare & Health Svc. Chgs. | -0.6% | 0.0% | 0.0% | 0.0% |
| Other Service Charges | 6.0% | 0.0% | 0.0% | 0.0% |
| Subtotal - Charges for Services | -0.4% | 0.0% | 0.0% | 0.0% |
| Recovery of General Government Costs | -4.8% | 0.0% | 0.0% | 0.0% |
| Other Revenues | 1.6% | 0.0% | 0.0% | 0.0% |
| TOTAL REVENUES | 4.7% | 2.4% | 1.9% | 1.7% |
| Transfers in to General Fund | | | | |
| Airport | -0.4% | 11.3% | 3.2% | 3.3% |
| Other Transfers | -2.1% | 0.0% | 0.0% | 0.0% |
| Total Transfers In | -1.7% | 3.1% | 0.9% | 1.0% |
| TOTAL GF Revenues and Transfers-In | 4.5% | 2.4% | 1.9% | 1.6% |

SOURCES – One-Time Sources Including Fund Balance & One-Time Reserves

Change in Starting Fund Balances

This plan assumes available fund balance of \$357.7 million, including \$288.2 million previously appropriated in FY 2018-19 by the FY 2017-18 and FY 2018-19 adopted budget, and anticipated surpluses from FY 2016-17 and FY 2017-18 of \$11.9 million and \$57.6 million, respectively. The report assumes one third of this fund balance will be used in FY 2018-19 and two-thirds will be used in FY 2019-20 as a one-time source. This results in a year over year reduction in starting fund balances of \$62.6 million in FY 2018-19, an increase of \$119.2 million in FY 2019-20, and a loss of \$238.5 million in FY 2020-21.

Changes in Use of Reserves

There are no uses of reserves assumed in any of the plan years. Please see Table A-5 below for detail on reserve balances.

SOURCES – Other Citywide and Departmental Revenues

Department of Public Health Revenues

The Department of Public Health (DPH) projects a revenue decrease of \$5.0 million in FY 2018-19, followed by increases of \$14.9 million in FY 2019-20, \$6.7 million in FY 2020-21, and \$7.0 million in FY 2021-22. The decrease in revenue in FY 2018-19 is attributed to scheduled funding reductions under the Medi-Cal 1115 Waiver implementing reductions to federal Disproportionate Share Hospital payments to California under the Affordable Care Act. This decrease is partially offset by projected growth in revenues from direct patient care in the San Francisco Health Network (SFHN), including capitated and fee-for-service reimbursement and rate increases for skilled nursing at Laguna Honda Hospital. Approximately 94,000 individuals are currently enrolled to receive health care services at SFHN through programs including Medi-Cal Managed Care, Healthy Workers, and Healthy San Francisco. The forecast assumes SFHN will maintain this level of enrollment. Fee-for-service and capitation payments are assumed to increase by an average of 2.25% each year.

Other General Fund-Supported Revenues

Other General Fund supported revenues are projected to increase by \$25.2 million in FY 2018-19, \$8.7 million in FY 2019-20, \$4.4 million by FY 2020-21, and \$4.5 million in FY 2021-22. These revenues include Human Services Agency revenues and Airport revenues as well as other small changes.

- **Human Services Agency Revenues:** The Human Services Agency (HSA) is projected to draw incremental state and federal revenues to pay for additional salaries and fringe benefit costs. In FY 2016-17, the Department had anticipated drawing down revenues for approximately 37.8% of salary and benefit costs in each year; however, moving forward, they estimate that increases above the FY 2017-18 salary and benefits amounts will result in drawdowns of only 29%. Given this, resulting incremental revenue increases will be of \$3.4 million in FY 2018-19, \$3.5 million in FY 2019-20, \$2.8 million in FY 2020-21, and \$2.8 million in FY 2021-22.
- **Airport Revenues:** The General Fund receives a portion of Airport concessions revenue annually. For FY 2018-19 through FY 2021-22, the Airport projects these revenues to decrease by \$0.2 million, and then increase by \$5.1 million, \$1.6 million, and \$1.7 million, respectively. The initial decrease in revenues is a result of the temporary closure of the duty-free concession area for construction.

USES – Baselines and Reserves

Changes to Baselines

The Charter specifies baseline-funding levels for various programs or functions that are generally linked to changes in discretionary General Fund revenues, though some are a function of citywide expenditures or base-year program expenditure levels.

As a result of growing discretionary revenue, the City’s mandated contributions to baselines and set-asides is increasing by \$65.5 million, \$50.7 million, \$40.4 million, and \$34.8 million in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively. Changes to a selection of baseline contributions and spending requirements are summarized below and in Table A-4. Please note that Table A-4 is not a comprehensive list of all revenue allocation and spending requirements.

Table A-4. Selected Baselines and Mandated Expenditures FY 2018-22 (\$ in millions)

| Total Contribution | FY 17-18 | | | | |
|--|----------------|----------------|----------------|----------------|----------------|
| | Budget | FY 18-19 | FY 19-20 | FY 20-21 | FY 21-22 |
| MTA Baselines (Including Prop B) | 418.4 | 448.3 | 473.5 | 490.1 | 502.5 |
| Public Education Enrichment Fund | 109.2 | 116.1 | 119.8 | 122.9 | 125.7 |
| Children's Fund (Property Tax Set Aside) | 86.4 | 99.0 | 102.6 | 106.2 | 109.7 |
| Children's Baseline | 164.8 | 175.2 | 180.7 | 185.4 | 189.6 |
| Library Preservation Fund (Baseline) | 78.0 | 82.9 | 85.5 | 87.8 | 89.7 |
| Recreation and Parks Baseline | 70.2 | 73.2 | 76.2 | 79.2 | 82.2 |
| Dignity Fund | 44.1 | 47.1 | 50.1 | 53.1 | 56.1 |
| Housing Trust Fund | 31.2 | 34.2 | 37.0 | 39.8 | 42.6 |
| Controller- City Services Auditor | 16.3 | 16.5 | 17.1 | 17.6 | 18.1 |
| Municipal Symphony Baseline | 2.9 | 3.1 | 3.3 | 3.4 | 3.5 |
| | 1,021.5 | 1,095.6 | 1,145.6 | 1,185.5 | 1,219.8 |
| Change from Prior Year | FY 18-19 | | | | |
| MTA Baselines (Including Prop B) | | 29.9 | 25.2 | 16.6 | 12.4 |
| Public Education Enrichment Fund | | 6.9 | 3.6 | 3.2 | 2.8 |
| Children's Fund (Property Tax Set Aside) | | 12.7 | 3.5 | 3.6 | 3.5 |
| Children's Baseline | | 10.4 | 5.5 | 4.8 | 4.2 |
| Library Preservation Fund (Baseline) | | 4.9 | 2.6 | 2.3 | 2.0 |
| Recreation and Parks Baseline | | 3.0 | 3.0 | 3.0 | 3.0 |
| Dignity Fund | | 3.0 | 3.0 | 3.0 | 3.0 |
| Housing Trust Fund | | 3.0 | 2.8 | 2.8 | 2.8 |
| Controller- City Services Auditor | | 0.2 | 0.6 | 0.5 | 0.5 |
| Municipal Symphony Baseline | | 0.2 | 0.1 | 0.1 | 0.1 |
| | | 74.2 | 50.0 | 39.8 | 34.3 |

Note: Does not include Transitional Aged Youth baseline, Street Tree Maintenance baseline or property tax allocations to Open Space or Library Preservation Funds.

The City’s current baselines include:

- MTA Baselines (including Prop B):** Charter section 8A.105 establishes a minimum level of funding for the Municipal Transportation Agency (MTA) and the Parking and Traffic Commission within the MTA. Funding for these two baselines is adjusted annually by the percent increase or decrease in General Fund Aggregate Discretionary Revenues (ADR). In addition, this baseline is required to be adjusted for significant service increases. Beginning in FY 2019-20, the MTA baseline will be increased due to the opening of the Central Subway. Also included in the MTA

baseline total is an amount equal to 80% of annual parking tax revenue as mandated by Charter Section 16.110.

Proposition B, passed by the voters in November 2014, additionally adjusts these baselines by the growth in population; first, in FY 2015-16 by the cumulative growth in population during the most recent ten year period, and subsequently by the annual growth in population.

The funds provided through Proposition B must be appropriated as follows:

- 75% of funds for transit system improvements to the Municipal Railway to improve the system’s reliability, frequency of service, capacity and state of good repair; and
 - 25% of funds for transportation capital expenditures to improve street safety for all users.
- Combining all required Muni baselines and parking tax transfers, the MTA is expected to receive additional incremental baseline revenue of \$29.9 million, \$25.2 million, \$16.6 million, and \$12.4 million, in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively.
- **Children’s Fund Property Tax Set-aside:** Proposition C extended the Children’s Fund and the property tax set-aside for 25 years, until June 30, 2041 and increased the property tax set-aside from \$0.03 for each \$100 of assessed property value in FY 2014-15 growing to \$0.04 by FY 2018-19. In addition, Proposition C added a new priority population to benefit: Transitional Aged Youth (TAY). The overall value of the Children and Youth Fund will increase from \$86.4 million in FY 2017-18 to \$99.0 million in FY 2018-19, \$102.6 million in FY 2019-20, \$106.2 million in FY 2020-21, and \$109.7 million in FY 2021-22. These are year over year increases of \$12.7 million, \$3.5 million, \$3.6 million, and \$3.5 million in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively.
- **Public Education Enrichment Fund Annual Contribution:** Proposition C, passed by the voters in November 2014, extended the Public Education Enrichment Fund Annual Contribution (PEEF) for 26 years, until June 30, 2041, eliminated a provision that allowed the City to defer up to a quarter of the contribution to PEEF in any year the City had a budget shortfall of \$100.0 million or more, and eliminated a credit for in-kind services allowed as an offset against the contribution.

The PEEF contribution as well as baseline are projected to increase by \$6.9 million, \$3.6 million, \$3.2 million, and \$2.8 million in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively. These increases reflect the percentage increase in the City’s aggregate discretionary revenue over the next four years, as prescribed by Charter Section 16.123-2.
- **Children’s Baseline:** Charter Section 16.108 established a Children’s Service Fund, where a base amount of required spending was established, adjusted annual by changes in ADR. Based on projected aggregate discretionary revenue, this report assumes a shortfall from required expenditure appropriation for the Children’s Baseline of \$1.0 million in FY 2018-19, \$5.6 million in FY 2019-20, \$4.8 million in FY 2020-21, and \$4.2 million in FY 2021-22.
- **Housing Trust Fund:** This report assumes that the Housing Trust Fund will continue to grow by \$2.8 million in each year, as prescribed by Charter.
- **Dignity Fund:** In November 2016, voters adopted Proposition I, a charter amendment creating the Dignity Fund and setting baseline appropriations to support seniors and adults with

disabilities. The measure requires the City to set a \$38.0 million baseline for the Dignity Fund in FY 2016–17, increasing by \$6.0 million in FY 2017–18, and \$3.0 million annually beginning in FY 2018–19. The City may temporarily suspend the required increases in any year beginning in FY 2017–18 in which a General Fund deficit of \$200.0 million or more is projected. This report assumes the Fund will grow by \$3.0 million in each year and does not assume suspension of required increases in any years.

- **Recreation and Parks Baseline:** In June 2016, voters adopted Proposition B, a charter amendment setting baseline appropriations to the Recreation and Parks Department. The FY 2015-16 budget appropriated approximately \$64.0 million of General Fund support to the department. The measure requires the City to increase those appropriations by \$3.0 million annually for the next ten years, after which it is adjusted by the change in General Fund aggregate discretionary revenues. The City may temporarily suspend the required increases in any year beginning in FY 2017–18 in which a General Fund deficit of \$200.0 million or more was forecast. This report does not assume suspension of required increases in any years.

Other Baseline and Mandate Requirements: In addition to those listed above, the Charter specifies baseline-funding levels for various programs or functions, including the Public Library, Children's Services, the Human Services Care Fund, and the City Services Auditor. Baseline amounts are generally linked to changes in discretionary city revenues, though some are a function of citywide expenditures or base-year program expenditure levels.

Changes to Reserves

The net change in deposits to reserves is estimated to be a cost of \$12.8 million in FY 2018-19, followed by savings of \$9.8 million in FY 2019-20, \$0.5 million of cost in FY 2020-21, and \$0.5 million of savings in FY 2021-22. Key changes to reserves are summarized below and reflected in Table A-5.

The City has a number of reserves that are available to insulate the City's budget and services from a dramatic event and soften the impact of economic shocks. Projected deposits to reserves include:

- **General Reserve:** Consistent with the financial policies adopted by the Board of Supervisors in April 2010 and codified in Administrative Code Section 10.60(b), this report anticipates the General Reserve rising from 2.25% of regular General Fund revenues in FY 2017-18 to 2.5% in FY 2018-19, 2.75% in FY 2019-20, and 3% in FY 2021-21 and after. Projected deposits to the General Reserve total \$18.1 million, \$15.7 million, \$15.9 million, and \$2.7 million in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively. This report does not assume General Reserve withdrawals in any year.
- **Rainy Day Economic Stabilization Reserve:** Charter Section 9.113.5 establishes a Rainy Day Economic Stabilization Reserve funded by 50% of revenue growth over 5%, which can be used when revenues decline. This report assumes no deposits to or withdrawals from this reserve.
- **Rainy Day One-Time Reserve:** Charter Section 9.113.5 establishes a Rainy Day One-Time Reserve funded by 25% of revenue growth over 5%, which can be used towards one-time expenses. This report assumes no withdrawals from this reserve.
- **Budget Stabilization Reserve:** Consistent with projections of transfer tax revenue, as well as the financial policies adopted by the Board of Supervisors in April 2010 and codified in

Administrative Code Section 10.60(b), this report anticipates no deposits to or withdrawals from this reserve during the plan period.

- Salary and Benefits Reserve:** In each of the four years, this plan projects increasing the Salary and Benefits Reserve by CPI from the \$14.5 million level appropriated in FY 2018-19 to support costs related to labor agreements not budgeted in individual departments, and assumes the entire reserve will be fully spent each year. The projected reserve need increases by \$10.3 million in FY 2018-19 to cover the cost to staff 24/7 operations on weekend days at the end of each fiscal year (Saturday, June 29 and Sunday, June 30, 2019). Future year reserve needs are assumed to grow by CPI.
- Litigation Reserve:** This reserve supports annual city liabilities related to claims, settlements, and judgments. This plan assumes \$11.0 million in FY 2018-19, as previously appropriated, and continues at that level in all subsequent years.

Table A-5 outlines the projected uses, deposits, and balances of all reserves discussed above and in the Sources section of this Plan.

Table A-5. Projected Uses, Deposits & Balances of Reserves FY 2018-22 (\$ in millions)

| | FY 17-18 (Deposit)/ Use | FY 18-19 (Deposit)/ Use | FY 19-20 (Deposit)/ Use | FY 20-21 (Deposit)/ Use | FY 21-22 (Deposit)/ Use |
|---|-------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| General Reserve | (14.6) | (15.4) | (15.4) | (15.7) | (3.3) |
| Budget Savings Incentive Fund | - | - | - | - | - |
| Recreation & Parks Budget Savings Incentive Reserve | - | - | - | - | - |
| Rainy Day Economic Stabilization Reserve | - | - | - | - | - |
| Rainy Day One-Time Reserve | - | - | - | - | - |
| Budget Stabilization Reserve | - | - | - | - | - |
| Salary and Benefits Reserve* | (19.3) | (24.8) | (15.6) | (16.1) | (16.6) |
| Litigation Reserve* | (11.0) | (11.0) | (11.0) | (11.0) | (11.0) |
| TOTAL | (44.9) | (51.2) | (42.0) | (42.8) | (30.9) |

| | FY 16-17 Ending Balance | FY 17-18 Ending Balance | FY 18-19 Ending Balance | FY 19-20 Ending Balance | FY 20-21 Ending Balance | FY 21-22 Ending Balance |
|---|-------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| General Reserve | 90.2 | 104.9 | 120.3 | 135.6 | 151.3 | 154.6 |
| Budget Savings Incentive Fund | 58.6 | 58.6 | 58.6 | 58.6 | 58.6 | 58.6 |
| Recreation & Parks Budget Savings Incentive Reserve | 3.6 | 3.6 | 3.6 | 3.6 | 3.6 | 3.6 |
| Rainy Day Economic Stabilization Reserve | 75.0 | 75.0 | 75.0 | 75.0 | 75.0 | 75.0 |
| Rainy Day One-Time Reserve | 45.1 | 45.1 | 45.1 | 45.1 | 45.1 | 45.1 |
| Budget Stabilization Reserve | 178.4 | 178.4 | 178.4 | 178.4 | 178.4 | 178.4 |
| Salary and Benefits Reserve* | - | - | - | - | - | - |
| Litigation Reserve* | - | - | - | - | - | - |
| TOTAL | 451.0 | 465.6 | 481.0 | 496.4 | 512.1 | 515.4 |

* These reserves are assumed to either be spent or closed to fund balance at the end of each fiscal year.

USES – Salaries and Benefits

This report projects General Fund supported salaries and fringe benefits to increase by \$132.7 million in FY 2018-19, \$158.1 million in FY 2019-20, \$147.0 million in FY 2020-21, and \$121.2 million in FY 2021-22. These increases, discussed in greater detail below, reflect the annualization of partial year positions approved in the current fiscal year, provisions in collective bargaining agreements, health and dental benefits for current and retired employees, retirement benefit costs, and other salary and benefit costs.

Growth in salary and benefits have escalated significantly over recent years, and continue to be a considerable driver of increasing deficits in the final years of this report. The rise of salary and benefit costs over the four years of this plan represent 49% of the growth in the deficit projections - the largest driver of the escalating deficit. Notably, employer pension contributions have spiked due to a multitude of factors in recent years, even despite higher than expected returns for 2017. Further, employer costs associated with employee health benefits continue to far outpace inflation.

Annualization of Partial Year Positions: In FY 2018-19, the City is projected to incur \$3.9 million in additional costs to annualize positions funded for only a partial year in the FY 2017-18 budget.

Previously Negotiated Closed Labor Agreements: The additional salary and benefit costs of closed labor agreements are projected to be \$57.1 million for FY 2018-19. The majority of City unions have closed Memorandum of Understandings (MOU), with a negotiated rate increase of 3% for FY 2018-19. Police officers and firefighter unions have open contracts starting in FY 2018-19 and will enter negotiations for Memoranda of Understanding (MOUs) with the City in the spring of 2018.

Projected Costs of Open Labor Agreements: Police officers and firefighter unions have open contracts starting in FY 2018-19 and will enter negotiations for Memoranda of Understanding (MOUs) with the City in the spring of 2018. Therefore beginning in FY 2018-19 the plan projects negotiated salary increases equal to the change in the Consumer Price Index (CPI) using the average projection of the California Department of Finance San Francisco Area CPI and Moody's SF Metropolitan Statistical Area CPI. This corresponds to 3.27% for FY 2018-19, 3.33% for FY 2019-20, 3.11% for FY 2020-21, and 3.04% for FY 2021-22. All other unions will have open contracts starting in FY 2019-20, and similarly for the purposes of projections, the plan applies CPI for those open contracts.

The additional salary and benefit costs for open collective bargaining agreements, using these assumptions, are projected to be \$17.5 million in FY 2018-19, \$100.8 million in FY 2019-20, \$98.1 million in FY 2020-21, and \$98.3 million in FY 2021-22. These increases are provided for projection purposes only; actual costs will be determined in labor negotiations to be conducted in FY 2017-18 for police officers and firefighters and FY 2018-19 for most other employee bargaining units.

Health and Dental Benefits for Current Employees: Each year, the San Francisco Health Service System (HSS) negotiates subsequent year rates in the spring, the HSS Board adopts these rates in July, and then HSS holds open enrollment for employees every October.

Overall, costs for employer contributions for health and dental benefits for active employees are expected to grow at a rapid rate far outpacing inflation. These cost increases are driven by a multitude of factors, notably attempts at the federal level to undermine the foundations of the Affordable Care Act have caused great uncertainty and instability in the health care market. Additionally, the precipitous increase of pharmaceutical prices is driving up the cost of plans.

Projections in this report assume increases in health and dental rates for active employees of approximately 6% in FY 2018-19 and an additional 8% for each the remaining three years of the Report. Given these assumptions, health and dental insurance premium costs paid by the employer related to current employees are projected to increase by \$15.0 million in FY 2018-19, \$21.4 million in FY 2019-20, \$23.1 million in FY 2020-21, and \$24.9 million in FY 2021-22.

Health and Dental Benefits for Retired City Employees: Charter Section A8.428 mandates health coverage for retired city employees. This projection assumes that the cost of medical benefits for retirees will increase by 9% per year over the next four years. Therefore, General Fund support for

retiree health costs increases by \$9.3 million in FY 2018-19, \$10.0 million in FY 2019-20, \$10.9 million in FY 2020-21, and \$11.9 million in FY 2021-22.

Proposition B, passed by voters in June of 2008, began to address the system's unfunded liability by requiring employees hired after January 10, 2009 and the City to contribute 2% and 1% of pre-tax compensation, respectively, into a Retiree Health Care Trust Fund. Proposition C, passed by voters in November of 2011, enhanced Proposition B's effects by requiring all remaining employees to begin contributing to this fund beginning in FY 2016-17 with corresponding employer contribution. Starting July 1, 2016, employees hired before January 10, 2009 began contributing 0.25% of pre-tax compensation into the retiree health care trust fund with additional 0.25% of each subsequent year, up to a maximum of 1%, and the City matches the contribution commensurately. As a result, this report also assumes General Fund contribution to the Retiree Health Care Trust Fund will grow \$3.7 million in FY 2018-19, \$1.7 million FY 2019-20, \$1.9 million in FY 2020-21, and \$2.0 million in FY 2021-22. The Trust assets at the end of FY 2016-17 were approximately \$187 million; an increase of \$138 million from FY 2013-14 yearend.

Similar to active employee cost increases, changes at the Federal level to amend or undercut the Affordable Care Act, as well as the increasing cost of pharmaceuticals are increasing the cost of health plans. Another key risk surrounds plans by the Federal government to voucherize Medicare, which would likely further increase the cost of retiree healthcare for the City.

Retirement Plan Employer Contribution Rates rise: SFERS employer contribution rates have risen significantly over the past couple years, substantially reversing prior year downward cost projections. At the time of March 2015 projections the City expected to see a decline in employer contributions to employee pensions. However, this trend was reversed significantly starting in 2016 due to several factors, outlined below. This report also reflects that despite 2017 returns exceeding projected return levels, an additional on-going supplemental COLA to certain retirees that is triggered by this one-time good news for returns, is adding even greater cost to the City's contribution rates. Details of these factors driving increased employer contribution costs include:

- An appellate court ruling against the City invalidated certain voter-adopted restrictions that would have placed additional conditions required to be met for retirees to receive a supplemental cost-of-living increase, and necessitated incorporation of two retroactive supplemental COLAs arising from 2013 and 2014 returns into contribution rate assumptions. Returns that exceed the 7.5% actuarially assumed rate trigger a supplemental cost-of-living adjustment (COLA) payment to certain retirees.
- Additionally, despite updated FY 2016-17 year-end return on assets which were 13.5%, 6.0% above the actuarially assumed rate of return of 7.5% per year, employer contributions are increasing in the first year of the Report due to the one-time benefit of the better than expected returns funding an on-going increase to some retirees supplemental COLA.
- Lower than expected actual FY 2014-15 and FY 2015-16 investment returns continue to impact employer contribution rates.
- Updated demographic assumptions show that retirees are living longer and collecting pensions longer than previously expected.

The San Francisco Employee Retirement System (SFERS) contribution rates are based on updated projections prepared by the Retirement System's Actuary incorporating amortization of unfunded actuarial accrued liability arising from the 2013 and 2014 Supplemental COLAs for Post-1996 Retirees in

September 2016, in addition to the 2017 return supplemental COLA as well. The plan does not assume supplemental COLAs will be paid to employees who retired prior to 1996; if the City needed to pay supplemental COLAs to this group it would further increase projected deficits.

SFERS contribution rates are based on projections prepared by the Retirement System's Actuary in October 2017. They assume continuation of the SFERS Board adopted long term investment return assumptions of 7.5% for FY 2018-19 onwards. Projections reflect employee contributions to retirement required under Proposition C.

The maximum employer contribution rate for non-safety employees in salary band 2 is 19.25% in the current fiscal year. This rate is projected to increase to 20.5%, 20.5%, 21.4%, and 20.4% in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively. Rates for police and fire safety employees vary based on date of hire. This report assumes the weighted average employer contribution rate for FY 2017-18 for police officers and fire fighters was 18.55% increasing to 19.8%, 19.8%, 20.7%, and 19.7% over the next four years.

For CalPERS members, the rate in the current year is 28.13% and is projected to increase to 31.1%, 35.3%, 40.5% and 44.1% in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively.

The net result of these changes to the employer share for SFERS and CalPERS contribution rates is an increase in total General Fund support of \$25.9 million in FY 2018-19, \$4.2 million in FY 2019-20, \$22.0 million in FY 2020-21, and reducing by \$17.2 million in FY 2021-22.

Table A-6 below reflects the total contribution rate, the portion of the rate that employees contribute, and the City's portion.

Table A-6. Estimated Employer Contribution Rates for the Retirement System
San Francisco Employees Retirement System (SFERS)

| | FY 2017-18 | FY 2018-19 | FY 2019-20 | FY2020-21 | FY2021-22 |
|---|------------|------------|------------|-----------|-----------|
| Estimated Total Contribution Rates | 31.5% | 31.7% | 32.1% | 33.6% | 33.0% |
| Non-Safety | | | | | |
| Employee Contribution (1) | | | | | |
| Band 1, < \$26.66/hour | 7.5% | 7.5% | 7.5% | 7.5% | 7.5% |
| Band 2, < \$53.32/hour | 11.0% | 11.0% | 11.0% | 11.0% | 11.0% |
| Band 3, >\$53.32/hour | 11.5% | 11.5% | 11.5% | 11.5% | 11.5% |
| Additional rate factors | | | | | |
| Band 1, < \$26.66/hour | 0.9% | 0.9% | 0.9% | 0.9% | 0.9% |
| Band 2, < \$53.32/hour | 0.7% | 0.7% | 0.7% | 0.8% | 0.8% |
| Band 3, >\$53.32/hour | 0.7% | 0.7% | 0.7% | 0.8% | 0.8% |
| Estimated Net Employer Contribution (1) | | | | | |
| Band 1, < \$26.66/hour | 23.1% | 23.3% | 23.7% | 25.2% | 24.6% |
| Band 2, < \$53.32/hour | 19.8% | 20.0% | 20.4% | 21.8% | 21.2% |
| Band 3, >\$53.32/hour | 19.3% | 19.5% | 19.9% | 21.3% | 20.7% |
| Police and Fire Safety Employees (2) | | | | | |
| Estimated Total Contribution Rates | 31.9% | 32.1% | 32.5% | 34.0% | 33.4% |
| Employee Contribution & additional rate factors | 12.8% | 12.8% | 12.9% | 12.9% | 12.9% |
| Estimated Net Employer Contribution | 19.0% | 19.2% | 19.6% | 21.0% | 20.5% |

California Public Employees Retirement System (CalPERS)

| | FY 2017-18 | FY 2018-19 | FY 2019-20 | FY2020-21 | FY2021-22 |
|---|------------|------------|------------|-----------|-----------|
| Total Estimated Contribution Rate | 29.8% | 33.1% | 36.4% | 38.0% | 39.7% |
| Employee Contribution & additional rate factors | 1.7% | 1.7% | 1.7% | 1.7% | 1.7% |
| Net Employer Contribution | 28.1% | 31.4% | 34.7% | 36.3% | 38.0% |

(1) Employees are divided into three bands based on wages. The wages shown are based on the FY 2016-17 wage floors.

(2) Employee base contribution rates vary depending on hire date.

Other Salaries and Fringe Benefits Costs: Other salary and benefit cost changes are expected to be modest, with the biggest changes occurring due to the changing number of work days in a given fiscal year. Most fiscal years consist of 261 workdays for regularly scheduled shifts and 365 days for 24/7 operations.

FY 2018-19 has 260 work days. As the prior year, FY 2017-18 also had only 260 regularly scheduled workdays, there are no year over year savings recognized in FY 2018-19. FY 2019-20 is a leap year and contains 262 workdays for regularly scheduled shifts; therefore, the City incurs additional General Fund costs of \$20.0 million in that year. FY 2020-21 and FY 2021-22 have 261 work days; therefore, the City incurs savings of \$9.1 million in FY 2020-21 compared to the prior year. These savings are partially offset

by assumed inflationary increases to salaries and growth rates for benefits in the final year of the projection, FY 2021-22, resulting in an incremental cost of \$1.0 million.

Other salary and benefit changes, including health service administrative and life insurance costs, have minimal projected changes.

USES – Citywide Operating Budget Costs

Over the next five years, the City will also incur increasing non-salary operating costs. Citywide non-salary operating costs are projected to increase by \$50.6 million, \$101.9 million, \$56.3 million, and \$73.2 million in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively. The impacts and costs associated with these increases span multiple departments and are described in more detail below.

Minimum Wage: In November 2014, voters adopted a Charter amendment increasing the local minimum wage from \$11.05 to \$15.00 per hour by 2018. After reaching \$15.00, the wage will increase by CPI on July 1 of every subsequent year.

Table A-7. Schedule of Minimum Wage Increases Pursuant to Proposition J

| | | | <i>Based on projected CPI</i> | <i>Based on projected CPI</i> | <i>Based on projected CPI</i> |
|--------------|-----------------|-----------------|-----------------------------------|-----------------------------------|-----------------------------------|
| | FY 17-18 | FY 18-19 | FY 19-20 | FY 20-21 | FY 21-22 |
| (start date) | (July 1, 2017) | (July 1, 2018) | (July 1, 2019) | (July 1, 2020) | (July 1, 2021) |
| New Wage | \$14.00 | \$15.00 | \$15.50 | \$15.98 | \$16.47 |

There are a limited number of city employees whose wages are affected by the Minimum Wage legislation, as well as several city contracts with service providers which directly pay for staff who will benefit from Minimum Wage increases. Notably, In-Home Supportive Services (IHSS) providers are seeing increases in their wages due to the minimum wage ordinance, since the state is no longer reimbursing counties for these costs. The minimum wage cost impacts associated with the IHSS program are not included here but reflected in the departmental cost section as part of the larger IHSS cost growth.

Overall, these changes to the City’s minimum wage result in an increase in General Fund costs of \$10.0 million in FY 2018-19, \$3.2 million in FY 2019-20, \$0.6 million in FY 2020-21, and \$0.6 million in FY 2021-22. Increases are lower in the final two years of the plan as the minimum wage increases are fully ramped up and then grow by CPI.

Capital, Equipment and Technology: Changes in funding for capital, equipment, and technology will result in General Fund cost increases of \$3.2 million in FY 2018-19, \$44.8 million in FY 2019-20, \$3.8 million in FY 2020-21, and \$14.5 million in FY 2021-22.

Table A-8. Capital, Equipment, & Technology (Millions \$)

| | Projected Levels - Absolute Costs | | | | |
|--|--|--------------|---------------|--------------|---------------|
| | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 |
| Capital Plan Budget | 137.7 | 147.3 | 157.6 | 168.6 | 180.4 |
| Capital Planning Fund (Onetime FY 2017-18 GFS) | 5.1 | - | - | - | - |
| Capital FF&E, Move Costs | 1.2 | 7.2 | 17.2 | 3.9 | 0.2 |
| Major IT Projects | 18.6 | 19.0 | 22.5 | 24.7 | 27.2 |
| Annual IT Investments | 6.9 | 1.5 | 14.1 | 15.5 | 17.1 |
| Equipment | 15.6 | 10.4 | 16.7 | 17.2 | 17.8 |
| Dept. of Technology Rates | 56.6 | 59.7 | 61.7 | 63.7 | 65.5 |
| Total One Time Costs | | 245.1 | 289.8 | 293.6 | 308.2 |
| | Incremental Change - Year-Over-Year Change | | | | |
| | 2017-18 | 2018-19 | 2019-20 | 2020-21 | 2021-22 |
| Capital Plan Budget | | (9.5) | (10.3) | (11.0) | (11.8) |
| Capital Planning Fund (Onetime FY 2017-18 GFS) | | 5.1 | - | - | - |
| Capital FF&E, Move Costs | | (6.0) | (10.0) | 13.3 | 3.7 |
| Major IT Projects | | (0.5) | (3.5) | (2.2) | (2.5) |
| Annual IT Investments | | 5.4 | (12.6) | (1.4) | (1.6) |
| Equipment | | 5.3 | (6.3) | (0.5) | (0.5) |
| Dept. of Technology Rates | | (3.1) | (2.0) | (2.0) | (1.8) |
| Incremental Change | | (3.2) | (44.8) | (3.8) | (14.5) |

This projection assumes the adopted FY 2018-19 funding level for capital, information technology (IT), and equipment. Notably, the most recent two year budget—adopted in the summer of 2017—was the first to fully fund the General Fund cash capital budget in both years of the budget. Historically, the second year of the budget has contained a lower level of funding for General Fund cash capital, necessitating a large expenditure to bring that year to full funding in the following cycle. However the FY 2017-18 and FY 2018-19 budget for the first time fully funded the capital plan in both years of the budget for \$285 million in funding. For General Fund cash capital spending in the remaining three out years of the plan, the report assumes funding will increase by 7% annually, as assumed in the City’s Ten-Year Capital Plan. This growth will take the general fund cash capital program to \$180 million annually by FY 2021-22.

Citywide information technology and communications costs for annual citywide technology costs are projected to decrease by \$5.4 million in FY 2018-19, as reflected in the adopted budget. Technology costs are then projected to increase by \$12.6 million in FY 2019-20, \$1.4 million in FY 2020-21, and \$1.6 million in FY 2021-22, consistent with the City’s latest Information and Communication Technology (ICT) Plan for FY 2017-18 through FY 2021-22.

This report also assumes an increase in funding for major Information Technology investments in the amount of \$0.5 million in FY 2018-19, \$3.5 million in FY 2019-20, \$2.2 million in FY 2020-21, and \$2.5 million in FY 2021-22. These funding levels are also consistent with the City’s ICT Plan, and assume full funding FY 2019-20 through FY 2021-22. Major IT projects assumed to receive funding in this estimate include the cost of replacing the Assessor-Recorder’s property assessment and tax system, and the cost of the citywide public safety radio replacement project. Additionally, this report assumes the implementation of the Department of Public Health’s (DPH) new integrated electronic health record (EHR) system, which will replace its existing suite of clinical, financial, and billing systems. The Department recently entered into a 10-year, \$167.4 million contract with Epic City Government, LLC for

the implementation and hosting of the EHR system. Implementation work will commence in early 2018, with a go-live in summer 2019. While there is no General Fund impact for this project, successful and timely implementation is necessary to the department's ability to appropriately bill for services, and to stay within the projected implementation budget.

Finally, the Department of Technology's rates are projected to increase by \$3.1 million in FY 2018-19, as reflected in the adopted budget, primarily due to citywide technology projects to update the City's network infrastructure and telephone systems. Rates are then projected to further increase by \$2.0 million in FY 2019-20, \$2.0 million in FY 2020-21, and \$1.8 million in FY 2021-22, due to assumed inflationary increases on salaries and benefits.

Additionally, the City will incur costs to furnish and equip new facilities. These costs will increase by \$6.0 million in FY 2018-19, will increase by \$10.0 million in FY 2019-20, then will decrease by \$13.3 million in FY 2020-21, and will decrease by another \$3.7 million in FY 2021-22. These costs are related to projects including various Fire Station improvements and replacements, the SFPD's new Crime Lab and Traffic Company facility, the new Animal Care and Control Facility, the Department of Public Health's office building replacement, and the Juvenile Probation administrative building replacement, and other large Certificates of Participation and General Obligation bond capital projects.

Citywide equipment costs are projected to decrease by \$5.3 million in FY 2018-19, as reflected in the previously adopted FY 2018-19 budget. To reach previous levels of investment as well as projected need, equipment costs are projected to increase by \$6.3 million in FY 2019-20. Increased cost assumptions based on CPI result in annual \$0.5 million increases in FY 2020-21 and FY 2021-22. Equipment is defined as an item costing \$5,000 or more with an expected life span of three years or more. This projection assumes that no equipment purchases will be funded through the use of lease revenue bonds in any of the next four years. By using cash instead of debt financing, the City saves on financing costs, reducing the overall cost of equipment purchases over the long term.

Hall of Justice Exit

The Hall of Justice is a large facility located at 850 Bryant Street. It houses numerous criminal justice related City departments as well as the San Francisco Superior Court criminal courts. City functions located at the Hall of Justice include the Police Department Investigations, Police Storage, the District Attorney, Adult Probation Department, Sheriff Warrants and Records, and the Sheriff's County Jail 4. Exiting the Hall of Justice has been a longstanding City priority, because the building has significant life safety and seismic risks.

These life safety risks include, but are not limited to, frequent sewage overflows, which originate in the jail on the top floor. In the last year, the sewage overflows reached staff and clients in offices below. These sewage overflows have a major, adverse impact on building-wide operations, compromising security and personal health and safety. Some repairs involve breaking into the asbestos-laden walls, creating an even more toxic situation to be abated. From November 2, 2016, through August 21, 2017; there were 110 flood events for County Jail #4. Numerous repairs and preventative measures have been made, to no avail. These problems are in addition to the failing elevators, Heating, Ventilation, and Air Conditioning (HVAC), and other subsystems, all of which are well beyond their useful life. These conditions have resulted in a complaint to the California Division of Occupational Safety and Health (Cal/OSHA) as well as most of the public employee unions with staff in the Hall filing grievances to the City.

The building's seismic risk is just as great as its life/safety risks. The Hall registers as one of the City's most dangerous buildings on the HAZUS analysis. That analysis, run most recently in 2017, shows that a 7.9M earthquake on the San Andreas Fault would bring to the Hall a probability of greater than 100

casualties, economic impact of greater than \$50 million, operational losses of greater than \$5 million, and greater than 70% building damage. In the event of such a disaster, the building will likely be red-tagged-uninhabitable until structural repairs can be made. This result would be a crisis situation, especially for the prisoners who would be unable to flee but also unable to remain.

In response to the unacceptable conditions at the Hall of Justice, the City Administrator’s Office, which operates the building through the Real Estate Division, has developed a plan to relocate the City functions from the Hall of Justice and close the building. The current plan includes:

- Lease privately owned office and storage space in the vicinity of the Hall of Justice to accommodate Police Investigations, Police Storage, the District Attorney, and the Adult Probation Department functions currently housed in the Hall of Justice. These moves will occur in FY 2018-19.
- Additionally, the City will issue Certificates of Participation (COPs), a form of General Fund debt, in order to finance capital improvements at the existing County Jail 2 (located on 7th Street, adjacent to the Hall of Justice) and County Jail 6 (located in San Bruno). These capital improvements will create enough additional capacity at those two facilities to house inmates currently housed in County Jail 4 in the Hall of Justice. These moves will occur in FY 2019-20.
- Once the administrative and custodial functions are removed from the City’s half of the Hall of Justice, in FY 2020-21, the City will issue additional COPs to fund a capital project which will demolish the City-occupied half of the Hall of Justice and will enclose the Superior Court-operated half of the building (which will still be in use).
- In FY 2025-26, as the administrative leases are nearing the end of their term, the City will fund the construction of a new justice administrative building at the vacated and cleared land on the Hall of Justice campus. The Police, Adult Probation, and District Attorney administrative functions, potentially among others, will then move back into the reconstructed administrative building at the hall of Justice campus.

The (costs) and savings related to closing the Hall of Justice are summarized below:

Table A-9. Hall of Justice Exit Cost

| | 2018-19 | 2019-20 | 2020-21 | 2021-22 |
|-------------------------------------|--------------|------------|-------------|--------------|
| Avoided HoJ Operating Costs | - | 4.7 | 0.8 | 0.1 |
| Cost of Leased Administrative Space | (8.2) | (2.0) | (2.4) | (0.4) |
| Moving Expenses | (7.7) | 7.7 | - | - |
| Tenant Improvements | (7.0) | 7.0 | - | - |
| General Fund Cash Capital Budget | 14.7 | (14.7) | - | - |
| Adopted Vs. New COPs | 0.2 | 0.3 | 20.6 | (3.4) |
| Incremental Change | (8.0) | 3.0 | 19.0 | (3.6) |

The City’s costs to exit the Hall of Justice and secure replacement facilities will grow by \$8 million in FY 2018-19, then will fall by \$3 million in FY 2019-20, will fall by another \$19 million in FY 2020-21, and will increase by \$3.6 million in FY 2021-22. The cost growth in FY 2018-19 is largely driven by the new administrative leases the City will need to secure in order to provide replacement space. The significant cost reductions in FY 2020-21 result because the prior plan assumed that the City would issue COPs to fund the replacement administrative building in 2021, which would have caused debt service costs to begin much sooner than with the existing plan. Furthermore the current plan assumes jail facilities

spending will total a smaller amount of money than the prior plan, resulting in a decreased debt service projection. Finally, the one-time moving and tenant improvement costs related to the administrative leases will be paid for with funds already appropriated from the City's General Fund Cash Capital budget.

Inflation on Non-Personnel Costs and Grants to Non-Profit Contractors

This projection assumes that the cost of materials and supplies, professional services, contracts with community-based organizations, and other non-personnel operating costs will increase by the CPI rate, as projected by the California Department of Finance and Moody's at a rate of 3.33% for FY 2019-20, 3.11% for FY 2020-21, and 3.04% for FY 2021-22. The projection also the adopted FY 2018-19 budgeted level of cost increases; this includes a 2.5% cost-of-doing business increase for nonprofit providers. This generates a total increase in costs to the City of \$12.8 million, \$36.3 million, \$35.0 million, and \$35.3 million in FY 2018-19, FY 2019-20, FY 2020-21, and FY 2021-22, respectively.

Debt Service & Real Estate

Over the next five years, total debt service and real estate costs are projected to increase by \$12.6 million in FY 2018-19, \$16.2 million in FY 2019-20, \$31.6 million in FY 2020-21, and \$14.8 million in FY 2021-22. This projection is based on current debt repayment requirements and projected debt service costs for investments anticipated in the Capital Plan, as well as cost increases related to the City's leased and owned real estate portfolio. This projection does not include debt service related to the Moscone Convention Center, which is reflected in the Convention Facilities Fund subsidy projection. The increases over the next several years are primarily due to the repayment of Certificates of Participation (COPs) for the replacement of the Department of Public Health office building at 101 Grove, the replacement of the Juvenile Probation administrative building, the replacement of the Animal Care and Control facility, and capital projects associated with the Justice Facilities Improvement Project (JFIP). Additionally, a smaller portion of the cost increase is due to growth in the annual cost of the City's leased and owned real estate portfolio.

Changes to the COP program and the City's leased and owned real estate costs due to the planned exit of the Hall of Justice are discussed in more detail in the section of this report dedicated to the Hall of Justice, above.

Sewer, Water, and Power Rates

The base case assumes increased General Fund transfers to the Public Utilities Commission (PUC) for the cost of sewer, water, and power expenses. Sewer and water rates have been adopted by the PUC Commission through FY 2017-18 to fund 24/7 operations and maintenance and planned capital improvement projects, including the Water System Improvement and the Sewer System Improvement Programs. The PUC will embark on adopting new rates for sewer and water in the spring of 2018 for FY 2018-19. For the purposes of this report, the four year projections utilize the increases assumed in the Wastewater and Water Ten Year Financial Plans. For FY 2018-19 and beyond, the power rate increases are from Power's Ten Year Financial Plan which assumes a half-cent per kilowatt hour (kWh) in FY 2017-18 through FY 2021-22. Additionally, the Power Enterprise bills and pays the cost of natural gas provided by Pacific Gas & Electric and the Department of General Services (DGS) to city departments. The increases in gas rates reflect increases in transportation costs, delivery of gas, and use of the pipelines. If these increases are implemented, the total General Fund impact resulting from the proposed increased sewer, water, and power rates is a cost of \$1.9 million, \$1.9 million, \$1.8 million, and \$1.9 million each year over the next four years.

Other Citywide Costs

This category includes assumed increases in costs across citywide services and other minor changes.

These items together result in increased General Fund costs of \$2.0 million, \$2.4 million, \$2.4 million, and \$2.4 million in the remaining four years of the report.

USES –Departmental Costs

This section provides a high-level overview of significant departmental costs over the next five years. Table A-1 displays departmental cost increases of \$16.6 million in FY 2018-19, \$47.2 million in FY 2019-20, \$22.9 million in FY 2020-21, and \$38.1 million in FY 2021-2022.

City Administrator’s Office – Convention Facilities Subsidy

This plan assumes the Convention Facilities Fund General Fund subsidy will decrease by \$1 million in FY 2018-19 and another \$9.6 million in FY 2019-20, then will increase by \$0.5 million in FY 2020-21 and another \$0.2 million in FY 2021-22. The decrease in subsidy needed in FY 2018-19 and FY 2019-20 are due to decreased operating losses at the Moscone Convention Center as the Moscone Expansion Project completes construction as well as a significant decrease in debt service costs in FY 2019-20. The modest increase in General Fund subsidy in FY 2020-21 and FY 2021-22 is due to slight growth in the cost of debt service and services provided by other departments.

Elections – Number of Scheduled Elections

The number of elections and the associated costs for holding elections vary annually. The current schedule includes: one Gubernatorial General Election is scheduled in FY 2018-19, two elections (a November Municipal Election and a March Presidential Primary) in FY 2019-20, one Presidential Election in FY 2020-21, and one Gubernatorial Primary Election in FY 2021-22. This schedule results in projected incremental savings of \$0.8 million in FY 2018-19 over FY 2017-18, primarily due to the receipt of bi-annual revenues from special district elections (i.e. BART, SF Unified School District, and Community College), an additional cost of \$5.9 million in FY 2019-20 due to having two scheduled elections, a savings of \$5.4 million in FY 2020-21 as a result of only have one election, and an increase of \$0.2 million in FY 2021-22. Any special election not included in this projection would result in increased General Fund costs dependent on the complexity of the ballot and the size of the electorate.

Table A-10. Number of Scheduled Elections FY 2018-19 through FY 2021-22

| Fiscal Year | Date | Type |
|--------------------|---------------|---|
| 2018-19 | November 2018 | Consolidated Gubernatorial General Election |
| 2019-20 | November 2019 | Municipal Election |
| 2019-20 | March 2020 | Consolidated Presidential Primary Election |
| 2020-21 | November 2020 | Consolidated Presidential General Election |
| 2021-22 | June 2022 | Consolidated Gubernatorial Primary Election |

Ethics Commission – Public Financing of Elections

The Ethics Commission administers the Election Campaign Fund. Annual General Fund deposits to the Campaign Fund are governed by ordinance and equal \$2.75 per resident per fiscal year with up to 15% of the amount in the Fund available for administrative costs in most years. Funds not used in one election are carried over for use in the following election and the total amount in the Fund can never exceed \$7.0 million.

The following projection assumes: General Fund deposits in all five years of the forecast; eligible candidates qualify and accept disbursements each fiscal year based on qualifying criteria and limits as established under the law for the election cycle; and that Mayoral elections will be held in FY 2019-20. Under these assumptions, General Fund costs will increase by \$0.5 million in FY 2018-19 and by an additional \$1.1 million in FY 2019-20, with no additional costs in the final two years of the plan. These costs are highly sensitive to the actual amount of funds disbursed in Mayoral and Supervisorial campaigns.

Free City College

In February 2017, San Francisco became the first city in the nation to make community college free for its residents. The Free City College Program allows California residents who live in San Francisco to attend City College of San Francisco (CCSF) for free and grants stipends to students who already receive enrollment fee waivers to make higher education accessible to as many San Franciscans as possible. The annual programmatic expenditures of \$5.4 million were initially funded with a one-time \$9 million supplemental in FY 2016-17. General Fund annual operating support is projected to phase in as this onetime source is expended with \$2.2 million in FY 2018-19 and an additional \$3.1 million, (or \$5.4 million on-going) in FY 2019-20. This program will allow more students to access the training and education they need to earn jobs that will help them to live and work in San Francisco.

Golden State Warriors Event Center

The Golden State Warriors are currently constructing a multipurpose event center and retail and office project at 16th Street and 3rd Street in Mission Bay. In November 2015, the Mayor and Board of Supervisors approved the creation of the Mission Bay Transportation Improvement Fund to pay for public infrastructure improvements, equipment and public services to address the community's transportation and other needs in connection with events at the center. In FY 2018-19, the cost will be \$0.1 million more than in FY 2017-18. From FY 2019-20 through FY 2021-22, this report projects estimated annual incremental project costs of \$7.3 million, \$0.2 million, and \$0.2 million. These costs will be funded entirely with revenue generated from the project through increased property, business, sales, hotel, utility user, and stadium admission taxes.

Mayor's Office of Housing and Community Development - HOPE SF and the Local Operating Subsidy Program

Over the next five years, costs related to HOPE SF and the Local Operating Subsidy Program will require an increase in General Fund support of \$5.2 million in FY 2018-19, \$3.3 million in FY 2019-20, \$8.6 million in FY 2020-21, and \$8.1 million in FY 2021-22. The majority of the cost growth is related to the Local Operating Support Program, an initiative which funds the ongoing operations and provides services for supportive housing units inhabited by formerly homeless individuals. Cost growth in this program is largely due to the 1,173 new units expected to come online over the next four years.

Human Services Agency – Aid

Historically, we have included IHSS (In-Home Supportive Services) in our Aid calculations. However, since that program's funding has represented significant cost increases this year (see below), it is now separated in this report from the Aid line.

The Human Services Agency projects that aid payments (including programs such as CAAP, Foster Care, CalWORKS, Care Not Cash, and others) show a decrease in General Fund support of \$1.1 million in FY 2018-19, an increase of \$1.4 million in FY 2019-20, and an additional increase of \$0.1 million in FY 2020-21, with no change in FY 2021-22. These changes are primarily due to projected changes in caseloads.

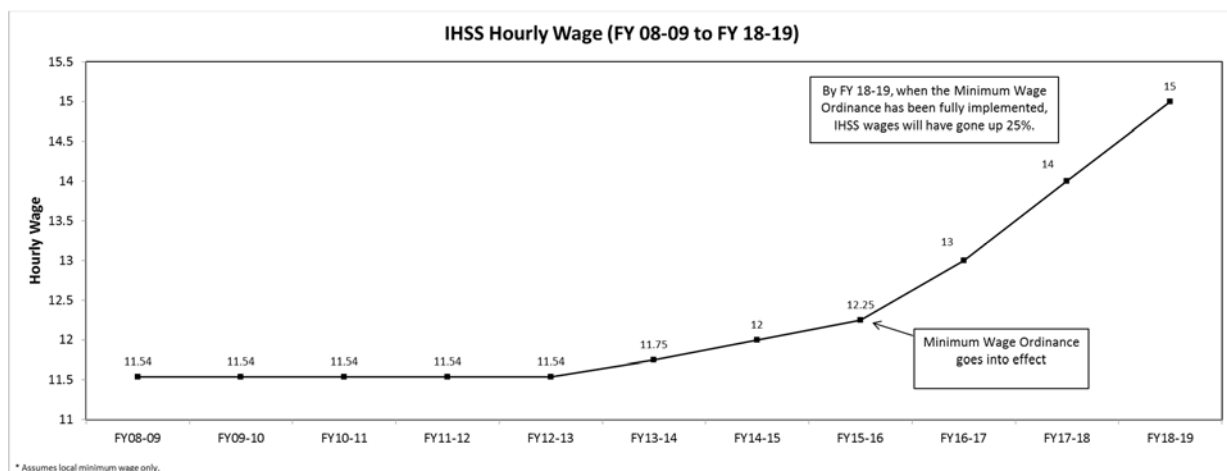
Human Services Agency – In-Home Supportive Services

The In-Home Supportive Services (IHSS) program assists about 22,000 low-income elderly, disabled, and/or blind San Franciscans to live safely in their own homes rather than in a nursing home or other group care facility. The program employs 19,000 individuals as independent providers. IHSS workers assist clients with domestic and personal care services. The program works with hospitals and other medical facilities to ensure that home care services are in place at the time of discharge, which helps to mitigate hospital readmissions. In San Francisco, IHSS is provided in two modes, the Independent Provider Mode and the Contract Mode; the latter serves the most complex clients, who are unable to manage their own care.

Since FY 2012-13, counties’ share of IHSS costs is based on a “maintenance of effort” (MOE). From the State’s 1991 Realignment until 2012, the county share of IHSS funding was 35%. The MOE cost structure in place through FY 2016-17 required counties to maintain their IHSS spending at FY 2011-12 levels, with two adjustments: an annual inflation factor of 3.5% and adjustments for any locally negotiated wage or benefit increases for IHSS workers. This framework has resulted in modest and predictable growth in counties’ share of IHSS costs over the past several years, while the state has taken on a relatively larger proportion of the program’s rising costs. The State FY 2017-18 budget reset the MOE at a higher level and increased the annual inflationary increase to 5% for FY2018-19 and 7% in subsequent fiscal years. In anticipation of these changes, the City budgeted \$11.1 million in FY 2017-18 and \$16.9 million in FY 2018-19 in cost increases for this program.

However, the trailer bill language in the State FY 2017-18 budget specifies additional instances in which a county’s MOE would be increased, resulting in additional large costs to San Francisco that were not anticipated in the City budget, beginning in FY 2017-18. One of the large cost drivers for San Francisco is the voter-approved minimum wage ordinance, which applies to IHSS workers. Under the prior MOE, wage increases resulting from voter-approved ordinances did not trigger an increase in the MOE, so the state paid the non-federal share of costs. As a result of the trailer bill language, these increases will now result in an MOE adjustment to reflect a share of the increased wage costs. Figure A-3 shows the increases in IHSS workers’ wages, which have grown 25% since implementation of the minimum wage increase in San Francisco.

Figure A-3. Growth in IHSS Providers’ Wages Due to Minimum Wage Ordinance



The updated estimates show much higher costs to San Francisco over and above the existing budget as shown below in Table A-11.

Table A-11. Impact of New IHSS MOE on San Francisco

| | FY 16-17 | FY 17-18 | FY 18-19 | FY 19-20 | FY 20-21 | FY 21-22 | Annual Growth |
|---|-------------|------------------|------------------|------------------|------------------|------------------|---------------|
| | (Budgeted) | (Budgeted) | (5-Year Proj) | (5-Year Proj) | (5-Year Proj) | (5-Year Proj) | FY 17 - FY 22 |
| Old MOE - SF Contribution | \$ 80.7 | \$ 83.5 | \$ 86.5 | \$ 89.5 | \$ 92.6 | \$ 95.9 | \$ 15.2 |
| <i>Annual 3.5% Inflation</i> | | \$ 2.8 | \$ 2.9 | \$ 3.0 | \$ 3.1 | \$ 3.2 | |
| | (Budgeted) | (New Projection) | (New Projection) | (New Projection) | (New Projection) | (New Projection) | Annual Growth |
| | (Budgeted) | (New Projection) | (New Projection) | (New Projection) | (New Projection) | (New Projection) | FY 17 - FY 22 |
| New MOE - SF Contribution | \$ 80.7 | \$ 103.4 | \$ 123.0 | \$ 146.6 | \$ 162.6 | \$ 175.4 | \$ 94.7 |
| | \$ 80.7 | \$ 83.5 | \$ 86.5 | \$ 89.5 | \$ 92.6 | \$ 95.9 | |
| <i>Revised MOE</i> | \$ - | \$ 10.0 | \$ 18.1 | \$ 33.3 | \$ 42.9 | \$ 49.0 | |
| <i>Min Wage Impact</i> | \$ - | \$ 3.7 | \$ 11.8 | \$ 16.5 | \$ 19.1 | \$ 22.1 | |
| <i>Contract Mode</i> | \$ - | \$ 2.5 | \$ 3.0 | \$ 3.6 | \$ 4.2 | \$ 4.8 | |
| <i>Admin Cap</i> | \$ - | \$ 3.7 | \$ 3.7 | \$ 3.7 | \$ 3.7 | \$ 3.7 | |
| Change in Annual SF Contribution | \$ - | \$ 19.9 | \$ 36.5 | \$ 57.1 | \$ 69.9 | \$ 79.6 | |

There are four drivers of increases in IHSS costs shown in the table above, including:

- *Maintenance of Effort (MOE).* The new MOE shifted a greater share of costs to counties. The increase was greater than originally expected.
- *Minimum wage impacts.* Language in the trailer bill indicates that a county’s IHSS MOE will be increased for wage increases resulting from local voter-approved initiatives. The City’s minimum wage remains higher than the state minimum wage (now \$14 vs. \$10.50/hour). We had previously been held harmless for our local minimum wage costs, but the new law explicitly holds counties responsible for these costs, which has an especially large impact on San Francisco due to the fast rate at which the minimum wage is rising.
- *Contract mode costs.* The trailer bill includes language indicating that the MOE will also be adjusted to reflect increased costs in IHSS contract mode. Costs are rising for IHSS services provided through Homebridge, which serves clients with mental and physical conditions that prevent them from being able to coordinate their own care. The City’s MOE will now be increased to account for these increases in IHSS contract mode.
- *Administrative costs cap.* The new MOE places a cap on the state’s contribution to administration costs, above which the non-federal share of these costs must be covered with additional local funds. Previously, the state covered any non-federal share of administrative costs beyond what the county paid through its MOE. Since regulatory language has not yet been made public, this part of the estimate is most likely subject to further change.

Our current estimates show IHSS costs increasing by \$36.5 million over the FY 2018-19 projected budget from the Five Year Plan published in 2016, an additional \$57.1 million in FY 2019-20, an additional \$69.9 million in FY 2020-21, and finally increasing by an additional \$79.6 million in FY 2021-22.

Public Health – Operating and one-time FF&E Costs

In June 2016 voters approved a \$311.0 million Public Health and Safety Bond. The bond supports Department of Public Health (DPH) capital improvements to make essential earthquake safety improvements at the Zuckerberg San Francisco General Hospital (ZSFG) campus, as well as the renovation of the Southeast Health Center. Costs assumed in this report are inclusive of the expiration of one-time expenditures for furniture, fixtures, and equipment (FF&E), and the addition of new ongoing operating funds to support additional staff and expanded services in the new health center. Additionally, the Department plans to consolidate its offices and clinics currently located in the Civic Center to more

efficient, seismically safer, and geographically appropriate locations over the next five years, and this report assumes the associated moving and FF&E costs. Together these operating and one-time costs are projected to increase by \$4.1 million in FY 2018-19 and \$1.4 million FY 2019-20, decrease by \$9.3 million in FY 2020-21, and then slightly increase by \$0.3 million in FY 2021-22 as one-time moving and FF&E savings and on-going operating expenditures are fully realized.

All Other Departmental Savings (/Costs)

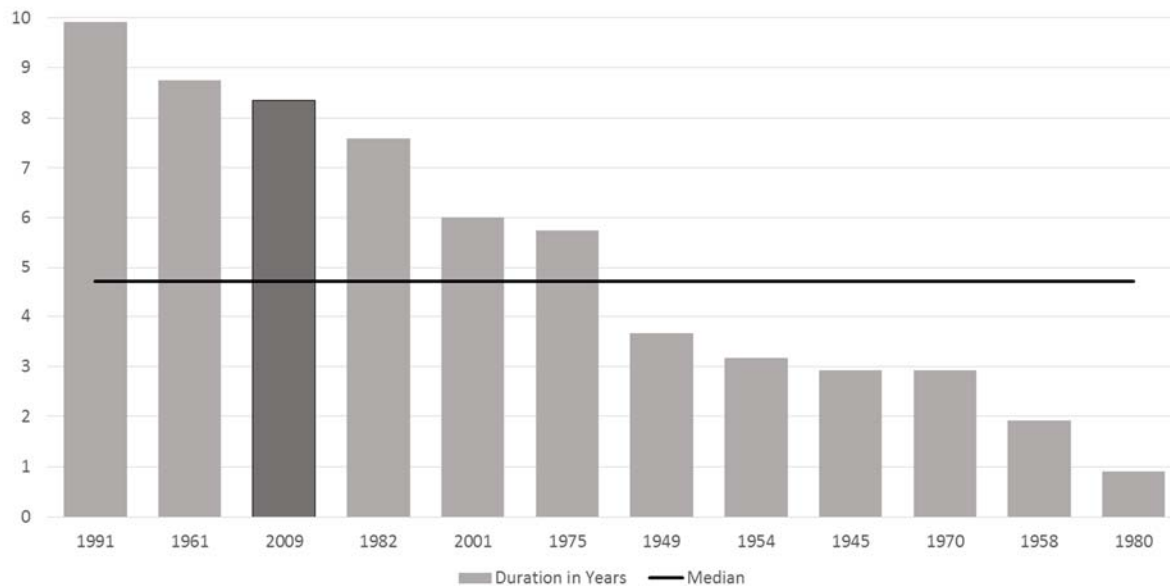
This section includes other smaller departmental changes including the expiration of limited-term project costs and several other small changes.

Planning Scenario: Economic Recession

Due to the difficulty of predicting recessions, the base case of this report does not anticipate an economic contraction in any of the next four years. However, it would be an historical anomaly if the City did not experience an economic downturn over the next four years.

As Figure A-4 shows, since 1945, the median duration of an expansion in the United States has slightly under 5 years. The current economic expansion has lasted over 8 years. If there is indeed no recession through FY 2021-22, as the projection assumes, it will mark the longest economic expansion since 1945.

Figure A-4. Number of Years of Economic Expansion in the U.S. from Start Year (1945 to Present)



Based on the historical length of economic expansions as discussed above, it is likely that a significant economic slowdown or recession will occur prior to FY 2021-22.

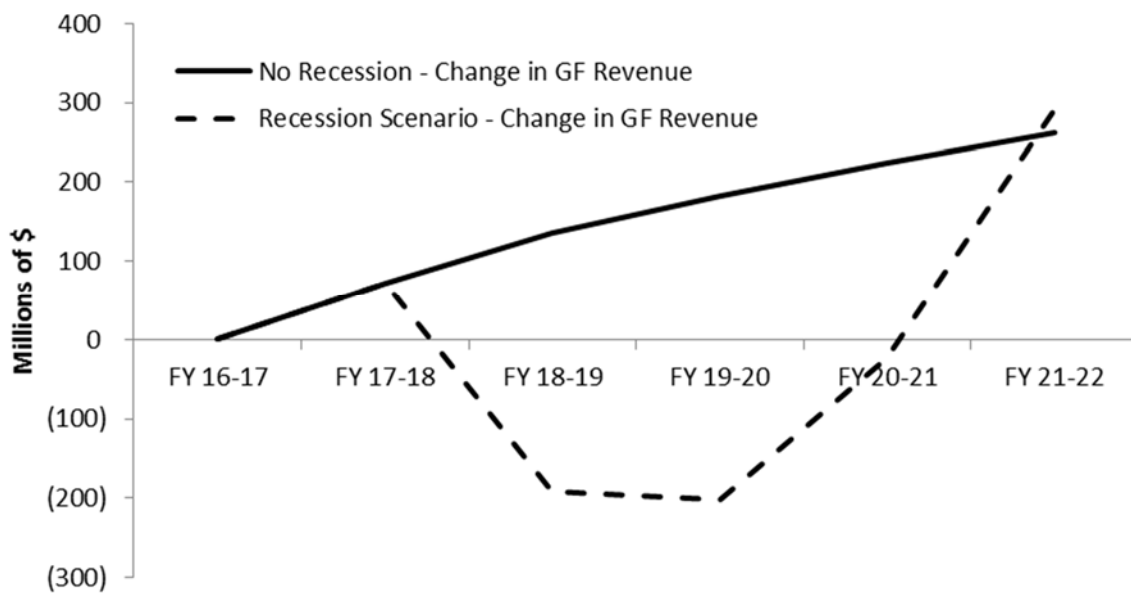
The biggest impact on the City's budget deficits in a time of recession come from reduced revenue and increased employer contribution rates for employee retirement benefits. The City's revenues are affected by the overall business cycle; the international, national, and regional economies; state and federal budget decisions; consumer confidence and spending; employment rates; and travel and tourism. Historically, projection variances follow the economic cycle, and revenues tend to outperform expectations in times of expansion and underperform in times of recession. Actual revenues exceeded budgeted revenues by over 6% in FY 2005-06 and FY 2010-11, both years of rapid revenue growth, but were more than 4% below budgeted revenues in FY 2002-03 and FY 2008-09, years of sharp economic contraction.

To illustrate the effect of a hypothetical recession on San Francisco's fiscal condition, this section describes a recession scenario that assumes weakness in the California and San Francisco economies beginning in FY 2019-20.

Economic Assumptions Included in the Recession Scenario

Recession Scenario – Impacts on Revenue Projections: This scenario assumes rates of revenue loss in major local tax sources consistent with the average declines experienced during the last two economic downturns - from FY 2001-02 through FY 2003-04 (the dot-com/September 11th recession) and FY 2008-09 through FY 2010-11 (the 2008 global financial crisis). Reductions in the City’s projected aggregate discretionary revenue would result in reduced contributions to baselines and set-asides affecting the MTA, DCYF, the Library, Recreation and Parks, and the School District, and would also result in lower required deposits to the General Reserve, which are also assumed. Using these parameters, the net revenue loss from a recession beginning in FY 2019-20 would be approximately \$822.4 million over the remaining three years of the forecast period compared to the base case described in this plan. Figure A-5 shows the difference between base case and recession scenario revenue projections.

**Figure A-5. Comparison of Revenue in Base Case and Recession Scenarios
Cumulative Change in Selected Local Taxes**



Recession Scenario – Reserve Withdrawals: The City’s reserve policies are designed to help absorb the impact of the revenue losses described above. The recession scenario assumes the maximum allowable use of the Budget Stabilization, Rainy Day, and General Reserves, or \$161 million in FY 2019-20, \$134 million in FY 2020-21, and \$105 million in FY 2021-22.

Recession Scenario – Impacts on Pension Contributions: An economic recession will also likely result in a significant increase in the employer contribution rates. The recession scenario therefore assumes a shock to the Retirement System’s (SFERS) assets during FY 2019-20 equivalent to the loss experienced during the 2008 global financial crisis and aftermath, which would affect contribution rates in FY 2021-22 as the valuation at July 1, 2020 determines the contribution rates for the fiscal year beginning July 1, 2021. The FY 2019-20 asset losses are then smoothed into the July 1, 2020 actuarial value of assets and employer contribution rates would increase over a five-year period beginning in FY 2021-22. In this scenario, employer contribution rates would rise by 3.6% in FY 2021-22 and by 7.5% in FY 2022-23. This estimate is intended to demonstrate sensitivity to a large negative return and should not be relied upon for any other purpose.

This plan projects that if an economic downturn similar to the two most recent recessions were to begin in FY 2018-19, it would increase the City's projected deficits by \$71 million, \$200 million, and \$198 million in FY 2019-20, FY 2020-21, and FY 2021-22 respectively.

San Francisco's Charter requires that each year's budget be balanced. The recession scenario detailed in this plan was modeled after the City's financial experience during the last two recessions; future economic slowdowns or reductions from the federal government could be less or more severe. As noted earlier in this report, significant risk from the federal budget and other policy changes at the federal level remain. In all cases, continuing to improve reserve balances and investment in critical one-time capital, equipment, and IT needs during periods of growth will help the City better weather the next economic downturn.

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