Budget Outlook & Department Instructions

December 2023
Overview

- Rate of expenditure growth far outpaces City’s General Fund revenues – creating $245 million deficit in FY 2023-24, $554 million in FY 2025-26 and worsening deficits in coming years.

- Mid-year budget reductions incorporated into the forecast – departments must include in February budget submissions.

- Additional reductions of 10% in each year required to balance FY 24-25 & FY 25-26, plus 5% contingency proposals.
Fiscal Outlook & Five Year Financial Plan Update
Fiscal Outlook – Deficit Grows to $1.3 billion

From current fiscal year, projected expenditures grow by over $1.3 billion (18%), while revenues only grow by $170 million (2-3%).

$245M deficit (FY 2024-25)

$554M deficit (FY 2025-26)

$945M deficit (FY 2026-27)

$1.35B deficit (FY 2027-28)
What Changed Since July?

• **Further reduced revenue** expectations, particularly in transfer, hotel & sales taxes.

• Increased **health care costs**: 9% projected health rate growth in FY 24-25.

• Multi-year **inflationary growth on CBO grants** (new ordinance).

• **Use of fund balance** spread over three-year period.
Fiscal Outlook – Major Assumptions in Forecast

• **Decline or nominal growth in major tax revenues:** ongoing reductions to property tax as office market resets, slower hospitality sector rebound, transfer taxes at 2011 levels, tepid business tax growth.

• **Salary & Benefits:** CPI growth on open contracts on same schedule as Police & Fire in next two years; 7.2% rate of return on pension investments.

• **Citywide & Departmental Costs:** CPI growth on non-personnel costs, IHSS wage agreements, full funding of Ten Year Capital & ICT Plans by FY 25-26, and other updates.
## Five Year Report Update – Summary

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<tr>
<td><strong>SOURCES Increase / (Decrease)</strong></td>
<td>(9.6)</td>
<td>181.0</td>
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<td><strong>Uses</strong></td>
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<td>Baselines &amp; Reserves</td>
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<td><strong>Two-Year Deficit</strong></td>
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Revenue Assumptions & Trends

- **High office vacancies** negatively impact property, business, and transfer taxes.

- **Business taxes** seeing significant rates of dispute & litigation, requiring City to reserve collections for litigation risks.

- **Hospitality industry expected to recover** after plan period, slower than previously forecasted. The City experienced rapid “bounce back” after the pandemic, but now plateauing.

- **Local & state sales tax growth** slower than previously forecasted.

- **One-time sources** including FEMA & fund balance budgeted through FY 26-27.
Key Revenue Sources Down by 20%

Change in GF Revenues FY 18-19 to FY 22-23 Year-End (actuals)

- Business Tax
- Sales Tax
- Hotel Tax
- Parking Tax
- Real Property Transfer Tax

FY 18-19: $1,974
FY 22-23: $1,570

-20%
Office Vacancy Rates Still Climbing

Seasonally Adjusted Office Vacancy Rates
2005 - 2023

Weekly office attendance at around 50% of pre-pandemic levels

30.4% in Q3 of 2023
Transfer Tax Revenue at Great Recession-Era Low

Real Property Transfer Tax Revenues
2000 – 2028 (projected)

- Less than $25M
- $25M or More

FY 22-23 ended at lowest levels since 2011
Hospitality Rebound Stalling

Revenue per Available Room – 12 month rolling average 2019 – 2028 (projected)

Projected

Convention activity helps drive up hotel taxes, but still at only 60% of total attendees compared to FY 2018-19.
Local & State Sales Tax Slowing

Percent Change in Sales Tax from Prior Year
2020 - 2023

San Francisco
California

10% 20% 30% 40% 50%

0% -10% -20% -30% -40% -50%

2020 Q1 2020 Q2 2020 Q3 2020 Q4 2021 Q1 2021 Q2 2021 Q3 2021 Q4 2022 Q1 2022 Q2 2022 Q3 2022 Q4 2023 Q1 2023 Q2

Percent Change from Same Quarter Prior Year

Mayor’s Office of Public Policy and Finance
City and County of San Francisco

13
Depletion of One-Time Sources

Projection assumes $350M in FEMA reimbursements over next three years, but City continues to see delays & changes in guidelines.
Key Expenditures

• **Salaries and benefits**: Increase by nearly $500 million over plan period.

• **Required baselines**: Grow by around $200 million & include newest Student Success Fund, which grows to $35 million in FY 2024-25 and $60 million by FY 2027-28.

• **Citywide operating costs**: Real estate, capital, debt payments, PUC rates, and implementation of multiyear inflation on all GF nonprofit grants.

• **Other major costs**: shelter costs due to expiring state grants, commitments to subsidizing housing for formerly homeless (LOSP), IHSS program growth.
Salary & Benefits – 30% Growth in 5 Years

Salary & Benefit Growth Since FY 18-19 (GFS Only)

FY 18-19: $3,239
FY 19-20: $3,466
FY 20-21: $3,481
FY 21-22: $3,678
FY 22-23: $4,026
FY 23-24: $4,091

Salary & Benefits Funding ($ millions)

Mayor’s Office of Public Policy and Finance
City and County of San Francisco
Health Care Cost Growth at 9-10%

Change in SFHSS Health Rates vs Benchmarks
2016 - 2023 (Calendar Year)
Fiscal Outlook – Risks & Uncertainties

• **Elevated interest rates** dampening business investments, real estate transactions, and borrowing costs.

• Level of **assessment appeals** and other tax refunds – current appeals volume has *tripled* from prior year.

• Significant **state budget shortfall** ($68 billion) and threat to ERAF, grants & funding for other programs.

• **Retirement** contribution rates - year-to-date returns trending negative, could trigger higher employer contributions.
Mayor’s Priorities & Department Budget Instructions
Mayor’s Priorities

• Improving public safety and street conditions

• Citywide economic vitality

• Reducing homelessness and transforming mental health service delivery

• Accountability & equity in services and spending
Budget Instructions to Departments

• Reduce General Fund support: 10% in FY 24-25 and 10% in FY 25-26.

• Submit contingency proposals of ongoing 5% in each year.

• Departmental budget reductions will help address only portions of total shortfall – the Mayor’s Office will convene departments to propose further citywide solutions and strategies.
Budget Instructions to Departments

- Implement mid-year cuts that are ongoing in FY 24-25 & FY 25-26.

- Do not add new FTE. Prioritize staffing key areas related to public safety and essential operations. Eliminate remaining vacancies for savings.

*Departments should only fill essential FTE in the current year and plan towards using additional vacancies for budget savings.*

- Focus on core department operations & services. Eliminate costs supporting non-essential, discretionary or redundant service areas.
Budget Instructions – Reminders

• Non-General Fund departments must balance their own budgets.

• MTA, PUC, Port & Airport will introduce fixed two-year budgets on May 1.

• Additional May 1 departments: Board of Appeals, Building Inspection, Child Support Services, Environment, Law Library, Library, Rent Board, Employee Retirement System.

• Budget transparency legislation requires 1-2 public meetings before February 14.
Calendar

December 13  Mayor’s Budget Outlook
Late December  Five Year Financial Plan Update (Joint Report)
January 19  Capital and COIT budget requests due
Early February  Controller’s 6-Month Report
February 21  Budget submissions due
March  March Update to the Joint Report
May  Controller’s 9-Month Report
      Governors May Revise
May 1  May 1 Department budgets introduced
June 1  Mayor proposes a balanced budget to the Board of Supervisors
June  Budget and Appropriations Committee hearings
Thank you