Agenda Date: 2/23/2021, **Item No.** 1

Five-Year General Fund Forecast

This report transmits the preliminary status for the General Fund (GF) fiscal year (FY) 2021-22 budget and a five-year GF forecast through FY 2025-26 (**Attachments A and B**). The five-year forecast is being presented to the Mayor and City Council for the 11th consecutive year and provides an essential tool in long-term budget discussions and decision making.

THIS ITEM IS FOR INFORMATION AND DISCUSSION.

Summary
The COVID-19 global pandemic has created significant challenges for residents, employees, City operations and has adversely impacted revenue streams, primarily in the hospitality and leisure sales tax categories. Fortunately, under the leadership of the City Council the GF has remained balanced and is projected to end FY 2021-22 with a surplus of $153 million of which nearly $100 million is one-time resources. The surplus is comprised of both one-time and ongoing resources. The one-time resources are due to the Council approved transfer of funding from the Coronavirus Relief Fund (CRF) to the General Fund to offset public safety salaries as permitted by the Federal guidelines. This action was specifically taken to preserve GF programs facing potential reduction due to revenue declines in the first three months of the pandemic (March-May). On December 8, in anticipation of the pending CRF deadline of December 30, Council again approved using the CRF public safety salary offset. This time the offset was used to free up GF resources to continue programs, originally funded from the CRF, that would have ended prematurely due to the pending CRF deadline.

Estimated one-time GF resources are $98 million and in order to maintain a structurally balanced budget, available ongoing resources are projected to be $55 million, for a combined surplus of $153 million. These resources could be used to provide new or expanded programs and services, employee compensation increases, one-time investments in city assets, infrastructure or increasing the pension stabilization reserve fund. <u>It is critical we do not use one-time resources to fund ongoing costs</u>, especially considering we are still dealing with the pandemic. While we are confident with our current forecast, it is important to note staff is still finalizing expenditure estimates and we are waiting on holiday sales tax collections to finalize

our revenue projections. We will bring back final estimates and recommendations on responsible cost additions using the combination of one-time and ongoing projected resources in March with the City Manager's Trial Budget.

Over the last few years the City Council has taken necessary actions to protect City services while facing very challenging financial conditions, and the current Coronavirus pandemic is no exception. The City Council has implemented important fiscal measures, including:

- Strategic use of CARES Act and Coronavirus Relief Funds to preserve city programs and services during the COVID-19 pandemic.
- $134 million in innovation and efficiency savings to date, since 2010.
- Net reduction in city employee count of approximately 2,700 positions since FY 2007-08, resulting in the smallest government per capita since 1970-71.
- Consistently raising the contingency fund to its highest level in our history.
- Paying Public Safety Pension costs on an expedited 25-year amortization schedule, instead of a 30-year schedule.
- Creating a Pension Funding Policy and Pension Reserve Fund, which currently carries a balance of over $40 million that can only be used to offset increased future costs for Public Safety Pensions.

General Fund Status and Forecast

FY 2021-22 The forecast shows a structurally balanced budget, where ongoing revenues are available for existing programs. However, we are mindful of the pandemic and how it may continue to impact the City's budget. This uncertainty calls for a cautious approach to forecasting our future revenues to ensure we can sustain a balanced budget into the future. This report also includes stress testing of the forecast (**Attachments C through E**), which has been done for the third consecutive year, to model the potential for a recession in the last two years of the forecast. While this is not anticipated to occur, the alternative models provide an opportunity to evaluate how declines in revenue could compromise the GF's structurally balanced budget.

The preliminary expenditure estimates may change as cost estimates are further refined in the coming weeks; however at this time the preliminary FY 2021-22 GF expenditures to continue existing levels of service are projected to be $1.452 billion. This compares to the adopted GF expenditure budget of $1.426 billion for FY 2020-21, or an increase of $26 million. The increase accounts primarily for higher costs for public safety pension, increases in capital equipment, lower than anticipated vacancy savings, higher contingency to maintain a four percent reserve and increases for pay-as-you-go capital projects, many of which reflect deferred maintenance over the past decade.

For FY 2021-22, combined GF civilian (COPERS) and sworn (PSPRS) pension costs are expected to increase by approximately $3 million as compared to the FY 2020-21 budget. PSPRS pension costs account for approximately $8 million of the total increase, and was offset by lower COPERS pension costs of $5 million. The decrease in COPERS pension costs was due to lower projected payroll growth in FY 2021-22.

As the five-year forecast shows, pension costs, particularly PSPRS, will continue to add significant pressure to the GF budget going forward. Public Safety pension costs are expected to increase by approximately $85 million and COPERS is expected to increase by $8 million from the FY 2020-21 Budget through FY 2025-26 (**Attachment F**). COPERS reform measures adopted by the City Council and Phoenix voters are expected to result in significant savings over the next two decades. PSPRS costs are expected to continue to significantly increase due to the high unfunded liability. Later this spring, staff will bring forward PSPRS pension strategies to address this ongoing financial challenge.

Overall, non-pension operating expenditures (not including pay-as-you-go and vehicles) have been planned and manageable, increasing by only 2.0% or $20 million, and represents increases in personnel services costs, required contractual costs to provide existing programs and services and capital replacement needs of critical public safety equipment for the Fire Department.

FY 2021-22 and Beyond

This year's forecast illustrates the GF baseline (midpoint) forecast (**Attachment A**) for each year reflects a balanced budget. As we look ahead the areas of concern for the GF budget are service costs and capital needs for facilities, vehicles and information technology, service levels, and revenue. Service costs include employee compensation levels, contractual increases, commodity purchases, capital needs for technology hardware and software, infrastructure and vehicles, including Fire apparatus. Service levels involve the amount of services, hours and the number of facilities we keep open to serve the public. Revenues consider taxes, fees, economic growth, any trying to predict the potential continuing negative impacts from the COVID-19 pandemic, along with the impact that the 2020 Census may have on the City's relative population share. The current forecast assumes no changes to existing labor contracts or service levels. It does, however, assume any surplus is incorporated into the subsequent years' expenditures, whether in increased one-time and ongoing costs for added programs and services, labor increases, set-asides, or other uses of the funds. The current labor contracts expire at the end of this fiscal year (June 2021) and contract negotiations are currently underway. Any changes to these contracts will impact FY 2021-22 and beyond.

Next Steps and Community Input

The Phoenix City Charter requires a balanced budget each year. On March 16, a balanced City Manager’s Trial Budget will be presented for Council and Community discussion along with the Preliminary Five-Year Capital Improvement Program (CIP). The CIP budget will present options for debt service payments and one-time capital requests. This year we plan to continue the practice of seeking community input on the proposed budget with several opportunities for residents to provide feedback through virtual Community Budget Hearings to be held during the month of April. In addition, we will make available to all residents our new budget balancing tool, FundPHX, which will include the proposed City Manager's Trial Budget. Residents are also welcome to contact the Budget and Research Department directly to provide input or ask questions about the budget (contact information is available on our website Phoenix.gov/budget). Feedback received from residents will be provided to the Council regularly as we progress through the budget adoption process.

Responsible Department

This item is submitted by City Manager Ed Zuercher and the Budget and Research Department.

City of Phoenix

RESEARCH REPORT
BUDGET AND RESEARCH DEPARTMENT

B.R. REPORT NUMBER
2021-05

DATE ISSUED
February 17, 2021

TO:	FROM:
ED ZUERCHER CITY MANAGER	**AMBER WILLIAMSON** BUDGET AND RESEARCH DIRECTOR

SUBJECT
FIVE-YEAR FORECAST AND PRELIMINARY GENERAL FUND STATUS FOR FY 2021-22

BACKGROUND

Development and presentation of the five-year forecast is an important step in the City's budget process. Evaluating projected available resources and identifying potential ongoing budget surpluses or funding gaps will allow City Management and Council to develop strategic plans to ensure the continuation of city operations and optimize services to the community.

The Five-Year Forecast estimates future revenues and expenditures of the General Fund for the current fiscal year through fiscal year 2025-26. The purpose of this forecast is to identify key trends in revenues and expenditures and to provide information about the financial landscape anticipated over the next few years. The information contained in this forecast is based on data available through January 2021.

The General Fund five-year forecast (**Attachment A**) is provided to the City Council and the community for consideration and provides city policy-makers:

- A strategic financial management best practice
- A framework for strategic decision-making
- The opportunity to make policy changes to maximize city resources and service delivery
- A roadmap to continued fiscal health and award-winning budgetary and financial reporting

The forecast is not an official policy or legal budget document and does not enact any budgetary allocations. The forecast is also not intended to set or precisely predict future revenues or expenditures. Rather, the forecast presents current estimates based on several economic and financial assumptions of the future direction and ranges of growth rates for both resources and expenditures. The economic, revenue, and expenditures assumptions are provided in **Attachment B**.

The forecast is built on several assumptions outlined in **Attachment B** regarding:

- The national, state and local economy
- Possible continued negative impacts to City revenues from the COVID-19 pandemic

- Population and job growth
- Revenue growth
- Impacts of anticipated increasing pension liabilities
- Cost management practices
- Future year expenses

All of these factors are subject to change and are detailed further in this report.

Projecting future available resources and expenses over multiple years is complex and involves several assumptions concerning how revenue and expenditures will grow over time. In order to model potential future budgetary scenarios under varying economic conditions, a range is provided for resources and expenditures. The differences between the upper and lower ends of the ranges increase in the later years of the forecast reflecting additional economic uncertainty. The top of each range represents the “optimistic” forecast, while the bottom of the range represents the “pessimistic” forecast. All of the ranges are based upon the assumptions described in this report.

It is important to note, if any of these assumptions as described were to change or modeled differently, the ranges of amounts presented in the forecast would need to be revised. Unexpected economic shocks, recessions, legislative mandates or other risks to the forecast can also adversely affect projections.

Additionally, even slight variances in the revenue and expenditure growth rates in the initial years of the forecast result in substantial changes to the later years due to the compounding effect of the changes. For example, a revenue growth variance of only 1% in FY 2021-22 can result in a $13.2 million change to the ending balance, which would impact the ending fund balances in the subsequent forecast years. Long term forecasts become less reliable the further they are from development because of the many underlying assumptions subject to frequent fluctuations.

Projections are formulated in the first six months of the fiscal year and are based on current estimates of where staff believes resources and expenditures will be for the current fiscal year and the subsequent five years. In order to create the most reliable revenue and expenditure projections, staff relies on several economic sources, months of actual collections and extensive technical reviews before recommending estimates to City management and ultimately the City Council for final consideration.

The COVID-19 pandemic inflicted an unprecedented recession and caused severe economic disruptions. Thanks to federal assistance from the CARES Act and more than expected revenue collections from retail and contracting sales taxes, the City did not need to significantly cut the budget. The FY 2021-22 ending General Fund balance is estimated to be $153M (**Attachment A**), with approximately $98M representing one-time resources mostly attributable to the Council approved transfer from the Coronavirus Relief Fund to offset public safety salaries as permitted by the Federal guidelines. The remaining $55M represents ongoing resources which could be used to add or expand city programs and services and provide for increased employee compensation. This report also includes stress testing of the GF forecast which is an essential fiscal tool to evaluate how revenues might respond to different levels of economic challenges. To better prepare for future challenges, “Stress testing” scenarios for moderate and severe recessions are included in this report (**Attachment C, D and E**).

OTHER INFORMATION

It is important to note that the preliminary FY 2021-22 budget is based on existing state-shared revenue models and statutory obligations. Any changes to state-shared revenue formulas or other revenue sources proposed in the Governor's budget or in legislative bills that would impact the GF budget are not reflected and would need to be addressed, if adopted by the State.

Preliminary Status of 2021-22 General Fund Budget

2021-22 Resources- The chart below shows the preliminary resources projection:

GF Resource Category	2021-22 Preliminary Estimate (in millions)	2021-22 Preliminary Projected Annual Growth Rate %
Local Sales & Excise Taxes	$550	4.2%
State-Shared Revenue [1]	$496	-1.8%
Primary Property Tax [2]	$190	5.7%
User Fees and Other	$117	8.3%
Beginning Balance [3]	$237	N/A
Transfers/Recoveries [3]	$ 15	N/A
Total GF Resources	**$ 1,605**	**-1.4%**

[1] This does not reflect any impact to State-Shared Revenue resulting from the FY 2021-22 State budget, nor legislative changes that have recently been proposed or discussed during the current legislative session.

[2] Assumes the continuation of City Council's adopted policy to maximize the primary levy in order to preserve GF services. Any deviation from this policy would require an ongoing reduction to GF programs.

[3] Estimates for beginning balance and transfers/recoveries are not derived from annual growth rate projections or broader economic factors.

Revenue Forecasting Model - In the fall of 2014, Budget and Research consulted with the University of Arizona's Eller College of Management, Economic and Business Research Center (EBRC) to enhance the City's sales tax revenue forecasting process. Dr. George Hammond, EBRC Director, and Dr. Alberta Charney, Senior Research Economist, spent several months working with City staff to develop an enhanced econometric sales tax forecasting model for all categories of City and State sales tax. In the Summer of 2017, staff worked with EBRC to update the tax forecasting model. The EBRC is updating the City's model again by including online sales tax. The City began collecting sales tax from online marketplace retailers effective October 2019 just prior to the pandemic, which has helped to offset losses experienced in the leisure and hospitality sales tax categories. The EBRC leads the State of Arizona Forecasting Project, which provides in-depth economic forecast analysis and databases on a subscription basis to businesses, organizations, and government via membership. The additional consulting with Drs. Hammond and Charney has provided the City with solid, independent economic and statistical expertise used to develop a statistically valid forecasting model specifically for the City of Phoenix. The projected growth rates in each category of sales tax for the FY 2021-22 estimate and the out years of the forecast are based on projections developed with the enhanced econometric forecasting model.

2021-22 Expenditures - The preliminary expenditure estimates may change as cost estimates are further refined in the coming weeks. At this time, the preliminary FY 2021-22 General Fund expenditures are projected to be $1.452 billion. This compares to the adopted GF expenditure budget of $1.426 billion for FY 2020-21, or an increase of $26 million. The increase accounts primarily for higher costs for public safety pension, increases in capital equipment, lower than anticipated vacancy savings, higher contingency to maintain a four percent reserve and increases for pay-as-you-go capital projects.

Pension Costs - Expected changes in COPERS and PSPRS pension costs are as follows:

- COPERS: GF pension costs for COPERS are expected to decrease by about $5 million as compared to the current year budget. The overall trend in COPERS pension cost has been driven by recent actuarial changes, plan earnings, payroll growth and pension reform. As the five-year forecast shows, COPERS pension costs are estimated to increase $8 million from the FY 2020-21 Budget through FY 2025-26 (**Attachment F**).

- PSPRS: The GF costs for sworn Police and Fire are expected to increase by about $8 million compared to the current year budget. The primary factors contributing to the growth over the current year budget are recent actuarial changes, plan earnings, and changes to the payroll base. Pension costs have also been impacted by repealed pension reform measures. As the five-year forecast shows, public safety pension costs are estimated to increase $85M from the FY 2020-21 Budget through FY 2025-26 (**Attachment F**), which adds significant pressure to the GF budget going forward and limits the City's ability to expand program and services to residents.

Contingency – The contingency fund is assumed to increase from $56 million to $57 million in FY 2021-22 and increases over the forecast period to reflect 4.0% of total General Fund operating expenditures per year from FY 2021-22 to FY 2025-26.

Detailed preliminary estimates with multiple year-to-year comparisons are included in the Zero-Based Budget Inventory of Programs document, which is available online at phoenix.gov/budget. Revenue and expense estimates continue to be developed, and more definitive estimates will be presented along with the City Manager's Trial Budget on March 16.

The General Fund preliminary 2021-22 budget status and Five-Year Forecast are provided for information and discussion.

ATTACHMENTS

Attachment A- Five-Year General Fund Forecast

Attachment B- Forecast Assumptions

Attachment C- Background, Methodology and Assumptions for Stress Testing

Attachment D- Stress Testing for Moderate Recession Scenario

Attachment E- Stress Testing for Severe Recession Scenario

Attachment F- Pension Cost Increases

ATTACHMENT A
5-Year General Fund Forecast ($Millions)

	2020-21 Adopted Budget	2021-22 Preliminary Budget Estimate	2022-23 Forecast	For Planning Purposes Only 2023-24 Forecast	2024-25 Forecast	2025-26 Forecast
Resources						
Local Taxes	$507	$550	$576 - $584	$599 - $617	$624 - $653	$651 - $691
State Shared Revenues	487	496	565 - 573	564 - 581	587 - 614	613 - 651
Primary Property Tax	180	190	198 - 201	204 - 211	210 - 220	217 - 231
User Fees and Other	136	117	118 - 120	120 - 123	121 - 126	123 - 131
Other (Carryover Balance, Transfers, Recoveries)	58	196	31	28	30	32
Unused Contingency from Prior Year	58	56	57	61	63	65
Total Resources	**$1,426**	**$1,605**	**$1,545 - $1,566**	**$1,576 - $1,621**	**$1,635 - $1,706**	**$1,701 - $1,801**
Expenditures						
Operating Expenditures	$1,004	$1,024	$1,102 - $1,097	$1,117 - $1,110	$1,147 - $1,139	$1,191 - $1,182
Civilian Pension	92	87	92	95	98	100
Sworn Public Safety Pension	236	244	268	290	310	321
Contingency	56	57	61	63	65	68
Pay-As-You-Go Capital (Includes Technology Plan)	20	25	20	20	20	20
Minimum Vehicles	18	15	15	15	20	20
Total Expenditures	**$1,426**	**$1,452**	**$1,558 - $1,553**	**$1,600 - $1,593**	**$1,660 - $1,652**	**$1,720 - $1,711**
PROJECTED (DEFICIT)/SURPLUS:	**$ -**	**$153**	**$(13) - $13**	**$(24) - $28**	**$(25) - $54**	**$(19) - $90**

Key Resource Forecast Assumptions:

* The forecast assumes modest revenue growth with no recession, no fee increases or decreases and no new revenue sources.

* No changes to current revenue base as provided in state and city laws or to state shared revenue formulas.

* Relative population share used in calculating state shared revenues in 2021-22 was based on the 2019 Census Bureau Population Estimate. It was projected to remain flat throughout the forecast period. The actual share will change annually based on Census Bureau Population Estimates and the 2021-22 share will be impacted by the 2020 Decennial Census.

Other Forecast Notes:

* Ranges provided for revenues and operating expenditures. Upper & lower ends of ranges increase slightly in later years of forecast reflecting additional economic uncertainty in the later years.

* Ranges include pessimistic and optimistic scenario within assumptions provided by the primary sources of economic information mentioned in this report.

* When a baseline deficit or surplus is projected, the next year's operating expenses are assumed to be decreased or increased by the baseline deficit/surplus amount prior to applying the assumed annual projected growth rate, as the City is required by Charter to balance the budget each year.

Key Expenditure Forecast Assumptions:

* The contingency fund is set as four percent of total General Fund operating expenditures every year.

* Includes no additional future funding for program enhancements, unfunded mandates, expiring grants, etc.

* 2021-22 employee costs based on projections under the current Council-adopted pay plan ordinance and employee contracts. No assumptions have been made concerning future labor contract negotiations. Pension costs based on required and projected contribution rates provided by the respective pension system actuaries.

* Non-personnel related expenditures for 2022-23 and beyond assumes expenditure growth is in line with recent historical averages.

ATTACHMENT B

Forecast Assumptions

<u>Economic Sources</u> - Budget and Research staff relies on several different sources for economic data and forecasts to assist with developing revenue and expenditure projections.

The list below includes the primary sources of information:

- State of Arizona Finance Advisory Committee (FAC) which includes several economists and finance professionals from the private and public sectors
- State of Arizona Joint Legislative Budget Committee (JLBC)
- University of Arizona (UofA), Economic Business Research Center
- Global Insight, IHS
- Arizona State University (ASU) – WP Carey School of Business, and Western Blue Chip
- Arizona Department of Administration (ADOA) - Employment and Population Statistics Office
- JP Morgan Chase Economic Outlook Center
- Blue Chip Economic Indicators – National Level
- U.S. Bureau of Labor Statistics
- U.S. Census Bureau
- Phoenix Business Journal
- University of Arizona (UofA) Forecasting Project – A community-sponsored research program within the Economic and Business Research Center providing project members with economic forecasts for Arizona, the Phoenix-Mesa metro area, and the Tucson metro area. City staff attends the Forecasting Project quarterly meetings and receives quarterly reports and data/projections used to assist in developing our forecasts. Forecasting Project data relies on Global Insight, IHS which is a well-known economics organization that provides comprehensive economic and financial information. The data from this project is incorporated into an econometric software program used to forecast sales tax.

<u>Economic Outlook</u>

Ever since the first cases in late 2019, the COVID-19 virus has spread to over 200 countries and all across the United States. This pandemic has severely impacted the global economy and ended the longest U.S. economic expansion on record — nearly 11 years. Although recent vaccine approvals and distribution have raised hopes of a turnaround in the pandemic later this year, renewed waves, new variants of the virus, and distribution challenges pose concerns for the outlook.

Amid exceptional uncertainty, at the national level, the National Blue Chip of Economic Indicators predicts GDP growth of 4.2% in 2021 and could grow modestly at a 3.4% pace in 2022 (Blue Chip Economic Indicators, Vol. 46, No. 1 January 2021). Although the overall economy is expected to manage the growing trend in 2021, a variety of factors will determine the way forward. Key variables include, a) the spread of the virus itself, b) the deployment and effectiveness of COVID-19 vaccines, c) the size and timing of fiscal support, and d) the status of labor markets and household consumption (The Conference Board, February 2021).

Throughout the pandemic, Arizona has been able to recover quicker than many other states. As of December 2020, Arizona replaced 69.4% of the jobs lost between February to April (UofA Economic Business Research Center). Overall, Arizona’s economy remains steady in terms of personal income, employment and population.

The State's FAC indicated in October 2020 that Arizona ranks 3rd in economic momentum among the nation. The rankings for major economic factors are listed below:

	AZ Rate	AZ Rank
Change in Personal Income	11.6%	21
Change in Population	1.7%	3
Change in Employment	-3.4%	4

Other significant economic assumptions from trusted sources built into this forecast include the following:

- Personal income for the Phoenix Metro area is projected to grow 2.4% in 2021 due to the impact of COVID-19 and range from 5.6% to 6.1% from 2022 to 2026 (UofA Economic Research Center).
- Growth in population is expected to continue, but at lower rates than historical growth. Phoenix Metro population is projected to grow 1.9% in 2021 and range from 1.6% to 1.8% for the remaining forecast period.
- Non-farm employment in metro Phoenix is estimated to grow 4.0% in 2021 and range from 2.3% to 3.3% from 2022 to 2026 (UofA Economic Business Research Center).
- Arizona unemployment rate is estimated to fall to 6.3% in 2021, and range from 3.6% to 5.2% for the remaining forecast horizon (UofA Economic Business Research Center).
- The near-term outlook for real estate in Greater Phoenix remains optimistic. Single-family residential permits are projected to increase by 15% in 2021, although multi-family permits are expected to be lower in 2021 than in 2020 (ASU W.P. Carey School of Business- Greater Phoenix Blue Chip Forecast/ Economic Forecasting Luncheon, December 2020).
- Inflation is expected to increase during the forecast period with the Consumer Price Index-All Urban Consumers (CPI-U) rising by 2.6% in FY 2021-22. (UofA Economic Research Center). In the past 50 years, CPI-U has ranged from negative 0.4% in 2009, to a high of 13.5% in 1980 (U.S. Department of Labor Bureau of Labor Statistics).

Resource Assumptions- Revenue growth rates are determined using information from our above-mentioned trusted sources, analyzing actual revenue trends and averages, and factoring in any known policy or legislative changes.

Revenue assumptions beyond the broader economic considerations are described below:

- No further period of recession with modest revenue growth for the forecast horizon.
- Annual revenue growth rates range from 2.5% to 8.4% during the forecast period.
- No impact to current revenue tax base, as provided in applicable state statutes and City ordinances.
- No future impact to state shared revenue formulas or legislation or action that could impact city revenue sources.
- Phoenix's relative population share, which impacts state shared revenue collections, was projected to remain flat throughout the forecast period. The actual share will change annually based on Census Bureau Population Estimates and the 2021-22 share will be impacted by the 2020 Decennial Census.

- No future fee increases or decreases and no new sources of revenue.
- Potential increases to revenue resulting from economic development efforts are not included in the forecast.
- Ranges provided for revenues: upper and lower ends of ranges increase slightly in later years of the forecast reflecting additional economic uncertainty.

Expenditure Assumptions- Assumptions regarding forecasted expenditures are described below:

- Annual operating expenditure growth rates, except for pension, are based on the historical growth rates and the estimated average of CPIs throughout the forecast period.
- Pension costs are based on historical actuals and information provided by the COPERS and PSPRS actuaries. The forecast does not attempt to predict future pension liabilities, assets or other plan assumptions, but rather to account for the anticipated costs of both pension systems.
- The forecast does not include the impact of additional potential reform measures for COPERS or PSPRS or the impact of pending litigation or proposed legislation.
- The forecast includes no additional future funding for program enhancements, unfunded mandates, expiring grants, etc.
- Pay-as-you-go capital costs are based on the preliminary estimates in the five-year Capital Improvement Program.
- The forecast includes projected debt service for the mandated Regional Wireless Cooperative radio replacements, the replacements of the city phone and badging systems, and associated technology infrastructure.
- The contingency fund is set at four percent of total General Fund operating expenditures throughout the forecast period.
- The 2021-22 total compensation costs are based on projections under the current Council-adopted pay plan ordinance and existing employee contracts.
- No other financial impact from changes to labor unit contracts resulting from current and future negotiations is assumed.
- In forecast years with a projected baseline deficit or surplus, the next year's operating expenses are assumed to decrease or increase by the baseline deficit/surplus amount prior to applying the assumed annual growth projection, as the City is required by Charter to balance the budget each year.
- Ranges provided for operating expenditures: upper and lower ends of ranges increase slightly in later years of the forecast reflecting additional economic uncertainty.

Other Items that Could Impact the Base Budget or the Five-Year Forecast- The cost and revenue items below either will likely require additional funding or could adversely impact revenue, and therefore could have a negative impact on the five-year forecast as it's currently presented. The cost items may need to be ultimately borne, in part or in whole, by the General Fund if no other funding source is identified by the time these costs are imminent. Under the direction of the Mayor and City Council, staff has been exploring the potential for a bond program that could address critical systems and other city infrastructure. Staff plans to discuss a potential bond election timeline at a future City Council meeting.

- The forecast reflects the continued funding of approximately $13 million per year earmarked to address aging City infrastructure and critical equipment. Examples of these projects include replacing fire life safety systems in City facilities and water intrusion and electrical projects at police headquarters. Also, under the direction of the City Manager, staff continues to identify critical needs in all City facilities. Staff continues to work with several external firms that specialize in facility assessments. Staff has also taken active steps to enhance facility maintenance oversight by centralizing general fund facility maintenance funding and creating a facilities review committee. This change has significantly enhanced the prioritization of GF facility projects.

- General Fund vehicle funding has been estimated at $15 million from FY 2021-22 to 2023-24 and increases to $20 million in FY2024-25 and FY2025-26, with the majority of the funding earmarked for public safety, particularly Fire apparatus. While the forecast shows increased funding for vehicle replacements, the citywide need is much greater than the funding that is available. The Public Works Fleet Management Division estimates the General Fund backlog of vehicle replacements to be approximately $180M representing just over 2,200 units. In the Fire Department additional funding is needed to replace expensive apparatus equipment including pumpers, ambulances and ladders, which were originally purchased with voter approved General Obligation Bond funds. Of the 101 fire pumper trucks in the fleet, over 70% are either due now or will be due for replacement in the next five years. With limited funding available, a lease/purchase program was approved by Council to authorize the purchase of 15 fire pumpertrucks at a cost of $1.2 million per year starting in FY 2014-15, and these costs have been included in the forecast.

- The Governor’s proposed budget includes reducing individual income tax by a combined $1.2 billion over three years (FY 21-22 through FY23-24), which if enacted is estimated to reduce the City’s state shared income tax revenues by $52 million over the three-year period. Since state shared income tax revenue is based on actual collections from two years prior, if enacted the impact would not be realized until FY 23-24 through FY 25-26.

ATTACHMENT C

Stress Testing for General Fund

Background – According to the National Bureau of Economic Research, the longest economic expansion on record was ended by COVID-19 in February 2020. With federal stimulus packages and more than anticipated revenue collections, the City was not forced to cut the budget dramatically. However, each recession has its own feature, and it is hard to predict when it will come and how significant the impact will be. Stress testing helps estimate the potential financial shortfalls that could result from adverse events. To help the City plan ahead, avert or limit a fiscal emergency and keep long-term priorities on track, stress testing was done for the General Fund.

Methodology/Assumptions- "Stress test" in financial terminology, is an analysis or simulation designed to determine the ability of a given entity to deal with an economic crisis. Instead of doing a financial projection on a "best estimate" basis, a company or its regulators may do stress testing to estimate how robust an entity performs in certain negative circumstances, a form of scenario analysis. There are two scenarios for this stress testing: moderate and severe recession scenarios.

Attachment D shows a hypothetical moderate recession that is estimated to start in 2024-25. This scenario assumes that General Fund revenue, except state-shared income tax, will decline by 1% for two consecutive years. According to Moody’s Analytics, a recession typically affects budgets for at least two years. Although a moderate recession may impact revenue by more than 1%, the model is simulated with a 1% decrease. State-shared income tax distributed to cities and towns is based on the collections from 2 years prior, so the state-shared income tax decrease due to a moderate recession will not affect revenues until 2026-27.

Attachment E shows a hypothetical severe recession that is estimated to start in 2024-25. This scenario assumes that General Fund revenue, except state-shared income tax, will decline by 3% for two consecutive years. Although a severe recession may impact revenues by more than 3%, for simulation purposes, this stress test used a 3% decrease. Similar to the moderate scenario, the state-shared income tax decrease caused by the economic recession will not affect revenues until 2026-27.

Assumptions for recoveries, fund transfers and expenditures remain the same as the model shown in **Attachment A**. However, the expenditures for the forecast period will be different due to the methodology applied in the model. When a deficit or surplus is projected, the next year’s operating expenses are assumed to be decreased or increased by the deficit/surplus amount prior to applying the assumed annual projected growth rate, as the City is required by Charter to balance the budget each year.

ATTACHMENT D

5-Year General Fund Forecast – Moderate Recession Scenario ($Millions)

	2020-21 Adopted Budget	2021-22 Preliminary Budget Estimate	For Planning Purposes Only 2022-23 Forecast	2023-24 Forecast	2024-25 Forecast	2025-26 Forecast
Resources						
Local Taxes	$507	$550	$576 - $584	$596 - $614	$585 - $613	$575 - $612
State Shared Revenues	487	496	565 - 573	563 - 580	568 - 594	574 - 610
Primary Property Tax	180	190	198 - 201	204 - 211	200 - 210	197 - 210
User Fees and Other	136	117	118 - 120	120 - 123	117 - 122	115 - 123
Other (Carryover Balance, Transfers, Recoveries)	58	196	31	28	30	32
Unused Contingency from Prior Year	58	56	57	61	63	65
Total Resources	**$1,426**	**$1,605**	**$1,545 - $1,566**	**$1,572 - $1,617**	**$1,563 - $1,632**	**$1,558 - $1,652**
Expenditures						
Operating Expenditures	$1,004	$1,024	$1,102 - $1,097	$1,117 - $1,110	$1,143 - $1,136	$1,115 - $1,106
Civilian Pension	92	87	92	95	98	100
Sworn Public Safety Pension	236	244	268	290	310	321
Contingency	56	57	61	63	65	65
Pay-As-You-Go Capital (Includes Technology Plan)	20	25	20	20	20	20
Minimum Vehicles	18	15	15	15	20	20
Total Expenditures	**$1,426**	**$1,452**	**$1,558 - $1,553**	**$1,600 - $1,593**	**$1,656 - $1,649**	**$1,641 - $1,632**
PROJECTED (DEFICIT)/SURPLUS:	**$ -**	**$153**	**$(13) - $13**	**$(28) - $24**	**$(93) - $(17)**	**$(83) - $20**

Key Resource Forecast Assumptions:

* The forecast assumes moderate recession in 2024-25 and 2025-26, no fee increases or decreases and no new revenue sources.

* No changes to current revenue base as provided in state and city laws or to state shared revenue formulas.

* Relative population share used in calculating state shared revenues in 2021-22 was based on the 2019 Census Bureau Population Estimate. It was projected to remain flat throughout the forecast period. The actual share will change annually based on Census Bureau Population Estimates and the 2021-22 share will be impacted by the 2020 Decennial Census.

Other Forecast Notes:

* Ranges provided for revenues and operating expenditures. Upper & lower ends of ranges increase slightly in later years of forecast reflecting additional economic uncertainty in the later years.

* Ranges include pessimistic and optimistic scenario within assumptions provided by the primary sources of economic information mentioned in this report.

* When a baseline deficit or surplus is projected, the next year's operating expenses are assumed to be decreased or increased by the baseline deficit/surplus amount prior to applying the assumed annual projected growth rate, as the City is required by Charter to balance the budget each year.

Key Expenditure Forecast Assumptions:

* The contingency fund is set as four percent of total General Fund operating expenditures every year.

* Includes no additional future funding for program enhancements, unfunded mandates, expiring grants, etc.

* 2021-22 employee costs based on projections under the current Council-adopted pay plan ordinance and employee contracts. No assumptions have been made concerning future labor contract negotiations. Pension costs based on required and projected contribution rates provided by the respective pension system actuaries.

* Non-personnel related expenditures for 2022-23 and beyond assumes expenditure growth is in line with recent historical averages.

ATTACHMENT E
5-Year General Fund Forecast – Severe Recession Scenario ($Millions)

	2020-21 Adopted Budget	2021-22 Preliminary Budget Estimate	2022-23 Forecast	For Planning Purposes Only2023-24 Forecast	2024-25 Forecast	2025-26 Forecast
Resources						
Local Taxes	$507	$550	$576 - $584	$595 - $613	$572 - $599	$551 - $587
State Shared Revenues	487	496	565 - 573	563 - 579	561 - 587	562 - 598
Primary Property Tax	180	190	198 - 201	204 - 211	196 - 206	189 - 201
User Fees and Other	136	117	118 - 120	120 - 123	115 - 120	111 - 118
Other (Carryover Balance, Transfers, Recoveries)	58	196	31	28	30	32
Unused Contingency from Prior Year	58	56	57	61	63	65
Total Resources	**$1,426**	**$1,605**	**$1,545 - $1,566**	**$1,571 - $1,615**	**$1,537 - $1,605**	**$1,510 - $1,601**
Expenditures						
Operating Expenditures	$1,004	$1,024	$1,102 - $1,097	$1,117 - $1,110	$1,142 - $1,134	$1,089 - $1,080
Civilian Pension	92	87	92	95	98	100
Sworn Public Safety Pension	236	244	268	290	310	321
Contingency	56	57	61	63	65	63
Pay-As-You-Go Capital (Includes Technology Plan)	20	25	20	20	20	20
Minimum Vehicles	18	15	15	15	20	20
Total Expenditures	**$1,426**	**$1,452**	**$1,558 - $1,553**	**$1,600 - $1,593**	**$1,655 - $1,647**	**$1,613 - $1,604**
PROJECTED (DEFICIT)/SURPLUS:	**$ -**	**$153**	**$(13) - $13**	**$(29) - $22**	**$(118) - $(42)**	**$(103) - $(3)**

Key Resource Forecast Assumptions:

* The forecast assumes severe recession from 2024-25 to 2025-26, no fee increases or decreases and no new revenue sources.

* No changes to current revenue base as provided in state and city laws or to state shared revenue formulas.

* Relative population share used in calculating state shared revenues in 2021-22 was based on the 2019 Census Bureau Population Estimate. It was projected to remain flat throughout the forecast period. The actual share will change annually based on Census Bureau Population Estimates and the 2021-22 share will be impacted by the 2020 Decennial Census.

Other Forecast Notes:

* Ranges provided for revenues and operating expenditures. Upper & lower ends of ranges increase slightly in later years of forecast reflecting additional economic uncertainty in the later years.

* Ranges include pessimistic and optimistic scenario within assumptions provided by the primary sources of economic information mentioned in this report.

* When a baseline deficit or surplus is projected, the next year's operating expenses are assumed to be decreased or increased by the baseline deficit/surplus amount prior to applying the assumed annual projected growth rate, as the City is required by Charter to balance the budget each year.

Key Expenditure Forecast Assumptions:

* The contingency fund is set as four percent of total General Fund operating expenditures every year.

* Includes no additional future funding for program enhancements, unfunded mandates, expiring grants, etc.

* 2021-22 employee costs based on projections under the current Council-adopted pay plan ordinance and employee contracts. No assumptions have been made concerning future labor contract negotiations. Pension costs based on required and projected contribution rates provided by the respective pension system actuaries.

* Non-personnel related expenditures for 2022-23 and beyond assumes expenditure growth is in line with recent historical averages.

ATTACHMENT F

The below chart illustrates the rise in General Fund (GF) costs for PSPRS and COPERS. The forecast for fiscal years 2021-22 through 2025-26 is based on information from plan actuaries and is based on the valuations dated June 30, 2020.