



Controller's Review

Mayor's Proposed Budget for FY 2024-25 and FY 2025-26



Office of the Controller
Budget and Analysis Division

June 12, 2024

Overview

Charter Section 9.102 requires the Controller to comment on the reasonableness of economic assumptions and revenue estimates in the Mayor's proposed budget.

We find the revenue to be reasonable but note that the budget relies heavily on one-time funds, and a structural gap near \$800m is likely to persist.

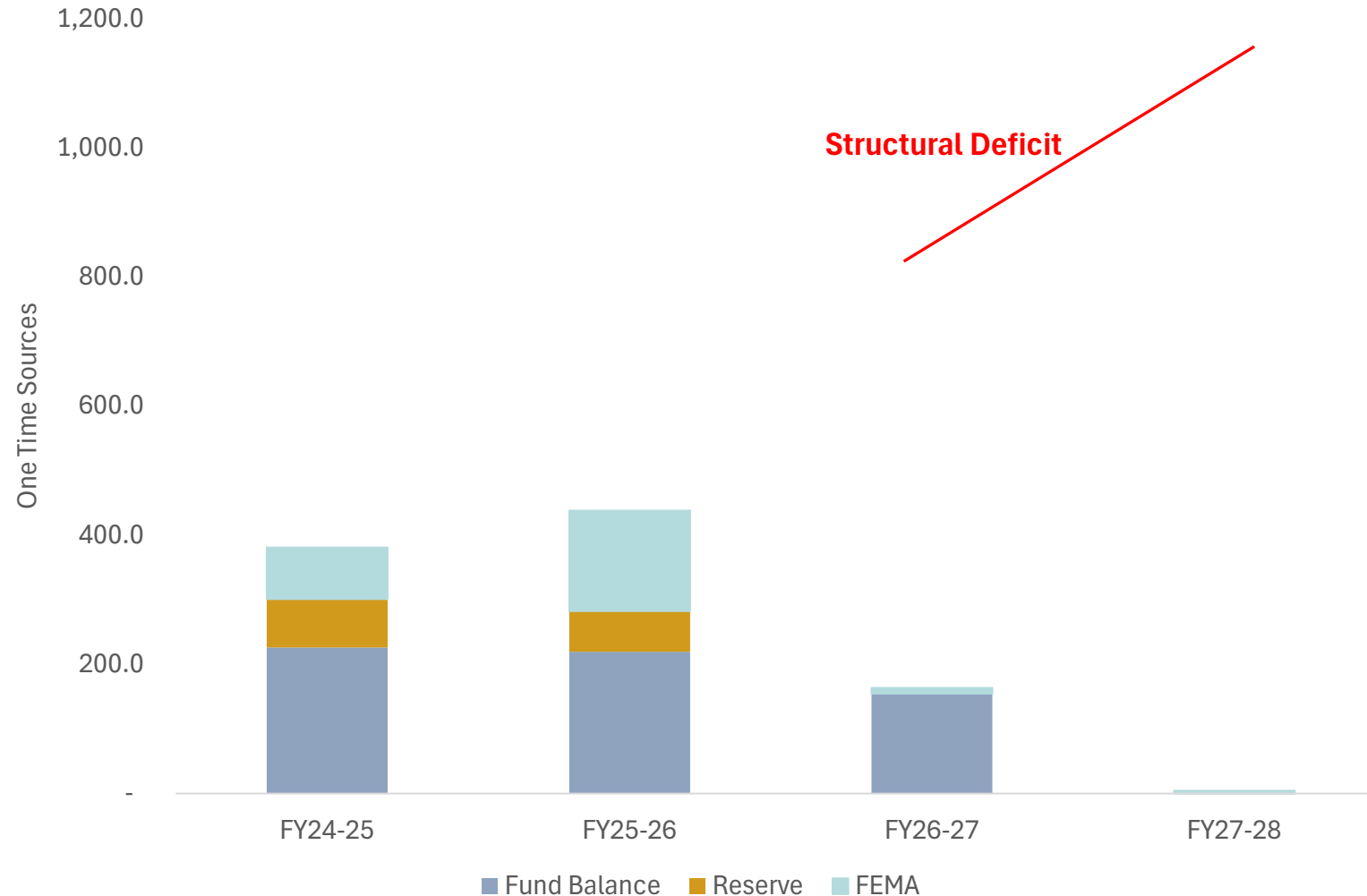
Key Findings

- **Tax revenue projections generally assume a continuing but slow economic recovery from the pandemic, with a significant drag created by the continuing effect of remote office work on economic activity in the City.** Most economically sensitive taxes, such as sales and hotel taxes, are projected to grow slowly during the coming two years, but in most cases remain below pre-pandemic levels.
- **The proposed budget assumes \$1 billion of General Fund-related one-time solutions over the two budget years, including:**
 - Drawdown of \$445.5 million in prior year fund balance, including \$106.1 million in prior year General Fund appropriations the Mayor's budget proposes to close. Accelerates use of fund balance, spending \$45.2 million previously held to address the FY 2026-27 shortfall.
 - \$235.7 million of FEMA reimbursement for previously incurred emergency response costs
 - \$138.3 million of reserve drawdowns
 - At least \$82.5 million of other one-time revenue in General Fund-supported funds.
 - At least \$137.6 million of short-term cost shifts in other funds, with a significant portion designed to achieve General Fund savings.

Key Findings

- **The proposed budget makes minimal progress towards closing projected structural budget gaps in years beyond the coming two-year budget period.** As one-time solutions are depleted, the structural budget gap will become larger, making future budgets more difficult to close. The March 2024 Joint report forecasted a structural budget gap of \$927 million in FY 2026-27, growing in subsequent years, absent ongoing corrective action by policy makers. Given our preliminary review of the mix of ongoing and one-time solutions proposed in the Mayor's budget, as well as known labor contract costs above the previously assumed levels in FY 2026-27, the shortfall likely remains more than \$800 million in FY 2026-27, growing in subsequent years.
- **The final adopted budget will require active monitoring and management by the Mayor and Board of Supervisors given a number of economic and financial risks.** These risks include the possibility of a slowing economic recovery or a recession, risks associated with both State and Federal revenue streams, and financial impacts of potential November 2024 ballot measures.

Heavy reliance on one-time solutions results in minimal progress toward structural deficit... with potential additional costs ahead.



Legislative Requirements and Proposals

- **The Mayor's proposed budget adheres to voter-adopted spending mandates, provided modifications to two requirements are adopted by the Board of Supervisors.** With the adoption of budget trailing legislation, voter-adopted spending requirements would be met, or exceeded, at a total cost of \$2.1 billion and \$2.2 billion in the two fiscal years. The March 2024 Update to the Five-Year Financial Plan forecasted a FY 2024-25 deficit of \$235.9 million, resulting in the suspension of required growth to the Early Care and Education and Street Tree Maintenance Fund baselines in FY 2024-25.
- **The proposed budget does not assume voter approval of potential measures on the November 2024 ballot.** Proposals with major fiscal impacts appear to include retirement plan changes for public safety employees, baseline funding for seniors and family housing, a new business tax on transportation network companies and autonomous vehicle businesses, and a local small business tax cut ordinance. Depending on which are placed on the ballot and approved by voters, these measures could significantly increase future deficits.
- **Minimum Compensation Rate.** The Mayor introduced legislation with the prior year's budget that would increase the minimum compensation rate in steps. For nonprofit organizations, the rate would be set at \$20.25 on July 1, 2024, \$21.55 on July 1, 2025, and \$23.00 on January 1, 2026. For public entities, the rate would be \$21.50 on July 1, 2024, \$22.00 on January 1, 2025, \$22.50 on July 1, 2025, and \$23.00 January 1, 2026. The Mayor's budget is sufficient to fund the impacts of the minimum compensation increases. These compensation increases, therefore, will be effective July 1, 2024.

Mayor's Proposed Budget

General Fund

	FY 2023-24 Budget	FY 2024-25 Proposed	FY 2025-26 Proposed
Fund Balance	\$ 122.7	\$ 225.9	\$ 219.6
Use of Reserves	101.5	75.2	62.8
Regular Revenues	6,396.4	6,350.0	6,617.6
Transfers In to the General Fund	211.3	206.9	203.9
Total GF Sources	\$ 6,832.0	\$ 6,857.9	\$ 7,103.9
<i>Change from Prior Year</i>		\$ 25.9	\$ 246.0
<i>Percentage Change</i>		0.4%	3.6%

All Funds

	FY 2023-24 Budget	FY 2024-25 Proposed	FY 2025-26 Proposed
Fund Balance	\$ 353.8	\$ 1,107.4	\$ 491.9
Use of Reserves	120.9	85.4	73.7
Regular Revenues	14,157.0	14,690.5	14,943.8
Total All-Funds Sources	\$ 14,631.7	\$ 15,883.3	\$ 15,509.4
<i>Change from Prior Year</i>		\$ 1,251.6	\$ (373.9)
<i>Percentage Change</i>		8.6%	-2.4%

General Fund Taxes (\$ millions)

Selected General Fund Taxes	Actual FY 2018-19	Actual FY 2019-20	Actual FY 2020-21	Actual FY 2021-22	Actual FY 2022-23	9M FY 2023-24	Proposed FY 2024-25	Proposed FY 2025-26
Total Property Tax	2,246.3	2,071.9	2,344.0	2,337.2	2,466.9	2,530.4	2,469.6	2,465.8
Business Tax	917.8	822.2	722.6	861.2	850.6	825.0	883.0	954.0
Hotel Tax	392.3	252.2	33.2	158.2	252.9	256.7	285.2	315.8
Sales Tax	213.6	180.2	146.9	188.3	197.9	189.0	193.7	198.9
Real Property Transfer Tax	364.0	334.5	344.7	520.3	186.2	157.4	218.9	267.6
Overpaid Executive Tax	-	-	-	-	206.0	125.0	140.0	140.0
Total	4,134.1	3,660.9	3,591.3	4,065.2	4,160.5	4,083.5	4,190.3	4,342.0
							Growth Since FY 2018-19	5.0%

General Fund Taxes

- **Property Tax**

- Roll growth of secured property assessments is assumed to be 3.0% in FY 2024-25 and 2.0% in FY 2025-26.
- \$110.2 million in FY 2024-25 and \$126.5 million in FY 2025-26 of property tax is assumed to be diverted from the General Fund for tax increment financing districts.
- Assume refunds of \$118.9 million in FY 2024-25 and \$136.1 million in FY 2025-26, to be paid when the Assessment Appeals Board determines reductions.

- **Business Tax**

- Underlying economic growth of 0% and 2% is assumed for tax years 2024 and 2025.
- Remote office work is assumed to continue indefinitely.
- Include impacts of 2020 Proposition F rate, which include increases for tax year 2024 and 2025 for large businesses in certain sectors and the expiration of temporary rate reductions for smaller businesses most affected by the pandemic in tax years 2025 and 2026.

Voter-Adopted Spending Requirements

- The budget supports over \$2.0 billion of baseline spending mandates. These mandates include spending for transit, libraries, schools, early childhood education, recreation and parks, among others.
- Legislation temporarily credits the Early Care and Education baseline (June 2018 Prop C) with interest of \$16.6 million in FY 2024-25 and \$16.9 million in FY 2025-26.
- Legislation temporarily allocates \$13.7 million of interest in FY 2024-25 of the Our City, Our Home fund (OCOH) across different expenditure categories.
- Several baselines are funded above the required levels, including Children's Services and Transitional Aged Youth baseline; Recreation and Parks baseline; Our City, Our Home Baseline and (November 2018 Prop C).
- Growth of two baselines suspended in FY 2024-25 due to size of deficit projected in March 2024: Early Care and Education baseline and the Street Tree Maintenance Fund.

Reserve Status

	FY 2023-24	FY 2024-25			FY 2025-26		
	Projected Balance	Deposit	Use	Projected Balance	Deposit	Use	Projected Balance
General Reserve	\$ 128.1	\$ 14.6	-	\$ 142.7	\$ 22.6	-	\$ 165.3
Rainy Day Economic Stabilization City Reserve	114.5	-	-	114.5	-	-	114.5
Budget Stabilization Reserve	275.2	-	-	275.2	-	-	275.2
Economic Stabilization Reserves	389.7	-	-	389.7	-	-	389.7
<i>Percent of General Fund Revenues</i>	6.2%			6.1%			5.9%
Budget Stabilization One Time Reserve	54.8	-	-	54.8	-	(54.8)	-
Rainy Day Economic Stabilization SFUSD Reserve	1.0	-	-	1.0	-	-	1.0
Federal and State Emergency Grant Disallowance Reserve	81.3	-	(38.2)	43.1	-	-	43.1
Fiscal Cliff Reserve	130.3	-	-	130.3	-	-	130.3
Business Tax Stabilization Reserve	29.5	-	(29.5)	-	-	-	-
Public Health Revenue Management Reserve	130.3	-	-	130.3	-	-	130.3
Free City College Reserve	7.5	8.0	(7.5)	8.0	-	(8.0)	-
Other Reserves	434.7	8.0	(75.3)	367.4	-	(62.8)	304.6
Litigation Reserve	-	11.0	(11.0)	-	11.0	(11.0)	-
Technical Adjustment Reserve	-	5.0	(5.0)	-	5.0	(5.0)	-
Salary and Benefits Reserve	-	20.5	(20.5)	-	21.5	(21.5)	-
Annual Operating Reserves	-	36.5	(36.5)	-	37.5	(37.5)	-
TOTAL, General Fund Reserves	952.5	53.6	(107.1)	899.0	62.7	(103.4)	858.3