Budget Outlook & Department Instructions

December 2023

Overview

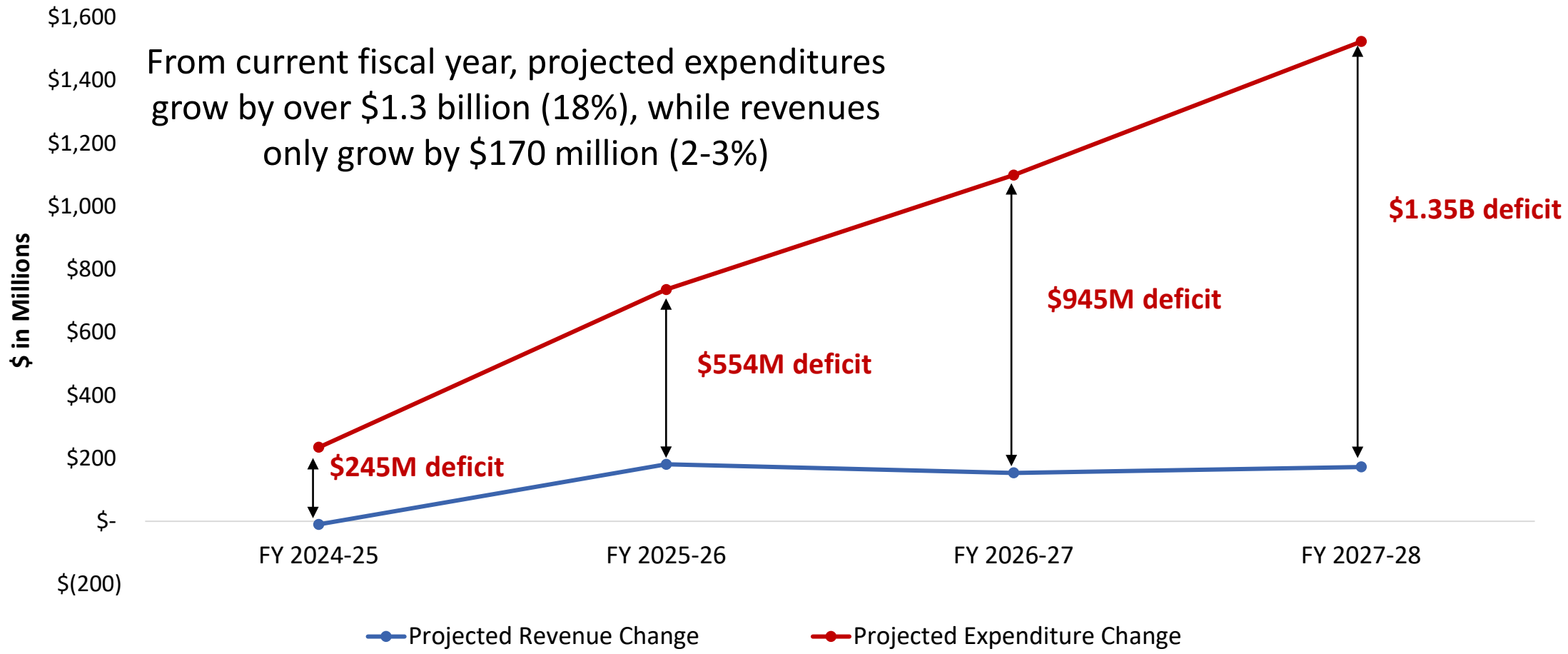
- Rate of expenditure growth far outpaces City's General Fund revenues – creating **$245 million** deficit in FY 2023-24, **$554 million** in FY 2025-26 and worsening deficits in coming years.

- **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



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.

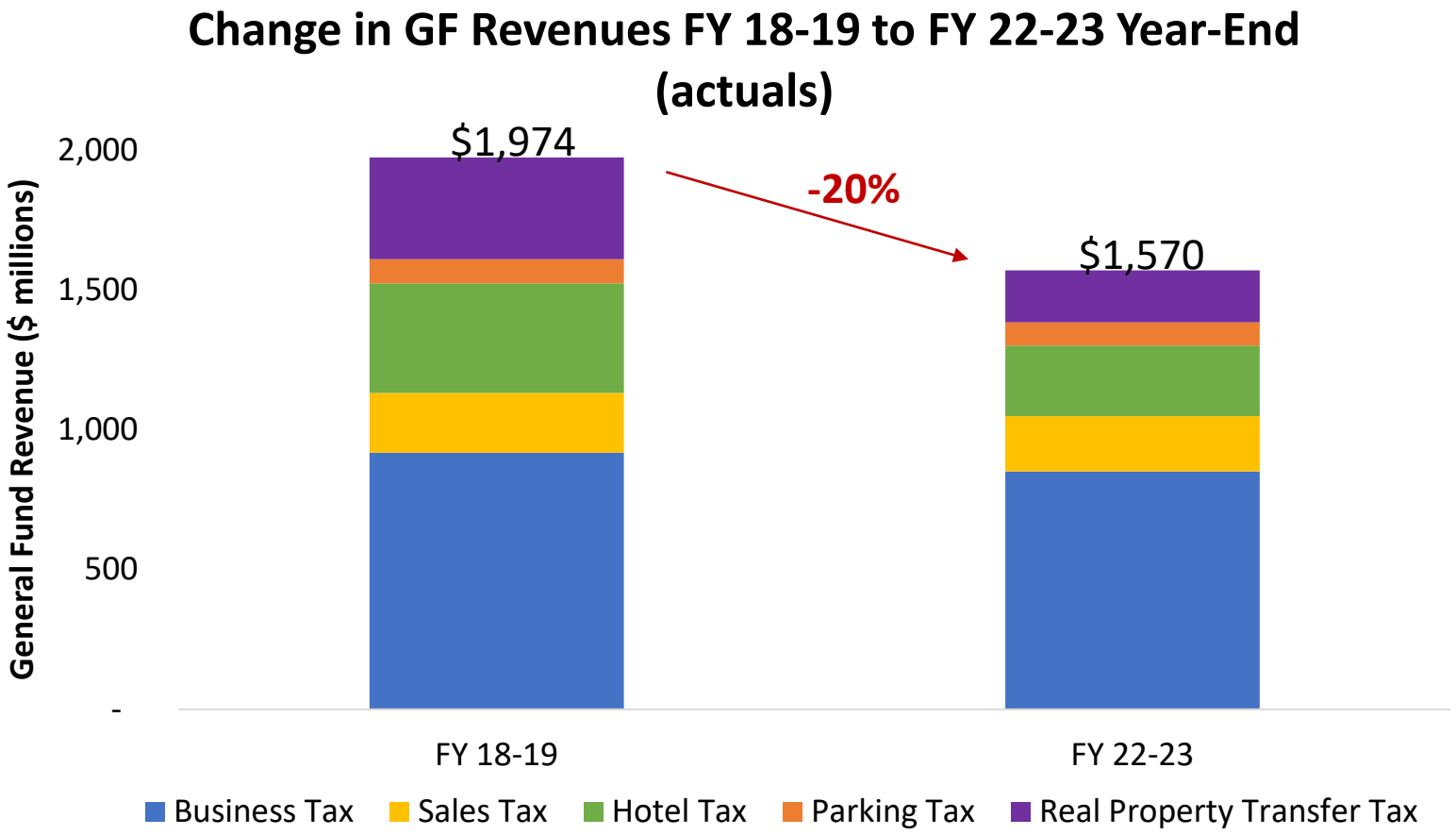
Five Year Report Update – Summary

	Projection 2024-25	Projection 2025-26	Projection 2026-27	Projection 2027-28
SOURCES Increase / (Decrease)	**(9.6)**	**181.0**	**153.9**	**172.8**
Uses				
Baselines & Reserves	(13.3)	(78.3)	(150.4)	(264.1)
Salaries & Benefits	(163.3)	(336.2)	(447.4)	(593.0)
Citywide Operating Budget Costs	(95.2)	(301.7)	(396.0)	(496.3)
Departmental Costs	36.8	(19.3)	(105.3)	(169.0)
USES Decrease / (Increase)	**(235.1)**	**(735.5)**	**(1,099.1)**	**(1,522.5)**
Projected Cumulative Projected Surplus / (Shortfall)	**(244.7)**	**(554.5)**	**(945.1)**	**(1,349.7)**
Two-Year Deficit	**(799.2)**			

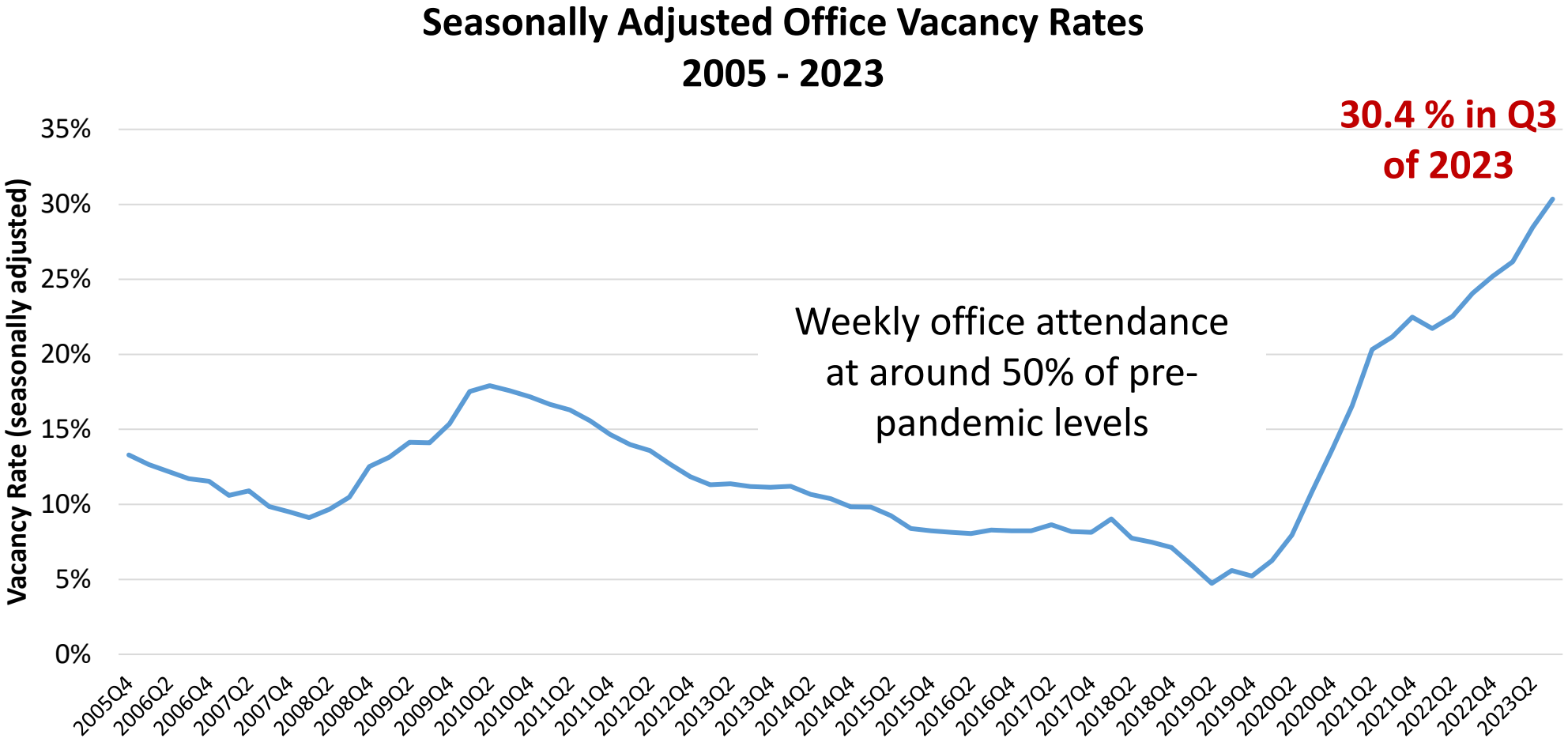
Revenue Assumptions & Trends

- **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.

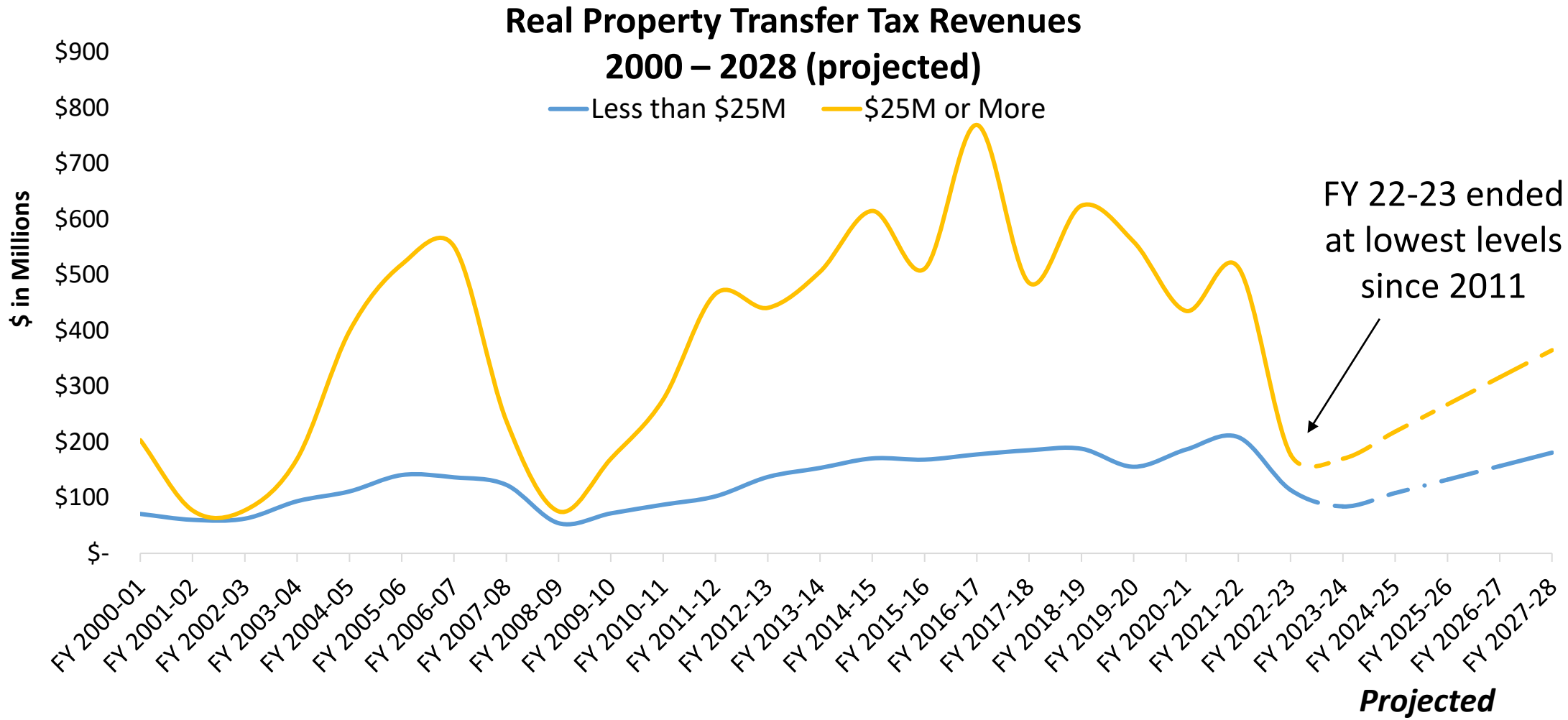
Key Revenue Sources Down by 20%



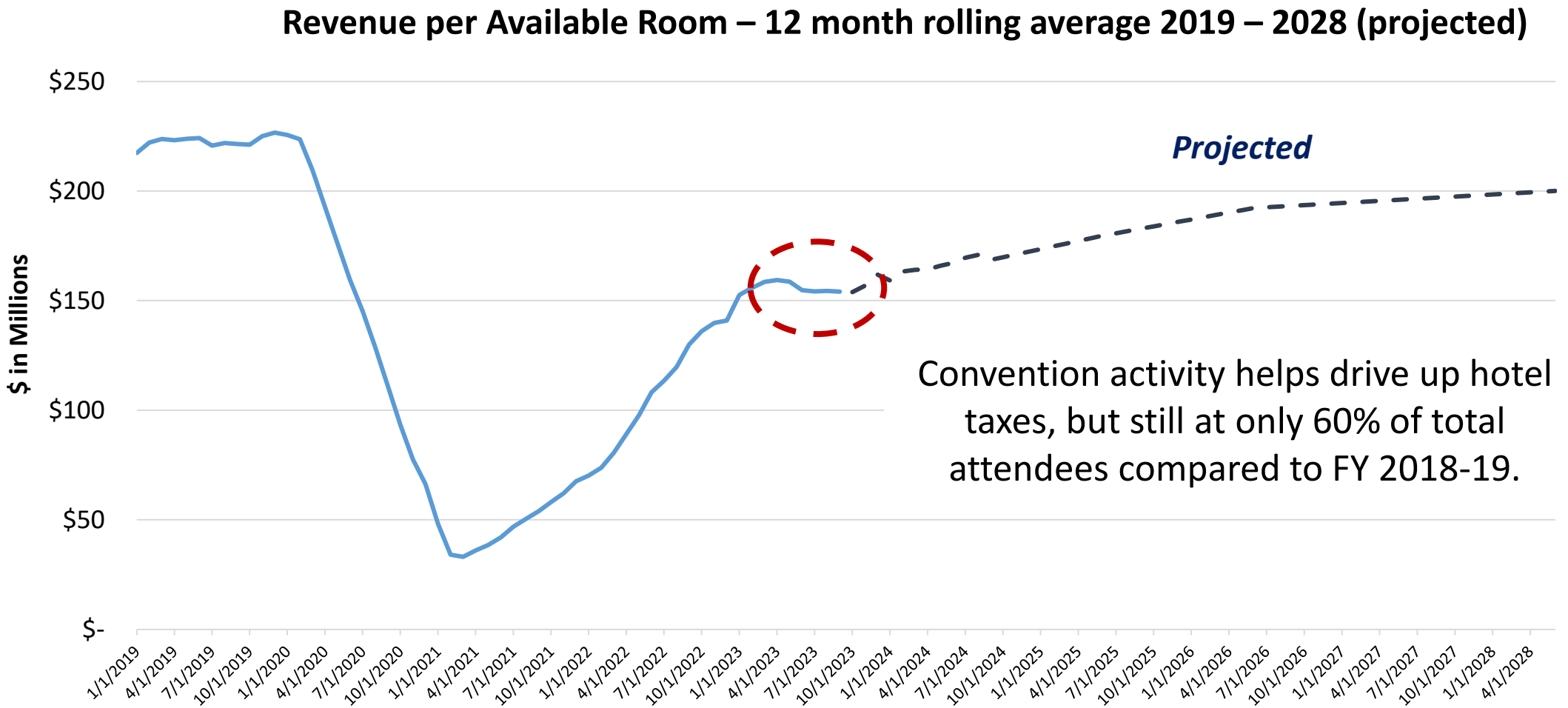
Office Vacancy Rates Still Climbing



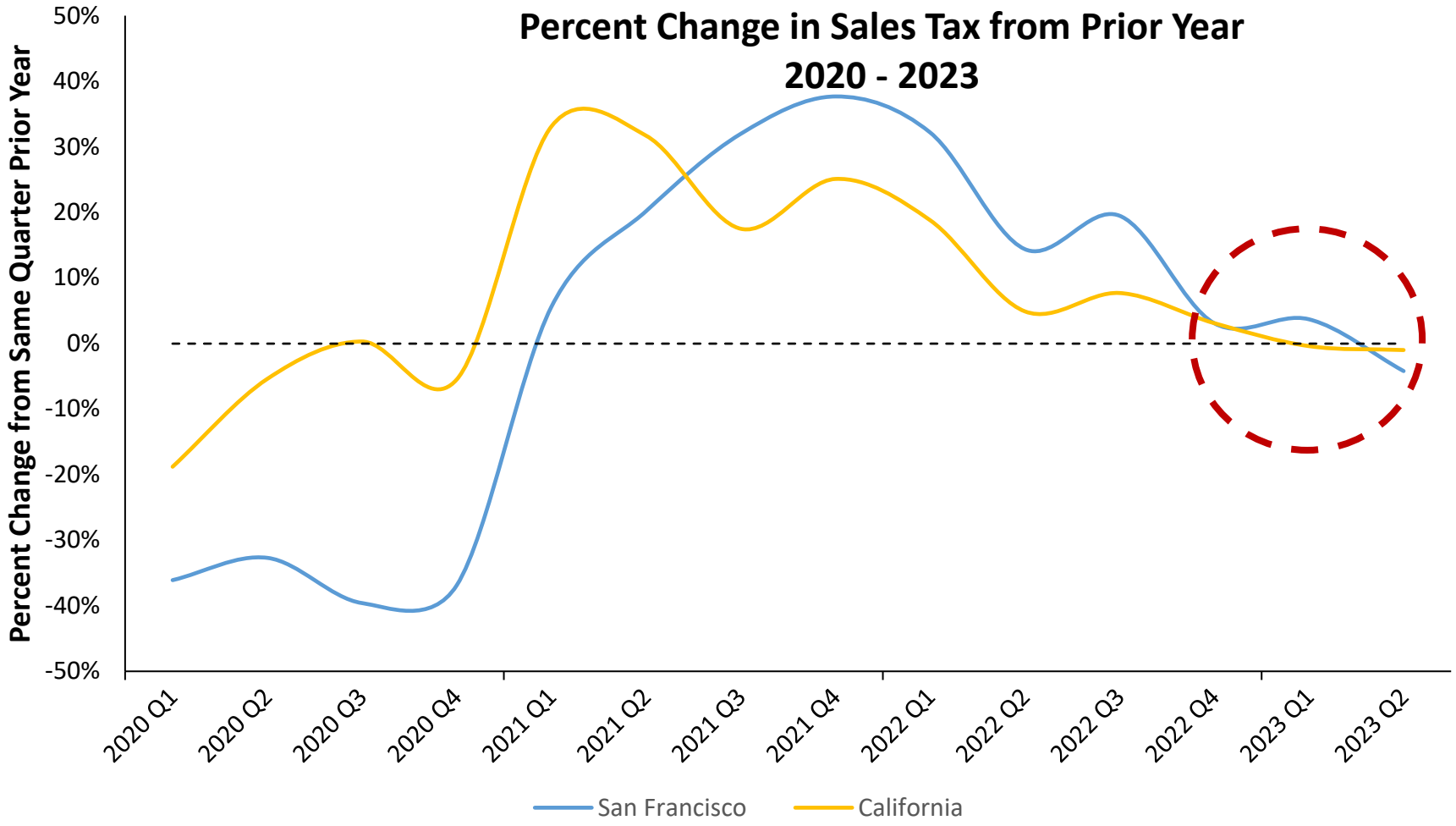
Transfer Tax Revenue at Great Recession-Era Low



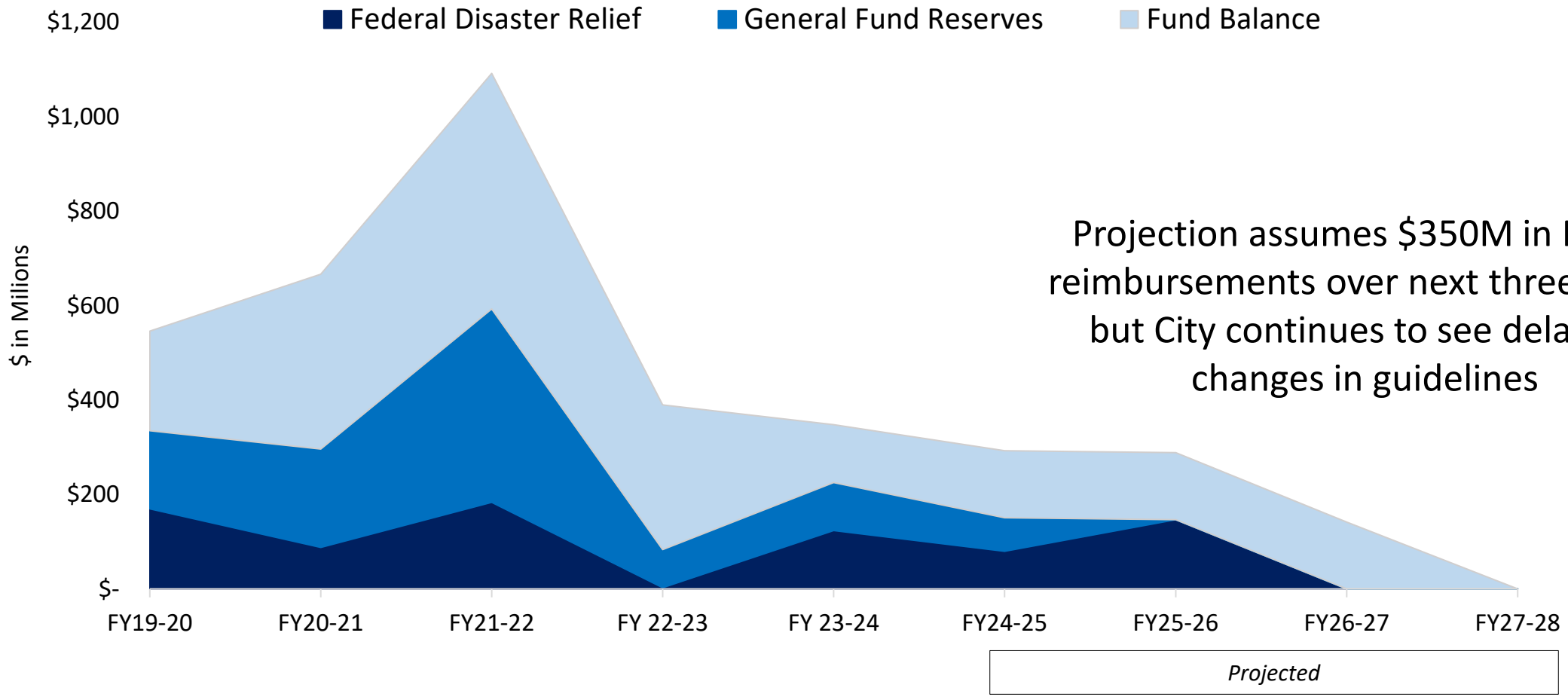
Hospitality Rebound Stalling



Local & State Sales Tax Slowing



Depletion of One-Time Sources

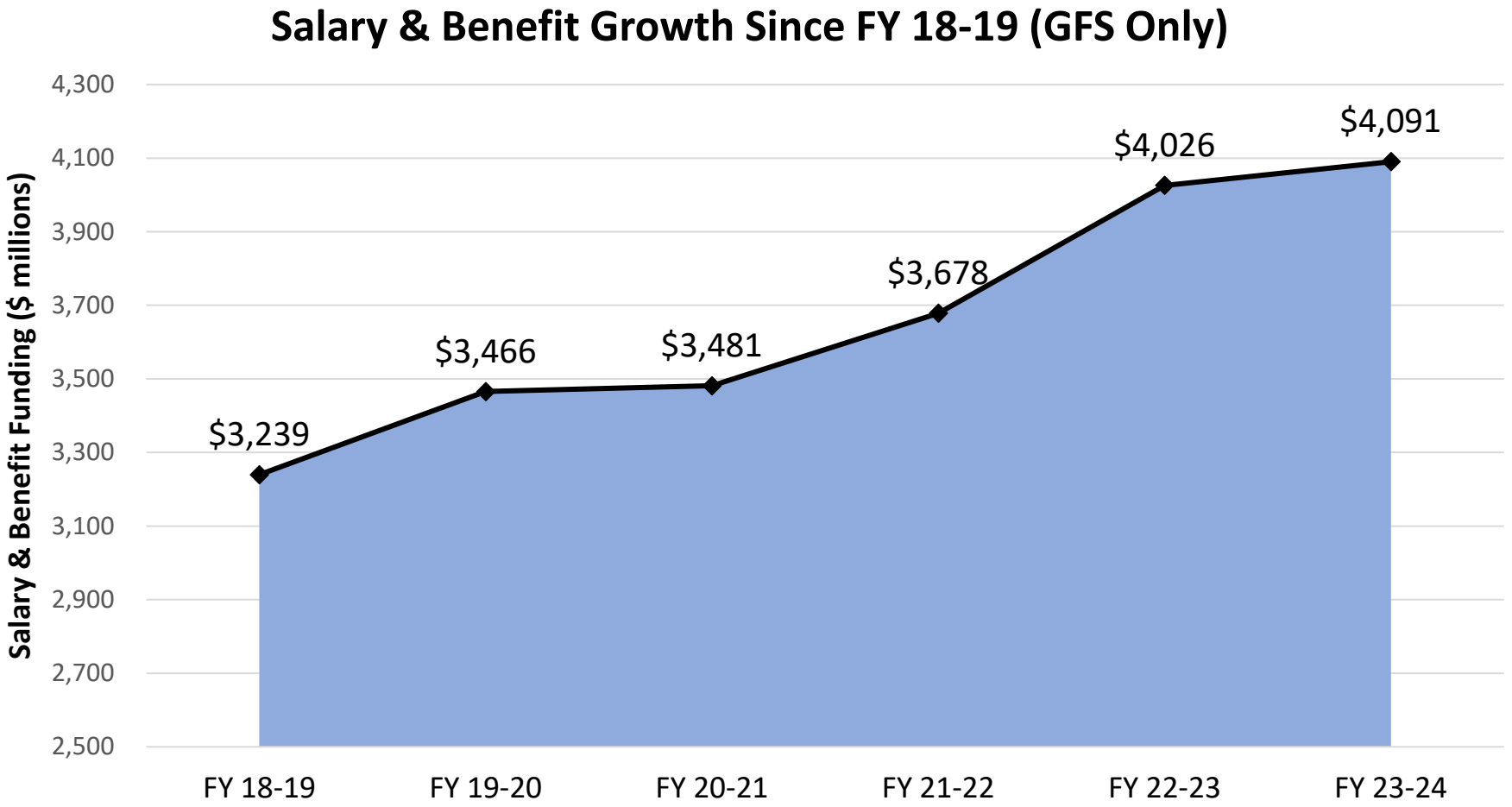


Projection assumes $350M in FEMA reimbursements over next three years, but City continues to see delays & changes in guidelines

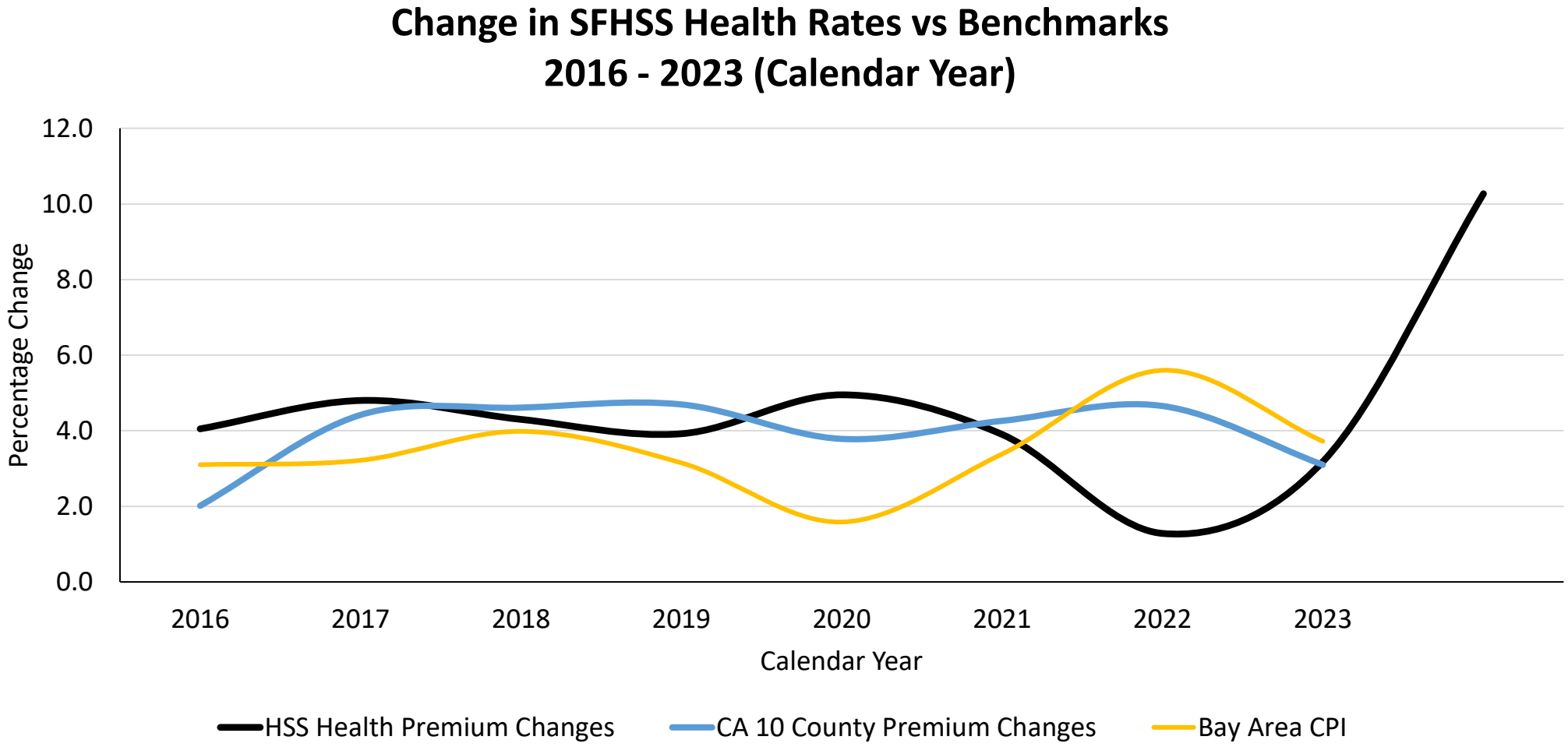
Key Expenditures

- **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



Health Care Cost Growth at 9-10%



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