



2018-19 Early General Fund Budget Status

The purpose of this report is to provide City Council with an update on the 2018-19 budget development process. Based on current information, we are confident that the 2018-19 budget can be balanced without increasing revenues or negatively impacting existing services based on the following:

- One-time expenditure savings carried in the fund balance;
- Ongoing savings from early Council budget actions; and
- Improved revenue.

This is the first of our annual series in building a City budget for 2018-19. The schedule includes:

1. Early GF Budget Status - today
2. Capital projects review, inventory of programs and 5-year GF Forecast - February
3. City Manager's Trial Budget - March
4. Public review of Trial Budget - April
5. Proposed Budget presentation - May
6. Formal Budget adoptions - June/July

THIS ITEM IS FOR INFORMATION AND DISCUSSION.

Summary

Since February 2017, the projected budget status for 2018-19 has been refined under the direction of the City Council as staff finds ways to tighten expenditures and receives access to current information on revenues and expenditure trends. Based on current information, we are confident that the 2018-19 GF budget can be balanced without negatively impacting existing services or requiring a revenue increase. This report also briefly discusses several other assumptions that will significantly impact the overall budget status as we look ahead.

The February 2017 Five-Year GF Forecast projected a potential GF budget shortfall of between (\$43 million) and (\$64 million) for fiscal year 2018-19. At the time of last year's forecast the estimated beginning balance for fiscal year 2017-18 was estimated at \$119 million. As reported in September 2017, the actual beginning balance was \$144 million ([Attachment A, Item 1](#)). The change in fund balance provides additional one-time resources of approximately \$25 million that can be used to address next year's projected shortfall.

In addition to the fund balance changes discussed above there are four other changes totaling approximately \$31 million that contribute to next year's improved budget forecast. These items include:

- Net increase in current year GF resources of approximately \$9 million ([Attachment A, Item 2](#));
- Early efficiencies approved by City Council in September totaling approximately \$4 million in 2017-18 ([Attachment A, Item 3](#));
- Current year savings resulting from staff's detailed technical reviews and tight spending controls totaling approximately \$10 million ([Attachment A, Item 4](#)); and
- Net increase in 2018-19 state-shared sales tax totaling approximately \$8 million ([Attachment A, Item 5](#)).

These items will be discussed in greater detail during next month's Five-Year GF Forecast as staff continues to analyze all revenue and expenditure data.

Areas to Monitor

While many variables ultimately influence the budget, it is our opinion that the following four items reflect the major areas of discussion over the next few months as staff develops the Five-Year GF Forecast and the Trial Budget to be presented in March. These items include the following:

General Fund Revenue Outlook

Excluding one-time revenue sources and timing issues, GF revenue collections at 5 months were \$18.5 million or 4.2% higher than last fiscal year. Budgeted revenue for 2017-18 is \$1.140 billion, representing 3.1% growth over 2016-17. As a result, revenue collections through five months are trending closely to budgeted revenue; however, because we only have five months of activity, GF revenue collections will be closely monitored until we receive all holiday-related sales tax data before we finalize our revenue projections. These estimates will be reflected in upcoming budget discussions with the City Council during the annual budget development process that will take

place over the next few months.

One area of concern for the GF revenue outlook to monitor closely is the future allocation of State-Shared Revenue, which is now based on annual population adjustments. State-shared sales tax is distributed to cities and towns based on relative population share. While Phoenix's population has grown over the years, our relative population share decreased from 30.3% in 2010 to 29.38% this year. The city's population becomes even more important as we look ahead to the 2020 Census. The city will need to take an active role to encourage strong resident participation. To assist with this effort, the city will need to allocate additional resources for marketing materials, advertisements and staff as soon as possible to ensure that Phoenix residents are accurately reported. In the absence of strong resident participation, the city's relative population share could decrease further.

GF Pension Costs

While total COPERS-related expenses are expected to increase next year, these increases are expected to be less than what was originally forecasted in last year's Five-Year GF Forecast. This change is due to the continued impact of pension reform, as well as strong plan performance over the last year. More detailed projections for COPERS-related costs in future years are currently being developed and will be discussed in greater detail during next month's Five-Year GF Forecast. The net pension unfunded liability for COPERS decreased from \$1.833 million to \$1.776 million. More detailed projections for COPERS-related costs in future years are currently being developed based on recently approved actuarial reports.

HB 2485, approved by the State in 2017, changed the amortization of Police and Fire pensions. As a result, GF costs are expected to decrease by approximately \$5 million in FY 2018-19 as compared to the current year budget and by as much as \$15 million when compared to last year's Five-Year GF Forecast. This decrease accounts for adoption of a 25-year amortization period, impact of pension reform and strong plan performance over the last year. In addition, this also provides resources needed to establish the pension stabilization fund. However, as discussed with the Council in December, the unfunded public safety pension liability still requires significant, ongoing attention. The net pension unfunded liability for PSPRS increased from \$2.108 million to \$2.687 million.

In the absence of the 25-year amortization period, GF public safety pension costs would increase by approximately \$25 million in 2018-19. This change would seriously impact our ability to balance next fiscal year without either additional revenue or difficult cuts to existing GF programs and services. Detailed projections for the next few years are currently being developed and will be included as discussion points in

next month's Five-Year GF Forecast.

Infrastructure and Capital Needs

Each year, the budget has to accommodate needed capital projects. The city's GF departments operate a large number of facilities in order to provide services to the residents of Phoenix. As these facilities age, they require significant investments for maintenance and general repairs. For the past few months Budget and Research and Finance staff have been working with Public Works staff to identify significant maintenance and other capital projects that must be addressed in the near future.

In addition to these facility projects, there are other projects like the IT server modernization project and an aging vehicle fleet, particularly in Police and Fire, that will require a significant increase in GF resources over the coming years. Staff will return to Council next month with additional information about these projects and potential funding options.

Service Levels

For more than 35 years, the city has conducted an annual Program Budget Review process to evaluate services, an essential step in the city's zero-based budgeting process. Departments are tasked with conducting a systematic review of programs at current service levels, identifying innovative service delivery changes that enable greater efficiency, evaluating priorities and recommending any changes to services. The process is also important in determining possible changes to programs to address reduced resources, increased costs and/or other factors. This process also affords city departments with an opportunity to request additional funding and resources needed to address new or increased demand for city services. As in past years, all GF departments will submit potential programmatic expenditure reductions for consideration should budget reductions be necessary. The potential reductions are in areas that would result in the least possible impact to the community and reflect the lowest priority programs within each department.

Although it is unlikely that reductions would be required, it is important that a full range of realistic potential options be available for discussion. Identifying more proposals than needed provides flexibility for the City Council and management to quickly deal with any unforeseen budgetary problems. It also allows us to address any potential cuts to state shared revenue that may arise during the legislative session.

Responsible Department

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

Attachment A

Summary of Balancing Efforts Since Last Year's Forecast

	<u>Adjustments to 2017-18 Beginning Balance</u>	<u>\$ Amount</u>
1.	At the time of last year's five-year forecast the estimated beginning balance for 2017-18 was estimated at \$119 million. As reported in September 2017, the actual beginning balance was \$144 million.	<u>\$25,000,000</u>
	Subtotal of Fund Balance Changes Since February 2017 Forecast	\$25,000,000
	<u>Additional Savings Identified After February 2017 Forecast</u>	
2.	After accounting for all estimated changes to resources (Local Sales Tax, State Shared Revenue, Primary Property Tax, User Fees, Fund Balance, Transfers and Unspent Contingency), staff is currently assuming a net increase in current year resources of approximately \$9.0M.	9,000,000
3.	In September 2017 Council approved early efficiency actions which resulted in current year one-time savings of \$4.0M.	4,000,000
4.	Current year savings resulting from staff's detailed technical reviews and tight spending controls.	<u>10,000,000</u>
	Subtotal Additional Savings	\$23,000,000
	<u>Net Adjustment to 2018-19 Resources</u>	
5.	Based on the most recent estimates staff projects that state shared revenues can be increased next fiscal year by approximately \$8.0M over estimates reflected in last year's five-year forecast	<u>8,000,000</u>
	Subtotal Adjustments to 2018-19 Resources	\$8,000,000
	Total All Adjustments	\$56,000,000