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March 12, 1997

The Honorable Willie L. Brown, Jr.  
City and County of San Francisco  
401 Van Ness Avenue, Room 336  
San Francisco, CA 94102

Honorable Members of the Board of Supervisors  
City and County of San Francisco  
401 Van Ness Avenue, Room 308  
San Francisco, CA 94102

Re: Three Year Budget Projection

Dear Mayor Brown, Ladies and Gentlemen:

Proposition F passed by the voters in November, 1994 called for a "joint report to be issued annually on the City's financial condition for the next three fiscal years from the Controller, the Mayor's budget analyst and the budget analyst for the Board of Supervisors." This is the report for fiscal years 1997-98 through 1999-2000.

Chart A provides a summary of the projected revenue shortfalls for the next three years. Please refer to Attachment I for a detailed breakdown of the sources of these projected shortfalls.

Chart A  
Summary of Projected Surplus/(Shortfall)  
(in millions)

|  | <u>1997-98</u><br>vs. 96-97 | <u>1998-99</u><br>vs. 97-98 | <u>1999-00</u><br>vs. 98-99 |
|--|-----------------------------|-----------------------------|-----------------------------|
| Projected Revenue Shortfall Without Estimate of Welfare Reform | \$(67.7)                    | \$(65.5)                    | \$(57.9)                    |
| Potential Additional Cost of Welfare Reform                    | \$(40.0)                    |                             |                             |

Our projections reflect the estimated cost of providing the City's current level of services. These projections are not intended to commit the City to make corresponding increases in future budgets. Funding the projected shortfalls will be subject to availability of funds as well as policy decisions of the Mayor and Board of Supervisors.

This is only a projection. Before future budgets are finally adopted, steps will be taken to bring these budgets into balance. We also acknowledge that projections several years ahead are less certain than those for the immediate future. In addition, this report assumes that revenue shortfalls are corrected in the year in which they first appear. To the extent shortfalls are corrected with one-time revenue or expenditure solutions, subsequent years' shortfalls will worsen.

### Unknown Public Health Costs

We have not attempted to quantify the impact of potential state and federal health legislation, except those related to welfare reform (see Welfare Reform section). Several federal revenues are expected to be at risk over the three year period, specifically Medi-Cal, Federally Qualified Health Centers (FQHC) and the Disproportionate Share program. In addition, the impact of the state's implementation of Managed Care is expected to decrease Medi-Cal revenues. The Department of Public Health does not expect to experience the full impact of Managed Care until 1999-2000. Since a precise estimate of the annual revenue losses are not currently available, we have not included these factors in our overall shortfall projection.

We have also not included any estimated costs to backfill any potential loss to grant revenues. It is a policy decision of the Mayor and the Board of Supervisors to "backfill" lost grant revenues. The Public Health department anticipates grant losses totaling over \$3 million in 1997-98 to fund HIV/AIDS services (Ryan White) and substance abuse treatment services. In addition, the 1997 California Supreme Court decision in County of San Diego v. State of California may lead to further changes in revenues, ranging from additional revenues for medically indigent health care to losses due to adjustment of the realignment revenue allocation formula.

### Base Closures

Although we have included costs for the detention center at Treasure Island in our capital program, we assume that any new demand for services due to base closures will be absorbed within our current budget allocations or with additional revenues.

### Detailed Summary of Projected Shortfalls

Below is a discussion of the items listed in Attachment I that comprise our projected budget shortfalls.

#### Revenues

- We project there will be moderate revenue growth of approximately 3% annually over the next three fiscal years. The estimate includes projected growth of 1% to 2% for property taxes, 3% to 5% for sales taxes and 4% to 5% for business taxes (see Attachment II for detail by specific revenue source).
- The General Fund receives an annual service payment each year from the San Francisco International Airport. The amount is partly based on concession sales and is expected to increase by \$500,000 in fiscal year 1997-98.

### Salary/Benefit-Related Items

We have assumed that employees will receive some level of salary and benefit increases over the next three years. We have based our projections on the following components:

- **Annualization of 1996-97 Memoranda of Understanding (MOUs) Provisions** - In many instances, new wage rates and benefits became effective during the fiscal year 1996-97. Providing these wages and benefits for a full year in fiscal year 1997-98 will cost an additional \$10.8 million.
- **New Provisions in Existing MOU's** - Several bargaining units, including those for the Police, Firefighters and Muni Operators, had previously negotiated contracts which extend into fiscal years 1997-98 and 1998-99. Wage and benefit increases have been pre-determined and the new provisions will cost the City \$20.4 million in fiscal year 1997-98 and \$12.5 million in fiscal year 1998-99. These estimates assume that Muni Operators will receive the maximum 3% wage cap as specified in their contract for fiscal years 1997-98 and 1998-99. None of these contracts have new wage or benefit provisions in fiscal year 1999-2000.
- **Estimated Cost of New MOUs** - We have projected that wages will be increased by the Consumer Price Index for Wages (CPI-W) over the next three years. These projected increases will result in additional wage costs of \$27.3 million in fiscal year 1997-98, \$39.7 million in fiscal year 1998-99 and \$59.8 million in fiscal year 1999-2000. The expected cost associated with unknown MOUs will increase in future years as current MOUs expire. No costs have been included for enhanced benefits since the City has agreed in past years to pick-up the full cost of the employees' share of retirement contributions and health care costs. **This estimate does not reflect the City's willingness or ability to pay, nor does it represent what will ultimately be negotiated.** Factors other than the CPI -W such as the availability of funds, the adequacy of previous year contracts, and the overall job market for similar job classifications will ultimately determine what will be agreed upon. Nonetheless, the CPI-W serves as an indication of overall wage inflation pressures in the region.
- In fiscal year 1997-98, the City will incur additional costs to annualize new positions added to the fiscal year 1996-97 budget. Since most of the new positions were funded for only three-quarters of a year, an additional \$7.6 million will be needed in fiscal year 1997-98 to fund the positions for a full year.
- The Health Services System has estimated the City's retiree subsidy payments will cost an additional \$1.6 million in fiscal year 1997-98.
- The PERS safety retirement contribution rate will increase by approximately one percent next fiscal year, resulting in an additional \$800,000 in General Fund costs.
- Health Service System contributions are established, pursuant to the City's Charter, by taking the average contributions paid by the 10 largest counties in California. Since these counties have increased their contribution, the City will have to increase the amount it provides by an estimated \$700,000.

## Mayor Brown and Board of Supervisors

### Joint Report

March 12, 1997

Page 4

- The federal government has increased the Social Security cap. This increases the maximum wage that the City has to match an individual's Social Security contributions. As a result, the City's matching payments for Social Security will increase by approximately \$600,000 next fiscal year.
- Retirement rates were lowered in January 1997. Additional savings of \$6.5 million will be realized in fiscal year 1997-98 as a result of these new rates being applied for the entire year.

### Known Public Health Items

Public Health is an area of great uncertainty given the status of federal and state funding decisions. As noted above, we have not attempted to estimate the costs resulting from these future decisions. The Public Health items we have quantified are detailed below (any salary and benefit related costs increases are included in our citywide line-items).

- Public Health is projecting a \$6.6 million loss in overall revenues. Revenue decreases in 1997-98 include one-time revenue losses and reductions in substance abuse revenue due to a rate reduction and eligibility restrictions. The department is projecting slight increases in realignment revenues in all three years.
- Pharmaceutical costs are projected to increase by 10% annually in each of the next three fiscal years. This increase would be partially offset by additional revenues, but would result in net new costs of \$1.3 to \$2.0 million over the next three years.
- Substance abuse costs are projected to increase by \$2.1 million in 1997-98 due to the annualization of the pending supplemental appropriation which would expand treatment services.
- Public Health projects no COLA adjustment for contractors in fiscal years 1997-98 and 1998-99. A 4% COLA adjustment is projected in fiscal year 1999-2000 costing \$6.9 million.
- Other Public Health items to maintain the current level of services would cost an additional \$1.1 million in 1997-98. Examples include the annualization of health services at County Jail No. 9 as well as the annualization of breast cancer and Emergency Medical Service Agency programs.

### Miscellaneous Items

- The fiscal year 1996-97 budget included \$21.5 million in funding for capital facilities maintenance projects. This level of funding was significantly higher than the five previous years. In fiscal year 1997-98, we expect the City to reduce capital project funding to \$14.5 million, consistent with prior years and resulting in a \$7.0 million reduction.
- General fund debt service payments related to lease financing are expected to increase by \$1.0 million in fiscal year 1997-98, decrease by about \$100,000 in fiscal year 1998-99

and decrease by \$1.0 million in fiscal year 1999-2000. No debt service payments were included for the 800mhz city-wide radio system project or the proposed football stadium project, because of the uncertainties associated with each. Debt related to General Obligation bonds is also not included since it is separately paid from property taxes.

- The City is building a new Combined Emergency Communication Center that relies on a mix of funding; including revenue from a surcharge attached to phone charges, grants, General Obligation Bond proceeds and the General Fund. In Fiscal Year 1997-98, the project has a potential General Fund requirement of \$2.0 million for computer software and hardware. The project does not have a General Fund cost in Fiscal Year 1998-99. In Fiscal Year 1999-2000, an additional \$2.0 million will also be required for computer hardware.
- We expect inflation, as measured by the consumer price index, to be 3.3% in 1997-98, 3.9% in 1998-99 and 4.6% in 1999-2000. We assume that the costs of goods and services will increase accordingly.
- Each year the City includes a general fund contingency reserve in its budget. The reserve is used to fund unanticipated and emergency needs that arise during the year, and must be replenished in subsequent years. Consistent with prior funding levels, we estimate that the City will establish an \$11 million reserve in fiscal year 1997-98, and will increase this amount by \$1 million in each of the next two years.
- The Controller's Six Month Report, issued February 6, 1997, projected that the City would end the current fiscal year with a \$24.5 million available surplus, which can be carried forward and used to help balance the fiscal year 1997-98 budget. However, since the prior year's surplus of \$32.5 million was higher, we are showing an \$8.0 million loss to reflect the difference.

96-97  
95-96

### Welfare Reform

On August 22, 1996, President Clinton signed the Personal Responsibility and Work Opportunity Act (P.L. 104-193), ending the federal entitlement to welfare benefits. P.L. 104-193 caps the amount of federal dollars available to the states, and gives states broad authority in both allocating those dollars and designing programs for low-income people. In addition, non-citizens, including legal immigrants, are restricted from eligibility for most federal welfare benefits.

Welfare reform will bring enormous long-term health and welfare financial responsibilities to the City beginning in FY 97-98. The Legislature is currently deciding how to allocate the block granted funds and what the programmatic requirements of the new welfare system will be. As such, there is a great deal of uncertainty for the City as to what level of funding will be provided by the State. We are projecting welfare reform could increase City expenditures by up to \$40.0 million in FY 97-98. We have not included in this estimate a projection of state or federal revenue reimbursements, although the City expects to be reimbursed for some or all of these increased costs. We have also not made a projection of potential incremental costs in FY 98-99 or FY 99-00. The major components of our \$40 million cost estimate are detailed below.

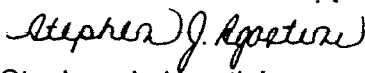
- Of most immediate concern and of largest significance financially to the City is the loss of Supplemental Security Income (SSI) benefits to aged, blind and disabled legal immigrants, which we estimate could cost up to \$35.0 million in increased General Assistance (GA) payments and administrative costs. There are 17,000 legal immigrants in San Francisco currently receiving SSI cash benefits who will lose their benefits by August 1997 unless they have become U.S. citizens prior to that time. To the extent that these individuals apply and are eligible for GA, the City's General Fund will have to pay 100% of the GA payments. We have assumed that with the City's aggressive naturalization program, approximately half of these recipients will become citizens and remain on SSI. The other half will be eligible for GA.
- Eligibility for the In Home Supportive Services (IHSS), which allows the frail to stay in their homes, rather than more costly nursing homes or hospitals, is linked with eligibility for SSI. Approximately 1,000 legal immigrants in San Francisco receive IHSS. Because they are ineligible for SSI benefits as of August, they will also be ineligible for IHSS. In the Governor's 97-98 Budget, there is no proposal to "de-link" IHSS and SSI eligibility. Without State action, San Francisco will save over \$1.0 million in IHSS costs, but may also see an accompanying rise in census at Laguna Honda and San Francisco General Hospital at a much more significant cost.
- As a result of federal legislation that took effect on January 1, 1997, 2,000 SSI recipients who became disabled solely because of a drug or alcohol addiction are now ineligible for SSI. We estimate that approximately half will re-qualify for SSI due to another disability and that 900 of those persons will become eligible for GA. Annualization of the approximately \$2.0 million budgeted in 96-97 will result in an additional \$2.0 million in GA payments for this population in 97-98.
- The new federal legislation prohibits all undocumented persons from receiving any state and local medical benefits except emergency medical services. In San Francisco, close to 1,000 undocumented women and their children receive prenatal services, resulting in another \$1.0 million decline in revenue for these services.
- Over one hundred SSI legal immigrants are in board and care homes, locked mental health facilities, or receiving other residential mental health and/or substance abuse treatment services. We assume approximately \$800,000 in additional annual costs for the Department of Public Health to provide these services. Unlike the rest of the SSI legal immigrant population, we do not project a 50% citizenship rate due to the likely inability of these clients to fully comply with the citizenship process and assume a GA offset.

### Summary

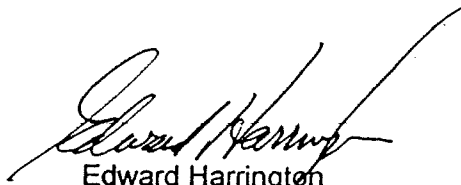
For Fiscal Year 1997-98, we are projecting a budgetary shortfall of \$67.7 million plus an additional potential cost of \$40 million for welfare reform. This projection assumes a continuation of the same service levels provided in Fiscal Year 1996-97. Our projected budgetary shortfalls for fiscal years 1998-99 and 1999-2000 are \$65.5 million and \$57.9 million, respectively. As previously indicated, when the City's annual budgets are finally adopted by the Mayor and the Board of Supervisors, such budgets must and will be fully balanced in accordance with Charter requirements.

This report is based on the best information available at this time. All three of our offices will continue to work closely together in the coming months and will keep you apprised of any changes that occur.

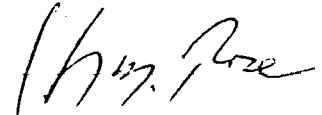
Respectfully submitted,



Stephen J. Agostini  
Director of Finance  
Office of the Mayor



Edward Harrington  
Controller



Harvey M. Rose  
Budget Analyst  
Board of Supervisors

Attachments

cc: Honorable Louise Renne, City Attorney  
John Taylor, Clerk of the Board

**Attachment I**  
**Joint Report 1997-98**  
**Estimated Costs of Providing Current Service Level**  
**12-Mar-97**

|  | <u>1997-98</u>             | <u>1998-99</u> | <u>1999-2000</u> |
|--|----------------------------|----------------|------------------|
| <b>Revenues:</b>   |                            |                |                  |
| GF Revenue Growth (Attachment II)                            | 27.5                       | 29.5           | 30.0             |
| Changes in Airport Service Payment                           | 0.5                        | (0.3)          | 1.0              |
| <b>Salary/Benefit-Related Items:</b>                         |                            |                |                  |
| Annualize 1996-97 provisions                                 | (10.8)                     |                |                  |
| New Provisions in existing MOU's                             | (20.4)                     | (12.5)         |                  |
| Estimated Cost of new MOU's                                  | (27.3)                     | (39.7)         | (59.8)           |
| Annualize New Positions                                      | (7.6)                      |                |                  |
| HSS- Retiree Subsidy   | (1.6)                      |                |                  |
| PERS Safety Rate   | (0.8)                      |                |                  |
| Health Service Rates   | (0.7)                      |                |                  |
| Increase in Social Security Cap                              | (0.6)                      |                |                  |
| Retirement Rate decrease                                     | 6.5                        |                |                  |
| <b>Public Health:</b>  |                            |                |                  |
| Public Health Revenue Projection                             | (6.6)                      | 3.2            | 3.2              |
| Pharmaceutical increases (net)                               | (1.3)                      | (1.8)          | (2.0)            |
| Substance Abuse Treatment on Demand                          | (2.1)                      |                |                  |
| Contractor COLA's  |                            |                | (6.9)            |
| Other  | (1.1)                      |                |                  |
| <b>Miscellaneous Items:</b>                                  |                            |                |                  |
| Capital Program  | 7.0                        |                |                  |
| Debt Service   | (1.0)                      | 0.1            | 1.0              |
| Combined Emergency Dispatch Center                           | (2.0)                      |                | (2.0)            |
| Professional Services Inflation                              | (1.4)                      | (1.7)          | (2.1)            |
| Other Non-Salary Inflation                                   | (4.9)                      | (5.9)          | (7.3)            |
| GF Reserve Replenishment                                     | (11.0)                     | (12.0)         | (13.0)           |
| Change in Expected Year-End Surplus                          | (8.0)                      | (24.5)         |                  |
|  | <u><del>325</del> 24.5</u> |                |                  |
| <b>Total Estimated Shortfall w/o Welfare Reform Estimate</b> | <u>(67.7)</u>              | <u>(65.5)</u>  | <u>(57.9)</u>    |
| <b>Potential Additional Cost of Welfare Reform</b>           | <u>(40.0)</u>              | -              | -                |

96-97

Use Year <sup>95-96</sup> 32.5

Proj Year <sup>96-97</sup> 24.5

8



Attachment II

CITY AND COUNTY OF SAN FRANCISCO  
Major Revenues - General Fund and General Fund-Supported Departments  
(figures in thousands of dollars)

|                               | FY94-95          | FY95-96          | FY96-97          |                  |                  | Forecast         |                 |                    |                 |                    |                 |
|-------------------------------|------------------|------------------|------------------|------------------|------------------|------------------|-----------------|--------------------|-----------------|--------------------|-----------------|
|                               | Actual           | Actual           | Budget           | Projected        | Base             | FY97-98          | Growth (1)      | FY98-99            | Growth          | FY99-00            | Growth (2)      |
| Property Taxes                | \$326,739        | \$317,016        | \$326,981        | \$326,981        | \$326,981        | \$330,251        | \$3,270<br>1.0% | \$336,030          | \$5,779<br>1.8% | \$342,751          | \$6,721<br>2.0% |
| Business Taxes                | 163,055          | 175,314          | 186,390          | 186,390          | 186,390          | 195,710          | 9,320<br>5.0%   | 203,538            | 7,828<br>4.0%   | 211,679            | 8,142<br>4.0%   |
| Sales Tax                     | 92,111           | 99,891           | 105,415          | 107,839          | 107,839          | 113,231          | 5,392<br>5.0%   | 117,760            | 4,529<br>4.0%   | 121,293            | 3,533<br>3.0%   |
| Utility Users Tax             | 51,579           | 53,695           | 57,024           | 57,024           | 57,024           | 57,822           | 798<br>1.4%     | 59,268             | 1,446<br>2.5%   | 60,750             | 1,482<br>2.5%   |
| Prop. Transfer Tax            | 20,038           | 22,968           | 23,443           | 28,639           | 28,639           | 30,787           | 2,148<br>7.5%   | 32,326             | 1,539<br>5.0%   | 33,943             | 1,616<br>5.0%   |
| Hotel Tax (2)                 | 34,651           | 39,519           | 40,294           | 43,365           | 43,365           | 43,579           | 214<br>6.5%     | 46,186             | 2,607<br>5.5%   | 48,734             | 2,548<br>5.5%   |
| Parking Tax                   | 24,073           | 28,518           | 28,616           | 30,188           | 30,188           | 31,094           | 906<br>3.0%     | 32,026             | 933<br>3.0%     | 32,987             | 961<br>3.0%     |
| Public Safety Sales Tax       | 45,237           | 49,741           | 51,798           | 52,705           | 52,705           | 55,077           | 2,372<br>4.5%   | 57,004             | 1,928<br>3.5%   | 59,000             | 1,995<br>3.5%   |
| Motor Vehicle-In-Lieu         | 61,733           | 64,520           | 68,536           | 68,966           | 68,966           | 72,069           | 3,103<br>4.5%   | 74,952             | 2,883<br>4.0%   | 77,950             | 2,998<br>4.0%   |
| Traffic Fines                 | 48,285           | 49,453           | 49,500           | 48,604           | 48,604           | 48,604           | 0<br>0.0%       | 48,604             | 0<br>0.0%       | 48,604             | 0<br>0.0%       |
| <b>Total - Major Revenues</b> | <b>\$867,501</b> | <b>\$900,635</b> | <b>\$937,997</b> | <b>\$950,701</b> | <b>\$950,701</b> | <b>\$978,223</b> | <b>\$27,522</b> | <b>\$1,007,696</b> | <b>\$29,472</b> | <b>\$1,037,691</b> | <b>\$29,995</b> |
| <b>% Change</b>               |                  |                  |                  |                  |                  |                  | <b>2.9%</b>     |                    | <b>3.0%</b>     |                    | <b>3.0%</b>     |