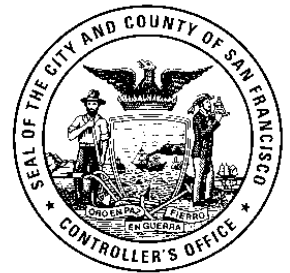


FY 2018-19 and FY 2019-20 Revenue Letter

Controller's Discussion of the Mayor's Proposed Budget

The Charter requires that the Controller comment on revenue estimates assumed in the Mayor's FY 2018-19 and FY 2019-20 proposed budget. We find tax revenue assumptions to be reasonable, and reserves and baselines to be funded at required levels. As a cautionary note, the proposed budget relies on continued revenue growth, use of prior year fund balance which is a one-time source, and certain assumptions about the outcome of current and future ballot measures.



June 12, 2018

City & County Of San Francisco
Office of the Controller
Budget & Analysis Division

About the Budget & Analysis Division

The Budget and Analysis Division (BAD) manages the technical development of the City's annual budget, including forecasting tax revenues, costing and budgeting labor and benefit costs, and assisting the Mayor and Board of Supervisors with costing and budgeting of policy initiatives. The group manages the City's adherence to voter-approved spending requirements and financial policies and produces a variety of reports, including quarterly budget status updates and various fee-related reports. Additionally, the division manages property tax apportionment, rate setting, and reporting to the state, places special assessments on property tax bills, and processes the Assessor's changes to prior and current year property tax rolls.

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Executive Summary

Key findings from our review of the proposed two-year budget:

- **The tax revenue assumptions in the adopted budget are reasonable and consistent with our expectation of a continued but slowing economic expansion.** Significant growth in property and business tax revenue is partially offset by weakness in certain economically sensitive sources including hotel, sales, and transfer tax. The duration and pace of the current economic expansion will warrant close monitoring during the upcoming budget cycle.
- **While the use of prior year fund balance is matched with one-time expenditures, the loss of this revenue source will create budget challenges in future years.** The two-year budget uses \$403.9 million of prior year fund balance, a decrease of approximately \$57.0 million from the prior adopted budget. Use of fund balance is considered a one-time source, and will create challenges in the FY 2020-21 budget absent additional revenue increases or expenditure savings. The loss of this source is the single largest driver of a projected \$521.0 million shortfall in FY 2021-22 in our most recent budget forecast.
- **The proposed budget was contingent on the outcome of a tax measure on the June 5, 2018 ballot that appears to have failed.** The budget assumed the passage of a new dedicated tax on commercial rent (June 2018 Prop D). Revenue from this tax supports \$29.9 million in specific new homelessness and housing services in FY 2018-19 and \$60.4 million in FY 2019-20. Appropriations have been placed on Controller's reserve given this outcome and will not move forward absent amendment to the proposed budget by the Mayor and the Board of Supervisors.
- **Two statewide initiatives likely to be on the November 2018 ballot would create other risks.** While not yet qualified for the ballot, the potential repeal of the Road Repair and Accountability Act of 2017 (SB1), which was passed by the State legislature in 2017, would result in an annual loss of approximately \$23.0 million for road paving and \$36.5 million for transit services and repair, and a total of \$89.3 million over the two-year budget. As noted below, the budget includes a reserve to reduce the General Fund impact of this and other risks. A second initiative to amend the California constitution to increase state and local approval thresholds for tax and fee increases is pending signature verification. If approved by voters, it would appear to invalidate two local measures on the June 5, 2018 ballot which appear to have passed: a new commercial rent tax for child care and education (Prop C) and a City parcel tax for the benefit of the San Francisco Unified School District (Prop G), neither of which is appropriated in the proposed budget.
- **Code-mandated reserves are funded and maintained at required levels, and new reserves are proposed given known uncertainties and risks.** General Reserve funding levels in the budget are at code-mandated levels. No deposits or withdrawals from

economic stabilization reserves are triggered given budgeted revenue assumptions. In addition, the budget sets aside \$110.0 million in unappropriated fund balance, including \$70.0 million for labor contingencies in the second year of the budget and \$40.0 million for potential state and federal impacts, including the potential repeal of SB1 on the November 2018 ballot.

- **Voter-required baseline and set-aside requirements are met or exceeded.** The majority of voter-adopted requirements are funded at required levels, while those for parks, children and transitional age youth are exceeded in the proposed budget.
- **Budgeted expenditures are projected to be within the appropriations limit mandated by the California Constitution, the "Gann Limit."** In November 2016, voters approved two measures that included temporary increases to the Gann Limit. Without the temporary voter adjustments, the City would have exceeded the Gann Limit in FY 2017-18 and would be expected to exceed the limit in FY 2018-19 and FY 2019-20. Absent a reduction in tax revenue or a shift in spending from general operating to excluded appropriations, such as capital expenditures, the City could exceed the limit in FY 2020-21 when the temporary adjustments expire. This could require the City to seek a voter-extension of these adjustments, shift spending to capital or other exempt expenditure types, or issue tax rebates in a future year.

FY 2018-19 and FY 2019-20 Revenue Letter

OVERVIEW

As shown in Exhibit 1, the Mayor's proposed budget for FY 2018-19 includes \$5.5 billion in General Fund sources and \$11.1 billion in all funds sources representing increases of 7.2 percent and 9.2 percent, respectively, from the FY 2017-18 original budget. The Mayor's proposed budget for FY 2019-20 includes \$5.5 billion in General Fund sources and \$11.2 billion in all funds sources representing increases from the FY 2018-19 proposed budget of 0.0 percent and 1.0 percent, respectively.

Exhibit 1. Overview of Budget Sources (\$ million)

General Fund			
	FY 2017-18	FY 2018-19	FY 2019-20
	Budget	Proposed	Proposed
Fund Balance	\$ 183.3	\$ 190.9	\$ 213.0
Use of Reserves	3.9	61.6	1.6
Regular Revenues	4,789.3	5,091.2	5,144.9
Transfers In to the General Fund	171.1	172.2	156.2
Total GF Sources	\$ 5,147.6	\$ 5,515.9	\$ 5,515.7
<i>Change from Prior Year</i>		<i>\$ 368.3</i>	<i>\$ (0.2)</i>
<i>Percentage Change</i>		<i>7.2%</i>	<i>0.0%</i>
All Funds			
	FY 2017-18	FY 2018-19	FY 2019-20
	Budget	Proposed	Proposed
Fund Balance	\$ 373.1	\$ 406.0	\$ 424.4
Use of Reserves	20.1	74.4	9.8
Regular Revenues	9,725.9	10,573.3	10,725.6
Total All-Funds Sources	\$ 10,119.1	\$ 11,053.7	\$ 11,159.8
<i>Change from Prior Year</i>		<i>\$ 934.6</i>	<i>\$ 106.1</i>
<i>Percentage Change</i>		<i>9.2%</i>	<i>1.0%</i>

Note: Totals may appear to differ from sum of line items due to rounding

Highlights include:

- Local tax revenue estimates are reasonable given current economic assumptions.** The proposed budget assumes continued economic expansion, consistent with the Joint Report Update published in March. General Fund FY 2018-19 regular revenues are increasing by \$302.0 million or 6.3 percent from the FY 2017-18 budget. In FY 2019-20 General Fund revenues are expected to increase further by \$53.6 million or 1.1 percent from the FY 2018-19 proposed budget. Local tax revenues are influenced by national and international economic developments that could cause changes to the currently favorable trends in job growth, property values and tourism. Any significant economic slowdown would require the Mayor and Board of Supervisors to adjust the budget to reflect reduced revenues. The Controller's Office will monitor revenues and provide

revenue projection updates throughout the budget years.

- **The proposed General Fund budget decreases the use of prior year fund balance.** The two-year FY 2018-20 budget uses \$403.9 million of prior year fund balance compared to \$462.1 million in the FY 2017-19 budget. The FY 2018-20 proposed use of fund balance is net of \$110.0 million in assigned but unbudgeted contingency reserves, of which \$70.0 million is to help address labor and benefit cost uncertainty and \$40.0 million is to address state and federal revenue risk.
- **The proposed General Fund budget complies with financial policies for depositing to reserves.** The proposed budget increases the use of prior year reserves from \$3.9 million in FY 2017-18 to \$61.6 million in FY 2018-19 and decreases to \$1.6 million in FY 2019-20. This includes the use of \$56.0 million of the Public Health Management Reserve in FY 2018-19 to repay the State for federally disallowed prior year payments under SB 1128. The proposed budget assumes commercial real estate market conditions will continue to slow from their FY 2016-17 peak, resulting in no projected deposits to the Budget Stabilization Reserve in FY 2018-19 or FY 2019-20. In addition, the budget complies with the General Reserve policy, which calls for increasing the General Reserve to 2.50 percent of budgeted General Fund revenues, or \$127.3 million in FY 2018-19, and 2.75 percent of budgeted General Fund revenues, or \$141.5 million, in FY 2019-20. The General Reserve is available to be appropriated by the Board for any purpose to accommodate shortfalls or new requirements during the year.

Exhibit 2. Select Reserve Balances (\$ millions)

	FY 2017-18 Projected	FY 2018-19 Budgeted	FY 2019-20 Budgeted
General Reserve	\$ 106.9	\$ 127.3	\$ 141.5
Rainy Day Economic Stabilization City	78.3	78.3	78.3
Rainy Day One-Time Reserve	47.4	47.4	47.4
Budget Savings Incentive Fund	72.5	72.5	72.5
Budget Stabilization Reserve	323.2	323.2	323.2
	\$ 628.3	\$ 648.7	\$ 662.9

- **The proposed budget includes significant Department of Public Health Revenue changes.** The Mayor's budget includes an ongoing increase of \$44.4 million in FY 2018-19 and FY 2019-20 at the Zuckerberg San Francisco General Hospital (ZSFG), which reduced General Fund support of the hospital by the same amount. In addition, the budget includes \$30.0 million in one-time revenues in FY 2018-19, which are appropriated to support one-time capital projects.

Net patient revenues at ZSFG were increased to mostly reflect FY 2017-18 actual levels, which came in higher than budgeted because of higher than anticipated patient census and increased collections from commercial insurers. The increased revenue also reflects the Medicaid managed care rule, which results in additional revenues to the City by transforming Medi-Cal supplemental payments into two new programs – the Enhanced

Payment Program (EPP) and the Quality Incentive Program (QIP). In addition to increases in hospital revenue, the Department of Public Health's budget includes \$39.8 million of one-time General Fund revenue from AB85 and the Mental Health State Plan Amendment.

- **Budgetary baselines and set-asides are funded at voter-approved levels.** Appendix 4 provides details on voter-approved mandates that determine minimum levels of revenues, expenditures or service for various programs, including:
 - **Children's baseline requirements are exceeded in both FY 2018-19 and FY 2019-20.** Children's baseline funding in the proposed budget is \$182.2 million in FY 2018-19 and \$184.5 million in FY 2019-20, which is above the required level by \$5.5 million and \$4.9 million, respectively.
 - **Disconnected Transitional-Aged Youth (TAY) baseline requirements are exceeded in both FY 2018-19 and FY 2019-20.** TAY baseline funding in the proposed budget is \$28.1 million in FY 2018-19 and \$28.8 million in FY 2019-20, which is above the required level by \$6.9 million and \$7.2 million, respectively.
 - **Police staffing requirements are met.** Police baseline staffing requires 1,971 full-duty officers net of any positions certified as civilianized pursuant to Charter section 16.123, which the Controller's Office estimates to be 77. Based on the Mayor's proposed budget, this staffing requirement will be met in FY 2018-19 and FY 2019-20.
 - **Recreation and Parks baseline requirements are exceeded in both FY 2018-19 and FY 2019-20.** Proposition B, passed by the voters on June 7, 2016, requires General Fund support to the department to grow by \$3.0 million annually from FY 2016-17 through FY 2025-26 and by aggregate discretionary revenue thereafter. The required baselines for FY 2018-19 and FY 2019-20 are \$73.2 million and \$76.2 million, respectively. The Mayor's proposed budget includes General Fund appropriations of \$75.5 million and \$77.5 million, representing surplus funding of \$2.3 million in FY 2018-19 and \$1.3 million in FY 2019-20.
 - **Dignity Fund baseline requirements are met.** Proposition I, passed by voters on November 8, 2016, requires funding for seniors and adults with disabilities to grow from \$44.1 million in FY 2017-18 to \$47.1 million in FY 2018-19 and \$50.1 million in FY 2019-20, which the Mayor's proposed budget meets.
 - **Street Tree Maintenance Fund baseline requirements are met.** Proposition E, passed by voters on November 8, 2016, requires funding for street tree maintenance of \$19.0 million in FY 2017-18, then changing by aggregate discretionary revenue thereafter. The fund grows to \$19.8 million in FY 2018-19 and \$20.1 million in FY 2019-20.
- **Ballot initiatives.** The proposed budget is contingent on the outcome of a June 5, 2018 ballot measure to establish a new gross receipts tax on commercial rent (Prop D) that

appears to have failed. The proposed budget also assumes revenue and expenditures from an anticipated November 2018 ballot measure dedicating hotel tax to arts programming will pass.

- **The Gross Receipts Tax on Commercial Rent (June 5, 2018 Prop D)** measure, which appears to have failed, imposed an additional tax of 1.7% on gross receipts from the lease of commercial space in the City to fund low- and middle-income housing, homelessness services, and the General Fund. The budget assumes \$32.0 million and \$64.0 million of revenue in FY 2018-19 and FY 2019-20, respectively, will be generated from this measure. As outlined in the proposal, after accounting for administrative costs (which are capped at 2%) and a transfer of \$1.5 million and \$3.0 million to the General Fund, the proceeds are budgeted to support \$13.4 million and \$27.2 million in FY 2018-19 and FY 2019-20, respectively, of programming at the Department of Homelessness and Supportive Housing and \$16.4 million and \$33.2 million in FY 2018-19 and FY 2019-20, respectively, of programming at the Mayor's Office of Housing and Community Development. Appropriations have been placed on Controller's reserve given this outcome and will not move forward absent amendment to the proposed budget by the Mayor and the Board of Supervisors.

Exhibit 3. Expenditures for Proposition D Budgeted in FY 2018-19 and FY 2019-20 (\$ millions)

Department	Description	FY 2018-19	FY2019-20
Homelessness and Supportive Housing	Programming for homeless adults, families or youth - temporary shelter, short and long-term subsidies; operations or acquisition of permanent supportive housing units	13.4	27.2
Mayor's Office of Housing & Community Development	Acquisition of Single Room Occupancy (SRO buildings) and associated protection of low-income households	3.0	6.0
	Acquisition of Rent-Controlled Apartment buildings, creation of a new affordable middle-income housing	10.5	21.1
	Permanent project-based subsidies to extremely low-income senior households	3.0	6.0
General Fund	Not programmed	1.5	3.0
Treasurer Tax Collector	Administration	0.6	0.6
Total		32.0	64.0

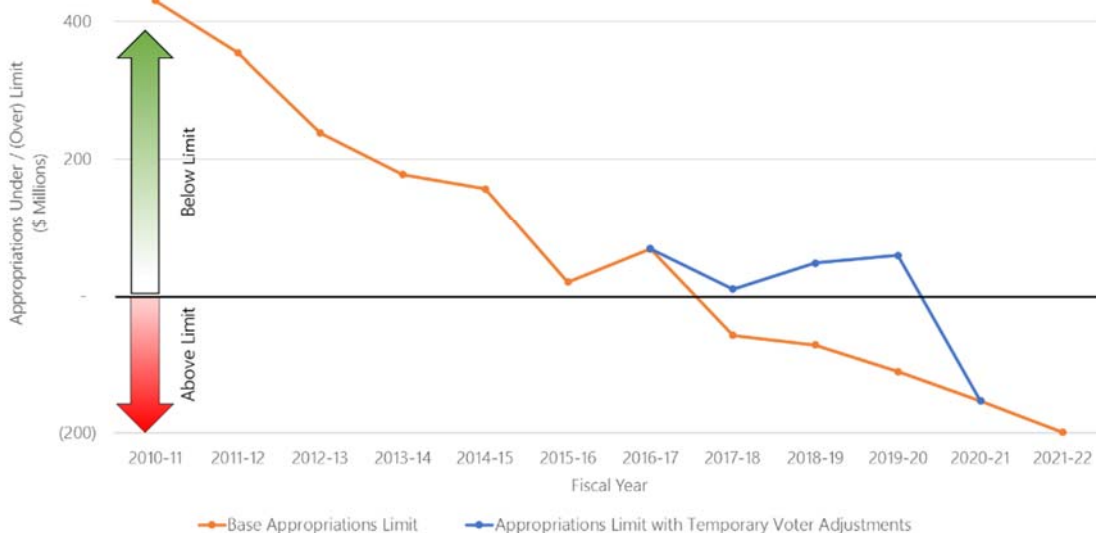
- **A measure to dedicate hotel tax for arts and cultural purposes, which is anticipated to be placed on the November 2018 ballot**, would dedicate a portion of hotel tax that is currently allocated to the General Fund to Grants for the Arts (Administrative Services Department), Cultural Equity Endowment (Arts Commission), Cultural Centers (Arts Commission), Cultural Districts (Mayor's Office of Housing and Community Development), and the Arts Impact Endowment (Arts Commission). The proposed measure establishes baseline allocations for FY 2018-19 and ties future allocations to growth or decline of hotel tax. If passed, the measure would take effect on January 1, 2019. The

budget assumes \$16.1 million of dedicated hotel tax allocations for half a year of FY 2018-19 and \$33.2 million of allocations for the full year of FY 2019-20. All expenditures associated with the ballot measure have been placed on Controller’s reserve pending passage of the measure.

- The City could exceed the appropriations limit, or “Gann limit,” mandated in Section XIII B of the California Constitution by FY 2020-21.** The Gann limit increases each year by changes in population and cost of living. Over the last ten years, the Gann limit has increased by an average of 4.2% annually. The City’s appropriations subject to the Gann limit have increased by an average of 5.2% over the last ten years, and an average of 7.7% since the end of the last recession

Voters adopted temporary increases in the Gann limit for FY 2017-18 through FY 2019-20. The chart below shows the City’s appropriations relative to the Gann limit, with and without the voter adjustments. In FY 2017-18, the City would have exceeded the Gann limit without the temporary voter adjustments. If current trends continue, the City is projected to remain below the Gann limit for the next two fiscal years. In FY 2020-21, the temporary voter adjustments will expire and, given current projections, the City would be above the limit by more than \$150 million in FY 2020-21 and more than \$200 million in FY 2021-22. This could require the City to seek a voter-extension of these adjustments, shift spending to capital or other exempt expenditure types, or issue tax rebates in a future year.

Exhibit 4. Actual and Projected Appropriations Under / (Over) the Gann Limit (\$ millions)



CONCLUSION

The Mayor's proposed budget appears to be reasonable given information currently available, with cautionary notes regarding its reliance on continued revenue growth, use of prior year fund balance, and assumptions about the outcome of ballot measures. The Controller's Office will continue to work closely with the Mayor and the Board to share information as necessary to ensure that the City's budget remains balanced.

APPENDICES

1. General Fund Sources
2. General Fund Reserve Uses and Deposits
3. One-Time Sources and Nonrecurring Revenue Policy Compliance
4. Baselines & Mandated Funding Requirements

Appendix 1. General Fund Sources

Exhibit 1-1 provides a summary of the General Fund sources in the Mayor's FY 2018-19 and FY 2019-20 proposed budget.

Sources of Funds	FY 2017-18 Budget	FY 2018-19 Proposed Budget	FY 2019-20 Proposed Budget	Notes
Prior Year Fund Balance - Operating Surplus	\$ 183.3	\$ 190.9	\$ 213.0	1
Use of Reserves	3.9	61.6	1.6	2
<i>Subtotal Fund Balance and Reserves</i>	187.2	252.5	214.6	
Regular Revenues				
Property Taxes	1,557.0	1,728.0	1,743.0	3
Business Taxes	750.8	879.4	914.7	4
Sales Tax (Bradley Burns 1%)	199.9	196.9	198.8	5
Hotel Room Tax	372.3	375.8	372.1	6
Utility Users Tax	99.7	99.1	99.9	7
Parking Tax	82.2	85.5	85.5	8
Real Property Transfer Tax	300.0	228.0	228.0	9
Stadium Admissions Tax	1.4	1.2	5.5	10
Sugar Sweetened Beverage Tax	7.5	15.0	15.0	11
Access Line Tax	49.6	51.9	53.5	12
Licenses, Permits & Franchises	30.0	30.8	31.0	
Fines and Forfeitures	4.6	3.1	3.2	
Interest & Investment Income	18.2	27.3	27.5	13
Rents & Concessions	14.1	14.8	15.0	
Intergovernmental - Federal	264.0	278.8	284.7	14
Intergovernmental - State				
Public Safety Sales Tax	101.6	104.7	106.2	15
1991 Health & Welfare Realignment	188.6	209.1	215.5	16
Public Safety Realignment	41.3	39.0	40.2	17
Other	420.3	408.3	413.8	18
Intergovernmental Revenues - Other	3.3	12.2	2.5	19
Charges for Services	232.9	248.4	234.9	20
Recovery of General Government Costs	9.9	12.9	12.9	
Other Revenues	40.1	41.1	41.4	21
<i>Subtotal Regular Revenues</i>	4,789.3	5,091.2	5,144.9	
Transfers In to the General Fund	171.1	172.2	156.2	22
Total Sources	5,147.6	5,515.9	5,515.7	

NOTES

1. Prior Year Fund Balance

The proposed budget uses \$403.9 million in unassigned General Fund surplus will be available at the end of FY 2017-18, versus the \$513.6 million ending fund balance projected in the Nine Month Report. The remaining unassigned fund balance is part of a contingency reserve: \$70.0 million for unknown labor costs related to open labor contracts with the majority of City unions, pension, and health insurance costs; and \$40.0 million for potential state and federal impacts.

Exhibit 1-2. Breakdown of Prior Year Fund Balance

Prior Year Fund Balance Projected at 9-Month	513.6
Additional Prior Year Fund Balance Projected Post 9-Month	0.3
Prior Year Fund Balance Reserved for Contingencies	(110.0)
Prior Year Fund Balance Appropriated in Budget	403.9

2. Use of Reserves

As shown in Exhibit 1-3, the Mayor's proposed budget uses of \$61.6 million from reserves established in prior years during FY 2018-19 and \$1.6 million during FY 2019-20. See Appendix 2 for projected year-end balances in FY 2017-18 through FY 2019-20.

Exhibit 1-3. General Fund Use of Reserves (\$ millions)

General Fund - Use of Prior Year Reserves	FY 2018-19	FY 2019-20
	Proposed Budget	Proposed Budget
Public Health Management Reserve	56.0	-
Recreation & Parks Savings Incentive Reserve	0.9	-
Recreation & Parks Soma Skate Park Custodial Services	0.1	-
Recreation & Parks Union Square Garage Revenue	4.6	1.6
Total Use of Prior Year Reserves	\$ 61.6	\$ 1.6

- Public Health Management Reserve.** The Public Health Management Reserve is authorized under Section 12.6 of the administrative provisions of the Annual Appropriation Ordinance to smooth volatile state and federal revenues at the Department of Public Health. The budget includes the use of \$56.0 million from this reserve to repay federally disallowed prior year payments under SB 1128. For more detailed information about this reserve, see Appendix 2.
- Recreation & Park Savings Incentive Reserve.** The Recreation and Park Savings Incentive Reserve is established by Charter Section 16.107(c) and prior to Proposition B, passed by the voters on June 7, 2016, was funded by the retention of year-end net expenditure savings and revenue surplus from the Recreation and Park Department. Proposition B eliminated the ability to retain expenditure savings while preserving deposits from surplus revenue. Any withdrawals from the reserve must go towards one-time departmental expenditures. The Mayor's proposed budget assumes the use of \$0.9 million in FY 2018-19, exhausting this reserve by the end of FY 2018-19.

- **Recreation & Park Union Square Revenue Stabilization:** The proposed budget includes a \$4.6 million use of Union Square Garage Revenue Stabilization Fund in FY 2018-19 and \$1.6 million in FY 2019-20. These withdrawals will exhaust the reserve by the end of FY 2019-20. The reserve was established to replace ongoing Recreation and Parks garage revenues lost due to the construction of the Union Square Market Street Central Subway Station.

Exhibit 1-4 provides projected growth rates for major local tax revenues. Notes are provided below.

Exhibit 1-4. General Fund Major Local Tax Revenues: Projected Growth Rates

Local Tax Revenues	FY 2018-19 Growth from FY 2017-18 Budget	FY 2019-20 Growth from FY 2018-19 Proposed Budget	Notes
Property Taxes	11.0%	0.9%	3
Business Taxes	17.1%	4.0%	4
Sales Tax (Bradley Burns 1%)	(1.5%)	1.0%	5
Hotel Room Tax	0.9%	(1.0%)	6
Utility Users Tax	(0.6%)	0.9%	7
Parking Tax	4.1%	0.0%	8
Real Property Transfer Tax	(24.0%)	0.0%	9
Stadium Admissions Tax	(11.8%)	358.3%	10
Sugar Sweetened Beverage Tax	100.0%	0.0%	11
Access Line Tax	4.7%	3.2%	12
Total Local Tax Revenue Change	7.0%	1.5%	

3. Property Tax

The FY 2018-19 General Fund share of property tax revenue is estimated at \$1,728.0 million, which is \$171.0 million (11.0 percent) more than the FY 2017-18 budget and \$77.0 million (4.7 percent) more than the Nine Month Report. The FY 2019-20 General Fund share of property tax revenue is estimated at \$1,743.0 million, which is \$15.0 million (0.9 percent) more than the proposed FY 2018-19 budget. Major changes include:

- **Roll growth:** The proposed FY 2018-19 budget reflects projected secured property assessment roll growth of 11.1 percent compared to the actual July 1st valuations for FY 2017-18. Increases in assessed values due to changes in ownership and new construction of real property are expected to account for about 82 percent of the increase. The remainder of the increase is due to the two percent inflation factor allowed under Proposition 13 for FY 2018-19. Roll growth is also estimated to increase state Vehicle License Fee (VLF) backfill revenue for the General Fund by \$28.9 million.

The proposed FY 2019-20 budget reflects projected secured roll growth of 4.6 percent compared to the proposed FY 2018-19 budget. The growth assumes about 57 percent of increased taxable value due to changes in ownership and new construction. It is assumed that the Proposition 13 inflation factor will be the maximum allowed two percent. Revenues reflect slowing sales of high value commercial properties leading up to the January 1, 2019 lien date, the point at which assessed values are set for FY 2019-20 secured annual property tax billings. The improved secured roll value is expected to increase VLF backfill revenue for the General Fund by \$12.6 million.

- Much lower escape property tax revenue anticipated:** The proposed FY 2018-19 budget reflects projected escape property tax revenues of \$48.6 million, which is \$62.0 million (56.1 percent) less than the FY 2017-18 Nine Month Report. The proposed FY 2019-20 budget reflects projected escape property tax revenues of only \$15.2 million, a \$33.4 million (68.7 percent) reduction from the FY 2018-19 projected revenue. This is, in part, a result in the reduction in commercial property turnover discussed above. Also, the number of instances when multiple, consecutive prior years of escape assessments are issued for a single assessable event is anticipated to dramatically decrease going forward, especially in FY 2019-20, highlighting the successful efforts of the Assessor-Recorder to reduce the average age of items in its enrollment queue. Supplemental property tax revenue, the other typically one-time property tax revenue per ownership change or new construction event, is anticipated to remain flat in FY 2018-19 compared to FY 2017-18 and decrease by approximately 25 percent in FY 2019-20.
- Changes in San Francisco Children's Fund allocation factor:** The proposed FY 2018-19 budget includes the change to the San Francisco Children's Fund allocation factor approved by San Francisco voters in November 2014 (Proposition C). The allocation factor will increase by \$0.0025 (from \$0.0375 to \$0.0400) on each \$100 valuation of taxable property in FY 2018-19 and remain at \$0.0400 on each \$100 valuation of taxable property in FY 2019-20, redirecting property tax revenues that would otherwise go to the General Fund.

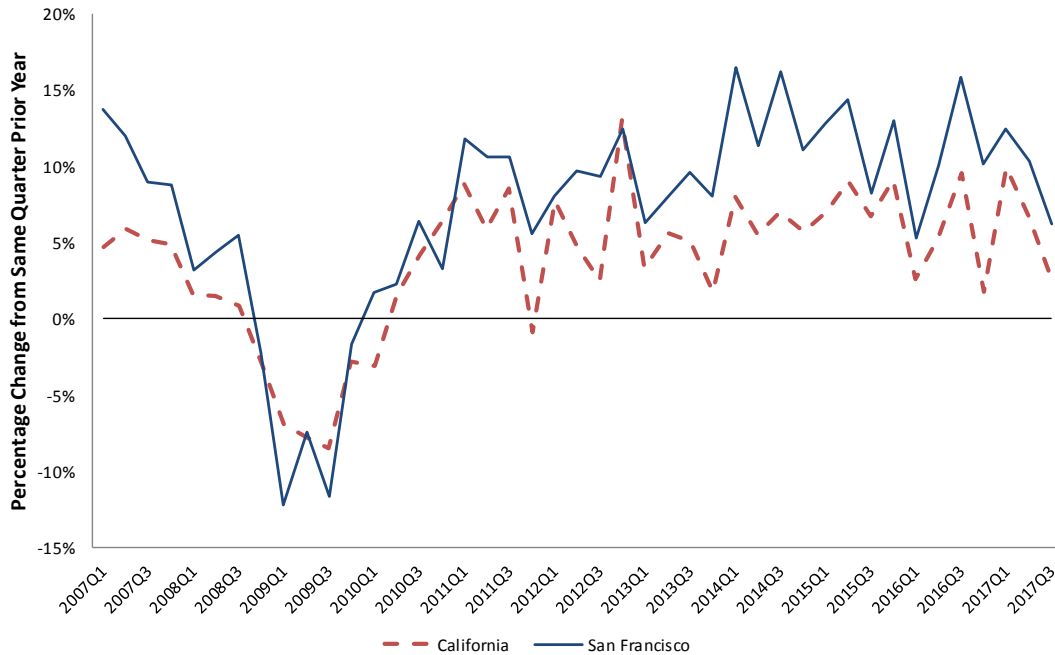
4. Business Tax

Business tax revenue is budgeted at \$879.4 million in FY 2018-19, which is \$128.6 million (17.1 percent) more than budgeted in FY 2017-18 and \$68.9 million (8.5 percent) more than projected for FY 2017-18 in the Nine Month Report. Business tax revenue is budgeted at \$914.7 million in FY 2019-20, which is \$35.3 million (4.0 percent) more than the FY 2018-19 proposed budget. The budget reflects continued economic growth in private sector employment and business activity. Revenues from business taxes and registration fees follow economic conditions in the City and have grown steadily from FY 2010-11 to FY 2017-18, reflecting underlying gains in City employment and wages during the period. The proposed budget incorporates the new business tax structure introduced by Proposition E, passed by the voters in November 2012.

The two main factors that determine the level of revenue generated by business taxes are employment and wages. Data from the Bureau of Labor Statistics show the unemployment rate for San Francisco peaked in 2010 and declined consistently in each subsequent year to a low of 2.4 percent as of March 2018. Additionally, beginning in 2011, San Francisco business tax revenue has benefitted from a rapid expansion of private sector wages, particularly in the

technology sector. As shown in Exhibit 1-5, private wages in all industries in San Francisco have seen strong growth since 2010. Over the last year and a half, total wages posted five straight quarters of double-digit year-over-year growth before dipping down to 6.2 percent growth in the third quarter of 2017. The Information Sector, which is comprised mostly of technology companies, saw wages grow by 11.0 percent during this period. In comparison, all other private sector industries excluding the Information Sector saw wages grow by 5.6 percent over the same period.

Exhibit 1-5. Change in Private Sector Wages for San Francisco and California, 2007 to 2017

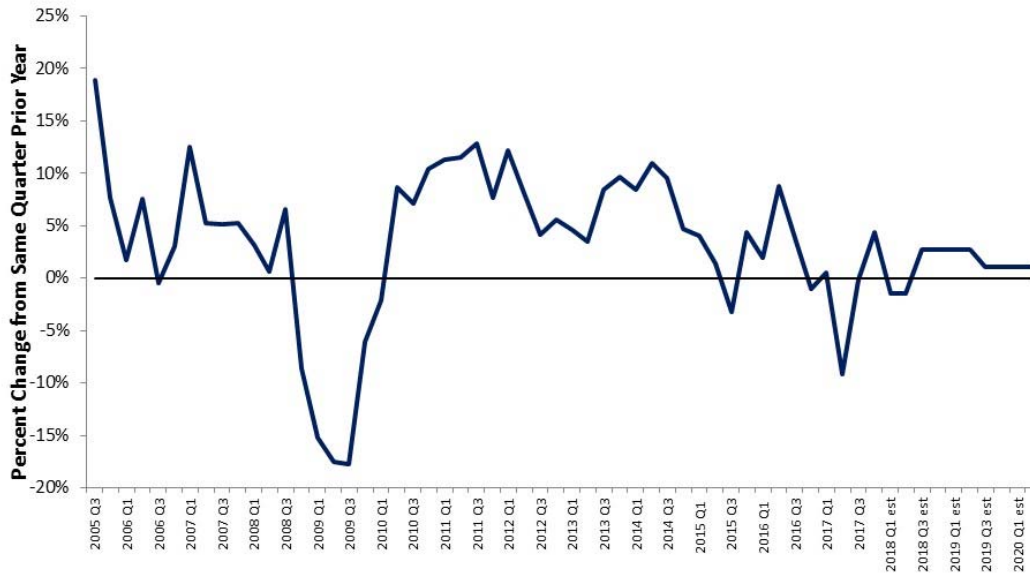


Business tax projections are based on projected growth in private sector wages and employment, which are then adjusted based on data available from the implementation of gross receipts taxes. Private employment growth is expected to slow to 1.8 percent in FY 2018-19 and 0.7 percent in FY 2019-20, while total wages are projected to continue to grow by 7.4 percent in FY 2018-19 and 6.7 percent in FY 2019-20. These projections reflect housing, transportation and other constraints to job growth. Projections are sensitive to the timing of national economic downturns, continued growth in the local technology sector, and implementation effects of the five-year phase-out of payroll taxes in favor of a tax on gross receipts.

5. Sales Tax

Local sales tax is budgeted at \$196.9 million in FY 2018-19, which is \$3.1 million (1.5 percent) less than the FY 2017-18 budget and a \$5.2 million (2.7 percent) growth from FY 2017-18 as projected in the Nine Month Report. FY 2019-20 local sales tax is budgeted at \$198.8 million, which is \$2.0 million (1.0 percent) higher than the proposed FY 2018-19 budget. Local sales tax is projected to grow at a much slower pace than previously anticipated due to continued declines in sales of general consumer goods and declines in receipts from the business sector. The budget assumes no changes to state and federal law affecting sales tax reporting for online retailers.

Exhibit 1-6. Actual and Projected Change in Sales Tax Revenues for San Francisco, 2005-2020



6. Hotel Tax

For the General Fund, FY 2018-19 hotel tax revenue is budgeted at \$375.8 million, which is \$3.5 million (0.9 percent) more than budgeted in FY 2017-18 and projected for FY 2017-18 in the Nine Month Report. The FY 2019-20 General Fund share of hotel tax revenue is budgeted at \$372.1 million, which is \$3.7 million (1.0 percent) less than budgeted in FY 2018-19.

For all funds, FY 2018-19 hotel tax revenue is budgeted at \$391.9 million, which is \$19.6 million (5.3 percent) more than budgeted in FY 2017-18 and projected for FY 2017-18 in the Nine Month Report. FY 2019-20 hotel tax revenue is budgeted at \$405.3 million across all funds, which is \$13.4 million (3.4 percent) more than budgeted in FY 2018-19.

Budgeted hotel tax levels assume the passage of a November 2018 ballot initiative which would, if approved, dedicate a portion of hotel tax proceeds to arts programs rather than to general purposes effective January 1, 2019. It would be in effect for the second half of FY 2018-19 and the entirety of FY 2019-20. As a result, despite the projected increase in total hotel tax revenue, the General Fund portion of hotel tax is projected to decline in FY 2019-20.

Hotel tax revenue growth is a function of changes in occupancy, average daily room rates (ADR) and room supply, measured in the aggregate as Revenue per Available Room (RevPAR). Exhibit 1-7 shows a recent history of RevPAR levels. During the first eight months of FY 2017-18 average RevPAR fell by 1.7 percent over the same period prior year, as four of the first eight months saw negative year-over-year RevPAR change. Between FY 2010-11 and FY 2014-15, RevPAR saw annual double-digit growth. In FY 2015-16 RevPAR began to slow, growing by 7.1%. FY 2016-17 was the first year since FY 2009-2010 that RevPAR declined. This was due to a combination of flattening or falling average daily room rates and the closure of Moscone Center in the latter part of the fiscal year, which impacted demand for hotel rooms. Despite some weakness in the first eight months of FY 2017-18, RevPar is expected to grow in the last part of the year, reflecting the reopening of the Moscone Center.

Exhibit 1-7. Revenue Per Available Room (RevPAR): FY 2010-11 to FY 2017-18

											Change - Change -	
	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14	FY 2014-15	FY 2015-16	FY 2016-17	FY 2017-18	\$	%		
July	\$ 141	\$ 171	\$ 188	\$ 208	\$ 233	\$ 248	\$ 240	\$ 249	\$ 9.26		4%	
August	\$ 154	\$ 173	\$ 196	\$ 230	\$ 261	\$ 260	\$ 250	\$ 251	\$ 1.76		1%	
September	\$ 166	\$ 189	\$ 212	\$ 242	\$ 269	\$ 280	\$ 273	\$ 256	\$ (16.71)		-6%	
October	\$ 174	\$ 205	\$ 229	\$ 251	\$ 274	\$ 288	\$ 282	\$ 271	\$ (11.10)		-4%	
November	\$ 112	\$ 152	\$ 152	\$ 195	\$ 190	\$ 206	\$ 196	\$ 223	\$ 27.49		14%	
December	\$ 106	\$ 109	\$ 128	\$ 145	\$ 190	\$ 160	\$ 179	\$ 157	\$ (21.90)		-12%	
January	\$ 124	\$ 135	\$ 148	\$ 176	\$ 209	\$ 237	\$ 252	\$ 272	\$ 20.38		8%	
February	\$ 136	\$ 156	\$ 153	\$ 187	\$ 186	\$ 260	\$ 230	\$ 189	\$ (41.41)		-18%	
March	\$ 136	\$ 148	\$ 166	\$ 188	\$ 230	\$ 238	\$ 222					
April	\$ 131	\$ 147	\$ 198	\$ 207	\$ 227	\$ 216	\$ 208					
May	\$ 165	\$ 170	\$ 190	\$ 216	\$ 231	\$ 250	\$ 222					
June	\$ 157	\$ 195	\$ 210	\$ 234	\$ 251	\$ 275	\$ 229					
Average YTD	\$ 141.71	\$ 162.47	\$ 180.73	\$ 206.52	\$ 226.98	\$ 243.10	\$ 231.74	\$ 233.57	\$ (4.03)		-1.7%	
\$ Change from PY	\$ 18.55	\$ 20.76	\$ 18.26	\$ 25.79	\$ 20.46	\$ 16.11	\$ (11.36)	\$ 1.82				
% Change from PY	15.1%	14.6%	11.2%	14.3%	9.9%	7.1%	-4.7%	0.8%				

San Francisco is currently involved in litigation with online travel companies regarding the companies' duty to remit hotel taxes on the difference between the wholesale and retail prices paid for hotel rooms. The Court of Appeal has ruled in favor of the online travel companies, and San Francisco is seeking review of that decision by the California Supreme Court. Final year-end revenue will be either greater or less than our projection depending on developments with this lawsuit.

7. Utility Users Tax

FY 2018-19 Utility Users Tax revenue is budgeted at \$99.1 million, which is \$0.6 million (0.6 percent) less than what was budgeted in FY 2017-18 and \$1.1 million (1.1%) more than projected in the FY 2017-18 Nine Month Report. FY 2019-20 Utility Users Tax revenue is budgeted at \$99.9 million, which is an additional \$0.8 million (0.9 percent) higher than the proposed FY 2018-19 budget. The budget assumes that moderate natural gas prices will continue, leading to tepid growth in gas, electric, and steam user tax revenue. Utility users tax includes prepaid mobile telephony services surcharge due to the passage of AB 1717.

8. Parking Tax

Parking tax revenue is budgeted at \$85.5 million in FY 2018-19, an increase of \$3.4 million (4.1 percent) over the FY 2017-18 budget, and no change from the FY 2017-18 Nine Month Report projection. In FY 2019-20, parking tax revenue is budgeted at \$85.5 million, which represents no change from the FY 2018-19 budgeted amount. Although parking tax revenue has historically been correlated with business activity and employment, this tax has experienced a decline since FY 2015-16, due to increased ride-sharing and decreased number of parking spaces related to Central Subway and other construction. The budgeted increase in FY 2018-19 is due to improved revenue control equipment and processes that began in FY 2017-18. Parking tax revenues are deposited into the General Fund, from which an amount equivalent to 80 percent is transferred to the San Francisco Municipal Transportation Agency for public transit as mandated by Charter Section 16.110.

9. Real Property Transfer Tax

Real property transfer tax (RPTT) revenue is budgeted at \$228.0 million in FY 2018-19, which is \$72.0 million (24.0 percent) less than the FY 2017-18 budget and a reduction of \$29.0 million (11.3 percent) from the FY 2017-18 Nine Month report projection. In FY 2019-20, RPTT revenue is

budgeted at \$228.0 million, which represents no change from the FY 2018-19 budget. The budget assumes continued constricted supply of commercial properties on the market. Considering the highly volatile nature of this revenue source, the Controller’s Office monitors collection rates throughout the fiscal year and provides regular updates to the Mayor and the Board of Supervisors. In November 2016 voters approved Prop W, which increased RPTT rates beginning in December 2016. The Prop W rate increase is projected to account for \$26.3 million of the \$228.0 million budgeted in FY 2018-19 and FY 2019-20.

Exhibit 1-8 shows revenue collections beginning in FY 2000-01. Since FY 2008-09, RPTT has been trending upward. However, as our most volatile revenue source, collections can see large year-over-year changes that have exceeded 70% in some instances. The main factors creating volatility are sales of high-value properties, which track well with economic cycles, as well as voter-approved rate changes, which occurred in 2008, 2010 and 2016.

Exhibit 1-8. Historical Real Property Transfer Tax Revenue (\$ millions), FY 2000-01 through FY 2019-20

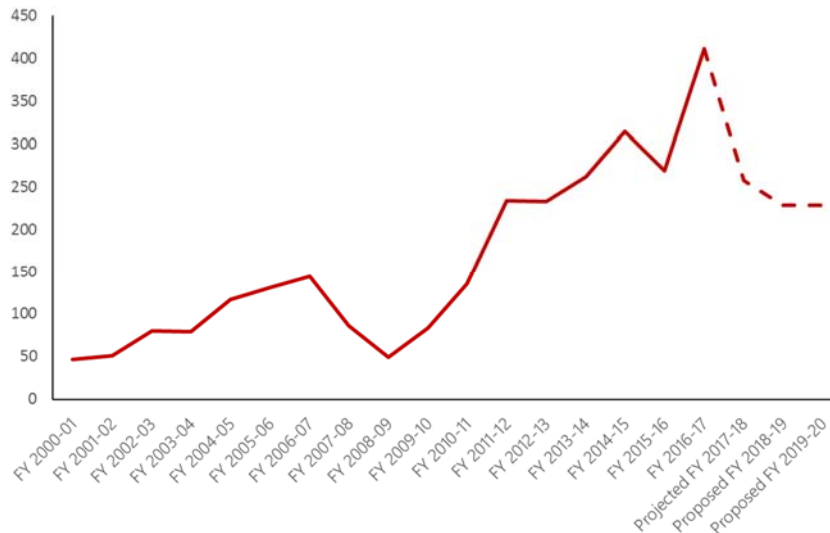
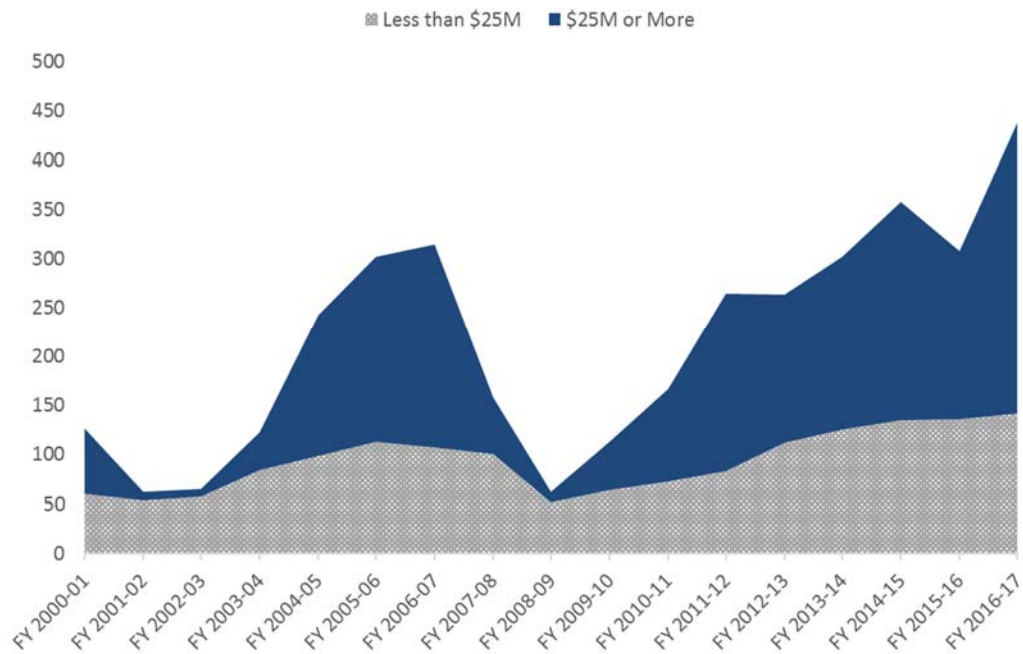


Exhibit 1-9 shows historical RPTT revenue by transaction size after being adjusted to reflect rate changes from Prop W (November 2016), Prop N (November 2010), and Prop N (November 2008). This exhibit demonstrates how the volatility of RPTT as revenue source is due mainly to the sales of high-value (largely commercial) properties over \$25 million. In FY 2008-09, transactions above \$25 million would have generated only \$10.6 million under the current rates compared to the peak in FY 2014-15, when these transactions generated \$222.2 million. Since the end of the recession in FY 2009-10, these large transactions made up on average 49.0 percent of total revenue but only 0.5 percent of the transaction count. This means that revenue is determined by a small handful of transactions.

Exhibit 1-9. Real Property Transfer Tax Rate-Adjusted Revenue by Transaction Size, FY 2000-21 through FY 2016-17 (\$ millions)



Deposits to the Budget Stabilization Reserve are funded with a portion of volatile revenues, including 75 percent of RPTT revenue in excess of the prior five-year average adjusted for any rate increases during the period. No deposits are expected during FY 2018-19 or FY 2019-20 as RPTT revenue is projected to be below the prior five-year average. See Appendix 2 for more detail on the Budget Stabilization Reserve.

10. Stadium Admissions Tax

FY 2018-19 stadium admissions tax revenue is budgeted at \$1.2 million, \$0.2 million (11.8 percent) less than the FY 2017-18 budget and no change from the FY 2017-18 Nine Month report projection. In FY 2019-20, revenue is budgeted at \$5.5 million, a \$4.3 million (358.3 percent) increase from the FY 2018-19 budget, due to the anticipated opening of the Chase Center, a multi-purpose arena that will be the home of the Golden State Warriors, in Fall 2019.

11. Sugar Sweetened Beverage Tax

In November 2016, voters adopted Proposition V, an initiative to tax sugar sweetened beverages by one cent per ounce, beginning on January 1, 2018. This new tax is expected to generate \$15.0 million in FY 2018-19 and FY 2019-20. As with all General Fund revenues, these figures reflect values before mandated contributions to baselines and reserves.

12. Access Line Tax

FY 2018-19 Access Line Tax revenue is budgeted at \$51.9 million, which is \$2.3 million (4.7 percent) more than what was budgeted in FY 2017-18 and \$0.1 million (0.3 percent) less than projected in the FY 2017-18 Nine Month Report. FY 2019-20 Access Line Tax revenue is budgeted at \$53.5 million, which is an additional \$1.7 million (3.2 percent) higher than the proposed FY 2018-19 budget. The budget reflects a proposed inflationary increase to the Access Line Tax rate of 2.94 percent as required under Business and Tax Regulations Code Section 784.

13. Interest & Investment Income

Interest and investment income for FY 2018-19 is budgeted at \$27.3 million, an increase of \$9.1 million (50.0 percent) from the FY 2017-18 budget and \$0.3 million (1.0 percent) from the Nine Month Report projection. FY 2019-20 revenue is budgeted at \$27.5 million, \$0.3 million (1.0 percent) more than budgeted in FY 2018-19. This increase is a result of the City's strong cash position, higher than expected interest rates during FY 2017-18, and continued expected interest rate increases through FY 2018-19 and FY 2019-20.

14. Intergovernmental – Federal

Federal support in the General Fund is budgeted at \$278.8 million for FY 2018-19, which represents growth of \$14.8 million (5.6 percent) from the FY 2017-18 budget and \$24.2 million (9.5 percent) from the FY 2017-18 Nine Month Report projection. FY 2019-20 revenue is budgeted at \$284.7 million, which is \$5.9 million (2.1 percent) more than the proposed FY 2018-19 budget.

FY 2018-19 growth includes a \$5.4 million increase related to prior year federal revenue adjustments and a \$7.0 million increase in federal In-Home Supportive Services funding. This increase in IHSS federal funding is more than offset by the shift in costs at the State level.

15. Intergovernmental – State – Public Safety Sales Tax

Public safety sales tax revenue is budgeted at \$104.7 million in FY 2018-19, an increase of \$3.0 million (3.0 percent) from the FY 2017-18 budget and an increase of \$1.0 million (1.0 percent) from FY 2017-18 as projected in the Nine Month Report. FY 2019-20 revenue is budgeted at \$106.2 million, which is \$1.6 million (1.5 percent) more than the proposed FY 2018-19 budget. This revenue is allocated to counties by the State separately from the local one-percent sales tax discussed above, and is used in San Francisco to fund police and fire services. Disbursements are made to counties based on the County Ratio, which is the county's percent share of total statewide sales taxes in the most recent calendar year. The county ratio for San Francisco in FY 2016-17 is 2.99 percent and is expected to decline slightly to 2.86 percent in FY 2018-19 and FY 2019-20. This decline is offset by expected increases in statewide sales tax receipts.

16. Intergovernmental – State – 1991 Health & Welfare Realignment

In FY 2018-19, the General Fund share of 1991 realignment revenue is budgeted at \$209.1 million, or \$20.4 million (10.8 percent) more than the FY 2017-18 budget and \$10.8 million (6.1 percent) more than the Nine Month Report projection. The FY 2017-18 revenue is budgeted at \$215.5 million, which is \$6.4 million (3.1 percent) more than the proposed FY 2018-19 budget. These changes are attributable to projected distributions from state sales tax and Vehicle License Fees, which are anticipated to be directed toward social service caseload growth payments.

Since FY 2014-15, the State has assumed savings from counties from treating fewer uninsured patients as a result of Affordable Care Act implementation and redirected these savings from realignment allocations to cover CalWORKs expenditures previously paid for by the State's General Fund ("AB 85 Redirection"). For San Francisco, there is a \$12.0 reduction assumed to the City's realignment allocation in FY 2018-19 and no reduction assumed in FY 2019-20.

17. Intergovernmental – State – Public Safety Realignment

Public Safety Realignment (AB 109), enacted in early 2011, transfers responsibility for supervising certain kinds of felony offenders and state prison parolees from state prisons and parole agents to county jails and probation officers. This revenue is budgeted at \$39.0 million in FY 2018-19, a \$2.3 million (5.6 percent) decrease from the FY 2017-18 budget and \$1.2 million (3.1 percent) more

than FY 2017-18 as projected in the Nine Month Report. The FY 2019-20 proposed budget assumes a \$1.2 million (3.1 percent) increase from FY 2018-19. This reflects the assumption that State sales tax revenues are projected to grow moderately over the next two years.

18. Intergovernmental – State – Other

Other State funding is budgeted at \$408.3 million in FY 2018-19, a decrease of \$12.0 million (2.9 percent) from the FY 2017-18 budget, or \$2.1 million (0.5 percent) less than the Nine Month Report projection. In FY 2018-19 other State funding is budgeted at \$413.8 million, an increase of \$5.5 million (1.4 percent) from FY 2018-19. The decrease in FY 2018-19 is attributable to a \$13.6 million decrease from the State of California's Whole Person Care pilot, for which two years of revenue were budgeted in FY 2017-18; a decrease of \$11.3 million in State alcohol funds; a decrease of \$7.5 million related to IHSS Administration; and a decrease of \$3.9 million in Food Stamp revenue. These decreases are partially offset by increases of \$11.3 million in community mental health services funding; \$2.8 million in IHSS Public Authority funding; \$2.6 million in Short-Doyle Medi-Cal funds; \$2.1 million in State Health Care Initiative Revenue; and \$2.8 million of Child Welfare Services funding.

19. Intergovernmental – Other

Other intergovernmental funding is budgeted at \$12.2 million in FY 2018-19, an increase of \$8.9 million (271.0 percent) from the FY 2017-18 budget. In FY 2019-20 other intergovernmental funding is budgeted at \$2.5 million, a decrease of \$9.7 million (79.8 percent) from FY 2018-19. The large increase in FY 2018-19 and subsequent decrease in FY 2019-20 is largely due to a \$9.6 million one-time payment from the Office of Community Investment and Infrastructure (OCII) to the City to fund the Mission Bay Ferry Terminal at the Port.

20. Charges for Services

The proposed budget assumes charges for services revenue of \$248.4 million in FY 2018-19, which represents growth from the FY 2017-18 original budget of \$15.5 million (6.7 percent), and a \$21.6 million (9.5 percent) decrease from the FY 2017-18 Nine Month Report projection. The proposed budget assumes charges for services revenue of \$234.9 million in FY 2019-20, which represents a decrease from FY 2018-19 of \$13.6 million (5.5 percent). The growth in FY 2018-19 and subsequent decrease in FY 2019-20 is primarily due to a \$12.0 million one-time Medi-Cal State Plan Amendment (SPA) allocation for mental health services budgeted in FY 2018-19.

21. Other Revenues

The proposed budget assumes revenues from other sources of \$41.1 million in FY 2018-19, an increase of \$1.1 million (2.7 percent) from the FY 2017-18 budget. FY 2019-20 revenue from other sources is budgeted at \$41.4 million, an increase of \$0.2 million (0.5 percent). These changes are primarily related to increased developer exactions.

22. Operating Transfers In

The proposed budget assumes operating transfers in of \$172.2 million in FY 2018-19, a change of \$1.0 million (0.6 percent) from the FY 2017-18 budget. In FY 2019-20 operating transfers in are budgeted at \$156.2 million, a decrease of \$16.0 million (9.3 percent) from FY 2018-19. The decrease in FY 2019-20 is primarily due to the loss of a one-time transfer of \$21.0 million of surplus revenues from The Zuckerberg San Francisco General Hospital (ZSFG) to the Electronic Health Records project in FY 2018-19 in the General Fund and a decrease of \$6.0 million to make intergovernmental payments.

Appendix 2. General Fund Reserve Uses and Deposits

As discussed in Appendix 1, the Mayor's proposed budget includes the use of \$61.6 million from reserves established in prior years during FY 2018-19 and \$1.6 million during FY 2019-20. As shown in Exhibit 2-1 below, the Mayor's proposed budget also includes \$58.7 million and \$42.7 million in deposits to General Fund reserves during FY 2018-19 and FY 2019-20, respectively. These appear to be prudent and reflect anticipated Memoranda of Understanding (MOU), litigation, and general contingency reserve requirements.

Exhibit 2-1. Proposed General Fund Reserve Uses and Deposits (\$ millions)

	FY 2017-18		FY 2018-19		FY 2019-20		Projected Ending Balance	Note
	Projected Ending Balance	Budgeted Deposits	Projected Withdrawals	Projected Ending Balance	Budgeted Deposits	Projected Withdrawals		
General Reserve	\$ 106.9	\$ 20.4	\$ -	\$ 127.3	\$ 14.2	\$ -	\$ 141.5	1
Rainy Day Economic Stabilization City Reserve	78.3	-	-	78.3	-	-	78.3	2
Rainy Day One-Time Reserve	47.4	-	-	47.4	-	-	47.4	2
Budget Stabilization Reserve	323.2	-	-	323.2	-	-	323.2	3
Subtotal Economic Stabilization Reserves	\$ 448.9	\$ -	\$ -	\$ 448.9	\$ -	\$ -	\$ 448.9	
Percent of General Fund Revenues	9.2%			8.8%			8.7%	
Budget Savings Incentive Fund	72.5	-	-	72.5	-	-	72.5	4
Litigation Reserve	-	11.0	(11.0)	-	11.0	(11.0)	-	5
Rainy Day Economic Stabilization SFUSD Reserve	44.2	-	-	44.2	-	-	44.2	2
Recreation & Parks Savings Incentive Reserve	0.9	-	(0.9)	-	-	-	-	6
Recreation & Parks Union Square Revenue Stabilization	6.2	-	(4.6)	1.6	-	(1.6)	-	6
Reserve for Technical Adjustments	-	2.5	(2.5)	-	2.5	(2.5)	-	7
Salary and Benefits Reserve	-	24.8	(24.8)	-	15.0	(15.0)	-	8
Affordable Care Act Contingency Reserve	50.0	-	-	50.0	-	-	50.0	9
State and Federal Revenue Risk Reserve	-	-	-	40.0	-	-	40.0	10
Labor Cost Contingency Reserve	-	-	-	70.0	-	-	70.0	11
Public Health Management Reserve	109.4	-	(73.3)	36.1	-	-	36.1	12
Total, All Reserves	\$ 839.0	\$ 58.7	\$ (117.1)	\$ 890.6	\$ 42.7	\$ (30.1)	\$ 903.2	

NOTES

1. General Reserve

The General Reserve, established in Administrative Code Section 10.60, is intended to address revenue and expenditure issues not anticipated during budget development, and is typically used to fund supplemental appropriations or to offset significant revenue losses following the adoption of the budget.

The policy requires the General Reserve to increase to 2.5 percent of budgeted General Fund regular revenues in FY 2018-19 and 2.75 percent in FY 2019-20. The General Reserve will continue to increase each year until it reaches 3.0 percent of budgeted General Fund regular revenues in FY 2020-21, with unused General Reserve carried forward from the prior year into the new budget year. In FY 2018-19, the Mayor's proposed budget anticipates \$20.4 million in deposits and projects an ending General Reserve balance of \$127.3 million. In FY 2019-20, the proposed budget anticipates \$14.2 million in deposits with an ending balance of \$141.5 million.

2. Rainy Day Reserves

Rainy Day Reserve balances are comprised of three separate reserves: Rainy Day Economic Stabilization Reserve - City Reserve, Rainy Day Economic Stabilization Reserve - School Reserve, and the Rainy Day One-Time Reserve. No deposits or uses of these reserves are budgeted in FY 2018-19 or FY 2019-20.

3. Budget Stabilization Reserve

Established by Administrative Code Section 10.60(c), the Budget Stabilization Reserve augments the Rainy Day Reserve. These two reserves are available to support the City's budget in years when revenues decline. The Budget Stabilization Reserve is funded by the deposit each year of 75 percent of three volatile revenue sources: real property transfer tax revenue above the prior five-year average (adjusted for rate changes), ending unassigned fund balance above what is appropriated as a source in the subsequent year's budget, and certain asset sales. Transfer tax revenues in FY 2018-19 and FY 2019-20 are not projected to exceed the prior five-year average and therefore no reserve deposit is budgeted. The Controller's Office will determine final deposits in September of each year based on actual receipts during the prior fiscal year.

4. Budget Savings Incentive Fund

The Citywide Budget Savings Incentive Fund is authorized by Administrative Code Section 10.20. No deposits or withdrawals in this fund are budgeted for FY 2018-19 or FY 2019-20.

5. Litigation Reserve

The Mayor's proposed budget includes \$11.0 million for the litigation reserve in both FY 2018-19 and FY 2019-20. The reserve provides funding for potential judgments and claims that will be paid out during the budget period based on historical experience. The City also maintains a separate reserve funded from prior year appropriations for large cases pending against the City. The proposed level of funding is consistent with the level recommended in the City's Five Year Financial Plan.

6. Recreation & Parks Reserves

The Recreation and Park Savings Incentive Reserve is established by Charter Section 16.107(c) and prior to Proposition B, passed by the voters on June 7, 2016, was funded by the retention of year-end net expenditure savings and revenue surplus from the Recreation and Park Department. Proposition B eliminated the ability to retain expenditure savings while preserving deposits from surplus revenue. Any withdrawals from the reserve must go towards one-time expenditures. The Union Square Garage Revenue Stabilization Fund is a reserve of one-time revenue received by the Recreation and Park Department to replace net garage revenues lost due to the construction of the Union Square Market Street Central Subway Station. The proposed budget assumes depletion of both reserves.

7. Reserve for Technical Adjustments

Reserves of \$2.5 million in FY 2018-19 and FY 2019-20 in the proposed budget allow for technical adjustments during the budget review process. The Mayor's Office will inform the Budget and Finance Committee prior to the final Committee vote on the budget as to the amount required for technical adjustments up to that point and any balance that may be available for other uses.

8. Salary & Benefits Reserve

The Mayor's proposed budget provides \$24.8 million in FY 2018-19 and \$15.0 million in FY 2019-20 to cover costs related to adopted MOUs with labor organizations, including cost associated with one additional weekend day of operation in FY 2018-19.

9. Affordable Care Act Contingency Reserve

The FY 2017-18 budget assigned \$50.0 million of unappropriated fund balance to a budget contingency reserve in the Zuckerberg San Francisco General Hospital Operating Fund for the purpose of managing cost and revenue uncertainty related to federal and state changes to the administration and funding of the Affordable Care Act. There are no anticipated deposits or withdrawals to this reserve.

10. State and Federal Revenue Risk Reserve

The Mayor's proposed budget assigns \$40.0 million of unappropriated fund balance from FY 2017-18 to a contingency reserve for the purpose of managing state, federal, and other revenue uncertainty during the term of the proposed budget.

11. Labor Cost Contingency Reserve

The Mayor's proposed budget assigns \$70.0 million of unappropriated fund balance from FY 2017-18 to a contingency reserve for the purpose of managing costs related to wage and salary provisions negotiated in the City's labor contracts in FY 2019-20, and to manage volatility in employee health and pension benefit costs.

12. Public Health Revenue Reserve

The Public Health Management Reserve is authorized under Section 12.6 of the administrative provisions of the Annual Appropriation Ordinance, authorizing the Controller to defer surplus transfer payments, indigent health revenues, and Realignment funding to offset future reductions of audit adjustments associated with the Affordable Care Act and funding allocations for indigent health services. This provision was adopted by the Board of Supervisors to smooth volatile state and federal revenues that can lead to large variances between budgeted and actual amounts due to unpredictable timing of payments, major changes in projected allocations, and delays in final audit settlements. The FY 2017-18 ending balance of the reserve is projected to be \$109.4 million, as reported in the Nine Month Report. In FY 2018-19, \$73.3 million of withdrawals are anticipated, including the \$56.0 million budgeted into the Laguna Honda Debt Service Fund to repay the State for federally disallowed prior year payments under SB 1128. Eligible uses include the potential liability of disallowed SB 1128 reimbursement, reductions to supplemental payments for Medi-Cal services, and greater budgeted withholding of 1991 health and welfare realignment subventions.

Appendix 3. One-time Sources and Nonrecurring Revenue Policy

The use of one-time or nonrecurring sources to support ongoing operations creates a future budget shortfall, requiring expenditures to be reduced or replacement resources identified. In December 2011, the Board approved a Nonrecurring Revenue Policy, codified in Administrative Code Section 10.61, which requires selected nonrecurring revenues to be used only for identified nonrecurring expenditures. The Controller is required to certify compliance with this policy. The selected revenues include:

- General Fund prior year-end unassigned fund balance, before reserve deposits, above the prior five-year average;
- The General Fund share of revenues from prepayments provided under long-term leases, concessions, or contracts after accounting for any Charter-mandated revenue transfers, set-asides, or deposits to reserves;
- Otherwise unrestricted revenues from legal judgments and settlements; and
- Otherwise unrestricted revenues from the sale of land or other fixed assets.

Controller's Certification

General Fund prior year-end unassigned fund balance is budgeted at \$190.9 million for FY 2018-19 and \$213.0 million for FY 2019-20. These amounts fall below the prior five-year average of year-ending CAFR fund balances, estimated through FY 2016-17 to be \$435.2 million. There are no other nonrecurring revenues that fall within the policy. As shown in Exhibit 3-1, in each of the two fiscal years, budgeted nonrecurring expenditures exceed this amount; therefore, the Controller's Office certifies compliance with the policy.

Exhibit 3.1. General Fund Nonrecurring Sources & Uses (\$ millions)

	FY 2018-19 Proposed	FY 2019-20 Proposed	Total
ONE-TIME SOURCES			
General Fund Prior Year Fund Balance	\$ 190.9	\$ 213.0	\$ 403.9
Total Nonrecurring General Fund Revenues	\$ 190.9	\$ 213.0	\$ 403.9
ONE-TIME USES			
Capital Planning GF Recommended Funding	\$ 147.0	\$ 157.0	\$ 304.0
COIT Annual & Major IT Projects	33.8	28.6	62.4
DPH - FF&E & Moving Costs	11.2	11.0	22.2
Other - FF&E & Moving Costs	10.5	9.6	20.1
Equipment	16.1	10.7	26.8
Non-Profit Stabilization Fund	4.0	3.0	7.0
Total One-Time Uses	\$ 222.6	\$ 219.9	\$ 442.5

Appendix 4. Baselines & Mandated Funding Requirements

Voters have approved baseline levels of funding or staffing. The mandates summarized below in Exhibit 4-1 reflect binding Charter requirements. The exhibit does not reflect non-binding ordinance measures such as the Neighborhood Firehouse, Treatment on Demand, and Office of Economic Analysis staffing baselines.

Exhibit 4-1. Baselines & Mandated Funding / Staffing Requirements (\$ millions)

	FY 2017-18 Original Budget	FY 2018-19 Proposed Budget	FY 2019-20 Proposed Budget	Note
<i>General Fund Aggregate Discretionary Revenue (ADR)</i>	\$ 3,411.3	\$ 3,659.0	\$ 3,719.7	
Financial Baselines				
Municipal Transportation Agency (MTA)				
MTA - Municipal Railway Baseline: 6.686% ADR	235.0	244.6	252.2	
MTA - Parking & Traffic Baseline: 2.507% ADR	85.5	91.7	93.3	
MTA - Population Adjustment	39.1	50.9	55.4	
MTA - 80% Parking Tax In-Lieu	65.7	68.4	68.4	
Subtotal Municipal Transportation Agency	\$ 425.4	\$ 455.7	\$ 469.2	1
Library Preservation Fund				
Library - Baseline: 2.286% ADR	78.0	83.6	85.0	2
Library - Property Tax: \$0.025 per \$100 Net Assessed Valuation (NAV)	57.6	63.6	63.9	3
Subtotal Library	135.6	147.2	148.9	
Children's Services				
<i>Children's Services Baseline - Requirement: 4.830% ADR</i>	<i>164.8</i>	<i>176.7</i>	<i>179.7</i>	4
Children's Services Baseline - Eligible Items Budgeted	171.3	182.2	184.5	4
<i>Transitional Aged Youth Baseline - Requirement: 0.580% ADR</i>	<i>19.8</i>	<i>21.2</i>	<i>21.6</i>	5
Transitional Aged Youth Baseline - Eligible Items Budgeted	27.2	28.1	28.8	5
Public Education Services Baseline: 0.290% ADR	9.9	10.6	10.8	6
Children and Youth Fund Property Tax Set-Aside: \$0.0375-0.4 per \$100 NAV	86.4	101.7	102.2	3
<i>Public Education Enrichment Fund: 3.057% ADR</i>	<i>104.3</i>	<i>111.9</i>	<i>113.7</i>	7
1/3 Annual Contribution to Preschool for All	34.8	37.3	37.9	
2/3 Annual Contribution to SF Unified School District	69.5	74.6	75.8	
Subtotal Childrens Services	399.0	434.5	440.0	
Recreation and Parks				
Open Space Property Tax Set-Aside: \$0.025 per \$100 NAV	57.6	63.6	63.9	3
<i>Recreation & Parks Baseline - Requirement</i>	<i>70.2</i>	<i>73.2</i>	<i>76.2</i>	8
Recreation & Parks Baseline - Budgeted	73.4	75.5	77.5	8
Subtotal Recreation and Parks	131.0	139.1	141.3	
Other Financial Baselines				
Housing Trust Fund	31.2	34.0	36.8	9
Dignity Fund	44.1	47.1	50.1	10
Street Tree Maintenance Fund	19.0	19.8	20.1	11
Homelessness and Supportive Housing Fund	17.6	17.6	17.6	12
Municipal Symphony Baseline: \$0.00125 per \$100 NAV	2.9	3.2	3.4	13
City Services Auditor: 0.2% of Citywide Budget	17.4	19.1	19.0	14
Subtotal Other Financial Baselines	394.2	419.1	429.7	
Total Financial Baselines	\$ 1,354.2	\$ 1,456.5	\$ 1,487.7	
Staffing and Service-Driven Baselines				
Police Minimum Staffing		Requirement met		15

NOTES

1. Municipal Transportation Agency (MTA) Baselines

Charter section 8A.105 established a Municipal Transportation Fund to provide a predictable, stable and adequate level of funding for the MTA. Consistent with the Charter, in FY 2000-01 a base amount of funding was established. Charter subsection (c) (1) requires the Controller's Office to adjust the base amount from year to year by the percent increase or decrease in General Fund Aggregate Discretionary Revenues (ADR). This baseline is required to be adjusted for significant service increases. Beginning in FY 2019-20, the MTA baseline will increase due to operating costs required in advance of the opening of the Central Subway, which is expected to fully come online in FY 2021-22. Beginning in FY 2002-03, this Charter section also established a minimum level of funding (required baseline) for the Parking and Traffic Commission based upon FY 2001-02 appropriations. The Mayor's proposed budget includes funding for the MTA baselines at the required levels of \$336.4 million in FY 2018-19 and \$345.4 million in FY 2019-20.

Proposition B, passed by the voters in November 2014, requires that in addition to adjusting annually for the change in ADR, these baseline amounts be increased for 10 years of population growth in the City in FY 2015-16 and annual population growth thereafter. The Mayor's proposed budget includes \$50.9 million and \$55.4 million in FY 2018-19 and FY 2019-21 respectively, for the Proposition B population baseline. Finally, it reflects the allocation of an amount equivalent to 80 percent of parking tax revenue to the MTA, or \$68.4 million in FY 2018-19 and \$68.4 million in FY 2019-20.

2. Library Baseline

Charter Section 16.109 established a Library Preservation Fund to provide library services and to construct, maintain, and operate library facilities. Consistent with the Charter, in FY 2006-07 a base amount of funding was established, which is adjusted annually by the percent increase or decrease in ADR. Based on revenue in the Mayor's proposed budget, the Library Baseline requirements of \$83.6 million in FY 2018-19 and \$85.0 million in FY 2019-20 are met.

3. Property Tax-Related Set-Asides

Charter Sections 16.108, 16.109, and 16.107 mandate property tax-related set-asides for the Children and Youth Fund, the Library Preservation Fund, and the Open Space Fund. As discussed in the Property Tax section in Appendix 1, the allocation factor for the Children and Youth Fund will increase by \$0.0025 (from \$0.0375 to \$0.0400) on each \$100 valuation of taxable property in FY 2018-19. The Library Preservation Fund and the Open Space Fund receive allocations of \$0.025 for each \$100 valuation of taxable property in both FY 2018-19 and FY 2019-20. The Mayor's proposed budget includes required funding of \$101.7 million in FY 2018-19 and \$102.2 million in FY 2019-20 for the Children and Youth Fund, and \$63.6 million and \$63.9 million in FY 2018-19 and FY 2019-20, respectively, for both the Library Preservation Fund and Open Space Fund.

4. Children's Baseline

Charter Section 16.108 established a Children and Youth Services baseline. Consistent with the Charter, in FY 2000-01 a base amount of funding was established, which is adjusted annually by the percent increase or decrease in ADR. Proposition C, approved by voters in November 2014, amended the Charter to exclude medical health services as an eligible service. As a result, and as part of establishing the Disconnected Transitional-Aged Youth Baseline, the Controller

reviewed City appropriations included in the fund and excluded medical health services and other expenditures now mandated by state law. The Controller then recalculated City appropriations as a percentage of ADR to arrive at an adjusted baseline rate. The required Children's baselines for FY 2018-19 and FY 2019-20 are \$176.7 million and \$179.7 million, respectively. The Mayor's proposed budget includes Children's Baseline appropriations of \$182.2 million and \$184.5 million, which exceeds the minimum requirement by \$5.5 million in FY 2018-19 and \$4.9 million in FY 2019-20.

5. Disconnected Transitional-Aged Youth Baseline

Proposition C, approved by voters in November 2014, amended Charter Section 16.108 to increase the Children's Baseline to include services for Disconnected Transitional-Aged Youth (TAY), known as the TAY Baseline. The Charter requires that the TAY Baseline be added to the Children's Baseline, however, it is tracked separately for reporting purposes. The TAY Baseline amount was established in FY 2013-14 and like the Children's Baseline is adjusted annually by the percent increase or decrease in ADR. The required baselines for FY 2018-19 and FY 2019-20 are \$21.2 million and \$21.6 million, respectively. The Mayor's proposed budget includes TAY eligible baseline appropriations of \$28.1 million and \$28.8 million, which exceeds the minimum requirement by \$6.9 million in FY 2018-19 and \$7.2 million in FY 2019-20.

6. Public Education Services Baseline

Charter Section 16.123-2 established a Public Education Enrichment Fund. Consistent with the Charter, in FY 2001-02 a base amount of funding was established, which is adjusted annually by the percent increase or decrease in ADR. The Mayor's proposed budget includes the required \$10.6 million in FY 2018-19 and \$10.8 million in FY 2019-20 for this baseline.

7. Public Education Enrichment Fund Annual Contribution

In addition to the Public Education Services Baseline, Charter Section 16.123-2 requires the City to support education initiatives with annual contributions equal to the City's total contribution in the prior year, adjusted for the change in ADR. The proposed budget includes \$111.9 million and \$113.7 million for the Public Education Enrichment Fund Annual Contribution in FY 2018-19 and FY 2019-20, respectively. One third of the contribution supports the Preschool for All program at the Office of Early Childhood Education and two thirds of the contribution supports programming at the San Francisco Unified School District.

8. Recreation & Parks Baseline

In June 2016, voters approved Proposition B, a Charter amendment which created a new baseline funding requirement for parks, recreation, and open space. The Charter amendment requires an annual contribution from the General Fund to the Recreation and Parks Department that will increase by \$3.0 million per year for the next ten fiscal years, and then be adjusted at the same rate as the percentage increase or decrease in ADR. The amendment allows the City to suspend growth in baseline funding in years when the City forecasts a budget deficit of \$200 million or greater. The required baselines for FY 2018-19 and FY 2019-20 are \$73.2 million and \$76.2 million, respectively. The Mayor's proposed budget includes General Fund appropriations of \$75.5 million and \$77.5 million, which exceeds the minimum requirement by \$2.4 million in FY 2018-19 and \$1.3 million in FY 2019-20.

9. Housing Trust Fund

In 2012, voters approved Proposition C, establishing a Housing Trust Fund codified in Charter section 16.110. The Charter requires an annual contribution from the General Fund to the

Housing Trust Fund of \$20.0 million beginning in FY 2013-14 and increasing annually by \$2.8 million. The Mayor's proposed budget includes the required funding of \$34.0 million and \$36.8 million in FY 2018-19 and FY 2019-20, respectively.

10. Dignity Fund

In November 2016, voters approved Proposition I, establishing the Dignity Fund to support programming for seniors and adults with disabilities. Charter section 16.128-3 establishes a baseline contribution from the General Fund to the Dignity Fund of \$38.1 million beginning in FY 2016-17, increasing by \$6.0 million in FY 2017-18 and by \$3.0 million per year from FY 2018-19 through FY 2026-27. From FY 2027-28 and beyond, the baseline is adjusted at the same rate as the percentage increase or decrease in ADR. The Mayor's proposed budget includes the required funding of \$47.1 million and \$50.1 million in FY 2018-19 and FY 2019-20, respectively.

11. Street Tree Maintenance Fund

In November 2016, voters approved Proposition E, establishing the Street Tree Maintenance Fund to maintain the City's street trees. Charter section 16.129 establishes a baseline contribution from the General Fund to the Street Tree Maintenance Fund of \$19.0 million in FY 2017-18 and adjusted at the same rate as the percentage increase or decrease in ADR every year thereafter. The Mayor's proposed budget includes the required funding of \$19.8 million and \$20.1 million in FY 2018-19 and FY 2019-20, respectively.

12. Homelessness and Supportive Housing Fund

Also known as the Housing First Program, the Human Services Care Fund was passed by voters as Proposition N in November 2002. Administrative Code Section 10.100-77 defines a formula for calculating the annual required contribution to the Fund based on the number of homeless people expected to participate in County Adult Assistance Programs during each upcoming fiscal year as compared to a base year. The City is required to credit the Fund with the difference between the average annual maximum cash grant for each program and the average annual special allowance or other residual cash payment provided by the City for each participant to whom the City expects to provide in-kind benefits in lieu of the full cash grant during the year. These funds are to be used on housing and services programs. The Mayor's proposed budget includes funding of \$17.6 million in both FY 2018-19 and FY 2019-20. The budgeted amounts include \$2.6 million in FY 2018-19 and FY 2019-20 of General Fund support above the Care Fund revenues of \$15.1 million in both years.

13. Municipal Symphony Baseline

Charter Section 16.106(1) mandates that the City provide an appropriation equivalent to 1/8 of \$0.01 of each \$100 of assessed valuation of property tax for the San Francisco Municipal Symphony Orchestra. Based on budgeted assumptions of assessed valuation, the required funding for the Municipal Symphony Baseline is \$3.2 million in FY 2018-19 and \$3.4 million in FY 2019-20.

14. City Services Auditor Baseline

Charter Section F1.113, approved by voters through Proposition C in November 2003, established the Controller's Audit Fund with a baseline funding amount of 0.2 percent of the City budget to fund audits of City services. The Mayor's proposed budget includes \$19.1 million in FY 2018-19 and \$19.0 million in FY 2019-20 for the City Services Auditor baseline.

15. Police Minimum Staffing Baseline

San Francisco Charter Section 4.127, approved by the voters in 1994 as Proposition D, mandates a minimum police staffing baseline of not less than 1,971 sworn full-duty officers. Pursuant to Proposition C, passed by the voters in March 2004, the Charter-mandated minimum staffing level may be reduced in cases where civilian hires result in the return of full-duty officers to active police work through the budget process.

The Police Department projects that as of July 1, 2018 it will have 2,350 sworn officer positions filled, supplemented by 162 officers graduating from the academy to full duty and offset by 80 retirements or other separations during FY 2018-19. In addition to this net increase of approximately 80 officers, an academy class of 50 recruits will begin in FY 2018-19. Projected staffing levels will change throughout the course of the fiscal year due to the timing of police academy graduations and officer retirements. The department projects that 473 officers will be on leaves of absence, modified duty, assignment to the Airport, or in the academy. These adjustments result in a projected total of 1,959 full-duty sworn officers available for neighborhood policing and patrol by the end of FY 2018-19, which is below the minimum staffing level of 1,971 by 12 officers. However, the Controller's Office estimates that as of the start of FY 2018-19, 77 positions have been civilianized. Subject to certification by the Chief of Police, this would reduce the minimum staffing level to 1,894. Net of these civilianized positions, the number of full-duty sworn officers available for neighborhood policing and patrol, would be above the adjusted baseline by 65 officers in FY 2018-19.

In FY 2019-20, the Police Department is projected to have 123 officers graduating from the academy, offset by 80 retirements. In addition, the department projects that an additional 21 officers (for a total of 494 officers) will be on leaves of absence, modified duty, assignment to the Airport, or in the academy. These adjustments result increasing the number of full-duty sworn officers by 22 officers between FY 2018-19 and FY 2019-20. Full-duty sworn officers available for neighborhood policing and patrol, are projected to be 1,981 in FY 2019-20, which is above the adjusted minimum staffing level of 1,894 by 87 officers.