

To: Bob Muscat, Executive Director, IFPTE Local 21

From: Steven Raphael and Michael Stoll

Date: June 4, 2008

Regarding: Meeting with the City Controller's Office

This memo summarizes the contents (and main take home points) of our May 14th meeting with the City's controller's office. We also present a brief summary of our research pertaining to a few follow up questions that were raised following our meeting with the city.

We discussed a wide range of topics pertaining to the city's current and future financial position and the proposal by the city that city employees accept a wage freeze in exchange for no layoffs. We also reviewed the revised revenue and expenditure projections prior to the meeting and discussed the projections contained in the Mayor's proposed budget for the coming fiscal year. In previous work for local 21, we found that the one-year forward revenue projections contained in the Mayor's budget are correct on average (i.e., they aren't biased in one direction or another) and are usually within three percent of actual revenue totals. In our meeting with the Controller's office, the staff members were quite clear regarding their revenue projections and the sources of the projected increase in uses, and in turn, the coming fiscal crisis.

In follow-up conversations following our meeting, we decided that the most important points established are the following:

- (1) The projected budgetary shortfall based on current service levels is indeed real. The revenue projections are based on a projection series from the controller's office that in the past has proved to be unbiased and fairly accurate. The projected increase in uses is determined by past policy decisions and other externally imposed service constraints (such as minimum standards in the city's jail system).
- (2) The city informed us that a one percent increase in the salaries of local 21 members costs approximately \$4.1 million. Thus, foregoing a 3 percent wage increase would mean that local 21 members give up \$12.3 million in wage and salary increases. The city also notes that of the \$4.1 million needed to finance a one percent increase, only \$1.3 million is charged against the general fund (with the remaining \$2.8 million charged to the budgets of the various enterprises). Thus, if local 21 members were to agree to the concessions, the \$12.3 million in foregone salary increases would only close \$3.9 million of the general fund budget gap. The remaining \$8.5 million in salary savings would accrue to the enterprise funds, many of which have running budgetary surpluses.
- (3) The city also informed us that local 21 members who are not funded by general fund revenues are not subject to the layoff risk, with the possible exception of DBI, however, employees in enterprise departments may be subject to bumping.

- (4) At the meeting, we spent much time trying to identify the source of the large budget deficit projected for FY 08-09. In a nutshell, revenues for the coming year are healthy, but selective increases in spending are driving the projected shortfall. A large component of the deficit is being driven by the increase in labor costs, primarily by the annualization of the cost of new hires made in the current fiscal years – i.e., new hires hired for part of FY07-08 are anticipated to be employed for all of FY 08-09, requiring a higher budgeted level of funds. With the city, we did a few a back-of-the-envelope calculations that suggested that much of the excess budgetary demands in FY 08-09 are being driven by increased hiring in select occupations in the current fiscal year (primarily of police officers and nurses). We learned that these additional hires were driven by policy decisions by the Mayor’s office. These uses require continued funding for the budgeted part year FTE’s from the current fiscal year as well as the supplemental appropriation to cover the annualization of these positions. It seemed that the lion’s share of the budgetary deficit in the coming year is being driven by these relatively new hires, which cost an additional \$37.4 million in the FY 08-09 budget. As well, many of these newly hired FTEs are also subject to COLA and MOU increases, negotiated in previous years, and thus drive further additional personnel costs in the budget for FY 08-09.
- (5) We reviewed the revenue projections that will form the basis for the Mayor’s June budget and how these projections are likely to change relative to those presented in the March joint report (the three year budgetary projections). We have been informed that the projected revenues that will make it into the budget are likely to be slightly worse than the revenue projections included in the joint report. This worsening of the revenue projection is driven largely by larger than anticipated declines in real estate transfer tax revenues.
- (6) Finally, we spent quite a bit of time exploring possible alternatives to the proposed concessions. Among the ideas discussed were offering incentives for early retirement, increasing the recharge rates for enterprise funds that make use of general fund supported services, and thinking about how to capture the salary savings that would otherwise accrue to enterprise funds in the event of wage concessions (spreading the loss over a larger pool of workers). The folks from the city were generally unenthusiastic about all such ideas

Finally, the city committed to providing us with an updated analysis of how the May revise of the state budget impacts their budget projections for the coming fiscal year. We have yet to have this discussion but are following up with the controllers’ office.

Response to Local 21 Research Questions as a Follow-up to Meeting with CCSF Controller

Following the meeting with the CCSF Controller, Local 21 requested follow-up research on three issues contained in the nine-month budget report: (1) the projected decline of \$150 million in beginning-of-year fund balanced, (2) the current fund balances among

the city many enterprise funds, and (3) the source of the near \$20 million increase in jail spending.

1. Analysis of the \$150 million loss in from FY2007-2008 fund balances

The \$150 million in fund balances is the year-over-year projection of the change in the starting balance left over from the previous fiscal year that can be applied to the subsequent fiscal year. As of the date of the joint report, the controller's office estimated that revenues exceeded uses by \$124.6 million in FY 06-07. In addition, at the close of the last fiscal year Mayor Newsom de-appropriated \$33.1 million in funds that were previously appropriated towards a designated use, giving \$157.7 million from FY06-07 that could be appropriate in FY 07-08.

At the time of the joint report, the controller's office was projecting that at the close of the current fiscal year (FY07-08), revenues (inclusive of last year's year-end unspent balance) would exceed uses by approximately \$7.6 million. Thus, the statement regarding the loss of \$150 million for FY 08-09 is referring the juxtaposition of these two starting balances. At the beginning of the 07-08 fiscal year there was \$157.7 million left over from the previous fiscal year that could be appropriated for the current fiscal year. By contrast, they are projecting only a \$7.6 million surplus at the end of FY07-08. The difference between these two gives the negative \$150 million year-over-year change.

Note, the nine-month report shows an improvement in the projected year end surplus for FY07-08 relative to what was in the joint report. While the joint report projected a \$7.6 million surplus, the 9-month report projects a \$41.64 million surplus, for a change of \$34.02 million. With this update, the change in reserve balances from the beginning of FY07-08 to the beginning of FY08-09 should be revised from a negative \$150 million change to a negative change of \$115.98 million. This change in the projected surplus was accounted for in the summary worksheet provided to local 21 by the Mayor's budget director (this document was shared with us during our pre-meeting on May 14th).

2. Research on enterprise funds from the City's CAFR

We reviewed the information in the city's latest CAFR as well as the summary of the projected operating revenue and uses for the current fiscal year for the city's major enterprise fund operations (see Appendix E in the FY07-08 nine month report). The summary financial statements for FY07-08 show fund balances for each enterprise fund from the previous year, projected differences between budgeted and latest projected revenues, the projected differences between budget and latest projected uses, and the projected operating surplus/deficit for the current fiscal year. With the exception of

the PUC wastewater operating fund, all of the enterprise funds are running substantial net operating surpluses in the current fiscal year. In addition, nearly all began the fiscal year with a fund balance from the previous fiscal year. Thus, the projected deficits on the general fund for the coming fiscal year do not apply to the enterprise funds.

3. Question regarding the additional \$19.5 million for jail inmates

Absent detailed information on arrest trends and average spell length behind bars, it is difficult for us to assess this particular projected budget increase. We did however perform a media search on the topic pertaining to San Francisco and came up with the following information.

Since 2004 the average daily jail population has steadily increased. The determinants of the daily population of any city's jail system depends primarily on a hand full of factors: the city's arrest rate, the rate at which people are making bail, and the amount of time for the charge to be adjudicated for those who do not make bail. Most convicted felons are transferred out of the city's jails and into the state prison system so the adjudication time is particularly important in determining the average daily jail population.

With regards to what has happened in San Francisco, media reports indicate that the District Attorney's office has stepped up prosecutions and that arrests have increased in recent years. There are also several mentions of higher bail amounts and a gradual lengthening of the time between arrest and adjudication for those who do not make bail. All of these factors would serve to increase the daily population.

In addition, prior to an October 2007 court ruling, there are several mentions of the fact that many jail inmates in San Francisco jails slept on mattresses on the floor. Apparently, this practice was ruled to be unconstitutional, forcing the city to expand jail capacity in order to house the current population. There was a supplemental appropriation approved by the city budget committee to open a previously closed jail in San Bruno in April of 2008. The increase in the 9-month budget report is likely to reflect the annualization of the cost of permanently operating this additional facility. We placed a call in to the analyst in the controller's office with detailed knowledge on this issue, but have yet to receive a response.