

PICA Staff Report
on the
City of Philadelphia's
Quarterly City Manager's Report

Second Quarter of FY2007

Submitted to PICA on February 15, 2007

February 16, 2007

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Overview

The Quarterly Report projects that the City's fund balance will drop by \$82.8 million during FY07. Despite strong revenues, the fund balance is projected to fall because of the continuing rapid growth in the costs of employee healthcare, pensions, prisons and debt service.

As PICA has written in the past, unless those cost increases are contained, the City will lack the financial flexibility to attack crime, maintain other essential services, make its tax structure more competitive and make essential investments in its infrastructure.

While the projected \$172 million fund balance is lower than FY06's ending balance, it is about \$6 million higher than the amount projected for FY07 in the approved FY07-FY11 Plan.

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Projected General Fund Balance for FY2007
in Quarterly Report: **\$171.7M**

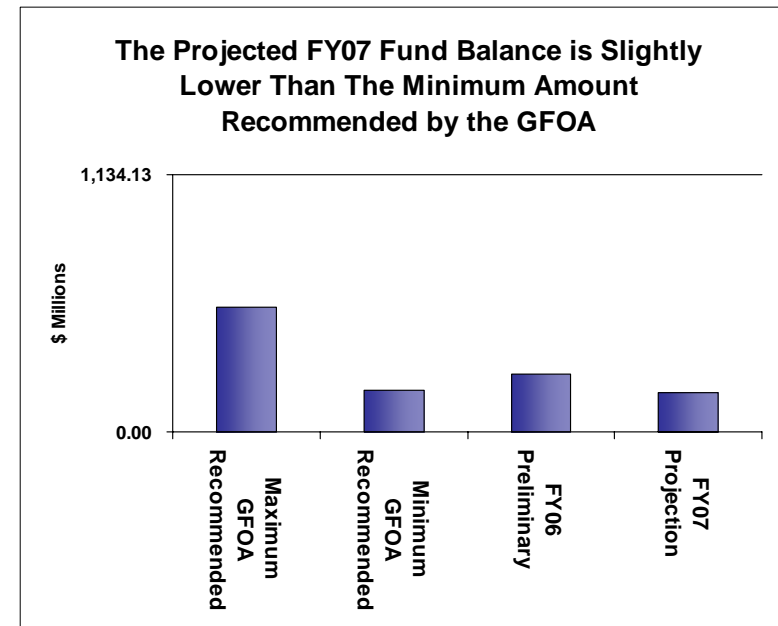
Projected General Fund Balance for FY2007
in the Plan: **\$166.1M**

Change in General Fund Balance from the Plan:
\$ 5.6M

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Fund Balance

- The projected FY07 fund balance is slightly lower than the minimum amount recommended by the Government Finance Officer's Association.
 - The GFOA recommends that fund balances be 5% -15% of revenues in order to provide contingencies against unexpected events during the year;
 - At \$172M, the City's projection is about \$11M lower than the minimum balance that the GFOA recommends and \$365M lower than the high end of the Association's guidelines.
- While the City's projected FY07 fund balance is close to the minimum level recommended by the GFOA, it almost certainly will fall further below that level in FY08 and the other years included in the Plan.



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Revenue Projections

Projected General Fund Revenues for FY2007
in Quarterly Report: **\$3,651.1M**

Projected General Fund Revenues for FY2007
in the Plan: **\$3,615.2M**

Change in General Fund Revenues from the Plan:
\$ 35.9M

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Obligations Projections

Projected General Fund Obligations for FY2007
in Quarterly Report: **\$ 3,753.9M**

Projected General Fund Obligations for FY2007
In the Plan: **\$ 3,668.7M**

Change in General Fund Obligations from the Plan:
\$ 85.2M

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Revenue Projections: Taxes

- Based on higher than anticipated FY06 tax collections and strong year-to-date collections, the Quarterly Report projects that taxes will exceed the amounts projected in the approved Plan.
- The report projects that wage, business privilege and real estate transfer tax collections will be a combined \$66.1 million higher than the amounts projected in the Plan.

<u>Tax</u>	<u>FY07 Plan</u>	<u>FY07 Quarterly Report</u>	<u>Change (in millions)</u>
Wage and Earnings	\$ 1,118.9	\$1.141.4	\$22.4
Business Privilege	\$ 378.9	\$408.0	\$29.1
Real Estate Transfer	\$ 195.0	\$210.0	\$15.0

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Revenue Projections: Local Non-Taxes

- The Quarterly Report projects receipt of the Eagles' \$8M rent in FY07. The rent was initially due in FY02, but is now the subject of a legal dispute between the Eagles and the City.
- The quarterly report projects that the City will receive \$6 million from the sale of City assets, but no revenue from a strategic marketing initiative. The strategic marketing initiative had been projected to generate \$2.5 million and the sale of assets was projected to produce \$10 million.
- The Quarterly Report increases the amount of projected revenue from emergency medical service fees by \$1.5 million based on year-to-date collections.

<u>Item</u>	<u>FY07 Plan</u>	<u>FY07 Quarterly Report</u>	<u>Change (in millions)</u>
Strategic Marketing	\$2.5	\$ 0.0	(\$2.5)
Asset Sales	\$10.0	\$6.0	(\$4.0)
Emergency Medical Service Fees	\$24.5	\$26.0	\$1.5

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Revenue Projections: Revenues from Other Governments

- The City is estimating that, in part because of reduced projected costs, the City's reimbursements for costs incurred by the Department of Human Services will drop by over \$30 million from the amount included in the Plan.
- The City projects that revenues from the Philadelphia Parking Authority and reimbursements for costs incurred by the Department of Public Health will be a combined \$5.5 million lower than projected. That variance will be almost completely offset by a higher than anticipated payment from the convention center.

<u>Item</u>	<u>FY07 Plan</u>	<u>FY07 Quarterly Report</u>	<u>Change (in millions)</u>
Human Services Reimbursements	\$ 574.9	\$543.7	(\$31.2)
Parking Authority	\$25.0	\$22.0	(\$3.0)
Health Department Reimbursements	\$ 58.6	\$56.1	(\$2.5)
Convention Center Offset	\$16.3	\$21.7	\$5.4

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Major Changes in Obligations Projections

- The largest estimated obligations increases from Plan are for pay as you go capital, employee benefits and prisons. These expenditures are all for areas that pose serious long-term threats to the City's fiscal condition.
- The increase in Fire costs is driven primarily by the continuing rapid escalation in the Department's overtime costs.

<u>Item</u>	<u>FY07 Plan</u>	<u>FY07 Quarterly Report</u>	<u>Change (in millions)</u>
City Council –(increase is for pay as you go capital)	\$14.8	\$44.7	\$29.9
Employee Benefits (increase is for workers compensation, health/medical and social security costs)	\$863.3	\$880.0	\$16.7
Prisons	\$194.2	\$206.7	\$12.5
Fire	\$180.5	\$188.7	\$8.2

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Major Changes in Obligations Projections

- The largest estimated obligations reduction from the Plan is for the Department of Human Services. Costs are lower than projected because of delays in program expansions and start ups.
- Costs for the Department of Public Property have increased because of higher than anticipated utilities costs and the approval of a \$5 million surveillance camera installation initiative.
- Increases in demand have driven up costs for the Office of Supporting Housing, which coordinates the City's homeless services, while the Office of Housing and Community Development's costs have increased to compensate for cuts in federal funding and because of a delay in the implementation of a reorganization plan.

<u>Item</u>	<u>FY07 Plan</u>	<u>FY07 Quarterly Report</u>	<u>Change (in millions)</u>
Department of Human Services	\$609.5	\$592.5	(\$17.0)
Public Property (excluding SEPTA)	\$112.4	\$121.6	\$9.2
Office of Housing and Community Development	\$1.4	\$5.7	\$4.3
Office of Supporting Housing	\$29.5	\$33.7	\$4.2

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

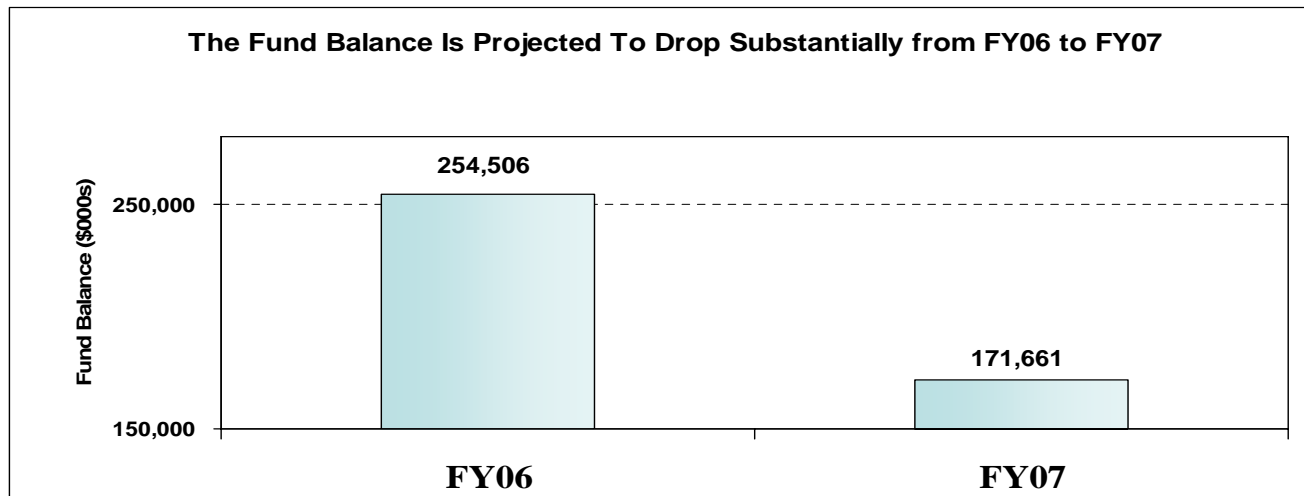
Key Financial Issues Raised in Quarterly Report:

- Reduction in Fund Balance
- Expenditure Growth
- Volatile Revenue Sources
- Reduced Reliance on Wage Tax
- Cuts in Federal Reimbursements
- Philadelphia Parking Authority

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Financial Issues Raised in Quarterly Report: Declining Fund Balance

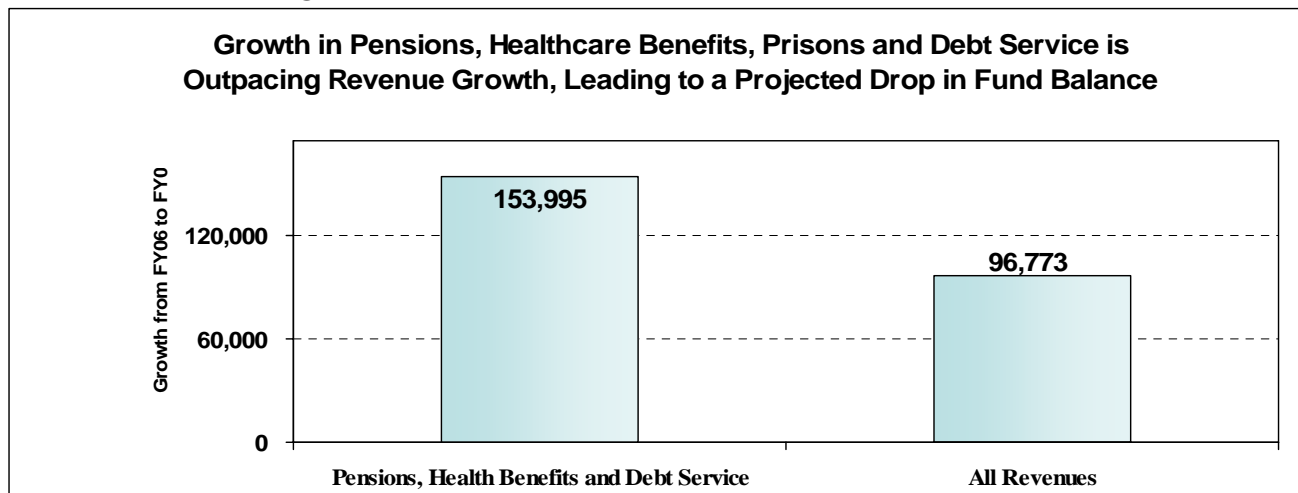
The quarterly report projects an \$82.8 million drop in the City's fund balance as expenditures are projected to grow more quickly than revenues. If the City does not correct that imbalance between revenues and expenditures, it is likely that the City will run deficits before the end of the plan period.



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Financial Issues Raised in Quarterly Report: Declining Fund Balance

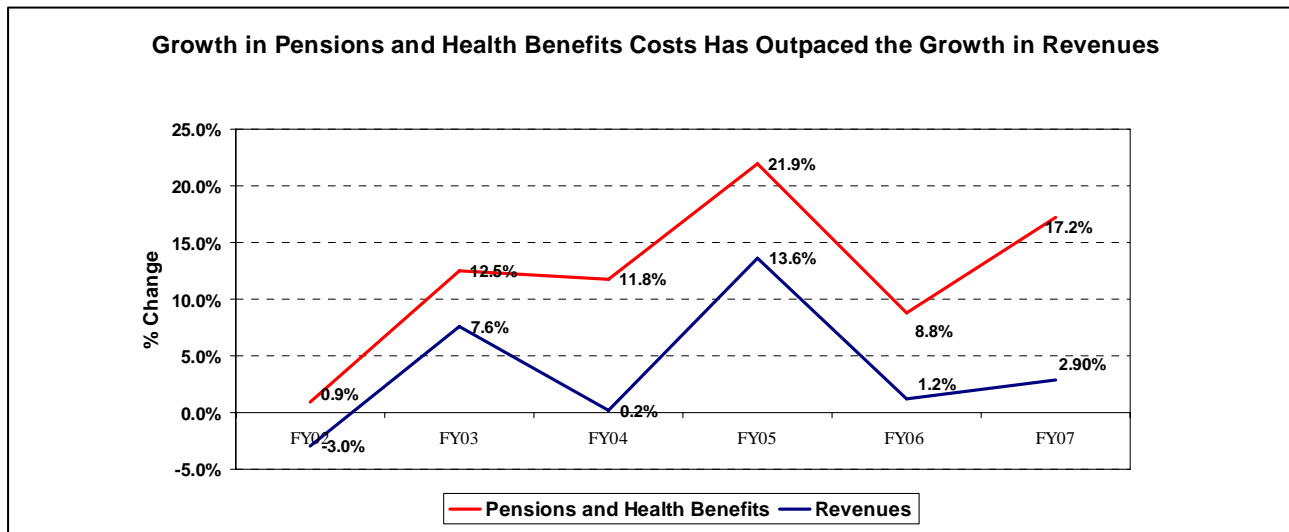
The fund balance is declining in large part because pensions, health benefits, debt service and prisons costs are growing far faster than revenues. These items are projected to grow by a combined \$154 million from FY06 to FY07 while revenues are projected to grow by \$97 million. The four items, combined with costs for the Department of Human Services, have grown from 38% of the budget in FY01 to a projected 45% of the budget in FY07.



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Financial Issues Raised in Quarterly Report: Expenditure Growth

The difference between the growth rates for revenues and just two of the fastest growing expenditure areas – pensions and health benefits – helps illustrate that revenue growth cannot keep up with these items' dramatic growth. Pensions and health benefits have grown faster than revenues in each of the last six years, with this year's gap eclipsing those of the previous five years.



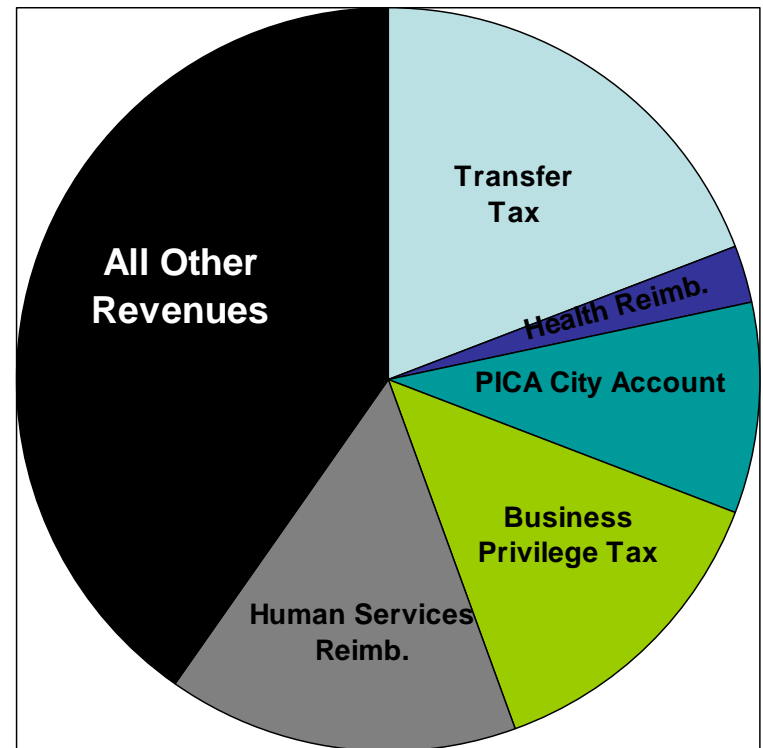
PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Financial Issues Raised in Quarterly Report:

Volatile Revenue Sources

- About 60% percent of the growth in revenues from FY01 through the FY07 projections is from only five sources (*see chart*).
- With the exception of the PICA City Account, all of these revenue sources are highly volatile. BPT revenues and the state and federal reimbursements each have declined in at least one year since FY01 and growth in the transfer tax, which is highly dependent on the continuing strength of the real estate market, has slowed considerably in FY07.
- Excluding these five areas, revenue growth is project to average less than 2.5% annually from FY01 through FY07.

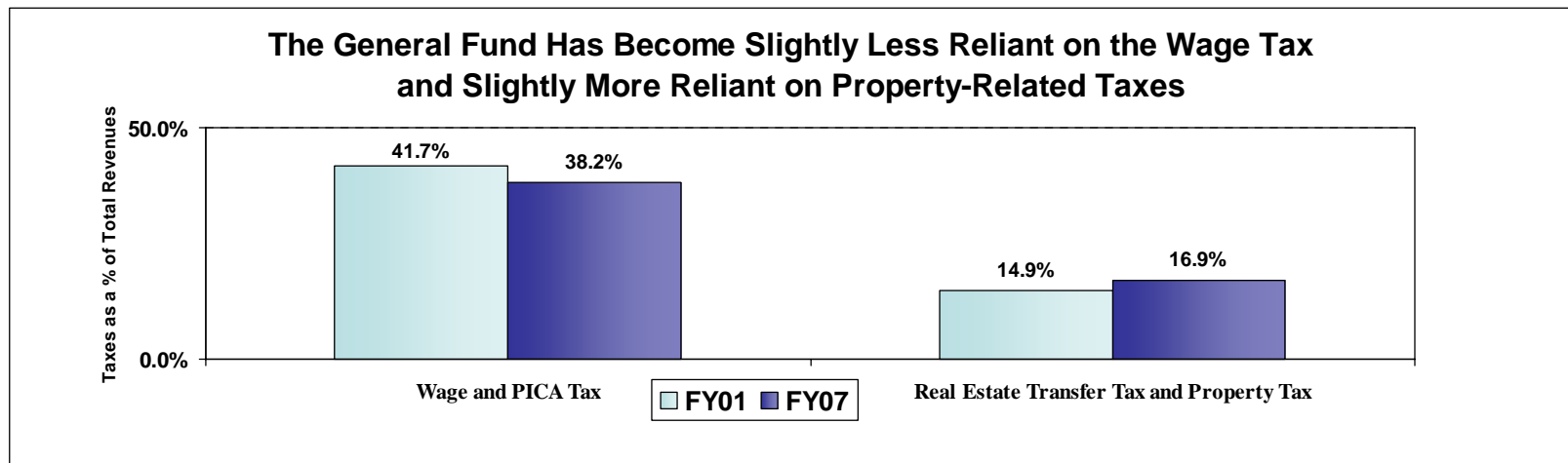
The General Fund is Very Dependent on a Small Number of Sources for Its Revenue Growth



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Financial Issues Raised in Quarterly Report: Reduced Reliance on Wage Tax

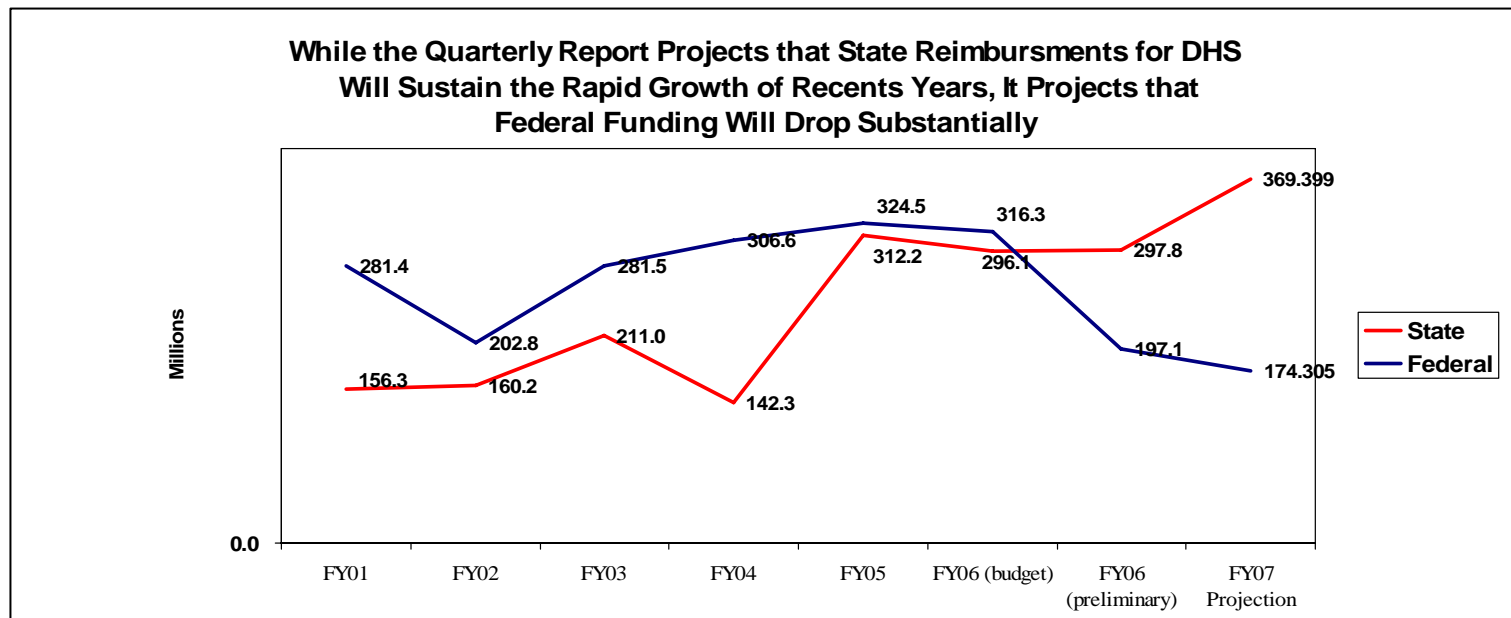
The dramatic increases in real estate transfer tax collections combined with smaller increases in property tax collections and the continuing cuts in wage tax rates have led to a small, but real, shift for the general fund towards more reliance on property based taxes. The shift makes the city less vulnerable to changes in income but more vulnerable to downturns in real estate.



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Financial Issues Raised in Quarterly Report: Cuts in Federal Reimbursements

The quarterly report demonstrates the risk of being dependent on a small number of revenue sources for growth by showing that one of those sources – federal reimbursements for human services costs -- is projected to be \$150 million lower in FY07 than it was in FY05.



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Financial Issues Raised in Quarterly Report:

Philadelphia Parking Authority

- The City projects that it will receive \$22M in parking violation fines from the Parking Authority in FY07, up from \$18.6M in FY06, but \$3M below the amount included in the original FY07 budget.
- Legislation enacted last spring has increased parking fines and increased the amount of revenue the City receives.

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

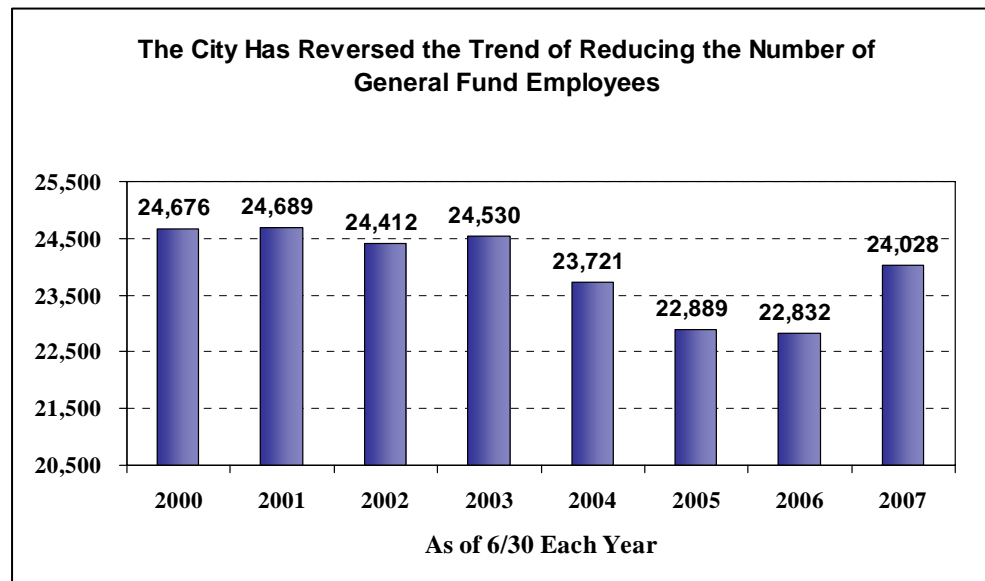
Key Managerial Issues Raised in Quarterly Report:

- Staffing Increases
- Increases in Overtime
- Other Managerial Issues

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Managerial Issues Raised in Quarterly Report Staffing Increases

- The City reduced staffing substantially from the end of FY03 to the end of FY05, but staffing remained virtually unchanged in FY06 – dropping by less than half a percent -- and is projected to increase by almost 1,200 filled positions in FY07. The increase would undo a substantial portion of the progress the City had made in cutting the size of its workforce.



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Managerial Issues Raised in Quarterly Report Staffing Increases

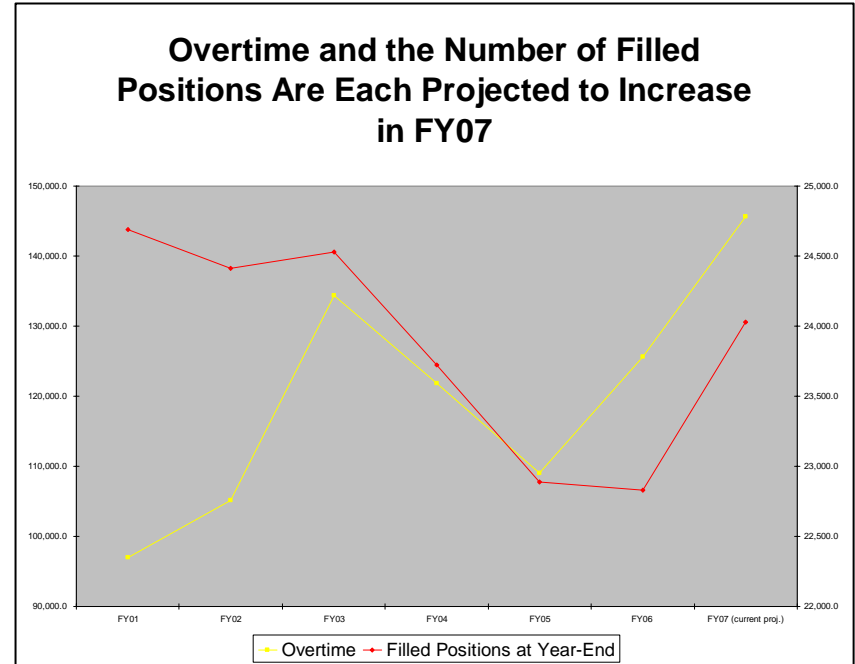
- While 19 departments are projected to add at least 10 full time employees during FY07, over 800 of the over 1,200 projected added jobs would be in only five departments.

<u>Department</u>	<u>FY06 Year-End</u>	<u>FY07 Quarterly Report Projection</u>	<u>Change</u>
Fire	2,270	2,455	185
Human Services	1,703	1,816	113
Police	7,287	7,508	221
Prisons	2,225	2,423	198
Public Health	622	730	108
Total of Five Departments	14,693	14,932	825

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Managerial Issues Raised in Quarterly Report: Increases in Overtime

- The increase in staffing is not projected to reduce overtime. In fact, overtime and staffing are each projected to increase in FY07. Overtime is projected to increase by over \$20m. Overtime and staffing each dropped in both FY04 and FY05.
 - While overtime is projected to be increased in a number of departments, the largest projected increases are \$8.5 in the Police Department (to \$57M), \$2.6m in the Prisons System (to \$21.8M) and \$4.9 million in the Fire Department (to \$30.3M);
 - As recently as FY03, Fire overtime was just under \$10M. The Department's overtime has risen in large part because of a change in sick leave policy and because the Fire Department reconfiguration plan was not implemented.



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key Managerial Issues Raised in Quarterly Report:

Other Management Issues

- The average monthly inmate population in the Prison System continues to increase. The Quarterly Report projects a 5.5% increase in FY07 and a 9.6% increase in just two years. At the same time, prisons expenditures are projected to be about \$11.8M over budget.
- The average number of employees on light duty status because of injuries is projected to jump from 255 in FY06 to 300 in FY07 after having dropped slightly from 284 in FY05. At the same time, the number of employees on no duty status is projected to increase to 200 after having jumped from 158 in FY05 to 190 for FY06.
- The average number of emergency shelter beds is projected to increase to 2,800, a 10% increase in just two years.

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key City Budget Characteristics

Cost Areas Projected to Exceed \$100M in FY2007

Item	FY07 Plan (Ms)	% Of Budget	FY07 QR (Ms)	% of Budget
Human Services	\$609.5	16.6%	\$592.5	15.8%
Police	\$491.9	13.4%	\$495.9	13.2%
Pensions Plus Pension Obligation Bonds	\$419.1	11.4%	\$419.2	11.2%
Health/Medical Benefits	\$322.7	8.8%	\$344.5	8.8%
Prisons	\$194.2	5.3%	\$206.7	5.5%
Debt Service	\$191.8	5.2%	\$191.8	5.1%
Fire	\$180.5	4.9%	\$188.7	5.0%
Public Property (excl. Septa Subsidy)	\$112.4	3.1%	\$121.7	3.2%
Health	\$114.3	3.1%	\$114.4	3.0%
Courts	\$111.1	3.0%	\$112.9	3.0%

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key City Budget Characteristics (continued)

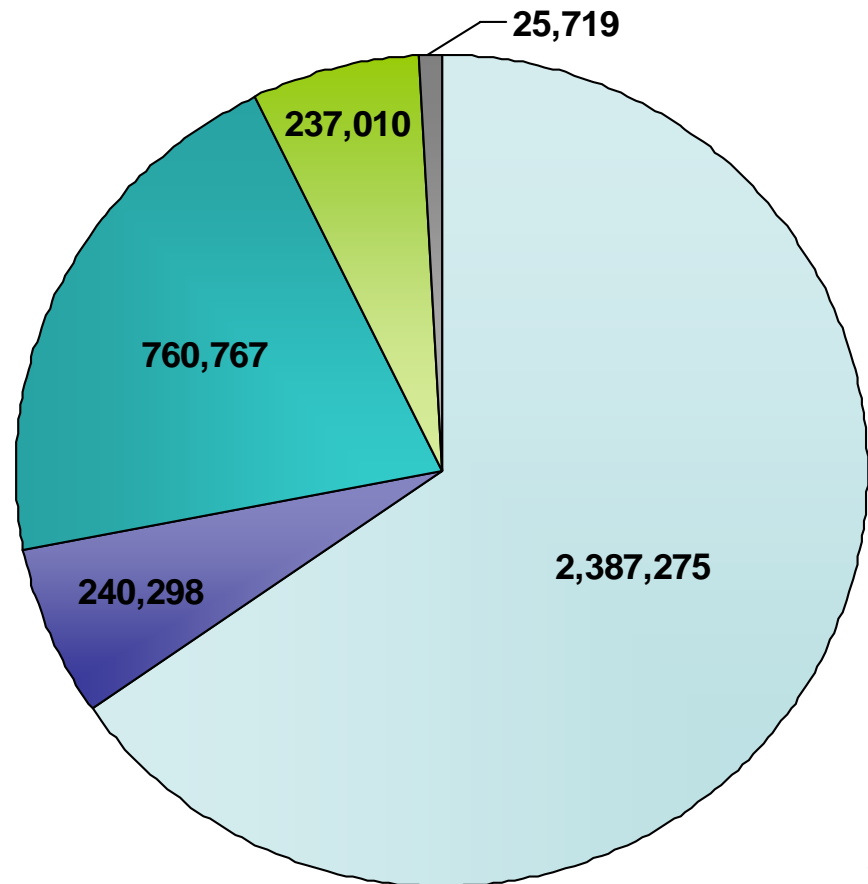
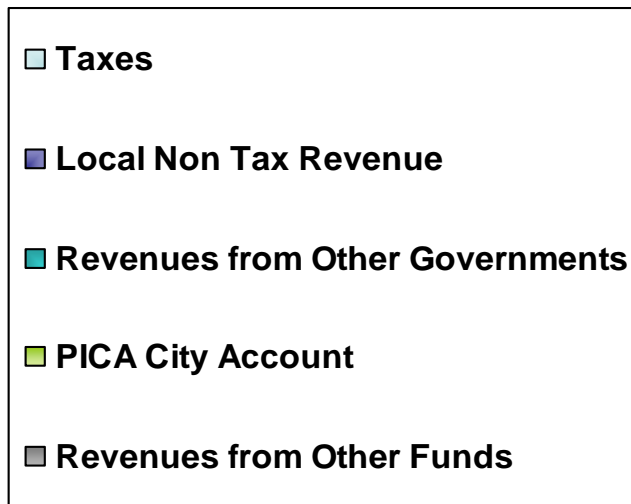
Revenue Areas Projected to Exceed \$100M in FY2007

Item	FY07 Plan (Ms)	% Of Budget	FY07 QR (Ms)	% of Budget
Wage and Net Profits Tax (including PICA City Account)	\$1,376.0	38.1%	\$1,393.0	38.2%
Human Services Reimbursement	\$574.9	15.9%	\$543.7	14.9%
Property Tax	\$409.6	11.3%	\$407.8	11.2%
Business Privilege Tax	\$378.9	10.5%	\$408.0	11.2%
Real Property Transfer Tax	\$195.0	5.4%	\$210.0	5.8%
Sales Tax	\$129.0	3.6%	\$135.0	3.7%

PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key City Budget Characteristics (continued)

FY2007 Sources of City Revenues
(\$000)



PICA Staff Report on the City of Philadelphia's Quarterly Report Second Quarter of FY2007

Key City Budget Characteristics (continued)

Distribution of FY07
Expenditures (\$000) -- \$3.42 Billion

