



**From:** Council President's Office – Finance and Budget Team

**Date:** 10/26/18

**RE:** Historical Trend Analysis Update - City of Philadelphia Financial Projections – General Fund (FY12 – FY18)

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## **Introduction**

As City Council begins to assess the City's fiscal health in FY19, it is important to highlight how projections have materialized in the past to better understand the City's current financial standing. Over the past decade, and particularly during the last fiscal year, Actual end-of-year General Fund balances have consistently exceeded the General Fund balance projected at the beginning of each year. Even with this pattern of actuals exceeding projections, the City has a significant amount of improvement needed to achieve true fiscal health and stability.

**As a reminder: the City of Philadelphia's fiscal year runs from July 1<sup>st</sup> to June 30<sup>th</sup>. FY19 for example, runs from July 1, 2018 through June 30, 2019. The Q3 City Managers Reports are included in this analysis because they contain the most up-to-date figures provided to City Council at the time that a new budget is adopted at the close of the current fiscal year.**

## **Budget Projections**

On July 25, 2018, the Board of the Pennsylvania Intergovernmental Cooperation Authority (PICA) approved the City's FY19-23 Five-Year Plan (FYP). PICA, a State board that oversees the City's long-term financial plans, approved the Five-Year Plan, citing "reasonable" revenue and expenditure projections, revenue growth due to economic expansion, and positive fund balances.<sup>1</sup>

Last year, when the FY18-22 Five Year Plan was approved, the General Fund was projected to end FY18 with a General Fund balance of \$75.4 million. At the end of the 3<sup>rd</sup> quarter, the Administration projected an FY18 year-end General Fund balance of \$208.3 million, which was adjusted upward to \$228.5 million in the PICA approved FY18-23 FYP. **However, the recently released *FY18 City of Philadelphia Annual Financial Report* notes that the unaudited General Fund balance for FY18 is approximately \$368.8 million – meaning the City is now expected to end FY18 almost \$293 million above the original projection of \$75.5 million, and \$160.5 million above the City Q3 Managers Report projection. This has increased the City's General Fund balance from an FY18 Adopted projection of 1.7% of expenditures to the current FY18 projection of 8.4% of expenditures (or 8.1% of revenues).<sup>2</sup> With that said, the City has reached its target of maintaining a General Fund balance that is 6-8% of expenditures, or one month of expenditures, on hand.<sup>3</sup> This higher than expected General Fund balance was fueled by robust growth in the Wage and Earnings tax and the Real Property Transfer tax, which outpaced adopted projections by approximately \$77.7 million and \$88.6 million, respectively, as well as the unused *Federal Funding Reserve*. This approximate \$50.8 million reserve (based on the PICA approved FYP), meant to act as a cushion against federal funding reductions, remained unused, and has flowed to the General Fund balance.**

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<sup>1</sup> "PICA Board Unanimously Approves City of Philadelphia's FY2019 to FY2023 Five Year Plan": [PICAPA.org](http://PICAPA.org), July 25<sup>th</sup>, 2018

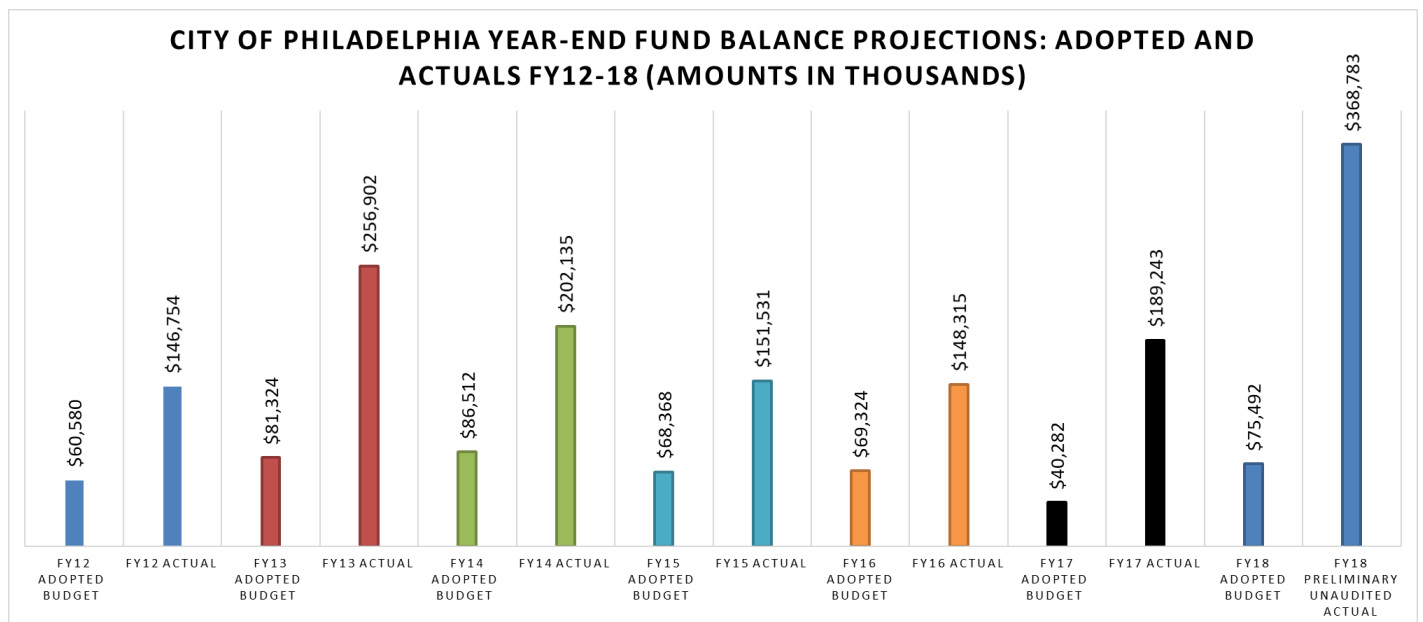
<sup>2</sup> Note, it takes several months after the close of the fiscal year to certify the year-end totals, so they are still listed as "preliminary unaudited actuals" in the report. Based on previous trends, the current amount of \$369M could potentially change as the City prepares the final, audited numbers for the Comprehensive Annual Financial Report (CAFR).

<sup>3</sup> Note, the General Fund balance is different than the end-of-fiscal-year cash balances, which were recently covered by the Controller's Office [Cash Report, Fiscal Year 2018](#). While the City is expected to end FY18 with \$769M cash-on-hand, this is a different measure than the actual unrestricted General Fund balance – which is projected to end FY18 at \$369M – since the City utilizes modified accrual accounting, which accounts for future, known revenues and expenditures. While the cash balance is an important indicator to understand the City's liquidity, it does not include known upcoming expenses and revenues within a given time period, and therefore should be evaluated in conjunction with actual fund balance data in order to have a more complete snapshot of the City's fiscal health.

Given the robust, sustained economic growth that has continued to exceed expectations since the depths of the Great Recession, we have compared the shifts in fiscal projections throughout each fiscal year from FY12-18. Although it is certainly preferable to continue to have Actual year-end General Fund balances exceed projections, the consistently conservative initial projections may negatively impact the City’s long-term credit rating and borrowing costs in the future. **In March, Moody’s downgraded the City’s credit rating to A2, stating: “The negative outlook reflects the City’s current weak financial reserve levels as well as its forward-looking projections for continued financial strain.”**<sup>4</sup>

### Summary

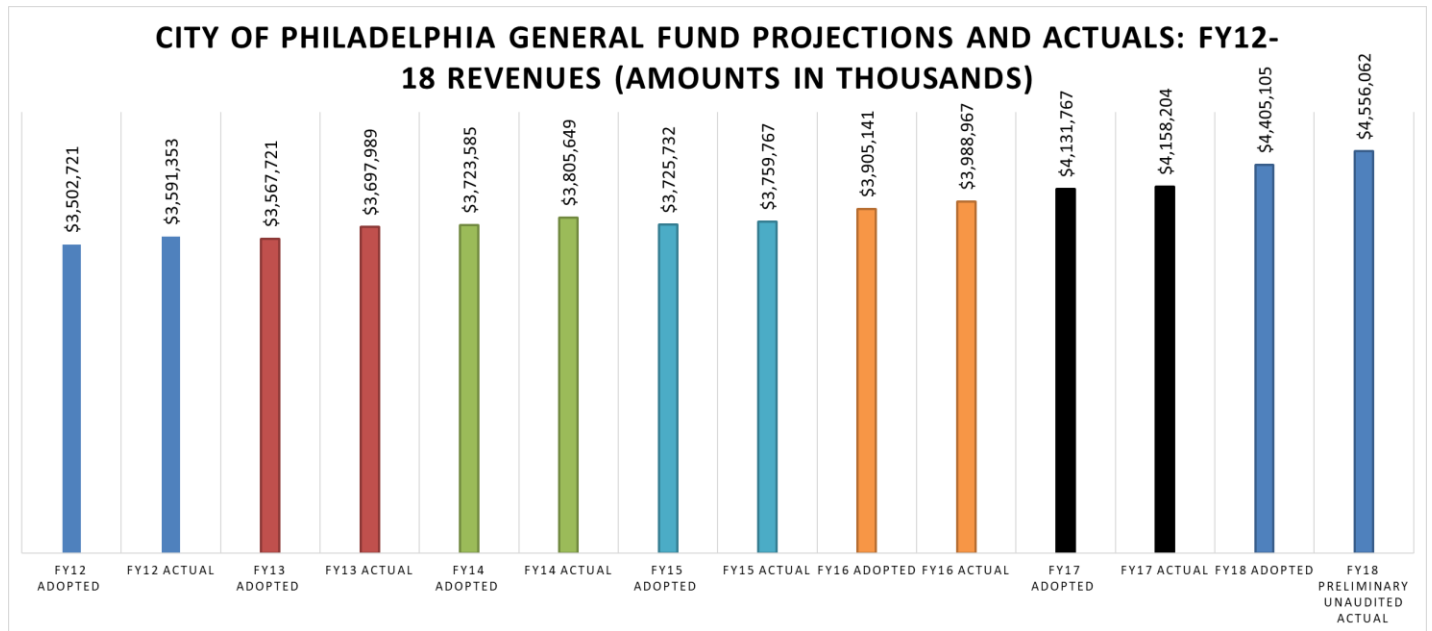
- The FY18 Q3 Managers Report, released in May of 2018, estimated an FY18 year-end General Fund balance of \$208.3 million. This is the estimate that was before Council when Council deliberated over the FY19 budget. In fact, however, this estimate was \$160.5 million lower than the current FY18 preliminary unaudited actual of \$368.8 million.
- The FY18 General Fund balance is currently projected to end the fiscal year \$293.4 million higher than what was originally adopted in June of 2017, increasing from \$75.4 to \$368.8 million.
- From FY12 to FY18, the Actual year-end General Fund balances have been understated by an average of \$140.2 million when compared to each fiscal year’s adopted budget projection.
- Expenditures from FY12 to FY18 are projected to end, on average, \$63.5 million lower than projections listed in each fiscal year’s Q3 Managers Report.
- Revenues from FY12 to FY18 are projected to end, on average, \$16.9 million higher than projections listed in each fiscal year’s Q3 Managers Report.



*Figure 1*

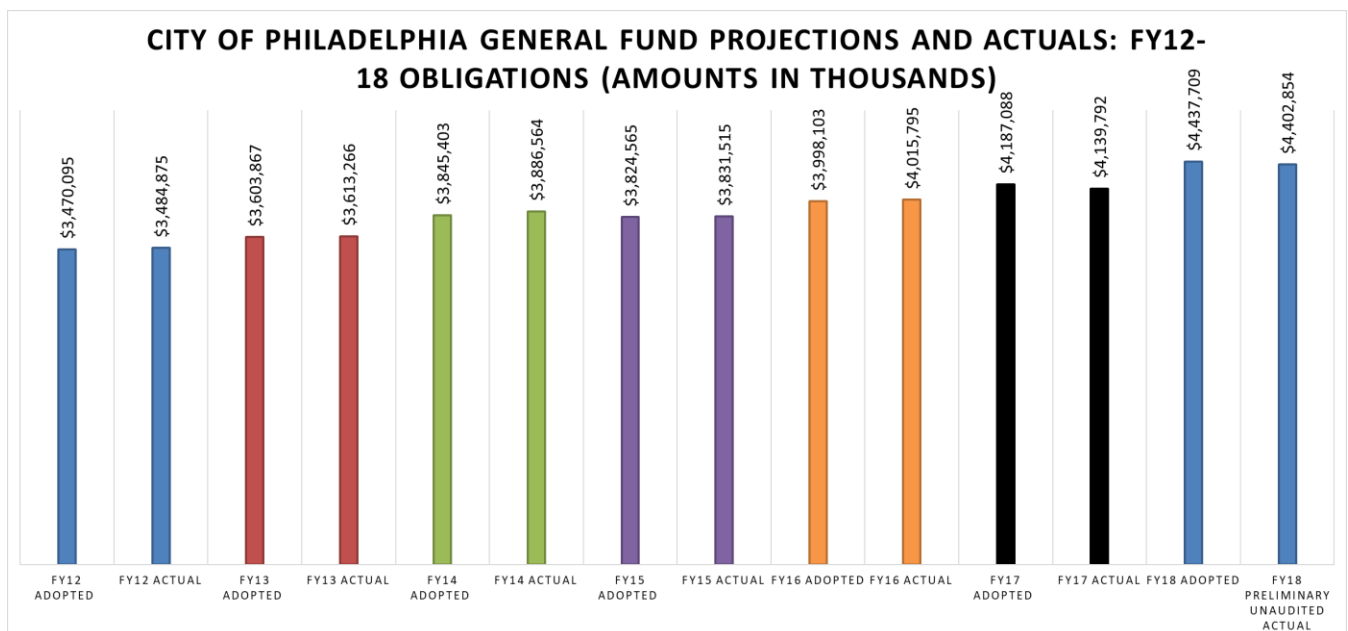
As demonstrated in **Figure 1** above, since FY12, the General Fund balance has **exceeded adopted projections by an average of \$140.2 million.**

<sup>4</sup>[https://www.moodys.com/research/Moodys-assigns-A2-rating-to-City-of-Philadelphia-PAs-378--PR\\_904516223](https://www.moodys.com/research/Moodys-assigns-A2-rating-to-City-of-Philadelphia-PAs-378--PR_904516223)



*Figure 2<sup>5</sup>*

**Figure 2**, above, highlights the revenues – adopted versus actual – in each fiscal year, back to FY12. This illustrates the consistent growth in revenues – **which are projected to have grown \$964.7 million, or 26.9%, since FY12.**



*Figure 3<sup>6</sup>*

**Figure 3**, above, highlights similar growth in obligations as shown in **Figure 2**. **From FY12 to FY18, obligations are projected to have grown \$917.9 million, or 26.3%, since FY12.**

<sup>5</sup> Adjusted for revenues related to the projected PGW sale. Since the sale did not occur, revenues and subsequent expenditures have been removed from calculations.

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### CITY OF PHILADELPHIA GENERAL FUND BALANCE ADJUSTMENTS: SHIFT FROM Q3 PROJECTION TO ACTUALS (AMOUNTS IN THOUSANDS)



Figure 4

Figure 4 illustrates the difference between the revenue and obligation projections in the Q3 report compared to the actual year-end totals. For example, FY17’s actual obligations, shown in red, were \$93.9 million lower than the projection shown in the Q3 report. As shown above, there is a tendency to downwardly adjust total expenditure numbers from the Q3 projection to the actual year-end total, while the revenue projections remain closer to actuals – likely due to the fact the Administration has more discretion over spending than revenue generation.

### CITY OF PHILADELPHIA GENERAL FUND CUMULATIVE TAX GROWTH BY SOURCE: FY12-18 (AMOUNTS IN THOUSANDS)

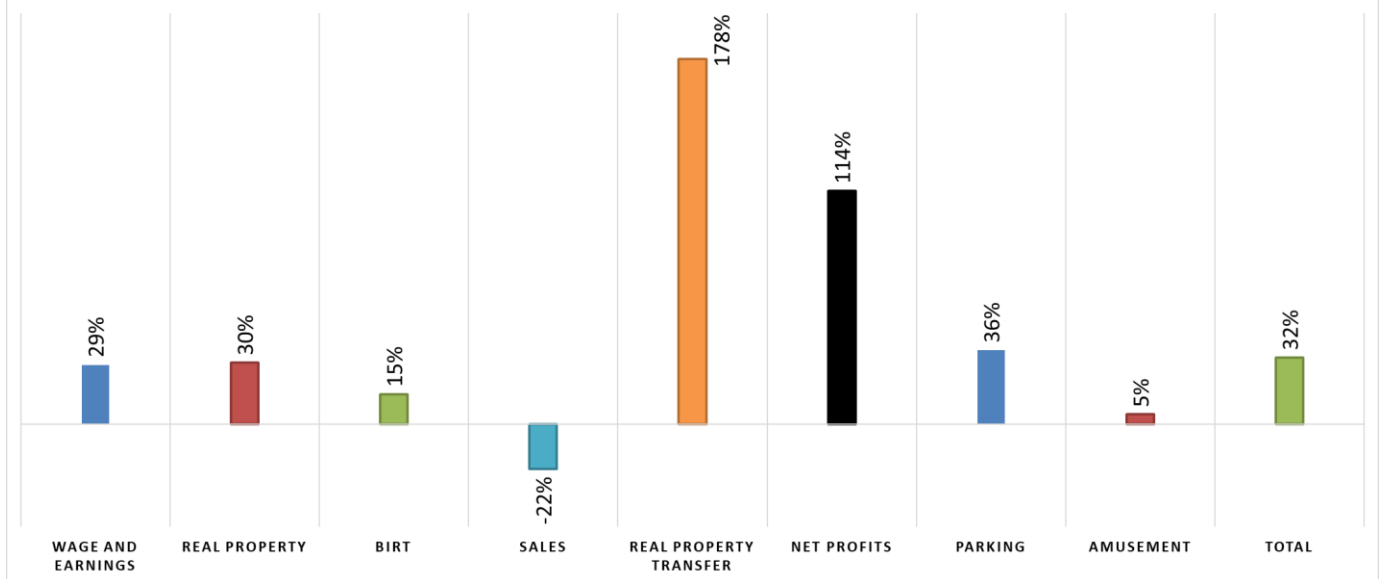
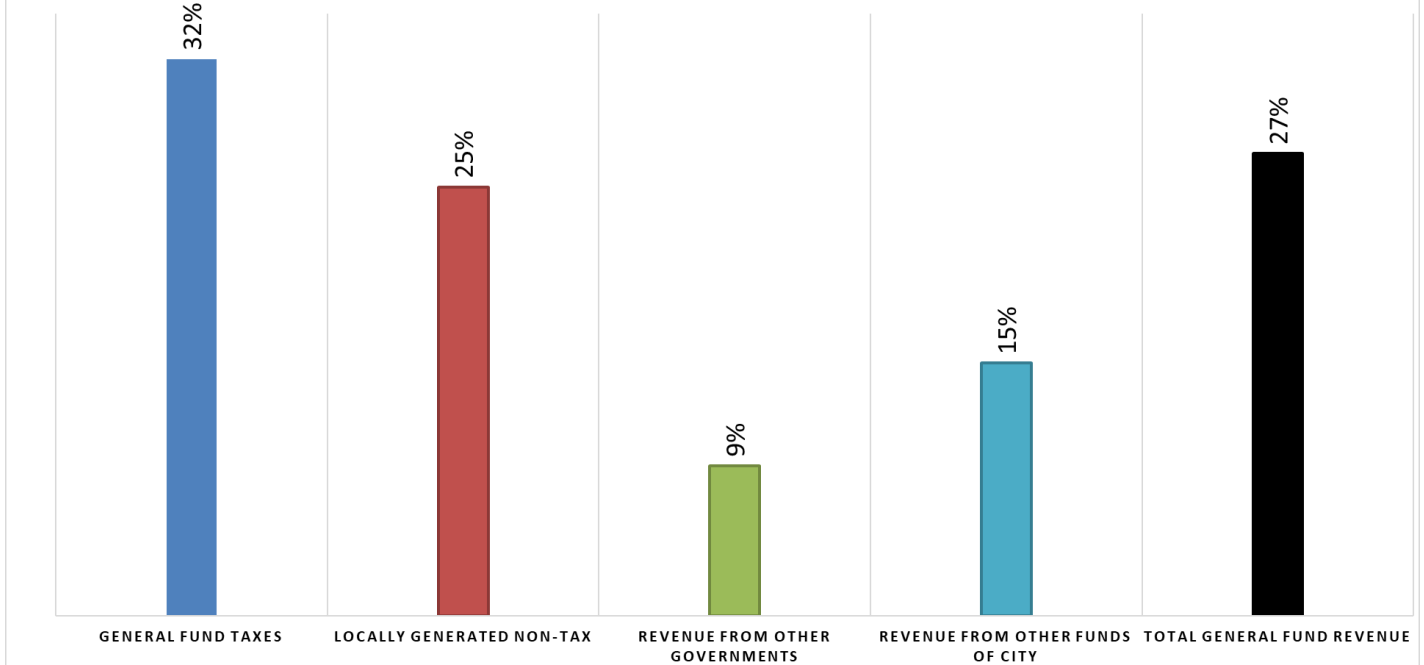


Figure 5

Figure 5, above, provides context to the City’s revenue growth. The largest growth is seen in the Real Property Transfer tax. Albeit volatile, the Real Property Transfer tax has grown 178% since FY12, and has been buoyed by the continuous investment and redevelopment in certain areas of Philadelphia.

**CITY OF PHILADELPHIA GENERAL FUND TAX CUMULATIVE GROWTH BY  
SOURCE: FY12-18 (AMOUNTS IN THOUSANDS)**



*Figure 6*

**Figure 6**, above, highlights the changes in revenues for the General Fund, by comparing FY12 to FY18. Although the City has experienced growth in local tax and non-tax revenues, “Revenue from Other Governments” has grown at the slowest pace – at 9% over the prior seven fiscal years.

**Conclusion**

Although the City continues to, on average, end each fiscal year exceeding revenue projections and realizing lower than projected expenditures, there is significant room to improve the City’s financial standing. This includes increasing reserve levels, as well as improving the City’s credit outlook. As City Council continues through this legislative calendar, City Council’s Finance and Budget Team will continue to provide information to Council – to ensure the legislative process continues in a structured and informed manner.

CITY OF PHILADELPHIA YEAR-END FUND BALANCE PROJECTIONS: FY12-FY18 (AMOUNTS IN THOUSANDS)

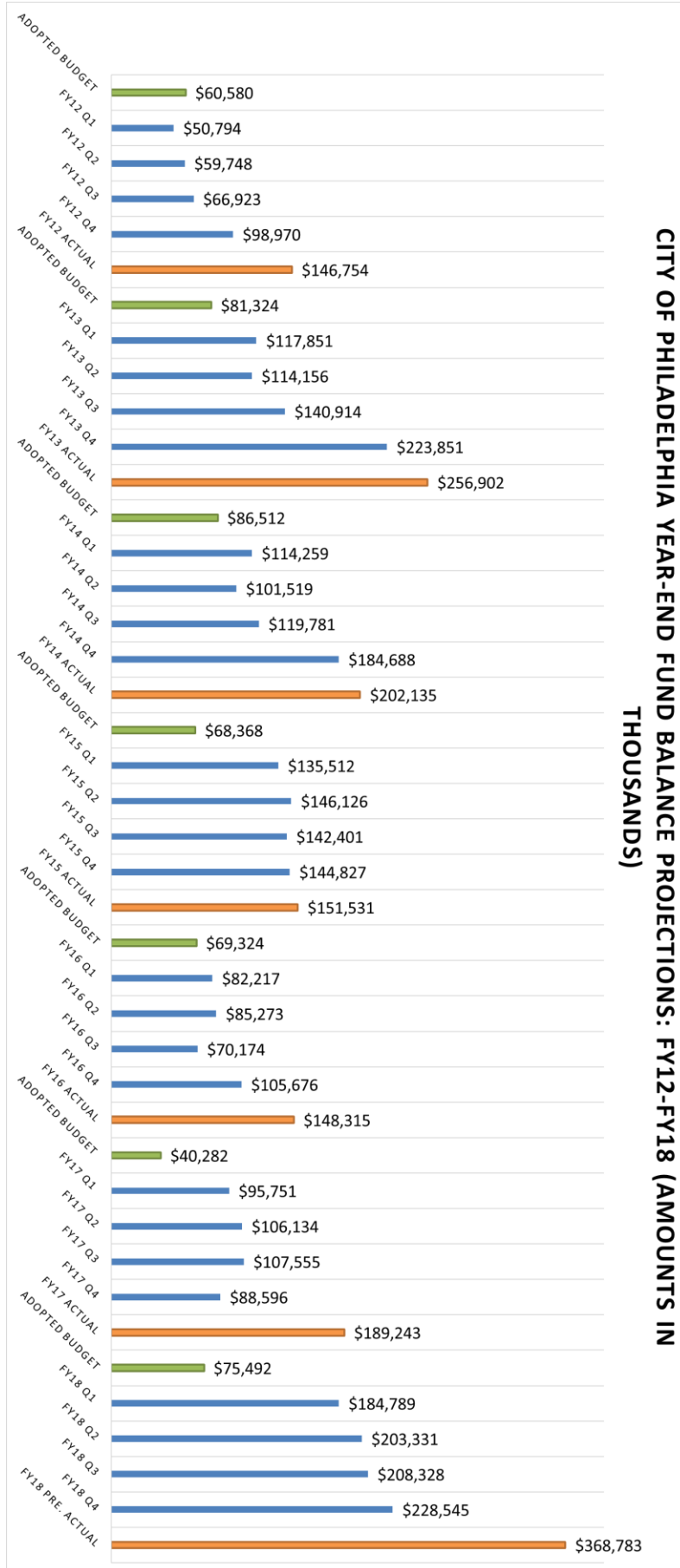


Figure 7