City Council *of* Philadelphia
Office of the President - Finance and Budget Team
11.12.19

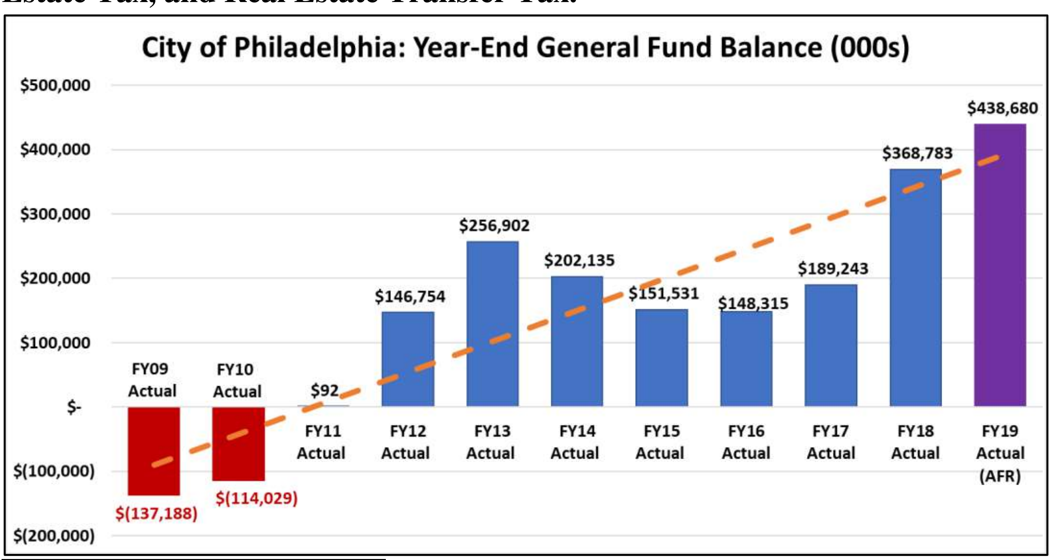
Preliminary Analysis of City of Philadelphia FY19 Annual Financial Report (AFR): Progress Since FY09

Executive Summary

On October 28, 2019, the City of Philadelphia released its FY19 *Annual Financial Report (AFR),* showing a **year-end General Fund balance of $438.7 million – which represents 9.1% of FY19 revenues.** This year-end balance not only meets, but **exceeds, the City's internal policy goal of 6-8% of annual revenues** – and takes into account several proposed, large fiscally responsible expenditures which lowered the FY19 General Fund year-end total.[1] However, please bear in mind that FY19's General Fund balance level is below the GFOA[2] recommendation of having 16-18% (two months) of annual General Fund revenues held in the fund balance.

City of Philadelphia Tax Revenue Differences: FY09 vs. FY19		
Tax	**FY09 vs. FY19 Actual ($ Increase, 000s)**	**FY09 vs. FY19 Actual (% Growth)**
Wage and Earnings	$ 464,858	42%
Real Property	$ 296,546	74%
BIRT	$ 154,883	40%
Sales	$ 95,967	75%
Real Estate Transfer	$ 213,313	185%
Net Profits	$ 23,609	194%
Parking	$ 28,931	41%
Amusement	$ 5,027	24%
Philadelphia Beverage Tax	n/a	n/a
Other	$ 2,033	84%
Total: Locally Generated Tax Revenue	$ 1,362,022	60%

Notably, the FY19 AFR shows a continuing trend of significant long-term General Fund revenue growth over the past decade, coupled with year-end City General Fund balances that have consistently exceeded the amounts projected at the beginning of each fiscal year, amounting to consistent, overall fiscal improvement for the City of Philadelphia.[3] **Much of the City's General Fund's 60% revenue growth realized in the past decade (FY09 vs. FY19) is attributable to several taxes: the Wage Tax, the Real Estate Tax, and Real Estate Transfer Tax.**



Combined, the growth in all General Fund tax revenues, which outpaced growth in expenditures, led to the continued growth in the General Fund balance out of negative values. The chart to the left highlights the pattern of year-to-year General Fund balances, dating back to FY09.

[1] The proposed FY19 year-end transfer ordinance includes additional pay-as-you-go capital expenditures, a planned budget stabilization reserve/rainy-day fund deposit, housing trust fund deposits, and economic stimulus spending.
[2] Government Finance Officers Association: Fund Balance Guidelines
[3] As a reminder: The City of Philadelphia's fiscal year runs from July 1st to June 30th. FY20 for example, runs from July 1, 2019 through June 30, 2020. The Q4 City Managers Reports release "year-end preliminary actual" totals, which are then updated in the *Annual Financial Report.*

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Progress Since the Great Recession (late 2000s)

The FY19 AFR shows significant improvement in the City's fiscal health since the Great Recession:

- **Fund Balances have significantly improved.** According to the FY19 AFR, the General Fund ended FY19 with a balance of $438.7 million (i.e., the City, through growing tax revenues, ended the year with $438.7 million that is not appropriated for an expense). This is lightyears ahead of FY09, when the General Fund balance ended the year at -$137.2 million.
  - The General Fund balance would have ended the year higher, had it not been for the following expenditures included in the *proposed* FY19 year-end transfer ordinance (Bill No. 190857) which are reflected in the FY19 AFR:
    - $47 million in Pay-As-You-Go Capital to reduce future borrowing costs.
    - $20 million to the Economic Stimulus Program Expenditures.
    - $10 million to the Housing Trust Fund.
  - In addition to the *current* General Fund balance, the **City is projected to deposit an additional $54.8 million into the *Budget Stabilization Reserve* in FY20** ($20 million included in transfer ordinance) and hold **$55.1 million in the *Federal Funding Reserve***.
- **Wages in Philadelphia are up.** In FY10, Wage Tax collections hit a low of $1.11 billion. The recently released *AFR* shows FY19 collections ended the year at $1.58 billion: a **$467.7 million increase – even after realizing continual, incremental rate reductions** (see chart on next page).
- **The local economy is structurally improving.** In FY10, the City collected $364.7 million in *Business Income and Receipts (BIRT)* taxes. FY19 ended with $540.9 million in collections, a $176.2 annual increase. This increase in collections happened even as the City has continued to incrementally reduce the BIRT burden. Since 2013, the Net Income tax rate has been reduced from a high of 6.5% down to the current rate of 6.2% while allowing businesses to exempt the first $100,000 in sales when determining tax liability.
- **Home Sales in Philadelphia are strong.** The City collected $328.4 million in Real Estate Transfer Taxes in FY19, representing significant growth over the decade. The tax saw 185% growth in annual revenues since FY19 – outpacing the overall 6% increase in the tax rate (see chart on next page).
- **Our pension system is improving.** Through a host of Council and City-led initiatives, the outlook of the City's pension system has substantially improved. The City continued to lower the *expected rate of return*, increased contributions significantly above and beyond the *Minimum Municipal Obligation (MMO)* required by the State, increased employee contributions, introduced a "stacked-hybrid" plan for new employees, and changed the investment strategy towards passive investing – to reduce fees and reflect a more balanced approach. Combined, these efforts have grown the Fund's assets and led to a **cash-flow positive 2018 (big news). The *AFR* shows, in relation to the Municipal Pension:**
  - Employee contributions reached $100.4 million in FY19, more than double FY13 contributions.[4]
  - The Pension Fund's *Net Position* (assets) increased in value by $255.6 million in FY19, ending the year at $5.6 billion. The City's overall *Net Pension Liability* ended FY19 at $6.03 billion.[5]

[4] In FY13, employee contributions totaled about $49.6 million. This figure includes the $1.2 million contributed to the Gas Works pension.
[5] These figures will be *further* explained when the Fund releases its 2019 *Actuarial Valuation* report. Prior year reports can be found here.

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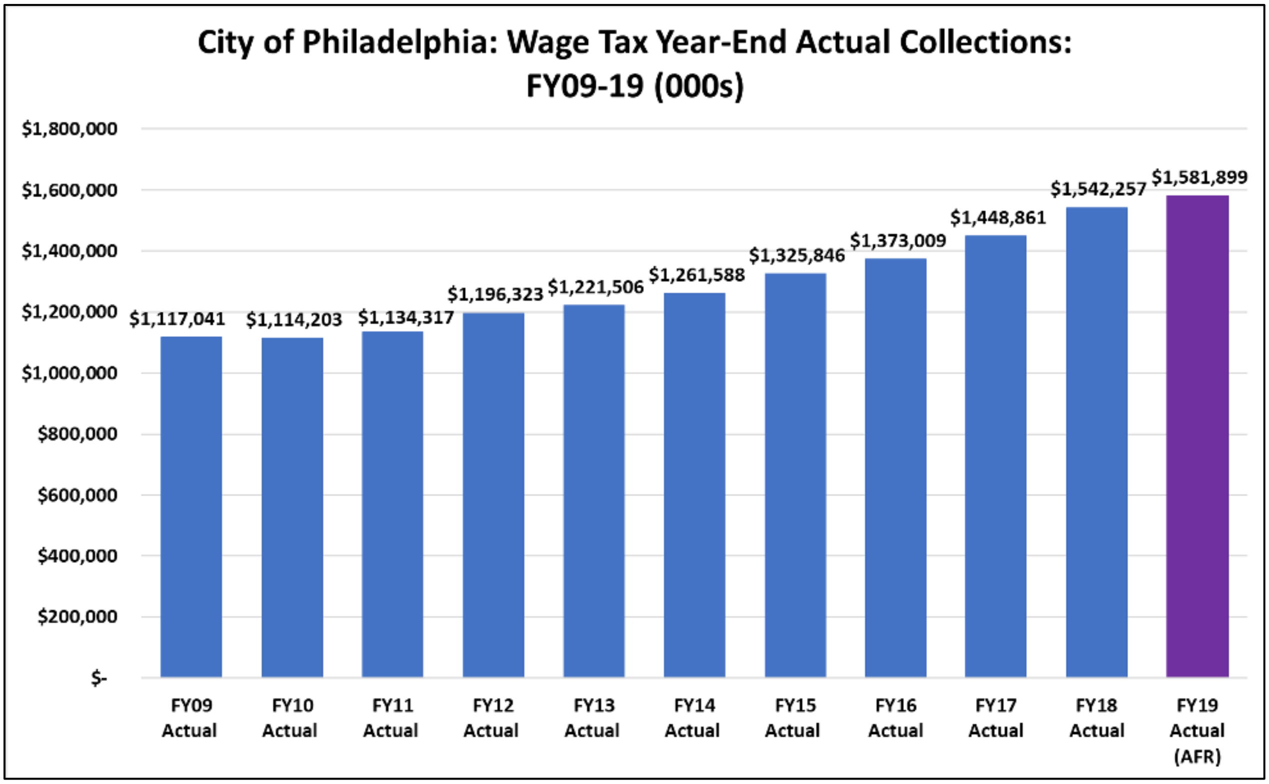

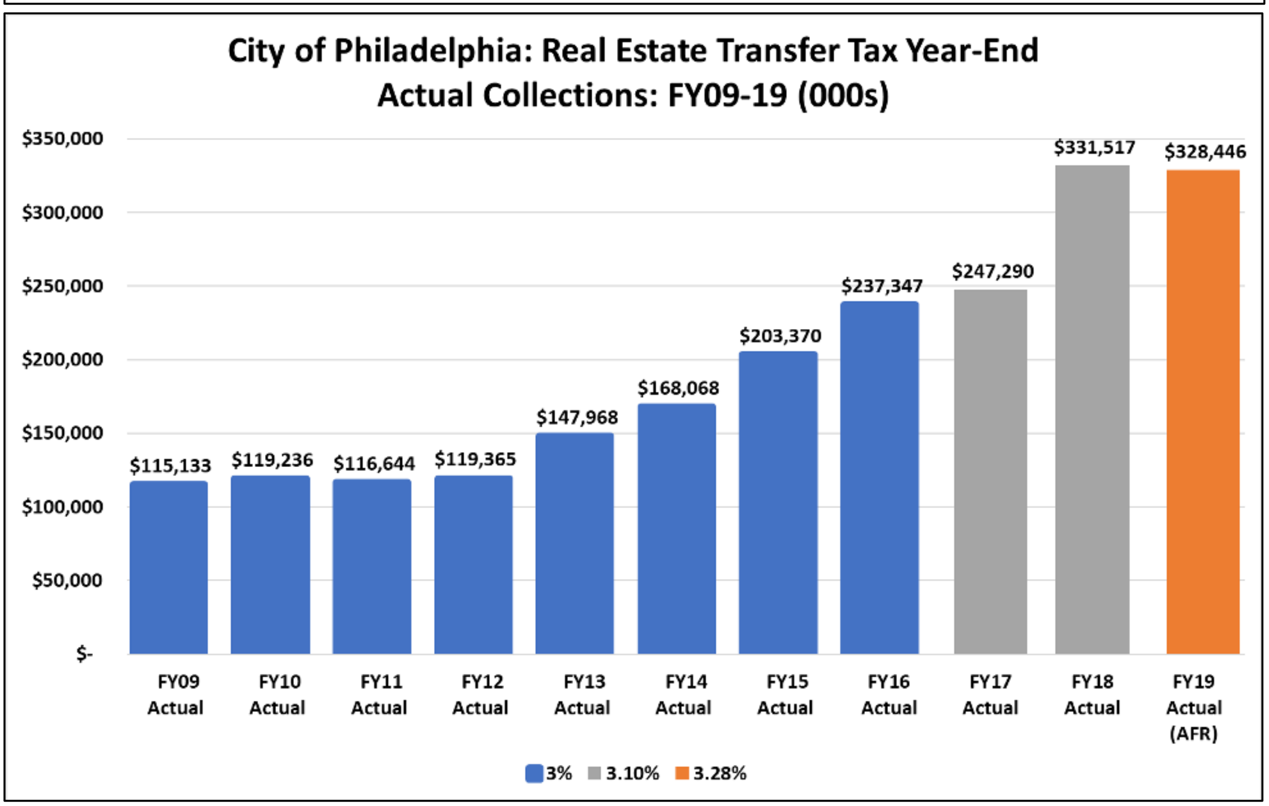

Conclusion

The FY19 *Annual Financial Report* continues the trend of the City of Philadelphia improving its financial standing. Over the last decade, the City has gone from *negative fund balances to balances that exceed internal policy goals* (i.e., General Fund balance equal to 6-8% of General Fund revenues), significant cash balances[6] which save the City in lower short-term borrowing costs[7], and an ever-improving credit rating that leave the City in a position to prepare for future downturns.

The progress made is important, and the flexibility granted through maintaining liquidity cannot be understated. However, as highlighted in the recently released *American Community Survey*, Philadelphia remains the poorest, large city in America.

Having appropriately large fund balances and contingency reserves are substantially important to a) maintaining and improving upon the City's credit ratings (which lowers borrowing costs), and b) mitigating against future potential economic downturns (e.g., large, unrestricted cash reserves should lower burden on City to "have to" *reduce* resources in response to meeting service demands during a downturn – when revenues are lower and service demands are potentially higher), but only if this exists in conjunction with a City that is actively investing in the most critical areas related to the future of our citizens – jobs, education, health and safety. As we continue throughout FY20, City Council will continue to maintain the balance of fiscal responsibility and active investment in sustained, equitable growth.

[6] City Controller: Cash Report Fiscal Year 2019
[7] When cash balances are low, the City will issue "revenue anticipation notes". High cash balances allow the City to skip issuing this type of short-term bond, which saves the City money in borrowing costs.