CITY OF PHILADELPHIA

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REBECCA RHYNHART
City Controller

July 8, 2019

Mr. Harvey M. Rice, Executive Director
Pennsylvania Intergovernmental Cooperation Authority
1500 Walnut Street, Suite 1600
Philadelphia, PA 19102

Dear Mr. Rice:

Pursuant to its mandate as specified in Section 12720.209(f)(1) of the Pennsylvania Intergovernmental Cooperation Authority (PICA) Act, the Office of the Controller conducted its annual review of the Forecasted General Fund Statements of Operations for each of the fiscal years ending June 30, 2020 through June 30, 2024. The Statement of Operations, also known as the Five-Year Plan (Plan), was prepared by the City of Philadelphia's Office of the Director of Finance and submitted to PICA on June 18, 2019. My staff conducted its review of the Plan in accordance with attestation standards set forth by the American Institute of Certified Public Accountants. Attached please find the independent accountant's report signed by my deputy who is a Certified Public Accountant.

I recommend that PICA approve the Plan; however, in reviewing the projected annual budgets, our office noted two sensitive assumptions and two causes for concern that PICA should take into consideration while evaluating the Plan. In particular, the scheduled dissolution of PICA at the end of fiscal year (FY) 2023 represents a serious risk to the Plan as indicated in the sensitive assumption detailed below. Our office expects the City to provide a plan with concrete steps for its course of action to resolve this issue by the next budget cycle.

Sensitive Assumptions

The Plan does not anticipate the dissolution of PICA at the close of FY23, following the City's repayment of outstanding PICA bonds. In the current iteration of the Plan, the City assumes $2.5B in Wage and Net Profits Tax revenue for FY24, inclusive of $628M that will no longer be collected by the PICA Tax. This assumption represents a significant risk to the Plan and requires either state legislative action to reinstate PICA or City Council legislation to amend the Wage Tax rate to account for the discontinued PICA portion.

As noted in the accountant's report, the City set aside roughly $140M for future labor obligations. Such provisions should anticipate future labor negotiations between the City and corresponding bargaining units certain to occur upon the expiration of existing contracts. It is our view that the budgetary allocations as specified in the Plan do not adequately account for the likely cost of such renegotiations.

Causes for Concern

The City's annual contribution to the School District was $104M in FY18 and is expected to grow over the life of the plan from $222M in FY20 to $273M in FY23. Over the lifetime of the Plan, the City budgeted for $1.3B in contributions to the School District. While not overly burdensome at present given the strength of Philadelphia's economy, in the event of lower-than-expected revenue receipts, these obligations may place significant strain on City resources. To meet these obligations during a potential economic downturn, budgetary adjustments may be required at the cost of vital City services.

Our office's revenue projections are more conservative than the Budget Office's estimates, resulting in a difference of $200M over the life of the Plan. In particular, our office's projections indicate the possibility of an economic slowdown, and subsequent weaker tax revenues, in the earlier years of the Plan. Given the recent uncertainty in both the national and global economies, as well as the City's reliance on the Wage Tax, our office believes that the current economic climate warrants fiscal prudence when appropriating for the future.

In closing, my office expresses its gratitude to the management and staff of the Office of Budget and Program Evaluation for their cooperation and assistance during this review and looks forward to our continued relationship.

Sincerely,

Rebecca Rhynhart
City Controller

cc: Chair and Board Members of the
Pennsylvania Intergovernmental Cooperation Authority
James F. Kenney, Mayor
Rob Dubow, Director of Finance
Anna Adams, Budget Director

City of Philadelphia Forecasted General Fund Statements of Operations Fiscal Years 2020-2024

City Controller Rebecca Rhynhart

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REBECCA RHYNHART
City Controller

CHRISTY BRADY
Deputy City Controller

INDEPENDENT ACCOUNTANT'S REPORT

To the Chair and Board Members of the
Pennsylvania Intergovernmental Cooperation Authority

We have examined the accompanying forecast of the City of Philadelphia, Pennsylvania, which comprises the forecasted general fund statements of operations and summaries of significant assumptions and accounting policies for each of the five years ending through June 30, 2024, of the City of Philadelphia, Pennsylvania, based on the guidelines for the presentation of a forecast established by the American Institute of Certified Public Accountants (AICPA). City of Philadelphia's Office of the Director of Finance management is responsible for preparing and presenting the forecast in accordance with the guidelines for the presentation of a forecast established by the AICPA. Our responsibility is to express an opinion on the forecast based on our examination.

Our examination was conducted in accordance with attestation standards established by the AICPA. Those standards require that we plan and perform the examination to obtain reasonable assurance about whether the forecast is presented in accordance with the guidelines for the presentation of a forecast established by the AICPA, in all material respects. An examination involves performing procedures to obtain evidence about the forecast. The nature, timing, and extent of the procedures selected depend on our judgment, including an assessment of the risks of material misstatement of the forecast, whether due to fraud or error. We believe that the evidence we obtained is sufficient and appropriate to provide a reasonable basis for our opinion.

In our opinion, the accompanying forecast is presented, in all material respects, in accordance with the guidelines for the presentation of a forecast established by the AICPA, and the underlying assumptions are suitably supported and provide a reasonable basis for management's forecast.

There will usually be differences between forecasted and actual results because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

The forecasted statement referred to above includes assumptions that are particularly sensitive because they require state or city legislative approval and successful labor negotiations. As discussed in Note C.3.a. the Wage Tax rate includes 1.5 percent that is reserved for PICA. This assumption is particularly sensitive because the plan assumes the state will enact legislation to reinstate PICA upon its dissolution at the end of fiscal year 2023 or, alternatively, City Council will pass legislation to increase the Wage Tax to produce the expected revenue. The assumptions pertaining to labor agreement costs as described in Note C.6. are particularly sensitive due to the uncertainty in the outcome of expected future negotiations with the four major municipal unions whose contracts are set to expire in 2020.

Christy Brady

CHRISTY BRADY, CPA
Deputy City Controller
Philadelphia, Pennsylvania
July 8, 2019

Forecasted General Fund Statements of Operations

Fiscal Years Ending June 30, 2020 through June 30, 2024

Prepared by:

Office of Budget and Program Evaluation
Office of the Director of Finance

City of Philadelphia - Office of the Director of Finance
Forecasted General Fund Statements of Operations
Fiscal Years Ending June 30, 2020 through June 30, 2024

(Amounts in thousands)

NO.	ITEM	FY 2020 Adopted	FY 2021 Estimate	FY 2022 Estimate	FY 2023 Estimate	FY 2024 Estimate
(1)	(2)	(3)	(4)	(5)	(6)	(7)
	OPERATIONS OF FISCAL YEAR					
	REVENUES					
1	Taxes	3,636,492	3,766,841	3,877,365	3,985,106	4,077,837
2	Locally Generated Non-Tax Revenues	353,328	314,947	316,376	326,371	319,587
3	Revenue from Other Governments	847,172	877,139	899,389	935,426	980,943
4	Sub-Total (1 thru 3)	**4,836,992**	**4,958,927**	**5,093,130**	**5,246,903**	**5,378,367**
5	Revenue from Other Funds of City	81,011	63,879	65,410	65,883	66,264
6	**Total Revenue and Other Sources (4)+(5)**	**4,918,003**	**5,022,806**	**5,158,540**	**5,312,786**	**5,444,631**
	OBLIGATIONS/APPROPRIATIONS					
7	Personal Services	1,820,084	1,827,596	1,833,217	1,839,141	1,841,407
8	Personal Services-Pensions	749,051	765,734	781,479	800,086	815,114
9	Personal Services-Other Employee Benefits	662,912	671,446	703,275	733,750	766,132
10	**Sub-Total Employee Compensation (7 thru 9)**	**3,232,047**	**3,264,776**	**3,317,971**	**3,372,977**	**3,422,653**
11	Purchase of Services	1,001,325	998,411	1,015,784	1,036,563	1,041,707
12	Materials, Supplies and Equipment	123,682	118,173	113,115	112,483	112,495
13	Contributions, Indemnities, and Taxes	322,432	350,139	363,564	367,147	370,787
14	Debt Service	187,483	189,461	214,845	228,965	253,787
15	Advances & Misc. Pmts. / Labor Obligations	0	20,000	30,000	40,000	50,000
16	Advances & Misc. Pmts. / Federal Grants	55,108	56,705	58,356	58,356	58,356
17	Sub-Total (10 thru 16)	4,922,077	4,997,665	5,113,635	5,216,491	5,309,785
18	Payments to Other Funds	103,189	98,572	91,492	97,047	107,186
19	**Total - Obligations (17)+(18)**	**5,025,266**	**5,096,237**	**5,205,127**	**5,313,538**	**5,416,971**
20	Oper.Surplus (Deficit) for Fiscal Year (6)-(19)	(107,263)	(73,431)	(46,587)	(752)	27,660
21	**Prior Year Adjustments:**					
22	Other Adjustments	19,500	19,500	19,500	19,500	19,500
23	Total Prior Year Adjustments	19,500	19,500	19,500	19,500	19,500
24	**Adjusted Oper. Surplus/ (Deficit) (20)+(23)**	**(87,763)**	**(53,931)**	**(27,087)**	**18,748**	**47,160**
	OPERATIONS IN RESPECT TO PRIOR FISCAL YEARS					
25	Fund Balance Available for Appropriation June 30 of Prior Fiscal Year	297,666	209,903	155,972	128,885	147,633
26	Fund Balance Available for Appropriation June 30 (24)+(25)	**209,903**	**155,972**	**128,885**	**147,633**	**194,793**

See accompanying summaries of significant accounting policies and assumptions and accountant's report.

A. Nature of the Forecast

The City of Philadelphia Office of Budget and Program Evaluation (OBPE) is responsible for providing revenue and obligation estimates to the Director of Finance and the Mayor for discussion and inclusion in the FY2020 budget and the FY2020-2024 Five Year Financial Plan (FYP) submitted by the Mayor to the Pennsylvania Intergovernmental Cooperation Authority (PICA) on June 18, 2019. These financial forecasts present, to the best of management's knowledge and belief, the City of Philadelphia's (City) expected results of operations for the forecast periods. Accordingly, the forecasts reflect the City's judgment as of June 18, 2019, the date of these forecasts, of the expected conditions and its expected course of action. The assumptions disclosed herein are those that management believes are significant to the forecasts. There will usually be differences between the forecasted and actual results because events and circumstances frequently do not occur as forecasted or expected and those differences may be material.

B. Summary of Significant Accounting Policies

The Forecasted General Fund Statements of Operations are presented on the budgetary basis of accounting. The budgetary basis of accounting differs from the modified accrual (Generally Accepted Accounting Principles) basis used in the preparation of the City's governmental fund financial statements in that both expenditures and encumbrances are applied against the current budget, adjustments affecting activity budgeted in prior years are accounted for through fund balance or as a reduction of expenditures and certain interfund transfers and reimbursements are budgeted as revenues and expenditures.

C. Summary of Significant Forecast Assumptions

1. Approach to Revenue Forecasting

The City's estimated general fund revenues for FY20 total $4.918 billion. Approximately 73.9% of the City's revenue comes from local taxes, and 17.2% comes from other governments. Locally generated non-tax revenues, which include fees, fines and permits, account for 7.2% of revenues.

OBPE provides forecasts for the seven major taxes, totaling over $3.636 billion in the adopted FY20 budget, as well as $353.3 million of Locally Generated Non-Tax revenues, and $847.2 million in Revenue from Other Governments. These three sources comprise 98.4% of the revenues anticipated for the FY20 budget.

OBPE employs several approaches to developing its forecasts of local revenues. These include:

a. Forecasts of economic activity provided by several sources including the Congressional Budget Office;

b. Continuous evaluation of national and local economic data on employment, inflation, interest rates, and economic growth;

c. Ongoing examination of the City's current tax receipts;

d. Economic forecasting of tax revenues provided by a revenue forecasting consultant;

e. Analysis and tax history provided by experienced staff within the Philadelphia Department of Revenue;

f. Discussions with economists at a meeting at the Federal Reserve Bank of Philadelphia; and

g. The extensive experience of its staff.

OBPE's tax forecasts for the FYP were developed in conjunction with a revenue forecasting consultant, IHS Markit, Ltd. (IHS). IHS created econometric models which included variables such as wage and salary disbursements in the metropolitan statistical area (MSA) and the county, personal income in the county, the unemployment rate, home prices in the county, real estate transaction growth, and national corporate profits. These models, together with their forecast of the Philadelphia economy, were used by IHS to forecast tax revenues for the City. IHS focused on the following taxes – Wage and Earnings Tax, Net Profits Tax, Business Income and Receipts Tax, Real Estate Transfer Tax, Parking Tax and Sales Tax. These forecasts were refined by OBPE after discussions with economists at a meeting at the Federal Reserve Bank of Philadelphia, as well as with experienced staff within the Department of Revenue. Forecasts for the remaining major taxes – Real Estate and Philadelphia Beverage – were developed using the internal expertise of employees within the City. The Real Estate Tax estimates were forecasted by OBPE with data and input from the Office of Property Assessment and the Department of Revenue. The Philadelphia Beverage Tax estimates were based upon initial collections of this new tax, along with an assumption of a 1% decline in consumption assumed based upon national trends of reduced sugar-sweetened beverage consumption, in consultation with the Department of Revenue.

2. The National and Local Economic Context

The strength of the economy is a key determinant of the fiscal health of the City since tax revenues, which are directly tied to the economy's strength, account for almost 73.9% of the City's General Fund revenue. The Congressional Budget Office (CBO) forecast for U.S. Real Gross Domestic Product shows projected growth of 2.7% for 2019, as compared to 2.9% growth in 2018. Growth is expected to continue to slow slightly in 2020 at 1.9%. The CBO forecast projects domestic economic profits to decrease by 1.8% in 2020.[1]

Wages and salaries are projected to grow at 4.8% in 2019 and 4.7 % in 2020. Unemployment is expected to decline from 3.9% in 2018 to 3.5% in 2019 and then increase to 3.7% in 2020.[2]

According to IHS Markit, the medium-term economic outlook for the city of Philadelphia remains moderately optimistic. The Center City area is doing well, and other neighborhoods are experiencing increased interest, especially in housing markets. Continued expansion of the city and regional economy will require ongoing gains in the labor force at all skill levels through education, access to transportation, affordable housing, and other means. IHS Markit expects total payrolls in the city to expand 0.2% per year on average from 2019 to 2024. Real gross county product looks poised to grow 1.2% on average, while increasing rates of gain in wage rates will improve the outlook for total incomes. Philadelphia's unemployment rate has dipped into the low-5% range, and will continue to press lower over the next couple of years.

3. The City's Major Taxes

The City receives revenue to fund its services and programs from seven major taxes which are budgeted to contribute almost 74% of the expected General Fund revenue in FY20. These include:

1. Wage and Earnings and Net Profit Tax (Wage),
2. Real Property Tax,
3. Business Income and Receipts Tax (BIRT),

[1] Congressional Budget Office, The Budget and Economic Outlook: 2019 to 2029 (January 2019 Report), Page 147.
[2] Congressional Budget Office, The Budget and Economic Outlook: 2019 to 2029 (January 2019 Report), Page 147.

4. Real Estate Transfer Tax (RTT),
5. Sales Tax,
6. Parking Tax, and
7. Philadelphia Beverage Tax.

The remaining taxes, including the amusement tax, are budgeted to provide less than 1% of General Fund revenue. Philadelphia's reliance on the Wage Tax (43.4% of the General Fund, including PICA portion), the BIRT (10.9%) and the Sales Tax (4.6%) places the City at risk from economic trends and employment fluctuations of the local economy. Other cities and counties that rely more heavily on property tax revenues are more susceptible to dramatic shifts in the housing market.

a. Wage Tax

The largest tax revenue source (comprising 44.9% of tax revenues, excluding the PICA portion) is the Wage Tax, which encompasses the wage, earnings, and net profits taxes. The Wage Tax is collected from all employees working within city limits, and all Philadelphia residents regardless of work location. In FY20, the Wage Tax rate has been reduced from 3.8809% to 3.8712% for residents and from 3.4567% to 3.4481% for non-residents. The resident rate includes 1.5% that is reserved for the PICA. PICA has overseen the City's finances since 1992, but under current statute is scheduled to dissolve following the repayment of all outstanding bonds at the close of fiscal year 2023. Revenue projections for fiscal year 2024 assume the City and Commonwealth will work together to extend PICA's existence or, alternatively, that City Council will adopt a Wage Tax rate, independent of the PICA portion, to produce the expected revenue. This FYP maintains the assumption that the 1.5% will continue in FY24. The PICA statute permits the Authority a "first dollar" claim on its portion of Wage Tax proceeds, which is used to pay debt service on bonds issued by PICA for the benefit of the City. Excluding the PICA portion, the Wage Tax and Net Profits Tax is projected to bring in $1.672 billion in FY20. This projection includes a 4.30% growth rate for the Wage and Earnings component and 5.52% growth rate for the Net Profit component of the tax.[3]

[3] Growth rates referenced throughout these notes are applied to the current portion of the tax base.

The City resumed cuts to the Wage Tax in FY14, after those cuts had been suspended during the fiscal crisis, and plans to continue Wage Tax cuts in each year of the FYP if the City's fund balances remains consistent with or higher than those in the FYP. By FY24, the Wage Tax rates in the FYP are 3.8327% for residents and 3.4137% for non-residents.

b. Real Property Tax

The Real Property Tax (Property) is the City's second largest source of tax revenue (19.0%), estimated to contribute $691.0 million of the FY20 tax revenues. This tax is levied on the assessed value of residential and commercial property in the City. The Adopted FY20 Budget has a combined City/School District property tax rate for FY20 of 1.3998%, unchanged from FY19. The City portion of the tax is 0.6317% and the School District portion is 0.7681%. The property tax projection includes an expansion of the homestead exemption from $40,000 of assessed value to $45,000 of assessed value for eligible property owners and the Longtime Owner Occupants Program (LOOP) capped at $30 million of waived revenue for the City and School District combined and additional relief programs. The FYP assumes taxable assessed values grow each year of the plan, based upon regular reassessments provided by the City's Office of Property Assessment. The projection also uses a collection rate of 96.1%, which is based upon the FY18 actual collection rate.

c. Business Income and Receipts Tax

The Business Income and Receipts Tax (BIRT) is projected to produce $497.3 million in FY20, 13.7% of total tax revenue. Most the BIRT is derived from corporate profits which are volatile and dependent on economic conditions within the City. In FY12, BIRT tax reform legislation was enacted, which incorporated several changes intended to help small and medium size businesses grow in Philadelphia. Under Bill 110548, business taxes for the first two years of operations for all new businesses that employ at least three employees in their first year and six in the second would be eliminated beginning in FY13. Bill 110554 provides for across the board exclusions on the gross receipts portion for all businesses scaled in over a three-year period beginning in FY15 and reductions in the net income portion of the BIRT. The first $100,000 of receipts have been excluded since the exclusions were first fully applied in FY17. The bill called for implementation of single sales factor apportionment in FY16. This enables businesses to pay BIRT solely on sales, not on property or payroll. By taxing property and payroll, the BIRT previously had provided disincentives to firms to locate in the city. Lastly, starting in FY20, the BIRT will be collected on a quarterly basis, easing the impact on new businesses.

d. Real Estate Transfer Tax

The Real Estate Transfer Tax (RTT) is projected to provide $339.3 million in FY20. After a strong several years, the base growth of the RTT is projected to grow by 1.37% in FY20. The City currently imposes a 3.278% tax on real property sales and an additional 1% is charged by the Commonwealth for a 4.278% total RTT.

e. Sales Tax

Sales Tax revenues are projected to generate $227.9 million for the City's general fund in FY20, based on a growth rate of 3.8%, and comprising 6.3% of tax revenues. As part of its response to projected City budget deficits in 2009, the Commonwealth of Pennsylvania (the Commonwealth) provided authorization and the City passed legislation to temporarily increase the Sales Tax rate from 1% to 2% through the end of FY14. This raised the total Sales Tax rate to 8%, with 6% going to the Commonwealth and 2% to the City. The tax was made permanent starting in FY15 with 1% of the local Sales Tax being for the benefit of the School District of Philadelphia and the City's pension fund whereby $120 million of the sales tax goes directly to the School District and remaining amounts flow through the City's General Fund to pay for debt service on a borrowing on behalf of the School District and for additional contributions to the Pension Fund. In FY20, the debt service on the borrowing is complete, and therefore all of the proceeds above the $120 million in Sales Tax receipts from the second 1% is going to the City's Pension Fund (projected to be $53.9 million). From FY20 through FY24, the City's pension fund is projected to receive $323.3 million from the proceeds of the Sales Tax.

f. Parking Tax

The Parking Tax is levied on the gross receipts from all parking transactions. Parking Tax revenue is projected to generate $100.2 million in FY20, based on prior-year revenue history and local economic trends.

g. Philadelphia Beverage Tax

The Philadelphia Beverage Tax is a relatively new revenue source, applied to non-retail distributions of both sugar-sweetened and diet beverages, at a rate of one and one-half cents per fluid ounce of sweetened beverages. Original tax estimates were developed by the City's Department of Revenue, and utilized local consumption data provided by the University of Connecticut's Rudd Center for Food Policy and Obesity, along with a -1-elasticity rate. The projections in the FYP were based upon past receipts, reduced by 1% annually, in line with national trends on consumption. The tax was effective January 1, 2017 and is projected to impact revenues and expenditures in the following ways:

- An estimated $371.9 million will be collected in gross revenue from FY20-FY24, before additional costs for collection, advertising and auditing.
- Revenues from the Philadelphia Beverage Tax is funding expenditures for three major initiatives: expanded Pre-K, community schools, and debt service for the Rebuilding Community Infrastructure program when those programs are fully implemented.

City of Philadelphia
General Fund
FY 2020 - 2024 Five Year Financial Plan
Major Taxes ($ in Millions) with Percentage Change from Previous Year

Tax	Actual FY18	Projected FY19	Projected FY20	Projected FY21	Projected FY22	Projected FY23	Projected FY24
Wage & Net Profits - Current & Prior	1,574.6	1,602.8	1,671.9	1,731.1	1,790.0	1,850.7	1,909.9
% change from prior year	n.a.	1.8%	4.3%	3.5%	3.4%	3.4%	3.2%
Real Property - Current & Prior	650.4	689.4	690.9	730.2	754.6	780.6	810.2
% change from prior year	n.a.	6.0%	0.2%	5.7%	3.3%	3.4%	3.8%
Business Income & Receipts - Current & Prior	446.1	503.3	497.3	512.3	512.4	507.1	516.4
% change from prior year	n.a.	12.8%	-1.2%	3.0%	0.0%	-1.0%	1.8%
Sales	198.4	215.2	227.9	238.7	249.5	260.5	269.9
% change from prior year	n.a.	8.5%	5.9%	4.7%	4.5%	4.4%	3.6%
Real Property Transfer	331.5	334.7	339.3	343.1	357.4	370.6	353.6
% change from prior year	n.a.	1.0%	1.4%	1.1%	4.2%	3.7%	-4.6%
Parking	96.5	98.1	100.2	102.1	104.0	105.9	107.8
% change from prior year	n.a.	1.7%	2.1%	1.9%	1.9%	1.8%	1.8%
Other Taxes	26.9	32.2	33.1	34.2	35.1	36.1	37.1
% change from prior year	n.a.	19.7%	2.8%	3.3%	2.6%	2.8%	2.8%
Philadelphia Beverage	77.4	76.6	75.9	75.1	74.4	73.6	72.9
% change from prior year	n.a.	-1.0%	-0.9%	-1.1%	-0.9%	-1.1%	-1.0%
Total Taxes	**3,401.8**	**3,552.3**	**3,636.5**	**3,766.8**	**3,877.4**	**3,985.1**	**4,077.8**
% Change from prior year	**10.8%**	**4.4%**	**2.4%**	**3.6%**	**2.9%**	**2.8%**	**2.3%**

Note: Wage & Net Profits Taxes include rate reductions that resumed in FY14. Business Income & Receipts Tax incorporate rate reductions that began in FY13. Wage tax does not include the PICA portion. Real Property Transfer Tax includes the rate increase from 3.1% to 3.278% effective July 1, 2018.

4. Locally Generated Non-Tax Revenues

Locally Generated Non-Tax Revenues are forecasted based on historical trends, rate changes, and current collection patterns. Certain revenues such as interest earnings, licenses and permits and recording fees are subject to economic conditions and are estimated accordingly.

5. Revenue from Other Governments

Revenue from Other Governments is forecasted based on historical trends and state and federal budget information. The PICA City account, which represents 58.9% of Revenue from Other Governments, is forecasted using Wage Tax variables.

6. Obligation Estimates

OBPE provided obligation estimates to the Director of Finance and the Mayor for discussion and inclusion in the revised annual FY2020 budget and FY2020-2024 FYP submitted by the Mayor to the PICA on June 18, 2019. OBPE provides forecasts of all major expenditure categories. Obligations total $5.025 billion, an increase of $192.5 million over the FY19 estimate. A handful of items account for much of that increase: pensions; the School District contribution; employee disability; disposal contracts, which have been driven up by global markets; a contribution to the budget stabilization reserve fund; and expansion of Pre-K and Community Schools with the resolution of the litigation challenging the Philadelphia Beverage Tax.

a. Labor Agreements

The forecasted statements include:

- The final contract pay raise for AFSCME DC33 of 3% in FY20 and a one-time $11 million lump sum payment to the union's health and welfare fund in FY20.
- Per the FY18 to FY20 arbitration award for the Fraternal Order of Police (FOP), a 3.75% increase in FY20.
- Per the FY18 to FY20 arbitration award for the International Association of Fire Fighters (IAFF), a 3.75% in FY20. Fire fighters also received an increase to premium pay rates of an additional 0.2 hours per week in FY20.

- Per the FY18 to FY20 arbitration award for Deputy Sheriffs and Register of Wills employees, a 3.25% increase in FY20 for Deputy Sheriffs. Register of Wills employees received wage increases in line with District Council 33: 3% in FY20.

- Per the FY18 to FY20 arbitration award for the Correctional Officers, Local 159 of AFSCME DC33, a 3.25% increase in FY20.

- Per the FY17-FY20 collective bargaining agreement with AFSCME DC47, a 3% increase in FY20 and a one-time lump sum payment of $1 million to the union's health and welfare fund in FY20.

The City has set aside $140 million from FY20 to FY24 in a labor reserve, to cover the costs associated with upcoming labor agreements as all of the union contracts and arbitration awards expire on June 30, 2020.

b. Health / Medical

The Administration implemented a self-insured group health plan in 2010 for medical benefits for non-union employees. The City also increased employee copays and instituted a disease management and wellness program with financial incentives for completing wellness activities. In FY15, the City added a tobacco user surcharge. The City has assumed a 5% annual growth in costs for the City Administered Plan.

DC47, the IAFF, and the FOP have also implemented self-insured group health plans. For the FOP, because the City has no control over the design of the its health plan, an increase of 7.5% per year based on medical cost trends has been included. For DC47, an increase of 5.0% per year based on medical cost trends has been included, and the recent agreement also included one-time lump sum payments to their fund in FY18, FY19, and FY20. For FY20, the City will contribute of $1 million in FY20.

AFSCME District Council 33 (DC33) projections are based on prior year expenditures. Under the new contract, there was a reopener to determine payments to the union health and welfare fund for FY19 and FY20. In FY20, the City will make an $11 million payment to the fund.

c. Pensions

As part of the effort to control major cost drivers and to improve the health of the pension fund, several changes have been made over the past few years. The City continues to seek ways to improve the long-term health of the fund.

The City's Act 111 interest arbitration awards with the FOP, Lodge No. 5 and IAFF, Local 22 both require most current members to make additional contributions to the pension fund of 0.92% starting in FY18 and an additional 0.92% in FY19, for a combined 1.84% additional contributions. New hires are now required to make an additional 2.5% contribution above rates in effect prior to the arbitration award.

Significant pensions changes were also included in the DC47 collective bargaining agreement, closely mirroring the earlier reforms agreed to with DC33. Effective in January 2019, current employees began participating in a tiered contribution system where those with higher annual salaries will pay higher contribution rates. New employees are now mandatory members of a stacked hybrid plan under which employees will receive a traditional defined benefit pension on their first $65,000 of salary as well as the option to participate in a voluntary defined contribution plan. These reforms have been applied to employees who are not represented by a union, which means that all City employees will be participating in strengthening the pension fund.

In addition to the abovementioned changes in pension benefits, the City's pension fund has also undergone the following changes:

- The City continues to make at least its full minimum municipal obligation (MMO) each year and has dedicated a portion of additional revenues to the fund. Under 2014 state legislation, the additional 1% local sales tax provides funding for the School District of Philadelphia (first $120 million), debt service on a four-year borrowing for the District (next $15 million through which was satisfied in FY18), and any remaining funds are dedicated to the pension fund. From FY20 through FY24, the City's pension fund is projected to receive $323.3 million from the proceeds of the Sales Tax. The Sales Tax revenues will supplement the City's MMO payment rather than supplanting a portion of it.

- The City also created the Revenue Recognition Policy under which the Sales Tax revenue and additional employee contributions achieved through collective bargaining and interest arbitration are to be paid above the City's annual required contribution to the pension fund. This means that the City will pay more than what is legally required each year to improve the funding status of the plan more quickly.

- Over the past eleven years, reduced the pension fund's earnings assumption from 8.75% to 7.60%, with an additional reduction to 7.55% scheduled for July 1, 2020. Lower earnings assumptions allow funds to moderate the risk of their investments, which can also reduce the likelihood of losses. In addition, lower earnings assumptions increase the amount the City is required to contribute to the pension fund, which improves the fund's health.

The net impact of these changes to the City's pension benefits and fund is to moderate what would have been devastating increases in pension costs and to increase the City's ability to fund existing liabilities in the long term. The specific changes to the pension fund assumptions have been tested by the City's actuary and have been determined to be actuarially sound. The pension amounts included in the FYP are provided by the City's actuary and are higher than the amounts required to be paid under state law.