CITY OF PHILADELPHIA

OFFICE OF THE CONTROLLER
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REBECCA RHYNHART
City Controller

Thursday, July 16, 2020

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, 2021 through June 30, 2025. 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 29, 2020. 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 three causes for concern that PICA should take into consideration while evaluating the Plan. Philadelphia, like cities across the country, is facing simultaneous public health and fiscal crises. The magnitude of the ultimate economic impact of the COVID-19 pandemic and the scale of the subsequent recovery remain unknown. As discussed below, our office estimates a more conservative recovery in revenues beginning in fiscal year (FY) 2022, particularly for the Business Income and Receipts Tax (BIRT). Furthermore, the Plan relies on a substantial revenue stream from the PICA Tax in FY24 and FY25, after the scheduled dissolution of PICA. The City has provided no concrete steps to remedy this matter, which our office first noted in our review of last year's Plan.

Sensitive Assumptions

In the recovery from the COVID-19 pandemic, the City anticipates a 30 percent growth rate for BIRT in FY22, representing a single-year increase of about $142M. While the tax base for BIRT has been historically volatile, this would represent the largest year-over-year increase in BIRT receipts in recent history. Our office's anticipated growth rate is substantially more conservative and given the Plan's low projected fund balance in FY22, the City's assumed rate warrants concern.

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 more than $5B in Wage and Net Profits Tax revenue in FY24 and FY25, inclusive of $1.3B 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.

Causes for Concern

Beginning in FY22, our office's revenue projections are more conservative than the Budget Office's estimates, resulting in a difference of nearly $700M over the life of the Plan. In particular, our office's projections indicate a weaker post-pandemic recovery driven primarily by BIRT receipts (as noted above) but also lower collections for the Sales, Wage, and Parking taxes in the later years of the Plan. Given the unprecedented uncertainty in both the national and global economies, our office believes that the current economic climate warrants fiscal prudence when appropriating for the future.

The Plan includes about $75M in reduced General Fund debt service in FY21 due to a restructuring of the City's pension obligation bonds. Financing operating expenses through debt restructuring is a practice that should generally be avoided if possible. While the City has noted that it would forego the restructuring if direct federal aid were to become available, the adopted Plan relies on this debt service savings in FY21 rather than spending reductions in other areas to meet its projected fund balance.

The City's annual contribution to the School District is expected to grow over the life of the plan from $253M in FY21 to $288M in FY25. Over the lifetime of the Plan, the City budgeted for $1.4B in contributions to the School District, an increase relative to last year's Plan. If the City's economic recovery from the current crisis is weaker than anticipated, these promised contributions may place significant strain on City resources, forcing difficult choices regarding funding for vital City services.

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, Finance Director
Marisa Waxman, Budget Director

City of Philadelphia
Forecasted General Fund
Statements of Operations
Fiscal Years 2021-2025

City Controller
Rebecca Rhynhart

July 21, 2020

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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, 2025, 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 two assumptions that are particularly sensitive as described in the footnotes contained herein. 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. Additionally, while the tax base for the City's Business Income and Receipts Tax (BIRT) has been historically volatile, the City anticipates an outlying 30% growth rate for BIRT in FY 22 that, in the wake of the Covid-19 pandemic, is considerably higher than our anticipated growth rate for that year or subsequent years.

Christy Brady

CHRISTY BRADY, CPA
Deputy City Controller
Philadelphia, Pennsylvania
July 16, 2020

Forecasted General Fund Statements of Operations

Fiscal Years Ending June 30, 2021 through June 30, 2025

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, 2021 through June 30, 2025

(Amounts in thousands)

NO.	ITEM	FY 2021 Adopted	FY 2022 Estimate	FY 2023 Estimate	FY 2024 Estimate	FY 2025 Estimate
(1)	(2)	(3)	(4)	(5)	(6)	(7)
	OPERATIONS OF FISCAL YEAR					
	REVENUES					
1	Taxes	3,330,098	3,699,848	3,903,572	4,049,008	4,193,105
2	Locally Generated Non-Tax Revenues	357,890	387,499	360,806	362,971	423,306
3	Revenue from Other Governments	768,197	832,395	882,596	929,647	953,808
4	Sub-Total (1 thru 3)	**4,456,185**	**4,919,742**	**5,146,974**	**5,341,626**	**5,570,219**
5	Revenue from Other Funds of City	125,608	61,772	63,315	63,801	64,311
6	**Total Revenue and Other Sources (4)+(5)**	**4,581,793**	**4,981,514**	**5,210,289**	**5,405,427**	**5,634,530**
	OBLIGATIONS/APPROPRIATIONS					
7	Personal Services	1,795,159	1,810,270	1,831,769	1,908,238	1,908,595
8	Personal Services-Pensions	650,183	748,149	770,897	789,179	807,892
9	Personal Services-Other Employee Benefits	636,976	673,882	704,445	740,466	773,773
10	**Sub-Total Employee Compensation (7 thru 9)**	**3,082,318**	**3,232,301**	**3,307,111**	**3,437,883**	**3,490,260**
11	Purchase of Services	948,562	957,186	993,885	1,082,616	1,087,215
12	Materials, Supplies and Equipment	117,304	97,532	97,163	126,963	113,898
13	Contributions, Indemnities, and Taxes	378,737	374,830	389,858	407,067	406,965
14	Debt Service	185,714	203,916	216,115	235,167	245,496
15	Advances & Misc. Pmts. / Labor Obligations	0	25,000	45,000	65,000	65,000
16	Adv. & Misc. Pmts. / Reopening and Recession Reser	25,000	55,000	30,000	25,000	25,000
17	Sub-Total (10 thru 16)	4,737,635	4,945,765	5,079,132	5,379,696	5,433,834
18	Payments to Other Funds	67,216	55,775	60,182	69,422	108,059
19	**Total - Obligations (17)+(18)**	**4,804,851**	**5,001,540**	**5,139,314**	**5,449,118**	**5,541,893**
20	Oper.Surplus (Deficit) for Fiscal Year (6)-(19)	(223,058)	(20,026)	70,975	(43,691)	92,637
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)**	**(203,558)**	**(526)**	**90,475**	**(24,191)**	**112,137**
	OPERATIONS IN RESPECT TO PRIOR FISCAL YEARS					
25	Fund Balance Available for Appropriation June 30 of Prior Fiscal Year	254,908	51,350	50,824	141,299	117,108
26	Fund Balance Available for Appropriation June 30 (24)+(25)	**51,350**	**50,824**	**141,299**	**117,108**	**229,245**

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

Notes to the Forecasted General Fund Statements of Operations Fiscal Years Ending June 30, 2021 through June 30, 2025

A. Nature of the Forecast

The City of Philadelphia Budget Office (Budget) is responsible for providing revenue and obligation estimates to the Director of Finance and the Mayor for discussion and inclusion in the FY2021 budget and the FY2021-2025 Five Year Financial Plan (FYP) submitted by the Mayor to the Pennsylvania Intergovernmental Cooperation Authority (PICA) on June 29, 2020. 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 29, 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 Account Principles

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 FY21 total $4.581 billion. Approximately 72.7% of the City's revenue comes from local taxes, and 16.8% comes from other governments. Locally generated non-tax revenues, which include fees, fines and permits, account for 7.8% of revenues.

Budget provides forecasts for the seven major taxes, totaling over $3.33 billion in the adopted FY21 budget, as well as $357.9 million of Locally Generated Non-Tax revenues, and $768.2 million in Revenue from Other Governments. These three sources comprise 97.3% of the revenues anticipated for the FY21 budget.

Budget 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.

Budget'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 Budget 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 Budget 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. We believe that the additional decline in FY20 is related to COVID-19 and won't be entirely permanent as the economy reopens.

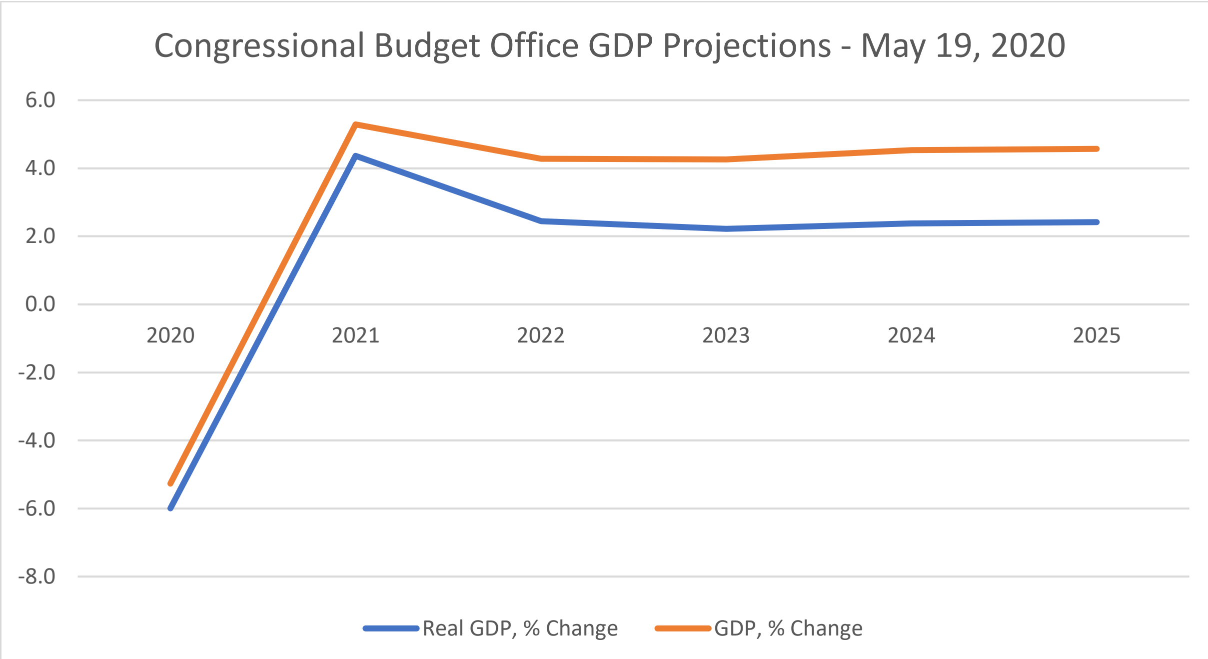
Due to the global health crisis and economic shut-down that ensued, the FY21-25 revenue projections were updated twice since the initial introduction in March; first for May 1st and then again on June 15th. These revisions were based on updated collections information, updated projections from IHS, additional discussions with economists convened by PICA and the Federal Reserve, and continuous evaluation of national and local economic data on employment, inflation, interest rates, and economic impacts from the COVID-19 and civic unrest.

Prior to the impacts of COVID-19, Philadelphia's medium-term economic outlook was moderately optimistic. Wage Tax revenue was projected to remain stable as IHS Markit, the City's economic consultants, projected payroll growth to continue to grow next year as a result of very solid gains in number of employees. However, IHS expected total payroll growth to downshift significantly in 2021 and beyond, as the region reached full employment. In line with its prediction for the U.S., IHS predicted that Philadelphia's Real Gross Metropolitan Product growth would also slow over the next few years, from 1.9% growth in 2020, to 1.7% growth in 2021, and to 1.2% growth in 2022 and 2023. Sales tax collections were up 6.3% for the first half of FY20, compared to the prior year, low unemployment, solid growth in personal income, and a stable housing market were supportive of growth in consumer spending. Realty Transfer Tax collections through the third quarter of FY20 were 19% higher than collections through the third quarter of FY19 ($262M versus $221M)..

However, even prior to COVID-19, while Philadelphia was much better prepared for a recession than it was in 2008, Moody's Recession Preparedness report released in December 2019 found that, like most of the 25 largest cities in the country, Philadelphia was only moderately prepared for a recession. Updated projections show that the COVID-19 outbreak has and will continue to significantly impact the local economy. The three largest drivers of Philadelphia's economy are educational institutions, medical institutions, and hospitality. Educational and medical institutions are relatively stable and account for 32% of the total Philadelphia workforce. The leisure and hospitality sector, the most vulnerable to the effects of social distancing measures, employs a much smaller proportion of the total workforce, but its contraction disproportionately impacts low wage workers. As the Wage Tax is the City's main revenue source, there will be significant shortfalls in revenue due to the higher rates of unemployment, as well as losses due to non-residents continuing to work from home, which when required by the employer eliminates the obligation to pay the Wage Tax. Projections show a weakening for Sales Tax, Real Estate Tax, Business Income and Receipts Tax, Realty Transfer Tax, and others.

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 72.7% of the City's General Fund revenue. In May 2020, the Congressional Budget Office (CBO) forecast for U.S. Real Gross Domestic Product shows projected decline of -5.6% for 2020. Growth is expected to return to being positive in 2021 at 4.2%. Annual unemployment is expected to increase to 11.5% in 2020 and then decline to 9.3% in 2021. CBO estimates for corporate net incomes, wages and salaries were last projected in January 2020 and are no longer relevant to include here due to the impacts of COVID-19. The CBO will be updating their projections for 2020 and 2021 in July 2020, after the development of these revenue estimates.



[1]

On June 1, 2020, IHS provided updated projections for the national, state, and city domestic product, indicating a relatively better outlook for the City of Philadelphia compared to Pennsylvania and the country due to the concentration in the health and finance sectors, and comparatively lower dependence of harder hit industries like hospitality and retail.

Economic Indicators: National, State, and City

	2019Q4	2020Q1	2020Q2	2020Q3	2020Q4	2019	2020	2021
United States								
Employment (millions)	151.8	152.1	124.4	121.2	124.8	150.9	130.6	136.2
Real Per Capita Income (Thousand $)	45.5	45.5	46.4	47.7	46.2	45.4	46.5	46.3
GDP Growth Rate (%)	2.1	-4.8	-36.5	6.1	9.4	2.3	-7.3	5.1
Pennsylvania								
Employment (millions)	6.08	6.09	4.90	4.79	4.91	6.07	5.18	5.30
Real Per Capita Income (Thousand $)	59.4	59.5	58.5	60.3	59.1	58.8	59.4	60.0
GSP Growth Rate (%)	2.1	-6.2	-40.6	7.4	11.4	2.3	-8.5	5.5
Philadelphia City								
Employment (thousands)	744.2	752.0	612.8	609.3	627.5	737.9	650.4	673.7
Real Per Capita Income (Thousand $)	51.5	51.7	51.2	53.3	51.8	51.2	52.0	52.1
GMP Growth Rate (%)	3.8	-3.8	-39.2	12.5	12.5	3.8	-6.5	6.4

[2]

[1] https://www.cbo.gov/publication/56351

[2] IHS Markit projections from June 1, 2020.

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 72.7% of the expected General Fund revenue in FY21. These include:

1. Wage and Earnings and Net Profit Tax (Wage),
2. Real Property Tax,
3. Business Income and Receipts Tax (BIRT),
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 (40.9% of the General Fund, including the PICA portion), the BIRT (9.6%) and the Sales Tax (3.0%) 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 46.5% 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 FY21, the Wage Tax rate has been held at 3.8712% for residents and increased 3.4481% to 3.5019% 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 years 2024 and 2025 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 and FY25.

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 $1.549 billion in FY21. This projection includes a -6.0% growth rate for the Wage and Earnings component and -22.28% growth rate for the Net Profit component of the tax.[3]

The City plans to sunset the increase to the non-resident Wage Tax rate after one year and resume Wage Tax cuts again in FY24 if the City's fund balances remains consistent with or higher than those in the FYP. By FY25, the Wage Tax rates in the FYP are 3.8519% for residents and 3.4309% for non-residents.

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

b) Real Property Tax

The Real Property Tax (Property) is the City General Fund's second largest source of tax revenue (20.5%), estimated to contribute $684.3 million of the FY21 tax revenues. This tax is levied on the assessed value of residential and commercial property in the City. The Adopted FY21 Budget has a combined City/School District property tax rate for FY21 of 1.3998%, unchanged from FY20. The City portion of the tax is 0.6317% and the School District portion is 0.7681%. The property tax projection includes the ending of the 1% discount for those who pay their bill by the last day of February. This revenue enhancement is anticipated to generate an additional $5.7M in FY21. 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 lowers the collection rate to 91.0% in FY21 because of the COVID-19 pandemic, but incrementally increases the collection rate to the FY19 level of 96.1% by the end of the FYP.

c) Business Income and Receipts Tax

The Business Income and Receipts Tax (BIRT) is projected to produce $464.3 million in FY21, 13.9% 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. Starting in FY20, the BIRT was collected on a quarterly basis, easing the impact on new businesses. Finally, in FY21 planned rate decreases to the net income portion of the BIRT were suspended; however, these rates decreases are planned to begin again in FY24.

d) Real Estate Transfer Tax

The Real Estate Transfer Tax (RTT) is projected to provide $292.8 million in FY21. After several strong years and largely due to the COVID-19 pandemic, the base growth of the RTT is projected to contract by -6.59% in FY21. 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 $174.5 million for the City's general fund in FY21, based on a growth rate of -6.27%, and comprising 5.2% 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 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 $27.3 million). From FY21 through FY25, the City's pension fund is projected to receive $225.3 million from the proceeds of the Sales Tax.

f) Parking Tax

The Parking Tax is levied on the gross receipts from all parking transactions. In FY21 only, the Parking Tax rate has been increased from 22.5% to 25.0%. Through the remainder of the FYP the Parking Tax rate will revert to 22.5%. Parking Tax revenue is projected to generate $76.7 million in FY21, based on lowered expectations prompted by the COVID-19 pandemic.

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 IHS Markit input, but closely align 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 $336.2 million will be collected in gross revenue from FY21-FY25, 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 2021 - 2025 Five Year Financial Plan
Major Taxes ($ in Millions) with Percentage Change from Previous Year

Tax	Actual FY19	Projected FY20	Projected FY21	Projected FY22	Projected FY23	Projected FY24	Projected FY25
Wage & Net Profits - Current & Prior	1,617.7	1,639.9	1,549.0	1,680.4	1,793.6	1,859.3	1,921.3
% change from prior year	n.a.	1.4%	-5.5%	8.5%	6.7%	3.7%	3.3%
Real Property - Current & Prior	696.6	691.5	684.3	731.7	765.4	797.4	829.5
% change from prior year	n.a.	-0.7%	-1.0%	6.9%	4.6%	4.2%	4.0%
Business Income & Receipts - Current & Prior	540.9	514.0	464.3	605.9	631.1	653.1	676.6
% change from prior year	n.a.	-5.0%	-9.7%	30.5%	4.2%	3.5%	3.6%
Sales	224.2	194.2	174.5	198.6	214.4	225.9	237.1
% change from prior year	n.a.	-13.4%	-10.1%	13.8%	8.0%	5.4%	5.0%
Real Property Transfer	328.4	313.5	292.8	301.3	313.8	325.5	337.7
% change from prior year	n.a.	-4.5%	-6.6%	2.9%	4.1%	3.7%	3.7%
Parking	99.3	80.7	76.7	83.3	86.0	88.3	90.9
% change from prior year	n.a.	-18.7%	-5.0%	8.6%	3.2%	2.7%	2.9%
Other Taxes	30.8	23.2	21.1	30.6	31.9	32.6	33.6
% change from prior year	n.a.	-24.7%	-9.1%	45.0%	4.2%	2.2%	3.1%
Philadelphia Beverage	76.9	65.8	67.4	68.0	67.4	66.9	66.4
% change from prior year	n.a.	-14.4%	2.4%	0.9%	-0.9%	-0.7%	-0.7%
Total Taxes	**3,614.8**	**3,522.8**	**3,330.1**	**3,699.8**	**3,903.6**	**4,049.0**	**4,193.1**
% Change from prior year	**6.3%**	**-2.5%**	**-5.5%**	**11.1%**	**5.5%**	**3.7%**	**3.6%**

Note: Wage & Net Profits Taxes include a one-year non-resident rate increase in FY21 and the resumption of rate decreases in FY24. Wage tax does not include the PICA portion. Business Income & Receipts Tax rate reductions will be paused in FY21 and then restarted in FY24. Parking Tax includes a one-year rate increase from 22.5% to 25% effective July 1, 2020.

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 61.3% of Revenue from Other Governments, is forecasted using Wage Tax variables.

6. Obligation Estimates

The Budget Office provided obligation estimates to the Director of Finance and the Mayor for discussion and inclusion in the revised annual FY2021 budget and FY2021-2025 FYP submitted by the Mayor to the PICA on June 29, 2020. The Budget Office provides forecasts of all major expenditure categories. Obligations total $4.805 billion, a decrease of $282.4 million over the FY20 estimate. A broad array of budget cuts were necessary to meet this requirement, however, a handful of items play a more prominent role: the restructuring of the pension obligation payment; decreased Sales Tax contribution to the pension fund resulting from reduced Sales Tax collections; lower School District contribution than the initial budget, but still $30 million more than the FY20 level); decreased health and medical costs; and the reevaluation of the Police, Fire and Prisons funding levels.

a) Labor Agreements

The forecasted statements include:

- A one-year extension for AFSCME DC33 which includes a 2% salary increase beginning May 1st of FY20, as well as, an attendance related bonus of either $750 or $475 per full-time member and a $250 bonus for School Crossing Guards and part-time members due June 1st. The amount of the bonus will be offset by lower health and welfare payments to the union in FY21.

- A one-year extension for the Fraternal Order of Police (FOP) which includes a 2.5% salary increase, as well as, a bonus of $750 per member due July 1st. In addition, the City is responsible for 50% of health and medical payments to the Law Enforcement Health Benefits (LEHB) of any expenses for administrative or claims incurred in the month of July 2020.

- A one-year extension for the International Association of Fire Fighters (IAFF) which includes a 2.5% salary increase beginning May 1st of FY20.

- A one-year extension for Deputy Sheriffs and Register of Wills employees which includes 2.25% salary increase beginning May 1st of FY20 for Deputy Sheriffs, as well as, a $400 bonus per member due July 1st. Register of Wills employees received wage increases in line with District Council 33 with no attached bonus: 2% as May 1st of FY20.

- A one-year extension for the Correctional Officers, Local 159 of AFSCME DC33 which includes a 2.25% salary increase beginning May 1st of FY20, as well as, an attendance related bonus of either $750 or $475 per member due June 1st. The amount of the bonus will be offset by lower health and welfare payments to the union in FY21.

- A one-year extension for AFSCME DC47 which includes a 2% salary increase beginning May 1st of FY20, as well as, an attendance related bonus of either $750 or $475 per member due June 1st. The amount of the bonus will be offset by lower health and welfare payments to the union in FY21.

- The City has set aside $200 million from FY21 to FY25 in a labor reserve, to cover the costs associated with upcoming labor agreements as all union contracts and arbitration awards expire on June 30, 2021.

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 and IAFF, 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.

AFSCME District Council 33 (DC33) projections are based on current year expenditures. As part of one-year contract extensions, a reduction in payments to the health and welfare funds for DC47 and DC33 is offset by bonuses to its members and a 50% reduction in payments to LEHB for expenses incurred in the month of July 2020

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 more than 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 FY21 through FY25, the City's pension fund is projected to receive $225.3 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 7.55%. 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 could 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.

The City is planning to restructure the Pension Obligation Bond (POB) payment due in FY21 that results in a postponement of $74.9M for the general fund from FY21 to future years and will result in additional interest payments.

D. Contingency Plan for Reduced Revenues

The global health pandemic COVID-19 and ensuing economic shut-down has led to unprecedented uncertainty around the local, state, national and world economies. Part of the uncertainty for Philadelphia stems from the delayed payment deadline for the Business Income and Receipts Tax for Tax Year 2019, which are counted as FY20 revenues. While the impacts of the pandemic would not affect the amounts due for Tax Year 2019, businesses' ability to pay and estimates for Tax Year 2020 are certainly affected and there are longer term impacts that are virtually impossible to predict with precision.

This uncertainty has led a gap between the tax collection projections included in the FY21-FY25 Five Year Plan, based on guidance of outside economic consultants, IHS Markit, and those made by PICA's external consultant. While over the life of the plan, the gap is minimal, at less than 1% of total tax collections, the timing of the differences on a year-by-year basis makes it prudent for the City to have a contingency plan in place, as outlined in the attached addendum, should the actual revenue collections be closer to the projections made by PICA's economist than to those included in the FY21-FY25 Five Year Plan. The contingency actions in the attached addendum would bring the FY21-FY25 Five Year Plan into balance in each year. It is possible, however, that after the FY20 BIRT numbers are known, the City would implement more or different measures to ensure that the Plan stayed balanced.

The City's contingency measures include recognizing known underspends of funds in FY20, utilizing reserves set aside for reopening the economy, recessions, and future labor contracts, delaying or reducing new initiatives not yet started, like Public Safety Enforcement Officers. With these measures, the City can still achieve a balanced plan and positive annual fund balances in each year of the FY21-25 Plan. Additionally, the Administration may pursue revenue enhancements in FY22 and beyond, like extending the Parking and non-resident Wage Tax increases beyond FY21 which would generate $22.5 million in FY22, but as those extensions require Council approval, they are not included in the contingency plan.

Contingency Plan for Reduced Revenues in the FY21-25 Five Year Financial Plan						
in millions	FY2020	FY2021	FY2022	FY2023	FY2024	FY2025
FY21-FY25 Five Year Plan Fund Balance	$ 254.91	$ 51.35	$ 50.82	$ 141.30	$ 117.11	$ 229.25
Fund Balance with PICA Projections	$ 218.47	$ (75.11)	$ (22.85)	$ 85.52	$ 117.62	$ 313.95
Fund Balance with Contingency Measures	$ 264.87	$ 23.65	$ 23.75	$ 86.75	$ 71.37	$ 272.22