CITY OF PHILADELPHIA

OFFICE OF THE CONTROLLER
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REBECCA RHYNHART
City Controller

July 16, 2021

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, 2022 through June 30, 2026. 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, 2021. 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 one sensitive assumption and two causes for concern that PICA should take into consideration while evaluating the Plan. Philadelphia, like cities across the country, has experienced unprecedented public health and fiscal crises since March 2020. With public health restrictions recently coming to an end, the city's recovery is now underway, but the ultimate timeline and scale of the recovery remain unknown. In the face of this uncertainty, our office finds the City's revenue forecasts to be appropriately conservative and in good agreement with our independent forecasts. However, the Plan relies on a substantial revenue stream from the PICA Tax in the final three fiscal years of the Plan, 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 the FY20-FY24 Plan.

Sensitive Assumption

As noted in the accountant's report, 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 $7B in Wage and Net Profits Tax revenue for FY24 through FY26, inclusive of $1.8B 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

Over the life of the Plan, the City has set aside $200M for future labor obligations. Such provisions should anticipate future labor negotiations between the City and corresponding bargaining units following the expiration of contracts with each union at the close of the fiscal year. With all four major union contracts being renegotiated, it is our view that the budgetary allocations as specified in the Plan do not adequately account for the likely cost, particularly in final years of the Plan.

The City's annual contribution to the School District is expected to grow over the life of the plan from $256M in FY22 to $288M in FY26, with a total contribution of $1.4B over the five years. If the City's economic recovery in the coming years is weaker than anticipated, these promised contributions may place significant strain on City resources, forcing difficult choices regarding funding for vital City services. While funding through the American Rescue Plan has alleviated short-term budgetary concerns for the School District, the District's latest adopted Plan includes a negative $378M operating deficit and negative $215M fund balance in FY26. This structural deficit could require increased City contributions to resolve, placing additional pressure on City finances in 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
Marisa Waxman, Budget Director
Christy Brady, Deputy Controller of Audit

City of Philadelphia Forecasted General Fund Statements of Operations Fiscal Years 2022-2026

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, 2026, 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, and footnote C.3.a), include an assumption that is particularly sensitive. The Wage Tax rate includes 1.5 percent that is reserved for PICA. PICA is scheduled to dissolve at the end of fiscal year 2023, yet the revenue projections in the plan assume that the 1.5 percent will continue in FY 24 and beyond. The plan assumes that the state will enact legislation to reinstate PICA or, alternatively, City Council will pass legislation to increase the wage tax to produce the expected revenue.

Christy Brady

CHRISTY BRADY, CPA
Deputy City Controller
Philadelphia, Pennsylvania
July 16, 2021

Forecasted General Fund Statements of Operations

Fiscal Years Ending June 30, 2022 through June 30, 2026

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, 2022 through June 30, 2026

(Amounts in thousands)

NO.	ITEM	FY 2022 Adopted	FY 2023 Estimate	FY 2024 Estimate	FY 2025 Estimate	FY 2026 Estimate
(1)	(2)	(3)	(4)	(5)	(6)	(7)
	OPERATIONS OF FISCAL YEAR					
	REVENUES					
1	Taxes	3,417,808	3,655,899	3,822,298	3,979,875	4,121,199
2	Locally Generated Non-Tax Revenues	364,391	327,914	314,230	312,645	368,030
3	Revenue from Other Governments	829,140	856,904	905,429	933,842	962,409
4	Sub-Total (1 thru 3)	**4,611,339**	**4,840,717**	**5,041,957**	**5,226,362**	**5,451,638**
5	Revenue from Other Funds of City	645,906	488,418	311,922	211,773	62,070
6	**Total Revenue and Other Sources (4)+(5)**	**5,257,245**	**5,329,135**	**5,353,879**	**5,438,135**	**5,513,708**
	OBLIGATIONS/APPROPRIATIONS					
7	Personal Services	1,888,766	1,896,185	1,896,679	1,899,189	1,899,431
8	Personal Services-Pensions	774,600	820,234	853,635	872,946	894,681
9	Personal Services-Other Employee Benefits	663,993	685,591	715,485	747,728	781,487
10	**Sub-Total Employee Compensation (7 thru 9)**	**3,327,359**	**3,402,010**	**3,465,799**	**3,519,863**	**3,575,599**
11	Purchase of Services	1,094,526	1,033,373	1,050,840	1,057,051	1,060,973
12	Materials, Supplies and Equipment	118,809	112,830	110,821	102,979	102,242
13	Contributions, Indemnities, and Taxes	386,793	384,906	398,260	404,597	404,297
14	Debt Service	192,667	204,369	234,852	247,879	261,406
15	Advances & Misc. Pmts. / Labor Obligations	25,000	35,000	40,000	50,000	50,000
16	Adv. & Misc. Pmts. / Reopening and Recession Reser	75,000	75,000	25,000	25,000	25,000
17	Sub-Total (10 thru 16)	5,220,154	5,247,488	5,325,572	5,407,369	5,479,517
18	Payments to Other Funds	48,792	47,215	55,986	55,046	59,745
19	**Total - Obligations (17)+(18)**	**5,268,946**	**5,294,703**	**5,381,558**	**5,462,415**	**5,539,262**
20	Oper.Surplus (Deficit) for Fiscal Year (6)-(19)	(11,701)	34,432	(27,679)	(24,280)	(25,554)
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)**	**7,799**	**53,932**	**(8,179)**	**(4,780)**	**(6,054)**
	OPERATIONS IN RESPECT TO PRIOR FISCAL YEARS					
25	Fund Balance Available for Appropriation June 30 of Prior Fiscal Year	78,748	86,547	140,479	132,299	127,519
26	Fund Balance Available for Appropriation June 30 (24)+(25)	**86,547**	**140,479**	**132,299**	**127,519**	**121,465**

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

Budget Office
CITY OF PHILADELPHIA

Notes to the Forecasted General Fund Statements of Operations
Fiscal Years Ending June 30, 2022 through June 30, 2026

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 FY2022 budget and the FY2022-2026 Five Year Financial Plan (FYP) submitted by the Mayor to the Pennsylvania Intergovernmental Cooperation Authority (PICA) on June 29, 2021. 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, 2021, 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 FY22 total $5.257 billion. Approximately 65% of the City's revenue comes from local taxes, and 15.8% comes from other governments (including the PICA tax). In FY22, $645.9 million (12.3% of revenues) will come from other funds of the City, primarily $575 million of American Rescue Plan federal funds being drawn down. The City is expected to receive $1.395 billion by the close of FY22 and has already received 50% of the grant funds. Locally generated non-tax revenues, which include fees, fines and permits, account for 6.9% of revenues.

Budget provides forecasts for the seven major taxes, totaling over $3.4 billion in the adopted FY22 budget, as well as $364.4 million of Locally Generated Non-Tax revenues, and $829.1 million in Revenue from Other Governments. These three sources comprise 87.7% of the revenues anticipated for the FY22 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, Philadelphia Beverage Tax, and Sales Tax. These forecasts were refined by Budget after discussions with economists at a meeting hosted by the Federal Reserve Bank of Philadelphia, as well as with experienced staff within the Department of Revenue. Forecasts for the remaining major tax – Real Estate– was 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 are based upon collections of this new tax and IHS-projected growth rates. Once the pandemic-related impacts even out at the end of the Plan, the City assumes ongoing annual losses of -0.75% to reflect broad trends in sweetened beverage consumption.

The revenue projections for FY22-26 reflect the ongoing impacts of the COVID-19 global health crisis with both temporary and permanent changes to Philadelphia's tax base. The estimates have been revised since the April 15, 2021 introduction of the Five Year Plan based on updated collections information and changes to the tax rates initially proposed.

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 as a result of very solid gains in number of employees. That outlook changed as a result of the pandemic. In May 2021, there were only minimal gains in Philadelphia payroll, with 50,000 of the 175,000 lost jobs regained since the low point for employment in April 2020. IHS predicts that Philadelphia's 2022 Gross Metropolitan Product will climb up to 4.8%, while the Gross Domestic and Pennsylvania Gross State Product will slow down to 4.8%.

Fiscal 2021 sales tax collections through May are down 2% from last year, as a robust May result reflects the beginning of the rebound as pandemic-restrictions on activity were eased. The continued easing of restrictions since then, along with warmer weather, and Federal stimulus money are expected to boost collections moving forward.

Realty transfer tax collections in May were slightly higher than the April level and, as with April, nearly double the year-ago level. The residential real estate market remains as active as limited for-sale inventories allow, while commercial real estate shows signs of revival with the end of the pandemic in sight, combined with robust activity in warehousing and life sciences.

The Business Income and Receipts Tax (BIRT) posted the highest May level of collections seen in several years as activity continues to recover. Comparisons with the year-ago level remain difficult, as year-ago collections were affected by the onset of the pandemic and a change in the timing of Federal business tax-filing deadlines.

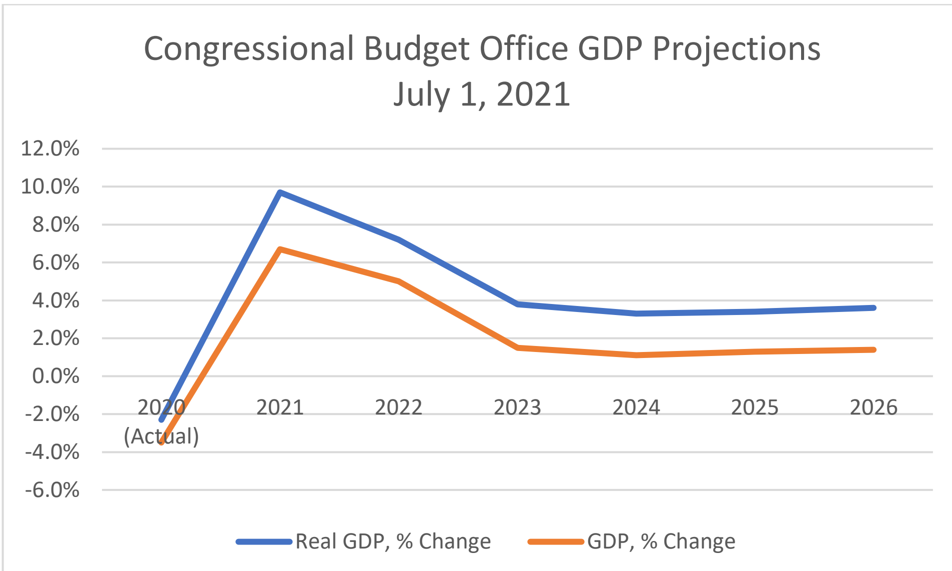
Despite improvements over the course of FY21, the COVID-19 outbreak has and will continue to significantly impact the local economy. Historically, the three largest drivers of Philadelphia's economy are educational institutions, medical institutions, and hospitality. In 2021, Philadelphia was not able to recover jobs to return to the pre-pandemic peak. Losses have been concentrated in leisure/hospitality, education, and professional and business services. Initially, losses in leisure/hospitality were driven by public health restrictions. These are now gradually returning but are constrained by difficulty hiring. Job gains in education and professional and business services have been slow but are anticipated to pick up in the fall when schools reopen and after the traditional vacation season. Although the leisure/hospitality sector has been the most vulnerable, it employs a much smaller proportion of the total workforce at relatively low wages, limiting the impact on Wage Tax collections, but its contraction disproportionately impacts low wage workers.

As the Wage Tax is the City's main revenue source, there will be significant shortfalls compared to pre-pandemic expectations for 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. The Plan incorporates the assumption of a permanent loss of 15% of the non-resident Wage Tax base within the overall Wage Tax projections. Projections show growth for all major tax types in FY22, with the exception of Realty Transfer Tax, which had a surprisingly strong FY21 given the general economic conditions and is historically volatile as a handful of commercial transactions can create tremendous swings in collections from year to year.

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 65% of the City's General Fund revenue in FY22 (a smaller share than in recent years, and than in later years of the Plan, due to the significant infusion of federal relief funds). On July 1, 2021, the Congressional Budget Office (CBO) forecast for U.S. Real Gross Domestic Product anticipates positive growth in 2021 of 6.7% and 5.0% in 2022, following a decline of -3.5% in 2020, based on the pandemic easing and demand for consumer services increasing. The projections for growth moderate to between 1.1% and 1.5% through 2026. Annual unemployment is expected to decline to 5.5% in 2021 and continue declining in 2022 and 2023 to a low of 3.7%, before increasing through 2026. The CBO notes that the labor force is expected to grow more slowly than in the past.

Notes to the Forecasted General Fund Statements of Operations
Fiscal Years Ending June 30, 2022 through June 30, 2026



[1]

On June 29, 2021, IHS provided updated projections for the national, state, and city domestic product, indicating comparable outlooks in 2022 for the City of Philadelphia, Pennsylvania, and the country.

Economic Indicators: National, State, and City

	2020Q4	2021Q1	2021Q2	2021Q3	2021Q4	2020	2021	2022
United States								
Employment (millions)	142.6	143.4	145.0	147.8	149.3	142.3	146.4	151.8
Real Per Capita Income (Thousand $)	46.9	52.8	48.8	47.7	47.2	47.6	49.1	48.1
GDP Growth Rate (%)	4.3	6.4	11.6	8.3	7.9	-3.5	7.4	4.8
Pennsylvania								
Employment (millions)	5.62	5.66	5.71	5.82	5.89	5.60	5.77	5.99
Real Per Capita Income (Thousand $)	60.8	70.0	65.7	64.6	64.0	62.2	66.0	66.0
GSP Growth Rate (%)	3.7	6.7	10.5	7.5	8.2	-4.4	7.0	4.8
Philadelphia City								
Employment (thousands)	664.8	667.9	675.5	689.1	699.1	678.3	682.9	716.0
Real Per Capita Income (Thousand $)	51.3	60.3	55.0	53.5	52.6	53.6	55.3	53.9
GMP Growth Rate (%)	1.7	4.3	8.2	7.0	8.6	-3.7	4.1	4.8

[2]

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 65% of the expected General Fund revenue in FY22. These include:

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

[1] https://www.cbo.gov/publication/57218
[2] IHS Markit projections from June 29, 2021.

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 (37.6% of the General Fund, including the PICA portion), the BIRT (9.9%) and the Sales Tax (4.1%) 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 44.3% 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 FY22, the Wage Tax rate for residents will decline to 3.8398% and will revert to the pre-pandemic level of 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 years 2024 through 2026 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 beyond. 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 $1.516 billion in FY22. This projection includes a 4.85% base growth rate for the Wage and Earnings component and 30.26% growth rate for the Net Profit component of the tax.[3] The overall growth rate, when incorporating rate changes, for the current and prior portions of the Wage and Earnings Tax, is 6.4%.

The non-resident portion of the Wage Tax remains due from employees working from outside Philadelphia if the employer is not requiring that the work location be outside the city. While this treatment will lessen the negative impact on collections of continued work from home initially necessitated by stay-at-home orders and business closures, revenue projections incorporation a permanent 15% contraction of the non-resident tax base.

b) Real Property Tax

The Real Property Tax (Property) is the City General Fund's second largest source of tax revenue (21.2%), estimated to contribute $723.1 million of the FY22 tax revenues. This tax is levied on the assessed value of residential and commercial property in the City. The Adopted FY22 Budget has a combined City/School District property tax rate for FY22 of 1.3998%, unchanged from FY21. 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%

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

discount for those who pay their bill by the last day of February, which went into effect in FY21. The FYP assumes taxable assessed values grow each year of the plan starting in FY23, based upon regular reassessments provided by the City's Office of Property Assessment. No growth is projected for FY22, as there will not be a citywide reassessment during the transition to a new computer system. The projection maintains the FY21 collection rate of 97.5%. The FY21 projected collection rate had been lowered from FY20 with the expectation that the COVID-19 pandemic and related economic impact would have a negative impact. Actual results in FY21 revealed continued strength in this area.

c) Business Income and Receipts Tax

The Business Income and Receipts Tax (BIRT) is projected to produce $521.2 million in FY22, 15.2% 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 for new businesses in the second year of operations, easing the impact on new businesses. 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 FY23.

d) Real Estate Transfer Tax

The Real Estate Transfer Tax (RTT) is projected to provide $294.9 million in FY22. After several strong years and largely due to the COVID-19 pandemic, the base growth of the RTT is projected to contract by -6.41% in FY21 and a further -1.49% in FY22, followed by increasing growth through the end of the Five Year Plan. 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 $216.4 million for the City's General Fund in FY22, based on a growth rate of 3.19%, 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 was 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 $48.2 million). From FY22 through FY26, the City's pension fund is projected to receive $298.6 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 was increased from 22.5% to 25.0%. For FY22 and through the remainder of the FYP, the Parking Tax rate will revert to 22.5%. Parking Tax revenue is projected to generate $56.4 million in FY22, exhibiting 9.6% growth, following a -33.4% decline in FY21 due to 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 at the time of implementation. 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 $376.6 million will be collected in gross revenue from FY22-FY26, before additional costs for collection, advertising and auditing.
- Revenues from the Philadelphia Beverage Tax are funding expenditures for three major initiatives: expanded Pre-K, community schools, and debt service for the Rebuilding Community Infrastructure program.

Budget Office
CITY OF PHILADELPHIA

Notes to the Forecasted General Fund Statements of Operations
Fiscal Years Ending June 30, 2022 through June 30, 2026

City of Philadelphia
General Fund
FY 2022 - 2026 Five Year Financial Plan
Major Taxes ($ in Millions) with Percentage Change from Previous Year

Tax	Actual FY20	Projected FY21	Projected FY22	Projected FY23	Projected FY24	Projected FY25	Projected FY26
Wage & Net Profits - Current & Prior	1,628.4	1,425.8	1,516.8	1,661.1	1,731.4	1,810.2	1,888.8
% change from prior year	n.a.	-12.4%	6.4%	9.5%	4.2%	4.6%	4.3%
Real Property - Current & Prior	699.1	712.3	723.1	756.7	794.6	833.4	861.8
% change from prior year	n.a.	1.9%	1.5%	4.6%	5.0%	4.9%	3.4%
Business Income & Receipts - Current & Prior	534.2	516.7	521.2	535.2	561.0	573.7	580.4
% change from prior year	n.a.	-3.3%	0.9%	2.7%	4.8%	2.3%	1.2%
Sales	204.6	209.7	216.4	225.8	238.2	251.7	265.2
% change from prior year	n.a.	2.5%	3.2%	4.3%	5.5%	5.7%	5.4%
Real Property Transfer	319.8	299.3	294.9	295.8	304.9	315.3	326.1
% change from prior year	n.a.	-6.4%	-1.5%	0.3%	3.1%	3.4%	3.4%
Parking	77.3	51.5	56.4	73.7	76.8	79.9	83.1
% change from prior year	n.a.	-33.4%	9.5%	30.7%	4.2%	4.0%	4.0%
Philadelphia Beverage	69.9	63.0	72.5	76.9	76.3	75.7	75.2
% change from prior year	n.a.	-9.9%	15.1%	6.1%	-0.8%	-0.8%	-0.7%
Other Taxes	22.6	5.7	16.5	30.7	39.1	40.0	40.6
% change from prior year	n.a.	-74.8%	189.5%	86.1%	27.4%	2.3%	1.5%
Total Taxes	**3,555.9**	**3,284.0**	**3,417.8**	**3,655.9**	**3,822.3**	**3,979.9**	**4,121.2**
% Change from prior year	**-1.6%**	**-7.6%**	**4.1%**	**7.0%**	**4.6%**	**4.1%**	**3.6%**

Note: Wage & Net Profits Taxes include a one-year non-resident rate increase in FY21 and the resumption of rate decreases in FY22. Wage tax does not include the PICA portion. Business Income & Receipts Tax rate reductions were paused in FY21 and FY22 but are to be restarted in FY23. Parking Tax includes a one-year rate increase from 22.5% to 25% effective July 1, 2020; the rate is planned to return to 22.5% in FY22. Construction Impact Tax will begin in FY23, where a $1 levy will be collected for each $100 improvement of residential space.

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. Additionally, in FY22 the City will begin budgeting for investment manager costs rather than showing discounted interest earnings to improve transparency. This results in a boost in interest earnings expectations.

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 57.8% of Revenue from Other Governments, is forecasted using Wage Tax variables.

6. Revenues from Other Funds

Revenues from Other Funds has typically represented transfers for services provided by the General Fund that are reimbursed by another fund, such as fire protection at the airport and are forecasted based on historical trends and operational expectations for the coming year. In FY22 and through FY25, there is significant growth in Revenues from Other Funds as American Rescue Plan deposited into the Grants Fund are drawn down to replace lost revenues to enable ongoing General Fund operations. The City received the first half of the $1.395 billion grant in FY21 and expects the balance to be received at the end of FY22. An initial draw down of $25.8 million was made in FY21 and $575 million will be utilized by the General Fund in FY22. The entire amount granted, plus interest earnings on those funds, are scheduled to be drawn down by FY25 in accordance with the federal deadline of December 2024 to expend all funds. In FY26, the Revenue from Other Funds is projected at a traditional level.

7. Obligation Estimates

The Budget Office provided obligation estimates to the Director of Finance and the Mayor for discussion and inclusion in the revised annual FY2022 budget and FY2022-2026 FYP submitted by the Mayor to PICA on June 29, 2021. The Budget Office provides forecasts of all major expenditure categories. Obligations total $5.269 billion, an increase of $349.6 million over the FY21 estimate. The largest driver of the increase is pension costs, with growth of $109 million beyond the FY21 level. This growth stems from restructuring pension obligation bonds in FY21 to save $75 million that year with the tradeoff that future year costs would increase. Additionally, an update on the cost allocation for pensions among the City's funds resulted in an increased contribution from the General Fund, while lowers contributions from the Aviation and Water Funds. The increase also incorporates a $75 million Recession and Reopening Reserve and $25 million Labor Reserve to absorb costs associated with new collective bargaining requires following the expiration of all four labor contracts by early FY22. The balance of the increases, about $140 million, represent increases in programs to address core needs of Philadelphians and restore services cut for financial reasons in FY21. This includes $68 million in new anti-violence funding and additional educational support for PHLpreK, Community Schools, the School District of Philadelphia, and the Community College of Philadelphia.

a) Labor Agreements

The forecasted statements include a set aside of $200 million from FY22 to FY26 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 their health plans, 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.

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 required 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% in 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 also been applied to employees who are not represented by a union, which means that all City employees, except for elected officials, are 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 FY22 through FY26, the City's pension fund is projected to receive $298.6 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 twelve years, reduced the pension fund's earnings assumption from 8.75% to 7.50%. 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. In four years, the pension system's funding percent has increased from 44 to 52. 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 restructured a portion of the Pension Obligation Bond (POB) payment due in FY21 and FY22 to postpone payment of $74.9M originally due from the General Fund FY21 and $19 million due in FY22 to future years, resulting in higher ongoing pension costs due to additional interest payments.