



AGENDA REPORT

TO: Steven Falk
Interim City Administrator

FROM: Eric Roseman
Director of Finance

SUBJECT: Fiscal Year 2024-28
Five-Year Financial Forecast

DATE: March 16, 2023

City Administrator Approval 

Date: Mar 29, 2023

RECOMMENDATION

Staff Recommends That City Council Receive An Informational Report On The City Of Oakland Five-Year Financial Forecast Prepared In Accordance With The City Of Oakland's Consolidated Fiscal Policy, Ordinance No. 13279 C.M.S.

EXECUTIVE SUMMARY

The Five-Year Financial Forecast (Forecast) for the City of Oakland (City), which is included as **Attachment A**, spans from Fiscal Years (FY) 2023-24 to FY 2027-28. The purpose of the Forecast is to help make informed budgetary and operational decisions by anticipating future revenues and expenditures as well as highlighting anticipated fiscal risks and opportunities. The Forecast is not a budget and does not include any proposed balancing solutions or revised service levels.

BACKGROUND/LEGISLATIVE HISTORY

On December 9, 2014, the City Council approved the Consolidated Fiscal Policy ([Ordinance No. 13279 C.M.S.](#)), which directs staff to produce a Five-Year Financial Forecast as part of the biennial budget development process. The City Council amended the Consolidated Fiscal Policy ([Ordinance No. 13487 C.M.S.](#)) on May 15, 2018. The amended Consolidated Fiscal Policy was designed to facilitate various goals and objectives, including enhanced public participation, adoption of best practices and to provide budgetary flexibility.

ANALYSIS AND POLICY ALTERNATIVES

Per the Consolidated Fiscal Policy, the Five-Year Financial Forecast shall contain the two-year baseline budget for the forthcoming budget period, clearly reflecting projected expenditures to maintain existing service levels and obligations, plus an additional three-year forecast of revenues and expenditures. The Baseline Budget shall consist of projected expenditures necessary to

maintain existing staffing and service levels, plus an estimate of anticipated revenues for the two-year period.

The Forecast shall also contain information on the variance between prior forecasts and actual amounts, including the factors that influenced these variances. Revenue estimates shall be based on the most current data available; minimally revenue projections shall take into account projected revenue for the current fiscal year, as reflected in the 2nd quarter Revenue and Expenditure Report, with appropriate trending into future years and an explanation as to how such revenue projections were derived.

The current forecast shows that while the worst of the COVID-19 pandemic's health effects appear to have passed, the economic and fiscal effects of the pandemic have lingered. Many workers have yet to return to work in downtown office buildings; those that have returned frequently only come to the office a few days each week. This has resulted in lower Business License Tax collections from downtown offices as well as reduced retail activity in businesses that serve office workers and property owners. Accompanying this trend has been a reduction in business travel, and with it a reduction in the City's hotel tax (known as Transient Occupancy Tax or TOT) revenue.

More recently, high inflation prompted the Federal Reserve Bank to raise interest rates. These higher interest rates, in turn, have acted to slow new construction activity and reduce housing prices, which has acted to slow the growth in property tax revenues. The uncertainty in the economy generally and in the real estate sector in particular has also led to a slowing of real estate transactions, which has resulted in a steep decline in the City's real estate transfer tax revenue in the current (2022-23) fiscal year.

In spite of these economic headwinds, however, the City's revenue base has proven resilient. With the exception of TOT and Parking Tax, all of the City's major tax general purpose revenue sources have now exceeded pre-pandemic levels, in some cases by large amounts. (Real estate transfer tax exceeded the pre-pandemic level in Fiscal Year 2021-22, but is expected to come in well below the previous high levels in the current fiscal year.) In addition, the City benefitted from a significant amount of one-time federal COVID relief funds. And, in November 2022, City voters approved an increase in the City's Business License Tax (BLT); this increase is expected to raise an additional approximately \$20 million in FY 2022-23 compared to the amount that would have been raised absent the voter approved increase.

While the City's revenue base has generally proven resilient, most expenditure categories, such as personnel costs for wages and retirement, have grown even faster, particularly in the most recent (FY 22-23) year. As a result, the City faces an anticipated General Purpose Fund (GPF) shortfall in the 2023-24 fiscal year of \$195.5 million. This gap is expected to persist through the forecast period, although the gap is anticipated to shrink somewhat as revenue growth exceeds the anticipated increases in expenditures.

Although General Purpose Fund (GPF) shortfalls are expected to decrease during the forecast period, the cumulative gap in the City's GPF over this period (assuming no corrective actions) is expected to exceed \$750 million. The City's Charter and Consolidated Fiscal Policy require adoption of a balanced budget each fiscal year, and the City will therefore need to develop strategies to address the shortfalls projected in the Forecast. This forecast assumes that the

City's economy avoids a recession in the coming fiscal year under a so called "soft landing" in which an outright recession is avoided as the Federal Reserve continues to fight inflation through higher interest rates. If a soft landing does not happen according to the forecast – and there remain many unknowns regarding the pace and contours of economic growth– projected shortfalls could be larger. Even modest changes in the assumed revenue growth rates or the onset of a new recession could significantly alter these results.

The Forecast for all Funds shows a trend similar to the GPF: shortfalls persist throughout the forecast period, although the expected increases in revenues outpace expected expenditure increases, resulting in a declining deficit during the forecast period.

The City maintains a 7.5% General Purpose Fund Emergency Reserve and in 2014 approved a Rainy Day policy. These responsible fiscal policies also enabled the City to set aside funds for long-term obligations and establish a Vital Services Stabilization Fund, which had approximately \$14.9 million as of June 30, 2020. However, as pandemic-induced revenue shortfalls mounted, the City utilized these funds to help balance the FY 2020-21 budget. The beginning balance in FY 2022-23 for the VSSF is \$2.58 million, after accounting for the FY 2022-23 GPF budgeted transfer of \$7.69 million, the FY2022-23 projected year-end balance is \$10.27 million.

Although signs point to the likelihood of a "soft landing" in which a recession is avoided and interest rates and inflation decline and growth accelerates over the forecast period, substantial uncertainty remains. Given these uncertainties, the City should focus on long-term sustainability through 1) expansion of the City's economic base; 2) management of expenditure growth through efficient service delivery; and 3) practical reductions to long-term unfunded liabilities. The City must focus on prioritizing funding to meet its current mandates (including long-term obligations, such as legally binding promises made to current and retired City employees) and needs, rather than adding services or programs that would expand the projected gap.

FISCAL IMPACT

This item is for informational purposes only and does not have a direct fiscal impact or cost.

PUBLIC OUTREACH/INTEREST

This item did not require any additional public outreach other than the required posting on the City's website.

COORDINATION

This report was prepared by the Finance Department.

SUSTAINABLE OPPORTUNITIES

Economic: No direct economic opportunities have been identified.

Environmental: No direct environmental opportunities have been identified.

Race & Equity: No direct social equity opportunities have been identified.

ACTION REQUESTED OF THE CITY COUNCIL

Staff recommends that the City Council receive an informational report on the City of Oakland's Five-Year Financial Forecast prepared in accordance with the City of Oakland's Consolidated Fiscal Policy, Ordinance No. 13279 C.M.S.

For questions regarding this report, please contact Bradley Johnson, Finance Department Budget Administrator, at (510) 207-5730.

Respectfully submitted,



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Finance Department

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Attachments (1):

A: Five-Year Financial Forecast Fiscal Year 2023-24 – Fiscal Year 2027-28

Appendixes (2):

A: Consolidated Fiscal Policy

B: Background on California Legal Revenue Limitations