

---

## OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

---

**Date Issued:** February 14, 2008

**IBA Report Number:** 08-14

**Budget Committee Date:** February 20, 2008

**Item Number:** 1

---

# City of San Diego Structural Budget Deficit

## OVERVIEW

The City of San Diego is facing a structural budget deficit. Over the past six fiscal year the City has endured significant budget reductions, employ the use of one-time solution, and sharply scaled back new programs or program enhancements in order to balance annual budgets. Unless clear, decisive, and long-term solutions are implemented, municipal services will continue to erode in the future.

The structural imbalance confronting the City is by nature persistent. The City cannot continue to use temporary or one-time solutions to effectively combat it's financial challenges. Structural deficits require structural solutions.

This report begins providing evidence that the City is struggling with a structural budget deficit. The next section looks at some of the consequences of operating within such a structural imbalance. Finally, a general overview of the steps that must be taken to solve the City's structural budget deficit is provided, including a model that was recently employed in the City of San Jose.

## DISCUSSION

In order to illustrate the City of San Diego's structural budget deficit and discuss the long-term ramifications, we must first have a general understanding of what is meant by *structural*. What is a structural budget deficit, and how is it different from a "regular" budget deficit that may occur from time to time on an annual basis? Any number of things may lead to a budget deficit in a given year. These *annual* budget deficits (as to distinguish from *structural* deficits) may be caused by factors such as:

- Declining revenues due to a slowing economy;
- Unexpected loss in revenue due to state actions;
- Increases in debt obligations;
- Costs due to one-time occurrences such as natural disasters;
- Increased costs related to mandated programs;
- Increases in committed expenditures, such as negotiated salary increases;
- Increases in non-discretionary expenses, such as energy or fuel;
- Other unanticipated expenses such as legal costs or settlements.

Typically, a regular annual budget deficit is the result of a combination of these effects, such as a confluence of declining revenues and an increase in committed expenditures. However, a general similarity among the causes of annual budget deficits is that they are often unexpected and are virtually always the result of one-time or short-term occurrences.

A structural budget deficit, in contrast, is marked by persistence. In general, a structural deficit is defined by a situation where ongoing expenditures consistently exceed ongoing revenues. Often, this situation may arise due to a combination of significant long-term needs that are consistently unfunded in the annual budget, over-reliance on a declining revenue base, and a continuing desire to meet the needs of a growing population. While the temporary causes of annual deficits are often overcome with temporary solutions, structural deficits cannot be mitigated with such an approach. Even if the use of one-time solutions are able to bring a structural deficit temporarily into balance, the divergent nature of ongoing expenditures and ongoing revenues will continue to result in future budgetary shortfalls.

But how do we know that the City has a structural deficit? Couldn't it be that we've just seen a remarkable string of annual budget deficits that will eventually come into balance? Maybe. But there are several indications that the imbalance facing the City is structural in nature. We examine these indications in the next section.

### ***Evidence of a Structural Budget Deficit***

There are a couple of challenges in demonstrating that a structural imbalance exists. First is the size and complexity of the City's budget. As mentioned above, a structural deficit is defined by a situation where ongoing expenditures exceed ongoing revenues. However, it would be virtually impossible to identify all the temporary and one-time revenues and expenditures in the City's budget and eliminate them from our analysis in order to identify whether a structural imbalance exists. The size, complexity and dynamic nature of the City's budget make such an arduous task prohibitively difficult.

This challenge is further complicated by the fact we cannot actually see any deficits directly. By law the City is required to enact a budget – and conclude the fiscal year – with revenues equal to or greater than total expenditures. This means that on an annual

basis the budget will always be balanced. So how can we tell whether the City has a structural budget deficit, or even any deficit at all? In order to do this, we must examine the indirect signs and symptoms of such phenomena. These are discussed below.

Persistent Budget Deficits

Even though the annual budget must be balanced, that does not mean that no deficit exists. Throughout the budget development process, General Fund revenues and expenditures are closely monitored. If it becomes apparent that expenditures will exceed revenues, solutions must be implemented to achieve a balanced budget. Often, these solutions will involve departmental budget reductions.

One of the clearest indications of the City’s budget deficit are the budget reductions that have been implemented. Beginning in FY 2003, and in each fiscal year since, the City has been forced to make budget reductions in order to balance the budget. The fact that these reductions have been persistent, and some cases increasing, is a strong indication that the City’s deficit is structural in nature. The table below shows the total General Fund budget reductions that were needed to balance the annual budget since FY 2003.

**Table 1. General Fund Budget Reductions**

<b>Fiscal Year</b>	<b>FTE Reductions</b>	<b>Budget Reductions</b>
2003	(34.20)	(\$10.3 million)
2004	(143.66)	(\$28.4 million)
2005	(124.57)	(\$23.3 million)
2006	(209.55)	(\$23.0 million)
2007 <sup>1</sup>	-	(\$35.9 million)
2008 <sup>2</sup>	(259.69)	(\$16.0 million)
<b>TOTAL</b>	<b>(771.67)</b>	<b>(\$126.9 million)</b>

1. 269.26 supplemental FTE added to GF in FY07; savings reflects General Fund vacancy savings

2. Includes FTE reductions due to BPR

This table shows that significant position and expenditure reductions have been necessary over the past six years. It should be noted that during these years, other measures such as one-time revenues were also employed to help balance the budget. Considerable changes were made to budget practices in FY 2007, including the proper budgeting of supplemental positions, and the application for the first time of a vacancy savings factor. In FY 2008, a significant number of positions were eliminated due to continued vacancies, as well as the Mayor’s Business Process Reengineering efforts.

What is more striking is that these deficits have occurred during a time of healthy economic conditions and strong revenue growth. While major revenues in FY 2003 were still feeling the effect of the national recession and the World Trade Center attacks, revenue growth since then has been robust. Since FY 2004, growth in the major revenues has averaged approximately 7.6 percent per year, including average growth rates of around 10 percent for both property tax and TOT. While state actions resulted in revenue reductions of approximately \$60 million from FY 2003 through FY 2006, the City still saw significant net revenue increases from the major revenues. Even without these State revenue diversions, the City still would have needed to enact budget reductions during this timeframe. The fact that budget deficits were persistent during good economic times is another clear indication of a structural imbalance.

#### Use of One-Time Solutions to Balance the Budget

Another indication that the City is facing a structural budget deficit is in the widespread use of one-time measures to balance the budget, usually in the form of one-time revenues. These may come in the form of balance transfers from other funds, one-time payments from other agencies, land sales, or other one-time sources of revenue.

A standard budget principle is that one-time revenues should not be used to fund ongoing expenditures. And while the City has tried in earnest to pair one-time revenues with one-time expenditures, the deficits over the last several years have simply been too great. Many one-time revenues have been employed as budgetary solutions in lieu of additional service reductions. Furthermore, some of the one-time challenges facing the City such as the backlog of deferred maintenance are so immense that the magnitude of one-time solutions pale in comparison, and ongoing solutions to such challenges will likely be necessary. Listed below are some of the one-time solutions that have been used to balance the budget since FY 2003<sup>1</sup>.

#### **One-Time Budgetary Solutions**

- Use of General Fund Reserves
- Transfer from Environmental Growth Fund
- Transfer from Vehicle Replacement Fund
- Transfer from State Contingency Reserve Fund
- Sales Tax Accrual Adjustment
- Transfer from Fire & Lifeguard Facility Fund
- Transfer of Tobacco Settlement Revenues from Central Library
- Loan Repayment from Redevelopment
- Release of Inactive/Unnecessary Encumbrances
- Cal American Franchise Fee
- Transfer from IT New Development Fund

---

<sup>1</sup> Includes one-time solution used both to balance the adopted Annual Budget, and for mid-year adjustments.

- Rebate from Storm Drain Fund
- Rebate from Naval Training Center
- Rebate from VLF Securitization
- Rebate from Naval Training Center
- Rebate from QUALCOMM
- Use of PETCO Park Fund reserve balance
- Transfer from PC Replacement Fund
- Transfer from Y2K Fund

As described earlier in this section, annual budget deficits are usually caused by temporary or one-time occurrences, and can often be mitigated through temporary or one-time solutions. Were this the case with the City's deficit, we would expect these one-time solutions to have substantially solved the problem. Yet this has not happened. As described above, the City has been faced with a new deficit in each year, and in each year new one-time solutions have been implemented – in addition to sharp budget reductions – in the hopes of “getting us through” to better times. Even budget reductions can be viewed as one-time solutions, if the cuts are restored in the near future. Yet this has not occurred either. In continuing to use one-time solutions to balance the City's budget, it appears that the City has taken an annual deficit approach to solving a structural problem.

#### Budget Under-Funding

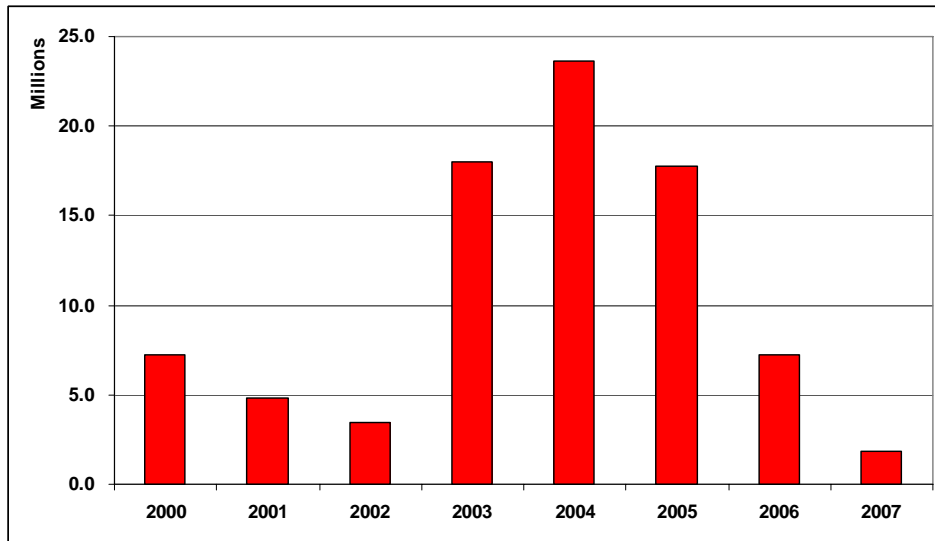
One of the underlying causes of a structural budget deficit is when programs and services are increased without increasing revenue. These new expenditure commitments are then dependent on the existing revenue base, and compete with other programs and services for funding. Often, the result is insufficient resources to adequately fund all expenditure commitments. As mentioned, this tends to result from a combination of over-reliance on a declining revenue base and a desire to meet the increasing needs of a growing population.

If the discrepancy between available resources and committed expenditures becomes large enough, it may require budget reductions or other one-time solutions, as described above. However, a more subtle way that this discrepancy is often addressed, particularly over longer periods of time, is by under-funding certain expenditure commitments in lieu of others. At times, departments are expected to absorb cost increases related to more pressing issues, and do so by shifting resources away from existing programs and services. If this occurs frequently for a long enough period of time, a structural imbalance will result.

The City of San Diego has also exhibited this trend. The public safety departments have long been underfunded in areas such as overtime and pays for both the Police and Fire-Rescue Department, leading to overages in personnel expense; and funding for public safety fleet replacement, resulting in significant maintenance and replacement needs for over-age police cruisers and fire engines. To illustrate this chronic underfunding, the

chart below shows the combined amount by which actual Police and Fire-Rescue expenditures have exceeded their annual budgets.

**Figure 1. Police & Fire Expenditures in Excess of Budget**



The declines evident in FY 2006 and FY 2007 reflect the efforts in the past several years to correct this underfunding. Additional funds were allocated to the Police and Fire-Rescue Departments in FY 2008, further correcting this structural under-funding. However, this only reflects the commitment to adequately fund existing services and required expenditures; it does not reflect continued funding needs for restoration of service cuts, or any service enhancements.

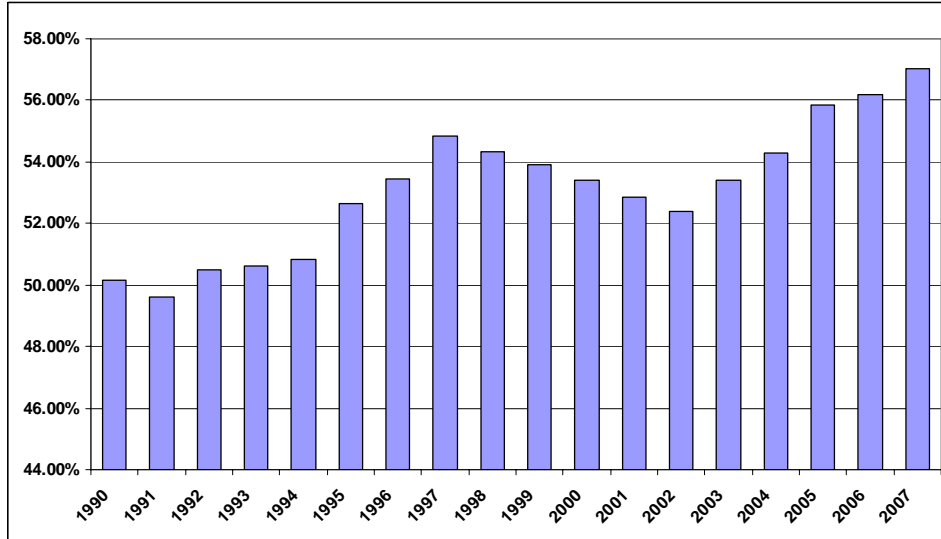
There are many other examples of budgeted items that have been or continue to be underfunded, including funding for disposal fees for residential refuse collection, which has degraded the financial health of the Refuse Disposal and Recycling Funds; routine maintenance for parks, streets and City facilities, which continues to increase the backlog of deferred maintenance; and funding for worker's compensation and public liability. A critical component to resolving the City's structural budget deficit is the adequate funding of core services and programs.

#### Other Statistical Indications

Looking at certain statistical trends in General Fund revenue and expenditures data can provide additional insights to the City's situation. These measures do not necessarily indicate that the City has a structural deficit *per se*, but rather indicate trends that may have helped cause the structural imbalance, that may have resulted from it, or that otherwise provide clues as to the precarious financial state that the City is in.

The chart below shows the percentage of General Fund expenditures that are attributable to public safety departments.<sup>2</sup>

**Figure 2. Public Safety Expenditures as a % of Total General Fund**



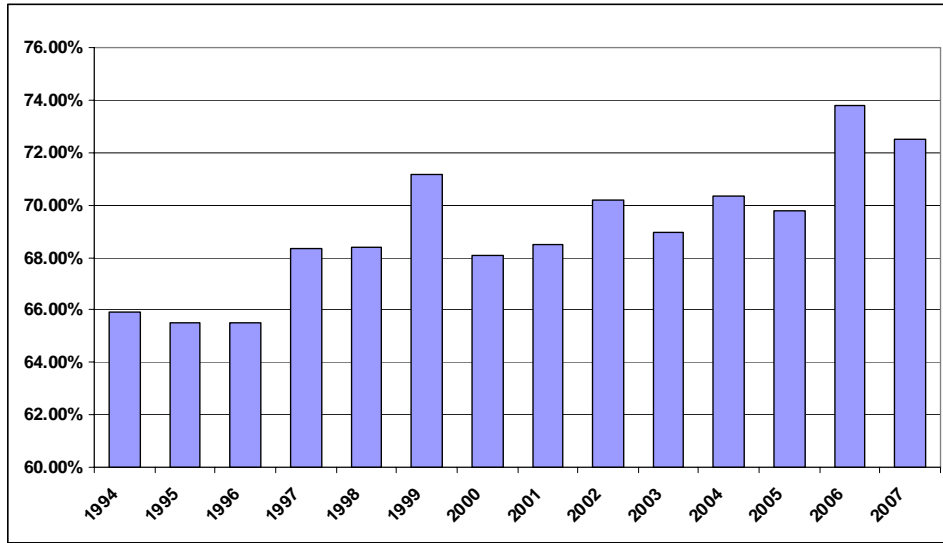
As this chart indicates, since FY 1990 public safety expenditures have increased as a percentage of total General Fund expenses. Public safety is often identified as a critical public service, and thus tends to be somewhat shielded from budgetary reductions. While both Police and Fire-Rescue have been subject to budget reductions in prior years, the chart still shows that public safety expenditures have increased as a percentage of the total General Fund, indicating that other General Fund departments and service areas have endured more significant cuts. Overall, this chart suggests that public safety expenditures are increasingly being supported at the expense of other City services.

Another measure that is informative is the percentage of total General Fund revenue that is comprised of the major revenue sources<sup>3</sup>. This is reflected in Figure 3.

<sup>2</sup> Public Safety includes Police, Fire-Rescue, paramedic expenditures, and Office of Homeland Security.

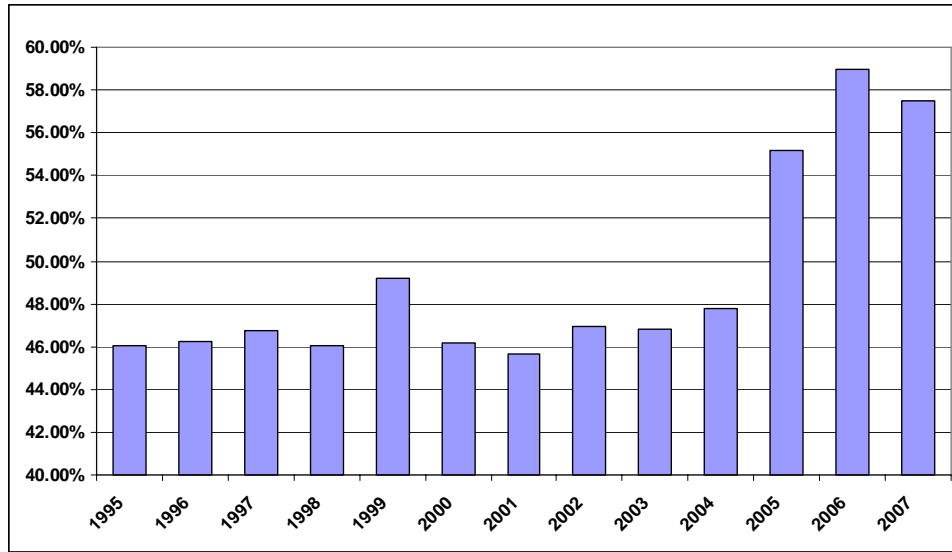
<sup>3</sup> For this analysis, major revenues include property tax, sales tax, transient occupancy tax, franchise fees and motor vehicle license fees. In addition, an adjustment has been made to reflect total city sales tax.

**Figure 3. Major Revenues as a % of Total General Fund**



This chart clearly shows that over the past 15 years the General Fund has become increasingly reliant on just a few major revenue sources. This is significant for two primary reasons. First, it reflects a general decline in diversification among the City's general revenues sources. Second, it means the City is increasingly reliant on revenue sources that are more cyclical and unstable. This can be problematic if funding commitments are dramatically increased during periods of strong growth. These factors are particularly evident by looking at the two largest revenue sources, property tax and sales tax, as a percentage of total General Fund revenues.

**Figure 4. Property and Sales Tax as a % of Total General Fund**



This chart shows that property tax and sales tax have experienced a dramatic increase as a percentage of total General Fund revenue. Significantly, this is *not* due primarily to the booming real estate market of a few years ago, but rather, to a revenue swap enacted by the State in FY 2005, whereby the City’s Vehicle License Fee revenue was reduced by nearly 90 percent and replaced by a commensurate amount of property tax<sup>4</sup>. This represents a structural consolidation of the City’s revenue base.

In summary, none of the elements examined in this section alone provide direct or irrefutable proof of a structural budget deficit. Each is merely an indication or a symptom of what we would expect to see in such a situation. Together, however, they do provide compelling evidence that the City is in a state of structural imbalance.

***Impact of Structural Budget Deficit***

The existence of a structural budget deficit poses dire problems for any municipality. As mentioned, structural deficits are persistent; consequences, therefore, will also be persistent unless corrective actions are taken. Since FY 2003, the City has endured significant service level reductions. As alluded to previously, if these service reductions were made in response to an annual deficit, they likely would have either fully or partially restored once the budget situation improved. But the budget situation has not improved over the course of several years. Not only have the initial service reductions not been restored, but additional reductions have been required in order to balance the budget. Unless corrective actions are taken, this trend is likely to continue in the future.

<sup>4</sup> More detail on this revenue swap and other state impacts can be found in the FY 2004 and FY 2005 Annual Budget Documents.

The table below shows the cumulative budget reductions that have been made by several departments from FY 2003 to FY 2006. These departments have been subject to the most significant reductions over that timeframe, accounting for over 70 percent of total FTE and budget reductions.

**Table 2. Significant Departmental Reductions, FY03-06**

<b>Department</b>	<b>FTE Reductions</b>	<b>Budget Reductions</b>
Police*	(72.75)	(\$16.4 million)
Park & Recreation	(164.01)	(\$11.9 million)
Community & Econ. Develop.	(21.65)	(\$10.4 million)
Library	(61.73)	(\$7.0 million)
Citywide Program Expenditures	(3.00)	(\$4.8 million)
Fire-Rescue	(4.00)	(\$4.5 million)
Planning	(25.00)	(\$3.8 million)
General Services**	(29.75)	(\$3.2 million)
<b>TOTAL</b>	<b>(381.89)</b>	<b>(\$62.0 million)</b>

\* Reflects removal of funding for 80.00 vacant civilian positions in FY04 & 05.

\*\* In lieu of making additional budget reductions, Facilities Division increased revenue by shifting workload to non-GF departments.

The budget reductions to these and other departments have resulted in significant service-level impacts. Listed below are some of the services reductions that have resulted from budgetary reductions imposed from FY 2003 to FY 2006. Additional detail and a more comprehensive list of service reductions can be found in the Annual Budget documents for those years.

**Service Reductions, FY03 – FY06**

**Park and Recreation**

- Reduction of operating hours at recreation centers
- Reduction of youth programs, including summer camps, homework programs and arts and crafts
- Reduction in maintenance for park facilities, equipment, restrooms and landscaping
- Reduction in range patrols, enforcement, educational and interpretive programs, train maintenance and habitat protection
- Reduced funding for replacement of worn or broken equipment
- Reduced funding for redevelopment of baseball fields
- Reduction in grant-matching funds

- Closure of certain community pools during winter months
- Closure of certain after-school sites

#### Library Department

- Reduction in extended weekday and Sunday service hours at most branch libraries
- Elimination of Sunday service at all but one branch library per district
- Reduction in Central Library branch hours
- Significant reduction in funding for replacement of aging and worn materials, or purchase of new materials
- Negative impact to customer service as a result of reduction in library support staff
- Elimination of funding for replacement of public-use equipment, such as computers and software
- Suspension of the Library Ordinance since FY 2005

#### Community and Economic Development

- Reduction funding for educational, employment assistance, and youth and family counseling services offered at Community Service Centers
- Significant reduction in funding for the “6 to 6” Extended School Day Program, reducing participation levels by eliminating student slots;
- Elimination of competitive portion of the City’s Social Services Program
- Closing of certain Community Service Centers
- Closing of certain police storefronts
- Reduction of staff support for grant research and application
- Reduction in revitalization services such as public infrastructure, street lighting and public art in older corridors and commercial districts

#### Police Department

- Reduction in civilian administrative support staff
- Reduction in non-personnel expense for safety supplies, service contracts, equipment purchases and training
- Continuation of civilian vacancies, resulting in limited support for officers and the need for officers to perform administrative tasks
- Reduction of Community Service Officers

#### Other Service Reductions

- Reduction in City Planning staff, reducing support for the General Plan, Community Planning Program, Multiple Species Conservation Program
- Reduction in staffing and support for Storm Water Permit compliance efforts, including public education and illegal discharge investigation
- Reduction in facility maintenance staff, and shifting maintenance effort to non-General Fund departments

- Reduction in Citywide Information Technology support and development

This list of service reductions, while not comprehensive, clearly illustrates how structural imbalances impact the community.

In FY 2007 and FY 2008 no service-level impacts were reported in the Annual Budget documents, despite the reductions in those years. As briefly mentioned, several significant new budgetary practices were implemented in FY 2007, including the proper budgeting of 269.26 supplemental General Fund positions, and the application of a vacancy factor to reflect anticipated savings in personnel expense. The vacancy factor resulted in budgetary savings of approximately \$35.9 million in FY 2007.

In FY 2008, 259.69 General Fund positions were eliminated from the budget. According to IBA calculations, 23.75 of these positions were reduced on account of the Mayor's Business Process Engineering initiative, while a vast majority of the remaining position reductions were vacant. It was purported that there would be no service reductions due to the reduction of vacant positions and operational efficiencies achieved through BPR. While it is unclear if there have been any significant additional service reductions in FY 2007 or FY 2008, baseline service levels were already sharply eroded as a result of budgetary reductions over the past several years.

Furthermore, even if there were no additional service impacts above and beyond those in previous years, the budgetary solutions in FY 2007 and FY 2008 result in a different kind of service impact. The service reductions implemented from FY 2003 to FY 2006 listed above reflect the *explicit* service impacts that have resulted from the City's structural deficit; however, there are also *implicit* service impacts in the form of service restorations, service enhancement or new services that are never implemented due to lack of funding.

In August 2004 the City Manager released an Unfunded Needs Report, providing a comprehensive overview of the funding requirements needed across the City to fulfill department missions, meet mandates or provide optimum service levels. These funding needs were divided into three categories: funding required for maintenance of (then) current service levels; funding needed for enhancement of service levels to meet increased demand or requirements; and funding for new services that are needed or required.

The Unfunded Needs Report indicated that non-public safety General Fund departments required an additional \$149 million; unfunded needs by the Police and Fire-Rescue Departments, developed separately but attached to the report, totaled an additional \$125 million, for a total General Fund need of \$274 million. It should be noted that this did not represent a one-time funding requirement, but rather, the additional funding that was needed *per year*.

**Table 3. 2004 Unfunded Needs Report**

<b>DEPARTMENT</b>	<b>UNFUNDED NEED</b>
Fire-Rescue	\$38.0 million
Police Department	\$87.1 million
Park & Recreation	\$81.1 million
Library Department	\$14.2 million
General Services	\$33.7 million
Other General Fund	\$20.1 million
<b>Total General Fund</b>	<b>\$274.2 million</b>

Unfortunately, the 2004 Unfunded Needs Report is the most up-to-date information of this kind. An update to this report would reveal that many of the unfunded needs listed in the report, such as funding for Storm Water Permit Compliance, Police and Fire-Rescue overtime and the Northwest Area Police Station, have already been or are currently being addressed. However, without significant new sources of revenue, it can be assumed that these needs are being addressed in lieu of many others. In addition, it is likely that new unfunded needs have arisen in the time since the 2004 report was developed.

In the absence of corrective actions, not only will the majority of these needs continue to be unfunded, but further service reductions will be imminent. The Mayor's revised Five-Year Financial Outlook, released in January 2007, projects significant deficits in each year of the Outlook period.

**Table 4. Five-Year Financial Outlook Projected Deficits, in millions**

	<b>FY 2009</b>	<b>FY 2010</b>	<b>FY 2011</b>	<b>FY 2012</b>	<b>FY 2013</b>
Total Revenues	\$ 1,163.6	\$ 1,212.8	\$ 1,238.3	\$ 1,285.7	\$ 1,323.1
Total Expenses	1,195.6	1,279.0	1,323.6	1,361.5	1,373.1
<b>Surplus/(Deficit)</b>	<b>\$ (32.0)</b>	<b>\$ (66.2)</b>	<b>\$ (85.3)</b>	<b>\$ (75.8)</b>	<b>\$ (50.0)</b>

The Outlook presumes that an additional \$32.0 million in budget reductions will be necessary in FY 2009 to balance the budget. No solutions have been identified to mitigate deficits in future years. However, as we noted in our review of the Five-Year Financial Outlook (IBA Report 08-9), these projected deficits are based on precarious assumptions such as no salary or wage increases and no additional public liability or workers' compensation claims, and do not take into account known future impacts such as implementation of the General Plan update or long-term waste management solutions. Given the significant budgetary impact of these factors, it is likely that actual deficits will be larger than those projected in the Outlook, and continue in future years.

The Five-Year Financial Outlook, and the Mayor’s commitment to funding the “Eight Significant Areas”, do begin to address some of the significant unfunded needs that have burdened the City for years, such as deferred maintenance, Storm Water Permit compliance, and pension under-funding. However, the Outlook provides funding for these areas largely through one-time solutions and unfocused budget reductions. As previously mentioned, the magnitude of some of these challenges is so great that more significant, ongoing solutions will likely be required to solve them. In addition, the Outlook does not provide for any restoration of prior service reductions or any service expansions.

### ***Correcting the Structural Budget Deficit***

The previous sections have provided strong evidence that the City is in the midst of a structural budget deficit, and have illustrated the consequences that can occur from operating with such an imbalance. Underscoring this discussion is the reality that these deficits – and associated service impacts – will continue into the future absent corrective actions. Now is the time to begin implementing structural reform in order to correct the persistent budgetary imbalance that has developed in the City of San Diego. But what can be done? What steps need to be taken?

The solution begins with a vision. Before appropriate remedies to the City’s structural deficit can be developed, we must first have a clear vision of what we want this city to be. This is a vision that must originate with the community at large. Public input and community participation is critical in order to draw upon different viewpoints and ideas, and to ensure that all stakeholders are represented and supportive of the eventual course of action. Budget workshops, community forums, strategic visioning sessions, and public outreach and education can be used to engage the community and elicit desired public input and participation.

Another critical component in solving the structural imbalance is being honest with the community about what they can expect given the available resources. The City can no longer afford to make promises to the public that it cannot meet. Not only must we work with the community to forge a vision of what we want this City to be, but we must be realistic and straightforward about what it will cost to achieve that vision. A clear understanding of the tradeoffs involved is essential. If free residential trash collection is determined by the community to be a desired General Fund service, there must be an understanding that it will be paid for through reduced services in other areas.

This report does not offer any specific recommendations on how the City might solve its financial problems. To do so would be to presume we know the desires of the community, and vision for the City that has yet to be developed. However, we do offer several points of guidance. First, solutions must be broad and structural in nature. The structural imbalance will not be solved through a patchwork of minor or temporary fixes. Quite simply, this will ultimately require a significant increase in revenue or decrease in

expenditures, or some combination thereof. The precise mix of these elements will depend on the vision for the City that is developed by the community.

Second, expenditure reductions should be targeted and focused, not haphazard or arbitrary. Across-the-board reductions may be suitable for balancing an annual deficit, but it lacks the visioning and strategic planning that is incumbent in resolving a structural imbalance. Finally, services that are ultimately deemed to be critical and desired by the community should be adequately funded. If the public desires park facilities, then the City must commit funding for adequate staffing, supplies and maintenance. Underfunding desired services not only leads back to a structural imbalance, but also runs afoul of the commitment the City has made to provide such services to the public.

#### City of San Jose Model

The City of San Jose serves as a timely example of a city recognizing that they were facing was a structural deficit rather than a regular annual deficit, and taking action and setting goals to address it. In January 2008, San Jose completed an in-depth process which included a full review of their budgetary and economic conditions, both past and future, and development of strategies to address the structural deficit. Not dissimilar to San Diego, their review identified the following as significant ongoing cost contributors to their structural deficit:

- Under funding of existing programs
- Annual unmet/deferred infrastructure and maintenance needs
- A one-time significant backlog of deferred maintenance needs
- Unfunded liability associated with post- employment health benefits

On the revenue side, they identified the economic downturn when the dot-com bubble burst in late 2001 as a significant contributor as well.

The City's stated goal through this process is to eliminate their structural deficit within three years. For a strategy to be considered in the process it had to be able to be effectively implemented within this three year window. Over a three month period, the City Manager's General Fund Structural Deficit Task Force worked with a consulting firm to solicit input and feedback on potential strategies to address the structural deficit, through focus groups with a wide variety of stakeholders including community and business groups, City boards and commissions, City employees, labor unions and City management. They also conducted employee and community surveys and performed benchmarking against "best practice" cities including Phoenix, Austin, Long Beach, Minneapolis, Virginia Beach, Fairfax County- all of whom have been recognized for their long term sound financial practices.

Two hundred strategies emerged from this effort with just over 100 meeting the criteria to qualify for further analysis. After extensive research and feedback from stakeholders, 21

priority strategies representing four major categories – Revenue Strategies, Service Delivery Model Changes, Expenditure Controls and Shifts and Service Reductions – were brought forward in the Task Force’s final report to the Mayor and City Council. The Task Force Report also developed 12 budget principles for Council consideration to help prevent a future structural deficit addressing matters such as use of one-time resources; budget requests during the year; fees and charges; performance measures; grants; proposed budget revisions and capital improvement projects operating and maintenance costs.

The Task Force’s report was developed to serve as a key resource to the Mayor’s Budget Shortfall Advisory Group that was charged with bringing forward its recommendations on eliminating the structural deficit within a three-year period to the City Council by February 12, 2008. The Advisory Group’s final recommendations along with City Council feedback is intended to provide the framework to eliminate the structural deficit within three years.

## CONCLUSION

Despite significant budgetary and service level reductions, employment of one-time revenues, and the lack of significant service enhancements over the past several fiscal years, the City of San Diego has been unable to resolve its financial and budgetary challenges. Several factors, such as persistent budget deficits in the face of strong economic growth, widespread use of one-time revenues and chronic under-funding of required expenditures indicate that the City is suffering from a structural budget deficit.

By nature, structural budget deficits are persistent, and cannot be solved with temporary or one-time solutions. Structural deficits require structural solutions. Unless clear, decisive, and long-term corrective actions are implemented, budget deficits will persist well into the future, resulting in continual erosion of municipal services.

The City must engage the community through budget workshops, community forums, and strategic visioning sessions in order to create a unified vision of what the City of San Diego should be. This vision will form the basis for the solutions to the City’s financial challenges. Finally, there must be a clear understanding of the tradeoffs that are inherent in making budgetary decisions. There are currently too many needs competing for limited resources, and the community will have to determine which services are deemed critical and desirable, and determine the means by which those services will be provided.

\_\_\_\_\_  
[SIGNED]  
Tom Haynes  
Fiscal & Policy Analyst

\_\_\_\_\_  
[SIGNED]  
APPROVED: Andrea Tevlin  
Independent Budget Analyst