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**Nancy Watt**  
County Executive Officer

To: Board of Supervisors

From: Nancy Watt, County Executive Officer

Date: March 16, 2010

Subject: **MID-YEAR FISCAL REVIEW – FISCAL YEAR 2009-10**

## **Introduction**

As you are aware, a mid-year review of the County's budget status, focusing particularly on the General Fund, is an important part of our on-going fiscal monitoring process. Using six months worth of actual revenue and expenditures, we work with departments and the Auditor's Office to forecast revenues, expenditures and Net County Cost, or General Fund Contribution, through the end of the fiscal year. This review enables us to address any current-year budget problems in a timely manner. It also assists us in preparing the FY2010-11 Budget, in part by providing an estimate of the FY2009-10 General Fund ending fund balance. As you know, the current year ending fund balance becomes the beginning fund balance, and thus a major budget source, for the next fiscal year.

As you are also aware, there are still many uncertainties with regard to future revenues and expenditures and these projections are, of necessity, somewhat problematic. After we have nine months worth of actual expenditure and revenue data, staff will be conducting a Third Quarter fiscal review which will provide a more accurate picture of what our year-end fiscal status is likely to be.

In addition to providing your Board with a Mid-Year fiscal status report, we typically take this opportunity to give you an update on the State's fiscal situation, focusing on its potential impact on the County's financial condition.

## **Mid-Year Fiscal Review**

### **General Fund Current Year Fiscal Status**

Using the most current information available, we believe that the General Fund will likely complete this fiscal year (2009-10) with an unreserved/undesigned ending fund balance of approximately \$20.8 million. This is roughly a \$7.5 million, or 57%, increase compared to the FY2009-10 Adjusted Budget Beginning Balance and a \$2.6 million, or 14%, increase compared to the actual FY2009-10 unreserved/unreserved beginning balance.

GENERAL FUND SUMMARY

	<u>2009-10 Adjusted Budget</u>	<u>Estimate</u>	<u>2009-10 Difference</u>
Resources:			
Fund Balance <sup>1</sup>	\$ 13,271,644	\$ 18,202,608	\$ 4,930,964
Revenue	198,671,353	201,243,689	2,572,336
Total Resources:	211,942,997	219,446,297	7,503,300
Requirements:			
Expenditures	206,322,306	198,675,467	(7,646,839)
Contingency	5,500,000	0	(5,500,000)
Total Required:	211,822,306	198,675,467	(13,146,839)
Difference:	\$ 120,691	\$ 20,770,830	\$ 20,650,139

The following is a brief explanation for the “differences” in each resource or requirement category identified in the above table.

1. Fund Balance: The General Fund’s undesignated/unreserved beginning fund balance is estimated to be approximately \$4.9 million, or 37%, higher than the Adjusted Budget level. This is due primarily to two factors:
  - The final, audited FY2008-09 ending fund balance was approximately \$2.4 million higher than the final unaudited ending balance estimate prepared in September of 2009. The September fund balance estimate assumed that a certain amount of revenue earned in FY2008-09 would be deferred to FY2009-10, based on the slow-down of payments from the State to counties. This estimate turned out to be overly conservative and some of those payments were received in time to be included as FY2008-09 revenue.
  - In January of 2010 the Board authorized the cancellation of \$2.5 million worth of the Designation for Fiscal Uncertainties, to allow the transfer of these monies to the Accumulated Capital Outlay (ACO) Fund. This has the effect of increasing the unreserved/undesignated fund balance and decreasing the reserved/designated fund

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<sup>1</sup> Unreserved/undesignated, except for reserve for encumbrances. In addition to the reserve for encumbrances, the Adjusted Budget Fund Balance number is based on the Final Budget estimated unreserved/undesignated Beginning Balance, revised to reflect budget adjustments, the cancellation of designations and new or increased designations and reserves approved through December 31, 2009. In addition to the reserve for encumbrances, the Estimated Fund Balance number is based on the final audited prior year ending fund balance, revised to reflect the actual or projected increase or cancellation of designations or reserves through June 30, 2010.

balance. This increase will be offset by an expenditure reflecting the transfer of these funds to the ACO Fund.

2. Revenue: FY2009-10 revenues are estimated to be approximately \$2.6 million, or 1.3%, higher than the amount included in the Adjusted Budget. Discretionary, or general purpose, revenues are projected to total approximately \$93.1 million, which is \$8.6 million, or 10%, higher than the budgeted level of \$84.5 million. The main reason for this increase in discretionary revenue is the projected receipt of approximately \$11.1 million in unbudgeted "Excess Excess ERAF" funds, partially offset by projected reductions in other discretionary revenues, including a \$2.6 million (28%) reduction in Transient Occupancy (hotel) tax revenue, a \$600,000 (50%) reduction in property transfer tax revenue and a \$600,000 (55%) reduction in investment earnings (see below for a more in-depth discussion of Excess Excess ERAF).

Departmental revenues are projected to be approximately \$6 million (5%) lower than the budgeted level. This is due primarily to:

- A projected \$1.3 million (8%) reduction in Realignment revenue that funds various Health & Human Services programs. Realignment revenue is allocated to counties based on formulae that involve statewide sales tax and Vehicle License Fee (VLF) collections. Those collections are projected to be down significantly due to the continuing impact of the national and state economic downturns.
  - A projected \$1.7 million (16%) reduction in Proposition 172 revenue that funds various public safety programs. Proposition 172 revenue comes from a statewide sales tax and is allocated to local governments based on a statutory formula. As indicated above, sales tax collections continue to decline statewide due to the economic downturn.
  - A projected \$2.6 million (43%) reduction in General Fund Capital Improvement Program (CIP) revenues from various sources, due primarily to delays in various capital construction projects. Appropriations for those projects, and related revenue, will be re-budgeted in FY2010-11.
3. Expenditures: Departmental expenditures are projected to be approximately \$7.65 million (4%) lower than the Adjusted Budget level. This is due primarily to: (1) salary savings in a number of departments due to higher than budgeted vacancy rates, in part related to the selective hiring freeze authorized by the Board; and (2) a \$4 million reduction in capital project expenditures in the Capital Improvement Program (CIP) budget (in most cases, these expenditures will be made in succeeding years).
  4. Contingency: This review assumes that none of the remaining Contingency will be "spent" this fiscal year (and any "use" of the Contingency that may be necessary is reflected in the above-projected expenditures).

An estimated unreserved/undesignated ending fund balance of approximately \$20.8 million indicates that the General Fund will have the necessary resources to make it through the rest of this fiscal year without the need to make expenditure reductions beyond those that have already been made or assumed in these projections. However, a major reason for the General Fund's positive situation this year is the receipt of a significant amount of Excess Excess ERAF revenue. The uncertain nature of this revenue source in the longer-term, when taken together with other factors described above and discussed below, suggests that caution is warranted concerning the secular condition of the General Fund.

The General Fund's actual, audited, FY2008-09 ending fund balance (including all designations and reserves) was \$50,670,646. This represents a \$699,000, or 1%, increase, compared to the FY2007-08 audited ending fund balance. If the Mid-Year projections come to pass, the FY2009-10 final ending fund balance will be \$53.2 million, a \$2.5 million (5%) increase compared to the FY2008-09 actual ending balance. However, the FY2008-09 ending fund balance reflected the receipt of \$6.6 million in Excess Excess ERAF in FY2008-09. If the County had not received that Excess Excess ERAF the General Fund's FY2008-09 ending balance would have stood at \$44 million, a \$5.9 million, or 12%, decrease from the FY2007-08 ending fund balance level. Similarly, if the County does not receive the estimated \$11.1 million in Excess Excess ERAF in FY2009-10, the estimated FY2009-10 ending fund balance would be approximately, \$42.1 million, an \$8.6 million (17%) decrease from the FY2008-09 actual ending fund balance level. If the County had not received any Excess Excess ERAF in FY2008-09 and FY2009-10, the FY2009-10 estimated ending fund balance would stand at approximately \$33 million, a 34% decrease from the FY2007-08 actual ending fund balance level. Thus, a key question in terms of the long-term condition of the General Fund is whether Excess Excess ERAF at the current level can be considered a reliable source of on-going revenue. Our conclusion is that it cannot, and thus, for long-term planning long-purposes, we should not assume Excess Excess ERAF at current levels will be available to fund on-going operations. As a consequence, the General Fund may still be facing a structural deficit. The prognoses for future Excess Excess ERAF revenue, along with other factors that will impact the General Fund's future fiscal condition, are discussed more fully below.

#### *Excess Excess ERAF*

As indicated above, the County's General Fund received \$6.6 million in Excess Excess ERAF in FY2008-09 and we estimate the General Fund will receive approximately \$11.1 million in FY2009-10. The County has received Excess Excess ERAF in previous years, but the amounts involved have been relatively small.

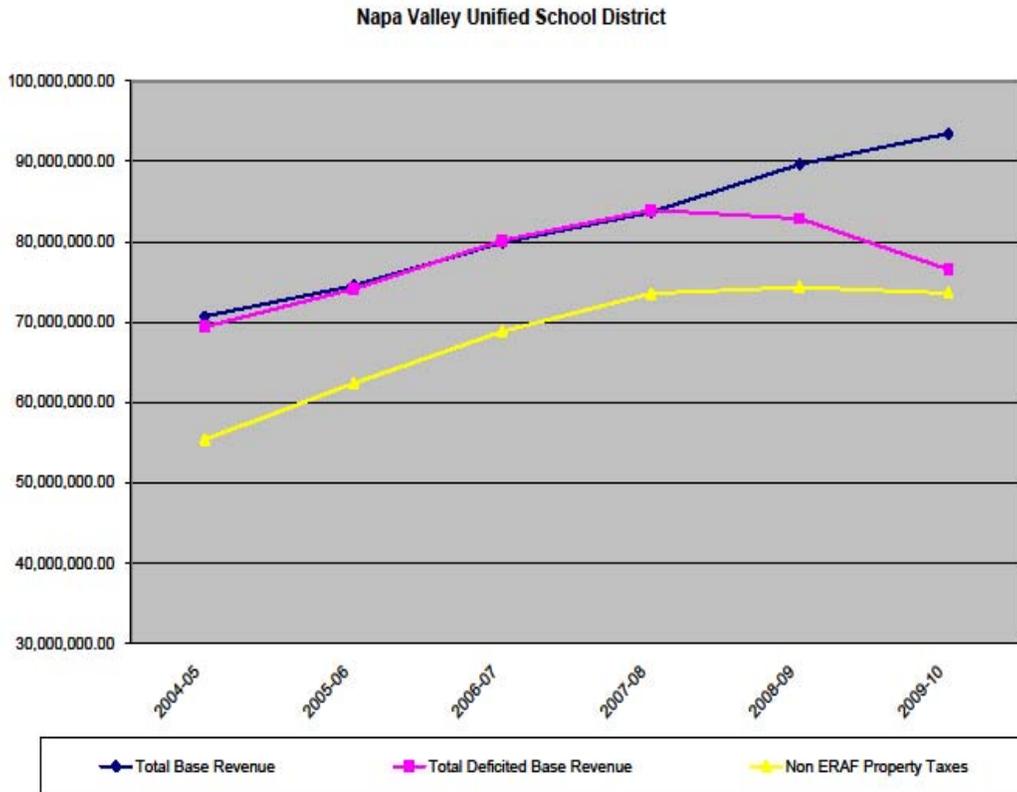
Research by the Auditor-Controller's Office indicates that there are a number of factors that determine whether and how much Excess Excess ERAF the County will receive. The most significant include: assessed value (and thus property tax) level and growth in the non-basic aid school districts, number of non-basic aid school districts (generally speaking, the fewer the number of non-basic aid school districts, the more likely it is there will be Excess Excess ERAF), average daily attendance in the non-basic aid districts, the amount of the non-basic aid school districts' Base Revenue Limit Cost of Living

Adjustments (COLAs), the Base Revenue Limit Deficit Factor, if any, and the special education programs designated to receive funding from Excess ERAF revenues<sup>2</sup>.

In the case of Napa County, we have only two non-basic aid school districts (Napa Valley Unified and the Community College), relatively high property tax assessed value and historic growth in assessed value, and little growth in student population. Thus the driving forces in whether we receive Excess Excess ERAF are assessed value growth in the Napa Valley Unified School District, the amount of the Base Revenue Limit COLA and the Base Revenue Limit Deficit Factor, if any, set by the State Legislature. Simply put, in those years where Napa Valley Unified School District property tax revenue is at least a certain amount lower than the Deficited Base Revenue Limit for the School District, no Excess Excess ERAF will be generated. In those years where the difference between School District property taxes and the Deficited Base Revenue Limit is less than a certain amount, Excess Excess ERAF is generated, and the amount of Excess Excess ERAF will increase as the gap between property tax revenues and the Deficited Base Revenue Limit narrows, but is not entirely eliminated (when property tax revenue equals or exceeds the Deficited Base Revenue Limit, then the school district becomes basic aid). The following table shows what has happened over the last few years in terms of Napa Valley Unified School District property tax revenues and Base Revenue Limit.

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<sup>2</sup>A Base Revenue Limit Deficit Factor occurs when the Legislature does not fully fund the Base Revenue Limit and, essentially, represents the percentage difference between the Base Revenue Limit (as adjusted by statutory COLAs) and the amount of funding provided by the Legislature.



As can be seen, from FY2004-05 through FY2007-08 the gap between the Napa Valley Unified School District’s property tax revenues and Base Revenue Limit narrowed. This generated Excess Excess ERAF in some years. This situation was exacerbated in FY2008-09 when, in an effort to limit the fiscal impact on the State (which is required to make up the difference between the Base Revenue Limit amount and local property taxes), the Legislature reduced funding below the Base Revenue Limit level, implementing a .07844 Deficit Factor. In that year the County’s General Fund received \$6.6 million in Excess Excess ERAF. For FY2009-10 the Legislature has increased the deficit factor to .18355 and we are projecting that the General Fund will receive \$11.1 million in Excess Excess ERAF. The following table shows what the Base Revenue Limit Deficit Factor and Excess Excess ERAF amounts have been for the last six years.<sup>3</sup>

<sup>3</sup> The numbers for the FY2004-05 through FY2007-08 calculations were based on Revenue Limit numbers provided by the School District. Based on information provided by the State, staff believes that these numbers were not the final Revenue Limit numbers and the Auditor-Controller’s Office is examining the Excess Excess ERAF calculations for those years to

	<u>Deficit Factor</u>	<u>Total E.E. ERAF<sup>4</sup></u>	<u>G.F. E.E. ERAF<sup>5</sup></u>
FY2004-05	.0245	\$ 816,450	\$ 632,550
FY2005-06	.00892	1,696,990	1,311,910
FY2006-07	0	0	0
FY2007-08	0	0	0
FY2008-09	.07844	8,574,920	6,638,360
FY2008-10 (Est.)	.18355	14,199,450	11,091,430

Given all of this, staff does not believe it would be prudent to assume that the County will continue to receive Excess Excess ERAF at current levels on a long-term basis. Once the economy, and State revenues, improve, it is likely the Legislature will come under increasing pressure to reduce the Deficit Factor, perhaps eventually fully funding school districts to the Base Revenue Limit level. At that point, unless assessed value and property taxes increase proportionally, the gap between the School District's property taxes and Base Revenue Limit will widen. And the amount of Excess Excess ERAF generated will decline, possibly, at some point, to zero.

Of course, it is possible that the Legislature will not reduce the Base Revenue Limit Deficit Factor any time in the future (or it may even increase it), or that property taxes will rise proportionally or at an even greater rate, or that Napa Valley School District property tax revenues will exceed its Deficit Base Revenue Limit, causing it to go basic aid. All of this, though, reinforces the point that there is considerable uncertainty about what will happen with Excess Excess ERAF in Napa County. At this point, we believe that a likely scenario would be that we will continue to receive Excess Excess ERAF revenue at somewhat less than the current level, but probably no less than \$5 million a year, for the next few years, and then the amount will decrease over time, possibly, eventually, to zero – unless the Napa Valley Unified School District goes basic aid in the near future - which is, in fact, a real possibility, particularly if the State does not reduce the Deficit Factor any time soon. If that were to happen, it is not entirely clear what the long-term impact would be on our Triple Flip/VLF Swap/Excess Excess ERAF revenues combined compared to the current level.

*Other Property Tax Revenue*

Leaving aside Excess Excess ERAF, it is clear that the rate of growth in property tax revenue is declining and the County may actually experience a decrease in property tax revenue (other than Excess Excess ERAF) over the next few years. Over the six-year period, from FY2001-02-through FY2007-08, secured property tax revenues – currently budgeted at \$43.5 million – increased at an average annual rate of 9.2%. In FY2008-09, secured property tax revenue increased by 6.6% compared to FY2007-08. We estimate that secured property tax revenue will grow by less than 2% in FY2009-10 and the Assessor is projecting a decline in assessed value of something less than 5% in FY2010-11. Based on

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determine if they are correct. Based on the Auditor's preliminary analysis, it appears that the County may have been entitled to additional Excess Excess ERAF in some of those years.

<sup>4</sup> Includes Excess Excess ERAF received by County, cities and special districts.

<sup>5</sup> County General Fund share of Excess Excess ERAF.

current trends, the Assessor also estimates that we will likely not see a turn-around in assessed value growth before FY2012-13.

#### *Transient Occupancy Tax Revenue*

Transient Occupancy Tax (TOT) revenue – budgeted at \$9.2 million – is declining due to the economic downturn. Between FY2007-08 and F2008-09, TOT revenue declined by 12.7% and we are currently projecting an additional 22% decrease this year compared to FY2008-09. We would generally expect TOT revenue to grow as the economy improves, and it does not appear that economic conditions are going to improve dramatically anytime soon. For example, the Federal Reserve Board (the “Fed”) is projecting moderate economic growth for the remainder of 2010 at the national level, with the rate of growth gradually picking up in 2011 and 2012, while some Fed economists hold the view that it could take 5 to 6 years before the economy will return to a state of sustainable economic growth. Similarly, economists at the Association of Bay Area Governments (ABAG) are predicting that the Bay Area economy will stabilize in 2010 and begin a slow recovery in 2011.

#### *Sales and Use Tax Revenue*

Sales and use tax revenue – currently budgeted at approximately \$4.8 million – is also declining due to general economic conditions. We are currently projecting a 10% decrease in sales tax revenue this year compared to FY2008-09. As with TOT, we would expect a very gradual growth in sales tax revenue starting in calendar year 2011.

#### *Realignment and Proposition 172 Revenues*

Realignment and Proposition 172 revenues – currently budgeted at approximately \$16.3 million and \$10.7 million respectively – are declining as well. Between FY2007-08 and FY2008-09, Realignment revenue declined by 12.5% and Proposition 172 revenue declined by 15%. We are currently projecting that Realignment revenue will decline by an additional 4% this year compared to FY2008-09 and Proposition 172 revenue will decline by an additional 14%. As indicated above, since these revenue sources are funded by statewide sales tax and vehicle license fee revenues, they have been impacted significantly by the national and state economic problems.

#### *Employee Compensation Costs*

General Fund employee salary and benefit costs currently exceed \$117 million annually (approximately 56% of total General Fund appropriations). It is certain that some of these costs will increase in the future, the County will likely be under pressure to increase some of these costs and the County faces a significant unfunded liability in a number of areas.

Currently, the General Fund cost of employee pensions exceeds \$15 million annually and the annual General Fund cost of Other Post Employment Benefits (OPEB – or retiree health benefits) exceeds \$3.8 million. Due to recent investment losses, CalPERS has indicated that employer pension costs will likely

increase over the next few years – by an estimated 4.5% in FY2011-12 and then an additional 20% in FY2013-14. In addition, CalPERS' investment losses have increased the County's pension unfunded liability, which now stands at \$55.7 million for our Miscellaneous (non-Safety) employees. For Safety employees, the County is part of a CalPERS pool that has a total unfunded liability of over \$387 million. In addition, we participate in two CalPERS Safety side funds, which together have an unfunded liability of approximately \$5.5 million. These unfunded liabilities will significantly impact the County's long-term pension costs which now exceed 17% of payroll for Miscellaneous employees and 27% for Safety employees. The County's OPEB unfunded liability currently stands at approximately \$30.4 million and that will have an impact on the County's long-term OPEB costs.

As the Board is aware, the current memoranda of understanding (MOUs) between the County and the two unions that represent most County employees expire this calendar year. The existing MOU with SEIU Local 1021, which represent most employees, did not provide for salary increases this year; the MOU with the Deputy Sheriff's Association provided for a 3.1% cost of living adjustment (COLA) this year. It is possible that one or both unions may seek employee compensation increases in negotiations for new MOUs. As a point of reference, every 1% increase in salaries, increases General Fund costs by approximately \$1 million per year.

#### *Facility Needs*

As the Board is aware, the County is facing the need to make significant investments in facilities in the relatively near future. Certain buildings on the Health & Human Services Campus have effectively reached the end of their useful life, other facilities (such as the Carithers Building) are obsolete and the County is out of space to meet current and/or projected needs. The recent Adult Correctional System Master Plan also identified the need to build a new, larger, jail.

The County currently has approximately \$19 million in the Accumulated Capital Outlay (ACO) Fund to help pay for needed facility improvements. However, the preliminary (and very rough) estimated cost of these improvements exceeds \$190 million to \$210 million (this includes approximately \$54 million to \$65 million to construct new buildings on the Health and Human Services Campus, approximately \$53 million to \$62 million to construct new office buildings on the Downtown Campus, approximately \$80 million to build a new jail and approximately \$3 million to exercise the County's option on the California Street property currently being leased to house the County's corporation yard). Some of this shortage can potentially be funded by the sale of certain surplus properties, but it is likely that a substantial gap between needed facility costs and identified funding will remain. As a point of reference, if the County were to borrow \$100 million to cover some of the improvement costs, the annual debt service would be in the area of approximately \$10 million for 20-year bonds.

#### *Analysis of Longer-term Fiscal Condition*

To factor all of the above and other issues (such as the impact of the State's budget situation on the County) into assessing the County's longer-term fiscal condition, staff will once again be preparing a General Fund Five Year Revenue/Expenditure Forecast for your review. As you will recall, based on information then available, staff presented your Board with a Five Year Forecast in September that

indicated that the General Fund would likely not be in structural balance over the next four years, with expenditures exceeding revenues by an average of 2% to 4% a year. That Forecast assumed the General Fund would receive at least \$4 million a year in Excess Excess ERAF and did not include additional costs related to meeting the County's major facility needs.

The above information suggests that it would not be prudent to assume that more than about \$5 million a year in Excess Excess ERAF can be used to fund on-going operations in the next few years, with that amount declining in subsequent years, as the national and state economies improve. The above information also suggests that other discretionary and semi-discretionary revenues (e.g., TOT revenue, sales tax revenue, Proposition 172 revenue) will likely decline more significantly than the September Five Year Forecast assumed.

As your Board knows, you have adopted a Fiscal Contingency Plan (copy attached) designed to provide a framework for addressing the County's fiscal problems and approved implementing certain elements of that Plan. The results of the upcoming General Fund Five Year Forecast will be used, along with other information, to help assess what additional Fiscal Contingency Plan actions, if any, may be needed.

#### Mid-Year Review of Department Budgets

This section generally focuses on current year General Fund, special revenue fund and enterprise fund departments, where expenditures and/or Net County Cost/General Fund Contributions are projected to exceed the budgeted level by \$50,000 or more. In addition, information is provided regarding certain other budget units where there are significant fiscal issues that the Board may need to address. Information concerning the Mid-Year status of all budget units is provided in Attachment A.

In general, where a budget unit is projected to exceed the approved appropriation level or Net County Cost, it is recommended that the department be directed to make every effort to come in within the budgeted Net County Cost level and that the department's fiscal status be revisited as part of the Third Quarter Fiscal Review. Any needed budget adjustments will be made at that time. Budget adjustments would be recommended at this time if it is estimated that there is insufficient appropriation authority to cover projected expenditures that will occur between now and the Third Quarter Review.

#### General Administration/Finance

##### *General Fund Budget Units:*

General Expenditures (18600): Expenditures and Net County Cost are projected to be approximately \$2.3 million (27%) higher than the Adjusted Budget level. This is due primarily to the budget adjustment approved by the Board in January, 2010 canceling part of a designation and transferring \$2.5 million to the Accumulated Capital Outlay (ACO) Fund. The Adjusted Budget for the Mid-Year Fiscal Review is based on the Final Budget plus changes made through December 31, 2009, and so does not reflect the January adjustment already made by the Board. This increase in expenditures is partially offset by expenditure decreases in a number of areas, including a \$190,000 decrease in the General Fund

transfer to the Napa County Housing Authority. This transfer will now be made from the Affordable Housing Fund.

Community Resources/Infrastructure

*General Fund Budget Units:*

Agricultural Commissioner/Sealer of Weights and Measures (26400): Expenditures are projected to be approximately \$81,000 (2%) higher than the Adjusted Budget level, revenues are projected to be approximately \$124,000 (6%) higher and the Net County Cost is projected to decrease by approximately \$43,000 (3%). The projected increase in expenditures is due to approximately \$120,000 in costs associated with the detection and trapping of the European Grape Moth that were not anticipated when the budget was approved. The Department anticipates that these costs will be fully offset by revenue from the State but, as of the time of this writing, official confirmation has not yet been received and so that additional revenue is not included in the Mid-Year Review estimates. Despite this, revenues are projected to exceed the Adjusted Budget level due to increases in other State contracts.

*Non-General Fund Budget Units:*

Building Inspection (26700)/Building and Code Enforcement Fund (1270): Expenditures are projected to be approximately \$300,000 (12%) lower than the Adjusted Budget Level and revenues are projected to be approximately \$530,000 (22%) lower. The Adjusted Budget reflected a \$230,000 reduction in the Building and Code Enforcement Fund's fund balance and these projections suggest the fund balance will be reduced by an additional \$230,000, for a total reduction of \$460,000 (40%) from the FY2008-09 audited ending fund balance level of \$1,125,000. The projected revenue reduction is due to the impact of the economic downturn on building activity in the unincorporated County. The Conservation, Development and Planning Department is currently seeing a roughly 10% decline in building permit activity compared to last fiscal year and a significant reduction in building permit value as well (and this is on top of a 20% decline in building activity in FY2008-09 compared to FY2007-08). The projected reduction in expenditures is due primarily to staff turnover and the Department's efforts to keep positions vacant. If these projections come to pass, the Building and Code Enforcement Fund's FY2009-10 ending balance will stand at approximately \$740,000 and Conservation, Development & Planning staff estimate that, depending on assumptions about future building activity, the fund balance could decline further to as low as \$200,000 in FY2011-12. For this reason, as part of this agenda item, staff will be requesting that the Board make a determination that a "financial hardship" exists, thus authorizing the Director of Conservation, Development and Planning, with the approval of the County Executive Officer, to implement a Voluntary Time Off program for employees in the Building Inspection Division.

Law and Justice

*General Fund Budget Units:*

District Attorney (22400): Expenditures are projected to be approximately \$110,000 (2%) lower than the Adjusted Budget level, revenues are projected to be approximately \$320,000 (18%) lower and Net County Cost is projected to increase by approximately \$210,000 (4%). The projected decrease in expenditures is due primarily to reductions in expenditures in various services and supplies categories. The projected decrease in revenue is due primarily to a \$179,000 reduction in Proposition 172 revenue and a reduction in the amount of Investigator time eligible to be billed to the Consumer Fraud and Vehicle Registration Funds due to an increase in the need for general investigation services. With regard to the latter situation, our Office is working with the District Attorney's Office to determine if this is a one-time issue or represents a long-term shift and, if the latter, how to deal with it in future budgets.

Public Safety and Justice

*General Fund Budget Units:*

Sheriff (23500): Expenditures are projected to be approximately \$171,000 (1%) lower than the Adjusted Budget level, revenues are projected to be approximately \$1,266,000 (10%) lower and Net County Cost is projected to increase by approximately \$1.1 million (11%). The primary reasons for the projected decrease in revenue are a \$587,000 reduction in Proposition 172 revenue and \$212,000 decrease in funding from the Court Service Agreement, due to mandatory furlough days at the Napa Superior Court. In response, the Department has reduced extra help Deputy hours and used these Court furlough days as training days in an effort to save on overtime costs. The Department is also estimating a \$120,000 reduction in RASCLEAP funds, a \$60,000 reduction in parking fine revenue and a \$100,000 reduction in funding from the American Canyon police services contract, where services have been reduced proportionately. The reduction in expenditures is due primarily to savings in various services and supplies line items. The Department has taken a more active role in monitoring overtime and other salary related expenses and, absent a major event, the Department should not need additional appropriations this year.

Corrections (24500): Expenditures are projected to be approximately \$243,000 (3%) lower than the Adjusted Budget level, revenues are projected to be approximately \$461,000 (11%) lower and Net County Cost is projected to increase by approximately \$218,000 (4%). The primary reason for the projected decrease in revenue is a \$433,000 reduction in Proposition 172 revenue. The primary reason for the projected decrease in expenditures is lower salary and benefit costs due to cost control efforts, such as intentionally holding positions vacant, under-filling positions with lower classifications and controlling overtime costs.

Detention Medical Services (24600): Expenditures are projected to be approximately \$298,000 (14%) higher than the Adjusted Budget level, revenues are projected to be approximately \$56,000 (19%) lower and Net County cost is projected to increase by approximately \$354,000 (20%). The projected increase in expenditures is due primarily to very high hospitalization costs for two seriously ill or injured inmates this fiscal year. Under its contract with the County, CFMG (the company that provides jail medical services) is only required to cover the first \$15,000 in offsite medical care costs, with the County responsible for anything above that amount. The projected decrease in revenues is due primarily to a reduction in Proposition 172 revenue. Staff is proposing a \$300,000 budget adjustment, and an offsetting reduction in the General Fund's Operating Contingency, to cover the projected expenditure increase.

### Human Services

#### *General Fund Budget Units:*

Overall, the Health & Human Services Agency is projecting that expenditures will be approximately \$2.47 million (3%) lower than the Adjusted Budget level, revenue will be approximately \$579,000 (1%) lower and Net County Cost will decrease by approximately \$1.9 million (18%). The projected decrease in revenue is due primarily to the projected \$1.3 million in reduction in Realignment revenue mentioned above. This and other revenue decreases are partially offset by various revenue increases, including the receipt of approximately \$1.9 million in unanticipated deferred revenue from the State.

As discussed with the Board in an October 27, 2009 update on the Health and Human Services Agency's budget, the Agency revised its operating plan to address various adverse fiscal developments beyond the control of the County. The Agency identified \$2.45 million in 50 detailed budget strategies to address funding shortfalls and has implemented most of the strategies and achieved approximately \$2 million in savings in FY2009-10.

Although the Agency is projecting that expenditures and Net County Cost for the Agency as a whole will not exceed the Adjusted Budget level, two of the Agency's eight budget units are projected to exceed their Adjusted Budget Net County Cost by more than \$50,000 as described below.

Health (40000): Expenditures are projected to be approximately \$119,000 (1%) lower than the Adjusted Budget level, revenues are projected to be approximately \$332,000 (3%) lower and Net County Cost is projected to increase by approximately \$213,000. The projected decrease in expenditures is due primarily to the implementation of various budget reduction strategies (including staffing reductions and the cancellation of contracts) in response to the decrease in State funding for various programs. The projected reduction in revenues is due to the projected decrease in Realignment revenue and in State categorical funding for various public health programs, including funding for Emergency Medical Services administration, HIV/AIDS education and prevention, maternal and child health services and the California Children's Services program. These and other revenue reductions are partially offset by the receipt of additional revenue from other sources, including unanticipated deferred revenue and \$256,000 in Public Health Emergency Response (PHER) funding that was not anticipated when the Budget was approved.

Substance Abuse Services (42200): Expenditures are projected to be approximately \$137,000 (3%) lower than the Adjusted Budget level, revenues are projected to be approximately \$413,000 (15%) lower and Net County Cost is projected to increase by approximately \$276,000. The primary reason for the projected decrease in expenditures is salary savings due to not filling vacant positions as a cost savings measure. The projected decrease in revenue is primarily a result of the termination of Proposition 36 funding from the State (treatment for non-violent offenders). Although not included in the Department's Mid-Year projections, the Department anticipates receiving a \$250,000 American Recovery and Reinvestment Act (ARRA) Justice Assistance Grant to cover the cost of Proposition 36 services this year.

#### Non-Operating Funds

This is the first Mid-Year Fiscal Review to include information on the fiscal status of the Non-Operating Funds, included in the County's Final Budget for the first time in FY2009-10. These funds were previously treated as trust funds, but are now included in the budget to comply with governmental accounting rules. These funds are classified as Non-Operating because direct expenditures are generally not made out of the funds. Instead, money in these funds is transferred to the relevant operating funds as appropriate to finance program expenditures.

#### *General Administration & Finance:*

Tobacco Settlement Trust (Fund 3103): Expenditures are projected to be the same as the Adjusted Budget level and revenues are projected to be approximately \$140,000 (9%) lower. This will require the cancellation of \$140,000 in designations to cover projected expenditures. The projected decrease in revenue is due to lower than expected interest earnings. This fund currently has approximately \$10.7 million in designations.

#### *Law and Justice:*

Proposition 64 Civil Penalties (Fund 3203): Expenditures are projected to remain as budgeted and revenues are projected to be approximately \$218,000 (75%) lower than the Adjusted Budget level. This will require the use of an additional \$218,000 in fund balance to cover projected expenditures. Resources in this Fund can only be used to pay for costs associated with the District Attorney's Consumer Fraud unit. When the budget was prepared, the District Attorney's Office expected that revenue would be generated as a result of the settlement of certain consumer fraud cases. These cases often take a very long time and it does not now appear that the expected settlements will occur this fiscal year. The Fund has a sufficient balance (approximately \$1.1 million as of June 30, 2009) to fund consumer fraud prosecution costs, with the expectation that settlements will result in substantial revenue in future years.

Consumer Fraud (Fund 3206): Expenditures are projected to remain as budgeted and revenues are projected to be approximately \$190,000 (94%) lower than the Adjusted Budget level. This will require the use of approximately \$37,000 in fund balance to cover projected expenditures. Resources in this Fund can only be used to pay for costs associated with the District Attorney's Consumer Fraud unit. As

was the case with Fund 3202 above, anticipated consumer fraud case settlements did not occur this fiscal year, but will likely occur in future years. This Fund had June 30, 2009 fund balance of \$83,822.

*Public Safety:*

Fingerprint ID (Fund 3222): Expenditures are projected to be approximately \$4,000 (9%) higher than the Adjusted Budget level, and revenues are projected to be approximately \$67,000 (47%) lower. This will require the use of approximately \$71,000 in fund balance to cover projected expenditures. Resources in this fund are used to help cover the Sheriff's Department's costs of purchasing and maintaining fingerprinting equipment. The reason for the projected increase in expenditures is that the Sheriff's Department needs to transfer an additional \$4,000 to the Sheriff's budget to cover the cost of maintaining the Department's fingerprinting equipment. A decrease in revenue is projected due to reduced interest earnings and a reduction in vehicle license fee revenue. This Fund had a June 30, 2009 fund balance of \$324,000.

*Human Services:*

HRSA – Health Resources & Services (Fund 3406): Expenditures are projected to be approximately \$75,000 (35%) higher than the Adjusted Budget level and revenues are projected to be approximately \$73,000 higher. This will require the use of approximately \$2,000 in fund balance to cover projected expenditures. The primary reason for the projected increase in expenditures and revenue is the receipt of additional federal funding for the Hospital Preparedness Program which prepares hospitals for public emergencies. These increased resources will be transferred to the Health & Social Services Agency's Public Health budget unit. Staff is proposing a budget adjustment increasing appropriations by \$74,804, revenue by \$72,804 and canceling \$2,000 worth of a designation to cover the projected expenditure increase.

CED – Public Health Emergency Response (Fund 3407): Expenditures and revenue are projected to be approximately \$300,000 (52%) higher than the Adjusted Budget level. The reason for the projected increase in expenditures and revenue is the receipt of approximately \$300,000 in additional revenue to reflect Phase 3 funding for H1N1 related activities. These increased resources will be transferred to the Health & Human Services Agency's Public Health budget unit.

**State Budget Issues**

On January 8<sup>th</sup>, the Governor released his proposed FY2010-11 State Budget, outlining a plan to eliminate an 18-month, \$19.9 billion deficit (\$6.6 billion in FY2009-10 and \$12.3 billion in FY2010-11). At the same time, the Governor declared a fiscal emergency and called the Legislature into session to address the State's immediate fiscal problems.

A key component of the Governor's proposed Budget is the assumption that the State will receive an additional \$6.9 billion in new federal funding. According to the Governor's proposal, if the State fails to secure these additional federal funds by July 15, 2010 then a list of reductions will be triggered, including:

- Eliminate CalWORKS;
- Use Proposition 63 monies to fund existing mental health services;
- Reduce Medi-Cal eligibility to the minimum allowed under current federal laws and eliminate most remaining optional benefits;
- Eliminate the In-Home Supportive Services (IHSS) program;
- Redirect county savings associated with the IHSS and CalWORKS reductions to the State;
- Expand crimes where convicted felons will serve time in local jails rather than State prison;
- Eliminate the Healthy Families Program.

Although it is possible the State will get some of the additional federal funds sought by the Governor, most observers believe that it is unlikely the State will get the full amount or even a significant portion of the amount reflected in the Governor's proposed budget. Even if the State were to get the full \$6.9 billion in additional federal funding, the Governor's budget still proposes significant reductions to health and human services programs (some of which would be made if the State doesn't get the additional federal funding as well), including:

- Medi-Cal: Implementation of various cost-containment strategies to achieve \$750 million in savings, including things like utilization controls, co-payments, etc.; eliminating Full-Scope Medi-Cal for certain immigrants; and eliminating Optional Adult Day Health Care benefits.
- Healthy Families Program: Reduce eligibility from 250% to 200% of the federal poverty level; eliminate vision coverage benefits; increase premiums for families with incomes from 151% to 200% of the federal poverty level.
- IHSS: Eliminate funding for all services for recipients with a Functional Index score of 4 or less; reduce State participation in provider wages to the State minimum wage of \$8 per hour.
- CalWORKS: Reduce CalWORKS grants by 15.7%; reduce child care provider reimbursements; eliminate the Recent Noncitizen Entrants program, which provides benefits to legal immigrants who have been in the U.S. less than five years (24,000 people).
- First 5: The Governor is proposing a ballot measure to redirect \$550 million in First 5 funds to other programs serving children. The proposal would shift 50% of the First 5 revenue to the State and counties to other State-administered programs and make a one-time sweep of State and local reserves.
- New County Share of Cost for Children's Programs: The Governor is proposing to redirect the counties' "savings" created by the proposed reductions to the CalWORKS and IHSS programs. The State would decrease State General Fund expenditures for children's programs and impose an increased county share of cost for Foster Care, Adoptions Assistance and Child Welfare Services.

- Mental Health Services Act: The Governor is also proposing to place another ballot measure before voters to redirect \$452.3 million in Mental Health Services Act (Proposition 63) funds to replace State General Fund support for the EPSDT and Mental Health Managed Care programs.

Some other provisions in the Governor's proposed Budget of interest to counties include:

- The continued elimination of funding for Williamson Act subventions.
- The modification of sentencing practices to allow offenders convicted of certain non-serious, non-violent, non-sex felonies to be incarcerated for up to one year in local jails rather than State prison.
- Funding to reimburse counties for the cost of last May's special election.
- Continued suspension of most reimbursable mandates which means, in theory, that the County could stop providing those services.
- Continued deferral of pre-2004 mandate reimbursements. The State had deferred mandate payments for several years prior to the passage of Proposition 1A in 2004, and had accrued a debt of more than \$1 billion. The provisions of Proposition 1A and State statute allow the State to repay that debt over a period of 15 years, but the State has deferred these annual repayments for the last few years.
- Eliminate the sales tax on gasoline (that funds Proposition 42 projects) and increase the excise tax on gasoline.

Staff has been analyzing the Governor's proposed Budget to determine its potential impact on Napa County, though it is likely that the final State budget will end up being significantly different than the Governor's proposal. In the meantime, the special session of the Legislature, called by the Governor to address the State's immediate fiscal problems, officially ended on February 22<sup>nd</sup>, after having passed bills reducing the State's deficit by approximately \$4 billion. It does not appear that any of these bills will have a major impact on Napa County's fiscal situation, with the exception of the bill dealing with the State's cash management, which will have an impact on the County's cash flow. That bill will allow the State to defer 9 months worth of HUTA (gas tax) payments to counties (from July 2010 through March 2011) – which would mean Napa County would not receive approximately \$1.1 million in revenue during this period. Under the bill, the County would be paid the entire deferred amount in April of 2011. It is expected that counties will also see up to three months of Social Services funding deferrals (representing about \$852,000 to Napa County) and a deferral of the July, 2010 Proposition 63 payment until May of 2011 (it is unclear what that would mean to Napa County because we don't always get a July payment, but we get a total of about \$3.2 million in Proposition 63 revenue each year).

As of this writing, there is one major budget bill still outstanding from the special session (it has passed the Assembly but not the Senate). This is a bill that builds on the Governor's budget proposal to eliminate the sales tax on gasoline (Proposition 42 funding) and replace it with an increase in the per

gallon excise tax on gasoline. Under the bill, as passed by the Assembly, the new excise tax monies would fund State General Fund transportation bonded debt service, State highway construction and local streets and roads improvements. In addition, Metropolitan Planning Organizations would be authorized to levy an additional local gas taxes, with the approval of a majority of the voters. If this bill were to pass it would likely not have an impact on Napa County's revenue in the short-term, but, in the longer-term Roads Fund revenue could be reduced because of the shift of the tax from a percent of value basis (that would grow with the increase in gas prices) to a cents per gallon basis (which would not grow with increase in gas prices).