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County Executive Officer

A Tradition of Stewardship
A Commitment to Service

To: Board of Supervisors

From: Nancy Watt, County Executive Officer

Date: March 4, 2011

Subject: **MID-YEAR FISCAL REVIEW – FISCAL YEAR 2010-11**

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 FY2011-12 Budget, in part by providing an estimate of the FY2010-11 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 (2010-11) with an unreserved/undesignated ending fund balance of approximately $22 million. This is roughly a $5.5 million, or 20%, decrease compared to the actual FY2010-11 undesignated/unreserved beginning balance.

GENERAL FUND SUMMARY

	2010-11 Adjusted Budget	Estimate	2010-11 Difference
Resources:			
Fund Balance	$ 24,952,841	$ 27,382,262	$ 2,429,421
Revenue	211,231,754	219,535,063	8,303,309
Total Resources:	236,184,595	246,917,325	10,732,730
Requirements:			
Expenditures	229,530,689	224,067,479	(5,463,210)
Contingency	5,771,000	0	(5,771,000)
Increase Reserves	961,154	961,154	0
Total Required:	236,262,843	225,028,633	(11,234,210)
Difference:	($ 78,248)	$ 21,888,692	$ 21,966,940

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 $2.4 million, or 10%, higher than the Adjusted Budget level. This is due primarily to the receipt of a higher level of Social Services revenue than the amount estimated in October 2010. Prior to the end of every fiscal year, the Health & Human Services Agency (HHSA) estimates the amount of state and federal revenue it will receive in that fiscal year and that number is factored into the calculation of the ending fund balance for that fiscal year (which becomes the budgeted beginning fund balance for the next fiscal year). That estimate is then updated after the end of the fiscal year to reflect revenue that will likely be accrued into the prior year. For FY2009-10 that update was reflected in the October 2010 report to the Board which included budget adjustments to incorporate the final, unaudited General Fund ending fund balance. This number, in turn, is trued up as part of the annual audit process. For the October 2010 report, HHSA under-estimated the amount of Social Services revenue that would actually be accrued into FY2009-10.

2. Revenue: FY2010-11 revenues are estimated to be approximately $8.3 Million, or 3.9%, higher than the amount included in the Adjusted Budget. Discretionary, or general purpose, revenues are projected to total approximately $105.4 million, which is $13.7 million, or 15%, higher than the budgeted level of $91.8 million. The main reason for this increase in discretionary revenue is the projected receipt of approximately $9.3

million in unbudgeted prior year Excess Excess ERAF revenue. When the County began receiving significant amounts of Excess Excess ERAF revenue, the Auditor's Office initiated a review of prior year ERAF calculations to determine if the calculations were correct. That review revealed that the General Fund was owed additional Excess Excess ERAF revenue for three prior years (FY2006-07, FY2007-08 and FY2008-09) totaling $9.3 million. In addition, a number of other discretionary revenues are projected to come in higher than the Adjusted Budget level, including Secured and Unsecured Property Taxes (3% and 30% higher respectively) and Transient Occupancy Tax (TOT) (28% higher). These and other projected increases compared to the Adjusted Budget level are partially offset by projected reductions in other discretionary revenue sources, including a 22% reduction in Supplemental Property Taxes, a 5% reduction in Sales and Use Tax revenue and a 58% reduction in interest earnings.

Departmental revenues are projected to be approximately $5.3 million (5%) lower than the budgeted level. This is due primarily to:

- A projected $2.5 million (25%) reduction in General Fund Capital Improvement Program (CIP) revenues from various sources, due primarily to delays in various capital construction projects. Appropriations for most of these projects and related revenue will be re-budgeted in FY2011-12.

- A projected $719,000 (4%) reduction in various Mental Health revenues, including the elimination of funding for the AB 3632 Mandate (Mental Health services for students) that was suspended by the State and a decrease in funds transferred in from the Managed Care Trust Fund.

- A projected $588,000 (24%) reduction in fee revenue in the Conservation, Development & Planning Department, due to the continued economic downturn and only one pass-through vineyard development project.

- A projected $468,000 (13%) reduction in revenue to the Probation Department, primarily because the Department will not draw down as much Youth Offender Block Grant rollover funding, due to position vacancies. Other revenue reductions include a $30,000 reduction in Gang Violence Suppression Grant funds.

- A projected $453,000 reduction in revenue to the Community & Intergovernmental Affairs (CIA) Division budget from Napa Redevelopment Partners. The CIA budget included $500,000 in revenue from the Napa Pipe developer to cover potential costs associated with reviewing the Napa Pipe development project. It is now estimated that only $50,000 will be spent on this project this fiscal year.

These and other revenue decreases are partially offset by certain revenue increases, including an unexpected reimbursement from the State of $228,000 to cover the costs of the May 19, 2009 special election.

3. Expenditures: Departmental Expenditures are projected to be approximately $5.5 million (2.4%) 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; (2) a reduction in contract costs in a number of departments, including the Health & Human Services Agency and the CIA Division; and (3) a $5.7 million reduction in capital project expenditures in the Capital Improvement Program (CIP) budget (in most cases these expenditures will be made in succeeding years). These projected expenditure decreases are partially offset by expenditure increases in a number of areas, including a $4.9 million increase in Employee-Retiree Benefits, due to the recently-approved Memorandum of Understanding (MOU) with the Deputy Sheriff's Association that calls for the County to pay off a pension side fund, which was originally created as a result of a CalPERS requirement that our Safety employees be pooled with like-sized entities.

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 $22 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. At the same time, the fact that the fund balance is projected to decline (indicating that expenditures are projected to exceed revenues) could be a cause for concern. It should be noted, though, that this fund balance reflects the impact of a number of one-time or limited duration revenues and expenditures. Taking the net result of those one-time impacts into consideration, along with certain other factors discussed below, suggests that caution is warranted concerning the secular condition of the General Fund.

The General Fund's actual, audited, FY2009-10 ending fund balance (including all designations and reserves) was $61,373,784. This represents a $10.4 million, or 20%, increase compared to the FY2008-09 audited ending fund balance. If the Mid-Year projections come to pass, the FY2010-11 ending fund balance will be $56.8 million, a $4.5 million, or 7.4%, decrease compared to the FY2009-10 actual ending balance. However, as suggested above, these numbers include a number of one-time or limited duration revenues and expenditures, including:

- Excess Excess ERAF: In FY2010-11 it is estimated that the General Fund will receive approximately $19.63 million in Excess Excess ERAF revenue. This includes the FY2010-11 allocation of $10.3 million and the $9.3 million in prior year revenues. All-told, between FY2004-05 and FY2010-11 it is estimated that the General Fund has received or will receive approximately $41.2 million in Excess Excess ERAF revenue (of which, approximately $30 million has been transferred to the Accumulated Capital Outlay Fund, as described below). Excess Excess ERAF is a volatile revenue source and its future is uncertain. For this reason, Board policy calls for not using more than $5 million a year in Excess Excess ERAF to fund on-going County operations.

- Transfer to the ACO Fund: The FY2010-11 General Fund Budget includes the transfer of $12.2 million to the Accumulated Capital Outlay (ACO) Fund as capital reserves that will be used to help pay for future capital facility needs. Board policy generally calls for transferring any remaining General Fund resources to the ACO Fund after all operating, capital and reserve requirements have been met. All-told, between FY2006-07 and FY2010-11, it is estimated that approximately $30.8 million will be transferred from the General Fund to the ACO Fund.

- Transfer to Roads Fund: The Board has historically allocated approximately $900,000 a year from the General Fund to the Roads Fund to help finance road maintenance activities. In addition, in three recent fiscal years (FY2005-06, FY2007-08 and FY2010-11), when additional General Fund resources were identified, the Board authorized extra allocations (in FY2010-11 the Board specified the extra allocation was to come from Excess Excess ERAF). Since FY2005-06, these extra allocations have totaled $3,623,000.

- PERS Safety Side Fund Payoff: As indicated above, this is a one-time General Fund cost of approximately $4.9 million.

To provide a better picture of what the General Fund's status would be based on on-going, or operating, costs and revenues, the following table adjusts the General Fund's actual historical revenues and expenditures and the FY2010-11 Mid-Year estimate as follows:

- No more than $5 million in Excess Excess ERAF revenue is recognized in any fiscal year.
- No transfers to the ACO or Roads Funds are included in annual expenditures.
- The one-time pay-off of the Safety side fund is not shown as an expenditure in FY2010-11.

Fiscal Year	2004-05 Actual	2005-06 Actual	2006-07 Actual	2007-08 Actual	2008-09 Actual	2009-10 Actual	2010-11 Estimated
Revenue	151,310,313	175,245,092	178,941,271	182,641,182	189,606,113	195,247,552	204,960,937
Expenditures	151,478,787	164,930,100	170,356,592	179,824,173	190,248,489	190,292,350	206,952,363
Difference	(168,474)	10,314,992	8,584,679	2,817,009	(642,367)	4,955,202	(1,991,426)
Percent Difference	0%	6%	5%	2%	0%	3%	(1%)

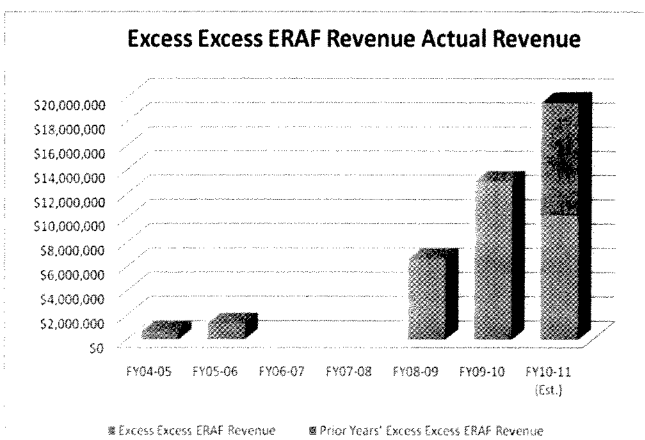
As can be seen, over the three fiscal years from FY2008-09 through FY2010-11 (roughly the period of the current economic downturn), General Fund "operating" revenue has exceeded or is projected to exceed "operating" expenditures by an average of approximately 0.3% each year. This does not suggest that the General Fund is in dire straits, but it does suggest that operating revenues and expenditures are finely balanced, particularly considering that FY2009-10 and FY2010-11 budgets reflect the impact of implementing the Board's Fiscal Contingency Plan and other cost saving actions, some of which will not likely be continued indefinitely. Those actions include:

- No Cost of Living Adjustments (COLAs) were provided to most employees in FY2009-10 and FY2010-11.
- Starting in FY2009-10, approximately $600,000 a year in Proposition 172 funding was shifted from the Fire Protection Fund to General Fund public safety departments.
- Starting in FY2009-10, approximately $680,000 a year in Housing Authority and Homeless Services costs were shifted from the General Fund to the Affordable Housing Fund.
- Starting in FY2010-11 the annual General Fund contribution to the Library Fund was reduced by $169,000.
- Starting in FY2009-10, the County moved from a 14-year to a 20-year amortization schedule for our Other Post Employment Benefits, saving approximately $400,000 annually in Net County Cost.
- In FY 2009-10 the County eliminated 8 positions and in FY2010-11 we eliminated 3 positions, for a total annual Net County Cost savings of $970,000.
- The County implemented a selective hiring freeze starting in FY2008-09.

A more detailed discussion of some of the above and other factors that will impact the General Fund's future fiscal condition is provided below.

Excess Excess ERAF

The following table shows the amount of Excess Excess ERAF the County has received or is projected to receive.



As noted above, Excess Excess ERAF is a volatile revenue source with an uncertain future in Napa County. As the Board is aware, Excess Excess ERAF is essentially a return to the taxing agencies of a portion of property tax revenue used by the State to meet its school funding obligation and there are a number of factors that determine whether and how much Excess Excess ERAF revenue the County will receive. The most significant include: assessed value (and thus property tax) level and growth in the non-basic aid school districts, the 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 school districts, the non-basic aid school districts Base

Revenue Limit Deficit Factor, if any, and the special education programs designated to receive funding from ERAF revenues.

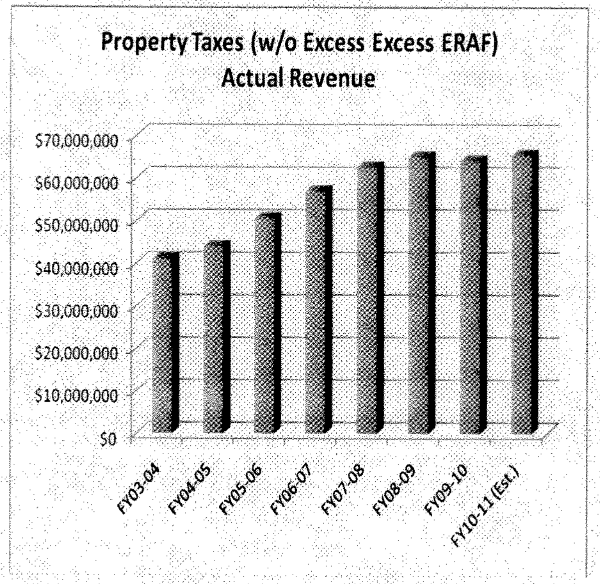
In the case of Napa County, we have only two non-basic aid school districts (Napa Valley Unified and the Community College), relatively high property assessed value and historic growth in assessed value and little historic growth in student population. Thus the driving forces in whether we receive Excess Excess ERAF are assessed value growth in the Napa Valley Unified School District, the amount of any Base Revenue Limit COLA and the Base Revenue Limit Deficit Factor, if any, set by the State Legislature. In recent years, the County received a substantial amount of Excess Excess ERAF due primarily to the Legislature's decision to impose a school Base Revenue Limit Deficit factor in order to reduce State education expenditure obligations. Since FY2007-08, the Deficit Factor has gone from 0 to 18.4%, and the County's annual Excess Excess ERAF revenue has gone from 0 to over $10 million.

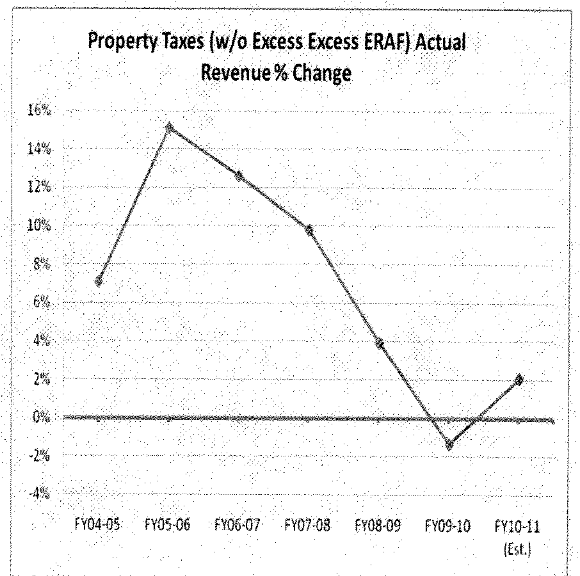
In terms of the future, it is difficult to predict what will happen with all of the Excess Excess ERAF variables, but staff continues to believe that it would not be prudent to assume that the County will receive Excess Excess ERAF at current levels on a long-term basis. Once the economy and State revenues 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 proportionately, 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.

Given all of this, staff believes that a likely scenario would be that we will continue to receive Excess Excess ERAF revenue at somewhat less than the current year level not including the prior years' repayment amount (approximately $10 million), but probably no less than $5 million a year, for the next few years, and then the amount will decrease, possibly, eventually, to zero – unless the Napa Valley Unified School District and the Napa Valley Community College District go basic aid. 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 compared to the current level.

Other Property Tax Revenue

The following tables show the amount of property tax revenue (other than Excess Excess ERAF) that the County has received or is projected to receive since FY2003-04.

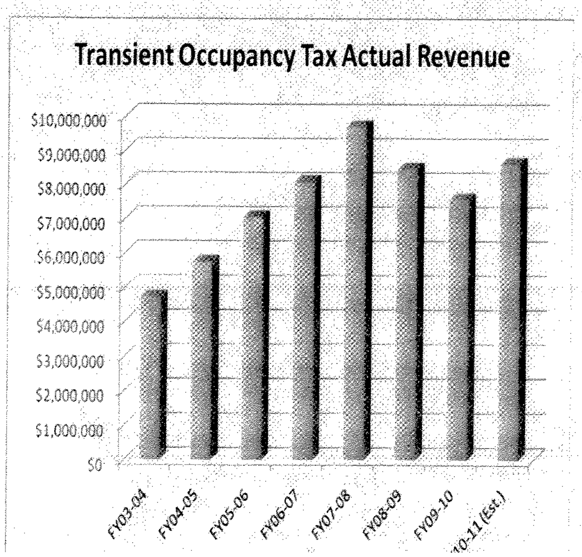


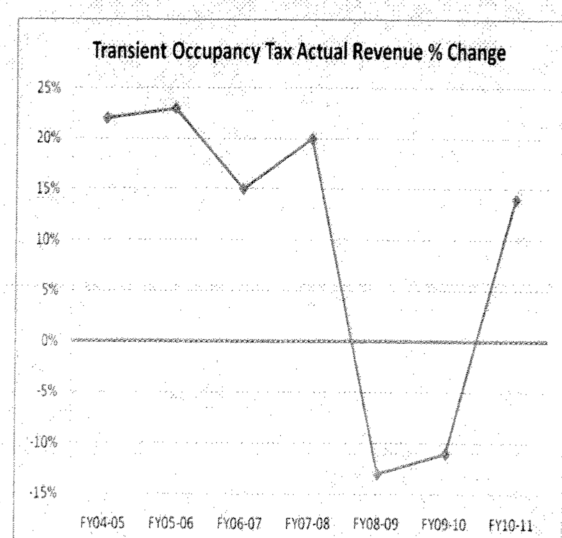


As can be seen, over the two year period between FY2007-08 and FY2009-10, non-Excess Excess ERAF property tax revenues increased by a total of 3%, a significant decline from the double-digit increases that were common in the years preceding the "Great Recession." For FY2010-11, staff is currently projecting a 2% increase in revenue from this source. Based on current market conditions, the Assessor is projecting that assessed value will remain roughly flat for at least the next two fiscal years.

Transient Occupancy Tax Revenue

The following tables show the amount of Transient Occupancy Tax (TOT) revenue the County has received or is projected to receive since FY2003-04.

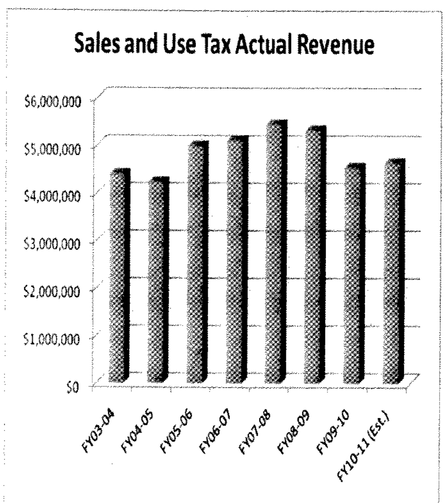


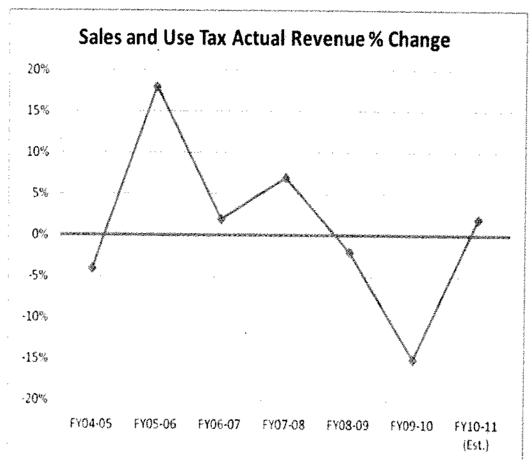


As can be seen, over the two year period between FY2007-08 and FY2009-10, TOT revenue declined by a total of 22%. For FY2010-11, staff is currently projecting 14% increase in revenue from this source compared to the FY2009-10 actual level. Based on recent experience, it appears that significant changes in economic conditions have a more immediate and robust impact on TOT than on the County's other major discretionary and semi-discretionary resources. According to many economists, the national and state economies have now stabilized and are beginning to grow at a relatively slow rate, suggesting that we will continue to see increases in TOT revenue in FY2011-12 and beyond, though perhaps at a somewhat lower growth rate than 14%.

Sales and Use Tax Revenue

The following tables show the amount of sales and use tax revenue the County has received or is projected to receive since FY2003-04.

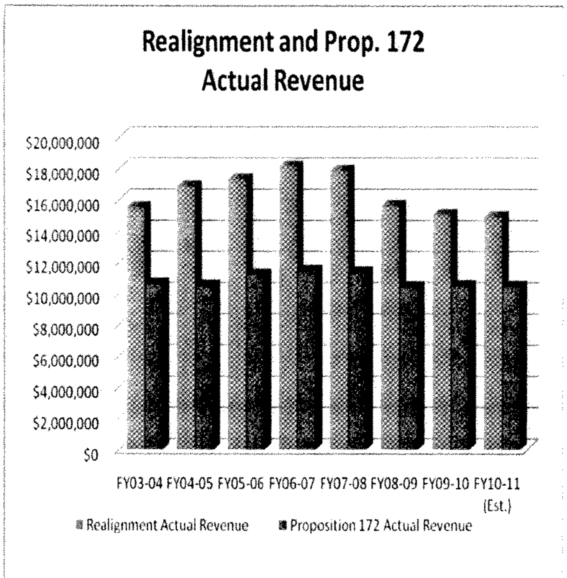


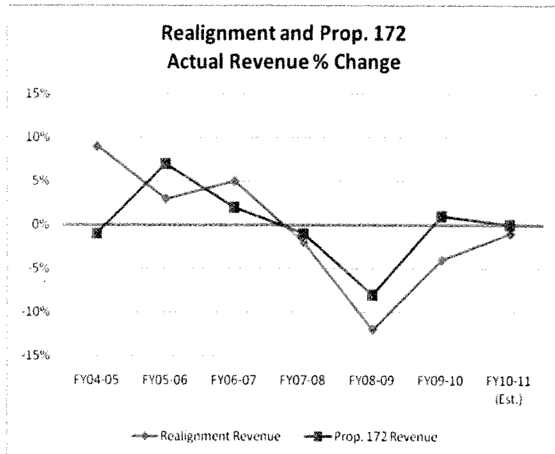


As can be seen, over the two year period between FY2007-08 and FY2009-10, sales and use tax revenue declined by a total of 17%. For FY2010-11, staff is currently projecting a 2% increase in revenue from this source, though based on more recent sales tax data, this number may be somewhat conservative and, at Third Quarter, staff may revise this estimate slightly upward. We would generally expect sales and use tax revenue to grow as the economy improves, and, as mentioned above, many economists are indicating that the economy has now stabilized and is beginning a period of relatively slow growth. For example, a recent forecast by Beacon Economics predicted that Bay Area taxable sales will not return to peak, pre-recession, levels until the first quarter of the 2015 calendar year.

Realignment and Proposition 172 Revenues

The following tables show the amount of Realignment and Proposition 172 revenue the County has received or is projected to receive since FY2003-04.





As can be seen, over the two year period between FY2007-08 and FY2009-10, Proposition 172 and Realignment revenues declined by a total 8% and 16% respectively. For FY2010-11, staff is currently projecting that Proposition 172 revenue will remain flat at the FY2009-10 level and Realignment revenue will decline by 1%, though based on more recent sales tax data these numbers may be somewhat conservative and, after another quarters worth of data is available, may be revised slightly upward. As the Board knows, Realignment and Proposition 172 revenue are funded by statewide sales tax and vehicle license fee revenues, and thus, as with local sales and use tax revenue, should roughly track general economic conditions.

Employee Compensation Costs

General Fund employee salary and benefit costs currently exceed $117 million annually (approximately 50% of General Fund expenditures). 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 significant pension and retiree health insurance unfunded liabilies.

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 $4 million. As the Board is aware, recent investment losses at CalPERS have increased the County's pension unfunded liability – by 50%, to $83.7 million, for our Miscellaneous (non-Safety) employees. Given this, the County's actuaries are projecting that the County's pension costs as a percent of payroll will increase by 17% - to 21% - by FY2013-14 (and this takes into account the recent agreement by the Deputy Sheriff's Association to move to a second tier retirement formula for new hires and the existing agreements with both of the County's unions that provide that the County and employees will share equally in any pension cost increases). Generally speaking, moving to a new retirement tier with a lower level retirement formula for new employees generates savings over the long-term rather than immediately.

Currently, the General Fund cost of employee health benefits exceeds $13 million annually and these costs have been increasing at a fairly significant rate. We are estimating that employee health insurance rates will increase by 9.5% in January of 2012, increasing General Fund costs by at least $600,000 in FY2011-12, with an annualized cost impact of approximately $1.2 million in future years. Further, there is a considerable uncertainty with regard to how the new Federal health insurance reform act will impact insurance rates.

The County recently signed a one-year Memorandum of Understanding (MOU) with the Deputy Sheriffs Association (DSA) that did not include a cost of living adjustment (COLA) and, as noted above, provided for a second tier retirement formula for new hires – with a pension benefit of 3% at 55 rather than 3% at 50. Under the current MOU with SEIU - the union representing the County's non-safety employees - those employees did not receive a COLA this year; they also did not receive a COLA last year. The current agreement expires June 30, 2011 and the County is currently in negotiations with SEIU. It is possible that SEIU will seek employee compensation increases this year and that both unions will seek compensation increases in future years. As a point 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 Adult Correctional System Master Plan has also identified the need to build a new, larger, jail. The Board recently received a Preliminary Financing Plan and Feasibility Analysis for the County's Major Facilities Capital Projects. That document identified a total of $276 million in facility needs, divided between projects that should be considered in the next five years and projects that should be considered in later years. For the next five years, the report identified $63 million in projects, with only $46 million in funds likely available. If the identified projects are to proceed, the difference – approximately $17 million – will need to come from some yet-unidentified source, potentially the issuance of Certificates of Participation (COPs). Borrowing $17 million through COPS would cost approximately $1 million a year in debt service.

For the post-2014-15 projects, the Preliminary Financing Plan only identified funding for a small fraction of the cost. This includes a new jail – at an estimated cost of $97 million - the need for which may become more urgent if the State Legislature approves the Governor's proposal to shift certain offenders from State prison to county jails. The annual debt service on $97 million in COPs would be in the area of $6 million.

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 last April that indicated that, assuming only $5 million a year in Excess Excess ERAF is available to fund on-going County operations, the General Fund would likely not be in structural balance over the next four years, with Net County Cost exceeding discretionary revenues by an average of approximately 3% a year.

Mid-Year Review of Department Budgets

This section generally focuses on current year General Fund, special revenue 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:

County Counsel (12500): Expenditures are projected to be approximately $222,000 (6%) higher than the Adjusted Budget level, revenues are projected to be approximately $84,000 (18%) higher and Net County Cost is projected to increase by approximately $139,000 (54%). Approximately $125,000 of the increase in expenditures is due to unanticipated costs associated with pending litigation involving recognition of the Native American tribe and the need for a County hearing officer related to the ambulance franchise proceedings. The remainder of the cost increase is due to the addition of a Deputy County Counsel position that the Board approved during the fiscal year, but with no adjustment to appropriations. Among other things, this new position will provide legal services to the Napa County Transportation and Planning Agency (NCTPA) and most of the current year cost of this position will be covered by additional revenue from that Agency. Staff is proposing budget adjustment increasing appropriations $225,000 for this budget unit, offset by an $84,000 increase in departmental revenue and a $141,000 reduction in the General Fund's Operating Contingency.

Employee/Retiree Benefits (18800): Expenditures and Net County Cost are projected to be approximately $4,850,000 (396%) higher than the Adjusted Budget level. This budget unit does not receive any revenues. The increase in expenditures and Net County Cost is due primarily to the need to pay off the PERS Safety side fund, as required by the recently approved MOU between the County and the Deputy Sheriff's Association. Paying off the Safety side fund will reduce both County and employee PERS costs compared to what they would otherwise have been and, over the long-term, result in net cost savings to the County. Staff is proposing a budget adjustment increasing appropriations by $4,850,000. This increase will be offset by an increase in budgeted revenues in the Non-Departmental Revenue budget unit.

Non-Departmental Revenue (11300): Revenues are projected to be approximately $13,646,000 (15%) higher than the Adjusted Budget level. This is due primarily to the receipt of approximately $9.3 million in unbudgeted prior-year Excess Excess ERAF revenue. Staff is proposing a budget adjustment, increasing Excess Excess revenue by $4,850,000, to cover the cost of the additional contribution to PERS to pay off the Safety side fund as discussed above.

Community Resources/Infrastructure

General Fund Budget Units:

Public Works/Engineering (17500): Expenditures are projected to be approximately $335,000 (5%) lower than the Adjusted Budget level, revenues are projected to be approximately $382,000 (8%) lower, and Net County Cost is projected to increase by approximately $47,000 (3%). The projected decrease in revenue is due primarily to a general reduction in permit revenues, reflecting the impact of the economic downturn on development in the unincorporated area. In addition, revenue from various funds and sources to pay certain engineering and/project management costs is down, due to delays in implementing a number of projects. The projected decrease in expenditures is due primarily to a higher than anticipated number of position vacancies. Currently, this Department has 5 vacant positions.

Roads (30000): Expenditures are projected to be approximately $147,000 (25%) lower than the Adjusted Budget level, revenues are projected to be approximately $242,000 (43%) lower and Net County Cost is projected to increase by approximately $94,000 (314%). This budget unit acts as a pass through for the two private parties that are paying CalTrans for the construction of turn pocket improvements to State Highway 121 between Duhig Road and the Sonoma County line. Each year the parties pay the County and the County then pays CalTrans as billed. Last year, one of the parties paid in advance because of pending litigation. At the end of FY2009-10, the balance of $99,054 rolled into the General Fund's ending fund balance but was inadvertently not designated for this project. The net effect is that this year there appears to a Net County Cost of $124,225. In fact, after applying the remaining balance from last year, the Net County Cost is actually only $25,171, slightly lower than the budgeted $30,000.

Non-General Fund Budget Units:

Building Inspection (26700)/Building and Code Enforcement Fund (1270): Expenditures are projected to be approximately $136,000 (6%) lower than budgeted, revenues are projected to be approximately $96,000 (5%) lower and the Division is projected to use $40,000 (12%) less of fund balance than budgeted. The Building Inspection budget unit does not receive a General Fund Contribution. The projected decrease in building fee revenue is due to the lingering effects of the recent recession on development in the unincorporated area. In response to the further decline in revenues, the Division has made a concerted effort to reduce expenditures in a variety of areas. At the end of the last fiscal year, the Building and Code Enforcement Fund's ending balance stood at $742,000, of which $570,000 was attributable to the Building Inspection function and $171,000 to the Code Enforcement function. Based on these projections, even with the projected reduction in use of fund balance, by the end of this fiscal year Building Inspection Division will spend down the fund balance by $285,000, leaving a Building Inspection-related fund balance of $285,000, which is 13% of Building Inspection expenditures (the Fund's total ending balance will be approximately $358,000). When the FY2010-11 Budget was developed, it was with the understanding that fund balance would be spent down significantly this year, but with the hope that fee revenues would begin to increase and the rate of fund balance reduction would decrease significantly in FY2011-12 and then the fund balance would start to grow again. Thus far, the Conservation, Development & Planning Department (CDPD) is not seeing an increase in fee revenues and is concerned about the fiscal sustainability of the Building Inspection function. CDPD and County Executive Office staff will be presenting options for dealing with this issue as part of the FY2011-12 budget study session.

Law and Justice

General Fund Budget Units:

Public Defender (22600): Expenditures are projected to be approximately $54,000 (2%) higher than the Adjusted Budget level, revenues are projected to be approximately $10,000 (1%) higher and Net County Cost is projected to increase by approximately $44,000 (0.2%). The projected increase in expenditures is due primarily to additional investigative and outside mitigation specialist costs, related to a potential death penalty case the Department is handling.

Public Safety

General Fund Budget Units:

Sheriff (23500): Expenditures are projected to be approximately $115,000 (0.5%) lower than the Adjusted Budget level, revenues are projected to be approximately $165,000 (1%) lower and Net County Cost is projected to increase by approximately $50,000 (0.5%). The primary reasons for the projected decrease in revenue are the projected loss of $127,000 in CAL-MMET (methamphetamine enforcement) funds and reductions in Rural and Small County Law Enforcement Assistance Program (RASCLEAP) and certain fee and service based revenues. The loss of CAL-MMET and reduction in RASCLEAP funds are due to the fact that the State over-allocated Vehicle License Fee (VLF) funds last fiscal year and have notified counties that they are using a substantial portion of this year's funding to cover the over-allocation, thus reducing the amount of VLF funds counties will receive this year. The Department has attempted to offset these revenue reductions with reduced supply and equipment purchases. It should be noted that these Mid-Year projections do not reflect the reduction in PERS costs that will result from the paying off of the Safety side funds. This reduction in costs will become effective April 1, 2011 and will be reflected in the Third Quarter estimate for this Department.

Corrections (24500): Expenditures are projected to be approximately $93,000 (1%) lower than the Adjusted Budget level, revenues are projected to be approximately $196,000 (5%) lower and Net County Cost is projected to increase by approximately $102,000 (2%). The reduction in revenue is partly due to a $90,000 reduction in the Federal allocation for the State Criminal Alien Assistance Program, which provides funds to offset the cost of housing individuals pending transport by the Immigration and Customs Enforcement Agency. The annual Federal allocation is distributed to all jails nationwide and it is difficult to estimate the amount the County will receive in each year. The remaining reduction in revenue reflects decreases in various fees for services, including a reduction in the number of meals prepared under the Senior Nutrition Program contract, booking fees and fees for correctional services like electronic monitoring. Correctional services fees are often waived based on an offenders ability to pay. The projected decrease in expenditures is due to reductions in various salary, benefit and services and supplies line items, in part resulting from salary savings due to employee turnover. The Corrections Department added four Correctional Officer positions in December without a budget adjustment and, had it not been for those additional positions, Net County Cost would have been projected to come in substantially below the Adjusted Budget level.

Human Services

General Fund Budget Units:

Overall, the Health & Human Services Agency is projecting that General Fund expenditures will be approximately $367,000 (0.5%) lower than the Adjusted Budget level, revenue will be approximately $152,000 (0.2%) and Net County Cost will decrease by approximately $215,000 (2%).

As the Board is aware, since FY2008-09, the Health & Human Services Agency has been revising its operating plan to address various adverse fiscal developments beyond the control of the County while staying within its Board-approved fixed Net County Cost. All-told, by the end of this fiscal year the Agency will have implemented 10 rounds of budget reductions or revenue increases, totaling $6.5 million, including $2.6 million in FY2010-11. The Agency is also looking at approximately $2.7 million in additional reductions that may be necessary in FY2011-12.

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

Public Health (40000): Expenditures are projected to be approximately $216,000 (2%) higher than the Adjusted Budget level, revenues are projected to be approximately $250,000 (2%) higher and Net County Cost is projected to decrease by approximately $33,000 (13%). The primary reasons for the projected increase in expenditures and revenues is projected increases in Women, Infants and Children and AIDS program funding, along with an increase in the State allocation for Diagnostic Treatment and Therapy. In addition, costs associated with the current ambulance franchise arrangement are projected to be approximately $50,000 higher than budgeted, because the Adjusted Budget assumed a new franchise agreement would be in place before now.

Social Services (50100): Expenditures are projected to be approximately $861,000 (3%) higher than the Adjusted Budget level, revenues are projected to be approximately $311,000 (1%) higher and Net County Cost is projected to increase by approximately $550,000 (79%). The primary reason for the projected increase in expenditures is an increase in foster care group home rates. This rate change, which increases costs by $1,161,000, was the result of a recent court decision. This increase in costs is partially offset by reductions in other Division costs, including a $200,000 reduction due to the fact that Workforce Investment Act (WIA) ARRA funding and associated expenditures were moved to a separate ARRA fund during the fiscal year. The primary reason for the projected increase in revenue is the receipt of the State and Federal shares of the foster care rate increase (approximately $671,000), partially offset by reductions in other revenue sources, including the $200,000 in WIA – ARRA funds now budgeted in a separate ARRA Fund.

IHSS Public Authority Administration (50800): Expenditures are projected to be approximately $570 (0.2%) higher than the Adjusted Budget level, revenues are projected to be approximately $63,000 (34%) lower and Net County Cost is projected to increase by approximately $64,000 (42%). The primary reason for the projected decrease in revenue is that two staff members are spending more time on activities related to the Social Services budget unit (Budget Unit 50100). The reimbursement for those activities will be captured through the County Expense Claim, with revenue flowing to the Social Services budget unit.

Non-General Fund Budget Units:

Workforce Investment Act – ARRA (50110)/Workforce Investment Act- ARRA Fund (1005): Expenditures and revenues are projected to be approximately $188,000 (26%) higher than the Adjusted Budget level. This budget unit does not receive a General Fund Contribution. The projected increase in revenue and expenditures is due to the receipt of an additional allocation of ARRA funding.

State Budget Issues

On January 10th, the Governor released his proposed FY2011-12 State Budget, outlining a plan to eliminate an 18-month $25.4 billion deficit ($8.2 billion in FY2010-11 and $17.2 billion in FY2011-12). The Governor's plan called for $12.5 billion in expenditure reductions or shifts, $14 billion in "new" revenue (predominantly extending existing, temporary, taxes that are set to expire at the end of this fiscal year) and $1.9 billion in borrowing or transfers from special revenue funds. A key component of the Governor's proposal to extend the temporary taxes for five years is a proposal to realign certain programs from the State to the counties, with funding to come initially from $5.9 billion a year in revenue from some of the extended taxes. The Governor specifically called on the Legislature to adopt his proposed budget reductions by March and call for a special election to be held in June for voters to decide whether to extend the temporary taxes that expire at the end of this fiscal year. If the proposed tax extension is not approved, the Governor indicated he would propose additional expenditure reductions to balance the budget, but did not identify specifically where those cuts would be made.

Key expenditure reductions or shifts proposed by the Governor include:

- Eliminate Redevelopment Agencies and shift a portion of redevelopment funds to Medi-Cal and the trial courts, with any residual amount allocated to the overlapping taxing agencies, including counties;
- Reduce benefits and provider payments and charge co-payments in Medi-Cal;
- Impose time limits, grant reductions and service cuts for CalWORKS;
- Reduce funding for the University of California and California State University;
- Use Proposition 10 (First Five) reserves and some revenues to fund certain children's programs;
- Fund transportation debt costs using weight fees;
- Use Proposition 63 (Mental Health Services Act) funds to support community mental health services;
- Reduce developmental center and regional center spending;
- Shift some adult and all juvenile offenders to counties;
- Reduce IHSS hours of service, limit domestic services and tighten eligibility;
- Reduce State employee salary and medical costs;
- Reduce SSI and SSP grants for individuals to federal minimum.

Aside from the realignment proposal, the areas of particular concern to counties in the Governor's proposed budget include:

- The funding (and service level) reductions in a variety of Health and Human Services programs, including Medi-Cal, CalWORKS, Health Families, IHSS, Child Welfare Services, Veterans Services, Supplemental Security Income (SSI) and State Supplementary Payment (SSP) programs and Public Health. For the most part this will not impact County operations directly, but will have a significant impact on the clients we serve. One area of general concern, however, is that reductions in State safety net programs could require the counties to assume responsibility for people under our Section 17000 obligation.

- The continued suspension of most State mandates not related to law enforcement or property taxes. The Governor did propose to fund the AB 3632 mandate (mental health services for special education students) with Proposition 63 funds. The Governor's proposed Budget also continues the deferral of mandate funding obligations for pre-2004-05 mandates.

- The continued elimination of Williamson Act subventions.

- The proposal to decrease State support for local libraries, which could cost the Napa County Library approximately $300,000 a year in revenue.

- The proposed restructuring of CalFire's services in State Responsibility Areas.

- The proposal that the Legislature reenact the "Gas Tax Swap" with a two-thirds vote. Without this action, the Legislature's previous action approving the Gas Tax Swap would have been invalidated by Propositions 22 and 26.

As indicated above, the Governor's Budget proposed to realign a number of State programs to counties, with funding for the first five years to come from his proposed extension of the 0.5% Vehicle License Fee (VLF) and 1% sales tax that are currently scheduled to expire at the end of this fiscal year. The Governor proposed that this Realignment take place in two phases, as follows:

Phase I, which would be enacted starting in FY2011-12, would include:

- Court Security
- Non-serious, non-violent, non-sex offenders from State prisons
- Adult Parole
- All Juvenile Justice Programs
- Three Mental Health programs: EPSDT, Mental Health Managed Care, and mental health services for special education students (AB 3632)
- Substance Use Disorder Treatment services
- Foster Care and Child Welfare Services
- Adult Protective Services

Phase II would focus on implementation of national healthcare reform and assumes most individuals served by county indigent programs will become eligible for Medi-Cal in 2014, shifting costs from counties to the State. The Governor wants to re-look at the 1991 Realignment related to indigent healthcare. Phase II assumes the State will become responsible for costs associated with health care, including California Children's Services and IHSS, while counties will assume responsibility for CalWORKS, food stamp administration, child support and child care.

Since the Governor unveiled his Proposed Budget, there has been considerable activity in Sacramento. Various legislative committees have met to review the Governor's proposals and CSAC and other advocacy organizations have been working with the Governor's Office. At this point, things stand essentially as follows:

- The Legislature has not yet approved any of the Governor's proposals, but, on March 3, the Assembly-Senate Budget Conference Committee approved a somewhat modified version of the Governor's proposed Budget, and the Governor has asked that the Legislature take action by March 10th.

- The Governor's Office has released language for a proposed State Constitutional amendment that, among other things, would extend the temporary taxes for another five years and purports to protect Realignment funding for counties. The current plan is for the proposed constitutional amendment to extend the temporary taxes and set in place the framework for realignment, but that the details of which programs would be realigned, how funds would be allocated, etc. would be worked out in implementing legislation approved by the Legislature by December 31, 2011.

- It is not clear that there are sufficient votes to put the constitutional amendment on a June special election ballot (a two-thirds vote is required), but negotiations are on-going. Again, the Governor has asked that action be taken by March 10th.

- As negotiations and discussions have progressed, the Governor has modified his original Realignment proposals in a number of ways, including:

    - The Fire realignment proposal has been scaled back significantly and now focuses on 6 counties (not including Napa);

    - The transfer of responsibility for low-level prisoners to counties has been revised to exclude a number of crimes currently classified as non-serious, non-violent and non-sex offense. In addition, the Realignment proposal would now allow counties to contract with the State for the cost of housing such offenders in State facilities.

    - The proposal to transfer responsibility for all parolees to counties has been revised to provide that counties will only be responsible for parolees who are convicted of a non-serious, not-violent, non-sex offense.

    - The proposal to transfer all juvenile justice responsibilities to counties has been revised to allow counties to contract with the State for the custody/supervision of all of a county's wards.

    - Various funding sources for Realignment have been changed or some new programs have been included under the Realignment proposal, such as domestic violence assistance, rape victim counseling, child abductions and recovery.

Staff has been analyzing the Governor's Realignment proposals to determine their potential impact on Napa County. This has proven difficult, in part because the proposals keep changing and, in part, because it appears that final decisions will not be made about exactly which programs will be realigned and how funding will be allocated until after the Legislature approves the various ballot measures for the June special election and implementing legislation is approved by the Legislature. There are a number of concerns that staff has with these proposals, however, including:

- Will sufficient funding be provided to the counties to cover the cost of these programs and what happens if that funding is not sufficient? What happens in five years when the proposed tax extensions would expire? A number of analysts have concluded that the total revenue generated by the proposed tax extensions does not cover the current cost of the programs proposed for Realignment.

- Will counties be given sufficient flexibility to operate these programs in the most efficient way possible? In particular, there are a number of Federal entitlement programs that are proposed to be realigned and counties will have almost no control over how those programs are provided and the costs of those programs.
- Will there be sufficient funding to cover cost increases in the realigned programs?
- How will we address the capital needs associated with some of these programs – particularly the transfer of responsibility for certain offenders, currently in State Prison to the counties? Our preliminary analysis, for example shows that we could need up to 100 additional jail beds to accommodate State prison inmates that would become the responsibility of the County if the Governor's Realignment proposal is approved.
- How much time will we have to implement any realigned programs?