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SUBMITTAL TO THE BOARD OF SUPERVISORS COUNTY OF RIVERSIDE, STATE OF CALIFORNIA

SUBMITTAL DATE:
August 13, 2003

FROM: Executive Office

SUBJECT: Budget Strategy for FY 2003/04

RECOMMENDED MOTION: That the Board of Supervisors consider the alternatives suggested in the attached report, and implement the recommendations on Attachment A.

BACKGROUND: On August 2, Governor Davis signed the FY 2003/04 California State Budget, giving counties a clearer picture of the coming year's financial realities. While many of the State budget's provisions had been anticipated, and can be dealt with by using reserve funds, this approach will leave reserve balances uncomfortably low. Rebuilding the General Fund reserve will allow the County to enter FY 2004/05 better prepared to address the next difficult budget. The following report describes the current situation and recommends a continued cautious approach in the coming year.

Kathryn Field, Principal Management Analyst

FINANCIAL DATA	Current F.Y. Total Cost:	\$ 23,400,000	In Current Year Budget:	No
	Current F.Y. Net County Cost:	\$ 23,400,000	Budget Adjustment:	Yes
	Annual Net County Cost:	\$ 0	For Fiscal Year:	03/04

SOURCE OF FUNDS: General Fund	Positions To Be Deleted Per A-30	<input type="checkbox"/>
	Requires 4/5 Vote	<input checked="" type="checkbox"/>

C.E.O. RECOMMENDATION: APPROVE

County Executive Office Signature

FISCAL PROCEDURES APPROVED
ROBERT E. BYRD, Auditor-Controller
8/13/03
Deputy
Departmental Concurrence BY *[Signature]*

Dep't Recomm.: Consent Policy
Per Exec. Ofc.: Consent Policy

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OFFICE OF THE BOARD OF SUPERVISORS
COUNTY OF RIVERSIDE, CALIFORNIA

Prev. Agn. Ref.: | District: all | Agenda Number:

3.81

BUDGET STRATEGY FOR FISCAL YEAR 2003/04



**County of Riverside
Executive Office**

August 13, 2003

Introduction

After months of anticipation, the California legislature and governor enacted a financial plan for the current fiscal year. Local governments, including Riverside County, are now faced with adjusting their budgets to conform to revised revenue estimates. While some seem grateful that the State budget wasn't any worse, most believe that it will be -- in FY 2004/05. Some signs indicate that the \$36 million impact to Riverside's General Fund, and overall impact of \$43 million this year could be a trend, not an anomaly. Preparing for that possibility is the focus of this report.

As reported on July 29, the State's failure to backfill the gap in Vehicle License Fee (VLF) revenue for 90 days this summer may cost Riverside County as much as \$19.9 million of discretionary funding. While the State has promised to repay this by FY 2006/07, collecting on that pledge may be difficult, and the three lag years will be tight. Adding to our financial challenges are the \$1.4 million of reduced allocations for mental health and child support services, the \$0.8 million reduction in grants for law enforcement programs, and the \$2.5 million shift in federal penalties related to child support automation. An \$800,000 reduction in Juvenile Justice Crime Prevention Act funding that will take place next spring will not affect this year's program but will certainly have a FY 2004/05 effect. While the future of these reductions is unknown, there is little reason to think they will be one-time State actions. For example, the State's "delay" in reimbursing counties annually for \$10 million of SB90 mandates is in its second year, with no end in sight.

In addition to affecting General Fund programs, the State budget has implications for a variety of other County functions. The Public Library Foundation cuts equate to a loss of nearly \$400,000 to the County Library system (however, the Transaction Based Reimbursement reduction, that would have cost Riverside \$90,000, was not included in the adopted budget). Partial suspension of Proposition 42 results in a \$5 million loss to this County's road maintenance resources. A property tax transfer from community redevelopment agencies to ERAF will cost the Economic Development Agency \$1.2 million, and it is rumored that flood control grant programs may be threatened. The known reductions are summarized in the chart following:

Local Effects of FY 2003/04 State Budget

General Fund	in millions
Vehicle License Fee "loan"	\$ (19.9)
Continued deferral of mandated cost reimbursements	(10.0)
Child Support Services federal automation penalty	(2.5)
Transfer of undesignated court fines	(1.0)
Child support allocation reduction	(1.0)
Cuts in law enforcement & prosecution grants	(0.8)
Mental Health managed care reduction	(0.4)
Increase in California Youth Authority fees	(0.3)
	(36.0)
Other Funds	
Transfer of local redevelopment taxes to Education	(1.3)
Reduction in funding for local street rehabilitation & maintenance	(5.0)
Reduction in State's Public Library Fund	(0.4)
	(6.7)
Total costs and lost revenue to Riverside County	
	\$ (42.7)

Though not directly related to the State budget, there will be a number of new expenses not included in the County budget but likely to have a significant impact this fiscal year. The special election to recall the governor, estimated to cost Riverside \$1 million, and an increase in IHSS caseloads, estimated to cost \$4 million, are two that have been quantified recently. Anticipated in the federal budget is a \$2 million reduction in local reimbursement revenue for incarcerating illegal aliens; this would affect Sheriff Corrections. Also, in recent years, the County's hospital, health and public social services departments have surfaced costly service issues with significant budget impacts. All of these, and potentially more, have the potential to decrease reserve funds further.

Budget adjustments recommended today will reduce the Reserve for Economic Uncertainty by \$23.4 million, although it may be necessary to reduce it further as the year progresses. The County's General Fund Contingency is budgeted at \$13.1 million, which is equivalent to only 3% of discretionary revenue. The Reserve for Economic Uncertainty, created in October of 2001 and totaling \$56 million at its peak, was at \$39 million in the final budget, and will now drop to about \$15 million. If the IHSS need is as great as estimated, the amount available could be \$11-12 million by the end of the first quarter. This reserve would be nearly depleted if it were necessary to make up for all of the increased costs and losses of revenue mentioned above. Fortunately, some of these changes were anticipated and included in the County budget. For example, the Department of Mental Health anticipated a reduction in funding and believes it can continue to operate within budget. In addition, the Probation Department expects to be able to absorb the increased fees charged by California Youth Authority this year.

Immediate Strategy

There are new expenses that are beyond the ability of departments to absorb. Part of the penalties assessed to California by the federal government, for not implementing a statewide child support automation system, will now be passed on to counties. This \$2.5 million cost cannot be reimbursed by our local Child Support Services Department's (DCSS) normal revenue sources, and is an appropriate charge to the Reserve for Economic Uncertainty. And while DCSS is taking positive steps to stay within the reduced allocation from the State this year, it may be necessary for the General Fund to contribute as much as \$1 million in order to avoid laying off staff. As stated in the Proposed Budget, the precise amount will be determined later this year and reported in a quarterly budget report.

The lost VLF revenue will not be recovered for three years, if then. It is therefore recommended that the VLF revenue estimate be reduced by \$19.9 million now. To balance this loss, the reserve should be lowered by the same amount.

The State has also taken action on undesignated Court fees. In each of the next two fiscal years (at least), approximately \$1 million of fees will be sent from the Court to the State instead of to the County General Fund. These fees were being used toward the County's Trial Court Funding maintenance of effort.

Several law enforcement grant programs are being reduced or eliminated by the State. Five of these affect the District Attorney (COPS, and vertical prosecution of elder abuse, statutory rape, major narcotic vendors and career criminals) and have a total annual impact of \$467,942. Consistent with Board Policy A-30, Coordination of Grants, we must recommend that some of the positions initially funded by these grants be eliminated. While the budget reductions can be made now, the District Attorney will return at the end of the first quarter with a list of positions to delete.

Grant program reductions totaling \$270,173, and equivalent to about 4 positions, affect the Sheriff's Department. The CATCH team funding has been eliminated, and COPS funds have been reduced. While the budget reductions can be made now, the Sheriff will return at the end of the first quarter with specific positions to eliminate.

The specific budget adjustments recommended for the above actions are listed in Attachment A. Other than adding appropriations for child support penalties, **the Board is asked to preserve remaining reserve funds by temporarily refraining from additional appropriations.** By October, the prior fiscal year's books should be closed and the amount of year-end reversions should be known. Given that this is the first year of operating the new financial system, it is difficult to make a projection with confidence now. Notification will be given as soon as a reliable number is available, possibly as soon as one month from now.

As well as enacting certain budget adjustments now, some policy changes are recommended. For example, the purchase of new vehicles represents a major expense to the General Fund each year. While many of these are used for front-line law

enforcement and fire protection, many others are not. The Purchasing Department has suggested a number of ways to reduce vehicle expenses, including keeping some patrol cars beyond 85,000 miles for use in less demanding situations, and keeping non-emergency vehicles beyond the normal replacement point of 100,000 miles. By implementing these strategies now, about \$1.1 million can be saved this fiscal year.

Growth in health and human services caseloads continues. While much of this was included in the local budget, we have seen that the actual growth rate is not simple to predict. Significant increases at the end of last fiscal year changed reserves and long-range expense projections. The Departments of Public Social Services, the Community Health Agency, and the Riverside County Regional Medical Center are, therefore, expected to report quarterly on caseload changes or other significant fiscal issues and on their ability to mitigate them within their budgets.

Outlook for the Future

The chart below summarizes what is, and is not, known about the State's plans for the next few fiscal years. While "only" \$12.1 million of continued reductions can be confidently projected at this time, it seems likely that others will be enacted to offset the \$7.9 billion shortfall that the State projects for the end of this fiscal year. It is reasonable to expect the State to adopt a budget next year that has another \$36 million annual impact to Riverside's General Fund.

Impact of California Budget on County General Fund					
<u>Action</u>	<u>Impact (in million\$)</u>				<u>Comments</u>
	FY 03/04	FY 04/05	FY 05/06	FY 06/07	
"Triple Flip" Revenue Swap:					
Sales Tax Transfer		(10.4)	(10.8)	(11.2)	Continues through FY 08/09
Property Tax Transfer		10.4	10.8	11.2	Continues through FY 08/09
VLF Backfill suspension	(19.9)			19.9	Approx. 90 days of payments
Continued loss of SB 90 reimbursements	(10.0)	(10.0)	(10.0)	(10.0)	
Increase in Cal.Youth Authority fees	(0.3)	(0.3)	(0.3)	(0.3)	Affects Probation
Decrease in Juvenile Justice Program		(0.8)	?	?	? Affects primarily Probation
Decrease in COPS funds	(0.3)	?	?	?	? Affects Sheriff & DA
Elimination of Hi-tech Law Enf. Grants	(0.1)	?	?	?	? Affects Sheriff
Reductions in OCJP prosecution programs	(0.4)	?	?	?	? Affects District Attorney
Transfer of undesignated court revenue	(1.0)	(1.0)	?	?	
Reduction in Mental Health managed care	(0.4)	?	?	?	
Child Support allocation reduction	(1.0)	?	?	?	
Transfer of federal child support penalties	(2.5)	?	?	?	
Additional program reductions	?	?	?	?	
TOTAL	(\$36.0)	(\$12.1)	(\$10.4)	\$9.5	

Riverside County has typically taken a conservative approach to financial planning. Revenue growth for this year was estimated at 5%, but that projection may prove optimistic. Uncertainty at the State level and in the world seem unlikely to breed prosperity in the near term. While there may be some one-time accounting and borrowing strategies available to us still, an over-reliance on these is not advised; they can mask fiscal realities, create structural imbalance and delay needed action. **Our best course of action is to continue to contain costs and build reserve funds.**

Options

Costs continue to rise. Employer contributions to PERS are likely to increase for FY 2004/05, at the same time that safety employee cost-of-living increases drive retirement costs up further. Insurance premiums and self-insurance costs may also rise. Without additional resources available, this County may have to ask departments to absorb salary and benefit increases once again, and may have to keep risk management rates below actuarial recommendations.

Other strategies available to improve the financial picture include the continued deferral of building maintenance funds and Healthy Kids program funds. Although not recommended at this time, together these could save \$6 million next year. Holding the rates charged by internal service functions at current levels might not have an easily-quantifiable impact, but would help departments cope with rising costs and shrinking revenues elsewhere.

One noteworthy financing tactic is still available to us. Since they first began arriving, Tobacco Settlement proceeds have not been appropriated until the year after receipt. However, it would be acceptable to appropriate this year's anticipated proceeds of \$16 million in this current year, as well as last year proceeds, which have already been budgeted for FY 2003/04. This would make an additional \$16 million available, but should only be applied if and when there is a clear need for this one-time accounting strategy.

<u>Year Rec'd</u>	<u>Year Spent</u>	<u>Available Amount</u>
FY 99/00	FY 00/01	0
FY 00/01	FY 01/02	18
FY 01/02	FY 02/03	14
FY 02/03	FY 03/04	21
FY 03/04	FY 03/04	36
FY 04/05	FY 04/05	16

Budget strategy changes

As reported in June, a structural gap has been created by the State's policy to delay (of two years, at minimum) reimbursing certain social service program costs. Overall, ongoing revenues to the County are growing more slowly than ongoing expenses, and with the State in an unhealthy financial position, this could continue for longer than initially anticipated. Unfortunately, the only proactive way to address this imbalance is by curbing local spending.

It is time, therefore, to consider reductions in the spending of General Fund departments. While this could be accomplished in a number of ways, the fairest might be to apply a defined percent reduction to the NCC of each General Fund department. This would allow managers to approach the reductions in a manner most appropriate (hiring freeze, program change or restructuring, for example) for their unique situations. Knowing that public safety is a high priority of this Board, it is suggested that reductions to the Sheriff, District Attorney, Public Defender and Fire Departments be less than those to other functions. A 1.5% cut to public safety, coupled with a 4% cut to other General Fund departments, would save about \$10 million a year. While immediate implementation of this is not recommended, we may soon find this strategy necessary.

The following chart lists a variety of budget reduction and balancing strategies. These are not the only ones available but they are the ones most often suggested.

STRATEGIES FOR REBUILDING GENERAL FUND RESERVE FUND				
(Savings estimates subject to refinement)				
	Option	Pros	Cons	Potential GF Savings
Recommended now:				
1	Freeze non-safety vehicle purchases (and keep older vehicles longer)	Quick & easy to implement or suspend	May increase maintenance costs of existing vehicles	1,100,000
2	Increase review of equipment purchases	Quick & easy to implement or suspend	May increase maintenance costs of existing equipment	300,000
For consideration in the future:				
3	Reduce non-safety budgets 4%	Involves most GF departments in solution	Public service may suffer	7,445,000
4	Reduce public safety budgets 1.5%	Involves all GF departments in solution	Public safety or service may suffer	2,880,000
5	Budget tobacco fees in advance	No impact on operations or service	One-time strategy; difficult to make precise estimate	16,000,000
6	Freeze non-safety hiring for next 10 months	Little impact on current employees	Public service may suffer	5,500,000
7	Discontinue use of temporary staff	Affects unrepresented employees	Decreases department flexibility	600,000
8	Mandate 160 hours/yr (7.7%) furloughs	Retains all current staff	Meet & confer item; Affects annual incomes of all GF employees; May cause disparity in depts. with GF & non-GF staff; Public service may suffer	10,500,000

Applying some of these strategies this year and/or next year produces the following scenarios:

General Fund Position, With Options for Balancing

	PROJECTED ACTUAL (in millions)			
	FY2003/2004		FY2004/2005	
	Current	Option	Current	Option
<u>RESOURCES:</u>				
Ongoing Revenue (5% growth)	411	411	423	423
Fund Balance & 1-Time Revenue	39	39	13	13
State Cuts	(24)	(24)	(24)	(24)
State Realignment Payment (2 yr prior)	n/a	n/a	20	20
Use of Reserves	37	25	10	24
	462	450	442	456
<u>APPROPRIATIONS:</u>				
Misc. Ongoing NCC	420	420	431	431
Misc. One-Time Appropriations	20	20	20	20
Across the board reductions	n/a	(10)	n/a	(10)
Other Departmental Savings	n/a	(2)	n/a	(2)
Reserves for Uncertainty and SB90	10	10	10	10
Contingency	13	13	10	10
Self Insurance (NCC portion)	0	0	10	0
PERS Misc. Costs Reserve	0	0	18	0
	462	450	498	458
Available for Budget Needs	0	0	(56)	(2)
<u>NOTATIONS:</u>				
Reserve for Economic Uncertainties	12	24	2	0
Reserve for SB90	10	10	0	0
Due From the State (approximate)	104	104	114	114

ASSUMPTIONS:

- 1) In 2004, state shorts us \$24M and in 2005, state shorts us \$24M.
- 2) In 2005, state is caught up on realignment payments (\$20M)
- 3) Reserves in "Notations" are year end amounts

As shown above, the shortages facing us currently, the anticipated IHSS costs, and the recommendations presented today will leave roughly \$12 million in the Reserve for Economic Uncertainties and \$13 million in Contingency. **Doing nothing further to prepare for next year, and assuming that State actions have another \$24 million impact, will create a FY 2004/05 deficit greater than the sum of the remaining reserves and contingency fund.**

In order to prevent this, a number of options are illustrated above. These include directing most departments to continue absorbing PERS rate increases, funding self-insurance funds at the FY 2002/03 rates, and making \$10 million of cuts to departments each year. These are painful proposals that need to be weighed against the possibility of operating with insufficient reserves.

Conclusion

Local governments have been placed in the difficult position of knowing that State funding is inadequate but not knowing from year to year what direct impact that may have. Affecting Riverside this year are delays in reimbursements, a loan that may not be repaid, increases in fees, re-appropriation of traditional revenues and suspensions of grant programs. Next year's funding deficiencies may take on another form, however. Making long-range plans or implementing new programs is scarcely possible under these conditions.

In preparation for this day, the Board long ago adopted sound policies for financial management. These have been successful in weathering past shortfalls and should be continued. In addition, as has been demonstrated in the recent past, the best way to prepare for uncertainty is to create a cushion to ease future blows from any direction. Implementing the recommendations on the next page will take the next step toward containing costs and rebuilding reserves.

Attachment A
RECOMMENDED MOTIONS

That the Board of Supervisors:

- 1 Direct the Purchasing Director to freeze the purchase of vehicles by and for General Fund departments, except those vehicles to be used for front-line public safety;
- 2 Require CEO review and approval of all fixed asset purchases by General Fund departments;
- 3 Direct DPSS, CHA & RCRMC to report quarterly on any unanticipated needs, and how they will be addressed within department budgets;
- 4 Direct the Auditor-Controller to adjust the FY 2003/04 budget as follows:

Decrease estimated revenue	
10000-1300100000-750200 CA-Motor Vehicle In-Lieu Tax	\$19,900,000
10000-1100900000-731160 Administrative Costs (Courts)	1,000,000
10000-2200100000-755660 CA-Career Criminal Program (DA)	122,500
10000-2200100000-755620 CA-Statutory Rape Vertical Prosecution (DA)	122,500
10000-2200100000-755600 CA-Elder Abuse Vertical Prosecution (DA)	90,000
10000-2200100000-755500 CA-Major Narcotic Vendors (DA)	82,500
10000-2200100000-755520 CA-Citizens Option for Public Safety (DA)	50,442
10000-2500300000-755180 CA-From Other State Govt Agencies (Patrol)	140,464
10000-2500300000-755520 CA-Citizens Option for Public Safety (Patrol)	79,266
10000-2500400000-755520 CA-Citizens Option for Public Safety (Corr.)	50,442
Decrease appropriations	
10000-2200100000-510040 Regular Salaries (DA)	316,048
10000-2200100000-518100 Budgeted Benefits (DA)	151,894
10000-2500300000-510040 Regular Salaries (Patrol)	142,803
10000-2500300000-518100 Budgeted Benefits (Patrol)	76,927
10000-2500400000-510040 Regular Salaries (Corrections)	32,873
10000-2500400000-518100 Budgeted Benefits (Corrections)	17,569
Increase appropriations	
10000-1101000000-536200 Contribution to Other Non-Co Agency	2,500,000
Decrease Reserve for Economic Uncertainty	\$23,400,000