BOARD OF SUPERVISORS
AGENDA LETTER

Clerk of the Board of Supervisors
105 E. Anapamu Street, Suite 407
Santa Barbara, CA 93101
(805) 568-2240

Agenda Number:

Department Name:	County Executive Office
Department No.:	012
For Agenda Of:	November 17, 2020
Placement:	Departmental
Estimated Time:	1 hour
Continued Item:	No
If Yes, date from:	
Vote Required:	Majority

TO:	Board of Supervisors	
FROM:	Department Director(s)	Mona Miyasato, County Executive Officer
	Contact Info:	Jeff Frapwell, Budget Director
SUBJECT:	**FY 2021-26 Five-Year Forecast**	

Digitally signed by Mona Miyasato
Date: 2020.11.10 10:37:18 -08'00'

County Counsel Concurrence
As to form: N/A

Auditor-Controller Concurrence
As to form: N/A

Other Concurrence: N/A

Recommended Actions:

That the Board of Supervisors:

a) Receive and file the FY 2021-26 Five-Year Forecast and Fiscal Issues Report; and

b) Determine pursuant to CEQA Guidelines §15378 that the above activity is not a project under the California Environmental Quality Act.

Summary

This five-year forecast report is presented to the Board of Supervisors to provide a context for balancing short-term objectives with long-term goals during the upcoming budget development cycle. This forecast report includes five years of revenue and expenditure projections for major County operating funds, and examines the drivers of any major anticipated gaps, including the impacts of COVID-19 on the County's budget. This report also identifies fiscal issues that have the potential to impact demands on County resources during the forecast period. Some are broad issues with countywide impact and others are smaller, specific issues within departments.

The FY 2020-21 budget was adopted with discretionary revenue growth and use of one-time funds sufficient to avoid potential cuts—despite COVID-related revenue losses—and departments have continued to implement restructuring initiatives to enhance services or increase efficiencies. Because of the uncertainties surrounding the pandemic response and economic impacts, the budget did not expand services, but rather focused on maintaining existing services. Contingency reduction plans for mid-year

were prepared by each department if greater-than expected revenue losses materialized. Given the current situation and cautious budget actions taken in June, mid-year cuts are not necessary at this time.

Five-Year Forecast. Despite the current recession, brought on by impacts of the pandemic on the economy, FY 2021-22 shows an anticipated modest General Fund budget gap of just under $2 million. However, the years beyond this are expected to show growing funding shortfalls, with the gap growing to over $27 million by the fifth year of the forecast. Because of the degree of uncertainty surrounding a recovery from the COVID-19 induced economic downturn, this report provides ranges of possible growth rates for major discretionary revenue sources to stress test the County's fiscal outlook.

In addition to recession-induced revenue impacts, described in detail below, another contributing factor is rising pension costs. Retirement costs are driven by salary increases, pension investment returns, and expectations regarding existing and future retirees. Costs are anticipated to increase nearly 12% ($17.7 million) in the first year of the forecast, largely due to 1% returns on the pension investment fund as of June 30, 2020, compared to a 7% assumed rate of return. The impact of the shortfall is smoothed in over a five-year period and will continue to affect future years. However, the contribution increases in subsequent years of the forecast average about 5% each year as the impact of the FY 2017-18 reduction in the assumed rate of return, from 7.5% to 7.0%, is fully smoothed in by FY 2021-22. For comparison, retirement costs increased over 25% in FY 2010-11 during the Great Recession, the largest single-year increase of the past 15 years.

General Fund Cumulative Gaps (Baseline Scenario)

Dollars in millions

	2021-22	2022-23	2023-24	2024-25	2025-26
General Fund	-$1.9	-$5.0	-$15.7	-$23.5	-$27.2
Incremental Change		-$3.1	-$10.7	-$7.8	-$3.7

For many years, the primary discretionary General Fund revenue sources have been property, sales, and transient occupancy taxes. With several years of cannabis tax revenue receipts, this additional discretionary revenue source has now joined that list. Because of the uncertainties in the stability of the cannabis market while the program was being established, cannabis revenue has not been used to fund ongoing programs or service level expansions. Instead, it has been used to cover enforcement and regulatory program costs, with any remaining available funds dedicated to one-time uses. Steady growth has occurred in these four taxes over the last several years (with the exception of sales tax and TOT losses following the Thomas Fire and subsequent debris flow and COVID-19), and the forecast presents three scenarios with differing revenue assumptions: the **baseline scenario** assumes a gradual economic recovery and moderate growth in tax revenues from FY 2022-23 onward; the **pronounced recession scenario** assumes lingering disruption to economic activity due to the pandemic and slow recovery as a result; and the **mild recession scenario** assumes that the adverse impacts of the pandemic on the economy improve in 2021 and most tax revenues experience growth beginning in FY 2021-22.

Figure 1.
Projected growth in major discretionary revenues (property, sales, and transient occupancy taxes) based on recession severity.

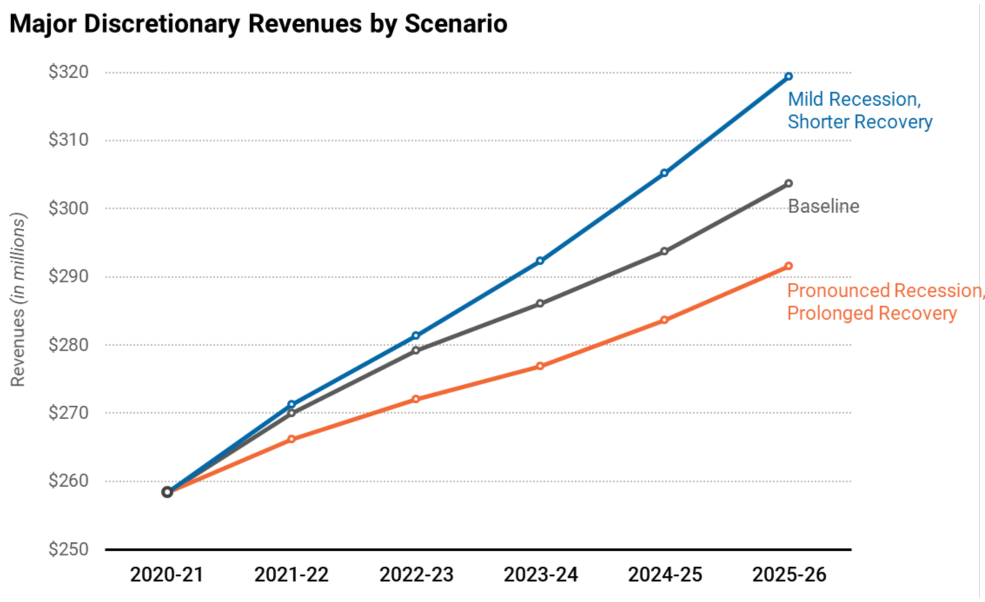


Figure 1a.
Comparison of revenue growth projections in Baseline Scenario and Mild Recession Scenario.

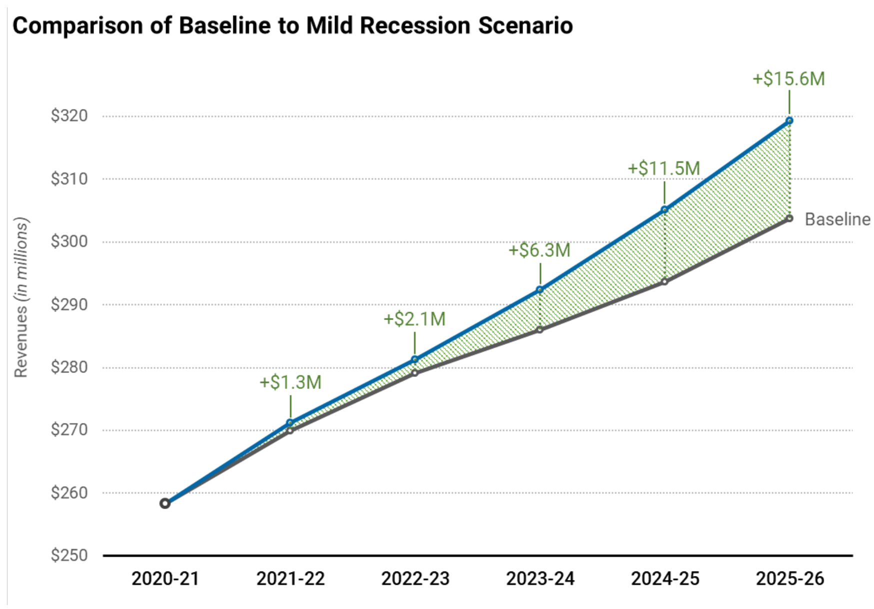
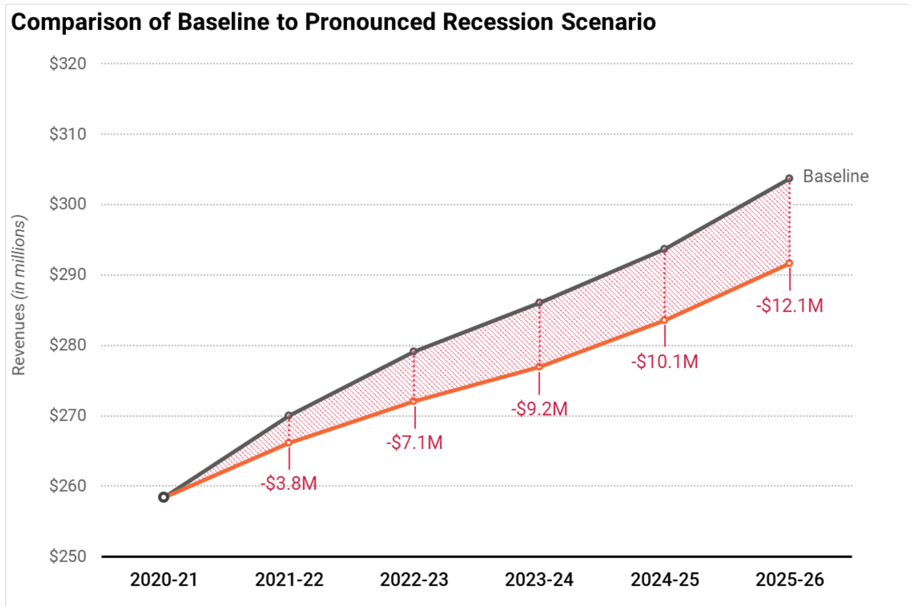


Figure 1b.
Comparison of revenue growth projections in Baseline Scenario and Pronounced Recession Scenario.



These major discretionary revenues are distributed to departments as General Fund Contribution (GFC), with nearly 90% allocated to General Fund departments. GFC finances departmental operations and services for which no special or dedicated revenues are available and, in special revenue departments, often serves as local match for State and federal funding.

The County's baseline forecast projects a $1.9 million deficit in FY 2021-22. If no mitigating actions are taken, the deficit grows to $5.0 million the following year and reaches $27.2 million by FY 2025-26. These projected deficits are cumulative. By law, the Board must adopt a balanced budget and, as such, the projected deficit in a given year would necessarily decrease by the amount of the prior year's deficit closed through reductions in ongoing expenditures or additional revenue.

General Fund expenditures are projected to grow throughout the forecast period primarily due to increases in salaries, retirement contributions, and health insurance costs as well as escalating general liability insurance premiums. This growth in expenditures exceeds the projected growth in General Fund revenues, inclusive of major discretionary revenues, which drives the cumulative gaps in each of the forecast years.

Figure 2.
Total General Fund expenditures and revenues forecasted through FY 2025-26. Revenue scenarios reflect differences in discretionary revenue growth based on recession severity.

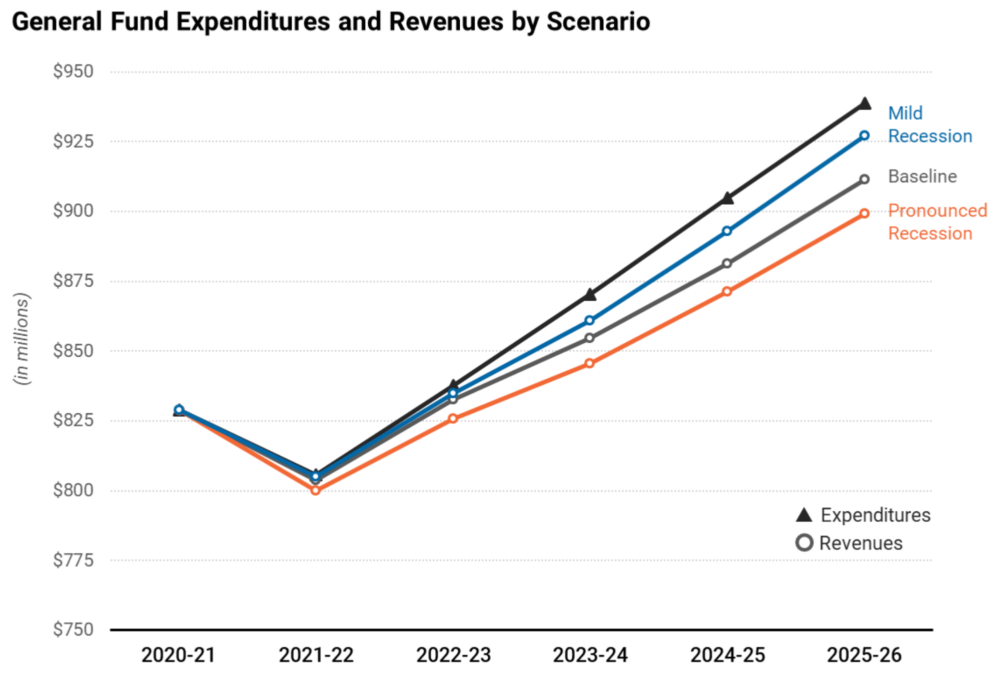


Figure 2a.
Cumulative gap projection with baseline scenario.

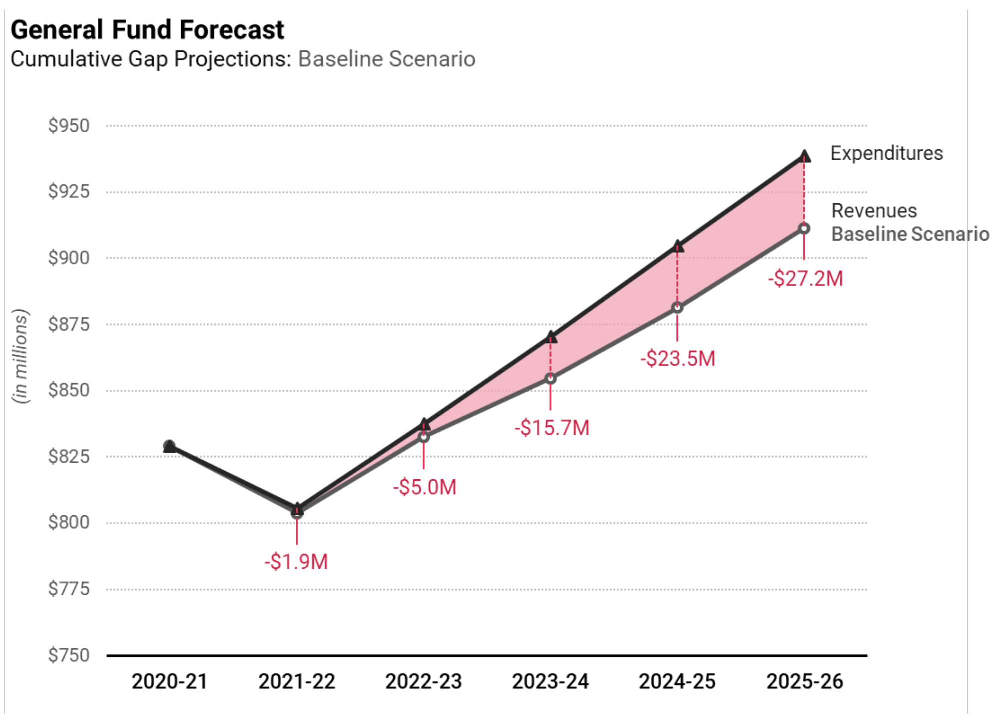


Figure 2b.
Cumulative gap projection with mild recession scenario.

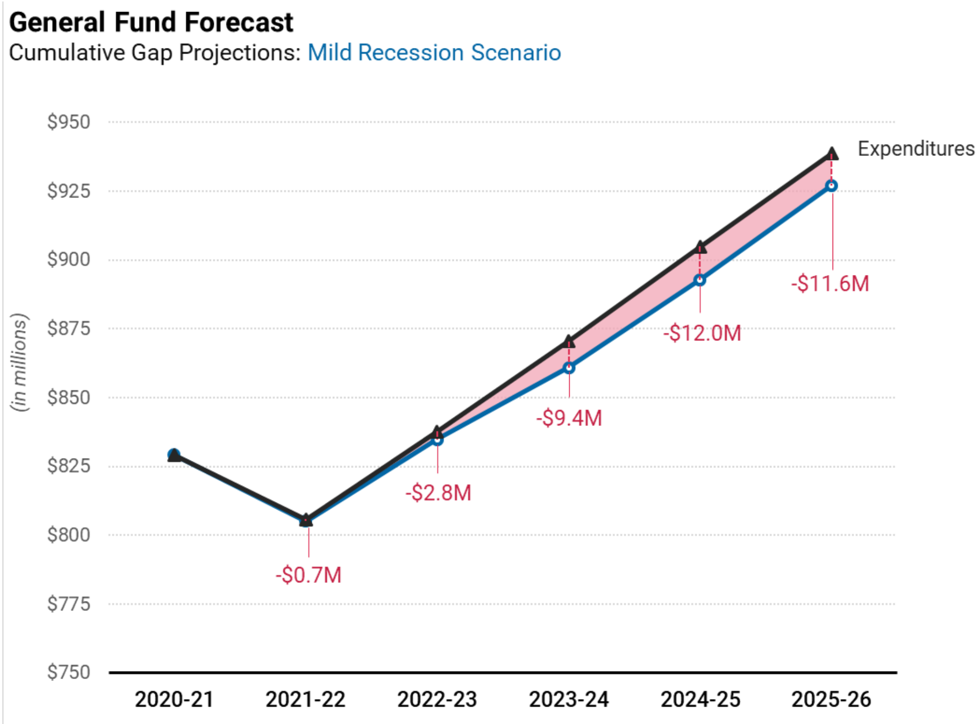
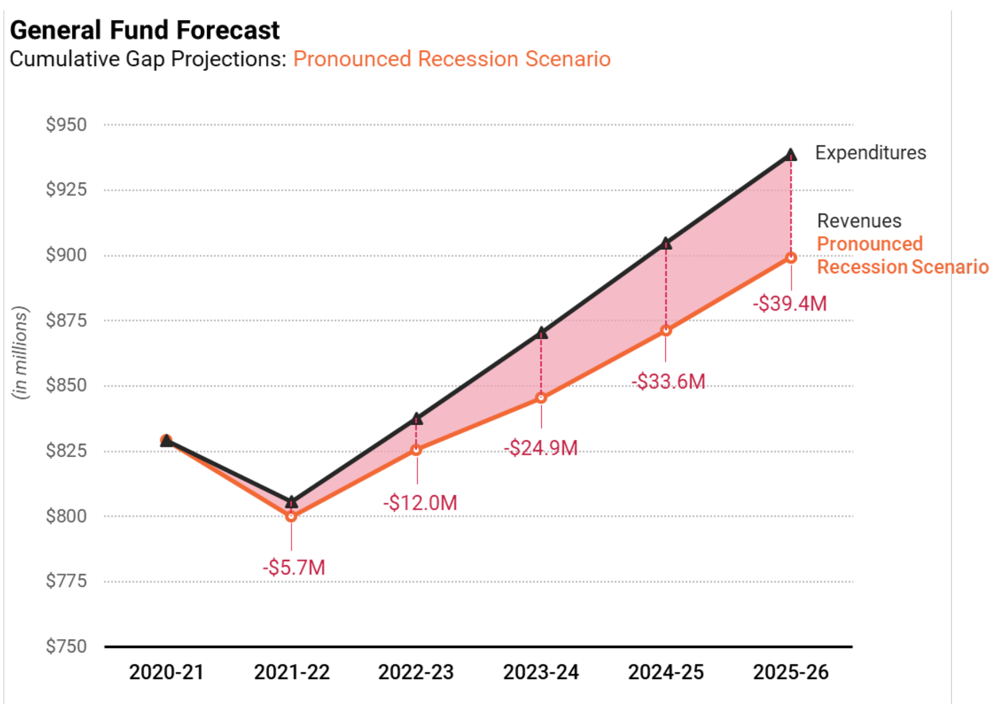


Figure 2c.
Cumulative gap projection with pronounced recession scenario.



In summary, in the General Fund:

- In a "mild recession" scenario, expenditures and revenues would largely balance next year but a funding gap would grow to $11.6 million by 2025-26.
- In the "baseline" scenario, a modest gap is projected for next year, but then would reach a cumulative $27.2 million by 2025-26.
- In the "prolonged recession" scenario, a gap of $5.7 million is projected, which grows to a cumulative $39.4 million by 2025-26.

Given that this pandemic-related recession is unlike recessions of the past, and that pandemic impacts will be further borne out as we approach FY 2021-22 budget development, estimates will be refined, and will continue to be refined until budget adoption to ensure available funds are appropriated prudently and according to Board priorities.

Several of the County's other major operating funds, including the Mental Health Funds, the Health Care Fund, the Social Services Fund, and the Roads Operations Fund, are anticipating gaps spurred largely by lingering COVID-related revenue losses, ongoing gaps between revenues and expenditures, and legislative impacts. These special revenue funds are projecting deficits in anticipation of state and federal revenue levels that will not keep pace with increases in salaries and benefits and reinforce the importance of limiting ongoing expansions in the coming years to ensure that these funds remain self-sufficient. As the recession continues, we could see further declines in federal or state revenue levels during times when our communities may need increased support.

Major Special Revenue Funds Cumulative Gaps

Dollars in millions

	2021-22	2022-23	2023-24	2024-25	2025-26
Roads-Operations (Public Works)	-$2.6	-$3.1	-$3.5	-$4.0	-$4.4
Health Care (Public Health)	-$2.8	-$4.8	-$5.9	-$8.0	-$9.7
Mental Health Services (Behavioral Wellness)	-$4.2	-$4.6	-$4.6	-$4.6	-$4.6
Mental Health Services Act (Behavioral Wellness)	-$2.5	-$10.6	-$9.3	-$8.4	-$8.4
Environmental Health Services (Public Health)	-$0.3	-$0.6	-$0.3	-$0.7	-$0.9
Social Services	-$3.7	-$5.9	-$7.0	-$8.2	-$9.8
SB IHSS Public Authority (Social Services)	-$1.5	-$1.0	-$1.1	-$1.1	-$1.0
Planning and Development	-$0.3	-$0.4	-$0.4	-$0.4	-$0.4

Significant Fiscal Issues. In addition to countywide and department-specific factors driving the budget gaps presented above, departments have identified potential issues that could have significant fiscal impacts over the next five years. These are not all included in the forecast assumptions because of the uncertainty surrounding their occurrence or because they would require Board policy to pursue; however, if some or all of these do occur, they have the potential to present difficult choices about where to direct our limited discretionary resources. Many of these issues were previously identified in last year's fiscal issues report. Information about these issues is provided to serve as context for future decisions about allocation of one-time and ongoing resources, potential establishment of reserves for specific projects, and scope of fiscal demands within the next several years.

Fiscal Issues and FY 2021-22 Potential Impacts	Status
Legislative and Policy Changes: Mandates will increase costs and/or workload	
Elimination of Revenue Sources and Cost Savings: $4.6M annually	
AB 1869 eliminates criminal justice administrative fees	$65M backfill is included in legislation but no distribution formula has been established
Probation: $1.9M ongoing Sheriff: $465K ongoing Public Defender: $50K ongoing	
Federal 340B Drug Discount Program will be eliminated	Legislation slated to become effective on January 1, 2021; backfill expected but details not yet finalized.
Public Health: $2.2M ongoing	
Impacts on Criminal Justice System: $3M-$6M annually	
Discovery process and materials	Sheriff, DA, and Public Defender impacted by lack of data integration and labor-intensity of sharing discovery materials.
District Attorney estimates workload equivalent to $250K annually to address discovery complexity and volume; impact to other departments not quantified.	
Technology	Criminal justice departments report need for digital storage space and system upgrades to meet legislative requirements.
Estimated $1.5M-$3.0M across criminal justice departments	
Lack of State funding for pre-trial assessments	State funding was to have been provided through SB 10, which was overturned with the failure of Prop 25. There is now no ongoing funding source identified.
Probation: $1.4M annually for pretrial assessments	
Deferred Maintence Backlog: Continues to grow and is addressed as funding is available	
Current deferred maintenance backlog is valued at $377M	
Public Works: $311M	Board policy allocates ongoing funding per the 18% maintenance policy and available one-time funds to maintenance projects based on prioritized needs.
Community Services: $53.5M	
General Services: $12.6M	
Investment in Technology: Upgrade countywide systems to meet complex and changing demands	
Cybersecurity	
$1.5M-$2.0M annually Countywide	The cost for tools, services and licenses to achieve the goals and objectives of the cybersecurity plan will need to phased in over the next few fiscal years.
Business Applications Needs Assessment recommended software solution and implementation	
$10M+ one-time plus Countywide annual licensing and maintenance costs	The needs assessment, currently underway, will determine the business application needs of departments to conduct their optimum business operations, and the product will be a recommended set of actions and requirements to seek a new systems solution for accounting, budgeting HR, payroll, and other functions.
Facility Conditions and Workspace Configurations: Aging facilities and the need to adapt workspaces to today's operations	
Many of the County's 300 facilities are aging and in need of repair or upgrades, as well as in need of reconfiguration to meet today's workplace demands.	Because of insufficient replacement funds for deterioriating facilities, repairs and upgrades are prioritized in the annual CIP process. Departments have relied on their own resources in many cases to reconfigure workspaces.
Innovations: Data-driven improvements in service delivery often have accompanying costs	
Holistic defense model (Public Defender)	
Public Defender: to fully implement the holistic defense model, the departmet estimates an annual cost of $650K	Public Defencer currently employs a holistic defense model, though is not able to expand as recommended by KPMG because of resource constraints.
Reform efforts in criminal justice to reduce the jail population and reduce recidivism	
Not yet quantified	These are being reviewed by KPMG as it completes its reports of the other criminal justice
Whole Person Care to address social determinants of health: Potential CalAIM Medi-Cal reform	
No impacts in the first year of the forecast, but possibly significant impacts or benefits to Behaviorial Wellness and Public Health if and when the reform is budgeted at the State level	CalAIM is not yet budgeted at the State level.

Given the uncertainties surrounding the impacts of the pandemic and the recovery from the recession, as well as the continuing need to address long-standing fiscal issues, discipline in our spending must remain a guiding principle.

Next Steps. We continue to face the daunting challenge of responding quickly to the pandemic and acting amid uncertainty. We prepared and positioned ourselves to adopt new practices, be responsive and resilient, and rethink what the public needs and expects of us through our Renew ‘22 initiative. The pandemic has caused an acceleration of Renew ’22, which was initiated in 2017 to fortify the organization against the next economic or natural emergency, which is occurring now.

As part of Renew ‘22, we are refocusing our efforts to build on recent adaptations and leverage our new knowledge and ways of operating while continuing internal process improvement and innovation efforts:

- **Process Improvement and Innovation Training** through the County's InnovateSBC program, which launched in July 2020, has already trained more than 60 employees, with a goal of training 225 by June 2022. This training provides staff at all levels with tools to review processes and practices, and empowers them to implement innovations in the ways we deliver services to our customers, with the ultimate result of streamlining and improving our outcomes.
- **KPMG Departmental Management Reviews** will continue and are expected to be completed within the next two fiscal years to improve departmental operations, management, efficiency and performance.
- **Additional or improved digital and online service,** which was part of the "Big Picture Goals," shared by all departments, will leverage and build upon what has been done during the pandemic to provide greater efficiency and customer service. Countywide, these include a new website platform making it easier to update content and new Microsoft Office tools in 2021.
- **More employee engagement**, in the form of regular feedback surveys to employees from County HR; expansion of e-learning opportunities; supervisorial, management and leadership trainings; and dissemination of our countywide values. These practices help fortify connections among employees, remind them of our purpose in serving the public, and accentuate the positive parts of our County culture. Strengthening the ties that bind us together is important in times of stress and uncertainty for employees, as we continue a hybrid workforce of virtual and on-site employees.

The next stage in budget development will be adoption of budget development policies in December, followed by budget workshops in April, where we will bring forward information about how certain issues have been or will be addressed through the recommended budget, and will provide a framework for Board consideration of options to prepare for and address anticipated fiscal demands in the coming years.

Fiscal and Facilities Impacts:

The five-year fiscal outlook on the county's general fund and other major operating funds are presented in the attached report, along with discussion of significant fiscal issues that may further impact demands on funding in future years.

Attachments:

A – Five-Year Forecast and Fiscal Issues Report

Authored by:

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