BOARD OF SUPERVISORS AGENDA LETTER

Agenda Number:

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

Submitted on: (COB Stamp)

Department Name:	CEO
Department No.:	012
For Agenda Of:	November 28, 2023
Placement:	Administrative
Estimated Time:	N/A
Continued Item:	No
If Yes, date from:	N/A
Vote Required:	Majority

TO:	Board of Supervisors	
FROM:	Department Director(s)	Mona Miyasato, County Executive Officer
	Contact Info:	Paul Clementi, Budget Director Nancy Anderson, Chief Assistant County Executive Officer

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SUBJECT: **Fiscal Year 2023-24 First Quarter Budget Status Report and Cannabis Taxation, Compliance and Enforcement Update**

County Counsel Concurrence
As to form: N/A

Auditor-Controller Concurrence
As to form: N/A

Recommended Actions:

It is recommended that the Board of Supervisors:

a) Receive and file the Fiscal Year (FY) 2023-24 First Quarter Budget and Status Report and Cannabis Taxation, Compliance and Enforcement Update as of September 30, 2023, showing the status of appropriations and financing for departmental budgets adopted by the Board of Supervisors; and

b) Determine that the above actions are not a project under the California Environmental Quality Act (CEQA), because pursuant to sections 15378(b)(4) and 15378(b)(5) the recommended actions consist of organizational, administrative, or fiscal activities of government that will not result in direct or indirect physical changes in the environment.

Summary:

The FY 2023-24 budget status report for the first quarter ending September 30, 2023 provides a fiscal year-to-date look at the County's financial position relative to the FY 2023-24 adjusted budget. As of the end of the first quarter, the General Fund is projecting a positive year-end variance of $2.7 million driven primarily by two departments with reportable positive variances due to salary savings on vacant funded positions, in addition to one department with a reportable positive variance due to higher-than-budgeted administrative revenue. This is significantly less than last year, which ended with a $27 million General

Fund surplus, and more in line with years where a softening of the economy has occurred. Cannabis tax revenue continues to trend lower than budgeted with a projected $1.5 million negative variance, which is discussed in greater detail below.

The fiscal position of the General Fund is monitored and presented to the Board on a quarterly basis, with a final report brought after the close of the fiscal year. At the end of the fiscal year, any funds resulting from a positive variance are carried forward for the Board to consider as part of the next budget development cycle as priorities and fiscal issues are identified. The five-year forecast for the General Fund will be presented to the Board in December, which will set the stage for FY 2024-25 budget development.

Additionally, there were no departments with reportable variances in the Special Revenue and Other Funds for the first quarter. All reportable variances will be discussed in greater detail below.

FIRST QUARTER REPORT

The first quarter for the fiscal year includes activity through September 30, 2023. In this report, projected financial results for the fiscal year end are compared to the annual adjusted budget. The major differences (variances) between budgeted and actual amounts are discussed on the following pages.

This report highlights the variances that exceed the following thresholds:

1) General Fund departments (including Discretionary General Revenues) with projected variances greater than $300 thousand per department; shown in the Financial Summary Report (Attachment A); and
2) Special Revenue and Other Funds with projected variances greater than $500 thousand per fund; shown in the Financial Summary Report (Attachment B).

Both Attachments A and B use actual revenues and expenditures for the first three months of FY 2023-24, and then add departmental projections for the remaining nine months to arrive at the "Projected Actual" columns. These annual Projections are then compared to Adjusted Budgets for both Sources and Uses to produce a "Net Financial Projected Variance" for the end of the fiscal year (shown in the far-right column of the Attachment A and Attachment B reports).

BUDGET POLICY

Departments are responsible for maintaining expenditure levels within the Board-approved budget appropriations in accordance with Board adopted policy and procedure *'Budgetary Control & Responsibility'* as the following abbreviated excerpt states:

A. If expenditures are projected to exceed appropriations, the department head responsible for the budget shall perform one or more of the following steps in the following order:

    1) Lower the expenditure level to maintain overall expenditures within the total amount budgeted,
    2) Request a transfer from fund balance within the same department and fund under the department head's control (if available for appropriation),

3) Prepare a transfer request from General Fund Contingency and an agenda item for the Board of Supervisors with a memo to the County Executive Office, providing adequate justification.

In addition, the County Budget Act, Section 29121, California Government Code, places liability for over-expenditure upon the department director authorizing the expenditure:

> Except as otherwise provided by law, obligations incurred or paid in excess of the amounts authorized in the budget unit appropriations are not a liability of the county or dependent special district, but a personal liability of the official authorizing the obligation.

GENERAL FUND SUMMARY (Attachment A)

As of September 30, 2023, the General Fund had a projected year-end positive variance of $2.7 million. This is the result of favorable results in most General Fund departments, partially offset by minor, non-reportable negative variances in three others.

General Revenues (Department 991) projects a positive year-end variance of $69 thousand (0.02% on an adopted budget of $372.7 million), with significant variances detailed in the table below. This variance is due primarily to higher than budgeted Interest Income and Franchise Fees, as well as a reduction in General Fund Contribution (GFC) sent to a special revenue department. These positive variances are offset by negative variances in Property Tax and Transient Occupancy Tax (TOT). Cannabis Cultivation and Retail Storefront Taxes are projected to come in lower than budgeted but are not contributing to the projected year-end variance and are explained later in this section.

Property Taxes are trending lower-than-budgeted mainly due to the timing of when the fiscal year's budget is developed and associated revenue assumptions are made, relative to when the budget is adopted. Property Taxes are projecting a negative variance of $2.6 million which constitutes just 0.9% of total adopted Property Tax revenue. TOT revenue is also trending lower-than-budgeted by about $400 thousand, indicating a softening in the economy and discretionary spending, but is being offset by unanticipated growth in Interest Income and Franchise Fee revenue. Interest Income remains strong with $1.6 million generated in the first quarter and a total of $5.4 million projected through year-end, resulting in a projected positive year-end variance of $2.1 million, primarily driven by the higher rate environment. Franchise Fees are also projecting higher-than-budgeted at $4.3 million through the fiscal year which would result in a positive year-end variance of $705 thousand. This is mainly attributable to increased gross receipts generated by a few of the utilities, which they are required to pay a percentage of as part of their Franchise Fee agreements. Additionally, Other Transfers show a net positive variance (the table reflects a negative expenditure which has a positive effect) of $865 thousand and is due to less GFC being allocated to the Department of Social Service's special revenue fund than was budgeted, due to higher than anticipated state revenues received. Overall, projections of discretionary revenues through the first quarter remain on target to meet budgetary expectations.

Discretionary General Revenue Summary (in thousands):			
Source	Adjusted FY 2023-24	Projected FY 2023-24	Variance Proj vs. Adjusted
Interest Income	3,283	5,389	2,106
Franchise Fees	3,598	4,303	705
Transient Occupancy Tax	17,562	17,163	(399)
Cannabis Tax	7,500	6,000	(1,500)
Property Taxes	295,362	292,777	(2,585)
All Other Revenues	45,445	44,822	(623)
Total Discretionary Revenues	**$ 372,750**	**$ 370,454**	**$ (2,296)**
Decrease to Cannabis Fund Balance	$ 7,500	$ 6,000	$ (1,500)
All Other Transfers	365,250	364,385	(865)
Projected Fiscal Year End Variance	**$ -**	**$ 69**	**$ 69**

Cannabis Cultivation and Retail Storefront Tax is currently projecting a negative variance of $1.5 million on an adopted budget of $7.5 million. This projected decrease continues to be driven by a decline in cultivation tax due to the oversupply of wholesale cannabis product and resulting price compression, in addition to the attrition of operators that have withdrawn from the program for a variety of reasons. Retail Storefront Tax also projects lower than budgeted primarily due to the timing of when each retail operator is expected to complete the land use entitlement and business licensing processes, relative to the timing assumptions made when the budget was developed. Additionally, receipts for the retail storefront businesses that have commenced operations have come in lower than anticipated as these are new operations in their respective locations. Staff will continue to monitor retail storefront tax receipts as this is a new activity being conducted in the unincorporated area without any historical data available for reference.

Probation is currently projecting a positive $721 thousand dollar variance (0.8% on an adopted budget of $87.0 million), primarily due to salary and benefit savings. The department's positive variance is significantly lower than projected at this time last year due to success in filling some vacant positions, with the current funded vacancies at 38 compared to a high of almost 60 last fiscal year.

Clerk-Recorder Assessor is currently projecting a positive $335 thousand dollar variance (1.9% on an adopted budget of $18.1 million), mainly attributable to vacant, funded positions.

Treasurer-Tax Collector is currently projecting a positive $351 thousand dollar variance (3.3% on an adopted budget of $10.6 million), primarily driven by higher-than-anticipated administrative revenues received for Tax Collector cost collection, supplemental property tax, and TOT late filing fees.

The **Sheriff's Office** is currently below the reportable threshold, with only a slightly negative projection of $1,731 at first quarter. Overtime costs through the first quarter were $4.3 million on a prorated quarterly budget of $1.3 million, exceeding the quarter's budget by $3 million. For comparison, overtime costs in the first quarter of FY 2022-23 were also $4.3 million, while overtime *hours* are down by 5% compared to last year at this time.

Currently the overage in overtime costs is being absorbed by salary and benefit savings due to vacant positions. If these trends continue, the department could ultimately exceed its overtime budget by $12 million, consistent with the prior year amount, which would be predominantly absorbed with salary savings, except for overtime related to filling behind deputies on leave or in training.

However, there may be periods of time when unbudgeted overtime cannot be covered by salary savings, particularly to the extent new deputies are hired and undergo mandatory academy and custody or field training, which requires overtime to backfill and is not offset with salary savings. As of the writing of this report, the Sheriff's Office just welcomed 11 new Custody Deputy hires to begin the custody academy in November. In addition, on November 7, the Board approved a $30,000 hiring bonus for Custody Deputies that should assist with hiring efforts.

The department recently received notification of a $527 thousand award from the State Criminal Alien Assistance Program (SCAAP) for 2022, which will be used to offset existing overtime costs in the jails. The notification was received after quarterly projections were finalized and is therefore not factored into the projection indicated above. The department also applied for funding for 2023 but has not yet been notified of that award. If awarded, the funding amount will vary based upon how many agencies apply for that year's funding.

Consistent with prior Board direction, to the extent there is a budget deficit at year-end, the department may then receive reimbursement for eligible overtime costs and recruitment incentives from the $2 million set-aside of Proposition 172 funds. CEO staff continues to work with the Sheriff's Office to vet the department's proposed overtime validation process, with the goal of accurately accounting for the various drivers of overtime costs, including the impact of vacancies, academy and field/custody training time, lost time (e.g. sick leave, vacation leave etc.), and special needs (e.g. emergencies, investigations, seasonal). The validation process is underway to determine to what extent the proposed methodology can be applied in future years; progress has been made over the quarter and CEO staff anticipates it will be substantially completed over the next quarter. The ultimate goal is to determine a baseline level of overtime that can be used to assess what level of additional ongoing resources may need to be added to the Sheriff's budget to address overtime costs in excess of budget. Additionally, it is possible that following the transition to Workday, the department may be able to develop and implement additional time tracking processes throughout the organization that would accomplish the desired level of precision in measuring the impact of various factors that drive overtime; however, this is yet to be determined.

SPECIAL REVENUE AND OTHER FUNDS SUMMARY (Attachment B)

As of September 30, 2023, there were no departments with reportable variances in the Special Revenue and Other Funds for the first quarter.

ADVANCE CONSTRUCTION RESERVE ACTIVITY

Beginning in FY 2021-22, the budget included the temporary transfer of General Fund cash to Public Works (Fund 0017) for costs associated with high-cost bridge construction that requires cashflow in advance of federal reimbursement. There have also been temporary transfers to General Services for design and construction of the new Probation headquarters, which is currently underway, as well as the EOC portion of the Fire Dispatch Center project. Both transfers will be reimbursed once debt is issued for this, and other projects. Additionally, a transfer was made at the end of the 2022-23 fiscal year to cover costs on the Betteravia Solar Array, which will be reimbursed by a loan from the California Energy Commission upon project completion. Finally, the Board approved temporary transfers of funds in the current fiscal year to support construction costs for the Cachuma Lake RV Renovation project as well as design services associated with the Main Jail Renovation project. Although funds on these last two projects have yet to be transferred, any amount that does get expended will be reimbursed once debt is issued for these projects later this fiscal year. The status of these transfers and reimbursements will be reported in each quarterly update to the Board, as summarized in the below table.

Project	Transferred To-Date	Reimbursed to General Fund To-Date
Floradale Bridge	($5,270,600)	$3,000,000
Foothill Bridge	($3,000,000)	$0
Probation HQ	($1,281,194)	$0
EOC/Fire Dispatch Center	($309,418)	$0
Betteravia Solar Array	($1,416,379)	$0

The Board approved a Budget Development policy in December 2021 to establish an Advance Construction Reserve in General County Programs to provide cashflow for reimbursable projects and track the activity. Staff will process budget revision requests as cashflow is needed for the projects.

FUNDED VACANCIES BY DEPARTMENT (Attachment C)

At the close of the first quarter, 695 of the County's 4,644 funded positions were vacant, resulting in a funded vacancy rate of 15%. Over half of the funded vacancies are concentrated in the Sheriff, Social Services, Public Health and Behavioral Wellness departments, with the Sheriff and Social Services share of vacancies slightly lower than their share of overall position allocations; and the Public Health and Behavioral Wellness share of vacancies slightly greater. Departments with funded vacancy rates over 20% include Information Technology, Human Resources, General Services, Public Defender and Auditor-Controller. The Board of Supervisors and District Attorney had the lowest funded vacancy rates of approximately 5%. A table of funded vacancy rates by department as of September 30, 2023, may be found in Attachment C.

CANNABIS TAXATION, COMPLIANCE AND ENFORCEMENT ACTIVITY (Attachment D)

As of the writing of this board letter the County collected $518 thousand in gross cannabis tax receipts for the first quarter period. Operators filed and reported more tax revenue but have an additional thirty days, per County Code to pay the taxes owed, which means total first quarter collections will be approximately $1.7 million. The County completed five enforcement actions against illegal cannabis activities: 11,287 plants and 218 pounds of cannabis product were confiscated totaling an estimated street value of $5.7 million. The County also issued two new cannabis business licenses.

Since the cannabis business licensing program began, operators submitted a total of 222 business license applications. To date, 109 have been issued and 61 license applications are still pending. Further details on the types of licenses can be found in Attachment D. The majority of these pending business license applications remain in process, largely due to: 1) applicants that have been approved for a land use entitlement, but have not yet been issued a final, un-appealable entitlement, as many applications are being appealed after approval, and 2) applicants that have not yet obtained required building permits to construct new buildings and other infrastructure, or change the use of existing buildings. The balance of submitted applications have been withdrawn or abandoned. Over the last year, the County has seen several prospective cannabis cultivation operators withdraw from the business license process mainly citing financial constraints. This is consistent with the reduction in cannabis taxes collected and the resulting price compression we have seen in the market.

ATTACHMENTS

A – Financial Summary Report – General Fund
B – Financial Summary Report – Special Revenue and Other Funds
C – Funded Vacancies by Department
D – Cannabis Taxation, Compliance and Enforcement, First Quarter FY 2023-24

Authored by:

CEO Budget and Research Division