



**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

**Department Name:** CEO  
**Department No.:** 012  
**For Agenda Of:** March 14, 2023  
**Placement:** Departmental  
**Estimated Time:** 30 minutes  
**Continued Item:** No  
**If Yes, date from:** N/A  
**Vote Required:** Majority

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**TO:** Board of Supervisors  
**FROM:** Department: Mona Miyasato, County Executive Officer  
Director(s)  
Contact Info: Paul Clementi – Budget Director  
Jeff Frapwell, Assistant CEO – Cannabis Administration Division

DocuSigned by:  
*Mona Miyasato*  
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**SUBJECT: Fiscal Year 2022-23 Second Quarter Budget Status Report and Cannabis Taxation, Compliance and Enforcement Update**

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**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) 2022-23 Second Quarter Budget and Status Report as of December 31, 2022, 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 2022-23 budget status report for the second quarter ending December 31, 2022 provides a fiscal-year-to-date look at the County’s financial position relative to the FY 2022-23 adjusted budget. The County’s General Fund is projecting a net positive variance of \$28.5 million compared to the adopted budget due to greater property tax revenues than budgeted, in part due to significant reassessments, and higher salary savings due to vacant positions. This higher property tax base has been used in the Five-Year Forecast and next year’s budget, which the Board will review at Budget Workshops in April 2023.

Midway through the fiscal year, cannabis tax revenue continues to trend lower than budgeted with a projected \$10.5 million negative variance, which is discussed in greater detail below. The fiscal position

of the General Fund will continue to be monitored and presented to the Board on a quarterly basis. At the end of the fiscal year, any funds resulting from a positive variance are typically carried forward for the Board to consider as part of the next budget cycle development as priorities and fiscal issues are identified.

Additionally, the Fire Protection District and Social Services Department had reportable positive variances in Special Revenue Funds totaling \$6.1 million driven by several factors including unanticipated State Realignment revenue, higher than anticipated property tax, and salary savings on vacant, funded positions, all of which will be discussed in greater detail below.

## **SECOND QUARTER REPORT**

The second quarter for the fiscal year includes activity through December 31, 2022. 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 six months of FY 2022-23, and then add departmental projections for the next six 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 December 31, 2022, the General Fund had a projected year-end positive variance of \$28.5 million. This is the result of favorable results in most General Fund departments, partially offset by a reportable negative variance in one department.

**General Revenues (Department 991)** projects a positive year-end variance of \$23.1 million, 6.8% over total budgeted revenues, shown in detail in the table below. This variance is due primarily to higher than budgeted Property Tax, Interest Income, Transient Occupancy Tax (TOT), and Sales and Use Tax. 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 the major driver of the General Revenue's positive variance through the second quarter as they project higher than budget by \$17.1 million. Secured and unsecured property taxes are mainly driving this variance as they project to exceed budget by \$13.9 million, primarily due to the real estate market that flourished over the last several years resulting from historically low mortgage rates and high demand for residential and commercial properties. As expected in a strong real estate market, a high volume of property ownership changes occurred over the past two years and were reassessed upon property transfer. In many instances, the reassessed property values increased substantially, thereby contributing to robust assessed property value growth of 8.1% for the property tax year 2022-23. At the time that the current fiscal year's property tax budget was developed, Auditor-Controller staff had anticipated that assessed value growth would be strong at 4.5%; however, the Assessor finalized the tax roll at the end of June with substantially higher growth resulting in the positive variance. Property Taxes In-lieu of Vehicle License Fees (VLF) are also contributing to the positive variance in property taxes as they project higher than budget by \$2.4 million, given that they too are driven by assessed value growth.

**Interest Income** is another significant driver of the General Revenue's positive variance as it projects to exceed budget by \$2.5 million due to treasury interest rates that have modestly, yet consistently, increased in each quarter of calendar year 2022 as banks enter a higher rate environment. Year-end projections have been updated accordingly to reflect this new trend in rates.

**Transient Occupancy Tax (TOT)**, which is highly dependent on tourism, is also projecting a positive variance and expected to exceed budget by \$2.2 million. Although TOT receipts remained elevated through the first two quarters of the fiscal year, growth could slow in the second half of the year, if continued inflation begins to impact consumers and discretionary spending. Of note, the Biltmore Hotel has continued to be closed since March 2020, but prior to 2020 had been one of the County's largest TOT generators. In the FY 2022-23 Adopted Budget, the Board funded a TOT Compliance position in the Treasurer Tax Collector's office to perform proactive audits of hotels and short-term rentals. The department was able to purchase software to assist with this effort, but the position is currently vacant.

Similarly, **Sales and Use Tax** revenue also projects a positive variance of \$980 thousand as consumer spending remained steady through the first half of the fiscal year. However, according to Sales and Use Tax consultant, HdL, the actions taken by the Federal Reserve to address inflation over the past year are expected to take effect and exert downward pressure on many of the major industry sectors, resulting in decreased consumer demand for goods and a deceleration in Sales and Use Tax growth in the second half of the current fiscal year.

<b>Discretionary General Revenue Summary (in thousands):</b>			
<b>Source</b>	<b>Adjusted FY 2022-23</b>	<b>Projected FY 2022-23</b>	<b>Variance Proj vs. Adjusted</b>
Property Taxes	\$ 262,545	\$ 279,623	\$ 17,078
Interest Income	727	3,219	2,492
Transient Occupancy Tax	15,165	17,344	2,179
Sales and Use Retail State Tax	14,240	15,220	980
Cannabis Tax	16,293	5,780	(10,513)
All Other Revenues	32,415	32,775	360
<b>Total Discretionary Revenues</b>	<b>\$ 341,385</b>	<b>\$ 353,961</b>	<b>\$ 12,576</b>
Decrease to Cannabis Fund Balance	\$ 16,293	\$ 5,780	\$ (10,513)
All Other Transfers	325,092	325,092	0
<b>Projected Fiscal Year End Variance</b>	<b>\$ -</b>	<b>\$ 23,089</b>	<b>\$ 23,089</b>

**Cannabis Cultivation and Retail Storefront Tax** is currently projecting a negative variance of \$10.5 million on an adopted budget of \$16.3 million. This projected decrease continues to be primarily driven by a decline in cultivation tax due to the oversupply of wholesale cannabis product and resulting price compression that continues to persist locally and state-wide. Other major factors contributing to the decrease in revenue include cultivators withdrawing from the program for a variety of reasons and some electing not to grow, mostly due to market conditions. Retail Storefront Tax is also projecting lower than budgeted but is directly related 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.

Despite declining cannabis revenues, the projected revenues in addition to fund balance carryover from last year will likely be sufficient to fund the 2022-23 cannabis program costs and other ongoing allocations made from cannabis revenues in prior years, including funding for libraries, planners in long range planning, deferred maintenance funding, and more. See Attachment D. However, if revenues remain at this level in FY 2023-24, there will not be enough to cover all the ongoing and one-time commitments made on cannabis revenues in prior years. Staff will continue to closely monitor cannabis tax revenues as the fiscal year progresses and will update the Board at the April Budget Workshops.

**Probation, Community Services, Public Health-Animal Services, Auditor-Controller, Treasurer Tax-Collector, and County Counsel** are all projecting positive year-end variances, primarily driven by salary savings associated with vacant, funded positions. The individual department variances are as follows: Probation - \$2.8 million (3.3% on total budget of \$83.2 million), Community Services - \$660 thousand (1.5% on total budget of \$44.4 million), Public Health-Animal Services - \$493 thousand (8.2% on total budget of \$6 million), Auditor-Controller - \$421 thousand (4.1% on total budget of \$10.3 million), Treasurer Tax-Collector - \$393 thousand (3.9% on total budget of \$10.1 million), and County Counsel - \$299 thousand (2.5% on total budget of \$11.7 million).

**Sheriff-Coroner Office** is projecting a negative year-end variance of \$369 thousand, 0.02% on a total budget of \$188.6 million, primarily due to overtime costs in excess of budget. Overtime costs through the second quarter were \$8.7 million on an annual budget of \$5.0 million, exceeding budget by \$3.7 million with two quarters left. However, the majority of this overage is being absorbed by salary and benefit savings as a result of numerous funded vacancies within the department. If these trends continue, the department could ultimately exceed their overtime budget by \$13 million, which would be predominantly absorbed with salary savings, except for overtime related to filling behind deputies on leave or in training.

While the direct financial impact may be addressed through salary savings, there are indirect costs associated with the levels of overtime being utilized, such as increase in disability retirements, staff fatigue, increased leave taking, and higher staff turnover, all of which make this situation untenable in the long-term.

While filling vacancies is a high priority for the Sheriff's Office and Board, there may be periods of time when unbudgeted overtime cannot be covered by salary savings. This would cause the Sheriff's projected negative variance to grow larger and is an unavoidable short-term cost as new staff come on board, which has occurred in the past several years.

To help assist the department, on October 18, 2022, the Board authorized use of the \$2 million set-aside of Proposition 172 for eligible overtime costs and recruitment incentives such as the new hiring incentive. The Board also directed the County Human Resources Department to develop a referral program for hard to fill positions, such as Custody Deputies, which was approved by the Board on February 14, 2023. The CEO's Office continues to work closely with the department to develop more robust tracking of overtime drivers.

#### **SPECIAL REVENUE AND OTHER FUNDS SUMMARY (Attachment B)**

As of December 31, 2022, there were two departments with reportable variances in the Special Revenue and Other Funds for the second quarter.

**The Fire Protection District (Fund 2280)** is projecting a positive year-end variance of \$3.5 million, 3.2% on a budget of \$110.8 million. This is primarily driven by higher property tax growth than originally anticipated, similar to the General Revenues department, and salary savings associated with unanticipated vacancies, including a four-month deferral of the firefighter recruit academy.

**Social Services (Fund 0055)** is projecting a positive year-end variance of \$1.8 million, 1.0% on a total budget of \$184.6 million, which is driven by unanticipated revenues and salary savings. 1991 Realignment and 2011 Realignment revenues are projected to exceed budgeted amounts due to the receipt of one-time sales tax growth payments of \$544 thousand and \$2.5 million in 1991 Realignment and 2011 Realignment revenues, respectively. Additionally, the department is projecting to underspend in Salaries and Employee Benefits by \$5.6 million due to staffing vacancies. The department regularly balances their adopted budget with fund balance draws because Realignment revenue growth isn't typically known until the fiscal year has started. These unanticipated revenues and savings will allow the department to preserve their fund balance for future years.

**SB IHSS Public Authority (Fund 0056)** is projecting a positive year-end variance of \$786 thousand, 6.0% on a total budget of \$13.0 million, due to unanticipated 1991 Realignment revenue. The department received a one-time caseload growth payment of \$810 thousand in 1991 Realignment revenue to support prior year increases in county costs for the In-Home Supportive Services (IHSS) program; this growth is expected to increase the program's base level of funding. As of December 31, 2022, realignment revenue is projected to fully cover this year's increase in the IHSS maintenance of effort.

#### **ADVANCE CONSTRUCTION RESERVE ACTIVITY**

Beginning in FY 2021-22, the budget includes 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. The Board has approved an estimated cashflow need for two bridge projects currently in progress. The status of those transfers will be reported in each quarterly update to the Board.

<b>Project</b>	<b>Board Date</b>	<b>Approved Maximum</b>	<b>Transferred To-Date</b>	<b>Net Remaining</b>	<b>Period of Cashflow Need</b>
Floradale Bridge	6/8/2021	\$6,800,000	(\$5,270,600)	\$1,529,400	2021-2024
Foothill Bridge	1/11/2022	\$6,000,000	-0-	\$6,000,000	2022-2025
<b>Totals</b>		<b>\$12,800,000</b>	<b>(\$5,270,600)</b>	<b>\$7,529,400</b>	

To the extent that federal reimbursements are received throughout the projects, that cash will be used first prior to any General Fund transfer. The Board approved a Budget Development policy in December 2021 to establish an Advance Construction Reserve in General County Programs to set aside the maximum amount estimated for the projects and track the activity. Staff will process budget revision requests as cashflow is needed for the projects.

#### **CANNABIS TAXATION, COMPLIANCE AND ENFORCEMENT ACTIVITY (Attachment C)**

During the second quarter, the County collected \$1.1 million in cannabis gross tax receipts. The County completed five enforcement actions against illegal cannabis activities: 1,969 plants and 586 pounds of cannabis product were confiscated totaling an estimated street value of \$1.6 million. The County also issued fourteen new cannabis business licenses.

As reported in the past, the County has approved enough cultivation acreage in land use entitlements to exceed the acreage cap in the unincorporated inland area. There are currently fourteen operators with approved land use entitlements on the waiting list for this area requesting a total of over 235 acres. The acreage cap in Carpinteria has yet to be committed. To date, operators submitted a total of 210 business license applications through the second quarter, of which 76 have been issued. 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 or change the use of existing buildings. Further details can be found in Attachment C.

#### **ATTACHMENTS Attachments:**

- A – Financial Summary Report – General Fund
- B – Financial Summary Report – Special Revenue and Other Funds
- C – Cannabis Taxation, Compliance and Enforcement, Second Quarter FY 2022-23
- D – Historical Cannabis revenue and expenditures

#### **Authored by:**

CEO Budget and Research Division  
Brittany Heaton, CEO Cannabis Administration Division