



Agenda Date: 1/10/2006
Agenda Placement: 9E

NAPA COUNTY BOARD OF SUPERVISORS Board Agenda Letter

TO: Board of Supervisors
FROM: Britt Ferguson for Nancy Watt - County Executive Officer
County Executive Office
REPORT BY: Britt Ferguson, Assistant County Executive Officer, 253-4406
SUBJECT: Approval of Fiscal Year 2006-07 Budget Policies and Budget Calendar

RECOMMENDATION

County Executive Officer requests approval of:

1. Proposed Budget Policies to guide the preparation and administration of the County's Fiscal Year 2006-2007 Budget; and
2. The Proposed Fiscal Year 2006-2007 Budget Calendar.

EXECUTIVE SUMMARY

With the County's FY2006-07 Budget process getting under way, your Board is being asked to review, revise and/or approve the Proposed Budget Policies that will guide staff in preparing and administering the FY2006-07 Budget. Last year, staff provided your Board with a General Fund Five Year Revenue/Expenditure Forecast that projected General Fund revenues, expenditures and fund balance under three different scenarios. All of the scenarios indicated that it is likely expenditures will continue to exceed revenues by increasing amounts. Taken together, the forecasts suggested that it will be necessary to spend down General Fund fund balance to balance the budget in the future and it will not be possible to continue reliance on the fund balance to meet long term needs, though, thanks to prudent financial planning in the past, we will have sufficient resources to maintain General Fund supported programs at current levels through at least the next two years. The Proposed Budget Policies take this information into account, but also reflect the fact that, the County is facing certain fiscal uncertainties in the future. These uncertainties include:

- | What the General Fund fund balance will be at the end of this fiscal year;
- | A clear understanding of the long-term impact on the General Fund of revenue and expenditure decisions made this year and, in particular, whether last year's General Fund Five Year Forecast remains valid; and
- | The impact of the State's budget on the County.

Given this, key provisions of the Proposed Budget Policies include:

- | For General Fund departments (except Health & Human Services), prepare budgets with a goal of funding current staffing levels. Departments are also asked to prepare a Decision Package showing the impact of holding the Net County Cost to the current (FY2005-06 Final Budget) level.
- | For non-General Fund departments and Health & Human Services, prepare budgets with a goal of holding the General Fund Contribution or Net County Cost to the current (FY2005-06 Final Budget) level.
- | No new or enhanced programs are to be proposed, unless they are funded by dedicated revenues or your Board has previously determined that they are a high priority.
- | Delete all vacant unfunded positions and all positions that have been vacant for more than 6 months, unless retention of a vacant funded position has been approved by the County Executive Office.
- | For departments or budget units with 20 or more allocated positions, budgets should be reduced to reflect historic salary savings.
- | Seek enhanced operational efficiency by eliminating, combining or reorganizing programs to reduce expenditures and/or respond to changing needs and priorities.
- | Do not backfill reductions in State or federal funding unless there is a legal mandate to do so or the program is a high priority for the Board.
- | Place at least 3% of the General Fund's appropriation in Contingency and work toward a goal of building General Reserves equivalent to approximately 5% of General Fund appropriations.
- | After meeting operating and capital budget needs, the General Fund Contingency and General Reserve requirements and making any required designations, place any remaining discretionary resources in Capital Reserves.

Your Board is also being asked to approve a proposed Budget Calendar for FY2006-07. This calendar includes the schedule for preparing the FY2006-07 Budget, as well as the schedule for preparing FY2005-06 Mid-Year and Third Quarter fiscal reviews and the Five Year General Fund Forecast. Key dates include presentation to your Board of the Mid Year fiscal review on March 7th, your Board's Budget Study Session on March 28th and budget hearings on June 12th through 14th.

FISCAL IMPACT

Is there a Fiscal Impact? No

ENVIRONMENTAL IMPACT

ENVIRONMENTAL DETERMINATION: The proposed action is not a project as defined by 14 California Code of Regulations 15378 (State CEQA Guidelines) and therefore CEQA is not applicable.

BACKGROUND AND DISCUSSION

Staff will soon begin the process of preparing the County's FY2006-07 Proposed Budget. One of the first steps in that process is to seek direction from your Board on Budget Policies that will guide staff in preparing and administering the Budget. To that end, the attached "Proposed FY2006/07 Budget Policies" are recommended for your review, possible modification and approval.

Over the last few years, your Board has controlled spending, and prudently set aside significant reserves and designations, to help ensure that funding for County programs can be sustained at an appropriate level. Nevertheless, the County is facing a number of uncertainties with regard to this fiscal year, next fiscal year and the

fiscal years immediately following. Those uncertainties include:

- | We do not know how much General Fund fund balance will be available at the end of this fiscal year. That fund balance will serve as an important resource for financing FY2006-07 expenditures and/or building appropriate reserves. We are just starting the FY2005-06 Mid-Year fiscal review process and will be able to provide your Board with a status report by early March. However, past experience has shown that the Mid-Year fiscal review is not as accurate at estimating the ending fund balance as the Third Quarter review, which will not be available until May.
- | The longer-term fiscal condition of the General Fund will need to be projected, since expenditure decisions made in FY2006-07 will have an impact on future years' budgets. As your Board knows, in recent years, actual General Fund expenditures have slightly exceeded revenues, requiring use of fund balance to cover the difference. A General Fund Five Year Revenue/Expenditure Forecast, prepared in March of last year, projected revenues, expenditures and ending fund balance under three different scenarios. All of those scenarios indicated that it is likely that expenditures will continue to exceed revenues by increasing amounts. Taken together, the forecasts suggested that it will be necessary to spend down the General Fund's fund balance to balance the budget in future years and it will not be possible to continue reliance on the fund balance to meet long-term needs, though we will have sufficient resources to maintain General Fund supported programs at current levels through at least the next two years. Following the completion of the Mid-Year fiscal review, staff will prepare a new General Fund Five Year Forecast, which will provide your Board with updated projections of the General Fund's fiscal condition.
- | The impact on the County of the State's budget situation is not entirely clear. The information available at this point suggests that the State's fiscal situation is the best it has been in at least the last three fiscal years. In a November 2005 report, the Legislative Analyst's Office (LAO) indicated that, due in part to significant revenue increases, the State should have sufficient carryover reserves to balance the FY2006-07 budget without new program reductions or added revenues. However, the Legislative Analyst also warned that the State is not out of the fiscal woods yet. According to the LAO, the State will continue to face significant operating shortfalls for at least the next five years, even assuming continued steady economic growth. Further, notwithstanding the protections provided local governments by Proposition 1A, counties continue to be at risk for efforts by the Governor and/or legislature to shift costs from the State to local governments. We will have some idea of what the impact of the State budget on the County might be after the Governor issues his FY2006-07 Proposed Budget and an even better idea after he issues his May Revise.

Given the above, the Proposed Budget Policies include the following key provisions:

- | For General Fund departments (except Health & Human Services), prepare budgets with a goal of funding current staffing levels. Departments are also asked to prepare a Decision Package showing the budget impact of holding the Net County Cost to the current (FY2005-06 Final Budget) level. Based on what we know about the current fiscal situation, it makes sense to budget conservatively, but not to require staffing reductions that might otherwise be necessary to fund salary and benefit cost increases approved this year. The Decision Packages would be used on a case by case basis if additional fiscal information suggests that expenditure reductions are necessary. Your Board has directed staff to prepare a Strategic Financial Plan for the County. Once prepared and approved by your Board, that plan will provide long term direction for funding levels for different departments and programs.
- | For non-General Fund departments and Health and Human Services, prepare budgets with a goal of holding the General Fund Contribution or Net County Cost to the current (FY2005-06 Final Budget) level. If necessary, Health & Human Services can prepare a Decision Package that shows the impact of increasing

Net County Cost for critical programs to maintain current staffing. Depending on specific circumstances and based on the most recent fiscal information available, the Decision Package will be considered by the County Executive Officer. These are departments that are typically funded with State and/or federal revenue or other dedicated resources and it is prudent to size the programs to fit the available revenues. There may be exceptions to this in Health & Human Services if holding to the current Net County Cost results in unacceptable impacts to critical programs.

- | Do not propose any new or enhanced programs, unless they are funded by dedicated revenues or your Board has previously determined that they are a high priority.
- | Delete from the Department Allocation List all vacant unfunded positions and vacant funded positions that have been vacant for more than 6 months, unless the County Executive Office has approved retaining a vacant unfunded position.
- | To the extent permitted by law, all revenues not previously earmarked for a particular purpose by the Board are to be treated as discretionary revenues rather than tied to a particular program, thus providing the Board with as much flexibility as possible in terms of use of resources.
- | Seek operational efficiencies by eliminating, combining or reorganizing programs to reduce expenditures and/or respond to changing needs and priorities. In general, the goal is to make sure that programs are still serving an important need or Board priority and, if so, that services are provided as cost-effectively as possible.
- | If funding is reduced for programs that are primarily a non-General Fund responsibility, there will be no increase in General Fund Contribution unless that is legally mandated or the program is a high priority for the Board.
- | For departments or budget units with 20 or more allocated positions, Departments should submit a budget that includes a reduction in salary and benefit costs to reflect a vacancy factor based on historic vacancy rates for that program, adjusted to reflect current circumstances. This is a new policy and, given the goal of funding current staffing levels in the General Fund, this will help to ensure that Net County Cost is not over-budgeted.
- | Place at least 3% of the General Fund's appropriation into Contingency and work toward a goal of building General Reserves equivalent to approximately 5% of General Fund appropriations. The Contingency would be utilized to cover the impact of unanticipated cost increases or revenue decreases during the fiscal year. With regard to the General Reserves, the idea would be to add to the reserves when resources are available until the 5% level is reached. Then, in times of fiscal difficulty, the Reserves can be utilized to help phase into needed reductions in expenditures. Cities and counties typically maintain contingencies in the area of 3 to 5% of appropriations. The FY2005-06 Final Budget included \$5 million in the General Fund Contingency, which represents approximately 3% of General Fund appropriations. The FY2005-06 Final Budget included General Reserves of approximately \$7.87 million, which represents approximately 4.6% of appropriations. The amount of General Reserves appropriate for a local government can vary considerably depending on specific circumstances, with goals in the range of 5 to 10% appropriations being common. Reserves are typically used for two purposes: to provide funds that can be used in future years to balance the budget (reserves cannot be spent in the current fiscal year) and to aid in cash flow, so that short term borrowing against anticipated revenue is not needed. In Napa County's case, we not only have General Reserves, but also Fund Balance Designations which are typically ear-marked for a specific purpose. Thus staff believes that a prudent Reserve of 3% and a goal over time of 5% would be adequate.
- | After meeting FY2006-07 operating and capital budget needs, the General Fund Contingency and General

Reserve requirements and making any required designations, place any remaining discretionary resources in Capital Reserves. This is a new policy and is being recommended due to the number of significant new capital projects on the horizon including the potential construction of additional jail beds and a new County Administration Building.

- | Continue to include quantitative performance indicators in the Recommended Budget document.

Also attached is the proposed FY2006-07 Budget Calendar. This calendar sets out the schedule for preparing the FY2006-07 Budget as well as the schedule for the FY2005-06 Mid-Year and Third Quarter reviews and the General Fund Five Year Forecast. As you can see, the schedule calls for your Board receiving a Mid-Year fiscal review on March 7, 2006, holding a Budget Study Session on March 28th and holding budget hearings June 12th through 14.

SUPPORTING DOCUMENTS

- A . Proposed FY2006-07 Budget Policies
- B . Proposed FY2006-07 Budget Calendar

CEO Recommendation: Approve

Reviewed By: Maiko Klieman