## COUNTY ADMINISTRATOR'S BUDGET MESSAGE

DATE: May 24, 2018

TO: Board of Supervisors

FROM: Birgitta E. Corsello, County Administrator

SUBJECT: FY2018/19 Recommended Budget

Staff recommends that the Board of Supervisors conduct Budget Hearings beginning at 9:00 a.m. on June 19, 2018 and approve an Adopted Budget at the conclusion of the hearings. During the hearings, the Board will be requested to consider increasing and/or funding additional positions, investments in technology and County facilities, contributions to non-county agencies, reserves, and the use of one-time funds received in FY2017/18.

In creating a Recommended Budget, departments were asked to submit a budget that balanced meeting their financial and policy requirements to provide services to the community while asking them to target the goal of “restrained growth” in General Fund costs throughout FY2018/19 in an effort to offset increased wages and benefits. The FY2018/19 Recommended Budget reflects a concentrated effort to balance increasing labor costs and services required while continuing to address priorities identified by the Board of Supervisors. Solano County has seen some job growth, further reductions in unemployment and an improving real estate market in 2017, but we continue to face uncertainty regarding adequate State and Federal funding and potential legislative changes that may affect how we deliver County mandated and discretionary services including health care, public assistance and public safety programs. We are confident the ongoing use of Board adopted Budget Strategies, including sound financial practices, enables departments to continue their commitment and efforts to contain costs by leveraging technology, partnerships, and State and federal funding when feasible.

The FY2018/19 Recommended Budget includes a section dedicated to the County Statistical Profile. This section provides key information on Solano County’s current economic outlook and captures indicators of the County’s achievements and challenges. Solano County had another year of solid job growth in 2017, adding 1,900 jobs to the local economy. Our population growth rate remains modest at 0.7% over the previous year, and according to the California Employment Development Department, overall employment in California also continues to improve, and has done so for the past several years. The unemployment rate in Solano County as of March 2017 stands at 4.1%, down from 5.4% in 2017 and in-line with the State average of 4.2%. While employment improves, Solano County’s 2016 Per Capita Income is the fourth lowest among benchmark counties at $46,151 according to the US Bureau of Economic Analysis. Further, slightly under one in four Solano County residents (24.5%) receives some form of public assistance, including CalFresh, CalWORKs, General Assistance, and Medi-Cal (health insurance). The local housing market has been strong and homeowners benefited as they experienced a 11.2% increase over the previous year in the median home price in 2018, which is partially driven by limited available inventory and increased demand. As home prices climb, the rental market follows with an average rental price for one and two-bedroom apartments climbing to $2,195 per month in December 2017, an increase of 30.1% from 2011 according to Zillow Research. While the economic indicators above reflect signs of Solano County’s continued recovery, they also reflect our challenges, and can affect how we provide services to Solano County residents. In FY2018/19 we will continue to monitor the County’s economic outlook, keeping in mind the potential impacts of the Federal 2017 Tax Cuts and Jobs Act and that by the end of the fiscal year the United States will have matched the longest economic recovery in its modern history. (*See County Statistical Profile Section*).

Included in this budget message are the following budget-related sections: 1) Budget Overview; 2) Financial Summary; 3) General Fund Reserves, Designations & Commitments and Fund Balance; 4) Overview of the federal and State Budgets; 5) Economic Risks; 6) FY2018/19 General Fund Recommended Budget; 7) General Fund and Fiscal Projection; 8) Pending Issues and 9) Summary of Recommendations.

## BUDGET OVERVIEW

| TOTAL FINANCING REQUIREMENTS - ALL GOVERNMENTAL FUNDS FY2018/19 | | | | |
|---|---|---|---|---|
| **FUND NAME** | **FY2017/18 ADOPTED BUDGET** | **FY2018/19 RECOMMENDED** | **CHANGE** | **% CHANGE** |
| GENERAL FUND | $ 273,369,859 | $ 268,940,129 | $ (4,429,730) | (1.6%) |
| SPECIAL REVENUE FUNDS | 714,495,730 | 715,200,992 | 705,262 | 0.1% |
| CAPITAL PROJECT FUNDS | 38,332,949 | 15,556,132 | (22,776,817) | (59.4%) |
| DEBT SERVICE FUNDS | 24,429,037 | 16,736,684 | (7,692,353) | (31.5%) |
| **TOTAL GOVERNMENTAL FUNDS** | **$ 1,050,627,575** | **$ 1,016,433,937** | **$ (34,193,638)** | **(3.3%)** |
| **BUDGETED POSITIONS** | 3,068.35 | 3,030.75 | (37.60) | (1.2%) |

The FY2018/19 Recommended Budget for Governmental Funds is balanced and totals $1,016,433,937 (*Schedules 1 and 2*). The total budget represents a decrease of $34.2 million or 3.3% when compared to the FY2017/18 Adopted Budget and relies on local, State and federal revenues, and the use of fund balances with limited draws from reserves.

The most significant change is reflected in the Capital Project Funds, which decreased by $22.8 million due to construction costs for the SB 1022 Sheriff training project mostly occurring in FY2017/18, and therefore not reflected in the FY2018/19 Recommended Budget. The increases in the Special Revenues Funds of $0.7 million are primarily due to increases in costs for Public Safety, Mental Health Services Act (MHSA), Road and other funds, offset by decreases in Health & Social Services and other funds. The decrease in the General Fund of $4.4 million is primarily due to reduced transfers to reserves and contingencies in FY2018/19; the reductions include the one-time transfer of $10 million from the General Fund – General Reserves to a new Reserve for the Property Tax System Replacement project in FY2017/18. These decreases are partially offset by increases in appropriations in General Fund departments, primarily reflecting increased labor costs and increased General Fund contributions to both Public Safety and Health and Social Services when compared to the FY2017/18 Adopted Budget. Finally, Debt Service Funds decreased by $7.7 million as a result of decreases in obligated fund balance due to the final principal payment on the 2004 Series Pension Obligation Bonds (POB's) paid in FY2017/18. Overall, the FY2018/19 Recommended Budget for All Governmental Funds decreased by 3.3% when compared to the FY2017/18 Adopted Budget.

The FY2018/19 Recommended Budget uses Midyear projected 6/30/18 fund balances in several departments with dedicated revenues and draws down $8.1 million from committed Fund Balances to meet County obligations. One-time General Fund revenues from FY2017/18 are recommended to be used to offset one-time costs and to fund increased liabilities for accrued leave payoff, employee related benefits for the projected PERS employer rate increases and to fund contributions to capital renewal reserves for the maintenance of the County buildings.

The Recommended Budget provides for a workforce of 3,030.75 FTE positions, excluding extra-help positions. This reflects a net decrease of 37.60 FTE from FY2017/18 Adopted Budget of which 40.8 were deleted in FY2017/18. A net difference of 3.2 FTE total additions results from the addition of 22.7 FTE, the deletion of 15.0 vacant FTEs, and 4.5 FTE expiring limited-terms. These changes over the past fiscal year, and the recommended changes included in the Budget, primarily reflect the continued efforts to align allocated positions throughout the County with evolving operational requirements.

The continued reliance on intergovernmental funding for State and federally mandated programs is a key aspect of the Recommended Budget. In FY2018/19, the Recommended Budget relies on the use of redirected 1991 Realignment growth funding, State General Fund, and one-time funding to cover known expenditure increases in In-Home Supportive Services (IHSS) and Social Services. New mandates without new funding and the redirection of 1991 Realignment growth funding beginning in FY2017/18 create an unsustainable budget for Mental Health in future years which will require service reductions, additional funding, or a combination of both. Social Services deleted 24.0 FTE in FY2017/18 and 3.5 FTE in the Recommended Budget to cover revenue shortfalls and may require additional program reductions during the upcoming year. Both IHSS and Social Services programs obligations are expected to increase County General Fund requirements in FY2018/19.

This Budget Summary narrative is accompanied by a series of budget tables that are intended to describe the budgeted expenditures and associated revenue used to fund the programs and services outlined in the respective budget units. The individual Department Recommended Budget narratives provide the following information: the purpose; function and responsibilities; significant challenges and accomplishments as identified by the Department Head; workload indicators (where pertinent and relevant); a summary of significant adjustments to the operation or budget; summary of position changes; and identification of pending issues and policy considerations as identified by the Department Head.

The following pages include a financial overview of the FY2018/19 Recommended Budget.

## FINANCIAL SUMMARY

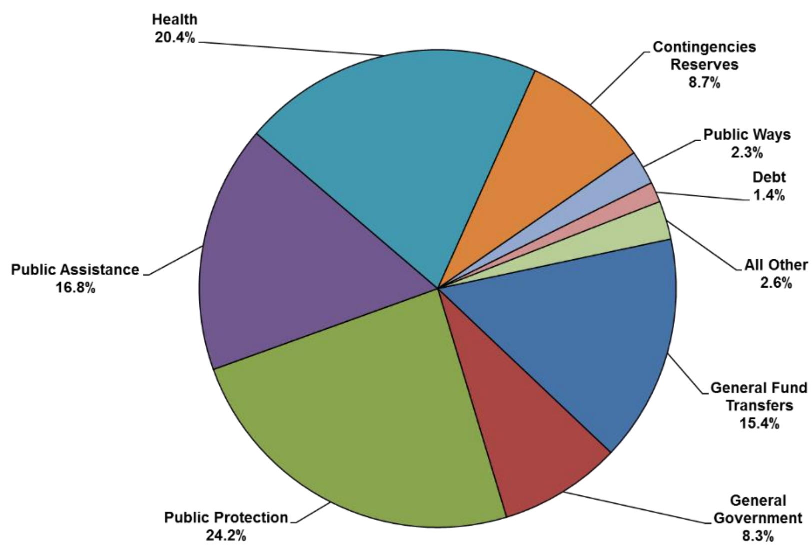
The Governmental Funds Spending Plan by Function graph portrays a total of $1 billion. The graph indicates the percent of the total for each of the functional areas required within the Governmental Funds part of the County Budget.

Public Protection represents the single largest category of County appropriations at 24.2% in the FY2018/19 Recommended Budget, which is in-line with the FY2017/18 Adopted Budget. Public Protection spending is projected to increase $9.6 million in FY2018/19 with the largest contribution to this increase being labor costs including wages and retirement, central data processing services, countywide administrative charges, and insurance.

Public Assistance, at 16.8%, and Health, at 20.4%, represent the social safety net function of County government, which together represents a decrease from FY2017/18. Health spending is projected to decrease by $8.9 million in FY2018/19, primarily due to decreased Intergovernmental Transfers (IGT) transactions and reduced spending in services and supplies including contracted services.

General Fund Transfers increase from a 14.3% share of the FY2017/18 Adopted Budget to a 15.4% share of the FY2018/19 Recommended Budget.

**Spending Plan by Function for FY2018/19**

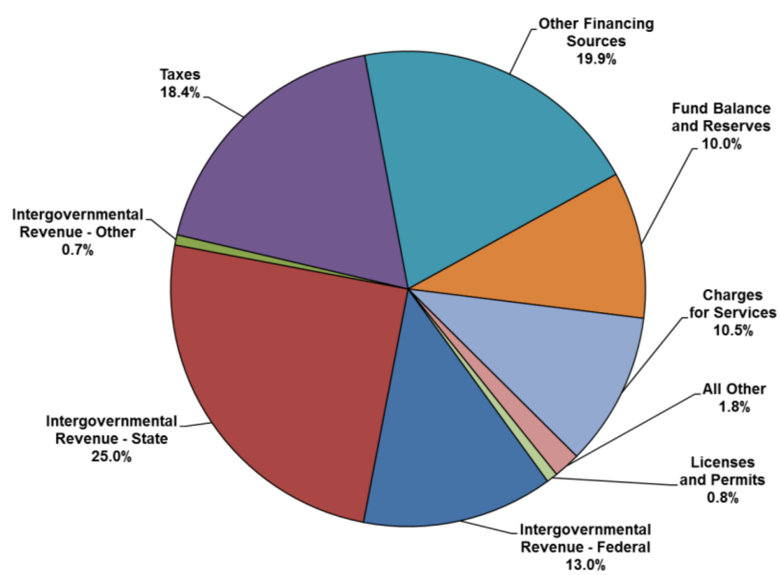



**GOVERNMENTAL FUNDS**
**Total: $1,016,433,937**

The Revenues by Source graph illustrates the different sources of funding to finance the Governmental Funds Budget. The largest revenue sources are Intergovernmental Revenue from State and federal agencies, which collectively account for 38% of the FY2018/19 Recommended Budget and generally have specific requirements on how funding can be used. Intergovernmental Revenue from State and federal agencies decreased by approximately $31.4 million primarily due to a reduction in State revenues related to the SB 1022 Jail Programing construction project funded in FY2017/18 and reduced IGT funding. Taxes represent 18.4% of the FY2018/19 revenue projections, which is up from the 16.9% share in FY2017/18.

Other Financing Sources represent 19.9% share of the FY2018/19 projected revenues, which is an increase from 18.9% share in FY2017/18. Fund Balance and Reserves represent a 10.0% share of the FY2018/19 revenues, which is a decrease from the 11.2% share in FY2017/18.

**Revenues by Source for FY2018/19**



The General Fund Spending Plan (*Fund 001*) graph portrays a total of $268.9 million. The Public Safety category represents the single largest category of expenditures at 44.6% in FY2018/19, which is in-line with its proportional share in FY2017/18. This category includes the Sheriff, District Attorney, Public Defender, Alternate Public Defender, Other Public Defense and Probation.

The General Government/All Other category represents a 32.5% share in FY2018/19, an increase from 29.5% share in FY2017/18. Functions listed under this category include Agricultural Commissioner, Resource Management, Registrar of Voters, General Government including Legislative, Administrative and Financing.

Health & Social Services is the third largest category of General Fund use at 10.7% of the total, which is up over the 9.7% share in FY2017/18 primarily due to the addition of the County Medical Services Program participation fee and increases in the IHSS MOE. The County's Maintenance of Effort (MOE) for the Courts is 3.4% of the total.

The Recommended Budget includes $8.8 million in one-time funds allocated to committed Fund Balances to address impacts of known future obligations for retirements, accrued leave payoff and capital renewal costs.

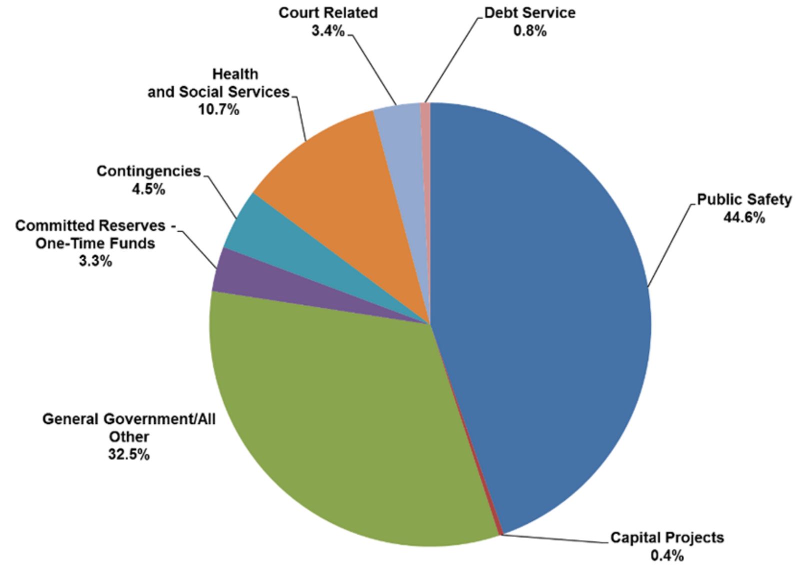
The Sources of General Fund Revenue graph provides information concerning General Fund financing for County operations.

Revenues derived from property values account for over half of General Fund revenues, with Property Taxes at 53.3% and ABX1 26 Residual and Pass-Through at 8.1%. Property taxes include secured, unsecured, supplemental, unitary, property tax in lieu of Vehicle License Fee (VLF) and property transfer tax. The FY2018/19 Recommended Budget projects a net increase of $8.1 million in these property related revenues when compared to the FY2017/18 Adopted Budget.

The next largest category is Charges for Services at 19.1%, which includes fees, permits, licenses, property tax administration fees and reimbursements for County costs of service.

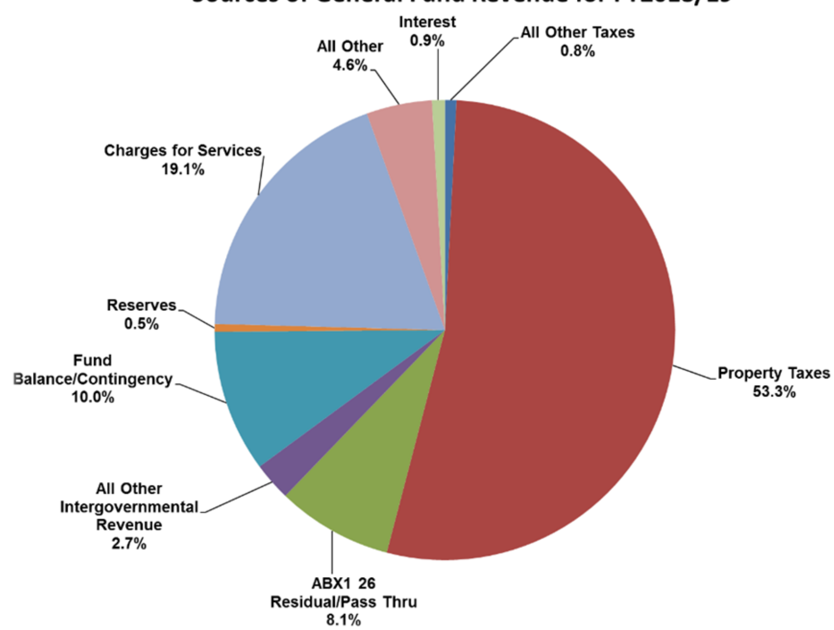
As shown, the third largest category is Fund Balance/Contingency at 10.0%. The General Fund projected Fund Balance at the end of FY2017/18 becomes a means of financing for the FY2018/19 Recommended Budget.

General Fund Spending Plan for FY2018/19




**GENERAL FUND**
**Total: $268,940,129**

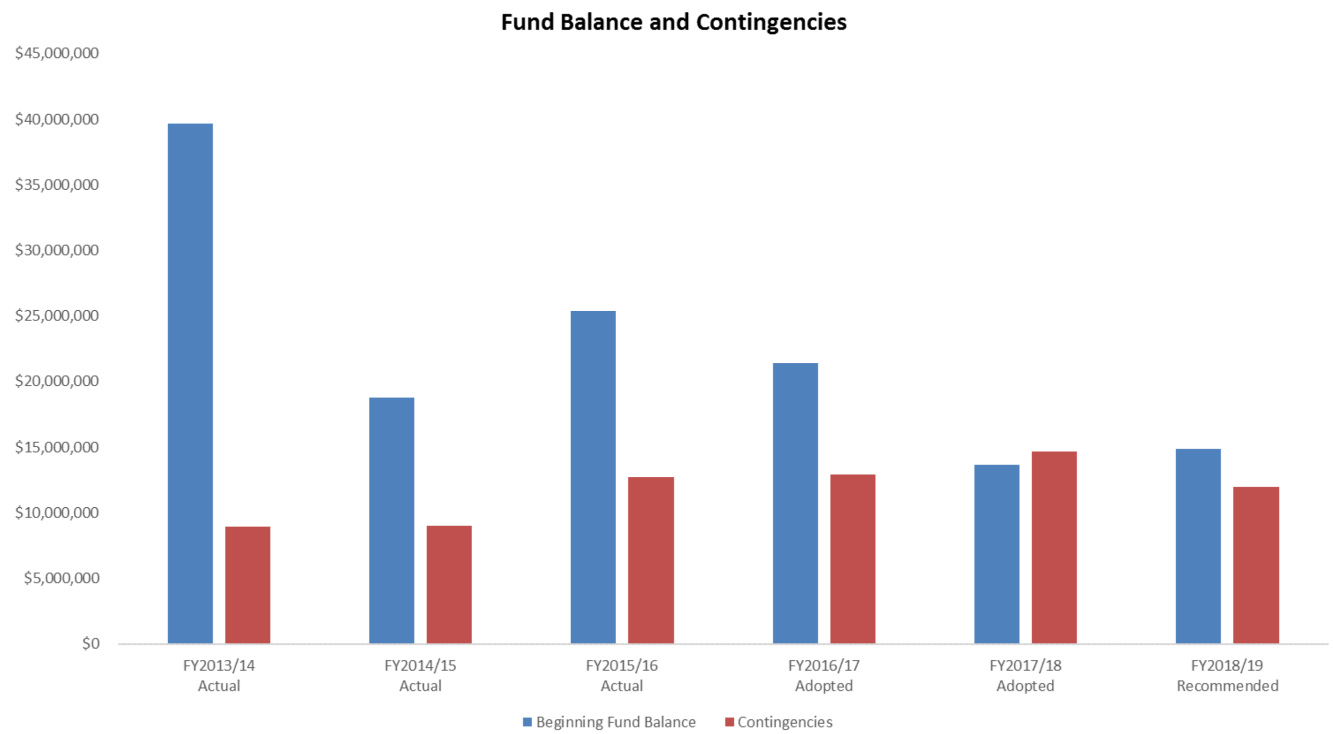
Sources of General Fund Revenue for FY2018/19



## GENERAL FUND RESERVES, DESIGNATIONS & COMMITMENTS AND FUND BALANCE

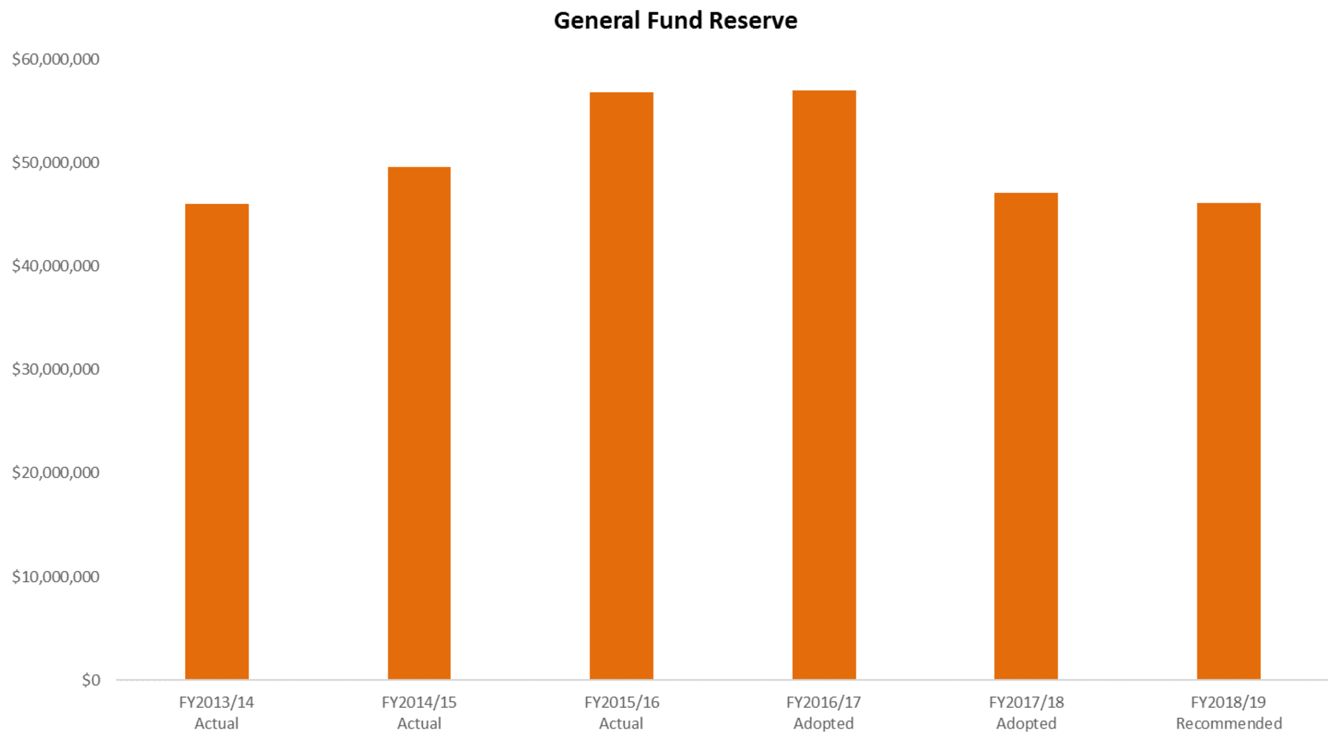
The Board has adopted financial policies and overarching principles intended to position the County to address the range of investments necessary to sustain and provide services. In establishing the Reserves, the County's intent was to draw from these resources and strategically step-down programs to align ongoing expenditures with ongoing revenues. However, in the past, the rate of decline in County revenues outpaced projections. At the same time, the State implemented changes in program responsibilities and funding in criminal justice, health care and Social Services Programs, and dissolved redevelopment agencies. These changes provided one-time revenues that augmented cost containment efforts, which allowed the County to direct resources back to these funds to ensure a sustainable source of funds to help manage future known and unknown fiscal exposures.

In better economic times the Board consciously set monies aside to fund and finance some of the General Fund obligations, liabilities, and responsibilities. The County has weathered the past few years due to the strong fiscal policies established by the Board and the execution of those policies by the County departments. The establishment of the General Reserve and the funding of the various General Fund Reserves has allowed the County to manage through the economic downturn. A stable economy is anticipated for FY2018/19; however, there are some significant unknowns that will have a financial impact on the County and further cost containment efforts may be necessary. In the following paragraphs, the unfunded obligations and potential liabilities that lie ahead are discussed in connection with the General Fund Reserves, designations and commitments, and Fund Balance.




The Fund Balance at June 30, 2018 is projected at $26.9 million, which includes $12 million for Contingencies.

On February 13, 2007, the Board adopted the General Fund Contingency policy to establish a level equal to 10% of the General Fund total budget. The current recommendation from staff for FY2018/19 is to maintain a $12 million contingency amount within the General Fund which is approximately 4% of Proposed General Fund Expenditures, reduced from $14.7 in FY2017/18. Appropriations for Contingencies are legal authorizations granted by the Board of Supervisors to be used for one-time unexpected needs that arise outside of the regular budget planning process. Pursuant to Government Code §29130, access to the Appropriation for Contingency requires a 4/5 vote of the Board of Supervisors.




Per Board policy outlined in the Budget Construction and Legal Requirements section of the FY2018/19 Recommended Budget the General Fund General Reserve will be maintained at a level equal to 10% of the County's total budget excluding inter-fund transfers, with a minimum balance of $20 million at all times. This level will be maintained to provide the County with sufficient working capital and a comfortable margin to support one-time costs for the following purposes:

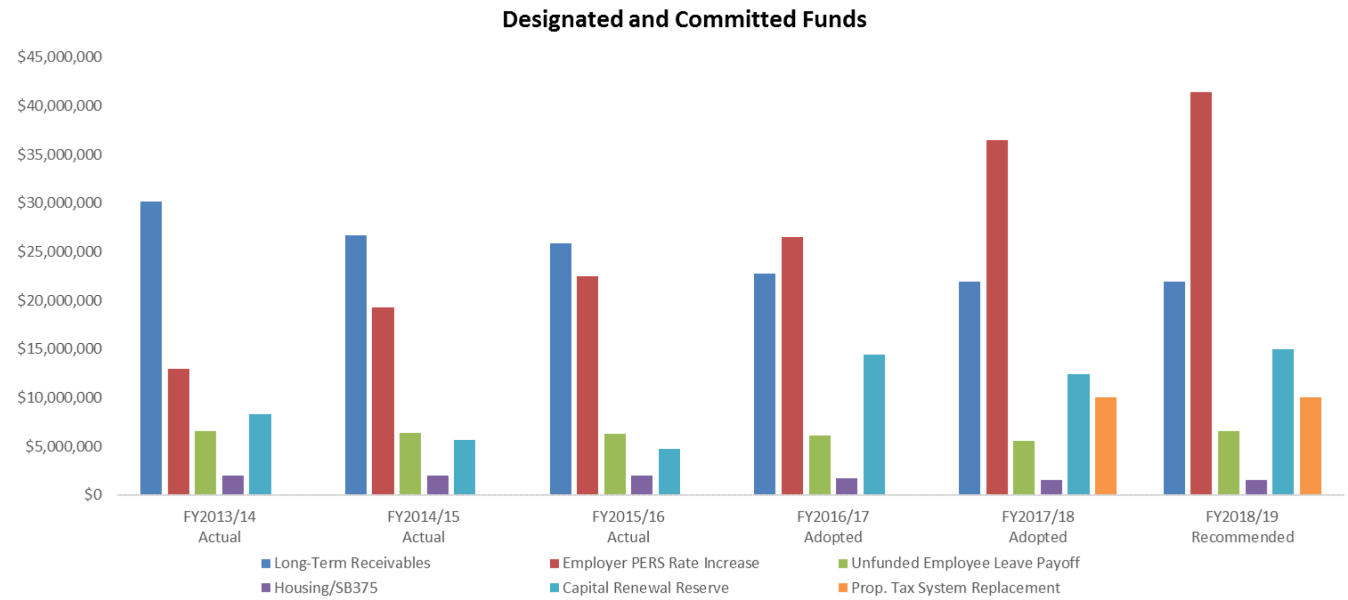
- When the County faces economic recession/ depression and the County must take budget action.
- When the County is impacted by a natural disaster or any other emergency.
- When the County experiences unexpected declines in revenues and/or when unpredicted large one-time expenditures arise.

In circumstances where the General Fund General Reserve has fallen below the established level, the County shall replenish the deficiency within five fiscal years or as soon as economic conditions allow from the following revenue sources: year-end surpluses, non-recurring revenues, or if legally permissible and with a defensible rational, from excess resources in other funds.

Subject to the Board of Supervisors' restrictions, the following will guide how the General Fund General Reserve should be used:

1. Use the General Fund General Reserve to phase into fiscal distress periods gradually, focusing on maintaining the Board's priorities.
2. To the extent possible, use the General Fund General Reserve as the last resort to balance the County Budget.
3. To the extent possible, the spending down of the General Fund General Reserve should not exceed $6 million a year (Board of Supervisors' policy direction on February 13, 2007).
4. The General Fund General Reserve should not be used to support recurring operating expenditures.
5. The General Fund General Reserve is subject to restrictions imposed by Government Code §29086, which limits the Board's access to the General Reserve during the annual budget process and requires 4/5 vote by the Board.

The FY2018/19 Recommended Budget for the General Fund General Reserve is projected at $46.1 million. Based on Board policy the reserve target should be maintained at 10% of the County's total budget, excluding Interfund transfers, which calculates to be $82.1 million in FY2018/19. At the current reserve of $46.1 million the County has funded the General Reserve at 56% of its target goal.




**Employer PERS Rate Increase**

The Employer Public Employee Retirement System (PERS) Rate Increase reserve was established to address both the County's unfunded actuarial accrued liability for the Miscellaneous & Safety Retirement Plans and to position the General Fund to address the future CalPERS rate increases for retirement cost should these rates initially exceed available ongoing revenues, as a means to allow a smoother transition year over year.

Actuarial changes were adopted and implemented by CalPERS beginning in FY2015/16 through FY2019/20 (over a 5-year period) and are expected to continue to increase employer pension rates by as much as 50%. Given that pension rates are expected to increase over the next five years, coupled with a Board of Supervisors stated goal of achieving a retirement funding ratio of 90% for both CalPERS plans (Miscellaneous and Safety), the County Debt Advisory Committee reviewed options to reduce the unfunded liability in FY2014/15. On February 10, 2015, the Committee presented a funding policy to the Board that included placing one-time funds into a Pension Trust to help reduce the unfunded pension liabilities, thereby reducing future employer retirement rates. The Board approved this policy, authorized the creation of an IRS 115 Trust Account, and agreed to fund it with one-time funds in the amount of $20 million at the end of FY2014/15. As of June 30, 2016, (most recent actuarial report), the County's unfunded actuarial accrued liability for both the Miscellaneous Plan and Safety Plan is $545 million (71% Funded Ratio). This figure includes the former court employees and county fair employees.

The FY2018/19 Recommended Budget for the Employer PERS Rate Increases includes both the value of the IRS 115 Trust at $20.5 and the Reserve for Employer PERS Rate Increase at $20.9 million for a total reserve of $41.4 million.

**Capital Renewal Reserve (Deferred Capital/Maintenance Projects)**

In 2007 the Board established a committed Fund Balance for capital renewal/deferred maintenance projects to fund deferred maintenance, unexpected maintenance and/or future maintenance of County facilities. The Board's adopted policies and strategies to address unfunded liabilities center on the need to:

- Replace infrastructure and building systems in aging County facilities where County public services are provided.
- Achieve code compliance in relation to current regulations.
- Effectively manage/reduce the County's risks associated with the programs dispensed from County-occupied buildings.

Annually, through the review and approval of the 5-Year Capital Facilities Improvement Plan (CIP), the Board reviews the status of County building infrastructure, building systems and maintenance needs. The Board weighs these exposures against available resources to determine how to budget for these facility demands.

General Services provided the Board a report titled 2016 Facilities Condition Analysis, prepared by EMG of Walnut Creek (Consultant). The report recommends an annual investment of $7.6 million to maintain County Facilities in "Very Good Condition", while a lower investment of approximately $2.8 million annually will maintain the portfolio within a "Good" range, which is the minimum maintenance level chosen by the Board in order to continue fixed asset protection, preservation and renewal.

In May 2018, the General Services Department presented to the Board a status update on capital projects included in the FY2018/19 Recommended Budget. Based on a preliminary prioritization of projects under consideration, the Department provided recommendations for funding specific projects, some of which will require funding from the Capital Renewal Reserve.

The reserve has a current balance of $13.5 million. It is recommended that the Board utilize $1.5 million of this balance to fund projects in FY2018/19 (see Capital Projects budget for details). In order to provide the annual funding necessary to maintain the County facilities a $3 million increase to the reserve is recommended in FY2018/19 using the one-time revenues projected to be realized based on Midyear projections for 6/30/18. This contribution from FY2017/18 year-end results in the FY2018/19 Recommended Budget for Capital Renewal Reserve of $15 million.

**Property Tax System Replacement**

The Solano County Integrated Property System (SCIPS) is the County's current internally developed and maintained property tax system, originally developed in 1982. On April 4, 2017, the Board of Supervisors authorized staff to proceed with the replacement of the SCIPS system. The total estimated cost to replace the SCIPS system is $10 million and will be completed over multiple years. To fund the replacement system, including the data migration and full implementation the Board authorized the creation of a reserve in FY2017/18 for the project in the amount of $10 million, funded by reclassifying funds from the General Fund - General Reserve. These funds will be a loan to the project, repaid over time once the project is completed.

**Unfunded Employee Accrued Leave Payoff**

In accordance with the Board's Fund Balance Policy, the Board established and maintains a General Fund Reserve for Accrued Employee Leave Payoff. Each year the County assesses the funds necessary to pay for any unanticipated leave payoff that departments cannot absorb with existing appropriations. Based on the County's aging workforce, continued utilization of the Accrued Leave Payoff funds is anticipated in FY2018/19. The FY2018/19 Recommended Budget for the Unfunded Employee Leave Payoff reserve is $6.6 million.

**Long-Term Receivables**

Long-Term Receivables represents amounts outstanding and payable to the County, not available as cash, which cannot be spent because they are either (a) not in a spendable form or (b) legally or contractually required to be maintained intact. It includes long-term loans and notes receivable, inventories and prepaid items. The FY2018/19 Recommended Budget for Long-Term Receivables is $21.9 million.

**Housing/SB 375**

Effective February 1, 2012, the redevelopment agencies (RDA) were dissolved. During the existence of the RDA, a percentage of the redevelopment funding was required to be used to meet the housing needs of low/moderate-income residents. As a result of the dissolution of the redevelopment agencies, this restricted source of funding was no longer available to address housing needs. As of February 1, 2012, any unspent housing funds in RDA's were redistributed to the local taxing agencies as one-time revenues. During this time the State passed SB 375 (Chapter 728, Statutes of 2008) which directed the California Air Resources Board to set regional targets for reducing greenhouse gas emissions. SB 375 included requirements for coordinating regional housing needs allocation with the regional transportation process. In FY2013/14 the Board approved the County Administrator's recommendation to establish the Housing/SB 375 reserve using $2 million of these one-time housing set-aside funds for SB 375 implementation and/or to address temporary and long-term housing needs for children, families, special needs clients, and older, indigent and disabled adults. In FY2018/19 Recommended Budget the current balance in the Housing/SB 375 reserve is $1.6 million.

## OVERVIEW OF THE FEDERAL AND STATE BUDGETS

### Federal Budget Update

In March, Congress approved and President Trump signed into law a long-awaited omnibus appropriations agreement (PL 115-141) that funds the federal government through the remainder of fiscal year 2018. Passage of the nearly $1.3 trillion spending bill brought closure to a months-long budget stalemate that was marked by five short-term funding patches and two brief government shutdowns. In the end, the House cleared the legislation on a 356-167 vote while the Senate passed the bill by a 65-32 margin.

As expected, the spending levels in the omnibus package adhere to the topline numbers set by lawmakers in the recent Bipartisan Budget Act (BBA, PL 115-123). The BBA, which established a two-year budgetary framework, authorized Congress to increase fiscal year 2018 defense and non-defense spending by $80 billion and $63 billion, respectively. All told, the omnibus provides $700 billion for the Pentagon and $591 billion for domestic discretionary programs in the current fiscal year.

While a series of 11th-hour disputes threatened to derail the budget negotiations, Republican and Democratic leaders struck several notable compromises that ultimately allowed a final spending deal to emerge. With regard to immigration and border security, lawmakers agreed to spend $1.6 billion for President Trump's border wall, instead of the $25 billion sought by the White House. Notably, the omnibus restricts the manner in which the funds may be allocated (i.e., the dollars may be used for repairs or secondary fencing where existing barriers are in place along the Southwest border; new barriers would need to be levees or bollard-type fencing). Missing from the package is language that would protect young undocumented individuals currently residing in the U.S.A. from the threat of deportation.

With regard to fiscal year 2019, the Trump administration released in February its spending request for fiscal year 2019 that starts on October 1. The White House budget proposes to exceed the BBA's spending limit for defense programs by nearly $70 billion but would cut domestic discretionary funding by $57 billion when compared to the new BBA caps.

While the president is recommending some program enhancements, the administration would significantly reduce funding for a number of key county programs in fiscal year 2019, including the Supplemental Nutrition Assistance Program (SNAP) and Medicaid. Likewise, the Temporary Assistance for Needy Families (TANF) program, state and local law enforcement grants, state and local Homeland Security and FEMA grants, and renewable energy programs all would be in line for large cuts under the Trump proposed budget. Both Houses in Congress continue to work on the 2019 Budget appropriations, but with the midterm elections it will likely be Fall 2018 before final actions are taken.

Below are highlights of the final FFY18 budget agreement from March 2018.

**Health and Human Services**

The omnibus appropriations Act provides significant spending increases for several key HHS programs, including the Child Care and Development Block Grant. Under the legislation, child care funding will receive a $2.4 billion boost, nearly doubling the program to $5.2 billion.

The omnibus appropriations Act also increases funding for opioid treatment and intervention programs by $2.55 billion, bringing total FFY18 funding to $3.6 billion. Within that total, the legislation provides: $415 million to expand behavioral health and substance use disorder prevention and treatment services, particularly in rural communities; $1 billion for a new State Opioid Response Grant; and, $40 million for mental health and substance use prevention and treatment for children and families in the child welfare system.

Furthermore, appropriations for incentive payments for adoption and legal guardianships were doubled from $37 million to $75 million. The Child Abuse Prevention and Treatment Act (CAPTA), which assists states in implementing child safety plans, was increased for the first time since fiscal year 2005, rising from $25 million to $85 million. Also receiving an increase in appropriations – from $385 million to $445 million – is the Promoting Safe and Stable Families Act (PSSF), which funds state and county programs that are designed to support at-risk families.

The omnibus also provides increases for the Healthy Start program and the Maternal and Child Health Block Grant ($7 million and $10 million, respectively). Head Start is receiving a $610 million increase for 2018.

Appropriators rejected the Trump administration's proposal to eliminate the Community Services Block Grant (CSBG), the Low-Income Home Energy Assistance Program (LIHEAP), and the Social Services Block Grant (SSBG). Under the final spending bill, CSBG is level funded at $715 million and LIHEAP is increased by seven percent, for a total of $3.6 billion. The SSBG again escaped elimination, receiving flat funding of $1.7 billion.

Due to its entitlement nature, the bill provides $74 billion for Supplemental Nutrition Assistance Program (SNAP), fully funding the program to meet the projected needs of all eligible individuals. Finally, the Women, Infants and Children (WIC) program is fully funded at $6.2 billion, which is based on USDA projections of program enrollments.

Family First Prevention Services Act

Despite a glaring lack of stakeholder input and public hearings, the text of the Family First Prevention Services Act (FFPSA) was included in the aforementioned BBA. The measure, which was strongly opposed by Solano County and other California stakeholders, will require the State and counties to revamp key processes under California's Continuum of Care Reforms. The end result will be significant cost shifts to the State and counties.

In 2018 and beyond, FFPSA implementation will place additional requirements on the assessment of youth for placement in congregate care facilities, as well as institute costly new requirements for the programs to operate with licensed nursing staff on call at all hours of the day (even if the program is not serving children with significant medical needs). In general, the FFPSA will restrict the number of youth who could be served in short-term residential treatment programs and reduce federal funding supporting them. The new law does allow states to request a delay in implementation of up to two years – from October 2019 until October 2021. However, it does not extend the state's child welfare waiver, which expires on October 1, 2019.

Children's Health Insurance Program (CHIP)

Funding for the CHIP program was recently extended by Congress for a total of 10 years. It should be noted that the program extension phases down the Affordable Care Act's (ACA) enhanced federal matching rate for CHIP coverage. Beginning in fiscal year 2020, the ACA's 88 percent federal match rate for California will be reduced to 76.5 percent. In fiscal year 2021, the rate will return to its pre-ACA level of 65 percent.

ACA Tax on High-Cost Health Insurance Plans

The ACA's so-called "Cadillac Tax" was postponed for an additional two years, until 2022, under a recent Continuing Resolution (PL 115-120). Pursuant to the ACA, a 40 percent excise tax is imposed on high-cost health insurance plans, which many public employers, including counties, offer to their employees. With the excise tax costs expected to rise over the years as health care expenses increase, the burden on county budgets could be significant.

**Water Resources**

Solano Project – The final FFY18 budget fully funds the Solano Project, which includes: $2.367 million for facility operations; and, $1.329 million for management of the recreation area at Lake Berryessa.

CALFED Bay-Delta Restoration – The omnibus provides $37 million for California Bay-Delta Restoration, a $1 million increase from the FY 2017 enacted level.

WIIN ACT Funding – Congress provided $134 million for water storage projects authorized in the Water Infrastructure Improvements for the Nation (WIIN) Act. With regard to California, the federal funds will partially match Proposition 1 storage dollars for the following projects: design and pre-construction work on the Shasta Reservoir project; feasibility study completions for the Sites Reservoir and the Temperance Flat Reservoir; and, initiation of a feasibility study to address subsidence on the Friant Kern Canal.

Clean Water and Drinking Water State Revolving Funds – The Clean Water State Revolving Fund and the Drinking Water State Revolving Fund will both receive an additional $300 million in funding in fiscal year 2018. These programs provide federal financial assistance for the construction of drinking water and wastewater infrastructure and treatment facilities.

**Transportation**

Federal-aid Highway Program – Consistent with the terms of the Fixing America's Surface Transportation (FAST) Act, the FY18 omnibus provides $45 billion for the Federal-aid Highway program, or a $1 billion boost compared to fiscal year 2017. The legislation also provides an additional $2.5 billion in discretionary funding for roads and bridges, bringing total federal highway spending to approximately $47.5 billion in fiscal year 2018.

BUILD Transportation Discretionary Grants - The Appropriations Act appropriates $1.5 billion to be awarded by the U.S. Department of Transportation for National Infrastructure Investments. This program was previously known as the Transportation Investment Generating Economic Recovery, or TIGER Discretionary Grants program, and is now known as the Better Utilizing Investments to Leverage Development, or BUILD Transportation Discretionary Grants program. Funds for the FY 2018 BUILD Transportation program are to be awarded on a competitive basis for projects that will have a significant local or regional impact.

Capital Investment Grants – The Capital Investment Grants program is a competitive discretionary grant program that funds major transit capital projects including heavy rail, light rail, commuter rail, bus rapid transit projects, and streetcars. The FY18 spending bill includes an additional $232 million for the program, bringing total spending to just over $2.6 billion.

Consolidated Rail Infrastructure and Safety Improvement Grants – The omnibus includes an additional $525 million for grants to improve the safety, efficiency, and reliability of passenger and freight rail systems. These competitive funds have supported a wide range of projects, including safety efforts like reducing grade crossing incidents.

**Housing and Urban Development (HUD)**

Community Development Block Grant (CDBG) – Lawmakers agreed to fund the CDBG program at $3.3 billion, or a $300 million increase above fiscal year 2017 levels.

Choice Neighborhoods Program – The omnibus includes an additional $12.5 million for the Choice Neighborhoods program in FY18, bringing total spending to $150 million. The program provides competitive planning and implementation grants to improve neighborhoods with distressed public and/or assisted housing.

HOME Investment Partnerships Program – The HOME program is receiving an additional $412 million in FY18, increasing total spending to over $1.3 billion. HOME provides flexible formula grants to local governments to expand the supply of affordable housing for low-income households.

Homeless Assistance Grants – The budget includes $2.5 billion for Homeless Assistance Grants, a $130 million increase over FFY17 spending. Pursuant to the final omnibus, $80 million of the $2.5 billion is allocated to address youth homelessness.

**Justice Funding**

State Criminal Alien Assistance Program (SCAAP) – The final budget provides $240 million for SCAAP, or a $30 million increase. The boost in funding represents the single largest annual increase in the program since fiscal year 2006.

Byrne Justice Assistance Grants (JAG) – JAG, which is the primary source of flexible federal criminal justice funding for state, local, and tribal jurisdictions, is set to receive $416 million in FY18, a $13 million boost. Of that amount, roughly $340 million is available for traditional JAG grants.

Victims of Crime Act (VOCA) – The omnibus sets the amount of funding for programs authorized under VOCA at roughly $4.4 billion, an increase of more than $1.8 billion.

Funding to Combat Opioid Abuse – The final budget directs $447 million for DOJ grant programs to help stem opioid abuse, including funds for drug courts, treatment, prescription drug monitoring, heroin enforcement task forces, overdose reversal drugs, and at-risk youth programs. The funding represents a nearly $300 million increase for opioid-related grant programs.

COPS Hiring Program – The omnibus provides nearly $226 million in COPS hiring grants. Within this total, $30 million is designated for Tribal Resources Grants, $10 million is for Community Policing Development, and $36 million will be used for the Regional Information Sharing System. As a result, local governments will be able to compete for approximately $150 million in traditional COPS hiring grants, compared to $137 million available in FY17.

**State Budget Update**

On January 10, 2018 the Governor presented his initial FY2018/19 budget plan to the Legislature. His budget proposal included estimated State General Fund revenues to be about $127 billion in FY2017/18 and roughly $130 billion in FY2018/19, and the Governor proposes to spend $131.7 billion from the General Fund in FY2018/19. There are also $56.1 billion in Special Funds and $2.5 billion in Bond Funds, increasing the overall size of the budget to a total of $190.3 billion. The FY2017/18 fiscal plan reflects a one-time surplus. Proposed General Fund spending is increased by approximately $9.2 billion this year as compared to FY2017/18.

Continuing his emphasis on fiscal prudence, Governor Brown proposes to fully fund the Rainy-Day Fund, which was established by the approval of Proposition 2 in 2014, which set a constitutional goal of reserving 10% of tax revenues. By the end of the current fiscal year, the Rainy-Day Fund will have $8.4 billion, or 65% of the target. The Proposed Budget includes a $3.5 billion supplemental payment in addition to the constitutionally required transfer, bringing the total Rainy-Day Fund to $13.5 billion. In May of 2011, Governor Brown identified $35 billion in debts, deferrals and budgetary obligations. That debt has been reduced since then, currently standing at less than $6 billion.

The FY2018/19 Proposed Budget continues to fund poverty-focused programs, including:

- The rising state minimum wage, which increased to $11 per hour in 2018 and is scheduled to eventually reach $15 per hour
- The restoration of health benefits to low-income Californians that were eliminated during the recession, including adult dental services
- The state's first Earned Income Tax Credit and its recently expanded coverage
- The increased CalWORKs grants and the repeal of the maximum family grant rule
- The increases in child care and early education provider rates and the number of children served

Governor Brown's Budget proposes to extend the California Competes tax credit program for another five years, with $180 million in credits awarded annually.

**Health and Human Services**

The Proposed Budget includes $155.7 billion ($37.4 billion General Fund and $118.3 billion other funds) for health and human services programs.

Ongoing Implementation of Medi-Cal and Children's Health Insurance Program (CHIP) - Since 2011, the number of Californians receiving coverage through Medi-Cal and CHIP has increased from 8.5 million to nearly 13.5 million, including the expansion of full medical coverage to undocumented children. Additionally, 1.3 million people receive medical coverage through Covered California.

Tobacco Tax Increase (Proposition 56) - Approved in 2016, the California Healthcare, Research, and Prevention Tobacco Tax Act of 2016 (Proposition 56) raises the tax on cigarettes from $0.87 to $2.87 per pack and expands this tax to electronic cigarettes. Estimated revenues for FY2018/19 are $1.3 billion. The Proposed Budget allocates $649.9 million in FY2018/19, an increase of $232.8 million, for supplemental payments and rate increases based on those approved in the 2017 budget package. Of the increased amount, about $163 million is for physician payments and $70 million is for dental payments.

Department of Health Care Services (DHCS) - After accounting for Proposition 56 funds, Medi-Cal General Fund spending is projected to increase 11% from $19.5 billion at the 2017 Budget Act to $21.6 billion in FY2018/19. Medi-Cal is projected to cover nearly 13.5 million Californians in FY2018/19. SB 28 (Chapter 244, Statutes of 2013) required DHCS to develop and implement a new budgeting methodology for Medi-Cal county administration base costs. Due to limited responses to the request for proposal, DHCS was unable to procure a qualified vendor. As an interim solution, the Budget proposes an increase of $54.8 million ($18.5 million General Fund) in FY2018/19 based on an adjustment to the existing funding level using the California Consumer Price Index. A similar increase will be used for two years as the county eligibility systems move to a single Statewide Automated Welfare System. DHCS will work with the County Welfare Directors Association to improve processing of eligibility determinations and annual redeterminations, correct beneficiary aid codes, and produce timely data and reports.

2011 Realignment Funding - Proposed FY2018/19 expenditures for 2011 realignment funding includes funding for mental health and support services.

Department of Social Services (DSS) - The Proposed Budget includes $24.2 billion ($8.6 billion General Fund) for DSS in FY2018/19.

The Governor's Budget proposes $238.2 million ($179.7 million General Fund) to continue implementation of Continuum of Care reforms for youth in the foster care program. Assumptions on caseload movement were revised to more accurately reflect the pace of implementation. In FY2018/19, county child welfare and probation departments will work to increase the availability of home-based family care and determine the local need for Short-Term Residential Therapeutic Programs as group home licenses expire and residential congregate care placements decline.

CalWORKs Program - The CalWORKs program is California's version of the federal Temporary Assistance for Needy Families (TANF) program, which provides temporary cash assistance to low-income families with children to meet basic needs and welfare-to-work services so families may become self-sufficient. Counties have flexibility in program design, services, and funding to meet local needs.

Total TANF expenditures are $7.4 billion (state, local, and federal funds) in FY2018/19, including $5.1 billion for CalWORKs program expenditures and $2.3 billion in other programs, such as for Cal Grants, Department of Education Child Care, Child Welfare Services, Foster Care, Department of Developmental Services programs, the Statewide Automated Welfare System, Work Incentive Nutritional Supplement, California Community Colleges Child Care and Education Services, and the Department of Child Support Services. The average monthly CalWORKs caseload is estimated to be 401,000 families in FY2018/19, an 11% decrease from the 2017 Budget Act projection.

The following adjustments are proposed:

- $26.7 million for a voluntary Home Visiting pilot program, which will continue through 2021 for young, first-time parents in the CalWORKs program. Home visitors will help parents navigate and connect to resources in the CalWORKs program and other available services, and report case progress and outcomes to the county. DSS will work with counties to establish outcome measures so the initiative can be evaluated for effectiveness. $158.5 million in one-time TANF funds is reserved for the pilot's costs through calendar year 2021.
- The Proposed Budget includes a one-time augmentation of $187 million for the county single allocation until a revised budgeting methodology is adopted to address the cyclical nature of the caseload changes and impacts to county services. The Brown Administration will continue to work with county representatives and the County Welfare Directors Association to develop recommendations for revising the methodology by the May Revision.
- County savings related to federal health care reform are estimated to be $657.1 million in FY2017/18 and $530.5 million in FY2018/19. The Proposed Budget includes a one-time General Fund decrease of $231.2 million in the CalWORKs program resulting from additional FY2015/16 County savings. The statewide indigent health savings were higher than previously estimated based on the preliminary reconciliation of FY2015/16, and the Proposed Budget assumes reimbursement of this amount from the counties in FY2018/19. The estimated savings will be updated in the May Revision based on audited data from the counties. These additional county savings are redirected to the CalWORKs program to offset General Fund costs.

In-Home Supportive Services (IHSS) - The Proposed Budget includes $11.2 billion ($3.6 billion General Fund) for the IHSS program in FY2018/19, a 7.7% increase in General Fund costs over the revised FY2017/18 level. Average monthly caseload is project to be 545,000 recipients in FY2018/19, a 5.4% increase from the 2017 Budget Act projection.

The following adjustments are proposed:

- IHSS Administration – The conclusion of a $27.8 million General Fund increase in FY2018/19 for county IHSS administrative costs to reflect revised workload and budget assumptions.
- IHSS Provider Paid Sick Leave – The inclusion of $29.9 million General Fund to implement eight paid sick leave hours for IHSS providers beginning on July 1, 2018.

Incompetent to Stand Trial Admissions - IST admission referrals from local courts are outpacing bed capacity in the state hospital system. The Proposed Budget includes $117.3 million ($114.8 million General Fund) to further develop the state-county partnership to address the growing number of IST commitments referred to the Department of State Hospitals. Nearly $100 million General Fund will be available over three years for community alternatives to increase diversion of mentally ill offenders and decrease county IST referrals to state hospitals. The Administration's goal is to strengthen existing local mental health treatment efforts, develop or enhance robust diversion programs, and reduce IST referrals by up to 30%.

The program will prioritize contracts with the 15 counties that have the majority of IST referrals to develop and expand diversion programs to support up to 640 placements (Solano County is one of the 15 counties identified in the legislation). These funds will also be used for up to 60 additional community placements in other counties. The Proposed Budget includes $2.5 million per year from Mental Health Services Act funds for the Mental Health Services and Accountability Commission to provide two years of consulting services to assist counties in developing Innovation Plans that incorporate ways to leverage and coordinate diversion programs to address IST populations.

The Department of State Hospitals will also continue to work with counties to identify other opportunities for collaboration, efficiencies, and approaches in treating IST patients.

The following adjustments are proposed:

- $16.1 million General Fund to allow the Department to contract for up to 159 beds through existing and new county jail treatment programs

Housing & Homelessness - The Budget continues the Administration's commitment to improving existing programs and maximizing its investment in housing. To implement the significant changes included in the 2017 statewide housing legislative package, the Budget allocates $3 million General Fund to the Department of Housing and Community Development in addition to resources from an estimated $258 million in real estate transaction fee revenue for housing programs and proceeds from the housing bond that will be available upon voter approval in the November 2018 election.

The Veterans and Affordable Housing Bond Act of 2018 proposes a $4 billion bond on the November 2018 ballot. The first $3 billion of the bond will support various existing housing programs, including affordable multifamily housing, farmworker, transit-oriented development, infill infrastructure, and homeownership programs, as well as matching grants for Local Housing Trust Funds. These funds are anticipated to be awarded over five years. The remaining $1 billion will be available to support home ownership for veterans, with down payment assistance, reduced fees and closing costs, and competitive interest rates.

The Budget includes $277 million local assistance for the Multifamily Housing Program, assuming passage of the Veterans and Affordable Housing Bond Act of 2018. The Multifamily Housing Program assists with new construction, rehabilitation, and preservation of permanent and transitional rental housing for lower-income households.

**Public Safety**

The FY2018/19 State Budget proposes total funding of $12 billion ($11.7 billion general fund and $313 million in other funds) for the Department of Corrections and Rehabilitation. The budget estimates that there will be a 2.1% increase in the adult inmate population and a decrease in the adult parolee population of 0.6% compared to 2017 budget projections.

$16 million general fund for the Statewide Prison to Employment Initiative which will provide services for regional and local planning and implementation to integrate reentry and workforce services to the formerly incarcerated. This initiative is designed to accelerate the alignment of correctional education, training, and increased workforce system collaboration.

$3.8 million general fund is included to establish two housing units to support a Young Adult Offender Pilot Program that would divert a limited number of young adult offenders who have committed specified crimes from adult prison to a juvenile facility.

The Budget includes $106.4 million to continue the Community Corrections Performance Incentive Grant program

The Budget includes $29 million general fund for county probation departments to supervise the temporary increase in the population of offenders on Post-Release Community Supervision as a result of the implementation of Proposition 57.

The Department of Finance estimates net savings of $64.4 million for Proposition 47 when comparing FY2017/18 budget to 2013-2014. Ongoing savings are estimated to be approximately $69 million. These funds will be allocated according to the formula outlined in the initiative.

The Administration is working with the State Attorney General's office on a funding proposal to be released in the Spring to implement SB 384 which replaces the existing lifetime sex offender registration system with a tiered registration system beginning on January 1, 2021.

Cannabis Regulation - The Brown Administration is deferring all cannabis-related budget proposals until the May 2018 Budget Proposal Revision.

**General Local Government**

The Budget includes $23.7 million General Fund to backfill the property tax revenue losses that cities, counties, and special districts will incur in FY2017/18 and FY2018/19 due to the October 2017 wildfires in Northern California. This funding estimate will be adjusted as part of the May Revision as more information becomes available from county assessors. This adjustment will also include backfills for the property tax revenue losses incurred by cities, counties, and special districts in FY2017/18 and FY2018/19 due to the Southern California wildfires that started in December 2017. Reliable estimates of the property tax impact of those fires were not available when the Budget was finalized.

The wildfire-related property tax revenue losses incurred by K-14 schools are generally automatically backfilled under the Proposition 98 school funding mechanism. The Budget estimates K-14 schools will incur $24.5 million in cumulative property tax revenue losses in FY2017/18 and FY2018/19 due to the Northern California wildfires.

The winding down of the state's former redevelopment agencies continues to be a priority for the Administration. The Budget notes that the elimination of redevelopment agencies “has allowed local governments to protect core public services by returning property tax money to cities, counties, special districts, and K-14 schools.”

From FY2011/12 through FY2016/17, approximately $2.1 billion was returned to cities, $2.6 billion to counties, and $781 million to special districts. The Budget anticipates that cities will receive an additional $926 million in general purpose revenues in FY2017/18 and FY2018/19 combined, with counties receiving $990 million and special districts $282 million.

The Budget anticipates that average annual property tax revenues of more than $1.2 billion will be distributed to cities, counties, and special districts through FY2021/22. The Budget states that this is “a significant amount of unrestricted funding that can be used by local governments to fund police, fire, housing, and other public services.”

The Administration sponsored Chapter 785, Statutes of 2014 (SB 628), which restored the ability of cities and counties to use tax increment financing for local development initiatives. The bill allows cities and counties to create Enhanced Infrastructure Financing Districts. Unlike the redevelopment agencies, Districts can only leverage property tax revenues from cities, counties, and special districts that agree to participate and cannot leverage property tax revenues from K-14 schools.

The Budget reflects the first $1.3 billion in natural resources and housing infrastructure spending from the bonds passed by the Legislature last year (SB 5), assuming passage by the voters in 2018.

**Cap and Trade**

The Governor’s FY2018/19 Proposed Budget acknowledges that the market for Cap and Trade auction allowances has rebounded since the passage of AB 398 (Garcia) [Chapter 135, Statutes of 2018].

The Proposed Budget notes that there will be $1.25 billion in Cap and Trade auction proceeds available for appropriation in FY2018/19, but does not offer a specific Cap and Trade Expenditure Plan as in past years.

**Water**

The Governor’s FY2018/19 Proposed Budget includes the following adjustments to the Sustainable Groundwater Management Act (SGMA):

- $61.8 million from SB 5 funds for DWR to support SGMA implementation by:
  - Providing technical assistance to aid in the development and evaluation of plans.
  - Supplementing existing planning grants to support a groundwater sustainability agency’s responsibility to define a path to achieve sustainable groundwater management.
  - Providing grants directly supporting the implementation of groundwater projects.
- $84 million from SB 5 funds for the State Water Board to support regional groundwater treatment and remediation activities that prevent or reduce contamination of groundwater that serves as a source of drinking water, including $10 million for technical assistance for drought and groundwater investments.

The Proposed Budget also includes $98.5 million from SB 5 funds for multi-benefit flood control projects that achieve public safety and fish and wildlife improvements, as well as funding for a new Floodplain Management, Protection, and Risk Awareness Program to protect California’s alluvial fan, coastal, and riverine floodplains. This funding seeks to support an integrated system-wide approach to flood management and implementation of the Central Valley Flood Protection Plan.

The Proposed Budget establishes a new special fund for the State Water Board to assist communities, particularly disadvantaged communities, in paying off the short-term and long-term costs of obtaining access to safe and affordable drinking water.

The Governor's Budget proposes $4.7 million in FY2018/19 for the State Water Board and the Department of Food and Agriculture to take steps toward implementation of this new program, including:

- Developing and implementing fee collection systems.
- Conducting an assessment to estimate the level of funding needed to assist water systems to ensure the delivery of safe and affordable drinking water.
- Developing and making available a map of high-risk aquifers used as drinking water sources.

**Transportation**

The FY2018/19 Governor's Budget represents the first full year of new revenues from Senate Bill 1 (Beall and Frazier). According to the Governor's Budget Summary, over the next decade, the $55 billion transportation package will provide $15 billion for state highway repairs and maintenance, $4 billion in state bridge repairs, $3.3 billion for state trade corridors, and $2.5 billion for the state's most congested commute corridors.

Local roads will receive more than $15 billion in new funding for maintenance and repairs and $2 billion in matching funds for local partnership projects. Transit and intercity rail will receive $7.6 billion in additional funding, and local governments will have access to $1 billion for active transportation projects.

## ECONOMIC RISKS

Nationally

Based on *The Budget and Economic Outlook: 2018 to 2028* published by the Congressional Budget Office in April of 2018, the federal governments recently enacted 2017 Tax Cuts and Jobs Act, Bipartisan Budget Act of 2018 and the Consolidated Appropriations Act, 2018 have direct impacts on the economy in the short and long term. In the short term, these legislations provide fiscal stimulus to individuals and businesses, continue to raise the Gross Domestic Product (GDP), and increase domestic output. In the long term, it is speculated that the budget deficit will continue to rise triggering higher interest rates, a rise in consumer prices, slower growth in federal outlays, and dampened economic growth and possible recession starting in 2020. US output continues to grow at a faster pace than in previous years adding to existing momentum in spending on goods and services. This growth, tracked as the GDP, continues to push the unemployment rate down to historic lows. Economic growth is projected to begin to move from relatively strong in 2018 and 2019 to moderate in 2020 and beyond. A surging federal budget deficit is expected to result in 1 to 2 more interest rate hikes in 2018. Currently, the U.S. economy is in its second longest period of economic expansion in history as businesses and individuals take advantage of current opportunities. For the global economy, the majority of world markets have moved out of recession and are either in a recovery (South America and Europe) or expansion (US and India) mode with China and the United Kingdom in a slowdown cycle.

Federal Tax Reform Bill-Now Law

In December 2017, Congress approved a major tax reform package (HR 1-Tax Cuts and Jobs Act) that represents the first major overhaul of the U.S. tax code in over three decades. This legislation was signed by President Trump on December 22, 2017. Among other things, this law will preserve the seven-rate structure for individuals, while modifying the marginal tax rates. In addition, HR 1 (now public law 115-97) nearly doubles the standard deduction and expands the Child Tax Credit. However, the measure also eliminates the personal exemption, which is currently valued at $4,050 per person. Furthermore, in an effort to simplify the code and increase revenues, the legislation eliminates or caps a number of tax deductions and credits. With regard to businesses, the corporate tax rate is reduced from 35 percent to 21 percent, beginning in 2018. It should be noted that many of the individual tax provisions, including those for small businesses, will expire at the end of 2025, while many of the corporate tax components are made permanent. The law allows taxpayers to deduct property taxes *and* income or sales taxes up to a combined cap of $10,000; fully preserves the tax-exempt status of municipal bonds but eliminates advance refunding bonds. Finally, the law repeals the penalties used to enforce the *Affordable Care Act's* (ACA) individual mandate. This tax reform package may impact the long term discretionary spending of California residents due to changes in the federal deductions allowed for personal federal tax returns effective 2018.

California

In the May Revise of the FY2018/19 California State Budget, Governor Jerry Brown proposes a $138 billion budget which includes increased revenues of $8 billion when compared to the January Budget, predominantly from unprecedented increases in capital gains. Strong gains in revenues from state income taxes are tied to rises in capital gains tax as a result of the rising Stock Market. This represents potential volatility to the state's income tax revenue should the Stock Market reverse trend and head downwards. This volatile revenue source is expected to remain historically high through 2022. The Governor continues to channel these additional revenues into the Rainy-Day Fund and a commitment to one-time spending in an effort to prepare for future recessions. This one-time General Fund spending will be primarily focused on funding for Infrastructure ($2 billion), Homelessness ($359 million) and Mental Health ($312 million) coupled with the overarching goals of paying down debts and liabilities, strengthening infrastructure, combating climate change, counteracting the effects of poverty and more money for schools. (Source: Governor Brown's May Revise). The state's unemployment rate of 4.3% is at a record low driven by stronger than expected job growth and slower population growth. The combination of a booming economy and insufficient home and apartment construction has escalated home and rent prices which has contributed to rising homelessness. The current federal administration's efforts to upend longstanding trade arrangements could threaten the state's economy, home of the United States' largest port complex in southern California.

Staff will continue to monitor state and federal budget developments and consider them in light of managing the County's budget.

## FY2018/19 GENERAL FUND RECOMMENDED BUDGET

The County's FY2018/19 Recommended Budget for the General Fund of $268.9 million is balanced with revenues of $240.6 million, drawdowns from committed fund balances of $1.5 million for Capital Renewal Reserve and use of Fund Balance ($26.9 million).

The Recommended Budget for General Fund reflects revenues of $240.6 million an increase of $14.4 million excluding reserves when compared to the FY2017/18 Adopted Budget of $226.2 million. The increase in revenues is attributed to an anticipated net increase in Tax Revenues, including taxes driven by the assessed roll changes, and local sales and use taxes and other tax revenue totaling $9 million primarily due to improved property values and an increase of $5.4 million primarily for charges for services for administration overhead and various permits and services.

The Recommended Budget for General Fund reflects appropriations of $248.1 million an increase of $11.4 million excluding transfers to reserves and contingencies when compared to the FY2017/18 Adopted budget of $236.7 million. The increases in appropriations is attributed to increases in General Fund departments of $3.9 million in labor costs and $1.1 million in services, supplies, other charges and fixed assets, and net increases in General Fund contributions to other funds of $6.4 million primarily due increasing costs in Public Safety and Health and Social Services when compared to the FY2017/18 Adopted Budget.

The Recommended Budget for General Fund including reserves which totals $268.9 million, reflects decreased General Fund appropriations when compared to the FY2017/18 Adopted Budget of $273.4 million. The net decrease of $4.4 million is primarily due to reduced transfers to reserves and contingencies in FY2018/19, including the one-time transfer of $10 million from the General Fund – General Reserves to a new Reserve for the Property Tax System Replacement project in FY2017/18. These decreases are partially offset by increases in appropriations in General Fund departments, primarily reflecting increased labor costs and increased General Fund contributions to both Public Safety and Health and Social Services when compared to FY2017/18 Adopted Budget.

## GENERAL FUND FISCAL PROJECTIONS

Solano County uses Fiscal Projections to provide insight into future trends for General Fund Revenues and Expenditures. Doing so allows the County to work proactively with departments to address potential program impacts in future years.

The fiscal projections shown in the table that follows reflect the FY2017/18 Midyear projections for comparison only. Using the FY2018/19 Recommended Budget as the starting point, revenues and expenditures are forecast through FY2020/21. While projections beyond 2021 are possible, it is more difficult to provide a meaningful longer forecast in light of the changing economic dynamics and an uncertain Federal Budget.

**Solano County**
**General Fund - Fiscal Projection**
**FY2018/19 Recommended Budget**
**(in million of dollars)**

| | | Midyear Projection For 6/30/18 | Recommended Budget FY2018/19 | Projected Budget FY2019/20 | Projected Budget FY2020/21 |
|---|---|---|---|---|---|
| a | **General Fund, Beginning Balance** | $ 28.40 | $ 26.88 | $ 12.00 | $ 11.39 |
| | TO Reserves: | | | | |
| | General Reserves | | | | |
| | Unfunded Employee Leave Payoff | (0.492) | (1.000) | | |
| | Capital Renewal Reserve | (5.874) | (3.000) | | |
| | Employer CalPERS Rate Increases | (5.629) | (4.808) | | |
| | Property Tax System Replacement | (10.000) | | | |
| b | Subtotal - TO Reserves | (21.995) | (8.808) | 0.000 | 0.000 |
| | FROM Reserves: | | | | |
| | General Reserves | 10.000 | | | |
| | Unfunded Employee Leave Payoff | 1.000 | | 0.800 | 0.800 |
| | Capital Renewal Reserve | 7.768 | 1.465 | 2.000 | 2.000 |
| | Employer CalPERS Rate Increases | | | 4.000 | 4.000 |
| | Encumbrances | 0.732 | | | |
| c | Subtotal - FROM Reserves | 19.500 | 1.465 | 6.800 | 6.800 |
| d | **Net Increase (Decrease) in Funding Sources: (b+c)** | (2.495) | (7.343) | 6.800 | 6.800 |
| e | **TOTAL AVAILABLE FINANCING (a+d)** | 25.905 | 19.538 | 18.802 | 18.190 |
| f | Operating Expenditures (excluding Contingencies/transfers to Reserves) | 234.612 | 248.132 | 252.133 | 261.293 |
| g | Contingencies | 0.000 | 12.000 | 9.000 | 9.000 |
| h | **Total Operating Expenditures** | 234.612 | 260.132 | 261.133 | 270.293 |
| i | Operating Revenues (excluding transfers from Reserves) | 232.118 | 240.596 | 244.721 | 252.779 |
| j | Operating Expenditures (excluding Contingencies/transfers to Reserves) | 234.612 | 248.132 | 252.133 | 261.293 |
| k | **Net operating Revenues over (under) Expenditures [known as Operational Deficit] (i-j)** | $ (2.494) | $ (7.536) | $ (7.412) | $ (8.514) |

***** General Fund, Beginning Balance in FY2018/19 includes estimated additional savings from County Departments and the anticipated one-time release of funds impounded from property tax as projected at Midyear. FY2019/20 and FY2020/21 are anticipated to be higher than shown in chart above based on historical trends in savings realized in departments. Contributions to Reserves are not included in FY2019/20 and beyond.

**Revenue Assumptions - From General Revenue Projections**:

The County's General Fund Budget is financed with General Revenues (refer to BU 1101), the use of certain one-time revenues, Fund Balance, and General Reserves, if necessary. The FY2018/19 Recommended Budget includes the use of General Fund – Committed Fund Balances of $1.5 million from Capital Renewal.

The significant Revenue Assumptions from the General Revenues budget include:

- An estimated 4% increase in assessed values from the FY2017/18 corrected assessment roll, the following increases are projected: $5.3 million in Current Secured Property Taxes, $2.8 million Taxes in Lieu revenues, $0.7 million in ABX1 26 Pass Through and $0.2 million increase in ABX1 26 Residual Revenue. It is anticipated assessed values will increase 4% in FY2019/20 and FY2020/21 as Solano County continues to recover from the Great Recession and subsequent local housing market collapse.

- Current Unsecured Property Taxes projected to remain flat in FY2018/19 and increase by 1% per year in FY2019/20 and FY2020/21 as there are a number of appeals from large businesses that may impact these projected revenues.

In addition to General Revenues, the County Budget is financed by Proposition 172 revenues for Public Safety and 1991/2011 Realignment funds (State sales tax and vehicle license fees) for Health and Social Services (H&SS), State and federal funding, and Fees for Services. While these revenues do not flow directly into the General Fund, they indirectly impact the General Fund.

  - The Recommended Budget reflects $37.5 million in Proposition 172 funding, an increase of $1.4 million. As Proposition 172 funds increase for the County, then the General Fund contribution to the Public Safety Fund Departments may be reduced correspondingly.
  - The Recommended Budget reflects $55.3 million drawdown in 1991 State – Local Realignment revenues, a decrease of $3.3 million; and $38.2 million in 2011 Realignment funds, an increase of $9.4 million. If federal and State revenues come in higher than anticipated, then General Fund Contribution may be reduced as long as the County's Maintenance of Effort is met. If federal and State revenues are lower than anticipated, then the demand for General Fund increases.

**Expenditure Assumptions:**

- As previously discussed, retirement costs are projected to continue to increase through FY2020/21 based on approved CalPERS actuarial assumptions for the proposed rates by CalPERS. Included is a rate of 22.939% for Miscellaneous and 30.258% for Safety in FY2018/19.
- Health insurance costs are projected to increase 6% per year based on past rate history.
- The County General Fund Contribution through FY2018/19 are listed below:
  - General Fund support for Public Safety is projected to increase from $110.9 million to $119.9 million; a $9 million net increase. This increase takes into consideration salary and benefit increases, increases in central data processing charges, insurance, and countywide administrative overhead costs, combined with a reduction in other revenue sources such as institutional care and contracted services.
  - General Fund support for H&SS and IHSS Public Authority is projected to increase from $26.5 million to $28.7 million; a $2.2 million increase. This primarily represents increases in Social Services in CalFresh, Public Guardian, and IHSS administration, IHSS services, Foster Care Assistance, and the FY2018/19 CMSP Participation Fee.
- The FY2018/19 Recommended Budget includes a Contingency appropriation of $12 million.

**General Fund Deficit Reduction Strategies for FY2018/19 if Revenue Shortfall:**

The Department Heads and the CAO will continue to utilize the Board adopted Budget Strategies to guide the departments in their continuing efforts to contain costs and where possible reduce further and serve as guidelines <u>if revenues do not materialize as anticipated</u>.

***Strategy 1:*** *Elimination or freezing of all vacant positions and only fill positions that are "Mission Critical" to the organization*

***Strategy 2:*** *Continue to review all discretionary and mandatory programs*

***Strategy 3:*** *Seek employee concessions, in addition to the current MOUs and agreements in place or in progress*

***Strategy 4:*** *Reduce General Fund Contribution to Health & Social Services and Public Safety departments, reducing the level of service to the community*

***Strategy 5:*** *Continue reducing the County's footprint in buildings in Fairfield, Vallejo and Vacaville, and move employees out of leased space in County-owned space; consider selling older/outdated County buildings to reduce operational expenses*

***Strategy 6:*** *Continue automating the delivery of services so reorganization/downsizing opportunities can continue*

## PENDING ISSUES

<u>Supplemental Budget</u>: The Recommended Budget document was prepared early in the month of May to facilitate a May release and longer review period prior to Budget Hearings in June. To accommodate the earlier release, the departmental budgets reflect only the known and approved State and federal programs changes as of April 2018, which will take effect July 1, 2018.

Historically, the County Administrator's Office prepares a Supplemental Budget document following the completion and distribution of the Recommended Budget, as more of an administrative function, primarily to address accounting notations. To the degree possible, the Supplemental Budget may reflect additional program and service changes including possible reductions that can be expected based on the Governor's May Revision and ultimately approved legislation including budget Trailer Bills.

Health and Social Services

AB 130 and SB 90 created a new County IHSS MOE effective July 1, 2017, resulting in the redirection of Mental Health and Public Health 1991 Realignment growth funding (funding above an annual base allocation) to Social Services to offset a portion of the increase in the County's maintenance of effort (MOE) for IHSS. Mental Health and Public Health will not receive funding above their base allocations through FY2018/19, and only half of their growth funding for two additional years through FY2020/21. In addition to funding levels remaining flat for multiple years, it is possible that in recessionary years 1991 Realignment base allocations may be reduced. Beyond the impacts of the redirection of 1991 Realignment funding, it is also possible that up to 10% of Public Health's base allocation may be redirected to County Social Services to help the County pay for the significantly increased IHSS MOE. While the potential 10% redirection will not occur in FY2018/19, it will have a revenue impact on Public Health in any year where it occurs. Both Public Health and Mental Health anticipate the need to revise future services levels to align with available funding with Mental Health potentially requiring additional County General Fund.

Affordable Care Act: The status of the Affordable Care Act (ACA) under the federal administration remains unresolved. Through ACA, counties' costs of serving the indigent population decreased as many formerly uninsured individuals obtained health coverage through the Medicaid expansion implemented under the ACA. In June 2013, the State signed into law AB 85 (See glossary for definition) which provided a mechanism for the State to redirect counties' 1991 Public Health Realignment funding previously dedicated to pay for indigent healthcare costs to fund social services programs (CalWORKs grant increases). For Solano County, the amount redirected each year is $6.9 million. In the meantime, counties remain responsible for providing healthcare to the indigent population under W&I Code section 17000. A repeal of the Medicaid expansion under ACA would significantly increase counties' indigent healthcare costs, leaving counties with no dedicated funding stream. Public Health programs could also be affected if the ACA Prevention and Public Health Fund is either cut or redirected, as these dollars are used to fund numerous programs at the Centers for Disease Control and Prevention, including funds directed to the State and local levels for immunizations, Tuberculosis control and other Communicable Disease programs.

AB 403 Continuum of Care Reform (CCR): CCR was initiated in FY2017/18 and added intensive services to all youth who would benefit from a particular intensive service array (a service type that was previously provided to Child Welfare Services (CWS) youth), intensive mental health care to youth who would formerly have been in group homes, and the ability for foster parents to bill Medi-Cal for services they deliver to their foster youth Mental Health is working closely with Social Services, CWS in monitoring the transfer of youth into the County; if numbers transferring into the County increase, the division may need to adjust service delivery and available contracted services based upon those trends. It is likely that due to more affordable housing and foster care placements in Solano County as compared to neighboring counties that there could be a net increase in youth with high service needs.

In-Home Supportive Services: The FY2018/19 Recommended Budget reflects a projected increase of $1.4 million in appropriations in Solano County's IHSS MOE for all components (services, IHSS (ODAS) administration, and IHSS Public Authority administration). The increase is primarily due to the negotiated $0.50 wage supplement effective May 1, 2018 and the 5% inflation increase in FY2018/19 as required by statute. The Recommended Budget does not include any adjustment of the FY2017/18 IHSS MOE as the State is not expected to finalize its annual reconciliation until September 2018. The reconciliation will establish the final FY2017/18 County IHSS MOE base amount and could result in either a decrease or no change in the base amount for both FY2017/18 and FY2018/19. If the County's FY2017/18 IHSS MOE costs are reduced and the County has received redirected revenues in excess of its costs, the County will be required to remit the excess redirected funds back to the State with the exception of redirected CMSP funds which can be rolled over to subsequent years.

2011 Public Safety Realignment/AB 109 Funding: The Recommended Budget reflects the County's share of the estimated total AB 109 base and growth funding allocations statewide. The budget recommended by the Solano Community Corrections Partnership (CCP) includes the continued use of one-time carry forward funding from prior years' unspent allocations to fund these programs previously approved by the Board under the 2011 Solano Public Safety Realignment Act Implementation Plan. AB 109 Growth funding, which is based on statewide revenue estimates is subject to change pending the final state revenue figures. County staff is continuing to monitor the State allocation of AB 109 funds as departments address the mandated changes resulting from the implementation of 2011 Public Safety Realignment. While one-time carry forward funds will provide necessary funding for FY2018/19, the continued use of unspent carry forward to balance the budget in future years is unsustainable. To maintain the existing level of AB 109 programs and services in future years, the Community Corrections Partnership will need to increase revenue or decrease appropriations. Departments are currently working to evaluate existing programs and services.

Property Tax Appeals/Prop 8 Values: As of May 9, 2018, there are 320 active property tax appeals on file with the Clerk of the Board representing $6.8 billion (cumulative over 8 years) in assessed value “at risk”. The final resolution of these appeals may have a significant impact on the County’s property tax revenues in the future. Efforts continue by the Assessor, with assistance from County Counsel, to address and resolve appeals and reduce the number and value of outstanding appeals to address the uncertainty.

The recovering residential real estate market results in a decrease in the number of properties on Proposition 8 status - a temporary reduction in property values below their established Proposition 13 base year value. According to the Solano County Assessor-Recorder’s Office, as of June 30, 2017, 14,400 parcels remain on Proposition 8 status, compared to 78,000 parcels in 2012. The county continues to have some residential neighborhoods that have not fully recovered their peak values from 2007.

Capital Renewal and Major Maintenance – County Roads and Bridges: As required by law, the Board adopted a 5-Year Capital Investment Plan for Roads and Bridges on April 24, 2017 which shows an estimated $80 million in improvements over the next 5 years and $12 million in unfunded road maintenance and bridge replacement projects. The Board’s existing policy has been for the County to secure State and federal funds for large projects, such as bridge replacements and major road reconstruction, and to use the local Road Fund to provide for all other required maintenance. As State and federal funding for this area of responsibility shrinks in the near term, other options and further consideration regarding adequate sustaining maintenance on Roads and Bridges will be necessary. (Refer to Public Ways budget)

Transportation Funding SB-1-2017: Transportation funding Gas Tax provides new revenue for expenditure for road maintenance and safety projects, among other eligible expenses. The first phase of the new tax began in 2017, with other portions of the tax phasing in during FY2018/19 and FY2019/20. The Department’s Capital Improvement Plan is tiered to include projects based on anticipated SB 1 revenue. A coalition opposing SB 1 is proposing a ballot measure aimed at the November 2018 statewide election to repeal the new gas tax. If it qualifies for the ballot and the repeal is successful, significant reduction in SB 1 revenue will occur for the remainder of FY2018/19 and subsequent fiscal years, decreasing the funding availability for the Department to complete non-federal projects.

Liability - Pending Litigation: The County’s Risk Management program administers the County’s Liability Insurance programs; monitors and directs administration of the program through the California State Association of Counties - Excess Insurance Authority (CSAC-EIA) Primary General Liability Insurance Program, Excess Liability Insurance Program, Medical Malpractice Insurance Program; and Cyber Liability Program; works collaboratively with County Counsel on civil lawsuits; and manages County risks. In FY2017/18 the County Liability Insurance Program utilized a significant portion of the Risk Management Liability Reserve due to unforeseen litigation and settlements which were not covered by existing insurance or Fund Balance. To address budget shortfalls the General Fund contributed $1.2 Million from General Fund Contingency as approved by the Board of Supervisors on April 10, 2018. The FY2018/19 Recommended Budget reflects the utilization of existing fund balance in the Liability Division and includes a transfer from the General Fund of $1 million related to one-time unanticipated litigation exposures. County staff continue to monitor potential exposure from pending litigation and will update the Board throughout the upcoming fiscal year.

Non-Profit– Throughout FY2017/18 the County continued efforts to work with the Non-Profit Community. In 2017, First 5 Solano received a grant award of $40,000 from the Zellerbach Family Foundation which allowed 25 non-profits to participate in an intensive capacity building program through UC Berkeley Extension. First 5 Solano Commission and staff also commissioned a non-profit capacity assessment for 103 non-profits which are funded by First 5 Solano or Solano County Health and Social Services to identify capacity building needs. The results of this study will be shared with the First 5 Commission and the Board of Supervisors later this spring. However, as we head into FY2018/19 Solano County non-profits continue to struggle with a select few closing and others indicating concern over future sustainability. According to the 2016 Applied Survey Research study funded by First 5, Foundation Giving (entities that fund organizations, institutions, or individuals for a range of charitable purposes) in Solano County lags considerably behind that of other Bay Area counties at $3 per capita. First 5 Solano and Health & Social Services are working to assist with non-profit capacity, building off the needs identified in the recent assessment study. The Board will be asked to consider supporting an overall Human Services Assessment to identify the greatest service needs in the County, the availability of existing services to meet the needs, and options to address the remaining gap in services, given the limited resources for FY2018/19.

**SUMMARY OF RECOMMENDATIONS**

For Board consideration are recommended increases to committed fund balances as depicted in Schedule 4. In addition to these recommendations of $1 million to Unfunded Employee Leave Payoff, $3 million to Capital Renewal, and $4.8 million to the Employer PERS Rate Increase, if the FY2017/18 Midyear projection for fund balance is not met the County Administrator will authorize the Auditor-Controller to reduce these recommendations accordingly. However, if the amount of the General Fund's Year-end Fund Balance at June 30, 2018 exceeds the Midyear projections for FY2017/18, then the County Administrator is authorized to direct the Auditor-Controller to increase unrestricted Fund Balance to finance the gap between revenues and expenditures for FY2018/19 of any amount and to transfer year end General Fund Balances to all or some of the following committed Fund Balances and reserves in the following manner:

1. Any amount up to $5 million to Deferred Maintenance/Capital Renewal Reserves
2. Any amount up to $5 million to the CalPERS Reserves and/or 115 Trust
3. Any amount up to $4 million to General Fund Reserves
4. Partially or wholly payoff the outstanding principal balance of the General Fund loan for Pension Obligation Bonds