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DATE: June 14, 2022

TO: Members of the Board of Supervisors

FROM: Sheryl Bratton, County Administrator

SUBJECT: Five-Year Fiscal Forecast

As part of the April Budget Workshops, staff presented a 5-year fiscal forecast. At the time it included a projected surplus of $12.8 million for FY 2021-22, a balanced budget for FY 2022-23, and a deficit of $12.5 million in in FY 2023-24, which gradually increases thereafter. Since that time staff have updated the forecast based on new information including:

1) Third-quarter estimates for 2021-22 revenues and expenditures
2) Additional information from supplemental adjustments to the Recommended Budget
3) Adjustment to the timing of the opening of the Behavioral Health Housing Unit in line with latest information

The primary assumptions included in the forecast have not changed, as there has not been significant new information to adjust these assumptions.

FY 2021-22 Projections

The updated forecast now shows a larger surplus of $20.2 million in FY 2021-22. The surplus is driven primarily by improved tax revenues ($14.6 million above budget and $5.8 million above the prior estimate) and greater than anticipated salary savings of ($13.3 million, $2.2 million in greater savings than was anticipated at the April workshops). The improvement in tax revenues has been seen in most categories, including property tax, documentary transfer tax, sales tax, and transient occupancy. The budgeted revenues for FY 2021-22 had assumed an ongoing level of impact from COVID, while revenues largely rebounded to pre-COVID levels or above. The salary savings reflect greater than expected vacancy rates. This is broadly in line with the recurring theme heard at the April Budget Workshops with regard to higher rates of attrition among employees and increased difficulty hiring replacements in a tight labor market. The increases described above were partially offset by expenditures on services and supplies and other non-employee costs, which are projected to come in above the initial budget.

One item in the 2021-22 projections that requires some explanation is the use of fund balance. The Adopted budget included $8.2 million in use of FY 2020-21 year-end fund balance programmed for use in 2021-22 for one-time needs. The use of fund balance line increased to $42.3 million based on the following:

- An additional $11.7 million in year end fund balance programmed according to Board Direction from Budget Hearings ($3.75 million to pay down pension liability, $3.75 million toward deferred maintenance, and $4.2 million toward Board approved strategic plan projects that were ready to initiate in FY2021-22).
- $20 million toward construction of a new public health lab/morgue (including $10.2 million in fund balance that had been assigned for demolition of the Chanate property if needed and $9.8 million in FY 2020-21 year-end fund balance above what was anticipated in the budget).
- Approximately $1.6 million in designated fund balance set aside for specific projects at the end of FY 2020-21 and re-budgeted in FY 2021-22, primarily related to information technology projects.

This extra use of fund balance was entirely offset by expenditures and was not responsible for the increase in projected FY 2021-22 year-end savings.

Looking Ahead

The forecast shows a balanced budget for FY 2022-23, which is unchanged since the April Workshops, although it does show increases of about $3.0 million in both revenues and expenditures related to items that are being added in supplemental adjustments based upon Board actions between March and May.

In FY 2023-24 the forecast shows a $3.5 million deficit, which is largely driven by increasing staffing costs, particularly an expected increase in pension costs due to the Sonoma County Employee Retirement Associations reduction of their discount rate from 7% to 6.75%, which was approved in 2021 but will only begin to impact pension rates in FY 2023-24. The forecast is significantly improved from the version shown in April, however this improvement is temporary. The April forecast assumed staffing costs associated with the Behavioral Health Housing Unit would come online during FY 2023-24. The current project timeline calls for the facility to open late in FY 2024-25. As such the Forecast has been updated to show those costs beginning to impact the budget during FY 2024-25, when a $6.5 million deficit is projected, and increasing in FY 2025-26, when a $10.4 million deficit is projected. In FY 2026-27 a $13.6 million deficit is projected.

Uncertainty

There is always a significant degree of uncertainty in looking toward the future, but several "known unknowns" raise cause for concern. First, the model projects modest, but slowing, growth in tax revenues. This is in line with data we see on property tax and with the latest forecasts from our Sales Tax consultants. Should high inflation and the actions taken to control it lead to a recession as the Legislative Analyst's Office has warned[1], however, we could see these modest rates decrease. On a related note, rising interest rates make purchase of homes

[1] https://lao.ca.gov/Publications/Report/4598

more expensive for the majority of buyers. This is likely to lead to a decrease in home sales or to a decrease in home prices, or to both. Because growth in property tax is limited by Proposition 13, growth in property tax revenue is driven largely by sales (which allow for a reassessment of the value to the market rate), and therefore declining sales or prices would have a disproportionate impact on revenue growth.

In addition to concerns about the economy, the County is entering labor negotiations with all of its bargaining units during the coming year. Absent information on what a new contract will look like, the model extends the assumptions in the current agreements, which call for cost of living adjustments to be between 2% and 4% depending on revenue growth and inflation. Under this model and the assumptions put forward, the forecast projects a 3% increase in FY 2022-23, with increases of about 2.3% thereafter. Should an actual agreement lead to higher adjustments or to increases in other areas such as medical benefits, the deficits would be larger than is shown here.

Five-Year Projections
General Fund

General Fund Only Forecast

General Fund - General Purpose Sources

	FY 21-22 Adopted	FY 21-22 Projected	FY 22-23 Projected	FY 23-24 Projected	FY 24-25 Projected	FY 25-26 Projected	FY 26-27 Projected
Secured Property Tax	282,937,330	287,828,114	297,318,316	306,576,405	316,112,237	325,854,587	335,889,208
Redevelopment Increment	(13,428,190)	(13,469,462)	(14,226,464)	(14,653,258)	(15,092,856)	(15,545,641)	(16,012,010)
Residual Property Tax RPTTF	10,000,000	10,000,000	10,000,000	10,000,000	10,000,000	10,000,000	10,000,000
Unsecured Property Tax	7,000,000	7,343,801	7,602,750	7,602,750	7,678,777	7,755,565	7,833,121
Supplemental Property Tax	3,500,000	4,778,971	3,883,676	3,889,697	3,963,192	3,987,642	4,064,106
Documentary Transfer Tax	5,500,000	9,000,000	7,973,454	8,093,056	8,214,452	8,337,668	8,462,733
Sales Tax[1]	23,702,000	26,184,558	25,723,283	26,737,000	27,996,000	29,248,000	29,832,960
TOT[2]	3,900,000	6,072,275	6,072,275	6,254,443	6,410,804	6,571,074	6,735,351
Other	60,000	64,855	75,000	75,000	75,000	75,000	75,000
Total Tax Revenue	**323,171,140**	**337,803,112**	**344,422,289**	**354,575,093**	**365,357,607**	**376,283,896**	**386,880,469**
Other General Purpose Revenues	**41,796,994**	**49,013,042**	**37,213,959**	**37,295,459**	**37,383,524**	**37,474,231**	**37,567,659**
Use of One Time Fund Balances[3]	**8,200,000**	**42,302,115**	**-**	**-**	**-**	**-**	**-**
Total General Purpose Sources	**373,168,134**	**429,118,269**	**381,636,248**	**391,870,552**	**402,741,131**	**413,758,127**	**424,448,128**

General Fund - Departmental Revenues

	FY 21-22 Adopted	FY 21-22 Projected	FY 22-23 Projected	FY 23-24 Projected	FY 24-25 Projected	FY 25-26 Projected	FY 26-27 Projected
Tax Revenue	17,430	77,179	17,430	17,430	17,430	17,430	17,430
Licenses, Permits, Franchises	15,135,989	13,450,372	13,299,011	13,423,854	13,549,945	13,677,298	13,805,924
Intergovernmental Revenues[4]	82,704,965	84,845,212	92,597,018	94,055,543	95,539,304	97,048,767	98,584,406
Fines, Forfeitures, Penalties	6,161,168	5,940,517	6,185,262	6,185,262	6,185,262	6,185,262	6,185,262
Revenue - Use of Money & Prop	631,917	785,319	1,001,901	1,001,901	1,001,901	1,001,901	1,001,901
Charges for Services	46,422,864	44,811,033	48,506,071	49,717,365	50,901,177	52,119,227	53,372,516
Miscellaneous Revenues	2,681,733	2,865,757	2,722,155	2,505,167	2,505,167	2,505,167	2,505,167
Other Financing Sources[5]	39,712,840	42,882,182	40,462,014	40,028,733	40,042,697	40,443,124	40,847,555
Total Departmental Revenues	**193,468,906**	**195,657,572**	**204,790,862**	**206,935,255**	**209,742,883**	**212,998,175**	**216,320,161**
Total General Fund Sources	**566,637,040**	**624,775,841**	**586,427,110**	**598,805,808**	**612,484,014**	**626,756,303**	**640,768,289**

General Fund Expenditures

Wages and Benefits

	FY 21-22 Adopted	FY 21-22 Projected	FY 22-23 Projected	FY 23-24 Projected	FY 24-25 Projected	FY 25-26 Projected	FY 26-27 Projected
Wages/Pay	194,154,737	187,467,808	200,446,904	205,057,342	209,439,849	213,849,931	218,489,580
Prorated Benefits	67,236,359	64,920,656	73,361,574	75,157,552	77,471,377	79,835,564	81,674,165
Medical Benefits	31,906,311	30,807,418	35,089,695	35,791,489	36,837,394	37,911,824	38,670,061
Other Fixed Benefits	1,463,783	1,413,369	1,642,709	1,642,709	1,657,741	1,673,119	1,673,119
Pension	45,928,556	44,346,720	46,556,871	56,414,919	59,352,936	62,417,388	65,131,948
Penson Obligation Bonds[6]	29,139,867	28,136,254	19,212,398	16,871,104	17,654,614	18,466,726	19,316,195
Other Retiree Benefits (OPEB)	16,814,755	16,235,634	17,583,830	18,014,303	18,604,943	19,209,316	19,651,703
Total Wages and Benefits[7]	**386,644,368**	**373,327,859**	**393,893,981**	**408,949,417**	**421,018,855**	**433,363,868**	**444,606,772**

Other Expenditures

	FY 21-22 Adopted	FY 21-22 Projected	FY 22-23 Projected	FY 23-24 Projected	FY 24-25 Projected	FY 25-26 Projected	FY 26-27 Projected
Services and Supplies	**160,607,944**	**162,450,153**	**161,012,100**	**167,129,963**	**171,036,612**	**176,167,711**	**181,452,742**
Other Charges	**27,224,674**	**26,841,350**	**27,762,944**	**28,318,203**	**28,884,567**	**29,462,259**	**30,051,504**
Fixed Assets	**5,909,326**	**6,331,329**	**5,516,982**	**5,516,982**	**5,516,982**	**5,516,982**	**5,516,982**
Transfers (Details Below)	**100,708,822**	**144,116,816**	**105,389,368**	**99,964,443**	**101,193,098**	**102,452,915**	**103,744,918**
Roads Ongoing Funding	*16,663,077*	*16,663,077*	*17,095,508*	*17,302,271*	*17,513,170*	*17,728,287*	*17,947,706*
In Home Support Services	*12,917,813*	*12,917,813*	*13,434,526*	*13,971,907*	*14,530,783*	*15,112,014*	*15,716,495*
Capital Projects/Facilities Maintenance	*13,406,745*	*14,401,761*	*16,401,761*	*16,401,761*	*16,401,761*	*16,401,761*	*16,401,761*
All Other Transfers	*57,721,187*	*100,134,165*	*58,457,574*	*52,288,504*	*52,747,384*	*53,210,853*	*53,678,957*
Reimbursements[8]	**-121,123,787**	**-112,242,231**	**-111,462,395**	**-112,577,019**	**-113,702,789**	**-114,839,817**	**-115,988,215**
Contingencies	**6,665,693**	**3,759,574**	**4,314,130**	**5,000,000**	**5,000,000**	**5,000,000**	**5,000,000**
Total Other Expenditures	**179,992,672**	**231,256,991**	**192,533,130**	**193,352,573**	**197,928,471**	**203,760,050**	**209,777,931**
Total General Fund Expenditures	**566,637,040**	**604,584,850**	**586,427,111**	**602,301,990**	**618,947,325**	**637,123,918**	**654,384,703**
Total Surplus (Deficit)	**-**	**20,190,992**	**-**	**(3,496,182)**	**(6,463,311)**	**(10,367,615)**	**(13,616,414)**

[1] Sales tax projections based on HdL 2021 Calendar Q4 projections.

[2] Includes only the 1/4 of Transient Occupancy Tax received by the General Fund.

[3] See cover memo for details.

[4] Includes Proposition 172 Public Safety Revenue.

[5] Primarily made up of transfers within the County.

[6] 2003 Pension Obligation Bonds are completed in FY 2022-23.

[7] Wages and benefits increase in beginning in January, 2025 and approximately $7.4 million for staffing at the Main Adult Detention Facility Behavioral Health Unit.

[8] Excludes Cost Plan Reimbursements, which are included in General Purpose Revenue.