COUNTY ADMINISTRATOR

June 10, 2014

Honorable Board of Supervisors
Administration Building
Oakland, California 94612

SUBJECT: FISCAL YEAR 2014-2015 PROPOSED BUDGET

Dear Board Members:

The County Administrator's Proposed Budget for Fiscal Year (FY) 2014-2015 is balanced and provides $2.8 billion in spending for County programs and services. The Budget reflects input from your Board, agency and department heads, and other County stakeholders to close a $67.1 million funding shortfall, the County's lowest deficit in seven years. The Budget does not propose layoffs or significant program reductions.

By most measures, the national economy continues to improve, with particularly strong growth in the Bay Area. According to the U.S. Bureau of Labor Statistics, wages and benefits in the nine-county region rose more over the past year than in any other major metropolitan area in the United States. Alameda County's unemployment rate recently dropped below 6% for the first time since before the recession. Perhaps recognizing greater opportunity, Alameda County is attracting more residents and is one of the fastest growing counties in the region and State, with a population of almost 1.6 million people. Alameda County's population grew by 1.5% last year, making it and Santa Clara County the two fastest growing counties in the State. The City of Dublin, one of Alameda County's 14 cities, was the third-fastest growing city in California last year, increasing its population by 7.1%.

The improving economy, low interest rates and greater demand have led to rising real estate values. Median home prices, which had lost close to half their value during the recession, have almost returned to their previous peaks, and foreclosures have declined dramatically. Reflecting higher real estate values, the Alameda County Assessment Roll increased 5.2% for FY 2013-14. Although still lower growth than the pre-recession average, the increase is welcome following the $7 billion in local government property tax revenue that was lost statewide during the recession, according to the Legislative Analyst's Office. Sales taxes are also increasing, an indication of greater consumer confidence and a brighter economic outlook in Alameda County than in recent years.

Unfortunately, the economic recovery has not benefitted everyone equally. Taking into account the cost of living, California has the highest poverty rate in the nation at 23.8%. In Alameda County, there are more than 50 neighborhoods with poverty rates that exceed 25%, and historically high numbers of families, adults, and children currently receive safety-net services. Recognizing that in spite of the country's great wealth, poverty persists unabated, on January 7, 2014, your Board adopted a resolution launching a "New War on Poverty" to raise awareness and seek solutions. In addition, the County continues to shine a spotlight on the people most affected by cumulative State budget reductions. These “human impacts” are again included in a special section of the Proposed Budget.

STATE BUDGET

Governor Brown deserves credit for returning the State’s finances to more stable footing. Even with State revenues now exceeding previous forecasts by several billion dollars, the Governor maintains a cautious approach, citing a list of higher spending obligations that offset new revenues. Moreover, the revenue increases come largely from the State’s most volatile revenue source: income taxes from capital gains. Stock market gains of almost 30% in 2013 are unlikely to be duplicated. Rather than investing in new programs or restoring prior cuts, Governor Brown proposes a strong Rainy Day Fund that would pay off debt and build up reserves for the next economic downturn. The Governor’s Budget also includes a new proposal to shore up the underfunded teachers’ pension retirement system.

While now is not the time for massive new spending, given the hardship that State cuts have had on the most vulnerable members of our community, the State could consider restoring some of the cuts to poverty-fighting programs like CalFresh, subsidized childcare, and housing assistance for CalWORKs recipients. In addition, the State’s transfer of many public safety programs to local government continues to pose new challenges, including the fact that County jails were not designed to house inmates for extended sentences. A California State Sheriff’s Association survey reveals that over 1,700 inmates in County jails statewide are serving sentences of five years or longer. Even with public safety realignment, the State has not been able to comply fully with a federal court order to reduce overcrowding in California’s prisons. Restoring planned cuts to public safety realignment funding and modest funding increases for programs targeted at reducing recidivism would serve the common goal of reducing prison and jail admissions.

The Governor does propose a long-overdue acceleration of reimbursements to local governments for State-imposed mandates. Unfortunately, the Legislature appears eager to use the $100 million the Governor proposes returning to local governments in FY 2014-15 as a means of paying for new investments in programs. The State should restore its own cuts to important programs, but not on the backs of local governments. The repayment of these mandates would help not only local governments but also assist the State’s goal of paying down its “Wall of Debt.”

HEALTH CARE REFORM

California has been a leader in implementing national health care reform, and far higher numbers of Californians are signing up for health coverage than previously expected. The Governor’s May Revise nearly doubles its enrollment estimates for the optional Medi-Cal expansion the State launched last year. Projected enrollments next year among those previously eligible to sign up for Medi-Cal have increased dramatically as well. Approximately 11.5 million Californians are projected to be on Medi-Cal in FY 2014-15, almost a third of the State’s population.

Last year the State adopted a major new realignment of health and public assistance programs to implement the Affordable Care Act (ACA). The State redirected $300 million statewide from county health departments to implement the State-administered Medi-Cal expansion program and to fund an increased local share of cost requirements for public assistance programs like CalWORKs and CalFresh. Alameda County’s share of 1991 realignment funding for indigent health was cut by $11 million in FY 2013-14. In FY 2014-15, Governor Brown proposes redirecting $725 million statewide, which would strip out all of Alameda County's $44 million in 1991 realignment funding for indigent health. The loss of revenue will reduce the Alameda Health System's contract for indigent health services, resulting in significant challenges for the public hospital system that serves vulnerable populations, including those least likely to benefit from coverage expansion under the ACA. To lessen the impact, the Proposed Budget adds $9.4 million in County General Fund support for primary care community-based providers, continuing for a full year the funding your Board approved for the current year.

The shift of 1991 realignment funding continues to raise significant concerns about the ongoing cost to counties of providing services to those individuals not covered by the expansion. In Alameda County, an estimated 100,000 people may still be uninsured and will require County indigent health care services. In addition, the transfer of projected cost savings comes in spite of the fact that the federal government will fully reimburse the State for its costs for the first three years of the optional Medi-Cal expansion.

Glitches in the State's implementation of the ACA have had significant impacts on the Social Services Agency—which is responsible for ACA implementation in Alameda County—as well as applicants and health care providers. Ongoing problems with the State's computer system have created a backlog of over 40,000 applications that Alameda County staff must review one-by-one. The Social Services Agency is currently prioritizing these cases while balancing new applications and processing Medi-Cal renewals for approximately 20,000 individuals per month. Applicants face uncertainty regarding whether they have Medi-Cal insurance coverage, while healthcare providers do not know whether they will receive reimbursements for serving pending applicants.

BUDGET OVERVIEW

The FY 2014-15 Proposed Budget for all funds totals $2.8 billion, an increase of $86.7 million, or 3.2%, from the FY 2013-14 Final Budget. The General Fund, which funds most County operations, totals $2.3 billion, an increase of $53.5 million, or 2.4%.

All Funds ($ billions)	2013-14 Final	2014-15 MOE	2014-15 Proposed	Change from 2013-14
Appropriation	$2.69	$2.80	$2.78	$0.09
Revenue	$2.69	$2.73	$2.78	$0.09
Funding Gap	$0.00	$0.07	$0.00	$0.00
FTE	9,196.82	9,499.67	9,493.67	296.85

General Fund ($ billions)	2013-14 Final	2014-15 MOE	2014-15 Proposed	Change from 2013-14
Appropriation	$2.26	$2.32	$2.31	$0.05
Revenue	$2.26	$2.26	$2.31	$0.05
Funding Gap	$0.00	$0.07	$0.00	$0.00
FTE	7,339.05	7,631.04	7,625.04	285.99

The Proposed Budget includes funding to provide mandated and essential services, meet debt service obligations, maintain a minimum level of infrastructure and capital funding, and adhere to the Board's financial management policies. The Proposed Budget supports a workforce of almost 9,500 full-time equivalent (FTE) positions and reflects a net increase of 297 FTE. This includes mid-year Board-approved adjustments of 303 positions, offset by the elimination of 6 vacant FTE as part of budget balancing.

The Proposed Budget funds cost-of-living adjustments (COLAs) for most of our employees based on negotiated labor agreements, and for many of our community-based organization (CBO) contractors. The Proposed Budget also includes $459.4 million for services provided by 242 CBOs, a decrease of $48 million from FY 2013-14. The funding reduction is due to a decline in State funding for indigent health services under the presumption that most of those enrolled in indigent health programs will receive federally-supported or other subsidized health care insurance coverage under the ACA. The Health Care Services Agency's contracts with Alameda Health System (AHS) and various clinics to provide indigent health care services are reduced as a result. AHS is budgeted to receive $77.3 million for these services, compared to $131 million in FY 2013-14. Other CBOs funded in the Proposed Budget include non-profit service providers, cities, school districts, and local hospitals. A list of all CBO contracts with funding recommendations is included in the Appendix of the Proposed Budget document.

Measure A, the voter-approved half-cent sales tax, continues to provide funding for essential health care services. AHS receives 75% of the revenue directly and the remaining 25% is allocated by the Board of Supervisors to support other essential health services. The Proposed Budget includes $28.7 million in Measure A funds for non-AHS essential health services, a decrease of approximately $0.45 million or 1.5%, compared to the FY 2013-14 budget based on the three year Measure A spending plan adopted by your Board. Recognizing the importance of this funding source, on June 3, 2014, voters supported Measure AA, extending the half cent sales tax dedicated to essential health care through 2034.

Board-approved funding of $15.9 million for capital projects supported with General Fund property tax revenues is included in the Proposed Budget. Prior to the State's dissolution of redevelopment agencies in February 2012, these discretionary property tax revenues had been committed to redevelopment projects in the County and many of our cities. The increase in capital project funding is consistent with your Board's decision to allocate for five years up to $18 million annually of former redevelopment agency property tax increment to fund certain infrastructure and capital projects in the unincorporated areas of the County.

Consistent with your Board's financial management policies, the Proposed Budget recommends increases of $5.6 million, the equivalent of 1% of discretionary revenue, for both capital projects and the general reserve. Contingencies for pending labor negotiations, benefit cost increases, and other contractual obligations are also included in the Proposed Budget.

CLOSING THE GAP

The Proposed Budget closes a $67.1 million funding gap that was projected based on the Maintenance of Effort (MOE) funding requirement. The funding gap was determined by identifying the difference between the cost of maintaining existing programs and projected revenues. The MOE Budget for the

General Fund is $2.32 billion, an increase of $67.7 million, or 3.0%. Available revenues to finance the projected MOE costs totaled $2.26 billion, an increase of just $0.6 million, or 0.03%.

To the extent possible, your Board's Values-Based Budgeting (VBB) priorities and Strategic Vision initiatives have been considered in developing balancing strategies within each program area. The table below summarizes the total proposed net cost reductions by program area:

PROPOSED BUDGET BALANCING
General Fund

Program Area	Net County Cost Reductions ($ millions)
General Government*	19.2
Health Care	23.7
Public Assistance	5.6
Public Protection	18.6
Total	**$67.1**

* includes cost reductions in Capital Projects and Internal Service Funds

Proposed solutions to close the $67.1 million funding gap include a combination of spending reductions, revenue increases, and one-time strategies. The Proposed Budget recommends the use of $17.4 million or 26% in ongoing strategies and $49.7 million or 74% in one-time strategies, with most of the one-time savings coming from the Fiscal Management Reward Program (FMR). The FMR net savings have been generated through the efforts of County agencies/departments to operate their programs efficiently and effectively within budget, to avoid further program and staffing reductions and preserve vital services. FMR is considered a one-time funding source as these savings may not be available to assist with balancing budgets in future years. A structural imbalance between ongoing revenues and expenditures remains.

Proposed Budget Balancing Strategies	Net County Cost Reductions ($ millions)
Ongoing Strategies	
Program appropriation reductions	$9.8
Program revenue increases	$7.6
Subtotal Ongoing Strategies	**$17.4**
One-Time Strategies	
Fiscal Management Reward Savings	$36.5
One-time appropriation reductions	$4.5
One-time revenues	$8.7
Subtotal One-Time Strategies	**$49.7**
Grand Total Balancing Strategies	**$67.1**

PROGRAM AREA NET COST REDUCTIONS

General Government (including Internal Service Funds and Capital Projects) – The General Government program area contributed net cost savings of $19.2 million through $5.1 million in Internal Service Fund savings in the County's self-insured general liability and dental programs; revenue increases of $2.8 million; and $11.3 million in FMR program savings.

Health Care – The Health Care Services Agency contributed net cost savings of $23.7 million through $3.3 million in appropriation reductions, $6.4 million in increased revenue, and $14.0 million in FMR Program savings. The spending reductions include $0.2 million from eliminating two vacant Public Health positions; $0.5 million cut to the Alameda Health System (AHS) indigent care contract; lowering community-based contracts by $0.7 million due to program completion and underutilization; a $0.6 million drop in Public Health diagnostic and therapy program, lab and equipment costs; a $1.0 million cost reduction in in-patient mental health services; and $0.3 million in other adjustments. Revenue increases include $3.1 million in Behavioral Care Medi-Cal funding; a $1.0 million in Mental Health Services Act funding; a $0.8 million in Environmental Health program revenue; the one-time use of $1.0 million of Tobacco Master Settlement Fund revenue; and $0.5 million in one-time Measure A funds to support CBO contracts.

Public Assistance – The Public Assistance program area achieved net cost savings of $5.6 million, including $2.1 million in FMR program savings contributed by the Social Services Agency. In addition, revised projections of caseload declines in the foster care program result in net savings of $1.9 million (reduced appropriations of $3 million, partly offset by reduced revenue of $1.1 million) plus about $0.4 million achieved by eliminating four vacant, project positions. Revenue increases from Fraud Recovery incentives and the CalFresh program account for $1.2 million in net cost savings.

Public Protection – The Public Protection program area achieved net cost savings of $18.6 million through $2.4 million in appropriations reductions, $7.2 million in revenue increases, and over $9 million of FMR Program savings. Balancing strategies in the Sheriff's Office include a $1.6 million reduction in discretionary operating costs, a $0.8 million decrease in capital equipment expenses, and increased revenues of $2.6 million for incarceration services provided to Sonoma County. FMR Program savings contributed by the District Attorney's Office, Probation Department, and Public Defender's Office, as well as Proposition 172 Public Safety sales tax revenue from a prior year designation further reduce the net cost of Public Protection programs.

FISCAL MANAGEMENT REWARD (FMR) PROGRAM SAVINGS

Your Board's FMR Program allows General Fund departments to carry-over net savings each fiscal year to be used in subsequent years for budget balancing, one-time expenditures and program enhancements. Through ongoing cost-saving and revenue generation efforts, County agencies/departments contributed $36.5 million in prior-year FMR savings to help balance the FY 2014-15 budget.

Program Area	Use of FMR ($ millions)
General Government	$11.3
Health Care	$14.0
Public Assistance	$2.1
Public Protection	$9.1
Total FMR	**$36.5**

Ongoing efforts by County departments to reduce spending and conserve resources have enabled the County to mitigate major program reductions and maintain vital services. However, departments must balance these efforts with the need to fund increased costs and meet the growing demand for essential services in all program areas.

COUNTYWIDE STRATEGIES

In past years, it has sometimes been necessary to recommend countywide strategies that are not unique to a particular program area to help balance the budget. This year, the early signs of economic recovery enabled us to include growth in both program and discretionary revenues in the initial phases of budget development. The Proposed Budget includes one-time strategies to reduce Internal Service Fund costs in both the self-insured risk management and dental insurance programs. While these programs and savings are budgeted and reflected in the General Government program area, the net cost reduction strategies are considered countywide as they will affect all County departments.

PENDING FACTORS

Numerous factors could impact the County's ability to provide services within existing resources in future years. The health of the economy affects the demand for the County's services as well as the revenues to pay for those services. After five consecutive years of modest growth, the Gross Domestic Product (GDP) declined in the first quarter of 2014. While probably more due to unusually harsh winter conditions in most of the rest of the country than indicative of a larger trend, better economic conditions will not last forever. The average length of a growth period in the Post-War era is five and a half years – similar to the County's funding gap trend over the last two decades. Events that could put the U.S. or world economies in recession include: the Federal Reserve's tapering of its bond purchasing program, tight lending from banks, slowing economic growth in China, the European economy, and/or the impact of conflicts around the world.

With about half of the County's funding coming from the State and federal governments, policy decisions in Sacramento and Washington, D.C. have a significant impact on the County. The State's shift of 1991 realignment funding for indigent health care brings greater uncertainty to counties already grappling with how to provide services to those who remain without health insurance coverage. In spite of surging and higher-than-expected enrollment in Medi-Cal, the Governor has not proposed additional funding for provider payments, making it difficult to attract medical professionals to meet the growing caseload. Absent higher State funding for providers, accessing health care services will remain a challenge for many.

Due to the unknown impacts of health care reform and other State cost shifts, the current year budget included a one-time designation of $12 million set aside for future budget balancing. Most of that $12 million has now been allocated to assist health care programs with the transition to the ACA – primary care community-based contract agencies, the Alameda Alliance for Health and other indigent care providers. The Proposed Budget does not include continuation of that designation as there is a $9.4 million recommended increase to the health care budget to address ongoing needs of the community-based provider network under the ACA.

ALAMEDA COUNTY'S WALL OF DEBT

Governor Brown's proposals to set aside excess State revenues for a "rainy day" and pay off the State's "Wall of Debt" have received headlines across the State and support for fiscal prudence and long-term financial stability. While your Board has generally adhered to your long-standing financial management policies that include strategies and guidelines to build and maintain prudent reserves and "rainy day" funds, the County still has its own unfunded obligations that must be addressed eventually.

Alameda County's "Wall of Debt" now totals almost $3 billion – about $1.2 billion represents pension costs for current and future retirees. In addition, the County has incurred $600 million of debt related to construction of the Acute Care Tower Replacement project for the Alameda Health System (AHS) and still has outstanding pension obligation bond debt that exceeds $450 million. Other debt includes the County's shared ownership of the Oakland-Alameda County Coliseum/Arena with over $100 million in outstanding bonds and other prior capital commitments for essential facilities like the Juvenile Justice Center and Santa Rita Jail.

Alameda County "Wall of Debt"	
Unfunded pension liability	$1.2 billion
Acute Care Tower debt	$607 million
Pension Obligation Bond debt	$452 million
Coliseum/Arena debt (County share)	$102 million
Compensated Employee Absences Payable	$63.1 million
Other debt (Juvenile Justice, Santa Rita, etc.)	$500 million
Total Outstanding Debt	**$2.92 billion**

The debt incurred by the County for capital improvements has always been based on sound financial plans that identify ongoing revenue sources to retire the debt over time and ensure that the County is still able to maintain its core services and other mandated commitments. The Proposed Budget includes over $50 million for annual debt service payments, plus the County's annual required contributions (ARC) to the pension fund through the Alameda County Employees' Retirement Association (ACERA). However, given the trend toward an improved economy and the possibility of more discretionary revenues as sales and property tax collections improve, plus the County's ability to now retain property tax increment formerly allocated to city and county redevelopment agencies, it is an opportune time for your Board to consider developing a responsible and prudent plan to reduce the County's long-term debt obligations. Paying down the County's Wall of Debt will limit our liabilities, reduce the cost of annual principal and interest payments, further strengthen our credit ratings, and enable us to plan for a more sustainable future.

The financial implications of current and future federal and State cost shifts, continued funding reductions, pending local negotiations with labor groups and health plan carriers, and uncertainty regarding costs of public safety realignment, health care reform and a host of other issues, underscores the need to start the new fiscal year with a balanced budget that is fiscally sound. Your Board will again be faced with difficult decisions as you continue to provide the strong leadership necessary to maintain the County's fiscal integrity and provide vital services to our residents and those in need.

RECOMMENDATIONS

The FY 2014-15 Proposed Budget is balanced and reflects the collective effort and contributions of County stakeholders to develop a balanced and sustainable approach to providing services in the coming year. In addition, balancing the budget using a significant amount of one-time funds will necessitate careful monitoring throughout the year to ensure that expenditures remain within budget and revenue estimates are fully realized.

As you conduct public hearings and deliberate on the FY 2014-15 Proposed Budget, your Board's leadership and strong fiscal management will assist the County in once again maintaining that critical balance between service demands and limited financial resources.

Therefore, it is recommended that your Board:

1. Accept the FY 2014-15 Proposed Budget for review pending public hearings;

2. Set public hearings on the Proposed Budget to commence on June 23, 2014 at 1:30 p.m. as outlined in the Attachment; and

3. Schedule public hearings and/or public meetings to consider charges for the Emergency Medical Services District, Vector Control Services District, Fire Department Emergency Medical Services, Flood Control District, Clean Water Protection, Public Works Agency-administered County Service Areas, and Lead Abatement as detailed in the attached budget hearing schedule.

Respectfully submitted,

/s/
Susan S. Muranishi
County Administrator

Attachment
c: Agency/Department Heads
Budget Workgroup Members
Legislative Advocates
Community-Based Organizations
Labor Representatives

FISCAL YEAR 2014-15
COUNTY BUDGET HEARING SCHEDULE

Date/Time		Program
• Tuesday, June 10	12:00 p.m.	Presentation of Proposed Budget
• Monday, June 23	1:30 p.m.	Opening Comments Health Care* Public Assistance
• Tuesday, June 24	2:00 p.m.	Public Protection** General Government*** Other Issues/Final Adjustments
• Wednesday, June 25	11:00 a.m.	Final Deliberations
• Friday, June 27	12:00 p.m.	Final Budget Adoption

* Includes public meeting to set charges for Emergency Medical Services and Vector Control

** Includes public meeting to set charges for Fire Emergency Medical Services

*** Includes public hearings to set charges for Flood Control District and Clean Water program. Also, includes public meetings to set charges for Public Works Agency-administered County Service Areas and the Lead Abatement program.