

## GENERAL OVERVIEW AND STATE BUDGET

While most economists agree that the recession has officially ended, the most optimistic economic forecasts project slow growth, if any, over the near future. Reminiscent of this last fiscal year, the county's budget plans for FY 11/12 anticipate little help from the economy or the state. Reports of stabilizing job and housing markets produce guarded optimism at best. Locally, the unemployment rate as well as housing foreclosures have been trending downward. This trend fuels the hope that the worst is in the past.

In March, the Governor proposed the FY 11/12 state budget that addressed the \$26.6 billion budget deficit with spending cuts, tax extensions, and other solutions. Spending cuts and the first phase of the Governor's realignment plan were approved by the state legislature. The effect of these items has been reflected in the impacted departments' budgets. Further progress was hindered when the Governor was unable to obtain the support for the other provisions, including the extension the current sales tax and vehicle licensing fees for five years, within his budget plan.

The May revisions to the budget have been released and represent the Governor's best effort to close the budget deficit and address the state's ongoing fiscal problems. Although the revisions reflect positive revenue data for the beginning of 2011, the state continues to report an \$11 billion budget shortfall. The May revise also reflects the Governor's preference for a balanced approach to meeting budget challenges although the impact of an all cuts approach was provided. The impact would include further reductions in CalWORKs, eliminating domestic and related services for IHSS recipients, capping Medi-Cal coverage, and making deeper reductions to developmental services. The Governor also notes that if the dedicated funding stream for realignment is not passed, many of these programs would be eliminated. The county's strategy is to keep current budget tactics unchanged and to direct departments to develop a state budget impact mitigation plan that can be executed as early as July 2011.

## COUNTY DISCRETIONARY REVENUE

A \$10.1 million decline in discretionary revenue is projected for FY 11/12. This decline includes a loss of \$2.0 million in franchise fees, \$1.7 million in sales taxes, \$0.9 million in interest income, and \$1.7 million in other miscellaneous revenue sources. See the table 4 on page 10 for more detail.

Most of Riverside's discretionary revenue is directly related to property values. Property taxes account for 46 percent of the revenue, 33 percent is from state property tax pass-throughs, and 6 percent is from delinquent property tax penalties. The property tax figure is based on the Assessor's preliminary Proposition 8 analysis of property valuation and it is expected the actual amount will not deviate significantly. The Auditor-Controller provides the property tax related estimates while the Treasurer-Tax Collector provides the estimates for interest income.

Three independent sales tax forecasts predict a moderate increase to sales tax revenue in the near term. This growth in sales tax revenue is not enough to compensate for tax

revenue that will be transferred (estimated to be approximately \$7 million) to the new cities of Eastvale and Jurupa Valley. The county's safety sales tax revenue seems to have stabilized at \$110.5 million in FY 09/10. It is expected to be between \$117 and \$121 million in FY 10/11. In FY 11/12, it is projected to be between \$118 and \$121 million. Additional revenue beyond \$110.5 million is placed into a separate fund for public safety needs as directed by the Board.

The county's long-term outlook for discretionary revenue is gradually improving. What remains a matter of active debate is if the county will begin to see a recovery in FY 12/13. The optimistic camp (Beacon Economics) calls for a modest gain in property values, while the more pessimistic camp (Cal State Fullerton economists) forecasts continued falling property values. By all accounts, the growth associated with a significant portion of the county's discretionary revenue will be modest at best. The county is currently projecting a smaller revenue loss (\$10 million) than last year's more than \$33 million loss. While encouraging, the county will not grow its way out of its current economic difficulties any time soon.

## **STRUCTURAL DEFICIT**

In FY 07/08, the first clear signs of economic deterioration became unmistakable. By the end of the next fiscal year, a sizeable disparity had developed between ongoing revenues and ongoing operating expenses. This disparity, or structural deficit, was projected to exceed \$130 million in FY 10/11 if the Board did not exercise steadfast fiscal restraint. It has been the Board's preference to temper the impact of revenue declines with the use of general fund reserves and a multi-year reduction in general fund support. Distributing reductions over several years has allowed department managers to implement gradual changes to business processes while minimizing the severity of service cut impacts during any fiscal year.

With the approval of the FY 10/11 budget, the Board strongly affirmed its commitment to balancing the budget in two years while preserving reserves that were fast approaching critical levels. The Board is still on target to eliminate the structural deficit during FY 11/12. Toward that end, this budget contains about \$55 million in cuts and reductions as well as the use of about \$28 million from the reserve for economic uncertainty. This final year of cuts will put seemingly insurmountable pressure on county managers and staff to preserve essential services. Unfortunately, some services will be slowed or eliminated while some portion of the workforce will be lost to attrition and layoffs.

## **ACTIONS TAKEN TO OVERCOME BUDGET CHALLENGES**

This budget is conservative and recognizes difficult economic conditions. Steps taken over the last few years to address some of the challenges include:

- Negotiation of increased employee participation in retirement costs
- Negotiation of second retirement tier for new employees

- Department-led control of general fund employment levels
- Implementation of Board-approved furloughs
- Implementation of countywide cost control efforts
- Reduction of the workforce through early retirement
- Reduction of the county's vehicle fleet
- Delay or cancellation of capital projects
- Revision or introduction of Board policies that improved business processes and cash management
- Organization of a long-term initiative to increase efficiency through information technology
- Organization of committees to evaluate pension policies and recommend reform as necessary

## **BUDGET WORKSHOPS, TESTIMONY, AND BEILENSEN HEARINGS**

As in the previous year, the Board asked for early budget impact workshops. These budget workshops began in late March and included testimony from department heads. This input and the additional time to consider options allowed the Board to assign measured, targeted cuts to general fund departments.

On May 16, the Board heard testimony from two independent economists hired by the Executive Office. The economist from Beacon Economics forecast that the county's assessed valuation will remain relatively flat for FY 11/12, experience moderate growth in FY 12/13, and pick up in earnest during FY 13/14 and beyond. Beacon Economics prognosis was encouraging although it reported significant risks remain. The next economists from Cal State Fullerton communicated a more pessimistic view of the county's recovery. They predicted assessed valuation would remain relatively flat for the next two fiscal years with modest growth thereafter. They reported many risks to the forecasted recovery.

A Beilensen hearing was held for the Community Health Agency's Children's Services Unit following the economists report. Prior to making a decision to eliminate or reduce the level of medical services offered to the public, the Board is required to hold public hearings. The Board heard testimony from the department head and various members of the public. Comments from the Board indicated a desire to restore cuts so that service levels would remain unchanged.

Based on comments during the workshops and hearings, it is clear that public safety remains a high priority. However, the Board also recognizes the severity of cuts to other departments over the last few years and acknowledges that public safety cuts are necessary to preserve other core services important to the public. On average, public safety departments net county cost targets will be cut by four percent for FY 11/12.

Other departments will be cut an average of 19 percent. Layoffs are expected and displaced employees will be offered similar positions in other divisions, when possible.

## FY 11/12 BUDGET HIGHLIGHTS

- Budget Impact workshops and department testimony allowed the Board to carefully consider general fund departments' challenges. The Board reaffirmed its goal of structural balance during FY 11/12.
- Community improvement funds will be reduced to \$2.4 million for FY 11/12.
- General fund contingency is about 3.4 percent of discretionary revenue (\$20 million), while the Board-approved benchmark is 4.0 percent of discretionary revenue (\$23.3 million.) If Board commitments require additional appropriations, contingency funds may be used.
- Together the reserves for economic uncertainty and disaster relief total about 23 percent of discretionary revenue (\$135.7 million). The Board-approved target minimum for these reserves is 15 percent of discretionary revenue (\$87.3 million.)
- No ongoing general funds are appropriated in the recommended budget for new capital projects.
- The state's fiscal situation remains uncertain. Known cuts are included in this budget. Additionally, departments have prepared contingency plans for likely potential cuts. The county will address the state's revised budget proposal in its final budget, assuming the state has adopted a budget by that time. Board direction to minimize the use of the reserve for economic uncertainty offers a cushion to adjust to the effects of the state's budget plan.
- Layoffs will be necessary. Departments will work to minimize the effect on employees by offering new positions in other divisions, if possible. The first-quarter report will include an update.
- The general fund carryover at year-end, excluding reserves, was budgeted at \$20 million. Historically, the carryover has been well over \$40 million. Additional beginning fund balance may be available when the final budget is presented to the Board for adoption. This assumption envisions that some contingency funds will not be needed and can be carried forward.

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## COUNTYWIDE BUDGET SUMMATION

### COUNTYWIDE SPENDING AND REVENUE

The FY 11/12 recommended budget establishes about \$4.8 billion in appropriations for Riverside County. Countywide revenue is expected to remain stable at about \$4.4 billion. The \$386 million difference between appropriations and revenue is backed with fund balance, reserves, and designations. These sources represent revenue collected in earlier fiscal years.

The county's budget is divided into three fund groups: governmental, proprietary, and special district. Governmental funds account for basic services such as public protection, social services, and general administration. Proprietary funds reflect activities financed primarily by revenue generated from the activities themselves, such as the county hospital. Special districts are separate local governmental agencies created to perform governmental or proprietary functions within limited boundaries. When local taxes are inadequate or competing demands for existing tax dollars make it difficult for the county to provide all of the services county constituents' desire, they form special districts to pay for new or higher levels of existing services. The following table provides a fiscal year comparison of the county budget by fund group.

Table 1

#### Fiscal Year Comparison of the County Budget (In Millions)

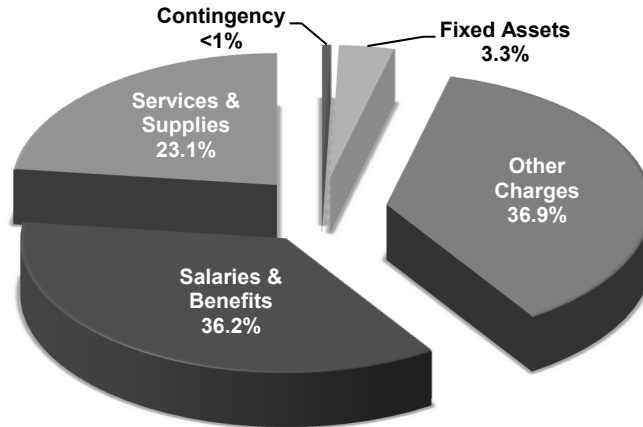
	FY10/11 Adopted Budget	FY11/12 Recommended Budget	Change (\$)	Change (%)
<b>Estimated Appropriations</b>				
Governmental funds	3,231.4	3,138.9	(92.5)	(2.9%)
Proprietary funds	926.8	956.7	29.9	3.2%
Special district funds	581.5	688.3	106.8	18.4%
<b>All County Funds</b>	<b>\$4,739.7</b>	<b>\$4,783.9</b>	<b>\$44.2</b>	<b>&lt;1%</b>

	FY10/11 Adopted Budget	FY11/12 Recommended Budget	Change (\$)	Change (%)
<b>Estimated Revenue</b>				
Governmental funds	3,050.0	2,951.0	(99.0)	(3.2%)
Proprietary funds	849.2	848.4	0.8	(<1%)
Special district funds	496.7	598.3	101.6	20.5%
<b>All County Funds</b>	<b>\$4,395.9</b>	<b>\$4,397.7</b>	<b>\$1.8</b>	<b>&lt;1%</b>

The county anticipates spending 36 percent of its resources on salaries and benefits. Another 60 percent is spent on supplies and other charges, such as payments on debt and intra-county transactions. About three percent of the county's appropriations are budgeted for the acquisition of capital assets. Chart 1 illustrates countywide spending by category.

Chart 1

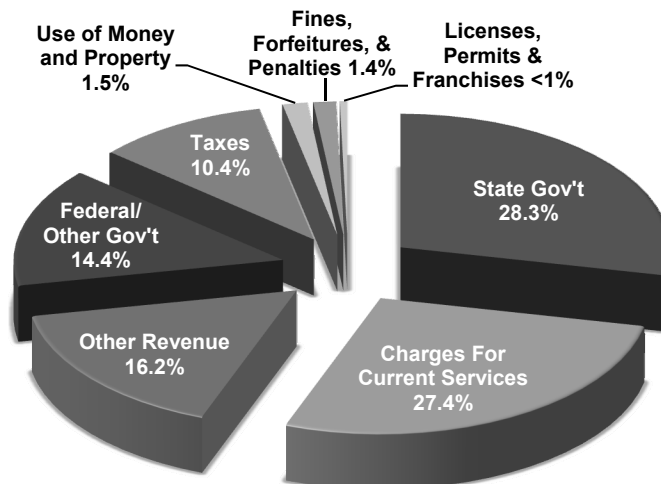
## Countywide Appropriations (by Category)



The county's largest source of revenue is derived from the state government. The smallest sources of revenue are from licenses, permits, and franchises; use of money and property; and fines, penalties, and forfeitures. Together, these sources represent less than four percent of the county's total revenue. The following chart reflects countywide revenue by its source.

Chart 2

## Countywide Revenue (by Source)



The governmental fund group accounts for most of the county's finances and includes:

- General fund - the county's basic operating fund which is used to report all operating activity not accounted for in other specialized funds.

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- Special revenue funds - used to report the operating activity associated with specific revenue sources that are restricted to a particular purpose
- Capital project funds – used to report the operating activity associated with the construction, rehabilitation, and acquisition of capital assets.
- Debt service funds – used to report activity associated with the repayment of debt.

The proprietary fund group includes internal service and enterprise funds. Internal service funds are used to account for operating activity between county departments that are supported by cost recovery. Enterprise fund are used to account for county functions that are primarily supported with user charges to external parties. The following table compares the FY 10/11 adopted budget to the FY 11/12 recommended budget and summarizes spending by fund group.

Table 2

<b>Fiscal Year Comparison of County Appropriations</b>				
<b>(In Millions)</b>				
	FY10/11 Adopted Budget	FY11/12 Recommended Budget	Change (\$)	Change (%)
<b>Governmental Funds</b>				
General fund	2,441.3	2,452.2	10.9	<1%
Special revenue funds	453.2	408.5	(44.7)	(9.9%)
Capital project funds	290.3	236.1	(54.2)	(18.7%)
Debt service funds	46.6	42.1	(4.5)	(9.7%)
<i>Total governmental funds</i>	<i>\$3,231.4</i>	<i>\$3,138.9</i>	<i>(\$92.5)</i>	<i>(2.9%)</i>
<b>Proprietary Funds</b>				
Internal service funds	369.1	350.4	(18.7)	(5.1%)
Enterprise funds	557.7	606.3	48.6	2.7%
<i>Total proprietary funds</i>	<i>\$ 926.8</i>	<i>\$ 956.7</i>	<i>\$29.9</i>	<i>3.2%</i>
<b>Special District Budgets</b>				
Community redevelopment	248.1	366.0	117.9	47.5%
IHSS Public Authority	2.7	2.6	(0.1)	(3.7%)
Parks and Open Space District	43.0	22.3	(20.7)	(48.1%)
County service areas	21.5	24.6	3.1	14.4%
Flood Control District	140.0	163.2	23.2	17.0%
Waste Management District	5.0	4.4	(0.6)	(1.2%)
Capital finance	72.1	79.6	7.5	10.4%
Cemetery District	0.5	0.9	0.4	80%
Children and Families Comm.	48.6	24.7	(23.9)	(49.2%)
<i>Total special districts</i>	<i>\$ 581.5</i>	<i>\$ 688.3</i>	<i>106.8</i>	<i>19.6%</i>
<b>Total gross appropriations</b>	<b>\$ 4,739.7</b>	<b>\$ 4,783.9</b>	<b>\$44.2</b>	<b>&lt;1%</b>

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Financing sources include all new revenue, any released reserves, and fund balance carried over from the previous year. Financing uses include all new appropriations and increases to reserves. By law, budgeted financing sources must equal financing uses. The table below summarizes the FY 11/12 recommended spending plan by financing sources and uses. In total, \$386 million in reserves and fund balance will be needed to support planned spending.

Table 3

## Summary of Sources and Uses by Fund Type (In Millions)

<b>Total Financing Sources</b>	Fund Balance and Reserve Cancellations	Financing Sources	Total Available Financing
General fund	74.8	2,377.4	2,452.2
Special revenue funds	24.1	384.5	408.6
Capital project funds	89.0	147.1	236.1
Debt service funds	0.0	42.1	42.1
Internal service funds	36.8	313.6	350.4
Enterprise funds	71.4	534.8	606.2
Special district funds	90.0	598.3	688.3
	<b>\$ 386.1</b>	<b>\$4,397.8</b>	<b>\$4,783.9</b>

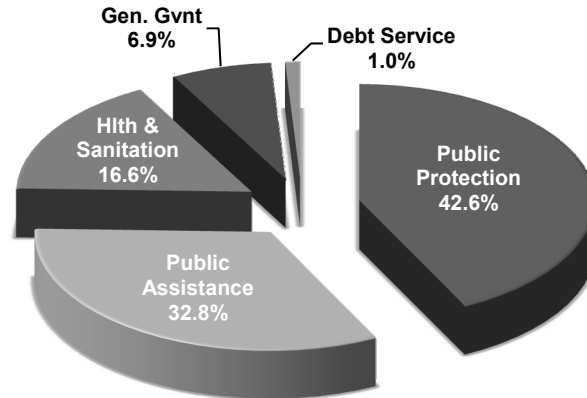
<b>Total Financing Uses</b>	Provisions for Reserves	Operating Expenditures	Total Available Requirements
General fund	2.8	2,449.3	2,452.1
Special revenue funds	0.2	408.3	408.5
Capital project funds	0.5	235.6	236.1
Debt service funds	0.0	42.1	42.1
Internal service funds	0.0	350.5	350.5
Enterprise funds	0.0	606.3	606.3
Special district funds	0.5	687.8	688.3
	<b>\$ 4.0</b>	<b>\$4,779.9</b>	<b>\$4,783.9</b>

## GENERAL FUND APPROPRIATIONS

The FY 11/12 general fund budget includes \$2.5 billion in spending authority. The chart on the next page shows general fund appropriations by function. Public protection accounts for the largest portion of general fund appropriations totaling slightly more than \$1 billion. About \$803 million is appropriated for public assistance and another \$406 million is appropriated in support of health and sanitation services. General government services account for just over \$169 million.

Chart 3

## General Fund Appropriations (by Function\*)



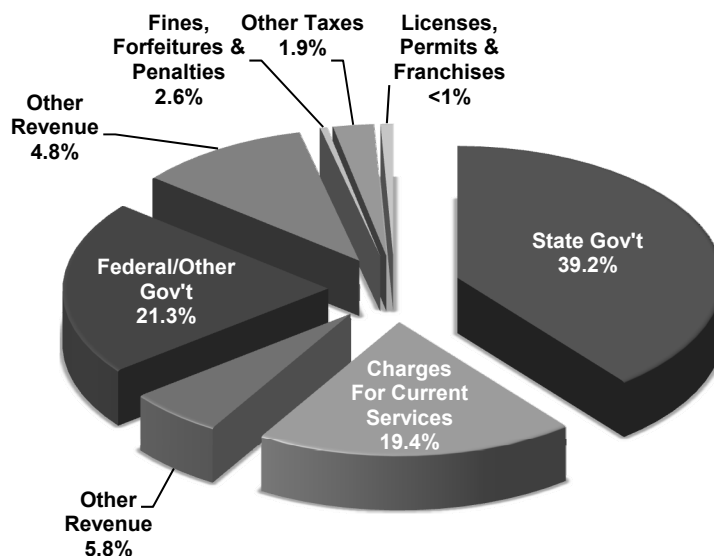
\* Functions not shown are public ways and facilities as well as education, recreation, and culture which account for less than one percent (\$2.9 million) of general fund appropriations.

## GENERAL FUND REVENUE

About \$2.4 billion in revenue is expected to support general fund operations using the county general fund. The next chart reflects all sources of anticipated general fund revenue, the largest portion of which will be received from the state (\$937 million). Revenue received from federal and other government entities totals \$507 million. The county expects to receive \$463 million from charges for services.

Chart 4

## General Fund Revenue (by Source)



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## GENERAL FUND DISCRETIONARY REVENUE

The greater part (76 percent) of general fund revenue is restricted and can only be used for the purpose it was collected. It is at the Board's discretion to determine how the unrestricted portion (24 percent) will be spent on core services. For FY 11/12, general fund discretionary revenue is estimated to be about \$582 million, a two percent decrease (\$10.1 million) from last year's budget projection. Although certain discretionary general fund revenues show signs of growth, other revenue estimates continue to weaken. The primary cause of the overall decrease was related to eroding Teeter Overflow revenue. Growth within sales tax collections would have offset this decrease except it is anticipated there will be a revenue loss associated with the newly incorporated cities. Revenue neutrality agreements with these cities will help offset these losses beginning in FY 14/15.

The following table reflects the allocation of discretionary revenue by source. A discussion of key revenue sources follows.

Table 4

### Year to Year Comparison of General Fund Discretionary Revenue (In Millions)

	FY10/11 Final Budget	FY11/12 Recommended Budget	Change (\$)	Change (%)	Percent of Revenue
Property Taxes	263.8	266.4	2.6	1%	45.8%
Motor Vehicle In-Lieu	188.8	189.0	0.2	0.1%	32.5%
Teeter Overflow	46.0	35.5	(10.5)	(22.8%)	6.1%
Fines & Penalties	25.7	27.0	1.3	5.1%	4.6%
Sales Tax*	23.0	21.3	(1.7)	(7.4%)	3.7%
Tobacco Tax	10.0	10.0	-	-	1.7%
Property Transfer Tax	9.3	10.5	1.2	12.9%	1.8%
Franchise Fees	7.0	5.0	(2.0)	(28.6%)	<1%
Interest Earnings	6.3	6.6	(0.9)	(14.3%)	1.1%
Misc. Federal & State	5.9	6.1	0.2	3.4%	1.0%
Other Miscellaneous	6.3	4.6	(1.7)	(27.0%)	<1%
<b>Total</b>	<b>\$ 592.1</b>	<b>\$ 582.0</b>	<b>(\$ 10.1)</b>	<b>(1.7%)</b>	

\* Does not include Public Safety Sales Tax

### **Property Taxes**

Property tax revenue is estimated at \$266.4 million for FY 11/12. This revenue represents 46 percent of the county's discretionary revenue and includes \$85.1 million in redevelopment tax increment pass-through funds. As property values in the county decline, this revenue falls.

### **Motor Vehicle In-lieu Fees**

Motor vehicle in-lieu revenue is estimated at \$189 million and represents about 33 percent of the county's discretionary revenue. The state converted this revenue source

to property tax revenue several years ago. This revenue is now tied to county assessed property values, just like property tax revenue.

### ***Teeter Overflow***

In 1993, the county adopted the Teeter Plan, which provides an alternate procedure to distribute property taxes. The Teeter Plan is financed, and debt service paid, as delinquent properties are redeemed. State law requires that a tax-loss reserve fund be established with a balance equal to one percent of the Teeter roll. Any delinquent collections exceeding the one percent may be transferred to the general fund. This excess is called the Teeter overflow.

Despite the frailty of the local housing and employment markets, there is a downward trend in property tax delinquency rates. Timely payment of property taxes by financial institutions that have taken ownership of distressed properties may be the primary cause. This trend, reinforced with a slow economic recovery, will continue to erode this revenue in future years. The recommended FY 11/12 budget projects this overflow to be about \$35.5 million.

### ***Court Fines and Penalties***

Fines and penalties are estimated at \$27 million. Comprising almost five percent of the county's revenue, fines and penalties are mostly dedicated to funding the county's obligation to the trial courts and are subject to state maintenance-of-effort requirements. The county continues to shift fines and fees resulting from trial-court reform to the state.

### ***Sales Taxes***

Sales and use taxes are estimated at \$21.3 million and represent about four percent of the county's discretionary revenue. This amount reflects anticipated losses of revenue associated with the incorporation of the cities of Eastvale and Jurupa Valley.

### ***Tobacco Taxes***

In 1998, when the Master Tobacco Litigation Settlement was finalized, tobacco companies agreed to pay compensation for causing tobacco-related problems across the nation. Riverside County along with other cities and counties entered into an agreement with the state regarding how California's share of the settlement was to be allocated. In 2007, the county sold bonds backed by the future stream of tobacco-tax settlement income for one lump-sum amount, reducing what it would have otherwise received to \$10 million per year. These funds are passed on to the county hospital.

## **GENERAL FUND RESERVES AND DESIGNATIONS**

The recommended budget incorporates the use of about \$55 million in general fund reserves to fund one-time and ongoing expenditures in support of general fund operations. In this budget, \$34 million in discretionary reserves (including \$7 million from the property tax system designation for the CREST project, as approved by the Board in October 2010), \$20 million in unreserved fund balance, and \$19.7 million in restricted reserves are being drawn upon to support recommended spending. Additionally, \$2.4 million will be set aside for community improvements. The table

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below depicts proposed changes to general fund reserves and expected year-end balances.

Table 5

<b>Estimated General Fund Reserves and Designations</b>			
<b>(In Millions)</b>			
Name	FY10/11 Expected Ending Balance	FY11/12 Recommended Changes	FY 11/12 Reserves and Designations
Economic Uncertainty	148.6	(27.8)	120.8
Disaster Relief	15.0	0.0	15.0
Property Tax System Replacement	17.0	(7.0)	10.0
Community Improvement	0.0	2.4	2.4
<i>Total Discretionary</i>	<i>\$ 180.6</i>	<i>(32.4)</i>	<i>\$ 148.2</i>
Restricted Reserves and Designations	<b>66.1</b>	(19.6)	53.7
<b>Total Reserves and Designations</b>	<b>\$246.7</b>	<b>(\$52.0)</b>	<b>\$202.9</b>

## GENERAL FUND DISCRETIONARY ALLOCATIONS - NET COUNTY COST

In accordance with Board policy, general fund support authorized by the Board in the previous year's final budget plus ongoing commitments approved by the Board during the year form the basis for the general fund's net county cost (NCC) allocated in the subsequent year's recommended budget. NCC represents the allocation of discretionary revenue and reserves in support of various county services. In an effort to move toward structural balance, net county costs were reduced disproportionately between departments, but overall by eight percent. For FY 11/12, NCC allocations are expected to exceed discretionary revenue by about \$28 million. The table on the next page compares ongoing net county cost for FY 10/11 and FY 11/12.

Table 6

<b>Changes in Ongoing Net County Costs</b>				
<b>(In Millions)</b>				
	FY10/11 Budget	FY11/12 Recommended Budget	Change (\$)	Change (%)
Public Protection	497.5	467.5	(30.0)	(6.0%)
General Government	34.0	25.4	(8.6)	(25.3%)
Health & Sanitation	67.4	57.8	(9.6)	(14.2%)
Public Assistance	45.9	37.2	(8.1)	(19.0%)
Education, Recreation, & Culture	1.5	1.2	(0.3)	(20.0%)
Debt Service and Contingency	39.5	41.2	1.7	4.3%
<b>Total Net County Cost</b>	<b>\$ 685.8</b>	<b>\$ 630.3</b>	<b>(\$55.5)</b>	<b>(8.1)%</b>

The largest share of discretionary resources (74 percent) is allocated to public protection (\$467.5 million). The Sheriff's Department will receive \$225.6 million. The District Attorney's Office will receive about \$58.7 million. The Fire Department, which also receives structural fire-tax revenue, will receive about \$40.6 million in general fund support. As required by state law, the county plans on spending almost \$35.1 million for individuals that have been charged with a crime and need legal representation but cannot afford to hire a privately retained attorney. Those funds are allocated to the Public Defender's Office, the Alternate Public Defender, confidential court orders, and indigent defense. The Probation Department will receive about \$29.4 million. The public ways and facilities function will not have a general fund allocation. Education, recreation, and culture make up less than one percent of general fund net county cost allocations (\$1.2 million). The chart on the next page illustrates ongoing general fund allocations by function.

Chart 5

