DEPARTMENT RECOMMENDATION

It is recommended that the Board receive a presentation regarding the USDA loan financing process and related lender requirements, as detailed above, and at the conclusion of the presentation and discussion, direct staff to update the *5 Year General Fund Budget Projection* as may be required.

Approval of recommendation #3, above, is a necessary step for the County to be able to successfully demonstrate to external creditors its ability to project, and fund, appropriations for loan payments for the Public Safety Facilities Project financing. If approved, the budget actions may have a significant impact on the County's finances and future budgets for the term of the loan.

DISCUSSION / BACKGROUND

El Dorado County's budget provides a plan to achieve service delivery goals while maintaining the agencies financial integrity, and is based upon sound financial assumptions regarding the allocation of financial resources given the revenues the county can expect to receive over the next fiscal year. The Board has adopted a budget policy that requires one-time funding should be used to support one-time expenditures. One time sources of funds should not be used to support ongoing operations. Expenditures such as capital construction, equipment replacement and operating contingencies and/or reserves are considered one-time in nature. Carryover fund balance, which results from savings in operations, is generally considered one-time funding.

A key component of the County's USDA final application process for financing the Public Safety Facility Project requires a financial feasibility analysis containing historical financial data as well as projections for 5 years of future General Fund budgets. This financial analysis should demonstrate to the interim credit market and the USDA's Credit Committee that El Dorado County has the ability to appropriate funds in the annual General Fund budget and can afford to make loan payments over the loan term.

INTERIM AND PERMANENT FINANCING PROCESS

As required by the USDA, the County will need to obtain interim financing for the construction phase of the Public Safety Facility Project, through a Grant Anticipation Note or similar type of Note financing. The interim financing could last up to 3 years. This interim financing would be obtained through a public offering with the USDA loan held as collateral, since the funds will be appropriated at the Federal level. The cost of issuance for this interim financing (bond counsel, underwriters, financial advisors, etc.) is estimated at $420,000. Interest will be charged on loan funds used to fund the construction phase of the project. Rating by a credit rating agency may be required for this financing.

Upon construction completion, the USDA will buy out the full remaining value of the interim financing through the issuance of a Certificate of Participation (COP). The COP is a common public financing tool, structured as a lease obligation of the County's General Fund, requiring an annual appropriation of funds for loan repayment. This type of financing mechanism does not require voter approval. The new Public Safety Facility will be used as collateral for the loan. At the time COPs are issued, the USDA will require the County to set aside funds in a reserve account that equates to 10% of the annual payment over a 10 year period. The first payment on the USDA loan would begin one year after the USDA takes over the lease obligation. The term of this loan could be up to 40 years. In order to qualify for this loan the County will need to demonstrate how the annual loan payments fit into the projected General Fund budget.

5 YEAR GENERAL FUND BUDGET PROJECTIONS

2016-17 Recommended Budget – "Status Quo"

On June 14, 2016 the Board approved the 2016-17 Recommended Budget. The approved Recommended Budget will accompany the final USDA final application when it is submitted.

During the budget presentation, Laura Schwartz, Chief Budget Officer, presented a *5 Year General Fund Budget Projection* schedule to brief Board members on what they could generally expect the County's financial direction to look like over the next few fiscal cycles. These figures forecasted funding deficits in FY 2018-19 through FY 2020-21 and did not include loan payments for the Public Safety Facility Project.

	FY 2016-17	FY 2017-18	FY 2018-19	^%$	FY 2019-20	^%$	FY 2020-21	^%
Revenue	$ 239,192,936	$ 245,131,926	$ 251,195,968	2.5%	$ 257,437,897	2.5%	$ 263,916,896	2.5%
Expenditures	(272,000,794)	(260,742,092)	(269,053,336)	3.2%	(277,756,808)	3.2%	(286,818,724)	3.3%
Excess Expense Over Revenue	$ (32,807,858)	$ (15,610,166)	$ (17,857,368)	2.15 M	$ (20,318,911)	2.29 M	$ (22,901,828)	2.52 M
Fund Balance	32,807,858	15,800,000	16,400,000		17,000,000		17,650,000	
Surplus/(Deficit)	**$ -**	**$ 189,834**	**$ (1,457,368)**		**$ (3,318,911)**		**$ (5,251,828)**	

Note: The FY 2016-17 Fund Balance is really $26.6 million. This table includes $6.2 million of cancelled capital reserves and excludes $3,146,003 that was identified in the June 14th presentation as these dollars were simply reallocated within in the reserve accounts.

Some areas for consideration:

1. The County's General Fund revenues are projected to grow at a steady pace over the next few fiscal cycles, however rising labor and other operating cost growth is expected to outpace the revenue growth.

2. As demonstrated in the "Excess Expense" row, forecast expenditure numbers exceed revenues every year displayed: $15.6 million (FY 2017-18) to $22.9 million (FY 2020-21). Anticipated growth in the General Fund's expenses are expected to exceed revenue growth each fiscal year, and at an increasing pace. Fund balance carryover is used to offset this trend and help balance projected budgets.

3. The FY 2016-17 Recommended Budget uses $32.8 million carryover fund balance which funds the following items: $18.6 million for re-budgeted capital projects; $5.3 million

for operating contingencies; $900,000 for one-time expenses with the $8.6 million funding budgeted salary and benefit and other department expenses. While capital projects, operating contingencies and other one-time costs are appropriate uses for carryover fund balance, ongoing salary and benefits costs are not and doing so creates a structural budget imbalance.

4. Fund balance carryover figures grow slightly each year but don't keep pace with "Excess Expense Over Revenue" growth, which results in deficits for FY 2018-19 through FY 2020-21.

The State Controller's Office, County Budget Act §29009 requires that "In the recommended, adopted, and final budgets the funding sources shall equal financing uses." As a result, every year counties and other public agencies make budget adjustments that are necessary to balance their budgets, by obligating surplus funds or eliminating deficits. The smaller the deficit, the easier it is for an agency to make adjustments to balance their annual budget. However, agencies with large or ongoing, budget deficit projections may require the implementation of operational efficiencies and/or increased cost recovery methods such as internal and/or external fee increases to balance those budgets.

"Lender" Requirements

Consistent with State Controller requirements, credit lenders also expect that an agency's current and future budget projections balance. Essentially, the USDA or any lender will require that the County demonstrates that it can repay the loan through its financial presentation. To meet this criteria, the County must address the multi-year shortfalls presented in the *5 Year General Fund Budget Projection* forecast prior to submitting a final application for financing.

Given the deficit projections noted previously, the County will need to find a way to maintain essential programs and services while implementing operational efficiencies and other measures to balance future budgets. The following table illustrates the budget constraints that would be necessary each fiscal year to mitigate these shortfalls.

Lender Requirements

	FY 2016-17	FY 2017-18	FY 2018-19	^%$	FY 2019-20	^%$	FY 2020-21	^%
Revenue	$ 239,192,936	$ 245,131,926	$ 251,195,968	2.5%	$ 257,437,897	2.5%	$ 263,916,896	2.5%
Expenditures	(272,000,794)	(260,742,092)	(269,053,336)		(276,299,440)		(282,042,445)	
Operational Efficiencies	**-**	**-**	**1,457,368**		**3,318,911**		**5,251,828**	
Subtotal Expenses:	(272,000,794)	(260,742,092)	(267,595,968)	2.6%	(272,980,529)	2.0%	(276,790,617)	1.4%
Excess Expense Over Revenue	$ (32,807,858)	$ (15,610,166)	$ (16,400,000)		$ (15,542,632)		$ (12,873,721)	
Fund Balance	32,807,858	15,800,000	16,400,000		15,542,632		12,873,721	
Surplus/(Deficit)	**$ -**	**$ 189,834**	**$ -**		**$ -**		**$ -**	
To Reserves		$ (189,834)						

In order for the County to meet lender expectations for a balanced budget, the “Status Quo” budget projections would need to be brought into balance by introducing “Operational Efficiencies” in FY 2018-19 and each subsequent year. To meet lender requirements for a balanced budget, the County’s General Fund budget would include expenditure constraints and/or revenue increases to meet the operational efficiency target as follows:

- FY 2018-19 - - $1.46 million,
- FY 2019-20 - - $3.32 million,
- FY 2020-21 - - $5.25 million.

This pattern would continue until carryover fund balance declined and operating revenues more closely aligned with expenditures.

It is important to note that the General Fund’s expenditures continue to grow each year under the “Loan” scenario, although at a much slower pace than the “Status Quo” scenario noted previously. For example, in FY 2020-21 “Status Quo” expenses are anticipated to be $286.8 million while the “Loan” expenses are estimated at $276.8 million, showing that both figures grew from FY 2017-18’s $260.7 million. When the budget is compressed with “reductions”, fund balance carryover will also begin to decline. Essentially, when flexibility or discretionary spending is reduced the budget tightens and results in less excess dollars to carry into the next budget cycle.

Public Safety Facilities Project – Loan Payments

Interim and financial lender’s financial feasibility analysis must incorporate financing costs into the *5 Year General Fund Budget Projection* and continue to maintain a balanced budget (no deficits). Current estimates place interim finance costs and interest payments at about $1 million per year for the first 3 years, and up to $2.2 million for the USDA loan each year thereafter (based on an estimated $50 million loan for 40 years at 3%). Please note that these loan figures are strictly estimates for presentation purposes, and are subject to change, as the actual loan and corresponding payment amounts have yet to be approved by the Board.

When estimated loan payment figures are added to the June 14th *5 Year General Fund Budget Projection* presentation, the budget deficit amounts increase, which will require the County to implement funding constraints in addition to those noted previously. “Loan” budget projections balance by introducing operational efficiencies starting earlier, in FY 2016-17, and continue into each subsequent year[1]. As discussed in the previous scenario, projected budgets would need to reflect operational efficiencies; however, the amounts have increased by the annual loan payment amounts:

- FY 2016-17 - - $1 million,
- FY 2017-18 - - $810,166,
- FY 2018-19 - - $2.46 million,
- FY 2019-20 - - $5.52 million,
- FY 2020-21 - - $7.45 million.

[1] The FY 2016-17 Recommended Budget includes $2.2 million in a Designation for Capital Project Reserve. These reserve funds could be cancelled by the Board and allocated to fund interim financing costs.

	FY 2016-17	FY 2017-18	FY 2018-19	^%	FY 2019-20	^%	FY 2020-21	^%
Revenue	$ 239,192,936	$ 245,131,926	$ 251,195,968	2.5%	$ 257,437,897	2.5%	$ 263,916,896	2.5%
Expenditures	(272,000,794)	(259,742,092)	(267,243,170)		(273,489,274)		(277,032,279)	
Loan Payments	(1,000,000)	(1,000,000)	(1,000,000)		(2,200,000)		(2,200,000)	
Operational Efficiencies	**1,000,000**	**810,166**	**2,457,368**		**5,518,911**		**7,451,828**	
Subtotal Expense:	(272,000,794)	(259,931,926)	(265,785,802)	2.3%	(270,170,363)	1.6%	(271,780,451)	0.6%
Excess Expense Over Revenue	$ (32,807,858)	$ (14,800,000)	$ (14,589,834)		$ (12,732,466)		$ (7,863,555)	
Fund Balance	32,807,858	14,800,000	14,589,834		12,732,466		7,863,555	
Surplus/(Deficit)	**$ -**	**$ -**	**$ -**		**$ -**		**$ -**	

In September the Board will be asked to consider adopting the FY 2016-17 County Budget. Staff will likely recommend that the Board direct excess carryover fund balance, identified since the Recommended Budget was approved on June 14th, toward the Public Safety Facility Project in an effort to reduce the final loan and annual loan payment amounts, which would then reduce the amount of future budget reductions that would be necessary.

The General Fund's budgeted expenditures are still expected to grow each year under the "Loan" scenario, just at a much slower pace than noted previously. For example, in FY 2020-21 "Status Quo" expenses are anticipated to be $286.8 million while the "Loan" expenses are budgeted at $271.8 million, showing that both figures grew from FY 2017-18's $260.7 million. When the "Loan" budget is compressed with reductions, fund balance carryover declines more rapidly. The more constrained budget results in less excess dollars to carry over into the next budget cycle.

To successfully accomplish the financial goals within the "Loan" scenario the County will need to implement a number of budget policy changes to constrain expenditure growth. These measures might include a reallocation of funding toward County priorities; constrained hiring and labor costs; streamlining programs and services; outsourcing functions that are more cost efficient and/or reducing funding currently allocated to external agencies.

OPERATIONAL EFFICIENCIES / COST RECOVERY

Over the last several years many California counties have implemented funding restrictions due to flat or declining revenue streams and rising labor and other operating costs. Recognizing the effects of these same economic indicators on El Dorado County, the CAO recommends taking steps now to prepare departments for budget actions that will be needed for the agency to live within its means in 2017 and beyond. Emphasis will be placed on maintaining critical programs and services, preserving current staffing and service levels where possible, and reducing expenditures to match anticipated revenue where necessary.

Over the next few months, the CAO will meet and begin discussions with county department heads and their key staff to identify efficiencies in service delivery, reductions in operating costs where possible, and other cost recovery options.

USDA APPLICATION

On November 18, 2015 the USDA responded to the Chief Administrative Office, Facilities Division, loan pre-application indicating that the proposal met their basic eligibility requirements for financial assistance through the Community Facilities Program. When the USDA pre-application was submitted staff had broadly identified the scope of the Public Safety Facility Project and related costs. To proceed with the USDA final application and ultimately project construction, detailed information is required and an up-to-date cost analysis must be completed.

In order to begin the next phase in this process, El Dorado County needs to determine a realistic budget and repayment plan, before constructing this capital project. It is for this reason project construction phases and related costs will be outlined for the Board of Supervisor's consideration at the July 11, 2016 meeting. Upon Board approval of the facility size, costs, and financing, this information will then be inserted into the final USDA application, submitted to the Board for approval at its July 26th meeting, and then relayed to the USDA. As a Federal agency, the USDA's fiscal year ends September 30th. Since the local USDA management team does not have the authority to approve a loan of $50 million, the application must be forwarded to the USDA's national office for final review and approval.

USDA interest rates are adjusted quarterly and the interest rate for July 1st through September 30th was released at 2.75%. While the maximum term on a USDA loan is up to 40 years, a shorter term is available if requested by the Board. The County could be required to contribute up to 15% of the project cost as a match to the project; however, it is possible that a lower match amount could be approved by the USDA. Purchase of the site, some consultant contract costs and interim financing costs can be applied to this match requirement.

PUBLIC SAFETY FACILITY PROJECT

In 2013 Vanir Construction Management prepared *The Sheriff's Operational Assessment and Facility Study* which outlined Sheriff Department capital facility uses and current and future needs. One critical element identified in the Study was replacement of the 22,000 square foot Sheriff's Administration building since that facility was clearly at the end of its useful life. The Board of Supervisors identified replacement of the Sheriff's Administration facility as a top priority for the County, and agreed to consider consolidation of other Sheriff functions, currently operating out of seven other facilities, into one new replacement facility.

On March 8, 2016 the Board of Supervisors approved $2.56 million for the acquisition of 30.73 acres of land for the new public safety facility site. The parcel is located in the Diamond Springs area of unincorporated El Dorado County at Industrial Drive.

On April 19, 2016 the Board directed staff to take steps necessary to file a USDA application to finance the Public Safety Facility construction.

On July 11, 2016, staff will present the Architectural Nexus (Arch Nexus) schematic project design, the project cost estimates, and will identify construction timeline projections for the Public Safety Facility Capital Project. At the close of the presentation, staff will ask the Board to consider approval of the project size and its estimated project cost, as well as related loan and annual loan payment amounts. This action is required prior to the final application submittal to the USDA.

OTHER DEPARTMENT / AGENCY INVOLVEMENT

Facilities Finance Committee

CAO RECOMMENDATION

The Chief Administrative Office Concurs with the recommendation.

FINANCIAL IMPACT

Board approval of the requested action directs staff to reflect the operational efficiencies in the *5 Year General Fund Budget Projections* that are necessary to bring the General Fund's projected budgets into balance when interim ($1 million / year estimated) and permanent ($2.2 million / year estimated) loan payments are added. These loan payment figures are strictly for presentation purposes and are subject to Board action on July 11, 2016. The County Budget Act requires public agencies adopt a balanced budget annually.

CLERK OF THE BOARD FOLLOW UP ACTIONS

N/A

STRATEGIC PLAN COMPONENT

Infrastructure

CONTACT

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