



# WASHOE COUNTY

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CM/ACM \_\_\_\_\_  
Finance \_\_\_\_\_  
DA \_\_\_\_\_  
Risk Mgt. \_\_\_\_\_  
HR \_\_\_\_\_  
Other \_\_\_\_\_

## STAFF REPORT

BOARD MEETING DATE: December 8, 2009

**DATE:** December 6, 2009  
**TO:** Board of County Commissioners  
**FROM:** John Sherman, Finance Director  
**THROUGH:** Katy Simon, County Manager  
**SUBJECT:** **Fiscal Year 2010/11 Budget Discussion including Preliminary Revenue Outlook and Direction to Staff. (All Commission Districts)**

### SUMMARY

Washoe County's fiscal condition remains stable but guarded for the current fiscal year. Barring a dramatic decline in sales tax for the rest of the year or unforeseen circumstances such as legislative action due to a Special Session and litigation, we do not anticipate further budget reductions this fiscal year. We have realized this stability because of the aggressive budget actions taken by the Board to reduce expenditures and the many sacrifices made by all County employees.

Still, Washoe County is experiencing the worst economic conditions since the Great Depression. The housing market has collapsed punctuated by one of the highest foreclosure rates in the country and the existing single family home value has fallen from its peak of \$350,000 in 2005 to \$182,950 in 2009. Unemployment is above 12% with 21,000 jobs lost in the valley since the peak in late 2007. All of which have driven down retail consumption, property values and equity, and consequently Washoe County's two major revenue sources: sales tax and property tax.

The preliminary revenue outlook for fiscal year 2010/11 indicates that the County will again be challenged to stabilize the organization and maintain services to the public. The outlook for the key revenue sources include:

- Property taxes are projected to be down between 7% and 12%.
- Sales taxes, which are extremely volatile to project at this time, could be flat or see slight growth if we assume the bottom has been reached. On the other hand, depending on what happens in the labor and housing markets, sales taxes could continue to decline by as much as 7%.
- Combined the County General Fund could potentially see a loss in sales and property tax revenue that ranges from \$9.5 million to \$24.5 million for Fiscal Year 2010/11.

In addition, the County will still be required to send about \$5.5 million General Fund property tax revenue to the State and all the capital facilities property tax revenue to the State. Lastly, there will be upward pressure on expenditures for items such as health

insurance costs, deferred infrastructure maintenance needs, indigent medical, merit pay, indigent defense, and longevity pay. On January 26, 2010, Staff will bring the Board a comprehensive outlook of revenues, expenditures, and the first estimate of the General Fund deficit that will need to be closed to balance the Fiscal Year 2010/11 budget.

This staff report is to begin the discussion on crafting the stabilization plan for Fiscal Year 2010/11, a plan that will continue our efforts of orienting the organization on a path toward long-term financial sustainability. With deep budget reductions for the last three years, guiding goals for the stability plan should be preservation and maximization. Preservation of the services provided to the public, preservation of jobs, and maximization of talent and resources. The major objective of the stability plan should be to align current expenditures with current revenues on an ongoing basis. To achieve this, the plan needs to evaluate:

- Services provided and department funding levels;
- Per employee cost to provide services; and
- Resources.

Today, we want to review the priority based approach we have used to manage services provided and department funding levels through these difficult times. We want to begin the consideration of alternatives to that approach, which should be informed by the Budget Policies and could be deployed for Fiscal Year 2010/11 stabilization and sustainability plan.

This is the first in a series of the formal discussions on the budget and we are not requesting that the Board make a decision on how to prioritize the budget for next year. We want to begin the public dialogue to allow adequate time for broad-based input and deliberation as we plan the next steps to stabilize and manage the continued delivery of services to the public through this deep recession.

County Priority supported by this item: Improve efficiency and financial stability of Washoe County.

### **PREVIOUS ACTION**

#### **May 18, 2009            The Board adopted the Fiscal Year 2009/10 Budget**

The Fiscal Year 2009/10 General Fund Budget was balanced closing the \$47 million deficit with a combination of labor cost concessions, programmatic budget reductions, and strategic use of financial reserves. The impacts of balancing the budget were substantial and represented structural changes that cut across all departments.

Major sacrifices have been made by Washoe County employees to help balance this budget:

- The Washoe County Employees' Association (WCEA) members agreed to a 2.5 percent wage reduction into December 2009;
- Management, confidential employees, Law Library employees, and Juvenile Services employees have all taken this same wage reduction;

- The Elected Officials, Nurses Association and Justices Courts employees have agreed to cost sharing health benefit costs through June 30, 2010;
- The employees of the Library, Parks, Technology Services and many other departments will be taking nearly a half million dollars in voluntary wage reductions; and
- District Court employees are also taking a 2.5 percent wage reduction.

In total, these sacrifices will produce more than \$4 million in savings for the fiscal year. In addition to these employee sacrifices, balancing the budget required:

- About 300 positions to be defunded, more than 90 of which required layoffs.
- An additional 144 employees took voluntary separations, and another 65 vacant positions were frozen.
- Overall, staffing was reduced by 14 percent in the General Fund and in many departments staffing reductions were as high as 25 to 35 percent of positions.
- For Fiscal Year 2009/10, department budgets were reduced on average by 11 percent from Fiscal Year 2008/09 adopted budgets.

**June 23, 2009            The Board amended the Fiscal Year 2009/10 Budget to absorb property tax and revenue shifts to the State**

The 2009 Legislative Session diverted more than \$25 million in revenue to the State over the next two fiscal years.

- AB 543 diverted 4 cents of General Fund property tax revenue to the State for the next two fiscal years, a combined loss of \$11 million.
- AB 543 diverted all 5 cents of the city and county shared capital facilities property tax to the State for the next two fiscal years. The combined loss for the biennium is \$9.9 million.
- The Legislature increased the gross sales tax retained by the State by increasing the administration fee by one percentage point resulting in an ongoing loss of sales tax revenue estimated at \$750,000 annually.
- The 2009 Legislative Session sustained the 25<sup>th</sup> Special Session redirection of 1 cent of property tax for indigent accident medical care for the current fiscal year causing a combined impact of \$2.9 million.

A short-term approach to strategically redirect restricted savings was used to offset the revenue diversions in the amended Fiscal Year 2009/10 Final Budget.

- Redirected savings accrued to pay for the long-term costs associated with Sheriff's Deputies heart-lung disability claims.
- Redirected savings accrued to respond to public health emergencies such as the West Nile Virus.
- Deferred the construction of a new Sparks Justice Court Facility.

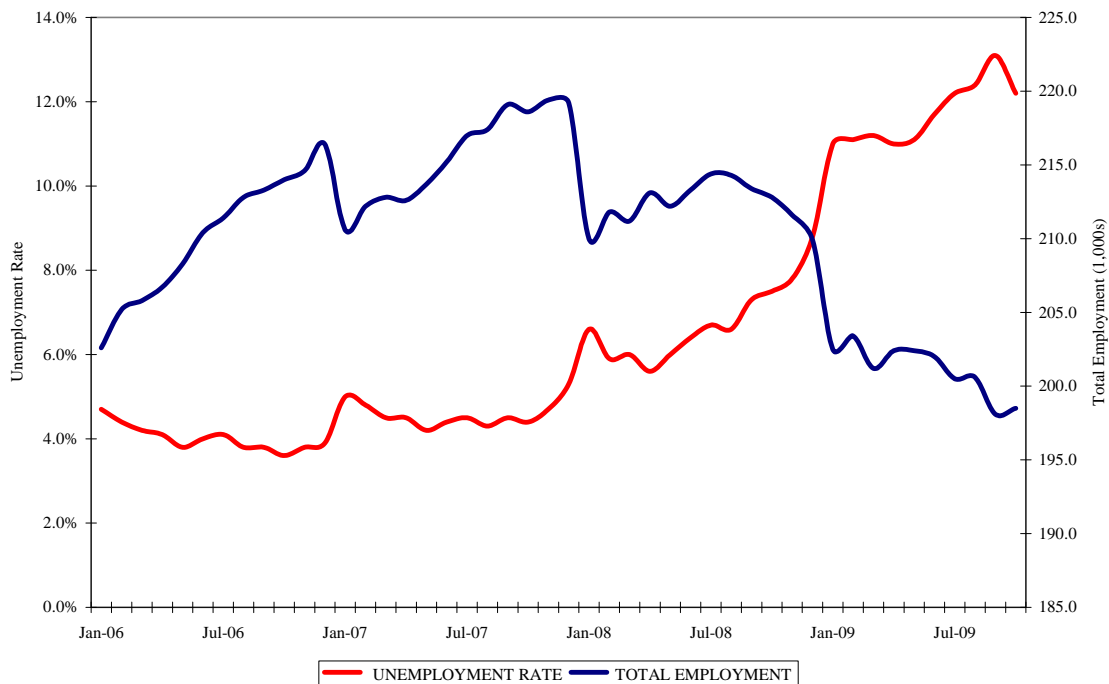
## **BACKGROUND**

### ***Economic Condition***

While Washoe County's fiscal condition remains stable but guarded for the current fiscal year, the local economy remains exceedingly weak. Key economic indicators show the County is in a deep and sustained recession characterized by high unemployment, job losses, and a housing market collapse. In the employment sector, job losses continue with a total of 21,000 jobs lost since the peak; and although the unemployment rate softened slightly in October, it still remains well above the 10% national average at 12.2%. The graph below shows Washoe County's total employment and unemployment rate.

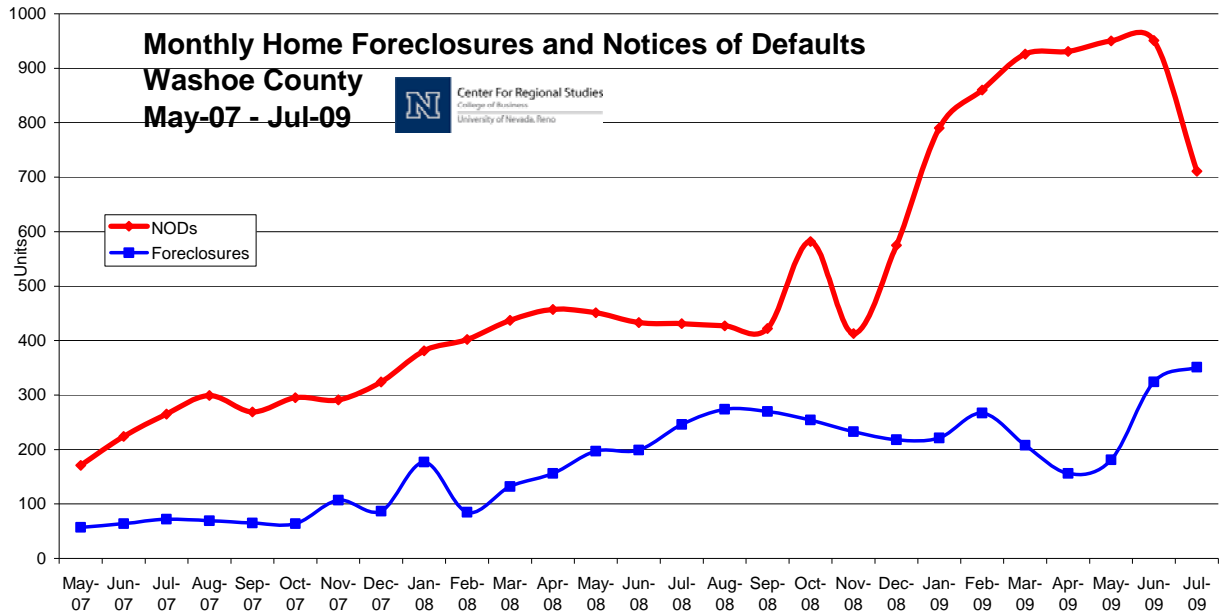
### **Exhibit 1:**

**Washoe County Employment and Unemployment Rate 2006 to Present**

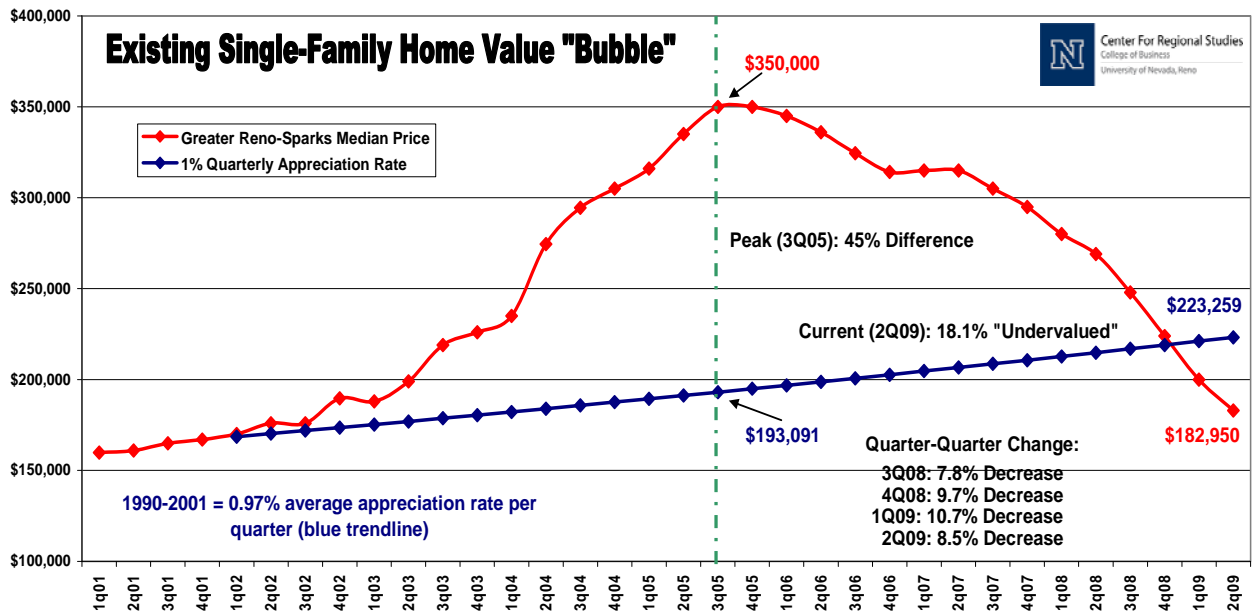


The housing market remains depressed with the worst declines on record. Through July 2009, notices of default and foreclosures were at all-time highs and still trending upward. A housing market overwhelmed by foreclosed property has returned the value of existing single family homes back to the 2002 level. The following two graphs provided by the UNR Center for Regional Studies illustrate the poor conditions of the local housing market.

**Exhibit 2:**



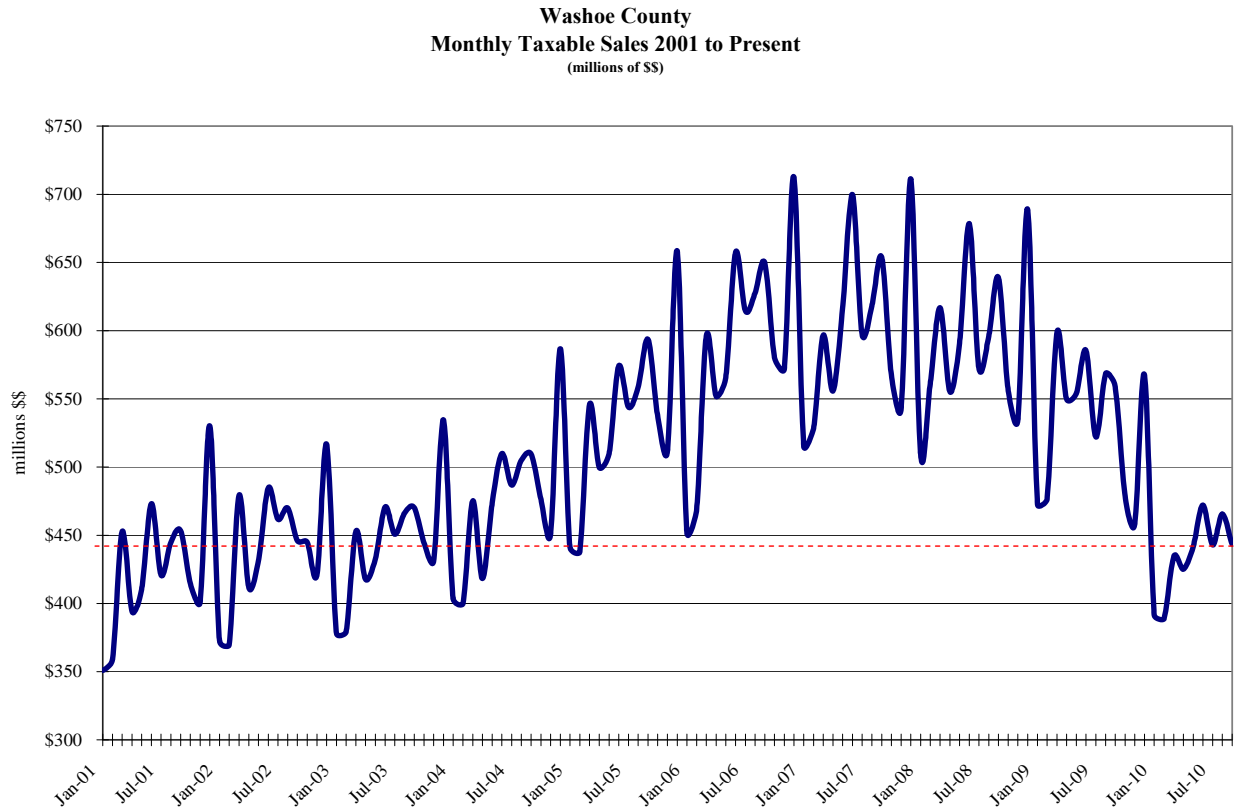
**Exhibit 3:**



The distressed labor and housing markets have negatively impacted people’s financial condition and hence their ability or willingness to spend causing taxable sales to decline all the way back to 2000/2001 levels. Taxable sales began an accelerating decline in 2007. As of September 2009, Washoe County’s taxable sales have declined for 30

consecutive months with the last 13 months declining at a double digit rate. The most recent month fell 20.64%. Exhibit 4 shows the precipitous decline in taxable sales.

**Exhibit 4:**



***Preliminary Revenue Outlook for Fiscal Year 2010/11***

The preliminary revenue outlook for Fiscal Year 2010/11 indicates that the County will again be challenged to stabilize the organization and maintain services to the public.

- Property taxes are projected to be down between 7% and 12%.
- Sales taxes, which are extremely volatile to project at this time, could be flat or see slight growth if we assume the bottom has been reached. On the other hand, depending on what happens in the labor and housing markets, sales taxes could continue to decline by as much as 7%.
- Combined, the County General Fund could potentially see a loss in sales and property tax revenue that ranges from \$9.5 million to \$24.5 million for Fiscal Year 2010/11.

The preliminary revenue outlook for the three scenarios is summarized in Exhibit 5.

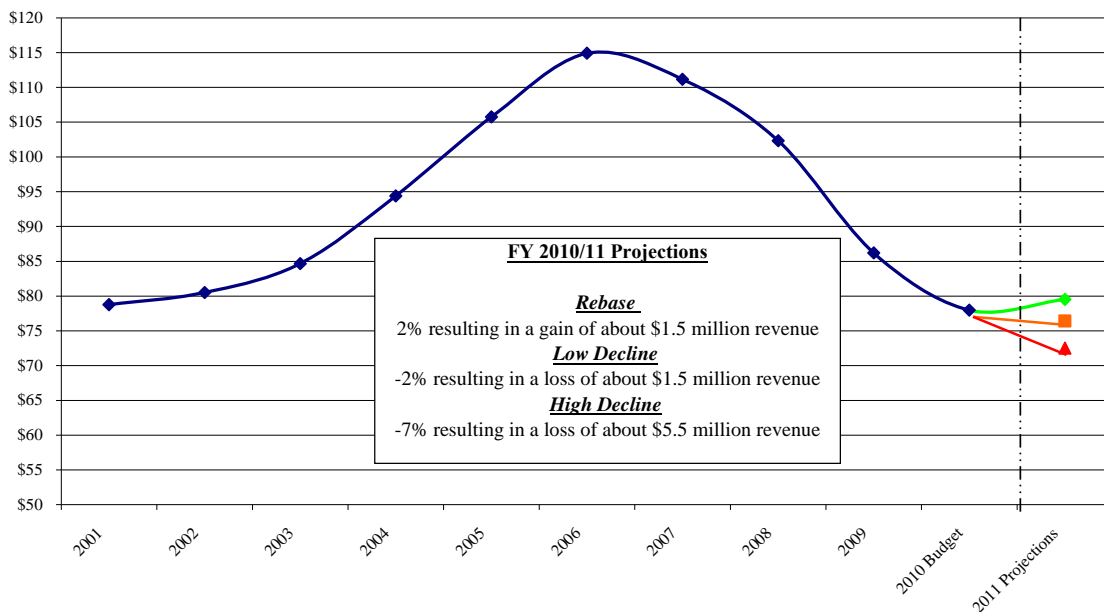
**Exhibit 5:**

<b>Preliminary Revenue Outlook FY 2010/11</b>			
<b>General Fund Combined Change in Property and Consolidated/AB104 Taxes</b>			
	<b>Property Tax</b>	<b>CTX/AB104</b>	<b>Combined Preliminary Revenue Change</b>
Scenario 1: Low Decline	-\$11 million	\$1.5 million	-\$9.5 million
Scenario 2: Med Decline	-\$14 million	-\$1.5 million	-\$15.5 million
Scenario 3: High Decline	-\$19 million	-\$5.5 million	-\$24.5 million

The anticipated decline in revenue for Fiscal Year 2010/11 continues a decline that began in Fiscal Year 2007/08. In that fiscal year, Washoe County began experiencing declines in consolidated taxes and AB 104 taxes, which are mostly sales tax based. Since that time, consolidated taxes and AB 104 taxes have fallen from about \$115 million per year to \$78 million per year, a decline of nearly 33%. Sales tax revenue to the County are now below 2000/01 levels. Exhibit 6 illustrates the declines in consolidated taxes and AB 104 taxes and shows the scenario projections for Fiscal Year 2010/11.

**Exhibit 6:**

**General Fund Consolidated Taxes and AB 104 Revenue  
with Preliminary Outlook for FY 2010/11**  
(in millions of \$\$)

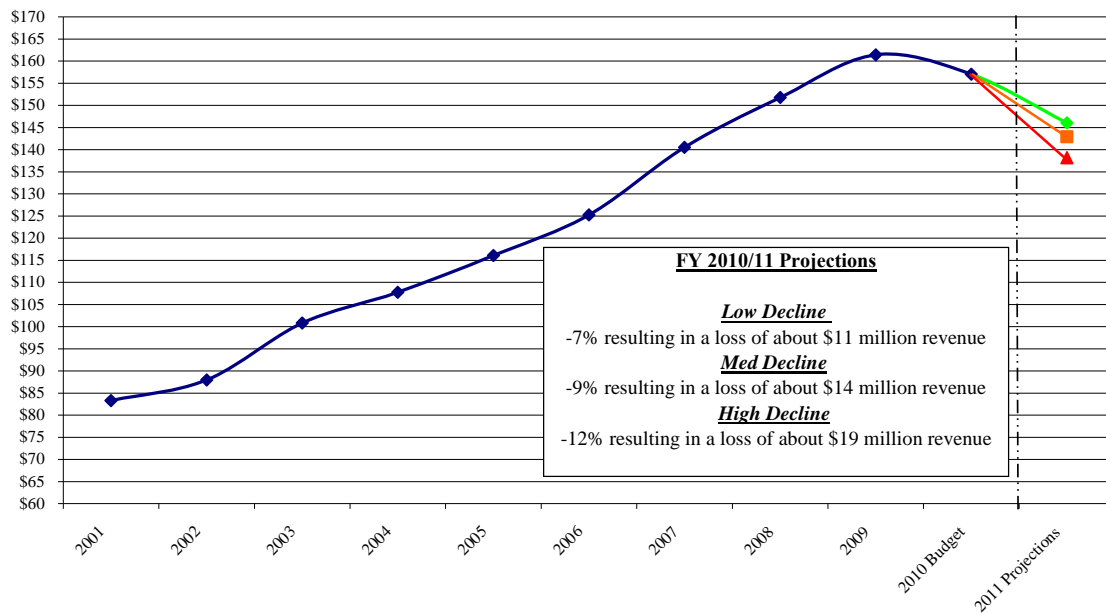


This loss in sales tax revenue has changed the make up of revenue support in the General Fund. Consolidated taxes and AB 104 taxes used to constitute around 40% of General Fund revenue and they are now down to less than 25% of total revenue.

At the same time, the County's reliance on property tax revenue to support operations has increased from about 40% of General Fund revenues in Fiscal Year 2007/08 to an estimated 55% in Fiscal Year 2010/11. This is notable because for Fiscal Year 2010/11, the impacts of the housing market collapse will result in a loss of property taxes substantially impacting the General Fund. Exhibit 7 displays the trends of General Fund property tax revenue with the projection scenarios for next fiscal year.

**Exhibit 7:**

**General Fund Property Tax Revenue  
with Preliminary Outlook for Fiscal Year 2010/11**  
(millions of \$\$)



***Expenditure Expectations for Fiscal Year 2010/11***

Changes in revenue are one-side of balancing the budget. The County will also experience changes in expenditures next fiscal year. Although estimates for expenditure changes are still being determined, there are some specific and general costs that are known. The County will still be required to pay the revenue derived from four cents of the General Fund property tax rate to the State resulting in an estimated loss of \$5.5 million. The diversion of the revenue derived from the full five cent capital facilities property tax rate to the State also remains for Fiscal Year 2010/11. Lastly, there will be upward pressure on expenditures for items such as:

- Health insurance costs
- Indigent medical
- Longevity pay
- Incline property tax litigation
- Deferred infrastructure maintenance needs
- Merit pay
- Indigent defense

On January 26, 2010, Staff will bring the Board a comprehensive outlook of revenues, expenditures, and the first estimate of the General Fund deficit that will need to be closed to balance the budget.

### ***Stabilization and Sustainability Plan***

Washoe County has faced and met the challenge of balancing its budget for the last three-years using budget prioritization as a way to manage budget reductions. We will again face the challenge of balancing the budget next fiscal year. This means past budget reductions will have to be sustained. Therefore a practical approach to begin the budgeting process would be to allow departments to flexibly reallocate current resource levels; however funding will not be available to increase resource levels with the possible exception for statutory or contractual obligations. It also means additional expenditure reductions will be necessary for Fiscal Year 2010/11.

A short-term stabilization and long-term sustainability plan should guide the policy choices to balance the budget. This plan should be informed by the Budget Policies adopted last year by the Board and address three broad areas:

- Services provided and department funding levels;
- Per employee cost to provide services; and
- Resources.

With deep budget cuts to services and employees in the last three years, it is recommended that the guiding goals for the stabilization and sustainability plan should be preservation and maximization. Preservation of the services provided to the public, preservation of jobs, and maximization of talent and resources. The major objective of the plan should be to align current expenditures with current revenues on an ongoing basis. Staff will bring forward the outlines of the plan at the January 26, 2010 Board meeting.

### ***Budget Prioritization***

Today we would like begin a discussion about one component of the stabilization plan, how budget prioritization has been used to reduce department funding levels and how that may be modified. The Board has established four broad groups to prioritize the reduction of department budgets.

- Public Safety
- Judicial/Health/ Social Services
- General Government including Legislative/Executive/Administrative Operations
- Culture and Recreation

Prior to the creation of the priority groups, budget reductions were done primarily on an “across the board” basis. The handicap of this approach was the lack of differentiation between services. Treating all funding units as equal did not give full consideration to

the varied imperatives for which a service existed such as legal mandates, voter direction, Board policy, etc. Therefore, in 2003 the Board established the Charting Our Course Committee made up of community leaders, commissioners, department heads, and bargaining group representation to develop criteria that could be used to prioritize budget choices. The criteria created by the Charting Our Course Committee and adopted by the Board, along with citizen surveys, helped inform the prioritization groupings that now exist and have been used three times to balance the budget:

- Fiscal Year 2008/09 Adopted Budget;
- Fiscal Year 2008/09 Mid Year Budget Reductions; and
- Fiscal Year 2009/10 Adopted Budget.

Based on experience and feedback from Department Heads, advantages and disadvantages have been observed about using budget prioritization.

#### Advantages

- Prioritization is an effective method to balance the budget, it clarifies choices and provides direction;
- Prioritization recognizes that the public values services differently; and
- Prioritization sets clear funding targets that direct departments to provide information to the Board about the impacts of budget reductions helping the Board to make more informed choices.

#### Disadvantages

- The reduction percentage point difference between the priority groups has been too great;
- The compound impact of repeatedly reducing one group more than another has to be considered; and
- The services provided by some departments may not clearly align with one priority group.

Absent a fundamental change in direction, some form of budget prioritization should continue to be used for fiscal year 2010/11. However, if no modifications are made to the current prioritization system, certain services will be cut to the point where they are no longer viable. For example, the percentage reduction range for fiscal year 2009/10 was:

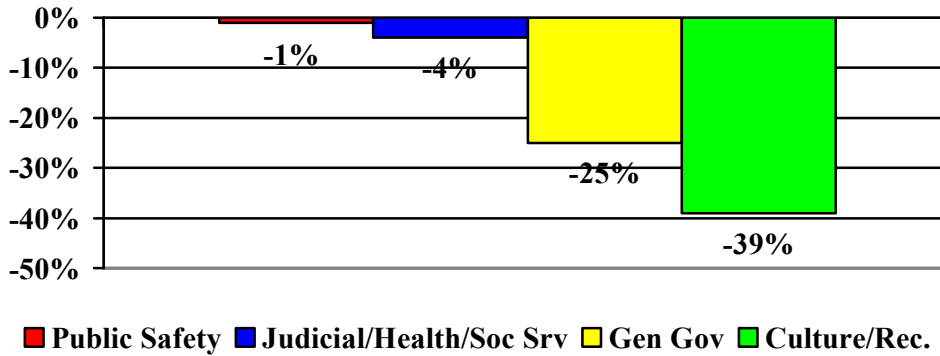
- 6% for the public safety group
- 12% for judicial/health/social services
- 28% general government, and
- 36% for the culture and recreation group

Repeating a relative reduction difference this large for a fourth time will again disproportionately cut services.

Since the priority groups began being used in fiscal year 2008/09, the percentage change in adopted budgets for each of the groups has changed in line with the prioritization, but at quite different rates as can be seen in Exhibit 8.

**Exhibit 8:**

**General Fund Priority Groupings Percent Change in Adopted Budget Fiscal Year 2008 to Fiscal Year 2010**



Understanding how the allocation of resources in the General Fund has changed since prioritization began in Fiscal Year 2007/08 can help to inform the choices about modifying the prioritization approach. Exhibit 9 below shows the percent of General Fund total for each group. The light green shaded column marks when prioritization began.

**Exhibit 9**

Allocating "The Pie" Percent of Total General Fund Budget By Priority Group FY 2005 to FY 2011 Hypothetical							
Priority	FY 2005 Adopted	FY 2006 Adopted	FY 2007 Adopted	FY 2008 Adopted	FY 2009 Adopted	FY 2010 Adopted	FY 2011 Model
Public Safety	30.8%	30.5%	30.5%	31.5%	32.8%	35.7%	39.8%
Jud./ Health/ Soc.	29.2%	28.4%	29.0%	28.4%	30.1%	31.4%	32.7%
Gen Gov.	32.1%	32.6%	32.1%	32.0%	30.0%	27.2%	23.1%
Culture/Rec	7.9%	8.5%	8.4%	8.1%	7.1%	5.7%	4.3%
<b>Totals</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

The data above clearly illustrates that as funding has been reduced for all groups, it has been done in a prioritized manner. The last column in yellow shows what the percent of total may look like if no changes are made for fiscal year 2010/11. The questions this data raise are:

- Would continuing past practices without any changes continue to reflect the desired priority based allocation of resources?
- How do we continue to prioritize and maintain a balance in the services that meet our community's needs?

Staff suggests alternative options of prioritization be considered. Many different alternatives could be pursued. Below are four possible options developed based on the input from Department Heads:

- Scenario A: 1 percentage point difference between the groups;
- Scenario B: Cap the maximum percentage point difference between the top and bottom at 10 percentage points;
- Scenario C: Apply the same percent reduction to all groups; and
- Scenario D: Prioritize programs and services based strictly on State and Federal mandates.

We have modeled what the allocation of General Fund resources would look like for scenarios A, B, and C in Exhibit 10. Currently, scenario D has not been modeled for two reasons. One reason being the complexities of measuring the cost to provide State and Federal mandates; and two, the difficulty of balancing with the funding for many functions that, while not strictly mandated in State or Federal law, are needed to provide mandates such as critical infrastructure maintenance and support services.

**Exhibit 10:**

<b>Comparison of Percent of General Fund Budget For Each Prioritization Scenario</b>				
<b>Priority</b>	<b>Scenario A (1% diff)</b>	<b>Scenario B (up to 10% Δ)</b>	<b>Scenario C (equal)</b>	<b>Current FY 10 Adopted</b>
Public Safety	36.1%	36.9%	35.7%	35.7%
Jud./ Health/ Soc.	31.4%	31.4%	31.4%	31.4%
Gen Gov.	26.9%	26.4%	27.3%	27.3%
Culture/Recreation	5.6%	5.3%	5.7%	5.7%
<b>Totals</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

Under scenarios A and B resources continue to be prioritized toward the top two groups, however at a slower rate. Scenario C holds the current allocation of resources constant, which is reflected in the yellow shaded column. The imbedded assumption of Scenario C is that the General Fund budget has been reprioritized, which could be supported by Exhibit 9 above.

There are many other options that could be modeled. The information we are providing today is the first in a series of the formal discussions on the budget and we are not

requesting that the Board make a decision on how to prioritize the budget for next year. We want to begin the public dialogue to allow adequate time for broad-based input and deliberation as we plan the next steps to stabilize and manage the continued delivery of services to the public through this deep recession.

**FISCAL IMPACT**

There is no fiscal impact directly related to this item. The fiscal impacts will be related to the Fiscal Year 2010/11 budget and reflected in the final adopted budget.

**RECOMMENDATION**

It is recommended the Board acknowledge the staff report on Fiscal Year 2010/11 budget discussion including preliminary revenue outlook and provide direction to staff.

**POSSIBLE MOTION**

Should the Board agree with Staff's recommendation, a possible motion would be acknowledge the staff report on Fiscal Year 2010/11 budget discussion including preliminary revenue outlook, and provide direction to staff including \_\_\_\_\_.