December 6, 2022

Marin County Board of Supervisors
3501 Civic Center Drive
San Rafael, CA 94903

SUBJECT: County Budget and Continuous Improvement Update

Dear Supervisors:

RECOMMENDATION:
1. Accept the Administrator’s report

OVERVIEW
The County has a history of strong fiscal management practices, and bond ratings agencies have cited this sound fiscal management and proactive approach to reducing unfunded liabilities as primary reasons for the maintaining the County’s AAA rating. Your Board’s Fiscal Policies reflect key long-term financial stability principles, such as matching one-time revenues with one-time expenses and maintaining adequate reserve levels.

In June, your Board approved a $716 million all-funds budget for FY 2022-23 that includes significant investments in the community’s highest priorities. The adopted budget included $5.0 million in ongoing General Fund enhancements to address priorities such as climate change and sea level rise, emergency response and the reorganization of the County’s Office of Emergency Services; enhanced permanent supportive housing support for formerly homeless residents; and enhancements to public communications, and more. Additionally, historically high levels of General Fund savings supported over $31 million in one-time initiatives to address affordable housing and public facility improvements, local matching funds for road improvement projects, and increased contributions to capital and technology improvement projects, among others.

COUNTYWIDE PRIORITIES
Our goal in developing the budget is to support and address our top community priorities, which include the following:

- Improving disaster preparedness
- Building a racially equitable community
- Reducing carbon emissions and adapting to climate change
- Preserving and increasing affordable housing
- Investing in county infrastructure
- Addressing recruitment and retention
To remain responsive during uncertain economic times, we must build upon the progress we have made, adapt to changing conditions, and continually improve services provided to our residents. The pandemic highlighted many of the challenges that our residents face when seeking critical services. It has also shown that developing partnerships with residents, non-profits and our cities and towns is vital if we are to leverage external resources and develop creative solutions to our emerging needs.

**FOCUS ON RACE EQUITY AND CONTINUOUS IMPROVEMENT**

Consistent with prior practice and direction from the Board, we now shift our focus in the second year of the two-year budget cycle towards strategic planning efforts with an overall goal of integrating race equity and continuous improvement into our operational culture. Through this process, we hope to update our budget workplans to better address Board and community needs, as well as to regain momentum – challenged by the COVID-19 pandemic and staffing challenges – toward a data-driven management culture that better integrates our continuous improvement efforts, including Marin Compass and Race Equity, with the budget process and our daily work.

To achieve this, departments will work with the County Administrator’s Office during mid-year review meetings in a strategic assessment of our needs and goals. Informed by this assessment, each department will highlight at least one continuous improvement effort for FY 2023-24 among the following:

1) An externally-focused indicator of service delivery
2) An assessment of race equity, using resources and support from the Office of Equity
3) A cross-departmental effort aimed at addressing critical needs
4) An internally focused business-process improvement that leads to improved customer service.

Our focus on continuous improvement reflects our ongoing responsibility to communicate and demonstrate the value of the public’s investments as well as to provide accountability to your Board. Through this review process, we plan to build a foundation that will inform priorities for FY 2023-24 and beyond, potentially also supported by a new Resident Survey and Employee Survey during 2023. We look forward to providing an update and receiving feedback on these efforts during the March Budget Workshop.

**NEXT YEAR’S BUDGET IS STABLE BUT INCLUDES STATE BUDGET RISKS**

Although local revenues will likely remain stable for the next 12 months, the projected state budget deficit will likely reduce or flatten the level of revenue we receive from the state. Given this uncertainty, staff will return to your Board with a multi-year budget projection after the Proposed Governor’s budget is presented in January.
The State is primarily financed by income tax, sales tax and corporation taxes, several of which have been negatively impacted by financial market losses in 2022. Recently, the Legislative Analyst’s Office (LAO) released its economic forecast for the state’s FY 2023-24 budget and is projecting a $25 billion deficit, largely due to significantly reduced revenue expectations and the threat of a recession.

The LAO’s projections incorporate current year revenue shortfalls of approximately $7 billion as of October, largely due to lower proceeds from capital gains and personal income tax receipts. The forecast also includes inflation only where it is referenced in current law and therefore may understate the rising cost of providing baseline services. As noted by the LAO, if we enter a significant recession in the coming year, or inflation continues to rise, the deficit will worsen.

According to the LAO, current state reserves are available to cover the projected deficit, but only if the state avoids a recession and inflation abates. We will receive more information in mid-January when the Governor releases his proposed budget, with revisions in May, however based on current projections we do not expect county budget reductions will be required.

INFLATION AND INTEREST RATE INCREASES ARE SLOWING DOWN THE ECONOMY
As seen in the chart below, beginning Q1 of 2022, the economy began two successive quarters of contraction, coupled with double-digit losses in the stock market compared to the previous year. These factors, among others, have contributed to concern of an impending recession in 2023. Initial estimates for Q3 2022 indicate 2.9% growth in GDP, at least temporarily halting recent downward trends.

PROPERTY TAX REVENUES WILL SLOW BUT LIKELY REMAIN STRONG
Property tax is the largest source of discretionary revenue for the County and accounts for approximately 36 percent of Marin County’s General Fund.
budget. In July 2022, the Marin County Assessor reported that annual growth in assessed value was 6.55 percent for FY 2022-23, consistent with our previous budget forecast and the strong housing market in 2021. We expect next year’s growth rate to return to the long-term average of approximately 5.0%.

As seen in the chart below, local real estate market sales between January and October are approximately 33% lower than the high point of the housing boom in 2021 and trail pre-pandemic trends.

![Marin Real Estate Sales January - October](chart)

**PENSION STABILIZATION STRATEGY HAS PAID OFF**

Your Board’s policy to dedicate prior year investment gains to the retiree health trust means we anticipated no service reductions due to the recent market losses. Pension costs, which account for approximately 10 percent of the County’s expense budget, are primarily driven by investment market returns. In 2021, the Marin County Employee Retirement Agency (MCERA) announced investment returns of 30 percent, which resulted in the elimination of the County’s portion of unfunded pension liabilities. In contrast, market losses in 2022 will likely lead to losses of at least 9 percent for the plan. Final budgetary impacts of investment returns as of June 30, 2022 will not be known until MCERA adopts its annual actuarial report in early 2023, in which any significant market gains or losses will be phased into long-term employer contribution requirements.

**FY 2023-24 BUDGET WILL MAINTAIN CURRENT SERVICES**

Based on our current budget estimates, we anticipated there will be no required budget reductions next year. Absent significant budget cuts from the state, we anticipate maintaining current services levels for FY 2023-24, consistent with the second year of our two-year budget plan. Given the uncertainty of the state budget, we will only be considering cost-covered and one-time budget change proposals from County departments.
In addition, departments are advised to review their current fee schedules to ensure alignment with the current costs of providing services, and work with the County Administrator’s Office to recommend adjustments in the Spring of 2023.

**EQUITY IMPACT**
The County of Marin strives to be an anti-racist, multicultural organization committed to accountability, transformational change, and community engagement. The Office of Equity’s vision is to dismantle inequities and modify systems inherited through centuries of racial, social, and political injustice.

We will continue to work with your Board and County Departments to ensure that the budget allocation process is informed by a race equity lens that evaluates the potential impacts on unserved and underserved populations within our community.

Please let me know if you have any questions or concerns.

Sincerely,

Joshua Swedberg
Interim Budget Director

Reviewed by,

Matthew H. Hymel
County Administrator