Children & Families
Commission of Orange County

Agenda Item No. 5
November 2, 2011 Meeting

DATE: October 24, 2011

TO: Children and Families Commission of Orange County

FROM: Michael M. Ruane, Executive Director

SUBJECT: Commission Workshop on Strategic Financial Planning

SUMMARY:
As directed at the October Commission Meeting, staff has developed a presentation (Attachment 1) addressing the following items for Commission discussion and policy direction:

a. Review of AB 99 budget reduction plan for FY 11/12
b. Updated year-end financial position
c. Funding options for three-year outlook
d. Review of funding strategies
e. Timeline for follow-up actions

STRATEGIC PLAN & FISCAL SUMMARY:
This agenda item does not include a funding request.

PRIOR COMMISISON ACTIONS:
- October 2011 – Received presentation of the Budget Update and Proposed Strategic Planning Process
- September 2011 – Received Annual External Audit Process and Preliminary Year-End Financial Results
- May 2011 - Approved Fiscal Year 2011/12 Budget

RECOMMMENDED ACTIONS:
1. Receive the Strategic Financial Planning Presentation
2. Provide Policy Direction

ATTACHMENT:
1. Commission Workshop on Strategic Financial Planning

CONTACT: Christina Altmayer

Attachment 1

Commission Workshop on Strategic Financial Planning

November 2, 2011

Commission Meeting

Agenda Item No. 5

Today's Discussion

- Commission used the Long Term Financial Plan and a three-year budget framework for addressing the AB 99 mandated cuts.

- Staff is bringing forward options and alternatives for consideration in advance of the regular financial planning cycle (January – March)
  - FY 10/11 Financial Results may impact three year working assumptions developed as part of the AB 99 mandated budget reduction.
  - Provide opportunities for early communication with grantees based on Commission direction.

- Commission direction is requested on the following :
  1. Confirm that the Commission will maintain the FY 11/12 Adopted Budget as amended.
  2. Direction on short and long-term financial planning assumptions based on options developed by staff.

AB 99 Background and Status

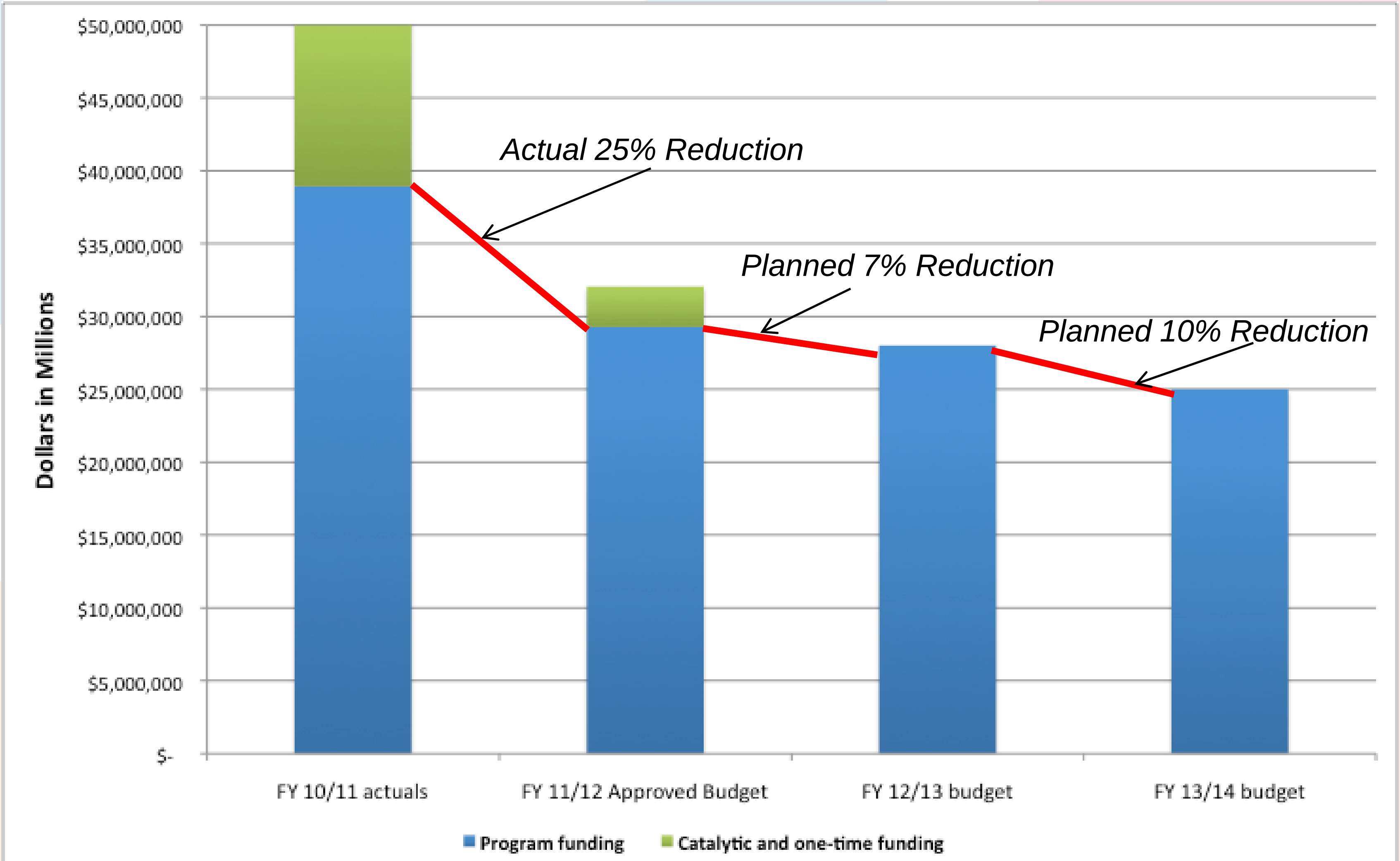
- As part of the State budget deliberations, the State Legislature passed AB 99 which requires a statewide payment of $1 billion from County Prop 10 Commissions. The OC Children and Families Commission payment under AB 99 is $51.4 million:
  - Payment due to State of California by June 2012.
  - Obligation was recognized in the FY 10/11 budget and reflected as an extraordinary expense on the FY 10/11 financial statements.
- Preliminary legal decision due by end of November; however, it is anticipated that decision may be appealed regardless of outcome. As a result, funds may be "tied up" for next 12 to 18 months, pending legal resolution.
- In anticipation of a successful outcome and based on Commission action in October, staff recognizes the importance to begin the planning process for the local reallocation of these funds.

AB 99 Budget Reduction Plan

Approved with FY 11/12 Budget

- **Immediate Reductions in FY 11/12 Budget** – The FY 11/12 budget reflects a 24% reduction in planned program expenses (over 40% from FY 10/11 budget) and a one-year term for most program grants. In addition, the approved budget included a 24% reduction in administrative expenses over prior year budget.
- **Catalytic Funding to Reduce Long-Term Demands** – The FY 11/12 budget included $2.65 million in catalytic funding to reduce demands in future years. The budget, dedicates 8% of total program funding for catalytic activities in the areas of: Homeless Prevention, Community Clinics and Specialty Medical Care, and Early Learning Math. These programs received relatively minor reductions in funding with expectation that future year demands would be reduced.
- **Annual Step Down Aligned with Revenue Forecasts** – The April Long Term Financial Plan assumed annual "step down" in program funding to align with revenue forecasts reducing total program spending from $30 million to $25 million over two years followed by continued gradual reductions.

Planned Three-Year Reductions
as of April 2011



Excludes administration and evaluation costs. Administration is limited to 10% of annual budget.

Children & Families
Commission of Orange County

What has changed since April 2011 Plan?

- As reported in October, FY 10/11 actuals were $4.5 million better than anticipated due to revenue increases, and program and administrative savings.
  - Revenue
    - Prop 10 FY 10/11 revenue better than previously forecasted by $600,000.
    - Other revenue realized from other grants and interest earnings.
  - Expenses
    - Administration – Actual expenses were $606,560 less, or 12.9% than budget.
    - Program – Actual expenses were $1.8 million less than plan.
- Using the FY 10/11 actuals as the new base, the FY 11/12 forecast is $800,000 better than previously projected.
- FY 11/12 year-end forecast is **$5.3 million** better than the April forecast.
- Changes to the FY 11/12 Budget were approved in October as part of the year-end audit. Adjustments reflected carryover actions. No further changes to FY 11/12 Budget are proposed by staff at this time.

Children & Families
Commission of Orange County

Long Term Implications

- Staff has updated the April Long Term Financial Plan based on FY 10/11 actuals:
  - Long term revenue outlook has improved due to higher baseline (FY 10/11). Staff still forecasting a 5% decline for FY 11/12 and on average a 3% decline for remaining years in planning horizon.

- No change in the following:
  - Assumes payment to the State of California by June 2012, consistent with AB 99 (encumbered in FY 2010/11).
  - Administrative expenses limited to 10% of operating budget.
  - Minimum cash fund balance requirements per Commission policy (target of 25% of operating budget). This requirement will be revisited and confirmed annually.

Funding Options for the Three-Year Outlook

- As indicated, the April AB 99 budget plan assumed that the Commission would reduce direct service funding from FY 11/12 to FY 12/13 by $2 million and an additional $3 million in FY 13/14 .
- The updated positive year-end forecast provides options to reconsider this three-year funding outlook balancing:
  - Short and long term demands against revenue forecasts.
  - Risks of unanticipated revenue declines - Staff will continue to monitor FY 11/12 actual revenue against plan.
- Staff has developed three options for Commission consideration. Options can also inform the Commission's strategy for reallocation of the $51.4 million funds currently restricted to meet the AB 99 payment.
- Based on Commission direction, staff will initiate a process for developing the FY 12/13 Budget including review of program level funding allocations.

Commission's Funding Strategies

- Since its formation, the Commission has recognized the need for program sustainability and has used revenue and funding strategies to ensure that the services funded by the Commission have capacity beyond the Commission's declining funding.
- Historically, the Commission has provided funding to programs to achieve targeted outcomes in three ways:
  - Direct Service Grants – Program grants for direct community services and/or capacity building.
  - Catalytic Funding – One-time funding to alleviate ongoing direct program funding requirements or one-time funding.
  - Endowment – Multi-year grant to support/sustain program services for an extended period of time (limited experience).

FY 2011/12 Amended Budget

	Direct Service Grants (92% of Total Funding)	Catalytic (8% of Total Funding)	Endowment* (None in FY 11/12)
Healthy Children	58%	47%	
Early Learning	21%	16%	
Strong Families	12%	33%	
Capacity Building	9%	4%	
Total Invested	$31.1 million	$2.75 million	

*The Commission created two limited endowments in FY 10/11 to support the Santa Ana YMCA: $1 million in federal MAA reimbursements were used to establish an endowment for water safety and aquatics programs; and, $2 million in Prop 10 funds to create a health and wellness fund focused on obesity prevention.

Direct Service Grants

- Generally, one to three year grants to provide services for targeted outcomes. Direct service grants are used to support program costs including:
  - Positions and staffing
  - Direct program expenses

- Challenge is to provide sustainable grant funding in environment of declining revenue.

- In 2008, Bridgespan recommended that the Commission "*Shift a greater percentage of funding to catalytic (versus sustaining) activities*."

Catalytic Investments

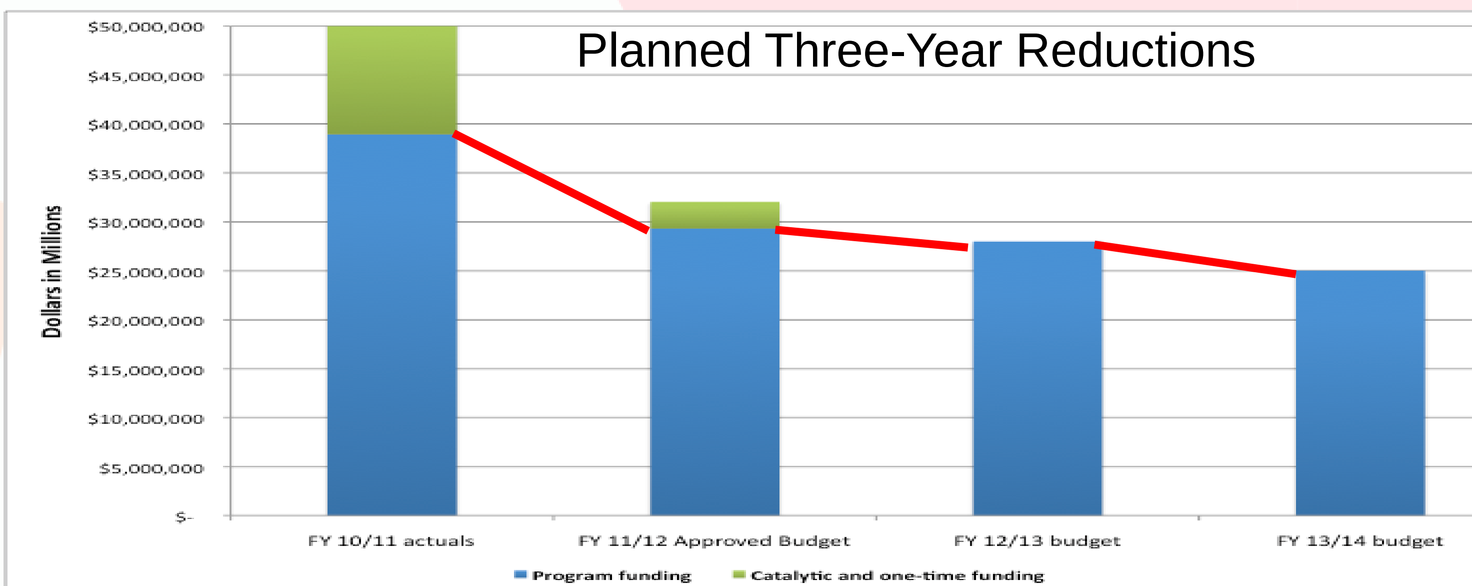
- Commission has invested catalytic projects to either:
  - **Reduce Operating Demands** – Provide one-time funding to eliminate or reduce *existing direct service grants* future year demands. Through one-time capital or other funding, the Commission is able to offset future operating demands and promote service sustainability. Experience is that catalytic investments take up to 18 months to realize savings.
    - Examples: Boys and Girls Club of Huntington Valley, Fullerton Interfaith Emergency Shelter– In both cases, Commission capital funding offset the need for ongoing operating support and increased program sustainability.
  - **Address Unmet Community Need** – Support a critical and recognized community need through *one-time funding (no operating offset)*. This funding has been used when a one-time investment will meet a community need and address a critical gap in the network of services to young families. Grantee amortizes payment through annual payback plan.
    - Examples: Santa Ana YMCA Capital Program, Pretend City – Did not offset a future operating demand, but addressed a Commission priority through one-time funding.

Endowments

- Commission has had limited experience in creating "Program Endowments".
- Endowment strategy has been done in one program on a modified basis and can be expanded in the future using the following criteria:
  - Education and prevention oriented – Potential to reduce long-term costs, but not likely to have dedicated revenue source. Example: dental education and prevention services offset treatment costs, but not likely to have a dedicated revenue source.
  - Critical programs with limited sustainability options from other government sources or revenue generation activities.
  - Costs that are *not* expected to be absorbed by the public service delivery systems (schools, health providers, etc) in the foreseeable future.
- Recent Example:
  - YMCA Health and Wellness Fund
    - Dedicated funding to support ongoing obesity prevention operating costs in exchange for multi-year service agreements; similar to a sinking fund.

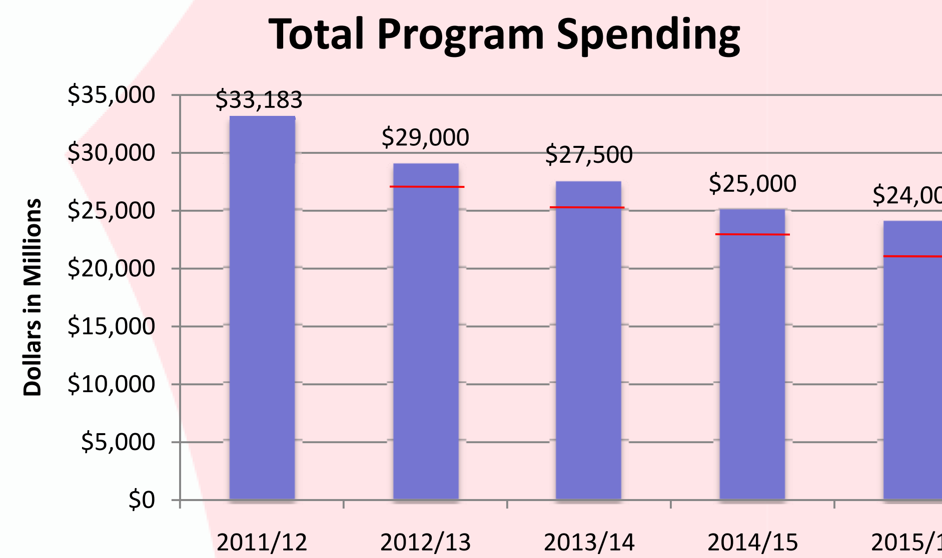
Proposed Options

- Staff has developed three options for Commission consideration. All three options:
  - Assume no changes in FY 11/12 budget plan.
  - Incorporate update revenue forecasts
  - Focus on immediate options related to the $5.3 million.
  - Provide a framework for addressing the AB 99 litigation recovery funds.
- Commission direction on addressing the FY 12/13 budget implications are time sensitive:
  - Program grants are expiring in June 30, 2012.
  - Allow sufficient time to notify grantees and work with them to respond to budget actions and to develop program reduction recommendations.



Option 1: Continue with Planned Step Down
Allocate Funds for One-Time Projects

- Summary of Option 1
  - Gradual reduction in program expenses over time consistent with prior plan.
  - With updated revenue forecast, program spending higher than April projection.
  - Dedicates $4.5 million for one-time funding actions (catalytic, endowment, or other projects as determined by the Commission).
- What this option provides………
  - Opportunity to support long-term catalytic strategies.
  - Conservative approach in addressing revenue forecasts; one-time money dedicated for one-time uses.
  - Potential to use catalytic funding to mitigate FY 13/14 and beyond reductions.
- What this option risks………………
  - Grantees are still implementing program cuts in current year and may have difficulty implementing additional cuts.
  - May require defunding of programs instead of across the board cuts.

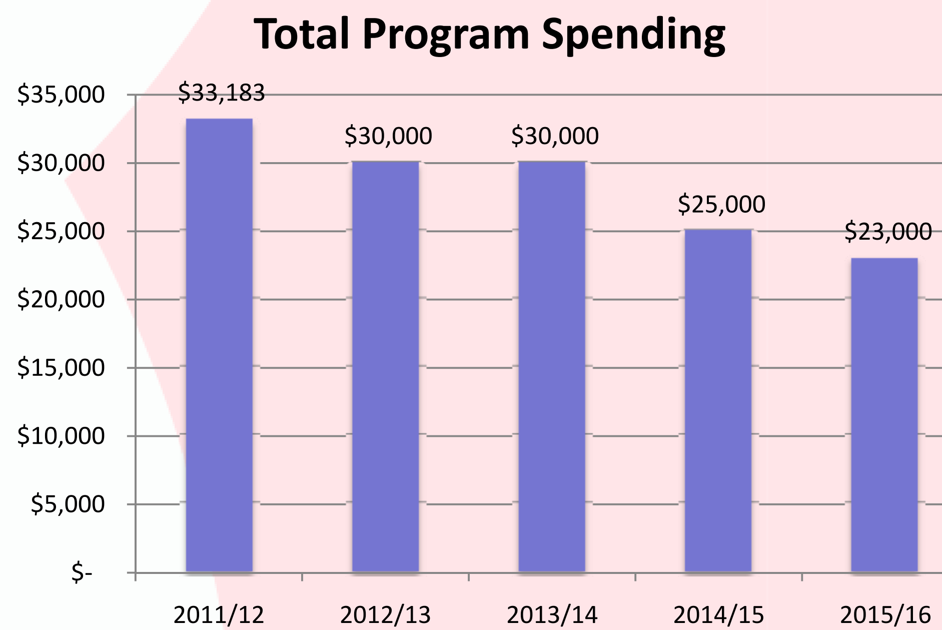


Note: FY 11/12 amended budget includes catalytic funding and carryover. Base direct service funding was $30 million. Red line indicates April planned funding level.

Children & Families Commission of Orange County

Option 2 – Use One-Time Funding to Maintain Level Funding for FY 12/13 and FY 13/14

- Summary of Option 2
  - Sustains Direct Services Funding at $30 million for the next two fiscal years.
  - Redirects all one-time funding to supporting Direct Services for the next two fiscal years.
- What this option provides………
  - Capacity to support priority programs for the next two fiscal years.
  - Provide stable funding until benefits from current catalytic funding is realized - catalytic funding assumed in FY 11/12 is not likely to yield one-year benefits.
  - Recognizes the significant cuts in current programs that just went into effect July 1. Programs are likely still implementing changes.
- What this option risks………………
  - Significant reduction in spending from FY 13/14 to FY 14/15.
  - If revenue falls short of projections, additional reductions may be necessary.



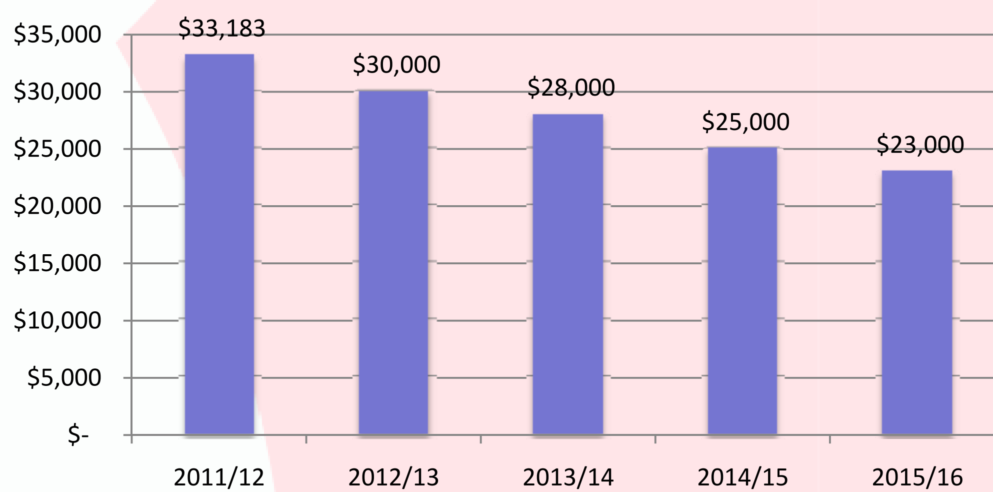
Note: FY 11/12 amended budget includes catalytic funding and carryover. Base direct service funding was $30 million.

Children & Families Commission of Orange County

Option 3 – Hybrid Plan

- Summary of Option 3
  - Sustains Direct Services Funding at $30 million FY 12/13 and begins reductions in FY 13/14.
  - Redirects a portion of one-time funding to continuing Direct Services and dedicates $3 million to one-time funding.
- What this option provides………
  - One year of stable funding for direct services, recognizing the highly strained non-profit environment.
  - More limited capacity for one-time catalytic/endowment or other one-time funding.
  - Provides time to realize catalytic savings.
- What this option risks………………
  - Cuts will still be significant if programs are working towards reduced funding in out years.
  - Grantees are still implementing program cuts in current year and may have difficulty implementing additional cuts immediately.

Total Program Spending



Note: FY 11/12 amended budget includes catalytic funding and carryover. Base direct service funding was $30 million.

Children & Families Commission of Orange County

Commissioner Direction & Discussion

1. Confirm FY 11/12 budget reduction plan as approved in the amended budget.

2. Provide direction to staff on proposed options and recommendations for funding for FY 12/13:
   - Address immediate question of funding levels for next three years.
   - Provide direction on implications for AB 99 funding.

3. Discuss program implications and provide direction on further program work to be developed.

Next Steps & Proposed Planning Process

- Based on Commission direction, develop plans for FY 12/13 Budget and subsequent years:
  - Return to Commission in December with proposed funding strategy and initiate formal planning related to funds potentially recovered through AB 99 litigation. Based on direction, staff will develop potential proposed investment strategy based on proposed funding strategy (catalytic, direct services, endowment).
- January
  - Convene funding panels to evaluate program implications, as necessary and implement necessary reductions.
- February/March 2012
  - Return with preliminary budget for FY 12/13 and three-year plan.