Executive Summary

Introduction

The County of Orange is dedicated to long-term strategic financial planning to ensure its ability to respond to economic changes and unanticipated events in a way that allows the County to preserve the range and quality of services provided to the community. The year leading up to the 2019 Strategic Financial Plan process evidenced slowing Gross Domestic Product (GDP) growth, decreasing employment growth, a lagging housing market, and a negatively sloped yield curve. Based on these factors, economists caution that the economy may reach a near-recession level by the end of 2020. While growth in recent years has allowed the County to fund one-time projects, the projected level of future growth does not allow for material increases in levels of service. The County is committed to maintaining current service levels to the extent possible while using fluctuations in revenue growth to prepare for or complete previously deferred projects.

A disciplined approach to fiscal management of the County's limited resources will ensure alignment with countywide strategic priorities and values. Commitment to the Board of Supervisors' priorities of budget stabilization, preparation for contingencies, and funding of agency infrastructure, accentuates the need for long-term strategic planning including building a reserve balance that best positions the County to weather future economic variations with minimal impact on the community it serves. This strategic planning process enabled the County to clear a significant financial milestone and complete the $150 million VLFAA repayment to the State in June 2019 without negatively affecting Departments' operations or depleting County reserves. It is important for the County to maintain its reserve position, even during any potential downturn in the economy or other fiscal challenges.

Although costs of doing business continue to outpace revenue growth, the County is committed to implementing key initiatives and moving toward a future that will enrich the lives of Orange County residents and visitors including:

- **Building a System of Care:** The County continues to move forward with several key initiatives to improve the overall response to homelessness across the region, including:
  - **Regional Response to Homelessness and Emergency Shelter Developments:** The most recent adopted budget includes funding for relocation of the Courtyard Transitional Center to the recently purchased Yale facility. The County also remains committed to supporting city-led shelter programs through field-based outreach teams that integrate County behavioral health resources. The continuous partnerships between the County and each of the 34 cities in Orange

County is essential to meet the needs of people, linking them from street outreach to shelter, as the System of Care continues to expand. Through these efforts and others, the County is working together with cities to respond to regional community needs. Also included in the budget is funding for bridge housing and housing navigation to assist homeless individuals in overcoming barriers as they transition from the street to permanent housing.

- **System Integration:** The County leverages available resources by integrating various County services within the emergency shelter, health care, behavioral health and community re-entry systems. Proposed initiatives address mental health and substance abuse treatment, providing linkages to services, recidivism reduction, and post-incarceration re-entry services to the community. To that end, the County purchased a centrally located building in the City of Orange to establish a behavioral health campus made possible through partnerships with community organizations. The campus will employ an integrated approach, co-locating mental health and substance abuse treatment and will provide the ability to leverage funding and establish more effective and efficient service delivery systems. Services offered will include crisis stabilization, recidivism reduction, and linkages to services for all community members.

- **Data Sharing Platform for Care Coordination:** A project is underway to develop a system platform that would integrate information and data across the County's System of Care, including health care, behavioral health, community corrections, housing, and benefits and support services. Contracted services and Whole Person Care funds ($3.8 million) were used to map processes across the involved departments and identify potential vendors to develop a system platform. Implementation of an operationally proven, innovative, scalable and sustainable platform is a priority for the County. In addition, efforts will continue to identify funding for the next phases of the project.

- **Integrated Services Strategy:** The Integrated Services 2025 Vision Report, presented to the Board of Supervisors on October 22, 2019, lays the groundwork for implementation of the Integrated Services Strategy. This strategy prioritizes behavioral health prevention and reentry efforts, in-custody behavioral health treatment, in-custody vocational and educational programming and collaboration with courts as part of the larger effort to strengthen the County's System of Care.

- **Capital and Infrastructure Improvements:** The County continues on a path to improve agency infrastructure in various areas including the Civic Center Facilities

Strategic Plan (CCFSP), an initiative that addresses the County's long-term occupancy in the Orange County Civic Center. The goals are to improve delivery of services to the community, space usage and Departmental adjacencies; address the aging portfolio of County facilities; and better manage long-term occupancy and maintenance costs. The County is also actively exploring options for development projects that would use County assets to generate ongoing revenue streams.

The Process

The Strategic Financial Plan (the Plan or SFP) is a financial component of the County's Strategic Plan that provides short and long-term operational linkage between the County's Strategic Plan and the annual budget process. It offers a means to gauge Departments' needs and resources to ensure the County's financial position is sufficient to support ongoing services and long-term needs while ensuring genuine sustainability within potential future economic constraints. The Plan provides policy makers with a tool for testing assumptions and evaluating the projected financial impact of policy decisions related to General Fund operations, capital requirements, strategic priorities, and emerging initiatives.

The Plan provides the context for a five-year operating budget and prepares for development of the next fiscal year budget with the condition that assumptions used in developing the plan may change over time. The Plan is developed with a goal of identifying any significant issues that must be addressed to achieve the County's mission, goals and long-term plan for financial stability. The County continues to focus on the following key fiscal goals:

- Budget stabilization and planning for contingencies
- Planning for and funding agency infrastructure

The primary focus of the SFP is the portion of the General Fund often referred to as discretionary funding or Net County Cost (NCC) which is funded by General Purpose Revenues. This is the funding source allocated to Departments and approved by the Board for programs and activities which are not funded by specific revenue streams. The non-discretionary portion of the budget contains mandated activities such as benefit payments to clients, which the County provides on behalf of the State and Federal governments. Such activities are primarily funded with State and Federal revenues and include programs such as In-Home Supportive Services (IHSS), CalWORKs, CalFresh and Medi-Cal.

Non-discretionary revenues projected by Departments over the five years of the Plan consist of the following in addition to the projected General Purpose Revenue:

(Amounts in Millions)

Revenue Type	FY 2020-21	FY 2021-22	FY 2022-23	FY 2023-24	FY 2024-25
State Revenue	$ 1,419.0	$ 1,441.6	$ 1,467.9	$ 1,493.7	$ 1,521.6
Federal Revenue	396.8	392.2	395.4	398.7	402.2
Charges for Services	485.5	489.1	506.3	505.2	517.3
Other Financing Sources	373.4	387.3	397.8	390.2	387.4
Licenses, Permits & Franchises	21.8	22.3	22.8	23.4	23.9
Miscellaneous Revenues	15.2	15.6	13.0	13.8	14.7
Fines, Forfeitures & Penalties	13.5	13.2	13.2	13.2	13.2
Use of Money & Property	12.8	11.2	11.2	11.2	11.3
Other Governmental Agencies	11.7	11.9	12.1	12.4	12.6
Subtotal	***$ 2,749.7***	***$ 2,784.4***	***$ 2,839.7***	***$ 2,861.8***	***$ 2,904.2***
General Purpose Revenue	911.2	939.6	965.8	993.4	1,017.6
Grand Total	**$ 3,660.9**	**$ 3,724.0**	**$ 3,805.5**	**$ 3,855.2**	**$ 3,921.8**

State and Federal revenue sources, in particular, are reviewed and closely monitored to identify possible issues. Any issues identified during the SFP process are reported to the County's Legislative Affairs unit, which then communicates the concerns to the County's State and Federal lobbyists as well as the California State Association of Counties (CSAC) and the National Association of Counties (NACo). In addition, County departments work closely with organizations such as the California Welfare Directors Association (CWDA), the County Health Executives Association of California (CHEAC), and the California State Sheriff's Association on any identified issues.

As in prior years, the SFP focuses on General Fund gap analysis to highlight the continuing impact of projected declining General Fund revenue growth and the ongoing cost of doing business. The plan focuses on identification of General Fund fiscal gaps (comprised of Departmental planned expenditures net of Departmental revenues and NCC) and imbalances that will need to be addressed during the FY 2020-21 annual budget process. Summary analyses of capital and information technology (IT) project needs were also conducted. This year's SFP lays the groundwork for establishing budget priorities and funding solutions for FY 2020-21 prior to the usual timeframe of the annual budget process, thereby allowing more time for collaboration and creative solutions.

The SFP also provides an opportunity to review the General Fund Reserves Policy, which is developed to provide governance over the maintenance and use of reserves and to reflect the County's continued commitment to sound fiscal policy. There are no recommended changes to reserve policies proposed in this year's SFP.

Relevant economic data used in preparing the County's 2019 SFP includes:

- General Purpose Revenue forecast developed in conjunction with forecasts by the Auditor-Controller, the 2019-20 Local Assessment Roll of Values, and revenue receipt trends.
- Various projections for capital and operating inflationary factors, as developed by governmental or industry experts in the related field.
- Continued monitoring of economic forecasts published by Chapman University, University of California, Los Angeles, the State Legislative Analyst Office and other various sources.

Economic data compiled in August 2019 was included as part of the 2019 SFP instructions. As changes occur in the economy, projections will be updated during the FY 2020-21 annual budget development process.

Key Assumptions:

- The total cost of salaries and benefits is expected to increase over the five-year plan and includes the following assumptions:
  - Salary growth factors include general salary increases consistent with existing memorandum of understanding (MOU) terms as of September 2019. Assumptions for salary increases beyond the September 2019 existing MOU terms included 0% growth for Years one through five of the plan and did not include new MOUs terms approved in October and November 2019 (see page 10 for information related to recently approved MOUs). Salary projections are developed independently and not in consultation with Human Resource Services or the Board. The use of growth factors is for planning purposes only and does not represent a commitment for bargaining purposes.

Included in the assumptions for the 2019 SFP are the following economic and demographic assumption changes adopted by the Orange County Employees Retirement System (OCERS) Board on October 16, 2017, which included a three-year phase-in of the cost impact to the contribution rates associated with the Unfunded Actuarially Accrued Liability (UAAL):

- Reduced the assumed investment rate of return from 7.25% to 7.00%
- Reduced the assumed rate of price inflation from 3.00% to 2.75%
- Adopted the use of generational tables, which have identified reduced rates of mortality for members

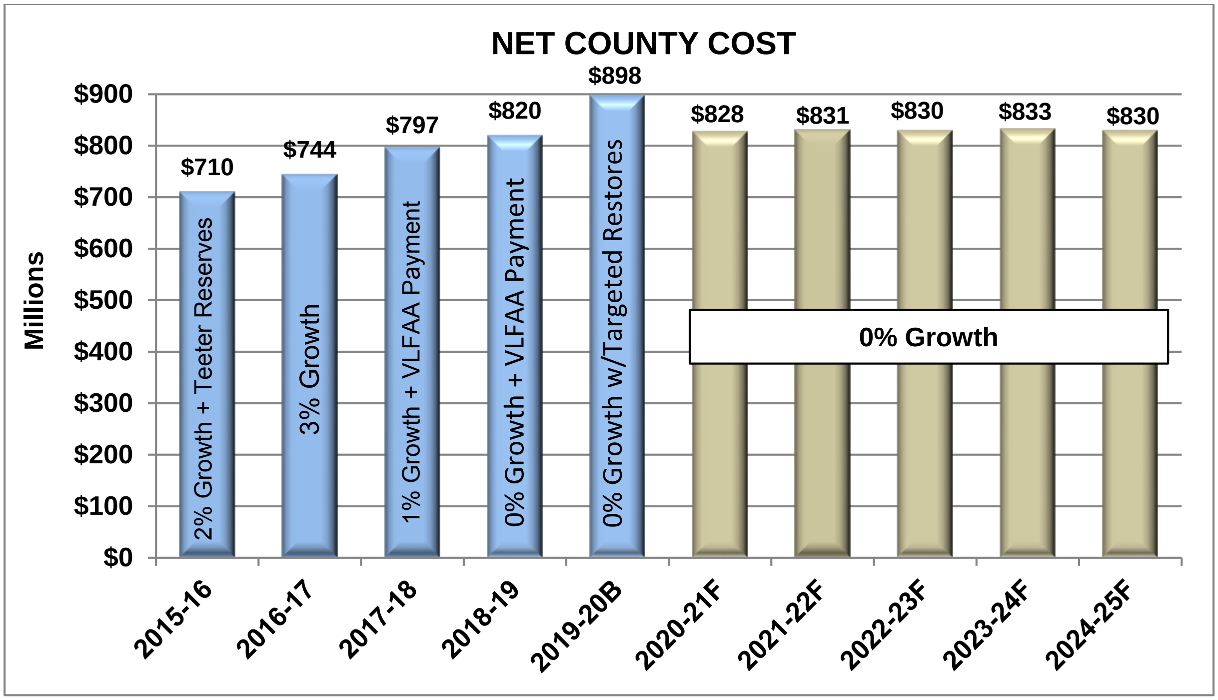
The cumulative effect of the three-year phase-in of the assumption changes had the impact of increasing contribution rates beginning in the current budget fiscal year, FY 2019-20, through the first two years of the 2019 SFP, FY 2020-21 and FY 2021-22. In addition, investment losses of -2.46% experienced in 2018 contributed to an increase in contribution rates of the five-year plan. (See Retirement section of this summary for additional information.)

- Retirement Rate Assumptions (Tier II) assume the market investment rate of return in calendar year 2019 is 7.00% for all years, which resulted in the following retirement rates over the five-year plan:
  - Safety Rate ranges from 72.4%% to 78.9% (3@50; excludes retiree medical)
  - Non-Safety Rate ranges of 31.5% to 34.6% (2.7@55; excludes retiree medical)
  - Retiree Medical for Safety ranges from 4.9% to 5.6% (7.5% to 8.3% for Law Enforcement Management)
  - Retiree Medical for Non-Safety is 3.9%

- Health Benefit Cost Assumptions
  - 5-Year Growth from $207 million to $275 million, a 33% increase

- Consumer Price Index (CPI) Assumptions for Services & Supplies: 2.7% to 3.3%

- Departmental NCC limits were set for ongoing baseline operations (current levels of service). FY 2020-21 NCC limits were projected using the adopted FY 2019-20 limits ($898 million) as a starting point, with amendments for technical adjustments and removal of one-time items resulting in proposed baseline limits for FY 2020-21 of $828 million. Departments have identified $82 million in appropriation reductions that would be required to meet the FY 2020-21 NCC limits. After factoring in NCC limit growth of 0% in FY 2020-21 through year five of the Plan and removing any one-time items, Departments identified a 5-year cumulative budget gap of $641 million. The following table summarizes historical budgeted and forecasted NCC.



The following table summarizes prior and current year Adopted Budget and Plan year projected NCC by program:

Program	15-16	16-17	17-18	18-19	19-20B	20-21F	21-22F	22-23F	23-24F	24-25F
Public Protection	$395.39	$413.37	$454.05	$441.67	$506.60	$490.05	$488.98	$488.98	$488.98	$488.98
Community Services	125.56	127.23	128.77	129.43	152.32	155.52	155.52	155.52	155.52	155.52
Infrastructure	20.98	22.33	22.27	37.10	35.71	35.85	35.85	35.85	35.85	35.85
General Government	125.19	121.27	123.84	116.25	140.98	126.72	129.70	126.17	129.70	126.17
Capital Improvements	21.80	20.31	15.74	22.93	53.81	21.99	20.89	20.89	20.89	20.89
Debt Service	0.87	0.87	0.87	0.24	0.05	0.42	0.42	0.42	0.42	0.42
Insurance, Reserves & Misc.	20.36	38.87	51.36	72.38	9.00	(2.33)	(0.85)	2.08	2.13	2.21
GRAND TOTAL NCC	**$710.15**	**$744.25**	**$796.90**	**$820.00**	**$898.47**	**$828.22**	**$830.51**	**$829.91**	**$833.49**	**$830.04**

Note: FY 19-20B NCC is the adopted budget. SFP years are forecasted (F).

Outlook and Opportunities

In general, trends in key economic indicators reflect relatively strong economic performance in the near term with growth dwindling to near recession levels by the third or fourth year of the plan. Continued rising costs of salaries and benefits and other costs of doing business may exert pressure on the County's ability to fund current and future service levels. Please see further discussion of economic impacts in the *Economic Forecast* section of this document.

Development of this SFP takes into account declining General Purpose Revenue growth consistent with current and projected economic conditions. The County should continue to follow fiscal policies that will maintain Department budget stability, prepare for contingencies, and address and fund agency infrastructure.

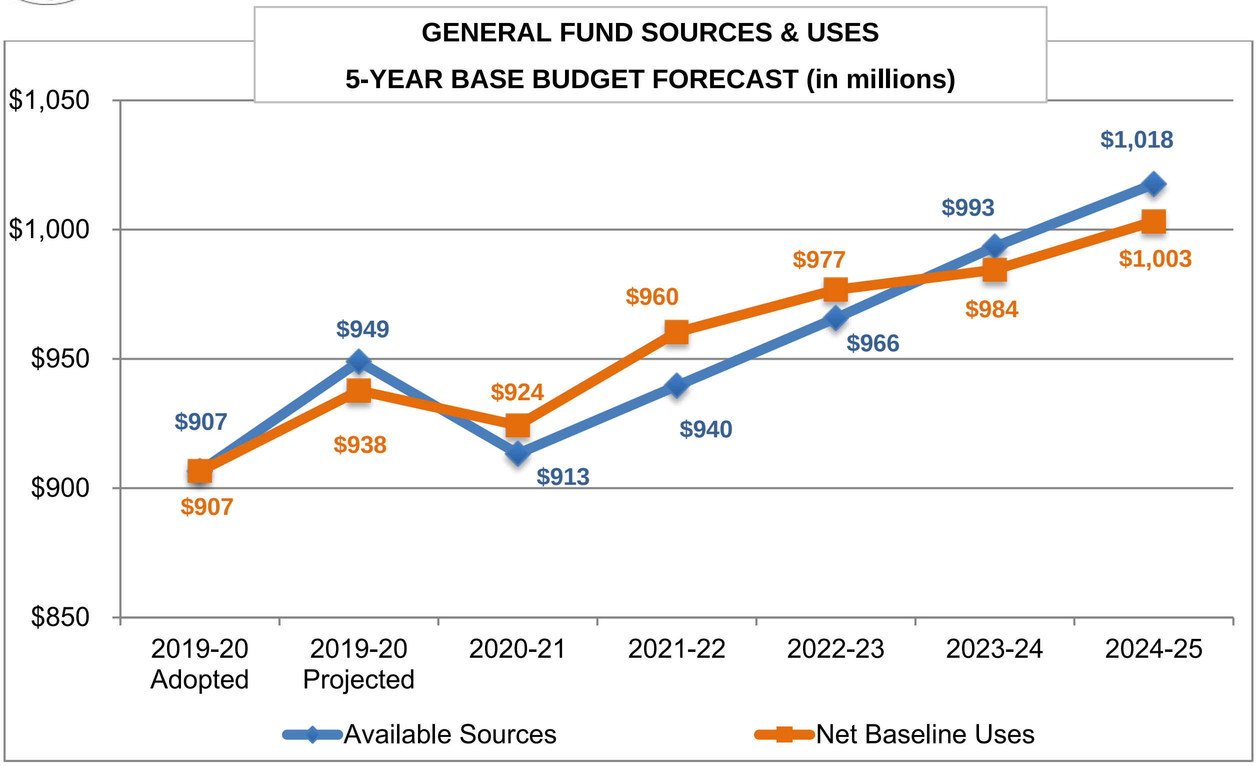
Expenditures

Key Issues –

- The cost of doing business continues to grow faster than the growth in revenue.
- Competing needs exist for General Funds, including the need to fund new and deferred capital and information technology projects, ongoing strategic priority requests, and reserve position.

The following chart illustrates the projected General Fund Sources and Uses. The Net Baseline Uses encompasses Department NCC requests including restore augmentations, but does not include the effects of negotiated salary and benefits increases approved after performance of initial Plan forecasting in September 2019.

The gap between sources and uses begins at a negative $11 million in the first year of the Plan; grows to $20 million and $11 million in years two and three, respectively; and then changes to positive variances of $9 million in year four and $15 million in year five. The projected cumulative deficit for the five years is $19 million if all restore requests were granted.



Notes:
[1] Available Sources is General Purpose Revenue and may include use of one-time revenue sources
[2] Net Baseline Uses is NCC limits plus restore augmentations and Budget Stabilization and other reserve increases

It is important to note that unexpected shifts in economic conditions could cause the gaps between available sources and net baseline uses to narrow or invert. In addition, increasing costs in the areas of Community Services including: shifts of IHSS program responsibility to counties by the State; growing General Relief costs, and homelessness initiatives are likely to constrain the ability to fund future operations in other areas.

Subsequent to the initial assumption calculations in September 2019, the Board of Supervisors approved new Memorandums of Understanding (MOU) with the following bargaining groups:

Bargaining Group	Abbreviation	Date Approved
Association of Orange County Deputy Sheriffs	AOCDS	October 8, 2019
Association of County Law Enforcement Managers	ACLEM	October 22, 2019
Orange County Employees Association	OCEA	October 22, 2019
Orange County Managers Association	OCMA	November 5, 2019
American Federation of State, County and Municipal Employees	AFSCME	November 19, 2019

The total estimated financial impact to Net County Cost of the recently approved MOUs ranges from $83.6 million in FY 2020-21 to $181.0 million in FY 2022-23 and beyond. Departments are developing action plans to handle the cost increases while avoiding possible negative impacts to the General Fund. The estimated financial impacts do not include potential increases for new MOUs with International Union of Operating Engineers (IOUE), Orange County Attorney's Association (OCAA) and Teamsters as bargaining for those groups is ongoing.

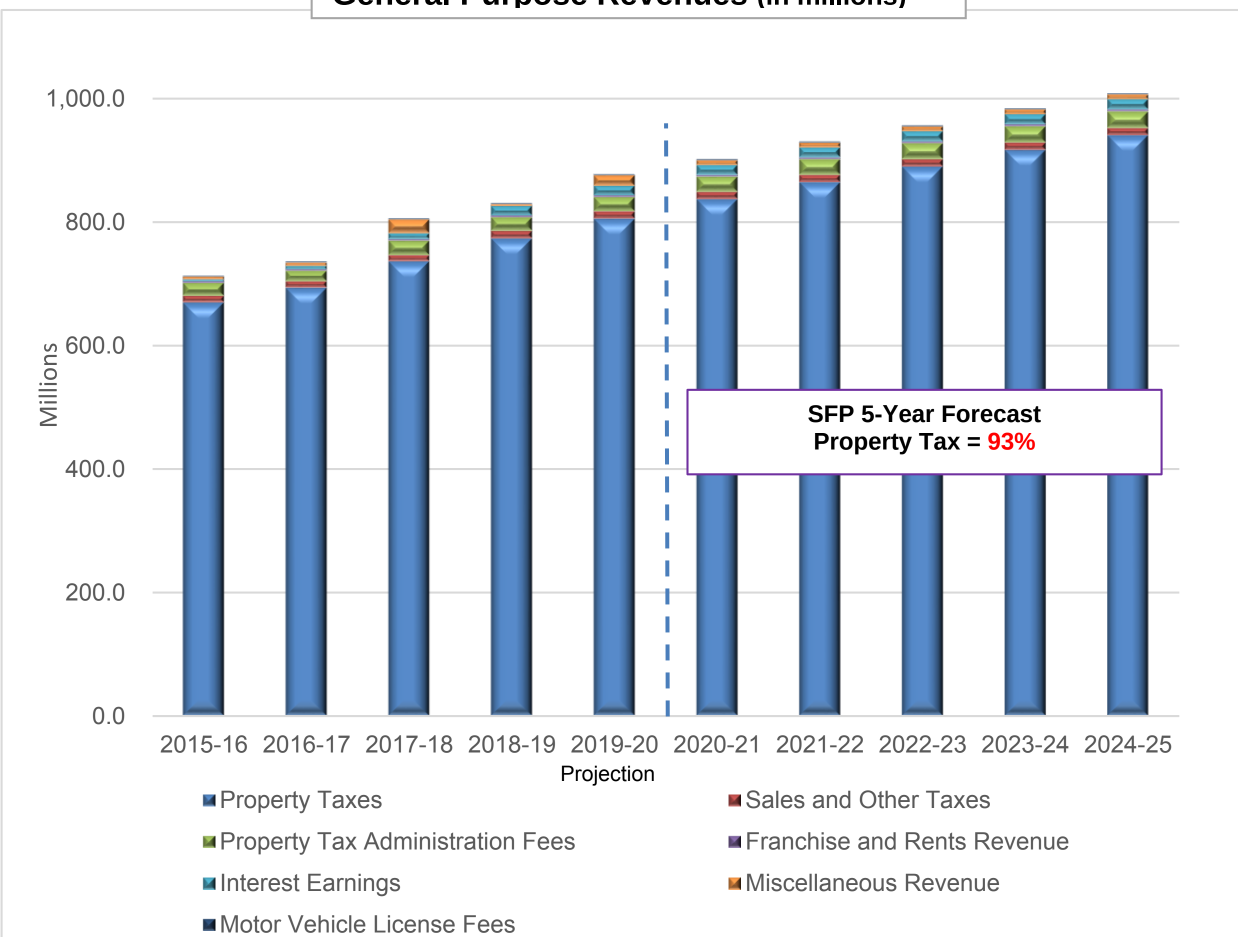
Over the five years of the Plan, departments requested a total of $34 million in expand augmentation requests primarily to fund increased staffing and equipment needs. In addition, departments requested a total of $425.4 million in strategic priority requests including $103.6 million related to Integrated Services programs with the remaining $321.8 million related to department-specific requests.

Revenues

As previously illustrated, Departmental base revenues (sources) are projected to decline slightly but not to the extent of Departmental base expenditures (uses) in year one, and experience low growth in years two through and five.

The Plan forecasts moderate increases in General Purpose Revenue (GPR) in years one through three of the Plan consistent with current economic trends. Lower growth is projected in the last two years of the plan consistent with economists' projections of a slowing economy. The following chart summarizes historical and forecasted growth in GPR. Detailed analysis of each component of GPR and Fund Balance Unassigned is provided in the *General Purpose Revenue Forecast* section of this document.

General Purpose Revenues (in millions)



Note: Miscellaneous Revenue includes transfers in from other funds.

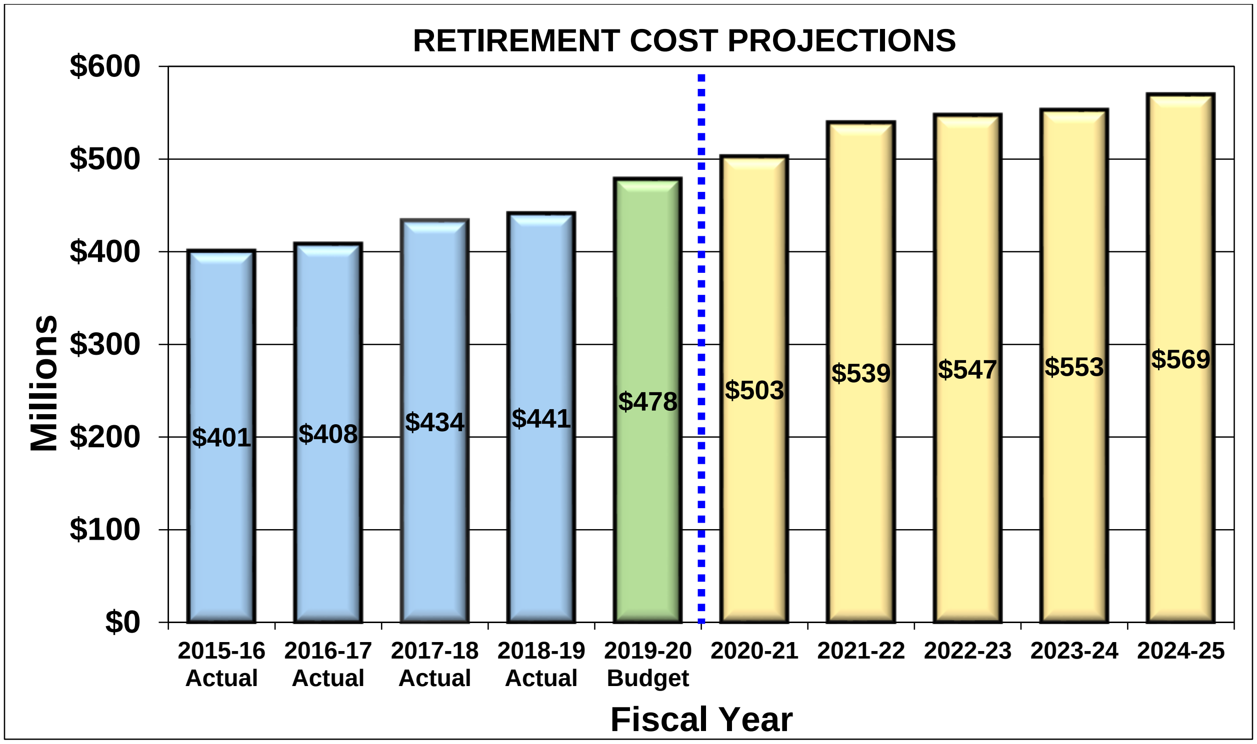
Retirement

The County participates in the Orange County Employees' Retirement System (OCERS), a cost sharing multiple-employer, defined benefit pension plan. The County's funding policy is to make annual required contributions to OCERS that, when combined with employee contributions and investment income, fully provide for member benefits by the time they retire.

For the 2019 SFP, the County's projected cost of retirement shows an increase over the 2018 SFP forecast primarily due to the investment losses experienced in 2018 of -2.46%. As of September 2019, OCERS' investment returns were 10.36%. OCERS' investment returns as of December 2019 will factor into the projected cost of retirement for the 2020 SFP.

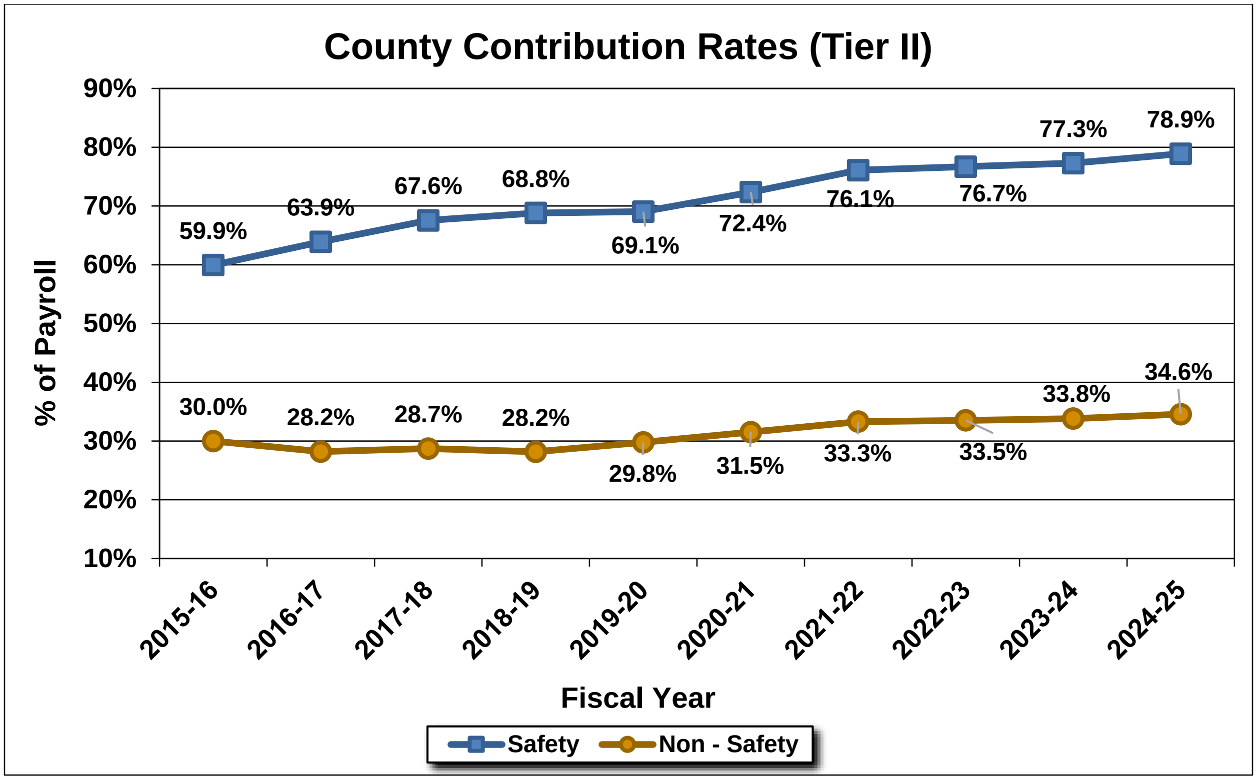
As illustrated in the following chart for retirement cost projections, forecasts for retirement reflect annual costs growing rapidly beginning in FY 2019-20 with a budgeted $478 million to a forecast of $539 million in FY 2021-22. The rapid increase is a result of the impact of the 2018 investment losses and the three-year phase-in of the UAAL cost impact due to the assumption changes adopted by the OCERS Board on October 16, 2017. Those assumption changes included a reduction in the assumed rate of return from 7.25% to 7.00%, a reduction in price inflation from 3.00% to 2.75%, and application of generational tables that indicate reduced rates of mortality. After the final year of the phase-in of the UAAL cost impact, retirement costs will begin to stabilize growing to $569 million in FY 2024-25. The average annual increase over the plan is 3.82%.

While the cost of retirement during this Strategic Financial Plan period shows increased costs, the reduced retirement benefits established under the California Public Employees' Pension Reform Act of 2013 (PEPRA) will have a long-term positive impact on the County's cost of retirement. New County employees hired on or after January 1, 2013, who are considered "New Members" within the Meaning of PEPRA, are enrolled in lower cost PEPRA retirement plans. As of September 2019, the County had 5,731 (approximately 35% of County employees) employees enrolled in PEPRA retirement plans, an increase from 4,874 (approximately 30% of County employees) employees as of September 2018. In addition, as the UAAL is paid down over the 20-year amortization period, costs are expected to decline.



Note: All years exclude Pension Prepayment and Retiree Medical.

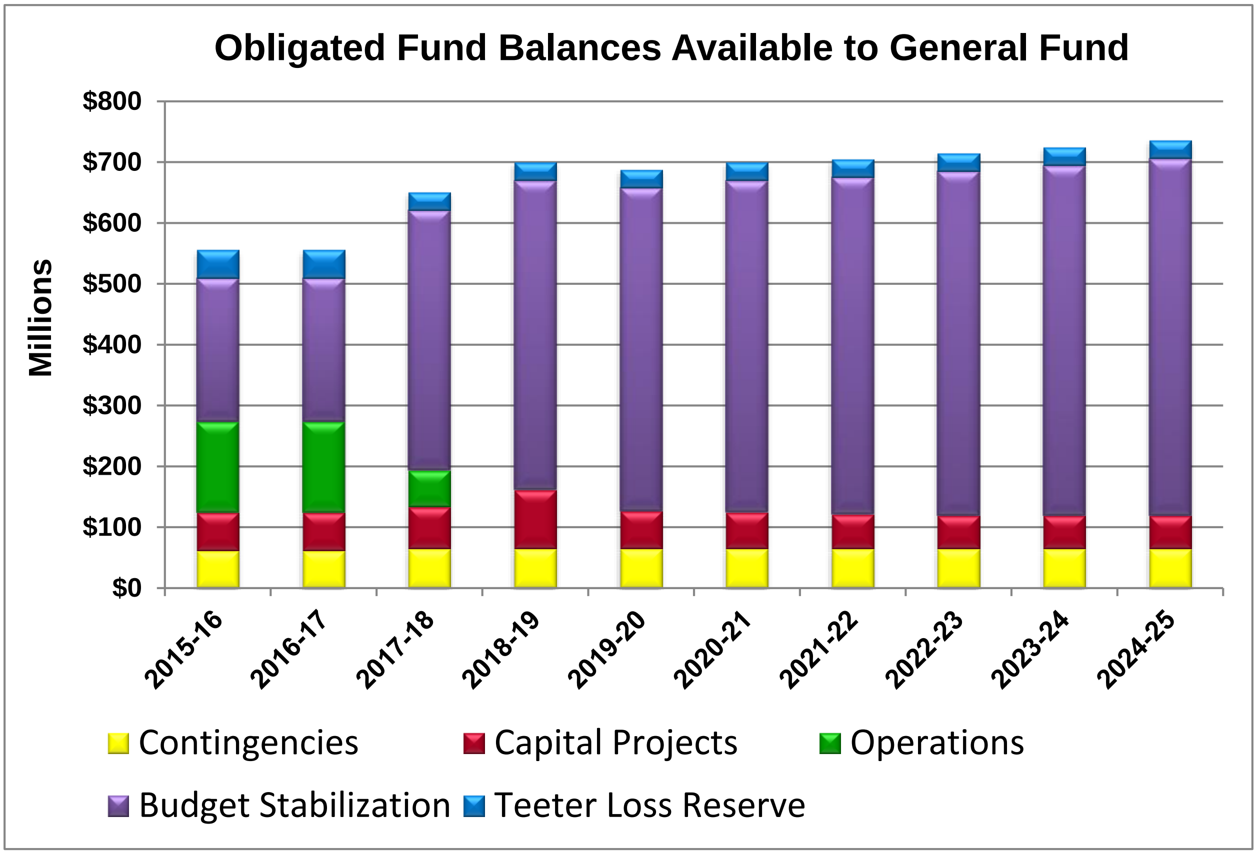
The following chart of estimated County Contribution Rates for Tier II employees reflects increased retirement rates for Non-Safety and Safety employees beginning in FY 2019-20 related to the impact of the 2018 investment losses and the three-year phase-in of the UAAL cost impact due to the assumption changes adopted by the OCERS Board on October 16, 2017. After the three-year phase-in, projected contribution rates are projected to stabilize beginning in FY 2022-23, assuming all actuarial assumptions are met in the future and there are no future changes in any of the actuarial assumptions.



Notes: All years exclude Retiree Medical.

Obligated Fund Balances and Cash

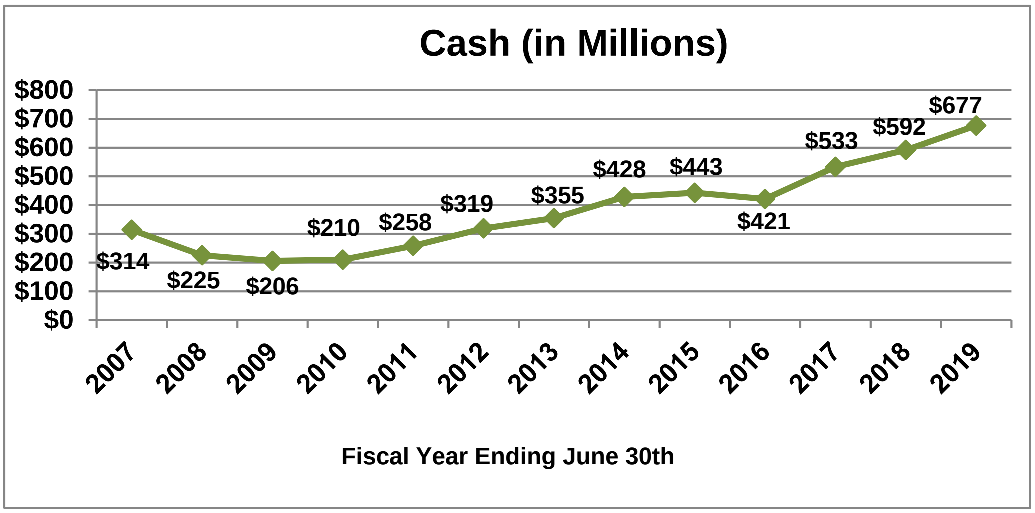
The County maintains an established reserves policy (please see the *Reserves Policy* portion of this document) to mitigate cash flow impacts, maintain best debt ratings and positive borrowing position, and to provide liquidity in the event of a catastrophic event.



(Note: Balances exclude accounts held by other authorities/agencies such as balances held by the Orange County Employees' Retirement System [OCERS].)

During economic downturns, reserves have been used to reduce the severity of impacts to clients and Departments. The County has been committed to building reserves back to a level that provides flexibility to maintain service levels and protects the County's cash position in order to meet its obligations. The current and projected obligated fund balances available to the General Fund reflect a healthier reserve position. Only increases to the Budget Stabilization reserve are forecasted in order to maintain the Government Finance Officers Association (GFOA) recommended target reserve in each of the Plan years. In accordance with Board Resolution 10-136, any excess Fund Balance Unassigned recorded at fiscal year-end is transferred to reserves by the Auditor-Controller during the year-end closing process.

The County is diligent in maintaining an adequate balance of General Fund cash to address timing variances that occur throughout the year between expense and revenue transactions. Based on the current cash management plan, it is anticipated that cash balances will remain stable throughout the financial planning period. The following chart reflects historical cash balances through June 30, 2019. Cash balances dipped between 2015 and 2016 due to timing of Health Care Agency Behavioral Health programs cash receipts. In the following year, the cash increase from 2016 to 2017 was due to the release of a yield-restricted investment to general fund cash. Finally, the increase to cash from 2018 to 2019 is primarily due to increase in property tax revenues, realignment and public safety tax revenues and one-time SB90 revenue and interest payments from the State.



Note: Cash balances are as of June 30 of each year as reported in the Comprehensive Annual Financial Report (CAFR). Cash balance for 2019 is preliminary as of November 14, 2019.

Infrastructure & Capital Expenditures

Economic conditions and competing priorities for General Funds influence how the County addresses capital spending. Beginning in FY 2007-08, like other peer counties, Orange County deferred necessary investments in capital assets and equipment to balance strained budgets and lessen potential cuts to ongoing operations and programs. Since that time, the County has used a portion of the modest growth in revenues to fund previously deferred critical projects such as the Sheriff's CCTV (closed circuit television) jail video system, jail electronic security and electrical upgrades, jail hardening, Sheriff vehicle replacement, and renovation and upgrade to the Katella Training Facility. In addition, one-time revenues are being utilized to repay the OC Waste and Recycling loan for the completed Animal Care Center and to fund upgrades to the County Property Tax System.

Strategies

It is essential that Departments continue to review programs and operations to determine the best practices when sizing programs for future economic conditions and to ensure services to the community are maintained and performance goals are met within the boundaries of available resources. Departments and the County Executive Office are currently planning for the FY 2020-21 budget process with a goal of preserving the capacity to provide quality services to stakeholders, including external clients and employees. Seeking opportunities for additional funding to maintain ongoing operations is essential to the process including efforts undertaken in development of the County's Legislative Platform. In addition, projected budgetary impacts in the Community Services program area from shifts of IHSS program responsibility to counties by the State; growing General Relief costs, and homelessness initiatives mean that re-evaluation of Department budgets and reprioritization of projects will be required during the budget process.

Summary

The County's long-term commitment to a balanced budget and early action has proven successful in maintaining core services with minimum impact to service recipients. Through their commitment to fiscal prudence, the Board of Supervisors developed a vision for the County to address critical community, capital, and organizational needs while also allowing for accommodation of new fiscal challenges and opportunities as they arise. The County continues to make significant progress with key initiatives including construction of the two new Civic Center Buildings and purchase of a building in Santa Ana to provide further homeless shelter capacity.

An ongoing commitment to fiscal prudence will be required as the County attempts to balance the funding of identified needs and priorities and strives to provide high quality services and advance major initiatives. The combined efforts of the Board of Supervisors and County employees toward careful and responsible fiscal management will position the County to overcome new challenges as they arise, while continuing to fulfill the County's mission.

The Board of Supervisors will be apprised of the County's fiscal status on an ongoing basis via the annual and quarterly budget reporting processes and other methods, as appropriate. Carrying out vital services and assurance of responsible management requires that:

- Impacts continue to be evaluated and communicated timely;
- The County continues to apply discipline to financial management;
- Structural balance focused on values and core services continues to be a priority;
- The County continues to seek creative alternatives and partnerships.

Coordinated efforts of the Board and the County employees make it possible to exercise fiscal stewardship and to maintain government core services and priorities.