FIRST 5 LA

APPROVED 1/15/2014

SUMMARY MEETING NOTES
Budget & Finance Committee
December 16, 2013

COMMITTEE MEMBERS PRESENT:
Marvin Southard [Committee Chair]
Sandra Figueroa-Villa
Suzanne Bostwick [Alternate]

COMMITTEE MEMBERS ABSENT:
Jonathan Fielding [Excused]
Jane Boeckmann [Excused]

STAFF PRESENT:
Kim Belshé, Executive Director
Genie Chough, Finance Director
Alison Mendes, Economic Analyst
Raoul Ortega, Finance Manager
Linda Vo, Executive Assistant
John Wagner, Chief Operating Officer

1. Call to Order/Roll Call

The meeting was called to order by Chair Southard. Roll call completed.

2. Review of Meeting Notes –Budget and Finance Committee, September 30, 2013

THE ITEM WAS RECEIVED AND FILED

3. Long Term Financial Projection (LTFP)

Ms. Mendes gives a presentation on the LTFP. She reviews some key points, trends, and big-picture highlights, including a look at both the historical and projected future data on the fiscal position of First 5 LA.

Ms. Mendes informs the Committee that in her conclusion, she will call out the major implications that these projections may have on Commission decision-making moving forward.

She states that the primary goal of the LTFP is to aid in the Commission's financial stewardship role by providing a framework that shows the long-term implications of funding decisions.

She emphasizes that it is important to note that the LTFP is a multi-year forecast, and is not a spending plan, that includes projections of revenue, Fund Balance, program commitments and expenditures, and operating expenditures.

She reminds the Committee that staff had brought a comprehensive LTFP to the full Commission in January 2013, and that there was an update provided with the annual budget at the June 2013 Commission.

Ms. Mendes goes on to inform the Committee that this LTFP presentation looks at the period of FY 13-14 through FY 17-18, extending three years beyond the term of the current Strategic Plan. She highlights that the projections do reflect the Commission's acknowledgement in the Strategic Plan Implementation Plan that the investments outlined in the Strategic Plan—Place-

Based investments and Countywide Strategies—would require more than the Plan's 5 years to fully implement. Accordingly, First 5 LA's projections assume that the Commission will continue to approve funding for these investments beyond June 2015.

Ms. Mendes continues her presentation by informing the Committee that some of the major assumptions within the LTFP include:

1. Fidelity to allocations and other funding decisions made by the Commission. This includes assuming that allocations currently scheduled to expire are NOT extended.
2. Allocations currently scheduled to expire are not extended.
3. Commission will continue to appropriate funds annually for programs associated with the current Strategic Plan that adhere to a zero-based budgeting platform.
4. Operating expenses increase 2% annually through FY 2015-16 with level funding thereafter; assume compliance with the Commission's annual administrative limit of 5%.

Some of the highlights in Ms. Mendes' presentation include the following:

1. Primary revenue source—Proposition 10 tax revenue—has been steadily decreasing since FY 2004-05
2. According to the State Department of Finance, this revenue source is projected to decline over the next four years by approximately 11%, from $90M in FY 13-14 to just over $80M projected for FY 17-18
3. First 5 LA's annual spending began to exceed incoming revenue in FY 08-09. By FY 12-13, First 5 LA's expenditures of just over $200M were more than double its total annual revenue of $93.9M.
4. In FY 13-14, First 5 LA is projected to spend more than $240M and remain above $220M annually through FY 15-16

In essence, anytime First 5 LA spends more than what it brings in in revenue, then it depends on its Fund Balance to cover the difference. Ms. Mendes says that this LTFP presentation shows a clear picture of First5 LA's declining resources—both revenue and Fund Balance—that is projected to continue.

On the next slide, Ms. Mendes goes over a graph that illustrates the difference between incoming revenue and expenditures through the duration of the current Strategic Plan. First 5 LA's revenue is shown in green, while the solid red line represents its expenditures, reflecting actual ability to get funds out the door. Projected revenue and expenditures are shown with dashed lines. Ms. Mendes, once again, reiterates that the current graph does assume that expiring programs are not extended and sunset as scheduled.

In looking at the time period of FY 01-02 through FY 07-08, Ms. Mendes informs the Committee that First 5 LA was building up its Fund Balance because revenue exceeded spending for that time period. Conversely, anytime the expenditure line is above the revenue line, First 5 LA is depending on its Fund Balance to cover the difference. Thus, as First 5 LA spends more than it brings in, a similar decrease in its Fund Balance will be seen. More recently, you can see that First 5 LA has been spending down its fund balance, since expenditures have far exceeded incoming revenue.

Ms. Mendes also explains that First5 LA's expenditures in FY 12-13 were more than double its annual revenue and that this gap is expected to expand during the time frame shown that is shown.

Ms. Mendes notes that the decrease in expenditures through FY 11-12, followed by a significant increase in spending in FY 12-13, is due to a number of factors:

1. Programs related to First 5 LA's prior strategic plan that were previously spending at a consistent rate were now ramping down.

2. At the same time, First 5 LA's current strategic plan investments—such as its place-based investments—were experiencing a slower-than-expected start-up rate; this was compounded by the number of new countywide initiatives that were approved by the Board during FY 10-11, which drew focus away from the investment areas outlined in the current Strategic Plan.

3. Programs ramping up during that fiscal year, including First 5 LA's investments in Welcome Baby/Home Visitation, as well as a number of the new countywide initiatives. These programs have continued to ramp up, demonstrating improved performance by First 5 LA in getting funds out the door.

4. $25M of the increase was due to the new Permanent Supportive Housing initiative and the contract with the Community Development Commission, for which funds were expensed up front

Ms. Mendes goes on to give the following highlights:

1. July 2013 beginning Fund Balance was $723.7 million.
2. Of the total Fund Balance of $723.7 million, about 71% ($513.0 million) is committed to approved Board allocations.
3. Total Fund Balance is projected to decrease by 66% to $249.0 million by June 2018, assuming programs scheduled to expire are not extended.
4. Of the $249.0 million, approximately $16.1 million is estimated to be committed for Board-approved allocations. Assuming FY 2018-19 is comparable to FY 2017-18, roughly $46.9 million would also be set aside for operating costs and the Reserve.

She says that on the next slide, it is important for the Committee to see that there is a significant decrease in spending for Prior Strategic Plan investments (purple) between FY 15-16 and FY 16-17. This is primarily due to the assumed expiration of the LAUP contract, which is scheduled to end in June 2015. She also points out that there is a decrease in spending on Countywide Initiatives (green), which is due to many of these spending down their approved allocation balances and either ramping down or ending according to schedule.

On this slide, Ms. Mendes also points out the following assumptions:

1. First 5 LA is projecting an increase in spending for Family Strengthening between FY 13-14 through FY 15-16, with funding stabilizing in FY 16-17 and FY 17-18 as the programs reach full implementation
2. Based on the cost projections for community-level funding approved by the Board in November 2013, First 5 LA is projecting an increase for FY 13-14, with assumed level funding after that.

Ms. Mendes informs the Committee that based on Finance's forecast, First 5 LA's Fund Balance at June 30, 2018 is projected to be just under $250M, where $16.1 M of this amount is estimated to still be committed for Board-approved allocations. And in assuming FY 2018-19 is comparable to FY 2017-18, Ms. Mendes states that roughly $46.9 million would also be set aside for operating costs and the Fund Balance Reserve.

On another chart, Ms. Mendes explains to the Committee of how more than 75% of the total Fund Balance is already committed to Board-approved allocations. The rest of the breakdown is as follows:

- Approximately 9% is in the Assigned category for use consistent with the Strategic Plan guidelines
- 10% is Unassigned, which includes $17.8M designated for our FY 13-14 Operating Budget and $53.1M designated for our Fund Balance Reserve
- Less than 4% is considered Nonspendable, which includes funds that we have advanced to various contractors or grantees

To better understand her terminology used, Ms. Mendes gives the following terms and definitions:

- <u>Nonspendable</u>: Funds that have been advanced to a contractor or grantee for services to be provided in the future and are considered to be an asset of First 5 LA.

- <u>Committed</u>: Funds appropriated for a specified purpose and directed by the Commission via Resolution. Commission must adopt another Resolution to re-appropriate these funds for other purposes.

- <u>Assigned</u>: Funds are reserved for Commission use consistent with the 2009-15 Strategic Plan (may be referred to as Uncommitted Fund Balance).

- <u>Unassigned</u>: Funds designated for the FY 13-14 Operating Budget ($17.8 million) and Reserve ($53.1 million).

In summary, Ms. Mendes states that each year, First 5 LA is relying on its Fund Balance. As a result, First 5 LA's Fund Balance is projected to decline each year. In the short term, Ms. Mendes states that resources are adequate enough to cover existing obligations through the course of the current Strategic Plan (June 2015). And in the long term, Ms. Mendes states that expenditures will continue to exceed incoming revenue during the next Strategic Plan period, thus putting pressure on the diminishing Fund Balance.

The hope is that this LTFP presentation will inform policy and fiscal decisions made in the context of the new Strategic Planning process. First 5 LA wants to ensure that funding commitments are sustainable and aligned with the Strategic Plan and the Building Stronger Families Framework and that the Commission consider implications of the various funding platforms, such as zero-based or multi-year allocation.

In addition, the LTFP assumes that programs scheduled to expire are not extended. And, if such programs are extended, Fund Balance is projected to be depleted in FY 2018-19. In other words, maintaining the current rate of spending is unsustainable in the long run. Ms. Mendes informs the Committee that for the next strategic planning period, the Commission will face many important and difficult decision in order to align First 5 LA's annual spending with its annual revenue.

Ms. Mendes concludes her presentation and opens up the floor for questions and concerns.

Commissioner Figueroa-Villa would like to know how staff plans to address those motions that come up at the last minute, primarily from Supervisors who sit on the Commission. For example, Commissioner Figueroa-Villa notes that Supervisor Ridley-Thomas has brought forth several motions this past year and would like to understand how staff plans to incorporate motions such as these into their Long term financial projection, understanding that there is a decline in revenues.

Committee Chair Southard says one of the issues that First 5 LA must deal with in regards to this is how the public perceives First 5 LA as having a surplus in its Fund balance. People assume that First 5 LA has a lot of money so it becomes natural to people when a program needs funding that they are turned to First 5 LA.

In response to Commissioner Figueroa's questions and concerns, Ms. Belshé informs the Committee that staff plans on establishing some guardrails for Commissioners regarding proposals for new funding and presenting them before the Commission for its review and consideration. Within these governance guidelines, staff will propose that any motions that are brought forth before the Commission, be vetted through the proper Committee first for discussion, then to the Commission as an information item, and then back to the Commission as an action item. This will allow staff to be able to go back and do the research that is necessary in order for them to do a 5 year fiscal impact on First 5 LA's Fund Balance.

Commissioner Bostwick is pleased with the presentation and feels that it captures all the important and necessary information that the Commission should be aware of in regards to the near and long term fiscal impact when spending is not aligned with the revenue coming in.

Ms. Belshé also informs the Committee that First 5 LA will ask for an approval of the LTFP at the February Commission meeting, instead of just a receive and file. The hope is that an approval will be a more formal acknowledgement by the Commission of its understanding of the major fiscal decisions that it will be tasked with in the near future.

The Executive Committee is in agreement that this is important to share with the full Commission.

There is no further discussion on this item.

4. Budget Development

Ms. Chough gives a brief presentation of the Budget development timeline for FY14-15. She explains to the Committee how First 5 LA's current process is that it requests approval from the Commission twice: on the front end and the back end.

Ms. Chough informs the Committee that there are not too many organizations that request approval twice during the contract approval process. And confirmed by Government Finance Officers' Association, seeking approval from a governing body at two points during the contract process is highly unusual and inefficient. Generally, organizations require approval at either the front-end of the process or the back-end, but rarely both.

Ms. Chough goes on to inform the Committee that staff is proposing two options for the Commissions consideration, with pros and cons of each:

Option 1: Eliminating the Front-end Approval Phase

Currently, Contract Authority is established as part of the annual fiscal year budget. When the Commission approves the budget in June, staff is authorized to start the contract process by developing a Request for Proposals, for example.

If First 5 LA eliminated this front-end contract approval phase, Commission approval would still be required prior to final contract execution. Instead of providing Contract Authority in the beginning of the process, as part of the budget, Contract Authority would be provided at the back-end, as part of the Consent Calendar. Some pros and cons to this approach include the following.

+ Eliminating this front-end approval phase may simplify the administratively burdensome contracting process.

+ Providing Contract Authority as part of the annual budget does not make business sense. The purpose of the budget is to provide a blueprint for Commission funding priorities, including outside spending parameters based on estimates. These spending caps are at the Initiative level. Contract authority should be provided at the individual contract level.

– It is possible that time and resources will have been devoted to a contract that may not ultimately be approved. Generally, staff would proceed with the contracting process based on direction or action from the Commission or Committee. However, without explicit upfront Contract Authority approval, it is possible that once the contract process is complete, Commission members may have concerns or issues with the contract.

–

Option 2: Eliminating the Back-end Approval Phase

As part of the Consent Calendar, the Commission provides Contract Approval allowing staff to execute a negotiated contract based on the contractor, scope of work and funding level.

If we eliminated this back-end approval phase, the Commission would continue to provide Contract Authority through the annual budget process in June. Some pros and cons to this approach include the following.

+ Eliminating the back-end approval phase may shorten the contracting process, allowing staff to execute the contract without having to return to the Commission.

– In order to provide effective oversight and avoid conflicts of interest, the Commission should be aware of the individuals or entities selected for contracts and grants. Though these records can be provided to the Board as informational, it would be after contract execution.

– In light of the recent changes to the Procurement policy, it is necessary to maintain the Consent Calendar, and thus, may not make business sense to eliminate the back-end approval phase for contracts.

– This back-end approval phase implements recommendations included in the 2011 Harvey Rose Audit. Specifically, recommendation 1.3 requires a Board approval process for new grants and contracts with clearly designated dollar thresholds and recommendation 4.2 requires a consent item listing all grantee and contractor agreements, amounts to be approved and other information.

Staff is proposing that First 5 LA eliminate the front-end contract approval phase. Ms. Chough indicates that providing Contract Authority as part of the annual budget does not make business sense nor does it seem to be meaningful information for the Commission that early in the process. AS an alternative, Ms. Chough recommends the following:

1. Budget Authority: The maximum amount or spending cap within which funds may be spent at the Initiative level within a given fiscal year. Budget Authority may be established via the annual budget in June or through a budget amendment approved by the Commission throughout the fiscal year.

2. Contract Authority: Approval to execute a negotiated contract (including the contractor, scope of work and funding level) to reflect the full term of the contract. Commission approval is requested as part of the Consent Calendar.

ADJOURNMENT:

The meeting was adjourned at 9:58 am.

NEXT MEETING:

The next Budget and Finance Committee meeting will take place on January 15, 2014 at 1:30 p.m..

First 5 LA
Conference Room B, First Floor
750 N. Alameda Street
Los Angeles, CA 90012

Summary action minutes were recorded by Linda Vo, Secretary to the Board of Commissioners.