



Committee: Directly to Council
Committee Review: N/A
Staff: Marlene Michaelson, Executive Director
Purpose: Receive briefing and discuss – no vote expected
Keywords: FY22 Budget

AGENDA ITEM #3
April 13, 2021
Discussion

SUBJECT

FY22 Operating Budget Highlights and Approach

EXPECTED ATTENDEES

Rich Madaleno, Chief Administrative Officer
Mike Coveyou, Director, Department of Finance
Jennifer Bryant, Director, Office of Management and Budget

COUNCIL DECISION POINTS & COMMITTEE RECOMMENDATION

- N/A

DESCRIPTION/ISSUE

The Executive submitted the recommended FY22 Operating Budget on March 15, 2021. The Council will receive a briefing on the key elements of the recommended budget as it prepares its work to approve a budget later in May.

SUMMARY OF KEY DISCUSSION POINTS

- FY21 is a year unlike any other as the County faced a global pandemic. **In response to this unprecedented emergency, the Council has appropriated more than \$382 million in FY20 and FY21 to respond to the pandemic.**
- The pandemic has not ended, though there is hope of recovery as vaccination rates increase. The FY22 budget and budget process will continue to be shaped by the ongoing emergency.
- The Federal response has been significant, with the County anticipating receiving more than \$380 million in Federal reimbursements and aid across FY21 and FY22. **This Federal aid plays an outsized role in the County's ability to balance the budget in both fiscal years.**
- **The County's revenue growth is minimal in FY22, even with the additional Federal aid.** The County's total tax supported revenues are anticipated to increase by 0.8% from the FY21 budget.
- The Executive recommended increasing the County Government's budget by 5.0% compared to the FY21 budget. This increase allows for funding and programmatic enhancements several key areas, many of which are part of the County's ongoing response to the pandemic.

- The Executive recommends funding MCPS and the College at each board's request for FY22. Park and Planning's budget is a 3.4% increase compared to the FY21 budget, but it is 3.8% less than the agency's request.
- The Executive's recommended budget includes adding 257.03 FTEs in FY22 across all agencies when compared to the FY21 budget.
- The Executive's recommends additional pay increases for County Government employees in FY22, with a total FY22 cost of \$13.8 million and an annualized cost of \$36.6 million.
- The Executive's recommended budget includes several key assumptions in FY21 and FY22 about Federal aid. These assumptions bolster the County's year-end FY21 position and free up FY22 general fund resources that the Executive has recommended for certain additions and enhancements in FY22. **If the Council is interested in re-examining or revising any of these assumptions, Council staff can provide additional analyses as needed.**
- The Executive's recommended budget achieves an ending reserve level of 9.6% in FY22. Council staff notes several caveats to this ending balance on pages 12-14 of the report. **If the Council is interested in re-examining or revising the Executive's approach, Council staff can provide additional analyses as needed.**
- The Executive recommended fully funding the annual actuarial contribution for OPEB in FY22.
- The Executive recommended funding PAYGO in FY22 at 50% of the policy level. The Council supported fully funding this policy goal when it approved the Capital Budget SAG in February 2021. **If the Council is interested in fully funding PAYGO in FY22, it will need to identify \$15.5 million in resources.**
- **Total tax supported compensation costs for County Government in the Executive's recommended budget increase by 3.2% in FY22, exceeding both the one-year (0.8%) and six-year annual average (2.4%) growth rate for tax supported revenues.** Under the approved policy on compensation sustainability, the Executive is required to explain how the compensation increases will be supported by additional revenues or spending reductions.
- The Council President's recommended approach to the FY22 Operating Budget is included on ©9-10. The Council will aim to target any additional funding increases into one of three categories – 1) One-time, non-recurring expenditures related to COVID-19 that can be funded with Federal aid; 2) additional base budget funding that should be considered if additional resources are identified; or 3) critical expenditures that should be considered in FY22 that require equivalent reductions in FY22 to fund.
- Council staff will continue to collaborate with Executive and agency staff to build a framework, including data and analyses, to inform a more robust racial equity and social justice analysis in future budgets.

This report contains:

Staff Report	Pages 1-18
CAO memorandum on Cost Efficiency Study Group	©1-2
Resolution 19-753 – Reserve and Select Fiscal Policies	©3-8
Council President memorandum on approach to FY22 budget	©9-10
OMB/ORESJ memorandum on Executive approach to racial equity in FY22	©11-13

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MEMORANDUM

April 8, 2021

TO: County Council

FROM: Marlene Michaelson, Executive Director
Craig Howard, Deputy Director
Gene Smith, Legislative Analyst
Aron Trombka, Senior Legislative Analyst, OLO
Nicole Rodriguez-Hernandez, Legislative Analyst
Liz Olsson, Racial Equity and Social Justice Manager

SUBJECT: **FY22 Operating Budget Highlights and Approach**

I. FY22 Budget Context

Montgomery County, along with the rest of the world, has endured a pandemic unlike anything in our lifetimes during the past year. In Montgomery County alone, more than 1,400 lives have been lost. In addition, thousands of County residents have lost jobs, needed assistance with food and rent security, and have had an entire school year disrupted.

The FY21 budget process was one of uncertainty. As a result, the Council made the decision to fund a continuity of services budget in FY21 that did the following:

- Rejected the Executive’s proposed tax increase.
- Eliminated nearly all programmatic and staffing increases proposed by the Executive.
- Funded the County’s educational institutions at the minimum maintenance of effort levels.
- Rejected pay enhancements that were included in collectively bargained agreements.
- Maintained budgeted reserves at the 10% policy level given the uncertainty in revenues and to provide flexibility to address emergency COVID-related funding needs.

The Council and the Executive worked together to address urgent needs in the County by using Federal and State funding made available during the pandemic, as well as County resources. To date, the Council has appropriated more than \$382 million in the FY20 and FY21 budgets as part of the pandemic response as detailed in Table 1 below.

This does not include additional federal funding made available through the second Coronavirus Aid, Relief, and Economic Security (CARES) legislation passed in December 2020 (including additional funding for MCPS and Montgomery College) or the American Rescue Plan Act (ARPA) passed in March 2021. These additional dollars will need to be appropriated either as part of the FY22 approved budget or via separate actions in either FY21 or FY22.

Table 1: Summary of COVID-19 Response Appropriations

Category of Assistance	Selected Programs/Initiatives
<p>Business Assistance: \$67.7 million</p>	<ul style="list-style-type: none"> • PHEG Program: \$20.9 million • Reopen Montgomery Initiative: \$8.9 million • COVID-19 Arts Relief Fund: \$3.6 million • Restaurant Relief Grant Program: \$4.9 million • Hotel Relief Grant Program: \$6.2 million
<p>Health System Support: \$13.0 million</p>	<ul style="list-style-type: none"> • Hospital COVID Response Aid: \$10.0 million • Assistance for Medical and Dental Clinics: \$3.0 million
<p>Assistance to Residents: \$52.5 million</p>	<ul style="list-style-type: none"> • Food Assistance and Security: \$25.1 million • Emergency Assistance Relief Payment Program: \$10 million • Latino Health Initiative – Por Nuestra Salud y Bienestar: \$10.2 million • African American Health Program COVID Response: \$6.6 million
<p>Rental/Housing Assistance: \$53.8 million</p>	<ul style="list-style-type: none"> • Rental Assistance and Eviction/Homelessness Prevention: \$53.4 million • Permanent Supportive Housing for Veterans and Unsheltered Adults: \$355,000
<p>Youth Assistance: \$13.6 million</p>	<ul style="list-style-type: none"> • Educational Enrichment and Equity Hubs: \$3.6 million • Therapeutic Youth Services and After School Support: \$718,000 • Youth Sports Initiative: \$1.56 million
<p>Education: \$66.5 million</p>	<ul style="list-style-type: none"> • MCPS CARES Act and GEER Funding: \$59.6 million • Montgomery College CARES Act and GEER Funding: \$6.9 million

The Council enters the FY22 budget process in a new phase of the COVID pandemic – vaccination rates are increasing, and there is hope for a strong post-pandemic economic recovery. However, the pandemic has a significant, ongoing impact on the FY22 budget as recommended by the County Executive – both in terms of how the budget was constructed and how the Council will conduct its budget review and approval process.

Most notably, the Executive’s FY22 Recommended Operating budget is shaped by federal resource assumptions – typically not an issue the Council and Executive consider as part of the budget development and review process. Significant Federal funding from ARPA and projected Federal Emergency Management Administration (FEMA) reimbursements has assisted the Executive’s recommended FY22 budget in two ways.

- **Bolstering the County’s projected FY21 year-end financial position.** These additional resources increased the estimated FY21 year-end reserve total.
- **Providing additional budget room for FY22 additions and enhancements.** The one-time federal resources and the increased FY21 year-end reserve total allowed the Executive to recommend allocating the County’s general funds elsewhere in the budget.

II. Summary of Executive’s FY22 Recommended Operating Budget

The Executive transmitted his Recommended FY22 Operating Budget to the Council on March 15, 2021. This section provides a broad overview of the Executive’s estimated resources, recommended funding and staffing for the FY22 budget.

A. FY22 Estimated Revenues

The County’s assumptions and estimates for revenues drive the budget process each year. **The total value of revenues determines the size of the “pie” that the County can spend on its fiscal policies, and the agencies’ programs and services.** Annual tax revenues generate the largest portion of the County’s revenues, about 77.0% or \$4,007.7 million in FY22, with the remaining revenues coming from other sources, like intergovernmental aid and charges for services.

State and local governments have experienced uneven revenue impacts due to the pandemic depending on the jurisdiction’s approach to the health orders and specific revenue mixture. Some jurisdictions have experienced significant revenue losses while other jurisdictions are experiencing [revenue surpluses](#).¹ **The County has experienced decreases in most types of revenues due to the pandemic.** The following are the highlights of the County’s shifting revenue picture:

- **Most tax supported revenues have decreased due to the pandemic.** See Table 2 below for the changes in the County’s tax supported resources in FY20-FY22.
- **Intergovernmental aid, which includes ARPA and FEMA reimbursements, plays an outsized role in the County’s resource picture in FY21 and FY22.** Both years see a significant increase to total resources available due to these two funding sources being included in the recommended budget.
- **The economic and revenue impacts from the pandemic will continue through FY21 and beyond.** It could take years for the County to fully understand and integrate the pandemic’s fiscal impact to the County’s revenues.
- **Most County tax revenues are estimated to be less than or equal to FY21 approved revenues** and are not expected to recover to FY21’s levels until FY24 or later.
- **The speed and magnitude of the economic recovery will determine the actual growth rate for the County’s revenues in FY22 and beyond.** There are many unknowns, including the potential impact of the virus variants, rate of vaccinations in the region, and global vaccination rates.

¹ <https://www.nytimes.com/2021/03/01/business/covid-state-tax-revenue.html>

Table 2: Change in Tax Supported Revenues by Category for FY20-FY22 (\$ millions)

	FY20 Actual Difference	FY21 Estimated Difference	FY22 Estimated Difference
Taxes	(16.3)	(40.5)	(181.8)
Other Revenues (e.g., fees)	(14.3)	(67.5)	(38.9)
Total Excl. Intergovernmental	(30.6)	(108.0)	(220.7)
Intergovernmental Aid	(12.2)	189.7	56.6
Total	(42.7)	81.7	(164.1)

Notes: FY20 Actual compares approved budget to actual year-end values, FY21 Estimated is approved budget to estimated values, and FY22 difference is based on the revenues estimated in the FY21-26 fiscal plan that did not include any impacts due to the pandemic.

1. Tax Supported Revenues

The recommended FY22 Operating Budget includes \$5.2 billion in tax supported revenues, an increase of 0.8% from the approved tax supported revenues in the FY21 budget. **The Council must adopt a balanced budget; therefore, total tax supported expenditure growth for all agencies cannot exceed the annual revenue growth.**

Table 3 below compares the year-over-year percent change in the County’s tax supported revenues in FY19-FY23, including the annual average growth estimated for FY22-FY27 and the actual growth from FY11-FY20 to compare the current estimates with historical averages. **Even with additional Federal aid assumed in FY22, the County’s overall revenue growth in FY21, FY22, and FY23 is significantly less than the annual average prior to the pandemic.**

Table 3: Annual Percent Change in Tax Supported Revenues for FY19-FY27

	FY19-FY20	FY20-FY21	FY21-FY22	FY22-FY23	Annual Average FY22-FY27	Annual Average FY11-FY20
Taxes	2.9%	1.0%	0.7%	3.0%	3.2%	3.2%
Intergovernmental aid	6.0%	1.3%	5.7%	(6.1%)	(0.2%)	4.8%
Other revenues	0.9%	5.7%	(15.8%)	1.6%	(1.3%)	1.0%
Total	3.4%	1.2%	0.8%	1.2%	2.4%	3.4%

Note: FY22 Intergovernmental aid includes \$60.3 in federal aid from ARPA and FEMA reimbursements.

2. Tax Revenues

Tax revenues are 77.0% of the tax supported revenues in FY22. Property and income tax revenues are the largest component of the County’s taxes, accounting for about 89.6% of the total estimated tax revenues. Below are notes about the County’s tax revenues as it relates to the FY22 budget.

Property Taxes. Property taxes are anticipated to increase through the six-year fiscal plan. **There has not been any significant decrease to property values during the pandemic, particularly for commercial properties.** Finance staff note that State Department of Assessments and Taxation (SDAT) has not seen any unusual volume of commercial property appeals to date, and there is some sense that commercial properties in the region have not experienced a significant decrease in rent due to business closures. There may be, however, some impact if a significant number of leases were sublet during the pandemic. In this circumstance, the commercial properties will need to find tenants as the master leases expire to replace the tenant or see a decrease in property value.

Income Taxes. Income taxes are estimated to end FY21 slightly greater, about \$12.4 million, than the FY21 approved budget. This is an unexpected boon to the County’s FY21 revenues. This estimate is a significant shift from the mid-year fiscal update in December 2020, when Finance estimated that income taxes would end FY21 \$57.5 million less than approved. The primary reason for the increased estimate is changes in the behavior of pass-through entities (i.e., S-corporations) choosing to pay estimated taxes throughout the year, not wait until April. **This shift in behavior is resulting in additional taxes in FY21, but it is unlikely that this increase will continue through FY22 as the new behavior and tax payments normalize.** Finance only estimates a 0.8% increase to the FY22 income taxes when compared to FY21 approved income taxes.

There are also two items that are reducing income tax estimates in the current budget projections.

- SB496 passed by the State in 2021 exempted unemployment insurance from being taxed for 2020 and 2021. The County receives income tax distributions from the State for multiple tax years, so this change will impact the County for multiple fiscal years. The County’s income taxes were decreased by \$25.0 million in FY21 and \$6.5 million in FY22 to account for this new State law. **The Executive has proposed the use of ARPA funding to offset this decrease in the County’s income tax estimates.**
- The County has begun the repayment to the State due to the Wynne Case. The County’s income tax estimates are reduced by \$7.3 million in FY22, and this reduction will be ongoing for many years.

Other Taxes. Several other tax revenues are anticipated to remain at or below the approved FY21 level through FY24 or later. **Generally, the pandemic and anticipated recovery rate is expected to keep these revenues depressed for several years.** While these revenues account for only 10.4% of the total tax revenues generated, the estimated decrease is about \$53.0 million in FY22.

B. FY22 Recommended Funding by Agency

The recommended budget totals \$5,969.1 million, an increase of \$127.8 million or 2.2% from the approved FY21 Operating Budget. Total tax supported expenditures of \$5,125.2 million are recommended for FY22, an increase of \$62.4 million or 1.2% from FY21. Table 4 details the FY22 recommended budget by agency and debt service.

Table 4: FY22 Recommended Budget by Agency (\$ millions)

Agency	Total Budget			Tax Supported Budget		
	FY22 CE Rec.	Change from FY21		FY22 CE Rec.	Change from FY21	
		\$	%		\$	%
Montgomery County Government	2,258.7	92.7	4.3%	1,775.4	83.5	5.0%
Montgomery County Public Schools*	2,780.5	25.0	0.9%	2,534.9	(27.5)	(1.1%)
Montgomery College	312.6	(5.7)	(1.8%)	265.5	(3.4)	(1.3%)
M-NCPPC	161.6	(4.4)	(2.8%)	141.8	4.6	3.4%
Debt Service	455.6	11.4	2.6%	427.7	5.2	1.2%
Total	5,969.1	127.8	2.2%	5,125.2	62.4	1.2%

Montgomery County Government. The Executive recommends FY22 expenditures of \$2,258.7 million for the County Government, or about 37.8% of the total recommended expenditures. The recommendation for County Government represents the largest increase among the agencies, both for the total budget and for the tax supported portion. In addition to allowing for pay adjustments (described in more detail on pages 8-9), the increased funding for County Government allowed for several important programmatic enhancements:

- Increasing the Working Families Income Supplement by \$20 million, with \$5 million included to support working households using a Tax Identification Number.
- Adding \$5 million to the Early Care and Education NDA.
- Including \$3.6 million to continue the operation of the eight community-based Consolidated Service Hubs.
- Continuation of funding initiated in FY21 and/or new funding for: Mobile Crisis Outreach Team, therapeutic recreation for school-aged children, expanded mental health services for Linkages to Learning, and mental health services for MCPS students and families.
- Adding over \$3 million for operations of the new homeless shelter, in additional to \$13.6 million in capital costs for the purchase and build-out of the facility.
- Increasing funding or staffing in other areas such as affordable housing, climate change, community engagement, and racial equity and social justice.

MCPS. The Executive recommends FY22 expenditures of \$2,780.5 million for MCPS, an increase of 0.9% from the FY21 approved budget and \$40.2 million more than the required Maintenance of Effort (MOE) level. **The Executive’s recommendation fully funds the Board of Education’s request.** The decrease in tax supported funding reflects a technical adjustment in how OMB categorized additional FY22 State Aid. Due to the impact of COVID-19 related public school enrollment declines on MOE funding calculations, the Maryland General Assembly has exempted FY22 local funding from future MOE calculations. As a result, exceeding MOE in FY22 would not increase funding requirements in future years.

Montgomery College. The Executive’s recommended budget for Montgomery College reflects a 1.8% decrease. **This recommendation is \$500,000 above the required MOE level and fully funds the Board of Trustee’s request.**

M-NCPPC. Recommended tax supported funding for Park and Planning is a 3.4% increase from FY21 but **approximately 3.8% less than the agency’s request.** Council staff is reviewing whether the Executive’s level of funding will allow for continuity of services budget and will provide additional analysts at the PHED Committee’s worksession on the M-NCPPC budget.

C. Recommended Staffing by Agency

Changes in Workforce. The Executive’s recommended FY22 Operating Budget provides staffing increases for all agencies except Montgomery College. The Executive’s recommends a total of 257.03 new FTEs, 228.50 of which are tax-supported. The recommendation for County Government includes an increase of 68.93 tax supported FTEs in FY22, slightly greater than the FY21 increase of 53.05 FTEs. Table 5 reflects changes in FTEs by agency.

Table 5: Total Staffing by Agency, FY20-FY22 CE Recommended

	FY20	FY21	Change FY20-21	FY22 CE Rec.	Change FY21- 22
Total All Agencies					
Tax Supported	32,974.63	33,639.44	664.81	33,867.94	228.50
Non-Tax Supported	3,338.96	3,379.05	40.09	3,407.58	28.53
County Government					
Tax Supported	8,579.67	8,632.72	53.05	8,701.65	68.93
Non-Tax Supported	1,853.55	1,886.19	32.64	1,896.46	10.27
MCPS					
Tax Supported	21,649.85	22,257.28	607.43	22,399.34	142.06
Non-Tax Supported	1,217.26	1,219.51	2.25	1,237.27	17.76
Montgomery College					
Tax Supported	1,803.35	1,803.5	0.15	1,803.5	0.00
Non-Tax Supported	107.50	107.50	0.00	107.50	0.00
M-NCPPC (Montgomery)*					
Tax Supported	941.76	946.09	4.33	963.60	17.51
Non-Tax Supported	160.65	165.85	5.20	166.35	0.50

*The FY22 CE Rec. for M-NCPPC is based on the agency request. It is unlikely that M-NCPPC would be able to support this level of staffing based on the Executive’s recommended funding.

Update on Cost Efficiency Study Group. As detailed in an August 6 letter from the Chief Administrative Officer (attached at ©1-2), the County Executive and MCGEO have convened a study group to “analyze existing government operations and consider alternate service delivery methods and organizational structures to better serve the residents of Montgomery County...The primary charge of the Study Group is to identify at least 100 vacant positions that can be abolished across various levels of County government without impacting service delivery.”

The Executive’s FY22 recommended budget does not include any position reductions related to the work of this Study Group. OMB provided the following update on the Group’s status:

The Cost Efficiency Study Group has experienced progress delays, mainly due to scheduling and availability difficulties, but has continued to meet. As of March 24, 2021, we are reviewing the final draft with the consultant, Matrix Consulting Group. We will then identify the next steps and conclude our work with the consultant by the end of April 2021, and then begin the process of reviewing, adapting, and approving recommendations from the report for implementation by Executive staff. While it is expected that the initial steps will include abolishing a small number of positions, the impact of this project is intended to result in more systematic cross-departmental changes over time, and will make service delivery in Montgomery County Government more effective and efficient.

D. Proposed FY22 Pay Adjustments

For FY22, the Executive negotiated pay increases with each bargaining unit. These proposed increases are in addition to the pay increases recommended by the Executive and approved by the Council on March 9, 2021. The FY21 mid-year pay increases included the following components:

- A General Wage Adjustment (GWA) of 1.5% effective June 20, 2021, with costs of \$452,889 in FY21 and \$13.7 million in FY22;
- Service increments and longevity adjustments effective April 11, 2021, with costs of \$3.3 million in FY21 and \$15.2 million in FY22; and
- Elimination of the COVID pay differential as of February 13, 2021, which reduces estimated expenditures by about \$35 million in FY21 compared to the cost of continuing the pay differential through the end of the fiscal year.

Table 6 below shows the FY22 general wage adjustments and service increments negotiated by the Executive. In addition, the Executive recommends funding a past year service increment for eligible MCGEO members who did not receive a service increment during FY11.

Table 6: Executive Recommended FY22 County Government Pay Increases

Employee Group	General Wage Adjustment	Service Increment ²	Past Year Service Increment	Longevity Increment	Lump Sum Payment
MCGEO	\$1,684 (effective June 2022)	3.5%	1.25% from FY11 (effective July 2021)	<u>Non-Public Safety</u> 3.0% at 18 and 24 years of service <u>Public Safety</u> 3.5% at 20 years of service and 2.5% at 24 years of service	\$600 for members not eligible for FY22 service increment
FOP	2.5% (effective Jan. 2022)	3.5%	None	3.5% at 16 and 20 years of service	None
IAFF	1.5% (effective June 2022)	3.5%	None	3.5% at 20 and 24 years of service	None
Non-Represented	\$1,684 (effective June 2022)	3.5%	None	2.0% at 20 years of service (employees with high performance ratings)	None
MLS/PLS	\$1,684 (effective June 2022)	Performance-based pay in lieu of service increments	None	None	None

² Non-MLS/PLS employees would receive the service increment at the first pay period following the employee's hiring anniversary date. The effective date for MLS/PLS performance-based pay increases is July 1, 2021.

In addition to the pay increases in the above table, the Executive also recommends a series of other pay adjustments including shift differential, sick leave payouts, and transit subsidies.

Table 7 shows that the pay adjustments recommended by the Executive would have a combined FY22 cost of \$13.8 million. These estimates include the salary and wage costs as well as employee benefit costs borne by the employer. Service increments account for more than half of the total FY22 cost. General wage adjustment for most employees would take effect at the very end of the fiscal year, resulting in a diminished cost in FY22.

Table 7: Total Cost (all funds) of Executive Recommended Pay Adjustments

	FY22 Cost	Annualized Cost
General Wage Adjustments	\$1,968,763	\$18,907,296
Service Increments	\$7,687,467	\$14,157,097
FY11 Increments	\$734,274	\$734,274
Lump Sum Payments	\$1,055,791	\$0
Longevity	\$474,114	\$884,228
Other	\$1,913,584	\$1,901,900
TOTALS	\$13,833,993	\$36,584,795

As many of the pay adjustments take effect at the end of the year, the amount budgeted for FY22 does not reflect the full annualized cost (that is, the 12-month cost) of the Executive's recommendations. **The annualized cost of the adjustments is \$36.6 million, more than two-and-a-half times greater than the FY22 cost.** As measured in annualized cost, general wage adjustments account for more than half of the total cost of the Executive's recommended pay increases. If approved, these costs will become part of the base budget in FY23 and all subsequent years. Future year annualized cost of the pay increases will have to be funded from on-going (as opposed to one-time) revenue sources.

III. Federal Resources and Fiscal Policies in the Recommended Budget

This section identifies key federal resource assumptions included in the Executive's recommended budget, and reviews adherence to the recently updated fiscal policies resolution.

A. Federal Resource Assumptions in FY21 and FY22's Budgets

The Executive's recommended FY22 Operating Budget includes several key assumptions in FY21 and FY22 about Federal aid. **These assumptions bolster the County's year-end FY21 position and free up FY22 general fund resources, which provides greater flexibility for the Executive's additions and enhancements in FY22.**

The FY21 estimated and FY22 recommended budgets include \$384.5 million in Federal aid due to the pandemic from the CARES Act, anticipated FEMA reimbursements, and ARPA. These resources are summarized below in Table 8 and discussed in more detail on pages 10-14.

Table 8: Summary of Federal Resources

	FY21 Estimated	FY22 CE Rec.	Total
CARES Act*	\$156.1 million	--	\$156.1 million
FEMA Reimbursement	\$83.7 million	\$23.7 million	\$107.4 million
ARPA	\$84.4 million	\$36.6 million	\$121.0 million
Total	\$324.2 million	\$60.3 million	\$384.5 million

*\$27.2 million in CARES Act funding was appropriated in the FY20 budget.

1. FY21 CARES Act Funding

The estimated County Government expenditures have been reduced in FY21 based on the expectation that the remaining CARES Act funding will be used to fund some of the County’s general fund expenditures, such as the pay differential. **The lower estimated expenditures result in fewer reserve resources being used in FY21, yielding a greater ending reserve balance.**

2. ARPA Funding

The County will receive about \$203.8 million through ARPA, and this amount will be received in two equal tranches. The County expects to receive the first \$101.9 million tranche in April or May of 2021, which will be available for the FY21 budget; the second \$101.9 million tranche will be received about the same time next year.

The ARPA law authorizes four broad uses of the funds: 1) respond to the public health emergency, including its negative economic impacts; 2) provide for premium pay for essential workers; 3) provide funds to help offset revenue losses and preserve government services; and 4) investments in water, sewer, and broadband infrastructure. The County is waiting for final guidance from the Internal Revenue Service on specific applications of this funding.

As detailed in the Table 9 on page 11, the Executive’s FY22 budget programs \$84.4 million in ARPA funding in FY21, \$36.6 million in FY22, and leaves \$82.7 million unallocated.

FY21 ARPA Use. The Executive assumes using \$84.4 million of the first tranche of ARPA funding to address certain expenditures in FY21. Like the CARES Act funding, these additional resources aid in balancing the FY21 Operating Budget to yield a greater ending reserve balance. The Executive assumes the following uses for ARPA funds in FY21:

- \$12.4 million to cover previously approved special appropriations that were funded with General Fund Reserves. **The Executive must submit a special appropriation for the Council’s approval to enact this proposed funding source switch.**
- **\$67.0 million to address revenue losses in the General Fund.** This includes \$41.1 million in combined FY21 tax revenue losses (based on FY19 financial statements), \$25.0 million to address lost income tax revenue from the State RELIEF Act, and \$5.9 million in lost revenue in the Bethesda Parking Lot District.

FY22 ARPA Use. The Executive also recommends programming \$36.6 million of ARPA funding in FY22, accounting for the remaining first tranche and part of the second tranche. The inclusion of these resources in FY22 provides flexibility by reducing the need for general fund resources or reserves to fund expenditures. The FY22 ARPA assumptions include:

- \$20.0 million to fund the Working Families Income Support Expansion.
- \$6.2 million to address a projected revenue loss from the State RELIEF Act.
- \$10.4 million in programmatic uses, primarily within HHS and MCEDC.

The Council will review the Executive’s recommended uses of ARPA in FY22 during budget discussions. Committees will consider whether: 1) the proposed use is appropriate for ARPA funds; 2) another source of funding is available for the same purpose (including other ARPA grant funds); and 3) the proposed use aligns with Council’s priorities for use of ARPA funds.

Table 9: Executive Recommended ARPA Uses (\$ millions)

	FY21	FY22
Previously approved special appropriations – funding shift		
19-683 Therapeutic Youth Services	0.31	
19-684 Youth Support and Engagement Hubs	0.41	
19-690 Streeteries Winterization	1.25	
19-695 Por Nuestra Salud y Bienestar	4.62	
19-696 AAHP COVID Response	3.34	
19-709 Conference Center	2.50	
Subtotal	12.43	
Bethesda PLD Debt Service Coverage	5.90	
FY21 Estimated Tax Revenue Losses	41.10	
RELIEF Act	25.00	6.20
FY22 Budget enhancements		
CCT – Remote Proceeding Facilitators & Schedulers		0.27
HHS – Therapeutic Recreation Services		0.75
HHS – Mobile Health Clinic		0.62
HHS – Mental Health Services for MCPS Students & Families		3.60
HHS – Rapid Rehousing Expansion		0.25
HHS – Rental Assistance		0.49
CVB – Backfill Revenue Shortfall Hotel/Motel Tax		1.00
Incubator NDA – Entrepreneurship Ecosystem		0.32
MCEDC – Entrepreneurship Development		0.30
MCEDC – White Flint Project		0.25
MCEDC – Inclusive Economy		0.10
MCEDC – Entrepreneurs in Residence		0.25
MCEDC – Talent Pipeline/Workforce Development		0.10
Working Families Income Supplement		20.00
DTS – FiberNet2 Maintenance		0.50
Cable – FiberNet3 Build Out		0.70
Cable – Digital Equity		0.10
Subtotal		30.41
Total		36.61
Unallocated		82.73

3. FEMA Reimbursements

The Executive's recommended budget includes FEMA reimbursements as resource in the FY21 and FY22 budgets. Based on a brief review, this appears to be the first time this item has been listed as a resource to fund the budget. **Typically, FEMA reimbursements are received for incurred expenditures from a discreet emergency response and are used to replace general fund expenditures after-the-fact.** The nature of this funding means it cannot be relied on as a common resource in the budget. The pandemic has altered the potential magnitude of this resource.

FY21 FEMA. The FY21 budget assumes that the County will receive \$83.7 million from FEMA. **As of this memorandum, the County has only received \$23.9 million from its first submission to FEMA in October 2020.** Like the assumed use of CARES Act and ARPA funding in FY21, the inclusion of FEMA reimbursements as a resource in FY21 allows the County to achieve a greater ending reserve balance and decreases the need for FY22 resources to replenish the reserves. The timing, however, of this resource is unknown. **It is possible that some of the assumed reimbursements in FY21 may be received in FY22.**

FY22 FEMA. The Executive assumes that the County will receive \$23.7 million from FEMA reimbursements in FY22. Like the ARPA funding in FY22, this additional resource grants additional flexibility by reducing the need for general fund or reserve resources to balance the FY22 Operating Budget.

Of note, the FEMA reimbursements assumed by the Executive in FY21 and FY22 reflect already incurred or projected operating costs and do not assume reimbursement for the pay differential. **While atypical, Council staff supports the inclusion of FEMA reimbursement as a resource in the FY22 recommended budget due to the nature of this emergency and with the understanding that: 1) the exact amounts are not guaranteed; and 2) the timing of the reimbursements could shift from FY21 to FY22.**

B. Fiscal Policies

The Council approved an updated fiscal policies resolution in March 2020. [Resolution 19-753](#) retains the previously approved fiscal policies, and the Council's action in March 2020 added the use and replenishment of reserves due to an emergency, clarified the use of one-time revenues, and added the Council's fiscal policies adopted since 2010 (see ©3-8). Below are the highlights from the Executive's recommended FY22 Operating Budget related to the County's fiscal policies.

1. Reserves

The Executive's recommended fiscal plan estimates that reserves will end FY21 at 8.9% of the County's Adjusted Governmental Revenues (AGR) for a total of \$479.3 million. Like all elements of the FY21 budget, this is an estimate and is subject to change until the fiscal year closes. The fiscal plan also estimates that the County will end FY22 at 9.6% of AGR or about \$521.9 million. **Based on the current assumptions and recommendations by the Executive, achieving the 10% policy goal requires an additional \$20.8 million added to the reserves in FY22.** There are several key assumptions that result in the estimated ending level in FY22.

Receipt of \$107.4 million in FEMA reimbursements. To date, the County has received \$23.9 million in FEMA reimbursements. If the actual FEMA reimbursements are greater or less than estimated, the County's reserve level will be adjusted commensurately.

The timing of the FEMA reimbursements is also important. **If some of the assumed FY21 reimbursements are received in FY22, then the December 2021 Fiscal Update will show a lower ending reserve level in FY21 than the Executive's recommended FY22-27 fiscal plan.** The FY22 ending reserve level, however, could still be achieved if the County receives all the estimated FEMA reimbursements and there are no other changes to the County's revenues or expenditures in FY22.

Use of ARPA funding. The Executive recommends using \$84.4 million in APRA funds in FY21 to replace lost revenue and cover eligible expenditures that would otherwise require the use of the General Fund reserves. **The Council must approve the use of ARPA funding as proposed by the Executive in FY21 and FY22 to achieve the assumed reserve level.** Depending on the Council's decisions for this funding, the reserve levels may change.

Final FY21 expenditures must end near the current estimates. FY21 expenditure estimates will continue to change as OMB reviews the quarterly analysis and adjusts for known or unknown expenditures through the remainder of FY21. Also, the Executive has assumed the use of unencumbered CARES funding to address most of the pay differential in FY21. Actual expenditures that differ significantly from the current estimate will impact FY21 final reserves.

The Executive proposes a one-time change to the AGR calculation in FY21 and FY22. The recommended fiscal plan notes that OMB excluded federal funding (CARES and ARPA) from the AGR calculation. **By removing these values from the AGR, the ending reserve percent in FY21 is boosted by about 0.5% and in FY22 by about 0.2%.**

Section 20-65 of the County Code defines the funds and values included in the AGR. AGR includes the County Grants Fund, which is the fund that will administer most of the CARES and ARPA funding. OMB, in consultation with the Office of the County Attorney (OCA), opined that the legal definition for AGR did not envision the one-time Federal aid for an emergency. OMB and OCA staff believe that a budget provision in the County Government's FY22 Operating Budget Resolution is sufficient to address this one-time change. The proposed language is below.

For FY 2021 and FY 2022, the Director of Finance must exclude from the determination of Adjusted Governmental Revenues any advanced funds received by the County to broadly respond to the COVID-19 pandemic under H.R. 748, the Coronavirus Aid, Relief, and Economic Security Act (\$183,336,953) AND H.R. 1319, the American Rescue Plan Act (\$203,774,467) for purposes of calculating the mandatory contribution to the Revenue Stabilization Fund required by County Code Section 20-68.

Council staff believes that it is unclear how the law, as originally constructed, intended to deal with large-scale, one-time federal revenues. However, Council staff:

- Supports the Executive branch’s position that it is reasonable to exclude the CARES and ARPA funding from the AGR calculation in FY21 and FY22 given the unique circumstances of this pandemic. Without this interpretation, the County would need to reserve about 10% of the Federal aid, or almost \$40 million, to avoid decreasing the County’s reserve percent.
- Agrees that the operating budget resolution language proposed by OMB and OCA is an appropriate mechanism to address this issue from a legal perspective as a one-time change.

2. PAYGO

The Executive, like his recommended amendments to the Capital Budget in January 2021, has recommended reducing PAYGO in FY22 by 50%. The Council supported the GO Committee’s recommendation to meet this fiscal policy goal and fully fund PAYGO in FY22 when approving the spending affordability guidelines for the Capital Budget in February 2021.

The Executive’s recommendation reduces the PAYGO funding by \$15.5 million in FY22 but does not specify how those funds were allocated. As a result, Council staff is unable to determine whether these funds are being used for one-time uses (i.e., bolstering the reserve or pandemic response) or are addressing ongoing costs.

3. Use of One-Time Revenues

The County’s one-time revenue policy states that one-time revenues or revenues greater than projections must be prioritized to meet the County’s fiscal policy goals or budgeted as required by law. The Executive’s recommended FY22 Operating Budget assumes a significant level of one-time funding from Federal sources and from the reduction in PAYGO. The Council will need to review how these one-time resources are funding the County’s responses to the pandemic, funding on-going operations, or funding the County’s fiscal policy goals.

As detailed above, the Executive’s budget ties one-time ARPA revenue directly to specific expenditure line-items which the Council will review. **Other one-time revenue from FEMA reimbursements and PAYGO reduction fall to the General Fund and as such are not readily associated with specific expenditures.** As a result, it is difficult to conclude whether some one-time revenue is being used to fund ongoing expenditures.

4. Other Post-Employment Benefits (OPEB)

The Executive’s recommended FY22 budget includes \$92.2 million in tax supported OPEB pre-funding, fully meeting the actuarially determined contribution. This represents an increase of \$2.1 million from the FY22 approved pre-funding of \$90.1 million.

5. Compensation Sustainability

The Council’s approved compensation sustainability policy states that the annual growth rate of total compensation costs (including all wage and benefit costs) should be similar to the annual growth rate of tax supported revenues. If the rates differ, the policy asks the Executive to explain how increases in total compensation costs requested in the budget will be supported by revenues or reductions in expenditures.

Tax-supported compensation costs in the Executive’s recommended FY22 budget exceed approved FY21 compensation costs by 3.2%. The total compensation costs in FY22 included the annualized cost of the pay adjustments approved in FY21, as well as the portion of the Executive’s proposed FY22 pay adjustments that would occur during the fiscal year. As detailed below, many of the pay increases recommended by the Executive take effect at the end of FY22 and much of the cost impact will not occur until FY23.

In contrast, the Executive’s budget projects that tax-supported revenues will grow by 0.8% in FY22. Over the six-year period of FY22 through FY27, the budget assumes that revenues will increase at an average annual rate of 2.4%. **Compensation costs in the Executive’s budget exceed the rate of projected revenue growth for both one year and six years thus triggering the requirement for the Executive to explain how compensation cost increases will be supported by additional revenues or spending reductions.**

IV. FY22 Operating Budget Approach

Council review of the FY22 budget will present a unique set of issues to consider, including differentiating between one time and ongoing revenues, considering short and long-term projections of revenues which have and/or may continue to be impacted by the pandemic, appropriately allocating one-time sources of funding, adhering to the Council’s fiscal policies, and maintaining a focus on supporting those most impacted by COVID-19.

All of this must occur while the time available for Committee review is limited due to remote operations (since the Council cannot hold simultaneous Committee meetings). To ensure that the Council review can successfully address these issues and focus on priorities, the Council President has proposed the strategy outlined below and attached on ©9-10.

1. For FY22, the Council’s budget review will focus on priorities rather than being an exhaustive review of all departments.
2. All departments/programs not identified for priority review will be considered on a “consent calendar” basis to enable the Council to spend most of its time on priority matters. Those departments/programs will be reviewed in greater depth during an oversight worksession in the fall to make sure that the Council can receive program updates and review spending and performance data.
3. The schedule of issues to be considered for full versus consent calendar review has been identified and posted as part of the Council’s Committee schedule. This schedule will be updated if Councilmembers believe issues require further consideration based on new information, such as testimony that raises issues that need to be addressed.
4. While all are optimistic about the County’s recovery from the pandemic, the timing is uncertain and therefore the Council President has recommended a conservative approach to this year’s budget in case revenues are not as strong as hoped over the next year. Ongoing revenue projections and the pace of economic recovery post-pandemic are still uncertain.
5. Potential funding increases proposed by Councilmembers should be put into one of the following three categories:

- **Category #1:** One-time, non-recurring expenditures related to COVID-19 response and recovery that should be considered for unallocated ARPA funding. Since a portion of the ARPA funds will not become available until later in FY22, the Council will have time to make the final determination on use of these funds. After the FY22 budget process is completed, the Council will work with the Executive to determine priorities for ARPA funding.
- **Category #2:** Additions to the base budget that should be considered as soon as additional resources are available. During FY22, perhaps as early as this summer, the Council can consider adding items from this list to the base budget if additional resources become available.
- **Category #3:** Critical expenditures that should be considered for funding in the FY22 base budget. Due to uncertainties for future-year revenues, only the most urgent ongoing expenditures should be considered for addition to the base budget, and they should be limited. The Council will need to identify potential offsetting reductions to the base that could help fund these critical needs while still meeting its fiscal policy goals. Staff will work with the Council to develop options for potential reductions that can provide flexibility if the Council identifies critical additions in this category.

A. Racial Equity Lens for FY22 Budget

Council staff's approach to racial equity considerations in the FY22 Recommended Operating Budget will focus on establishing an official baseline for each department with regards to the application of a racial equity lens to programming and budget decisions. This approach is preferred given the status of where the County is in terms of training employees on racial equity and social justice, developing metrics to measure progress in redressing disparate outcomes, and developing departmental racial equity and social justice action plans. This process will involve identifying gaps in information and analysis necessary to ensure a more rigorous analysis for FY23.

Council staff is following up with departments to request their responses to the questions outlined in the Office of Management and Budget (OMB) and the Office of Racial Equity and Social Justice's (ORESJ) April 2nd memo on Racial Equity and the FY22 Recommended Capital and Operating Budgets (see ©11-13), which include:

- Does your department use quantitative and qualitative data to track program access and/or service outcomes for different population groups?
- Which community residents will potentially benefit the most from your program proposal or be burdened by your program proposal?
- How does the program promote racial equity?

Staff will highlight information provided by those departments able to provide meaningful information in response to OMB's questions in advance of the training that should allow all departments to successfully address these issues.

The Council's Co-Equity Leads will convene the Council's Racial Equity Core Team beginning later this Spring to further align its work with the County's racial equity and social justice goals, including by developing a Racial Equity and Social Justice Action Plan for the Council. This work will also include evaluating what quantitative and qualitative data departments are utilizing, or could potentially utilize, to apply a racial equity lens to budget decisions.

The Racial Equity and Social Justice Manager will also collaborate with the OMB and ORESJ to ensure coordination and alignment between legislative and executive branch efforts and to help inform a more robust racial equity and social justice analysis for FY23 and future budget cycles.

B. Council Review of FY22 Budget Assumptions

As detailed above, the Executive's recommended budget includes several assumptions and uses that the Council will need to consider during the budget process. Some of these items, like recommended uses of ARPA in FY22, can be considered during the committees' review of those specific budget items. Other items, like FY21 assumed uses of ARPA or fiscal policy assumptions, may require additional Council action to enact the Executive's recommendations or broader changes to the structure of the budget if the Council disagrees with the Executive's approach.

Below is a summary of these items. **If the Council is interested re-examining or revising any of the Executive's assumptions, Council staff is prepared to provide additional analysis of options and implications for changes to each.** If the Council would like more information on the fiscal picture prior to making a final decision on any of these aspects, staff can revisit these assumptions with the Council after Committee worksessions are completed but before full Council worksessions begin.

- **Use of ARPA funding in FY21.** The Executive assumes \$12.4 million in ARPA funding in FY21 to fund certain previously approved pandemic response special appropriations. If the Council does not approve all or some of the FY21 funding proposed by the Executive, it would increase the amount of ARPA funding available in FY22. However, it would also: 1) reduce the FY21 and FY22 ending reserve; or 2) require reductions in FY22 base-budget expenditures.
- **FEMA Reimbursements Assumptions.** The Executive assumes a total of \$107.4 million in FEMA reimbursements across FY21 and FY22. Council staff does not disagree with the Executive Branch's specific methodology in developing these assumptions, but also notes that there is not a guarantee that these reimbursements will come in as planned. If the Council wanted to take a more conservative approach by reducing the budgeted FEMA reimbursement, it would likely need to reduce FY22 expenditures by the same amount.
- **Reserve Calculation.** Due to the unprecedented nature of the pandemic and the federal aid that has been made available, the Executive recommends excluding the CARES and ARPA funding from the calculation of AGR. If the Council determines that the AGR calculation should include these federal resources, it would either decrease the projected ending reserve or would require additional federal funds to be held as reserve instead of spent on pandemic response.

- **10% Reserve Policy Goal.** The Executive’s budget does not achieve the County’s 10% reserve policy goal in FY22 or FY23. However, the fiscal plan indicates that the County would achieve the 10% goal in FY23 as required by the current policy. If the Council prefers to achieve 10.0% reserve level in FY22 instead of FY23, an additional \$20.8 million in resources must be identified to add to reserves.
- **PAYGO Policy Goal.** The Council chose to maintain the full PAYGO policy goal as part of the CIP Spending Affordability Guidelines process; however, the Executive chose to fund FY22 PAYGO at 50% of the policy level. If the Council determines that it should fund PAYGO at the policy level, it will need to identify \$15.5 million in resources to restore this funding in FY22.

This packet contains:

Circle #

CAO memorandum on Cost Efficiency Study Group	1
Resolution 19-753 – Reserve and Select Fiscal Policies	3
Council President memorandum on approach to FY22 budget	9
OMB/ORESJ memorandum on Executive approach to racial equity in FY22	11



OFFICE OF THE COUNTY EXECUTIVE
Rockville, Maryland 20850

Marc Elrich
County Executive

Andrew Kleine
Chief Administrative Officer

August 6, 2020

Council President Sidney Katz
Councilmember Andrew Friedson
Councilmember Nancy Navarro
100 Maryland Avenue
Rockville, MD 20850

Councilmembers Katz, Friedson and Navarro,

Thank you for your letter regarding the Cost Efficiency Study Group that has been convened by the County Executive and our MCGEO union partner. This group will analyze existing government operations and consider alternate service delivery methods and organizational structures to better serve the residents of Montgomery County. The group has sought consultant support for this effort, which began out of the collective bargaining process and represents a shared vision of the Executive Branch and MCGEO. This process began prior to the current COVID-19 emergency and resulting economic crisis, which has only magnified the need to prioritize this effort.

The following are the responses to your questions on this Cost Efficiency Study Group:

1. Who is the consultant who will assist the Government Efficiency Work Group, how were the consultant's services procured, how much will the consultant be compensated, and for how long?

In accordance with the County's Procurement Regulations, the County advertised and requested responses to informal solicitation # 1118023 for a consultant to assist the County with its Cost Efficiency Study Group. The County received six submissions. Matrix Consulting Group Ltd. (Consultant) was selected with a bid of \$92,000 for a 12-week project term beginning mid-August.

2. What individuals and organizations are involved in the Work Group? How will findings and recommendations be made and when should the Council expect to receive them?

The Study Group consists of the Director of the Office of Management and Budget, the Director of the Office of Human Resources, the Deputy Chief Administrative Officer, the MCGEO President, and two other MCGEO representatives. The Consultant will assist the group abolish at minimum 100 vacant positions by identifying potential cost savings and/or efficiency enhancements. Additionally,

the Consultant will provide a written report approximately 3 months after the project commences that will contain findings and recommendations. The report will be shared with the County Council once it has been finalized.

3. What are the Work Group's targeted total actual savings and total budgeted savings?

The primary charge of the Study Group is to identify at least 100 vacant positions that can be abolished across various levels of County government without impacting service delivery. Abolishing these 100 positions will create savings as we will eliminate positions that are not currently being lapsed or where the service is being provided via temporary or contractual support. As a result, the project is not targeting a specific dollar value for savings.

Additionally, while the preference would be to eliminate at least 100 vacant positions immediately upon identification, in order to ensure there is no impact to service delivery it may require the eliminations to occur in phases. This phasing would impact any FY21 savings estimates but is not anticipated to affect any long-term savings.

4. Can you provide the total number of positions added to County government in the last two years, and will that figure be included in the Work Group's findings and recommendations?

Full time positions have increased from 9,549 in the FY19 approved budget to 9,733 in the FY21 approved budget, a total net increase of 184. Part time positions have increased from 987 in the FY19 to 999 in FY21, a total net increase of 12. This is a total net increase over the last two years of 196, a 1.86% increase. This two-year increase is less than the preceding two-year increase from FY17 to FY19 of a net 268 additional positions, for a 2.61% increase. Any of these newly created positions that are currently vacant will be included in the review. While several variables concerning vacant positions will be considered, it is not anticipated that there would be any specific focus on positions created in the last two years.

Please let me know If you have any additional questions regarding the Cost Efficiency Study Group.

Sincerely,



FOR

Andrew Kleine
Chief Administrative Officer

CC: Fariba Kassiri, Deputy Chief Administrative Officer
Rich Madaleno, Director, Office of Management and Budget
Marlene Michaelson, Executive Director, Montgomery County Council
Aron Trombka, Senior Legislative Analyst
Gene Smith, Legislative Analyst, Montgomery County Council

Resolution No:	<u>19-753</u>
Introduced:	<u>March 2, 2021</u>
Adopted:	<u>March 2, 2021</u>

**COUNTY COUNCIL
FOR MONTGOMERY COUNTY, MARYLAND**

Lead Sponsor: Government Operations and Fiscal Policy Committee

SUBJECT: Reserve and Select Fiscal Policies

Background

1. Fiscal policy corresponds to the combined practices of government with respect to revenues, expenditures, debt management, and reserves.
2. Fiscal policies provide guidance for good public practice in the planning of expenditures, revenues, and funding arrangements for public services. They provide a framework within which budget, tax, and fee decisions should be made. Fiscal policies provide guidance toward a balance between program expenditure requirements and available sources of revenue to fund them.
3. As a best practice, governments must maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. Fund balance levels are a crucial consideration, too, in long-term financial planning. Credit rating agencies monitor levels of fund balance and unrestricted fund balance in a government's general fund to evaluate a government's continued creditworthiness.
4. In FY 2010, the County experienced an unprecedented \$265 million decline in income tax revenues and weathered extraordinary expenditure requirements associated with the H1N1 flu virus and successive and historic winter blizzards. The costs of these events totaled in excess of \$60 million, only a portion of which was budgeted and planned for.
5. In a memorandum dated April 22, 2010, the County Executive recommended that the County Council restore reserves first to the current 6% policy level for FY11 and also revise and strengthen policy levels in order to more appropriately position the County to weather economic cycles in the future, and to achieve structural balance in future budgets.
6. The County's financial advisor recommended that the County strengthen its policy on reserves and other fiscal policies to ensure budget flexibility and structural stability, and provided specific recommendations, which are reflected below.

7. On June 29, 2010, the Council approved Resolution No. 16-1415, *Reserve and Selected Fiscal Policies*. This resolution established a goal of achieving the Charter §310 maximum for the reserve in the General Fund of 5% of General Fund revenues in the preceding fiscal year and building up and maintaining the sum of Unrestricted General Fund Balance and Revenue Stabilization Fund Balance to 10% of Adjusted Governmental Revenues, as defined in the Revenue Stabilization Fund law.
8. On November 29, 2011, the Council adopted Resolution No. 17-312, *Reserve and Selected Fiscal Policies*. This resolution amended and replaced Resolution No. 16-1415 to further clarify and strengthen the County's reserve policy.
9. On February 22, 2021, the Government Operations and Fiscal Policy Committee reviewed Resolution No. 17-312, *Reserve and Selected Fiscal Policies* in response to the COVID-19 pandemic and its impact on the County's financial stability.
10. The County's reserve and selected fiscal policies should be further clarified and strengthened. This resolution replaces the reserve policy established in Resolution No. 17-312.

Action

The County Council for Montgomery County, Maryland approves the following policies regarding reserves and selected fiscal matters:

1. Structurally Balanced Budget

Montgomery County must have a goal of a structurally balanced budget. Budgeted expenditures should not exceed projected recurring revenues plus recurring net transfers in minus the mandatory contribution to the required reserve for that fiscal year. Recurring revenues should fund recurring expenses. No deficit may be planned or incurred.

2. Use of One-Time Revenues

One-time revenues and revenues greater than projections must be prioritized to meet the County's fiscal policy goals or budgeted as required by law. One-time revenues and revenues greater than projected that remain after any contributions required by law will be applied in the following order until the policy goal is met, or the resources are fully utilized:

- a) Reserves to policy goal.
- b) OPEB more than the annual actuarial prefunding contribution and/or Pension prefunding more than the annual actuarial goal, if unfunded liabilities exist.

- c) Other unfunded liabilities and/or
Other non-recurring expenditures and/or
PAYGO for the CIP more than the County's target goal.

3. PAYGO for the CIP

The County should allocate to the CIP each fiscal year as PAYGO at least 10% of the amount of general obligation bonds planned for issue that year.

4. Fiscal Plan

The County should adopt a fiscal plan that is structurally balanced, and that limits expenditures and other uses of resources to annually available revenues. The fiscal plan should also separately display reserves at policy levels, including additions to reserves to reach policy level goals.

5. County Government Reserve

- (a) **County Government Reserve.** The County Government Reserve has three components. The components of the budgeted reserve at the end of the next fiscal year are:

- (i) **Reserve in the General Fund.** The County's goal is that this reserve will be the maximum permitted by §310 of the Charter, which is 5% of revenues in the General Fund in the previous year;
- (ii) **Reserve in the Revenues Stabilization Fund (RSF).** This budgeted reserve at the end of the next fiscal year is the reserve beginning of the year, plus interest on the fund balance, plus a mandatory transfer from the General Fund, as defined in the RSF law, plus a discretionary transfer if the Council approves one. The actual amount of the mandatory transfer is calculated in accordance with §20-68 of the County Code; and
- (iii) **Reserve in other tax supported funds in the County Government.** The budgeted reserve at the end of the next fiscal year for the following funds – Fire, Mass Transit, Recreation, Urban District, Noise Abatement, Economic Development, and Debt Service – and any other tax supported County Government fund established after adoption of this resolution, should be the minimum reserve possible (as close as possible to zero, but not negative), since the Council sets the property tax rate to the nearest one tenth of 1¢.

- (b) **Calculation of budgeted reserve as a percent of Adjusted Governmental Revenues (AGR).** The target reserve as a percent of AGR is the sum of the reserves in the General Fund and RSF divided by AGR, as defined in the RSF law. The reserves in the other tax supported funds in County Government are not included in this calculation.

- (c) **Budgeted reserve as a percent of AGR.** The County's goal for County Government Reserves is to budget the amount necessary to achieve 10% of AGR annually, except for the emergencies described in paragraph (d) below. The Council may make a discretionary transfer each year from the General Fund to the Revenue Stabilization Fund, if necessary, to reach the County Government Reserve policy goal of 10% of AGR.
- (d) **Use of budgeted reserves during economic recessions or national emergencies.**
 - (i) Definitions: An **economic recession** is defined when the United States Gross Domestic Product, as published by the U.S. Department of Commerce Bureau of Economic Analysis, has experienced negative growth for at least two quarters; and/or the National Bureau of Economic Research has determined that the United States economy is in a recession. A **national emergency** is defined as an event that is a federally declared natural or national disaster or emergency in all or part of the County.
 - (ii) The County's goal is to identify targeted budget reductions to reduce the use of the County Government Reserves during economic recessions or national emergencies. The Council and Executive will work collaboratively to identify targeted reductions that will minimize impact on the County's service delivery in response to the economic recession or national emergency.
 - (iii) The County must replenish the County Government Reserves to its policy goal within three fiscal years following a decrease in County Government Reserves during an economic recession or national emergency. The replenishment schedule must be included in the County's six-year fiscal plan. The County should avoid deferring the replenishment of reserves until the last year of the replenishment period.

6. Reserves in Other Agencies

The reserves for the Montgomery County Public Schools (MCPS), the Maryland-National Capital Park and Planning Commission (M-NCPPC), and Montgomery College are not included in the target reserves for the County Government. The County's reserve policies for these agencies are:

- (a) **MCPS.** The Council should not budget any reserve for the MCPS Current Fund.
- (b) **M-NCPPC.** The reserve in the Park Fund should be approximately 4% of the budgeted resources. The reserve in the Administration Fund should be approximately 3% of the budgeted resources. The reserve in the Advance Land Acquisition Debt Service Fund should be the minimum reserve possible, since the Council sets that property tax rate to the nearest one tenth of 1¢.
- (c) **Montgomery College.** The reserve in the Current Fund should be 3% to 5% of the budgeted resources minus the annual contribution from the County. The target reserve

in the Emergency Plan Maintenance and Repair Fund – as stated in Resolution No. 11-2292, approved by the Council on October 16, 1990 – “may accumulate up to \$1,000,000 in unappropriated fund balance, such goal to be attained over a period of years, as fiscal conditions permit.”

7. Debt Policy

The County’s goal is to remain at or below the debt capacity indicators included in the annual capital budget publication. These indicators are reviewed annually during the spending affordability guideline process for the capital budget.

8. OPEB Policy

The County’s goal for OPEB is detailed in Resolution No. 16-555 or any successor resolution.

9. Other Fund Balances Generally

The County’s goal for fund balances not specifically detailed in this resolution are approved each year with the annual operating budget. These fund balances are reviewed annually during the operating budget review and approval process.

10. Compensation Sustainability Policy

As a means to preserve long-term budget sustainability, the annual growth rate of total compensation costs (including all wage and benefit costs) should be similar to the annual growth rate of tax-supported revenues. In submitting a recommended annual operating budget, the Executive should indicate how recommended compensation cost increases compare with projected rates of revenue growth. Should recommended compensation cost increases exceed the projected one-year or six-year rate of revenue growth, then the Executive should provide a written explanation of: (a) how operating budget resources are re-allocated to pay for total compensation costs; and (b) how the recommended rate of compensation cost growth can be sustained over time.

11. Reports to Council

The Executive must report to the Council:

- (a) The prior year reserve and the current year reserve projection as part of the annual fiscal plan update, usually in December;
- (b) Current and projected reserve balance in the Executive’s annual recommended operating budget;
- (c) Any material changes expected to have a permanent impact on ending reserve fund balance; and
- (d) Current and projected reserve balances in any proposed mid-year savings plan.

This is a correct copy of Council action.



Selena Mendy Singleton, Esq.
Clerk of the Council



MONTGOMERY COUNTY COUNCIL
ROCKVILLE, MARYLAND

TOM HUCKER
Council President

Member, Public Safety Committee
Chair, Transportation & Environment Committee

M E M O R A N D U M

March 29, 2021

TO: County Council

FROM: Tom Hucker, Council President

SUBJECT: Proposed Process for Review of the FY22 Operating Budget

Each year the Council President proposes a process for the review of the operating budget. This year once again presents unique challenges as we continue to deal with the pandemic and our remote operations limit our time for Committee review. The following are my recommendations for this year to allow us to focus on priorities and adhere to the Council's recently updated fiscal policies. The Council Vice-President and Chair of the GO Committee agree with this approach.

1. Consistent with my earlier memorandum, from now until the end of May, the Council should focus on budget and issues related to COVID-19. While most other issues should be deferred until after the budget review is completed, I will consider exceptions for critical issues or ones that require immediate action (e.g., receipt of a grant). This does not include issues already scheduled for Committee or Council review.
2. Remote meetings mean there will not be as much time for Committee meetings as normally occurs during the budget review period (since it is not possible to have two Committees meet at once). Between the limit on time and the need to focus on expenditures related to the pandemic, the budget review should focus on priorities rather than being an exhaustive review of all departments.
3. Obvious priorities are those related to fiscal policy (including taxes) and expenditures necessary to address COVID-19 related issues. Staff have begun the process of reviewing the budget to identify other priorities that they believe will deserve more detailed review. After the public hearings, staff will identify whether additional issues were raised in testimony that should have priority review. Staff will share the draft list of issues to be considered on a consent calendar basis to provide Councilmembers with the opportunity to request a more detailed review of any program/department. Issues identified as priorities will be scheduled for the normal Committee review in April.

4. Programs/departments not identified as requiring priority review this spring would instead be approved via a Consent Calendar-type format (first in Committee and then at full Council). However, those programs/departments will be scheduled for a Committee oversight review session in September to make sure that the Council can meet with Department Directors, receive program updates, and review spending and performance data.
5. Many of the underlying assumptions in the budget and key fiscal policies should be reviewed by the Council in early April, before the Committees begin work on individual budgets – in particular, the calculation of the reserve, the assumptions regarding FEMA reimbursements, and PAYGO. Staff will also review the impact of the State budget and how American Rescue Plan Act (ARPA) funds have been allocated.
6. We all continue to be optimistic about the County’s recovery from the pandemic, but I recommend a conservative approach to this year’s budget in case revenues are not as strong as hoped over the next year. Ongoing revenue projections and the pace of economic recovery post-pandemic are still uncertain. Any additional revenues that become available should be used to further bolster reserves and increase PAYGO.
7. In general, I recommend we limit potential funding increases to the following three categories:
 - **Category #1: One-time, non-recurring expenditures related to COVID-19 response and recovery that should be considered for unallocated ARPA funding.** Since a portion of the ARPA funds will not become available until later in FY22, we have time to make the final determination on use of these funds. After the FY22 budget process is completed, the Council will work with the Executive to determine priorities for ARPA funding.
 - **Category #2: Additions to the base budget that should be considered as soon as additional resources are available.** During FY22, perhaps as early as this summer, the Council can consider adding items from this list to the base budget if additional resources become available. For example, receiving more FEMA reimbursements than anticipated could free up County General Fund dollars.
 - **Category #3: Critical expenditures that should be considered for funding in the FY22 base budget.** Due to uncertainties for future-year revenues, only the most urgent ongoing expenditures should be considered for addition to the base budget and they should be limited. It is likely that we will need to identify potential offsetting reductions to the base that could help fund these critical needs while still meeting our fiscal policy goals.
8. Our staff will develop options for potential reductions that can provide flexibility if the Council identifies critical Category #3 additions to the base budget.



MONTGOMERY COUNTY MARYLAND
ROCKVILLE, MARYLAND 20850

MEMORANDUM

April 2, 2021

TO: Tom Hucker, President, County Council

FROM: Jennifer Bryant, Director, Office of Management and Budget
Tiffany Ward, Director, Office of Racial Equity and Social Justice

SUBJECT: Racial Equity and the FY22 Recommended Capital and Operating Budgets

Background

In the Fall of 2020, Office of Management and Budget (OMB) staff received training from the Director of the Office of Racial Equity and Social Justice (ORESJ). This training and facilitated discussion helped to equip analysts with some of the tools and thought processes they could use in bringing a racial equity lens to their analyses. The ORESJ Director urged OMB and departments to consider who benefits and who is burdened by budget proposals to avoid negatively impacting communities that are already marginalized, and to ask departments how their program proposals promoted equity.

Working closely with ORESJ, OMB ramped up incorporating racial equity and social justice considerations into the budget process to ensure that budget decisions were made to advance racial equity considerations in the County, with the intent to advance racial equity and social justice thinking on all fronts. This has included:

- Instructing departments to consider these factors in proposing potential budget reductions and additions;
- Discussing the equity dynamics of proposed budget changes during the OMB, department head, and County Executive budget review meetings;
- Including representatives from ORESJ in County Executive budget meetings;
- Meeting with Council of Government (COG) and Maryland-National Capital Park and Planning Commission (M-NCPPC) staff to understand the equity data and related analysis those agencies have been developing, and how it might be used in OMB's budget analyses;
- Extracting data from Montgomery County Public Schools' (MCPS) most recent budget book publication related to FARMS rates and ethnicity composition per school and linking those data points to MCPS' Capital Improvement Program (CIP) projects; and
- Explaining to the community during CIP Resident Advisory Board and Operating Budget Forums the importance of incorporating racial equity and social justice considerations into the budgeting process.

Racial Equity and Social Justice in the Capital Budget

In some respects, it has been easier to develop CIP racial equity and social justice analysis tools because facilities have concrete locations that can be mapped and compared to easily available demographic data. As a result, OMB has worked with ORESJ, COG, M-NCPPC, and the DTS to map all current and proposed CIP projects to specific census tracts with the related demographic income and ethnicity data. OMB has also incorporated data regarding census tracts that COG has identified as Emphasis Equity Areas due to high ratios of concentration of low-income population and/or minority groups with respect to regional averages.

OMB, using COG's methodology, has also determined the equivalent values for ratios of concentration per ethnic group, low income, and equity emphasis areas with respect to the County's averages. OMB has also incorporated MCPS ethnicity and FARMS data into its data systems so that proposed MCPS and related Department of Health and Human Services (DHHS) projects (i.e. Linkages to Learning) can be understood in the context of the communities they serve. Using this data, OMB has developed reports that were used to evaluate the likely equity impacts of possible changes to the CIP. OMB will continue developing and making available reports to assist in budget decisions. These reports and related maps will be available to Council staff, and OMB is in the process of setting up training for Council staff on these tools.

Racial Equity and Social Justice in the Operating Budget

For the FY22 operating budget development process, OMB, working with ORESJ, developed and dedicated a section of the program proposal form to addressing racial equity. The purpose was to prompt departments to integrate racial equity into their program proposals (budget requests) at the proposal development phase. Departments were:

- Provided a definition of racial equity; and
- Were asked the following guiding questions:
 - Does your department use quantitative and qualitative data to track program access and/or service outcomes for different population groups?
 - Which community residents will potentially benefit the most from your program proposal or be burdened by your program proposal?
 - How does the program promote racial equity?

OMB received a variety of responses to the questions posed. Some departments were able to provide more refined answers because of the nature of their core mission. For example, DHHS largely already applies a racial equity lens to their budget requests because many of the residents served are from marginalized communities. In preparing their analyses, OMB analysts actively discussed the responses to the racial equity questions with department staff and directors, considered how those thought processes can be incorporated into recommendations, and presented those recommendations to the County Executive for consideration.

The results of these efforts primarily fall into two categories – potential budget reductions not taken and budget additions. When OMB began the budget development cycle, the fiscal picture was uncertain and potentially very bleak. As a result, OMB had to prepare two savings plans, and solicited budget reduction recommendations from departments for FY22. By using an equity lens, departments, OMB, and the County Executive ruled out many potential reductions from consideration. For example, CIP amendments did not delay funding for any projects in Equity Emphasis Areas unless there were other factors that would have necessitated delays, and many program reduction proposals that would have largely impacted marginalized communities were

rejected out of hand. Similarly, new or expanded recommended CIP projects (i.e. Linkages to Learning, Homeless Shelter) and operating budget additions (such as the expansion of the Working Families Income Supplement program and the budget actions surrounding reimagining public safety) generally address issues that relate to racial equity and social justice.

Future

ORESJ is using, in part, the methodology taught by GARE (Government Alliance on Race & Equity) to develop plans to address racial equity challenges. Some of the stages to implementation are:

- Normalize;
- Organize; and
- Operationalize.

As part of the implementation of the County's Racial Equity and Social Justice initiative, the ORESJ will:

- Perform an equity assessment to identify the County policies and practices that do not advance racial equity and that must be modified to address racial disparities;
- Develop metrics to measure the progress in redressing disparate outcomes based on race and social justice;
- Work with County departments to develop racial equity and social justice action plans to remedy issues adversely impacting county residents;
- Provide training to County employees on racial equity and social justice; and
- Develop short-term goals and long-term plans to redress disparate outcomes based on race and social justice as well as develop metrics to measure success and progress.

The incorporation of more robust racial equity and social justice tools into the budget process will be iterative. OMB will work with ORESJ to:

- Provide broader training to County staff to facilitate more meaningful equity analysis and program design;
- Find new ways to incorporate the input of marginalized communities earlier into the budget process;
- Consider the equity implications of base budget programs; and
- Develop additional analytical tools to facilitate equitable budgeting.

JB/TW;jw

Attachments: Capital Budget Reports

c: Richard S. Madaleno, Chief Administrative Officer
Fariba Kassiri, Deputy Chief Administrative Officer
Dale Tibbitts, Special Assistant to the County Executive
Debbie Spielberg, Special Assistant to the County Executive