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TO: BOARD OF SUPERVISORS

FROM: FINANCE COMMITTEE
Mary N. Piepho, Chair
John Gioia

Contra Costa County

DATE: November 14, 2006

SUBJECT: **County Budget Policy**

SPECIFIC REQUEST(S) OR RECOMMENDATION(S) & BACKGROUND AND JUSTIFICATION

RECOMMENDATION:

ACCEPT report from the Finance Committee on the need for a formal County Budget Policy; ADOPT the attached County Budget Policy (Resolution 2006/677).

FISCAL IMPACT:

No specific fiscal impact.

BACKGROUND:

On November 2, 2006 the Finance Committee reviewed and discussed a report regarding establishing a County Budget Policy. The Committee directed staff to report to the full Board on November 14, 2006 the recommendation to adopt the attached County Budget Policy (Resolution 2006/677).

In June, 2006 Standard & Poor's announced new Financial Management Assessment Criteria[1]. This announcement was important. In the past, it was difficult to judge how an agency would be rated; now rating agencies are starting to provide investors with specific assessments of issuer's policies, or lack thereof. There is a long history of "public policy analysis" and "public finance". The Government Financial Officers Association (GFOA), Securities and Exchange Commission, National Federation of Municipal Analysts, and rating agencies all promote sound financial disclosure policies, but only recently began formal "scoring" of polices. The National Advisory Council on State and Local Budgeting (NACSLB), which was created by the GFOA and other public sector associations, published the first comprehensive report on best practices in 1998. The publication was formalized from the lessons learned from public sector crises[2]. There obviously exists a correlation between poor disclosure policies and fiscal crisis.

CONTINUED ON ATTACHMENT: ________ YES SIGNATURE: Lisa Driscoll

____ RECOMMENDATION OF COUNTY ADMINISTRATOR ____ RECOMMENDATION OF BOARD COMMITTEE
____ APPROVE ____ OTHER

SIGNATURE(S):

ACTION OF BOARD ON November 14, 2006 APPROVED AS RECOMMENDED X OTHER X

Speaker: Roland Katz, P.E.U. Local 1, Martinez, Ca.

VOTE OF SUPERVISORS

X UNANIMOUS (ABSENT IV)
AYES: ____ NOES: ____
ABSENT: ____ ABSTAIN: ____

I HEREBY CERTIFY THAT THIS IS A TRUE AND CORRECT COPY OF AN ACTION TAKEN AND ENTERED ON MINUTES OF THE BOARD OF SUPERVISORS ON THE DATE SHOWN.

Contact: Lisa Driscoll 335-1023

Cc: Steve Ybarra, Auditor Controller
County Budget Cabinet (via CAO)

ATTESTED November 14, 2006
JOHN CULLEN, CLERK OF THE BOARD OF SUPERVISORS

BY: Lee O'Leary, DEPUTY

[1] "Financial Management Assessment in U.S. Public Finance" and "Public Finance Criteria: Financial Management Assessment", articles by Standard & Poor's, June 27, 2006.
[2] New York City (1975), Orange County (mid 1990s), Nassau County (late 1990s).

What did Standard & Poor's (S&P) June report say and how will it impact Contra Costa County? S&P enhanced its Financial Management Assessment. The Financial Management Assessment (FMA) conveys to investors the quality of an issuer's financial management practices. Scores will be assigned to general governments such as counties, including Contra Costa County. Although S&P has always evaluated the County's financial polices as one of the four key credit areas[3], this new scoring mechanism is a more explicit way of reporting analytical results. Interestingly, FMA will not score the County's governing body or the effectiveness of its governance practices and issues of public policy; but will focus on the existence and implementation of practices, not necessarily the results of those practices. The results of the practices will be visible in fund balances and annual budgets. In other words, FMA focuses of whether polices have the *potential* to move credit quality away from what current results indicate. Issuers who rank well are those whose policies help reduce the likelihood of credit deterioration and whose polices help them benefit from changing conditions (economic, budgetary, statutory or personnel related. This is important to Contra Costa County.

Given this information, what are the most important financial management practices? Fitch Ratings answers this question in an article entitled "The 12 Habits of Highly Successful Finance Officers"[4]. Our Advisor has indicated that the three **most significant** practices/policies are:

1. Fund balance reserve policy/working capital reserves[5];
2. Debt affordability reviews and polices; and
3. Superior debt disclosure practices.

The four **significant** practices/polices are:

4. Multiyear financial forecasting;
5. Monthly or quarterly financial reporting and monitoring;
6. Pay-as-you-go capital funding polices; and
7. Rapid debt retirement polices (greater than 65% in 10 years).

And finally, five **influential** practices/polices are:

8. Contingencies planning polices;
9. Policies regarding nonrecurring revenue;
10. 5-year capital improvement plan that integrates operating cost of new facilities;
11. Financial reporting awards; and
12. Budgeting awards.

How can these practices be applied to policy areas? S&P compresses these "12 Best Practices" to Seven Policy Areas:

1. Revenue and expenditure assumptions (high weight). Are the County's financial assumptions and projections realistic and well-grounded from both long-term and recent trend perspectives?
2. Budget amendments and updates (high weight). Are there procedures for reviewing and amending the budget based on updated information and actual performance to assure fiscal targets are met?
3. Long term financial planning (average weight). Does the County have a long-term financial plan that allows it to identify future revenues and expenditures as well as address upcoming issues that might affect these?
4. Long term capital planning (less weight). Has the County created a long-term capital improvement program?
5. Investment management polices (less weight). Has the County established policies pertaining to investments, such as the selection of financial institutions for services and transactions; risk assessment; investment objectives; investment maturities and volatility; portfolio diversification; safekeeping and custody; and investment performance reporting, benchmarking and disclosure?

[3] Management Factors, Economic Factors, Fiscal Factors, and Debt Factors.
[4] Criteria Report dated November 21, 2002.
[5] GFOA recommends an unreserved fund balance of 5-15% of General Fund Expenditures or revenues, whichever is less volatile (Contra Costa's reserve is 8.4% as of June 30, 2006.

6. Debt management policies (less weight). Has the County established policies pertaining to the issuance of debt, such as projects that may or may not be funded with debt (including economic development projects); maturity and debt service structure; use of security and pledges; credit enhancement and derivatives; and debt refunding guidelines?
7. Reserve and liquidity policies (less weight). Has the County established a formalized operating reserve policy, which takes into account the County's cash flow/operating requirements and the historic volatility of revenues and expenditures through economic cycles?

Finally, how are scores assigned? After each of these areas has been reviewed S&P assigns an overall "Score":

- **Strong** indicates that practices are strong, well-embedded and likely sustainable; County maintains best practices that support credit quality and are used in daily operations; policies may be formal
- **Good** indicates that practices are good, but not comprehensive; County maintains best practices that support credit quality and are used in daily operations, especially in the finance department; practices may not be formal, may lack detail and long-term elements, or may have little recognition by decision makers outside the finance department
- **Standard** indicates the finance department maintains adequate policies in most, but not all, key areas; policies may lack formal detail and may not include best practices
- **Vulnerable** indicates the County lacks policies in many areas deemed critical for credit quality support; suggests high degree of uncertainty regarding County's ability to effectively adapt to changing conditions that could threaten long-term financial position

THE BOARD OF SUPERVISORS OF CONTRA COSTA COUNTY, CALIFORNIA

Adopted this Resolution on November 14, 2006, by the following vote:

AYES: I, II, III, V
NOES: NONE
ABSENT: IV
ABSTAIN: NONE

Resolution No. 2006/677

Subject: ESTABLISHING A)
COUNTY BUDGET POLICY)

WHEREAS, the Board of Supervisors has an interest in the County's long-term financial stability, service delivery consistency, and departmental empowerment;

WHEREAS, the Board wishes to be a leader in County public service delivery in this country;

WHEREAS, the establishment and maintenance of a budget policy is a key element in enhancing the management of the County's finances and maintaining the County's credit quality;

WHEREAS, services will be supported as the County achieves and maintains an Aa2 (Moody's)/AA (Standard & Poors) credit rating, maintains its facility and equipment assets in "good" to "excellent" condition, promotes a highly skilled workforce, and effectively responds to the changing needs of its residents;

WHEREAS, the Board whishes to recognize that Contra Costa County has the experience/asset of 25 Department Heads who are experts in their particular fields, and are committed to helping the County continue to achieve its goals;

WHEREAS, it is the County's desire to improve its fiscal health by continuing to establish formal fiscal policies;

WHEREAS, these Budget Policies have been prepared to guide, advise, and empower our Department Heads in providing services to residents of Contra Costa County.

It is hereby RESOLVED by the Board that:

1. Contra Costa County shall annually adopt a budget that balances on-going expenditures with on-going revenue.

2. Contra Costa County shall adopt a budget each year early enough (and no later than May 31) to allow all impact on programs and/or revenues to be in effect by July 1.

3. Contra Costa County shall prepare multi-year (3-5 year) financial projections as part of the annual budget planning process.

4. Contra Costa County shall at a minimum prepare formal mid-year budget reports to the Board of Supervisors detailing actual expenditures and projections through the remainder of the fiscal year. This report will include through December 31 of each year:
   a. actual net County cost by department by fund
   b. actual and budgeted expenditure by major object by department
   c. actual and budgeted revenue by major object by department
   d. If a particular cost center is projected to be over-budget, a report clearly indicating planned corrective action will be presented to the Board of Supervisors within 30 days of the mid-year report. If necessary, this report will include appropriation and revenue adjustments.

5. The County will not directly allocate a specific General Purpose Revenue source to specific programs/communities. The policy would not apply to mitigation revenue that is derived from a project and intended to offset the environmental impacts from the project on the "host" community.

6. Short-term funding sources shall be used for short-term requirements, one-time uses, or contingencies.

7. Revenue windfalls not included in the budget plan will not be expended during the year unless such spending is required in order to receive the funding.

8. Fee-for-service and federal/state revenue offsets will be sought at every opportunity.

9. As part of the annual budget process, each department shall analyze its fee structure in order to maintain maximum offset for services.

10. The Board of Supervisors shall make reserve funding available for venture capital to be used to increase efficiencies and economies in departments, that do not have resources available within their normal operating budgets for such expense. Requests for these funds will be included as part of the annual budget process.

11. The year-end practice of "use it or lose it" shall be changed to "save it and keep it". The County Administrator's Office will continue to refine the concept of fund balance sharing as an incentive to departments to maximize resources. Some portion of fund balance credit may be used by operating departments for one-time expenditure. These one-time expenditures shall be used to maximize economy/service delivery/efficiencies/employee satisfaction. Unless specific arrangements are made with the County Administrator's Office, fund balance credit will be spent/encumbered within the following fiscal year.

12. The annual budget process will include funding decisions for maintaining the County's facility assets, allowing the Board of Supervisors to weigh competing funding decisions using credible information.

13. Beginning in FY 2008-09, the annual budget process will include a strategic planning and financing process for facilities renewal and new construction projects (short and long term capital budgets) and establishment of a comprehensive management program for the County's general government real estate assets relative to acquisition, use, disposition, and maintenance.

I hereby certify that this is a true and correct copy of an action taken and entered on the minutes of the Board of Supervisors on the date shown:

ATTESTED: (date) 11/14/2006

JOHN CULLEN, Clerk of the Board of Supervisors and County Administrator

By Lena O'Neal, Deputy

Contact: Lisa Driscoll 925-335-1023
cc: Steve Ybarra, Auditor-Controller
County Budget Cabinet

RESOLUTION NO. 2006/677