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Date: June 11, 2019

To: Members of the Board of Supervisors

From: Sheryl Bratton, County Administrator

Re: Recommendations to Adopt Additional and Amend Current Financial Policies

The Board has a number of financial policies in place to provide a sufficient financial base and the resources necessary to support and sustain adequate and responsible levels of community services. The cornerstone of Sonoma County's financial policies is "fiscal integrity." The current set of financial policies can be found in the FY 2019-20 Recommended Budget book (starting at page 3), as well as the County's website at http://sonomacounty.ca.gov/CAO/Public-Reports/Budget-Reports/.

I am recommending that the Board adopt the following additional financial policies to strengthen our ability to remain fiscally sustainable and to help us prepare for the future:

- Unfunded Pension Liability Pre-Payment Policy
- Shared Service Contract Cost Recovery Policy
- Fund Balance language clean up

In addition, policies related to Government Accounting Standards were reviewed by staff in the Auditor-Controller-Treasurer-Tax Collector's Office and the County Administrator's Office, and certain revisions are suggested to clarify accounting practices. There are no substantive policy changes associated with these additional edits.

Unfunded Pension Liability Pre-Payment Policy

On September 11, 2018, the Board of Supervisors approved its Ad-Hoc Pension Committee's recommended strategies for reducing the County's unfunded pension liability. One of the strategies addressed was making accelerated payments toward the Retirement System's Unfunded Actuarial Accrued Liability (UAAL). The report called for the County to:

> *Implement a structured approach for making recurring accelerated UAAL payments annually, financed with a baseline employer contribution equal to 0.5% of pensionable payroll, and*

supplemented by ad hoc prepayments approved by the Board during annual Budget Hearings, and potentially financed by available year-end funds.

In accordance with this recommendation, staff recommend the following policy be added to the financial policies:

In order to further the Board's pension reform goals, the County will implement an ongoing, structured approach for pre-paying unfunded pension liabilities on an annual basis. Effective Fiscal Year 2019-20 a baseline annual pre-payment contribution equivalent to 0.5% of pensionable payroll will be made (above and beyond the required employer contribution rate). In order to maximize employer cost avoidance as a result of pension discount costs, the pre-payment will be applied to the longest outstanding layers of the County's share of Unfunded Actuarial Accrued Liability, as determined by annual actuarial valuations of the Sonoma County Employees' Retirement Association. In addition, the Board will consider use of available one-time funding to make additional pre-payments as funding is available.

The most recent actuarial reports on the status of the Other Post-Employment Benefits funding indicate that the full budgeted rate of collections toward this funding is not needed. If approved, 0.5% budgeted for payment of OPEB will be redirected toward prepayment of the pension UAAL. This will allow implementation of this policy without further impact to departments in the FY 2019-20 budget.

For further information on unfunded liabilities, see Tab 3.

Shared Service Contract Cost Recovery Policy

From time to time, the County enters into agreements with other public agencies to provide shared services. Examples of such agreements include those with the Town of Windsor and the City of Sonoma for the Sheriff's Office to provide police services and agreements to provide staffing to the Local Area Formation Commission. In the past, there has not been a clear financial policy regarding cost recovery in these contracts, and at times they have not achieved full cost recovery either through explicit discounts or through failure to capture the full cost of services, including costs associated with unfunded pension liabilities.

In order to clarify the expectations for Departments and outside entities that may be considering such contracts in the future staff recommend that the following policy be adopted:

Shared service contracts with other political jurisdictions should include full cost recovery for any portion of services provided by the County, including recovery of full future retirement costs of County employees who act as employees for the other jurisdiction, unless otherwise directed by the Board of Supervisors. Any contract being brought to the Board that does not achieve full cost recovery should be accompanied by specific information about what level of subsidy is being provided and a justification for doing so.

This policy would not affect existing agreements, but would guide any future agreements, including extensions of current agreements. At their discretion, the Board of Supervisors could approve an agreement for less than full cost recovery if it was found to be in the public interest and was supported by the board, but the onus would be on the requesting Department to explain and justify any subsidy being provided to the Board, so that the such a decision would be made through informed deliberation.

Additional Technical Modifications

In addition to the Basic Fiscal Principles, the Financial Policies lay out a number of more technical items, such as the accounting basis used in the budget and the way the County classifies funds in accordance with Government Accounting Standards. These policies are periodically reviewed by the Auditor-Controller-Treasurer-Tax Collector's Office as well as County Administrator Staff in order to ensure that they are clear and accurately reflect the County's compliance with current standards. This year staff are recommending significant reorganization of these sections, to include proper elements under the "Government Accounting Standards" section rather than the "Other Policies and Methodologies" section and clarification of some language in the items.

In addition, these edits update the schedule for capitalization and depreciation/amortization of capital assets to bring it in line with current standards. The changes to this include:

1) Reduction of the capitalization threshold for software from $100,000 to $25,000
2) Removal of the $5,000 threshold for capitalizing Non-Amortizable Intangibles
3) Change of the depreciation/amortization schedule for:
    a. Buildings from 50 years fixed to 15-50 years
    b. Infrastructure from 30-50 year to 25-50 years
    c. Software from 7 years to 3-10 years.

Staff recommend adoption of these modifications, which do not significantly change county financial operations and clarify the policies and bring them in line with current standards.