Department of County Management

Finance & Risk Management Division

Multnomah County

TO: Board of County Commissioners

FROM: Eric Arellano, Chief Financial Officer

DATE: May 15, 2020

SUBJECT: FY 21 Financial and Budget Policies
FY 21 Investment Policy

FINANCIAL AND BUDGET POLICIES

GENERAL OVERVIEW

The County's Financial and Budget Policies set the framework for financial and budgetary decision making for the organization. The policies reflect the short and long term direction of the County Board. The policies reflect best practices set by the Government Finance Officers Association (GFOA) and are organized under four principles of budget process:

- Establish broad goals to guide decision making
- Develop approaches to achieve goals
- Develop a budget consistent with those principles
- Evaluate performance and adjust when necessary

The polices reflect the intent of the Multnomah County Board of Commissioners to comply with all federal and statutory requirements, Generally Accepted Accounting Principles (GAAP), and Governmental Accounting Standards Board (GASB) requirements.

The policy goals of the financial policies are:

1. To preserve capital through prudent budgeting and financial management
2. To achieve the most productive use of County funds that meets the goals of the Board of County Commissioners.
3. To achieve a stable balance between the County's ongoing financial commitments and the continuing revenues available to the County.
4. To leverage local dollars with federal and state funding/grants.
5. To support accountability to the citizens of Multnomah County.

The policies are organized into 16 statements listed below:

- General Fund Forecast
- Tax Revenues
- Federal/State Grants and Foundation Revenues
- Recovery of Indirect Costs
- Use of One-Time Only Resources
- User Fees, Sales, and Service Charges
- General Fund Reserve

- General Fund Contingency
- Capital Asset Transportation Planning
- Long Term Liabilities
- Other Fund Balances
- Internal Service Funds
- Investment, Banking and Cash Management
- Short-Term and Long-Term Debt Financings
- **Conduit Debt**
- Interfund Loans

PROPOSED POLICY CHANGES AND HIGHLIGHTS

We are proposing one new policy and only minor revisions to update data references for the current fiscal year. We are planning a broader level review in fiscal year 2022.

New Policy Statement - Conduit Debt

Per State Statute (ORS 441.530 and ORS 352.795) the County is authorized to issue bonds or other debt obligations on behalf of non-profit organizations that provide Hospital Facilities and Higher Education Facilities. Hospital Facilities are defined as adult congregate facilities, behavioral treatment facilities, family safety facilities, and healthcare facilities. The County issues debt for hospital facilities through the County's Hospital Facilities Authority established in 1998. This new policy statement describes the authority, intent, and how the County will evaluate future conduit requests. Below is the criteria being proposed:

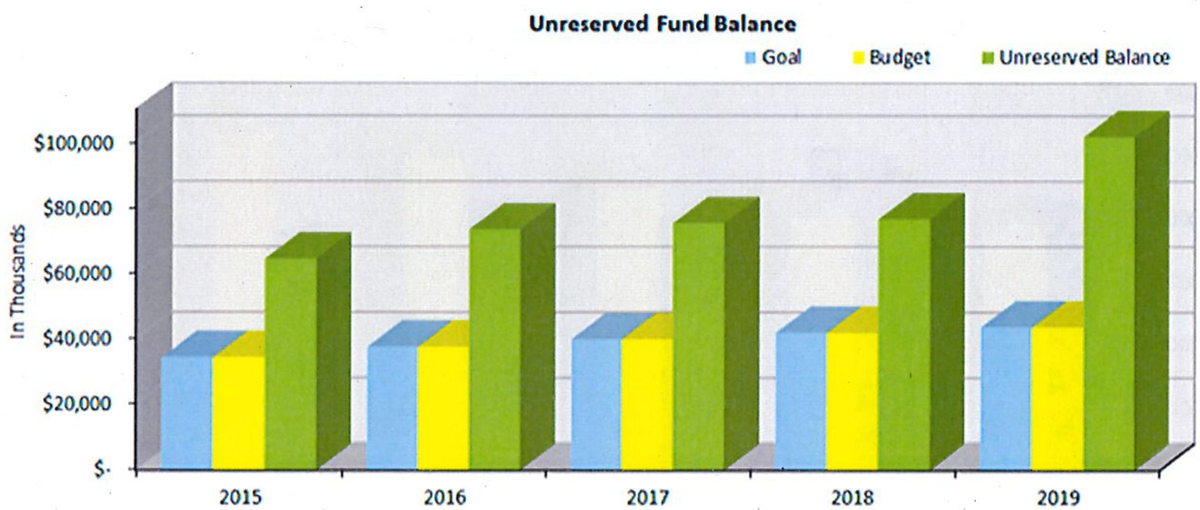
- Borrower must submit a letter of intent describing the request, purpose, benefit to community, and describe how request aligns with Multnomah County's mission and values
- Borrower facilities must reside in County and directly benefit County residents
- Borrower must be a non-profit entity
- A Pro Forma and 3 years of audited financial statements must be provided
- Chief Financial Officer will complete a financial position review. Projected revenues from borrower can be expected to cover cost of borrowing
- Request must be in alignment with state statutes
- A board briefing is required in which borrower will present in coordination with Chief Financial Officer

Conduit debt is not a direct or contingent liability of Multnomah County, the liability is directly with the borrower. Conduit debt does not count against the County's statutory debt capacity. Conduit debt is disclosed in the notes of Comprehensive Annual Financial Report (CAFR). As of June 30th 2019 total conduit debt outstanding was $221 million of which 98% was on behalf of hospital facilities.

Policy Highlights – Fiscal year 2021

Tax Revenues – on March 19th 2019 the Board approved an increase to Business Income Tax rate from 1.45% to 2.00% beginning with tax year 2020. The change also increases the gross receipts exemption from $50,000 to $100,000 and Owner Compensation Allowance from $108,000 to $127,000 beginning tax year 2020. Prior to COVID-19 impacts the tax rate change net of exemptions and allowance changes was estimated to net $30.5 million in addition revenue.

Budgeted General Fund Reserves – it is the goal of the board to fund and maintain a general fund budgeted reserves at 10% of corporate general fund revenues (property tax, business income tax, motor vehicle rental tax, state revenue sharing, and interest earnings). The graph below depicts the reserve goal, actual budgeted reserve, and actual unreserved general fund balance at fiscal year end. These strong financial practices protect the County in times of economic downturns, as we are experiencing with COVID-19.



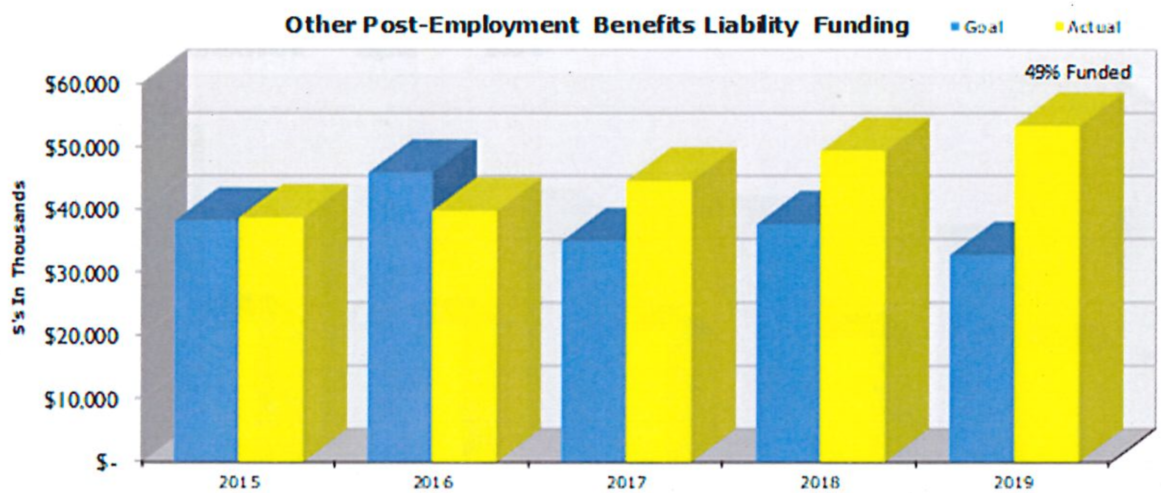
General Fund Reserves	2015	2016	2017	2018	2019
Goal	$ 34,322	$ 37,529	$ 39,855	$ 41,865	$ 43,536
Budget	$ 34,322	$ 37,529	$ 39,855	$ 41,865	$ 43,536
Unreserved Balance	$ 64,345	$ 73,348	$ 75,283	$ 76,553	$ 101,640

Long Term Liabilities – In fiscal year 2017 the board set the goal to establish four side accounts with Oregon PERS. The County would fund $25 million annually until reaching the goal of $100 million. The creation of side accounts allows the County to more effectively mitigate anticipated increases in PERS rates. Funds in side account are invested by PERS and earn the same rate of return as the overall PERS portfolio. In November 2019 the County met its goal and funded the fourth side account.

The County participated in the Oregon PERS Employer Incentive Fund (EIF) match program established by Senate Bill 1049. The EIF provides a 25% match on qualifying side accounts made after June 2nd 2018. The County received full match on one side account and a partial match on a second side account. This incentive match reflects good financial planning and strategy by County.

As of latest actuarial valuation on December 31st 2018, the County's Pension Liability (UAL) was $689.9 million.

The County's Post-Employment Benefits program (OPEB) that provides contracted retiree healthcare benefits has an incurred liability. As of the latest actuarial valuation dated January 1st 2019 the OPEB liability was $109 million. The board set the goal to fund the liability at 30% by the end of fiscal year 2018. The liability is currently funded at 49%. The graph below depicts the progress over the last five years.



		2015		2016		2017		2018		2019
Goal	$	38,156	$	45,787	$	34,953	$	37,642	$	32,775
Actual	$	38,663	$	39,726	$	44,496	$	49,249	$	53,256

I plan to brief the board in FY 2021 on the latest OPEB actuarial valuation and provide recommendations on future funding structures for liability.

FUTURE POLICY ANALYSIS/DEVELOPMENT

The Financial and Budget policies are reviewed annually to ensure our financial practices stay current, align with the board's long term direction, incorporate changes to external requirements/regulations, and reflect what ratings agencies want to see when evaluating the financial health of our organization. Below are topics for future review:

- Capital and Infrastructure Development
- GASB Pronouncements
- Recovery of Indirect Costs
- Internal Service Fund reserve balance thresholds
- CARES Act – Federal Guidance

OTHER FINANCIAL MANAGEMENT TOOLS

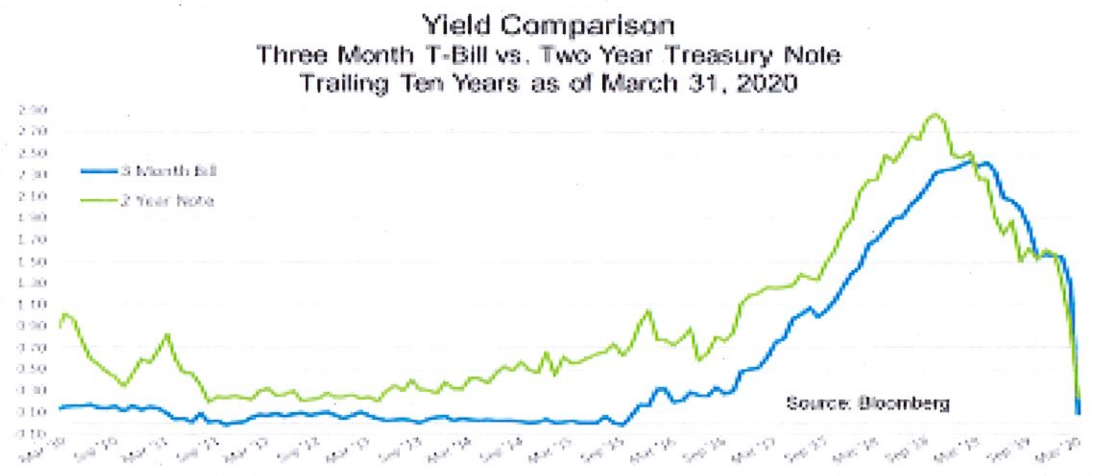
Below are other tools the County uses to maintain good and sounds financial practices

- Debt Manual
- Grants Management Manual
- Procedures
  - Facilities Procedures (FAC's)
  - Financial Procedures (FIN's)
  - Procurement Procedures (PUR's)
  - Risk Management (RSK's)
- Business Process Internal Controls
- Audit Recommendations
  - External Audits (financial statement, internal controls, IT systems, and federal expenditures)
  - Internal Audits (central and departmental processes)
- Governmental Accounting Standard Board (GASB) Pronouncements
  - Could lead to development of new policies

INVESTMENT POLICY

MARKET UPDATE AND GENERAL OVERVIEW

Market yields have plummeted in the first quarter of 2020 in response to the economic fallout of COVID-19. The 2 year treasury closed at 0.25% (1.57% at 12/31/19), 10 year treasury closed at 0.67% (1.92% at 12/31/19), and 3 month treasury closed at 0.06% (1.54% at 12/31/19). Yield markets are now adjusting to the massive federal stimulus program (CARES Act). Below is a 10 year yield comparison between 3 month and 2 year treasury. The pace of the drop has been unprecedented



Market yields are expected to recover in the coming quarters but at a very modest rate, nowhere near yields prior to COVID-19. Below is an economic projection on yields over the next four quarters

Economist Survey Projections for Rates

	Q2-20	Q3-20	Q4-20	Q1-21
Fed Funds	0.35	0.40	0.45	0.55
2 Year	0.40	0.53	0.62	0.70
10 year	0.73	0.94	1.10	1.23

In the short term the County's investment portfolio has not been impacted by the dramatic yield drops. The County completes the majority of its security purchases during property tax season (October-December) and strategically plans maturities to meet County expenditures obligations (e.g. debt service, payroll, PERS, etc.) throughout the fiscal year.

For the month of March the County's Investment Portfolio annualized earnings rate was 2.11% and year to date return was 2.17%. We do anticipate in the coming quarters our portfolio yields will drop as higher yield securities mature and we reinvest.

The County's investment program is operated in conformity with State Statute (ORS 294 and 295) and applicable federal laws. Investment funds are handled with highest public trust, in manner that assures security of principal. Cash assets are managed and invested with three primary objectives (in order of priority):

1. **Safety of Principal** – preservation of capital
2. **Liquidity** – portfolio is sufficiently liquid to meet its anticipated operational obligations
3. **Yield and Return** – attain a healthy market rate of return (exceeding portfolio benchmarks)

The County manages its investment portfolio in two separate funds, Core Fund and Liquidity Fund. The Core Fund ($260 million) incorporates fund balance which exceeds the County's current (fiscal year) liquidity needs. Core funds are generally invested longer than one year on the yield curve to diversity portfolio and earn higher yields. The Liquidity Fund represents funds necessary to meet annual budgeted obligations (e.g. debt service, payroll, etc). The County's portfolio has maturity constraints to ensure sufficient liquidity is available to meet planned and unexpected obligations. See below for specific policy constraints.

Maturity Constraints	Minimum % of Total Portfolio
Under 30 days	10%
Under 1 year	35%
Under 5 years	100%
Weighted Average Maturity	2 Years

The County is restricted on the types of securities it can hold by state statute and investment policy. The investment parameters set restrictions on holding types, maximum holding by type, maximum holding per issuer, and security rating requirements (e.g. corporate bonds must be rated AA- by S&P or Aa3 by Moody's). These parameters help ensure safety of principal, supports diversification, and mitigates credit exposure. The County cannot hold equities (stocks) per statute, fossil fuel corporate bonds, and Walmart bonds as they do not match the values of Multnomah County. The next page lists portfolio holdings by security type as of March 31st 2020.

Investment Type	Book Value	Percentage
Bank Deposits	1,618,194	0%
Money Market Accounts	24,824,070	4%
LGIP	50,680,581	9%
Certificate of Deposit	6,960,000	1%
Coporate Notes (Bonds)	56,386,254	10%
Commerical Paper	9,938,000	2%
US Treasury	184,994,846	32%
US Agency	222,951,470	38%
Municipal Bonds	21,132,141	4%
Total	579,485,557	100%

PROPOSED POLICY CHANGES:

Local governments investing in securities with maturities longer than 18 months are required to adopt investment policy annually per ORS 294.135(a). We are proposing three minor policy changes for FY 2021. The recommended changes do not materially change the risk in the portfolio but provide clarity and procedure regarding certain processes.

- **Update rating requirements language for allowable investments, specifically Corporate Bonds, Municipal Bonds, US Agency obligations, and Commercial Paper.**

Our current policy requires securities listed above to have a minimum credit rating through S&P or Moody's. The proposed language change aims to align our policy with state statues by expanding our rating agency reference.

Proposed Language: Specific issues must be rated by S&P or Moody's *or equivalent rating by any nationally recognized statistical rating organization*.

- **Increase US Agency primary issuer allocation to 40% per issuer agencies**
- **Increase Municipal Bonds maximum holdings to 25% to provide for added diversification**

Though interest rates are at an all-time low spreads on US Agencies and Municipal Bonds are at a decade high. We are proposing increasing the maximum holding per issuer for US Agencies from 25% to 40% and increasing maximum holding for Municipal Bonds from 10% to 25%. These allocation changes will allow for more investment opportunities in high quality securities. Per policy the County can only invest in Municipal Bonds within Oregon, California, Idaho, and Washington. All other changes to policy are cosmetic.