



BOARD OF SUPERVISORS
AGENDA LETTER

Agenda Number:

Clerk of the Board of Supervisors
105 E. Anapamu Street, Suite 407
Santa Barbara, CA 93101
(805) 568-2240

Department Name: Auditor-Controller
Department No.: 061
For Agenda Of: December 13, 2016
Placement: Administrative
Estimated Tme:
Continued Item: No
If Yes, date from:
Vote Required: Majority

TO: Board of Supervisors

FROM: Department Theodore A. Fallati, CPA, CPFO, Auditor-Controller
Director(s)
Contact Info: Betsy Schaffer, CPA, CPFO, Asst. Auditor-Controller

SUBJECT: Fund Balance Policy Amendment

County Counsel Concurrence

As to form: N/A

Auditor-Controller Concurrence

As to form: Yes

Other Concurrence:

Recommended Actions:

That the Board of Supervisors:

- a) Adopt an amended comprehensive fund balance policy for the County of Santa Barbara to effect implementation of changes to the provisions of the Enterprise Funds portion of the policy, and
- b) Determine that pursuant to California Environmental Quality Act (CEQA) Guidelines Section 15378(b)(5) that the above action is a governmental administrative activity which does not involve any commitment to a specific project which may result in a potentially significant physical impact on the environment, and therefore is not a project subject to environmental review.

Summary Text:

The proposed amendment adjusts the size of the general operating reserve of the County's Enterprise Funds, eliminates the requirement for a post closure retained earnings account and allows for the addition of any restricted retained earnings accounts that are required by bond or debt instruments issued by the Enterprise Funds.

Background:

The County maintains certain financial and budgeting policies to promote sound financial management. These policies require occasional updates and modification in order to remain current and meet the

needs of the organization while complying with accounting standards, the needs of the organization and best practices. This policy was last updated and approved by your Board in June of 2011.

As a result of a proposed debt financing of the Tajiguas Resource Recovery Project, certain fund balance requirements for the Resource Recovery and Waste Management Fund are required by the financing documents. Specifically, a general operating retained earnings account that, at a minimum covers 180 days of operating expenses of the fund. Additionally, a Bond Holders Rate Stabilization restricted retained earnings account of \$5,000,000 is required. The post closure account that was intended to fund a new facility or alternative technology is being eliminated because the post closure account is recorded as a fund liability and not a reserve or retained earnings.

This amendment will allow the Enterprise Funds to establish any retained earnings accounts required in future financing documents as necessary.

Fiscal and Facilities Impacts:

The amount of fund balance will not be any different with this amendment, but required accounts will be established and segregated from other retained earnings of the Enterprise Funds.

Attachments:

Attachment A: Comprehensive Fund Balance Policy for the County of Santa Barbara (untracked/final)
Attachment B: Comprehensive Fund Balance Policy for the County of Santa Barbara (changes tracked)

Authored by:

Betsy Schaffer, Assistant Auditor-Controller

Comprehensive Fund Balance Policy **For the County of Santa Barbara**

The County's fund balance policy establishes a minimum level at which unrestricted fund balance is to be maintained.

The County believes that sound financial management principles require that sufficient funds be retained by the County to provide a stable financial base at all times. To retain this stable financial base, the County needs to maintain unrestricted fund balance in its county funds sufficient to fund cash flows of the County and to provide financial reserves for unanticipated expenditures and/or revenue shortfalls of an emergency nature.

The purpose of the County's fund balance policy is to "maintain a prudent level of financial resources to protect against reducing service levels or raising taxes and fees because of temporary revenue shortfalls or unpredicted one-time expenditures" (recommended Practice 4.1 of the National Advisory Council on State and Local Budgeting).

Appropriate Level of Unrestricted Fund Balance in the General Fund

The County hereby adopts a policy to achieve and maintain unrestricted fund balance in the General Fund of 15% of operating revenue (approximately 60 days working capital) at the close of each fiscal cycle, consistent with the recommended level promulgated by the Government Finance Officers Association (GFOA). All committed, assigned and unassigned fund balance in the General Fund is considered unrestricted.

Fund Balance in the Special Revenue Funds

Special revenue funds are created to account for the proceeds of specific revenue sources that are legally restricted to expenditure for specified purposes. Only nonspendable and restricted fund balance should be maintained within the special revenue funds.

Appropriations of General Fund contributions to the special revenue funds should be maintained in the General Fund. Transfers of general fund contributions should be made on a reimbursement basis for qualified expenditures. To the extent that special revenue fund balances are sufficient to support annual operations, appropriated General Fund contributions should not be utilized and should lapse at the end of the fiscal year.

Debt Service Funds

Debt service funds contain specific debt reserve amounts that are subject to the requirements set forth by the ordinances or resolutions that authorize the issuance of debt. It is the County's policy that debt reserve requirements for any outstanding debt issue will be consistent with the ordinance or resolution authorizing the issuance of debt.

Capital Projects Fund

Capital Projects Funds account for resources accumulated to construct or acquire general capital assets and major improvements (capital maintenance activities/projects are accounted for in the General Fund or an appropriate Special Revenue Fund and not in a Capital Projects Fund). Capital projects may extend beyond a single fiscal year. The County's policy is that the fund should maintain, at a minimum, a fiscal year end fund balance plus estimated revenues sufficient to meet the outstanding projects for the upcoming fiscal year.

Residual project proceeds are bound by the same conditions and restrictions as the original funding source. If there are no restrictions on residual project proceeds it is the County's policy to return the residual proceeds to the appropriate operating fund.

Enterprise Funds

Generally, Enterprise Funds are used when services are provided to external users for goods and services. The majority of the fund's revenues are fee generated and are maintained to meet the following objectives:

1. Ensure adequate funding for operations;
2. Ensure adequate funding for infrastructure repair and replacement; and
3. Provide working capital to absorb rate fluctuations and provide stable rates to customers.

Enterprise Funds must be operated and managed as an ongoing business entity and therefore the focus is on long term sustainability using the economic resources measurement focus and the full accrual basis of accounting. Accordingly, Enterprise Funds will have revenues (customer charges, interest income, and all other income) sufficient to meet all cash operating expenses, depreciation expense, and prescribed cash reserves per financial policies unique to each enterprise activity. The following policies regarding reserving fund equity are intended to meet the above objectives:

1. Enterprise Fund Reserved Retained Earnings accounts for capital replacement and investment in capital assets will be funded and maintained as necessary for the operation of the specific Enterprise Fund. These accounts and their funding will be reviewed either annually or bi-annually during the budget process.
2. Each Enterprise Fund should maintain working capital to provide sufficient resources in order to allow the Board to react and adopt a financial plan which can adequately deal with a variety of short-term adverse economic circumstances which may materialize. A common "general operating" reserve for Enterprise Funds should be 180 days of operating expenses.

3. Enterprise Funds should maintain a Retained Earnings Contingency account which will support operations during times of financial emergencies. The amount of the contingency will be determined based on a risk assessment of each Enterprise Fund including funding status of other Retained Earnings accounts.
4. Enterprise Funds will establish restricted reserve accounts as required by covenants in financing documents necessary for the issuance of new debt.
5. The Laguna Sanitation District shall establish a Retained Earnings account for capital expansion that will provide for the expenses associated with expanding the capacity of the plant facilities due to new or additional growth, upgrades and major rehabilitations. Funding will be collected from new and existing development via connection fees.

Internal Service Funds

The County of Santa Barbara operates in accordance with OMB Circular A-87 regarding working capital balances. Internal service funds are dependent upon a reasonable level of working capital to operate from one billing cycle to the next. Charges by an internal service activity to provide for the establishment and maintenance of a reasonable level of working capital reserve, in addition to the full recovery of costs, are allowable. A working capital reserve as part of retained earnings of up to 60 days cash expenses for normal operating purposes is considered reasonable. A working capital reserve exceeding 60 days may be approved by the cognizant Federal agency in exceptional cases.

Circumstances in Which Unrestricted Fund Balance Can Be “Spent Down”

Unrestricted fund balance includes committed, assigned and unassigned fund balance. Committed and assigned fund balances indicate amounts set aside by the Board of Supervisors for specific purposes. Committed and assigned fund balances shall be spent for the approved purpose but may be redirected by majority approval of the Board of Supervisors according to the requirements of the County Budget Act.

In the event that the County has a positive unassigned fund balance, the excess may be utilized for any lawful purpose approved by the Board of Supervisors. It is recommended that first priority shall be to set aside sufficient resources in the committed Strategic Reserve fund balance to provide 30 days working capital consistent with the County’s Strategic Reserve Policy.

Year-end Fund Balances

If a portion of existing fund balance is included as a budgetary resource in the subsequent year's budget to eliminate a projected excess of expenditures over expected revenues, then that portion of fund balance should be classified as assigned. The assignment automatically releases with the loading of the budget and expires with the appropriation. If the expected excess does not occur, a budget correction is required from the affected department.

Excess fund balance remaining over and above the projected budgeted excess of expenditures over expected revenues should be classified as "unassigned" in the General Fund and "Restricted for Purpose of Fund" in Special Revenue Funds.

Replenishment

Should the unrestricted fund balance fall below the 15% targeted level, the Board shall approve and adopt a plan to restore this balance to the target level within 24 months. If restoration of unrestricted fund balance cannot be accomplished within such period without severe hardship to the County, then the Board will establish a different time period.

Strategic Reserve Policy

There shall be established a separate committed fund balance account known as the County's Strategic Reserve.

The Board shall approve the establishment of a Strategic Reserve with the intent of limiting the use of Strategic Reserve funds for the purposes set forth herein. The initial funding level shall be equivalent to the amount set aside in the County's Strategic Reserve designation at the date of GASB 54 implementation.

The target funding level for the committed Strategic Reserve fund balance shall be an amount equivalent to 8% of operating revenue (approximately 30 days working capital) for the General Fund. Funding for the Strategic Reserve shall be appropriated annually by the Board of Supervisors as part of the budget approval process.

The purpose of the County's Strategic Reserve is to:

1. Mitigate economic downturns that reduce County general revenue;
2. Mitigate State or Federal budget actions that may reduce County revenue;
3. Maintain core service levels essential to public health, safety, and welfare;
4. Front-fund or completely fund, if necessary, disaster costs or costs associated with emergencies. Only those events that have been legally declared to be a disaster at the local, state or federal level are eligible for funding from the Strategic Reserve; and
5. Absorb liability settlements in excess of available resources in the County's litigation designation.

The monies in the Strategic Reserve are separate monies to be used only for the purposes stated above. The Strategic Reserve should only be used to support the operating budget when general revenue increases less than 3% from the prior fiscal year.

Any transfer of funds shall be approved by the Board of Supervisors and shall not exceed the amount sufficient to balance the General Fund. Transfers shall require approval by 3/5 vote during budget hearings and 4/5 vote at all other times during the fiscal year in accordance with the County Budget Act.

Monitoring and Reporting

The Auditor-Controller shall annually prepare a report documenting the status of the fund balance with this policy and present to the Board in conjunction with the presentation of the County's annual financial statements.

Review

The County's Fund Balance Policy shall be reviewed annually, within the context of long-term forecasting, to evaluate sufficiency of the adopted level of fund balance.