



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: CEO and Auditor
Department No.: 012 & 061
For Agenda Of: June 5, 2007
Placement: Set Hearing
Estimated Tme: 15 Minutes on 6/26/7
Continued Item: No
If Yes, date from:
Vote Required: Majority

TO: Board of Supervisors
FROM: Department Michael F. Brown, County Executive Officer
Director(s) Robert W. Geis, CPA CPFO, Auditor-Controller
Contact Info: Ken Masuda, Assistant County Executive Officer (568-3411)
Theo Fallati, CPA CPFO, Assistant Auditor-Controller (568-2102)
SUBJECT: Enterprise Fund Reserve Policy

County Counsel Concurrence

As to form: N/A

Auditor-Controller Concurrence

As to form: N/A

Other Concurrence: N/A

As to form:

Recommended Actions:

Set a hearing on Tuesday, June 26, 2007 for 15 minutes to consider a recommendation to adopt an Enterprise Fund Reserve Policy.

Summary Text:

Enterprise Funds are used to account for a government's business-type activities where a given fund provides services primarily to customers outside the financial reporting entity, such as citizens and ratepayers. Generally Accepted Accounting Principles (GAAP) mandate the use of an enterprise fund when management policy requires that the full cost of providing services (including capital costs) be recovered through fees and charges. The County has a full cost recovery policy and operates two significant enterprise funds, the Resource Recovery and Waste Management Fund and the Laguna County Sanitation District Fund.

General and Special Revenue Funds use the current financial resources measurement focus, and have the objective of operating using near-term inflows and outflows of financial or spendable resources. 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 like businesses in the private sector. Accordingly, Enterprise Funds will have revenues (customer charges, interest income, and all other income) sufficient to meet all cash operating expenses, debt service, non cash expenses such as depreciation expense, capital replacement and reserve funding to insure the long term sustainability of the business operation.

The purpose of Enterprise Fund Reserve Policy is to provide adequate reserve levels to meet the needs and criteria of an ongoing business operation. Adequate reserve levels are a necessary component of the County's overall financial management strategy and a key factor to external agencies' measurement of the County's financial strength, not only in these operational areas, but on an entity wide basis.

Background: Both of the County's significant enterprise funds have not had a reserve policy in place in the past and have operated in a manner more consistent with a special revenue fund, leaving the funds short on capital replacement reserves and requiring the issuance of debt for capital outlay. This policy will minimize the need for debt over time and minimize liabilities and in the future will provide funding towards one or a combination of:

- Replacement facilities
- Alternative technological processes to dispose of waste
- Fully funding landfill post closure costs should the pledge of revenue stream be reduced or eliminated.

The proposed Enterprise Funds Reserve Policies and Resource Recovery & Waste Management Long Range Fiscal Plan were originally going to be presented during the CEO and Auditor Controller's mid year report on 2/27/07; however, it was felt that this subject deserved a separate hearing and therefore was postponed to this hearing. The Board may wish to trail the adoption of this item until after the presentation of the Resource Recovery & Waste Management Long Range Fiscal Plan as it will include a combination of a financial forecast and proposed financial reserve policies, plus possible debt financing, all of which include revenue assumptions tied to actions by the Board of Supervisors.

Fiscal and Facilities Impacts:

Narrative:

There are no current fiscal and facilities impacts related to the adoption of the Enterprise Fund Reserve Policy however, there are long range fiscal impacts related to the level of application of these policies within the enterprise funds.

Attachments:

Enterprise Fund Reserve Policy

Authored by:

John Jayasinghe, CEO Administrative Analyst (568-2246) and
Mark Paul, CPFO, Auditor-Controller Division Chief (568-2141)

CC:

Mark Schleich, Assistant Public Works Director

Rochelle Camozzi, Public Works Chief Financial Officer

Colleen Hankins, Public Works Cost Analyst

County of Santa Barbara

Enterprise Fund Reserve Policy (Proposed)

Generally, Enterprise Funds are used when services are provided primarily to customers outside the County reporting entity and are maintained to meet the following objectives:

- a. Ensure adequate funding for operations;
- b. Ensure adequate funding for infrastructure repair and replacement; and;
- c. 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 Reserves such as **reserve for capital replacement**, and **reserve for investment in capital assets** will be funded and maintained as necessary and prudent for the operation of the specific Enterprise Fund. Such reserves and their funding will be reviewed either annually or bi-annually during the budget process.
2. Each Enterprise Fund should maintain a **reserve for working capital** to provide enough funds 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 standard for Enterprise Fund operations ranges anywhere from 30 to 90 days of operating expenses.
3. Enterprise Funds should maintain a **reserve for contingency** which will support operations during times of financial emergencies. The amount of the contingency reserve will be determined based on a risk assessment of each Enterprise Fund including funding status of other reserves.
4. The Resource Recovery and Waste Management Fund should establish a **reserve for post closure** that, at the end of the useful life of the Tajiguas Landfill, will provide funding towards one or a combination of:
 - a) A replacement facility,
 - b) An alternative technological process to dispose of waste currently being buried at the landfill, or
 - c) Fully funding landfill post closure costs should the pledge of revenue stream be reduced or eliminated.
5. The Laguna Sanitation District shall establish a **reserve 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.

Glossary of Enterprise Fund Retained Earnings Reserves

Reserve for Capital Replacement – This reserve accumulates dollars collected for depreciation expense and is to be used for replacement of fixed assets at the end of their useful lives. Only assets intended to be replaced as part of an asset replacement plan should be reserved for.

Reserve for Investment In Capital Assets – This reserve accounts for the current investment in fixed assets net of associated debt (i.e. fixed asset costs less accumulated depreciation less associated debt). This reserve segregates the portion of retained earnings that is invested in net assets and is not available for appropriations.

Reserve for Working Capital – This reserve is established to allow the fund to weather short-term adverse economic circumstances only.

Reserve for Contingency – This reserve is restricted for use during times of financial emergencies.

Reserve for Post Closure – This reserve accounts for dollars collected from current landfill users to fund post closure monitoring/maintenance costs and to eliminate the pledge of future post closure revenue that may not materialize.

Reserve for Capital Expansion – This reserve funds facility expansions, upgrades or major rehabilitations and is collected from new and existing development connection fees.