



# **Reserve Policies: General Fund and Internal Service Funds**

**City Council Meeting  
March 19, 2013**





# Overview

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- ▶ Updated General Fund and Internal Service Fund reserve policies
  - ▶ More comprehensive
  - ▶ Increased sophistication
  - ▶ Greater financial control
  - ▶ Modernized



# Why Update?

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- ▶ **Current policy very basic:**
  - ▶ *The City will establish an undesignated General Fund Reserve goal based on 100% of the City's General Fund yearly operating expenditures. Any excess funds in the General Fund reserve should not be used to replace ongoing General Fund operating expenditures, new programs, or salary and benefits. Funds should only be allocated to projects that are one-time expenditures, capital in nature, and/or to replace the City's equipment, buildings and infrastructure.*
- ▶ **Has been this way since FY 2009-10**



# Why Update?

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- ▶ Current policy lacks comprehensiveness and sophistication
- ▶ Updated version moves beyond simple percentage statement/goal
- ▶ Covers Internal Service Funds (five) as well as General Fund
- ▶ Utilizes GASB 54 classifications to fuller extent



# Best Practices

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- ▶ GFOA recommends General Fund reserves of 5% to 15% (of either revenue or expenditures)
- ▶ Most California agencies in 15% to 20% range
  - ▶ Twenty-Nine Palms and Mission Viejo: 50%
  - ▶ La Habra Heights: 100%
  - ▶ Difficult to find other agencies at or near 100% level...
- ▶ Best practices involve more than just a dollar or percentage goal...



# Best Practices

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- ▶ **Well-crafted policies do several things:**
  - ▶ Outline a goal amount (dollar or percentage)
  - ▶ Provide guidance as to when certain reserves can and should be used
  - ▶ Provide guidance on how to replenish reserves (if and when used)
  - ▶ Fully incorporate GASB 54
- ▶ **Ultimately...**
  - ▶ Policy should help guide decisions, not constrain them...



# Recommended Policies: Intent

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- ▶ Set reasonable and sustainable levels for General Fund reserves
- ▶ Fully utilize the power of GASB 54 reserve classifications
- ▶ Establish guidelines and conditions for when General Fund reserve can and should be utilized
- ▶ Establish guidelines for returning General Fund reserves to prescribed levels if utilized
- ▶ Set reasonable and sustainable reserve levels for each of the five Internal Service Funds
- ▶ Provide information to City Council and Staff to inform decisions regardless of economic situation



# What's New?

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- ▶ General Fund reserve policies:
  - ▶ Creates **“Economic Uncertainties Reserve:”**
    - ▶ Equal to 60% of General Fund expenditures
    - ▶ Established by City Council resolution as part of annual budget adoption
  - ▶ Creates **“Capital Projects Reserve:”**
    - ▶ Equal to 40% of General Fund expenditures





# What's New?

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- ▶ **General Fund reserve policies:**
  - ▶ Establishes general reasons for using each reserve
  - ▶ Establishes method for replenishing reserves if they drop below established goal levels (i.e., 60% or 40%)
  - ▶ Creates guidelines for utilizing excess General Fund reserves beyond the 60% Economic Uncertainties Commitment and 40% Capital Projects Assignment
    - ▶ i.e., use of funds in excess of 100% of General Fund expenditures



# What Would New Policy Look Like?

**General Fund Reserves (Projected) at 06/30/2013:  
Current Policy of 100%**

Nonspendable	643,508
<b>Restricted</b>	
<b>Committed</b>	
<b>Assigned</b>	4,541,983
<b>Unassigned</b>	9,289,212
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	<b>14,474,703</b>
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<b>Spendable (Net Nonspendable)</b>	<b>13,831,195</b>
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GF FY 2012-13 Projected Revenue	9,648,405
GF FY 2012-13 Projected Expenditures*	(9,099,400)
Transfer to COR	(1,700,000)
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Add To / (Use Of) Reserves	(1,150,995)
<b>Projected GF Fund Balance 06/30/2013</b>	<b>12,680,200</b>
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<b>"Surplus" FB over 100%</b>	<b>3,580,800</b>
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# What Would New Policy Look Like?

**General Fund Reserves (Projected) at 06/30/2013:  
Recommended (Updated) Reserve Policies**

Nonspendable 643,508

**Restricted -**

**Committed (Economic Uncertainty Reserve, 60%) 5,459,640**

**Assigned (Infrastructure/Capital Projects, 40%) 3,639,760**

Unassigned (Excess of 100% / Available) 3,580,800

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**Restricted + Committed + Assigned 9,099,400**

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**Total 12,680,200**

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# What Does It Mean?

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## ▶ **Committed Reserve:**

- ▶ Established via resolution
- ▶ Can only be used for reason(s) stated in resolution
- ▶ Created for “Economic Uncertainties” (i.e., “emergencies”)
  - ▶ Reduction in revenue equal to or greater than 20% of adopted General Fund appropriations
  - ▶ Natural disaster
  - ▶ Unfunded/unplanned State or Federal actions/mandates
  - ▶ Any other unplanned event causing expenditures in excess of 10% of adopted appropriations
- ▶ Equal to approximately 7 months of operating expenditures (using FY 2012-13 amended budget amount)



# What Does It Mean?

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## ▶ **Assigned Reserve:**

- ▶ Intended for un-programmed and/or unfunded capital and infrastructure projects
  - ▶ Major emergency/unexpected repairs to City assets (streets, facilities, etc.)
  - ▶ Could be utilized per City Council direction for unfunded capital projects



# What Does It Mean?

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## ▶ **Unassigned:**

- ▶ Amounts in excess of Economic Uncertainties (60%) Commitment + Capital Projects (40%) Assignment
  - ▶ No specific restrictions
  - ▶ Can be appropriated via City Council action
    - OPEB trust?
    - Energy projects?



# Replenishment

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- ▶ If you use it, put it back...
- ▶ Reserve policy includes replenishment clause:
  - ▶ If either Commitment or Assigned reserves fall below policy levels...
    - ▶ City Council develops plan to replenish to policy levels within one to three years



# What's New (Internal Service Funds)?

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- ▶ **Internal Service Fund reserve policies:**
  - ▶ Establishes for the first time individual fund balance levels for each of the five Internal Service Funds
  - ▶ Creates guidelines for annually calculating fund balance for each fund, based on criteria unique to each fund
  - ▶ Provides a process for adjusting annual cost allocations in order to maintain the reserve policy levels
- ▶ **Each of the five funds has own reserve level metric....**





## Updated Fund Balance Estimates

- ▶ Internal Service Fund projected fund balances updated as part of FY 2013-14 budget planning:
  - ▶ Updated projections include revised FY 2012-13 expenditure estimates
  - ▶ Utilized FY 2011-12 audited fund balances
    - ▶ All funds ended FY 2011-12 with larger fund balances than shown in FY 2012-13 adopted budget
    - ▶ Flows through to FY 2013-14....



# Insurance

- ▶ **Insurance Reserve Level:**
  - ▶ Equal to 3X annual insurance expenses of immediately preceding fiscal year
    - ▶ Allows sufficient funding for ongoing operations + contingency

FY 2012-13 INSURANCE PREMIUM ESTIMATE	308,300		
3X ANNUAL INSURANCE EXPENSES	924,900		
<b>TOTAL SUGGESTED FB</b>		<b>1,000,000</b>	
		1,001,583	<= 06/30/2013 Projected Fund Balance
		<b>1,583</b>	<b>&lt;= EXCESS / (DEFICIT) from 06/30/2013 Projected Fund Balance</b>



# Employee Benefits

- ▶ **Employee Benefits Reserve Level:**
  - ▶ Equal to total amount of compensated absences, as noted in CAFR “Statement of Net Assets”
    - ▶ Allows for one “unfunded liability” to be planned for/covered
    - ▶ Unlikely full amount would come due at once, but...

COMPENSATED ABSENCES DUE WITHIN ONE YEAR	144,738		
COMPENSATED ABSENCES DUE BEYOND ONE YEAR	434,213		
<b>TOTAL SUGGESTED FB 580,000</b>		864,315	<= 06/30/2013 Projected Fund Balance
		284,315	<= <b>EXCESS / (DEFICIT)</b> from 06/30/2013 Projected Fund Balance



# Facilities Maintenance

## ▶ Facilities Maintenance Reserve Level:

- ▶ Equal to rolling six-year average of actual Maintenance and Operations expenses (updated annually)
- ▶ Plus contingency amount equal to 1/2 the rolling six-year operating amount

	FY 2006-07	316,134		
	FY 2007-08	287,002		
	FY 2008-09	368,775		
	FY 2009-10	338,840		
	FY 2010-11	280,495		
	FY 2011-12	338,720		
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6 YR AVERAGE EXPENDITURES	(ACTUALS)	321,661		
	CONTINGENCY AMOUNT	178,339		
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	<b>TOTAL SUGGESTED FB</b>	<b>500,000</b>	953,292	<= 06/30/2013 Projected Fund Balance
				<= <b>EXCESS / (DEFICIT)</b> from 06/30/2013
			<b>453,292</b>	<b>Projected Fund Balance</b>



# Vehicle Maintenance & Replacement

- ▶ **Vehicle Maintenance and Replacement Reserve Level:**
  - ▶ Equal to 1/3 of replacement value of all rolling stock
    - ▶ Allows more than enough in case of catastrophic or other unplanned replacement need

ESTIMATED  
REPLACEMENT VALUE OF  
VEHICLES 2,065,500

1/3 OF REPLACEMENT  
VALUE 688,500

<b>TOTAL SUGGESTED FB</b>	<b>689,000</b>
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697,761

<= 06/30/2013 Projected Fund  
Balance

<= EXCESS / (DEFICIT) from  
**8,761** 06/30/2013 Projected Fund Balance



# Technology Maintenance & Replacement

- ▶ **Technology Maintenance and Replacement Reserve Level:**
  - ▶ Equal to full replacement value of City's entire technology network (as determined annually)
    - ▶ Allows sufficient funding for necessary, periodic upgrades
    - ▶ Contingency amount

FY 13-14 EST CITYWIDE NETWORK  
REPLACE VALUE 394,300

<b>TOTAL SUGGESTED FB</b>	<b>390,000</b>	451,200	<= 06/30/2013 Projected Fund Balance
		61,200	<= EXCESS / (DEFICIT) from 06/30/2013 Projected Fund Balance



# Internal Service Fund Reserves

- ▶ Recommended reserve levels robust
- ▶ Other agencies put aside (reserve) less:
  - ▶ Fresno County uses “60 days operating” as reserve level target
  - ▶ Newport Beach utilizes various levels:
    - ▶ Equipment (Vehicle) Maintenance: \$0 reserves
      - Strictly pay as you go
    - ▶ Compensated Absences: 50% of long-term liability



# One-time Use of Reserves

- ▶ FY 2013-14 proposed budget plan incorporates “one-time” uses of reserves
  - ▶ Some items could be funded with internal service fund reserves
    - ▶ OPEB trust: could use portion of Employee Benefits to help fund part of “start up” deposit
    - ▶ Energy projects: could use Facilities Maintenance to partially offset project costs
      - Use of reserves all depends on actual expenditures in FY 2012-13 and FY 2013-14
      - Potential for “excess” reserves exists...
- ▶ No intent to utilize internal service fund reserves for operating





# Next Steps...

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- ▶ **Recommended Reserve Policies will evolve**
  - ▶ Other funds can be discussed at future date to be covered by the policies:
    - ▶ Special revenue funds (Gas Tax, Measure M2, etc.)
    - ▶ Enterprise funds (Water and Sewer)
- ▶ **Discussion and questions...**
- ▶ **Approve resolution adopting updated reserve policies**



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