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**Sponsors:** James O'Leary

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Staff Report for Resolution Authorizing Transfers from General Fund Fund Balance to Self Insurance Fund and Economic Uncertainty Reserve

**RECOMMENDATION**

Staff recommends that the City Council approve the resolution authorizing transfers from the General Fund fund balance to the Economic Uncertainty reserve and to the Self Insurance Fund. The transfer to the Self Insurance Fund was administratively approved by the City Manager to facilitate the preparation of the City's 2010-11 financial statements. This transfer should be confirmed by City Council approval of the resolution. A separate transfer to the Economic Uncertainty reserve is also recommended by the Finance Committee.

**BACKGROUND**

The Finance Committee reviewed the 2010-11 Budget Review and Budget Amendment at its meeting on September 9, 2011. The report confirmed that the 2010-11 year-end forecast for the General Fund reflected a significant improvement over the adopted budget, largely due to an increase in projected revenues. Revised projections reflected an operating (revenue over expenditures) increase of \$2,356,200. The adopted budget had shown an operating deficit of (\$3,079,000). As a result of this improvement in the revenue and expenditure balance, the General Fund fund balance was similarly improved to about \$4,000,000.

The attached worksheet shows reserve funds totaling \$12,723,000 for General Fund reserve designations and \$308,000 for Self Insurance reserves. The Major Emergencies reserve totals \$5,000,000, a consistent amount since 2007-08. The Economic Uncertainty reserve amounted to \$10,033,000 in 2007-08 and has declined over the past three years to the current amount of \$3,796,500. The Major Emergencies and the Economic Uncertainty reserves are currently 13% of the General Fund operating expenditures.

The City Council initially established a philosophy for financial reserve funds over twenty years ago. In 1989-90, the City Council adopted a series of financial values that were utilized to develop the budget. The Financial Goals Statement identifies and formalizes the financial principles by which the organization is guided. The Statement provides direction for preparing annual budget strategies and budgets and for conducting the day-to-day and long-term municipal affairs.

Related to Fund Balance Designations and Reserves Management, the Financial Goals Statement spells out the following:

**C. Fund Balance Designations and Reserves Management**

1. *The City will maintain fund or working capital balances of at least 20% of operating expenditures in the General Fund and Enterprise Funds. This is considered the minimum level necessary to maintain the City's credit worthiness and to adequately provide for:*

- (i) Economic uncertainties, local disasters, and other financial hardships or downturns in the local or national economy.*
- (ii) Contingencies for unseen operating or capital needs.*
- (iii) Cash flow requirements.*

**DISCUSSION**

The General Fund finances the operations of the City that have no special or dedicated revenue sources and pays for all basic municipal operations. The General Fund reserve, based on City Council direction, sets aside savings for economic uncertainty, emergencies, and other future contingency. Reserves allow for the designation of funds received for the Kaiser Hospital development, Street Improvement Funds and Community Impact Fund, Plaza loan repayment, and Other Designations (including equipment acquisitions and encumbrances) on the worksheet.

Together, the Major Emergencies and Economic Uncertainty designations reflect the General Fund reserves set aside for future unplanned contingencies. The amount of the Major Emergencies reserve has remained unchanged during the recent years of depressed economics. The reserve has remained at \$5,000,000 since 2007-08. The Economic Uncertainty reserve, at \$10,033,000 in 2007-08, has since been partially utilized for operations over the past several years. The balance in the Economic Uncertainty is \$3,796,500. This amount reflects the June 30, 2011 unaudited balance and the 2011-12 budget was approved without any further draw-down of the reserve.

The Major Emergencies and the Economic Uncertainty reserves totaled \$15,033,000 in 2007-08, about 19% of the General Fund operating expenditures (\$77,397,000). The percentage has declined over the past several years and was recorded at 13% as of June 30, 2011. Staff recommends a transfer of \$2,000,000 from the General Funds fund balance to the Economic Uncertainty reserve. This transfer will bring the Major Emergency reserve and the

Economic Uncertainty reserve total to \$11,096,500, about 15% of the General Fund operating expenditures. This transfer moves the percentage significantly closer to the City Council's goal of 20%.

The Self Insurance Fund provides the City insurance protection against public liability cases and worker's compensation claims related to injuries to City employees. The Fund's balance sheet records the liability for Claims and Judgments for outstanding cases and claims. As of June 30, 2011, the total liability amounted to \$7,931,100. In addition, as noted on the reserve worksheet, the Self Insurance Fund fund balance was recorded at \$308,000.

The preliminary year-end close for the Self Insurance Fund reflected a fund balance deficit of (\$1,192,000). The deficit occurred as a result of significantly higher Fund expenditures in 2010-11. One unanticipated cost was that case reserves

for liability and workers' compensation increased by \$2,361,400. The City Manager authorized a transfer of \$1,500,000 from the General Fund fund balance to the Self Insurance Fund allowing the year-end financial statements to be prepared without a fund balance deficit.

Staff recommends that the City Council confirm this transfer and direct that this transfer be included in the budget amendment resolution to be presented to the City Council. It should be noted that \$3,000,000 has been transferred from the Self Insurance Fund to the General Fund since 2007-08 as a budget strategy to balance the General Fund.

**Current City Council Policy**

The City Council initially established a philosophy for financial reserve funds over twenty years ago. In 1989-90, the City Council adopted a series of financial values that were utilized to develop the budget. The Financial Goals Statement identifies and formalizes the financial principles by which the organization is guided.

**Previous City Council Action**

The City Council reviewed the 2010-11 Budget Review and Budget Amendment at its meeting on September 9, 2011. The report confirmed that the 2010-11 year-end forecast for the General Fund reflected a significant improvement over the adopted budget, largely due to an increase in projected revenues.

**City Council Committee Review and Action**

The Finance Committee reviewed and recommended this action at its meeting on October 21, 2011.

**Attachment**

Attachment 1, Fund Reserves Worksheet.

**CONCLUSION**

Staff recommends that the City Council approve the resolution authorizing transfers from the General Fund fund balance to the Economic Uncertainty reserve and to the Self Insurance Fund. The transfer to the Self Insurance Fund was administratively approved by the City Manager to facilitate the preparation of the City's 2010-11 financial statements. This transfer should be confirmed by City Council approval of the resolution. A separate transfer to the Economic Uncertainty reserve is also recommended by staff.

**PREPARED BY:** Jim O'Leary, Interim Finance Director, Finance