RESOLUTION NO. _________

A RESOLUTION OF THE COUNCIL OF THE CITY OF SANTA BARBARA ESTABLISHING POLICIES FOR RESERVES FOR THE CITYS GENERAL FUND, ENTERPRISE FUNDS AND INTERNAL SERVICE FUNDS, AND RESCINDING RESOLUTION NOS. 95-157 AND 99-066.

WHEREAS, the City desires to establish policies regarding reserves for the various City funds for the purpose of providing consistent designations for different categories of reserves, ensuring fiscal security for the funds, and defining standards for minimum and maximum amounts to be maintained in reserves;

WHEREAS, such reserves policies will be most readily communicated and understood if they are consolidated and formally adopted in a single document;

WHEREAS, the Council has considered the proposed reserves policies applicable to the General Fund and Internal Service Funds at a regular Council meeting on June 12, 2012; and

WHEREAS, the Council has not proposed changes to reserve policies applicable to Enterprise Funds, which are contained in Council Resolution Nos. 95-157 and 99-066, but are nonetheless incorporated into this policy document.

NOW, THEREFORE, BE IT RESOLVED BY THE COUNCIL OF THE CITY OF SANTA BARBARA THAT the following reserves policies are adopted:

SECTION 1: CALCULATION OF RESERVE AMOUNTS

Final reserve balances will be calculated at end of each fiscal year after the closing of the City’s accounting records. An amount will be established for each fund, as applicable, as a commitment of fund balance for each type of reserve established by this policy.

As soon as practical after the close of a fiscal year, staff will provide City Council a report showing the status of reserves as of June 30. At any time it is proposed to utilize reserves pursuant to this policy, staff will provide a similar report on reserves and projected fiscal impact from the proposed use of reserves.

SECTION 2: DISASTER RESERVES

The amount of the required Disaster Reserve is calculated based on 15% of the most recently adopted fiscal year operating budget.

The Disaster Reserve is restricted to use in addressing the financial impacts of natural disasters, such as floods, fires, tsunamis, earthquakes and any other event that results in significant damage to City facilities and infrastructure.

The use of Disaster Reserves should generally be limited to federal or state declared disasters. The use of Disaster Reserves is also allowable in cases where the natural disaster is less severe, such as a major fire to a City building that requires temporary facilities to be leased. Disaster reserves may be used only after other available funds are exhausted, including the Contingency Reserve.

Examples of financial impacts that would justify the use of Disaster Reserves include:

- Extraordinary costs incurred in connection with the immediate emergency response to address public safety matters.
- Revenue losses resulting from a significant decline or temporary halt in visitors to the City due to major damage to facilities, infrastructure and local businesses.
- Additional costs necessary to maintain City operations.
- Long term costs incurred to rebuild City facilities and infrastructure.

SECTION 3: CONTINGENCY RESERVES

The Contingency Reserve is calculated based on 10% of the most recently adopted fiscal year operating budget.

The purpose of the Contingency Reserve is to allow for the orderly implementation of a balancing strategy to address the fiscal impacts of unexpected events in order to minimize the impacts to the organization and community. The most common of these events would be an economic recession that results in a significant impact on key revenues such as sales, transient occupancy or property taxes.

Other unexpected events for which these reserves could be used include the following:

- Natural disasters, as described above for Disaster Reserves;
- Revenue impacts resulting from State of California actions or unfunded State mandates;
- Unexpected loss of external funding from sources such as grants or entitlements;
- An unplanned loss of, or damage to, a City facility such as the loss of a building due to fire;
- Mitigation of an emergency that poses a threat to public health and safety; and
- An adverse judicial action that requires large cash payments to third parties and is not covered by insurance.

The general intent of the Contingency Reserve is for unexpected events or situations. In general, its purpose is not to fund known or anticipated financial impacts, such as negotiated salary and benefit increases or scheduled increases to health insurance premiums or retirement costs.

SECTION 4: COUNCIL APPROVAL OF DISASTER AND CONTINGENCY RESERVES

Any use of the Disaster or Contingency reserves described in Sections 2 and 3 requires a majority vote of approval by the City Council.

When the use of reserves is recommended to the City Council by staff, the justification should include the following elements:

<u>An Assessment of the Fiscal Condition and Outlook:</u>

This assessment should include an objective evaluation of the operating fund's fiscal condition and an evaluation of the impacts of the event that triggered the need to use of reserves. The purpose of this evaluation is to measure and define the scope and duration of the problem to assist in developing an appropriate balancing strategy.

This assessment of fiscal condition should include the use of available and relevant financial and non-financial data, including economic and demographic indexes and trends; historical revenue and expenditures results; and local economic forecasts developed by recognized academic and financial institutions and paid consultants.

<u>Balancing Strategy</u>

The balancing strategy should include measures that minimize the use of Contingency Reserves, such as:

- Expenditure reductions achieved through efficiency measures, cuts to programs, services and staffing;
- Revenue enhancement measures that generate new or increased revenues;
- Use of existing one-time funds; and
- Use of available reserves in other funds, as allowable and appropriate.

The balancing strategy should also be consistent with the nature of the fiscal impact. For example, a one-time impact may be resolved fully with the use of reserves, depending on its severity. However, an event that has an ongoing financial impact, such as decline in revenues due to a major recession, will require a balancing strategy that includes ongoing budget adjustments to minimize the use of reserves.

Plan of Replenishment

The replenishment plan should include the following elements, as appropriate:

- A one-time (one-year) use of reserves should be accompanied by a specific plan for how and when the reserves will be restored.

- An extended use of reserves for more than one year should be accompanied by a long-term strategy that includes a more general plan for how the reserves will be restored.

SECTION 5: ENTERPRISE FUNDS

Enterprise Funds will be subject to the same Disaster and Contingency Reserve and approval requirements as described in Sections 2, 3 and 4 of this resolution.

In addition, each Enterprise Operating Fund will establish a Capital Reserve funded to at least 5% of the value of its capital assets. In the alternative, the amount may be established at an amount equal to the average of the adopted capital program budgets for the previous three years. Appropriations from these reserves will be to fund major capital costs.

For the Waterfront Enterprise Fund, the Capital Reserve requirement will be met through reserves accumulated in the Harbor Preservation Fund (HFP). Pursuant to Chapter 17.40 of the Santa Barbara Municipal Code, the HFP is required to maintain reserves of no less than $2 million for preservation, enhancement and management of Waterfront and State Tidelands Trust properties.

SECTION 6: RESERVE REQUIREMENTS FOR INTERNAL SERVICE FUNDS

Internal Service Funds are not subject to the reserve requirements for Disaster Reserves or Contingency Reserves. Instead, Internal Service Funds will maintain an operating reserve equal to 10% of the operating budget of the most recently adopted budget. This reserve will be available to address unexpected events and natural disasters that affect the operations and revenue streams of the Internal Service Funds.

Within the City budgetary structure there are a number of Internal Service Funds that are used to provide services to operating departments throughout the City. These Internal Service Funds include the following:

- Information Systems Fund
- Fleet Maintenance Fund
- Facilities Management Fund
- Self Insurance Fund

All of the Internal Service Funds listed above will be subject to the 10% reserve requirement, with the exception of the Self-Insurance Fund, which by design builds up assets for the payment of claims several years into the future. As a result, there should be adequate cash reserves to cover unanticipated costs. In addition, the reserve requirements do not apply to Internal Service Funds that are specifically designed to accumulate reserves for capital, such as the Vehicle Replacement Fund.

SECTION 7: APPROPRIATED RESERVES

An Appropriated Reserve will be included in each operating fund's adopted budget to provide for unanticipated expenditures or to meet unexpected small increases in service delivery costs within the fiscal year. For the General Fund, the appropriated reserve should be at least $150,000. For Enterprise and Internal Service operating funds, this reserve will be at least one-half of one percent of the operating budget. Any unused portion of the appropriated reserve in each fund will be returned to fund balance at the end of the fiscal year.

The use of the General Fund appropriated reserve requires an affirmative vote of a majority of the City Council; use of appropriated reserves in Enterprise and Internal Service Funds requires approval of the appropriate department head.

SECTION 8: ALLOCATION OF GENERAL FUND YEAR-END SURPLUS TO CAPITAL

At the end of each fiscal year, any General Fund surplus realized from actual revenues exceeding actual expenditures including the annual capital program will be used as follows:

- 50% will be used to fund any deficit and/or maintain reserve balances at levels required by this policy.

- The remaining surplus of at least 50% will be transferred into a capital sinking fund that will be available for capital improvements and replacements.

To the extent less than 50% of the surplus is needed to maintain required reserve balances, the remaining balance will be transferred into the capital sinking fund.

Any allocation of year-end surplus towards capital should not be used to supplant the annual capital program funding. Therefore, the calculation of the year-end surplus will be after including the expenditures for the annual capital program.