



MEMORANDUM

TO: City Council

FROM: Matthew Downing, City Manager

BY: Nicole Valentine, Administrative Services Director

SUBJECT: Adoption of a Resolution Updating the Fund Balance and Reserve Policy

DATE: June 11, 2024

RECOMMENDATION:

1) Adopt a Resolution Updating the Fund Balance and Reserve Policy; and
2) Determine that adopting a resolution updating the Fund Balance and Reserve Policy is not subject to the California Environmental Quality Act ("CEQA") because it has no potential to result in either a direct, or reasonably foreseeable indirect, physical change in the environment. (State CEQA Guidelines, Cal. Code Regs., tit. 14, §§ 15060, subd. (c)(2)- (3), 15378.)

IMPACT ON FINANCIAL AND PERSONNEL RESOURCES:

There is no fiscal impact resulting from updating the Fund Balance and Reserve Policy. The total fund balance amounts reported in any given fund will not be altered. Only the consideration of reporting of the individual components that make up the total fund balance are being discussed.

BACKGROUND:

The City Council first adopted the Fiscal Policy on September 5, 1995, and has revised the policy several times, most recently on June 28, 2011. Many of these updates were included with a review of the budget adoption. The current Fiscal Policy states the City will:

- Establish and maintain a Fund Balance reserve goal of 20% of expenditures with a minimum of 15% in the General Fund.
- Maintain a minimum of 5% of the General Fund budget as a Contingency Reserve.

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- Contribute 10% of annual appropriations to the improvement of Infrastructure.

Over many years, the City has established a comprehensive and extensive budget and financial policy framework. This framework is reviewed with each Biennial Budget and periodically amended based on the need of the organization as well as changes in mandates and best practices.

In 2009, the Governmental Accounting Standard Board (GASB) introduced GASB Statement No. 54 – Fund Balance Reporting and Governmental Fund Type Definitions. The statement’s objective is to enhance the usefulness of fund balance information by providing clearer fund balance classifications that can be applied consistently. The classifications comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in its governmental funds.

In order to apply GASB 54, staff amended the established policies and combined them into a stand-alone comprehensive policy document for easy access and reference. The City’s Biennial Budget will continue to incorporate this information in the financial policy section and reference the adopting resolution. Additionally, the Fund Balance and Reserve Policy will be posted on the City website. The City’s independent auditor will use the definitions of fund balance when providing the City’s annual audit and annual financial statements.

On [June 27, 2023](#), the City Council adopted the FY 2023-25 Biennial Budget, which included an overview of the Consolidated General Fund to provide the City Council and the community the full picture of City revenues, expenditures, ending fund balances, and the updated Consolidated General Fund as shown in Table 1.

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Table 1: FY 2023-25 Consolidated General Fund Budget & Available Fund Balance in Thousands

	FY 2023-24			FY 2024-25		
	General Fund	Local Sales	Consolidated Total	General Fund	Local Sales	Consolidated Total
Beginning Fund Balance	\$8,993	\$3,093	\$12,086	\$8,462	\$2,904	\$11,366
Revenues:						
Revenues	18,544	2,962	21,506	19,000	3,033	22,033
Transfers In	3,114	-	3,114	3,185	-	3,185
Total Revenues	21,658	2,962	24,620	22,185	3,033	25,218
Expenditures:						
Salaries and Benefits	12,089	-	12,089	12,437	-	12,437
Services and Supplies	9,435	1,042	10,477	9,775	1,087	10,862
Debt Service	310	-	310	294	-	294
Capital Outlay	240	-	240	150	-	150
Transfers Out	115	2,109	2,224	2,475	3,858	6,333
Total Expenditures	22,189	3,151	25,340	25,131	4,945	30,076
Total Operating Incr/(Dec)	(531)	(189)	(720)	(2,946)	(1,912)	(4,858)
Available Fund Balance	\$8,462	\$2,904	\$11,366	\$5,516	\$992	\$6,508
Reserve %	38.1%	92.2%	44.9%	22.0%	20.1%	21.6%
\$ Above Reserve Policy	4,025	2,274	6,299	491	3	494
Funds Available to Allocate	3,500	1,695	5,195	400	-	400

The City's Annual Comprehensive Financial Report (ACFR) was presented on [January 23, 2024](#), and a request to review the reserve policy was discussed. The Beginning Fund Balances for the funds have been updated upon completion of the ACFR and are shown in Table 2.

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Table 2: Updated Fund Balances FY 2023-25 Consolidated General Fund Budget & Available Fund Balance in Thousands

	FY 2023-24			FY 2024-25		
	General Fund	Local Sales	Consolidated Total	General Fund	Local Sales	Consolidated Total
Beginning Fund Balance	\$11,862	\$7,625	\$19,487	\$11,331	\$7,436	\$18,767
Revenues:						
Revenues	18,544	2,962	21,506	19,000	3,033	22,033
Transfers In	3,114	-	3,114	3,185	-	3,185
Total Revenues	21,658	2,962	24,620	22,185	3,033	25,218
Expenditures:						
Salaries and Benefits	12,089	-	12,089	12,437	-	12,437
Services and Supplies	9,435	1,042	10,477	9,775	1,087	10,862
Debt Service	310	-	310	294	-	294
Capital Outlay	240	-	240	150	-	150
Transfers Out	115	2,109	2,224	2,475	3,858	6,333
Total Expenditures	22,189	3,151	25,340	25,131	4,945	30,076
Total Operating Incr/(Decr)	(531)	(189)	(720)	(2,946)	(1,912)	(4,858)
Available Fund Balance	\$11,331	\$7,436	\$18,767	\$8,385	\$5,524	\$13,909
Reserve %	51.1%	236.0%	74.1%	33.4%	111.7%	46.3%
\$ Above Reserve Policy	6,895	6,806	13,701	3,360	4,536	7,896
Funds Available to Allocate	3,300	4,520	7,820	2,800	3,780	6,580

The estimated Consolidated General Fund available fund balance at the end of FY 2024-25 is \$13,909,000.

Staff brought forward a Fund Balance and Reserve Policy during the [April 9, 2024](#), City Council meeting to update the existing policy and consider updating the policy to incorporate a Budget Stabilization Reserve, as well as, three replacement/repairs reserves. This item was continued and staff incorporated this discussion in the preliminary budget item presented to the City Council on [May 28, 2024](#).

The City Council reviewed the preliminary budget and provided direction to appropriate \$560,000 of Excess Available Consolidated General Fund Balance to the three replacement/repairs reserves:

- Information Technology Reserve
- Fleet Replacement Reserve
- Facility Repairs Reserve

The Fund Balance and Reserve Policy has been updated to incorporate this direction.

ANALYSIS OF ISSUES:

Healthy reserves are a mark of fiscal stability and a cornerstone of financial flexibility. The Government Finance Officers Association best practice recommends, at a minimum, that general-purpose governments, regardless of size, maintain unrestricted budgetary fund

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balance in their General Fund of no less than two months (16.67%) of regular general fund operating revenues or operating expenditures.

The updated Fund Balance and Reserve Policy included as Exhibit A to Attachment 1 does not change the current Operating Reserve policy that is equal to 15%, with a goal of 20% of the City's annual operating expenditures.

The updated Fund Balance and Reserve Policy also maintains a Pension and Other Post-Employment Benefits Reserve. Funds set aside under this reserve shall be used to further mitigate costs associated with pensions and other post-employment benefits. These funds will be used as a funding source for potential additional discretionary payments to pay down unfunded liability, held in the reserve account, or placed in a City Council approved trust instrument. Funds may be used for such purposes as a supplemental funding source for unanticipated increases to the annual pension and/or other post-employment benefit costs resulting from future actuarial assumptions and investment market volatility, or to make the City's annual payments during times of economic uncertainty as brought on by such circumstances as a recession resulting in funding gaps.

Additionally, the updated Fund Balance and Reserve Policy establishes three replacement/repairs reserves:

- Information Technology Reserve – Funds set aside under this reserve shall be used for information system and technology projects including communications systems, hardware, and software, which are capital in nature. Technology can change rapidly within the information systems sphere and often comes at a large cost. This reserve helps the City keep pace with changes in information technology and take advantage of improvement/efficiency opportunities in this area. While this will not eliminate the need to utilize the General Fund to support technology, it will help defray costs associated with unforeseen impacts to the City's Information Technology system.
- Fleet Replacement Reserve – Funds set aside under this reserve shall be used to maintain a Fleet Replacement Reserve in the Consolidated General Fund to provide for the timely replacement of existing vehicles should they come to the end of their useful life or become inoperable. The intent of this fund is to help self-finance the City's fleet needs into the future.
- Facility Repairs Reserve – Funds set aside under this reserve shall be to address any unforeseen maintenance and repairs or planned replacements within City

owned facilities. This fund is not intended to support planned facility maintenance and repairs.

The three replacement/repairs reserves would have a maximum fund balance of 1% each, bringing the full Reserve Policy to a total of 23% of the City's annual operating expenditures. Any Excess Available General Fund Balance above 23% would be brought back to the City Council each year for consideration and options of how to appropriate funds.

ALTERNATIVES:

The following alternatives are provided for the Council's consideration:

1. Adopt a Resolution updating the Fund Balance and Reserve Policy;
2. Modify as appropriate the Fund Balance and Reserve Policy; or
3. Provide other direction to staff.

ADVANTAGES:

The last update to the Fund Balance and Reserve Policy was more than thirteen years ago. The proposed changes align the GFOA best practices and continue to improve the City's ongoing commitment to responsible stewardship and transparency of public funds.

DISADVANTAGES:

There are no disadvantages in relation to the recommended action.

ENVIRONMENTAL REVIEW:

Adopting a resolution updating the Fund Balance and Reserve Policy is not subject to the California Environmental Quality Act ("CEQA") because it has no potential to result in either a direct, or reasonably foreseeable indirect, physical change in the environment. (State CEQA Guidelines, Cal. Code Regs., tit. 14, §§ 15060, subd. (c)(2)- (3), 15378.)

PUBLIC NOTIFICATION AND COMMENTS:

The Agenda was posted at City Hall and on the City's website in accordance with Government Code Section 54954.2.

ATTACHMENTS:

1. Proposed Resolution