WASHOE COUNTY

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STAFF REPORT
BOARD MEETING DATE: May 17, 2016

DATE: May 4, 2016

TO: Board of County Commissioners

FROM: Mark Mathers, Budget Manager
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THROUGH: Al Rogers, Director of Management Services
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SUBJECT: Recommendation to amend the County's fund balance policy that sets minimum fund balance levels for working capital. (All Commission Districts)

SUMMARY

The purpose of this item is to amend the County's fund balance policy that sets minimum fund balance levels in the General Fund for the purpose of sustainability of a working capital balance in accordance with the Government Finance Officers Association (GFOA) best practices.

Washoe County Strategic Objective supported by this item: Sustainability of our financial, social and natural resources.

PREVIOUS ACTION

May 10, 2011 – the Board of County Commissioners (BCC) approved a fund balance policy that sets minimum fund balance levels in the General Fund for the purpose of stabilization at 1.5%, and for the purpose of sustainability of a working capital between 8% and 10%.

June 26, 2012 – the BCC approved an amendment to the fund balance policy that set a minimum fund balance level in the General Fund for the purpose of stabilization at 1.5% of expenditures and other uses excluding material one-time expenditure items.

April 28, 2015 – the BCC approved an amendment to the fund balance policy that set a minimum fund balance level in the General Fund for the purpose of stabilization at $3,000,000.

January 19, 2016 – At the BCC's Strategic Plan retreat, staff presented a preliminary recommendation to amend the County's fund balance policy that sets minimum fund balance levels in the General Fund for the purpose of sustainability of a working capital balance from the current range of 8% to 10% to a new range of 10% to 17%.

AGENDA ITEM # 10

April 26, 2016 – the County Manager's recommended Fiscal Year 2016-17 budget was presented to the BCC. The recommended budget tentatively budgeted a working capital fund balance of 13%.

BACKGROUND

It is essential that the County maintain adequate levels of fund balance to mitigate current and future risks that can occur from unforeseen revenue fluctuations and/or unanticipated expenditures, and to fund all existing encumbrances. The General Fund balance also provides cash flow liquidity to fund general operations.

In 2009, the Government Finance Officers Association (GFOA) issued Best Practice Appropriate Levels of Unrestricted Fund Balance in the General Fund, which recommended at a minimum, that general-purpose governments, regardless of size, incorporate in its financial policies that unrestricted fund balance in their general fund be no less than two months of regular general fund operating revenues or regular general fund operating expenditures. This best practice was most recently updated in September 2015, and again recommends a minimum "unrestricted budgetary fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures." Two months' reserve equates to 16.66%.

Nevada Administrative Code 354.650 essentially mandates a minimum 4% ending fund balance for local governments. In 2015, Senate Bill 168, which allows for a budgeted ending General Fund balance of up to 25%, was signed into law. Staff recommends that in the short- to intermediate-term, Washoe County meets the GFOA's recommendation of a minimum available General Fund balance of two months of General Fund operating expenditures and other uses. In recognition of the fact that the County's current policy is 8% to 10% and in FY 2016-17, property taxes are unexpectedly capped below 3%, it is recommended that the BCC amend the County's fund balance policy that sets minimum working capital fund balance levels in the General Fund to a range of 10% to 17%. This should allow the County to achieve a budgeted available fund balance in compliance with GFOA's recommendation in the next one to three years. An increase in the General Fund's available ending fund balance should also help the County better manage a decline or flattening of revenues in the future due to a recession or economic slowdown.

It is also recommended that the County set a policy for the ending fund balance of special revenue funds of 10% to 17% of operating expenditures and other uses, allowing for certain exceptions.

FISCAL IMPACT

Based on direction of the Board of County Commissioners in January 2016 and on April 26, 2016, the County's Fiscal Year 2016-17 Final Budget incorporates an available ending General Fund balance for working capital above 10%.

An analysis of special revenue funds' balances as of June 30, 2015, shows that all special revenue funds maintained an ending fund balance above 10% except the Senior Services Fund (8.8%) and Child Protective Services Fund (7.9%). The Budget Office has been in contact with departments affected by this new policy for special revenue funds and will work with departments not currently in compliance to raise the level of reserves in future years.

RECOMMENDATION

It is recommended that the Board approve the attached "Washoe County, Nevada, Fund Balance Policy", which amends the County's fund balance policy that sets a minimum fund balance level in the General Fund for the purpose of working capital to between 10% and 17% and an ending fund balance for special revenue funds of 10% to 17%, with certain exceptions.

POSSIBLE MOTION

Should the Board agree with staff's recommendation, a possible motion would be "move to approve the attached 'Washoe County, Nevada, Fund Balance Policy', which amends the County's fund balance policy that sets a minimum fund balance level in the General Fund for the purpose of working capital to between 10% and 17% and an ending fund balance for special revenue funds of 10% to 17%, with certain exceptions."

WASHOE COUNTY, NEVADA
FUND BALANCE POLICY

Purpose of Fund Balance Policy

The purpose of this policy is to establish a key element of the financial stability of the County by ensuring adequate levels of unrestricted fund balance are maintained in the General Fund, the County's main operating fund. It is essential that the County maintain adequate levels of fund balance to mitigate current and future risks that can occur from unforeseen revenue fluctuations and/or unanticipated expenditures, and to fund all existing encumbrances. The General Fund balance also provides cash flow liquidity to fund general operations.

Another consideration in the establishment of a sound fund balance policy is that credit rating agencies consider the County's fund balance policy, history of use of fund balance, and policy and practice of replenishment of fund balance when assigning ratings. Thus, a well-developed and transparent strategy to replenish fund balance may reduce the cost of borrowing.

The Government Finance Officers Association (GFOA) recommends, at a minimum, that general-purpose governments, regardless of size, incorporate in its financial policies that unrestricted fund balance in their general fund be no less than two months of regular general fund operating revenues or regular general fund operating expenditures. This policy specifies the size and composition of the County's financial reserves and identifies certain requirements for replenishing any utilized fund balance reserves that is intended to comply with sound financial management and best practices as identified by the (GFOA).

Definitions

Fund balance is the difference between a fund's assets and liabilities and is classified in five categories that focus on the extent to which the County is bound to honor constraints on the specific purpose for which amounts can be spent.

- ***Nonspendable fund balance***—amounts that are not in a spendable form (such as inventory) or are required to be maintained intact (such as the corpus of an endowment fund)
- ***Restricted fund balance***—amounts constrained to specific purposes by their providers (such as grantors, bondholders, and higher levels of government), through constitutional provisions, or by enabling legislation
- ***Committed fund balance***—amounts constrained to specific purposes by the County, using its highest level of decision-making authority (the Board of County Commissioners); to be reported as committed, amounts cannot be used for any other purpose unless the Board of County Commissioners (BCC) takes the same highest-level action to remove or change the constraint
- ***Assigned fund balance***—amounts the County intends to use for a specific purpose; intent can be expressed by the BCC or by an official or body to which the BCC delegates the authority
- ***Unassigned fund balance***—amounts that are available for any purpose; these amounts are reported only in the general fund.

Unrestricted fund balance comprises the committed, assigned and unassigned fund balance categories.

General Fund Minimum Fund Balance Policy

General Fund Stabilization:

It is the County's policy to maintain a General Fund account of $3,000,000 for the purpose of budgetary stabilization. NRS 354.6115 authorizes the creation of a fund to stabilize operation of local governments and mitigate effects of natural disaster. The intent of this policy is to include in the General Fund budgeted reserved ending fund balance pursuant to NRS 354.6115 that will be committed to stabilization. Fund balance that is committed to stabilization can be used under the following circumstances after approval by the Board of County Commissioners.

1. An unanticipated decline in Consolidated Tax revenues, General Fund property tax revenues or other significant General Fund revenues that is sustained for at least 6 months and has declined from budget by 2.5% or greater.
2. To cover unanticipated expenditures caused by declared emergency or natural disaster.

In the event fund balances committed for stabilization are required to be used under the above circumstances, the Budget Manager shall make a recommendation to the BCC that includes the following:

- The reasons for the use of fund balance;
- The amount required for stabilization;
- The long-term financial plan to stabilize economic condition that has occurred; and
- A plan explaining the steps that will be taken to replenish fund balance to the minimum target level, which ideally would involve a timeframe for replenishment not to exceed three years but that should take into consideration the severity and length of an economic slowdown, recession or depression.

General Fund Working Capital:

It is the County's policy to maintain an unrestricted General Fund balance, excluding that held for stabilization, which seeks to meet the minimum level that complies with recommended best practice. Based on GFOA recommended best practices, the County has determined a minimum of 10% and a maximum of 17% of expenditures and other uses, less capital outlay, is required to meet the County's cash flow and operating needs that complies with best practices.

In the event fund balances are anticipated to be outside of the target range for the current fiscal year, the Budget Manager shall make a recommendation to the BCC that includes the following:

- The reasons for the fund balance being outside the range of this policy;
- The long-term financial plan that addresses working capital needs; and
- A plan explaining the steps that will be taken to replenish or reduce fund balance to the target levels which ideally would involve a timeframe for replenishment not to exceed

three years but that should take into consideration the severity and length of an economic slowdown, recession or depression.

All Governmental Funds Order of Fund Balance Use Policy

When both restricted and unrestricted funds are available for expenditure, restricted funds should be spent first unless legal requirements disallow it.

When committed, assigned and unassigned funds are available for expenditure, committed funds should be spent first, assigned funds second, and unassigned funds last.

Special Revenue Funds Ending Fund Balance Policy:

It is the County's policy for special revenue funds to maintain an ending fund balance between a minimum of 10% and a maximum of 17% of expenditures and other uses, less capital outlay, in order to meet cash flow and operating needs that complies with best practices. Exceptions to this policy include:

1. When such a policy contradicts federal or state laws or regulations specific to a fund's purpose.
2. A fund's ending fund balance may exceed 17% depending on the following factors:
    a. The predictability of its revenues, especially if a fund's revenues are highly concentrated, and the volatility of its expenditures.
    b. If there are known resource requirements, such as for significant capital improvement projects, in the future that require an increase in reserves.
    c. Its perceived exposure to significant one-time events (e.g., disasters, immediate capital needs, state budget cuts).
    d. An oversight or governing board of a fund has determined that a higher ending fund balance is warranted.
    e. One of the fund's primary purposes is to finance future capital outlay or improvements, which requires a build-up of reserves.
    f. The potential impact on the entity's bond ratings and the corresponding increased cost of borrowed funds.

Because of the limitations in State law concerning budgeting practices and mid-year augmentations, this policy recognizes that there may significant variations between a fund's budgeted ending fund balance and actual fund balance at fiscal year-end. Therefore, compliance with the above policy for special revenue funds will be measured based on the actual, audited ending fund balance of a fund.