

Staff Report
Library Joint Powers Board

DATE: 5/23/13

AGENDA OF: 6/03/13

DEPARTMENT: City of Santa Cruz Finance Department
BY: Marcus Pimentel, City of Santa Cruz Finance Director

SUBJECT: Library Reserve Levels- Recommendation

RECOMMENDATION: That following the Finance Committee's recommendation, the Board amend the Board's Budgetary Policy to (a) replace the 5% operating reserve and future 10% reserve with a System Wide Stabilization Arrangement (i.e., Reserve) at a 2-month funded level; and (b) adopt a Library operating fund Surplus policy.

BACKGROUND: On April 6, 2009, the Library Board approved two primary reserve related requirements; that it maintain an operating reserve equal to 5% and that 8% of its revenue stream be dedicated for Materials purchases. Almost two years later, on April 4, 2011, the Board subsequently adopted a goal of reaching a 10% reserve by Fiscal Year 2016/17 with a goal of increasing available "Fund Balance" to 5% of revenues by Fiscal Year 2015/16 for unexpected service model funding.

On April 22, 2013, the Finance Committee reviewed various reserve recommendations prior to incorporating alternatives into the Board's May 6, 2013 Budget 13/14 review. Subsequently, during the May 18, 2013 Board Retreat, the Board held additional discussion regarding reserves and surplus policies. On May 20, 2013, the Finance Committee reviewed and made its final recommendation to adopt a 2-month reserve effective immediately and supported the surplus policy. The Committee will bring back, for additional discussion in the coming year, other reserve recommendations surrounding a 2-week operating reserve and a capital reserve.

As of the close of April 2013, the Library's cash balance was 22.3% of its budgeted revenue, or equivalent to 2.7 months.

On June 6, 2011, the Library Board was required to adopt new GASB Accounting requirements for fund balance and reserves. GASB replaced prior Fund Balance categories (or reserves) with specially defined new categories of Nonspendable, Restricted, Committed, Assigned and Unassigned (listed respectively from the most restrictive to the least restrictive). The first two categories can only be established by third parties. The third category of a "Committed" reserve can be created by the Library Board. The Library Director (staff) can create any "Assigned" reserve. The final category, "Unassigned" is just that, all remaining fund balance without any higher level restrictions. Note that it would still require the Library JPA Board's approval to appropriate budget dollars using any "unassigned" Fund Balance. Another action of the GASB requirements was to limit the ability to show within the face of the Library's financial statements reserves to only those reserves that meet the strict requirements defined within GASB 54's "Stabilization Arrangements" section. Therefore, we are using this technical reference with regard to our reserve recommendation.

Within the action to adopt the new Fund Balance policy, the Board also authorized the elimination of the Capital Projects Reserve Fund and Contingency Reserve Fund but retained the "5% cash flow reserve", a "Technology" reserve accounted for as a Special Fund (#956) and

a "Felton" reserve accounted for as a Special Fund (#960). The Library also holds a "Vehicle Replacement" reserve within a Special Fund (#961).

In addition to the reserves included in the GASB policy, the Library also maintains restricted trust accounts whose funding is segregated from any other operating, general reserve or Special Fund accounts. They include the following restricted trusts; McCaskill (2 accounts), Finkeldey, Whalen, Leet-Corday, Morley and Hale.

DISCUSSION: Over the course of the past few months, the Finance Committee has discussed reserve options and, on May 20, 2013 finalized their recommendation to establish a 2-month reserve and adopt a surplus policy. The 2-month reserve will replace the current 5% operating reserve and the future 10% reserve that was to be funded by FY2016/17.

The uses of the 2-month reserve could include unanticipated but significant drops in revenue or new operating or facility immediate costs to preserve safety or operations. For example, the closure of a significant sales tax retailer would allow the Board to dip into this reserve to keep operations funded while providing time for evaluation of new budget strategy. Another potential use could be for the sudden and immediate need to protect the community or library patrons from a facility failure (such as damage to the floors, wall or ceiling).

As a point of comparison, presented below are examples of other Library reserve policies. These libraries were identified during a statewide survey of systems similar in structure.

Palos Verdes	Rancho Cucamonga	Santa Clara County	GFOA- National Association
1. 6-month Op. expenses 2. 5% Minimum for emergency 3. Next Year's "asset replacement" 4. Election years-pay election expenses of Board 5. Additional 5% for emergencies	1. 50% reserve 2. formally included a "Redevelopment Agency" capital reserve	No policy	2-month minimum consideration

In addition, the City of Santa Cruz conducted research of reserve policies of 9 comparable cities as summarized in the table below:

Santa Cruz	Davis	Monterey	Napa	Palm Springs	San Luis Obispo	Santa Barbara	Santa Maria	Ventura
10% of budget	15% of revenue	15% of revenue	15% of exp	10% of budget	20% of op costs	25% of op bud	25% of op bud	90 days plus \$3M catastrophic

RECOMMENDATION: Staff's recommendation is that the Board adopts a 2-month reserve policy and a surplus policy. The impact of these two actions is summarized below.

Reserve/Funding Category	Staff Recommendation	Current Funding Level	New Funding Level
System Wide 2-month	Increase from 5% to 2-months (16.7%)	\$ 604,450	\$ 2,014,833
Surplus Policy	Distribution of annual surplus; limited to 1/3 of the lowest surplus in the last 3 FY's	n/a	est. \$260,000

The reserves that will be considered in the future, based on results of future operations, include, but may not be limited to:

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Reserve/Funding Category	Staff Recommendation	Current Funding Level	Proposed Increase
Materials	Increase from 8% to 12%	\$ 909,826	\$ 460,000
Facility Capital Projects	Reestablish based on unfunded projects	n/a	Tbd
Operating	Reestablish with a 2-week level	n/a	\$ 440,000

RESERVE & POLICY DEFINITIONS

Following are the legally required guidelines to be adopted by the Library Board to adhere to GASB requirements for establishment of official reserves.

[1] Library Joint Powers System Wide Stabilization Arrangements (amendment to Fund Balance Policy)

It is in the best interest of the citizens of Santa Cruz County, who rely upon the Library System, that a portion of the Library's Fund Balance be set aside in a Library System Wide Stabilization Arrangement in order to provide a reserve against certain specified conditions listed herein that are sudden and unexpected drop in revenues and/or unforeseen emergencies including unanticipated expenditures of a nonrecurring nature or unanticipated adverse financial or economic circumstances that would lead to operating shortfalls.

Therefore, the Library Board shall, by Resolution, authorize the establishment of a continuing and non-lapsing Stabilization Arrangement as an amendment to the Board's Fund Balance Policy.

Note that included in the specific use circumstances below is the ability to temporarily, for pure timing situations, fall below this arrangements funding level. This provides cash-flow flexibility when the timing of a revenue source or prepayment of a large expenditure would cause, for example, the reserve to be temporarily reduced.

System Wide Stabilization Arrangement amount. The funding level shall be equal to but can exceed the equivalent of 2-months of the current fiscal year's Adopted Total General Fund Operating Revenue Budget.

Contributions and immediate funding of the System Wide Stabilization Arrangement. The Library Board shall authorize the Library Director to maintain a minimum balance defined above through transfers of available ending Fund Balance after the Budget is adopted for the upcoming year, but before the end of the current fiscal year.

Therefore, given that the Library's current cash balance as of the month ended April 30, 2013 is already in excess of 2-months of the General Fund's Operating Revenue Budget for FY12/13, the Library Board shall authorize the Library Director to fully fund this arrangement.

Conditions under which the System Wide Stabilization Arrangement may be spent. Appropriations shall require a Resolution from the Library Board approved by a majority of the Board. However, if there is an urgent safety need, the Library Director can authorize expenditures of this fund provided it is brought back to the board at its next Board meeting.

Under either case, the Library Director, shall within 6 months, present to the Board a plan and timeline for replenishing the Arrangement to its minimum funding level. Requests for

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appropriations shall occur only after exhausting current year's budgetary flexibility and spending of the current year's appropriated contingency, if any.

Circumstances where the Stabilization Arrangement can be spent are:

1. Within a 12-month period, funding can be used for cash-flow purposes when timing requires a one-time reduction in cash that will be 100% restored within 12-months.
2. Unanticipated Library revenues, in total, are expected to decline more than 1 percent of total projected, and actual revenues for one of the following major revenue sources are projected in the current year to fall below the actual amount from the prior year:
 - a.) Sales Taxes
 - b.) Maintenance of effort contributions
3. If any one of the unforeseen and non-recurring events listed below occur that create significant financial difficulty for the Library and are in excess of the current year's appropriated contingency:
 - a.) Sudden and unexpected significant facility failures that threaten the immediate safety of Library patrons, staff or the community;
 - b.) Declaration of a State of Emergency by the Governor;
 - c.) Unanticipated expenditures as a result of legislative changes from State/Federal governments in the current fiscal year;
 - d.) Acts of Terrorism declared by the Governor or the President of the United States;
 - e.) Acts of Nature which are infrequent in occurrence.

[2] Library Surplus policy (new).

It is in the best interest of the citizens of Santa Cruz County who rely upon the Library System that the Board makes prudent use of one-time resources to provide stability and sustainability to the Library's operations.

Therefore, the Library Board shall by Resolution authorize that beginning with the results of Fiscal Year 2013-14, any future amounts attributed to one-third (1/3) of the Library's last year's audited General Fund surplus (defined as "Net Change in Fund Balance" as contained within the annual Basic Financial Statements "State of Revenues, Expenditures and Changes in Fund Balance-Governmental Fund") shall be used for the purposes as outlined below in priority order:

1. To take advantage of prepayment, one-time operating discounts such as CalPERS Employer Retirement Obligations.
2. To pay down outstanding debt
3. To build up "available Fund Balance" for future, one-time operational purposes
4. To, if after three (3) consecutive years of surplus, increase the operating budget by one-third of the lowest surplus within any single year of the past the three (3) surplus years.

This policy could supplement future policies to allocate one-third (1/3) of any prior year's surplus to fund Materials and another one-third (1/3) to be transferred to the Facility Capital Project reserve.

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RESOLUTION # 2013-04

**RESOLUTION OF THE
SANTA CRUZ LIBRARY JOINT POWERS AUTHORITY BOARD
AMENDING THE FUND BALANCE POLICY TO INCLUDE ESTABLISHING A
LIBRARY SYSTEM WIDE STABILIZATION ARRANGEMENT**

WHEREAS, it is in the best interest of the citizens of Santa Cruz County, who rely upon the Library System;

WHEREAS, that a portion of the Library's Fund Balance be set aside in a Library System Wide Stabilization Arrangement;

WHEREAS, in order to provide a reserve against certain specified conditions listed herein that are sudden and unexpected drop in revenues and/or unforeseen emergencies including unanticipated expenditures of a nonrecurring nature or unanticipated adverse financial or economic circumstances that would lead to operating shortfalls.

NOW THEREFORE, be it resolved by the Library Joint Powers Authority Board that it authorize the establishment of a continuing and non-lapsing Stabilization Arrangement as an amendment to the Board Fund Balance Policy.

PASSED AND ADOPTED this 3rd day of June 2013 by the following votes:

AYES: Board Member(s):

NOES: Board Member(s):

ABSENT: Board Member(s):

DISQUALIFIED: Board Member(s):

APPROVED

ATTEST

Chair

Board Clerk



RESOLUTION # 2013-05

**RESOLUTION OF THE
SANTA CRUZ LIBRARY JOINT POWERS AUTHORITY BOARD
ESTABLISH A LIBRARY SURPLUS POLICY**

WHEREAS, it is in the best interest of the citizens of Santa Cruz County who rely upon the Library System that the Board makes prudent use of one-time resources to provide stability and sustainability to the Library's operations;

WHEREAS, beginning with the results of Fiscal Year 2013-14, any future amounts attributed to one-third (1/3) of the Library's last year's audited General Fund surplus shall be used for the purposes as outlined herein.

NOW THEREFORE, be it resolved by the Library Joint Powers Authority Board that it authorize the establishment of Library Surplus Policy.

PASSED AND ADOPTED this 3rd day of June 2013 by the following votes:

AYES: Board Member(s):

NOES: Board Member(s):

ABSENT: Board Member(s):

DISQUALIFIED: Board Member(s):

APPROVED

ATTEST

Chair

Board Clerk

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