

From: Conan Smith  
Sent: Thursday, May 01, 2014 4:14 PM  
To: Felicia Brabec; Andy LaBarre; Yousef D. Rabhi; Alicia D. Ping  
Subject: !! Spring Budget Process

Leaders . . . my apologies for an extensive email, but I want to get a mess of my thought process in front of you in hopes that we can take some actions at the 5/7 meeting regarding the upcoming budget process, and I want to spend a little time advocating over the next week. I'd prefer to do that with you advice and engaged support, so I'm dumping a bunch of stuff on you here. :-)

Per our budget boilerplate we are supposed to enter into a process this month, culminating in board action in July, to allocate surplus funds available in 2014. We have received and voted now on both the 2013 audited financials and the 2014 county equalization report. These two items clarify the annual surplus/deficit for 2014 (blessedly, a surplus).

The audited financials indicate a General Fund fund balance of \$20,708,905. The budget we adopted for 2014-17 allocates \$17,867,835 to this purpose. This means there is \$2,841,070 in excess revenue over expenditures from 2013 that the Board of Commissioners has not appropriated for use in 2014.

In addition, the equalization report showed an increase in property values resulting in \$720,486 in unbudgeted revenue.

All told the County has \$3,561,556 in "unallocated reserves" (funds that the BOC has not yet voted to appropriate).

I know this is kind of confusing for people because any excess revenue or unspent funds automatically accrue to General Fund fund balance without action by the board per our policy, so in a sense we have voted to not allocate those funds at all. However, I believe the board should make proactive decisions about the appropriation of these funds to ensure investments are meeting the community's priorities and to create confidence throughout our organization that an array of interests are being considered (beyond the growth of fund balance).

I have a few thoughts about what I would like us to do in regards to the allocation of funds like this.

Recommendation 1: Create a formal Budget Stabilization Fund (BSF) to segregate our strategic reserves from our unallocated GF fund balance.

There is always confusion over the GF fund balance. It is strategically important for us to have strong reserves for cashflow purposes and to act as our own "rainy day fund". However, because dollars automatically accrue to fund balance without a discussion about whether or not they should be used for other

purposes, elected officials, department heads, project managers, union negotiators, and community/nonprofit leaders all experience frustration when they see fund balance going up while their own priorities are unaddressed (or worse, when we continue to ask them to accept cuts).

Our conversations over the past several years have focused on the need for fund balance for two purposes 1) to secure sufficient cash to manage operations without short-term borrowing and 2) to support high degrees of creditworthiness, i.e. to improve our bond rating. The board has adopted a target of 20 percent of GF for these purposes. This target is somewhat higher than the minimum recommended by the Government Finance Officers Associations of 16 percent, and it is double what our bond attorneys have indicated is necessary to maintain our High Grade bond rating. Should you be interested, the GFOA policy <[http://www.gfoa.org/downloads/AppropriateLevelUnrestrictedFundBalanceGeneralFund\\_BestPractice.pdf](http://www.gfoa.org/downloads/AppropriateLevelUnrestrictedFundBalanceGeneralFund_BestPractice.pdf)> (2 pages long) is a very nice guidepost.

I recommend we create a Budget Stabilization Fund (BSF) with the specific purpose of serving as a cash reserve for cashflow management and emergencies. Since these funds would only be restricted by BOC policy our audits under GAAP should reflect any funds we appropriate to the BSF as unrestricted fund balance, meeting both of our strategic priorities (cashflow and credit worthiness) with regards to reserves.

We should adopt a policy for the BSF indicating how and by whom those funds may be used. We should set a floor for the BSF at 10 percent of the General Fund, and we should amend the budget boilerplate (Section D.11) to apply the 20 percent goal to the BSF. Finally, we should appropriate \$18,167,835 to the BSF immediately. This is the amount that the 2014-17 budget anticipates being in reserve at the end of this current calendar year.

To me there are two main benefits to creating a BSF: 1) it will be clear to the public that we are building a cash reserve in a specific place for a specific purpose, and 2) it makes it clear to commissioners and others that any funds in the GF fund balance are unallocated reserves that the BOC has not taken action on.

Recommendation 2: Clearly articulate a process for setting priorities, soliciting projects and appropriating unallocated reserves each Spring.

Since this is the first year we are using a supplemental budget process, it's a great time to set expectations for the organization and the public about the open process we will use to appropriate unallocated funds. I have a few principles that I think should guide us:

1. We should separate the immediate non structural bump in the current fiscal year from the structural increase/decrease accruing to future fiscal years. Any

structural changes to expenditures precipitated by revenue changes should be brought in October as part of the budget renewal process. Thus the Spring process should focus on one-time allocations -- items that nobody should expect to necessarily see renewed the following year.

2. The first appropriations should be to meet any current year obligations to employee compensation and benefits triggered by our contract clauses related to revenue growth.

3. The second appropriation should be to maintain a proportional commitment to the BSF (e.g., if total revenue increases then our allocation to reserves needs to go up as well so that the target percent for that year can be achieved). This policy would also help ensure that the BSF isn't inappropriately overfunded in years where revenue declines.

4. The process for allocating budget surpluses should be clear, open and transparent. It needs to be accessible to both our internal leaders and our external partners.

Regarding that process, here are some steps I think need to be included:

- \* In May (preferably next week) the BOC should declare what the unallocated fund balance is for the Spring supplemental budget process and discuss the general principles above (or whatever ones we think we need);

- \* No later than our second May meeting, administration should indicate any additions or reductions they expect due to the the above considerations and the BOC should vote on some general parameters (e.g. we want to put X% more to reserves, we want to put X% toward unfunded pension liabilities, we want to put X% to grant matching funds, we want to put X% to special projects, etc. etc.) or some broad priorities.

- \* Administration should recommend and the BOC adopt an open process for people to make recommendations regarding the use of those funds

- \* In June, we should have a budget amendment recommendation from administration at W&M indicating an increase in revenue and suggesting the disposition of the unallocated reserves, and we should vote that through the full board in July (per the budget boilerplate).

I'd like us to take some of these actions next week, and I'd love to work with any of you to write them up as discussion pieces. I welcome a chance to talk about this too, so feel free to call or track me down.

C

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