



MEETING DATE: 01-22-08

ITEM NO: 3.b

## COUNCIL AGENDA REPORT

DATE: JANUARY 17, 2008

TO: MAYOR AND TOWN COUNCIL

FROM: GREG LARSON, TOWN MANAGER

A handwritten signature in cursive script that reads "Greg Larson".

SUBJECT: REPORT EXPLAINING THE COMPOSITION OF THE  
TREASURER'S FUND BALANCE FOR THE MONTH ENDING  
NOVEMBER 30, 2007

### RECOMMENDATION:

Accept report explaining the composition of the Treasurer's Fund Balance for the month ending November 30, 2007.

### BACKGROUND:

On June 18, 2007, staff presented a staff report to the Council clarifying the composition of the cash balances and reserves effective the last audited balance sheet date of June 30, 2006. This report was in response to a number of public comments about the level of Town reserves. Specifically, public comments were that the Town had "\$65 million (or more) in cash reserves." These comments have been repeated in recent months with reference to the fund balance presented in various Treasurer's reports. Due to these recent comments, staff is taking this opportunity to explain the composition of the fund balance presented in the Treasurer's Report for the month ending November 30, 2007, which appears on this agenda. This report provides similar information to that provided in the June 18<sup>th</sup> staff report. In summary, the report notes that only a portion of this balance is reserves. The portion of the balance that is considered Town reserves is further classified into different levels of flexibility and accessibility in terms of the potential for use for public purposes. This report provides information on the total reserves, how they are classified, the rationale used in making that classification, and the potential for discretion in terms of their use.

PREPARED BY: A handwritten signature in cursive script that reads "Stephen Conway".  
STEPHEN CONWAY  
DIRECTOR OF FINANCE

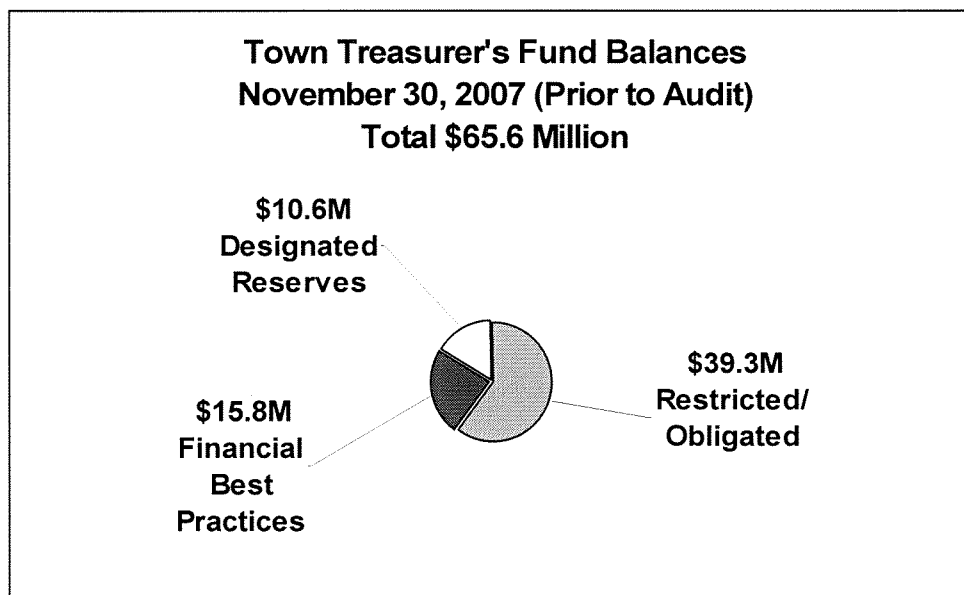
Reviewed by: PS Assistant Town Manager OK Town Attorney \_\_\_\_\_ Clerk  
Administrator \_\_\_\_\_ Finance \_\_\_\_\_ Community Development

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DISCUSSION:

First, it is important to clarify that the \$65.6 million reported as the Treasurer's Fund is not the actual balance of Town reserves. This report is a "one point in time" look at the total cash held in various investment instruments. The amount of cash and investments held by the Town changes every day. In addition, the balance on any given day cannot be considered available to the Town for any public purpose. As discussed below, there are legal restrictions and commitments regarding the use of the funds.

Presented below is a visual summary of the Town Treasurer's Fund Balances as of November 30, 2007, categorized as to the flexibility for general public expenditure purposes:



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Following is a detailed schedule of the amounts shown above:

**SCHEDULE OF TOWN OF LOS GATOS AND REDEVELOPMENT AGENCY  
FINANCIAL STATUS  
(Prior to Audit 11/30/2007)**

Description	Amount (\$ in Millions)
<b>RESTRICTED/OBLIGATED</b>	
Cash Used for Operations	\$ 10.85
Redevelopment Agency Use	12.50
Capital Project Funds	10.60
Special Revenue Funds	0.60
RDA Loan	4.20
Notes Receivable	0.50
<b>Total Restricted</b>	<b>\$ 39.25</b>
<b>Financial BEST PRACTICES</b>	
Internal Service Funds	9.60
Economic Uncertainty	3.70
Liability for Accrued Absences	2.50
<b>Total Financial Best Practices</b>	<b>\$ 15.80</b>
<b>DESIGNATED</b>	
Capital & Special Projects	4.30
Revenue Stabilization	4.80
Civic Center Improvements	0.66
Open Space	0.56
Manager's Contingency & Productivity	0.20
Grants & Carryover Encumbrances	0.03
<b>Total Designated</b>	<b>\$ 10.55</b>
<b>Total Treasurer's Fund Balances</b>	<b>\$ 65.60</b>

**Categories and Classification Criteria**

The categories included in the pie chart and schedule above reflect the level of flexibility with regard to the use of the funds. Following are the criteria used by staff to classify these balances into their respective categories:

Restricted/Obligated (\$39.25 million)

The Restricted/Obligated category includes a mix of restricted reserves and obligated cash. The Restricted/Obligated amounts include:

*Obligated Balance.* This balance represents the working capital of the Town, and is classified as "Obligated." The criteria staff uses for cash to be considered "obligated" is that there are legal or binding contracts for services the Town receives for which payment is expected, which places a hold upon those funds. These funds are equivalent to an

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amount a household would keep in an interest bearing checking account to be used for obligated household expenditures such as paying the monthly mortgage, utilities, credit cards, gas, etc.

- Cash Used for Operations (\$10.85 million). These obligated funds include amounts needed for paying outstanding operating costs like employee compensation, Town vendor invoices, refundable deposit liabilities, and in the case of the RDA, to pay property tax pass-throughs to other taxing agencies.

*Restricted Balances.* Balances considered restricted are actual fund reserves that are legally restricted or have been legally appropriated for specific use. Again, to use the analogy of family finances, these are like different savings accounts a household might establish, for instance, a retirement account that has restrictions on its use or a college savings plan that is restricted by law for use only for higher education costs.

- Redevelopment Agency Use (\$12.5 million). Redevelopment funds are restricted for the elimination of blight in the Agency's project area. A significant portion (\$5.1 million) of this amount is legally restricted to be used for low and moderate housing purposes.
- Capital Project Funds (\$10.6 million) Capital project balances represent amounts appropriated or set aside in the Town capital projects funds (General Fund Appropriated Reserve (GFAR), Storm Drain, Construction Tax) to pay for Council-approved capital projects in accordance with the current year of the Town's Five Year Capital Improvement Plan (CIP). The CIP includes capital improvements like street paving, sidewalk repair, retaining walls and so on. Funds in this category that have not been encumbered legally with construction agreements or purchase orders could technically be "re-programmed" and appropriated for another use by Council, but that would mean that the scheduled infrastructure improvement would not be made as provided for in the Town's current-year CIP.
- RDA Loan / Notes Receivable- (\$4.7 million). Funds are required to be reserved by generally accepted accounting principles for outstanding loans or advances made by the Town to these agencies or programs until repayment is made.
- Special Revenue Funds (\$.6 million) Special revenue funds (Solid Waste, Community Development Block Grant (CDBG), Urban Runoff, Lighting and Landscape Districts) are legally restricted to be used for their specified purpose. For instance the Town's CDBG grant funds must be expended on housing rehabilitation or similar public improvement projects and Solid Waste funds are restricted for use in the Town's solid waste program.

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Financial Best Practices (\$15.8 million)

The reserves presented in the Financial Best Practices category are classified as such by staff recognizing the prudent use of "pre-funding" methods for routine ongoing business needs such as vehicle and equipment replacement or the establishment of an emergency reserve to be available for unanticipated catastrophic events. The funds were established by the Town in prior years following the recommended best practices for state and local governments as established by the Government Finance Officer's Association (GFOA). The targeted funding levels are subject to some discretion in terms of the level of "pre-funding," however, the levels set are considered by staff to be prudent to serve the function for which they were established. To use a household analogy, a financial best practice for a household budget would be insurance policies for earthquakes, floods and fire and dollars set aside to replace the family vehicle, major appliances, etc.

- Internal Service Funds (\$9.6 million) Internal Service funds are set aside to fund vital Town operational needs, providing a reliable source of funding to replace police and public works vehicle fleets, and to pay for vehicle maintenance, building maintenance services, management information services, general liability and worker's compensation claims.
- Economic Uncertainty (\$3.7 million) Established in prior years at a level approximating 15% of the Town's General Fund operating budget, this reserve serves as a financial buffer against unanticipated natural or economic catastrophic events.
- Liability for Accrued Absences (\$2.5 million) This reserve was established by the Town in prior years as a funding source to pay the accumulated employee accrued vacation and sick leave balances that would be due to the employee upon termination or retirement from duty with the Town. The Town currently uses a conservative method, funding this balance at 100% of the total leave balance due as determined at the end of each fiscal year.

Designated Reserves (\$10.6 million)

The criterion for these reserves is that they have been designated for specific purposes by Council policy. Designated reserves are considered discretionary, and can be re-programmed for another purpose by a change in Council policy. Changes to the use of the discretionary reserves would have impacts on the particular purpose for which the reserves have been designated. For example, the \$4.1 million designated Reserve for Capital and Special Projects has been entirely programmed in the Town's Five Year CIP. A policy change in the use of this reserve could be made with the recognition that it would affect the ability to fund future infrastructure improvements. Designated reserves are similar to savings accounts a household might have: for example, a college tuition

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fund, a savings account for future major planned home repairs and improvements like a new roof in ten years, potential loss of income, etc.

- Designated for Capital and Special Projects (\$4.3 million) This reserve was established by Council policy to provide a funding source for Town infrastructure capital and other special projects, and is currently programmed as a funding source for the 5-year CIP. The funds are set aside annually from year-end budget savings. Since the Town has no dedicated source of capital funding, this designated reserve has been a primary source for funding major street and other infrastructure improvements in recent years,
- Designated for Revenue Stabilization (\$4.8 million) The Revenue Stabilization Reserve was first established in the FY 2005/06 budget as a funding source for the Town to pro-actively implement more efficient organizational structures, explore new service delivery options, provide "bridge" funding during short term transitions of businesses that may temporarily reduce sales taxes until a new use is in place, and to allow time for new initiatives and programs to become more fully formed. The availability of bridge funding from this reserve enables the Town to use a longer planning horizon to bring services in line with ongoing available resources. This reserve serves as a vital tool in preserving basic services to the community while making incremental organizational adjustments to align services with revenues over time.
- Designated for Civic Center Improvements (\$0.7 million) This reserve was established by Council to provide a potential funding source for future civic center design and improvements.
- Designated for Open Space (\$0.6 million) This reserve was established in prior years as a funding source for acquisition and maintenance of open space.
- Designated for Manager's Contingency & Productivity (\$0.2 million) Established by Council policy to provide a funding source for productivity initiatives and unforeseen operating budget needs during the fiscal year.
- Designated for Grants & Carryovers (\$0.03 million) This reserve represents amounts set aside for outstanding purchase orders authorized to be carried forward for payment in the next fiscal year.

CONCLUSION:

As the review of the Treasurer's fund balance indicates, the \$65.6 million does not represent the Town's reserves or available cash. Rather, it reflects a comprehensive accounting of all of the working capital, restricted funds, funds used to ensure responsible fiscal management, and funds designated for specific purposes. Of this comprehensive snapshot of the Town's cash and investments, approximately \$10.6 million is considered as designated reserves, subject to Council policy change with consideration as to the impacts on the particular purpose for which the reserves have been designated.