A Tradition of Stewardship
A Commitment to Service

COUNTY EXECUTIVE OFFICE

GENERAL FUND AND CAPITAL RESERVES – POLICY AND HISTORY

March 15, 2012

Napa County has a long history of conservative budgeting, including such practices as saving rather than spending one-time or limited duration revenues, not using local funds to back-fill reductions in state or federal funding for state or federal programs, paying for capital projects on a pay-as –you- go basis rather than issuing debt, aggressively paying off unfunded liabilities and maintaining significant fund balances and reserves, particularly in the General Fund, the County's main operating fund. Maintaining adequate reserves is important because it provides a hedge against economic downturns or other emergencies, ensures that there is sufficient cash flow to meet expenditure obligations without the need for short-term borrowing, and provides resources that can be used for one –time needs, such as major capital projects.

General Fund Reserves

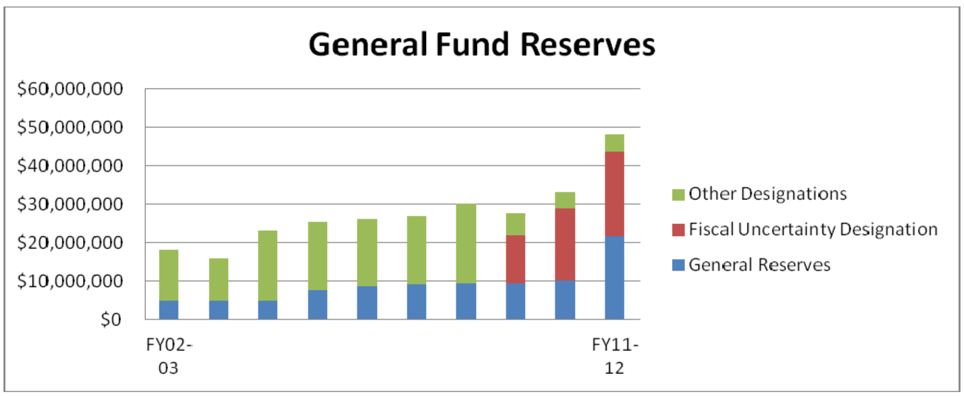
General Fund reserves are typically categorized as either **General Reserves** – which, by law, cannot be spent during a year except in an emergency– or **designations** – which represent money set aside for various purposes and can be spent during a fiscal year if approved by a four-fifths vote of the Board of Supervisors. **Designations** are either "**restricted,**" that is, legally earmarked for a particular purpose (like unspent grant funds, for example) or "**unrestricted**," which can be spent for any purpose as directed by the Board of Supervisors. In the case of Napa County, most General Fund designations have historically been unrestricted.

Prior to Fiscal Year 2005-06, the County's practice was to maintain General Reserves that were roughly equal to 3% of General Fund appropriations, not including the General Fund's budgeted Operating Contingency. Starting with FY2005-06, the Board of Supervisors adopted Budget Policies that called for maintaining General Reserves that were equal to at least 5% of General Fund appropriations, not including the budgeted Operating Contingency. In FY2008-09, in response to the so-called "Great Recession," the Board approved the County's Fiscal Contingency Plan that, among other things, called for maintaining a minimum of 10% of General Fund appropriations in General Reserves and unrestricted designations combined. In FY2009-10, the Board of Supervisors created a Designation for Fiscal Uncertainties to be used specifically as a resource to deal with the impact of economic downturns or emergencies. Finally, in FY2011-12, the Board approved a Strategic Financial Plan that included the following provisions regarding General Fund reserves:

- Maintain a General Reserves balance of 10% of General Fund appropriations, not including the appropriation for Contingency and any budgeted transfer to the Accumulated Capital Outlay Fund. General Reserves are to be maintained at this level at all times, except in the case of a dire fiscal emergency.

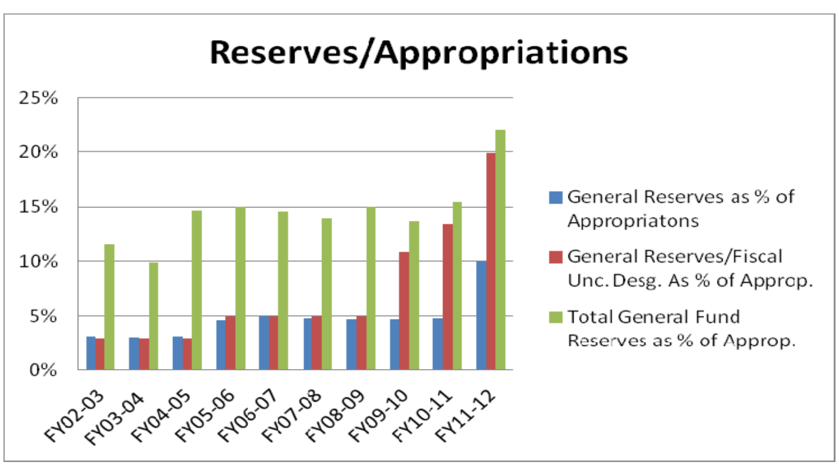
- Strive to maintain a Designation for Fiscal Uncertainties balance in the General Fund of 10% of General Fund appropriations, not including the appropriation for Contingency and any transfer to the Accumulated Capital Outlay Fund. In times of fiscal distress, these funds can be used to help balance the General Fund budget as part of a plan to achieve long-term structural balance. Any plan to achieve long-term structural balance should include a provision to replenish the Designation for Fiscal Uncertainties balance to the 10% level.

The following table shows the history of budgeted General Fund reserves since FY2002-03.



As can be seen, over the last ten years, General Fund reserves have grown from approximately $18.2 million to approximately $48.2 million, a 165% increase. It is noteworthy that General Fund reserves increased by almost 80% over the last four fiscal years, the period of the Great Recession and its aftermath – the steepest economic downturn in the United States since the Great Recession of the 1930s. In addition, from FY2009-10 to FY2011-12 the County was able to increase the combined amount of General Reserves and the Designation for Fiscal Uncertainties by 98%, to almost $44 million.

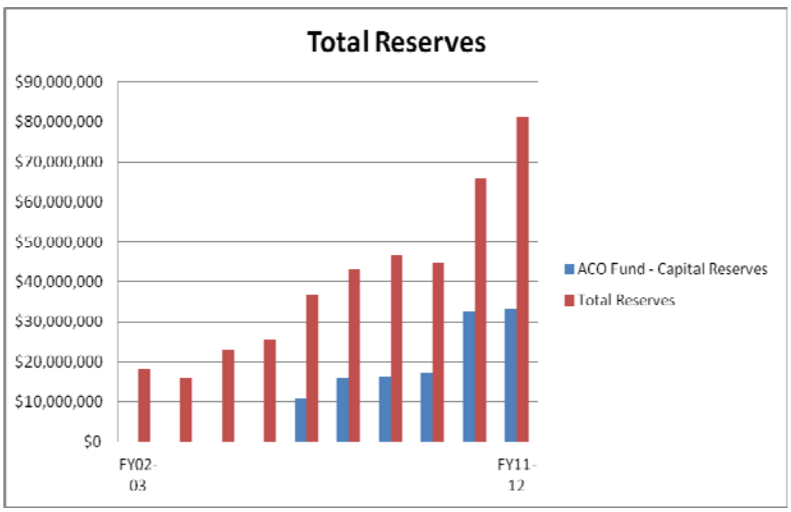
In each of the last 10 years, the County has also been able to meet the Board of Supervisors' goals regarding the General Fund reserve level as a percent of appropriations, as shown in the following table.



As can be seen, General Reserves increased from 3% of appropriations in FY2002-03 to 10% in FY2011-12 and General Reserves and the Designation for Fiscal Uncertainties combined increased from 11% in FY2009-10 to 20% in FY2011-12. Over the last 10 years, total General Fund reserves have grown from 12% of General Fund appropriations to 22%, an 83% increase.

Capital Reserves

Recognizing that the County was facing the need to invest in a number of major facility improvement projects (such as the redevelopment of the Health and Human Services campus and the construction of a new jail) and that borrowing money for this purpose could create a costly on-going expenditure obligation, in FY2006-07 the Board of Supervisor's created the Accumulated Capital Outlay (ACO) Fund and adopted a Budget Policy that called for placing in capital reserves any discretionary resources remaining after all budget year capital and operating costs and General Fund reserve requirements were met. The following table shows the history of the capital reserves included in the ACO Fund as well as the total reserves available in both the ACO and General Funds. The latter is important because, until ACO resources are actually obligated for a particular capital project, those monies can be used as additional General Fund reserves if necessary.



As can be seen, between FY2006-07 capital reserves in the ACO Fund grew from approximately $10.9 million to approximately $33.2 million, a 204% increase. This is due in large part to the receipt of almost $50 million in Excess ERAF revenue over this period. Excess ERAF revenue is new and volatile revenue source and its future is uncertain. For this reason, Board policy states that no more than $5 million a year from that source may be spent on on-going operations and a significant portion of Excess ERAF revenue was therefore transferred to the ACO Fund.

As the above table also shows, between FY2002-03 and FY2011-12 total General Fund and capital reserves increased from approximately $18.2 million to more than $81 million, a 347% increase.