Memorandum

CITY OF DALLAS

Date August 20, 2010

To Members of the Budget, Finance, & Audit Committee:
Jerry R. Allen, Chair; Ann Margolin, Vice Chair; Vonciel Jones Hill;
Delia D. Jasso; Ron Natinsky; and David A. Neumann

Subject FY 2010-11 Proposed Budget: Reserve Levels

The Budget, Finance, and Audit Committee will be briefed on the FY 2010-11 Proposed Budget Reserve Levels on Tuesday, August 24th. Attached is a copy of the briefing for your review.

Please let me know if additional information is needed.

Jeanne Chipperfield

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Chief Financial Officer

C: Honorable Mayor & Members of the City Council Ryan S. Evans, First Assistant City Manager
Mary K. Suhm, City Manager A.C. Gonzalez, Assistant City Manager
Deborah Watkins, City Secretary Jill A. Jordan, P.E., Assistant City Manager
Tom Perkins, City Attorney Forest E. Turner, Assistant City Manager
Craig Kinton, City Auditor

FY 2010-11 Proposed Budget: Reserve Levels

Budget, Finance & Audit Committee

August 24, 2010

Purpose

- To provide information on the General Fund Reserves, including:
  - Background
  - Reserve Requirements of Financial Management Performance Criteria (FMPC)
    - Emergency Reserve
    - Contingency Reserve
    - Combined Reserve Levels
    - Risk Reserve
  - Fund Balance Considerations

Background – FMPC

- FMPC initially adopted by the City Council in 1978 to set standards and to guide decision making
- Dallas was one of the first cities in the U.S. to develop criteria, and the criteria was subsequently used by others to model their own
- Rating agencies highly regard the Dallas FMPC
- FMPC includes 52 criteria in 5 categories
  - Operating Programs
  - Capital and Debt Management
  - Accounting, Auditing and Financial Planning
  - Cash Management
  - Grants and Trusts
- Dallas Water Utilities has its own set of 13 criteria
- FMPC is updated/evaluated for compliance during budget preparation and approval process, at year end, and for each debt issuance
- Council periodically reviews and updates the criteria
  - Last update was approved by Council on September 24, 2008

Background – Fund Balance

- Fund Balance reported annually in the City's Comprehensive Annual Financial Report (CAFR)
- Fund Balance
  - The difference between a fund's assets and liabilities; the fund balance is adjusted annually by the difference between revenues and expenditures
  - Is further divided into 3 categories:
    1. <u>Reservations</u> – those amounts of the fund balance that are not available for appropriation because they are set aside for a specific future use
       - Includes encumbrances and inventory purchases
    2. <u>Designations</u> – allocation of the fund balance which indicates management's tentative plans for the future utilization of financial resources
       - Includes Contingency, Risk, Emergency reserves
    3. <u>Undesignated, Unreserved Fund Balance</u> – remaining fund balance after Reservations and Designations are deducted from the total Fund Balance

FMPC Reserve Requirements

- Emergency Reserve (FMPC #7)
  - Funds may be used to provide for temporary financing of unanticipated or unforeseen extraordinary needs of an emergency nature
  - Use of Emergency Reserve would require authorization by Council resolution
  - Any uses must be replenished in the next fiscal year
    - FY11 Proposed Emergency Reserve of $17,563,082 is funded from the FY10 Emergency Reserve projected ending balance

FMPC Reserve Requirements

- Contingency Reserve (FMPC #8)
  - Provides for unanticipated needs that arise during the fiscal year
    - Use of Contingency Reserve would require authorization by Council resolution
    - FMPC requires reserve to be established annually at 0.5% to 1.0% of General Fund expenditures
    - Requirements reviewed annually and may be funded with the carry forward of ending balance from the prior fiscal year
    - FY11 Proposed Contingency Reserve of $5,103,005 or 0.53% of General Fund expenditures
      - Funded from FY10 projected ending balance of $1,457,236 and FY11 appropriated transfer from General Fund of $3,645,769

FMPC Reserve Requirements

- Combined Reserve Levels (FMPC #9)
  - Requires the sum of the undesignated, unreserved fund balance + the Contingency Reserve + the Emergency Reserve to be no less than 5% of budgeted expenditures

FY11 Proposed Combined Reserve Levels	
Undesignated, unreserved fund balance	$36.9m
Contingency Reserve	$5.1m
Emergency Reserve	$17.6m
Combined Total	$59.6m
FY09-10 Proposed General Fund Expense	$965.5m
5% of General Fund expense – Minimum Requirement	$48.3m
Over/(Under) Reserve Requirement	$11.3m
% General Fund Expense	6.2%

FMPC Reserve Requirements

FMPC #9 History	FY07 Actual	FY08 Actual	FY09 Actual	FY10 Budget	FY10 Estimate	FY11 Proposed
Undesignated, Unreserved Fund Balance	$44.9m	$49.1m	$47.3m	$36.6m	$36.9m	$36.9m
Contingency Reserve	$3.8m	$3.2m	$4.9m	$5.1m	$1.5m	$5.1m
Emergency Reserve	$18.3m	$17.6m	$17.6m	$17.6m	$17.6m	$17.6m
Total	$67.0m	$69.9m	$69.8m	$59.3m	$56.0m	$59.6m
General Fund Operating Expenditures	$1,007.0m	$1,032.4m	$1,037.6m	$1,018.4m	$1,016.2m	$965.5m
% of GF Expenses	6.7%	6.8%	6.7%	5.8%	5.5%	6.2%

FMPC Reserve Requirements

- Risk Reserve (FMPC #10)
  - Required to be maintained at a level, which, together with purchased insurance policies, adequately protects the City's assets against loss
  - FY11 proposed reserve funded at $1,250,00 using the FY10 projected ending balance

Fund Balance Considerations

- Bond rating agencies consider fund balance as a percent of expenditures as part of their analysis in determining a rating

- On a percentage basis, Dallas' fund balance is lower than other cities that are also highly rated at Aa1

- In its March 2009 ratings report, Moody's Investors Service included the following commentary regarding the City's fund balance

   "Moody's considers the diminishment of the general fund reserves to have weakened the city's financial flexibility and the negative outlook reflects our concerns regarding creditworthiness over the medium term."