



AGENDA

MEETING OF THE
FINANCE COMMITTEE
OF THE
SANTA BARBARA METROPOLITAN TRANSIT DISTRICT
A PUBLIC AGENCY
TUESDAY, JANUARY 19, 2016
9:00 A.M.
SANTA BARBARA MTD CONFERENCE ROOM
550 OLIVE STREET (UPSTAIRS), SANTA BARBARA, CA 93101

1. **CALL TO ORDER**
2. **ROLL CALL OF THE FINANCE COMMITTEE**
Bill Shelor, Committee Chair; Roger Aceves, Director; Dave Tabor, Director
3. **REPORT REGARDING POSTING OF AGENDA**
4. **APPROVAL OF PRIOR MINUTES (ATTACHMENT- ACTION MAY BE TAKEN)**
The Committee will be asked to waive the reading of and approve the draft minutes for the committee meeting of November 17, 2015.
5. **PUBLIC COMMENT**
Members of the public may address the Committee on items within the jurisdiction of the Committee that are not scheduled for public hearing. The time allotted per speaker will be at the discretion of the Committee Chair. **Please complete and deliver to the MTD Board Clerk, before the meeting is convened, a "Request to Speak" form including a description of the subject you wish to address.**
6. **CASH RESERVES POLICY-SECOND DRAFT (ATTACHMENT-ACTION MAY BE TAKEN)**
The Committee will be requested to review the second draft of the Cash Reserves Policy and, if found satisfactory, approve it for presentation to the full MTD Board for its consideration.
7. **OTHER**
8. **ADJOURNMENT**

AMERICANS WITH DISABILITIES ACT: If you need special assistance to participate in this meeting, please contact the MTD Administrative Office at 963-3364 at least **48 hours in advance** of the meeting to allow time for MTD to attempt a reasonable accommodation.



MINUTES

MEETING OF THE
FINANCE COMMITTEE
OF THE
SANTA BARBARA METROPOLITAN TRANSIT DISTRICT
A PUBLIC AGENCY
TUESDAY, NOVEMBER 17, 2015
9:00 A.M.
SANTA BARBARA MTD CONFERENCE ROOM (UPSTAIRS)
550 OLIVE STREET, SANTA BARBARA, CA 93101

1. **CALL TO ORDER**
Director Aceves called the meeting to order at 9:01 a.m.
 2. **ROLL CALL OF THE FINANCE COMMITTEE**
Director Aceves reported that all members were present with the exception of Committee Chair Shelor who was expected to arrive shortly.
 3. **REPORT REGARDING POSTING OF THE AGENDA**
Lilly Gomez, Administrative Assistant, reported that the agenda was posted on November 13, 2015 at MTD's Administrative Office, mailed and emailed to those on the agenda list, and posted on MTD's website.
 4. **APPROVAL OF PRIOR MINUTES (ATTACHMENT- ACTION MAY BE TAKEN)**
Director Tabor moved to waive the reading of and approve the draft minutes for the meeting of September 22, 2015. Director Aceves seconded the motion. The motion passed unanimously.
- COMMITTEE CHAIR SHELOR JOINED THE MEETING AT 9:04 A.M.***
5. **PUBLIC COMMENT**
None was made.
 6. **DIRECTORS AND OFFICERS (D&O) AND FIDUCIARY LIABILITY INSURANCE (ACTION MAY BE TAKEN)**
The Finance Committee discussed D&O, and supported staffs recommendation. The Finance Committee recommended staff forward to the full board.
 7. **DISCUSSION REGARDING DRAFT FINANCIAL STATEMENTS FOR FISCAL YEAR 2014-15 (ATTACHMENT-INFORMATIONAL)**
A representative of McGowan Guntermann updated the Committee of the District's draft Financial Statements for fiscal year 2014-15.
 8. **DRAFT CASH RESERVES POLICY (ATTACHMENT-ACTION MAY BE TAKEN)**
The Committee reviewed the first draft of the Cash Reserves Policy and provided comments and direction to staff.
 7. **OTHER**
No other items were discussed.
 8. **ADJOURNMENT**
The meeting was adjourned at 9:30 a.m.



FINANCE COMMITTEE REPORT

MEETING DATE: JANUARY 19, 2016 **AGENDA ITEM #:** 6

TYPE: ACTION

PREPARED BY: BRAD DAVIS _____
Signature

REVIEWED BY: GENERAL MANAGER _____
Signature

SUBJECT: **Cash Reserves Policy – Second Draft**

RECOMMENDATION:

The Committee will be requested to review the second draft of the Cash Reserves Policy and, if found satisfactory, approve it for presentation to the full MTD Board for its consideration.

DISCUSSION:

Background

The Finance Committee was presented with the first draft of the Cash Reserves Policy at its meeting on November 17, 2015. At that time, staff reported that the target funding level for the Capital Reserve Fund was based on the District's depreciation expense. Staff further indicated that it believed a more accurate methodology would take into account the District's anticipated future capital expenditures. The Committee concurred with the assessment and directed staff to modify the capital reserve determination process and bring the revised Policy back to the Committee. The revised Policy and staff report from that previous meeting are attached.

Capital Reserve Fund

Staff reviewed the capital reserve policies of other public agencies and, while they differed substantially, it was concluded that those based on the unfunded portion of the near-term capital plans were most appropriate. The revised Capital Reserve Fund target level in the second draft Policy now takes into account the District's five-year capital plan. Specifically, the reserve target amount is set as the sum of the unfunded portion of 100% of the capital plan for the current budget year; plus 80% of the unfunded balance of the Capital Plan for the subsequent fiscal year; plus 60%, 40%, and 20%, respectively, of the next three fiscal year unfunded capital expenditures. For purpose of the Policy, the unfunded portion of the capital budget is defined as the shortfall in capital revenue after taking into account revenue that has previously been accumulated or approved, or is reasonably expected to be received.

Other Draft Policy Modifications

There were a number of other refinements to the Cash Reserve Policy second draft. Most of these are minor and meant to add further clarity. Listed below are two of more consequence:

- The Appropriated Reserve was modified to include minor emergencies. The impetus for this addition were the emergency services required for the recent shop roof damage resulting from the El Nino rains. This type of incident was not of the magnitude required for use of the Emergency Reserve fund nor did it fit clearly within the use of other funds.
- The Policy states that the reserve funds are presented in order of priority. Wording was added to *Section III - Funding* clarifying the replenishment of the reserve balances based upon this priority. For instance, if the Working Capital Reserve fund falls below its target level, funds from lower priority reserves will automatically be shifted to the Working Capital Reserve.

If the Finance Committee finds the second draft acceptable, including any further changes that are decided upon at the meeting, staff requests that the Cash Reserves Policy be taken to the full Board for consideration at its next meeting this January 26.

ATTACHMENTS:

1. Santa Barbara Metropolitan Transit District – Cash Reserves Policy
2. Staff Report Finance Committee - Cash Reserves Policy (11/17/2015)

Santa Barbara Metropolitan Transit District Cash Reserves Policy

Effective Date: January 26, 2016

I. Purpose

The establishment of cash reserves is based upon prudent financial management. A reserve policy will greatly increase the District's ability to maintain continued fiscal health and minimize interruptions in transit service in the event of economic disruptions, natural disasters, major funding losses, and significant risk-related outlays. Additionally, the funding of reserves provides for the replacement or addition of District capital assets.

This Policy covers the type and purpose of the cash reserves funds to be established, the process for determining the target reserve amount, the authority for using accumulated reserves, and the means for funding the reserves.

II. Reserve Funds

The following cash reserve funds shall be established by the District which shall be prioritized and funded to the target dollar sum in the order in which they are presented below.

A. Working Capital Reserve

Basis – A working capital reserve shall be funded to meet the normal cash flow requirements of the District to avoid disruption of operating activities. Working capital is required for:

- Regular short-term cash flow requirements to accommodate operating costs.
- Receipt of federal operating assistance late or in the following fiscal year.
- Upfront outlays for capital acquisitions that are funded on a reimbursement basis.

Target – The amount of the reserve shall be equal to the FTA 5307 formula operating funds budgeted for the fiscal year which is considered sufficient to meet all working capital needs.

Usage – Use of working capital reserves shall be at the discretion of the General Manager or his/her designee to meet cash flow needs as they arise.

B. Appropriated Reserve

Basis – An appropriated reserve shall be used as a contingency fund in the event of unanticipated, high-priority operating or capital needs, including minor emergencies, that may arise during the fiscal year. Examples include economic downturns affecting revenue, volatile energy costs, storm-related damage, and significant self-insurance outlays.

Target – The amount of the reserve shall be 2% of the approved operating budget.

Usage – Use of the appropriated reserve shall require approval of the Board of Directors.

C. Emergency Reserve

Basis – An emergency reserve shall be used to fund extraordinary losses resulting from natural or man-made disasters, major funding losses or suspensions, and other similar circumstances.

Target – The amount of the reserve shall be 10% of the approved operating budget.

Usage – Use of the emergency reserve shall require approval by the Board of Directors. Such authority is granted to the General Manager when circumstances require the immediate commitment of resources to preserve life or property, or to protect public health, welfare, and safety

D. Capital Reserve

Basis – A capital reserve shall be funded for the purpose of future capital expenditures for the replacement, improvement, or expansion of District capital assets including but not limited to the revenue vehicle fleet, passenger facilities, and operating facilities.

Target – The amount of the capital reserve shall be based upon the unfunded portion¹ of the five-year capital plan in the following manner:

- 100% of the capital budget for the current fiscal year (year one); plus,
- 80% of the capital budget for the subsequent fiscal (year two); plus,
- 60% of the capital budget for year three; plus,
- 40% of the capital budget for year four; plus,
- 20% of the capital budget for year five.

¹ The unfunded portion of the capital budget is defined as the difference between the capital budget less the capital funding that is or is reasonably expected to be secured for that year.

Additional capital sinking funds may be established by the Board of Directors as needed for projects that require a substantial capital outlay (e.g., a large bus purchase or new facility).

Usage – Use of the capital reserve shall require approval of the Board of Directors. Such authority is granted to the General Manager when circumstances require the immediate commitment of resources provided that such use is consistent with the priorities established by the Board of Directors as part of the annual budget process.

III. Funding

The funding of reserves shall be from the District's Unrestricted Net Position. In the event that a reserve fund balance falls below the target level, to the extent feasible, it shall be replenished to the target level by shifting funds from the lowest priority reserve fund with a fund balance. Increasingly higher priority reserve funds shall be used for such replenishment as necessary.

IV. Reporting

Staff shall report to the Board of Directors on the status of the cash reserve funds as part of the annual budget process. If reserve balances are not meeting the targets established in this policy, staff shall develop a plan for moving towards the authorized cash reserve levels.

V. Modifications

This Cash Reserves Policy may be amended at any time by approval of the Board of Directors.



FINANCE COMMITTEE REPORT

MEETING DATE: NOVEMBER 17, 2015 **AGENDA ITEM #:** 8

TYPE: ACTION

PREPARED BY: BRAD DAVIS

Signature

REVIEWED BY: GENERAL MANAGER

Signature

SUBJECT: **Draft Cash Reserves Policy**

RECOMMENDATION:

The Committee will be requested to provide comments and direction on the attached first draft of the proposed Cash Reserves Policy.

DISCUSSION:

Background

The Finance Committee had previously indicated to staff the need for the development of a reserve fund policy. While the District considers a portion of its cash and cash equivalents as reserves—and indicated as such on the Cash Report provided to the Board of Directors—there is currently no formal policy that establishes specific reserve types and funding levels. Staff provided the Finance Committee with a suggested approach to developing a cash reserve policy at its August 31, 2015, meeting. Based on feedback from the Committee at that time, a draft Cash Reserves Policy has been developed and is attached for your consideration.

Purpose

The establishment and funding of cash reserves is based upon prudent financial management. A reserve policy will greatly increase the District's ability to maintain continued fiscal health and minimize interruptions in transit service in the event of economic disruptions, natural disasters, major funding losses, and other significant unexpected occurrences. Additionally, reserves provide for the normal working capital needs of the District and as well as the replacement and addition of its capital assets. As described by the California Special Districts Association:

“Reserves are the foundation of the sustainable delivery of core services. Through prudent reserves, special districts offer taxpayers and ratepayers significant benefits including savings to balance budgets, emergency preparedness, stable rates, well maintained infrastructure, and investment in the future.”¹

¹ California Special Districts Association, *Special District Reserve Guidelines-Second Edition* (2013), 6.

Description

As presented to the Committee last August 31, staff is recommending the formation of four separate cash reserve funds. The attached Cash Reserves Policy includes detailed information on the reserves. A summary of key information is provided in the below table.

RESERVE TYPE	PURPOSE OF RESERVE	TARGET RESERVE LEVEL
Working Capital	Cash flow requirements of the District to avoid disruption of ongoing operating activities	Prior Year FTA Operating Assistance
Appropriated	Unbudgeted important operating or capital needs arising during the course of the fiscal year	2% of Operating Budget
Emergency	Extraordinary losses from natural disasters and major funding eliminations or suspensions	10% of Operating Budget
Capital	Future capital expenditures for replacement, improvement, or expansion of capital assets	Average of depreciation expense for preceding 3 years plus 10%

Funding

The funding of cash reserves would be provided from the District's cash balances that are not specifically dedicated to other purposes by statute, grant, contract, or direction of the Board. Because of the nature of fund accounting, the source of reserve funds is represented by the District's unrestricted net assets—which are reported on the Statement of Net Assets (i.e., the balance sheet). At the end of FY14/15, the District carried an unrestricted net assets balance of \$10,293,617. Changes in the balance are for the most part determined by the operating surplus or deficit for the year. The tables below show the projected operating budget over the next five years and its effect on the unrestricted net assets balance and by extension the ability of the District to fund the recommended cash reserves.

Operating Budget Projection

	FY 2015-16	FY 2016-17	FY 2017-18	FY 2018-19	FY 2019-20
Operating Revenues	\$24,902,995	\$25,134,578	\$25,556,144	\$25,989,438	\$26,448,139
Operating Expenditures	25,122,302	25,955,860	26,891,242	27,803,663	28,827,048
Budget Surplus/(Deficit)	<u>(\$219,307)</u>	<u>(\$821,282)</u>	<u>(\$1,335,099)</u>	<u>(\$1,814,225)</u>	<u>(\$2,378,909)</u>

Change in Unrestricted Net Assets

	FY 2015-16	FY 2016-17	FY 2017-18	FY 2018-19	FY 2019-20
Start of Year Unrestricted Net Assets	\$10,293,617	\$10,074,310	\$9,253,028	\$7,917,929	\$6,103,705
Budget Surplus/(Deficit)	(219,307)	(821,282)	(1,335,099)	(1,814,225)	(2,378,909)
End of Year Unrestricted Net Assets	<u>\$10,074,310</u>	<u>\$9,253,028</u>	<u>\$7,917,929</u>	<u>\$6,103,705</u>	<u>\$3,724,796</u>

As is the practice of the District, the five-year budget projection is developed using conservative estimates. With recent and anticipated future trends, this leads to increasing budget deficits. It should be noted that the margin of error increases with each succeeding year. As a result, only the first two years should be considered with some degree of confidence. Nonetheless, the numbers do indicate a situation that will likely affect the ability of the District to fund reserves in the future.

The first table below shows the cash reserves that meet the calculated target funding levels. The second table indicates what the actual cash reserves would be taking into account the projected deficits. The final line represents the shortfall in meeting the reserve levels for each year. The projection concludes that the level of restricted net assets will support the full funding of proposed operating-related cash reserves for this and the following fiscal year. Thereafter, projections show a growing gap between the targeted and actual reserve funding levels.

Targeted Reserve Balances

RESERVE FUNDS	FY 2015-16	FY 2016-17	FY 2017-18	FY 2018-19	FY 2019-20
Working Capital	\$4,943,999	\$4,943,999	\$4,943,999	\$4,943,999	\$4,943,999
Emergency	2,512,230	2,595,586	2,689,124	2,780,366	2,882,705
Appropriated	502,446	519,117	537,825	556,073	576,541
Total Reserves Target Balance	\$7,958,675	\$8,058,702	\$8,170,948	\$8,280,439	\$8,403,245

Projected Reserve Balances

RESERVE FUNDS	FY 2015-16	FY 2016-17	FY 2017-18	FY 2018-19	FY 2019-20
Working Capital	\$4,943,999	\$4,943,999	\$4,943,999	\$4,943,999	\$4,001,083
Emergency	2,512,230	2,595,586	2,689,124	1,381,337	0
Appropriated	502,446	519,117	441,967	0	0
Total Reserves Projected Balance	\$7,958,675	\$8,058,702	\$8,075,090	\$6,325,336	\$4,001,083
Total Targeted Reserves Shortfall	\$0	\$0	\$95,858	\$1,955,102	\$4,402,161

The capital reserve fund, also referred to as a sinking fund, is not addressed in the above discussions because the capital budget is generally more complex and filled with uncertainty than the operating budget. Many of the funding sources are discretionary programs that are irregular in frequency and amount. Capital acquisitions also vary considerably by year and amount. At this point, staff is recommending the use of a simple but common method for determining a capital reserve level based on the cost of replacing equipment as measured by the District’s depreciation expense. Staff will come back in the future with a more comprehensive methodology that will more closely represent an accurate reserve level.

To address the means of maintaining adequate cash reserves requires the same analysis necessary for consideration of the options available for confronting the projected operating deficits. It necessarily involves key policy decisions concerning such matters as service levels and fares structures. Such consideration is beyond the scope and purpose of this report.