

CITY OF SANTA BARBARA WATERFRONT DEPARTMENT

MEMORANDUM

Date: July 19, 2012
To: Harbor Commission
From: Scott Riedman, Waterfront Director
Subject: **Waterfront Department Capital Reserve Policy**

RECOMMENDATION: That Harbor Commission:

- A. Review Waterfront Department reserve policies in general, and particularly as they pertain to the Reserve for Capital / Harbor Preservation Fund; and
- B. Make a finding that current Waterfront Reserve for Capital / Harbor Preservation Fund policies are adequate for the Waterfront Department Enterprise Fund and forward that finding to the City's Finance Department.

BACKGROUND:

In 1995, Council Resolution 95-157 established reserve policies for the General Fund and Enterprise Funds. From that time through Fiscal Year 2004, General Fund reserves were fully funded and excess funds were used to fund capital projects. In Fiscal Year 2005, General Fund reserves fell below policy minimums and have remained below policy minimums for the past seven years. Waterfront Department reserves remained in compliance with policy minimums throughout this period.

As a result of the General Fund reserve shortfall, the City Council and Finance Committee directed staff to look into improving existing policies and guidelines regarding use and replenishment of General Fund reserves. Additionally, the Finance Department requested that Waterfront staff evaluate its current Capital Reserve / Harbor Preservation Fund policy with the Harbor Commission and, if necessary, bring recommended changes to City Council (Attachment 1).

Harbor Commissioners will recall that a brief description of Waterfront reserves was attached to the March budget presentation. Reserve policies for the General Fund and Enterprise Funds were established by Council Resolution. In essence, resolutions required the establishment of four reserve categories as follows:

1. **Reserve for Capital** – For Enterprise Funds, the Reserve for Capital should either be 5% of net fixed assets or the average of capital funded from operating revenues in the previous three years. In the Waterfront Fund, the Harbor Preservation Fund (HPF) serves as the Reserve for Capital and is required to be maintained at a minimum level of \$2 million. Five percent of the Department's net fixed assets is \$1,118,000 and the average capital funded from the Waterfront operating fund for three previous years is

\$928,000, so the \$2 million HPF requirement exceeds both criteria. As of June 30, 2011, the Waterfront Department had approximately \$3.7 million in the HPF Reserve for Capital (Attachment 2).

2. **Reserve for Emergencies** – As the name implies, this reserve provides to respond to emergencies, such as natural disasters, during which the City would face increased costs immediately to respond to the emergency and also potentially see a decline in revenues. The reserve requirement is equal to 15% of the adopted operating budget. As of June 30, 2011, the Waterfront Department had approximately \$1.4 million in this reserve.
3. **Reserve for Future Years' Budgets** – This reserve is intended to provide funds for meeting ongoing costs and minimizing any disruption of services during periods of declines in operating revenues typically associated with economic downturns. The reserve requirement is equal to 10% of the adopted operating budget. As of June 30, 2011, the Waterfront Department had approximately \$900,000 in this reserve.
4. **Appropriated Reserve** – This reserve establishes an appropriated (i.e., budgeted) item that serves as a cushion for unexpected costs which may arise during a budget year. The policy requires that the Appropriated Reserve for the General Fund and each of the Enterprise Funds is an amount equal to 0.5% percent of the operating budget. The Waterfront operating fund is \$11,454,451 for FY 2013, so the \$100,000 in appropriated reserve exceeds the 0.5% requirement of \$57,272.

Other Waterfront Reserves

The Waterfront Department also maintains \$1,393,260 in reserve to fund its senior debt obligation, Certificates of Participation (COPS), for approximately one year if necessary.

DISCUSSION:

Nature and Volatility of Revenues

The General Fund's primary revenues are derived from property taxes and consumer spending including sales tax, Transient Occupancy Tax, (also known as hotel bed tax), and utility users' tax, and therefore are susceptible to economic fluctuations.

The Waterfront Fund does not receive tax revenue and derives its revenues from users' fees such as marina and parking fees and commercial property rentals. These assets are in limited supply and high demand and not as susceptible to economic fluctuations as the General Fund tax base.

Susceptibility to Natural Disasters

The attached Finance Committee Agenda Report states that Santa Barbara is vulnerable to floods, earthquakes, fires and tsunamis, and that potential loss of revenues must be considered in the event of such disasters. The Harbor Preservation

Fund can be used as a disaster fund, along with the Reserve for Emergencies, giving Waterfront additional flexibility in responding to disasters.

In considering the potential damage from natural disasters it is important to consider the City's insurance coverage in addition to disaster reserves. The City's insurance covers losses due to liability, fire, flood, wave wash, tsunami and earthquake. Additionally, Waterfront is covered for loss of revenues. For example, if a storm damaged the marinas and/or the Wharf, insurance will pay to repair the damage and compensate for the loss of revenue while the tenants are displaced.

An example is the November 1998 Stearns Wharf fire which consumed 20% of the Wharf including Moby Dick Restaurant, Santa Barbara Shellfish Company, Mike's Bait & Tackle, and the Passenger Loading Ramp serving Captain Don's Cruises and Blue Edge Parasailing. The fire damage was \$11,036,897 plus loss of rental income of \$445,341 for a total of \$11,482,238. The Department was responsible for the \$250,000 deductible and \$530,595 in facility upgrades (primarily upgrading wood piles and understructure to steel piles and pile caps supporting a concrete pad). Insurance paid \$10,701,643 (93%) and the Department paid \$780,595 (7%).

Staff Recommendation

The Harbor Commission Budget Committee (Commissioners Cramer, Kelly and Sloan) met with staff at a publicly-noticed meeting on June 5, 2012 to discuss the Department's Capital Reserves and related issues. The Budget Committee concurred with staff that the \$2 million minimum on the HPF is adequate for the Waterfront Department needs at this time and recommended that the current Waterfront Capital Fund / Harbor Preservation Fund policies remain unchanged.

Attachments 1: Finance Committee Agenda Report
2: Waterfront Reserves 6/30/2011

Prepared by: Scott Riedman, Waterfront Director