WHATCOM COUNTY
EXECUTIVE'S OFFICE
County Courthouse
311 Grand Ave. Suite #108
Bellingham, WA 98225

Satpal Singh Sidhu
County Executive

MEMORANDUM

TO:	Whatcom County Council
THROUGH:	Satpal Sidhu, County Executive
FROM:	Aly Pennucci, Deputy Executive Kayla Schott-Bresler, Deputy Executive
CC:	Brad Bennett, Finance Manager Randy Rydel, Finance Director
RE:	2025-2026 Budget Recommendations – GF Fund Balance
DATE:	October 28, 2024

In response to councilmember comments during the October 8, 2025, Committee of the Whole meeting regarding the projected ending fund balance in the County's General Fund (GF) in 2026, this memo:

1. Provides background on County debt policies and historic fund balance levels;
2. Outlines pending liabilities that inform the recommendation to maintain a greater than policy projected ending fund balance in GF for the next biennium; and
3. Offers policy options for the Council's consideration.

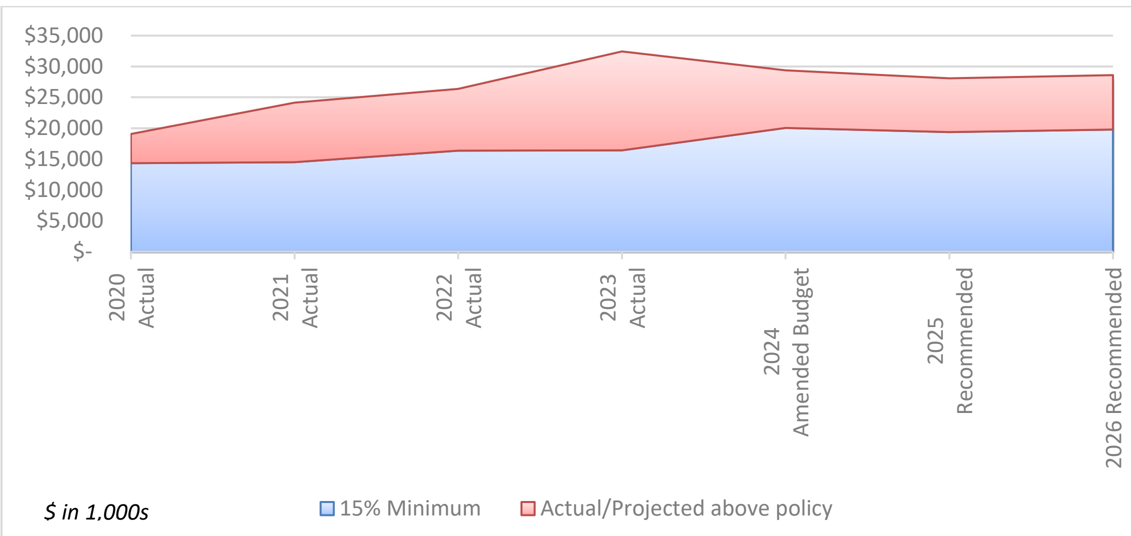
Background

The appropriate level of fund balance in the GF varies depending on a number of factors, such as: revenue predictability and expenditure volatility; vulnerability to natural disasters or immediate expenses; the potential drain on general fund resources from other funds and the availability of resources in other funds; the potential impact on the bond rating and borrowing costs; and funds that are already committed or assigned for specific purposes.

The Government Finance Officers Association (GFOA) recommends, at minimum, general purpose governments, regardless of size, "maintain unrestricted budgetary fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures" noting that a government's particular situation may require a level of unrestricted fund balance in excess of this recommendation depending on circumstances.

The Whatcom County Debt Policy requires that “[c]onsistent with maintenance of its current “AA” or “Aa” general obligation rating, the County shall maintain an undesignated balance in its general fund (or any related reserve fund that may be created for this purpose), **at least** equal to 15% of its previous year’s general fund actual revenue” *[emphasis added]*.[1] This is equivalent to less than two months of operating (15% = 1.8 months).

The Executive’s 2025-2026 Recommended Biennial Budget includes a projected ending fund balance for the General Fund (GF) at the end of 2026 of about $28 million or 22% of the prior year’s revenues. This is consistent with past practices; historically, the County has maintained closer to a 20-25% fund balance (see chart below that shows fund balances over the last five years). **It is important to note that the 22% projected fund balance assumes that the County will lapse/underspend (e.g., not spend) 5% of budgeted expenses annually. If departments spend 100% of their budget, the fund balance at the end of 2026 would drop to 16%.**



Maintaining more than 15% fund balance is particularly important at this time when the County is (1) preparing to issue significant debt to finance major capital projects; (2) facing a revenue landscape that is increasing complex and volatile (e.g., fluctuations in sales tax revenues that impacts both GF and other funds); and (3) vulnerability to other expenses that are not yet certain enough to budget to a department but may become a reality in the 2025-2026 biennium.

[1] This policy is established by the County’s Finance Committee, that is established in accordance with RCW 36.48.070, consisting of the Treasurer, the Auditor, and the Chair of the County Council. This Committee is responsible for approving the debt policies. The County has not established policies related to the GF fund balance beyond those of the Finance Committee. Best practices related to fund balances and risk reserves is evolving; updated and more nuanced fund balance policies is something Whatcom County could consider in the future.

Pending Liabilities

As discussed previously, the Executive has identified potential expenses that could occur in the next biennium but determined it is premature to budget specific expenses for departments until there is more certainty on total costs and timing of those expenses. Budgeting now would give departments spending authority prematurely, impact labor negotiations, and could impact the County's ability to seek state and federal funding. These potential expenses should be considered in determining the amount of fund balance to target in the GF.

The Executive's Recommended Budget includes a projected ending fund balance in 2026 of 22%, or about $8.8 million above the minimum required by the County's debt policy.[2] There are several potential expenses that could occur in 2025 and 2026 that those funds would be needed for, such as:

- Increasing labor costs: all of the County labor contracts are open for negotiations in 2026; due to new caseload standards, labor costs for the Public Defender's Office may increase significantly; in addition, the County is experiencing increasing personnel related expenses for things like workers compensation, insurance, equipment etc. *Estimated costs/recommended reserve: $3.5-5 million (ongoing).*
- Environmental cleanup issues: including the GF portion of the costs to remove and remediate a tank at the PW Maintenance Shop. *Estimated costs/recommended reserve $500k-1 million (one-time).*
- Facilities improvements: this includes work to expand and upgrade County courtroom and the associated relocation of administrative services; the County is seeking reimbursement for the costs associated with water adjudication work, however, expenses may exceed those reimbursements. In addition, given the growth in County employees and new buildings, facilities maintenance and tenant improvement costs are increasing. *Recommended reserve: $500k-$1M (one-time).*
- Jail Health Costs: The County's contract with Northwest Regional Council and Ideal Options will expire in 2025 and the administration is anticipating a cost increase in these services. The recommended budget provides an additional $300,000 for this purpose in 2025, however, the costs could exceed that estimate and additional funding will likely be needed in 2026. *Recommended reserve: $500k (potentially ongoing)*
- Tort increases: The recommended budget includes a $530k annual increase for the County's insurance premium amounts (established annually) as well some increase to pay small and large claim amounts related to our Tort liability. Tort costs have been steadily increasing and additional funding may be needed in 2026 for premiums or for settlements. *Recommended reserve: $500k-$1M (one-time)*

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[2] It is important to note that these are one-time resources and would drop to 15% if the lapse assumptions are not met. If used for ongoing needs (e.g., some of the pending liabilities are ongoing needs) the County will have to identify offsetting reductions or new revenues in the future to sustain those costs. Some of the pending liabilities are ongoing costs that will require ongoing reductions or new revenues before the 2027-2028 biennium.

- IT Reserve: The County's Mitel telecommunications system has reached the end-of-life point and needs to be replaced – Mitel will no longer provide hardware replacements after 2024 and will stop supporting the system in the next few years.[3] The IT division requested $1.2 million in the 2025-26 budget to replace this system prior to 2028. The Executive denied the ASR and asked the IT Division to research alternative systems (e.g., moving to a computer-based phone system using programs like Microsoft Teams or WebEx). Until that research is done and a policy choice can be made it is premature to budget for those expenses. However, given that the phone system is a primary communications channel for the public to access county services and the critical public safety services that rely on our telecommunications system, the Executive recommends maintaining a reserve to ensure resources are available should the system begin to fail before the end of the 2025-2026 biennium.

  In addition, there are several major technology projects underway, including replacement of the County's Enterprise Financial System and permitting systems. While the recommended budget includes resources for these initiatives, it is not uncommon for these types of projects to need additional funding to address issues that emerge closer to completion. *Recommended IT reserve: $1.5M-$2M (one time)*

In total, if all of the pending liabilities become realities in the 2025-2026 biennium, GF expenses could increase by $7-$10.5 million over the biennium.

Other potential liability: Behavioral Health Fund

In addition to the potential cost liabilities described above, the Executive learned very late in the budget process that the revenue and expense projections in the Behavioral Health Fund (BHF) are resulting in a structural imbalance in the fund that appears worse than previously understood. The Finance Department saw this in their final verification of fund balance numbers. This appears in part due to lower than projected sales tax revenue, spending from the fund in other departments, uncertainty and fluctuations in grant revenue, and use of fund balance in 2023 and 2024 for one-time uses (e.g. school contracts, crisis relief center). In response, the Executive rejected most ASRs for 2025-2026 that impact the BHF, some of which may be priorities in 2025-26 and can be accommodated through base budget adjustments. Health and Community Services has already identified some technical corrections in the BHF to mitigate this problem and is working to address the funding gaps from the rejected ASRs. The Executive will prepare and transmit technical corrections for discussion on November 6th and will work with the Department, BH Advisory Committee, and that Council to make further adjustments if needed over the next few months.

Policy Options

The Executive's Recommended Budget accounts for the pending liabilities by proposing a higher than required projected ending fund balance in the GF, assuming a 5% lapse in both years. This

[3] The IT Division is purchasing extra inventory in 2024 to ensure that the County has replacement parts on hand should they be needed in 2025-2026.

is consistent with past practices in Whatcom County. The Council could choose to create an appropriated reserve in the non-departmental budget or provide spending authority for specific purposes in individual departments. There are pros and cons to any approach; if the funds are not appropriated or are held in a non-departmental reserve, any proposal to move the funds to provide a department with spending authority for specific purposes would require approval from the Council. If instead the Council chose, for example, to increase the IT Division's budget for the phone replacement project, the spending authority would not require additional budget approval, though there may be other Council approvals necessary (e.g., for spending on a contract exceeding $40,000).

Given the complexity of this budget season and other ongoing work the Executive decided to delay implementation of a larger appropriated risk reserve until a future budget as the Finance Division noted that there are technical complexities in setting that up. In future budgets and as the Executive continues to improve the County's fiscal oversight work, there is an intent to review our fund balance policies and create an appropriated risk reserve.

Ultimately the Council could also choose to spend a portion of the fund balance on other things and risk the impact to our financing costs and other pending liabilities. Fund balances are one-time resources and would be a short-term solution that could exacerbate the longer-term stability of the GF; the Executive does not recommend this approach.