

## FINANCIAL POLICIES

*Originally Adopted by the City Council on September 15, 2014*

*Latest Revision on August 20, 2018*

### OPERATING BUDGET

The objective of the operating budget policy is to ensure the appropriate levels of City services at reasonable costs.

**Biennial Budget Document.** The budget should be a performance, financing and spending plan agreed to by the City Council, City Manager and Department Directors. It should contain information and data regarding expected revenues, expected expenditures and expected performance. The budget should be developed using a performance based, results oriented approach that incorporates line items, zero-based, programs, and priorities of governments.

- As a comprehensive business plan, the budget should provide the following critical elements recommended by the Government Finance Officers Association: public policies, financial plan, operations guide, and communications device.
- The City's budget presentation should display the City's service delivery/performance plan in a City Council/constituent-friendly format. Therefore, the City will use a program budgeting format to convey the policies for and purposes of City operations. The City will also prepare the line-item format materials for those who wish to review that information.

**Goals to Guide Preparation.** The City will prepare and annually refine written policies and goals to guide the preparation of performance, financing and spending plans for the City budget. Adopted budgets will comply with the adopted budget policies and City Council priorities.

**Long Range Forecast.** With each budget, the City will update expenditure and revenue projections for the next six years. Projections will include estimated operating costs for capital improvements that are included in the capital budget. This budget data will be presented to the City Council in a form that will facilitate budget decisions, based on a multi-year perspective. This forecast is intended to be an internal planning tool and shall be included in the biennial budget document and updated at least annually as part of the adopted budget process in the even years and the mid-biennial review in the odd years.

**Capital Projects.** Decision making for capital improvements will be coordinated with the operating budget to make effective use of the City's limited resources for operating and maintaining facilities.

**Balanced Budget.** The City will adopt a balanced budget for all funds. Balanced budget for operating funds means ongoing operating program costs do not exceed the amount of ongoing revenues to finance those costs. The ongoing revenue will be identified along with new program costs including impact from new capital projects. Any available carryover balance will only be used to offset one-time or non-recurring costs. Balanced budget for non-operating funds means total resources equal to or exceed total uses.

**Excess Cash Balances.** Cash balances in excess of the amount required to maintain General and Street Operations & Maintenance Fund reserves may be used to fund one-time or non-recurring costs.

**Department Director Responsibility.** All Department Directors will participate in the responsibility of meeting policy goals and ensuring long-term financial health. Under the City Manager's direction, Department Directors have primary responsibility for: formulating budget proposals in line with City Council priority and direction; and implementing those proposals once they are approved.

**Citizen Involvement.** Citizen involvement shall be encouraged in the budget decision making process through public hearings and study sessions.

**Nonprofit Organizations.** Funding decisions regarding nonprofit organizations shall be based on policy guidelines and priorities determined by the City Council and availability of funds.

**Budgetary Controls.** Legal budgetary control is established at the fund level, i.e., expenditures for a fund may not exceed the total appropriation amount. Any unexpended appropriation balances for annually budgeted funds lapse at the end of the year. Appropriations for other special purpose funds that are non-operating in nature are adopted on a "project-length" basis and, therefore, are carried forward from year to year without re-appropriation until authorized amounts are fully expended or the designated purpose of the fund has been accomplished.

**Quarterly Financial Reports.** The budget will be produced so that it can be directly compared to the actual results of the fiscal year and presented in a timely quarterly report. All budget amendments, both revenues and expenditures, will be noted in the quarterly financial report.

## **FUND BALANCE**

The objective of the fund balance policy is to provide adequate working capital for cash flow and contingency purposes.

**General Fund.** The General Fund ending fund balance reserves shall be 12% of the combined General and Street Operations & Maintenance Funds operating revenues. These reserves are as follows:

- *2% General Fund Contingency Reserves:* The purpose of this reserve is to accommodate unexpected operational changes, legislative impacts, or other economic events affecting the City's operations which could not have been reasonably anticipated at the time the original budget was prepared. The City Council will determine how the Contingency Reserves are spent.
- *5% General Fund Ending Fund Balance Reserves:* The purpose of this reserve is to provide financial stability, cash flow for operations and the assurance that the City will be able to respond to revenue shortfalls with fiscal strength.
- *5% Strategic Reserves:* The purpose of this reserve is to provide some fiscal means for the City to respond to potential adversities such as public emergencies, natural disasters or similarly major, unanticipated events.

**Enterprise Funds.** The City shall maintain a minimum fund balance in its enterprise funds equal to 33% of operating expenses (equivalent to 120 days of operating expenses due to the infrequent revenue stream from annual or bi-annual revenue receipt). This balance shall be maintained to ensure adequate maintenance reserves and cash flow. Additionally, the City shall maintain a capital fund balance equal to 1% of the original system cost, establish and maintain debt service reserves if required as a condition of future debt issuance, and fund system reinvestment annually through rates based on original cost depreciation using a phased in strategy to mitigate potential impacts on rate increases. Balances in excess of reserves may be utilized for capital projects.

**Internal Service Funds.** The City shall maintain a balance equivalent to the accumulated replacement reserves at year-end for those internal service funds that collect replacement reserves. Replacement reserves based on estimated replacement value will be established for fleet and equipment when the need will continue beyond the estimated useful life, regardless of whether the vehicle or equipment is acquired via

lease, gift, grant or purchase. An equal amount will be included in the service charges paid by the user department to the Fleet and Equipment Fund during the expected life of the asset.

The City shall maintain separate internal service funds to account for the activities of Fleet and Equipment, Property Management, Information Technology, and Risk Management. The City shall establish replacement reserves for information technology related equipment and property management related to facilities no later than year 2020.

**All Other Funds.** The appropriate balances shall be the amount needed to maintain positive cash balances throughout the year.

**Use of Fund Balances.** Fund balance is the cumulative years' excess or deficit of all revenues and expense. Available fund balances shall not be used for ongoing operating expenditures, unless a determination has been made that available balances are in excess of required guidelines and plans have been established to address any future operating budget shortfalls. Emphasis shall be placed on one-time uses that achieve future operating cost reductions and/or service level efficiencies.

**Timeline.** The timeline to achieve the target reserves is no later than December 31, 2016.

**Replenishing General Fund Balance.** The fund balance shall be replenished within one to two years depending on the reserve fund. The 2% General Fund Contingency Reserves and 5% General Fund Ending Fund Balance Reserves shall be replenished within one year while the 5% Strategic Reserves shall be replenished within 2 years. The sources for replenishment shall be via expenditure control, expenditure savings, one-time revenues and/or excess revenues.

## REVENUE

The objective of the revenues policy is to ensure that funding is derived from fair, equitable, defensible, and adequate resource base, while minimizing tax burdens.

**Revenue Estimates.** Revenues shall be estimated conservatively so as not to introduce regular shortfalls in individual revenue accounts. Revenue estimates shall not assume excess growth rates. Real growth that occurs will be recognized through budgetary adjustments only after it takes place. This practice imposes short term constraint on the level of public goods or services. However, in the event that revenues are less than expected, it minimizes the likelihood of severe cutback actions which may be profoundly disruptive to the goal of providing a consistent level of quality services.

**Revenue Diversification.** The City shall maintain a stable and diverse revenue system to shelter programs and services from short-term fluctuations in any single source of revenue. Services that have a city-wide benefit shall be financed by revenue sources generated from a broad source such as property tax, utility tax and sales tax. Services where the customer determines the use shall be financed by a combination of broad-based revenues as well as user fees and charges.

**Fees.** Fees shall be phased toward covering 100% of the cost of service delivery, unless such amount prevents an individual from obtaining an essential service. Fees or service charges should not be established to generate money in excess of the cost of providing service. Fees may be less than 100% if other factors (e.g. market forces, competitive position, etc.) need to be recognized.

**User Charges.** User charges for enterprise services such as the Surface Water management Fund shall be set at rates sufficient to finance all direct and indirect operating, capital, reserve/working capital, and debt service. Overhead expenses and general government services provided to the enterprise activities shall be included as indirect costs. Rates shall be set such that the enterprise fund maintains a positive cash position throughout the year and provide for sufficient reserves as determined by the fund balance policy.

**Use of One-Time/Unpredictable Revenues.** The City shall not utilize one-time revenues for recurring operating expenditures. One-time revenues include, but are not limited to: proceeds from the sale of land or surplus equipment, legal settlements, or revenue windfalls.

**Investment Income.** Investment income earned through the City's investment pool shall be budgeted based upon the allocation methodology, i.e. the projected average monthly balance of each participating fund.

**Grants.** Grant applications to fund new services/programs will be reviewed by the City as they become available, with due consideration being given to whether locally generated revenues will be required to support these programs when outside funding is no longer available.

## **EXPENDITURES**

The objective of the expenditure policy is to prioritize services, establish appropriate levels of service, and administer the resources to ensure that fiscal stability is attained and that services are delivered in an effective and efficient manner.

**Operating Funding Basis.** Operating expenditures shall be budgeted and controlled to not exceed operating revenues.

**Operating Deficits.** Immediate corrective action should be taken if at any time during a fiscal year expenditures are projected to be greater than projected revenues at year-end. Corrective actions could include, but are not limited to expenditure reductions, fee increases, or new revenues.

**Capital Asset.** Capitalization of assets shall occur with assets that have a useful life of at least two years following the date of acquisition with a historical or market value at time of acquisition equal to or greater than \$5,000. The threshold is applied to individual items rather than to groups of similar items unless the effect of doing so would eliminate a significant portion of total capital assets.

## **INTERFUND LOANS**

The objective of the interfund loans policy is to provide guidelines regarding the establishment, management and repayment of interfund loans.

**Definition.** Interfund loans are loans from one City fund to another City fund for a specific purpose with a requirement for repayment.

**Purpose.** Interfund loans should be considered temporary or short-term borrowing of cash and may be made for the following reasons: to offset timing differences in cash flow; to offset timing differences between expenditures and reimbursements, typically associated with grant fund. The use of interfund loans for other purposes should be carefully evaluated. Interfund loans should not be used to solve ongoing structural budget problems.

**Term.** The term of the interfund loan may continue over a period of more than one year, but must be “temporary” in the sense that no permanent diversion of the lending fund results from the failure to repay by the borrowing fund. Additionally, interfund loans should not hinder the accomplishment of any function or project for which the lending fund was established.

## **DEBT MANAGEMENT**

The objective of the debt management policy is to articulate the guiding principles for City debt issuance and management before consideration of specific actions. This policy set forth certain equally important objectives for the City and establishes overall parameters for responsibly issuing and administering the City's debt.

- Minimize debt service and issuance costs
- Maintain access to cost-effective borrowing
- Achieve and maintain highest practical credit rating
- Repay debt timely and in full
- Maintain full and complete financial disclosure and reporting
- Ensure compliance with state and federal laws and regulations

**Debt Capacity.** A long-term debt capacity will be completed on an annual basis as a means for ensuring that the City does not exceed the debt limits set by applicable laws and regulations.

**Bond Rating.** The City will seek to maintain, and if possible, improve its current bond rating(s) in order to minimize borrowing cost and preserve access to credit.

**Minimize Debt.** Whenever possible, the City shall identify alternative sources of funding and shall examine the availability of those sources in order to minimize the level of debt.

**New Issues and Refinancing.** New issues, and refinancing of existing debt, must be analyzed for compatibility within the City's overall financial planning. The review shall include, but is not limited to: cash flow analysis; potential for unexpected revenue changes; and the maintenance of the City's bond ratings. Annual debt service shall not produce an inordinate impact upon future operations.

- *Long-term Debt.* Long-term debt may be used to finance the acquisition or improvement of land, infrastructure, facilities, or equipment for which it is appropriate to spread costs over more than one budget year. Long-term debt may also be used to fund capitalized interest, cost of issuance, required reserves, any other financing-related costs that may be legally capitalized. Long-term debt shall not be used to fund City operating costs.
- *Short-term Debt.* Short-term debt will be considered as an interim source of funding in anticipation of long-term debt. Short-term debt may be issued for any purpose for which long-term debt may be issued, including capitalized interest and other financing-related costs. Short-term debt is also appropriate to address legitimate short-term cash flow requirements during a given fiscal year to fund operating costs of the City to provide necessary public services. The City will not engage in short-term borrowing solely for the purpose of generating investment returns.
- *Refunding.* Periodic reviews of outstanding debt will be undertaken to identify refunding opportunities. Refunding will be considered (within federal tax law constraints) when there is a net economic benefit of the refunding. Noneconomic refundings may be undertaken to achieve City objectives relating to changes in covenants, call provisions, operational flexibility, tax status, issuer, or the debt service profile, etc. When contemplating a refunding, the City shall have a minimum of 3.0% economic savings, as expressed on a net present value basis, as a benchmark to proceed with a refunding. The City may purchase its bonds in the open market for the purpose of retiring the obligation when the purchase is cost effective.

**Financing Period.** The City shall structure its debt issues so that the maturity of the debt service does not exceed the economic or useful life of the capital project to be financed.

**Method of Sale.** The City may use either a competitive bidding or negotiated process in the sale of debt due to market timing requirements, or a unique pledge of debt or debt structure.

**Bond Counsel.** The City will use the services of a legally certified and credible bond counsel in the preparation of all bond representations.

**Underwriter(s).** An underwriter(s) will be used for all debt issued in a negotiated or private placement sale method. The underwriter(s) is responsible for purchasing negotiated or private placement debt and reselling the debt to investors.

**Fiscal Agent.** A fiscal agent will be used to provide accurate and timely securities processing and timely payment to bondholders.

**Debt Administration.** The Assistant City Manager/Administrative Services shall maintain written procedures outlining required actions to ensure compliance with local, state, and federal regulations. Such procedures shall include: continuing disclosure, arbitrage rebate, and other requirements.

## **CAPITAL IMPROVEMENT**

The objective of the capital improvement policy is to forecast and match projected revenues and capital needs. Long range capital planning is an important management tool that strengthens the linkages between infrastructure needs and the financial capacity of the City.

**Capital Project Proposals.** Capital project proposals should include as complete, reliable, and attainable cost estimates as possible. Project cost estimates for the Capital Budget should be based upon a thorough analysis of the project and are expected to be as reliable as the level of detail known about the project. Project cost estimates for the 6-Year City Capital Improvement Plan will vary in reliability depending on whether they are to be undertaken in the first, second or 3<sup>rd</sup> biennium years of the plan.

- *Resource Plan.* Capital proposals should include a comprehensive resource plan. This plan should include the amount and type of resources required, and the funding and financing strategies to be employed. The specific fund and timing should be outlined. The plan should indicate resources needed to complete any given phase of a project in addition to the total project.
- *Expenditure Plan.* All proposals for the expenditure of capital funds shall be formulated and presented to the City Council within the framework of a general capital budget and, except in exceptional circumstances of an emergency nature, no consideration will be given to the commitment of any capital funds, including reserve funds, in isolation from a general review of all capital budget requirements.
- *Changes in Project Estimates.* Changes in project estimates for the comprehensive resource plan should be fully reported to the City Council for review and approval.
- *M&O Impact.* Project proposals should indicate the project's impact on the operating budget, including, but not limited to, long-term maintenance costs necessary to support the improvement.
- *Biennial Budget.* The biennial capital budget shall include only those projects which can reasonably be accomplished in the time frame indicated. The detail sheet for each budgeted capital project should include a projected schedule.
- *Carry Over.* Capital projects which are not encumbered or completed during the fiscal year will be re-budgeted or carried over to the next fiscal year except as reported to and subsequently approved by the City Council. All re-budgeted capital projects should be so noted in the adopted capital budget. Similarly, multi-year projects with unencumbered or unexpended funds will be carried over to the subsequent year(s).
- *Revenue Expectation.* Capital projects will not be budgeted unless there are reasonable expectations that revenues will be available to pay for them.

- *Negative Impact from Project.* If a proposed project will cause a direct negative impact on other publicly-owned facilities, improvements to the other facilities will be required as part of the new project and become a part of the new project's comprehensive costs.

### **Capital Improvement Plan**

The purpose of the Capital Improvement Plan is to forecast and match projected revenues and capital needs over a 6-Year period. Long range capital planning is an important management tool that strengthens the linkages between infrastructure needs and the financial capacity of the City. The City's Capital Improvement Plan includes transportation, parks, storm water and sewer improvement projects.

**Citizen Participation and City Council Review.** Citizen participation in the Capital Improvement Program is a priority for the City. Among the activities which shall be conducted to address this need are the following:

- *Timing.* The 6-Year Capital Improvement Plan shall be provided to the City Council in a timely manner to allow time for the City Council members to review the proposal with constituents before it is considered for adoption.
- *Public Meeting Notice.* The City Council study sessions on the Capital Improvement Plan shall be open to the public and advertised sufficiently in advance of the meetings to allow for the attendance of interested citizens.
- *Public Hearing.* Prior to the adoption of the Capital Improvement Plan, the City Council shall hold noticed public hearings to provide opportunities for citizens to express their opinions on the proposed plan.
- *Committee, Boards and Commission Review.* The appropriate committee, board and/or commission shall review the proposed Capital Improvement Plan and provide its comments on the Plan's contents before the City Council considers the Plan for adoption.

**Capital Improvement Plan in Relation to the Comprehensive Plan.** All projects included in the Capital Improvement Plan shall be consistent with the City's Comprehensive Plan. The goals and policies for services, facilities, and transportation should be followed in the development of the City Improvement Plan. The Comprehensive Plan service level goals should be called out in the Capital Improvement Plan.

**Financing.** Capital projects shall be financed to the greatest extent possible through user fees and benefit districts when direct benefit to users results from construction of the project. Refer to Debt Management policy for further detail.

**Intergovernmental Cooperation.** Projects that involve intergovernmental cooperation in planning and funding should be established by an agreement that sets forth the basic responsibilities of the parties involved.

**Project Criteria Factors.** The City Council will annually review and establish criteria against which capital proposals should be measured. Included among the factors which will be considered for priority-ranking are the following:

- Projects which have a positive impact on the operating budget (reduced expenditures, increased revenues);
- Projects which are programmed in the 6-Year Operating Budget Forecast;



- Projects which can be completed or significantly advanced during the 6-Year Capital Improvement Plan;
- Projects which can be realistically accomplished during the year they are scheduled;
- Projects which implement previous City Council-adopted reports and strategies.

## **COST RECOVERY**

The objective of the cost recovery policy is to provide guidelines for setting fees given the cost of service and establishes provisions for ongoing review, process for establishing cost recovery levels and target cost recovery levels for development review and parks programs/services.

*Ongoing Review.* Fees will be periodically reviewed in order to keep pace with changes in the cost of living and methods or levels of service delivery. In order to facilitate a fact-based approach to this review, a comprehensive analysis of the City's costs and fees should be made at least every five years. In the interim, fees may be adjusted annually on January 1, based on the Seattle-Tacoma-Bremerton Consumer Price Index for all Urban Consumers (first half year change of the prior year), contract changes, market rates and other economic conditions.

*Factors to be Considered.* The following factors will be considered when setting cost recovery levels for user fees:

- *Community-wide Versus Special Benefit.* The use of general purpose revenue is appropriate for community-wide services while user fees are appropriate for services that are of special benefit to easily identifiable individuals or groups. Full cost recovery is not always appropriate.
- *Development of a "Value Added" Strategy in Future Cost Recovery Modeling.* Public Value is created in two different ways, directed at two different audiences. Public value is created when governmental agencies use the money and authority given to them to produce things that benefit individuals. Public value is also created when government agencies meet the expectations of citizens and elected officials, that these agencies be accountable for the way they operate; that is, that they be efficient, fair, open, and accountable.
- *Elasticity of Demand.* Pricing of services can significantly impact demand. At full cost recovery, this has the specific advantage of ensuring that the City is providing services for which there is a genuine market, and that it is not over-stimulated by artificially low prices. Conversely, high levels of cost recovery may negatively impact the delivery of services to lower income groups. This negative feature can work against public policy, especially if the services are specifically targeted to low income groups.
- *Feasibility of Collection.* Although it may be determined that a high level of cost recovery may be appropriate for specific services, it may be impractical or too costly to establish a system to identify and charge the user. The method of assessing and collecting fees should be as simple as possible in order to reduce the administrative cost of collection.

*General Concepts.* Revenues should not exceed the reasonable cost of providing services. Cost recovery goals should be based on the total cost of delivery the service as calculated using the fully burdened hourly rates, including direct costs, departmental administration costs and organization-wide support costs such as accounting, personnel, information technology, legal services, fleet maintenance and insurance. The method of assessing and collecting fees should be as simple as possible in order to reduce administrative cost of collection. Rate structures should be sensitive to the "market" for similar services as well as to



smaller, infrequent users of the service. A unified approach should be used in determining cost recovery levels for various programs based on factors discussed above.

*Target Cost Recovery Level for Development Review Services.* The cost recovery policy applies to the following development programs/services: planning (long and short plats, privately initiated re-zonings and comprehensive plan amendments, variances, use permits); building and safety (building permits, structural plan checks, inspections); engineering (public improvement plan checks, inspections, subdivision requirements, encroachments, right-of-way permits); and fire plan check. Cost recovery for these services should generally be very high. In most instances, the City's cost recovery ratio goal should be 85%. The timeline to achieve the cost recovery is no later than year 2021. In setting cost recovery levels, the City shall clearly establish and articulate performance measurements to ensure that there is "value for cost."

*Target Cost Recovery Level for Parks Programs/Services.* The cost recovery policy applies to the following parks and recreation programs/services: recreation services; special events and community gathering; senior services; and all parks. The following should be considered when determining pricing levels: The higher the community benefit, the higher the General Fund subsidy level and the higher the individual benefit, the lower the General Fund subsidy level. The overall cost recovery goal for all parks programs and services should be 45%.

## **CASH MANAGEMENT AND INVESTMENTS**

The objective of a cash management and investment policy is to help balance the day-to-day need for revenues while achieving the highest rate of interest that is reasonable and within the City's acceptable level of investment risk.

Funds will be invested in only those investments permitted by Federal and State law as it relates to public funds. All of the City's funds will be invested with the following objectives (listed in order of priority):

- *Safety.* Investments will be undertaken in a manner that seeks to ensure the preservation of capital in the portfolio. Specifically, the City will: (a) seek to avoid realizing any loss through the sale or disposal of an investment; and (b) seek to mitigate the risk of unrealized losses due to a decline in value of investments held in the portfolio.
- *Liquidity.* The investment portfolio will remain sufficiently liquid to meet all cash requirements that may be reasonably anticipated. This will be accomplished by structuring the portfolio in the following manner: (a) the City will purchase investments scheduled to mature in accordance with its anticipated cash needs, in order to minimize the need to sell investments prior to maturity; (b) a portion of City funds will be maintained in cash equivalents, including money market fund, investment pools and overnight securities, which may be easily liquidated without a loss of principal should an unexpected need for cash arise; and (c) the portfolio will consist largely of investments with active secondary markets.
- *Yield.* The City's investments will be designed with the objective of maximizing a fair rate of return consistent with the safety and liquidity noted above.

## **FINANCIAL REPORTING**

**Reporting Frequency.** Departments will be provided monthly budget and actual reports and comprehensive quarterly reports will be presented to the City Council.

**Reporting Improvements.** The City will strive to continue to make improvements in its financial reporting scheme so that information is available to the City Council, City Manager, departments and public is the best available for sound financial decisions.

**Comprehensive Annual Financial Report (CAFR).** The City will produce the CAFR within 150 days and submit to the GFOA's award program for Excellence in Financial Reporting.

**Transparency.** All financial reports will be posted to the City's website in a timely manner.