



Agenda Item #: _____

Staff Report

City of Manhattan Beach

TO: Honorable Mayor Fahey and Members of the City Council

THROUGH: Geoff Dolan, City Manager

FROM: Bruce Moe, Finance Director
Russell Morreale, Assistant Finance Director
Henry Mitzner, Controller

DATE: May 17, 2005

SUBJECT: Consideration of Revised Financial Policies

RECOMMENDATION:

The Finance Subcommittee and staff recommend that the City Council approve the revisions to the City's Financial Policies.

FISCAL IMPLICATION:

There are no fiscal implications associated with the recommended action.

BACKGROUND:

The City developed its first set of financial policies in the mid 1990's. Since then, only minor modifications have been made to the guidelines. A recent comprehensive review of those policies prompted a number of revisions which were presented and approved by the Finance Subcommittee.

DISCUSSION:

The City's financial policies exist as a guiding document for financial issues. It addresses such areas as:

- ❖ General Policies
- ❖ Accounting, Auditing and Reporting
- ❖ Reserves
- ❖ Debt
- ❖ Revenue
- ❖ Capital Improvements
- ❖ Capitalization & Depreciation
- ❖ Cash Management & Investments
- ❖ Operating Budget

A number of changes have been suggested to the policy, which are presented on the attached document in redline format. While many of the changes approved by the Finance Subcommittee are clean-up/clarification types of items, there are several meaningful changes recommended. These changes include:

Reserve Policies

General Fund (Page 5):

The prior policy stated that the reserve in the General Fund would be equal to 20% of the annual General Fund budget, and that reserves in excess of 20% would be available for capital equipment, transfer to the Capital Improvement Fund, or other one-time expenditures. The revised policy states that the reserve will be equal to at least 20% of the General Fund, and provides flexibility to the Council to reserve in excess of the 20% if desired. Additionally, it provides that any added reserves may be set aside for specific purposes such as capital projects.

City Council Contingency Account (Page 5)

The previous version of the policy stated that the contingency amount would be equal to one-half percent of the General Fund budget. The revised language states that the account will not exceed one-half percent of the General Fund. This change allows flexibility in budgeting if funds are needed to balance a budget (as was the case in FY 2004-2005 when the contingency was budgeted below the one-half percent).

Enterprise Funds (Page 5)

The new policy removes the requirement that enterprise funds (water, wastewater, etc.) reserve for one year of estimated capital spending. This policy was difficult to enforce since capital spending varies from one year to the next.

Information Systems Fund (Page 5)

This is a new section which describes the purpose of the Information Systems Fund, which was created in 1996. This simply adds the fund to the policy. There are no policy changes.

Trust and Agency Funds (Page 6)

This is a new section which addresses how we handle funds that we hold on behalf of others, such as supplemental retirement funds. The main policies are that we segregate those funds from general purpose funds; supplemental retirement programs will be actuarially valued every two years; and that any unfunded liabilities will be disclosed in accordance with Generally Accepted Accounting Principles.

Debt Policies

Credit Rating (Page 6)

This is a new section that states that it is our goal to maintain our AAA/Aaa credit ratings from the three rating agencies, and continue to provide full financial disclosure and perform proactive fiscal planning.

Revenue Policies

User Service Fees (Page 8)

This new section states the City's intention to recover costs wherever appropriate; that fees may be adjusted lower by Council for particular purposes (such as non-profit rates, etc.); that any proposed waivers be presented to the Council for approval as appropriate; and that user fees will be reviewed periodically, but no less often than every five years.

Capitalization & Depreciation Policies (Page 9)

This new policy section adds definitions of the dollar levels for capitalization, and depreciation. These dollar amounts are consistent with those adopted by the Council in prior actions.

Operating Budget Policies

Balanced Operating Budget (Page 10)

The existing policy states that the City shall annually adopt a balanced budget where operating revenues are equal to, or exceed, operating expenditures. The revised guidelines state that it is the City's policy to adopt such a budget, but in the event one is not attainable, the planned use of reserves is permitted under certain circumstances. The existing policy does not allow for a use of reserves in balancing the budget, even if those reserves were set aside in advance for a specific purpose. The revised policy provides such flexibility.

Budget Control and Accountability (Page 10)

The current policy provides that amendments to the budget are approved by the City Council. The recommended modification adds an exception that the City Manager may amend the budget in situations where an appropriation is needed to cover unplanned termination leave expenditures. This would allow the City Manager to move funds from the Employee Leave reserve in the General Fund to a specific department's budget to cover the unplanned added cost of a long term employee discontinuing employment. Depending upon the tenure of the employee, this unplanned payout can be thousands of dollars in unused vacation/leave which can have a significant impact on the department's operating budget. This does not usurp the Council's settlement authority in cases involving employees over a certain dollar threshold.

CONCLUSION:

The Finance Subcommittee reviewed, discussed and approved the revised policy as it is presented. We believe that the new policy serves to clarify issues, strengthens controls in some important areas and more accurately reflects the standards that have evolved since the policy was first created nearly ten years ago. If the full Council approves, the new policy will take effect immediately and will appear in the FY 2005-2006 budget.

Attachment: A. Recommended Financial Policy

cc: Tim Lilligren, City Treasurer

City of Manhattan Beach



Financial Policies

Statement of Purpose

The financial integrity of our City government is of utmost importance. To discuss, write, and adopt a set of financial policies is a key element to maintaining this integrity. Our City has evolved with a variety of financial policies that can be found in many different sources, including: City Council Resolutions; Budget documents; and Capital Improvement Programs. The set of policies within this document, adopted contemporaneously each year with our budget, serves as a central reference point of the most important of our policies, which are critical to the continued financial health of our local government.

Written, adopted financial policies have many benefits, such as assisting the elected officials and staff in the financial management of the City, saving time and energy when discussing financial matters, engendering public confidence, and providing continuity over time as elected officials and staff members change. While these policies will be amended periodically, they will provide the basic foundation and framework for many of the issues and decisions facing the City. They will promote sound financial management and assist in the City's stability, efficiency and effectiveness.

The following policies are divided into eight (8) general categories for ease of reference. These categories include: 1) General Policies; 2) Accounting, Auditing, and Financial Reporting Policies; 3) Reserve Policies; 4) Debt Policies; 5) Revenue Policies; 6) Capital Improvement Policies; 7) Capitalization & Depreciation Policies; 8) Cash Management Investment Policies; and 9) Operating Budget Policies. Except as otherwise noted, all policies included in this document are currently adhered to.

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GENERAL POLICIES

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AUDITING, AND FINANCIAL
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The City will:

- ❖ manage its financial assets in a sound and prudent manner;
- ❖ maintain and further develop programs to ensure its long term ability to pay all costs necessary to provide the level and quality of service required by its citizens;
- ❖ establish and maintain investment policies that are in accordance with State laws;

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ACCOUNTING, AUDITING, AND FINANCIAL REPORTING POLICIES

FINANCIAL INFORMATION

It ~~is~~ the policy of the City of Manhattan Beach to provide all financial information in a thorough, timely fashion, and in a format that is easy for Council, citizens, and City employees to understand and utilize.

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ACCOUNTING STANDARDS

The City's accounting of financial systems shall be maintained in accordance with Generally Accepted Accounting Principles (GAAP), standards of the Governmental Accounting Standards Board (GASB), and the Government Finance Officers Association (GFOA).

ANNUAL AUDIT

An independent public accounting firm will perform an annual audit and its opinions will be included in the comprehensive annual financial report.

The independent audit firm will be selected through a competitive process at least once every five years. The contract will be for an initial period of three years with two additional one-year options at the City ~~Council's~~ discretion. ~~The~~ Finance Subcommittee, City Manager and Finance Director will review the qualifications of prospective firms and make a recommendation to the City Council. The audit contract, ~~and any extensions~~, will be awarded by the City Council.

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An Annual Financial Report shall be prepared within ~~six~~ months of the close of the previous fiscal year. It will be reviewed with the Finance Subcommittee, ~~and presented~~ to the City Council and community at a public meeting ~~no later than February 1st of the following year~~.

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~~It is the City's goal~~ to maintain accounting records, ~~processes and procedures~~ in such a manner as to receive an unqualified audit opinion and to ~~maintain~~ a Certificate of Achievement for Excellence in Financial Reporting from the GFOA.

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RESERVE POLICIES

The City utilizes a variety of accounting funds for recording revenues and expenditures of the City. At each fiscal year-end, budgeted/appropriated expenditure authority lapses with ~~the exception of~~ capital project spending, ~~and operating expenses that~~ have been incurred but not paid (encumbered). The remaining dollars left in each fund that are undesignated and unencumbered constitute available reserves of the City. It is appropriate that reserve policies for the City be established for each of the various

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funds, that the purpose of these reserves be designated, and that dollars available in excess of the reserve amounts be appropriately and effectively utilized.

GENERAL FUND

The General Fund reserve will be maintained in an amount equal to at least 20 percent of the annual General Fund expenditure budget. These reserves are designed to be used in the event of significant financial emergency. Council may, at its discretion, reserve additional funds above the 20% minimum. Such additional reserves may be set aside for specific purposes, such as capital projects, for known significant future cost items, or as general operational reserves.

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CITY COUNCIL CONTINGENCY ACCOUNT

A contingency account in an amount not to exceed one-half of one percent (0.5 percent) of the City's General Fund expenditure budget will be maintained annually in the City Council's budget. This account will be available for unanticipated, unbudgeted expenditures and will require City Council approval to spend. The purpose of this account is to provide some flexibility for unforeseen events without the necessity to appropriate additional funds from the City's reserves.

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ENTERPRISE FUNDS

The City's Enterprise Funds will maintain reserves equal to four months of operating expenses.

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FLEET MANAGEMENT FUND

Through the use of the Fleet Management Fund, the City will annually budget sufficient funds to provide for the orderly maintenance, repair and replacement of the City's vehicles. This fund is supported by charges to user departments which are adjusted annually based on the department's proportionate share of estimated fleet management expenses. Sufficient reserves will be maintained in the fund to provide for the scheduled replacement of fleet vehicles at the end of their useful lives.

INFORMATION SYSTEMS FUND

Through the use of the Information Systems Fund, the City will annually budget sufficient funds to provide for the orderly maintenance, repair and replacement of the City's technology infrastructure. This fund is supported by charges to user departments which are adjusted annually based on departments' proportionate share of estimated expenses. Such share may be determined based upon the departments' number of devices supported by the IS Division. Sufficient reserves will be maintained in the fund to provide for the scheduled replacement of equipment at the end of their useful lives.

RISK MANAGEMENT FUND

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The City maintains a self-insurance fund for the purpose of property, liability, and workers' compensation expenses. This fund pays insurance premiums, benefit and settlement payments, and administrative and operating expenses. The Risk Management Fund is supported by charges to other City funds for the services it provides. These annual charges for service shall reflect historical experience and shall be established to approximately equal the annual expenses of the fund. Separate reserves shall be maintained for current and long term general liability and workers' compensation liability at a level which will adequately fund the City's potential loss exposure in each area as determined by historical loss data. The Risk Management Fund shall maintain an annual working capital balance of \$2 million.

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TRUST AND AGENCY FUNDS

The City maintains funds on a trustee basis for a number of purposes, including City-sponsored post employment benefits programs and trust accounts for such purposes as utility underground projects. These funds shall be segregated from the City's general funds.

The estimated cost of City-sponsored retirement programs will be actuarially valued biennially. On-going annual normal costs for such programs will be budgeted in the department receiving the benefit. Unfunded liabilities will be disclosed and accounted for in accordance with Generally Accepted Accounting Principles (GAAP).

DEBT POLICIES

ISSUANCE OF DEBT

The City will not use long-term debt to pay for current operations.

The use of bonds or certificates of participation will only be considered for significant capital and infrastructure improvements.

The term of the debt shall never extend beyond the useful life of the improvements to be financed.

CREDIT RATING

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It is the City's goal to maintain our AAA/Aaa credit rating from all three major rating agencies. The factors that contribute to our high rating include the City's strong financial management, low debt levels, budgetary and fiscal controls, and accountability. To support this policy, the City will continue to maintain its position of full financial disclosure and proactive fiscal planning.

LEASE PURCHASE

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The City will lease ~~purchase~~ equipment if necessary because of funding availability, ~~or~~ if lease rates are ~~more favorable~~ than the rate attained from investment return. ~~Equipment may also be leased if the lease terms compare favorably when reviewing the total life cycle cost of the equipment.~~ In no case shall the City lease ~~purchase~~ equipment whose useful life is not greater than the term of the lease.

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REVENUE POLICIES

GENERAL FUND REVENUE

The City will strive to develop and maintain a diversified and reliable revenue stream so as to avoid becoming overly dependent on any single type of revenue. Efforts will be directed to optimize existing revenue sources while periodically reviewing potential new revenue sources.

Budgeted revenues will be estimated conservatively using accepted standards and estimates provided by the state, ~~other governmental agencies~~ ~~or reliable economic forecasters~~ when available.

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~~If revenues from "one-time" or limited duration sources are used to balance the City's annual operating budget, it is to be fully disclosed and explained at the time the budget is presented. It is the City's goal to not rely on these types of revenues to balance the operating budget.~~

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~~The City will pursue revenue collection and auditing to assure that moneys due the City are accurately received in a timely manner.~~

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Fees and charges for service shall be evaluated and, if necessary, adjusted annually to assure that they cover all direct and indirect costs, unless it is determined that full cost recovery would not be in the best interest of the public.

~~The City will seek reimbursement for State and Federal mandated costs whenever possible.~~

GRANTS AND GIFTS

The City shall actively pursue federal, state and other grant opportunities when deemed appropriate. Before accepting any grant the City shall thoroughly consider the implications in terms of ongoing obligations that will be required in connection with acceptance of said grant.

ENTERPRISE FUND CHARGES

The City will set user fees for each enterprise fund at a rate that fully covers direct and indirect costs of providing the service, ~~as well as planned capital improvements that may be necessary from time to time.~~

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PARKS AND RECREATION FEES

~~All Parks and Recreation department expenses and revenues will flow through the General Fund (except those transactions related to Proposition A). The goal of the Parks and Recreation Department shall be to generate General Fund revenue equal to at least 35 percent of the total General Fund expenditures of the department.~~

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Recreation fees ~~for such activities as classes and room rentals~~ shall be established and reviewed periodically. ~~The purpose of these fees is to recover the direct cost of the program, and to generate additional revenues to support the overall operation of the Parks and Recreation department and programs.~~ As appropriate within the marketing of the recreation programs, higher non-resident fees are charged, as well as priority registration procedures for Manhattan Beach residents.

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USER SERVICE FEES

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The City may impose user fees wherever appropriate. Such fees will recover the cost of providing the service, including all direct and indirect costs, administrative overhead, depreciation, etc. By policy, Council may direct certain fees to be lowered for particular purposes. Waivers of user fees will be presented for Council approval as appropriate. Fees will be reviewed periodically, but not less than every five years, to ensure that full cost recovery levels are identified.

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Fees such as space rental, parking meter rates, etc. are based upon market conditions and are not subject to the limitations of cost recovery. These fees may be adjusted periodically by the City Council.

CAPITAL IMPROVEMENT POLICIES

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DEDICATED CIP FUNDING SOURCES

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Most of the City's infrastructure has a designated revenue source to pay for its upgrade or replacement as appropriate. For example, water/wastewater rates fund utility infrastructure needs; gas tax revenues fund street needs; and storm drainage needs are paid for with related fees and assessments. However, our public buildings and our park system are the primary beneficiaries of the City's Capital Improvement Fund (CIP). Specific revenue sources have been designated to provide permanent funding in support of general operational infrastructure. In particular, the City has dedicated:

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- ❖ 15% of annual hotel transient occupancy tax (1.5% of the 10% tax);
- ❖ Fifty cents of the per hour charge for all on-street city parking meter collections
- ❖ \$4 of each parking citation (with the exception of expired meter cites).

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Transfers into the CIP Fund will be processed by the Finance Department on a monthly basis and recorded as such in the annual adopted budget.

FIVE YEAR CAPITAL IMPROVEMENT PROGRAM (CIP)

The City shall annually prepare a capital improvement spending program projecting capital needs for a five year period. This CIP shall address all of the City's funds.

The first year of the five year CIP will be consistent with, and adopted as a component of, the annual operating budget.

In the development of the Capital Improvement Program, the operating costs associated with the capital project will be projected and considered in conjunction with the CIP.

ENTERPRISE FUND CAPITAL IMPROVEMENTS

Capital Improvements funded from the Enterprise Funds shall be paid for in combination of "pay-as-you-go" financing and the use of long-term debt. The City shall periodically review its enterprise capital needs and establish capital spending plans that are appropriate and reflect a combination of debt and "pay-as-you-go," while attempting to keep our rates competitive with those in the surrounding area.

CAPITALIZATION & DEPRECIATION POLICIES

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The City shall capitalize equipment and facilities within the following parameters:

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Equipment - \$5,000 per unit
Buildings & Facilities - \$100,000

Minor equipment that falls below the \$5,000 threshold, but is subject to shrinkage, such as cellular telephones and computers, shall have a non-numbered City of Manhattan Beach property tag affixed when placed into City service.

The City shall depreciate capital assets such as machinery, equipment, buildings and improvements, and infrastructure (roads, sidewalks, parks, etc.). Depreciation shall be performed on a straight line basis over the expected useful life of the asset and in accordance with Generally Accepted Accounting Principles (GAAP).

CASH MANAGEMENT INVESTMENT POLICIES

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The Finance Subcommittee & City Council shall annually review and update, or modify as appropriate, the City's investment policy. Reviews shall take place at public meetings and the policy shall be adopted by minute action of the City Council based upon the Finance Subcommittee's recommendations.

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Reports on the City's investment portfolio and cash position shall be developed and presented to the City Council monthly. Additionally, expenditure reporting showing year-to-date budgeted and actual expenditures shall be prepared monthly and distributed to all departments.

City funds will be managed in a prudent and diligent manner with emphasis on safety, liquidity, and yield, in that order.

OPERATING BUDGET POLICIES

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BALANCED OPERATING BUDGET

~~It is the City's policy to adopt a balanced budget where operating revenues are equal to, or exceed, operating expenditures. In the event a balanced budget is not attainable, and the cause of the imbalance is expected to last for no more than one year, the planned use of reserves to balance the budget is permitted. In the event that a budget shortfall is expected to continue beyond one year, the planned use of reserves must be developed as part of a corresponding strategic financial plan to close the gap through revenue increases or expenditure decreases.~~

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~~Any year end operating surpluses will revert to unappropriated balances for use in maintaining reserve levels set by policy and will be available for capital projects and/or "one-time only" General Fund expenditures.~~

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BUDGET DOCUMENT

The operating budget shall serve as the annual financial plan for the City. It will serve as the policy document of the City Council for implementing Council goals and objectives. The budget shall provide the staff the resources necessary to accomplish City Council determined service levels.

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The City Manager shall annually prepare and present a proposed operating budget to the City Council no later than ~~the second regular Council meeting in May~~ of each year; and Council will adopt said budget no later than June 30 of each year. Funds may not be expended or encumbered for the following fiscal year until the budget has been adopted by the City Council.

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The City's annual budget will be presented by department, with a logical breakdown of programs and ~~proposed expenses.~~ ~~The budget document will also summarize expenditures at the personnel, operating and maintenance, and capital levels.~~

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Where practical, the City's annual budget will include measures of workload, efficiency, and effectiveness.

BUDGET CONTROL AND ACCOUNTABILITY

Budget control is maintained at the departmental level. The City Manager has the authority to approve appropriation transfers between programs or departments. In no case may total expenditures of a particular fund exceed that which is appropriated by the City Council without a budget amendment. ~~Amendments to the budget are approved by the City Council with the exception of the appropriation and transfer of~~

funds from employee leave reserves to a specific department's program budget to cover unplanned customary termination leave expenditures within a given year. Such amendments may be approved by the City Manager.

Budget accountability rests primarily with the operating departments of the City.

CAPITAL PLANT AND EQUIPMENT

The annual budget will provide for adequate maintenance and replacement of capital assets.

ENTERPRISE FUNDS

The Enterprise Funds shall be supported by their own rates and not subsidized by the General Fund.

The Enterprise Funds will pay their share of overhead services provided by the General Fund.