

**City of Pacific Grove  
Council Policy**

<b>Subject</b>	<b>Policy Number</b>	<b>Effective Date</b>	<b>Page</b>
<b>Budget and Financial Management</b>	<b>400-6</b>	<b>October 1, 2014</b>	<b>Page 1 of 7</b>

**Purpose**

This Budget and Financial Management policy is established to help ensure that the City’s financial resources are managed in a manner that fosters administrative transparency and confidence among the City Council, citizenry, and staff that the City’s resources shall be available to fund ongoing City services, consistent with local economic conditions and the City Council’s service priorities.

**Budget Process**

Budget management occurs year-round, with ongoing City Council direction and public input. In addition to formal updates on the budget and fiscal forecast, staff provides periodic updates on revenues and expenditures.

The City uses a five-year fiscal planning horizon, in which the annual budget is the first year of the forecast. The forecast is a tool that helps decision-makers identify important trends and understand long-term consequences of budget decisions. Importantly, the forecast is not a budget and does not represent a plan. It is a model based on cost and revenue assumptions that is updated continuously. Since the degree of revenue uncertainty increases with each successive year of the forecast (i.e., we can place much more confidence in projections for the first year of the forecast period than for the last, the forecast is a more viable framework for decision-making in the near-term, and only suggests relative financial health based on stated economic assumptions in the later years.

The annual budget process begins in January or February with City Council discussion of goals for the following year. At this meeting, staff presents an update of the current year budget and five-year fiscal forecast, as well as estimates of revenues for the following year and baseline expenditure assumptions. Baseline expenditures include existing staffing levels and other costs required to continue current service levels. At this meeting, the City Council provides direction to staff on the goals for the following budget year and five-year forecast, which include both goals for services and capital projects as well as the amount of additional funding or expenditure reduction required to achieve the goals.

Based on this direction, the City Manager distributes budget instructions and baseline staffing cost information to department managers for developing the budget. Subsequently, the City Manager and Finance Director work with program managers to develop the budget consistent with Council goals.

In February and March, the City Council reviews evolving revenue information and expenditure assumptions and determines the process for City Council consideration of the budget.

The City Manager finalizes the recommended budget and presents it to the City Council in May. After public input and discussion at this meeting, the City Council either directs modifications to the budget or introduces an ordinance adopting the budget. At the second reading of the ordinance at a subsequent regular City Council meeting, the budget is adopted and effective July 1<sup>st</sup> of the fiscal year.

### **Fiscal Forecast**

- Staff shall maintain a five-year General Fund fiscal forecast to include revenues, expenditures, as well as the net results of operations and the beginning and ending fund balances for each year of the forecast.

### **Operating Budget**

- The City Council shall adopt an annual operating budget, pursuant to Article 29 of the City Charter, prior to the start of the fiscal year.
- Revenue projections for a given year shall include a contingency reserve of 1%, either positive or negative, depending on the general direction of the economy. The need for such a contingency can be re-evaluated after January 1 of the budget year.
- Subject to exception for specific circumstances, the City Manager's recommended budget shall include an expenditure contingency in the General Fund equal to 1%, which may only be spent on projects required to advance City Council goals, expressed either explicitly or through the City Council's work plan.
- The operating budget shall include ongoing operating revenues sufficient to fund ongoing operating expenditures. Reserves may be used as a resource to fund operations, with City Council acknowledgement of such use and a plan for re-establishing operations within annual anticipated revenues.
- The budget shall provide for adequate maintenance and the orderly replacement of fixed assets and equipment.
- Each October, staff shall present a report to the City Council estimating the year-end results for the preceding fiscal year. This report shall compare unaudited actual figures with budgeted and the most recently estimated actual figures.
- Appropriations are approved at the fund level, and in the case of the General Fund, at the department or program level. All amendments to the budget at these levels may be approved only by the City Council.
- For budget purposes, programs and departments are defined as follows:
  - City Council
  - Legal Services
  - City Manager/Human Resources/City Clerk
  - Finance
  - Information Systems
  - Community and Economic Development
  - Police and Disaster Preparedness
  - Fire and Emergency Medical Services
  - Library
  - Museum
  - Recreation
  - Public Works

The City Manager shall have authority to transfer funds within a given fund and between department appropriations to ensure that programmatic budgets may adapt throughout the year to evolving circumstances. Departmental appropriations in the 5100 series of the chart of accounts (salary and benefits) that reflect salary and benefit savings, may not be used to offset expenditures in the 5200 series of account codes (services and supplies) or the 6000 series of account codes (capital expense) without the express, written approval of the City Manager. These changes shall have no negative effect on the given fund or the General Fund.

### **Capital Projects**

The City shall adopt a five-year capital improvement and maintenance plan, with the first year of the plan to be appropriated as part of the operating budget. The purpose of the plan is to identify and prioritize capital project needs.

The budget shall also include capital expenditures; where possible, such capital expenditures will be funded with non-recurring revenues or grants.

At least the first two years of the plan shall be fully funded, with funding shortfalls and challenges clearly identified in remaining years.

A Capital Improvement is defined as property, plant, or improvements having a useful life of two or more years and a total amortized acquisition and maintenance cost of \$2,500 or more. All estimated construction, maintenance, and operating costs and potential funding sources for each proposed capital improvement shall be identified.

The City shall finance only those capital improvements consistent with the adopted capital improvement plan and City priorities. All capital improvement operating and maintenance costs shall be included in the fiscal forecast.

### **Basis of Accounting**

Financial statements are prepared in accordance with General Accepted Accounting Principles and all relevant Pronouncements promulgated by the Governmental Accounting Standards Board (GASB). All governmental fund types are accounted for using the modified accrual basis of accounting. Their revenues are recognized when they become measurable and available as net current assets.

Expenditures are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred. An exception to this general rule is principal and interest on general long-term debt, which is recognized when due. Financial resources usually are appropriated in other funds for transfer to a debt service fund in the period in which maturing debt principal and interest must be paid. Such amounts are not current liabilities of the debt service fund, as their settlement shall not require expenditure of existing fund assets.

All proprietary fund types and nonexpendable trust funds are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned, and their expenses are recognized when they are incurred.

## **Basis of Budgeting**

The basis of budgeting is the same as the basis of accounting.

## **Treasury and Cash Management**

The City shall manage the treasury in compliance with California Government Code Section 53600 and City Council Policy 400-5, which requires quarterly Treasurer's Reports to the City Council, reconsideration of Policy 400-5 by the Council at least once every two years, and selection of investments based on considerations of safety, liquidity, and yield, in order of decreasing priority.

In circumstances where short-term borrowing (i.e., fewer than 12 months) is required to mitigate the effects of uneven revenue disbursements from the state and ensure expenditure cash-flow demands may be met, the following options shall be considered, with the ultimate course of action dependent on the least cost, greatest security for the City, and administrative efficiency:

- Tax and Revenue Anticipation Notes (TRAN)
- Treasury Loan from Monterey County
- Inter-fund loans
- Commercial line of credit.

Should inter-fund loans be selected as a cash-flow strategy, the following conditions shall apply:

- City Council approval required for all loans;
- Duration of less than 12 months with the loan and repayment occurring within the same fiscal year;
- Fixed loan term (i.e., specific number of months with repayment date);
- Borrowing fund must pay interest at level to result in no loss of interest revenue to the lending fund;
- Specific revenue pledged to repay the loan based on realistic expectations for receipt;
- Funds in the lending fund must not be needed for operations during the period of the loan; and
- Loans must not be made from grant funds or other funds enabled by State or Federal legislation.

The City Council shall receive real-time reports of warrants drawn on the City Treasury.

## **Reserves**

Reserves are established to ensure that sufficient resources shall be maintained in specified funds in amounts sufficient to manage reasonable risks, meet unanticipated needs, capitalize on opportunities, and provide for reasonable contingencies. Further, reserve balances shall be categorized and prioritized in accordance with GASB Statement #54 (GASB 54).

- In the City of Pacific Grove, "operating reserve" is equivalent to portions of the accumulated fund balance that are classified as either committed, assigned, or unassigned, per GASB 54.

- The order in which spendable reserves may be used is prioritized as follows: restricted, committed, assigned, and then unassigned, per GASB 54. Council action is required to increase, decrease, eliminate or reclassify amounts reported in each category.
- Use of reserves must be authorized in advance by the City Council.
- If reserves are expended for their intended use, the City Council shall prioritize restoration of reserves to levels established by policy before allocating resources to fund new or improved services.
- *General Fund.* The City establishes a target reserve level of 10% of the General Fund annual operating budget, and shall maintain reserves of at least 10%, unless otherwise approved by the City Council for specific purposes. The 10% reflects the following components:
  - Emergency financial need (e.g., capital repair, natural disaster)
  - Economic contingency (to mitigate sudden service and staffing cuts in response to economic shocks and downturns)
  - Economic opportunity (to leverage public resources for public investment opportunities, e.g., downtown property)
  - One-time opportunities to invest in assets (e.g., an expanded Library), as an alternative to debt financing
- *Golf Fund.* The purpose of the Golf Fund is to enable operation of the golf course as an enterprise without operating subsidies from the General Fund, unless deliberately authorized. The City establishes a target reserve level of 25% of revenues of the Golf Fund, as of June 30<sup>th</sup> of two fiscal years prior, to be used for capital improvements, cash management, and emergency protection. Given the vulnerability of the golf business to recession, 20% of the 25% would be retained for use in mitigating the effects of unexpected revenue downturns, and 5% would be available retained for emergency repairs or other emergencies.
- *Sewer Fund.* The Sewer Fund shall maintain a reserve of at least \$500,000.
- *Workers Compensation Fund:* The Workers Compensation Fund shall maintain a balance of current assets equal to 67% of total liabilities, or higher, should actuarial analysis conclude an imminent risk to the City for unanticipated losses.
- *Liability Insurance Reserve:* The Liability Insurance Reserve shall maintain a balance of at least \$300,000 in current assets, which is equivalent to the maximum amount the City would be required to pay in the event of two catastrophic losses in a single year (City's Self-Insured Retention Limit is currently \$150,000 per claim).

### **Debt Management**

- Long-term borrowing shall be restricted to the purpose of funding capital improvement projects and equipment. The use of long-term borrowing for ongoing operations shall be avoided.
- The term of the debt shall not exceed the expected useful life of the object of the financing.
- Debt obligations shall be prioritized in the budget process and payments shall be made in a timely and efficient manner.
- Refunding techniques shall be employed where appropriate, and with all due City Council approval, to allow for restructuring of outstanding debt to remove or change restrictive covenants, and/or to reduce annual debt service in an amount sufficient to justify the costs related to restructuring the debt.
- Total debt in any fund shall not exceed prudent levels.

### **Property Acquisition and Disposition**

- Acquisition of real property shall be tied to a specific objective, with the source of adequate funds identified and considerations given for the long-term fiscal and policy impacts.
- Disposition of real property shall be considered for those properties without specific deed restrictions and that are unused, under-utilized, economically not viable, or that were acquired for an outdated plan or purpose.

### **Annual Audit**

The City of Pacific Grove shall undertake an annual independent audit.

- The City's Comprehensive Annual Financial Report (CAFR) including accompanying schedules and notes shall be completed no later than December 31 of each contract year.
- All funds of the City shall be audited in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller of the United States.
- The form of the CAFR shall be compliant with the requirements of the Government Finance Officers Association (GFOA) Certificate Program and will include the independent auditor's opinion on the Government-Wide Financial Statements and Fund Financial Statements.
- A separate "management letter" shall be published that includes recommendations for improvements in internal control, accounting procedures and other significant observations.

**Capital Policy**

All assets, including land, buildings, machinery and equipment, with an original cost in excess of \$5,000 and a useful life of three years or more will be subject to capitalization.

- The capitalization threshold is applied to individual units of fixed assets. For example, ten chairs purchased via a single order, each costing \$600 will not qualify for capitalization although the total cost of \$6,000 exceeds the threshold of \$5,000.
- Repair costs for fixed assets will be subject to capitalization when the repair extends the useful life of the related fixed asset.
- Useful Life Schedule

Description	Useful Life In Years
Buildings	100 Years
Machinery and equipment	5 Years
Furniture and fixtures	5 Years
Improvements other than buildings	3 Years
Sidewalks, curb, gutters, and streets	20-50 Years
Traffic signals	15 Years
Street signs	15 Years
Storm drains	20-50 Years
Park equipment	10-50 Years

- For construction in progress, no depreciation is recorded until the asset is placed in service. When construction is completed, the asset shall be reclassified as building, building improvement, land improvement, or equipment and should be capitalized and depreciated.
- The City shall use the straight-line method for depreciating all fixed assets (the basis of the asset is written off evenly over the useful life of the asset). Depreciation shall begin in the month the asset is placed in service.
- All computer and computer related equipment will be recorded and controlled as inventory and not depreciated. Constant changes in technology, software demands, and system configurations cause this asset class to be obsolete before it reaches its useful life.

**Donated Assets**

Fixed assets acquired by gift, donation or payment of a nominal sum not reflective of the asset's market value shall be assigned cost equal to the fair market value at the time of receipt.

- Adopted: Resolution 11-086 (Adopted November 2, 2011)
- Amended: Resolution 14-063 (Amended October 1, 2014)
- Amended: Resolution 15-055 (Amended October 21, 2015)
- Amended: Resolution 16-048 (Amended September 7, 2016)