# FINANCIAL POLICIES

## POLICY PURPOSE

The financial integrity of our City government is of utmost importance. To that end, the establishment of appropriate financial management, debt administration, budget and capital plan development, and long-range planning policies ("Financial Policies") will promote the fiscal health of Portsmouth, as well as the cost-effective and efficient delivery of services to our citizens.

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. These policies will be reviewed annually and reaffirmed by City Council at least once every three years.

## FINANCIAL POLICY LINKAGES

The City has developed these Financial Policies, with input from its Financial Advisor, based upon municipal finance "Best Practices" as promulgated by the Government Finance Officers Association and the National Advisory Council on State and Local Budgeting. The City and its agents will regularly monitor the evolution of such "Best Practices" and update these Financial Policies and the City's operating practices accordingly.

## GENERAL FINANCIAL PRINCIPLES

The City will continuously evaluate programs and operating practices as a means of ensuring the City's residents an efficient and highly effective local government.

The City will strive to utilize technological advances as a means of increasing employee productivity and reducing the need for new positions.

The City will allocate new dollars (after meeting fixed commitments such as debt service requirements and benefits changes) to the key priority areas as established by Council.

The City will attempt to utilize benefits of new economic development successes as a means of maintaining an adequate tax rate for services rendered to our residents coupled with our ability to manage expectations with the long term operational needs of the City.

## REVENUES

### Revenue Diversification

The City will strive to maintain diversified and stable revenue streams to protect the government from problematic fluctuations in any single revenue source and provide stability to ongoing services.

### Fees and Charges

All fees established by the City for licenses, permits, fines, services, applications and other miscellaneous charges shall be set to recover all or a portion of the City's expense in providing the attendant service. Fees and charges will be reviewed annually in connection with the development of the operating budget.

### Use of One-Time Revenues

The City will 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 (i.e.; unusually large building permits, etc).

### Conservative Estimation

Revenues will be budgeted conservatively so as not to introduce regular shortfalls in individual revenue accounts. Revenue estimates shall be reviewed and validated, whenever possible, by an independent outside professional engaged by the City. The Budget Officer shall utilize appropriate collection percentages in estimating revenues for each account or class of accounts based upon historical collection patterns. Unusual economic circumstances shall require adjustments to collection assumptions.

## BUDGET

### Balanced Budget

The City's budgetary policies are based upon guidelines and restrictions established by State and City Codes and Generally Accepted Accounting Principles for Governmental entities. These provisions set forth the City's fiscal year, public hearing and advertising requirements, restrictions on taxation, and also stipulate that the City must maintain a balanced budget.

The City will annually adopt and execute a biennial budget for such funds as may be required by law or by sound financial practices and generally accepted accounting principles. The budget shall control the levy of taxes and the expenditure of money for all City purposes during the ensuing fiscal year.

The City's budget may be considered balanced if estimated revenues meet planned expenditures.

**Contingency Appropriation**

The budget shall strive to include in the annual budget a contingency appropriation of at least 0.5% of budgeted expenditures. The contingency appropriation is designed to meet unanticipated revenue shortfalls or emergency expenditures.

**Use of Fund Balance**

While accumulated fund balance in the General Fund may legally be used as revenue to support the budget, the City's intention is not to use fund balance to fund recurring operating expenditures. Accumulated fund balance over and above the City's fund balance target may be considered for funding one-time expenditures.

**Quarterly Budget Monitoring**

Staff will provide City Council with a quarterly update of actual revenues and expenditures for the Fiscal Year and comparisons will be made in such report to: (1) the adopted budget, and (2) revenues and expenditures through the same period of the immediately prior Fiscal Year. Tabular presentations will be supplemented by sufficient narrative to explain material variances from budget and the prior year. These reports are intended to provide sufficient information to City Council to allow for mid-year budget adjustments necessary to avoid operating budget shortfalls. As appropriate, Staff will provide recommendations for amendments to the budget to ensure budgetary balance.

**Multi-Year Operating Budget Forecast**

The City will prepare and annually update a long range (5 year) financial forecast of the operating budget utilizing trend indicators and projections of annual operating revenues, expenditures, capital improvements, associated debt service and incremental operating costs, and fund balance levels. This forecast is intended to be an internal planning tool for Staff and the City Council, but will be shared with the rating agencies each year, as well as interested citizens upon request. The Forecast should be prepared with the intention of showing projected results based on programs, trends, and policies then in effect and without undue influence on its outcome.

## FUND BALANCE

### Policy Minimum

The City will maintain an Unreserved, Undesignated General Fund Balance equal to 15% of General Fund revenues.

If the Unreserved, Undesignated General Fund Balance falls below the minimum level described above, Staff will submit a detailed plan ("Staff Plan") to City Council that proposes actions necessary to return the fund balance to the policy minimum over not more than two succeeding Fiscal Years. City Council shall act upon the Staff Plan by taking the actions necessary to implement same or substituting alternatives that achieve the same objective.

If, upon the effective date of these Financial Policies, the City is not in compliance with this Fund Balance Policy Minimum, the City Staff will prepare a Staff Plan to restore the fund balance to the policy level and such plan will be presented within not more than three (3) months from the effective date.

## DEBT MANAGEMENT PRINCIPLES

All long-term financings shall comply with Federal, State, and City Charter requirements.

Accompanying each long-term financial obligation will be a cost benefit analysis, the identification of the funding source, an assessment of the ability to repay the obligation, the impact on the current budget, commitments to the future budgets, maintenance and operational impact of the facility or asset and the impact on the City's credit rating.

The project should be incorporated into the City's multi-year capital and equipment improvement plan.

The term of the long-term obligation for the acquisition, replacement or expansion of physical assets, will not exceed the useful life or the average life of the project or projects being financed.

Long-term financial obligations will not be used to meet current operations, or for recurring purposes.

Variable rate obligations shall not exceed 15% of the City's outstanding long-term obligations and must be approved by the Chief Financial Officer.

The City Council may consider conduit financing on behalf of the EDA, PRHA, and PPIC upon recommendation of the Debt Advisory Committee. Initial contact will be directed to the Chief Financial Officer. Council will consider whether the conduit is feasible, financially and economically prudent, coincides with the City's objectives, and does not impair the City's creditworthiness (All expenses related to the conduit financing will be borne by the applicants).

Except as noted below, long-term obligations issued through the City must qualify for an underlying (i.e.; rated on the basis of the security for the loan) investment grade rating by one of the nationally recognized rating agencies or qualify for alternative credit enhancement. An exception to this requirement would be debt issued via the Virginia Resources Authority, a political subdivision of the Commonwealth of Virginia. In the case of long-term obligations that are privately placed as bank qualified investments by the City, such obligations would not be required to qualify for an investment grade rating.

The City shall encourage and maintain good relations with credit rating agencies, investors in the City's long-term financial obligations, and those in the financial community who participate in the issuance and sale of our long-term obligations. A policy of full and open disclosure on every financial report and long-term obligation transaction will be enforced and credit rating agency presentations/updates shall be conducted at least annually.

The City shall comply with all on-going disclosure requirements and shall file such documents in a timely manner.

The City shall monitor earnings on bond proceeds and rebate excess earnings as required to the U.S. Treasury to avoid the loss of tax-exempt status.

The City will enforce filing notices of completion on all projects within five years of their financing.

The City shall continually review outstanding obligations and aggressively initiate refinancings when economically feasible and advantageous.

The Chief Financial Officer will periodically report unspent capital project funds to the City Manager and City Council not less than annually.

## Debt Administration

The City shall comply with the Internal Revenue Code Section 148 — Arbitrage Regulations for all tax-exempt debt issued. An annual estimate of arbitrage liabilities shall be obtained by the City and recorded on the financial statements.

A good faith deposit of 2.0% of the par amount of the bond sale shall be presented by the underwriter in the form of a check or surety acceptable to the City and Bond Counsel prior to the approval of the bonds by the Mayor and City Council.

The City shall use a competitive bidding process in the sale of debt unless the use of a negotiated process is warranted due to market timing requirements (refunding), or a unique pledge or debt structure. The City will award competitively issued debt on a true interest cost (TIC) basis.

The City welcomes ideas and proposals from investment bankers and will seek to give first consideration to those firms that submit unique and innovative ideas that benefit the City. Unsolicited proposals should be submitted to the City's Chief Financial Officer.

The selection of an underwriter or group of underwriters for a negotiated sale shall be based on the following factors:

- Participation in the City's competitive sales;
- Submission of unique or creative proposals;
- Qualifications of firm;
- Size and geographic distribution of their sales staff.

All professional service providers selected in connection with the City's debt issuance and management program shall be chosen through a competitive process such as request for proposals (RFP's) on an as needed basis.

The use of reimbursement resolutions shall be encouraged as a cash management tool for debt funded projects. Reimbursement resolutions may be used for any project that has been approved in the City's Capital Budget. Reimbursement resolutions may be used for other projects if the projects are revenue supported or fund within departments' operating budget.

The City shall obtain a clear opinion from qualified legal counsel that the City is not liable for the payment of principal and/or interest in the event of default by a conduit borrower. If no such opinion can be obtained, the conduit borrower will be required to purchase insurance or a letter of credit in the City's name in the event of default. Examples of a conduit issuer are special authorities, tax-increment financing districts, public improvement districts, or industrial development issuers.

**Debt Capacity and Affordability**

A long-term debt capacity and affordability analysis will be completed on an annual basis as a means of ensuring that the City does not exceed its ability to service current and future debt requirements. This analysis will verify that the City is maintaining the following ratios and will be performed in conjunction with the City's Capital Improvement Program (CIP) process. The guidelines that are utilized for direct City debt are as follows:

1. The ratio of Net Tax-Supported Debt Service to General Fund Revenues should not exceed 12%, within the six-year CIP projection;

2. The ratio of Net Tax-Supported Debt Service to Market Value should not exceed four percent (4%), within the six-year CIP projection;

3. The 10 Year Debt Payout Ratio of Net Tax-Supported Debt Service Should Be Greater Than or Equal To 50%.

**Utility Fund Debt**

The City will adopt annual water and sewer rates that will generate sufficient revenues to meet the legal requirements of Enterprise Fund bond covenants. These rates will also allow for adequate capital replacement in water and sewer systems.

**Refunding Bonds**

The City, with the assistance of its Financial Advisor, shall monitor the City's debt portfolio on a regular basis for refunding opportunities. When contemplating a refunding, the City will have a minimum of 3.0% economic savings (as expressed on a net present value basis) as a benchmark to proceed with a refunding. This policy is not intended to preclude the possibility of refunding one or more maturities of existing debt that generate a lesser amount of net present value savings if conditions warrant, but it is the intention to generate overall net present value savings equal to at least 3.0% of refunded par amount on any given transaction.

The City may from time to time consider a restructuring of its existing debt. Such restructurings are not subject to the net present value savings threshold identified above, but should be undertaken only rarely and the rationale and possible ramifications explained fully to the City Council.

**Capital Improvement Program Guidelines**

The City will develop a Five-Year Capital Improvement Program annually. The first year of this plan will be approved and appropriated by the City Council after legal advertising and public hearing requirements have been met.

The City will continue to enhance the level of pay-as-you-go funding in the annual Capital budget as a means of reducing reliance on debt financing for capital projects.

The City will maintain its physical assets at a level adequate to protect the City's capital investment and minimize future maintenance and replacement costs. The operated budget will provide for the adequate maintenance of these facilities and infrastructure.

## Retirement System Funding

**The City will use an actuarially-accepted method of funding its City managed pension systems to** achieve a fully-funded status and will continually strive to attain fully-funded pensions.

## Other Post-Employment Benefits (OPEB) Funding

The City will implement the accounting precepts of the Governmental Accounting Standards Board's Statement #45 and, if required, Statement #43. A funding strategy will be developed that sets aside resources to pre-fund OPEB liabilities on an actuarially sound basis over time, although as of the effective date of these Financial Policies, the City has no plans to establish an irrevocable trust fund to accumulate assets. In light of ongoing discussions regarding national health care, the City will determine the utility of a trust fund at a later date and amend these Financial Policies as necessary once a final decision regarding the establishment of a trust fund is made.

### Investment Policy

By State statute, the City Treasurer is responsible for the investment of the City's operating and bond funds consistent with the Code of Virginia. The Treasurer operates under a written investment policy that provides policy guidance on the placement of investments.

In addition to the functions of the City Treasurer, City Staff will annually review the investment program of the City. The City's Financial Advisor shall prepare, in consultation with Staff, an "Annual Investment of City Funds" report to be delivered within three months of the close of the Fiscal Year. This report will analyze, amongst other items:

1. Compliance with adopted investment policy guidelines;
2. Diversification of investments;
3. Concentration of trades with broker-dealers; and
4. Benchmarking of investment return performance against relevant peer comparisons.

## Special Revenue / Enterprise Funds

It is the general policy of the City to avoid designation of discretionary funds in order to maintain maximum financial flexibility. The City may, however, create dedicated funding sources when there are compelling reasons based on state law or policy objectives. Polices will be developed for the use of each fund.

## OVERSIGHT

### Independent Audit

The City will be audited annually by an independent external auditing firm that specializes in independent financial and compliance auditing services. The audit will comply fully with the Code of Virginia, Generally Accepted Accounting Principles ("GAAP"), and federal requirements for "Single Audit."

The City will rotate external auditing firms not less than once every five (5) years.