

CITY COUNCIL COMMUNICATION



MEETING DATE: February 2, 2010 **ITEM NUMBER:** 4A
TYPE OF ITEM: Study Session
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SUBJECT/AGENDA TITLE: Fiscal Sustainability

EXECUTIVE SUMMARY: This agenda item will cover two topics that were unable to be covered at the City Council Retreat: Rainy Day Fund and Fiscal Transparency. Information included below is the same as was included in the Council Retreat binder.

COUNCIL OPTIONS: Direct staff as to the desired size of the City's emergency reserve or on the desire to create a separate Rainy Day Fund and/or a formal policy on the level and use of fund balance in the General Fund.
Direct staff as to whether to further pursue fiscal transparency.

RECOMMENDED OPTIONS: Direct staff to bring back a proposed formal policy on the level and use of fund balance in the General Fund after the completion of the 2009 CAFR (Comprehensive Annual Financial Report).

FISCAL IMPACT & FUND SOURCE FOR RECOMMENDED ACTION: N/A

BACKGROUND AND ISSUE ANALYSIS:

Rainy Day Fund

The term "rainy day fund" is not a technical term that can be found in the formal statements of the Government Accounting Standards Board (GASB) who set the accounting standards which Longmont is bound to follow. Nevertheless, the term "rainy day fund" is widely used in government and it commonly refers to some sort of contingency fund or stabilization account that can provide a financial cushion in emergency situations or when revenue shortages or budgetary imbalances arise. A rainy day fund could be the amount of emergency reserves maintained in the General Fund or it could be a separate fund.

Longmont has had a financial policy that requires an unappropriated reserve in the General Fund for over twenty-five years. Two years ago the amount of that reserve requirement was increased from 6% to 8% of the General Fund operating budget. This policy is shown as indicator #1 on the chart on Attachment A.

The Government Finance Officers Association (GFOA) is a professional association of state and local finance officers in the US and Canada whose members are dedicated to the sound management of government financial resources. The GFOA provides leadership to the government finance profession through research, education and recommended practices. Attachment B is the recommended practice from the GFOA issued in 2002 on the appropriate levels of unreserved fund balance in the General Fund. Within it, GFOA recommends, at a minimum, an unreserved fund balance in the General Fund of no less than five to fifteen percent of regular General Fund operating revenues, or of no less than one to two months (8.3% to 16.6%) of regular General Fund operating expenditures. Due to the issuance of a new GASB Statement No. 54 on Fund Balance Reporting this recommended practice was reissued this past October as a Best Practice with a new recommendation of no less than two months



(16.6%) of operating revenues or operating expenditures. In our annual adopted budget operating revenues and expenditures are always equal so the measurement of either is the same. This is indicator #2 on the chart on Attachment A and it shows that over the past five years we exceeded the recommended best practice except for year-end 2008 which was slightly below it.

Bond rating agencies look at a number of different indicators when they perform a rating analysis of a municipal entity. Guidelines from Moody's and Standard & Poors from back in 2005 were similar to the 2002 GFOA guidelines ranging from 5% to 15%. In fact, S&P indicated that high fund balances could be an indicator that ongoing maintenance and capital needs are not being met and could require large dollar needs down the road.

The rating agencies look to measures such as total assets, current assets, total debt outstanding and debt coverage. They also have their own tests of an entities fund balance. In early 2009, Moody's released their 2008 Local Government National Medians. In regards to the fund balance of a General Fund, they measure it in two ways: the total General Fund fund balance as a percentage of revenues; and the unreserved undesignated General Fund fund balance as a percentage of revenues. Regarding the latter indicator, their glossary states that "in some cases" the unreserved, undesignated fund balance may include certain amounts shown as reserves or designations that Moody's analysts have deemed would be available to meet operating contingencies. We believe that this probably would make this the same measurement as the GFOA Best Practice definition. The median results for these indicators from Moody's were:

	<u>All Cities</u>	<u>All Aa Cities</u>	<u>All Aa cities Population 50-100K</u>
General Fund fund balance as a percentage of revenues	29.76%	29.81%	32.63%
Unreserved fund balance & TABOR reserve as a percentage of revenues	24.50%	25.12%	26.57%

These two indicators are #3 and #4 on the chart on Attachment A. Longmont has not reached these median levels in any of the years presented. It is important to realize that these are median figures as opposed to best practices. Since these are median results, there are cities within the same Aa bond rating as our own that fall below the stated medians. The greater concern is that the direction of our trend in these indicators has been downward over the five year period.

The final indicator shown is a measurement of the unreserved, undesignated fund balance as a percentage of revenues. While this is not necessarily a best practice measurement or a benchmark indicator, it is of note that this measurement has dropped to all time low levels in recent years. The significance of this measure is that the unreserved undesignated fund balance of the General Fund is typically the starting point for what is available for capital and one-time expenditures in the subsequent year budget process. Capital and one-time expenditures are a key component of the resources in our annual budget that allow the essential city services to be provided to the citizens of Longmont. In order to meet these needs this percentage should be a minimum of 5% and preferably as high as 10%.

Attachment C includes data on minimum fund balance polices for other Colorado cities. This data has been collected in different efforts over the past two years so some of it could be outdated. Generally, the smaller the City the larger the policy that may be in place. This is partially because of the size of the budgets. It is also a reflection of the stability of the revenue base. The more stable the revenue base is, the lower the reserves are. Likewise, cities that are reliant on property tax are able to have lower reserve policies than sales tax reliant cities. While we do have the minimum fund balance percentage for each of these cities it is not likely that all of them are consistent in how they define the measurement of the reserve. In Longmont, our 8% applies only to what we specifically set aside as an emergency reserve. But as shown in indicators #2 and #3 on the chart on Attachment A, if other components of the fund balance are also considered our fund balance percentage rises considerably.

TABOR requires that the city have an emergency reserve of 3% of total "fiscal year spending". "Fiscal year spending" in TABOR is a complicated definition, but it involves most all of the governmental fund (non-enterprise) revenue (as opposed to spending). Based on 2008 revenue, this reserve was just over \$3 million for 2009. Currently, we account for all of that reserve in the General Fund although it would be possible to allocate it across the other governmental funds that maintain operating reserves. We also choose to include the TABOR reserve within our total 8% reserve requirement dictated by our financial policy. Thus there is over \$1.8 million designated

for emergencies within the General Fund 2008 fund balance. Combined, these two amounts make up the 8% emergency reserve of \$4,884,520 in the 2009 General Fund.

The TABOR reserve has restrictions that limit its use and make it almost impossible to use. It can only be used for "emergencies" which is defined to exclude economic conditions, revenue shortfalls and salary or benefit increases. Since the reserve has to be in place each year, effectively, if any of the reserve were to be used for an allowable emergency during any fiscal year, it would need to be replenished by year-end anyway.

In addition to the 8% reserve in the General Fund, there is a fund balance in the Health Benefit Fund of over \$6 million. From the early 1980's through 2006 the City operated a self insured employee health and dental benefit program. Since 2007, the City has been fully insured for its health benefits but it still continues the self insured dental program. When the self insured health program terminated in 2006, the fund balance of the fund was \$6.8 million. Besides the self insured dental program the City also pays for EAP services and premiums for vision, long term disability and life coverage from this fund. These costs are budgeted to be covered by city and employee program contributions. Expenditures that draw down the fund balance are for wellness incentives and the amortization of an OPEB (other post employment benefit) liability from a partial subsidy of retiree health care premiums. Additionally, in 2010, this fund will transfer \$490,666 to the General Fund to cover the cost of increased contributions to the general employees defined benefit retirement plan.

While the fund balance in the Health Benefit Fund is technically not an emergency reserve or a rainy day fund, it does present similar opportunities. There will be a continual need for some of the balance to be available to cover some of the minor costs related to wellness and the OPEB liability (these annually combine to be \$200,000 but could grow to over \$300,000). As long as it exists without a stated intended use it certainly serves the purpose of a rainy day fund. If there were to be an emergency or catastrophe causing a dire need for funds staff would probably recommend consideration of this fund balance.

As the 2009 Comprehensive Annual Financial Report is prepared, the staff plans to implement the new requirements of the GASB Statement No. 54 on Fund Balance Reporting. This will change some of the terminology and classification of the reserves and designations in the General Fund fund balance. After its completion in the second quarter it would present an opportune time to propose a more comprehensive formal policy on the level and use of the fund balance in the General Fund. This would put the City in a better position of compliance with the GFOA Best Practice and would be an opportunity for the City Council to change the reserve targets if it sees fit.

Fiscal Transparency

Two government entities in Colorado have recently implemented fiscal transparency efforts where detailed financial information is accessible through their web pages. Staff reviewed the capabilities of these efforts and the resources that could be needed to do the same in Longmont.

Fort Collins - The City of Fort Collins offers what they call "Open Book" which is an online spending transparency database that allows residents to view all City spending records. Open Book can be accessed at the following web address <http://www.fcgov.com/openbook/> . It includes data for the City of Fort Collins, the Poudre River Library District, Poudre Fire Authority and the Downtown Development Authority. Open Book includes all expenditures, except for information restricted by the Health Insurance Portability and Accountability Act (HIPAA) or other confidential information. It includes expenses paid directly to vendors as well as those made with a City credit card. Also provided is a listing of the prior annual wages by position title.

Their information can be browsed by:

- ◆ Vendor (search by alphabetical list or expense amounts)
- ◆ Expense type (choose from nearly 200 categories such as computer software, motor vehicles or wireless service). It provides definitions of these expense types so the user can better understand what they are looking at.
- ◆ Department or service area
- ◆ Fund (choose from 35 fund types, such as the City's General Fund, Natural Areas Fund, Transportation Fund, or Library District Fund).

The current data runs from January 1, 2009 through the present. The database is automatically updated 15 days after the end of each month with the previous month's data. For example, July data is posted on August 15. Open Book will accumulate data for two years; thereafter the database will contain a rolling two year history of data.

Fort Collins reports that it took about 100 hours of staff time to develop their monthly extracts of the ten or so main financial data fields of their JD Edwards ERP system into a data repository inside their web application domain. They used a LAMP software tool to develop the web queries and presentation on their website. The data is not provided in excel or other formats, but instead only in PDF images. The data extraction was the bulk of the effort and the most difficult part of the work, as they needed to put the data in a form that was more useful to citizens, not labeling a department as PW/NR etc. Most of this work was done by a Financial Analyst with strong SQL skills.

Fort Collins staff also stated there have been limited pages viewed by citizens. They use Google Analytics to measure usage. They have discovered that most of the views were from internal sources. They also believe that some of the external views are from staff of other entities (like our own) wanting to "see how transparency sites are designed".

Jefferson County - Jefferson County offers what they call "Transparent Jeffco" which is also an online spending transparency database that allows residents to view their spending records. Their goal is "to provide a rich, interactive citizen engagement." According to the following website <http://www.co.jefferson.co.us/transparentgov/index.htm>, Transparent Jeffco provides easy access to the services the residents of Jefferson County require. Transparent Jeffco is currently a work in progress. They have completed the searchable tool for procurement cards with the rest of the expenditures and budgets due to be available Winter of 2009 (although this information is available in pdf report in the interim). In addition, they provide a listing of contracts and legal notices by month. Their website also provides contact information for all elected officials and department and division directors.

Their procurement card information can be searched by:

- ◆ Transaction date
- ◆ Vendor name
- ◆ Vendor category
- ◆ Transaction description
- ◆ Cardholder office/department/division name
- ◆ Approver title
- ◆ Dollar amount

It has drill-down capabilities to further show the vendor city and state.

The current data runs from May 7, 2009 through current. Data updates occur monthly. Their website does not specifically state how long the data will be available, however, in looking at the searchable transaction date field it appears they are eventually planning on providing up to 5 years worth of data.

They also plan to include more portals into non financial data that would benefit their citizens and save clerical effort as well. To accomplish this, they have developed some online forms, blogs, and survey tools to ask the citizens using the site what data they would like to have. Rather than trying to guess what the public may want, building it at a great cost and then wondering why they are not accessing their screens, they are hoping to get the feedback from the citizens on what they would really want to see. They did not try to do budget vs expense and really had not planned to spend much effort breaking things out by division or department, because they believe the citizens really are not interested in how well one department or division is doing against their budget goals.

They also are doing an analysis on clerical time used to support open records requests to identify the top requests that cost the most to produce, and that will also be used in deciding what else to provide.

The cost of the first phase of this project was approximately 200 hundred man hours. Depending on the cost per hour of programming staff or consultants, that is about \$20,000 for internal staff or \$30,000 for consultants. They have a JD Edwards package that provided much of the automated queries and used an Oracle Application Express forms generation software program to create most of the queries and web content. The APEX software gives them the ability to filter, sort, compute and aggregate data over all years right out of the box.

Longmont – In Longmont we are very close to being able to offer access to most of records in the City Clerk’s office over web access. All monthly financial reports prepared by the Finance & Support Services Department for the City Council as well as annual documents such as the annual budget; five year CIP; the Comprehensive Annual Financial Report (CAFR); and the results of the 2009 budget prioritization process are all accessible over the City’s web page. We currently do not have such access for the detailed financial information within the financial systems of the City as offered in Fort Collins and Jefferson County.

Given that both of these entities needed resources ranging from 100 to 200 man hours it is logical to at least use that as a starting point for our own potential cost estimate. We will need to gather further information from these other entities as well as assess our own systems and solutions to estimate a firm cost for Longmont to provide some sort of financial transparency. We would probably use IBM’s Webquery to retrieve and present our DB2 data. We are meeting with an IBM consultant in January to learn more about that software’s ability to easily mine our general ledger data and present it dynamically on the web. We would not have to have a separate piece of software to access our purchase card data, as that data is already integrated into our database. Unfortunately, we do not know what we would need to build, nor how difficult it would be to build it at this time.

While we do have staff that could work on this project, it would require a re-prioritization of ETS projects that are already slowed due to staffing reductions and unplanned projects that became new priorities. For instance, the collective bargaining agreement required changes to payroll programs. If this becomes a high priority with a desire to have it implemented in 2010 it may be necessary to consider the consultant route so that current project efforts are not further derailed.

ATTACHMENTS:

Attachment A: General Fund Fund Balance Indicators

Attachment B: GFOA Recommend Practice on Appropriate Level of Fund Balance in the General Fund

Attachment C: Minimum Fund Balance Policies for Colorado Municipal Governments

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General Fund Fund Balance Indicators

Fund Balance Breakdown	2004	2005	2006	2007	2008
Reserved for encumbrances	1,713,104	1,735,985	1,162,459	1,046,307	1,708,936
Reserved for TABOR	2,916,360	2,773,219	2,779,156	3,085,410	3,060,058
Reserved for loans/notes receivable	117,770	113,750	106,088	86,345	83,090
Reserved for prepaid expenditures	66,279	71,729	120,334	96,153	66,169
Reserved for staff contracts	100,248	104,532	105,636	111,291	114,489
Reserved for police block grant	9,664	3,408	59,100	63,376	55,879
Reserved for donations	5,048	5,048	5,048	17,750	6,748
Designated for carryover projects	746,230	1,211,068	1,898,536	665,212	795,197
Designated for emergencies	597,930	823,465	764,098	1,626,856	1,824,462
Designated for subsequent years' expenditures	3,944,233	3,892,616	2,613,114	1,850,000	2,608,085
Designated for future Council 1 time exp		993,825	993,825	907,566	407,566
Undesignated	4,285,943	2,171,284	1,128,399	2,426,469	933,219
	\$14,502,809	\$13,899,929	\$11,735,793	\$ 11,982,735	\$ 11,663,898

Indicator #1: City Financial Policy: 8%

TABOR reserve & emergency designation	3,514,290	3,596,684	3,543,254	4,712,266	4,884,520
Subsequent year budget	58,571,496	59,944,727	59,054,241	58,903,325	61,373,394
Emergency reserves as % of subseq. Yr budget	6.00%	6.00%	6.00%	8.00%	7.96%

Indicator #2: GFOA Best Practice: 16.6%

Unreserved fund balance & TABOR reserve	12,490,696	11,865,477	10,177,128	10,561,513	9,628,587
Subsequent year budget operating revenue	54,627,263	56,052,111	56,441,127	56,824,934	58,623,231
Unreserved FB as % of subseq. Yr oper rev	22.87%	21.17%	18.03%	18.59%	16.42%

Indicator #3: Moody's measure: 29.7% to 32.6%

Total fund balance	\$14,502,809	\$13,899,929	\$11,735,793	\$11,982,735	\$11,663,898
Subsequent year budget operating revenue	54,627,263	56,052,111	56,441,127	56,824,934	58,623,231
Total fund balance as % of subseq. Yr oper rev	26.55%	24.80%	20.79%	21.09%	19.90%

Indicator #4: Moody's measure: 24.5% to 26.6%

Unreserved fund balance & TABOR reserve	12,490,696	11,865,477	10,177,128	10,561,513	9,628,587
Subsequent year budget operating revenue	54,627,263	56,052,111	56,441,127	56,824,934	58,623,231
Unreserved FB as % of subseq. Yr oper rev	22.87%	21.17%	18.03%	18.59%	16.42%

Indicator #5

Unreserved undesignated fund balance	4,285,943	2,171,284	1,128,399	2,426,469	933,219
Subsequent year budget operating revenue	54,627,263	56,052,111	56,441,127	56,824,934	58,623,231
Unres undesig FB as % of subseq. Yr oper rev	7.85%	3.87%	2.00%	4.27%	1.59%

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Appropriate Level of Unreserved Fund Balance in the General Fund (2002)

Background. Accountants employ the term *fund balance* to describe the net assets of governmental funds calculated in accordance with generally accepted accounting principles (GAAP). Budget professionals commonly use this same term to describe the net assets of governmental funds calculated on a government's budgetary basis.¹ In both cases, *fund balance* is intended to serve as a measure of the financial resources available in a governmental fund.

Accountants distinguish *reserved fund balance* from *unreserved fund balance*. Typically, only the latter is available for spending. Accountants also sometimes report a *designated* portion of unreserved fund balance to indicate that the governing body or management have tentative plans concerning the use of all or a portion of unreserved fund balance.

It is essential that governments maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. Fund balance levels are a crucial consideration, too, in long-term financial planning.

In most cases, discussions of fund balance will properly focus on a government's *general fund*. Nonetheless, financial resources available in other funds should also be considered in assessing the adequacy of unreserved fund balance in the general fund.

Credit rating agencies carefully monitor levels of fund balance and unreserved fund balance in a government's general fund to evaluate a government's continued creditworthiness. Likewise, laws and regulations often govern appropriate levels of fund balance and unreserved fund balance for state and local governments.

Those interested primarily in a government's creditworthiness or economic condition (e.g., rating agencies) are likely to favor increased levels of fund balance. Opposing pressures often come from unions, taxpayers and citizens' groups, which may view high levels of fund balance as "excessive."

Recommendation. GFOA recommends that governments establish a formal policy on the level of unreserved fund balance that should be maintained in the general fund.² GFOA also encourages the adoption of similar policies for other types of governmental funds. Such a guideline should be set by the appropriate policy body and should provide both a temporal framework and specific plans for increasing or decreasing the level of unreserved fund balance, if it is inconsistent with that policy.³

The adequacy of unreserved fund balance in the general fund should be assessed based upon a government's own specific circumstances. Nevertheless, GFOA recommends, *at a minimum*, that general-purpose governments, regardless of size, maintain unreserved fund balance in their general fund of no less than five to 15 percent of regular general fund operating revenues, or of no less than one to two months of regular general fund operating expenditures.⁴ A government's particular situation may require levels of unreserved fund balance in the general fund significantly in excess of these recommended minimum levels.⁵ Furthermore, such measures should be applied within the context of

¹ For the sake of clarity, this recommended practice uses the terms *GAAP fund balance* and *budgetary fund balance* to distinguish these two different uses of the same term.

² Sometimes reserved fund balance includes resources available to finance items that typically would require the use of unreserved fund balance (e.g., a contingency reserve). In that case, such amounts should be included as part of unreserved fund balance for purposes of analysis.

³ See Recommended Practice 4.1 of the National Advisory Council on State and Local Budgeting governments on the need to "maintain a prudent level of financial resources to protect against reducing service levels or raising taxes and fees because of temporary revenue shortfalls or unpredicted one-time expenditures" (Recommended Practice 4.1).

⁴ The choice of revenues or expenditures as a basis of comparison may be dictated by what is more predictable in a government's particular circumstances. In either case, unusual items that would distort trends (e.g., one-time revenues and expenditures) should be excluded, whereas recurring transfers should be included. Once the decision has been made to compare unreserved fund balance to either revenues or expenditures, that decision should be followed consistently from period to period.

⁵ In practice, levels of fund balance, (expressed as a percentage of revenues/expenditures or as a multiple of monthly expenditures), typically are less for larger governments than for smaller governments because of the magnitude of the amounts involved and because the diversification of their revenues and expenditures often results in lower degrees of volatility.

long-term forecasting, thereby avoiding the risk of placing too much emphasis upon the level of unreserved fund balance in the general fund at any one time.

In establishing a policy governing the level of unreserved fund balance in the general fund, a government should consider a variety of factors, including:

- The predictability of its revenues and the volatility of its expenditures (i.e., higher levels of unreserved fund balance may be needed if significant revenue sources are subject to unpredictable fluctuations or if operating expenditures are highly volatile).
- The availability of resources in other funds as well as the potential drain upon general fund resources from other funds (i.e., the availability of resources in other funds may reduce the amount of unreserved fund balance needed in the general fund, just as deficits in other funds may require that a higher level of unreserved fund balance be maintained in the general fund).
- Liquidity (i.e., a disparity between when financial resources actually become available to make payments and the average maturity of related liabilities may require that a higher level of resources be maintained).
- Designations (i.e., governments may wish to maintain higher levels of unreserved fund balance to compensate for any portion of unreserved fund balance already designated for a specific purpose).

Naturally, any policy addressing desirable levels of unreserved fund balance in the general fund should be in conformity with all applicable legal and regulatory constraints. In this case in particular, it is essential that differences between GAAP fund balance and budgetary fund balance be fully appreciated by all interested parties.

Approved by the Committee on Accounting, Auditing and Financial Reporting and the Committee on Governmental Budgeting and Management, January 30, 2002

Approved by the Executive Board, February 15, 2002.

Minimum Fund Balance Policies for Colorado Municipal Governments

Central City	5%
Arvada	8%
Longmont	8%
Boulder	10%
Commerce City	10%
Lakewood	10%
Westminster	10%
Woodland Park	10%
Broomfield	10% to 16.67%
Golden	10% to 20%
Fort Collins	15%
Louisville	15%
Parker	16.67%
Fountain	20%
Thornton	20%
Evans	25%
Brighton	25%
Greenwood Village	25%
Lafayette	25%
Northglenn	25%
Ouray	25%
Estes Park	30%
Gunnison	33%
Crestone	50%
Superior	75% to 100%
Westcliffe	200%