



CITY of NOVI CITY COUNCIL

Agenda Item 2
September 12, 2011

SUBJECT: Approval to amend the City's Fund Balance/Reserve policy to include certain Special Revenue Funds and the Capital Replacement Reserve policy for the Enterprise Funds (in addition to the General Fund-Fund Balance policy).

SUBMITTING DEPARTMENT: Managers/Finance

CITY MANAGER APPROVAL: 

BACKGROUND INFORMATION:

Special Revenue Funds are restricted by the nature of the funds. However, the timing of the use of the funds, and the minimum balance in certain funds (i.e. minimum for contingencies for road funds) has been determined through the budget process, including discussions and input from the Leadership Team, as well as computations and projections by the Finance Department.

The Capital Replacement Reserve policy for the City's Enterprise Funds mirrors policies in the private sector which are approved by the governing body (i.e. Association Board, Board of Directors, etc.).

The Finance staff uses the enclosed procedures during the budget preparation process, and pursuant to your request, have prepared the attached information for purposes of consideration by City Council for a formal resolution for funds other than the General Fund.

Separately, in March 2009, the Governmental Accounting Standards Board issued Statement No. 54 Fund Balance Reporting and Governmental Fund-type Definitions. The objective of this statement is to enhance the usefulness of fund balance information by providing clearer fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds. Under this standard, the fund balance classifications of reserved, designated and unreserved will be replaced with five new classifications: non-spendable, restricted, committed, assigned and unassigned. The City will be implementing Statement 54 with the comprehensive annual financial report (CAFR) for the year ended June 30, 2011. For purposes of the City's budget, generally "fund balance" refers to the total fund balance inclusive of all of the five new classifications.

Pursuant to GASB 54, the formal policy adopted by City Council for minimum fund balance will be included in the notes to the financial statements in the City's Comprehensive Annual Report.

The Library and Walker Fund – Fund Balance policy will be presented based on a recommendation by the Library Board. Attached is the memorandum requesting policy direction and recommendation from the Library Board.

Attached is the amended Fund Balance/Reserve policy for City Council’s consideration.

RECOMMENDED ACTION:

Approval to amend the City’s Fund Balance/Reserve policy to include certain Special Revenue Funds and the Capital Replacement Reserve policy for the Enterprise Funds (in addition to the General Fund-Fund Balance policy).

	1	2	Y	N
Mayor Landry				
Mayor Pro Tem Gatt				
Council Member Fischer				
Council Member Margolis				

	1	2	Y	N
Council Member Mutch				
Council Member Staudt				
Council Member Wrobel				

Fund Balance/Reserve Policies

- The City will establish a reserve to pay for expenditures as a result of unforeseen emergencies or for shortfalls caused by revenue declines. The City will seek to maintain a diversified and stable revenue system to shelter itself from short-run fluctuations in any one revenue source. The City will attempt to obtain additional revenue sources to insure a balanced budget.
- The City will follow an aggressive policy of collecting revenue.
- The City will establish all user charges and fees at a level considering the cost (operating, direct, indirect and capital) of providing the service.
- The City will establish reserves to comply with the terms and conditions of the debt instruments used to finance capital improvement projects.
- The City will review fund balance/reserves annually during the budget process.
- In the event the level of expenditures exceeds the estimated appropriations, the City will create a plan to replenish fund balance/reserves within three years by controlling operating expenditures, adjusting operations and/or dedicating excess or specific revenue sources.

General Fund

For the General Fund, the reserve will be maintained at an amount that represents approximately 18-22 percent of the budgeted expenditures as adopted by City Council Resolution, January 24, 2011. Additional reserves can be designated for a specific purpose as identified by City Council during the budget process. Fund balance will be established to:

- Provide a fund or reserve to meet emergency expenditures;
- Provide cash to finance expenditures from the beginning of the budget year until general property taxes or other revenues are collected;
- Demonstrate financial stability and therefore preserve or enhance its bond rating, thereby lowering debt issuance costs;
- Accumulate sufficient assets to make designated purchases;
- Avoid short-term borrowing and associated interest costs.

As part of the budget process excess fund balance may be used to reduce liabilities or fund expenditures of the next fiscal period.

Special Revenue Funds

Resources in a fund other than the general fund are either (1) required to be used for the purpose of the fund or (2) intended by the government to be used for that purpose. Special revenue funds report specific revenue sources that are limited to being used for a particular purpose.

Road Funds (Major, Local and Municipal Street)

The City's fund balance for the road funds will be established within a minimum range of 10-20%, individually and collectively amongst the three funds, to cover extraordinary maintenance events (i.e. unusual winter maintenance events, emergency reconstruction, etc.), and contingencies for budgeted construction projects. In addition, the City **may**

establish a designation for capital projects in excess of \$1.5 million, to be completed in future years based on the capital improvement program.

Police and Fire Fund

The fund balance for the Police and Fire Fund will vary, based on future major fire equipment capital needs and operational costs for the Police and Fire departments. The City will look at both major fire equipment needs and operational expenditures for a 3-10 year period in the future. The revenue from the special voted property tax millage for this fund is transferred to the General Fund to support police and fire department expenditures based on the future outlook.

Drain Funds (Drain Revenue and Drain Perpetual Maintenance)

The Drain Revenue Fund reports the City's special property tax millage for the drain system. The Drain Perpetual Maintenance Fund revenue resources are from connection tap fees. The City's has a combination drain system, regional and site, resulting in the two types of revenue sources. The revenue from these funds is intended to cover the maintenance, construction and repairs of the drain system. The system includes basins and structures with other entities administered by Oakland County, with two of the larger systems being Caddell and Randolph.

The City's fund balance for the drain funds will vary as these funds are intended to be sufficient to cover current and future costs of the system given the limitation on the tap fee revenue source. In addition to annual maintenance, significant expenditures include construction and repair of large basins, lake dredging and shared systems. The City monitors and reviews future projects annually during the budget process, and reports the next six years projects in the Capital Improvement Program.

Parks, Recreation and Cultural Services Fund

The fund balance for the Parks, Recreation and Cultural Services Fund will be established within a minimum range of 12-22% of fund annual budgeted expenditures, since this fund is similar to the General Fund in terms of covering operations. This fund reports two major sources of revenue: special voted property tax millage and program revenue. The City **may** establish a designation for capital projects in excess of \$300,000; to be completed in future years based on the capital improvement program.

Special Assessment Revolving Fund

The fund balance for the Special Assessment Revolving Fund will be used for future reconstruction and maintenance of City roads. The fund's resources are primarily from interest from special assessment construction and debt service funds. The fund balance is recommended to be at least \$1,000,000 until special assessment funds created prior to 2000 are closed, and at least \$500,000 until the 2003 Special Assessment District Limited Tax Bonds are paid in full, or collections are sufficient to cover the repayment of the bonds.

Other Special Revenue Funds

The fund balance for other special revenue funds (Forfeiture Funds, Tree Fund, Contributions and Donations Fund) will be used for appropriations based on the specific purpose of those funds.

Capital Replacement Reserve Policy – Enterprise Funds

The City has established Capital Replacement Reserve accounts in each of its three Enterprise Funds.

The key Capital Replacement Funding principle is that the money is collected and segregated, over a period of time, to cover the repair or replacement cost of existing

common elements; that is, capital assets already in existence (for example, the replacement of an existing HVAC system, roof, parking area, etc.). Capital Replacement Funds are part of a long-term financial plan, which helps:

- Strengthen the community's fiscal health
- Increase the market value of units
- Provides stability to avoid large future assessments or rate increases

User charges and fees will be computed based on current year operating expenses, debt service requirements and annual contribution/replenishment of the capital replacement reserve.

The City will conduct a Capital Needs Assessment and Replacement Reserve Analysis for the Ice Arena and Meadowbrook Commons facilities every 5-7 years. The user charges and fees will include annual contribution/replenishment of the capital replacement reserve. Cash and investments for operations will be computed based on a minimum of two months expenditures.

The Capital Replacement Reserve for the Water & Sewer Fund is targeted at 10-25% of the current fair market value of water and sewer infrastructure assets. The City uses the overall national CPI to compute the fair market value of these assets. Cash and investment balances for operations will be computed based on a minimum of two months expenditures plus planned capital improvement projects of \$10 million or less for the year.

MEMORANDUM



TO: JULIE FARKAS

CC: CLAY PEARSON
VICTOR CARDENAS

FROM: KATHY SMITH-ROY

SUBJECT: LIBRARY & WALKER FUND – FUND BALANCE POLICY

DATE: SEPTEMBER 8, 2011

The City Council is considering a policy amendment to the Fund Balance/Reserve policy on the September 12, 2011 agenda to include Special Revenue Funds (the Library and Walker Funds are Special Revenue Funds). Pursuant to the City Charter, the City Council levy's the primary source of revenue, property taxes. The Library Board "controls" expenditures (see Charter excerpt at end of this memo). Since Fund Balance is in part a function of the difference between revenue and expenditures, the City administration request the Library Board consider the following Fund Balance policy and provide a recommendation for Fund Balance/Reserve policy for the Library and Walker Funds to City Council.

Library & Walker Library Funds

The fund balance for the Library Fund will be established within a minimum range of 12-22% of fund annual budgeted expenditures, since this fund is similar to the General Fund in terms of covering operations. A new library facility was completed in 2010, more than doubling the square footage of the space of the former building. The City did not propose any additional operating millage, and therefore the Library Fund has carried a much higher fund balance than the minimum range to provide for future operating costs. The Library Fund is intended to report the special voted property tax millage for the library and general operating expenditures. The Walker Fund was created in 2004 to record donation revenue, and was established with the receipt of the generous initial gift of \$1,000,000 from Charles and Myrtle Walker for use in the replacement or expansion of the existing Library building. The Walker Family also matched donations of other donors over a one-year period. The Library Board also entered into a Library Building Fund Gift Agreement with the Walker family to encourage additional donations. This fund balance from this fund will be used to support library operations into the future.

If you have any questions, or need any additional information, please let me know.

Section 19.3 Library Fund

The council may levy a tax not to exceed one (1) mill on the dollar annually on all taxable property in the city, such tax to be levied and collected in like manner with other general taxes of the city, to be known as the "library fund."

Sec. 19-21 Appointment of members

The mayor shall, with the approval of the council, appoint a **library** board of seven (7) directors, chosen from the citizens at large, with reference to their fitness for such office. Not more than one (1) member of the council shall be at any one time a member of the board of directors.

Sec. 19-21 Appointment of members

The **library** board of directors shall:

- (1) Immediately after appointment as the first board of directors and annually thereafter, meet, organize and elect from their numbers a president, a secretary and a treasurer and such other officers as they deem necessary;
- (2) Make and adopt such bylaws, rules and regulations for their own guidance and for the government of the **library** and reading room as they may deem expedient, not inconsistent with the statute, charter or this chapter;
- (3) Have the exclusive control of the expenditure of all moneys collected to the credit of the **library** fund, and of the construction of any **library** building, and of the supervision, care, and custody of the grounds, rooms or buildings constructed, leased or set apart for that purpose; provided, that all moneys received for such **library** shall be deposited in the treasury of the city to the credit of the **library** fund and shall be kept separate and apart from other moneys of the city, and drawn upon by the proper officers of the city, upon the properly authenticated vouchers of the **library** board of directors;
- (4) Have the authority to retain funds in a special bank account for the purpose of maintaining a petty cash account to be managed by the **library** administrator, and may requisition the city treasurer for funds accordingly. The petty cash account shall not exceed an amount set by resolution of the council, and may only be used for the payment of small charges and expenses as authorized or ratified by the majority action of the **library** board of directors. The **library** administrator shall provide the board with a monthly report of expenditures or disbursements from the petty cash account;
- (5) Have exclusive care and custody of the grounds, rooms or buildings constructed, leased or set apart for that purpose;
- (6) Have power to appoint suitable personnel and fix their compensation, and shall have power to remove such appointees;
- (7) Maintain a public **library** and reading room for the inhabitants of the city;
- (8) In general, carry out the spirit and intent of the statute and City Charter provisions under which the public **library** and reading room is established;
- (9) At the end of each and every year from and after the organization of the **library**, make a written report to the council stating the condition of their trust at the date of such report, the various sums of money received from the **library** fund and other sources, and how such moneys have been expended and for what purposes, and all other details and information as required by statute. (*Ord. No. 83-109, § 9.01, 5-2-83*)