IN CITY COUNCIL

Marlborough, Mass., MAY 8, 2017

ORDERED:

Suspension of the Rules requested – granted

That the attached Review & Approval of Financial and Investment Policies, be and is herewith **APPROVED**.

ADOPTED
In City Council
Order No. 17-1006888A

Approved by Mayor
Arthur G. Vigeant
Date: May 11, 2017

TRUE COPY
ATTEST:

City Clerk

Financial Policies

Introduction

Financial policies set the boundaries within which financial decisions are made by governments. Unlike the budget adopted for a single fiscal year, financial policies are long-range in nature. They are carried over from one year to the next, adding continuity and stability to a government's financial structure.

Financial policies can also serve as the foundation for a government's long-range financial plan. By adopting and adhering to these policies Marlborough will improve its ability to provide a level and quality of services it can afford while protecting and improving the public health, safety, education and general well being of its citizens. Adherence to proper financial policies will help Marlborough develop flexibility to withstand external economic, environmental or other shocks or disruptions caused by factors over which it has no control while meeting the demands and challenges of natural growth, decline and change within the community.

Budget Policies

- Budget Policy 1: Marlborough will develop balanced budgets in which current revenues (non-one-time) equal or exceed current expenditures.

- Budget Policy 2: Marlborough will not balance the budget by using one time revenues to fund ongoing expenditure items.

- Budget Policy 3: Marlborough will not use budgetary procedures that balance the budget at the expense of meeting future years expenses, such as: postponing or deferring expenditures, accruing future year revenues, or rolling over short-term debt.

The purpose of Budget Policies One, Two and Three is to prevent the use of procedures that appear to balance the budget at the expense of our future. Delaying building and equipment maintenance or postponing the cost of operations are two of the most common procedures used to artificially create the appearance of a balanced budget. These actions merely pass today's costs onto future taxpayers and residents, and these costs usually grow as they are deferred.

Budget Policy One was developed to ensure that Marlborough does not spend more than it receives in revenue in any one year and therefore does not degrade its overall financial condition. This ensures that Marlborough does not "live beyond its means" and build a structural deficit into its budget.

Budget Policy Two helps ensure that Marlborough does not use one-time revenue to support ongoing operations. Simply put, this policy prevents the use of temporary funding to support ongoing needs. Such expenditures are considered unadvisable because the ongoing expenditure need will still exist after the non-recurring revenue disappears. Use of non-recurring revenue for recurring purposes only delays appropriate action to correct what would otherwise be a budget imbalance.

Budget Policy Three prevents the use of gimmicks such as expenditure deferral, booking future revenue in the current fiscal year or the inappropriate rolling over of debt. These fiscal maneuvers generally occur in times of poor financial performance and only serve to delay necessary expenditures and increase the overall cost for a community.

- Budget Policy 4: The budget proposed to Marlborough shall include the following sections: a summary of Marlborough's financial condition, an analysis of revenues used in the proposed budget, an analysis of outstanding debt and a summary of Marlborough's capital condition (buildings, infrastructure, rolling stock and information technology).

- Budget Policy 5: Marlborough's annual budget shall be presented by the Mayor and accepted by the City Council.

Budget Policies Four and Five guide the development of Marlborough's annual budget. Budget Policy Four requires that certain information be provided to Marlborough's City Council and the public along with the budget. This policy mandates communication with the City Council regarding the most pressing financial issues before Marlborough – overall fiscal condition, debt, revenues and capital needs and condition. This information will allow the City Council to make decisions on the annual budget with necessary information regarding Marlborough's overall financial condition, the condition of our capital assets and other matters of importance.

Budget Policy Five sets forth the form of budget passage by Marlborough's City Council. This provides the City Council with maximum oversight with regard to budgetary expenditures but permits some level of flexibility to departmental managers by allowing them to transfer funding among certain line items previously approved by Marlborough's City Council.

- Budget Policy 6: The budget will provide for adequate maintenance and the replacement of capital plant and equipment. All budgetary procedures will conform with existing state and local regulations.

Budget Policy Six ensures that the annual operating budget funds necessary maintenance and capital investment. The capital investment portion of this policy will take time to be fully enacted this policy will help ensure that necessary maintenance is conducted.

Required maintenance is critical if our taxpayers are to receive the maximum return on their dollars invested. The delay in routine maintenance to a roof, for instance, may lead to the premature replacement of the roof and also avoidable damage within the building. Budget Policy Six is intended to prevent this.

- Budget Policy 7: Marlborough's City Auditor shall issue a monthly report on revenues and expenditures (at the line item level). This shall be provided to the Mayor and the City Council.

Budget Policy Seven provides a tool for Marlborough to monitor expenditures and ensure that revenue projections are being met. Provision of this information is necessary to ensure accountability and allow the City to react promptly to unforeseen events and prevent problems from going unnoticed by the public and policymakers.

Revenue Policies

- Revenue Policy 1: Marlborough's annual budget shall include a revenue budget that is created in line item detail formatted consistent with the recap for Marlborough operations.

- Revenue Policy 2: Marlborough will estimate its revenue with conservative methods and present this along with the balanced budget.

- Revenue Policy 3: Marlborough shall review and update the fee schedule of each of its departments no less than every three years to ensure that costs of service are being fully recovered.

Significant attention is provided to Marlborough's expenditure budget to ensure that taxpayer money is expended prudently and in a cost-effective manner. Marlborough's revenue budget is equally as important; this budget provides the funding that is detailed in the expenditure budget. Marlborough can not expend more money than it expects to receive in revenue in the course of a year and therefore the manner in which revenue is estimated is very important.

Revenue Policy One ensures that Marlborough's revenue projections will be provided to the City Council and the public along with the expenditure budget. This will facilitate an examination of the procedures used to estimate revenue as well as provide information to the public regarding Marlborough's revenue condition.

Revenue Policy Two ensures that revenue estimation will be conducted prudently, in a conservative manner. Overly optimistic estimates can create the appearance of a balanced budget when in reality a deficit will result. According to Massachusetts Finance Statutes, any deficit that remains at the end of one fiscal year will be automatically deducted from the budget of the next; overly optimistic revenue estimates will drive reduced public spending in the next fiscal year. Underestimation of revenue can also present problems as it prevents revenue from being used to benefit the public in the year it was raised.

Many services provided by Marlborough benefit all residents, though others benefit only the specific users of service (building inspections, water and sewer hook-ups, marriage licenses). Revenue Policy Three is designed to ensure that user fees – fees charged for specific services provided to individuals – cover the costs of providing those services.

- Revenue Policy 4: Marlborough may build into its revenue base from one fiscal year to the next an increase in each revenue category of no more than 4.5%, with the exception of real and personal property taxes, chapter 70 (school aid) and MSBA (Massachusetts School Building Assistance) and water and sewer.

- Revenue Policy 5: Any revenue increase in excess of this 4.5% shall be considered upwardly volatile revenue and may only be expended to increase reserve fund levels, applied towards the OPEB liability, or to fund non-recurring capital expenditures .

Revenue Policies Four and Five relate to "upwardly volatile revenue". In brief, upwardly volatile revenue occurs when one or more revenue sources increase at an atypically fast rate. The danger of upward revenue volatility is that a community can become dependant on an artificially high level of revenue that exists merely because of a strong economy. This revenue may decrease sharply or disappear entirely when the economy contracts, leaving critical services under funded if the upwardly volatile revenue was not used wisely.

Revenue Policy Four prevents Marlborough from building into the "base" of its revenue model an increase in any source of greater than 4.5%. Property tax revenue is excepted from this limitation because it is already limited – to a lower level – by Proposition 2 ½ . Chapter 70 school aid and school building assistance are also exempt from this limitation because they are provided by the Commonwealth for a specific purpose and can not be redirected for any other use.

Revenue Policy Five limits the use of upwardly volatile revenue to ways that will prevent Marlborough from relying on unstable revenue while simultaneously strengthening Marlborough's financial position. Use of this revenue to build reserve fund balances will help Marlborough prepare for cyclical revenue contractions while strengthening our financial condition and giving us much-needed financial flexibility. Use of this revenue to make non-recurring capital investments will provide a service benefit to our taxpayers by improving our physical infrastructure. It will also develop a reserve fund by allowing us to "get ahead" of our capital plan. This will allow Marlborough to reduce its future capital investment needs if necessary, saving operating money without impacting our long-term capital plan.

- Revenue Policy 6: Marlborough will maintain property assessment for the purpose of taxation at full and fair market value, as prescribed by State law.

Revenue Policy Six ensures that Marlborough continues to regularly assess the value of property in Marlborough. Regular reassessments are required by Massachusetts Finance Statutes and are critical to ensuring the fairness of our system of property taxation.

Policies With Regard to Self-Supporting Operations

- Self-Supporting Policy 1: The Director of Public Works shall annually recommend to the Mayor rates and fees for the Water and Sewer Departments, with the final approval of the Mayor.

- Self-Supporting Policy 2: Rate and fees proposed for the Water and Sewer Departments shall include all direct and indirect costs (such as the costs of payroll, property and liability insurance, legal services, etc.).

Self-supporting operations are generally those that provide specific benefits to individual service users without assisting the public in general. Because benefits accrue to individuals and not the general public, these services should be paid for entirely by service users through user fees, not through general tax revenue. Use of general tax revenue to support these services forces all residents to help pay for services (and therefore benefits) that accrue to certain individuals, not everyone. Tax dollars should not be used to finance operations that can and should be self-supporting because this drives a reduction in other government services.

Self- Supporting Policy One requires that rates and fees in the Water and Sewer Departments be submitted and reviewed annually by the Mayor.

Self-Supporting Policy Two requires that rates and fees for the Water and Sewer Departments reflect the true and total cost of providing those services. This is intended to prevent these operations from forcing costs upon the general taypayer who may not receive the benefit of these services. A corollary to this is that the rates and fees for these departments should not provide for the appropriation of money to the City's General Fund, as to do so would force an undue burden on ratepayers in excess of those needed to provide the service they are receiving.

Capital Planning Policies

Capital planning and budgeting is central to economic development, transportation, communication, delivery of essential services, environmental management and quality of life of our citizens. Much of what is accomplished by local government depends on a sound long-term investment in infrastructure and equipment. In that regard, the City recognizes conditions that necessitate capital intervention and include:

- *Imminent threat to the health and safety of citizens/property*
- *Preservation of operations*
- *Legal requirement of Federal or State agencies*
- *Improvement of infrastructure*
- *Improvement in the efficiency and effectiveness of service delivery*
- *Alleviation of an overtaxed/overburdened situation*

The City endeavors to conduct the following to satisfy these objectives:

- Capital Policy 1: The Capital Improvement Program will directly relate to the long-range plans and policies of the City.

- Capital Policy 2: A five-year Capital Improvement Plan shall be proposed by the Mayor to the City Council annually. The first year of the Capital Improvement Plan shall include the proposed capital improvements for the forthcoming fiscal year.

- Capital Policy 3: Except as required by an emergency, all approved capital projects must be part of the adopted Capital Improvement Plan.

Capital Policy One merely states that the Capital Improvement Plan (CIP) must conform to the policies and long-term plans of the City. The Plan must be consistent with our financial plans – it can not cause annual debt levels to exceed the City's debt ratio included in the City's debt policies and should meet the items highlighted above. Conformance with municipal policies and long-term plans will ensure this occurs.

Capital Policy Two requires that the CIP be a five-year plan that is updated annually and submitted to the City Council each year. This plan shall be created by the Mayor and Capital Planning Committee. The CIP is a "rolling plan" such that the first year of the plan is always the upcoming year, and years two through five represent the next four years. In this manner the CIP always looks ahead four years, facilitating the planned and rational replacement, upgrade and acquisition of capital.

Capital Policy Three requires that all capital projects approved for funding be part of the CIP. The CIP is a long-term document that will facilitate planning and improve the means by which capital investment decisions are made. Funding items that are not in the CIP will undermine the effectiveness of the CIP and will likely result in inefficiency. Capital investments can often be made in ways that are complimentary to each other, reducing cost or inconvenience through proper sequencing. Funding capital projects that have not been approved through the capital improvement process, will likely lead to inefficiency; and will undermine the City's effort to rationally plan for its future and long-term growth.

- Capital Policy 4: The Capital Improvement Plan shall include a multi-year forecast of annual debt service requirements of items in the Plan to permit the examination of the future implication of debt issuance.

- Capital Policy 5: Decisions to undertake specific capital improvements shall include in their analysis the identification and cost estimation of additional operational funding and personnel requirements.

- Capital Policy 6: All proposals for capital improvements shall include sources of funding for each capital improvement or category of capital improvement. Pay-as-you-go capital funding (direct capital) shall be considered as a financing source for each proposed capital improvement.

Capital Policy Four ensures that the CIP demonstrates the full cost (principal and interest) of approved projects that require the issuance of debt. This analysis will help policy makers make decisions based on the total impact of a project on our community and permit longer term planning as current decisions can be made based on their future implication on the City's debt service budget and overall capacity.

Capital Policy Five requires that all proposed capital investments include in their analysis not only capital costs but also the cost of additional personnel required as a result of the capital investment (new teachers required for a new school, for example) as well as increased operational costs. This will ensure that capital investments are made with full knowledge of the entire cost of the project.

Capital Policy Six requires the identification of a funding source for each proposed capital investment. This policy helps make each proposal more "real" by ensuring that funding is tied to each capital item. The CIP is intended to be both an identification of needs and a working document that results in the actual funding of capital. To do so requires that each capital item be proposed with funding sources attached so individual investments can be undertaken after they are reviewed and approved.

"Net operating revenues" are gross City revenue less: water and sewer operations, taxable debt exclusion funds, MSBA revenues, fund transfers, non-appropriated charges, special revenue, grants, and non-recurring revenues.

Financial Reserve Policies

- Reserve Policy 1: The City shall maintain a reserve fund balance of at least 15% of general fund expenditures.

For this policy, reserve funds are defined as unassigned and assigned fund balance as reflected annually in the GAAP financial statements. Standard and Poor Rating Service uses a metric that includes the sum of unassigned and assigned fund balance divided by total expenditures plus transfers out. In order to achieve the highest grade in this area a calculation of 15% or greater is required. The City shall maintain such a ratio at 15% or greater. For purposes of this policy, this will be called the reserve ratio.

Free cash is a community's unrestricted available funds that may be used as a funding source for appropriations. To appropriate free cash a positive balance must exist and free cash must be certified by the Department of Revenue.

Free cash is generated when operating results are favorable. Operating results compare actual revenue collections to actual expenditures for the past fiscal year. In addition the figure includes the cumulative effect of the prior year's free cash amount net of any transfers.

Free Cash and stabilization are significant components of the reserve funds described above. Accordingly, the City will manage Free Cash and Stabilization funds annually to assure that any reductions in these areas will not cause the City's overall reserve ratio to drop below 15%.

The City will maintain a level of reserves that protects the City from emergency conditions that maintains financial flexibility and contributes to sufficient liquidity to fund all City expenses without short term borrowing and to contribute to maintaining a high credit ratings. To provide for adequate levels of reserves to protect the City of Wilmington's financial condition over the long-term, the City has adopted the following financial reserve policies.

The City will appropriate 10% of Free Cash annually to the City's stabilization account in order to assist in maintaining the reserve fund balance. If the total balance of the stabilization reserve fund amount would be greater than 10% of the City's budget then this allocation will be limited to maintain that percentage.

The City will appropriate 10% of Free Cash annually to the City's OPEB Trust Fund in order to assist in funding the trust for this future liability. This allocation will continue until the fund is fully funded.

The City will only recommend appropriating funds from free cash for the following:

- Emergency, urgent or unforeseen expenses for which there are no immediate funding sources. (i.e. damage to roadways or Water/Sewer infrastructure)
- To stabilize the budget when variances are due to unexpected adverse economic conditions that are expected to be of a duration of one year or less.
- To enhance reserves, such as, but not limited to special purpose stabilization funds, OPEB stabilization funds or trust funds, and retirement benefits funds.

- To fund capital projects including those included in the Capital Improvement plan, studies and the acquisition of property.
- To fund debt issued for capital projects or property acquisition.
- To fund unanticipated court decisions on legal settlements of a magnitude that exceed the Finance Committee reserve account or other available funds.

In the unexpected situation when the City's reserve ratio drops below 15%, the City will make best efforts to forecast revenues conservatively and implement expenditure restrictions to such a degree that the reserve ratio increases back above 15%.

This policy shall be reviewed annually; percentages, various account names and standards established by rating agencies will be evaluated.

Debt Policies

Debt policies are intended to sustain or enhance a government's financial stability, to evaluate a government's long-term capability to issue and repay debt, and to control debt issuances. Strong debt policies that are followed by a community also improve credit worthiness by establishing controls on the amount of debt that can be issued as well as its impact. Improved bond ratings result in lower interest rates that generate savings for taxpayers.

❖ Debt Policy 1: The City shall manage the issuance of debt in line with the following debt ratios:

- General Fund debt service as a percentage of net general fund expenditures (as defined in 'Capital Planning' section) – not to exceed 5%.
- Water and Sewer Fund debt service as a percentage of enterprise operating expenditures – not to exceed 25%.
- Percentage of Tax Supported Debt that will be retired at the end of ten years – 65% (minimum).

Debt Policy One provides standards for debt issuance and requires that outstanding debt conform to various ratios deemed appropriate for the City or for debt issuers in general. This provides a finer level of control than the overall debt ceiling authorized by Massachusetts General Law and ensures that our debt does not negatively impact our taxpayers even though its aggregate amount is in conformance with State Law.

❖ Debt Policy 2: Short-term debt, such as bond anticipation notes, tax anticipation notes, or grant anticipation notes, may be used when it provides immediate financing along with an interest rate advantage, or if there is an advantage to delaying long-term debt until market conditions are more favorable.

- Debt Policy 3: Short term debt will not be rolled over beyond two years Without a principal pay down or as prescribed by state law.

Debt Policy Two permits the City to issue short-term debt to meet immediate financing needs. The primary reason for issuing short-term debt is to provide "bridge financing" for capital projects. This financing is needed to actually conduct many bond-backed capital projects and allows the City to avoid the expense of the multiple bond issuances that would be required without short-term borrowing. This policy also permits borrowing in anticipation of the receipt of awarded grants, borrowing for cash flow purposes in anticipation of revenue and the temporary use of short-term debt when it is preferable to the issuance of long-term debt.

Debt Policy Three requires that principal pay down occur on short-term debt carried for more than two years. Short-term debt generally only places an interest cost on a community (that is, no principal pay down is required). This may provide an incentive to carry short-term debt for as long as possible, though the result is a debt balance that never gets smaller. This policy is consistent with Internal Revenue Service rules regarding short-term debt and will help the City reduce the long-term cost of the capital projects by paying down principal before long-term bonds are issued.

- Debt Policy 4: Revenue used to finance debt shall be projected in a conservative manner.

Debt Policy Four requires that revenue dedicated to debt payments be estimated in a conservative manner as is required for general City revenues in Revenue Policy One.

- Debt Policy 5: The term of debt issued to finance capital improvements or procurements may not exceed the useful life of the asset or improvement.

Debt Policy Five ensures that debt will not be outstanding beyond the useful life of the asset it purchased or improved. This is consistent with best practices in municipal finance and prevents future taxpayers from paying for capital investments from which they are not benefiting.

- Debt Policy 6: The City shall conduct debt financing on a competitive basis unless for reasons of market volatility, unusual financing structure or a complex security structure the City would be better served through a negotiated financing.

Debt Policy Six requires that the sale of City debt be conducted in a competitive manner (that is, sold on the open market) unless there is an advantage to negotiating the sale with large investors. This policy provides flexibility to conduct negotiated sales in instances when it is preferable to do so (in complicated bond issuances and when unique circumstances surround a community and its credit quality).

Future Financial Policies

These policies set forth an overall architecture for financial operations in the City of Marlborough. They are promulgated with the recommendation that the City working with the finance team with the City Council expand upon them. Many other policies can be developed and it is recommended that the City move forward in doing so. Developing additional policies can be of significant benefit to our government because they will codify the best practices under which we seek to operate and will be another opportunity for our residents to lend their expertise and interest to their government.

CITY OF MARLBOROUGH, MASSACHUSETTS

Policy Title: Investment of City Funds **Effective Date: FY18**

1. Introduction

This policy covers investments in the following fund categories: General Funds, Special Revenue Funds, Enterprise Funds, Agency Funds, Capital Project Funds and Trust Funds.

2. Authority

The Treasurer has the authority to invest the City's funds, subject to the statutes of the Commonwealth of Massachusetts, Chapter 44, § 55, 55a and 55b.

The Treasurer has the authority to invest the City's Trust Funds, subject to the statutes of the Commonwealth of Massachusetts, Chapter 44, § 54. All trust funds shall fall under the control of the Treasurer unless otherwise provided or directed by the donor.

Massachusetts General Laws, Chapter 44, § 55B and Chapter 740 of the Acts of 1985 requires the Treasurer to invest all public funds not designated for immediate distribution at the highest possible rate of interest reasonably available, taking into account safety, liquidity and yield.

3. Operational Considerations

The Treasurer shall negotiate for the highest rates possible, consistent with safety principles. Whenever necessary, the Treasurer will seek collateralization for all investments not covered by FDIC and/or DIF.

The Treasurer will utilize a bank rating service (Veribanc, etc.) to ensure dollars are invested with banking institutions of the highest quality.

The Treasurer shall require any brokerage houses, brokers and dealers wishing to do business with the City, to supply the following information:

a. Audited financial statements;
b. Proof of National Association of Security Dealers certification;
c. A statement of compliance with the City's investment policy;
d. Proof of creditworthiness (minimum of 5 years in operation and capital that exceeds $10 million).

4. Reporting Requirements

On a regular basis (quarterly, semi-annually, or annually), a report containing the following information will be prepared by the Treasurer

:

a. A listing of the individual accounts and individual securities held at the end of the reporting period;
b. A listing of the short-term investment portfolio by security type and maturity to ensure compliance with the diversification and maturity guidelines established within the framework of GASB 45;
c. A summary of the income earned on a monthly and year to date basis;
d. A brief statement of general market and economic conditions and other factors that may affect the City's cash position.

5. Restrictions

MGL Chapter 44, Section 55 sets forth the several restrictions of which the Treasurer must be aware when making investment selections.

a. A Treasurer shall not at any one time have on deposit in a bank or trust company an amount exceeding 60% of the capital and surplus of such bank or trust company, or banking company, unless satisfactory security is given to it by such bank or trust company, or banking company for such excess;
b. The Treasurer shall not make a deposit in any bank, trust company or banking company that he/she is associated as an officer or employee or has been the same for any time during the three years immediately preceding the date of any such deposit;
c. All securities shall have a maturity from date of purchase of one year or less.

Massachusetts General Laws Chapter 44, Section 54 states that money should be deposited into banking institutions and trust companies incorporated under the laws of the Commonwealth, which are members of the Federal Deposit Insurance Corporation.

The Treasurer may invest funds in securities, other than mortgage and collateral loans, which are legal for the investment of funds under the laws of the Commonwealth provided that not more that fifteen percent of any Trust Fund shall be invested in bank stocks and insurance company stock, nor shall more than one and one-half percent of such funds be invested in the stock of any one bank or insurance company.

Common and preferred stock as well as other investment vehicles listed on the Commonwealth of Massachusetts List of Legal Investments, are permissible investment vehicles. The List of Legal Investments is maintained by the Office of the Commissioner of Banks.

The Treasurer must apply the "prudent person" standard in the context of managing the overall portfolio. The Treasurer, acting in accordance with the Investment Policy and exercising due diligence, shall be relieved of personal responsibility for an individual security's credit risk or market price changes, provided the transactions are carried out in accordance with the terms of this policy.

Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs; not for speculation but for investment considering the probable safety of their capital, as well as the probable income to be derived.

The Treasurer shall refrain from any personal activity that may conflict with the proper execution of the investment program or which could impair or appear to impair the ability to make impartial investment decisions. The Treasurer must disclose any material financial interest in financial institutions that do business with the City.