

RESOLUTION NO. 1433

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF EDMONDS,
WASHINGTON, ADOPTING THE FUND BALANCE / RESERVE POLICY
AS ATTACHED HERTO.

WHEREAS, the City Council heard a detailed introduction to the City's Fund Balance / Reserve Policy at the May 7, 2019 council meeting; and

WHEREAS, the May 7, 2019 introduction focused on amending the Fund Balance / Reserve Policy to incorporate the Governmental Accounting Standards Board Pronouncement No. 54 *Fund Balance Reporting and Governmental Fund Type Definitions*, and

WHEREAS, the May 7, 2019 introduction focused on amending the Fund Balance / Reserve Policy for the City Contingency Reserve Fund to incorporate Washington State Revised Code of Washington Chapter 35A.33.145, setting statutory limitations at \$0.375 per \$1,000 of assessed property valuation; and

WHEREAS, the May 7, 2019 introduction focused on amending the Fund Balance / Reserve Policy target levels for the City; now therefore,

THE CITY COUNCIL OF THE CITY OF EDMONDS, WASHINGTON, HEREBY
RESOLVES AS FOLLOWS:

Section 1. ADOPT THE CITY OF EDMONDS FUND BALANCE / RESERVE POLICY. The city council hereby adopts the following attached document:

1. City of Edmonds Fund Balance / Reserve Policy to read as set forth in **Attachment A** hereto, which is attached hereto and incorporated herein by this reference as if set forth in full.

RESOLVED this 2nd day of July, 2019.

CITY OF EDMONDS


MAYOR, DAVE EARLING

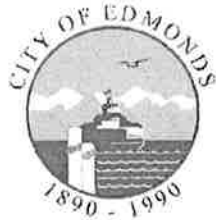
ATTEST:


CITY CLERK, SCOTT PASSEY

FILED WITH THE CITY CLERK:
PASSED BY THE CITY COUNCIL:
RESOLUTION NO.

June 28, 2019
July 2, 2019
1433

City of Edmonds



Fund Balance Reserve Policy

July 2019

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ARTICLE I INTRODUCTION

The overall objective of Fund Balance/Reserve Management Policy is to define that portion of fund balance that is unavailable to support the current budget. In many ways, fund balance represents working capital, which can either be used as a liquidity reserve or for spending in future years. A comprehensive fund balance/reserve management policy provides guidelines for the major funds of the City of Edmonds and provides a structured approach in setting reserve levels in specifically designated funds.

This Fund Balance/Reserve Management Policy is intended to guide prudent use of resources to provide for the much needed services to taxpayers and to maintain sound management policies. It is essential that governments maintain adequate levels of fund balance reserves to mitigate risks and provide a back-up for revenue shortfalls.

Policy

It is the policy of the City of Edmonds to provide for the continuity of City government by planning ahead for economic uncertainties and unforeseen or unplanned major expenditures. In order to achieve reserve goals the City must exercise prudent debt and liability management policies and follow sound fiscal management policies that prioritize the City's core services. This policy establishes reserve fund balance accounts that will provide funding for emergencies, economic uncertainties and for unanticipated operating expenses or revenue shortfalls. In addition, this policy incorporates provisions of Governmental Accounting Standards Board Statement (GASB) no. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*.

Objectives

The purpose of this Fund Balance/Reserve Management Policy is to assist the City in the pursuit of the following equally important objectives:

1. Build adequate reserves which will provide the City the resources necessary for financial stabilization, particularly during times of unforeseen emergencies and economic downturns;
2. Establish sound fiscal reserve policies that will serve as the foundation for ensuring that strong fiscal management policies guide future City decisions;
3. Provide prudent guidelines regarding the establishment, use and replenishment of City committed or assigned fund balances/reserves;
4. Establish a process for periodic reporting and review of the City's various fund balances (reserves); and
5. Enhance the City's credit ratings received from rating institutions through the establishment of clearly delineated Fund/Reserve policies that promote strong fiscal management;
6. Establish reserve policies that are in full compliance with GASB 54 financial reporting requirements.

ARTICLE II CRITERIA FOR ESTABLISHING APPROPRIATE FUND BALANCE RESERVE LEVELS

There are key elements that must be reviewed and analyzed to determine the appropriate size of a given fund balance reserve. Failure to follow the guidelines established in this policy can result in developing unattainable fund reserve goals or unsustainable fund balance reserve levels. The following criteria shall be used in determining the appropriate fund balance reserve levels:

Section 1. Volatility

The predictability and/or the volatility of its revenues or its expenditures (i.e., higher levels of fund balance reserves may be needed if significant revenue sources are subject to unpredictable fluctuations or if operating expenditures are highly volatile).

Section 2. Operating Fund Size

The overall size of the fund's budgetary events should be taken into consideration in setting the required fund balance reserve level and type for a particular fund.

Section 3. Purpose of Fund Balance Reserves

Another consideration for determining the size of each reserve will be the purpose of the reserve: Is there significant or perceived exposure to one-time outlays (e.g., disasters, immediate capital needs, state budget cuts, or are there potential drains upon fund resources from other funds, or conversely, are there potential reductions in funding transfers from other funds)?

Section 4. Bond Ratings

The potential impact on the entity's bond ratings and the corresponding increased cost of borrowed funds.

ARTICLE III COMMITTED GENERAL FUND BALANCE RESERVES POLICY

This Policy shall establish a committed fund balance reserve within the General Fund, define funding levels and call the reserve the ***General Fund Operating Reserve***. The purpose of the reserve is for meeting economic uncertainties, and unanticipated expenses or revenue shortfalls. This Policy requires the City to establish and maintain a General Fund Operating Reserve, within the General Fund, in an amount equal to or greater than 16% of the General Fund's Adopted Annual Operating Expenditure Budget. If it is determined that the reserve balances are not adequate, the Finance Director shall propose an amendment to these policies.

A detailed accounting of this reserve account will be maintained by the Finance Department to show deposits, withdrawals (when authorized pursuant to policies contained herein) and interest earned. All accounting for these accounts shall be recorded in the City's ERP system. A detailed report, prepared by the Finance Department, shall be presented annually to the Council.

Section 1. Establishment and Purpose of Operating General Fund Operating Reserve

A separate balance sheet account shall be setup by the Finance Director for the General Fund Operating Reserve, to be used in instances of fiscal emergencies that include: economic uncertainties, unforeseen emergencies and unanticipated operating expenses or revenue shortfalls.

The Mayor has the power to declare a fiscal emergency based upon one of the following:

- 1) A natural catastrophe;
- 2) An immediate threat to health and public safety; or
- 3) A significant decline in General Fund revenues.

The fiscal emergency declared by the Mayor must be approved by a simple majority of the City Council.

Limitations of Fund Use

Any use of the committed General Fund Operating Reserves shall be used only in cases of fiscal emergency and shall not be used to augment ongoing budgetary/operating spending increases. The committed General Fund Operating Reserve may also be used for one-time non-reoccurring expenditures and/or capital projects (operations and maintenance shall not be included), all as submitted by the Mayor and approved by the Council.

The amount of funds to be withdrawn from this committed fund balance reserve shall be determined by the Mayor. In his/her presentation to the Council, the Mayor or his/her designee shall include a detailed list of how the funds will be applied. A simple majority vote of the Council shall be required to approve the amount and use of funds.

Transition Policy

Council adoption of this policy will trigger moving an amount not less than 16% of the General Fund's unrestricted fund balance to the ***General Fund Operating Reserve***.

General Fund Operating Reserve Replenishment

If any use of the committed General Fund Operating Reserve has occurred, the Finance Director must present to Mayor and City Council an annual Replenishment Report during the month of November. The Replenishment Report must be presented each year, until the Reserves are fully replenished. The Replenishment Report must include the following information:

- 1) Amount of Reserves used
- 2) Whether it is anticipated additional Reserves will be needed in the following budget cycle, or
- 3) If no additional Reserves are needed, then the Replenishment Report must include a plan for replenishing the Reserve to policy mandated levels.

The committed General Fund Reserve shall be restored pursuant to the guidelines delineated below:

- 1) If a reserve is drawn down by 0-10% of reserve fund balance, then a solution to replenish to at least the minimum shall be structured over a 1 to 3 year period.
- 2) If a reserve is drawn down by 11-25% of reserve fund balance, then the budgetary plan to restore the reserve shall be structured over a 3 to 5 year period.
- 3) If the reserve is drawn down by 26-50% of reserve fund balance, then a budgetary plan shall be implemented to return the reserve level to between 75% and 100% of the minimum balance over a 5 to 7 year period.

ARTICLE IV CONTINGENT RESERVE FUND BALANCE POLICY

This Policy shall establish a fund and define funding levels for a committed Fund Balance Reserve to

be called the ***Contingent Reserve Fund***. The primary purpose of the reserve is for meeting emergencies of the City and, secondarily, if the ***General Fund Operating Reserve have been exhausted***, the ***Contingent Reserve Fund*** can be use in times of economic uncertainties, and for unanticipated expenses or revenue shortfalls. The target balance of the Reserve shall 1) not exceed the limitations set forth by RCW 35A.33.145, which sets the statutory maximum at \$0.375 per \$1,000 of assessed valuation and 2) when combined with the ***General Fund Operating Reserve***, the two fund balance reserves shall not exceed 20% of the General Fund's Adopted Annual Operating Expenditure Budget. In other words, if the ***General Fund Operating Reserve*** balance equals 16% of operating budget, then the ***Contingent Reserve Fund*** balance cannot exceed 4% of the operating budget. It further requires a simple majority vote of Council with a statement declaring the reason for their use.

A detailed accounting of the Fund shall be maintained by the Finance Department to show deposits, withdrawals (when authorized pursuant to policies contained herein) and be presented annually to the Council.

The Mayor has the power to declare a fiscal emergency based upon one of the following:

- 1) A natural catastrophe;
- 2) An immediate threat to health and public safety; or
- 3) A significant economic decline in General Fund revenues.

The fiscal emergency declared by the Mayor must be approved by a simple majority of the City Council.

Limitations of Fund Use

Any use of the committed Contingent Reserves shall be used in cases of fiscal emergency, shall not be used to augment ongoing budgetary/operating spending increases and should be used only after the ***General Fund Operating Reserves have been exhausted*** or when City Council approves specific used of the committed Contingent Reserve for one-time non-reoccurring expenditures and/or capital projects (operations and maintenance shall not be included).

The amount of funds to be withdrawn from this committed fund balance reserve shall be determined by the Mayor. In his/her presentation to the Council, the Mayor or his/her designee shall include a detailed list of how the funds will be applied. A simple majority vote of the Council shall be required to approve the amount and use of funds.

Contingent Reserve Replenishment

If any use of the committed Contingent Reserve has occurred, the Finance Director must present to Mayor and City Council an annual Replenishment Report during the month of November. The Replenishment Report must be presented each year, until the Reserves are fully replenished. The Replenishment Report must include the following information:

- 1) Amount of Reserves used
- 2) Whether it is anticipated additional Reserves will be needed in the following budget cycle, or
- 3) If no additional Reserves are needed, then the Replenishment Report must include a plan for replenishing the Reserve to policy mandated levels.

The committed Contingent Reserve shall be restored pursuant to the guidelines delineated below:

- 1) If a reserve is drawn down by 0-10% of reserve fund balance, then a solution to replenish to at least the minimum shall be structured over a 1 to 3 year period.

- 2) If a reserve is drawn down by 11-25% of reserve fund balance, then the budgetary plan to restore the reserve shall be structured over a 3 to 5 year period.
- 3) If the reserve is drawn down by 26-50% of reserve fund balance, then a budgetary plan shall be implemented to return the reserve level to between 75% and 100% of the minimum balance over a 5 to 7 year period.

ARTICLE V ANNUAL FUND BALANCE TYPES - STATUS REPORT

Once a year, in August, the City Finance Director shall present to the Council Finance Committee a comprehensive report on the City's fund balance reserve types as of June 30th. The report shall include an updated fund balance reserve level for each fund balance type. This report shall include the following funds:

1. General Fund Operating Reserve balance;
2. Contingency Reserve Fund balance.

ARTICLE VI FIVE-YEAR RESERVE RATE REVIEW

Every five years, during the annual budget hearings, the Mayor, based upon a comprehensive financial and economic review of all City fund balance types and in consultation with the City Finance Director, and Department Directors as necessary, shall make recommendations to the City Council for either maintaining existing fund balance reserve policies or revising fund balance reserve policies including percentage ranges established by category herein and replenishment requirements by categories established herein.

ARTICLE VII DEVIATIONS FROM POLICY

No deviations from the fund balance reserve policies set forth in this Policy will be allowed except as approved by a simple majority of vote by the Council. This includes any increase or decrease in the base fund balance reserve levels established by this policy and expenditures from fund balance reserve accounts for anything other than the intended budgeted use of said fund balance.

ARTICLE VIII DEFINITIONS

Budget - A plan of financial operation containing an estimate of proposed expenditures for a given period (usually a fiscal year) and a proposed forecast of revenues (receipts) to cover them. A budget is also a plan that outlines an organization's financial and operational goals and strategies in monetary terms.

Capital Expenditures are expenditures incurred when monies are spent either to buy fixed assets or to add to the value of an existing fixed asset with a useful life that extends beyond the fiscal year. In accounting, a capital expenditure is added to an asset account ("capitalized"), thus increasing the asset's basis (the cost or value of an asset). The general rule (even for municipalities) is that if the property acquired has a useful life longer than the fiscal year, the cost must be capitalized. The capital expenditure costs are then amortized or depreciated over the life of the asset in question.

Comprehensive Annual Financial Report (CAFR) - A CAFR is a set of financial statements for a state, municipality or other governmental entity that comply with the accounting requirements established by the Governmental Accounting Standards Board (GASB). It must be audited by an independent auditor using generally accepted government auditing standards.

The CAFR consists of three sections: Introductory, Financial and Statistical.

The Introductory section orients and guides the reader through the report. The Financial section presents the entity's basic financial statements as well as notes to the statements and the independent auditors' report. The Statistical section provides additional financial and statistical data, including data about financial trends that may better inform the reader about the government's activities.

Council - Means the legislative body (the city council) that governs the City of Edmonds.

Expenditure - The actual payment of cash or cash equivalent for goods delivered or services rendered, or a charge against available funds in settlement of an obligation as evidenced by an invoice, voucher or other such document during the fiscal year. For governmental reporting purposes, expenditures include expenses or a provision for debt retirement not reported as a liability of the fund from which retired.

Fiscal Year - A 12 month period to which the annual operating budget applies and the end of which a governmental unit determines its financial position and the results of its operations. The City has specified January 1 through December 31 as its fiscal year.

Fund - A fund is a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and "residual" equity or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain planned objectives in accordance with special regulations, restrictions or limitations.

Fund Balances - The overall objective of fund balance reporting is to isolate that portion of a fund balance that is unavailable to support the following period's budget (see GASB 54 definition below). In general, an unassigned fund balance shall be defined as those amounts that are not restricted, committed, or assigned, of a particular fund at the end of the fiscal year.

GASB 54 - Fund Balance Reporting and Governmental Fund Type Definitions - The City of Edmonds's CAFR Financial Statements are required to comply with GASB 54 beginning with its Fiscal Year End 2011 CAFR going forward. GASB 54 changes and identifies fund balance classifications that can be more consistently applied by clarifying existing governmental fund type definitions.

- Fund balance is basically the difference between the assets and liabilities reported in a fund. GASB statement No. 54 provides the following five categories for classifying fund balance and related definitions to be used for describing the components of fund balance:
 1. **Nonspendable Fund Balance** Amounts that are not in a spendable form or are required to be maintained intact. Due to the nature or form of the resources, they generally cannot be expected to be converted into cash or a spendable form (e.g. Inventories and prepaid amounts). This also

includes long-term loan and notes receivable and property held for resale. Applies as well to amounts that must be retained intact legally or contractually.

2. **Restricted Fund Balance** – Amounts that can be spent only for the specific purposes stipulated. Constraints are placed on the use of resources by external parties (e.g. by creditors, grant providers, contributors) or by laws or regulations (e.g. constitution or legally enforceable language). Restrictions may be changed or lifted only with the consent of the resource provider.
3. **Committed Fund Balance** – Amounts can only be used for the specific purposes determined by a formal action of City Council. Constraints on fund balance use are imposed by internal formal action of the government's highest level of decision-making authority (e.g. City Council) and can only be removed or changed by taking the same type of action it employed to commit those amounts through legislation, resolution, or ordinance (e.g. funds committed to satisfy contractual obligations). Action to constrain resources must occur prior to year-end; however the amount can be determined in the subsequent period.
4. **Assigned Fund Balance** – Assigned fund balances include amounts that are limited by the Council, Mayor, or his/her designee, for its intended use, but little or no formal action is required to modify or eliminate those limitations. Assigned fund balances comprises amounts intended to be used for a specific purpose. Amounts reported as assigned should not result in a deficit in unassigned fund balance. Also relates to all governmental funds other than the General Fund, with any remaining positive amounts not classified as nonspendable, restricted or committed.
5. **Unassigned Fund Balance** – Comprises the residual classification for the General Fund and includes all amounts not contained in the other classifications. Unassigned amounts are available for any purpose. This represents the residual amount of the fund balance that has not been restricted, committed, or assigned.

General Fund - In public sector accounting, the General Fund is the primary operating fund for all revenues of the City that are not otherwise restricted as to their use, including monies from local property and sales tax, and other revenue sources that are not assigned for a specific purpose. The General Fund provides the resources necessary to pay/sustain the day-to-day activities for City services such as administration, community services, parks and recreation, police, fire, public works, elected officials, Mayor, and City Council. When governments or administrators talk about “balancing the budget” they typically mean balancing the budget for their general fund.

Government Accounting Standards Board (GASB) - GASB is the private, nonpartisan, nonprofit organization that works to create and improve the rules U.S. state and local governments follow when accounting for their finances and reporting them to the public. While the GASB does not have the power to enforce compliance with the standards it promulgates, the authority for its standards is recognized under the Rules of Conduct of the AICPA. Also, legislation in many states requires compliance with GASB standards, and governments usually are expected to prepare financial statements in accordance with those standards when they issue bonds or notes or otherwise borrow from public credit markets. The GASB was established in 1984 and is funded by publication sales, contributions from state and local governments, and voluntary assessment fees from municipal bond issues.

Operating Budget – A detailed projection of all estimated income and expenses based on forecasted revenue during a given period (usually one year). Since an operating budget is a short-term budget, capital outlays are excluded because they are long-term costs. One-time revenues, such as grants, settlements,

sales of assets and transfers are excluded because often they are non-recurring sources of revenues and cannot be counted on coming in from one budget cycle to the next.

Revenue - The income of a government from all sources appropriated for the payment of the public expenses. It includes such items as tax payments, fees from specific services, receipts from other governments, fines, forfeitures, grants, shared revenues and interest income.

Structural Budget Deficit or “Gap” - A budget deficit (Gap) that results from a fundamental imbalance whereby current year governmental expenditures exceed current year revenues without any consideration of carryover or prior year unspent revenue balances if they exist. A structural deficit remains across the operating fiscal cycle because the general level of government spending is too high for the prevailing revenue structure (e.g., taxes, fees and other sources). A fiscal Gap, is a structural budget deficit over an extended period of time and not only includes the structural deficit at a given point in time but also the difference between promised future government commitments, such as health and retirement spending, and future planned or anticipated tax and other revenues. Another description is that the current revenue structure is insufficient to maintain services at the current level.

ARTICLE IX EFFECTIVE DATE

This policy shall take effect upon its final adoption by the City Council.