

**MEETING DATE:** 8/2/2022

**DEPARTMENT:** Finance

**AGENDA ITEM:** Bill No. 2950-22, Amending the General Fund Reserve Policy – 2nd Reading

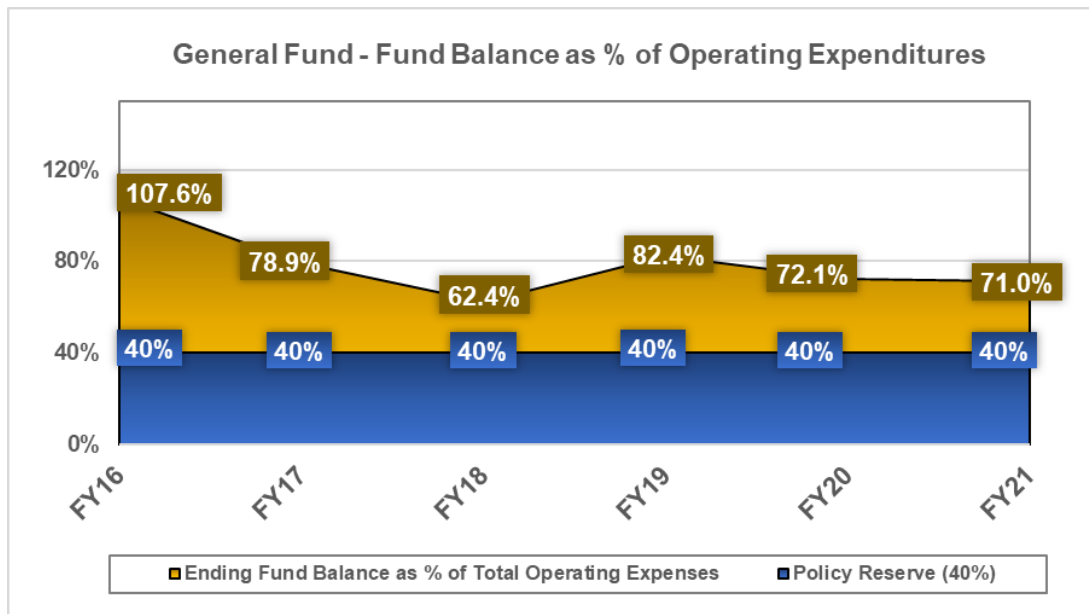
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**REQUESTED BOARD ACTION:**

A motion to approve Bill No. 2950-22, Amending the General Fund Reserve Policy – 2<sup>nd</sup> reading by title only.

**SUMMARY:**

The City's current General Fund reserve policy requiring a cash balance of 40% of operating expenditures was adopted on December 1, 2015 (Bill No. 2734-15). This cash balance was chosen specifically after consultation with the City's financial advisor and GFOA (Government Finance Officer's Association) as an appropriate policy to provide resources in the case of unanticipated events which could adversely affect the City's financial condition. As seen in the chart below, for 6 years, the City has maintained a cash balance reserve level well above the 40% requirement (the lowest level being 62% of operating expenditures held in reserves at the conclusion of FY2018).



Prior to the financial summit, staff researched the General Fund reserve policies in place for surrounding/comparable. In this research, staff found that Parkville, MO also had a 25% of budgeted operating expenditures policy and a similar sized General Fund budget (approximately \$5.9 million budget).

Finance staff have provided a redlined version of the City's reserve policy. As stated above, current policy requires a cash/fund balance of 40% of General Fund operating

expenditures. Staff also believe holding 25% in reserves will provide a practical/pragmatic level of available funds in the case of unanticipated events (for example, in the case of a 25% cash balance policy, \$6 million in expenditures would require holding a cash balance of \$1.5 million).

Finance staff consulted with Piper Sandler, the City's financial advisor, regarding any potentially negative consequences of changing the fund balance policy. Piper Sandler stated that a simple change from a 40% reserve policy to a lesser number (such as 25%) is not likely to immediately result in a rating downgrade. Rather, concerns will come into play if the City continues to run an annual deficit which results in a projection of a declining fund balance falling below the policy requirement. One-time expenses also play a role as these count as discretionary spending which the City can control (CIP projects or one-time capital acquisitions). If the City plans to spend down fund balance, ensuring a financial plan/budget is created over the next 3 to 5 years indicating to what levels fund balance is expected to drop is important in continuing to maintain a strong financial rating and position.

Following discussion at the financial summit, the Board directed an alteration to the policy by requiring only 25% of General Fund operating expenditures to be held in fund balance.

**PREVIOUS ACTION:**

During the Board of Aldermen financial summit on May 25, the Board expressed interest in changing the City's General Fund reserve policy.

**POLICY OBJECTIVE:**

The intention in changing the policy was to maximize the City's existing cash-on-hand to better provide for public amenities and service delivery.

**FINANCIAL CONSIDERATIONS:**

Lowering the general fund reserve from 40% to 25%.

**ATTACHMENTS:**

- |   |                                   |
|---|-----------------------------------|
| <input checked="" type="checkbox"/> Ordinance | <input type="checkbox"/> Contract |
| <input type="checkbox"/> Resolution           | <input type="checkbox"/> Plans    |
| <input type="checkbox"/> Staff Report         | <input type="checkbox"/> Minutes  |
| <input type="checkbox"/> Other:               |                                   |

**AN ORDINANCE AMENDING THE RESERVE POLICY OF THE CITY OF SMITHVILLE**

**WHEREAS**, the City of Smithville, Missouri endorses sound financial policies and practices; and

**WHEREAS**, in September 2018, the Board of Aldermen revised the General Fund Reserve Policy as part of the Policy Manual; and

**WHEREAS**, it is essential that the City maintain adequate reserve in its major funds to continue to maintain the capacity to: (1) provide sufficient cash flow for daily financial needs, (2) secure and maintain investment grade bond ratings, (3) offset against significant economic downturns or revenue shortfalls, and (4) provide funds for unforeseen expenditures related to emergencies; and

**WHEREAS**, following review by staff, consultation with the City's financial advisor, and recommended action from the Board of Aldermen, it has been determined that adjusting the General Fund Reserve Policy from 40% of budgeted operating expenditures to 25% of budgeted operating expenditures is beneficial to the City's overall goals and strategy; and

**NOW THEREFORE BE IT ORDAINED BY THE BOARD OF ALDERMEN OF THE CITY OF SMITHVILLE, MISSOURI AS FOLLOWS:**

The General Fund reserve policy (attached hereto) is hereby amended to be the Fund Reserve Policy and shall include guidelines for General Fund balance reserves and is in full force from and after its passage according to law.

PASSED THIS 2<sup>nd</sup> Day of August 2022

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Damien Boley, Mayor

ATTEST:

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Linda Drummond, City Clerk

First Reading: 07/19/2022

Second Reading: 08/02/2022

## **Title: Fund Balance Reserve Policy**

**Adopted: ~~September 18, 2018~~ July 19, 2022**

### PURPOSE:

The purpose of the Fund Reserve Policy is to provide guidelines to the Board of Aldermen and staff for establishing, maintaining and performing an annual review of the minimum and appropriate level for General Fund and Combined Water and Wastewater Systems Fund balance.

### BACKGROUND:

The Government Finance Officers Association (GFOA) recommends that governments establish a formal policy regarding the level of fund reserves that should be maintained to mitigate current and future risks such as revenue shortfalls, unanticipated expenditures, natural disasters and to ensure the ability for stable and acceptable rate changes.

A minimum unassigned fund reserve is generally considered a prudent and fiscally responsible policy to deal with unforeseen situation including but not limited to:

- Unfunded Federal, State or Other Mandates
- Revenue Shortfalls due to Economic Downturns or other unexpected conditions
- Expenses Incurred for Restoration of Service due to Weather Events or other Natural Disasters
- Credit rating agencies continually monitor the levels of unassigned fund balance when evaluating the creditworthiness and assigned a credit rating for debt issuance.

The City has established and approved a Fund Balance Reserve Policy where the City shall maintain a minimum unassigned fund balance equal to ~~forty~~ twenty-five percent (~~40%~~ 25%) of the General Fund budgeted expenditures for any given year.

The City has established and approved a Fund Balance Reserve Policy where the City shall maintain a minimum unassigned fund balance equal to twenty percent (20%) of the Combined Water and Wastewater Systems Fund budgeted expenditures for any given year.

Designation of an appropriate level for fund reserve is recommended for use as a financial planning tool in the budget process and with bond rating agencies.

### POLICY:

The City shall maintain a minimum General Fund reserves equal to ~~forty~~ twenty-five percent (~~40%~~ 25%) of the approved operating annual expense budget for

the fund for any given year. The City Shall maintain a minimum Combined Water and Wastewater Systems Fund reserve equal to twenty percent (20%) of the total approved operating and annual expense budget for the fund for any given year. The reserves shall be used when approved by formal Board of Aldermen action or under the following circumstances:

- Large one-time cost where use of reserves would provide long-term cost savings.
- To mitigate service impacts from significant revenue shortfall due to economic downturn or other unexpected loss of revenue.
- Restoration due to weather events or other natural disasters.
- Unexpected liabilities created by Federal, State or other mandates out of its control.

If in any fiscal year the Reserve Balance in either fund is required to be used or is not achieved, the City Administrator shall present to the Board of Aldermen a strategy to meet the Fund Reserve minimum reserve level within two (2) fiscal years.

Staff shall ensure that the provisions of this policy are effectively implemented. If it is determined that there is a conflict between this policy and other more specific governing policies involving the operating or capital improvement budgets, this shall be brought to the attention of the City Administrator who will determine the appropriate course of action.