

# Financial Policies, Guidelines and Practices

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The City of Topeka relies on formal policies, state law and established financial principles to guide its budgeting and financial practices. It also has policies established in accordance with GAAP and other best practices. These policies set forth the basic framework for the overall fiscal management of the City. The financial policies provide guidelines for evaluating both current activities and proposals for future programs. Most policies and procedures represent long-standing principles, traditions, and practices that guide the City and help to maintain its financial stability. The City is in the process of reviewing and establishing financial policies. The City Council adopted policies for capital improvements and debt management in 2004. It also adopted a resolution requiring a structurally balanced General Fund budget beginning in 2006. These and other financial policies are to be reviewed annually.

**Budgeting, Accounting and Audit Practices.** Kansas law prescribes the policies and procedures by which the cities prepare annual budgets. By August 25<sup>th</sup> of each year, prior to commencement of the new fiscal year on the following January 1<sup>st</sup>, the governing body of the City must adopt a budget, which is filed with the City Clerk and the State Director of Accounts and Reports. The budget itemizes anticipated revenues and proposed expenditures, detailed by program and object of expenditures, for the next fiscal year. Funds must be balanced so that total resources equal obligations in accordance with Kansas law (K.S.A. 79-2927), which requires that, “The budget of expenditures for each fund shall balance with the budget of revenues for such fund....”. The level of budgetary control or expenditure limit is at the fund level, except for the General Fund which also has established expenditure limits for each Department financed. However, statutes allow for the transfer of budgeted amounts between line items within a fund. Departments are responsible for managing their budgets to the fund or department total level. Changes from expenditure category to expenditure category may be made administratively. Transfers of \$15,000 or more from department to department within the General Fund may only be made with the approval of the City Council. The City maintains a financial and budgetary control system. Expenditures and revenues are tracked to ensure adherence to the budget and awareness of the financial environment. Monthly reports are prepared that compare actual revenues and expenditures to budgeted amounts and provide a picture of the City’s cash position.

Kansas statutes require that the budget be prepared for the next fiscal year by August 1<sup>st</sup> of each year. The proposed budget must then be published along with a notice of public hearing on or before August 5<sup>th</sup>. The public hearing is held by August 15<sup>th</sup>, but at least ten days after publication. The budget is to be adopted on or before August 25<sup>th</sup>. The statutes allow for the governing body to increase the originally adopted budget if that increase is financed with previously unbudgeted revenue other than ad valorem property taxes. A notice of public hearing to amend the budget must be published in the local newspaper. At least ten days after publication, the hearing may be held and the City Council may amend the budget.

In order to ensure that Kansas municipalities conduct their affairs in a fiscally responsible manner, the State Legislature enacted a cash basis law in 1933 (K.S.A. 10-1101 et seq.) which states in part that it is unlawful, except where bonds, temporary notes, or no-fund warrants are authorized, “for the governing body of any municipality to create any indebtedness in excess of the amount of funds actually on hand in the treasury of such municipality, or to authorize the issuance of any order, warrant or check, or other evidence of such indebtedness of such municipality in excess of the amount of funds actually on hand in the treasury of such municipality at the time for such purpose.” The purpose of the cash basis law is to prevent municipalities from spending more than they receive annually in operating revenues, and to prevent the issuance of short-term debt to cover operating expenditures.

Kansas statutes and regulations of the Kansas Board of Accountancy provide for municipal accounting in conformance with generally accepted accounting principles (GAAP). Separate funds are maintained by the City for specific purposes and projects, in compliance with GAAP, State laws and regulations, bond covenants, tax levies, grant agreements, and City ordinances and resolutions. The City prepares a Comprehensive Annual Financial Report (CAFR), disclosing the financial position, results of operations, and changes in fund equities or retained earnings for all funds and account groups in accordance with GAAP. An independent firm of certified public accountants performs annual audits of this information. The audited CAFR is filed in the Office of the City Clerk and with the Nationally Recognized Municipal Securities Information Repositories (NRMSIRs), among other agencies.

**Investment Policy.** The City of Topeka recognizes that effective cash management is an integral component of good financial management. It shall be the policy of the City that funds deemed idle, based on projected cash flow, be invested in a manner that seeks to maximize their productivity until such time as they are needed for the operations of the City. The City’s investment portfolio shall be designed and managed in accordance with this policy to ensure public trust and be consistent with state and local laws. Investments shall be at the highest rates obtainable at the time of the investment, within the limitations of the law and the city’s prudent investment policy in accordance with the following criteria.

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**Safety:** Safety of principal will be the foremost objective of the investment program for the City of Topeka. Each investment will be made in a manner, which ensures the preservation of capital in the portfolio.

**Liquidity:** The City of Topeka shall remain sufficiently liquid so as to meet all operating needs and expenses. The City will consider liquidity as a priority, while still recognizing the need to maximize yield.

**Return on Investment:** The investment portfolio shall be designed to attain a market-average rate of return throughout budgetary and economic cycles, taking into account the City's investment risk constraints, state statutes, cash flow needs of the City. Investments shall be made at the highest rates obtainable at the time of investment, within the limitation of the law and the City's prudent investment policy.

**Diversification:** Market risk shall be minimized by diversification of investment types. The City shall diversify (where prudent judgment dictates) its investments so that reliance on any one issuer (financial institution) or investment type will not place an undue burden on the City.

The investment policy also outlines safeguards, investment procedures, legal authority and other procedures related to the prudent investment of funds.

**Capital Improvement Policy and Procedure.** The Capital Improvement Policy provides a guideline and methodology for the development of the City's five-year capital improvement plan. The first two years of the Capital Improvement Plan (CIP) will consist of projects adopted as part of the Capital Improvement Budget (CIB). The first year of the CIB contains projects that will be initiated and completed during the proposed operating budget year. The second year projects are those for which plans are prepared for implementation. The projects in the following three years are those planned for implementation as they move towards the CIB. Thoughtful planning is essential for all departments submitting CIP requests. The Capital Improvement Policy includes definitions of a capital improvement project and other terms. It provides the following review principles to be followed in the adoption of the CIP.

1. The property tax levy for capital improvements should be maintained at a relatively consistent level from year to year. If movement either upward or downward becomes necessary, it should be done gradually.
2. When considering a consistent capital improvement property tax levy, the City should include the property tax requirements for debt service as well as for projects financed by direct appropriation or other means.
3. The City should maximize utilization of all Federal and State revenue sources for capital improvements.
4. The CIP is viewed as a long-term program that will continually address capital requirements far into the future. The use of long-term debt should be minimized, allowing the City to put money into actual projects that benefit Topeka residents and businesses rather than into interest payments to financial institutions and bond holders. The City should issue debt only for major capital projects and not try to finance the entire capital program with debt.
  - Bonds should not be used to fund operating projects or costs.
  - Bonds should not be used to fund any project whose expected life does not exceed the maturity on the bonds.
  - To the extent practicable, bonded indebtedness should be considered only for major capital projects where the City share is a minimum of \$100,000.
5. Approved capital improvement projects should have a funding plan for maintenance and operating costs identified in the project description and project budget. When feasible, priority should be given to those that will result in a reduction in operating costs.
6. The City should not acquire and hold land that is not needed for existing or near future City purposes. Land for projects that are not part of the approved five-year Capital Improvement Plan should not be acquired, except as part of a long-range annexation plan or other adopted plan.
7. Unless otherwise mandated by City ordinances, revenues derived from the sale and lease of surplus City real properties should be dedicated to the Capital Improvement Program and programmed after receipt by the City.
8. Enterprise funds should generate sufficient revenue to finance operations and related capital projects including debt service.
9. The City should fully investigate alternative financing sources for its capital projects, but should use such sources only if it can be clearly shown that they are in the best interests of the City.
10. The City should maximize utilization of current facilities and should give higher priority to maintaining present facilities and infrastructure over new construction where feasible.
11. In order to increase the long-term use of a City facility, as much flexibility as is consistent with operating efficiency should be built into all new or renovated facilities projects that the City undertakes.

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12. Inflation factors for all projects in the capital improvement program should be considered each year and appropriate adjustments made to all project estimates.
13. All projects should be reviewed by the CIP Review Committee for a recommendation to the Mayor and City Council.

In accordance with the definition of a capital improvement, City Departments submit capital improvement requests for each five year period of the Capital Improvement Budget and Plan. Projects are to be submitted by priority and year. The CIP Review Team, which is a cross-departmental group, will then review all projects and rank them based on established Capital Project Criteria (listed below). These rankings will be provided to the Mayor for use in determining the Mayor's recommended CIP. The Public Works City Engineer and the Budget Director will prepare a status report of prior approved projects. This status review allows the Mayor and City Council the opportunity to stay informed of these projects. Individual requests and a compilation are forwarded to the City Planning Commission for their review and input to the Mayor and City Council. The Mayor reviews the capital improvement project requests, considers the recommendations of the Planning Commission, if available, and develops the Mayor's Proposed CIP. The Proposed CIP is presented to the City Council, which reviews the document and makes changes as it deems necessary. The City Council has the final responsibility to adopt the CIB and CIP.

The following criteria will be used by the CIP Review Team to evaluate capital projects. Each project is measured accordingly and a score assigned.

**Community Goals** Capital projects should be consistent with or directly promote the Goals supporting the City Mission and Vision as stated in the annual City of Topeka Budget. As such, they should also support the objectives listed in Departmental budgets.

**Legal** State or Federal mandate may require that a particular project be implemented. Court orders and judgments concerning annexation, property owners' rights, environmental protection, etc. are also legal requirements that may affect how projects are prioritized.

**Safety** The benefit to the environment, safety or public health of the community should be evaluated. For example, all street projects concern public safety, but streets for which documented evidence of safety hazards exist should be given higher priority treatment.

**Funding** The proposed methods of funding should be evaluated. State and federal grants and other outside funding should be pursued and used to the extent possible.

**Preserve Existing Infrastructure** Reflects policy to ensure adequate resources are provided to preserve existing infrastructure before targeting resources toward building new facilities that also have maintenance obligations.

**Comprehensive Plan** Consistency with the City's Comprehensive Plan is important. Capital projects may directly or indirectly implement the comprehensive plan. Projects should not be inconsistent with the comprehensive plan.

**Quality of Life** The degree to which the project impacts the quality of life of the City's citizens and visitors should be given consideration. Does the project add to the quality of life through cultural, educational and artistic experiences, exposure to different cultures, or environmental enhancements?

**Cost to Operate** The annual and long range commitment associated with the project must be evaluated. What costs are associated with the project for maintenance, staffing pattern, energy utilization, and accessibility?

**Citizen Support** Projects are generally more easily implemented if there is public demand and support for them. Such public support should be gauged in terms of its strength and the depth of understanding in represents.

**Service Delivery** The degree to which projects improve service delivery should be identified using this category. Projects which substantially improve the quality of service are desirable. Immediate needs will be given more weight than future.

**Area Served** The scope of the project in terms of area and population served is measured by this criteria. Spreading capital improvement dollars to serve the greatest area and population is desirable.

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**Debt Management Policy.** The purpose of the debt management policy is to establish debt issuance and management guidelines. The policy is applicable to all debt financing for the City of Topeka. The City of Topeka projects debt requirements on a five-year basis to facilitate better short-term decisions in light of other priorities that may arise and to examine the long-range implications and effects of existing and contemplated debt. The City does not fund current operations or routine maintenance costs from the proceeds of long-term debt. The City confines long-term borrowing and capital leases to capital acquisitions, improvements, projects, or equipment that cannot be financed from current financial resources, under the following circumstances:

- The project is included in the City's Capital Improvement Budget;
- The project is the result of growth-related activities within the community that require unanticipated and unplanned infrastructure or capital improvements by the City;
- The project's useful life, or the projected service life of the equipment, will be equal to or exceed the term of the financing;
- There are revenues sufficient to service the debt, whether from future property taxes, user fees, or other specified and reserved resources, and debt supported by user fees, special assessments or special charges shall be preferred over that supported from taxes;
- The debt shall be primarily used to finance capital projects with a relatively long life, typically ten years or longer;
- Any equipment to be financed is an item that is purchased infrequently, has an expected useful life of at least five years, and costs \$100,000 or more.

In an effort to conserve statutorily limited debt capacity, the City borrows only when necessary and uses "pay-as-you-go" financing to the extent possible. The City intends to maintain its overall debt burden within the following generally accepted benchmarks as established for municipalities by municipal debt rating agencies:

- Net debt *per capita* should remain under nine hundred fifty dollars (\$950).
- Net debt as a percentage of estimated assessed value of taxable property within the City's corporate limits should not exceed thirteen percent (13%). The ratio of debt service expenditures as a percent of governmental fund expenditures should not exceed fourteen percent (14%).
- The debt *per capita* as a percentage of personal income *per capita* should not exceed five percent (5%).
- The City strives to achieve, and maintain a General Fund "Fund Balance" equal to no less than ten percent (10%) of General Fund "Revenue" for the next year.

The City strives to achieve, maintain, and, whenever possible, improve its bond credit ratings (currently assigned by Moody's Investors Services), to at least the following standards: General Obligation Bonds rated "Aa3"; Revenue Bonds rated "A2"; and General Obligation Temporary Notes rated "MIG -1". The City understands that such ratings will facilitate the achievement of favorable interest rates in, and the preservation of its access to, the credit markets.

In general, the City adheres to the following debt guidelines:

- When measuring its commitment to its infrastructure and related service delivery potential, the City addresses both its capital needs and its operating and maintenance requirements.
- In the case of capital needs, when measuring inter-period equity, the City considers the allocation of any debt burden among generations that will benefit from the financed capital assets, as well as the need to distribute the financing burden over appropriate fiscal periods.
- The City uses a "level debt service" strategy as a means to equalize the burden of its debt service assessment over time. This approach provides a slightly declining percentage of budget over time, presuming a gradually increasing budget.
- The City maintains a minimum ratio of Combined Utility Fund revenues to annual total revenue bond debt service requirements of 125%.
- The City strives to keep the average maturity of its general obligation bonds at or below fifteen (15) years.
- When the City finances capital projects by issuing bonds, it will amortize the debt over a term not to exceed the average useful life of the projects being financed.

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- The City reviews its outstanding debt at least annually for the purpose of determining if the financial marketplace will afford the City an opportunity to refinance long-term debt and so reduce its debt service costs. In order to consider the possible current refunding of an issue, a net present value (NPV) savings of at least three percent (3%) of outstanding principal of the refunded debt shall be the threshold expected to be achieved before proceeding with such refunding, unless the refinancing is expected to relieve the City of other onerous obligations or significantly reduce the remaining term of the financing. The City considers advance refunding when a five percent (5%) NPV threshold is met and synthetic refunding when a seven percent (7%) NPV threshold is met.
- Capital acquisitions, improvements, equipment, and projects are categorized into "pay-as-you-go" or "debt financing" classifications. Pay as you go capital items are those with a cost of less than \$100,000, those with short asset lives of five or fewer years, and those that extend the useful life of an existing capital asset for five or fewer years. Debt financing capital items is limited to those major, non-recurring capital expenditures for assets or asset improvements costing more than \$100,000 and having a useful life of more than five years. However, the City will use current operating funds for capital items categorized as "debt financing" as well, whenever it is cost feasible to do so.
- The City confines long-term debt financing to capital items with useful lives of ten or more years, which cannot be financed from current revenues or fund equity. When appropriate, the City uses special assessment taxes or other user-based revenue sources to pay the costs of related debt financing, so that those benefiting from the improvements will absorb all or most of the cost of the capital item being financed.
- The City uses State Revolving Fund (SRF) Loan programs in lieu of revenue bond financing for utility projects whenever such funds are available at more favorable rates. The City continues to monitor bond rating agency concerns with overall utility debt levels when participating in the SRF program.
- The City will continue to comply with SEC Rules by disclosing and updating its financial information to nationally recognized municipal securities information repositories, bondholders, and appropriate municipal debt rating agencies. The City will continue to follow a policy of full disclosure in its Comprehensive Annual Financial Report (CAFR) and in its bond offering documents.

The Debt Management Policy also lays out guidelines for debt administration and financing procedures and methods. This includes investment and arbitrage, use of an independent financial advisor, temporary note financing, conduit financings, and communication with credit rating agencies.