



# **DRAFT FINANCIAL POLICY GUIDELINES**

**Presented by:**

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# RECOMMENDATION

That the Council receive and provide feedback on the following draft financial policy statements:

- Debt Policy
- Fund Balance Reserve Policy
- Cash Management and Investment Policy
- Other Post-Employment Benefit (OPEB) Pre-Funding Policy

# RECOMMENDATION

Specifically asking for Council feedback on the following draft financial policy strategies and measures:

- I. Net Debt to Assessed Valuation
- II. Debt Service to Expenditure Ratio
- III. 10-Year Payout
- IV. General Fund Unassigned Fund Balance %
- V. Liquidity
- VI. Maturity
- VII. Diversification
- VIII. Pre-Funding Contributions

# WHY HAVE POLICIES?

- Financial policies are central to a strategic, long-term approach to financial management
- Formalizes the Town's financial management practices
- Recommended by the Government Finance Officers Association (GFOA)
- Encouraged by the bond rating agencies
- Solidifies Town's good financial standing

# BACKGROUND

- Council Retreat (01/25/19) Davenport & Company presented:
  - Town's Credit Rating
  - Current & Future Debt Portfolio
  - Financial Policies
- Budget Work Session (03/04/19) Town Manager & Business Management Director presented draft Financial Policy Guidelines
- April 24<sup>th</sup> returning for Council review and discussion
- Goal of returning to Council in June for policy adoption



# ABOUT THE POLICIES

- Draft Policies:
  - Developed in collaboration with Davenport & Company
  - Designed using quantitative scoring ranges from bond rating agencies
  - Measures aligned with other North Carolina AAA peer comparative agency ratings

# BENEFITS

- Institutionalizes good financial management by promoting stability and continuity
- Clarifies how Town will develop its financial practices and manage its resources
- Supports Town's excellent bond credit rating
- Promotes long-term strategic thinking
- Complies with established public management best practices

# DEBT POLICY

Debt policy assists in decision making process and supports Town's approach to project finance and debt management.

Sets proper balance between limits on use of debt financing and providing flexibility to respond to unforeseen circumstances and opportunities.

Recommended Measures:

- I. Net Debt to Assessed Valuation measure
- II. Debt Service Expenditure Ratio
- III. 10-Year Payout



# I. NET DEBT TO ASSESSED VALUATION

- Measures Town's net debt (tax supported debt) compared to the value of real property purchased as assessed (assessed valuation)
- Lower number represents less risk of government being unable to repay its debt
- Current = 0.79%
- Strong bond rating criteria range = 0.75% - 1.75%
- NC AAA average = 0.9%

## Recommendation

- **Net debt to assessed valuation should not to exceed 1.5%**

## II. DEBT SERVICE EXPENDITURE RATIO

- Measures amount committed to annual debt service as percentage of total expenditures
- Higher number represents less flexibility because more operating resources are being committed
- Current = 11.85%
- Strong bond rating criteria range = 8% - 15%
- NC AAA average = 10.5%

### Recommendation

- **Ratio of debt service expenditures as a percent of total governmental expenditures should not exceed 15%**

# III. 10-YEAR PAYOUT

- Measures amount of principal that will be retired in next ten years as percentage of municipality's net debt
- Lower number may indicate whether locality is back-loading its debt
- Current = 75.1%
- Strong bond rating criteria range = greater than 65%
- NC AAA average = 85%

## Recommendation

- **10-year principal payout ratio should be 65% or better**

# FUND BALANCE RESERVE POLICY

Fund Balance Reserve Policy ensures that adequate levels of fund balance are maintained to mitigate current and future risks and ensure stable tax rates.

Recommended Measures:

IV. General Fund Unassigned Fund Balance %



## IV. GENERAL FUND UNASSIGNED FUND BALANCE % TARGET

- *Unassigned Fund Balance* = portion of fund balance that is not restricted, committed, or assigned to specific purposes
- *Unassigned Fund Balance %* = unassigned fund balance as a percent of budgeted expenditures
- Current = 22%
- Strong bond rating criteria range = 10% - 22%
- NC AAA average = 24.5%

### Recommendation

- **Maintain a targeted unassigned fund balance at the close of the fiscal year equal to 22% of General Fund expenditures**



# CASH MANAGEMENT AND INVESTMENT POLICY

Cash management policy establishes sound practices and safeguards cash receipts

Investment policy provides guidance on investment of public funds

Recommended Measures:

V. Liquidity

VI. Maturity

VII. Diversification

# V. LIQUIDITY

- Measures extent to which Town has access to its cash

## Recommendation

- **No less than 20% of funds available for investment will be maintained in liquid investments**

# VI. MATURITY

- Measures date on which life of financial instrument ends, after which it must either be renewed or it will cease to exist

## Recommendation

- **Investments will mature in no more than 36 months from their purchase date**

# VII. DIVERSIFICATION

- Process of allocating capital in way that reduces exposure to any one particular asset or risk

## Recommendation

- **No more than 5% of the Town's investments may be invested in one company's commercial paper**
- **No more than 20% of the Town's investments may be invested in commercial paper**
- **No more than 25% of the Town's investments may be invested in one U.S. Agency's Securities**

# OPEB PRE-FUNDING POLICY

Other Post-Employment Benefit (OPEB) policy allows Town to develop a funding strategy for the future liability related to retiree healthcare costs.

Recommended Measure:

VIII. Pre-funding Contributions



# VIII. PRE-FUNDING CONTRIBUTIONS

- Pre-Funding Contributions – set aside funding in advance of required date of contribution for retiree healthcare costs

## Recommendation

- **Town may contribute additional amounts to prefund retiree healthcare benefits**

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