City of Amesbury

Financial Policies
A Community Compact Initiative

The Abrahams Group

October 2017

THE ABRAHAMS GROUP

FOR BETTER GOVERNMENTS

October 17, 2017

Mr. James Lynch
Chief Financial Officer
City of Amesbury
62 Friend Street
Amesbury, MA 01913

Dear Mr. Lynch:

I am pleased to submit this Financial Policies Document to the City of Amesbury. The financial policies were written with a focus on five key areas – (1) Financial Reserves, (2) Financial Forecasting, (3) Capital Improvements Planning and Budgeting, (4) Debt Management, and (5) Unfunded Liabilities. I hope that this document provides the City the guidance it seeks to make sound financial decisions for years to come.

I look forward to the adoption of the financial policies by City Council in the near future.

Sincerely yours,

Mark D. Abrahams

Mark D. Abrahams, CPA
President

Attachment

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CITY OF AMESBURY FINANCIAL POLICIES

INTRODUCTION

Financial policies are central to a strategic, long-term approach to financial management. The adoption of formal, written financial policies helps the City to:

- Institutionalize good financial management practices to promote stability and continuity.
- Clarify and crystallize strategic intent for financial management by defining a shared understanding of how the City will implement financial practices to provide the best value to the City.
- Support good bond ratings and thereby reduce the cost of borrowing.
- Manage risks to financial condition. A key component of governance accountability is not to incur excessive risk in the pursuit of public goals. Financial policies identify important risks to financial condition.
- Comply with established public management best practices from the Commonwealth of Massachusetts, the Government Finance Officers Association (GFOA), and other organizations.

This document codifies the City's financial policies including:

1. Financial Reserves
2. Financial Forecasting
3. Capital Improvements Planning and Budgeting
4. Debt Management
5. Unfunded Liabilities

The City of Amesbury is committed to safeguarding public funds, protecting local assets, and complying with financial standards and regulations. To that end, this manual of financial policies provides guidance for local planning and decision making. The policies as a whole are intended to outline objectives, provide formal direction, and define authority to help ensure sound fiscal stewardship and management practices.

The City desires that the financial policies, including those for establishing financial policies for funding and using reserves such as free cash and stabilization funds, become an integral part of the budget process.

With these financial policies, the City commits to the following objectives:

- Being fiscally responsible with municipal finances
- Providing full value to residents by delivering quality services as financially efficiently as possible
- Planning for on-going capital improvements, ensuring the quality and maintenance of capital assets

- Ensuring appropriate financial capacity for present and future needs
- Providing a measurable framework regarding the fiscal impact of the cost of government services against established benchmarks
- Maintaining and achieving the highest credit rating realistically possible
- Sustaining a consistent level of service and value for residents and businesses
- Conforming to general law, uniform professional standards, and municipal best practices
- Protecting and enhancing the City's credit rating
- Promoting transparency and public disclosure

The City's commitment to these policies and objectives will be regularly weighed against maintaining a tax rates(s), and average residential tax bill, that is near the average for Essex County. At the discretion of the Mayor, some of these policies and objectives may be prioritized or deferred in order to make the City's tax burden comparable to neighboring communities. Furthermore, the Mayor will consider and weigh out the prevailing economic environment and the needs of the public schools.

This project is funded by the Community Compact Program, an initiative striving to create clear mutual standards, expectations, and accountability for both the Commonwealth and municipalities. It is hoped that these policies provide useful guidance and consistency in the City's fiscal decisions, as the City and the Commonwealth strive to build a better government for residents and businesses. This document should be reviewed periodically to incorporate new developments in municipal finance law and best practice.

1. FINANCIAL RESERVES

OBJECTIVE

This policy establishes prudent practices for appropriating to and expending financial reserves to help the City stabilize finances and maintain operations. With well-planned sustainability, the City can use its reserves to serve as revenue sources for the annual budget, finance emergencies and other unforeseen needs, and to hold money for specific future purposes. Reserve balances and policies can also positively impact the City's credit rating and consequently its long-term cost to fund major projects.

This policy pertains to short- and long-range budget decision-making and applies to the Mayor, City Council, School Committee and City and School finance officials.

POLICY

The City commits to building and maintaining its reserves in order to provide flexibility in budgeting and to provide a funding source for tax and user charge rate stability, capital improvements, and extraordinary and unforeseen expenditures. These reserves include free cash, stabilization funds, reserve funds, and retained earnings.

Undesignated Fund Balance

Undesignated fund balance is the amount of fund balance remaining after reductions for reserves and designated balances. Fund balance is intended to serve as a measure of the financial resources available in the general fund. The City's policy is to maintain an undesignated fund balance in the general fund in an amount equivalent to no less than 10 percent of the operating expenditure budget, with a goal of 15 percent. If the balance falls below 10 percent at the end of the fiscal year, then free cash usage may be reduced to bring the amount up to 10 percent, as described in the free cash policy.

Free Cash

The Division of Local Services (DLS) defines free cash as "the remaining, unrestricted funds from operations of the previous fiscal year, including unexpended free cash from the previous year." DLS must certify free cash before the City can appropriate it.

Each year, the Chief Financial Officer will submit to the Division of Local Services (DLS) a year-end balance sheet, a balance sheet checklist, a statement of indebtedness, accounts receivable and cash reconciliations, and a free cash schedule. Once DLS certifies free cash, the City may appropriate these funds for any legal purpose.

As much as practicable, the City will limit its use of free cash to funding one-time expenditures (like capital projects or emergencies and other unanticipated expenditures). Budget decision-makers will plan to preserve a portion of free cash so that the succeeding year's calculation can begin with a positive balance.

General Stabilization

The City shall establish stabilization funds consistent with MGL Chapter 40, Section 5B, which allows municipalities to create one or more stabilization funds and appropriate any amount into the funds. Stabilization funds may be established by a majority vote of City Council upon recommendation by the Mayor. Once established, monies can be transferred into or out of the stabilization fund by two-thirds vote of the City Council upon recommendation by the Mayor. Any interest shall be added to and become part of the fund.

The City may dedicate, without further appropriation, all, or a percentage not less than 25 percent, of a particular fee, charge or other receipt to any stabilization fund established pursuant to MGL Chapter 40, Section 5B; provided, however, that the receipt is not reserved by law for expenditure for a particular purpose. For purposes of the general stabilization fund, a receipt will not include taxes or excises assessed pursuant to Chapter 59, Section 25, Chapter 60A, Chapter 60B, Chapter 61, Chapter 61A or Chapter 61B or surcharges assessed pursuant to Chapter 40, Section 39M or Chapter 44B. A dedication would be approved by a two-thirds vote of the City Council, and may be terminated in the same manner. A vote to dedicate or terminate a dedication shall be made before the fiscal year in which the dedication or termination is to commence and will be effective for at least three fiscal years.

The City will endeavor to maintain a minimum balance of five (5) percent of the current operating budget in its general stabilization fund. Withdrawals from the general stabilization fund should only be used to mitigate emergencies or other unanticipated events that cannot be supported by current general fund appropriations. When possible, withdrawals of funds should be limited to the amount available above the five-percent minimum reserve target level. If any necessary withdrawal drives the balance below the minimum level, the withdrawal should be limited to one-third of the general stabilization fund balance. Further, the Chief Financial Officer will develop a detailed plan to replenish the fund to the minimum level within the next two (2) fiscal years.

Capital Stabilization

The City will establish and appropriate annually to the capital stabilization fund so that, over time, it achieves a balance sufficient to cover the City's cash outlay for capital. The City's capitalization policy is any fixed asset equal to or greater than $5,000 with a useful life greater than one year and any infrastructure investment equal to or greater than $25,000 are capitalized. As a general rule, subject to review, the City's maximum amount of cash outlay for capital is $100,000 for any one particular item. Any capital item in excess of this amount may be financed through the use of short- and/or long-term borrowings. By establishing this policy, the City will pay capital outlays for minor and moderate capital expenditures and thereby preserve debt capacity for major, higher-dollar purchases or projects. This approach balances debt with pay-as-you-go practices and protects against unforeseen costs.

Overlay Reserve Fund

The City's Overlay Reserve fund (allowance for abatements and exemptions), or Overlay, will be established annually in the General Fund consistent with MGL Chapter 59, § 23, 25, and 70A, as amended by Chapter 218, § 131, 133, 152 and 249 of the Acts of 2016

The City shall annually establish the Overlay via the Tax Recapitulation Sheet. Overlay is an account to fund anticipated abatements and exemptions of committed real and personal property taxes. The overlay amount is determined by the board of assessors (assessors) and may be raised in the tax rate without appropriation. Excess overlay is determined, certified and transferred by vote of the assessors to the Overlay Surplus Account. Overlay surplus may then be appropriated by the City Council for any lawful purpose until the end of the fiscal year, i.e., June 30. Overlay surplus not appropriated by year-end is closed to the general fund undesignated fund balance.

Under the Municipal Modernization Amendments, overlay is now a single account for purposes of funding abatements or exemptions granted for any fiscal year. Previously, a separate overlay account was established for each fiscal year and that account could only be charged for abatements and exemptions for that year's taxes.

Annually, the Chief Financial Officer will review the Overlay balances with the Board of Assessors and request the Board of Assessors to declare unneeded Overlay balances as surplus. Once Overlay is declared surplus, the surplus will be transferred to the Overlay Surplus Account. The Overlay Surplus Account may be appropriated by the City Council during the fiscal year for any legal purpose. At the end of the fiscal year, any balance in the overlay reserve fund shall be closed to the general fund undesignated fund balance account.

SPED Reserve Fund

Under Chapter 40, Section 13E, the City may establish a SPED Reserve Fund, upon the recommendation of the School Committee and the acceptance by majority vote of the City Council upon recommendation by the Mayor. The School Department is authorized to retain any unexpended funds of the present fiscal year so voted, to be placed in a separate reserve fund to be utilized in the upcoming fiscal year or years, to pay, without further appropriation, for unanticipated and/or unbudgeted costs of special education, out-of-school-district tuition and/or transportation. School Committee may include a separate line item in their annual budget request to appropriate monies into the SPED reserve fund. Funds can only be expended or transferred out after a majority vote of both the School Committee and City Council. The balance in such separate SPED reserve fund shall not exceed two (2) percent of the annual required net school spending of the school district.

Retained Earnings

MGL Chapter 44 Section 53F ½ allows the establishment of enterprise funds to account for City activities that operate similar to a business where the intent is to recover total costs primarily through user charges including utilities (i.e., water and sewer), health, transportation and recreation. By accounting for each utility's revenues and expenditures in individual funds segregated from the general fund, the City can identify the true costs of each service—direct, indirect, and capital—and recover these through user fees and other charges. Retained earnings are maintained in the respective enterprise funds and are not closed to the general fund's undesignated fund balance.

For each enterprise fund, the City will maintain an unreserved retained earnings balance of 10 percent of the enterprise fund's total annual budget, at minimum, with the objective of 20 percent, but any reserve may be significantly higher if major infrastructure improvements are necessary. These retained earnings would be used to provide rate stabilization, offset revenue shortfalls due to declining consumption or revenue shortfalls, and to fund major, future capital projects. To maintain the target reserve levels for each enterprise fund requires the respective departments to periodically review, and when necessary, recommend rate, fee and other charges adjustments to the Mayor.

REFERENCES

- Reserve Funds: MGL c. 40, §5A
- Stabilization Funds: MGL c. 40, §5B
- SPED Reserve Funds: Section 24 of Chapter 218 of the Acts of 2016
- Water Infrastructure Surcharges: MGL c. 40, §39M
- Community Preservation (with sections on assessment of surcharges): MGL c. 44B
- Additional Local Assessments: MGL c. 59, §25
- Motor Vehicle Excise Tax: MGL c. 60A
- Boat Excise Tax: MGL c. 60B
- Forest Tax: MGL c. 61
- Agricultural and Horticultural Land Tax: MGL c. 61A
- Recreational Land Tax: MGL c. 61B
- Enterprise Funds: MGL c. 44, §53F½
- DLS Best Practice: Free Cash
- DLS Best Practice: Reserve Policies
- DLS Best Practice: Special Purpose Stabilization Funds
- DLS Informational Guideline Release 08-101: Enterprise Funds
- DLS Informational Guideline Release 04-201: Creation of Multiple Stabilization Funds
- MA Clean Water Trust Best Practice: Full Cost Pricing http://www.mass.gov/treasury/docs/mwpat/inthenews/full-cost-pricing.pdf
- MA Clean Water Trust Best Practice: Enterprise Funds
- http://www.mass.gov/treasury/docs/mwpat/inthenews/entereprise-fund.pdf
- Government Finance Officers Association Best Practice: Appropriate Level of

Unrestricted Fund Balance in the General Fund
- American Water Works Association Cash Reserves Draft Policy

ADOPTION DATE

This policy was adopted on ___________________.

EFFECTIVE DATE

This policy became effective on ___________________.

2. FINANCIAL FORECASTING

OBJECTIVE

A financial forecast conservatively projects revenues and expenditures over a multi-year period. It is designed to allow the City to evaluate the impact of various decisions and policy choices over time. A financial forecast includes reasonable assumptions that must be continuously evaluated and updated to reflect changing circumstances and events. By doing so, the forecast provides a fair representation of the City's fiscal future built to help guide the budget process and planning.

The main goals of a financial forecast are to conservatively project revenues and expenditures over a period of years based on documented assumptions and to provide a tool to continuously update those assumptions and forecasts. The financial forecast is not intended to present a balanced forecast, which is the function and role of a budget.

POLICY

The City commits to conduct an annual financial forecast to facilitate long-range financial planning.

Revenue Guidelines

Revenues will be forecasted conservatively. The City will continuously seek to diversify its revenue to broaden financial resources and improve the equity and stability of sources. Each year and whenever appropriate, the City will reexamine existing revenues and explore potential new sources. Additionally, intergovernmental revenues (e.g., local aid, grants) will be reviewed annually to determine their short- and long-term stability in order to minimize detrimental impacts.

The City will avoid using one-time revenues to fund ongoing or recurring operating expenditures. These one-time revenue sources can include, but are not limited to, free cash, overlay surplus, sale of municipal equipment, legal settlements, insurance proceeds, and gifts. Additionally, the City hereby establishes the following priority order when appropriating one-time revenues:

- Free Cash
- General stabilization fund
- Capital stabilization fund
- Other

Economic downturns or unanticipated fiscal stresses may compel reasonable exceptions to the use of one-time revenues. In such cases, the Mayor will recommend to the City Council its use for operational appropriations. Such use will trigger the Chief Financial Officer to develop an action plan to avoid continued reliance on one-time revenues.

Historically, bond premiums (net of issuance costs) have been considered general one-time revenue to be used as an available source. Chapter 218 of the Acts of 2016 amends current law by allowing communities to either apply the proceeds to the issuance, thereby reducing the amount needed to borrow, or to place the money in a separate fund and appropriate it for a future capital project. (Note: Premiums received for excluded debt must still be used to offset the stated interest costs of financing the project.)

State laws impose further restrictions on how certain types of one-time revenues may be used. The City will consult the following General Laws when the revenue source is:

- Sale of real estate: M.G.L. c. 44, §63 and M.G.L. c. 44, §63A
- Gifts and grants: M.G.L. c. 44, §53A and M.G.L. c. 44, §53A½

This policy further entails the following expectations regarding revenues:

- The Assessing department will maintain property assessments for the purpose of taxation at full and fair market value as prescribed by state law and will provide new growth information.
- City departments that charge fees will annually review their fee schedules and propose adjustments when needed to ensure coverage of service costs.
- The Water/Sewer department will set rates for the enterprise operations sufficient to cover all their direct, indirect, and capital improvement costs on self-supporting bases.
- The Building department will notify the Chief Financial Officer of any moderate-to-large developments that could impact building permit volume.
- Department heads will strive to seek out all available grants and other aid and will carefully consider any related restrictive covenants or matching requirements (both dollar and level-of-effort) to determine the cost-benefit of pursuing them.
- Revenue estimates will be adjusted throughout the budget cycle as more information becomes available.

Expenditure Guidelines

Annually, the City will determine a particular budget approach for forecasting expenditures, either maintenance (level service), level funded, or one that adjusts expenditures by specified increase or decrease percentages (either across the board or by department). A maintenance budget projects the costs needed to maintain the current staffing level and mix of services into the future. A level- funded budget appropriates the same amount of money to each municipal department as in the prior year and is tantamount to a budget cut because inflation in mandated costs and other fixed expenses still must be covered.

Financial Forecast Guidelines

To determine the City's operating capacity for each forthcoming fiscal year, the Chief Financial Officer will annually create and provide the Mayor with a detailed budget forecast. The Chief Financial Officer will also annually prepare a [five]-year financial projection of revenues and expenditures for all operating funds. These forecasts shall be used as planning tools in developing the following year's operating budget as well as the five-year capital improvement plan.

To ensure the City's revenues are balanced and capable of supporting desired levels of services, forecasts for property taxes, local receipts, and state aid will be conservative and based on historical trend analyses and will use generally accepted forecasting techniques and appropriate data. To avoid potential revenue deficits, estimates for local receipts (e.g., inspection fees, investment income, license fees) should generally not exceed [90] percent of the prior year's actual collections without firm evidence that higher revenues are achievable.

Additionally, the City's forecast model should assume that:

- The current level of services will be maintained.
- Municipal salaries and wages will be forecasted consistent with contractual agreements. Where the forecast period extends beyond collective bargaining agreements, three year averages will be utilized.
- Municipal salaries and wages will be forecasted as follows:
  - Teachers will be forecasted consistent with their collective bargaining lanes and steps.
  - Non teachers will be forecasted consistent with contractual agreements. Where the forecast period extends beyond collective bargaining agreements, three year averages will be utilized.
- Non salary expenditures will be forecasted based on (1) contractual provisions for known and measurable costs, (2) three year averages or (3) inflation, whichever is more practical.
- Historical trends in the growth of specific operating expenses and employee benefits will prevail.
- Potential cost-of-living adjustment estimates for the impact of future contract settlements and compensation plan increases are included.
- Debt service on existing debt will be paid and Capital Planning and Debt Management policies will be followed.
- Annual pension contributions and appropriations to amortize its other postemployment benefit liabilities will continue.
- New growth will be projected conservatively, taking into account the City's three-year average by property class.
- Local receipts and state aid will reflect economic cycles.
- Reserves will be built and maintained in compliance with its Financial

Reserves policy.

REFERENCES

- Chapter 218 of the Acts of 2016, Section 67 M.G.L. c. 44, §20
- M.G.L. c. 44, §53A
- M.G.L. c. 44, §53A½
- M.G.L. c. 44, §63
- c. 44, §63A
- Division of Local Services Best Practice: Revenue and Expenditure Forecasting
- Division of Local Services Bulletin 2013-01B: Bond Premiums and Debt Exclusions
- Government Finance Officers Association article: Structuring the Revenue Forecasting Process
- City of Amesbury Financial Forecast

ADOPTION DATE

This policy was adopted on __________________.

EFFECTIVE DATE

This policy became effective on __________________.

3. CAPITAL IMPROVEMENTS PLANNING AND BUDGETING

Policies designed to guide capital planning help to assure that the City's capital needs are fully considered in the capital planning process. Effective policies can also help the City to assure the sustainability of its infrastructure by establishing a process for addressing maintenance, replacement, and proper fixed asset accounting over the full life of capital assets. In addition, capital planning policies can strengthen the City's borrowing position by demonstrating sound fiscal management and showing the City's commitment to maximizing benefit to the public within its resource constraints.

Good capital planning policies can lead to the development of a capital plan that is consistent with best practices; however, they do not constitute the capital plan itself. Rather, capital planning policies establish a framework in which stakeholders understand their roles, responsibilities, and expectations for the process and an end result. Ideally, such policies also include guidelines for coordinating capital projects and promoting sound, long-term operational and capital financing strategies.

To create a sustainable capital plan, the Chief Financial Officer and other participants in the capital planning process need to consider all capital needs as a whole, assess fiscal capacity, plan for debt issuance, and understand impact on reserves and operating budgets, all within a given planning timeframe. Capital planning policies provide an essential framework for managing these tasks and for assuring that capital plans are consistent with overall organizational goals.

POLICY

The City shall develop and adopt capital planning policies that take into account the city's unique organizational characteristics including the services it provides, how the services are structured, and their external environment.

The City's capital plan provides:

- A description of how the City will approach capital planning, including how stakeholder departments will collaborate to prepare a plan that best meets the operational and financial needs of the organization.
- A clear definition of what constitutes a capital improvement project.
- Establishment of a capital improvement process.
- Identification of how decisions will be made in the capital planning process including a structured process for prioritizing need and allocating limited resources including an assessment of the City's fiscal capacity so that the final capital plan is based on what can realistically be funded by rather than being simply a wish list of unfunded needs.
- A procedure for accumulating necessary capital reserves for both new and replacement purchases.

- A policy for linking funding strategies with the useful life of the asset including identifying when debt can be issued and any restrictions on the length of debt.
- A requirement that a multi-year capital improvement plan be developed and that it include long-term financing considerations and strategies.
- A process for funding to ensure that capital project funding is consistent with legal requirements regarding full funding, multi-year funding, or phased approaches to funding.

Capital Asset Definition

A capital asset is a tangible item that has a value of $5,000 or higher and an estimated useful life of in excess of one year.

Capital Project Definition

A capital improvement project is any project that improves or adds to the City's tangible infrastructure, has a substantial useful life of 5 years or longer, and costs $25,000 or more in total, regardless of funding source. Examples of capital projects include the following:

- Construction of new buildings
- Major renovation of, or additions to, existing buildings
- Land acquisition or major land improvements
- Street, sidewalk, or parking lot reconstruction and resurfacing
- Water system construction and rehabilitation
- Sewer and storm drain construction and rehabilitation
- Major vehicle or equipment acquisition and/or refurbishment
- Planning, feasibility studies, and design for potential capital projects

Capital Planning Process

The City will continually develop and maintain a five (5) year capital improvement program. This will include maintaining an updated inventory of capital assets, including fixed assets and infrastructure. The City will maintain a capital asset inventory consistent with Generally Accepted Accounting Principles. The capital asset inventory will be distributed by the Chief Financial Officer to City departments and the School Department annually. The City departments will submit capital requests based on useful live schedules and priorities. The City will determine the status of previously approved projects including City Council appropriations and balances within capital projects funds and develop a priority listing of projects. Consideration will be given to projects that:

- Are necessary to maintain the City's current infrastructure
- Involve correcting a current Safety or Health issue, and/or to meet a Federal or State legal requirement

- Are designed to modernize and upgrade existing City facilities
- Are required to increase capacity of existing facilities in order to accommodate the increase in growth of the City

City departments will submit capital projects using an inventory of capital form submission which should, for each item, identify:

- The capital request control number
- Description of the request
- Location
- Responsible department and individual
- Department priority
- Total cost
- Number of years until completion
- Expenditures by fiscal year
- Suggested financing plan
- Operating and maintenance cost impact
- Project justification

Capital Budgeting Process

Each capital project shall have a corresponding plan to finance the capital asset or improvement. The financial analysis helps the City determine how much it can afford to finance considering current revenues, expenditures and debt capacity. Consideration will be given to:

- Smoothing out the tax rate
- Balance debt service (principal and interest) payments
- Determine debt service levels and debt capacity
- Maximizing other financing sources including
  - Reallocated Capital Project Funds
  - State & Federal Grants
  - Special Assessments and Betterments
  - Revolving Funds
  - Enterprise Funds
  - Community Preservation Funds
  - Gifts and Donations
  - Public Private Partnerships
  - Mitigation funds
- Stabilization Funds
- Debt—General Obligation Bonds & Exclusions
- Pay-as-you-go—Operating Budget or Free Cash

The major focus of the capital budgeting process is to determine the amount of capital improvements the City can afford. Capital budgeting works well when aligned with other City financial policies such as:

- Debt Policy – debt service should not exceed 10% of annual operating expenditures
- Undesignated Fund Balance and Free Cash Policies – the City should maintain a minimum of 10 percent of the operating expenditure budget, with a goal of 15 percent
- Financial Reserve Policy – the City should maintain financial reserves consistent with these policies
- Capital Stabilization Policy - the City should maintain financial reserves consistent with these policies
- Financial Forecasts – the City should plan capital projects and acquisitions to maintain a balanced financial forecast

The Five Year Capital Improvement Program will be adopted annually by the City Council upon recommendation by the Mayor. The first year of the capital budget will be integrated with the annual City budget.

Capital Monitoring

The City should monitor capital project activity on a regular basis. Such monitoring should include a review of project accounts, budgets, and transactions. It should also include confirming the adequacy of cash flow and revenue sources for the corresponding project.

REFERENCES:

- GFOA Best Practice, Capital Planning, (Multi-Year Capital Planning (2006)
- GFOA Best Practice, The Role of Master Plans in Capital Improvement Planning (2008)
- GFOA Best Practice, Asset Maintenance and Replacement, 2010
- GFOA Best Practice, Understanding Your Continuing Disclosure Responsibilities, 2010
- GFOA Best Practice, Establishing Appropriate Capitalization Thresholds for Capital Assets, 2006
- Capital Improvement Programming: A Guide for Smaller Governments, GFOA, 1996
- Recommended Budget Practices: A Framework for Improved State and Local Government Budgeting, National Advisory Council on State and Local Budgeting, 1998.

- Managing the Capital Planning Cycle: Best Practice Examples of Effective Capital Program Management, Government Finance Review, GFOA, 2004.
- Capital Budgeting and Finance: A Guide for Local Governments, ICMA, 2004.
- Abrahams, Mark D. The Nuts and Bolts of Capital Programming and Budgeting, The Municipal Advocate.

ADOPTION DATE

This policy was adopted on ________________.

EFFECTIVE DATE

This policy became effective on ________________.

4. DEBT MANAGEMENT

OBJECTIVE

Debt management policies are written guidelines that document the debt issuance practices of the City. A debt management policy should improve the quality of decisions, articulate policy goals, provide guidelines for the structure of debt management, and demonstrate a commitment to long-term capital and financial planning. Adherence to a debt management policy signals to rating agencies and the capital markets that the City is well managed and therefore is likely to meet its debt obligations in a timely manner. Debt management policies should be written with attention to the City's specific needs and available financing options and are typically implemented through more specific operating procedures. Finally, debt management policies should be approved by the City to provide credibility, transparency and to ensure that there is a common understanding among elected officials and staff regarding the city's approach to debt financing.

The purpose of this policy is to establish written guidelines and restrictions for issuing debt and managing the outstanding debt portfolio, and to provide guidance to decision makers regarding the purposes for which debt may be issued, types and amounts of permissible debt timing and method of sale that may be used, and structural features that may be incorporated. Adherence to a debt management policy helps to ensure that government maintains a sound debt position and that credit quality is protected.

POLICY

The City's debt management policy exists to:

- Ensure high quality debt management decisions
- Impose order and discipline in the debt issuance process
- Promote consistency and continuity in the decision making process
- Demonstrate a commitment to long-term financial planning objectives
- Ensure that the debt management decisions are viewed positively by the rating agencies, investment community, and taxpayers

Massachusetts General Laws, Chapter 44, Sections 7 & 8 regulate the purposes for which municipalities may incur debt, and the maximum maturity for bonds issued for each purpose. MGL Chapter 44, Section 10 specifies that the debt limit for cities is 5% of Equalized Valuation. Various federal laws, regulations and agencies also have requirements with which the City must comply.

Capital Improvement Plan

The City shall establish and maintain a five (5) year Capital Improvement Plan (CIP), including all proposed projects and major pieces of equipment that may require debt financing. The City's long-term debt strategies shall be structured to reflect its capital needs and ability to finance.

Bond Rating

The City's bond rating is important because it determines the rate of interest it pays when selling bonds and notes as well as the level of market participation (number of bidders). Other things being equal, the higher the bond rating, the lower the interest rate. Bond analysts including Moody's, Standard & Poor's, and Fitch typically look at the following four factors in assigning a credit rating:

- **Debt Factors**: debt per capita, debt as a percentage of equalized valuation, debt service as a percent of operating budget, rate of debt amortization, and the amount of exempt versus non-exempt debt.
- **Financial Factors**: operating surpluses or deficits, free cash as a percent of revenue, state aid reliance, property tax collection rates, and unfunded pension liability.
- **Economic Factors**: property values, personal income levels, tax base growth, tax and economic base diversity, unemployment rates, and population growth.
- **Management Factors**: governmental structure, the existence of a capital improvement plan (CIP), financial forecast, and financial policies, the quality of accounting and financial reporting, etc.

The City shall continually strive to maintain the highest bond rating through sound financial management, improved receivables management, accounting and financial reporting, and increased revenues and other financing sources such as the General Stabilization Fund and the Capital Stabilization Fund.

Debt Guidelines

General Fund Debt Service: The City recognizes that maintaining debt levels within supportable standards favorably impacts credit ratings and ensures the City will have an affordable repayment obligation on residents. Due to Proposition 2 1/2 constraints, it is important to limit debt service costs as a percentage of the city's total budget. At the same time, the regular and well-structured use of long-term debt signifies commitment to maintaining and improving its infrastructure.

Municipal credit analysts often use 10% as a maximum benchmark for financial soundness. In order to stabilize the desired ceiling, it will be necessary for the City to schedule future debt service to coincide with maturing debt service. The City will strive to obtain these financial targets.

1) It shall be the City's policy to establish a debt service ceiling of 10%. The annual debt service payable on bonded general fund debt including debt

exclusions net of aid subsidies, reimbursements and offsets shall not exceed 10% of the annual operating budget.

2) Debt financing for projects supported by General Fund revenue shall be reserved for capital projects and expenditures which either cost in excess of $100,000 or have an anticipated life span of five years or more.
3) Total outstanding general obligation debt shall not exceed 5.0 % of the total assessed value of property.

4) Bond maturities for all City issued debt shall not exceed the anticipated useful life of the capital project being financed, except for major buildings, infrastructure, and water and sewer projects. The City will evaluate market rates to see if refunding debt can save the City money.

Debt Maturity Schedule

As previously stated, Chapter 44 of the General Laws specifies the maximum maturity for bonds issued for various purposes. However, with a reasonable maturity schedule, a City may choose to borrow for a shorter period than allowed by the statutory limit in order to reduce interest costs. Except for major buildings and water, sewer, and community preservation projects, it shall be the City's policy that bond maturities shall be limited to no more than ten years or a maturity that is consistent with the life of the asset financed. Exceptions may be made when grants, reimbursements or other situations warrant the City's goal of aggressive amortization of new debt service, and shortening terms for existing debt when there is an opportunity to refinance a bond at a lower cost. Bond maturities shall not exceed the anticipated useful life of the capital project being financed. It shall be the goal of the City to maintain bond maturities so that at least 60% of the outstanding debt (principal net of debt exclusion and enterprise fund amounts) shall mature within 10 years.

Debt Strategies

The City shall:

- Issue long-term debt only for objects or purposes that are financially supported and authorized by state law
- Use available funds to the greatest extent possible to reduce the amount of borrowing on all debt-financed projects
- Confine long-term borrowing to capital improvements and projects that cost at least [$25,000] and that have useful lifespans of at least [five] years or whose lifespans will be prolonged by at least [five] years
- Refrain from using debt to fund any recurring purpose, such as current operating and maintenance expenditures
- The City shall continually pursue opportunities to finance the capital budget by means other than conventional borrowing such as state and/or federal grant funding, use revenue bonds, special assessment bonds, or other types of self-supporting bonds instead of general obligation bonds

whenever possible

- Capital projects for enterprise operations shall be financed solely from enterprise revenues. Debt financing shall be reserved for capital projects and expenditures that cost in excess of $100,000 for projects supported by enterprise fund revenue.

Debt Issuance

The City shall work closely with the City's Financial Advisor and Bond Counsel to ensure that all legal requirements are met and that the lowest possible interest rate can be obtained. This includes preparation of the official statement, preparation of all required documents, and compliance with reporting requirements.

REFERENCES:

- MGL Chapter 44 §7
- MGL Chapter 44 §8
- MGL Chapter 44 §6
- Division of Local Services Guidance: Understanding Municipal Debt
- GFOA Best Practice, Selecting Bond Counsel, 2008.
- GFOA Best Practice, Selecting Financial Advisors, 2008.
- GFOA Best Practice, Selecting Underwriters for a Negotiated Bond Sale, 2008.
- GFOA/NABL Post Issuance Compliance Checklist, 2003.
- Benchmarking and Measuring Debt Capacity, Rowan Miranda and Ron Picur, GFOA, 2000.
- A Guide for Preparing a Debt Policy, Patricia Tigue, GFOA, 1998.
- GFOA, Small Cities Debt Indicators

ADOPTION DATE

This policy was adopted on __________________.

EFFECTIVE DATE

This policy became effective on __________________.

5. UNFUNDED LIABILITIES

Compensation packages for active workers may include health-care and pension benefits for employees who have completed their active service. These represent a significant challenge in terms of their funding and long-term sustainability. Meeting this challenge will require the City to ensure that these benefits are sustainable over the long term – that they are affordable to stakeholders, competitive, and sufficient to meet employee needs, and that they may be reasonably expected to remain so.

Unfunded liabilities represent a significant financial obligation of the City. Unfunded liabilities are defined as "the actuarial calculation of the value of future benefits payable less the net assets of the fund at a given balance date." The two primary unfunded liabilities are for Pension Benefits and Other Post – Employment Benefits (OPEB), primarily Retiree Health Insurance.

POLICY

The City shall be in compliance with pension and OPEB requirements as promulgated by the Commonwealth of Massachusetts, the Federal Government and the Governmental Accounting Standards Board. The City shall annually appropriate sufficient funds to (1) meet the pay as you go amount and (2) to contribute additional amounts in a prudent manner with the ultimate goal to fully-fund its actuarially calculated Annual Required Contribution (ARC).

Pension

The Essex County Retirement System is a defined benefit program that is governed by Massachusetts General Laws, Chapter 32 and is regulated by the Public Employee Retirement Administration Commission (PERAC), a State entity responsible for the oversight, guidance, monitoring, and regulation of Massachusetts' public pension systems.

Funding for this system covers the pension costs of Amesbury employees who are part of the Essex County Retirement System, which does not include teachers, as their pensions are funded by the State. In accordance with State law, PERAC regulations and government accounting standards, the Essex County Retirement System contracts for an actuarial valuation of the retirement system to quantify the unfunded liability on a biennial basis.

Under current State law, the Essex County Retirement System establishes a funding schedule to fully-fund this liability by at least FY 2040, if not sooner. The City shall continue to fund this liability in the most fiscally prudent manner, by funding in full the annual City assessment.

Other Postemployment Benefits (OPEB)

Other Postemployment Benefits (OPEB) consists primarily of the costs associated with providing health insurance for retirees and their spouses. OPEB covers retiree benefits other than pensions. OPEB is governed substantially by pronouncements of the Government Accounting Standards Board (GASB) and MGL Chapter 32B, Section 20.

The City will maintain an "Other Post-Employment Benefits Liability Trust Fund" or "OPEB Fund"; consistent with Chapter 32B Section 20. The City may appropriate amounts to be credited to the fund and the City Treasurer may accept gifts, grants and other contributions to the fund. The OPEB Fund shall be a Trust Fund subject to appropriation and shall be managed by a trustee or a board of trustees. Any interest or other income generated by the fund shall be added to and become part of the fund. All monies held in the fund shall be accounted for separately from other funds of the City and shall not be subject to the claims of any general creditor of the governmental unit. Employer contributions to the fund shall be irrevocable.

The OPEB Fund exists for the benefit of retired employees and their dependents and the reduction and elimination of the City's unfunded liability for such benefits.

The City Treasurer shall be the custodian of the OPEB Fund and shall be bonded in any additional amounts necessary to protect fund assets. The duties and obligations of the trustee or board of trustees with respect to the fund shall be set forth in a declaration of trust to be adopted by the trustee or board. The declaration of trust and any amendments thereto shall be filed with the Mayor and City Clerk.

The City shall annually appropriate sufficient funds to (1) meet the pay as you go OPEB amount and (2) to contribute additional amounts to the OPEB Fund in a prudent manner with the ultimate goal to fully-fund its actuarially calculated Annual Required Contribution (ARC). The City's enterprise funds shall annually appropriate sufficient amounts to fully fund the ARC from enterprise fund receipts. To address the OPEB liability, decision makers shall analyze a variety of funding strategies and subsequently implement them as appropriate with the intention of fully funding the obligation. The Town shall derive funding to invest in the OPEB trust from taxation, free cash, and any other legal form. Achieving full funding of the liability requires the Town to commit to funding its annual required contribution (ARC) each year, which is calculated based on actuarial projections. Among strategies to consider for funding the ARC:

- Appropriate amounts equal to the Town's Medicare Part D reimbursements
- Determine and commit to appropriating annual portions of free cash
- Appropriate a percentage of ongoing revenues that is increased incrementally each year
- Dedicate a revenue stream
- Once the pension system is fully funded, on a subsequent annual basis,

appropriate to the OPEB trust amounts equivalent to the former pension-funding payment

Amounts in the OPEB Fund may be appropriated by a two thirds vote of the City Council upon recommendation of the Mayor, to pay the City's share of health insurance benefits for retirees and their dependents upon certification by the trustee or board of trustees that such amounts are available in the fund. The City Treasurer after consulting with the Mayor shall determine the amount to be appropriated from the fund to the annual budget for retiree health insurance and notify the trustee or board of trustees of that amount at the earliest possible opportunity in the annual budget cycle. Upon notification, the trustee or board of trustees shall take diligent steps to certify those funds as available for appropriation by the City, or will be available by the time the appropriation would become effective or provide an explanation why the funds are or will not be available or should not be made available.

The City will periodically evaluate and design benefits to help control costs and ensure that postemployment benefits are sustainable by evaluating the structure of offered benefits and their cost drivers while at the same time avoiding benefit reductions that would place undue burdens on employees or risk making the City an uncompetitive employer.

Monies in the OPEB Fund not required for expenditures or anticipated expenditures, shall be invested and reinvested by the custodian as directed by the trustee or board of trustees from time to time; provided such investment is made in accordance with MGLs, including potentially investing in the State Retiree Benefits Trust Fund or other alternatives.

REFERENCES

- M.G.L. c. 32
- M.G.L. c. 32B, §20
- M.G.L. c. 44, §54
- M.G.L. c. 44, §55
- M.G.L. c. 203C, §3
- Chapter 218 of the Acts of 2016
- An Elected Official's Guide to Defined Benefit and Defined Contribution Retirement Plans, Nicholas Greifer, GFOA, 1999.
- GFOA Best Practice, Pension Investment Policies, 2003.
- GFOA Checklist, Investment Policy Checklist for Pension Fund Assets
- GASB Statement 74: Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, July 2016.
- GASB Statement 75: Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, July 2017.
- GFOA Best Practice: Ensuring Other Postemployment Benefits (OPEB)

Sustainability.

ADOPTION DATE

This policy was adopted on ___________________.

EFFECTIVE DATE

This policy became effective on ___________________.