



To: Finance Committee

William T. Lichter
Village Manager

From: Leonard J. Flood
Director of Finance

Date: April 17, 2007

Subject: Financial Policy Update 2007

Below are various sections of proposed amendments to the Village's Financial Policies. These changes are being recommended as result of a review undertaken by the Finance Department staff as well as policy decisions that have been made in regard to the FYE 2008 Village Board. The following information will provide the Finance Committee information as to whether or not the changes are technical corrections to existing policies, deletions of out dated or obsolete policies or new policies.

In cases where existing policies are presented with recommended revisions or deletions, both the old policy and the redlined version of the revised changes are presented. In the case of new policies, specifically those related to the DuPage Water Commission rebate and the use of Utility Tax revenue, the new policies are shown in their entirety.

CAPITAL BUDGET POLICY: The changes to this policy are minor *technical changes* in policy language.

OLD POLICY: Adopted December 3, 1987

The Village will develop a multi-year plan for capital improvements updated annually and will budget all capital improvements in accordance with the plan. Various funding sources including sales tax, motor fuel tax, a portion of water and sewer revenues, utility tax, revenue sharing and public benefit will be allocated to support these improvements. In addition, the Village will consider long term debt borrowing for projects where applicable.

The Village will maintain its physical assets at a level adequate to protect the capital investment and to minimize future maintenance and replacement cost. The operating budget will provide for adequate maintenance and orderly replacement of the capital plant and equipment from current revenues where possible.

Capital investment objectives will be prioritized by the Village Board and appropriately reflected in the capital budget.

REVISED POLICY:

The Village will develop a multi-year plan for capital improvements updated annually and will budget all capital improvements in accordance with the plan. Various funding sources including sales tax, motor fuel tax, a portion of water and sewer revenues, telecommunication and utility taxes, public benefit and TIF property tax will be allocated to support these improvements. In addition, the Village will consider long term debt borrowing for projects where applicable.

The Village will maintain its physical assets at a level adequate to protect the capital investment and to minimize future maintenance and replacement cost. The operating budget will provide for adequate maintenance and orderly replacement of the capital plant and equipment from current revenues where possible.

Capital investment objectives will be prioritized by the Village Board and appropriately reflected in the capital budget.

FUND BALANCE AND RESERVE POLICY: The changes to this policy are minor *technical changes* in policy language.

OLD POLICY: Adopted December 3, 1987; Revised November 1, 2001; Revised May 1, 2003

As of June 1, 2002, the General Fund contains revenues and expenditures that were previously shown in a number of separate funds. These include the following special revenue accounts which had been separate funds prior to GASB 34: Special Service Area #3, Donations, Seizure, Foreign Fire Insurance, Hotel Motel Tax, Economic Incentive, IMRF/Social Security, Recycling, and Liability Insurance. These funds are now accounts within the General Fund and their fund balances are now reported as restricted. In addition to the aforementioned accounts, Technology Reserve has also been merged into the General Fund and the fund balance is now reported as unrestricted – designated. Finally, the former Emergency Preparedness, MIS O & M and Health Insurance Funds have been merged into the General Fund and are now reported, along with the fund balance from the old General Fund, as unrestricted – undesignated.

The Village will establish an adequate fund balance to pay for expenses caused by unforeseen emergencies or for shortfalls caused by revenue declines. For the General Fund (*unrestricted – undesignated*), Water and Sewer Fund and Parking System Fund, the fund balance will be maintained at an amount which

represents an average of three (3) months operating expenditures. Any fund balances exceeding these amounts will be appropriately budgeted in programs experiencing the most need as determined by the Village Board.

The Liability Insurance Account will maintain a reserved fund balance equal to the actuarially determined amount required to make future payments on workers compensation and property and casualty losses. In addition, an unreserved fund balance of ten percent (10%) of total annual expenditures shall be maintained to cover additional unanticipated insurance costs or reserve requirements. The Village will establish a contingency expenditure reserve to provide for unanticipated expenditures of a non-recurring nature or to meet unexpected increases in service delivery costs.

REVISED POLICY:

In accordance with GASB 34, the General Fund contains revenues and expenditures for accounts that are restricted in their use by statute. These included Special Service Area #3, Donations, Seizure, Foreign Fire Insurance, Hotel Motel Tax, Economic Incentive, IMRF/Social Security, Recycling, Grants, Business District #1, DUI User Fee, and Liability Insurance. In addition, the General Fund contains two accounts, the Technology Reserve account and the Utility Tax Reserve account that are considered unrestricted but designated. The General Fund also includes the corporate account consisting of all general operating revenues and expenditures. Finally, the Water and Sewer Fund contains an unrestricted but designated Lake Michigan Water Reserve account..

The Village will establish an adequate fund balance to pay for expenses caused by unforeseen emergencies or for shortfalls caused by revenue declines. For the General Fund (*unrestricted – undesignated*), Water and Sewer Fund (*unrestricted – undesignated*) and Parking System Fund, the fund balance will be maintained at an amount which represents an average of three (3) months operating expenditures. Any fund balances exceeding these amounts will be appropriately budgeted in programs experiencing the most need as determined by the Village Board.

The Liability Insurance Account will maintain a reserved fund balance equal to the actuarially determined amount required to make future payments on workers compensation and property and casualty losses. In addition, an unreserved fund balance of ten percent (10%) of total annual expenditures shall be maintained to cover additional unanticipated insurance costs or reserve requirements. The Village will establish a contingency expenditure reserve to provide for unanticipated expenditures of a non-recurring nature or to meet unexpected increases in service delivery costs.

INVESTMENT POLICY: The changes to this policy are minor *technical changes* in policy language to reflect current reporting practices. Due to the length of the Investment Policy, only the section where changes are being recommended has been shown.

OLD POLICY: Adopted December 3, 1987; Revised December 5, 1996 & December 2, 1999; Revised May 1, 2003

REPORTING: OLD POLICY

The Director of Finance shall submit a bi-monthly investment report that provides the following information:

- Principal and type of investments by Fund
- Purchase date, call date and provisions and final maturity date
- Book value
- Earnings for the current month and year to date
- Yield to maturity
- Breakdown of cash and investments
- Percentage of the Portfolio represented by each investment category

From time to time the Director of Finance shall suggest policies and improvements that might be made in the investment program.

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- Principal and type of investments
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From time to time the Director of Finance shall suggest policies and improvements that might be made in the investment program.

LAKE MICHIGAN WATER RESERVE ACCOUNT: This is a **new policy** which has been added as a result of the approval of the DuPage Water Commission to issue a rebate of funds to members. The policy indicates how the funds will be used in the FYE 2008 Village Budget and establishes a reserve to monitor future use of the remaining funds.

On April 12, 2007, the DuPage Water Commission approved a rebate to customers of approximately \$40 million of which the Village of Lombard's estimated rebate was \$2,227,998. The FYE 2008 Annual Budget anticipated the use of approximately \$188,160 from the rebate in order to eliminate any increase in the Water and Sewer operations rate and the bi-monthly service charge.

In order to monitor future utilization of the remaining portion of the rebate received by the Village, a Lake Michigan Water Reserve account has been established as an unrestricted but designated account in the Water and Sewer Fund to account for rebated funds from the DuPage Water Commission not previously utilized for rate stabilization or capital improvements. Future use of these funds for rate stabilization or capital improvements to the water and sewer system will be discussed as part of the Village's annual budget process.

MOTOR FUEL TAX POLICY: The changes to this policy are minor *technical changes* in policy language to reflect current practices for the use of Motor Fuel Tax revenue. Out-dated language has been eliminated.

OLD POLICY: Adopted December 3, 1987, Revised April 25, 1996 & May 7, 1998

The State of Illinois, Motor Fuel Tax Act, (35 ILCS 505/8), provides for a tax on fuel used for operational motor vehicles upon highways and waters. The Act also provides that the Illinois Department of Transportation shall allot to each municipality its share of the amount of tax appropriated to the municipalities in the state in proportion to their share of the total population of the state, as determined by the last census in the both the state and individual communities. Except as otherwise specified, it is the policy of the Village of Lombard, that Motor Fuel Tax allotments can be used for operational purposes (salaries, wages, overtime, materials and supplies for snow & ice control and/or street maintenance and repairs) provided that no more than 33 1/3% of the total estimated allotment will be budgeted from the MFT Fund for operational purposes in any given fiscal year. This policy does not require the expenditure of 33 1/3% of MFT allotments on operations, but rather provides that if the Village's financial position requires the use of MFT funds for operating purposes, that the amount to be used for such purposes is limited to 33 1/3%.

An amount in excess of the 33 1/3% will be allowed for MFT eligible operating expenses provided that there was an offsetting capital improvement expense funded with general Village revenue (e.g. sales tax, income tax) rather than MFT.

All operating expenses for which MFT revenue is used will be budgeted in the MFT Fund. All capital improvements using general revenue in lieu of motor fuel tax would be budgeted in the Capital Projects Fund.

The remaining MFT funds not allocated to operating expenses shall be used for capital improvements and engineering based on the Village's 10-Year Capital Improvement Program.

The actual amount of the budgeted MFT revenue devoted to operational purposes will be reviewed each year by the Village Manager, Finance Committee, and Village Board as part of the annual budget process.

REVISED POLICY:

The State of Illinois, Motor Fuel Tax Act (35 ILCS 505/8), provides for a tax on fuel used for operational motor vehicles upon highways and waters. The Act also provides that the Illinois Department of Transportation shall allot to each municipality its share of the amount of tax appropriated to the municipalities in the state in proportion to their share of the total population of the state, as determined by the last census in the both the state and individual communities. Except as otherwise specified, it is the policy of the Village of Lombard, that Motor Fuel Tax allotments can be used for operational purposes (salaries, wages, overtime, materials and supplies for snow & ice control and/or street maintenance and repairs) provided that no more than 33 1/3% of the total estimated allotment will be budgeted from the MFT Fund for operational purposes in any given fiscal year. This policy does not require the expenditure of 33 1/3% of MFT allotments on operations, but rather provides that if the Village's financial position requires the use of MFT funds for operating purposes, that the amount to be used for such purposes is limited to 33 1/3%. The remaining MFT funds not allocated to operating expenses shall be used for capital improvements and engineering based on the Village's 10-Year Capital Improvement Program.

The actual amount of the budgeted MFT revenue devoted to operational purposes will be reviewed each year by the Village Manager, Finance Committee, and Village Board as part of the annual budget process.

SALES TAX REVENUE POLICY: It is recommended that this policy be **deleted** as it does not reflect how sales tax revenue is allocated.

OLD POLICY: Adopted December 3, 1987

1. During budget preparation sessions, Village staff will make a recommendation of various revenue sources to be used to support the operating fund, liability insurance fund, and health insurance fund. Various revenue sources including sales tax will be used to support these funds.
2. Any sales tax projected over the amount needed to support these mentioned will be placed in the General Capital Projects Fund to conduct various capital improvements throughout the community.

STREET IMPROVEMENTS – DISPOSITION OF FUNDS COLLECTED PURSUANT TO THE MUNICIPAL UTILITY AND TELECOMMUNICATIONS TAX: It is recommended that this policy be **deleted**. It is superseded by the proposed **UTILITY TAX RESERVE POLICY** (Below).

OLD POLICY: Adopted May 8, 1986, Revised April 21, 1994; Revised May 1, 2003

On May 8, 1986, the Village Board of Trustees passed Ordinance #2844, which authorized the disposition of funds collected under the utility tax. That ordinance stated that any and all taxes collected under the municipal utility tax shall be used for the sole purpose of improving, maintaining, and rehabilitating portions of the public streets and appurtenances throughout the Village. On April 21, 1994, this ordinance was amended due to the elimination of the utility tax on telephones and the imposition of a municipal telecommunications tax (Ordinances #3827 & #3828). Beginning January 1, 2003, the State collects the municipal telecommunications tax and distributes it to the Village.

UTILITY TAX RESERVE POLICY: This **new policy** reflects the Board's direction regarding the allocation of Utility tax revenue not allocated for General operating purposes or for capital improvements as discussed during the FYE 2008 Budget workshops and meetings.

On March 21, 2006, Village residents approved through referendum a 1% Non-Home Rule Sales Tax. Pursuant to State law, Non-Home Rule Sales Tax may only be used for property tax relief or infrastructure improvements. The Village's commitment at the time of the referendum was to use it for the latter. As a result of utilizing Non-Home Rule Sales Tax for infrastructure purposes, the Village is in a position to re-allocate some or all of the Village's Utility and Telecommunication Tax revenue previously used for capital improvements toward meeting future operating needs. In order to monitor future utilization of the Utility and Telecommunications Tax revenue, a Utility Tax Reserve Account has been established as an unreserved but designated account in the General Fund to account for Utility and Telecommunications Tax revenue that is not designated for capital or operating purposes within a given fiscal year. The Utility Tax Reserve will be updated each year during the annual budget process based upon expenditure decisions made in previous fiscal years and updated revenue forecasts.

Staff is requesting the Finance Committee's approval of these proposed changes to the Village's Financial policies and recommendation to the Village Board of Trustees for consideration at their May 3, 2007 meeting.

c. Tim Sexton, Assistant Director of Finance