Financial Policies
Fund Balance & Reserve Policy for General Fund and Street Operations, Special Reserves and Utility Funds

☐ ADOPTED BY COUNCIL: AUGUST 8, 2022	EFFECTIVE DATE: AUGUST 8, 2022

I. PURPOSE

Fund balance is an approximate measure of liquidity. Fund balance/reserves are a cornerstone of financial flexibility and provide the City of Sequim with options to respond to unexpected issues and provide a buffer against fiscal challenges. It is the intent of the City to provide a stable financial environment for which its citizens can depend on a consistent and quality level of service and for planned future expenditures. The Finance Director is responsible for monitoring reserve levels and reporting current and projected reserves during each budget development cycle. The purpose of this policy is to establish an understanding of the proper level and use of those reserves for the City of Sequim.

Adequate levels of fund balance or reserves are essential to protect against temporary revenue shortfalls and helps to ensure stable taxes and fees. It provides resources criteria crucial in long-term financial planning. The value of strong fund balances and reserves needs to be balanced with pressures from unions, taxpayers and citizens' groups, which may view high levels of fund balance as "excessive."

For the City of Sequim, fund balance equals cash (which includes cash and investments held by the City) as the city reports and budgets financial activity on a cash basis.

The City of Sequim follows BARS (the Budgeting, Accounting and Reporting System) promulgated by the State of Washington which includes the prescribed uniform charts of accounts, accounting and budgeting policies, guidance for preparing financial statements and instructions for preparing supplemental year end schedules (Revised Code of Washington Section 43.09.230) for local governments.

Fund Balance and Cash and/or Investments is defined in the BARS Manual as follows:

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3082100 NONSPENDABLE

The amount of cash and investments that, according to laws or contract, cannot be spent (required to remain intact). This category applies to items like permanent endowments when the donor stipulates that the principal amount of the contribution must be preserved and invested and only the earnings can be used for governmental purposes.

3083100 RESTRICTED

The amount of cash and investments that is subject to externally enforceable legal restrictions (imposed by creditors, grantors, donors, other governments, most voter approved levies, etc.) The restrictions may also be imposed by law through constitutional

provisions or enabling legislation. For example, any unspent taxes or other collections restricted by RCW for a specific purpose (e.g., hotel/motel tax, public safety tax, retainage collected or withheld, unspent bond proceeds, etc.).

3084100 COMMITTED
The amount of cash and investments that is constrained by specific limitations that the government imposes upon itself at the highest level of decision making (normally the governing body) through the most binding formal action (e.g., resolution, ordinance, etc.) and that remains binding unless removed in the same manner. A motion, plan or stated management intent regarding how resources will be used does **not** meet criteria for classifying balances as committed because the commitment has to occur at the highest level of authority through the most binding formal action.

3085100 ASSIGNED
The amount of cash and investments that reflects a government's intended use of resources. These are amounts intended to be used by the government for specific purposes that are neither restricted nor committed. Intent can be expressed in one of two ways:

- The governing body can state its intent to use resources for a specific purpose. The intent would be expressed in an informal way such as a motion or other form of a directive.
- The governing body can delegate authority to others (e.g., finance or executive director, chief, head of a department, manager, etc.) to express intent to use amounts for specific purposes.

Any transfer of resources to funds other than the general fund represents an assignment since the transfer represents the intent for those resources to be used for a specific purpose. The creation of a fund outside of the general fund is considered at least assigned, since the creation of a fund automatically sets aside the monies for a purpose.

3089100 UNASSIGNED
The amount of cash and investments that are remaining after classifying amounts as nonspendable, restricted, committed or assigned. Unassigned amounts are technically available for any purpose. The General Fund is the only fund that can have a positive unassigned cash and investment balance since all other funds represent a specific purpose for their resources.

The City of Sequim has the following fund structure:

General Fund and Streets Unrestricted Fund (funds available for general government operations).

Equipment Reserve (funds set aside and available for General Government equipment replacement)
Long term General Obligation Debt:
Capital Funds
Facilities (funds set aside for City Hall and other facility related capital projects)

Enterprise Funds
Water Unrestricted (Water Operations)
Water Restricted (Water Capital, Debt Service and Equipment Replacement)
Sewer Unrestricted (Sewer Operations)
Sewer Restricted (Sewer Capital, Debt Service and Equipment Replacement)

Special Revenue Funds (restricted by law or City Ordinances, no targeted reserves)
Stormwater Operations, Project Stormwater, Street Restricted, Affordable Housing Tax, Lodging Tax Hotel / Motel, Criminal Justice, Police Restricted, Police Asset Seizure, Parks Restricted, Real Estate Excise Tax, Gifting & Donations and
Rainy-Day Fund (This Rainy Day fund will be replenished from one-time revenues not committed for other purposes, excess operating reserves or by budgetary action. No reserve level is established.)

Trust, Agency & Permanent Funds (funds not available for City services)
Police Expendable Trust, Intergovernmental Agency Fund
Haller Park Fund Permanent

City Targeted Reserve Funds: The City uses the following classifications:

1. **Minimum Fund Balance Reserves:** Provides a financial cushion for revenue fluctuations and cyclical activity through General Operations.

a) Targeted Fund Balance

	Min	Max
General Fund and Streets	15% ongoing revenues	20% ongoing revenues
Water Unrestricted	3 months operating expenditures	5 months operating expenditures
Sewer Unrestricted	3 months operating expenditures	5 months operating expenditures

2. **Economic Uncertainty Reserves**: Provides a financial cushion against unanticipated adverse financial or economic circumstances, emergencies, or litigation.

a) Targeted Reserve: The maximum fund balance should take into consideration level of volatile revenues, such as Development related revenues (Building Permits, Inspections, Plan Check Fees, other Development Fees) and Sales Tax.

	Min	Max
General Fund and Streets	1% ongoing revenues	3% ongoing revenues
Water Unrestricted	1% ongoing revenues	3% ongoing revenues
Sewer Unrestricted	1% ongoing revenues	3% ongoing revenues

3. **Future Liabilities Reserves**: These amounts are set aside for a specified purpose, related to an accrued obligation or to self-insure for a future obligation. This should include reserves for unemployment self-insurance or a portion of accrued compensation (paid time off and sick leave) that is paid to an employee upon separation from employment.

a) Targeted Reserve: The amount necessary to mitigate a specific future expense is based on a historical pattern or other appropriate measure. Unemployment could be based on +/- 10% of the estimated annual payment to the state, or 1% of wages, or other appropriate measure. Accrued compensation is based on historical pattern or other appropriate measure.

	Min	Max
General Fund and Streets	1% ongoing revenues	3% ongoing revenues
Water Unrestricted	1% ongoing revenues	3% ongoing revenues
Sewer Unrestricted	1% ongoing revenues	3% ongoing revenues

4. **Facilities and Equipment Reserve Funds:** Established to purchase, replace or refurbish City facilities and operating equipment such as computers, copiers, operating equipment and vehicles (see Capital Improvement Plan policy).

a) Targeted Reserve Fund Balance: Maintained at a level sufficient to meet scheduled equipment replacement so as to sustain an acceptable level of services. (Targeted reserve calculations can exclude those projects that are grant or loan funded.)

	Min	Max
Equipment Replacement (General Government)	2.5 years scheduled replacement	6 years scheduled replacement
City Facilities	2.5 years scheduled replacement	6 years scheduled replacement
Water Restricted	2.5 years scheduled replacement	6 years scheduled replacement
Sewer Restricted	2.5 years scheduled replacement	6 years scheduled replacement

II. PROCEDURES

1. Ongoing Revenues and Operating Expenditures: Reflects the ongoing operations and excludes one-time, nonrecurring and capital items. (See Budget Development Policy.)

2. Addition to Fund Balance/Reserves: Typically provided by surplus from prior years, one-time revenues and revenues in excess of operating expenditures.

3. Replenishment of Fund Balance/Reserves: Where a deficit causes a fund balance to be reduced, contributions will be made over a three to five year period until targeted level is attained using one-time revenues first and surplus next.

4. Minimum Fund Balance: Replenishing the fund balance to the minimum level will be the first priority use of excess year-end resources.

5. Budgeted Fund Balance and Targeted Reserves: All reserves will be presented in the budget and will be compared to the adopted financial policy. If the resulting targeted reserves fall below policy a plan will be presented to bring the fund balance into compliance.

6. Periodic Reporting: The Finance Department will provide the City Council with periodic reports (quarterly) regarding fund balance and targeted reserves, according to policy.