MEMORANDUM

TO: Board of Trustees

THROUGH: Indra S. Winquest
District General Manager

FROM: Paul Navazio
Director of Finance

SUBJECT: Review, discuss and provide feedback on potential revisions to selected Board Policies and Practices

DATE: April 29, 2021

I. RECOMMENDATION

Staff recommends that the Board of Trustees review, discuss and provide feedback on potential revisions to selected Board Policies and Practices, including:

1) Capitalization Policy – (Board Policies 8.10 and 9.10, and Board Practice 2.9.0)
2) Capital Planning / Capital Budgeting/Capital Expenditures – (Board Policies 12.1.0 and 13.1.0, and Board Practice 13.2.0)
3) Fund Balance Policy – (Board Policy 7.1.0 and Board Practice 7.2.0)
4) Working Capital Policy – (Board Policy 19.1.0 and Board Practice 19.2.0)
5) Central Services Overhead – (Board Policy 18.1.0 and Board Practice 18.2.0)

II. BACKGROUND

The Board of Trustees and General Manager have identified the need to update Board policies, procedures and practices as a priority initiative. Specific policies have been identified by the Board of Trustees, third-party review of District policies and practices, management's review of internal controls and, most recently, during recent Board budget workshops.

Staff has initiated a review of Board policies and practices, as well as internal Accounting and Financial Procedures that have a direct impact in the development of the FY2021/2022 budget, including update to the District's Five-Year Capital

Improvement Plan. This review includes areas highlighted during the series of Board Budget Workshops as well as third-party review of selected accounting and financial reporting practices.

At their meeting of March 10, 2021, the Board authorized the re-allocation of up to $40,000 in available General Fund appropriations to support the review and update of selected Board Policies and Procedures, specifically to support engagement of outside consultant(s) to assist in this process.

At that time, Staff identified the priority areas for review of selected Board Policies and Practices with a focus on those policies/practices with direct implications for staff's work in the development of the FY2021/22 annual budget, as follows:

- Policy 6.1.0 Adoption of Financial Practices
  - Staff Lead with Board of Trustees input (6.1.2.1 -Revenues/Pricing Policies)

- Policy 7.1.0/Practice 7.2.0 - Fund Balance
  Policy 19.1.0 / Practice 19.2.0 – Working Capital
  - Solicit assistance from Government Finance Officers' Association (GFOA);
  - Incorporate input from on-going Raftelis review regarding Utility operations

- Policies 8.1.0, 9.1.0/ Board Practice 2.9.0 - Capitalization Thresholds/Useful Life of Capital Assets; Policies 12.1.0 and 13.1.0 – Capital Project Planning and Capital Budgeting
  - Solicit Assistance from Moss Adams, LLP to provide "best practices", identify areas for revision and propose updated policy language.
  - Review with District's newly-designated Independent Auditor
- Policies 18.1.0,. Practice 18.2.0 – Central Services Cost Allocation
  - Staff Lead with assistance from District's newly-designated Independent Auditor

Also at the Board of Trustees meeting on March 10, 2021, Trustee Tonking was identified, as Board Treasurer, to serve as Board liaison to this effort.

III. DISCUSSION

This memo is intended to provide the Board of Trustees with a preliminary assessment of selected, current Board Policies and Practices in relation to best practices, and identifies potential areas for updates and revisions.

Based on Board of Trustees feedback as well as additional consultation with outside consultants as well as the District's newly-designated Independent Auditor, formal revisions to the referenced Board Policies and Practices are anticipated to be brought back to the Board of Trustees for formal approval as early as May 26, 2021 (concurrent with budget adoption), but no later than June 21, 2021 (prior to the start of the new fiscal year on July 1, 2021).

IV. FISCAL ANALYSIS

There is no direct fiscal impact from the recommendations contained in this memorandum.

Staff is developing a set of recommendation for Board consideration in conjunction with the FY2021/2022 budget process, utilizing existing funding (up to $40,000 from the General Fund) authorized by the Board for this purpose. Any unused funding at the end of the fiscal year are anticipated to be re-appropriated for possible use during FY2021/22 for ongoing review and update of Board Policies and Practices.

Attachments:

I - Capitalization Policy
- Background / Preliminary Recommendations (DRAFT)
- Board Policy 8.1.0 and 9.1.0
- Board Practice 2.9.0
- Best Practices / Guidelines

II - Capital Planning / Capital Budgeting / Capital Expenditures
- Background / Preliminary Recommendations (DRAFT)
- Board Policy 12.1.0 and 13.1.0
- Board Practice 13.2.0
- Best Practices / Guidelines

III - Fund Balance / Working Capital Policy
- Background / Preliminary Recommendations (DRAFT)
- Board Policy 7.1.0 and 19.1.0
- Board Practice 7.2.0 and 19.2.0
- Best Practices / Guidelines

IV - Central Services Overhead Policy

- Background / Preliminary Recommendations (DRAFT)
- Board Policy 18.1.0
- Board Practice 18.2.0
- Best Practices / Guidelines

I - Capitalization Policy

- Background / Preliminary Recommendations (DRAFT)
- Board Policy 8.1.0 and 9.1.0
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CAPITALIZATION POLICY
Board Policy 8.1.0
Board Policy 9.1.0
Board Practice 2.9.0

Background:

- Board Policy 8.1.0 relates to "Establishing Estimated Useful Life of Capital Assets
- Board Policy 9.1.0 relates to Appropriate Capitalization Threshold for Capital Assets
- Board Practice 2.9.0 relates to Capitalization of Fixed Assets
    - Capitalization Threshold: Equipment = $ 5,000
      Structures / Improvements = $10,000
    - Useful Life 3+ years (All assets categories)

Best Practices and Resources:

- GFOA provides guidance on best practices for development of policies related to Capitalization Thresholds as well as Estimating Useful Life of Capital Assets
- Moss Adams, LLP Identified several observations and recommendations related to capital asset accounting in their report, "Evaluation of Certain Accounting and Reporting Matters," dated January 14, 2021, to include:
    - District's policies and practices should be revised to acknowledge different stages to a project, definition of costs incurred in each stage, consistent with established and accepted governmental accounting practices.
    - The District should expense expenditures for feasibility studies and master plans. Policies should be revised to address the few circumstances where preliminary engineering, architectural, or design costs are actually utilized in a capital project and eligible for capitalization.
    - Board policies and practices should be revised to provide for capitalization of expenditures that truly increase service capacity, and further, that provide the criteria to be followed in making the increased service capacity decision on expenditures by nature or function of the different asset types versus expenditures that should be expensed.
- Staff has reviewed sample Capitalization Policies provided by consultants, the District's Independent Auditor and comparable public agencies.

CAPITALIZATION POLICY

Preliminary Recommendations:

1) It is recommended that Board Policies 8.1.0 and 9.1.0 be consolidated into a single, comprehensive Capitalization Policy to include direction related to:
    a. Capitalization Thresholds
    b. Estimated Useful Life of capital assets
    c. Definition of capital expense to be capitalized versus repair and maintenance costs to be expensed in period incurred
    d. Distinction of costs incurred at various phases of capital project life-cycle to inform expensing of costs incurred prior to establishment of formal project definition, scope and financing plan. *(Cross-reference to Board Policy 13.1.0 and Board Practice 13.2.0)*

2) Board Practice 2.9.0 should be updated to reflect:
    a. Updated numbering sequence (previously Practice 9.2.0)
    b. Specific Capitalization Thresholds for ALL asset types
    c. Default Estimated Useful Life for All asset types
    d. Application of distinction between capital costs to be capitalized and repairs and maintenance costs to be expensed
    e. Definition of pre-planning costs to be expensed versus capitalized

3) The updated capitalization policy will also need to reflect implementation of GASB 87, related to leases, which are required – as of 7/1/21 - to be reported as "intangible assets" and depreciated of the remaining lease term(s).

CAPITALIZATION POLICY
(Sample)

Policy Overview

Capital assets include land, improvements to land, water rights, easements, buildings, building improvements, vehicles, machinery, equipment, infrastructure, construction in process (CIP), and all other tangible or intangible assets that are used in operations, that have initial useful lives extending beyond one year and meets the capitalization threshold.

The District classifies capital assets in the following groups for financial reporting:

- Land
- Buildings and structures
- Venue Improvements
- Service Infrastructure
- Equipment and Vehicles
- Construction in progress

The District's capitalization threshold shall be as follows:

ASSET CLASS	CAPITALIZATION THRESHOLD
Land	All
Building and Structures	~~$ 10,000~~ $ 25,000
Venue Improvements	~~$ 10,000~~ $ 10,000
Service Infrastructure	~~$ 10,000~~ $ 25,000
Equipment and Vehicles	~~$ 5,000~~ $ 10,000

Capital assets purchased by the District are recorded at cost. Capital assets donated to the District are recorded at fair value on the date accepted.

Items should only be capitalized if they have an estimated useful life of ~~greater than two~~ <u>three</u> years of more.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

ASSET CLASS	YEARS
Buildings and Structures	10-40
Venue Improvements	10-25
Service Infrastructure	5-40
Equipment and Vehicles	3-20

Capital projects will be capitalized if they meet one of the following criteria:

- The project is creating a new asset for the District
- The project significantly extends the useful life of an asset beyond what was originally established as the estimated useful life for that asset and/or significantly increases the service capacity of the asset.

Improvements, replacement and major repairs of all capital assets, which were approved on the basis that the alterations or repairs achieve greater future benefits such as improving efficiency or materially extending the useful life of the asset should be capitalized. Expenditures that simply maintain a given level of service should be expensed.

Three major categories of costs subsequent to original construction or acquisition are incurred relative to capital assets:

- Improvements - an improvement is the substitution of a better component for which possesses superior performance capabilities, whereas a replacement is the substitution of a similar component.
- Replacement – a replacement, which is a substitution of a component of the asset with one of similar quality is to be expensed. On rare occasions, a replacement can be considered improvements and be capitalized if it meets certain established criteria.
- Maintenance - certain activities budget as capital projects will be expensed as repair and maintenance expenses if they meet one of the following criteria:
    - The activity is performed on a regular and recurring basis to keep the District's assets in their normal operating condition over the course of the originally-established useful life.
    - The project represents a repair activity that restores an asset to its original condition.

Capital Project Planning

Major capital projects, as defined in Board Policy 12.1.0, will often (but not always) be managed through the application of distinct project phases. These may include:

- Project Definition
- Planning
- Feasibility
- Design
- Construction

Costs incurred in pre-planning phases, including Master Plans and Project Feasibility Studies that explore potential capital projects should be expensed. Once a master-planning site-specific feasibility study results in a defined project, with a specific scope and cost, and the Board determines that a financing plan is to be developed for inclusion in the District's Capital Improvement Budget, costs associated with the capital project are to be capitalized.

To facilitate the tracking of capital project costs to be expensed versus capitalized, the District will consider establishing separate capital project codes to distinguish between phases where costs will be expensed and those capital project phases where costs are to be capitalized.

Capital project costs to be capitalized will be reported as Construction In Progress until the capital project is completed and the capital asset is placed into service.

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT – ONE TEAM

Accounting, Auditing and Financial Reporting
Establishing the Estimated Useful Lives of Capital Assets
Policy 8.1.0

POLICY. The best source of relevant information on the estimated useful lives of the District's capital assets comes from its own past experience with similar assets. In situations where the documentation of the District's own past experience, for a given type of capital asset, is not adequate for this purpose, the District will consider the experience of other governments, professionally determined specifications, and private-sector enterprises. The District will make whatever adjustments are needed to estimated useful lives that were obtained from others to ensure that such estimates are appropriate to its own particular circumstances. It is especially important to consider the potential effect of each of the following factors when depending on the experience of others:

1.0 **Quality**. Similar assets may differ substantially in quality, and hence in their useful lives, because of differences in materials, design and workmanship.

2.0 **Application**. The useful life of a given type of capital asset may vary significantly depending upon its intended use.

3.0 **Environment.** Environmental conditions in the Tahoe Basin include climate and regulatory sources. Conditions can be defined by the Tahoe Regional Planning Agency, the United States Forest Service Basin Management Unit and the North Lake Tahoe Fire Protection District. The service life of some capital assets used in connection with highly regulated activities could be affected by these agencies codes or best management practices.

4.0 **Life Cycle Considerations**. The vast majority of the District's capital assets are used in conjunction with programming activities. Useful lives reflect the amount of utilization that will be consumed by an operating period and could affect the care and condition needed for services rendered by those venues. The District should also consider the possibility of varying useful lives for components of larger assets, both for capitalization and to reflect the appropriate life cycle maintenance interval for such components.

Accounting, Auditing and Financial Reporting
Establishing the Estimated Useful Lives of Capital Assets
Policy 8.1.0

5.0 Maintenance. The potential effect of each of the factors just described may be mitigated or exacerbated as a consequence of the District's evaluation of capital asset care and condition, as well as the approach to maintenance and replacement policy. Once established, estimated useful lives for major categories of capital assets should be periodically compared with the District's actual experience and appropriate adjustments should be made to reflect this experience.

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Accounting, Auditing and Financial Reporting
Establishing Appropriate Capitalization Threshold for Capital Assets
Policy 9.1.0

POLICY. The District will consider the following guidelines in establishing capitalization thresholds:

1.0 Potentially capitalizable items should only be capitalized if they have an estimated useful life of greater than two years following the date of acquisition or placed into service.

2.0 Capitalization thresholds are best applied to individual items rather than to groups of similar items (e.g., desks and tables), unless the effect of doing so would be to eliminate a significant portion of total capital assets.

3.0 In no case will the District establish a capitalization threshold of less than $5,000 for any individual item.

4.0 In establishing capitalization thresholds, when the District is a recipient of federal awards, then federal requirements that prevent the use of capitalization thresholds in excess of certain specified maximum amounts for purposes of federal reimbursement will prevail.

5.0 Capitalization of buildings and infrastructure should consider the use of componentization as a way to reflect the varying life cycle considerations of mechanical, structural elements, and wear items that may require different cycles of maintenance and replacement from the main asset being capitalized. The significance of such componentization takes precedent over the $5,000 threshold, and thus smaller amounts may be listed to facilitate proper asset management.

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Accounting, Auditing and Financial Reporting
Capitalization of Fixed Assets
Practice 2.9.0

RELEVANT POLICIES: 8.1.0 Establishing the Estimated Useful Lives of Capital Assets and 9.1.0 Establishing Appropriate Capitalization Threshold for Capital Assets

1.0 ACCOUNTING CONTROL

The capitalization threshold for all asset classes shall be identified during the budget process each fiscal year by the Finance and Accounting staff and approved by the Board of Trustees as part of the adoption of the annual Debt Management Policy, including the Five Year Capital Improvement Plan and its statement on Minimum level of expenditure.

1.1 The capitalization threshold per item shall be:

ASSET CLASS	MINIMUM COST
Equipment	$ 5,000.00
Structures and Land Improvements	$10,000.00

1.2 In addition to cost, all of the following criteria shall also be used:

1.2.1 The normal useful life of the item is three or more years.

1.2.2 The item has an acquisition cost (including freight and installation) of at least the amounts listed above in each asset class.

1.2.3 The item will not be substantially reduced in value by immediate use.

1.2.4 In case of repair or refurbishment that will be capitalized, the outlay will substantially prolong the life on an existing fixed asset or increase its productivity significantly, rather than merely returning the asset to a functioning unit or making repairs of a routine nature.

1.2.5 The capitalization threshold is applied to individual items rather than to groups of similar items (e.g. desks and tables).

1.2.6 The utilization of componentization of assets under the project, to provide a more appropriate management of an assets care, condition and associate maintenance or replacement, takes precedent over the stated thresholds under section 1.1.

2.0 PHYSICAL CONTROL

All fixed assets acquired either as operating or capital expenditures will be identified as IVGID property and recorded. Such items represent a value to the operations that have an ongoing usefulness to justify safeguarding them from loss or abuse. The items should be expected to be in service at least two years and can be readily assigned to a function or activity as responsible for its care and condition.

BEST PRACTICES

Capitalization Thresholds for Capital Assets

State and local governments should adhere to appropriate guidelines for capitalization thresholds.

The term capital assets is used to describe assets that are used in operations and that have initial lives extending beyond a single reporting period. Capital assets may be either intangible (e.g., easements, water rights, licenses, leases) or tangible (e.g., land, buildings, building improvements, vehicles, machinery, equipment and infrastructure).

As a practical application of the materiality principle, not all tangible capital-type items with useful lives extending beyond a single reporting period are required to be reported in a government's statement of net position. Items with extremely short useful lives (e.g., less than 2 years) and/or of small monetary value are properly reported as an "expense" or "expenditure" in the period in which they are acquired.

When outlays for capital-type items are, in fact, reported on the statement of net position, they are said to be capitalized. The monetary criterion used to determine whether a given capital asset should be reported on the statement of net position is known as the capitalization threshold. A government may establish a single capitalization threshold for all of its capital assets, or it may establish different capitalization thresholds for different classes of capital assets. In selecting capitalization thresholds, governments should be able to report and depreciate substantially all capital asset value while eliminating the cost of tracking a large number of small-value items.

A government's threshold for capitalization does not need to be calculated in the same way that the government would measure the asset, if it is ultimately capitalized, for reporting in accordance with GAAP. For example, a government's capitalization policy may be to determine whether improvements to an office building (primarily plumbing and electrical upgrades) meet a dollar threshold ($20,000) before including the cost of new window and floor treatments, which will be part of the improvements, because it does not consider those to be "core costs" of the asset improvement. For assets constructed by a government's own employees, the dollar threshold might distinguish between direct costs (time spent by construction workers, architects and engineers on that project) and indirect costs (allocated costs of the capital improvements department of public works).1

The capitalization threshold should not be the only factor used when determining if an item should be capitalized. A government should be cognizant of whether similar items are capitalized in order to be consistent in reporting. For example, assume a government, with a capitalization threshold of $10,000, purchases two pieces of similar equipment. Item A was purchased three years ago for $11,000, and item B was purchased in the current year for $9,000. The government also incurred its own direct costs (time spent by construction workers, architects and engineers on that project) and indirect costs (allocated costs of the capital improvements department of public works) for both items, which increased the values of the items to $13,000 for item A, and $11,000 for item B. Without the inclusion of the government's own costs, item B would not have been capitalized, while other similar items would be capitalized because they were purchased at a higher price. In this case, the government may choose to capitalize item B for the sake of consistent treatment.

Capitalization is, of its nature, primarily a financial reporting matter. That is, a government's principal concern in establishing specific capitalization thresholds ought to be the anticipated information needs of the users of the government's external financial reports. While it is essential to maintain control over all potentially capitalizable items, there are more efficient means than capitalization for accomplishing this objective in the case of a government's smaller tangible capital-type items. Furthermore, practice has demonstrated that capital asset management systems that attempt to incorporate data on numerous smaller items are often costly and difficult to maintain and operate.

Recommendation:

GFOA recommends that state and local governments adhere to the following guidelines for capitalization thresholds:

- Establish minimum cost and useful-life based thresholds to avoid the cost of capitalizing immaterial items;
- Establish a minimum capitalization threshold of $5,000 for any individual item;
- Establish a minimum capitalization threshold of at least a two-year useful life for any individual item;
- Consider establishing different dollar capitalization thresholds for different classes of capital assets (i.e. land, infrastructure, buildings and improvements, and equipment);
- Capitalization thresholds are best applied to individual items rather than to groups of similar items (e.g., desks and tables), unless the effect of doing so would be

to eliminate a significant portion of total capital assets (e.g., books of a library district);

- Governments should perform a periodic review of their capitalization thresholds;
- In establishing capitalization thresholds, governments that are recipients of federal awards should be aware of federal capitalization thresholds requirements; and
- Governments should exercise control over potentially capitalizable items that fall under the operative capitalization threshold but require special attention.

1) Note that while indirect costs pertaining only to capital projects should be capitalized, general overhead costs such as human resources services or the commissioner's office staff of an agency not exclusively performing capital work should not be allocated to capital projects and capitalized. [Accounting for Capital Assets, A Guide for State and Local Governments, Stephen J. Gauthier, GFOA, 2008].

This best practice was previously titled Establishing Capitalization Thresholds for Capital Assets.

Estimated Useful Lives of Capital Assets

PRIMER

Generally accepted accounting principles (GAAP) require, in most cases, that capital assets be depreciated. Depreciation is the systematic and rational allocation of the historical cost of a capital asset over its useful life. The estimated useful life assigned to a capital asset will directly affect the amount of depreciation expense reported each period in an accrual-based operating statement. Therefore, it is important to the quality of financial reporting that governments establish reasonable estimates of the useful lives of all of their depreciable capital assets.

The best source of relevant information on the estimated useful lives of a government's capital assets normally is its own past experience with similar assets. In situations where the documentation of a government's own past experience for a given type of capital asset is not adequate for this purpose, a government should profit as much as possible from the experience of other governments, private-sector enterprises, and applicable engineering professional standards and guidelines from other associations. At the same time, a government should make whatever adjustments are needed to estimated useful lives that were obtained from others to ensure that such estimates are appropriate to its own particular circumstances. It is especially important that a government consider the potential effect of each of the following factors when depending on the experience of others:

- Quality. Similar assets may differ substantially in quality, and hence in their useful lives, because of differences in materials, design and workmanship. For example, an asphalt road will not have the same useful life as a concrete road. Likewise, the depth of the material used for paving purposes, as well as the quality of the underlying base, will also affect the useful life of a road;
- Application. The useful life of a given type of capital asset may vary significantly depending upon its intended use. For example, a residential street may be expected to have a longer useful life than a major arterial thoroughfare because of differences in the type and volume of traffic; and
- Environment. Environmental differences among governments can have an important impact on the useful lives of their respective capital assets. For instance, the useful life of a road in a climate subject to extremes in temperature is likely to be different from that of a similar road located in a more temperate climate. Also, regulatory obsolescence may shorten the service life of some capital assets used in connection with highly regulated activities (e.g., utilities).

The potential effect of each of the factors just described may be mitigated or exacerbated as a consequence of a government's maintenance and replacement policy. For example, the potential for road damage is increased in a cold environment when cracks are not promptly repaired, because water settling in the cracks will expand and contract, thereby accelerating the initial deterioration represented by the crack itself.

Once established, estimated useful lives for major categories of capital assets should be periodically compared with a government's actual experience and appropriate adjustments should be made to reflect this experience. Useful lives of capital assets should also be adjusted when circumstances warrant a change. In addition to capital asset impairments, other factors may trigger a government to consider the need to change an asset's estimated useful life. For example, the breakdown of a vehicle may trigger a government to change the useful life of similar vehicles. If the intended use of an asset changes, the useful life may also have to be adjusted. For example, if a vehicle used by the water department for water meter readings starts to be used for hauling heavy materials for the public works department, its estimated useful life should be reconsidered and possibly shortened.

Depreciation is a financial reporting concept. Therefore, all of the considerations just discussed are only of concern to the extent that they could have a material impact on a government's financial statements.

II - Capital Planning / Capital Budgeting / Capital Expenditures

- Background / Preliminary Recommendations (DRAFT)
- Board Policy 12.1.0 and 13.1.0
- Board Practice 13.2.0
- Best Practices / Guidelines

CAPITAL PLANNING, CAPITAL BUDGETING and CAPITAL EXPENDITURES

Board Policy 12.1.0
Board Policy 13.1.0
Board Practice 13.2.0

Background:

- Board Policy 12.1.0 relates to "Multi-Year Capital Planning"
- Board Policy 13.1.0 relates to "Capital Project Budgeting"
- Board Practice 13.2.0 relates to "Capital Expenditures

Best Practices and Resources:

- GFOA provides guidance on best practices for development of Capital Planning policies and Capital Budget Presentation
- Moss Adams, LLP Identified several observations and recommendations related to capital planning, and capital budgeting in their report, "Construction Advisory Fact Validation Report", December 21, 2020, to include:
  - Implement and finalize policies and procedures defining processes for master planning, reporting, scope definitions and prioritization, and communication efforts.
  - Implement policy and procedures for the competitive solicitation of professional services
  - Continue development of ongoing project-level budget-to-actual expenditure reporting

Preliminary Recommendations

(Subject to review and recommendations from outside consultant)

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT – ONE TEAM

Capital Planning
Multi-Year Capital Planning
Policy 12.1.0

POLICY. The District will prepare and adopt comprehensive multi-year capital plans to ensure effective management of capital assets. A prudent multi-year capital plan identifies and prioritizes expected needs based on a community's strategic plan, establishes project scope and cost, details estimated amounts of funding from various sources, and projects future operating and maintenance costs. The capital plan should cover a period of at least five years, preferably ten or more.

1.0 Identify needs. The first step in the District's capital planning is identifying needs. The District has a commitment to the maintenance of its existing infrastructure. The District's Multi-Year Capital Plan will use information including development projections, strategic plans, comprehensive plans, facility master plans, regional plans, and citizen input processes to identify present and future service needs that require capital infrastructure or equipment. In this process, attention will be given to:

1.1 Capital assets that require repair, maintenance, or replacement that, if not addressed, will result in higher costs in future years.
1.2 Infrastructure improvements needed to support new development or redevelopment.
1.3 Projects with revenue-generating potential.
1.4 Improvements that support economic development.
1.5 Changes in policy or community needs.

2.0 Determine costs. The full extent of project costs should be determined when developing the multi-year capital plan. Cost issues to consider include the following:

2.1 The scope and timing of a planned project should be well defined in the early stages of the planning process.
2.2 The District should identify and use the most appropriate approaches, including outside assistance, when estimating project costs and potential revenues.

2.3 For projects programmed beyond the first year of the plan, the District should consider cost projections based on anticipated inflation.

2.4 The ongoing operating costs associated with each project should be quantified, and the sources of funding for those costs should be identified.

2.5 A clear estimate of all major components required to implement a project should be outlined, including land acquisition needs, pre-design, design, and construction or acquisition, contingency and post-construction costs.

2.6 Recognize the non-financial impacts of the project (e.g., environmental) on the community.

3.0 Prioritize capital requests. The District continually faces extensive capital needs and limited financial resources. Therefore, prioritizing capital project requests is a critical step in the capital plan preparation process. When evaluating projects the District will:

3.1 Categorize each submittal under Project Types:

3.1.1 Major Projects

- A non-recurring project with scope and management complexity with a project budget greater than $1,000,000 and a 25-year minimum asset life.

3.1.1.1 New Initiatives

- A project that creates a new amenity or significantly expands an existing facility with new programming, operations or capacities.

3.1.1.2 Existing Facilities

- A project that maintains, renews, and re-invests in existing facilities without significantly adding new programming, operations or capacities.

3.1.2 Capital Improvement

– A non-recurring project with some scope and management complexity with a project budget generally less than $1,000,000.

3.1.2.1 New Initiatives

3.1.2.2 Existing Facilities

3.1.3 Capital Maintenance

– A generally recurring project at an existing facility with limited scope and management complexity and a project budget less than $1,000,000.

3.1.4 Rolling Stock

– On-going projects for the replacement of vehicles, heavy and light duty wheeled and tracked machinery, tractors, mowers, trailers, etc.

3.1.5 Equipment & Software

– On-going replacement of non-rolling stock and non-building system equipment (kitchen, ski rental, uniforms, furniture, serviceware, etc.), information technology hardware and software.

3.2 Prioritize Projects under these criteria:

3.2.1 Priority 1 are projects that address Existing Facilities or replace existing assets via Capital Maintenance, Rolling Stock, or Equipment & Software projects that have reached or are near the end of useful life and are necessary to meet existing programming, operations, or capacities that the community wants, needs and uses.

3.2.2 Priority 2 are New Initiative projects that address existing facilities and assets that have reached or are near the end of useful life in order to expand existing programming, operations, or capacities to meet the community's wants, needs and uses.

3.2.3 Priority 3 are New Initiative projects that create new amenities that are wanted by the community and will be funded by new sources.

3.2.4 Priority 4 are New Initiative projects that create new amenities that are wanted by the community and will be funded by existing sources.

3.3 Ongoing consideration of Project Types and Prioritization by District Staff will consider:

3.3.1 Reflect the relationship of project submittals to financial and governing policies, plans, and studies.

3.3.2 Allow venues to provide a prioritization recommendation.

3.3.3 Incorporate input and participation from major stakeholders and the general public.

3.3.4 The condition assessment of existing assets as it relates to asset life-cycle, industry best practices, manufacturer's guidelines, safety, and the aesthetic character of the facility.

3.3.5 Adhere to legal and regulatory requirements and/or mandates.

3.3.6 Anticipate the operations and operating budget impacts resulting from capital projects.

3.3.7 Apply analytical techniques, as appropriate, for evaluating potential projects (e.g., return on service, payback period, cost-benefit analysis, cash flow modeling).

3.3.8 Re-evaluate capital projects approved in previous multi-year capital plans.

3.3.9 The availability of outside funding (e.g. grants, direct community contribution, in-kind contribution, public private partnership) to support completion of a capital project.

4.0 Develop financing strategies. The District recognizes the importance of establishing a viable financing approach for supporting the multi-year capital plan. Financing strategies should align with expected project requirements while sustaining the financial health of the District. The capital financing plan should:

4.1 Anticipate expected revenue and expenditure trends, including their relationship to multi-year financial plans.
4.2 Prepare a flow of resources projection of the amount and timing of the capital financing and expenditure
4.3 Continue compliance with all established financial policies.
4.4 Recognize appropriate legal constraints.
4.5 Consider and estimate funding amounts from all appropriate funding alternatives.
4.6 Ensure reliability and stability of identified funding sources.
4.7 Evaluate the affordability of the financing strategy, including the impact on debt ratios, taxpayers, ratepayers, and others.

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT ~ ONE TEAM

Capital Planning
Capital Project Budgeting
Policy 13.1.0

POLICY. The District will prepare and adopt a formal capital budget as part of their annual budget process. The capital budget will be directly linked to, and flow from, the Multi-Year Capital Improvement Plan. It may be necessary to modify projects approved in the capital plan before adopting them in a capital budget. Modifications may be necessary based on changes in project scope, funding requirements, or other issues. If these modifications are material, the District will consider the impacts these may have on its multi-year capital and financial plans. The capital budget should be adopted by formal action of the Board of Trustees, either as a component of the operating budget or as a separate capital budget. It will comply with all state and local legal requirements.

1.0 Preparing and Adopting the Capital Budget. The capital budget will include the following information:

1.1 A definition of capital expenditure for the District.
1.2 Summary information of capital projects by fund, function, venue/service or activity.
1.3 A schedule for completion of the project, including specific phases of a project, estimated funding requirements for the upcoming year(s), and planned timing of or acquisition, pre-design, design, and construction or acquisition activities and transition to complete operation.
1.4 Descriptions of the general scope of the project, including expected service and financial benefits to the District.
1.5 A description of any impact the project will have on the current or future operating budget.
1.6 Estimated costs of the project, based on recent and accurate sources of information.
1.7 Identified funding sources for all aspects of the project, specifically referencing any financing requirements for the upcoming fiscal year.
1.8 Funding authority based either on total estimated project cost, or estimated project costs for the upcoming fiscal year. Consideration should be given to carry-forward funding for projects previously authorized.

Capital Planning
Capital Project Budgeting
Policy 13.1.0

1.9 Any analytical information deemed helpful for setting capital priorities.

The District needs a greater level of detail and information for non-routine capital projects than for routine projects. For non-routine projects, the capital budget should thoroughly describe the impact on the operating budget, number of additional positions required, tax or fee implications, and other financial or service impacts.

2.0 Reporting on the Capital Budget. The District recognizes the importance of timely and accurate reporting on projects adopted in the capital budget. Management, Trustees, and citizens should all have the ability to review the status and expected completion of approved capital projects. Periodic reports will be issued routinely on all on going capital projects. The reports will compare actual expenditures to the original budget, identify level of completion of the project, and enumerate any changes in the scope of the project, and alert management to any concerns with completion of the project on time or on schedule.

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT – ONE TEAM

Capital Planning
Capital Expenditures
Practice 13.2.0

RELEVANT POLICIES: 1.1.0 Strategic Planning, 9.1.0 Establishing Appropriate Capitalization Threshold for Capital Assets, 12.1.0 Multi-Year Capital Planning, and 13.1.0 Capital Project Budgeting

1.0 AUTHORITY

Decision-making responsibilities and duties on capital projects shall be allocated by the General Manager to specific members of the IVGID staff as provided herein. The staff member so assigned may delegate "duties" to another, but shall remain "responsible" for their actions pertaining to the project.

A Project Manager will usually be a representative of the IVGID department which will acquire or construct the project. The Project Manager may seek the input or assistance of a representative of the IVGID department that will utilize the capital asset. A planner, analyst, designer, or construction representative usually reports to the Project Manager as an employee or through a contract for services.

2.0 CAPITAL PROJECT FINANCING RESOURCES

Financial management of capital projects is controlled through a system including the Multi-Year Capital Improvement Plan and each fiscal year's Capital Improvement Project Budget. The ability to pay for the costs of a project will be based on identifiable and predictable financing resources at the time of acquisition.

2.1 **Establishment.** A capital project's financing resources may be established by action of the Board of Trustees by the adoption of a Capital Project Report. Financing resources may be established for each fund; for each program; or for each project or group of projects. The preference is on each project to facilitate calculating the affects of each project on the Multi-Year Capital Improvement Plan.

2.2 **Status.** All financing resources identified and received for a Capital Improvement Project shall be held in cash or investments and shall constitute an element of fund balance or net position until expended or released by an action of the Board of Trustees.

2.3 Interest. Investment earnings on a project's financing resources shall accrue to the project to the extent they were included in the Capital Improvement Project Data Sheet or are deemed needed for possible project cost adjustments. In any project where part of the financing resources came from bond proceeds, the investment earnings must be attached to the project in order to determine and comply with IRS arbitrage regulations.

2.4 Expenditures. Funds identified as financing resources may only be expended by action of the Board of Trustees according to the District's Capital Improvement Project Budget. Projects carrying over from one fiscal year to another are expected to be identified during each budget process to extend spending authority and facilitate completion of the construction or acquisition of the capital assets. The General Manager has the authority to redirect the design or specifications affecting up to an aggregate of $50,000 if it does not exceed the total approved cost of the project.

2.5 Exclusivity. All financing resources identified for a project, are considered exclusively for expenditures related to that project. No expenditures or obligations shall be made related to that project which cumulatively exceeds the available balance in identifiable and predictable financing resources.

2.6 Changes. The amount of funds in identifiable and predictable financing resources may be increased or decreased by action of the Board of Trustees, provided that no decrease shall occur which causes the unexpended financing resources for any project to fall below the cumulative total of obligations outstanding pertaining to the project.

2.7 **Close-out.** Upon completion or termination of a project, the unexpended financing resources for that project may be closed out by the General Manager, except when a previous action by the Board of Trustees, designates where the unexpended amount, if any, shall be transferred.

3.0 PROJECT LIFE CYCLE

Projects shall be managed in relation to the following typical project life cycle:

3.1 **Definition**. The process of developing a document which describes a specific project, in terms of location, function, cost, and other parameters. Approval of a Capital Project Data Sheet means the project has been **"defined."**

3.2 **Planning**. The process of developing documents which identify the location and function of projects, in relation to other projects and existing facilities. Approval of a project plan document within an approved Capital Project Summary means the project has been **"planned."**

3.3 **Feasibility**. The process of analyzing the practicality of a project, in terms of capital financing and cost, operating revenue and cost, environmental and permit conditions, and other factors. Acceptance information stated on the Capital Project Data Sheet as a feasibility report, means the project has been **"justified."**

3.4 **Scheduling**. The process of developing an outline identifying the cost, timing and financing of the capital project. All capital project expenditures shall be evaluated through a Multi-Year Capital Improvement Plan and authorized for expenditure through a specific fiscal year's Capital Improvement Plan Budget. Inclusion of a project within an approved Multi-Year Capital Improvement Plan means the project has been **"scheduled."**

3.5 Funding Identified. The process by which funds are identified, as either planned or set aside to underwrite capital costs. Identification of predictable financing resources for inclusion of a project in a specific fiscal year's Capital Improvement Plan Budget means the project has been **"funded."**

3.6 Design/Specification. The process of determining the size, specifications, acquisition/construction methods, and other factors prerequisite to construction or acquisition, including the selection of the designers. Approval of final design means the project has been **"designed."**

3.7 Construction/Acquisition. The process entails constructing or acquiring a project's assets, including the selection of contractors or vendors. Approval of final payment means the project has been **"completed."**

3.8 Requirements. All projects may not be subject to all phases, or be phased in the same order. However, all capital projects shall be defined. All capital projects shall be scheduled and have funding identified, prior to design/specification. All construction projects shall be planned. All construction projects shall be justified, prior to design/specification.

3.8.1.0 <u>Definition</u>

3.8.1.1 Trustees Responsibility: Relate District needs identified through the Strategic Plan to capital projects placed on the Multi-Year Capital Improvement Plan. **Duties:** Consider project definitions as part of Capital Improvement Project Budget submittal.

3.8.1.2 General Manager Responsibility: Ensure capital projects developed for consideration by the Board of Trustees relate to strategies and actions developed under the District's Strategic Planning Process. **Duties:** Approve capital project definitions.

3.8.1.3 Staff Duties: Prepare an accurate and up to date Capital Project Data Sheet, containing statement of project cost, schedule, location, financing, and other factors.

3.8.2.0 Planning

3.8.2.1 Trustees Responsibility: Ensure adequate planning basis for capital improvement projects. **Duties:** Define general goals, constraints, and directions. Award and execute planning contracts according to Nevada Revised Statutes. Establish public input process. Review and approve final plan.

3.8.2.2 General Manager. Responsibility: Ensure all issues are addressed and plans are coordinated with the Multi-Year Capital Improvement Plan. **Duties:** Review and approve planning scope. Approve requests for proposals on consulting contracts. Approve planning methods and planning team. Provide guidance to Project Manager during planning.

3.8.2.3 Project Manager. Responsibility: Administration, quality and accuracy. **Duties:** Define specific objectives, alternatives, criteria, and scope. Prepare requests for proposals and administer selection process for planning team. Prepare planning contracts. Recommend approval for and executing planning contracts. Coordinate project with, public, staff, and General Manager. Review and approve progress reports, make substantive and procedural decisions during planning process, and recommend preferred alternatives and final plans to the General Manager and Board of Trustees.

3.8.2.4 Engineering and Staff. **Duties:** Provide input to planning scope, methods, analysis, conclusions, and recommendations.

3.8.2.5 Planner Duties: Conduct analysis and produce planning documents and reports, for review by Project Manager.

3.8.3.0 <u>Feasibility</u>

3.8.3.1 Trustees. **Responsibility**: Ensure feasibility of capital improvement projects prior to design and construction. **Duties**: Determine when feasibility studies are required. Identify issues to be addressed. Award and execute consulting contracts according to Nevada Revised Statutes.. Review and accept the final "Capital Improvement Project Budget" as a basis for decision-making.

3.8.3.2 General Manager. **Responsibility**: Ensure critical issues are addressed and conservative approach to feasibility is applied. **Duties**: Review and approve study scope. Approve requests for proposals on consulting contracts. Approve study methods and team. Provide guidance to the Project Manager during study.

3.8.3.3 Project Manager. **Responsibility**: Administration, quality and accuracy. **Duties**: Define specific concerns, alternatives, criteria, and scope. Prepare requests for proposals and administer selection process for study team. Prepare study contracts. Recommend award and execute study contract. Coordinate project with, staff and General

Manager. Review and approve progress reports, make substantive and procedural decisions during study process, and approve conclusions and recommendations.

3.8.3.4 Finance, Engineering, and Staff. Duties: Provide input to study contract, scope, methods, analysis, conclusions, and recommendations.

3.8.3.5 Analyst. Duties: Conduct analysis and produce study documents and reports for review by the Project Manager.

3.8.4.0 <u>Scheduling</u>

3.8.4.1 Trustees. Responsibility: Prioritization and prudent investment of capital assets. **Duties:** Review and approve Multi-Year Capital Improvement Plan considering financing programs, priorities and needs and validity to proceed as scheduled. Approve project amendments and substitutions according to District purchasing policies.

3.8.4.2 General Manager. Responsibility: Validate scheduling in terms of sound financial planning and the ability to construct or acquire the capital assets. **Duties:** Review, revise and recommend capital improvement projects to the Board of Trustees.

3.8.4.3 Engineering Staff. Responsibility: Accuracy of cost projections and coordination of project scheduling. **Duties:** Identify capital project scheduling issues correlated to timing of expenditures and acquisition of the capital assets. Coordinate input of operating staff receiving the capital asset.

3.8.4.4 Finance Staff Responsibility: Adequacy of identifiable and predictable financing resources to meet the timing of expenditures. **Duties:** Analyze alternative financing schemes and prepare capital financing program coordinated with appropriate Capital Improvement Project Budget and the Multi-Year Capital Improvement Plan.

3.8.5.0 <u>Funding</u>

3.8.5.1 Trustees. Responsibility: Adequate identifiable and predictable financial resources exist for the project prior to the approval to proceed. **Duties:** Establish appropriate identifiable predictable financing resources are available. Increase and decrease funding level.

3.8.5.2 General Manager Responsibility: Approve recommendations for project to proceed and increases in project financing resources beyond levels identified in Capital Project Report, prior to submitted to Board. Duties: Review updated financial analysis for the capital project with Finance Staff for adequate financing resources and cash flows. Approve close-out upon project termination or completion.

3.8.5.3 Project Manager. Responsibility: Accuracy. **Duties:** Assemble and update project cost estimates.

3.8.5.4 Finance Staff. Responsibility: Administration of project finances. **Duties:** Produce periodic report on capital project financing resources, obligations and expenditures. Recommend periodic action to establish, increase, decrease, and close out financing resources. Consider the current affects of projects on the Capital Improvement Project Budget and the Multi-Year Capital Improvement Plan.

3.8.5.5 Engineering Staff. Duties: Coordinate estimates of project cost for periodic funding report.

3.8.6.0 <u>Design/Specification</u>

3.8.6.1 Trustees. Responsibility: General oversight of project design and specifications. **Duties:** Award and execute design contract according to Nevada Revised Statutes. Review and accept regulatory permit conditions on construction projects, if $50,000 or more.

3.8.6.2 General Manager. Responsibilities: Ensure design and specifications correlate to defined capital project. **Duties:** Approve design methods and team. Provide guidance to Project Manager during design. Review and approve final design/specification reports on projects. Review and accept regulatory permit conditions.

3.8.6.3 Project Manager. Responsibility: Administration, detailed oversight and design functionality. **Duties:** Prepare scope of services and requests for proposals for design services. Administer selection process for design team. Prepare design contracts. Recommend for award and execute design contracts. Assemble cost estimates; prepare project budget and budget revisions. Prepare project schedule and schedule revisions. Approve project budget and budget revisions. Approve project schedule and schedule revisions. Establish, execute, and administer arrangements for surveys, analysis, environmental studies, and other forms of technical support. Supervise designers. Establish functional and performance requirements. Coordinate activities of designers with the balance of the technical team, and operating staff. Present major design alternatives and issues. Provide direction to on major design alternatives and issues. Review and approve ongoing design reports and documents. Sign all regulatory permits and permit applications. Review, approve, and correct ongoing design reports and documents, including all technical specifications. Prepare construction contract forms. Assemble and submit regulatory permit applications and coordinate regulatory process. Approve all requests for payment.

3.8.6.4 Designer Duties: Analysis of design alternatives. Preparation of plans and specifications. Preparation of support material for permit applications, and other contract documents. Coordination of various members of the design team. Preparation of cost estimates.

3.8.7.0 Construction/Acquisition

3.8.7.1 Trustees. Responsibility: General oversight of contract awards, major payments and acceptance of capital assets constructed or acquired. **Duties**: Award and execute construction/acquisition contract according to Nevada Revised Statutes. Approve change orders cumulatively exceeding 10% of construction contract or $50,000, whichever is the greater.

3.8.7.2 General Manager. Responsibility: Ensure contracts and requests for payments submitted to the Board of Trustees for approval meet the requirements outlined in the Capital Improvement Project Budget. **Duties:** Approve change orders cumulatively not exceeding 10% of construction contract or $50,000. Upon substantial completion, approve release of retention for Construction projects.

3.8.7.3 Project Manager Responsibility: Detailed oversight. **Duties**: Recommend award and execute construction/acquisition contracts. Recommend approval of change orders. Recommend release of retention to General Manager and Board of Trustees. Recommend approval of the final payment. Administer bid process. Recommend contract award. Coordinate final contract preparation, including insurance, bonding, and certificates. Establish, administer and execute arrangements for inspection and testing. Supervise construction representatives. Review all inspection, testing and construction observation reports. Serve as District's representative to contractor and regulatory agencies. Approve all shop drawings. Approve requests for equals. Approve all certificates for payment. Update construction schedule.

3.8.7.4 Construction Representative. **Duties:** Observe construction and testing. Prepare construction observation reports. Advise Project Manager of deficiencies when noted. Notify Project Manager of deviations from plans and specifications. Prepare and execute notice to proceed.

BEST PRACTICES

Capital Planning Policies

Governments should develop and adopt capital planning policies that take into account their unique organizational characteristics including the services they provide, how they are structured, and their external environment.

Policies designed to guide capital planning help to assure that each jurisdiction□'s unique needs are fully considered in the capital planning process. Effective policies can also help a government 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 a government□s borrowing position by demonstrating sound fiscal management and showing the jurisdiction□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.[1] 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 finance 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.

GFOA recommends that governments develop and adopt capital planning policies that take into account their unique organizational characteristics including the services they provide, how they are structured, and their external environment.

Capital planning policies should provide, at minimum:

1. A description of how an organization 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.
2. A clear definition of what constitutes a capital improvement project.[2]
3. Establishment of a capital improvement program review committee and identification of members (for example, the finance officer or budget officer, representatives from planning, engineering, and project management, and, as deemed appropriate, operations departments most affected by capital plans, along with a description of the responsibilities of the committee and its members.
4. A description of the role of the public and other external stakeholders in the process. (The level and type of public participation should be consistent with community expectations and past experiences.)
5. Identification of how decisions will be made in the capital planning process including a structured process for prioritizing need and allocating limited resources
6. A requirement that the planning process includes an assessment of the government□s fiscal capacity so that the final capital plan is based on what can realistically be funded by the government rather than being simply a wish list of unfunded needs.
7. A procedure for accumulating necessary capital reserves for both new and replacement purchases.
8. A policy for linking funding strategies with useful life of the asset including identifying when debt can be issued and any restrictions on the length of debt.[3]
9. A requirement that a multi-year capital improvement plan be developed and that it include long term financing considerations and strategies.
10. 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.
11. A requirement that the plan include significant capital maintenance projects.
12. Provisions for monitoring and oversight of the CIP program, including reporting requirements and how to handle changes and amendments to the plan.

Notes:

1 See GFOA Best Practives on capital planning. (Multi-Year Capital Planning (2006) and The Role of Master Plans in Capital Improvement Planning (2008)

2 See GFOA⊠s Best Practice, Establishing Appropriate Capitalization Thresholds for Capital Assets

3 Capital planning policies should be consistent with or reference an organization⊠s debt policies

References:

- GFOA Best Practice, Asset Maintenance and Replacement, 2010
- GFOA Best Practice, Understanding Your Continuing Disclosure Responsibilities, 2010
- GFOA Best Practice, Disaster Preparadness, 2008
- GFOA Best Practice, Multi-Year Capital Planning, 2006
- GFOA Best Practice, Establishing Appropriate Capitalization Thresholds for Capital Assets, 2006

BEST PRACTICES

Capital Budget Presentation

Governments should incorporate a number of appropriate guidelines when presenting its capital budget.

GFOA has several best practices that should be incorporated into the presentation of the capital budget. These best practices include (1) capital planning policies, (2) master plans and capital improvement planning, (3) multi-year capital planning, (4) capital asset management, (5) communicating capital improvement strategies, and (6) capital project monitoring and reporting. In addition, the capital presentation should include a summary/highlights section, project detail on major capital items, and operating impacts. An exceptional capital presentation enhances the transparency and accountability to citizens. It gives a broader context for citizens to understand major components of the capital budget.

GFOA recommends that governments incorporate the following guidelines when presenting the capital budget

1. *Capital planning policies.* Capital planning policies should be included as part of the overall financial policy section of the entity. The policies essentially set up the "ground rules" on how the organization will approach capital planning. Capital planning policy items may include such items as a clear definition of capital projects, the role of the various stakeholders in the process, financing policies (debt options versus pay as you go), funding sources, multi-year requirements, legal requirements, and monitoring oversight.
2. *Master plans and capital improvement planning.* The presentation of the capital section should include a linkage with how CIP decisions relate to master plans. This can be done through diagrams, tables, and/or discussion.
3. *Multi-year capital planning.* The capital budget should have a direct link to the multi-year capital improvement plan. The multi-year capital plan should identify needs, determine financial impacts, prioritize, and include a comprehensive financial plan. In addition, assumptions for sources and uses need to be identified. This would include contingencies as well.
4. *Capital asset management.* Major categories under capital asset management include condition ratings and service reliability. Presenting this information can be a good selling point for aspects of the capital program.
5. *Communicating capital improvement strategies.* The strategy of the capital improvement plan needs to be communicated to stakeholders with corresponding feedback. This can be done through a clear message and the use of various presentation methodologies including signage, press articles, website, social media, interest groups, public meetings, use of media, and a budget document.
6. *Capital project monitoring and reporting.* When presenting capital planning information, there is a need to decide what data is relevant for both the internal and external stakeholders. Systems need to be in place to make sure that the data presented for projects is accurate for both timing and dollars.
7. *Highlights/Summary.* The capital presentation should focus on both sources and uses. The government should indicate the total dollar amount of capital expenditures for the budget year and for the multi-year plan. The capital plan sources and uses summary should include all projects (regardless of fund) that fit within the government's definition of capital expenditures. This information can be presented by fund, category, priority, strategic goal, or geographic location. The government should identify the funding sources for the same time period as expenditures. Pie charts are useful for identifying components, while bar charts show specific trends (historical and future). A budget overview or separate budget in brief could be included that presents both operating and capital highlights. Capital projects should be broken out between recurring and non-recurring. Recurring capital projects are those that 1) are included in almost every budget and 2) have a regular replacement cycle. Capital projects could be grouped by category, department, type, function, or funding. Unfunded projects should be summarized.
8. *Individual Capital Project Detail.* Including individual capital project detail for major projects can be a very effective communication tool. To avoid placing excessive detail in the capital section of the budget document, consideration may be given to placing the additional information on the web or in a separate capital document. Detail for major projects should include:
   a. *Description.* For significant and/or non-recurring capital expenditures, the document should concisely describe these items (i.e. indicate the project's purpose and funding sources) and indicate the amount appropriated for the project during the budget year(s).

   b. *Timetable.* Showing a timetable for different phases of a project is very informative. Capital project schedules can be presented on the individual sheets.

   c. *Graphics.* Legible graphic illustrations (pictures or maps) can add value to a capital project presentation.

   d. *Links to Other Plans.* Governments may consider indicating on the individual capital project sheets what specific goals that the capital project is fulfilling.

   e. *Revenue and Expenditure Estimates.* The individual project dollar estimates should be broken out by revenue type and expenditure component.
9. *Operating Impacts.* Governments should discuss and quantify the operating impact of capital projects. The impacts should be identified on an individual project basis, but may be summarized.
   a. *Policies:* A specific policy on operating impacts should be included under the capital section in the financial policies of the government. A rule might be established that the capital improvement program may not be submitted/approved until specific dollar impacts are noted.

   b. *Assumptions.* Items to consider when making assumptions include:Timeframe to determine when costs, savings or revenue will start. For example, first-year startup costs will likely differ from costs in successive years when savings may be realized.
      i. Various anticipated phases of the project.

      ii. In-house or external operations.

      iii. Type of work being done.

      iv. Whether the costs, savings, or revenues are recurring or non-recurring. For example, replacement and maintenance costs may occur on alternating or periodic years rather than annually over the life of a capital asset. A government should analyze the cycles for such up-keep costs and plan accordingly.

   c. *Classification.* Operating impacts can be classified into one of three elements or a combination of the three. These include increased revenues, increased expenditures or additional cost savings. When possible, included specific dollar quantification with accompanying discussion of the impact.
      i. Increased revenues may be the result of additional volume, like opening a new train line, a new swimming pool, or a sports facility.

      ii. Increased expenditures are often the result of a new facility, like a school building, fire station, etc. This would result in additional headcount and associated expenditures. Expenditures can be broken out by component.

iii. Savings may result from a number of items such as more efficient energy savings, more productive software, and lower maintenance and repair expenditures.

III - Fund Balance / Working Capital Policy

- Background / Preliminary Recommendations (DRAFT)
- Board Policy 7.1.0 and 19.1.0
- Board Practice 7.2.0 and 19.2.0
- Best Practices / Guidelines

FUND BALANCE AND WORKING CAPITAL
Board Policy 7.1.0
Board Practice 7.2.0
Board Policy 19.1.0
Board Practice 19.2.0

Background -

- Board Policy 7.1.0 relates to "Appropriate Level of Fund Balance"
    - GFOA and GAAP guidelines and definitions
- Board Practice 7.2.0 relates to "Appropriate Level of Fund Balance"
    - Minimum requirement under NAC 354.650
- Board Policy ~~17.1.0~~ relates to "Appropriate Level of Working Capital"
    - GFOA and GAAP guidelines and definitions
- Board Practice ~~17.2.0~~ relates to "Appropriate Level of Working Capital"
    - Operating Working Capital = 25% of Operating Expenses
    - Debt = 1-year interest expense
    - Capital = 1-year of 3-year average depreciation

Best Practices and Resources:

- GFOA provides guidance on best practices for development of policies related to Unrestricted Fund Balance and Appropriate Level of Working Capital for Enterprise Funds.
    - Based on "risk" to be mitigated
- Best practices suggest that formal fund balance policies be established to provide for:
    - Appropriate level of fund balance
    - Appropriate use(s) of established reserves, and
    - Guidelines for replenishment of reserves when used.
- Fund Balance – General Fund
    - Nevada Administrative Code (NAC 354.650) establishes a (minimum) fund balance of 4% of operating expenditures for public agencies; the NAC further provides for notification/explanation to be provided to the Department of Taxation in the event that reported fund balances fall below 4% of actual expenditures.
    - The GFOA acknowledges that the appropriate level of fund balance for the General Fund should take into account each government's own unique circumstances, but recommends general-purpose governments maintain an unrestricted fund balance of no less than 2-months of regular general fund revenues or general fund expenditures.

- Working Capital – Enterprise Funds
    - GFOA recommends that government's target for working capital be no less than 45-days of annual operating expenses (1.5 months).
    - The District has contracted with an outside consultant (Raftelis) to review the Public Works operations and capital asset management and provide recommendations, to include appropriate level of working capital to inform update of Board Policy 17.1.0 and Board Practice 17.2.0.

Preliminary Recommendations:

1) It is recommended that Board Policy 7.1.0, Board Practice 7.2.0, Board Policy 17.1.0 and Board Practice 17.2.0 be updated to establish a target minimum fund balance(s) as well as incorporate fund balance policy language consistent with GFOA guidelines for best practices

2) It is recommended that Board Policy 17.1.0 and Board Practice 17.2.0 related to Appropriate Levels of Working Capital be updated to establish appropriate level of working capital for the District's Enterprise Funds, informed by pending recommendations from the review of the District's utility operations by third-party consultant.
    a. Debt Service should be reviewed in relation to bond covenants; usually require annual revenues equal to 100-120% of annual debt payments, which have <u>priority</u> over operating expenses
    b. Policy should distinguish between Capital Reserve (as a % of annual capital budget or depreciation) and Capital Asset Replacement fund (as a percentage of five-year CIP).

3) Staff is reviewing the applicability of establishing a Working Capital policy for its Internal Service Funds; while reported as Enterprise Funds, these funds activities are generally self-funded with year-end adjustments made to clear fund balances.

4) Board Practices 7.2.0 and 17.2.0 should also be updated to reflect the transition of the District's Community Services Fund and Beach Fund from Special Revenue Funds to Proprietary (Enterprise) Funds.

5) Consideration should be given to consolidating updates to Policies 7.1.0 and 17.1.0 as well as Practices 7.2.0 and 17.2.0 to provide for a comprehensive Policy and related Practice related to appropriate levels of fund balance and working capital across all District funds.

Appropriate Level of Fund Balance
Practice 7.2.0 / Practice 19.2.0
(Sample Update)

PRACTICE. It is the practice of the Incline Village General Improvement District, hereinafter referred to as the District, to maintain Fund Balance in the General Fund and each governmental or proprietary fund type in a manner which provides for contractual, bond and customer service obligations, while meeting its routine and non-routine cash flow requirements and complying with all federal, state and local statutes and regulations.

This policy/practice establishes the minimum level of funding to be maintained in reserve within the fund balance of the District's governmental and proprietary funds, defines the conditions under which these funds can be utilized, and provides a timeline for replenishment of reserve funds, when utilized.

1.0 Scope

This Practice shall apply accounting principals as forth in Governmental Accounting Standards Board (GASB) Statement 54 considering the unique characteristics of the District. To that end the following measurements will apply to each fund or type:

2.0 Appropriate Level of Fund Balance and Working Capital

General Fund

The policy of the District shall be to maintain a minimum funds balance within the General Fund of ___ % to provide for economic uncertainty, fluctuations in General Fund revenues and unforeseen events that may require of unbudgeted expenditures.

In no case shall the fund balance for the District's General Fund fall below the 4% of expenditures required under Nevada Administrative Code Section 354.

The appropriate level of fund balance to be maintained in reserve within the District's General Fund shall be reviewed annually

Proprietary Fund Types:

Measurements of target working capital ~~fund balances~~ with Stabilization Arrangements:

Community Services .... Operations - 25% of operating expenses
Debt Service - One year's payments *(or as set by debt coverage ratio established in bond documents)*

(Capital Expenditure – 1 year of a 3 year average depreciation)

Beach .... Operations - 25% of operating expenses
Debt Service - One year's payments *(or as set by debt coverage ratio established in bond documents)*
(Capital Expenditure – 1 year of a 3 year average depreciation)

Utilities .... Operations - 25% of operating expenses
Debt Service - One year's payments *(or as set by debt coverage ratio established in bond documents)*
Capital Expenditure – 1 year of a 3 year average depreciation

Internal Services .... Operations - ~~25%~~ ____% of operating expenses

Operating expenses for these calculations do not include depreciation or interest expense since they are covered by separate definitions.

The appropriate level of working capital to be maintained in reserve within the District's enterprise funds shall be reviewed annually.

~~**Governmental Activities:**~~

~~Workers Compensation .... SIR - Stated Deductible~~

3.0 Appropriate Use of Fund Balances and Working Capital Held in Reserve

The targeted level of fund balance and working capital established by Board policy and practice serves to address significant short-term issues, including unexpected revenue shortfalls, higher than anticipated expenditures, or unforeseen emergencies.

It is the intent of the Board of Trustees to limit the use of reserved fund balances to address unanticipated, non-recurring needs. Fund balances should not be applied to recurring annual operating expenditures. Fund balances may, however, be applied buffer the impacts of a loss or reduction in revenues to allow time for the District to restructure its operations, but such use will only take place in the context of a Board-approved long-term financial plan.

4.0 Excess Fund Balance or Working Capital

At the end of each fiscal year, the Finance Department will report on the audited year-end budgetary fiscal results. Should actual revenues exceed expenditures, including contractual obligations and carry-forward items, a year-end surplus shall be reported.

Any year-end operating surplus which results in unrestricted fund balances in excess of the targeted fund balances established by the Board, shall be deemed available for allocation to specific needs, subject to Board action. These include:

1) *Payments toward unfunded liabilities, deferred maintenance and asset replacement, or other non-recurring needs.*
2) *Transfer to other funds, as deemed appropriate, to offset year-end deficits within those funds*
3) *Allocation to capital projects with shortfalls in funding sources and/or to provide matching funds for awarded grants.*
4) *Re-appropriation within the subsequent year's operating budget to provide for one-time, non-recurring needs.*

5.0 Replenishment of Fund Balances or Working Capital

If the General Fund fund balance reserve or Enterprise Fund Working Capital reserve are required to be drawn-down below the minimum level established by Board policy, a plan will be developed and implemented to replenish fund balances. Replenishing fund balances will be a priority use of one-time resources, and minimum fund balances will be restored within a maximum of two fiscal years.

6.0 Definition of Stabilization Arrangement

(To be updated in conjunction with pending Utility Rate Study)

In conformity with GASB Statement 54, the District will establish a stabilization arrangement only when it includes:

2.0.1 Recognition of the authority by which the arrangement is established including resolution, ordinance or other action.
2.0.2 When to make additions to the stabilization amount
2.0.3 When stabilization amounts can be spent
2.0.4 That a balance will be reported at each fiscal year end.

7.0 Other Classifications

The District will apply other classifications and accounting standards under GASB 54 including the use of Non-spendable, Restricted, Committed, Assigned, Unassigned and Unrestricted when presenting either a Statement of Net Assets or other forms of fund balance in its financial reports.

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT -- ONE TEAM

Budgeting and Fiscal Management
Appropriate Level of Fund Balance
Policy 7.1.0

POLICY. The District will maintain a formal practice on the level of Fund Balance that should be maintained in the General and Special Revenue Funds.

The adequacy of Unassigned Fund Balance in the General Fund should be assessed based upon the District's own specific circumstances. (Nevertheless, the Government Finance Officers Association (GFOA) recommends, at a minimum, that general-purpose governments, regardless of size, maintain Unassigned Fund Balance in their General Fund of no less than five to fifteen percent of regular General Fund operating revenues.) The Nevada Administrative Code (NAC 354.650) requires a budgeted fund balance of 4%, based on the actual expenditures of the General Fund's previous fiscal year.

Building "stabilization arrangements" in the General Fund is an acknowledged purpose in response to revenue shortfalls and unanticipated expenditures.

The District employs the term "fund balance" to describe the net position of governmental funds calculated in accordance with Generally Accepted Accounting Principles (GAAP) at the individual fund level. Budget professionals commonly use this same term to describe the net position of governmental funds calculated on a government's budgetary basis. In both cases, fund balance is intended to serve as a measure of the financial resources available for use in a governmental fund type.

Financial reporting distinguishes restricted fund balance from unassigned and unrestricted fund balance. Typically, only the latter is available for spending. A "stabilization arrangement" indicates a designated portion of unassigned or unrestricted fund balance is subject to an action by the governing body concerning the use of that amount.

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
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Budgeting and Fiscal Management
Appropriate Level of Fund Balance
Practice 7.2.0

RELEVANT POLICIES: 1.1.0 Strategic Planning, 7.1.0 Appropriate Level of Fund Balance, 12.1.0 Multi-Year Capital Planning, and 13.1.0 Capital Project Budgeting, 14.1.0 Debt Management

PRACTICE. It is the practice of the Incline Village General Improvement District, hereinafter referred to as the District, to maintain Fund Balance in the General Fund and each governmental or proprietary fund type in a manner which provides for contractual, bond and customer service obligations, while meeting its routine and non-routine cash flow requirements and complying with all federal, state and local statutes and regulations.

1.0 SCOPE

This Practice shall apply accounting principals as forth in Governmental Accounting Standards Board (GASB) Statement 54 considering the unique characteristics of the District. To that end the following measurements will apply to each fund or type:

General Fund

The General Fund must meet the minimum balance requirements under Nevada Administrative Code Section 354.650.

Special Revenue Funds

Community Services; 25% of a fiscal years' operating expenditures (based on the current adopted budget) other than capital expenditure and debt service.

Beach Enterprise; 25% of a fiscal year's operating expenditures (based on the current adopted budget) other than capital expenditure and debt service.

Proprietary Fund Types:

Measurements of target fund balances:

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Budgeting and Fiscal Management
Appropriate Level of Fund Balance
Practice 7.2.0

Utilities....................................Operations - 25% of operating expenses for the fiscal year based on the current adopted budget. **

Internal Services......................Operations - 25% of operating expenses for the fiscal year based on the current adopted budget. **

Workers Compensation...........An amount equal to the State of Nevada required deposit, plus sufficient resources to cover the last determined open exposure for prior claims, if not covered by purchased insurance or a termination insurance policy.

** Operating expenses for these calculations do not include depreciation or interest expense since they are covered by separate definitions.

2.0 Definition of Stabilization Arrangement

In conformity with GASB Statement 54, the District may establish a stabilization arrangement only when it includes:

2.0.1 Recognition of the authority by which the arrangement is established including resolution, ordinance or other action.

2.0.2 When to make additions to the stabilization amount

2.0.3 When stabilization amounts can be spent

2.0.4 That a balance will be reported at each fiscal year end.

3.0 Other Classifications

The District will apply other classifications and accounting standards under GASB 54 including the use of Nonspendable, Restricted, Committed, Assigned, Unassigned and Unrestricted when presenting either a Statement of Net Position or other forms of fund balance in its financial reports.

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT – ONE TEAM

Budgeting and Fiscal Management
Appropriate Level of Working Capital
Policy 19.1.0

POLICY. The District will maintain a formal practice on the level of working capital that should be maintained in the Enterprise (Utility) Fund.

Enterprise Funds distinguish between current and non-current assets and liabilities. It is possible to take advantage of this distinction to calculate Working Capital (i.e., current assets less current liabilities). The measure of working capital indicates the relatively liquid portion of total Enterprise Fund capital, which constitutes a margin or buffer for meeting obligations.
It is essential that the District maintain adequate levels of working capital in its Enterprise Funds to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenses) and to ensure stable services and fees. Working Capital is a crucial consideration, too, in long-term financial planning. Credit rating agencies consider the availability of working capital in their evaluations of continued creditworthiness. Likewise, laws and regulations may speak to appropriate levels of working capital for some Enterprise Funds.

The Government Finance Officers Association (GFOA) recommends that local governments adopt a target amount of working capital to maintain in each of their Enterprise Funds. The District's targets will be formally described in the Practice as adopted and amended as needed.

Working capital is defined as current assets minus current liabilities; the District will consider certain characteristics of working capital that affect its use as a measure. Specifically, the "current assets" portion of working capital includes assets or resources that are reasonably expected to be realized in cash (e.g., accounts receivable) or consumed (e.g., inventories and prepaid expenses) within a year.

Stability of revenues and expenses are also considerations for an accurate calculation of working capital. The District will consider the adequacy of Working Capital in its Enterprise Funds during each annual budget process. The majority of such consideration will be established by the predictability of the revenues to be received from users. Building Working Capital in the Enterprise Funds is an acknowledged purpose in response to revenue shortfalls and unanticipated expenditures, debt service requirements and planning for capital expenditures.

Budgeting and Fiscal Management
Appropriate Level of Working Capital
Policy 19.1.0

The District employs the term "Net Position" for Enterprise Funds, calculated in accordance with Generally Accepted Accounting Principles (GAAP). Financial reporting distinguishes Restricted from Unrestricted Net Position. Typically, only the latter is available for spending. Working Capital for operating needs should be sourced from Unrestricted Net Position. The District has debt service and capital expenditure needs that extend beyond one year. Therefore, amounts outside of the calculation of Working Capital may develop for those purposes. As such these may also be considered elements of both Restricted and Unrestricted Net Position.

INCLINE VILLAGE
GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT – ONE TEAM

Budgeting and Fiscal Management
Appropriate Level of Working Capital
Practice 19.2.0

RELEVANT POLICIES: 1.1.0 Strategic Planning, 12.1.0 Multi-Year Capital Planning, and 13.1.0 Capital Project Budgeting, 14.1.0 Debt Management, 19.1.0 Appropriate Level of Working Capital

PRACTICE. It is the practice of the Incline Village General Improvement District, hereinafter referred to as the District, to maintain Working Capital in each Enterprise Fund in a manner which provides for contractual, bond and customer service obligations, while meeting its routine and non-routine cash flow requirements and complying with all federal, state and local statutes and regulations.

1.0 SCOPE

This Practice shall apply accounting principals as forth in Generally Accepted Accounting Principles (GAAP) considering the unique characteristics of the District. To that end the following measurements will apply to each fund:

- Strength of collections of accounts receivable, to the extent they can be converted to cash within a timeframe expected for use in the District's operations.
- Historical consumption of inventories and prepaid expenses, to the extent they can be utilized to support operations within the timeframe of the District's budget cycle.
- Levels and flow of annual operating expenses. At no time will the calculation consider less than 45 days operating needs. However, any amount over 90 days needs must be specifically supported and approved in writing by the District's General Manager.
- Support by the General Fund. This includes shared expenses and operating transfers that represent Central Services Cost Allocations.
-
- Control over rates and revenues.
- Asset age and condition, whether there is a chance of extra ordinary repairs or a replacement under the Capital Improvement Plan.
- Volatility of expenses and the ability to control fixed and variable costs.

Budgeting and Fiscal Management
Appropriate Level of Working Capital
Practice 19.2.0

- Management plans for Working Capital including any inherent affects of Restricted Net Position or items extending beyond one year that would normally not be covered by Working Capital.
- Debt Service or Multi-Year Capital Plan needs identified as current requirements.

2.0 Definition of Target amounts for Working Capital as measured each Fiscal Year End

Utilities

Operations – 45 to 90 days of operating expenses**

Debt Service – up to one year's payments of interest expense, since current maturities of long term debt are already considered in determining working capital, when classified as a current liability.

Capital Expenditure – up to 1 year of a 3 year average depreciation

** Operating expense excludes depreciation and interest.

3.0 Other Accumulation of Resources

The District may accumulate other resources in support of Debt Service or the Multi-Year Capital Plan in addition to Working Capital since these needs extend beyond the measurement period of one year.

BEST PRACTICES

Fund Balance Guidelines for the General Fund

Governments should establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund for GAAP and budgetary purposes.

In the context of financial reporting, the term *fund balance* is used to describe the net position of governmental funds calculated in accordance with generally accepted accounting principles (GAAP). Budget professionals commonly use this same term to describe the net position of governmental funds calculated on a government's budgetary basis.1 While in both cases *fund balance* is intended to serve as a measure of the financial resources available in a governmental fund; it is essential that differences between GAAP *fund balance* and budgetary *fund balance* be fully appreciated.

1. GAAP financial statements report up to five separate categories of fund balance based on the type and source of constraints placed on how resources can be spent (presented in descending order from most constraining to least constraining): *nonspendable fund balance, restricted fund balance, committed fund balance, assigned fund balance,* and *unassigned fund balance.*2 The total of the amounts in these last three categories (where the only constraint on spending, if any, is imposed by the government itself) is termed *unrestricted fund balance.* In contrast, budgetary fund balance, while it is subject to the same constraints on spending as GAAP fund balance, typically represents simply the total amount accumulated from prior years at a point in time.
2. The calculation of GAAP fund balance and budgetary fund balance sometimes is complicated by the use of sub-funds within the general fund. In such cases, GAAP fund balance includes amounts from all of the subfunds, whereas budgetary fund balance typically does not.
3. Often the timing of the recognition of revenues and expenditures is different for purposes of GAAP financial reporting and budgeting. For example, encumbrances arising from purchase orders often are recognized as expenditures for budgetary purposes, but never for the preparation of GAAP financial statements.

The effect of these and other differences on the amounts reported as *GAAP fund balance* and *budgetary fund balance* in the general fund should be clarified, understood, and documented.

It is essential that governments maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. In most cases, discussions of fund balance will properly focus on a government's general fund. Nonetheless, financial resources available in other funds should also be considered in assessing the adequacy of unrestricted fund balance in the general fund.

GFOA recommends that governments establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund for GAAP and budgetary purposes.3 Such a guideline should be set by the appropriate policy body and articulate a framework and process for how the government would increase or decrease the level of unrestricted fund balance over a specific time period.4 In particular, governments should provide broad guidance in the policy for how resources will be directed to replenish fund balance should the balance fall below the level prescribed.

Appropriate Level. The adequacy of unrestricted fund balance in the general fund should take into account each government's own unique circumstances. For example, governments that may be vulnerable to natural disasters, more dependent on a volatile revenue source, or potentially subject to cuts in state aid and/or federal grants may need to maintain a higher level in the unrestricted fund balance. Articulating these risks in a fund balance policy makes it easier to explain to stakeholders the rationale for a seemingly higher than normal level of fund balance that protects taxpayers and employees from unexpected changes in financial condition. Nevertheless, GFOA recommends, at a minimum, that general-purpose governments, regardless of size, maintain unrestricted budgetary fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures.5 The choice of revenues or expenditures as a basis of comparison may be dictated by what is more predictable in a government's particular circumstances.6 Furthermore, a government's particular situation often may require a level of unrestricted fund balance in the general fund significantly in excess of this recommended minimum level. In any case, such measures should be applied within the context of long-term forecasting, thereby avoiding the risk of placing too much emphasis upon the level of unrestricted fund balance in the general fund at any one time. In establishing a policy governing the level of unrestricted fund balance in the general fund, a government should consider a variety of factors, including:

1. The predictability of its revenues and the volatility of its expenditures (i.e., higher levels of unrestricted fund balance may be needed if significant revenue sources are subject to unpredictable fluctuations or if operating expenditures are highly volatile);
2. Its perceived exposure to significant one-time outlays (e.g., disasters, immediate capital needs, state budget cuts);
3. The potential drain upon general fund resources from other funds, as well as, the availability of resources in other funds;
4. The potential impact on the entity's bond ratings and the corresponding increased cost of borrowed funds;
5. Commitments and assignments (i.e., governments may wish to maintain higher levels of unrestricted fund balance to compensate for any portion of unrestricted fund balance already committed or assigned by the government for a specific purpose). Governments may deem it appropriate to exclude from consideration resources that have been committed or assigned to some other purpose and focus on unassigned fund balance, rather than on unrestricted fund balance.

Use and Replenishment.

The fund balance policy should define conditions warranting its use, and if a fund balance falls below the government's policy level, a solid plan to replenish it. In that context, the fund balance policy should:

1. Define the time period within which and contingencies for which fund balances will be used;
2. Describe how the government's expenditure and/or revenue levels will be adjusted to match any new economic realities that are behind the use of fund balance as a financing bridge;
3. Describe the time period over which the components of fund balance will be replenished and the means by which they will be replenished.

Generally, governments should seek to replenish their fund balances within one to three years of use. Specifically, factors influencing the replenishment time horizon include:

1. The budgetary reasons behind the fund balance targets;
2. Recovering from an extreme event;
3. Political continuity;

4. Financial planning time horizons;

5. Long-term forecasts and economic conditions;

6. External financing expectations.

Revenue sources that would typically be looked to for replenishment of a fund balance include nonrecurring revenues, budget surpluses, and excess resources in other funds (if legally permissible and there is a defensible rationale). Year-end surpluses are an appropriate source for replenishing fund balance.

Unrestricted Fund Balance Above Formal Policy Requirement. In some cases, governments can find themselves in a position with an amount of unrestricted fund balance in the general fund over their formal policy reserve requirement even after taking into account potential financial risks in the foreseeable future. Amounts over the formal policy may reflect a structural trend, in which case governments should consider a policy as to how this would be addressed. Additionally, an education or communication strategy, or at a minimum, explanation of large changes in fund balance is encouraged. In all cases, use of those funds should be prohibited as a funding source for ongoing recurring expenditures.

Notes:

1. For the sake of clarity, this recommended practice uses the terms GAAP fund balance and budgetary fund balance to distinguish these two different uses of the same term.
2. These categories are set forth in Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions.*
3. Sometimes restricted fund balance includes resources available to finance items that typically would require the use of unrestricted fund balance (e.g., a contingency reserve). In that case, such amounts should be included as part of unrestricted fund balance for purposes of analysis.
4. See Recommended Practice 4.1 of the National Advisory Council on State and Local Budgeting governments on the need to "maintain a prudent level of financial resources to protect against reducing service levels or raising taxes and fees because of temporary revenue shortfalls or unpredicted one-time expenditures" (Recommended Practice 4.1).
5. In practice, a level of unrestricted fund balance significantly lower than the recommended minimum may be appropriate for states and America's largest governments (e.g., cities, counties, and school districts) because they often are in a better position to predict contingencies (for the same reason that an insurance company can more readily predict the number of accidents for a pool of 500,000 drivers than for a pool of fifty), and because their revenues and expenditures often are more diversified and thus potentially less subject to volatility.
6. In either case, unusual items that would distort trends (e.g., one-time revenues and expenditures) should be excluded, whereas recurring transfers should be included. Once the decision has been made to compare unrestricted fund balance to either revenues and/or expenditures, that decision should be followed consistently from period to period.

This best practice was previously titled Appropriate Level of Unrestricted Fund Balance in the General Fund.

BEST PRACTICES

Working Capital Targets for Enterprise Funds

Local governments should adopt a target amount of working capital to maintain in each of their enterprise funds. Additionally, governments should use working capital as the measure of available margin or buffer in enterprise funds.

Enterprise funds distinguish between current and non-current assets and liabilities. It is possible to take advantage of this distinction to calculate working capital (i.e., current assets less current liabilities). The measure of working capital indicates the relatively liquid portion of total enterprise fund capital, which constitutes a margin or buffer for meeting obligations.

It is essential that a government maintain adequate levels of working capital in its enterprise funds to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenses) and to ensure stable services and fees.

Working capital is a crucial consideration, too, in long-term financial planning. Credit rating agencies consider the availability of working capital in their evaluations of continued creditworthiness. Likewise, laws and regulations may speak to appropriate levels of working capital for some enterprise funds.

GFOA recommends that local governments adopt a target amount of working capital to maintain in each of their enterprise funds. Ideally, targets would be formally described in a financial policy and/or financial plan.

GFOA recommends that governments use working capital as the measure of available margin or buffer in enterprise funds. Although as previously stated, working capital is defined as current assets minus current liabilities, government finance officers should be aware of certain characteristics of working capital that affect its use as a measure. Specifically, the current assets portion of working capital includes assets or resources that are reasonably expected to be realized in cash (e.g., accounts receivable) or consumed (e.g., inventories and prepaids) within a year, which leads to two considerations for an accurate calculation of working capital:

- Strength of collection practices. An appropriate allowance for uncollectibles should be established and the amount of the receivable that is expected to be collected in cash within one year should be determined in a manner that is consistent with the collection practices of the government. If the accounts receivable collection practices of the enterprise fund are inconsistent or weak, then less of the accounts receivable amount should be reported as current assets.
- Historical consumption of inventories and prepaids. The amount of inventories and prepaids included in current assets should be a realistic estimate of the amount that will be consumed in one year based on a historical usage pattern and current operating levels (inventories) or based on the time periods to which the items relate (prepaids).
- Support from general government. Some enterprise funds may be supported by general taxes or transfers from a general government. These enterprise funds may require lower levels of working capital if they are supported by these contributors. For a heavily subsidized enterprise fund the 45-day minimum working capital recommendation contained in this Best Practice might be met through support from the general government, if a financial buffer or cushion for the enterprise fund is to be provided by the general government (or other outside contributor).
- Transfers out. If the enterprise fund is expected to make a transfer to the general government or to some other fund, then this sort of claim on the enterprise fund's assets may call for higher levels of working capital to maintain flexibility. Transfers could include an enterprise fund's contributions to overhead/support functions, subsidies granted to other operations, or any other transfer of resources. Regardless of the rationale of the transfer, governments should take into account the claim on working capital when setting a target amount.
- Cash cycles. Does the enterprise fund experience large peaks and valleys in its cash position during the year? For example, a water enterprise fund may experience significantly higher levels of cash on hand during the summer months compared to the winter. Volatile cash cycles call for higher levels of working capital. Another consideration is the length of the billing cycle. A longer billing cycle would call for higher levels of working capital because the enterprise fund will have longer durations between major infusions of cash.
- Customer concentration. Is the enterprise fund dependent on a few customers for a large portion of its revenues or is the customer base diversified? For example, a port enterprise fund may be dependent on a few major shippers or commerce in a niche product. Lower customer concentration may mean that the enterprise fund can safely operate with lower levels of working capital.
- Demand for services. Does the enterprise fund face a steady demand for service or is demand potentially volatile, thereby leading to volatility in of income? For example, the demand for utility services is steady compared to demand for air travel. Also consider the impact of competitive position on demand. Direct competitors or the availability of reasonable substitutes could lead to greater volatility in demand for the enterprise fund's services. More volatility implies greater need for working capital margins.
- Control over rates and revenues. Does the enterprise fund have the ability to change rates, implement new charges, or otherwise raise revenues from its customers in a simple fashion? For example, transit enterprise funds are often constrained from raising rates by political pressure. Other enterprise funds may be subject to a rate control board. Those that face competitors in their market may have less effective control over their rates and revenues. More revenue constrained enterprise funds may need higher levels of working capital.
- Asset age and condition. What is the age and condition of the enterprise fund's infrastructure? Older infrastructure has greater exposure to extraordinary repair needs. Enterprise funds with newer and/or well maintained capital assets may be able to operate with less working capital than other enterprise funds.
- Volatility of expenses. Are the expenses of the enterprise fund volatile or does the enterprise fund have a high degree of control over its expenses? For example, the expenses of a solid waste enterprise fund tend to be fairly stable throughout the year. In another example, water or sewer enterprise funds may be more vulnerable to large expense spikes from extreme weather. Enterprise funds with more stable expenses can safely operate with less working capital than other enterprise funds.
- Control over expenses. Consider the enterprise fund's level of fixed and variable costs and the ability to reduce variable costs in response to lower revenues. For instance, if a convention center does not book an event, it does not need to hire temporary help and incur other expenditures in support of the event. An enterprise fund with a high percentage of operational costs which vary depending upon revenues or operating levels may operate with lower levels of working capital.
- Management plans for working capital. Working capital includes assets, which can include both truly unrestricted resources and resources that have internal limitations placed upon them (e.g., board-designated) and/or that may be committed for future capital spending. These amounts may appear as unrestricted on the balance sheet but, in actuality, may be unavailable in the future to serve as a buffer or

tool to help manage financial risk. If these types of limitations exist, the working capital target should be adjusted to arrive at an amount that represents a true amount available as a tool to manage financial risk.

- Separate targets for operating and capital needs. Depending on the nature of the enterprise fund, governments might also consider designating separate targets for operating and capital needs, especially when the enterprise fund is very capital intensive. For example, there might be a separate amount identified for equipment replacement or debt service. In such a case, targets should be separately evaluated based on the particular features of the isolated amounts.
- Debt position. Enterprise funds often carry significant amounts of debt, which is used to acquire capital assets. The amount and type of debt an enterprise fund carries can have important ramifications for working capital targets. For example, an enterprise fund with a large amount of variable rate debt may need additional buffer to manage the risk associated with interest rate volatility. In addition, uneven and increasing or lump-sum debt principal payments to be made in future years may raise the amount of working capital that the enterprise fund should maintain. Viewing the amount of working capital in this broader context will help ensure that resources are available to make debt payments as they come due.

Notes:

1 The recommendation is to use annual operating expenses which include depreciation expense. If, however, annual depreciation expense is significantly more or less than the anticipated capital outlays of the next period to be paid from working capital consideration should be given to adjusting the benchmark. An appropriate adjusted benchmark may be annual operating expenses – annual depreciation expense + capital outlays of the next period to be paid from working capital.
* Subject to the exception for heavily subsidized enterprises, described later in this Best Practice.

This best practice was previously titled Determining the Appropriate Levels of Working Capital in Enterprise Funds.

IV - Central Services Overhead Policy

- Background / Preliminary Recommendations (DRAFT)
- Board Policy 18.1.0
- Board Practice 18.2.0
- Best Practices / Guidelines

CENTRAL SERVICES OVERHEAD

Board Policy 18.1.0
Board Practice 18.2.0

Background

- Board Policy 18.1.0 relates to "Adoption of Central Services Cost Allocation Plan "
    - Establishes that cost allocation plan will be developed to determine billing rates on allowable costs of services provided by the General Fund to other departments, divisions and funds.
    - Establishes that the cost allocation plan will be reviewed annually during the budget process, and provides that the annual cost allocation plan will be filed with the Department of Taxation
    - Establishes that the related Practice (18.2.0) should specify: costs allowed, allocation method, and billing rates
- Board Practice 17.2.0 relates to "Central Services Cost Allocation Plan"
    - Identifies costs allowed, allocation method and billing rates
    - Costs to be determined in accordance with GAAP and approve by Board
    - Identifies costs that MAY be included
    - Allocation method provides that costs will be allocated to Enterprise Funds, and NOT to General Fund and Internal Service Funds
    - Allocations will be based on budget data (either statistic or amount)
    - Monthly billings will be charged based on budgeted amounts
    - June billings (accounting period 12) will be adjusted such that total charges for the fiscal year will not exceed actual costs

Best Practices and Resources

- GFOA, GASB provide guidance and best practices related to Central Services Cost Allocation plans, methodology and accounting practices
- NRS provides specific requirements related to application of Central Services Cost allocations to Enterprise Funds

Preliminary Recommendations

1) It is recommended that Board Policy 18.1.0 and Board Practice 18.2.0 be updated to include language related to:
    a. Basis for allocating costs (FTW, Personnel Costs, Operating Costs)

b. Accounting for charges to users of General Fund services (revenue or cost off-sets in General Fund)

2) Consideration should be given to transitioning from charging budgeted "amounts" each month versus use of "billing rates" (expressed as a central services overhead rate).

3) Need procedure to ensure that annual (or monthly) charges for central services do not exceed actual costs incurred.

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Budgeting and Fiscal Management
Adoption of Central Service Cost Allocation Plan
Policy 18.1.0

POLICY. The District will maintain practices in conformity with the Nevada Revised Statute Section 354.107 (Regulations) and 354.613(c) (Enterprise Funds Cost Allocation), including:

0.1 Central Service Cost Allocation Plan for accumulating, allocating and developing billing rates on allowable costs of services provided by the District's General Fund to departments, divisions and Funds.

0.2 This Policy and related Practice can only be modified by a non-consent agenda item during a regular meeting of the Board of Trustees.

The District's adopted other Financial Policies (6.1.0) that should be used to frame major practice initiatives and be summarized in the budget document. This Policy is specific to the equitable distribution of general, overhead, administrative and similar costs incurred by the District's General Fund in the process of supporting the operation of the District funds.

The underlying practice, along with any others that may be adopted for other financial purposes, will be reviewed during the budget process. The Finance and Accounting staff should review the practices to ensure continued relevance and to identify any gaps that should be addressed with new practices. The results of the review should be shared with the Board of Trustees during the review of the proposed budget. Each budget year, the current Central Service Cost Allocation Plan will be filed with the Nevada Department of Taxation as required.

Practice categories that should be considered for development, adoption and regular review are as follows:

0.1.1 Costs Allowed
0.1.2 Allocation Method
0.1.3 Billing rates for services provided

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GENERAL IMPROVEMENT DISTRICT
ONE DISTRICT – ONE TEAM

Budgeting and Fiscal Management
Central Service Cost Allocation Plan
Practice 18.2.0

RELEVANT POLICY: 18.1.0 Adoption of Central Service Cost Allocation Plan

1.0 COSTS ALLOWED

1.0.1 Costs will be determined in accordance with generally accepted accounting principles and approved by the Board of Trustees as part of the annual budget process, including any budget augmentation.

1.0.2 Costs incurred by a department, division or Fund specifically associated with their activities and operation will be Direct Costs to those departments, divisions or Funds.

1.0.3 Costs incurred for a common or joint purpose, benefitting more than one objective, will be considered Indirect Costs. These Indirect Costs must be necessary and reasonable for proper and efficient performance and administration.

1.0.4 Costs incurred may include, without limitation:

1.0.4.1 Legislative costs for the Board of Trustees
1.0.4.2 Legal Costs
1.0.4.3 General Administration
1.0.4.4 Emergency Services
1.0.4.5 Public Relations
1.0.4.6 Property Management
1.0.4.7 Grants Management
1.0.4.8 Contract, Procurement and Accounts Payable
1.0.4.9 Grounds and Building Maintenance
1.0.4.10 Budgeting, Accounting, Payroll and Audit
1.0.4.11 Human Resources and Risk Management
1.0.4.12 Information Technology and Communications
1.0.4.13 Warehouse and Storage

1.0.5 Applicable Credits

1.0.5.1 Applicable Credits will reduce the total costs allowed, when the credit relates directly to a transaction included in total costs.

1.0.6 Costs allowed should be deemed reasonable, ordinary and necessary for the operation of an Enterprise Fund.

2.0 ALLOCATION METHOD

2.0.1 The District's Proprietary Funds include both Enterprise and Internal Service Funds. The Internal Service Funds have and will continue to develop specific billing rates for services based on individual units of service to each department, division or Fund. Enterprise Funds will be billed an annual allocation of Indirect Costs Allowed, net of applicable credits, as evidenced by the adopted budget. The General Fund and Internal Service Funds be allocated a portion of these costs, but will not be billed, as it would only add a layer to recalculating their related rates and charges to the other funds.

2.0.2 The proportion of the allocation will be based on budget data in the form of statistics or amounts.

2.0.3 The basis of the allocation will be scheduled in support of current rates and be presented to the Board of Trustees in conjunction with establishing the Operating Budget for each fiscal year.

2.0.4 The Allocation Method for each Cost will be appropriate in relation to the cost's objective or measurement.

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ONE DISTRICT – ONE TEAM

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3.0 BILLING RATES

3.0.1 Monthly billings will be recorded and paid from the Enterprise Funds to the General Fund, based on a total as adopted with the District's Annual Operating Budget, including any Board approved amendments or budget augmentation.

3.0.2 The June billing each year, may be adjusted such that the total charges to the Enterprise Funds, for the fiscal year ending that respective June, does not exceed the actual allowed incurred costs net of actual applicable credits. The District may bill less than the budgeted total for a fiscal year, but in no case can the total billing exceed the total approved with the adoption of the District Annual Operating Budget for that fiscal year, including any Board approved amendments or budget augmentation.

3.0.3 Payment for billings will be considered completed by an entry in the general ledger for the District, through the Cash Clearing Fund, with appropriate amounts posted to the General Fund and the respective Enterprise Fund(s).

BEST PRACTICES

Indirect Cost Allocation

When considering the allocation of indirect costs, governments should consider: Who should perform the allocation?, What factors need to be considered if an external party is involved?, How often should an external cost allocation occur?, and What factors need to be considered if an allocation is performed internally?

In addition to the direct cost of providing services, governments also incur indirect costs. Such indirect costs include shared administrative expenses where a department or agency incurs costs for support that it provides to other departments/agencies (e.g., legal, finance, human resources, facilities, maintenance, technology). Certain important management objectives can be served by allocating these indirect costs (measuring the cost of government services, establishing fees and charges, charging back the cost of internal services to departments/agencies, and requesting reimbursements under federal and state grants, when allowed). Regardless of the purpose of an indirect cost allocation, a systematic and rational methodology should be used to calculate the amounts allocated.

The Government Finance Officers Association (GFOA) encourages governments to allocate their indirect costs. There are a number of issues a government needs to address in connection with indirect cost allocation. Because of the varied reasons for which indirect cost allocations are performed, a one-size-fits-all approach typically is not possible. Therefore, the GFOA recommends that governments considering the allocation of indirect costs consider the following:

1. *Who should perform the allocation?* An indirect cost allocation can be performed either by the government's own staff or by an external party. Specific factors that should be considered in choosing between the two include:

- In certain political environments, a government's constituents may be more accepting of an externally prepared cost allocation;
- The optimal choice may depend on the purpose of the cost allocation (for example, departmental chargebacks vs. grant reimbursement);
- Regardless of who prepares the cost allocation, management needs to be involved in the process and knowledgeable about the methodology used;

2. *What factors need to be considered if an external party is selected to perform the allocation?* If an external party is engaged to perform a cost allocation, the government should consider the following:

- The need for independence may prevent the financial statement auditor from serving in this role;
- The selected preparer should have knowledge and experience that is specifically relevant to the purpose for which the cost allocation will be used;
- The government should obtain ownership of the final work product;
- The government's staff should obtain at least a basic understanding of the process used to prepare the cost allocation;
- The contract for services with the preparer should state whether the preparer will assist in negotiating with a grant provider, if necessary, and which party (the government or the preparer) would be responsible for any indirect costs that are ultimately disallowed; and
- The government is responsible for having a system in place that ensures that data are appropriately classified in the accounting system.

3. *How often should an externally performed cost allocation take place?* An indirect cost allocation should be used for a maximum of three years (unless a law or regulation requires a shorter period). Moreover, an even shorter interval may be necessary based on the following considerations:

- Complexity of the calculation;
- Changes in grant requirements;
- Purpose for which the allocation is to be used1;
- Implementation of a new enterprise resource planning (ERP) system;
- A change in the government's administration; or
- A structural change in the government.

4. *What factors need to be considered if a cost allocation is to be performed by the government's own staff?* If in indirect cost allocation is to be performed by the government's own staff, a team approach normally is preferable. That team should consist of stakeholders from the government's departments/agencies and should have a designated team leader to make decisions when there are differing positions on the team and it is not possible to reach consensus. In addition:

- The internal staff that works on the project should have knowledge and experience that is specifically relevant to the purpose for which the indirect cost allocation will be used. Likewise, it is important that internal staff be aware of all applicable laws and regulations if the cost allocation is to be used as the basis for requesting reimbursement under a grant;
- The government should develop an educational process to ensure that the staff involved remain knowledgeable;
- Agencies/departments of the government should be responsible for using classifications that identify direct costs to the greatest extent possible to maximize the amount recovered from grant providers, when applicable (as should also be true for externally prepared cost allocations); and
- Data should be captured and documented contemporaneously to avoid audit problems that could otherwise arise as a result of subsequent data changes.

5. *Should the government use an indirect cost allocation plan or an overhead percentage rate?* There are pros and cons to using either an indirect cost allocation plan or an overhead percentage rate for recouping indirect costs, regardless of whether cost allocations are performed by an external party or by the government's own staff. Since an indirect cost allocation plan involves a greater level of detail and more complex calculations, a government should consider whether increased cost recovery from grantors would justify the extra effort.

Notes:

1 For example, a cost allocation used to chargeback costs to governmental departments/agencies may need to take place more frequently.

This best practice was previously titled Taking Advantage of Indirect Cost Allocations.