



## **City of Covington Financial Management Policies**

### **Purpose**

Good stewardship of public funds and assets is the hallmark of sound financial policies. The following policies provide the guidelines necessary to stay in legal compliance and meet the needs of the community both now and in the future.

#### **A. GENERAL BUDGET POLICIES**

- A-1 Department directors have primary responsibility for formulating budget proposals in line with City Council and City Manager priority direction, and for implementing, monitoring, and reporting them once they are approved.
- A-2 The Finance Department is responsible for coordinating the overall preparation and administration of the City's budget and Capital Investment Program Plan. This function is fulfilled in compliance with applicable State of Washington statutes governing local government budgeting practices.
- A-3 The Finance Department assists department staff in identifying budget problems, formulating solutions and alternatives, and implementing any necessary corrective actions.
- A-4 The City Council shall adopt the budget by ordinance at the fund level.
- A-5 Interfund charges will be based on recovery of the direct costs associated with providing those services.
- A-6 Regular employee positions will normally be budgeted only in the City's operating funds.
- A-7 Quarterly financial reports, including a review of budgeted expenditures and revenues, will be prepared and reported to the Council at regular meetings. Included will be provisions for amending the budget during the year in order to address unanticipated needs, emergencies, or compliance with State of Washington budgetary statutes. Budget adjustments requiring City Council approval will occur through a process coordinated by the Finance Department and will occur prior to fiscal year end.
- A-8 The Finance Department will review agenda items with potential fiscal impact submitted for City Council action. The objective of these reviews will be to ensure compliance with the budget and disclosure of all fiscal issues to the Council. This information will be presented in the fiscal impact section of each agenda bill.
- A-9 Revenues derived from fees associated with development will be designated for the support of the development activities in the Development Services Fund.
- A-10 The City's budget presentation will be directed at displaying the City's services plan in a Council/constituent-friendly format.

## A-11 Fund Balances

- a. It is essential that the City maintain adequate levels of unreserved fund balance to mitigate current and future risks and to ensure stable tax rates. As such, unreserved ending fund balances, excluding contingency and cumulative reserve funds, for the operating funds (General, Parks, Street, and Surface Water Management) will be required to have a minimum of 10% of operating expenditures in unreserved ending fund balance. All other funds, such as Development Services and Capital Investment, will be required to have a 15% minimum unreserved ending fund balance of expenditures.
  - b. It is the City's policy to maintain a Contingency Fund in accordance with RCW 35A.33.145. The reserve will be available for unforeseen, urgent, or emergency needs. The contingency reserve is intended to provide for unanticipated expenditures or revenue shortfalls of a non-recurring nature. The maximum allowable in the contingency reserve is 37.5 cents per thousand dollars of assessed valuation.
  - c. It is the City's policy to maintain a Cumulative Reserve Fund in accordance with RCW 35.21.070.
- A-12 The City will maintain equipment replacement funds that will receive annually budgeted contributions from the operating expenses of departments owning the capital equipment in an amount necessary to replace the equipment at the end of its useful life. Life cycle assumptions and required contributions will be reviewed annually as part of the budget process. Monies collected from the sale of assets carried on the equipment replacement schedules will be receipted to equipment replacement funds.
- A-13 Interfund loans will be permissible if practical. Interest rates will be computed based on a rolling 12-month average of the State Investment Pool earnings rate.
- A-14 Distinguished Budget Presentation: The City will seek to obtain the Government Finance Officers Association Distinguished Budget Presentation Award for each annual budget. The Budget will be presented in a way that clearly communicates the budget to members of the public.

## B. REVENUE POLICIES

The City shall be sensitive to the balance between the need for services and the City's ability to raise fees, charges, and taxes to support those services.

- B-1 The City should strive to maintain a diversified mix of revenues in order to maintain needed services during periods of declining economic activity.
- a. A base of property taxes and other stable revenues should be developed and maintained to provide a reliable base of revenues during periods of economic downturn.
  - b. The City's overall revenue structure should be designed to recapture for the City some of the financial benefits resulting from City economic and community development investments.
- B-2 The following factors will be considered when the City's taxes are increased, extended, changed, or reduced:
- a. Stability of the tax source over its expected life.
  - b. Suitability for a pledge against future debt, if that is part of the City Council's long-range intent for the new tax.
  - c. Spread the tax burden throughout the City's tax base by utilizing a broad array of the tax sources available and by investigating mitigation of inequities and hardships where appropriate (e.g., property tax rebates for low-income elderly). Legislative remedies for harmful tax impacts should be sought where appropriate.

- d. Apply the tax impact information for both residential and business taxpayers against a future vision of what the tax policy decision is intended to foster, in addition to the raising of revenues.
  
- B-3 As much as is reasonably possible, City services that provide private benefit should be supported by fees and charges in order to provide maximum flexibility in use of general City taxes to meet the cost of services of broader public benefit. Charges for services that benefit specific users should be fully recovered, including all direct and indirect costs including but not limited to, capital costs, department overhead, and Citywide overhead. Departments that impose fees or service charges should prepare and periodically update cost-of-service studies for such service. When consistent with legal requirements, other City interests such as remaining competitive within the region or meeting other City objectives, may dictate a subsidy of a portion of the costs of such services.
  
- B-4 Sales tax revenues are designed to support general government operations. As such, they will be allocated between the General Fund and the Parks Fund at a level to be determined during each budget cycle.
  
- B-5 All regular property tax revenues will be allocated to support General Fund services unless there is a ballot measure approved by the voters that directs a certain amount of the property tax capacity be used for other City services.
  
- B-6 Revenue estimates should be prepared on a conservative basis to minimize the economic fluctuations that could imperil ongoing service programs during the upcoming budget cycle. Revenue increases greater than inflation will require additional documentation. Major revenue sources will require explanation.
  
- B-7 The Surface Water Management Fund will be reviewed annually and it must have a rate structure adequate to meet its operations and maintenance and long-term capital requirements.
  
- B-8 Rate increases should be small and applied frequently to avoid an overly burdensome future increase.

### **C. OPERATING POLICIES**

- C-1 Ongoing resources should be equal to or exceed ongoing expenditures. Each City fund budget shall identify ongoing resources that at least match expected ongoing annual requirements. One-time cash transfers and non-recurring ending fund balances will be applied to reserves or to fund one-time expenditures; they will not be used to fund ongoing programs.
  
- C-2 Unless otherwise stated explicitly by the City Council, the City will not earmark unrestricted revenues for specific purposes in the General Fund. This will preserve the ability of the Council to determine the best use of available revenues to meet changing service requirements.
  
- C-3 The City will seek to optimize the efficiency and effectiveness of its services to reduce costs and improve service quality.
  
- C-4 Accurate inventories of all physical assets, their condition, life span, and cost will be maintained. (refer to section K. Fixed Assets)
  
- C-5 The Finance Department will develop, maintain, and constantly seek to improve cash management systems which ensure the accurate and timely accounting, investment, and security of all cash assets. All cash received by City departments will be deposited the same business day. The Finance Director has oversight and final authority over cash handling policies and procedures.

## **D. PURCHASING AND EXPENDITURE CONTROL**

- D-1 It is the general policy of the City that all expenditures be rationally related to some public purpose and is reasonable in the amount and nature.
- D-2 Primary responsibility and authority for the expenditure of monies according to the adopted budget will be vested by the City Manager in the department heads.
- D-3 In addition to the primary responsibilities in Policy A-1, the Finance Director will exercise a secondary oversight responsibility for ALL budget expenditures. This includes responsibility for both technical errors and errors of judgment, which should be brought immediately to the attention of the responsible department head and the City Manager. However, unilateral changes may be made in line item expenditures by the Finance Director if deemed necessary in order to expedite the accounts payable process.
- D-4 All purchase orders and/or invoices will be signed by the responsible department head or his/her designee (or City Manager), and reviewed by the appropriate personnel in Finance for budget authority and proper coding.
- D-5 Invoices for the costs of public utilities, telephone, postage, copy machine expenses, and others shared by more than one department will be reviewed and approved by the Finance Director or his/her designee.
- D-6 All expenditures/expenses shall be pre-audited and certified by the Finance Director or his/her designee prior to submitting them to the City Council.
- D-7 The accounts payable process will occur every other week opposite payroll. City Council approval will occur at the following Council meeting. The execution of checks in advance of City Council approval will occur under the following condition:
- Members of the City Council's Finance Committee will review and approve the supporting documentation of such disbursement before the next regularly scheduled meeting.
- If the City Council at the subsequent Council meeting (after review), disapproves any such checks, the disapproved claims will be recognized as a receivable of the City and collections of said receivable will be diligently pursued until the amounts disapproved are collected or until the Council is satisfied and approves the claims.
- D-8 All significant purchases should be made only after an effort to compare prices and alternatives from more than one vendor (see [Resolution 06-36](#)).
- D-9 Credit cards may be issued to the City Manager, Department Heads, and employees for travel and other business related expenses. (see Ordinance 03-06)
- D-10 Non-employees such as volunteers are required to get prior authorization from staff before making purchases.

## **E. CONTRACT MANAGEMENT**

- E-1 When a project is presented to the Council for consideration, a preliminary budget estimate will be included. This estimate will show separate costs for the various phases of the project, including preliminary design, construction, and administration costs. Preliminary budget estimates may also provide for additional contract cost contingencies with the amount dependent upon the type of project and degree of uncertainties. When the Council approves a project they are also authorizing the budget in each contract category including the contingencies budget.
- E-2 Prior to formal bidding for construction services, an engineer's estimate will be approved by the Council. Once the bids are opened, a revised budget may be brought back to the Council for

approval, with the request to award the bid. When the Council awards the bid, it will also approve a revised budget or confirm the original budget as it finds to be in the best interest of the City.

- E-3 When awarding professional service contracts the Council will authorize the City Manager to enter into a contract for a written scope-of-work on a cost plus basis with a stated "not-to-exceed" contract total cost. The dollar total will be broken down by major tasks, including a contingency budget if necessary.
- E-4 The City will comply with RCW 39.80.010 when negotiating contracts for architectural and engineering services.
- E-5 Professional service contracts may be authorized with a single consultant for several phases of work on the same project. The contract may be approved by Council, and subsequent phases may be authorized by the Council in the form of contract amendments.
- E-6 The Public Works Director will have the authority to authorize payments up to the total contract only. If the scope-of-work does not change and the total cost is not violated, different amounts may be spent among the tasks within project budget categories. Changes in either the scope-of-work or the authorized budget shall be approved by the City Council as an amendment to the original contract.
- E-7 After the award of contract only the City Manager or his/her designee will have the authority to approve change orders per the [purchasing policy](#). The process for handling change orders will be spelled out in the construction contract.
- E-8 The City Manager will report all change orders to the City Council including the dollar amount.
- E-9 Any proposed change orders that exceed the budget amount will be submitted to Council for approval.
- E-10 All contract and lease agreements will be reviewed by the Finance Director and City Attorney prior to final approval.

## **F. GENERAL LEDGER ACCOUNTS**

- F-1 A Petty Cash Fund is hereby authorized from the General Fund in the amount of \$500 for minor disbursements. It will be periodically restored by a check drawn and charged to applicable accounts. The amount of the check should equal the aggregate of the disbursements.

Petty Cash purchases are limited to expenditures of \$50 or less, and shall be approved by the appropriate Department Head or his/her designee, using a Petty Cash Request Form, prior to receipt of cash.

Individuals receiving Petty Cash shall immediately return to the Finance Department the receipt, any change due, and sign a verifying receipt of cash.

The Finance Director will delegate the custodian of the Petty Cash, and this individual will be independent of cashiering and check signing duties.

The Petty Cash Fund will be periodically audited by a person other than the custodian, usually the Finance Director or his/her designee

- F-2 New revenue and expenditure accounts can only be authorized by the Finance Director or his/her designee and will only be set up if it's in the best interest of the accounting system. Finance will limit the number of new accounts.

## G. DEBT POLICY

### Background

The City of Covington (City) maintains conservative financial policies to assure strong financial health both in the short- and long-term. The City is an infrequent issuer of debt with debt primarily used as a tool to finance large capital investments.

Achieving and maintaining a solid bond rating is an important objective of the City's financial policies. To this end, the City is constantly working to improve its financial policies, budgets, forecasts, and financial health.

### Purpose

This policy sets forth the criteria for issuance and repayment of debt. The primary objective of the Debt Policy is to establish criteria that will protect the City's financial integrity while providing a funding mechanism to meet the City's capital needs. All debt issued will be in compliance with this policy, Chapter 35A.40 Revised Code of Washington (RCW) - Fiscal Provisions Applicable to Code Cities and Chapter 43.80 RCW - Fiscal Agencies along with all other City, State, and Federal laws, rules, and regulations.

### Scope

This Policy provides general guidance for the issuance and management of all City debt.

### Responsibility

Authority to issue and manage debt is derived from titles 35 and 35A RCW (including without limitation RCW 35A.40.080-.090, chapter 35.37 RCW and chapter 35.41 RCW). This section gives the Finance Director authority to act in the capacity of City Treasurer, which includes the duties of debt management.

The Finance Director is responsible for assuring that the activities related to the issuance and payment of bonds or other obligations not jeopardize the bond rating.

#### G-1 Budgeting and Capital Planning

The City shall develop and maintain a capital planning process such as the annual Capital Investment Program for consideration and adoption by the City Council as part of the City's budget process. The Finance Department is responsible for coordinating and analyzing the debt requirements. This will include timing of debt, calculation of outstanding debt, debt limitation calculations and compliance, impact on future debt burdens, and current revenue requirements.

Prior to issuance of debt, the City will prepare revenue projections, such as the annual budget or the Financial Forecast, to ensure that there is adequate revenue to make principal and interest payments.

#### G-2 Types of Long-Term Debt

The following is a description of the types of long-term debt the City may issue:

##### 1. General Obligation

This debt is backed by the full faith and credit of the City. State law limits this debt to 2.5% of the value of taxable property within the City for each of three purposes:

###### A. General Purposes

Debt issued in this category can be used for any purpose allowed by law.

#### Non-Voted

The City Council may authorize the issuance of general obligation debt up to 1.5% of the City's assessed value without a vote of the public as long as there is an available source of funding to pay the debt service. This funding source can be the diversion of an existing revenue source or a new revenue coming from the enactment of a new tax or other revenue source. The debt can take the form of bonds, lease-purchase agreements, conditional sales contracts, certificates of participation, or other forms of installment debt.

#### Voted

The City Council may place any general obligation debt issue before the electorate. According to State law, if a debt issue is placed before the City's electorate, it must receive a 60% or greater yes vote and have a turnout of at least 40% of those voting at the previous general election. Voted issues are limited to capital purposes only.

#### B. Open Space and Parks

Debt issued in this category must be used for park and open space and/or recreation facilities. All debt in this category must be approved by the voters, and if so approved, the City is provided with an additional amount of debt capacity up to 2.5% of the value of taxable property within the City.

#### C. Local Option Capital Asset Lending (LOCAL) Program Debt

The City Council may authorize a financing contract with the Office of the State Treasurer under chapter 39.94 RCW. LOCAL borrowings count against the City's non-voted debt limit.

### 2. Revenue Debt

Revenue bonds are generally payable from a designated source of revenue generated by the project which was financed. No taxing power or general fund pledge is provided as security. Unlike general obligation bonds, revenue bonds are not subject to constitutional or statutory debt limitations nor is voter approval required.

### 3. Local Improvement District (LID) Debt

LID bonds are payable solely from assessments of property owners within the local improvement district. Similar to revenue debt, no taxing power or general fund pledge is provided as security, and LID bonds are not subject to statutory debt limitations.

The debt is backed by the value of the property within the district and an LID Guaranty Fund. The LID Guaranty Fund is required by State law.

Assessment Debt (LID) is preferred to General Debt to fund improvements that specially benefit specific properties

### G-3 Short-Term Debt and Interim Financing

The City may utilize short-term borrowing in anticipation of long-term bond issuance or to fund cash flow needs in anticipation of tax or other revenue sources.

The Finance Director is authorized to make loans from one City fund to another City fund for periods not exceeding three months. The Finance Director or designee is required to assure that the lending fund will have adequate cash balances to continue to meet current expenses after the loan is made and until repayment from the receiving fund.

## Interim Financing of Major Capital Projects

Interim financing of major capital projects may be arranged by Bond Anticipation Notes (BANS), interfund loans, or lines of credit with a major financial institution.

a. General Guidelines:

1. To the extent possible the City will utilize interfund loans for interim financing of capital projects, either in whole or in part. Interfund loans provide the lowest borrowing cost to the City as the interest expense to the borrowing fund is offset by interest income to the lending fund. Available funds consist of cash, State Investment Pool balances or other relatively liquid investments. The decision to sell long-term investments to provide funds for interfund loans will be made by the City Council based on applicable policies.
2. The decision to use the City's line of credit or the issuance of BANS should employ a cost/cash flow analysis comparing the two financing options. The administrative costs for bond counsel, underwriter and other fees will be taken into account for the costs of BANS. Other factors impacting the decision, such as the capacity of the line of credit, the timing of issuing permanent financing for paying down the line of credit prior to its maturity date, anticipated interest rate changes and arbitrage regulations will also be considered.

b. Line of Credit: If a line of credit is used the following policies will apply:

1. The line of credit is restricted to use for interim financing of capital projects for which long term-bonds are expected to be issued within two years of adoption of the ordinance or for which reimbursable grant monies are expected.
2. Upon sale of bonds for permanent financing of a project or receipt of grant funds, such funds will be used to immediately pay off the amount of the line of credit utilized by each project, including interest charged for use of the line of credit.
3. Each authorization of the line of credit will identify the particular project eligible and contain a specific not-to-exceed amount for each project.
4. Use of the line of credit for normal operating expenditures is prohibited.
5. The outstanding general obligation line of credit amount in conjunction with the City's other general obligations may not at anytime exceed the City's statutory debt limit.

c. Bond Anticipation Notes (Bond Anticipation Notes). If BANS are used the following policies will apply:

1. The BANS will have a maximum maturity of two years from their issue date.
2. BANS can only be issued after a formally adopted bond ordinance by City Council.
3. The bond ordinance for the BANS will set a specific principal amount and identify the specific project(s) for which the proceeds are to be used.
4. Bond counsel charges, underwriter fees and other issuance costs may be included and paid from the BAN proceeds.
5. BANS will be subordinate to any outstanding bonds of the City.

d. Tax Anticipation Notes (TANs). If TANs are used the following policies will apply:

1. TANs will be used only where there is a significant misalignment between the timing of City tax receipts and City cash needs.
  2. TANs will be structured to conform to federal tax requirements, i.e. no longer than 13 month maturities and state law where they must mature within six months after the end of the fiscal year in which the TANs are issued.
- e. Grant Anticipation Notes (GANs) If GANs are used the following policies will apply:
1. GANs will be used only to assist with City cash flow needs on projects and programs where federal and/or state grants have been committed, but where there is a lag between City expenditures and reimbursement but the granting agency.
  2. GANs will be structured to conform to federal tax requirements.
- f. If an interfund loan is used the following policies will apply.
1. Interfund loans may only be made upon formal adoption of a resolution by the City Council.
  2. The resolution for the interfund loan will set forth the term and amount of the loan, a schedule of repayment including interest; and set a current market rate of interest for loans of similar maturity and amount.
  3. Interfund loans for interim financing of major capital projects made in anticipation of the issuance of long term bonds shall be repaid in full (including accrued interest) upon receipt of the bond proceeds.

The loaning fund shall have adequate funds to make the loan and to meet its anticipated operating needs over the life of the loan.

**G-4 Limitation of Indebtedness**

In addition to the limitations required by the RCW, the City's indebtedness is further limited by this policy to assure strong financial health. The limitations are applied to the assessed value of the City to arrive at a dollar value of indebtedness. For example, the 2005 assessed valuation used to determine the 2006 property tax levy was \$1.5 billion, and the statutory limitation for general obligation debt is 2.5%. Therefore, the City's statutory debt limitation is \$37.5 million. The following matrix shows the general limitation by type of debt. These limitations may be modified by the City Council up to the statutory limitation at the Council's discretion.

Type of Debt	Statutory Limitations	Policy Limitations	2006 Covington Actual
General Obligation:	2.5%	2.5%	0.0%
General Purpose			
Non-Voted	1.5%	1.5%	0.0%
Voted	1.0%	1.00%	0.0%
Parks, Open Space and Economic Development	2.5%	1.75%	0.0%
Utilities	2.5%	1.75%	0.0%
Revenue	no limit	no limit *	NA
Local Improvement District	no limit	no-limit *	NA

\* Revenue and LID debt is not limited because no taxing power or general fund pledge is provided as security.

G-5 Structure and Term of Debt

1. Debt Repayment

The City shall pay all interest and repay all debt in accordance with the terms of the bond ordinance. The maturity of bonds issued should be the same or less than the expected life of the applicable project for which the bonds were issued. To the extent possible, the City will seek level or declining debt repayment schedules.

2. Variable-Rate Securities

When appropriate, the City may choose to issue securities that pay a rate of interest that varies according to a pre-determined formula or results from a periodic remarketing of the securities. However, other than for short-term lines of credit and BANS, the City will avoid over use of variable-rate debt due to the potential volatility of such instruments

G-6 Professional Services

The City's Finance Department shall be responsible for the solicitation and selection of professional services that are required to administer the City's debt program.

1. Bond Counsel

All debt issued by the City will include a written opinion by bond counsel affirming that the City is authorized to issue the proposed debt. The opinion shall include confirmation that the City has met all city and state constitutional and statutory requirements necessary for issuance, a determination of the proposed debt's federal income tax status and any other components necessary for the proposed debt. The City's Finance Department shall be responsible for the solicitation and selection of professional services that are required to administer the City's debt program

2. Financial Advisor

A Financial Advisor(s) will be used to assist in the issuance of the City's debt. The Financial Advisor will provide the City with objective advice and analysis on debt issuance. This includes, but is not limited to, monitoring market opportunities, structuring and pricing debt, and preparing official statements of disclosure.

3. Underwriters

An Underwriter(s) will be used for all debt issued in a negotiated or private placement sale method. The Underwriter is responsible for purchasing negotiated or private placement debt and reselling the debt to investors.

4. Fiscal Agent

A Fiscal Agent will be used to provide accurate and timely securities processing and timely payment to bondholders. In accordance with Chapter 43.80 RCW, the City will use the Fiscal Agent that is appointed by the State.

G-7 Method of Sale

Presumption of Competitive Sale — The City will generally issue its debt through a competitive process but may use a negotiated process under the following conditions:

- The bond issue is, or contains, a refinancing that is dependent on market/interest rate timing.
- At the time of issuance, the interest rate environment or economic factors that affect the bond issue are volatile.

- The nature of the debt is unique and requires particular skills from the underwriter(s) involved.
- The debt issued is bound by a compressed time line due to extenuating circumstances such that time is of the essence and a competitive process cannot be accomplished.

Competitive Bid Method — any competitive sale of the City of Covington debt will require approval of the City Council. City of Covington debt issued on a competitive bid basis will be sold to the bidder proposing the lowest true interest cost (TIC) to the City. Such bid may take the form of hand-delivered or electronically transmitted offers to purchase the bonds.

Negotiated Bid Method — when deemed appropriate to minimize the costs and risks of the City of Covington’s debt issue, the Finance Director will submit to the City Council a request to sell the debt issue on a negotiated basis. If debt is sold on a negotiated basis, the negotiations of terms and conditions shall include, but not be limited to, prices, interest rates, underwriting or remarking fees and commissions.

The City of Covington, with assistance of its Financial Advisor, shall evaluate the terms offered by the underwriting team. Evaluations of prices, interest rates, fees and commissions shall include prevailing terms and conditions in the marketplace for comparable issuers.

The City of Covington shall, with assistance of its Financial Advisor, oversee the bond allocation process. The bond allocation process shall be managed by the lead underwriter, with the following requirements:

- ✓ The bonds are allocated fairly among members of the underwriting team, consistent with the previously negotiated terms and conditions;
- ✓ The allocation process complies with all Municipal Securities Rulemaking Board regulations governing order priorities and allocations; and
- ✓ The lead underwriter shall submit to the Finance Director a complete and timely account of all orders, allocations, and underwriting activities.

The Finance Director shall require a post-sale analysis and reporting for each negotiated bond sale. The independent Financial Advisor shall perform such analysis and provide a final pricing book by the day of the closing. A post-sale analysis will include, but not be limited to:

- ✓ Summary of the pricing, including copies of the actual pricing wires;
- ✓ Results of comparable bond sales in the market at the time of the City’s pricing;
- ✓ Detailed information on a) orders and allocation of bonds, by underwriting firm, b) detailed information on final designations earned by each underwriter, and c) a summary of total compensation received by each underwriter; and
- ✓ Historic comparisons to Municipal Market Data indexes — day of sale basis.

No debt issue will be sold on a negotiated basis without an independent Financial Advisor.

#### G-8 Credit Ratings

The City will maintain good communication with bond rating agencies about its financial condition. This effort will include providing periodic updates on the City’s general financial condition, coordinating meetings, and presentations in conjunction with a new issuance. The City will continually strive to maintain its bond rating by improving financial policies, budgets, forecasts and the financial health of the City.

Credit enhancements may be used to improve or establish a credit rating on a City debt obligation. Credit enhancements should only be used if cost effective.

#### G-9 Refunding Debt

A debt refunding is a refinance of debt typically done to take advantage of lower interest rates.

Unless otherwise justified, such as a desire to remove or change a bond covenant, a debt refunding will require a present value savings of three percent of the principal amount of the refunding debt being issued.

G-10 Arbitrage Rebate Monitoring and Reporting

The City will, unless otherwise justified, use bond proceeds within the established time frame pursuant to the bond ordinance, contract, or other documents to avoid arbitrage. Arbitrage is the interest earned on the investment of the bond proceeds above the interest paid on the debt. If arbitrage occurs, the City will pay the amount of the arbitrage to the Federal Government as required by Internal Revenue Service Regulation 1.148-11.

The Finance Director shall, when deemed necessary or when required, procure the services of an arbitrage rebate calculation firm. The purpose of the arbitrage rebate calculation firm is to provide arbitrage rebate compliance services in accordance with the Internal Revenue Code of 1986, as amended ("Code").

The City will maintain a system of recordkeeping and reporting to meet the arbitrage rebate compliance requirement of the IRS regulation. For each bond issue not used within the established time frame, the recordkeeping shall include tracking investment earnings on bond proceeds, calculating rebate payments, and remitting any rebatable earnings to the federal government in a timely manner in order to preserve the tax-exempt status of the outstanding debt.

G-11 Covenant Compliance

The City will comply with all covenants stated in the bond ordinance, contract, etc.

G-12 Ongoing Disclosure

The Finance Director shall be responsible for providing annual disclosure information to established national information repositories and for maintaining compliance with disclosure statements as required by state and national regulatory bodies. Disclosure required by the Securities & Exchange Commission shall occur by the date designated in the bond ordinance, which is currently July 31 of each year. Disclosure shall take the form of the Comprehensive Annual Financial Report (CAFR) unless information is required by a particular bond issue that is not reasonably contained within the CAFR.

G-13 Structural Elements

**Maturity** — The City of Covington shall issue debt with an average life less than or equal to the average life of the assets being financed. Unless otherwise stated in law, the final maturity of the debt shall be no longer than 40 years (RCW 39.46.110).

**Debt Service Structure** — unless otherwise justified and deemed necessary, debt service should be structured on a level basis. Refunding bonds should be structured to produce equal savings by fiscal year. Unless otherwise justified and deemed necessary, debt shall not have capitalized interest. If appropriate, debt service reserve funds may be used for revenue bonds.

**Maturity Structure** — the City of Covington's long-term debt may include serial and term bonds. Unless otherwise justified, term bonds should be sold with mandatory sinking fund requirements.

**Price Structure** — the City of Covington's long-term debt may include par, discount, and premium bonds. Discount and premium bonds must be demonstrated to be advantageous relative to par bond structures, given applicable market conditions,

**Coupon Type**— unless otherwise justified and deemed necessary, long-term debt will be sold using current interest coupons. If justified and deemed necessary, capital appreciation bonds (zero coupon bonds) may be issued.

Redemption Features — for each transaction, the City of Covington shall evaluate the costs and benefits of call provisions.

Bond Insurance — for each transaction, the City of Covington shall evaluate the costs and benefits of bond insurance or other credit enhancements. Any credit enhancement purchases by the City of Covington shall be competitively procured.

Tax-exemption - Unless otherwise justified and deemed necessary, the City of Covington shall issue its debt on a tax-exempt basis.

G-14 Pledge of revenues — The City of Covington's pledge of revenues shall be determined for each debt issue depending upon the debt instrument:

- ✓ **Unlimited Tax General Obligation Bonds:** Unlimited Tax General Obligation Bonds of the City of Covington shall be repaid from voter- approved excess property taxes on property within the jurisdiction of the City of Covington.
- ✓ **Limited Tax General Obligation Bonds:** Limited Tax General Obligation Bonds of the City of Covington shall be repaid from regular property taxes on property within the jurisdiction of the City of Covington, together with other legally available sources such as sales tax, real estate excise tax, or reserve funds.
- ✓ **Revenue Bonds:** Revenue Bonds of the City of Covington shall be repaid from specified revenues, as defined in the authorizing ordinance.
- ✓ **Special Assessment Bonds:** Special Assessment Bonds of the City of Covington shall be repaid from assessments collected from within a special assessment district formed by the City of Covington pursuant to applicable law.
- ✓ **Local Option Capital Asset Lending (LOCAL) Program Debt:** (LOCAL) Program Debt of the City of Covington shall be repaid from property taxes on property within the jurisdiction of the City of Covington, together with other legally available sources.
- ✓ **Other Debt Instruments [if applicable]:** Other Debt Instruments of the City of Covington shall be repaid from revenues, as defined in the authorizing ordinance

G-15 Rating Agencies

The Finance Department shall manage relationships with the rating analysts assigned to the City of Covington's credit, using both informal and formal methods to disseminate information. Communication with the rating agencies shall include:

- ✓ Full disclosure, on an annual basis, of the financial condition of the City of Covington;
- ✓ A formal presentation, on a regular basis, to the rating agencies, covering economic, financial, operational and other issues that impact the City of Covington's credit;
- ✓ Timely disclosure of any financial events that may impact the City of Covington's credit;
- ✓ Timely dissemination of the Annual Financial Report, following its completion; and
- ✓ Complete and timely distribution of any documents pertaining to the sale of bonds.

Credit Objective - The City of Covington shall seek to maintain and improve its credit rating.

#### Bond Insurers

The Finance Director shall manage relationships with the analysts at the bond insurers assigned to the City of Covington's credit, using both informal and formal methods to disseminate information.

G-16 Investment of Proceeds

General — The City of Covington shall comply with all applicable Federal, State, and contractual restrictions regarding the investment of bond proceeds, including City of Covington's Investment Policy. This includes compliance with restrictions on the types of investment securities allowed, restrictions on the allowable yield of some invested funds as well as restrictions on the Time

period over which some bond proceeds may be invested.

Refunding Escrow – Unless otherwise justified and deemed necessary City of Covington shall utilize State and Local Government Series (SLGS) for the refunding escrow. SLGS are special series of U.S. Treasury securities.

If open markets securities are deemed appropriate the City of Covington shall in consultation with bond counsel comply with each of the following:

- a) Make a bona fide solicitation for securities and, of the bids received, at least three are bona fide bids from sellers that have no involvement in the pricing of the issue; and
- b) Purchase securities from the bidder which made the highest yielding bid and such securities have a yield at least as high as such bid.

G-17 Bond Users Clearinghouse

The City of Covington shall ensure that the Bond Users Clearinghouse receives municipal bond information for all debt sold as provided by Chapters 39.44.200 through 39.44.240 RCW and Chapter 365-130 WAG. The information requested by RCW 39.44.210 includes but is not limited to:

- ✓ the par value of the bond issue;
- ✓ the effective interest rates;
- ✓ a schedule of maturities;
- ✓ the purposes of the bond issue;
- ✓ cost of issuance information; and
- ✓ the type of bonds that are issued.

G-18 Legal Covenants

The City of Covington shall comply with all covenants and conditions contained in governing law and any legal documents entered into at the time of a bond offering.

G-19 Refunding Savings Thresholds

Refundings will be conducted in accordance with the Refunding Bond Act, chapter 3953 RCW. Unless otherwise justified, City of Covington will refinance debt to achieve true savings as market opportunities arise.

Unless otherwise justified, an “advance refunding” transaction will require a present value savings of five percent of the principal amount of the refunding debt being issued.

Unless otherwise justified, a “current refunding” transaction will require graduated present value savings as follows:

Years Between Call and Final Redemption	Present Value Standard
1-2 years	1%
3-4 years	2%
5-6 years	3%
7-8 years	4%
9+ years	5%

Selection of maturities to be refunded — unless otherwise justified, all callable maturities of an issue will be included in a refunding.

G-20 Derivative Products

No derivative products will be utilized unless permitted by law, and not without prior City Council approval. No derivative products shall be utilized without an analysis by an independent financial advisor. No derivative products shall be used for the purpose of interest rate speculation.

G-21 Alternative Financings Schemes

The City of Covington shall not utilize alternative financing schemes to avoid restrictions imposed by law or to utilize tax loop-holes.

G-22 Evaluating Capital Improvement Program Spending

The City of Covington shall integrate its debt issuance with its Capital Improvement Program spending.

G-23 Modeling the Impact of Capital Program Needs

The City of Covington shall develop and maintain a capital finance model to evaluate the impact of capital program spending, operations and maintenance costs, and debt service on its financial condition. To that end, the Finance Department shall oversee the ongoing maintenance of quantitative modeling that includes, but is not limited to, the following:

- ✓ Historic and projected cash flows for capital and operating expenditures;
- ✓ Historic and projected fund balances;
- ✓ Historic and projected debt service coverage; and
- ✓ Projected revenue requirements.

G-24 Debt Database Management

The City of Covington shall maintain complete information on its outstanding debt portfolio, in a database format. The information in the database shall include, but not be limited to, the following:

- ✓ Issue Name
- ✓ Initial Par Amount of the Issue
- ✓ Dated Date and Sale Date of the Issue
- ✓ Purpose of the Issue
- ✓ Security Type (Fixed or Variable) of the Issue
- ✓ Issue Type (New Money or Refunding) of the Issue
- ✓ Sale type (Competitive or Negotiated) of the Issue
- ✓ TIC, Arbitrage Yield, Avg. Life, and Underwriters Discount of the Issue
- ✓ Underwriter(s) of the Issue
- ✓ Principal Amounts by Maturity
- ✓ Principal Amounts Outstanding by Maturity
- ✓ Coupon Rate and Coupon Type (Current Interest or Zeros) by Maturity
- ✓ Original Yield and Original Price by Maturity
- ✓ Interest Payment Frequency by Maturity
- ✓ First Interest Payment Date by Maturity
- ✓ Call Provisions by Maturity
- ✓ Sinking Provisions by Maturity
- ✓ Credit Enhancement, if any, by Maturity

The City of Covington shall use the debt database for the following purposes:

- ✓ Generate reports;
- ✓ Refunding Analyses; and
- ✓ Output to Fund Accounting System.

G-25 Accounting for the Issuance of Debt

The City of Covington shall account for the issuance of debt using general accepted accounting principals ("GAAP") as established by the Governmental Accounting Standards Board ("GASB"). Cost of issuance shall be reported as an expenditure rather than netted against proceeds.

G-26 Debt Policy Review

The City of Covington shall review and update its debt policy every four years.

## H. INVESTMENT

H-1 The City's primary objective is to manage its total cash and cash equivalent assets in a manner that conforms completely to the constraints of this policy while maximizing the interest earnings of the portfolio. This will be done in a manner that supports the government's primary purpose of providing services to its citizens.

The primary purpose in determining a strategy for the City of Covington's investment activities is as follows:

Legality: The City's investments will be in compliance with all statutes governing the investment of public funds. This includes the Revised Code of Washington, the BARS manual, this investment policy and corresponding administrative procedures.

Safety: Safety of principal is of primary importance to the City. Investments of the City will be undertaken in a manner that seeks to guard the preservation of capital in the overall portfolio. To attain this objective, diversification is required in order that potential losses on individual securities do not exceed the income generated from other investments.

Liquidity: The City's investments will remain sufficiently liquid to facilitate the City's need to meet all operating and debt requirements which might be reasonably anticipated.

Yield: The City's investments will be established with the objective of achieving a market rate of return throughout budgetary and economic cycles, taking into account the City's investment risk constraints and cash flow characteristics of the portfolio.

H-2 The City has also determined to limit investment purchases to the following investment types, which the City has determined best meet their overall investment strategy. This authorization applies to all City funds.

- a.) Investment deposits, including certificates of deposit, with qualified public depositories as defined in Chapter 39.58 RCW.
- b.) Certificates, notes, or bonds of the United States, or other obligations of the United States or its agencies, or of any corporation wholly owned by the government of the United States (such as the Government National Mortgage Association). However, this authorization will specifically exclude Collateralized Mortgage Obligations (CMOs), Real Estate Mortgage Investment Conduits (REMICs), and other Principal Only (POs) and Interest Only (IOs) obligations that are secured with mortgages issued by any federal agency, instrumentality or private firm.
- c.) Obligations of government-sponsored corporations which are eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System. (These include but are not limited to Federal Home Loan Bank notes and bonds, Federal Farm Credit Bank consolidated notes and bonds, Federal National Mortgage Association notes, debentures, and guaranteed certificates of participation.)
- d.) Washington State Local Government Investment Pool.

- e.) Bonds of the State of Washington and any local government in the State provided they carry a current debt rating in the top three categories of a nationally recognized rating agency at the time of investment.
  - f.) Prime Banker's Acceptances purchased on the secondary market with ratings of A1/P1 by a nationally recognized rating agency.
  - g.) Repurchase agreements for securities listed above, provided that the transaction is structured so that the City of Covington obtains control over the underlying securities and a Master Repurchase Agreement has been signed with the bank or dealer. Collateralization will be required on all repurchase agreements at a level of 102% of the market value of principal and accrued interest. This is to anticipate any market changes and to provide an adequate level of security for all funds. Collateral is limited to the types of investments detailed in this section.
- H-3 The Finance Director will consider all investments as common investments whose ownership is derived from each participating fund. Interest earned by the common investment portfolio will be applied in its entirety to each participating fund on the basis of its available cash balance. Unless specified by the Finance Director, all cash and cash equivalent assets of every fund will be considered available for investment. The only exception to the common investment portfolio will be investments made from the proceeds of bond sales and only to the extent necessary to provide a separate accounting of investment activity.
- H-4 Funds set aside to satisfy City debt in conjunction with an advance refunding agreement will be invested in accordance with appropriate bond documents and not necessarily in compliance with this policy. If bond covenants are more restrictive than this policy, funds will be invested in full compliance with those additional restrictions.
- H-5 All investments of the City of Covington shall be made in compliance with Federal and State law and in accordance with those legal interpretations that apply. The investment of any tax-exempt borrowing proceeds and of any debt service funds shall comply with the 1986 Tax Reform Act if that Act applies to the debt issued.
- H-6 The Finance Director is the investment officer of the City. The Finance Director will develop written procedures for the operation of the investment program consistent with this investment policy and approved by the City Manager. These procedures will include a detailed delegation of authority to persons responsible for investment transactions. The Finance Director will be responsible for all transactions undertaken and will establish a system of controls to regulate the activities of subordinate employees. The Finance Director will ensure a periodic independent annual review of investment activities and internal controls are performed by the external-auditing agency.
- H-7 The City Manager will provide investment oversight to the Finance Director. The Finance Director will report investment activity monthly to the City Manager and semi-annually to the City Council. The City Council will amend the Investment Policy, as needed, by Resolution.
- H-8 Investments will be made with judgment and care, in consideration of the circumstances then prevailing, which person(s) of prudence, discretion and intelligence would exercise in the management of their own affairs for investment purposes, not for speculation, taking into account the probable safety of their capital as well as the probable income expected to be derived.
- H-9 Officers and employees involved in the investment process will refrain from personal business activity that could conflict with the proper execution of the investment program or impair their ability to make impartial investment decisions. Employees and investment officials will disclose to the City Council any substantive financial interest in financial institutions that conduct business within this jurisdiction. They will also disclose any material personal financial or investment positions that could be related to the performance of the City's portfolio. Employees and Officers will subordinate their personal investment transactions to those of the City of Covington, particularly in regard to the timing of purchases and sales.

- H-10 The Finance Director will conduct investment transactions with several competing, reputable investment securities broker/dealers. A list will be maintained of approved security broker/dealers selected for their credit worthiness, industry reputation, knowledge of public sector investment practices, and who maintain an office in the State of Washington. The Finance Director has the authority to remove any broker/dealer from the list, with or without cause by written notice. Broker/dealers may appeal the Finance Director's action by written appeal to the City Manager.
- H-11 The Finance Director will maintain a list of financial institutions as required by the Public Deposit Commission (PDC), authorized to provide investment services as outlined in R.C.W. 39.58.080.
- H-12 All investment securities bought by the City, including collateral being held on repurchase agreements, will be held by the City or in safekeeping for the City by the City's custodian bank. A third party bank trust department may be appointed as agent for the City under the terms of a custody or trustee agreement signed by both the bank and the City. The primary agent of the custodian bank will provide a safekeeping receipt to the City listing the specific instrument, its rate and maturity, and any other pertinent information. All security transactions, including collateral for repurchase agreements, entered into by the City of Covington will be conducted on a delivery-versus-payment (DVP) basis.
- H-13 Repurchase Agreements may be entered into on a safekeeping basis only if a master agreement with the bank or trust department providing the safekeeping service is first obtained. This agreement shall very clearly establish that the bank/trust is acting as a third party agent for the Finance Director, not the broker/dealer arranging the repurchase agreements. Such third party safekeeping arrangements will be documented with a signed agreement between the Finance Director and the bank/trust involved assuring that the Finance Director has absolute control over the securities once they are delivered to safekeeping and that the dealer does not have access to them under any circumstances.
- H-14 Investment officials will be bonded to provide protection to the City against loss due to possible embezzlement or malfeasance.
- H-15 The City will assure that no single institution or security is invested to such an extent that a delay of liquidation at maturity is likely to cause a current cash flow emergency. With the exception of U.S. Treasury securities and the State Investment Pool, the City will invest no more than twenty-five percent (25%) of its total investment portfolio in a single security type or with a single financial institution.
- H-16 To the degree possible, the City will attempt to match its investments with anticipated cash flow requirements. Liquidity should be ensured through practices that include covering the next vendor disbursement and payroll dates through maturing investments. Unless specifically matched to a certain cash flow, or estimated to meet cash flow needs, the City will not directly invest in securities maturing more than three (3) years from the date of purchase.
- H-17 The City of Covington's investment portfolio will be designed to obtain a market average rate of return during budgetary and economic cycles, taking into account the City's investment risk constraints and cash flow needs. The City will report investment yield benchmarked to the yield of the six-month Treasury Bill and/or the Average Fed Funds rate and/or the return provided by the State Investment Pool.
- H-18 The Finance Director will actively manage daily cash to the extent that transaction costs do not overcome interest earnings. The goal is to have ninety percent of the city's entire cash and cash equivalent assets invested.

## **I. INTERGOVERNMENTAL REVENUES AND RELATIONS POLICIES**

Many service costs of the City are influenced by other governments, either because of service overlap or service mandates imposed by the county, state, or federal government. The City shall take advantage of opportunities to enhance service delivery through intergovernmental cooperation, shared revenues, and grants while aggressively opposing mandates that distort local service priorities.

- I-1 The City will refrain from using grants to meet ongoing service delivery needs. In the City's financial planning, grants will be treated in the same manner as all other temporary and uncertain resources and will not be used to fund ongoing, basic service needs.
- I-2 All grant agreements will be reviewed to ensure compliance with state, federal, and City regulations.
- I-3 The City will budget expenditures for grant-funded programs only after a grant award or letter of commitment, and only for the amount of grant award. City overhead or indirect costs for grant-funded programs will be included in all grant proposals, where permitted.
- I-4 The City will aggressively oppose state or federal actions that mandate expenditures which the City Council considers unnecessary. The City will pursue intergovernmental funding to support the incremental cost of those mandates.
- I-5. The City will work with other governments to identify the jurisdiction most capable and appropriate to provide specific public services. All intergovernmental agreements and contracts for service delivery will be brought forward to the City Council for approval.
- I-6. Capital grants with local matching requirements can only be accepted for with the express approval of the City Council regardless if indicated in the Capital Investment Program.

## **J. ACCOUNTING, AUDITING, AND FINANCIAL REPORTING POLICIES**

The City shall maintain a system of financial monitoring, control, and reporting for all operations and funds in order to provide effective means of ensuring that overall City goals and objectives will be met and to assure the City's partners and investors that the City is well managed and fiscally sound.

- J-1 The City will maintain its accounting records in accordance with state and federal law and regulations. Budgetary reporting will be in accordance with the state's budget laws and regulations. The City will report its financial condition and results of operations in accordance with state regulations and generally accepted accounting principles applicable to governments.
- J-2 The State Auditor will annually perform a financial and compliance audit of the City's financial statements. Their opinions will be contained in the City's Comprehensive Annual Financial Report (CAFR) and the Report on Compliance with the Single Audit Act of 1984 (if required).
- J-3 The City will minimize the number of funds. The funds will be categorized in accordance with generally accepted accounting principles (GAAP) for reporting purposes.
- J-4 Excellence in Financial Reporting: As an additional independent confirmation of the quality of the City's financial reporting, the City will annually seek to obtain the Government Finance Officers Association Certificate of Achievement for Excellence in Financial Reporting. The CAFR will be presented in a way designed to communicate with citizens about the financial affairs of the City.

## **K. FIXED ASSETS**

- K-1 Fixed assets are defined as land, buildings, equipment, and improvements to existing assets costing more than \$5,000 and having a useful life in excess of one year. Assets with a value or cost under \$5,000 are to be expensed in the year of acquisition.

- K-2 Costs associated with remodeling or changes to the City's buildings will not be capitalized unless the useful life of the structure is extended.
- K-3 Enhancements or additions to equipment will be capitalized only if the cost or value is \$1,000 or more and the useful life is extended.
- K-4 Additions to City acquired vehicles will be capitalized only if the item is to remain with the vehicle upon disposal.
- K-5 Each department director is responsible for notifying Finance in writing of all assets sold, traded, transferred, and surplused or lost at the time of the occurrence.
- K-6 All assets that can be labeled will have a numbered City of Covington tag attached in a prominent, convenient location. Assets of a lesser value than the capitalization standard of \$5,000, may be tagged where there is a need for property control and accountability. Finance will supply the tags which will be attached by the department receiving the assets.
- K-7 All assets, regardless of value or capitalization, are the department director's responsibility with regard to tracking, inventory, and safekeeping. Finance is responsible for keeping and updating the fixed asset database.
- K-8 The Finance Director may administratively surplus office equipment, computer equipment, small tools, computer software, minor equipment and police weapons with a value of less than or equal to \$5,000. Titled vehicles, real property, and any City property with a value of greater than \$5,000 will be surplused by City Council resolution.
- K-9 All property with an expected value greater than the cost to surplus will be offered through a competitive process, in which at least three interested parties are notified. Property where the expected value is less than the cost to surplus may be destroyed or donated to another governmental agency or local community non-profit. The City may elect to partner with another City's annual auction to save on costs and resources.
- K-10 The Finance Director will have oversight for the accounting of all surplus property transactions. In cases of administrative surpluses, the Finance Director will record property description, estimated value, number of bidders, and the lowest-highest bid range for accounting and auditing purposes.
- K-11 The Public Works Director shall manage the GASB-34 infrastructure inventory providing the Finance Department with annual reports as required.

## **M. FINANCIAL PLANNING POLICIES**

The City shall develop and maintain a six-year Financial Forecast that estimates resource and expenditure behavior for five years beyond the current budget period. This Forecast will provide the City's decision-makers with an indication of the long-term fiscal impact of current policies and budget decisions. This planning tool must recognize the effects of economic cycles on the demand for services and the City's resources. To this end, the Forecast should differentiate between revenue associated with one-time economic activities and revenues derived as a result of base economic growth. City financial planning should ensure the delivery of needed services (many of which become more critical during economic downturns) by assuring adequate reliance on ongoing resources in order to support continued City services during economic downturns.

### **M-1 Operational and Capital Funds:**

- a. The Finance Department will prepare and maintain a Financial Forecast for Operational and Capital Funds based on current service levels and current funding sources. This forecast will include the upcoming year as well as five years beyond the current period (a total of six forecast years). This future-oriented look will provide insight into whether the current mix and level of resources are likely to continue to be sufficient to cover current service levels. The forecast also

allows staff and City Council to test various “what-if” scenarios and examine the fiscal impact on future budget cycles.

- b. The City will periodically test both its planning methodology and use of planning tools in order to provide information that is timely, accurate, and widely disseminated to users throughout the City.
  - c. Departments will forecast and monitor their respective revenues and expenditures with assistance from the Finance Department. The Finance Department will assist departments in developing appropriate systems for such monitoring and will retain overall fiscal oversight responsibility for the General Fund.
- M-2 Expenditure estimates should anticipate contingencies that are reasonably predictable and also differentiate between ongoing expenditures and those that are one-time activities.