KING WILLIAM COUNTY, VIRGINIA

FINANCIAL POLICIES

RESOLUTION 20-32

King William County has a responsibility to carefully account for public funds, to manage its finances prudently, and to diligently and effectively allocate its resources to provide the citizens the governmental services they desire. Fiscal integrity is critical and should form the basis of the County's management and decision-making processes of its fiscal affairs. The primary objective of establishing Financial Policies is to provide a framework within which sound financial decisions may be made for the long-term betterment and stability of the County. The County's financial policies will provide guidelines and goals to guide its financial practices.

The goals of the Financial Policies are to:

- Guide King William County Board of Supervisors in reaching a consensus on the financial condition desired for the County.
- Provide a link between long-range financial planning and current operations.
- Promote long-term financial stability by establishing clear and consistent guidelines.
- Provide a framework for evaluating the fiscal impact of budgetary decisions related to providing government services and programs.
- Reduce the risks to the County of experiencing fiscal crises.

1.0 Operating Budget Policy

1. King William County will prepare and approve an annual budget per Code of Virginia, Title 15.2-2503. The County will annually adopt and execute a budget for such funds as may be required by law or by sound financial practices and generally accepted accounting principles. The budget shall control the levy of taxes and the expenditure of money for all County purposes during the ensuing fiscal year. The County budget shall be balanced within all available operating revenues, including fund balance, and adopted by the Board of Supervisors.
   - King William County does not intend to issue tax or revenue anticipation notes to fund operations. The County's intent is to manage cash to prevent cash flow needs.

2. Revenues will be projected conservatively, but realistically, considering:
   - Historical trends;
   - The volatility of the revenue sources;
   - Inflation and other economic conditions; and
   - The costs of providing directly associated services.

3. Expenditures will be projected conservatively considering:
   - A conservative, but likely, scenario of events (versus "worst case scenario");
   - Specific, identified needs of programs and services;
   - Historical consumption and trends; and
   - Inflation and other economic conditions.

4. An unplanned operating contingency line item shall be included in the annual operating budget to provide for the ability to react to unforeseen circumstances in operations that arise during the fiscal year. An amount equivalent to 0.005% of general government expenses will be set aside for the operating budget contingency reserve. The contingency line item shall be an annual appropriation that will not accumulate or carry forward from fiscal year to fiscal year.

5. The County will prepare the capital improvement budget in conjunction with estimates of available revenues in order to assure that the estimated costs and future impact of capital projects on the operating budget will be considered prior to its inclusion in the Capital Improvements Plan.

6. The operating budget preparation process will be conducted in such a manner as to allow decisions to be made regarding anticipated resource levels and expenditure requirements for the levels and types of services to be provided in the upcoming fiscal year. The following budget procedures will ensure the orderly and equitable appropriation of those resources:
   - Operating budget requests are initiated at the department level within targeted guidelines set by the County Administrator.

7. Budget adjustments within a department involving transfers from one category – i.e., personnel (pay and benefits), capital and operations - to another shall be approved by the County Administrator.

8. Beginning in the first year subsequent to the adoption of these policies, quarterly cash basis actual-to-budget financial reports prepared after bank statement reconciliation will be provided to the Board of Supervisors. The reports will be provided within 45 days after the end of the quarter to enable the Board of Supervisors to monitor the budget.

9. Any amendments to the budget "which exceed one percent of total expenditures shown in the current adopted budget or the sum of $500,000, whichever is lesser, and be accomplished by publishing a notice of the meeting and a public hearing once in a newspaper having general circulation" at least seven days prior to the meeting date (Code of Virginia, Title 15.2-2507).

2.0 Capital Budget Policy

1. The County will approve an annual capital budget as an integral part of its total County budget. The capital budget will align with a 5-year Capital Improvements Plan (CIP).

2. The County will coordinate the development of the capital budget with the development of the operating budget so that future operating costs, including annual debt service, associated with the new capital projects will be projected and included in operating budget forecasts.

3. The 5-year Capital Improvements Plan will include all new facilities and major improvements to buildings and real estate as well as all projects requiring debt financing. The CIP will include sources of funding for the capital projects, including operating revenues, Restricted General Fund balances, non-General Fund departmental reserves, grants, capital leases, and debt financing.

4. Emphasis will continue to be placed upon a viable level of "pay-as-you-go" capital construction to fulfill needs in the Board's approved Capital Improvements Plan.

5. The acquisition of vehicles, IT hardware and software, and other depreciable equipment and machinery shall be considered in the capital budget in addition to the Capital Improvements Plan and shall reflect the departments to which they should be charged.

6. Upon completion of a capital project, any remaining appropriated funds in that project will be returned to the original appropriating fund. Any transfer of remaining funds from one project to another must be approved by the Board of Supervisors.

7. The County shall maintain a capital budget that includes the Capital Improvements Plan and a plan for the acquisition and replacement of vehicles, IT hardware and software, and depreciable equipment and machinery.

- The County will provide funding for vehicles, IT hardware and software, equipment and machinery as part of the annual budget to replace assets at the end of their useful life, or to upgrade capital assets as appropriate.
- The County's objective is to use pay-as-you-go funding (using cash resources) to acquire those items. Other sources will supplement cash funding such as lease purchase agreements, bonds, General Fund Balance, reserves and grants, when available.
- The County shall conduct a periodic physical inventory annually of all vehicles, computers, and depreciable equipment and machinery.

3.0 Debt Management Policy

1. Introduction

King William County recognizes that a formal debt policy is essential to effective financial management. Adherence to a debt management policy signals that a locality is well managed and, therefore, is likely to meet its debt obligations in a timely manner and is also a recommended practice of the Government Finance Officers Association. Debt management policies are written guidelines, allowances, and restrictions that guide the debt issuance practices. Adherence to a debt policy helps to ensure the County maintains a sound financial position.

The debt policy is to be used in conjunction with applicable laws and regulations and with the operating and capital budgets and other financial policies of the County. Objectives of the debt policy have been set to assist the County in:

- Funding a Capital Improvement Plan
- Maintaining an appropriate mix of pay-as-you-go and debt funding
- Maintaining an adequate fund balance, including an appropriate amount of unassigned fund balance
- Structuring debt repayment schedules that provide for reasonable and equitable annual payments

2. Debt Instruments

The County will use appropriate debt instruments to provide funding for capital assets at the lowest cost with minimal risk:

General Obligation Bonds:

General obligation bonds are bonds secured by a promise to levy taxes in an amount necessary to pay debt service, principal and interest, coming due each fiscal year. General obligation bonds are backed by the full faith and credit of the County. These bonds are authorized by a referendum or by non-voted (2/3's) authorization by the governing body. The non-voted authorization allows

governments to issue up to two-thirds of the previous year's net debt reduction without a referendum.

Revenue and Special Obligation Bonds:

Revenue bonds are bonds that pledge revenues generated by the debt-financed asset or by the operating system of which that asset is a part. Special obligation bonds are bonds that are payable from the pledge of revenues other than locally levied taxes.

Other Financing Arrangements:

Installment financings are an alternative financing method that does not require voter approval. Certificates of participation or limited obligation bonds represent an undivided interest in the payments made by a public agency pursuant to a financing lease or an installment purchase agreement. The security for this financing is represented by a lien on the property acquired or constructed.

An Installment Purchase Contract is an agreement in which the equipment or property is acquired and periodic payments, which are sufficient to pay debt service, are made. The County will use this type of financing for short-term equipment purchases of 3 to 5 years.

The County will use pay-as-you-go funding for capital improvements or capital assets having a cost of less than $250,000 or assets having a useful life of less than 10 years unless budgetary restraints require the use of financing to acquire the necessary funding for those capital improvement or capital assets.

3. Purposes for Debt Issuance

The County may issue debt for the purpose of acquiring or constructing capital assets including land, buildings, machinery, equipment, fixtures and any other eligible expenses of the project and for making major renovations to existing capital improvements, for the good of the public. Exceptions to this rule will be considered on a case-by-case basis to determine if the contemplated debt is in the best interests of the County. Long-term debt shall not be used to finance ongoing operational expenses. When applicable, debt issuance will be pooled together to minimize issuance expense.

Before issuing any new debt, the County will consider the following factors:

- Global, national and local financial environment and economy
- Current interest rates and expected interest rate changes
- Cash position and current debt position
- Availability of funds to repay
- Urgency of current capital needs and flexibility to cover future needs
- Appropriate debt issuance practices and debt structuring

4. Debt Structure

The debt structure is made up of the life of the debt, interest rate and principal maturity schedule. This debt could be general obligation, revenue or special obligation bonds, or other installment financings. The cost of taxable debt is higher than the cost of tax-exempt debt. However, the issuance of taxable debt is mandated in some circumstances, and may allow flexibility in subsequent contracts with users or managers of the improvements constructed with the bond proceeds. The County will usually issue obligations on a tax-exempt basis, but may occasionally issue taxable obligations when there is an expected benefit from doing so. The County shall establish an affordable debt level to ensure sufficient revenue is available to pay annual debt service.

General obligation bonds will generally be competitively bid with no more than a 20-year life unless there are compelling factors which make it necessary to extend beyond this point and applicable law allows a longer term. In a competitive sale, the County may sell its debt obligations in which any interested underwriter or syndicate is invited to submit a proposal to purchase an issue of bonds. The bonds are awarded to the underwriter presenting the best bid according to stipulated criteria set forth in the notice of sale.

Negotiated sales or private placements, however, may be used where allowed when complex financing or sales structure is a concern with regard to marketability. In a negotiated sale, the bonds may be sold through an exclusive arrangement between the County and an underwriter or underwriting syndicate. At the end of successful negotiations, the issue is awarded to the underwriters. This method offers flexibility for the County. The criteria used to select an underwriter or syndicate in negotiated sales should include, but not be limited to the following: overall experience, marketing philosophy, capability, previous experience, underwriter's discount, and expenses.

Debt service for each issue will be structured in an attempt to minimize the County's interest payments over the life of the issue while taking into account the existing debt obligations of the County. Any debt issued shall not have a maturity date beyond the useful life of the asset being acquired or constructed by the debt proceeds.

5. Debt Ratios

The County will use an objective, analytical approach to determine the amount of debt to be considered for authorization and issuance. This process involves the comparison of generally accepted debt ratios from comparable counties to the current County ratios. The ratios will be re-evaluated every five (5) years or sooner as market conditions dictate.

The County shall adhere to the following:

Net Direct Debt per Capita

This ratio measures the burden of direct debt placed on the population supporting the debt. This ratio is widely used as a measure of an issuer's ability to repay debt. The County's general obligation debt as a percentage of the assessed value of real taxable property.

Net Direct Debt as a Percentage of Assessed Valuation

This ratio measures debt levels against the property tax base that generates the tax revenues, which are the main source of debt repayment. The County will maintain its debt at no more that 3% of the countywide assessed value.

Net Direct Debt Service as Percentage of Operational Budget

This ratio reflects the County's budgetary flexibility to adapt spending levels and respond to economic condition changes. The County will maintain its net debt service at no more than 10% of the operational budget.

6. Refinancing of Outstanding Debt

The County will continually review the County's outstanding debt and recommend issues for refunding as market opportunities arise. Debt shall be refinanced only for the purpose of achieving debt service savings, unless required to achieve specific debt management goals of the County. The estimation of net present savings should be, at a minimum, in the range of 4% of the refunded maturities before a refunding process would be considered unless the County otherwise determines the annual savings warrants the refunding. The County will not refinance debt for the purpose of deferring scheduled debt service, unless unique circumstances are present.

The County may issue advance refunding bonds when advantageous, legally permissible, and prudent and a net present value savings is achieved. Advance refunding transactions are those undertaken in advance of the first date the refunded debt can be called for optional redemption, and will require an establishment of an escrow account for the defeasance of the refunded debt. All costs incurred in completing the refunding shall be taken into account when determining the net present value savings.

7. Pay-As-You-Go Funding

The County shall use pay-as-you-go and other alternative sources of funding for capital projects to minimize debt levels. To have an effective pay-as-you-go program, at least one funding source must be identified that is consistent, reliable and large enough to provide for capital needs in an amount that reduces dependency on debt. In order to reduce the impact of capital programs on future years, the County will annually appropriate funds for its capital improvement plan. The County will also appropriate proceeds from all county land sales and other capital assets as deemed appropriate for capital projects. This practice will allow additional funding of capital improvement projects and reduce the County's dependence on borrowing. Pay-as-you–go funding will save money by eliminating interest expense on the funded projects and will improve financial flexibility in the event of sudden revenue shortfalls or emergency spending.

8. Issuance of Debt

The scheduling and amount of bond sales and installment purchase transactions will be recommended by the Finance Director and the County Administrator. The Board of Supervisors must approve the sale. These decisions will be based upon the identified cash flow requirements for each project to be financed, market conditions, and other relevant factors including debt ratios.

9. Arbitrage Liability Management

The County will maintain a system of record keeping and reporting to meet the arbitrage and rebate compliance requirements of the federal tax code. This effort includes tracking investment earnings on bond proceeds, calculating rebate payments in compliance with tax law, and remitting rebatable earnings to the federal government in a timely manner in order to preserve the tax-exempt status of the County's outstanding debt issues.

It is the County's policy to minimize the cost of arbitrage rebate and yield restriction while strictly complying with the applicable laws. Because of the complexity of arbitrage rebate regulations and the severity of non-compliance penalties, arbitrage calculation will be performed by qualified arbitrage professionals in strict adherence to applicable laws and regulations. These calculations will be done in accordance with required Internal Revenue Service reporting dates.

10. Financing Team

The County will provide for a solicitation and selection process for securing all professional services required in connection with any debt issues. The service professionals selected will be required to develop and implement the County's debt management policy with the goal of continuity, quality service and competitive prices.

11. Administration and Implementation

The County Administrator and the Finance Director are responsible for the administration and issuance of debt including the completion of specific tasks and responsibilities included in this policy with approval of the Board of Supervisors.

4.0 Fund Balance Policy

1. Purpose

Establish key elements of the financial stability of the County by setting guidelines for the General Fund balance. Available fund balance is an important measure of economic stability. It is essential that the County maintain adequate levels of available fund balance in order to ensure against unanticipated events that would adversely affect the financial condition of the County and jeopardize the continuation of County services and/or activities and to provide the capacity to:

- Provide sufficient cash flow for daily financial needs;
- Offset significant economic downturns or revenue shortfalls;
- Provide funds for unforeseen expenditures related to emergencies;
- Adhere to Local Government Finance Officers Association minimum fund balance recommendations
- Provide citizens with a stable property tax rate

This policy will also establish guidelines for the replenishment of the County's fund balance in the event that the fund balance falls below the required levels set forth herein.

2. Definition

a. Fund balance. Fund balance is the difference between assets and liabilities reported in a governmental fund. An accounting distinction is made between classifications of fund balance based on restrictions on the use of fund balance. These classifications as defined by the Government Finance Officers Association are (1) Non-spendable, (2) Restricted, (3) Committed, (4) Assigned, and (5) Unassigned.

b. Non-spendable fund balance: Non-spendable fund balance are the components of fund balance that cannot be spent because they are either (a) not in a spendable form or (b) contractually required to be maintained intact.

c. Restricted fund balance: Restricted fund balance are the components of fund balance that have constraints placed on the use of resources either (a) externally imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or (b) imposed by law through constitutional provisions or enabling legislation. Example, Split Levy legislation.

d. Committed fund balance: Committed fund balance are the components of fund balance that are used for specific purposes pursuant to constraints imposed by formal action of the government's highest level of decision-making authority. In King William County, the highest level of decision-making authority would be considered the Board of Supervisors. These self-imposed limitations must be set in place prior to year-end, but can be calculated after year-end to be considered committed for that fiscal year end. In addition, to be considered committed, the limitations that were imposed at the highest level of decision-making authority must also require the same action to remove or modify the limitations.

e. Assigned fund balance: Assigned fund balance are the components of fund balance that are constrained by the government's intent to be used for specific purposes, but are neither restricted nor committed. These assignments can occur any time before the issuance of financial statements to be considered assigned for that fiscal year end. Further, this assignment ability can be delegated by the Board of Supervisors to an appropriate person (i.e. County Administrator or Director of Finance).

f. Unassigned fund balance: Unassigned fund balance is the remainder of fund balance that has not been reported in another classification and represents assets that are available to appropriate for future purposes.

g. Available fund balance: Available fund balance is the total fund balance less the total of non-spendable fund balance and fund balance restricted for stabilization by state statute.

3. Policy

   a. The King William County Board of Supervisors formally establishes the goal of maintaining unassigned fund balance in the General Fund in an amount of twenty (20) percent (approximately 2-3 months) of the General Fund expenditures and outflows at the end of each fiscal year. It is the duty of the Director of Finance to ensure the Board of Supervisors is informed on the annual unassigned fund balance level. If the level nears the allowed range, the Director of Finance will make recommendations on where that level should be. If any significant event or change occurs during a fiscal year which the Director of Finance believes will lead to the County being below the allowed range, the Director of Finance will notify the Board of Supervisors.

   b. If the unassigned fund balance level exceeds the twenty (20) percent ceiling in a given year, the Board of Supervisors delegates authority to assign the funds for the purpose of paying for future capital and capital project needs to the Director of Finance. Alternatively, Director of Finance may recommend to the Board of Supervisors that a budget amendment be adopted to move the amount above the ceiling to a capital project fund.

   c. The County's budget and revenue spending policy provides for programs with multiple revenue sources. The Director of Finance will use resources in the following hierarchy: bond proceeds, federal funds, state funds, local funds and county funds. For purposes of fund balance classification, expenditures are to be spent from restricted fund balance first, followed in order by committed fund balance, assigned fund balance and lastly unassigned fund balance. The Director of Finance has the authority to deviate from this practice if it is in the best interest of the County.

   d. The independent auditor of the County shall monitor the County's compliance with this established Fund Balance Policy. The auditor shall report related findings and recommendations annually as part of the County audit.

4. Replenishment of Fund Balance

   a. If it is anticipated at the completion of any fiscal year that the projected or estimated amount of fund balance falls below the required levels set forth in section 3, the County Administrator shall prepare and submit in conjunction with the proposed budget a plan for the expenditure reductions and/or revenue increases necessary to restore the amount of fund balance to the minimum requirements within two (2) fiscal years.