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City of Sugar Land

Financial Management Policy Statements

Introduction

The Financial Management Policy Statements, adopted by City Council, are an overview of the City's financial policies and provide guidelines to City staff in managing and planning the City's finances. Some policy statements are driven by requirements of state law or City Charter, while others are formally documented through policies and procedures. Statements that are driven by legal requirements will be noted as such.

In some case, exceptions to the policy statements may be appropriate and/or necessary. Exceptions to stated policies will be specifically identified and the need for the exception will be documented and explained to City Council and/or the City Manager.

Accounting, Auditing & Financial Reporting

Maintain accounting practices that conform to generally accepted accounting principles and comply with prevailing federal, state, and local statutes and regulations. Prepare and present regular reports that analyze and evaluate the City's financial performance and economic condition.

Accounting Practices and Principles

The City will maintain accounting practices that conform to generally accepted accounting principles (GAAP) as set forth by the Governmental Accounting Standards Board (GASB), the authoritative standard setting body for units of local government. All city financial documents, except monthly interim financial reports, including official statements accompanying debt issues, Comprehensive Annual Financial Reports and continuing disclosure statements will meet GASB standards. Monthly interim financial reports are on a cash basis and will be reported as budgeted. At year-end the general ledger and financials will be converted to full accrual basis.

Financial and Management Reports

Pursuant to City Charter requirements, Interim Financial Reports will be provided monthly to management and City Council that explain key economic and fiscal developments and note significant deviations from the budget. These reports will be reviewed monthly with the City Manager and provided to City Council by the end of each month for the prior month. These reports will be prepared on a cash basis. Quarterly reports on the status of the City's Strategic Projects will be provided through the City Manager's office and made available to the City Council. The reports will include project scope and work plan as well as comment on noteworthy activity.

Quarterly, departments will report on service level measures and/or indicators as compared to target and prior years through the Office of Strategic Initiatives. Capital Projects are reported quarterly to the City Manager and included in the quarterly report to City Council.

Annual Audit

Pursuant to State Statute, the City shall have its records and accounts audited annually and shall have an annual financial statement prepared based on the audit. The audit shall be performed by a certified public accounting (CPA) firm, licensed to practice in the State of Texas. Although the Texas Local Government Code, Section 103.003 Filing: Public Record requires the annual financial statement including the auditor's opinion on the statement to be filed with the City Secretary within 180 days after the last day of the fiscal year, it is the City's goal to file the

audit at the second City Council meeting in February. The audit firm shall provide a management letter to the City prior to the filing of the audit. The audit firm shall also provide a Single Audit of Federal and State grants, when necessary.

The objective of the ordinary audit of financial statements by the independent auditor is the expression of an opinion on the fairness with which they present, in all material respects, financial position, results of operations, and its cash flows in conformity with generally accepted accounting principles. The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud. The financial statements are management's responsibility. The auditor's responsibility is to express an opinion on the financial statements.

An official Comprehensive Annual Financial Report (CAFR) shall be issued no later than six (6) months following the end of the fiscal year. The CAFR shall be prepared to meet the requirements of the Certificate of Achievement for Excellence in Financial Reporting program through GFOA. This program establishes criteria that go beyond the minimum requirements for Generally Accepted Accounting Principles to prepare CAFRs that evidence the spirit of transparency and full disclosure. The Chief Accountant (or equivalent) shall be responsible for establishing a process to ensure timely resolution of audit recommendations.

Finance/Audit Committee

The City Council shall designate a Finance/Audit Committee. The role of the committee is to review and guide financial policy and strategic financial issues as needed and determined by the City Manager or City Council. The Finance/Audit Committee responsibilities related to the audit will include but not be limited to:

- Overview of the planning and timeline of the audit and risk assessment.
- Final audit review, results, findings, management letter as well as major audit adjustments as identified under Sarbanes-Oxley Act of 2002.
- Meet as soon as practical and appropriate after final audit review to assess the status of issues addressed in the management letter, if warranted.
- Meet during the course of the audit regarding any major issues/concerns/findings that may arise.

Continuing Disclosure

The Director of Finance will ensure that the Municipal Securities Rulemaking Board's EMMA® website is current and all disclosures are filed timely with assistance from the City's Municipal Advisor and Bond Counsel. EMMA® is the official repository for information on virtually all municipal securities. Continuing disclosure includes annual disclosure required within 180 days of fiscal year end, as well as material event disclosure required under the Securities and Exchange Commission (SEC) Rule 15c2-12 within 10 days of the occurrence of the event.

Signature of Checks

All checks shall have two signatures. Three persons shall be authorized to sign checks: the City Manager, an Assistant City Manager or Director of Finance, and the Chief Accountant. Signatures shall be affixed to all City checks via facsimile signatures, made with a secure laser check printing system or through handwritten signatures affixed to each check.

FINANCIAL CONSULTANTS

The City will employ qualified financial advisors and consultants as needed in the administration and management of the City's financial functions. These areas include but are not limited to audit services, debt administration, delinquent tax collection attorney, and financial modeling. The City shall implement evaluation criteria for each financial consultant to ensure the City receives the highest quality services available. The principal factors in the selection of these consultants will be experience/expertise, ability to perform, the services offered, references, and methodology to name a few. In no case should price be allowed to serve as the sole criterion for the selection.

Independent Auditors

In all matters relating to the assignment, an independence in mental attitude is to be maintained by the auditor or auditors. To emphasize independence from management, many corporations follow the practice of having the independent auditor appointed by the board of directors or elected by the stockholders. As such, the City has established a practice of the City Council appointing the auditor, and the auditor reporting to the City Council.

At least every five years, the City shall request proposals from qualified firms, including the current auditors if their past performance has been satisfactory. The City Council shall select an independent firm of certified public accountants to perform an annual audit of the accounts and records, and render an opinion on the financial statements of the City.

- It is the City's preference to rotate auditor firms every five years to ensure that the City's financial statements are reviewed and audited with an objective, impartial, and unbiased point of view. The rotation of the audit firm will be based upon the proposals received, the qualifications of the firm, and the firm's ability to perform a quality audit.
- However, if through the proposal and review process, management and the Finance/Audit Committee select the current audit firm, then, under the Sarbanes Oxley Act of 2002, the lead audit partner must be rotated as well as the lead reviewer after a maximum of five years.
- Annually, the independent auditor will provide a letter of engagement to the City for annual audit services.

Arbitrage Consultants

While the City is responsible to ensure that the records are in order, the calculations made, reporting completed, and filings made, the actual arbitrage calculation and reporting shall be contracted out to a qualified firm.

- The City's Chief Accountant and the Arbitrage Consultant shall complete a risk assessment of positive arbitrage on each bond issue annually to determine the necessity for a calculation of positive/negative arbitrage in the current year.
- All bond issues in accordance with arbitrage regulation shall have each 5th year and final arbitrage calculations completed.
- Due to the complexity of the City's financial structure and the benefits that come with the history and knowledge of the City, the contract with the Arbitrage Consultant shall be considered evergreen, however with a termination clause.
- In order to ensure that the City is still receiving services for fair market value, staff will conduct a survey every five years of arbitrage calculation fees and present a comparison and analysis to the City Manager and Finance/Audit Committee.

Delinquent Tax Collections

Due to the nature and expertise required, the City shall hire a delinquent tax collection attorney to collect delinquent taxes, represent the City in filing bankruptcy claims, foreclose on real property, seize personal property, and represent the City in court cases and property sales.

- The City shall contract for a delinquent tax collection attorney either through Fort Bend County in conjunction with the contract for billing and collection of the City's property taxes or shall contract directly with an attorney.
- The City shall review delinquent tax collection services and determine if they choose to contract direct or contract through the County either at the end of a direct contract for delinquent tax services or annually if contracted with Fort Bend County.
- If the City chooses to contract directly for delinquent tax collection services, requests for proposals and statements of qualifications are to be solicited at least every five years.
- There is not a requirement for rotation.

Bond Counsel

Bond Counsel to the City has the role of an independent expert who provides an objective legal opinion concerning the issuance and sale of bonds and other debt instruments. As bond counsel are specialized attorneys who have developed necessary expertise in a broad range of practice areas, the City will always use a consultant for these services. Generally, bonds are not marketable without an opinion of nationally recognized bond counsel stating that the bonds are valid and binding obligations stating the sources of payment and security for the bonds and that the bonds are exempt from State and Federal income taxes (if applicable).

Bond Counsel is responsible for the following tasks in a transaction:

1. Prepares and oversees bond proceedings;
 2. Gets required government approval;
 3. Ensures that the City meets all the legal requirements and authorization of the bond offering;
 4. Discloses and analyzes all relevant legal proceedings that may have a bearing on the validity of the offering;
 5. Interprets relevant regulations and laws and assists in structuring the issue;
 6. Writes key financing documents.
- Due to the complexity of the City's financial structure and the benefits that come with the history and knowledge of the City, the contract with Bond Counsel shall be considered evergreen, however with a termination clause.
 - In order to ensure that the City is still receiving services for fair market value, staff will conduct a survey every five years of bond counsel fees and present a comparison and analysis to the City Manager and Finance/Audit Committee.

Disclosure Counsel

Disclosure Counsel is an independent firm, separate from bond counsel, retained by the City to provide a legal opinion concerning accuracy of the information presented in disclosure and bond documents. With scrutiny of municipal disclosure increasing by the SEC and Municipal Securities Rulemaking Board, the engagement of

disclosure counsel provides an added layer of assurance that the City's financial position is accurately presented in bond documents.

- Due to the complexity of the City's financial structure and the benefits that come with the history and knowledge of the City, the contract with Disclosure Counsel shall be considered evergreen, however with a termination clause.
- In order to ensure that the City is still receiving services for fair market value, staff will conduct a survey every five years of disclosure counsel fees and present a comparison and analysis to the City Manager and Finance/Audit Committee.

Municipal Advisor

The Government Finance Officers Association (GFOA) recommends that issuers hire a municipal advisor (MA) prior to the undertaking of a debt financing unless the issuer has sufficient in-house expertise and access to current bond market information. The City issues various types of securities to finance its capital improvement program. Debt structuring and issuance requires a comprehensive list of services associated with municipal transactions, including but not limited to: method of sale; analysis of market conditions; size and structure of the issue; preparation of disclosure documents; coordinating rating agency relations; evaluation of and advice on the pricing of securities; assisting with closing and debt management; calculating debt service schedules; and providing recommendations on management of the City's finances, including evaluation of debt structures and refinancing opportunities.

- While retaining the services of an MA, the City shall post an IRMA Exemption Certificate on the City's website and on EMMA (Electronic Municipal Market Access, a service of the Municipal Securities Rulemaking Board). The IRMA Exemption Certificate states that the City has retained an independent registered municipal advisor (IRMA) and that the City will rely on the advice of the Municipal Advisor in the issuance of municipal securities.
- The Municipal Advisor must be registered with the Securities & Exchange Commission and Municipal Securities Rulemaking Board as a Municipal Advisor
- As municipal advisors to governmental entities have developed the necessary expertise in a broad range of services, the City will use a consultant for these services, until such time that the City wishes to bring these services in-house.
- Due to the complexity of the City's financial structure and the benefits that come with the history and knowledge of the City, the contract with the Municipal Advisor shall be considered evergreen, however with a termination clause.
- In order to ensure that the City is still receiving services for fair market value, staff will conduct a survey every five years of Municipal Advisory fees and present a comparison and analysis to the City Manager and Finance/Audit Committee.
- While a municipal advisor plays a key role on the financing team, it is important to note that the City remains in control of the decision making process necessary for the issuance and sale of the bonds or implementing the financing.
- The selected Municipal Advisor shall not be permitted to serve as underwriter on any bond transactions while serving in the Municipal Advisor role. Upon termination of the Municipal Advisor contract, a period of one year should pass before the firm may be engaged as an underwriter on any bond transaction for the City.

Depository Bank

Pursuant to State law, the City of Sugar Land may approve a depository services contract whose term does not exceed five years. There is no requirement for rotation. The City of Sugar Land will select its official banking institution through a formal process based on best value in order to provide the City with the most comprehensive, flexible, and cost-effective banking services available. Depository accounts may only be opened by employees with authority specifically granted in the depository agreements approved by City Council.

BUDGET AND LONG RANGE FINANCIAL PLANNING

Establish guidelines for budgeting to ensure a financially sound City and to establish a long-range financial planning process that assesses the long-term financial implications of current and proposed operating and capital budgets.

Balanced Budget

The City Manager shall file annually, a balanced budget for the ensuing fiscal year with City Council in compliance with state law and the City Charter.

In addition, it is expected that the annual operating budget will be structurally balanced. A structurally balanced budget is further defined as recurring revenues funding recurring expenditures and adherence to fund balance policies. Deferrals, short-term loans, or one-time sources will be avoided as budget balancing techniques. If economic conditions dictate that the City Manager file a structurally imbalanced budget, it shall be accompanied by a plan to return the budget to structural balance and the resulting five-year financial forecast that reflects steps to be taken to return the budget to structural balance.

Current Funding Basis (Recurring Revenues)

The City shall budget and operate on a current funding basis. Revenues and expenditures shall be budgeted on a cash basis. Expenditures shall be budgeted and controlled so as not to exceed current revenues. Recurring expenses will be funded exclusively with recurring revenue sources to facilitate operations on a current funding basis.

Use of Non-Recurring Revenues

Non-recurring revenue sources, such as a one-time revenue remittance or fund balance in excess of policy can only be budgeted / used to fund non-recurring expenditures, such as capital purchases or capital improvement projects. This will ensure that recurring expenditures are not funded by non-recurring sources.

The following expenditures are considered non-recurring for budgetary purposes:

1. Transfers to Replacement Funds (Fleet and High Technology)
2. Capital Expenditures
3. Contingency Funds
4. Lump sum payments to employees

The following revenues are considered non-recurring in the definition of a structurally balanced budget:

1. Grant Revenues
2. Red Light Camera proceeds
3. Annexation/Dissolution Proceeds
4. Reimbursements for One Time Items
5. Short Term/Inter-Fund Loans

Allowable uses of one-time revenues received during the year (over the budgeted amounts):

1. To replenish a draw down in the fund balance below policy requirements (including Self-Insurance Reserve in the Employee Benefits Fund)
2. Provide a one-time boost to infrastructure rehabilitation funding
3. To fund capital projects without an identified funding source
4. Lump sum payment to employees if merit pool is reduced
5. To fund one-time expenditures in the following fiscal year's budget

Property Taxes

Tax Rate

By law, the City must levy a tax rate sufficient to generate revenues that will meet outstanding debt obligations, net of outside funding sources (transfers from other funds). The City Manager will recommend a tax rate that the City finances require in order to operate efficiently, yet effectively, and meets the City Council's expectations of services provided and service levels.

As economic conditions permit, the City Manager will recommend a tax rate not greater than the effective tax rate plus 3%. The goal is not to exceed an average annual increase in the residential tax bill of 3% unless the voters approve a general obligation bond referendum. The following shall be taken into account in managing growth in the average tax bill: property revaluation, tax rate adjustments and/or changes to the residential homestead exemption.

The effective tax rate is defined by the State of Texas as the tax rate that raises the same amount of total tax revenue in the current year as the prior year's tax rate for properties taxed in both years. The effective tax rate is calculated based on a formula mandated by the state truth in taxation laws, and excludes new property value. Depending on valuation changes, the effective tax rate may be higher or lower than the prior year's tax rate and generate the same amount of total property tax levy. The only increase in tax revenue is from new value added to the tax roll since the prior year. Therefore, the effective tax rate plus 3% also may result in an increase to the nominal tax rate in order to achieve a 3% increase in the tax levy, excluding new value.

Homestead Exemption

Annually the City Manager shall review the homestead exemption based on anticipated revaluation increases. When the financial health of the City's finances and the economic and market conditions of the local economy justify, the City Manager may recommend an increase to the homestead exemption to minimize the impact of revaluation on homeowners. In accordance with state statute, a recommended change in the homestead exemption shall be presented to City Council to allow approval prior to July 1. The 2015 legislative session saw passage of Senate Bill 1, which prohibits cities from reducing or repealing the residential homestead exemption below the 2014 value (7%) through December 31, 2019.

The total exemption percentage granted cannot exceed the state limitation of 20%.

Over-Age Exemptions and Disabled Persons Exemption

The City shall grant a \$70,000 over-age exemption and disabled persons' exemption each year when economic and financial conditions allow. This amount shall remain stable during the period in which the City is considering adjusting the homestead exemption.

If a tax freeze were ever implemented for over-age and disabled persons, these exemptions would be reduced to zero. (Chapter 2 Article V Sec 2-119, Code of Ordinances)

Sales Tax

Sales tax used to fund recurring operations shall have a target of 45%. As sales tax revenue fluctuates due to changes in economic conditions, the City shall endeavor through long-term strategies to reduce its reliance on sales tax revenues for funding recurring operating expenditures. The goal is to reduce the percentage dependence on sales tax for recurring operations, and set aside extra funds for one time needs. Sales Tax revenue shall be estimated conservatively (See Revenue Estimating for Budgeting).

Sales Tax from Incentive Grant Agreements

1. Sales tax revenues generated from incentive grant agreements will not be used to fund recurring operating expenditures but rather non-recurring capital purchases, economic development projects or capital improvement projects.
2. As the economic development sales tax is intended for use to promote economic development activities, the City shall strive to fund incentive agreements from economic development sales tax first, then from general fund sales taxes.
3. The portion of the City's sales tax adopted for property tax reduction shall not be included in the calculation of incentive grants.

Water/Wastewater Transfer for Pay-As-You-Go Capital Projects

As discussed under Capital Expenditures, the transfer from the City's Utility Fund to fund pay-as-you-go capital projects will be budgeted at a target of \$2,500,000, when financially feasible. It will be based on the financial health of the Utility Fund with the long-term goal of adequately funding rehabilitation.

Revenue Estimating for Budgeting

In order to protect the City from revenue shortfalls and to maintain a stable level of services, the City shall use a conservative, objective, and analytical approach when preparing revenue estimates. The process shall include analysis of probable economic changes and their impacts on revenues, historical collection rates, and trends. This approach should reduce the likelihood of actual revenues falling short of budget estimates and should avoid mid-year service changes.

Sales Tax

With such a large portion of the City's operating budget dependent on sales tax, it is important to forecast revenue conservatively. Sales tax revenue shall utilize the current year's projected revenue as a baseline for the following year's budget, net of audit adjustments and large one-time payments.

The purpose of defining forecast parameters is to better realize when changes in the utilization of property tax use may be necessary (ie. slowing general CIP due to shifting the tax rate from debt service to O&M), as well as permit for better planning opportunities. These parameters are designed to simulate the cyclical nature of the economy based on the most often used economic indicator, the Consumer Price Index.

The Long Range Sales Tax Forecast will utilize the following parameters to grow sales tax in years 2-5 of the forecast: February CPI as published by the Bureau of Labor Statistics for -All Urban Consumers.

1. Positive CPI:
 - a. Year 2 growth = lesser of CPI or 3%
 - b. Year 3-5 growth = 3%
2. Negative CPI:
 - a. Year 2 growth = flat from current year projection

- b. Year 3 growth = lesser of 3% or 5-year average CPI
- c. Year 4-5 growth = 3%

Water and Wastewater Revenues

The Utility Fund and Surface Water Fund revenues will be budgeted using consumption based on an average year's rainfall/consumption (excluding extremely wet and dry years). The City will anticipate neither drought nor wet conditions. Adjustments to utility rates shall be made based on revenue requirements over the five year forecast for the utility fund, and increases necessary to maintain revenue coverage requirements shall be made in advance of anticipated bond issues, if possible, to allow for smaller increases to be made over time.

Employee Compensation

When funding is available, the proposed budget shall include an amount adequate to cover an overall average performance and merit increase as determined annually by the City Manager. This amount will be calculated for each department, based on budgeted salaries for the year, and will be placed in the appropriate budget accounts. The City does not give cost of living increases. Other than adjustments due to changes in the compensation plan, salary increases are to be earned through merit and/or promotion increases.

The City's compensation plan shall be approved by City Council and administered by the City Manager as identified in the City Charter and the Council adopted Compensation Philosophy. All employees shall be paid within the approved budget and established salary ranges.

Budget Management

The budget is adopted by City Council through one reading of an ordinance, no later than the 25th day of September, as directed by Section 6.03b of the City Charter. Upon approval, the budget can be either amended or adjusted based on the level of changes needed. Under Local Government Code 102.009(a)- The governing body may levy taxes only in accordance with the budget. This means that the budget must be adopted before an ad valorem tax rate may be adopted.

- Amendment- an increase to the overall appropriation in the fund or capital project. Must be approved by City Council through one reading of an ordinance.
- Adjustment- a reallocation of funds between departments without changing the total operating fund budget. Must be approved by the City Manager.

Operating Budget Adjustments

The City Manager is responsible for managing the operating budget after it is formally adopted by City Council, including the transfer of funds within program, between programs, between departments, and expenditure of contingency funds as long as there is no change in service levels as a result of the adjustments. The City Manager may further delegate levels of authority for the daily operation of the budget.

Operating Budget Amendments

Under State law, the budget must be adopted before a tax rate can be adopted. Should the adopted tax rate generate more or less ad valorem tax revenue than the adopted budget, the operating budget shall be amended as soon as possible to ensure that budgeted expenditures remain balanced with anticipated revenue sources.

Budget reductions shall be targeted to regain structural balance and focused on reductions to recurring expenditures for non-core services, when the imbalance is due to recurring a revenue shortfall.

In order to preserve projected fund balances/ ending balances based on projected revenues and expenditures for the current fiscal year, City Council will amend the annual operating budget for all funds, excluding capital improvements funds, as set forth in the projections. City Council will amend the current fiscal year budget to projections annually through adoption of an ordinance amending the budget.

Contracts or purchases presented for City Council approval shall identify the budgeted amount for the item within the current approved budget. A budget amendment by City Council is only necessary if the total appropriation for the fund is increased. This could occur under, but is not limited to, the following situations:

1. The budgeted appropriation will be exceeded at the fund level prior to year-end.
2. Acceptance of a grant that was not included in the annual budget.
3. Appropriation from fund balances for items that were not budgeted.
4. A donation or sponsorship that exceeds budgeted revenues and cannot be absorbed within contingency funding.

To streamline the process, budget amendments are to be considered by City Council on an as-needed basis and then formally adopted by ordinance periodically. Each budget ordinance shall summarize and include all budget amendments approved by City Council for affected funds since the last ordinance was approved.

At year end, the annual operating budget will be amended by ordinance through projections and will reflect adjustments that were approved by the City Manager.

Capital Projects Budget Amendments

As capital projects are budgeted on a project length basis and not a fiscal year basis, a project budget needs approval of a budget amendment when one of the following applies:

1. Increase to project funding with a corresponding increase in revenues
 - a. Inter-local agreements
 - b. Award of a grant to enhance or expand the project
2. Reallocation of funding from one capital project to another, except:
 - a. When splitting funding for a project into multiple projects for tracking purposes when the total amount budgeted for the overall project does not change, or
 - b. When allocating additional funds from CIP fund balance to a project to accommodate a change order, as long as the additional funding needed does not exceed the lesser of 5% of the original project budget or \$50,000, and the change order does not need approval from City Council nor materially change the scope of the project.
3. Increase to project funding from the Capital Projects Fund Balance
4. Reduction to project budgets as discussed below:
 - Capital Project budgets shall be amended (reduced) when construction bids come in significantly under estimates, project estimates shall be adjusted to reflect the construction bid plus a sufficient contingency and other project needs, and the remaining budget shall be reduced as necessary to reflect savings.
 - When a project is funded from the issuance of debt, if the debt has not been sold at the time of the budget reduction, the revenue budget for bond proceeds shall be reduced accordingly.

Mid-Year Operating Deficits

During the fiscal year, the City may find revenues falling short of anticipated levels. If so, the City shall take immediate corrective actions if at any time during the fiscal year expenditure and revenue re-estimates are such that an operating deficit is projected at year end. Corrective actions are to be implemented by the City Manager with a report to advise the City Council of the actions taken. Corrective actions in order of precedence are:

1. Manage Vacant Positions
2. Deferral of capital purchases
3. Expenditure reductions
4. Hiring freezes
5. Freeze merit increases
6. Use of fund balance, including Replacement Fund balances.
7. Increase fees
8. Lay-off employees

Short-term loans shall be avoided to balance the budget.

The use of fund balance, which is a one-time revenue source, may be used to fund an annual operating deficit, only with a plan prepared as part of the annual budget to replenish the fund balance within two years if it is brought down below policy level.

Five-year Forecast of Revenues and Expenditures

A five-year forecast of revenues and expenditures shall be prepared in conjunction with the annual budget process for the following funds:

- General Fund
- Debt Service Funds
- Tourism Fund
- Water/Wastewater Utility Fund
- Surface Water Fund
- Airport Fund
- Economic Development Corporations
- Five-Year Capital Improvement Program

The forecast assesses long-term financial implications of current and proposed policies, programs, and assumptions that develop appropriate strategies to achieve the City's goals. The forecast will provide an understanding of available funding; evaluate financial risk; assess the likelihood that services can be sustained; assess the level at which capital investment can be made; identify future commitments and resource demands; and identify the key variables that may cause change in the level of revenue. The forecast will be used to identify anticipated financial issues so that a plan can be developed to correct anticipated issues before they become reality. The assumptions used to prepare the five-year forecast shall be consistent with those used to prepare the annual operating budget, unless specifically directed by a majority of City Council.

REVENUES AND OTHER RESOURCES

The City shall strive to maintain a balanced and diversified revenue system to protect the City from fluctuations in any one source due to changes in local economic conditions, which may adversely impact that source. The Budget Office shall maintain a revenue manual documenting the various revenue sources of the City and how those revenues are derived and estimated.

Property Taxes

- a. Taxes on Airport Value- Property taxes collected on taxable property at the Airport will be transferred to the Airport Fund to use for operations and development. This will ensure that users paying the property tax will see a direct benefit to the Airport.
- b. Rebates to Municipal Utility Districts (MUDs) – As stipulated in the individual utility agreements, the City has agreed to rebate a portion of City taxes collected on properties within in-city MUDs back to the districts through various utility agreements. Rebate payments shall be calculated based on the taxes collected by the City on properties within the district since the point of the last rebate calculation (quarterly or semi-annually depending on the MUD), less any refunds given on those properties during that period.
- c. Payments to Tax Increment Reinvestment Zones (TIRZ)- The City has several TIRZ established within the City. Taxes paid to the City on properties in each zone are paid to each TIRZ annually; payments due shall be adjusted for any refunds given on those properties since the last TIRZ payment was made.

Sales Tax Revenue

- a. Monthly, the Economic Development Corporations will be allocated their percentage of the actual monthly sales tax remittances.
- b. Of the remaining amount allocated to the City, funds will be allocated to General Fund operations, based upon the budgeted sales tax for operations, to ensure operating expenditures are funded. .
- c. Actual sales tax revenue received above the amount budgeted, on a cumulative annual basis, will be treated as one-time revenue and only used as identified in the section “use of non-recurring revenues” :
- d. Sales Tax from Sale of Aircraft
 1. Sales/Use tax remitted to the City that is determined to be from the sale/purchase of aircraft at the City’s Airport will be transferred to the Airport Fund, excluding the percent allocated to the Economic Development Corporations.
 2. The proceeds that are allocated to the Economic Development Corporations will be identified as potential funding for Airport projects that legally meet the requirements of the Corporations.

Administrative Services Charges

The City shall determine annually the administrative services charges due to the General Fund from the enterprise funds for overhead and staff support using a cost allocation model.

Utility Transfer to the Debt Service Fund for Assumed Water/Wastewater Debt

The Utility Fund shall transfer to the Debt Service fund an amount/percent calculated annually for water/wastewater infrastructure debt assumed by the City due to annexation and dissolution of municipal utility districts.

- a. The goal is to have water/wastewater debt funded by water/wastewater revenues as much as possible within the financial resources of the Utility Fund, without negatively impacting the utility fund.
- b. The City's intent is to fund a transfer amount that equates to 100% of the annual debt service requirements for water/wastewater debt in the Debt Service Fund.
- c. If the City should assume additional debt from municipal utility districts in the Debt Service Fund, the annual transfer for water/wastewater infrastructure debt will be reviewed and recalculated, if necessary. The overall percentage covered may need to be adjusted based on affordability.

Surface Water Revenues

The City will maintain a Surface Water Fund to account for revenues and expenses associated with the mandated reduction in groundwater usage.

- a. All participants in the City's Groundwater Reduction Plan will pay into the fund an amount based on water supplied at a rate established per 1,000 gallons (GRP fee).
- b. The GRP fee shall be paid monthly based on metered water pumped from groundwater sources.
- c. City customers will be billed a surface water fee based on billed water consumption. The City shall contribute monthly GRP fees to the Surface Water Fund for City customers.

Water/Wastewater Billings

Water, wastewater and surface water charges are billed in arrears, as customer meters are read monthly for the previous month's water usage. At year end, revenues are accrued to adjust revenues to full accrual basis but during the year, revenues are recorded on a modified accrual basis (when billed).

Revenue Collections

The City shall maintain high collection rates for all revenues by monitoring monthly receivables. The City shall follow an aggressive, consistent, yet reasonable approach to collecting revenues to the fullest extent allowed by law for all delinquent taxpayers and others overdue in payments to the City.

- a. The City shall contract for billing and collection services when it makes financial sense to do so.
 - a. Emergency Medical Transport billing requires a high level of knowledge relating to medical billing; in this case, outsourcing the billing & collection of EMS transport fees is the most prudent thing to do.
 - b. Property Tax billing & collection requires certification of a tax assessor/collector and significant staff time; contracting this service to Fort Bend County makes financial sense.
- b. The City shall contract for collection of delinquent receivables when it makes economic sense for the City to do so. The City currently contracts directly for the following delinquent receivables:
 - a. Court Fines & Warrants
 - b. Photographic Traffic Signal Fines
 - c. Emergency Medical Services
 - d. Miscellaneous Receivables, including Alarm Response Fees
 - e. Property Taxes- through the contract with Fort Bend County Tax Office
- c. Write-off of Uncollectible Receivables (excludes court fines and warrants)

- a. Receivables shall be considered for write-off as follows:
 - i. Undeliverable mail – accounts that remain outstanding for 6 months and all steps have been exhausted
 - ii. State Statute authorizing the release or extinguishment, in whole or in part, of any indebtedness, liability, or obligation, if applicable
 - iii. Accounts outstanding for 3 years, identified as uncollectible, and all attempts to collect have been taken
 - iv. The write-off of uncollected accounts is a bookkeeping entry only and does not release the debtor from any debt owed to the City.
 - v. The City shall estimate uncollectible accounts through an allowance for doubtful accounts in each fund with receivables.

User Fees

The City shall design, maintain, and administer a revenue system that will assure a reliable, equitable, diversified and sufficient revenue stream to support desired City services.

General Fund

- a. For services that benefit specific users the City shall establish and collect fees to recover the costs of those services.
- b. Where services provide a general public benefit, the City shall finance those services through property and sales taxes.
- c. For services that provide both specific benefits and a general public benefit, it may be appropriate to subsidize from property and sales tax revenues.
- d. Costs of Services are defined as full-cost; direct, indirect, and overhead.
- e. Factors in setting of fees shall include but not be limited to: market and competitive pricing, effect on demand for services, and impact on users, which may result in recovering something less than full cost.

Enterprise Funds

- a. Utility rates and other fund user fees shall be set at levels sufficient to cover operating expenditures (direct and indirect), meet debt obligations and debt service coverage, provide pay-as-you-go funding for capital improvements, and provide adequate levels of working capital.
- b. The City shall seek to eliminate all forms of subsidization between the General Fund and Enterprise Funds
- c. The Five-Year Financial Plan shall serve as the basis for rate change considerations.
- d. If rate increases are necessary, the Five-Year Financial Plan shall be built around smaller rate increases annually versus higher rate increases periodically.

User Fee Creation and Revision

Working with the department or office, the Budget Office will determine the cost for each service and determine a full-cost price. Once a fee has been proposed for a particular service, the fee will be compared to market, evaluated for potential effects on users such as low-income households, market demands of service, etc. A fee will then be recommended to the City Manager and City Council based on all information gathered through the fee evaluation.

User fees shall be adjusted by the Houston- Sugar Land- Baytown MSA CPI annually as part of the budget process, and a fee ordinance shall be adopted at the beginning of each fiscal year to reflect the fee revisions. Fee changes are effective for all activity billed or generated after the effective date of the fee revision.

Non-Resident Surcharges

For services provided to municipal utility districts or individuals who reside outside the city limits, the City may assess an out-of-city service fee or non-resident user fee. The surcharges shall be set either as an additional percentage fee or a separate fee for non-residents and can be established by ordinance or by contract.

EXPENDITURES AND SERVICES

Operating Expenditures

Identify services, establish appropriate service levels and administer the expenditure of available resources to assure fiscal stability and the effective and efficient delivery of those services.

Purchasing and Vendor Selection

The City Manager shall maintain policies and procedures to ensure compliance with state laws relating to procurement of goods and services.

It is the policy of the city that, when lowest qualified bid is not the sole determining factor for a contract award, the contract shall be awarded to the highest ranked vendor based on merit as determined by a thorough evaluation by a team of staff evaluators. Merit factors that can be taken into consideration include: qualifications, past experience, quality of team, equipment, scheduling, and proven performance. In accordance with state law, City Council approval is required on purchases that will expend more \$50,000 of City funds over the term of the contract. After purchasing staff verification that all applicable state laws, purchasing policies, and procedures have been followed, a recommendation for award is made to City Council by staff.

Departmental & Office Business Plans

Departments and Offices shall prepare a business plan to define their operating objectives.

- a. The business plan should provide a link between the budget and the services provided; there should be no gaps or holes in accountability, either in accounting for resources provided or in defining services delivered.
- b. The business plan shall include an organizational chart, service description and service levels, and measures that indicate how well the service is being delivered.
- c. The business plan shall include an explanation of how services are delivered (by city staff or contracted) and expected results of the service delivery.

Annual Program of Services

Annually, as part the budget document, a program of services for each department will be established for the ensuing year. The program of services will include a summary of services and service levels from the business plan, as well as service level expectations and staffing levels.

Maintenance of Capital Assets

Within the resources available each fiscal year, the City shall maintain capital assets and infrastructure at a sufficient level to protect the City's investment, to minimize future replacement and maintenance costs, and to maintain service levels.

Periodic Program/Service Reviews

The City Manager and staff shall undertake periodic reviews of City programs and services for both efficiency and effectiveness. Outsourcing and contracting with other governmental agencies and/or the private sector will be evaluated as alternative approaches to service delivery. Programs or services determined to be inefficient and/or ineffective shall be recommended through the annual budget process to be reduced in scope or eliminated.

Outsourcing of City Services

The City provides many municipal services to its citizens covering a wide variety of disciplines. Attempting to perform all of these services in-house could dilute the City's efficiency and not be cost effective. Two of the management tools utilized by the City to maximize efficiency and cost effectiveness are outsourcing and managed competition processes, the mere consideration of which provides economic benefits that flow from competition. The economic benefits of competition include lower costs and improved quality of performance irrespective of whether a given service is ultimately performed in-house or outsourced.

FUND BALANCE/WORKING CAPITAL

Maintain the fund balance and working capital of the various operating funds at levels sufficient to protect the City's creditworthiness as well as its financial position during emergencies or economic fluctuations. Should the budgeted fund balance drop below the minimum identified by the policy below, the City will establish a plan to replenish the balances within two years.

Governmental Fund Balances

There are five categories of Fund Balance in all governmental funds, not all will always be present. The categories are defined below:

1. Non-spendable- cannot be spent due to being non-spendable in form or the city being legally or contractually required to maintain this amount intact.
2. Restricted- balances are subject to external restrictions from creditors, grantors, contributors, or laws of other governments.
3. Committed- use of funds is only for specific purposes as determined by City Council. City Council will approve obligations of funds such as multi-year contracts prior to the end of the fiscal year.
4. Assigned- intended use of balances for specific purposes is established by the City Council or delegated to the City Manager that is neither restricted or committed and includes the remaining positive balance of all governmental funds except the General Fund. Balances for encumbrances, other than those committed by City Council, fall into this category.
5. Unassigned- balances are available for any purpose; excess fund balances after above categories have been deducted. This type of balance is reported in the General Fund and negative fund balances in other than General Fund.

General Fund Unassigned Fund Balance

The City must maintain a General Fund unassigned fund balance equivalent to at least three months of normal recurring operating costs, based on current year budgeted expenditures. If the fund balance exceeds this amount, the amount in excess of policy requirements may be utilized to fund one-time expenditures in the next fiscal year's budget.

Other governmental operating funds that do not have a policy minimum defined shall adhere to the general fund balance policy.

The City will typically use Restricted fund balances first, followed by Committed resources, and then Assigned resources, as appropriate opportunities arise, but reserves the right to selectively spend Unassigned resources first to defer the use of these other classified funds.

Working Capital of Enterprise Operating Funds

In enterprise operating funds, the City shall maintain working capital sufficient to provide for reserves for emergencies and revenue shortfalls, specifically in the Utility and Airport Funds. Enterprise funds without major infrastructure or assets will have no minimum balance requirement. A cash equivalent operating reserve will be established and maintained as follows:

1. Utility Fund - 25% of the current year's budget appropriation for recurring operations and maintenance.
2. Airport Fund - 25% of the current year's budget appropriation for recurring operations and maintenance, excluding fuel for resale.
3. Surface Water Fund – 50% of the current year's budgeted expenses, less any debt service reserve requirements. Funds in the reserve may be utilized as a general purpose reserve without limitation to type (debt, capital expense, etc).

The cash equivalent operating reserve is derived by dividing the total cash equivalents balance by recurring operating expenses. (Cash equivalents = Cash + Investments + Accounts Receivable – Accounts Payable)

Use of Fund Balance/Working Capital

Fund Balance/Working Capital shall be used only for emergencies, non-recurring expenditures/ expenses, or major capital purchases that cannot be accommodated through current year savings. Should such use reduce balances below the level established as the minimum for that fund, the request/decision to utilize said balances will include a plan to replenish funds within two years.

Inter Fund Loans

Through the long range financial planning process, the City may identify a short term capital financing need that does not qualify for debt financing, and funds are available in special revenue or enterprise funds balances. An inter fund loan is a loan from one fund to another that specifies repayment terms, and requires approval by City Council Resolution. Inter fund loans may not be used to support operating needs, but are allowable for cash flow needs related to capital projects involving third party financial transactions, such as grants or reimbursements.

Inter fund loans may be considered in cases where a short term loan is needed to cash-flow a project that does not qualify for tax-exempt bond financing. An example of this situation, but not limiting to this case, is a future reimbursement by a grant or developer for project funding that needs to move forward prior to funds being available. This is similar to how the IRS allows the City to reimburse itself from future bond proceeds, except the funds are coming from a source other than tax exempt bonds. Inter fund loans may be considered when one fund has excess reserves (over policy requirements) that are not anticipated to be needed prior to repayment.

The inter fund loan shall be documented by City Council Resolution and shall define the following:

1. Source of the Funding
2. Use of the Funds (project)
3. Maximum Amount
4. Repayment Schedule
5. Interest accrual, consistent with City investment rates

The proposed inter fund loan shall be identified during the annual budget and CIP process as a funding source, and discussed with the Council Finance/Audit Committee prior to the Resolution being considered by City Council. Any changes to repayment terms shall be approved by City Council via Resolution and clearly identified in the budget document.

Debt Service Funds

The City shall maintain the debt service fund balance at 10% of annual debt service requirements OR a fund balance reserve as required by bond ordinances, whichever is greater.

The City shall maintain a separate Debt Service Fund for any taxable bonds. This debt service fund shall have a reserve requirement separate from the tax –exempt debt service fund to be defined in the bond documents as bonds are issued.

Internal Service Funds

1. Fleet Replacement Fund-The Fleet Replacement Fund reserve will be maintained based upon a lifecycle or useful life replacement plan to ensure adequate fund balance required for systematic replacement of fleet vehicles. Fund Balance shall not be less than 10% of the total inventory asset value.
2. Technology Replacement Fund- The High Technology Replacement Fund reserve will be maintained based upon a lifecycle or useful life replacement plan to ensure adequate fund balance required for systematic replacement of technology. Fund Balance shall not be less than 10% of the total inventory asset value.
3. Employee Benefits Fund- The Employee Benefits Fund is funded through City and employee contributions. Estimated costs shall be determined during each budget year and the contributions adjusted accordingly. This fund should carry a reserve equal to the maximum amount that the City is liable for before aggregate stop loss coverage kicks in. If the reserve drops below this level, the City should increase contributions to the fund over the next 2 years, until the aggregate stop loss liability is met.

Special Revenue Funds

Tourism Fund is supported by a 7% City tax on hotel occupancy within the City, which can fluctuate based on changes in the economy. A fund balance of no less than 10% of budgeted occupancy tax collections shall be maintained in the fund.

Economic Development Corporations

As sales taxes fluctuate due to changes in the economy, the SLDC and SL4B Corporations shall maintain a minimum fund balance of 15% of budgeted annual sales tax revenues.

CAPITAL EXPENDITURES AND IMPROVEMENTS

City staff will review and monitor the state of the City's capital equipment and infrastructure annually, setting priorities for its replacement and renovation based on needs, funding alternatives, and availability of resources.

Capitalization Threshold for Tangible Capital Assets

Tangible capital items should be capitalized only if they have an estimated useful life of at least two years following the date of acquisition or significantly extend the useful life of the existing asset and cannot be consumed, unduly altered, or materially reduced in value immediately by use and has a cost of not less than \$5,000 for any individual item.

The capitalization threshold of \$5,000 will be applied to individual items rather than to a group of similar items, (i.e.: desks, chairs, etc.) unless doing so would have a material impact on financial reporting. The capitalization threshold for infrastructure will be \$50,000 or more.

GASB requires software to be capitalized if criteria described in GASB Statement 51 (Accounting & Financial Reporting for Intangible Assets) is met. Internally developed or contracted development of or off-the-shelf and then modified software should be capitalized given cost & useful life threshold is met. Other licensed software implemented without modification or minimal modification is not capitalized.

To maintain adequate control over non-capitalized tangible items, items costing \$1,000 to \$4,999 will be monitored and tracked through the City's financial software system.

Five-Year Capital Improvement Plan (CIP)

The City shall annually prepare a five-year capital improvement plan based on the needs for capital improvements and equipment, the status of the City's infrastructure, replacement and renovation needs, and potential new projects. Capital projects are improvements or additions to the City's physical plant/facilities and become part of the City's asset inventory. Capital projects can be further categorized into land, buildings, improvements other than buildings, and infrastructure, which includes roads, sidewalks, bridges, utility lines, etc. Capital costs typically consist of preliminary design, final design, and construction, and may involve the acquisition of land or easements. For every project identified in the plan, a project scope and project justification will be provided. Also, project costs shall be estimated, funding sources identified and annual operation and maintenance costs computed.

Citizens, Parks Board and the Planning and Zoning Commission will be provided opportunities to review the list of CIP projects for the Five-Year Capital Improvement Plan and may suggest additions and/or changes to the plan as appropriate. Pursuant to the City Charter, the Planning & Zoning Commission makes recommendations to the City Manager and the City Council on the City's Five-Year Capital Improvement Plan.

The City Manager is charged with recommending a Capital Improvement Plan to City Council. Projects submitted, either by staff, through a neighborhood or citizen request, or through joint participation, will be reviewed in conjunction with the entire capital improvement program and submitted to City Council for final consideration. The Five-Year Capital Improvement Plan shall be filed and year one funding approved with the annual budget. Years two through five are for planning purposes only, and may move up, back, or be phased as the project becomes more refined based on preliminary engineering and design work gets completed.

The Five-Year CIP shall be limited to the affordability limits identified in the long-range financial plans of the City, taking into consideration pay-as-you go funding debt capacity, operating costs, etc. Affordability shall be determined by the revenue assumptions used to build the five year forecast.

Projects that cannot be funded in the Five Year CIP using the affordability assumptions will be included in the CIP for future reference as an appendix of unfunded requests, and considered for future funding or a bond referendum

The City will establish and maintain Capital Project Funds based on various funding sources as identified below:

- General Capital Projects (non-bond) - includes projects funded from general fund transfers, grants and other funding sources.
- Corporation Capital Projects (non-bond)- supported by funding resolutions of the Sugar Land Development Corporation and Sugar Land 4B Corporation. Projects must qualify for funding by the respective corporation and meet all applicable public notice and public hearing requirements.
- General Capital Projects (tax-exempt bond funds)- supported by proceeds of tax exempt bonds that are to be repaid from property taxes and interest earned thereon; projects funded from this source must be consistent with the uses identified in the bond documents.
- Taxable Bonds Capital Projects- supported by proceeds of taxable bonds that are to be repaid from sources other than property taxes.
- Federal Grant Funded Capital Projects- funding for federally funded projects, which have additional requirements that must be met; this includes matching funds from the state, which are pass-through from federal funding sources.
- Utility Enterprise CIP (non-bond) - includes projects funded from revenues of the utility system. Includes rehabilitation of infrastructure to extend its useful life. Revenues are budgeted as a transfer from the Utility System Operating fund.
- Utility Enterprise CIP (bond funds) - supported by proceeds of tax-exempt bonds that are to be repaid from enterprise utility revenue sources. Bonds payable are recognized in the Utility Enterprise Fund as long term liabilities.
- Surface Water CIP (non-bond)- includes projects funded from revenues of the surface water fund. Includes projects that facilitate the objectives of the Groundwater Reduction Plan. Revenues are budgeted as a transfer from the Surface Water Operating fund.
- Surface Water CIP (Bond Funds)- supported by proceeds of tax-exempt bonds that are to be repaid from the Surface Water Enterprise Fund. Bonds payable are recognized in the Surface Water Enterprise Fund as long term liabilities.
- Airport Enterprise CIP (non-bond) - includes projects funded from revenues of Sugar Land Regional Airport and outside funding sources. Revenues are budgeted as a transfer from the Airport Operating fund or as grants from third parties (FAA/TxDOT).
- Airport Enterprise CIP (bond funds) - supported by proceeds of tax-exempt bonds that are to be repaid from enterprise airport revenues. Bonds payable are recognized in the Airport Enterprise Fund as long term liabilities.

Annually, through the budget process and at year-end, projects are to be reviewed and if identified as complete will be closed according to the Project Close-out Procedures by Budget and Engineering, and any remaining funds closed to the CIP fund balance, which can then be re-appropriated during the next fiscal year capital budget. Funds remaining from bond proceeds will only be used in accordance with the legal use of those funds.

Appropriations for capital projects are for the life of the project; therefore, re-appropriation of capital funding for budgeted projects will not be necessary.

1. Infrastructure Evaluation and Replacement/Rehabilitation

Water, wastewater, drainage, street lighting, streets and sidewalks, municipal facilities, and other infrastructure are fundamental and essential functions for public health and safety, environmental protections and the economic well-being of the City. As a result, the City's CIP should be focused on ensuring that infrastructure is replaced or rehabilitated as necessary to protect the City's investment, to minimize future replacement and maintenance costs, extend the useful life of the asset, and to maintain existing levels of service and accommodate growth.

Infrastructure will be replaced or rehabilitated at the end of its useable service life if it is financially feasible to do so.

2. If upgrades are warranted to meet current design standards, a cost/benefit analysis will be performed. (See Infrastructure Evaluation Policy)

Community Redevelopment Projects

A Community Redevelopment Project is a capital project approved, funded, and implemented within an identified neighborhood for the purpose of upgrading public infrastructure to an established standard without regard to the remaining serviceable life of the infrastructure. Requests will be reviewed and prioritized in conjunction with the entire capital improvement program and within the City's financial ability for pay-as-you-go funding, not to exceed ½ of one percent of the total City operating budget. There will be a dollar for dollar match to City funds from non-City third-party sources. (See Capital Improvement Projects for Community Redevelopment Policy)

Joint Capital Improvement Projects

The City will establish guidelines for City participation in Joint Capital Improvement Projects with community based organizations that would either add to or enhance the City's Five-Year Capital Improvement Plan (See Resolution 14-27, Policy No. 5000-09 Joint Capital Improvement Projects with Community Based Organizations using Sugar Land 4B Funds)

The projects must benefit the general public and be located in the public right of way. In the proposed budget, \$200,000 will be set aside annually for the City's participation in these type projects, funded through the Sugar Land 4B Corporation, pending funds availability and subject to approval by the City Council. A maximum of \$75,000 will be contributed to any one project, and in no case will the Corporation contribute over 50% of project funding. The request will be reviewed, verified to ensure the request meets the criteria set forth in the policy, and prioritized within the financial ability of the Sugar Land 4B Corporation.

Replacement of Capital Assets on a Regular Schedule (Fleet and Technology)

The City shall annually prepare a schedule for the replacement of its fleet and high technology capital assets. Funding for the replacement of these assets will be accomplished through the use of an annual depreciation structure charged to each participating fund at 100% of annual depreciation based on lifecycle or useful life of the asset. Within the resources available each fiscal year, the City shall replace these assets according to the Fleet and High Technology Replacement Policies.

Capital Expenditure Financing

The City recognizes that there are three basic methods of financing its capital requirements: Funding from current revenues; funding from fund balance/working capital as allowed by the Fund Balance/Working Capital Policy; or funding through the issuance of debt. Types of debt and guidelines for issuing debt are set forth in the Debt Policy Statements.

Pay-As-You-Go Capital Improvements

1. The City will pay cash for capital improvements within the financial affordability of each fund versus issuing debt when funding capital improvements and capital purchases. This will reduce/minimize the property tax and utility rate impacts on Sugar Land citizens.
2. Pay-as-you-go projects shall be budgeted based on funding available in the section on Revenues
3. Unless CIP balances are sufficient to pre-fund pay-as-you-go projects, scheduling of pay-as-you-go capital improvement projects shall coincide with the collection and accumulation of sales tax and system revenues. CIP projects shall be initially scheduled based on the budgeted accumulation of funding. CIP projects funded by pay-as-you-go funding must receive approval from the Budget Office before they begin, to ensure funding is available.

Capital Projects Management

Capital project status reports shall be completed by project managers monthly, and project status and issues shall be reported to the City Council quarterly.

- a. Project Close Out- A project will be closed once the original scope of the stated project has been completed as determined by Engineering and the project manager.
- b. Remaining Funds- Funds left in a project after completion shall be closed out and fall to the CIP fund balance. Engineering, Accounting and Budget will identify and close out projects on a quarterly basis to facilitate identification of funds that can be used for other projects.
- c. Annual rehabilitation projects- unused funds budgeted for annual rehabilitation and repairs will close out at the end of each fiscal year if not encumbered.

DEBT

Establish guidelines for debt financing that will provide needed facilities, land, capital equipment and infrastructure improvements while minimizing the impact of debt payments on current and future revenues.

Use of Debt Financing

Debt financing, to include general obligation bonds, revenue bonds, certificates of obligations, certificates of participation, lease/purchase agreements, and other obligations permitted to be issued or incurred under Texas law, shall only be used to purchase capital assets that cannot be prudently acquired from either current revenues or fund balance/working capital and to fund infrastructure improvements and additions. Debt financing is utilized to better ensure inter-generational equity by spreading payments of assets and infrastructure over their useful lives. Debt will not be used to fund operating expenditures.

The City will pay cash when possible for capital improvements within the financial affordability of each fund versus issuing debt when funding capital expenditures and capital improvements. Projects that are rehabilitative in nature shall be earmarked for funding from cash instead of debt when possible. (This is not intended to include reconstruction projects that significantly extend the useful life of an asset.) Cash sources include, but are not limited to general fund one-time revenues, utility and airport system revenues, economic development corporation funding, developer fees, inter-local agreements, and state and federal grants.

Bond Ratings

In evaluating the issuance of additional debt to finance projects, the City shall take into account the statements of the rating agencies in regards to the City's financial condition.

Ratings reflect the assessment of the following factors, and these must be evaluated to determine the impact of potential bond issues:

- Local economic activity
- Strong financial policies as evaluated under the Financial Management Assessment methodology
- Budgetary performance & flexibility
- Total liquidity and reserve balances
- Debt and contingent liability- evaluation of debt carrying costs as a percent of expenditures
 - With adjustments for self-supporting debt
- Impact of future debt issuance on bond ratings/debt profile and outlook

Affordability

The City shall use an objective analytical approach to determine whether it can afford to issue new general-purpose debt, both General Obligation bonds and Certificates of Obligation. This process shall compare City accepted standards of affordability to the current values for the City. These standards may include debt per capita, debt as a percent of taxable value, taxable value per capita, and tax rate. The process shall also examine the direct costs and benefits of the proposed expenditures. In addition, the analysis will evaluate the capacity within the General Fund to take on the operating expenditures associated with the completion of the proposed capital improvements. When a project will have a significant impact on the operating budget, the tax rate shall be shifted from debt service to maintenance & operations to support the increased expenditures. Further debt capacity shall be evaluated based on the remaining debt service tax capacity. The decision on whether or not to issue new debt shall be based on these costs and benefits, current conditions of the municipal bond market, and City's ability to "afford" new debt as determined by the aforementioned standards.

Debt Capacity

The City shall complete an annual debt capacity assessment to ensure that proposed debt is affordable and contributes to the financial strength of the City. The debt capacity is the upper limit on the dollar amount of capital improvements that the City can afford to fund from debt.

Debt capacity calculations for long-term planning shall assume market rates for the average annual interest costs at the time the capacity is determined. The analysis shall not assume future refunding of any outstanding bonds and shall consider both debt service requirements on current and proposed debt.

For property tax supported debt, maximum capacity shall be determined by an amount of annual debt service that the City can absorb within the proposed tax rate allocation for debt based on assumed growth in assessed valuation.

For revenue debt, maximum capacity shall be determined by the amount of annual debt service that the City can absorb within a proposed rate structure that has been reviewed with City Council and which can support the proposed debt within the additional bonds test as defined in the revenue bond covenants. The City shall not exceed debt capacity as defined through bond covenants or fall below bond coverage ratios for additional revenue bonds.

Factors that will be included in the annual debt capacity determination shall include:

- Existing debt obligations

- Evaluation of revenue and expenditure trends
- Various measures of debt burden on the community
- Debt per capita
- Debt to assessed value ratio
- Taxable value per capita
- Statutory or constitutional requirements
- Market factors such as interest rates, credit ratings or market status

Certificates of Obligation (CO's)

Certificates of Obligation may be issued without voter approval to finance any public works project or capital improvement, as permitted by State law. However, it is the policy of the City to utilize Certificates of Obligation to finance public improvements in certain circumstances and only after determining the City's ability to assume additional debt based on the standards identified above.

Circumstances in which Certificates might be issued include, but are not limited to the following:

- The City may issue CO's when there is insufficient funding on a general obligation bond-financed capital improvement;
- The City may issue CO's when conditions require a capital improvement to be funded rapidly rather than waiting for a GO bond election;
- The City may issue CO's for projects when the City can leverage dollars from others to reduce the City's capital cost for a community improvement;
- The City may issue CO's for projects when there is no other funding source available and the project is determined to be in the best interest of the City.
- The City may issue CO's if it would be more economical to issue Certificates of Obligation rather than issuing revenue bonds; and
- The City may issue CO's for projects for which the City will be reimbursed by Developer (principal plus interest)

General Obligation Bonds (GO's)

General Obligation bonds require voter approval. When the list of unfunded projects contains projects that the City Council wishes to fund but cannot afford, then the City will consider taking a GO Bond Proposition(s) to the voters.

1. Bond Elections-

- a. Timing of general obligation bond elections shall be determined by the inventory of current authorized, unissued bonds remaining to be sold and the City's ability to fund projects in the five-year CIP
 - b. The total dollar amount of bond election propositions recommended to the voters may not exceed the City's estimated ability to issue the bonds within a seven-year period after the election passes.
 - c. An analysis showing how the new debt combined with current debt impacts the City's tax rate and debt capacity will accompany every bond issue proposal. The analysis will also include the estimated impact on the operations and maintenance portion of the tax rate.
2. General Obligation bonds must be issued to accomplish projects identified in the bond referendum and associated material.

3. General Obligation bonds must be issued for projects that are consistent with the wording in the bond propositions.
4. In the tax year after a GO bond election, the tax rate is to be increased by the projected impact - before any projects from the GO bond election are funded in the CIP. If the tax rate is not adjusted to fully fund approved projects, the projects will not be included in the CIP nor bonds issued.

Revenue Bonds

For the City to issue new revenue bonds, revenues, as defined in the ordinance authorizing the revenue bonds in question, shall be a minimum of 125% of the average annual debt service and 110% of the debt service for the year in which debt requirements are scheduled to be the greatest. Annual adjustments to the City's rate structures for enterprise funds will be made as necessary to maintain the coverage factor.

When the City issues CO's for enterprise fund projects, the City shall prepare a five-year financial plan to ensure that the enterprise fund maintains appropriate reserves and coverage requirements without overly burdening rates and user fees.

General purpose reserves in the Surface Water Fund shall be maintained at levels high enough to meet debt service payments, if pledged revenues should fall short of projections, in addition to serving as a normal operating reserve. Future Surface Water projects will be funded through the issuance of revenue bonds.

Debt Structures

- The City shall normally issue bonds with a life not to exceed 25 years for general obligation bonds and 25 years for revenue bonds, but in no case longer than the useful life of the asset.
- The City shall seek level or declining debt repayment schedules and shall seek to retire 50% of the total principal outstanding within 10 years of the year of issuance.
- There should be no debt structures that include increasing debt service levels in subsequent years, with the first and second year of a bond payout schedule the exception or as special situations may warrant.
- There shall be no "balloon" bond repayment schedules, which consist of low annual payments and one large payment of the balance due at the end of the term.
- There shall always be at least interest paid in the first fiscal year after a bond sale and principal payments starting generally no later than the second fiscal year after the bond issue.
- Normally, there shall be no capitalized interest included in the debt structure except for debt issuances reimbursing developers for infrastructure, which shall not exceed 2 years of capitalized interest.

Debt Refunding

The City's financial advisor shall monitor the municipal bond market for opportunities to obtain interest savings by refunding outstanding debt. As a general rule, the net present value savings of a particular refunding should exceed 3.0% of the refunded maturities unless (1) a debt restructuring is necessary or (2) bond covenant revisions are necessary to facilitate the ability to provide services or to issue additional debt.

Interest Earnings and Remaining Bond Proceeds

Interest earnings on bond proceeds will be limited to funding changes to the bond financed Capital Improvement Plan in compliance with the voted propositions, cost overruns on bond projects, or be applied to debt service payments on the bonds issued. Issued but unspent bond proceeds may be appropriated for projects consistent with the ballot language after completion of projects identified in the approved bond propositions.

Sale Process

The City shall use a competitive bidding process in the sale of debt unless the nature of the issue warrants a negotiated sale. The City will utilize a negotiated process when the issue is, or contains, a refinancing that is dependent on market/interest rate timing. The City shall award the bonds based on a true interest cost (TIC) basis. However, the City may award bonds based on a net interest cost (NIC) basis as long as the financial advisor agrees that the NIC basis can satisfactorily determine the lowest and best bid.

Underwriting Syndicates

In response to the MSRB Rule G-17, which recognizes that the motivations of an underwriter may not be consistent with the best interest of the City, the City shall refer underwriters to its Municipal Advisor to review potential refunding opportunities. The City's municipal advisor is prohibited from underwriting the City's bonds while under contract with the City for municipal advisory services, and for a period of one year after termination of the municipal advisory contract.

The City will consider past participation and results of competitive City of Sugar Land and component unit bond sales when engaging one or more firm to underwrite a negotiated bond transaction.

Rating Agency Presentations

Full disclosure of operations and open lines of communications shall be maintained with the rating agencies. City staff, with the assistance of financial advisors, shall prepare the necessary materials and presentation to the rating agencies. Credit ratings will be sought from one or more of the nationally recognized municipal bond rating agencies, currently Standard & Poor's and Fitch Ratings Inc., as recommended by the City's municipal advisor.

Bond Ratings

The City will prudently manage the General, Economic Development Corporations, and Enterprise Funds and attempt to issue and structure debt to help maintain or increase the current bond ratings.

Lease/Purchase Agreements

The City will use lease/purchase agreements for capital items (such as fire trucks) when it is cost-efficient and provides for more attractive terms than issuance of bonds.

CASH MANAGEMENT AND INVESTMENTS

To maintain the City's cash in such a manner so as to ensure the absolute safety of principal, to meet the liquidity needs of the City, and to achieve the highest possible yield in compliance with the Public Funds Investment Act (Chapter 2256 of the Local Government Code or equivalent provision) and the City's Investment Policy & Strategy, as adopted annually by City Council.

Investment Policy

All aspects of cash/investment management shall be designed to ensure safety and integrity of the City's financial assets. Cash/Investment management activities shall be conducted in full compliance with prevailing local, state, and federal regulations. Please reference the City's Investment Policy as adopted annually by City Council.

The City shall design and establish policies relating to a variety of cash/investment management issues, such as the eligibility and selection of various broker/dealers, safekeeping requirements, collateral requirements, delivery

versus payment requirements, weighted average maturity requirements and such other aspects of the program, which necessitate standard setting in pursuit of appropriate prudence and enhanced protection of assets.

Investment Strategy

The City of Sugar Land maintains a consolidated portfolio in which it pools its funds for investment purposes. The City's investment program seeks to achieve safety of principal, adequate liquidity to meet cash needs, and reasonable yield commensurate with the preservation of principal and liquidity. Refer to the City's Investment Strategy as adopted by City Council annually for detail.

Interest Income

Interest earned from investments shall be distributed to the funds from which the funds were provided.

Arbitrage Investments and Reporting

The City's investment position as it relates to arbitrage is as follows: Investments on bond proceeds will be made with safety of principal and liquidity in mind, but with a competitive rate of return. Investment of bond proceeds will be clearly tracked and investment earnings recorded for arbitrage purposes.

Depository Bank

The City of Sugar Land will select its official bank depository through a formal bidding process in order to provide the City with the most comprehensive, flexible, and cost-effective banking services available. The City will at a minimum, bid depository services every five years. Only officials authorized by the City Council through the depository contract may open accounts in the name of the City or its component units.

Collateralization of Deposits

The City of Sugar Land shall have pledged collateral held at an independent third-party institution and evidenced by a written receipt.

The value of the pledged collateral should be marked to market monthly and shall be at least 102 percent of par or market value of the investments, whichever is greater. The City's depository bank monitors the required collateral and makes necessary adjustment to increase or decrease it.

Substitutions of collateral shall meet the requirements of the collateral agreement and have prior written approval. Collateral shall not be released until the replacement collateral has been received.

The pledge of collateral shall comply with the City's Investment Policy.

GRANTS

The City will seek, apply for, and effectively administer federal, state and local grants, which support the City's current priorities and policy objectives.

Grant Guidelines

The City shall apply and facilitate the application for only those grants that are consistent with the objectives and high priority needs identified by Council and City Management.

Grant funding will be considered to leverage City funds. Inconsistent and/or fluctuating grants should not be used to fund ongoing programs.

The potential for incurring ongoing costs, to include assumptions of support for grant-funded positions from local revenues, will be considered prior to applying for a grant.

Grant Review and Acceptance

All grant submittals shall be reviewed for their cash match requirements, their potential impact on the operating budget, and the extent to which they meet the City's goals. If there is a cash match requirement, the source of funding shall be identified prior to application. (Refer to City's Inter-Departmental Grant Policy AC104)

All grants must be reflected in the budget. Grants may be officially accepted by action of the City Council during budget adoption or with a budget adjustment. If the funding is not already included in the annual budget, the budget shall be amended to reflect revenues and expenditures associated with the grant.

Grant Termination and/or Reduced Grant Funding

In the event of reduced grant funding, City resources will be substituted only after all program priorities and alternatives are considered during the budget process, unless the City is obligated through the terms of the grant to maintain the positions.

The City shall terminate grant-funded programs and associated positions when grant funds are no longer available, and it is determined that the program no longer supports City goals and/or is no longer in the best interest of the City, unless the City has obligated itself through the terms of the grant to maintain the positions after the grant period ends.