



Local Agency Financial Policies and Practices

Financial policies can provide a solid foundation for sound public agency fiscal practices. Adopted by the governing body, such policies provide:

- A means through which the governing body can communicate its collective policy judgments and goals to staff, the public and others.
- Direction to staff and standards against which
 - 1) current practices can be measured and
 - 2) proposals for changes in practices can be evaluated.

Ratings agencies (who assess local agencies' credit for borrowing) also look at local agencies' financial policies; well crafted polices can mean higher rating grades which can translate into lower borrowing costs.

QUESTIONS TO ASK

Financial Policies

- Does the agency have written financial policies?
- If so, what do they cover? See sidebar on next page for a checklist of possible topics.
- How often does the governing body review them?
- With respect to each policy, is it clear who is responsible for implementing that policy?

- What procedures does management use to make staff aware of such policies? What training does staff receive to allow them to competently implement such policies?
- How does the agency monitor compliance with such policies?

Financial Practices

- Are agency accounting policies and procedures documented in writing?
- What kinds of practices does the agency use (sometimes referred to as "internal controls") to make sure that the agency has systems for cross checks to minimize the risk of mistakes or maximize the likelihood that misconduct is detected?
- Does agency financial staff participate in relevant professional organizations to keep abreast of developments in the field and best practices?
- Are agency financial staff familiar with and do they adhere to the codes of ethics applicable to their professions? For example, both the California Society of Municipal Finance Officials¹ and the California Municipal Treasurers Association² have codes of ethics.

CHECKLIST OF FINANCIAL POLICY TOPICS³

Local agencies have various—and various levels—of financial policies. Some policies relate to big picture, strategic topics (for example, budget policy, long-range planning and debt policy); others are very specific and practical policies (for example, credit card policies and expense reimbursement).

Having a range of policies (from big picture to practical and operational) helps an agency to chart a wise course financially and avoid operational missteps. Whether a specific policy makes sense given the nature and scope of an agency's operations will vary.

Financial Planning Policies.⁴

- **Budget Policy.** Such a policy commits to a balanced operating budget (and defines what that is) and requires that decision-makers be alerted when deviations are either planned or otherwise occur.
- **Long-Range Planning.** Such a policy supports financial analysis and strategies to assess the long-term implications of current and proposed capital improvement needs, cost of services, operating budgets, budget policies, cash management and investment policies, program and assumptions. For example, a capital improvement plan enables the agency to detail the agency's plans and relative priorities for making improvements to and replacing capital facilities (a process that normally takes years to complete).⁵
- **Asset Inventory.** Such a policy requires an up-to-date listing of all major capital assets. The policy can also require an assessment of asset condition and a plan for replacing assets (sometimes referred to as a "capital plan"). The definition of what constitutes a "major" asset is established by local policy, as is the determination of how often the inventory is to be updated.
- **Long-Range Planning for Pension and Other Post-Employment Benefit Costs.** Such a policy analyzes how the agency will meet the future costs of agency employee pensions and other employee benefit obligations.

- **Reserve and Other Fund Balances.** Such a policy enables decision-makers to maintain a prudent level of resources to protect against a need to reduce service levels or increase revenues due to revenue shortfalls or unpredicted one-time expenses. Specific kinds of reserves can also enable an agency to set aside moneys to replace assets (for example, fleet replacement reserves).

Revenue Policies.⁶ These policies help decision-makers understand and manage revenue flows.

- **Revenue Diversification.** Such a policy encourages a diversity of revenue sources to protect the agency against fluctuations in individual sources, such as sales taxes, which can rise and fall dramatically with the general economy.
- **User Fees and Charges.** Such policies establish the extent to which users of agency services are expected to cover the cost of providing the service and how those costs are determined. Note that most fees may only be used for the purposes for which they were collected and may not exceed the cost of providing the service for which the fee is charged.⁷ Such policies also can provide for regular review of fee levels and calculation methods to assure that the agency meets its objectives relating to cost-recovery on an ongoing basis.

- **One-Time and Unpredictable Revenues.** A goal of such a policy is to encourage the use of one-time or unplanned revenues for one-time needs or reserve replenishment rather than for ongoing expenses.
- **Limited Purpose Revenues.** By law or policy, certain revenues must be spent for specific purposes (for example, proceeds from special taxes). This policy explains which funds are restricted and why, limits their use to those purposes, and explains how the agency tracks their use to ensure the funds are spent only on permissible expenses.

Expense Policies.⁸ These policies enable decision-makers to manage and monitor how the agency incurs expenses.

- **Financial Reporting.** Financial reports compare actual expense levels (and revenue levels) to those predicted in the agency’s budget. This policy specifies the content and frequency (for example, quarterly) of these reports to decision-makers and the public.
- **Debt Financing.** This kind of policy allows an agency to specify when it can use debt for either short- or long-term needs. The policy also establishes what levels of debt and debt service payments are appropriate for the agency. It can also be a tool for complying with ongoing disclosure requirements associated with the agency’s debt and monitoring compliance with those requirements.
- **Expense Reimbursement.** Such policies determine the circumstances under which elected officials and staff may be reimbursed for expenses incurred in the course of their service to the agency. This includes setting limits on certain kinds of expense levels (for example, meals and hotel rates) according to community standards. Policies also specify the kind of documentation that must be provided to demonstrate that the expense was incurred in compliance with the policy before an expense will be reimbursed. Agency counsel should review the policy for compliance with AB 1234 and other state laws.⁹

- **Credit and Purchase Card Use Policies.** The practice of issuing credit cards to agency officials and staff is increasingly rare because of the potential for misuse, either accidentally or intentionally. It can however, be useful to have one or more agency credit cards to make travel arrangements and the like. Some agencies also use purchase cards. A policy specifies controls to prevent misuse of such cards.¹⁰
- **Petty Cash Policies.** Such a policy provides guidelines and accountability mechanisms for day-to-day cash handling by the agency and its departments.

Cash Management and Investments. State law requires agencies to adopt an investment policy specifying how the agency may invest funds not needed for the agency’s immediate and short-term needs.¹¹ Such a policy allows the governing body to establish and keep current the agency’s investment philosophy and risk tolerance. Although well-defined policies are more than a list of allowed investments,¹² such policies should be reviewed by agency counsel to make sure that the agency’s investments and practices conform with state law.¹³

Purchasing/Procurement. These policies determine the processes the agency uses in determining with whom it does business (including under what circumstances contracts are competitively bid) and which staff have decision-making responsibility in that area. Such policies also typically specify how the opportunity to do business with the agency is to be announced, with the goal being to reach a widespread number of potential reputable and cost-efficient goods and services providers.

Endnotes

- 1 The California Society of Municipal Finance Official Code of Ethics can be found at: <http://www.csmfo.org/index.cfm?fuseaction=Detail&CID=4&NavID=154> .
- 2 The California Municipal Treasurers Association Code of Ethics can be found at: <http://www.cmta.org/?page=4> .
- 3 GFOA Recommendations: Adoption of Financial Policies, with cross references to National Advisory Council on State and Local Budgeting (NACSLB), <http://www.gfoa.org/downloads/budgetAdoptionofFinancialPolicies.pdf>.
- 4 GFOA Recommendations: Adoption of Financial Policies, with cross references to National Advisory Council on State and Local Budgeting (NACSLB), <http://www.gfoa.org/downloads/budgetAdoptionofFinancialPolicies.pdf>.
- 5 See GFOA website with long-term financial planning resources: http://www.gfoa.org/index.php?option=com_content&task=view&id=360&Itemid=186.
- 6 GFOA Recommendations: Adoption of Financial Policies, with cross references to National Advisory Council on State and Local Budgeting (NACSLB), <http://www.gfoa.org/downloads/budgetAdoptionofFinancialPolicies.pdf>.
- 7 See, for example, Cal. Gov't Code § 66016.
- 8 GFOA Recommendations: Adoption of Financial Policies, with cross references to National Advisory Council on State and Local Budgeting (NACSLB), <http://www.gfoa.org/downloads/budgetAdoptionofFinancialPolicies.pdf>.
- 9 See Cal. Gov't Code § 53232.2(b) (“If a local agency reimburses members of a legislative body for actual and necessary expenses incurred in the performance of official duties, then the governing body shall adopt a written policy, in a public meeting, specifying the types of occurrences that qualify a member of the legislative body to receive reimbursement of expenses relating to travel, meals, lodging, and other actual and necessary expenses.”). See also <http://www.leginfo.ca.gov/calaw.html> for additional information on what such policies must include.
- 10 See GFOA Best Practices: Purchasing Cards, <http://www.gfoa.org/downloads/PurchasingCardFINAL.pdf> for suggested practices for preventing and detecting abuse.
- 11 See Best Practices for Treasury Management, Government Finance Review (April 2000), available at <http://www.gfoa.org/downloads/CASHTreasuryapr00.pdf>. The California Municipal Treasurers' Association offers sample investment policies at <http://www.cmta.org/?page=39>.
- 12 Back to Basics: Making the Case for Investment Policies, *Government Finance Review* (August 2002) available at <http://www.gfoa.org/downloads/CASHInvestPol0802.pdf>.
- 13 See Cal. Gov't Code §53600 and following (note that an agency is not required to authorize the full range of all investments allowed by state law). See also <http://www.leginfo.ca.gov/calaw.html> for specific statutory language.

To access the Institute's resources financial management resources, including the complete version of this booklet, go to <http://www.ca-ilg.org/finance>.

This publication excerpt is a service of the Institute for Local Government (ILG) whose mission is to promote good government at the local level with practical, impartial, and easy-to-use resources for California communities. ILG is the nonprofit 501(c)(3) research and education affiliate of the League of California Cities and the California State Association of Counties. For more information and to access the Institute's resources financial management go to <http://www.ca-ilg.org/finance>.

The Institute welcomes feedback on this resource:

- *Email:* info@ca-ilg.org Subject: *Financial Management for Elected Officials: Questions to Ask*
- *Fax:* 916.444.7535
- *Mail:* 1400 K Street, Suite 205 ▪ Sacramento, CA ▪ 95814