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Reserve and Reserve Fund Policy

1. Purpose

The purpose of this Reserve and Reserve Fund Policy (Policy) is to provide guidance with respect to the development, maintenance and use of City of Greater Sudbury (City) reserves and reserve funds (reserves). It will establish guidelines, limits and conditions applicable to the reserves and reserve funds of the City.

The establishment of reserves assists in providing for the long-term financial stability and flexibility of the City, positions the City to respond to varying economic conditions and changes that affect the City's financial position, and ensures the organization continues with its ability to carry out its responsibilities.

2. Policy Statement

The organization actively manages reserves and reserve funds to ensure minimum fund balances are available. Council has flexibility to react to unanticipated opportunities and the ability to minimize annual changes in taxation or debt.

3. Principles of Reserves and Reserve Funds

All reserves must be established, maintained and used for a specific purpose mandated by this policy, statute, or City by-law.

The capital reserves are to be used for the future replacement or acquisition of capital assets.

The City shall strive to develop appropriate reserves and reserve funds to meet future financial obligations with respect to City equipment and infrastructure, fiscal needs and employee benefit obligations.

4. Scope / Application

Administrative criteria:

- reserves must have a unique Corporate purpose
- all reserve funds earn interest each year
- a minimum balance may be established for a reserve fund
- a time period shall be specified for the repayment or replenishment of each reserve fund to its specified minimum balance
- a business case shall be provided specifying the purpose, benefits and method of repayment for each proposed departmental use of a reserve fund

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Definitions

- 4.1. *Reserve* means funds set aside for a specific purpose and does not earn interest.
- 4.2. *Reserve Fund* means funds set aside for a specific purpose and earns interest.
- 4.3. *Obligatory Reserve Fund* means external sources of funds received but not yet spent or earned for the purpose it was received. Typically, these are funds are restricted to be spent in accordance with various funding agreements or legislation or acts such as the Federal Gas Tax funding agreement and Development Charges Act. Obligatory Reserve Funds are also known as deferred revenue on the annual financial statements.
- 4.4. *External Sources of Funds* includes government grants, donations and third-party financing. If these sources have external restrictions as to their use, they are to be recorded within an obligatory reserve fund or deferred revenue and not form part of a year-end reserve amount.
- 4.5. *Internal Sources of Funds* includes approved budget contributions; annual surplus contributions; and carryover of current year's budget funds that have been approved for a specific purpose but not expended during the year.
- 4.6. *Transfer* means funds moved between two or more reserves or reserve funds.
- 4.7. *Working Reserve* means staff have the delegated authority to spend funds from the reserve without Council approval when in accordance with the reserve fund by-law.
- 4.8. *Executive Director of Finance, Assets and Fleet* position is also known as the City Treasurer or Chief Financial Officer.

5. Objectives

Reserves shall be established and expended to achieve the following objectives:

- 5.1. Promotion of financial stability and flexibility (stable and predictable property tax levies)

The City recognizes that unstable and unpredictable property tax levies can adversely affect residents and businesses in Greater Sudbury. In order to maintain stable and predictable levies, the City will maintain sufficient reserves to buffer the impact of unusual or unplanned cost increases and revenue reductions over multiple budget cycles.

- 5.2. Provide for operating emergencies

The City is exposed to unusual operating emergencies resulting from inclement weather, catastrophic events, environmental hazards and so on. It may not be feasible, or cost-effective, to absorb the costs of such emergencies during one

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budget cycle. The City will maintain adequate reserves to mitigate such emergencies, extensive service interruptions, and manage risks to infrastructure and public safety.

5.3. Financing for capital assets and projects

Use of reserves for financing new capital assets is an effective means of matching one-time funds to one-time capital projects. In addition, the City requires financial resources to quickly respond to opportunities that could provide capital infrastructure through private or public sector partnerships, and other alternative service delivery methods.

5.4. Safeguard and maximize existing assets

The City has an inventory of specialized machinery, equipment and technology systems necessary for the efficient delivery of services to the public, which need to be replaced on well-defined lifecycle standards. The City also has a need to provide insurance against unforeseen losses of these and other assets and claims against its assets where it is found legally liable.

5.5. Facilitate Long-Term Financial Planning

Reserves are essential to sound long-term financial planning in order to manage risk as well to mitigate higher property tax levies in years where one-time costs are expected or may occur.

It would also enable funds to be set aside to pay for future obligations that are known to occur such as sick leave, post-employment benefits, WSIB, election and so on.

5.6. Adherence to statutory requirements

Reserve funds that are required to maintain funds received from others until earned or spent on the specific purpose as outlined in legislation or agreements are established as Obligatory Reserve Funds. Examples would include Federal Gas Tax, subdivision deposits, and development charges.

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6. General Criteria

6.1. Least cost to taxpayers

Reserves should support the least cost alternative in the long-term for delivering standards of service adopted by Council. This means they will be used to:

- Buffer the effects of large cost increases and revenue reductions and allow time to adjust City service costs or revenue generation to avoid unnecessary tax increases, and
- Provide internal capital financing which may be more cost-effective than external borrowing or leasing.

6.2. Fairness and equity to taxpayers

Reserves should serve to balance the impact of the operating costs and capital costs, on both current and future taxpayers by:

- Applying reserves derived from one-time revenue sources to one-time capital or operating projects.
- Applying reserve funds and current revenues in a ratio, which recognizes the appropriate sharing of savings from current taxpayers with contributions from future taxpayers (this will likely require repayment of all or a portion of, reserves from future rates or user fees).

6.3. Meet statutory and legal requirements

Reserves must meet the requirements of grant funding agreement, federal statutes, acts, City by-laws or any other contract or judgment enforceable by law.

6.4. Meet accounting standards

Reserves must meet generally accepted accounting principles (GAAP) and accounting standards applicable to local governments (PSAB).

7. Methodology

This policy is intended to ensure funds are available for each of the City's reserves as set out in the Reserves and Reserve Funds By-law to fund both operational and capital expenditures. At this point, this policy excludes deferred revenues (also known as obligatory reserve funds).

Reserves and Reserve Funds are grouped into the following categories:

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- Operating
- Capital
- Statute (Obligatory)

An operating reserve/reserve fund is generally used to stabilize or mitigate the impact of fluctuations in operating costs and revenues or to accumulate funds for future or contingent liabilities. Capital reserve funds are used to fund capital works and are invested by the City until required for use thereby earning interest.

7.1. General Policy

- Reserve Funds that earn interest are to be invested in accordance with the City's Investment Policy. The interest earned remains within the respective reserve funds in order to be used for the specified purpose. This enables the funds set aside to grow in relation to inflation and rising costs.
- Transfers from reserves must not deplete the reserve below the minimum target unless recommended by the Executive Director of Finance, Fleet and Assets and it can be reasonably demonstrated that future sources of revenue will provide sufficient funding to restore the reserve to a minimum balance.
- All approved funding must be used for the specific purpose as outlined in the reserve request, unless Council directs otherwise.
- All spending from respective reserves and reserve funds must be approved by Council, unless it is noted as a working reserve or as noted in the by-law.
- Reserves should never have a negative balance. A plan approved by the Executive Director of Finance, Assets and Fleet should be made if a reserve is below an appropriate minimum balance.
- All existing reserves shall follow the established minimum and maximum balances as identified in Appendix A (which will be incorporated into the by-law).

7.2. Establishment and Modification

- Reserves can be established through inclusion in the annual operating or capital budget, which is approved by Council, or through a separate resolution of Council. The Reserves and Reserve Funds By-Law will be amended on a periodic basis to reflect these new reserves.
 - An Exception is for Obligatory Reserve Funds which will be created when required to be in accordance with funding agreement, contracts or Acts. Staff will notify Council of these changes on the annual update report to Council or the Finance & Administration

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Committee and the Reserve and Reserve Fund By-Law will be amended on a periodic basis.

- All new reserve requests must:
 - Be established with a specific purpose for which the reserve funding is intended. New reserve requests shall include the correlation with the City's Strategic Plan and/or the City's Long-Term Financial Plan. Each request shall link to specific pillars within the Strategic Plan and/or the financial policies outlined in the Long-Term Financial Plan in order for a new reserve to be created. All funds within a reserve are considered committed for the specific purpose as outlined in the reserve request, unless Council directs otherwise.
 - Designate as to whether the reserve is capital or operating, or both.
 - Identify funding sources and use of funds from the reserve.
 - Identify a minimum balance. A minimum balance ensures that each reserve fund is not depleted to where it is ineffective in serving its intended purpose.
 - Identify the consequences of not creating the reserve (e.g. risks, possible alternatives and consequences).
- Repayment or replenishment of each new reserve to its specified minimum or fixed amount shall be in accordance with Section 8.4 of this policy.
- Year-end surpluses of each new reserve shall be transferred out of the reserve in accordance with Section 8.4.

7.3. Investment

- Reserves shall be invested for a term that will not exceed its expected date of need.
- Reserves are to be invested in accordance with the City's Investment Policy.
- Interest earned on reserves shall be recognized as revenue in the operating budget; whereas interest earned on reserve funds shall be recognized in each specific reserve fund.
- Interest earned or accrued each month is credited to each reserve fund, based on its balance at the previous month-end.
- Interest enables the reserve funds to keep in line with cost increases and that sufficient funds are available when required.

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7.4. Contributions to and Withdrawals from Reserve Funds

- Contributions to and withdrawals from reserves shall be made in accordance with applicable resolutions, by-law and this Policy.
- Contributions to and withdrawals from reserves and reserve funds shall be approved by Council as part of the annual budget process, or specifically by resolution with the following exceptions:
 - Direct contribution to obligatory reserve funds such as development charges revenue;
 - Transfers that are a direct result of Council approved by-laws or resolutions such as annual operating surplus or deficit as part of Operating Budget Policy and the Reserves and Reserve Fund By-law, or the Capital Budget Policy;
 - Transfer of funds between reserves and reserve funds based upon adequacy analysis or other related information, at the discretion of the City Treasurer, or designate.

7.5. Lending / Temporary Borrowing Between Reserve Funds

Temporary borrowing from another reserve or reserve funds to cover a short-term operating or capital deficit or internal financing is permitted, when justified, adequately supported and authorized by Council.

The following conditions must be met in order to allow borrowing from reserve funds:

- Borrowing is consistent with the intended purpose of the reserve.
- A plan to repay the reserve fund (including any applicable interest) within a reasonable timeframe is required and documented.
- Within legislative requirements (ie. Development Charges Act).

7.6. Termination and Closure of Reserve Funds

If the purpose for which the reserve or reserve fund was created have been accomplished and the reserve or reserve fund is determined to be no longer necessary, a report shall be presented to Council with the recommendation on:

- The closure of the reserve or reserve fund
- The disposition of any remaining funds
- The necessary amendment to the Reserve and Reserve Fund By-law

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A resolution of Council will be required to close a reserve or reserve fund. The By-law establishing the reserve fund will be required to be repealed in order to close a Reserve Fund.

8. Standard of Care / Responsibilities

This section outlines how the reserves will be monitored and maintained by staff and Council. Overall, once City Council approves reserves and reserve funds by resolution and/or by-laws, the Executive Director of Finance, Assets and Fleet (Treasurer) shall have overall authority for the reserves and reserve funds managed by the City.

City Council shall:

- In accordance with the Municipal Act 2001, Section 224 develop and evaluate policies, ensure that administrative policies, practices and procedures and controllership policies, practices and procedures are in place and maintain the financial integrity of the municipality.
- Approve transactions to and from reserves and reserve funds through the budget process or by specific resolution or by-laws.

The Executive Director of Finance, Assets and Fleet (or designate) shall:

- Develop and update this Policy as necessary and present changes to Council;
- Ensure that the principles and requirements contained in this Policy are applied consistently across all departments;
- Perform the transfers to and from reserves and reserve funds as authorized by Council through a resolution and/or by-law;
- Recommend strategies for the adequacy of reserves including target levels;
- As part of the reporting to City Council, review and report on the adequacy and continuing need for reserves managed by the City;
- Preparation and presentation of reports and/or by-laws associated with the establishment, monitoring, or termination of reserves;
- Updates the City's long-term financial plan with consideration of appropriate reserves to effectively meet the City's operating and capital budget financing needs;
- Ensure reserves managed by the City are in line with senior government statutes and agreements and other pertinent policies.

9. Reporting

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The Treasurer or designate shall prepare the following reports regarding reserves managed by the City:

- Annual Audited Financial Statements – the balances of reserves and reserve funds along with comparisons to minimum levels and adequacy of reserve fund levels shall be included within the Annual Report.
- Budget Document – the annual budget document shall include total reserve fund balances and forecasted amounts based on staff recommendations within the tabled Budget document.
- Development Charges (DC) Reserve Funds Report – an annual report detailing pertinent information regarding DC reserve funds shall be presented to Council as required by the Development Charges Act, 1997, as amended.