

**CITY OF CASTROVILLE, TEXAS
FINANCIAL MANAGEMENT POLICIES**



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CITY OF CASTROVILLE, TEXAS

FINANCIAL MANAGEMENT POLICIES

SECTION I

FINANCIAL MANAGEMENT POLICY STATEMENT

SUMMARY

The City of Castroville, Texas (City) has an important responsibility to its citizens to carefully account for public funds, manage municipal finances wisely, manage growth, and plan the adequate funding of services desired by the public, including the provision and maintenance of public facilities. The City staff is dedicated to providing services to the citizens of Castroville in order to sustain and enhance the quality of life in the community. The aim of these policies is to ensure that the financial resources are available to meet the present and future need of our citizens. The following Financial Management Policy is designed to establish guidelines for the fiscal stability of the City. The City's financial management includes integrity, prudent stewardship, planning, accountability, and full disclosure.

The scope of these policies generally spans, among other issues, accounting, auditing, financial reporting, internal controls, operating and capital budgeting, revenue management, cash and investment management, expenditure control, asset management, debt management, and planning concepts.

The Goals of this Policy Statement are to:

1. Demonstrate to citizens of Castroville, the investment community, and the bond rating agencies that the City is committed to a prudent fiscal operation;
2. Provide precedents for future policy makers and financial managers on common financial goals and strategies;
3. Present fairly and with full disclosure the financial position and results of the financial operations of the City in conformity to Generally Accepted Accounting Principles (GAAP) and Government Account Standards Board (GASB); and,
4. Determine and demonstrate compliance with finance-related legal and contractual issues in accordance with provisions of the Texas Local Government Code, the Internal Revenue Code and other pertinent legal documents and mandates.

Adopted policies shall be applied to all funds maintained by the City, unless otherwise specially stated herein. Specifically this policy framework mandates the pursuit of the following objectives:

Section II: Accounting, Auditing and Financial/Fiscal Reporting and Monitoring:

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.

Section III: Budget Development:

Preparation and adoption of procedures as outlined in the Texas Local Government Code for general law cities.

- Section IV: Budget Guidelines:**
Establish guidelines for budgeting to help ensure a financially sound City and establish a long range financial planning process that assesses the long-term financial implications of current and proposed operating and capital budgets.
- Section V: Revenues:**
Maintain and administer a revenue stream that will assure a sufficient revenue stream to support desired City services.
- Section VI: Expenditures (non-capital):**
Identify and set priorities for services, establish appropriate service levels and administer the expenditure of available resources to help ensure fiscal stability and the effective and efficient delivery of services.
- Section VII: Fund Balance/Ending Balances:**
Maintain a minimum 90 day targeted reserve in the General fund balance and retained earnings of the various operating funds sufficient to protect the City's credit worthiness as well as its financial position during emergencies.
- Section VIII: Internal Control:**
Establish written procedures and responsibilities for internal control.
- Section IX: Training Policy Statement**
Establish written procedures and responsibilities for employee training
- Section X: Capital Expenditures and Improvements:**
Annually review and monitor the capital equipment and/or the City's capital facilities or other improvements that are expected to provide services over a considerable period of time.
- Section XI: Debt:**
Establish guidelines for debt financing that will provide needed facilities, land, capital equipment and infrastructure improvements while minimizing the impact of debt payments.
- Section XII: Cash Management/Investments:**
Invest the City's operating cash to ensure its absolute safety of principal, provide for the necessary liquidity needs of the City, and to generally optimize yield, subject to the limitations imposed by debt ordinances and the Internal Revenue Code.
- Section XIII: Grants:**
Seek, apply for and effectively administer federal, state and local grants, which support the City's current priorities and policy objectives.
- Section XIV: Financial Consultants:**
The City may employ the assistance of qualified financial advisors and consultants as needed in the administration and management of the City's financial functions.
Coordinate efforts with governmental agencies to achieve common policy objectives and cost sharing.

<p style="text-align: center;">SECTION II ACCOUNTING, AUDITING AND FINANCIAL REPORTING</p>

A. Accounting Practices and Principles

The City shall comply with prevailing local, state, and federal regulations. Its accounting practices and financial reporting shall conform to General Accepted Accounting Principles (GAAP) as promulgated by the Government Accounting Standards Board (GASB), the American Institute of Certified Public Accounts (AICPA), and the Government Finance Officers Association (GFOA). The City Council shall select an independent firm of certified public accounts to perform an annual audit of all operations.

The Comprehensive Annual Financial Report (CAFR) shall be submitted to GFOA annually for evaluation and consideration for the Certificate of Achievement for Excellence in Financial Reporting.

B. Monthly Financial and Management Reports

Monthly reports shall be prepared comparing expenditures and revenues to current budget, for the month and fiscal year-to-date, projecting expenditures and revenues through the end of the year, and outlining any remedial actions necessary to maintain the City's financial position. Financial Reports will be provided monthly to all Department Directors and the City Administrator in a summary format and in a detail line item format comparing expenditures and revenues to current budget, for the month and fiscal year-to-date. The Directors will be responsible for reviewing the revenue, where applicable, and expenditures and making any spending adjustment that may be required.

C. Quarterly Financial Reports to City Council

Quarterly reports will be prepared comparing expenditures and revenues to current budget, for the quarter and fiscal year-to-date, projecting expenditures and revenues through the end of the year, and outlining any remedial actions necessary to maintain the City's financial position. These reports will be presented to the City Council on a timely basis at a City Council meeting following the end of the quarter. The status of the City's projects will be provided to the City Administrator and made available to the City Council. The reports may include project scope and work plan as well as comment on noteworthy activity.

D. Annual Audit

Pursuant to Texas Law, the City shall have its records and accounts audited annually and shall have an annual financial statement prepared on the audit. The audit shall be performed by an independent certified public accounting (CPA) firm licensed to practice in the State of Texas. The annual financial statement, including the auditor's opinion, shall be filed within time frame outlined in the State Statutes. 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. An official Comprehensive Annual Financial Report (CAFR) shall be issued no later than 180 days (Texas Local Government Code §103.003) following the end of the fiscal year. The Director of Administrative Services shall be responsible for establishing a process to ensure timely resolution of audit recommendations.

E. Annual Financial Disclosures

As required by the United States Securities and Exchange Commission (SEC) and the City's debt ordinances, the City, with support of the City's financial advisor, will provide certain annual financial information to Municipal Securities Rulemaking Board through Electronic Municipal Market Access through disclosure documents or set of documents that include the necessary information. This will include any periodic material event notices as required by the SEC.

F. Signature of Checks

All City checks shall have two (2) signatures. One of the two signatures must be a Councilmember and both may be Councilmembers. The other signature may be a staff member, the City Administrator, Director of Administrative Services or the City Secretary.

G. Compliance with City Council Policy Statements

The Financial Management Policy Statement will be revised or refined as deemed necessary. Policy Statements adopted by the City Council are guidelines, and occasionally exceptions may be appropriate and required. 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 Administrator.

<p style="text-align: center;">SECTION III BUDGET DEVELOPMENT</p>

Preparation Adoption and Amendment

Preparation and Adoption procedures are outlined in the Texas Local Government Code, Chapter 102.

The City Administrator shall prepare each year, a budget to cover all proposed expenditures of the government of the City for the succeeding year. Such budget shall be carefully itemized so as to make as clear a comparison as practicable between expenditures included in the proposed budget and actual expenditures for the same or similar purposes for the preceding year. The budget must also be so prepared as to show as definitely as possible each of the various projects for which appropriations are set up in the budget, and the estimated amount of money carried in the budget for each of these projects. The budget shall also contain a complete financial statement of the City showing all outstanding obligations of the City, the cash on hand to the credit of each and every fund, the funds received from all sources during the previous year, the funds available from all sources during the ensuing year, the estimated revenue available to cover the proposed budget, and the estimated rate of tax which will be required.

The budget prepared by the City Administrator in the manner hereinbefore described shall be filed with the City Secretary not less than thirty (30) days prior to the date the City Council makes its tax levy for the fiscal year and such budget shall be available for the inspection of any citizen.

The City Council shall each year, provide for a public hearing on the Annual City Budget, which hearing shall take place on some date to be fixed by the City Council in accordance with State law and the Tax Code. Public notice of the hour, date, and place of such hearing shall be published in the "official" newspaper. The City Council shall have the authority to make such changes in the budget as in their judgment the law warrants and is in the best interests of the residents of the City. When the budget has been approved by the City Council, the budget as approved will be filed with the City Secretary and taxes levied only in accordance therewith, and no expenditures of the funds

of the City shall be made except in strict compliance with such adopted budget, except as from time to time be authorized by the City Council, as amendments to the original budget. In all cases where such amendment to the original budget is made, a copy of the order or resolution of the City Council amending such budget shall be filed with the City-Secretary and attached to the budget originally adopted. . In the preparation of the budget, the City Administrator shall have the authority to require the directors of all city divisions to furnish such information as may be necessary for him to work with in the development of his budget.

SECTION IV

BUDGET GUIDELINES

Within the established guidelines established in the Texas Local Government Code, these guidelines are designed 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.

A. Balanced Budget

The City Administrator shall file annually, a structurally balanced budget for the ensuing fiscal year with City Council pursuant to Texas law and other laws as appropriate. 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.

B. Planning

The budget process will be coordinated so as to identify major policy issues for City Council consideration several months prior to the budget approval date so that proper decision analysis can be performed. Additionally, a fiscal forecast will be performed such that revenues and expenses/expenditures for the next five (5) years are projected and updated annually, in conjunction with other guidelines and using an objective analytical projection process. The purpose of the Five Year Fiscal Forecast is to provide an analysis of affordability based on a set of assumptions about the future. This planning tool will help determine the impact of decisions and strategies from a five-year perspective.

C. Use of Non-Recurring Revenues

Non-recurring revenue sources, such as a one-time revenue remittance or fund balance in excess of policy, should only be budgeted to fund non-recurring expenditures, such as capital purchases or capital improvement projects (CIP). Non-recurring revenue sources may be used to offset normal expenditures, but this should not be a common procedure so as to ensure that recurring expenditures are not funded by non-recurring sources.

Enhancements

Enhancements are one-time or recurring expenditures/expenses that will provide an improved level of service and/or enhance the quality of the service. These items will be reviewed and approved on an individual basis by department need and by the City Administrator. The value of the enhancement must increase the service level of the entire City operations.

D. Tax Rate

The City Administrator's objective for the recommended tax rate will be that the nominal tax rate will not exceed the roll back tax rate.

E. Avoidance of Operating Deficits

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 in order of precedence are:

- Deferral of capital purchases
- Expenditure reductions
- Hiring freezes
- Use of General fund balance.
- Increase fees
- Lay-off employees/Reduction in force

F. Reserves and Contingency Funds

The City's funds will maintain minimum fund balances and/or working capital balances at a targeted reserve level of ninety (90) days of budgeted operations and maintenance expenditures in the General Fund. The City will work toward and maintain minimum fund balance in the Enterprise Fund and the Airport Fund of ninety (90) days. The right is reserved by the City Council to change the targeted reserve level by resolution, ordinance or budget adoption process.

I. 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 continue service levels.

J. Revenue Estimating for Budgeting

1. 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.
2. The City will review and adopt utility rates, as needed, which will generate revenues required to fully cover operating expenditures, meet the legal restrictions of all applicable bond covenants, and provide for an adequate level of working capital.
3. In addition, utility rates will include a transfer to the General Fund that covers funds for services of general overhead, such as administration, finance, and other costs, as appropriate.
4. Any potential grants will be examined for matching requirements. Generally, these revenue sources should be used for capital improvements that are consistent with the Capital Improvement Plan and which have their operating and maintenance costs included

in the Operating Budget or for special programs associated specifically with the grant. Grant revenues and matches need to be budgeted each year.

K. 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
- Enterprise Fund
- Airport Fund

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; 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.

<i>SECTION V</i> <i>REVENUES</i>

Design, maintain and administer a revenue system that will assure reliable, equitable, diversified and sufficient revenue stream to support desired City services. A knowledge and understanding of revenue sources increases the reliability of the revenue system.

A. Balance and Diversification in Revenue Sources

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 and variations in the weather, which may adversely impact that source. A balance between elastic and inelastic revenue sources also achieves this stability. The revenue base will have the characteristics of fairness and neutrality as it applies to cost of service, willingness to pay, and ability to pay. All revenue forecasts shall be conservative.

B. Use Fees – General Fund

1. For services that benefit specific users, it is the City's intent to establish and collect fees to recover the costs of those services. Where services provide a general public benefit, the City shall subsidize these services through property and sales taxes.

C. User Fees – Enterprise Funds

1. Utility rates and other Enterprise Fund user fees shall be set at levels sufficient to cover operating expenditures (direct and indirect), meet debt obligations, debt service coverage, and provide adequate levels of working capital.
2. The Five-Year Financial Plan, and budgeted enhancements, shall serve as the basis for rate increase considerations.

D. Non-Recurring Revenues

One-time or non-recurring revenues will not be used to finance current on-going operations. Non-recurring revenues should be used for one-time expenditures such as long-lived capital needs. Non-recurring revenue sources may be used to offset normal expenses, but this should not be a common practice so as to ensure that recurring expenditures are not funded by non-recurring sources.

E. Property Tax Revenue

All real and business personal property located within the City shall be valued at 100% of its fair market value for any given year based on the current appraisal supplied to the City by the Medina County Appraisal District. A penalty shall be assessed on all delinquent property taxes, which shall include all court costs as well as an amount for compensation of the attorney, as permitted by Texas law, and in accordance with the delinquent tax attorney's contract with Medina County.

F. Interest Income

Interest earned from investment of available monies, will be distributed to the funds in accordance with the equity balance of the fund from which monies were provided for investment.

G. Equipment Replacement Transfer

A minimum of one percent (1%) of Operations and Maintenance Funds will be transferred from the General Fund and Enterprise Funds into Equipment Replacement Funds for capital purchases.

H. Sales Tax Revenue Collections

Actual sales tax revenue received above the amount budgeted on an annual basis and over the fund balance may be used to fund non-recurring expenses or be transferred to the Capital Improvement Fund.

I. 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.

J. Write-Off of Un-Collectible receivables (excludes court fines and warrants)

1. Receivables shall be considered for write-off as follows:
 - a. Undeliverable mail – accounts that remain outstanding for six (6) months and all steps have been exhausted.
 - b. Texas law authorizing the release or extinguishments, in whole or in part, of any indebtedness, liability, or obligation, if applicable.
 - c. Accounts outstanding for three (3) years, identified as uncollectible, and all attempts to collect have been taken.
2. The write-off of uncollected accounts is a bookkeeping entry only and does not release the debtor from any debt owed to the City.

K. General and Administrative Service Charges

Administrative costs may be charged to all funds for services of general overhead, such as administration, finance, personnel, engineering, legal counsel and other costs, as appropriate. The charges will be determined through an indirect cost allocation following accepted practices and procedures.

<i>SECTION VI</i>

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.

A. Services and Service Levels

As part of the financial planning process, services and service levels will be outlined. The outline of services should include a brief description of the services provided, and service levels/standards.

B. 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.

SECTION VII

FUND BALANCE/WORKING CAPITAL

Maintain the fund balance and working capital of the various operating funds at levels sufficient to protect the City's credit worthiness as well as its financial position during emergencies or economic fluctuations.

A. General Fund Unreserved Fund Balance

The City shall maintain the General Fund unreserved fund balance at a level sufficient to provide for emergency expenditures and unanticipated revenue shortfalls. The targeted reserve level shall be a minimum of ninety (90) days of budgeted operations and maintenance expenditures. The right is reserved by the City Council to change the reserve level by resolution, ordinance or budget adoption.

B. Working Capital of Enterprise Operating Funds

The City shall maintain the Enterprise Fund and Airport Fund unreserved fund balance at a level sufficient to provide for emergency expenditures and unanticipated revenue shortfalls. The targeted reserve level shall be ninety (90) days of budgeted operations and maintenance expenditures. The right is reserved by the City Council to change the targeted reserve level by resolution, ordinance or budget option.

C. Use of Fund Balance/Working Capital/Retained Earnings

Fund Balance/Working Capital/Retained Earnings should 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 objective for that fund, restoration recommendations will accompany the request/decision to utilize said balances.

D. Debt Service Funds

Revenues in the Debt Service Fund are stable, based exclusively on property tax revenues and transfers from other funds. Reserves in the Debt Service Fund are designated to provide funding between the date of issuance of new debt and the time that property tax levies are adjusted to reflect the additional debt. The City should maintain the debt service fund balance as required by bond ordinances. The tax revenue is allocated as taxes are collected for that fiscal year. A transfer from the Utilities Fund and the Airport Fund to their respective Debt Service Funds as revenue permits and debt payment schedules require. Revenue Obligations will maintain Debt Coverage Ratios, as specified by the bond ordinances.

E. Equipment Replacement Fund

The Equipment 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 equipment, including vehicles. Fund Balance will be the accumulated depreciation but in no case not less than 1% of the general operating and maintenance funds and 1% of the enterprise operating and maintenance funds.

<p style="text-align: center;"><i>SECTION VIII</i> <i>INTERNAL CONTROL POLICY STATEMENT</i></p>

A. Written Procedures

Whenever possible, written procedures will be established and maintained by the Director of Administrative Services for all functions involving cash handling and/or accounting throughout the City. These procedures will embrace the general concepts of fiscal responsibility set forth in this policy statement.

B. Department Head Responsibilities

Each Department head is responsible for ensuring that good internal controls are followed throughout his or her department, that all Administrative Services Department directives or internal controls are implemented, and that all independent audit or internal control recommendations are addressed.

<p style="text-align: center;"><i>SECTION IX</i> <i>TRAINING POLICY STATEMENT</i></p>

Training

The City will support the continuing education efforts of all City staff including the investment in time and materials for maintaining a current perspective concerning City issues. Staff will be held accountable for communicating, teaching, and sharing with other staff members all information and training materials acquired from seminars, conferences, and other related education efforts.

<p style="text-align: center;">SECTION X CAPITAL IMPROVEMENT PROGRAM POLICY</p>

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

A. Capitalization Threshold for Tangible Capital Assets.

1. Tangible capital items should be capitalized only if they have an estimated useful life of at least two (2) 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.
2. Fixed asset capitalization of non-expendable items; i.e. vehicles, equipment, machinery, etc. with an estimated life span of two years or greater and per item cost of \$5,000 or greater shall be recorded on a fixed asset list and depreciated as required by Generally Accepted Accounting Principles.
3. A capitalization threshold of \$5,000 will be applied to individual items rather than to a group of similar items (i.e. desks, chairs, etc.).
4. Computer software, regardless of cost, will not be capitalized.

B. Five-Year Capital Improvement Plan (CIP)

1. 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, 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.
2. The City Administrator 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 adopted with the annual budget.
3. The Five-Year CIP shall be limited to the affordability limits identified in the long-range financial plans of the City, taking into consideration, bond issuances, operating costs, etc.
4. Annually, through the budget process and at year-end, projects are to be reviewed and if identified as complete will be closed by Finance and any remaining funds closed to 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.

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

C. Infrastructure Evaluation and Replacement/Rehabilitation

Water, wastewater, electric, gas, 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 wellbeing of the City. As a result, the City's CIP should be focused on ensuring that infrastructure is replaced as necessary to protect the City's investment, to minimize future replacement and maintenance costs, and to maintain existing levels of service and accommodate growth.

D. Replacement of Capital Assets on a Regular Schedule (Fleet and High 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 rate structure charged to each participating fund at 100% of annual the 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 aforementioned schedule and criteria/guidelines established for each fund.

E. Capital Expenditure Financing

The City recognizes that there are two (2) basic methods of financing its capital requirements:

1. Funding from current revenues; or,
2. Funding through the issuance of debt.

Debt financing includes general obligation bonds, revenue bonds, certificates of obligation, tax notes, lease/purchase agreements, certificates of participation, and other obligations permitted to be issued or incurred under Texas law. Guidelines for issuing debt are set forth in the Debt Policy Statements.

F. Capital Improvements/Project Reporting

A summary/status report not only on capital projects completed but also on the entire City's various capital projects will be prepared quarterly and presented to the City Council.

<i>SECTION XI</i> <i>DEBT</i>

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.

A. Use of Debt Financing

Debt financing, to include general obligation bonds, revenue bonds, certificates of obligations, tax notes 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 normally will not be used to fund current operating expenditures.

The City will pay cash for capital improvements within the financial affordability of each fund versus issuing debt when funding capital expenditures and capital improvements, which shall include but not be limited to sales tax, utility system revenues, developer fees, inter-local agreements, and state and federal grants.

B. Debt Financing

Affordability

The City shall use an objective approach to determine whether it can afford to issue ad valorem backed debt, both general obligation bonds, tax notes, and certificates of obligation. This process shall compare City accepted standards of affordability to the current values for the City.

General Obligation (GO) Bonds

General Obligation Bonds require voter approval.

- a. General Obligation Bonds must be issued to accomplish projects identified in the bond referendum and associated material.
- b. General Obligation Bonds must be issued for projects that are in accordance with the language in the bond propositions.

Certificates of Obligation (CO)

Certificates of Obligation may be issued without voter approval to finance any public works project or capital improvement, as permitted by Texas 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 CO's might be issued include, but are not limited to, the following.

- a. The City may issue COs when there is insufficient funding on a general obligation bond-financed capital improvement;
- b. The City may issue COs when "emergency" (urgent, unanticipated) conditions require a capital improvement to be funded rapidly;
- c. The City may issue COs for projects when the City can leverage dollars from others to reduce the City's capital cost for a community improvement;
- d. The City may issue COs for projects when there is no other funding source available and the project is determined to be in the best interest of the City;
- e. The City may issue COs if it would be more economical to issue CO's rather than issuing revenue bonds, and
- f. The City may issue COs for projects for which the City will be reimbursed by developer fees (principal plus interest).

Revenue Bonds

For the City to issue new revenue bonds, revenues, as defined in the ordinance authorizing the revenue bonds in question, shall generally be a minimum of 125% of the average annual debt service and 110% of the debt service, or set at levels acceptable to the rating agencies to maintain quality ratings, for the year in which debt requirements are scheduled to be greatest. Annual adjustments to the City's rate structures for Enterprise Funds will be made as necessary to comply with bond ordinance provisions.

C. Debt Structures

The City shall normally issue bonds with a life not to exceed 40 years for general obligation bonds and 40 years for revenue bonds, but in no case longer than the useful life of the asset. 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. The general obligation debt must also be structured to comply with the Texas Constitution. Normally, there shall be no capitalized interest included in the debt structure except for debt issuances reimbursing developers for infrastructure, which shall not exceed three (3) years of capitalized interest.

D. 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.

E. Interest Earnings on Debt Proceeds

Debt interest earnings 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.

F. Bond Elections

1. Timing of general obligation bond elections shall be determined by the inventory of current authorized, un-issued bonds remaining to be sold and the Five-Year Capital Improvement Program.
2. 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 5 year period.
3. An analysis showing how the new debt combined with current debt impacts the City's tax rate and debt capacity will accompany every future bond issue proposal.

G. 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 or bank private placement. 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.

H. Underwriting Syndicates

The City attempts to involve qualified and experienced firms, which consistently submit ideas to the City and financial advisors and actively participate in the City's competitive sales in its negotiated underwritings. In conjunction with the City's financial advisor, City staff will recommend the structure of underwriting syndicates, which will be effective for the type and amount of debt being issued.

I. Rating Agency Presentations

Full disclosure of operating 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 Moody's Investors Services, Inc., Standard & Poor's Corporation, and Fitch Ratings, as recommended by the City's financial advisor.

J. Bond Ratings

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

K. Lease/Purchase Agreements

The City will use lease/purchase agreements when it is cost efficient and provides for more attractive financing terms.

<p style="text-align: center;"><i>SECTION XII</i> <i>CASH MANAGEMENT AND INVESTMENTS</i></p>

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.

A. Investment Management

1. All aspects of cash/investment management shall be designed to ensure safety and integrity of the City's financial assets.
2. Cash/Investment management activities shall be conducted in full compliance with prevailing local, state, and federal regulations. (See City Investment Policy and Strategy)
3. The City will utilize competitive bidding practices wherever practical, affording no special advantage to any individual or corporate member of the financial or investment community.
4. The City will only do business with City authorized broker/dealers and/or financial institutions as approved by City Council and who have executed a written certification of their review of the City's Investment Policy.
5. 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. (See Investment Policy)

6. Investments of the City shall be made with the exercise of judgment and care which persons or prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment.

B. Investment Strategy

The City 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.

C. Interest Income

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

D. 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, subject to bond ordinance compliance. Bond proceeds will be invested in separate instruments and not commingled with other investment purchases. Arbitrage rebate calculations will be performed annually on all debt issues and funds set aside annually for any positive arbitrage. Arbitrage will be rebated to the United States Treasury, as necessary.

E. Depository

The City 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 (5) years.

F. Collateralization of Deposits

1. The City shall have pledged collateral held at an independent third-party institution and evidenced by a written receipt.
2. The value of the pledged collateral should be marked to market monthly and shall be at least 102% of par or market value of the investments, whichever is greater.
3. 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.
4. The pledge of collateral shall comply with the City's Investment Policy.

F. Bank Accounts

The City will maintain the minimum number of bank accounts that are needed for financial operations or that may be required by law.

SECTION XIII 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.

A. Grant Guidelines

1. The City shall apply and facilitate the application for only those grants that are consistent with the objectives and high priority needs identified by City Council and City Management.
2. Grant funding will be considered to leverage City funds. Inconsistent and/or fluctuating grants should not be used to fund on-going programs.
3. The potential for incurring on-going costs, to include assumptions of support for grant-funded positions from local revenues, will be considered prior to applying for a grant.
4. Anticipated grant retained revenue and expenses should be budgeted wherever possible.

B. Grant Review

1. 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 sources of funding shall be identified prior to application.
2. The City Administrator shall approve all grant submissions and City Council shall approve all grant acceptances over \$25,000 and any grant acceptance no matter the dollar amount if a budget adjustment is required.
3. *Grants applied for, received in the last twelve (12) months, and those sought shall be covered in the quarterly financial reviews. (Added August 27, 2013).*

C. Grant Termination and/or Reduced Grant Funding

1. 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 has obligated through the terms of the grant to maintain the positions.
2. 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.

<p>SECTION XIV FINANCIAL CONSULTANTS</p>

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, tax collection including delinquent tax collection attorney, and financial modeling. The principal factors in the selection of these consultants will be experience/expertise, ability to perform the services offered, references and prior experience with the City. In no case should price be allowed to serve as the primary criterion for selection.

A. Selection of Auditors

1. At least every five (5) 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.
2. It is the City's preference to rotate auditing firms every five (5) 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.
3. Annually the independent auditor will provide a letter of engagement to the City Council for annual audit services.

B. Arbitrage

1. The City shall calculate positive/negative arbitrage on each bond issue every five (5) years to comply with bond ordinance covenants and the rules and regulations promulgated by the Internal Revenue Service. 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 may be contracted out to a qualified firm.
2. Requests for proposals and statement of qualifications are to be solicited at least every five (5) years. There is not a requirement for rotation for these firms.

C. Tax Collection and Delinquent Tax Collection Attorney

1. The City may contract for Tax Collection Services and a delinquent tax collection attorney to collect all real and business personal property taxes located within the City due to the nature and expertise required or, utilize those services as provided by the Medina County Tax Assessor-Collector.

D. Bond Counsel

1. Bond Counsel to the City has the role of an independent professional 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 interest on the debt is excludable from the gross income of the holders thereof.
2. Requests for proposals and statements of qualifications are to be solicited at least every five (5) years. There is no requirement for rotation for these firms.

Financial Advisory Services

3. 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 advising on financial management. As financial advisors to government entities have developed the necessary expertise in a broad range of services, the City will use a consultant for these services.
4. Requests for proposals and statements of qualifications are to be solicited at least every five (5) years. There is no requirement for rotation.

E. Investment Advisory Services

1. The City is charged with investing funds available maintaining absolute safety of principal, the necessary liquidity and the optimum yield. In order for the City to provide these objectives, the City may request proposals for the services of an Investment Advisor to assist the Director of Administrative Services in maintaining the investments in accordance with the City's Investment Policy and to obtain the optimum yield on investments in the marketplace. As Investment Advisors to governmental entities have developed the necessary expertise in a broad range of investing, the City will use a consultant for these services until such time that the City wishes to bring these services in-house.
2. Requests for proposals and statement of qualifications are to be solicited at least every three (3) years. There is not a requirement for rotation.

F. Depository Bank

1. Pursuant to Texas law, the City may approve a depository services contract whose term does not exceed five (5) years. The City 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.

This Financial Policies Manual for the City of Castroville was amended by City Council action on August 27, 2013.

Robert Lee
Mayor

Debra Howe
City Secretary