

Operating Management Policy

The purpose of the Operating Management Policy is to provide guidance and clarification on how the budget will be structured and developed, define the budget control system, how to amend the budget, and specific revenue and expenditure principles to ensure ongoing financial sustainability and operating practices.

Key Budget Features

Scope and Length of Budget Period: The budget shall be based on a fiscal year beginning July 1 through June 30, and revenue and expenditures for all funds shall be adopted annually (excluding funds maintained for financial reporting purposes only).

Level of Control: The budget process shall be decentralized, allowing all Departments to provide updated revenue and expenditure amounts entered directly into an online budget system. Budgetary control shall be at the Departmental level and managed separately between the Personnel budget (5100-series of accounts) and the Operating budget (5200-8900 series of accounts). A Department cannot spend more than the budget appropriated; however, line item appropriations shall be established for each cost center (division) within each Department.

Balanced Budget Definition: According to the City Charter, the total of proposed expenditures shall not exceed the total of estimated income and fund balances available. Each fund in the budget must also be in balance; total anticipated revenues plus the necessary portion of fund balance (all resources) must equal total expenditure appropriations for the upcoming fiscal year. Appropriation shall be for a specific fund and balanced based on specific funding sources, therefore savings in one fund shall not be used to cover over-expenditure in another fund.

Basis of Budgeting: The City's accounting system is maintained on the same basis as the Adopted Budget. This enables Departmental budgets to be easily monitored via accounting system reports on a monthly basis. The City's financial records, as reported each year in the Comprehensive Annual Financial Report (CAFR), are maintained in accordance with Generally Accepted Accounting Principles (GAAP). For comparison purposes, the City's CAFR shows fund revenues and expenditures on both a budget basis and a GAAP basis in all funds for which budgets are adopted.

The budgets for general governmental fund types, (i.e., General Fund, Special Revenue, Capital Projects, and Expendable Trust) are prepared on a modified accrual basis, which is a mixture of the cash and accrual basis. This basis is consistent with GAAP except for the following:

- a. Compensated absences are recorded as expenditures when paid (cash basis) as opposed to a liability that is expected to be liquidated from available financial resources as earned and accrued by employees (GAAP basis).
- b. Sales tax and grant revenue are recorded on the basis of cash collected (cash basis) as opposed to the accrual basis (GAAP basis) whereby amounts are recorded to the period the revenue was earned.
- c. Capital outlays for Enterprise funds are recorded as expenses (cash basis) as opposed to fixed assets (GAAP basis).
- d. Principal payments on long-term debt are recorded as expenses (cash basis) as opposed to a reduction of a liability (GAAP basis).
- e. Proceeds from the sale of bonds and utility system development fee revenues are recognized as revenue when received (cash basis) as opposed to a reduction of a liability and an increase in contributed capital (GAAP basis).
- f. No depreciation is budgeted (on a cash basis for any fund) as opposed to depreciation expense recorded in financial statements (GAAP basis).

The budgets for Proprietary fund types such as the City's Enterprise (water, wastewater, reclaimed water, reverse osmosis, solid waste, and airport), Internal Service, Fiduciary, and Permanent Trust funds are budgeted and reported on a full accrual basis of accounting. Under the full accrual basis, expenses are recorded at the time liabilities are incurred, and revenues are recognized when they are obligated to the City (for example, water user fees are recognized as revenue when bills are produced, not when the cash is received). All operating and capital expenditures (except depreciation) are identified in the budgeting process because of the need for appropriation authority.

Cost Allocation: Costs incurred in the General Fund to support the operations of the Enterprise funds (water, wastewater, reclaimed water, reverse osmosis, solid waste and airport) will be recovered through an indirect cost allocation. The indirect cost allocation plan will be reviewed annually and costing adjustments made after approval of the City Manager or Designee.

Long-Term Financial Forecasts: Forecasts will be prepared annually covering a ten year period and considered during budget development.

Performance Measurement: Each Department will establish goals and objectives and create and track performance measurements to assure the goals and objectives are achieved in an efficient and effective manner. Performance measures may be eliminated if approved by the Department Director.

Budget Principles and Process

Budget Links to Strategic Financial Plans: The City's annual budget will be developed in accordance with the policies and priorities set forth in the Council Strategic Goals, the needs of the community, and local, federal and state laws.

Examination of Spending Patterns: The City will seek to maximize the value the public receives through its spending by critically examining existing spending patterns to make sure they continue to provide value, and if not, reallocate to services that do.

Prioritizing Services: The Priority Based Budgeting (PBB) results will be used annually to prioritize City services based on City Council's long-term desired results. Costs of City services will be updated every three years.

All competing Department needs (decision package requests), will be weighed taking into account PBB results and other information based on available City resources within projected fiscal constraints. All requests must be fully justified to show that they will maintain or enhance service delivery or support new programs.

Additions to Department budgets outside of the annual budget process are discouraged and only approved by the City Manager's office in unique circumstances or by Mayor and Council when required by City Code.

Funding Liabilities: The current portion of long-term liabilities (i.e. capital infrastructure, annual costs of maintaining and replacing capital assets, contributions to employee pensions), at a minimum, should be funded in the annual budget so as to maintain the trust of creditors and ensure a manageable payment plan.

Budget Process: The budget will be developed following a detailed calendar to ensure timely preparation and execution, provide opportunities for citizen participation at different points, follow State law and City Charter, and be summarized within a budget document to clearly communicate policy decisions.

Budget Control System

Modified Expenditure Control Budgeting (MECB): MECB will be utilized in order to encourage cost effectiveness while providing quality services to Chandler citizens. MECB assumes existing service levels

will be maintained and new or enhanced programs require an ongoing source of funding before initiation. The use of MECB supports the following basic philosophies:

- a. Department management is expected to manage wisely and to look for effective and efficient ways to deliver quality services to our citizens while meeting the goals of Council; and
- b. Department management can find ways to do things more efficiently if given the freedom to innovate and control their own resources.

Base Budget Method: The base budget method will be utilized for ongoing Operations and Maintenance (O&M) appropriation. Departments shall be allocated the prior year's base budget to support all ongoing operations, but may request supplemental funding through a decision package. Requests approved in the Adopted Budget shall be incorporated into Department's base budgets. Departments develop their own expenditure line item budgets; however, exceptions exist for certain citywide expenditure line items and can only be spent for the specified purpose (department fleet, equipment and technology replacement transfers out, and fuel).

Under the MECB philosophy, Departments may request to carryforward savings achieved in their Base Budget operating accounts to the next year, with justification, through a request to the City Manager. Funds available for carryforward will exclude the above noted exceptions.

The City will use an Encumbrance Accounting System whereby budgeted funds are committed and no longer available for spending when a purchase order is approved in the financial system. Encumbered funds will be carried forward to the next budget year if not spent by year end.

Personnel Services Budgeting: All personnel costs are funded outside of the base budgets, and any personnel savings accumulated remain in their original fund. The Budget Division develops all personnel services budgets based on full funding of all approved positions. If revenues are available during the budget process, positions may be added to maintain or enhance service levels after City Manager review and City Council approval. Additions outside of the budget process are discouraged and only approved by the City Manager's Office in unique circumstances. Overspending of overtime and temporary budgets must be funded from base budgets if not directly related to a vacancy.

Budget Resolution Transfer Authority: The Adopted Budget Resolution for each fiscal year gives authority to the City Manager or his/her designee regarding transfers to/from departments of non-departmental encumbrance, carryforward, lump sum agreements, fuel and utility reserves, non-departmental personnel, department operations and maintenance savings, and Information Technology telecommunications appropriation.

Budget Expenditure Limitation: State Expenditure Limitation options, the level at which expenditures cannot legally exceed the appropriated amount, will be reviewed and implemented as required by State statute to ensure the best approach for the City. The City of Chandler currently falls under the Home Rule Option: Under the Home Rule Option, the expenditure limitation is free from any ties to the State imposed expenditure limitation if the majority of the qualified electors vote in favor of this alternative. On August 26, 2014, the City of Chandler voters approved to continue under Home Rule for four years. Chandler adopts its expenditure limitation along with the annual budget. The maximum legal expenditure limit is the total of all departmental appropriations in the final budget adopted by the City Council. The City's next Home Rule election will be in 2018.

Budget Amendments

In accordance with the City's Alternative Expenditure Limitation, total expenditures may not exceed the final appropriation once the budget is adopted. The City can amend the total appropriation for an individual fund; however, if one fund's total appropriation is increased, another fund must be decreased by an equal amount.

Amendments moving budget appropriation between departments may be processed at any time during the fiscal year upon written request by the City Manager to the City Council (Section 5.08, City of

Chandler Charter). Organizational changes resulting in appropriation shifts between departments should be timed for the start of a new budget year, whenever possible.

Revenue and Expenditure Principles

One-time expenses will be funded from one-time balances/revenues and ongoing expenses will be funded by ongoing revenues, except as is provided for by the budget stabilization reserve as described in the Reserve Policy.

Fund balances are non-recurring revenue, and will be appropriately used for one-time expenditures or budgeted as contingency fund appropriations.

Revenues: The City strives to ensure diversification and stabilization of its revenue base.

Revenue projections will be based on historical trends by developing base lines for ongoing types of revenues versus one-time.

Projections used to balance revenues to expenditures will be prepared for a five to ten-year period and updated annually to ensure financial sustainability. A revenue manual will be maintained to document important characteristics and historical background of each revenue source.

Conservative but realistic revenue projections will be prepared to assess the limits of budget appropriation using trend analysis and current data to minimize estimating too high, which could result in mid-fiscal year budget cuts.

User fees and charges will be periodically analyzed and updated to ensure that all direct and indirect costs are recovered for services benefiting individuals/groups (unless an economic disadvantage is caused) versus a larger public benefit.

Utility rate consultant studies will be performed at a minimum every four years, and internal rate analyses will be completed every year for Water, Wastewater, and Solid Waste funds based on ten-year projections. Reviews will ensure fees are adequate to fund operations, debt service, bond covenants and reserves. Additionally, periodic reviews of the rate design and cost of service between customer classes will be completed.

The City will vigilantly pursue outstanding collections through revenue collectors, and periodic Transaction Privilege Tax audits will be performed on businesses to ensure compliance with City tax code. Education will always be a part of taxpayer interactions to protect this major revenue source.

Expenditures: The City will commit to a level of expenditures sufficient to ensure the ongoing health, safety, and welfare of citizens.

Departments are encouraged to periodically review operations for efficiencies and reallocate existing expenditure appropriation before requesting new funding.

Personnel expenditures, the largest operating cost, will be appropriated based on full funding of all approved positions, but a vacancy saving percentage will be determined based on past trends and will reduce the ongoing personnel services budget for forecasting purposes in the General Fund, shifting the amount to one-time funding. Vacant public safety sworn positions will be budgeted at bottom of range and other general positions will be budgeted at mid-range.

Employee benefits expenditures (i.e. pensions, health, worker's compensation) will be appropriated at levels to ensure adequate funding to remain current and maintain appropriate reserves if self-insured.

Compensation packages will be reviewed periodically to ensure they are sufficient to attract and retain quality employees.