Adoption of Financial Policies

The original recommended practice was developed by the Government Finance Officers Association (GFOA). Some aspects of the practice have been revised by the Financial Management Capacity Building Committee (FMCBC) for use by Nova Scotia municipal governments. The original GFOA recommended practice is *Adoption of Financial Policies,* approved by the GFOA Canadian Committee in 2002. Other sources used are footnoted in the text.

Recommendation

The GFOA recommends that, at a minimum, financial planning, revenue, and expenditure policies be developed by professional staff and formally adopted by a municipality's Council. Specifically, the GFOA recommends that municipalities adopt recommended practices offered by the National Advisory Council on State and Local Budgeting (NACSLB). The specific NACSLB practices focusing on financial planning, revenue, and expenditure policies have been selected because they are considered fundamental to the budget process.[1]

Purpose

Financial planning, revenue and expenditure policies should be adopted by municipalities in Nova Scotia to enhance financial health, sustainability, and stability. These recommended practices offered by the NACSLB can act as a solid foundation for municipalities to develop their own unique financial policies in those specific areas.

- Financial planning policies address the need for a long-term view;
- Revenue policies address the need for prudent planning to avoid revenue shortfalls; and
- Expenditure policies address the need to ensure fiscal stability and service to the public through expenditure planning and accountability.[2]

Background

The NACSLB was established in 1995, whose original members included representatives from the GFOA and seven other state and local government associations. The NACSLB developed a set of recommended practices in the area of state (provincial) and local budgeting. The NACSLB has been endorsed by a number of key governmental associations, by academia, and by labour groups associated with local governments.[3]

[1] Government Finance Officers Association. Adoption of Financial Policies, Approved 2002. http://www.gfoa.org/downloads/rpCCIadoptionoffinancialpolicies2002.pdf.
[2] Ibid.
[3] Government Finance Officers Association. Recommended Budget Practices of the National Advisory

The recommended practices outline a budget process that encompasses the broad scope of governmental planning and decision making.

Considerations for Policy Development

In order to develop the recommended financial planning, revenue, and expenditure policies, the GFOA has recommended that certain NACSLB practices be adopted. *Appendix I* provides a detailed description of the following NACSLB recommended practices:

Financial Planning Policies
1. Long-Range Planning
2. Asset Inventory

Revenue Policies
1. Revenue Diversification
2. Fees and Charges
3. Use of One-Time and Unpredictable Revenues

Expenditure Policies
1. Debt Capacity, Issuance, and Management
2. Reserve or Stabilization Accounts
3. Operating/Capital Expenditure Accountability

Appendix II provides a complete list of all of the recommended practices offered by the NACLSB. This can allow municipalities in Nova Scotia to find guidance on its specific budgetary concerns.

Appendices

Appendix I: NACSLB Financial Policies
Appendix II: Complete List of NACSLB Recommended Practices

Council on State and Local Budgeting (NACSLB), January 2002. http://www.gfoa.org/downloads/rpCCInationaladvisorycouncilonstatelocalbudgetingnacslb2002.pdf.

Appendix I: NACSLB Financial Policies

The following is a description of the financial planning, revenue, and expenditure policies offered by the NACSLB, which are considered crucial for municipalities to adopt for long-term viability.

Financial Planning Policies

Financial planning policies help municipalities establish a more comprehensive long-term view. In order to create a vision towards a sustainable future, municipalities in Nova Scotia should consider establishing formal long-range financial planning and asset inventory policies. The following is a description of the NACSLB's interpretations, with additional information provided to help municipalities implement these policies.

1. Long-Range Financial Planning

Long-range planning varies between municipalities. Municipalities should adopt financial plans to assess the long-term implications of current and proposed policies, programs, and assumptions. The plan should be reviewed regularly to ensure it achieves its strategies and goals.

According to the NACSLB, financial planning has the capacity to expand a municipality's awareness of options, potential problems, and opportunities. The long-term revenue, expenditure, and service implications of continuing or ending existing programs and adding new programs, services, and debt can be identified. The financial planning process should shape decisions and permits necessary and corrective action.

The NACSLB recommends that municipalities engage in a planning process by analyzing financial trends, risks and opportunities facing the municipality and the actions needed to address these issues, and a long-term forecast of revenues and expenditures that uses alternative economic, planning, and policy assumptions. The financial plan identifies key assumptions and choices related to achievement of goals. The plan may be summarized in the budget document or in a separate report. Decision makers should use the plan to make choices and decisions related to the budget process.

A financial plan can illustrate the likely financial outcomes of particular courses of actions or factors affecting the environment that the municipality operates. A financial plan is not a forecast of what will happen, but rather it is a device to highlight significant issues or problems that should be addressed if the goals are to be achieved.[4]

[4] The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 9.1 Conduct Long-Range Financial Planning. http://www.gfoa.org/services/nacslb/Practices/9_1.htm.

Developing a Long-Range Financial Plan

There are various methods and approaches to developing a long-range financial plan. The following is a description of the City of Edmonton's long-range financial plan (LRFP). The City of Edmonton's model is based on a 10-year projection. Municipalities should develop their LRFP to reflect the same length of time as the multi-year capital plan. For more information on a multi-year capital plan, reference the Financial Management Capacity Building Committee's best practice *Multi-Year Capital Plan*. This LRFP is particularly applicable because the City of Edmonton follows the recommendations of the NACSLB.[5] The content has been modified to be more applicable to Nova Scotia municipalities.

Background of LRFP and Links to the Planning Process

The LRFP should contain ten-year financial projections and comprehensive statements of principles and policies to guide financial decision making. The goal is to ensure that municipalities become financially stable and are able to continually finance services to the public.

The policies embedded in the LRFP are long-term in nature, but short-term directions should be developed to ensure the long-term goals are being met. LRFP policies can address eight key areas:

1. **Financial Management**
    a. Fiscal Autonomy
        i. Ensure municipal responsibilities are aligned with appropriate revenue sources.
    b. Sustainability
        i. Plan the operating expenditures and operating revenues beyond a single budget year to account for future years.
    c. Program Costing
        i. Enhance Council's policy making ability by providing accurate and timely information on full costing of programs.
2. **Financial Reporting**
    a. Management depends on information.
        i. Management depends on relevant, accurate, timely, and comparable information.
3. **Operating Revenues**
    a. Maintain competitive tax rates over the long term:
        i. Achieve real revenue growth, stability, and diversity.
        ii. Pursue new revenue sources.

[5] City of Edmonton. 2006 Long Range Financial Plan. http://www.edmonton.ca/CityGov/corpservs/lrfp06.pdf#search=%22edmonton%20long%20range%20financial%20plan%20pdf%22.

iii. Guide revenue generation by the following principles:
- Tax supported services that benefit the community should be paid by all.
- Increase emphasis on user fees to finance services used by specific individuals or groups.

4. Operating Expenditures

a. Best value means delivering services in the most cost-effective manner.

5. Capital Improvement Program

a. Infrastructure is key to economic development:

i. Provide basic public facilities and infrastructure, and prevent deterioration of the municipality's public facilities and capital plan in a coherent program.

ii. Provide stable long-term capital funding.

iii. Include full life cycle cost provisions and asset replacement in the budget capital plan.

b. Strive to achieve the future replacement of assets avoiding pay-as-you-go-financing:

i. Seek new sources and alternatives for capital funding.

ii. Ensure new developments pay an appropriate share of new infrastructure costs.

c. A capital improvement plan has been developed by Service Nova Scotia and Municipal Relations for municipalities in Nova Scotia to use. This document can be found at:

http://www.gov.ns.ca/snsmr/muns/manuals/PDF/LGRH/LocalGovernmentResourceHandbook_6.2.pdf

6. Capital Financing

a. Base capital financing decisions on:

i. Equity (fairness): finance over a term consistent with the expected life of an asset.

ii. Effectiveness: be positioned to provide a sufficient sum of money when required.

iii. Efficiency: minimize the cost of the financing method.

7. Reserves

a. Maintain a reserve level as approved by Council.

8. Land Management

a. Land values and transactions should be recorded in the manner prescribed by PSAB.[6]

Financial Projections and Estimates

The ten-year financial projections in the LRFP should be updated annually, while the policies can remain either intact, or be modified for various circumstances.

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[6] City of Edmonton. 2006 Long Range Financial Plan. http://www.edmonton.ca/CityGov/corpservs/lrfp06.pdf#search=%22edmonton%20long%20range%20financial%20plan%20pdf%22.

To ensure reasonable operating and capital projections, detailed revenue and cost estimates should be developed. The operating projections can be presented in three components:

- Current Expenditures
  - The costs to maintain the services currently provided.
- Growth or Reduction of Existing Services
  - Increased or decreased demands for existing services.
- New or Enhanced Services
  - A service not currently offered or significant changes to current services or service levels.[7]

Operating Projections

Municipalities should project the operating costs for the length of the LRFP, adjusted for inflation, and costs of adding new services or expanding current services beyond the current levels to meet growing and declining demand. Revenues, including all operating revenues should also be projected. This would include a projection of business and property taxes, user fees, fines and permits, investment income, grants, and other sources. The following is a list of factors municipalities should consider including when conducting operating projections:

- Cost Impacts;
- Service Needs; and
- Revenues.[8]

Capital Projections

As part of a LRFP, municipalities should also include capital projections. The following elements should be included in a capital projection:

- Assessment of Existing Infrastructure
  - In order to develop a capital plan, a municipality should complete an assessment of its existing infrastructure before considering new projects.
- Ten-Year Capital Plan
  - The ten-year capital plan is a plan to help determine how a municipality's revenues will supply its infrastructure needs. The ten-year capital plan can be divided into various areas, based on department, demand, or cost.
- Ten-Year Capital Financing
  - Funding over a long period of time can be broken down into internal and external sources.
- Meeting Capital Demands
  - Municipalities could consider implementing different strategies to either minimize costs or maximize funding.[9]

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[7] City of Edmonton. 2006 Long Range Financial Plan. http://www.edmonton.ca/CityGov/corpservs/lrfp06.pdf#search=%22edmonton%20long%20range%20financial%20plan%20pdf%22.

[8] Ibid.

The NACSLB contends that municipalities should implement a Long-Range Plan for municipalities to become more financial healthy and sustainable.

The complete version of the City of Edmonton's LRFP can be found at:
http://www.edmonton.ca/CityGov/corpservs/lrfp06.pdf#search=%22edmonton%20long%20range%20financial%20plan%20pdf%22

2. Asset Inventory

The NACSLB recommends that municipalities implement a formal policy to routinely assess its capital assets, and identify the municipality's issues, opportunities, and challenges. The condition of the assets and factors that could affect the need or ability to maintain the assets in the future should also be analyzed. This recommendation aligns with PSAB's requirements.

The capital assets, and the condition of the capital assets are critical to the quality of services provided by a municipality. It is very important to determine whether the needs and priorities of the taxpayers are being met. [10]

The Public Sector Accounting Board (PSAB) has developed a guideline on asset inventory. A standard will be in effect for municipalities with fiscal years beginning on or after January 1, 2009. Since this is not an official accounting standard yet, the PSAB has developed an exposure draft outlining the actions necessary of municipalities after January 1, 2009. The Province of Nova Scotia is in the process of developing a manual for municipalities to use when fulfilling the requirements of PSAB 3150 (Tangible Capital Asset reporting). The link below is the exposure draft provided by PSAB. Please refer to this link and PSAB for further information.

http://www.cica.ca/download.cfm?ci_id=33893&la_id=1&re_id=0

Asset Inventory and Asset Management

To create a comprehensive asset inventory policy, municipalities should also consider implementing relevant aspects of asset management. Asset inventory and asset management are complimentary. The following is a description of asset inventory, asset management, and how the two work together.

When conducting asset inventory, municipalities should be able to determine:

- Which assets are owned;
- Where the assets are;

[9] City of Edmonton. 2006 Long Range Financial Plan. http://www.edmonton.ca/CityGov/corpservs/lrfp06.pdf#search=%22edmonton%20long%20range%20financial%20plan%20pdf%22.

[10] The National Advisory on State and Local Budgeting. Best Practices in Public Budgeting Practice 2.2 Assess Capital Assets, and Identify Issues, Opportunities, and Challenges. http://www.gfoa.org/services/nacslb/Practices/2_2.htm

- How much the assets are worth;
- What condition the assets are in; and
- What, when, and how much investment is needed to maintain the assets.[11]

Infrastructure asset management is a systematic program to inventory and evaluate the condition of infrastructure assets combined in a management and improvements program that integrates operations and maintenance with capital renewal or improvements. An infrastructure assets management program can provide a municipality with infrastructure that meets expected performance levels at the lowest possible cost.[12]

Asset management can provide a municipality with sound long-term capital investment decisions for new assets and maximize the usefulness and service of existing infrastructure. The following are some of the valuable reasons for engaging in asset management:

- Accountability for the proper use and stewardship of capital assets is increasing, just as it is for financial management.
- Life cycle asset management minimizes total costs.
- If assets are in good condition, they provide better and more efficient service.
- Poorly maintained assets may increasingly present liability concerns.
- There are growing links between asset management and financial reporting as accounting practices change.
- There is increasing emphasis on asset management by other levels of government.
- There are changes in regulations that require knowledge about assets to determine compliance.
- Asset management increases in importance as governments and the broader public sector entities move to capitalizing their tangible capital assets.[13]

For instance, municipalities can apply asset management to road maintenance. The rate of deterioration of pavement rapidly increases after 12 years. After approximately 15 years, the entire road must be replaced at high cost. Periodic preventative maintenance effort can significantly extend the longevity of road subsurface. As an example, a 4 km segment of six-lane highway with paved shoulders was last resurfaced 10 years ago. The pavement structure will deteriorate within five years and would require $12 million for reconstruction. However, resurfacing now would extend asset life by another 12 to 15 years and would only cost $2.4 million.[14]

[11] Province of Ontario Ministry of Public Infrastructure Renewal. Asset Management.
[12] Hogan, M. G. State of the Municipal Infrastructure – Summary Status Through Year-End 2004. City of Shreveport Department of Operational Services. February 7, 2005. http://www.ci.shreveport.la.us/DEPT/dos/pdf/Year%20End%202005%20State%20of%20Infrastructure.pdf.
[13] Province of Ontario Ministry of Public Infrastructure Renewal. Asset Management.
[14] Ibid.

If municipalities would conduct such analysis on their existing assets, they may be able to save the municipality and taxpayer's significant funds. Asset management can become a comprehensive addition to the asset inventory process.

The most basic elements necessary for implementation and utilization of an infrastructure assets management program should consist of:

- A system that provides the ability to inventory the assets. This enables management to implement preventative maintenance to help avoid a failure, and develop an approach to replace the assets.
- A condition assessment system that relates assets condition to expected service levels. This condition assessment system should look at the infrastructure systems as whole units rather than as a conglomeration of unrelated individual assets. This allows decisions on trade-offs between asset maintenance and asset replacement.
- A systematic, quantitative system for evaluating costs of operation/maintenance compared with asset renewal/replacement. This is an aspect of asset management that utilizes data to make better management decisions concerning costs of operation/maintenance versus renewal/replacement of assets.

These tasks may already be performed to some degree within municipalities, however, it is important to place these into a formalized asset management program. An infrastructure assets management program systematically and quantitatively utilizes all of the above tools to continually assess and improve the infrastructure as a whole rather than considering the infrastructure as independent discrete assets that are repaired as they fail.

Revenue Policies

Understanding the revenue stream is also essential to sensible planning. Most of the following policies seek stability to avoid potential service disruptions caused by revenue shortfalls. Municipalities should develop policies focusing on revenue diversification, fees and charges, use of one-time revenues, and use of unpredictable revenues.

1. Revenue Diversification

Municipalities should adopt a policy that encourages a diversity of revenue sources. All revenue sources have particular characteristics in terms of stability, growth, sensitivity to inflation or business cycle effects, and impact on tax and ratepayers. Diversity of revenue sources can improve a government's ability to handle fluctuations and potentially, help to better distribute the cost of providing services.

The policy should identify approaches that will be used to improve revenue diversification. As a first step, an analysis of particular revenue sources is often undertaken in implementing the policy. Analysis should address the sensitivity of revenues to changes in rates, the fairness of the tax or fee, administrative aspects of the revenue source, and other relevant issues. The policy and the approach to implementation should be periodically reviewed.

Over time, municipalities should strive to improve its revenue diversity to the extent feasible. When a municipality is statutorily or otherwise limited as to the types of revenues it may raise, it should consider options to enhance flexibility within the constraints of available sources. For instance, municipalities that must rely heavily on property taxes may seek to diversify the tax base on the property tax that is levied. A municipality should also recognize that changes in the diversity of revenue sources could affect the relative tax burden on different stakeholders.[15]

Approaching Revenue Diversification

In order to diversify a municipality's revenue sources, three major approaches can be taken to reduce the reliance on a single revenue source, namely property taxes. These three approaches can be used in various combinations.

In examining these approaches, a few concepts should be considered:

- Acceptability
  - How will residents and businesses react to particular revenues?
  - This concept may be viewed as how fair or equitable a revenue appears.
- Stability
  - Does the revenue reflect a steady pattern over time? Is it predictable?

[15] The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 4.6 Develop Policy on Revenue Diversification. http://www.gfoa.org/services/nacslb/Practices4_6.htm.

- Adequacy
    - The cost of providing services rises with inflation and with growth in demand for services. Efficiencies may affect some of the increases, but additional revenue is required each year. An indication of stable revenues is if it is able to keep pace with the need for funds to maintain service standards over time. The characteristic may be referred to as 'strong' versus 'weak' revenue growth.[16]

Approaches to Diversifying Revenues

Municipalities need to consider various aspects before simply reducing property taxes and increasing another source of revenue. The following components focus on different mechanisms municipalities can use when trying to diversify its revenues.

Approach #1 – Shrink the Budget
Approach #2 – Raise New Revenue
Approach #3 – Replace a Portion of Property Taxes with New Revenue

Options for Diversifying a Municipality's Revenue Portfolio

Municipalities have a variety of options in terms of trying to diversify its revenue portfolio. Although it is not feasible to remove property taxes as the main source of revenue, other revenues sources can be expanded or created. The following are some suggestions that municipalities may consider when developing a revenue diversification policy:

- New or expanded user fees;
- Increase fines; and
- Collection of delinquent fees and fines.[17]

2. Fees and Charges

A municipality should adopt a policy that establishes a formal mechanism to set fees and charges, and the extent that they cover the cost of the service provided. Policies that require identification of both the cost of the program and the portion of the cost that will be recovered through fees and charges allow municipalities and stakeholders to develop a better understanding of the cost of services and to consider the appropriateness of established fees and charges.[18]

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[16] Revenue "Portfolio" Diversification for Hillborough County. http://www.hillsboroughcounty.org/managementbudget/resources/publications/revenueportfolio.pdf#search=%22revenue%20portfolio%20diversification%20for%20hillsborough%20county%20pdf%22.

[17] Ibid.

[18] The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 4.2 Develop Policy on Fees and Charges. http://www.gfoa.org/services/nacslb/Practices/4_2/htm.

The Financial Management Capacity Building Committee has established a recommended best practice focusing specifically on setting government charges and fees. The recommended practice can be used to help municipalities establish a formal policy on setting fees and charges.

3. Use of One-Time and Unpredictable Revenues

Municipalities should limit and monitor the use of one-time and unpredictable revenues. A municipality should adopt a policy limiting the use of one-time revenues for ongoing expenditures. A municipality should also identify major revenue sources it considers unpredictable and define how these revenues may be used. Unpredictable revenue sources should not be used to fund ongoing regular programs. An excessive use of one-time and unpredictable revenues can have disruptive effects on services due to the non-recurrence of these sources.

Examples of one-time revenues may include: infrequent sales of municipal assets, infrequent revenues from development, and grants. These revenues may be available for more than one year, but are expected to be non-recurring. Examples of expenditures that a municipality may want to use one-time revenues for may include start-up costs, stabilization, early debt retirement, and capital purchases.

For each unpredictable revenue source, a government should identify aspects of the revenue source that make the revenue unpredictable. A municipality should identify the expected or normal degree of volatility of the revenue source.[19]

One-time revenues and allowable uses for those revenues should be explicitly defined. The policy should be publicly discussed before adoption and should be readily available to stakeholders during the budget process. The policy, and compliance with it, should also be reviewed periodically.[20]

The following in an example of how a municipality in Nova Scotia could structure its "Use of One-Time Revenue Policy":

Policy
A Nova Scotia municipality will discourage the use of one-time revenues for ongoing expenditures.

Background
One-time expenditures are rarely budgeted, and if one does get budgeted, it is tied to a specific expenditure in the same budget year. When one-time revenues occur in a fiscal year, the municipality should determine if there are expenditures to offset revenue. If

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[19] The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 4.4a Evaluate the Use of Unpredictable Revenues. http://www.gfoa.org/services/nacslb/Practices/4_4a.htm.

[20] The National Advisory Council in State and Local Budgeting. Best Practices in Public Budgeting Practice 4.4 Develop Policy on Use of One-Time Revenues. http://www.gfoa.org/services/nacslb/Practices/4_4.htm.

nothing is identified, the revenue should be transferred to a capital project fund, where the revenue can wait until a project is identified.

Action
The municipality should not budget one-time revenues without having a specified expenditure established for the revenue. If one-time revenues occur without an expenditure identified, the revenue should be transferred to a capital project fund.[21]

When developing a policy on the use of unpredictable revenues, municipalities can prepare monthly financial reports that track cash, revenues, expenditures, and accounts receivable. This report can help municipalities examine the actual totals compared to the budgeted amounts, determining if revenues are significantly varying from their originally predicted amounts.[22]

[21] City of Lehi. Accounting System, Management and Budget Policies.
[22] Ibid.

Expenditure Policies

The expenditures of municipalities reflect the ongoing service commitment to the public. Strategic expenditure planning and accountability help ensure fiscal stability. The NACSLB recommends that municipalities adopt debt capacity, issuance, and management; reserve or stabilization accounts; and operating/capital expenditure accountability policies.

1. Debt Capacity, Issuance, and Management

Debt Capacity

Municipalities should adopt a policy on the maximum amount of debt and debt service that should be outstanding at any one time. Policies guiding the amount of debt that may be issued by a municipality ensure that outstanding and planned debt levels do not exceed an amount that can be supported by the existing and projected tax and revenue base.

A municipality should develop distinct policies for their own debt, debt supported by revenues of their municipal enterprises and other types of debt such as short-term debt, variable-rate debt, and leases. Limitations on outstanding debt and maximum debt service may be expressed in dollar amounts or as ratios, such as debt per capita. Policies on debt level and capacity should be incorporated into existing debt policies. Furthermore, policies on debt level and capacity should include an analysis of debt capacity. Factors that are recommended in evaluating debt capacity include current financial capacity, projected future capacity, and statutory and legislated limitations.[23]

Develop Policy on Debt Issuance and Management

A municipality should adopt policies to guide issuance and management of debt. Issuing debt commits a municipality's revenues several years into the future, and may limit the government's flexibility to respond changing service priorities, revenue inflows, or cost structures. Adherence to a debt policy can help ensure that debt is issued and managed sensibly in order to maintain a sound fiscal position and protect credit quality.

Elements of policies on debt issuance and management can include:

- Purposes that debt may be issued;
- Consider the useful life of an asset with respect to the maturity of its debt;
- Limitations on the amount of outstanding debt;
- Types of permissible debt;
- Structural features, including payment of debt service and any limitations resulting from legal provisions or financial constraints; and
- Refunding of debt.[24]

[23] The National Advisory on State and Local Budgeting. Best Practices in Public Budgeting 4.3a Develop Policy on Debt Level and Capacity. http://www.gfoa.org/services/nacslb/Practices/4_3a.htm.
[24] Ibid.

Debt policies should be made available to the public and other stakeholders. Debt issuance and management policies should also be reviewed by key decision makers during the annual budget process and summarized in the budget document. Debt policies should also be integrated with other financial policies, particularly operating and capital budget policies.[25]

Policy Suggestions for Nova Scotia Municipalities

Municipalities may structure their debt management policy to be very specific or broad. This policy focuses on increasing debt capacity and debt issuance management. These are similar, yet different aspects of debt management. Municipalities could establish a policy that outlines the specific uses for debt, and identify the maximum amount of debt and debt service that should be outstanding at any time.

For example, municipalities wishing to increase their debt capacity could consider adopting the following recommendations for their debt capacity, issuance, and management policy:

- Try to pay cash for capital and infrastructure projects;
- Debt financing should only be used under the following circumstances:
    - One-time capital improvements and unusual equipment purchases,
    - When the useful project life will exceed the term of financing,
    - When can be proven sufficient to cover the long-term debt, and
    - Major equipment purchases.[26]
- Debt financing should not be used for operating or and maintenance expenses.[27]

In order to help municipalities manage its debt capacity and issuance, the Nova Scotia Municipal Finance Corporation has developed a debt management tool called the Debt Affordability Model. The Model enables municipalities to determine the appropriate level of debt that is suitable. The Model can also provide various aspects such as multi-year budgeting and forecasting, and analyzing revenue and expenditure options. For more information on the Debt Affordability Model, please contact the Nova Scotia Municipal Finance Corporation at 902-424-4590, or visit http://www.gov.ns.ca/nsmfc.

2. Reserve Accounts

A municipality should develop policies to guide the creation, maintenance, and use financial reserve accounts. Municipalities should maintain a level of financial resources sufficient to protect against reducing service levels or raising taxes and fees because of temporary revenue shortfalls or unpredicted one-time expenditures. Under the Municipal

[25] The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 4.3 Develop Policy on Debt Issuance and Management. http://ww.gfoa.org/services/nacslb/Practices4_3.htm.
[26] City of Lehi. Accounting System, Management and Budget Policies.
[27] Ibid.

Government Act, municipalities are required to develop capital reserve funds, however, municipalities are not required to develop general reserve funds.

Capital reserve fund policies must establish how and when a municipality builds up reserve funds and it should identify the purposes that they may be used. Development of a policy on minimum and maximum reserve levels may be advisable. Policies on reserve funds must be publicly available and summarized in materials used in budget preparation. They must also be identified in other municipal documents, including planning and management reports.

Non-capital reserve funds may be used at a municipality's discretion to address temporary cash flow shortages, emergencies, unanticipated economic downturns, and one-time opportunities. They provide flexibility to respond to unexpected opportunities that may help a government achieve its goals. Policies on the use of these funds may also be tied to an adverse change in economic indicators to ensure that the funds are not depleted before an emergency arises. The minimum and maximum amounts to be accumulated may be based on the types of revenue, the level of uncertainty associated with revenues, the condition of capital assets, or the municipality's level of security with its financial position.[28]

Capital Reserve Funds

Nova Scotia municipalities are required to follow the *Municipal Government Act* (MGA), which includes legislation on capital reserve funds. Municipalities must adhere to the guidelines established in the MGA, however, it is possible to take aspects from the NACSLB recommendation to improve a municipality's own capital reserve fund. Section 99 of the MGA, states the following:

Capital Reserve Fund

(1) A municipality shall maintain a capital reserve fund.
(2) The capital reserve sections of a special reserve fund in existence, on the coming force of this Act, is a capital reserve fund.
(3) The capital reserve fund includes
    a. funds received from the sale of property;
    b. the proceeds of insurance resulting from loss or damage of property that is not used for replacement, repair, or reconstruction of the property;
    c. any surplus remaining from the sale of debentures that is not used for the purpose for which the debentures were issued;
    d. the surplus remaining in a sinking fund when the debentures for which it was established are repaid;
    e. any capital grant not expended in the year in which it was paid;
    f. proceeds received from the winding up of a municipal enterprise as defined in the *Municipal Finance Corporation Act*;

[28] The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 4.1 Develop Policy on Stabilization Funds. http://www.gfoa.org/services/nacslb/Practices/4_1.htm.

g. the current fiscal year's accrual for landfill closure and post closure costs; and
h. amounts transferred to the fund by the council.

(4) A withdrawal from the capital reserve fund shall be authorized by a council, by resolution, and may only be used for
a. capital expenditures for which the municipality may borrow;
b. repayment of the principal portion of capital debt; and
c. landfill closure and post closure costs.

(5) The council may borrow from a capital reserve fund, by resolution, if the resolution prescribes the terms of repayment, including interest, at a rate not less than the interest rate that the municipality would pay to borrow the funds for a similar term from another source.

Non-Capital Reserve Fund

Section 99.6 of the MGA describes the reserve funds that are not mandatory.

99(6) A municipality may maintain other reserve funds for such purposes as the council may determine.

Although municipalities are not required to establish non-capital reserve funds, it may be in their best interest. The following are some suggestions municipalities could use to create a more comprehensive reserve fund policy:

- Establish discretionary reserve funds:
  - Discretionary reserve funds can enable a municipality to spend money without affecting the general municipal levy or the need to issue debentures, and the assets of the reserve fund can be invested to earn the municipality income.
  - Some specific examples of funds for different purposes may involve:
    - Future expenditures or land acquisitions;
    - New buildings and other capital projects;
    - Industrial promotion; and
    - Future sick leave commitments.
- Reserve for working funds.
    - Meet cash requirements of the municipality prior to the collection of current revenue.
- Reserves for contingencies provided for unusual or extraordinary expenditures, such as damage claims.
- Reserves for equipment replacement.
- Periodic review of reserves
  - The policy on reserves should be periodically reviewed.[29]

[29] Province of Ontario Ministry of Municipal Affairs and Housing. Reserves, Reserve Funds, Allowances, Trust Funds and Other Funds, Ministry of Municipal Affairs and Housing, July 1995. http://www.mah.gov.on.ca/Page1551.aspx.

3. Expenditure, Monitoring and Reporting

Municipalities should have mechanisms in place to ensure compliance with the adopted budget. Appropriate management processes and systems allow a government to detect and correct significant deviation, if it occurs.

Mechanisms should be in place to detect, correct, and report deviations from the budget. These measures may be as simple as a requirement that managers do not deviate (under or over) from the projected budget. Budgetary compliance is encouraged through the use of data collection and reporting systems that control disbursements of funds, and to facilitate the evaluation of revenue and expenditure trends, and financial projections. Development of a monthly or quarterly revenue and spending plan should also be considered to address significant deviation. Mechanisms can also include the assignment of budget or finance personnel to conduct monthly or quarterly reviews of trends in actual expenditures and revenues and actual-to-budget comparisons, so timely corrective action can be taken. A municipality also should institute procedures to review the budget periodically and decide on actions to bring the budget into balance, if necessary.[30]

In order to ensure that the budget is being adhered to throughout a budget year, municipalities need to implement control mechanisms to ensure that the budget is being met. The following are some control mechanisms that could be implemented to help determine if the budget is being spent as planned:

- Conduct regular reviews (no less than quarterly) on operating and capital expenditures.
- Set benchmarks, in keeping with the review period, for each item in the operating and capital budget.
- Compare expenditures with budget benchmarks across established periods or years within the budget year.
- If a significant deviation exists, an explanation for the deviation should be obtained. Appropriate action should be taken to stay within the appropriate action of the budget.
    - For example, greater expenditure spent than planned for snow removal, which could be due to an unusually greater snowfall, or an explanation of increased fuel cost.

[30] The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 7.2 Develop Mechanisms for Budgetary Compliance. http://www.gfoa.org/services/nacslb/Practices/7_2.htm.

Appendix II: Complete List of NACSLB Recommended Practices

The previous detailed nine recommended NACSLB practices are only a small sample of the various practices that is offered by the NACSLB. These particular practices that have been discussed focus on financial policies; however, the NACSLB has many different areas. The following is a list of the various practices offered by the NACSLB, which can be found at its website: http://www.gfoa.org/services/nacslb/.

Element 1 – Assess Community Needs, Priorities, Challenges, and Opportunities

Practice 1.1 – Identify Stakeholder Concerns, Needs, and Priorities
Practice 1.2 – Evaluate Community Condition, External Factors, Opportunities, and Challenges

Element 2 – Identify Opportunities and Challenges for Government Services, Capital Assets, and Management

Practice 2.1 – Assess Services and Programs, Identify Issues, Opportunities, and Challenges
Practice 2.2 – Assess Capital Assets, and Identify Issues, Opportunities, and Challenges
Practice 2.3 – Assess Governmental Management Systems and Identify Issues, Opportunities, and Challenges Budget Practices

Element 3 – Develop and Disseminate Broad Goals

Practice 3.1 – Identify Broad Goals
Practice 3.2 – Disseminate Goals and Review with Stakeholders

Element 4 – Adopt Financial Policies

Practice 4.1 – Develop Policy on Stabilization Funds
Practice 4.2 – Develop Policy on Fees and Charges
Practice 4.3 – Develop Policy on Debt Issuance and Management
Practice 4.3a – Develop Policy on Debt Level and Capacity
Practice 4.4 – Develop Policy Use of One-Time Revenues
Practice 4.4a – Evaluate the Use of Unpredictable Resources
Practice 4.5 – Develop Policy on Balancing the Operating Budget
Practice 4.6 – Develop Policy on Revenue Diversification
Practice 4.7 – Develop Policy on Contingency Planning

Element 5 – Develop Programmatic, Operating, and Capital Policies and Plans

Practice 5.1 – Prepare Policies and Plans to Guide the Design of Programs and Services
Practice 5.2 – Prepare Policies and Plans for Capital Assets Acquisition, Maintenance, Replacement, and Retirement

Element 6 – Develop Programs & Services that are Consistent with Policies & Plans

Practice 6.1 – Develop Programs and Evaluate Delivery Mechanisms

Practice 6.2 – Develop Options for Meeting Capital Needs and Evaluate Acquisition Alternatives
Practice 6.3 – Identify Functions, Programs, and/or Activities of Organizational Units
Practice 6.4 – Develop Performance Measures
Practice 6.4a – Develop Performance Benchmarks

Element 7 – Develop Management Strategies
Practice 7.1 – Develop Strategies to Facilitate Attainment of Program and Financial Goals
Practice 7.2 – Develop Mechanisms for Budgetary Compliance
Practice 7.3 – Develop the Type, Presentation, and Time Period of the Budget

Element 8 – Develop a Process for Preparing and Adopting a Budget
Practice 8.1 – Develop a Budget Calendar
Practice 8.2 – Develop Budget Guidelines and Instructions
Practice 8.3 – Develop Mechanisms for Coordinating Budget Preparation and Review
Practice 8.4 – Develop Procedures to Facilitate Budget Review, Discussion, Modification, and Adoption
Practice 8.5 – Identify Opportunities for Stakeholder Input

Element 9 – Develop and Evaluate Financial Options
Practice 9.1 – Conduct Long-Range Financial Planning
Practice 9.2 – Prepare Revenue Projections
Practice 9.2a – Analyze Major Revenues
Practice 9.2b – Evaluate the Effect of Changes to Revenue Source Rates and Bases
Practice 9.2c – Analyze Tax and Fee Exemptions
Practice 9.2d – Achieve Consensus on a Reserve Forecast
Practice 9.3 – Document Revenue Sources in a Revenue Manual
Practice 9.4 – Prepare Expenditure Projections
Practice 9.5 – Evaluate Revenue and Expenditure Options
Practice 9.6 – Develop a Capital Improvement Plan

Element 10 – Make Choices Necessary to Adopt a Budget
Practice 10.1 – Prepare and Present a Recommended Budget
Practice 10.1a – Describe Key Policies, Plans, and Goals
Practice 10.1b – Identify Key Issues
Practice 10.1c – Provide a Financial Overview
Practice 10.1d – Provide a Guide to Operations
Practice 10.1e – Explain the Budgetary Basis of Accounting
Practice 10.1f – Prepare a Budget Summary
Practice 10.1g – Present the Budget in a Clear, Easy-to-Use Format
Practice 10.2 – Adopt the Budget

Element 11 – Monitor, Measure, and Evaluate Performance

Practice 11.1 – Monitor, Measure, and Evaluate Program Performance
Practice 11.1a – Monitor, Measure, and Evaluate Stakeholder Satisfaction
Practice 11.2 – Monitor, Measure, and Evaluate Budgetary Performance
Practice 11.3 – Monitor, Measure, and Evaluate Financial Condition
Practice 11.4 – Monitor, Measure, and Evaluate External Factors
Practice 11.5 – Monitor, Measure, and Evaluate Capital Program Implementation

Element 12 – Make Adjustments as Needed

Practice 12.1 – Adjust the Budget
Practice 12.2 – Adjust Policies, Plans, Programs, and Management Strategies
Practice 12.3 – Adjust Broad Goals, if Appropriate

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The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 4.1 Develop Policy on Stabilization Funds. http://www.gfoa.org/services/nacslb/Practices/4_1.htm.

The National Advisory Council on State and Local Budgeting. Best Practices in Public Budgeting Practice 4.3 Develop Policy on Debt Issuance and Management. http://www.gfoa.org/services/nacslb/Practices4_3.htm.

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