



Staff Report

TO: City Council
FROM: Jeff Mohlenkamp, Finance Director
DATE December 15, 2020
SUBJECT: **Allocation of CFD Administrative Funds (One Time Allocation)/
Creation of Internal Service Funds**

Background and Analysis:

The City has accumulated a balance of Community Facility District Administrative funds in the amount of \$7.5 million as of June 30, 2020. City staff recommends allocation of approximately \$6.5 million of these funds to priority projects and to fund newly created internal service funds.

CFD Administrative Funds are collected from homeowners as an assessment to support City operations. These funds are required to be used to support City operations with the use of the funds restricted by the applicable CFD formation documents. City staff has reviewed the formation documents and consulted with legal counsel and recommend allocation of \$6,481,270 the of fund balance for certain one-time expenses to support ongoing operations as follows:

- \$3,500,000 to a Facility Maintenance/ Replacement Fund (newly created internal service fund),
- \$1,400,000 to a Vehicle Replacement Fund (newly created internal service fund)
- \$600,000 to an Equipment Replacement Fund (newly created internal service fund),
- \$800,000 to an Information Technology Equipment Replacement Fund (newly created internal service fund),
- \$150,000 for Information Technology security– business continuity package, and
- \$31,270 for Incode 10 Payroll/HR module and Fixed Asset Module.

Creation of Internal Service Funds

City operations require the use of buildings, vehicles, equipment and information technology equipment/infrastructure. The amount of expenditures for these areas are not consistent and fluctuates from year to year. As a result, it is very difficult and not recommended to budget these costs through the normal operating budget.

Instead, the standard for municipal governments is to establish internal service funds to accumulate capital and address these periodic and sometimes large expenditures.

For example, a City building may require a new roof every 15 to 20 years. In order to plan for this replacement and gather the funds necessary for the repair when it becomes necessary, an internal service fund can be used to gather the resources necessary to cover the costs at the time it is required.

For example, the City will need to purchase vehicles and expensive equipment to replace existing inventory. Vehicles and equipment often have useful lives from 5 to 10 years. An internal service fund can be used to gather the resources necessary to purchase these items when the replacement is required.

The use of internal service funds provides for a smoothing of the costs over the useful life of the asset. This is a better budgeting process in that it does not require large allocations in one year and smaller allocation in other years. Instead, the estimate for repairs or replacement is calculated and allocations are made from the operating budget into internal service funds so that resources are available when required.

The process is essentially as follows:

1. Staff identify the costs associated with replacing assets or maintaining facilities,
2. The costs are spread over the useful life of the asset,
3. An annual contribution to the internal service fund is identified,
4. The use of assets by various departments is estimated,
5. Departments are charged their respective portions of the annual cost estimate as a transfer to the internal service fund, and
6. Replacement purchases or major maintenance is funded directly from the internal service fund rather than the individual department budgets.

Staff is initially recommending the creation of the following internal service funds:

- Facility Maintenance/Replacement Fund – this fund will be used to cover major maintenance and for replacement of City buildings and facilities,
- Vehicle Replacement Fund – this fund will be used to replace vehicles across City operations,
- Equipment Replacement Fund (non-IT) – this fund will be used to replace equipment used in City operations (mowers, street repair, etc.), and
- IT Equipment Replacement Fund – this fund will be used to replace infrastructure and equipment used to support City technology needs (servers, switches, data security, etc.).

Staff is further recommending the use of CFD Admin funds to provide an initial balance in the funds. This will allow for the City to immediately move to the use of these internal service funds beginning with the FY 2022 budget.

Another important value to the creation of internal service funds is that funds will be available to ensure facilities are maintained and equipment replaced during challenging financial years when allocations to the funds from the various departments may be reduced.

Fiscal Impact:

The transfer of funds from the CFD Admin Fund to internal service funds has no immediate fiscal impact. Instead, this action directly allocates these funds for future defined uses. Future expenses from the internal service funds will be taken to the City Council for consideration. Part of future budgeting processes will be the consideration of expenditures from the internal service funds and department operating allocations to the internal service fund.

Funding Information Technology security upgrades has an estimated cost of \$150,000. Upon approval, these funds will be transferred from the CFD Admin Fund to the Information Technology budget to support this one-time cost. Annual cost to support this upgrades data security/ business continuity package are estimated at \$25,000 annually. This project provides for significant improvements in scans for ransomware and other anomalies. It also provides for immutable backups that make the City far less vulnerable to attacks as data recovery and restoration will be seamless and more timely. Note: this allocation provides the funding to move forward with the contract preparation. The actual contract for these services will be subject to approval by the City Council when the contract is ready to be executed.

Funding to support the acquisition of the Incode 10 Payroll/HR module and Fixed Asset module is \$31,270. Upon approval, these funds will be transferred from the CFD Admin Fund to the Information Technology budget to support this one-time cost. This contract is included as a separate item on this City Council agenda.

Recommended Action:

Approve the creation of internal service funds as follows:

- Facility Maintenance/ Replacement Fund,
- Vehicle Replacement Fund,
- Equipment Replacement Fund, and
- Information Technology Equipment Replacement Fund.

Approve the transfer of funds from the CFD Admin Fund to internal service funds as follows:

- \$3,500,000 to the Facility Maintenance/ Replacement Fund,
- \$1,400,000 to the Vehicle Replacement Fund,
- \$600,000 to the Equipment Replacement Fund, and
- \$800,000 to the Information Technology Equipment Replacement Fund.

Approve the allocation of CFD Admin Funds to two information technology projects as follows:

- \$150,000 to fund data security/ business continuity, and
- \$31,270 to fund the one-time costs to acquire the Incode 10 payroll/HR module and the Fixed Asset module.

Attachments:

- A. GFOA Best Practices for Capital Assets