

Free Cash Policy & FY23 Planning

City of Somerville, MA

Katjana Ballantyne, Mayor

Mike Mastrobuoni, Budget Director
Ed Bean, Finance Director

*Presented to
City Council Finance Committee*

March 7, 2023



Order# 22-1517

That the Director of Finance and the Budget Director update this Council on the progress of the free cash certification and any anticipated plans for additional free cash use.



Values Statement

Every spending decision we make regardless of the funding source is always made through a lens of community values and priorities, whether that is investing in people, affordability, education, infrastructure, transit, sustainability or more.

Agenda

Introductions

01. Definitions & Purpose

Free cash in context and why have a policy?

02. Targets for Generation

How much free cash is appropriate?

03. Uses & Priorities

How should we use the free cash we generate?

04. Free Cash & the CIP

Funding critical infrastructure and assets

05. Other Uses

Additional priorities for using free cash

06. Question & Answer



Section 1

Definitions & Purpose

What is a free cash and how do we utilize financial policies?

Free Cash

Free cash is a revenue source that results from the calculation, as of July 1, of the community's remaining unrestricted funds from its operations of the previous fiscal year.

The calculation is complicated, but the primary generators of free cash are funds unspent at the end of a fiscal year, as well as revenue received beyond what was budgeted.

Policy & Purpose

Why have financial policies?

- Institutionalize good financial management practices.
- Clarify and crystallize strategic intent for financial management.
- Define boundaries.
- Support good bond ratings and thereby reduce the cost of borrowing.
- Promote long-term and strategic thinking.
- Manage risks to financial condition.
- Comply with established public management best practices.



Section 2

Free Cash

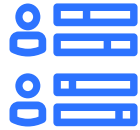
Generation Targets

How much is enough?

Targets for Free Cash

(per policy)

01



Expectations

Generate 3-5% of annual operating revenue in free cash each year.

02



Preferred Limits

Unappropriated free cash should not fall outside 0.5-8% of prior year revenue except in unusual economic cycles.

03



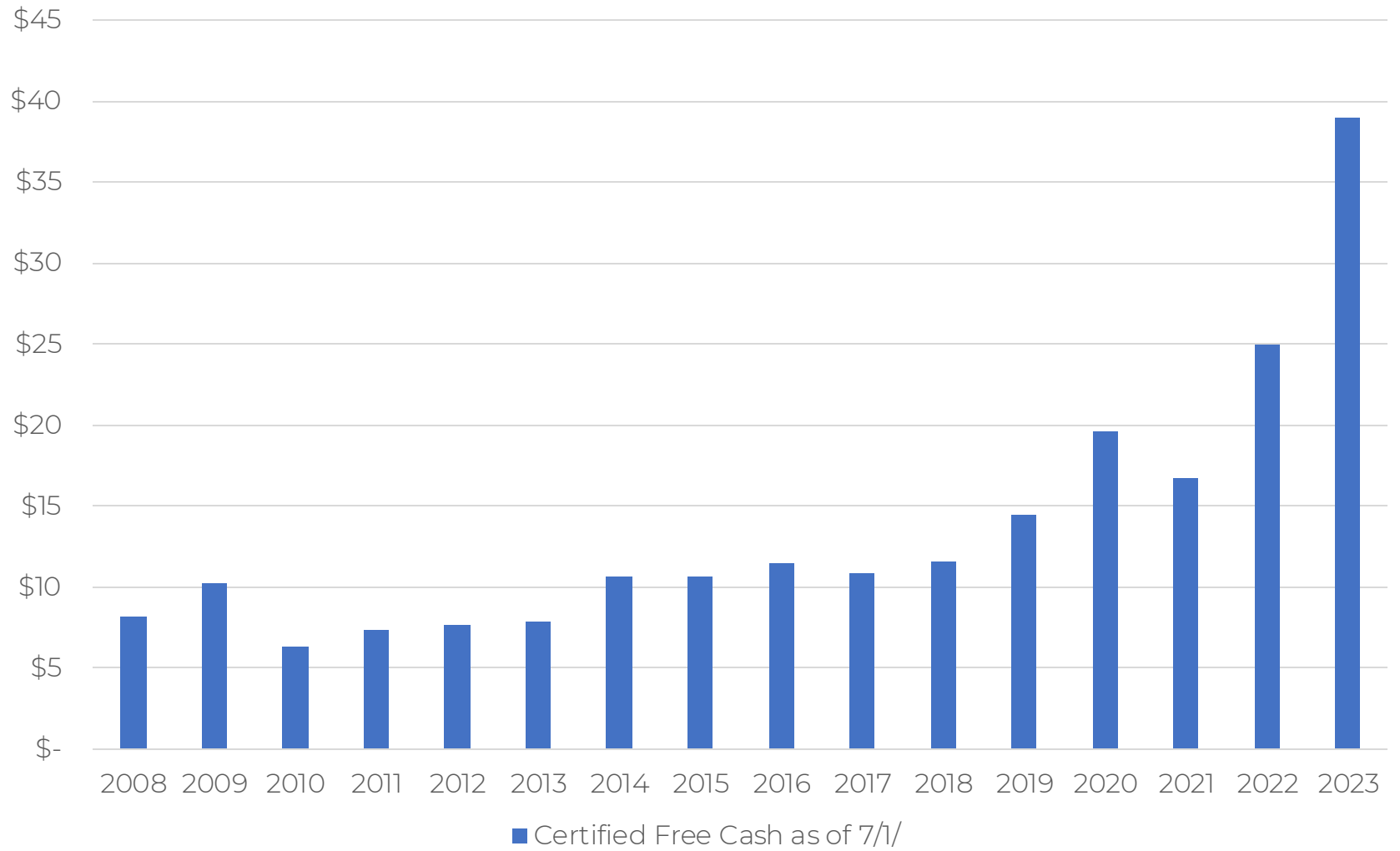
End-of-year

Free cash shall not be **depleted** in any particular year to retain positive balances.

Free Cash Certifications since FY08

Free cash certifications have grown quickly in the pandemic era, part of a trend in the commonwealth.

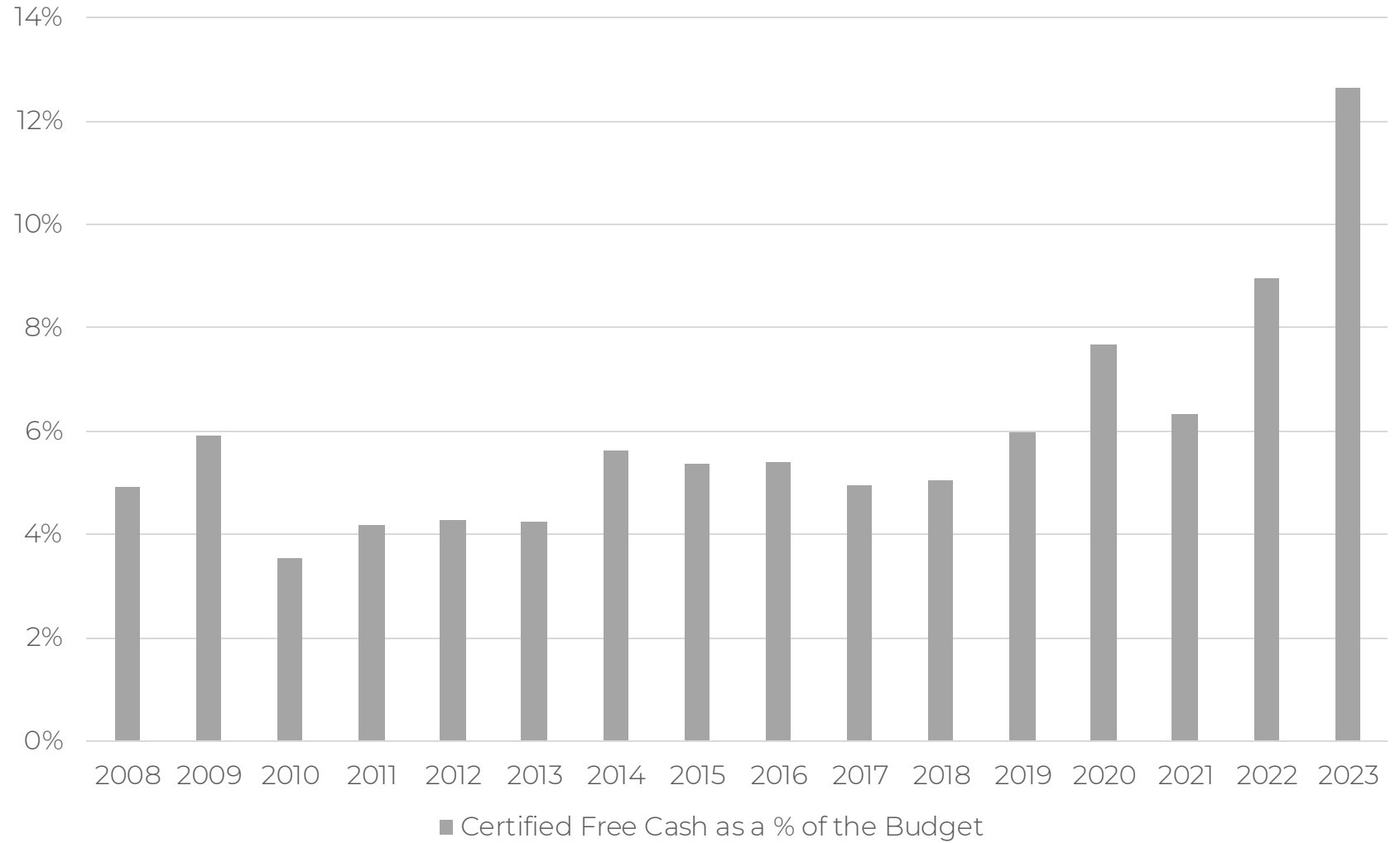
Certified Free Cash since FY08 (Millions)



Free Cash Balances since FY08

When normalized for budget size, the growth trend is moderated.

Certified Free Cash as a % of the Budget



Record free cash is a **statewide trend** in the pandemic era

Malden

Up \$11M since FY20
(+73%)

13%
of budget

Waltham

Up \$20.5M since FY20
(+61%)

17%
of budget

Watertown

Up \$13M since FY20
(+37%)

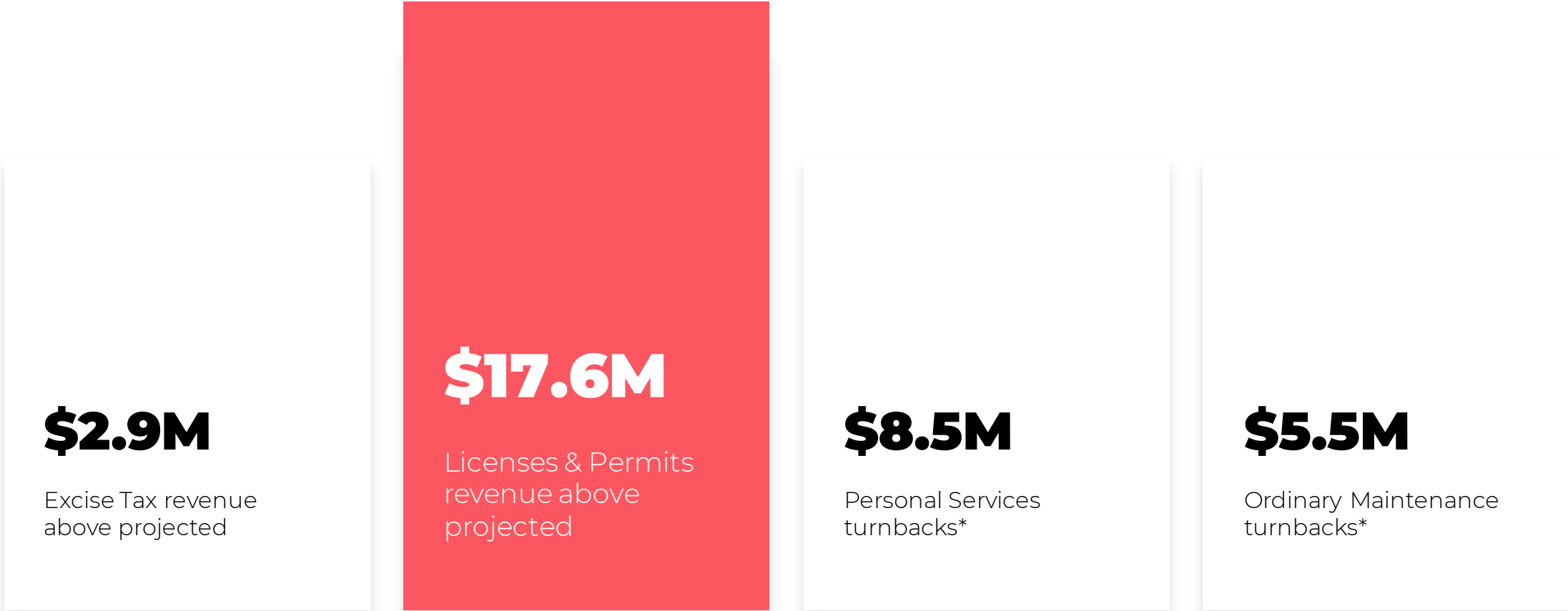
17%
of budget

Somerville

Up \$19M since FY20
(+65%)

12.6%
of budget

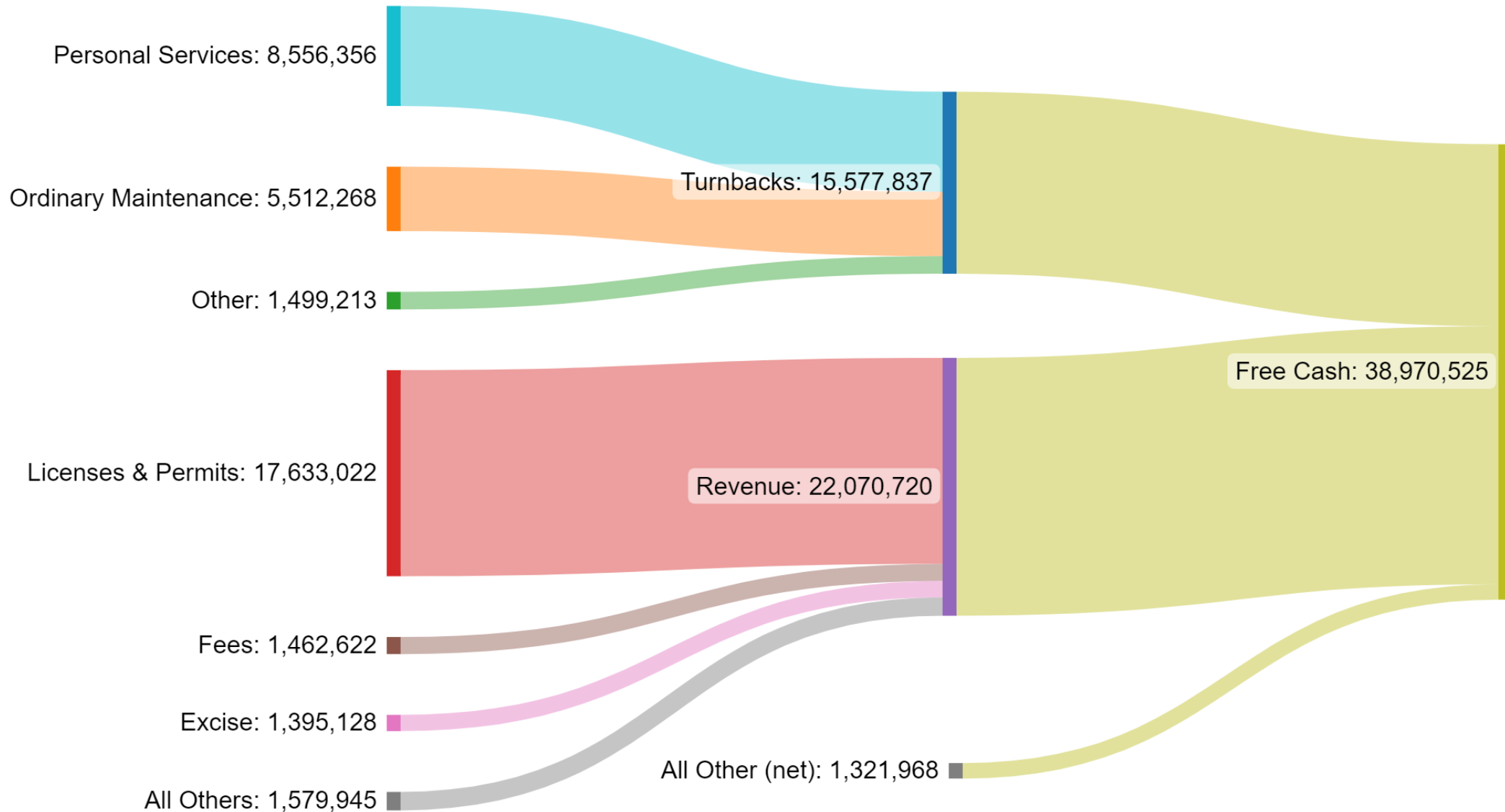
FY23 Free Cash **Primary** Generators



(*Includes School Department)



How did we get \$39M of free cash?



Section 3

Uses & Priorities

What do we expect for free cash in FY23?

What should free cash be used for?

01



One-Time Expenditures

Avoid recurring investments which may put the General Fund in a difficult position

02



Capital Projects

Mitigate costs of the City's CIP and reduce debt service

03



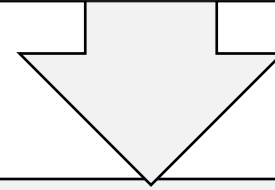
Replenishing Reserves

Maintaining healthy reserve levels at the City's targets

Priorities for appropriation in FY23

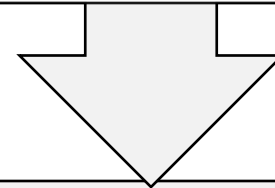
1. Maintain reserve ratio

The City shall maintain an Unassigned Fund Balance plus Rainy-Day Stabilization Fund at an amount equivalent to no less than 10% of General Fund Revenue, as defined in the City's Audited Financial Statements, with a goal of 15%.



2. Emergency expenditures

Free cash may be used to provide temporary financing for unplanned or emergent extraordinary expenses that cannot otherwise be remediated on the Operating Budget.

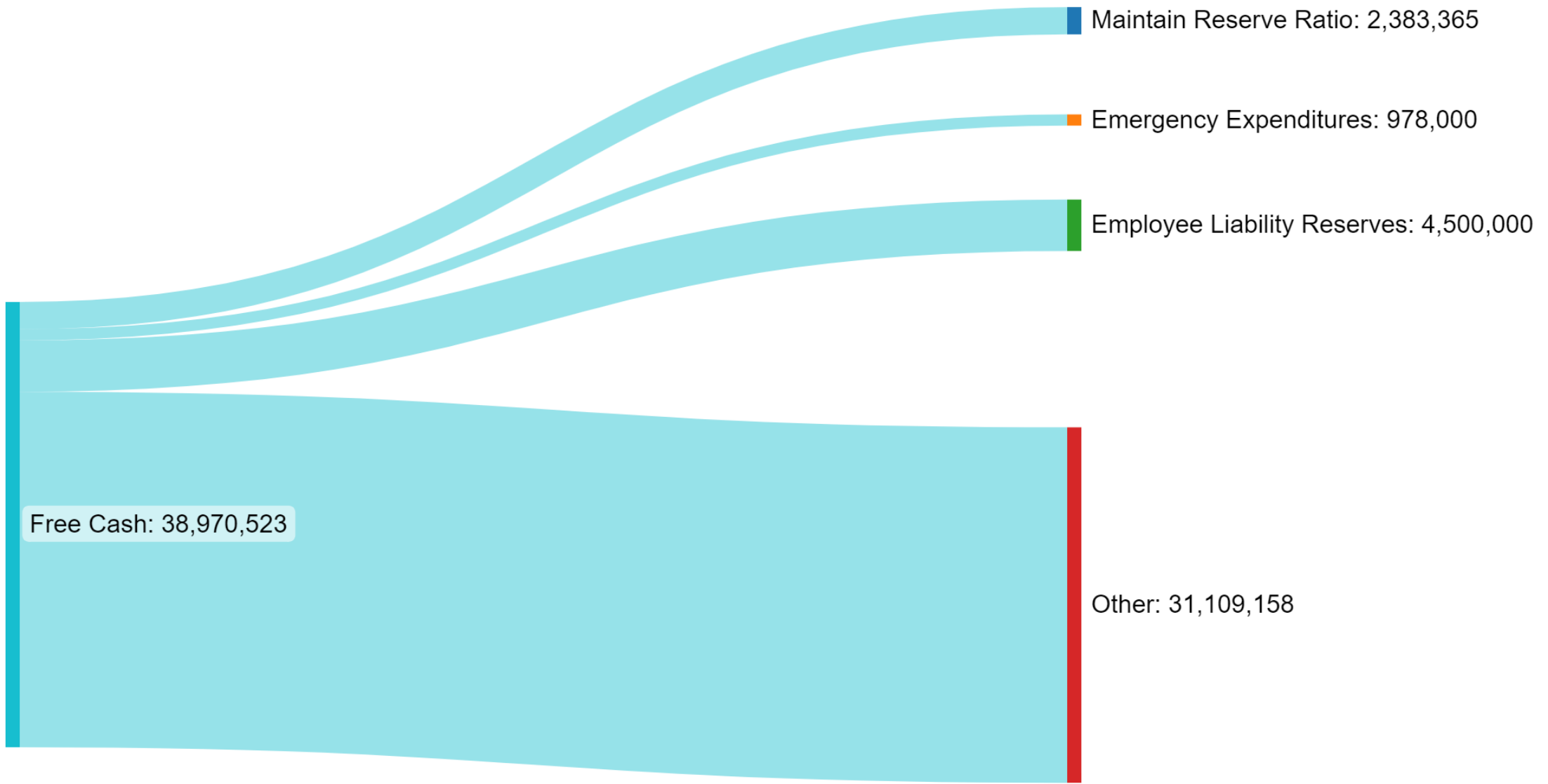


3. Employee liability reserves

Free cash should be used to build up reserves for long-term employee-related liability accounts.



First priorities for free cash



Section 4

Free Cash + CIP

Enabling an ambitious capital plan

The **Capital Investment Plan** requires free cash allocations

Allocation Percentage

City policy states that “The City will endeavor to apportion a minimum of 50% of its yearly free cash certification to the 5-year Capital Investment Plan.”

Use Cases

Using Free Cash as a source to pay debt service for specific projects according to the CIP financing plan.

Enabling the CIP

The City has an ambitious CIP, and we need to make it sustainable.

What are our core stabilization funds?

Utilities

Water & Sewer Capital
Stabilization Funds

Infrastructure

Street Reconstruction &
Resurfacing

Facility Construction &
Renovation

Parks & Climate Resilience

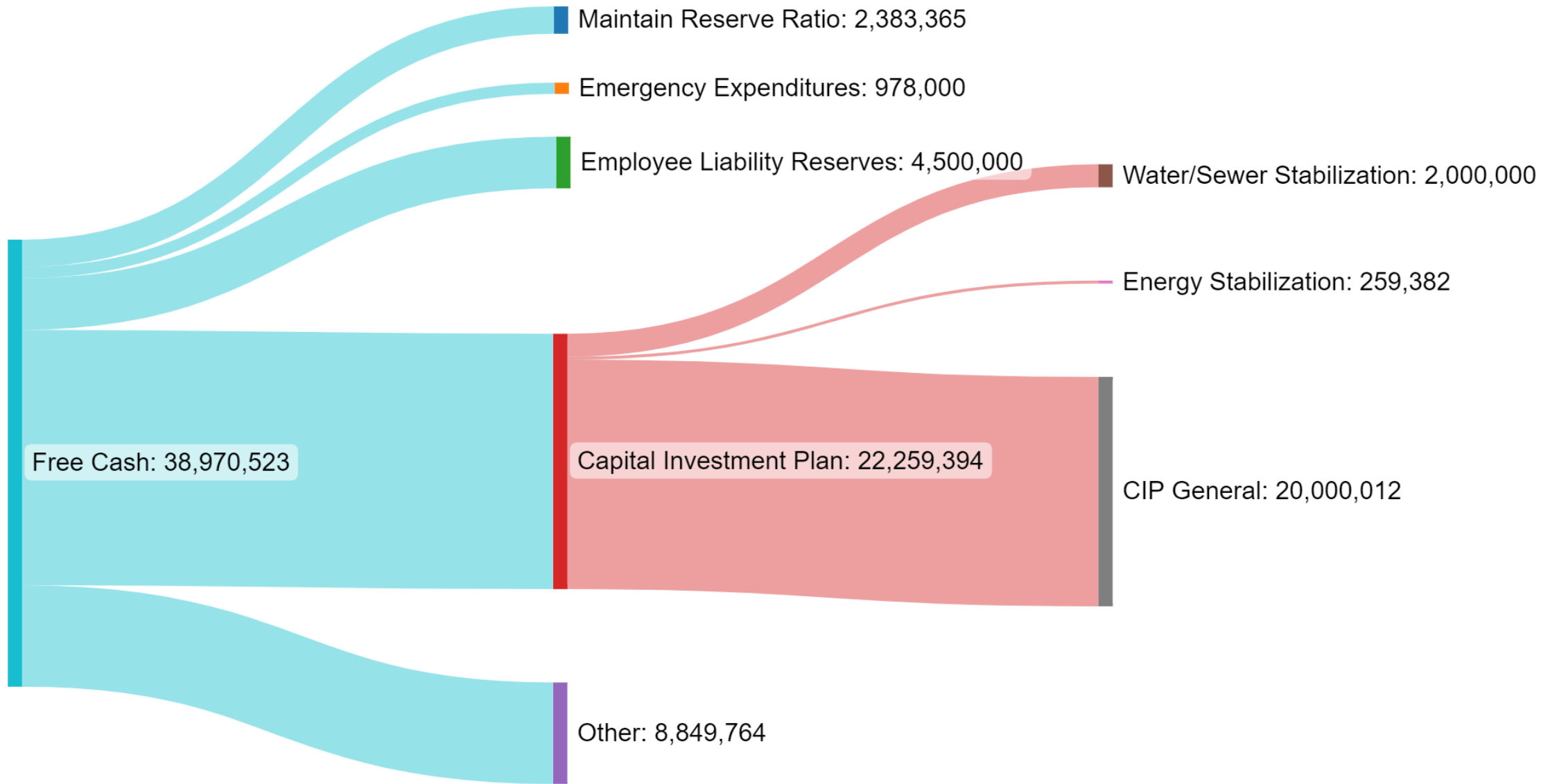
Park Construction
Stabilization

Energy Stabilization

General Capital

Capital Projects
Stabilization

Expected FY23 Free Cash Plan (add CIP)



Section 5 Other Uses

What other needs are currently identified for FY23?

Other uses of free cash

After appropriating Free Cash in accordance with the City's free cash policy and priorities listed above, available free cash may be used to (in no specific order):

- Replenish reserves
- Augment other special purpose stabilization funds
- Dedicate additional funding to the Capital Investment Plan
- Fund other one-time uses
- Establish new special purpose stabilization funds
- Appropriate to the Community Preservation Act Fund

Sustaining the Affordable Housing Trust Fund (AHTF)

To support the City's efforts toward creating and maintaining affordable housing, 15% of remaining Free Cash shall be appropriated into the AHTF if the unreserved fund balance in the AHTF, as calculated in the City's financial system, is less than \$5 million.



Other proposed uses of free cash in FY23



Safe Consumption Site

\$827k for startup costs



Municipal Housing Voucher Program

\$1.9M to continue this ARPA-funded program for three additional years



Outdoor Prefab Toilet Installation

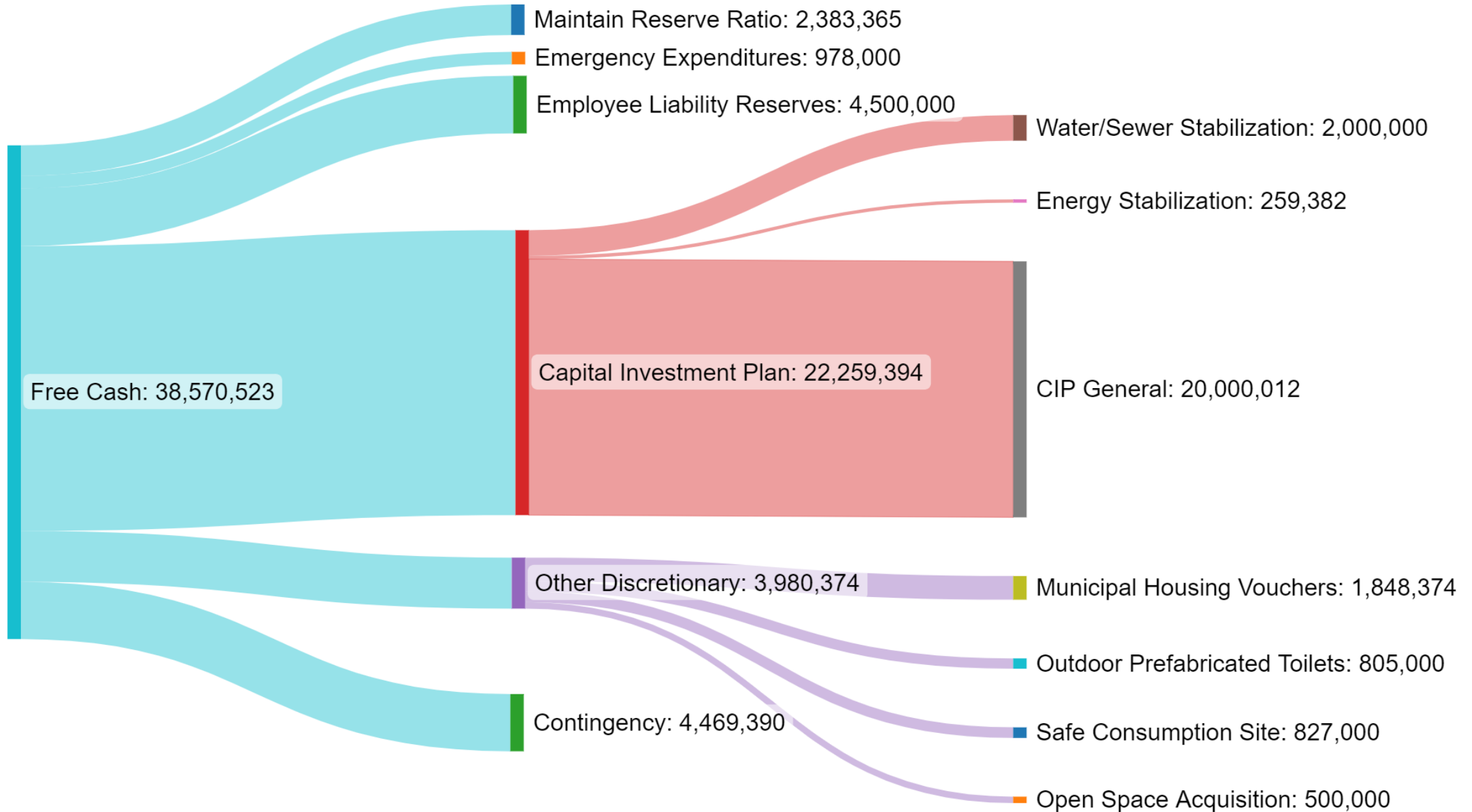
\$805k to install at three locations



Open Space Acquisition Fund

\$500k to grow this fund

Expected FY23 Free Cash Plan (*add Discretionary*)



How much of a change is this?

Mayor Ballantyne requested appropriation of \$24M of free cash in FY22.

100%

All appropriations from free cash in FY22 fell into the priorities of this policy

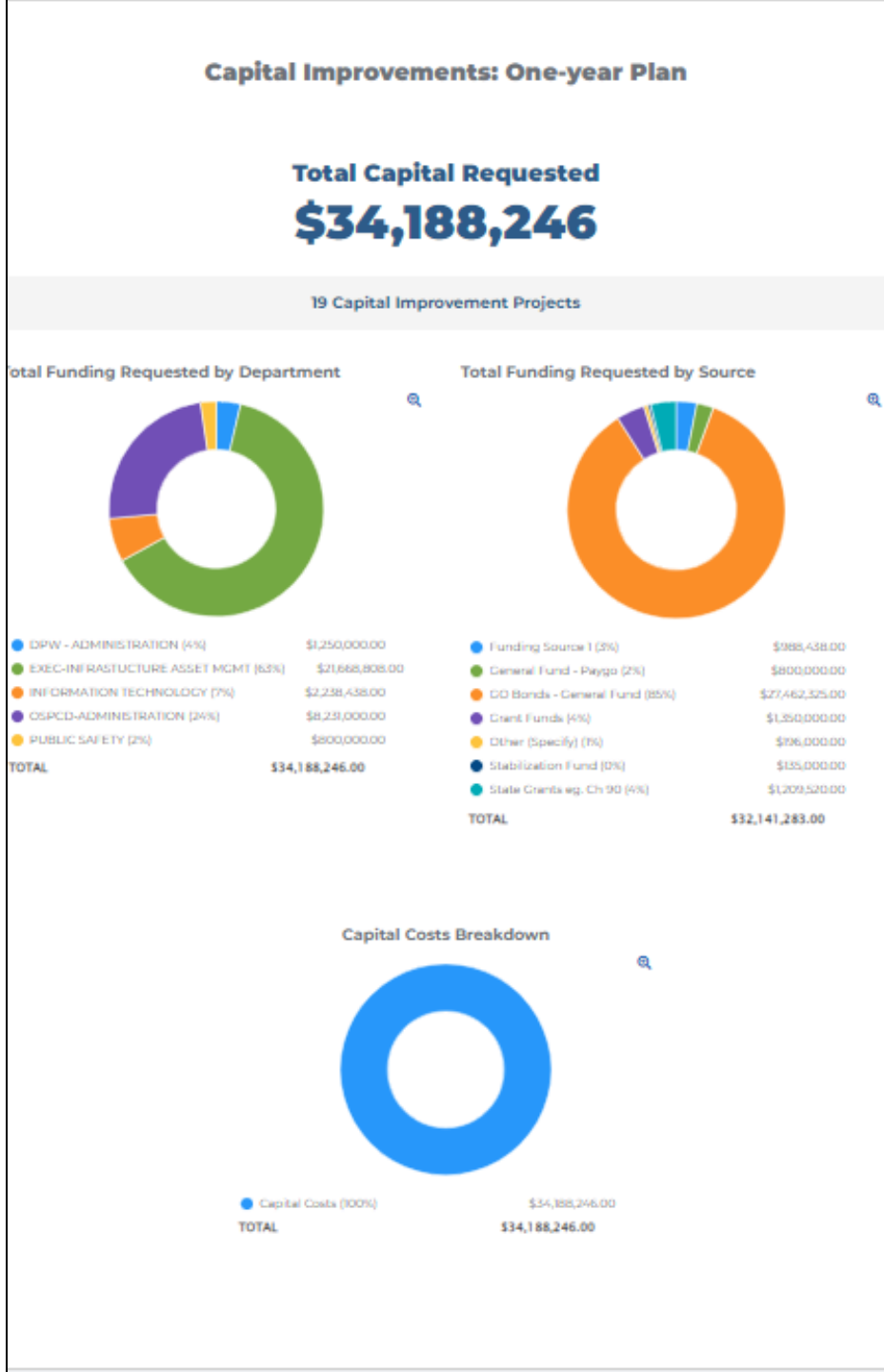
87%

Nearly all appropriations authorized by the City Council were to capital accounts and stabilization funds



What comes next?

| | |
|-----------------------------|---|
| <p>Now</p> | <p>Requested <input checked="" type="checkbox"/></p> <ul style="list-style-type: none"> Municipal Housing Voucher Program Outdoor Prefab Toilets Safe Consumption Site Startup |
| <p>Meantime</p> | <ul style="list-style-type: none"> Capital Investment Plan presented Thursday, March 9th. Resolve emergent issues, eg. Snow or other deficits. |
| <p>Before July 1</p> | <p>Submit appropriation orders for final allocations.</p> |





Question & Answer