

Appendix H: Financial Policies

Budget and Financial Policies

Budget Policies Overview

Pace is one of three Service Boards (Pace, the CTA and Metra) subject to the budgetary control provisions of the Regional Transportation Authority Act which is an Illinois State statute. One of the RTA's chief responsibilities is to ensure compliance with the budgetary controls set forth by the Act.

In addition to the budgetary controls defined by the RTA Act, the Pace Board of Directors has adopted additional budgetary policies which further enhance the control and utilization of resources. The following sections describe the budgetary controls and policies that govern Pace at both the RTA level and internally.

Balanced Budget Definition and Criteria

As described in the Budget Process and Calendar section, the RTA Act requires Pace to submit an adopted budget for the coming fiscal year (calendar basis); a three year financial plan for the proposed budget year and two subsequent years; and a five year capital improvement program and budget by November 15th.

Once the final program and budget is submitted to the RTA, the RTA is required to evaluate it in accordance with seven key criteria as established in the RTA Act. These criteria constitute the definition of a balanced budget.

- The budget plan must show a balance between (a) anticipated revenues from all sources including operating subsidies and (b) the costs of providing the services specified and of funding any operating deficits or encumbrances incurred in prior periods, including provision for payment when due of principal and interest on outstanding indebtedness.
- The budget and plan must show cash balances, including the proceeds of any anticipated cash flow borrowing, sufficient to pay with reasonable promptness all costs and expenses as incurred.
- The budget and plan must provide for a level of fares or charges and operating or administrative costs for the public transportation provided by, or subject to, the jurisdiction of the Service Board, sufficient to allow the Service Board to meet its required system generated

recovery ratio and ADA paratransit revenue recovery ratio.

- The budget and plan are based upon, and employ, assumptions and projections which are reasonable and prudent.
- The budget and plan must have been prepared in accordance with sound financial practices and be in the form and format as determined by the RTA Board.
- The budget and financial plan must meet such other financial, budgetary, or fiscal requirements that the Board may, by rule or regulation, establish.
- The budget and plan is consistent with the goals and objectives adopted by the RTA Board in its strategic plan.

If the RTA finds a Service Board budget submittal does not meet these criteria, it can withhold 25% of the public funding from the Service Board. The RTA Act further requires that the RTA adopt a budget for the Service Board, should the Service Board fail to submit a budget which meets the criteria.

In addition to the seven statutory criteria, the RTA has adopted additional budgetary and financial policies which govern Pace. They are summarized as follows:

Budget Monitoring and Reporting

In order to ensure compliance with the RTA Act requirements for a balanced budget, Pace is required to report quarterly budget results to the RTA within 45 days after the quarter end. The RTA evaluates the results and formally adopts an ordinance which assesses compliance with budgetary funding levels and recovery ratio requirements. If found to be non-compliant with the budget, the RTA may direct Pace to provide a corrective action plan and corresponding budget for their approval.

Pace also produces a monthly budget report for its Board and management. Managers are also advised on a monthly basis as to significant budget variances which are further evaluated by the Budget Department and the respective manager. In addition, all procurement contracts in excess of \$25,000 require the sign off of the Budget Department Manager who reviews the contract proposal for budget compliance.

Budget Control Policies

The Pace Board of Directors has adopted three key budget policies which further govern the control of financial resources. They are summarized as follows:

Line Item Budget Control

This policy identifies the specific budgetary line items under control of the Pace Board as established via the annual appropriations ordinance. It further identifies that the Executive Director has control over the individual expense components and budgets which comprise the Board established line items.

Authorized Head Count

This policy establishes the Pace Board as controlling the total employee head count in full time equivalents (FTE's) and allows the Executive Director to make FTE changes between individual areas within the Board approved total.

Use of Positive Budget Variance (PBV)

This policy establishes that earnings generated by favorable budgetary performance are restricted to capital uses, finite operating purposes or to offset future unfavorable budget performance.

Long Range Financial Planning

Pace is required by the RTA Act to prepare and submit to the RTA for review annually, a three year financial plan for operations and a five year capital investment program. The plans are to be balanced to the RTA's projections of available resources. Pace prepares these plans based on detailed assumptions and plans for each program element. Major assumptions regarding program service levels, ridership, fleet requirements, revenue and expense growth serve as the basis for these plans and are documented in the plan narratives, charts and tables.

Stabilization Funds/Working Cash Policy

In order to allow for the payment of obligations in a timely manner, the Pace Board of Directors has adopted a Working Cash Policy. The policy requires that Unrestricted Net Assets in the amount of 8% of annual budgeted operating

expenses be retained for working cash purposes. Based on the policy, \$15,600,000 of Unrestricted Net Assets are being retained for working cash purposes during 2012.

Due to unfunded deficits resulting in the ADA Fund and the volatile cash flow, the ADA paratransit service is excluded from this policy.

Investment Policy

The Pace Board of Directors has adopted an investment policy that governs the investment of public funds. The policy conforms to all applicable State statutes. The primary objectives, in priority order, of Pace's investment activities shall be:

Safety of Principal

Safety of principal is the foremost objective of Pace. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio.

Liquidity

The portfolio will be substantially liquid for the purpose of meeting all operating and capital requirements which might be reasonably anticipated.

Yield

The portfolio is designed with the objective of attaining a competitive rate of return throughout budgetary and economic cycles which is equivalent with the portfolio's investment risk constraints and the cash flow characteristics.

An objective of Pace's investment policy is to maximize earnings. To facilitate in the evaluation of investments, the 90 day Treasury Bill rate has been established as a performance benchmark.

Use of One Time Revenues

Pace's use of one time revenues are subject to policies established by both the Pace and RTA Boards.

RTA Funding Policy

This policy establishes the basis for RTA funding of Pace and places restrictions on the use of Pace's retained earnings. In summary, the RTA policy is to fund the established budgeted deficit of Pace and not the actual results for the year. In addition, the policy restricts use of any funding provided as a result of a positive budget variance to capital projects or finite operating uses subject to RTA budgetary approval. The Pace policy is consistent with the RTA policy limitations for capital project use and finite operating expense.

RTA Lease Financing Transactions Policy

This policy establishes the allowable uses and budgetary requirements for equipment and facility lease transactions. In summary, it restricts the use of the proceeds from such transactions to capital expenditures and finite operating uses. It further establishes budgetary guidelines for capital projects funded with such proceeds. The Pace policy is consistent with the RTA policy limitations for capital project use and finite operating expense.

Asset Inventory/Condition Assessment

Pace performs a biennial fixed asset inventory as required by the Federal Transit Administration (FTA). The FTA has established stringent controls over the procurement, use, maintenance and disposition of federally funded public transportation assets. The FTA requires the biennial fixed asset inventory to be reconciled to records and accurately reported on the audited financial statements of the agency. Pace is required to ensure safeguards are in place to prevent loss, damage, theft and premature failure of assets. Leases of equipment by Pace to subcontractors must provide for use and control of assets in accordance with federal regulations. Disposition of assets is also strictly controlled by federal regulations with useful life standards established for each asset type. All Pace fixed assets are subject to these control standards.

In addition to management of fixed assets in accordance with FTA requirements, Pace performs routine assessments of its fixed assets to ensure they are maintained in good condition, to achieve their maximum useful life. All major assets are included in future capital improvement replacement plans contained in the annual capital program and budget document.

Risk Management

Pace purchases excess insurance for potential catastrophic occurrences and incorporates risk control and claims management techniques to manage the cost of more frequent, predictable property/casualty loss exposures. Pace utilizes Risk Management and actuarial data to establish reserves for incurred, and incurred but not reported claims, in order to establish appropriate funded reserves to pay future potential liabilities.

Pace currently maintains a \$3 million Self-Insured Retention (SIR) for each occurrence for Automobile Liability exposures. Insurance provides \$12 million in excess coverage above the SIR. For claims above \$15 million, additional Risk Financing techniques are available including Excess Auto Liability coverage, and the ability to borrow funds through the RTA Loss Financing Plan. Excess General Liability insurance is also purchased from an insurance carrier for coverage above a SIR of \$250,000 each occurrence. Additionally, Pace may utilize the RTA Loss Financing Plan to finance recovery from General Liability losses that may exceed the \$15 million. Pace purchases other property/casualty excess policies including Workers Compensation, Pollution, Employment Practice Liability, Crime, Property and Boiler & Machinery.

Pace also has elected to self-insure a portion of its Health and Welfare exposures. Pace maintains stop-loss coverage for any individual health claims exceeding \$150,000 with an aggregate stop-loss of \$4.9 million.

Debt Policy

Pace has no outstanding debt. Pace does not have statutory authority to independently issue debt, but may direct the RTA to issue up to \$5.0 million in working cash notes on its behalf. Pace has never exercised this option.

Basis of Accounting and Budgeting

Pace prepares its financial statements and budget reports using the accrual method of accounting.

Accounting

Pace maintains its accounting records and prepares its financial reports in conformity with generally accepted accounting principles. The financial activities of Pace are organized on a basis of an individual fund which is an accounting entity segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with specific regulations, restrictions, or limitations. Pace operates as an Enterprise Fund, a type of Proprietary Fund. The Suburban Services fund accounts for operating and capital financial information, for all activities other than those assigned to the Regional ADA Paratransit fund. Beginning January 1, 2007, Pace established a second enterprise fund to account for the financial activities of the Regional ADA Paratransit program. Revenue and expenses for these two funds are recognized using the accrual basis of accounting.

Budgeting

Pace's operating budget is prepared in a manner consistent with Pace's financial statements which are prepared on the accrual basis of accounting for a proprietary (enterprise) fund type. All expenditures under the Suburban Service and Regional ADA Paratransit funds are included in this budget for appropriation by the Pace Board of Directors.

Pace maintains a chart of accounts consistent with the Federal Transit Administration's financial reporting requirements. In general, these accounts are established by activity type (i.e., labor, materials and other) for four main expense object areas—operations, maintenance, non-vehicle maintenance and administration. Further segregation of accounts is used to identify activities by object class for individual service programs (i.e., vanpool, dial-a-ride, etc.).

Reporting Entity

Pace has defined its reporting entity as a primary government unit based on the criteria in the Governmental Accounting Standard Board (GASB) Statement No. 14—"The Financial Reporting Entity." Pace's financial statements include the accounts of Pace's nine wholly-owned operating divisions.

External Audit

An independent accounting firm performs an annual examination of Pace's financial statements including Single Audit requirements. Pace's goal is to receive an unqualified opinion on the financial statement audit and a separate report that Pace is in compliance with all Federal Single Audit Requirements.



Administrative functions are performed from Pace's offices in Arlington Heights.