

Developing an Effective Fund Balance Policy

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Learning Objectives

- What is Fund Balance?
- History of Fund Balance Legislation
- What are the components of Fund Balance?
- Benefits of a Fund Balance Policy
- What is a “Reasonable Amount” of Fund Balance?
- Keeping Fund Balance at Desired Levels

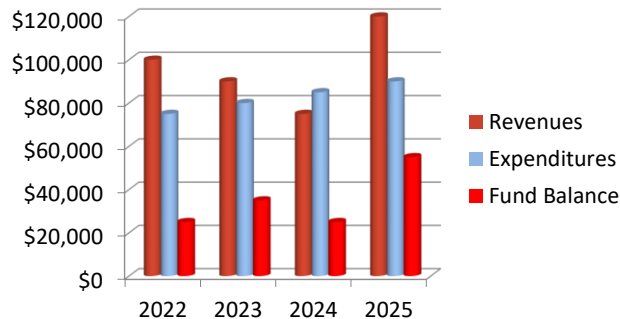


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Fund Balance – What Is It?

- Fund Balance is the total accumulation of operating surpluses and deficits since the beginning of a local government's existence.



Excessively Low Fund Balance

- Normally caused by:
 - Poor budget practices
 - Desire to reduce taxes, or keep them at same level
 - Political reasons
- Can result in:
 - Short-term borrowing (RANs, TANs, Budget Notes)
 - Deficit financing
 - Credit rating reduction
- Should be increased in conformity with long-term plans.

Excessively High Fund Balance

- Normally caused by:
 - Poor budget practices
 - Unduly high property taxes
 - Political reasons
- Greater opportunity for fraud if controls are weak.
- Should be appropriated or reduced in conformity with long-term plans.

Components of Fund Balance

- Pre-GASB 54 - Made up of two parts:
 - Reserved – The portion that is not available for discretionary appropriation due to the creation of reserve funds (legal and accounting)
 - Unreserved (account 909) – The portion that is available for appropriation to reduce taxes and other uses
 - Unreserved / Appropriated (account 910) – the portion of the unreserved fund balance the governing board has applied to reduce property taxes in the ensuing year budget
 - Unreserved / Unappropriated (account 911) – the portion of unreserved fund balance available to provide for economic uncertainties

Components of Fund Balance

- GASB 54 – Five Categories
 - (effective June 15, 2010)
 - Nonspendable (accounts 806 & 807)
 - Restricted (accounts 814-898)
 - Committed (account 913)
 - Assigned (accounts 914 & 915)
 - Unassigned (account 917)
- Essentially what was *reserved*
- Essentially what was *unreserved*

Fund Balance Limits

- Prior to January 2001
 - Counties, Towns, Villages and Fire Districts had no legal authority to carry over any unappropriated / unreserved balance.
- Chapter 528 of the Laws of 2000
 - Bill submitted by Comptroller to provide mandate relief and greater flexibility to local governments.
 - Counties, Towns, Villages and Fire Districts can carry over a “**reasonable amount**” of unreserved / unappropriated fund balance.

Legislative Intent - Prior to 2001

- Public Policy Underlying Rule of Law:
 - Governments need to make a full accounting of all public funds to prevent municipal governments from acquiring tax proceeds faster than they are needed
 - Municipal governments should not accumulate funds for the remote future or for contingencies which may never occur
 - Protection provided to taxpayers from misuse of surplus funds to hide deficit spending or to reap political gain

So Why the Change?

- Legislators recognized the need to set aside a portion of unrestricted fund balance in order to:
 - Reduce the cost of borrowing for cash flow
 - Offset revenue shortfalls in poor economic times as well as unexpected expenditures
 - Stabilize taxes and maintain services without budget cutbacks
 - Improve long-term planning initiatives
 - Enhance the credit ratings of local government

So Why the Change? (Cont'd)

- Legislators also recognized the potential for abuse if local governments were allowed to amass excessive fund balances.
 - The legislation was intended to strike a balance between the potential misuse of fund balance and the inflexibility of the previous legislation.
- Legislation did not define what is meant by a “reasonable amount”.
- An OSC July 2001 accounting bulletin recommended each local government assess what is a “reasonable amount” for its particular situation and adopt a fund balance policy.

Benefits of a Fund Balance Policy

- Provides for an orderly provision of services.
- Provides taxpayers with information about why resources have been set aside.
- Provides a framework to help guide budgetary decisions and multi-year plans.
- Helps ensure an adequate fund balance is available to:
 - Ensure efficient cash flow for daily needs.
 - Protect against unforeseen expenditures related to emergencies.
 - Offset economic downturns or revenue shortfalls.
 - Maintain investment-grade bond rating.

Effective Fund Balance Policies

- Should:
 - Be adopted by the governing board with input from key officials (e.g., CFO, budget officer).
 - Be in written form and subject to review by governing board on a regular basis.
 - Be used to develop and amend multi-year capital and operational plans.
 - Address how surplus balances will be applied.
 - Address the timing for balances to be replenished to the desired level.

So What Is a “Reasonable Amount”

- GASB 54 eliminated the unappropriated / unreserved terminology and instructed local governments to apply the “reasonable amount” calculation to the “unrestricted portion” of fund balance, defined as:
 - The total of the committed (913), assigned (914 & 915), and unassigned fund balance classifications (917).
 - In determining the amount to carry over, this total should then be reduced by any amount appropriated for the ensuing year’s budget (914).
- Local government officials must consider a number of factors when determining how much unrestricted fund balance is “reasonable” to carry over.

“Reasonable” Factors to Consider

- Composition of the fund balance (is it all cash?)
- Timing of receipts and disbursements
- Volatility of revenues and expenditures
- Contingent appropriations
- Established reserves
- Potential for one-time outlays not provided for by reserves
- Dependence on resources from other funds as well as the need to provide resources to other funds
- Size of the fund
- Experience in prior fiscal years

Calculating a “Reasonable Amount”*

- Percentage of Expenditures or Revenues
 - Example: 15% of annual operating expenditures
- Expenditures or Revenues for a set number of months
 - Example: Total estimated expenditures for the first two months of the fiscal year
- Specific dollar amount

***OSC does not recommend any one method or amount – these decisions are the responsibility of each local government based on its own situation.**

Estimating Available Fund Balance

General Fund

Fund Balance @ 1/01/XX	\$782,005
+ Revenues to date (8/31/xx)	\$916,870
- <u>Expenditures to date (8/31/xx)</u>	<u>\$1,151,525</u>
Balance to date	\$547,350
+ Projected Revenues (9/1/ -12/31/XX)	\$177,004
- <u>Projected Expenditures (9/1/-12/31/XX)</u>	<u>\$125,349</u>
Estimated Fund Balance at Year-End – 12/31/XX*	<u>\$599,005</u>

Allocation of Estimated Fund Balance @ 12/31/XX:

Restricted	
(A878, Capital Reserve -\$175,000 + A806, Prepaid Insurance - \$12,500)	\$187,500
Unrestricted / Assigned, Appropriated (A914)	\$100,000
Unrestricted / Assigned, Unappropriated (A915 + A917)	\$311,505

*** Fund balance must be able to be converted to cash
within the first 2 months of the fiscal year**

Budget Requirement

**County Law §355(g); Town Law §107(1)(b), §181(2)(b);
Village Law §5-506(1)(c)**

- Each municipal budget must contain:
 - A statement for each fund of the fund balance estimated to be on hand at the close of the current fiscal year, together with a breakdown of such fund balance estimated for:
 - Encumbrances
 - Amount appropriated for ensuing year's budget
 - Amounts reserved for stated purpose
 - Remaining unappropriated amount, not to exceed a "reasonable amount".

Schedule of Estimated Fund Balances

	General (A)	Highway (DA)	Water Dist (SW)
Estimated Total Fund Balance @ 12/31/25	\$599,005	\$786,990	\$76,650
Nonspendable Portion (Prepaid Insurance)	\$12,500	\$7,800	\$0
Restricted Fund Balance:			
Capital Reserve (878)	\$175,000	\$75,000	\$0
Repair Reserve (882)	\$0	\$50,000	\$22,000
Total Estimated Unrestricted FB @ 12/31/25	\$411,505	\$654,190	\$54,650
Assigned, Appropriated toward 2026 Budget (914)	\$100,000	\$170,000	\$10,000
Assigned, Unappropriated / Unrestricted FB	\$311,505	\$484,190	\$44,650
Assigned for Highway Projects	-	\$65,400	-
Encumbrances	\$3,650	\$6,230	-
Other Assignments	-	\$412,560	\$44,650
Unassigned (917)	\$307,855	-	-

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Four-Pronged Approach

- Manage excess unrestricted fund balance through:
 - One-shot expenditures
 - Reducing Debt Principal
 - Financing Reserve Funds
 - Reducing Property Taxes

One-Shot Expenditures

- Expenditures that do not normally occur annually, such as:
 - Equipment and capital outlay expenditures (.2)
 - Court-ordered judgments
 - Extraordinary public service contracts (legal, assessor, etc.).

Reduce Debt Principal

- Decreases future interest payments
- Shortens life of the loan
- Improves credit ratings

Note: Since not all debt instruments allow for the reduction of principal ahead of schedule, local governments should check with their lender or bond counsel before pursuing this option.

Finance Reserve Funds

- Reserves must be legally established.
 - General Municipal Law (§§ 6-c through 6-r)
 - Town Law (§§ 55, 55-a, 55-b)
 - County Law (§ 372)
- Reserves should be limited to amounts specified in resolution or other statutory limitations.
- Establishment and use of reserves should be linked to long-term capital and operational plans.

Reduce Property Taxes

- Be cautious: One-shot revenues should not be used to fund recurring expenditures.
- Consider budgetary practices.
 - Operating surpluses (deficits)
- Can result in unstable tax rates.
- Link to long-term plans.

Appropriated Fund Balance (a.k.a. Planned Deficit)

	2022	2023	2024	2025
Beginning Unrestricted FB	\$440,000	\$335,000	\$198,600	\$ 41,430
Budgeted Appropriations	\$1,300,000	\$1,339,000	\$1,379,170	\$1,379,170
Estimated Revenues	\$780,000	\$750,000	\$815,000	\$820,000
Appropriated FB	\$90,000	\$159,000	\$134,170	\$41,430
Tax Levy	\$430,000	\$430,000	\$430,000	\$517,740
Budgeted Operating Deficit	(\$90,000)	(\$159,000)	(\$134,170)	(\$41,430)
Actual Operating Surplus (Deficit)	(\$105,000)	(\$136,400)	(\$157,170)	?

\$87,740 increase in taxes (20%)

**\$0 available to offset 2025 revenue shortfalls
and/or unexpected expenditures**

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Replenishing Unrestricted Fund Balance

- Budgetary Provisions
 - When possible - replenish to desired levels in next fiscal year budget
 - When not possible – develop a plan to replenish to desired level over a period of years (e.g., 3 years)
 - Maximum use of contingency account and apply budget surpluses to replenish fund balance
- One-Shot Revenues
 - Sale of equipment & property
 - Gifts / donations

Resources

- OSC Academy Page
 - <https://www.osc.ny.gov/local-government/academy>
- On-Demand Training
 - <https://www.osc.ny.gov/local-government/academy/webinars>
- OSC Contacts
 - <https://www.osc.ny.gov/local-government/contact-division-local-government-and-school-accountability>



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Thank You

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