

Understanding Fund Balance

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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.

The Fund Balance Formula:

$$\text{Fund Balance} = \text{Assets} - \text{Liabilities}$$



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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.

- **Operating Surplus / Deficit**

The difference between a unit's revenues and expenditures for a fiscal year.

$$\begin{array}{r} \text{Revenues} \\ - \text{Expenditures} \\ \hline \text{Operating Surplus / (Deficit)} \end{array}$$

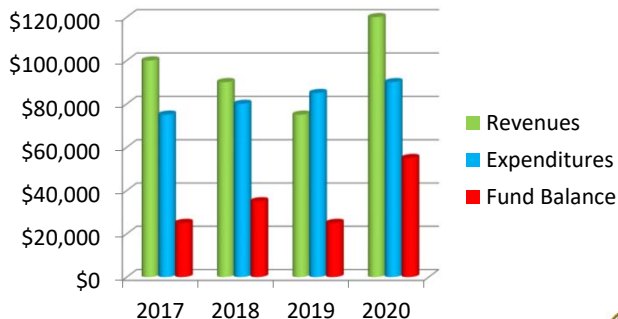


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Fund Balance – What Is It?

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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)

1. Nonspendable (accounts 806 & 807)
 2. Restricted (accounts 814-899)
- } *Reserved Portion of FB*
3. Committed (account 913)
 4. Assigned (accounts 914 & 915)
 5. Unassigned (accounts 916 & 917)
- } *Unrestricted Portion of FB*



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Components of Fund Balance

- *GASB 54 – Five Categories* (effective June 15, 2010)

Reserved Portion of Fund Balance

1. Nonspendable (accounts 806 & 807)
 - Inventory, prepaid items
2. Restricted (accounts 814-899)
 - Reserves



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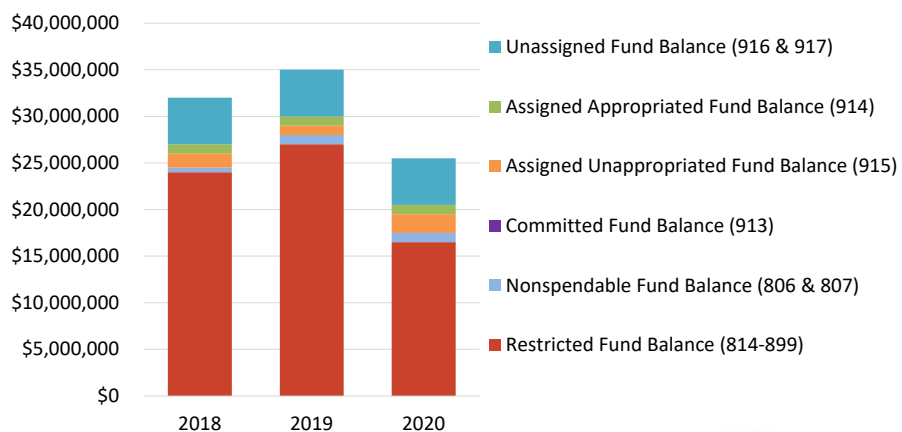
Components of Fund Balance

- *GASB 54 – Five Categories* (effective June 15, 2010)

Unrestricted Portion of Fund Balance

3. Committed (account 913)
4. Assigned (accounts 914 & 915)
 - Surplus revenues in special revenue funds, amounts set aside by Board other than legal reserves, and Reserve for Encumbrances
5. Unassigned (accounts 916 & 917)
 - Amount of surplus revenues over expenditures remaining that is not restricted or assigned in the General Fund, or deficit fund balance in all other funds

Fund Balance



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



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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.



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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



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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



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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 (916 & 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



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“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
- Experience in prior fiscal years
- Size of the fund



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Common Methods Used to Calculate 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

Beginning Fund Balance @ 1/01/21	\$782,005
+ Revenues to date (10/31/21)	\$916,870
<u>- Expenditures to date (10/31/21)</u>	<u>\$1,151,525</u>
Balance to date	\$547,350
+ Projected Revenues (11/1/ -12/31/21)	\$177,004
<u>- Projected Expenditures (11/1/-12/31/21)</u>	<u>\$125,349</u>
Estimated Fund Balance at Year-End – 12/31/21*	<u>\$599,005</u>
<u>Allocation of Estimated Fund Balance @ 12/31/21:</u>	
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 first 2 months**

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



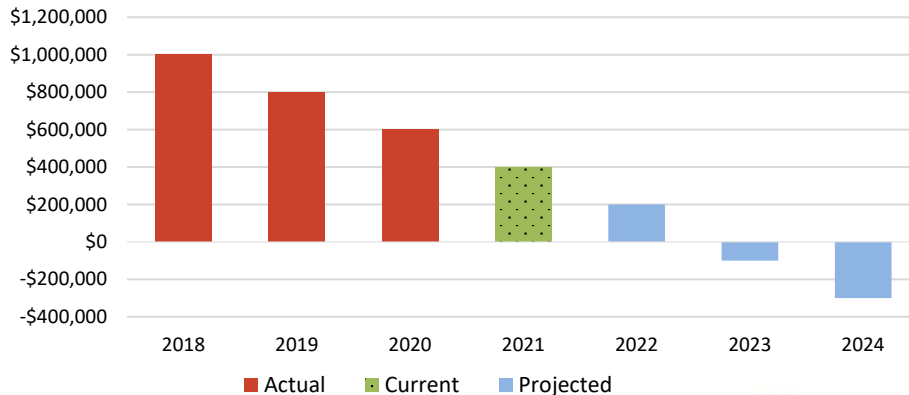
Excessively Low Fund Balance

- 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



Fund Balance Won't Last Forever

General Fund (A) Unassigned Fund Balance
(Accounts A916 & A917)



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Budget Requirement

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

- 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"

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Schedule of Estimated Fund Balances

	General (A)	Sewer (G)	Water (FX)
Estimated Total Fund Balance @ 12/31/21	\$599,005	\$186,990	\$76,650
Nonspendable Portion (Prepaid Insurance)	\$12,500	\$0	\$0
Restricted Fund Balance:			
Capital Reserve (878)	\$175,000	\$75,000	\$0
Repair Reserve (882)	\$0	\$50,000	\$22,000
Total Estimated Unrestricted FB @ 12/31/21			
Amount appropriated toward 2022 Budget (914)	\$100,000	\$10,000	\$10,000
Assigned, Unappropriated / Unrestricted FB	\$311,505	\$51,990	\$44,650
Encumbrances	\$3,650	\$6,230	-
Other Assignments	-	\$45,760	\$44,650
Unassigned (917)	\$307,855	-	-

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A Four-Pronged Approach to Managing Excess Unrestricted Fund Balance

- One-shot Expenditures
- Reduce Debt Principal
- Finance Reserve Funds
- Reduce Property Taxes

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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.).



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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.



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Finance Reserve Funds

- Reserves must be legally established
 - General Municipal Law (§§ 6-c through 6-r)
- 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



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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



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

	2018	2019	2020	2021
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 2022 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



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Thank You

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