

Town of Sangerville, Maine Fund Balance Policy

Purpose:

The purpose of this policy is to establish a target level of fund balance for the general fund and to establish a process and criteria for the continued evaluation of that target level as conditions warrant. This policy shall also establish a process for reaching and maintaining the targeted level of unassigned fund balance, and the priority for the use of amounts in excess of the target. Finally, this policy shall provide a mechanism for monitoring and reporting the Town's fund balance. This policy applies only to the general fund.

Definitions and Classifications:

Fund Balance is a term used to describe the net assets of governmental funds. It is calculated as the difference between the assets and liabilities reported in a governmental fund.

Governmental fund balance is reported in five classifications that comprise a hierarchy based primarily on the extent to which the Town is bound to honor constraints on the specific purposes for which amounts in those funds can be spent. The five classifications of fund balance are as follows:

1. *Non-spendable* – resources which cannot be spent because they are either (a) not in spendable form or: (b) legally or contractually required to be maintained in tact. Examples: inventory, prepaid expenses, long-term loans and notes receivable, principal amount of permanent funds.
2. *Restricted* – resources with constraints placed on the use of resources which are either (a) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or (b) imposed by law through constitutional provisions or enabling legislation. Examples: grants, revolving loan fund, TIFs, impact fees.
3. *Committed* – resources which are subject to limitations the government imposes upon itself at its highest level of decision-making authority, and that remain binding unless removed in the same manner. Examples: funds set aside by Town Meeting action to fund capital equipment and projects.
4. *Assigned* – resources neither restricted nor committed for which a government has a stated intended use as established by the Board of Selectmen, or a body or official to which the Board of Selectmen has delegated the authority to assign amounts for specific purposes. Examples: encumbrances, approved carry forward amounts by Town Meeting warrant articles.

5. *Unassigned* – resources which cannot be properly classified in one of the other four categories. The General Fund should be the only fund that reports a positive unassigned fund balance amount.

A negative residual amount should not be reported for restricted, committed, or assigned fund balances in any fund.

The committed, assigned, and unassigned classifications are often referred to, in the aggregate, as the *unrestricted fund balance*.

GAAP means generally accepted accounting principles in the United States.

Background and Considerations:

Fund balance is intended to serve as a measure of financial resources in a governmental fund. The Town's management, credit rating services, and others monitor the levels of fund balance in the general fund as an important indicator of the Town's economic condition. While the credit rating services have always analyzed fund balance as part of their evaluation of credit-worthiness, these services have recently focused increased attention on evaluating appropriate fund balance levels due to concerns reflected in the credit markets.

The Government Accounting Standards Board (GASB) also brought increased attention to fund balance with its fund balance project. This project culminated in GASB Statement No. 54 *Fund Balance Reporting and Governmental Fund Type Definitions*. In response to GASB's project and resulting statement, and the increased attention from credit rating agencies and others, the Government Finance Officers Association (GFOA) issued a revised "Best Practice" in 2009 entitled, *Appropriate Level of Unrestricted Fund Balance in the General Fund*. All of these events have prompted the Town of Sangerville to evaluate its circumstances and develop this policy.

In establishing an appropriate level of fund balance for the Town of Sangerville, the following factors were considered:

- *Property tax base* – The property tax is the largest revenue source of the Town's general fund. It is the source of revenue for any debt backed by the Town's general obligation pledge. In analyzing the health of the tax base it is necessary to look at the diversification of the tax base and its potential for growth.
- *Non-property tax revenues* – These resources must be considered in terms of the percentage each comprises of the total budget, as well as the reliability and stability of these resources.
- *Exposure to significant outlays* – The Town must consider its potential exposure to significant one-time outlays, either resulting from a disaster, immediate capital needs, state budget cuts or other events.

- *Debt profile* – It is essential that the Town have sufficient capacity to make its debt service payments. Sufficient capacity must be maintained in the event of interruptions or reductions in revenue flow, or in the event of unforeseen expenditures. In determining the appropriate capacity, the Town will consider its existing debt service profile as well as its future debt service profile as developed in the Town’s capital improvement program. Debt service shall be reviewed in total as well as net of any other revenues that may be used to result in a net amount to be funded from property taxes.
- *Liquidity* – An adequate level of fund balance should be maintained to ensure sufficient liquidity. The potential drain on general fund resources from other funds, as well as the availability of resources in other funds, must be considered.
- *Budget management* – Budgetary variances are an indicator of an ability to manage the Town’s financial affairs. A consistent pattern of positive budgetary variances along with moderate increases in the growth of the annual operating budget can be viewed as evidence of strong budgetary management. Evidence of weak budgetary management would necessitate higher levels of fund balance.
- *Future uses* – An adopted capital improvement program anticipates future uses of fund balance to fund minor capital improvements. Those planned uses should be considered in evaluating the appropriate level of fund balance.
- *GFOA Best Practice* – The Government Finance Officers Association (GFOA) has established a best practice that recommends, “... at a minimum, that general-purpose governments, regardless of size, maintain unrestricted fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures.” The GFOA’s best practice also states, “...governments may deem it appropriate to exclude from consideration resources that have been committed or assigned to some other purpose and focus on unassigned fund balance rather than unrestricted fund balance.”

Statement of Town Policy:

It is the policy of the Town of Sangerville to maintain an unassigned fund balance in the general fund at 12.5% of the succeeding year’s general fund including county tax and education budgeted appropriations. The Town will develop a plan in the event that the unassigned fund balance drops below this level, and implement that plan through the annual budgetary process, to bring the balance to the target level. Amounts in excess of the target may be used to fund the capital needs of the community as deemed appropriate by the Board of Selectmen if approved by Town Meeting.

The Board of Selectmen will only consider using the unassigned fund balance for exigencies that cannot be addressed through a normal budget process. However, the use of unassigned fund balance will be a last resort solution. The Board of Selectmen will consider using committed or assigned fund balance first to address exigent funding needs.

The Finance Director, in accordance with GAAP, shall report fund balance in the appropriate classifications and make the appropriate disclosures in the Town's financial statements. Unless classified as restricted or committed, the following balances shall be classified as assigned per GAAP or as required by this policy.

Encumbrances: Amounts encumbered at year-end by purchase order or another means shall be classified as assigned.

Approved Carry-Forward Amounts: Any unspent appropriations approved by Town Meeting warrant articles to be carried forward until spent, shall be classified as assigned.

Budgeted Use of Unassigned Fund Balance: Use of unassigned fund balance in a future budget and approved at Town Meeting shall be classified as assigned.

Policy Administration:

Annually the Town Manager shall report the Town's fund balance and the classification of the various components in accordance with GAAP and this policy.

The Town Manager shall annually review this policy and the considerations used in establishing the unassigned fund balance target with the Board of Selectmen. The Town Manager shall report whether changes in those considerations or additional considerations have been identified that would change the recommended level of unassigned fund balance.

Signed as approved by and on behalf of the board of selectmen at its DATE ACCEPTED regular meeting.

Melissa Randall, Chairman

Dale Gray

Mike Wark