City of Stoughton, Wisconsin
Fund Balance Policy
(REVISED JANUARY 25, 2022)

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A formal written policy governing the purpose and acceptable range of the City's various fund balances is an effective financial management tool to responsibly utilize the City's resources, to ensure the continued provision of services to residents, and to demonstrate a commitment to long term financial planning.

Although fund balance primarily focuses on the City's general fund, financial resources available in other funds should also be considered in assessing the adequacy of unrestricted fund balance (i.e. the total of the amounts in the various fund balances reported as committed, assigned, and unassigned). It is essential that the City maintain adequate levels of fund balance in the various funds to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures).

Credit rating agencies monitor levels of fund balance and unrestricted fund balance in a government's general fund to evaluate continued creditworthiness. Likewise, laws and regulations often govern appropriate levels of fund balance and unrestricted fund balance for state and local governments.

Fund balance will be classified into the following five categories depicting the relative strength of the spending constraints placed on the purposes for which resources can be used, with the highest level of constraint being "nonspendable," and the lowest being "unassigned."

1. NONSPENDABLE

Nonspendable fund balance amounts are those not in a spendable form or are required to be maintained intact. Examples are:

- Assets that will never be converted to cash *(i.*e. inventories).
- Assets that will not convert to cash soon enough to affect the current period (i.e. long-term portion of receivables and the nonfinancial assets held for resale such as land).
- Resources that must be maintained intact based on legal or contractual requirements (i.e. principal of an endowment or the capital of a revolving loan fund).

2. RESTRICTED

Restricted fund balance amounts are constrained to specific purposes by their providers, through constitutional provisions, or by enabling legislation. If amounts collected from the long-term portion of receivables or from other long-term assets held for sale are also limited externally in how they can be spent, they would be shown as restricted instead of nonspendable. Funds can become restricted because of or through:

- Other governments through laws and regulations.
- Grantors or contributors through agreements.
- Creditors through debt covenants or other contracts.
- Enabling legislation that limits how revenue can be used.

3. COMMITTED

Committed fund balance amounts are constrained to specific purposes by the City itself, using its highest level of decision-making authority. Committed fund balance amounts cannot be used for any other purpose *unless* the City takes the same highest-level action to remove or change the constraint. (Super Majority Vote)

- The action to commit the resources must be taken by the end of the reporting period.
- Note that any resources accumulated as "stabilization funds" are sometimes reported as "committed."
- If amounts collected from the long-term portion of receivables or from other long-term assets held for sale are also limited internally, they would be shown as "committed" instead of "nonspendable."

4. ASSIGNED

Assigned fund balance amounts are funds the City *intends* to use for a specific purpose. Intent can be expressed by the governing body or by an official or body to which the governing body delegates the authority. The City Finance Director is authorized to designate funds as "assigned" if the governing body does not express the intent of the fund.

- Assigned fund balance does not have to come from the governing body.
- Assigned fund balance does not have to have formal action to be considered assigned.
- Amounts in excess of "nonspendable," "restricted," and "committed" fund balance in funds other than the general fund automatically will be reported as "assigned" fund balance.
- If amounts collected from the long-term portion of receivables or from other long-term assets held for sale are limited in this manner, they would be shown as "assigned" instead of "nonspendable."
- Amounts in "assigned" fund balance can never cause "unassigned" fund balance to be a deficit.
- This is the category used to reflect the portion of existing fund balance that is planned for use to eliminate a projected deficit in the subsequent year's budget.

5. UNASSIGNED

Unassigned fund balance amounts are available for any purpose. If the general fund has net resources in excess of the other four categories that surplus is considered "unassigned."

- "Unassigned" fund balances are typically reported only in the general fund.

The order in which unrestricted resources are to be used when any of these amounts are available for expenditure will be "committed," "assigned," and then "unassigned."

GENERAL FUND BALANCE (RESERVE FUND *)

An adequate general fund (Reserve Fund *) balance provides resources to:

- Maintain sufficient working capital to finance operating expenditures without short-term borrowing for cash flow purposes.
- Temporarily finance unanticipated expenditures or unusual fluctuation in the City's revenue sources.

In determining the acceptable range of general fund (Reserve Fund *) balance, the City considers the following:

- Historical stability of the City's revenues, expenditures, and mill rate.
- Timing of revenue collections in relation to payments made for operational expenditures.
- Anticipated growth in the City's valuation and/or services and programs to be provided to City residents.
- Perceived exposure to significant one-time outlays (e.g. disasters, immediate capital needs, state budget cuts)
- The potential drain upon general fund resources from other funds as well as the availability of resources in other funds (i.e. deficits in other funds may require that a higher level of unrestricted fund balance be maintained in the general fund, just as, the availability of resources in other funds may reduce the amount of unrestricted fund balance needed in the general fund).
- Liquidity (i.e. a disparity between when financial resources actually become available to make payments and the average maturity of related liabilities may require that a higher level of resources be maintained).
- Commitments and assignments (i.e. governments may wish to maintain higher levels of unrestricted fund balance to compensate for any portion of unrestricted fund balance already committed or assigned by the government for a specific purpose).
- It is appropriate to exclude from consideration resources that have been committed or assigned to some other purpose and focus on unassigned fund balance rather than on unrestricted fund balance.

Accordingly, the City seeks to maintain its "unassigned" general fund balance (Reserve Fund *) at 20-25% of total general fund annual budgeted expenditures. In addition, any amount at year end in excess of the 25% will be allocated in the following manner:

1.) Funds in excess of the anticipated year end fund balance over the 25% will be committed to stabilization of the City's Maintenance Reserve funds (Equipment Maintenance, Building Maintenance and IT Maintenance Funds).
2.) The remaining balance of the unused excess fund balance (Reserve Fund *) each year will be committed to "one-time" equipment purchases, projects, or expenses as recommended by the Director of Finance and approved by the Common Council.

The Finance Committee will review the Reserve Fund * annually following the City's Annual Audit to recommend allocations of excess Reserve Fund * to the Common Council.

A 2/3 vote of the entire Common Council is required to allocate fund balance (Reserve Fund *).

To maintain the City's general fund balance (Reserve fund *), the City shall:

- Strive to eliminate the budgeted use of fund balance.
- Allocate any operational surplus at the end of the fiscal year as detailed above, with Council consideration given to requested carry over amounts, yet ensuring this policy's requirements are maintained.
- Caution shall be exercised to ensure the utilization of fund balance (Reserve Fund *) does not result in a spike in the required subsequent year tax levy.
- Annually where the "unassigned" fund balance (Reserve Fund *) is in excess of the recommended amount, the allocation of the excess shall be in accordance with the previously stated section of this policy.

In addition, the City Council shall establish a contingency reserve fund balance amount on an annual basis to provide for unanticipated expenditures of a nonrecurring nature, or to meet unexpected small increases in service delivery costs for any budget year. This account shall be funded at a minimum of 0.75% (.0075) and a maximum of 1.0% (.01) of the annual general fund budgeted expenditures for general fund departments 51100 through 56300. The City Council may fund the contingency reserve amount at a level higher than the maximum 1.0% of the annual general fund budgeted expenditures if it deems the action necessary.

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It shall be the responsibility of the Finance Director to monitor the aforementioned reserve balances on a regular basis and report material deviations to the Finance Committee. The amount to be reserved will be calculated on annual basis following completion of the budget and the reserved fund balance amount shall be replenished to the appropriate level at the beginning of each budget year. The process of reserving bund balance for contingency purposes shall continue until the City's unassigned balance falls below 20% of the total general fund annual budgeted expenditures as defined below. If the City falls below the 20% threshold, the City Council will need to determine whether or not it wishes to budget contingency amounts in the annual budget until the minimum threshold is once again met.

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The annual reserved fund balance amount for contingency spending shall be recorded to account 100-00000-34032 – Reserved – Contingency Spending. Annual contingency expenditures incurred shall be recorded to account 100-59200-50930.

EXAMPLE:

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2022 general fund operating budget for departments 51100 through 56300 totals $9,858,166.

$9,858,166 * .75% = $73,936

1/1/2023 or any time following that date the $79,936 will be recorded to account 100-00000-34032.

Expenditures during 2022 will be recorded to account 100-59200-50930.

The Finance Director will determine the balance required during the subsequent years' budget process and true the balance in account 100-00000-34032 as needed.

* -Defined as General Fund Unassigned Fund Balance less Unassigned Fund Balance amounts for any Other Governmental Fund not specifically shown as Nonspendable Fund Balance in the General Fund.