



CITY MANAGER'S OFFICE Executive Summary

TO: Jim Scholl, City Manager

FROM: Mark Z. Finigan, Assistant City Manager

DATE: September 9, 2010

SUBJECT: Executive Summary
Fund Balance Policy

ACTION STATEMENT:

Establish a fund balance/retained earnings policy tailored to the needs of the City of Key West to insure against unanticipated events that would adversely affect the financial condition of the City and jeopardize the continuation of necessary public services. This policy will ensure the City maintains adequate fund balance/retained earnings and reserves in the City's various operating funds to provide the capacity to: (1) provide sufficient cash flow for daily financial needs, (2), offset significant economic downturns or revenue shortfalls, and (3) provide funds for unforeseen expenditures related to emergencies. The proposed Fund Balance Policy for the City of Key West is attached.

BACKGROUND:

To follow is the "Best Practice" directive from the Government Finance Officers Association, entitled "Appropriate Level of Unrestricted Fund Balance in the General Fund (2002 and 2009) (BUDGET and CAAFR)". Such guidance can also be used when setting ranges for other City funds.

The Government Finance Officers Association (GFOA) recommends that governments establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund. Such a guideline should be set by the appropriate policy body and should provide both a temporal framework and specific plans for increasing or decreasing the level of unrestricted fund balance, if it is inconsistent with that policy.

*The adequacy of unrestricted fund balance in the general fund should be assessed based upon a government's own specific circumstances. **Nevertheless, GFOA 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 choice of revenues or expenditures as a basis of comparison may be dictated by what is more predictable in a government's particular circumstances. Furthermore, a government's particular situation often may require a level of unrestricted fund balance in the general fund significantly in excess of this recommended minimum level. In any case, such measures should be applied within the context of long-term forecasting, thereby avoiding the risk of placing too much emphasis upon the level of unrestricted fund balance in the general fund at any one time.

In establishing a policy governing the level of unrestricted fund balance in the general fund, a government should consider a variety of factors, including:

- The predictability of its revenues and the volatility of its expenditures (i.e., higher levels of unrestricted fund balance may be needed if significant revenue sources are subject to unpredictable fluctuations or if operating expenditures are highly volatile);
- Its 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); and
- 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).

Furthermore, 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 on unrestricted fund balance.

Naturally, any policy addressing desirable levels of unrestricted fund balance in the general fund should be in conformity with all applicable legal and regulatory constraints. In this case in particular, it is essential that differences between GAAP fund balance and budgetary fund balance be fully appreciated by all interested parties.

To follow are a few policy excerpts from other Florida governmental units which address unrestricted fund balance percentages and/or ranges:

- City of Leesburg
 - In the general fund, there shall be created a reservation of fund balance equal to 20% of the current fiscal year budget for the fund.
 - The City has created a total of six enterprise funds to account for the following utility services: electric, natural gas, sanitation services, communication services, water and wastewater treatment. In each of the enterprise funds now or hereafter created by the Commission, there shall be created a reservation of retained earnings equal to 25% of the current fiscal year budget for that fund.
- City of Tamarac
 - The fund balance range for the General Fund shall be not less than 7.5% and not more than 10% of the total budgeted expenditures of the General Fund budget.
 - The fund balance range for the Stormwater Fund shall be not less than 5% and not more than 7.5% of the total budgeted expenditures of the Stormwater Fund budget.
- City of Tarpon Springs
 - General Fund. There shall be a reservation (unrestricted / undesignated) of fund balance equal to 20% of the current fiscal year operating expenditure and transfers out budgeted for the fund.
- City of Fort Walton Beach.
 - Maintain a minimum General Fund unreserved/undesignated fund balance of 30% of total annual expenditures as endorsed by City Council at the May 2008 Budget Policy Meeting.
- Citrus County
 - The County will establish a minimum unreserved fund balance in the General Fund of eight (8%) and a maximum of seventeen (17%).

The aforementioned governmental units have adopted a policy which obviously has considered the unique factors and conditions of their community. It should be noted that for the most part, coastal communities tend to establish unrestricted fund balance levels which are higher than other communities. Additionally, coastal communities largely dependent on a stream of revenues that may be subject to volatility – tourist based revenues – also tend to factor such possible instability into unrestricted fund balances levels.

RECOMMENDATION:

City Commission approve the recommended Fund Balance Policy for the City of Key West.