

I. Purpose:

To ensure financial stability, the City of Cottonwood desires to manage its financial resources by establishing fund balance/net asset ranges for selected funds. This will ensure the City maintains a prudent level of financial resources to provide sufficient cash flow for daily financial needs, secure and maintain investment grade bond ratings, offset significant economic downturns and revenue shortfalls, and provide funds for unforeseen expenditures related to emergencies.

II. Definitions:

A. Fund Balance: Fund balance means the difference between fund assets and fund liabilities as reported in a governmental fund. Furthermore, Government Accounting Standard Board (GASB) Statement 54 establishes the following fund balance classifications depicting the relative strength of the constraints that control how specific amounts can be spent:

1. **Non-spendable fund balance** includes amounts that are not in a spendable form (inventory, for example) or are required to be maintained intact (the principal of an endowment fund, for example).
2. **Restricted fund balance** includes amounts that can be spent only for the specific purposes stipulated by external resource providers (for example, grant providers), constitutionally, or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
3. **Committed fund balance** includes amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority. Commitments may be changed or lifted only by the government taking the same formal action that imposed the constraint originally.
4. **Assigned fund balance** comprises amounts *intended* to be used by the government for specific purposes. Intent can be expressed by the governing body or by an official or body to which the governing body delegates the authority. In governmental funds other than the general fund, assigned fund balance represents the amount that is not restricted or committed. This indicates that resources in other governmental funds are, at a minimum, intended to be used for the purpose of that fund.
5. **Unassigned fund balance** is the residual classification for the general fund and includes all amounts not contained in the other classifications. Unassigned amounts are technically available for any purpose. If another governmental fund has a fund balance deficit, then it will be reported as a negative amount in the unassigned classification in that fund. Positive unassigned amounts will be reported only in the General Fund.

- B. Net Assets: Net assets are the difference between assets and liabilities as reported in a financial reporting unit such as proprietary funds and fiduciary funds.
- C. Fund Balance Range: Fund balance range is the range of amounts this policy has set within which the City means to maintain the undesignated fund balance.
- D. Surplus: Surplus is the amount by which the undesignated fund balance exceeds the upper limit of the fund balance range.
- E. Shortfall: Shortfall is the amount by which the lower limit of the fund balance range exceeds the undesignated fund balance.
- F. Expenditures: Expenditures are all uses of financial resources, budgeted for any purpose, and include operating and capital expenses, debt service, and transfers to other funds.
- G. Operating Expenditures: Operating expenditures are uses of financial resources for personnel, supplies, services and materials, and exclude capital expenses, debt service, and transfers to other funds.

III. Fund Balance Range:

Fund balance ranges are established for each governmental fund type which contains operating expenses, as well as, the proprietary funds. The amounts set for each fund are based on the predictability of revenues, volatility of expenditures, and liquidity requirements of each fund and may need to be reviewed periodically.

The calculation of the various fund balances to proposed expenditures will be established as part of the budget preparation process taking the previous year's revised expenditures and the established fund ratio to determine the ensuing budget year's fund balance requirements.

IV. Designations for Proprietary Funds:

Unrestricted net assets in proprietary funds do not necessarily represent resources available for appropriation. This is due to the fact that capital assets are included in proprietary funds and are offset in unrestricted net assets. Since it is not likely the organization will sell the capital asset in order to fund operations, its value is not available for appropriation. In order to take this into account when calculating the ratio related to the fund balance range, staff will identify the portion of unrestricted assets that does not represent resources available for appropriation and consider the amount "designated".

V. Funds:

- A. General Fund: The fund balance for the General Fund consists of several balances for multiple purposes. These balances are depicted below.
1. General Fund Balance: The unassigned fund balance range for the General Fund shall be not less than 16.66% and not more than 25% of the total revised budgeted operating expenditures of the General Fund budget.
 2. General Fund Capital Accumulation Fund: The assigned fund balance range for the General Fund Capital Accumulation Fund shall be any current accumulation plus not less than 2.67% of the total revised budgeted operating revenues of the General Fund budget. Currently capped at \$1,000,000.
 3. Public Safety Capital Accumulation Fund: This restricted fund balance range is an accumulation of the City's .2% sales tax after all current library bonded debt service is satisfied. The fund balance requirement for this fund should not fall below \$100,000 with no upper limit.
 4. The City may establish additional committed, assigned, or unassigned fund balances in any amount as deemed necessary.
- B. Highway User Revenue Fund (HURF): The restricted fund balance range for the HURF shall be not less than 5% and not more than 16.66% (60 days) of the total budgeted revenues of the HURF.
- C. Library Fund: The assigned fund balance range for the Library Fund shall be not be less than 0% and not more than 5% of the total budget revised expenditures of the Library Fund budget.
- D. Enterprise Funds: The fund balance range for the Enterprise Funds, including maintenance, operations and administration shall be not less than 25% (90 days) and not more than 33.3% (120 days) of the total budgeted operating expenses of the Fund. For the purpose of calculation, this reserve shall be in addition to all other required reservation of net assets including, but not limited to, amounts restricted for debt service, amounts reserved for replacement of capital assets, amounts set aside for resource development, and/or required bond covenants.
- E. Capital Projects Fund: The Capital Projects Fund was created to account for resources (such as the local government infrastructure sales surtax) designated to construct or acquire general fixed assets and major improvements. Occasionally, these projects may extend beyond a single fiscal year. Therefore, although no specific reserve requirement is established for the capital projects fund, at a minimum, the fiscal year-end assigned and unassigned fund balance, coupled with estimated revenues for the ensuing fiscal year, must be sufficient to fund all outstanding capital fund obligations.

- F. Debt Service Fund: The restricted fund balance for the Debt Service Fund is dictated by a bond indenture or similar agreement to be reserved for debt service payments in the event the government defaults on its debt.
- VI. Surplus:
If it is determined that there is a surplus (an amount in excess of the upper limit of the fund balance range for any fund), the funds are to be designated or appropriated at the next budget cycle for the following purposes in order of priority:
- A. Eliminate shortfalls in related funds. Any General Fund surplus shall be transferred to cover shortfalls within HURF, Library Fund, or any other fund initiated by the City to provide City services. Any Utilities Operating Fund surplus shall be transferred to the respective Utilities Capital Improvements Fund.
 - B. Reduction for avoidance of debt. If there is short-term debt within the fund the surplus may be applied to reduce or eliminate the debt if financial analysis proves this to be advantageous for the City. If a borrowing is scheduled, the surplus may be used to reduce the principal amount the City needs to obtain if financial analysis proves this to be advantageous for the City.
 - C. Applied to a replacement program. Surplus funds may be used to supplement or enhance a capital replacement program such as vehicle, personal computer, or heavy equipment replacement, or any other capital replacement program initiated by the City.
 - D. One-time capital needs. Since a surplus does not represent a recurring source of revenue it should not be used to fund a recurring expense; however, if a one-time capital expenditure has been identified, but not already funded through an appropriation, the surplus may be appropriated for this use.
 - E. Tax, fee, or rate stabilization. Surplus funds may be designated for stabilization in order to avoid raising taxes, fees, or rates related to the fund in subsequent years.
- VII. Shortfall:
If it is determined there is a shortfall (an amount below the lower limit of the fund balance range for any fund), the fund balance is to be replenished through the following mechanisms in order of priority:
- A. With exception of the HURF, Proprietary Fund, and Fiduciary Fund, a distribution of surplus from other related funds as delineated under “Surplus” category.
 - B. An appropriation during the next annual budget process of at least 20% of the lower limit of the fund balance range until the lower limit has been reached.

- C. If this is financially infeasible, a written plan shall be forwarded by the Administrative Services General Manager to the City Manager for Council approval in order to restore the fund balance to an amount within the range within a practical time frame. This plan may require reduction of services, increases in taxes, fees, or rates, or some combination thereof.