

## **714 FUND BALANCES**

*[Note: The provisions of this policy include the provisions of Statement No. 54 of the Governmental Accounting Standards Board (GASB).]*

### **I. PURPOSE**

The purpose of this policy is to create new fund balance classifications to allow for more useful fund balance reporting and for compliance with the reporting guidelines specified in Statement No. 54 of the Governmental Accounting Standards Board (GASB).

### **II. GENERAL STATEMENT OF POLICY**

The policy of this school district is to comply with GASB Statement No. 54. To the extent a specific conflict occurs between this policy and the provisions of GASB Statement No. 54, the GASB Statement shall prevail.

### **III. DEFINITIONS**

- A. “Assigned” fund balance amounts are comprised of unrestricted funds constrained by the school district’s intent that they be used for specific purposes, but that do not meet the criteria to be classified as restricted or committed. In funds other than the general fund, the assigned fund balance represents the remaining amount that is not restricted or committed. The assigned fund balance category will cover the portion of a fund balance that reflects the school district’s intended use of those resources. The action to assign a fund balance may be taken after the end of the fiscal year. An assigned fund balance cannot be a negative number.
- B. “Committed” fund balance amounts are comprised of unrestricted funds used for specific purposes pursuant to constraints imposed by formal action of the school board and that remain binding unless removed by the school board by subsequent formal action. The formal action to commit a fund balance must occur prior to fiscal year end; however, the specific amounts actually committed can be determined in the subsequent fiscal year. A committed fund balance cannot be a negative number.
- C. “Enabling legislation” means legislation that authorizes a school district to assess, levy, charge, or otherwise mandate payment of resources from external providers and includes a legally enforceable requirement that those resources be used only for the specific purposes listed in the legislation.

- D. "Fund balance" means the arithmetic difference between the assets and liabilities reported in a school district fund.
- E. "Nonspendable" fund balance amounts are comprised of funds that cannot be spent because they are either not in spendable form or are legally or contractually required to be maintained intact. They include items that are inherently unspendable, such as, but not limited to, inventories, prepaid items, long-term receivables, non-financial assets held for resale, or the permanent principal of endowment funds.
- F. "Restricted" fund balance amounts are comprised of funds that have legally enforceable constraints placed on their use that either are externally imposed by resource providers or creditors (such as through debt covenants), grantors, contributors, voters, or laws or regulations of other governments, or are imposed by law through constitutional provisions or enabling legislation.
- G. "Unassigned" fund balance amounts are the residual amounts in the general fund not reported in any other classification. Unassigned amounts in the general fund are technically available for expenditure for any purpose. The general fund is the only fund that can report a positive unassigned fund balance. Other funds would report a negative unassigned fund balance should the total of nonspendable, restricted, and committed fund balances exceed the total net resources of that fund.
- H. "Unrestricted" fund balance is the amount of fund balance left after determining both nonspendable and restricted net resources. This amount can be determined by adding the committed, assigned, and unassigned fund balances.

#### **IV. CLASSIFICATION OF FUND BALANCES**

The school district shall classify its fund balances in its various funds in one or more of the following five classifications: restricted, committed, assigned, and unassigned.

#### **V. MINIMUM FUND BALANCE**

The school district will strive to maintain a minimum unassigned general fund balance of **six (6) months** of operating expenses.

#### **VI. ORDER OF RESOURCE USE**

If resources from more than one fund balance classification could be spent, the school district will strive to spend resources from fund balance classifications in the following order (first to last): restricted, committed, assigned, and unassigned.

## **VII. COMMITTING FUND BALANCE**

A majority vote of the school board is required to commit a fund balance to a specific purpose and subsequently to remove or change any constraint so adopted by the board.

## **VIII. ASSIGNING FUND BALANCE**

The school board, by majority vote, may assign fund balances to be used for specific purposes when appropriate. The board also delegates the power to assign fund balances to the following: finance committee. Assignments so made shall be reported to the school board on a monthly basis, either separately or as part of ongoing reporting by the assigning party if other than the school board.

An appropriation of an existing fund balance to eliminate a projected budgetary deficit in the subsequent year's budget in an amount no greater than the projected excess of expected expenditures over expected revenues satisfies the criteria to be classified as an assignment of fund balance.

## **IX. REVIEW**

The school board will conduct an annual review of the sufficiency of the minimum unassigned general fund balance level.

***Legal References:*** Statement No. 54 of the Governmental Accounting Standards Board

***Cross References:*** MSBA Service Manual, Chapter 7, Education Funding





Adopted: May 2011

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## 714 FUND BALANCES

*[Note: The provisions of this policy include the provisions of Statement No. 54 of the Governmental Accounting Standards Board (GASB).]*

### I. PURPOSE

The purpose of this policy is to create new fund balance classifications to allow for more useful fund balance reporting and for compliance with the reporting guidelines specified in Statement No. 54 of the Governmental Accounting Standards Board (GASB).

### II. GENERAL STATEMENT OF POLICY

The policy of this school district is to comply with GASB Statement No. 54. To the extent a specific conflict occurs between this policy and the provisions of GASB Statement No. 54, the GASB Statement shall prevail.

### III. DEFINITIONS

- A. "Assigned" fund balance amounts are comprised of unrestricted funds constrained by the school district's intent that they be used for specific purposes, but that do not meet the criteria to be classified as restricted or committed. In funds other than the general fund, the assigned fund balance represents the remaining amount that is not restricted or committed. The assigned fund balance category will cover the portion of a fund balance that reflects the school district's intended use of those resources. The action to assign a fund balance may be taken after the end of the fiscal year. An assigned fund balance cannot be a negative number.
- B. "Committed" fund balance amounts are comprised of unrestricted funds used for specific purposes pursuant to constraints imposed by formal action of the school board and that remain binding unless removed by the school board by subsequent formal action. The formal action to commit a fund balance must occur prior to fiscal year end; however, the specific amounts actually committed can be determined in the subsequent fiscal year. A committed fund balance cannot be a negative number.
- C. "Enabling legislation" means legislation that authorizes a school district to assess, levy, charge, or otherwise mandate payment of resources from external providers and includes a legally enforceable requirement that those resources be used only for the specific purposes listed in the legislation.
- D. "Fund balance" means the arithmetic difference between the assets and liabilities reported in a school district fund.
- E. "Nonspendable" fund balance amounts are comprised of funds that cannot be spent because they are either not in spendable form or are legally or contractually required to be maintained intact. They include items that are inherently

unspendable, such as, but not limited to, inventories, prepaid items, long-term receivables, non-financial assets held for resale, or the permanent principal of endowment funds.

- F. "Restricted" fund balance amounts are comprised of funds that have legally enforceable constraints placed on their use that either are externally imposed by resource providers or creditors (such as through debt covenants), grantors, contributors, voters, or laws or regulations of other governments, or are imposed by law through constitutional provisions or enabling legislation.
- G. "Unassigned" fund balance amounts are the residual amounts in the general fund not reported in any other classification. Unassigned amounts in the general fund are technically available for expenditure for any purpose. The general fund is the only fund that can report a positive unassigned fund balance. Other funds would report a negative unassigned fund balance should the total of nonspendable, restricted, and committed fund balances exceed the total net resources of that fund.
- H. "Unrestricted" fund balance is the amount of fund balance left after determining both nonspendable and restricted net resources. This amount can be determined by adding the committed, assigned, and unassigned fund balances.

#### IV. CLASSIFICATION OF FUND BALANCES

The school district shall classify its fund balances in its various funds in one or more of the following five classifications: nonspendable, restricted, committed, assigned, and unassigned.

#### V. MINIMUM FUND BALANCE

The school district will strive to maintain a minimum unassigned general fund balance of **three months** of operating expenses. *6 months*

#### VI. ORDER OF RESOURCE USE

If resources from more than one fund balance classification could be spent, the school district will strive to spend resources from fund balance classifications in the following order (first to last): restricted, committed, assigned, and unassigned.

#### VII. COMMITTING FUND BALANCE

A majority vote of the school board is required to commit a fund balance to a specific purpose and subsequently to remove or change any constraint so adopted by the board.

#### VIII. ASSIGNING FUND BALANCE

The school board, by majority vote, may assign fund balances to be used for specific purposes when appropriate. The board also delegates the power to assign fund balances to the following: **Finance Committee**. Assignments so made shall be reported to the school board on a monthly basis, either separately or as part of ongoing reporting by the assigning party if other than the school board. An appropriation of an existing fund balance to eliminate a projected budgetary deficit in the subsequent year's budget in an amount no greater than the projected excess of expected expenditures over expected revenues satisfies the criteria to be classified as an assignment of fund balance.

## **IX. REVIEW**

The school board will conduct an **annual review** of the sufficiency of the minimum unassigned general fund balance level.

***Legal References:*** Statement No. 54 of the Governmental Accounting Standards Board

***Cross References:*** MSBA Service Manual, Chapter 7, Education Funding

1<sup>st</sup> reading April 25, 2011

2<sup>nd</sup> reading May 23, 2011

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### **Statement of Position Fund Balances for Local Governments Based on GASB Statement No. 54**

#### **Background**

Governmental Accounting Standards Board's (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, defines the classifications of fund balance based on the focus of the constraints placed on the use of current fund balance. The Statement also identifies the governmental fund type definitions. This Statement of Position addresses only the fund balance classifications and reporting.

The requirements of GASB 54 are applicable to all local governments. Implementation was required for the first fiscal year ended June 30, 2011. However, most Minnesota local governments report on a calendar year. For those reporting on a calendar year, the first required year for implementation was the year ended December 31, 2011.

In governmental funds,<sup>1</sup> local government should identify fund balance separately based on a hierarchy of the constraints placed on the use of the financial resources within governmental funds. A local government will classify its fund balances into one of up to 5 classifications: nonspendable, restricted, committed, assigned, and unassigned. While some of the GASB 54 classifications are similar in nature to the classifications under pre-GASB Statement No. 54, the focus is different, and thus, what is classified into these classifications may be different.

#### **Fund Balance Classifications/Definitions for Governmental Funds**

The fund balances of a local government's governmental funds should be reported in the new classifications based on the definitions in the following table:

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<sup>1</sup> Governmental fund reporting focuses primarily on the sources, uses, and balances of current financial resources and often has a budgetary orientation. The governmental fund category includes the general fund, special revenue funds, capital projects funds, debt service funds, and permanent funds. Codification of Governmental Accounting and Financial Reporting Standards § 1300.102.

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This Statement of Position is not legal advice and is subject to revision.

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<b>Fund Balance Reporting</b>			
<b>Classification</b>	<b>Definition</b>	<b>Examples</b>	
<b>Nonspendable</b>	“Amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.” <sup>2</sup>	<ul style="list-style-type: none"> <li>• Inventories,</li> <li>• Prepaid items,</li> <li>• Long-term receivables in the general fund, and</li> <li>• Permanent principal of endowment funds.</li> </ul>	
<b>Restricted</b>	“Fund balance should be reported as restricted when constraints placed on the use of resources are either: <ol style="list-style-type: none"> <li>Externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or</li> <li>Imposed by law through constitutional provisions or enabling legislation.”<sup>3</sup></li> </ol>	<ul style="list-style-type: none"> <li>• Restricted by state statute,</li> <li>• Unspent bond proceeds,</li> <li>• Grants earned but not spent,</li> <li>• Debt covenants,</li> <li>• Taxes dedicated to a specific purpose, and</li> <li>• Revenues restricted by enabling legislation.</li> </ul>	
<b>Unrestricted</b>	<b>Committed</b>	“Used for specific purposes pursuant to constraints imposed by formal action of the government’s highest level of decision-making authority.” <sup>4</sup>	<ul style="list-style-type: none"> <li>• The governing board has decided to set aside \$1M for a new city hall.</li> <li>• Property tax levies set for a specific purpose by resolution.</li> </ul>
	<b>Assigned</b>	“Amounts that are constrained by the government’s intent to be used for specific purposes, but are neither restricted nor committed.” <sup>5</sup>	<ul style="list-style-type: none"> <li>• Governing board has set aside \$2 million for a county hospital and the county manager may amend this up to \$100,000.</li> <li>• Governing body delegates the authority to assign fund balance to the finance officer.</li> <li>• Governing board has appropriated fund balance often to balance next year’s budget.<sup>6</sup></li> <li>• Positive residual balances in governmental funds other than the general fund.</li> </ul>
	<b>Unassigned</b>	Unassigned fund balance is the residual classification for the General Fund. This is fund balance that has not been reported in any other classification. The General Fund is the only fund that can report a positive unassigned fund balance. Other governmental funds would report deficit fund balances as unassigned. <sup>7</sup>	

<sup>2</sup> GASB Statement No. 54, ¶ 6.

<sup>3</sup> GASB Statement No. 54, ¶ 8.

<sup>4</sup> GASB Statement No. 54, ¶ 10.

<sup>5</sup> GASB Statement No. 54, ¶ 13.

<sup>6</sup> See appropriated fund balance section of this document.

<sup>7</sup> GASB Statement No. 54, ¶ 17.

## **Classifying Fund Balance**

A local government should classify its fund balances based on the nature of the particular net resources reported in a governmental fund. The government would first start by identifying nonspendable net resources, followed by restricted, committed, assigned and lastly unassigned. This will classify a fund's net resources from those that have the most constraints placed on their use to the least. A fund's net resources also are affected by the spending policy of that government. A local government should determine the order of use of resources when expenditures are incurred. Are restricted resources used first? Or, if available for use, are unrestricted net resources (committed, assigned, or unassigned) used first? If a local government does not have an accounting policy that identifies the order of use of resources, then the net resources with the most constraints are used first.

## **Unrestricted Fund Balance**

Unrestricted fund balance is the amount of fund balance left after determining both nonspendable and restricted net resources. The unrestricted fund balance is the amount of fund balance that a local government, itself, has placed constraints on its use (committed and assigned) and fund balance that does not have any specific purpose identified for the use of those net resources (unassigned). Unrestricted fund balance, therefore, includes the committed, assigned, and unassigned classifications. Committed and assigned fund balance represent resources set aside by the government to fund specific purposes. The two classifications differ in the formality of the action required to set aside the net resources.

The government's highest level of decision-making authority is required to commit available fund balance to a specific purpose. Once the action has been taken, the committed funds cannot be used for any other purpose unless the commitment is rescinded by the same type of action that previously committed the funds. The action taken to commit the funds must be taken prior to the end of the fiscal year, but the specific amount may be determined in the subsequent period.

The authority to assign may be delegated to an official other than the governing body. Unlike committed fund balance, the action taken to assign fund balance may be made after year end. In governmental funds other than the general fund, the assignment must follow the government's intent for the specific purpose of the individual funds. Therefore, all remaining positive fund balances in the special revenue, debt service, and capital projects funds are classified as assigned.

Unassigned fund balance represents the remaining unrestricted fund balance in the general fund after identifying fund balance that has been committed or assigned. Deficits in fund balances of other governmental funds are reported as unassigned. Assignments should never cause a deficit in unassigned fund balance to occur.

## **Stabilization Arrangements: Restricted/Committed vs. Unassigned**

Many local governments currently set aside part of fund balance for emergencies, working capital, cash flows, revenue shortages, or other contingencies. The authority to set aside these



amounts usually comes from ordinance or resolution. The GASB calls these types of funds “stabilization arrangements.” For a government to be able to set aside these types of funds as restricted or committed, they need to specifically define when these amounts may be used and specify a situation that cannot be expected to occur routinely. For example, identifying funds to be accessed “in an emergency” does not sufficiently detail the circumstance or condition that must be met for the funds to be considered committed. To commit these funds, the government needs to be more specific in defining an emergency. If the arrangement meets these requirements, it would be considered a specific purpose and reported as either restricted or committed, depending on the source of the constraint. Stabilization arrangements that do not meet the requirements should be reported as part of unassigned fund balance in the general fund.

### **Appropriated Fund Balance**

Usually a local government only classifies fund balances at year end for financial reporting purposes. Thus only current, and not future, net resources are classified. Typically, the subsequent year’s budgeted expenditures are expected to be paid from the subsequent year’s revenues and not the current reporting year’s ending fund balances. On occasion, local governments will “deficit” budget, or in other words, budget more expenditures than anticipated revenues and drawdown beginning fund balance for the subsequent year. An appropriation of existing fund balance to eliminate a projected budgetary deficit in the subsequent year’s budget in an amount no greater than the projected excess of expected expenditures over expected revenues satisfies the criteria to be classified as an assignment of fund balance.<sup>8</sup>

### **Recommendations**

#### Adoption of Comprehensive Fund Balance Policy

The GASB’s Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, identifies fund balance accounting policies that a local government may have or should consider. The Office of the State Auditor recommends that each local government establish/approve a formal comprehensive fund balance policy relating to accounting and financial reporting of governmental fund balances. A local government’s fund balance policy could address the following areas:

- Minimum fund balance
- Order of resource use
- Stabilization arrangements
- Committing fund balance
- Assigning fund balance

#### *Minimum Fund Balance*

The Office of the State Auditor recommends that local governments determine and establish in their fund balance policy a desired minimum level of unrestricted fund balance to maintain in

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<sup>8</sup> GASB Statement No. 54, ¶ 16.



their general fund and other significant governmental funds. The local government's governing body should keep revenue streams in mind when determining a minimum level of fund balance for their policy. Often a local government's revenue stream is not evenly distributed throughout the year. A local government will need sufficient beginning fund balances to pay expenditures until these revenues are received. For example, funds that rely heavily on property taxes must maintain sufficient financial resources until the next tax revenue collection cycle. Funds that rely on state appropriations and grants should consider the timing of those payments. Also, local governments need to maintain a prudent level of financial resources to protect against a forced service level reduction or having to raise taxes and fees because of temporary revenue shortfalls or unpredicted one-time expenditures.

Other considerations include the predictability of revenues and the volatility of expenditures. A local government may need higher levels of unrestricted fund balance if significant revenue sources are subject to unpredictable fluctuations or if operating expenditures are highly volatile, such as greater expenditures in the early part of the year. The availability of resources in other funds and the potential drain on the general fund resources from other funds could affect the necessary level of minimum unrestricted fund balance. The availability of resources in other funds may reduce the amount of unrestricted fund balance needed in the general fund, just as deficits in other funds may require that a higher level of unrestricted fund balance be maintained in the general fund.

After establishing a minimum level of unrestricted fund balance, the policy should provide for both a time frame and a specific plan for increasing or decreasing the level of unrestricted fund balance. If the actual unrestricted fund balance is not consistent with the policy, a plan should be developed by the governing body that will allow for compliance with the desired minimum level. The fund balance policy should include a provision for a regular review of the sufficiency of the minimum fund balance level.

#### *Order of Resource Use/Fund Balance Flow Assumption*

The Office of the State Auditor recommends that local governments include in their comprehensive fund balance policy the normal order of resource use. The policy should identify which fund balance resources (restricted or unrestricted) are normally used first when an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available. Also, for unrestricted fund balance, the local government should identify the order in which committed, assigned, or unassigned amounts are spent when an expenditure is incurred for purposes for which amounts in any of those unrestricted fund balance classifications could be used.

#### *Stabilization Arrangements*

The Office of the State Auditor also recommends that local governments consider establishing a stabilization arrangement for emergency situations in their comprehensive fund balance policy. The policy should establish the amount to be set aside, identify the types of nonroutine emergencies/situations that would meet the need for use of stabilization funds, and clearly state that the amount set aside may only be used for the identified emergency situations.

### *Committing Fund Balance*

The Office of the State Auditor also recommends that a local government's governing body identify in its comprehensive fund balance policy its process for committing fund balance to a specific purpose. The policy could identify the local government's highest level of decision making authority, what formal action is required to commit fund balance, and what specific purposes normally will require committing resources.

### *Assigning Fund Balance*

Furthermore, the Office of the State Auditor recommends each local government that decides to delegate the authority to assign fund balance for a specific purpose include in their comprehensive fund balance policy the body or official authorized to assign amounts to a specific purpose and the types of specific purposes that may be assigned by that delegated body or official. The policy should also specify how the amounts for such assignments are arrived at and whether the governing body will set the assignments annually or will set up a process to make the assignment based on the guidelines established by the governing body.

### Appropriate Fund Balance Levels

The Office of the State Auditor recommends that, at year-end and/or at other key times of the year, local governments that rely significantly on property taxes maintain an unrestricted fund balance of approximately 35 to 50 percent of fund operating revenues or no less than five months of operating expenditures in their general fund and special revenue funds. This amount of unrestricted fund balance should provide the local government with adequate funds until the next property tax revenue collection cycle. The adequacy of unrestricted fund balance should be assessed based on an individual local government's own circumstances. If the local government's unrestricted fund balance is less than or greater than the recommended level, the local government should be able to explain the reason for the difference.

According to the Minnesota Department of Education, Minnesota school districts, unlike most local governmental units, experience timing of receipts from local property tax levies, state aids, and federal aids that provide a more reliable flow of cash to fund operations. Therefore, a recommended unrestricted fund balance for school districts may be less than the amounts recommended above for other local governmental units. Each school district should determine the appropriate level of unrestricted fund balance based on the school district's circumstances.

Local governments should also consider taking a position on the level of unrestricted fund balance in other funds that have unrestricted revenues. In setting an appropriate level, the local government should consider any long-term forecasting/planning issues to avoid the risk of placing too much emphasis on the level of unrestricted fund balance at any one time.