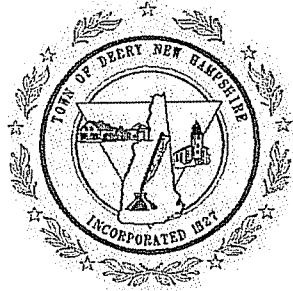


Town of Derry, NH



To: Town Council
From: Dave Caron, Town Administrator
Susan Hickey, CFO
Date: February 25, 2017
Re: Use of Fund Balance

It appears that the use of fund balance as discussed at the Council's February 21 meeting has spurred questions regarding the amount of Unassigned Fund Balance (UFB, or "true surplus") which was expended in FY16. Adding to the confusion is the auditor's practice to include all fund balance categories into its presentation, which leads to the erroneous conclusion that the Town expended over \$6.6M in "true surplus" in FY16.

Conclusion: During FY16, the Town Council issued Supplemental Appropriations which expended "true surplus" in the amount of \$1,966,187 net of guaranteed reimbursement, for the following expenses:

<i>Exit 4A</i>	<i>\$ 1,271,387</i>
<i>Tax Stabilization</i>	<i><u>\$ 694,800</u></i>
<i>UFB used</i>	<i>\$ 1,966,187</i>

The amount does not include the temporary use of UFB in the amount of \$2,509,000 for MTBE mitigation (water line extension) which will be repaid to the UFB by the NH Department of Environmental Services. Thus, the total amount expended from UFB was approximately \$4.47M; the NHDES reimbursement will show an addition of \$2.51M to UFB once the Town receives these funds.

It is first helpful to understand the various categories of Fund Balance:

Fund Balance – Generally, fund balance represents the difference between current assets and current liabilities. In accordance with the Governmental Accounting Standards Board (GASB) Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, it is recognized that fund balance shall be classified into one or more of the following categories in order to be compliant with GASB standards:

- i) Non-spendable Fund Balance contains Permanent trust funds (non-expendable portion) and non-cash assets such as inventories or prepaid items.
- ii) Restricted Fund Balance contains funds legally restricted for specific purposes, such as grants, revenues library funds, income balances of permanent funds and capital project funds. The category also includes the amount available in the Waste Water Fund and the Water Enterprise Fund; those amounts would be reported similar to UFB in the General Fund or as retained earnings in the private sector, however, these available “surplus” funds are noted as restricted as they are restricted to the fund from which they are derived (e.g. sewer funds for sewer purposes, etc..).
- iii) Committed Fund Balance are reported and expended as a result of motions passed by the highest decision making authority in Town (i.e. Town Council).
- iv) Assigned Fund Balance is used for specific purposes as established by management, such as encumbrances. Encumbrances occur when funds are appropriated by the Town Council for a specific purpose, and that purpose or item has not been completed or acquired prior to the end of the budget year. In these instances, the funds are encumbered into the next fiscal year and used to complete that project or acquisition.

v) Unassigned Fund Balance (UFB) - Unassigned fund balance is an important measure of economic stability, and contains residual spendable fund balance after deducting all of the above amounts from total fund balance. It is from UFB that the Town Council determines annually the appropriate amount to use to stabilize the tax rate or vote Supplemental Appropriations. UFB is ‘true surplus’.

Applying the definitions of fund balance listed above, resources flow between these funds based upon the budget approved by the Council and the timing of purchases and completion of projects. Listed below is the FY16 year-end performance of the various funds:

Use of Unassigned F/B	(4,475,187)
Use of Committed and Restricted F/B	(2,153,243)
Change in nonspendable FB	151,820
Change in restricted FB	87,264
Change in committed FB	156,768
Change in assigned FB	(185,734)
Add back CY encumbrances to get back to GAAP basis	1,690,825
Less expenses of PY encumbrances - various	(114,899)

The confusion arises when the auditors lump the first two categories together (UFB and Committed/Restricted Fund Balance) which leaves the impression that the Council approved the use of over \$6.6M in “true surplus”. As stated previously, of that amount, approximately \$1.97M was expended from “true surplus” for projects. Looked at a different way, the amount expended on Exit 4A (\$1.27M) to satisfy part of the Town’s legal obligation to that project is quite similar to the amounts transferred from surplus to various Capital Reserve Funds (CRF) in past years, in accordance with the Council’s current Fund Balance Policy. Simply put, the Council for FY16 reprioritized its use of UFB for Exit 4-A instead of funding CRFs.

Going forward, I anticipate the following presentation on UFB which portrays a more accurate picture of UFB “true cash” from which the Council may appropriate to CRFs and other community priorities or obligations such as 4A or conservation land:

Beginning Unassigned Fund Balance (UFB)	11,319,369
Excess Revenues from budget vs actual on budgetary basis	657,758
Unexpended appropriations from BVA (budgetary basis)	1,841,846
Use of Unassigned F/B	(4,475,187)
Changes in other Fund Balance categories and encumbrances	(367,199)
Ending Unassigned Balance (UFB)	8,976,587

We will present on this issue at the Council’s March 6 meeting, and Councilors are encouraged to share this information with any members of the public who have the misperception that over \$6.6M was expended from “true cash” or there is some confusion within the organization regarding the use, accountability and allocation of fund balance.