

COUNTY OF SANTA CRUZ POLICIES AND PROCEDURES MANUAL FUND BALANCE POLICY

TITLE I – FINANCE AND ACCOUNTING

SECTION 450 - FUND BALANCE POLICY

A. PURPOSE

The County of Santa Cruz establishes and will maintain classifications of fund balance, as defined herein, in accordance with Governmental Accounting and Financial Standards Board Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. The Fund Balance Policy will help the County maintain a strong fiscal position to weather negative economic trends, and provide financial resources to protect the County against unforeseen circumstances and events such as revenue shortfalls and unanticipated expenditures. It also is intended to preserve flexibility to make adjustments in funding for programs approved in connection with the annual budget. The Fund Balance Policy is established with a long-term perspective, recognizing that stated thresholds are considered minimum balances. This Policy shall only apply to the County's governmental funds.

B. FUND BALANCE DEFINITIONS

Fund balance is essentially the difference between the assets and liabilities reported in a governmental fund. There are five separate components of fund balance, each of which identifies the extent to which the County is bound to honor constraints on the specific purpose for which amounts can be spent.

1. **Nonspendable Fund Balance** - consists of funds that cannot be spent due to their form, such as inventories or prepaid invoices, or funds that legally or contractually must be maintained intact.
2. **Restricted Fund Balance** - includes amounts that can be spent only for the specific purposes stipulated by constitution, external resource providers, or through enabling legislation.
3. **Committed Fund Balance** - includes amounts that can be used only for the specific purposes determined by a formal action of the Board of Supervisors. Formal action must be taken prior to the end of any fiscal year to establish, change or remove the limitation placed on these funds.
4. **Assigned Fund Balance** – consists of funds set aside for specific purposes but do not meet the criteria for Restricted or Committed. These can be established, changed or removed by the Board of Supervisors or delegated to an official. Assigned funds cannot cause a deficit in Unassigned fund balance. Governments are required to disclose information about the processes through which constraints are imposed on amounts in the Committed and Assigned classifications.

5. **Unassigned Fund Balance** – is the residual classification for the General Fund and includes all spendable amounts not contained in the other classifications. These funds are available for any purpose in the fund.

PROVISIONS

1. Nonspendable Fund Balance

Funds will be classified as Nonspendable based upon the underlying nature of the related asset. No policy statement is required for funds to be classified as Nonspendable.

2. Restricted Fund Balance

Funds will be classified as Restricted based upon the nature of the externally stipulated restriction. No policy statement is required for funds to be classified as Restricted.

3. Committed Fund Balance

The Board of Supervisors has the authority to set aside funds for a specific purpose. The establishment of Committed fund balance requires the passage of a resolution by a simple majority vote before June 30 of the applicable fiscal year. Board action is required to change or remove the commitment. The Board resolution shall identify the title of the commitment, describe the specific purpose for the commitment, and the actual amount of the commitment or the process or formula necessary to calculate the actual amount. Funding for Committed fund balance shall be approved annually by the Board of Supervisors as part of the budget approval process.

4. Assigned Fund Balance

The Board of Supervisors has the authority to assign funds for a specific purpose with a simple majority vote. The same action is required to change or remove an assignment.

The County Administrative Officer also has the authority to assign funds for specific purposes, and to change or remove the assignment. The establishment change or removal of an assignment by the County Administrative Officer must be reported to the Board of Supervisors at the earliest opportunity. The Board may change or remove an assignment established by the County Administrative Officer with a simple majority vote.

An appropriation of existing fund balance to eliminate a projected budgetary deficit in the subsequent year's budget may be classified as Assigned fund balance.

5. Unassigned Fund Balance

Unassigned fund balance is the residual amount of fund balance in the General Fund. It represents the resources available for future spending. An appropriate level of Unassigned fund balance should be maintained in the General Fund to cover unexpected expenditures and revenue shortfalls. Unassigned fund balance may be accessed in the event of unexpected expenditures.

C. STABILIZATION ARRANGEMENTS

A stabilization arrangement may be established to provide funds for an urgent event that affects the safety of employees, residents or property. A stabilization arrangement will be classified as either Restricted or Committed fund balance, depending on the source of constraint on its use. The Board of Supervisors has the authority to establish a stabilization arrangement that will be classified as Committed fund balance. The Board resolution establishing the committed

stabilization arrangement shall identify the title of the stabilization arrangement, and describe the specific, non-routine circumstances under which the stabilization arrangement may be spent. Stabilization arrangements that do not meet the criteria to be classified as Restricted or Committed are required to be classified as Unassigned fund balance.

D. MINIMUM BALANCE

The minimum fund balance in the County General Fund's Committed and Assigned fund balance categories shall be no less than a total of 7% of the upcoming budget year's estimated revenues. The amount of each fund balance classification shall be estimated and reported in both the Proposed Budget and the Adopted Budget based on the upcoming budget year's revenues as estimated in those documents. If the General Fund balance falls below the minimum, the County shall develop a funding plan and a timeframe to bring it to the minimum balance.

E. ORDER OF USE OF FUND BALANCE

Unless the Board of Supervisors takes action stating otherwise at the time the expenditure is approved, the County considers Restricted fund balances to be spent first when an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available. Similarly, when an expenditure is incurred for purposes for which amounts in any of the unrestricted classifications of fund balance could be used, the County considers Committed amounts to be reduced first, followed by Assigned amounts and then Unassigned amounts.

F. MONITORING, REPORTING AND REVIEWING

The County Executive Officer and Auditor-Controller shall jointly prepare an annual report documenting the status of fund balance for the Board's review in conjunction with consideration of the annual budget. The County's Fund Balance Policy shall be reviewed annually to evaluate its sufficiency.

G. SPECIFIC GENERAL FUND COMMITTED RESERVES

1. Reserve for Working Capital

Purpose – The Reserve for Working Capital is intended to remain intact and unused to assist the County in maintaining a minimal fund balance.

Establishment and Approval – This stabilization arrangement will be established by a resolution of the Board of Supervisors, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a four-fifths vote of the Board of Supervisors appropriating the funds, and a resolution by the Board of Supervisors declaration of Fiscal Emergency.

Fund Balance Classification – Committed fund balance stabilization arrangement

2. Reserve for Economic Uncertainty

Purpose – The Reserve for Economic Uncertainty will only be used during recessions or periods of economic distress as measured by periods of time when the local unemployment rate exceeds 8% and or the rate of inflation exceeds the growth in property tax revenue.

Establishment and Approval – This stabilization arrangement will be established by a resolution of the Board of Supervisors, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a four-fifths vote of the Board of Supervisors appropriating the funds.

Fund Balance Classification – Committed fund balance stabilization arrangement

3. Reserve for Natural Disasters

Purpose – The Reserve for Natural Disasters is to fund the extraordinary operating costs, legal costs and cash flow problems associated delays in State and Federal reimbursements for any natural disaster declared by County’s Director of Emergency Services and subsequently ratified by the Board of Supervisors, and the State of California or the federal government.

Establishment and Approval – This reserve will be established by a resolution of the Board of Supervisors, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a four-fifths vote of the Board of Supervisors appropriating the funds.

Fund Balance Classification – Committed fund balance

4. Reserve for Mental Health Services

Purpose – Welfare and Institutions Code (WIC) Section 5847(a)(7) require each county establish and maintain a MHSA Prudent Reserve fund to ensure that in years in which revenues for the MHSA Fund are below recent averages, the county will be able to continue to serve children, adults and seniors through the MHSA Community Services and Supports (CSS) and Prevention and Early Intervention (PEI) programs.

Establishment and Approval – This reserve will be established by a resolution of the Board of Supervisors, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a four-fifths vote of the Board of Supervisors appropriating the funds.

Fund Balance Classification – Committed fund balance

H. SPECIFIC GENERAL FUND ASSIGNED RESERVES

1. Assignment for Federal Qualified Health Programs

Purpose – This assignment for Federal Qualified Health Programs is intended to provide a reserve for federally qualified health service programs 1) to provide a cushion to mitigate risk associated with mental health managed care programs, (2) to provide an audit reserve for disallowed mental health costs under State or federal programs, and (3) to hold for possible future repayments of grant funds. Other cost savings and unanticipated revenues should be relied on first before the use of the assignment for federally qualified health service programs.

Establishment and Approval – This assignment will be established by the County Administrative Officer, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a simple majority vote of the Board of Supervisors appropriating the funds

Fund Balance Classification – Assignment for federally qualified health programs.

2. Assignment for Unanticipated Liabilities

Purpose – The Assignment for Unanticipated Liabilities is intended to provide a reserve to mitigate the risk of unanticipated liabilities not covered by the Property and Liability Fund. Other cost savings and any unanticipated revenues should be relied on first before the use of the assignment for unanticipated liabilities.

Establishment and Approval – This assignment will be established by the County Administrative Officer, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a simple majority vote of the Board of Supervisors appropriating the funds.

Fund Balance Classification – Assignment for unanticipated liabilities.

3. Assignment for Human Services Programs

Purpose – The Assignment for Human Services Programs is intended to provide a reserve for human services programs 1) to provide a cushion to mitigate risk associated with one-time only fluctuations in federally or State funded human services programs, and (2) to provide an audit reserve for disallowed human services costs under State or federal programs. Other

cost savings or unanticipated revenues should be relied on first before the use of the assignment for human services.

Establishment and Approval – This assignment will be established by the County Administrative Officer, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a simple majority vote of the Board of Supervisors appropriating the funds.

Fund Balance Classification – Assignment for Human Services programs.

4. Assignment for the Budgeted Structural Deficit

Purpose – The Assignment for the Budgeted Structural Deficit is to provide adequate funding when the current year budget to actual savings does not fund the necessary carryover fund balance. Contingencies and other cost savings and unanticipated revenues should be relied on first before the use of the assignment for the budgeted structural deficit.

Establishment and Approval – This assignment will be established by the County Administrative Officer, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a simple majority vote of the Board of Supervisors appropriating the funds.

Fund Balance Classification – Assignment for Budgeted Structural Deficit.

5. Assignment for the Budgeted Salary Savings

Purpose – The Assignment for the Budgeted Salary Savings is to provide coverage for the salary and benefit cost which is typically not budgeted and relies on turnover and salary savings during the year. Contingencies and other cost savings and unanticipated revenues should be relied on first before the use of the assignment for the Salary Savings.

Establishment and Approval – This assignment will be established by the County Administrative Officer, and will be approved annually by the Board during the budget approval process.

Use of Funds – Requires a simple majority vote of the Board of Supervisors appropriating the funds.

Fund Balance Classification – Assignment for the Budgeted Salary Savings.

I. OTHER PROVISIONS

1. Special Revenue Funds

Special revenue funds are created to account for the proceeds of specific revenue sources that are legally restricted to expenditure for specified purposes. Special revenue funds shall maintain a positive fund balance without the need for support from the County General Fund. If the fund balance is not positive at any year end, the County shall develop a funding plan and a timeframe to bring it into a positive state. Unless the Board of Supervisors takes action stating otherwise at the time the expenditure is approved, fund balance in special revenue funds shall be spent in the following order of priority when possible: Restricted, Committed, and then Assigned.

2. Debt Service Funds

Debt service funds are typically required to create specific reserve amounts as part of the ordinance or resolution which authorizes the issuance of the bonds. This policy does not create any specific fund balance requirement within any debt service fund. Reserve requirements for any outstanding bond issue will be consistent with the ordinance or resolution authorizing the issuance of the bonds.

3. Capital Projects Fund

The Capital Projects Fund is created to account for resources designated to construct or acquire capital assets and major improvements. These projects may extend beyond a single fiscal year. No specific fund balance requirement is established for this fund. However, the fund should maintain, at a minimum, a fiscal year end fund balance plus estimated revenues sufficient to meet all outstanding projects.

4. Internal Service Funds

Internal service funds are dependent upon a reasonable level of working capital reserve to operate from one billing cycle to the next. Charges by an internal service activity to fund the establishment and maintenance of a reasonable level of working capital reserve, in addition to the full recovery of costs, are allowable. Internal service funds shall maintain a positive fund balance without the need for support from the County General Fund. If the fund balance is not positive at any year end, the County shall develop a funding plan and a timeframe to bring it into a positive state. The only exception to this general rule is the Workers' Compensation Internal Service Fund because of the nature of actuarial liabilities in that fund.