Submitted by: Chair of the Assembly at the Request of the Mayor
Prepared by: Finance Department
For reading: December 13, 2011

See AR 2011-345(S)

ANCHORAGE, ALASKA
AR No. 2011-345

A RESOLUTION OF THE MUNICIPALITY OF ANCHORAGE AMENDING THE FUND BALANCE POLICY TO COMPLY WITH GASB STATEMENT NO. 54.

WHEREAS, in 2002, the Municipality of Anchorage entered into a Memorandum of Agreement with the Anchorage School District to "maintain general fund unreserved fund balances in an amount equal to or greater than 8.25% of revenues from local tax appropriations" in support of the municipality's bond rating;

WHEREAS, the Assembly approved AR 2004-154 adopting an unreserved fund balance designation policy for Municipality of Anchorage General Government that designated 8.25% of prior year revenues as Bond Reserve Designation and 2.5% as an Operating Emergency Reserve;

WHEREAS, it has been the practice of the ASD to set aside approximately 10% of its prior year total general fund expenditures as unreserved fund balance, including funds restricted for support of the bond rating;

WHEREAS, in 2011 the Governmental Accounting Standards Board implemented a new statement, GASB 54, that modifies the financial reporting requirements and fund balance definitions;

WHEREAS, in 2010 Fitch Ratings has indicated that "the policy of maintaining reserves equal to at least 10.25% of revenues provides sufficient financial flexibility for the 'AA" rating category…";

WHEREAS, in 2011, Fitch indicated that the MOA's unreserved fund balance of 11.4% "is somewhat below average for this rating level";

WHEREAS, the Municipality's Financial Advisor, First Southwest, has recommended a modification to our fund balance designations (see attached); and

WHEREAS, the Government Finance Officers Association states that "As a general rule, unrestricted fund balance in the general fund should represent no less than two months of operating revenues or operating expenditures *(whichever is less volatile)"*; now, therefore,

THE ANCHORAGE ASSEMBLY RESOLVES:

<u>Section 1.</u> The MOA Fund Balance Policy is amended to conform to GASB 54 Standards.

Section 2. It is the policy of the Municipality of Anchorage to prepare and manage budgets so as to maintain unrestricted general fund balance in an amount equal to 10% of current year revenues as a Bond Rating Designation that will become committed fund balance.

Section 3. It is the policy of the Municipality of Anchorage to prepare and manage budgets so as to maintain unrestricted fund balances in its five major funds in an amount between 1.25% and 3% of current year's revenues as a Working Capital Reserve that will become part of unassigned fund balance.

Section 4. The Administration is requested to work with the Anchorage School District to modify the Memorandum of Agreement to reflect an ASD restriction of fund balance equal to 10% of revenues from local tax appropriations as a Bond Rating Designation.

Section 5. It is the policy of the Municipality to replenish deficiencies in either the Bond Rating Designation or Working Capital Reserve over a period not to exceed two years.

Section 6. AR 2004-154 is hereby superseded.

Section 7. This resolution shall be effective immediately upon passage and approval by the Assembly.

PASSED AND APPROVED by the Anchorage Assembly this _______ day of _______________, 20___.

____
Chair of the Assembly

ATTEST:

____
Municipal Clerk

MUNICIPALITY OF ANCHORAGE

ASSEMBLY MEMORANDUM

No. AM733-2011

Meeting Date: December 13, 2011

From: **MAYOR**

Subject: **A RESOLUTION OF THE MUNICIPALITY OF ANCHORAGE AMENDING THE FUND BALANCE POLICY TO COMPLY WITH GASB STATEMENT NO. 54.**

Purpose:
The Municipality of Anchorage recommends amending the current fund balance policy in order to address the implications of Governmental Accounting Standards Board ("GASB") Statement No. 54, Fund Balance Reporting and Governmental Fund Definitions. The policy is created in consideration of unanticipated events that could adversely affect the financial condition of the Municipality and jeopardize continuation of necessary public services. This policy will ensure that the Municipality maintains adequate fund balances and reserves in order to:

a. Provide sufficient cash flow for daily financial needs,
b. Secure and maintain investment grade bond ratings,
c. Offset significant economic downturns or revenue shortfalls, and
d. Provide funds for unforeseen expenditures related to emergencies.

Fund type definitions:
Unless Municipal Code specifies a different requirement, the following definitions will be used in reporting activity in governmental funds across the Municipality. The Municipality may or may not report all fund types in any given reporting period, based on actual circumstances and activity.

The general fund is used to account for all financial resources not accounted for and reported in another fund.

Special revenue funds are used to account and report the proceeds of specific revenue sources that are restricted or committed to expenditures for specific purposes other than debt service or capital projects.

Debt service funds are used to account for all financial resources restricted, committed or assigned to expenditure for principal and interest.

Capital projects funds are used to account for all financial resources restricted, committed or assigned to expenditures for the acquisition or construction of capital assets.

Permanent funds are used to account for resources restricted to the extent that only earnings, and not principal, may be used for items that support the Municipality's purposes.

Fund balance reporting in governmental funds:
Fund balance will be reported in governmental funds under the following categories using the definitions provided by GASB Statement No. 54:

Nonspendable fund balance includes amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained in-tact.

Nonspendable amounts will be determined before all other classifications and consist of the following items (as applicable in any given fiscal year):

- The Municipality will maintain a fund balance equal to the balance of any long-term outstanding balances due from others (including interfund loans of the Municipality).
- The Municipality will maintain a fund balance equal to the value of inventory balances and prepaid items.
- The Municipality will maintain a fund balance equal to the corpus (principal) of any permanent funds that are legally or contractually required to be maintained in-tact (e.g. cemetery trust).
- The Municipality will maintain a fund balance equal to the balance of any land or other nonfinancial assets held for sale.

Restricted fund balance includes amounts that can be spent only for the specific purposes imposed by creditors, grantors, contributors, laws and regulations of other governments or through enabling legislation (e.g. E911 funds, grants including match).

Committed fund balance includes amounts that can be used only for the specific purposes determined by a formal action of the Municipality's highest level of decision-making authority (i.e., the Assembly). Commitments will only be used for specific purposes pursuant to a formal action of the Assembly and any changes can only be done with similar formal action. Formal action must be approved prior to the end of the fiscal year (e.g. bond rating designation).

Assigned fund balance includes amounts intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed. In governmental funds other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed (e.g. TAPS reserve).

Unassigned fund balance includes the residual classification for the Municipality's general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification should be used only to report a deficit balance from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

Operational guidelines

The following guidelines address the classification and use of fund balance in governmental funds:

Classifying fund balance amounts

Fund balance classifications depict the nature of the net resources that are reported in a governmental fund. An individual governmental fund may include nonspendable resources and amounts that are restricted, committed, or assigned, or any combination of those classifications. The general fund may also include an unassigned amount.

Encumbrance reporting

Encumbering amounts for specific purposes for which resources have already been restricted, committed or assigned should not result in separate display of encumbered amounts. Encumbered amounts for specific purposes for which amounts have not been previously restricted, committed or assigned, will be classified as committed or assigned, as appropriate, based on the definitions and criteria set forth in GASB Statement No. 54.

Prioritization of fund balance use

When an expenditure is incurred for purposes for which both restricted and unrestricted (committed, assigned, or unassigned) amounts are available, it shall be the policy of the Municipality to consider restricted amounts to have been reduced first. When an expenditure is incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used, it shall be the policy of the Municipality that committed amounts would be reduced first, followed by assigned amounts and then unassigned amounts.

Minimum unrestricted fund balance

The Municipality recognized that an adequate level of unrestricted fund balance is essential to mitigating current and future risk such as revenue shortfalls and unanticipated expenditures to ensure stable tax rates and establish a level of predictability necessary to facilitate effective long-range fiscal planning. The appropriation of fund balance should be limited to uses of a one-time or emergency nature, or to fund investment opportunities expected to achieve significant cost savings.

It is the policy of the Municipality of Anchorage that the general government will prepare and manage budgets so as to maintain unrestricted general fund balance in an amount equal to 10% of current year revenues as a Bond Rating Designation. Revenues will exclude Anchorage School District revenues and Other Financing Sources. The Bond Rating Designation will become part of the committed fund balance for financial statement reporting.

Additionally, the Municipality of Anchorage will prepare and manage budgets so as to maintain unrestricted fund balances in its five major funds – Areawide General, Anchorage Fire SA, Anchorage Roads and Drainage SA, Anchorage Metro Police SA and Anchorage Parks and Recreations SA in an amount between 1.25% and 3% of current year's revenues as defined above. This Working Capital Reserve shall be used for nonrecurring, unpredictable or unforeseen needs that arise during the fiscal year including expenses associated with emergencies declared by the Mayor, Governor of the State of Alaska or the President of the United States, unexpected liability created by Federal or State law, shortfalls of budgeted revenue, or unanticipated expenditures.

A Working Capital Reserve will also be established for the following Non-Major Governmental Operating Funds:

104	Chugiak Fire SA	2.50%
105	Glen Alps SA	20.00%
106	Girdwood Valley SA	20.00%
111	Birch Tree/Elmore LRSA	20.00%
112	Section 6/Campbell Airs LRSA	20.00%
113	Valli Vue Estates LRSA	20.00%
114	Skyranch Estates LRSA	20.00%
115	Upper Grover LRSA	20.00%
116	Raven Woods/Bubblng Brook LRSA	20.00%
117	Mountain Park Estates LRSA	20.00%
118	Mountain Park/Robin Hill RRSA	20.00%
119	Chugiak/Birchwood/ER RRSA	$100,000 flat
123	Lakehill LRSA	20.00%
124	Totem LRSA	20.00%
125	Paradise Valley South LRSA	20.00%
126	SRW Homeowners LRSA	20.00%
129	Eagle River Street Lighting SA	20.00%
142	Talus West LRSA	20.00%
143	Upper O'Malley LRSA	20.00%
144	Bear Valley LRSA	20.00%
145	Rabbit Creek View/Heights LRSA	20.00%
146	Villages Scenic Parkway LRSA	20.00%
147	Sequoia Estates LRSA	20.00%
148	Rockhill LRSA	20.00%
149	South Goldenview Area RRSA	5.00%
162	ER/Chugiak Park & Rec SA	2.50%

This Working Capital Reserve can be used for any needs listed above as well as for inordinate snow and ice events, emergency road repairs and other unexpected qualifying needs for both Limited Road Service Areas and Rural Road Service Areas, as approved by the appropriate advisory boards.

The Working Capital Reserve will become part of the Unassigned Fund Balance for financial statement reporting purposes.

Replenishing deficiencies **:**
When fund balance falls below the minimum 10% for Bond Rating Designation or 1.25%-3% for Working Capital Reserve, the Municipality will replenish shortages/deficiencies using the budget strategies and timeframes.

The following budgetary strategies shall be utilized by the Municipality to replenish funding deficiencies:

- The Municipality will reduce recurring expenditures to eliminate any structural deficit or,
- The Municipality will increase revenues or pursue other funding sources, or,
- Some combination of the two options above.

It is policy of the Municipality to replenish fund balance deficiencies over a period not to exceed two years.

THE ADMINISTRATION RECOMMENDS APPROVAL OF THE RESOLUTION OF THE MUNICIPALITY OF ANCHORAGE AMENDING THE FUND BALANCE POLICY TO COMPLY WITH GASB STATEMENT NO. 54.

Prepared by:	David Ryan, Controller
Approved by:	Lucinda Mahoney, CFO
Concur:	George J. Vakalis, Municipal Manager
Respectfully submitted:	Daniel A. Sullivan, Mayor

FirstSouthwest
A PlainsCapital Company.

Memorandum

250 West 57th Street
Suite 1420
New York, NY 10107

(212) 642-4350 Direct
(917) 545-2864 Cell
(212) 642-4357 Fax

Steven J. Kantor
Managing Director

steven.kantor@firstsw.com

Date: July 29, 2011

To: Ross Risvold, Public Finance Director, Municipality of Anchorage

Cc:

Subject: Municipality of Anchorage Fund Balance - Peer Comparison

---

As you know, on May 18, 2011, Fitch Ratings released a new issue credit report for the Municipality of Anchorage ("MOA") in conjunction with the MOA's Series 2011 A, B and C general obligation bond issue. In the report, Fitch affirmed its "AA+" rating and Stable Outlook for the MOA, citing various inherent credit strengths that figured prominently in the rating review process. Two key rating drivers identified by Fitch included:

- Maintenance of structural budget balance and adequate reserve levels in the face of cost pressures; and
- Performance of the local and state economy.

However, the report also included the comment that the MOA's "*...current reserve position is somewhat below average for this rating level.*"

In response to your request to determine the veracity of the aforementioned comment, following please find a peer comparison table listing the unreserved fund balance positions of cities of comparable size to the MOA (i.e., population between 200,000 – 500,000) and who are also rated either Aa1 or Aa2 by Moody's Investors Service. Please note the information is extracted from the Moody's Municipal Financial Ratio Analysis ("MFRA") database. We recognize the MOA's bonds are no longer rated by Moody's, but it is the only agency that has a product that can generate such comparative analysis.

Please note the MFRA-generated information is a calculation of the given city's reserve amount as a percentage of total General Fund revenues. The Fitch-cited reserve percentages are calculated using total General Fund expenditures. While these calculations are different, since most fiscal year budgets are "balanced", one could argue the MFRA data can be used as a proxy to the Fitch calculation.

To facilitate your review, we have divided the peer information by rating category:

	Rating	Unreserved General Fund Balance as % of Revenues
Albuquerque, NM	Aa1	8.8
Anaheim, CA	Aa1	15.8
Arlington, TX	Aa1	29.0
Aurora, CO	Aa1	9.4
Cincinnati, OH	Aa1	15.0
Fort Wayne, IN	Aa1	25.3
Islip, NY	Aa1	73.8
North Hempstead, NY	Aa1	21.8
St Paul, MN	Aa1	17.1
Tampa, FL	Aa1	33.3
Tulsa, OK	Aa1	19.1
Wichita, KS	Aa1	11.2
Atlanta, GA	Aa2	13.0
Babylon, NY	Aa2	-8.7
Birmingham, AL	Aa2	23.8
Brookhaven, NY	Aa2	36.5
Colorado Springs, CO	Aa2	15.7
Corpus Christi, TX	Aa2	13.7
Glendale, AZ	Aa2	21.0
Kansas City, MO	Aa2	5.2
Las Vegas, NV	Aa2	15.7
Long Beach, CA	Aa2	11.1
Mesa, AZ	Aa2	22.9
Montgomery, AL	Aa2	2.4
Norfolk, VA	Aa2	8.7
Oakland, CA	Aa2	24.7
Oyster Bay, NY	Aa2	7.1
Sacramento, CA	Aa2	13.1
St. Petersburg, FL	Aa2	19.8
Tucson, AZ	Aa2	9.4

Based on the information above, First Southwest believes the MOA's unreserved fund balance of 10.0% for fiscal year 2010 could appropriately be described as "...somewhat below average" – for an entity in either rating category.

Rating agencies have long held that a credit rating is a composite of quantitative factors (e.g. financial ratios) and qualitative characteristics, such as strength of management. Local government ratings are based on the following four credit factors:

- Economic Strength,
- Financial Strength,
- Management & Governance, and
- Debt Profile.

In determining a rating, the rating agencies compare the MOA to other issuers with similar characteristics. The importance of these so-called "peer comparisons" in the credit rating process has risen as the rating agencies face increased scrutiny over the appropriateness and accuracy of their ratings. But while the rating agencies have published reports acknowledging the importance of such peer analysis, it has avoided stating what financial and debt ratio levels correspond to specific rating categories.

The fact that the MOA's ratings were affirmed earlier this year is evidence that its' "below average" reserve level is not – in and of itself – a ratings driver. However, the level of importance of such balances in the ratings process may increase if the MOA begins to experience weakness in other credit areas and the balances are projected to be insufficient to offset these declines should the downward trend continue.

Thus, to protect the MOA's high investment grade ratings, FirstSouthwest would advocate a change in the MOA's reserve policy such that its ratios would be more in line with those of its peers.

I hope this adequately responds to your request. Please do not hesitate to contact me if you have any questions or require any additional information.

Sincerely yours,

Steven J. Kantor

Steven J. Kantor
Managing Director