



# Fund Balance

## Definition

When an entity collects more money than it spends within a year, it has *retained earnings*. Retained earnings, in its simplest form, is cash. However, by definition, it is the amount by which assets are greater than liabilities.

Different industries sometimes use other names for retained earnings, such as: equity, capital, surplus, accumulated earnings, rainy day fund, etc.

In governmental accounting, we have specific names for retained earnings as well, depending on fund type. In governmental funds, like the general fund and capital projects fund, retained earnings is called *fund balance*. In proprietary funds, like the water fund and sewer fund, retained earnings is called *net position*. However, when we are referring to retained earnings in a government entity, it is appropriate to use the term *fund balance* as a catch-all term for all fund types.

## Purpose

The accumulation of funds in the general fund are restricted to the following purposes:

- a. Financing expenditures from the beginning of the period until general property taxes, sales taxes, and other revenues are collected.
- b. Providing a reserve to meet emergency expenditures.
- c. Covering unanticipated deficits for future years.

## Classifications

The general fund has five classifications (included as line-items under fund balance on your balance sheet in your financial report) that further delineate the use of fund balance. These include:

- a. Unassigned
  - a. Only used for the general fund, these amounts cannot be classified by any other classification.
- b. Assigned
  - a. Amounts intended to be used for specific purposes, but don't meet the criteria of committed or restricted.
- c. Committed
  - a. Amounts spent for purposes determined by ordinance or resolution.
- d. Restricted

- a. Amounts spent for purposes stipulated in the constitution, external providers, or legislation.
- e. Nonspendable
  - a. Amounts that cannot be spent because they are in a nonspendable form, like inventories or prepaids (i.e. insurance); or
  - b. Legally or contractually required to remain intact (i.e. property acquired for resale).

## Limits

Local governments may accumulate retained earnings in any fund. However, the State Legislature has set limits on how much retained earnings (fund balance) may be retained in the general fund of a local government. These limits vary depending on the entity type. **Note that these fund balance limits are applied to the sum of the unassigned, assigned, and committed fund balance classifications.** They do not include the restricted or nonspendable fund balance classifications. All other funds may accumulate retained earnings without limits. Additionally, Utah Code procedures are established for correcting excess and negative fund balances, as well as balance transfers.

General fund balance limits ensure governments do not collect more taxes than necessary, but still allow for the prudent accumulation of rainy day funds. The fundamental principle underlying these limits is that governments should generally tax citizens on a “pay as you go” basis. This means that purchases and services which benefit current taxpayers should not be made with funds accumulated from prior taxpayers. Conversely, governments should not issue excessive debt, which places the burden on future taxpayers to provide current benefits.