



ALEDO ISD BOARD MEETING TEMPLATE

MEETING DATE: October 20, 2014

AGENDA ITEM: Fund Balance Policy Report

PRESENTER: Earl Husfeld

ALIGNS TO BOARD GOAL(S): Financial/Facilities – The District shall exhibit excellence in financial and facility planning, management, and stewardship.

BACKGROUND INFORMATION:

- During the budget development process the past three years, much discussion has been held regarding the use of General Operating Fund Balance and the appropriate amount of General Operating Fund Balance the District should strive to maintain.

ADMINISTRATIVE CONSIDERATIONS:

- For many years, the Aledo ISD has been committed to sound financial management through prudent stewardship, integrity, planning, accountability, and open communication.
- The purpose of these guiding principles is to enable the District to achieve and maintain a stable long-term financial condition and provide guidelines for the day-to-day planning and operations of the District's financial affairs.
- These principles/guidelines are exemplified by the District's bond rating, School FIRST rating, FAST rating, and consistent tax rate for seven years.
- With the on-going school finance litigation, legislative "philosophy" against higher wealth school districts, and significant projected enrollment growth, increasing pressures will be placed on the District's financial practices.
- In conjunction with BOSC, Inc., the District's financial advisory firm, the following memorandum was prepared for your review, discussion, and consideration as we develop a General Operating Fund Balance policy for the District.

FISCAL NOTE:

None

ADMINISTRATIVE RECOMMENDATION:

None – Informational Report



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September 29, 2014

Mr. Earl Husfeld
Chief Financial Officer
Aledo Independent School District
1008 Bailey Ranch Road
Aledo, Texas 76008

Re: Aledo Independent School District – General Operating Fund Balance Considerations

Dear Earl:

Introduction

This letter is to review certain financial and operating considerations that we thought may be helpful as Aledo Independent School District (the “District”) reviews and considers the appropriate level of General Operating Fund Balance for the District, including the creation and ratification of a General Operating Fund Balance policy.

Why Maintain a General Operating Fund Balance

The District’s General Operating Fund Balance is designed to provide ongoing fiscal independence to meet its annual expenditures during normal times and times of crisis. It is important to emphasize the District’s fund balance does not equal the sum of its “cash and investments” as the District’s property taxes receivable, accounts receivable, due from other funds and inventories are also included within the definition of “General Operating Fund Balance”. In particular, a General Operating Fund Balance:

- Provides cash management flexibility as the District’s revenues and expenditures are not received/incurred in equal monthly amounts throughout the fiscal year;
- Allows the District to consistently meet the educational requirements of its community in the event lower revenues (i.e. tax collections are reduced/delayed, State funding is reduced/delayed, etc.) or higher expenditures (i.e. gas price increases, utility prices increases, etc.) are experienced in a fiscal year;
- Allows the District to meet its operating expenditures in the event of an unanticipated emergency, natural disaster, etc.;
- Serves as an ongoing tax rate/budget management tool –This is especially important for Aledo ISD as it is currently at the maximum M&O tax rate cap and is afforded limited flexibility to increase annual revenues to meet future operational expenditures (i.e. teacher salaries, additional teaching positions, etc.); and it
- Is a stated “Best Practice” of the Texas Education Agency, Government Finance Officers Association, Texas Association of School Business Officials and the bond rating agencies to maintain an adequate fund balance.

What is an Appropriate Amount of General Operating Fund Balance

In general, an “Unrestricted General Operating Fund Balance” equal to 3-4 months of operating expenditures is deemed financially appropriate. However, a higher fund balance is recommended for “fast growth school districts”, property wealthy districts and school districts that are at the maximum M&O or I&S tax rate or have highly concentrated tax bases. In our opinion, given these factors we recommend the District maintain an “Unrestricted General Operating Fund Balance” equal at least 27.5% of annual operating expenditures and a “Restricted General Operating Fund Balance” equal to at least 7.50% of annual operating expenditures – Which collectively totals a fund balance equal to 35% of annual expenditures.

Potential Consequences of Not Maintaining an Adequate General Operating Fund Balance

While not all-inclusive, the following is a summary of potential ramifications associated with school districts that have spent down their General Operating Fund Balance below acceptable guidelines:

- Need to annually borrow funds to meet operating cash flow – Increasing a district’s operating costs;
- Bond rating is “downgraded” – Increasing borrowing cost for future bond sales. A 0.15% interest rate difference on a \$61.5 million bond sale changes the District’s interest cost by approximately \$1,925,000;
- The flexibility to capitalize on new opportunities is diminished;
- Ability to re-establish an adequate fund balance is very difficult under the current State funding system as additional revenue sources are limited. Replenishing fund balance is also much more painful than the alternative of deciding not to spend down fund balance in previous years; and
- Although not relevant based upon current market conditions, a lower fund balance will result in lower investment earnings for operating expenses.

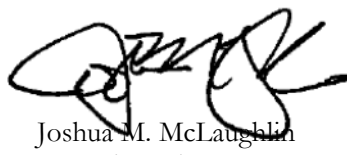
Closing

We hope this material is helpful as Aledo ISD contemplates the appropriate level of General Operating Fund Balance within the District. Should any questions arise, additional information is preferred or we may be of any assistance to the District, please do not hesitate to let us know. Hope all is well and hang in there!

Sincerely,



William J. Gumbert
Managing Director



Joshua M. McLaughlin
Managing Director