



City and Borough of Sitka

100 Lincoln Street • Sitka, Alaska 99835

MEMORANDUM

To: Mayor Hunter and Assembly Members
Keith Brady, Municipal Administrator

From: Jay Sweeney, Chief Finance and Administrative Officer

Date: October 17, 2017

Subject: Approve Re-appropriation (Roll-over) of Encumbered Balances as of June 30, 2017

Issue:

Per Section 11.12 of the Home Rule Charter (SHRC), appropriations for encumbered funds as of the end of the fiscal year do not lapse. To accomplish this Charter provision, a re-appropriation of encumbered funds in the new fiscal year is required. Such re-appropriation has historically occurred each year once fiscal year-end accounting has been finalized.

Facts:

1. Per the SHRC Section 11.12, encumbered appropriations do not lapse at the end of the fiscal year:

"Every unencumbered surplus of the general fund or a service area shall lapse at the close of the fiscal year to the general fund or service area, respectively. An appropriation for a capital improvement shall not lapse until its purpose has been accomplished or abandoned."
2. An encumbrance is a legally binding commitment by the Municipality for a purchase which has yet to be finalized by receipt of the good or service which has been ordered. Encumbered funds are normally documented by either a purchase order or a contract.
3. Under governmental accounting rules and guidelines, an expenditure is recorded in the fiscal year in which the expenditure transaction is completed, not the year in which the purchase commitment is made. Thus, purchase commitments made in a prior year (encumbrances) which are finalized in a later year (expenditures) will be recorded in the year of the expenditure.

4. The accounting system that the Municipality utilizes, New World Systems, during the soft close process, automatically created FY2018 budget adjustments for all encumbrances recorded in prior fiscal years, thus increasing the overall FY2018 expense budget to account for commitments (via purchase order or contract) made in prior years. All operating expenditures are measured against the current operating year's budget.
5. In the Municipality's Comprehensive Annual Financial report (Section F, Required Supplementary Information), expenditures during the fiscal year are reported against approved budgets for that fiscal year.

Discussion:

1. The SHRC, by setting forth the policy that unencumbered surpluses lapse at the end of the fiscal year, implies that encumbered funds do not lapse.
2. The Municipality has historically extended the interpretation on non-lapsing of encumbered funds to all funds, including enterprise funds, even though the Charter does not specifically mention them.
3. The manner in which the Municipality's accounting system, New World Systems, operates automatically adjusts the current fiscal year during the year-end close process, thus changing the current year's budget from the one approved by the assembly. For this reason, the Municipality has historically passed a supplemental budget ordinance to re-appropriate all encumbered fund at the end of each fiscal year. Even though it is not technically a re-appropriation (as the old appropriation does not lapse, per the Charter, for encumbered funds), a re-appropriation is the most efficient method to accomplish the guidelines of the Charter.
4. The re-appropriation of encumbered funds will have the effect of increasing the budgeted deficit for the fiscal year, as the expenditure budget will increase but there will be no matching revenue increase.
5. The amount of the encumbered funds was subtracted from the available amount of funds to be transferred to the Public Infrastructure Sinking Fund when that calculation was made; thus, the available cash to pay for the appropriations resides in the General Fund.
6. The similar Ordinance passed last year to re-appropriate encumbered funds was Ordinance 2016-33.

Analysis of Alternatives (Pros and Cons):

1. Approval of the re-appropriation ordinance has the following pros:

- a. The guidelines set forth in the Charter concerning encumbered funds are effectively carried out.
 - b. There is no adverse effect on the balance of the General Fund and other funds involved, as cash to pay for the encumbrances is contained in fund balances.
2. Non-approval of the re-appropriation ordinance would have the following pro and con:
- a. If the ordinance was not passed, the prior purchase commitments (many of which have already been executed since July 1) would squarely fall against this fiscal year's unadjusted budgets. Departments have planned for re-appropriation of encumbered funds to take place in the same fashion as prior years; changing the methodology would leave many with unanticipated budget shortfalls in key expenditure areas.
 - b. A possible pro is that non-approval of the ordinance would enact a type of forced expenditure reduction. While it would be a possible expenditure reduction (a possible pro), it would at the same time be unplanned and unevenly implemented, obvious cons.

Recommendation:

Administration recommends that Ordinance 2017-35 be approved by the Assembly.