

Revenue Estimating Conference

Fund Balance Uses and Potential Implications

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Historical Context

- The City of New Orleans, LA (the “City”) is preparing to issue approximately \$200M in public improvement bonds in or around the third quarter of 2024
- As part of the bond issuance process, the outstanding credit ratings from Fitch (A, stable outlook), Moody’s (A2, stable outlook), and Standard and Poor’s (A+, stable outlook) will be reassessed
- All of the rating agencies cite ample fund balance as a credit positive and budget gaps, imbalanced operations, and/or use of fund balance as credit negatives

Fund Balance

- Fund balance is the difference between assets and liabilities (net position) of governmental funds
 - Portions of fund balance may be held in assets other than cash (some assets may not be liquid)
 - Provides working capital for use during the year
 - Provides excess funds on hand in case of unexpected events (e.g. revenue shortfalls, etc.)
- Should generally not be used to support recurring expenditures
 - i.e. to pay for an increase in operating expenditures or to cover a decrease in recurring revenues
- GFOA recommends a formal fund balance policy be established at a minimum of two months of general fund revenues/expenditures
 - Some governments may require fund balance levels significantly higher

Fund/Cash Balances and Credit Ratings

- Credit Ratings are one of the primary drivers in the cost of borrowing
- Rating agencies heavily weight fund balance and cash balance ratios as a component of the quantitative rating process – ranging from 25% - 35%
- The rating agencies are heavily focused on this particular area

S&P's "Downside Scenario" for the City-

"If the city cannot maintain structural balance without federal stimulus funds, or if our view of the city's financial management practices weakens, we could lower the rating" -September 15, 2022

Moody's "Factors that could lead to a downgrade of the ratings" for the City –

"Structurally imbalanced operations driving a deterioration in reserves; Growth in fixed costs that lead to structural imbalance" -September 12, 2022

Fitch's "Factors that could, individually or collectively, lead to negative rating action/downgrade"

"Recurring failure to address future budget gaps that erodes the current satisfactory gapclosing capacity...; An increase in carrying costs that restricts the city's expenditure flexibility..." - September 15, 2022

Use of Fund Balance

- The City has received its full allocation of American Rescue Plan Act (“ARPA”) funds
- As of May 2024, the general fund balance levels and the current amount appropriated is as follows:

Fund	FY 2023 Unaudited Ending Balance (\$000s)	FY 2023 Grant Related Receivables ¹	FY 2024 Appropriations (\$000s)	FY 2024 Estimated Ending Balance (\$000s)	Percent of Balance Used
Committed	7,297	-	-	7,297	0%
Nonspendable	-	-	-	-	0%
Restricted	133,041	-	-	133,041	0%
Unassigned	186,257	57,707	92,270	36,280	81%
Total	326,595	57,707	92,270	176,618	

¹Grant related receivables are considered reductions in cash until or unless written off or collected

Potential Implications of Using Fund Balance

- Use of fund balance reduces the cash position of the City and erodes availability of working capital (cash used for current operating expenditures, i.e. salaries, vendor payments, etc.)
 - General Fund expenditures typically exceed revenues in the first few months of each year until major revenue sources are received
 - During the first three months of 2024, expenditures exceeded revenues by approximately \$72MM resulting in a use of fund balance held in cash
- Although occasionally using fund balance is not necessarily a credit negative, the speed and amount of the use of fund balance may be cause for concern for the rating agencies
- A downgrade in credit ratings would increase borrowing costs to the City

Mitigation of Concerns

- There are several possible steps the City can take to mitigate the concerns including:
 - establishing or formally codifying and adhering to the minimum level of fund balance
 - refraining from further use of fund balance until FY 2024 financial results are known, and ensuring future uses align with minimum targets
 - delaying, reducing, or canceling approved projects that draw on fund balance, or identify other funding sources
 - ensure the adoption of a structurally balanced budget in FY 2025 and beyond
 - exploring increasing revenue through charges for services or taxes that generate additional revenue
 - decreasing ongoing expenditures by reducing or eliminating services

Questions?