

## VIII—18.00 – Policy on Unrestricted Fund Balances

(Approved by the Board of Regents April 20, 2018)

### I. Purpose

This policy establishes processes for the use of unrestricted fund balances by University System of Maryland institutions. The policy also includes provisions for developing plans to eliminate accumulated deficits in unrestricted fund balances associated with state-supported activities, and addresses parameters for annual reporting to the General Assembly relating to changes in unrestricted fund balances and plans for their use.

Unrestricted fund balances are accounted for and their use managed by each institution of the University System of Maryland. The only constraints on an institution's ability to use unrestricted fund balances are the fund balance goal set annually regarding the use or increase in unrestricted fund balances, and required approvals of the Board of Regents, Chancellor and Board of Public Works, as appropriate.

The University System of Maryland facilitates access to funding by encouraging institutions and their units and departments to accumulate resources needed for future spending needs, initiatives and opportunities. The accumulation of resources ensures that funds are available for institutional departmental needs when required, and provides a source of liquidity and surety to holders of University System of Maryland debt. University System of Maryland financial planning strives to ensure that unrestricted fund balances are maintained at a level appropriate and proportionate to other public universities and colleges in the same credit rating category over time. A single fiscal year where the System reports a decline in unrestricted fund balances, by itself, should not be the basis for significant and dramatic changes in the System's financial plan other than the short-term and temporary measures such as curtailing new authorizations of cash-funded projects or initiatives.

This policy provides guidance and establishes a process for institutions' use of accumulated resources within a planning and control structure that enables the Chancellor and staff to have up to date information on commitments, claims and likely obligations that need to be considered in evaluating spending proposals outside of planning parameters, such as expectations that institutions manage their resources to ensure a particular change in unrestricted fund balances.

### II. Definitions

- (1) **Fund balances** – the difference between assets, deferred outflows, and liabilities and deferred inflows. Also referred to as net position or reserves.
- (2) **Unrestricted fund balances** – the difference between assets not subject to external (external to both the institution and System) stipulations that govern or control how resources are expended, and associated liabilities.
- (3) **State-supported fund balances** – under state of Maryland budgetary practices, unspent resources derived from state-supported activities such as teaching and instructional activities
- (4) **Available funds** – as reported in the most recent audited financial statements, the sum of:
  - (a) University System of Maryland Unrestricted Fund Balances

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- (b) Unrestricted Fund Balances of component units (affiliated foundations) of USM and its institutions
  - (c) Accrued leave liability
  - (d) Pension obligation including deferred outflows and deferred inflows associated with pension accounting
- (5) **Adjusted available funds** – available funds reported in the most recent audited financial statements, adjusted for unspent commitments and likely obligations.
  - (6) **Debt outstanding** – the sum of debt outstanding and obligations under lease agreements as reported in the most recent audited financial statements for the University System of Maryland and its component units (affiliated foundations).
  - (7) **Unfunded capital projects approved for debt funding** – the total, as of a particular date, of unspent capital projects authorizations approved for funding with USM debt proceeds in excess of bond proceeds on hand.
  - (8) **Adjusted debt outstanding** – debt and lease obligations reported on the Balance Sheet of the most recent audited financial statements, adjusted for additional debt to be issued to provide cash for unfunded capital projects approved for debt funding.
  - (9) **Commitments** – spending needs, initiatives, or opportunities approved by the Board of Regents or Chancellor, as required, considered to be spending outside of annual fund balance change goals. Commitments include temporary uses of cash balances pending receipt of gift or other funds scheduled for transfer to the System or its institutions at some point in the future.
  - (10) **Likely obligations** - amounts anticipated to be required to fund spending needs, initiatives, or other activities that have not yet been formalized, but are judged to be highly likely.
  - (11) **Adjusted ratio of available funds to adjusted debt outstanding** – the result of dividing adjusted available funds by adjusted debt outstanding

### III. Process for Use of Unrestricted Fund Balances

The University System of Maryland considers new spending needs, initiatives, and opportunities in the context of both System-wide financial capacity and institutional financial capacity. System-wide financial capacity is the ability to fund a specific spending need or objective without reducing the adjusted ratio of available funds to adjusted debt outstanding below a target ratio minimum, as determined annually in advance of the capital budget process.

This policy does not exempt institutions from spending approval requirements otherwise imposed by the Board of Public Works, or Board of Regents Policy.

Assessment of whether or not an institution satisfies the fund balance change goal will be based on the change in unrestricted fund balance reported on Balance Sheet of the audited financial statements for that institution.

The reported change in unrestricted fund balances will be adjusted for spending and donor collections associated with permanent and temporary uses of fund balances that result from the following:

- (1) Cash spending on capital projects approved as part of the Capital Improvement Plan / System-funded Construction Program approval, or

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- (2) Cash spending for capital projects or other spending initiatives greater than \$1 million and less than \$5 million approved by the Chancellor or designee, or
- (3) Cash spending for capital projects or other spending initiatives \$5 million or greater approved by the Board of Regents, or
- (4) Collections of pledged amounts of donor funding that support the temporary use of fund balances for a Board of Regents or Chancellor approved project or initiative, or
- (5) Cash use in arrangements agreed to (or imposed by the state) as part of a budget reduction outside of the normal budget approval cycle.

The status of spending of cash on capital projects or other spending initiatives that are outside of the fund balance goal assessment are to be surveyed as of June 30 and December 31 annually, so that a current and updated status of spending can be used in conjunction with audited year-end financial statements or mid-year internal financial statements for financial planning purposes.

Institutions can request that the Board of Regent review any decision by the Chancellor or designee rejecting a spending proposal request at its next regularly scheduled meeting.

#### **IV. Fund balance change goals**

Annually, in advance of the annual capital budget workshop, a goal for the expected change in unrestricted fund balances for the fiscal year for which the operating budget has not yet been submitted to the state government (simply, the goal will set for the fiscal year that begins in more than 12 months). The goal will be formalized as a percentage increase as a function of total unrestricted operating budget spending appropriation. Institutions have full responsibility for deciding how and through what operations or transactions the expected change in fund balance is to be achieved, and institutional actual results will be compared with the goal annually and reported to the Board of Regents.

Spending on cash-funded capital or other projects where the fund source is unrestricted fund balances, transactions with the state government involving transfers of fund balance back to the state in lieu of reductions in annual base appropriations, one-time uses of fund balances determined as a response to mid-year budget reductions, and other transactions imposed on institutions such as the change in the pension liability, all are to be excluded from the assessment of actual results in determining whether or not an institution met the fund balance goal. Other transactions may be excluded subject to agreement between the universities and the University System Office on a case by case basis.

Institutions with accumulated and uncommitted unrestricted fund balances beyond the institution's benchmark level of unrestricted fund balances may request the use of the unrestricted fund balance to pay for a project or initiative's spending needs by forwarding a request to the Chancellor and Vice Chancellor for Administration and Finance, or the Board of Regents, as spending approval requirements dictate. Institutions can formally communicate intentions to spend unrestricted fund balances on a specific major initiative or project in advance of receiving formal Board of Regents approval, to ensure that System-wide financial planning and Board of Regents decisions do not obligate an institution's accumulated funds for another institution's funding needs.

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The benchmark level of unrestricted fund balances is the institutions' unrestricted fund balance as reported at June 30, 2017, increased by each succeeding fiscal years final, adjusted fund balance goal, and reduced by spending on Board or System Office approved capital project spending and other spending agreed to be outside of the fund balance goal (for example, transfers of state-supported fund balances back to the state government as part of a mid-year budget reduction action). The calculation of the benchmark level of unrestricted fund balances, as well as any amounts beyond the benchmark level as adjusted for actual results year by year, will take into consideration unspent authorizations and any formally communicated intentions to spend not reflected in the most recent audited financial statements.

### **V. State-supported accumulated deficit elimination plans**

Institutions may from time to time manage state-supported operations in a fashion that operating budget fund balances attributable to those activities have negative fund balances, or an accumulated deficit. Negative state-supported operating budget negative fund balances or accumulated deficits may arise due to institutional decisions, or alternatively be an outcome of System-wide or Statewide decisions.

In circumstances where an institution reports an accumulated deficit in state-supported operating budget funds at June 30, the institution will be required to submit a plan to the Chancellor, due no later than December 31, for eliminating the accumulated deficit over time. The plan will identify the cause(s) for the accumulated deficit, describe remediation measures and efforts put in place by the institution to address the cause, and provide a timetable for addressing the cause and elimination of the accumulated deficit.

### **VI. Reporting Requirements**

Each year, no later than December 30 for the previous fiscal year, the USM will provide state general assembly budget committees on:

- The financial health of the System based on the financial metrics and standards contained in the Board of Regents Policy VIII-15 Policy on Debt Management for available resources to debt outstanding, and debt service as a percentage of operating revenues and state appropriations
- The amounts transferred to and expended from the plant fund and the fund balance by each institution during the prior fiscal year along with a brief description of the major projects supported with those funds during the year and planned for future years; and
- Progress in eliminating negative State-supported fund balances at institutions.