Revenue and Appropriation Deficits

Field visits with municipal finance officials have revealed several misconceptions about what constitutes a budget "deficit." Oftentimes, the term is used when projected revenues fail to meet anticipated expenditures at the start of the budget process. However, because municipal budgets must be in balance, this shortfall or gap should be closed before the start of the fiscal year. Once the tax rate is set, appropriation and revenue deficits arise through the course of the fiscal year and must be addressed before the following year's tax rate can be approved.

An "appropriation deficit" is described as:

The excess of expenditures at any point during a fiscal year over the legally authorized amount approved by the local appropriating authority for the same period.

With three spending exceptions (i.e., for court judgments, snow and ice costs and overlay), or in case of an emergency that threatens public health or safety, a city or town department may not over expend its appropriation under M.G.L. c. 44, §31. Unless corrected, or covered, prior to year-end through the transfer or appropriation of unexpended reserves, all appropriation deficits must be raised on the Tax Rate Recapitulation Sheet (Recap Sheet) for the ensuing fiscal year. Illegal appropriation deficits are also a negative hit to free cash, which creates a double penalty.

A "revenue deficit" is defined as:

The amount by which actual revenues at year-end fall short of projected revenues and are insufficient to cover actual expenditures (not including appropriation deficits).

A revenue deficit must also be raised on the Recap Sheet for the following year, but unlike an appropriation deficit, it will not affect a community's free cash calculation.

It is useful to remember that in determining revenue deficits, municipalities are allowed to regard the current year's net real and personal property taxes as 100 percent collectible. This effectively narrows the source of a revenue deficit to the state aid or local receipts categories. For more information including common questions, answers and examples, see the DLS on-line publication Revenue Deficits.

In the instance of both deficit types, monitoring expenditure and revenue trends during the year can help identify potential problems. Oftentimes, an appropriation deficit can be corrected during the fiscal year. To address an anticipated revenue deficit usually requires a corresponding mid-year spending reduction. However, a revenue deficit is not fully quantified until after the fiscal year is closed and a balance sheet is prepared.

There are methods of avoiding and/or remedying deficits

- Town accountants and city auditors should monitor revenues and departmental expenditures throughout the course of the fiscal year. Trends in actual revenue compared to projections and actual expenditures compared to appropriations should foreshadow the threat of a deficit.

- Under M.G.L. c. 41, §56, the accountant or auditor should disallow any payment request from a department when the appropriation balance in the line-item to be charged is insufficient to cover the invoice amount. This method is exercised through the warrant process and will prevent appropriations deficits if performed timely.

- A town meeting or the city council may approve mid-year line-item transfers, or appropriate from reserve balances. In each case, the request would originate with the executive branch.

- Under M.G.L. c. 44, §33B, a city council, or a board of selectmen with concurrence from the finance committee, may transfer appropriations between line items provided that:

    Appropriations are not taken from the school department or municipal light plant;

    The transaction is approved during the last 2 months of the fiscal year or the first 15 days of the ensuing fiscal year; and

    Transfers are limited to 3% of the total appropriation from which the transfer is being made or $5,000, whichever is higher.

Under M.G.L. c. 40, §5A & M.G.L. c. 40, §6, the city council or town finance committee may vote to transfer from the reserve fund an amount to fund extraordinary or unforeseen expenses.