

KENSINGTON POLICE PROTECTION AND COMMUNITY SERVICES DISTRICT

****Revised AGENDA****

A Special Meeting of the Finance Committee of the Kensington Police Protection and Community Services District will be held **Thursday April 28, at 6: 00 P.M.**, at the Community Center, 59 Arlington Avenue, Kensington, California.

1. **Call to Order/Roll Call 6:00 P.M.**
2. **Public Comments-** Members of the public may address the Committee on any issue not listed on the agenda that are within the purview of the Committee. Comments on matters that are listed on the agenda may be made at the time the Committee is considering each item. Each speaker is allowed a maximum of five (5) minutes per Board Policy 5030.41.
3. **Approval of the Finance Committee Minutes.**
 - a. Minutes of the Finance Committee Special Meeting of April 6, 2016. Page 2
4. The Committee will receive a report regarding the draft Independent Auditor's Financial Report ending Fiscal year June 30, 2015. The Committee will review and possibly vote to recommend the Kensington Police Protection and Community Services Board of Directors approve the report. P-8
5. The Committee will review and consider recommending approval to the Board of Directors the Fiscal Year 2016/17 proposed budget. The Kensington Police Protection and Community Services District Board of Directors will review and possibly vote to approve the proposed budget for FY 16/17 at its Regular Meeting held on May 12, 2016. P-43
6. The Finance Committee will receive a report from the sub-committee on the development of a Budget Reserve Policy. The Committee may take action to vote on recommendations from the sub-committee to the Board of Directors.

ADJOURNMENT

General Information-Accessible Public Meetings

NOTE: UPON REQUEST THE KENSINGTON POLICE PROTECTION AND COMMUNITY SERVICES DISTRICT WILL PROVIDE WRITTEN AGENDA MATERIALS IN APPROPRIATE ALTERNATIVE FORMATS, OR DISABILITY-RELATED MODIFICATION OR DISABILITIES TO PARTICIPATE IN PUBLIC MEETINGS. PLEASE SEND A WRITTEN REQUEST, INCLUDING YOUR NAME, MAILING ADDRESS, PHONE NUMBER AND A BRIEF DESCRIPTION OF THE REQUESTED MATERIALS AND PREFERRED ALTERNATIVE FORMAT OR AUXILIARY AID OR SERVICE AT LEAST 2 DAYS BEFORE THE MEETING. REQUESTS SHOULD BE SENT TO:

Interim General Manager Kevin. E. Hart, Kensington Police Protection & Community Services District, 217 Arlington Ave, Kensington, CA 94707. POSTED: Public Safety Building-Colusa Food-Library-Arlington Kiosk- and at www.kensingtoncalifornia.org.

Complete agenda packets are available at the Public Safety Building and the Library.

All public records that relate to an open session item of a meeting of the Kensington Police Protection & Community Services District that are distributed to a majority of the Board less than 72 hours before the meeting, excluding records that are exempt from disclosure pursuant to the California Public Records Act, will be available for inspection at the **District offices, 217 Arlington Ave, Kensington, CA 94707** at the same time that those records are distributed or made available to a majority of the Board.

To: Chairman Welsh, Co-Chairman Toombs, and IGM/COP Hart

From: Paula Black, Rob Firmin, Karl Kruger, Gloria Morrison, and Jim Watt

Date: April 19, 2016

Subject: KPPCSD Budget Reserves Policy

Background

At the Finance Committee meeting on February 1, 2016, Committee members discussed the need to formulate a reserve policy for possible adoption by the Board. To commence the process the Finance Committee unanimously agreed to appoint a 5-member subcommittee to provide recommendations for review by the full Finance Committee. The five-subcommittee members are: Black, Firmin, Kruger, Morrison and Watt.

Methodology

In addition to an exchange of e-mail information on the subject, the subcommittee had two meetings to discuss the appropriate course of action and the areas that should be included as part of an over-arching reserve policy. The subcommittee unanimously agreed that a reserve policy should include not only specifying the reserves necessary to meet day-to-day cash flow needs and unforeseen contingencies, but also major capital reserves necessary to fulfill the District's obligations for the Kensington Community Center and capital improvements for other District owned and operated buildings.

We looked at reserve policies in other communities, and found significant variations by community. Therefore, we concluded that any final decision by Kensington has to fit its own unique circumstances. Those circumstances include the fact that Kensington has a fairly stable revenue base and that the daily cash flow needs can be met with somewhat minimal reserves. Subcommittee members felt it was imperative that we adopt a systematic approach to building up our reserves to complete necessary capital improvements.

The attachments identified as "Source Material" were beneficial in formulating our recommendations.

Recommendations

That the following three funds be established by Board resolution.

General Fund Unallocated reserve – That the District maintain a contingency reserve for operating expenditures of no less than \$500,000 or 16% of total annual revenues, whichever is greater, in order to maintain the sound financial operation of the District. This reserve may only be utilized in the event of a severe economic downturn or a natural

disaster and only after all reasonable expenditure cuts have been implemented, as determined by final Board approval.

Community Center Building Upgrade - That the category currently designated in the Budget under the heading Fund Balances as "Committed – Park Bldgs. Replacement" be redesigned as "Community Center Upgrade". That the funds currently shown as \$206,976 be augmented by an additional \$150,000 in FYE 16/17 and an additional \$150,000 in FYE 17/18. The purpose of these additional "Committed" funds shall be to set aside sufficient capital to meet the possible capital required to retrofit the building. Upon completion of these Community Center improvements, any surplus funds shall be assigned to the newly created General Capital Building Fund – see following.

General Capital Building Fund – That this new capital building fund be created with the purpose of setting aside annual restricted funds for the purpose of completing necessary capital improvements to District owned and operated facilities. The initial amount to be included in this fund shall be based upon 4% of the annual revenues from the County levy tax (code 401), and shall commence with budget year 16/17. The initial 4% may be increased, but not decreased, at the time each annual budget is approved. The money in this account may only be used for major capital building improvement with an expected useful life of 15 or more years.

The following would be the recommended changes to the line items shown under Fund Balances – see attached complete page from the budget.

Fund balances, in audit terms (see definitions included)

Nonspendable – District Portion of Bond	
Restricted – Est'd vacation/comp liability	
Committed – Park Bldgs Replacement	DELETED
Committed – Community Center Bldg Upgrade	ADDED
Committed - Annex Renovation Expenditure	DELETED
Committed – General Capital Bldg. Fund	ADDED
Committed – Bay view Net Balance	

Total Identified Fund Balances

Conclusion

This proposed recommended reserves policy has been thoroughly vetted by the sub-committee, with concessions made by all members in the interest of providing the full committee with a recommended policy that has the unanimous approval of the sub-committee.

KPPGSD
Projected Revenue and Expense
2015/2016

ATTACHMENT

Budgeted Revenues 2015/2016	
400 · Police Activities Revenue	
Total 400 · Police Activities Revenue	\$2,791,952
Total 420 · Park/Rec Activities Revenue	71,500
440 · District Activities Revenue	
448 · Franchise Fees	48,800
456 · Interest-District	0
Total 440 · District Activities Revenue	<u>48,800</u>
Total Revenues	\$2,912,252
Budgeted Expenditures 2015/2016	
500 · Police Sal & Ben	
Total 500 · Police Sal & Ben	\$2,053,670
Total 550 · Other Police Expenses	325,268
Total 600 · Park/Rec Sal & Ben	31,147
Total 635 · Park/Recreation Expenses	96,716
Total 800 · District Expenses	271,119
Total 950 · Capital Outlay	<u>81,000</u>
Total Expenditures	<u>\$2,858,920</u>
Excess of Revenue over Expense 2015/2016	\$53,332
Previously Allocated Funds	
Total Allocated Funds Used	0
Excess Funding over Expenses 2015/2016	<u>53,332</u>
Cash Carryovers 2014/2015	<u>\$1,480,663</u>
Estimated Fund Carryovers into 2015/2016	\$1,533,994
Fund Balances, in audit terms (see definitions included)	
Nonspendable - District Portion of Bond	\$92,830
Restricted - Est'd Vacation/Comp Liab	80,000
Committed - Park Bldgs Replacement less FY 15/16 expenditures	206,976
Committed - Annex Renovation Expenditure in Current Year	0
Committed - Bay View Net Balance	<u>-7,977</u>
Total Identified Fund Balances	\$371,829
Unassigned Fund Balance available for Contingencies	\$1,162,165
Percentage of Total Expenditures	40.65%



Reserve Levels Developing a Policy Framework

- The adequacy of fund balance should be assessed based on an agency's own specific circumstance – there is no universally accepted "right level"
 - **Revenue Source Stability:** How stable is the District's tax base in the face of adverse economic conditions? How broad are the District's revenue sources? Are any revenue sources at risk due to State or Federal actions?
 - **Expenditure Volatility:** What are the District's contractual obligations and how much will they mandate ongoing expenditure levels? Are there new programmatic areas that the District will undertake?
 - **Extreme Circumstances:** What is the risk of natural disaster or other one-time outlay (i.e., earthquake, fire, etc.)? How much (if any) of this risk can be insured against?
 - **Liquidity:** What are the District's cash flow needs (i.e., when are property tax revenues received relative to when expenses are incurred)? How have reserves fluctuated in the past and what is the general trend?
 - **Leverage:** What are the City's unfunded liabilities and ongoing capital needs? Pension? OPEB?

SOURCE MATERIAL PMG Analysis



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Appropriate Level of Unrestricted Fund Balance in the General Fund

Type: Best Practice

Approved by GFOA's Executive Board: September 2015

Background:

In the context of financial reporting, the term *fund balance* is used to describe the net position of governmental funds calculated in accordance with generally accepted accounting principles (GAAP). Budget professionals commonly use this same term to describe the net position of governmental funds calculated on a government's budgetary basis.¹ While in both cases *fund balance* is intended to serve as a measure of the financial resources available in a governmental fund; it is essential that differences between GAAP *fund balance* and budgetary *fund balance* be fully appreciated.

1. GAAP financial statements report up to five separate categories of fund balance based on the type and source of constraints placed on how resources can be spent (presented in descending order from most constraining to least constraining): *nonspendable fund balance*, *restricted fund balance*, *committed fund balance*, *assigned fund balance*, and *unassigned fund balance*.² The total of the amounts in these last three categories (where the only constraint on spending, if any, is imposed by the government itself) is termed *unrestricted fund balance*. In contrast, budgetary fund balance, while it is subject to the same constraints on spending as GAAP fund balance, typically represents simply the total amount accumulated from prior years at a point in time.
2. The calculation of GAAP fund balance and budgetary fund balance sometimes is complicated by the use of sub-funds within the general fund. In such cases, GAAP fund balance includes amounts from all of the subfunds, whereas budgetary fund balance typically does not.
3. Often the timing of the recognition of revenues and expenditures is different for purposes of GAAP financial reporting and budgeting. For example, encumbrances arising from purchase orders often are recognized as expenditures for budgetary purposes, but never for the preparation of GAAP financial statements.

The effect of these and other differences on the amounts reported as GAAP *fund balance* and budgetary *fund balance* in the general fund should be clarified, understood, and documented.

It is essential that governments maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. In most cases, discussions of fund balance will properly focus on a government's general fund. Nonetheless, financial resources available in other funds should also be considered in assessing the adequacy of unrestricted fund balance in the general fund.

Recommendation:

GFOA recommends that governments establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund for GAAP and budgetary purposes.³ Such a guideline should be set by the appropriate policy body and articulate a framework and process for how the government would increase or decrease the level of unrestricted fund balance over a specific time period.⁴ In particular, governments should provide broad guidance in the policy for how resources will be directed to replenish fund balance should the balance fall below the level prescribed.

Appropriate Level. The adequacy of unrestricted fund balance in the general fund should take into account each government's own unique circumstances. For example, governments that may be vulnerable to natural disasters, more dependent on a volatile revenue source, or potentially subject to cuts in state aid and/or federal grants may need to maintain a higher level in the unrestricted fund balance. Articulating these risks in a fund balance policy makes it easier to explain to stakeholders the rationale for a seemingly higher than normal level of fund balance that protects taxpayers and employees from unexpected changes in financial condition. Nevertheless, GFOA recommends, at a minimum, that general-purpose governments, regardless of size, maintain unrestricted budgetary fund balance in their general fund of no less than two months of regular general fund operating revenues or regular general fund operating expenditures.⁵ The choice of revenues or expenditures as a basis of comparison may be dictated by what is more predictable in a government's particular circumstances.⁶ Furthermore, a government's particular situation often may require a level of unrestricted fund balance in the general fund significantly in excess of this recommended minimum level. In any case, such measures should be applied within the context of long-term forecasting, thereby avoiding the risk of placing too much emphasis upon the level of unrestricted fund balance in the general fund at any one time. In establishing a policy governing the level of unrestricted fund balance in the general fund, a government should consider a variety of factors, including:

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Appropriate Level of Unrestricted Fund Balance in the General Fund | Government Finance Officers Association

1. The predictability of its revenues and the volatility of its expenditures (i.e., higher levels of unrestricted fund balance may be needed if significant revenue sources are subject to unpredictable fluctuations or if operating expenditures are highly volatile);
2. Its perceived exposure to significant one-time outlays (e.g., disasters, immediate capital needs, state budget cuts);
3. The potential drain upon general fund resources from other funds, as well as, the availability of resources in other funds;
4. The potential impact on the entity's bond ratings and the corresponding increased cost of borrowed funds;
5. Commitments and assignments (i.e., governments may wish to maintain higher levels of unrestricted fund balance to compensate for any portion of unrestricted fund balance already committed or assigned by the government for a specific purpose). Governments may deem it appropriate to exclude from consideration resources that have been committed or assigned to some other purpose and focus on unassigned fund balance, rather than on unrestricted fund balance.

Use and Replenishment.

The fund balance policy should define conditions warranting its use, and if a fund balance falls below the government's policy level, a solid plan to replenish it. In that context, the fund balance policy should:

1. Define the time period within which and contingencies for which fund balances will be used;
2. Describe how the government's expenditure and/or revenue levels will be adjusted to match any new economic realities that are behind the use of fund balance as a financing bridge;
3. Describe the time period over which the components of fund balance will be replenished and the means by which they will be replenished.

Generally, governments should seek to replenish their fund balances within one to three years of use. Specifically, factors influencing the replenishment time horizon include:

1. The budgetary reasons behind the fund balance targets;
2. Recovering from an extreme event;
3. Political continuity;
4. Financial planning time horizons;
5. Long-term forecasts and economic conditions;
6. External financing expectations.

Revenue sources that would typically be looked to for replenishment of a fund balance include nonrecurring revenues, budget surpluses, and excess resources in other funds (if legally permissible and there is a defensible rationale). Year-end surpluses are an appropriate source for replenishing fund balance.

Unrestricted Fund Balance Above Formal Policy Requirement. In some cases, governments can find themselves in a position with an amount of unrestricted fund balance in the general fund over their formal policy reserve requirement even after taking into account potential financial risks in the foreseeable future. Amounts over the formal policy may reflect a structural trend, in which case governments should consider a policy as to how this would be addressed. Additionally, an education or communication strategy, or at a minimum, explanation of large changes in fund balance is encouraged. In all cases, use of those funds should be prohibited as a funding source for ongoing recurring expenditures.

Committee: Accounting, Auditing, and Financial Reporting
Governmental Budgeting and Fiscal Policy

Notes:

1. For the sake of clarity, this recommended practice uses the terms GAAP fund balance and budgetary fund balance to distinguish these two different uses of the same term.
2. These categories are set forth in Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*.
3. Sometimes restricted fund balance includes resources available to finance items that typically would require the use of unrestricted fund balance (e.g., a contingency reserve). In that case, such amounts should be included as part of unrestricted fund balance for purposes of analysis.
4. See Recommended Practice 4.1 of the National Advisory Council on State and Local Budgeting governments on the need to "maintain a prudent level of financial resources to protect against reducing service levels or raising taxes and fees because of temporary revenue shortfalls or unpredicted one-time expenditures" (Recommended Practice 4.1).
5. In practice, a level of unrestricted fund balance significantly lower than the recommended minimum may be appropriate for states and America's largest governments (e.g., cities, counties, and school districts) because they often are in a better position to predict contingencies (for the same reason that an insurance company can more readily predict the number of accidents for a pool of 500,000 drivers than for a pool of fifty), and because their revenues and expenditures often are more diversified and thus potentially less subject to volatility.
6. In either case, unusual items that would distort trends (e.g., one-time revenues and expenditures) should be excluded, whereas recurring transfers should be included. Once the decision has been made to compare unrestricted fund balance to either revenues and/or expenditures, that decision should be followed consistently from period to period.

Download Best Practice

SOURCE MATERIAL

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Unassigned fund balance is typically the primary subject of a reserve policy. However, committed and assigned fund balance may also be thought of as part of a reserve policy as the governing board or management, respectively, has some control over the balances. Conversely, restricted fund balances or nonspendable fund balances are fundamentally constrained, making it unnecessary to place parameters on them through reserve policy in order to achieve prudent savings and expenditures of public resources.

It is recommended that every district establish policies regarding minimum fund balance and spending priorities in order to communicate to users the importance of a reserve for economic uncertainties, why it consists of amounts that are unassigned and that it is not available for spending.

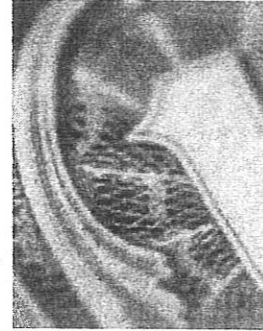
Districts' policies should specify the order in which fund balances are spent when more than one amount is available for a specific purpose. Where such policies do not exist, GASB 54 prescribes that the default order in which these amounts should be spent is committed, assigned, and then unassigned.



GASB 54

According to the Governmental Accounting Standards Board, statement No. 54 was issued after, "...research revealed that the existing standards guiding fund balance reporting were being interpreted inconsistently by different governments. Consequently, the fund balance information reported by many governments also was inconsistent. It also became clear that the understandability of fund balance information was affected and that financial statement users were unable to readily interpret reported fund balance information."

GASB fact sheet about Fund Balance Reporting and Governmental Fund Type Definitions



Sample Policy Language

The "X" district maintains a minimum unassigned fund balance of not less than "X" percent of budgeted general fund expenditures and other financing uses as a reserve for economic uncertainties. The district believes a reserve of this level is prudent to maintain a high bond rating and to protect the district from the effects of fluctuations in property tax revenues to which special districts are vulnerable. Because amounts in the nonspendable, restricted, committed and assigned categories are subject to varying constraints on their use, the reserve for economic uncertainties consists of balances that are otherwise unassigned.