

MENLO PARK FIRE PROTECTION DISTRICT

FUND BALANCE RESERVE POLICY

1.0 PURPOSE

This policy outlines the Menlo Park Fire Protection District's ("District") strategy for building and maintaining healthy reserve levels across various District funds. Adequate reserves are essential to mitigate current and future risks, ensuring the District's long-term financial stability. Maintaining appropriate reserves is a key component in keeping the District's overall financial health stable. To retain a stable financial base, the District must maintain sufficient balances to fund all operating cash flows of the District, provide financial reserves for the replacement of capital assets, aid in reducing financial impacts for unanticipated expenditures and/or revenue shortfalls due to unfavorable economic conditions or emergencies, address the increasing pension costs, and ensure sufficient funds for other operating and capital needs.

2.0 SCOPE

The District's reporting and communication relating to fund balance reserves will utilize the classifications outlined in generally accepted accounting principles (GAAP). The District will maintain reserves of fund balances, as defined herein, in accordance with Governmental Accounting and Financial Standards Board Statement No. 54 (GASB 54), Fund Balance Reporting, and Governmental Fund Type Definitions. This policy will ensure that the District maintains adequate fund balances and reserves in order to:

- a) Ensure sufficient funding to support short-term and long-term operating financial obligations.
- b) Limit adverse annual and multi-year budgetary impacts from anticipated and unanticipated expenditures or revenue shortfalls.
- c) Secure internal financing of future capital improvement projects and replacement of existing fixed assets.
- d) Mitigate the impacts of increasing retirement contributions.
- e) Build and maintain financial resiliency.

This policy and the procedures promulgated under it supersede all previous regulations regarding the District's fund balance and reserve policies. This policy shall apply to all District governmental funds.

3.0 DISTRICT FUNDS

The District's finances are accounted for within the following four major funds:

- **General Fund** - The general fund is the main operating fund of the District. It is used to record all financial resources of the District except those required to be accounted for in another fund.

- **Capital Improvement Projects Fund (CIP)** - The CIP fund is used for the acquisition, renovation, or complete rebuild of the District's fire stations and other facilities.
- **Special Revenue Fund** - The special revenue fund is used to account separately for funds received and disbursed for federal emergencies. This fund includes federal grant activities from the Federal Emergency Management Agency's (FEMA) cooperative agreements for the District's California Task Force 3 (CATF3) Urban Search and Rescue (US&R) and other emergency responses.
- **Debt Service Fund** - the debt service fund is used to account for the accumulation of resources and payments made for the principal and interest on long-term debt.

4.0 FUND BALANCE CLASSIFICATIONS

Fund balance is essentially the difference between the assets and liabilities reported in a governmental fund. Statement GASB 54 requires local governments to focus on the constraints imposed upon resources when reporting fund balance in government funds. The five fund balance classifications of non-spendable, restricted, committed, assigned, and unassigned indicate the level of constraints placed upon resources and identify specific purposes for which resources in a fund can be spent.

The District's Fund Balances are classified as follows:

- **Non-spendable** - consists of assets that cannot be spent because they are not in spendable forms, such as prepaid items and inventories, and items that are legally or contractually required to be maintained intact, such as the principal of an endowment or revolving loan fund. The District has one non-spendable fund balance:
 - **Prepaid Assets:** This reserve represents resources that have been paid to another entity in advance of the accounting period in which the resource is deducted from the fund balance. An example is the prepaid purchase of a fire apparatus or other fixed assets.
- **Restricted** - consists of amounts that are subject to externally enforceable legal restrictions. This includes externally imposed restrictions by creditors, such as through debt covenants, grantors, contributors, laws or regulations of other governments, as well as restrictions imposed by law through constitutional provisions or enabling legislation.
 - **Debt Service:** The debt service reserve is established to guarantee the availability of funds required to fulfill the debt requirements as mandated by debt covenants. This reserve is set aside to ensure timely payments of debt service obligations.
- **Committed** - consists of amounts that are subject to a purpose constraint imposed by a

formal action of the government's highest level of decision-making authority and remain binding unless the constraint is removed in the same manner.

- **Budgetary Deficit:** The budgetary deficit reserve is established to set up reserves to address financial impacts resulting from changes in the economic environment. If revenues are insufficient to meet the normal operating requirements of essential services in times of economic downturn, this fund may be used.
- **Capital Asset Replacement:** The capital asset replacement reserve is established to fund the replacement of various capital assets, including but not limited to the following:
 - a. Fire trucks, engines, and other vehicles
 - b. Safety devices
 - c. Communication radios
 - d. Emergency medical equipment
 - e. Information technology equipment

The reserve is to ensure the timely replacement of capital assets should they come to the end of their useful life or become obsolete or inoperable. The timing of the replacement varies and depends on the criteria set by the District. Since replacing capital assets often comes at a large cost, maintaining sufficient reserve funds ensures adequate resources are available without adverse budgetary impacts.

- **Capital Improvement Projects:** The capital improvement projects reserve is established to fund the improvement, expansion, or replacement of fire stations and administration facilities to meet future demand and maintain and/or improve the District's existing level of service. The District has a vital CIP program and is continually keeping stable reserve funding to support the projects needed due to the aging of facilities, growth, and development in its jurisdictions.
- **Assigned** - consists of the portion of net fund resources reflecting the government's intended use of resources. Assignment of resources can be done by the highest level of decision-making or by a committee or official designated for that purpose. The District's assigned fund balances include the following:
 - **Encumbrances:** Encumbrances are materials or services ordered but not received before the end of the fiscal year. These consist of open purchase orders at the end of the fiscal year that will roll over to the new fiscal year. As such, a reserve for encumbrances is necessary to provide funding requirements for the approved expenditures.
 - **Pension Stabilization:** The pension stabilization reserve is established to

mitigate the impact of changes in employer contributions to the California Public Employees' Retirement System (CalPERS) which includes normal cost and unfunded accrued liability (UAL). This fund can be used to pay down the unfunded pension liabilities.

- **Workers' Compensation:** The workers' compensation fund is established to provide a reserve for payment of workers' compensation claims as the District is self-insured for claims up to the first \$1,000,000.
- **Compensated Absences:** The compensated absences fund is established for payment of current and terminated employees' accrued annual leave and compensatory time off.
- **Unassigned** - represents any portion of the fund balances or the residual positive net resources that do not fall into one of the above categories. The general fund is the only fund that reports a positive unassigned fund balance amount. In other funds, it is not appropriate to report a positive unassigned fund balance. In funds other than the general fund, where expenditures incurred for specific purposes exceed the amounts that are restricted, committed, or assigned to those purposes, it may be necessary to report a negative unassigned fund balance in that fund.

The Unassigned fund balance is maintained to provide for contingencies to mitigate financial and service delivery risk due to unexpected revenue shortfalls or unanticipated expenditures. This can be used for activities that the District deems appropriate and beneficial to operations. The use of unassigned fund balance is based on availability and need. However, the purpose of this reserve is to provide budgetary stabilization and not serve as an alternate funding source for new programs and ongoing operating expenditures.

5.0 RESERVE FUNDING POLICY

The Fund Balance Policy establishes target reserve levels for the following fund balances:

Category	Target Reserve Level
Nonspendable	
Prepaid Assets	The amount is determined by the prepaid transactions in a given fiscal year.
Restricted	
Debt Service	The amount is determined by debt covenant requirements.
Committed	
Budgetary Deficit	The target balance will be a minimum of 15% and a maximum of 30% of the general fund operating expenditure budget.
Capital Asset Replacement	The reserve will be funded by annual appropriation in the amount of the yearly straight-line accumulated depreciation from existing capital assets until it reaches a sufficient amount to cover the cost of replacing the District’s entire fleet and capital equipment.
Capital Improvement Projects	The funding for this reserve will be based on current and future capital improvement needs. At a minimum, the reserve will be funded by annual appropriation in the amount of the yearly straight-line accumulated depreciation from existing facilities. Since capital project needs are long-term and will constantly change, there is no recommended maximum reserve level.
Assigned	
Encumbrances	The amount set aside will be the remaining balance of the outstanding purchase orders at the end of a given fiscal year.
Pension Stabilization	The reserve balance will be equal to 20% of the annual required UAL amortization amount.
Workers’ Compensation	The amount is determined by the three-year average of workers’ compensation claims.
Compensated Absences	The amount is determined by the three-year average of the annual leave cash-out expenditures.
Unassigned	
Unassigned	Residual balance. No target reserve level.

6.0 PROCEDURES

Use of Reserves

When both restricted and unrestricted funds are available for expenditures, restricted funds should be spent first unless legal requirements disallow it. Committed and assigned fund balances are available for use when purchases or disbursements are specific to the fund balance classifications. The assigned fund balance requires approval from the Board of Directors ("Board") to use. On the other hand, the committed fund balance can be used through authorization from the Fire Chief or designated staff.

Allocation of Reserves

Final reserve balances will be calculated at the end of each fiscal year after the closing of the District's accounting records. Staff will present to the Board for approval the recommended allocation of funds in various reserve classifications resulting from the surplus realized from actual revenues exceeding expenditures. The reserve balances will be maintained as outlined in this policy. The Board may also approve any reallocation of funds, transfers among reserve funds, or action that is inconsistent with this policy at any given time.

Replenishment of Reserves

If any balance established in this policy falls below the minimum required level, the District shall strive to restore it to the minimum required balance within one to three years of use by any feasible means, including, but not limited to, adopting a budgetary surplus, applying cost savings, seeking other sources of revenues, and reallocating reserve balances.

Policy Review

This policy shall be reviewed annually as part of the year-end financial reporting process. It will be the responsibility of the Finance Manager to keep this policy current and up-to-date.

Adopted: September 20, 2022

Amended: June 11, 2024