

Introduction

The County of Orange Reserves Policy, Phase I, is intended to inventory the existing reserves available to the General Fund and to guide the creation, maintenance and use of reserves. It is intended to provide flexibility to the County in dealing with future planned capital expense needs, unanticipated or cyclical economic conditions, emergencies, catastrophes, temporary cash flow shortages, unexpected large one-time expenses, opportunities to use funds to produce future ongoing savings and some level of protection against statutory changes to County revenues.

Phase I of the reserves policy project covers reserves and reserve-type funds available to the County General Fund. Phase II will cover non-general funds and departmental (program-restricted) reserves.

Examples of recent events demonstrating the need for reserves include the Governor's original FY 04-05 proposed budget that would have caused an on-going \$62 million reduction of the County's general purpose revenues. This was subsequently reduced to a reduction of \$27.7 million per year for two years. In addition the State passed on a share of the Federal child support system penalty (\$4 million per year for two years), deferred reimbursement of mandated cost claims and FY 03-04 Vehicle License fees were reduced by \$26.5 million; scheduled to be repaid by the State in August 2006.

This policy includes both formal and informal reserves. It includes provisions for reserves as reported on Schedule 3 of the County Budget Book compiled by the Auditor-Controller, appropriated reserve-type funds and reserve-type funds held by the Orange County Employees Retirement System (OCERS). A summary schedule of the reserve balances, additions, uses and target amounts is attached.

Provisions for Reserves

These are formal reserves as reported on Schedule 3 of the Auditor-Controller Budget Book. There is currently one Reserve for Contingencies and a Strategic Priority Reserve (also labeled Reserve for Operations (Strategic Plan)) with two parts (one for specific capital improvements and one unallocated).

Reserve for Contingencies: This reserve was established through the Strategic Financial Plan process. It is normally modified at the time of adopting the budget (Government Code Section 29085). Changes to reserve amounts at other times require a 4/5 vote of the Board of Supervisors. A 4/5 vote is also required to make such reserves available for appropriation to expend these funds if needed during the fiscal year (Government Code Section 29130). The purpose and use of this reserve is to cover unanticipated and severe economic downturns, major emergencies or catastrophes that cannot be covered with existing appropriations. The target amount for

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Phase I: Reserves Available to the General Fund

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this reserve is up to 10% of ongoing annual General Purpose Revenues (excludes fund balance available and one-time amounts and transfers) or \$41,300,000. The 10% compares to Government Finance Officers Association (GFOA) guidelines of 5 to 10% and to surrounding counties that use targets from 5% to 15%. The current balance is \$18,000,000 and will be increased by \$5,000,000 to \$23,000,000 when consolidated with the Provision of Contingencies. The balance will be \$18,300,000 below target. Future Strategic Financial Plans may recommend changes to this reserve within the target amounts as funds become available.

Strategic Priority Reserve—Capital Improvements: This reserve was established through the Strategic Financial Plan process. It is normally modified at the time of adopting the budget. Changes to reserve amounts at other times require a 4/5 vote of the Board of Supervisors. A 4/5 vote is also required to make such reserves available for appropriation to expend these funds if needed during the fiscal year (Government Code Section 29130). The purpose and use of this reserve is currently for specific items shown on the detail sheet. In some cases, the amounts represent “down payments” on the capital improvements and will need to be augmented by other funds. Funds would be withdrawn from this reserve and appropriated in the fiscal year in which the projects are expected to be encumbered or expended. The current balance is \$23,536,004. Future Strategic Financial Plans may recommend changes to the projects and/or amounts of this reserve.

Strategic Priority Reserve—Unallocated: This reserve was established through the Strategic Financial Plan process and built up with periodic additions of unanticipated General Fund Balance available at the close of prior fiscal years. It is normally modified at the time of adopting the budget. Changes to reserve amounts at other times require a 4/5 vote of the Board of Supervisors. A 4/5 vote is also required to make such reserves available for appropriation to expend these funds if needed during the fiscal year (Government Code Section 29130). The purpose and use of this reserve is to provide flexibility to the County in dealing with future planned capital expense needs, unanticipated or cyclical economic conditions, emergencies catastrophes, unexpected large one-time expenses and opportunities and some level of protection against statutory changes to County revenues. The current balance is \$37,051,155 after the reduction of \$27,730,861 for the FY 04-05 local government revenue shift to the state. This revenue shift will occur again in the same amount in FY 05-06 further reducing the balance to \$9,320,294. Future Strategic Financial Plans may recommend changes to this reserve as funds are needed or become available.

Appropriated Reserve-type Funds

These are informal reserve amounts annually appropriated in the budget. There are currently four of these: Vacancy Factor & Miscellaneous Reserve, Provision for Contingencies, Debt Prepayment Fund and Designated Special Revenue Fund.

Vacancy Factor & Miscellaneous Reserve: This appropriation is contained in the 004 Miscellaneous Budget within the County General Fund. It was first established in the FY 99-00 budget when the CEO implemented a salary & wages budget policy based on historical vacancy factors. The purpose and use of this reserve is to provide additional appropriations to a general fund department should its actual vacancy factor fall below the budgeted vacancy factor for most of the fiscal year and the department has insufficient appropriations to make it to the end of the fiscal year. It may also be used for significant unanticipated emergencies, catastrophes, one-time expenses and opportunities. A 4/5 Board of Supervisors vote would be required if these funds are transferred outside the general fund. The current balance is \$5,000,000. If a portion of the reserve is used during any fiscal year the full \$5,000,000 is re-budgeted the following fiscal year. Future Strategic Financial Plans may recommend changes to the current balance as funds are needed or become available.

Provision for Contingencies (Agency Code 099): This appropriation is allowed by Government Code Section 29084 and based on this code it may not exceed 15% of the total appropriations from the General Fund. This appropriation has been budgeted for decades in various amounts. Government Code Section 29126 allows the Board to transfer unneeded appropriations into this account during the year. Government Code Section 29130 requires a 4/5 vote to use these appropriations elsewhere in the budget during the year. The purpose and use of this reserve is as the appropriated companion component of the Reserve for Contingencies (see above) and beginning FY 05-06 will be combined with the existing Reserve for Contingencies.

Debt Prepayment Fund (14V): This fund was established through the Strategic Financial Plan process during FY 99-00. The purpose and use of this reserve is to reduce the County's amount of debt and realize corresponding savings in principle and interest payments. The County's debt defeasance plan will be presented to the Board in the near future. A 4/5 Board of Supervisors vote would be required if these funds are transferred out of this fund. The current balance is \$116,180,924. The target amount for this reserve is \$122,625,000 or an amount sufficient to call the first set of 1995 Recovery Bonds. The current balance is \$6,444,076 below target. Future Strategic Financial Plans and the Debt Defeasance Plan may recommend changes to this fund as funds are needed or become available.

Designated Special Revenue Fund (15S): This fund was established in FY 96-97 and is now governed through the Strategic Financial Plan process. The purpose and use of this fund is to cover temporary cash flow shortages in other County funds as authorized

annually by the Board and to fund strategic priorities identified in the Strategic Financial Plan. These priorities currently include deferred maintenance, projects to remedy Americans with Disabilities Act (ADA) infrastructure deficiencies and partial funding for a new regional animal care facility. The June 30, 2005 balance will be \$19,554,717. Future Strategic Financial Plans may recommend changes to these projects and amounts as new priorities are identified and funds are needed or become available.

Reserve-type Funds held by OCERS

Currently there is a reserve held by the Orange County Retirement System on behalf of the County. This reserve is called the Retirement Investment Account.

Retirement Investment Account: This account was established with the proceeds of the 1994 Pension Obligation Bonds. The purpose and use of this account includes the offset of County retirement expenses and reducing the County's share of the retirement system unfunded liability. The balance of this account as of December 31, 2004 was \$155,245,123. A portion of retirement system earnings are credited to this account. The FY 04-05 budget plans on using \$7,754,142 (a portion of the current year estimated interest earnings) of this account to offset FY 04-05 retirement expenses. Future debt defeasance strategy and Strategic Financial Plans may recommend changes to the use of this account. Use of this account to offset the County's retirement expenses may free up existing or future general fund resources for other purposes.

Future Reserve Consolidation

There are several reserve and reserve-type funds and accounts that could be consolidated to reduce the number of accounts and simplify the reserve structure. At this time, the CEO recommends the following change be incorporated into the FY 2005-06 recommended budget. The change is illustrated in the second attached worksheet:

- Combine the Provision for Contingencies with the Reserve for Contingencies

Phase II

Phase II of the County's Reserves Policy will cover non-general funds and departmental (program-restricted) reserves. Due to the fact that Phase II will include over 65 individual funds or accounts, it will be completed in about 12 months. Quarterly Budget Reports will include status updates of the Phase II project.

SD: reserves policy 4-12-05

Reserve for Contingencies

Fund/Agency Number	100
Authority	Government Code Section 29085
When established	Budget Adoption
Budgeted	Schedule 3 of the County Budget
Board approval required	4/5 vote to change amount during the year or to appropriate and make available for use during the year (Government Code Section 29130)
Purpose	Unanticipated and severe economic downturns, major emergencies or catastrophes that cannot be covered with existing appropriations
Target	Up to 10% on ongoing annual General Purpose Revenues (excluding FBA, transfers & other one-time revenue) or currently \$36,300,000
Expiration Date	Ongoing
Current Balance	\$18,000,000 + \$5,000,000 will be \$23,000,000
Variance from target	\$18,300,000
Interest Earnings	Credited to general fund
Plan for reducing the variance	Combine with Provision for Contingencies reserve. Future Strategic Financial Plans may identify additional available funds.
Other Comments	

Strategic Priority Reserve—Capital Improvements

Fund/Agency Number	100
Authority	Adopted Strategic Financial Plan (SFP)
When established	June 20, 2004
Budgeted	Schedule 3 of the County Budget
Board approval required	4/5 vote to change amount during the year or to appropriate and make available for use during the year
Purpose	Specific items as shown below
Target	Projects identified in the SFP
Expiration Date	Project completion
Current Balance	\$23,536,004
Variance from target	N/A
Interest Earnings	Credited to the general fund
Plan for reducing the variance	N/A
Other Comments	

Reserve Account Detail

	6/30/2004 Balance	FY 04-05 Activity	FY 04-05 Balance	FY 05-06-07 Activity	6/30/2007 Balance
Child Support System Fed. Penalty	\$ 4,000,000	\$ 291,119	\$ 4,291,119	\$ (4,291,119)	\$ -
CAPS Upgrade	5,000,000		5,000,000	(5,000,000)	-
Assessment Tax System	9,200,000		9,200,000	(1,500,000)	7,700,000
Computer System	4,600,000		4,600,000	TBD	4,600,000
Los Pinos land acquisition	-	444,885	444,885	TBD	444,885
Other Capital Improvements	2,434,256	(2,434,256)	-		-
Total	\$ 25,234,256	\$ (1,698,252)	\$ 23,536,004	\$ (10,791,119)	\$ 12,744,885

Strategic Priority Reserve—Unallocated

Fund/Agency Number	100
Authority	Adopted Strategic Financial Plan (SFP)
When established	June 20, 2004
Budgeted	Schedule 3 of the County Budget
Board approval required	4/5 vote to change amount during the year or to appropriate and make available for use during the year
Purpose	Provide flexibility to the County in dealing with future planned capital expense needs, unanticipated or cyclical economic conditions, emergencies catastrophes, unexpected large one-time expenses and opportunities, and some level of protection against statutory changes to County revenues
Target	Driven by the SFP
Expiration Date	N/A
Current Balance	\$37,051,155 will be reduced to \$9,320,294 after the FY 05-06 revenue shift to the State
Variance from target	N/A
Interest Earnings	Credited to the general fund
Plan for reducing the variance	N/A
Other Comments	

Vacancy Factor & Miscellaneous Reserve

Fund/Agency Number	100-004
Authority	Board adoption of the Final Budget
When established	June 29, 2004
Budgeted	Yes
Board approval required	Majority vote to transfer appropriations within the General Fund. 4/5 vote to transfer out of the General Fund.
Purpose	Provide additional appropriations to a general fund department should its actual vacancy factor fall below the budgeted vacancy factor for most of the fiscal year and the department has insufficient appropriations to make it to the end of the fiscal year. May also be used for significant unanticipated emergencies, catastrophes, one-time expenses and opportunities.
Target	\$5,000,000
Expiration Date	Re-budgeted annually
Current Balance	\$5,000,000
Variance from target	\$ 0
Interest Earnings	Credited to the general fund
Plan for reducing the variance	N/A
Other Comments	

Provision for Contingencies

Fund/Agency Number	100-099
Authority	Government Code Sections 29084 & 29126
When established	Board adoption of the Final Budget
Budgeted	Yes
Board approval required	4/5 vote to use appropriations elsewhere in the budget during the fiscal year (GC 29130)
Purpose	Unanticipated and severe economic downturns, major emergencies or catastrophes that cannot be covered with existing appropriations
Target	\$5,000,000
Expiration Date	N/A
Current Balance	\$5,000,000
Variance from target	\$ 0
Interest Earnings	Credited to the general fund
Plan for reducing the variance	N/A
Other Comments	Recommended for consolidation into Reserve for Contingencies in the FY 05-06 Budget

Debt Prepayment Fund

Fund/Agency Number	14V
Authority	Board Adoption of the Final Budget
When established	June 29, 2004
Budgeted	Yes
Board approval required	4/5 vote to transfer funds out of 14V
Purpose	Reduce the County's amount of debt and realize corresponding savings in principle and interest payments
Target	\$122,625,000
Expiration Date	When debt is defeased
Current Balance	\$116,180,924
Variance from target	\$6,444,076
Interest Earnings	Credited to the general fund
Plan for reducing the variance	Debt reduction plan is in development
Other Comments	

Designated Special Revenue Fund

Fund/Agency Number	15S
Authority	Board Adoption of the Strategic Financial Plan (SFP)
When established	June 29, 2004
Budgeted	Yes
Board approval required	4/5 vote to transfer appropriations out of fund 15S
Purpose	To cover temporary cash flow shortages in various County funds as annually authorized by the Board. To fund strategic priorities as identified in the Strategic Financial Plan. See detail below.
Target	N/A
Expiration Date	N/A
Current Balance	\$19,554,717
Variance from target	N/A
Interest Earnings	Credited to the general fund
Plan for reducing the variance	N/A
Other Comments	

Account Detail

	6/30/2004 Balance	FY 04-05 Activity	FY 04-05 Balance	FY 05-06-07 Activity	6/30/2007 Balance
Relocate Animal Shelter	\$ 4,150,000	\$ (880,000)	\$ 3,270,000	\$ (3,270,000)	\$ -
Deferred Maintenance/ADA	13,320,000	(6,220,000)	7,100,000	(7,100,000)	-
Future Strategic Priorities	4,588,564	4,596,153	9,184,717	(9,184,717)	-
From Fund 13N - Loan Repayment			-	8,563,092	8,563,092
Total	<u>\$22,058,564</u>	<u>\$(2,503,847)</u>	<u>\$19,554,717</u>	<u>\$(10,991,625)</u>	<u>\$ 8,563,092</u>

Retirement Investment Account

Fund/Agency Number	Held by OCERS
Authority	Board agreement with OCERS
When established	1994
Budgeted	N/A
Board approval required	N/A
Purpose	Helps fund County retirement expenses and reduces the County's share of the retirement system unfunded liability
Target	N/A
Expiration Date	N/A
Current Balance	\$155,245,123 at December 31, 2004
Variance from target	N/A
Interest Earnings	Credited to this account
Plan for reducing the variance	N/A
Other Comments	Use of this account to offset the County's retirement expenses may free up existing or future general fund resources for other purposes.