



## **Reserves Policy**

### **Obligated Fund Balances and Reserves Available to the General Fund**

#### **Introduction**

The County of Orange General Fund Reserves Policy provides guidance in the creation, maintenance and use of reserves. The policy covers formal and informal reserves, and includes provisions for reserves such as appropriations for contingencies, reserve-like appropriations, and reserve-like funds held by others such as the OCERS Investment Account. The policy also recognizes whether funds are legally required or discretionary, or have special restrictions.

The importance of having and maintaining healthy reserve balances became evident during the Great Recession and more recently with the Novel Coronavirus (COVID-19) pandemic. Temporary utilization of fund balance or reserves aided departments in offsetting decreases in revenue growth, funding reductions from various sources, and accommodating increased costs of doing business.

The General Fund Reserves policy strategy is to provide flexibility to the County and offer:

- Resources to address unanticipated or cyclical economic conditions.
- Resources for emergencies and/or catastrophic events.
- Mitigation of the volatility of revenues and expenditures in managing temporary cash flow shortages.
- Capacity to cover unexpected large one-time expenses and opportunities.
- Capacity to fund capital investments.
- Capacity to minimize borrowing costs.
- Capacity to provide some level of protection against statutory changes to County revenues and impacts from Federal and State actions.

The County has a variety of reserve funds available to both the General Fund and Non-General Funds including:

- Fund Balance Assigned for Contingencies – This reserve was established through the Strategic Financial Plan process for the purpose and use of covering unanticipated and severe economic downturns, major emergencies, or catastrophes that cannot be covered with existing appropriations. The current target for this reserve is 15% of ongoing annual General Purpose Revenues.
- Fund Balance Assigned for Capital Projects – This reserve was established through the Strategic Financial Plan process for the purpose and use of funding future capital projects, including information technology projects. Funds are



withdrawn from this reserve and appropriated in the fiscal year in which the projects are expected to be encumbered or expended.

- Fund Balance Assigned for Maintenance and Construction – This reserve, established through the quarterly budget report process, is for the purpose and use of funding of future construction and maintenance projects. Appropriation of funds withdrawn from this reserve occurs in the fiscal year in which the projects are expected to be encumbered or expended.
- Fund Balance Assigned for Teeter Loss Reserve – On October 28, 2014, Board Resolution 14-096 established this reserve to maintain a balance not less than 25% of the total delinquent secured taxes and assessments for participating entities in the County as calculated by the Auditor-Controller at the end of each fiscal year. This reserve provides flexibility to cover losses that may occur if tax-defaulted property sells for less than the amount necessary to cover outstanding tax and assessment liens on that property. In addition, this reserve may be used to pay down note purchases or cash finance the Teeter plan in the future.
- Fund Balance Assigned for Budget Stabilization – This reserve, established through the quarterly budget report process, ensures prudent reserve levels that are maintained and replenished on a regular basis. The current year target, based on the GFOA's best practice, is set at two months (approximately 17%) of General Fund operating revenues as budgeted in FY 2020-21.
- Reserve-like Appropriations – These are informal reserve amounts annually appropriated in the budget such as the Miscellaneous Contingency Reserve and Annual Leave Payouts.
- Reserve-like Funds – The reserve held by the Orange County Employees Retirement System (OCERS) on behalf of the County and established with the proceeds of the 1994 Pension Obligation Bonds is an example of a reserve-like fund. 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. Use of this account to offset the County's retirement expenses may free up existing or future General Fund resources for other purposes.
- Department Type Reserves – These are restricted reserves set aside in non-General Funds for specific purposes. Department type reserves are limited to the purpose and use for which the non-General Fund was established.

All of the aforementioned are reserves customarily modified at the time of budget adoption (Government Code Section 29085) or at fiscal year-end (in accordance with GASB 54



requirements). Changes to reserve amounts at other times require a 4/5 vote of the Board of Supervisors in order to make such reserves available for appropriation to spend, if needed, during the fiscal year (Government Code Section 29130).

The County has provided for General Fund Obligated Fund Balances, developing specific targets for each reserve type based upon recommendations by the Government Finance Officers Association (GFOA) and best practices based upon review of reserve policies implemented by other local governments. The County’s policy follows GFOA’s current recommendation, which states that, “at a minimum, general-purpose governments, regardless of size, maintain unrestricted fund balance in their General Fund of no less than two months of regular General Fund operating revenues or regular General Fund operating expenditures.”

As part of the 2010 Strategic Financial Plan, the Board granted the County Executive Office approval to implement GFOA best practice for funding reserves and to continue reviewing the management of those reserve funds. Regular monitoring of reserves ensures effective control and consolidation of resources, if appropriate, while maintaining proper designations and flexibility. There is no request to change the existing reserve policy with this Strategic Financial Plan.

**Reserve Targets and Descriptions**

Under GFOA recommended practice, the County establishes an overall reserve target, and allocates the calculated target among the classes of obligated fund balances as appropriate. The County may fund more or less to each reserve class, for a variety of reasons such as current financial conditions, the need to set aside for particular goals or directives, the need to bridge one-time gaps, etc. The goal is to ensure regular maintenance and replenishment of a prudent reserve balance.

In implementing the GFOA’s best practice, the County elected to establish a funding target based upon two months of General Fund operating revenues to lessen current and future risks such as revenue shortfalls and unexpected expenditures. As such, the current year target is set at two months (approximately 17%) of General Fund operating revenues as budgeted in FY 2020-21 as follows:

General Fund Budgeted Revenues FY 2020-21	\$4,085,080,400
Less: Non-Operating Items	(432,696,357)
Less: One-Time Items – CARES Act	(473,266,267)
Net FY 2020-21 Operating Revenues	3,179,117,776
Target - 2 Months General Fund Operating Revenues	\$ 529,852,963



The following table summarizes the current reserves by classification. When compared to the overall target, total General Fund reserves are \$158,194,754 above target, but projected to fall to \$109,087,748 by the end of the current fiscal year due to planned use of reserves for capital projects and unplanned use of reserves in response to the COVID-19 pandemic. Moreover, due to strategic and prudent allocation of one-time funding and sources, the Budget Stabilization Reserve for FY 2020-21 is anticipated to meet the GFOA recommended target of \$529,852,963. Going forward, as General Fund budgeted revenues are expected to increase over the five years of the Plan, the goal is to increase the Budget Stabilization Reserve in each year to maintain the GFOA recommended target. Increases to maintain the target could be achieved by allocation of General Purpose Revenue growth, allocation of one-time funding and sources, re-allocation of specific-use reserve balances, or any combination of the three. The 2020 SFP assumes use of General Purpose Revenue growth each year to meet the target amount; however, the ability to achieve this will be determined during the FY 2021-22 Budget development process.

	<b>Balance at 6/30/2020</b>	<b>Projected Change</b>	<b>Projected Balance at 6/30/2021</b>
<b>Budget Stabilization Reserve</b>			
Reserve for Budget Stabilization [Goal = \$529.9M]	531,309,425	2,849,669	534,159,094
<b>Budget Stabilization Reserve Target</b>	<b>\$ 531,309,425</b>		<b>\$ 529,852,963</b>
Stabilization Reserve Over/(Under) Target	\$ -		\$ 4,306,131
<b>Specific-Use Reserve Classification</b>			
Assigned (9740)	\$ 2,849,669	\$ (2,849,669)	\$ -
Catastrophic Event Contingencies [Goal = 15% of GPR = \$131M]	65,000,000	(39,781,120)	25,218,880
Reserve for Capital and IT Projects	50,906,319	(5,817,830)	45,088,489
Reserve for Maintenance & Construction	9,438,766	(658,387)	8,780,379
Teeter Loss Reserve	30,000,000	-	30,000,000
<b>Subtotal - General Fund (GF) Specific-Use Reserves</b>	<b>\$ 158,194,754</b>	<b>\$ (49,107,006)</b>	<b>\$ 109,087,748</b>
<b>Grand Total - General Fund (GF) Total Reserves</b>	<b>\$ 689,504,179</b>	<b>\$ (46,257,337)</b>	<b>\$ 643,246,842</b>

An alternate approach used by some credit rating agencies is to evaluate the County's available fund balance as a ratio of the General Fund's assigned and unassigned fund balances (from the County's Comprehensive Annual Financial Report [CAFR]) as a percentage of total expenditures. A threshold of 15% of expenditures or greater is considered strong. On a Generally Accepted Accounting Principles (GAAP) basis, the County's percentage in FY 2018-19 was 12% of expenditures and the preliminary percentage for FY 2019-20 is 11%. The County prepays its pension contribution and reports the prepaid amount as Non-Spendable Fund Balance rather than Unassigned Fund Balance in the CAFR as required by Governmental Accounting Standards Board (GASB) Statement Number 54. However, if the prepaid costs for General Fund short



term Taxable Pension Obligation Bonds (POB) were to be considered as available, which they are, the percentages change to 24% and 25% for fiscal years 2018-19 and 2019-20 (preliminary), respectively. The following table demonstrates the available fund balance for FYs 2018-19 and 2019-20 (preliminary):

Amounts in thousands				
	2018-19 CAFR [1]	2018-19 CAFR [2]	2019-20 Prelim CAFR [1]	2019-20 Prelim CAFR [2]
Fund Balance				
Non-Spendable	396,541	1,995	460,074	1,488
Non-Spendable-POB		394,546		458,586
Restricted	49,989	49,989	78,982	78,982
Assigned	147,686	147,686	106,929	106,929
Unassigned	196,517	196,517	217,317	217,317
Total Fund Balances	790,733	790,733	863,302	863,302
General Fund Expenditures	3,297,168	3,297,168	3,517,729	3,517,729
Calculated %	12%	24%	11%	25%

[1] Fund balance amounts in CAFR are calculated by Auditor-Controller based on Generally Accepted Accounting Principles (GAAP)

[2] Calculated % assumes that the non-spendable fund balance associated with the County's short-term Taxable Pension Obligation Bonds (POB) is available to the General Fund.

**General Fund Obligated Fund Balances**

Obligated Fund Balances are formal reserves and currently include Fund Balance Assigned for Contingencies, Fund Balance Assigned for Operations, Fund Balance Assigned for Capital and IT Projects, Fund Balance Assigned for Maintenance and Construction, Fund Balance Assigned for Teeter Loss Reserve and Fund Balance Assigned for Budget Stabilization. The reserves defined in the following pages are General Fund Obligated Fund Balances that are neither restricted nor committed as defined by Governmental Accounting Standards Board (GASB) Fund Balance Reporting policy.



**Contingencies**

Target	15% of ongoing annual General Purpose Revenues (excluding FBA, transfers & other one-time revenue) or, currently, \$130,830,143
Projected Balance @ June 30, 2021	\$25,218,880 (2.9% of ongoing General Purpose Revenues)
Variance from target	\$105,611,263 below target

This compares to Government Finance Officers Association (GFOA) guidelines for funding contingencies at 15% or higher. A review of surrounding counties found contingency targets were set from 5% to 15%. The COVID-19 pandemic had a financial impact, which resulted in the County Fund Balance Unassigned (FBU) ending the year with a deficit of \$29,781,120 and necessitating a draw from contingency reserves to balance the General Fund for FY 2019-20. In addition, on December 15, 2020, the Board allocated \$10 million to small business economic support in response to the COVID-19 pandemic. As the economy recovers, replenishment of this reserve will be a priority to prepare for future catastrophic events.

Please see the following table for specific details of the contingency reserve:

<b>Contingencies</b>	
Fund 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)
Expiration Date	Ongoing
Interest Earnings	Credited to General Fund
Plan for reducing the variance	This Strategic Financial Plan recommends no change to this reserve.



**Assigned for Capital Projects**

Target	\$50,000,000
Projected Balance @ June 30, 2021	\$45,088,489
Variance from target	\$4,911,511 below target

Draws from the Capital Project reserve are anticipated in FY 2021-22; however, due to COVID-19 financial impacts, during the 2020 SFP development process the specific draws were unknown and will be determined through the budget development process.

The following table provides specific details of the capital projects reserve:

<b>Reserve for Capital Projects</b>	
Fund Number	100
Authority	Adopted Strategic Financial Plan (SFP)
When established	June 20, 2004
Budgeted	Schedule 4 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
Expiration Date	Upon completion of designated projects
Interest Earnings	Credited to the General Fund
Plan for reducing the variance	This Strategic Financial Plan recommends no change to this reserve.



**Assigned for Maintenance and Construction**

Projected Balance @ June 30, 2021	\$8,780,379
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The following table provides specific details of the maintenance and construction projects reserve:

<b>Reserve for Maintenance and Construction</b>	
Fund Number	100
Authority	Approved Quarterly Budget Report
When established	November 17, 2015
Budgeted	Schedule 4 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
Expiration Date	Upon completion of designated projects
Interest Earnings	Credited to the General Fund
Plan for reducing the variance	This Strategic Financial Plan recommends no change to this reserve.





**Assigned for Teeter Loss Reserve**

Target	Varies with fluctuations in delinquent secured taxes and assessments, but use could include the following: possible transfer back to Fund 656 in the event of an economic downturn; pay down notes; future cash financing of Teeter plan
Projected Balance @ June 30, 2021	\$30,000,000

The following table provides specific details of the Teeter Loss reserve:

<b>Assigned for Teeter Loss Reserve</b>	
Fund Number	100
Authority	Board Resolution No. 14-096 in accordance with R&T Code 4703.2
When established	October 28, 2014
Budgeted	Schedule 4 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
Expiration Date	N/A
Interest Earnings	Credited to the General Fund



**Assigned for Budget Stabilization Reserve**

Target	\$529,852,963
Projected Balance @ June 30, 2021	\$534,159,094
Variance from target	\$4,306,131 above target

Please see the following table for specific details of the Target reserve:

<b>Reserve for Budget Stabilization</b>	
Fund Number	100
Authority	Approved Quarterly Budget Report
When established	November 17, 2015
Budgeted	Schedule 4 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
Expiration Date	N/A
Interest Earnings	Credited to the General Fund
Plan for reducing the variance	This Strategic Financial Plan recommends no change to this reserve; however, additional contributions to the reserve will be recommended from General Purpose Revenue growth or fund balance and will be allocated through the Annual Budget adoption process and/or the Mid-Year Budget Report.



**Appropriated Reserve-type Funds**

**Miscellaneous Contingency Reserve & Annual Leave Payouts**

These appropriations are maintained in the Budget Control 004 Miscellaneous Fund budget within the County General Fund. The purpose and use of the appropriations is to provide additional appropriations to General Fund Departments through the end of the fiscal year for budgetary shortfalls, unanticipated one-time expenditures, emergencies, and opportunities. The appropriations are typically distributed during the mid-year budget report process and require a 4/5 Board of Supervisors vote for transfers of these funds per Government Code Section 29125(a)(2). The FY 2020-21 beginning balance is \$10,031,522 with an additional \$1,000,000 earmarked by the Board on November 23, 2010 to establish funding for unanticipated annual leave payouts impacting small departments (approximately 100 employees or less). Five to ten million dollars is typically budgeted each year. Future Strategic Financial Plans may recommend changes to the current balance as funds are needed or become available.

Please see the following specific details of the Miscellaneous contingency and Annual Leave Payouts appropriations:

<b>Miscellaneous Contingency Reserve &amp; Annual Leave Payouts</b>	
Fund/Budget Control Number	100-004
Authority	Board adoption of the Final Budget
Budgeted	Yes
Board approval required	4/5 Board of Supervisors vote to transfer funds
Target	\$10,000,000
Expiration Date	Re-budgeted annually
Interest Earnings	Credited to the General Fund



**Reserve Type Funds - OCERS Retirement Investment Account**

The balance of this account at June 30, 2020 was \$135,341,559. The assets held in the Investment Account are invested with the OCERS portfolio. As such, the balance in the account will change based on the performance of the investment assets and any draws from the account.

Projected Balance @ June 30, 2021	\$124,815,468 including projected net investment earnings/<losses> and draws
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Please see the following table for specific details of the OCERS Investment Account:

<b>Retirement Investment Account</b>	
Fund Number	Held by OCERS
Authority	Board agreement with OCERS
When established	1994
Interest Earnings	Credited to this account