

Definitions of Reserves and Fund Balances for the Unrestricted General Fund

9/13/2020

Reserves

Reserves are those funds set aside in the budget process for unanticipated needs as well as for working capital. For a college district, reserves are typically reviewed by external auditors, ACCJC and the State Chancellor's Office to determine that the district has sufficient reserves to be a "going concern." For a company to be a **going concern**, it must be able to continue operating long enough to carry out its commitments, obligations, objectives, and so on. In other words, the company will not have to liquidate or be forced out of business. For a college district, it needs to have sufficient resources to cover its obligations, etc., for at least the next 3-6 months. The state does not have a requirement for a minimum reserve, but recommends a minimum of 5%. Operating expenses means all unrestricted general fund expenditures less one-time expenditures and passthrough line items.

Fund Balance

The fund balance is the amount left in the fund at a specified point in time (inclusive of the reserve), usually calculated at fiscal yearend, which for community colleges is June 30. The fund balance may include funds that are committed, such as for a project that the Board has specifically authorized or a contract that has yet to be fulfilled; and funds that are unassigned that are available for any authorized use. These unassigned funds are usually the ones that make up a district's reserve.

A board usually sets a reserve percentage that must be set aside in the budgeting process. The calculation involves looking at the proposed budget, calculating that percentage of all expenditures and transfers and making sure that there are sufficient funds in the proposed ending balance to fund that amount.

For example

Proposed budget for 2020-2021	
Revenues	\$ 102,000,000
Expenses and transfers	100,000,000
Net change	2,000,000
Reserve balance 7/1/2020	\$ 10,000,000
Reserve balance 6/30/2021	\$ 12,000,000
Reserve percentage	12%

Reserves are to be used for unanticipated expenses or for an unanticipated loss in revenues. Permitted uses can include a change in the state formula resulting in a drop in revenue, either retroactively or in an amount too large to handle in one year, a natural disaster resulting in unforeseen expenses, a sudden failure in any infrastructure requiring immediate repair or replacement, and any other similar unforeseen difficulty. The board approval of the use of reserves should be accompanied by a plan to replenish the reserves over one or more years. The replenishment typically comes by either reducing spending in future year(s) or not spending new revenues received. The replenishment would be one of the highest priorities of the district, and the plan cannot be changed without board approval.

A sample board policy is:

Fund Balance Policy for the Unrestricted General Fund

Purpose:

To help the District weather unanticipated changes in revenues or expenses and provide for adequate cash flow. This policy establishes the appropriate level of reserves that the District will strive to maintain in its Unrestricted General Fund; how the fund balances will be funded and the conditions under which the fund balances can be used.

1. Amounts Held in Reserve

The District's unrestricted General Fund reserve shall be maintained at a prudent level, as defined in Board Policy 6305. The reserve funds are to be used to provide:

- Budget Stabilization Reserve for economic uncertainty as well as known or anticipated future obligations.
- Emergency Disaster Reserve for unforeseen events or catastrophic accidents.
- Working Capital to provide sufficient cash flow.

2. Funding Target Fund Balance

The target total fund balance for the District defined as the Board Designated Reserve (BP 6305) is a minimum of percentage of operating expenses net of one-time expenditures or passthroughs. Funding of this target will generally come from excess revenues over expenditures or one-time revenues. The reserve will be funded in the following priority order:

- Budget Stabilization
- Emergency Disaster
- Working Capital

Fund balance may also include additional reserves to cover other priorities. These reserve amounts may be for Total Cost of Ownership (TCO) for Facilities and IT, future anticipated increases in PERS and STRS, or other priorities. These allocations are in addition to the Designated Reserve target. These savings may also be used to offset impacts from unforeseen situations that affect the District budget.

Additionally, the fund balance may include savings amounts for all three sites that are in addition to the Designated Reserve target. These funds are to be used by the colleges and Central Services at their discretion; however, all three sites may be required to use their savings to offset impacts from unforeseen situations that affect the District and colleges' budgets. The goal is that addressing the impact of budget reductions would come first from each site's reserve, followed by other undesignated fund balances, and finally the board designated reserve funds.

3. Conditions for Use of Reserves

The use of reserves shall be limited to unanticipated, non-recurring needs, or anticipated future obligations. Fund balances shall not be used for normal or recurring annual operating expenditures without a plan to balance the budget and restore the reserves to minimum percentage of budget expenditures in future years. Per Board Policy 6305, the Chancellor and the Vice Chancellor of Fiscal Services shall recommend a plan to the Board of Trustees to restore the District's unrestricted General Fund reserve to the Designated Reserve percentage of the total budgeted annual expenditures, less funds allocated for one time expenditures (such as for TCOs) and passthrough expenditures (such as the STRS On Behalf), in all unrestricted General Funds.