

LAKE DON PEDRO COMMUNITY SERVICES DISTRICT

Policy and Procedures Manual

POLICY TITLE: Reserve Policy
POLICY NUMBER: (to be established)
ADOPTED: July 18, 2016
AMENDED:

This statement is intended to provide policy and direction concerning the District's comprehensive reserve policy.

BASIC POLICY AND OBJECTIVES

The Lake Don Pedro Community Services District reserve policy is a financial policy guided by sound accounting principles of public fund management. The policy establishes several reserve funds intended to:

- Minimize adverse annual budgetary impacts from fluctuations in anticipated and unanticipated District expenses
- Ensure that new water system customers and new development projects pay the proportional cost of the value in the existing system and the cost of system expansion needed to serve the water demand of these new connections
- Plan and set aside funding in advance for known future expenditures, to make cash available for purchases when necessary and to conduct planning, design, permitting and other capital improvement project preparatory actions
- Ensure that adequate funding is available connection and other mitigation type fees to construct improvements related to system capacity

The adequacy of the target reserve year end balance ranges and/or annual contributions will be reviewed annually during the budgeting and rate setting process and may be revised accordingly as necessary. The following District reserve fund categories are established:

1. Capital Facility Replacement Reserve (Water Service and Administration)

1.1. **Purpose:** Fees are collected for the future replacement of existing facilities and major equipment.

1.2. **Target Balance:** The target balance continually fluctuates with the addition and replacement of new facilities and equipment. As new facilities and equipment are built, acquired or purchased, the target balance will increase in order to provide for the ultimate replacement of these facilities at the end of their life-cycle. As such, the current target reserve balance is the amount that should be funded at

the end of each fiscal year according to a replacement reserve study and Capital Improvement Plans (CIP), which are reviewed annually.

1.3. **Methodology/Rational:** The District records depreciation using the straight-line method over the estimated useful lives of facilities and equipment. The fee is collected to replace District facilities and equipment as they reach the end of their useful life and also to handle unanticipated repairs during the life-cycle.

1.4. **Use of Funds:** The funds will be used to replace facilities and equipment as necessary to continue reliable and efficient District water services.

1.5. **Funding:** Annual contributions from user fees are currently based upon annual projected requirements in conjunction with the overall budget, replacement reserve study and CIP. Interest earnings will be accrued on and added to fund balance, using the District's earnings rate on investments. In addition, the Board of Directors may approve the designation of available fund balance as Capital Replacement Reserves provided, however, that sufficient Operating Fund balances are preserved.

2. **Capital Facility Improvement Fee Reserve**

2.1. **Purpose:** To provide funds for the orderly and timely expansion of the District facilities to meet future demand and to maintain and/or improve the District's regulatory compliance and existing level of service.

2.2. **Target Balance:** AB1600 does not designate a target reserve balance. A Government Code 66000 Compliance Report identifies the proposed capital projects necessary to maintain and/or improve services and the amount needed to fund those capital projects. In accordance with Government Code 66000, the balance shall not exceed the amount specified by that law. The target funding level will be established at an amount adequate to fund the estimated cost of future system expansion.

2.3. **Methodology/Rational:** Virtually all development that may occur within the District requires the use of District facilities, plant and equipment for public services. This fee is established to insure the adequacy and reliability of such facilities, plant and equipment as development of undeveloped land occurs. The fee is charged when vacant properties established prior to this policy apply for new meter installation. The fee is also charged to new development projects specifically to offset and avoid any cost or negative impact to the existing system caused by the water demand of future customers. Connection and capacity fees shall be set at the level to fund the necessary capacity improvements in a timely manner in advance of the new water demand occurring.

2.4. **Use of Funds:** The funds generated by the fee will be used to acquire and/or construct various capital facilities, both replacement and capacity related for the water plant, distribution system and equipment for the provision of water and administrative services.

2.5 **Funding:** Annual contributions from connection fees (capacity portion) and developer fees will depend upon new construction within the District. Additionally, interest earnings will be accrued on and added to fund balance, using the District's earnings rate on investments.

3. **Water Supply Contingency Reserve Fee**

3.1. **Purpose:** To provide funds for the orderly and timely augmentation of the District's water supply to meet future demands during a major drought event, determined based on the water demand of the undeveloped lands, as it develops within the District's existing boundaries.

3.2. **Target Balance:** This reserve fund is based on a combination of the development of groundwater well systems and the lowering of the existing Lake McClure Intake pumps to provide a more reliable water supply system during drought, and an alternate water supply when the Lake McClure surface elevation drops below the lake's statutory Minimum Pool. The amount of the reserve will be set at the level detailed in the current Water Supply Assessment Report prepared by or under the supervision of the District Engineer.

3.3. **Methodology/Rational:** Virtually all development that occurs within the District requires a potable water supply, as well as a non-potable supply for fire suppression. The current water supply facilities of the District are adequate to meet the human consumption, sanitation and fire protection supply needs of the existing development, but additional water supply facilities are required to serve future development within the District. Specifically, this fee applies on an equitable basis only to those future connections and developments that require water service, and the funds generated from this fee will be used to develop water supply facilities that will be capable of meeting the water supply needs of said new connections and future development. This fee is established to insure the adequacy and reliability of the District's water supply as development of undeveloped lands occurs, and to continue to meet the minimum water supply needs of the community during extreme drought conditions.

3.4. **Use of Funds:** The funds generated by the fee will be used to pay the proportional share of cost of the Lake McClure Intake Pump Extension Project and the construction cost of the number of new groundwater wells necessary to serve the drought water demand of new system connections and new development projects. The fund may also be used to pay for the construction of the transmission and treatment facilities determined necessary by the District, and may also include the cost of performance of various studies and other miscellaneous management and administrative functions.

3.5. **Funding:** Annual contributions from accumulated connection and developer fees will depend upon new construction within the District. Additionally, interest earnings will be accrued on and added to fund balance, using the District's earnings rate on investments.

4. **Capital Improvement Connection Fee Reserve (Vacant Parcels)**

4.1. **Purpose:** Fees are collected as a primary source of funds for the development of additional water treatment and system capacity to serve the parcels existing within the District at the time of adoption of this policy. The fee is set at a level which will defray the costs of providing service to the existing vacant parcels including additional water treatment and/or distribution facilities, major trunk and transmission pipelines and facilities for pumping when such facilities are needed.

4.2. **Target Balance:** The target balance is set at the amount as determined by the District Engineer, necessary to:

1) Fund the cost of the value of capacity in the existing water treatment and distribution system, as necessary to serve the demand of full buildout of the existing system vacant lots; and

2) Fund the cost of the installation of additional water treatment plant capacity, distribution pumps, water storage tanks, valves, controls and pipelines necessary to serve full buildout of the existing system vacant lots; and

3) Mitigate the impact of any future land development project, set on a project by project basis using established per parcel fees.

4.3. **Methodology/Rational:** Vacant lots have been paying an annual standby assessment since the inception of the system. This funding has been dedicated toward general system maintenance and replacement to maintain the system in a ready-to-serve capacity. The buildout of the system has occurred much slower than ever anticipated, requiring major system renovations and improvements, and the vacant lot standby fee has been determined to be wholly inadequate to fund a proportional share of these improvements.

A study will be prepared by the District Engineer to identify the cost of major existing system renovations attributable to vacant parcels but not paid with standby fees; and the cost of future system improvements needed to serve the added capacity of full system buildout (all vacant lots connected). The expense detailed by this study will be used to calculate new connection and capacity fees which when charged, will be deposited into this reserve account to fund the improvements when needed.

4.4. **Use of Funds:** The funds will be used to maintain and enhance system water treatment and distribution system capacity.

4.5. **Funding:** This fee is collected in connection fees with each service application from a vacant parcel. In addition, the per new connection value of treatment and distribution capacity will be charged to all new land development projects and deposited into this account. Interest earnings will be accrued on and added to fund balance, using the District's earnings rate on investments.

5. **Rate Stabilization Contingency Fund Reserve (Water Service and Administration)**

5.1. Purpose: To offset revenue shortages due to high levels of water conservation, economic hardships and/or unforeseen major expenses.

5.2. Target Balance: The minimum and maximum balances will be periodically reviewed by the Board and are to be maintained based upon the level of next year's revenue. The minimum level is no less than 25% of one year's current operating revenue. The maximum limit will be no greater than 75% of next year's fund revenue.

5.3. Methodology/Rational: An economic hardship or unforeseen event could cause a loss of revenue for the District. If such an event occurs, the District could use these funds to stabilize revenues while adjusting rates if necessary to compensate for the fluctuation.

5.4. Use of Funds: These funds will be used to supplement differences in revenue projections resulting from economic hardships and unforeseen events.

5.5. Funding: Initial contributions will be set at up to 50% of any positive fund balance at the close of a fiscal year, net of transfers to other capital reserves. The Board will allocate the highest feasible amount annually to this fund considering near future operating and capital expense needs. Additionally, interest earnings will be accrued on and added to fund balance, using the District's earnings rate on investments.

6. Operating Fund Contingency Reserve (Water and Administration)

6.1. Purpose: To ensure cash resources are available to fund daily administration, operations and maintenance of providing and administering water services.

6.2. Target Balance: A minimum of six months of cash to fund District expenditures.

6.3. Methodology/Rational: The District is required to have sufficient cash flow to meet the next six months of budgeted District expenditures (Government Code Section 53646(b)(3)). The next six months of projected cash revenues can be included as a source of cash flow to satisfy this requirement. Revenues in excess of reserve contributions and expenditures resulting from expenditure savings or timing differences are also reflected in this fund.

6.4. Use of Funds: These funds will be used to pay for expenditures according to budget and expenditure authority.

6.5. Funding: Annual contributions will vary, depending upon other reserve requirements and current year expenditure requirements. Additionally, interest earnings will be accrued on and added to fund balance, using the District's earnings rate on investments.