

Contra Costa Water District Reserve Policy

Reserve Policy

The purpose of the Contra Costa Water District's (CCWD) Reserve Policy is to ensure that the District will at all times have sufficient funding available to meet its operating, capital and debt service cost obligations. Reserves will be managed in a manner that allows the District to fund costs consistent with its annually updated Capital Improvement Program and Ten-Year Financial Plan as well as other long-term plans while avoiding significant rate fluctuations due to changes in cash flow requirements. Operating reserves will be maintained at a minimum level of six months of budgeted operating costs, consistent with the adopted Rate Setting Policy. Adequate reserves and sound financial policies promote CCWD's bond ratings in the capital markets; provide financing flexibility; avoid potential restrictive debt covenants; and ensure the District's customers of stable rates. The Reserve Policy covers all reserve funds of the District. At the end of each fiscal year compliance with the Reserve Policy will be reported to the District's Board of Directors as part of each Fiscal Year-End Financial Report.

Reserve Fund Types

There are three major types of reserve funds: Legally Restricted Reserves, Board Designated Reserves and Unrestricted Reserves. Legally Restricted Reserves have restrictions imposed by an outside source, such as bond covenants, contractual obligations, etc. Board Designated Reserves are set aside for a specific purpose as determined by the Board of Directors. The Board of Directors has the authority to redirect the use of these reserves as the needs of the District change. Unrestricted Reserves are planned for use in each update to the Capital Improvement Program and Ten-Year Financial Plan to assist in providing for minimal orderly rate increases at or below inflation, consistent with the Board's Rate Setting Policy.

CCWD Reserve Fund Specific Purposes

Legally Restricted Reserves

- **Bond Reserve Fund:** This fund is governed by legal bond covenants for the District's revenue bonds. Bond covenants require that this fund be maintained at a level sufficient to fund maximum annual debt service payments. These funds are held by the bond trustee during the term of the bonds and are to be used in the event that the District is unable to meet its required semi-annual debt service obligation.

Reserve funds for each revenue bond issue will be used to make the last two semi-annual debt service payments for that issue. Annual interest earnings on bond reserve funds shall be applied to each year's debt service payments. Reserve funds related to state revolving fund

loans shall be treated identically to revenue bond reserve funds as these loans are contractually defined as parity debt to the District's senior lien bonds.

- United States Bureau of Reclamation (USBR) Reserve Fund: This fund is required by the District's water service contract with the USBR to have a minimum balance of \$1 million for the purpose of paying any annual obligation to the USBR. If the USBR reserve fund balance is drawn down below \$1 million in a given fiscal year, the fund use must be reported to the USBR, and the balance must be returned to the \$1 million minimum balance by the end of the same fiscal year.

This fund will be maintained at the minimum level of \$1 million as long as the District's water service contract with the USBR requires such a fund. If the District's water service contract with the USBR is amended to exclude this reserve fund requirement, the fund balance shall be transferred to unrestricted reserves.

Board Designated Reserves

- Rate Stabilization Reserve Fund: This fund was established in accordance with the Master Bond Resolution adopted by the Board in October 1987. The purposes of the fund were to assist in smoothing rates to pay Los Vaqueros Project debt service and to assure that minimum debt service coverage ratios required by the District's bond covenants would be met in the future. Funds deposited into this reserve were treated as operating costs in the year of deposit and will be treated as revenues in years of use for the purposes of computing the District's debt service coverage ratio. The District's bond covenants and the Board of Directors' rate policy specify that the District's coverage ratio must be at least 1.25 to 1 for senior lien debt. This fund is applied in the ten-year financial plan and annual rate model along with other reserve funds to smooth future rate increases. This fund is sufficient to provide for average bond coverage of 1.275 times over the term of the District's outstanding bonded and other parity debt. This is moderately higher than the minimum levels required, and provides a buffer should revenue estimates in any year not meet projections.

The Rate Stabilization Reserve Fund will be drawn down to smooth rate increases consistent with the District's Rate Setting Policy and to ensure that minimum debt service coverage of 1.25 times annual debt service is met. Specifically, they will be applied in any year where other revenues are not sufficient to meet the required debt service coverage ratio of 1.25 times. They will also be applied if meeting only minimum coverage levels could result in the District's bond ratings being downgraded.

- Capital Improvement Reserve Fund: This fund was established by the Board in FY94 to fund two years of revenue funded capital projects as planned in the Capital Improvement Program (CIP) and the two-year capital budget. The basis for funding two fiscal years is that the typical construction season for many capital projects span the spring and summer months, which fall into two fiscal years. This fund is applied in the ten-year financial plan and annual rate model along with other reserve funds to smooth future rate increases.

This fund will be drawn down annually as revenue capital expenditures are made. At the end of each fiscal year, the fund balance will be evaluated and replenished based on the next two years' revenue funded capital requirements. Annual replenishment shall be reported to the Board of Directors as part of each Fiscal Year-End Financial Report.

- Vehicle Replacement Fund: This fund was established in FY89 to fund planned replacement of vehicles and heavy equipment that have reached the end of their useful lives. This fund is utilized to cover equipment replacement while smoothing cash flows in the ten-year financial plan and annual rate model to minimize annual pressure on rates.

This fund will be drawn down annually as replacement vehicles are purchased consistent with the adopted budget. At the beginning of each fiscal year, funds will be deposited in this sinking fund as provided for in the adopted fiscal year budget. Budget levels will be based generally on annualized deposit requirements as determined by the District's Ten-Year Financial Plan. Annual deposits shall be reported to the Board of Directors as part of each Fiscal Year-End Financial Report. In addition, interest earnings on fund balances will be deposited into the fund as will the net proceeds of the sale of replaced vehicles and equipment. These additional deposits are to provide for inflationary increases to replacement vehicle and equipment costs. This fund shall be maintained at a minimum balance of the funds required for the following year's budgeted fleet replacements. The balance shall not exceed total expenditures planned in the Capital Improvement Program and Ten-Year Financial Plan.

- Future Water Supply Reserve Fund: A portion of each charge for a new connection to the District's system is designated for the purchase of new water supplies for both additional supply and improved supply reliability. The amount collected per new connection is based on the District's adopted Future Water Supply Study. These funds are set aside in a designated reserve for future water purchases as necessary to meet demand reliably.

The designated future water supply component of every charge for a new connection will be deposited into this reserve fund. The growth element of this fund will be used to purchase future water supplies, options, transfers, etc., to ensure that sufficient supply is available to serve planned growth in the District's service area. The reliability element may be used at the Board's discretion to fund capital projects to improve water supply and/or quality reliability or to purchase water supplies aimed at improving reliability. Fund balances will be re-evaluated against future requirements following each update of the Future Water Supply Study, and any proposed adjustments will be presented to the Board of Directors for consideration.

- Seismic Reliability Improvement Program (SRIP) Reserve Fund: A portion of each charge for a new connection to the District's system is designated to pay growth's share of debt service for those components of the SRIP that provide additional capacity for growth, principally the Multi-Purpose Pipeline project. The amount collected per new connection is based on the SRIP study. Long-term debt for the program's projects has been issued as of August 2003, with the exception of the raw water pipeline, which is planned for construction in 2015.

This fund will be used to supplement each year's annual connection fees collected for paying SRIP debt service to fully cover growth's share of annual debt service until the fund is exhausted.

- Self-Insurance Reserve Fund: This fund was established to pay extraordinary liability claims and/or workers' compensation costs up to deductible levels specified in the District's insurance policies. Based on advice from the District's insurance broker, the fund was set to cover five claims of \$250,000, for a minimum balance of \$1,250,000. This level of funding was reaffirmed in a 2004 analysis based on the District's self-insured retention or deductible per claim for general liability, employment practices and property claims.

This fund will be maintained at a level of \$1,250,000 million to provide for extraordinary liability and/or workers' compensation costs exceeding any year's initial adopted budget for those costs. Use of these funds would require an approved budget transfer consistent with budget transfer authority levels determined by the Board of Directors. If funds are transferred in a given year resulting in a fund balance of less than \$1,250,000 at year-end, the fund will be replenished annually from unrestricted reserves to a balance of \$1,250,000 and reported to the Board of Directors as part of the Fiscal Year-End Financial Report.

- Workers' Compensation Fund: This fund is established to pay workers' compensation deductible obligations from claims initiated in prior fiscal years under a large deductible insurance program. It will be initially funded in the amount of \$500,000, consistent with the adopted FY07 budget, although the Board of Directors may approve additional deposits into this fund.

Regular annual fund deposits will be made at the beginning of each fiscal year as budgeted based on the most recent actuarial estimate of annualized obligations. This fund will maintain a positive balance until all claims to be paid from the fund are resolved.

- Los Vaqueros Commitments Reserve Fund: This fund was established in FY97 to provide for contractual obligations to potentially repair land-slide damage to Vasco Road or relocate Los Vaqueros Project facilities. It was initially funded at \$2,442,000 based on the contractual cap with Contra Costa County for slide repairs. Although the slide repair obligation expired in November 2004, the District has additional contractual obligations related to the Los Vaqueros Project, such as potential pipeline relocations at the District's cost should County roadways be relocated in the future. Based on close out of the Los Vaqueros Project, there were \$906,000 of funds remaining in a separate project fund at the end of FY06 that were added to this fund, for a new fund balance of \$3,348,000. The existing fund balance will be retained in the event any of these obligations are triggered.

This reserve fund will pay for any costs resulting from contractual obligations related to the Los Vaqueros project. As these obligations expire or are required to be implemented, the fund balance will be evaluated, and any proposed changes will be presented to the Board for consideration.

- Sacramento/EBMUD Mitigation Reserve Fund: This reserve fund will provide funding for wheeling up to 3,200 acre-feet per year of the District's Central Valley Project water allocation through East Bay Municipal Utility District raw water facilities to meet the District's source water quality needs beginning in approximately the year 2010.

This reserve fund will initially be funded at \$1,290,000, and all funds received as a result of the District's settlement related to the Sacramento Regional Growth Project shall be deposited to this fund. It will be maintained at a level sufficient to fund three to five years of wheeling charges to the East Bay Municipal Utility District for use of its raw water facilities to transport up to 3,200 acre feet annually of the District's Central Valley Project water allocation.

- Clean Water Act Reserve Fund: In FY90 the District received a low-interest loan to pay for a portion of the improvements in the Castlerock and Northgate Assessment Districts. The loan proceeds has been set aside for low-interest loans to assist property owners living within those assessment districts' zone of benefits to buy into the assessment districts.

These funds will continue to be used to assist property owners within the Castlerock and Northgate Assessment District to buy into those assessment districts until the funds are exhausted. They will not be replenished from other District reserves.

- OPEB Reimbursement Reserve Fund: To comply with Government Accounting Standards Board (GASB) standard 45, the District established a trust fund in early FY08 to fund the actuarial value of other post-employment benefits (OPEB) for retirees and their beneficiaries, primarily medical insurance premiums. In FY12 employee contributions to the OPEB Trust have been initiated pursuant to agreements reached with all District employees. A term of those agreements provides that employee contributions plus 5% interest would be reimbursed when an employee separates from District service prior to vesting in the OPEB benefit. Internal Revenue Service regulations prescribe that OPEB Trust assets cannot be used for any purpose other than to fund the OPEB benefit. Consequently, such reimbursements will be made from this Board designated reserve fund.

An initial allocation of \$100,000 from unrestricted reserves will be deposited into the OPEB Reserve Fund. At the end of each fiscal year the fund balance will be adjusted to maintain the target balance of \$100,000. Annual adjustments shall be reported to the Board of Directors as part of each Fiscal Year-end Financial Report.

- Drought Contingency Reserve: Water sales revenue may be impacted under drought conditions due to regulatory or State and Federal mandated reductions in supply. This fund is established to supplement water sales revenue at the direction of the Board of Directors. It will be initially funded in the amount of \$3,500,000. The balance in this reserve may be increased or decreased as authorized by the Board based on the continuance and severity of a drought.

Unrestricted Undesignated Reserves

Unrestricted reserves will be drawn down over time to smooth rate increases and will be maintained at a minimum balance of six months of annual operating budget requirements, consistent with the Board's Rate Setting Policy.