



October 16, 2024

TO: Utilities Advisory Committee
FROM: Ron Munds, General Manager
SUBJECT: **Agenda Item 6 – 10/16/2024 UAC Meeting**
Proposed Changes to Fund 500 Reserves Policies

STAFF RECOMMENDATION:

Staff recommends that the UAC:

- 1. Review the draft Fund 500 reserve policy update; and**
- 2. Provide feedback and recommendations to staff regarding the proposed changes.**

DISCUSSION

Background

The District's original reserve policies were adopted in 2006 (Resolution 2006-23). The policies established encumbered fund balances for each fund to provide a protected source of funding for operational, emergency, expansion and capital replacement needs of the District. The policies were amended in 2007 (Resolution 2007-24) to change the funding goals for each fund. In 2012, the reserve policies were significantly amended to add more specific language for the funding goals for Funds 100/Administration, 301/Fire, 500/Water, 650/Solid Waste and 800/Drainage (Resolution 2012-09).

In 2016 (Resolution 2016-14), the Board adopted a resolution that appears to have amended the 2007 reserve policies since the format and language in both are similar. Also, there is no reference to the 2012 reserve policies. Staff believes the 2012 policies better reflect how the District has been operating and accounting for reserves across all funds and recommends using those policies as a basis for the updates.

Fund 500 Recommended Updates

Currently, there are six reserve categories in the Fund 500 policy. The following are the proposed changes to those categories.

Rate Stabilization

Delete Section 1.ii- the fee waiver or reductions referenced in this section are not a realistic reason to utilize the rate stabilization funds.

The maximum funding goal under 10% of the operations and maintenance budget is estimated at \$200,000; the current balance is \$158,456.

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General Water Contingency Reserve

In 2017, the 2016 policy for this reserve category was amended to reflect the annual appropriation of \$57,000. This change is carried over to amend the 2012 policy. The funding goal is 60% of the water operation and maintenance budget which would be approximately \$1,200,000. The current reserve balance is \$756,183.00.

Water Capital Outlay Reserve

The annual funding goal of \$150,000 is dated and the cumulative funding goal of \$470,000 is not relative at this point in time. The draft language is a result of past water rate setting efforts. During the last water rate analysis, the annual funding goal was set at \$800,000 to fund projects in the District’s five-year capital improvement plan which was approved by the Board during the budget process. The proposed language provides flexibility for the Board to set an annual funding goal as part of any future water rate setting process. This will also allow for changing capital project priorities and the ability to tailor the funding goal to change in revenue and expense projections.

Staff recommends adding the long-term goal of the reserve is to maintain a balance of \$1,000,000 for unforeseen expenses. This was discussed during the 2021 water rate setting study as a prudent amount since capital project costs have risen significantly over the past five years. The current amount in the reserve is \$1,999,562.85.

Water Quality Reserve

The Water Quality Reserve was created using funds from a settlement with an oil company associated with groundwater contamination from leaking gas tanks. To staff’s knowledge, the reserve has not been utilized for many years. It is recommended the reserve be eliminated and the funds transferred to other existing reserves like Capital Outlay and/or Rate Stabilization. The current amount in the reserve is \$91,517.27.

Water Conservation Reserve

This reserve was created around 2008. At that time, the conservation program was just being initiated and there was no line item in the water fund budget to support the effort. Since that time, the water conservation program has been supported by an independent line item therefore eliminating the need for the reserve. It is recommended that the funds be transferred to another existing reserve. The current amount in the reserve is \$59,288.00.

Basin Management Reserve

This reserve was established when the District was in the early stages of the litigation on limiting groundwater pumping in the Los Osos Groundwater Basin. Similar to the Water Quality and Water Conservation Reserves, the funds have not been utilized for many years and are now budgeted annually in the Fund 500 budget. It is recommended that the funds be transferred to another existing reserve. The current amount in the reserve is \$50,031.00.

Attachments

- Redline version of the Fund 500 Reserve Policy
- Clean version of the Fund 500 Reserve Policy
- Fund 500 Reserves as of 8/31/24

SECTION 1: RESERVE POLICIES

A. Water – Fund 500:

1. A Rate Stabilization Reserve shall be established to:

i. Equalize revenues should District income from the Utility billings decrease due to conservation efforts initiated by the District or by the public; ~~and.~~

~~ii. Provide a funding source to offset operation and maintenance revenues associated with fee waivers or reductions approved by the District Board of Directors in accordance with District policies and procedures established pursuant to Government Code Section 61123).(d). Reserves in this category shall be funded by water sales revenues.~~

The funding goal of this Rate Stabilization Reserve shall be \$32,000 annually until such time as this Rate Stabilization Reserve reaches a total of ten (10%) percent of the total annual water Operation and Maintenance Budget as approved by the Board of Directors from time to time.

2. A General Water Contingency Reserve shall be established for Emergency Operations should a natural or other disaster occur that would temporarily interrupt the District's income from Utility bills, repair District facilities, and to provide funding for unforeseen circumstances not covered by the District's Fund 500 Operation and Maintenance Budget. The funding goal of this reserve account is an annual appropriation of at least ~~\$25,000~~57,000 per year up to a maximum cumulative goal of sixty (60%) percent of the District's Fund 500 annual Operation and Maintenance Budget as approved by the Board from time to time.

3. A Water Capital Outlay Reserve will be established for the replacement of water infrastructure. The funding goal of the Water Capital Outlay Reserve is to fund the timely replacement of water infrastructure and facilities as referenced in the District's Water Master Plan or other subsequent water planning documents approved by the District. The annual funding goal of this reserve will be determined during periodic water rate studies approved by the Board from time to time~~is at least \$150,000 per annum, with a short term cumulative funding goal of \$470,000 and The~~ long-term cumulative funding goal is to maintain a minimum reserve balance of \$1,000,000 while also funding the equal to the total of needed capital improvement projects identified in the Water Master Plan~~five-year Capital Improvement Plan approved by the Board annually.~~

~~4. A Water Quality Reserve shall be established to fund studies on the causes of pollution and contamination of the District's water supply, to mitigate the problem so as to continue delivery of safe drinking water and fund short term and long term solutions to prevent and mitigate water contamination problems in the future for the whole community. There is no annual funding set for this Reserve but will continue to exist only as long as there is a balance in the settlement account of a water pollution~~

~~case received in 2005. When the funds are exhausted, this Reserve will cease to exist.~~

~~5. A Water Conservation Reserve is established with an initial funding of \$25,000 in FY 2012/13. No annual funding for this reserve is set but will increase annually by the appropriation balance in the Water Conservation Program account (No. 7348) as of the end of each fiscal year. The cumulative funding goal of this reserve is \$100,000.~~

~~6. A Designation for Water Basin Management or ISJ Commitments is hereby established. This will be funded by any appropriation balances in account no. 9155, ISJ Costs- Inter-Agency Cost Sharing, remaining as of the end of each fiscal year that is not otherwise held in a Reserve for Encumbrance or Fund Reservation starting with the close of FY 2011/12. Initially, the cumulative funding goal of this Reserve is \$1 million.~~

B. Drainage - Fund 800:

1. A Drainage Capital Outlay Reserve fund shall be established for the replacement of equipment and facilities associated with the operation of District drainage services. The funding goal of this Capital Outlay Reserve will be at least \$10,000 per annum with a total funding goal of \$500,000. The total funding goal may be adjusted by the Board of Directors from time to time as part of the adoption of the annual budget. The maximum goal is set to a level that is sufficient to replace at least half of the drainage equipment and facilities at any point.
2. A General Contingency Reserve shall be established for contingency expenditures resulting from natural disasters or unforeseen circumstances. Funding goal for this reserve account is \$5,000 per annum with a cumulative funding goal of \$50,000. When this goal is reached, it shall be funded with an annual increase in accordance with the CPI index change as per Section 3 applied to the balance of this reserve as of the last audited fiscal year.

SECTION 2: RESERVE FUNDING INCLUDING INVESTMENT INCOME

Reserve funding sources include rates, charges, special taxes, and property taxes collected by the District related to the services referenced in Section 1 of this Resolution.

All interest and other investment income earned on funds held in reserves or designations will be added to the associated Reserve/Designation Balance. Reserves and Designations that have reached their cumulative funding goal will continue to increase with investment income unless the Board approves a specific amount cap to a specific reserve or designation.

In any year where there is a major shortfall in revenues due to unusual circumstances which may or may not be under the control of the Board of Directors, funding for Reserves is held in abeyance and is subsidiary to the funding of Operations and Maintenance expenditure accounts. After the circumstance is resolved, funding for Reserves for all years that were not fully funded will be restored whenever feasible. A description of the unusual circumstance will be presented to the Board at the time the Proposed Budget or the Final Budget is presented along with a statement of the impact on the reserves funding goals.

SECTION 3: INCREASE FUNDING OF RESERVES EQUAL TO THE INCREASE IN THE CONSUMER PRICE INDEX (CPI)

Funding increases to Reserves on account of the change in CPI Index as used in Section 1 is computed as the percentage change in the average of the annual averages of the last calendar year over the prior calendar year using the Los Angeles-Riverside-Orange CPI and the San Francisco-Oakland-San Jose CPI for all consumer items. This section will apply once certain reserves reach their maximum funding goal and is intended to bring the reserve in line with current values each year.

SECTION 4: SPECIFIC ACCOUNTS THAT WILL AUTOMATICALLY GO TO RESERVES OR DESIGNATIONS

~~1. Appropriation balances of specific accounts, not otherwise held in a Reserve for Encumbrance or Fund Reservation, as of the end of each fiscal year will automatically roll over to the subsequent fiscal year as increases to the associated reserve/designation unless the Board directs otherwise during the adoption of the annual budget; these accounts are as follows:~~

- ~~a. Capital Outlay accounts~~
- ~~b. ISJ Charges~~
- ~~c. Water Conservation Program~~
- ~~d. Appropriation for Contingencies~~

~~The positive net fund balance at the end of each fiscal year will be allocated, by the Board, to another reserve within the originating budget.~~

2. Proceeds of sale of fixed assets will automatically roll over to the subsequent fiscal year as increases to the Vehicle, Equipment ~~or Plant Replacement~~ Reserve if one exists or to the Capital Outlay Reserve unless the Board directs otherwise during the adoption of the annual budget.

SECTION 5: TRANSFERS

Pursuant to Government Code Section 61112(c), the District Board of Directors may only transfer reserve funds for purposes other than the purposes outlined in Section 1, above, by a four-fifths (4/5) vote of the total membership of the Board of Directors and upon a finding that the reserves are no longer required for the designated purpose. In this instance, the funding may then be allocated to another reserve within the originating fund. Reserve transfers are limited to funding shortfalls in other related budget categories of the particular service and to funding shortfalls in administrative services budget.

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2. A General Water Contingency Reserve shall be established for Emergency Operations should a natural or other disaster occur that would temporarily interrupt the District's income from Utility bills, repair District facilities, and to provide funding for unforeseen circumstances not covered by the District's Fund 500 Operation and Maintenance Budget. The funding goal of this reserve account is an annual appropriation of at least \$57,000 per year up to a maximum cumulative goal of sixty (60%) percent of the District's Fund 500 annual Operation and Maintenance Budget as approved by the Board from time to time.
3. A Water Capital Outlay Reserve will be established for the replacement of water infrastructure. The funding goal of the Water Capital Outlay Reserve is to fund the timely replacement of water infrastructure and facilities as referenced in the District's Water Master Plan or other subsequent water planning documents approved by the District. The annual funding goal of this reserve will be determined during periodic water rate studies approved by the Board from time to time. The long-term cumulative funding goal is to maintain a minimum reserve balance of \$1,000,000 while also funding the capital improvement projects identified in the five-year Capital Improvement Plan approved by the Board annually.

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the CPI index change as per Section 3 applied to the balance of this reserve as of the last audited fiscal year.

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WATER RESERVES

LOS OSOS COMMUNITY SERVICES DISTRICT

Balance Sheet
As of 8/31/2024

		<u>Current Period Balance</u>
LIABILITIES & EQUITY		
CURRENT LIABILITIES		
Trust Liability		
Water Quality Trust Reserve	3050	<u>91,517.27</u>
Total Trust Liability		<u>91,517.27</u>
Total CURRENT LIABILITIES		91,517.27
Other Liabilities		
Other Liabilities		
Replacement Reserve - Vehicle, Equip & Fire Engines	3110	144,644.25
General Contingency Reserve	3111	756,183.00
Capital Outlay Reserve	3160	1,999,562.85
Water Stabilization Reserve	3163	158,456.00
Basin Management Reserve	3165	50,031.00
Water Conservation Reserve	3167	<u>59,288.00</u>
Total Other Liabilities		<u>3,168,165.10</u>
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Total LIABILITIES & EQUITY		<u><u>3,259,682.37</u></u>