

Clear Creek Community Services District
Reserve Fund Policy
December, 2008

Introduction:

In 2001, the Little Hoover Commission reviewed eight independent water districts for reserve fund balances, among other items. The resulting report included a scathing opinion on *excessive and unjustifiable* reserves held by most districts. Only two districts had reserve policies in place to justify the amount of their reserves.

It is this district's opinion that the Little Hoover Commission opinion, based on their report was in error due to cash reserves being overstated by incorporation of numbers that did not belong into the broader category of "retained earnings". The correct representation and clarification is that retained earnings represent cash and investments as well as net value of capital facilities, land and equipment from the inception of the agency.

The Commission broadly described water agency reserves as funds in excess of the actual agency need. In reality, Clear Creek CSD funds are not surplus, but for specific purposes as outlined herein.

It is to this end that Clear Creek CSD establishes a comprehensive reserve policy to ensure the safety of district reserves from seizure by the state or other local governments to fill budget gaps, and assure the customers of the district that all reserves are necessary and justifiable.

Part I - Intent of this Plan

Establishes a comprehensive reserve policy to ensure use of the accumulated public funds cover only reasonable and necessary expenses.

Distinguishes between restricted and unrestricted net assets.

Establishes distinct purposes for all reserves held by the district.

Establishes target levels, i.e. minimum and maximum amounts for the accumulation of reserves.

Identifies triggering events or conditions that prompt the use of each.

Conforms to the district's plan to acquire or build capital assets.

Receives Board of Directors approval in the form of an Ordinance adopting the policy.

Requires periodic review of reserve balances and the rationale of maintaining such balances.

Part II - Background Information

All governments are required to report equity - assets minus liabilities - in terms of net assets.

The accumulated equity does not include net investments (funds already spent on capital assets, less outstanding debt) because net investments should not be viewed as available funds for future activities. Refer back to the Little Hoover Commission report concerning overstated cash reserves by incorporating capital facilities, lands and equipment into "retained earnings" without clarification.

Clear Creek CSD is a fiscally responsible local government agency. Its responsibilities should not be jeopardized by the State of California and/or other local government's inability to manage its finances.

Clear Creek CSD is responsible to build and maintain millions of dollars worth of infrastructure critical to the continued long-term economic health of the district and the southern Shasta County area.

Clear Creek CSD has a constitutional authority under Article XIII B to establish such reserve funds as the Board of Directors deems "reasonable and proper".

Clear Creek CSD's cash reserve accounts were established as part of the overall financial management strategy for the district.

Clear Creek CSD complies with GASB 34 in reporting reserves. It also has the obligation to assist the public and legislature in understanding the purpose of special district reserves and the appropriate levels to be held.

Part III - District Specific

Description of Reserve Funds

Restricted Funds - held to satisfy specific purposes set by requirements of creditors, law, grantors, statutes, etc.

- a) **USBR Emergency Reserve** - held to satisfy the requirements contained in the long-term water service contract with the Bureau of Reclamation. The minimum amount of this fund is \$35,000 as established in the contract. The triggering event for use is a declaration by the Board of Directors that an emergency situation exists on the conduit, and is likely to jeopardize health and safety standards, fish and wildlife, etc. if immediate corrective action is not taken. The district is contractually obligated to replenish the fund within 10 years.
- b) **Filter Plant Reserve** - held to satisfy the requirement by the Department of Water Resources Revolving Loan Fund. This reserve is required to equal two semi-annual payments of the DWR filter plant debt service, in the amount of \$244,000. The triggering event for use is default on the loans on the part of the district. In that instance, DWR would seize the funds to satisfy the amount due, and the district would then be contractually obligated to replenish the fund.
- c) **Expansion and Modernization** - held as capital improvement fund for infrastructure additions and improvements within the distribution system. Current balance is \$843,000. This account is funded annually by capacity charges collected, after the close of the fiscal year. Target amount is \$2,000,000 to allow for future storage, line loops, etc. without concern for depletion of the fund. Triggering event for use is project funding approval by the Board of Directors.
- d) **Water Deposits** - held in trust for customers as required by district rules and regulations. There is no target amount for this fund and the triggering event for use is to satisfy delinquent accounts or refund to customers under certain terms and conditions outlined in district rules and regulations.

Designated or Discretionary Reserve Funds - not required by creditors, law, grantors, statute, etc. The purpose of establishing these funds is to insure adequate levels of reserves or funds are designated for legitimate purposes that are critical to the success of stable short and long term operation of the district.

- a) **Discretionary Reserve** - established by the Board of Directors to be used totally at its discretion for situational or operational issues not otherwise covered by specific reserves or operation and maintenance funding. The current balance is \$178,000¹ and the target amount is \$250,000.
- b) **Contingency Fund** - established for rate stabilization and other emergencies as declared by the Board of Directors. Allows the district to balance short-term fluctuations in revenue, such as during drought, without unplanned significant rate increases that could impact rate-payers. The current balance is \$83,000 and the target amount is \$375,000, 25% of operating sales or 17% of the annual operation and maintenance budget.
- c) **Merchant Account** - established as operational reserves to provide flexibility for quick response to emergency repairs; water quality emergencies; catastrophic incidents, debt reduction, etc. Current balance of \$267,000 is close to target of \$300,000. When fund meets target, overages will be used to increase Contingency Fund to target.
- d) **Filter Plant Savings** - established exclusive for funding capital improvements at the filtration plant as a part of the overall financial planning for the district. These funds will be used to accomplish as many of the improvements listed in the 2007 Master Water Plan as is possible. The current balance is \$302,700 and the target is \$1,000,000.

Reserves for agency operations ensure customers experience stable rates and security that Clear Creek CSD can respond to short and long-term emergencies without delay made necessary by seeking out loans, grants, etc.

The ability to maintain adequate reserves is critical to providing reliable, stable service insuring the district's overall financial strength. Adequate reserves directly affect the district's bond rating and ability to access favorable interest rates, securing the ability to finance and/or construct infrastructure necessary to the existing system and expand facilities for future demand.

¹ Balance was modified to include \$26,000 payoff from Trust Deed. Current CD 10736 matures 12/16/08 and will be increased by that amount as authorized by the Board in October 2008..