

## MARINA COAST WATER DISTRICT RESERVE FUND POLICY - 2009

### ***Purpose of Reserve Policy***

Adequate designations of reserves--funds set aside for various legitimate purposes--are critical to the successful and stable, short and long-term operation of the Marina Coast Water District.

Adequate reserves for District operations ensure that customers experience both stable rates for service and the security that the District can respond to emergencies, especially regarding water and wastewater quality issues. Adequate reserves ensure that the District will at all times have sufficient funding available to meet its operating, capital and debt service cost obligations, together with future debt or capital obligations, as well as any unfunded mandates, including costly regulatory requirements.

The District manages its working capital in a manner that allows the District to fund costs consistent with its annually updated five-year capital improvement program and five year rate study financial plan, and that avoids significant rate fluctuations due to changes in cash flow requirements. The ability of the Marina Coast Water District to maintain reserve funds is a critical factor in providing reliable service, mitigating rate increases, and ensuring overall financial strength.

Adequate reserves directly affect the District's bond rating and ultimately the ability to access debt markets at favorable interest rates, thereby ensuring the ability to finance and construct the infrastructure necessary to renew existing systems and expand service levels to meet future needs.

Annually during the budget adoption process, the Marina Coast Water District Board approves the appropriate levels and uses for reserve funds based upon the needs of the District.

### ***Legally Restricted Reserves***

#### ***Capital Reserve Fund***

The purpose of this fund is to hold funds that are intended for general use on Capital projects. The funds come from contributions from other agencies or from funds that were budgeted on capital projects in prior years but unspent. This fund is spent directly on capital expenditures over the current or future year's normal capital budget and is not held in reserve for some other purpose.

Included in this fund are capacity charge reserves with funds collected from developers to pay for the new facilities necessary to deliver water and wastewater service to newly developed property. These fees are for offsite improvements such as the development's fair share cost of wells, reservoirs, transmission mains, treatment plant capacity, wastewater facilities and other necessary facilities. The fees are collected at rates established by the Board of Directors based upon specific financial rate studies. The rates charged are based on a project's equivalent dwelling unit (EDU) basis. These funds are restricted to the design and construction of capital

facilities for water and wastewater delivery.

This Capital Reserve Fund is drawn down annually as planned capital expenditures amounts are made. At the end of each fiscal year, any unspent budgeted capital amount will be reallocated to this fund and will be used in the following year's capital budget. Annual replenishment is reported to the Board of Directors as part of preliminary and final budget approvals. The minimum balance for this fund will be maintained \$1 million.

#### ***Debt Service 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. Any 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.

#### ***Board Restricted Funds***

##### ***Rate Stabilization Fund***

This fund is governed by legal bond covenants for the District's revenue bonds. The purpose of the fund is to assist in smoothing rates to pay MCWD 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 are treated as operating revenues in the year of deposit and will be treated as such in years of use for the purposes of computing the District's debt service coverage ratio.

This fund is applied in the five-year financial plan and annual rate model along with other reserve funds to smooth future rate increases. This fund will provide a buffer should revenue estimates in any year not meet projections. The Rate Stabilization Fund will be drawn down to smooth rate increases. Specifically, they will be applied in any year where other revenues are not sufficient to meet the required debt service coverage ratio. They will also be applied if meeting only minimum coverage levels could result in the District's bond ratings being downgraded.

##### ***O&M Operating Reserve***

The O&M Operating Reserve will vary over time with a goal of maintaining six months average operating expenses excluding depreciation. This reserve is considered a working cash requirement. It bridges the gap between the time expenses are paid and the time revenues from the same service are collected from customers.

##### ***Capital Replacement Reserve Fund***

This fund pays for the replacement of existing facilities and equipment as it reaches the end of its useful life or for major repairs that extend the useful life of facilities. The purpose of this policy is to fund 100% of annual replacement costs.

***Unrestricted Reserves***

Unrestricted reserves also termed “General Reserves” represent a remainder balance of cash that is not yet designated for some use by the Board of Directors.

***Summary***

The reserve fund policy states that designated reserves will be maintained to allow for funding of the District’s operating, capital and debt service obligations, as well as funding for unforeseen events. Reserves will be established, replenished, and used only in a manner which allows the District to fund costs consistent with the Capital Improvement Plan, Five-Year Financial Plan and Rate Study, and other Board adopted actions, and in a manner that requires minimal annual adjustment to water and wastewater rates. The District’s reserve fund policy shall be periodically reviewed and adjusted to meet the needs of the District.