



**LOS ANGELES COUNTY  
SANITATION DISTRICTS**  
*Converting Waste Into Resources*

# **WASTEWATER FINANCIAL RESERVE POLICY**

*Adopted by All Boards November 2022 through February 2023*

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# Wastewater Financial Reserve Policy

## SECTION 1. POLICY STATEMENT

The Los Angeles County Sanitation Districts (Collectively Districts or individually District) are providers of essential public services and, to that end, have made an extensive investment in public infrastructure, operating facilities, and other related assets. Given the impact these essential services have on public health, the environment, and the overall quality of life, very few options exist for service reduction levels in the event of revenue shortfalls or other funding deficiencies. Maintaining prudent financial reserves provides the resources to allow each District to continue to fulfill its commitment to deliver reliable and high-quality service to its customers. Financial reserves provide significant benefits including:

- Stabilizes user charge rates, creating more certainty so ratepayers can better plan their budgets;
- Minimizes risk associated with borrowing, which can result in lower interest costs;
- Demonstrates each District's financial stability to credit rating agencies;
- Improves liquidity so capital projects can be constructed in a timely fashion, despite fluctuations in cost from year to year;
- Allows each District to effectively respond to economic, environmental, and regulatory changes.

## SECTION 2. TREASURER; ADMINISTRATION

- 2.1 Each District, through the Investment Policy, has appointed the District's Chief Engineer and General Manager as the Treasurer of the District.
- 2.2 The Treasurer, or his or her designee, is hereby authorized to implement this Policy, and establish and maintain all financial reserves in accordance with this Policy and all provisions of law.
- 2.3 The Treasurer shall develop procedures to implement this Policy and shall report to the Board of Directors (Board) of each District in accordance with the requirements of law and this Policy.

## SECTION 3. TYPES OF FUNDS/RESERVES

Each District will maintain its financial assets in various "Funds" as described in this Policy. Fund balances will be maintained in amounts sufficient to meet appropriate target goals, as established in this Policy in cash and/or cash equivalents, and permitted investments as prescribed in the Districts' Investment Policy. Each District's Funds are categorized under this Policy as Unrestricted, Designated, or Restricted as follows:

### 3.1 Unrestricted

The Unrestricted Reserve Funds includes all monies collected or generated by or on behalf of each District, without regard to the source, except those that have been deemed to be Designated or Restricted.

### 3.2 Designated

Designated Reserve Funds are the group of Reserve Funds for which the Board has imposed restrictions on the use of the monies in them for specific purposes such as capital facilities, land acquisition, and repair and replacement of existing assets. The Board may designate these purposes either through specific action or through approval of the annual budget. These monies are not otherwise legally restricted, and the Board has the discretion to redesignate the actual or intended usage of these monies.

### 3.3 Restricted

Restricted Reserve Funds are the group of Reserve Funds that have been established to comply with restrictions that have been imposed externally through law (federal, state, or local governments), administrative action (District adopted ordinances), or contractual arrangements (e.g., bond indentures, State Revolving Fund installment sales agreements). The monies in Restricted Reserve Funds can only be used for the purpose for which they were established or dedicated until the restrictions are removed by the party that imposed them or the contractual agreement that created them has expired.

## **SECTION 4. SYSTEM FUNDS**

Each District may participate with other members of the Los Angeles County Sanitation Districts in separate agreements (e.g., the Joint Administration, Joint Outfall System, and Solid Waste System Agreements). Funds necessary for operations related to these agreements will be pooled. District No. 2 has separately adopted a Solid Waste Financial Reserve Policy for all Solid Waste Funds. The Joint Outfall System Funds are subject to a separate Joint Outfall System Financial Reserve Policy that is adopted by the Joint Outfall Districts pursuant to the Joint Outfall Agreement. Pooled funds described in this policy represent funds that are applicable to at least one District.

## **SECTION 5. UNRESTRICTED RESERVES**

### 5.1 Operating Fund

#### 1. Purpose

Monies in the Operating Fund may be used for any purpose consistent with the budget, other Board direction, legal requirements, and this Policy. Operating Fund monies include all types of revenue unless otherwise restricted. The Operating Fund must be sufficient to meet the cash flow needs of the District and to meet current and anticipated expenses in accordance with the long-term budgetary projections.

#### 2. Targeted Goal

For Districts without an active sewerage system, the targeted goal is sufficient monies to meet projected expenses of the District.

For Districts that participate in the Joint Outfall System<sup>1</sup> (except District 29): The minimum targeted goal balance on July 1 of each fiscal year is twenty percent (20%) of projected service charge and ad valorem tax revenue, which is sufficient for cash flow needed for the individual District. The Joint Outfall System manages operating funds for the system's cash flow needs.

For all other Districts: The minimum targeted goal balance on July 1 of each fiscal year is the projected net expenses during the first six months of that fiscal year. Net expenses shall be equal to all projected expenses less any anticipated revenues (e.g., industrial wastewater surcharges) and funding sources (e.g., State Revolving Fund loans).

3. Review Timeline

The minimum targeted goal shall be reviewed annually in conjunction with the adoption of each District's final budget.

4. Funding

All revenues other than those placed in a Designated Reserve Fund or Restricted Reserve Fund shall be placed in the Operating Fund.

5.2 Districts Business Funds

1. Purpose

The Districts maintain several pooled funds for time sensitive cash-flow purposes. These funds are listed in Table 1 of Appendix A.

2. Targeted Goal

There is no targeted goal for these funds.

3. Review Timeline

These funds are regularly reviewed to ensure that sufficient funds are available for the business need of each fund.

4. Funding

Funding for these reserves comes from various Districts Operating Funds based on each District's share of expenses for the business purpose of each fund.

**SECTION 6. DESIGNATED RESERVES**

6.1 Emergency Fund

1. Applicability

This Fund is applicable to Districts 4, 9, 14, 20, 27, 29, the Santa Clarita Valley Sanitation District, and the Newhall Ranch Sanitation District. District 34 is excluded as it does not have an active sewerage system. The remaining Joint Outfall Districts are excluded as they do not own or maintain their own sewerage system and Joint Outfall System reserves are in place to serve this purpose.

2. Purpose

Each District budgets for all anticipated expenditures, but emergencies and unforeseen circumstances can occur during the course of the year. The Emergency Fund is intended to provide funding for work that must be undertaken to address emergencies or unforeseen circumstances (such as repairing a sinkhole) and to ensure each District can continue to provide all of its vital public services. This fund is only used when insufficient funds are available in a District's Unrestricted and other Designated Reserves.

3. Targeted Goal

The targeted goal balance is the greater of:

- (a) 0.5% of the Net Sewerage Operations Capital Assets as identified in the most recently filed Annual Comprehensive Financial Report multiplied by the ratio of the total number of sewage units in the District to the total number of sewage units in all Districts; or
- (b) \$50,000.

4. Review Timeline

The targeted goal will be reviewed and adjusted annually in conjunction with the adoption of each District's final budget.

5. Funding

The Treasurer will annually transfer from or to its Operating Fund an amount sufficient to meet the Emergency Fund's targeted goal specified in Section 6.1.2. If there are insufficient funds for this transfer, the Treasurer will present to the Board a plan to fully fund this reserve within the next 5 years.

6.2 Operations and Maintenance (O&M) Financial Stability Fund

1. Applicability

This Fund is applicable to Districts 4, 9, 14, 20, 27, 29, the Santa Clarita Valley Sanitation District, and the Newhall Ranch Sanitation District; other Districts are excluded as discussed in Section 6.11.

2. Purpose

The O&M Financial Stability Fund is a dynamic fund that will be used to facilitate wastewater rates transitioning smoothly from year to year. Monies will be withdrawn from this Fund in some years, allowing expenses to be met without having to impose spiked increases in the rates. In other years, monies will be deposited into this Fund, replenishing it in lieu of having spiked decreases in the rates. In any given year, as the need arises, each District may use up to 10% of the Fund for any purpose without Board authorization, in addition to any use previously authorized as part of the rate setting and budget process. When monies are used from this Fund that drop the balance below the targeted goal, the Treasurer will prepare a plan to fully restore the Fund to its targeted goal by the latter of:

(a) Five years; or

(b) Six years of the date for which the last adopted service charge becomes or has become effective.

3. Targeted Goal

The long-term targeted goal balance is equal to six months of operational expenses plus one year of debt service (excluding any debt service that has a Debt Service Reserve Fund). Any District's share of Joint Outfall System operational expenses is excluded from this calculation as the Joint Outfall System maintains reserves for this purpose.

4. Review Timeline

The targeted goal will be reviewed and adjusted annually in conjunction with the adoption of each District's final budget.

5. Funding

The Treasurer will annually transfer moneys from its Operating Fund to the O&M Financial Stability Fund an amount equal to the annual targeted goal. If the transfer of the full targeted goal amount would cause an undue financial hardship on the District or result in a significant rate hike, the Treasurer may transfer less than the targeted goal provided a plan has been prepared to achieve the targeted goal within ten years.

6. Additional Monies

Each District may also place additional monies into the O&M Financial Stability Fund at any time so that the balance exceeds the targeted goal. Monies in excess of the targeted goal can be withdrawn at any time without prior Board authorization as part of the overall plan to stabilize rates.

6.3 Capital Projects Financial Stability Fund

1. Applicability

This Fund is applicable to Districts 4, 9, 14, 20, 27, 29, the Santa Clarita Valley Sanitation District, and the Newhall Ranch Sanitation District; other Districts are excluded as discussed in Section 6.11.

2. Purpose

The size and scope of capital projects (and the associated cost) varies from year to year, which could result in peaks and valleys in user charge rates if the projects are to be funded dollar-for-dollar in the year in which the expenses are incurred. This Fund will ensure that monies are not only available to meet capital expenses over the long-term, but also to meet the annual demand without requiring significant rate fluctuations.

3. Targeted Goal

The targeted long-term average goal balance will be equal to the greater of:

(a) \$100,000 or

(b) The difference between the projected maximum and average annual capital expenditures, to be cash funded from revenues identified in the Capital Improvement Plan over the ensuing ten (10) years. Any District's share of Joint Outfall System capital expenses is excluded from this portion of the calculation as the Joint Outfall System maintains reserves for this purpose.

4. Review Timeline

The targeted goal will be reviewed and adjusted annually in conjunction with the adoption of each District's final budget.

5. Funding

The Treasurer will annually transfer monies from its Operating Fund to its Capital Projects Financial Stability Fund an amount equal to the annual targeted goal. If the transfer would cause an undue financial hardship on the District or result in a significant rate hike, the Treasurer may transfer less than the targeted goal provided a plan has been prepared to achieve the target goal within ten years. In no case shall the fund balance be less than \$100,000 immediately after the annual transfer.

6. Additional Monies

Each District may place additional monies into its Capital Projects Financial Stability Fund at any time so that the balance exceeds the targeted goal. Monies in excess of the targeted goal can be withdrawn at any time without prior Board authorization as part of the overall plan to stabilize rates.

6.4 Rate Stabilization Fund

1. Purpose

The Rate Stabilization Fund is a set aside of monies to ensure a District meets its required Debt Coverage Ratio targets included in its adopted Debt Management Policy or in any financial obligations (e.g., bonds) of the District.

2. Targeted Goal

The minimum targeted balance for the Rate Stabilization Fund is the minimum amount of reserves projected to be needed to meet the District's Debt Coverage Ratio.

3. Review Timeline

The targeted goal will be reviewed and adjusted annually in conjunction with the adoption of each District's final budget.



#### 4. Funding

The Treasurer will annually transfer monies from its Operating Fund to its Rate Stabilization Fund as necessary and presented to the Board to meet the Targeted Goal.

### 6.5 Natural Disaster and Self-Insured Retention (SIR) Fund

#### 1. Purpose

The Natural Disaster and SIR Fund is designated to pay for: 1) short-term costs in the event of an earthquake or other natural disaster in order to continue District operations until state or federal relief funds are received; 2) costs related to a natural disaster that do not result in reimbursement; 3) costs incurred due to an insurance claim that requires the use of the Districts' SIR amount; and 4) costs incurred due to an insurance claim that exceeds the Districts' insured limit; 5) costs incurred due to a loss or claim against the Districts for facilities or events for which the Districts are self-insured. This can include funding immediate repairs to existing facilities and, if the Joint Administration Office becomes unusable, securing other office space. The Natural Disaster and SIR Fund will be pooled and available to all of the Districts and Solid Waste entities.

#### 2. Targeted Goal

The current targeted goal balance for the pooled Natural Disaster and SIR Fund is \$25 million. The targeted goal and the appropriate share for each District and Solid Waste entity may be revised, as needed, to account for changes to risks, property values and SIR requirements.

#### 3. Review Timeline

The targeted goal balance will be reviewed and adjusted every five years with the next review to be completed by June 30, 2027.

#### 4. Funding

At the end of each five-year review period, the Treasurer will make a transfer from a District's Operating Fund to the SIR Fund, as necessary, for the District's share of any increase in the targeted goal. For significant increases, the Treasurer may elect to make a series of transfers as long as the SIR Fund will meet its targeted goal prior to the next five-year review.

### 6.6 Other Future Designated Reserve Funds

From time to time, the Board of Directors may deem it prudent to establish other designated reserve funds in order to further the mission of each District. The Treasurer will create such Reserve Funds as directed and will establish appropriate targeted goals, review timelines, and funding mechanisms. This Policy will be amended to reflect the Board's direction with respect to any additional Designated Reserve Funds.

## SECTION 7. RESTRICTED RESERVES

### 7.1 Other Post-Employment Benefits (OPEB) Reserve Fund

#### 1. Purpose

The Districts collectively provide health care and dental benefits for all retired employees and their dependents or survivors. The Districts have voluntarily elected to enter into a prefunding plan for their OPEB program. The OPEB funds must be held by a qualified third-party trustee.

#### 2. Targeted Goal

The yearly targeted goal will be to transfer to the OPEB Reserve Fund an amount equal to the Districts' actuarially determined contribution (ADC) as determined by a qualified actuarial consultant.

#### 3. Review Timeline

The actuarial review is required at least biennially.

#### 4. Funding

Each year the Treasurer will collectively transfer the ADC to the third-party trustee in installments as required under the terms of the agreement with the trustee. Each transfer shall be apportioned among the Districts and Solid Waste entities in proportion to the salaries incurred by each District or Solid Waste entity since the previous transfer was made.

### 7.2 Debt Service Reserve Fund

#### 1. Purpose

Some debt instruments (e.g., bond indentures, installment sales agreements) may require a Debt Service Reserve Fund, typically equal to the maximum annual debt service over the life of the debt. A separate Debt Service Reserve Fund will be established for each debt instrument that requires it. The monies in each Debt Service Reserve Fund will only be used:

- (a) To support payment of principal and interest of outstanding obligations if revenues pledged for repayment are insufficient to meet the required payment; or
- (b) To extinguish the debt.

#### 2. Targeted Goal

The targeted goal balance for any Debt Service Reserve Fund must equal the amount required by the associated debt instrument.

### 3. Review Timeline

Each Debt Service Reserve Fund balance will be reviewed at least annually as part of the continuing disclosure process required under the debt instrument, but no less than such increments of time as required by any debt instrument.

### 4. Funding

Each Debt Service Reserve Fund will generally be funded at the time the debt is incurred, using a portion of the debt proceeds, if allowable. If the debt proceeds cannot be used to fund the Debt Service Reserve Fund, the Debt Service Reserve Fund may be funded from any allowable District's monies. If the District makes a draw on the Debt Service Reserve Fund, the Debt Service Reserve Fund must be replenished in the time and manner specified in the debt instrument.

## 7.3 Capital Improvement Fund

### 1. Applicability

This Fund is applicable to Districts 4, 9, 14, 20, 27, 29, the Santa Clarita Valley Sanitation District, and the Newhall Ranch Sanitation District; other Districts are excluded as discussed in Section 6.11.

### 2. Purpose

New users and existing users that significantly increase their wastewater discharge are required to pay a connection fee. The capital portion of the connection fee is deposited into one or more Capital Funds in accordance with the District's Master Connection Fee Ordinance. Funds are withdrawn as necessary to fund capital projects.

### 3. Targeted Goal

There is no targeted goal balance for the Capital Improvement Fund. The amount of money deposited into the Capital Improvement Fund is dependent on the rate at which additional burdens are placed on the wastewater system. The Capital Improvement Fund balance varies depending on connection fee revenues and expenditures for capital projects.

### 4. Review Timeline

Connection fee rates will be reviewed in conjunction with setting the District's Service Charge and/or Industrial Waste Surcharge rates.

### 5. Funding

The capital portion of the connection fees will be deposited into the Capital Improvement Fund in accordance with the District's Master Connection Fee Ordinance.

## 7.4 Joint Sewerage Services Agreement (JSSA) Funds

### 1. Applicability

This fund is only applicable to the Newhall Ranch Sanitation District and Santa Clarita Sanitation District.

### 2. Purpose

The JSSA Escrow Fund was established pursuant to the JSSA between the Newhall Ranch Sanitation District and the Santa Clarita Valley Sanitation District.

The JSSA Reserve Fund was established pursuant to the Operating Cost Agreement after first connection between the Newhall Ranch Sanitation District and the Newhall Land and Farming Company.

### 3. Targeted Goal

There is no targeted goal for these funds.

### 4. Review Timeline

Balances for these funds are evaluated at least annually.

### 5. Funding

The JSSA Reserve Fund is only funded through payments from the Newhall Land and Farming Company. The JSSA Escrow fund is funded through payments from the JSSA Reserve Fund.

## 7.5 Trust Funds

### 1. Purpose

The Districts maintain several trust funds required to be held for specific purposes and governed by agreements and/or legal requirements. These funds are listed in Table 2 of Appendix A.

### 2. Targeted Goal

There is no targeted goal for these funds.

### 3. Review Timeline

These funds are regularly reviewed to ensure that sufficient funds are available for the business need of each fund.

### 4. Funding

Funding for these reserves comes from various Districts Operating Funds based on each District's share of expenses for the business purpose of each fund or from Districts' customers.

## 7.6 Bond Construction Fund

### 1. Purpose

When bonds are issued, all of the proceeds are received at the time of issuance. Except for a small portion which is used for the cost of issuance, the proceeds are placed into a Bond Construction Fund and can only be used for the purposes identified in the Official Statement, Tax Certificate, and Installment Purchase Agreement for the bond issuance.

### 2. Targeted Goal

The amount of money in the Bond Construction Fund is dependent on the size of the bond issuance, with the expectation that the proceeds will be expended in the time frames detailed in the Tax Certificate.

### 3. Review Timeline

No review is necessary as there is a single deposit into each Bond Construction Fund.

### 4. Funding

Bond proceeds, except for the cost of issuance, capitalized interest, any required debt service reserve funds, and refunding escrows, will be deposited into the Bond Construction Fund at the time of issuance.

## 7.7 Other Reserve Funds

From time to time, it may be necessary to establish other restricted reserve funds in accordance with law or other statutory requirements or with contractual agreements to which a District is a party. The Treasurer will create such Reserve Funds as mandated and will establish appropriate targeted goals, reviews, and funding mechanisms.

## **SECTION 8. WASTEWATER FINANCIAL RESERVE POLICY ADOPTION**

This Policy will become effective after approval by all of the Districts Boards and supersedes the Wastewater Financial Reserve Policy for each individual District. This Policy will be reviewed on an annual basis and any modifications must be approved by the Boards. After each review, the matter will be referred to the Personnel Committee (comprised of the Chairpersons of the Board of Directors of each active County Sanitation District of Los Angeles County) for its consideration.

# Appendix A

**Table 1. Current Districts Business Funds.**

Fund	Purpose
Payroll	Payroll funding
Workers Comp	Workers Compensation Claims
Vacation/Sick Leave	Vacation and sick leave payments
Carl Warren Fund	Settle Non-Workers Compensation Claims
Flexible Benefits	Employee payments for Flexible Benefits (e.g., Health Savings Accounts)
Transfer	Pass through fund for received monies. Monies are transferred to the respective District or Solid Waste entity monthly
Suspense	Pass through fund used to facilitate wire transfers from the County to the Payroll Account currently held by Bank of America
Undistributed Receipts	Pass through fund for unknown receipts until the correct receiver can be determined
Petty Cash	Petty Cash
Revolving Funds (Various)	Funds to pay for meal benefit checks

**Table 2. Current Districts Trust Funds**

Fund	Purpose
Liquid waste	Draw down fund for monies deposited by liquid waste customers
Connection Fee Collateral	Holding fund for collateral associated with Connection Fees
State Board of Equalization (SBE)	Pass through fund for monies due to the State Board of Equalization due to Annexations
Local Agency Formation Commission (LAFCO)	Pass through fund for monies due to the Local Agency Formation Commission due to Annexations
Miscellaneous	General trust fund for smaller trust account monies (e.g., sewer inspection fee estimates, restitution with a specific purpose, etc.)
Local Strike Force	Accumulated restitution payments and settlement funds from successfully prosecuted cases involving the Districts resulting in efforts with other local government agencies
Property Security Deposits	Holding fund for deposits for required in Districts' leases
Federal Lab Strike Force	Accumulated restitution payments and settlement funds from successfully prosecuted cases involving the Districts resulting in efforts with the Federal Government.
Districts Store	Pass through fund for employee purchases of Districts' merchandise
Duck Farm SEP (Escrow & Interest)	Funds associated with the River Park Supplemental Environmental Project (SEP) that was formerly known as the Duck Farm SEP
Tesoro	Funds held in escrow to address potential future groundwater remediation costs in Long Beach at the Golden-Baker site per settlement agreement with Tesoro SoCal Pipeline