

WASTEWATER
FINANCIAL RESERVE POLICY

County Sanitation District No. 29
of
Los Angeles County

TABLE OF CONTENTS

1.	Policy Statement	1
2.	Treasurer; Administration.....	1
3.	Types of Funds/Reserves	1
4.	System Funds	2
5.	Unrestricted Funds	2
6.	Designated Reserves	3
7.	Restricted Reserves.....	6
8.	Wastewater Financial Reserve Policy Adoption.....	9

Wastewater Financial Reserve Policy

County Sanitation District No. 29 of Los Angeles County

1. Policy Statement

County Sanitation District No. 29 of Los Angeles County (District) is a provider of essential public services and, to that end, has 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 the 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 the 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 the District to effectively respond to economic, environmental, and regulatory changes.

2. Treasurer; Administration

- 2.1 The District, through its 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) in accordance with the requirements of law and this Policy.

3. Types of Funds/Reserves

The 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 District's Investment Policy. The 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 the 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.

4. **System Funds**

The District may participate with other members of the County Sanitation Districts of Los Angeles County (collectively, the 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. Except for Funds dedicated solely to the Solid Waste System and the Joint Outfall System, all pooled Funds will be held and managed by County Sanitation District No. 2 of Los Angeles County as the administrative district for the Districts in accordance with the respective agreements and District No. 2's Wastewater Financial Reserve Policy. District No. 2 will separately adopt a Solid Waste Reserve Policy for all Solid Waste Funds. The Joint Outfall System Districts will separately adopt a Joint Outfall System Financial Reserve Policy for all Joint Outfall Funds.

5. **Unrestricted Reserves**

5.1 Operating Fund

5.1.1 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.

5.1.2 Targeted Goal

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).

5.1.3 Review Timeline

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

5.1.4 Funding

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

6. **Designated Reserves**

The Designated Reserve Funds include the Emergency Fund, the Operations and Maintenance Financial Stability Fund, the Capital Projects Financial Stability Fund, the Natural Disaster and Self-Insured Retention Fund, and any other funds designated by the Board of Directors other than Unrestricted and Restricted Reserve Funds.

6.1 Emergency Fund

6.1.1 Purpose:

The 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 the District can continue to provide all of its vital public services.

6.1.2 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 Comprehensive Annual 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.

6.1.3 Review Timeline:

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

6.1.4 Funding:

The Treasurer will, on July 1 of each year, transfer from or to its Operating Fund an amount sufficient to meet the Emergency Fund's targeted goal specified in Section 6.1.2.

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

6.2.1 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, the 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.

6.2.2 Targeted Goal:

The long-term targeted goal balance is equal to six months of O&M expenses, excluding the District's share Joint Outfall System O&M expenses, plus one year of debt service (excluding any debt service that has a Debt Service Reserve Fund).

6.2.3 Review Timeline:

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

6.2.4 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. In order for the fund balance to be less than 50% of the targeted goal, the sum of the monies in the fund plus the amount the District can borrow from its Capital Improvement Fund, pursuant to the District's Debt Management Policy, must be greater than 60% of the targeted goal.

6.2.5 Additional Monies

The 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

6.3.1 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.

6.3.2 Targeted Goal:

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

(a) The difference between the projected maximum and average annual capital expenditures, excluding the District's share Joint Outfall System capital expenditures, to be cash funded from revenues identified in the Capital Improvement Plan over the ensuing ten years; or

(b) \$100,000.

6.3.3 Review Timeline:

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

6.3.4 Funding:

The Treasurer will annually transfer monies from its Operating Fund to the 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.

6.3.5 Additional Monies

The District may place additional monies into the 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 Natural Disaster and Self-Insured Retention (SIR) Fund

6.4.1 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; and 3) costs incurred due to an insurance claim that requires the use of the Districts' SIR amount. 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, shared proportionally among the Districts and Solid Waste entities.

6.4.2 Targeted Goal:

The initial targeted goal balance for the pooled Natural Disaster and SIR Fund is \$17 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.

6.4.3 Review Timeline:

The targeted goal balance will be reviewed and adjusted every five years with the first review to be completed by June 30, 2022.

6.4.4 Funding:

At the end of each five-year review period, the Treasurer will make a transfer from the Operating Fund to the Natural Disaster Fund, as necessary, for the District's share of any increase in the targeted goal.

6.5 Other 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 the 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.

7. **Restricted Reserves**

7.1 Other Post-Employment Benefits (OPEB) Reserve Fund

7.1.1 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.

7.1.2 Targeted Goal:

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

7.1.3 Review Timeline:

The actuarial review is required at least biennially.

7.1.4 Funding:

Each year the Treasurer will collectively transfer the ARC 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 the District or Solid Waste entity since the previous transfer was made.

7.2 Debt Service Reserve Fund

7.2.1 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.

7.2.2 Targeted Goal:

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

7.2.3 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.

7.2.4 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

7.3.1 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. If the monies are not needed in the short-term, the District may borrow the funds as long as they are repaid with interest before they are needed.

7.3.2 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, expenditures for capital projects, and permitted borrowing from the Fund.

7.3.3 Review Timeline:

Connection fee rates will be reviewed annually.

7.3.4 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 Bond Construction Fund

7.4.1 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.

7.4.2 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.

7.4.3 Review Timeline:

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

7.4.4 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.

7.5 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 the District is

a party. The Treasurer will create such Reserve Funds as mandated and will establish appropriate targeted goals, reviews, and funding mechanisms.

8. Wastewater Financial Reserve Policy Adoption

This Policy will become effective on the later of the approval of the Joint Outfall Agreement dated July 1, 2022 or July 1, 2022. This Policy will be reviewed on an annual basis and any modifications must be approved by the Board. Prior to such 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.

Adopted this _____ day of _____.