

RESOLUTION NO. 05-24

RESOLUTION OF THE BOARD OF DIRECTORS OF
TEHACHAPI-CUMMINGS COUNTY WATER DISTRICT
AMENDING AND RESTATING THE DISTRICT RESERVES POLICY

A. Recitals.

1. The District desires to amend and restate the District's Reserves Policy, set with Resolution No. 15-23 to add a new restricted reserve fund (Engine Project) and incorporate various other revisions.

B. Resolutions.

NOW, THEREFORE, BE IT FOUND, DETERMINED, AND RESOLVED by the Board of Directors of TEHACHAPI-CUMMINGS COUNTY WATER DISTRICT as follows:

1. Each of the above recitals is true and correct and the Board so finds and determines.

2. The Board of Directors of the Tehachapi-Cummings County Water District adopts the amended and restated Reserves Policy set forth in Exhibit A attached hereto as the reserves policy of the District.

PASSED, APPROVED, AND ADOPTED by the Board of Directors of TEHACHAPI-CUMMINGS COUNTY WATER DISTRICT this 15th day of May 2024.



Robert W. Schultz, Board President

ATTEST:



Catherine Adams, Board Secretary

SECRETARY'S CERTIFICATE

I, CATHERINE ADAMS, Secretary of the Board of Directors of Tehachapi-Cummings County Water District, hereby certify as follows:

The foregoing is a full, true and correct copy of Resolution No. 05-24 duly adopted at a regular meeting of the Board of Directors of the District duly and legally held at the regular meeting place thereof on May 15, 2024. All of the members of the Board of Directors received due notice of the meeting and a majority thereof was present. At the meeting the resolution was adopted by the following vote:

AYES: Ables, Hall, Sasia, Schultz, Zanutto

NOES: None

ABSTAIN: None

ABSENT: None

ATTEST:


Catherine Adams, Board Secretary

(SEAL)

EXHIBIT A

TEHACHAPI-CUMMINGS COUNTY WATER DISTRICT RESERVES POLICY

A. PURPOSE

The purpose of this Reserves Policy is to establish various reserve targets, funding priorities, and accomplish prudent financial planning to ensure sufficient funding is available for current operating, capital, and debt service needs. Additionally, fiscal responsibility requires anticipating the likelihood of, and preparing for, unforeseen events. This Reserves Policy serves to ensure Tehachapi-Cummings County Water District's (TCCWD or District) reserves are accumulated, managed, and maintained to protect the District's creditworthiness; to provide for continuing operations including cash flow requirements, maintenance and eventual replacement of existing facilities and infrastructure, addition of new capital assets, and unforeseen and unexpected emergencies; to ensure certain financial resources are used only for specified purposes; and to facilitate stable services and fees.

The policy directives outlined in this Reserves Policy are intended to ensure TCCWD has sufficient funds available to meet current and future needs. The District is comprised of one major enterprise fund for its water operations. This one fund is segmented into twelve internal sub-funds to account for the reserve balances. The Board of Directors of TCCWD (Board) shall designate and restrict specific reserves and maintain minimum reserve balances consistent with the reserve definitions and funding levels outlined in this policy. The Board will annually review the level of the reserve funds in conjunction with its review and approval of the District's budget. For purposes of compliance with this policy, TCCWD will use working capital (i.e., current assets less current liabilities) as of the final day of each fiscal year to calculate the reserve fund levels. Working capital is a better measure than either cash or net position to determine the District's ability to meet its financial obligations and to accomplish its financial plans.

Through this policy and the District's Strategic Plan, TCCWD has set forth a number of its short-term, mid-term, and long-term goals. A fundamental purpose of this policy and the strategic plan is to link what must be accomplished with the necessary resources to successfully do so. Upon Board adoption of this Reserves Policy, TCCWD will take the necessary actions to comply with this policy.

B. GENERAL PROVISIONS

TCCWD will maintain its reserve funds in separate internal sub-funds in a clearly identifiable manner that provides transparency to its ratepayers. Moneys that are legally restricted will be held in Restricted Reserves. Moneys that are not legally restricted will be held in unrestricted Designated Reserves, which includes the General sub-fund accounts.

Moneys will be accumulated in the designated reserve sub-funds in the order presented until the interim target is achieved, at which time the next designated reserve will begin to accumulate. Once all seven interim designated reserve targets have been achieved, money will accumulate in each reserve fund in the order presented until the full target for each reserve fund has been reached. Once a Designated Reserve's full reserve target is funded, any surplus unrestricted funds may be reallocated.

In assessing the funding of future capital facilities and maintaining and replacing existing assets, TCCWD will analyze the benefits and tradeoffs of utilizing pay-as-you-go and/or debt financing and determine the optimal funding strategy. The analysis will consider TCCWD's current and projected reserve fund levels.

In the event that the Designated Liquidity reserve fund balances exceed the established target levels, excess moneys will be transferred annually into the Designated Capital reserve funds. Moneys from the Designated

Capital reserve funds can be moved to pay for operating **emergencies** to supplement the Designated Liquidity reserve funds. In addition, in the event the Capital reserve fund balances exceed the established maximum, the Board will make a determination regarding the reallocation of excess moneys.

Interest income will be credited to the fund on which it was earned until the fund's full target balance is achieved. Once the full target balance is reached within a specific reserve fund, the surplus interest earnings will be reallocated to other reserve funds whose funding level is below the interim or full target levels recommended by this policy.

C. TYPES OF RESERVES

The District maintains two types of reserves: 1) **Designated Reserves** and 2) **Restricted Reserves**. Designated Reserves are further broken down based on one of two purposes: 1) **Liquidity** and 2) **Capital**.

1. **Designated Reserves.** Designated Reserves are unrestricted reserves established by an action of the Board of Directors and set aside for a designated, specific purpose to ensure flexibility and stability. The source of their money is the General sub-fund; therefore, the designated purpose may be changed by the Board. **Liquidity** reserves may be changed or made available for short-term operating loans, when deemed appropriate. **Capital** reserves may be changed or made available for borrowing when deemed necessary in **emergency** situations resulting from extreme, unforeseen, or unexpected circumstances.

2. **Restricted Reserves.** Restricted Reserves have restrictions on their use as imposed by an outside source such as creditors, grantors, contributors, statutes, court orders, contracts, or bond covenants. These reserves must remain in their respective funds, except for Board-approved short-term borrowing (with full interest repayment).

D. DESIGNATED RESERVES

1. Liquidity

General Fund. The District maintains a General reserve fund, which is comprised of the working capital generated from the District's water operations. Although the District operates as an enterprise fund, its primary funding source is general property taxes. The current fiscal year budget forecasts that approximately __%¹ of general fund revenues will be from property taxes and approximately __%¹ will be operating revenues from water sales and services. Costs to perform the District's Watermaster duties under the three basin judgments are also paid from the General reserve fund.

The Government Finance Officers Association recommends that for enterprise funds "governments should start with a baseline of ninety (90) days' worth of working capital and then adjust the target based on the particular characteristics of the enterprise fund in question (using 45 days as the minimum acceptable level)". Since the District's General reserve fund is primarily tax-supported and the first installment of property tax revenue is received five months after the start of the fiscal year, the fund's beginning working capital as of July 1st will be equal to or greater than 90 days of operating expenses and at no point during the year will the working capital fall to less than 45 days of operating expenses. From time-to-time, moneys in excess of 90 days' operating expenses may be set aside within the General reserve fund and earmarked by the Board as **Water Banking** reserve to cover the cost to replace or extract the District's banked water.

[Water Allocation Update to be provided with Preliminary Budget]¹

¹ To be updated in the Reserves Policy that is included as part of the Preliminary Budget.

In addition to the General reserve fund, the District has established four (4) Designated Liquidity reserve funds and one (1) Designated Capital reserve fund. Full reserve targets and interim targets are established herein. All expenditures or transfers from these reserve funds will be replaced as quickly as possible in the manner of priority as described in the above General Provisions.

Tax Revenue Liability Fund. This reserve fund was established to continue normal operations in the aftermath of property tax revenue losses resulting from taxpayer appeals. Each year Kern County publishes a tax revenue liability estimate for the District's General Fund. Since it is unlikely that all taxpayer appeals will be granted, the District will fund this reserve at 50% of the County's estimate. The interim target shall be set at 50% of the full reserve target.

Emergency Fund. This reserve fund was established in 1986 to mitigate the fact that the District does not carry insurance coverage for earthquake or flood damage. Its purpose is to set aside money for (1) repair, restoration, or replacement of District facilities damaged as the result of natural disasters, (2) matching fund payments for cost sharing required under federal or state disaster assistance programs, and (3) District personnel overtime costs and supplies used during eligible disaster response and recovery activities, including the cost of administering those activities. It shall be the policy of this District to maintain working capital in this fund at 5% of the general fund's operating expenses. The interim reserve target shall be set at 50% of the full reserve target.

Major Repairs and Overhaul Fund. This reserve fund is for the purpose of major, unanticipated repairs, or replacement of the District's water importation system components. Of particular concern is the failure or replacement of one or more natural gas engines at one of the pump plants; however, the funds may be used for the unexpected replacement of other system components as well. It shall be the policy of this District to maintain working capital in this fund at 5% of the book value of the General Fund's capital assets. The interim reserve target shall be set at 50% of the full reserve target.

Rate Stabilization Fund. This reserve fund is used to normalize fluctuations in revenues so that water rates will be more stable over time. The moneys are used as a buffer to reduce the frequency of changes to the District's water rates, and also to satisfy pledges and revenue calculations pursuant to long-term financing rate covenants. The amount is intended to fluctuate between 1% and 5% of the General Fund's operating expenses. The interim reserve target shall be set at 50% of the full reserve target.

2. Capital

Equipment/Infrastructure – Replacement/Upgrade. This reserve fund was established and designated for future capital needs to fund the cost of both new and replacement projects as a part of the District's strategic planning. The fund was created with the approval of the FY 2019-2020 budget. The Strategic Plan document sets out a short-term (1-2 years), mid-term (3-5 years), and long-term (6-10 years) capital improvement plan. The current fiscal year capital improvement needs shall be funded from the General Fund and included in the annual budget process. The full reserve target shall be equal to 20% of the mid-term capital improvement plan. The interim target shall be set at 50% of the full reserve target. Any water rate revenues greater than debt service obligations and the cost of natural gas shall be designated for transfer to this fund annually. The designated purpose of this fund may be changed or made available for borrowing when deemed necessary in **emergency** situations resulting from extreme, unforeseen, or unexpected circumstances. Any expenditure or transfer from this fund will be replaced as quickly as possible to ensure funding stability.

The District has attained its goal of 90 days working capital in the General Fund and intends to maintain this minimum funding level in perpetuity. As of June 30, 2024, all four (4) of the Designated Liquidity reserve funds' targets are fully funded. The Designated Capital reserve fund's interim target is funded. The budget for the current fiscal year shows that costs will be controlled, and sufficient revenues will be generated such that all

Designated reserve funds will continue to be funded in accordance with this policy to meet the targets and manner of priority set out in the General Provisions.

E. RESTRICTED RESERVES

The District maintains five (5) Restricted Reserve Funds:

State Payment Fund. This reserve fund is for the purpose of paying the obligations of the Kern County Water Agency contracts for State Water Project costs. The District levies a special **ad-valorem** tax sufficient to cover all current costs under its two water supply contracts. The reserve balance is maintained at a level sufficient to cover six-months' of operating expense obligations and one-half (1/2) of the Fund's **tax revenue liability** as determined by the Kern County Auditor-Controller. All unspent moneys in this fund remain in the fund.

Improvement District No. 2. This reserve fund is maintained for the purpose of providing flood control within the discrete area known as ID2. Property within ID2 is subject to property taxes to fund this service. All unspent moneys in this fund remain in the fund for future maintenance and replacement of its flood control facilities. The District sets a reserve target for this fund at 50% of the estimated replacement cost of the facilities. The estimated replacement cost is calculated as the original construction cost adjusted for inflation.

Improvement District No. 3. This reserve fund is maintained for the purpose of providing flood control within the discrete area known as ID3. Property within ID3 is subject to property taxes to fund this service. All unspent moneys in this fund remain in the fund for future maintenance and replacement of its flood control facilities. The District sets a reserve target for this fund at 50% of the estimated replacement cost of the facilities. The estimated replacement cost is calculated as the original construction cost adjusted for inflation.

Benefit Assessment District No. 1. This reserve fund is maintained for the purpose of providing flood control within the discrete area known as AD1. Property within AD1 is subject to a special benefit assessment to fund this service. All unspent moneys in this fund remain in the fund for future maintenance and replacement of its flood control facilities. The District sets a reserve target for this fund at 50% of the estimated replacement cost of the facilities. The estimated replacement cost is calculated as the original construction cost adjusted for inflation.

Engine Project Fund. The purpose of this reserve fund is for tracking all costs and reimbursements related to the 2023 Revenue Certificates of Participation (COP) that the District issued in June of 2023 for \$10,925,000 to finance certain capital improvements to the District's water system. The reserve balance will be maintained to reflect the unspent COP proceeds.

Reserve targets for the three (3) flood control districts (i.e., ID2, ID3, and AD1) are not fully funded and are not anticipated to be so for quite some time. Ideally, these reserves should be adequate to repair or replace structures damaged in a flood event. Flood control assets tend to stay in place for long periods of time and function without damage under normal conditions. However, they can be damaged or destroyed by natural disaster events requiring rebuilding. Some funds may become available from federal or state agencies in a declared disaster event, but it is possible that facilities could be damaged in a localized flood event that is not part of a declared disaster.

In the event of a declared disaster, it is likely that FEMA and CalEMA would provide funding assistance to the District to rebuild the flood control facilities. Under this scenario, the District's reserves would be used for matching funds (typically 10-20% of total cost) to secure the disaster assistance funds.

F. MANAGEMENT OF RESERVE FUNDS

Reserve fund balances will be reviewed, at a minimum, on an annual basis to ensure compliance with this policy. The General Manager will be responsible for managing the accumulation of reserves in the various funds in accordance with Board policy. Only the Board shall approve any reallocation of funds or any transfers between reserve funds. The Board will work collaboratively with the General Manager to ensure the accuracy of the annual report and evaluate the goals and purposes of each reserve fund and adopt policy changes as may be necessary or desirable.

The minimum levels established for each reserve fund represent the baseline financial condition that is acceptable to TCCWD from risk and long-term financial planning perspectives. Maintaining reserve funds at appropriate levels is a prudent, ongoing business process that consists of an iterative, dynamic assessment and application of various revenue generating alternatives. These alternatives (either alone or in combination with each other) include but are not limited to: fees and charges, energy usage, capital financing, investment of surplus funds, and levels of capital expenditures.