



EAST VALLEY WATER DISTRICT Administrative Policies & Programs

Policy Title: Reserve Funds Policy

**Original Approval Date:
August 10, 2010**

**Last Revised:
February 28, 2024**

**Policy
No: 7.2**

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Purpose

It is the purpose of East Valley Water District Reserve Policy to ensure that 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. East Valley Water District (District) will always strive to have sufficient funding available to meet its operating, capital, and debt service obligations. Reserve Funds (Reserves) will be accumulated and maintained to allow the District to fund expenditures in a manner consistent with the District's Capital Improvement Plan while avoiding undue pressure on District operations.

The Board of Directors (Board) may designate specific Reserve Funds and maintain minimum reserve balances consistent with statutory obligations that it has determined to be in the best interest of the District. The Policy directives outlined in this document are intended to ensure the District has sufficient reserves to meet current and future needs. The Board will annually review the level of Reserves.

General Provisions

The District has established and will maintain the following primary reserves and their respective sub-accounts:

- Legally Restricted Reserves – comprised of Debt Proceeds and Customer and Developer Deposits.
- Capital Reserves – includes the Capital Replacement Reserves and Emergency Reserves.
- Operating Reserves

The District will maintain its operating and capital reserves in designated sub-accounts in a manner that ensures their financial soundness and provides transparency to its ratepayers. The Reserve balances are considered the minimum necessary to maintain the District's credit worthiness and adequately provide for:

- Compliance with applicable statutory requirements.
- Financing of future capital facilities and repair and replacement of existing assets.



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- Cash flow requirements.
- Economic uncertainties, local disasters, and other financial hardships or downturns in the local or national economy.
- Contingencies or unforeseen operating or capital needs.

In the context of funding future capital facilities and maintaining and replacing existing assets, in each instance, the District will analyze the benefits and tradeoffs of utilizing pay-as-you-go and/or debt financing and determine the optimal funding strategy or combination of funding strategies. The analysis should consider the District's current and projected liquidity and capital positions, as well as the impact of inflation and other factors on the operations of the District and its capital improvement program.

Through a variety of policy documents and plans, including East Valley's Capital Improvement Plan, Water and Sewer System Master Plans, Strategic Plan, and Five-Year Financial Plan, the Board has set forth several long-term goals for the District. A fundamental purpose of these documents is to link what must be accomplished with the necessary resources to successfully do so. Among the resources which may be considered are the District's Reserves.

A principal tenet of the District's Reserve Funds Policy shall be the crediting of interest income to specific reserves until the respective reserve maximum is achieved. Once the maximum balance is reached within a specific Reserve, the surplus interest earnings will be reallocated to other Reserves whose funding level is below the minimum or maximum requirement recommended by this Policy.

Reserve balances will be reviewed on an annual basis at, or near, the end of the fiscal year to ensure compliance with this Policy. In the event the Operating Reserve balance exceeds the established maximum, excess monies will be transferred annually into the Capital Replacement Reserves. On an as-needed basis, monies from Capital Replacement Reserves can be moved to pay for operating emergencies to supplement Operating Reserves. In addition, if the Capital Replacement Reserve balance exceeds the established maximum, the Board will make a determination regarding the reallocation of excess monies.

The minimum established for each Reserve represents the baseline financial condition that is acceptable to the District from risk and long-range financial planning perspectives. Maintaining Reserves at appropriate levels is a prudent, ongoing business process that



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consists of an 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, water usage, capital financing, investment of funds, and levels of capital expenditures.

To achieve and maintain a strong credit rating, in every fiscal year the District will strive to maintain unrestricted cash and designated reserve balances totaling a minimum of 120 days of budgeted operating expenses. Should the District determine to target a higher credit rating level, this minimum will be adjusted accordingly. However, should the District decide to pursue a credit rating upgrade, it will need to analyze carefully under what circumstances and in what timeframes it will be optimal to achieve this goal.

The Board shall approve any reallocation of reserves or any transfers among Reserves.

LEGALLY RESTRICTED RESERVES

A. Debt Proceeds – Debt proceeds funds are monies derived from the proceeds of a bond issue. Typically, they consist of construction fund monies, and a debt service reserve fund (DSRF). The use of these proceeds is restricted by conditions set forth in the respective legal debt documents. These funds may be held by a Trustee in favor of bond holders, if applicable.

1. Target Level – The debt service reserve requirement is established at the time of the bond issue or execution of debt agreements. This amount may be recalculated as the debt is paid down. Any excess principal and/or interest earnings can be used to pay debt service on the bonds.
2. Events or Conditions Prompting the Use of the Reserves – As stipulated in the respective debt documents. Construction fund monies are expected to be spent on applicable projects, while DSRF can only be used in the event of a shortfall in revenues to pay debt service or to pay down principal at maturity.
3. Periodic Review Dates for Balances – Reviewed by the Trustee on a semi-annual basis (i.e., every interest and/or principal payment date).



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- B. Customer Deposits and Construction Advances – Monies held on behalf of District customers as required for their utility account or as cash bonds for development projects.
1. Target Level – Customer deposits, and deposit requirements for development projects, are outlined in District Ordinances and Schedule of Water and Sewer Rates and Charges. The balance in these accounts will fluctuate depending on the number of utility customer deposits required and the number of development projects in process. Therefore, no minimum or maximum levels will be established.
 2. Events or Conditions Prompting Use of the Reserves – As deposits on utility accounts are released, they will be refunded to the customer. When development projects are complete, the projects will be closed, and a final accounting will be completed. Excess deposit monies will be returned to the development customer.
 3. Periodic Review Dates for Balances – Reviewed by staff on a regular basis as part of the monthly closing process.

CAPITAL REPLACEMENT RESERVE

The District will strive to maintain the minimum balances as defined for each of the reserves listed below:

- A. Replacement Reserve – All divisions will maintain a replacement reserves for the replacement of capitalized assets when they reach the end of their useful lives. The source of replacement reserves will be user fee revenue from the respective enterprises.
1. Target Level – The District may set aside replacement reserves on a project-by-project basis. The minimum target level should be equal to twice the five-year average of the District’s annual Capital Improvement Plan budget. The maximum balance in Capital Replacement Reserves shall not exceed the projected needs for five years according to the District’s Capital Improvement Plan.
 2. Events or Conditions Prompting the Use of the Reserve – Staff will recommend assets to be replaced during the Capital Improvement Plan / Capital Budget



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presentation. As projects are approved, reserves will be appropriated from undesignated reserves or available revenues.

3. Periodic Review Dates for Balances – Reserve balances and projected improvement projects will be reviewed by staff and the Board during the preparation and approval of the annual budget.

B. Emergency Reserve – The Emergency Reserve may be used to begin repair of the water and sewer systems after a catastrophic event or other unforeseen circumstances.

1. Target Level – The minimum target for this reserve is one (1%) percent of the total value of plant and equipment while striving to achieve a two (2%) percent target.

2. Events or Conditions Prompting the Use of the Reserves – The Board may designate use of this reserve after establishing that conditions exist as called out in the definition and purpose of the reserve.

3. Periodic Review Dates for Balances – Reserve balances and target levels will be reviewed by staff and the Board during the preparation and approval of the annual budget.

OPERATING RESERVES

A. Operating Reserve – The Operating Reserve is used for unanticipated operating expenses. This reserve is designated by the Board to maintain working capital for current operations and to meet routine cash flow needs.

1. Target Level – Funding shall be targeted at a minimum amount equal to 90 days of the District's budgeted total operating expenses, and the maximum amount shall not exceed 120 days of the budgeted total operating expenses.

2. Events or Conditions Prompting Use of the Reserve – This reserve may be routinely utilized by staff to cover temporary cash flow deficiencies caused by timing differences between revenue and expenses and extraordinary decreases in revenues and unexpected increases in expenses.



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3. Periodic Review Dates for Balances – Reserve balances and target level will be reviewed by staff and the Board during the preparation and approval of the annual budget.

Investment Guidelines

It has been the District's practice to rely primarily on a pay-as-you-go (pay-go) strategy to fund capital improvements and replacement of existing assets. However, maintaining a balance between debt and pay-go sources may provide an added benefit to the District in terms of allowing for a more optimal investment strategy. In the context of these policies and in circumstances where such balance is present, the investment portfolio can be separated into short and long portfolios to maximize investment returns. The balance in the Operating Reserves should be kept in short-term investments. Monies in the Capital Reserves, however, may be invested for a longer horizon as the reserves are needed in later years.

Delegation of Authority

The Board has sole authority to amend or revise the Reserve Funds Policy. Through approval of this Policy, the Board has established written procedures for staff to follow in the management of East Valley Water District's Funds.