



SAN MIGUEL COMMUNITY SERVICES DISTRICT

“STRATEGIC FINANCIAL and CAPITALIZATION POLICIES”

Key objectives of these policies are to list practices/concepts that foster, preserve and protect the District’s fiscal stability and sustainability.

The following policies are hereby established by the Board of Directors to:

- (1) provide adequate funding to meet the District's short-term and long-term plans,
- (2) provide funds for unforeseen expenditures related to emergencies such as natural disasters or man-made events,
- (3) strengthen the District’s financial stability against present/future uncertainties such as economic downturns and revenue shortfalls,
- (4) maintain an investment-grade bond rating, and
- (5) meet GASB 34 and 54 requirements.

A. CAPITAL RESERVE/REPLACEMENT FUND

Purpose:

For future replacement of existing facilities, major equipment and depreciable assets as well as handling unanticipated major repairs during an asset's life cycle.

Money placed into Replacement Funds shall be restricted for replacing capital assets and the cost of repairing vulnerable parts of our systems that are costly to replace, and/or could cause the greatest disruption of services.

Target: - Assets over \$5,000 are depreciated on a straight line basis over an estimated useful life of each piece of equipment, vehicle or facility.

The District shall annually contribute into Replacement Funds an amount equal to 100% of the total depreciation of the District's assets belonging to that fund. Funded replacement amounts will be based on depreciation costs from the most recent previous closed fiscal year.

For example: the FY 2016-17 budget amounts will be based from the 2014-15 depreciation schedule costs.

Each Operating Fund shall maintain its own Replacement Fund which will also earn its own share of interest allocation. This will require a re-structuring of the existing bank account for Capital

Reserves. Reserve/Replacement fund levels will be calculated, over any 5-year period, as follows:

Until such time as the Reserve/Replacement Fund balance has reached 65% of the accumulated depreciation for that fund, contributions will be 100% of the prior fiscal year net revenues.

When the fund balance reaches 65% of the accumulated depreciation for that fund then that fund may reduce its contribution to 75%.

When the Reserve/Replacement Fund balance reaches 100% of the accumulated depreciation for that fund then that fund may reduce its contribution to 50%.

When the Fund balance reaches 110% of the accumulated depreciation for that fund then that fund may reduce its contribution to 25%.

When the Fund balance reaches 125% of the accumulated depreciation for that fund then that fund may reduce its contribution to zero.

For example, the Water Department Fund has a 2014-15 Reserve/Replacement Fund balance of \$663,143 in cash and cash equivalents, and accumulated depreciation of \$1,617,434, making the Reserve/Replacement Fund currently funded at 40%.

Since this falls below the 75% target mark, the Water Fund must contribute 100% of its prior FY net revenues to its Reserve/Replacement fund. For the FY 2016-17 budget the funded replacement amount would be based on the 2014-15 Financial Audit accumulated depreciation costs.

EXCEPTION: The Board may approve, at its discretion, a budget that does not fully contribute per the above policies, should the Board find that there is a higher priority need for the funding for specific operating and maintenance needs within one or more given funds in a given fiscal year.

B. CAPITALIZATION POLICY

District assets will be capitalized as follows:

- 1) All land will be capitalized regardless of cost.
- 2) All other assets must cost \$5,000 or more and has a useful life of two or more years.
- 3) The capitalization threshold is applied to individual units of capital assets rather than groups. For example, ten desks purchased for \$1,000 each will not be capitalized even though the total (\$10,000) exceeds the threshold of \$5,000.

Repairs or improvements to existing capital assets will generally not be subject to capitalization unless the repair exceeds \$5,000 and extends the useful life of the asset.

Recommended Asset Life or Lives

The District shall follow GFOA Recommended Practices when establishing recommended lives for capitalized or able to be capitalized assets. If the life of a particular asset is estimated to be different than these guidelines, it may be changed with Board consent.

Summary of the estimated useful lives:

<u>Asset Class</u>	<u>Useful Life</u>
Buildings	40 Years
Collection Facilities- (wastewater, lines & lift stations)	20-50 Years
Equipment	5-10 Years
Furnishings	10 Years
Land	Not depreciable
Land Improvements	15-40 Years
Office Equipment	5 Years
Transmissions & Distributions (Water lines, pump stations & tanks)	20-50 Years
Vehicles	5-10 Years
Wells	25 Years

Proceeds from assets sold and declared as surplus will be booked into that fund's Replacement Fund. New assets are not eligible for the use of these funds, only replacement assets qualify.

Unless a specific exception is approved by the Board, no more than 50% of the Replacement Fund shall be used in any given year.

EXCEPTION: The Board may approve, at its discretion, a budget that does not fully contribute per the above policies, should the Board find that there is a higher priority need for the funding for specific operating and maintenance needs within one or more given funds in a given fiscal year.

C. CASH RESERVES

Cash Reserves may be used for cash flow purposes, economic uncertainties and financial hardship; Local disaster or catastrophic events; Insuring against significant revenue losses; future capital obligations; Unfunded mandates; and/or to establish or maintain credit worthiness.

District will maintain multiple types of cash reserves to minimize adverse annual budgetary impacts from anticipated and unexpected District expenses. Minimum and Maximum reserve balances will be periodically reviewed by the Board and will be based upon that current fiscal year's expenditures.

1) Operating Reserves

Purpose is to: ensure cash resources are available to fund daily administration operations and maintenance of providing water, waste water, solid waste, street lights, fire protection services and mitigate year-to-year fluctuations in revenues and expenses.

The funds may also be used to offset revenue shortage due to economic hardships, changes in energy cost, prolonged drought conditions and/or unforeseen major expenses as may be determined by the Board of Directors.

Target: District reserves shall be maintained in a liquid account with a 25% balance of that years budgeted expenditures in cash reserves in each operating fund budget. The District is required to have sufficient cash flow liquidity to meet the next six months of budgeted District Expenditures. Cash reserves coupled with available balances in capital and replacement funds will ensure compliance with Government Code 53646b)(3).

2) Debt Service Reserve

Purpose: helps ensure timely loan re-payments can be made even if there is a financial emergency within the District. Money placed in Debt Service Fund shall be restricted for the payment of a bond/loan and interest thereon.

Target: equivalent to 1 year of debt service (USDA loan for reservoir tank). In our case, this reserve should be set at \$67,000 in reserve. The existing bank account will be renamed to fit this purpose and function as a means to track for accountability and auditing.

D DEBT ISSUANCE

This policy establishes parameters for evaluating, issuing and managing the District's debt and may be used as a guideline to promote sound financial management.

The District objective in issuing debt will be to:

- (1) Achieve the lowest cost of capital

- (2) Ensure rate payers equity
- (3) Maintain high credit rating and gain access to credit enhancement
- (4) Preserve financial flexibility.

Prior to the new debt issuance, the District shall hold a public hearing to outline the debt to be financed. This requirement shall not apply to the refinancing of existing debt.

Standards for use of Debt Financing – The District, when appropriate, will use long-term debt financing to:

- achieve an equitable allocation of capital costs/charges between current and future system users;
- provide more manageable rates in the near and medium terms; and
- minimize rate volatility.

Financing Criteria - Each debt issuance should be evaluated on an individual basis within the framework of a District long range financing plan, as well as within the context of the District's overall financing objectives and current market conditions.

Refinancing outstanding Debt - The District shall have the responsibility to evaluate potential refunding opportunities presented by underwriting and/or financial advisory firms. The District follows the GFOA (Government Finance Officers Association) guidelines of 3-5% savings for determining refinancing appropriateness.

Method of issuance - The District will determine on a case-by-case basis, whether to sell its bonds competitively or through negotiation.

E CAPITAL FEES/OBLIGATION FOR NEW DEVELOPMENT

Purpose: to provide funds for orderly and timely expansion of the District facilities to meet future demand and maintain the District's existing level of service. The resources will be spent on projects which expand the District facilities, or for major capital projects.

Target: The District will strive for new development to cover its costs through a mitigation fee program. Capital impact fees/ Connection fees will be evaluated annually and updated as necessary. The District's Master Plans shall be evaluated every 5 years to ensure the mitigation fee programs are designed to fund the necessary projects.

F. BUDGET CONTROLS

The approved annual operating budget is a planning and program execution tool. It consists of Board approved revenue estimates and expenditure recommendations to carry out the mission of the District.

Departmental fund budgets are established in the annual budget and approved by the Board of Directors, and then managed and controlled under the overall supervision of the General Manager. The Board of Directors may transfer funds from reserves or approved budget amendments to departmental funds as deemed appropriate during the fiscal year.

Department heads with General Manager approval may transfer funds between line items within the same fund without approval from the Board as long as the overall funds budget amount does not increase. Any approved transfer of funds between line items will be reported in that month's Monthly Financial Reports.

The budget shall include a long range economic outlook discussion and trends of revenues and expenditures by fund. This fiscal outlook shall include a discussion of any potentially needed revenue rate adjustments by fund.

G RETIREE OPEB (OTHER POST EMPLOYEE BENEFITS) FUND

Purpose: Per GASB 74 the District must report Postemployment Benefits on its financial statements. Currently the District is "pay as you go" meaning it pays retiree health Insurance each month as it is due.

Target: The District shall select an OPEB investment tool by January 2017. The District will continue to pay retiree health insurance as "pay as you go" and continue to invest into an OPEB investment program until such time the account is 100% funded.

The District's OPEB cost is calculated based on the annual required contribution (ARC) of the District, an amount actuarially determined every three years. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and to amortize any unfunded actuarial liabilities over a period not to exceed thirty (30) years.

As of June 30, 2015 the current OPEB liability, an estimated \$180,000 for the District is distributed as follows:

Water Fund-	\$72,000
Wastewater Fund-	\$72,000
Solid Waste Fund-	\$26,207
Administration Fund-	\$0
Fire Fund-	\$29,700
Lighting Fund-	\$5,400

For example, the Water Fund could contribute: \$7,200 each Fiscal Year for ten (10) years. This example is based off of the 2013-14 actuarial analysis. Every three years when the actuarial is recomputed and completed by CalPERS, this contribution may rise or decrease based on actuarial computations by CalPERS.

The District could determine to fully fund the OPEB liability with an unrestricted fund contribution. The District may, in the alternative, fully contribute that funds for a portion of OPEB liability in the 2017/2018 fiscal year. Thus, future year contributions may not be required. (Future actuarial valuation will determine if future contributions are needed).

For funds that cannot make a full contribution, the annual budget could include OPEB costs following the breakdown listed above.

The Board may approve, at its discretion, a budget that does not fully contribute per the above policies, should the Board find that there is a higher priority need for the funding for specific operating and maintenance needs within one or more given funds or within a given fiscal year.

H. FACILITY RENTAL AND DEVELOPMENT DEPOSITS FUND

A Facility Rental and Developmental Deposit Fund shall be established with monies held on behalf of customers who:

1. rent District buildings,
2. require fire hydrant meter rentals/deposits,
3. are required to install a mainline extensions or post a cash bond(s), if required by District policy or ordinance, for development projects.

As deposits are released, they will be refunded to the customer. Mainline extensions and development projects on a monthly basis will be reconciled to reflect staff time as well as any invoices that have been charged against that particular project. If additional amounts are owed, the development customer will be invoiced. Once a project is finished it will be closed and a final accounting will be completed.

Excess deposit monies will be returned to the development customer. These deposit amounts would be found under the balance sheet section of the Monthly Financial Reports under deposits. These deposit monies are not used for District O & M purposes.

I. COMPONENTS OF FUND BALANCE

The District will report fund balance in accordance with GASB 54. The following five components will be used.

- 1) Non-Spendable Fund Balance-Fund Balance amounts set aside for items that do not represent available, spendable resources such as loan receivables and inventories.
- 2) Restricted Fund Balance- defined as Fund Balance amounts that have external restrictions imposed by creditors, grantors, contributors, laws, regulations or enabling legislation which requires the funds to be used only for specific purposes.
- 3) Committed Fund Balance- defined as Fund Balance amounts having a constraint imposed by formal Board action of the Board: Once adopted, the limitation imposed by the Ordinance/Resolution remains in place until a similar action is taken (the adoption of another ordinance) to remove or reverse the limitation.
- 4) Assigned Fund Balance- defined as Fund Balance amounts that are constrained by the District's intent to be used for a specific purpose but are either restricted or committed.

5) Unassigned Fund Balance- Represents residual amounts that have not been restricted, committed.

J. PURCHASING POLICY

The District has an adopted Purchasing Policy. These policies shall be reviewed no less than every three years. The first 3-year review of existing Purchasing Policy as adopted by the Board will be in 2017.

K. FINANCIAL REPORTING

The following reports are distributed by the General Manager:

- The annual audited financial statements ending June 30th.
- The Monthly Financial Reports-Includes Statement of Operating Cash and Investments, Summary of Reserve and Restricted Capital, Summary of Active Capital Project Budgets and Expenses, Statement of Claims for Payment, Statement of Revenues, Statement of Expenses, Monthly and YTD Budget Report and content of any approved budget amendments submitted and approved by Board action. These reports are submitted for Finance & Budget Committee review at its scheduled monthly meeting after the close of each month and to the Board of Directors each month.
- Monthly Budget to Actual Reports are distributed to operations and maintenance departments.
- District complies with all deadlines for State Controllers Report and State Compensation Reports.