

RESOLUTION NO. 12-732

A RESOLUTION OF THE BOARD OF DIRECTORS OF THE GOLETA WEST SANITARY DISTRICT REVISING THE DISTRICT'S RESERVE FUND POLICY

Recitals

A. On November 18, 2003, the Board of Directors adopted Resolution No. 674 establishing a District policy with respect to its reserve funds. On April 7, 2009, the Board of Directors adopted Resolution No. 09-717 which entirely replaced Res. No. 674 and adopted certain amendments to the Reserve Fund Policy recommended by the District's financial consultant, Raftelis Financial Consultants ("Raftelis").

B. The Board of Directors has received a report from Raftelis dated May 8, 2012 (2012 Raftelis Report) which recommends certain changes to the District's reserve fund policy (copy attached as Exhibit A).

C. The Board of Directors has determined to adopt those recommendations.

D. By adoption of this Resolution, the Board intends to entirely replace Resolution No. 09-717.

NOW, THEREFORE THE BOARD OF DIRECTORS OF GOLETA WEST SANITARY DISTRICT DOES RESOLVE AS FOLLOWS.

Section 1. Created. The reserve funds set forth in Sections 3 and 4 are hereby created. The General Manager shall establish and maintain those Reserve Funds in accordance with this policy. All dollar amounts indicated are 2012 dollars.

Section 2. Utilization. The reserve funds so created will be utilized for the specific purposes set forth in this Resolution.

Section 3. Funds.

A. Operations Reserve Fund No. 4930

Purpose: Operations reserves shall be used to meet ongoing cash flow requirements as well as unanticipated increases in operating costs. These funds shall also be used to ensure sufficient funding for District purposes in the event of an unanticipated increase in Operations costs, such as those caused by large unexpected fluctuations in energy costs, or reduction in wastewater revenues. Unrestricted reserve funds may be used for any proper district purpose.

Funding: The Operations Reserve Fund shall be funded by income from sources other than property tax. This fund should maintain a minimum balance of one hundred percent (100 %) of annual operating costs. In addition, this fund includes any excess revenues that are

part of the unrestricted reserve funds. The District will seek to achieve the Operations Reserve Fund target levels as recommended in the 2012 Raftelis Report, Figure 1.

B. Restricted Reserve Funds

The following reserve funds are restricted pursuant to state and/or federal law.

(1) Collection System/Plant Upgrade Reserve Fund No. 4932

Purpose: This is an encumbered reserve fund for capital costs related to increasing system capacity or capital improvements. This fund may be used to finance the expansion or upgrade of existing facilities that will benefit customers that have paid fees to the fund.

Funding: Pursuant to Government Code §66000 *et seq.*, the fees collected by the District and deposited into this fund are accounted for separately and are used for the specific purposes authorized by law. This fund is funded by capacity charges, developer fees and interest earned thereon. All interest earned on monies contained in this fund shall remain in the fund. The District anticipates that it will complete several large capital projects over the next six years, including trunk line pipeline upgrades (13.2 million).

(2) Capital and Treatment Plant Reserve Fund No. 4935

Purpose: The Capital and Treatment Plant Reserve Fund may be used to replace, upgrade and improve the existing system. This fund is designated for ongoing needs for financing capital projects and the replacement and upgrade of the existing treatment plant facilities. Interest earned on this fund may be used for operations.

Funding: This reserve fund shall be funded with property taxes. The 2012 Raftelis Report indicates that the Goleta Sanitary District plant upgrade project will require \$15.5 million over the next few years from this fund and an additional \$776,700 in capital expenditures over the next nine years. The 2012 Raftelis Report sets forth in Figure 2 the target funding levels for Fund No. 4932 and 4935 (combined).

C. Additional Reserve Funds. The following restricted funds for specified capital projects may include debt reserves that are required by the covenants of bonds sold and reserves for specific projects to be used only for those projects. Interest from these accounts may be used for operations so long as adequate reserves are maintained to fund the project for which the fund is set aside. The reserve funds should maintain the following recommended balances:

(1) Property Tax Reserve Fund No. 4910

Purpose: To fund the street sweeping operations and to replenish the capital upgrades and replacement reserve funds.

Funding: All property tax monies collected during the current fiscal year and any accrued interest

(2) Equipment/Vehicle Replacement Reserve Fund No. 4960

Purpose: To fund replacement of District sewer cleaning and street sweeping equipment and other vehicles at the end of their life cycle.

Funding: \$640,000 (accumulated annually).

(3) Building Replacement Reserve Fund No. 4965

Purpose: To fund upgrade of existing administration building.

Funding: \$2 million (accumulated annually).

Section 4. Repeal. By this resolution, Resolution No. 09-717 is repealed.

THE FOREGOING RESOLUTION was adopted at the regular meeting of the District Board of Directors held on the 15th day of March, 2012 by the following vote:

AYES:	Bearman, Geyer, Lewis, Meyer, Turenchalk
NOES:	None
ABSENT:	None
ABSTAIN:	None



Diane Powers, Secretary

ATTEST:

(SEAL)



Larry Meyer, President



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Memo

To: Mark Nation
General Manager/Superintendent
Goleta West Sanitary District
P.O. Box 4
Goleta, CA 93116-0004

From: Sudhir Pardiwala/Khanh Phan

Date: May 8, 2012

Re: Goleta West Sanitary District 2012 Reserve Policy Update Memo

1. Introduction

Goleta West Sanitary District (District or GWSD) engaged Raftelis Financial Consultants, Inc. (RFC) to update its reserve policy based on new financial information and the “2011 Capital Improvement Plan Update” completed by CDM in April 2011 (CDM Report). This memorandum (Memo) summarizes RFC’s findings and recommendations on the District’s reserve policy in response to recent changes to its financial condition.

Major changes have occurred since the last reserve policy was established (GWSD Resolution 09-717); these are as follows:

1. **Intensive Capital Improvement Program.** In the next 6 years (from FY 2012 to FY 2017), GWSD will have several large capital projects to be completed including the upgrade of Goleta Sanitary District (GSD) Wastewater Treatment Plant (WWTP) (~\$15.5 million) and the trunk line pipeline upgrades (~\$13.2 million – un-inflated). These projects will completely deplete the current reserves of \$27.5 million. The

Devereux Creek Project is completed, thus the associated dedicated reserve 4933 is no longer needed.

2. **Increased Capital Replacement & Refurbishment (R&R) Needs.** The upgraded GSD WWTP will start operation in 2014. It is estimated that annual R&R expenditures at the WWTP will increase to approximately \$400K by FY 2019 from less than \$100K in FY 2012. Long-term Collection System annual R&R program is projected to be approximately from \$350 to \$400K. The building and vehicle replacement costs have also significantly increased.
3. **Reducing Risk Management Capability.** After the GSD WWTP upgrade and the completion of other major CIP projects, the financial plan study (completed by RFC in 2011) indicates that the District’s reserves will be depleted and the District will be exposed to more financial risk.

2. Reserve Policy Review

Prudent financial management requires that reserves be established to meet working capital requirements, provide for capital expenses, risk management, emergency requirements and other needs.

At the end of FY 2010-11, the District had various reserves as shown in Table 1. Connection fee income is deposited in Fund 4932, Collection System and Plant Upgrade Reserve.

**Table 1:
Estimated Ending Balances of GWSD’s Reserves as of June 30, 2011 (FY 2010-11)**

Descriptions	Ending balances as of June 30, 2011
4900 – Running Expenses	\$ 1,100,000
4910 – Property Tax	\$ 1,700,000
4930 – Operating Reserves	\$ 2,130,000
4932 – Collection System and Plant Upgrade	\$ 610,000
4933 - Devereux Creek Project	\$ 2,490,000
4935 – Plant Replacement	\$ 17,350,000
4960 – Equipment and Vehicle Replacement	\$ 610,000
4965 – Building Replacement	\$ 1,475,000
Total	\$ 27,465,000

The current reserve policy is as follows:

1. **Operations Reserve Fund 4930:** 65% of operating budget to meet ongoing cash flows requirements as well as unexpected increases in operating costs.
2. **Collection System and Plant Upgrade Reserve Fund 4932:** \$7.78 million from connection fees is required for pipeline and manhole rehabilitation in the next 9 years.
3. **Devereux Creek Project Reserve Fund 4933:** The reserve is funded by Reserve 4932 and will be eliminated since the project is completed.
4. **Capital and Treatment Plant Upgrade Reserve Fund 4935:** The reserve is funded by property tax for replacement, upgrade and improvement of existing system. The current target is 100% of the 5-year annual rolling average projected capital expenditures.
5. **Property Tax Reserve Fund 4910:** to fund street sweeping operations and to replenish the Capital & Treatment Plant Upgrade Reserve Fund.
6. **Equipment / Vehicle Replacement Reserve Fund 4960:** to fund replacement of District sewer cleaning and street sweeping equipment and other vehicles at the end of their life cycle. The target level is \$640,000.
7. **Building Replacement Reserve Fund 4965:** to fund upgrade of existing administration building. Current target is \$1.5M.

3. RFC Recommendations

The District has historically funded capital expenditures from cash reserves. For the District to maintain a strong financial position and adequate reserves for future operations and capital expenditures, RFC recommends the following:

1. Increase Operations Reserve Fund 4930 target level to 100% of annual operating costs: Operations reserves are used to meet ongoing cash flow requirements as well as unanticipated increases in operating costs. Inflation has been low in recent years due to the economic recession. It is expected that it will pick up in the coming years;

it is recommended that a balance of at least 50% of the operating costs in the operations reserve to cover working capital needs and an additional 50% to cover unanticipated operating costs.



Figure 1: Operations Reserve Target Level

2. Eliminate Devereux Creek Project Reserve Fund 4933 as the project is completed in FY 2012. The remaining balance will be transferred to Collection System and Plant Upgrade Reserve Fund 4932.
3. Capital and Treatment Plant Upgrade Reserve 4935: One of the challenges of managing the wastewater system is to plan financial sufficiency for highly fluctuating and intensive capital expenditures. The average useful life of GWSD's capital assets is around 40 years. Pumping stations and other equipment has even shorter lives. To maintain adequate reserves for future R&R needs for its collection and treatment system, the District should start with 2.5% of its asset value as a target and gradually increase it to 5% over ten years based on replacement cost to cover future upgrade costs and for emergency purposes. Some agencies maintain between 5 and 10% of the system asset value in this reserve.

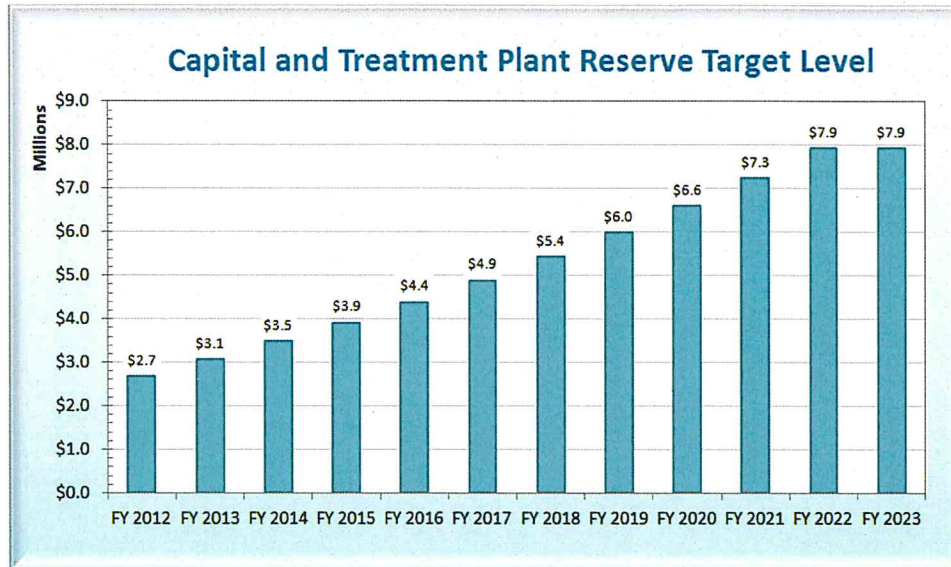


Figure 2: Capital and Treatment Plant Reserve Target Level

4. Increase target level for Building Replacement Reserve Fund 4965 to \$2M based on the 2012 CDM Report.
5. Maintain the current policies for other reserve funds: Collection System and Plant Upgrade Reserve Fund 4932, Property Tax Reserve Fund 4910 and Equipment / Vehicle Replacement Reserve Fund 4960.

The recommended target balances for all reserves are shown in the chart below.

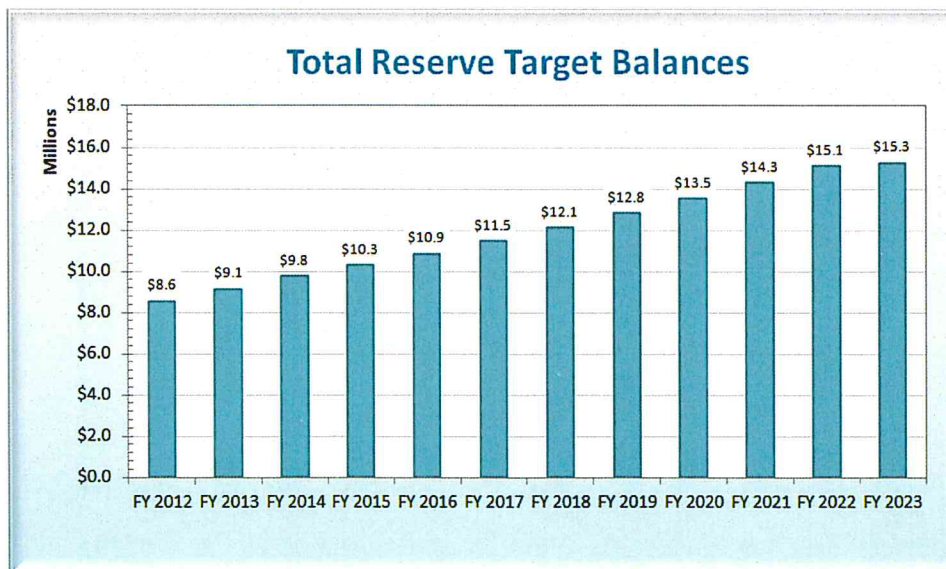


Figure 3: Total Reserve Target Balances

GWSD – Reserve Policy Update 2012

The financial plan model indicates that to sufficiently fund the reserve to the recommended target levels, the following revenue adjustments are required and the ending reserve balances are projected in the chart follows:

- FY 2013 – 36% (\$5.04 per month)
- FY 2014 to FY 2017 – 7% per year (\$1.33 to \$1.63 per month)
- No further increases are projected beyond FY 2017

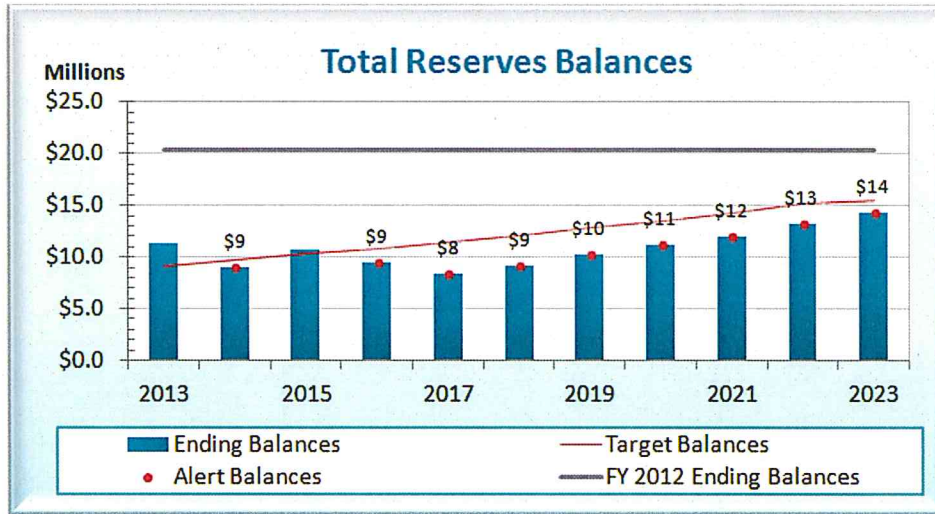


Figure 4: Total Reserve Balances under Proposed Revenue Adjustments