

# NOVATO SANITARY DISTRICT

March 8, 2013

The Finance Committee of Novato Sanitary District will hold a meeting at 10:00 AM, Friday, March 8, 2013, at the District offices, 500 Davidson Street, Novato.

## AGENDA

**1. AGENDA APPROVAL:**

**2. PUBLIC COMMENT (PLEASE OBSERVE A THREE-MINUTE TIME LIMIT):**

This item is to allow anyone present to comment on any subject not on the agenda, or to request consideration to place an item on a future agenda. Individuals will be limited to a three-minute presentation. No action will be taken by the Board at this time as a result of any public comments made.

**3. MINUTES**

- a. Consider approval of the minutes of the December 6, 2012 meeting.

**4. FINANCIAL POLICIES:**

- a. Review the Reserve Policy and consider the proposal from Bartle Wells to update the policy.

**5. RATE STRUCTURE:**

- a. Consider initiating review of the connection fee structure.

**6. PENSION AND OTHER POST-RETIREMENT BENEFIT LIABILITIES:**

- a. Review pension and other post-retirement benefit liabilities.

**7. ADJOURNMENT:**

***In compliance with the Americans with Disabilities Act, if you need special assistance to participate in this meeting, please contact the District at (415) 892-1694 at least 24 hours prior to the meeting. Notification prior to the meeting will enable the District to make reasonable accommodation to help ensure accessibility to this meeting.***

***Materials that are public records and that relate to an open session agenda item will be made available for public inspection at the District office, 500 Davidson Street, Novato, during normal business hours.***

December 6, 2012

The Finance Committee of Novato Sanitary District held a meeting at 10:37 a.m., Thursday, December 6, 2012, at the District office, 500 Davidson Street, Novato.

COMMITTEE MEMBERS PRESENT: Members William C. Long and Jean Mariani.

STAFF PRESENT: Manager-Engineer-Secretary Beverly B. James, Deputy Manager-Engineer Sandeep Karkal, Finance Officer Laura Creamer and Administrative Secretary Julie Swoboda.

No members of the public were present.

AGENDA APPROVAL: The agenda was approved as presented.

REVIEW OF MINUTES: The November 5, 2012 meeting minutes were approved as written.

FINANCIAL POLICIES:

- Consider adding Marin County Investment Pool to the preferred investments list. The Manager gave an overview of the Marin County Investment Pool, stating that it was rated AAA by Fitch in October 2010 and again in August 2012. She reported that the return on investment was 0.245% for September as compared to 0.348% for LAIF (Local Agency Investment Firm). The Manager stated that she spoke to Karen Shaw, Investment Officer for the pool, who indicated that the Pool is limited to long-term participation. The Manager stated that after consideration, she recommends the District not include the Marin County Investment Pool as an investment option. The Committee members agreed with Ms. James.

- Review and make recommendations to the Investment Policy which contains draft revisions. The Manager stated that the suggested edits to the Policy are intended to remove the procedures covered elsewhere and restrict this to a policy document consistent with CSDA recommendations.

The Manager reviewed the revisions to the Policy Handbook, Policy #3120: Investment of District Funds. Editing & grammatical changes were discussed and the Manager stated she would make the requested modifications before presenting the final Policy for Board approval at their regular December 10<sup>th</sup> Board meeting.

2011-12 AUDIT:

- Review Draft 2011-12 Audit and make recommendation to the Board on acceptance of the audit. The Manager stated that the Committee was provided a revised transmittal letter which highlighted the changes requested by the Committee at their meeting on

November 5<sup>th</sup>. She discussed the additions to the letter which were included as highlighted text and the Committee discussed further changes.

Member Long questioned the cost of replacing the District's sewer system lines, pumps, etc. The Manager replied that the District is predicting system replacement at 2% each year at a cost of approximately \$2 million per year. Member Long suggested that an addition be made to include the \$2 million per year cost for repairs/replacements. The Manager stated that those changes would be included.

Finance Officer Laura Creamer reviewed the changes to the Management's Discussion and Analysis (MD&A) letter. The Committee accepted and agreed upon the changes to the letter.

The Manager stated that once the final Audit is accepted, it will be posted to the District website.

ADJOURNMENT: The meeting was adjourned at 11:34 a.m.

Respectfully submitted,

Beverly B. James  
Secretary

Julie Swoboda, Recording

## NOVATO SANITARY DISTRICT

### MEMORANDUM

Date: March 8, 2013  
To: Board of Directors  
From: Finance Committee: Jean Mariani, William Long  
Subject: Reserve Policy

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#### **Current Reserve Policy**

The District adopted an Operating Reserve Fund Policy in October 2001. Tom Gaffney prepared the analysis and recommended reserve levels. A copy of the report is included as Attachment 1. A copy of the current Reserve Policy is included as Attachment 2.

In 2001, the operating reserve fund target was set at a fixed dollar amount equal to approximately half of the annual operating budget. This target has become increasingly out-of-date as the District's operating costs have increased over the past twelve years. The District has continued to follow the spirit of the policy by maintaining operating reserves of at least half of the annual operating budget but it would be better to formally set the target as a percent of budget so that it would stay current over time.

The 2001 Policy also set up four additional reserve funds with set dollar amounts:

- Service Charge Rate Stabilization Reserve
- Emergency Repair Reserve
- Self-insurance and Self Retention Reserve
- Vehicle Replacement Reserve

It is time to determine if maintaining separate reserve funds still is the best policy and, if so, what the appropriate targets are.

#### **CSDA Special District Reserve Policy Guidelines**

The California Special Districts Association first issued reserve policy guidelines in 2001 in response to the Little Hoover Commission. These guidelines have now been revised and updated include insights gained over the past ten years as well as changes in accounting guidelines. A copy of the newly revised guidelines is included as Attachment 3.

#### **Bartle Wells Proposal**

Tom Gaffney of Bartle Wells has submitted a proposal to review the District's reserve policy in light of the new CSDA guidelines, changes at the District, and new accounting guidelines and make recommendations for revising the policy. He proposes to do the

work on a time and materials basis for an amount not to exceed \$4,500. Since this amount is within the Manager-Engineer's authority it will not go to the Board for approval but the committee's input is requested. The Bartle Wells proposal is included as Attachment 4.



**BARTLE WELLS ASSOCIATES**  
INDEPENDENT PUBLIC FINANCE ADVISORS

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**TO:** Tom Selfridge, General Manager/District Engineer  
**FROM:** Tom Gaffney  
**DATE:** September 5, 2001  
**SUBJ:** Operating Fund Reserves

## **Introduction**

Bartle Wells Associates has been asked to evaluate Novato Sanitary District's (NSD or District) operating reserve fund for proper allocation to potential use. This report reviews operating revenues and expenses and the District's current sources of operating funds. The report also explains the purpose of the operating reserve, identifies reserve fund uses and quantifies the levels of a recommended operating reserve fund balance.

## **The District**

NSD provides wastewater collection, treatment, reclamation, and disposal for properties within the City of Novato and adjacent unincorporated areas in northern Marin County. Treatment is provided at two treatment plants operated by the District. Collection is provided for about 22,300 equivalent single family connections. During dry months, treated wastewater effluent is used to irrigate pasture land that is rented to ranch operators. In rainy months, the treated effluent is discharged to San Pablo Bay. The District also provides for the collection of garbage and trash in unincorporated areas and jointly supports recycling and hazardous waste programs with the city of Novato.

## **Finances**

The District maintains the following funds: operating fund, vehicle replacement fund, self-insurance fund, capital improvement fund, bond interest and redemption fund, and AB 939 Solid Waste program. This report is involved with review and recommendations for only the operating fund.

## **Operating Fund**

This fund is the source of ongoing cash flow for the District and all operating costs are paid from this fund. Normal practice is also to pay vehicle replacements and liability claims from the operating fund and then receive transfers back from the other funds during the year.

District operating revenues are derived from two principal sources: service charges and property taxes. Both of these main revenue sources are collected by the Marin County

tax collector in two equal installments due from property owners on December 10 and April 10 each year. Property taxes and service charges together account for about 84 percent of total operating revenues. Other District operating revenue sources include interest earnings, rentals from farm property, and various fees. Connection charges are another major revenue source. However, connection charge revenues are restricted for capital expenses serving future uses and are not available for operating expenses.

Table 1 shows estimated operating revenues and expenses for the past year and budgeted for the current year. Budgeted wastewater operating expenses average about \$377,000 per month. Note that the District budgeted a 2001/02 deficit of about \$370,000. The District intends to fund this deficit from District reserves.

The operating fund receives most of the District's revenues and pays most expenses. The fund basically serves as the main source of cash flow to fund the entire operations of the District. Expenses occur monthly and fairly evenly over the whole year. Over 84% of revenues, however, are collected by the Marin County tax collector. The District receives these revenues twice a year after the county collects them. This creates a need for the District to have operating reserves available until revenues are received from the county.

## **Operating Fund Balance**

Several needs for an operating fund reserve are identified.

- Operating cash flow
- Service charge rate stabilization
- Emergency repairs

Operating cash flow - The District needs to fund ongoing monthly operating expenses prior to receipt of the majority of its revenues from the Marin County tax collections. Tables 2 through 4 demonstrate the need for an operating reserve and quantifies the recommended amount.

Table 2 develops the average monthly wastewater expenses versus average monthly revenues other than property taxes and services charges. Wastewater expenses average about \$401,000 per month and non-tax collection revenues average just under \$34,000 monthly.

Table 3 shows the impact of uneven monthly revenues on wastewater cash flow. The District needs to fund the difference between monthly revenues and expenses. Assuming a zero beginning operating fund balance, the District would have a deficit of over \$2.2 million by December. Then the District would receive its first revenue installment. Revenues are assumed to be promptly received from the county in January after the December 10 property tax collections. Any delay by the county would further impact this deficit projection. The cumulative balance remains negative throughout the year because the District budget projects an annual deficit to be funded from reserves.

Table 4 calculates the minimum beginning balance in the operating reserve to eliminate a negative cumulative balance based on this year's budget. A beginning operating fund balance of about \$2.2 million is needed to fund District operations until the first installment is received from the county. This beginning reserve balance is drawn down to a zero balance by early January each year. It must be maintained by the District and is not available to fund other District expenses.

Service charge rate stabilization -This year's budget is an example of how use of a reserve fund can stabilize rates. The District is able to plan for most costs such as salaries and normal maintenance, utilities and other. However, last year after the District adopted a budget, unexpected cost increases were experienced in power purchases, liability claims, and permit fees and newly imposed mandatory fines due to SB 709. Much of these increases are likely to be permanent, so eventually the District will need to increase service charge revenues. However, the District was able to fund these increases this year by a draw down of reserves.

As an example, Table 5 shows a history of an expense that may increase unexpectedly. Liability claims averaged about \$10,000 to \$12,000 for a number of years. Last year these claims shot up to nearly \$100,000 mainly due to pressure from private companies to sell services for much expanded cleanup procedures. The operating fund paid the claims and then received a transfer from the self-insurance fund. But ultimately because of District policy, the operating fund is required to replenish the self-insurance fund.

A rate stabilization reserve is used to spread a permanent cost increase over a number of years or to fund one-time expenses without the need for a service charge adjustment. Such a reserve provides flexibility if unexpected costs occur beyond a budgeted amount.

Use of a rate stabilization reserve involves drawing on the reserve when needed and then eventually replacing the funds used. Otherwise funds won't be available to mitigate some future unexpected expense increase.

Table 6 shows an example of how a rate stabilization reserve would work. The example is based on \$350,000 of expense increases that are expected to be permanent. This amount is close to that experienced by NSD last year. A beginning balance of about \$600,000 is used to fund the full \$350,000 increase in expenses during the first year. This is realistic, because by definition, the expenses were unplanned. During the second year, a rate increase is enacted to cover part of the new expenses, say \$150,000 of the \$350,000 total. Two further increases in each of the next two years would enable the District to fully fund the new costs from revenues and begin to replenish the rate stabilization reserve.

In this example the District was able to spread rate increases over four years rather than a single sharp increase in the second year. The fund balance decreases for the first four years. Thereafter the fund balance increases. After eight years the rate stabilization reserve is back up to its original balance.

Emergency repairs – A sanitary district is by its very nature capital intensive. Such an agency requires a series of expensive public works facilities including pipelines, manholes, pump stations, and treatment structures and equipment. These facilities cost many millions of dollars and are subject to constant use under potentially hazardous conditions. In the event of a breakdown or equipment failure, the District is legally obligated to instigate repairs under emergency conditions if necessary. Under this condition, there is no time for financial planning. The repairs must be implemented and a permanent capital plan developed after the fact.

A source of emergency funding is required. For NSD capital funds are available, but these funds are mostly from accumulated connection charge revenues and are intended for capacity expansions rather than repairs. State law restricts the use of these funds. While short-term interfund borrowing is legal, an emergency repair reserve is an efficient and less painful method of funding emergency repairs.

An emergency repair reserve to fund a major general catastrophe such as one caused by an earthquake is not practical. Damage caused by this type of disaster could be widespread and would likely result in state and federal emergency assistance. In any event, an emergency reserve for a major catastrophe is beyond the scope of the District to provide.

The amount of an emergency repair fund may be determined in several ways. One method is to use the replacement cost of a key facility subject to a possible emergency breakdown and crucial to operations. A pump station is an example of a facility subject to flooding and one that must keep operating to avoid extensive sewage spills. Pump station equipment may cost upwards of \$500,000 to \$700,000.

Another method used to determine the magnitude of an emergency repair reserve is to use a percentage of the replacement cost of the District's facilities. The latest financial statement shows the book value of property plant and equipment of \$61.5 million. Replacement cost is at least double book value or about \$120 million. A rule of thumb used for emergency repairs is 1 to 3 percent of replacement value. This assumption generates an emergency repair reserve of \$1.2 to \$3.6 million.

This report recommends a emergency repair reserve of \$600,000. This amount is about equal to the cost of fully replacing a pump station in an emergency situation. In addition, for an emergency the \$600,000 available in the rate stabilization reserve could also be used to fund up to a combined \$1.2 million or about 1 percent of replacement costs.

A general philosophy for an emergency repair fund is to assume that the District prepares for one equipment emergency at a time. The District could use the fund to make the needed repairs and gain time to seek grants, disaster relief, or permanent funding.

## Recommendations

Based on our review of the requirements of the District, we recommend that the District establish a policy regarding a prudent amount to retain as an operating fund reserve. The following outlines the purpose and recommends an initial amount for the operating fund reserve.

The purpose of the operating fund reserve is to provide funds for working cash flow, service charge rate stabilization, and possible emergency repairs. The initial funding level would be established as follows:

Working cash flow -	\$2,200,000
Rate stabilization -	600,000
Emergency repair -	<u>600,000</u>
Total	3,400,000

- Working cash flow is equal to seven months of average operating expenses plus any budgeted operating deficit.
- Rate stabilization is designed to allow spreading unexpected but ongoing costs over four years or sufficient to fund a one-time expense of up to \$600,000.
- Emergency repair is based on the estimated emergency repair of a pump station or other major facility.
- If the reserve is used for any of these purposes then the District would develop a plan to replenish the fund balance to the recommended level.
- The District should review the reserve level about every 5 years.

Table 1  
 Novato Sanitary District  
 Budgeted Operating Revenues and Expenses

	Estimated 2000/01	Budget 2001/02
<b>Operating Revenues</b>		
Service charges	\$2,375,000	2,423,000
Property taxes	<u>1,246,000</u>	<u>1,308,000</u>
Subtotal collected with taxes	3,621,000	3,731,000
Plan check/inspection fees	19,000	36,000
Engineering/Administration Charges	60,000	75,000
Other revenues	36,000	25,000
Ranch income	83,000	83,000
Interest earnings	<u>215,000</u>	<u>185,000</u>
Subtotal - other wastewater revenues	413,000	404,000
County collection fee	27,000	28,000
Solid waste revenues	278,000	281,000
Total revenues	4,339,000	4,444,000
Other wastewater revenues/month	34,400	33,700
<b>Operating Expenses</b>		
Treatment plants, lab & monitoring	1,914,000	2,036,000
Reclamation/disposal facilities	304,000	330,000
Sewers and pump stations	583,000	663,000
AB 939 Solid waste program	201,000	291,000
Administration and engineering	<u>1,329,000</u>	<u>1,494,000</u>
Total expenses	4,331,000	4,814,000
Less: AB 939 Solid waste program	<u>201,000</u>	<u>291,000</u>
Wastewater expenses	4,130,000	4,523,000
Average monthly wastewater expenses	344,200	376,900
Budgeted surplus (deficit)*	8,000	-370,000

\* - Total revenues less Total expenses

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**Table 2**  
**Novato Sanitary District**  
**Monthly Service Charge & Property Tax Revenues (Final 2001/02 budget)**

	<b>Annual</b>	<b>Average Monthly</b>
Wastewater expenses	\$4,814,000	\$401,200
Non-tax collection revenues	404,000	33,700
Budgeted service charge & property tax revenue	3,731,000	n/a (1)

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1 - District receives service charge and property tax revenues in January and May.

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**Table 3**  
**Novato Sanitary District**  
**Example Cash Flow Requirement (1)**

Month	Average Non-Tax Roll Revenue (2)	Average Monthly Expense	Difference	Actual Service Chg & Property Tax Revenue	Cumulative Balance
July	\$33,700	\$401,200	-\$367,500		-\$367,500
August	33,700	401,200	-367,500		-735,000
September	33,700	401,200	-367,500		-1,102,500
October	33,700	401,200	-367,500		-1,470,000
November	33,700	401,200	-367,500		-1,837,500
December	33,700	401,200	-367,500		-2,205,000
January	33,700	401,200	-367,500	1,865,500	-707,000
February	33,700	401,200	-367,500		-1,074,500
March	33,700	401,200	-367,500		-1,442,000
April	33,700	401,200	-367,500		-1,809,500
May	33,700	401,200	-367,500	1,865,500	-311,500
June	<u>33,700</u>	<u>401,200</u>	<u>-367,500</u>		-679,000
Totals	404,400	4,814,400	-4,410,000	3,731,000	

1 - Based on FY 2000/01 Final Budget; Amount to balance operating fund cash flow.

2 - Revenues other than service charges and property taxes

**Table 4**  
**Novato Sanitary District**  
**Minimum Beginning Operating Fund Balance for 2001/02**

Month	Average Non-Tax Roll Revenue (1)	Average Monthly Expense	Difference	Budgeted Service Chg & Property Tax Revenue	Cumulative Balance
Minimum beginning balance					\$2,205,000
July	\$33,700	\$401,200	-\$367,500		1,837,500
August	33,700	401,200	-367,500		1,470,000
September	33,700	401,200	-367,500		1,102,500
October	33,700	401,200	-367,500		735,000
November	33,700	401,200	-367,500		367,500
December	33,700	401,200	-367,500		0
January	33,700	401,200	-367,500	1,865,500	1,498,000
February	33,700	401,200	-367,500		1,130,500
March	33,700	401,200	-367,500		763,000
April	33,700	401,200	-367,500		395,500
May	33,700	401,200	-367,500	1,865,500	1,893,500
June	<u>33,700</u>	<u>401,200</u>	<u>-367,500</u>		1,526,000
Totals	404,400	4,814,400	-4,410,000	3,731,000	

1 - Revenues other than service charges and property taxes.

2 - Minimum amount to fund operating fund cash flow with no contingency.

**Table 5**  
**Novato Sanitary District**  
**Operating Fund Reserve**  
**Self Insurance Reserve Fund**

	1998/99	1999/00	2000/01	Budget 2001/02
Beginning fund balance	\$206,300	\$205,700	\$205,600	\$219,200
Liability claims (insurance deducta	-12,200	-11,000	-98,200	-10,000 (1)
Interest earnings	11,600	10,900	11,800	11,000 (1)
Transfer from operating fund			100,000	
Ending fund balance	205,700	205,600	219,200	220,200

1 - Estimated

**Table 6**  
**Novato Sanitary District**  
**Operating Fund Reserve**  
**Rate Stabilization Reserve**

Year	Beginning Balance	Permanent New Expenses	Service Charge Revenue Increase	Ending Balance
1	\$600,000	\$350,000	\$0	\$250,000
2	250,000	350,000	150,000	50,000
3	50,000	350,000	300,000	0
4	0	350,000	450,000	100,000
5	100,000	350,000	450,000	200,000
6	200,000	350,000	450,000	300,000
7	300,000	350,000	450,000	400,000
8	400,000	350,000	450,000	500,000
9	500,000	350,000	450,000	600,000

## RESOLUTION NO. 2760

### RESOLUTION OF NOVATO SANITARY DISTRICT ADOPTING OPERATING RESERVE FUND POLICY, DATED SEPTEMBER 2001, AND DIRECTING IMPLEMENTATION OF POLICY

**WHEREAS**, the Novato Sanitary District (hereinafter "District"), was formed and lawfully operates under the Sanitary District Act of 1923; and

**WHEREAS**, District pursuant to the statutory authority invested in it is charged with protecting the health and safety of the citizens within the jurisdictional limits of the District with regard to sanitation, including collection, treatment and disposal of sewage, as well as solid waste collection and disposal; and

**WHEREAS**, the District is charged with operating a collection and treatment system for sewage pursuant to the terms of its NPDES permit No. CA0037958, which sets forth stringent requirements for the District's operations and protection of the water environment; and

**WHEREAS**, the Sanitary District Act of 1923 and other statutory authority provides the District with the power to levy and collect fees, tolls, charges and assessments in order to meet its operating revenue requirements and capital funding needs; and

**WHEREAS**, the District must accumulate and maintain sufficient fund balances in its operating accounts to meet current and projected operating expenses, cover operating cash flow requirements, and provide for both anticipated and unanticipated liabilities and expenses without adversely affecting the District's ability to provide both short and long term, high quality, uninterrupted service in compliance with applicable federal and state law, and regulatory permits.

**NOW, THEREFORE,** the Novato Sanitary District Board of Directors resolves as follows:

1. The Board of Directors finds that the District must have sufficient funds available to meet both the projected and unanticipatable cash flow needs in order to insure uninterrupted sanitation services to District's constituents and in order to provide continued compliance with applicable federal and state regulations and permit requirements.
2. The Board further finds that not all operating expenses of the District can be precisely forecast, and factors such as weather, emergency repairs, energy cost fluctuations, third party liability claims, vehicle and equipment replacement, regulatory changes and regional or national calamities require that the District retain prudent amounts of reserves in its operating fund.
3. The Board further finds, that in order to carry out the state and federal mandates of the District to provide sanitation services within its jurisdictional boundaries, it must develop and maintain revenue program which provides sufficient funds to meet budgeted operating expenses, as well as to provide sufficient reserves to meet short and long term District expenditure requirements.
4. The Operating Reserve Fund Policy, dated September 2001, is hereby adopted as the policy of the District. The policy shall remain in effect until the policy is repealed or amended by future action of the District Board and the following Operating Reserve Funds are created consistent with said policy:
  - Operating Cash Flow Reserve
  - Service Charge Rate Stabilization Reserve
  - Emergency Repair Reserve
  - Self-insurance and Self Retention Reserve
  - Vehicle Replacement Reserve

5. Staff is directed to implement this Operating Reserve Fund Policy by continuing to plan for, prepare and bring to the Board for adoption revenue programs adequate to provide for the ongoing operating needs of the District and to provide for the reserves addressed in the Policy.
  
6. This resolution shall take effect immediately upon its passage.

**PASSED AND ADOPTED** by the Novato Sanitary District Board of Directors on this 8<sup>th</sup> day of October, 2001 by the following vote:

**AYES:** Members: Knutson, Quesada, Renati, Silveira  
**NOES:** Members: None  
**ABSENT:** Members: York

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Arthur T. Knutson, President  
Board of Directors

ATTEST:

APPROVED AS TO FORM:

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Thomas S. Selfridge,  
Secretary-Treasurer  
Novato Sanitary District  
County of Marin,  
State of California

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Kenton L. Alm,  
District Counsel  
Novato Sanitary District  
County of Marin,  
State of California



**California Special  
Districts Association**  
*Districts Stronger Together*

# Special District Reserve Guidelines

SECOND EDITION



A GUIDE TO DEVELOPING A PRUDENT RESERVE.



## Acknowledgements

In preparing the Special District Reserve Guidelines, the California Special Districts Association (CSDA) greatly benefited from individuals who were generous with their time and insightful with their views. Our task force consisted of finance staff and general managers from independent special districts, as well as professional financial consultants.

CSDA extends its appreciation to its special district task force members:

- Paul Hughes of South Tahoe Public Utilities District
- Jeff Ramos of Cosumnes Community Services District
- John Rossi of Western Municipal Water District
- Rainy Selamat of Olivenhain Municipal Water District
- Ward Winchell of Southgate Recreation & Park District

To the finance professionals on our task force, who significantly contributed to the development of the principles and guidelines, CSDA extends its sincere gratitude. The contributions of the following were invaluable:

- David Becker, CPA, of James Marta & Company
- Eric S. Berman, MSA, CPA, CGMA of Brown Armstrong Accountancy Corporation
- Russ Powell, Senior Vice President of Economic & Planning Systems, Inc.
- Jim Marta, CPA, of James Marta & Company
- Saul Rosenbaum of the investment banking firm, Prager Sealy & Co, LLC
- Tim Schaefer of the public financial advisory firm, Fieldman, Rolapp & Associates

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 *Printed on recycled paper.*





## The Formation of Special District Reserve Guidelines

Answering a  
Call, Fulfilling  
a Need

The genesis for CSDA's Special District Reserve Guidelines was a 2000 Little Hoover Commission report entitled, *"Special Districts: Relics of the Past or Resources for the Future?"* The report included a section on special district reserves with an introductory finding that stated: *"Hundreds of independent special districts have banked multi-million dollar reserves that are not well publicized and often not considered in regional or statewide infrastructure planning."*

The 2000 report raised a number of issues relating to special district reserves including:

- Lack of guidelines and consistency
- Lack of visibility and publication of district financial information
- Lack of understanding among constituents and policymakers of district finances
- Lack of districts incorporating reserve information into infrastructure planning

News media reacted to the Little Hoover Commission report with banner headlines claiming that "obscure" public agencies have "hoarded" billions in reserves. Legislative hearings on special district finances were held and interest was spiked among grand juries, leading them to investigate how special districts within their counties handle reserves.

Ultimately, the Little Hoover Commission recommended that guidelines for prudent reserves be established, and that investment policies and practices be reviewed to determine if additional oversight was warranted.



...many independent special districts already have established reserve policies and most, if not all, special district officials recognize their fiduciary responsibilities and take them seriously.

## **CSDA Reserve Guidelines Task Force**

Although special district advocacy organizations disagreed with some of the Little Hoover Commission's findings and data interpretation, CSDA concurred that the establishment of reserve guidelines would assist special district governing officials and administrators in fulfilling their fiduciary responsibilities. To accomplish this, CSDA formed a task force in 2001 to identify both the essential elements of a reserve policy and the issues to be discussed during policy development.

The Special District Reserve Guidelines were developed by the task force as a tool for special district governing officials and administrators to assist them in fulfilling their commitment to provide cost-effective and efficient public services for the communities they serve.

## **Special District Reserve Guidelines**

### Second Edition

Today, with over a decade having passed since CSDA convened its original task force in 2001, many special districts have utilized the guidelines to evaluate their reserve policies, develop new reserve policies, and/or promote comprehensive and easily understood policies.

Through this decade-long process, special districts have gained new insights on improved best practices. Furthermore, certain accounting practices and terminologies have evolved. Therefore, in order to ensure the most accurate and updated guidelines, and in continuance of efforts to promulgate widespread adoption, CSDA commissioned a second task force in 2012 to produce a Special District Reserve Guidelines, Second Edition. CSDA encourages district officials to incorporate these new guideline elements into their policies, where applicable, based on size and services offered.

In developing and updating the second edition, the CSDA task force recognized that many independent special districts already have established reserve policies and most, if not all, special district officials recognize their fiduciary responsibilities and take them seriously. What may have generated most of the concern regarding special district reserves in 2000 is not lack of policy, but lack of outreach to constituents and others regarding district operations. It is essential that special districts continue to promote understanding outside their boardroom and perform outreach on district financial management to facilitate understanding among the public, media and legislators.



## Introduction

Reserves are the foundation of the sustainable delivery of core services.

### *Importance of Maintaining a Reserve*

Reserves are the foundation of the sustainable delivery of core services. Through prudent reserves, special districts offer taxpayers and ratepayers significant benefits including:

1. Savings to balance budgets
2. Emergency preparedness
3. Stable rates
4. Well-maintained infrastructure
5. Investment in the future

The fundamental question in maintaining a reserve is, how much is enough? In other words, when are reserves too low and when are they too high? These can be delicate questions because unwarranted reserves could undermine taxpayer and ratepayer support, while insufficient reserves could jeopardize the district's long-term sustainability.

There is also the question of where reserve funds should be spent. Pressure to expend reserves on making current services cheaper, rather than planning for the future, is all too frequent. Adopting a reserve policy will assist your agency in answering these fundamental questions.



## Reasons for Adopting a Reserve Policy

In addition to the over-arching taxpayer and ratepayer benefits of reserves noted earlier, there are many specific reasons for a special district to adopt reserve policies:

### Shared Vision:

A formally adopted policy promulgates a shared understanding of the proper level and use of reserves, which facilitates healthy working relationships.

### Objectivity:

Revenue decisions represent some of the most controversial and difficult choices that governing boards must face. Utilizing reserve policies reduces political gamesmanship and promotes responsible long-term planning.

### Fiscal Justification:

Inevitably, public agencies will face scrutiny over whether to raise or reduce rates, taxes or fees. Having reserve policies in place prior to such occasions serves as a valuable tool for both making and explaining difficult decisions.

### Public Awareness:

Keeping the public informed about what you do is a fundamental responsibility for any public agency. They are the boss, after all, and all of us understand from personal experience that our jobs are a lot easier and a lot less stressful when the boss knows about and approves of what you are doing. Adopting a policy can help the district better communicate to the public the motives for adopting a reserve, as well as convey the reasons for maintaining the reserve at a certain level.



### Important questions about reserves

The fundamental question in maintaining a reserve is, how much is enough? In other words, when are reserves too low and when are they too high? These can be delicate questions because unwarranted reserves could undermine taxpayer and ratepayer support, while insufficient reserves could jeopardize the district's long-term sustainability.



## Prudent Accumulation and Management of Reserves: Developing Policy

Each special district should develop and adopt a reserve policy.

The Special District Reserve Guidelines reflect the common belief among special districts that there should be a clear and well-articulated rationale for the accumulation and management of reserve funds. Each special district should develop and adopt a reserve policy as a commitment to financial prudence and careful stewardship of community assets. It is critical to understand that a reserve fund is designated by a public agency to carry out specific purposes in a manner consistent with other financial policies, budgetary practices, district programs, and legal requirements.

### *Reserve Policy Objectives:*

1. To provide adequate funding to meet the agency's short-term and long-term plans.
2. To minimize adverse annual and multi-year budgetary impacts from anticipated and unanticipated expenditures, thus minimizing the possibility of unplanned service fees or rate fluctuations.
3. To strengthen the financial stability of the agency against present and future uncertainties in an ever-changing environment.

### *Foundational Elements of a Reserve Policy:*

Prior to developing a reserve policy, a district should first establish the three prerequisites below.

1. Clear, organizational philosophy/mission.
2. Policy-oriented board of directors, with long-term focus on fiscal sustainability.
3. Standardized method of financial reporting, such as Governmental Accounting Standards Board (GASB) Statement Nos. 34 and/or 54.

## Communicating regularly about district financials and reserve priorities creates trust.

### Principles for Developing a Reserve Policy:

1. Identify the uniqueness of the district.
  - a. Consider district goals, needs and constraints.
  - b. Utilize life-cycle analysis if district is capital intensive.
  - c. Regularly measure condition of assets.
2. Form a complete understanding of the district's core business and significant cost drivers for district operations.
3. Engage in strategic planning.
  - a. By developing, regularly evaluating and, when necessary, modifying strategic plans, districts can more efficiently plan and shape their futures. Strategic planning can help district boards anticipate and adapt to changing environmental, regulatory and demographic conditions. This assists districts in establishing appropriate reserve funds and adopting adequate target levels.
  - b. Seek community input in the strategic planning process, i.e., ratepayers and taxpayers, business groups, community organizations, other public agencies serving the same constituency, etc.
4. Make communicating a priority.
  - a. A regular newsletter and annual report are good starting points; it is critical for districts to reach out to the public and explain their financial position.
  - b. Seek input through customer surveys, community meetings, and other meaningful engagement.
  - c. Inform customers and constituents of output and seek their input in evaluating policies.
5. Recognize that a good reserve policy must be consistent with other financial policies, such as a balanced operating budget and investment policies.
6. Create and maintain a well-developed capital improvement plan.
7. Estimate the ebb and flow, or "seasonality," of cash-flow during the fiscal year and build a basic understanding of the degree of short-term borrowing necessary to meet such needs.
8. Clearly identify reserves—both categories and purposes. Set target levels for reserves that are consistent with the district's mission, the district's uniqueness and the philosophy of the district's board and community.
9. A broad reserve policy may include many elements or sub-policies. Some areas that may need sub-policies include:
  - a. Rate-stabilization funds
  - b. Fees and charges
  - c. Debt issuance and management
  - d. Deferred maintenance
  - e. Level of unrestricted (contingency) funds
  - f. Long-term repair and replacement



Every district has unique circumstances and a proper fund balance should be considered on a case-by-case basis.

## Fund Balance and Net Position/Net Assets

There are many factors that must be considered when establishing an appropriate fund balance and ensuring the prudent management of your district's finances. Every district has unique circumstances and a proper fund balance should be considered on a case-by-case basis. Thoughtfully accounting for variables such as your district's revenue sources and income volatility will assist your district in determining its reserve amount. On the following pages are issues that should be considered when adopting a reserve level.



## Specific Considerations for Budgeting and Allocating Fund Balance or Net Position/Net Assets

### Considerations

1. Define the special district's fiscal objectives:

- a. Short-term
- b. Long-term
- c. Operating
- d. Capital

2. Identify where funds are used:

- a. Operating revenues are the general-purpose funds through which ongoing activities are funded.
- b. Special-purpose revenues often are legally restricted for a particular use. For example, a special assessment for infrastructure must be separately accounted for and spent on designated infrastructure costs.
- c. Debt proceeds should be used to fund costs that provide a benefit across fiscal years. The issuance of debt allows the district to allocate these costs by spreading the debt service to these periods. Debt proceeds should never be used for short-term operating costs because this would entail allocating current operating costs to future periods.
- d. One-time revenues should be used for one-time expenses. If a special district gets one-time revenues and uses it to provide additional full-time positions or to fund on-going operating costs, it may lead to a budget crisis when the one-time funding runs out.



### One-time Revenue

According to the Government Finance Officers Association, "Examples of one-time revenue include: infrequent sales of government assets, bond refunding savings, infrequent revenues from development and grants. These revenue may be available for more than one year (e.g., a three-year grant) but are expected to be non-recurring."

### One-time Expenditures

According to the Government Finance Officers Association, "Examples of expenditures which a government may wish to use one-time revenue include start up costs, stabilization (e.g. to cover expenditures that temporarily exceed revenues), early debt retirement, and capital purchases."

## Components of Fund Balance

In governmental funds, “reserves” typically comprise a portion of the total fund balance. Fund balance reporting standards play a part in describing how much of fund balance might be available for a reserve and how much is limited to other purposes. GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, changes how fund balance has traditionally been reported.

In the past, reporting of fund balance focused on whether resources were available for appropriation (i.e., budgeting) and distinguished between “unreserved fund balance” (i.e., available for appropriation) and “reserved fund balance” (i.e., not available for appropriation). GASB Statement No. 54 changes the focus to the “extent to which the government is bound to honor constraints on the specific purposes for which amounts in the fund can be spent” and establishes five different components of fund balance:

### COMPONENTS OF FUND BALANCE

NONSPENDABLE FUND BALANCE	RESTRICTED FUND BALANCE	COMMITTED FUND BALANCE	ASSIGNED OR DESIGNATED FUND BALANCE	UNASSIGNED OR UNDESIGNATED FUND BALANCE
This category is inherently nonspendable, such as the long-term portion of loans receivable, the principle of an endowment and inventories.	This classification has externally enforceable limitations on the use of fund balance, imposed by parties such as creditors, grantors or laws or regulations of other governments.	This encompasses limitations imposed by the special district upon itself at its highest level of decision making (e.g., governing board through a resolution). For example, the governing board might commit a portion of fund balance to a “stabilization fund” to provide a cushion against unknown economic shocks and revenue declines.	This portion is earmarked for an intended use. The intent is established at either the highest level of decision making or by a body or official designated for that purpose. For example, a share of fund balance might be assigned to offset a gap in the budget stemming from a decline in revenues or an allotment could be assigned for an upcoming special project.	This comprises all fund balances that are left after considering the other four categories. Use is least constrained in this category of fund balance.



Unassigned fund balance is typically the primary subject of a reserve policy. However, committed and assigned fund balance may also be thought of as part of a reserve policy as the governing board or management, respectively, has some control over the balances. Conversely, restricted fund balances or nonspendable fund balances are fundamentally constrained, making it unnecessary to place parameters on them through reserve policy in order to achieve prudent savings and expenditures of public resources.

It is recommended that every district establish policies regarding minimum fund balance and spending priorities in order to communicate to users the importance of a reserve for economic uncertainties, why it consists of amounts that are unassigned and that it is not available for spending.

Districts' policies should specify the order in which fund balances are spent when more than one amount is available for a specific purpose. Where such policies do not exist, GASB 54 prescribes that the default order in which these amounts should be spent is committed, assigned, and then unassigned.



### **GASB 54**

According to the Governmental Accounting Standards Board, statement No. 54 was issued after, "...research revealed that the existing standards guiding fund balance reporting were being interpreted inconsistently by different governments. Consequently, the fund balance information reported by many governments also was inconsistent. It also became clear that the understandability of fund balance information was affected and that financial statement users were unable to readily interpret reported fund balance information."

*GASB fact sheet about Fund Balance Reporting and Governmental Fund Type Definitions*



### **Sample Policy Language**

The "X" district maintains a minimum unassigned fund balance of not less than "X" percent of budgeted general fund expenditures and other financing uses as a reserve for economic uncertainties. The district believes a reserve of this level is prudent to maintain a high bond rating and to protect the district from the effects of fluctuations in property tax revenues to which special districts are vulnerable. Because amounts in the nonspendable, restricted, committed and assigned categories are subject to varying constraints on their use, the reserve for economic uncertainties consists of balances that are otherwise unassigned.

## Reserve Level Targets

A reserve policy must set a target level of reserves to maintain. The target is typically defined in terms of unrestricted fund balance as a percentage of either regular operating revenues or regular operating expenditures. The choice between revenue and expenditures as a basis depends on which element is more predictable. A government that relies heavily on property taxes typically would choose revenues, whereas a government with a less predictable revenue portfolio might choose expenditures. In either case, the base should only reflect operating numbers and should remove the effect of unusual spikes or drops that would distort long-term trends.

With the basis of the target defined, the next step is to select a reserve-level target number. The Government Finance Officers Association (GFOA) offers guidance as to the amount of unassigned fund balance governments should maintain in their general fund operating revenues or regular general fund operating expenditures, regardless of size. As special-purpose governments, special districts should carefully balance such general advice with the unique circumstances associated with the district's operational environment.

In considering what constitutes adequate reserves, a special district may want to establish key benchmarks or ratios. Many industries have key equity target formulas or ratios that establish minimums to provide a red flag warning when equity may be too low. Some of those ratios may include the following:

- Debt to Equity
- Property Taxes to Equity
- Current Ratio
- Capital Outlay to Equity
- Capital Outlay to Operating Expenses

Certain districts may establish their own ratios based on the unique aspects of the district or an operating environment that may be different than other organizations in their industry.



### Local Conditions as a Basis

The Government Finance Officers Association notes that fund balance is ultimately a local decision based on local conditions. "...Finance staff should analyze the risks that influence the need for maintaining reserves as a hedge against uncertainty and loss."

*(p.57, GFOA, Financial Policies)*

## Articulating Financial Position and Decisions

Is this organization in good financial shape? That depends on the condition of the current assets and the short-term and long-term needs of the organization as they relate to its resources. If there exists significant current infrastructure needs, then financing may be required. Is enough set aside for contingencies? If water costs increase by 10 percent, or new environmental or health standards are issued, how will that affect total net assets?

Governmental entities collect, hold and expend resources in public trust. If too little is collected, they risk failing to meet mandated needs. If too much is collected, they overburden the public and tie up resources that taxpayers and ratepayers could use in the economy. Historically, governments have been known to spend most of their resources each year and too often fail to properly plan for long-term needs. Special districts should carefully examine their operations and budget to ensure that expenses, such as capital needs and contingencies, are anticipated and appropriate resources are set aside.

Some governments, either through good fortune or good planning, have reserved net assets for future plans and needs. What most governments have failed to do, as emphasized in the 2000 Little Hoover Commission's report, is to effectively communicate their plans for the net assets and explain why the balance is appropriate.

Each special district needs to:

1. Analyze its financial position.
2. Examine its current and long-term needs, including a capital improvement plan.
3. Establish its target fund balance or net assets.
4. Outline its goals and needs through policy, budgets and enhanced financial statement note disclosures.
5. Anticipate public scrutiny of financial statements and proactively communicate how finances are being used in a manner the public can easily digest.

It is recommended that special districts, at minimum, conduct a review of their reserve policy annually to ensure it meets the needs of the district and is in compliance with any requirements/standards that may have changed.

## Conclusion

Each special district's financial and legal professionals should review reserve policies prior to adoption to ensure they are in compliance with all current laws and regulations. Reserve policy should be established based on each district's unique financial situation. Any reserve policy needs to be reviewed regularly as the financial environment within which it functions is dynamic and there may be applicable legislative or regulatory changes.

The 2000 Little Hoover Commission report concluded that there was a disconnect between special districts and their constituents and other local government entities. Therefore, it is important that each agency not only develop a reserve policy, but ensure that stakeholders know and understand the district's financial position and decision-making process.

Districts should consider preparation of a public outreach program to communicate financial and program information on a regular basis to affected or interested populations. How involved each respective public outreach program is for a district is typically determined by the size and complexity of the district. A first step may be as simple as adding the information to an agency's website or the development of an annual report. CSDA encourages districts to take the next step and proactively engage the public to ensure its awareness.

We hope you find these guidelines helpful and if you have any comments or suggestions on how we can improve this document, please contact us at 877.924.2732.



## Addendum I: Glossary

**Assigned Fund Balance:** Amounts that are intended to be used by the special district for specific purposes but do not meet the criteria to be classified as restricted or committed.

**Capital Improvement Program (CIP):** A short-range plan that identifies capital projects and equipment purchases, provides a planning schedule and identifies options for financing the plan.

**Committed Fund Balance:** Amounts that can only be used for the specific purposes as determined by a formal action of the special district's highest level of decision-making authority.

**Net assets:** The amount of assets in excess of liabilities. For non-enterprise fund types, this excess is referred to as "fund balance." For enterprise-fund types, this excess is referred to as "net assets" or, as of July 1, 2012, "net position."

**Nonspendable Fund Balance:** Amounts that cannot be spent or where cash has been spent previously to produce a fund balance – for example, inventory, pre-paid expenses or restricted assets.

**Pay-Go:** Is the practice of financing expenditures with funds that are currently available rather than borrowed.

**Restricted Fund Balance:** Amounts that can only be spent for specific purposes which are stipulated outside the control of the special districts, such as the constitution, external resource providers (such as granting entities) or enabling legislation.

**Unassigned Fund Balance:** The residual of all other funds that are not nonspendable, restricted, committed or assigned. Unassigned balances are not in special revenue, capital projects, permanent or debt service funds unless the fund is in deficit.



## Addendum II: Special District Reserves Talking Points

### **PRUDENT RESERVES MAKE FOR SOUND BUDGETING**

For countless families, saving for a rainy day is common-sense. For special districts, reserve funds are not just money in a bank; they are fundamental resources for ensuring reliable core services and community security.

#### *How Taxpayers and Ratepayers Benefit*

Special districts designate money toward savings in order to balance their budget, respond to emergencies, keep rates affordable, maintain current infrastructure and plan for future public works projects.

- **Balancing Budgets** – Over the course of the fiscal year, short-term reserves help balance the ebb and flow of revenues verse expenditures.
- **Emergency Preparation** – In the event of a disaster, communities can't afford not to have savings readily available to quickly repair critical local infrastructure and bring core services back online.
- **Affordable Rates** – With appropriate savings, special districts are able to use resources wisely and smooth out the highs and the lows of volatile economic conditions, rather than spend their entire surplus and then seek new revenue or jeopardize services.
- **Infrastructure Maintenance** – Reserves mean the pipes are fixed, roofs are patched, and worn equipment is replaced without going back to the taxpayers or ratepayers to pay for routine upkeep.
- **Planning for the Future** – A long-term, thoughtful approach to public infrastructure requires the foresight to plan for, and discipline to save for, future needs.

#### *Reserves are Much More than Liquid Assets*

- **What comprises a reserve fund?** Reserve fund balances and net assets are not just cash and investments. They also include the net value of capital facilities, land and equipment measured from the very inception of the district.
- **Assigned funds** are budgeted for specific long-term public needs as planned by the board of directors.
- **Committed funds** are set aside via established policies for specific uses such as cash-flow, capital improvements, contingencies, and rate stabilization.
- **Restricted funds** are limited by legal or contractual requirements, or cannot otherwise be spent.

#### *Best Practices for Sensible Budgets*

- Historically, governmental agencies and departments have been known to spend everything they have before the end of the fiscal year in order to justify increased future allocations from their larger bureaucracy.
- Special districts are different because they empower core local service providers with budgetary control, encouraging efficiency and fiscal restraint rather than punishing it.
- The CSDA Reserve Guidelines Task Force identified both the essential elements of reserve policies and key issues to be discussed during reserve policy development to assist districts in fulfilling their commitment to provide cost-effective and efficient public services to their communities.



## Addendum III: Capital Planning

A Capital Improvement Program (CIP), also referred to as a capital plan, exists to identify and prioritize a special district's need for capital goods. A CIP should prioritize the importance and timing of the various assets to be acquired. In addition, a CIP should contemplate how those goods will be paid for – cash (equity) or debt. A capital plan is a strategic and comprehensive plan for the acquisition and implementation of the district's capital assets over time. In that sense, it is different from a finance plan, which focuses on individual acquisitions and how to pay for them.

To fulfill their mission, every district makes capital investments. Debt, especially tax-exempt debt, is recognized as an important and continuing source of a district's capital to fund improvements necessary to achieve its mission and strategic objectives. A CIP provides the framework by which decisions will be made regarding the use of cash and debt to finance capital projects.

Debt is defined to include all short and long-term obligations, guarantees and instruments that have the effect of committing the district to future payments. The assumption of debt, both direct and indirect, is subject to the district's approval. Any debt issued by subsidiary entities is subject to these policies. In satisfying their fiduciary responsibilities, it is important that a district's board and management know the extent of debt obligations.

### **CIP Objectives**

1. To provide guidelines to management on the use of reserves and debt to support a special district's capital needs while achieving the lowest overall cost of capital.
2. To provide selected financial measures, with specific targets, to ensure that the district continues to operate within appropriate financial parameters while allowing the agency to maintain financial stability and the highest acceptable credit rating that permits it to issue debt at favorable rates.
3. To bridge the cash flow gap between the district's available funds and its capital needs when the assumption of debt is deemed prudent.

### **Creating a Capital Plan**

1. Establish goals
2. Assess needs
3. Determine pay-go or borrow
4. Identify methods available for funding
5. Design the loan—the tactical plan
6. Organize approach

*Details on the following pages.*

### ***Establish Goals***

The key elements in setting clear capital plan goals include:

- 1. *Understanding the role of the planning horizon.*** Planning horizons are important considerations in well-developed capital plans. For example, it makes little sense to try to plan for a 10-year or 20-year horizon if innovation, technology, demographics or legislative threats to the plan occur frequently or on short notice. Conversely, agencies that are in low-technology businesses and stable demographic circumstances can more effectively and more appropriately plan for long periods. Planning horizons should mirror long-term repair and replacement requirements of existing facilities.
- 2. *Integrating the use (or lack thereof) of reserves.*** The extent to which a particular district has accumulated reserves will dramatically impact the CIP. The development of, and adherence to, strong reserve policies can greatly simplify funding choices for a capital plan, but blind adherence to arbitrary reserve levels can be just as inhibiting as no reserves at all. The key is to make reserve accumulation, or depletion, work in harmony with the CIP, operating budget and risk management of the district.
- 3. *Recognizing the repetitive nature of implementing the CIP.*** A capital plan is by its nature repetitive. For that reason, many districts choose to review and update it annually, usually as an adjunct to deliberation of the operating budget. This keeps the CIP current and tempered by present information on the priorities of the district.

### ***Assess Needs***

Every capital plan starts with a needs assessment. The assessment should be based on a comprehensive review of the agency's assets at the time an asset is recorded and an estimated useful life is assigned to each asset. This information later will be used as an indicator of when an asset is scheduled to be replaced. Estimated future replacement costs need to be obtained in order to reasonably estimate CIP fund requirements within an agency's long term financial plan.

### ***Determining Pay-Go or Borrow***

The "pay-go" method of using current revenues to pay for long-term infrastructure and other projects is often considered when sufficient revenues and reserves are available and long-term borrowing rates are higher than expected cash reserve fund earnings.

On the other side of the spectrum, the "pay-as-you-use" or "borrow" strategy limits the need for building of major amounts of equity in capital assets. Such accumulation can be less economically efficient, particularly for those districts that are capital intense and whose capital goods are "used up" over long periods of time. Similarly, financing of smaller capital goods, or those with short or uncertain useful lives, is also inefficient. The rationale behind the borrow approach is that the district's stakeholders should "pay" for the assets required to deliver the goods or services of the agency over a time period that more closely mirrors the useful life of those assets.

Most districts use a blended approach based on their debt management policy. Often, a district's approach is dictated as much by affordability as by philosophy, given that few public bodies are capable of paying cash for all capital assets.

### ***Identify Methods Available for Financing***

Once the goals have been set, the needs assessed and the decision whether to pay cash or finance the asset has been made, some thought must be given to the method of financing. For example, even if an asset is to be procured for cash, and the cash is on hand in a reserve set aside for that purpose, a decision still must be made on whether to replenish or restore that reserve, and over what time period and from what source it will be replenished.

Choosing to issue debt means that the following choices must be made: form of debt, mode (fixed or variable rate), repayment terms and method of sale. These are the tactical decisions that often blur the understanding of the strategic elements of the capital plan.

### ***Design the Loan – The Tactical Plan***

If a decision is made to borrow, an array of choices will follow. Some districts choose to borrow from banks or private lenders; others choose public offerings of debt. Lease financing may be considered as an alternate to bond financing. Some districts pool their needs with other similarly situated districts in order to reduce costs through economies of scale.

Regardless of the choice of lenders or approach matching the useful life of the financed asset to the borrowing term is an important consideration. Common sense tells us that we should hesitate to finance automobiles with 30-year bonds. By the same token, a water treatment plant with a design-life of 50 years can be safely and prudently financed over long periods of time. Still, debt issuances over 30 years are rare.

This element of the CIP should also carefully consider other needs within the strategic plan when pledging assets or revenues to lenders. A generous package to a lender on today's asset may make tomorrow's asset financing problematic or impossible. The key is to ensure that each tactical financing plan within the capital plan works harmoniously with other elements of the plan and is flexible enough to allow for the inherently changing nature of the CIP.

### ***Organize the Approach***

The successful capital planning process looks a great deal like the successful budgeting process. The end-result articulates the goals and objectives of the organization to all stakeholders and relies on an accurate and unbiased assessment of needs. It provides for an evaluation of the desired assets to distinguish between "wants" and "needs." It is written and shared with the district's stakeholders.

The capital plan is revisited often and provisions for changing or amending it are straightforward. Finally, it incorporates periodic analysis of results and achievements for management and the governing body.

## **Summary**

A CIP need not be elaborate or weighty to be effective. Many effective capital plans consist of a single spreadsheet and several paragraphs of supporting text. The development of the program is vital to the efficient use of capital. It is a key ingredient in a lender's assessment of management's effectiveness and control. It is among the most important tools an elected official possesses to discharge the duties of office.

Readers who are interested in additional information about the development of capital plans should consider a variety of books, and other information sources, on the topic. Some suggested examples are shown in the attached resource listing at the back of this document.



## Addendum IV: Resources

The Government Finance Officers Association (GFOA) is a great source for more information regarding various government financial matters, including fund balance and financial reporting. GFOA has an extensive publications department. View a list of its full offerings at [www.gfoa.org](http://www.gfoa.org). The following publications may be useful:

1. "An Elected Official's Guide to Financial Reporting"
2. "Best Practice – Replenishing Fund Balance in the General Fund"
3. "Governmental Accounting, Auditing, and Financial Reporting"
4. "Recommended Budget Practices: A Framework for Improved State and Local Government Budgeting"

The Governmental Accounting Standards Board (GASB) has a number of user guides written by the standard setter for use in many types of governments. These include:

1. *An Analyst's Guide to Government Financial Statements—revised, updated, and significantly expanded*
2. *What You Should Know about the Finances of Your Government's Business-Type Activities—a completely new guide for 2012*
3. *What You Should Know about Your Local Government's Finances*

In addition, in 2013, GASB is expecting to publish a guide directed at "Business-Type Activities." Most special districts in California are "Business-Type Activities."



**California Special  
Districts Association**

*Districts Stronger Together*

1112 I Street, Suite 200  
Sacramento, CA 95814  
toll-free: 877.924.2732  
csda.net



**BARTLE WELLS ASSOCIATES**  
INDEPENDENT PUBLIC FINANCE ADVISORS

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February 28, 2013

Board of Directors  
Novato Sanitary District  
500 Davidson Street  
Novato, CA 94947

Attn: Beverly James, Manager - Engineer

Re: Proposal for Financial Planning Sale Services

Bartle Wells Associates is pleased to submit this proposal to the Novato Sanitary District to provide financial advisory services in connection with recommendations to revise the District's reserve fund policy. The general scope of services and the fees for such services is set forth below. Bartle Wells Associates specializes in water and wastewater financing for California public agencies. We have assisted the District for many years regarding financial policy, project financing, determination of service charges, capacity charges and other financing matters. We previously assisted the District with implementation of a reserve fund policy in 2001.

## **Services**

Bartle Wells Associates will perform the following services in connection with the revision of the District's reserve fund policy, working at all times in close cooperation with the District's staff and other consultants and advisors.

1. Review District's current reserve fund policy and implementing documentation. Review the number of reserve funds and the amounts in each fund to determine if the funds overlap. Examine the current fund amount for adequacy and ease of administration.
2. Review the CSDA Special District Reserve Guidelines for applicability to Novato Sanitary District and identify assigned and unassigned fund balance components.
3. Determine if the number of reserve funds may be reduced. Examine the possibility of combining all reserves into one or two all-encompassing funds.
4. Recommend an appropriate reserve fund targets for the District to maintain with a rationale for sizing the appropriate amount. Develop a plan for annually updating the reserve target during the District's regular budgeting process.
5. Prepare a draft Reserve Policy and memo for District review and comment.

February 28, 2013

Page 2

6. Prepare a final Reserve Policy document and a final memo incorporating District comment.

### **Availability and Fees**

1. We are prepared to begin work upon your authorization to proceed.
2. During the project development period, we will be available at all reasonable times and on reasonable notice for meetings and for consultation with the District, its staff, attorneys, and others as necessary.
3. Bartle Wells Associates will perform all work. Thomas E. Gaffney, one of our principals, will be placed in charge of the work, and will devote time and effort to the project as needed.
4. For services as requested by the District we will be reimbursed on a time and materials basis and payable as provided in our Billing Rate Schedule 2013.
5. Our fee will not exceed \$4,500 without prior written authorization of the District.
6. In addition to the services provided under this proposal, the District may authorize us to perform additional services for which the District will compensate us based on consultants' hourly rates at the time the work is performed, plus direct expenses.
7. Bartle Wells Associates will maintain in force, during the full term of the assignment, insurance in the amounts and coverage as provided in the Schedule of Insurance attached.

We would very much like to work for the District on this assignment, and hope that this proposal will constitute a suitable basis for our serving you.

Very truly yours,

BARTLE WELLS ASSOCIATES



Thomas E. Gaffney, CIPFA  
Principal

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Enc.  
Schedule 2013

## NOVATO SANITARY DISTRICT

### MEMORANDUM

Date: March 8, 2013  
To: Board of Directors  
From: Finance Committee: Jean Mariani, William Long  
Subject: Rate Structure

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#### **Current Rate Structure for Connection, Permit, and other Fees**

The District's Strategic Plan identified the need to "Plan for and manage finances to achieve long-range financial stability, and competitive and fair rates and charges, while enabling effective Board and public oversight".

The first part of achieving this goal was to conduct a Revenue and Rate Analysis and adopt sewer service charges through 2016. This was completed in the spring of 2012.

The next step is to look at the fees and charges other than sewer service charges. A schedule of these charges is included as Attachment 1. These charges were adopted in Ordinance 70 as amended by Ordinance 101. Attachment 2 contains the excerpts from Ordinance No. 70 that relate to fees and charges.

The Connection fee was last evaluated in 2004 and has been increasing at a set rate of 5%/year since. Attachment 3 shows the history of the connection fees.

The permit and other fees were last evaluated and adjusted in 1994.

#### **Recommendation**

The District's objective is to ensure that the rates are sustainable, defensible, understandable, and fair. To the extent possible, the fees should represent the cost of providing the service. Staff recommends requesting a proposal from Bartle Wells to assist staff in preparing the analyses needed for setting each of the fees and charges.

NOVATO SANITARY DISTRICT

FEEES AND CHARGES - EFFECTIVE 7/1/12

CONNECTION

\$8950.00 per family unit less prepaid charges.

\$448.00 per fixture unit as per CA plumbing code. This rate applies to all non-residential connections.

PERMIT & INSPECTION

\$40.00 per single family dwelling/residential.  
Plus \$20.00 "Y" charge where it applies.

\$60.00 minimum for non-residential inspection.

\$20.00 per space in trailer park or each SFDU in development where more than one building connected to common side sewer with minimum of \$60.00 charge.

COLLECTOR SEWER CHARGE

4" \$1,000.00

6" \$2,000.00

8" \$3,000.00

SPECIAL EQUALIZATION CHARGE

Ignacio Assessment District =

\$90.00 per equivalent family unit

Novato Auto Mart =

\$197.00 per gross acre

BAHIA (Outside approved subdivisions) on individual basis.

\$250/Family Unit

Hamilton Project \$535/acre

REPAIR

\$15.00

ADDITIONAL FIXTURE ONLY NO INSPECTION

\$25.00 - 01-20 Fixture Units

\$35.00 - 21-40 Fixture Units

\$45.00 - 41-up Fixture Units

ALTERATION

\$40.00

EXPIRED PERMIT

Connection permit renewal - \$25.00

Main extension permit renewal - \$100.00

DEVELOPERS PREPAYMENT

\$1,790.00

NON-DOMESTIC DISCHARGE FEES

(For Temporary Class 1Permits ONLY)

Application Fee ----- \$ 175.00

Permit Issuance Fee --- 1,240.00

Monitoring/Sampling ---- 40.00 per site visit

7/11/12

Conveyance/Treatment/Disposal - (Determined on a case-by-case basis, but utilizes a base rate of \$18.19 per 1,000 gallons, multiplied by an appropriate strength factor based on the nature of the discharge.)

# NOVATO SANITARY DISTRICT

Excerpts from  
District Ordinance No. 70 (Sanitary Code of Novato Sanitary District)  
Adopted April 1991, Revised June 1993, February 1994

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## Sec. 708. Connection Charges.

(b) Connection Charge. A connection charge of Three Thousand Dollars (\$3,000.00) per family unit shall be paid to the District by each person desiring connection to the public sewer. Payment of said connection charge shall be made prior to the issuance of a connection permit and shall be in addition to all other fees and charges required to be paid under District rules and regulations. [ORD 75, 6/14/93 - **\$3,000.00**] [ORD 101, 6/14/04 - **\$6,030.00**]

(c) Annual Increase of Connection Charge. On July 1, 1994, and each July 1st thereafter, the connection charge required under Section 708(b) shall be increased by five percent (5%) rounded upward to the nearest Ten Dollars (\$10.00); provided that the District Board may, at its option, determine by resolution adopted prior thereto that such increase shall not be effective for the next succeeding fiscal year. [ORD 75, 6/14/93]

(d) Partial Prepayment - Subdivisions. A partial prepayment of the connection charges required under this section, amounting to twenty percent (20%) - rounded upward to the nearest Ten Dollars (\$10.00) - of the applicable connection charge per family unit, shall be paid to the District for each family unit before any final subdivision map is approved by the District and before any permit to install sewerage facilities to serve the subdivision is issued. However, the amount of the required partial prepayment of connection charges may be increased in the event that a special service agreement has been required as provided in Section 603 hereof. Subdivisions involving a type of development such that the number of family units to be connected cannot be accurately determined at the time of subdivision, shall make a partial prepayment of connection charges based on one (1) family unit for each subdivision lot. [ORD 75, 6/14/93]

Sec. 709. Sewer Permit and Inspection Fees. Permit and inspection fees are hereby established as follows:

(a) Single-Family Dwellings and Trailer Courts. A fee of Forty Dollars (\$40.00) shall be paid for issuance of a permit and inspection of each single-family dwelling building and/or lateral sewer installation. A fee of Twenty Dollars (\$20.00) shall be paid for issuance of a permit and inspection of building and/or lateral sewers for each space in a trailer court, or for each single-family dwelling unit in developments where more than one (1) building is permitted to be connected to a common side sewer as provided in Section 504 of this Ordinance, with a minimum fee of Sixty Dollars (\$60.00) for each building and/or lateral sewer constructed.

(b) Multiple-Family Dwellings, Commercial, Industrial, Church, School, Public and Other Users. A fee of Sixty Dollars (\$60.00) shall be paid for issuance of a permit and inspection for each building and/or lateral sewer installation serving multiple-family dwellings, commercial, industrial, church, school, public and other users.

(c) Alteration or Repair of Existing Side Sewers. A fee of Forty Dollars (\$40.00) shall be paid for issuance of a permit and inspection of any work adding to or extending an existing side sewer. In the case of connections of other than single or multiple-family dwellings, when modifications are made in existing buildings increasing the number of plumbing fixtures connected, but not involving work on the existing side sewer, a fee shall be paid for the issuance of a permit for these modifications based on the added plumbing fixture units, as follows:

<u>Fixture Units Added</u>	<u>Permit Fee</u>
1 to 20	\$25.00
21 to 40	\$35.00
41 up	\$45.00

A fee of Fifteen Dollars (\$15.00) shall be paid for issuance of a permit and inspection of any repair work done on an existing side sewer.

(d) Saddle or Manhole Connections. In addition to other permit and inspection fees required herein, a fee of Twenty Dollars (\$20.00) shall be paid for the inspection of a saddle, wye or tee connection to an existing main sewer or the connection of a lateral sewer to an existing manhole.

(e) Public Sewers. A fee based on a percentage of the amount estimated by the Manager-Engineer to be the cost of construction of public sewers, laterals, and other public sewerage facilities shall be paid to the District for reviewing plans and specifications, issuing a permit, and inspecting the installation of said facilities, as follows:

<u>Estimated Cost of Sewerage Facilities to be Constructed</u>	<u>Plan Checking and Permit &amp; Inspection Fees</u>
Less than \$75,000	3% of estimated cost.
\$75,000 and up	3% for first \$75,000 of estimated cost, plus 2% of the estimated cost over \$75,000.

The minimum fee for this purpose shall be One Hundred Dollars (\$100.00).

A plan review fee of One Hundred Dollars (\$100.00) shall be paid when plans are presented to the District for review. Said fee shall be credited against the fees hereinabove provided upon issuance of a permit for public sewer construction. In the event that a permit is not issued, the fee shall be retained by the District to reimburse its plan review costs.

(f) Overtime Inspections. Persons requesting inspections of side sewers or public sewers at any time other than the regular working hours of the District shall make such request in writing at least twenty-four (24) hours in advance and shall pay an additional inspection fee equal to the required inspection hours multiplied by the District Inspector's overtime salary rate, plus an overhead and supervision charge calculated at one hundred (100) percent of the Inspector's straight-time salary for the time involved. The minimum fee for this service shall be based on two (2) hours' inspection time.

(g) Renewal or Extension of Permit. Whenever a permit for sewer installation expires, as provided in Section 721 of this Ordinance, an additional fee of Twenty-five Dollars (\$25.00) shall be paid for the issuance of a new permit for said installation. In the event that an extension of time is granted to complete work under a public sewer extension permit, an additional fee of One Hundred Dollars (\$100.00) shall be paid for the renewal or extension of said public sewer permit.

Sec. 710. Collector and Trunk Sewer Charges.

(a) Collector Sewer Charge. In addition to any other fees and charges established by the ordinances, rules and regulations of the District, there shall be collected, prior to connection to the sanitary sewerage system of the District, a Collector Sewer Charge to be paid by persons desiring to connect a side sewer directly to an existing main sewer of the District which was installed without direct or indirect cost to the connecting property with respect to its use as a collector sewer, which charge shall be based upon the required size of connecting side sewer, as follows:

<u>Size of Side Sewer</u>	<u>Amount of Charge</u>
4 inch	\$1,000.00
6 inch	2,000.00
8 inch	3,000.00

Provided, however, that in the event the connecting property is within a Special Benefit Zone in which a Special Equalization Charge for collector sewers has been established by the District Board in accordance with Section 707 of this Ordinance, the Special Equalization Charge for collector sewers so established shall be paid in lieu of the Collector Sewer Charge herein provided.

(b) Trunk Sewer Charge. A portion of the Connection Charge, levied pursuant to Section 708 of this Ordinance, shall be considered a Trunk Sewer Charge. Said Trunk Sewer Charge, amounting to Twenty Dollars (\$20.00) per family unit, shall be paid by all persons connecting to the public sewer system and shall be deposited in the Oversize Reimbursement Fund of the District to partially reimburse installers of oversize sewers in accordance with Section 614 of this Ordinance. Any amounts remaining in said Oversize Sewer Reimbursement Fund after annual reimbursement payments are made shall be transferred to the Capital Improvement Fund of the District.

Sec. 711. Fees and Deposits - Environmental Quality Act. Where the District is the lead agency or a responsible agency for any project under the State and local guidelines adopted pursuant to the Environmental Quality Act of 1970, the person or persons beneficially interested shall deposit with District the estimated cost of District preparation of materials, reports and the making of evaluations of the proposed project as estimated by the Manager-Engineer. Should the amount of deposit be inadequate to meet the District's costs as lead agency or as a responsible agency involved in providing consultation to the lead agency, as required by law, District shall, prior to completion of the District's evaluation of the proposed project, notify the person or persons beneficially interested of the amount necessary to complete the review of the proposed project which shall be immediately deposited with District. Should there be a surplus remaining in the deposit following completion of the District's evaluation of the project, the surplus shall be returned to the person or persons making such deposit.

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