ZONE 7 BOARD OF DIRECTORS
FINANCE COMMITTEE

October 9, 2012
4:00 p.m.

Location: Board Room
Zone 7 Administration Building
100 North Canyons Parkway
Livermore, CA 94551

Director Figuers
Director Machaevich
Director Ramirez Holmes

A G E N D A

1. Public Comment

2. Reserve Fund Policy

3. Staff Reports –
   a) Information Replying to Inquiry About Untreated Water
   b) Background Information on Water Rates

4. Verbal Reports

5. Adjournment

10/4/2012

ALAMEDA COUNTY FLOOD CONTROL AND WATER CONSERVATION DISTRICT, ZONE 7
100 NORTH CANYONS PARKWAY • LIVERMORE, CA 94551 • PHONE (925) 454-5000 • FAX (925) 454-5727

DATE: October 9, 2012

TO: Finance Committee

FROM: Tom Hughes, Assistant General Manager
Tamara Baptista, Financial and System Services Manager
JaVia Green, Staff Analyst

SUBJECT: **Proposed Revisions to the Current Zone 7 Reserve Policy**

SUMMARY:
The Zone 7 Board of Directors (Board) adopted a Reserve Fund Policy in March 2005 that set forth the principals to be followed in creating and maintaining reasonably prudent reserves for conducting the Agency's business (Attachment A). During the 2012 water rate development process, on October 5, 2011, the Board reviewed current reserves policies and levels. This agenda item is attached as Attachment B and gives additional background information on Zone 7 reserve funds.

On November 16, 2011, the Board adopted a Financial Management Framework which includes planning for current operating and capital resource needs to ensure it can achieve its mission by providing for financial stability and health of the Agency. One of the framework's goals is to be able to respond to changes in the economic environment and service demands with minimal impact on its customers while maintaining the financial integrity of the Agency.

As part of the 2013 water rate process, Board members requested a closer look at reserves related to water system funds, particularly the Water Enterprise Fund (Fund 52). This agenda item provides additional details on water system fund reserve balances as of 6/30/12 and includes proposed revisions to the March 2005 Fund Policy to reflect current conditions, in keeping with the November 16, 2011, Financial Management Framework (Attachment C).

BACKGROUND:
Reserve funds generally fall into three categories – restricted, designated and unrestricted. Restricted reserves have their use imposed by an outside entity such as debt service reserves which are governed by bond covenants. Board-designated reserves, although they have no externally-imposed restrictions, have internally designated purposes.

The State Water Project Fund (Fund 51) receives property tax revenue to pay for voter approved State Water Project fixed costs. No changes are being recommended to this fund's reserve; however, since it is a water system fund, the reserve balance is shown in Table 1 below:

Table 1 – Fund 51 Unaudited Reserve Balances as of 6/30/2012	
Reserve	Unaudited Balance as of 6/30/12
Designated for State Water Project Fixed Costs	$10,603,823
Total Reserve	$10,603,823

The Reserve Fund Policy established several Board designated reserves for specific purposes within Fund 52. Fund 52 reserves and their respective unaudited balances are shown in Table 2 below:

Table 2 – Fund 52 Unaudited Reserve Balances as of 6/30/2012	
Reserve	Unaudited Balance as of 6/30/12
Operating/Emergency Reserves	$6,708,414
Rate Stabilization Reserve	$5,000,000
Designated Reserves	$ -
Unrestricted Reserves (includes Encumbrances)	$15,544,541
Total Reserves	$27,252,955

Water rate revenue provides funding for the Renewal and Replacement/System-wide Improvements Fund (Fund 72). For reference, reserve balances in Fund 72 are shown in Table 3, below:

Table 3 – Fund 72 Unaudited Reserve Balances as of 6/30/2012	
Reserve	Unaudited Balance as of 6/30/12
Capital Projects and Contingencies	$19,041,132
Sinking Fund	$2,691,980
Total Reserves	$21,733,112

Water system expansion (Fund 73) is funded by connection fees from new development, in keeping with the Board policy that new development pays for itself. Staff recommends revisions to the Capital Projects and Contingencies Reserve, so for reference, reserve balances in Fund 73 are shown in Table 4, below:

Table 4 – Fund 73 Unaudited Reserve Balances as of 6/30/2012	
Reserve	Unaudited Balance as of 6/30/12
Capital Projects and Contingencies	$12,287,426
Sinking Funds	$8,994,748
Installment Sale Agreement (ISA)	$30,500,000
Total Reserves	51,782,174

The above tables represent all of the water system operating and capital funds.

DISCUSSION:

Water rates fund water related operating and capital expenses. Fund 52 is the operating and maintenance fund for the water enterprise system and Fund 72 is a water system capital fund for existing infrastructure. Fund 52 generates revenue from water sales to fund cost of service. The cost of service includes Fund 52 operating expenses and the annual capital transfer to Fund 72. The transfer to Fund 72 is based on the Asset Management Program (AMP) funding schedule adopted by the Zone 7 Board on June 15, 2011 and as shown below:

$6.6 million in FY12/13;
$8.5 million in FY13/14;
$9.5 million in FY 14/15;
$10.5 million in FY 15/16; and
Beginning in FY16/17 and beyond, $11.4 million (in 2011 dollars) to be adjusted by other sources of revenue, inflation and any future AMP updates.

In general, annual water sales revenue should be sufficient to cover operating expenses and the pre-established transfer (together, cost of service). Since operating expenses and the capital transfer have increased over time, and water usage has decreased, Zone 7 plans for a combination of water rate increases and use of unrestricted reserves to fund cost of service. The unrestricted reserve functions similar to a Rate Stabilization Reserve. This type of reserve is typically used to smooth rate increases.

A Drought Contingency Reserve is used to supplement losses to water sales revenue resulting from drought conditions or a natural disaster. The current reserve policy designates the Rate Stabilization Reserve for this purpose. Staff recommends revising the current policy to reflect the appropriate purposes of the Rate Stabilization and Unrestricted Reserves. It is recommended that the current Rate Stabilization Reserve be designated as the Drought Contingency Reserve and to be used to supplement losses to water sales revenue resulting from drought conditions. It is further recommended that the Unrestricted Reserve is designated as the Rate Stabilization Reserve to be drawn down as needed to smooth rate increases. The proposed Rate Stabilization Reserve will include encumbrances for outstanding purchase orders for goods and services.

Within the Capital Projects and Contingencies Reserve, staff recommends establishing minimum reserve levels for Fund 72 and Fund 73 to ensure funding is available to fund current and future projects. These targets are currently used for capital planning purposes, so staff recommends formally incorporating them into the reserve policy. The minimum reserve balance for Fund 72 is proposed to be no less than 75% of the following year's capital transfer. This fund shall accumulate sufficient reserves to pay for future projects set forth in the AMP and the reserve balance shall be consistent with the reserve balances forecasted in the 2011 AMP Update and subsequent updates. For the Water Expansion Fund, a minimum reserve balance is proposed to be set at 50% of the following year's non-discretionary expenditures.

A draft Reserve Fund Policy is attached as Attachment D. Staff requests the Finance Committee to discuss the recommended policy revisions and provide staff with direction on when and how to proceed.

Attachments:
Attachment A – Current Zone 7 Reserve Policy
Attachment B – October 5, 2011 Board Agenda Item – Status of Reserve Funds
Attachment C – Draft Zone 7 Financial Management Framework
Attachment D – Draft Zone 7 Reserve Policy Revision

ATTACHMENT A
Current Zone 7 Water Agency
Reserve Fund Policy

Policy Statement

Zone 7 of the Alameda County Flood Control and Water Conservation District has adopted a Financial Management Policy which includes planning for current operating and capital resource needs to ensure it can achieve its mission by providing for financial stability and health of the Agency. Among the stated goals is to be able to respond to changes in the economic environment and service demands with minimal impact on its customers while maintaining the financial integrity of the Agency.

Key elements of prudent financial planning include ensuring sufficient funding is available for current operating, capital and debt service costs; anticipating and preparing for future funding needs; and allowing for unforeseen disasters and other unforeseen events.

Zone 7 will maintain reserve funds to ensure it can fund emergency expenses; cash flow requirements; capital improvement plans and future operating requirements while avoiding significant rate fluctuations due to changes funding needs. It will also maintain a cash reserve position that may be utilized to fund unexpected fluctuations in revenue and operating/capital expenditures. Staff will review the amount of reserves recommended each year with the Board of Directors at the presentation of the annual Agency budget.

Definitions

- <u>Restricted Reserves:</u> Restrictions imposed by an outside source. May be required by bond covenants in the case of debt issuance.
- <u>Designated Reserves:</u> Set aside for a specific purpose determined by the Board of Directors. The Board of Directors has the authority to redirect the use of these funds as needs of the Agency change.
- <u>Unrestricted Reserves:</u> Have no imposed restrictions as to their use.

Designated Reserve Funds

- <u>Emergency/Operating Reserves:</u> Designated by the Board of Directors to provide for emergencies and cash flow requirements. The amount of these reserves is determined by the fund to which they apply. The water enterprise is maintained at 20% of operating expenses; flood control estimated at flood repair cash flow needs; and the State Water Project at 50% of revenue.
- <u>Rate Stabilization:</u> Designated by the Board of Directors to provide funds in the case of an unforeseen event such as a natural disaster, water shortage or other catastrophic event. Use of these funds is approved by the Board of Directors.

- <u>Designated Reserve:</u> Designated by the Board of Directors to provide for increases in operating expenses in excess of the target established by the Board. The Board authorizes use of these funds.
- <u>Capital Projects and Contingencies Reserve:</u> These reserves are earmarked by the Board of Directors for capital improvements to meet regulatory requirements, system reliability and future demand. These capital improvements are included in the 10 year Capital Improvement Program and the Asset Management Program both of which are reviewed by the Board of Directors each fiscal year. These reserves are also used to fund unanticipated capital projects. Use of these funds is approved by the Board of Directors.

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ATTACHMENT B

ORIGINATING DIVISION: Finance and Business Services
CONTACT PERSON: Tamara Baptista/John Yue

AGENDA DATE: October 5, 2011 ITEM NO. 4

SUBJECT: **Status of Reserve Funds**

SUMMARY:

- On August 29, 2011, and September 13, 2011, the Finance Committee met for staff presentations of the preliminary treated water rates for calendar year 2012.
- The Finance Committee discussed the alternatives presented, and directed staff to forward for the Board's discussion a recommendation of a 5% increase to the treated water rate for 2012.
- After discussion at the Board meeting September 21, 2011, the Board requested a special Board meeting to discuss the status of reserve funds prior to finalizing the treated water rate.

FUNDING:

Reserves, commonly referred to as working capital, come from the accumulated balances (surpluses) of the respective Funds over time. The Water Enterprise (Fund 52), Renewal/Replacement & System-Wide Improvements (Fund 72), Expansion (Fund 73) and State Water Facilities (Fund 51) have distinct reserves in the respective Funds.

RECOMMENDED ACTION:

Receive the presentation and discuss the reserve funds status.

x:/sec2/bl/prelim water rate 2012.doc

M E M O R A N D U M

DATE: October 5, 2011
TO: Jill Duerig, General Manager
FROM: Tamara Baptista and John Yue
SUBJECT: **Reserve Funds**

SUMMARY:

Key elements of prudent financial planning include ensuring sufficient funding is available for current operating, capital and debt service costs; anticipating and preparing for future funding needs; and allowing for unforeseen disasters and other unforeseen events.

BACKGROUND:

In governmental accounting, there are generally three categories of reserves.

1. Restricted Reserves: Restrictions are imposed by an outside source. For example, it may be required by bond covenants in the case of debt issuance. Zone 7 currently has no restricted reserves.

2. Designated Reserves: Set aside for a specific purpose determined by the Board of Directors. The Board of Directors has the authority to redirect the use of these funds as needs of the Agency change.

3. Unrestricted Reserves: Have no imposed restrictions as to their use.

In considering such general definitions and other best management practices, the Zone 7 Board of Directors adopted a Financial Management Policy in March 1999 that documented the principals to be followed in conducting the financial activities of Zone 7. A copy of the adopted Financial Management Policy and minute order are enclosed (Attachment A). In summary, these principals fell into the general categories of financial management goals, budgeting (to ensure a balanced budget, reserves for emergencies and cash sufficient to pay bills on a timely basis), revenue policies (to ensure that funds are available so that the Agency can accomplish its mission), expenditure policies (to ensure the Agency adheres to its spending plans and effectively manages its services) and policies related to capital improvement and expansion funding (to ensure that assets are properly maintained, replaced and expanded over time to meet the level of service expectations of the community). The expansion policy itself is consistent with the Mitigation Fee Act (Government Code §66000, *et seq.*) which requires that any fees collected from developers be kept in a separate fund and that these fees shall not be commingled. Annual reports must be prepared and published within 120 days of the end of each Fiscal Year. Typically, these reports are presented to the Board at the regular December meeting. Generally Accepted Accounting Principles for Government also calls for separate accounting and reporting of government functions (Flood Control – Funds 50 and 76) and proprietary functions (Water – Funds 51, 52, 72 and 73).

In March 2005, the Board expanded the Financial Management Policy by adopting a Reserve Fund Policy. The policy and minute order are attached (Attachment B). The Reserve Fund Policy established several Designated Reserve funds for various specific purposes related to the water enterprise and, thus, water rates. The purpose of each is described in the policy.

- Emergency/Operating Reserves: Designated by the Board of Directors to provide for emergencies and cash flow requirements. The amount of these reserves is determined by the fund to which they apply. This reserve is maintained at 20% of operating expenses; Flood Control estimated at flood repair cash flow needs; and the State Water Project at 50% of revenue.

- Rate Stabilization: Designated by the Board of Directors to provide funds in the case of an unforeseen event such as a natural disaster, water shortage or other catastrophic event. Use of these funds is approved by the Board of Directors.

- Designated Reserve: Designated by the Board of Directors to provide for increases in operating expenses in excess of the target established by the Board. The Board authorizes use of these funds. [Note that there are no funds in this reserve at present.]

- Capital Projects and Contingencies Reserve: These reserves are earmarked by the Board of Directors for capital improvements to meet regulatory requirements, system reliability and future demand. These capital improvements are included in the 10-Year Capital Improvement Program and the Asset Management Program both of which are reviewed by the Board of Directors each fiscal year. These reserves are also used to fund unanticipated capital projects. Use of these funds is approved by the Board of Directors.

The Water Enterprise Fund (52) generates revenue from water sales to fund the operating expenses and transfer capital contribution, in accordance with the funding levels determined by the Asset Management Plan (AMP), to fund Renewal/Replacement & System-Wide Improvements (R/R&SWI) projects (Fund 72). As the AMP projects are fully integrated with the 10-Year Capital Improvement Program (CIP), the reserves in the R/R&SWI Fund are wholly designated for capital projects identified in the CIP.

The Expansion Fund (73) and State Water Facilities Fund (51) are funded by water connection fee revenue, and property taxes, respectively. These two Funds have no impact on the funding requirements of Water Enterprise or R/R&SWI Funds, and therefore have no effect on water rates. The discussion below will focus mainly on the Water Enterprise reserves, and review the use of capital in R/R&SWI Funds.

The following summarizes the unaudited balance as of June 30, 2011, in each of the three general categories of Restricted, Designated and Unrestricted reserves in the Water Enterprise and R/R&SWI Funds.

1. Restricted Reserves – None in either funds
2. Designated Reserves
    a. Emergency/Operating Reserves – Applicable to Fund 52 only, $7,333,506
    b. Rate Stabilization - Applicable to Fund 52 only, $5,000,000

c. Designated – Applicable to Fund 52 only, none

d. Capital Projects & Contingencies – Applicable to Fund 72 only, $16,543,984

e. Sinking Funds - Applicable to Fund 72 only, $2,313,878 (building)

3. Unrestricted Reserves - Applicable to Fund 72 only, $7,577,506

DISCUSSION:

The Government Finance Officers Association (GFOA) cites the following major reasons for adopting a reserve (fund balance) policy:

1) Plan for contingencies
2) Maintain good standing with rating agencies
3) Avoid interest expenses for operating budget needs and capital projects
4) Invest fund balance
5) Ensure cash availability when revenue is unavailable

The GFOA also notes that, "A government's unreserved fund balance should be inversely proportional to its total budget size."

There are a variety of factors to consider when determining the unrestricted reserve fund balance, including:

a) The predictability of revenues and volatility of its expenditures
b) The availability of resources in other funds as the potential drain on the General Fund
c) Liquidity
d) Designations[1]

For additional reference, California Special District Association's Special District Reserve Guidelines is attached.

A review of other water agencies' reserves policies reveal a diverse range of reserve types and levels. This reflects the differing considerations contemplated by each agency's unique financial management and other policies, and make-up of revenue and expense components. Additionally, target or minimum-maximum amounts for identified reserves are not readily described in policy statements. For example, the proportion of volumetric revenue; use of debt or pay-as-you-go; and size of the agency. These varying considerations make for an imperfect benchmarking comparison. In an attempt to determine the range of reserves budgeted in other water agencies, a basic measure looking at the amount of reserves as a percentage of annual operating budget was used. The results ranged from 13% (Sonoma County Water Agency) to 80% (Contra Costa Water Agency). Based on a 5% water rate increase scenario for 2012, the Water Enterprise Fund reserves is projected at 52% of the annual operating budget.

Water Enterprise Reserves

[1] Appropriate Level of Unreserved Fund Balance in the General Fund (2002) GFOA Recommended Practice

As previously outlined, the Water Enterprise Fund (52) has the following Designated and Unrestricted Reserves for FY10/11 (unaudited actuals), and FY11/12 (projected assuming a 5% water rate increase for 2012):

Water Enterprise Fund (52)	Unaudited Actuals Ending Balance FY10/11	Projected Reserves Ending Balance FY11/12
Designated Reserves		
Rate Stabilization Reserve	$5.0 Million	$5.0 Million
Operating/Emergency Reserve	$7.3 Million	$6.7 Million
Designated Reserve	$0	$0
Unrestricted Reserve	$7.6 Million	$5.6 Million
Total	$19.9 Million	$17.3 Million

Approximately $2.0 million of the FY10/11 and FY11/12 Total Reserve balances is set aside for anticipated future Bay-Delta related expenses based on estimated costs received from DWR and other Delta-related expenses.

Under the Reserve Fund Policy, the Operating/Emergency Reserve is currently targeted at 20% of the annual operating budget. Given the current budget, 20% is a target level of $6.7 million. A recent Water Research Foundation survey of water agencies' Internal Financial Policies performed in the first quarter of 2011 recommends a working capital reserve of greater than or equal to 3 months (or 33%) of annual operating and maintenance expenses. The Unrestricted and Designated (not Rate Stabilization or Operating/Emergency) Reserves are typically used for planned budget smoothing. A prescribed target amount for the Designated Reserve at, say, 10% of the annual operating budget, can facilitate absorption of budget bumps in the future. Another way of looking at this is that while 20% may be low for an Operating/Emergency Reserve, taken together with the Unrestricted Reserve, the total reserve might be considered $12.3 million, or 37% of the operating budget.

The Water Research Foundation survey also suggests that a contingency/rate stabilization-type reserve should be targeted at 20% of the annual water volume revenues. If applied to Zone 7, the Rate Stabilization Reserve could be targeted at $6.4 million (20% of projected FY10/11 water volume revenue). Applying this guideline, the current level of $5,000,000 might be considered low. A higher target level makes some sense given that over the last dozen years, actual deliveries have varied from 80% to 106% of the requested deliveries. Given the unpredictability of revenue plus the significant swings in water costs (budgets are based on normal operations but there are major variations in hydrology and allocations; taken with the desire to store as much as possible both in-basin as well as in Semitropic and Cawelo, when the water is available), a larger Rate Stabilization Reserve could make sense.

Renewal/Replacement & System-Wide Improvements Working Capital

The recent AMP study established an annual transfer amount for capital projects. Establishing an annual amount preserves rate stability even when actual capital expenditures may vary. The R/R&SWI Fund (72) has the following Designated and Unrestricted Reserves for FY10/11 (unaudited actuals), and FY11/12 (projected assuming a 5% water rate increase for 2012):

Renewal/Replacement & System-Wide Improvements Fund (72)	Unaudited Actuals Ending Balance FY10/11	Projected Reserves Ending Balance FY11/12
Designated Reserves		
Capital Projects and Contingencies Reserve	$16.5 Million	$14.6 Million
Building Sinking Fund	$2.3 Million	$2.7 Million
Unrestricted Reserve	$0	$0
Total	$18.8 Million	$17.3 Million

The working capital amount is based on the funding needs of capital projects as described in the 10-Year CIP for R/R&SWI. The CIP is updated, reviewed, and adopted by the Board every two years. The 40-year AMP (most recently adopted by the Board in June 2011) to maintain, renew, replace and improve existing assets is periodically updated to reflect necessary and changing project needs and related funding. As the AMP projects are systematically incorporated into the 10-Year CIP for R/R&SWI, the Designated Reserve levels in this Fund is maintained at a level necessary to carry out the planned projects without any excess or Unrestricted Reserve.

The use of these various reserve funds over the last several years is shown in a series of graphs, along with a table showing existing Water Enterprise reserves and different options which are attached.

RECOMMENDED ACTION:

Receive the presentation and discuss the reserve funds status.

Attachments:
A – Financial Management Policy
B – Reserve Fund Policy
Historical Use of Reserves and Balances – Funds 52 and 72
Existing Reserves and Various Options
CSDA Special District Reserve Guidelines

ATTACHMENT C

Financial Management Framework

1. Purpose

To direct staff to prudently manage Zone 7's funds and to maintain financial and accounting records of all transactions in accordance with generally accepted accounting principles.

To adequately plan for the funding of current and future operational requirements and capital resources necessary to achieve the Agency's mission.

To provide staff with a framework to develop policies and procedures to ensure Zone 7's mission by providing financial health and stability to the Agency.

To direct staff that the assessment, levy and collection of taxes, the adoption of the Agency budget, and the appropriation, accounting, and transfer of funds shall be governed by general law and in accordance with generally accepted accounting principles and practices.

2. Administration of the system

In keeping with Resolution No. 09-3266, which states that "The Agency's General Manager has full charge and control of the day-to-day management, operation and administration of the Agency," the General Manager shall retain primary jurisdiction, responsibility, and authority for all matters pertaining to the day-to-day financial management of the Agency. To direct, control, supervise, and manage the development, preparation, organization, administration, operation, implementation, and maintenance of a comprehensive financial management program for Zone 7 Water Agency, the General Manager shall be designated as the fiscal officer of the Agency.

The General Manager may delegate any of the powers and duties conferred upon him or her as fiscal officer to any other employee of the Agency or may recommend that such powers and duties or any part of them be performed under contract.

3. Security of the system

The General Manager shall cause an audit of the financial transactions and records of the Agency to be made at least annually by a third party certified public accountant (i.e., one not employed by the Agency). As soon as possible at the end of each fiscal year a final audit and report shall be completed and submitted to the Board of Directors. Copies shall be placed on file in the office of the General Manager and be available for public inspection.

The General Manager shall also prepare such additional reports as the Board of Directors may from time to time request for information and use in setting financial policies for the Agency.

Attachment D
Zone 7 Water Agency
DRAFT Reserve Fund Policy

Policy Statement

The Zone 7 Board of Directors adopted a Reserve Fund Policy in March 2005 that set forth the principals to be followed in creating and maintaining reasonably prudent reserves for conducting the agency's business.

On November 16, 2011, the Zone 7 ~~of the Alameda County Flood Control and Water Conservation District~~Board ~~has~~ adopted a Financial Management ~~Policy~~ Framework which includes planning for current operating and capital resource needs to ensure it can achieve its mission by providing for financial stability and health of the Agency ~~(copy attached)~~. ~~Among the stated goals is to be able to respond to changes in the economic environment and service demands with minimal impact on its customers while maintaining the financial integrity of the Agency.~~ The ~~following updates the March~~following updates the March 2005 Reserve Fund Policy has been revised to reflect current conditions, in keeping with the November 16, 2011, Financial Management Framework.

One of the Framework's goals is to be able to respond to changes in the economic environment and service demands with minimal impact on its customers while maintaining the financial integrity of the Agency.

Key elements of prudent financial planning include ensuring sufficient funding is available for current operating, capital and debt service costs; anticipating and preparing for future funding needs; and allowing for unforeseen disasters and other unforeseen events.

Zone 7 will maintain reserve funds to ensure it can fund emergency expenses; cash flow requirements; capital improvement plans and future operating requirements while avoiding significant rate fluctuations due to changes funding needs. It will also maintain a cash reserve position that may be utilized to fund unexpected fluctuations in revenue and operating/capital expenditures. Staff will review the amount of reserves recommended each year with the Board of Directors at the presentation of the annual Agency budget.

Definitions

- Restricted Reserves: Restrictions imposed by an outside source. May be required by bond covenants in the case of debt issuance.
- Designated Reserves: Set aside for a specific purpose determined by the Board of Directors. The Board of Directors has the authority to redirect the use of these funds as needs of the Agency change.
- Unrestricted Reserves: Have no imposed restrictions as to their use.

~~Designated~~ Reserve Funds

- Emergency/Operating Reserves: Designated by the Board of Directors to provide for emergencies and cash flow requirements. The amount of these reserves is determined by the fund to which they apply. The water enterprise is maintained at 20% of operating expenses; flood control estimated at flood repair cash flow needs; and the State Water Project at 50% of revenue.

- Drought Contingency Reserve: ~~(previously Rate Stabilization Reserve):~~ Water sales revenue may be impacted under drought conditions due to regulatory or State and Federal mandated reductions in supply or in the case of an unforeseen event such as a natural disaster, water shortage or other catastrophic event. This reserve will supplement losses to water sales revenue resulting from drought conditions. The balance may be increased or decreased as authorized by the Board based on the continuance and severity of a drought.

- Rate Stabilization: ~~(previously Unrestricted Reserve):~~ The Rate Stabilization Reserve is a means to provide more stable water rates; it will be drawn down as needed to smooth rate increases. This reserve will be used to accumulate revenues for use during periods of unanticipated fluctuations in treated water rate revenues. It provides a buffer should actual revenue in any year not meet projections. The use of the reserve shall be in accordance with budget authorizations. This reserve will also include encumbrances for outstanding purchase orders.

- Designated Reserve: Designated by the Board of Directors to provide for increases in operating expenses in excess of the target established by the Board. The Board authorizes use of these funds.

- Capital Projects and Contingencies Reserve: These reserves are earmarked by the Board of Directors for capital projects to meet regulatory requirements and ~~,~~ system reliability. Reserves accumulated in the Water Expansion Fund and Flood Protection and Stormwater Drainage Development Impact Fee Fund are earmarked for projects that address the impacts of future demands ~~and future demand~~. ~~-~~These capital improvements are included in the 10~~-~~-year Water System and 5-year Flood Protection Capital Improvement Program ~~Capital Improvement Program, and~~ and the Asset Management Program (AMP) ~~and the 5-year Flood Capital Improvement Program,~~ all~~both~~ of which are reviewed by the Board of Directors each fiscal year. To ensure funding is available to fund future projects, a minimum reserve balance for the Water Renewal and Replacement/System-wide Improvements Fund is set at 75% of the following year's capital transfer ~~and as set forth in~~

~~the AMP~~. This fund shall accumulate sufficient reserves to pay for future projects set forth in the AMP and the reserve balance shall be consistent with the reserve balances forecasted in the 2011 AMP Update and subsequent updates. For the Water Expansion Fund, a minimum reserve balance is set at 50% of the following year's non-discretionary expenditures. These reserves are also used to fund unanticipated capital projects. Use of these funds is approved by the Board of Directors.

ALAMEDA COUNTY FLOOD CONTROL AND WATER CONSERVATION DISTRICT, ZONE 7
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DATE: October 9, 2012

TO: Finance Committee

FROM: Tom Hughes, Assistant General Manager
Tamara Baptista, Financial and System Services Manager
JaVia Green, Staff Analyst

SUBJECT: Staff Report – Information Replying to Inquiry About Untreated Water

On September 18, 2012, staff received an email from Dave Lunn, an indirect untreated water customer who is also a former Zone 7 employee who historically managed the untreated program. The questions follow:

1. Would you please provide some historic breakdown of the water costs and water quantities associated with the untreated water program so I can understand what costs are changing? It would be most helpful if this information was provided in a table that listed the components covering the 10 year period shown in the graph (or at least back to 2007 before the Bay-Delta related costs were added as a Delta Charge). Please include the volumes of treated and untreated water and not just the total water sales.

2. Please include the projected reduced administrative costs of the untreated water program under the new contract. Also please identify and describe the "pass through" costs and what general tasks are included in that item.

3. The Bay Delta costs are a significant part of the water cost. Would you provide a breakdown of the Bay Delta costs for this budget year including the costs of "outreach"? Is there a list of the outreach products provided and a link to those items? Is there an estimate of when these Delta costs may end?

4. Could you provide a comparison of the projected costs versus the actual costs for the program in 2011 and if possible an estimate of the projected costs for 2012? I realize that the SWP variable rate and some of the water volumes may change and the actual costs may be higher or lower than expected.

5. I looked at the web site for this information and could not find it. See here I found even less detail on the treated water agenda item. I even tried to find some of the information in the Budget but was unable to find the 2012-13 Budget listed on the web. Providing the information in a simple draft spreadsheet would be perfect.

First of all, annual budget information covering the last several years is on Zone 7's website at http://www.zone7water.com/component/content/article/36-content/161-our-annual-budget.

The proposed Delta surcharge for Calendar Year 2013 is $21 out of the total untreated water rate of $110 or a little less than 20%. Bay-Delta costs have been discussed and included every year since 2007 (first adopted for the 2008 calendar year) during both the Finance Committee and Regular Board meetings on water rates. The first year a percentage was applied but, after further public and retailer discussions, the percentage was determined to be inequitable as it resulted in untreated customers paying significantly less per acre foot than treated water customers. Since water for both untreated and treated water customers is conveyed through the Delta, expenses incurred as Zone 7's share of developing the Bay Delta Conservation Plan (BDCP), the Delta Habitat Conservation and Conveyance Program (DHCCP) and related environmental assessments and outreach programs have since been charged on a per acre foot basis.

It is not always possible to break down costs as requested. Since the Delta expenses have been shared by state and federal contractors, Zone 7 pays approximately 1% of the overall program costs (currently estimated at about $240 million). In addition, some local expenses have been incurred for staff to actively participate in the BDCP Steering Committee, the DHCCP business committee and joint outreach programs. When staffing does not allow full participation, outside services are sometimes used. These are tracked internally by job numbers and, together with projected billings from the California Department of Water Resources (DWR), used to establish the following year's Delta charge. Outreach often consists of giving presentations, participating in joint strategy sessions, staff time to prepare e-newsletters, maintaining Delta-specific websites or submitting OpEd pieces to the local papers. Actual products are available on the Zone 7 website (see, for example, http://www.zone7water.com/bay-delta-invisible-menu-218?task=view), the State Water Contractors website (http://www.swc.org/issues/delta-disrupted, for example) or the BDCP website (http://baydeltaconservationplan.com/Home.aspx). Outreach on Delta projects will likely continue through construction and start-up periods.

Projected administrative cost savings with the new ordinance have not yet been fully realized. However, it is important to note that administrative costs are a small portion of the overall untreated water rate ($10 of the total $110) so administrative cost savings are unlikely to have a major impact on untreated rates.

Some of the information requested requires extensive staff time due to the functionality of our current financial software. Tracking detailed information like this is one of our priorities for the new software which is planned to go live January 1, 2013.

ALAMEDA COUNTY FLOOD CONTROL AND WATER CONSERVATION DISTRICT, ZONE 7
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DATE: October 9, 2012
TO: Finance Committee
FROM: Tom Hughes, Assistant General Manager
Tamara Baptista, Financial and System Services Manager
JaVia Green, Staff Analyst

SUBJECT: Staff Report - Background Information on Other Water Rates

In addition to setting basic treated and untreated water rates each October, the Zone 7 Board also adopts a number of other treated and untreated water rates. A list of all the various rates, a description of each and the proposed Calendar Year 2013 amounts are shown below.

Municipal and Industrial Water Rates for Treated/Potable Water

Treated Water Rate (proposed 2013 rate, $945/AF for top/4th tier):
The treated water rate is the wholesale rate charged to retailers purchasing potable water from Zone 7. There is a service charge per metered service plus four tiers to capture differences between wholesale and direct, retail purchases. Generally, low volume users pay a higher unit cost due to the fixed costs being spread over a smaller volume of water, thereby increasing the cost per unit. The tiers are: the first 3,300 cubic feet, $3.875 per 100 cubic feet; the next 30,000 cubic feet, $3.102 per 100 cubic feet; for the next 300,000 cubic feet, $2.473 per 100 cubic feet and for all over 333,300 cubic feet, $2.169 per 100 cubic feet (or $945/AF). The service charge is $136.00 per month per metered service.

Recharge Fee (proposed 2013 rate, $611/AF):
The annual rate schedule includes a recharge fee for retailer pumping beyond the groundwater pumping quota (formerly, the Independent Quota). This rate applies to the retail agencies with which we have either treated water delivery contracts or Terms and Conditions for Supply. Groundwater allocations were developed in the 1960s and incorporated into the 1968 contracts as Exhibit C, "Statement of Principles and Method of Allocation of Safe Yield of the Livermore-Amador Groundwater Water Basin in the Determination of the Independent Quota." Basically, the natural or safe yield of the basin was allocated based on historical pumping and additional yield related to importing water and artificially recharging the basin could not be pumped without reimbursing Zone 7. The rate includes the Delta charge. This fee applies only when the Retailers exceed their groundwater pumping quota (GPQ). Historically, this fee has been rarely used and then only for small quantities since the retailers generally do not exceed their respective groundwater quota.

Temporary Treated (proposed 2013 rate, $1,688/AF or $3.875/100 cubic foot or per CCF):
The temporary treated water rate is based on the first tier of the scheduled treated water rate schedule. No increase is proposed in the 2013 treated water rate. The need for temporary services stems from the inability of customers to obtain water in the outlying areas of the valley. The use of these services is limited.

Fire and Standby Service (proposed 2013 rate, $1,688 per AF or $3.875 per CCF):
Each year the Board also sets a treated water schedule for fire and standby service for the Lawrence Livermore National Laboratory (LLNL). In 2004, the Board adopted the recommendation by staff that this rate be set at the first tier of the treated water rate, which is equivalent to the temporary treated water rate, with the application that LLNL must also pay the same monthly service charge of $136 per connection as the regular treated water contractors. Low volume users pay a higher unit cost due to the fixed costs being spread over a smaller volume of water, thereby increasing the cost per unit.

In-Lieu Water Rate (proposed 2013 rate, $93/AF)
In the event staff concludes that surplus surface water is available in 2013 and that it would be cost-effective to offer it to retailers at a reduced rate to achieve groundwater management objectives, in-lieu treated water could be offered. In-lieu water is treated water that the Retailers can purchase from Zone 7 instead of pumping their respective GPQ. This rate was established in 1993 to encourage artificial recharge when surplus surface water is available. The rate is based on the power and chemical costs at the Del Valle and Patterson Pass Water Treatment plants.

Untreated Water Rates

Untreated Water Rate (proposed 2013 rate, $110/AF)
The Untreated Water Rate is charged for State Project water that is delivered to irrigation customers without treatment (i.e., for nonpotable water). On November 16, 2011, Zone 7 adopted the Rules and Regulations Governing Untreated Water Service that clarifies its role with regard to remote untreated water customers. This is water served pursuant to those Rules and Regulations.

Temporary Untreated (proposed 2013 rate, $437 per AF or $1.34 per 1,000 gallons)
The need for temporary services results from the inability of customers to obtain water in the outlying areas of the valley. The use of these services is limited. The temporary untreated water rate is based on the estimated cost of water from the State Water Project, Bay-Delta costs and the Byron-Bethany Irrigation District divided by the estimated customer deliveries minus the estimated available water from the Del Valle reservoir plus an administrative cost component based on actual staff costs. The use of these services is limited.

Non-Scheduled Untreated Water (proposed 2013 rate, $437 per AF)
Non-scheduled water is all untreated water deliveries exceeding scheduled deliveries by more than 10% in any year. It is based upon the temporary untreated water rate.

Surplus Untreated (proposed 2013 rate, $232 per AF.)
Surplus water deliveries are available only in years when the supplies exceed our customer's demands. Tentative surplus water delivery requests are submitted to Zone 7 by March 15 of each year; availability of surplus water is determined in April; and actual deliveries are announced in May. The rate fluctuates depending on the source of the surplus. However, in order to establish a rate, staff is recommending that the rate for 2013 be maintained at the Byron-Bethany Irrigation District water transfer cost, the cost of transporting water, and the Bay-Delta charge of $21 per AF.