

Water Fund Reserve Policy

INTRODUCTION

Objective

This Water Fund Reserve Policy (or “Policy”) establishes policy parameters to guide the City’s Water Fund’s long term fiscal stability, including parameters for establishing and implementing the Water Fund Reserves. This Policy is intended to provide direction for the management of the City’s Water Enterprise Fund finances to establish reserves necessary to meet known and unknown future obligations.

Policy Areas

This Policy addresses the following areas:

1. Fiscal Policy Overview
2. Definitions
3. General Reserve Policies
4. Water Operating Fund Reserves
5. Water Capital Improvement Project (CIP) Fund Reserve
6. Unassigned Fund Balance

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1. Overview of Purpose and Scope of this Policy

- a. The purpose of this Policy is to establish appropriate reserve levels for the City's Water Fund.
- b. **Applicability.** This Policy applies solely to the Water Fund for the City of Napa.

2. Definitions. The definitions set forth below shall apply to this Policy. Unless otherwise defined in this Policy, the definitions and interpretations set forth in the Budget shall apply to this Policy.

- a. "Budget": An annual plan approved by the City Council of financial activity including anticipated expenditures and the estimated means to finance those expenditures. Budget appropriations are authorized by formal City Council action with any budget adjustments approved in accordance with the provisions of the City's Fiscal Policy.
- b. "Capital Improvement Program (CIP) Project Budget": The Budget includes a listing of all planned capital improvement projects by category.
- c. "Fund": An independent fiscal and accounting entity with a self-balancing set of accounts recording cash and/or other resources together with all related liabilities, obligations, reserves, and equities.
- d. "Fund Balance": The difference between assets and liabilities reported in a governmental fund.
- e. "Fund Balance Categories" per current governmental accounting standards (GASB 54):
 - i. "Non-Spendable": Cannot be readily converted to cash or cannot legally be spent
 - ii. "Restricted": External imposed (by granting agencies, governmental entities, etc.) restrictions on spending
 - iii. "Committed": City Council formally-imposed (by resolution or other action) restrictions on spending
 - iv. "Assigned": Funds reserved by Council direction or City Manager for designated purposes
 - v. "Unassigned": Residual balance not classified in any of the above categories
- f. "Non-Recurring": Revenues or expenditures not expected to recur on a regular basis; not to be included in the regular operating budget.
- g. "Water Fund": A proprietary enterprise fund operated by the City for the purpose of providing portable water service.
- h. "Water Fund Operating Budget": total Water Fund expenditure budget less expenditure budget for capital projects and Non-Recurring and less transfers to other Water funds and reserves.

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3. General Reserve Policies

- a. It is the intent of the City to establish and maintain reserve funds in the Water Fund to ensure the continued delivery of water services to address emergencies, address a temporary revenue shortfall or provide stability during economic cycles. Sufficient reserve funds will be managed to provide adequate cash flow, stabilize the City's interest rates, and provide continuity in service delivery. The City shall maintain adequate cash reserves in the Water Fund to maintain a positive cash position at any time during a fiscal year and at year-end.
- b. If fiscal changes require staff to recommend funding reserves that differ from the amounts identified in this Policy, staff will bring this recommendation to Council as a specific action for approval.

4. Water Operating Fund Reserves

- a. Operating Reserve. The City Council hereby authorizes the City Manager to maintain a Water Fund Operating Reserve in accordance with this Policy. The primary purpose of this Water Fund Operating Reserve is to cover day-to-day expenses and maintain sufficient funds to cover accounts payable if there are supplier issues, periods of low water sales, or unforeseen cost increases.
 - i. The Water Fund Operating Reserve shall be maintained at a level between a minimum of 12 percent and a maximum of 25 percent of the Water Fund Operating Budget.
 - ii. The use of the Water Fund Operating Reserve must be approved by the City Council.
 - iii. Each fiscal year, the Water Fund will include in the Budget a transfer from the Water Fund Operating Budget to the Water Fund Operating Reserve to bring the reserve balance to within the required level. However, this transfer may be excluded from the Budget to the extent necessary to avoid a budgeted deficit.
 - iv. Approved use of Water Fund Operating Reserve funds may cause the balance of the reserve to drop below the minimum percent level. The City will begin to restore reserves used under this Policy within 24 months after their first use. The proposed timing of repayment of reserves will be subject to approval by the City Council and will be included in the Water Fund Budget.
- b. Emergency Reserve. The City Council hereby authorizes the City Manager to maintain a Water Fund Emergency Reserve in accordance with this Policy. The primary purpose of this Water Fund Emergency Reserve is to protect the City's Water Fund during significant events such as (but not limited to) economic

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downturns/recessions/droughts that impact Water Fund revenues, natural disasters, declared emergencies (as defined by Napa Municipal Code Chapter 2.89), state government reductions or takeaways of Water Fund revenues, or other situations that could not be reasonably foreseen during preparation of the budget.

- i. The Water Fund Emergency Reserve shall be maintained at a minimum level of 10 percent of the Water Fund Operating Budget.
- ii. In the event the City Manager declares that action is needed to be taken to resolve an emergency, in accordance with Napa Municipal Code Section 2.91.040, the City Manager is authorized to encumber and spend the Water Fund Emergency Reserve to pay the costs of the action to resolve the emergency. These actions shall be reported to the City Council at their next meeting after the declaration of the emergency, and during the duration of the declared emergency in accordance with Napa Municipal Code Section 2.91.040.
- iii. In the case of natural disasters, the Water Fund Emergency Reserve may be used to pay for FEMA-approved projects. If used, the project total amount shall be transferred from the Emergency Reserve and deposited into the appropriate project fund.
 1. The City Manager is authorized to deposit any reimbursement funds received from FEMA and CalOES, into the Emergency Reserve to replenish the fund.
 2. The City Manager is authorized to initially fund the Water Fund's portion of FEMA projects from the Water Fund Emergency Reserve. The proposed timing of repayment will be included in the Water Fund's Budget.
- iv. The use of the Water Fund Emergency Reserve must be approved by the City Council. As an exception, in the situations described in 4.b.i and 4.b.ii above, the City Manager is authorized to use the Water Fund Emergency Reserve and then report to the City Council. All other situations require advance approval from the City Council.
- v. Each fiscal year, the City will include in the Budget a transfer from the Water Fund Operating Budget to the Water Fund Emergency Reserve to bring the reserve balance to a minimum of 10 percent of that year's Water Fund Operating Budget. However, this transfer may be excluded from the Budget to the extent necessary to avoid a budgeted deficit.
- iv. Approved use of Water Fund Emergency Reserve funds may cause the balance of the reserve to drop below the required 10 percent level. The City will begin to restore reserves used under this Policy within 24 months after their first use. The proposed timing of repayment of

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reserves will be subject to approval by the City Council and will be included in the Water Fund's Budget.

- c. **Rate Stabilization Reserve.** The City Council hereby authorizes the City Manager to maintain a Water Fund Rate Stabilization Reserve in accordance with this Policy. The primary purpose of this Water Fund Rate Stabilization Reserve is to provide funding to absorb revenue shortfalls due to short-term decreases in water sales due to drought or other circumstances.
 - i. The Water Fund Rate Stabilization Reserve shall be maintained at a minimum level of 10 percent of the Water Fund Operating Budget.
 - ii. The use of the Water Fund Rate Stabilization Contingency Reserve must be approved by the City Council.
 - iii. Each fiscal year, the City will include in the Budget a transfer from the Water Fund Operating Budget to the Water Fund Rate Stabilization Reserve to bring the reserve balance to a minimum of 10 percent of that year's Water Fund Operating Budget. However, this transfer may be excluded from the Budget to the extent necessary to avoid a budgeted deficit.
 - iv. Approved use of Water Fund Rate Stabilization Reserve funds may cause the balance of the reserve to drop below the required 10 percent level. The City will begin to restore reserves used under this Policy within 24 months after their first use. The proposed timing of repayment of reserves will be subject to approval by the City Council and will be included in the City's Long-Term Financial Forecast.
- d. **Water Supply Reserve.** The City Council hereby authorizes the City Manager to maintain a Water Fund Water Supply Reserve in accordance with this Policy. The primary purpose of this Water Fund Water Supply Reserve is to invest in future water supplies or to purchase supplemental water supplies during a drought or other circumstance where supplemental water supplies are necessary.
 - i. The Water Fund Water Supply Reserve shall be maintained at a minimum level of \$1,500,000.
 - ii. The use of the Water Fund Water Supply Reserve must be approved by the City Council.
 - iii. Each fiscal year, the City will include in the Budget a transfer from the Water Fund Operating Budget to the Water Fund Water Supply Reserve in the amount of \$200,000. However, this transfer may be excluded from the Budget to the extent necessary to avoid a budgeted deficit.
 - iv. The City will begin to restore reserves used under this Policy within 24 months after their first use. The proposed timing of repayment of

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reserves will be subject to approval by the City Council and will be included in the City's Long-Term Financial Forecast.

- e. In the event that budgeted revenue is not enough to fully fund all reserves, they shall receive funding in the following priority order: first the Water Fund Operating Reserve, then the Water Fund Emergency Reserve, then the Water Fund Rate Stabilization Reserve, then the Water Fund Water Supply Reserve.

5. Water Capital Improvement Program (CIP) Fund Reserve

- a. The City Council hereby authorizes the City Manager to maintain a Water Fund CIP Reserve in accordance with this Policy. The primary purpose of this Water Fund CIP Reserve is to provide funding for ongoing and future Capital Improvement Projects for the City's water system.
 - i. The Water Fund CIP Reserve shall be maintained at a minimum level of \$4,000,000.
 - ii. The use of the Water Fund CIP Reserve must be approved by City Council, generally through the CIP Budget adoption.
 - iii. Each fiscal year, the City will include in the Budget a transfer from the Water Fund Operating Budget to the Water Fund CIP in the minimum amount of \$6,000,000 less the budgeted amount of revenue to the Water Fund CIP Budget from capacity fees from new development. In Fiscal Year 2027-2028 and beyond, the minimum amount shall be increased to \$8,000,000 less the budgeted amount of revenue to the Water Fund CIP Budget from capacity fees from new development. However, this transfer may be reduced or excluded from the Budget to the extent necessary to avoid a budgeted deficit.

6. Unassigned Fund Balance

- a. The City Council hereby authorizes the City Manager to maintain an Unassigned Fund Balance in the Water Fund Operating and Non-Recurring Funds for the purpose of cash-flow and unforeseen changes in revenues and/or expenditures.
 - i. The use of Unassigned Fund Balance in the Water Fund must be approved by the City Council.
 - ii. At the end of each fiscal year, Unassigned Fund Balance exceeding \$3,000,000 in the Operating Fund or \$1,000,000 in the Non-Recurring Fund shall be transferred to fully fund other Water Fund Reserves in the following priority order: first the Water Fund Operating Reserve, then the Water Fund Emergency Reserve, then the Water Fund Rate Stabilization Reserve, then the Water Fund Water Supply Reserve, then the Water Fund CIP Reserve.