

**AGENDA**

**INVESTMENT AND FINANCE COMMITTEE MEETING  
LEUCADIA WASTEWATER DISTRICT**

February 1, 2021 – 1:00 p.m.  
Via Teleconference

Pursuant to the State of California Executive Order N-29-20, and in the interest of public health, the District is temporarily taking actions to mitigate the COVID-19 pandemic by holding meetings by teleconference. The general public may not attend this meeting at the District's office due to social distancing requirements.

Members of the public attending via teleconference will be provided with an opportunity to comment on each agenda item prior to Committee discussion.

**To join this meeting via Teleconference please dial: (669) 900-6833**  
**Meeting ID: 867 4533 0362      Password: 139779**

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1. **Call to Order**
2. **Roll Call**
3. **Public Comment**
4. **New Business**
  - A. Authorize the General Manager to execute a one-year contract amendment (contract amendment No 2) with Davis Farr LLP for Financial Auditing Services for Fiscal Year 2021 (FY21) in an amount not to exceed \$23,500. (Pages 2-11)
  - B. Annual Review of LWD Reserve Fund Policy. (Pages 12-17)
5. **Information Items**

None.
6. **Directors' Comments**
7. **General Manager's Comments**
8. **Adjournment**

## MEMORANDUM

Ref: 21-7484

**DATE:** January 28, 2021  
**TO:** Investment & Finance Committee  
**FROM:** Paul J. Bushee, General Manager  
**SUBJECT:** Contract Amendment No. 2 to Davis Farr LLP for Financial Auditing Services



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### RECOMMENDATION:

Staff requests that the Investment & Finance Committee (IFC) recommend that the Board of Directors:

1. Authorize the General Manager to execute a one-year contract amendment (contract amendment No 2) with Davis Farr LLP for Financial Auditing Services for Fiscal Year 2021 (FY21) in an amount not to exceed \$23,500.

### DISCUSSION:

On April 13, 2016, the Board of Directors authorized an initial three-year contract with Davis Farr LLP for financial auditing services for Fiscal Years ending 2016 through 2018, with the option to extend for two additional years. A two-year extension (contract amendment No.1) was subsequently approved by the Board on November 14, 2018 for Fiscal Years ending 2019 and 2020. During their service, Davis Farr LLP has worked closely with the District to conduct thorough financial audits.

It has been customary for the District to replace District auditors after five years of service. However, since Richard Duffey, the District Administrative Services Manager, who manages the District's Accounting and Financial functions will be retiring in July 2021, staff believes it is in the District's best interest to maintain continuity with our current auditing firm during this time.

Therefore, staff requests that the IFC recommend that the Board of Directors authorize the General Manager to execute a one-year contract amendment with Davis Farr LLP. The proposed Amendment No.2, which authorizes a one-year extension is attached for the Board's review. If approved, fees totaling \$23,500 will be included in the FY 2022 budget.

PJB:

Attachment

**AMENDMENT NO. 2  
TO THE PROFESSIONAL SERVICES AGREEMENT  
BETWEEN THE LEUCADIA WASTEWATER DISTRICT  
AND DAVIS FARR LLP  
FOR FINANCIAL AUDITING SERVICES**

Ref: 21-7486

This Amendment No. 2 to the AGREEMENT is made and entered into this 10th day of February, 2021 between the LEUCADIA WASTEWATER DISTRICT, hereinafter referred to as DISTRICT, and DAVIS FARR LLP, a Certified Public Accounting firm, hereinafter referred to as CONSULTANT.

WHEREAS, the DISTRICT and CONSULTANT entered into an AGREEMENT on April 13, 2016 for financial auditing services; and

WHEREAS, the AGREEMENT was extended for an additional two-years on November 14, 2018.

WHEREAS, the DISTRICT has determined that a one-year extension is in the best interest of the District.

NOW THEREFORE, in consideration of their mutual promises, obligations, and covenants hereinafter contained, DISTRICT and CONSULTANT agree to amend the AGREEMENT as follows:

**ARTICLE 2: SERVICES TO BE PERFORMED BY CONSULTANT**

The Scope of Work shall be amended to include financial auditing services for an additional one-year period for the fiscal years ending June 30, 2021 as described in Exhibit A.

**ARTICLE 4: COMPENSATION**

Compensation for all work performed under Amendment No. 1 shall be calculated on a time and materials basis. Compensation for the services described in this AMENDMENT shall not exceed \$23,500.00. This amount shall be added to the previous amount to bring the total not to exceed amount for the AGREEMENT to \$135,350.00. This amount shall not be exceeded unless there is a change in scope of work, in writing and agreed to by both parties.

All other terms and conditions of the Agreement shall remain unchanged.

IN WITNESS WHEREOF, the parties hereto caused this AGREEMENT to be executed the day and year first above written.

**LEUCADIA WASTEWATER DISTRICT**

**DAVIS FARR LLP**

By: \_\_\_\_\_  
Paul J. Bushee  
General Manager

By: \_\_\_\_\_  
Shannon Ayala  
Engagement Partner



**Davis Farr LLP**  
2301 Dupont Drive | Suite 200 | Irvine, CA 92612  
Main: 949.474.2020 | Fax: 949.263.5520

**December 29, 2020**

**To the Board of Directors  
Leucadia Wastewater District  
1960 La Costa Avenue  
Carlsbad, CA 92008**

We are pleased to confirm the arrangements of our engagement and the nature of the services we will provide **Leucadia Wastewater District** (the "Entity").

**ENGAGEMENT OBJECTIVES**

We will audit the financial statements Entity's comprehensive annual financial report, as of **June 30, 2021** and for the year then ended, and the related notes to the financial statements.

Accounting Standards generally accepted in the United States of America ("US GAAP") provide for certain required supplementary information ("RSI"), such as management's discussion and analysis ("MD&A"), to supplement the Entity's basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. As part of our engagement, we will apply certain limited procedures to the Entity's RSI in accordance with auditing standards generally accepted in the United States of America ("US GAAS"). These limited procedures will consist of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We will not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance. The following RSI is required by US GAAP and will be subjected to certain limited procedures but will not be audited.

1. Management's Discussion and Analysis
2. Schedule of the District's Share of the Proportionate Net Pension Liability and Related Ratios
3. Schedule of Pension Plan Contributions
4. Schedule of Net OPEB Liability
5. Schedule of OPEB Contributions

We have also been engaged to report on supplementary information other than RSI that accompanies the Entity's financial statements. We will subject the following supplementary information to the auditing procedures applied in our audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America, and we will provide an opinion in relation to the financial statements as a whole.

1. Combining Schedule of Changes in Net Position

The following other information accompanying the financial statements will not be subjected to the auditing procedures applied in our audit of the financial statements, and for which we will not provide an opinion on or any assurance.

1. Introductory Information
2. Statistical Information

### **OUR RESPONSIBILITIES**

The objective of our audit is the expression of an opinion as to whether the financial statements are fairly presented, in all material respects, in conformity with US GAAP and to report on the fairness of the additional information referred to above when considered in relation to the financial statements taken as a whole.

We will also provide a report, which does not include an opinion on, Internal controls related to the financial statements and compliance with the provisions of laws, regulations, contracts, and grant agreements, noncompliance which could have a material effect on the financial statements as required by *Government Auditing Standards*. The report on internal control and compliance will each include a paragraph that states the report is solely to describe the scope and testing of internal control over financial reporting and compliance, and the results of that testing and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance and the results of that testing and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance and that the report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering internal control over financial reporting and compliance and that the report is not suitable for any other purpose.

### **Audit**

Our audit will be conducted in accordance with US GAAS, the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our audit will include tests of the accounting records and other procedures we consider necessary to enable us to express such an opinion and render the required reports. We cannot provide assurance that an unmodified opinion will be expressed. Circumstances may arise in which it is necessary for us to modify our opinion or add an emphasis-of-matter or other-matter paragraph. If, for any reason, we are unable to complete the audit, or are unable to form or have not formed an opinion, we may decline to express an opinion or withdraw from this engagement.

Our procedures will include tests of documentary evidence supporting the transactions recorded in the accounts (e.g., tests of the physical existence of inventories, direct confirmation of certain assets and liabilities by correspondence with selected customers, creditors, and financial institutions, etc.). We may also request written representations from the Entity's attorneys as part of the engagement, and they may bill the Entity for responding to this inquiry.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.



We will plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether from errors, fraudulent financial reporting, misappropriation of assets, or violations of laws or governmental regulations that are attributable to the Entity or to acts by management or employees acting on behalf of the Entity.

Because of the inherent limitations of an audit, combined with the inherent limitations of internal controls, and because we will not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us, even though the audit is properly planned and performed in accordance with US GAAS. In addition, an audit is not designed to detect immaterial misstatements or violations of laws or governmental regulations that do not have a direct and material effect on the financial statements. We will inform the appropriate level of management and those charged with governance of any material errors, fraudulent financial reporting, or misappropriation of assets that comes to our attention. We will also inform the appropriate level of management and those charged with governance of any violations of laws or governmental regulations that come to our attention, unless clearly inconsequential, and any material abuse that comes to our attention. Our responsibility, as auditors, is limited to the period covered by our audit and does not extend to any later periods for which we are not engaged as auditors.

#### **Internal Control**

Our audit will include obtaining an understanding of the government and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Tests of controls may be performed to test the effectiveness of certain controls that we consider relevant to preventing and detecting errors and fraud that are material to the financial statements and to preventing and detecting misstatements resulting from illegal acts and other noncompliance matters that have a direct and material effect on the financial statements. Our tests, if performed, will be less in scope than would be necessary to render an opinion on internal control and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to *Government Auditing Standards*.

An audit is not designed to provide assurance on internal control or to identify significant deficiencies or material weaknesses. Accordingly, we will express no such opinion. However, during the audit, we will communicate to management and those charged with governance internal control related matters that are required to be communicated under AICPA professional standards and Government Auditing Standards.

#### **Compliance**

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we will perform tests of the Entity's compliance with the provisions of applicable laws, regulations, contracts, agreements, and grants. However, the objective of our audit will not be to provide an opinion on overall compliance, and we will not express such an opinion in our report on compliance issued pursuant to *Government Auditing Standards*.

The services described above do not relieve management or those charged with governance of their responsibilities.

### **THOSE CHARGED WITH GOVERNANCE**

The preparation and presentation of the financial statements of the Entity are the responsibility of management with oversight from those charged with governance. Those charged with governance are also responsible for overseeing the strategic direction of the Entity and any obligations related to its accountability, resolving disagreements between management and us regarding financial reporting, appointing us to perform the services described above, and informing us about all known or suspected fraud involving the Entity. In turn, we will provide those charged with governance with any communications required by the professional standards described above.

### **MANAGEMENT'S RESPONSIBILITIES**

Management is responsible for all management decisions and performing all management functions, and for designating an individual, preferably from senior management, with suitable skill, knowledge, or experience to oversee these services, any bookkeeping services, tax services, or other services we provide. Management is responsible for evaluating the adequacy and results of the services performed and accepting responsibility for them.

Management is responsible for making all financial records and related information available to us and for the accuracy and completeness of that information. Management is also responsible for providing us with (a) access to all information they are aware of that is relevant to the preparation and fair presentation of the financial statements, (b) additional information that we may request for the purpose of this engagement, and (c) unrestricted access to persons within the Entity from whom we determine it necessary to obtain information.

Management is responsible for establishing and maintaining internal controls, including monitoring ongoing activities, for the selection and application of accounting principles, for the safeguarding of assets, and for the preparation and fair presentation of the financial statements in conformity with US GAAP even though we may assist management with their preparation. Accordingly, management may be required to acknowledge in the written representation letter our assistance with preparation of the financial statements and that management has reviewed and approved the financial statements and related notes prior to their issuance and has accepted responsibility for them.

Management is responsible for adjusting the financial statements to correct material misstatements and for confirming to us in the management representation letter that the effects of any uncorrected misstatements aggregated by us during the current engagement and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Management is responsible for the design and implementation of programs and controls to prevent and detect fraud, and for informing us about all known or suspected fraud affecting the Entity involving (a) management, (b) employees who have significant roles in internal controls, and (c) others where the fraud could have a material effect on the financial statements. Management is also responsible for informing us of any known allegations of fraud or suspected fraud affecting the Entity received in communications from employees, former employees, regulators, or others. In addition, management is also responsible for identifying and ensuring that the Entity complies with applicable laws, regulations, contracts, agreements, and grants and for taking timely and appropriate steps to remedy any fraud, illegal acts, violations of contracts or grant agreements, or abuse that we may report.

During the course of our engagement, we will request information and explanations from management regarding the Entity. At the conclusion of our engagement, we will require, as a precondition to the issuance of our report, that management provide certain representations in a written representation letter. The procedures we will perform in our engagement and the conclusions we reach as a basis for our report will be heavily influenced by the written and oral representations that we receive from management. In view of the foregoing, the Entity agrees to release our firm, its shareholders, and other personnel from any liability and costs relating to our services under this letter resulting from false or misleading representations made to us by any member of the Entity's management.

Management is responsible for establishing and maintaining a process for tracking the status of audit findings and recommendations. Management is also responsible for identifying for us previous financial audits, attestation engagements, performance audits or other related studies. This responsibility includes relaying to us corrective actions taken to address significant findings and recommendations resulting from those audits, attestation engagements, performance audits, or other studies. Management is responsible for providing its views on our current findings, conclusions, and recommendations, as well as management's planned corrective actions, for the report, and for the timing and format for providing that information.

#### **ENGAGEMENT FEES**

We estimate that our fixed fees for the services previously outlined will be \$23,500.

Additionally, our fees are dependent on the availability, quality, and completeness of the Entity's records and, where applicable, upon the Entity's personnel providing the level of assistance identified in the "prepared by client" request list distributed at the end of our planning work (e.g., Entity employees preparing confirmations and schedules we request, locating documents selected by us for testing, etc.).

Should our assumptions with respect to these matters be incorrect, or should the condition of the records, degree of cooperation, or other matters beyond our reasonable control require additional commitments by us beyond those upon which our estimated fees are based, we may adjust our fees and planned completion dates. If significant additional time is necessary, we will discuss it with management and arrive at a new fee estimate as soon as reasonably practicable.

#### **OTHER ENGAGEMENT MATTERS**

This letter set forth the rights and responsibilities of the parties with respect to the services to be provided. This engagement is being undertaken solely for the benefit of the parties to this agreement and no other person shall be entitled to enforce the terms of this agreement.

Enclosed, as required by *Government Auditing Standards*, is a copy of the report on the most recent peer review of our firm.

The workpapers for this engagement will be retained in accordance with our firm policy. If we are aware that a federal awarding agency, pass-through entity, or auditee is contesting an audit finding, we will contact the party contesting the audit finding for guidance prior to destroying the workpapers.

The undersigned is the engagement partner responsible for supervising the engagement and signing the report.



We appreciate the opportunity to provide these services and believe this letter accurately summarizes the significant terms of our engagement. Please sign the enclosed copy of this letter and return it to us.

Very truly yours,

*Shannon Ayala*

**Shannon Ayala, Partner**  
Davis Farr LLP

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The services and arrangements described in this letter are in accordance with our understanding and are acceptable to us.

**Leucadia Wastewater District**

By \_\_\_\_\_

By \_\_\_\_\_

Name \_\_\_\_\_

Name \_\_\_\_\_

Title \_\_\_\_\_

Title \_\_\_\_\_

Date \_\_\_\_\_

Date \_\_\_\_\_



## Report on the Firm's System of Quality Control

### **Davis Farr LLP**

Irvine, California;

and the Peer Review Committee of the California Society of CPAs

We have reviewed the system of quality control for the accounting and auditing practice of Davis Farr LLP (the firm) in effect for the year ended May 31, 2019. Our peer review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants (Standards).

A summary of the nature, objectives, scope, limitations of, and the procedures performed in a System Review as described in the Standards may be found at [www.aicpa.org/prsummary](http://www.aicpa.org/prsummary). The summary also includes an explanation of how engagements identified as not performed or reported in conformity with applicable professional standards, if any, are evaluated by a peer reviewer to determine a peer review rating.

### **Firm's Responsibility**

The firm is responsible for designing a system of quality control and complying with it to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. The firm is also responsible for evaluating actions to promptly remediate engagements deemed as not performed or reported in conformity with professional standards, when appropriate, and for remediating weaknesses in its system of quality control, if any.

### **Peer Reviewer's Responsibility**

Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review.

### **Required Selections and Considerations**

Engagements selected for review included engagements performed under *Government Auditing Standards*, including a compliance audit under the Single Audit Act, and examination of a service organization (SOC 1, Type 2 Report).

As part of our peer review, we considered reviews by regulatory entities as communicated by the firm, if applicable, in determining the nature and extent of our procedures.

### **CPAs ■ Advisors**

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909.948.9990 / 800.644.0696 / FAX 909.948.9633  
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### Opinion

In our opinion, the system of quality control for the accounting and auditing practice of Davis Farr LLP in effect for the year ended May 31, 2019, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of *pass*, *pass with deficiency(ies)* or *fail*. Davis Farr LLP has received a peer review rating of *pass*.

GFL LLP

Ontario, California  
September 23, 2019

# MEMORANDUM

Ref: 21-7436

**DATE:** January 28, 2021  
**TO:** Investment and Finance Committee  
**FROM:** Paul J. Bushee, General Manager  
**SUBJECT:** Annual Review of LWD Reserve Fund Policy

## RECOMMENDATION:

Staff requests that the Investment and Finance Committee (IFC) recommend that the Board of Directors:

1. Receive and file the Annual Reserve Fund Review Report; and
2. Discuss and take other action, as appropriate.

## DISCUSSION:

### **Tactical Goal: Financial / Finance Policy Reviews**

In February 2005, the Board of Directors (Board) adopted Leucadia Wastewater District's (LWD) Reserve Fund Policy which established a means for LWD to ensure that sufficient funds are available for current operating and capital needs. The policy was last revised in February 2020.

The Reserve Fund Policy establishes two distinct reserves at LWD: 1) Restricted Reserves and 2) Unrestricted Reserves. The policy also establishes various designations within each type of reserve and calls for an annual review of the reserve balances. This report constitutes that review.

Staff has reviewed the Reserve Fund Policy and is recommending no changes to the existing Reserve Fund Policy. A copy of the policy is attached for the committee's review.

During November 2020, the Board received the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2020 that included the following reserve balances:

### **Restricted Reserves:**

<i><b>Reserve Designation</b></i>	<i><b>Reserve Balances</b></i>
<i>Capital Improvement Reserve</i>	\$ 102,422
<i>Encina Wastewater Authority Reserve</i>	\$2,041,200
<b>Total</b>	<b>\$2,143,622</b>

### **Unrestricted Reserves:**

<i><b>Reserve Designation</b></i>	<i><b>Reserve Balances</b></i>
<i>Operations Reserve</i>	\$ 2,748,321
<i>Replacement Reserve</i>	\$20,454,735
<i>Water Recycling Reserve</i>	\$ 1,393,983
<i>Emergency Reserve</i>	\$ 7,500,000
<b>Total</b>	<b>\$32,097,039</b>

Staff will provide an overview of the FY 2020 reserve activity during the committee meeting.

rad:PJB

Attachment

## Exhibit A

### LEUCADIA WASTEWATER DISTRICT RESERVE FUND POLICY

Ref: 20-7013

#### A. POLICY STATEMENT:

One key element of prudent financial planning is to ensure that sufficient funding is available for current operating, capital, and debt service cost needs. An additional critical element of fiscal responsibility is to anticipate and prepare for future funding requirements as well as for unforeseen disasters and other unforeseen events. The Leucadia Wastewater District (LWD) will at all times strive to have sufficient funding available to meet its operating, capital, and debt service cost obligations. Reserve funds will be accumulated and maintained in a manner, which allows LWD to fund costs consistent with LWD's adopted Asset Management Plan and Financial Plan, while avoiding significant rate fluctuations due to changes in cash flow requirements. LWD will also maintain an emergency reserve position that may be utilized to fund unexpected disasters or unanticipated major failures. The Board of Directors will annually review the level of reserve funds maintained.

#### B. DEFINITIONS:

Restricted Reserves: These reserves have restrictions on their use that are imposed by outside sources such as creditors, grantors, contributors, or laws or regulations of other governments.

Unrestricted Reserves: These reserves have no externally imposed use restriction. The use of Unrestricted Reserve funds is at the discretion of the Board of Directors. There are two categories of Unrestricted Reserves; Designated and Undesignated. At LWD, all Unrestricted Reserves have been Designated.

Designated Reserves: These reserves are set-aside for a specific purpose, which is determined by the Board of Directors. The Board of Directors also has the authority to redirect the use of these reserve funds as the needs of LWD change.

#### C. LEUCADIA WASTEWATER DISTRICT RESERVES:

LWD maintains the following reserve funds:

##### 1.0 RESTRICTED RESERVES:

###### a) Capital Improvement Reserve:

The purpose of the Capital Improvement Reserve is to finance future capital facilities that are expansion/growth related. These capital improvements are identified in LWD's Asset Management Plan and Financial Plan. These reserve funds are accumulated in an orderly manner in conformance with State law and drawn down as required by growth related capital projects.

###### b) Encina Wastewater Authority Reserve:

LWD is a member agency of the Encina Wastewater Authority Joint Powers Authority (EWA). EWA maintains member agency deposits on hand to meet its operational, inventory, and capital demands during any quarter. These deposits are restricted for that use.



## **2.0 UNRESTRICTED DESIGNATED RESERVES:**

a) Operating Reserve:

Since the majority of operating revenues are received periodically over the fiscal year and operating expenses are incurred uniformly over the fiscal year, an operating reserve is necessary to fund those costs attributable to daily operations. To meet daily operational needs, LWD has established an Operating Reserve balance at 33% of annual budgeted operating expenses.

b) Replacement Reserve:

The Replacement Reserve provides funds for capital replacement and refurbishment of existing wastewater facilities. These capital improvements are identified in LWD's adopted Asset Management Plan and Financial Plan. Replacement Reserve funds are accumulated in an orderly manner and drawn down as required to fund capital replacement projects. To avoid abrupt sewer service rate changes, this reserve may be used to stabilize rates. The Replacement Reserve shall not exceed the total 20-year capital replacement costs for wastewater facilities as identified in the Financial Plan. The yearly average of the 20-year capital replacement costs is the minimum target balance to ensure that LWD is able to fund capital replacements as they are scheduled or needed.

c) Water Recycling Reserve:

The Water Recycling Reserve will fund capital improvements and replacement of water recycling facilities. This reserve can also be used to fund operating expenses in the Water Recycling Fund whenever there is a shortfall of recycled wastewater sales revenue. These capital improvements are identified in LWD's adopted Asset Management Plan and Financial Plan. The Water Recycling Reserve shall not exceed the total 20-year capital replacement costs for water recycling facilities as identified in the Financial Plan.

d) Emergency Reserve:

The Emergency Reserve provides funds for emergency response for potential repair or replacement of capital facilities due to damage from a natural disaster or unanticipated major failure in a period when capital improvements funds have otherwise been purposely spent down to preset limits on planned projects. The Emergency Reserve is at the discretion of the Board of Directors and is maintained at a level of \$7,500,000, which is based on the recommendation by LWD staff and the District Engineer (Exhibit A).

For further detail of the sources and uses of the above reserves please refer to following section "D".

## **D. SOURCES AND USE OF FUNDS:**

This section describes the sources and uses of funds for LWD reserves and includes maximum and minimum reserve balances and other informational notes.



## RESTRICTED RESERVES

RESERVE	SOURCE OF FUNDS	USE OF FUNDS	NOTES
Capital Improvement	Interest earned on reserve	Growth related capital expenditures	Funds previously accumulated from capacity fees. Now, capacity fees reflect 100% buy-in to the system and are transferred to the Replacement Reserve
EWA	Funds transferred from LWD to EWA for deposit with EWA	Funds transferred back from EWA to LWD due to reduction in deposit requirements	Deposit balances determined by EWA approved financial reserve policy. Deposit is for EWA Operating, Inventory, and Capital demands during any quarterly period

## UNRESTRICTED DESIGNATED RESERVES

RESERVE	SOURCE OF FUNDS	USE OF FUNDS	NOTES
Operating	Operating income and interest earned on reserve	Wastewater Operating expenses	Reserve balance maintained at 33% of budgeted operating expenses. Excess (deficit) funds transferred to (from) Replacement Reserve
Replacement	Property taxes, interest earned on reserve, 100% of Capacity Fees, and other non-operating income. Also excess operating net income transferred from Operating Reserve, and excess interest earned on emergency reserve	Replacement related capital expenditures and rate stabilization	Maximum reserve balance is 20-year capital replacement costs as identified in the Financial Plan. Minimum reserve target balance is the yearly average of the 20-year capital replacement costs as identified in the Financial Plan
Water Recycling	Recycled Water sales, grant income, and interest earned on reserve	Recycled Water capital improvement and replacement costs as well as water recycling operating expenses	Maximum reserve balance is 20-year capital replacement costs as identified in the Financial Plan.
Emergency	Originally funded by board action. Interest earned on reserve. Additional funding as needed to maintain Reserve level.	Emergency repair or replacement expenditures	Reserve balance maintained at \$7,500,000 level. Excess (deficit) funds transferred to (from) Replacement Reserve

## EXHIBIT A

### Leucadia Wastewater District Discussion of Emergency Reserve Fund

Maintenance of an Emergency Reserve Fund (ERF) would provide the benefit of providing funds for emergency response for repair or replacement of capital facilities potentially necessary due to natural disaster damage or unanticipated major failure in a period when capital improvement funds have otherwise been purposely spent down to preset limits on planned projects. Separately, Capital Reserve Funds will be accumulated in a planned manner through financing, setting aside a portion of sewer service fees, or a combination of both methods, as determined by Board policy.

The amount to be recommended for maintenance in the ERF has been evaluated and discussed by Leucadia Wastewater District (LWD) staff and the District Engineer. The following table lists some pros and cons for three potential levels of ERF.

ERF Alternatives	Pros	Cons
Alternative 1: LWD maintain small ERF of \$1.0 million	<ol style="list-style-type: none"><li>1) Reduces initial reliance on borrowing.</li><li>2) Would extend period of reduced rate increases.</li></ol>	<ol style="list-style-type: none"><li>1) Not enough reserve to respond to many reasonably possible emergency events.</li><li>2) Increased risk at point of ERF exhaustion that emergencies could not be responded to timely.</li><li>3) Reduced District liquidity and lesser financing qualifications.</li><li>4) Increased long term reliance on borrowing.</li></ol>
Alternative 2: LWD maintain a Moderate ERF of \$7.5 million	<ol style="list-style-type: none"><li>1) Sufficient funds to adequately replace or repair two major District facilities on an emergency basis.</li><li>2) Sufficient funds to replace or repair about six or seven concurrent intermediate size facility problems at any given time.</li><li>3) Unlikely to deplete ERF in a time period that would not allow establishment of additional financing, if necessary.</li><li>4) Provides opportunity for investment of modest amount of about 1.5 years worth</li></ol>	<ol style="list-style-type: none"><li>1) Ties up \$7.5 million of funds that could be used to offset or defer rate increases.</li><li>2) May be considered as ability to pay discretionary fines in the potential event of a major wastewater spill.</li><li>3) Over time, it may be determined that the \$7.5 million amount should be decreased or increased depending on facility performance and risk tolerance.</li></ol>

	<p>of sewer service fee collections.</p> <p>5) Provides ability to fund one to two years of typical CIP schedule projects, while additional funding is being established.</p> <p>6) Increases liquidity of District that would be considered positively by financial markets when considering other financing issues.</p>	
Alternative 3: LWD maintain a Large ERF of \$15 million	1) Very little risk that any emergency situation would result that funds were not available for immediate response.	1) Maintenance of large reserves is considered by some watch dog entities as a negative attribute.

Based on an analysis of the above three ERF funding alternatives above, LWD staff and the District Engineer recommend that LWD adopt Alternative 2 – LWD Maintain a Moderate ERF of \$7.5 million.