

Southwest Metropolitan Water and Sanitation District

2019 Budget Policy Issues

1. In 2014, the District adopted a water and sanitary sewer service fee to stabilize the reserve fund and provide additional revenue for operations. The initial fee was set at \$1.00 per month per $\frac{3}{4}$ -inch equivalent water tap. Subsequent adjustments have raised the fee to \$5.00 per month per $\frac{3}{4}$ -inch equivalent tap in 2018 with an additional increase to \$7.00 per month scheduled for 2019. The initial goal established by the Board was to have the service fee and other non-development related revenue equal operating expenses to halt depletion of the reserve fund.

In the past, the District has considered investment income as operating revenue. This results in a reduction in the amount of service fee revenue needed to balance operating expenses. However, the practice also limits the ability to increase the reserve fund to tap fee revenues only which are likely to be significantly reduced over time due to limited growth potential. A service fee of \$9.00 per month when combined with expected investment income in 2020 will equal projected operating expenses.

Question: Should the District transfer investment income to the reserve fund and continue to increase the service fee over time to a level whereby it will generate sufficient revenue to equal operating expenses? Using 2019 budget numbers, a fee of \$10.54 per month would be required to match service fee revenue to operating expenses.

2. In June 2018, the Board of Directors adopted a Cash Reserve Policy that included criteria to evaluate and establish an appropriate level of cash reserves. The criteria contain three elements; an operating reserve component, a capital reserve component and a debt service reserve component. The operating reserve component is equal to one year of operating expenses which, for 2019 is \$1,888,458. The capital reserve component is the greater of 10 percent of the replacement cost of each asset adjusted for depreciation (\$9,226,573) or the total of the first five years of projected capital expenses identified in the most recent Ten-Year Financial Plan (\$1,648,362). The debt service reserve component is zero since the District is debt free. Therefore, for 2019 the minimum level of cash reserves is \$11,115,031.

District staff are revising the criteria by which water pipelines are evaluated for rehabilitation or replacement. This work should be completed in late 2018 and will result in changes to the District's Capital Master Plan and Ten-Year Financial Plan. It is anticipated that capital expenditures planned for the next ten years will increase.

The Cash Reserve Policy states that each year the Board will determine if the capital portion of the reserve should be based on 10 percent of replacement cost of District assets or a lesser or greater percentage.

The District's 2019-2048 Financial Plan indicates that, based on current revenue, operating expenses and asset replacement assumptions, cash reserves will not drop below \$14,307,498 and will be \$24,001,600 in 2048.

Question: Does the Board of Directors want to continue to base the capital reserve portion of cash reserves on 10 percent of the replacement cost of District assets adjusted for inflation or consider using a higher or lower percentage.