

FOX CANYON GROUNDWATER MANAGEMENT AGENCY CASH RESERVE POLICY

ADOPTED BY THE
BOARD OF DIRECTORS
ON
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CASH RESERVE POLICY

I. POLICY OBJECTIVE

The purpose of Fox Canyon Groundwater Management Agency (Agency) Cash Reserve Policy (Policy) is to ensure that the Agency will have adequate funding and liquidity in order to mitigate risk or uncertainty in revenue and expenses, to maintain a stable financial base to sustain the Agency's operations and provide for the timely replacement of critical infrastructure. The Policy is intended to be used in conjunction with the Agency's budgets and long-range financial plan. Properly designed policies demonstrate that the Board is committed to the Agency's long-term financial health and include:

- establishing prudent fiscal reserve policies to ensure strong fiscal management to guide Agency decisions;
- providing the ability to meet the Agency's short-term and long-term obligations and to ensure that the Agency maintains the ability to receive a high credit rating (AA or better);
- ensuring funding is available for current and future replacement of assets; and
- helping smooth rates from year-to-year while promoting long-term equity to ratepayers.

II. BACKGROUND AND INTRODUCTION

The complex nature of Fox Canyon's operations and its various legal and legislative requirements dictates a multifaceted and sophisticated financial structure. The Agency has implemented numerous operating programs to ensure it is meeting all requirements imposed by the Fox Canyon Groundwater Management Agency Act, the Sustainable Groundwater Management Act (SGMA), and other legal requirements.

To ensure the Agency satisfies its commitments under its numerous financial, regulatory, and contractual obligations, the Agency has developed and segregated several types of accounts. The prudent management of these accounts will provide assurance that the current levels of Agency performance will continue, and the Agency will be able to meet all statutory requirements.

These accounts can be broken out into two types: Operating and Designated. Currently, the Agency maintains the following accounts:

Account	Type	Purpose
Operating Account	Operating	Routine annual operation expenses as identified in Work Plan.
Groundwater Extraction Management Enforcement Surcharge (GEMES) Account	Designated	Fund litigation costs including Agency counsel and outside counsel.
Surcharges Account	Designated	For Board-directed uses only, not to be used for routine Agency operations.
Operating Reserves	Designated	Maintain a flat fee reserve balance based on Board direction.

During the adoption of the Agency's budget, a comprehensive assessment is conducted of all accounts and their respective prioritization and funding levels. In accordance with sound financial management practices, the strategic determination of the optimal level and distinct delineation of reserve subcategories is imperative for the fiscal well-being of the Agency. This policy establishes the mandated reserve types along with their corresponding funding thresholds, including defining new accounts. This policy shall be reviewed annually during the budget development process, during

which the Executive Officer shall provide a Reserve Status Report showing the current balance for each fund category.

III. RESERVE DEFINITIONS

A. Operating Reserves

The Operating Reserves are comprised of two reserve funds with individual target levels based on the major classifications of risk to the Agency's operations. This expands upon the current Operating Reserves Account.

1. Working Capital Reserve

This reserve acts as the "base" reserve and is intended to provide sufficient liquidity from a cash-flow perspective to facilitate the normal dynamic of ongoing expenses and episodic revenue collection.

- a. **Funding Sources:** Operating revenues (pump charges and groundwater sustainability fees) or Board-approved transfers from other funds.
- b. **Target Levels:** The target level for this reserve shall be 180 days of annual budgeted operating costs and shall maintain a minimum balance equal to 120 days of the total annual operating budget and a maximum balance of 240 days of the total annual operating budget.
- c. **Events or Conditions Prompting the Use of the Fund:** This fund may be routinely utilized by staff to cover temporary cash flow deficiencies caused by timing differences between revenue and expenses or decreases in revenues and unexpected increases in expenses. Requires Executive Officer approval with a report to the Board.

- d. **Replenishment:** Upon the drawing of funds resulting in a balance at or below the target, staff will recommend a course of action to meet the target level. The recommendation will include:
 - Identification of the cause of the draw-down.
 - Incorporation of a Replenishment Line Item in the subsequent fiscal year's budget.
 - A target of full restoration of the floor within 24 to 36 months.

2. Rate Stabilization Reserve

The Agency's Rate Stabilization Reserve provides broad protection against unexpected costs or loss of revenues and acts as the primary reserve when considering mitigating rate increases. This fund is differentiated from the Working Capital Reserve in that its intent is to absorb unanticipated short-term costs without triggering a rate increase, whereas the Working Capital Reserve allows for uninterrupted operations despite cyclical revenue collection. The Rate Stabilization Reserve can also be used to reduce the need for rate increases if the rate increase is contemplated for short-term reasons.

- a. **Funding Sources:** Operating revenues (pump charges and groundwater sustainability fees).
- b. **Target Level:** The Rate Stabilization Reserve shall have a target level of 120 days of annual budgeted operating costs. This reserve may increase in order to plan for anticipated increases in operating costs.
- c. **Events or Conditions Prompting the Use of the Fund:** Used to cover funding for unanticipated major expenses during a year which may otherwise impact rates or fees charged. Requires Executive Officer approval with a report to the Board.
- d. **Replenishment:** Upon the drawing of funds below the target level, staff will recommend a course of action within the budget

and long-range financial planning process to meet the target level. The recommendation will include:

- Identification of the cause of the draw-down.
- Incorporation of a Replenishment Line Item in the subsequent fiscal year's budget.
- A target of full restoration of the floor within 24 to 36 months.

B. Non-Operating Reserves

1. Water Supply Reliability Reserve

This reserve helps to mitigate the risk of short-term low- to moderate-drought impacts by funding unanticipated purchases of imported water resulting from reductions in local water supplies and is also used for the funding of new projects or for the funding of the replacement of assets (such as monitoring wells) when they reach the end of their useful lives. Replacement of capital assets shall include repair, rehabilitation, improvements, and/or extensions of existing capital assets. This replaces the current Surcharges Account.

- a. **Funding Sources:** Surcharges or Board directed transfers from other funds.
- b. **Target Levels:** The Water Supply Reliability Reserve target is set at two (2) years' impact of estimated imported water costs resulting from a decrease in groundwater yield during a drought or other conditions which create imported water costs. The Agency may also set aside funds for certain identified projects until such time as work commences on the identified project.
- c. **Events or Conditions Prompting the Use of the Fund:** Used to supplement revenues during drought years or other conditions which create imported water costs. In addition, Staff will recommend new projects during the annual budget preparation. As projects are

approved, funds will be appropriated from other reserve funds or available revenues. Use of this fund requires Board approval.

- d. **Replenishment:** Upon the drawing of funds resulting in a balance at or below the target, staff will recommend a course of action to meet the target level. The recommendation will include:
 - i. Identification of the cause of the draw-down.
 - ii. Incorporation of a Replenishment Line Item in the subsequent fiscal year's budget.
 - iii. A target of full restoration of the floor within 24 to 36 months.

2. Debt Service Reserve.

- a. Not currently operative.
- b. The category will be defined should it be required in the future.

3. Risk Management Reserve.

- a. Not currently operative.
- b. The category will be defined should it be required in the future.

IV. ADDITIONAL USES OF RESERVES

If reserve funds have reached their maximum target levels, the Board may instruct staff to utilize additional reserves in the following ways.

- 1. Advance fund any of the Agency's short-term or long-term liabilities, including but not limited to outstanding debt, lease obligations, State Revolving Fund (SRF) loans, interfund loans, or other loans.
- 2. In the event the Agency's budget process identifies large future spending plans, reserves can be transferred to fund the Project Reserve, other special purpose reserves for special projects or purchases, cash funding capital projects, and/or future capital commitments at the Board's discretion.
- 3. Consideration will be given to reducing fees and charges to ratepayers should no other reasonable and timely use exist for the funds.

V. RESERVE TABLE SUMMARY

Reserve Fund	Minimum	Target	Maximum
Working Capital Reserve ⁽¹⁾	120 days of total annual operating budget.	180 days of total annual operating budget.	240 days of total annual operating budget
Water Supply Reliability Reserve	N/A	Two (2) years' impact of estimated imported water costs plus project costs.	N/A
Rate Stabilization Reserve		120 days of total annual operating budget.	
Debt Service Reserve & Risk Management Reserve	Not currently operative.		

(1) Base Reserves - Agency Minimum