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**ORANGE COUNTY WATER DISTRICT**

ORANGE COUNTY'S GROUNDWATER AUTHORITY

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MICHAEL R. MARKUS, P.E., D.WRE

April 12, 2022

Mr. Robert J. Hunter  
General Manager  
Municipal Water District of Orange County  
18700 Ward Street  
Fountain Valley CA 92708

SUBJECT: Municipal Water District of Orange County Reserves Policy

Dear Mr. Hunter:

The Municipal Water District of Orange County (MWDOC) is in the process of reviewing its reserves policy. Orange County Water District (OCWD) would like to thank you for this review and is providing comments for your Board's consideration:

**General Operations Reserve** – The target for this reserve is to maintain 90 to 180 days cash on hand. MWDOC has been maintaining reserves in this fund at the 180 day level which we believe is unnecessarily high. MWDOC's operations are unique and relatively simple which makes its general operating reserve needs less as compared to other water agencies. Several specific reasons why MWDOC's general operations reserve target can be lowered are provided below:

- MWDOC's revenues are very secure as they are tied to the amount of retail meters in its service area. Most other water agencies revenues are tied to varying degrees to fluctuating water sales.
- MWDOC receives its revenues at the beginning of the fiscal year which reduces collection risk and gives MWDOC time to respond to possible revenue shortfalls.
- MWDOC does not maintain or operate any infrastructure other than its administrative building.
- MWDOC's operating expenses are very stable and predictable.
- MWDOC has no plans to implement any new substantial programs.
- Using credit rating agency metrics to establish reserve targets is inappropriate given MWDOC has no outstanding debt and no plans to implement any projects requiring the issuance of debt.
- A large amount of money annually passes through MWDOC via its member agency imported water purchases. However, these financial transactions are relatively seamless with little risk.

As previously mentioned MWDOC has been using the 180 day figure for the amount of cash reserves kept in this fund. OCWD suggest a cash reserves target of 90 days more accurately fits MWDOC's operation, financial profile and need.

**Grant and Project Cash Flow** - This reserve amount is set at \$1.5 million. OCWD questions the need for this fund and its amount. Your reserve policy indicates MWDOC submits requests for reimbursement for expenditures and recovers the funds under various agreements and rebate programs for itself and its member agencies. OCWD is curious how frequently this fund is needed and in what amount and requests the MWDOC staff make this information available to your member agencies for discussion. OCWD suggest the MWDOC general operations fund can provide the primary cash flow needs for these transactions, if and when such is required. With this change this fund could be eliminated or significantly reduced to say \$500,000.

**Building Reserve** - MWDOC has a building reserve of 15 days cash which equates to \$437,000. MWDOC's exposure and risk to emergency events such as a fire (which is covered by insurance) or earthquakes is minimal as the MWDOC administrative building was recently retrofitted to current earthquake standards. The most probable need for money would be to make roof or HVAC type repairs. It seems a reserve amount of \$200,000 is more appropriate for these types of potential expenses.

If the MWDOC administrative building was significantly damaged in some type of unlikely event, MWDOC has shown via the COVID-19 crises the ability to operate remotely which would give it time to accumulate required funding to make any necessary repairs. Additionally, carrying 90 days of cash in the MWDOC general operations reserve also provides funding for such emergencies.

**Election Reserve** - The District has no comments on the Election Reserve.

**OPEB Reserve**- The District has no comments on the OPEB Reserve.

**Metropolitan Water District Tier II Reserve** – The District concurs with what appears to be general consensus based upon recent discussions that the \$1.03 million Metropolitan Water District Tier II reserve can be eliminated.

**General Reserves Policy Comment** - OCWD would also like to provide one general comment on the MWDOC reserves policy. The recent outside review of the MWDOC reserves by Brian Thomas, which uncovered approximately \$5 million in excess reserves, indicates the current reserves policy and reporting is too complicated. MWDOC reports its reserves monthly to the Administration and Finance (A&F) Committee, yet it was not evident to your board or member agencies that this excess reserve amount existed. We generally recommend MWDOC simplify and clarify its reserve policies so your monthly financial reporting clearly shows any excess reserves that may be accumulating.

OCWD understands that an internal audit is occurring with the source and accumulation of this money and the amount that could be considered excess could change based upon those findings.

### Summary

Based upon recent information and our recommendations and calculations, MWDOC would have approximately \$9.14 million in excess reserves as shown below:

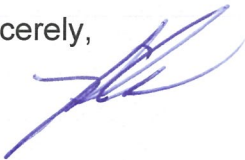
- \$5.0 million identified by Brian Thomas
- \$1.87 million reduction in general operating reserves going to 90 days cash
- \$1.03 million Tier II reserves
- \$1.0 million reduction in Grants and Project Cash Flow reserve
- \$0.24 million building fund reduction

We recommend this money be used to fully fund MWDOCs OPEB and PERs liabilities and if any monies are left, to refund the MWDOC member agencies using an appropriate formula that is ultimately approved by the MWDOC Board. This money was collected from the MWDOC member agencies thus it is appropriate to return it to them.

Please forward these comments to the MWDOC Board and include them in future meeting discussions of this subject.

Thank you for your consideration.

Sincerely,

A handwritten signature in blue ink, appearing to read 'Michael R. Markus', is written over a horizontal line.

Michael R. Markus, P.E., D.WRE, BCEE, F.ASCE  
General Manager

Bcc: OCWD Board of Directors