

Fiscal Policies

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Revision History

DATE	GOVERNING BODY	APPROVAL HISTORY
06/26/2001	CC	RPU Fiscal Policy
12/18/2015	PUB	Review of RPU Cash Reserve Policy
02/10/2016	FC	Review of RPU Cash Reserve Policy
03/22/2016	CC	Approval of RPU Cash Reserve Policy
05/23/2016	PUB	Review of RPU Updated Fiscal Policies
07/13/2016	FC	Review of RPU Updated Fiscal Policies
07/26/2016	CC	Approval of RPU Updated Fiscal Policies
06/25/2018	PUB	Review of RPU Updated Fiscal Policies, including Cash Reserve Policy
07/11/2018	FC	Review of RPU Updated Fiscal Policies, including Cash Reserve Policy
07/24/2018	CC	Approval of RPU Updated Fiscal Policies, including Cash Reserve Policy
06/21/2021	PUB CR/F	Review of RPU Updated Cash Reserve Policy
	PUB	Review of RPU Updated Cash Reserve Policy
	CC	Approval of RPU Updated Cash Reserve Policy

Related Policies Referenced

- City of Riverside Administrative Manual Policy 06.003.00
- City of Riverside Investment Policy
- City of Riverside Debt Management Policy
- RPU Power Resources Risk Management Policies
- Resolution No. 22203 – Eighth Supplemental Resolution authorizing the issuance of 2011A Variable Rate Refunding Water Revenue Bonds
- Resolution No. 22537 – Seventeenth Supplemental Resolution authorizing the issuance of 2013A Refunding Electric Revenue Bonds and 2013B Taxable Electric Revenue Bonds

Glossary of Terms

The following terms are used frequently throughout the Fiscal Policy document. Definitions are provided for terms that are common to Riverside Public Utilities. For definitions of terms unique to a specific component of the policy, please refer to the body of the document where the term is discussed.

Accrual Basis of Accounting
A system of accounting based on the accrual principal, under which revenue is recognized (recorded) when earned, and expenses are recognized when incurred. Totals of revenues and expenses are shown in the financial statements (prepared at the end of an accounting period), whether or not cash was received or paid out in that period. Accruals basis accounting conforms to the provisions of GAAP in preparing financial statements for external users, and is employed by most companies except the very small ones (which use cash basis accounting).

Allocation
A distribution of funds or costs from one account or appropriation to one or more accounts or appropriations.

Appropriation
Authorization for a specific agency to make expenditures or create obligations from a specific fund for a specific purpose. It is usually limited in amount and period of time during which the expenditure is to be recognized.

Arbitrage
In general, arbitrage is the practice of taking advantage of a price difference between two or more markets. With respect to the issuance of municipal securities, arbitrage usually refers to the difference between the interest paid on tax-exempt bonds and the interest earned by investing the proceeds of the tax-exempt bonds in higher-yielding taxable securities. Federal income tax laws generally restrict the ability to earn arbitrage in connection with tax-exempt bonds or other federally tax-advantaged bond.

Base Budget
Ongoing expense for personnel, contractual services, materials and supplies, and the replacement of supplies and equipment required to maintain service levels previously authorized by the City Council.

Budget Carryover
The unencumbered balance of an appropriation that continues to be available for expenditure in years subsequent to the year of enactment.

Budgetary Control System
A system for controlling costs and revenues by comparing actual results with budget plans and then taking corrective action where necessary.

California Public Utilities Commission (CPUC)
A regulatory agency that regulates privately owned electric, natural gas, telecommunications, water, railroad, rail transit, and passenger transportation companies in the state of California.

Capital Improvement Plan (CIP)
A plan for capital expenditures to be incurred each year over a period of five future years setting forth each capital project, the amount to be expended in each year, and the source of funding for those expenditures.

Cash Basis Accounting
Accounting method that recognizes revenues and expenses at the time physical cash is actually received or paid out. This contrasts to the other major accounting method, accrual accounting, which requires income to be recognized in a company's books at the time the revenue is earned (but not necessarily received) and records expenses when liabilities are incurred (but not necessarily paid for).

Chart of Accounts
The Chart of Accounts is a list of all the accounts, or nominal codes as they are called in the general ledger, summarized in a systematic manner to represent the sequence on financial statements.

Contribution in Aid of Construction
Any amount of money or other property contributed by an outside agency or developer for the purpose of providing the expansion, improvement, or replacement of the utility's water or electric infrastructure.

Credit Rating
An assessment of the creditworthiness of a borrower in general terms or with respect to a particular debt or financial obligation. Credit assessment and evaluation for companies and governments is generally done by a credit rating agency such as Standard & Poor's, Moody's or Fitch. The highest rating is usually AAA, and the lowest is D.

Debt Service
The amount of money required to pay principal and interest on outstanding bonds.

Debt Service Coverage Ratio
The Debt Service Coverage Ratio is used as a benchmark to measure the Utility's ability to produce enough cash to cover its debt service payments.

Derivative
Any financial instrument, such as a futures contract, swap or option, which derives its value from the value of an underlying security or physical commodity.

Direct Debt
Direct Debt is the total amount of debt, including notes and short-term financing issued by Riverside Public Utilities as a department of the City.

Encumbrance
Encumbrance is the name given to funds that have been reserved when a purchase requisition is finalized and encumbered. When a requisition is processed, funds are placed aside for that transaction. Those funds are no longer available for use in other transactions. The purpose and main benefit of encumbrance accounting is avoiding budget overspending.

Enterprise Risk
Potential events that may affect an entity's ability to achieve its strategic and financial objectives.

Federal Energy Regulatory Commission (FERC)
Independent agency within the Department of Energy. FERC is vested with broad regulatory authority. Virtually every facet of electric and natural gas production, transmission, and sales conducted by private investor-owned utilities, corporations or public marketing agencies is placed under the commission's purview through either direct or indirect jurisdiction, if any aspect of their operations are conducted in interstate commerce.

Generally Accepted Accounting Principles (GAAP)
The accounting principles, rules, conventions, and procedures that are used for accounting and financial reporting. GAAP for governments are set by the Governmental Accounting Standards Board (GASB), the accounting and financial reporting standards setting body for state and local governments.

Governmental Accounting Standards Board (GASB)
The independent organization that establishes and improves standards of accounting and financial reporting for U.S. state and local governments.

Hedge
Hedges are utilized to reduce risk. It includes activities that reduce risk or that convert one type of risk to another deemed more tolerable. To qualify as Hedging, an activity should be expected to produce a measurable offset to risk relating to an asset, liability, committed transaction, or probable forecasted transaction. Such offset should be measured against changes in market values or cash flows (e.g., marked-to-market).

Indirect Debt
Indirect debt is debt that is issued on behalf of the City or RPU by another entity which is normally associated with a joint capital project within a joint powers agency like Southern California Public Power Authority, Intermountain Power Agency, etc.

Interest Rate Risk
The possibility of unexpected rise in interest cost.

Internal Controls
Methods put in place by a company to ensure the integrity of financial and accounting information, meet operational and profitability targets and transmit management policies throughout the organization.

Investment Risk
Probability that an actual return on an investment will be lower than the investor's expectations. All investments have some level of risk associated it due to the unpredictability of the market's direction.

Leverage
The use of various financial instruments or borrowed capital to acquire additional assets.

Long-term Debt
Bonds, loans, and any other debt with a maturity of longer than one year. Long-term debt is used mainly to fund the Utility’s capital improvement plan, buildings and other long-term assets.

Revenue Requirement
The reasonable level of revenue required for a utility to operate and maintain its system, and meet its financial obligations. The revenue requirement provides the basis for determining the amount of revenue to be collected through rates.

Safekeeping of Securities
To protect against fraud, embezzlement, or losses caused by collapse of an individual securities dealer and to enhance access to securities and interest payments, all securities owned by the City shall be held in safekeeping by a third party bank trust department acting as agent for the City under the terms of a duly executed custody agreement. In connection with the City’s annual independent audit, securities held in custody are audited to verify investment holdings. All exceptions to this safekeeping policy must be approved by the City Treasurer in written form and included in monthly reporting to City Council.

Short-term Debt
Any bond or other debt that must be repaid or refinanced within one year. Short-term debt is recorded on the balance sheet as a current liability.

Unencumbered Balance
The balance of an appropriation not yet committed for specific purposes.

Uniform System of Accounts
A chart of accounts with detailed instructions prescribed by a regulatory agency.

Purpose

Overview

Riverside Public Utilities (RPU), pursuant to policies adopted by the City Council of the City of Riverside (City Council) and the Board of Public Utilities (Board), is responsible for managing RPU's finances. The fiscal policies are designed to establish guidelines for the fiscal stability of RPU and provide guidance to staff in carrying out their fiscal responsibilities.

Goals

These policies are guidelines and goals that provide a framework for the financial management of RPU. Strong fiscal policies are the cornerstone of sound financial management. These goals include:

- Promote long term financial stability by establishing clear and consistent financial reporting guidelines.
- Ensure that RPU will maintain its financial health in order to meet its strategic goals.
- Development of cash reserve and budgeting policies.
- Provide guidelines for capitalization of RPU assets.
- Provide funds to maintain and invest in its utility infrastructure.
- Enhance short and long-term financial credit quality by helping to achieve the highest possible credit and bond ratings.
- Provide guidance and controls for effective investment of RPU funds in accordance with City investment policies and State law.
- Provide the Board and City Council with a framework for measuring fiscal performance of RPU against established parameters and guidelines.
- Link long-term financial planning with day-to-day operations.
- Document the Board and City Council philosophy for effective ratemaking and recovery of RPU costs of electric and water service.

These policies will be updated at a minimum once every three years to reflect needed changes in policy.

Financial Reporting

In accordance with the City's policies and procedures, RPU shall maintain a strong system of internal controls, with appropriate segregation of duties, to ensure reliable financial reporting, effective and efficient operations, and compliance with applicable state and federal laws and regulations. RPU shall maintain its accounting records on an accrual basis and report on its financial condition and results of operations in accordance with Generally Accepted Accounting Principles (GAAP) as promulgated by the Governmental Accounting Standards Board (GASB). RPU shall establish its electric chart of accounts following the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission (FERC) and its water chart of accounts following the Uniform System of Accounts prescribed by the California Public Utilities Commission (CPUC). While the electric and water utilities are not subject to the regulations of FERC and CPUC, respectively, certain regulatory reporting requires that financial information be presented using the Uniform System of Accounts. RPU shall follow electric and water industry practices in accounting for operations.

RPU shall prepare financial reports for the Board in accordance with the requirements of Section 1202 of the City Charter. RPU shall annually prepare full-accrual financial statements, including the Management's Discussion and Analysis and the accompanying Notes to the Financial Statements.

Internal and External Audits

RPU's Finance Division with the approval of the General Manager may arrange for periodic internal audits which will be performed by the City's Office of Organizational Performance and Accountability Division staff as needed.

RPU's Finance Division shall also participate in the auditing and monitoring of joint power agencies and joint projects in which RPU shares an interest or entitlement.

RPU's annual financial statements shall be subject to an audit by independent auditors from a certified public accounting firm whose report shall be included as part of RPU's annual report. These statements shall be prepared within six months of the close of the previous fiscal year, and will be presented to the Board and City Council.

Cash Reserves

Properly designed reserve policies send a positive signal to ratepayers, investors, and regulatory and credit rating agencies that the City is committed to maintaining the long-run fiscal strength of RPU. Strong and transparent financial policies, including maintaining prudent reserves for emergencies, rate stability, working capital and capital improvements are consistent with best practices in the utility industry and are important to RPU as they help to:

- Maintain the short-term and long-term financial health of RPU.
- Maintain stable rates for customers and help ensure manageable rate increases.
- Provides funding unanticipated cost contingencies.
- Ensure funds exist for system improvements.
- Ensure cash exists for the timely payment of bills.
- Act as a significant positive credit factor in bond ratings.

The Cash Reserve Policy describes the following reserves:

- Restricted Reserves,
- Unrestricted, Designated Reserves, and

- Unrestricted, Undesignated Reserves.

The policy sets target (minimum) and maximum levels for the unrestricted, undesignated reserves. Please refer to Appendix A for RPU's Cash Reserve Policy.

Operating and Capital Budgeting

Sound budgeting processes are needed to provide a control framework for management, governance oversight of the operation of RPU, and transparency to our customers. Budget processes allow for proper planning and accountability for meeting spending targets and key performance indicators.

RPU shall prepare two-year operating and five-year capital budgets, which shall serve as RPU's revenue and expenditure plan. These budgets shall be prepared in accordance with existing City Management, Board, and City Council policies, procedures, and guidelines.

Operating Budget

Budget Development

RPU shall strive to maintain a balanced budget in which operating revenues shall fully cover operating expenditures and debt service. In the event a balanced budget is not attainable, and the cause of the imbalance is not expected to last for more than one year, the planned use of undesignated, unrestricted reserves to balance the budget is permitted. In the event that a budget shortfall is expected to continue beyond one year, the planned use of these reserves must be developed as part of a corresponding strategic financial plan to close the gap through revenue increases and/or expenditure decreases. Staff will also adhere to withdrawal and replenishment of reserve guidelines as outlined in the Cash Reserve Policy.

Operating budgets shall be developed to meet the strategic goals and mission of RPU. The budget shall provide for adequate maintenance of capital plant and equipment, and funding for their orderly replacement within the approved rate plan. RPU will avoid using temporary revenues to fund ongoing operating expenses, programs, or services. Using RPU'S rate plan and guidance provided by the City's Finance Department, RPU's Finance Division shall prepare and distribute budget targets to the various divisions to assist with preparing their individual budgets. Any amounts exceeding budget targets will require adequate justification for approval by the General Manager to be included in the Department's proposed budget submittal to City Finance.

Supplemental appropriations must be approved by the Board and City Council in the event expenditures in a fiscal year are expected to exceed the approved budget. RPU is prohibited from exceeding its City Council authorized expenditures.

As appropriate, performance measurements shall be included in the annual budget to gauge the effectiveness of programs and identify areas for improvement.

Approval Process

The General Manager shall review the budget and recommend approval of the base budget and supplemental items exceeding targets to the City Manager and the Board before forwarding to the City Council for adoption.

Budget Monitoring

RPU shall maintain a budgetary control system to ensure adherence to the amounts authorized by the City Council. Operating budget versus actual expenditure reports shall be prepared monthly. Budget variances shall be provided in the financial reports to the Board with a written explanation of the variance.

The use of unencumbered prior year operating budget balances (e.g., carryovers) shall be scrutinized and carefully limited, primarily for one-time expenditures, mainly capital expenditures. Operating budget carryovers, in most cases, shall be re-budgeted in the following fiscal year. Per City Charter, all appropriations lapse at fiscal year-end except for capital projects. City Council action is required to carry over the balance of appropriations for all ongoing special programs, grants, and other restricted balances.

Budget Transfers

As per Administrative Manual Policy 06.003.00 Budget Execution and Expenditure Control, transfers between operating and capital accounts are permitted with authorization from the City Finance Budget Division after a written request from management.

Cost Allocations

Annually, a cost allocation plan will be updated by City Finance to document overhead costs of the shared City services to be charged to RPU based on industry standards and Federal Office of Management and Budget (OMB) guidelines and actual costs. In turn, RPU will update annually their cost allocation for shared services of the Electric and Water funds to be allocated to internal RPU divisions and other City Departments, as appropriate.

Operating Grant Applications and Use of Grant Funds

RPU shall actively pursue federal, state and other grant opportunities when deemed appropriate. Before accepting any grant, RPU shall obtain Board and City Council approval and thoroughly consider ongoing obligations that will be required in connection with acceptance of said grant. All grant accounting should follow City grant accounting policies and procedures.

Expenditures and Board Authority

On November 2, 2004, the voters in the City passed Measure MM (Measure) which became effective upon approval of the City Council on May 17, 2005. The Measure amended the City Charter provisions and granted the authority to award bids and authorize procurement contracts exceeding $50,000 to the Board. The effect of the Measure streamlines the process for procurement approvals by eliminating the need for City Council approval, assuming funding authority exists in RPU's budget, as adopted or amended by the City Council. Contracts that are subject to the Measure are public works, goods, non-professional and professional services. Contracts related to property acquisition/dispositions, power and transmission and other negotiated agreements are not affected by the Measure and are approved by the City Council after review and recommendation by the Board.

Capital Budget

RPU will prepare a Capital Improvement Plan (CIP) based on internally developed financial targets and established priorities.

Budget Development

Capital improvement budgets shall be developed to meet the strategic goals and mission of RPU. The CIP is prepared every two years in conjunction with the operating budget. This is a multi-year plan forecasting annual capital improvements for a minimum of the next five years. This budget shall be prepared in

accordance with existing Board and City Council policies, procedures, guidelines, and any requirements included in the California Government Code.

The plan will identify expected funding sources for the budgeted costs, with the goal of minimizing rate impacts over the long term. Funding options include recovery through rates, contributions in aid of construction, use of reserves, and/or borrowing. RPU will strive to fund no less than 10% of the current budget year CIP through the use of rates or current revenues such as contribution in aid of construction or other reimbursements.

As part of the biennial CIP, budgeted capital projects shall include a brief report on the need for the project, funding source, description, prioritization, and impact on the operating budget of RPU, water and electric customer service and system reliability.

Approval Process

The CIP shall be reviewed and approved by the Board and City Council biennially, with the first two years of said plan included in the City Council adopted two-year operating budget.

Budget Monitoring

RPU shall maintain a budgetary control system to ensure adherence to the amounts authorized by the City Council. Budget versus actual expenditure reports shall be prepared monthly and provided to managers. For projects over $200,000, monthly reports showing budget versus actual, percentage of completion, and status shall be provided to the Board.

Completed capital projects should be closed out timely. Unencumbered balances of capital projects should be reviewed at year-end for appropriateness and scrutinized to ensure any carryover balances into the following fiscal year are appropriate.

On completion, a final report of capital projects over $200,000 shall be prepared for management and Board review. The report shall detail the actual and budgeted project costs, provide analysis for final project costs with explanations, and include final comments regarding the impact to customer service and system reliability.

Asset Capitalization

Capitalization policies establish the minimum cost that shall be used to determine the capital assets that are to be recorded in RPU's annual financial statements.

As a policy, assets with an acquisition value of $5,000 or more and a useful life of more than one year are capitalized, except for those assets that are capitalized at lower amounts due to industry standards, such as electric and water meters, and transformers. Acquisition value includes the cost of the equipment and any associated costs incurred to make the equipment ready for service in the purpose for which it was intended, including installation costs. Intangible assets, such as software, that cost more than $100,000 with useful lives of at least three years are capitalized at cost.

The costs of improvements and replacements are capitalized if they meet at least one of the following criteria:

1. The useful life of the asset is extended.
2. The quantity of services provided by the asset is increased.
3. The quality of services provided by the asset is enhanced.

Debt Management

The City's Debt Management Policy shall govern, except as otherwise directed by the City Charter, the issuance and management of all debt and lease financings funded in the capital markets. While adherence to this policy is desired, the City and RPU recognize that changes in the capital markets as well as unforeseen circumstances may, from time to time, produce situations that are not covered by the Debt Management Policy and may require modifications or exceptions to achieve RPU and City goals. Exceptions to the policy will be approved by the City's Chief Financial Officer/City Treasurer, Board, and City Council.

The City's Chief Financial Officer/City Treasurer, with the assistance of RPU's Assistant General Manager - Finance, will have the responsibility and authority for structuring, implementing, and managing RPU's debt and financing program, in accordance with Board and City Council authorizations and the City's debt management guidelines and policies.

Repayment of RPU debt issues and setting of utility rates

The revenues generated by RPU must be sufficient to meet the minimum coverage ratios of principal and interest. RPU's Revenue Bonds will not be secured by any pledge of ad valorem taxes or general fund revenues of the City and will be payable solely from the Electric or Water Fund.

The Board will make necessary adjustments to, and the City Council shall approve rate structures and rate plans relating to, revenues pledged to a bond issue, if necessary to meet bond covenants.

In determining the affordability of proposed revenue bonds, RPU will perform an analysis comparing proposed annual net revenues to estimated annual debt service. For the City to issue new revenue bonds, RPU net revenues (as defined in the resolution authorizing the revenue bonds in question) shall be at least 110% and 125% of average annual debt service for electric and water bonds, respectively, and for the year in which the payment requirements are scheduled to be the greatest.

However, for planning purposes, and in order to maintain RPU's favorable credit ratings, RPU will target annual net revenues at 200% of average annual debt service for direct debt, and 130% of average annual debt service including indirect debt. In addition, estimated net revenues will be targeted at a minimum of 175% of the maximum annual debt service for financial projection purposes. Should financial planning indicate dropping below the minimum target, RPU will implement plans to return the annual debt service coverage to their minimum targeted levels within three years. Such plans will be provided to the Board and City Council within twelve (12) months.

RPU shall monitor its system leverage (i.e., debt ratio) in comparison to other similarly sized and rated utilities and report such information to the Board at least quarterly.

For additional details, refer to the City's Debt Management Policy.

Credit Ratings

Maintaining high credit ratings from the major rating agencies, such as Standard and Poor's (S&P), Fitch Ratings, and Moody's, is crucial in meeting RPU's goal of providing utility services to the citizens of Riverside at the most economical cost. Higher ratings equate to reduced borrowing cost and greater

financial flexibility particularly in unstable financial markets; consequently, maintaining or improving the electric and water credit ratings is a high priority.

RPU shall maintain on open dialog, communicate any significant events to the rating agencies and investors, and provide annual audited financial statements within prescribed deadlines.

RPU seeks to minimize financing costs to its ratepayers by maintaining the highest possible credit ratings for all categories of short- and long-term debt that can be attained without compromising delivery of services and achievement of adopted RPU policy objectives and goals. RPU recognizes that external economic, natural, or other events may, at times, affect the creditworthiness of its debt. Nevertheless, RPU is committed to ensuring that actions within its control are prudent.

Minimum Bond Ratings

RPU will seek a minimum investment grade rating of "A+" or greater on any direct debt and will seek credit enhancements such as lines and letters of credit or insurance when necessary for marketing purposes, while considering such factors as availability and cost-effectiveness.

RPU will maintain lines of communication with the rating agencies to ensure that it has a focus on some of the main ratings drivers used in developing a bond rating. An example from Moody's as to the areas of focus is in the following table:

Rating factor	Influences
Cost recovery framework	• Monopoly power • Service area characteristics • Customer base stability
Cost recovery willingness	• Political risks • Timeliness of recovery and history • Local government supportiveness • General fund transfer policy
Management of generation risks	• Diversity of supply • Reliability and cost of supply & distrib • Resource planning
Competitiveness	• Rate competitiveness
Financial strength	• Liquidity (reserves) • Leverage (debt ratio) • Operating resiliency (debt service coverage)

Determination of the Number of Ratings and Selection of Rating Services

In the planning stage of a bond issuance, the City's Chief Financial Officer/City Treasurer in conjunction with RPU's Assistant General Manager – Finance and RPU financial advisors shall determine the number of credit ratings and which credit rating services are desired on an issuance-by-issuance basis.

Investments

Investment Policy overview

RPU's cash and investments, except for cash and investments with fiscal agents, are invested in a pool managed by the City Treasurer. RPU does not own specific, identifiable investments of the pool. Cash

accounts of all City funds are pooled for investment purposes to enhance safety and liquidity, while maximizing interest earnings. The pooled interest earned is allocated monthly to RPU by the City based on RPU's month-end cash balances.

Prudent investing will allow the City to generate returns that can be used as a revenue source, while allowing for safety of principal for its future use.

As outlined in the City of Riverside Investment Policy (Investment Policy), the primary objectives of the City's investment activities, in accordance with California Government Code Sections 53601 through 53659 include:

Safety: Safety of principal is the foremost objective of the investment program. Investments of the City shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio.

Liquidity: The City's investment portfolio will remain sufficiently liquid to enable the City and RPU to meet all operating requirements which might be reasonably anticipated.

Return on Investments: The City's investment portfolio shall be designed with the objective of attaining a rate of return commensurate with the City's investment risk constraints and the cash flow characteristics of the portfolio.

The Investment Policy requires the "prudent investor" standard, defined as: *"Investment shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, direction and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived. Generally investments are limited to an average maturity of the portfolio of three years, with maximum maturities of any one security limited to five years".*

The City's Investment Policy is reviewed annually by the City Council Investment Committee and approved by Resolution by the City Council.

General oversight of investments

The Riverside City Charter grants the City Treasurer authority for investing unexpended cash in the City Treasury. The Investment Policy applies to all financial assets of the City of Riverside as accounted for in the Comprehensive Annual Financial Report—including those of RPU. Actual investment performance is monitored continually by the City Treasurer with statistics and activity reports presented at least quarterly to the City Manager and the City Council.

The City Treasurer shall meet monthly (or as otherwise agreed) with the Assistant General Manager – Finance to review the performance of RPU's investments, RPU's short- and long-term cash flow forecasts and the investing of RPU unexpended funds in investments to meet RPU cash flow needs. The Assistant General Manager - Finance may offer investment recommendations to the City Treasurer. The City Treasurer has the final authority for the investment decisions as stated in the City's Investment Policy.

The Investment Policy also contains guidelines for performance evaluation, delegations of authority, investment committee, ethics and conflicts of interest, safekeeping of securities, internal controls, reporting, qualified brokers, collateral requirements, authorized investments, derivative investments, legislative changes, allocation of investment earnings, limitations of market value erosion, and portfolio management activity.

The Investment Policy requires that annual revisions be adopted via resolution of the City Council. For additional details, refer to the City's Investment Policy.

Risk Management

Managing enterprise risk is a control measure for ensuring that assets and operations are safeguarded and that proper mitigation plans are in place for the sustainability of RPU.

RPU's assets will be protected by maintaining adequate insurance coverage through commercial insurance carriers, by maintaining adequate RPU reserves, or via the City's self-insurance fund administered by the Risk Management Division of the City's Finance Department. Annually coverage needs are evaluated by the City's Risk Manager with the assistance of the RPU Finance Division.

Investment risks shall be mitigated via the City's Investment Policy, and are administered by the City's Finance Department.

Interest rate and other risks associated with RPU's debt portfolio will be addressed under the City's Debt Management Policy.

Risks associated with wholesale power markets, including purchases and sales of wholesale energy and other transactions with the California Independent System Operator's balancing authority area shall be mitigated via RPU's Power Resources Risk Management Policies. This set of policies includes the Energy Risk Management Policy, Wholesale Counterparty Risk Management Policy and Authorized Energy Transactions Policy. The Board will review and recommend City Council approval of substantive modifications to the Power Resources Risk Management Policies. Substantive modifications and amendments require approval of the City Council prior to becoming effective.

Except for periods of peak demand or system emergencies, the water utility provides 100% of its retail customer demand from entitlements in local groundwater, which is subject to federal and state water quality standards concerning maximum contaminant levels. RPU will proactively pursue potentially responsible parties for negative impacts due to their contamination of these sources and seek financial protection to avoid imposing these costs on RPU ratepayers.

RPU operates in a continually evolving regulatory environment. In order to help mitigate the negative impacts to RPU and its ratepayers, RPU shall monitor regulations that both negatively and positively impact RPU's rates and advocate or influence legislation and/or regulation that is most beneficial to RPU's ratepayers.

Forecasting and Financial Planning

Long-range forecasting is an integral part of developing RPU strategic objectives and ensuring that user rates will support current operations and long-term goals.

RPU shall prepare a five-year financial plan for electric and water operations to be used for internal planning purposes. The financial plan for each utility (i.e., electric and water) shall contain projections for future expenditures (all operating expenses, forecasted capital improvements and debt service) and forecasted revenues and other funding sources. The financial plan should be updated quarterly for use in reporting to the City's Finance Department and other needs, such as rating agency monitoring, etc.

The financial plans shall calculate future key performance indicators (including coverage ratios, liquidity levels, leverage, reserve requirements, and operating ratios) and will be used to compare forecasted financial performance with internal benchmarks and industry trends. The financial plans can be used to project future rate adjustments and develop rate plans necessary to maintain or improve the financial strengths of each utility.

Revenue Development and Monitoring of Customer Rates

Ratemaking Principles

RPU rate structures will be designed to provide a transition to rates that align with the transformational changes occurring in the electric and water industries. RPU's rates shall be designed to achieve the following goals:

- Achieve full recovery of costs.
- Equitably allocate costs across and within customer classes.
- Encourage efficient use of water and electricity.
- Provide rate stability.
- Offer flexibility and options.
- Maintain rate competitiveness in region.
- Be simple and easy to understand.

Development of customer rates for RPU electric and water services

Rates will be established by developing a cash basis revenue requirement for electric and water services that recovers these RPU cash outflows:

1. Operation and maintenance expenses
2. Rate funded capital improvements
3. Debt service
4. Contributions to the City and other obligations of RPU

Retail rates for water and electric services shall be cost-based and consistent with industry practices and California law. Rate studies shall be conducted periodically to ensure that water and electric rate structures are equitable and adequate to meet RPU's revenue requirements.

Revenue Monitoring

Revenues shall be monitored regularly, showing variances between current revenues, prior-year amounts, and amounts currently budgeted. If projections show that actual results will fall below financial targets, RPU will develop plans necessary to improve the Utility's financial strength and report to the Board and City Council.

RPU will establish internal controls to ensure that all revenues are collected in a timely manner. Delinquent customer accounts and miscellaneous invoices shall be collected in compliance with collection procedures outlined in the established Rules and Rates Schedules and/or City Administrative Policies.

One-time revenues received from the sale or disposal of a long-term asset, such as land, shall not be used for ongoing operations, but will be segregated to be used for the acquisition of other long-term assets. Proceeds from any sale should be placed in the designated Property Reserve as discussed in the Cash Reserve Policy.

APPENDIX A

CASH RESERVE POLICY



Cash Reserve Policy

Adopted on March 22, 2016

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Introduction & Purpose

Riverside Public Utilities ("RPU") is a department of the City of Riverside and manages the City's water and electric utilities. RPU provides high quality and reliable services to over 109,000 metered electric customers and approximately 65,000 metered water customers throughout the City of Riverside.

RPU is governed by the City Council and the Board of Public Utilities (the "Board"). The City Council sets financial management policies, as recommended by the Board. This Cash Reserve Policy (the "Policy") is designed to establish guidelines to ensure the fiscal stability of RPU and provide guidance to RPU staff in the management of RPU's finances.

Properly designed reserve policies send a positive signal to ratepayers, investors, and regulatory and credit rating agencies that the City is committed to maintaining the long-run fiscal strength of RPU. Strong and transparent financial policies, including maintaining prudent reserves for emergencies, rate stability, working capital and capital improvements, are consistent with best practices in the utility industry and are important to RPU as they help to:

- Maintain the short-term and long-term financial health of RPU.
- Maintain stable rates for customers and help ensure manageable rate increases.
- Fund unanticipated cost contingencies.
- Ensure funds exist for system improvements.
- Ensure cash exists for the timely payment of bills.
- Act as a significant positive credit factor in bond ratings.

This Cash Reserve Policy describes the following reserves:

- Restricted Reserves,
- Unrestricted - Designated Reserves, and
- Unrestricted, Undesignated Reserves.

The policy sets target (minimum) and maximum levels for the unrestricted, undesignated reserves.

Definitions

RPU's reserves are classified into three categories:

- Restricted Reserves,
- Unrestricted - Designated Reserves, and
- Unrestricted, Undesignated Reserves.

Restricted Reserves

Restricted reserves are established and utilized for narrowly defined purposes as specified by legal restrictions, bond covenants, and other regulations or ordinances. Current Restricted Reserves include:

- Decommissioning Fund for San Onofre Nuclear Generating Station ("SONGS")
- Regulatory Requirements Reserve (Cap and Trade auction proceeds)
- Unspent Bond Proceeds
- Bond Redemption Reserve
- Electric Public Benefit Fund
- Water Conservation Fund

Unrestricted - Designated Reserves

Unrestricted, designated reserves are that portion of unrestricted reserves that meet specific purposes set aside by the Board and City Council. Designated reserves may be held for specific capital and operating purposes. Current unrestricted, designated reserves are as follows:

- ***Customer Deposits*** (electric and water funds) – Monies held on behalf of RPU's customers as required to be utilized if a customer fails to pay their utility bill. The amount held equals amounts collected from electric and water customers based on Board and Council adopted Electric and Water Rules.
- ***Additional Decommissioning Liability Reserve*** (electric fund only) – Established to accumulate funds for the uncertainty of costs associated with the SONGS Decommissioning activities. These funds are in addition to RPU's funded trust held by the trustee (restricted reserve). The decommissioning funds held in the restricted reserve represent RPU's proportionate share of the independent Decommissioning Cost Estimate ("DCE"). If the DCE is increased, RPU will need to fund additional monies to the trust for decommissioning. On June 8, 2020 and June 16, 2020, the Board of Public Utilities and City Council, respectively, approved the increase in annual funding to the SONGS Additional Decommissioning Liability Reserve from $1.6M to $2.0M annually beginning in fiscal year 2020/21, due to an anticipated increase in the SONGS DCE. ~~Annual funding of the designated reserve is currently $1.6M which equaled the amount contributed annually to meet RPU's proportionate share of the restricted decommissioning trust.~~ This amount can be evaluated and adjusted as needed.
- ***Electric Reliability Reserve*** (electric fund only) – Established to accumulate amounts received from retail customers through the Reliability Charge for the purpose of funding debt service and capital costs for transmission and internal generation projects. Funding for this reserve will inherently fluctuate based on revenue received from customers, offset by approved debt service payments and capital costs on transmission and internal generation projects.
- ***Mission Square Improvement Reserve*** (electric fund only) – Established to accumulate funds for major improvements to the Mission Square facility. This reserve is funded by an annual contribution equal to 2% of the building value up to a maximum reserve equal to 25% of the building value.
- ***Capital Repair/Replacement Reserve*** (electric and water funds) – Established to accumulate amounts for repairs and replacement of facilities, vehicles, and technology outside of the Capital Improvement Program. Examples would be roof replacement, vehicle replacement, desktop technology replacement, etc. Funding for this reserve will be accumulated~~built~~ over a three year period based on a historical 10-year averages of replacement costs.
- ***Recycled Water Reserve*** (water fund only) – Established to set aside funds for a recycled water program. Funding was from a legal settlement from the City.
- ***Property Reserve*** (electric and water funds) – Established to accumulate all proceeds from surplus property sales to be used in the future for the purchase of property needed for operations, or for other long-term capital assets/projects. Funding is from proceeds from the sale of surplus property.
- ***Dark Fiber Reserve*** (electric fund only) – Established to accumulate proceeds from fiber leasing activity and account for expenditures of the dark fiber program.

RPU will use designated reserves to mitigate the impacts of known and impending exposures. The withdrawal and replenishment of Council/Board approved designated reserves and their allowable uses will be tracked individually, but the specific use of designated reserves falls outside the scope of this policy and is subject to Board and Council approval.

Unrestricted, Undesignated Reserves

Undesignated reserves are the remaining unrestricted reserves that may be used for any lawful purpose and have not been designated for specific capital and operating purposes. The following Unrestricted, Undesignated Reserve Policy addresses the levels, use and replenishment of this type of unrestricted reserves.

Unrestricted, Undesignated Reserve Policy

The Cash Reserve Policy outlines the appropriate types and target (minimum and maximum) levels of unrestricted, undesignated reserves as prescribed below.

Overall Policy Statement

RPU will have sufficient unrestricted, undesignated reserves to maintain or improve its credit ratings, ensure that operating and maintenance costs will be paid in a timely manner, to pay debt service obligations, and to invest in needed capital improvements and equipment replacement on a timely basis. In addition, RPU will maintain sufficient reserves to minimize rate increases due to market volatility, weather impacts on demands, emergencies (such as natural disasters), and regulatory changes.

Operating (Working Capital)

- Definition and Purpose: Ensures sufficient resources to pay budgeted operating and maintenance expenses, including power supply costs, recognizing the timing differences between payment of expenditures and receipt of revenues.
- Target (Minimum) Level:
  - Electric: Equal to 60 days of operating and maintenance expenses, including power supply costs~~,~~ and less operating and maintenance expenses funded with restricted or unrestricted – designated reserves,~~,~~ based on the most recent audited financial statements.
  - Water: Equal to 60 days of operating and maintenance expenses and less operating and maintenance expenses funded with restricted or unrestricted – designated reserves, based on the most recent audited financial statements.
- Maximum Level:
  - Electric: Equal to 90 days of operating and maintenance expenses, including power supply costs, and less any operating and maintenance expenses funded with restricted or unrestricted – designated reserves based on the most recent audited financial statements.
  - Water: Equal to 90 days of operating and maintenance expenses and less operating and maintenance expenses funded with restricted or unrestricted – designated reserves, based on the most recent audited financial statements.
- Events or Conditions Prompting Use of the Reserve: This Reserve may be routinely used by RPU to cover temporary cash flow deficiencies caused by timing differences between revenues and incurring expense obligations and unexpected increases in operating expenses.

Rate Stabilization

- Definition and Purpose: Mitigates rate shock due to temporary and transitional regulatory changes, loss of a major resource, sharp demand reduction or market volatility.
- Target (Minimum) Level:
  - Electric: 10% of operating revenues, reflecting the low-end of the risk quantification for power cost uncertainties due to load reduction, market energy price fluctuations, unit contingencies, transmission costs, and regulatory mandates.
  - Water: Equal to 7% of operating revenues, reflecting the low-end of historic fluctuations in retail sales from year to year due to unforeseen events (e.g., recession, drought).
- Maximum Level:
  - Electric: 20% of operating revenues, reflecting the high-end of the risk quantification for power cost uncertainties due load reduction, market energy price fluctuations, unit contingencies, transmission costs, and regulatory mandates.
  - Water: Equal to 15% of operating revenues, reflecting the high-end of projected fluctuations in retail sales from year to year due to unforeseen events (e.g. recession, drought).

- Events or Conditions Prompting Use of the Reserve: This Reserve may be used to cover unexpected decreases in operating revenues and increases in operating costs to reduce year-over-year volatility in needed rate increases, as approved by Board and City Council.

Emergency Capital

- Definition and Purpose: Provides funds to ensure ability to repair system after an emergency or natural disaster such as a flood, earthquake or major windstorm
- Target (Minimum) Level: Equivalent to approximately 1% of the value of depreciable capital assets for the Electric and Water Utility, as reported on the most recent audited financial statements.
- Maximum Level: Equivalent to approximately 2% of the value of depreciable capital assets for the Electric and Water Utility as reported on the most recent audited financial statements.
- Events or Conditions Prompting Use of the Reserve: An emergency event requiring the need to fund necessary capital expenditures (e.g. natural disaster causing treatment facility closure, conveyance disruption, loss of substation or generating asset, etc.) as approved by Board and City Council.

System Improvements Capital

- Definition and Purpose: Provide funds to ensure continuity of construction over fiscal years to be reimbursed by bond proceeds or other resources.
- Target (Minimum): 6 months of the ~~following years~~ three year average of approved ongoing capital improvement plan expenditures or budget including previous year audited actual expenditures, current years original budget expenditures, and the following years original budget expenditures for each Utility. The calculation is exclusive of any capital improvement expenditures funded with restricted or unrestricted – designated reserves other than the unspent bond proceeds restricted reserve.
- Maximum Level: 9 months of the ~~following years~~three year average of approved ongoing capital improvement plan expenditures or budget including previous year audited actual expenditures, current years original budget expenditures, and the following years original budget expenditures for each Utility. The calculation is exclusive of any capital improvement expenditures funded with restricted or unrestricted – designated reserves other than the unspent bond proceeds restricted reserve.
- Events or Conditions Prompting use of the Reserve: This Reserve may be used to fund capital expenditures during the year as funding resources are acquired (e.g., bond proceeds, capital contributions, revenues, etc.), as approved by Board and City Council.

Debt Service

- Definition and Purpose: Ensures ability to make debt service payments in an extreme event that may impact RPU's ability to provide services, thus impacting revenues at a time critical infrastructure repairs are needed to restore systems. The Debt Service Reserve is intended to prevent an event where RPU would be unable to pay its debt service obligations during such emergencies, or extreme market disruptions.
- Target (Minimum) and Maximum Level: The maximum debt service payment (semi-annual) in the upcoming fiscal year for each Utility.
- Events or Conditions Prompting the Use of the Reserve: The Debt Service Reserve may be utilized in the event RPU is otherwise unable to pay its debt service obligations. It is not anticipated that RPU would ever utilize these reserves absent a significant disaster or extreme market disruption, and only with the approval of Board and City Council.

Use of Line of Credit as Available Reserves

RPU may obtain and utilize a line of credit (LOC) as an alternative to holding cash reserves to meet its target minimum reserve level as prescribed. A LOC is a low-cost financing arrangement between a bank and RPU that establishes an available amount of credit that RPU can draw on if needed. Utilizing a LOC to augment RPU's cash reserves will benefit RPU during periods of capital spending allowing RPU to utilize cash reserves on capital projects and reduce rate impacts to customers, while remaining in compliance with target minimum reserve levels. RPU does not plan to draw on the LOC. Instead, it provides flexibility and operating liquidity similar to cash reserves if there is an emergency need and also allows RPU to meet the overall liquidity and reserve levels that support RPU's strong credit ratings. The size of the line of credit will be determined as part of the financial planning process, taking into account forecasted revenues and other funding sources, timing of debt issuance, as well as projected fiscal performance to meet long-term financial goals. Should the Board and City Council decide to no longer utilize an LOC as a reserves balance tool, staff will provide the financial planning and increase in rates necessary to build back cash reserves to minimum required targets.

General Provisions

While these areas of consideration were evaluated in order to determine the appropriate size of the reserves, RPU will maintain such monies pooled in each utility's unrestricted, undesignated reserve. These reserve allocations are consistent with industry standards for similarly rated electric and water utilities. Each component of the reserves is sized at less than the maximum possible exposure for each component because it is unlikely several of the risks each enterprise faces would materialize simultaneously.

Withdrawal & Replenishment of Reserves

RPU will treat the targeted reserve levels as practical minimums and allow reserves to increase or decrease as necessary within the minimum and maximum levels prescribed above.

To the extent that unrestricted, undesignated reserves plus the LOC, if applicable, are above the target and below the maximum, the Board and Council have the flexibility to direct staff to utilize those available funds to pay for capital projects (reducing the need for future debt), pay down unfunded liabilities such as pension obligations, defease outstanding debt, or fund other strategic objectives. No other action by RPU will be required if reserves are between the minimum and maximum level unless directed by the Board and City Council.

If reserve funds exceed the Maximum level, RPU will seek Board and City Council approval to use the excess to finance capital improvements on a pay-as-you-go basis, pay down existing debt, offset other long-term liabilities such as pension obligations, reduce rates or for other strategic purposes.

Reserve levels below the minimum targeted reserves will leave RPU exposed to significant operational risks. Should RPU draw down reserves below the minimum targeted level, RPU will implement plans to return reserves to their minimum targeted levels within three years. Such plans will be provided within twelve (12) months.

Reporting and Oversight

Reserve levels will be monitored during the fiscal year and reported in the financial reports. Reserve target (minimum) and maximum levels will be analyzed annually and an over/under reserve determination shall be made in conjunction with year-end financial results. These results will be reported to the Board and City Council as part of the year-end financial report presentation. Should unrestricted designated or undesignated reserve levels need adjustment due to new risk factors due to changes in the industry, these will be brought to the Board and City Council as part of the year-end report.

The Policy will be reviewed annually, and updated (at a minimum once every three years) if there are material changes in the risk exposures or new conditions that require changes in reserve levels.

Conclusion

This Policy provides directives to RPU management and staff for decisions and recommendations related to the financial profiles of RPU.

In its most abbreviated form, the Policy sets targets for reserve balances based on the risk profiles of the Electric and Water utilities individually and establishes tolerable maximums. The Policy also provides recommended actions when reserves deviate from the target levels.