
LCRA BOARD POLICY

301 – FINANCE

Aug. 23, 2023

301.10 PURPOSE

This policy provides a framework from which LCRA's financial integrity will be maintained while serving the long-term interests of its customers and other constituencies. LCRA recognizes that maintaining financial integrity is critical to accomplishing its goals and discharging LCRA's primary customer and public service responsibilities. This policy establishes processes to be used by the LCRA Board of Directors (Board) to define the strategic plan for LCRA and to approve specific program goals, objectives and associated budgets.

301.20 DEFINITIONS

Business Plan – The business plan is the document approved by the Board annually that establishes the Board's goals and priorities. The business plan includes operating and capital budgets as well as projections of LCRA's overall financial performance and capital financing plans. It describes the projects, products and services that support the associated revenues and expenditures over a five-year period.

Debt Service Coverage (Coverage) – Debt service coverage is the ratio of the fiscal year's ending total revenues minus total operating and maintenance expenses (net of depreciation, amortization, and other revenue and expense exclusions resulting from prior period funding), divided by scheduled debt service on all obligations as approved in the business plan.

Equity Ratio (Ratio) – The calculation is the ratio of total equity divided by total assets.

Fixed-Rate Debt – Fixed-rate debt consists of coupon securities that have a scheduled maturity or mandatory sinking fund redemption date. Fixed-rate debt that has been synthetically converted to variable rate debt via a derivative instrument will be classified as variable-rate debt for the term of the derivative instrument.

Long-Term Liabilities – Long-term liabilities are (1) principal amounts on long-term debt instruments, (2) pension liabilities, and (3) amounts owed on long-term obligations.

Operating and Maintenance Expenses – Operating and maintenance expenses consist of all reasonable and necessary costs and expenses incurred in the operation and maintenance of the LCRA system.

Variable-Rate Debt – Variable-rate debt consists of securities on which the interest rate varies over time (a) based on an index or formula such as variable-rate demand notes or auction-rate bonds, or (b) because the securities are sold in the short-term market (with a maturity not exceeding 270 days), such as commercial paper.

301.30 FINANCIAL OBJECTIVES

In seeking to fulfill its customer and public service objectives, LCRA will maintain a high level of financial stability and will not compromise long-term financial integrity to achieve short-term benefits.

The GM/CEO is authorized to engage financial service providers and other related professional service providers if deemed necessary and appropriate by the GM/CEO in consultation with the chief financial officer, considering the expertise and cost of any such service provider. The GM/CEO will provide an annual report to the Board listing all contracts into which LCRA entered pursuant to this paragraph.

301.301 Debt Service Coverage. To provide a margin of safety in LCRA's financial affairs, revenue levels will be set to target a debt service coverage ratio of 1.25x on the total debt service for all debt obligations. In the event overall debt service coverage is projected to be below 1.25x for any fiscal year, the Board will promptly implement a plan, to be recommended by staff, which could include rate increases, cost reductions or other means to achieve a debt service coverage ratio of 1.25x.

In the event the actual LCRA system fiscal year debt service coverage ratio exceeds 1.25x, the financial performance of the wholesale power business will be evaluated to determine if the actual wholesale power debt service coverage ratio exceeds 1.25x for the fiscal year. If such excess exists, staff will submit to the Board a plan to provide the existing long-term wholesale electric customers with appropriate credits or other rate relief in an amount equal to the excess, provided that after such credit or rate relief, LCRA will achieve an actual system debt service coverage ratio of 1.25x and be in compliance with any covenant requirement in any bond resolution or policy of LCRA. This policy will be applicable except in periods when funds are needed to provide equity for the generation capital program and meet operating reserve requirements.

Upon completion of the annual audit of fiscal year-end financial statements, the existing long-term wholesale electric customers will be provided an analysis of LCRA's financial performance for that period in order to provide a complete accounting of funds above a 1.25x debt service coverage ratio.

301.302 Rates and Prices. LCRA will design rates and prices that are intended to ensure LCRA meets its financial obligations, recover reasonable costs in a timely fashion, and maintain financial integrity as required by regulatory and contractual requirements. These rates will provide a stable and predictable flow of revenues to maintain appropriate levels of revenue to achieve LCRA's goals. Revenue levels will be evaluated in consideration of, but not limited to, bond ratings, capital funding

requirements, current business conditions, economic projections and load-growth assumptions, delays inherent in the regulatory process, and the projected size and frequency of necessary rate adjustments. These revenues will be adequate to cover operating and maintenance expenses, debt service, covenanted debt service reserves, liquidity requirements, and equity funding for the capital program.

Rates and prices for wholesale power services to existing long-term wholesale electric customers will be consistent with contractual commitments regarding rates and prices. Revenue collected from wholesale power rates, with the exception of contributions to the Public Service Fund (PSF), will be used for the benefit of the generation system. Rates and prices for service to other electric customers will be set, at a minimum, to recover the cost of providing the services.

Rates and prices for LCRA's raw water services will be based on criteria as specified in LCRA Board Policy 501 – Water Resources.

For other LCRA services for which rates are charged, LCRA may employ other appropriate pricing methods as approved by the GM/CEO.

301.303 Sources of Financing. LCRA will use a combination of equity and debt to finance capital additions to the system such that both current and future customers are allocated an equitable portion of the costs. LCRA may borrow for capital projects when it is appropriate to spread the cost of capital assets over their useful lives.

The issuance of debt requires an affirmative vote of three-fourths of the Board. LCRA will not issue debt for working capital items.

Capital market considerations require an equity base to support financing. LCRA will build equity during those periods when major capital projects are not being undertaken by financing capital projects from revenues. In this way, LCRA will build equity sufficient to maintain financial integrity, ensure access to the debt markets and provide for the growing needs of customers.

As appropriate, LCRA will evaluate mechanisms to restructure or refinance debt. LCRA will continually evaluate alternatives to conventional financing to lower the overall cost of capital for ratepayers. Separate system financing also will be considered.

LCRA may structure debt issues such that the average maturity of the debt funding the assets approximates the average life of the assets financed; however, debt issues may be structured with a shorter average maturity if economically justified. LCRA will attempt to maintain a long-term average 30% equity ratio. At no time will the equity ratio fall below 20% without specific Board approval in the business plan. Equity funding of the capital program will be approved in the business plan in compliance with this policy and taking into consideration the extent of contractual obligations of customers to provide the sources of revenue that will support the financing program.

301.304 Variable-Rate Financing. LCRA may use variable-rate debt to provide flexibility in its overall capital program and to manage its overall interest rate exposure.

The variable-rate limit is 25% of total capitalization, long-term debt plus capital employed as presented periodically in LCRA's financial statements.

301.305 Debt Service Reserves. LCRA will covenant debt service reserves in the amount of six months of average annual debt service requirements on outstanding debt.

Debt service reserves may be collected through nonfuel rates or met with proceeds from additional debt or through the use of a surety to mitigate rate impacts.

301.306 Operating Reserves. LCRA will target three months of average operating and maintenance expense for purposes of operating liquidity and maintain reserves for liquidity of two to three months. Compliance will be evaluated at the end of each fiscal year.

These reserves will be collected through nonfuel rates.

If at any time the level of the operating reserves is projected to fall below the minimum two months established by this policy, the Board will promptly implement a plan, to be recommended by staff, to increase rates, reduce costs or otherwise cause there to be sufficient revenues to replenish the level of operating reserves to such target levels within 12 months.

301.307 Management Reserves. The GM/CEO may establish reserves from time to time for management activities.

301.40 PLANNING

301.401 Business Plan. LCRA will prepare a business plan to be submitted for Board approval before the start of each fiscal year. The business plan will include the organization's goals and objectives and will describe the projects, products and services that comprise a five-year forecast for:

- Operating and maintenance expenses.
- Capital expenditures.
- Capital funding sources.
- Operating and other reserve requirements.
- Debt service requirements.

This information will be provided in appropriate detail for LCRA's lines of business and affiliated corporations and for LCRA as a whole.

Adoption of the business plan authorizes the GM/CEO to complete work plans and make associated expenditures within budgets as provided for in accordance with Board policies.

The resolution adopting the business plan will establish the capital and operating budgets for the upcoming fiscal year. Such amounts may not be exceeded without Board approval. Approval of the business plan constitutes authorization to proceed with capital projects included in year one of the plan and establishes the projects' respective lifetime budgets. The resolution adopting the business plan also will include guidelines for authorizing capital spending and reporting requirements for business plan results.

If annual expenditures for operations or capital are expected to exceed Board-authorized levels, additional approval from the Board will be required, except as otherwise provided below. Staff will provide sufficient support for the additional funding request and provide analysis for impacts on current and future rates.

For any project not previously authorized by the Board in the capital plan, authority is delegated to the GM/CEO to approve any capital project with a lifetime budget not to exceed \$1.5 million. Such approval by the GM/CEO will meet the official intent requirements set forth in Section 1.150-2 of the IRS Treasury Regulations. This delegation will apply only when such approval does not cause total capital expenditures to exceed the approved capital plan or materially adversely impact business planning assumptions. In such a situation, Board approval will be required. Staff will communicate any GM/CEO-approved projects to the Board on a quarterly basis. If Board approval is required, staff will communicate to the Board the funding source and rate impact of any new project when Board approval is requested. A new project may require an amendment to the existing capital plan or be managed within the previously authorized annual spending limits.

The general manager and chief executive officer may approve additional funding for an approved capital project that is expected to exceed its lifetime budget, so long as such additional funding does not cause total capital expenditures to exceed the approved capital plan or materially adversely impact business planning assumptions.

301.402 Quarterly Business Plan Update. The GM/CEO will provide quarterly updates that include indicators of year-to-date operational and financial performance, progress toward key goals, general manager and chief executive officer-approved capital project funding, and financial performance projections.

301.403 Customer Involvement. LCRA will seek appropriate input from its customers before the Board's approval of the business plan.

301.50 AFFILIATED CORPORATIONS

Each LCRA affiliated corporation will implement a planning process similar to the process used by LCRA. However, each affiliated corporation should use a process appropriate for its level of activity. The business plan of the affiliated corporation submitted for Board approval will include the following components:

- A description of the affiliated corporation's major programs.
- Operating and capital budgets for the upcoming fiscal year.
- A summary of its annual goals and objectives.
- Five-year forecasts of operating and capital budgets.
- A summary of its rate plan, if applicable.

301.60 SPECIAL FUNDS

LCRA will establish a process to transfer a portion of its revenues derived from its various product lines into special funds to be used to support mission-based activities, long-term resource development, and other activities.

The Board may establish special funds with appropriate implementation policies and program guidelines in order to set aside funds for these various special purposes.

In the event LCRA's financial performance from non-electric operations exceeds the budget targets set forth in the business plan, the Board may approve the supplemental transfer of funds to the established special funds. Any funds approved for transfer by the Board will be subject to compliance with LCRA's bond resolutions.

To the extent established special funds, including accumulated interest earnings, are not disbursed for the special purposes described in the separate policy and program guidelines, LCRA may use the funds for any lawful purpose. In the event that LCRA net revenues are insufficient to satisfy bond obligations, the monies from the Public Service Fund (PSF), Infrastructure Reserve Fund, Resource Development Fund, Liability Reduction Fund, Agriculture Reserve Fund or Public Recreation and Conservation Land Acquisition Fund (PRCLA Fund) – with the exception of any loans, grants or gifts comprising a portion of the PRCLA Fund – may be applied to such deficiencies.

301.601 LCRA Public Service Fund. The LCRA enabling legislation, as amended, and other applicable state laws provide that LCRA has certain statutory duties in the area of community services. While these service activities produce some revenues, the level of their revenue potential is insufficient to provide LCRA the means of implementing effective service programs. LCRA will maintain the PSF to support those activities. The LCRA enabling legislation contemplates the use of revenues derived from LCRA's wholesale power, transmission and water operations for service activities as described in the business plan. Wholesale power, transmission and water rate tariffs will include, as an element of the cost of service, revenue transfers to community service activities.

The amount available to annually fund service activities will equal a total of 5% of budgeted operational gross revenues of the LCRA transmission activities, accomplished through LCRA Transmission Services Corporation; 5% of budgeted operational gross revenues of Strategic Services; and 5% of budgeted operational gross revenues of raw water activities, with the specific allocation of such funds between PSF and the Resource Development Fund to be established by the Board in the LCRA business plan. Amounts

available to fund service activities through the PSF from LCRA's interruptible water business activities will be 3%.

Wholesale power customers and wholesale power affiliated corporations will fund service activities in accordance with their contracts.

301.602 Flood Recovery and Disaster Fund. LCRA will maintain a Flood Recovery and Disaster Fund (FRD Fund) of up to \$500,000 to aid in the response to a natural flood disaster that causes structural, environmental or navigational damage or creates a hazard to public health and safety along the Highland Lakes and Colorado River within LCRA's 10-county statutory district. LCRA intends the fund to be used to assist cities, counties and local communities in restoring essential services, mitigating public health hazards and ensuring public safety. LCRA expects that LCRA's assistance using this fund will be in support of the affected communities' self-help response to the disaster. Unless otherwise approved by the Board, expenditures from this fund for any single flood event will be limited to \$200,000 and will not extend past the expiration date of a state disaster declaration.

The types of activities that qualify under the FRD Fund are related to public health and safety and may include some or all of the following activities:

- (1) Inspection of septic systems.
- (2) Water quality assessments.
- (3) Emergency repair of water and wastewater treatment plants.
- (4) Removal of major navigational hazards within LCRA lakes and the Colorado River.
- (5) Use of heavy equipment to clear roadways and shorelines of major flood debris.
- (6) Assistance of LCRA personnel in public safety activities.

The following types of activities do not qualify under the FRD Fund:

- (1) The repair or improvement of private property.
- (2) The repair or improvement of LCRA facilities except those facilities that are for public use and enjoyment.

As monies in the FRD Fund are used for eligible expenditures, the Board may approve additional transfers to replenish the fund.

301.603 Agricultural Water Conservation Fund. Section 8503.029, Texas Special District Local Laws Code, requires that a separate charge of at least 10% of LCRA's applicable water rates be applied for any new surface water transfers to the Brazos River watershed in Williamson County. LCRA may use money from this fund only for the development of water resources or other water use strategies to replace or offset the amount of surface water to be transferred to Williamson County. The water development or water use strategies must take into consideration the surface water and groundwater needs of the affected Colorado River basin users and will benefit the

water service areas of LCRA's irrigation operations. The Board may deposit other monies within its discretion in the Agricultural Water Conservation Fund.

The staff will consult, as required by Section 8503.029, with an advisory committee representing agricultural irrigation interests before using money from the Agricultural Water Conservation Fund. The Board must approve all expenditures from the Agricultural Water Conservation Fund, but will not consider using the funds to buy out the production of a second crop.

On or before the April Board meeting of each year, the general manager will submit to the Board a report summarizing activities related to the implementation of Section 8503.029, including management and use of the Agricultural Water Conservation Fund, the sufficiency of the separate charge to implement the requirements of Section 8503.029, and updated projections of anticipated water demands for customers subject to the requirements of Section 8503.029.

301.604 Infrastructure Reserve Fund. LCRA will maintain a fund in which the Board may set aside proceeds from above-budget performance from water, park and strategic services activities. Availability of these funds, if any, will be determined after completion of the annual financial audit. Additionally, PSF monies not identified for a specific purpose during the preparation of the annual business plan also may be set aside in this fund. The Board may use these funds at its discretion for purposes of improving existing or developing new infrastructure or any other lawful purpose. The Board must approve all expenditures from the Infrastructure Reserve Fund. The Infrastructure Reserve Fund is part of the revenue fund and accounted for separately.

301.605 Resource Development Fund. LCRA will maintain a fund to specifically support investment in and payment of debt service on borrowings that have been used to construct long-term capital assets that (i) provide for the development of water supply resources for the Colorado River basin, or (ii) otherwise support LCRA's mission activities. The deposit of monies into this fund will be pursuant to Board action authorizing a one-time transfer of funds or creating a program that creates periodic transfers from sources described in this policy. The Board must approve all expenditures from the Resource Development Fund. The Resource Development Fund is part of the revenue fund and accounted for separately.

301.606 Public Recreation and Conservation Land Acquisition Fund. LCRA has established a Public Recreation and Conservation Land Acquisition Fund (PRCLA Fund) to be used for non-utility land acquisition and/or the development of any project included in LCRA's Public Services or Enterprise Capital Improvement Plan. The PRCLA Fund is part of the revenue fund and accounted for separately.

LCRA intends to maintain a minimum balance in the PRCLA Fund of at least \$1 million. If the PRCLA Fund is drawn down below this level, the Board may direct staff to replenish it with an equal or greater amount from the approved sources within a reasonable time frame. At any time that it is anticipated that an expenditure will draw the balance below

the \$1 million level, the source of funds, the process and the time period for replenishing the PRCLA Fund will be subject to approval by the Board.

The Board must approve all expenditures from the PRCLA Fund. The monies for the PRCLA Fund may come from the following sources:

- Proceeds from the sale of nonessential non-utility lands.
- Loans, grants or gifts allocated to the acquisition of non-utility lands.
- Revenues resulting from LCRA's agreements with the private sector for managing and operating park, recreation and natural science projects.
- Other sources as approved by the Board.

301.607 Community Assistance Fund. A Community Assistance Fund will be established to provide money for LCRA's Community Development Partnership Program (CDPP). The LCRA PSF will be the source of funds for the Community Assistance Fund. The Community Assistance Fund is part of the revenue fund and is accounted for separately.

The CDPP operates as a grants program, and LCRA intends the CDPP to support communities and economic growth by contributing to education, transportation, public safety, recreation, health care, training, community planning or employment efforts in LCRA's service area. Specific program guidelines governing the process, criteria and procedures for disbursements made from the Community Assistance Fund and PSF will be approved by the Board.

301.608 Liability Reduction Fund. LCRA will establish a fund specifically for the reduction of long-term liabilities. The purpose of this fund is to reduce LCRA's long-term cost structure by paying for liabilities when appropriate and funds are available. The Board will approve the source of funds for the Liability Reduction Fund and the disbursements from the Liability Reduction Fund.

The Liability Reduction Fund is part of the revenue fund and accounted for separately. Interest income attributable to the Liability Reduction Fund may be deposited into the fund periodically and no less frequently than once per fiscal year.

301.609 Agriculture Reserve Fund. LCRA will establish a fund specifically to be used for mitigating rate shock to customers. The monies for the Agriculture Reserve Fund may come from any source approved by the Board. The Board must approve all expenditures from the Agriculture Reserve Fund. The Agriculture Reserve Fund is part of the revenue fund and accounted for separately.

301.70 RESPONSIBILITIES

An annual report will be submitted to the Board on the activities of the Flood Recovery and Disaster Fund and the Agricultural Water Conservation Fund. It is the responsibility of the GM/CEO, chief financial officer and the Board to review this policy statement

periodically and make recommendations for necessary revisions to ensure that LCRA maintains a high level of financial integrity.

301.80 AUTHORITY

LCRA enabling legislation, Chapter 8503, Texas Special District Local Laws Code
Texas Water Code, Chapter 152
Public Funds Investment Act, Chapter 2256, Texas Government Code
IRS Treasury Regulations, Section 1.150-2

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