



EAST VALLEY WATER DISTRICT Administrative Policies & Programs

Policy Title: Debt Management Policy

Original Approval Date:
August 10, 2010

Last Revised:
August 26, 2020

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Purpose

The purpose of this Debt Management Policy is to establish guidelines for the issuance and management of District debt, and to provide guidance for decision makers with respect to options available for financing infrastructure, and other capital projects, so that the most prudent, equitable, and cost effective financing can be chosen.

This policy documents the objectives to be achieved by staff both prior to, and subsequent to, issuance of debt, and is designed to promote objectivity in the decision making process, and to facilitate the financing process by establishing important policy decisions in advance.

Goals

It is a goal of the District to provide for the infrastructure and capital project needs of its ratepayers, financing those capital project needs from a combination of current revenues, available reserves, and prudently issued debt.

Debt is an equitable means of financing projects and represents an important means of providing for the infrastructure and project needs of the District's customers. Debt will be used to finance projects if:

- Debt is issued and managed prudently;
- Debt enables the District to maintain a sound fiscal position;
- Issuing the debt will not negatively impact the District's credit rating;
- The District's goal of equitable treatment of all customers, both current and future, would be met;
- It is the most cost-effective means available to the District; and
- It is fiscally responsible under the prevailing economic conditions.



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Budget Integration

Issuance of debt may only be utilized to finance a capital project(s). Debt proceeds are not to be used to fund operating expenses. The decision to incur new indebtedness should be integrated with the Board-adopted annual Operating Budget and Capital Improvement Program (CIP) Budget. Issuance of debt for a capital project will not be considered unless such project has been incorporated into the District's CIP, or is otherwise approved by the Board of Directors (Board).

Annual debt service payments shall be included in the Operating Budget.

Standards for Use of Debt Financing

When appropriate, the District will use long-term debt financing to:

- Achieve an equitable allocation of capital costs / charges between current and future system users
- Provide more manageable rates in the near and medium term
- Minimize rate volatility

For growth-related projects, debt financing will be utilized, as needed, to better match the cost of anticipated facility needs with timing of expected new connections to the system and spread the costs evenly over time. Capacity / Connection Fees will be maintained at a level sufficient to finance a portion of growth-related capital costs and cover related annual debt service requirements.

The District shall not construct or acquire a facility if it is unable to adequately provide for the subsequent annual operation and maintenance costs of the facility throughout its expected life.

Capital projects financed through debt issuance will not be financed for a term longer than the expected useful life of the project.



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Methods of Financing

The Finance Department will investigate all possible project financing alternatives including, but not limited to, annual operating revenue, reserves, bonds, loans, and grants. When applicable, capacity fees collected from developers will be used to pay for increased capital costs resulting from new development.

The District may legally issue both short term and long-term financing using the debt instruments described below.

1. **Cash Funding** - The District funds a significant portion of capital improvements on a pay-as-you-go basis. Sources for pay-as-you-go may include appropriations from annual operating revenue, reserves, and grants.
2. **Inter-fund Borrowing** - The District may borrow internally from other funds with temporarily surplus cash to meet short term needs in lieu of issuing debt. Purposes for such could include short term cash flow imbalances due to grant terms (i.e., the need to incur costs prior to reimbursement) and interim financing pending the issuance of long-term debt. The District funds from which the money is borrowed shall be repaid with interest, accruing quarterly based upon the apportionment rate set by the State of California Local Agency Investment Fund (LAIF). To the extent any inter-fund borrowing is undertaken in anticipation of long-term financing, the District shall adopt a Resolution of its intention to repay such funds out of tax-exempt debt proceeds so as to meet the requirement of federal tax law for such borrowing.
3. **Line of Credit** - The District may consider a line of credit as a short-term borrowing option. The Chief Financial Officer (CFO) shall determine when it is prudent to recommend that the District enter into an agreement with a commercial bank or other financial institution, for the purpose of acquiring a line of letter of credit.
4. **Capital Lease Debt** - A lease purchase obligation placed with a lender without the issuance of securities may be used to finance certain equipment purchases if the aggregate cost of the equipment exceeds \$50,000 and the terms of financing are cost-effective. The term of a capital lease must be at least five years, and shall not exceed the useful life of the equipment or ten years, whichever is shorter.



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5. **State Revolving Fund Loans** - The State Revolving Fund (SRF) is a low or zero interest loan program generally for the construction of water and wastewater infrastructure projects. The SRF loan interest rate is typically calculated by taking half of the True Interest Cost (TIC) of the most recent State of California General Obligation Bonds sale. The repayment term of the loans ranges from 20 to 30 years.
6. **Certificates of Participation** - The District may issue Certificates of Participation (COP) which provide financing through a lease, installment sale agreement, or contract of indebtedness and typically do not require voter approval. Board action is legally sufficient to authorize a COP issue, and District revenues are pledged for repayment of COPs under terms specified in the indenture.
7. **JPA Revenue Bonds** - The District may obtain financing through the issuance of debt under a joint exercise of powers agreement (East Valley Water District Financing Authority) with such debt payable from amounts paid by the District under a lease, installment sale agreement, or contract of indebtedness.
8. **Refunding Revenue Bonds** - The District may issue refunding revenue bonds to refund District indebtedness pursuant to the State of California local agency refunding revenue bond law (Title 5 of the California Government Code)

Financing Team - Roles and Responsibilities

The primary responsibility for developing debt financing recommendations rests with the CFO. In developing such recommendations, the CFO shall consider the need for debt financing and assess progress on the current capital improvement program (CIP). The CFO will present all proposed debt financings to the Board, which has sole authority to approve the issuance of debt.

1. **Bond Counsel** - The District will retain external bond counsel for all debt issues. Bond counsel will prepare the necessary authorizing resolutions, agreements and other documents necessary to execute the financing. All debt issued by the District will include a written opinion by bond counsel affirming that the District is authorized to issue the debt, stating that the District has met all state constitutional and statutory requirements necessary for issuance, and determining the debt's federal income tax status.



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- 2. Financial Advisors** - The District will utilize the services of independent financial advisors when deemed prudent by the CFO. Services and compensation caps shall be defined by contract. The primary responsibilities of the financial advisor are to advise and assist on bond document negotiations, transaction structuring including advising on call provision options and timing of issuance, running debt service cash flow analysis, assistance in obtaining ratings on the proposed issuance, and generally acting as an independent financial consultant and economic market expert.
- 3. Underwriters** - For negotiated sales, the District will generally select or pre-qualify underwriters through a competitive process. This process may include a request for proposal or qualifications to firms considered appropriate for the underwriting of a particular issue or type of bonds. The Chief Financial Officer, with the concurrence of the General Manager/CEO, will determine the appropriate method to evaluate the underwriter submittals and then select or qualify firms on that basis. The District will not be bound by the terms and conditions of any underwriting agreements; oral or written, to which it was not a party.

Structure and Term

- 1. Term of Debt** - Debt will be structured for the shortest period possible, consistent with a fair allocation of costs to current and future users. The standard term of long-term debt borrowing is 10 to 30 years. Consistent with its philosophy of keeping capital facilities and infrastructure systems in good condition and maximizing a capital assets useful life, the District will budget to set aside operating revenue to finance ongoing maintenance and to provide reserves for rehabilitation and replacement. No debt will be issued for periods exceeding the useful life of projects to be financed.
- 2. Debt Repayment** - In structuring a bond issue, the District will manage the amortization of the debt and, to the extent possible, match its cash flow to the anticipated debt service payments. In addition, the District will seek to structure debt with aggregate level debt service payment over the life of the debt.

A non-level debt service structure will be considered if it is beneficial to the District's overall debt payment schedule, or if such structuring will allow debt service to more closely match project revenues during the early years of a project's operation.



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3. **Interest Rate Structure** - The District currently issues long-term debt on a fixed interest rate basis only. Fixed rate securities ensure budget certainty through the life of the issue and avoid the volatility of variable rates.
4. **Credit Enhancement** - The District will consider the use of credit enhancement on a case-by-case basis. Types of credit enhancement include letters of credit, bond insurance, and surety policies. Only when clearly demonstrable savings can be realized shall credit enhancement be utilized.
5. **Debt Service Reserve Funds** - Debt service reserve funds are held by the Trustee to make principal and interest payments to bondholders in the event that pledged revenues are insufficient to do so. The District will fund debt service reserve funds when it is in the District's overall best financial interest.

In lieu of holding a cash funded reserve, the District may substitute a surety bond or other credit instrument in its place. Additionally, the District may decide not to utilize a reserve fund if the District's financing team determines there would be no adverse impact to the District credit rating or interest rates.

6. **Call Provisions** - In general, the District's securities should include optional call provisions. The District will avoid the sale of non-callable, long-term fixed rate bonds, absent careful evaluation of the value of the call option.
7. **Debt Limits** - There is no specific provision within the California Government Code that limits the amount of debt that may be issued by the District. The District's borrowing capability is limited by the additional bonds test and debt coverage ratio required by the existing bond covenants. The District will be mindful of its overall debt burden in the context of its revenues, expenses, reserves, and overall financial health.
8. **Refunding** - Current and advance refunding are important debt management tools for the District. They are commonly used to achieve debt service (interest cost) savings, remove or change bond covenants, or restructure debt service obligations. With consideration of the Federal Tax Law, careful planning and timing must be used when reviewing an advance refunding.

To the extent that debt having fixed interest rates originally structured with a long-term amortization structure (ten years or greater) is refunded with fixed rate debt,



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the District will not generally issue refunding debt which extends beyond the final maturity of the refinanced debt. Extending the final maturity may occur when warranted, such as restructuring of debt to match debt amortization with the useful life of the financed assets.

Method of Issuance and Sale

The District will select the method of sale, which best fits the type of bonds being sold, market conditions, and the desire to structure bond maturities to enhance the overall performance of the entire debt portfolio. Three general methods exist for the sale of municipal bonds:

1. **Competitive Sale** - Bonds will be marketed to a wide audience of investment banking (underwriting) firms. The underwriter is selected based on its best bid for its securities. The District will award the sale of the competitively sold bonds on a true interest cost (TIC) basis. Pursuant to this policy, the General Manager/CEO, is hereby authorized to sign the bid form on behalf of the District, fixing the interest rates on bonds sold on a competitive basis.
2. **Negotiated Sale** - In a negotiated sale, the underwriter or underwriting syndicate is selected through a Request for Proposal (RFP) process. The interest rate and the underwriter's fee are negotiated prior to the sale, based on market conditions. The underwriter will actively assist the District in structuring the financing and marketing of bonds including providing assistance in preparing the bond offering circular.
3. **Private Placement** - The District may elect to issue debt on a private placement basis. Such method may be considered if it is demonstrated to result in cost savings or provide other advantages relative to other methods of debt issuance, or if it is determined that access to the public market is unavailable and timing considerations require that financing be completed.

Creditworthiness Objectives

Ratings are a reflection of the fiscal soundness of the District and the capabilities of its management. Typically, the higher the credit ratings are, the lower the interest cost on the District's debt issues. To enhance creditworthiness, the District is committed to



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prudent financial management, systematic capital planning, and long-term financial planning. The District recognizes that external economic, natural, and other events may affect the creditworthiness of its debt.

The District's most recent bond issues have been assessed by the nationally recognized rating agencies Standard and Poor's, and Fitch Ratings. When issuing a credit rating, rating agencies consider various factors including but not limited to:

- District's fiscal status
- District management capabilities
- Economic conditions that may impact the stability and reliability of debt repayment sources
- District reserve levels
- District debt history and current debt structure
- Projects being financed

Post Issuance Administration / Internal Control

1. **Investment of Proceeds** - The proceeds of bond sales will be invested until used for the intended project(s) in order to maximize utilization of the public funds. The investments will be made to obtain the highest level of 1) safety, 2) liquidity, and 3) yield, and may be held as cash. The District's investment guidelines and bond indentures will govern objectives and criteria for investment of bond proceeds. The Finance Department will oversee the investment of bond proceeds in a manner to avoid, if possible, and minimize any potential negative arbitrage over the life of the bond issuance, while complying with arbitrage and tax provisions.
2. **Use of Proceeds** - Bond proceeds will be deposited and recorded in separate accounts to ensure funds are not comingled with other District funds. The District's Trustee will administer the disbursement of bond proceeds pursuant to each certain Indenture of Trust or Fiscal Agent Agreement, respectively. To ensure proceeds from bond sales are used in accordance with legal and tax requirements, invoices are submitted by the Engineering Department and approved by the Finance Department



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and General Manager/CEO for payment. Requisition for the disbursement of bond funds will be approved by the District's CFO.

The Finance Department will be tasked with monitoring the expenditure of bond proceeds to ensure they are used only for the purpose and authority for which the bonds were issued and exercising best efforts to spend bond proceeds in such a manner that the District will meet one of the spend-down exemptions from arbitrage rebate. Tax-exempt bonds will not be issued unless it can be demonstrated that 85% of the proceeds can reasonably be expected to be expended within the three-year temporary period.

3. **Arbitrage Compliance** - The use of bond proceeds and their investments must be monitored to ensure compliance with all Internal Revenue Code Arbitrage Rebate Requirements. The CFO shall ensure that all bond proceeds and investments are tracked in a manner which facilitates accurate calculation; and, if a rebate payment is due, such payment is made in a timely manner.
4. **Compliance with Bond Covenants** - The District is responsible for verifying compliance with all undertakings, covenants, and agreements of each debt issue on an ongoing basis. This typically includes ensuring:
 - Annual appropriations of revenues to meet debt service payments
 - Timely transfer of debt service payments to the Trustee
 - Compliance with insurance requirements
 - Compliance with rate covenants

The District shall comply with all covenants and conditions contained in the governing law and any legal documents entered into at the time of the bond offering or signing of agreements. The CFO or designee will coordinate verification and monitoring of covenant compliance.

5. **Rating Agency Communication** - The CFO shall be responsible for maintaining the District's relationships with S&P Global Ratings, Fitch Ratings and/or Moody's Investment Service. In addition to general communication, the CFO shall meet with



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credit analysts prior to each competitive sale and offer conference calls with the District financing team in connection with the planned sale.

6. **Board Communication** - The CFO will report to the Board of Directors any feedback from rating agencies and/or investors regarding the District's financial strengths and weaknesses and recommendations for addressing any weaknesses.
7. **Continuing Disclosure** - The District shall remain in compliance with Rule 15c2-12 by filing its annual financial statements and other financial and operating data for the benefit of its bondholders by December 31st of each year. The CFO will ensure the District's timely filing with each Nationally Recognized Municipal Securities Information Repository.

The CFO and/or the District's general counsel, with the assistance of Bond Counsel, will provide written notice to the Board of any receipt by the District of any default, event of acceleration, termination event, modification of terms (only if material or may reflect financial difficulties), or other similar events (collectively, a "Potentially Reportable Event") under any agreement or obligation to which the District is a party and which may be a "financial obligation" as discussed below. Such written notice should be provided by the CFO and/or the District's general counsel to the Board as soon as the CFO is placed on written notice by District staff, consultants, or external parties of such event or receives written notice of such event. The CFO, with the assistance of bond and disclosure counsel, will determine and notify the Board whether notice of such Potentially Reportable Event is required to be filed on EMMA pursuant to the disclosure requirements of SEC Rule 15c2-12 (the "Rule"). If filing on EMMA is required, the filing is due within 10 business days of such Potentially Reportable Event to comply with the continuing disclosure undertaking for the various debt obligations of the District.

The CFO and/or the District's general counsel, with the assistance of Bond Counsel, will report to the Board regarding the execution by the District of any agreement or other obligation which might constitute a "financial obligation" for purposes of Rule 15c2-12. Amendments to existing District agreements or obligations with "financial obligation" which relate to covenants, events of default, remedies, priority rights, or other similar terms should be reported to the Board as well as soon as the CFO is placed on written notice by District staff, consultants, or external parties of such event or receives a written notice of such amendment requests. The CFO will



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determine, with the assistance of bond and disclosure counsel, whether such agreement or other obligation constitutes a material “financial obligation” for purposes of Rule 15c2-12. If such agreement or other obligation is determined to be a material “financial obligation” or a material amendment to a “financial obligation” described above, notice thereof would be required to be filed on EMMA within 10 business days of execution or incurrence. The types of agreements or other obligations which could constitute “financial obligations” and which could need to be reported on EMMA include:

1. Bank loans or other obligations which are privately placed;
2. State or federal loans;
3. Commercial paper or other short-term indebtedness for which no offering document has been filed on EMMA;
4. Letters of credit, surety policies or other credit enhancement with respect to the District’s publicly offered Debt;
5. Letters of credit, including letters of credit which are provided to third parties to secure the District’s obligation to pay or perform (an example of this is a standby letter of credit delivered to secure the District’s obligations for performance under a mitigation agreement);
6. Capital leases for property, facilities, fleet or equipment; and
7. Agreements which guarantee the payment or performance obligations of a third party (regardless of whether the agreements constitute guarantees under California law);
8. License agreements.

Types of agreements which could be a “financial obligation” under the Rule include:

1. Payment agreements which obligate the District to pay a share of another public agency’s debt service (for example, an agreement with a joint powers agency whereby the District agrees to pay a share of the joint powers agency’s bonds, notes or other obligations); and



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2. Service contracts with a public agency or a private party pursuant to which the District is obligated to pay a share of such public agency or private party's debt service obligation (for example, certain types of P3 arrangements).

Types of agreements which may be a "financial obligation" subject to the Rule include:

- Any agreement the payments under which are not characterized as an operation and maintenance expenses for accounting purposes if such agreement could be characterized as the borrowing of money.

The CFO will continue to work with bond and disclosure counsel to refine the definition of financial obligation going forward based on future SEC guidance.

8. **Record Retention** - A copy of all debt-related records shall be retained at the District's offices. At minimum, these records shall include all official statements, bid documents, bond documents / transcripts, resolutions, trustee statements, leases, and title reports for each District financing (to the extent available). Electronic copies - preferably in pdf or CD-ROM format - shall also be retained.
9. **State Reporting Requirements** - Pursuant to Government Code section 8855(k), the District will submit annual debt transparency reports for any debt for which it has submitted a report of final sale on or after January 21, 2017 every year until the later date on which the debt is no longer outstanding and the proceeds have been fully spent.

The District shall also comply with Government Code Section 5852.1 by disclosing specified good faith estimates in a public meeting prior to the authorization of the issuance of debt.

Board Discretion

This policy was drafted with the intent of providing East Valley Water District's Board-approved guidelines to management and staff for decisions and recommendations related to capital financing by the District, and to support the District's debt obligations to present and future generations of ratepayers.



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This policy is ultimately intended to serve as a guide and it in no way restricts the ability of the East Valley Water District Board to review proposed rate actions, debt issuances, or other actions of substance to the District. The Board maintains authorization to waive elements of the policy in connection with individual financings at its discretion. This policy shall be reviewed during the third quarter of each odd fiscal year.

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