

POLICY NO. 1.5 Debt Management Policy	DISTRICT CODE Chapter 3.11 Sections 3.11.010 – 3.11.130	APPROVAL DATE 03/23/2021 EFFECTIVE DATE 03/24/2021
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SECTION 1: POLICY STATEMENT (3.11.010)

This policy documents the goals of the Cucamonga Valley Water District (“District”) for the use of debt instruments and provides guidelines for the use of debt for financing District water, sewer and recycled water infrastructure and project needs. The District’s overriding goal in issuing debt is to respond to and provide for its infrastructure, capital project and other financing needs while ensuring that debt is issued and managed prudently in order to maintain a sound fiscal position and protect credit quality. The District issues debt instruments, administers District held debt proceeds and makes debt service payments, acting with prudence, diligence and attention to prevailing economic conditions.

The District will pay for all infrastructure, projects, and other financing needs from a combination of current revenues, available reserves, if any, and prudently issued debt. The District believes that debt can provide an equitable means of financing projects for its customers and provide access to new capital needed for infrastructure and project needs. Debt will be used to meet financing needs (i) if it meets the goals of equitable treatment of all customers, both current and future; (ii) if it is the most cost-effective means available; (iii) if it is fiscally prudent, responsible, and diligent under the prevailing economic conditions; and (iv) if there are other important policy reasons. The District will not issue debt without the approval of the Board of Directors (“Board”).

SECTION 2: PURPOSE AND USE OF DEBT (3.11.020)

The District will utilize reasonable debt financing as an acceptable and appropriate approach to fund long-term improvements and thus ensure that existing and future users pay their fair share. Long-term improvements include the acquisition of land, facilities, infrastructure, and supplies of water; and enhancements or enlargements to existing capacity and facilities for obtaining,

importing, transporting and delivering additional quantities of water. These improvements are typically included in the District's Capital Improvement Budget and Water Master Plan. Bond proceeds can be issued to fund the planning, design, land acquisition, construction, attached fixtures or equipment and moveable pieces of equipment, or other costs as permitted by law.

SECTION 3: PURPOSE OF POLICY (3.11.030)

The purpose of this debt management policy is to:

- A. Establish parameters for issuing debt
- B. Provide guidance to decision makers:
 - a. With respect to all options available to finance infrastructure, capital projects, and other financing needs
 - b. So that the most prudent, equitable and cost effective method of financing can be chosen
 - c. Document the objectives to be achieved both prior to issuance and subsequent to issuance
 - d. Promote objectivity in the decision-making process
 - e. Facilitate the financing process by establishing important policy decisions in advance

The District will adhere to the following legal requirements for the issuance of public debt:

- A. The state law which authorizes the issuance of the debt
- B. The federal and state laws which govern the eligibility of the debt for tax-exempt status
- C. The federal and state laws which govern the issuance of taxable debt
- D. The federal and state laws which govern disclosure, sale, and trading of the debt both before and subsequent to issuance

SECTION 4: TYPES OF DEBT (3.11.040)

Revenue Bonds, Notes, Certificates of Participation, special tax or special assessment bonds, capital leases, commercial paper, bank loans or government-sponsored loans, direct placements and lease-purchase financings will be treated as debt and subject to these same policies. There may be special circumstances where other forms of financing are appropriately utilized by the District. The District will evaluate such proposed transactions on a case-by-case basis. Such other forms include, but are not limited to, grant anticipation notes and judgment or settlement obligations bonds.

SECTION 5: GENERAL PROVISIONS (3.11.050)

The District will provide for a periodic review of its financial performance and review its performance relative to the financial policies outlined herein. These financial policies will be taken into account during the capital planning, budgeting, and rate setting processes. Necessary

appropriations for annual debt service requirements will be routinely included in the District's annual budget. The District will maintain proactive communication with the investment community, including rating agencies, credit enhancers and investors, to ensure future capital market access at the lowest possible interest rates.

The District's Debt Management Policy No. 1.5, the Reserve and Financial Benchmark Policy No. 1.3, and the Investment Policy No. 1.4 are integrated into the decision-making framework utilized in the budgeting and capital improvement planning process. As such, the following principles outline the District's approach to debt management:

- A. The District will issue debt only in the case where there is an identified source of repayment. Debt will be issued to the extent that (i) projected existing revenues are sufficient to pay for the proposed debt service together with all existing debt service covered by such existing revenues, or (ii) additional projected revenues have been identified as a source of repayment in an amount sufficient to pay for the proposed debt.
- B. The District will not issue debt to cover operating needs, unless specifically approved by the Board.
- C. Debt issuance for a capital project will not be considered unless such project has been incorporated into the District's adopted Capital Improvement Budget or as otherwise approved by the Board.
- D. Each proposal to issue debt will be accompanied by an analysis that demonstrates conformity to this Policy. This analysis will address the purpose for which the debt is issued and the proposed debt structure.

SECTION 6: CONDITIONS FOR DEBT ISSUANCE (3.11.060)

The following guidelines formally establish parameters for evaluating, issuing, and managing the District's debt. The guidelines outlined below are not intended to serve as a list of rules to be applied to the District's debt issuance process, but rather to serve as a set of practices to promote prudent financial management.

In issuing debt, the District's objectives will be to:

- A. Achieve the lowest cost of capital
- B. Ensure ratepayer equity
- C. Maintain the adopted credit rating strategy, or a more effective credit rating strategy, and access to credit enhancement
- D. Preserve financial flexibility

SECTION 7: STANDARDS FOR USE OF DEBT FINANCING (3.11.070)

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, to provide more manageable rates in the near and medium term and to minimize rate volatility. 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.

SECTION 8: DEBT CAPACITY (3.11.080)

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 future borrowing capability is limited by the debt coverage ratio and additional debt limitations required by the existing bond covenants.

SECTION 9: FINANCING CRITERIA (3.11.090)

- A. Each debt issuance should be evaluated on an individual basis within the context of the District's overall financing objectives and current market conditions. The District will evaluate alternative debt structures (and timing considerations) to ensure the most cost-efficient financing under prevailing market conditions.
- a. Credit Enhancement – The District will consider the use of credit enhancement on a case-by-case basis. Only when clearly demonstrable savings can be realized shall credit enhancement be utilized.
 - b. Cash-Funded Reserve vs. Surety – If the issuance of debt requires a cash-funded debt service reserve fund, the District may purchase a surety policy or replace an existing cash-funded debt service reserve fund when deemed prudent and advantageous. The District may permit the use of guaranteed investment agreements for the investment of reserve funds pledged to the repayment of any of its debt when it is approved by the Board.
 - c. 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.
 - d. Additional Bonds Test/Rate Covenants – The amount and timing of debt will be planned to comply with the additional bonds tests and rate covenants outlined in the appropriate legal and financing documents, and this policy.
 - e. Short-Term Debt – The District may utilize short-term borrowing to serve as a bridge for anticipated revenues, construction financing or future bonding capacity.
 - f. Variable Rate Debt – Variable rate debt products are rolling series of short-term investments that are resold periodically and are therefore priced at the short-end of the yield curve at low interest rates. If an issuer accepts the risks inherent in variable

interest rates, the issuer can take advantage of some of the lowest rates available on the market. Variable rate debt may be appropriate for the District's portfolio, especially in an environment where increased interest earnings on invested funds offset the increased cost of variable rate debt. Variable rate debt products include variable rate demand obligations, commercial paper, and auction rate securities. The District may consider the use of variable rate debt products to achieve a lower cost of borrowing or for short-term borrowing. In determining whether or not to use variable rate debt, the District will analyze the risks associated with the variable rate debt products, including derivative products.

- g. Use of Variable Rate Debt – The District may consider the use of variable rate debt products to achieve a lower cost of borrowing or for short-term borrowing. In determining whether or not to use variable rate debt, the District will analyze, among other things, the risk associated with the variable rate debt and the impact on the District's overall portfolio. Before issuing variable rate debt, the District will analyze its cash position; the District will not issue variable rate debt in an amount that exceeds 30% of its outstanding debt obligations at the time of issuance of any variable rate debt.
- h. Investment of Bond Proceeds - Bond proceeds will be invested in accordance with the permitted investment language outlined in the bond documents for each transaction. The District will seek to maximize investment earnings within the investment parameters set forth in the respective debt financing documentation. The reinvestment of bond proceeds will be incorporated into the evaluation of each financing decision; specifically addressing arbitrage/rebate position, and evaluating alternative debt structures and refunding savings on a "net" debt service basis, where appropriate.

SECTION 10: REFINANCING OUTSTANDING DEBT (3.11.100)

The Director of Finance and Technology Services (Director of Finance) shall have the responsibility to evaluate potential refunding opportunities. The District will consider the following issues when analyzing potential refunding opportunities:

- A. Debt Service Savings – The District shall establish a target savings level greater or equal to 3% of the par of debt refunded on a net present value (NPV) basis (after payment of all costs associated with the issuance) for a current refunding and 5% for advanced refunding transactions. These targets will serve only as a guideline and the District may determine that a different savings target is appropriate; the District shall evaluate each refunding opportunity on a case-by-case basis. In addition to the savings guideline, the following shall be taken into consideration:
 - a. Remaining time to maturity
 - b. Size of the issue
 - c. Current interest rate environment
 - d. Annual cash flow savings
 - e. The value of the call option
 - f. Revision of restrictive or onerous covenants

- g. Other factors approved by the Board of Directors and recommended by the Director of Finance.

- B. Restructuring – The District may seek to refinance a bond issue on a non-economic basis, in order to restructure debt, to mitigate irregular debt service payments, accommodate revenue shortfalls, to achieve a proper matching of debt service with revenues, release reserve funds, or comply with and/or eliminate rate/bond covenants.

- C. Term/Final Maturity – The District may consider the extension of the final maturity of the refunding bonds in order to achieve a necessary outcome, provided that such extension is legal. The term of the debt should not extend beyond the reasonably expected useful life of the asset being financed. The District may also consider shortening the final maturity of the bonds. The remaining useful life of the assets and the concept of inter-generational equity will guide these decisions.

- D. Defeasance – Defeasance is when a debt financing is refinanced or paid off through an escrow where certain authorized investments and cash are deposited to pay the redemption price, principal and interest until such time the debt is fully redeemed. On the date when proceeds are deposited into the escrow, the debt will no longer be deemed outstanding and is defeased.

There are two types of defeasances: legal and economic. A legal defeasance ends all of the rights and interest of the debt holders provided under the governing documents, including the pledge of revenues or other security interest. An economic defeasance does not end the rights and interest of the debt holders until such debt is fully redeemed.

When evaluating an economic versus legal defeasance, the District shall take into consideration both the financial impact on a net present value basis as well as the rating/credit impact. The District shall take all necessary steps to optimize the yield on its refunding escrows investments and avoid negative arbitrage.

SECTION 11: OUTSTANDING DEBT LIMITATIONS (3.11.110)

Prior to issuance of new debt, the District shall consider and review the latest credit rating reports and guidelines to ensure the District’s credit ratings and financial flexibility remain at levels consistent with the most highly rated comparable public agencies.

SECTION 12: METHOD OF ISSUANCE (3.11.120)

The District will determine, on a case-by-case basis, whether to sell its bonds competitively or through negotiation.

- A. Competitive Sale – In a competitive sale, the District’s debt shall be awarded to the bidder providing the lowest true interest cost (“TIC”), as long as the bid adheres to the requirements set forth in the official notice of sale.

- B. Negotiated Sale – The District recognizes that some bond issues are best sold through negotiation with a selected underwriter or team of underwriters. The District has identified the following circumstances below in which this would likely be the case:
- a. Issuance of variable rate or taxable bonds
 - b. Complex structures or credit considerations (such as non-rated bonds), which require a strong pre-marketing effort. Significant par value, which may limit the number of potential bidders, unique/proprietary financing mechanism (such as a financing pool), or specialized knowledge of financing mechanism or process
 - c. Market volatility, such that the District would be better served by flexibility in the timing of its sale, such as in the case of a refunding issue wherein the savings target is sensitive to interest rate fluctuations, or in a changing interest rate environment
 - d. When an underwriter has identified new financing opportunities or presented alternative structures that financially benefit the District
 - e. As a result of an underwriter’s familiarity with the project/financing, that enables the District to take advantage of efficiency and timing considerations
- C. Private Placement – From time to time the District may elect to issue debt on a private placement basis. Such method shall 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 a financing be completed.

SECTION 13: MARKET COMMUNICATION, DEBT ADMINISTRATION AND REPORTING REQUIREMENTS (3.11.130)

- A. Responsibilities – For purposes of this policy the General Manager/CEO delegates responsibility to the Director of Finance or his/her successor in position and in responsibility.
- B. Rating Agencies – The Director of Finance shall be responsible for maintaining the District’s relationships with Standard & Poor’s Ratings Services, Fitch Ratings, and Moody’s Investors Service, as appropriate. The District shall, from time to time, deal with one, two or all of these agencies as circumstances dictate. In addition to general communication, the Director of Finance shall (1) strive to meet, (either in person or via phone) with credit analysts at least annually, as appropriate, and (2) prior to each competitive or negotiated sale, offer conference calls or meeting(s) with rating analysts in connection with the planned sale.
- C. Observance of Debt Covenants – The Director of Finance will periodically ensure that the District is in compliance with all legal covenants for each debt issue.
- D. Continuing Disclosure – The Director of Finance will comply for all debt issued with Rule 15c2-12(b)(5) by (the “Rule”) required filing as covenanted in each debt issue’s Continuing

Disclosure Agreement. The Director of Finance will maintain a calendar with the reporting deadlines and procedures for dissemination of annual reports and notices.

- E. The Director of Finance 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 soon as the Director of Finance 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 Director of Finance will 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 the Electronic Municipal Market Access "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:

- a) Bank loans or other obligations which are privately placed;
- b) State or federal loans;
- c) Commercial paper or other short-term indebtedness for which no offering document has been filed on EMMA;
- d) Letters of credit, surety policies or other credit enhancement with respect to the District's publicly offered debt;
- e) Letters of credit, including letters of credit which are provided to third parties to secure the District's obligation to pay or perform;
- f) Capital leases for property, facilities, fleet or equipment; and
- g) Agreements which guarantee the payment or performance obligations of a third party (regardless of whether the agreements constitute guarantees under California law);
- h) License agreements.

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

- a) 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
- b) 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

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

- a) 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 Director of Finance will continue to work with bond and disclosure counsel to refine the definition of financial obligation going forward based on future SEC guidance.

- F. Record Keeping – A copy of all debt-related records shall be retained at the District’s offices or in an approved storage facility. At minimum, these records shall include all official statements, bid documents, bond documents/transcripts, resolutions, trustee statements, leases, and title reports for each financing (to the extent available). To the extent possible, the District shall retain an electronic copy of each document, preferably in PDF or CD-ROM format.
- G. Arbitrage Rebate – The District will comply with the administratively adopted policies and procedures regarding tax-exempt financings and tax-exempt financed property, as well as the tax and arbitrage certifications associated with each issue.
- H. Internal Controls for Use of Proceeds – To ensure that the proceeds of debt issuances are used in accordance with the intended uses, staff will perform annual procedures as outlined in the District’s Post-Issuance Compliance Manual.
- I. California Debt and Investment Advisory Commission (CDIAC) Filings – The District will comply with required CDIAC rules and regulations and applicable filings including, but not limited to, the Annual Debt Transparency Report and the Marks-Roos Yearly Fiscal Status Report. 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.
- J. Policy Review – This policy should be reviewed on a biennial basis by the Finance Committee and adopted by the Board.

POLICY REVISION DATES

3/23/2021 (Resolution No. 2021-3-10)
12/08/2020 (Resolution No. 2020-12-2)
08/28/2018 (Resolution No. 2018-8-3)
10/25/2016 (Resolution No. 2016-10-3)
08/28/2012 Adoption of New Policy