

RESOLUTION NO. 1443

**RESOLUTION OF THE
MESA WATER DISTRICT BOARD OF DIRECTORS
ADOPTING A DESIGNATED FUNDS POLICY**

WHEREAS, the Mesa Water District (Mesa Water) is a county water district organized and operating according to California Law; and

WHEREAS, the Board of Directors (Board) of the Mesa Water District had previously adopted Resolution No. 1387 which included designated funds; the Board desires to adopt a specific policy statement and policy regarding designated funds relative to Mesa Water's finances.

NOW THEREFORE, THE BOARD OF DIRECTORS OF THE MESA WATER DISTRICT DOES HEREBY RESOLVE, DETERMINE AND ORDER AS FOLLOWS:


Section 1. This Resolution replaces the designated funds portion(s) of Resolution No. 1387 Financial Policies and Guidelines for Establishing Rates and adopts a specific policy statement regarding designated funds as set forth in Exhibit A.

Section 2. This Resolution shall be reviewed by the Finance Committee at least once every five years to determine if the policies and guidelines are still relevant and appropriate.

Section 3. The Designated Funds Policy of the Mesa Water District Board of Directors, as set forth in Attachment A is adopted effective upon approval of this resolution.

PASSED AND ADOPTED this 15th day of March 2014, and adopted by the following roll call vote:

AYES: DIRECTORS: Atkinson, Bockmiller, Temianka, Dewane, Fisler
NOES: DIRECTORS:
ABSENT: DIRECTORS:
ABSTAIN: DIRECTORS:



Coleen L. Monteleone
District Secretary



James R. Fisler
President, Board of Directors

EXHIBIT A

RESOLUTION NO. 1443

RESOLUTION OF THE MESA WATER DISTRICT BOARD OF DIRECTORS ADOPTING A DESIGNATED FUNDS POLICY

1. MESA WATER SHOULD CONTINUE TO MAINTAIN FINANCIAL STABILITY OVER TIME

Mesa Water should strive to maintain financial stability over time. Financial stability is not only a prudent management goal; it can also minimize financial costs in the long-term (e.g., unnecessary borrowing). Above all, financial stability will provide the community with the confidence of knowing a strong, consistent team is managing the utility.

Financial policies and measures will be developed to measure, manage and achieve financial stability.

1.1 DESIGNATED FUNDS

A key element of prudent financial planning is to ensure that sufficient funding is available for current operating, capital, and debt service needs. Additionally, fiscal responsibility requires anticipating the likelihood of, and preparing for, unforeseen events. Mesa Water will at all times strive to have sufficient funding available to meet its operating, capital, and debt service obligations. Designated Funds (Funds) will be accumulated and maintained to allow Mesa Water to fund expenditures in a manner consistent with Mesa Water's Water System Master Plan, and avoid significant rate fluctuations due to changes in cash flow requirements.

The Board of Directors (Board) may designate specific fund accounts and maintain target fund balances consistent with statutory obligations that it has determined to be in the best interest of Mesa Water. The Designated Funds Policy directives are intended to ensure Mesa Water has sufficient Funds to meet current and future needs. The Board will review the level of Funds on a periodic basis.

1.2 DESIGNATED FUNDS TARGET

1.2.1 Mesa Water will maintain sufficient reserves, and of such a nature, that it strives to target designated fund balances totaling 600 days of budgeted operating expenses as defined by the policy.

1.3 CASH FLOW

1.3.1 At the end of a fiscal year, Mesa Water should strive to have total revenues, less operation and maintenance expenses, debt service and capital projects funded from rates, greater than or equal to zero.

1.4 TARGET DEBT SERVICE COVERAGE:

- 1.4.1 Mesa Water will strive to maintain an actual debt service coverage ratio of 1.30 on all outstanding debt service. (Industry norm for revenue bond coverage ratio covenants is 1.25. Mesa Water's certificates of participation covenant coverage ratios of 1.15).
- 1.4.2 The debt service coverage ratio will be calculated at fiscal year-end and reviewed by the outside auditor. The calculation and the auditor's opinion will be included in Mesa Water's Comprehensive Annual Financial Report.
- 1.4.3 Mesa Water's annual budget will be prepared to have an annual debt service coverage ratio greater than or equal to 1.50 on all outstanding debt that carries a legal bond covenant.
- 1.4.4 The Board will review Mesa Water's projected debt service coverage ratio prior to the adoption of the annual budget.

ATTACHMENT A

RESOLUTION NO. 1443

**RESOLUTION OF THE
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ADOPTING A DESIGNATED FUNDS POLICY**

**Mesa Water District's
Designated Funds Policy**

March 2014



MesaWater
DISTRICT

DESIGNATED FUNDS POLICY

March 2014

MESA WATER DISTRICT DESIGNATED FUNDS POLICY

1. **Policy Statement**

A key element of prudent financial planning is to ensure that sufficient funding is available for current operating, capital, and debt service needs. Additionally, fiscal responsibility requires anticipating the likelihood of, and preparing for, unforeseen events. Mesa Water District (Mesa Water) will at all times strive to have sufficient funding available to meet its operating, capital, and debt service obligations. Designated Funds (Funds) will be accumulated and maintained to allow Mesa Water to fund expenditures in a manner consistent with Mesa Water's Water System Master Plan, and avoid significant rate fluctuations due to changes in cash flow requirements.

The Board of Directors (Board) may designate specific fund accounts and maintain target fund balances consistent with statutory obligations that it has determined to be in the best interest of Mesa Water. The Policy directives outlined in this document are intended to ensure Mesa Water has sufficient funds to meet current and future needs. The Board will review the level of Funds on a periodic basis.

2. **Definitions**

There are three types of Funds:

- I. **RESTRICTED FUNDS:** Restrictions on the use of these funds are imposed by an outside source such as creditors, grantors, contributors, laws, or regulations governing use.
- II. **CAPITAL FUNDS:** Established by action of the Board and designated for specific purposes. This fund is utilized primarily to fund capital and asset replacement costs.
- III. **LIQUIDITY FUNDS:** Established by action of the Board to safeguard the financial viability and stability of Mesa Water and is funded from accumulated revenues.

3. **General Provisions**

Mesa Water will maintain its liquidity and capital funds in designated sub-accounts in a manner that ensures its financial soundness and provides transparency to its customers. The targeted level of Fund balances are considered the minimum necessary to maintain the District's credit worthiness and adequately provide for:

- Compliance with applicable statutory requirements
- Financing of future capital facilities and repair and replacement of existing assets
- Cash flow requirements
- Economic uncertainties, local disasters, and other financial hardships or downturns in the local or national economy
- Contingencies or unforeseen operating or capital needs

In the context of funding future capital facilities and maintaining and replacing existing assets, in each instance, Mesa Water will analyze the benefits and tradeoffs of utilizing pay-as-you-go and/or debt financing and determine the optimal funding strategy or combination of funding strategies. The analysis should consider Mesa Water's current and projected liquidity and capital positions, as well as the impact of inflation, the cost of water, and other factors on the operations of Mesa Water and its capital improvement program.

Through a variety of policy documents and plans, including Mesa Water's Asset Management Plan, Capital Improvement Plan, Water System Master Plan, and Strategic Plan, the Board has set forth a number of long-term goals for Mesa Water. A fundamental purpose of Mesa Water's policy documents and plans is to link what must be accomplished with the necessary resources to successfully do so.

Mesa Water has established and will maintain the following primary Funds and their respective sub-accounts:

- Restricted Funds – comprised of the Bond Proceeds Fund and the Customer and Development Deposits
- Capital Funds – comprised of the Capital Replacement Fund
- Liquidity Funds – comprised of the Operating Fund, Rate Stabilization Fund, Administrative & General Fund, and the Catastrophe Fund

A principal tenet of Mesa Water's Designated Fund Policy shall be the crediting of interest income to specific designated funds until the respective designated fund's maximum is achieved. Once the maximum balance is reached within a specific designated fund, the surplus interest earnings will be reallocated to other designated funds whose funding level is below the targeted or maximum requirement recommended by this policy.

Fund balances will be reviewed on an annual basis at, or near, the end of the fiscal year to ensure compliance with this Policy. In the event the Liquidity Fund balance exceeds the established maximum, excess monies will be transferred annually into the Capital Fund. On an as-needed basis, moneys from the Capital Fund can be moved to pay for operating emergencies to supplement the Liquidity Fund. In addition, in the event that the Capital Fund balance exceeds the established maximum, the Board will make a determination regarding the reallocation of excess monies.

The targeted established for each Fund represents the baseline financial condition that is acceptable to Mesa Water from risk and long-range financial planning perspectives. Maintaining Funds at appropriate levels is a prudent, ongoing business process that consists of an iterative, dynamic assessment and application of various revenue generating alternatives. These alternatives (either alone or in combination with each other) include, but are not limited to: fees and charges, water usage, capital financing, investment of funds, and levels of capital expenditures.

To preserve its AAA credit ratings, in every fiscal year Mesa Water will strive to target unrestricted cash and designated fund balances totaling 600 days of budgeted operating expenses less pass-through expenses (defined as "Operating Expenses"). Should Mesa Water determine to target a different credit rating level, this target will be adjusted accordingly.

Higher credit ratings have provided economic benefit to Mesa Water in terms of lower interest rates on the future borrowings and broader investor base and greater demand for the Mesa Water's bonds, resulting in lower annual debt service cost. However, should Mesa Water decide to pursue a different credit rating, it will need to analyze carefully under what circumstances and in what timeframes it will be optimal to achieve the goal.

The Board shall approve any reallocation of funds or any transfers among Funds.

4. **Mesa Water District Funds**

I. RESTRICTED FUNDS

- a. Bond Proceeds Fund(s): Bond proceeds funds are monies derived from the proceeds of a bond issue. Typically they consist of construction fund monies, and a debt service reserve fund (DSRF). The use of these proceeds is restricted by conditions set forth in the respective legal bond documents. These funds are usually held by the Trustee in favor of the bond holders.

Target Level – The debt service reserve requirement is established at the time of the bond issue. This amount may be recalculated as the bonds are paid down. Any excess principal and/or interest earnings can be used to pay debt service on the bonds.

Events or Conditions Prompting the Use of the Fund(s) – As stipulated in the respective bond documents. Construction fund monies are expected to be spent on applicable projects, while DSRF can only be used in the event of a shortfall in revenues to pay debt service or to pay down principal at maturity.

Periodic Review Dates for Balances – Reviewed by the Trustee and Mesa Water staff on an annual basis.

- b. Customer and Development Deposits: Monies held on behalf of Mesa Water customers as required for their utility account or as cash bonds for development projects.

Target Level – Customer deposits required are based upon the process outlined in Mesa Water's Rules and Regulations for Water Service. Deposit requirements for development projects are outlined in Mesa Water's Miscellaneous Fees and Charges Resolution. The balance in this account will fluctuate depending on the number of utility customer deposits required and the number of development projects in process. Therefore, no target or maximum levels will be established.

Events or Conditions Prompting the Use of the Fund(s) – As deposits on utility accounts are released, they will be refunded to the customer. When development projects are complete, the projects will be closed and a final accounting will be completed. Excess deposit monies will be returned to the development customer.

Periodic Review Dates for Balances – Reviewed by staff on a regular basis as part of the monthly closing process.

II. CAPITAL FUNDS

Mesa Water will strive to maintain a target balance of \$10.0 million in the Capital Funds. The Capital Funds will consist of the following sub-account:

- a. Capital Replacement Fund: The Capital Replacement Fund is used for the replacement of capitalized assets when they reach the end of their useful lives.

Target Level – Mesa Water may set aside replacement funds on a project-by-project basis. The target level should be equal to the \$10.0 million required for the Capital Fund. The maximum balance in the Capital Replacement Fund shall be determined based on Mesa Water's Asset Management Plan.

Events or Conditions Prompting the Use of the Fund – Staff will recommend assets to be replaced during the annual budget preparation. As projects are approved, funds will be appropriated from undesignated funds or available revenues.

Periodic Review Dates for Balances – Fund balances and projected improvement projects will be reviewed by staff and the Board during the preparation and approval of the annual budget.

III. LIQUIDITY FUNDS

Liquidity Funds will be comprised of the following sub-accounts: the Rate Stabilization Fund and the Operating Fund. The balance in the Liquidity Funds will fluctuate depending on the annual Operating Expenses. The maximum balance in the Liquidity Funds will be equal to 180 days of the annual budgeted Operating Expenses.

- a. Administrative & General Fund: The Administrative & General Fund is used to fund certain major general, administration and overhead projects. It is intended to fund (or partially fund) offices, fixtures, furnishings, vehicles and equipment on a pay-as-you-go basis. The Board will appropriate funds for specific projects which can be funded on an as-needed or project-by-project basis.

Funding Levels:

1. Target – The target balance in the Administrative & General Fund will be equal to 20 days of the annual budgeted Operating Expenses.
2. Maximum – The maximum balance in the Administrative & General Fund will be equal to 25 days of the annual budgeted Operating Expenses.

Events or Conditions Prompting the Use of the Fund – Improvement projects will be identified by staff and recommended to the Board during the preparation of the annual budget. As projects are approved, funds will be appropriated from available revenues.

Periodic Review Dates for Balances – Fund balances and projected improvement

projects will be reviewed by staff and the Board during the preparation and approval of the annual budget.

- b. Catastrophe Fund: The Catastrophe Fund is used to begin repair of the water system after a catastrophic event, such as a severe earthquake or fire, while long-term financing is being arranged or insurance claims are being processed.

Funding Levels:

1. Target – The target balance in the Catastrophe Fund will be equal to 150 days of the annual budgeted Operating Expenses.
2. Maximum – The maximum balance in the Catastrophe Fund will be equal to 180 days of the annual budgeted Operating Expenses.

Events or Conditions Prompting the Use of the Fund – The Board may designate use of this fund after establishing that conditions exist as called out in the definition and purpose of the fund.

Periodic Review Dates for Balances – Fund balances and target level will be reviewed by staff and the Board during the preparation and approval of the annual budget.

- c. Rate Stabilization Fund: This fund is established to provide flexibility to the Board when setting rates to allow for absorbing temporary rate fluctuations or for one-time expenditures.

Funding Levels:

1. Target – The target balance in the Rate Stabilization Fund will be equal to 60 days of the annual budgeted Operating Expenses.
2. Maximum – The maximum balance in the Rate Stabilization Fund will be equal to 75 days of the annual budgeted Operating Expenses.

Events or Conditions Prompting the Use of the Fund – This fund is intended to be used to defray any temporary unforeseen and extraordinary increases in the cost of water supply. The Board, on a case by case basis, will determine the amount and timing for any use of the fund.

Periodic Review Dates for Balances – Fund balances will be reviewed by staff and the Board during the preparation and approval of the annual budget.

- d. Operating Fund: The Operating Fund is used for unanticipated Operating Expenses. This fund is designated by the Board to maintain working capital for current operations and to meet routine cash flow needs.

Funding Levels:

1. Target – The target balance in the Operating Fund will be equal to 120 days of the annual budgeted Operating Expenses.
2. Maximum – The maximum balance in the Operating Fund will be equal to 150 days of the annual budgeted Operating Expenses.

Events or Conditions Prompting the Use of the Fund – Upon Board authorization, this fund may be routinely utilized by staff to cover temporary cash flow deficiencies caused by timing differences between revenue and expenses and extraordinary decreases in revenues and unexpected increases in expenses.

Periodic Review Dates for Balances – Fund balances and target level will be reviewed by staff and the Board during the preparation and approval of the annual budget.

5. **Investment Guidelines**

It has been the Mesa Water's practice to rely primarily on a pay-as-you-go (pay-go) strategy to fund capital improvements and replacement of existing assets. However, maintaining a balance between debt and pay-go sources may provide an added benefit to Mesa Water in terms of allowing for a more optimal investment strategy. In the context of these policies and in circumstances where such balance is present, the investment portfolio can be separated into short and long portfolios to maximize investment returns.

6. **Delegation of Authority**

The Board has sole authority to amend or revise the Designated Funds Policy. Through approval of this Policy, the Board has established written procedures for staff to follow in the management of Mesa Water's Designated Funds.