Amador Water Agency

External Debt Management Policy

Reviewed and Adopted
March 25, 2021

100.00 Purpose of the Policy

This policy sets forth comprehensive guidelines for the financing of capital expenditures in accordance with Government Code Section 8855(i). It is the objective of this policy that – 1) the Agency obtain financing when necessary, 2) the process for identifying the timing and amount of debt or other financing be as efficient as possible, 3) the most favorable interest rate and issuance costs be obtained, and 4) when appropriate, future financial flexibility be maintained.

200.0 Policy

The issuance of long-term debt is a valuable funding resource for the Agency. Used appropriately and prudently, long-term debt can stabilize the Agency's charges and rates over time. Long-term debt is defined as financing greater than 5 years. Short term debt is defined as 5 years or less and will be used for short term financing of equipment, hardware, software and other items where long term financing might otherwise exceed the asset life.

To minimize dependency on debt financing for capital projects, annual renewal and replacement capital projects should be adequately funded from rates and capacity charge. Funding levels for capital investments will be sufficient to meet capital improvement projections needed as outlined in the current budget and five year Capital Improvement Plan (CIP). Long-term debt will be considered only for large capital improvement projects. The Agency will meet the minimum and target Debt Service Coverage (DSC) requirements as imposed by bond covenants. The Agency will not issue long-term debt to support operating costs.

A. Use of Long-Term Debt As a Funding Mechanism – Use of long-term debt will be minimized. The Agency may consider the use of long-term debt financing when it appears that a capital project, or other expenditures as deemed appropriate by the Board, is of such a magnitude that it will negatively impact the Agency's rates in the short-term. The benefit of long-term debt financing is that it will spread the costs of the capital asset over a longer period of time and will, therefore, approximate the useful life of the asset, and over time, charge those customers that benefit from that asset more equitably.
B. Types of Long-Term Debt – The Agency will strive to utilize the type of debt that has the lowest costs, while not imposing any burdensome covenants or reporting requirements. Types of long-term debt to be used by the Agency include: revenue bonds, certificates of participation, installment purchase agreements or direct placement debt with a bank or government agency.

C. Legal Covenants – The Agency will manage its operations and maintenance to meet all bond covenants associated with the long-term debt. Bond covenants are legal obligations of the Agency.

D. Debt Service Coverage Covenants – Long-term debt issuances typically contain legal covenants regarding DSC. A DSC ratio is an important financial measure of the Agency's ability to repay the outstanding debt obligation, and is reviewed for adequacy by banks and rating agencies. Generically, the DSC ratio is the Agency's net operating income divided by the total annual debt service payment. For financial planning purposes, the targeted annual DSC ratio will be greater than or equal to 1.50 on all outstanding debt that carries such a covenant.

E. Reporting Standards – The Agency will fully adhere to all applicable Government Accounting Standards Board (GASB) requirements and recognized best practices for the accounting treatment and disclosure of debt obligation transactions in its audited financial statements and other relevant publications.

F. Revenue-Bonded Debt Capacity – The issuances of debt are supported by the revenues of the Agency. The ability of the Agency to fund and support revenue bonded debt will financially establish a debt level and capacity for revenue-bonded debt.

300.00 Conditions for Debt Issuance

When the Agency determines that debt issuance is necessary, the Agency will assess the market conditions and timing for debt issuance to include issuing debt – 1) in times of favorable market conditions, 2) when Bond ratings would qualify Agency issuances to be investment grade, and 3) when revenues are sufficient to adequately cover expected debt service and issuance costs.

Bond credit enhancements will be considered when necessary for market acceptance and when costs are favorable to the Agency.

400.00 Conditions for Debt Refinancing

Debt refinancing (refunding) is an important debt management tool for the Agency. There are three key concepts that must be taken into consideration when evaluating a debt for refunding:

1. Financial and Policy Objectives
2. Financial Savings/Results of Financing
3. Bond Structure and Escrow Efficiency

A. Financial and Policy Objectives – The Agency may undertake a refinancing for a number of financial and/or policy objectives, including to achieve debt service savings, eliminate restrictive debt/legal covenants, restructure the stream of debt service payments, or to achieve other policy objectives. Although in most circumstances the Agency may undertake a refunding to obtain economic savings, it may refund an issue to restructure its debt portfolio in order to obtain budgetary/cash flow relief or to address exposure to other costs/liabilities. Refunding debt may not be used to extend the maturity of existing debt.

B. Financial Savings/Results of Financing - The financial framework regarding the evaluation of refunding opportunities is to be developed and evaluated by the Agency. Such evaluation will be conducted by the Financial Services Manager or Executive Management staff, typically to include the efforts of outside financial advisors.

C. In certain circumstances, lower savings thresholds may be justified but must be approved explicitly by the Board.

D. Bond Structure and Escrow Efficiency – The Agency's debt management practices should anticipate the potential for future refundings. When debt is issued, careful attention should be paid to the bond structure to address features that may affect flexibility in the future. To that end, upon debt issuance the Agency shall consider: optional redemption provisions, bond coupon characteristics giving up call rights for certain maturities in exchange for a lower interest rate on the bonds, call provisions that permit the redemption of bonds in any order of maturity or on any date, call provisions that permit the issuer to call bonds at the earliest date without incurring a significant interest-rate penalty, and coupons on callable bonds priced as close to par as possible at the time of original issue.

500.00 Internal Controls

To ensure that proceeds of any debt issued in accordance with its governing documents and this Policy no disbursements shall be made without the approval of the General Manager or Financial Services Manager. For Capital improvement Plan projects, the draw request shall be provided to the Finance Manager for budget approval by the project engineer with the consent of the Agency's inspector. Draw request approval shall only be provided when the General Manager is in receipt of the Financial Services Manager's budgetary approval and an appropriate certification from the construction project manager with supporting invoices from suppliers and/or contractors evidencing appropriate expenses in connection with the project.

In the case of an issue of bonds, the proceeds of which will be used by a governmental entity other than the Agency, the Agency may rely upon a certification by such other governmental entity that it has adopted the policies described in SB 1029.

600.0 Interest Rate Swaps

The Agency will not use interest rate swaps as a method to reduce bond costs or manage interest rate risk. The size of the Agency's resources and the complexity of financial derivate products are not deemed appropriate.

700.00 Authority

The General Manager and Financial Services Manager are responsible for adherence to this policy and regular reporting of the Agency's financial status. Board oversight will be accomplished through regular reporting of financial status and review of this Policy.

800.00 Policy Review

This Policy will be reviewed at least every 2 years.