CAMBRIA COMMUNITY SERVICES DISTRICT

DEBT MANAGEMENT POLICY

Purpose of the Policy

This policy establishes parameters for evaluating, issuing and managing the Cambria Community Service District's (the "District") debt and may be used as a guideline to promote sound financial management.

The District objective in issuing debt will be to: (1) Achieve the lowest cost of capital; (2) Ensure rate- and tax- payers equity; (3) Maintain high credit rating and access to credit enhancement; and (4) Preserve financial flexibility.

Prior to the issuance of new debt, the Board of Directors shall review the debt to be financed. If required by law, such review shall be at a public hearing. This requirement shall not apply to the refinancing of existing debt.

Policy

Short-Term Debt

The District may utilize short-term debt financing (including leases) to finance certain essential equipment and vehicles. These assets can range from service vehicles to equipment. The underlying asset must have a minimum useful life of one year or more. Short-term financing, including leases, on bill financing and capital lease purchases are executed to meet such needs. The Board of Directors must approve any such short-term financing for assets costing more than $25,000 by Resolution.

Long-Term Debt

The issuance of long-term debt is a valuable funding resource for the District. Used appropriately and prudently, long-term debt can minimize the District's charges and rates over time, depending on which Fund issues debt.

To minimize dependency on debt financing for capital projects, annual renewal and replacement capital projects will be adequately funded from rates. Funding levels for capital investments will be sufficient to meet capital improvement projections needed as outlined in the current Capital Improvement Plan. Long-term debt will be considered only for large capital improvement projects or greater-than-normal capital plans. The District will be managed to at least meet, and potentially exceed, the minimum and target Debt Service Coverage (DSC) requirements as imposed by bond covenants. The District 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 District 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 District'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 District will strive to utilize the type of debt that has the lowest costs, while not imposing any burdensome covenants or reporting requirements.

C. Legal Covenants – The District will meet all bond covenants associated with the long-term debt. Bond covenants are legal obligations of the District.

D. Debt Service Coverage Covenants – Long-term debt issuances typically contain legal covenants regarding debt service coverage (“DSC”). A DSC ratio is an important financial measure of the District’s ability to repay the outstanding debt obligation, and is reviewed for adequacy by banks and rating agencies. Generically, the DSC ratio is the District’s net operating income, as specifically defined by the relevant bank or rating agency, divided by the total annual debt service payment. For financial planning purposes, the targeted annual DSC ratio will be greater than or equal to 1.85 on all outstanding debt that carries such a covenant.

E. Reporting Standards – The District 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 District. The ability of the District to fund and support revenue-bonded debt will financially establish a debt level and capacity for revenue-bonded debt.

G. The District will issue debt only in the case where there is an identified source of repayment. Bonds 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.

Conditions for Debt Issuance

When debt issuance is determined necessary, the District 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 District issuances to be investment grade, and 3) when revenues, including anticipated increases, are sufficient to adequately cover expected debt service and issuance costs.

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 financing be completed.

Bond credit enhancements, such as insurance against default, will be considered when necessary for market acceptance and when costs are favorable to the District.

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

A. Financial and Policy Objectives
B. Financial Savings/Results of Financing
C. Bond Structure and Escrow Efficiency

Financial and Policy Objectives – The District 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 District 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 and to extend the maturity.

Financial Savings/Results of Financing - The financial framework regarding the evaluation of refunding opportunities is to be developed and evaluated by the District's Financial Manager, typically to include the efforts of outside financial advisors. It is important to note that federal tax law typically permits an issuer to conduct one advance refunding over the life of a bond issue2. As such, the District must take greater care (i.e., require a higher savings threshold) when evaluating an advance refunding opportunity.

In certain circumstances, lower savings thresholds may be justified. For example, when an advance refunding is being conducted primarily for policy reasons (other than economic savings), interest rates are at historically low levels or the time remaining to maturity is limited, and as such, future opportunities to achieve greater savings are not likely to occur.

Bond Structure and Escrow Efficiency – The District'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 District 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.

Escrow Efficiency - The lower the cost of the escrow the more efficient the escrow. Also, in order to be efficient, escrow securities need to mature or pay interest when debt service payments of the refunded escrow are due.

Current vs. Advance Refunding - There are two types of refundings, as defined by Federal Tax laws; a current refunding in which a refunding takes place (i.e., refunding bonds are sold) within 90 days of the optional call date, and an advance refunding in which refunding bonds are sold more than 90 days prior to the first call date. Federal tax law typically permits an issuer to conduct one advance refunding over the life of a bond issue.

Interest Rate Swaps
The incurring or carrying of variable-rate debt obligations by the District involves a variety of interest rate payments and other risks that interest rate swaps are available to offset, hedge, or reduce. It is the policy of the District to utilize such interest rate swaps to better manage its debt portfolio. The District will consider executing an interest rate swap transaction if it expects the swap transaction will result in any of the following:

A. Reduce exposure to changes in interest rates on a financial transaction;
B. Result in a significantly lower net cost of borrowing with respect to the District's debt consistent with an established target; or
C. Manage variable interest rate exposure consistent with prudent debt practices and guidelines as approved by the Board.

Savings Target
Interest rate swaps will require a significant financial benefit or savings versus traditional fixed-rate debt. For an interest rate swap intended to produce the effect of a synthetic fixed rate transaction, the swap transaction must generate 3% or greater net present value savings compared to standard fixed-rate bonds which have the same optional redemption features.

Restrictions
The District will not enter into any swap transaction:

A. for speculative purposes.
B. if the swap presents an extraordinary risk to the District's liquidity to terminate the agreement due to unforeseen events.
C. if there is insufficient price transparency to allow for fair market valuation.

Provider Requirements
The transaction provider will have a credit rating of AA (or equivalent) or better from at least two nationally recognized credit rating agencies (at the time of agreement execution). The transaction provider will have a demonstrated record of successfully executing derivative transactions and have a minimum capitalization of $2 billion.

Use of Independent Advisor
The District will use a professional advisor or designated swap representative ("Swap Advisor") to assist in the assessment, structuring, and pricing of proposed or existing interest rate swaps. The Swap Advisor will be a firm which:

A. is a Municipal Advisor registered with the Securities and Exchange Commission;
B. has sufficient knowledge to evaluate the swap transaction and risks;
C. is not subject to a statutory disqualification;
D. is independent of the swap dealer or major swap participant;
E. undertakes a duty to act in the best interests of the District;
F. provides appropriate and timely disclosures to the District; and
G. evaluates fair pricing and the appropriateness of the swap.

Authority

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

Policy Review

This Policy will be reviewed at least biennially.