ZONE 7 BOARD OF DIRECTORS
SUMMARY NOTES OF THE FINANCE COMMITTEE

February 14, 2018
11:00 a.m.

Directors present: Dick Quigley
Angela Ramirez Holmes
Bill Stevens

Staff present: Jill Duerig, General Manager
Osborn Solitei, Treasurer/Assistant General Manager, Finance
Linda VanBuskirk, Executive Assistant

Director Quigley called the meeting to order at 11:00 a.m.

1. Public Comment on Items Not on the Agenda: There were no comments from the public.

2. FY 2017-18 Second Quarter Revenue & Expenditure Report

Osborn Solitei, Treasurer/Assistant General Manager, Finance, presented a summary of the Second Quarter Revenue and Expenditure Report. He stated that the report covers the first six months of Fiscal Year 2017-18, July 1 through December 31, 2017 and year-end projections for FY 2017-18. Mr. Solitei highlighted revenues and expenditures for each of the Agency's funds as outlined in the staff report.

Fund 100 – Water Enterprise Operations. Unaudited actual year-to-date water sales are $27.4M. Unaudited actual year-to-date expenses include staff labor ($7.0M) and AMP funding ($6.7M) plus other operating costs brought the total to $22.4M. The projected FY estimated ending fund balance is $10.3M. There was some discussion about the current low allocation of 20% from the Department of Water Resources and the possibility of the allocation dropping to zero due to very low snow levels. Reserves are increasing but are still below Board policy.

The Committee discussed seeing behavioral changes of rate payers/water users such as replanting lawns and softscapes. Director Quigley expressed concern over the Agency having no funds in the Drought Contingency reserve while we may head into another drought year. Ms. Duerig advised that a cost-of-service study was planned for this year. Director Stevens emphasized that recovery of reserves should not be delayed too much, given the possibility of another drought in the near future.

Fund 110 – State Water Facilities is funded through property taxes. The unaudited actual year-to-date expense is $16.7M. The projected FY estimated ending fund balance is $22.3M. Reserves in this fund are compliant with Board policy.

Fund 120 – Water Renewal/Replacement & System-Wide Improvements. Staff issued the bid package for the DVWTP Ozone project in January 2018, and bids are due February 20, 2018. The Agency is on track to issue bonds for the ozone projects in late March/April 2018; therefore, the FY 2017-18 Q2 revenue projection includes bond proceeds of approximately $55M for both projects. Staff recommends establishing an initial Rate Stabilization Reserve of $6.3M equal to two years of debt service payments from the capital project reserves concurrently with the current debt financing. This will be in lieu of a debt service reserve requirement. This recommendation will be brought before the full Board at the March meeting along with the other debt financing items. Director Ramirez Holmes inquired about the funding for the Rate Stabilization Reserve and asked where the $6.3M comes from. Mr. Solitei explained that, to optimize Zone 7's ratings, the Finance Team for the current debt financing for the ozone project and refinancing of the Cawelo capital obligation recommends setting up an initial rate stabilization fund equivalent to two years of annual debt service payment or, alternatively, setting up a debt service reserve fund. A debt service reserve fund is a fund which is set up at the time of issuing bonds to pay for principal and interest if pledged revenues are insufficient to satisfy the debt service requirements; it would be under the control of a trustee rather than Zone 7. Staff recommends setting up an initial rate stabilization reserve of $6.3M from the existing capital reserves in lieu of a debt service reserve fund. This amount is equal to two years of debt service payments. Setting up a debt service reserve fund will increase the current debt financing and would remain under Zone 7's control. Director Ramirez Holmes suggested that Staff include this explanation on the rate stabilization reserve to the full Board.

Fund 130 – Water System Expansion Fund. Unaudited actual year-to-date revenue of $14.2M is comprised of connection fees from 530 connections, mainly from the Dublin Crossings, Gale and Wallis Ranch developments. Mr. Solitei explained that the the FY 2017-18 budget estimated 1,600 connections, which is the Connection Fee Study estimate, but the end-of-year estimate has been reduced to around 80% of that amount based on recent trends and information from Retailers. The Cawelo Water District (Cawelo) capital obligation of approximately $16M will be refinanced for net present value (NPV) saving of approx. $2.5 million. In addition, at the February 2018 Board meeting, staff will be recommending early payoff of the Semitropic Water Storage District (Semitropic) capital obligation with a cost savings of $0.12M. Staff recommends setting up an initial rate stabilization reserve of $2.3M equal to two years of debt service payments for this Cawelo refinancing from the capital project reserves concurrently with the current debt financing. This will be in lieu of a debt service reserve.

Director Ramirez Holmes asked if the Cawelo refinance would extend the time frame beyond the original debt service timeline. Mr. Solitei responded that no, payments will continue annually through 2035. Director Ramirez Holmes asked what are the issuance costs of the refinancing. Mr. Solitei responded that the cost is estimated to be $20,000 for the Agency's Bond Counsel, and another estimated $10,000 for Cawelo's Bond Counsel. Director Ramirez Holmes stated it is important to have a conversation about the costs vs. the savings. Mr. Solitei stated that the Agency will be saving about $200,000 per year on capital payments, which will be very good for the rate payers.

Director Quigley expressed support for paying off Cawelo and Semitropic earlier as this will save the Agency a lot of money. He stated it is important for rate payers to know that both

Semitropic and Cawelo water is like an insurance policy and is more expensive water by a considerable amount per acre foot. He would like to see this pointed out so that rate payers are aware of the cost savings measures the agency has employed. Director Stevens concurred, adding that, with the savings achieved through purchase of the North Canyons office building, Zone 7 is really reducing its costs.

Fund 200 – Flood Protection Operations. Unaudited actual year-to-date revenue of $4.6M is comprised mostly from property taxes. The unaudited actual year-to-date expense is $6.1M. The projected FY estimated ending fund balance is $12.3M. The reserves are decreasing due to increased expenses for the storm damage repair projects, currently estimated at $44M to repair 208 sites. Projected reserves in this fund are compliant with Board policy.

Fund 210 – Flood Protection Development Impact Fee Fund. The primary funding source is from development fees and the unaudited year-to-date actuals are $2.5M. The unaudited actual year-to-date expenditures include agency staff labor for capital projects such as the SMMP Update and the Arroyo Mocho - Granada/Murrieta Project. The projected FY estimated ending fund balance is $60.8M. Reserves in this fund are compliant with Board policy and will be used to fund new development's share of the SMMP. A draft SMMP amendment will be discussed with the Water Resources Committee in the coming months.

Other Funds: Mr. Solitei also presented the other miscellaneous funds (Fund 300 Water Facilities Fund, Fund 310 Water Supply and Reliability Fund).

Director Stevens stated that all Agency reserve funds are compliant with minimum reserve requirements except for Fund 100. He suggested creating a list which shows everything the Agency has done to save money such as the purchase of the main office building, refinancing Cawelo and paying off Semitropic. Director Quigley concurred that this would be good for the public to know.

Director Ramirez Holmes asked for clarification that the only change made to this report is the addition of the rate stabilization reserves within Fund 120 and Fund 130. Mr. Solitei reiterated that the funding of the rate stabilization reserves is from the existing capital reserves.

Director Quigley asked if there were any public comments. None were received.

3. Investment Report as of December 31, 2017

Mr. Solitei then provided a brief summary of the investments held in Zone 7's name by securities categories as of December 31, 2017. These investments are made pursuant to the Agency investment policy as adopted by the Board in May, 2017 by Resolution No. 17-42. As of December 31, 2017, the Agency had $27.7 million in its investment portfolio.

Director Ramirez Holmes inquired what instructions were given to the investors regarding where the money should be invested and how can the policy be changed if the Agency does not what to invest on some companies, securities etc.? Mr. Solitei explained that the investments are made pursuant to the Agency investment policy adopted by the Board in May 2017. The investment policy provides investment guidelines and eligible securities as defined by the California Code Section 53600, et seq. He referred to page 5 of the Agency's Investment Policy as an example of the Medium Term Corporate Notes & Bonds securities. He added, the investment policy is to be reviewed and then renewed annually by the board.

The Committee members expressed support that Staff should forward the investment report to the full board at its February meeting.

Director Quigley asked if there were any public comments. None were received.

4. Verbal Reports - None.

5. Adjournment - Director Quigley adjourned the meeting at 11:58 a.m.