

# *Financial Policies*

EPWU is accounted for as an Enterprise Fund, which is a proprietary fund. Enterprise Funds are used to account for operations that are financed and operate in a manner similar to private business enterprises, where the intent of the governing body is that the costs (including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. All activities necessary to provide such services are accounted for in this fund, including, but not limited to, administration, operations, maintenance, financing and related debt service, and billing and collection. EPWU uses no other funds to account for its' activities.

## **FLOW OF FUNDS POLICY**

City Ordinance No. 752 established certain “funds”. These “funds” are mandatory asset segregation and not funds in the sense of governmental fiscal and accounting entities with self-balancing sets of accounts. These funds are described in the following paragraphs.

EPWU funds are designated in City Ordinance No. 52 which was adopted on May 22, 1952. This ordinance authorized the issuance of a series of Revenue Bonds entitled “City of El Paso, Texas, Water and Sewer Revenue Bonds Series 1952”, and the City reserved the right and option in the 1952 resolution to issue, under certain conditions, additional bonds on a parity as to lien and right with the Series 1952 Bonds.

Ordinance No. 752, as amended, requires that gross revenues of the System be applied in sequence to: (a) current expenses of maintenance and operations; (b) debt service and service requirements; (c) capital expenditures, or unexpected or extraordinary repairs or replacements, or for any other lawful purpose. The following funds have been established to account for the application of gross revenues: (i) Water and Sewer Fund; (ii) Water and Sewer Revenue Bond Funds, known as the Interest and Sinking Fund; (iii) Water and Sewer Revenue Bond Reserve Funds; and (iv) Water and Sewer Improvement Fund. All revenues of every nature received through operations of the System shall be paid into the Water and Sewer Fund. The Bonds Funds are required to contain an amount of money and investments equal to the principal and interest requirement during the fiscal year. The funds are described as follows:

### ***Water & Sewer Fund***

All gross revenues shall be deposited from day to day as collected in the Revenue Fund. Moneys on deposit in the Revenue Fund shall be first used to pay all Operation and Maintenance Expenses. The revenues of the System not actually required to pay Operation and Maintenance Expenses (the "Net Revenues") shall be transferred from the Revenue Fund to the other funds, in the order of priority, in the manner set forth in the Bond Ordinance.

### ***Interest and Sinking Fund***

The following shall be deposited in the Interest and Sinking Fund:

1. Such amounts, in equal monthly installments, commencing on the first day of the month next following the month of Closing, and on the first day of each month thereafter, as will be sufficient to pay the interest scheduled to come due on the bonds next interest payment date, less any amounts already on deposit therein for such purposes derived from the proceeds of the bonds or from any other lawfully available source.
2. Such amounts, in equal monthly installments, commencing on the first day of the month next following the month of Closing, and on the first day of each month thereafter, as will be sufficient to pay the next maturing principal of the bonds, including any scheduled mandatory redemption of bonds.

### ***Reserve Fund***

So long as the funds on deposit in the Reserve Fund created for the benefit of all bonds are equal to the Reserve Fund Requirement, no deposits need to be made to the credit of the Reserve Fund. However, should the Reserve Fund at any time contain less than the Reserve Fund Requirement, then subject and subordinate to making the required deposits to the credit of the Interest and Sinking Fund, the Utility shall transfer from the Net Revenues in the Revenue Fund and deposit to the credit of the Reserve Fund, on the first day of each month, such amounts in equal monthly installments to accumulate within at least five years and one month a sum equal to the Reserve Fund Requirement. The money on deposit in the Reserve Fund may be used to pay the principal and interest on all bonds at any time there are not sufficient funds on deposit in the Interest and Sinking Fund for such purpose.

### ***Improvement Fund***

All money remaining in the Revenue Fund at the end of each month after all payments required to be made from the revenue fund have been made and all deficiencies accumulated from prior months have been paid shall continue to be paid to the Improvement Fund established in connection with the System, and shall be held in and paid out from such fund for the following purposes:

1. To pay the cost of any special or extraordinary repairs or replacements to or of the properties comprising the System, properly payable with such money under the laws of the State of Texas, necessitated by reason of some emergency.
2. To the extent permitted by law, for the making of extensions, improvements, and betterments of the System.

### ***Contributions in Aid of Construction Fund***

Any moneys that may be received by the Board that shall represent contributions in aid of construction shall be deposited in a separate account at the Depository Bank. Such contributions shall not be considered as part of the gross revenues of the System. Payments from such bank account shall be made only for the purposes for which the contributions were made, including any refunds that may become due to any contributor.

## **CAPITAL IMPROVEMENTS BUDGET POLICY**

For capital budgeting purposes, the Utility staff uses a strategic weighting scale to determine priorities for each of the scheduled projects. Criteria used to prioritize capital projects include regulatory requirements; aging and condition; overloaded or overtaxed infrastructure; environmental impacts; reliability; drought, customer service; other agency driven projects (street and highway construction); growth and new development; new water supplies, financial impacts; and operational efficiency. The Utility defines a capital expenditure as an asset with an individual cost of \$5,000 or more and an estimated useful life in excess of one year.

Due to state procurement laws and the nature of capital improvement expenditures, it generally takes more than one fiscal year to completely spend one year's appropriations. By law, EPWU cannot award a project unless it is fully funded. However, many large projects have multiple year and/or multiple phase construction periods. El Paso Water Utilities uses several benchmarks of efficiency to ensure capital budget integrity. These include timely completion clauses, aggressive efforts to minimize change orders, and

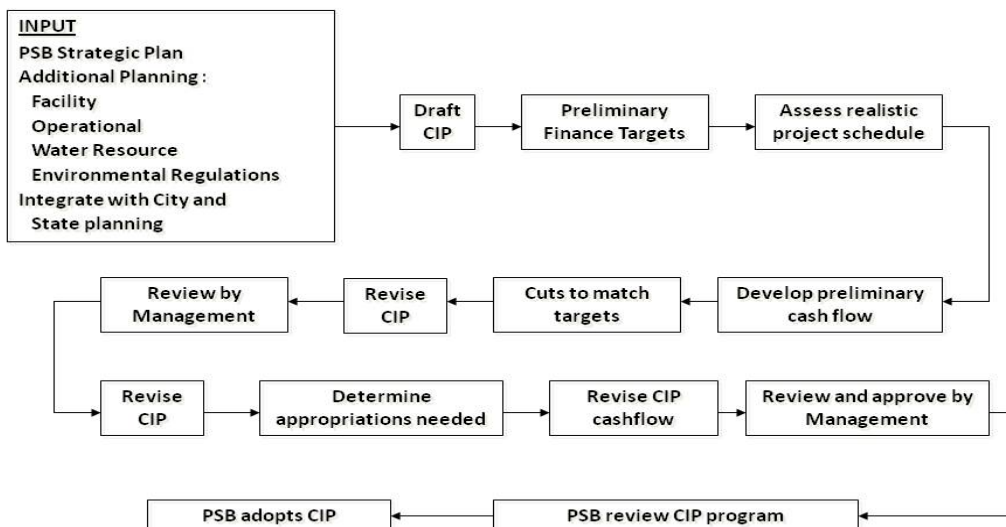
tracking the progress of the overall **capital improvement plan (CIP)**. On an annual basis, staff members from Engineering, Planning, Operations, and Finance update the CIP. The final CIP document stretches from a mid-year update out to a ten year planning horizon. It incorporates all known or likely to occur variables based on growth, maintenance of the current system, and addresses issues including new and/or probable regulatory requirements or political directives.

The following is a typical schedule for the development of a CIP budget:

- ❑ March 1 – fiscal year begins
- ❑ April to May – strategic planning updates to the 10 year capital plan
- ❑ August – Project managers gather information for 1<sup>st</sup> draft CIP budget
- ❑ September – draft CIP budget reviewed by Management and Finance
- ❑ October – revisions made to draft and presented to President/CEO
- ❑ November – Management approves capital budget and Finance assigns necessary funding
- ❑ November to December – budget workshops to review the operating and capital budget requests with the Public Service Board and the public can comment
- ❑ December – PSB approves and adopts the final combined operating and capital budget for the fiscal year beginning next March 1

This simplified flowchart graphically represents the entire capital budgeting process. In

## Annual Capital Improvement Program



addition, operating costs related to new infrastructure is incorporated in the financial plan. There are numerous opportunities for staff updates, public input, and revisions, so this chart is a representative snapshot of a truly dynamic process.

## **OPERATING BUDGET POLICY**

The Utility's fiscal year runs from March 1 to the last day of February the following year. EPWU ties its 12-month budget year to the water "season." Historically speaking, without a year-round water supply of surface water to treat, the water treatment plants shut down for maintenance during the winter months. The surface water supply is not year-round because the upstream irrigation and diversion dams, including Elephant Butte and Caballo dams, are served by snow melt from the Rocky Mountains. The water is released annually in conjunction with the farmers' irrigation season, which normally starts in mid-February and ends in early October. The Utility's surface water production season runs concurrently with the farmers' irrigation season. A normal fiscal year would include the following significant financial events:

- ❑ Mid February – surface water production season begins except in times of drought
- ❑ March 1 – fiscal year begins
- ❑ April to May – strategic planning updates to the 10 year capital plan
- ❑ May to September – peak consumption months for EPWU customer demand
- ❑ September – six month operating results distributed to each section manager so sections can begin planning for the upcoming fiscal year beginning next March
- ❑ October – surface water production ends (mid-month) and water treatment plants shut down except in times of drought
- ❑ October – sections submit operating budget requests
- ❑ October – internal budget conferences begin between the Sections and Management/Finance
- ❑ November – Management approves preliminary capital and operating budget requests
- ❑ November/December – budget workshops in which the Public Service Board reviews the budget requests and the public can comment
- ❑ December – PSB approves and adopts the final combined operating and capital budget for the fiscal year beginning next March 1

The Utility's FY 2011-12 budget is a balanced budget, with the revenue and other financing sources equal to the expenditures and other uses.

## **BUDGET AMENDMENT POLICY**

Operating or capital budget line item transfers are done on a memorandum basis, submitted by the requesting manager to Finance. The transfer is subject to approval by management but does not need approval by the Public Service Board. Emergency funding authorizations and amendments to the approved operating or capital budgets can only be done with approval by the Public Service Board.

## **REVENUE POLICY**

Ordinance No. 752 also requires that the Board maintain rates sufficient to produce or yield revenues to produce in each fiscal year an amount adequate to pay all expenses incurred for the operations and maintenance of the System as such expenses shall accrue during the year and to produce an additional amount equal to 150% of the aggregate amount required to be paid in such year for principal and interest and redemption premiums on bonds payable from the Bond Funds. Another financial target that is used in preparing the five-year financial plan is maintaining a 45-day operating reserve fund balance.

Ordinance No. 752 also provides that the Board will permit no free water or services to be supplied to the City or to any other user. However, the ordinance requires that 10% of the total amounts received by the Board from the sale of water be paid to the City Treasurer. The money received by the City Treasurer may be expended by the City under the direction of the City Council for any purpose for which revenues of the System may be legally used under the state laws of the State of Texas.

EPWU is a component unit of the City of El Paso and operates as an autonomous enterprise fund. Enterprise funds are used to account for operations that are financed and operated in a manner similar to a private business enterprise, where the intent of the governing body is that the costs (including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. All activities necessary to provide such services are accounted for in this fund, including (but not limited to) administration, operations, maintenance, financing and related debt service, and billing and collection. Because the Utility operates in a proprietary manner, the major revenue sources are user charges for water and wastewater services. The Utility's revenue requirements are based on cost of service.

This includes operating costs, expenditures for capital improvements, and repayment of debt. The description and figures of the revenue sources are covered in the financial overview section of this budget.

### **INVESTMENT POLICY**

The Utility also has an Investment Policy which establishes the guidelines for: 1) who can invest PSB funds; 2) how PSB funds will be invested; and 3) when and how a periodic review of investments will be made. In addition to this policy, bond funds shall be managed by their governing ordinance and all applicable State and Federal Law. The investment policy must comply with the Texas Public funds Investment Act of 1995 and any such amendments since then. The primary objectives of the investment policy are 1) preservation of capital; 2) safety of PSB funds; 3) maintenance of sufficient liquidity; 4) maximization of return within acceptable risk constraints; and 5) diversification of investments. The investment policy requires an annual review and adoption of its investment policy and strategies, and a quarterly comprehensive report to the PSB.

### **DEBT SERVICE POLICY**

Planned rate increases on a consistent basis are programmed in the Financial Plan, and are mainly driven by the capital improvement program and debt service coverage required both by the revenue bond covenants and by the Public Service Board's benchmarks for financial management. While the revenue bond covenants require debt service coverage of 1.5 times (meaning 150% of the current year's debt service requirements must be available that fiscal year), the Public Service Board's financial benchmark is to maintain as close to a 2.0 times coverage as feasibly possible. The Utility does not have a legal debt limit.

