

ORDER ADOPTING CODE OF ETHICS, TRAVEL EXPENSE POLICY,  
INVESTMENT POLICY, POLICIES AND PROCEDURES FOR SELECTION  
AND REVIEW OF CONSULTANTS, POLICIES CONCERNING THE USE  
OF MANAGEMENT INFORMATION INCLUDING THE FORMATION OF AN  
AUDIT COMMITTEE, APPOINTMENT OF INVESTMENT OFFICER AND CHIEF  
FINANCIAL OFFICER AND CERTAIN OTHER MATTERS

THE STATE OF TEXAS

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§

COUNTY OF DENTON

DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B

We, the undersigned officers of the Board of Directors (the "Board") of Denton County Fresh Water Supply District No. 1-B (the "District"), hereby certify as follows:

1. The Board convened in special session, open to the public, on October 18, 1995, at 2001 Bryan Tower, Suite 700, Dallas, Texas, and the roll was called of the members of the Board, to-wit:

Michael Scott Rohrman	President
John Philip Brosseau	Vice President
Jerry Peterman, Jr.	Secretary
Charles Curtis Vaughn	Assistant Secretary
Robert Lowell Pierce	Assistant Secretary

All members of the Board were present except Michael Scott Rohrman

Whereupon, among other business conducted by the Board, Director Pierce introduced the Order set out below and moved its adoption, which motion was seconded by Director Brosseau and after full discussion and the question being put to the Board of Directors, said motion was carried by the following vote:

"Aye" 4; "No" 0.

The Order thus adopted is as follows:

WHEREAS, DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B (the "District") is a water control and improvement district operating pursuant to Chapter 49 and Chapter 51, of the Texas Water Code, as amended; and

WHEREAS, Texas Water Code §49.001 et seq., requires that the Board of Directors of the District adopt certain policies and procedures in writing, including a code of ethics, a travel expense policy, an investment policy, policies and procedures for selection, monitoring, or review and evaluation of professional services, a uniform method of accounting and reporting that complies with requirements of the Texas Natural Resource Conservation Commission ("Commission") and policies that ensure a better use of management information, including budgets for use in planning and controlling cost, a functioning audit committee of the board and uniform reporting requirements that use "Audits of State and Local Governmental Units" as a guide on audit working papers and that uses "Governmental Accounting and Financial Reporting Standards";

WHEREAS, pursuant to an amendment to Chapter 2256, Government Code, as amended, the Public Funds Investment Act (the "Act"), requires that the Board of Directors of the District revise its current written investment policy regarding the investment of its funds and funds under its control and designate one or more officers or employees of the District to be responsible for the investment of such District Funds in accordance with the Act as well as designate a Chief Financial Officer of the District; and

WHEREAS, the Board of Directors deems it necessary and advisable to designate the District's Bookkeeper as the Investment Officer of the District responsible for the day to day investment and reinvestment of the District's funds and to additionally appoint and designate the District's treasurer as the District's Chief Financial Officer of the District;

NOW, THEREFORE, BE IT RESOLVED BY THE BOARD OF DIRECTORS OF DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B THAT:

I.

The Board of Directors hereby adopts Attachments "A" through "E" hereof as its written policies and procedures required by Texas Water Code §49.001 et seq. and the Act.

II.

The Board of Directors hereby designates and selects the District's Bookkeeper to be the Investment Officer of the District, and authorizes the District's Bookkeeper to exercise responsibility for the investment of District Funds in accordance with the provisions of the Act and further designates the District's Treasurer as its Chief Financial Officer.

III.

The Board of Directors hereby authorizes such Investment Officer and Chief Financial Officer to attend at least one training session relating to the treasurer's or officer's responsibilities under Chapter 2256.008(a), Government Code, as amended, within 12 months after taking office or assuming duties. Should the individual Bookkeeper assigned to the District by the Company who provides bookkeeping services to the District change, such company shall automatically provide the District with a trained qualified Investment Officer at all times.

IV.

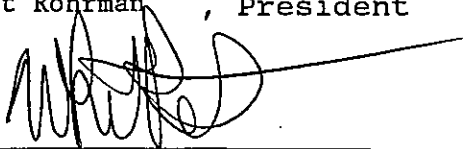
The President or Vice President and the Secretary or Assistant Secretary of the Board of Directors are authorized to evidence adoption of this Order on behalf of the Board of Directors and to do all other things proper and necessary to carry out the intent hereof.

APPROVED AND ADOPTED the 18th day of October, 1995.

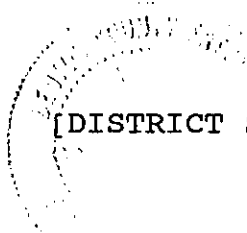


Michael Scott Rohrman, President

ATTEST:



Jerry Whitaker Peterman, Secretary



[DISTRICT SEAL]

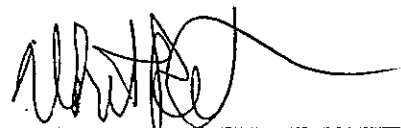
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COUNTY OF DENTON §

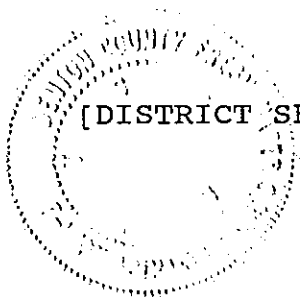
DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B §

I, the undersigned Secretary of the Board of Directors of Denton County Fresh Water Supply District No. 1-B, certify that the attached and foregoing is a true and correct copy of the ORDER ADOPTING CODE OF ETHICS, TRAVEL EXPENSE POLICY, INVESTMENT POLICY, POLICIES AND PROCEDURES FOR SELECTION AND REVIEW OF CONSULTANTS, POLICIES CONCERNING THE USE OF MANAGEMENT INFORMATION INCLUDING THE FORMATION OF AN AUDIT COMMITTEE, APPOINTMENT OF INVESTMENT OFFICER AND CHIEF FINANCIAL OFFICER AND CERTAIN OTHER MATTERS of said Board and an excerpt of the minutes of the meeting of the Board of Directors showing adoption and passage thereof; the original of said order and minute entry is on file in the District's office.

WITNESS MY HAND AND THE OFFICIAL SEAL OF THE DISTRICT this 18th day of October, 1995.



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Jerry Whitaker Peterman , Secretary



[DISTRICT SEAL]

ATTACHMENT "A"

CODE OF ETHICS

SECTION 1. Purpose. The Purpose of this Code of Ethics is to set forth the standards of conduct and behavior for the members of the Board of Directors of DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B (the "District"), and its officers, employees, and persons handling investments for the District (collectively with the Directors, the "District Officials") in accordance with Chapter 171, Local Government Code, as amended.

SECTION 2. Conflicts of Interest. A Director will abstain from participating in a vote or decision on a matter involving a business entity in which the Director has a substantial interest if it is reasonably foreseeable that an action on the matter would confer an economic benefit on the business entity. A Director will abstain from acting as a surety for a business entity that has work, business, or a contract with the District. A Director will abstain from acting as a surety on any official bond required by an officer of the District. For these purposes, a person is considered to have a "substantial interest" in a business if (1) he owns 10% or more of the voting stock or shares of the business entity or owns either 10 percent or more or \$5,000 or more of the fair market value of the business entity; or (2) funds received from the business exceed 10% of his gross income for the previous year. A person has a substantial interest in real property if the interest is an equitable or legal ownership with a market value of \$2,500 or more. A Director is considered to have a substantial interest for these purposes if a person related to the Director within the first degree of affinity or consanguinity, as determined under Chapter 573, Government Code, has a substantial interest as defined herein.

ATTACHMENT "B"

TRAVEL EXPENSE POLICY

SECTION 1. Purpose. The purpose of this Travel Expense Policy is to set forth the policies of DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B (the "District") concerning travel expenses for members of the Board of Directors of the District at all meetings other than Board meetings.

SECTION 2. Attendance at Meetings. Attendance at conferences, hearings, or other meetings outside the Metroplex or Denton County area by the members of the Board of Directors must be sanctioned by the Board of Directors; attendance at local meetings will be at each Director's discretion, however, such local meetings must relate to the business of the District. Following the meeting, Directors attending any meeting shall report to the Board concerning the meeting.

SECTION 3. Meeting Expenses Outside of Metroplex or Denton County. The District will pay Directors a per diem of \$100 per day for days of the meeting and a per diem of \$100 for one travel day. At sanctioned meetings, the District will pay the single room rate for the hotel at which the meeting is being held or any other comparable hotel. For travel connected with attendance at a sanctioned meeting, the District will pay round trip mileage at the current IRS mileage rate for travel by car or round trip airfare at current commercial rates for standard (not first class) airfare.

SECTION 4. Meeting Expenses for Local Meetings. The District will pay Directors a per diem of \$100 per day for the days of the meeting only.

SECTION 5. Reimbursement. Directors attending meetings will submit an itemized expense report to the Bookkeeper of the District before reimbursement is made. The Bookkeeper will submit such expense report to the Board of Directors for approval. Items on the expense report shall include lodging, meals, reasonable tips, and transportation. Reimbursement for meals will be limited to \$50 per day. Directors sharing expense items may split reported expenses in any matter they deem equitable, but the Board will pay no more than 100% of the actual total cost of reimbursable items.

SECTION 6. Extraordinary Expenses. Any extraordinary expenses for a Director attending a sanctioned meeting must be approved by the Board prior to incurring the expense.

ATTACHMENT "C"  
INVESTMENT POLICY

INVESTMENT POLICY AND STRATEGY  
FOR DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B

I. General Policy

It is the policy of the Denton County Fresh Water Supply District No. 1-B (the "District") to invest public funds in a manner which will provide the maximum security of principal while meeting the daily cash flow demands of the District and achieving a reasonable rate of return while conforming to all state statutes and District regulations governing the investment of public funds.

II. SCOPE

This investment policy applies to all financial assets held directly by the District. These financial assets are accounted for in the District's annual financial reports and include all moneys in the following funds:

- General Fund
- Debt Service Fund
- Capital Projects Fund
- Debt Service Reserve Fund
- Any new fund created by the governing body

Financial assets of the entity held and invested by trustees or fiscal agents are excluded from these policies; however, such assets shall be invested in accordance with state laws applicable to the investment of local government funds and in accordance with the District's primary investment objectives.

III. INVESTMENT OBJECTIVES

The District's primary investment objectives, in order of priority, are the following:

- A. Safety. Safety of principal is the foremost objective of the District's investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. To attain this objective, diversification is required in order that potential losses on individual securities do not exceed the income generated from the remainder of the portfolio.
- B. Liquidity. The District's investment portfolio shall remain sufficiently liquid to enable the District to meet all operating requirements which might be reasonably anticipated.

- C. Return on Investment. The District's investment portfolio shall be designed with the objective of attaining a market rate of return throughout the budgetary and economic cycles, taking into account the District's investment risk constraints and the cash flow characteristics of the portfolio.

#### IV. INVESTMENT AUTHORITY

Management responsibility for the District's investment program is hereby delegated to the District's Bookkeeper. The Bookkeeper shall designate an individual within such firm to serve as the District's Investment Officer and so notify the District in writing, as to such individual's name, along with a certification that such individual has completed the investment training as required by Chapter 2256 of the Government Code, as may be amended from time to time. The Chief Financial Officer shall have the authority, subject to the approval of the governing body, to establish additional specific written procedures for the operation of the investment program which are consistent with this investment policy. The procedures shall include explicit delegation of authority, if any, to persons responsible for investment transactions. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the Chief Financial Officer. The Investment Officer shall be ultimately responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials and employees. The controls shall be designed to prevent and control losses of public funds arising from fraud, employee error, misrepresentation by third parties, unanticipated changes in financial markets or imprudent actions by officers and employees. The Investment Officer shall maintain all records related to the entity's investment program.

#### V. PRUDENT PERSON RULE

The actions of the Investment Officer in the performance of his or her duties as manager of the District's funds shall be evaluated using the "prudent person" standard. Investments shall be made with judgment and care under prevailing circumstances which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment considering the probable safety of their capital as well as the probable income to be derived.

The Investment Officer acting in accordance with written procedures and exercising due diligence shall be relieved of personal responsibility for an individual security's



performance provided that deviations from expectations are reported in a timely fashion to the governing body and appropriate action is taken to control adverse developments.

#### VI. AUTHORIZED INVESTMENTS

At such time as the District has funds available for investment, such funds shall be invested in accordance with this policy and all applicable state statutes only in the following types of investment instruments:

##### Authorized Investment Instruments

1. Obligations of the United States and of its agencies and instrumentalities.
2. Direct obligations of the State of Texas or its agencies and instrumentalities.
3. Obligations of any corporation of the United States government, including, but not limited to:
  - a. Federal Home Loan Mortgage Corporation;
  - b. Federal Farm Credit Banks;
  - c. Bank of Cooperatives;
  - d. Federal Intermediate Credit Banks;
  - e. Federal Land Banks;
  - f. Federal Home Loan Banks; and
  - g. Federal National Mortgage Association.

Collateralized mortgage obligations secured by or a derivative of securities issued by the above-listed or any other entities are permitted only within certain restrictions more fully described by the Public Funds Investment Act, Chapter 2256, Texas Government Code, as amended by HB 2459.

4. Certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution domiciled in the State of Texas which are insured by the Federal Deposit Insurance Corporation or similar entity or its successor or which are collateralized, to the extent uninsured by the instrument described in (1), (2) or (3) set forth above.
5. Repurchase agreements with a defined termination date, secured by obligations set forth in No. 1 above and placed through a primary government securities dealer or a financial institution doing business in Texas.

6. Bankers' acceptance with a stated maturity of 270 days or less which will be liquidated in full at maturity and which meet certain other requirements.
7. Money market mutual funds which are no-load and are:
  - a. regulated by the Securities and Exchange Commission (SEC);
  - b. have an average weighted maturity of 90 days or fewer; and
  - c. has an investment objective of maintaining a stable net asset value of \$1 per share
8. Other types of mutual funds which are no-load and:
  - a. are registered with the SEC;
  - b. have an average weighted maturity of less than two (2) years;
  - c. are invested exclusively in obligations approved by this Act;
  - d. have a "AAA" rating; and
  - e. meet certain requirements of investment pools.
9. Securities issued by a state or local government, or any instrumentality or agency thereof, in the United States, and rated in one (1) of the three (3) highest categories by a nationally recognized rating agency.
10. Public Funds investment pools which strive to maintain a stable \$1.00 net asset value and maintain either a "AAA" or "AAA-m" rating from a national-recognized rating agency.

The District shall take all prudent and necessary measures consistent with its investment policy to correct any deviation from the minimum rating requirements of certain investments described above should a change in rating occur.

#### VII. DIVERSIFICATION OF INVESTMENTS

The District recognizes that some level of risk is inherent in any investment transaction. Losses may be incurred due to issuer default, market price changes, or closing investments prior to maturity due to unanticipated cash flow needs. Diversification of the District's investment portfolio by institution, type of investment, instrument, and term to maturity is the primary method to minimize investment risk.

## VIII. INVESTMENT STRATEGY BY FUND

1. Debt Service Funds - The District shall maintain as its primary objective to maximize the suitability of the investment in such funds to the financial requirements of the District, while preserving the safety of principal with regard to all monies collected or allocated for debt service. Secondly, the District will seek to maximize the return on such funds while insuring sufficient funds for timely payments of its obligations.

In order to accomplish this, the District will invest such funds in amounts and maturity dates that most likely match the debt service requirements of the District, taking into account the need for liquidity, marketability if the need arises to liquidate, diversification and yield.

2. Operating Fund - The District shall maintain as its primary objective to maximize the suitability of the investment in such funds to the financial requirements of the District, while preserving the safety of principal with regard to all monies collected or allocated for debt service. Secondly, the District will seek to maximize the return on such funds while insuring sufficient funds for timely payments of its debt obligations.

In order to accomplish this, the District will maintain adequate balances in short-term investments with necessary liquidity to ensure that sufficient funds are available for the continued operations of the District. Funds will not be invested in securities with stated maturities that exceed the reasonable expected expenditure time period. This strategy is intended to ensure that the District will avoid liquidating all or part of its investments in uncertain market conditions.

3. Debt Service Reserve Funds - Investment strategies for debt service reserve fund shall have as the primary objective to maximize the suitability of the investment in such funds to the financial requirements of the District, while preserving the ability to generate a dependable revenue stream to the appropriate debt service fund from securities with a low degree of volatility. Except as may be required by the bond ordinance specific to an individual issue, securities should be of high quality, with short to intermediate term maturities. Volatility shall be further controlled through the purchase of securities carrying the highest coupon available within the desired

maturity and quality range, without paying a premium, if at all possible. Such securities will tend to hold their value during economic cycles.

4. Capital Improvement Fund - The District may choose to have a capital improvement fund or capital projects fund from time to time and, if so, shall maintain as its primary objective to maximize the suitability of the investment in such funds to the financial requirements of the District while preserving the safety of principal with regard to all monies collected or allocated for such fund. Secondly, the District will seek to maximize the return on such funds while insuring sufficient funds for timely payments of its budgeted capital obligations.

In order to accomplish this the District will maintain adequate balances in short-term investments with necessary liquidity to ensure that sufficient funds are available for the capital programs of the District. Funds will not be invested in securities with stated maturities that exceed the reasonable expected expenditure time period. This strategy is intended to ensure that the District will avoid liquidating all or part of its investments in uncertain market conditions.

To the extent possible, the District will attempt to match its investments with uninterrupted cash flow requirements. Unless matched to a specific cash flow need, the District's funds should not, in general, be invested in securities maturing more than 10 (ten) years from the date of purchase.

#### **IX. AUTHORIZED FINANCIAL DEALERS AND INSTITUTIONS**

The District's Investment Officer shall maintain a list of financial institutions authorized to provide investment services to the District. In addition, a list shall be maintained of approved security brokers/dealers who maintain an office in the State of Texas.

All financial institutions and broker/dealers who desire to provide investment services to the District shall execute a written statement stating that an authorized principal of the business has received and thoroughly reviewed the investment policy and that reasonable procedures and controls have been implemented to preclude imprudent investment activities. Additionally, these firms should supply the District's Investment Officer with information sufficient to adequately evaluate the institution and answer any and all inquiries posed by the District's Investment Officer or the governing body, including the following information:

- A. Audited financial statements.
- B. Regulatory reports on financial conditions.
- C. Written memorandum of Agreement for the deposit of public funds or trading resolution, as appropriate.
- D. Proof of National Association of Security Dealers certification and proof of state registration.
- E. Any additional information considered necessary to allow the District's Investment Officer to evaluate the credit worthiness of the institution.

The District's Investment Officer shall evaluate the financial capacity and credit worthiness of financial institutions and broker/dealers prior to the placement of the District's funds. The District's Investment Officer shall conduct an annual review of the financial condition and registrations of financial institutions and broker/dealers and, based on the review, make any recommendations regarding investment policy or program changes determined to be necessary.

**X. SAFEKEEPING AND CUSTODY**

To protect against potential fraud and embezzlement, investment assets shall be secured through third-party custody and safekeeping procedures. Bearer instruments shall be held only through third-party institutions. The District's Investment Officer and any other officers or employees of the District authorized to engage in investment transactions shall be bonded in an amount established by the governing body. Collateralized securities, such as repurchase agreements shall be purchased using the delivery vs. payment procedure. Money market mutual funds used for investments must provide for independent custodians of their portfolios and delivery vs. payment on their portfolio securities. Once sufficient funds are on hand to warrant an annual audit of the District's records, the safekeeping procedures utilized in the District's investment program shall be reviewed annually by the independent auditor.

**XI. COLLATERAL**

Except as set forth in subsection B of this section, it is the policy of the District to require that all cash and investments maintained in any financial institution names as a depository be collateralized. In order to anticipate market changes and provide a level of security for all funds, the collateralization level shall be 100% of the market value of principal, plus accrued interest. Collateral shall be limited to the types of instruments authorized as collateral for public funds.

Collateral shall always be held by an independent third-party custodian with whom the District has a current custodial agreement. A clearly marked evidence of ownership (safekeeping receipt) must be supplied to the District and retained by the District's Investment Officer. The right of collateral substitution is hereby granted.

## **XII. INVESTMENT REPORTING**

At the current time only minimal operating funds are on hand in the District's operating account; however, in conjunction with the levy of the District's first tax rate or at any time the deposits in the District's operating or other accounts exceeds \$10,000, the District's Investment Officer shall prepare and submit to the governing body at least quarterly a report regarding the status of the entity's investment program. As to each investment, the report shall include the following information:

- A. Name of financial institution from which the investment was purchased or in which assets are deposited.
- B. Type of investment.
- C. Certificate or other reference number, if applicable.
- D. Percentage yield on an annualized basis.
- E. Purchase date, purchase price and maturity date.
- F. Current market value of the investment.

In addition, the report shall explain the quarter's total investment return and compare the return with budgetary expectations.

The quarterly report shall also summarize recent market conditions, economic developments and anticipated investment conditions, and indicate any areas of policy concern and suggested revisions of investment strategies. Copies of the report shall be submitted to each member of the governing body and the chief executive officer of the District.

## **XIII. AUDIT**

In connection with the audit of the District's funds conducted by an independent certified public accountant, the auditor shall conduct a review of the District's investment program, including internal controls and procedures, and the results of the reviews, including recommended changes, shall be included in the District's audit.

#### XIV. INVESTMENT POLICY ADOPTION

The District's investment policy shall be adopted by order of the governing body and shall become effective on the date set forth in the order. The policy shall be reviewed annually and revised, as appropriate. Any amendments to this policy must be made by order of the governing body.

Any investment held on the date of initial adoption of this policy which does not meet the guidelines of this policy shall be exempted from its provisions. At maturity or liquidation, the monies so invested, if reinvested, shall be reinvested only in accordance with this policy. The District's Investment Officer may take a reasonable period of time to adjust the existing portfolio to the provisions of this policy in order to avoid the premature liquidation of any current investment.

CERTIFICATION

I hereby certify that I have received and thoroughly reviewed the investment policy of Denton County Fresh Water Supply District No. 1-B ("District") and have implemented reasonable procedures and controls designed to preclude imprudent investment activities arising out of investment transactions conducted between this firm and the District. Transactions between this firm and the District will be directed towards protecting the District from credit or market risk.

All the sales personnel of this firm dealing with the District's account have been informed and will be routinely informed of the District's investment horizons, limitations, strategy and risk constraints, whenever we are so informed.

This firm pledges due diligence in informing the District through its duly appointed Chief Financial Officer and its duly appointed Investment Officer of foreseeable risks associated with financial transactions connected to this firm.

\_\_\_\_\_  
(Firm)

\_\_\_\_\_  
(Signature of Registered Principal)

\_\_\_\_\_  
(Name)

\_\_\_\_\_  
(Title)

\_\_\_\_\_  
(Date)

Notification Phone Nos. & Addresses of officers of the District:

Chief Financial Officer  
\_\_\_\_\_, Treasurer  
Denton County Fresh Water  
Supply District No. 1-B

Investment Officer  
\_\_\_\_\_  
Murtle Cruz Incorporated  
1621 Milam, 3rd Floor  
Houston, Texas 77002-8017  
(713) 759-1368

\_\_\_\_\_  
(214) \_\_\_\_\_



ATTACHMENT "D"

POLICY CONCERNING SELECTION, MONITORING,  
REVIEW, AND EVALUATION OF PROFESSIONAL CONSULTANTS

SECTION 1. Purpose. The purpose of this Policy Concerning Selection, Monitoring, Review, and Evaluation of Professional Consultants is to set guidelines for the Board of Directors for DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B (the "District") concerning its Professional Consultants.

SECTION 2. Definition of Professional Consultant. "Professional Consultant" shall include the District's attorney, auditor, manager, financial advisor, engineer, tax assessor/collector, development consultant and such other consultants other than employees that the District may hereafter engage.

SECTION 3. Selection of Consultants. Whenever the Board of Directors of the District decides to terminate the services of one or more of its Professional Consultants, the Board shall solicit proposals and shall appoint a committee of two Directors to review any proposals received by the Board, to interview applicants if deemed necessary by such committee, and to make a recommendation to the entire Board of Directors concerning the selection.

SECTION 4. Monitoring of Professional Consultants. For those Professional Consultants with annual contracts, the Board of Directors of the District will review the performance of the Professional Consultants for the prior year at the time the contract is renewed. The Board of Directors shall review the performance of its other Professional Consultants in connection with the review of its annual financial report or annual audit.

## ATTACHMENT "E"

### POLICIES RELATING TO USE OF MANAGEMENT INFORMATION AND FORMATION OF AN AUDIT COMMITTEE

SECTION 1. Purpose. The purpose of this Policy Relating to Use of Management Information and Formation of an Audit Committee for DENTON COUNTY FRESH WATER SUPPLY DISTRICT NO. 1-B (the "District") is to provide written policies concerning use of management information.

SECTION 2. Annual Budgets. Prior to each fiscal year, the Board of Directors of the District shall adopt an annual budget in which revenues are anticipated for the next fiscal year for use in planning and controlling of costs and shall compare the actual revenues and expenditures of the District to the budgeted revenues and expenditures on a semiannual basis or more frequently if warranted. This annual budget shall cover operations expenses and revenue as well as debt service expenses and revenue.

SECTION 3. Audit Committee. At such time as the District is required to conduct annual audits, the District hereby appoints its Board of Directors as an audit committee, or any two such members of the Board that the Board may appoint from time to time to review the annual audit prepared by the District Auditor.

SECTION 4. Accounting Standards. At such time as the District is required to conduct annual audits, the District hereby directs its auditor to adopt uniform auditing reporting requirements that use "Audits of State and Local Governmental Units" as a guide on audit working papers and that uses "Governmental Accounting and Financial Reporting Standards" and any further standards as may be required by the Texas Natural Resource Conservation Commission, Commission rules or State statutes as may be amended from time to time.