

TO: James L. App, City Manager
FROM: Mike Compton, Director of Administrative Services
SUBJECT: Long-term Financing for Wastewater Collection and Treatment Plant Improvements
DATE: September 17, 2002

Needs: For the City Council and Public Financing Authority to consider approval of various documents for the long-term financing of wastewater collection and treatment facility improvements.

Facts:

1. The Council has been previously informed by staff of the need to expand the capacity of the Templeton interceptor line, not for the benefit of TCSD but to serve Theatre Drive within Paso Robles.
2. Public Works construction contracts have been issued for these improvements.
3. Within the last year or so, it was determined that the solids handling capacity of the treatment plant is also nearing capacity.
4. The estimated cost to undertake both the collection and treatment plant improvements, just noted above, is estimated at \$8 million.
5. The Council has been previously advised that the City does not have existing resources to cover the \$8 million and issuing long-term financing debt was the only alternative to doing nothing.
6. In December 2001, the Council approved increased sewer user fees that anticipated that issuance of long-term debt financing.
7. Generally, the rating agencies and bond trustee requires 125% coverage ratio. In other words, operating revenues must exceed operating expenses including the new debt service by 25%.
8. The sewer user fee increase approved by the Council last December provided for a phasing of the increase and a significant delay in the implementation of the first annual CPI adjustment.

9. In order to mitigate potential concerns of the rating agencies and bond trustee, it is desirable to escalate the first CPI adjustment from July 1, 2005 to July 1, 2004. This shortens the time period between the last of three phased increases to the first CPI escalation from 18 months to 6 months.
10. Given that interest rates are at historical lows, staff is proposing to include the re-financing of the existing 1993 Sewer Refunding Bonds in the issuance of the new debt .

Analysis
and
Conclusion:

As noted above, long-term interest rates are at historical lows. Issuing debt in this market will provide considerable savings over initial debt service cost estimates. Lower interest rates also provides sufficient savings to re-finance the 1993 Sewer Revenue Refunding Bonds (a re-funding of the 1987 Sewer Revenue Bonds). The estimated savings over the remaining life of the current bonds is \$125,000. To re-finance the current bonds, the City will issue \$3,250,000 in refunding debt.

The City's financial advisor, Craig Hill of Northcross, Hill & Ach, is working with MBIA Insurance Corporation to eliminate the requirement for a reserve fund. Rather than establish a \$1.2 million reserve fund, the City would insure the bond issue. The purpose would be to reduce the amount of bonds to be issued in order to save interest and issuance costs. If successful, the total bond issue would be about \$11.5 million. Staff has even gone as far as suggesting that should insurance not be available or too expensive, the City would fund the reserve from existing resources. However, just to be conservative and assume the worst case scenario, the documents presented to Council will identify "an amount not to exceed \$13 million".

The debt financing will be called "2002 Installment Sale Sewer Revenue Bonds". An installment sale financing is a blend of a straight revenue bond issue and a certificate of participation (COP). By way of explanation, a revenue is a pledge (guarantee) of a revenue stream usually user fees while a COP is a lease-purchase obligation wherein the asset purchased or improvements undertaken becomes the property of a third party as collateral. If the entity did not make lease payments, the third party could, theoretically, sale the asset to pay off bond holders

An installment sale financing provides a higher degree of fiscal assurances to the bond holders, rating agencies and trustee because it is backed by both a revenue stream and the improvements as "collateral". However, as people will note, it is a complicated type of financing. As described in the previous paragraph, the Public Financing Authority (PFA) will be used as the "third party" to whom ownership of the improvements will be transferred. The PFA will then lease back use of the improvements to the City. The lease payments will then be used by the PFA to pay principal and interest to the bond holders.

This type of financing will require the City and the PFA to approve/adopt the following documents:

Acquisition Agreement – Transfers ownership of the improvements to the PFA.

Installment Sale Agreement – Establishes the requirement of the City to lease or buy back the improvements over time. The City's payments to the PFA are then used by PFA to make debt service payments to the bond holders via the trustee.

Escrow and Trust Agreement - Establishes the escrow account for the refunding of the 1993 Sewer Refunding Bonds for which the trustee will pay bondholders for the old debt.

Indenture of Trust Agreement – Establishes the requirement of the PFA to forward installment sale payments received from City to the trustee in order to make principal and interest payments to the bond holders.

Approval of the above noted documents is accomplished via the adoption of two ordinances, one each for the City and the PFA. For those councilmen unfamiliar with the PFA, the PFA was established by the Council in 1993 as a conduit for the combined financing of the city hall/library facility and the refinancing of the Centennial Park construction debt. The Council sits as the board for the PFA much like it does for the Redevelopment Agency. The sole purpose of the PFA is to be conduit and provide flexibility for certain types of long-term financing. In the case of lease-purchase and/or lease installment financings, the trustee is not desirous of holding title to City improvements or facilities. The creation of the this separate, legal, third party agency performs this function to the satisfaction of all interested parties; i.e. bond rating agencies, bond holders and trustee.

To provide additional assurances to the bond holders, rating agencies and trustee that the City is capable of meeting debt service obligations and the 125% coverage ratio, staff is recommending that the Council amend the user fee ordinance to accelerate the first annual CPI adjustment from July 1, 2005 to July 1, 2004.

The Council will no doubt notice that many of the issuing documents have blank spaces and appear incomplete. This is because many of the blanks can not be filled in until such time as the financing is complete and the data/info is known. The ordinances generally ask the Council to approve documents "as to form".

Fiscal
Impact:

It is estimated that the annual debt service would be about \$1.2 million annually through fiscal year 2008. The refunding bonds would be entirely repaid by the end of fiscal year 2008 at which time the annual debt service would decline to about \$610,000.

Options:

- a(1)** That the **COUNCIL** take the following actions:
1. Introduce for first reading Ordinance No. XXX N.S. authorizing:
 - a) The installment purchase of certain sewer improvements for the El Paso de Robles Public Financing Authority;
 - b) Authorizing and directing the execution of an acquisition agreement and an installment sale agreement;
 - c) Approving the sale of 2002 Installment Sale Revenue Bonds (Sewer Enterprise) by the Authority;
 - d) Authorizing official actions; and
 2. Introduce for first reading Ordinance No. XXX N.S amending Section 14.04.020 of the City of El Paso de Robles to adjust Sewer User Fees .
- a(2)** The the **PUBLIC FINANCING AUTHORITY** introduce for first reading Ordinance No. XXX N.S:
- a) Authorizing the issuance of not to exceed \$13,000,000 principal amount of 2002 Installment Sale Revenue Bonds (Sewer Enterprise) relating to certain sewer improvements and the refunding of the 1993 El Paso de Robles Public Financing Authority Sewer Revenue Bonds, Series A;
 - b) Authorizing and directing the execution of a related indenture of trust, installment sale agreement and escrow deposit and trust agreement;
 - c) Authorizing the sale of 2002 Installment Sale Revenue Bonds (Sewer Enterprise);
 - d) Approving an official statement, an official notice of sale and an official bid form; and
 - e) Authorizing official actions.
- b.** Amend, modify, or reject the above option.