



REPORT TO MAYOR AND CITY COUNCIL

AGENDA ITEM

TO: THE HONORABLE MAYOR
AND CITY COUNCIL

DATE September 2, 2008

SUBJECT: Issuance of Series 2008 Water Revenue Bonds to Fund Water
Enterprise System Capital Projects

Report in Brief

Certain capital projects associated with the Water Enterprise System need to be completed in a timely manner in order to keep the system functioning and meet mandated water meter installation deadlines. The resources necessary to complete these projects require the issuance of water revenue bonds that will generate a not to exceed amount of \$20,000,000. Actions that need the City Council's approval as described herein include adopting a resolution to that effect, approval of the forms and authorization of execution and delivery of an Installment Purchase Contract, a First Supplemental Installment Purchase Contract, a Trust Agreement, a First Supplemental Trust Agreement, the Preliminary Official Statement, the Notice of Sale, the Bond Purchase Contract and a Continuing Disclosure Certificate, and authorizing related actions and matters thereto.

Staff recommends that the City Council adopt Resolution No. _____ approving the issuance of the 2008 Water Revenue Bonds with a principal amount not to exceed \$20,000,000, approving the form and authorizing distribution of the official statement and other related documents.

Background

Several projects have been identified and analyzed by staff related to this financing effort. A number of presentations have been made to the public, the Infrastructure Committee, and the Council as a whole regarding the needs of the Water Enterprise System related to water supply, infrastructure maintenance, and the mandatory implementation of water meters. These projects include the following:

- Acquisition and Installation of Water Meters (post January 1, 1992 construction)
- Demolition of an existing water storage tank, construction of an approximately 400,000 gallon replacement water storage tank and related service lines and pipes

- Acquisition and Installation of a Supervisory Control and Data Acquisition System (SCADA) radio communication system
- Construction, Installation and Modification of wells

City water revenues are derived from three sources: (i) monthly service charges imposed, billed, and collected by the City; (ii) water service installation charges (connection fees and MPFP fees); and (iii) other miscellaneous sources, including interest income.

The current water system rate structure was approved by the City Council on June 7, 2005 and became effective July 1, 2005. This revenue stream is insufficient to provide funding for the above mentioned projects. The City has never issued bonds related to the Water Enterprise and this financing vehicle is recommended to provide the cash flow necessary to complete these projects within the prescribed timeframes. If approval is granted, the projects will be financed by the sale of Water Revenue Bonds issued by the Woodland Finance Authority. The City will pledge to make installment payments to the Authority from Net Revenues of the Water Enterprise defined as Gross Revenues less Operations & Maintenance (O&M). Gross Revenues include all revenues of the Enterprise including rate revenues, connection fees, Water MPFP fees charged to new development and other sources including interest income.

The City is currently under contract with HDR Engineering, Inc. to perform a water system rate study. This rate study will take into consideration a Net Revenue stream sufficient to cover debt service by at least 1.25 times and Net Revenues (excluding MPFP fees) sufficient to cover debt service by at least 1.00 times. The City will have the capacity to issue additional bonds in the future upon meeting certain tests described in the bond documents.

A financing team, consisting of Del Rio Advisors, LLC as Financial Advisor, Kronick, Moskovitz, Tiedemann & Girard as Bond Counsel, and Lofton & Jennings as Disclosure Counsel, has been assembled to prepare and present the 2008 Bonds to Council for approval.

Discussion

The issuance of water revenue bonds will provide the resources necessary to complete the identified projects in a timely manner. While bond financing is a commonly accepted practice for major projects, it is important to note that the current economic climate has generated a significant level of uncertainty in the municipal bond market over the last several months. At one time municipal finance authorities could solicit competitive bids from up to seven AAA bond insurance providers and the competition drove premiums lower and commoditized the bonds. This helped to reduce the cost of capital for issuers looking to acquire or construct projects. However, due to exposure to insured portfolios of mortgage obligations, five of the seven bond insurers have been downgraded one or more rating notches. As a result, the ongoing viability of the bond insurance business is now in question. The two remaining insurers, Assured Guaranty Corporation (AGC) and Financial Security Assurance (FSA), have now been placed on Negative Watch for possible downgrade by

Moody's Investors Service. Many issuers are bypassing bond insurance altogether and are issuing bonds based on the stand-alone rating of the public agency.

The financing team intends to pursue a bond rating from Standard & Poor's Corporation (S&P) and bond insurance from the two remaining AAA insurance providers. If the insurance is unavailable and/or too expensive, it is anticipated that the team will sell the bonds with a stand-alone rating from S&P. Currently, the sale is anticipated to be competitive using an online auction system called MuniAuction. The Woodland Finance Authority sold Lease Revenue Bonds in 2007 using this same system. The bonds are awarded to the firm showing the lowest true interest cost to the City. Should the stand-alone rating come in too low, the team anticipates recommending the hiring of an underwriter at that time to negotiate the sale directly to the buyers.

The following legal documents related to the Water Revenue Bonds, Series 2008 have been prepared in substantially final form and attached for Council and Authority review:

- **Installment Purchase Contract:** By and between the Woodland Finance Authority and the City of Woodland, whereby the City has determined to make certain improvements to its water system, and the Authority has agreed to finance the acquisition of those improvements and sell them to the City upon the terms and conditions set forth within the Agreement
- **First Supplemental Installment Purchase Contract:** Governs the terms and conditions related to sale of the 2008 Bonds specifically.
- **Trust Agreement:** This agreement between the Woodland Finance Authority and U.S. Bank National Association, as Trustee sets the conditions associated with the sale of respective series of Water Revenue Bonds.
- **First Supplement Trust Agreement:** Governs the terms and conditions of the City's relationship with U.S. Bank and the bondholders related to the sale of the 2008 Bonds specifically.
- **Preliminary Official Statement:** Primary marketing document describing the bonds and the Water Enterprise, used by bidders should the sale be competitive or sent directly to prospective bondholders by an underwriter chosen by the City should a negotiated sale be necessary. Upon the successful sale, a Final Official Statement will be sent to each bondholder who purchases the 2008 Bonds.
- **Notice of Sale:** If competitive sale method is chosen, this document is used to notify potential bidders of the date and time of the competitive sale.
- **Bond Purchase Contract:** If negotiated sale method is chosen, an agreement between an Underwriter (to be determined by the City) and the Woodland Finance Authority in connection with the sale and purchase of Water Revenue Bonds, Series 2008.

- **Continuing Disclosure Certificate:** document whereby the City agrees to provide continuing information to the bondholders related to the Enterprise operations and other matters.

Fiscal Impact

The City pledges to set rates sufficient enough to generate the necessary debt service coverage and meet all requirements identified in the documents related to the issuance of the Water Revenue Bonds, Series 2008. A rate study is currently underway which will account for the debt service requirements, and the rate structure resulting from that study will be presented to Council for review and approval subsequent to its completion early next calendar year.

Public Contact

Posting of the City Council Agenda.

Alternative Courses of Action

1. Adopt a resolution approving the issuance of the 2008 Water Revenue Bonds with a principal amount not to exceed \$20,000,000, approving the form and authorizing distribution of the official statement and other related documents as described herein.
2. Direct staff to seek alternative funding sources for the proposed Water Enterprise System projects, including well repair, water meter implementation and water storage tank replacement.

Recommendation for Action

Staff recommends that the City Council approve Alternative No. 1.

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Attachments