

BOARD LETTER APPROVAL


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DATE: July 20, 2018

SUBJECT: Initial Authorization to Issue up to \$1.113 Billion of Water System Revenue Bonds Under Resolution No. 4943

SUMMARY

Proposed Resolution No. 4943 will authorize the issuance of up to \$1.113 billion of fixed-rate tax-exempt Water System Revenue Bonds (Water Bonds) to finance a portion of the budgeted capital improvements for Fiscal Years (FYs) 2018-2019 and 2019-2020 including the related costs of issuance. The debt service on the Water Bonds will be covered by the multi-year rate increase approved by the City Council in March 2016 and became effective on April 15, 2016. The debt service on the Water Bonds will be payable out of the Water Revenue Fund.

Resolution No. 4943 is an initial resolution. A supplemental resolution, which provides additional information about the proposed Water Bond issuance, will be introduced at a subsequent Board meeting. Mayoral and City Council approvals are required pursuant to Section 609 of the Charter of the City of Los Angeles (Charter).

RECOMMENDATION

It is recommended that the Board of Water and Power Commissioners (Board) adopt Resolution No. 4943 authorizing the issuance of up to \$1.113 billion of Water Bonds per Charter Section 609.

ALTERNATIVES CONSIDERED

The LADWP has two sources for funding its capital improvements program: (1) directly through rates collected from customers and (2) borrowing from the capital market which is repaid from customer rate collections over time.

Collections directly from rates do not provide sufficient funding for the entire capital budget. Accordingly, it has been determined that public interest and necessity demand that LADWP borrow \$1.113 billion in this instance by issuing Water Bonds pursuant to Section 609 of the Charter for the purpose of financing a portion of the Water System's budgeted capital improvements for FYs 2018-2019 and 2019-2020.

FINANCIAL INFORMATION

As a fixed-rate issue, the total estimated cost for the \$1.113 billion Water Bonds, including principal and interest, is approximately \$2.2 billion over 30 years based on current interest rates for tax-exempt bonds. The debt issuance costs are estimated at \$4.5 million equivalent to 0.4 percent of the total bond issue which includes underwriters' discount, bond counsel, disclosure counsel, financial advisor, and rating agencies fees.

The Board adopted financial metrics to use for Water System financial plans as follows:

1. maintain a minimum debt service coverage at 1.7 times,
2. maintain a minimum operating cash target of the equivalent to 150 days of operating expenses, and
3. maintain a debt to capitalization ratio of less than 65 percent.

As of April 30, 2018, the Water System's liquidity is equivalent to approximately 265 days of operating expenses. The updated financial projection for fiscal year 2018, anticipates the debt service coverage to be at 2.0 times, and the debt to capitalization ratio to be at 63 percent. Attached is a historical financial overview of the Water System operating results and financial metrics.

BACKGROUND

Overview of Bond Funding Need

The Water System's FY 2018-2019 Budget, approved by the Board on May 22, 2018, and transmitted to City Council in accordance with Charter Section 684, reflects a need to borrow approximately \$305 million to support a portion of its planned \$891 million capital improvements program over the same period. Additionally, the multi-year financial plan, which supports the budget, indicates a need of approximately \$808 million external financing to support a portion of its planned \$1.2 billion capital improvements program for FY 2019-2020.

Proposed Resolution No. 4943 will authorize the issuance of up to \$1.113 billion of fixed-rate, tax-exempt Water System Revenue Bonds to finance a portion of the budgeted capital improvements for FYs 2018-2019 and 2019-2020, including the related costs of issuance. The combined two-year issuance authorization will provide LADWP the flexibility to better plan its issuances to meet the Water System's needs and mitigate interest costs given the rising interest rate environment.

The debt service on these Water Bonds will be funded by the multi-year rate increase approved by the City Council in March 2016 and became effective on April 15, 2016. The proceeds from the issuance of these bonds will be deposited into the Construction Fund of the Water System and would be drawn down to fund a portion of its capital improvements program.

Resolution No. 4943 is an initial resolution of the Board, setting forth the purpose for future indebtedness and establishing the maximum limit as to principal, interest costs, and term. Resolution No. 4943 also provides for the private sale of the Water Bonds to one or more of the firms included in the team of underwriting firms recently selected by the Board (in June 2018) pursuant to the Procedural Ordinance. At a future Board meeting, the Financial Services Organization will present a supplemental resolution that will authorize the specific terms and conditions for the Water Bonds, including the underwriting firms that will be selected from among LADWP's investment banking team members and the principal financing documents related to the Water Bonds.

Both LADWP's Interim Chief Financial Officer (CFO) and its financial advisor, the Public Resources Advisory Group (PRAG) recommend the Water Bonds be sold on a negotiated basis (i.e., private sale). The CFO's Report in connection with the proposed private sale, as required by Charter Section 609, is attached. Also attached is the report setting forth PRAG's opinion with respect to a private sale.

Ordinance No. 182138 requires investment banks to disclose their corporate citizenship which shall include their participation in charitable programs or scholarships within the City of Los Angeles (City of LA) and internal policies regarding utilization of subcontractors which are designated as small business and disabled veteran business enterprises. All of the 19 investment banks that are in LADWP's current Pool of Underwriters are in compliance with Ordinance No. 182138. Their current disclosures are posted in the City of LA's website at <http://cao.lacity.org/RBO/>.

In accordance with the Mayor's Executive Directive No. 4, the City Administrative Officer's (CAO) Report is attached.

ENVIRONMENTAL DETERMINATION

Determine item is exempt pursuant to California Environmental Quality Act (CEQA) Guidelines 15060 (c)(3). In accordance with this section, an activity is not subject to CEQA if it does not meet the definition of a project. Section 15378 (b)(4) states that the creation of government funding mechanisms or other fiscal activities which do not involve any commitment to any specific project which may result in direct or indirect physical changes in the environment does not meet that definition. Therefore the issuance of an Initial Authorization for the issuance Water System Revenue Bonds is not subject to CEQA.

CITY ATTORNEY

The Office of the City Attorney reviewed and approved Resolution No. 4943 as to form and legality.

ATTACHMENTS

- Resolution
- CFO Report
- PRAG's letter on Negotiated Bond Sale
- Water System Financial Overview
- CAO Report