


0220-05209-0004

TRANSMITTAL

TO David H. Wright, General Manager Department of Water and Power	DATE 7/12/18	COUNCIL FILE NO.
FROM The Mayor	COUNCIL DISTRICT	

AUTHORITY TO ISSUE \$1.113 BILLION IN WATER SYSTEM REVENUE BONDS

Approved and transmitted for further processing including Council consideration.
See the City Administrative Officer report attached.


(Ana Guerrero) for
MAYOR

REPORT FROM

OFFICE OF THE CITY ADMINISTRATIVE OFFICER

Date: July 10, 2018

CAO File No. 0220-05209-0004

Council File No. --

Council District: --

To: The Mayor

From: Richard H. Llewellyn, Jr., City Administrative Officer

Reference: Communication from the Department of Water and Power dated June 20, 2018

Subject: **AUTHORITY TO ISSUE \$1.113 BILLION IN WATER SYSTEM REVENUE BONDS**

RECOMMENDATIONS

That the Mayor:

1. Approve the proposed Resolution 4943 authorizing the Department of Water and Power (DWP) to issue up to \$1.113 billion in Water System Revenue Bonds to fund a portion of the Water System Capital Improvements Program for Fiscal Years 2018-19 and 2019-20 in accordance with the provisions of City Charter Section 609 and Article 6.5 of the Los Angeles Administrative Code Sections 11.28.1 – 11.28.9; and,
2. Return the proposed resolution to the Department for further processing, including Council consideration.

SUMMARY

DWP intends to issue bonds to finance a portion of its Water System Capital Improvements Program (CIP) which is \$0.891 billion in Fiscal Year (FY) 2018-19 and \$1.197 billion in FY 2019-20. Approval of the proposed resolution is intended by DWP to represent an 'initial resolution' of the Board, which sets forth the purpose for future indebtedness and establishes the maximum limits for this issuance as follows:

- The maximum principal is \$1.113 billion;
- The maximum term of the debt is 45 years from the date of issuance;
- The maximum interest cost to be incurred through the issuance of bonds is 12 percent.

The maximum legally permissible interest cost that could be incurred through the issuance of the bonds is 12 percent per annum consistent with California Code Section 53531. DWP expects that the current market conditions will provide an interest cost in the range of 4.0 to 5.5 percent.

The proposed resolution also authorizes the private sale of the bonds to one or more underwriting firms selected by the DWP Board of Commissioners (Board) pursuant to City

Charter Section 609(d) and Los Angeles Administrative Code (LAAC) Section 11.28.4 (the Procedural Ordinance) governing proprietary department bond resolutions.

The \$1.113 billion bond issuance will be funded by the multi-year rate increase approved by the City Council in March 2016, effective on April 15, 2016. The bonds will be Water Revenue Fund obligations and will not constitute an obligation of the City or the General Fund.

The City Attorney has approved the proposed resolution as to form and legality. In compliance with the Responsible Banking Ordinance No. 182138 (RBO), DWP's Pool of Underwriters have disclosed, or are in the process of disclosing, their involvement in charitable programs or scholarships within the City of Los Angeles and internal policies regarding use of subcontractors designated as small business and disabled veteran business enterprises.

Background information relating to this request is provided in the attached Appendix.

FISCAL IMPACT STATEMENT

Approval of the proposed resolution will impact the DWP Water Revenue Fund. There is no fiscal impact to the City General Fund.

RHL:RR:10180100

Attachment

APPENDIX

In order to support the CIP for FY 2018-19 and FY 2019-20, DWP proposes the use of external financing with bonds and internally generated funds. The Water System FY 2018-19 CIP includes approximately \$305 million of tax-exempt revenue bonds to support a portion of the \$891 million program. Additionally, the multi-year financial plan for FY 2019-20 CIP includes approximately \$808 million of external financing to support a portion of the \$1.197 billion program.

The CIP for FY 2018-19 and FY 2019-20 is illustrated in the table below:

	FY 2018-19 (\$millions)	FY 2019-20 (\$millions)	Total (\$millions)
Water Quality Improvements			
WQIP Reservoir Improvements	\$97	\$56	\$153
WQIP Trunkline Improvements	63	113	176
Groundwater Remediation and Clean Up	79	115	194
Chloramination Station Installations and Water Treatment Improvements	39	50	89
Meter Replacement Program	16	17	33
Water Quality Improvements	\$294	\$351	\$645
Water Supply			
Water Recycling	\$37	\$65	\$102
Watershed - Stormwater Capture	27	32	59
Groundwater, LA Aqueduct, and Water Conservation	79	84	163
Water Supply	\$143	\$181	\$324
Water Infrastructure Programs			
Distribution Mains, Trunkline, and Major System Connections	\$194	\$264	\$458
WSO Facilities, Pump Stations, and Infrastructure Reservoir Improvements	47	74	121
Services, Meters, and Hydrants	56	56	112
Infrastructure Support, Regulator Stations and Seismic Improvements, WSO Information Technology, Resource Development, and Tools and Equipment	34	63	97
Water Infrastructure Programs	\$331	\$457	\$788
Regulatory Compliance - Owens Valley			
Owens Valley Dust Mitigation	27	22	49
Owens Lake Master Project	12	102	114
Regulatory Compliance-Owens Valley	\$39	\$124	\$163
Operating Support			
Water System's share of Joint Capital including Customer Service	\$84	\$84	\$168
Operating Support	\$84	\$84	\$168
Total Water System CIP			
	\$891	\$1,197	\$2,088
Proposed External Financing with Water Revenue Bonds			
	\$305	\$808	\$1,113

Capital Program Financing

The DWP Board establishes the financial planning criteria utilized by the Department. On May 21, 2009, the DWP Board adopted financial planning criteria to maintain:

- A minimum debt service coverage of 2.0 times;
- An operating cash target of \$200 million; and,
- A capitalization ratio of less than 60 percent.

On May 20, 2014, the Board revised the financial planning criteria to maintain:

- A minimum debt service coverage of 1.7 times;
- An operating cash target of 150 days; and,
- A capitalization ratio of less than 65 percent.

The following table illustrates the Water System's actual financial performance since 2010.

Financial Performance	2010	2011	2013	2013	2014	2015	2016	2017
Debt Service Coverage	2.0	1.7	1.8	2.2	2.1	1.9	2.0	1.7
Oper Cash Target (\$,000)	\$203,365	\$240,546	\$329,803	\$448,945	\$369,809	187 days	172 days	191 days
Capitalization Ratio	54%	58%	57%	58%	60%	62%	64%	64%

Financial data used for calculation is based on audited financial statements and official statements.

Charter Section 609 Compliance

Charter Section 609 requires approval by the Mayor and Council for the issuance of debt by the proprietary departments. The City's Debt Management Policy states the issuance of debt shall be through a competitive sale whenever feasible, however, Charter Section 609(d) allows the private sale of bonds subject to the following conditions:

- The DWP Board has authorized the sale of bonds pursuant to private sale after written recommendation of the Chief Financial Officer (CFO) stating the reasons why a private sale will benefit DWP;
- The Council, after receiving a report from the City Administrative Officer, has approved the sale; and,
- The Council is provided an opportunity, as set forth in the Procedural Ordinance, to disapprove the selection of the underwriting firm(s) for the private sale of bonds.

Pursuant to the Procedural Ordinance, the recommendations for private bond sale (Attachments) have been made by both the DWP's CFO and by its financial advisor, the Public Resources Advisory Group (PRAG). Accordingly, DWP requests authority to conduct private, negotiated sales of bonds to one or more investment banking firms. The table below lists the firms approved by the DWP Board on June 26, 2018, to serve as the DWP's underwriting team for a three year duration expiring in June 2021. DWP will select from the approved team of underwriters for each

individual bond issuance.

DWP Selected Underwriting Team

SENIOR MANAGERS	CO-MANAGERS
Bank of America Merrill Lynch ^(A)	Academy Securities, Inc.
Barclays Capital Inc.	Cabrera Capital Markets, LLC
Citigroup Global Markets Inc.	FTN Financial Capital Markets
Goldman, Sachs & Co.	J.P. Morgan Securities LLC
RBC Capital Markets, LLC	Jefferies LLC
Samuel A. Ramirez & Co., Inc.	Loop Capital Markets LLC
Siebert Cisneros Shank & Co., LLC	Morgan Stanley & Co. LLC
Wells Fargo Bank, N.A.	Piper Jaffray & Co.
	Raymond James & Associates, Inc.
	Stern Brothers & Co.
	Stifel, Nicolaus & Co., Inc.
	USB Financial Services Inc.

^(A) Legal name: Merrill Lynch, Pierce, Fenner & Smith Inc.

It is noted the composition of the underwriting team includes participation by local business, women-owned, minority-owned, and disabled veteran business enterprises. Two of the eight Senior Managers and four of the twelve Co-Managers (totaling 30 percent) are women-owned, minority-owned, and/or disabled veteran business enterprises.

Competitive v. Negotiated Bond Sale

The DWP proposal for the use of a negotiated or private bond sale is based upon the determinations made by the CFO in consultation with its financial advisor. The rationale for recommending a negotiated sale includes the following:

- Allows for DWP to encourage significant involvement of local and regional firms in addition to retail investors who are less sensitive to price compared to institutional investors;
- Allows DWP to structure specialized bonds to meet specific investor needs; and,
- Provides DWP flexibility in timing the pricing of debt to respond to market volatility including shifts in interest rates and changes of investor demand.

Furthermore, a negotiated bond sale can provide DWP an opportunity to communicate directly with investment firms regarding potential concerns including, but not limited to, operations, developments, challenges, and mitigation efforts, to ensure appropriate borrowing rates.

Debt Issuance Costs

DWP estimates the total cost of this proposed debt issuance is approximately \$4.460 million. A list of the debt issuance services and estimated costs is provided in the following table.

Debt Issuance Costs \$1.113 billion Water System Revenue Bonds	
Service	Estimated Cost
Rating Agencies	\$ 1,050,000
Financial Advisor	180,000
Bond Counsel	285,000
Disclosure Counsel	150,000
Underwriter's Discount	2,783,000
Printing of Official Statements	12,000
TOTAL	\$4,460,000
<i>Source: DWP Financial Services Organization</i>	

Indebtedness

As of April 30, 2018, the Water System reported approximately \$5.340 billion in debt obligations. This consists of \$4.456 billion of fixed rate bonds, \$325 million of variable rate bonds, and approximately \$559 million of loans from the California Department of Water Resources.