

CALIFORNIA INFRASTRUCTURE AND ECONOMIC DEVELOPMENT BANK (IBank)

STAFF REPORT

**INFRASTRUCTURE STATE REVOLVING FUND PROGRAM (ISRF) DIRECT FINANCING
EXECUTIVE SUMMARY**

Applicant: City of Laguna Beach (City)		ISRF Project Type: Sewage Collection and Treatment		
Financing Amount: \$6,000,000	Financing Term: 20 years	Interest Rate: ¹ 3.45%		
Source of Repayment: Net sewer system revenues (Net Revenues) and all legally available amounts in the Sewer Service Fund (Fund)		Fund Rating/Date: None		
Security: The ISRF Program financing (Financing) would be secured by a senior lien on Net Revenues and all legally available amounts in the Fund, on parity with IBank’s existing liens of the two Installment Sales Agreements No. CIEDB-B04-052 and No. ISRF 18-123.				
Project Name: Coastal Treatment Plant Facility Improvements (Project)		Project Location: 28303 Alicia Pkwy, Laguna Niguel, CA 92677		
Project Description / Sources and Uses of Proceeds: The Project will improve the Coastal Treatment Plant (CTP). The CTP is owned by a joint powers authority (JPA) and the City is one of the JPA members. The City is part of a JPA subcommittee known as “PC 15” that is responsible for the cost of the Project. The City will use the Financing to pay for its share of the Project. The Project consists primarily of the following components: 1) Switchgear Replacement Inside Modified Building, 2) Ferric Chloride System Improvements, 3) Headworks Building Modifications, 4) Basin Structural Improvements, 5) East Secondary Basins & East Return Activated Sludge Channel Rehabilitation, 6) West Secondary Collectors & Launderers Upgrade, 7) Contact Basin Gates, 8) Fall Protection Safety Improvements, 9) Dissolved Air Flotation Motor Control Center (MCC) Replacement and Electrical Room Environmental Controls, 10) Drainage Pump Station Construction Improvements, 11) MCC E8M Replacement, and 12) Electrical Distribution System Improvements.				
Use of Financing Proceeds: The Financing will provide funds for completion of the Project including, but not limited to: construction, construction contingency ² , equipping, machinery, installation, engineering, architecture, design, permitting, environmental review, project administration, construction management, demolition and general project development activities. IBank’s loan origination fee is included in the loan amount.				
PROJECT USES		PROJECT SOURCES		
	IBank	City of Laguna Beach	Other PC 15 Members	Total³
Coastal Treatment Plant Facility Improvements	\$5,940,000	\$132,527	\$9,945,744	\$16,018,271
Origination Fee	\$60,000			\$60,000
Total	\$6,000,000	\$132,527	\$9,945,744	\$16,078,271

¹ As of August 27, 2018

² A construction contingency of 4.8% is included in the total project cost, of which \$250K would come from IBank funds.

³ Moulton Niguel Water District (MNWD) is a member of PC 15 and is currently in litigation with the other members. The worst case scenario of the outcome would be that the other members would be responsible for MNWD’s \$4.7M share of Project costs, \$2.5M of which would be the City’s additional share. The City has sufficient cash on hand to make up any difference in their share of Project costs.

Credit Considerations:

Cash flow and debt service analysis for the Financing is summarized as follows:

CASH FLOW					
For Fiscal Year Ending (FYE) June 30	2014	2015	2016	2017	2018
Cash Available for Debt Service	2,484,958	2,899,136	2,968,463	2,829,416	1,525,534
Debt Service Calculation					
Total Existing Debt Service	798,426	798,426	798,426	798,426	798,426
Proposed IBank MADS ⁽¹⁾	434,580	434,580	434,580	434,580	434,580
Total Obligations	\$1,233,006	\$1,233,006	\$1,233,006	\$1,233,006	\$1,233,006
Debt Service Coverage Ratio	2.02	2.35	2.41	2.29	1.24

⁽¹⁾ Calculated as \$6,000,000 at 3.45% for 20 years

The historical cash flow over the last five years demonstrates the Fund's ability to service existing debt and the proposed Financing with a debt service coverage ratio (DSCR) of 1.24 or greater in all years reviewed. For further analysis, see the Credit Analysis section of this report.

Support for Staff Recommendations:

1. Cash flow analysis demonstrates the Fund's ability to service existing debt and the proposed Financing.
2. City has successfully increased rates in order to cover expenses and service its debt.
3. The estimated useful life of the Project exceeds 20 years, which is greater than the 20 year term of the Financing.
4. The City's existing IBank debts are being paid as agreed, and all post funding conditions continue to be met.

Special Terms and Conditions:

1. In implementing rates and charges, the City will covenant to ensure its rate structure conforms to the requirements of Proposition 218. Further, the City will notify IBank immediately upon the filing of any legal challenge to its rates or charges.
2. Disbursement to be conditional upon satisfactory evidence that all project funding sources, other than IBank's financing, are secured to pay for the entire project.

IBank Staff:

John Lee

Date of Staff Report:

March 15, 2019

Date of IBank Board Meeting:

March 27, 2019

Resolution Number:

19-08

Staff Recommendation:

Staff recommends approval of Resolution No.19-08 authorizing ISRF Program financing in an amount not to exceed \$6,000,000 to the City of Laguna Beach, for the Coastal Treatment Plant Facility Improvements Project.

PROJECT DESCRIPTION

The City of Laguna Beach (City) requests Infrastructure State Revolving Fund (ISRF) Program financing (Financing) in the amount of \$6 million (M) to fund the Coastal Treatment Plant Facility Improvements (Project) (Exhibit 1).

Project Background

The Project will rehabilitate aging wastewater treatment infrastructure at the Coastal Treatment Plant (CTP). The CTP is operated by a joint powers authority known as the South Orange County Wastewater Authority (SOCWA or JPA). SOCWA consists of ten member agencies, including the City. The City collects wastewater from its residents under a City-owned and operated collection system and pipes untreated wastewater to the CTP's collection system. From there, the City's wastewater is combined with that of other member agencies and transmitted to the CTP. Wastewater is treated at the CTP and discharged to the Pacific Ocean via an outfall. The improvements are critical to the protection of the local coastal environment. The Project improvements are based on a series of evaluations prepared by the consultant CH2M Hill, which identified necessary capital improvements and replacements at the CTP.

The City along with a subset of other SOCWA members, known as "Project Committee 15" (PC 15), is responsible for funding the construction of the Project. SOCWA will be the entity responsible for entering into the contracts for the Project and for administering the Project. See "System Description – South Orange County Wastewater Authority" for a detailed description of SOCWA and PC 15. The Financing will provide funds for the City's share of Project costs, including, but not limited to: construction, construction contingency, equipping, machinery, installation, engineering, architecture, design, permitting, environmental review, project administration, construction management, demolition, and general project development activities. The Project consists primarily of the following components: 1) Switchgear Replacement Inside Modified Building, 2) Ferric Chloride System Improvements, 3) Headworks Building Modifications, 4) Basin Structural Improvements, 5) East Secondary Basins & East Return Activated Sludge Channel Rehabilitation, 6) West Secondary Collectors & Launderers Upgrade, 7) Contact Basin Gates, 8) Fall Protection Safety Improvements, 9) Dissolved Air Flotation Motor Control Center (MCC) Replacement and Electrical Room Environmental Controls, 10) Drainage Pump Station Construction Improvements, 11) MCC E8M Replacement, and 12) Electrical Distribution System Improvements.

Public Benefits

The rehabilitation of the aging infrastructure is critical to the protection of the local coastal environment (Exhibit 2). The Project will serve to ensure the quality of the water discharged to the ocean outfall meets stringent regulatory standards, thereby preventing damage to the local environment and economy. The Project will address components that are critical to the operation and reliability of the wastewater treatment plant, which are at the end of their useful life having been installed 30 years ago.

The City anticipates approximately 15 temporary jobs will be created during the construction period as a result of the Project.

GENERAL INFORMATION

The City, a community of approximately 23,190 residents, is located midway between Los Angeles and San Diego, along the southern coast of Orange County (County). The City was incorporated in 1927 as a general law city, operates under a Council-Manager form of government, and is governed by a five-member council. The position of mayor is non-elected and chosen annually among the members of the city council.

The City's location on the Pacific Coast has enhanced its position as a regional arts and tourism center, and is home to more than 70 art galleries and 400 working artists and studios. The City's economy, based predominately on tourism, is dependent upon its unique coastal environment that showcases beaches and views that draw a variety of visitors to the area. An estimated six million visitors annually are drawn to the City for its picturesque beaches, art festivals, village-scale shopping district, and bluff top walkways. The City ranks No. 1 in the U.S. in economic impact of the arts on a per capita basis, which includes total spending by both organizations and audiences, according to Visit Laguna Beach. Condé Nast Traveler named the City among "The Best Small Cities in the U.S." in 2016.

The City has a history of environmental stewardship and historic preservation, and is the only Orange County city protected by a dedicated greenbelt inland and blue belt seaward. As of 2011, the City has successfully protected from development more than 20,000 acres of contiguous wildlands, the majority for which is located in The Laguna Coast Wilderness Park, Jim Dilley Preserve, Crystal Cove State Park, and the Aliso-Wood Canyons Wilderness Park. The coastal area of the City is a bird sanctuary and a marine life refuge. All of the City's marine refuge system is a fully protected marine reserve - nothing can be fished for or removed from this area. The City is known throughout Southern California for its tide pools and the variety of marine life they support.

SYSTEM DESCRIPTION

System Infrastructure

Per the City, the Sewer System (System) serves a population of approximately 22,723 in an 8.7 square mile service area. (Exhibit 1) The System serves 8,190 residential connections and 754 commercial, industrial and institutional customers as of 2018. The System consists of 85.7 miles of gravity sewers, 2,674 manholes, 9.4 miles of force mains, and 25 lift stations. The sewers range in size from 4 to 27 inches in diameter.

In addition to the sewer system facilities, the City maintains a system of 25 urban water diversion units that connect the storm drain system to the sewer system so dry weather nuisance flows may be diverted away from the receiving waters to the sanitary sewer system. These diversion units also divert sanitary sewer overflows within the watersheds they serve.

South Orange County Wastewater Authority

The City is a member of SOCWA, a JPA composed of 10 member agencies consisting of local water and service districts and cities. SOCWA facilitates and manages the collection, transmission, treatment, and disposal of wastewater, as well as the production of recycled water for irrigation and commercial usage, for approximately 500,000 homes and businesses across the southern portion of the County.

SOCWA members enter into agreements with each other to share the costs of various SOCWA facilities in exchange for member's use of the facility for processing their wastewater or for other purposes. The Project consists of capital improvements to the CTP (Exhibit 2), the costs of which are shared through a Project Committee (PC 15) Agreement between the City, Emerald Bay Service District (EBS), Moulton

Niguel Water District (MNWD), and South Coast Water District (SCWD). The PC 15 Agreement defines how much of the project costs each member is obligated to financially support. The CTP is owned, operated, and maintained by SOCWA through, on behalf of, and for the use and benefit of the City, EBSD, MNWD, and SCCWD. SOCWA has no taxing authority, and nearly all funding for its operation comes directly from the contributions of its members. SOCWA bills members for their share of SOCWA's costs to construct, operate, and maintain the facilities the members use. As such, the City will contribute its proportionate share of the cost for the CTP facility improvements to SOCWA.

Litigation

The PC 15 Agreement, approved in 1976 with a 50 year term, is the subject of an ongoing litigation between MNWD, on one side, and SOCWA and the other PC 15 members, on the other side. The PC 15 Agreement establishes capacity ownership of the CTP for the member parties, and though the ownership has fluctuated over the years, MNWD's capacity ownership is 29.25% as of 1999. MNWD filed a lawsuit seeking to release itself from the PC 15 Agreement and the associated financial responsibilities. Further, MNWD is arguing that it is not obligated to fund its proportionate share of various costs associated with the operation of CTP, including the Project costs.

The MNWD litigation was separated into two phases. The first phase was to determine the scope and extent of MNWD's obligations under the SOCWA JPA Agreement and the PC 15 Agreement. The second phase was to address alleged breaches of the SOCWA JPA Agreement and the PC 15 Agreement and associated damages, if any. The trial court recently issued a Tentative Decision, Statement of Decision, and Judgment ruling that MNWD is obligated to pay its proportional share of costs associated with the SOCWA JPA Agreement and the PC 15 Agreement. This would necessarily include costs associated with the Project. If the trial court's tentative decision stands, the litigation will move on to the second phase to determine whether MNWD breached any of its obligations and, if so, the extent of damages associated with any such breach.

Although the trial court has issued a tentative decision, the underlying litigation is far from resolved. The trial court could reverse its tentative decision, or it could be reversed on appeal. Also, the second phase of the trial has not even started and so the issue of MNWD's financial responsibility to the JPA and PC 15 has not yet been reached. Therefore it is not yet clear whether, or to what extent, MNWD will contribute to Project costs. If MNWD is able to avoid financial responsibility for the Project, the City's (and the other PC 15 members') proportionate share of the costs for the Project will most likely increase. However, the remaining PC 15 members intend to proceed with the Project regardless of the outcome of the lawsuit. The City has available funds to make up any difference in their share of Project costs. The City has advised that the remaining PC 15 members also have available funds to pay for any increase in their proportionate share of Project costs. The City's position is that the shared cost of the Project, as currently established by the PC 15 Agreement, for the City, SCWD, MNWD, and EBSD is approximately \$6.1M, \$4.8M, \$4.7M and \$479K, respectively. If MNWD ultimately prevails in its lawsuit, it's approximately \$4.7M share of Project costs would be reallocated proportionally among the other PC 15 members. IBank will condition disbursement upon receipt of adequate proof that the City and other PC 15 members have secured funding for the entire Project cost.

Capital Improvement Plan

The City has a ten-year Capital Improvement Plan (CIP) through which it recommends upgrades to all of the elements of the System. It also has a "Financing Plan" that is used to project the rate increases and debt issuance needed to finance the CIP projects. The CIP budget identifies the Project along with other improvements. The City estimates it still needs \$41.7M in System improvements that will take until fiscal year (FY) 2027 to complete.

The following table displays the Number of Users by Category and reflects stability in the number of users. The City of Laguna Beach is fully built-out. There are no changes expected in service demand forecast in the next 5 years. The table further reflects a high proportion of residential users, which is consistent with the residential nature of the City and represents a strong diversity in the user base.

NUMBER OF USERS BY CATEGORY					
For Fiscal Year Ending (FYE) June 30	2014	2015	2016	2017	2018
Residential	8,174	8,177	8,185	8,189	8,190
Commercial	364	355	362	363	361
Other	427	415	407	402	393
Total	8,965	8,947	8,954	8,954	8,944
% change	N/A	-0.20%	0.08%	0.00%	-0.11%

Source: Financing Application Addendum

The table below displays Current System Usage and Revenue as of March 31, 2018. Residential customers represent more than 82.2% of the Gross Annual Revenues.

CURRENT SYSTEM USAGE & REVENUE		
	Gross Annual Revenue	% Gross Annual Revenue
Residential	\$6,498,800	82.2%
Commercial	\$1,214,600	15.4%
Other	\$189,800	2.4%
Total	\$7,903,200	100.0%

Source: Financing Application

The following table displays the Historical Rate Increases adopted over the past five years, and reflects the City's ability to increase rates in order to meet its operational and capital improvement needs.

HISTORICAL RATE INCREASES PAST FIVE YEARS		
Date Adopted	Date Effective	Percent Increase
July 1, 2015	July 1, 2015	4.75%
July 1, 2015	July 1, 2016	4.75%
July 1, 2015	July 1, 2017	4.75%
July 1, 2015	July 1, 2018	4.75%
July 1, 2015	July 1, 2019	4.00%

Source: Financing Application Addendum

The following table displays the Historical and Current Average Monthly User Charge per Residential Unit and the year-over-year percent increase of the charge since FY 2015. The table also reflects each year's charge as a percent of the County's Median Household Income (MHI) for residential units as of FYE 2016.

HISTORICAL AND CURRENT AVERAGE MONTHLY USER CHARGE PER RESIDENTIAL UNIT				
For Fiscal Year Ending (FYE) June 30	2015	2016	2017	2018
Residential	\$48.42	\$50.75	\$52.50	\$55.67
% change	NA	4.8%	3.4%	6.0%
% of MHI	0.05%	0.05%	0.05%	0.06%

Source: Financing Application Addendum

The following table displays the Projected Average Monthly User Charge Per Residential Unit in FYs 2018 through 2022. The City projects increasing rates by 4.0% to 4.8% in the first two fiscal years presented, which is consistent with the adopted rate increases reflected in the Historical Rate Increases table above. At this time there is no planned rate increase beyond the current adopted rates that go into effect each year through FY 2020. The proposed Sewer Service Fund (Fund) budget continues to move forward with the ten year financial plan for the wastewater system that includes rate increases of 4.8% through FY 2018-19 and 4.0% in FY 2019-20, as well as setting aside funding toward a goal of reaching a \$1.8M reserve by FY 2024-25.

PROJECTED AVERAGE MONTHLY USER CHARGE PER RESIDENTIAL UNIT					
For Fiscal Year Ending (FYE) June 30	2018	2019	2020	2021	2022
Residential	\$55.67	\$58.33	\$60.67	\$60.67	\$60.67
% change	NA	4.8%	4.0%	TBD	TBD

Source: Financing Application Addendum

The following table displays the City’s Average Monthly System User Charge Compared to Nearby Systems as of April 14 2015, the most recent comparison available. The City states the comparison costs are difficult to compile since there are various ways to manage a wastewater system, e.g. stand-alone enterprise fund, an enterprise fund combined with a water system, etc. The City has the most lift stations per population served of any agency known in the state, due to its topography and need to lift waste water in areas where gravity flow is not possible. The additional lift stations required by the City’s System drive up the cost for operating and maintaining the System as compared to nearby systems.

CURRENT AVERAGE MONTHLY SYSTEM USER CHARGE COMPARED TO NEARBY SYSTEMS			
System Name	Distance in Miles	Location	Average Monthly Residential Rate
Seal Beach	30.8	Seal Beach	\$53.21
South Coast Water District	3.7	South Laguna	\$51.61
City of Laguna Beach		N/A	\$48.42
San Clemente	14.1	San Clemente	\$38.70
Huntington Beach	15.5	Huntington Beach	\$37.03
Newport Beach	10.5	Newport Beach	\$35.03
		Average Monthly Charge	\$39.80

Source: Financing Application Addendum

The following table displays the Top 10 System Users and reflects that the City complies with IBank's underwriting requirements that revenues derived from the top ten ratepayers not exceed 50%, and that no single ratepayer generates 15% or greater of the System's annual revenues.

TOP 10 SYSTEM USERS as of April 10, 2018			
	User	% System Revenues	Customer Class
1	Apartment Building (211 Units)	1.44%	Residential
2	Apartment Building (210 Units)	1.44%	Residential
3	Surf and Sand Hotel	1.38%	Commercial
4	Las Brisas Restaurant	0.47%	Commercial
5	Hotel Laguna	0.38%	Commercial
6	Vons	0.33%	Commercial
7	Carmelita's Restaurant	0.26%	Commercial
8	Watermarc, Gelato, La Rue Chocolate	0.24%	Commercial
9	Earth Café	0.23%	Commercial
10	The Roof Top Lounge	0.23%	Commercial
	Total	6.40%	

Source: Financing Application Addendum

CREDIT ANALYSIS

Source of Financing and Security

The ISRF Program financing (Financing) would be secured by a senior lien on Net Revenues and all legally available amounts in the Fund, on parity with IBank's existing liens of the two Installment Sales Agreements Numbers CIEDB-B04-052 and ISRF 18-123.

Source of Revenue to Repay Proposed ISRF Program Financing:	Net sewer system revenues and all legally available amounts in the Sewer Service Fund
Outstanding Obligations:	Two Installment Sales Agreements Numbers CIEDB-B04-052 and ISRF 18-123 with an outstanding balance of \$2,295,678 and \$4,000,000, respectively.
Type of Audited Financial Documents Reviewed:	<input checked="" type="checkbox"/> Comprehensive Annual Financial Reports (CAFR) <input type="checkbox"/> Basic Financial Statements (F/S) <input type="checkbox"/> Other:
Fiscal Year Ends:	June 30
Audit Fiscal Years Reviewed:	2014-2017
The auditor's reports for all years indicate that the financial statements present fairly, in all material respects, the financial position of the City, and that the results of its operations and the cash flows are in conformity with generally accepted accounting principles.	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No. [If no, explain]
Adopted Budget(s) Reviewed:	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No. [If no, explain]
Budget Year(s) Reviewed:	2018-2019

Comparative Statement of Net Position Analysis

Analysis of the Fund's Comparative Statement of Net Position for the last five fiscal years is as follows:

SEWER SERVICE FUND COMPARATIVE STATEMENT OF NET POSITION											
For Fiscal Year Ending (FYE) June 30		2014		2015		2016		2017		2018	
Source:		CAFR	%	CAFR	%	CAFR	%	CAFR	%	CAFR	%
Assets											
Cash and Investments		\$2,666,994	5.6%	\$4,592,893	9.7%	\$3,683,555	7.5%	\$2,277,463	5.4%	\$1,285,420	2.8%
Receivables:											
Taxes		85,665	0.2%	87,158	0.2%	40,114	0.1%	73,533	0.2%	72,921	0.2%
Accounts		94,689	0.2%	169,235	0.4%	184,221	0.4%	21,895	0.1%		
IBank Installment Agreement										4,000,000	8.9%
Total Current Assets		2,847,348	6.0%	4,849,286	10.3%	3,907,890	7.9%	2,372,891	5.7%	5,358,341	11.9%
Noncurrent Assets											
Capital Assets, Not Being Depreciated		3,674,156	7.8%	1,235,312	2.6%	5,213,877	10.6%	380,743	0.9%	410,691	0.9%
Capital Assets, Net of Depreciation		40,810,918	86.2%	41,206,015	87.1%	40,152,539	81.5%	39,141,980	93.4%	39,376,317	87.2%
Total Noncurrent Assets		44,485,074	94.0%	42,441,327	89.7%	45,366,416	92.1%	39,522,723	94.3%	39,787,008	88.1%
Total Assets		47,332,422	100.0%	47,290,613	100.0%	49,274,306	100.0%	41,895,614	100.0%	45,145,349	100.0%
Deferred Outflows of Resources											
Deferred Amounts Related to Pensions				353,656	0.7%	377,788	0.8%	793,785	1.9%	871,297	1.9%
Liabilities											
Current Liabilities:											
Accounts Payable and Accrued Liabilities		262,688	0.6%	212,506	0.4%	505,773	1.0%	324,144	0.8%	236,124	0.5%
Compensated Absences Due Within One Year		8,328	0.0%	7,487	0.0%	9,881	0.0%	10,265	0.0%	11,943	0.0%
IBank Installment Sale Agreement Due Within One Year		379,966	0.8%	390,339	0.8%	400,996	0.8%	411,943	1.0%	423,189	0.9%
Total Current Liabilities		650,982	1.4%	610,332	1.3%	916,650	1.9%	746,352	1.8%	671,256	1.5%
Noncurrent Liabilities											
Compensated Absences Due Within One Year		33,311	0.1%	29,947	0.1%	39,523	0.1%	41,061	0.1%	47,771	0.1%
IBank Installment Sale Agreement		3,922,145	8.3%	3,531,806	7.5%	3,130,809	6.4%	2,718,867	6.5%	6,295,678	13.9%
Total OPEB Liability										96,814	
Net Pension Liability				2,153,142	4.6%	2,288,952	4.6%	2,661,436	6.4%	2,909,216	6.4%
Total Noncurrent Liabilities		3,955,456	8.4%	5,714,895	12.1%	5,459,284	11.1%	5,421,364	12.9%	9,349,479	20.7%
Total Liabilities		4,606,438	9.7%	6,325,227	13.4%	6,375,934	12.9%	6,167,716	14.7%	10,020,735	22.2%
Deferred Inflows of Resources											
Deferred Amounts Related to Pensions				514,522	1.1%	173,171	0.4%	80,059	0.2%	35,810	0.1%
Net Position											
Net Investment in Capital Assets		40,182,963	84.9%	38,519,182	81.5%	41,834,611	84.9%	36,391,913	86.9%	37,068,141	82.1%
Unrestricted		2,543,021	5.4%	2,285,338	4.8%	1,268,378	2.6%	49,711	0.1%	(1,108,040)	-2.5%
Total Net Position		\$42,725,984	90.3%	\$40,804,520	86.3%	\$43,102,989	87.5%	\$36,441,624	87.0%	\$35,960,101	79.7%

Cash and Investments shows a 72.2% increase in FY 2015, primarily attributable to a reduction in the outflow of funds for projects completed, including the SOCWA Capital Improvements and 3rd Street projects. The decrease of 43.6% in FY 2018 is mainly due to an increase in operating costs; primarily legal fees. The decrease of 88.1% in Accounts Receivable for FY 2017 is primarily due to higher collection activity. Total Current Assets increased 125.8% for FY 2018, primarily attributable to the reporting of the 2018 IBank financing for the Sewer System Collection and Treatment Facility Rehab and Replacements project.

Capital Assets, Not Being Depreciated increased to \$5.2M in FY 2016 due to an increase of construction in progress. Total Assets shows a 15.0% decrease between FY 2016 and FY 2017, primarily due to the above mentioned decrease in the Capital Assets, Not Being Depreciated and Cash and Investments line items.

Beginning FY 2015, Net Pension Liability and Deferred Pension Inflows of Resources, reflect the implementation of Governmental Accounting Standards Board Statement No. (GASB) 68. The Unrestricted balance of (1,108,040) in FY 2018, is primarily due to a one-time increase in legal fees. According to the City, this one-time event is not expected in FY 2019.

The City collects the sewer system payments through annual property tax bills, and given this method it collects approximately 98% of revenues each year, with 100% collected within five years.

Comparative Statement of Revenues, Expenses, and Changes in Net Position Analysis

Analysis of the Fund's Comparative Statement of Revenues, Expenses, and Changes in Net Position for the last five years follows:

SEWER SERVICE FUND										
COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION										
For Fiscal Year Ending (FY) June 30	2014		2015		2016		2017		2018	
Source:	CAFR	%	CAFR	%	CAFR	%	CAFR	%	CAFR	%
% Change Year-over-Year in Total Revenues		N/A		4.1%		4.3%		4.0%		4.6%
Operating Revenues										
Charges for Services	\$6,814,418	100.0%	\$7,093,423	100.0%	\$7,400,257	100.0%	\$7,699,521	100.0%	\$8,050,631	100.0%
Total Operating Revenues	6,814,418	100.0%	7,093,423	100.0%	7,400,257	100.0%	7,699,521	100.0%	8,050,631	100.0%
Operating Expenses										
Personnel Services	1,401,236	20.6%	1,171,641	16.5%	1,245,199	16.8%	1,401,478	18.2%	1,725,642	21.4%
Contractual Services	1,912,367	28.1%	2,076,394	29.3%	2,198,632	29.7%	2,418,256	31.4%	3,064,202	38.1%
Material and Supplies	1,009,196	14.8%	958,211	13.5%	1,012,652	13.7%	1,047,823	13.6%	1,741,613	21.6%
Administration	6,661	0.1%	13,371	0.2%	11,011	0.1%	20,635	0.3%	10,833	0.1%
Depreciation	1,184,398	17.4%	3,242,893	45.7%	1,399,232	18.9%	1,746,598	22.7%	1,735,451	21.6%
Total Operating Expenses	5,513,858	80.9%	7,462,510	105.2%	5,866,726	79.3%	6,634,790	86.2%	8,277,741	102.8%
Operating Income (Loss)	1,300,560	19.1%	(369,087)	-5.2%	1,533,531	20.7%	1,064,731	13.8%	(227,110)	-2.8%
Nonoperating Revenues (Expenses)										
Investment Income			25,330	0.4%	35,700	0.5%	18,087	0.2%	17,193	0.2%
Intergovernmental	276,923	4.1%	555,307	7.8%	172,837	2.3%			9,563	0.1%
Interest Expense	(122,496)	-1.8%	(106,933)	-1.5%	(96,277)	-1.3%	(85,322)	-1.1%	(85,169)	-1.1%
Gain (Loss) on Disposal of Capital Assets			(6,537)	-0.1%					(18,134)	-0.2%
Other Revenue	25,103	0.4%	252,214	3.6%	262,564	3.5%	21,895	0.3%	74,577	0.9%
Total Nonoperating Revenues (Expenses)	179,530	2.6%	719,381	10.1%	374,824	5.1%	(45,340)	-0.6%	(1,970)	0.0%
Income (Loss) Before Contributions and Transfers	1,480,090	21.7%	350,294	4.9%	1,908,355	25.8%	1,019,391	13.2%	(229,080)	-2.8%
Capital Contributions and Transfers										
Transfer In	100,000		233,957		390,114		546,074			
Transfer Out							(106,000)		(155,000)	
Total Transfers			233,957		390,114		440,074		(155,000)	
Change in Net Position	1,580,090		584,251		2,298,469		1,459,465		(384,080)	
Net Position at Beginning of Year	41,145,894		42,725,984		40,804,520		43,102,989		36,441,624	
Prior Period Adjustment (=/-)			(2,505,715)				(8,120,830)		(97,443)	
Net Position at Beginning of Year, as Restated			40,220,269				34,982,159		36,344,181	
Net Position at End of Year	\$42,725,984		\$40,804,520		\$43,102,989		\$36,441,624		\$35,960,101	

Total Operating Revenues increased each year of five years reviewed, and overall by 18.1%, primarily due to a steady increase in Charges for Services that reflect annual rate increases. The latest 5-year rate increase was implemented in FY 2016, and increases rates 4 to 4.75% each year.

Total Operating Expenses increased 20.3% between FYs 2014 and 2015, primarily attributable to annual increases in Contractual Services, and an increase in Depreciation for FY 2015. The increase in Depreciation in FY 2015 is primarily due to an adjustment by auditors for accumulated depreciation in sewer plant & lines. The increase in Contractual Services is primarily due to annual SOCWA Operations & Maintenance share increases, and increases in insurance and legal fees. Material and Supplies increased 66.2% in FY 2018, primarily due to maintenance and repairs performed through a contract.

Intergovernmental increased 97.1% from FY 2014 to FY 2015, due to an increase in operating grants received. Other Revenue reflects recurring reimbursement from EBSD for services related to the North Coast Interceptor. Transfer In has increased each year for FYs 2014 to 2017, primarily attributable to an internal service fund used to acquire vehicles. In FY 2017, \$106K was transferred out to the General Fund for expenditures related to repairs to sewer lines as part of the Anita Storm Drain project. In FY 2018, \$155K was transferred out to the General Fund for the Dewitt Property project.

Net Position, End of Year decreased 15.8% between FYs 2014 and 2018. The decrease was primarily attributable to Prior Period Adjustments of \$2.5M in FY 2015 due to implementation of GASB 68 and 71, and \$8.1M in FY 2017, which accounts for capital assets and accumulated depreciation for infrastructure assets not previously depreciated. The Prior Period Adjustment of \$97.4k in FY 2018 was due to the implementation of GASB 75 to record the net OPEB liability as of the beginning of the year.

Existing Obligations Payable from the Fund

The table below shows the Fund's outstanding obligations payable from the Fund, the outstanding balance of the obligations (as of August 1, 2018), and the proposed Financing for the Project.

SEWER SERVICE FUND OBLIGATIONS					
Debt Issued	Date Issued	Maturity	Amount Issued	Outstanding Balance	Parity Lien Position
2004 IBank ISA No. CIEDB-B04-052	2004	2023	\$7,000,000	\$2,295,678	Senior
2018 IBank ISA No. ISRF 18-123	2018	2038	\$4,000,000	\$4,000,000	Senior
Proposed IBank Financing		2038	\$6,000,000	\$6,000,000	Senior
	Total		\$17,000,000	\$12,295,678	

The above outstanding obligations permit subsequent parity debt upon certain conditions including satisfying a 1.20 debt service coverage ratio (DSCR). As shown in the following Cash Flow table, the City meets the 1.20 DSCR requirement.

Fund Cash Flow and Debt Service Analysis

Fund cash flow and debt service analysis for the Financing is as follows:

CASH FLOW					
For Fiscal Year Ending (FYE) June 30	2014	2015	2016	2017	2018
Operating Income (Loss)	\$1,300,560	(\$369,087)	\$1,533,531	\$1,064,731	(\$227,110)
Transaction Specific Adjustments					
+ Depreciation	1,184,398	3,242,893	1,399,232	1,746,598	1,735,451
+ Interest Earnings		25,330	35,700	18,087	17,193
Total of all Adjustments	1,184,398	3,268,223	1,434,932	1,764,685	1,752,644
Cash Available for Debt Service	2,484,958	2,899,136	2,968,463	2,829,416	1,525,534
Debt Service Calculation					
Total Existing Debt Service MADS	798,426	798,426	798,426	798,426	798,426
Proposed IBank MADS ⁽¹⁾	434,580	434,580	434,580	434,580	434,580
Total Obligations MADS	\$1,233,006	\$1,233,006	\$1,233,006	\$1,233,006	\$1,233,006
Debt Service Coverage Ratio	2.02	2.35	2.41	2.29	1.24

⁽¹⁾ Calculated as \$6,000,000 at 3.45% for 20 years

The historical cash flow over the last five years demonstrates the Fund's ability to service existing debt and the proposed Financing with a DSCR of 1.24 or greater in all years reviewed. FY 2018, experienced a lower DSCR due in large part to legal fees paid for the MNWD litigation and in part to an increase in maintenance and repairs. Once the MNWD litigation is resolved, which the City is hopeful will be negotiated in the near term, there would be a decrease in the expense of legal fees. Additionally, a 4.0% rate increase is approved for FY 2020, which would go into effect July 1, 2019. Further, the 2004 IBank ISA will be paid off in four years, and represents 40% of the Fund's annual debt service payment, inclusive of the proposed debt.

RISK FACTORS

1. The City is not prohibited from incurring additional obligations payable from the Fund.

MITIGATING FACTORS

1. The City will be prohibited from issuing future debt senior to the IBank financing, and new parity debt would only be permitted if annual Net Revenues are at least 1.20 times the MADS.

Compliance with IBank Underwriting Criteria

- The financing will be secured by a lien on Net Revenues, on parity with IBank's existing liens of the two Installment Sales Agreements Numbers CIEDB-B04-052 and ISRF 18-123.
- Revenues derived from the top ten System ratepayers do not exceed 50% of annual System revenues.
- Revenues derived from any single ratepayer do not exceed 15% of annual System revenues.
- The City has the power to establish and enact rates and charges without the approval of any other governing body.
- The useful life of the Project exceeds 20 years. Therefore, the Project useful life exceeds the 20 year financing term.

STAFF RECOMMENDATION

Staff recommends approval of Resolution No.19-08 authorizing ISRF Program financing to the City of Laguna Beach (City), for the Coastal Treatment Plant Facility Improvements.

1. **Applicant/Borrower:** The City of Laguna Beach
2. **Project:** Coastal Treatment Plant Facility Improvements
3. **Amount of Financing:** \$6,000,000
4. **Maturity:** Twenty (20) years
5. **Repayment/Security:** The ISRF Program financing (Financing) would be secured by a senior lien on the City's sewer system revenues (Net Revenues) and all legally available amounts in the City's Sewer Service Fund (Fund) on parity with IBank's existing liens of the two Installment Sales Agreements Numbers CIEDB-B04-052 and ISRF 18-123.
6. **Interest Rate:** 3.45%
7. **Fees:** The City to pay an origination fee of 1.00%, \$60,000, included in loan amount, and an annual fee of 0.30% of the outstanding principal balance.
8. **Not an Unconditional Commitment:** IBank's resolution shall not be construed as an unconditional commitment to finance the Project, but rather IBank's approval pursuant to the Resolution is conditioned upon entry by IBank and the City into a Financing Agreement, in form and substance satisfactory to IBank.
9. **Limited Time:** The Board's approval expires June 10, 2019. Thus, the City and IBank must enter into the Financing agreement no later than June 10, 2019. Once the approval has expired, there can be no assurances that IBank will be able to provide the Financing to the City or consider extending the approval period.
10. **ISRF Program Financing Agreement Covenants and Conditions:** The Financing Agreement shall include, among other things, the following covenants:
 - a. The City will be required to maintain rates and charges in an amount sufficient to ensure that Net Revenues produce a minimum 1.20 times aggregate annual debt service ratio for obligations on parity with the Financing.
 - b. The City has no senior liens and the City will be prohibited from issuing future debt senior

- to the Financing.
- c. Parity debt will be allowed if Net Revenues amount to at least 1.20 times the Maximum Annual Debt Service (MADS) taking into consideration the MADS payable in any Fiscal Year on all existing debt and the proposed parity debt.
 - d. Subordinate debt will be allowed if Net Revenues are at least 1.00 times the sum of the MADS on all outstanding debt, payable from the Fund, including the proposed Subordinate Debt.
 - e. The City will covenant against reducing rates below levels used for all debt service payable from the Fund, and to take actions to increase rates or fund a rate stabilization fund if the debt service coverage ratios fall below required levels.
 - f. Upon implementing rates and charges, the City to covenant to ensure that its rate structure conforms to the requirements of Proposition 218 and those of the statutes implementing it and the cases interpreting it. Further, the City to covenant to notify IBank immediately upon the filing of any legal challenge to its rates or charges.

- g. The City to comply with the requirements of the Criteria, except to the extent of any Criteria waivers, and all applicable laws, regulations, and permitting requirements associated with public works projects.
- h. The City to provide to IBank annually within 180 days of the end of each of the City's fiscal year a copy of its audited financial statements together with an annual certificate demonstrating compliance with the foregoing covenants, as well as other information as IBank may request from time to time.
- i. No disbursements will be allowed until the City provides evidence reasonably satisfactory to IBank that all project funding sources, other than IBank's financing, are secured to pay for the entire project.

Exhibit 1

SOCWA COASTAL TREATMENT PLANT



Source: Google Earth

Exhibit 2

OVERVIEW OF THE LAGUNA BEACH STATE MARINE RESERVE AND CONSERVATION AREA



Source: Google Earth