- Board of Directors
  Finance and Insurance Committee

7/9/2019 Board Meeting

Revised 8-1

Subject

Adopt resolution authorizing the reimbursement of capital expenditures from bond proceeds for fiscal years 2018/19 and 2019/20 and other capital expenditures relating to Metropolitan's water delivery systems; the General Manager has determined that the proposed action is exempt or otherwise not subject to CEQA

Executive Summary

The resolution of reimbursement of capital expenditures from bond proceeds in **Attachment 1** (Resolution of Reimbursement) evidences the intention to use tax-exempt bond proceeds or other forms of indebtedness to finance capital expenditures for projects and to use some or all of such proceeds to reimburse Metropolitan for costs of such projects initially funded from operating revenues. If adopted, Metropolitan would be authorized to use tax-exempt debt proceeds to reimburse capital expenditures initially paid or to be paid by operating revenues, providing Metropolitan with additional financial flexibility in fiscal years (FY) 2018/19 and 2019/20. Adoption of the resolution of reimbursement preserves Metropolitan's ability to use tax-exempt debt proceeds to reimburse the use of operating revenues.

Details

The Biennial Budget for FYs 2018/19 and 2019/20, adopted by Metropolitan's Board on April 10, 2018, included funding capital expenditures from a combination of bonds and operating revenues. The planned capital spending as developed by Engineering Services and presented in the capital expenditures section of the FYs 2018/19 and 2019/20 Biennial Budget was estimated to be $514 million over the biennium. The capital expenditures in the FYs 2018/19 and 2019/20 Biennial Budget were 80 percent of the planned engineering spending or $200 million in each fiscal year. This $200 million was planned to be funded with $120 million of operating revenues and $80 million in bonds in each fiscal year.

As reported at the June 2019 Engineering and Operations Committee meeting, $204 million for capital expenditures is anticipated to be expended in FY 2018/19; the forecast for FY 2019/20 is $275 million for capital expenditures. Combined, actual and forecasted expenditures are $479 million, $79 million over the capital expenditures in the Biennial Budget.

In April 2019, the Board approved participating in the Antelope Valley East Kern (AVEK) Agency's High Desert Water Bank Program (Program), with a total estimated construction cost of $131 million. This Program was not included in the Biennial Budget. Anticipated costs to Metropolitan in FY 2019/20 are approximately $26 million to $30 million. These costs cannot be bond funded by Metropolitan; however, an equivalent amount of capital expenditures that would have otherwise been funded from operating revenues could be funded with debt, freeing up operating revenues to fund the AVEK Program.

The current hydrologic conditions and record low water transactions have impacted FY 2018/19 water revenues and financial reserve balances. As reported to the Finance and Insurance Committee at its meeting of April 8, 2019, the modified accrual Unrestricted Reserve Balance is estimated to end FY 2018/19 at approximately $425 million, approximately $50 million below the beginning of the fiscal year. FY 2019/20 water transactions will be reviewed for potential reductions from budgeted levels. Therefore, the ability for the Board to use tax-exempt bond proceeds to finance and reimburse Metropolitan for capital expenditures paid or to be paid by operating revenues will provide the Board with the additional financial flexibility to meet these challenges in FY 2019/20.

Finally, in recent years, Metropolitan has issued new money bonds in late June, making the bond proceeds available on July 1 to fund capital expenditures. The new money bonds for FY 2019/20 are not anticipated to be issued until later in the fiscal year when the appropriate size of the bond issue can be more accurately determined and market conditions are anticipated to be more favorable. Metropolitan will want to reimburse the use of operating revenues used to fund capital expenditures during the period until bonds are issued.

By adopting the Resolution of Reimbursement, Metropolitan indicates its expectation to issue up to $280 million in tax-exempt debt and use the proceeds to reimburse certain capital expenditures initially funded with operating revenues. In accordance with Internal Revenue Service (IRS) regulations, Metropolitan would be required to declare its “official intent” to reimburse a capital expenditure no later than 60 days after the payment of the original expenditure to be reimbursed. The IRS regulations for the applicable time periods are detailed, but generally, reimbursements can be received for General Fund, and Replacement & Refurbishment Fund funded capital expenditures three years after the date on which each capital expenditure was paid.

Additional bond funds beyond the planned $80 million in FY 2019/20 will be needed. The anticipated additional capital spending in FY 2018/19 and FY 2019/20 of approximately $79 million and the addition of the AVEK Program spending of $26 million to $30 million in FY 2019/20, combined with the ongoing wet hydrologic conditions, present significant uncertainties regarding available operating revenues and financial reserve balances.

Resolutions of reimbursement were adopted by the Board in 2015 and 2016.

Policy

Metropolitan Water District Act Section 61: Ordinances, Resolutions and Orders

Metropolitan Water District Administrative Code Section 5108(d): Appropriations

Metropolitan Water District Administrative Code Section 5109: Capital Financing

Metropolitan Water District Administrative Code Section 5200(a) and (b): Funds Established

Metropolitan Water District Administrative Code Section 11104: Delegation of Responsibilities

California Environmental Quality Act (CEQA)

CEQA determination for Option #1:

The proposed action is not defined as a project under CEQA (Public Resources Code Section 21065, State CEQA Guidelines Section 15378) because the proposed action will not cause either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment and involves continuing administrative activities, such as general policy and procedure making (Section 15378(b)(2) of the State CEQA Guidelines). In addition, the proposed action is not defined as a project under CEQA because it involves the creation of government funding mechanisms or other government fiscal activities, which do not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment (Section 15378(b)(4) of the State CEQA Guidelines).

CEQA determination for Option #2:

None required

Board Options

Option #1

Adopt resolution authorizing the reimbursement of capital expenditures from bond proceeds for fiscal years 2018/19 and 2019/20 and other capital expenditures relating to Metropolitan's water delivery systems as contained in **Attachment 1.**

Fiscal Impact: The Resolution of Reimbursement would allow Metropolitan to use debt proceeds to reimburse capital expenditures for FYs 2018/19 and 2019/20 initially funded with operating revenues. However, debt service costs would increase if bonds were issued to reimburse capital expenditures. Annual debt service costs for a $280 million bond issue could range from $3.6 million to $5.6 million for variable rate debt and approximately $17 million for fixed rate debt.

Business Analysis: Option #1 would provide Metropolitan the ability to reimburse operating revenue-funded capital expenditures with tax-exempt debt proceeds. Such reimbursed funds would replenish funds that then may be used for any lawful purpose, including funding for water supply management programs.

Option #2

Do not adopt the Resolution of Reimbursement as contained in **Attachment 1**.

Fiscal Impact: Option #2 would result in a reduction in Metropolitan's financial flexibility during FY 2019/20. There would, however, be no increase in projected debt service costs, as only $80 million of capital expenditures would be funded from debt proceeds.

Business Analysis: Option #2 would limit Metropolitan's financial flexibility in FY 2019/20, as Metropolitan could not reimburse operating revenue-funded capital projects from debt proceeds. Therefore, Metropolitan's operating revenues may not be sufficient to pay for approved capital expenditures.

Staff Recommendation

Option #1

6/25/2019

June M. Skillman — *Date*
Interim Assistant General Manager/
Chief Financial Officer

6/27/2019

Jeffrey Kightlinger — *Date*
General Manager

Attachment 1 – Resolution of The Board of Directors of The Metropolitan Water District of Southern California Pertaining to the Reimbursement Of Capital Expenditures From Bond Proceeds

Ref# cfo12670573

THE METROPOLITAN WATER DISTRICT OF
SOUTHERN CALIFORNIA

RESOLUTION ____

RESOLUTION OF THE BOARD OF DIRECTORS
OF THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA
PERTAINING TO THE REIMBURSEMENT OF CAPITAL EXPENDITURES FROM BOND PROCEEDS

The Board of Directors of The Metropolitan Water District of Southern California (the "Board") hereby finds that:

1. The Metropolitan Water District of Southern California ("Metropolitan") desires and expects to debt finance certain construction costs relating to its fiscal years 2018/19 and 2019/20 Capital Investment Plan and other capital expenditures relating to Metropolitan's water delivery system ("Projects");

2. Metropolitan expects to issue up to $280 million in debt during fiscal year 2019/20 to finance the Projects, or portions of the Projects, with the sale of obligations, the interest upon which is excluded from gross income for federal income tax purposes (the "Debt");

3. Metropolitan expects to expend (or to have expended) moneys (other than moneys derived from the issuance of bonds) on expenditures relating to the costs of the Projects prior to the issuance of the Debt, which expenditures will be properly chargeable to a capital account under general federal income tax principles;

4. Metropolitan reasonably expects to reimburse certain of such capital expenditures with the proceeds of the Debt;

5. Metropolitan expects that the maximum principal amount of Debt which will be issued to pay for the costs of the Projects (and related issuance costs) will not exceed $280 million;

6. At the time of the reimbursement for the Projects, Metropolitan will evidence such reimbursement in a writing which identifies the allocation of the proceeds of the Debt to Metropolitan for the purpose of reimbursing Metropolitan for the capital expenditures prior to the issuance of the Debt;

7. Metropolitan expects to make each of the reimbursement allocations no later than eighteen (18) months after the later of (i) the date on which the earliest original expenditure for the relevant Project is paid or (ii) the date on which such Projects are placed in service (or abandoned), but in no event later than three (3) years after the date on which the earliest original expenditure for the relevant Project or other capital expenditure is paid;

8. Metropolitan will not, within one (1) year of any reimbursement allocation, use the proceeds of the Debt received in the reimbursement allocation in a manner that will result in the creation of replacement proceeds of the Debt or another issue (e.g., Metropolitan will not pledge or use the proceeds received for the payment of debt service on the Debt or another issue, except that the proceeds of the Debt can be deposited in a bona fide debt service fund); and

9. This Resolution is intended to be a "declaration of official intent" in accordance with Section 1.150-2 of the U.S. Treasury Regulations.

NOW, THEREFORE, the Board hereby finds, resolves, determines and orders as follows:

Section 1. That in accordance with Section 1.150-2 of the U.S. Treasury Regulations, Metropolitan hereby declares its intention to issue Debt in a principal amount not to exceed $280 million, the proceeds of which will be used to pay for the costs of the Projects and other capital expenditures (and related issuance costs), including the reimbursement to Metropolitan for certain capital expenditures relating to the Projects made prior to the issuance of the Debt.

Section 2. This declaration of intent does not bind Metropolitan to make any expenditure, nor incur any indebtedness, or proceed with the issuance of any Debt, or proceed with the Projects.

I HEREBY CERTIFY, that the foregoing is a full, true and correct copy of a Resolution adopted by the Board of Directors of The Metropolitan Water District of Southern California, at its meeting held July 9, 2019.

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Secretary of the Board of Directors
of The Metropolitan Water District
of Southern California