

DATE ISSUED: January 27, 2005 REPORT NO. 05-027

ATTENTION: Honorable Mayor and City Council
Docket of January 31, 2005

SUBJECT: Wastewater and Water Capital Improvement Funding Update

REFERENCE: December 1, 2004 Memorandum to Mayor and Council from City
Manager P. Lamont Ewell - Subject: Wastewater and Water
Capital Improvement Funding Issues

SUMMARY :

Manager's Recommendation: Accept the Report.

BACKGROUND

In early December, an analysis indicated it would be prudent to curtail both the wastewater and water capital improvement programs until such time as the City can proceed with obtaining additional public financing. This report gives background information regarding the wastewater and water capital programs from fiscal year 2001 through 2004, the size of the capital programs as planned in fiscal 2005 through fiscal 2007, and how the programs have been downsized for calendar year 2005.

This report also describes how the wastewater and water capital programs have been funded. It includes a history of the bond financings for both wastewater and water as well as a description of how the departments have been monitoring their cash flow.

DISCUSSION

Size of Wastewater & Water Capital Programs:

The Metropolitan Wastewater Department (MWWD) had a total capital budget of \$456.1 million from fiscal year 2001 through fiscal year 2004.

The Water Department had a total capital budget of \$444.6 million from fiscal year 2001 through fiscal year 2004.

APPROPRIATIONS FY01 – FY04
(In millions of dollars)

	FY 2001	FY 2002	FY 2003	FY 2004	FY'01-04 TOTAL
Total Sewer	\$83.1	\$138.8	\$70.8	\$163.4	\$456.1
Total Water	\$132. 3	\$105.9	\$89.6	\$116.8	\$444.6

MWWD had anticipated executing another \$477.7 million from fiscal year 2005 through fiscal year 2007 had they been able to get to the capital market by early spring 2005. The Water Department anticipated executing another \$305.8 million from fiscal year 2005 through fiscal year 2007 based on getting to the capital market in the fall of 2005.

APPROPRIATIONS FY05 – FY07
(Inflated and in millions of dollars)

	FY 2005	FY 2006	FY 2007	FY'05-07 TOTAL
Total Sewer	\$155.4	\$155.9	\$166.4	\$477.7
Total Water	\$113.3	\$94.5	\$98.0	\$305.8

As of mid December 2004, both departments have ceased awarding new contracts for their CIP programs. This was done to ensure the City does not obligate itself to contracts it may not be able to fully fund without additional financing. The Water Department has sufficient funding to continue work on vital Water Treatment Plants and major pipelines in FY05 and FY06, pursuant to existing phase funded contracts.

This curtailment decreases the need for appropriations in fiscal year 2005 by \$48.6 million for MWWD and \$24.1 million for the Water Department. The capital improvement appropriations for the first half of fiscal 2006 will be \$10.6 million for MWWD and \$55.1 million for the Water department.

The impact to the remainder of fiscal year 2006 and beyond is contingent upon the City's ability to obtain public financing.

APPROPRIATIONS as RESCHEDULED

(Inflated and in millions of dollars)

	FY 2004	FY 2005	FY 2006 Thru 12/31/2005	TOTAL
Total Sewer	\$163.4	\$106.8	\$10.6	\$280.8
Prior Sewer	163.4	155.4		
Change	<u>\$0.0</u>	<u>(\$48.6)</u>		

	FY 2004	FY 2005	FY 2006 Thru 12/31/2005	TOTAL
Total Water	\$116.8	\$89.2	\$55.1	\$261.1
Prior Water	116.8	113.3		
Change	<u>\$0.0</u>	<u>(\$24.1)</u>		

How the capital improvement program is funded:

The capital improvement programs are financed with cash, grants, loans, and debt financing. Cash financing (Pay As You Go) involves using current revenues or cash on hand, whereas debt financing involves leveraging debt to spread the acquisition expense over a period of years. Grants come from the state and federal government and generally require matching contributions. Loans are acquired from the state (State Revolving Fund – SRF) to supplement the program when interest rates are favorable.

MWWD began its capital program in 1993. Since 1993, 53.03% of MWWD's capital program has been debt funded.

**METROPOLITAN WASTEWATER DEPARTMENT
EXPENDITURES & FUNDING SOURCES**

FY 1993 THROUGH FY 2004

(In millions of dollars)

	METRO		MUNI		TOTAL	
	Dollars	Percent	Dollars	Percent	Dollars	Percent
Total Expenditures	\$1,554.8		\$690.7		\$2,245.5	
Pay As You Go	\$275.2	17.70%	\$401.1	58.07%	\$676.3	30.12%
Debt Financing	\$904.8	58.19%	\$286.1	41.42%	\$1,190.9	53.03%
Grants/Loans	\$374.8	24.11%	\$3.5	0.51%	\$378.3	16.85%

The Water Department began its capital program in 1998. The Water Department has funded its capital program using 67.04% debt financing.

**WATER DEPARTMENT
EXPENDITURES & FUNDING SOURCES**

FY 1998 THROUGH FY 2004

(In millions of dollars)

	TOTAL	
	Dollars	Percent
Total Expenditures	\$576.5	
Pay As You Go	169.0	29.31%
Debt Financing	\$386.5	67.04%
Grants/Loans	21.0	3.64%

The last MWWD capital financing occurred in March 1999 for \$315 million. Due to the issues surrounding the City's disclosure documents, they were not able to complete a capital financing and refinancing in September 2003 for \$506 million. In June 2004 MWWD was able to secure interim financing of \$152 million to continue the CIP on schedule.

Bond Issuance	Total
1993	\$250
1995	350
1997	250
1999	315
2004 (Interim Financing)	152
	\$1,317

The last Water Department capital financing occurred in August 2002 for \$201 million (The total financing was for approximately \$286.9 million, of which \$86 million was a refunding of a prior financing). They planned on being back to the bond market by September 2005 in order to continue their CIP on schedule.

**WATER DEPARTMENT
WATER BOND ISSUANCES – NEW MONEY**

(In millions of dollars)

Bond Issuance	Total
1998	\$385
2002	201
	\$586

The Water Department has sufficient resources to continue Water Treatment Plant and major Pipeline Capital Improvements through the end of Fiscal Year 2006. All other new capital work will not be awarded until the City is able to get back to the bond market.

The current impact of funding limitations to MWWD and Water Department capital programs:

MWWD and the Water Department have been closely monitoring their cash needs. They have been careful to only award contracts that would be fully funded without the need for new capital financing. Both departments have the resources necessary to fund all current contractual obligations. We have communicated the status of our programs to the contracting communities.

MWWD and Water utility operations and maintenance will not be impacted. Planning and design of delayed and future projects will continue. Sufficient funding is planned to support engineering staff in MWWD, Water, and E&CP through calendar year 2005, for those activities so that the Departments will have the ability and the resources to ramp up quickly and smoothly once debt financing is in place to proceed with the CIP execution.

Through the end of calendar year 2004, the Water Department has met all obligations related to the capital program with the Department of Health Services and MWWD has met all obligations to the Environmental Protection Agency. The Water Department and MWWD are meeting with their respective regulatory agencies to inform them of the rescheduling of projects and to discuss with them how we plan to maintain the systems in the interim. It is likely the City will not be able to comply with some milestones in the existing U.S. Environmental Protection Agency (EPA) Administrative Order the proposed consent decree as well as the California Department of Health Services (DHS) Compliance Order.

CONCLUSION

The City will begin the process of accessing the public financing market once fiscal year 2003 and 2004 audited financials are complete. The duration of this process is dependent on several factors including the policies and procedures that will be developed by the Disclosure Practices Working Group. However, both MWWD and Water operations and maintenance should not be significantly affected by this, and as such, customers should see no service impacts.

MWWD has sufficient resources to complete all wastewater projects currently in construction including those that are phase funded. The Water Department has sufficient resources to complete water projects currently in construction, and to continue water treatment plant and major pipeline projects through the end of fiscal year 2006.

Both departments are continuing the design and engineering of delayed and future projects in order to ramp up the program as smoothly and quickly as possible once debt financing is restored. The departments will continue to meet with the contracting community on a regular basis to ensure they are informed on the progress of our program.

Both departments will also continue discussions with the regulatory agencies concerning the status of our programs and on how we will maintain the systems in the interim.

Staff reductions and/or furloughs may be required for MWWD, the Water Department and Engineering and Capital Projects if debt financing is not in place by January 2006. The City may also not be able to meet the requirements of the regulatory agencies until the projects are back on schedule.

Respectfully submitted,

Richard Mendes
Deputy City Manager

Approved: P. Lamont Ewell
City Manager

RM/RG:sml