



TAHOE CITY PUBLIC UTILITY DISTRICT

MEMORANDUM

TO: Board of Directors **DATE:** March 17, 2022
FROM: Sean Barclay
General Manager **SUBJ:** Long-Term Financial Planning -
Water System Reconstruction Capital Funding
Alternatives

RECOMMENDATION:

The Board receive a presentation and provide feedback on the District's Long-Term Financial Planning (LTFP) process. The District's LTFP team will provide a presentation to the Board outlining the potential capital funding alternatives the District can consider for the necessary system reconstruction of the Tahoe Cedars and Madden Creek water systems and introduce important related policy considerations.

BACKGROUND:

Since acquiring the former privately-owned Tahoe Cedars (TC) and Madden Creek (MC) water systems in 2018, the District has spent considerable time and resources in performing emergency repairs, completing system master plans and completing several capital improvement projects. Beginning in early 2021, with the adoption of the TC and MC Master Plans, which call for the complete replacement of both systems, the District began long-term financial planning efforts specifically designed to determine how the District might generate enough revenue to fund the estimated \$46M necessary to complete the system reconstructions (not including privately owned service relocations). In recognition of the magnitude of these costs, the District has been concurrently working to identify other existing District priority projects, including other critical water infrastructure projects, sewer projects and parks and recreation projects, so that a comprehensive approach to project prioritization and funding development can be completed.

The Board has expressed interest in pursuing debt financing for the TC and MC system reconstruction projects. To prepare the Board for this discussion, the District's LTFP team worked with the District's LTFP Ad-Hoc Committee to prepare a presentation which outlines potential capital funding alternatives the District may consider pursuing. The funding alternatives presented can be used individually or in combination to provide the necessary revenue to secure debt financing. The goal of the presentation is to answer questions, gain feedback from the Board and determine if there is a consensus on a general approach moving forward.

The presentation will also introduce important policy considerations for the Board to explore in-depth at a future meeting. The District's Water System Acquisition Policy provides the Board with broad latitude in selecting mechanisms necessary to guarantee funding for debt issuance when significant expenditures need to be made to meet minimum District and regulatory standards.

STRATEGIC FOCUS AREA:

- Long-Term Financial Sustainability
- Infrastructure & Property – Protection and Improvement

FINANCIAL IMPACTS:

No financial impact.

ATTACHMENTS:

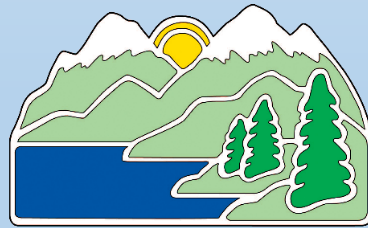
- Long-Term Financial Planning Presentation – Tahoe Cedars and Madden Creek Water System Reconstruction Capital Funding Alternatives
- Capital Funding Alternatives Outline
- TCPUD Financial Policy No. 2025 – Water System Acquisition Policy

REVIEW TRACKING:

Submitted By: Sean Barclay
Sean Barclay
General Manager

Long-Term Financial Planning

Tahoe Cedars and Madden Creek Water System Reconstruction Capital Funding Alternatives



Tahoe City Public Utility District

Long-Term Financial Planning (LTFP) Team

Consultant Team

- Ken Dieker, Municipal Advisor, Principal, Del Rio Advisors, LLC
- Shawn Koorn, Associate Vice President, HDR Engineering Inc.
- Martin Rauch, Principal Consultant, Rauch Communication Consultants, Inc.
- Steve Gross, District Counsel

Ad-Hoc Committee

- Director Pang
- Director Wilkins



Today's Goals

- Discuss funding alternatives for reconstructing the Tahoe Cedars and Madden Creeks water systems
- Discuss policy considerations regarding customers paying a share of reconstruction costs (above and beyond rate revenue)
- Discuss next steps in LTFP process
- Receive feedback



LTFP – Past Discussions

May 21, 2021 - Tahoe Cedars & Madden Creek Water Infrastructure Funding Discussion – Part 2

Board Feedback:

- Interest in evaluating customer willingness towards contributing financially to speed up the pace of system reconstruction
- Hire Communications consultant and develop communications strategy – bring back to Board for review



Tahoe Cedars & Madden Creek System Reconstruction Costs

Madden Creek Water System Reconstruction Cost	\$8M
Tahoe Cedars Water System Reconstruction Cost	<u>\$38M</u>
<i>Total Estimated Costs</i>	\$46M

- ❖ No private water infrastructure included (service line relocations)
- ❖ Estimated annual debt service payment: \$2.87M
- ❖ Plus debt service coverage (x 1.20) = \$3.44M
- ❖ 30-year amortization period
- ❖ Bond Rates @ 4%



Capital Funding Alternatives

Available funding mechanisms to pay for reconstructing the Tahoe Cedars & Madden Creek Systems

All or portions of the reconstruction costs (either on a pay-go or debt financing basis) could be paid for by:

- Water rate revenue paid by entire rate base
- Special capital surcharge for Tahoe Cedars/Madden Creek system customers
- Property tax revenues (possible offset to 1 or 2 above)
- Benefit Assessment District

Considered but not recommended

- *Mello-Roos Special Tax*
- *General Obligation Bonds*
- *Parcel Tax*
- *General Fund Lease Financing*



Capital Funding Alternatives

Water rate revenue paid by entire rate base - (paid through annual rates charged to all customers)

➤ Discussion Points:

- In keeping with past practice of funding capital improvement needs through general system rates
- Improvements for these systems are not “normal” or routine improvements because of acquisitions
- Would need to comply with Proposition 218 requirements when setting rates

➤ Advantages:

- Proposition 218 process to set rates (lower threshold for adoption vs. benefit assessment, Mello-Roos special tax, parcel tax or general obligation bonds)

➤ Disadvantages:

- Not equitable to current rate base when funding these “out of the ordinary”, full reconstruction costs for the Tahoe Cedars and Madden Creek service areas



Capital Funding Alternatives

Specific rate or charge for Tahoe Cedars/Madden Creek customers - (Capital Surcharge)

➤ Discussion Points:

- Rate or charge reflects the capital costs specific to the customers of the system
- Would reflect the uniqueness of the required improvements for these customers
- Would need to comply with Proposition 218 requirements for establishing the surcharge or rate
- Surcharge is the better option – set at amount necessary to pay debt service and keep it for the duration of the debt service period as opposed to rates, which would require Prop 218 process every 5 years
- Likely needs to be accomplished through two separate rate studies (could be done simultaneously)
- Consider establishing “operational rate”, “capital rate” and “special capital surcharge” (specific to only TC and/or Madden Creek)
- Consider whether TC/MC Customers also pay into District-wide “capital rate” or not

Note:

- (1) Surcharge can continue for length of obligation with no further 218 proceedings if the fixed surcharge charge does not increase. Would structure level debt service to keep the surcharge fixed throughout the term of any obligation used to finance the improvements
- (2) Would require entire District rates and charges to backstop the debt even though internal source of repayment would be the specific rate or surcharge



Capital Funding Alternatives

Property tax revenues - (paid using District property tax revenue collected from all customers)

- Discussion Points:
 - Board has discretion on how to use property tax revenues
- Advantages:
 - No Proposition 218 process
 - Reduced water rate or surcharge impacts
- Disadvantages:
 - Significantly impacts parks and recreation projects, future expansion of programming and flexibility to respond to community needs/changes
 - Potential for a decline in property tax revenue due to reduced assessed values



Capital Funding Alternatives

Benefit Assessment District - (assessment charged to property owner and repaid through the annual property tax bill)

➤ Discussion Points:

- Would require specific assessment district approach and process
- Customer vote for approval, weighted by value of the benefit to the property
- Requires an engineering report outlining benefit, and calculation, for each parcel

➤ Advantages:

- Can set specific boundaries (Tahoe Cedars and Madden Creek service areas)
- Does not require proposition 218 process
- Lower voter threshold than Mello-Roos at 50% +1
- Lower debt service coverage requirement than water revenue bonds (1.10x vs. 1.20x)

➤ Disadvantages:

- Requires Assessment Engineer's report to determine benefit to each parcel
- High cost to Tahoe Cedars and Madden Creek customers
- Requires an affirmative vote (50%+1) rather than the protest threshold with Prop. 218
- Requires administration of a separate district once formed



Financial Impacts of Funding Alternatives

If reconstruction costs of \$46M were paid via debt financing solely by:

- Property tax revenues = \$2.87M^(*)/year
 - In 2021, District had \$5.8M of available property tax after P&R operations
 - District has \$565K/year of General Fund debt service for the \$20M WLTRWTP SRF
- All water customers = \$3.44M^(*)/year
 - 5,740 customers
 - Additional \$600/year = \$50 / per customer / per month
- Tahoe Cedars/Madden Creek Customers = \$3.44M^(*)/year
 - 1,410 customers
 - Additional \$2,440/year = \$203 / per customer / per month

Note: (*) \$2.87M annual debt service x 1.20 for debt service coverage = \$3.44M



Recommendation

Pursue a blend of:

- Water rate revenue from all water customers
- Specific capital surcharge for Tahoe Cedars/Madden Creek system customers
- Property tax revenue as offset to water rates or surcharge

**TCPUD Financial Policy No. 2025 - Water System Acquisition Policy –
allows board to pursue all options we have discussed today**



Future Board Policy Considerations

- Capital surcharge for TC/MC system customers (policy considerations):
 - **District may not be able to afford full reconstruction** under current rate structure alone
 - **Need to find equitable funding approach** that balances use of property taxes, general water rate for all customers, possible capital surcharge for TC/MC customers
 - Whatever is done here may set a precedent for future water system acquisitions
- TC/MC customers level of financial responsibility for infrastructure replacements
 - Set policy direction on % of overall system improvement costs
- TC/MC property owner responsibility for private infrastructure relocations
 - Mechanisms for property owner (no/low interest loan program)



Next Steps

Future presentations for the Board:

- Review 10-year capital program scenarios and related financial impacts
- Evaluate overall District borrowing capacity for both water and parks/recreation facility projects
- Evaluate policy considerations and provide policy direction
- Evaluate debt financing options



Next Steps – 10-Year Capital Scenarios

Team will present revenue requirements (using combination of water rates, property taxes, and other capital funding alternatives) needed to fund three (3) 10-Year Capital Plan scenarios (Water and General Fund):

- Each will include the same slate of pay/go rehabilitation and replacement projects – \$1.5M/year Water Fund + \$500k/year General Fund on average.
- Scenarios will present different slates of projects for debt financing:
 - 1) MINIMUM NEEDED CIP FINANCING: Projects necessary for end-of-life, legal, and/or regulatory requirements or prior commitments.
 - 2) BALANCED/PRIORITIZED CIP FINANCING: All above projects plus some additional projects to further address end-of-life, safety, and service-level requirements.
 - 3) MAXIMUM POTENTIAL CIP FINANCING: All prioritized projects identified to Board in February (\$81.3M Water and General Fund Projects)



Questions, Comments, Feedback?



Capital Funding Alternatives Outline For the Reconstruction of the Tahoe Cedars/Madden Creek Water Systems

1. Water rate revenue paid by entire rate base (paid through annual rates charged to all customers)

- a. Discussion:
 - In keeping with past practice of funding capital improvement needs through general system rates
 - Improvements for these systems are not “normal” or routine improvements because of acquisitions
 - Would need to comply with Proposition 218 requirements when setting rates
- b. Advantages:
 - Proposition 218 process to set rates
- c. Disadvantages:
 - Not equitable to current rate base when funding these “out of the ordinary”, full reconstruction costs for the Tahoe Cedars and Madden Creek service areas

2. Specific Rate for Tahoe Cedars/Madden Creek Customers (capital surcharge)

- a. Discussion:
 - Rate or charge reflects the capital costs specific to the customers of the system
 - Would reflect the uniqueness of the required improvements for these customers
 - Would need to comply with Proposition 218 requirements for establishing the surcharge or rate
 - Surcharge is the better option – set at amount necessary to pay debt service and keep it for the duration of the debt service period as opposed to rates, which would require Prop 218 process every 5 years
 - Likely needs to be accomplished through two separate rate studies (could be done simultaneously)
 - Consider establishing “operational rate”, “capital rate” and “special capital surcharge” (specific to only TC and/or Madden Creek)
 - Consider whether TC/MC Customers also pay into District-wide “capital rate” or not

Note:

Surcharge can continue for length of obligation with no further 218 proceedings if the fixed surcharge charge does not increase. Would structure level debt service to keep the surcharge fixed throughout the term of any obligation used to finance the improvements

Would require entire District rates and charges to backstop the debt even though internal source of repayment would be the specific rate or surcharge

- b. Advantages:
 - Prop 218 – protest vote

- Would be equitable to the current rate base
- c. Disadvantages:
 - Prohibitive cost to Tahoe Cedars and Madden Creek customers
 - Specific, and separate Prop 218 process for surcharge customers
 - Would require entire District rates and charges to backstop the debt even though internal source of repayment would be the specific rate or surcharge
 - May require subsidy (property tax or cash reserves)

3. Property tax revenues (paid using District property tax revenue collected from all customers)

- a. Discussion:
 - Board has discretion on how to use property tax revenues
- b. Advantages:
 - No Proposition 218 process
 - Reduced water rate or surcharge impacts
- c. Disadvantages:
 - Significantly impacts parks and recreation projects, future expansion of programming and flexibility to respond to community needs/changes
 - Potential for a decline in property tax revenue due to reduced assessed values

4. Benefit Assessment District (Assessment charged to property owner and repaid through the annual property tax bill)

- a. Discussion:
 - Would require specific assessment district approach and process
 - Customer vote for approval, weighted by value of the benefit to the property
 - Report outlining benefit, and calculation, for each parcel
- b. Advantages:
 - Can set specific boundaries (Tahoe Cedars and Madden Creek service areas)
 - Does not require proposition 218 process
 - Lower voter threshold than Mello-Roos at 50% +1
 - Lower debt service coverage requirement than water revenue bonds (1.10x vs. 1.20x)
- c. Disadvantages:
 - Requires Assessment Engineer's report to determine benefit to each parcel
 - High cost to Tahoe Cedars and Madden Creek customers
 - Requires an affirmative vote (50%+1) rather than the protest threshold with Prop. 218
 - Requires administration of a separate district once formed

5. Mello-Roos Special Tax ("Community Facilities District") (Special Tax charged to property owner and repaid through the annual property tax bill)

- a. Discussion:
 - Would require two meetings to form District (ROI and ROF)
 - Customer vote for approval

- Rate and Method of Apportionment describes the special tax
- b. Advantages:
 - Can set specific boundaries (Tahoe Cedars and Madden Creek service areas)
 - Does not require proposition 218 process
 - Tax formula does not need to show benefits to each property (tax formula extremely flexible)
- c. Disadvantages:
 - Requires 2/3rds voter approval
 - High cost to Tahoe Cedars and Madden Creek customers

6. General Obligation Bonds (Annual tax levied on property tax roll in proportion to total assessed property values)

- a. Discussion:
 - Requires a 2/3rds voter approval
 - Voters approve total bond authorization and use of proceeds, not tax rate or annual payment
 - Tax rate is calculated each year around July and based on annual debt service divided by total assessed value for that fiscal year
- b. Advantages:
 - Best used when there is broad-based support for Public Improvements
 - Highest rating and lowest interest cost due to ad valorem security and unlimited tax pledge
 - Generates new revenue source to repay debt
 - No reserve fund required as this is the most secure form of municipal debt
 - Taxes based off assessed value, not market value of Property
 - No annual administration as debt service is collected by the County and sent directly to the Trustee to pay investors
- c. Disadvantages:
 - Cannot set boundaries to incorporate only Tahoe Cedars and Madden Creek service areas
 - Time, expense and uncertain outcome of the election
 - Property tax increase
 - Adjacent homes may have different annual taxes depending on when property was purchased per Proposition 13
 - No ability for property owner to prepay tax obligation
 - Cannot fund equipment, maintenance or other projects not defined as capital improvements

7. Parcel Tax (Fixed amount charged per parcel per year)

- a. Discussion:
 - Like General Obligation Bond structure but instead of charging \$ per \$100k of assessed value it is a fixed annual charge
- b. Advantages:

- Tax is specific to the intended purpose approved by the voters
- c. Disadvantages:
 - Property tax increase, repaid on the property tax bill like a General Obligation Bond
 - Requires a 2/3rds voter approval
 - Cannot be specifically pledged to the repayment of bonds
 - Generally combined with one of the lease financing structures to issue an obligation

8. General Fund Lease Financing (Lease-Leaseback Structure) aka “Lease Revenue Bonds” / “Certificates of Participation”

- a. Discussion:
 - Not subject to constitutional debt limits per Offner-Dean Lease Exception
 - Lease-Leaseback structure with third-party entity a joint power authority “JPA” of the local agency aka public financing authority “PFA”
 - Lease an asset to the PFA and lease it back with payments equivalent to debt service on the bonds
 - Issuer covenants to appropriate annual lease payments from General Fund
 - Lease subject to abatement if no longer have “use and occupancy” of the asset
 - Lease cannot be accelerated
 - Lease payments must equal “fair rental value”
 - Must fund capitalized interest if leased asset is the one being constructed
 - Requires unencumbered leasable assets
 - Lease term cannot exceed useful life of the improvements
- b. Advantages:
 - No voter approval required
- c. Disadvantages:
 - Increases General Fund burden to make lease payments

Tahoe City Public Utility District Financial Policy

Water System Acquisition Policy Policy Number: 2025

I. PURPOSE

This policy is established to provide guidance and set forth the approach and process that the Tahoe City Public Utility District will take during the acquisition of water systems. This policy is intended to provide the background, intent, and process that will be followed in a variety of acquisition situations.

II. POLICY OVERVIEW

In 1939, the people of Tahoe City voted to form the Tahoe City Public Utility District with the primary purpose of acquiring the existing private water system in order to better serve the community's needs. Over the decades since, the community-based TCPUD has continually expanded its service area by acquiring water systems from investors, owners, and developers. Consideration of acquisitions of water companies and water systems is an essential component of fulfilling the District's mission and responsibilities. The District intends to continue to address and respond to the changing water needs in the community and provide safe and reliable water service for the protection of public health and provide for the equitable future use of property tax revenues.

The District has acquired water companies and water systems based upon the following rationale and benefits:

- Overall community health, safety, and well-being;
- Governmental responsibility and fairness to all taxpayers;
- Historical precedence;
- District-wide cost-savings and efficiencies realized by adding additional customers and revenues to cover the fixed and operational costs of the District's system; and,
- Cost-savings and efficiencies realized by reducing unnecessary duplication of administrative and general overhead costs and in water system facilities and infrastructure.

The evolution of the District's water delivery system has resulted in separate, independent water systems that comprise the District's total system and require duplication in water sources, storage and infrastructure, some of which would be unnecessary if not for the geographical separations. As the District strives for increased efficiencies, it is hampered by this inefficient infrastructure. It is beneficial to the overall community to consolidate, share resources, and address water needs in a planned and organized manner.

Over time, the District's water customers (ratepayers) have grown as a percentage of total District taxpayers and extensive historical research indicates that the District's existing water systems were acquired and upgraded using almost exclusively property tax revenues paid by all taxpayers in the District.

III. DEFINITIONS

As used in this policy, the following terms shall have the meanings specified below:

- a. Board – The lawfully elected or appointed governing body of the TCPUD.

- b. Constituents - Residents, property owners, taxpayers, ratepayers, customers, beneficiaries of services, business owners, and voters within the District's boundaries.
- c. District – The Tahoe City Public Utility District (District or TCPUD).
- d. Policy – This “Water System Acquisition Policy.”
- e. Proposition 218 - In November 1996, California voters passed Proposition 218, the “Right to Vote on Taxes Act”. This constitutional amendment protects taxpayers by limiting the methods by which local governments can create or increase taxes, fees and charges without taxpayer consent.
- f. Property tax revenues – Property tax revenue shall mean property tax revenue received by the District from Placer and El Dorado counties.

IV. PROCESS

General

The District respects the assets and ownership rights of private water system owners; therefore, the District will only consider acquisition of private or mutual water company systems on a case-by-case basis as outlined below:

- The owner of a private water company advises the District that they are interested in selling their water system;
- Customers of a private or mutual water company within the District's service area boundary advise the District that they are dissatisfied with their current water purveyor, and two-thirds of the owners of private parcels located within the system make a request that their water system be acquired by the District;
- Other circumstances as specifically determined by the Board of Directors;
- The District, other public agencies with jurisdictional authority over the District or a private or mutual water company, or a court of law makes a determination that due to an imminent public health or safety threat, public interest and necessity dictate that it should acquire the system through receivership, eminent domain or other legal means.

In any event, the decision to commence acquisition of any water company shall be at the discretion of the District's Board of Directors.

The District has limited ability to assist investor-owned water company customers. Regulation of these water companies is generally the responsibility of the California Public Utilities Commission (CPUC) and the California State Water Resources Control Board, Division of Drinking Water. The District can enter into a contractual relationship, negotiate an outright purchase, take possession through a receivership, or use contested or uncontested eminent domain proceedings to acquire the water company.

The District may authorize an independent appraisal of the water company value and a reconnaissance level engineering study, including some or all of the following: a review of the water company's existing facilities; analysis of the District's ability to serve the system; evaluation of the necessary or immediate improvements to meet minimum District or regulatory standards; preliminary cost estimates as relevant; and preparation of a financing plan. The District may use other methods as necessary to determine the value of a water system with Board approval.

The District may utilize its property tax revenues, grant funds, or loans pledged from the new customer revenues, as well as new net revenues gained from additional customers, to acquire and improve water systems. New net

revenues may also include surcharges or assessments imposed upon the additional customers being acquired. The District reserves the right to time acquisitions and necessary improvements according to funding availability and prioritization of need throughout its entire system.

Consistency and Equitability

For purposes of meeting legal rate setting requirements (i.e., CA Constitution Article 13D) and to provide consistency and equitability between customers, the District will require all new customers to pay the Board adopted rates in effect at the time of the acquisition. The District may consider a rate transition plan in the event that the acquired systems are unmetered and/or its existing rates are lower than the average District customer water rate. The District may utilize its property tax revenues for the rate transition plan. The District may require an additional surcharge or assessment if immediate, significant capital expenditures are required to serve the new customers in order to meet Minimum ⁽¹⁾ District or regulatory standards, including, but not limited to, fire suppression, water meter installation, source redundancy and distribution system improvements.

The District may require a Proposition 218 protest process for implementation of District rates on new customers. The District may also initiate the formation of an improvement district, assessment district, or other legal mechanism in order to guarantee funding for debt issuance if significant immediate expenditures need to be made to a water system to meet minimum District or regulatory standards. The funding for such mechanism will be implemented through a Proposition 218 vote process, if required by law.

Safe and Adequate Water

Based upon the critical importance of safe, adequate water for the community's well-being, the Board finds that:

- The District will consider the entire community's overall water needs when planning and sizing water resources and infrastructure so that, to the extent reasonably and fiscally possible, such water system infrastructure can accommodate eventual connections by all District taxpayers, regardless of their current water system provider. The District may consider entering into joint exercise of powers and contractual agreements with public and private water providers where the District determines that to do so is in the best interest of the District and its customers.
- Consolidation of the District's water systems with other public and private water systems results in greater efficiencies, less duplication, and improved public health and safety benefits for all constituents within District boundaries. Therefore, the District may seek to acquire water systems as funding is available and in accordance with the guidelines established herein.
- Rebuilding or repairing existing water system infrastructure or constructing new water system infrastructure sized to meet current fire flow and storage requirements is beyond the capacity of the District's rate revenues alone. Therefore, property tax revenue, as available, may be used to supplement rate revenue to fund water system reconstruction and improvements sized for existing and future customers that best addresses applicable current legal mandates and regulatory requirements.
- Persons and entities owning property within the District's boundaries pay taxes which have been used in part for the acquisition, development and improvement of facilities and systems that are now part of the existing District water system. This Policy seeks to ensure that future expansion and improvements to the public water system will continue this historical practice and future customers will benefit from the use of property tax in both acquisitions and/or improvements.
- The District's adopted cost of service analysis and rate structure is estimated to produce adequate revenues to fund all operational costs and prudently maintain the annual renewal and replacement costs of District water system infrastructure. This formula may be applied to all future water customers through the District's water

rate structure.

- The District has established a Water System Acquisition and Infrastructure Improvement Property Tax Reserve to provide the ability to continue to address and respond to the changing water needs in the community and provide for equitable future use of property tax.

¹ “Minimum” District or regulatory standards will be evaluated and determined on a case-by-case basis by District management and staff in consultation with appropriate agencies and the Board of Directors.