



CITY OF SAN MATEO

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Agenda Report

Agenda Number: 17

Section Name: {{section.name}}

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TO: City Council
FROM: Drew Corbett, City Manager
PREPARED BY: Finance Department
MEETING DATE: May 17, 2021

SUBJECT:

2021 Wastewater Revenue Notes to Finance Clean Water Program Costs and 2021 Wastewater Revenue Bonds to Refund Sewer Revenue Bonds 2011 Series A – Approval

RECOMMENDATION:

Adopt a Resolution to approve the documents and actions relating to the sale of 2021 Wastewater Revenue Notes, Series B by the San Mateo-Foster City Public Financing Authority in the maximum amount of \$295,480,000 to finance Clean Water Program capital costs related to wastewater treatment plant and sewer collection improvement projects and the sale of 2021 Wastewater Revenue Bonds, Refunding Series A in the maximum amount of \$25,000,000 to refund the City of San Mateo Sewer Revenue Bonds, 2011 Series A.

BACKGROUND:

Clean Water Program Capital Costs

In 2009, the Regional Water Quality Control Board issued a Cease and Desist Order requiring the City of San Mateo ("City"), the Town of Hillsborough, and the Crystal Springs County Sanitation District to take specific actions to eliminate the occurrence of sanitary sewer overflows. In order to comply with the 2009 Cease and Desist Order, the City developed a preliminary 10-year Integrated Wastewater Master Plan (the "Clean Water Program") calling for a major upgrade to the wastewater treatment plant (the "WWTP") owned jointly by the City and the Estero Municipal Improvement District (the "District"), and improvements to the City's collection system. Current estimated costs for all improvements are approximately \$986 million. The City's share is \$832.3 million, of which \$330.7 million is for collection and \$501.6 million is for the WWTP. The \$501.6 million includes the shares attributable to Hillsborough (\$30.1 million), the Crystal Springs County Sanitation District (\$13.3 million) and the County of San Mateo (\$740,500) (collectively, the "Regional Customers"). The Regional Customers will repay the City over time for their respective shares via an annual capacity charge.

The City requires financing to complete these improvements. The City and the District established the San Mateo-Foster City Public Financing Authority ("Authority") in 2016 to facilitate the financing of both agencies' capital contributions to the WWTP upgrade project. The Authority may be used by either member to facilitate any capital financing.

The following table shows current estimated Clean Water Program sources and uses of funds.

**San Mateo-Foster City Public Financing Authority (PFA)
Clean Water Program
Sources and Uses of Funds**

	San Mateo¹	Foster City	Total
Sources			
WWTP WIFIA Loan	\$ 210,339,360	\$ 66,860,640	\$ 277,200,000
Basin 2/3 WIFIA Loan	\$ 85,140,000	\$ -	\$ 85,140,000
Revenue Bonds/SRF ²	\$ 386,727,326	\$ 73,807,594	\$ 460,534,920
Cash	<u>\$ 150,108,919</u>	<u>\$ 12,981,012</u>	<u>\$ 163,089,931</u>
Total Sources	\$ 832,315,605	\$ 153,649,247	\$ 985,964,851
Uses			
Program Management	\$ 72,368,591	\$ 9,924,553	\$ 82,293,144
Misc. Collection	\$ 144,930,063	\$ -	\$ 144,930,063
Basin 2&3 Collection	\$ 162,381,428	\$ -	\$ 162,381,428
Other WWTP	\$ 36,778,684	\$ 11,536,146	\$ 48,314,830
WWTP - WIFIA	<u>\$ 415,856,839</u>	<u>\$ 132,188,547</u>	<u>\$ 548,045,386</u>
Total CIP	\$ 832,315,605	\$ 153,649,247	\$ 985,964,851

Notes:

¹ Includes Subregional Customers

² Includes Original Issue Discount

PLAN OF FINANCE

The plan of finance consists of six funding sources: (1) loans to each city for the WWTP from the United States government under the Water Infrastructure Finance and Innovation Act (“WIFIA”) loan program administered by the EPA (the “WWTP WIFIA Loan”), (2) a second WIFIA loan to the City only for the Basins 2 and 3 portion of the collection system improvements (the “Collection WIFIA Loan” and collectively, the “WIFIA Loans”), (3) wastewater revenue notes that will fund construction draws in lieu of direct draws on the WIFIA Loans and which will be repaid with a single draw on each of the WIFIA Loans in 2025, (4) free cash flow (surplus revenues over expenses) produced by each city’s sewer enterprise, (5) a loan from the State of California issued under the State Revolving Fund (SRF) loan program, and (6) revenue bonds secured by each city’s respective sewer enterprise revenues. The first such financing was revenue bonds issued by the Authority in 2019. Additional revenue bonds are not expected to be needed if the State approves the requested SRF loan.

The City has closed both the WWTP WIFIA Loan and the Collection WIFIA Loan but has not made any draws on either loan. The 2021 Wastewater Revenue Notes, Series B (“Series B Notes”) are part of the wastewater revenue notes identified in (3) above, and the sale of 2021 Wastewater Revenue Bonds, Refunding Series A (“Refunding Series A Bonds”) to replace the City of San Mateo Sewer Revenue Bonds, 2011 Series A (“2011 Bonds”) are the subject of this staff report. Other information is provided for context.

Cash

Pay-go financing, which carries no interest charge, is the least expensive way to finance capital projects. The City’s municipal advisors have developed a cash flow and debt financing financial projection model to estimate the optimal combination of loans (WIFIA and SRF), revenue bonds, and cash for the City’s share of the WWTP and its collection system capital needs. Free cash flow not necessary for reserves and the collection system will be applied to WWTP capital costs. This amount is expected to be approximately \$150.7 million through 2027.

Revenue Bonds

The Authority sold \$270 million 2019 Wastewater Revenue Bonds (the “2019 Bonds”) for Clean Water Program costs for both cities. The 2019 Bonds were marketed with an original issue premium (the coupons attached to maturity dates were higher than market yields for those maturities) that generated an additional \$53.8 million in bond proceeds. As such, the

total bond proceeds received by the Authority from the 2019 Bonds was \$323 million, of which the City's share of proceeds was \$282.7 million. Of that amount, \$20 million was applied to pay off a sewer enterprise State Street Bank line of credit, \$18.2 million to reimburse the sewer enterprise for prior capital expenditures, \$166.4 million was made available for collection capital costs, and \$78.1 million was made available for WWTP capital costs. The \$78.1 million is expected to be substantially depleted by July 2021 and the \$166.4 million fully expended by March 2022.

WWTP WIFIA Loan

The City and the District have secured WWTP WIFIA Loans in an aggregate amount not to exceed \$277.2 million under the WIFIA loan program administered by the EPA for the WWTP upgrade costs. The City's maximum WWTP WIFIA Loan is \$210,339,360. The City Council approved the loan and related actions on October 19, 2020, and the Authority followed suit on October 22, 2020. The loan was closed on November 5, 2020. This loan is expected to be sufficient to fund the City's WWTP capital obligations until 2023 (with a proviso that WWTP wastewater revenue notes, which are less costly than loan draws, will be substituted for loan construction draws, and be repaid with a single draw on the WWTP WIFIA loan on August 1, 2025), at which time an SRF loan is expected to be available. If the SRF loan does not come to fruition, the Authority will sell additional revenue bonds.

Collection WIFIA Loan

The City also secured a \$85,140,000 Collection WIFIA loan. This loan closed on December 17, 2020. 2019 Bond proceeds are projected to be sufficient to fund collection CIP costs through March 2022, at which time additional capital funding will be required. Although the City could draw directly on the Collection WIFIA Loan, staff believes it will be more cost effective to sell collection wastewater revenue notes at this time and use the Collection WIFIA Loan to repay the collection wastewater revenue notes on August 1, 2025.

Series B Notes

The interest cost on 4-year Series B Notes is presently less than the interest cost on the WIFIA Loans. Rather than use draws on the WIFIA Loans to fund construction, the plan is for the Authority to sell 4-year Series B Notes to fund amounts that would have been drawn on the two City WIFIA Loans. The Series B Notes will be paid off with a single draw on each of the City WIFIA Loans, while the Series A Notes for the District will be paid off with a draw on its WWTP WIFIA Loan. The Authority's underwriter, BofA Securities, estimates that Series B Notes will allow the City to realize net present value savings of approximately \$4.1 million over direct draws on the WWTP WIFIA Loan and \$1.5 million over direct draws on the Collection WIFIA Loan. The following table summarizes the results of the Series B Notes versus direct draw on the WWTP WIFIA loan analysis, followed by another table that looks at Series B Notes versus direct draws on the Collection WIFIA loan. These analyses by BofA Securities show aggregate net present value savings of \$5.6 million for Series B Notes that will be paid off by both the WWTP WIFIA loan and the Collection WIFIA loan, instead of drawing on those loans for construction, based on market levels as of 4/7/21 for a 4-year final maturity. A 3-year term was also examined as a structuring alternative, but the 4-year term produces greater savings at this time.

CITY OF SAN MATEO WWTP

Scenario	WIFIA Loan Only	Note + WIFIA Loan Takeout	
		3-Year Term	4-Year Term
Delivery Date		7/1/2021	7/1/2021
Maturity Date	8/1/2055	8/1/2024	8/1/2025
Coupon	1.32%	5.00%	5.00%
Yield		0.38%	0.52%
Par Amount		\$ 210,335,000	\$ 204,665,000
Premium		29,758,196	36,995,245
Total Sources		\$ 240,093,196	\$ 241,660,245
Project Fund		\$ 210,339,360	\$ 210,339,360
Capitalized Interest		29,127,757	30,699,750
Cost of Issuance		308,456	309,635
Underwriter's Discount		320,130	311,500
Total Uses		\$ 240,095,703	\$ 241,660,245
Arbitrage Yield		0.47%	0.57%
True Interest Cost		0.43%	0.55%
All-In TIC		0.47%	0.59%
Note Net Interest		\$ 3,298,888	\$ 11,086,021
WIFIA Loan Interest	67,032,288	60,198,597	55,868,789
WIFIA Loan	210,339,360	210,335,000	204,665,000
Total Payments	277,371,648	273,832,485	271,619,810
Savings	-	3,539,163	5,751,838
PV Total Payments	208,639,291	205,172,366	204,512,659
Savings	-	3,466,925	4,126,632
Breakeven Rate		0.90%	0.98%
Spread to Current Yield		0.52%	0.46%

CITY OF SAN MATEO BASIN 2&3

Scenario	WIFIA Loan Only	Note + WIFIA Loan Takeout	
		3-Year Term	4-Year Term
Delivery Date		7/1/2021	7/1/2021
Maturity Date	8/1/2055	8/1/2024	8/1/2025
Coupon	1.31%	5.00%	5.00%
Yield		0.38%	0.52%
Par Amount		\$ 85,140,000	\$ 82,840,000
Premium		12,045,607	14,974,158
Total Sources		\$ 97,185,607	\$ 97,814,158
Project Fund		\$ 85,140,000	\$ 85,140,000
Capitalized Interest		11,792,727	12,426,000
Cost of Issuance		123,297	122,076
Underwriter's Discount		129,583	126,082
Total Uses		\$ 97,185,607	\$ 97,814,158
Arbitrage Yield		0.47%	0.57%
True Interest Cost		0.43%	0.55%
All-In TIC		0.47%	0.59%
Note Net Interest		\$ 1,333,023	\$ 4,487,167
WIFIA Loan Interest	22,079,976	19,487,745	17,900,332
WIFIA Loan	85,140,000	85,140,000	82,840,000
Total Payments	107,219,976	105,960,768	105,227,499
Savings	-	1,259,208	1,992,477
PV Total Payments	84,304,958	83,071,618	82,811,675
Savings	-	1,233,340	1,493,283
Breakeven Rate		0.83%	0.93%
Spread to Current Yield		0.45%	0.41%

SRF Loan

The City has applied to the State of California for a low-interest loan under the State Revolving Loan Fund program, and subject to final credit approval and the availability of funds, has qualified for funding. Funding from that loan would be used in FYE 2023 and FYE 2024. The interest cost on the SRF loan will be at ½ of the State's general obligation bond rate, and is lower than what the City can obtain in the municipal bond market.

The following table shows the estimated sources and uses of funds for the City's sewer enterprise Clean Water Program. To avoid double counting with the WIFIA loans, the Series B Notes, which will be repaid with the proceeds of the WIFIA loans, are not reflected as a separate source of funds in the table.

Sources of Funds (1)	2015 - 2020	2021	2022	2023	2024	2025	2026	2027	Total
2019 Bond Construction Draws	104,081,702	116,681,345	12,740,826	35,214,660	14,053,194	-	-	-	282,771,726
Basin 2/3 Construction Note/WIFIA Loan	-	-	61,842,419	23,297,581	-	-	-	-	85,140,000
WWTP Construction Note/WIFIA Loan	-	5,336,404	173,529,790	31,473,167	-	-	-	-	210,339,360
Bonds/SRF Loan Construction Draws	-	-	-	83,729,685	20,225,915	-	-	-	103,955,600
Cash	73,133,040	-	4,763,522	5,490,281	21,238,774	37,923,602	6,458,668	1,101,032	150,108,919
Total Sources	177,214,741	122,017,748	252,876,556	179,205,374	55,517,883	37,923,602	6,458,668	1,101,032	832,315,605
Uses of Funds (1)	2015 - 2020	2021	2022	2023	2024	2025	2026	2027	Total
Basin 2/3 Collection Project	31,168,255	46,706,009	61,842,419	22,664,744	-	-	-	-	162,381,428
Other Collection Projects	38,298,389	11,922,551	6,795,175	29,834,751	30,040,092	25,192,243	2,846,861	-	144,930,063
WWTP Project	66,440,394	56,954,622	178,293,311	121,325,969	20,867,978	8,625,321	127,927	-	452,635,523
Program Management	41,307,704	6,434,565	5,945,650	5,379,910	4,609,812	4,106,037	3,483,880	1,101,032	72,368,591
Total Uses	177,214,741	122,017,748	252,876,556	179,205,374	55,517,883	37,923,602	6,458,668	1,101,032	832,315,605

REQUIRED APPROVALS

The proposed Authority financing consists of the following three components:

2021 Wastewater Revenue Notes, Series A (Estero Municipal Improvement District);

2021 Wastewater Revenue Notes, Series B (City of San Mateo); and
2021 Wastewater Revenue Bonds, Refunding Series A (City of San Mateo).

2021 Wastewater Revenue Notes, Series A

The District will take legislative action to approve the Authority's sale of the 2021 Wastewater Revenue Notes, Series A (the "Series A Notes"). The District is solely obligated to pay debt service on the Series A Notes and will pay it off with the District's WWTP WIFIA Loan.

2021 Wastewater Revenue Notes, Series B

The City must take legislative action to approve the Series B Notes. The maximum amount of the Series B Notes is \$295,480,000, consisting of \$210,340,000 for San Mateo's share of WWTP improvements and \$85,140,000 for San Mateo collection system improvements. The Series B Notes will be repaid with draws on the City's WWTP WIFIA Loan and the Collection WIFIA Loan.

2021 Wastewater Revenue Bonds, Refunding Series A

The City must also take legislative action to approve the Refunding Series A Bonds. On May 11, 2011, the City issued \$31,990,000 2011 Bonds to finance capital improvements to the City's sewer enterprise and to refund three series of prior sewer revenue bonds. The 2011 Bonds have a final maturity of 8/1/41 and can be optionally redeemed starting on 8/1/21. The current outstanding principal balance of \$19,700,000 has interest rates ranging from 4.15% - 5.25%. Under current federal law, the 2011 Bonds can be refunded starting 90 days prior to the optional redemption date (meaning after 5/1/21). Refunding Series A Bonds would refund and replace the 2011 Bonds, with lower annual debt service.

The City's existing annual debt service payments for the 2011 Bonds is about \$1.7 million for the bond years ending August 1 of 2021 through 2028, stepping down to about \$1.4 million annually thereafter through 2041. The current structure of the Refunding Series A Bonds will generate savings of almost \$500,000 for the first bond year ending 8/1/21 and more than \$300,000 annually thereafter, for aggregate total savings of about \$6.7 million. Net present value savings, which is a measure of future year savings discounted to the present, are approximately \$6.3 million. This is over 41% of the refunding bond issue size.

The City's Debt Policy recommends that a refunding produce net present value savings of at least 3% of the refunding bond issue size. This estimate of savings is based on 4/7/21 market rates and actual savings will not be set until the Refunding Series A Bonds are priced in mid-June. These debt service savings entirely benefit the City's sewer enterprise, as the 2011 Bonds are secured by the sewer enterprise and not by the City's General Fund.

The resolution before the City Council tonight consents to the Authority's sale of the Series B Notes and the Refunding Series A Bonds, approves a Financing Agreement that documents a loan from the Authority to the City, which loan will be pledged to the bond trustee and which will provide the Authority a source of revenue to repay its loan from the Authority, a continuing disclosure certificate that obligates the City to make certain annual disclosures to investors, and information under the caption "THE SAN MATEO SEWER ENTERPRISE" and contained in Appendix A2 to the preliminary official statement that makes certain disclosures relating to the City. The resolution appoints BofA Securities as underwriter and Jones Hall as bond counsel and disclosure counsel. William Euphrat Municipal Finance, Inc. and Kitahata & Company are already under contract to the City as the municipal advisors.

RESPONSIBILITIES OF ELECTED OFFICIALS UNDER FEDERAL SECURITIES LAWS

The preliminary official statement has been reviewed and approved for transmittal to the City Council and the Authority by staff and its financing team. The preliminary official statement must include all facts that would be material to an investor in the Series B Notes and Refunding Series A Bonds. Material information is information that would have a substantial likelihood of actual significance in the deliberations of a reasonable investor in deciding whether to buy or sell the Series B Notes and Refunding Series A Bonds. Members of the City Council and the Authority should review the preliminary official statement and may question staff and consultants to make sure members feel comfortable that it includes all material facts, and in particular, those portions that disclose information relating to the City.

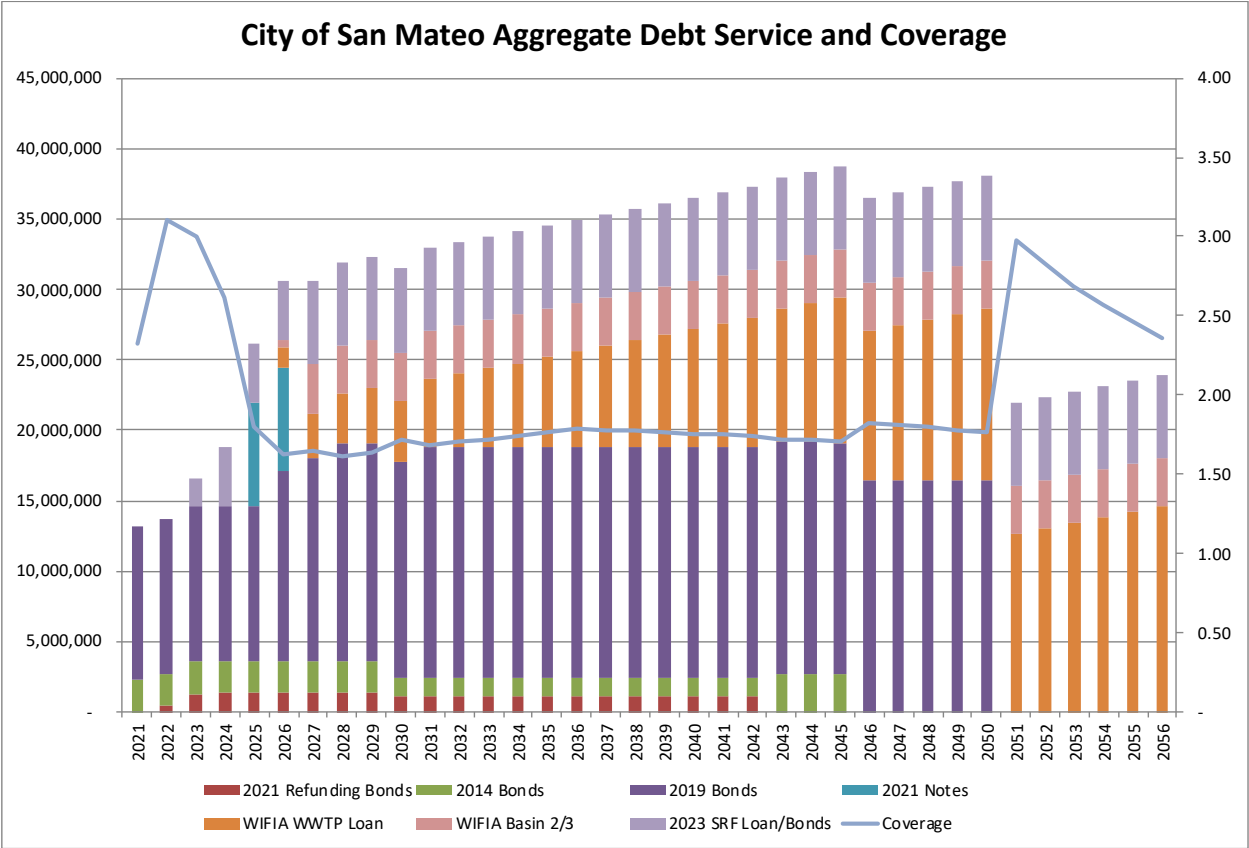
The security for the Series B Notes and Refunding Series A Bonds is described in the sections of the preliminary official statement entitled “SECURITY AND SOURCES OF PAYMENT FOR THE 2021 OBLIGATIONS and “SECURITY AND SOURCES OF PAYMENT FOR THE AUTHORITY BOND PAYMENTS”; information about the City and its sewer enterprise is set forth in “THE CITY,” “THE SAN MATEO SEWER ENTERPRISE,” “FINANCIAL STATEMENTS,” and “Appendix A2”; the key risk factors associated with the Series B Notes and Refunding Series A Bonds are described in the section of the preliminary official statement entitled “CERTAIN RISKS TO BOND OWNERS”; and certain limitations imposed by the California Constitution are described in “CONSTITUTIONAL AND STATUTORY LIMITATIONS ON TAXES AND APPROPRIATIONS.”

BUDGET IMPACT:

The sale of the Series B Notes will cause the sewer enterprise to assume additional debt service payments. The first three years of debt service on the Series B Notes will be capitalized (that is, borrowed, and so paid from Series B Note proceeds), but the City will make the debt service payment in the fourth year from cash resources. This debt, or in the alternative, draws on the WIFIA Loans, is necessary to fund a portion of the City’s Clean Water Program capital costs. The Series B Notes will be repaid with draws on the WIFIA Loans, the debt service on which will be paid with sewer enterprise revenues. Draws on the WIFIA Loans for construction would, in the aggregate, cause the City to pay more in total debt service than would using Series B Notes for construction followed by the WIFIA Loans for long-term financing. See the tables above under “PLAN OF FINANCE – Series B Notes.”

The following chart shows the expected debt service profile of the sewer enterprise and debt service coverage. The stacked bars represent debt service, with different debt issues identified by color, and the line shows debt service coverage over the projection period. Actual results will differ from projected results, and the farther out in time projections extend, the less reliable they tend to be. Revenue increases and debt repayment characteristics have been designed to produce approximately level coverage over the majority of the projection period.

San Mateo Sewer Enterprise Projected Debt Service and Debt Service Coverage



To pay operating and maintenance expenses, and pay debt service on the City's share of the 2019 Bonds, on the City's WIFIA Loans/Notes and on the City's share of future debt necessary to complete the Clean Water Program, sewer rates will need to increase annually through 2023 faster than the projected rate of inflation in operation and maintenance costs. After 2025, it is expected that a nominal increase of only 3 percent will be sufficient keep the enterprise on an even financial keel. No decisions have been made on sewer rate increases for FYE 2024 and FYE 2025, although modest rate increases in these years will likely be necessary to close the anticipated SRF Loan (or allow for the sale of additional bonds if the State loan does not come to fruition) in FYE 2022. The following table shows recent and future estimated required sewer revenue increases. Sewer rate increases were approved in FYE 2019 for a 5-year period through FYE 2023 to allow the City to meet additional bonds covenants and close projected loans during this period.

Fiscal Year Ending June 30	Projected Revenue Increases	Status
2019	14%	Approved
2020	14%	Approved
2021	13%	Approved
2022	13%	Approved
2023	12%	Approved
2024	0%	No Decision ⁽¹⁾
2025	0%	No Decision ⁽¹⁾
2026-2036	3%	Projected

(1) 0% is a placeholder only. Operating results in FYE 2021 will influence whether rate increases for FYE 2024, FYE 2025 and FYE 2026 should be adopted in FYE 2022 so that the final segment of WWTP funding (SRF loan or market rate bonds) can be obtained on advantageous terms.

ALTERNATIVE ACTIONS

The City Council may decline to approve the sale of the Series B Notes and Refunding Series A Bonds. If the Series B Notes are not issued, the City would make direct draws on the WWTP WIFIA Loan when proceeds of the 2019 Bonds borrowed for the WWTP are depleted. Likewise, the City would make direct draws on the Collection WIFIA Loan when proceeds of the 2019 Bonds borrowed for collection projects are depleted. Staff estimates an added cost to the City of approximately \$5.6 million with a direct draw strategy.

If Refunding Series A Bonds are not sold, then the 2011 Bonds will remain outstanding. Staff estimates that the City would forgo total aggregate savings of approximately \$6.7 million if the Council declines to refund the 2011 Bonds. The 2011 Bonds may be refunded on any date after 5/1/21. Savings from a future refunding could be greater than, or less than, present estimated savings.

ENVIRONMENTAL DETERMINATION:

This approval of note and bond documents is not a project subject to CEQA, because it is an organizational or administrative activity that will not result in direct or indirect physical changes in the environment. (CEQA Guidelines Section 15378(b)(5).)

NOTICE PROVIDED

All meeting noticing requirements were met.

ATTACHMENTS

Att 1 - Proposed Resolution

Att 2 - Preliminary Official Statement including,

- Appendix A2 – Certain Economic, Demographic, and Financial Information Relating to the City of San Mateo
- Appendix B2 – Summary of the City of San Mateo Financing Agreement
- Appendix C – Proposed Forms of Continuing Disclosure Certificates

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