

## PROPOSED FINANCING - MVU PROJECTS - \$25.1 MILLION

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## Why did the City of Moreno Valley form a Municipally-Owned Utility? What are the benefits?

- The City was facing the threat of losing large tax based business to the City of Riverside lured by reduced electric rates offered by Riverside Public Utility (RPU)
  - This was possible due to the City's 100 year old, financially stable Municipal Electric Utility
  - The mature RPU generates surplus cash to the General Fund based on the City Charter and provides a source for economic development rate incentives to bring jobs and tax base to the City (\$40 million annually)
- Moreno Valley City Council began the process of building a successful municipally-owned electric utility in 2004 to bring these same benefits to Moreno Valley
- The originating documents included statements that surplus revenue would be used to support additional police and fire services
- Economic development rates would attract critically needed businesses and jobs to the City
- The recession delayed the financial maturing of the Moreno Valley Utility (MVU)
  - MVU is now generating significant surplus cash and is financially strong

## What is the Financial Vision for MVU?

- **MVU will generate a revenue surplus exceeding \$3 million for FY 2014/15**
- Staff will work with City Council to establish direction to fund long needed reserves for the utility
- These include Equipment Replacement Reserves, Working Capital Reserves, Emergency Reserves and Rate Stabilization Reserves (estimated total need is a minimum of \$14 million today)
- Establishing these reserves over the next 5 years will allow MVU to issue tax exempt debt as a municipally owned utility in 2021
- With a strong balance sheet, the MVU debt will garner lower rates than general fund debt with tax exempt investors
- MVU may refinance the General Fund backed Taxable Lease Revenue Bonds as tax exempt debt of the utility - allowing the utility to stand alone as a financially stable entity
  - Frees-up General Fund borrowing capacity for new projects

## Why does the City want a financially strong Municipally Owned Utility?

- Financially strong MVU established with a properly funded balance sheet (est. FY 2021), the City can consider additional options to support City Services:
  - The City may consider a charter - including a General Fund transfer from MVU to support services (police/fire) or reduce the Utility Users Tax (UUT)
  - The City could consider breaking from SCE rate parity, providing an extra economic incentive to draw more businesses and jobs to the community
  - Continue to be able to offer economic incentives for job creation and tax base development
    - Tax base growth may allow weaning off of the UUT

## How do we grow MVU and ensure the vitality of the Utility for years to come?

- Borrow money at low cost interest rates to build and expand MVU capacity timely to serve more customers, particularly large electric use customers:
  - This approach allows the utility to have the capacity to grow and take advantage of the current rapid pace of development of large electricity consuming businesses
  - Manage MVU like a business - A growing business either takes on equity investors or borrows money to invest in the business infrastructure
  - As a public agency, the City (S&P rating of A+) and the Utility have access to the lowest borrowing rates available

## MVU Projects proposed to be funded (included in CIP)

Project Title	Project Description	Estimated Cost
<b>Kitching Substation</b>	Install 115kV/12kV substation	\$13,489,000
<b>Kitching Substation to Edwin Rd.</b>	Install conduit and cable from Kitching to Edwin Rd.	\$480,000
<b>Kitching Backbone to Indian</b>	Circuit going north towards Heacock for reliability	\$787,000
<b>Kitching Substation to Perris Blvd.</b>	Allow part of Iris circuit to transfer to Kitching substation	\$414,000
<b>Kitching Substation to Lasselle Sports Park</b>	Create a tie to Lasselle 12kV	\$477,000
<b>Load transfer to Iris Interconnect</b>	Install cable from Iris to Indian	\$378,000
<b>Kitching Substation to Globe</b>	Connect new circuit to Globe interconnect	\$459,000

## MVU Projects proposed to be funded (included in CIP)

Project Title	Project Description	Estimated Cost
<b>Kitching Backbone to Perris Blvd.</b>	Install conduit and cable along Modular Way to Perris Blvd.	\$465,000
<b>Kitching – Nason 12kV tie</b>	Ties Kitching substation to MoVal substation providing additional reliability	\$816,000
<b>Alessandro Blvd.</b>	Ties Centerpointe Interconnects to MoVal substation	\$2,025,000
<b>Heacock St.</b>	Ties Centerpointe Interconnects to South Industrial area	\$1,396,350
<b>Electrical system automation</b>	Build automation, communication, and protection in circuits that serve critical customers	\$2,000,000
<b>MoVal Substation - 3<sup>rd</sup> transformer bank</b>	Addition of a 3 <sup>rd</sup> transformer bank at MoVal substation. 50% of cost funded by bonds.	\$1,925,000
<b>Total</b>		<b>\$25,111,350</b>

## History of MVU Project Need and Financing Strategy

### **The substation and reliability projects have been planned since early 2014**

- February 26, 2014: Need for the South Substation and Reliability projects identified in the Distribution System Plan (DSP) for years 2014 – 2018
- June 2014: Identified property for Substation Project – completed appraisal
- August 26, 2014: Closed session to discuss negotiation of property purchase
- October 21, 2014: Study Session regarding DSP and cost of service study
- November 18, 2014: City Council approved property purchase, use of General Fund line of credit to fund purchase and reimbursement agreement for GF to be reimbursed from future bond proceeds

## History of MVU Financing Strategy and Need

- March 10, 2015: Request for Proposals completed – Finance Subcommittee and City Council approve Financing Team to support future financings for the City
  - Financing referenced is MVU projects totaling about \$25 million
- April/May review and May 26, 2015 Approval: City Council approved the Fiscal Year 2015/16 Five Year Capital Improvement Program; CIP includes MVU projects, stating they are contingent upon a June 2015 bond issue to fund the projects
- June 26, 2015: MVU Utility Commission reviewed and discussed the proposed financing structure and projects. Approved by Commission on a 4-1 vote.
- June 25, 2015: Materials distributed for a June 29, 2015 Finance Subcommittee meeting – meeting rescheduled to July 8, 2015

## Time sensitivity of the project

- Recent large customers that have connected in the past 24 months:
  - Procter and Gamble
  - Deckers Outdoor
  - Amazon 1
  - Amazon 2
  - Fisker

## Moreno Valley Utility South Industrial Planning Area



## Time sensitivity of the project

- Capacity Issues –
  - MVU South Substation – with recent rapid building of distribution centers and manufacturing, known large customers put the **current system infrastructure at capacity in 2016**
  - To serve additional large usage customers (**SEE MAP**) substation **completion is needed as early in 2017 as possible (project goal May 2017)**
  - System capacity expansion directly ties to continued Economic Development (ED) and Job Growth
  - With Loss of Redevelopment Agency, MVU is most significant ED tool
- Reliability Improvements –
  - The balance of projects funded creates reliability by guaranteeing service through multiple source points
  - Reliability is a key business attraction point for MVU
  - The reliability projects will be completed by 2018

## What occurs if capacity is not available for large projects?

- If capacity is not available by May 2017:
  - If substation project is not available when a developer is ready to connect, staff will need to advise the developer in 2016 to prepare to connect to SCE system to ensure service availability upon project completion
  - Result – loss of revenue stream for years ....
  - Negatively impacting the financial strength of MVU
- Staff is ready to proceed to prevent delays to the project

## Other Financing Options Considered

- General Obligation Bonds
  - Not a feasible option since it requires a vote – earliest election date would be November 2016; need the project online by early 2017
  - Economists anticipate an increase in Fed Reserve rates by late 2015
  - No guarantee the vote would pass, essentially shutting down the economic development capacity of MVU
  - Would require all citywide property owners to increase taxes to support the MVU rate payers

## Other Financing Options Considered

- Public Private Partnership (P3)
  - MVU would need to start an RFP process that will take many months to complete – delaying project completion
  - Cost of capital is higher than the City's (A+ bond rating)
  - Additional parties involved, adding a cost layer that is not necessary
  - Any cost savings is typically from avoiding paying Prevailing Wages – MVU will own the asset at completion, therefore prevailing wages is required
  - The bulk of the \$15 million substation is equipment; so avoiding prevailing wages will not have a great savings impact
  - No opportunity to include an operating/maintenance element, since Enco has the private operating/maintenance contract through December 2020

# Alternatives

## Alternative 1

### Objective:

- Complete a financing to fund the identified projects for the Kitching Substation, Reliability Projects and Moreno Beach Substation Expansion (\$25.1 million)
  - One issue of \$25.1 million in FY 2015 (fund the issuance ASAP)
- Reserve the \$5.0 million in cash available at June 30, 2015
- Reserve all future operating cash to fund balance sheet needs
- Direct staff to complete a 10 year financial plan reflecting the financial impact of this project and funding on the financial development of the utility

### Advantages:

- Completes the Kitching Substation by May 2017
- MVU reserves net excess cash beginning June 30, 2015 and future excess cash necessary to support refinancing bonds with MV Utility credit in 2021
- Takes advantage of funding entire project debt in favorable municipal markets at very low interest rates
- Needed projects are completed timely, including meeting capacity and reliability needs of the utility
- Bond issue expected to be called in 5 years utilizing the Utility's improved financial position (removes the General Fund from 2007 LRB debt and this proposed debt)

### Disadvantages:

- Uses General Fund property to secure debt through lease revenue financing, thereby removing these properties for other General Fund project financing that may arise
- Commits the General Fund to debt service payments, in the unlikely event that the Moreno Valley Utility was unable to make the payments

### Direction:

- Direct staff to **complete a 10 year financial plan** reflecting the financial impact of this project and funding on the financial development of the utility prior to returning with the second bond financing

# Alternatives

## Alternative A

### Objective:

- Reduce the Lease Revenue Bond to fund only the Kitching Substation and related feeder line projects
  - One issue of \$17.2 million in FY 2015 (fund the issuance ASAP)
- Reserve the \$5.0 million in cash available at June 30, 2015
- Create a repayment schedule for the property purchase from MVU to the General Fund (\$492,194 over 5 years)
- Direct staff to complete a 10 year financial plan reflecting the financial impact of this project and funding on the financial development of the utility prior to returning with the second bond financing
- Review the financing for the remaining \$7.5 million Reliability Projects and Moreno Beach Substation expansion to determine the mix of cash and bond financing and present options to Finance Subcommittee and City Council by March 2016

### Advantages:

- Completes the Kitching Substation by May 2017
- General Fund issues less total debt
- MVU reserves excess cash at June 30, 2015, beginning to fund reserves
- Allows the total debt issuance to be lowered to \$17.2 million from \$25.1 million
- Lower total interest expense through 2045

### Disadvantages:

- Defers other reliability projects by at least a year
- Uses MVU cash in 2016 and 2017 that would have funded reserves; MVU may rely on General Fund cash for emergencies and major equipment repairs
- Increases risk that MV Utility may not be able to refinance bonds in 5 years due to decreased liquidity, potentially impacting bond rating
- Municipal bond rates are at historic lows, although future rates of return are unknown, delaying completion of the debt issuances risks a higher interest cost for the issuances

### Direction:

- Direct staff to **complete a 10 year financial plan** reflecting the financial impact of this project and funding on the financial development of the utility prior to returning with the second bond financing
- Evaluate the pay as you go vs debt financing options for the remaining \$7.5 million in Reliability Projects and Moreno Beach Substation expansion.

# Alternatives

## Alternative B

### Objective:

- Utilize a portion of MVU cash to lower the amount borrowed in total
- Split the Lease Revenue Bond into two separate issues, staged in two lower borrowings
- Focus first on Kitching Substation Project and All feeder lines (\$17.7 million)
  - \$4.5 million in cash (pay as you go)
  - \$13 million in debt financing (fund the issuance by December 2015)
- Direct staff to complete a 10 year financial plan reflecting the financial impact of this project and funding on the financial development of the utility prior to returning with the second bond financing
- Focus secondly on additional Reliability Projects and Moreno Beach capacity expansion (\$7.5 million) – possible scenario, for instance:
  - \$2.0 million in cash (pay as you go)
  - \$5.5 million in debt financing (fund the issuance by September 2016)

### Advantages:

- Completes the Kitching Substation by May 2017
- General Fund issues less total debt
- Utilizing MVU Cash totaling \$6.5 million, allows the total debt issuance to be lowered to \$18.5 million from \$25.1 million
- Lower total interest expense through 2045

### Disadvantages:

- Defers the reliability projects and Moreno Beach Expansion by at least a year
- Uses MVU cash in 2016 and 2017 (\$6.5 million) that would fund reserves; MVU may rely on General Fund cash for emergencies and major equipment repairs
- Increases risk that MV Utility may not be able to refinance bonds in 5 years due to decreased liquidity, potentially impacting bond rating
- Adds additional bond issuance cost to complete a second lease revenue bond issuance (\$200,000 to \$300,000)
- Municipal bond rates are at historic lows, although future rates of return are unknown, delaying completion of the debt issuance risks a higher interest cost for the issuance(s)

### Direction:

- Direct staff to **complete a 10 year financial plan** reflecting the financial impact of this project and funding on the financial development of the utility prior to returning with the second bond financing
- Evaluate the pay as you go vs debt financing options for the remaining \$7.5 million in Reliability Projects and Moreno Beach Substation expansion.

# Alternatives

## Alternative C

### Objective:

- Utilize all available MVU cash to fund the MVU Capital Projects using “pay as you go” approach
- The MV Utility would have sufficient cash to award a construction contract for the Kitching Substation by Spring of 2017
- Kitching Substation project would be complete in late summer 2018
- MVU would have no reserves established until beginning in June 2018
- System reliability projects would begin in 2018 and be completed in 2019
- MV Utility would not begin to establish reserves until 2019 or 2020

### Advantages:

- General Fund issues no debt
- General Fund property is not committed to secure the proposed bond issue and is available to support a General Fund related financing if it arises
- MV Utility would save the interest expense on the bonds and the debt issuance costs

### Disadvantage

- Does not complete the Kitching Substation on time to connect new large customers in the MV South Industrial area
- Defers the reliability projects and Moreno Beach Expansion until 2019
- No reserves funded until 2019 or 2020; MVU would have to rely on General Fund cash for emergencies and major equipment repairs
- MV Utility would not be able to refinance 2007 bonds to reduce debt service costs

### Direction:

- Direct staff to **reserve any remaining cash to begin to fund the construction phase of the project**

## Next Steps

- Moreno Valley Utilities Commission recommended Alternative 1 to City Council for approval by a vote of 3-1 on August 21, 2015
- Staff recommends Alternative 1
- Finance Subcommittee requested the four options be presented for City Council consideration
- City Council has directed staff to bring the four options reviewed at Study Session on September 1, 2015 to Council on September 22, 2015 for consideration