

Municipal Utility Policy and Administration

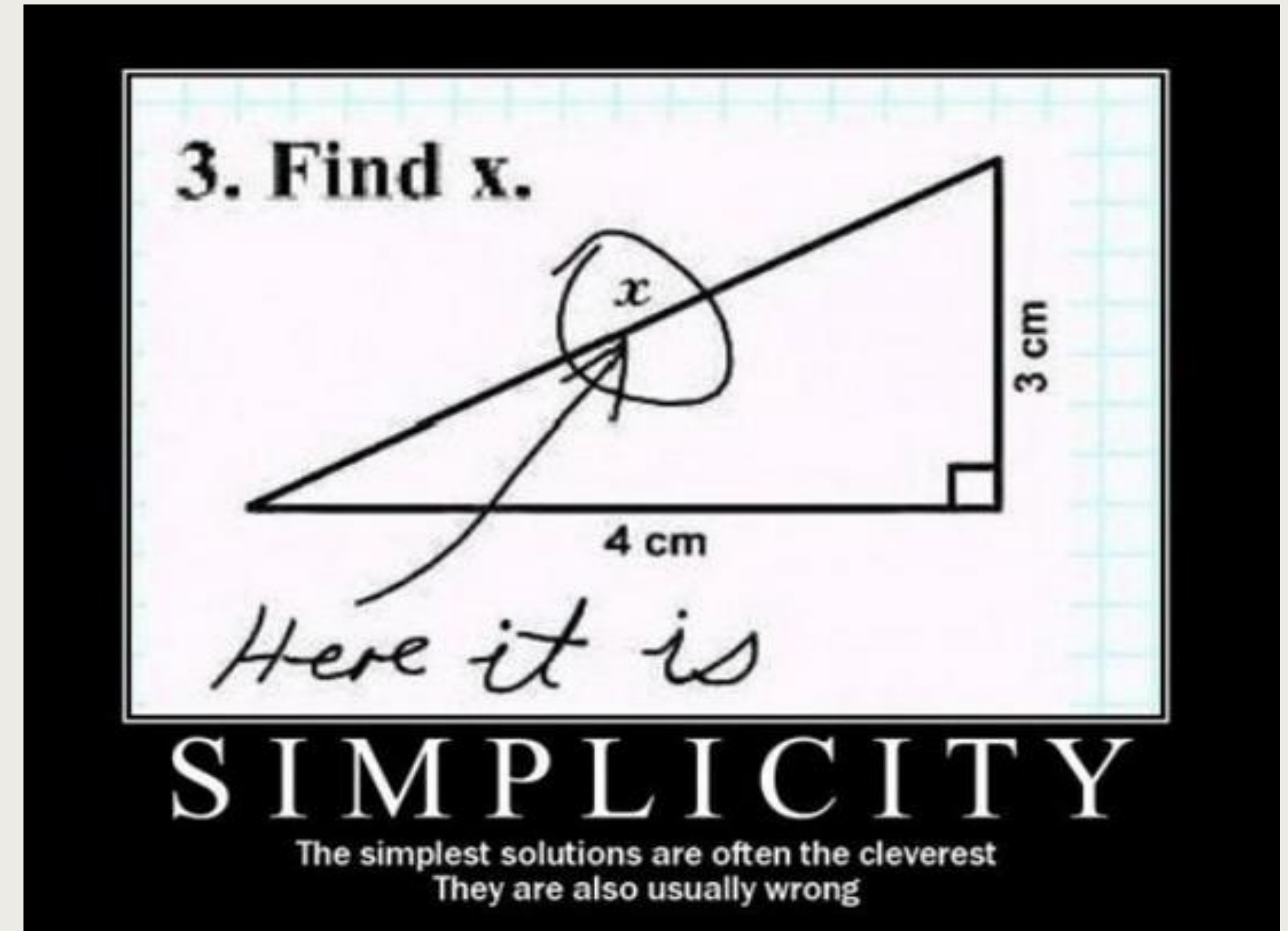
Advanced MEO Institute

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A BRIEF HISTORY LESSON

- ▶ Can't just sign a "note"
- ▶ Dillon's Rule v. Home Rule
- ▶ Role of Bond Counsel
- ▶ Restrictions under State law-relate to the validity of the borrowing
- ▶ Restrictions under Federal law- relate to "tax exemption" of interest
- ▶ General Fund v. Proprietary/Enterprise Fund
- ▶ Municipal Boundary v. Service Area – S.C. Code Section 5-7-60
- ▶ Constitutional Authority for Utilities (Article VIII, Section 16) & Borrowing (Article X, Section 14)



Revenue Issues for Infrastructure

**Constitution of
the State of South
Carolina, Ratified
in Convention,
December 4, 1895**

South Carolina

- Why? Pay as you go v. long-term borrowing
- Capital planning process
- SC Constitution (1895): Article X, Section 14(10): “[i]ndebtedness payable solely from a revenue-producing project or from a special source, which source does not involve revenues from any tax or license, may be issued upon such terms and conditions as the General Assembly may prescribe by general law.”
- State law authority: (1) Revenue Bond Refinancing Act (S.C. Code Section 6-17-10 et seq.); and (2) Revenue Bond Act for Utilities (S.C. Code Section 6-21-10 et seq.)
- Constitution; State law; Federal law; Local law
 - Action/contract of council:
 - Bond Ordinance; Master/Trust Indenture
 - Series/Supplemental Ordinance; Supplemental Indenture

Understanding the Players

- ▶ Issuers (Direct v. Conduit)
- ▶ Legal Counsel
 - ❖ Bond Counsel: Required to deliver validity opinion for borrowing
 - ❖ Local Counsel: Know day to day operations; required to deliver an opinion as to underlying documents and litigation
- ▶ Municipal Advisors
 - ❖ Evolving role, far more involved in transactions; Should have discussions with Counsel or existing FA about role in transactions or on-going operations
- ▶ Bankers/Underwriters
 - ❖ Underwriter: Only for Market-sold deals
 - ❖ Other Counsel: Represent Trustee, Underwriter, Issuers (i.e. Disclosure or Special Tax matters)



Tax Exemption

- ▶ With tax-exemption comes agreement to abide by certain rules and regulations regarding use and payment sources
- ▶ Set forth in IRS rules and regulations
- ▶ Section 103 – Substantially overhauled in 1986
- ▶ Bank-qualification (Section 265) – Applicable to Qualified Small Issuers
- ▶ Reduction of Corporate Tax Rate (35% to 21%)



Revenue Issues for Infrastructure

- ▶ Revenue and Rate Covenants
- ▶ Flow of Funds (Gross v. Net Pledge)
- ▶ Operating Covenants



Revenue Issues for Infrastructure

Revenue and Rate Covenants

Coverage Ratios

- ▶ Rate Covenant – requires that rates be maintained at a certain level (a multiple of O&M and debt service)
 - Projected & Historical
- ▶ Additional Bonds Test – requires certain coverage before the issuance of new debt

Additional Debt

- ▶ “Parity” bonds enjoy the same lien status as the prior bonds, and must meet the additional bonds test
- ▶ Junior lien bonds may be issued at any time
- ▶ Special projects, lease/purchase exceptions in bond documents



Rate Covenant

Section 5.01 Rate Covenant.

(A) It is hereby determined that the rates for services and facilities furnished by the System shall, until otherwise revised, be as now established. Said rates and charges are determined to be sufficient to meet the requirements of this Bond Ordinance but they shall be revised by the City Council whenever necessary in order that they shall at all times be maintained on a basis sufficient to meet the requirements of this Bond Ordinance. The City specifically covenants and agrees to maintain rates and charges for all services furnished by the System which shall at all times be sufficient:

- (1) To provide for the payment of the Operation and Maintenance Expenses as may be necessary to preserve the same in good repair and working order;
- (2) To maintain the Debt Service Fund and the Debt Service Fund Accounts and thus provide for the punctual payment of the principal of and interest on the Bonds;
- (3) To maintain the Debt Service Reserve Funds in the manner prescribed herein and in any applicable Series Ordinance;
- (4) To pay all amounts owing under a reimbursement agreement with any provider of a surety bond, insurance policy or letter of credit as contemplated under Section 7.05(D) hereof;
- (5) To provide for the punctual payment of the principal of and interest on all Junior Lien Bonds that may from time to time hereafter be outstanding;
- (6) To build and maintain a reserve for depreciation of the System, for contingencies and for improvements, betterments and extensions to the System other than those necessary to maintain the same in good repair and working order; and
- (7) To discharge all obligations imposed by the Enabling Act and by this Bond Ordinance and any applicable Series Ordinance.

(B) The City covenants and agrees that it will, at all times, prescribe and maintain and thereafter collect rates and charges for the services and facilities furnished by the System which, together with other income, are reasonably expected to yield annual Net Earnings in the current Fiscal Year equal to at least the sum of one hundred fifteen percent (115%) of the Annual Principal and Interest Requirement in such Fiscal Year for all Bonds Outstanding. Promptly upon any material change in the circumstances which were contemplated at the time such rates and charges were most recently reviewed, but not less frequently than once in each Fiscal Year, the City, with or without the aid of an Independent Consultant, shall review the rates and charges for its services and shall promptly revise such rates and charges as necessary to comply with the foregoing requirement. Prior to the beginning of each Fiscal Year, the City shall adopt an Annual Budget including amended rate schedules for such Fiscal Year which shall set forth in reasonable



Revenue Issues for Infrastructure

as may be necessary to make the value of the moneys and securities in each Debt Service Reserve Fund equal to the applicable Reserve Requirement, unless:

(a) the Series Ordinance and any previous Series Ordinances shall have provided for successive monthly payments beginning in the first month following the date of the issuance of the Bonds of any such Series in substantially equal monthly amounts (the “*Monthly Series Payments*”) so that by the end of twelve (12) months from the date of issuance of such Series of Bonds there shall be in the applicable Debt Service Reserve Fund an amount equal to the applicable Reserve Requirement with respect to such Bonds; and

(b) there shall be no unremedied defaults of any Monthly Series Payments required to have been made.

(6) Except in the case of the first Series of Bonds issued under this Bond Ordinance or in the event no Bonds are Outstanding:

Net Earnings during the most recent Fiscal Year for which audited financial statements of the System are completed shall be certified by the Auditors or the Independent Consultant on the basis of such audited financial statements to be not less than one hundred twenty percent (120%) of the maximum Annual Principal and Interest Requirements on all Bonds Outstanding and on such proposed Series of Bonds; provided that for purposes of this Section 4.02(6), such Net Earnings may be adjusted to reflect (1) any rate increases currently adopted and to be in effect prior to, coincident with or during the current Fiscal Year of the issuance of such proposed Series of Bonds and determined *pro forma* as though such rate increases had been in continuous effect during such recent Fiscal Year; (2) in the event a utility, system or enterprise that is in existence and operating and whose current customers have become customers of the System prior to the issuance of the proposed Series of Bonds or will become customers of the System concurrently with the issuance of such proposed Series of Bonds, 100% of the Net Earnings that the Auditors or the Independent Consultant estimate would have been received during such Fiscal Year if the utility, system or enterprise had been a part of the System throughout such recent Fiscal Year, taking into account, for the estimation of such Net Earnings in this subparagraph (2) only, the then-existing customer base and population of the acquired utility, system or enterprise; (3) in the event proceeds of such proposed Series of Bonds will be used to construct or to acquire a newly-constructed utility, system, enterprise, or component of the System which will serve an existing customer base and currently-populated area, 100% of the Net Earnings, estimated by the Independent Consultant, to be received by the System during the first Fiscal Year beginning after the date on which such project constructed or acquired with the proceeds of the proposed Series of Bonds is placed in service, taking into account for the estimation of such Net Earnings in this subparagraph (3) only the then-existing customer base and population; (4) in the event proceeds of such proposed Series

of Bonds will be used to pay interest on such proposed Series, 100% of the interest that will accrue on such Series of Bonds following the date of delivery of the proposed Series and that will be paid from such proceeds; and (5) in the event proceeds of such proposed Series of Bonds will be used to construct or to acquire an expansion to the System and to the extent not included by sub-paragraph (3), 100% of estimated Net Earnings to be received by the System in the first Fiscal Year following the completion of such project, certified by the Independent Consultant, from customers under long-term contracts which extend for the life of such proposed Series of Bonds.

Provided that in the instance of any Series of Bonds in the aggregate principal amount of \$5,000,000 or less, such calculation required by Section 4.02(6) may, unless provided to the contrary in any Series Ordinance, be made by the Treasurer.

In the event that a Series of Bonds is Outstanding and the City determines to issue a note or other obligation in anticipation of the issuance of a Series of Bonds, for the purposes of complying with the additional bonds test established in this Section 4.02(6) above, the Auditors, the Independent Consultant, or the City shall project the maturity schedule (including rate, term and principal maturities) of the future Series of Bonds that will be used to pay the note or other obligation at maturity; such future Series of Bonds and the accompanying projections shall qualify as a proposed Series of Bonds for purposes of the additional bonds test in Section 4.02(6) herein.

Whenever this Section 4.02(6) requires a certification for the most recent Fiscal Year for which audited financial statements are available, the City may, in its discretion, provide for a special audit and a certification based upon such special audit, in lieu of the audit for such Fiscal Year, provided such special audit covers twelve (12) consecutive calendar months of the eighteen (18) full consecutive calendar months preceding the date of issuance of the proposed Series of Bonds.

(7) Notwithstanding Section 4.02(6) hereinabove, in the case of Bonds issued for the purpose of refunding any Bonds, Series of Bonds, or a portion of a Series of Bonds:

(a) the Annual Principal and Interest Requirement of the refunding Bonds shall not exceed one hundred ten percent (110%) of the Annual Principal and Interest Requirement of the refunded Bonds for any Fiscal Year until a time subsequent to the last maturity of Bonds issued prior to the issuance of such refunding Bonds which are not refunded and which remain Outstanding following the issuance of the refunding Bonds; or

(b) the additional bonds test prescribed by paragraph (6) herein shall be complied with.

(8) If any Series of Bonds shall contain Variable Rate Bonds:



Revenue Issues for Infrastructure

Outstanding Sewer Revenue Bonds

The table below sets forth the City's outstanding indebtedness secured by the revenues of the Sewer System.

<u>Year Ending June 30</u>	<u>USDA RD Loans</u>	<u>SRF Loans</u>	<u>Series 2020A Revenue Bond</u>	<u>Series 2020B Revenue Bond</u>	<u>Combined Debt Service</u>
2025	59,664	\$1,462,259	\$68,807	\$33,013	\$1,623,743
2026	59,664	\$1,462,259	\$275,227	\$66,025	\$1,863,175
2027	59,664	\$1,462,259	\$275,227	\$66,025	\$1,863,175
2028	59,664	\$1,462,259	\$275,227	\$66,025	\$1,863,175
2029	59,664	\$1,462,259	\$275,227	\$66,025	\$1,863,175
2030	59,664	\$1,462,259	\$275,227	\$66,025	\$1,863,175
2031	59,664	\$1,417,267	\$275,227	\$66,025	\$1,810,002
2032	59,664	\$1,321,911	\$275,227	\$66,025	\$1,694,867
2033	31,704	\$1,302,435	\$275,227	\$66,025	\$1,675,391
2034	31,704	\$1,215,143	\$275,227	\$66,025	\$1,588,099
2035	31,704	\$1,186,045	\$275,227	\$66,025	\$1,559,001
2036	28,521	\$944,089	\$275,227	\$66,025	\$1,313,862
2037	-	\$853,772	\$275,227	\$66,025	\$1,195,024
2038	-	\$823,666	\$275,227	\$66,025	\$1,164,918
2039	-	\$823,666	\$275,227	\$66,025	\$1,164,918
2040	-	\$794,010	\$275,227	\$66,025	\$1,135,262
2041	-	\$612,897	\$275,227	\$66,025	\$954,149
2042	-	\$323,129	\$275,227	\$66,025	\$664,381
2043	-	\$291,792	\$275,227	\$66,025	\$633,044
2044	-	\$260,453	\$275,227	\$66,025	\$601,705
2045	-	\$260,453	\$203,421	\$33,013	\$496,887
2046	-	\$260,453	-	-	\$260,453
2047	-	\$260,453	-	-	\$260,453
2048	-	\$260,453	-	-	\$260,453
2049	-	\$260,453	-	-	\$260,453
2050	-	<u>\$131,031</u>	-	-	<u>\$131,031</u>
Totals	\$564,804	\$22,377,124	\$5,501,541	\$1,320,501	\$29,763,970



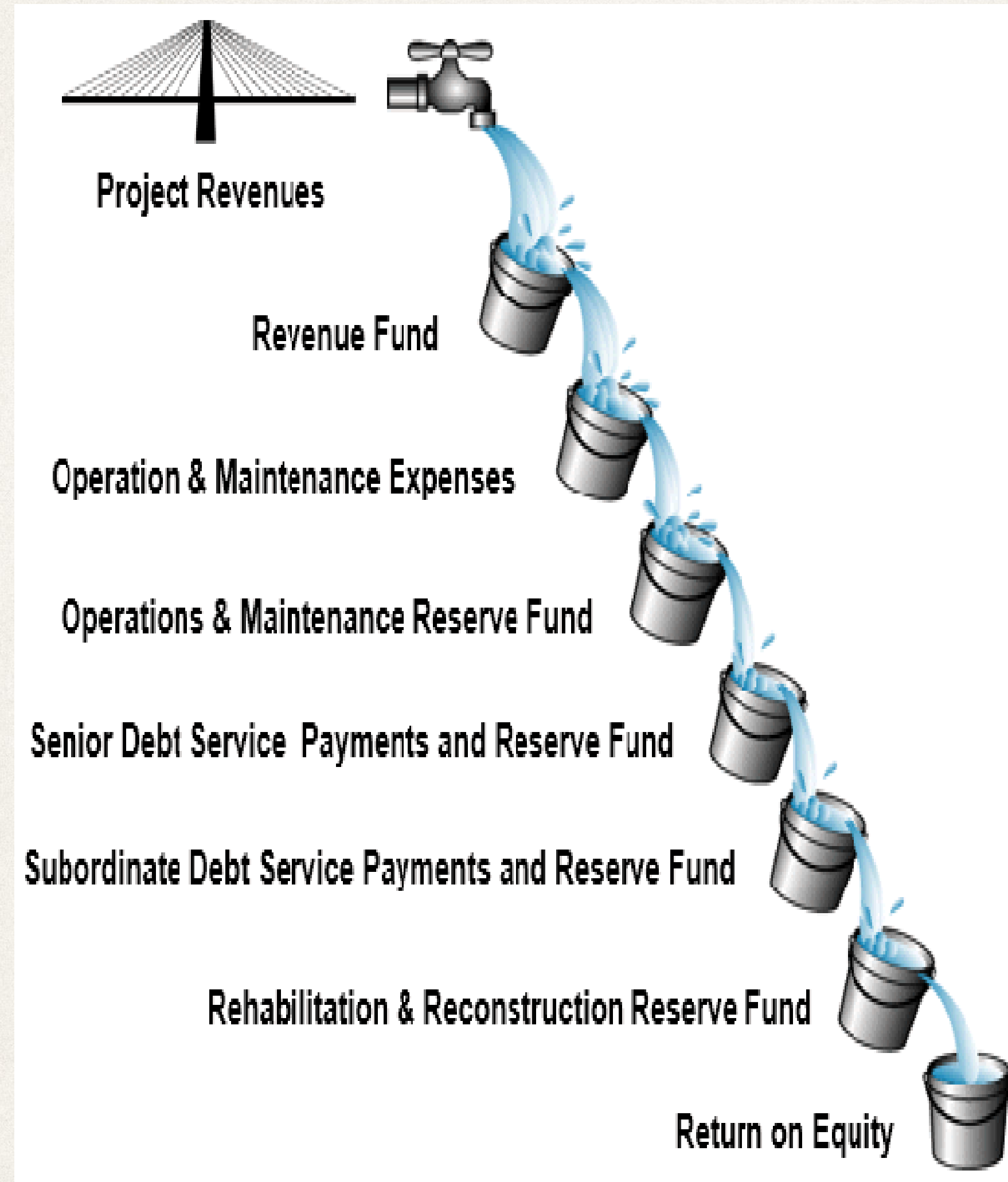
Revenue Issues for Infrastructure

Calculating “Coverage”

	2024/25
REVENUES	
BASE CHARGE	\$2,000,000
USAGE RATES	3,000,000
SUBTOTAL	<u>\$5,000,000</u>
OTHER OPERATING REVENUES	<u>1,000,000</u>
GROSS REVENUES	\$6,000,000
O&M EXPENSES	<u>4,500,000</u>
NET EARNINGS	\$1,500,000
DEBT SERVICE	
EXISTING BONDS	\$750,000
2021 BONDS	<u>250,000</u>
TOTAL DEBT SERVICE	<u>\$1,000,000</u>
NET SURPLUS (DEFICIT)	\$500,000

COVERAGE (NET EARNINGS/DEBT SERVICE)	1.5x
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Flow of Funds



- ▶ Secured by Revenue Stream
 - ❖ A limited pledge
 - ❖ Bond documents will establish a “waterfall” to control the flow of revenues
 - ❖ Generally debt service on the bonds will come before O&M expenses (gross pledge) or after (net pledge)



Revenue Issues for Infrastructure

Operating Covenants

- Asset ownership/maintenance
- No free service
- Furnish audit requirement (state law & EMMA)
- Maintain Insurance (assets, defalcation, liability)
- Sale of assets/system
- Efficient/prudent operations
- Good repair and working order
- Compliance with law – health, safety, environmental
- Dealing with surplus appropriations
- Lease limitations



Revenue Issues for Infrastructure

Transfers

- ▶ Cumberland v. Columbia – how are you using the net profits of the enterprise? What does this tell us about reliance on enterprise fund transfers?
- ▶ Utility fees are user fees under Section 6-1-320
- ▶ City issues bonds under Revenue Bond Act for Utilities – Section 6-21-440 expressly allows for distribution of surplus revenues
- ▶ Surplus should be distributed only after all costs of utility are funded
- ▶ Do you provide for calculation of surplus in your budget ordinance?
- ▶ Do you have or have you established financial policies to deal with transfers?
- ▶ SCAG Opinion – questioning Rock Hill model

CONCLUSION:

In summary, section 6-21-440 of the Revenue Bond Act for Utilities⁸ mandates that bonded utility revenues must fund certain expenses and reserves before those funds can be used at the municipality's discretion. Pursuant to [Azar v. City of Columbia, 414 S.C. 307 \(2015\)](#), a municipality's transfer of its utility revenues to its general fund is lawful if it constitutes either "surplus revenues" pursuant to [S.C. Code Ann. § 6-21-440](#) or "related" costs under [S.C. Code Ann. § 6-1-330\(B\)](#). In order to be "related" costs under [section 6-1-330\(13\)](#), the utility revenues must be used to pay costs sufficiently related to the provision of the utility services. If those mandatory reserves have not been met as required by law, and the expenditure or transfer of the utility revenues does not constitute "surplus revenues" or "related" costs as permitted by law and discussed in [Azar](#), then a court would most likely find the transfer of those funds to be unlawful.

Lease Purchase Agreements

- ▶ Not a “True” Lease
- ▶ Financing institution provides funds and “leases” the assets to the municipality
- ▶ Lease payments have principal and interest components
- ▶ Assets will pass to municipality free and clear upon conclusion of lease term
- ▶ Compliance with “new” leasing rules under GASB 87



Lease Purchase Agreements

Debt Limit Considerations

- ▶ Previously all lease-purchase transactions were exempt from the debt limit
- ▶ Statute passed in 1995 disallows debt-limit exemption for real property and fixtures
- ▶ Now lease-purchase agreements are used almost exclusively for vehicles, equipment, and rolling stock
- ▶ Paid out of Operations; Not considered debt
- ▶ General fund lease payments are now limited by Act 388

Tips for a Smoother Borrowing Experience



- ▶ Financial Statements (be timely)
- ▶ Define the project: sizing of issue
- ▶ Stability in financial administration
- ▶ Stability in professionals, including bank and bond counsel
- ▶ Pricing is important, but not sole determining factor
- ▶ Discussion on front end of expectations – don't agree to things you do not understand
- ▶ Policies and Procedures (debt administration, tax, disclosure, coverage, OPEB, Pension, cash management)

Additional Legal Considerations

- ▶ FOIA
- ▶ Arbitrage and rebate
- ▶ Spend down requirements
- ▶ Tax Covenants (Ownership)
- ▶ Continuing Disclosure
- ▶ Bank-Qualified
- ▶ Economic Development/Public Purpose



Disclosure

- ▶ 1933 Securities Act
 - ❖ Section 17(a): Antifraud
- ▶ 1934 Exchange Act
 - ❖ Tower Amendment
 - ❖ Section 10b-5: Antifraud
 - ❖ Rule 15c2-12
- ▶ Continuing Disclosure
 - ❖ Rule 15c2-12 (1975; 1994)
 - ❖ MSRB; EMMA
 - ❖ Municipalities Continuing Disclosure Cooperation initiative

Disclosure


▶ Continuing Disclosure Defined

- ❖ “Continuing disclosure consists of important information about a municipal bond and its issuer that arises after the initial issuance of the bond. This information generally reflects the financial or operating condition of the issuer as it changes over time, as well as specific events occurring after issuance that can have an impact on the ability of issuer to make payments on the bond, the value of the bond if it is traded prior to its maturity, the timing of repayment of principal, and other key features of the bond”
- ❖ Enforced through SEC regulation of Broker-Dealers; Required in Primary Offer as an Aid to Secondary Market
- ❖ Exempt from Registration and Reporting Requirements of ‘33 Act and ‘34 Act (Tower Amendment – Pre-sale) – But see Rule 10b-5 and Rule 15c2-12 and SEC’s 1994 Interpretative Release (not private placements)

Disclosure

- ▶ What are my Continuing Disclosure Responsibilities?
 - ❖ Established in the Continuing Disclosure Agreement (CDA) executed at the closing of your Bonds.
 - ❖ Issuer may engage a Dissemination Agent to assist with disclosure responsibilities.
 - ❖ Generally Requires:
 - ❖ Disclosure of Financial and Operating Information
 - ❖ Material Event Notices

Disclosure






CAYCE S C WTRWKS & SEW REV (SC)

Click on a tab to access data and documents about this issuer's municipal securities.

Issuer's Contact Information This issuer has not provided contact information.

Educational Resources

-  [Customizing an Issuer Homepage](#)
-  [How Can Issuers Use EMMA?](#)
-  [Contact Us](#)

Issues
Trade Activity
Pre-Sale Documents
Official Statements
Refunded Issues
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Click on the issue description to view details about the issue. [View all Issues](#) ▼

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Issue Description	Dated Date	Maturity Dates
WATER AND SEWER SYSTEM REFUNDING REVENUE BONDS, SERIES 2020	07/21/2020	2021 to 2036
WATER AND SEWER SYSTEM REFUNDING REVENUE BONDS, SERIES 2016A (TAXABLE)	03/29/2016	2016 to 2024
WATER AND SEWER SYSTEM REFUNDING REVENUE BONDS, SERIES 2016B	03/29/2016	2024 to 2028
REF REV BDS 2007-A	09/11/2007	2008 to 2027
RFDG & IMPT	07/15/2004	2005 to 2015
<Issue description not available>	07/15/1998	2000 to 2020
RFDG	07/01/1993	1994 to 2015
<Issue description not available>	03/01/1990	1992 to 2015
<Issue description not available>	02/01/1974	1985 to 1990
<Issue description not available>	12/25/1966	1985 to 1986

Displaying 1 to 10 of 10 results

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Hypothetical #1

An out of town restaurant developer reaches out to the Mayor about building a “Biscotti Phippen” in your community. The developer says that they are interested in the City, but “cannot make the numbers work unless you waive capacity fees and give them a year of free utility service”

What do you do?





Hypothetical #2

Your city is planning to issue utility revenue bonds. As Mayor of the City, you are aware that a major community and employer is planning to down-size – do you have a responsibility to tell someone?

What if they are planning a major investment, but you have signed a non-disclosure agreement?



Hypothetical #3

A smaller utility approaches you about acquiring their sewer system. Can you do it?

What if they require that you “lock-in” rates as a condition of transfer?

What if they have outstanding revenue utility debt?

What if you have outstanding revenue utility debt?



Hypothetical #4

Your City borrows \$20,000,000 to expand its sewer plant. You bid the project, but the bids get delayed.

What do you do with the proceeds?

Can you invest them? If so, how, where, and how long?

Do you get to keep everything you earn?



Month	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
July	2.42	0.50	0.11	1.72	5.42	5.50	4.45
August	2.28	0.34	0.10	2.32	5.59	5.48	4.46
September	2.18	0.28	0.10	2.62	5.60	5.34	4.40
October	2.08	0.21	0.10	3.24	5.64	5.03	4.32
November	1.92	0.17	0.11	3.94	5.68	4.86	4.19
December	1.84	0.16	0.14	4.32	5.67	4.74	4.08
January	1.81	0.16	0.15	4.57	5.61	4.61	
February	1.74	0.14	0.17	4.75	5.57	4.56	
March	1.58	0.13	0.34	4.85	5.54	4.54	
April	1.40	0.13	0.52	5.10	5.52	4.52	
May	1.00	0.11	0.87	5.27	5.52	4.49	
June	0.76	0.09	1.26	5.35	5.52	4.47	

Contact Information

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