



YESTERDAY, TOMORROW AND FINANCE
2020 CSMFO ANNUAL CONFERENCE
JANUARY 28-31, 2020
DISNEYLAND CA



Understanding “Debt Affordability” ... How Much Is Too Much?





KNN Public Finance, LLC
David Leifer, Senior Managing Director



Napa Sanitation District
Jeff Tucker, Director of Administrative Services / Chief Financial Officer

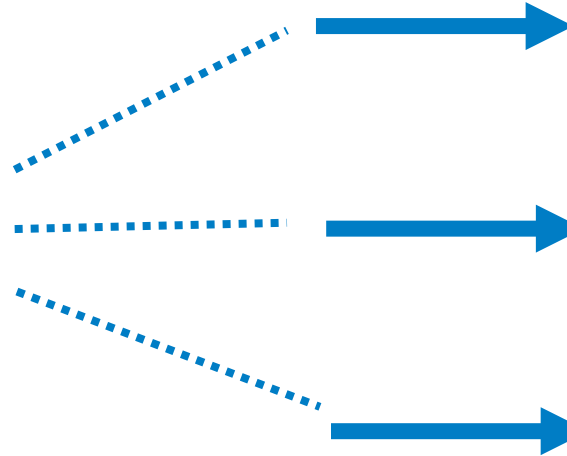


County of San Luis Obispo
James Hamilton, Auditor-Controller-Treasurer-Tax Collector

Debt Capacity versus Debt Affordability



What are my limits?



How much can I afford?



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Revenue Bonds versus General Fund Backed Bonds

- Cities, counties and special districts commonly issue Revenue Bonds for water, sewer, solid waste or other enterprise financings
 - Debt is paid from special revenues and used to finance an asset which is part of a project or system generating such revenues
 - Debt or Installment Purchase payments are limited to “Net Revenues” of enterprise or district
 - No general fund impact or support
- Cities and counties generally issue general fund backed Certificates of Participation or Lease Revenue Bonds for facilities necessary to support General Fund operations
 - Debt service (lease payments) paid from General Fund



Different Approaches to Considering Debt Capacity/Affordability

Revenue Bonds

- Capacity can be quantifiable through debt service coverage metrics
- Capacity can be increased through additional rates and user fees, within limits
- Affordability driven by service area and customer base

General Fund Backed Obligations

- No single measure of capacity or affordability
- No ability to increase major revenues absent voter approval (i.e. property tax, sales tax, other special taxes)
- Affordability impacted by reserve levels, fixed obligations, and budgetary trade-offs



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Evaluating Debt Capacity: Special District / Revenue Borrower





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Features of Revenue Bonds/ Installment Purchase Revenue COPs

- Primary feature: “Debt Service Coverage”
 - Debt service coverage - cash cushion from annual “net revenues”
 - “Gross revenues” minus operating and maintenance cash expenses (depreciation excluded)
- Other Revenue Bond Features
 - Rate Covenant
 - Additional Bonds Test
 - Debt Service Reserve Fund (as needed)
 - Rate Stabilization Fund (as needed)

Example Net Revenue Pledge		\$
Flow of Funds		Amount
A	Gross System Revenues	\$100
B	Operation and Maintenance Expenses	85
C = A-B	Net Revenues	15
D	Debt Service Payments	10
E = C/D	Debt Service Coverage Ratio	1.50x





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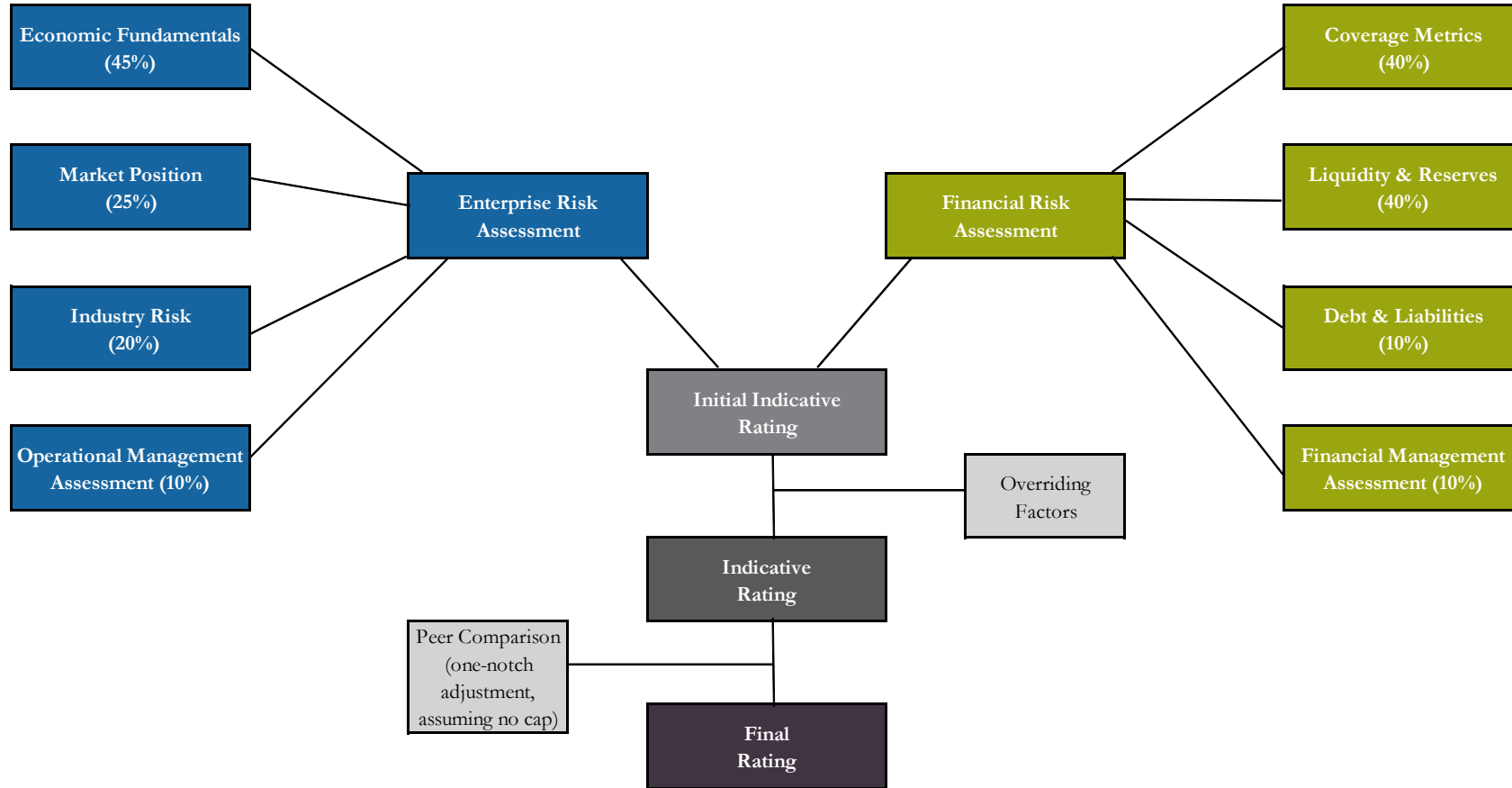
Forecasting Debt Capacity For Revenue Bonds

A Operating Revenues	\$1,000,000		
B Operating Expenditures	\$600,000		
C Net Revenues (A – B)	\$400,000		
Debt Service Coverage and ABT	1.5x		
Max Annual D/S	$\frac{\$400,000}{1.5} =$	266,666	
Outstanding Annual D/S	\$100,000		
Annual D/S Capacity for New Debt	\$166,666		

- Levers that impact debt capacity include:
 - Rate structure (i.e., future increases);
 - Timing and amount of capital expenditures; and
 - Debt service coverage requirements and legal covenants in bond indenture.



Standard & Poor's Enterprise System Rating Methodology



Source: Standard & Poor's Rating Services, U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Rating Methodology and Assumptions, January 19, 2016.

Coverage Metrics – 40%

S&P Initial Assessment	All-In Coverage
1	1.60x or above
2	1.40x to 1.60x
3	1.20x to 1.40x
4	1.10x to 1.20x
5	1.00x to 1.10x
6	Below 1.00x

- There may be certain qualitative factors that could impact the initial scoring assessment up or down.

Source: Standard & Poor’s Rating Services, *U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Rating Methodology and Assumptions*, January 19, 2016.

Liquidity and Reserves – 40%

Liquidity and Reserves Preliminary Assessment		
Preliminary Assessment	Days' Cash	Actual Cash
1	> 150	> \$75m
2	90 to 150	\$20m - \$75m
3	60 to 90	\$5m - \$20m
4	30 to 60	\$1m - \$5m
5	15 to 30	\$500k - \$1m
6	< 15	< \$500k

Liquidity and Reserves Assessment (40% of Indicative Rating)							
		Actual Cash on Hand					
		1	2	3	4	5	6
		Days' Cash	1	1	2	2	3
2	1	2	2	3	3	4	
3	2	2	3	4	4	5	
4	2	3	4	4	5	5	
5	3	3	4	5	5	6	
6	4	4	5	5	6	6	

- There may be certain qualitative factors that could impact the initial scoring assessment up or down.

$$\text{Days' Cash} = \frac{\text{Unrestricted Cash}}{1/365\text{th of Operating Expenses}}$$

Source: Standard & Poor's Rating Services, U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Rating Methodology and Assumptions, January 19, 2016.

Debt and Liabilities – 10%

S&P Initial Assessment	Debt to Capitalization
1	Up to 20%
2	20% to 35%
3	35% to 50%
4	50% to 65%
5	65% to 80%
6	Greater than 80%

- There may be certain qualitative factors that could impact the initial scoring assessment up or down.

$$\text{Debt to Capitalization} = \frac{\text{Short and Long-Term Debt}}{\text{Total Debt} + \text{Net Position}}$$

Source: Standard & Poor's Rating Services, *U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Rating Methodology and Assumptions*, January 19, 2016.

Introduction to NapaSan

- NapaSan is an independent special district that provides wastewater collection, treatment, and disposal services to the residents and businesses in the City of Napa and surrounding unincorporated areas of Napa County.
- The District maintains 270 miles of underground sewer main and another 270 miles of sewer laterals that convey influent to the Soscol Water Recycling Facility.
 - The facility is a District owned wastewater treatment plant that treats wastewater and recycled water.
- During the wet season, NapaSan discharges full secondary treated wastewater to the Napa River.
- NapaSan has several series of Revenue Certificates of Participation and state revolving fund installment sale agreements outstanding, which were issued to construct a variety of essential infrastructure projects.





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The Capital Improvement Plan

- The District’s annual CIP is designed to identify capital expenditures *for the next ten-years* and outlines an action plan to complete these projects within projected revenues and staffing capacity.
- Capacity charges on new developments are used to pay for their proportionate share of expanding the collection, treatment, and water recycling system.
- Sewer service charges in excess of operational needs are used for replacement and rehabilitation projects.

Project	FY2019-20	10-Year CIP
Collection System	\$20,201,500	\$146,937,250
Collection System Equipment	17,800	4,513,400
Lift Stations	5,500,000	11,269,500
Treatment	4,305,000	59,006,100
Treatment Equipment	2,872,300	11,779,200
Lab Equipment	20,000	1,362,200
SCADA	0	886,000
Recycling Projects	510,000	7,566,400
Recycling-Expansion	109,700	4,250,600
Other	337,000	6,686,000
Total:	\$33,873,300	\$254,256,650

Source: NapaSan.





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Capital Cash Flow Model

- The District maintains a detailed multi-year cash flow model to aide in the assessment of the affordability of future capital:

Fiscal Year Ending:	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029
Beginning Fund Equity:	\$22,447,700	\$20,089,400	\$20,324,700	\$23,444,500	\$23,824,500	\$24,425,100	\$25,778,500	\$26,922,200	\$28,416,400	\$29,053,900
Operating Revenue:	36,481,500	38,008,100	38,818,700	39,618,400	40,561,200	42,056,000	43,600,900	45,206,900	46,870,900	48,590,000
Non-Operating Revenue:	15,994,600	20,830,900	6,723,300	1,366,000	1,785,000	6,870,000	4,593,000	23,135,500	3,393,000	9,412,000
Total Revenue:	\$52,476,100	\$58,839,000	\$45,542,000	\$40,984,400	\$42,346,200	\$48,926,000	\$48,193,900	\$68,342,400	\$50,263,900	\$58,002,000
Operating Expenses:	20,961,100	21,851,200	22,657,300	24,204,000	24,912,000	25,329,800	27,881,200	28,358,800	28,845,600	28,648,800
Capital Expenditures:	33,873,300	36,752,500	19,764,900	16,400,400	16,833,650	22,242,850	19,169,000	38,489,450	20,780,800	29,949,800
Net Revenue:	-2,358,300	235,300	3,119,800	380,000	600,550	1,353,350	1,143,700	1,494,150	637,500	-596,600
Ending Fund Equity:	\$20,089,400	\$20,324,700	\$23,444,500	\$23,824,500	\$24,425,050	\$25,778,450	\$26,922,200	\$28,416,350	\$29,053,900	\$28,457,300

Source: NapaSan.





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Projected Coverage with New Projects is One Measure of Affordability

- NapaSan utilizes its cash flow model to help determine the affordability of future projects.

FY Ending:	2020	2021	2022	2023	2024
Operating Revenues:	\$37,059,500	\$38,589,100	\$39,708,700	\$40,882,400	\$41,836,200
Operating Expenses:	16,367,200	17,264,000	17,246,400	17,772,200	18,536,500
Net Revenues:	\$20,692,300	\$21,325,100	\$22,462,300	\$23,110,200	\$23,299,700
Existing Debt Service:	\$4,593,900	\$4,587,200	\$4,590,900	\$4,579,800	\$4,523,500
Existing Debt Service Coverage:	4.5 x	4.6 x	4.9 x	5.0 x	5.2 x
Initial S&P Assessment:	1	1	1	1	1

Debt Service for New Projects:					
Trunk Rehab:	0	0	820,000	820,000	820,000
Browns Valley River Project:	0	0	0	1,032,000	1,032,000
Total New Debt Service:	\$0	\$0	\$820,000	\$1,852,000	\$1,852,000
Total Debt Service (with New Projects):	\$4,593,900	\$4,587,200	\$5,410,900	\$6,431,800	\$6,375,500
Coverage with New Projects:	4.5 x	4.6 x	4.2 x	3.6 x	3.7 x
Initial S&P Assessment:	1	1	1	1	1

Source: NapaSan.

Initial S&P Assessments based upon KNN's interpretation of methodology described in Standard & Poor's Rating Services, *U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Rating Methodology and Assumptions*, January 19, 2016. Not confirmed by Standard & Poor's.





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S&P Scoring: Liquidity and Reserves

NapaSan Actual Results (FYs 2017-2019)			
Fiscal Year Ending:	2017	2018	2019
Actual Cash on Hand:	\$22,532,461	\$26,420,531	\$28,309,295
Days' Cash:			
Unrestricted Cash:	\$22,532,461	\$26,420,531	\$28,309,295
Total Operating Expenses:	\$22,288,999	\$20,246,764	\$24,650,976
Less Depreciation:	\$8,845,731	\$9,072,852	\$8,911,062
Net Operating Expenses:	\$13,443,268	\$11,173,912	\$15,739,914
Days' Cash:	612	863	656

Liquidity and Reserves Preliminary Assessment		
Preliminary Assessment	Days' Cash	Actual Cash
1	> 150	> \$75m
2	90 to 150	\$20m - \$75m
3	60 to 90	\$5m - \$20m
4	30 to 60	\$1m - \$5m
5	15 to 30	\$500k - \$1m
6	< 15	< \$500k

Liquidity and Reserves Assessment (40% of Indicative Rating)							
		Actual Cash on Hand					
		1	2	3	4	5	6
Days' Cash	1	1	1	2	2	3	4
	2	1	2	2	3	3	4
	3	2	2	3	4	4	5
	4	2	3	4	4	5	5
	5	3	3	4	5	5	6
	6	4	4	5	5	6	6

Source: NapaSan Comprehensive Annual Financial Reports for FYs 2017-2019.

Initial S&P Assessments based upon KNN's interpretation of methodology described in Standard & Poor's Rating Services, *U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Rating Methodology and Assumptions*, January 19, 2016. Not confirmed by Standard & Poor's.



S&P Scoring: Debt and Liabilities

NapaSan Actual Results (FYs 2017-2019)			
Fiscal Year Ending:	2017	2018	2019
Debt to Capitalization			
Outstanding Debt:	\$52,408,842	\$47,669,770	\$44,339,189
Total Net Position:	\$176,245,107	\$186,252,045	\$194,036,321
Debt to Capitalization:	23%	20%	19%

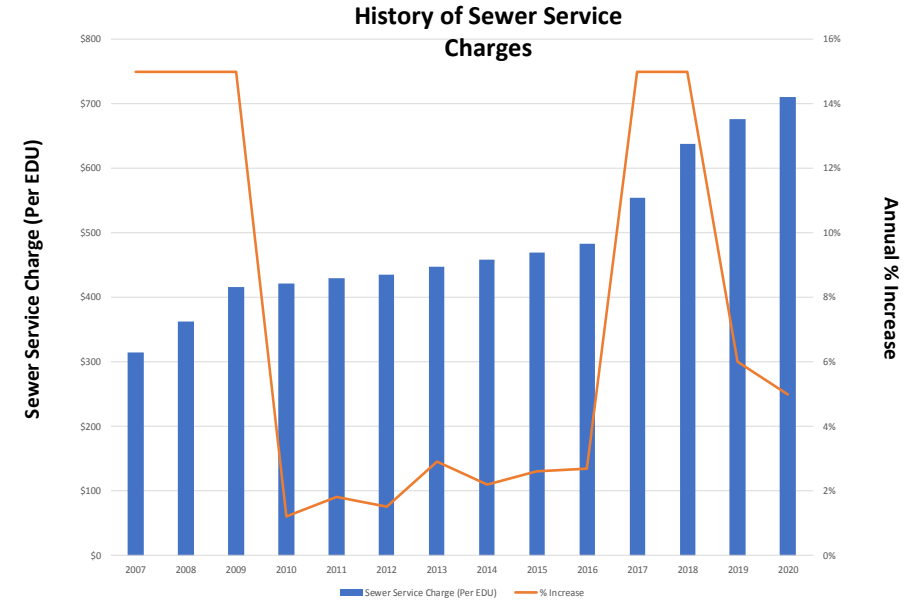
S&P Initial Assessment	Debt to Capitalization
1	Up to 20%
2	20% to 35%
3	35% to 50%
4	50% to 65%
5	65% to 80%
6	Greater than 80%

Source: NapaSan Comprehensive Annual Financial Reports for FYs 2017-2019.

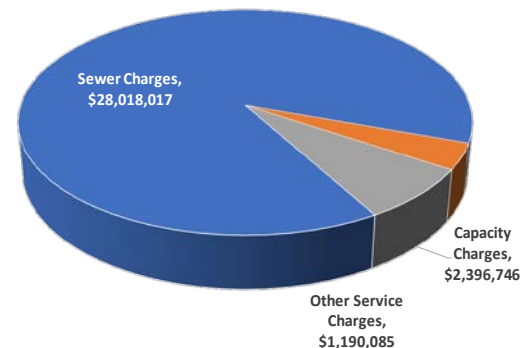
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Breakdown of System Revenues

- Residential sewer service charges are annually collected via property tax bills.
- Commercial charges are based on water consumption and are also collected on annual property tax bills.
- District staff annually determines the service charge structure after full consideration of expected operations, maintenance and capital costs.
 - Service charges are approved annually by the Board of Directors.



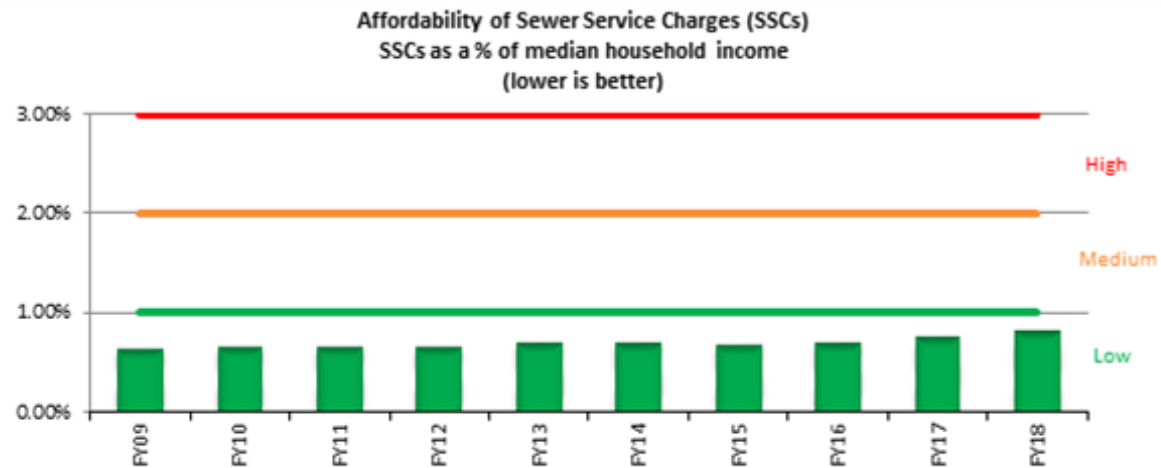
Total Operating Revenues (FY2019)



Source: NapaSan FY2019 Comprehensive Annual Financial Report.

Policy and Political Considerations

- NapaSan maintains a strict debt policy that states debt can only be used for non-reoccurring projects.
 - For example, annual sewer rehabilitation projects are not financed with long-term debt.
- From an affordability perspective, the District annually evaluates the rates as a percentage of median household income.
 - This affordability ratio is forecasted when the District undergoes Prop 218 rate hearings to set future rate increases.



Source: NapaSan.



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Evaluating Debt Capacity: Local Government / General Fund Borrower





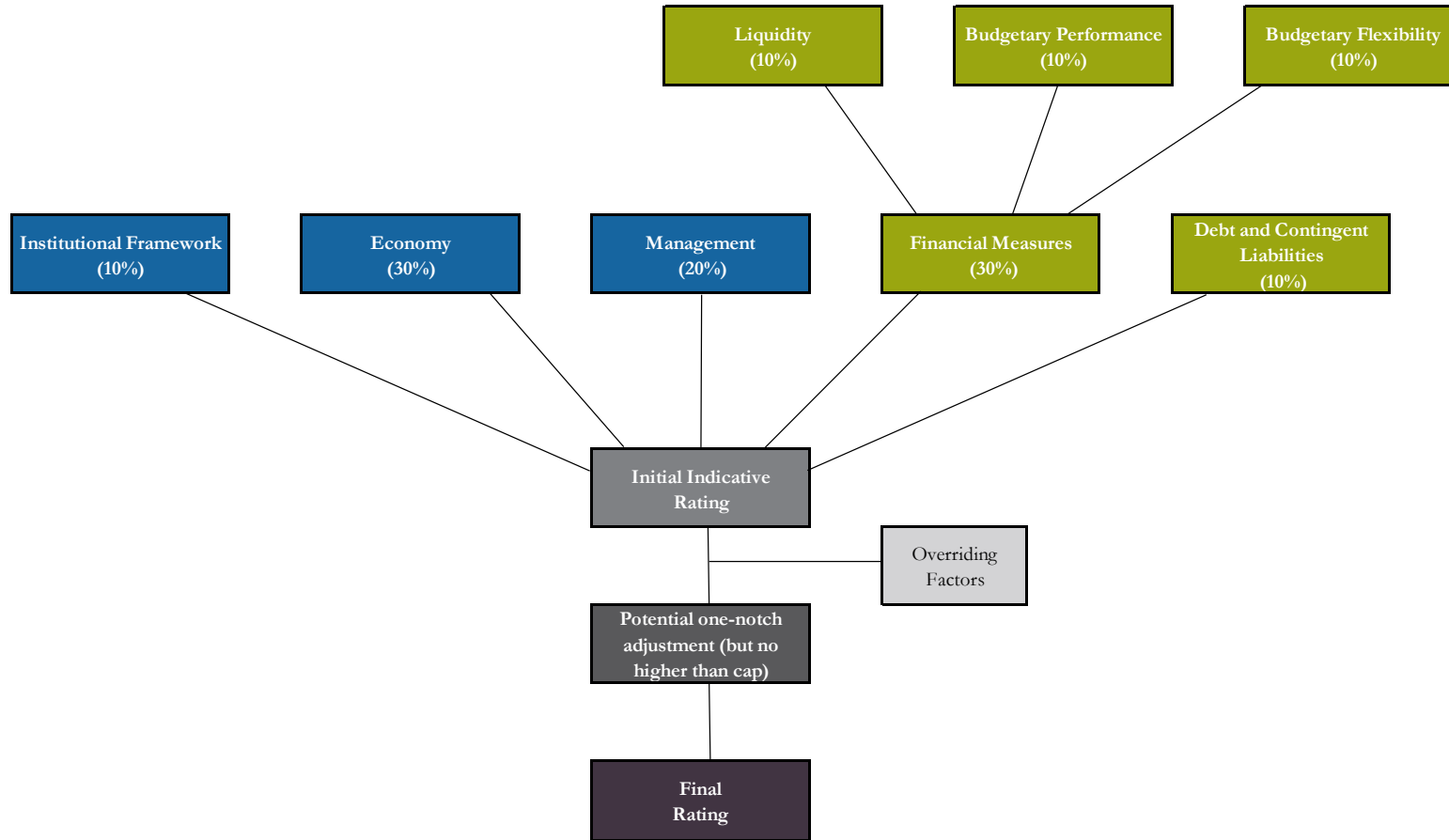
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Approach to Considering Debt Affordability

- There is no simple formula or measure of debt affordability or capacity for a General Fund-backed organization, few legal limits, and even bond market constraints have more to do with the relative cost of funds than with “debt capacity.”
- There are different measures of debt affordability:
 - **Market** capacity – what the bond market will reasonably allow without adverse consequence or penalty.
 - **Budgetary** capacity – what a local government’s budget can reasonably allow without undue stress.
- Our approach generally begins with the perspective of the credit markets and “**market capacity.**”
- We examine certain measures of a local government’s financial position which, when considered together, are widely viewed by market participants as key indicators of creditworthiness.



Standard & Poor's Local Governments General Obligation Rating Criteria



Source: Standard & Poor's U.S. Local Governments General Obligation Ratings: Methodology and Assumptions, dated September 12, 2013.



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Credit Metrics

		Financial Measures (30%)		
		Budgetary Performance (10%)	Budgetary Flexibility (10%)	Liquidity (10%)
S&P Ratios:	1. Total Gov. Funds Net Result ¹		1. Available Fund Balance as a % of Expenditures ³	1. Total Gov. Available Cash as % of Total Gov. Funds Debt Service ⁴
	2. General Fund Net Result ²			2. Total Gov Available Cash as % of Total Gov. Funds Expenditures ⁴
Debt and Contingent Liabilities (10%)				
S&P Ratios:	1. Net Direct Debt as % of Total Gov. Funds Revenue			
	2. Total Gov. Funds Debt Service as % of Total Gov. Funds Expenditures			

¹ **Total Governmental Funds Net Result (%)**: (total governmental revenues – total governmental expenditures) divided by total governmental fund expenditures.

² **General Fund Net Result (%)**: (total general fund revenues - total general fund expenditures + transfers in from other funds - transfers out to other funds) divided by general fund expenditures.

³ **Available Fund Balance**: the sum of Available General Fund Balance + any other fund balances of the government legally available for operations. For entities that report on a cash basis, the criteria use cash balances instead of fund balances.

⁴ **Total Government Available Cash**: total cash (cash, and cash equivalents + investments (when grouped with cash in the audit)) – proceeds of borrowings that are otherwise dedicated – other encumbered cash + liquidation of certain highly liquid securities.



The Debt Affordability Model

- To assist local governmental borrowers in considering debt affordability, KNN has developed a “Debt Affordability Model” (DAM), which can be used for financial forecasting as well as capital planning purposes.
- The DAM uses various inputs from a county’s financial statements to calculate key economic, financial and debt ratios.
- The DAM also models the impacts of potential *new debt* on key debt ratios.
- A local governmental borrower can then consider the potential impact of new debt on the scoring of its rating metrics. It also can compare its debt ratios under different debt issuance scenarios to “target ranges” it may establish in its debt policies, or otherwise, in order to draw conclusions about debt affordability and creditworthiness.
- Targeted debt ratios, ones can be developed based on rating agency metrics, though peer group analysis, or otherwise.



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DAM Output and San Luis Obispo County Scoring: Debt & Contingent Liabilities

Fiscal Year Ending June 30,	2017	2018
Economic and Financial Data (in 000s)		
Total Governmental Fund Revenue ⁽¹⁾	528,882	543,801
Total Governmental Funds Expenditures ⁽¹⁾	496,141	591,306
Annual Debt Service ⁽²⁾	12,725	56,758
Par Amount Outstanding ⁽²⁾	228,097	176,539
Net Direct Debt as % of Total Governmental Funds Revenue	43.13%	32.46%
Total Governmental Funds Debt Service as a % of Total Governmental Funds Expenditures	2.56%	9.60%

Total Governmental Funds Debt Service as % of Total Governmental Funds Expenditures		Debt & Contingent Liabilities (10% of Indicative Rating)				
		Net Direct Debt as % of Total Governmental Funds Revenue				
		< 30	30 to 60	60 to 120	120 to 180	≥ 180
< 8	1	2	3	4	5	
8 to 15	2	3	4	4	5	
15 to 25	3	4	5	5	5	
25 to 35	4	4	5	5	5	
≥ 35	4	5	5	5	5	

⁽¹⁾County of San Luis Obispo Annual Financial Report FY 2016-17 and 2017-18.

⁽²⁾Includes 2012 Lease Revenue Bonds, Certificates of Participation, 2003 Series A and Series C Pension Obligation Bonds, and 2009 Pension Obligation Bonds. Excludes County's 2016 I-Bank loan and 2015 State Note.

Source: Ratios calculated utilizing Standard & Poor's U.S. Local Governments General Obligation Ratings: Methodology and Assumptions as published on September 12, 2013. Ratio results are based on financial data as of fiscal year end June 30, 2018.





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DAM Output and San Luis Obispo County Scoring: Budgetary Performance and Flexibility

Fiscal Year Ending June 30,	2017	2018
Economic and Financial Data (in 000s)		
Committed Fund Balance ⁽¹⁾	\$51,262	\$53,186
Assigned Fund Balance	126,596	107,145
Unassigned Fund Balance	0	0
"Available" General Fund Balance ⁽²⁾	177,858	160,331
General Fund Revenue ⁽²⁾	464,504	483,244
General Fund Expenditures ⁽²⁾	413,876	449,519
General Fund Transfers In ⁽²⁾	995	2,269
General Fund Transfers Out ⁽²⁾	-52,221	-45,026
Total Governmental Fund Revenue ⁽²⁾	528,882	543,801
Total Governmental Funds Expenditures ⁽²⁾	496,141	591,306
"Available General Fund Balance as a % of Expenditures"	38.16%	32.42%
General Fund Net Result	-0.13%	-1.83%
Total Governmental Funds Net Result	6.60%	-8.03%

Budgetary Performance (10% of Indicative Rating)						
General Fund Net Result		Total Governmental Funds Net Result				
		> -1	-1 to -5	-5 to -10	-10 to -15	≤ -15
		> 5	1	2	3	3
-1 to 5	2	3	3	4	5	
≤ -1	3	4	4	5	5	

Budgetary Flexibility (10% of Indicative Rating)					
	Available General Fund Balance as a % of				
	> 15	8 to 15	4 to 8	1 to 4	≤ 1
		1	2	3	4

⁽¹⁾Committed Fund Balance includes: "General Reserve" and "Tax Reduction Reserve".

⁽²⁾ County of San Luis Obispo Annual Financial Report FY 2016-17 and 2017-18.

Note: Ratios calculated utilizing Standard & Poor's U.S. Local Governments General Obligation Ratings: Methodology and Assumptions as published on September 12, 2013. Ratio results are based on financial data as of fiscal year end June 30, 2018.





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DAM Output and San Luis Obispo County Scoring: Liquidity

Fiscal Year Ending June 30,	2017	2018
Economic and Financial Data (in 000s)		
Total Government Available Cash ⁽¹⁾	409,610	360,897
Total Governmental Funds Expenditures ⁽¹⁾	496,141	591,306
Total Governmental Funds Debt Service ⁽¹⁾⁽²⁾	12,725	56,758
Total Governmental Available Cash as % of Total Governmental Funds Debt Service	3218.86%	635.85%
Total Governmental Available Cash as % of Total Governmental Funds Expenditures	82.56%	61.03%

		Liquidity (10% of Indicative Rating)				
		Total Governmental Available Cash as % of Total Governmental Funds Debt Service				
Total Governmental Available Cash as % of Total Governmental Funds Expenditures		> 120	100 to 120	80 to 100	40 to 80	≤ 40
	> 15	1	2	3	4	5
	8 to 15	2	2	3	4	5
	4 to 8	3	3	3	4	5
	1 to 4	4	4	4	4	5
	< 1	5	5	5	5	5

⁽¹⁾County of San Luis Obispo Annual Financial Report FY 2016-17 and 2017-18.

⁽²⁾Includes 2012 Lease Revenue Bonds, Certificates of Participation, 2003 Series A and Series C Pension Obligation Bonds, and 2009 Pension Obligation Bonds. Excludes County's 2016 I-Bank loan and 2015 State Note.

Source: Ratios calculated utilizing Standard & Poor's U.S. Local Governments General Obligation Ratings: Methodology and Assumptions as published on September 12, 2013. Ratio results are based on financial data as of fiscal year end June 30, 2018.



San Luis Obispo County

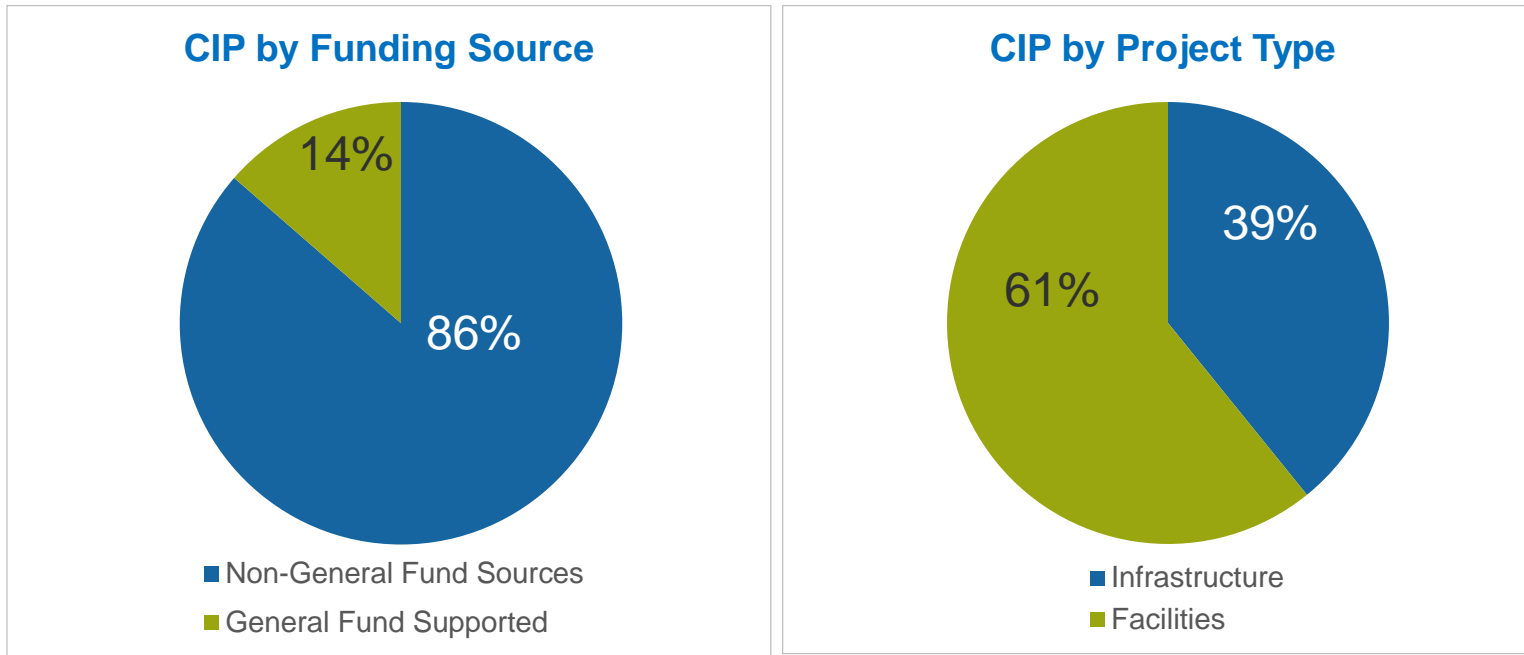
- Located on the California coast midway between the metropolitan areas of the San Francisco Bay Area and Los Angeles
- Occupies 3,300 square miles with a combined population of 280,393
- 7 incorporated cities, plus unincorporated areas
- Home to world-class beaches, a leading university in California Polytechnic State University, and prominent wine and agricultural regions in the interior of the County

- FY 2019-20 Adopted Budget
 - Total Governmental: \$648.0 million
 - General Fund: \$557.3 million



Five-Year Capital Improvement Plan (CIP)

- A multi-year planning tool design to identify facilities and infrastructure improvements with estimated costs exceeding \$100,000 over the next 5 years.



164 total projects with an estimated cost of \$559 million

Source: County of San Luis Obispo Infrastructure and Facilities Five Year Capital Improvement Plan FY 2019-20 through 2023-24.



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Facilities Projects and Various Funding Sources

<p>General Government & Community Buildings</p>	<ul style="list-style-type: none"> ▪ Capital Project Reserves ▪ General Government Building Replacement Reserves ▪ General Government Public Facility Fees ▪ Depreciation charges ▪ General Fund ▪ Grant funds when available ▪ State of California Courts
<p>Health and Social Services</p>	<ul style="list-style-type: none"> ▪ Health operating budget ▪ DSS operating budget ▪ Capital Project Reserves ▪ General Government Building Replacement Reserves ▪ Depreciation charges ▪ General Fund ▪ Grants when available
<p>Library</p>	<ul style="list-style-type: none"> ▪ Library Public Facility Fees ▪ Library Reserves ▪ Library operating budget ▪ 50% funding from the community

Source: County of San Luis Obispo Infrastructure and Facilities Five Year Capital Improvement Plan FY 2019-20 through 2023-24.





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CIP Funding Policies and Approach

- **Board of Supervisor Policies**
 - Projects that have 100% revenue offset or have their own funding source are prioritized.
 - Enterprise funds are expected to utilize their own funding for capital and maintenance improvements.
 - Library projects (except for deferred maintenance) are to be funded with 50% of the cost coming from the community in which the library improvements are proposed.

- **General Fund Support for Certain Priority Projects**
 - New facility construction
 - Deferred maintenance
 - Seismic and ADA compliance

- **New Revenue Measures for Other Priority Projects**
 - Library
 - Affordable Housing





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Impact of New General Fund Debt Issued for Priority Projects

Priority Capital Projects	Project Estimates	
	Timing (FY)	Total Cost (\$000)
Animal Shelter	2019-20	\$14,800
Subtotal Group 1:		\$14,800
Co-Located Dispatch	2020-21	\$15,000
Parking Garage	2020-21	4,750
County Operations Center Parking	2020-21	3,500
JIC Relocation	2020-21	400
Ag Commissioner & UC Extension Offices	2021-22	3,000
Subtotal Group 2:		\$26,650
Probation Office	2022-23	\$19,800
Kimball Building	2023-24	34,500
County Operations Center Buildings	2024-25	11,000
Subtotal Group 3:		\$65,300
Total All Projects:		\$106,750

■ Bonding Assumptions:

- FY 2020 and FY 2021 issuances to fund Group 1 and Group 2 projects.
- Issuance of General Fund lease obligations under “asset transfer” structure – no capitalized interest.
- 25-year, “AA” lease credit – no debt service reserve fund.





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Projected Debt & Contingent Liabilities: Impact of New Debt Upon Debt Ratios

Fiscal Year Ending June 30,	2017	2018	2019	2020	2021	2022	2023	2024
Direct Debt (including POBs, COPs, LRBs) (in 000s)								
Total Governmental Fund Revenue ^{(1),(2)}	528,882	543,801	560,115	576,918	594,226	612,053	630,414	649,327
Total Governmental Funds Expenditures ^{(1),(2)}	496,141	591,306	609,045	627,317	646,136	665,520	685,486	706,050
Existing Annual Debt Service ⁽³⁾	12,725	56,758	11,017	11,549	12,104	12,691	13,293	13,911
Existing Par Amount Outstanding ⁽³⁾	228,097	176,539	166,788	156,436	145,458	133,818	121,493	108,461
Proposed Financing 1: Animal Shelter (\$14.8 MM)								
Annual Debt Service ⁽⁴⁾				407	938	937	936	939
Par Amount Outstanding ⁽⁴⁾				14,570	14,355	14,130	13,895	13,645
Proposed Financing 2: Capital Improvement Projects (\$26.65 MM)								
Annual Debt Service ⁽⁴⁾					1,182	1,183	1,184	1,185
Par Amount Outstanding ⁽⁴⁾					26,530	26,105	25,660	25,190
Total Annual Debt Service	12,725	56,758	11,017	11,956	14,224	14,811	15,412	16,034
Total Par Amount Outstanding	228,097	176,539	166,788	171,006	186,343	174,053	161,048	147,296
Net Direct Debt as % of Total Governmental Funds Revenue	43.13%	32.46%	29.78%	29.64%	31.36%	28.44%	25.55%	22.68%
Total Governmental Funds Debt Service as a % of Total Governmental Funds Expenditures	2.56%	9.60%	1.81%	1.91%	2.20%	2.23%	2.25%	2.27%
Debt and Contingent Liabilities Scoring	2	3	1	1	2	1	1	1

⁽¹⁾County of San Luis Obispo Annual Financial Report FY 2016-17 and 2017-18.

⁽²⁾Future Total Governmental Fund Revenues and Expenditures are projected to grow at a rate of 3.00% annually.

⁽³⁾Includes 2012 Lease Revenue Bonds, Certificates of Participation, 2003 Series A and Series C Pension Obligation Bonds, and 2009 Pension Obligation Bonds. Excludes County's 2016 I-Bank loan and 2015 State Note.

⁽⁴⁾The proposed financing of the Animal Shelter project (\$14.8 million) is assumed to place in FY 2019-20. The proposed financing of the County's other capital improvement projects (\$26.65 million) is assumed to take place in FY 2020-21.

Source: Ratios calculated utilizing Standard & Poor's U.S. Local Governments General Obligation Ratings: Methodology and Assumptions as published on September 12, 2013. Ratio results are based on financial data as of fiscal year end June 30, 2018.





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Conclusion





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Conclusions – Revenue Bond Capacity

- Capacity is driven by rate structure/revenues, legal covenants (i.e., additional bonds test), debt service coverage, and policy and political considerations
- Operating reserves and liquidity provide important cushion in the event of revenue volatility.
- Rate structure planning should go hand-in-hand with capital planning
- Rating agency metrics are instructive, but should not be prescriptive.
- Agencies with fewer on-going capital needs, requiring little annual pay-as-you go funding, may prefer to aim for a lower Additional Bonds Test and lower debt service coverage, while agencies with larger on-going capital needs, requiring more pay-as-you-go annual funding may want to target higher debt service coverage



Conclusions – General Fund Affordability

- Precisely how much additional debt a local government can prudently incur may depend in large part on a variety of factors *in addition* to debt levels, such as the magnitude of other fixed obligations (i.e., pension and OPEB) and the other financial metrics discussed earlier, such as budgetary performance, budgetary flexibility and liquidity.
- Economic and demographic factors play an important role too, including population growth, employment base, tax base and revenue diversity.
- If a local government is in a “growth phase” in its capital plan, reflecting growth in population and tax base, then it may find itself needing to be at the higher end of affordability metrics, even if doing so puts pressure on credit ratings.
- Consider availability of matching or offsetting revenues in prioritization of projects: i.e., grants, enterprise revenues, new taxes or fees and/or federal and state reimbursements, all of which might suggest a more “affordable” project overall from a budgetary perspective.
- Finally, consider establishing some debt affordability targets in the capital planning process and in advance of all new debt issues.
- Utilize Debt Affordability Model and update prior to new debt at a minimum



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MSRB Rule G-42 Disclosures





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MSRB Rule G-42: Disclosure of Conflicts of Interest and Legal or Disciplinary Events

Pursuant to Municipal Securities Rulemaking Board (“MSRB”) Rule G-42, on Duties of Non-Solicitor Municipal Advisors, Municipal Advisors are required to make certain written disclosures to clients which include, amongst other things, Conflicts of Interest and any Legal or Disciplinary events of KNN Public Finance, LLC (“KNN Public Finance”) and its associated persons.

Conflicts of Interest

Other Municipal Advisor Relationships. KNN serves a wide variety of other clients that may from time to time have interests that could have a direct or indirect impact on the interests of another KNN client. For example, KNN serves as municipal advisor to other municipal advisory clients and, in such cases, owes a regulatory duty to such other clients just as it will to your entity, if hired. These other clients may, from time to time and depending on the specific circumstances, have competing interests. In acting in the interests of its various clients, KNN could potentially face a conflict of interest arising from these competing client interests. KNN fulfills its regulatory duty and mitigates such conflicts through dealing honestly and with the utmost good faith with its clients.

Compensation. KNN Public Finance represents that in connection with the issuance of municipal securities, KNN Public Finance may receive compensation from an Issuer or Obligated Person for services rendered, which compensation is contingent upon the successful closing of a transaction and/or is based on the size of a transaction. Consistent with the requirements of MSRB Rule G-42, KNN Public Finance hereby discloses that such contingent and/or transactional compensation may present a potential conflict of interest regarding KNN Public Finance’s ability to provide unbiased advice to enter into such transaction. This conflict of interest will not impair KNN Public Finance’s ability to render unbiased and competent advice or to fulfill its fiduciary duty to the Issuer.

If KNN Public Finance becomes aware of any additional potential or actual conflict of interest after this disclosure, KNN Public Finance will disclose the detailed information in writing to the Issuer in a timely manner.

Legal or Disciplinary Events

KNN Public Finance, LLC, has never been subject to any legal, disciplinary or regulatory actions nor was it ever subject to any legal, disciplinary or regulatory actions previously, when it was a division of Zions First National Bank or Zions Public Finance, Inc.

A regulatory action disclosure has been made on Form MA-I for one of KNN Public Finance municipal advisory personnel relating to a 1998 U.S. Securities and Exchange Commission (“SEC”) order that was filed while the municipal advisor was employed with a prior firm, (not KNN Public Finance). The details of which are available in Item 9; C(1), C(2), C(4), C(5) and the corresponding regulatory action DRP section on Form MA and Item 6C; (1), (2), (4), (5) and the corresponding regulatory action DRP section on Form MA-I. Issuers may electronically access KNN Public Finance’s most recent Form MA and each most recent Form MA-I filed with the Commission at the following website: www.sec.gov/edgar/searchedgar/companysearch.html.

The SEC permits certain items of information required on Form MA and Form MA-I to be provided by reference to such required information already filed on a regulatory system (e.g., FINRA CRD). The above noted regulatory action has been referenced on both Form MA and MA-I due to the information already filed on FINRA’s CRD system and is publicly accessible through BrokerCheck at <http://brokercheck.finra.org>. For purposes of accessing such BrokerCheck information, the Municipal Advisor’s CRD number is 4457537.

