

MEMORANDUM

June 1, 2018

TO: Chris Cummings, Assistant Director, Economic Development

THRU: Ed Tabor, Programs & Incentives Manager

FROM: Shanna Bailey, Regional Project Manager

Rich Rodriguez, Finance Officer

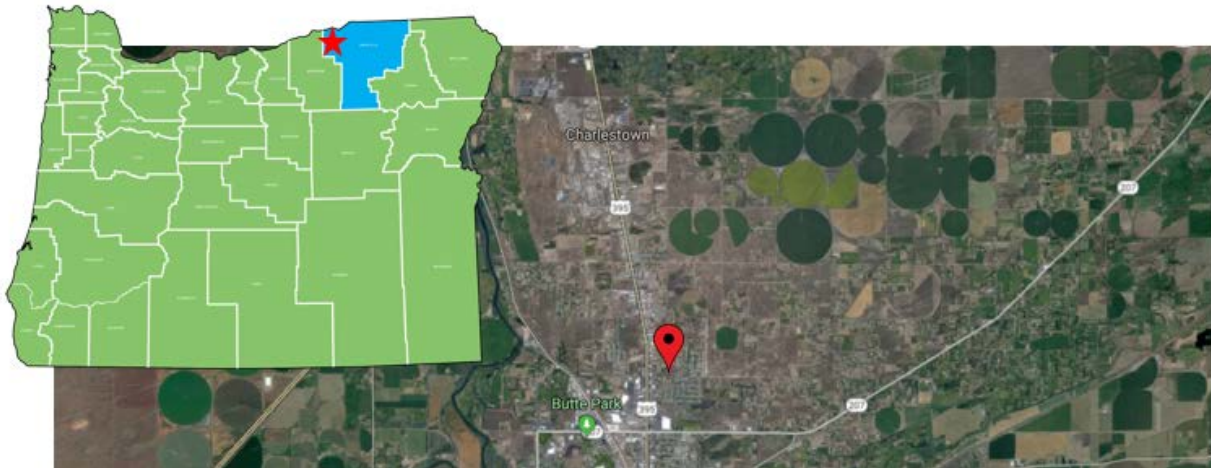
SUBJ: Funding Opportunity of \$4,516,575 – Special Public Works Program for City of Hermiston, North Hermiston Water Storage & Distribution System, No. 178-13244

Please accept this memorandum for the *Oregon Infrastructure Finance Authority* (IFA) for funding assistance. Business Oregon's (statutorily and by rule referred to as *Oregon Business Development Department*) staff administers the IFA. This memorandum will provide an application review, findings and analysis, and staff's recommendation for requested action. There may also be post approval follow-up instructions for staff.

BACKGROUND

Applicant: City of Hermiston located in Umatilla County. The city has a 2016 certified population of 17,730. The city is considered both rural and distressed.

Hermiston, North Hermiston Water Storage & Distribution 178-13244



Funding Request: Loan, grant & Principal Forgiveness

Project Type:

- Planning (technical)
- Design
- Construction

SPWF Source: SPWF Other

Project Background: The city of Hermiston is the only eastern Oregon city to have seen population growth in the past several years. However, the city recognizes that continued growth will not come without continued investment in infrastructure improvements. In addition; recent, current, and anticipated employment gains in Umatilla County have led to an increase in the number of employees commuting into the county from elsewhere for work. In an effort to capture some of these commuting employees, the city of Hermiston wishes to provide improved infrastructure, which in turn will foster investment by developers to expand the housing stock in the city. Improving the municipal water system is a viable way for the city to stimulate additional economic development.

As part of the city's planning efforts, they completed a preliminary engineering report (PER) of the water system to recommend improvements to meet current and long-term needs. Through this process the city has identified storage and pressure issues in their water distribution system. The report identified alternatives to increase supply, storage, and distribution within the Northeastern portion of the city.

An opportunity to make this infrastructure investment came when Lamb Weston, a major food processor announced their \$225,000,000 expansion project at the Hermiston Facility.

Lamb Weston, a publically traded company, has been a leader in the frozen potato industry. Headquartered in Eagle, Idaho, Lamb Weston has products in more than 100 countries. Manufacturing operations are focused in the Pacific Northwest, primarily the Columbia River Basin. Lamb Weston employs more than 6,000 people. The company has two Oregon locations, Boardman (completed a major expansion in 2013) and Hermiston (the project expansion). Lamb Weston employs over 1,600 people in Oregon with an annual payroll exceeding \$100 million including benefits. Impacts in Oregon include: producing over 1.25 million pounds of product sold domestically and internationally; paying approximately \$4.8 million in withholding for Oregon employees; \$900,000 in corporate income tax and \$3.7 million in property tax. The company's February 25, 2018 SEC 10-Q balance sheet shows \$49.4 million of cash and cash equivalents. Moody's Corporate Family Rating is 'Ba2' as of April 17, 2018.

As part of the expansion project the city of Hermiston and Umatilla County have negotiated and executed a Long Term Rural Enterprise Zone (LTREZ) agreement with Lamb Weston. As consideration of the LTREZ agreement, Lamb Weston will pay annually for 15 years, beginning in 2020, to the city of Hermiston \$450,000 and to Umatilla County \$500,000. In addition, Lamb Weston will be making a direct payment of \$50,000 to Hermiston's Parks and Recreation Department.

The city would like to move forward with their infrastructure project instead of waiting for the LTREZ payments to begin in 2020. This will alleviate some of the economic challenges associated with a growing community and housing stock shortage.

In addition, the city is partnering with Umatilla County in a revenue sharing agreement. In the agreement between the city and the County, Umatilla County will give the city of Hermiston \$500,000 each year for 4 years. In return, the city has agreed to use these funds to make water system improvements, which in turn will foster economic growth.

Project Description: The city will contract for final design and construction services to upgrade their water system through a design-build process. The proposed project will install a 1,000,000 gallon standpipe reservoir and the final design build-out will determine the pipeline route and where it will connect into the existing system, and the final upgrades needed at existing booster pump stations.

Work Plan: The work will be completed in two phases, design and construction. The attached work plan table on page eight below includes the project activities and the anticipated completion dates.

Public Involvement Statement: The city has held several public meetings discussing this project throughout the planning stages over the last two years.

FINDINGS AND ANALYSIS

This project helps implement the following goals and objectives of providing funding to municipalities for publicly-owned facilities that support economic and community development in Oregon:

- Special Public Works Fund: *to provide financial or other assistance to enable municipalities to construct, improve and repair those facilities that are essential for supporting continuing and expanded economic activity (ORS 285.B.413 (2))*
- Statewide planning goals #6 air, water, and land resources quality; #9 economic development; and #11 public facilities and services.
- Department's strategic plan priority: Cultivate Rural Economic Stability

Program Findings & Compliance

1. The city of Hermiston is an eligible applicant as defined in ORS 198.010
2. Project is not to achieve compliance.
3. Project priority is high.
4. Program suggestions: desktop monitoring conducted approximately halfway through the project.
5. Pre-agreement Costs have been authorized, with no guarantee of reimbursement. Costs include: Land Acquisition \$8,575 and Engineering fees \$23,000. Invoices incurred before funding may be requested, for these budget line-items, for no more than \$31,575.
6. This project is found to be compliant with applicable Department policies, Rules and Statutes. The programmatic and financial sections of the Eligibility Checklist have been completed and the application has been determined per current ORS to be eligible for funding.

Financial Findings & Compliance

Repayment source

The repayment source is the city's General Fund. The next section provides a summary of the General Fund.

General Fund summary

The following table shows a performance review of the Applicant's General Fund for the last three audited fiscal years ending 2017 and fiscal year 2018 budget.

General Fund				
City of Hermiston				
Performance Review	audited	audited	audited	budgeted
FY Ending June 30th	2015	2016	2017	2018
Beginning Fund Balance	4,928,927	5,066,753	4,709,050	4,102,770
<u>Revenues</u>				
Property Taxes	4,917,591	5,021,221	5,167,756	5,168,000
Other Operating Revenues	2,073,242	2,451,625	2,310,832	2,862,590
Operating Revenues	6,990,833	7,472,846	7,478,588	8,030,590
Interest and Miscellaneous	176,932	151,631	222,381	140,000
Other Non-Operating Revenues	1,083,115	531,826	586,966	572,780
Total Non-Operating Revenues	1,260,047	683,457	809,347	712,780
Total Revenues	8,250,880	8,156,303	8,287,935	8,743,370
<u>Expenditures</u>				
Personal Services	5,680,963	6,034,286	6,456,741	7,217,860
Materials & Services	2,044,256	2,236,939	2,359,538	2,743,548
Total Operating Expenses	7,725,219	8,271,225	8,816,279	9,961,408
Net Operating Income	(734,386)	(798,379)	(1,337,691)	(1,930,818)
Capital Outlay	125,810	776,315	141,577	240,300
Debt Service	0	0	0	198,900
Total Expenses	7,851,029	9,047,540	8,957,856	10,400,608
Net Revenues	399,851	(891,237)	(669,921)	(1,657,238)
Net Transfers/Adjustments	(262,025)	533,534	63,641	1,932,145
Ending Fund Balance	5,066,753	4,709,050	4,102,770	4,377,677

General Fund operating revenues during the three most recent years have shown an increasing trend, up 7%. Expenditures in 2017 relative to 2016 benefited from a \$635,000 decrease in capital expenditures through this was largely offset by an increase of \$423,000 in personal costs and an overall decrease of expenses by 1%.

Of the 2017 ending fund balance 94% is designated as unassigned. The three most recent year's average unassigned ending fund balance was a generous 48% of average operating expenses.

Debt service analysis

Net Revenues for Debt Coverage: The \$450,000 in annual payments between 2020 and 2035 from Lamb Weston, and directed into the city's General Fund, total \$6.75 million while the County's

agreed annual contribution of \$500,000 to the city for the four years 2020 and 2023 for the project totals \$2 million. The available General Fund monies derived from Lamb Weston total \$6.75 million which is more than adequate to repay the \$4,516,575 loan. The city intends to use the \$2 million in County monies to accelerate payments on the loan.

The below table reflects the Projected Net Revenues for the Applicant’s General Fund as provided with the application. The proforma focuses solely on the source of repayment monies and the associated debt service for the Project. It reflects more than adequate net revenues necessary to provide 1.10 debt service coverage ratio. The 1.10 coverage was selected because of the source of repayment being the General Fund and the dedicated strength of the revenue stream.

Summary of Revenues, Expenditures, and Debt Service Coverage							
City of Hermiston							
PRO FORMA	Current FY	Projected					
Year (ending June 30th)	2018	2019	2020	2021	2022	2023	2024
Beginning Fund Balance	0	0	0	851,000	1,420,300	1,989,600	2,558,900
Operating Revenues							
City fee payments from Lamb Weston	0	0	450,000	450,000	450,000	450,000	450,000
County fee payments from Lamb Weston to City	0	0	500,000	500,000	500,000	500,000	0
Total Operating Revenues	0	0	950,000	950,000	950,000	950,000	450,000
Operating Expenses							
Personal Services	0	0	0	0	0	0	0
Materials & Services	0	0	0	0	0	0	0
Total Operating Expenses	0	0	0	0	0	0	0
Debt Service							
Funds Avail for Debt Coverage	(0)	(0)	950,000	950,000	950,000	950,000	450,000
Other Proposed Loan	0	0	0	0	0	0	0
IFA Proposed Loan	0	0	99,000	380,700	380,700	380,700	380,700
Total Debt Service	0	0	99,000	380,700	380,700	380,700	380,700
Debt Service Coverage Ratio	<i>N/A</i>	<i>N/A</i>	<i>9.60</i>	<i>2.50</i>	<i>2.50</i>	<i>2.50</i>	<i>1.18</i>
Other Activities							
Cash Avail After Debt Service	(0)	(0)	851,000	569,300	569,300	569,300	69,300
Loan Proceeds / Drawdowns	150,000	2,759,575	1,607,000	0	0	0	0
Capital Outlay (OUT)	(150,000)	(2,759,575)	(1,607,000)	0	0	0	0
Other Non-Operating Activity	0	0	0	0	0	0	0
Net Other Activity	0	0	0	0	0	0	0
Net Transfers IN (OUT)	0	0	0	0	0	0	0
Adjustments	0	0	0	0	0	0	0
Net Transfers & Adjustments	0	0	0	0	0	0	0
Ending Fund Balance	0	0	851,000	1,420,300	1,989,600	2,558,900	2,558,900

While the proforma is based on a 15-year loan amortization, the city intends to fully repay this obligation in about nine years. This is possible because of the dedicated \$500,000 available annually from the County for the first four years.

Existing obligations and risks

The following table reflects the applicant’s debt service as of the 2017 audit.

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Summary of Outstanding Debt Obligations					
City of Hermiston					
Loan Source	June 30, 2017 Balance	Annual Debt Service	Primary Pledge	Secondary Pledge	Maturity
Net Direct Debt					
2017 Series FF&C	\$3,713,190	\$126,749	URA, Tourism Assessments, Water	FF&C	2037
2013 Series FF&C - Pool refunding bonds	\$2,926,471	\$116,342	Property and transient room taxes.	FF&C	2032
2011 LTGO - Refunding regional water bonds	\$2,124,296	\$259,912	Water and Sewer System	LTGO - Taxes	2024
<i>Net Direct Debt</i>	\$8,763,957	\$503,003			
Self-Supporting Debt					
2017 FF&C - Water bonds	\$3,368,148	\$120,562	URA, Tourism Assessments, Water	FF&C	2037
2016 FF&C Series A and B Refunding - Electric bonds	\$16,407,668	\$635,495	Electric System	FF&C	2033
2014 Revenue bonds - Sewer and water	\$4,957,558	\$135,546	Utility Fund Net Revenues	Revenue Pledge	2039
Other Self-Supporting Debt					
BizOR - L09004	\$26,923	\$9,884	Utility Fund Net Revenues	FF&C	2019
Oregon DEQ - R43770	\$3,643,679	\$290,127	Utility Fund Net Revenues	FF&C	2035
Oregon DEQ - R43771	\$14,963,812	\$1,203,865	Utility Fund Net Revenues	FF&C	2035
<i>Net Self-Supporting Debt</i>	\$43,367,788	\$901,487			
Gross Bonded Debt	\$52,131,745	\$1,404,490			

(Note: The 2017 Full Faith and Credit Bond was one issuance. The city's audit opted to break out the liabilities according to the underlying primary pledged repayment source)

The city's refunding bonds are evidence long-term liabilities are being well managed, a favorable factor. Access to the public debt markets is also a favorable factor because the city has the option to use its own liquidity or to gain liquidity from the public markets for finance capital projects or other needs. See also the section "Applicant's bond rating".

Underwriting standards

The Applicant meets 11 of the 15 applicable indicators in the attached Financial Summary. The following indicators are not met:

- Net Direct Debt Service to General Fund Revenues (mry) [6.07% is not < 5%]
- Percentage of Debt Retired in 10 Yrs. [29.34% is not > 60%]
- Unemployment Rate as a Percentage of State Avg. [113.64% is not < 110% standard]
- Per Capital Income as Percentage of State Avg. [83.21% is not > 85% standard]

Applicant's bond rating The city's underlying rated is 'AA-' by Standard and Poor's (S&P) while the city's dedicated revenue bonds are rated 'AA' by S&P. The most recent rating action, associated with the March 2017 Full Faith and Credit issuance, was S&P raising its long-term underlying rating from 'A+' to 'AA-' along with a stable outlook.

Financial statement of program SPWF, as of April 8, 2018

1. Available funds \$32,776,721
2. Remaining balance, if the project is approved, is \$28,260,146
3. State disbursement schedule will be submitted as required by the contract. Funds will be disbursed on a reimbursement basis.
4. All existing Business Oregon loans paid as agreed

Project Repayment Phase Loan Summary						
Type	Award Amount	Grant Amount	Total Loan Amount	Interest Rate	Amortized [in years]	Est. Annual Payment*
SPWF	\$4,516,575	\$0	\$4,516,575	3.09%	15	\$380,700
Total	\$4,516,575	\$ 0	\$4,516,575			\$383,500
<i>Payment rounded to nearest \$100.</i>						

Funding Recommendation

Budget Line Items	SPWF	Totals
Engineering / Architecture	\$ 250,000	\$250,000
Construction	\$ 3,212,900	\$ 3,212,900
Construction Contingency	\$ 482,100	\$ 482,100
Land Acquisition	\$ 90,000	\$ 113,000
Construction Management	\$ 340,000	\$ 340,000
Environmental/Cultural	\$ 50,000	\$ 50,000
Right of Way Acquisition	\$ 60,000	\$ 60,000
Preliminary: Engineering	\$ 23,000	\$ 23,000
Preliminary: Land Acquisition	\$ 8,575	\$ 8,575
Total	\$ 4,516,575	\$ 4,516,575

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Proposed Work Plan

Activity	Date
Begin Design Engineering	May 2018
Complete Design Engineering	Aug 2018
Property Acquisition – water tank location	Sept 2018
Bid, Review, and Award project	Oct 2018
Begin Construction	Oct 2018
Complete Construction	Dec 2019
Project Close-out	Feb 2020

Source of Business Oregon Funds (Indicate Loan/Grant/Principal Forgiveness, Bond, Private or Public, and Taxable or Tax Exempt)	Amount
Special Public Works Fund: Loan, Public, Tax Exempt (after consulting with Bond Counsel)	\$4,516,575
	\$0
Total	\$4,516,575

Source of Other Funds (For other State funds, indicate loan / grant, et cetera)	Amount
None	\$0
	\$0
Total	\$ 0

Staff’s Recommendation

The proposed loan will be structured in two phases. The first phase, Construction, will accrue interest on actual funds disbursed, estimated first disbursement will be in July 1, 2018. All accrued interest during the construction phase (estimated to be \$99,000) will be due prior to or with the first principal and interest payment. The interest rate will be set at 3.09% for this phase. Construction is scheduled for completion by December, 2019.

The second phase (Repayment Phase) will begin with constant annual payments of principal and interest sufficient to repay the outstanding principal balance, together with interest, within a 15 year period. The estimated first principal and interest payment due date is December 1, 2021 . The loan can be prepaid in part or in full without penalty. The interest rate will be set at 3.09% for the repayment phase. The “Repayment Phase Loan Summary” table summarizes the repayment phase of the proposed financing.

Funding Recommendation and Conditions of Award

Conditions:

Based upon the following analysis, the award recommended above should be subject to the following conditions:

- A. Full Faith and Credit Pledge.** The Recipient will be required to pledge its full faith and credit and taxing power within the limitations of Article XI, Sections 11 and 11 b, of the Oregon Constitution to pay the amounts due under the Financing Contract. The Financing Contract shall be payable from all legally available funds of the Recipient.

- B. Financial Covenants.** The Recipient shall collect taxes, charge rates and fees and manage expenses in connection with the operation of the General Fund which, when combined with other revenues, are adequate to generate Net Revenues each fiscal year at least equal to one hundred (100%) percent of the annual debt service due in the fiscal year on the Loan, any outstanding senior lien obligations, and any outstanding Parity Obligations.

- C. Other Requirements.** The Recipient will be required to grant to the State a security interest in and irrevocably pledge the Recipient's Lamb Weston Fee Payments derived from executed agreement between Umatilla County, city of Hermiston, and Lamb Weston and the County's agreed payment to the City.

List of Attachments

Financial Summary