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Meeting: **Reservoir Committee & Authority Board** **April 19, 2024**
Agenda Item 3.3

Subject: **Draft Plan of Finance Update – Funding Construction Payments**

Requested Action:

Discuss the development of an Interim Financing Plan, including reviewing assumptions related to how the project construction costs will be funded and the plan for cash needs from all the Storage Partners throughout construction.

Detailed Description/Background:

As presented in the Draft Plan of Finance in May 2023, Amendment 3 funding is expected to support activities through the end of calendar year 2025. Looking beyond 2025, the Sites Authority anticipates executing a borrowing (either through the public market, a bank loan or a direct placement of a debt instrument) to provide ongoing funding for design and construction activities, including land purchases. It is important to be discussing this now to ensure that Participants are incorporating the appropriate cash needs within their CIP's and Capital Budgets.

The Interim Financing Plan is being prepared to describe the different borrowing instruments, the pros and cons of each and provide a recommended path forward to executing a borrowing in sufficient time to meet the Sites Authority's funding needs in 2026 and beyond.

Interim Financing encompasses the entire construction period as it is short-term construction financing that is anticipated to be refunded with long-term debt such as a WIFIA loan or long-term tax-exempt revenue bonds or a combination of both around the conclusion of construction and the beginning of operations.

A critical factor for interim financing is answering the question "will interest on short term debt issued during construction be paid off as accrued during construction or will the interest be accumulated and compounded to be paid off upon refinancing to the long-term debt (also known as capitalized interest)?" This has implications for the amount of the annual payments, which affects project affordability (i.e unit cost of water).

There are three primary reasons for using interim financing through construction:

1. To meet cash flow needs as the project moves forward.
2. To cash flow the expenditures to be reimbursed by the state and federal governments.

3. To reduce the overall interest cost of the project since, under most market circumstances, short-term interest rates are lower than long-term interest rates.

The two primary choices for interim financing are issuing short-term notes (1-5 years) or bank loans (e.g., revolving lines of credit, direct placements/drawdown loans). Each of these instruments has different levels of administrative complexity, interest rates, and flexibility. The Interim Financing Plan will outline evaluative criteria to rank the alternatives, including:

a. Administrative ease
b. Rollover risk
c. Credit terms
d. Structuring flexibility (e.g., capitalizing interest - which is the option to defer repayment of interest during construction. Whether or not to capitalize interest is a decision that will need to be made as part of the interim financing plan
e. Upfront cost
f. Interest rate risk (e.g., locking in a 5-year interest rate vs. Monthly interest rate resets)

Assumptions and approach for developing the Interim Finance Plan were reviewed with the WIFIA Ad Hoc Subcommittee and their feedback will be integrated. The Interim Finance Plan will be part of the forthcoming Plan of Finance update (anticipated to be available concurrent with the Class 3 cost estimate (refer to Agenda Item 3.2). Further, the Ad Hoc Subcommittee concurred with proceeding with a competitive Request for Proposals from investment and commercial banks to solicit banking support for these financings. This will likely get started later this year or early 2025.

Staff would benefit from Participants identifying any other information needs that will be required between now and execution of the B&O Contract.

Prior Action: May 2023: Received update on Draft 2023 Plan of Finance.

Fiscal Impact/Funding Source: The Amendment 3 Work Plan includes a sufficient budget to cover required resources and activities in support of the Plan of Finance and ultimately, the Benefits and Obligations Contract development. Any required adjustments based on feedback during the final rating or the WIFIA Loan development will be considered within the Fiscal Year Budget development process.

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Attachments: None.