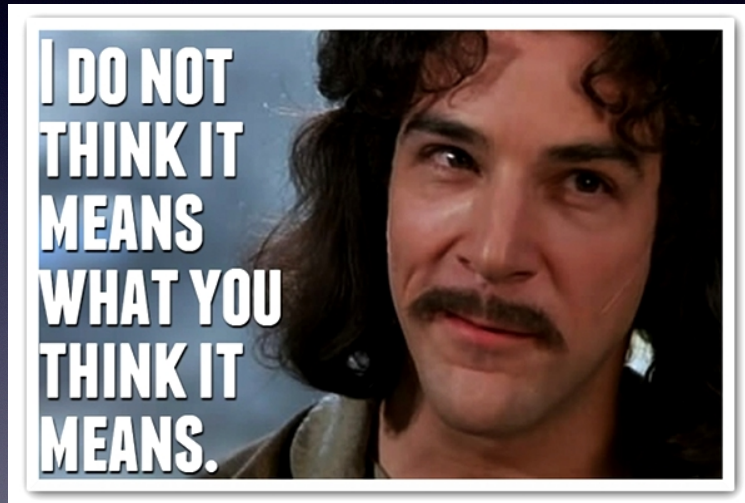


The Lompico Surcharge

or...



SLVWD Regular Board Meeting: 10/20/2016

Lompico Surcharge.key - October 20, 2016

A long time ago in a galaxy far,
far away....

Lompico and SLVWD began merger
discussions



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At some point, the County joined in...



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In 2014, a
4-Point Agreement
was reached:

- A. Capital Bond or Other Financial Instrument
- B. Bond Oversight Committee
- C. Pay-Off PERs Side Fund Loan
- D. Lompico Surcharge

SAN LORENZO VALLEY WATER DISTRICT

RESOLUTION NO. 31 (13-14)

SUBJECT: RESOLUTION APPLYING TO THE SANTA CRUZ LOCAL AGENCY FORMATION COMMISSION TO AMEND THE SPHERES OF INFLUENCE OF THE LOMPICO COUNTY WATER DISTRICT AND THE SAN LORENZO VALLEY WATER DISTRICT, AND FOR A BOUNDARY REORGANIZATION CONSISTING OF DISSOLUTION OF THE LOMPICO COUNTY WATER DISTRICT AND ANNEXATION OF TERRITORY WITHIN THE LOMPICO COUNTY WATER DISTRICT TO THE SAN LORENZO VALLEY WATER DISTRICT

WHEREAS, the Lompico County Water District and the San Lorenzo Valley Water District are located adjacent to one another in the watershed of the San Lorenzo River, provide potable water to their respective customers, and operate under the authority of the State of California, County Water District Law (Water Code Section 39000 et seq.); and

WHEREAS, the Lompico County Water District and the San Lorenzo Valley Water District have studied options for providing future water service in Lompico and concluded that the Lompico water system could be operated more efficiently if the Lompico water system were part of the San Lorenzo Valley Water District; and

WHEREAS, representatives of the two districts have negotiated the terms and conditions under which the Lompico County Water District can be reorganized into the San Lorenzo Valley Water District in a manner that provides for the efficient provision of potable water to the territory presently served by both districts;

NOW, THEREFORE, BE IT RESOLVED by the Board of Directors of the San Lorenzo Valley Water District as follows:

1. Pursuant to Government Code section 56428, the Lompico County Water District and the San Lorenzo Valley Water District jointly propose and apply to the Local Agency Formation Commission ("LAFCO") for the following Sphere of Influence Amendments:
 - a. The San Lorenzo Valley Water District Sphere of Influence to be expanded to include the current Lompico County Water District Sphere of Influence (Exhibit "A").
 - b. The Lompico County Water District Sphere of Influence to be amended to have a "zero" sphere of influence.
2. Pursuant to Government Code section 56654, the Lompico County Water District and the San Lorenzo Valley Water District jointly propose and apply to the Local Agency Formation Commission for a boundary reorganization consisting of the following changes of organization:
 - a. The Lompico County Water District will be dissolved.
 - b. The San Lorenzo Valley Water District will annex all the current territory within the boundaries of the Lompico County Water District (Exhibit "A").

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Lompico Surcharge as approved by LCWD, SLVWD and LAFCo

D) LOMPICO WATER RATES AND CHARGES

SLVWD shall bill the Lompico customers of SLVWD the same rates as the other customers within SLVWD. However, prior to filing of the Certificate of Completion, in order to cover the difference between SLVWD's estimated revenues collected in Lompico and SLVWD's estimated operating costs in Lompico, Lompico County Water District shall enact a reduction in their water rates, effective only upon the reorganization, so that \$140,000 in excess of the amount generated by SLVWD rates would be collected in the first year following the effective date of the reorganization. LAFCo shall authorize SLVWD to continue to collect these Lompico charges after the reorganization. Prior to the Certificate of Completion being filed, SLVWD will deliver a letter to the LAFCo Executive Officer indicating that the charges adopted by the Lompico County Water District are structured in a manner that SLVWD is willing to implement. The Lompico charges shall not exceed the following amounts:

Year	Beginning	Per Month/Per Connection
1	Upon the effective date of the reorganization	\$23.50
2	One year after affective date of the reorganization	\$19.50
3	Two years after affective date of the reorganization	\$8.50
4	Three years after affective date of the reorganization	\$5.50
5	Four years after affective date of the reorganization	\$5.50

The Lompico charges shall be phased out no later than five years after the effective date of the reorganization.

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Tonight's Question

- Should SLVWD reduce the Lompico Surcharge to account for full payment of the two debts recognized in the 2014 pro forma?

Lompico Surcharge per month per connection					
	2015/16	2016/17	2017/18	2018/19	2019/20
Per Agreement ->	\$23.50	\$19.50	\$8.50	\$5.50	\$5.50
W/O Debts ->	\$18.85	\$15.95	\$8.50	\$5.50	\$5.50
Difference ->	(\$4.65)	(\$3.55)	0	0	0

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From LAFCO... "Its (Lompico Surcharge) origin is from the pro forma for the SLVWD's operating costs of the Lompico system. Since the infrastructure is in poor shape and does not have electronic controls or meters, the Lompico system initially will cost the SLVWD more to run on a per-connection basis than the rest of their district. The charge would avoid a situation where the SLVWD customers in its other service areas are subsidizing the Lompico operating costs."

FIVE YEAR MERGER PRO FORMA BUDGET FY 14/15 TO FY 18/19						LEVEL CFD PAYMENTS	
LCWD FY12/13	LCWD FY13/14	Merger FY14/15	Merger FY 15/16	Merger FY 16/17	Merger FY 17/18	Merger FY 18/19	
SALARIES AND BENEFITS	259,385	235,119	270,375	278,486	243,815	226,016	221,157
SUPPLIES AND SERVICES	279,170	265,460	104,751	169,679	174,783	174,783	179,952
DEBT SERVICE, JUDGMENTS, TRANSFER	44,678	80,820	27,315	20,068	0	0	0
TOTAL EXPENDITURES	577,237	599,425	462,421	468,227	418,578	400,779	401,109
PROPERTY TAXES	52,000	52,000	53,040	54,101	55,183	56,286	57,412
CONNECTION FEES, OTHER CHARGES	2,300	5,425	3,000	3,000	0	0	0
RESIDENTIAL WATER SALES	449,150	530,000	266,000	295,000	310,000	310,000	310,000
LOMPICO CHARGE	0	0	138,381	114,066	51,273	32,307	31,446
OTHER REVENUE	2,000	2,000	2,000	2,060	2,122	2,185	2,251
TOTAL REVENUES	570,391	599,425	462,421	468,227	418,578	400,779	401,109
ANNUAL CFD PAYMENTS ON PROPERTY TAX	0	0	0	468	468	468	468
CFD PAYMENTS, CONVERTED TO BI-MONTHLY	0	0	0	78	78	78	78
LOMPICO CHARGE, MONTHLY			23.50	19.50	8.50	5.50	5.50
LOMPICO CHARGE, BI-MONTHLY			47	39	17	11	11
LOMPICO TOTAL BI-MONTHLY COST			137	217	200	194	194

Lompico Surcharge.key - October 20, 2016

Pro Forma

Business Financial statements

In business, **pro forma financial statements** are prepared in advance of a planned transaction, such as a merger, an acquisition, a new capital investment, or a change in capital structure such as incurrence of new debt or issuance of stock. The pro forma models the anticipated results of the transaction, with particular emphasis on the projected cash flows, net revenues and taxes. Consequently, **pro forma statements summarize the projected future status of a company, based on the current financial statements.** For example, when a transaction with a material effect on a company's financial condition is contemplated, the finance department will prepare, for management and board review, a business plan containing pro forma financial statements demonstrating the expected effect of the proposed transaction on the company's financial viability. Lenders and investors will require such statements to structure or confirm compliance with debt covenants such as debt service reserve coverage and debt to equity ratios. Similarly, when a new corporation is envisioned, its founders will prepare pro forma financial statements for the information of prospective investors. Pro forma figures should be clearly labeled as such and the reason for any deviation from reported past figures clearly explained.

Also, banks will request pro forma statements in lieu of tax returns for a start up business in order to verify cash flow before issuing a loan or line of credit.

https://en.wikipedia.org/wiki/Pro_forma

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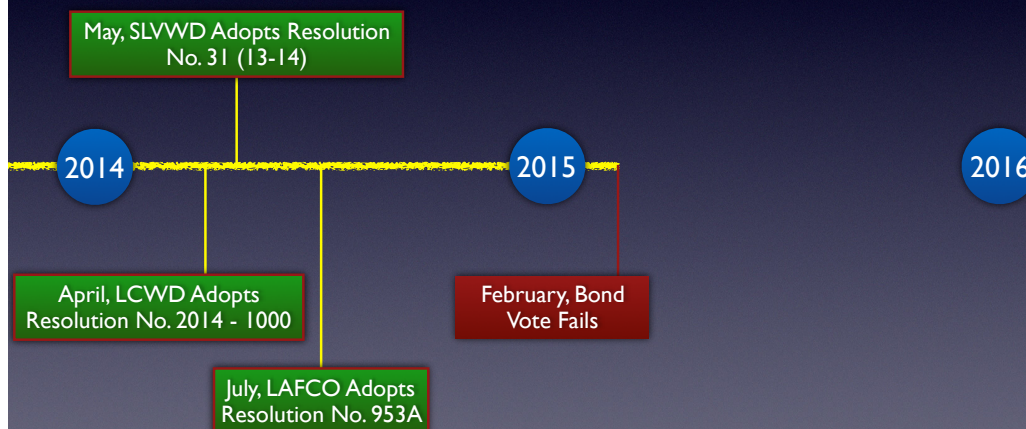
Pre 2014...Negotiating the Future...

- During negotiations someone asked, “What happens to the surcharge if Lompico pays off its debts prior to merger?”
- Someone on SLVWD side offered, “The Lompico Surcharge would/could be reduced accordingly.”
- Director Rapoza stated at a Feb 14, 2014 Lompico Liaison Committee, “... Discussion will continue until final document is done.”
- Final Agreement...



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Abbreviated History of LCWD/SLVWD Merger



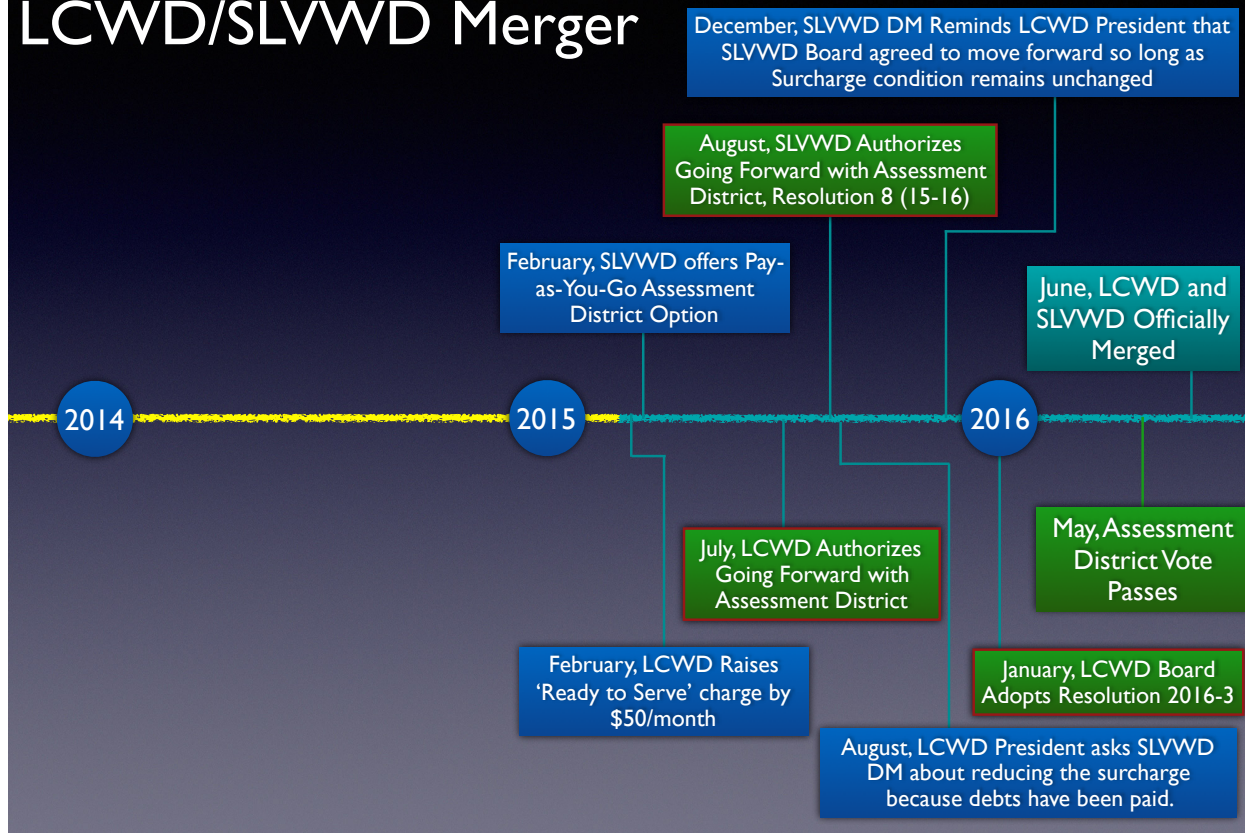
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Bond Vote Failure the End of the Merger?

- No... SLVWD Proposes a pay-as-you-go 10-year Assessment District as an alternative 'similar revenue instrument' provided for in Condition A, Infrastructure Bond.
- All Other Conditions of Agreement Shall Remain Unchanged, otherwise a new LAFCO Application is needed.

Lompico Surcharge.key - October 20, 2016

Abbreviated History of LCWD/SLVWD Merger



Lompico Surcharge.key - October 20, 2016

Last Minute Discussion in Late 2015

"... but what about the surcharge that we were told would be reduced if the debts we owe were paid off before the merger? What about if we have money in the bank at the end of the day?"

- eMail from Lois Henry to Brian Lee, August 27, 2015

"...if we have \$100,000 in the bank when the vote passes can we use that money to reduce the surcharge? I suppose that would need to be written up by a lawyer. I know Pat sent you information on the surcharge that showed the charge included two debts one which has been paid off and one that will be paid off by the time the vote is counted."

- eMail from Lois Henry to Brian Lee, December 21, 2015

"... I am confused about the loans and surcharge discussion, so a meeting to discuss is a very good idea. My understanding is that 'loans' and 'surcharges' were separate items in the LAFCO application:

Item A was the Infrastructure Bond or similar revenue instrument (Assessment District).

Item B was the Bond Oversight Committee

Item C was the Loan Payback

Item D was the Lompico Water Rates and Charges (The 'Lompico Charges' or surcharge)

My Board agreed to move forward with the Assessment District as a similar revenue instrument to the Infrastructure Bond, but specifically avoided changing any of the conditions on B, C and D to avoid the need for refiling the LAFCO application.

However, that does not answer your question regarding what to do about 'money in the bank' upon merger. I'm not sure anyone expected there to be a bank account worth discussion. Now is a good time to figure that out.

Financially it might be better to apply that money to capital costs vs. the labor surcharge. It is the difference between reducing a 20-year loan @ 3%-ish vs. reducing a 5-year surcharge that gets reduced every year anyway. I also recognize that political issues may get in the way of what is financially best."

- eMail from Brian Lee to Lois Henry, December 21, 2015

Lompico Surcharge.key - October 20, 2016

January 19, 2016 -

LCWD Board Approves Rate Reduction to match Lompico Surcharge

RESOLUTION NO. 2016-3

A RESOLUTION AUTHORIZING REDUCTION OF LOMPICO COUNTY WATER DISTRICT RATES EFFECTIVE UPON COMPLETION OF MERGER WITH SAN LORENZO VALLEY WATER DISTRICT.

LOMPICO COUNTY WATER DISTRICT

RESOLVED, by the Board of Directors of the Lompico County Water District, Santa Cruz County, California, that,

WHEREAS, the Board of Directors has the duty and authority to establish policies governing District operations, activities, and finances.

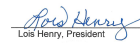
NOW, THEREFORE, BE IT RESOLVED THAT the Board of Directors of the Lompico County Water District as follows:

1. Effective only upon the completion of the Lompico Reorganization (the "Merger") as authorized in Resolution No. 953-A of the Local Agency Formation Commission, the Lompico County Water District rates will be reduced to the following amounts:

Year	Beginning	Per Month Per Connection
1	Upon the effective date of the reorganization	\$23.50
2	One year after effective date of the reorganization	\$19.50
3	Two years after effective date of the reorganization	\$8.50
4	Three years after effective date of the reorganization	\$5.50
5	Four years after effective date of the reorganization	\$5.50

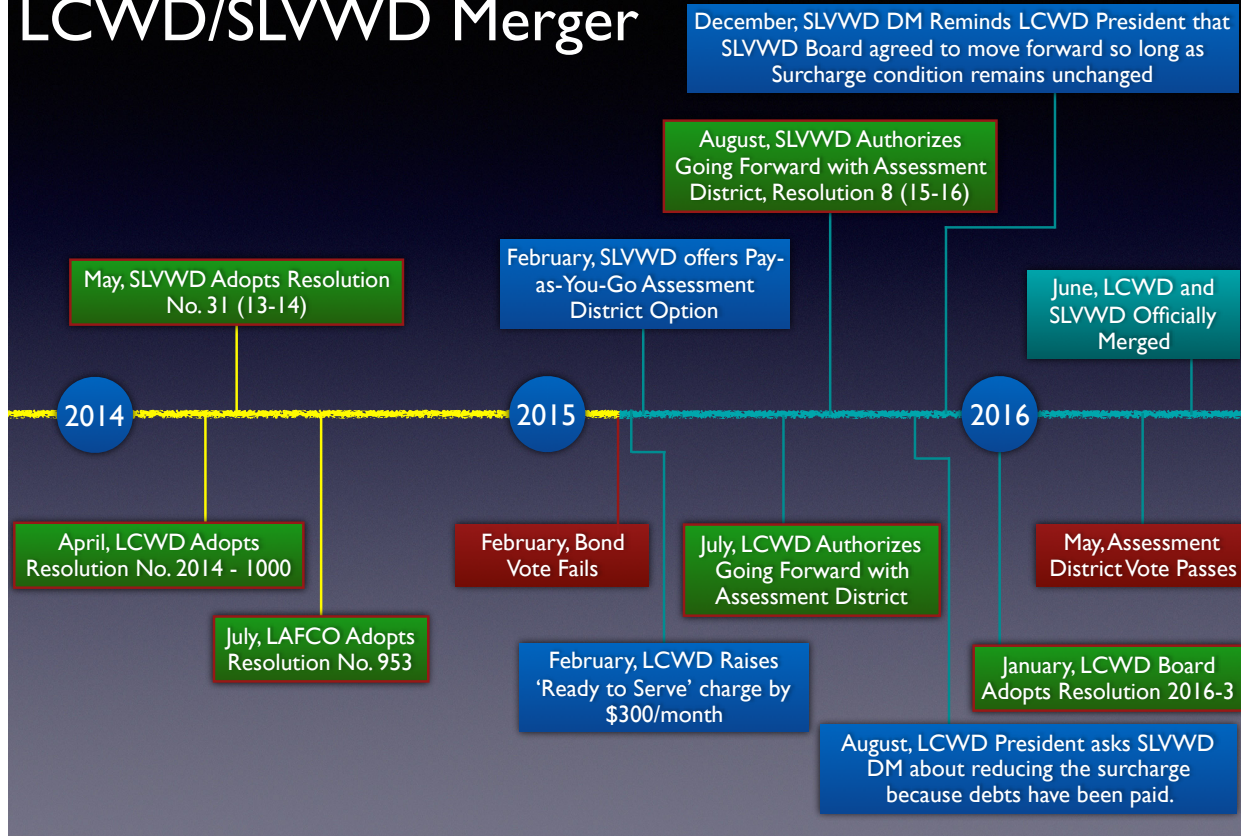
The forgoing Resolution was duly and regularly introduced and passed, and adopted by the Board of Directors of the Lompico County Water District at a regular meeting thereof held on the 19th day of January 2016.

AYES: Henry, Schneider, Smallman, St. Germain
NOES: none
ABSENT: Schaller


Lois Henry, President

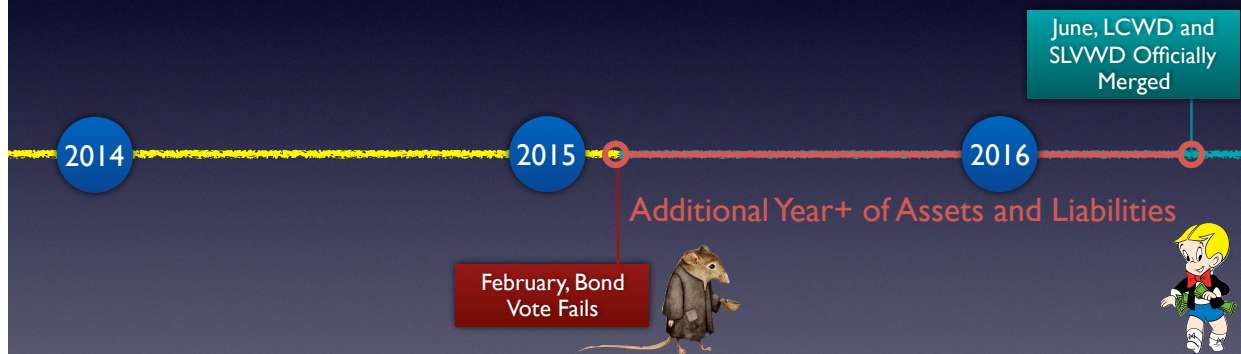
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Abbreviated History of LCWD/SLVWD Merger



Lompico Surcharge.key - October 20, 2016

Abbreviated History of LCWD/SLVWD Merger



Lompico Surcharge.key - October 20, 2016

The clear language contained in the agreement has been reviewed publicly at least six times.

From the Agreement:

... in order to cover the difference between SLVWD's **estimated** revenues collected in Lompico and SLVWD's **estimated** operating costs in Lompico...

LAFCO's Explanation:

... The charge would avoid a situation where the SLVWD customers in its other service areas are subsidizing the Lompico operating costs...

Lompico Surcharge.key - October 20, 2016

Additional Year of Assets and Liabilities

15-16 Assets

- "Ready-to-Serve" Charge of \$50 /month per connection increased bank account and allowed payment of outstanding debt.
- ???

15-16 Liabilities

- Yearly auditor services for 14-15 & partial audit for 15-16
- Merger legal fees
- Merger engineering fees
- Worker's Comp Premiums
- River crossing replacement
- Fire hydrant replacement
- ???

Lompico Surcharge.key - October 20, 2016

Will of the Board?

The District Manager's job is to carry out the will of the Board.

- In May of 2014 when the merger agreement was approved, the will of the SLVWD Board was to move the merger forward **at no cost** to then current District ratepayers.
- In August of 2015 the will of the SLVWD Board was to move the merger forward **at no cost** to then current District ratepayers.
- In January 2016 the will of the Lompico Board was to collect the full Lompico Surcharge, as agreed to, ensuring **no cost** to then current SLVWD ratepayers..

Lompico Surcharge.key - October 20, 2016

Options?

- Revert back to the clear language of the agreement. Override staff's decision to expand committee oversight beyond Bond expenditures.
- Take no action. Surcharge remains 'as-is'. Agreement remains unchanged.
- Commit to renegotiate the terms of the agreement.
- Commit to review surcharge.

Lompico Surcharge.key - October 20, 2016

Staff's Recommendation... Again

- Complete audit to determine what Lompico brought to the table, both assets and liabilities, as of June 1, 2016 (16 months after Lompico's failed bond vote).
- Conduct a review of Lompico Service Area overhead (above normal costs) between June 1, 2016 and current.
- If warranted, modify conditions of the agreement and adjust surcharge at that time.

Audit is scheduled to be complete ~ February 2017