Date of Hearing: April 27, 2022

ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT
Cecilia Aguiar-Curry, Chair
AB 1765 (Nazarian) – As Amended April 18, 2022

SUBJECT: Marks-Roos Local Bond Pooling Act of 1985: rate reduction bonds: review.

SUMMARY: Specifies the California Pollution Control Financing Authority (CPCFA) may charge additional fees to retain an independent financial advisor to review applications for rate reduction bonds (RRBs). Specifically, **this bill**:

1) Specifies that the CPCFA may charge additional fees in an amount equal to the amount of any additional expenses incurred by CPCFA in retaining an independent financial advisor to review the application under circumstances involving the verification of all requirements, as specified.

2) Provides that any fees for review and processing of the application shall be nonrefundable.

EXISTING LAW:

1) Authorizes, under the Joint Exercise of Powers Act (Joint Powers Act), two or more public agencies (i.e. federal government, any state, any state department or agency, county, county board of education, county superintendent of schools, city, public corporation, public district, and regional transportation commission in any state) to enter into a joint powers agreement to exercise jointly any power common to the contracting agencies that each can do by itself.

2) Authorizes joint powers authorities (JPAs) to issue tax-exempt bonds for a variety of purposes.

3) Authorizes JPAs to issue RRBs for local publicly owned water and electric utilities to finance projects necessary to comply with water quality, water conservation, or water reclamation mandates, as specified.

4) Regulates publicly owned utility (POU) activities and rates at the local level, through locally elected boards and/or city councils.

5) Defines, pursuant to Section 224.3 of the Public Utilities Code "local publicly owned electric utility" to mean a municipality or municipal corporation operating as a "public utility" furnishing electric service as provided in Section 10001, a municipal utility district furnishing electric service formed pursuant to Division 6 (commencing with Section 11501), a public utility district furnishing electric services formed pursuant to the Public Utility District Act set forth in Division 7 (commencing with Section 15501), an irrigation district furnishing electric services formed pursuant to the Irrigation District Law set forth in Division 11 (commencing with Section 20500) of the Water Code, or a JPA that includes one or more of these agencies and that owns generation or transmission facilities, or furnishes electric services over its own or its member's electric distribution system.

FISCAL EFFECT: This bill is keyed fiscal.

COMMENTS:

1) **Bill Summary and Author's Statement.** This bill specifies that CPCFA may charge additional fees to retain an independent financial advisor to review applications for rate reduction bonds. This bill is sponsored by the author.

   According to the author, "AB 1765 provides technical changes to last year's AB 758. Simply, AB 1765 will allow for the California Pollution Control Financing Authority to charge the appropriate fees to outside financial experts, when assisting with and reviewing rate reductions bonds."

2) **Background**. California's Joint Powers Act authorizes the joint exercise of powers by federal, state, and local public agencies that jointly perform functions that each entity may perform on its own. This structure allows multiple agencies to collaborate on addressing public needs, such as financing public infrastructure, forming insurance pools, and enhancing planning and regulation. A joint exercise of powers can be limited to a joint powers agreement (akin to a contract) among participating agencies. It can also include the creation of a new, separate entity that administers the joint powers agreement. These are variously called joint powers agencies or JPAs.

   POU activities and rates are regulated by locally elected boards and/or city councils. POUs are subject to the Ralph M. Brown Act, the Public Records Act, and competitive bid requirements.

3) **Rate Reduction Bonds**. RRBs are asset-backed securities that are structured to minimize borrowing costs by qualifying for AAA credit ratings, which allow borrowing at an interest rate that is well below the rate that would otherwise apply to a utility's long-term debt. To qualify for a AAA rating, RRB financing typically includes:

   a) Statutory authority to impose a dedicated charge on utility customers to repay the bonds.

   b) A requirement that the bonds must be issued, and the dedicated charge must be imposed, by a "bankruptcy-remote special purpose entity."

   c) A "true-up" mechanism that allows the dedicated charge to be regularly adjusted to ensure that the bonds are paid off at the final maturity date.

   d) A pledge made by the state not to impair the right to collect the dedicated charge until the bonds are paid in full.

   RRBs were introduced in response to electricity market deregulation in the 1990s to allow investor-owned utilities (IOUs) in deregulated markets to recover so-called "stranded" costs of investments the utilities made before deregulation. California's IOUs used RRBs when the state restructured its energy industry. In that instance, the California Infrastructure and Development Bank (I-Bank) formed a trust that issued the bonds on behalf of the IOUs.

4) **AB 850 of 2013 – RRBs for California's POUs**. California's POUs were first authorized to use RRBs by AB 850 (Nazarian), Chapter 636, Statutes of 2013. This enabling legislation

allowed JPAs to issue RRBs to finance specified projects for specified POUs. The bill included the following parameters:

a) Types of POUs were limited to POUs that provide water service.

b) Size of POUs was limited to POUs that have at least 25,000 retail customers.

c) Types of projects were limited to infrastructure projects for conservation or reclamation purposes, or projects necessary to respond to or comply with a water quality mandate (such as a mandate under the Safe Drinking Water Act).

Bond proceeds were allowed to fund projects that reduce the amount of potable water supplied by the utility or reduce the amount of water imported by the utility. This included projects for storm water capture and treatment, water recycling, development of local groundwater resources, groundwater recharging, and water reclamation.

Los Angeles Department Water & Power (LADWP) sought this financing structure because it qualifies for a higher bond-rating (AAA) than other types of financing available to the utility, reducing interest rates and financing costs and, ultimately, rates for its customers. At the time, LADWP estimated that ratepayers would save as much as $3 million per year for each $100 million of financing under the provisions of AB 850. In the case of LADWP, with its planned spending for water quality and local water supply projects, rates were projected to be 2-4% lower during the course of the ensuing five years than they would have been absent the financing approach allowed by AB 850.

5) **Role of the California Pollution Control Financing Authority (CPCFA)**. The CPCFA is housed in the State Treasurer's office, and provides low-cost financing for projects that control pollution. It also assists with clean-up of contaminated sites. Among other activities, CPCFA assists the California Alternative Energy and Advanced Transportation Financing Authority, which provides financing for facilities needed to develop and commercialize advanced transportation and alternative energy technologies that reduce air pollution, conserve energy, and promote economic development and jobs.

   Amendments to AB 850 adopted in the Senate required CPCFA to review each issue of bonds and determine whether the issue is qualified for issuance under the bill's provisions, "in order to allow the state to review the issuance of RRBs, collect data, ensure transparency, and conduct an independent analysis of the effectiveness of the use of RRBs." It also required CPCFA to report annually to the Legislature on its activities related to the bill.

6) **AB 305 of 2019**. Although enacted in 2013, the authority to issue RRBs had not yet been exercised when AB 305 (Nazarian), Chapter 225, Statutes of 2019, was introduced to address challenges LADWP had encountered in using the financing mechanism. According to LADWP, the utility had formed a JPA in October of 2016, completed stakeholder and city review and approvals, and engaged in extensive interaction with CPCFA. LADWP made substantial progress toward issuing RRBs in 2017, including production of near final documents and opinions which involved extensive feedback on the rating agency requirements. Unfortunately, work on the issuance of the RRBs stopped as the result of problems with the implementation of a new billing system at LADWP, which prevented the

utility from meeting rating agency requirements for the direct billing and collection of the utility project charge.

AB 305 contained changes to the RRB statutes that LADWP reported were necessary as a result of rating agency requirements raised in connection with the attempt to issue RRBs in 2017, clarifications the RRB working group realized were needed resulting from LADWP's efforts to implement a RRB program, or the result of LADWP's interactions with CPCFA. AB 305 made a number of changes to the authorization to issue RRBs, including the following:

a) Expanded the types of POUs allowed to form JPAs and issue RRBs to include those that provide wastewater service.

b) Expanded the types of projects that may be financed to include projects that facilitate the use of wastewater by a POU for conservation purposes, and wastewater recycling.

c) Allowed RRBs to be used to refinance projects.

d) Altered the determinations a POU with 500,000 or more retail customers must make as a condition of applying for RRB financing.

e) Required CPCFA to determine that an issue of RRBs is qualified for issuance solely on the basis of submitted documentation, and prohibited the determination from being conditional in any respect, including conditional on the submission or review of additional material after the determination.

f) Eliminated CPCFA review of the issuance of RRBs if the determinations of the local agency that must be made before the agency can apply for RRB financing are subject to review by a ratepayer advocate or similar entity whose function is to provide public independent analysis of a public utility's actions as they relate to water or wastewater rates.

g) Made a number of additional changes to the RRB statutes.

h) Extended the sunset date until December 31, 2026.

7) **AB 785 of 2021**. AB 758 (Nazarian), Chapter 233, Statutes of 2021 made additional changes to the authorization of RRBs. Specifically, the bill:

a) Expanded the types of POUs that can use RRBs to include POUs that provide electric service. The measure further expanded the types of projects that RRBs can finance to include projects:

   i) Used in connection with future operations of a POU.

   ii) For the provision of generation, transmission, or distribution of electrical service.

   iii) For any other utility purpose designated a "utility project" by a POU.

b) Clarified that CPCFA must submit its report to the Legislature to relevant policy committees with jurisdiction over energy and public utilities.

c) Extended the sunset date for the authorization to issue RRBs from December 31, 2026, to December 31, 2036.

Despite these additional changes, according to CPCFA's annual reports, no one has ever submitted an application for review. Every year the report indicates that CPCFA anticipates receiving an application, but that appears not to have materialized.

8) **Arguments in Support.** According to California State Treasurer Fiona Ma, "This legislation will ensure that CPCFA has the tools and expertise to verify these rate reduction bonds as required by AB 758 (Nazarian) (Chaptered: 2021). AB 758 requires CPCFA to determine if the issue is qualified for issuance under Government Code Section 6588.7. In order to make this determination, CPCFA would be required to review, analyze, and engage an independent consultant. CPCFA and the State Treasurer's Office do not maintain legal or financial personnel with the specific expertise required to meet and fulfill the requirements, nor do industry standards have universally accepted protocols for an issuer or state agency to provide such a determination.

   "Despite CPCFA's long history of successful conduit issuances of tax-exempt bonds for solid waste disposal, water furnishing, and sewage treatment facilities, CPCFA's experience is also that of the issuer. Like all prudent issuers of securities, CPCFA seeks to obtain the specific direction needed to engage with subject matter experts to fulfill its responsibility under existing law. Equally important, CPCFA must be assured that the financial resources necessary to discharge its duties are clearly authorized and disclosed."

9) **Arguments in Opposition.** None on file.

REGISTERED SUPPORT / OPPOSITION:

Support

California State Treasurer Fiona Ma.

Opposition

None on file

Analysis Prepared by: Jimmy MacDonald / L. GOV. / (916) 319-3958