

RatingsDirect®

Summary:

**Oxnard Financing Authority,
California**

Oxnard; Joint Criteria; Water/Sewer

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Credit Profile

Oxnard Fincg Auth, California

Oxnard, California

Oxnard Fincg Auth (Oxnard) wastewtr (AGM)

Unenhanced Rating BBB(SPUR)/Watch Neg On CreditWatch Negative

Oxnard Fincg Auth wastewtr VRDB (Headworks & Septic Sys Projs) ser 2004B

Unenhanced Rating BBB(SPUR)/Watch Neg On CreditWatch Negative

Long Term Rating A+/A-1 Affirmed

Oxnard Fincg Auth wastewtr (Headworks)

Unenhanced Rating BBB(SPUR)/Watch Neg On CreditWatch Negative

Many issues are enhanced by bond insurance.

Rationale

S&P Global Ratings placed on CreditWatch with negative implications its 'BBB' long-term rating and underlying rating (SPUR) on the City of Oxnard Financing Authority, Calif.'s fixed-rate wastewater revenue bonds. At the same time, we affirmed the 'A+' long-term component of our dual rating on the authority's series 2004B variable-rate demand wastewater revenue bonds (A+/A-1). All debt was issued for the City of Oxnard. The 'A-1' short-term component of the dual rating remains unchanged.

We have placed the ratings on CreditWatch with negative implications based on significant financial stress that the wastewater system could experience during the next 90 days depending on specific near-term decisions to be made by the city council, the judicial system, and two financial counterparties.

The wastewater system's financial performance during the past seven fiscal years has been predominantly insufficient, and in our opinion, a recently approved ballot measure repealing a substantial service rate increase is a significant setback to the city's actions to stabilize the system. Through the California voter initiative process, a candidate for city council gathered a sufficient number of signatures to qualify a measure (Measure M) for the November 2016 ballot. We understand that the city filed a complaint for declaratory relief (City of Oxnard v. Aaron Starr) that challenged the legality of using the initiative process to reduce service rates to a level that would impair contractual obligations, including obligations to bond holders, but the judge presiding over the case deferred making a ruling pending the outcome of the election.

Measure M posed the question to the electorate whether the city's wastewater rates that were adopted in January 2016 should be repealed. The first rate increase of the adopted multiyear rate schedule was a 35% rate increase effective

March 2016, with additional rate adjustments of 10%, 8%, 8%, and 8% approved for the subsequent four fiscal years, respectively. The multiyear schedule was based on a cost-of-service study that was completed by an external consultant and was designed to restore the system's financial capacity. In our opinion, the wastewater system's financial performance during the past seven fiscal years was insufficient in five fiscal years and adequate in the remaining two fiscal years. Measure M was approved by a vote of 72% (24,723 votes) in favor of repealing the city's wastewater rates.

We believe that the wastewater system's credit profile could materially degrade during the next 90 days depending on a few key upcoming decisions. In our opinion, the first--and most critical upcoming decisions--are anticipated to occur on Nov. 29, 2016, when the city council is scheduled to meet and consider several possible actions in response to Measure M. The actions that the city council may consider at this meeting include, but are not limited to, requesting a stay of the implementation of Measure M, halting nonessential services and capital projects, borrowing cash from other city funds to provide funds for the wastewater system to make a portion of its June 1, 2017, debt service payment, and initiating a new rate setting process with new service rates likely to be effective in early fiscal year 2018. We understand that the city council could choose to not request a stay and not proceed with the litigation based on the level of support from the electorate for Measure M; however, this is not a course of action that we expect will be recommended by the city administration. We also understand that Measure M does not impair or restrict the city's future rate setting authority and that new service rates may be set as long as the city complies with the substantive and procedural requirements of Proposition 218 as it normally does.

If the city requests a stay of Measure M, the next decision will be for the courts to decide whether to grant the stay in a timely manner prior to the implementation date. The city expects the certification of the election to occur on Dec. 6, 2016, and the implementation will occur 10 days after the certification. The city, with assistance from its financial advisor, has produced a cash flow projection indicating that the wastewater system's liquidity position could be reduced to \$0 by the end of fiscal year 2017 if Measure M is implemented. Based on draft financial data provided by the city, we understand that the wastewater fund held about \$5.9 million of unrestricted cash and investments at the end of fiscal year 2016.

There are also two decisions to be made by financial counterparties that could result in significant draws on the wastewater system's cash reserves. Union Bank provides a direct-pay letter of credit (LOC) that supports the authority's series 2004B variable-rate demand wastewater revenue bonds, and this LOC is scheduled to expire on Feb. 28, 2017. We understand that Union Bank is not likely to extend the expiration date of the LOC if the city does not request a stay and continue pursuing the existing litigation. If the LOC is not extended or a substitute credit facility is not procured prior to the LOC expiration date, then the trustee will issue a mandatory tender for the series 2004B bonds with a current existing par amount of \$16.75 million. The mandatory tender will be funded by a draw on the LOC, and the series 2004B bonds--then bank bonds--would be immediately due and payable. We understand that the city is not currently considering a fixed-rate refunding of the series 2004B bonds. We also understand that degradation in the wastewater system's credit profile--as determined by a rating lower than 'BBB' by S&P Global Ratings--would trigger a termination event for an interest rate swap with RBC. The mark-to-market value of the swap as of Nov. 16, 2016, was negative \$3,752,925. We understand that RBC is not likely to waive the termination event if the city council does not pursue a stay. It is not clear at this time what actions Union Bank and RBC will take if the city requests a stay,

but it is not granted by the courts prior to the implementation of Measure M.

We anticipate resolving our CreditWatch following the city council's decision on Nov. 29, 2016, and, if applicable, the court's decision whether to grant a stay. We will likely take a negative rating action if, in our opinion, these decisions are likely to result in a significant reduction in the wastewater system's liquidity position or otherwise compromise the wastewater system's financial condition. We could remove the rating from CreditWatch if the decisions are likely to stabilize the wastewater system's financial condition and materially reduce the likelihood of any substantial draws on the wastewater system's liquidity in the near term.

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