

TOWN OF STERLINGTON



INVESTIGATIVE AUDIT
ISSUED NOVEMBER 14, 2019

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LOUISIANA LEGISLATIVE AUDITOR
DARYL G. PURPERA, CPA, CFE

November 14, 2019

**THE HONORABLE CAESAR VELASQUEZ, MAYOR,
AND THE BOARD OF ALDERMEN**
Sterlington, Louisiana

We are providing this report for your information and use. This investigative audit was performed in accordance with Louisiana Revised Statutes 24:513, *et seq.* to determine the validity of complaints we received.

We found that a municipal advisor hired by the Town to prepare financial projections to obtain debt used information that, in some instances, overstated actual revenues and understated actual expenditures when compared to audited financial reports and/or records that were available at the time. The projections were submitted to the State Bond Commission as supporting documentation for the Town's request to issue bonds and to the financial institutions that purchased the bonds.

In addition, Sterlington's mayor directed \$3.1 million in bond proceeds be spent on items inconsistent with the stated purpose of the bond between January 2016 and September 2018. State law requires bond proceeds to be used exclusively for the purpose for which the bonds are authorized.

The Town also entered into two lease purchase agreements – one for lighting for the sports complex and one for a water management system – that were not publicly bid, as required by state law. We found as well that the Town spent some of the loan proceeds from the water management lease purchase on items not covered in the price quote. The Town does not have sufficient funds to finish the water management system and will not be able to generate the additional revenue needed to pay the amount due on the lease purchase.

The procedures we performed primarily consisted of making inquiries and examining selected financial records and other documents and were not an examination or review in accordance with generally accepted auditing or attestation standards. Consequently, we provide no opinion, attestation, or other form of assurance with respect to the information upon which our work was based.

The accompanying report presents our findings and recommendations as well as management's response. This is a public report. Copies of this report have been delivered to the

The Honorable Caesar Velasquez, Mayor,
And the Board of Aldermen
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District Attorney for the 4th Judicial District of Louisiana, the United States Attorney for the
Middle District of Louisiana, and others as required by law.

Respectfully submitted,



Daryl G. Purpera, CPA, CFE
Legislative Auditor

DGP/aa

TOWNOFSTERLINGTON

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EXECUTIVE SUMMARY

Incorrect Financial Information Used to Obtain Bonds

The Town of Sterlington (Town) engaged a municipal advisor to prepare financial projections that were submitted to the Louisiana State Bond Commission when the Town was seeking approval to incur bonded debt. These projections were also provided to financial institutions that purchased the bonds and were based on information that, in some cases, overstated actual revenue and understated actual expenditures when compared to audited financial reports and/or Town records that were available when the projections were made. If the municipal advisor knowingly submitted financial projections based on incorrect financial information to the State Bond Commission and financial institutions, the municipal advisor may have violated state and federal law.

Improper Use of Bond Proceeds

At Mayor Vern Breland's direction, the Town spent \$3,118,103 from bond proceeds that were inconsistent with the stated purpose of the bond between January 4, 2016 and September 10, 2018. State law provides that proceeds from the sale of bonds be used exclusively for the purpose for which the bonds are authorized to be issued. By continuing to direct the improper use of the bond proceeds after receiving a finding in the Town's 2016 annual audit, Mayor Breland may have violated state law.

Lease Purchases Were Not Publicly Bid

The Town had two lease purchase agreements for Sterlington Sports Complex lighting and a water management system that were not publicly bid, which may violate state law. In addition, the Town spent some of the loan proceeds from the water management lease purchase on items that were not covered in the price quote. Since the Town does not have sufficient funds to complete the water management system that was financed by the lease purchase, the Town will not generate the additional revenue to pay the amount due on the lease purchase.

BACKGROUND AND METHODOLOGY

The Town of Sterlington (Town) is located in Ouachita Parish and has a population of 1,594 (2010 Census). The Town was incorporated under the Lawrason Act and has a mayor-board of alderman form of government. The Town’s mayor and five aldermen are elected at-large and serve four-year terms. The town provides utility, public safety (police), street maintenance, and general administrative services. During the period covered in this report, Mr. Vern Breland was Mayor of Sterlington.

The Town – which had \$3,010,746 in annual revenues (unaudited) in 2018 and averaged \$2,112,488 in annual revenues from 2011 to 2017 – incurred \$18,201,000^A in bonded debt obligations and \$2,904,000 in lease purchase obligations from 2011 through 2018, largely due to the construction of a sports complex and utility improvements. The Town operated at a net loss (i.e., the Town’s operating expenses exceeded total revenue) in 2013, 2015, 2016, and 2017, when these debt obligations were incurred. The Town was placed under fiscal administration by the 4th Judicial District Court for the Parish of Ouachita on August 6, 2019, as it was unable to pay the debt obligations coming due. The following table shows the Town’s outstanding debt^B as of August 28, 2019.

Issuance Year	Bond Amount and Title/Purpose	Maturity Date	Principal Balance as of August 28, 2019
2011	\$696,000 - Sewer Revenue Bonds, Series 2011	June 1, 2031	\$443,585
2013	\$350,000 - Taxable Sales Tax Bonds, Series 2013	December 1, 2033	256,717
2013	\$2,710,000 - Revenue Refunding Bonds, Series 2013	June 1, 2028	2,111,000
2014	\$600,000 - Wastewater and Utilities Revenue Bonds, Series 2014	September 1, 2034	490,143
2015	\$1,700,000 Revenue Bonds - \$1,200,000 - Wastewater and Sewer Treatment Utilities Revenue Bonds \$500,000 - Water Treatment and Utilities Revenue Bonds ^C	September 1, 2018	0

^A This does not include the 2015 Utility Revenue Bonds for \$1,700,000, which the Town refinanced in 2018 for \$1,845,000.

^B The Town also has two lease purchase agreements for an additional \$2,904,000: one for a lease purchase for lighting at the Sterlington Sports Complex (\$840,000) and one for a water management system (\$2,064,000). The Town did not obtain State Bond Commission (SBC) approval for the two lease purchase agreements since both agreements contain non-appropriation clauses, and La. R.S. 39:1410.60(C)(1) does not require SBC approval for leases or install purchase agreements.

^C These two 2015 Revenue bonds (\$500,000 and \$1,200,000) were refinanced in 2018 as the \$1,845,000 Wastewater, Water and Sewer Treatment Utilities Revenue Bonds.

Issuance Year	Bond Amount and Title/Purpose	Maturity Date	Principal Balance as of August 28, 2019
2016	\$2,000,000 Revenue Bonds- \$500,000 Revenue Bonds, Series 2016A (Tax Exempt); \$1,000,000 Taxable Revenue Bonds, Series 2016B; \$500,000 Taxable Revenue Bonds, Series 2106C (LPFA Program)	A: June 1, 2036 B&C: June 1, 2026	\$1,790,000
2017	\$4,000,000 - Revenue Bonds, Series 2017	December 1, 2036	3,850,000
2017	\$4,000,000 Utility Revenue Bonds - \$3,500,000 Utility Revenue Bonds, Series 2017A (Tax Exempt); \$500,000 Taxable Utility Revenue Bonds, Series 2017B (LPFA Program)	A: December 1, 2036 B: December 1, 2026	3,950,000
2018	\$2,000,000 - Sports Complex Concessions Facility and Parking Facility Bonds	April 21, 2021	1,980,000
2018	\$1,845,000 - Wastewater, Water and Sewer Treatment Utilities Revenue Bonds, Series 2018	December 31, 2038	1,845,000
	Total Outstanding Bond Obligations as of August 28, 2019		\$16,716,445

We received complaints that the Town of Sterlington spent bond proceeds for unauthorized purposes. This audit was initiated to determine the validity of those complaints. The procedures performed during this audit included:

- (1) interviewing Town employees and other persons, as appropriate;
- (2) examining selected Town documents and records;
- (3) gathering and examining external parties' documents and records; and
- (4) reviewing applicable state laws and regulations.

FINDINGS AND RECOMMENDATIONS

Incorrect Financial Information Used to Obtain Bonds

The Town of Sterlington (Town) engaged a municipal advisor to prepare financial projections that were submitted to the Louisiana State Bond Commission (SBC) when the Town was seeking approval to incur bonded debt. These projections were also provided to financial institutions that purchased the bonds and were based on information that, in some cases, overstated actual revenue and understated actual expenditures when compared to audited financial reports and/or Town records that were available when the projections were made. If the municipal advisor knowingly submitted financial projections based on incorrect financial information to the SBC and financial institutions, the municipal advisor may have violated state¹ and federal law.²

The state Constitution³ and state law⁴ requires political subdivisions, such as the Town, to obtain the SBC's written approval before issuing or selling bonds or other obligations. The Background and Methodology section of this report, at pages 3-4, sets forth 10 bonds^D the Town issued between 2011 and 2018. As of August 28, 2019, these bonds had an outstanding balance of \$16,716,445.

According to the applications the Town submitted to the SBC, bond proceeds were to be used for utility (sewer and water) projects and a sports complex, as well as for refunding prior bonds. To obtain SBC approval, the Town Engineer estimated the projects' cost. Those estimates were used to determine the amount the Town should borrow. The Town's bond counsel and municipal advisor used that information to prepare documentation to submit to the SBC.

Mr. Aaron Fletcher served as the Town's municipal advisor on eight bonds and as a financial advisor on two lease purchases from 2013 to 2018. Mr. Fletcher was the Town's municipal advisor while working for different brokers from 2013 to 2015.^E As municipal advisor, Mr. Fletcher assisted the Town in placing seven of the 10^F bonds with banks after obtaining SBC approval.

^D The Town also has two lease purchase agreements for an additional \$2,904,000: one for a lease purchase for lighting at the Sterlington Sports Complex (\$840,000) and one for a water management system (\$2,064,000). The Town did not obtain SBC approval for the two lease purchase agreements since both agreements contain non-appropriation clauses, and La. R.S. 39:1410.60(C)(1) does not require SBC approval for leases or installment purchase agreements.

^E According to the Financial Industry Regulatory Authority (FINRA), Mr. Fletcher worked for brokerage firms M. R. Beal & Company from April 9, 2013 to January 1, 2014; and Sterne Agee & Leach from January 24, 2014 to April 30, 2015, during which time he was Sterlington's municipal advisor. Mr. Fletcher's employers were paid the municipal advisor fees when Mr. Fletcher was employed by them. He also served as a Managing Director of OPHDE Advisors, LLC.

^F Mr. Fletcher worked on the 2013 \$2,710,000 Revenue Refunding Bonds and all subsequent Town bonds through M.R. Beal & Company, Sterne, Agee & Leach, and Twin Spires, LLC. This bond is the only open market bond Mr. Fletcher worked on for the Town; all the rest were private placement with banks.

Twin Spires Financial, LLC

In 2015, Mr. Fletcher started Twin Spires Financial, LLC (Twin Spires),^{G,H} through which he served primarily as Sterlington's municipal advisor. The Town paid Twin Spires \$209,119 between 2015 and 2018. As Sterlington's municipal advisor, Mr. Fletcher prepared the financial projections the Town submitted to the SBC.

In March 2018, Twin Spires contracted with the Town to become the Town's cash management officer. The contract required Mr. Fletcher to travel "to Sterlington every four to six weeks to review collections, expenditures, and make recommendations to deposits into debt service funds, debt service reserve funds, operation accounts and maintenance/repair accounts." Twin Spires was to be paid \$2,000 per month for these services.

We reviewed the financial projections and other records submitted to the SBC for the three most recent bonds:

- (1) \$4,000,000 Utility Revenue Bonds, \$3,500,000 Series 2017A (Tax Exempt); \$500,000 Taxable Utility Revenue Bonds, Series 2017B (LPFA Program) (2017):
- (2) \$2,000,000 Sports Complex Concessions Facility and Parking Facility Bonds (2018): and
- (3) \$1,845,000 Wastewater, Water and Sewer Treatment Utilities Revenue Bonds (2018).

Using information available at the time of Twin Spires' projections for Bond No. 1 and No. 3, such as audited financial statements and Town billing records, we compared our results to the Twin Spires' projections for revenues and expenses. The results are presented in the tables on the next page. We used the Town's unaudited financial statements for 2018, which were not available at the time of Twin Spires' projection, to estimate revenues and expenses for Bond No. 2 since the Sports Complex started operations in 2018 and there was no other data available.

^G On July 6, 2015, Twin Spires Financial, LLC, a Texas limited liability company domiciled in Frisco, Texas, was formed. Mr. Fletcher is Twin Spires' managing member and registered agent.

^H Mr. Fletcher's broker dealer's license was held by First Kentucky Securities from July 23, 2015 until July 31, 2018.

Bond # 1						
\$4,000,000 Utility Revenue Bonds - \$3,500,000 Utility Revenue Bonds, Series 2017A (Tax Exempt); \$500,000 Taxable Utility Revenue Bonds, Series 2017B (LPFA Program)						
	Revenues			Expenses		
	Twin Spires	LLA	Difference	Twin Spires	LLA	Difference
Sewer System	\$33,719,766	\$19,142,693	\$14,577,073	\$3,786,204	\$4,673,479	(\$887,275)
Water System	16,644,337	17,109,481	(465,144)	1,197,300	8,495,310	(7,298,010)
Totals	\$50,364,103	\$36,252,174	\$14,111,929	\$4,983,504	\$13,168,789	(\$8,185,285)

Bond # 2						
\$2,000,000 - Sports Complex Concessions Facility and Parking Facility Bonds						
	Revenues			Expenses		
	Twin Spires	LLA	Difference	Twin Spires	LLA	Difference
Sports Park	\$1,794,503	\$1,015,428	\$779,075	\$1,054,638	\$835,817	\$218,821

Bond # 3						
\$1,845,000 – Wastewater, Water and Sewer Treatment Utilities Revenue Bonds, Series 2018						
	Revenues			Expenses		
	Twin Spires	LLA	Difference	Twin Spires	LLA	Difference
Sewer System	\$35,108,297	\$20,602,246	\$14,506,051	\$11,841,714	\$11,760,295	\$81,419
Water System	5,831,414	No Data Available	N/A	1,965,848	No Data Available	N/A
Totals	\$40,939,711		N/A	\$13,807,562		N/A

Debt Service Coverage Ratio			
	Bond # 1	Bond # 2	Bond # 3
Twin Spires	1.02	1.06	1.11
LLA	0.72	0.26	0.49
Difference	0.30	0.80	0.62

- **Bond No. 1** – Twin Spires’ estimate for net income is \$22,297,214¹ higher than our projection over the life of the bond.
- **Bond No. 2** – Twin Spires’ estimate for net income is \$560,254^J higher than our projection over the life of the bond.

¹ Calculated as Twin Spires vs. LLA difference in sewer/water revenues \$14,111,929 less the sewer/water expense differences of (\$8,185,285) or \$22,297,214

^J Twin Spires versus LLA difference in revenues and expenses (\$779,075 to \$218,821) or \$560,254.

- **Bond No. 3** – Twin Spires’ estimate for sewer revenues is \$14,424,632^K higher than our projection over the life of this bond. We were unable to determine how Twin Spires calculated water revenue/expense; therefore, that difference is unknown.

Bond No. 1
\$4,000,000 Utility Revenue Bonds, \$3,500,000 Series 2017A
(Tax Exempt); \$500,000 Taxable Utility Revenue Bonds, Series
2017B (LPFA Program) (2017)

- Amount SBC Approved to Borrow: \$4,500,000
- Amount Borrowed: \$4,000,000 Bonds
- Loan Origination Date: April 27, 2017
- Purpose: Utility Improvements and Maintenance
- Security: Utility Revenues
- Maturity Dates: December 1, 2036 (A); December 1, 2026 (B)

On February 16, 2017, the SBC authorized the Town to borrow up to \$4,500,000 with a maturity not to exceed 30 years. The Town’s ordinance, passed April 11, 2017, approved the bonds to be used for “constructing and acquiring utility improvements, extensions and replacements to the System, including utility improvements to the Issuer’s new sports complex and other municipally owned projects, including appurtenant equipment, accessories, replacements and additions to such works of public improvement for the Issuer...” The SBC approval describes the security for the debt as the revenues of the water system and the sewer system. The SBC’s analysis also shows the Town’s sewer system revenue was already pledged to four of the Town’s outstanding bonds.

The Town issued \$4,000,000 of utility revenue bonds (Series A and B) on April 27, 2017. Twin Spires was the Town’s municipal advisor. Twin Spires prepared a financial projection that estimated revenues and operating expenses for the Town’s sewer system and the Town’s proposed surface water treatment plant. The Town operates its own sewer system, but has not operated a water system or owned water treatment facilities since 1965.

The Town’s engineer told us the Town received a government grant in the 1950s to install water lines to residents of the Town. A Town engineer report states that the Town has not produced its own source of potable water since 1965. In 1965, the Sterlington Water Company donated the water distribution system it owned and operated to the Greater Ouachita Water Company (GOWC). The GOWC and the Town entered into a franchise agreement for GOWC to use the water lines to provide water to Town residents. The franchise agreement expired in June 2016. The Town and GOWC entered into an Asset Purchase Agreement (APA) in April 2015 for the Town to purchase water lines north of Keystone Road in Sterlington.

^K Twin Spires versus LLA difference in sewer revenues and expenses (\$14,506,051-\$81,419) or \$14,424,632.

The APA required both parties to meet certain conditions before completing the purchase. If the conditions were not met by April 9, 2017, the APA expired by its own terms, which it did. The Town sued GOWC in April 2017, and again in August 2017, to expropriate the water system within the Town's corporate limits. Both cases were dismissed by December 2017. GOWC's President told us that GOWC counted 950 water customers that would have been affected had the Town won the expropriation lawsuit. The Town lost the expropriation lawsuits, and GOWC continues to use the water lines and provide water to Sterlington's residents.

Sewer and Water System Revenue Projections

Twin Spires' financial projection for Bond No. 1 showed sufficient sewer and water system revenues to service this debt. The projection used 2016 as a baseline year for revenue and 2015 as a baseline for expenses. It estimated revenue would grow at 1 to 9% for residential customers and 1.5 to 5% for commercial customers and assumed expenses would grow 2.5% annually during the life of the Bond. Since the projection was submitted to the SBC on January 18, 2017, we compared the Town's December 2016 sewer system customer records and 2015 audited financial statements^L to Twin Spires' financial projection.

The Town's December 2016 sewer system records showed that the Town billed 960 customers. Twin Spires' financial projection shows the Town had 1,574 sewer system customers for 2016, or 614 more than Town records. We discussed this difference with Aaron Fletcher, Twin Spires' managing director. Mr. Fletcher told us he used the GOWC water usage report to arrive at 1,574 sewer system customers. The Town's utility clerk told us she also used the GOWC water usage report to bill the Town's sewer system customers, and that the Town has never had that many sewer system customers.^M

The GOWC water usage report indicates how many gallons of water each customer uses and lists the customer's street address. The Town's utility clerk told us she uses the GOWC water usage report to bill the Town's sewer system customers but does not bill for vacant addresses, inactive accounts with no usage, and addresses where residents used a septic system instead of the Town's sewer system. GOWC's water usage report for December 2016 had a total of 1,425 customer accounts, 149 less than the number Twin Spires used in its financial projection. Furthermore, 561 of the accounts were either inactive accounts with no usage, customer name is "VACANT" or "NO NAME," or addresses where residents used a septic system instead of the Town's sewer system, which left 864 accounts,^N 710 less than the number Twin Spires used.

^L The Town's 2016 audited financial statements were not due until after the financial projection was submitted to the SBC.

^M The Town's utility clerk told us that former Mayor Vern Breland asked her "off and on all the time" about how many sewer system customers the Town had. The utility clerk told us that Mayor Breland and Mr. Fletcher were aware the Town did not have 1,574 sewer system customers.

^N The difference between the Town's records of sewer system customers (960) and the GOWC water usage report (864) is due to the Town's billing practice for apartment complexes.

By basing the financial projection on 1,574 sewer system customers instead of the Town's 960 actual sewer system customers, the financial projection overstates revenue by \$14,577,073 than if the financial projection used the actual number of sewer customers.

Twin Spires' financial projection for the proposed water system shows \$650,000 of revenue in 2019, the first full year of operations. Although the financial projection included how several of the numbers were determined, there was no explanation of how water system revenue was determined. According to the engineer's report submitted with the SBC application, the Town planned to begin operating its own water system in early 2018. We used the estimates and assumptions^O in the engineer's report to calculate the annual revenue of the proposed water system. For 2019, the first scheduled full year of operations, the annual revenues of the water system would be \$661,249, or \$11,249 higher than the estimate by Twin Spires. Over the life of the bond, the Twin Spires' financial projection was \$465,144 less in revenue than if the engineer's estimate was used.

Sewer and Water System Expense Projections

We also reviewed the estimated expenses of Twin Spires' financial projection for the Town's sewer system and proposed water system. Twin Spires' projected 2015 operating expenses for the Town's sewer system to be \$141,077, with an annual growth rate of 2.5%. Since the financial projection was submitted to the SBC in January 18, 2017, we compared the Twin Spires' \$141,077 sewer system annual operating expense to the \$177,923 reported in the 2015 audited financial statements.^P We found Twin Spires' financial projection was \$36,846 less than the actual sewer system operating expenses reported in the Town's audit report. Over the life of the bond, the projected operating expenses are \$887,275 less than if the projections had been made using the actual sewer system expenses.

The financial projection also estimated the Town's proposed water system would have \$51,250 in operating expenses in 2019^Q and assumed a 2.5% increase for each subsequent year. According to the engineer's report submitted with the SBC application, the Town planned to begin operating its own water system in early 2018 and that the annual operating expenses of the water system would be \$354,770, or \$303,520 higher than the amount of estimated by Twin Spires. Over the life of the bond, the Twin Spires' financial projection was \$7,298,009 less in operating expenses than if the engineer's estimate was used.

Debt Service Coverage Ratio

Loan officers at two of the banks holding Sterlington's bonds told us the debt service coverage ratio (DSCR) is a key factor in determining whether or not to fund a loan. The debt service coverage ratio measures whether a potential borrower will have sufficient cash flow

^O To estimate annual revenue, we used the midpoint of the range (\$13.98 to \$21.41 per customer per month) for water rates suggested by the engineer.

^P Expenses for audited financial statements do not include depreciation since depreciation is a non-cash item to be consistent with Twin Spire's financial projection assumptions.

^Q The financial projection included an operating expense of \$50,000 for the water system for 2018, but we used 2019 as the base year since that was the estimate of the first full year of operations.

available to pay current debt obligations. The SBC DSCR ratio uses current net operating income divided by the highest annual debt service for an agency.

Twin Spires' DSCR for this bond was 1.02, which means the Town would be able to make 100% of its debt service payments out of its available funds and have 2% of funds remaining. We performed the same analysis using the audit report and the engineer's report and found the DSCR on Bond No. 1 was 0.72, which means that the Town would have a shortfall of at least 28% and will not have sufficient cash flow to pay its current debt.

Bond No. 2
\$2,000,000 Sports Complex Concessions Facility and Parking
Facility Bonds (2018)

- Amount SBC Approved to Borrow: \$2,000,000
- Amount Borrowed: \$2,000,000
- Loan Origination Date: April 20, 2018
- Purpose: Sports Complex Construction
- Security: Sports Complex Revenues
- Maturity Date: April 20, 2021

On March 15, 2018, SBC authorized the Town to borrow up to \$2,000,000, with a maturity not to exceed 27 years, to construct, acquire, maintain, operate, and equip a concessions facility and parking for the sports complex and to pay costs associated with the installation of lighting and electrical systems at the sports complex. The SBC's approval described the security for the debt as the revenues from the operation of the sports complex, 0.5% sales tax for the sports complex, 0.5% sales tax for road construction and maintenance, and 1.5% sales tax for general town operations. The SBC's analysis showed some of these revenues were previously pledged to outstanding debt from a lease for sports complex lighting.

The Town issued \$2,000,000 of sports complex concessions and parking revenue bonds on April 20, 2018. The financial projection prepared by the Town's municipal advisor, Twin Spires, shows revenue and expense estimates for the Town's sports park for 2018. Since this was the first year the Town operated the sports complex, there were no historical revenues and expenses to compare to the financial projection. As a result, we used Town records and current financial information to compare to the financial projection.

The financial projection estimated the sports complex would generate \$513,750 of revenue in 2018 from concessions, rental fees, and sponsorships. The Town does not charge parking fees. The projected revenue growth rate ranged from 1% to 4% per year until 2035, when the growth rate would be 0%. The Town's unaudited financial records show the sports complex generated only \$290,708^R in revenue during 2018, or \$223,042 less than projected.

^R The Town's financial records show it received \$725,170 from the Monroe-West Monroe Convention and Visitor's Bureau as part of a cooperative endeavor agreement to help construct various components of the sports complex, but

The financial projection also estimated the sports complex would cost \$305,550 to operate in 2018, and that expenses would grow between 1 to 3% annually through 2035. The expense projection included employee wages and concession costs but omitted other expenses, such as utilities, insurance, advertising, and audit fees. The Town's financial records show the sports complex payroll and concession costs were \$77,160, or \$228,390 less than the financial projection. After adding the omitted operating expenses, it cost the Town \$242,153 to operate the sports complex, or \$63,397 less than the projected operating expenses.

Debt Service Coverage Ratio

The Twin Spires financial projection shows the DSCR for this bond was 1.06, which means the Town would be able to make 100% of its debt service payments from available funds and still have 6% left over. We performed the same analysis using unaudited sports complex revenues and expenses for 2018, which were not available to Twin Spires at the time of their projection, and found the DSCR on this bond would be 0.26, which means the Town would have an 84% shortfall and will not have sufficient cash flow to pay its current debt.

Bond No. 3
\$1,845,000 Wastewater, Water and Sewer Treatment Utilities
Revenue Bonds (2018)

- Amount SBC Approved to Borrow: \$1,845,000
- Amount Borrowed: \$1,845,000
- Loan Origination Date: September 28, 2018
- Purpose: Refinance 2015 Utility Revenue Bonds
- Security: Utility Revenues
- Maturity Date: December 1, 2038

On August 16, 2018, the SBC authorized the Town to borrow up to \$1,845,000, with a maturity not to exceed 25 years, to refund the Wastewater and Sewer Treatment Utilities Revenue Bonds and Water Treatment and Utilities Revenue Bonds, Series 2015A and 2015B. The SBC approval describes the security for the debt as the revenues of the wastewater and sewer treatment system and the water treatment system. The SBC's analysis shows the sewer treatment system revenue was already pledged as security for four outstanding bonds.

The Town issued \$1,845,000 of utility revenue bonds on September 28, 2018. Twin Spires' financial projection estimated revenue and operating expenses for the Town's sewer system based on the number of residential and commercial customers. It also estimated revenue and operating expenses for the Town's proposed groundwater treatment plant.

since it was not included in the financial projection, we did not include the cooperative endeavor agreement revenue in our comparison.

Sewer System Projection

Twin Spires' financial projection shows the Town had 1,486 sewer system customers in 2017 and would have 1,940 sewer system customers in 2018. Calendar year 2018 was the baseline for this projection and showed residential growth rates of 1% to 14% annually. Since the financial projection was submitted to the SBC on July 18, 2018, we compared the number of sewer system customers (1,486) in the financial projection to the Town's sewer system billing records (1,031), and found the projection assumed the Town had 455 more sewer system customers than it actually had in 2017.

We compared the 2018 estimate of sewer system customers (1,940) in the financial projection to Town's June 30, 2018, sewer system billing records (1,076), and found the estimate was 864 higher than the actual number of sewer system customers as of June 2018.

By calculating revenue using 1,940 sewer system customers instead of the Town's actual 1,076 sewer system customers, the financial projection overstates projected revenue by \$14,506,051 over the life of the bond.

We asked Mr. Fletcher to explain why he used a higher number of sewer system customers than the Town was billing in his projection. His emailed response stated, "It reflects the actual number of sewer customers the Town of Sterlington was billing on a monthly basis. The data was coming from Greater Ouachita Water Company (GOWC). GOWC was reading the meters and providing Sterlington with monthly usage data. Sterlington then manually prepared 1,400+ invoices which they mailed out for sewer usages as Sterlington manages its own sewer system, the single revenue source to cover all related sewer debt." Mr. Fletcher's response also said that he used the GOWC number of customers in 2016 as his baseline and projected a 3.5% growth for 2017 and 2018, even though the number of 2017 customers was available to him.

As discussed above in Bond No. 1, the Town's utility clerk told us she used the GOWC water usage report to bill the Town's sewer system customers and that the Town never had the number of sewer system customers in the Twin Spires' financial projection. Moreover, the Town's utility clerk furnished us a copy of the Town's sewer system customers for June 2018 and told us that former Mayor Breland asked her "off and on all the time" how many sewer system customers the Town had, and that he and Mr. Fletcher were aware the Town did not have 1,940 sewer system customers as reported in the Twin Spires' financial projection.

We also reviewed the estimated expenses of Twin Spires' financial projection for the Town's sewer system. Twin Spires' projected the 2017 operating expenses for the Town's sewer system to be \$425,000, with an annual growth rate of 2.5%. Since the financial projection was submitted to the SBC in July 18, 2018, we compared the Twin Spires' \$425,000 sewer system annual operating expense to the \$432,630 reported in the 2017 unaudited financial statements.^S We found Twin Spires' financial projection of sewer system expenses was \$7,630 less than the actual sewer system operating expenses reported in the Town's unaudited financial statements.

^S Expenses do not include depreciation as depreciation is a non-cash item to be consistent with Twin Spire's financial projection assumptions.

Over the life of the bond, the projected operating expenses are \$81,419 more than if the projections were made using the actual sewer system expenses.

Water System Projection

The Town's engineer prepared a preliminary engineering report in 2016 for the Town's plans to operate a surface water treatment plant to provide potable water. In December 2017, the Town contracted with Capstone Metering, LLC to provide a water filtration plant to filter ground water instead of the previously planned surface water treatment plant. The Town did not have an engineer's report for the proposed water filtration plant.

We also reviewed Twin Spires' financial projection for the water filtration plant's revenues and expenses. The financial projection shows 2019 would be its first full year of operation and it would generate \$200,000 in revenue. Although the financial projection included how many of the numbers were determined, there was no explanation of how water filtration plant revenue was determined.

The financial projection also estimated operating expenses at \$75,000 for 2019, but there was no explanation of how the estimate was determined. Since the Town does not have a water filtration plant, we could not compare actual expenses to the estimates in the financial projection.

Debt Service Coverage Ratio

The Twin Spires financial projection shows the DSCR for this bond was 1.11, which means the Town would be able to make 100% of its debt service payments from available funds and still have 11% leftover. Since there was no data available to use for the water system, we used the unexplained estimates for the water system that Twin Spires used and our estimates for the sewer system. We performed the same analysis and found the DSCR on this bond would be 0.49, which means the Town would have a 51% shortfall and will not have sufficient cash flow to pay its current debt.

If the municipal advisor knowingly submitted financial projections based on incorrect financial information to the SBC and financial institutions, the municipal advisor may have violated state¹ and federal law.²

Improper Use of Bond Proceeds

At Mayor Breland's direction, the Town spent \$3,118,103 from bond proceeds that were inconsistent with the stated purpose of the bond from January 4, 2016 to September 10, 2018. State law⁵ provides that proceeds from the sale of bonds be used exclusively for the purpose for which the bonds are authorized to be issued. By continuing to direct the improper use the bond proceeds after receiving a finding in the Town's 2016 annual audit, Mayor Breland may have violated state law.⁶

A Town ordinance was passed in conjunction with each bond, defining the bond's purpose and how the proceeds from the bond could be spent. State law⁵ provides that the proceeds from the sale of the bond shall constitute a trust fund to be used exclusively for the purpose for which the bonds are authorized to be issued.

The Town's audited financial statements for the year ended December 31, 2016, included a finding that the Town improperly spent \$322,280 of bond proceeds from two 2015 bonds that were issued for the sewer system and water treatment plant. Mayor Breland responded to the finding on August 29, 2017, stating "After consulting with our Bond Attorney and CPA...the Town plans to have all funds repaid by December 31, 2017." Mayor Breland's response identified the repayment source of funds as current funds and the proceeds derived from the sale of two tracts of surplus real estate.

Town records show that only \$39,800 of the \$322,280 was repaid by December 31, 2017; the remaining \$282,480 was not. We also found an additional \$110,367 of 2015 water treatment plant bond proceeds that were improperly spent. In total, the bond accounts are still owed \$392,847. The 2015 Wastewater and Sewer Treatment Utilities Revenue Bonds and Water Treatment and Utilities Revenue Bonds were refunded in 2018 (Bond No. 3 in first finding). The table below describes the improper spending by period and type of expense.

Improperly Spent Bond Proceeds from 2015 Sewer System and Water Treatment Plant Bonds January 1, 2016 to July 31, 2018				
Expense Category	January 1, 2016 to December 31, 2016	January 1, 2017 to August 29, 2017	August 30, 2017 to July 31, 2018	Total
Payroll	\$151,084	\$53,928		\$205,012
Gas Line Extension	78,802			78,802
Police Cars	65,770			65,770
Legal Fees		44,272		44,272
Audit Fees	19,824		\$8,251	28,075
Survey-Town Hall Land Purchase	6,800			6,800
Other		3,566	350	3,916
Total	\$322,280	\$101,766	\$8,601	\$432,647

We reviewed Town records for the use of the other bond proceeds and found the Town improperly spent \$2,685,456 of 2017 Utility Revenue Bond (Bond No. 1) proceeds between June 16, 2017 and September 10, 2018. An additional \$179,879 was spent prior to management's response to the finding regarding the improper use of bond proceeds, leaving \$2,505,577 spent improperly after Mayor Breland met with the Town's bond counsel and CPA and concluded the funds were improperly spent and the Town would pay back the funds to the bond account. The Town Clerk told us she processed all the bond payments and recorded them in the Town's accounting system as directed by Mayor Breland. A summary of the improper use of the 2017 Utility Revenue Bond proceeds is in the following table.

Improperly Spent Bond Proceeds From 2017 Utility Revenue Bonds, Series 2017A (Tax Eexmpt) and Taxable Utility Revenue Bonds, Series 2017B (LPFA Program) June 16, 2017 to September 10, 2018			
Expense Category	June 16, 2017 to August 29, 2017	August 30, 2017 to September 10, 2018	Total
Sports Complex (fencing, backstops, archways)	\$52,314	\$2,124,192	\$2,176,506
Legal Fees (Expropriation Lawsuit with GOW)	127,565	234,619	362,184
Gas Lines		93,312	93,312
Interest on Other Loan		19,459	19,459
Engineering Fees (Not related to water or sewer system)		17,725	17,725
Financial Consultant Fees		12,170	12,170
Court/Trial costs		4,100	4,100
Total	\$179,879	\$2,505,577	\$2,685,456

Since former Mayor Breland knew that bond proceeds could only be used as specified in the bond ordinance yet continued to direct the bond proceeds to be used on other Town expenses, he may have violated state law.⁶

Lease Purchases Were Not Publicly Bid

The Town had two lease purchase agreements for sports complex lighting and a water management system that were not publicly bid, which may violate state law.⁷ In addition, the Town spent some of the loan proceeds from the water management lease purchase on items that were not covered in the price quote. Since the Town does not have sufficient funds to complete the water management system that was financed by the lease purchase, the Town will not generate the additional revenue to pay the amount due on the lease purchase.

The Town entered into two lease purchase agreements: one to lease purchase a lighting system for the Sterlington Sports Complex on September 27, 2017, and one to lease purchase a water management system on January 16, 2018. Both lease purchase agreements included a non-appropriation clause and, therefore, were not required to be approved by the SBC.^T

^T The SBC director told us she unaware of a municipality using a lease purchase to acquire a water system before hearing of this transaction.

Sports Complex Lighting

Mayor Breland contracted with Musco Lighting for a 10-year lease purchase on September 27, 2017, to buy an \$840,000 lighting system for the Sterlington Sports Complex. There was no labor or installation included in the price; it appears the whole purchase was for the lighting equipment. The Town paid for the installation of the lights using Bond No. 3 in 2018.

In 2017, state law⁷ required purchases greater than \$30,000 of materials and supplies and public works contracts greater than \$152,550 by public entities to be publicly bid; however, the lighting cost was \$840,000, and there was no evidence of a public bid for the lighting lease purchase in the Town's records. The Town Clerk told us she could not remember why this lease purchase was not bid. Town records include a written opinion from the Town attorney that the purchase was in accordance with public bid laws. The Town attorney told us that the Town's bond counsel had reviewed the lease purchase and determined the lighting did not have to be bid. The Town's bond counsel told us he had never seen the lease purchase agreement and did not provide any legal advice on public bid law.

Water Management System

On December 8, 2017, Mayor Breland contracted with Capstone Metering, LLC (Capstone) for a \$2,064,000 water management system. On January 16, 2018, the Town also contracted with Government Capital Corporation for a 14-year lease purchase agreement to fund the purchase of the water management system from Capstone. Government Capital Corporation subsequently sold the lease purchase to Citizen's Bank & Trust of Vivian. Citizen's Bank & Trust of Vivian funded this lease purchase on February 22, 2018.

In 2018, state law⁷ required public works contracts greater than \$154,450 be publicly bid, far less than the water management system's cost of \$2,064,000. We found no evidence of a public bid for the water management system in the Town's records. The Town clerk told us she did not have any records of a public bid for the water management system and that the first time she heard of this transaction was at a Board of Aldermen meeting where a resolution was passed to authorize the Mayor to enter into the contract.

The Town's contract with Capstone called for the installation of 420 water meters and a 300,000 gallon per day freshwater filtration system. Capstone's CEO told us that he added \$300,000 of "contingency" to the price at the request of Mr. Fletcher. The contract specifies four payments of 25%: the first payment upon execution of the lease, the second payment upon delivery of the water treatment plant and installation of 100 meters, the third payment upon finalization of the water treatment plant, and the final payment upon installation of all remaining meters. A representative of Governmental Capital told us there is an escrow agent agreement between the Town, Government Capital, and a bank where the Town submits an approved invoice to Government Capital, then Government Capital authorizes payment from the bank (escrow agent).

Of the \$2,064,000 the Town financed, four disbursements were made totaling \$1,843,565.23: three of the disbursements were to Capstone totaling \$1,651,200 for 375 water

meters, and the fourth disbursement was used to pay \$192,365.23 that was due to Citizen's Bank & Trust of Vivian for the lease purchase agreement.^U The remaining balance in the lease purchase escrow account is approximately \$223,000, which is not enough to complete the water filtration system.

Capstone's CEO told us Capstone could not deliver the freshwater filtration plant according to the terms of the contract because of a delay in obtaining state approval of the water filtration plant; therefore, they began installing the water meters. He said 298 water meters were installed, and the Town has possession of the remaining water meters. He also said the reason the loan balance is not sufficient to complete the project is because Mayor Breland directed Capstone to pay the Town for work that was not in the quote, such as \$406,215 to dig water wells^V and \$40,000 to Twin Spires Financial, LLC (Town's financial advisor). There were also increased labor costs to install the water meters since the Town did not get permission from GOWC to remove the existing water meter. The result was that Mayor Breland directed Capstone had to manually dig to install the new water meter between the existing water meter and the home instead of replacing the existing water meter.

Since the Town did not publicly bid either of these lease purchases, they may have violated state law.⁷

Recommendations

We recommend that Town management consult with its legal counsel to determine the appropriate actions to take regarding the improper financial projections and use of bond proceeds. We also recommend that Town management develop and implement policies and procedures to ensure all of its purchases are in accordance with state law.

^U Mayor Caesar Velasquez authorized a payment out of the escrow account to make the first lease payment due to Citizen's Bank & Trust of Vivian.

^V The Town's management directed the wells to be dug at three locations: one well did not produce water and was capped, and one of the two remaining wells was dug on private property.

LEGAL PROVISIONS

¹ **Louisiana Revised Statute (La. R.S.) 14:133(A)** states, “Filing false public records is the filing or depositing for record in any public office or with any public official, or the maintaining as required by law, regulation, or rule, with knowledge of its falsity, of any of the following: (1) Any forged document. (2) Any wrongfully altered document. (3) Any document containing a false statement or false representation of a material fact.”

² **18 U.S.C. § 1344, Bank Fraud** states, in part, “Whoever knowingly executes, or attempts to execute, a scheme or artifice—(1) to defraud a financial institution; or (2) to obtain any of the moneys, funds, credits, assets, securities, or other property owned by, or under the custody or control of, a financial institution, by means of false or fraudulent pretenses, representations, or promises....”

³ **Louisiana Constitution Article VII, Section 8(B)** states, “Approval of Bonds. No bonds or other obligations shall be issued or sold by the state, directly or through any state board, agency, or commission, or by any political subdivision of the state, unless prior written approval of the bond commission is obtained.”

⁴ **La. R.S. 39:1410.60(A)** states, “No parish, municipality, public board, political or public corporation, subdivision, or taxing district, and no road or subroad district, school district, sewerage district, drainage or subdrainage district, levee district, waterworks or subwaterworks district, irrigation district, road lighting district, harbor and terminal district, or any other political subdivision, taxing district, political or public corporation, created under or by the constitution and laws of the state shall have authority to borrow money, incur debt, or to issue bonds, or other evidences of debt, or to levy taxes, or to pledge uncollected taxes or revenues for the payment thereof, where they are authorized by the constitution or laws of the state so to do, without the consent and approval of the State Bond Commission.”

⁵ **La. R.S. 39:577** states, “The proceeds of the sale of bonds issued under the provisions of this Subpart shall constitute a trust fund to be used exclusively for the purpose or purposes for which the bonds are authorized to be issued, but the purchaser of the bonds shall not be obliged to see to the application thereof. In the event that all or part of the proceeds of the sale of such bonds are no longer needed for the purpose for which the bonds were authorized to be issued, the governing authority of the subdivision which has issued such bonds may use the proceeds of the sale of such bonds for a purpose different from that for which the bonds were originally issued, provided that such new purpose is one for which the bonds could have been issued in the original instance and provided further that such proposed action shall have been approved by a majority in number and amount of the qualified property taxpayers voting at an election held in the manner provided by the provisions of this Chapter for authorizing bonds. In the event any governing authority has, prior to May 1, 1950, taken action substantially like that herein provided in order to obtain authorization to use the proceeds of the sale of bonds for a purpose different from that for which the bonds were originally issued, such action is hereby approved, validated and ratified.”

⁶ **La. R.S. 14:134(A)** states, “Malfeasance in office is committed when any public officer or public employee shall: (1) Intentionally refuse or fail to perform any duty lawfully required of him, as such officer or employee; or (2) Intentionally perform any such duty in an unlawful manner; or (3) Knowingly permit any other public officer or public employee, under his authority, to intentionally refuse or fail to perform any duty lawfully required of him, or to perform any such duty in an unlawful manner.”

La. R.S. 42:1461(A) states, “Officials, whether elected or appointed and whether compensated or not, and employees of any "public entity", which, for purposes of this Section shall mean and include any department, division, office, board, agency, commission, or other organizational unit of any of the three branches of state government or of any parish, municipality, school board or district, court of limited jurisdiction, or other political subdivision or district, or the office of any sheriff, district attorney, coroner, or clerk of court, by the act of accepting such office or employment assume a personal obligation not to misappropriate, misapply, convert, misuse, or

otherwise wrongfully take any funds, property, or other thing of value belonging to or under the custody or control of the public entity in which they hold office or are employed.”

⁷ **La. R.S. 38:2212** states, in part, “(A)(1)(a) All public work exceeding the contract limit as defined in this Section, including labor and materials, to be done by a public entity shall be advertised and let by contract to the lowest responsible and responsive bidder who bid according to the bidding documents as advertised, and no such public work shall be done except as provided in this Part...C.(1) Except as provided in Paragraphs (2) and (3) of this Subsection, the term "contract limit" as used herein shall be equal to the sum of one hundred fifty thousand dollars per project, including labor, materials, and equipment as per the rates in the latest edition of the Associated Equipment Dealers Rental Rate Book and administrative overhead not to exceed fifteen percent, provided that beginning February 1, 2015, and annually on February first of each subsequent year, the office of facility planning and control within the division of administration shall adjust the "contract limit" by an amount not to exceed the annual percentage increase in the Consumer Price Index in the preceding year. The office of facility planning and control within the division of administration shall publish the new contract limit for public works contracts in the Louisiana Register in January of each year.”

La. R.S. 38:2212.1(A)(1)(a) states, “All purchases of any materials or supplies exceeding the sum of thirty thousand dollars to be paid out of public funds shall be advertised and let by contract to the lowest responsible bidder who has bid according to the specifications as advertised, and no such purchase shall be made except as provided in this Part.”

APPENDIX A

Management's Response



Town of Sterlington

503 Highway 2 Sterlington, LA 71280 Phone # 665-2157 Fax # 665-2841
Mayor, Caesar Velasquez

October 28, 2019

To Louisiana Legislative Auditor's:

After reviewing the report from the Louisiana Legislative Auditor's, I feel confident in their findings and recommendations. I believe Sandra Whitehead and team of Louisiana Legislative Auditors have researched and documented an accurate report. However, in my opinion the comments from the CEO of Capstone are not accurate. I do not feel that Capstone provided the documentation necessary to accurately show the use of the funds obtained for the water system. In response to the recommendations, the Town has implemented policies and procedures to ensure adherence to state laws.

One of the positives to come out of this report has been to determine that no one on the current administration or staff has taken any actions to misappropriate funds or resources from the Town. As the Town pushes forward to fiscal solvency, we are committed to performing our responsibilities at highest level.

You may contact me if you should have any additional questions.

Sincerely Yours,

Caesar Velasquez
Mayor

CV/md