OCII
office of
COMMUNITY INVESTMENT
and INFRASTRUCTURE

107-0562017-002

Agenda Item **No. 5(d)**
Meeting of June 20, 2017

MEMORANDUM

TO: Community Investment and Infrastructure Commissioners

FROM: Nadia Sesay, Interim Executive Director

SUBJECT: Authorizing the issuance of taxable and tax-exempt refunding tax allocation bonds captioned 2017 Series D Taxable Subordinate Tax Allocation Refunding Bonds (San Francisco Redevelopment Projects) in an aggregate principal amount not to exceed $ 158,000,000 and 2017 Series E Subordinate Tax Allocation Refunding Bonds (San Francisco Redevelopment Projects) in an aggregate principal amount not to exceed $27,000,000, approving and directing the execution of a first supplement to the Indenture of Trust, bond purchase contract and one or more redemption agreements, and approving other related documents and actions, various project areas

EXECUTIVE SUMMARY

The Office of Community Investment and Infrastructure (OCII) proposes issuing two series of refunding bonds to refund certain loan agreements (the "2017 Refunded Loan Agreements") related to loans made by the City and County of San Francisco Redevelopment Financing Authority (the "Authority") to the former Redevelopment Agency of the City and County of San Francisco. The refunding bonds will refund up to seven outstanding bonds of the Authority (the "2017 Refunded Bonds"). The 2017 Series D bonds ("2017D") would have an estimated par of $123 million and would refund five prior series of 2017 Refunded Bonds. The 2017 Series E bonds ("2017E") would have an estimated par amount of $22 million and would refund two prior series of 2017 Refunded Bonds. Refunding the 2017 Refunded Bonds and the associated 2017 Refunded Loan Agreements would reduce OCII's debt service costs, increasing the amount of tax increment available to fund its enforceable obligations. In addition, the proposed refunding of certain bonds would allow OCII to preserve funding for enforceable obligations which remain in effect for several years.

Issuance of the 2017D and 2017E bonds requires Commission approval of Resolution 23-2017. Resolution 23-2017 approves in form documents necessary to seek Oversight Board and Department of Finance approval for the sale of 2017D and 2017E. The resolution sets forth not-to-exceed amounts for the bond principal amounts, interest rates, and underwriter's discount. The resolution also approves the underwriter selection and authorizes staff to take all actions necessary to complete the transaction.

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Subsequent OCII Commission and Financing Authority action will be required to approve the preliminary official statement and other final documents and actions.

Staff recommends the Commission approve Resolution 23-2017 to allow the refunding transactions to proceed.

DISCUSSION

OCII proposes issuing refunding bonds to refund up to seven outstanding bonds and related loan agreements issued by the former San Francisco Redevelopment Agency. Prior to the dissolution of redevelopment agencies, the Authority issued bonds utilizing a cross-collateralized credit. The cross-collateralized credit combined the unpledged property tax increment generated by most Project Areas, creating a large, diverse, and therefore strong credit. However, because Redevelopment Law required that property tax increment generated in a Project Area be expended, for non-housing purposes, in the same Project Area, the former Redevelopment Agency utilized the Financing Authority to issue the bonds and enter into loan agreements relating to each Project Area. This structure allowed OCII to bond against the collective strength of Project Areas, while adhering to the Redevelopment law requirement that tax increment generated in a Project Area be spent in that Project Area, except for affordable housing, which could be funded anywhere in the City and County of San Francisco. When OCII refunds bonds issued by the Authority, it must also refund the loan agreements related to those bonds.

OCII plans to issue two series of refunding bonds, 2017D and 2017E. 2017D would have an estimated par amount of approximately $123 million and would refund three taxable bonds and one tax-exempt bond and the related loan agreements. 2017E would have an estimated par amount of $22 million and would refund two tax-exempt bonds and related loan agreements. Refunding these bonds would reduce OCII's debt service costs and preserve funding for development costs associated with existing enforceable obligations. The FY16-17 budget authorizes OCII to issue refunding debt where savings can be achieved.

Proposed Bonds

2017D is a taxable refunding bond and would be issued in an estimated par amount of $123 million. 2017D would refund up to five outstanding taxable bonds issued prior to Dissolution. Current candidates include 2009A, 2009B, 2009E, 2010A, and 2011A. The final size of the refunding may increase or decrease depending on market conditions. 2009B, issued on a tax-exempt basis, would be refunded on a taxable basis in order to preserve OCII's ability to expend up to $5 million in proceeds from the prior bonds that are held on reserve for enforceable obligations. Generally, refunding tax-exempt bonds on a taxable basis results in lower savings than refunding on a tax-exempt basis. Currently, the interest rate for tax-exempt and taxable bonds are very similar. Therefore the impact of refunding 2009B on a taxable basis is minimal. The final size of the refunding may increase or decrease depending on market conditions.

2017E would be issued in an estimated amount of $22 million and would refund up to two outstanding tax-exempt bonds issued prior to Dissolution. Current candidates include 2009F and 2011B.

Section 34177.5 of the Dissolution Act authorizes the Successor Agency to issue refunding bonds pursuant to Article 11 (commencing with Section 53580) of Chapter 3 of Part 1 of Division 2 of Title 5 of the Government Code for the purpose of achieving debt service savings provided that the following conditions are satisfied (the "Savings Parameters"): (A) the total interest cost to maturity on the refunding bonds or other indebtedness plus the principal amount of the refunding bonds or other indebtedness shall not exceed the total remaining interest cost to maturity on the bonds or other indebtedness to be refunded plus the remaining principal of the bonds or other indebtedness to be refunded, and (B) the principal amount of the refunding bonds or other indebtedness shall not exceed the amount required to defease the refunded bonds or other indebtedness, to establish customary debt service reserves, and to pay related costs of issuance.

To determine compliance with the Savings Parameters for 2017D and 2017E, OCII directed its Municipal Advisor, CSG Advisors, to prepare a debt savings analysis. A debt savings analysis identifies the potential savings of issuing a refunding bond. The debt savings analysis prepared by CSG Advisors shows significant potential savings, in compliance with the Savings Parameters, as described below.

Exhibit 1 describes the sources and uses for the most conservative cases e.g., the highest interest rate assumption. The sources and uses are estimated and subject to change.

Exhibit 1:
Sources and Uses of Funds 2017 & 2017E

Sources of Funds		2017D		2017E
Par Amount	$	122,855,000	$	21,270,000
Net Premium / Discount			$	2,235,420
Other Sources of Funds				
Prior Debt Service Reserve	$	10,022,500	$	2,224,500
Total Sources	**$**	**132,877,500**	**$**	**25,729,920**

Uses of Funds		2017D		2017E
Refunding Escrow Deposits				
SLGS Purchases	$	131,842,402	$	25,520,412
Cash Deposit	$	1	$	0
Delivery Date Expenses				
Cost of Issuance	$	383,589	$	66,411
Underwriter's Discount [1]	$	448,421	$	105,287
Reserve Surety (2.15%)	$	202,302	$	35,025
Additional Proceeds	$	785	$	2,785
Total Uses	**$**	**132,877,500**	**$**	**25,729,920**

[1] The underwriter's discount is the difference between the price the underwriter pays the issuer and price at which it sells the offering to the public and reflects the underwriter's fee for issuing the bonds.

The debt service savings analysis assumes an All-In True Interest Cost ("All-in TIC") of 4.44 percent for the 2017D bonds and 4.10 percent for the 2017E bonds. The All-In TIC is the real cost of issuing the proposed refundng bonds. As the All-In TIC includes all ancillary fees and costs, it is higher than the market interest rate. The All-In TIC in the debt service savings analysis is based on market conditions as of May 15, 2017, plus a 50 basis point (0.5 percent) cushion to account for market volatility. Given these parameters, OCII anticipates achieving $11.8 million net present value savings (10.3 percent) for 2017D and $2.6 million net present value savings (11.6

percent) for 2017E.

The projected savings for both 2017D and 2017E is greater than the savings required by the OCII Debt Policy, passed by the Commission in 2004. As per OCII's debt policy, and consistent with the Redevelopment Dissolution Law, each refunding should achieve an approximate minimum net present value savings of three percent of par for each refunded bond.

The final size of 2017D and 2017E will depend on market conditions and the economics of each refunding under consideration.

Credit

All bonds are issued against a credit. The credit is the revenue stream the issuer, in this case OCII, will use to pay the debt service on the bonds. As previously described, the Authority issued bonds using a cross-collateralized credit in order to comply with the Redevelopment Law requirement that tax increment generated in a Project Area be spent in that Project Area, except for affordable housing, which could be funded anywhere in the City and County of San Francisco.

The Redevelopment Dissolution Law eliminated the restrictions on project area funding so long as any state-approved enforceable obligation exists. Therefore, post-Dissolution, OCII replaced the cross-collateralized credit with the Redevelopment Property Tax Trust Fund (RPTTF) credit (Section 34177.5(g) of the Health and Safety Code). Like the cross-collateralized credit, the RPTTF credit combines the unpledged property tax increment generated by most Project Areas. However, because Redevelopment Dissolution Law eliminated the general requirement of Redevelopment Law that property tax increment generated in a Project Area be expended in the same Project Area, (Section 34177.5(g) of the Health and Safety Code), the RPTTF credit does not utilize the loan structure and authority utilized by the cross-collateralized credit. In 2014, OCII issued the 2014B and 2014C refunding bonds secured by amounts deposited in the RPTTF with respect to certain Project Areas, after the payment of Existing Loan Agreements and other amounts. The proposed 2017D and 2017E bonds would be issued against the RPTTF credit and would be secured by such amounts in the RPTTF on a parity with, e.g. on the same terms as, the 2014B and 2014C bonds.

Financing Team

OCII issues bonds with the assistance of a financing team composed of experts in issuing public debt. The financing team is composed of a Municipal Advisor, Bond Counsel, Disclosure Counsel, Fiscal Consultant, and Underwriter.

<u>Municipal Advisor</u>

The Municipal Advisor ("MA") oversees the financing process and opines on the pricing. The MA for 2017D and 2017E is CSG Advisors. OCII selected CSG Advisors via a competitive process issued to the City's Financial Advisor Pool. The Commission approved the CSG Advisors contract on October 4, 2016 by OCII Resolution 44-2016.

<u>Bond Counsel</u>

Bond Counsel ensures and opines that all required steps are taken to ensure the bonds are compliant with legal and regulatory requirements. Bond Counsel for 2017D and 2017E is Jones Hall. OCII selected Jones Hall via a competitive process issued to the City's Bond Counsel pool. The Commission approved the Jones Hall Contract on August 2, 2016 by OCII Resolution 38-2016. The Executive Director amended the contract as described in a

December 6, 2016 memo to the Commission.

Disclosure Counsel
Disclosure Counsel drafts and guides the content of the disclosure document used to market the bonds. Disclosure Counsel for 2017D and 2017E is the Law Offices of Alex Chiu. Chiu was selected via a competitive process issued to the City's Bond Counsel pool. The Commission approved the Chiu contract on August 2, 2016 by OCII Resolution 36-2016. The Commission will consider an amendment to the contract's not-to-exceed amount and Scope of Service on June 20, 2017.

Fiscal Consultant
The Fiscal Consultant assembles and prepares the Fiscal Consultant's Report, which is one of the components of the Official Statement. The Official Statement is the prospectus for the bond issuance and discloses the finances surrounding the issuance the bond and identifies how the bond will be repaid. Post-issuance, the Financial Consultant prepares Securities and Exchange (SEC)-mandated continuing annual disclosure reports for each credit against which bonds have been issued. The Fiscal Consultant for 2017D and 2017E is Urban Analytics. OCII selected Urban Analytics via a competitive process issued to the City's Fiscal Consultant pool. The Commission approved the Urban Analytics contract on December 15, 2015 by OCII Resolution 80-2015 and amended the contract on December 6, 2016 by OCII Resolution 55-2016, which modified Scope of Service to include refunding bonds and increased the not-to-exceed amount commensurately.

Underwriter
The Underwriter markets, purchases, and sells the bonds. The Underwriters for 2017D and 2017E are Piper Jaffrey & Co., Steifel, Nicolaus, & Co. and Stinson Securities, LLC.

OCII selected the underwriters via a competitive process issued to the City's Underwriter pool. OCII staff directed CSG Advisors (CSG), the MA for the proposed transactions, to issue a Request for Proposals (RFP) for bond underwriting services. CSG issued the RFP on December 19, 2016 and received 12 responses: Backstrom McCarley Berry & Co., Blaylock Beal Van, LLC, Citigroup Global Markets, Mesirow Financial, Inc., Morgan Stanley, Piper Jaffray & Co ("Piper"), RBC Capital Markets, Rice Financial Products Co, Stern Brothers & Co, Stifel, Nicolaus & Company, Inc. ("Stifel"), Stinson Securities, LLC ("Stinson") and Wells Fargo Securities.

A panel composed of Scott Smith of CSG, Jamie Querubin of the City Controller's Office of Public Finance, and John Daigle, OCII Senior Financial Analyst evaluated the proposals based on:

- experience in selling California tax allocation bonds, especially since January 1, 2012 (i.e. post-Dissolution),
- the number and size of financings in which the firm and the primary service providers participated,
- the relevance of prior transactions to the proposed transactions,
- the depth and quality of the discussion of the structure, credit, and marketing of the proposed transactions, and
- the proposed underwriter's discount.

The panel also considered OCII's Local Business Enterprise and Small Business Enterprise contracting goals.

The panel recommended one senior manager and two co-managers for 2017D and 2017E. Based on its strong position in the sale of post-Dissolution redevelopment debt, as well as its prior experience underwriting OCII bonds issued under the cross-collateralized credit, the panel recommended Piper Jaffray as senior manager. Based on its prior performance working on OCII issuances, most recently the 2017A and 2017B bonds, and its extensive presence in the California tax allocation bond market, the panel recommended Stifel as co-manager. Pursuant to OCII's Small Business Enterprise (SBE) policy goals, the panel also recommended Stinson as co-manager. Stinson has provided OCII satisfactory service as a co-manager in the past. Of the firms in the SBE category, the panel ranked Stinson the highest.

PROPOSED ACTION

Approving the above described refunding bond issuances requires the Commission to approve the Resolution 23-2017. Resolution 23-2017 authorizes the issuance of the 2017D taxable refunding bonds in a principal amount not-to -exceed $158 million and the 2017E tax-exempt refunding bonds in a principal amount not-to-exceed $27 million. Based on current market conditions, OCII expects to issue 2017D in the par amount of $123 million and 2017E in the principal amount of about $22 million.

For 2017D, the difference between the estimated size of the issue and the maximum authorization amount is to allow for two possible scenarios: the taxable refunding of additional tax-exempt bonds to accommodate an unforeseen federal tax issue; and, the need to cash fund a debt service reserve, rather than using a surety bond as currently expected. In the first case, some bonds would move from 2017E to 2017D increasing the size of 2017D. In the second case, more bonds would have to issued in order to provide funding for the 2017D debt service reserve.

For 2017E, the difference between the estimated size of the issue and the maximum authorization allows for the cash funding of the debt service reserve as described above and, secondly, allows for market conditions where investors are willing to pay a lesser premium than they are currently. The lower premium (amount by which the price paid for the bonds is higher than the par amount of the bonds) would require a higher par amount to generate funds sufficient to complete the refundings.

In support of these issuances, the Resolution approves a first supplement to the indenture of trust, the bond purchase agreements, and the redemption agreements for each of the 2017 Refunded Loan Agreements and 2017 Refunded Bonds. An indenture of trust is a written agreement between the issuer of a bond and the bondholders that specifies the terms of the bond, including the interest rate and maturity date. A bond purchase agreement is a written agreement between the issuer and the underwriter that establishes the terms of the bond sale, including sale price, bond interest rate, bond maturity, and redemption provisions. Both the indenture of trust and the bond purchase agreements are required for Oversight Board and Department of Finance review. The resolution also affirms the selection of Underwriters and directs staff to take all necessary actions to close the proposed transactions.

Staff recommends the Commission approve Resolution 23-2017 in support of 2017D and 2017E.

NEXT STEPS

Pending approval of Resolution 23-2017, staff will request approval of the 2017D and 2017E bond issuances from the Oversight Board. Pending Oversight Board approval, staff will request approval of the 2017D and 2017E issuances from the Department of Finance. Pending Department of Finance approval, staff anticipate issuing the bonds prior to December 31, 2017.

California Environmental Quality Act

Authorization of bonds and contracting for services related to the sale and issuance of bonds is a Successor Agency fiscal activity that does not constitute a "Project," as defined by the California Environmental Quality Act ("CEQA") in CEQA Guidelines Section 15378(b) (4) and will not independently result in a physical change in the environment, and is not subject to environmental review under CEQA.

(Originated by John Daigle, Senior Financial Analyst)

Nadia Sesay
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