MEMORANDUM

TO: Office of Community Investment and Infrastructure Commissioners

FROM: Tiffany Bohee
Executive Director

SUBJECT: Resolution Authorizing the Issuance of Taxable and Tax-Exempt Refunding Tax Allocation Bonds in a Combined Aggregate Principal Amount Not to Exceed $300,000,000, and Approving and Directing the Execution of an Indenture of Trust and a Bond Purchase Contract, and Approval of Other Related Documents and Actions, Various Project Areas, Subject to Oversight Board and Department of Finance Concurrence

EXECUTIVE SUMMARY

Under current or reasonably foreseeable market conditions, the opportunity exists to issue refunding bonds to refinance as many as fifteen outstanding tax allocation bonds, reducing the amount of RPTTF funding required for debt service in future years. Under current market conditions, the net present value of the savings is estimated at over $12 million. Two refunding bond series are proposed: 2014 Series B Taxable Subordinate Tax Allocation Refunding Bonds (the “2014 Series B Bonds”) and 2014 Series C Subordinate Tax Allocation Refunding Bonds (the “2014 Series C Bonds”).

The Resolution approves in form several critical bond documents (Bond Indenture, Bond Purchase Contract, and Redemption Agreements) necessary to seek Oversight Board and Department of Finance approval for the sale of the Bonds. The Resolution further authorizes and directs staff to take all actions necessary to complete the transaction and requests the Oversight Board to make certain determinations and to direct the OCII to proceed with the transaction.

The Resolution sets forth not to exceed limits for the principal amount of the bonds, interest rate and underwriter’s discount.

Subsequent OCII Commission action will be required to approve the bond underwriter selection and the Preliminary Official Statement before the transaction can be completed.

Staff recommends approval of this resolution so that the refinancing transaction can proceed without delay.

DISCUSSION

Refunding Opportunity

At current or reasonably foreseeable market interest rates as many as 15 of the currently outstanding bonds are candidates for refunding. These 15 bonds comprise 51 separate project area loans. At current rates, at least 12 of the refunding candidates are economic and would generate overall savings equal to about $13 million, or 6.3% of the bond principal of the bonds to
be refunded. Refunding of these 12 candidates would require a combined refunding bond issuance of approximately $190 million. If all 15 bonds are ultimately included in the refunding, the total size of the refunding bond transaction would be approximately $275 million and savings would be considerably higher.

OCII debt policy establishes, as a guideline, that present value savings for each refunded bond should be 3% of outstanding bond principal but allows flexibility in the application of this criterion depending on circumstances. In the current transaction staff is proposing to include all bonds with positive savings. There are three primary considerations behind this: first, as rates are at extreme lows right now, it is unlikely greater savings could be realized by waiting for better market conditions; second, the large size of the transaction makes the marginal issuance cost of each additional bond very small; and, third, consolidating the debt portfolio and eliminating individual loans simplifies State and secondary market reporting and administration over time.

**New Bond Structure**

The Resolution approves issuance of the 2014 Series B Bonds in an aggregate initial amount not to exceed $110,000,000, at a true interest cost not to exceed 5.4%, and with an underwriter’s discount not to exceed .462% of the aggregate initial amount of the bonds; and approves issuance of the 2014 Series C Bonds in an aggregate initial amount not to exceed $190,000,000, at a true interest cost not to exceed 5%, and with an underwriter’s discount not to exceed .45% of the aggregate initial amount of the bonds.

The proposed refunding bonds will be issued directly by the OCII under a new subordinated credit structure. Technically this means that debt service on the new bonds can only be paid after debt service is paid on the existing bonds. Ordinarily this would result in higher interest rates for the subordinated bonds. However in the experience and judgment of the financing team, this is unlikely to have a significant effect as the old credit will be closed to the issuance of any new money bonds and the investor perception of the San Francisco economy is very positive.

The existing bonds were all issued through the City and County of San Francisco Redevelopment Financing Authority, a Marks-Roos joint powers authority. This allowed various project area loans to be pledged to the repayment of a single bond. This pooling of pledged loan revenues under a single bond allowed smaller project area loans efficient access to the bond market and lowered financing costs for all. But under this structure each loan retains its own reserve requirements, debt service coverage requirements, maturities, and repayment schedule.

Under the new credit there will be no individual project area based loans, rather the pledged revenues will come from the RPTTF without distinction as to project area source (other than the exclusion of the Mission Bay and Shipyard project areas). This effectively creates a merged project area, greatly simplifying both the credit and long-term administration of the debt portfolio.

This structure also will allow the transaction to proceed more quickly to completion, reducing market risk. If the refunding bonds were issued under the existing credit structure, time consuming negotiations with the various insurers of certain of those bonds would need to occur in order for certain of the refundings to proceed. As the outcome of such negotiations would impact the Bond Indenture, the approval process would be delayed until such negotiations were complete, exposing the savings to additional market risk. Additional complexities which would
have a strong negative impact on the tax-exempt issuance will become effective if those bonds are not delivered prior to calendar year end. Thus any delay will put the majority of the transaction at substantial risk.

After careful consideration of all of these factors, the financing team decided without reservation that it was to the best advantage of the OCII, and of the taxing entities who are the beneficiaries of this transaction, to proceed with the refunding under the proposed subordinate structure.

**The Bond Documents**

Commission approval of certain documents, specifically, the Indenture of Trust, the Bond Purchase Contracts and the Redemption Agreements, is necessary before OCII can request approval of the Oversight Board and the Department of Finance. The Indenture of Trust between OCII and the Trustee establish the Trusts to hold bond related funds, and secure the bond payments and performance of other bond covenants. The Bond Purchase Contracts set forth the terms under which the bonds are sold by the OCII and purchased by the bond underwriters. The Redemption Agreements are among the OCII, the Redevelopment Financing Authority (as issuer of the bonds to be redeemed) and the respective trustees for the bonds to be refunded (as Escrow Trustee). There is a Redemption Agreement for each series of refunded bonds. These agreements establish escrows to hold the proceeds of the new bonds until such time as those funds are used to redeem the old bonds.

**Next Steps**

- September 22: OCII will seek bond sale approval of the Oversight Board.
- September 23: OCII will submit its request for Department of Finance approval.
- October (or as soon as possible thereafter) Commission will consider approval of the bond underwriters recommended by staff.
- November 18: Commission will consider approval of the Preliminary Official Statement. This is the final Commission action prior to the sale and issuance of the bonds.
- November 18: the Financing Authority will meet to approve execution of the Redemption Agreements.
- 11/28 (or sooner): DOF approval expected.
- Early December: bond pricing
- Prior to December 31: closing of transaction.

**Enabling Law**

Redevelopment Dissolution Law grants Successor Agencies the authority to issue bonds, subject to review and approval by the Oversight Board and the Department of Finance, for the purpose of creating savings in the use of tax increment to service debt, to smooth debt service spikes, and to address certain other circumstances. California Health and Safety Code Section 34177.5(a)(1).

**California Environmental Quality Act**

The issuance of refunding bonds is not a “project,” as defined by the California Environmental Quality Act (“CEQA”) in CEQA Guidelines Section 15378(b) (5), because the action will not
result in a physical change in the environment and therefore is not subject to environmental review under CEQA.

(Originated by John Daigle, Sr. Financial Analyst)

Tiffany Bobee
Executive Director

Attachment A: Indenture of Trust
Attachment B: Bond Purchase Contract, Series B
Attachment C: Bond Purchase Contract Series C
Attachment D: Sample Redemption Agreement, Series B (others on file, available upon request)
Attachment E: Sample Redemption Agreement, Series C (others on file, available upon request)