



THE CITY OF SAN DIEGO
REPORT TO THE CITY COUNCIL

DATE ISSUED: February 22, 2012 REPORT NO: 12-020

ATTENTION: Budget and Finance Committee

SUBJECT: Bond Refundings

REFERENCE: Bond Refundings (Report No. 11-334), dated October 12, 2011;
Proposed Fiscal Year 2011 Economic Bond Refundings, Report dated
October 6, 2010; 2012 Deferred Capital Improvement Program Bond
Authorization (Report No. 11-152), dated November 16, 2011;
Convention Center Expansion Financing Authority Subordinated Lease
Revenue Refunding Bonds, Series 2010 (Report No. 10-132), dated
October 6, 2010

REQUESTED ACTIONS:

Forward the refunding of the 2002 Fire and Life Safety Bonds, 1998 Convention Center Bonds, and CFD No. 1 Special Tax Bonds to City Council for consideration and approval in accordance with the timelines established for the bond refundings. The City Council will be requested to authorize the issuance of the refunding bonds for the respective transactions, and approve the related financing and disclosure documents.

STAFF RECOMMENDATION:

Forward the requested actions for City Council's consideration and approval.

EXECUTIVE SUMMARY:

I. Background

Since the bond refundings update presented to the Budget and Finance Committee on October 19, 2011, interest rates have continued to trend lower. To illustrate the recent interest rate trend movements on the long end, the 20-year Municipal Market Data AAA Index (the "MMD Index," which is a standard index of AAA rated municipal bonds) was 3.47% on October 19, 2011, which was already down from 4.33% in December 2010. As of February 14, 2012, the MMD 20-year Index is at 2.78%, down 69 basis points or approximately 20% from the already historically low rates of October 2011. At the January 25, 2012 Federal Open Market Committee meeting, the Federal Reserve reconfirmed its expectation of a low interest rate environment, and extended the period in which interest rates would be expected to remain low to 2014 from the previously targeted mid-2013 time-frame. However, the Federal Reserve's stated

anticipated actions are still a forecast and recent economic trends and an improving stock market may result in higher interest rates. In addition, the equity and bond markets remain volatile. While municipal bond nominal yields continue to be at, or near, all-time lows, other factors including investor demand (both retail and institutional), the amount of municipal bond supply, and municipal bond mutual fund inflows/outflows can impact yields. Fund flows into municipal bond funds have been positive in all but two of the last six months. Proposed fiscal policy in Washington as well as continued European sovereign debt concerns can also impact actual yields, but the current interest rate environment remains positive for the foreseeable future in terms of conducting additional economic refundings.

Due to the more recent drop in interest rates, the Fire and Life Safety Facilities Lease Revenue Bonds, Series 2002B and the Community Facilities District No. 1 (Miramar Ranch North) Special Tax Refunding Bonds Series 1998 can now be economically refunded. In addition, while the interest rate environment in fall 2011 did not support resumption of work on the partial economic refunding of the Convention Center Expansion Financing Authority Lease Revenue Bonds, Series 1998A, the current favorable interest rate environment now supports a full refunding of these bonds as well.

II. 2002 Fire and Life Safety Bonds Refunding

In 2002, the Public Facilities Financing Authority of the City of San Diego issued the Fire and Life Safety Facilities Lease Revenue Bonds, Series 2002B (“2002 F&LS Bonds”) in the amount of \$25.1 million. The proceeds of the Series 2002 F&LS Bonds were used to finance the construction of various fire station and lifeguard improvements within the City. Approximately \$21.2 million in 2002 bonds is currently outstanding.

Under existing market conditions, the 2002 F&LS Bonds can be refunded in full on an economic basis. Based on rates as of February 21, 2012, all the 2002 bonds could be current refunded generating cumulative cash flow savings estimated at \$2.5 million over the remaining life of the bond issue, which would generate average annual cash flow savings of approximately \$130,000 in Fiscal Years 2014 - 2032. The net present value savings is projected to be \$1.9 million or 9.4%.

As previously discussed at the Budget and Finance Committee on November 16, 2011, Debt Management is currently working on the 2012 Deferred Capital Improvement Lease Revenue Bonds (2012 Deferred CIP Bonds). Debt Management recommends executing the refunding of the 2002 F&LS Bonds concurrent with the issue of the proposed 2012 Deferred CIP Bonds.

The proposed 2012 Fire and Life Safety Refunding Bonds, along with the 2012 Deferred CIP Bonds, could be issued under the Master Indenture, Master Site Lease and Master Lease established in 2010 with the issuance of the Master Refunding Bonds, Series 2010A. Using a Master Lease and Master Indenture structure provides for lower costs, stronger credit, and more diversity in the Leased Properties. The assets originally pledged for the 2002 F&LS Bonds will be maintained for the proposed 2012 Fire and Life Safety Refunding Bonds. No change to the 2002 F&LS Bonds repayment term will be made and the term of the refunding bonds will match the term of the bonds being refunded.

Refunding Timeline

Debt Management is developing the legal documents and Financing Ordinance, which would include both the 2012 Deferred CIP Bonds and the 2012 Fire and Life Safety Refunding Bonds, to take to City Council for review and approval by March 2012 and the Preliminary Official Statement (“POS”) for approval via resolution in May 2012. The proposed 2012 Lease Revenue Refunding Bonds are expected to be priced by the end of May, with closing planned for early June 2012. The refunding proceeds will be placed in an escrow fund for 30-days, and outstanding bonds will be redeemed by early July 2012.

III. 1998 Convention Center Bonds Refunding

In September 1998, the Convention Center Expansion Financing Authority of the City of San Diego issued the Convention Center Expansion Financing Authority Lease Revenue Bonds, Series 1998A (the “1998A Convention Center Bonds”) in the amount of \$205 million. The 1998A Convention Center Bonds were issued to finance the costs of the first expansion to the San Diego Convention Center. Currently, \$156.8 million in 1998 bonds is outstanding.

Under existing market conditions, the 1998A Convention Center Bonds can be refunded in full on an economic basis. Based on rates as of February 6, 2012, approximately \$150.7 million in bonds could be current refunded generating cumulative cash flow savings of approximately \$12.2 million or average annual cash flow savings of approximately \$750,000 over the remaining life of the bonds, Fiscal Year 2013 through Fiscal Year 2028. The net present value savings is projected to be approximately \$9.2 million or 6.11%. No change to the 1998A Convention Center Bonds repayment term will be made and the term of the refunding bonds will match the term of the bonds being refunded.

The 2012 Convention Center Refunding Bonds will use a lease revenue bonds structure involving leasing agreements, similar to the 1998A Convention Center Bonds, concerning the City, the San Diego Unified Port District, and the Convention Center Expansion Financing Authority. The leased property remains the 1998 expanded portion of the Convention Center, which is the same property that was built relying on the 1998A bond proceeds and leased under the 1998A Convention Center Bonds.

The 1998A Convention Center Bonds currently meet the one-half year debt service reserve fund requirement with an Ambac surety policy; there is no established cash reserve for the 1998A Convention Center Bonds. Purchase of a similar surety or cash funding of the debt service reserve fund for the 2012 Convention Center Refunding Bonds is not economic for refunding purposes. A refunding with a debt service reserve fund requirement would not generate necessary present value savings; therefore, a refunding that includes a debt service reserve fund requirement is not recommended. Due to the nature of the credit and the financing structure, the underwriters for the transaction and the City’s independent financial advisor, KNN Public Finance, have advised the City that under current market conditions, it is viable to market the bonds with no debt service reserve fund requirement to produce an economic refunding that results in the necessary net present value savings.

Refunding Timeline

Debt Management is developing the legal documents and Financing Ordinance to take to City Council for review and approval in March 2012 and the POS for approval via resolution in May 2012. The proposed 2012 Convention Center Refunding Bonds are expected to be priced by the end of May, with closing planned for early June 2012. The refunding proceeds will be placed in an escrow fund until they can be redeemed in early July 2012.

IV. Conduit Financing – CFD No. 1 Special Tax Bonds Refunding

In July 1998, the City issued the Community Facilities District No. 1 (Miramar Ranch North) Special Tax Refunding Bonds Series 1998 in the amount of \$59.5 million to advance refund the Community Facilities District No. 1 Special Tax Bonds 1991 Series A and 1995 Series B (the "1998 Special Tax Refunding Bonds"). The bonds were conduit issuances, executed to fund certain public infrastructure facilities within or serving the district. The facilities include major street improvements, water and sewer facilities, community park improvements, a library contribution, and a portion of Fire Station No. 37. The facilities were substantially completed in the late 1990's and all facilities have been acquired by the City. The 1998 Special Tax Refunding Bonds are secured solely by special taxes levied upon 3,149 parcels of property located within the district. The special taxes are levied and collected annually via property tax bills. Currently, \$31.7 million in 1998 bonds is outstanding.

It is anticipated that approximately \$27 million of special tax refunding bonds (the "CFD No. 1 Special Tax Refunding Bonds") will be issued in June 2012 to execute a full refunding of the 1998 Special Tax Refunding Bonds. The refunding bonds will be offered as a current refunding requiring a minimum of 3% net present value savings in debt service compared to the outstanding bonds. Assuming an investment grade rating of BBB+, and based on rates as of February 17, 2012, the refunding bonds would generate net present value savings over the remaining term of the bonds (through 2020) of approximately \$1.6 million, representing 5.0% of the refunded bonds. The average annual savings to the district and the special tax payers would be approximately \$470,000 through 2020 starting tax year 2013. No change to the 1998 Special Tax Refunding Bonds repayment term will be made and the term of the refunding bonds will match the term of the bonds being refunded.

Refunding Timeline

Debt Management is preparing to take the legal documents, POS, and the Financing Resolution to City Council for review and approval in April or May 2012. The proposed CFD No. 1 Special Tax Refunding Bonds are expected to be priced by the end of May, with closing planned for early June 2012. The refunding proceeds will be placed in an escrow fund until September 1, 2012, when the outstanding bonds will be redeemed.

CITY COUNCIL AUTHORIZATION

At this time, it is expected that the legal and financing documents for the three transactions would be presented to City Council in accordance with the respective time-lines provided above. The POS for each transaction will be reviewed by the Disclosure Practices Working Group before it is docketed.

FISCAL CONSIDERATIONS:

The pricing and closing of the economic refunding bonds would be subject to favorable market conditions and the fulfillment of the City’s net present value savings requirements for economic refundings. As described above, under current market conditions, the proposed economic refundings would produce substantial annual debt service savings, and produce annual savings for the special taxpayers within CFD No. 1.

PREVIOUS COUNCIL and/or COMMITTEE ACTION:

Debt Management presented the potential economic refunding of a portion of the 1998A Convention Center Bonds to the Budget and Finance Committee on October 13, 2010. This refunding transaction was forwarded for City Council approval by the Budget and Finance Committee. On October 19, 2010, the financing ordinance and the legal documents for the partial refunding of the bonds were introduced at City Council. Subsequently, the refunding was put on hold due to the late release of the Fiscal Year 2010 CAFR and market conditions were no longer conducive to proceeding with an economic refunding. Since the bonds can now be fully refunded and the plan of finance has changed, the refunding is being presented to the committee as part of this action.

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS: See above.

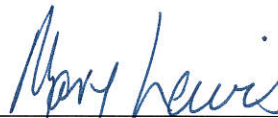
KEY STAKEHOLDERS AND PROJECTED IMPACTS:

Business entities involved in the proposed financings include investment banks, financial advisors, bond and disclosure counsels and trustees. The selected firms will be identified in the Reports to City Council that are issued when the financing and legal documents are docketed for City Council action.

Respectfully submitted,



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Mary Lewis
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