THE CITY OF SAN DIEGO

REPORT TO THE CITY COUNCIL

DATE ISSUED: March 6, 2012 REPORT NO: 12-023

ATTENTION: Council President and City Council

SUBJECT: Refunding of the Convention Center Expansion Financing Authority Lease Revenue Bonds, Series 1998A

REFERENCE: Bond Refundings (Report No. 12-020), dated February 22, 2012; Bond Refundings (Report No. 11-334), dated October 12, 2011; Proposed Fiscal Year 2011 Economic Bond Refundings, Report dated October 6, 2010; Convention Center Expansion Financing Authority Subordinated Lease Revenue Refunding Bonds, Series 2010 (Report No. 10-132), dated October 6, 2010

REQUESTED ACTIONS:

Authorize the issuance of Lease Revenue Refunding Bonds, Series 2012A ("the 2012A Refunding Bonds") by the Convention Center Expansion Financing Authority in a principal amount not to exceed $159 million and the execution of related financing documents to refund the outstanding Convention Center Expansion Financing Authority Lease Revenue Bonds, Series 1998A. The related financing documents include an Amended and Restated Expansion Lease, a Convention Center Facility Lease, an Indenture, a Bond Purchase Agreement, and a Continuing Disclosure Certificate.

STAFF RECOMMENDATION:

Approve the requested actions.

SUMMARY:

I. Background

The proposed 2012A Refunding Bonds provide for the economic refunding of the Convention Center Expansion Financing Authority Lease Revenue Bonds, Series 1998A (the "1998A Convention Center Bonds"). The 1998A Convention Center Bonds were issued in 1998 in a principal amount of $205 million to finance the costs of expanding the San Diego Convention Center. The expanded portion of the facility was substantially completed and opened in August 2001. As of the date of this report, the outstanding principal amount of the bonds is $156.8 million (after the April 1, 2012 debt service payment, $150.7 million will remain outstanding) and the final maturity is April 1, 2028.

On October 19, 2010, the financing ordinance and the legal documents for a partial refunding of the 1998A Convention Center Bonds were introduced at City Council. Subsequently, the refunding was put on hold and the financing ordinance was not ratified due to the late release of the Fiscal Year 2010 CAFR and market conditions were no longer conducive to proceeding with an economic refunding. The interest rate environment has recently shifted to a point that supports a full refunding of the bonds.

II. Discussion

A. Refunding Plan and Structure

Under existing market conditions, the 1998A Convention Center Bonds can be refunded in full on an economic basis. Based on rates as of March 2, 2012, approximately $150.7 million in bonds could be current refunded generating cumulative cash flow savings of approximately $12.8 million or average annual cash flow savings of approximately $790,000 over the remaining life of the bonds, Fiscal Year 2013 through Fiscal Year 2028. The net present value savings is projected to be approximately $9.7 million or 6.42%. 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 2012A Refunding Bonds will use a lease revenue bonds structure. Key aspects of the financing plan and structure are provided below:

- **Features:** Current full refunding (not a partial refunding; all outstanding 1998A Convention Center Bonds will be redeemed soon after the bond sale); public offering.

- **Not to Exceed Principal Amount**: $159 million refunding bonds authorization, based on aggregate net present value savings threshold level, expressed as a percentage of the par amount of the refunded bonds, of at least 3%.

- **Latest Final Maturity**: Matches the term of the existing bonds. Final maturity remains at 2028.

- **Debt Service Reserve Fund:** 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 2012A 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.

B. Legal Structure

Issuing Authority

The issuer of the 1998A Convention Center Bonds was the Convention Center Expansion Financing Authority (the "Authority"). The Authority was established under the Joint Exercise of Powers Law found in the California Government Code. Pursuant to a Joint Exercise of Powers Agreement between the City and the San Diego Unified Port District (the "Port District"), filed with the Clerk's Office on March 5, 1996, the Authority was established for the purpose of issuing the 1998A Convention Center Bonds to finance the expansion of the original Convention Center facility. The 2012A Refunding Bonds will also be issued by the Authority.

Lease Structure

The 2012A 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 Port District, and the Authority. The leased property remains the 1998 expanded portion of the Convention Center (the "Leased Property"), which is the same property that was built relying on the 1998A bond proceeds and leased under the 1998A Convention Center Bonds.

1998 Financing Leases

Under the 1998A Convention Center Bonds lease agreements, the Port District leases the Leased Property to the Authority for a nominal rent. In turn, the Authority leases the Leased Property to the City, and the City makes rental payments to the Authority annually for leasing the properties. The annual payments made by the City are equivalent to the annual debt service on the 1998A Convention Center Bonds. The Authority receives the annual rental payments from the City and assigns the payments to the trustee for the 1998A Convention Center Bonds to make principal and interest payments to bondholders.

Proposed 2012 Financing Leases

Under the proposed transaction, an Amended and Restated Expansion Lease would be executed between the Authority and the Port District for the purpose of reflecting the issuance of the 2012A Refunding Bonds and under which the Port District would continue to lease the Leased Property to the Authority. In turn, under a Convention Center Facility Lease, the Authority would sublease the Leased Property to the City. The annual lease payments made by the City would be equivalent to the annual debt service on the 2012A Refunding Bonds.

The City's obligation to make lease payments to the Authority is not debt that requires voter approval under either the City Charter or the California Constitution. It is considered a contingent obligation because it is subject to abatement, meaning that the City is not legally required to make lease payments unless it has use and occupancy of the Leased Property. The City is required to budget and make lease payments from any general funds legally available to it, but the requirement to make lease payments is not one for which the City is obligated to levy or pledge any form of taxation.

Similar to the approval required for the 1998 Convention Center Bonds, the Board of Port Commissioners must approve the Amended and Restated Expansion Lease.

C. Leased Property

The Leased Property--the expanded portion of the Convention Center--is being appraised for current market value through an appraisal performed by an outside firm retained by the Real Estate Assets Department. An updated appraised value is needed to establish the annual fair rental value of the facility for the purpose of the refunding. As legally required under the lease financing structure, the maximum annual rent payable by the City (equal to the debt service payments on the 2012A Refunding Bonds) cannot exceed the annual fair rental value of the Leased Property.

D. City Council Approval Process

It is recommended that City Council approve the financing legal documents included with this item for the successful pricing and closing of the economic refunding. Certain of the documents, including the leases, the indenture, and a continuing disclosure certificate, must be approved via ordinance, and are subject to a 30 day referendum period. The Preliminary Official Statement (POS) for the transaction will be reviewed by the Disclosure Practices Working Group, and then docketed separately to be authorized via resolution in early May. This timing would ensure the POS is current, and approved by City Council closer to the date the POS will be released to the market.

E. Financing Legal Documents

The financing documents that would be approved through the requested actions include:

1. Amended and Restated Expansion Lease – The Amended and Restated Expansion Lease is an agreement between the Port District and the Authority under which the Port District leases the Leased Property to the Authority. The Board of Port Commissioners is expected to approve the Amended and Restated Expansion Lease in early May 2012.

2. Convention Center Facility Lease – The Convention Center Facility Lease is the agreement between the City and the Authority under which the Authority subleases the Leased Property to the City, and the City agrees to make base rental payments sufficient to pay debt service on the 2012A Refunding Bonds. The agreement contains certain covenants of the City, including that it will take the necessary action to include all lease payments due under the lease in the City's operating budget each year.

3. Indenture – The Indenture is an agreement between the Authority and the Trustee for the 2012A Refunding Bonds. The Indenture provides for the issuance of the 2012A Refunding Bonds, and includes information regarding the amount of the bonds, the maturities and interest rates on the bonds, the use of bond proceeds, and the nature of the security for the bonds (i.e., that the bonds are limited obligations of the Authority payable from lease payments made by the City under the Convention Center Facility Lease). The Indenture also sets forth the specific rights, responsibilities, and obligations of each party with respect to the issuance of the 2012A Refunding Bonds. Under the Indenture, the Authority assigns its rights to receive lease payments under the Convention Center Facility Lease to the Trustee to make payments to bondholders.

4. Bond Purchase Agreement – The Bond Purchase Agreement ("BPA") is an agreement among the City, the Authority, and the Underwriters for the transaction pursuant to which the Authority agrees to sell, and the Underwriters agree to buy, the 2012A Refunding Bonds. It specifies the purchase price of the bonds, and certain terms of the bonds, such as interest rates and maturities. The agreement also specifies documents that the parties must receive prior to bond closing, including the Bond Counsel opinion regarding the validity and tax exempt nature of the bonds as well as certain opinions and certificates of the City Attorney and other City and Authority officials. Such opinions and certificates would confirm, among other things, that all steps necessary to authorize the execution of the financing documents and the issuance of the bonds have been properly taken.

5. Continuing Disclosure Certificate – The Continuing Disclosure Certificate ("CDC") details the City's ongoing obligation to file annual reports and material events with the Municipal Securities Rulemaking Board through its Electronic Municipal Market Access system for the benefit of the 2012A Refunding Bonds bondholders.

F. Financing Time-Line

The targeted time-line for the key financing milestones is provided below.

March 20, 2012	Introduction of the Financing Ordinance authorizing the issuance of the bonds, and related Financing Documents
April 10, 2012	Approval of the Financing Ordinance and Financing Documents
May 7/8, 2012	Approval of the POS via Resolution
May 9-11, 2012	Authority meeting to approve the 2012A Refunding Bonds
Week of May 21, 2012	Pricing and execution of the Bond Purchase Agreement
June 6, 2012	Bond Closing

G. Financing Team

The selection of the core Financing Team for the transaction was originally completed in 2010 and has been maintained for this transaction. The City's Financing Team for the 2012A Refunding Bonds consists of staff of the Department of Finance, including staff of the Debt Management Department, the Comptroller's Office, and the Financial Management Department. The Financing Team also includes staff of the City Attorney's Office, the Real Estate Assets Department, and the Risk Management Department. Outside consultants include: KNN Public Finance ("KNN") as the financial advisor; Squire Sanders (US) LLP as Bond and Disclosure Counsel; Nixon Peabody LLP as Underwriter's Counsel; Bank of New York Trust Company as Trustee; Chicago Title Company as title insurance provider; and DF Davis Real Estate, Inc. as appraiser.

KNN is selected to provide financial advisory services for this transaction from the City's As-needed Financial Advisors List based on the firm's experience in General Fund lease revenue bond financings and the fee estimate. The fee to KNN for this issuance, which is contingent upon the successful closing of the 2012A Refunding Bonds, is for an amount not to exceed $50,000, plus out of pocket expenses not to exceed $5,000.

The City Attorney's Office selected Squire Sanders (US) LLP ("Squire Sanders") to serve as bond and disclosure counsel for the transaction. Squire Sanders proposed to provide such services for a fee in an amount not to exceed $130,000. Expenses are not to exceed $6,900. The bond counsel fee is contingent upon the successful closing of the 2012A Refunding Bonds.

The Bank of New York Trust Company will serve as the trustee for the 2012A Refunding Bonds. Compensation for the Trustee includes $1,700 for the transaction and ongoing annual fees of $700.

Underwriting Syndicate

Stone & Youngberg LLC was identified as the Book Running Senior Manager for the 2012A Refunding Bonds through a competitive process. Requests for Proposals for the refunding of the 1998A Convention Center Bonds and other eligible General Fund bonds were issued in September 2009. In total, 22 underwriting proposals were received of which 15 firms proposed to serve as a Senior Manager or Co-Manager and seven firms proposed solely as a Co-Manager. Barclays Capital, Inc. was selected to serve as Co-Senior Manager. The Co-Managers identified for the transaction are Southwest Securities, Inc. and Loop Capital Markets LLC. (Purchasing & Contracting is in the process of finalizing the engagement of the Co-Managers.) The syndicate members were identified based on the investment banking experience of the firms on similar transactions, capacity to underwrite the transaction, and marketing outreach capabilities.

FISCAL CONSIDERATIONS:

A. Estimated Sources and Uses of Bond Proceeds (preliminary and subject to change)

Based on current market conditions as of March 2, 2012, the par amount of the 2012A Refunding Bonds would be approximately $142.4 million. This amount, in addition to a net original issue premium, would provide sufficient funds to execute the refunding and pay costs of issuance (see Attachment 1 for additional detail on costs of issuance). The following table provides a breakdown of the estimated sources and uses of funds.

Estimated Sources and Uses of Funds

Estimated Sources	
Par amount of 2012A Refunding Bonds	$142,395,000
Original Issue Premium[(1)]	11,555,757
Total Proceeds	**$153,950,757**
Estimated Uses	
Deposit to Refund 1998A Convention Center Bonds[(2)]	$152,650,948
Costs of Issuance[(3)]	1,297,263
Additional Proceeds Due to Rounding	2,546
Total Uses of Funds	**$153,950,757**

(1) Original issue premium is a bond structure feature, which results from premium couponing of the bonds and is driven by investor preference.

(2) Reflects outstanding principal to be defeased ($150,720,000), and accrued interest to the defeasance date ($1,930,948).

(3) Costs of Issuance include bond and disclosure counsel fees, financial advisor fees, underwriter's discount, City staff costs, and other expenses related to the issuance.

B. Interest Rate and Projected Lease Payments

Under current market conditions as of March 2, 2012, the estimated True Interest Cost for the 2012A Refunding Bonds is approximately 3.89%. The estimated annual lease payments due on the 2012A Refunding Bonds would be approximately $12.9 million over a 16 year period, compared to $13.7 million for the existing bonds being refunded. This will generate average annual cash flow savings of approximately $790,000 in Fiscal Years 2013 - 2028. The net present value savings achieved through the refunding is expected to be approximatley $9.7 million or 6.42% of refunded debt.
As set forth in the Financing Ordinance, refunding bonds would only be issued if a net present value savings level of at least 3.00% is achieved.

Attachment 2 provides the Lease Payment Schedule for the 2012A Refunding Bonds.

C. Source of Bond Repayment Similar to the 1998A Convention Center Bonds, the 2012A Refunding Bonds will be payable from the General Fund. The Port District also provides $4.5 million annually through 2014 under the Support Agreement between the City and the Port District dated September 17, 1998. Annual debt service/lease payments for the 1998A Convention Center Bonds are currently budgeted in the Convention Center Expansion – Administration Fund. If an economic refunding occurs as currently anticipated, the expected lower lease payments will result in annual savings to the General Fund in Fiscal Years 2013 - 2028.

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. Since the bonds can now be fully refunded and the plan of finance has changed, on February 29, 2012, Debt Management presented a report to the Budget and Finance Committee on Bond Refundings, including the Proposed 2012A Refunding Bonds, and the committee took action to forward the refunding transaction to City Council for consideration and approval.

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS:

N/A

KEY STAKEHOLDERS AND PROJECTED IMPACTS:

Business entities involved in this transaction are: Stone & Youngberg LLC (Underwriter - Book Runner Senior Manager); Barclays Capital, Inc. (Underwriter - Co-Senior Manager); Southwest Securities, Inc. and Loop Capital Markets LLC (Co-Managers) (Purchasing & Contracting is in the process of finalizing the engagement of the Co-Managers); Squire, Sanders (US) LLP (Bond and Disclosure Counsel); Nixon Peabody LLP (Underwriter's Counsel); Bank of New York Trust Company, N.A. (Trustee); KNN Public Finance (Financial Advisor); Chicago Title Company (title insurance); and DF Davis Real Estate, Inc. (appraisal).

Lakshmi Kommi
Debt Management Director

Jay M. Goldstone
Chief Operating Officer

Attachments:

1. Costs of Issuance Budget
2. Debt Service Comparison

Attachment 1

2012A RefundingBonds - Estimated Costs of Issuance (COI)

Description	Firm		Budget
Bond & Disclosure Counsel	Squire Sanders (US) LLP	$	136,900
Financial Advisor	KNN Public Finance		55,000
Trustee/EscrowAgent	Bank of New York		1,700
Title Insurance Policy	Chicago Title Co.		71,000
PropertyAppraisal	DF Davis Real Estate Inc.		6,500
Rating Agencies	TBD		187,000
State Reporting	CDIAC		3,000
Electronic Posting of Official Statement	Elabra and City		1,000
Reimbursementfor City Labor Costs	City		123,500
	subtotal		585,600
	Contingency(5%)		29,400
	Total COI Budget	$	615,000
	Underwriter's Discount	$	681,763
	(Estimated) Costs of Issuance	**$**	**1,296,763**

Attachment 2

Debt Service Comparison
Economic Refunding (1998 Convention Center Expansion)

FISCAL YEAR	Existing Total Lease Payments[1]	Estimated New Lease Payments[2]	Estimated Lease Payment Savings
2013	$ 13,697,275.00	$ 12,900,298.96	$ 796,976.04
2014	$ 13,697,325.00	$ 12,897,975.00	$ 799,350.00
2015	$ 13,699,787.50	$ 12,900,875.00	$ 798,912.50
2016	$ 13,698,612.50	$ 12,903,925.00	$ 794,687.50
2017	$ 13,698,012.50	$ 12,898,525.00	$ 799,487.50
2018	$ 13,696,300.00	$ 12,897,125.00	$ 799,175.00
2019	$ 13,701,062.50	$ 12,906,250.00	$ 794,812.50
2020	$ 13,696,850.00	$ 12,900,000.00	$ 796,850.00
2021	$ 13,698,400.00	$ 12,899,250.00	$ 799,150.00
2022	$ 13,699,525.00	$ 12,902,750.00	$ 796,775.00
2023	$ 13,699,275.00	$ 12,904,250.00	$ 795,025.00
2024	$ 13,696,700.00	$ 12,897,750.00	$ 798,950.00
2025	$ 13,700,850.00	$ 12,902,500.00	$ 798,350.00
2026	$ 13,700,300.00	$ 12,901,750.00	$ 798,550.00
2027	$ 13,699,100.00	$ 12,904,500.00	$ 794,600.00
2028	$ 13,696,062.50	$ 12,899,250.00	$ 796,812.50
Total	**$ 219,175,437.50**	**$ 206,416,973.96**	**$ 12,758,463.54**

(1) Existing Lease Payments for the 1998A Convention Center Bonds

(2) Estimated refunding lease payment schedule based on rates as of March 2, 2012