



THE CITY OF SAN DIEGO  
**REPORT TO THE CITY COUNCIL**

DATE ISSUED: April 6, 2015 REPORT NO: 15-027

ATTENTION: Council President and City Council

SUBJECT: Community Facilities District No. 2 (Santaluz) Improvement Area No. 3 Special Tax Refunding Bonds, Series 2015 and Community Facilities District No. 2 (Santaluz) Improvement Area No. 4 Special Tax Refunding Bonds, Series 2015

REFERENCE: Budget and Government Efficiency Committee Report No. 15-006, titled Economic Bond Refunding Opportunities – General Fund, Sewer Utility Fund, and Community Facilities District Credits, dated January 16, 2015

REQUESTED ACTION(S):

- 1 Authorize the issuance of the Community Facilities District No. 2 (Santaluz) Improvement Area No. 3 Special Tax Refunding Bonds, Series 2015 in a principal amount not to exceed \$3.6 million, and the execution of related financing documents to refund the Community Facilities District No. 2 (Santaluz) Improvement Area No. 3 Special Tax Bonds Series B of 2000. The related financing documents include a Bond Indenture, a Bond Purchase Agreement, a Preliminary Official Statement, and a Continuing Disclosure Certificate. In addition, authorize the City Attorney to retain and enter into an agreement with Norton Rose Fulbright US LLP to provide Bond and Disclosure Counsel services in connection with the issuance.
- 2 Authorize the issuance of the Community Facilities District No. 2 (Santaluz) Improvement Area No. 4 Special Tax Refunding Bonds, Series 2015 in a principal amount not to exceed \$7.0 million, and the execution of related financing documents to refund the Community Facilities District No. 2 (Santaluz) Improvement Area No. 4 Special Tax Bonds Series A of 2004. The related financing documents include a Bond Indenture, a Bond Purchase Agreement, a Preliminary Official Statement, and a Continuing Disclosure Certificate. In addition, authorize the City Attorney to retain and enter into an agreement with Norton Rose Fulbright US LLP to provide Bond and Disclosure Counsel services in connection with the issuance.

STAFF RECOMMENDATION:

Approve the requested actions.

## **SUMMARY:**

### **I. Background**

The Mello-Roos Community Facilities Act of 1982 (the “Mello-Roos Act”) was enacted by the State of California to help growing areas finance essential public infrastructure that typically accompanies major development projects. The Mello-Roos Act provides for the establishment of a Community Facilities District (“CFD”) for the purpose of financing certain public improvements and/or services. The City’s Council Policy 800-03, which was in effect at the time Community Facilities District No. 2 (Santaluz) was formed, allowed for utilization of CFDs to finance public facilities required in connection with development.

In accordance with the Mello-Roos Act and the Council Policy, following public hearings and special elections held in March of 2000 and February of 2004, the City Council adopted the necessary resolutions and ordinances to form Community Facilities District No. 2 (Santaluz) (“CFD No. 2” or “District”) and establish Improvement Areas No. 3 and No. 4 therein (“IA 3” and “IA 4”). Subsequently, the District issued CFD No. 2 (Santaluz) Improvement Area No. 3 Special Tax Bonds Series B of 2000 (“2000 Special Tax Bonds”) in the amount of \$4.4 million in October of 2000, and CFD No. 2 (Santaluz) Improvement Area No. 4 Special Tax Bonds Series A of 2004 (“2004 Special Tax Bonds”) in the amount of \$10.0 million in February of 2004. The bonds were issued to fund public infrastructure facilities within or serving the District, including street improvements, water and sewer facilities, and regional park improvements.

The 2000 Special Tax Bonds and 2004 Special Tax Bonds are secured solely by Special Taxes levied via property tax bills upon 317 parcels of primarily residential property located within IA 3 (94 parcels) and IA 4 (223 parcels), respectively. Currently, \$3.4 million of 2000 Special Tax Bonds remain outstanding, and \$6.6 million of 2004 Special Tax Bonds remain outstanding. Both series of bonds are eligible to be called on September 1, 2015, and the proposed issuances would fully refund all outstanding bonds.

### **II. Discussion**

#### **A. Financing Plan Summary**

A separate series of bonds (the “IA 3 Refunding Bonds” and the “IA 4 Refunding Bonds”) would be issued to refund each of the respective existing transactions. This is due to the independent nature of the improvement areas, including their formations and Rate and Method of Apportionments (taxing formula established at the time of formation). A summary of the key elements of the financing plans (which are similar for both series of bonds) is provided below. Additional detail is provided following the summary.

- **Issuer:** CFD No. 2 (Santaluz)
- **Not to Exceed Amount:** CFD 2 IA 3: \$3.6 million; CFD 2 IA 4: \$7.0 million

- **Method of Sale:** Public Offering; Negotiated Sale. With a negotiated sale, the underwriter is selected early in the financing process. This gives the underwriter adequate time to pre-market the bonds to appropriate investors.
- **Legal Structure:** Mello-Roos Act Special Tax Bonds issued under an Indenture.
- **Tax Status:** Tax-exempt bonds.
- **Repayment Source:** Payable from Special Taxes levied on taxable property within the respective District Improvement Area. No funds of the General Fund are pledged to repayment of the refunding bonds.
- **Debt Service Reserve Fund:** Similar to the existing bonds, a full debt service reserve fund sized approximately equal to the maximum annual debt service will be established for each bond series. A debt service reserve fund is an important element of most CFD bonds because the security for repayment is limited to the Special Taxes levied on property within the district.
- **Final Maturity:** The final maturity for each series will remain the same as the respective current transaction: CFD 2 IA 3 Refunding: 15-year term (through September 1, 2030); CFD 2 IA 4 Refunding: 18-year term (through September 1, 2033).

## **B. Legal Structure**

The CFD 2 IA 3 and IA 4 Refunding Bonds would be Special Tax Bonds issued pursuant to the Mello-Roos Act. CFD No. 2 (Santaluz) is a separate legally constituted public entity formed under the Mello Roos Act, and the City Council, as the public entity that created the District, sits as the legislative body of the District. Under the Mello-Roos Act, the District has the authority to issue Special Tax Bonds and levy a Special Tax to repay the bonds. The bonds would be limited obligations of the District, secured by Special Taxes levied upon property within the District. CFD Special Tax Bonds are not fiscal obligations of the City; therefore, no City taxes or revenues are pledged to the repayment of the bonds.

## **C. City Council Authorization**

The City Council is requested to (i) authorize the issuance of CFD 2 IA 3 Refunding Bonds and CFD 2 IA 4 Refunding Bonds (ii) approve the respective financing and legal documents; and (iii) authorize the City Attorney to appoint the Bond and Disclosure Counsel for the refundings. The financing documents for each series of refunding bonds include a Bond Indenture, a Bond Purchase Agreement, a Continuing Disclosure Certificate, and a Preliminary Official Statement.

### Financing & Legal Documents

The Financing Resolutions approve the issuances and authorize the execution of the following financing documents:

1. Form of Indenture (Indenture) – The Indenture is an agreement between the District and the Trustee for the bonds. The Indenture provides for the issuance of the bonds, and includes information regarding the amount of 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 District payable from Special Tax receipts). The Indenture also sets forth terms, including the specific rights, responsibilities, and obligations of each party with respect to the issuance of the bonds. Under the Indenture, the District covenants to levy sufficient Special Taxes annually to make principal and interest payments on the bonds, and to punctually transfer the Special Tax receipts apportioned to the respective Improvement Area of the District to the trustee for the benefit of bondholders.
2. Form of Bond Purchase Agreement (BPA) – The BPA is an agreement between the District and the Underwriter for the transaction pursuant to which the District agrees to sell, and the Underwriter agrees to buy, the bonds. It specifies the purchase price of the bonds, and 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 District 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.
3. Form of Preliminary Official Statement (POS) – The POS describes the bond issue to potential investors. It provides information that a reasonable investor in these types of securities would need to make an informed investment decision. Specifically, the POS includes information about the Refunding Bonds, sources of repayment of the Refunding Bonds, respective Improvement Area of the District, development status, and property ownership.

The POS also includes information on risk factors. Land based securities are generally considered more risky than securities backed by a governmental entity such as the City. For example, a downturn in the economy or a natural disaster could result in a reduction in property values and could adversely affect the ability or willingness of property owners to pay the Special Taxes, which are the security for repayment of the Refunding Bonds.

Appendices to the POS include: A copy of the Rate and Method of Apportionment (Appendix A); supplemental economic information relating to the City (Appendix B); a summary of the Bond Indenture (Appendix C); the Continuing Disclosure Certificate of the District (Appendix D); the form of Bond Counsel Opinion (Appendix E); and information concerning the Depository Trust Company's book entry only system (Appendix F).

Each POS has been reviewed by the Disclosure Practices Working Group, which has approved forwarding the document to City Council for consideration.

4. Form of Continuing Disclosure Certificate (CDC) – The CDC details the District’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 bondholders.

#### **D. Financing Timeline**

Following are the critical milestones related to the execution of the the CFD 2 IA 3 and IA 4 Refunding Bonds:

April 2015	Approval of the Financing Resolutions authorizing the issuance of the CFD 2 IA 3 and IA 4 refundings, and approval of the respective disclosure (POS) and financing documents
Mid-May 2015	Pricings
Mid-June 2015	Bond Closings

#### **E. Financing Team**

The City’s Financing Team for the refundings consists of staff of the Department of Finance, including the Chief Financial Officer and staff of the Debt Management Department, the Comptroller’s Office, and the Treasurer’s Office. The Financing Team also includes the City Attorney’s Office. External members include: Fieldman Rolapp & Associates (“Fieldman”) as the financial advisor; Norton Rose Fulbright US LLP as Bond and Disclosure Counsel; Willdan Financial Services (“Willdan”) as Special Tax Consultant; Stifel, Nicolaus & Company, Incorporated (“Stifel”) as Underwriter; MUFG Union Bank, N.A. as Trustee; and Causey Demgen & Moore P.C. as Verification Agent.

Financial Advisor: Fieldman was selected to provide financial advisory services for the transaction through a competitive process utilizing the City’s As-needed Financial Advisors Pool based on the firm’s experience in land-secured bond financings and the fee proposal. The fee to Fieldman is for an amount not to exceed \$23,500, plus out of pocket expenses not to exceed \$200 for each issuance.

Bond and Disclosure Counsel: The City Attorney’s Office identified, via a RFP process, Norton Rose Fulbright US LLP to serve as Bond and Disclosure Counsel for the CFD 2 IA 3 and IA 4 refundings. The fee is an amount not to exceed \$60,000 inclusive of reasonable out of pocket expenses for each issuance.

Special Tax Consultant: Willdan is the City’s current CFD Administrator/Special Tax Consultant and will provide Special Tax Consultant services for the new refunding issuances. The fee to Willdan is for an amount not to exceed \$9,500, plus out of pocket expenses not to exceed \$1,000 for each issuance.

Underwriter: Stifel was selected to serve as the sole Underwriter for the issuances through a competitive process utilizing the City’s established Pool of Underwriters. The firm has

significant investment banking services experience in CFD transactions and bond marketing outreach capabilities.

Trustee: MUFG Union Bank, the existing trustee for the 2000 Special Tax Bonds and 2004 Special Tax Bonds, will continue to serve as the Trustee for the new refunding issuances. Compensation for the Trustee for each issuance includes \$2,950 for the transaction and ongoing annual fees of \$1,950.

Verification Agent: Causey Demgen & Moore P.C. was selected via a competitive process. Compensation for the Verification Agent is not to exceed \$1,750.

The fees payable to the above consultants are contingent on the closing of the bonds and will be paid out of bond proceeds for each issuance.

**FISCAL CONSIDERATIONS:**

**A. CFD 2 IA 3 Refunding - Estimated Sources & Uses of Funds and Debt Service Savings**

Based on current market conditions, the proposed CFD 2 IA 3 Refunding Bonds issuance is anticipated to total approximately \$3.4 million to execute a full refunding of the 2000 Special Tax Bonds. The table below specifies the estimated sources and uses of funds for the proposed transaction:

**Estimated Sources & Uses of Funds\***

**Estimated Sources**

Bond Proceeds	\$	3,382,000
Release of 2000 Bonds Debt Service Reserve Fund		340,000
Additional Available District Funds <sup>1</sup>		<u>233,000</u>
<b>Total Proceeds</b>	<b>\$</b>	<b><u>3,955,000</u></b>

**Estimated Uses**

Escrow Fund Deposit to Refund 2000 Bonds <sup>2</sup>	\$	3,453,000
Refunding Bonds Debt Service Reserve Fund		299,000
Costs of Issuance <sup>3</sup>		<u>203,000</u>
<b>Total Uses of Funds</b>	<b>\$</b>	<b><u>3,955,000</u></b>

\* Preliminary; subject to change. Based on interest rates as of March 2015.

<sup>1</sup> Projected Additional Available District Funds includes Special Taxes collected in Fiscal Year 2015 to pay the September 1, 2015 debt service due on the 2000 Special Tax Bonds and other available District funds.

<sup>2</sup> Includes debt service on the 2000 Special Tax Bonds through the September 1, 2015 call date and the redemption of remaining principal on that date.

<sup>3</sup> Costs of Issuance include legal fees, special tax consultant fees, financial advisor fees, underwriter's discount, City staff costs, and other expenses related to the issuance of the bonds.

The estimated All-in True Interest Cost (All-in TIC) on the CFD 2 IA 3 Refunding Bonds, based on current market conditions, is approximately 4.19%. The estimated annual debt service payments due on the CFD 2 IA 3 Refunding Bonds would be \$292,000 compared to \$335,000

for the existing bonds, which translates into annual savings of approximately \$43,000 through the term of the bonds (Fiscal Years 2016-2030). The net present value (“NPV”) savings level for the refunding, including costs of issuance, is \$459,000 in aggregate, or approximately 13.7% expressed as a percentage of the bonds refunded. The refunding bonds will only be issued if a NPV savings level of at least 3.0% is achieved, in accordance with the City’s Debt Policy and the docketed Financing Resolution for the CFD 2 IA 3 Refunding Bonds. The following table provides a financing comparison between the Series 2000 Bonds and the proposed CFD 2 IA 3 Refunding Bonds.

	<b>CFD 2 IA 3 Series 2000 Existing Bonds</b>	<b>CFD 2 IA 3 Series 2015 Refunding Bonds</b>
Bond Proceeds	\$4.4 million	\$3.4 million
Average Annual Debt Service	\$335,000	\$292,000
Final Maturity	September 2030	September 2030
Total Debt Service <sup>(1)</sup>	\$5.0 million	\$4.4 million

<sup>(1)</sup> For the 2000 Special Tax Bonds, the Total Debt Service figure reflects the amount remaining following the payment of debt service due September 1, 2015

**B. CFD 2 IA 4 Refunding - Estimated Sources & Uses of Funds and Debt Service Savings**

Based on current market conditions, the proposed CFD 2 IA 4 Refunding Bonds issuance is anticipated to total approximately \$6.5 million to execute a full refunding of the 2004 Special Tax Bonds. The table below specifies the estimated sources and uses of funds for the proposed transaction:

**Estimated Sources & Uses of Funds\***

**Estimated Sources**

Bond Proceeds	\$ 6,475,000
Release of 2004 Bonds Debt Service Reserve Fund	576,000
Additional Available District Funds <sup>(1)</sup>	<u>484,000</u>
<b>Total Proceeds</b>	<b>\$ 7,535,000</b>

**Estimated Uses**

Escrow Fund Deposit to Refund 2004 Bonds <sup>(2)</sup>	\$ 6,813,000
Refunding Bonds Debt Service Reserve Fund	508,000
Costs of Issuance <sup>(3)</sup>	<u>214,000</u>
<b>Total Uses of Funds</b>	<b>\$ 7,535,000</b>

\* Preliminary; subject to change. Based on interest rates as of March 2015.

<sup>1</sup> Projected Additional Available District Funds includes Special Taxes collected in Fiscal Year 2015 to pay the September 1, 2015 debt service due on the 2004 Special Tax Bonds and other available District funds.

<sup>2</sup> Includes debt service on the 2004 Special Tax Bonds through the September 1, 2015 call date, and the redemption of remaining principal on that date.

<sup>3</sup> Costs of Issuance include legal fees, special tax consultant fees, financial advisor fees, underwriter’s discount, City staff costs, and other expenses related to the issuance of the bonds.

The estimated All-in True Interest Cost (All-in TIC) on the CFD 2 IA 4 Refunding Bonds, based on current market conditions, is approximately 4.03%. The estimated annual debt service payments due on the CFD 2 IA 4 Refunding Bonds would be \$500,000 compared to \$568,000 for the existing bonds, which translates into annual savings of approximately \$68,000 through the term of the bonds (Fiscal Years 2016-2033). The net present value (“NPV”) savings level for the refunding, including costs incurred for the refunding, is \$735,000 in aggregate, or approximately 11.1% expressed as a percentage of the bonds refunded. The bonds will only be issued if a NPV savings level of at least 3.0% is achieved, in accordance with the City’s Debt Policy and the docketed Financing Resolution for the CFD 2 IA 4 Refunding Bonds. The following table provides a financing comparison between the Series 2004 Special Tax Bonds and the proposed CFD 2 IA 4 Refunding Bonds.

	<b>CFD 2 IA 4 Series 2004 Existing Bonds</b>	<b>CFD 2 IA 4 Series 2015 Refunding Bonds</b>
Bond Proceeds	\$9.9 million	\$6.5 million
Average Annual Debt Service	\$568,000	\$500,000
Final Maturity	September 2033	September 2033
Total Debt Service <sup>(1)</sup>	\$10.2 million	\$9.0 million

<sup>(1)</sup> For the 2004 Special Tax Bonds, the Total Debt Service figure reflects the amount remaining following the payment of debt service due September 1, 2015

**PREVIOUS CITY COUNCIL ACTIONS:**

On January 28, 2015, Debt Management presented four proposed economic refunding items to the Budget and Government Efficiency Committee, of which two were the CFD 2 IA 3 Refunding Bonds and CFD 2 IA 4 Refunding Bonds. The Budget and Government Efficiency Committee forwarded the CFD 2 IA 3 Refunding Bonds and CFD 2 IA 4 Refunding Bonds to the City Council for approval.

**COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS:**

Not applicable.

**KEY STAKEHOLDERS AND PROJECTED IMPACTS:**

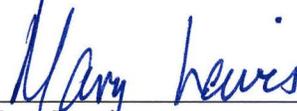
Key stakeholders include the Special Taxpayers in CFD No. 2 (Santaluz) Improvement Area No. 3 and Improvement Area No. 4 who would benefit from the refunding due to the lower debt service on the Refunding Bonds. Business entities involved in the transaction are: Norton Rose Fulbright US LLP (Bond and Disclosure Counsel); Fieldman Rolapp & Associates (Financial Advisor); Willdan Financial Services (Special Tax Consultant), Stifel, Nicolaus & Company,

Incorporated (Underwriter), MUFU Union Bank, N.A. (Trustee), Causey, Demgen & Moore P.C. (Verification Agent) and AVIA Communications (Electronic Printing of POS and OS).



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Lakshmi Kommi  
Debt Management Director



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Mary Lewis  
Chief Financial Officer