



AUGUST 27, 2009

AGENDA ITEM # 8

ISSUANCE OF SERIES 2009 A SALES TAX REVENUE BONDS; EXECUTION OF STANDBY BOND PURCHASE AGREEMENTS; AND RELATED MATTERS

Action Requested: Approve resolution to issue bonds

Key Staff: Brian Williams, Executive Director

Recommendation

Approve the attached resolution to authorize and facilitate the following:

1. Issuance of one or more series (Series 2009 Bonds) of Measure A sales tax revenue bonds in a cumulative principal amount not to exceed \$350,000,000.
2. Execution and delivery of the Indenture, Supplemental Indentures, Bond Purchase Agreements, Liquidity Facilities, Remarketing Agreements, and Official Statements required for the issuance of the Series 2009 Bonds.
3. Any other actions necessary to accomplish the foregoing.

Background

In October 2006, The STA executed three interest rate swaps of \$106.1 million each. The swaps were executed following Board adoption of the **New** Measure A Plan of Finance which identified \$318.3 million of projects to be advanced via debt financing. Of the \$318.3 million, approximately \$190 million consists of proceeds from Bond Anticipation Notes (BANs) that STA issued in 2006 and 2007 to accelerate the delivery of capital projects prior to the commencement of the 30-year **New** Measure A term. Those Notes must be refunded prior to October 1, 2009. Proceeds for the refunding, along with an additional \$128 million for capital expenditures during the first two years (FY 2010 and 2011) of the **New** Measure A term and related issuance costs, will be derived from long-term bonds to be issued in September. The objective of the interest rate swap agreements was to take advantage of prevailing low interest rates and hedge the STA against the risk of rising interest rates between 2006 and 2009 when the long-term bonds are issued.

The three swaps establish a fixed interest rate on the long-term bonds of 3.71%. The swaps become effective on October 1, 2009. In conjunction with the start date of the swaps, the Measure A Plan of Finance calls for STA to issue \$318.3 million of variable rate bonds. The fixed rate index (67% of London Interbank Offered Rate "LIBOR") received by the STA via the swaps represents the historical trading value of tax-exempt floating rate debt. It is expected to offset the floating rate paid on the long-term bonds (described below) that STA will issue in September. Since implementation of the swaps in 2006, the index has worked as intended, providing an effective hedge when compared to the tax-exempt variable rate index. In today's market, if the STA were to terminate the swaps and directly issue fixed rate debt, we would owe approximately \$11 million to each of the swap counterparties.

Discussion

As discussed with your Board at recent meetings, there is general consensus among STA's consulting financial advisors (*PFM, Inc. and The Pineapple Group*) and our banking partners that the financing strategy envisioned in the 2006 Measure A Plan of Finance is sound,

and should be pursued. As such, staff recommends that your Board authorize the issuance of \$318.3 million of variable rate demand bonds (VRDBs). VRDBs are long term, variable rate securities whose interest rate resets every week based upon investor demand. They are a commonly used bond structure. The bonds are "remarketed" each week and the rate changes each week. The weekly rate on the VRDBs is expected to match the variable rate received on the bonds thus having the fixed payer swap rate be the Authority's cost of funds. Since these bonds have a practical maturity of just one week, the associated interest rates are typically the lowest of all bond types. This strategy provides the STA the option of terminating the swaps and issuing fixed rate bonds in the future to take advantage of changing market conditions.

VRDBs are commonly held by tax exempt money market funds. To ensure that bond holders can exit the bonds on a weekly basis, a liquidity facility from a bank is required in the form of a Standby Bond Purchase Agreement (SBPA). The SBPA guarantees the investors' option to "put" the bonds every week. If the remarketing agent is unable to find a new buyer at the end of the weekly period, the liquidity bank buys and holds the bonds until a new investor(s) is identified.

STA received liquidity bids from three institutions: JP Morgan, Barclays Capital and Bank of America N.A./Merrill Lynch. Through negotiation, Authority staff and the Authority's financing team finalized the liquidity costs at approximately 117 basis points (bps) annually without any upfront fees. This represents a significant reduction in fees when compared to the initial proposals. The results of the proposal and negotiation process are presented below.

Before Negotiation				After Negotiation			
Liquidity Providers	Bank of America*	JP Morgan	Barclays	Liquidity Providers	Bank of America	JP Morgan	Barclays
Upfront Fee			25 bps	Upfront Fee			
1 year	95 bps	150 bps		1 year			115 bps
2 year	105 bps		115 bps	2 year	117 bps	117 bps	
3 year	115 bps			3 year			

**Before Negotiation: Bank of America's rates were subject to change based on other firm's fees.*

The recommended financing strategy achieves several important objectives:

- It implements the financing structure originally contemplated by the 2006 Measure A Plan of Finance, and provides for low, stable borrowing costs.
- It pays off the outstanding Bond Anticipation Notes (BANs) which come due October 1st and maximizes funds to pay for ongoing projects today. Capital projects that will benefit from the associated bond proceeds include:
 - Bradshaw Road improvements
 - Hazel Avenue improvements
 - Watt Ave/US50 interchange
 - US50 bus/carpool lanes
 - Downtown Intermodal Station
 - Sunrise Blvd improvements (in CH & RC)
 - Central Galt interchange
 - DNA Light Rail extension
 - Southline light rail extension
 - I-5/SR99/US50 Connector project
- It is based on a well established product (VRDBs) supported by a diversified group of liquidity providers with strong credit ratings.
- It provides flexibility for the Authority to terminate the interest rate swaps at any future date, refund the VRDBs in a short time frame, and convert the entire transaction to a traditional fixed rate bond structure if economically beneficial.

In order to issue municipal debt, a public agency must execute a variety of legal documents which describe the terms of the debt, the security for the debt, the covenants of the

borrower, and the events of default and remedies. STA's consulting bond counsel (Orrick) prepared the Indenture, Supplemental Indentures and Resolution (attached) associated with the proposed Series 2009 VRDBs. Consulting disclosure counsel (Nossaman) prepared the Official Statement. The Liquidity Bank counsels prepared the Standby Bond Purchase Agreements with detailed review and negotiation by Orrick.

The **Indenture** is a legal document between the STA and its trustee (Deutsche Bank) under which STA pledges the "Pledged Sales Tax Revenues" to the repayment of the Series 2009 Bonds and other Bonds to be issued by STA in the future and to the repayment of certain other obligations, including the payment of the swaps described above. The Indenture also contains the covenants of STA, events of default, and other key features of the bond program's legal structure. The **Supplemental Indenture** describes the terms of the particular Series 2009 Bonds. The **Continuing Disclosure Agreement** obligates STA to make annual filings of financial and operating information that are material to investors, as well as to provide notices of certain specified material events.

The **Official Statement** (OS) is the offering document for a municipal security. It discloses security features and economic, financial, and legal information about the issuer. The OS also includes pricing information on the Authority's bonds. The **Bond Purchase Agreement** and the **Remarketing Agreement** represent an agreement between the STA and the remarketing agents (Bank of America/Merrill Lynch, Barclays, and JP Morgan) to purchase the Series 2009 Bonds and remarket them weekly. The Bond Purchase Agreement and Remarketing Agreement have been reviewed by Bond Counsel and Disclosure Counsel on behalf of the STA, and all of these documents have received review and comment from STA's general legal counsel.

The **Standby Bond Purchase Agreements** (SBPAs) describe the terms and conditions under which the liquidity banks will purchase the Authority's bonds in the event of a failed remarketing (i.e. in a given week, no investors can be found to purchase the bonds). The SBPAs set forth specific covenants which the Authority agrees to meet as well as events of default and other detailed provisions.

At today's meeting, our consulting financial advisors will explain the advantages of the proposed VRDB financing strategy. They will also quantify the benefits, costs, and risks associated with the liquidity facilities.

Please note that the terms of certain bond documents were still being negotiated on Friday, August 21. All related documents will be compiled and distributed under separate cover.

C: PFM, Inc. – Keith Curry, Peter Shellenberger, Vrinda Shah
Pineapple Group – Mark Harris
Orrick Herrington & Sutcliffe, LLP – Mary Collins, Jenna Magan