OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

Date Issued: May 11, 2007 **IBA Report Number:** 07-51

City Council Docket Date: May 15, 2007

Item Number: 331

Subject: Redevelopment Agency Issuance of 2007 Tax Allocation Bonds

OVERVIEW

On May 15, 2007, the City Council will be asked to adopt a resolution approving the issuance of tax allocation bonds (the "Bonds") for three Redevelopment Agency (the "Agency") project areas in a principal amount not to exceed $42 million. The bond proceeds will be used to finance or refinance projects costs for the Southcrest Redevelopment Project, the Central Imperial Redevelopment Project and the Mount Hope Redevelopment Project (collectively, the "Project Areas"). The IBA has reviewed documents related to the proposed financing and offers this report to comment on elements of the contemplated bond issuance.

FISCAL/POLICY DISCUSSION

Background and Financing Objectives

The Southeastern Economic Development Corporation (SEDC) administers redevelopment activities in the Project Areas. Established in 1981, SEDC is a public benefit, non-profit corporation with responsibility for the planning, implementation and administration of four adopted redevelopment areas and one study area. SEDC has identified projects in each of the Project Areas that will require financing. The types of projects to be financed include, but are not limited to, public improvements (streetscape, infrastructure, etc.), acquisitions, commercial façade improvement loans, and low and moderate income housing. On November 29, 2006, the SEDC Board of Directors recommended approval of the proposed tax allocation bonds.

The Agency has previously issued six series of tax allocation bonds (the "Prior Agency Bonds") to finance or refinance redevelopment activities in the Project Areas. In addition to the need for new financing, SEDC has been advised that debt service savings on the

Prior Agency Bonds can be realized by refinancing four series of the outstanding bonds. The contemplated issuance of Bonds will finance identified projects in the Project Areas and refinance outstanding bonds to achieve debt service savings.

Structure of the Proposed Bonds

Although the resolution before the City Council authorizes the issuance of Bonds in a principal amount not to exceed $42 million, the Agency staff report estimates a total issuance amount of approximately $35.4 million. Of this amount, approximately $10.9 million would be used to refinance existing debt and $24.5 million would be used for new projects in the Projects Areas. Because some of the new and refinanced projects do not qualify for tax-exempt financing, the Bonds will be split into a taxable series (Series A - $17.1 million) and a tax-exempt series (Series B - $18.3 million). Taxable Series A bonds will be issued for all three Project Areas while tax-exempt Series B bonds will only be issued for the Southcrest and Central Imperial redevelopment project areas.

The Bonds will be issued on behalf of the Agency by the Public Facilities Financing Authority (the "Authority"), a joint powers authority created in 1991 by the City and the Agency to facilitate certain financings. Other financing structures could be used to issue Agency bonds; however, an Authority issuance enables the agency to utilize a "pooled" bond structure which can provide pricing and marketing advantages. Pooling the Bonds effectively blends the credit rating of the Project Areas, creates a larger offering which reduces issuance costs and may result in pricing advantages. While pooled bond issuances can sometimes adversely impact stronger credits in a pool, the larger scale benefits often outweigh these concerns.

The Bonds are obligations of the Authority and are not a debt of the City of San Diego. Debt service on the bonds is payable exclusively from tax increment generated in the Project Areas, and certain other moneys held under the respective Bond Indentures or Agency loan agreements. The Preliminary Official Statement for the Bonds informs potential purchasers that bondholders will have no recourse to the general fund of the City and that the City will have no obligation to repay the Bonds.

Factors that will Impact Bond Pricing

There are two critical factors that will impact bond pricing: the assignment of a credit rating and cost/availability of bond insurance. The Agency recently made a credit presentation to Moody's Ratings for the proposed Bonds and expects to receive a rating on May 18, 2007. Once a rating is received for the Bonds, the Agency's financial consultants will immediately solicit an insurance commitment from bond insurers. The Agency's bond underwriter has informed the IBA that they believe an insurance commitment will be received if the Bonds are assigned an investment grade credit rating by the rating agency.

If an insurance commitment is received, the underwriter will analyze the projected interest cost differential between uninsured bonds and insured bonds. The interest cost savings on the Bonds should be more than sufficient to offset the cost of the insurance premium. The Agency's staff report assumes that bond insurance is available and cost-effective. If, however, bond insurance is not available or cost-effective, the cost savings associated with the refunding portion of the bonds may have to be reevaluated or even postponed depending on the debt service savings associated with uninsured bonds.

DPWG Certification and Office of the City Attorney Memorandum

The Disclosure Practices Working Group (DPWG) has reviewed, analyzed, discussed and commented on the draft Preliminary Official Statement for the Bonds. The DPWG has issued a group certification for the Bonds indicating that, in their best judgment, the Disclosure Document is in substantially final form, the Disclosure Document contains no City financial information and that SEDC has complied with the Disclosure Controls and Procedures. On May 9, 2007, the Office of the City Attorney issued a memorandum discussing the Bonds, related Bond documents and the City Council's due diligence responsibilities. Attachment A to this memorandum provides a list of questions and answers to assist the City Council in their review of the proposed transaction. The IBA has reviewed this document and supports the City Attorney's recommendation that the City Council raise any questions they might have related to the Bonds.

CONCLUSION

The IBA is generally supportive of proposed Agency financing having reviewed some of the associated Bond documentation and having spoken with representatives from the Agency's underwriting team to better understand the proposed issuance. The IBA has been informed that the Bonds will enable the Agency to finance pending redevelopment projects / activities and realize debt service savings (estimated to be $44,000 annually). As a bond rating and bond insurance commitment have yet to be received, we note that the viability of the contemplated refinancing may need to be reevaluated and that estimated pricing levels may increase if bond insurance is not available or cost effective.

Attachment A to the City Attorney's Memorandum dated May 9, 2007 provides a list of questions for the City Council to either review or ask of the financing team for the proposed Agency Bonds. The IBA has been informed that representatives of the Agency's financing team will be present at the City Council meeting on May 15, 2007. We would encourage members of the City Council to direct any questions they might have to members of the Agency's financing team including the financial advisor, bond counsel or underwriter of the Bonds. The availability of financing consultants to the

City Council at or before City Council meetings where approval is sought for debt issuances is a component part of the comprehensive financial training program adopted by the City Council on December 6, 2006.

[SIGNED]

Jeff Kawar
Fiscal & Policy Analyst

[SIGNED]

APPROVED: Andrea Tevlin
Independent Budget Analyst