OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

Date Issued: January 12, 2007 **IBA Report Number:** 07-7

City Council Docket Date: January 16, 2007

Item Number: 332

Subject: Refunding of the Ballpark Bonds

OVERVIEW

This item requests the approval and authorization for the issuance and sale of not to exceed $172,000,000 of the Public Facilities Financing Authority's Lease Revenue Refunding Bonds, Series 2007A (Ballpark Refunding), introduction of an Ordinance approving the form of and authorizing the execution and delivery of related documents, and authorizing the City Attorney to appoint bond counsel and disclosure counsel.

FISCAL/POLICY DISCUSSION

The original Ballpark Bonds were issued in February 2002 under a Lease Revenue Bond structure by the City's Public Facilities Financing Authority, a joint powers authority between the City of San Diego and its Redevelopment Agency. Principal and interest payments on the tax-exempt bonds are paid from lease payments made by the City for use and occupancy of the Ballpark Facility. Average annual lease payments of $15.0 million are funded from Transient Occupancy Tax revenues, and are required through Fiscal Year 2032.

Interest rates on the bonds are 8.53% (true interest cost) and 7.66% (average coupon). As described in the staff report, the true interest cost accounts for the time value of money and the costs of issuance relating to the bonds, whereas the coupon rate represents amounts actually paid to the holder of a bond. Outstanding litigation at the time the bonds were issued caused legal uncertainty and triggered an increase to the interest rate which was considerably higher than comparable tax-exempt bonds issued at the time.

Staff has been working diligently to initiate the refunding of the bonds to lower the rate of interest and the annual debt service payments, since the litigation was resolved. Unfortunately, obstacles have been repeatedly encountered due to the identification of errors in the City's financial reporting and related investigations, and the suspension of the City's credit rating by Standard & Poor's.

The City's disclosure counsel and the City Attorney's Office have advised that the City's Comprehensive Annual Financial Reports ("CAFRs") should be current before the City attempts to publicly offer bonds. Because of this, a private placement is being recommended.

It is proposed that fixed rate Lease Revenue Refunding Bonds be issued, with the same lease, lease-back structure utilized for the original bonds. The refunding bonds would be insured by Ambac Assurance Corporation, and would be privately placed with Bank of America N.A. By structuring the refunding as a private placement, the City can proceed with a bond sale now, while interest rates are historically low, and can immediately obtain debt service savings, rather than wait until the City is current with its CAFRs.

Under the proposed financing, no disclosure document, or official statement, would be required. As outlined in the Purchase Agreement, Bank of America makes certain representations regarding its investment in the bonds, including, among other things, that it:

1) has such knowledge and experience in financial and business matters and that it is capable of evaluating the merits and risks of the prospective investment in the bonds
2) has conducted its own investigation into the merits and risks of its investment in the bonds and has received all information it deems necessary to make an informed investment decision
3) is purchasing the bonds for its own account or for resale to an affiliated entity
4) acknowledges that there are restrictions on the transfer of the bonds, and
5) understands that the City is not current with its CAFRs

Based upon current estimates, the par amount of the refunding bonds would be $156.4 million, with the following economic improvements anticipated:

- Estimated true interest cost and average coupon rates on the Refunding Ballpark Bonds would be approximately 4.78% and 5.23% (a reduction of 3.75% and 2.43%), respectively
- Estimated annual lease payments would be approximately $11.3 million, resulting in estimated annual savings of $3.7 million from the original $15 million payment
- Over the term of the bonds, total savings is estimated to reach $92.9 million, or $51.5 million on a net present value basis

The Mayor's Five Year Financial Outlook anticipates annual savings to the General Fund of $3.8 million for Fiscal Years 2008 through 2012, due to this refunding proposal.

Included in the proposed refunding is the ability of the City to publicly reoffer the bonds, once the CAFRs become available. For a three-year period, the City could cause the bonds to be resold or revalued in a public offering, provided the City delivers a disclosure document. Under this option, Bank of America would provide the City with a cash payment based on the improvement in the value of the refunding bonds due to the lessening of the credit spread relative to the agreed upon index. This option is a unique and creative addition to the financing documents, given the City's current financial situation, and allows the City to possibly further benefit once financial reports become current, and the City's rating situation improves. In no way does this option hinder the City's ability to again refund the bonds, if it proves economically feasible to do so, based on future market conditions.

It should be noted that documents related to the proposed financing were distributed to the City Council on December 20, 2006, which provided ample time (over three weeks) for sufficient review, in accordance with recommendations made in the Kroll Remediation Plan. The Disclosure Practices Working Group reviewed the proposed financing on December 14, 2006, and its certification was distributed to the Mayor and City Council on January 10, 2007. In addition, the City Attorney's Office has provided a comprehensive memorandum outlining the financing transaction, related documents, and the due diligence obligations of the City Council. Also included were a list of questions and answers to facilitate the City Council's review of the proposed actions. If the requested actions are approved, bond closing and receipt of funds could occur in February 2007. Anticipated debt service savings would begin in Fiscal Year 2008.

CONCLUSION

The IBA supports the approval of the actions related to the issuance and sale of not to exceed $172,000,000 of the Public Facilities Financing Authority's Lease Revenue Refunding Bonds, Series 2007A (Ballpark Refunding). Approval of these actions will allow the City to lower the rate of interest on its outstanding debt, and to experience annual debt service savings of approximately $3.7 million to the benefit of the General Fund starting in Fiscal Year 2008.

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