Agenda Report

October 22, 2018

TO: Honorable Mayor and City Council
Pasadena Public Financing Authority

THROUGH: Finance Committee

FROM: Director of Finance
PPFA Treasurer

SUBJECT: **JOINT ACTION: TAX EQUITY AND FISCAL RESPONSIBILITY ACT (TEFRA) HEARING AND ADOPTION OF RESOLUTIONS RELATED TO THE 2018 SERIES A&B ROSE BOWL REFUNDING BONDS**

RECOMMENDATIONS:

It is recommended that the City Council:

1. Find that the proposed action is not a project subject to California Environmental Quality Act (CEQA) as defined in Section 21065 of CEQA and section 15378 of the State CEQA Guidelines and, as such, no environmental document pursuant to CEQA is required for the project; and

2. Hold a TEFRA hearing, pursuant to Section 147(f) of the Internal Revenue Code of 1986, as amended (the "Code") regarding the issuance of the tax-exempt lease revenue bonds ("Tax-Exempt Bonds") by the Pasadena Public Financing Authority. Under the Code, the Tax-Exempt Bonds may qualify for tax exemption under Section 103 of the Code only if the Tax-Exempt Bonds are approved by the "applicable elected representative" of both the governmental unit issuing the Tax-Exempt Bonds or on behalf of which the Tax-Exempt Bonds are to be issued, and a governmental unit having jurisdiction over the area in which the Project is located after a public hearing held following reasonable public notice; and

3. Adopt a resolution of the City Council of the City of Pasadena approving the issuance of lease revenue refunding bonds in an amount not to exceed $50,000,000, including approval for purposes of Internal Revenue Code Section 147(f) , and the execution and delivery of a second amendment to amended and restated lease, third amendment to amended and restated sublease, purchase agreement, continuing disclosure agreement, preliminary official statement and final official statement in connection therewith, and authorizing the taking of certain other actions in connection therewith; and

4. Approve the termination of the swap with Deutsche Bank.

It is recommended that the Pasadena Public Financing Authority:

5. Hold a public hearing, pursuant to Section 6586.5(a)(2) of the Marks-Roos Local Bond Pooling Act of 1985, constituting Article 4 of Chapter 5 of Division 7 of Title 1 of the Government Code of the State of California. At the public hearing the Authority will consider whether the issuance of the bonds will provide "significant public benefits." "Significant public benefits" include, among others, demonstrable savings in effective interest rate, bond preparation, bond underwriting or bond issuance costs; and

6. Adopt a resolution of the Board of the Pasadena Public Financing Authority authorizing the issuance of lease revenue refunding bonds in an amount not to exceed $50,000,000 and the execution and delivery of a second amendment to amended and restated lease, third amendment to amended and restated sublease, purchase agreement, escrow agreement, preliminary official statement and final official statement in connection therewith, and authorizing the taking of certain other actions in connection therewith.

EXECUTIVE SUMMARY:

In 2006, the City issued its 2006 Variable Rate Demand Lease Revenue Bonds to refund prior outstanding Rose Bowl bonds and provide financing for the construction of the Rose Bowl locker rooms and media center. The City restructured the 2006 bonds and borrowed additional $30 million by the issuance of the 2013 Series A&B Variable Rate Lease Revenue Bonds (the 2013 Bonds). The 2013 Bonds were privately placed with MUFG Union Bank and have a current outstanding balance of $48.425 million with a mandatory tender date of January 2, 2019. The recommendation is to refund all of the outstanding 2013 bonds at a fixed interest rate, terminate the swap associated with the bonds, and smooth out the overall Rose Bowl debt structure without extending the maturity of the existing bonds.

BACKGROUND:

In February 2006, the Pasadena Public Financing Authority issued $47.3 million Variable Rate Demand Lease Revenue Bonds (Rose Bowl Refinancing and Improvement Project), to refinance the then outstanding 1991 and 1996 Rose Bowl Certificates of Participation ("COPs") and provide additional funds to complete improvements to the Rose Bowl stadium and City Hall. The 2006 Lease Revenue Bonds were issued as weekly variable rate demand bonds ("VRDBs"). Concurrently with the original issuance of the bonds, the City synthetically fixed the rate on the bonds by entering into an interest rate swap agreement with Deutsche Bank which requires the City to pay a fixed rate of 3.285% on the notional amount of the swap and receive 65% of London Interchange Bank Offering Rate ("LIBOR") on a like amount.

The liquidity crisis that began in late 2007 had intensified in 2008 and placed severe pressure on banks and other financial institutions. As a result, the credit capacity of many banks that were able to continue to participate in the municipal credit market was reduced. As a result, in April 2011, the City Council approved a direct purchase of the City's outstanding Lease Revenue Bonds by MUFG Union Bank, pursuant to a negotiated deal by the Director of Finance of an initial term sheet which had an expiration date in 2015.

As a result of the incremental increase in the Rose Bowl project cost, in January 2013, the City restructured and partially refunded the 2006 Bonds by issuing the 2013A (Tax-Exempt) Series in the amount of $34.9 million, and 2013B (Taxable) Series Bonds in the amount of $19.065 million. The 2013A and 2013B Bonds were also privately placed with MUFG Union Bank. The 2013A Bonds and 2013B Bonds structure extended the Rose Bowl portion of the 2006 debt to 2043 and raised an additional $30 million of new money to complete the Rose Bowl project. The un-refunded balance of $6.7 million of the 2006 Bonds was General Fund's debt and represented the financing of a portion of the City Hall renovation project.

The 2013A Bonds and 2013B Bonds originally had a mandatory tender date of January 2, 2018, and were remarketed with a new mandatory tender date of January 2, 2019. MUFG Union Bank has informed the City that it will no longer be able to privately hold the bonds and cannot extend the tender date, therefore, the City has to refund the bonds prior to their mandatory tender date of January 2, 2019.

Currently, there is $34,900,000 of 2013A (Tax-Exempt) Bonds outstanding and there is $13,525,000 of 2013B (Taxable) Bonds outstanding. At the time the 2006 variable rate bonds were issued and later partially refunded in 2013, the City concurrently entered into an interest rate swap agreement with Deutsche Bank to synthetically fix the interest rate on the bonds. As of today, $19,700,000 of the

2013A Series is hedged with a synthetically fixed rate and the balance of $15,200,000 is unhedged, all of which is being recommended for the refunding.

The current variable rate for the series 2013A Bonds is 67% of the one-month London Interbank Offered Rate (LIBOR) rate plus 0.80%. The Series 2013B Bonds has an interest rate of 2.70%. A summary of the current interest rates and terms of the 2013A and 2013B and the related swap is detailed in the chart on the following page.

	Hedged Tax-Exempt Variable Rate Bonds[1]	Unhedged Tax-Exempt Variable Bonds	Unhedged Taxable Variable Bonds
Bond Series	2013A (Tax-Exempt)	2013A (Tax-Exempt)	2013B (Taxable)
Principal Amount	$19,700,000	$15,200,000	$13,525,000
Current Interest Rate	4.130%	2.321%	2.70%
Interest Rate Reset Date	12/1/23	Resets monthly	1/3/19

[1]A portion of the 2013A Bonds are hedged with a $19,700,000 interest rate swap with Deutsche Bank.

Refunding Plan

In July 2018, the City issued a Request For Proposal (RFP) seeking underwriting services as well as lending services for private placements from various banks and underwriters. The City received eight proposals from various underwriting firms and banks. After carefully reviewing the proposals with Urban Futures Inc, the City's Municipal Advisor, Stifel and Bank of America Merrill Lynch were selected as Co-underwriters for this proposed refunding transaction.

Both the 2013A (tax-exempt) and 2013B (taxable) series are variable rate bonds. The 2013A series is partially hedged and synthetically fixed with a swap. Given the shape of the current treasury and tax-exempt yield curve, it is most advantageous to terminate the swap and refund these bonds at a fixed rate with conventional fixed rate bonds. This strategy eliminates the interest rate risk by eliminating the variable rate feature of the current financing, eliminates the risk of obtaining higher priced credit facilities, if needed, during tight credit markets, and refinances the currently synthetically fixed rate bonds at lower fixed rates therefore creating economic benefits.

In addition to the inherent risk of a rise in interest rates with variable rate debt, the termination of the swap eliminates the following risks:

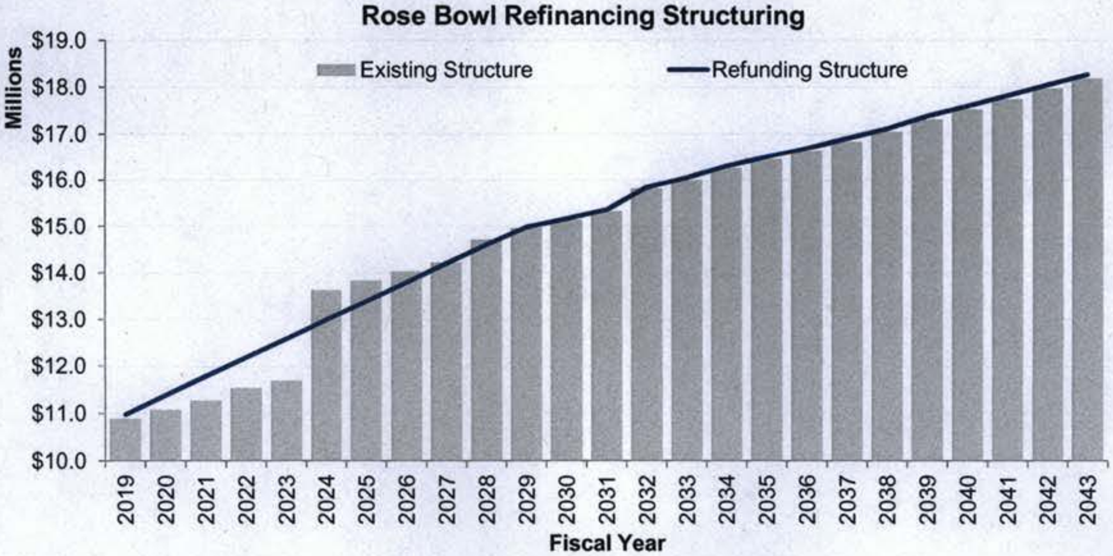
- Counterparty Risk: The risk that the swap counterparty defaults or its credit rating declines. Deutsche Bank, the swap counterparty, was downgraded to BBB+ in June 2018 by S&P and is currently rated Baa2 by Moody's.

- Tax Risk: If there is a tax law change that eliminates tax-exemption, the City could face higher interest rates. With fixed rate financing, a tax law change would not change the City's interest rates.

- Basis Risk: The City currently receives 65% of LIBOR from the swap counterparty and pays 67% of LIBOR plus 80 basis points. The difference between what the City receives and pays may grow larger depending on market conditions.

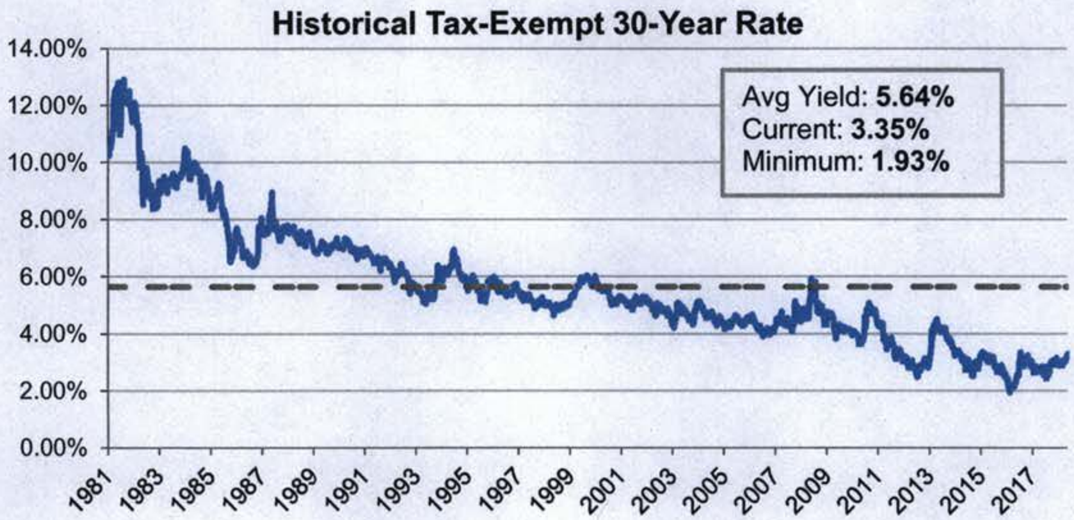
By taking advantage of low interest rates currently available in the market and the flatter yield curve, refinancing the portion of the 2013A bonds associated with the swap is projected to produce an interest rate savings of 0.30%.

The current 2013A Series will be refunded to its original term with the final payment in 2043 and the 2013B Series will be refunded to its original term with the final maturity in 2028. The amortization of the principal of the 2018B (taxable series) series will be adjusted to generate aggregate debt service payments that mitigate the current principal payment spike in 2024. The following graph depicts the current debt service schedule versus the proposed one.



As a result of the smoothing of the annual debt service by eliminating the spike in year 2024, the aggregate annual debt service amount of the Rose Bowl will increase on average by $200,000 annually in years 2020 to 2023 and decrease on average by the same amount in years 2024 through 2027. The attached Table A and B illustrate the existing debt service versus the expected debt service after refunding.

With further Fed Funds hikes almost certain for the next meeting, variable rates (short-term rates) will continue to rise. Current long-term interest rates remain relatively close to historic lows as a result of flat yield curve and low supply of municipal tax-exempt issuance.



This report was presented to the Rose Bowl Operating Company (RBOC) Finance Committee at its special meeting on September 21, 2018, and to the RBOC Board of Directors on October 5, 2018.

ENVIRONMENTAL ANALYSIS:

The proposed actions are governmental fiscal activities that would not cause either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment. Therefore, the proposed action is not a "project" subject to CEQA, as defined in Section 21065 of CEQA and Section 15378 of the State CEQA Guidelines. Since the action is not a project to CEQA, no environmental document is required.

FISCAL IMPACT:

The recommended refunding will not extend the current term on the bonds nor will it borrow any additional funds. Based on current market conditions as of September 5, 2018, it is anticipated that the true interest cost of the 2018A tax-exempt series will be an estimated 3.83% (25 year bonds) and the true interest cost on the taxable 2018B series will be 3.80% (10 year bonds).

All costs associated with the refunding will be incorporated and paid by the bond proceeds of the 2018 series A&B refunding bonds. Funds have already been appropriated in RBOC's Fiscal 2019 budget to pay debt service on the bonds. There is no anticipated impact to other operational programs or capital projects as a result of this action.

The swap termination cost is estimated at $750,000 to $800,000 depending on the interest rates at the time of termination. In May 2018, the City redeemed all outstanding principal of the 2006 bond issue which was issued in association with the swap. Therefore, the balance of the reserve fund associated with the 2006 bonds will be released back to the City in the amount $790,000 to satisfy the termination cost of the swap.

Respectfully submitted,

MATTHEW E. HAWKESWORTH
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PPFA Treasurer

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Approved by:

STEVE MERMELL
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PPFA Executive Director

Attachments:

1. Table A – Existing Rose Bowl Debt Service
2. Table B – Proforma Rose Bowl Debt Service (after refunding)
3. Second Amendment to Amended and Restate Lease
4. Third Amendment to Amended and Restated Sublease
5. Indenture
6. Escrow Agreement
7. Continuing Disclosure Agreement
8. Preliminary Official Statement and Appendix A
9. Bond Purchase Agreement