

RIVERSIDE PUBLIC UTILITIES

Board Memorandum

BOARD OF PUBLIC UTILITIES

DATE: JANUARY 14, 2019

ITEM NO: 16

SUBJECT: ISSUANCE OF 2019 REFUNDING WATER REVENUE BONDS

ISSUE:

Approval of the issuance of up to \$160 million of Water Revenue Bonds for purposes of refunding the previously issued 2008B Water Revenue Bonds to capture interest rate savings; terminate some or all of its Water Utility interest rate swaps and refund the associated portions of the previously issued 2011A Variable Rate Refunding Water Revenue Bonds to reduce financial risk and finance identified Water Utility capital projects. Proceeds will also be used to pay bond issuance costs.

RECOMMENDATIONS:

That the Board of Public Utilities recommend that the City Council:

1. Approve the City's Financing Team, as described herein;
2. Conduct a public hearing to consider the issuance of Refunding Water Revenue Bonds in an amount not-to-exceed \$160 million;
3. Adopt a resolution for the issuance of Refunding Water Revenue Bonds;
4. Delegate to the City's Financing Team, at the time of issuance, the determination of specific maturities to be refunded, the amount of interest rate swaps to be terminated and the form of new bonds as outlined in Recommendation No. 3 above;
5. Authorize the City Manager, or his designee, to execute all documents related to this transaction; and
6. Upon closing of the 2019 Refunding Water Revenue Bonds, authorize the Chief Financial Officer to make the necessary budget adjustments and/or appropriations to properly record the refunding and financing expenses in accordance with governmental accounting requirements.

BACKGROUND:

2008B Water Revenue Bonds

In May 2008, the City of Riverside issued \$58,235,000 of 2008B Water Revenue Bonds to fund the Water Utility's Capital Improvement Program. The 2008B Bonds are fixed-rate bonds maturing in 2038 and have remaining coupons ranging from 4.00% to 5.00% and an outstanding principal balance of \$53,880,000.

SIFMA Indexed Variable Rate Bonds

The Water Utility currently has outstanding approximately \$50,950,000 (principal amount) of SIFMA Indexed Variable Rate Bonds in one series of revenue bonds (2011A Bonds). The variable rate bonds, in conjunction with the Water Utility's interest rate hedges (discussed below), have proven to be very effective in lowering the overall debt costs.

Interest Rate Hedge (Swap) Agreement

In addition to the low rates realized using variable rate debt, the City also executed an interest rate swap agreement in which the Water Utility receives 62.68% of LIBOR plus 12 basis points (which offsets/hedges the variable rate the Water Utility pays to its bondholders) in exchange for a fixed interest rate of 3.2%. The Financing Team recommends possibly terminating a portion of the existing hedge agreement as part of the 2019 plan of finance as discussed below.

Water Utility Capital Projects

The City Council approved a five-year Capital Improvement Program for the Water Utility totaling approximately \$129 million, of which \$95 million is projected to be funded with bond proceeds with the remaining \$34 million funded with a combination of rates, reserves and developer contributions. The Water Utility Five-Year Rate Plan, approved by City Council on May 22, 2018, supports the bond financing of the capital improvement program.

DISCUSSION:

2019 Refunding Water Revenue Bonds

The 2019 Water Utility plan of finance has three components: a refunding component to refinance the 2008B Water Revenue Bonds for debt service savings, a new money component to finance a portion of the Water Utility Capital Improvement Program, and a fixed-rate refinancing component of certain maturities of the 2011A SIFMA Indexed Variable Rate Bonds and partial termination of the associated interest rate swaps.

Refunding of Series 2008B Bonds

The 2008B Bonds, currently outstanding in the amount of \$53,880,000, are eligible to be refunded on April 1, 2019. The bond markets continue to experience historically low interest rates for tax-exempt bonds—particularly for high-grade credits such as the Water Utility (AAA/AA+). From an economic and financial viewpoint, Riverside Public Utilities (RPU) will be able to take advantage of favorable market conditions and refinance the 2008B bonds using fixed-rate bonds at a lower interest rate, generating debt service savings for the Water Utility. The refinancing will result in lower debt service than the Water Utility is currently paying on the 2008B Bonds and will not extend the current final maturity of the 2008B Bonds (2038).

New Money Component

The Water Utility plans to finance approximately \$52 million of capital projects identified in the five-year Capital Improvement Program from the proceeds of the 2019 Bonds. The new money component is expected to be amortized over a period of 30 years, consistent with traditional new money borrowing in the tax-exempt market and prior City practice, on a substantially level annual debt service basis. Level fixed-rate debt service provides for budget certainty and promotes equitable financing of projects among current and future ratepayers.

Fixed Rate Refinancing of SIFMA Indexed Variable Rate Bonds

The 2011A SIFMA Indexed Variable Rate Bonds and the associated interest rate swap have more risks than fixed rate bonds. Risks could include difficulty remarketing the 2011A Bonds on subsequent mandatory tender dates, exposure to market dislocations between the variable rate of interest paid on the 2011A Bonds and the rate received under the swap agreement, etc. SIFMA Indexed Variable Rate Bonds with a swap typically have a lower interest cost than fixed rate bonds, therefore it is uncommon to be able to refinance without increasing costs. However, RPU is currently in a unique financial market with very low tax-exempt interest rates, particularly in California, that make it possible to refinance certain maturities of the 2011A Bonds and the associated swap with fixed rate bonds at no additional cost to the Water Utility and ratepayers. This refinancing has no downside as the fixed rate bonds will have the same debt service costs (including costs of issuance and any payment to the swap counterparty necessary to terminate all or a portion of the interest rate swap) but will lower the associated risk of SIFMA Index Bonds and swaps. The swap termination payment is equal to the market value of the swap at the time the swap is terminated and will be paid to the swap counterparty (JPMorgan Chase) using proceeds from the 2019 Refunding Water Revenue Bonds, in the event the fixed-rate refinancing of SIFMA Index Bonds component of the financing plan is executed.

The 2019 Refunding Water Revenue Bonds will be issued as fixed rate bonds and the applicable interest rate swap agreement will be terminated, either in whole or in part, which will mitigate the various risk exposures. The ability to execute this component of the 2019 Plan of Finance is very market-dependent and the amount of the 2011A Bonds that can be refinanced at no cost fluctuates daily. Accordingly, the financing team will analyze and determine the best course of action and maturities to be included in the bond transaction with the goal of the SIFMA Indexed Variable Rate Bond refinancing component of the transaction remaining cost neutral, including bond issuance costs.

Financing Team

A Financing Team has been assembled, consisting of staff from the Public Utilities Department, the Finance Department, and the City Attorney's Office, with PFM Financial Advisors LLC, serving as the Municipal Advisor. This Financing Team has selected Stradling Yocca Carlson & Rauth as bond counsel and Jones Hall as disclosure counsel based on recent favorable experience and knowledge of the City's and RPU's debt resolutions and other relevant legal covenants. The Financing Team has also selected via a competitive bidding process Citigroup Global Markets Inc., and J.P. Morgan Securities LLC as underwriters to sell the bonds. These firms have participated and provided outstanding service in previous bond transactions. Additional members of the Financing Team include the City's Fiscal Agent, U.S. Bank, and a Verification Agent, which will be selected closer to the bond sale via a competitive bidding process. Fees for services will be paid from bond proceeds. Staff recommends approval of the Financing Team, as described herein.

Good Faith Estimates

On October 9, 2017, the Governor approved Senate Bill 450 (SB 450), adding Section 5852.1 to the California Government Code. SB 450 requires, prior to an issuance of bonds, a public agency to disclose in a public meeting good faith financing estimates provided by an Underwriter, Municipal Advisor or private lender. These estimates include: (1) the True Interest Cost of the bonds; (2) the total finance charge of the bonds, equal to the sum of all fees and charges paid to third parties; (3) the amount of estimated bond proceeds minus the total finance charge of the bonds, and any reserves funded from proceeds of the bonds; and (4) the total payment amount, which includes the projected sum of all payments the Water Utility will make to pay debt service on the bonds plus any portion of the finance charge of the bonds that will not be paid with the proceeds of the bonds.

The following information was obtained from PFM Financial Advisors, as Municipal Advisor, and is provided in compliance with SB 450:

1. **True Interest Cost.** Assuming a par amount of \$139,200,000 of 2019 Refunding Water Revenue Bonds is sold and based on market interest rates prevailing at the time of preparation of this information, a good faith estimate of the true interest cost of the bonds, which means the rate necessary to discount the amounts payable on the respective principal and interest payment dates to equal the purchase price received for the bonds, is 3.50%.
2. **Finance Charge.** A good faith estimate of the finance charge of the bonds, which means the sum of all fees and charges paid to third parties, is \$587,000 (exclusive of any swap termination payment) or \$5,225,000 (in the event the swap termination payment is to be construed as a component of the finance charge). If market conditions permit refinancing the SIFMA Index Bonds and associated swap termination, the swap termination payment will be paid to the swap counterparty using proceeds of the 2019 Refunding Water Revenue Bonds.
3. **Amount of Proceeds to be Received.** A good faith estimate of the amount of proceeds expected to be received for sale of the bonds less the finance charge of the bonds described in 2, above, and any reserves or capitalized interest paid or funded with proceeds of the bonds, is \$155,207,000.
4. **Total Payment Amount.** Assuming a par amount of \$139,200,000 is sold and based on market interest rates prevailing at the time of preparation of this information, a good faith estimate of the total payment amount, which means the sum total of all payments the Water Utility will make to pay debt service on the bonds plus the finance charge of the bonds described in paragraph 2, above, not paid with the proceeds of the bonds, calculated to the final maturity of the bonds, is \$235,000,000.

The foregoing information constitutes good faith estimates only. The actual interest cost, finance charges, amount of proceeds and total payment amount may vary from the estimates above due to variations from these estimates in the timing of bond sale, the amount of bonds sold and market interest rates at the time of the bond sale.

The Chief Financial Officer/Treasurer concurs with the recommendations above.

Due to the time sensitivity of the refinancing of the 2008B Bonds and the potential refinancing of 2011A Bonds, the City Council is scheduled to hear this item for consideration on January 22, 2019. If approved by the Board of Public Utilities and City Council, this schedule will allow adequate time to execute the transactions as described above.

FISCAL IMPACT:

The estimated present value savings from refunding of the 2008B Water Revenue Bonds is expected to be approximately \$7.5 million (\$10.5 million gross savings) based on market conditions in early December 2018, which will equate to an annual cash flow savings of approximately \$0.5 million per year through 2038.

The plan for swap termination/variable rate bond refunding is for the Water Utility to remain cost neutral on debt service obligations, but reduce risk factors associated with variable rate bonds and interest rate swaps by refinancing with fixed rate debt.

Annual debt service payments for the new money (capital projects) component are expected to be \$2.8 million and have been included in the approved biennial budget for Fiscal Years 2018-19 and 2019-20.

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Approved by: Todd M. Corbin, Utilities General Manager
Approved by: Al Zelinka, FAICP, City Manager
Approved as to form: Gary G. Geuss, City Attorney

Certifies availability
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Attachment(s):

1. Reimbursement Resolution No. 22849
2. Reimbursement Resolution No. 23352
3. Presentation