

NOV 12 1987



1

OFFICE OF THE  
CITY TREASURER

CITY OF SACRAMENTO  
CALIFORNIA

800 TENTH STREET  
SUITE ONE  
SACRAMENTO, CA.  
95814-2688

THOMAS P. FRIERY  
TREASURER

November 5, 1987

87167TPF/DAlv:cc87cop(b)11

DONALD E. SPERLING  
ASSISTANT TREASURER

916-449-5318  
OPERATIONS

Budget and Finance Committee  
Sacramento, California

916-449-5168  
INVESTMENTS &  
ADMINISTRATION

SUBJECT: Preliminary Approval of Financing Plan to Finance Various City  
Projects

916-448-3139  
DEX TRANSCIEVER

Honorable Members in Session:

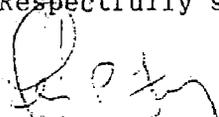
SUMMARY

Transmitted herewith is a report to the full Council recommending approval to proceed with the financing of the 1987 COP.

RECOMMENDATION

It is recommended that after hearing the attached report, the Budget and Finance Committee recommend approval to the full Council to proceed with the 1987 COP financing.

Respectfully submitted,

  
THOMAS P. FRIERY  
City Treasurer

RECOMMENDATION APPROVED:

  
JACK R. CRIST, Deputy City Manager

November 17, 1987  
All Districts



OFFICE OF THE  
CITY TREASURER

THOMAS P. FRIERY  
TREASURER

DONALD E. SPERLING  
ASSISTANT TREASURER

CITY OF SACRAMENTO  
CALIFORNIA

November 5, 1987

87167TPF/DAlv:cc87cop(b)11

800 TENTH STREET  
SUITE ONE  
SACRAMENTO, CA  
95814-2688

916-449-5318  
OPERATIONS

916-449-5168  
INVESTMENTS &  
ADMINISTRATION

916-448-3139  
DEX TRANSCEIVER

Sacramento City Council  
Sacramento, California

SUBJECT: Preliminary Approval of Financing Plan to Finance  
Various City Projects

Honorable Members in Session:

SUMMARY

City Council has previously approved numerous projects totalling \$95.2 million in the 1987/88 Capital Improvement Budget some of which will require debt financing. Staff is recommending that City Council approve a financing program that will permit the financing of projects totalling \$26,736,800.

Specifically, five of the capital projects requiring \$11,745,700 of debt financing are a Police Substation at Franklin Boulevard and Fruitridge Road, the second phase of the Public Safety System Project (PSSP), purchase of 60,000 90-gallon refuse containers, a Utility Customer Information System (UCIS), and a geographic information System (GIS/CAD Mapping).

The proposed debt financing will also provide approximately \$15 million which will be available for one or more of three projects that are currently waiting for final cost estimates or EIR approval. These projects designated as Category II projects in the Official Statement, include the purchase of land for the Community Center expansion, the East End parking garage, and/or a new animal control facility.

The decision to maximize the size of the proposed debt issue by including a Category II project was made for three reasons. First, it is believed that at least one of the Category II projects will be ready to proceed in the next 6 to 8 months. Second, it is less costly and more efficient to minimize the number of times the City goes to the financing market each year. Finally, it is the City's policy to avoid, when possible, going to market more than once a year.

Of the total cost of these projects estimated to be \$26,736,800, it is necessary to finance the entire amount through the sale of Certificates of Participation. The City Treasurer and other City staff have determined that the most efficient method of providing the required money for these projects is through a sale and lease-back of an existing City asset. For purposes of this financing, the sale/lease-back of the existing Community Center has been selected because of the amount of funds required to support the capital projects.

The need to finance these projects had previously been identified when the Capital Improvement Program was formerly adopted. It is necessary for the City Council to preliminarily approve the financing plan which includes approval of:

- legal documents associated with the financing which are in preliminary form and on file with the City Clerk, and
- the Preliminary Official Statement (POS) which is also on file with the City Clerk, and
- the financing action plan shown in Attachment A, and
- the financing team shown in Attachment B.

It is understood that City Council will make the final formal approval of all the legal documents and the Official Statements as well as the sale of the COPs when such financing occurs.

It is recommended that City Council approve the financing of a 1987 Certificates of Participation.

#### BACKGROUND

The sale and lease-back of existing municipal real property assets has emerged in recent years as an effective and efficient method to raise the money required to fund various capital projects and equipment acquisitions. Two major advantages of this method of financing are the elimination of construction risk because the structure/facility already exists and the elimination of a need to finance interest payments from bond proceeds that may be required during the time that the project is still to be constructed or acquired.

The City has issued four Certificates of Participation (COP) since 1983 which have been used to construct various City real property improvements and purchase equipment. Since the legal structure of a COP is in the form of a lease between the City and another legal entity, lease payments for the projects are paid from City funds only after the projects are complete or have been acquired. Prior to project completion, interest due to the bondholders is paid from a capitalized interest account held by the trustee that is funded from bond proceeds. Therefore, during the construction period, interest is paid from borrowed funds.

If an existing asset such as the Community Center is used as security for a lease, the City can begin making lease payments immediately because there is no construction period. Avoiding the need for capitalized interest results in a smaller issue size, lower annual debt service payments and a smaller reserve requirement. The amount of capitalized interest required varies with the type of projects financed but can represent as much as 20% of total par bonds issued.

The sale/lease-back of the Community Center was selected because of its attractiveness from an investors viewpoint, which will afford the City a maximization of bond proceeds at as favorable an interest rate as possible. A preliminary appraisal of the above property has revealed a land and structure value of \$43 million, which is sufficient to support the COP size envisioned.

The Community Center Authority currently has \$15,500,000 par bonds outstanding of the total \$19,100,000 issued in 1971. Because of existing bond covenants, if Certificates were issued with the Community Center as collateral, the new COP would be placed in a subordinate position to the prior bonds. Having a subordinate COP would in turn receive a lower rating from the rating agencies which will result in a larger borrowing cost. It is recommended that the existing \$15.5 million par bonds be defeased through an advance refunding technique with new bonds. Effectively, a portion of the bond proceeds raised in the new issue will be re-invested at their borrowing cost with the U. S. Treasury and will result in effectively no interest cost to the City for this arrangement other than the normal financing costs and expenses which should be no more than 2% of the bond issue size. In so implementing this technique, it will only be necessary to fund 6 months of capitalized interest on the City capital projects to be financed which will result in a substantial reduction in the debt service payments that ordinarily would have been made had we not advance refunded the issue.

Another advantage of defeasing existing bonds is the release of Reserve funds held with the trustee. These reserve funds have grown to 3.5 times the original reserve requirement established in 1971. This growth is the result of interest income being earned on the funds held by the Trustee which presently cannot be returned to the City. Further, bond covenants require that rental income insurance be maintained equal to 24 months of debt service. The result being that bondholders have a double guarantee of annual debt service at the expense of the City. Through the defeasance, interest income on the Reserve fund will then flow to the City.

A final advantage to issuing debt against the Community Center and not the projects being constructed is that, when complete, the projects being funded may serve as assets for future financings. In turn, future debt financings will avoid the necessity of borrowing capitalized interest. We believe this method of debt issuance is the most efficient means of financing City projects.

Throughout the process, bond counsel has been consulted to assure that such a sale/lease-back of the Community Center will not result in a future decision that the City has issued arbitrage bonds.

FINANCIAL

It is envisioned that approximately \$42,275,000 of par bonds will be sold which will yield approximately \$24,700,000 of net construction/acquisition proceeds while a total of \$2,036,800 of interest earnings will be earned on the funds held with the Trustee during the construction/acquisition period which brings the total amount of money available for the projects to \$26,736,800. Also, \$12,538,100 of proceeds will be placed in U. S. Treasury securities to defease the existing 1971 bonds. Further, six months of capitalized interest (representing the first interest payment due 6/1/88 on the bonds) will also be set aside and held by the Trustee. The sole reason for 6 months capitalized interest is to provide a cash flow advantage for the City. Finally, a reserve fund of \$4,000,000, equal to maximum annual debt service will be maintained over the life of the COP.

The 1986 Tax Reform Act placed tighter restrictions on the earning of arbitrage profits on tax-exempt bond proceeds than had existed under prior law. Accordingly, an Arbitrage Rebate Fund will be established to hold any interest earnings on bond proceeds which exceed the allowable yield on the bonds. The arbitrage-restricted rate on the bonds is determined after bonds are sold to the public. The rate is a function of the actual price a substantial number of bonds of each maturity are sold and the yield that the investor receives upon purchase of the tax-exempt bonds.

The estimated annual debt service on the COP is approximately \$4 million, which is an even annual debt service over the 25 year life of the bonds. Support for this debt service is estimated at this time to come from the following sources but will be finalized at the time that the actual projects funded from bond proceeds are identified.

General Fund	23%
* Community Center Fund	65%
Waste Removal Fund	9%
Water Fund	1%
Sewer Fund	1%
Storm Drainage Fund	1%
	<u>100%</u>

- \* This will only be accomplished if the EIR, et al are completed for the Community Center expansion and Council approved these monies to be used for property acquisition.

LEGAL DOCUMENTS

A due diligence meeting between City staff and the external consultants has been scheduled for November 18, 1987. The due diligence process is a review of all pertinent issues and documents pertaining to the issue and the City of Sacramento.

As part of the due diligence process, various legal documents have been prepared in draft form, are presently under review by appropriate City staff and will be edited and amended as appropriate. Prior to final City Council approval of the financing, such legal documents will be completed and presented to the City Council for approval.

PRELIMINARY OFFICIAL STATEMENT

A Preliminary Official Statement (POS) has been drafted and circulated to City staff for review and is on file with the City Clerk. This document will be under continual review by staff and will later be forwarded to rating agencies for review and subsequent ratings.

FINANCING TEAM

Attachment B contains the members of the financing team acting on the proposed financing.

On January 27, 1987, City Council approved an Investment Banking/Financial Advisors contract with the firms of Paine Webber, Inc., Stone & Youngberg and an unnamed third broker/dealer to serve as co-managers for City financings. Contained in the contract were the conditions that the Budget and Finance Committee and the City Council approve the financing team and such preliminary concurrence of the financing and expenses envisioned with the financing. Accordingly, the following is recommended.

- 1) The broker/dealer firm of Cranston/Prescott Securities be named as the third co-manager for this financing only (see Attachment B).
- 2) The law firms of Orrick, Herrington & Sutcliffe as well as Arnelle & Hastie be named as co-bond counsel for the financing (see Attachment B).
- 3) The law firms of Mudge Rose Guthrie Alexander & Ferdon as well as Harrison, Taylor & Bazille be named as co-underwriter's counsel (see Attachment B).

For Council information, these firms have been working with the City to date on the actions pertaining to the financing. Further, the Treasurer advises that the appointment of these firms as well as other broker/dealer firms who have been added to the selling group for this financing comply with the City's DBE/WBE requirements which have been requested by City Council to be implemented if possible when performing public financings.

FINANCING COSTS (FEES)

At this time the Financial Advisor/Investment Banking contract of the City requires preliminary Council concurrence with the financing expenses associated with the financing. However, it is pointed out that expenses relative to underwriting are conditioned upon a sale of securities. Therefore, as it pertains to expenses for underwriting, such expenses will be incurred only if a financing is accompanied. However, as it pertains to bond counsel fees, such fees are customarily paid regardless of whether a financing is completed or not.

Financing costs are generally grouped into four major categories. The categories are:

- 1) Management Fees - Such fees are paid to the underwriters for structuring the transaction.
- 2) Takedown or Sales Concessions - Such fees are paid to the sales group for marketing securities.
- 3) Underwriter's Risk - Such fee is customarily paid to the underwriter to compensate for the risk of having to market the bonds to the general public after they have made their bid to the City for the securities.
- 4) Expenses - Consider those items involved with the financing such as printing of the OS, rating agency fees, California Debt Advisory Commission charges, travel expenses, etc.

As it pertains to the 1987 COP financing issue, the following are our estimate of fees which are based on a cost of \$1,000 par value of bonds issued:

Management Fee	- \$ 3.00
Takedown (1)	13.00
Underwriter Risk	1.50
Expenses	<u>6.88</u>
Total	\$24.33
	=====

(1) Estimated for retail sales as opposed to institutional.

From the above table it is pointed out that the estimated financing costs associated with the financing are \$24.33 per \$1,000 of bonds issued. It is pointed out that these fees are in compliance with the Financial Advisors/Investment Bankers contract the City has and, further, they are reasonable in the marketplace. Finally, it is possible that there will be changes to this fee prior to the financing, but it is not envisioned such changes will be increases.

BOND COUNSEL FEES

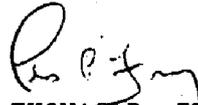
Bond counsel fees for this transaction are estimated to be \$140,000 plus expenses. However, \$110,000 of these fees are attributable to this bond issue, whereas \$30,000 is attributable to the refunding issue associated with the light rail bond issue that was recently terminated because of higher interest rates. As it pertains to the fees for this issue, these fees are competitive within the marketplace and are consistent with such for prior bond issues. Such fees also include the costs of co-bond counsel. Finally, as it pertains to the \$30,000 in fees for the terminated light rail refinancing, the costs are both appropriate and reasonable as bond counsel fees are paid irrespective of whether a financing is completed or not.

RECOMMENDATION

It is recommended that the City Council:

- 1) Preliminarily approve the financing action plan for financing the 1987 COP issue which includes:
  - Approval of the financing action plan (see Attachment A)
  - Approval of the Financing Team (see Attachment B)
  - Preliminary approval of the legal documents and POS which are on file in the City Clerk's Office (see Attachment A).

Respectfully submitted,

  
THOMAS P. FRIERY  
City Treasurer

RECOMMENDATION APPROVED:

\_\_\_\_\_  
WALTER J. SLIPE, City Manager

November 17, 1987  
All Districts

ATTACHMENT A

ACTION PLAN

CITY OF SACRAMENTO  
\$42,275,000  
1987 CERTIFICATES OF PARTICIPATION  
AS OF 10/30/87

- 11/17/87 - Budget & Finance as well as Council action on ordinance.  
- Bond Counsel to provide Appendix B to Official Statement
- 11/18/87 - Due diligence meeting with all hands to review for all documents - City Hall, Council Chambers.
- 11/21/87 - Mail Preliminary Official Statement to rating agencies and bond insurance companies.
- 11/23/87 - Decision on use of municipal bond insurance.
- 11/27/87 - Complete report on sale of COP for 12/8 Budget and Finance Committee and City Council.  
- Provide Resolution authorizing legal documents, COP Purchase Contract and approval of 1987 COP.
- 11/30-12/1 - NY trip to rating agencies.
- 12/04/87 - Credit ratings to be received from Moody's and Standard and Poor's.
- 12/05/87 - Mail Preliminary Official Statement to underwriters and Wall Street (include all preliminary supporting documents).
- 12/07/87 - City Treasurer to negotiate preliminary COP interest rate.  
- City Treasurer to prepare final report to Council describing and accepting bid.
- 12/08/87 - City Treasurer to present COP recommendation to Budget and Finance as well as Council to approve COP sale.
- 12/23/87 - All comments or changes to be made to Underwriter's Counsel to prepare final COP Official Statement.  
- COP rates to bond printer.
- 01/06/88 - Pre-Closing - Friery to San Francisco, receipt for bonds to Paine Webber.  
- Auditors comfort letter
- 01/07/88 - Closing of COP's in San Francisco, dated January 7, 1988.

ATTACHMENT B

CITY OF SACRAMENTO, CALIFORNIA  
1987 \$42,275,000 CERTIFICATES OF PARTICIPATION  
FINANCING TEAM

EXTERNAL CONSULTANTS

Co-Bond Counsel

Orrick, Herrington & Sutcliffe  
600 Montgomery St.  
San Francisco, CA 94111  
Carlo S. Fowler, Esq.  
Mary Collins, Esq.

Telex #415-773-5759  
(415) 773-5884  
(415) 773-5998

Arnelle & Hastie  
1160 Battery St., Ste. 380  
San Francisco, CA 94111-1204  
William M. Lofton, Esq.  
Michael S. Bernick

Telex #415-544-7991  
(415) 544-6864

Underwriters

PaineWebber Incorporated  
100 California Street, Suite 1200  
San Francisco, CA 94111  
Ashford D. Wood  
Vice President

Telex #415-788-3271  
(415) 954-6898

Eric T. Bischof  
Analyst

(415) 954-5997

Deborah Donnelly  
Analyst

(415) 954-5993

Stone & Youngberg  
One California St.  
San Francisco, CA 94111  
David E. Hartley  
Partner

Telex #415-397-9592  
(415) 981-1314

Cranston/Prescott Securities  
444 So. Flower St., Penthouse Ste.  
Los Angeles, CA 90071  
David Cunningham, Jr.

Telex #213-627-8480  
(213) 488-0010

James R. Bechtel  
Cranston/Prescott Securities Company  
444 South Flower Street, 48th Floor  
Los Angeles, CA 90071

Telex #213-627-8488  
(213) 488-0010

FINANCING TEAM (Cont.)

Page 2

Co-Underwriter's Counsel

Mudge Rose Guthrie Alexander & Ferdon  
333 South Grand Avenue, Suite 2020  
Los Angeles, CA 90071  
William K. Kramer, Esq.  
David S. Tan, Esq.

Telex #213-680-1358 or 3256  
(213) 613-1112

Harrison, Taylor & Bazile  
449 - 15th St., Suite 303  
Oakland, CA 94612  
John S. Harrison, Esq.

Telex #415-834-7188  
(415) 465-0203

AUDITORS

Touche Ross  
100 Howe Ave.  
Suite 100 South  
Sacramento, CA 95825

(916) 971-3032

Attention Terry Krueger, Partner

TRUSTEE

Joel Tenorio  
Security Pacific Bank  
33 Montgomery St., 11th Floor  
P. O. Box 7887, N5-145  
San Francisco, CA 94120

Telex #415-445-4978  
(415) 995-2108

LESSOR

Sacramento City Public Facilities Financing Corporation (SCPFPC)

Mr. Ralph Scurfield  
Scurfield Co.  
601 University Avenue  
Sacramento, CA 95825

Bus. Phone: (916) 925-7648

Mr. Burnett Miller  
Burnett & Sons Planing Mill & Lumber Co.  
11th & C Streets  
Sacramento, CA 95814

Bus. Phone: (916) 442-0493

Mr. John Varozza  
1732 63rd Ave.  
Sacramento, CA 95822

Bus. Phone: (916) 489-7447  
Home Phone: (916) 421-1094

RATING AGENCY

Mr. Joseph Rosenblum  
Ms. Nancy Barbe  
Moody's Investors Service  
99 Church St.  
New York, New York 10004

Telex #212-267-1466 or 1410  
(212) 553 0337  
(212) 553-0300

INTERNAL STAFF

Issuer

City of Sacramento  
800 - 10th St., Suite 1  
Sacramento, CA 95814  
Thomas P. Friery                      Telex #916-448-3139  
Treasurer                              (916) 449-5168

David Affleck  
Treasury Operations Ofcr.              (916) 449-5318

Walter J. Slipe  
City Manager                              (916) 449-5704

Solon "Doc" Wisham, Jr.  
Asst. City Manager                      (916) 449-5704

Jim Jackson  
City Attorney                              (916) 449-5346

Jack R. Crist  
Deputy City Manager                      (916) 449-1228

Lorraine Magana  
City Clerk                                (916) 449-5426

Betty Masuoka  
Director of Finance                      (916) 449-5736

Ken Nishimoto  
Budget Officer                              (916) 449-5736

Mike Stamper  
Accounting Officer                      (916) 449-5832

Mike Medema  
Revenue Officer                              (916) 449-5854

Mel Johnson                              (916) 449-5283  
Director, Public Wks. Dept.

Sam Burns                                (916) 449-5291  
Director, Comm./Convention Center