



COUNTY OF SAN MATEO
Inter-Departmental Correspondence
County Manager



Date: March 19, 2014

Board Meeting Date: March 25, 2014

Special Notice / Hearing: 5 Days Publicly
Noticed Hearing

Vote Required: 4/5ths

To: Honorable Board of Supervisors

From: John L. Maltbie

Subject: Issuance of up to \$215 Million of Lease Revenue Bonds to finance the site acquisition and remediation, design, architecture, and construction of the Maple Street Correctional Center.

RECOMMENDATION:

Adopt a Resolution:

- A) Approving the issuance by the San Mateo County Joint Powers Financing Authority of not to exceed \$215 million aggregate principal amount of Lease Revenue Bonds (Capital Projects), 2014 Series A;
- B) Authorizing the forms of and directing the execution and delivery of a site lease, a facility lease, a bond purchase contract, a continuing disclosure agreement and an official statement;
- C) Authorizing a lease financing with the San Mateo County Joint Powers Financing Authority; and
- D) Approving the taking of all necessary actions in connection therewith.

BACKGROUND:

The overall construction cost for the Maple Street Correctional Center Project ("Project") is determined to be approximately \$165 million, which includes design, construction and equipping of the facility, and site remediation. In addition, the County issued a short-term borrowing of \$16.3 million in December 2013 to finance site acquisition and related costs for the intended purpose of reimbursing itself for those costs and will be refinancing those costs from the bond proceeds. The County now requests the Authority to issue Lease Revenue Bonds to finance the site acquisition and construction costs. Based on current interest rates and market conditions, the total bond size is projected to be \$210.2 million, including approximately \$19.6 million for interest payments made to investors during construction (capitalized interest), \$7.4 million for an investor required reserve account held for the Authority by the trustee, and \$1.9 million in expenses for

legal, financing and bond underwriting services. The financing team is investigating the possibility of purchasing a surety bond in lieu of the reserve account, which would lower the bond size by \$7.3 million – net of the surety premium fee and reductions to capitalized interest and issuance costs resulting from a smaller bond issuance. Once the bonds are sold, the funds will be transferred to the trustee to fund construction, refinance the reimbursement note, fund capitalized interest, establish the reserve account, pay closing costs and reimburse the County for out-of-pocket expenditures, which currently approximate \$29 million. The actual reimbursement will include amounts that accrue as progress payments are made through the closing date in late April.

The County has selected Citigroup to lead an underwriting team that includes Raymond James, Barclays, and Siebert Brandford & Shank to coordinate the sale of the Maple Street Correctional Center lease revenue bonds. Mark Epstein, of California Financial Services, will serve as the County's financial advisor, Orrick Herrington as bond counsel, Sidley Austin as disclosure counsel, and US Bank as trustee.

DISCUSSION:

In the past, the debt service repayment schedules were structured on a level annual payment basis or on a slightly increasing payment basis. These are the two most common debt structures associated with lease revenue bonds. Prior issuances were structured these two ways in order to: 1) maximize the potential for reimbursement by State and Federal programs where reimbursement of the borrowed principal is capped at 2% per year (50 year straight-line depreciation); 2) mirror the rental payments and minimize the fiscal impact to County departments when transitioning from privately owned facilities to County-owned facilities; and 3) contain the initial fiscal impact of the capital debt service on the General Fund when replacing a facility.

In the process of discussing the project with our advisors and reviewing underwriter proposals, the County has elected a different repayment structure for the Maple Street Correction Center Project. This new structure takes into account that the Maple Street capital costs are not reimbursable from outside sources, hence not subject to the 2% cap referenced in the preceding paragraph, and that the new facility and programs are not being transitioned from a private landlord. This model is designed to reflect "the total cost of ownership and operation" (TCOO) of the Maple Street facility – the cost of programs and capital are considered together as a single budgetary impact of operating the facility.

The TCOO model reduces debt service payments each year by the amount that operating costs (i.e., staffing, supplies, maintenance, utilities, etc.) are expected to increase, thereby maintaining a more level cost of operations. The Board should be aware that the debt service costs will be fixed at closing while the operating costs will fluctuate with broader inflationary conditions, changing staffing needs, program and occupancy levels. However, the TCOO approach will result in a "more level" cost of ownership even if the operating costs escalate faster than estimated at the time that the bonds are sold.

More importantly, the TCOO structure will result in lower interest costs over the term of the bonds due to the accelerated payment of principal. It is also our expectation that the rating agencies will view this structure more favorably than a level payment or escalating payment approach and that the TCOO structure will be seen as prudent and conservative when our ratings are reviewed. We believe this approach gives the County the strongest argument for retaining the highest rated credit among all California counties.

The interest rate on the bonds shall not exceed a true interest cost of 5.50% per annum, the underwriting discount shall not exceed 0.6% of the principal amount of bonds sold, and the maximum term of the bonds would be 33 years from the date of issuance. These are the maximum authorized parameters. If, for any reason, one or more of these parameters cannot be met, additional authorization would be required before the bonds could be sold.

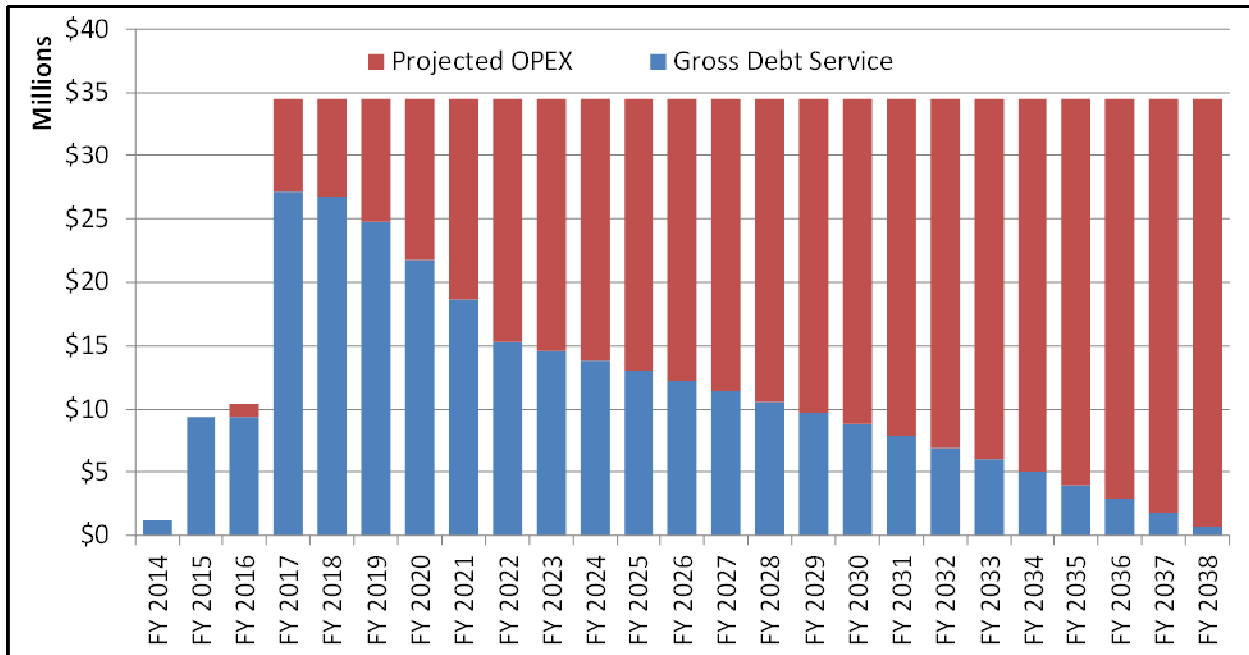
The San Mateo County Joint Powers Financing Authority reviewed and approved the refunding parameters at a Special Meeting on March 5, 2014. County Counsel, Bond Counsel and Disclosure Counsel have reviewed the Resolution and financing documents as to form.

Approval of this Resolution contributes to the Shared Vision 2025 outcome of a Collaborative Community by ensuring a cost effective approach to financing the Maple Street Correctional Center Project and leveling the cost of owning and operating the facility over the term of the financing.

FISCAL IMPACT:

The total amount of the bonds issued will not exceed \$215 million. Based on current market conditions, total debt service would approximate \$284 million over the term of the bonds (\$11.8 million average annual debt service), with the highest annual debt service estimated at \$27.1 million in FY 2016-17. From that point forward debt service will decline each year, approximating \$15.3 million by FY 2021-22, \$11.5 million by FY 2026-27, \$7.0 million by FY 2031-32 and \$1.8 million by FY 2036-37. Interest rates cannot be “locked-in” until the bonds are sold in April. The actual fiscal impact will vary according to market conditions at time of sale but cannot exceed the parameters specified in the resolution as described above.

The chart below illustrates the level cost of ownership and operation over the term of the bonds.



ATTACHMENTS

Preliminary Official Statement – 2014 Series A Lease Revenue Bonds

Bond Purchase Contract

Continuing Disclosure Agreement

Site Lease

Facility Lease

Trust Agreement