



CITY OF SANTA BARBARA FINANCE COMMITTEE AGENDA REPORT

AGENDA DATE: March 5, 2013

TO: Finance Committee

FROM: Administration Division, Finance Department
Water Resources Division, Public Works Department
City Attorney's Office

SUBJECT: Professional Services Agreements – Financial Advisory Services And
Bond Counsel And Disclosure Services

RECOMMENDATION: That Finance Committee:

- A. Hear a report from staff regarding the potential sale of Water Fund certificates of participation ("COPs") to refinance existing debt and the proposed hiring of a financial advisory firm and bond and disclosure counsel firm to assist in the potential issuance of Water, Wastewater and Waterfront Fund COPs; and
- B. Recommend to Council approval, subject to approval as to form by the City Attorney, of a professional services agreement with Orrick, Herrington & Sutcliff, LLP, for bond and disclosure counsel services in an amount not to exceed \$255,000 for all three potential transactions, and a professional services agreement with KNN Public Finance for financial advisory services in an amount not to exceed \$195,000 for all three potential transactions, with the costs of these services payable from the proceeds of the COPs if, and at such time as, the COPs are issued.

DISCUSSION:

Over the next year, City staff will be evaluating the feasibility of issuing certificates of participation (COPs) in the Water Fund, Wastewater Fund and Waterfront Fund. In the case of the Water and Waterfront Funds, the purpose of such a sale would be to refinance existing long-term indebtedness primarily to capitalize on historically low interest rates. In the case of the Wastewater Fund, the purpose is twofold: first, to refinance existing debt; and second, to provide financing for a large capital improvement project at El Estero Treatment Plant.

The first COP City staff will be evaluating is for the Water Fund. Later, within the year, staff will be considering two other bond sales for the Wastewater Fund and Waterfront Fund. Staff from the Public Works, City Attorney and Finance Departments have been completed a preliminary analysis and it appears that the City could reduce its overall annual debt service costs. Additionally, the refinancing of existing debt will eliminate

Council Agenda Report

Professional Services Agreements – Financial Advisory Services And Bond Counsel And Disclosure Services

March 5, 2013

Page 2

confusing and conflicting covenants among all outstanding debt, which will facilitate the sale of future debt.

The Water Fund currently has five outstanding debt obligations, which include the 2002 Refunding Certificates of Participation, the 1994 Refunding Revenue Bonds, and three separate loans from the State Department of Water Resources (DWR) through its revolving loan program.

In total, the Water Fund has \$79.4 million in outstanding long-term debt. It is unlikely that the most recent loan of \$29 million from the DWR will be included in the refinancing and the 1994 bonds may be cash refinanced from existing reserves rather than new COPs. As such, a total of \$48.3 million in debt would likely be included within the potential debt refinancing.

Whether staff ultimately recommends moving forward with debt refinancing in the Water Fund is dependent on what savings in debt service costs will actually be realized. The calculation of savings is impacted by the interest rate on the refunding COPs and to what extent they may rise as we move closer to the actual sale; and the costs to sell the COPs (i.e., legal and financial advisory costs, rating agency and underwriting costs that might be paid). With the exception of rating agency costs, all of the costs are payable solely from COP proceeds, and only if the COPs are actually sold; therefore, only minimal costs will be incurred up front and there is no commitment to incur other costs until these factors have been appropriately analyzed and the COPs are actually sold.

Based on the work done to date, staff is at the point where bond/disclosure counsel and a financial advisor should be retained to assist City staff with the analysis, gathering appropriate documentation and preparing the necessary documents for a potential sale. A description of the firms, their respective scope of services and related fees are provided below.

Financial Advisory Services

The City historically has used financial advisors with the issuance of long-term debt. For example, with the recent sale of Airport Certificates of Participation, the City used a financial advisor. For a number of years, the City has retained the services of KNN Public Finance for financial advisory services. KNN is a highly qualified firm with extensive knowledge of the City's operations and past bond sales. Staff believes this expertise and knowledge of the City is important to ensure any bond sale is based on a thorough understanding of the City's needs and the bond market.

In general, the role of a financial advisor is to serve as an independent advocate for the seller of bonds or other indebtedness and provide the seller with the information necessary to make intelligent, informed decisions. The sale of bonds is a highly specialized, complicated and nuanced transaction, requiring a level of expertise not generally held by municipal finance professionals within the City. Specifically, the financial advisor helps

Council Agenda Report

Professional Services Agreements – Financial Advisory Services And Bond Counsel And Disclosure Services

March 5, 2013

Page 3

structure the financing to get the best rate for the City, reviews and gives advice on the bond underwriter's proposals in a negotiated bond sale, reviews documents from bond counsel and disclosure counsel, and coordinates the bond issuance closing process. For a competitive sale of the bonds, the financial advisor structures the bond issue, conducts a public sale, identifies the winning bidder and coordinates the bond issuance closing process.

While staff is currently seeking financial advisory services in connection with the sale of refinancing Water bonds, other bond sales will also be evaluated within the year. Therefore, the scope of services described below encompasses the full range of services that may be provided to the City.

The scope of KNN's service will include, but not be limited to, the following:

1. In conjunction with the underwriter, as appropriate, the City and the Rate Consultant develop a financing plan to meet the City's construction time line for new capital projects, capital plan, any additional covenants and projected cash flow needs.
2. Assist in the selection of other financing team members, such as underwriter, bond counsel, verification agent, trustee and Rate Consultant, as necessary.
3. Coordinate the efforts of the underwriter, if any, City staff, bond and disclosure counsel, Rate Consultant, City Attorney, and City elected officials, with respect to the preparation and approval of the financing documents by the City Council.
4. In conjunction with the underwriter, if any, and bond counsel, recommend specific financial covenants, terms and provisions, including maturity schedules, timing of sale, call provisions and related matters.
5. Review and provide appropriate revisions and recommendations to legal documents, Rate Consultant report, the official statement and other documents.
6. Prepare and coordinate the appropriate presentation to the rating services and bond insurer.
7. Coordinate the sale and closing of the transactions.

KNN's fee for an initial bond sale is \$75,000. Their fees would be reduced to \$60,000 for any subsequent bond sale within 9 months of the closing of the first sale.

Bond and Disclosure Counsel Services

Staff recommends retaining Orrick, Herrington & Sutcliff, LLP (OH&S) for both bond counsel and disclosure counsel. OH&S has assisted the City with a number of bond sales over the years. They have a strong knowledge of City operations and have tremendous experience in the area of bond sales and public finance.

Council Agenda Report

Professional Services Agreements – Financial Advisory Services And Bond Counsel And Disclosure Services

March 5, 2013

Page 4

As Bond Counsel, OH&S will provide the legal opinion delivered with the bonds confirming that the bonds are valid and binding obligations of the City and, customarily, that interest on the bonds is exempt from federal and state income taxes. For each bond the City sells, OH&S will provide the following services:

1. Consultation with representatives of the City, the underwriter and/or the financial advisor, consultants and others concerning the financing, its timing, terms and structure. Such consultation will include considerations of the California law, federal tax law and municipal bond law as they affect the proposed financing.
2. Preparation of legal proceedings for the authorization, sale and issuance of the Certificates of Participation; preparation of the proceedings for the execution, delivery and sale of the COPs and advice to the City concerning the terms thereof; preparation of other proceedings (including closing papers) required in connection with the issuance of the COPs. All legal proceedings for action by the City necessary for the execution and delivery of the COPs will be prepared by Bond Counsel and will be subject to the approval of the City Attorney.
3. The rendering of a final legal opinion on the validity of the COPs and exclusion from gross income for federal tax purposes of interest payable on the COPs.

As Disclosure Counsel, OH&S will advise the City with respect to compliance with federal and state securities laws in the course of the debt issuance process. Specifically, OH&S will provide the following services:

1. With the assistance of the City Attorney's Office and staff of the City, prepare disclosure documents including the Official Statement which shall contain disclosures relating to the City, the underlying funds and the COPs.
2. Examine the proceedings, participate in any conference calls, and attend all due diligence meetings of the financing teams and the City Council relating to the drafting and approval of the Official Statement.
3. Issue a "10b-5 opinion" in the Firm's customary form addressed to the City.

Fees for both bond counsel and disclosure counsel services will not exceed \$85,000 for each bond sale, subject to reductions should the City pursue more than one debt issuance within 18 months.

SUBMITTED BY: Robert Samario, Finance Director
Sarah J. Knecht, Assistant City Attorney

APPROVED BY: City Administrator's Office