

REPORT FROM

OFFICE OF THE CITY ADMINISTRATIVE OFFICER

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Council File No. 10-1763-S2

Council District: ALL

To: Mayor and City Council

From: Miguel A. Santana, City Administrative Officer 

Reference: C.F. 10-1763-S2

Subject: **STATUS OF THE MUNICIPAL IMPROVEMENT CORPORATION OF LOS ANGELES COMMERCIAL PAPER PROGRAM**

SUMMARY

In accordance with the City's Financial Policies, the City Administrative Officer (CAO) reports the status of the Municipal Improvement Corporation of Los Angeles Commercial Paper (MICLA CP) Program in the Financial Status Reports. In the "First Financial Status Report" dated September 29, 2011, the CAO reported an outstanding MICLA CP balance of \$204.2 million (C.F. 11-0600-S145). Currently, short-term interest rates are still at historic lows and range from 0.08% to 0.23%. The issuance of CP is dependent on the timing of invoice payments for various capital projects and equipment purchases therefore there is not a specific project or equipment that triggered the need to issue over \$200 million in MICLA CP.

Over the past few months, MICLA CP was used towards the construction and improvements of various capital projects such as the 16 Transportation ARRA projects, Aiso Street Parking Structure, Alternative Fuel – Hollywood CNG Station, East Valley Multipurpose Center, Elephants of Asia Exhibit, Financial Management System Project, Living Amphibians, Invertebrates and Reptiles Exhibit, Mount Lee Communications Project, Neighborhood City Hall – Council District 14, and Vine Street Parking Garage. Capital equipment and replacement vehicles were purchased for the departments of Fire, General Services, Information Technology Agency and Police.

In the coming months, several capital projects need MICLA CP financing to continue construction (see Attachment A for a project list). The most crucial project is the Sixth Street Viaduct Seismic Improvement Project (SSVIP) which anticipates borrowing approximately \$98.4 million over seven years for its cash flow financing needs. MICLA CP will be fully reimbursed, including interest costs and costs of issuance, from funds by the Federal Highway Bridge Program and the State Proposition 1B Local Seismic Retrofit Account. Since the SSVIP is 98 percent funded by federal and state programs on a reimbursement basis, the MICLA CP financing is a critical component to the SSVIP's financial plan for cash flow project expenditure needs. If SSVIP was not able to use MICLA CP to cash flow its project expenditures, the project will likely be delayed

or canceled. The delay or cancellation of this project is a public safety concern as it has been determined that the Sixth Street Bridge has a 70 percent probability of failure in a major seismic event (e.g. earthquake).

The CAO anticipates a \$100 million to \$150 million MICLA CP refinancing to occur in January 2012. This refinancing will convert outstanding MICLA CP into long-term obligations. After the refinancing is completed the MICLA CP Program will have more short-term borrowing capacity for future capital projects such as the SSVIP. Overall, the MICLA debt program total outstanding debt is approximately \$1.4 billion.

Impact of Council Discussions Regarding Partnerships with Financial Institutions

In 2008, the City Attorney through outside counsel filed a lawsuit against 35 financial institutions alleging wrongdoing related to derivatives and bid rigging. Ongoing discussion continues with outside counsel and the defendants in this litigation. The recent Council dialogue regarding not doing business with financial institutions that the Council believes have committed financial wrongdoing in the past five years could potentially put the City's CP Program at risk. More importantly, two of the three letter of credit (LOC) providers for the MICLA CP Program are defendants in the Lawsuit. If Council instructs the CAO to stop doing business with its current LOC providers, the financial repercussions will be immense as the City could be forced to terminate the LOCs within 30 days and pay as much as \$27.8 million in termination fees (one-time cost) and replacement costs.

Replacing the current LOCs will be extremely difficult as many banks reserve their credit for existing clients and fewer banks are providing credit in this difficult financial climate. For example, in the last MICLA LOC transaction, the City sent Requests for Indication to 28 banks, including local banks, but only received two responses. None of the local banks responded to the City's Requests for Indication. In a recent LOC survey of banks, local banks were offering LOCs at rates that were nine times higher than standard market rates. Hence the City is likely to incur higher LOC costs from new providers, not withstanding whether the City is even able to obtain new LOCs.

Furthermore, if the City is unsuccessful in replacing the LOCs, the City will not have a cost effective financing mechanism to continue financing its capital projects and equipment. Without sufficient LOCs providers, the City will also need to refinance the entire outstanding CP into long-term debt. The refinancing will result in additional General Fund annual debt service costs of approximately \$14.9 million over 30 years. Due to banking policy uncertainties and financial ramifications, CAO recommends suspending the financing of all MICLA approved capital equipment and projects, including those previously authorized by Council, until a resolution is reached relating to the City's ability to do business with financial institutions involved in the City's Lawsuit. This allows the Council the flexibility to resolve its policy discussions surrounding the financial institutions without incurring any more General Fund debt.

As previously mentioned, the CAO anticipates refinancing approximately \$100 million to \$150 million of MICLA CP to long-term MICLA debt. If the CAO is unable to proceed with this planned

transaction in a timely fashion, it is likely the City will incur higher borrowing costs over the long term.

Lastly, the ramifications of not doing business with certain financial institutions not only affects other debt programs managed by the CAO such as the issuance of bonds for the Convention Center Renovation and Downtown Event Center Project and the Los Angeles Wastewater System Debt Program, but also affordable housing and economic development bond financings managed by CDD and Housing. These financing programs also include transactions with many of the financial institutions that are included in the City's Lawsuit. A policy decision regarding these financial institutions should be resolved as soon as practical so that the issuing departments can avoid project/program delays and minimize any financing costs. Depending on the phase of the financing, the issuing department may incur significant costs if the transaction cannot be completed with the pre-selected financing team. A typical financing takes approximately three to five months to complete and the costs of issuance range from \$300,000 to \$800,000. Another critical factor to consider is the complexity of the debt program as some smaller financial institutions may not have the capital resources and capabilities to provide the financial services at attractive rates.

RECOMMENDATIONS

That the City Council, subject to the approval of the Mayor:

1. INSTRUCT City departments to immediately suspend ordering equipment, halt all transactions or processing invoices related to all Municipal Improvement Corporation of Los Angeles (MICLA) financed equipment and projects.
2. INSTRUCT the City Administrative Officer to suspend issuing commercial paper notes to finance previously approved MICLA capital equipment and projects; and
3. INSTRUCT other City departments to suspend all future bond financing including affordable housing and economic development, until the City has resolved its policy deliberations over financial institutions.

FISCAL IMPACT STATEMENT

If the City is prohibited from doing business with certain financial institutions, the potential General Fund impact may be as high as \$27.8 million to pay for termination fees and LOC replacement costs.

DEBT IMPACT STATEMENT

If the City refinances the entire commercial paper outstanding, it will result in an estimated annual debt service cost of \$14.9 million over 30 years.

Attachment A

MICLA Project List

Lists of MICLA Capital Projects (partial list only)

MICLA Capital Projects using CP in last 3 to 4 months			
CD	Project	Project Status	
9	Aiso Street Parking Structure	99% complete	
4	Alternative Fuels-Hollywood CNG Station	70% complete	
2	East Valley Multipurpose Center	100% complete	
4	Elephants of Asia Exhibit	100% complete	
4	Living Amphibians, Invertebrates and Reptiles Exhibit	80% complete	
	Mt. Lee Communications	5% complete	
14	Neighborhood City Hall - 14	50% complete	
13	Vine Street Parking Structure	51% complete	
4	Rainforest of the Americas	5% complete	
MICLA Capital Projects requiring CP within the next 12 months			
CD	Project	Amount required	Comments
9	Aiso Street Parking Structure	2,500,000	Work already completed
6	Alternative Fuels: N. Hollywood Maint. Shop Retrofit	10,000,000	
	Asphalt Plant Retrofit	10,000,000	
4	Elephants of Asia Exhibit	320,000	Retention payment; work already completed
9	Figueroa Plaza - Private Use Defeasance	7,000,000	
4	Living Amphibians, Invertebrates and Reptiles Exhibit	1,950,000	
	Mt. Lee Communications	2,400,000	
14	Neighborhood City Hall - 14	1,985,000	
14	Sixth Street Viaduct Seismic Improvement Project	67,000,000	Total authority of \$98.5M needed by December 2011.
13	Vine Street Parking Structure	7,200,000	
	Total	110,355,000	