



BOARD LETTER APPROVAL



JEFFERY L. PELTO
Chief Financial Officer



DAVID H. WRIGHT
General Manager

DATE: September 12, 2016

SUBJECT: Initial Authorization to Issue up to \$1 Billion in Water System Refunding Revenue Bonds Under Resolution No. 4916

SUMMARY

Proposed Resolution No. 4916 seeks authorization to issue up to a maximum of \$1 billion of tax-exempt Water System Refunding Revenue Bonds (Refunding Bonds) payable from the Water Revenue Fund. The Bonds will be used to refinance or replace existing Water System Revenue Bonds mostly set with higher interest rates with lower rates thereby lowering LADWP's cost of debt.

Mayoral and City Council approvals are required pursuant to Section 609 of the Charter of the City of Los Angeles (Charter). A subsequent resolution, to be introduced at a subsequent Board of Water and Power Commissioners' (Board) meeting, will provide additional details about the specific proposed refunding issuances. The \$1 billion authorization will provide sufficient authority for particular transactions contemplated to take place in the current fiscal year, as well as capacity for future refundings.

RECOMMENDATION

It is requested that the Board adopt the attached Initial Resolution (Resolution No. 4916) recommending City Council's approval to issue up to \$1 billion of tax-exempt Water System Refunding Revenue Bonds per Charter Section 609.

ALTERNATIVES CONSIDERED

The LADWP could forego any refinancing opportunity to save millions of dollars on debt service costs and continue to pay the stated debt service on certain outstanding higher coupon Water System debt. LADWP also has the choice as to when to execute the refunding transactions, and could wait for interest rates to potentially fall further from current levels.

FINANCIAL INFORMATION

The debt issuance costs are estimated at \$3.37 million representing 0.34 percent of the total Refunding Bond issue of \$1 billion which include underwriter's discount, bond counsel, disclosure counsel, financial advisor, and rating agencies fees. As noted above, the \$1 billion authority may be utilized to refund certain debt in the current fiscal year and additional debt in the future.

Every one percent drop in market rates relative to the coupon rates of outstanding bonds could yield \$80-85 million in present value savings or \$5.5 million annually over 20 years, if all authorization is utilized to refund long term fixed rate bonds.

BACKGROUND

Refunding or refinancing of debt primarily involves replacing outstanding bonds with refunding bonds that pay a lower rate of interest than the refunded bonds. The proceeds from the sale or issuance of the Refunding Bonds are used to pay off the refunded bonds. The savings realized from a refunding are derived mainly from the reduction in interest costs. The lower interest costs will help keep rates lower, improve the Water System's financial coverage ratios and enhance its borrowing capacity.

Pursuant to the Procedural Ordinance, two sets of Board Resolutions are required for each Bond transaction. The Authorizing ("Initial") Resolution, which at a minimum, must specify the purpose of the proposed Revenue Bonds to be issued, the maximum limit as to principal amount, term, and interest costs, requires approval by the Mayor and the City Council pursuant to Section 609 of the Charter. The Supplemental Resolutions approve the principal financing documents, amendments to the Master Bond Resolution, and provide more specific information about the transaction including term, costs, and the sale of the bonds pursuant to the Contract of Purchase with the underwriting team for the related revenue bonds. The Supplemental Resolutions are generally presented to the Board after the Initial Resolution is approved and when the opportunity or necessity to issue the refunding bonds arises.

Resolution No. 4916 is an "initial resolution" of the Board, for the purpose of refunding or refinancing higher interest rate bonds with lower interest rate bonds. It sets forth the maximum limit as to principal, interest costs, and term for future indebtedness. Resolution No. 4916 also provides for the private sale of each series of the Refunding Bonds to one or more of the firms included in LADWP's investment banking team members (Banking Team) selected by the Board at the time of the sale. At a future Board meeting, when a determination has been made that a refunding or refinancing would be beneficial to the Water System, the Financial Services Organization (FSO) will present a "supplemental resolution" that will authorize the specific terms and conditions for the Refunding Bonds, including the underwriting firms that will be selected from among the Banking Team and the principal financing documents related to the Refunding Bonds.

With the adoption of Resolution No. 4916, LADWP will have the flexibility to maximize the opportunities for savings that are available in the currently low-interest rate environment. The FSO, along with its financial advisors and Banking Team, is constantly monitoring the market, looking for ways and opportunities to reduce the Water System's borrowing costs.

Recently, various financial institutions proposed unique ideas for responsibly restructuring some of the Water System's debt through a refunding. In accordance with the Board-approved Debt Management Policy, FSO's goal is to achieve a minimum of three percent present value savings of the refunded par amount for current and advance refundings. A current refunding is a refunding transaction that is executed 90 days before the call date of the refunded bonds. An advance refunding transaction can be executed any time before the call date (the call date is usually ten years from the date of issuance) of the refunded bonds. Federal tax law allows issuers to advance refund bonds only once. There is no such limit on current refundings.

Resolution No. 4916 is a standing authorization by the Board and would provide the FSO with the flexibility to execute multiple refunding transactions (up to \$1 billion) in the future that will produce economic savings for the Water System when relative interest rate levels decline. LADWP may also refund bonds for other reasons, as outlined in the Debt Management Policy, such as removing restrictive bond covenants, reducing risk, debt restructuring, or to free up cash on a short-term basis by restructuring future principal payments.

At this time, we estimate there may be over \$375 million of Water System revenue bonds outstanding as potential refinancing candidates that could yield, at a minimum, three percent net present value savings of refunded bonds, and possibly another \$300 million to repay short-term Notes to be drawn for bridge financing of securitization bonds. In addition, the Water System has approximately \$325 million in variable rate debt bonds (VRDBs) outstanding which are long dated bonds with short-term interest rates that reset daily or weekly. Investors can choose to not continue to hold the debt upon the interest rate reset. In the event that the investors no longer want to hold the VRDBs, LADWP may have to replace them with long-term fixed rate debt expeditiously. In anticipation of these refinancing opportunities, a \$1 billion refunding authorization is being requested.

Both the LADWP's Chief Financial Officer (CFO) and its financial advisor, the Public Resources Advisory Group (PRAG), recommend the Refunding Bonds be sold on a negotiated basis (i.e., private sale). The CFO's Report in connection with the proposed private sale, as required by Charter Section 609, is attached. Also attached is the report setting forth PRAG's opinion with respect to a private sale.

In accordance with the Mayor's Executive Directive No. 4, the City Administrative Officer's Report is attached.

ENVIRONMENTAL DETERMINATION

In accordance with the California Environmental Quality Act (CEQA), it has been determined that the request for authority to issue Water System Refunding Revenue Bonds is exempt pursuant to the General Exemption described in CEQA Guidelines Section 15061(b)(3).

CITY ATTORNEY

The Office of the City Attorney reviewed and approved Resolution No. 4916 as to form and legality.

ATTACHMENT

- Resolution
- CFO Report
- PRAG Report
- CAO Report