CITY OF SAN MATEO

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Agenda Report

Agenda Number: 13 | Section Name: {{section.name}} | File ID: {{item.tracking_number}}

TO: City Council

FROM: Drew Corbett, City Manager

PREPARED BY: Finance Department

MEETING DATE: February 16, 2021

SUBJECT:
City of San Mateo Joint Powers Financing Authority Variable Rate Demand Revenue Bonds (Public Safety Project) Series 2007A – Letter of Credit Renewal

RECOMMENDATION:
Adopt a Resolution as the San Mateo City Council and a Resolution as the Governing Board of the City of San Mateo Joint Powers Financing Authority, each authorizing the Finance Director to approve the Fourth Amendment to Reimbursement Agreement for the renewal of an irrevocable letter of credit with Wells Fargo Bank according to the terms specified in the agreement, for a five-year term from 4/5/21 to 4/5/26.

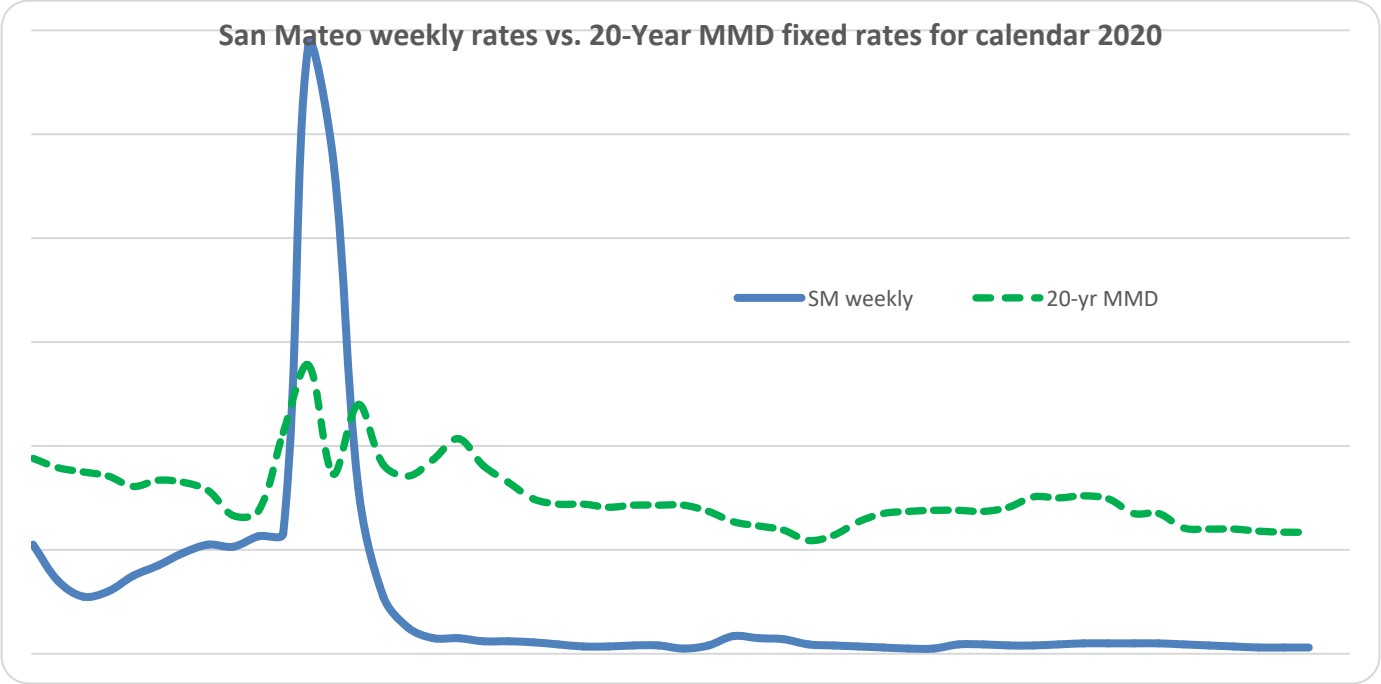
BACKGROUND:
The above-referenced bonds ("Series 2007A") were issued in the initial par amount of $17,400,000 on 4/19/07 for a final maturity of 4/1/39 to complete the financing for the police administration building. Current par amount is $14,475,000. Series 2007A was issued as variable rate to save money during the construction period and has been kept as the City's only variable rate debt because the average debt service has been favorable compared to fixed rate debt alternatives. Variable rate bonds require a bank letter of credit ("LOC") that will be drawn upon if the bonds cannot be remarketed at the weekly variable rate. Wells Fargo Bank has been the LOC provider since 2009. This LOC has been subsequently renewed in 2012, 2015 and 2018 for three-year terms. The current LOC has an annual premium of .45% and expires on 4/5/21.

The City's municipal advisors ("MAs") have in the past analyzed keeping this debt as variable rate with different credit enhancement and refunding to a fixed rate. The current variable rate structure continues to be the lowest average cost of funds and their recommendation is to keep the variable rate structure with the current LOC bank to save on processing costs. A longer LOC term of five years has been negotiated with Wells Fargo Bank for the same annual premium of .45%, with minimal renewal fees.

Although there are marketing, credit bank, and interest rate risks associated with variable rate debt, the benefits can be significant. The City's FY 2019-20 CAFR on pages 94-95 discusses the history of Series 2007A. The interest rate on this debt resets weekly and so it can be volatile, especially during times like the spring of 2020 when COVID-19 concerns resulted in short-term rates spiking almost five hundred basis points (five percentage points). The graph on the next page shows Series 2007A weekly rates as a solid blue line and the Municipal Market Data ("MMD") 20-year fixed rate index (which corresponds to the remaining term of Series 2007A) as a dashed green line. MMD is an index comprised of AAA-rated tax-exempt bonds and is used as a municipal market "gold standard" interest rate proxy, much the way US Treasury bonds are in the taxable market. Were the City to convert Series 2007A to a fixed rate it could expect to pay an average interest rate approximately 25 basis points (.25%) higher than the MMD index.

San Mateo's weekly rate jumped from 1.16% to 5.85% in one week, then fell to .25% in four weeks. Fixed rates jumped by a much lower amount during this same period. It is important with variable rate debt to consider the average interest rate

over a longer period of time. Series 2007A averaged .50% for calendar 2020, compared to 1.52% for 20-year MMD fixed rates. For the last half of calendar 2020, after the financial market turmoil ended, Series 2007A has averaged .09% compared to 1.31% for 20-year MMD. Considering interest rates over either the fiscal or calendar year, the City continues to save money on variable rate debt service over fixed rate alternatives.



The variable rate shown in the graph above is paid to bondholders. Additional costs are the LOC fee of .45% paid to the LOC bank and an annual remarketing fee of .09% paid to the remarketing agent. The sum of all of these costs still results in total variable rate debt cost over time being considerably lower than with a fixed rate alternative. Staff and the MAs considered fixed rate restructuring when variable rates spiked in the spring of 2020, but there would have been no debt service savings and the increased cost would have come at a time when the source of debt service payments (the 2% Hotel Tax Fund) has been heavily impacted by COVID-19. Should the City decide in the future to replace the variable rate structure with a fixed rate, the LOC can be terminated and the variable rate bonds prepaid at any time with no penalty.

Staff recommends Council approval of a resolution (Attachment 1) and Authority approval of a similar resolution (Attachment 2) that each authorize the Finance Director to sign a proposed Fourth Amendment to Reimbursement Agreement (Attachment 3) with Wells Fargo Bank for renewal of an existing irrevocable LOC according to terms specified in the agreement.

BUDGET IMPACT:
The LOC annual fee of .45% remains the same, with the new term of five years guaranteeing this fee for two years beyond the current term. The City can refund the debt and terminate the LOC at any time in the next five years with no prepayment penalty.

Certain one-time costs associated with the financial analysis and legal review for this LOC renewal are expected to total $12-15,000 and can be paid from the fiscal year 2020-21 budget of the 2% Hotel Tax Fund (Fund 56). These costs are routinely required for LOC renewal and are much lower than for LOC replacement with a new bank or refunding to a fixed rate. The fiscal year 2020-21 budget assumed interest expense of $175,000 for Series 2007A and due to the historically low rates for the fiscal year to date, actual interest expense has only been about $5,000 to date.

ENVIRONMENTAL DETERMINATION:
This LOC renewal is not a project subject to CEQA, because it is an organizational or administrative activity that will not result in direct or indirect physical changes in the environment. (CEQA Guidelines Section 15378(b)(5).)

NOTICE PROVIDED
All meeting noticing requirements were met.

ATTACHMENTS
Att 1 – City Authorizing Resolution
Att 2 – Authority Authorizing Resolution
Att 3 – Fourth Amendment to Reimbursement Agreement

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