COUNCIL AGENDA: 03-25-08
ITEM: 6.4

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Scott P. Johnson
William F. Sherry, A.A.E.

SUBJECT: **AIRPORT COMMERCIAL PAPER PROGRAM EXPANSION**

DATE: March 24, 2008

Approved

Date 3/25/08

SUPPLEMENTAL

REASON FOR SUPPLEMENTAL

The purpose of this supplemental memorandum is to transmit the Letter of Credit and Reimbursement Agreement with Lloyds TSB Bank plc (the "New Reimbursement Agreement") related to the financing, provide information regarding the terms of the New Reimbursement Agreement, provide information regarding the budgetary impact if the 2004A/B Bonds are not refunded on April 4, 2008, and provide a summary of the estimated costs of issuance.

DOCUMENTS RELATED TO THE FINANCING

The New Reimbursement Agreement is on file in the City Clerk's Office and is presented for City Council approval in substantially final form. The First Amendment and Supplement to the Issuing and Paying Agent Agreement and the Commercial Paper Dealer Agreement were placed on file in the City Clerk's Office in substantially final form on Friday, March 21, 2008, as described in the supplemental memorandum dated March 21, 2008.

TERMS OF THE NEW REIMBURSEMENT AGREEMENT

As described in the Financing Documents section of the memorandum dated March 14, 2008, the New Reimbursement Agreement is necessary in order to increase the amount of commercial paper notes that can be outstanding at one time from $450 million to $600 million. The market for credit facilities has been fundamentally altered in the last few months, as the impact of recent events related to the subprime mortgage crisis have led to an overall reduction in available credit capacity at the same time that demand for credit facilities has increased dramatically. Due to the limited availability of credit, banks have begun to require higher pricing and more stringent terms for credit facilities. Therefore, a number of the business terms of the New Reimbursement Agreement differ from the terms of the agreement currently supporting the Airport Commercial

Paper Program, and a summary of the key business terms of the New Reimbursement Agreement is provided below.

The issuance of the new letter of credit and the agreement set forth in the New Reimbursement Agreement are subject to approval by Lloyds' credit committee. Lloyds investment bankers have indicated that credit approval is expected by Friday, March 28, 2008. Staff will not proceed with the refunding until credit approval is in place.

Facility Fees

The facility fees are based on the City's Airport revenue bond long-term rating and the fees escalate in the event that the rating is downgraded. Based on the current ratings of "A2", "A+" and "A" from Moody's, Fitch and Standard & Poor's, respectively, the initial fee will be 0.59% for the utilized portion of the facility and 0.29% for the unutilized portion of the facility. The complete table of rating levels and fees is provided in the New Reimbursement Agreement.

18-Month Lock Period

The term of the New Reimbursement Agreement is three years, unless the commitment expiration date is extended as provided for in the agreement. The New Reimbursement Agreement includes a termination provision whereby if the City elects to terminate the agreement prior to the end of the 18th month, for a reason other than a rating downgrade of the letter of credit bank, then the City will be required to pay a termination fee. The termination fee would be equal to eighteen months of fees at the applicable rates then in effect, less any amounts actually paid through that date.

Definition of Base Rate

The Base Rate is used throughout the agreement as the basis for interest rates that the City will pay on amounts the City has drawn on the Letter of Credit and not reimbursed. The Base Rate is defined as the higher of (i) the Federal Funds Rate plus 1.00% per annum, (ii) the Prime Rate and (iii) 12%. This definition is used in the agreement as described below.

Repayment of Drawings

In the event that the commercial paper dealers are unable to remarket the commercial paper notes, it will be necessary to draw on the letter of credit to make payments on any maturing commercial paper notes. The draws on the letter of credit will bear interest at a rate initially set at the Base Rate plus 1.00%. If the draw is not reimbursed by the 30th day following the drawing, then the interest rate increases to the Base Rate plus 1.50%. If the draw is not reimbursed by the 90th day following the drawing, then the interest rate increases to the Base Rate plus 2.50%.

Payback of Unreimbursed Drawings upon Conversion to Term Loans

The City may elect to convert unreimbursed drawings into a term loan if certain conditions are satisfied on the conversion date. Term loans bear interest at a rate equal to the Base Rate plus 2.50% and the principal must be repaid over five years in twenty equal quarterly installments. If an event of default occurs, the interest rate increases to the Base Rate plus 3.00%.

Illustration of Terms of the New Reimbursement Agreement

Although the commercial paper market has not been adversely affected by recent market events and there are presently no indications that it will be, it is possible that the commercial paper market may be adversely affected in the future. In the event that the commercial paper dealers are unable to remarket the commercial paper notes on a maturity date, the draw on the letter of credit would remain unreimbursed until the commercial paper dealers are able to remarket the commercial paper notes. Using the interest rates in effect today for the purpose of illustrating the terms of the New Reimbursement Agreement, the unreimbursed drawing would bear interest at a rate of 12% until reimbursed. Similar to the existing letter of credit, there is no maximum interest rate for unreimbursed drawings or term loans.

BUDGETARY IMPACT IF BONDS NOT REFUNDED ON APRIL 4, 2008

The current interest rates for the Airport auction rate securities to be refunded are 6.50% for the 2004A Bonds and 6.00% for the 2004B Bonds. If the City Council approves the recommendations identified in the memorandum dated March 14, 2008, commercial paper notes will be issued to refund the 2004A/B Bonds on April 4, 2008 that are anticipated to bear interest of approximately 2%. If the 2004A/B Bonds are not refunded on April 4, 2008, but are then refunded on the next possible date, the City will incur approximately $333,000 of additional interest costs.

SUMMARY OF THE ESTIMATED COSTS OF ISSUANCE

As described in the Cost Implications section of the memorandum, compensation for the City's consultants and the costs of issuance will be paid from Airport operating funds or taxable commercial paper note proceeds. A summary of the estimated costs is provided in the table on the following page.

Description	Amount
Financial Advisory Fees and Expenses	$ 60,000
Bond Counsel Fees and Expenses	50,000
Letter of Credit Bank Fees and Expenses, including Counsel	55,500
Commercial Paper Dealer Counsel	10,000
Issuing and Paying Agent Fees and Expenses, including Counsel	5,000
Rating Agency Fees (Moody's, S&P, and Fitch)	67,000
Document Management, Printing, and Distribution Expenses	10,500
Contingency	42,000
Total	**$ 300,000**

The estimated costs are subject to revision because a number of the consultants are working on "time and materials" based agreements rather than fixed-fee contracts.

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WILLIAM F. SHERRY, A.A.E.
Director, Airport Department

For questions, please contact Scott Johnson, Director of Finance, at 535-7000, or William Sherry, Director of Aviation, 501-7669.