COUNCIL AGENDA: 5-22-12
ITEM: 9.1

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Julia H. Cooper

SUBJECT: SEE BELOW

DATE: April 30, 2012

Approved

Date 5/8/12

SUBJECT: MERGED AREA REDEVELOPMENT PROJECT REVENUE BONDS, SERIES 1996 A & B AND SERIES 2003 A & B – JPMORGAN LETTERS OF CREDIT EXTENSION

RECOMMENDATION

It is recommended that the City Council, acting as the Successor Agency to the Redevelopment Agency of the City of San José, adopt a resolution to:

a. Authorize, subject to the approval of the Oversight Board, the execution and delivery of a Fifth Amendment to Reimbursement Agreements in substantially final form with JPMorgan Chase Bank, NA ("JPMorgan"), to extend the terms of the letters of credit relating to the Redevelopment Agency of the City of San José Merged Area Redevelopment Project Taxable Revenue Bonds (Subordinate Tax Allocation), Series 2003A and 2003B (collectively, "2003 Bonds") and the Redevelopment Agency of the City of San José Merged Area Redevelopment Project Revenue Bonds (Subordinate Tax Allocation), Series 1996A and Series 1996B (collectively, "1996 Bonds");

b. Authorize, subject to the approval of the Oversight Board, the execution and delivery of a Letter Agreement regarding fees and charges for the various letters of credit in substantially final form provided by JPMorgan under the Fifth Amendment to Reimbursement Agreements for the 1996 Bonds and the 2003 Bonds in the amount of 2.25% of the aggregate outstanding amounts of the letters of credit, depending on the underlying ratings of the Redevelopment Agency of the City of San José (the "Agency");

c. Authorize the Executive Officer of the Successor Agency to the Redevelopment Agency of the City of San José ("Successor Agency") or her designee to take any actions and execute any and all documents necessary to complete this transaction.

OUTCOME

Approval of these recommendations will result in an extension of the letters of credit providing credit and liquidity support for the 1996 Bonds and 2003 Bonds from July 1, 2012 through July 1, 2013.

BACKGROUND

On January 24, 2012, the City of San José, pursuant to Resolution No. 76132, acknowledged its designation as the Successor Agency to the Redevelopment Agency of the City of San José (Successor Agency) as provided for in AB X1 26. On February 1, 2012, the Redevelopment Agency of the City of San Jose (the "Agency"), by operation of law, was dissolved, and a Successor Agency was established and began the process of winding down the affairs of the former Agency including the payment of enforceable obligations. The enforceable obligations include variable rate subordinate tax allocation bonds supported by letters of credit ("LOC") furnished by. Outlined below is the history of the indebtedness and agreements between JPMorgan and the Agency:

- June 1996 - The Agency issued the 1996 Bonds in an aggregate amount of $59,000,000. In order to provide credit and liquidity support for the bonds, the Agency obtained an irrevocable direct-pay letters of credit issued by JPMorgan to support the payment of debt service on the bonds (credit component) as well as the payment of the purchase price of the bonds upon their optional or mandatory tender (liquidity component). In connection with the issuance and delivery of the LOCs, the Agency entered into a Reimbursement Agreement (the "1996 Agreement") with JPMorgan. The 1996 Agreement had an initial expiration date of June 27, 2001. JPMorgan extended the 1996 Agreement in 2001 and 2006 under the same terms.

- August 2003 - The Agency issued the 2003 Bonds in an aggregate amount of $60,000,000. Payment of principal and interest on the bonds is supported by LOCs provided under a Reimbursement Agreement with the Agency (the "2003 Agreement"). The 2003 Agreement had an initial expiration date of August 27, 2006. In August 2006, JPMorgan agreed to extend the 2003 Agreement until August 27, 2009, under the same terms.

- July 31, 2009 - JPMorgan extended the 2003 Agreement through November 27, 2009, under the terms of an Amendment to Reimbursement Agreement. Which included two principal changes relating to the 2003 Agreement: 1) the annual fee would increase from 0.60% to 1.50% of the outstanding commitment amount and 2) the definition of the "Base Rate", which defines interest rates to be paid under various circumstances, including default, was changed to include a floor of 8.5%.

- November 27, 2009 - JPMorgan extended the 1996 Agreement and 2003 Agreement to November 26, 2010, under the terms of an Amendment to Reimbursement Agreements that amended both the 1996 Agreement and the 2003 Agreement. That Amendment to the

Reimbursement Agreements included the following basic terms:

(1) The annual fee with respect to the 2003 Agreement increased from 1.50% of the outstanding commitment amount to 2.30%, subject to an increase of 0.15% for each downgrade of the Agency's senior tax allocation bond rating by either Moody's or Standard & Poor's (each, a "Rating Downgrade Event").

(2) The annual fee with respect to the 1996 Agreement increased from 0.45% of the outstanding commitment amount to 2.10%, subject to an increase of 0.15% for each Rating Downgrade Event.

(3) The Agency limited to issuing additional Senior Merged Area Redevelopment Project tax allocation bonds to a par size of not more than $33,500,000.

(4) The Agency was required to reduce, by November 27, 2009, the aggregate amount of 2003 Bonds and 1996 Bonds to no more than $100 million from the then outstanding amount of $105.3 million. This was accomplished by directing the trustee of the Bonds to redeem approximately $5,300,000 of outstanding Bonds.

- October 27, 2010 - JPMorgan and the Agency entered into the Second Amendment to Reimbursement Agreements (the "Second Amendment") extending the LOCs to November 25, 2011 and a Letter Agreement regarding fees and charges. The Second Amendment included the following terms:

  (1) No new debt obligations, senior parity, or subordinate may be incurred by the Agency during the term.

  (2) A Liquidity Reserve in the amount of $5,000,000 was set aside as an added source of security for JPMorgan.

  (3) The Agency would hire a real estate consultant to develop strategies designed to enhance the Agency's revenues and increase the value of its assets by December 31, 2010.

  The Letter Agreement decreased the annual fee from 2.10% and 2.30% for the 1996 Bonds and 2003 Bonds, respectively, to 1.95% for all series. It also maintained the downgrade pricing provision increasing the fee by 0.15% for each Rating Downgrade Event. Subsequent downgrades of the Agency in 2011 by Moody's Investor Service ("Moody's") and Standard & Poor's ("S&P") to "Baa1" by Moody's and "BBB" by S&P increased the annual fee to 2.25%.

- January 4, 2011 - JPMorgan and the Agency entered into the Third Amendment to Reimbursement Agreements (the "Third Amendment") amending the timeline for hiring the real estate consultant from December 31, 2010 to February 28, 2011.

- March 9, 2011 - JPMorgan and the Agency entered into the Fourth Amendment to Reimbursement Agreements (the "Fourth Amendment") to primarily address uncertainty surrounding the then pending proposal to abolish redevelopment agencies in the State. In order to provide additional assurance to JPMorgan, the Agency pledged 18 properties to secure the bank's obligations. The Agency recorded a deed of trust against the 18 properties to secure these obligations.

- October 24, 2011 - JPMorgan delivered amendments to the LOCs directly to the Fiscal Agent, U.S. Bank National Association, providing an extension of the Stated Termination Dates of the LOCs from the existing Termination Date of November 25, 2011, to the current date of July 1, 2012, with no other change in terms.

ANALYSIS

Overview

In connection with the issuance of the 1996 and 2003 Bonds, the Agency obtained four LOCs as credit facilities from JPMorgan. The 1996 Bonds and 2003 Bonds are variable rate demand bonds with an approximate outstanding balance of $94,000,000. The interest rates for these bonds are reset weekly by a remarketing agent. The Agency's remarketing agents are required to use their best efforts to remarket the bonds and, to the extent that bonds are not remarketed, the Agency's Fiscal Agent is authorized to draw on the credit facilities. The rate resets for the week ended May 1, 2012 were: 0.22% and 0.24% for the tax-exempt 1996 Bonds, 0.23% for the taxable 2003 Bonds and 0.24% for the tax-exempt 2003 Bonds. In addition the Agency is required to pay JPMorgan an annual commitment fee for each credit facility. That annual commitment fee is currently 2.25% on the aggregate outstanding amounts of letters of credit.

Under the Fiscal Agent Agreement, the Fiscal Agent is obligated to draw on the LOC to pay debt service on the Bonds, when due, and payments made by the Agency are used to reimburse JPMorgan for such draws on the LOC or, in the event a bank dishonors a draw on the LOC for whatever reason, to pay debt service on the bonds when due. Additionally, the Fiscal Agent is obligated to draw on the LOC to provide liquidity support in the event the bonds are subject to optional or mandatory tender for purchase and the remarketing agent is unable to find a buyer (i.e., a failed remarketing) or the bonds are not remarketed in the case of certain mandatory tenders.

The current LOC agreement between the Agency and JPMorgan expires on July 1, 2012. Staff has negotiated an extension through July 1, 2013. JPMorgan is requiring that the City in its capacity as Successor Agency execute a Fifth Amendment to Reimbursement Agreement (the "Fifth Amendment") with JPMorgan and enter into a Letter Agreement regarding fees.

Over the past three years, the market for letters of credit has changed dramatically in light of the global financial recession and disruption in the financial markets. As a result of these disruptions the universe of banks issuing letters of credit has contracted significantly and annual fees have increased due to the reduced supply. Continued concerns over the depressed levels of real estate prices and uncertainty surrounding uniform implementation of ABX126 has particularly affected the availability of letters of credit for California tax allocation bonds.

The forms of the proposed Fifth Amendment and the Letter Agreement will be posted to the agenda webpage on or about May 10, 2012 for the Council Meeting on May 22, 2012. Staff recommends that the Executive Officer of the Successor Agency or the Executive Officer's designees (the "Successor Agency Designated Officers") be authorized to execute these agreements as posted, subject to the approval of the Oversight Board of the Successor Agency with such modifications as the Successor Agency Designated Officer's determines to be desirable or appropriate, upon consultation with the City Attorney.

Fifth Amendment to Reimbursement Agreement

Pursuant to the Fifth Amendment, JPMorgan will extend the term of the LOCs through July 1, 2013. The annual fee payable for the LOC will remain at 2.25% of the commitment amount. The commitment is equal to the outstanding principal on the bonds plus 51 days of interest calculated at 12 percent (the "Commitment") for an estimated annual amount of $2,300,000.

Under the Letter Agreement in the event that the long-term debt ratings of the Agency are upgraded or downgraded by one or more rating agencies, the annual commitment fee shall decrease/increase pursuant to the following table. In light of the Agency's current bond ratings, it is anticipated that the rate for the annual fee will be at Level 2. The fee is set based on the lowest rating of the two rating agencies.

LEVEL	MOODY'S RATING	S&P RATING	FACILITY FEE RATE
Level 1:	Baa1 (or higher)	BB+ (or higher)	2.10%
Level 2:	**Baa2**	**BBB**	**2.25%**
Level 3:	Baa3	BBB-	2.50%
Level 4:	Below Baa3	Below BBB-	3.00%

In connection with winding down the affairs of the former Agency, the Successor Agency is required to dispose of the assets and properties of the former Agency. As previously stated the Fourth Amendment pledged 18 properties to JPMorgan as security for payment of debt service under the existing LOCs. JPMorgan also allowed a second lien to be recorded on 17 of the 18 properties in favor of the County of Santa Clara as collateral for monies owed to the County. Schedule 1 of this memorandum lists the 18 properties. Of the 18 properties, 17 are assets owned by the Successor Agency and one is the property of the City (California Theater).

The proposed Fifth Amendment requires that as the Successor Agency sells these assets it shall apply no less than 100% of the proceeds of each such sale to the optional redemption of the 1996

Bonds and/or 2003 Bonds as well as to the reimbursement of JPMorgan for draws made under the LOC to fund such optional redemptions. In addition the Agreement requires that, consistent with ABX126, the sale of the Successor Agency assets shall be done expeditiously and in a manner aimed at maximizing value and shall not encumber or otherwise modify the existing pledge of tax revenues supporting the bonds. The benefit of the application of sale proceeds to the reduction of principal on the bonds is assisting in reducing fees paid and debt service paid on the bonds. Additionally the $5,000,000 Reserve Account established in the Second Amendment will be maintained. The Fifth Amendment also requires that all legal fees, disbursements and out of pocket costs incurred by JPMorgan be paid by the Successor Agency at closing.

Financing Team Participants

The financing team participants consist of:

Financial Advisor:	Ross Financial
Bond Counsel:	Jones Hall, A Professional Law Corporation
Letter of Credit Bank:	JPMorgan Chase Bank, N.A.
Bank Counsel:	White Case LLP
Fiscal Agent:	U.S. Bank, N.A.
Remarketing Agents:	Bank of America, N.A. (1996B, 2003B) Citigroup (1996A) JPMorgan Chase (2003A)

Financing Schedule

The current proposed schedule is as follows:

Council approval of amendments to financing documents:	May 22, 2012
Oversight Board approval:	May 24, 2012
Document closing (no later):	June 6, 2012

EVALUATION AND FOLLOW-UP

This memorandum presents the set of recommendations related to the City Council's, acting as the Successor Agency to the Redevelopment Agency of the City of San José, approval of various actions related to the 1996 Bonds and 2003 Bonds and requires no follow-up to the City Council.

PUBLIC OUTREACH/INTEREST

☒ **Criteria 1**: Requires Council action on the use of public funds equal to $1 million or greater. **(Required: Website Posting)**

☐ **Criteria 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**

☐ **Criteria 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

This action meets Criteria 1 above and will be posted on the City's website for the May 22, 2012 Council meeting.

COORDINATION

This report was prepared by the Finance Department in coordination with SARA and the City Attorney's Office.

COST SUMMARY/IMPLICATIONS

Compensation for professional services (bond counsel, financial advisor and bank counsel) and other related costs will be paid from the FY 2012-13 appropriations for debt service and associated costs. These costs are estimated to be approximately $25,000 for all these services. Any necessary budget adjustments resulting from the LOC extension will be brought back to Council at a future date.

CEQA

Not a Project, File No. PP10-066, Agreements/Contracts (New or Amended).

/s/ JULIA H. COOPER
Acting Director of Finance

For questions, please contact Julia H. Cooper, Acting Director of Finance, at (408) 535-7011.

Attachments

SCHEDULE 1

Pledged Properties

Site Description	Address
Marriot Hotel	301 S. Market Street
Westinghouse Site	292 Stockton Avenue
Parking Lot	Balbach/Almaden
Vacant Lot	501 Locust Street
Old Foxtail Bar Site	551 W, Julian Street
Hanchett Parking Lot	1343 The Alameda
Parking Lot	30 Eastwood Court
Plaza Hotel	96 S. Almaden Avenue
Two Fish	366 S. 1st Street
Anti – Graffiti Office	501 Vine Street
Vacant Lot	75 Bassett Street
California Theatre[1]	345 S. 1st Street
Miraido	280 Jackson Street
Mexican Heritage Retail	1770 Alum Rock Avenue
SJ Stage	490 S. 1st Street
Old Fire #1	201 N. Market Street
Billy De Frank Center	938 The Alameda
Block 7 Theater (Camera 12)	201 S. 2nd Street

[1] City Owned Property