RethinkWaste
South Bayside Waste Management Authority

STAFF REPORT

To: SBWMA Board Members
From: Brian Ponty, Board Member and Financing Manager
Kevin McCarthy, Executive Director
Date: July 23, 2009 Board Meeting
Subject: Approval of Sale of Bonds for Shoreway Environmental Center

Recommendation

The Financing Team recommends Board approval of the resolution authorizing the issuance of solid waste enterprise revenue bonds Series 2009A (tax-exempt) and Series 2009B (taxable) and directing the execution of an indenture of trust for each series, and approving various documents related thereto, including continuing disclosure certificate, preliminary official statement (includes Authority's Consultant Report), bond purchase agreement, use of funds agreement, escrow agreement, first amendment to the 2000 Bonds indenture of trust that remedies a drafting error and makes clear that the first permissible redemption date for the 2000 Bonds is March 1, 2009, a deposit agreement and authorizing other actions in connection with the sale and delivery of the bonds.

Analysis

The proposed maximum authorized amount of Series 2009A Bonds is $56.5 million and the proposed maximum amount of Series 2009B Bonds is $3 million. These amounts are not additive. For every dollar of Series 2009B Bonds sold, the Series 2009A Bonds will be reduced by a like amount. The proposed maximum authorized true interest cost (TIC) on the Series A Bonds is 6.75%. This maximum TIC allows for an increase in interest costs between now and the sale date due to reduced call protection from 10 years to five years (25 basis points estimated cost) and an adverse rating result (ratings less than the current rating of A2 by Moody's and A- by S&P) and an adverse market movement resulting in higher interest rates (70 basis point allowance for both adverse rating and market movement). Based on interest rates at the time bonds are marketed, the finance team will evaluate the feasibility and cost effectiveness of shortening call protection to five years and will structure the bond sale at that time in the most cost-effective manner. The proposed maximum maturity on the Series A Bonds is 28 years. The bonds are anticipated to be sold as 27-year bonds. There is no expectation that it will be necessary to increase the term of the bonds. The proposed maximum interest rate on the Series B Bonds is 5%.

The Series 2009A Bonds will be structured with two years of interest only followed by 25 years of fully amortized level debt service. The Series 2009B Bonds will be five years of interest only with a balloon payment due at maturity in the fifth year. Unallocated reserves are expected to be sufficient to pay off the Series 2009B Bonds in full.

Project Cost

Construction bids for the project were opened on April 22nd. S.J. Amoroso Construction submitted the low bid of $17,637,000. Since then staff has recommended exercising a transfer station education center bid deduction in the amount of $1,428,000, obtained final single stream equipment prices and negotiated equipment installation costs, and negotiated final construction management (CM) costs to arrive at a final estimated project cost of $46,971,900,

which is approximately $1 million less than the amount shared at the May 19th special board meeting.
The breakdown of the cost of the major project components is shown in the following table:

	SUMMARY	July 09 ($000)	April 09 ($000)
OTHER COSTS:	Planning, Design, and Engineering	2,404.0	2,404.0
	Non-Contingent Bond Issuance Costs	90.5	90.5
	Construction Management	2,798.3	2,716.3
	OTHER COSTS sub-total	**5,292.8**	**5,210.8**
PHASE I:	**Scales & Traffic Improvements**	**2,405.0**	**2,322.6**
PHASE II:	**MRF and Transfer Station Improvements**		
	Soft Costs	786.7	786.7
	MRF & TS Building construction	16,937.0	17,637.0
	PHASE II sub-total	**17,723.7**	**18,423.7**
PHASE III:	**MRF Equipment and Installation**		
	MRF Equipment	14,273.2	13,730.4
	Installation and Start-up	2,592.4	3,487.8
	PHASE III sub-total	**16,865.6**	**17,218.2**
	TOTAL PROJECT COST	**42,287.1**	**43,175.3**
	Contingency 12.5%, (excl PD&E, Phase I)	4,684.8	4,806.1
	MAXIMUM COST	**46,971.9**	**47,981.4**
April 2009 figures were shared at the 5/19/09 special Board meeting.			

Project Funding

On June 26, 2008 the Board voted to appropriate $17.9 million of its cash reserves toward the project including redemption of the 2000 bonds. That appropriation was made based on the expectation of substantial operating profits in FY 2008/09 and 2009/10. $2.1 million of that appropriation has been expended to date. The fall of 2008 started a period of sudden and dramatic events that negatively impacted the Authority's FY 2008/09 and FY 2009/10 operating budget assumptions. These events have had a collateral adverse effect on the Authority's capital budget assumptions which now assume internal funding of $15.57 million.

The Authority experienced a $383,000 investment income loss in the County Investment Pool as a result of the Lehman Brothers bankruptcy. Unexpected declines in interest rates further eroded budget interest income assumptions by $700,000. And in September 2008, commodity prices began to decline and then suddenly collapsed after the global credit crises emerged, resulting in a $2.8 million shortfall in commodity revenues. For FY 2009/10, commodity revenues have been forecast at only 60% of the levels in the FY 2008/09 budget.

The Authority closed the deficit in its FY2008/09 budget with a $1.7 million transfer of the balance in its rate stabilization fund, $480,000 of administrative cost reductions and $800,000 of estimated, though not fully realized, Shoreway operating expense reductions. The projected net cash flow deficit for FY 2008/09 is $1.4 million (which amount includes non-operational interest earnings and interest expenses but excludes principal repayment).

Because the Authority closed FY 2008/09 with a net cash flow deficit and is expecting a net cash flow deficit in calendar year 2009/10 due to depressed commodity prices and extraordinary operating expenses during construction attributable to offsite commodity processing costs of $3.35 million (net of operational savings attributable to closing the MRF), additional bond funded resources have been devoted to the project to shore up operating reserves and bring debt service coverage ratios during construction to acceptable levels. These bond funded resources include:

1) $1.37 million reimbursement for prior project expenditures. This amount will flow to the operating reserve.
2) $2.8 million of working capital. This amount will flow to the operating reserve and rate stabilization fund. Amounts in the rate stabilization fund are used both to meet operating expense contingencies and to satisfy required operating ratio covenants.
3) $4.15 million of capitalized interest. Capitalized interest is interest borrowed to meet interest payment obligations during construction. It is treated as a non-operating source of income in the pro forma cash flow statements that will serve to off-set expected operating deficits during construction and will allow the Authority to show acceptable debt service coverage during this period.

Current interest rate estimates range from 3.2% in 2012 to 6.15% in 2036, producing an estimated true interest cost of approximately 5.80%. Allowing for a 25 basis point additional cost to reduce the call protection period from 10 years to five years and 70 basis points for a n adverse rating assignment and an adverse interest rate move in the market, our maximum interest cost estimate is 6.75%. This is an estimate only and the cost could be higher, or lower, when the bonds are marketed in mid-August. As a rating has not yet been assigned to the bonds and the bond sale date is five weeks from the preparation of the pro forma cash flow estimates and this staff report, this very conservative interest cost assumption of 6.75% is used in the pro formas and has been proposed as the maximum authorized interest rate on the Series A Bonds. Based on a 6.75% interest rate on the Series A Bonds and a 5% interest rate on the Series B Bonds, the table on the following page presents the estimated sources and uses of funds.

Shoreway Environmental Center
Plan of Finance

		Redeem 2000 Bonds	MAXIMUM CASE 6.75% Fixed Rate Bonds
2009 BOND FUNDING			
1	**Project Cost to Fund**		**46,971,863**
	Less: Paid in 2008		(2,109,002)
	Plus Redeem 2000 Bonds	14,149,543	
	Less Prior Bonds DSRFs	(1,690,000)	
	Less: Cash from SBWMA Reserves	(12,459,543) (1)	(2,373,437) (2)
2	**Net Project Cost to Finance**		**42,489,424**
	Plus: Bond Issuance Costs		746,000
	Less: Interest Earnings on Bond Proceeds		-
	Plus: DSRF Reserve		4,446,006
	Plus: Reimbursement for Prior Amts Paid		1,370,000
	Plus: Original Issue Discount		500,000
	Plus 2009 Capitalized Interest		4,147,203
	Plus: Working Capital		2,801,367
3	**Bond Issue Size**		**56,500,000**
4	**Member Agency Loan**		**3,000,000**
	Interest Rate		5.00%
	# Years		5.0
	Interest only Payment		150,000
5	**Fixed Rate Loan**		**53,500,000**
	Interest Rate		**6.75%**
	# Years		25.0
	Debt Service		**4,488,000**
6	**Total Annual Debt Service - 2010**		**4,638,000**
	Less 2000 Bonds Debt Service		(1,690,000)
7	**Incremental New Debt Service**		**2,948,000**
8	**Interest Only**		**3,761,250**

(1) Funded at bond closing
(2) Funded in 2011 as change orders/contingency allowance requires

The following table shows projected cash flows and fund balances on a calendar year basis through 2014. The Authority's future cash appropriation for the project, which is equal to approximately half of the construction contingency allowance, is proposed to be held in unallocated reserves until a change order is executed that will require an amount be appropriated as a capital obligation. If the full contingency is used, it is not expected that this amount would be appropriated for capital expenses until near the end of the project in 2011. Management considers the projected total unrestricted reserve balances in calendar years 2009 and 2010 to be the minimum acceptable levels necessary to meet unforeseen operating contingencies.

Projected Operating Results - 6.75% Cost of Funds

		2009	2010	2011	2012	2013	2014
	Operating Revenues	1	2	3	4	5	6
1	Franchise Tip Fees	19,624,000	21,839,000	23,119,000	24,268,000	24,365,000	25,087,000
3	Public Tip Fee Revenue	6,698,000	7,510,000	8,323,000	8,780,000	8,860,000	9,122,000
4	Public Other	325,000	334,000	344,000	355,000	365,000	376,000
5	Sales of Recyclable Materials	7,687,000	8,755,000	11,577,000	12,174,000	12,803,000	12,708,000
6	Total Operating Revenues	$34,334,000	$38,438,000	$43,363,000	$45,577,000	$46,393,000	$47,293,000
7	**Total Operating Expenses**	$33,991,089	$36,952,496	$34,690,495	$35,137,500	$36,245,000	$37,192,000
8	**Net Operating Revenue**	$342,911	$1,485,504	$8,672,505	$10,439,500	$10,148,000	$10,101,000
9	Plus: Interest Income	226,398	95,297	133,858	217,856	583,000	592,000
10	Plus: Capitalized Interest	385,953	3,761,250				
11	Plus: Working Capital Transfer in	1,701,367	1,100,000				
12	Plus: Transfer in from Rate Stabilization Fund	1,712,020					
13	**Net Revenues**	$4,368,649	$6,442,051	$8,806,364	$10,657,356	$10,731,000	$10,693,000
14	Less: Debt Service - 2000 Bond	(1,279,783)					
15	Less: Debt Service - New Bonds	(1,253,750)	(3,761,250)	(3,761,250)	(4,638,000)	(4,638,000)	(4,638,000)
16	Debt Service Coverage Ratio	1.72	1.71	2.34	2.30	2.31	2.31
17	**Net Revenue Available After Debt Service**	$1,835,116	$2,680,801	$5,045,114	$6,019,356	$6,093,000	$6,055,000
18	less San Carlos Fee	1,269,000	1,414,000	1,514,000	1,591,000	1,600,000	1,647,000
19	**Net Operating Cash Flow**	$566,116	$1,266,801	$3,531,114	$4,428,356	$4,493,000	$4,408,000
20	**Beginning Reserve Balance (Unrestricted)**	$18,927,000	$4,309,553	$4,667,854	$5,495,231	$9,743,287	$14,050,587
21	Balancing Account Payment to Allied	(2,132,000)	(101,000)				
22	Miscellaneous Capital Projects	(250,000)	(807,500)	(330,300)	(180,300)	(185,700)	(191,300)
23	Changes to Rate Stabilization Reserve	(1,712,020)					
24	2000 Bonds Debt Service Reserve Fund	1,690,000					
25	2000 Bonds Redemption	(14,149,543)					
26	2009 MA Bond Redemption						(3,000,000)
27	Reimbursement for funds spent on MP project	1,370,000					
28	Transfer to Capital Project			(2,373,437)			
29	**Ending Available Balance (Unrestricted)**	$4,309,553	$4,667,854	$5,495,231	$9,743,287	$14,050,587	$15,267,287
	Reserve Ending Balance:						
30	Operating Reserve	3,272,656	3,399,109	3,469,049	3,513,750	3,624,500	3,719,200
31	Rate Stabilization Reserve	1,036,897	1,268,745	2,026,182	3,761,250	3,761,250	3,761,250
32	Equipment Replacement Reserve				1,225,000	2,525,000	3,864,000
33	Unallocated Reserve	-	-	-	1,243,287	4,139,837	3,922,837
34	**Total Unrestricted Reserve**	$4,309,553	$4,667,854	$5,495,231	$9,743,287	$14,050,587	$15,267,287
	Project Financing						
35	Beginning Balance	$0	$27,842,705	$2,687,755	$0		
36	Bond Proceeds, Net (less 2000 Bond redemption	42,489,424					
37	Capital Project Payments	(14,646,718)	(25,154,950)	(5,061,192)			
38	Internal Funds Transfer			2,373,437			
39	**Project Fund Balance**	$27,842,705	$2,687,755	$0	$0		

Scheduling
The following schedule shows the milestone events leading to a bond sale and closing.

Date	Activity
July 23	SBWMA Board approves bond documents and bond issuance.
July 31	Ratings issued
August 3	Mail Preliminary Official Statement
August 13	Sell bonds
September 1	Close bonds

Background
On May 19th the Board considered six financing options,

Option A – Public Sale of 100% Fixed Rate Tax Exempt Bonds
Option B – Public Sale of 100% Variable Rate Bonds
Option C – Public Sale of 70% Fixed Rate/30% Variable Rate Bonds
Option D – Member Agency 5-year Bond, Balance Fixed Rate Bonds
Option E – Private Placement for 100% of the Project Cost
Option F – Private Placement for Sorting Equipment Only, Balance Public Sale of Fixed Rate Bonds

The Board requested additional information regarding the Option D – Member Agency 5-year Bond, Balance Fixed Rate Bonds and directed staff to bring back to the Board on May 28th for its final consideration Options D and A. On May 28th the Board approved a financing plan consisting of fixed rate (tax exempt) bonds plus a Member Agency loan provision subordinate to the publicly offered fixed rate debt. Documents for both a Member Agency loan and a fixed rate bond sale will be prepared simultaneously. The Member Agency loan portion of the financing was not to exceed $10 million. Staff was directed to bring to the Board for its final approval substantially final bond financing documents on July 23rd. The City of Burlingame has adopted a resolution approving its purchase of member agency bonds in an amount not to exceed $3 million. The rate on the Member Agency bonds has been negotiated at 5%. No other members have adopted resolutions stating their intent to purchase member agency bonds. The rate on the publicly offered bonds will not be known until they are priced in mid-August.

Pursuant to the JPA Agreement, at least eight member agency legislative bodies must approve the sale of bonds. To date, ten agencies (the County of San Mateo, the City of San Mateo, Redwood City, Burlingame, Menlo Park, San Carlos, Foster City, East Palo Alto, West Bay Sanitary District, and Atherton) have approved the sale of bonds. While the Town of Hillsborough originally approved the bonds they have subsequently instructed its Board representative to vote against the sale of bonds. Belmont also voted against the sale of bonds. Two thirds of those Board Members present at the July 23rd meeting must approve the bond resolution in order to authorize the Authority to sell bonds.

Fiscal Impact

The rate impact associated with the sale of bonds will not be known until the bonds are sold and the final interest rates are determined. The following table shows the rate impact based on both the current market interest cost of 5.80% and the proposed maximum cost of 6.75%. At current interest costs the rate impact based on a level payment of principal and interest would be approximately 2.80%. At the proposed maximum authorized interest cost the rate impact would rise to 3.42%.

Incremental Rate Impact of New Debt

		At Current Rate of 5.8%			**At Maximum Rate of 6.75%**		
		2010	**2011**	**2012**	**2010**	**2011**	**2012**
Incremental New Debt		$ 1,413,000	$ 1,413,000	$ 2,416,000	$ 2,071,250	$ 2,071,250	$ 2,948,000
RATE IMPACT							
Bond Term (yrs)	25						
Debt Service - Franchise Operations	85%	$1,201,050	$1,201,050	$2,053,600	$1,760,563	$1,760,563	$2,505,800
2009 SBWMA Collection Rate Revenue [1]		$73,236,500	$73,236,500	$73,236,500	$73,236,500	$73,236,500	$73,236,500
SBWMA Collection Rate Impact		**1.64%**	**1.64%**	**2.80%**	**2.40%**	**2.40%**	**3.42%**
Increase over Prior Year		**1.64%**	**0.00%**	**1.16%**	**2.40%**	**0.00%**	**1.02%**

[1] Assumes rate increases as per HFH Rate Report

Alternative Actions

The Board can reduce the authorized bond amount and/or the maximum TIC for the Series A Bonds and the negotiated interest rate on the Series B Bonds. If the maximum authorized amount of bond is reduced and such reduction results in a material change in the Authority's projected financial condition, such change will be reflected in the Official Statement. A reduction in the authorized par amount of bonds could result in an adverse rating outcome and/or higher interest rates. The probable effect of a reduced bond size would be to reduce the scope of the project in some fashion with likely negative long term impacts, higher tipping fees to replace reduced bond funds, or unacceptably low reserve balances.

The Board can reduce the maximum authorized TIC for the Series A Bonds. There is no assurance that the proposed maximum TIC or any reduced maximum TIC will be sufficient to allow a successful sale of the bonds, although the financing team believes the proposed TIC is sufficiently conservative that it will not impede the sale of bonds.

The Board can vote against approval of the proposed resolution. Failure to approve the resolution will prohibit the sale of bonds at this time. If the Board fails to approve the resolution, award of the construction contract cannot proceed at this time. The $10 million lower than expected J.S. Amoroso construction bid will lapse and the project will be delayed. There can be no assurance that any rebid project would result in a cost equal to or less than the Amoroso bid. A delay of the project will require renegotiation of the management contract and will delay the roll out of single stream processing.

Attachments:

A Summary Descriptions of Principal Legal Documents
B Series A Bonds Indenture of Trust
C Series B Bonds Indenture of Trust (for Member Agency Loans)
D Continuing Disclosure Certificate
E Preliminary Official Statement (includes Authority's Consultant Report)
F Bond Purchase Agreement
G Use of Funds Agreement
H Form of Escrow Instructions
I First Amendment to the 2000 Bonds Indenture of Trust
J Deposit Agreement

Resolution 2009-21

Attachment A

Summary Descriptions of Principal Legal Documents

Series A Bonds Indenture of Trust

This document is the contract with bond owners specifying the terms under which the Authority is borrowing money and establishes a trust estate for the benefit of the bond owners administered by the bond trustee. It places a first priority lien on the Net Revenues of the solid waste system enterprise, establishes certain performance, financial and other covenants of the Authority, including a promise to establish rates annually in each calendar year an amount sufficient, in combination with commodity revenues, other revenues of the enterprise and any transfers from the rate stabilization reserve, to produce calendar annual Net Revenues that exceed annual debt service by 140% and to establish rates and charges for the enterprise so as to yield Revenues at least equal to all expenses of the enterprise. It establishes the conditions under which additional bonds secured by the enterprise Net Revenues may be sold, establishes certain financial and other duties of the Authority in connection with the operation and maintenance of the solid waste enterprise, and establishes events of default and remedies of bond owners, duties of the trustee, bond redemption provisions and miscellaneous other provisions relating the bonds and the security therefore.

Series B Bonds Indenture of Trust

This document is similar to the Series A Bond trust indenture but is applicable only to the Series B Bonds, which will be subordinate to the Series A Bonds.

Continuing Disclosure Certificate

The SEC does not have the authority to regulate municipal bond issuers. It can, however, regulate bond underwriters. The official statement provides comprehensive disclosure to investors at the time bonds are initially sold. In the interest of requiring more up-to-date information to be provided to investors, the SEC also requires bond underwriters to provide continuing disclosure of material events and key credit information on all bond issues that they underwrite. To comply with this requirement, bond underwriters, as a condition to purchasing the bonds, require issuers to provide this information to the public on an annual basis. The continuing disclosure certificate requires the Authority to annually collect and disseminate to certain firms serving as national repositories, audited financial statements of the Authority and certain operating information regarding the solid waste enterprise, information regarding bonds outstanding and debt service coverage, the balance in the debt service reserve fund, the status of any significant legislative, administrative, and judicial challenges or investigations to the operation of the facilities that are known to the Authority, and the occurrence of certain significant events (all of which are listed) relating to the security provided to investors.

Preliminary Official Statement

The preliminary official statement (POS) is the primary disclosure document provided to investors in connection with the Authority's issuance of bonds. Disclosure of these risks is a prudent and necessary condition to the issuance of bonds. It discloses material information regarding the Authority, the solid waste enterprise, the authority for and purpose of the bonds, the project to be financed and the security for the payment of interest on and the repayment of the principal of the bonds, the terms of the bonds and the redemption provisions therefore, debt service on the bonds and material risk factors relating to the Authority's ability to make debt service payments and the Authority's collection of these payments, as well as material risk factors relating to the security for the bonds in general, and other miscellaneous matters. Attachment A to the POS is the Authority's Consultant Report which provides a broad overview of the project, project finances and offers an expert opinion on the key project information, cost estimates, and assumptions and conditions.

Bond Purchase Agreement

This agreement specifies the obligation of the underwriter to purchase the bonds from the Authority and sell them to the public, the agreed upon fees of the underwriter for this service and the conditions necessary for closing.

Use of Funds Agreement

This agreement specifies the terms under which of a member agency will purchase the bonds from the Authority and the conditions necessary for closing.

Form of Escrow Instructions

This document instructs the escrow agent to hold a portfolio of treasury securities designed to pay the principal of and interest on the 2000 Bonds and to use the proceeds of the escrow to redeem the 2000 Bonds on the specified redemption date.

First Amendment to the 2000 Bonds Indenture of Trust

This is an amendment to the 2000 Bonds Indenture of Trust that remedies a drafting error and makes clear that the first permissible redemption date for the 2000 Bonds is March 1, 2009.

Deposit Agreement

This agreement provides assurance to the Authority that funds will be delivered for the purchase of Member Agency bonds on the closing date. On the date the Authority sells the Series 2009A Bonds each member agency that purchases Series 2009B Bonds will deposit the purchase price for the Series 2009B Bonds in an escrow to be held by the bond trustee. If the Series 2009A Bonds close on the designated closing date the amount in the escrow will be used to purchase the Series 2009B Bonds. The Authority will retain the interest earnings and the Series 2009B Bonds will bear interest from the date of the escrow deposit. If the Series 2009A Bonds do not close, the deposit will be returned to the Member Agency, with interest.