OCTA

January 23, 2019

To: Finance and Administration Committee

From: Darrell E. Johnson, Chief Executive Officer

Subject: Issuance of Series 2019 Measure M2 Bonds, Measure M2 Financing Documents, and Trustee Services Amendment

Overview

The Orange County Local Transportation Authority Board of Directors has adopted a Plan of Finance for the Interstate 405 Improvement Project that requires the issuance of approximately $400 million of Measure M2 sales tax revenue bonds in 2019. In addition, there is $43.5 million of outstanding M2 bonds that can be refinanced at this time at a cost savings. Final approval for the issuance of the bonds and the financing documents for the proposed transaction are presented for review and approval.

Recommendations

A. Approve the issuance and sale of the Orange County Local Transportation Authority Measure M2 Sales Tax Revenue Bonds, Series 2019.

B. Approve the refinancing of $43.5 million of the outstanding 2010 Series A Bonds, if market conditions are favorable and Orange County Transportation Authority realizes debt service savings.

C. Authorize the Chairman, Vice-Chairman, Chief Executive Officer, Executive Director of Finance and Administration/Treasurer, and Director of Finance and Administration of the Orange County Transportation Authority to sign all documents on behalf of the Orange County Local Transportation Authority.

D. Adopt Resolution No. 2019-008 authorizing the Orange County Local Transportation Authority to proceed with the issuance and sale of up to $450 million in Measure M2 Sales Tax Revenue Bonds and approve the required financing documents necessary for the Orange County Local Transportation Authority to proceed with the issuance and sale of Measure M2 sales tax revenue bonds.

E. Approve a total of $610,000 in cost of issuance expenses for bond counsel services, financial advisory services, rating fees, trustee services, and other miscellaneous expenses related to the issuance and sale of Series 2019 Measure M2 sales tax revenue bonds.

F. Authorize the Chief Executive Officer to execute Amendment No. 1 to Purchase Order No. C-5-3790 between the Orange County Transportation Authority and the Bank of New York Mellon Trust Company, in the amount of $8,500, to provide trustee services for the Orange County Local Transportation Authority Sales Tax Revenues Bonds. The total contract amount will be $23,500.

Background

The Measure M2 (M2) ordinance expresses a preference for pay-as-you-go project financing. The ordinance states that the Orange County Transportation Authority (OCTA) may use bond financing as an alternative method if the planned expenditures make pay-as-you-go financing unfeasible. OCTA's Board of Directors (Board) has continued to advance implementation of M2 through the adoption of early delivery plans through strategic financing. In 2010, OCTA issued $353 million in M2 bonds to support the Early Action Plan.

By 2041, OCTA plans to deliver $13.1 billion of M2 transportation improvements to Orange County. The $1.9 billion Interstate 405 Improvement Project (405 Project) is the largest project in the M2 plan and in OCTA's history. The general-purpose lanes portion of the 405 Project, 75 percent of the total cost, will be funded by a combination of local, state, and federal funds. The 405 Express Lanes portion of the 405 Project, 25 percent of the total cost, will be paid for by user-generated toll revenue from those who use the 405 Express Lanes.

A total of $1.136 billion is programmed from M2 funds for the 405 Project. The current 405 Project Plan of Finance includes $243 million pay-as-you-go M2 funds and approximately $900 million of bond proceeds from the sale of M2 sales tax revenue bonds to be issued in 2019 and 2021.

Source of Funds		Amount (millions)
Local - M2		
Pay-as-you-go	$	242.651
Bond Financing		893.000
Total	$	1,135.651
Federal & State		
TIFIA*	$	628.930
Federal & State Grants		135.419
Total	$	764.349
Total Funding	$	1,900.000

* TIFIA - Transportation Infrastructure Finance and Innovation Act

On May 23, 2016, the Board approved the 405 Project Preliminary Plan of Finance. OCTA carefully reviewed the debt financing options for the 405 Express Lanes portion of the 405 Project (25 percent of total costs) that must be financed with non-M2 sources. To address this, OCTA closed a 35-year $628.93 million TIFIA loan in July 2017. The non-recourse TIFIA loan is secured solely by future net toll revenues from the 405 Express Lanes. M2 funds cannot be used to repay the TIFIA loan or pay for the cost of the 405 Express Lanes.

The Build America Bureau (Bureau), which administers TIFIA loans for the United States Department of Transportation, ultimately required OCTA to secure committed M2 funds as a condition of closing the TIFIA loan. OCTA chose a cost-effective solution to this condition by obtaining an aggregate $900 million line of credit (LOC) secured by a subordinate lien on future M2 receipts. Through a competitive procurement, OCTA selected Bank of America, N.A. (BANA) to provide the LOC required by the Bureau. The BANA LOC is structured with two tranches, with one tranche for $400 million maturing July 1, 2019, and one tranche for $500 million maturing on July 1, 2021. The LOC was structured this way to match OCTA's anticipated M2 financing. Once the bonds have been issued, the LOC associated with the respective series of bonds can be terminated.

On November 12, 2018, the Board approved the selection of an underwriting team and additional funds required for bond counsel services to support the transaction.

Discussion

Consistent with the adopted Plan of Finance for the 405 Project, OCTA plans to issue M2 sales tax revenue bonds producing approximately $400 million in bond proceeds in early 2019 and M2 sales tax revenue bonds producing approximately $500 million in bond proceeds in 2021.

Level Debt Service

Historically, OCTA has issued long-term fixed-rate sales tax revenue bonds utilizing a level debt service structure. A level debt service structure allows OCTA to make an annual payment that is level over the term of the offering, and the payment is combined to include both principal and interest. The level payment is sized to fully amortize, or retire, the outstanding principal by the final payment in 2041 when the sales tax sunsets.

Call Options

The call options for the sales tax revenue bonds are subject to market conditions and will be determined at the time of pricing. The proposed structure assumes a ten-year par call, the standard convention for fixed-rate tax-exempt bonds. However, based on market conditions at the time of pricing, shorter call options may be considered for all or some of the sales tax revenue bonds.

Line of Credit

The BANA LOC is structured with two tranches, with one tranche for $400 million maturing July 1, 2019, and one tranche for $500 million maturing on July 1, 2021. The LOC was structured this way to match OCTA's anticipated M2 financings. The Bureau will allow OCTA to reduce the required LOC amount when OCTA issues M2 sales tax revenue bonds as planned. The $400 million of M2 sales tax revenue bond proceeds in 2019 will reduce TIFIA's requirement for committed funds provided by the BANA LOC by $400 million to $500 million when the $400 million M2 bond proceeds are deposited with OCTA's trustee. OCTA currently pays BANA a fee of 26 basis points, totaling $1.04 million annually, for the $400 million tranche maturing July 2019. Similarly, when OCTA sells the planned $500 million of M2 sales tax revenue bonds in 2021 and deposits the $500 million M2 sales tax revenue bond proceeds with its trustee, TIFIA will no longer have a requirement for committed funds, and the BANA LOC will terminate. OCTA currently pays BANA a fee of 36 basis points, totaling $1.8 million annually, for the outstanding $500 million tranche maturing July 2021.

Refinancing

Separately, OCTA has evaluated the savings associated with a partial defeasance of the outstanding M2 Sales Tax Revenue Bonds, 2010 Series A (Taxable Build America Bonds), serial maturities 2021 to 2025. The serial maturities of the 2010 Series A Bonds contain an optional par call on February 15, 2020. Based on analysis from the underwriting team, OCTA could refund approximately $43.540 million to achieve approximately $1,000,000 in potential savings in today's current market. Due to the nominal size of par outstanding that could be refunded for potential savings, OCTA would recommend including the defeasance of a portion of the 2010 Series A as part of the Series 2019 financing if there continues to be savings from doing so.

Recommended Structure

- Level debt service
- Standard 10-year optional par call
- Refinance $43.5 million of the 2010 Series A Bonds

Debt Service Costs Under the Recommended Structure

Staff recommends an approximate issue size not to exceed $450 million for the recommended structure discussed above. Of that amount, $400 million will fund M2 project expenses, $43.5 million will partially defease the 2010 Series A Bonds, $600,000 for underwriter's discount, and $610,000 for cost of issuance expenses. For the Series 2019 proposed issue size, it is estimated that debt service costs will average $25.598 million per year. The arbitrage yield is estimated at 2.62 percent.

Legal Documents

OCTA has also been working with the financing team to develop the documents for the transaction. The financing documents for the OCTA M2 Sales Tax Revenue Bonds, Series 2019, have been submitted to S&P Global Ratings (S&P) and Fitch Ratings (Fitch) for their review and ratings on the bonds. OCTA is scheduled to meet with S&P and Fitch on January 29, 2019, to provide an update of OCTA and discuss sales tax history and forecasts, in addition to the proposed financing. OCTA is targeting current ratings of AA+ from both S&P and Fitch for the proposed 2019 Bonds. It is anticipated that the ratings and commentary from S&P and Fitch will be released by February 4, 2019.

The financing documents for the proposed 2019 Bonds incorporate the recommended approximately $400 million bond issue and approximately $43.540 million refunded par for the 2010 Series A Bonds. To proceed with the issuance and sale of M2 sales tax revenue bonds, Orange County Local Transportation Authority (OCLTA) is required to execute several financing documents with related parties. Below is a list of items for approval with an accompanying description:

Resolution - The resolution (Attachment A) is the legal document which ratifies the approval of the issuance and sale of M2 sales tax revenue bonds, in an amount not to exceed $450 million. The resolution has 23 whereas clauses which state the statutory existence of OCLTA, M2 sales tax, and the legal authority of the OCLTA to issue the sales tax revenue bonds. The resolution also notes that to accomplish the issuance of the sales tax revenue bonds, OCLTA must enter into the documents summarized below.

Third Supplemental Indenture - The Master Indenture and Third Supplemental Indenture (Attachment B and C) are written agreements with the Trustee that specify the terms and conditions for issuing sales tax revenue bonds. The Third Supplemental Indenture, along with the Master Indenture executed in 2010 (the “Indentures”) describe the sales tax revenue bonds being offered, the maturity of the program, the protective covenants, and other terms. The Indentures describe the legal obligations of OCLTA to the bondholders and the powers of the trustee. The trustee has the responsibility for ensuring that interest and principal payments are made to registered holders of the sales tax revenue bonds. The indentures are an agreement between OCLTA and the trustee for the benefit of the bondholders.

Purchase Contract – This is the agreement between OCLTA and the underwriters, which outlines the final terms, conditions, and prices for the sale of the M2 sales tax revenue bonds. The final pricing for the bonds will occur after ratings have been obtained and premarketing efforts completed. This document is included as Attachment D.

Preliminary Official Statement – This is the preliminary version of the official statement which generally discloses material information about the bond issue, including the purpose of the bond issue, how the bonds will be repaid, and the financial, economic, and demographic characteristics of OCLTA and Orange County. It is used by underwriters to market the bonds to investors. The OCTA Board has the responsibility under federal securities laws to review the preliminary official statement to make sure there are no material misstatements or omissions of material facts. This document is included as Attachment E.

Continuing Disclosure Certificate – This is the certificate prepared for the benefit of bondholders outlining the conditions OCLTA must comply with under the Securities and Exchange Commission Rule 15c2-12(b)(5). Under this rule, OCLTA is required to provide certain financial information and operating data no later than six months following the end of the fiscal year and to provide notices of the occurrence of certain enumerated events, if material. This information will be filed on an annual basis. This document is included as Attachment F.

Debt Policy

OCTA's Debt Management Policy contains the policies and procedures that govern all debt sales. The debt policy confirms the commitment of the Board, management, staff, advisors, and other decision makers to adhere to sound financial management practices, including full and timely repayment of all borrowings, achieving the lowest cost of capital within practical risk parameters, and maintaining required disclosures to rating agencies and investors. This document is included as Attachment G.

Cost of Issuance Expenses and Underwriting Fees

Cost of issuance expenses for debt issuances are paid at the closing of a financing transaction. These costs include legal fees, financial advisory fees, rating fees, printing, roadshow, and other miscellaneous expenditures. The estimated cost of issuance expenses for an M2 debt issuance will total approximately $610,000. In addition to these costs, the underwriting fees for the transaction are estimated at approximately $600,000.

Included in these costs are trustee and trustee counsel services. OCTA currently contracts with Bank of New York Mellon Trust Company to provide trustee services. To proceed with the M2 financing, funds will need to be added to the trustee services agreement for the debt transaction. The amendment is needed to fund trust services as part of closing the transaction and for trustee's legal counsel review of documents.

Next Steps

The financing documents for the M2 sales tax revenue bonds will be sent to the rating agencies for their review and ratings. On January 29, 2019, staff and OCTA's financing team will meet with the rating analysts in San Francisco and request formal ratings for the Series 2019 Bonds. It is anticipated that ratings from S&P and Fitch will be released by February 4, 2019.

If the Board approves the recommended financing structure and amendment to trustee services, the financing team will release the preliminary official statement to the investment community. Investors will review the preliminary official statement and determine their level of interest in the bonds and whether they require additional information from staff and the financing team.

Following the release of the preliminary official statement, an investor presentation will be posted online the week of February 4, 2019. The presentation will focus on the details of the transaction, including the legal structure. The presentation will be recorded by staff and the financing team. Investors will have the option to contact staff or the underwriting team to request additional information or follow-up meetings.

On February 11, 2019, staff will be at the Bank of America Merrill Lynch offices in New York to meet with investors and answer any questions prior to pricing the transaction. It is anticipated that the retail order period will commence on February 12, 2019, and the institutional sales period will follow on February 13, 2019. Staff will meet with the financing team to review final structuring as it relates to recommended coupons and interest rate levels.

Once the bonds are sold, staff will be provided a list of investors and presented a final spreadsheet detailing the costs of the transaction. OCTA’s Executive Director of Finance and Administration will execute the purchase contract and the transaction is expected to close on February 26, 2019. On the closing date, all legal documents are executed, and funds are exchanged between parties.

Summary

The financial documents for the 2019 Series Measure M2 Bonds are presented for approval by the Finance and Administration Committee and the Board of Directors.

Attachments

A. Orange County Local Transportation Authority, Resolution No. 2019-008
B. Master Indenture of Trust
C. Third Supplemental Indenture
D. Purchase Contract
E. Preliminary Official Statement dated February __, 2019
F. Continuing Disclosure Certificate
G. Orange County Transportation Authority Comprehensive Debt Management Policy
H. Bank of New York Mellon, Agreement No. C-5-3790 Fact Sheet

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