

## A G E N D A



## Recommendation for Council Action

Austin City Council	Item ID	14138	Agenda Number	16.
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Meeting Date:	4/12/2012	Department:	Treasury
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## Subject

Approve an ordinance authorizing (i) the replacement of the Letter of Credit and Reimbursement Agreement between the City of Austin (City) and KBC Bank related to the \$236,300,000 currently outstanding City of Austin, Airport System Variable Rate Revenue Refunding Bonds, Series 2005 with a Letter of Credit and Reimbursement Agreement issued by State Street Bank and Trust Company (State Street), and (ii) all necessary related documents actions, and fees.

## Amount and Source of Funding

Funding for the facility fee payable by the City of Austin to State Street pursuant to the Direct-pay Letter of Credit, estimated at \$263,259 for the duration of the extension during FY 2012 as well as the one time cost of issuance are included in the Fiscal Year 2011-12 Approved Operating Budget of the Airport Fund.

## Fiscal Note

<b>Purchasing Language:</b>	
<b>Prior Council Action:</b>	The City of Austin, Texas Airport System Variable Rate Revenue Refunding Bonds, Series 2005 were approved by Council on August 4, 2005. A Direct-pay Letter of Credit between the City of Austin and KBC Bank was approved by Council on May 26, 2011.
<b>For More Information:</b>	Art Alfaro, Treasurer, 974-7882
<b>Boards and Commission Action:</b>	
<b>MBE / WBE:</b>	
<b>Related Items:</b>	

## Additional Backup Information

In 2005, the City entered into an interest rate management agreement to refund part of its outstanding Airport System debt from fixed rate bonds to variable rate obligations. A necessary component of any variable rate demand bonds (VRDB) is a Letter of Credit and Reimbursement Agreement (LOC). A LOC serves two functions: first, to provide liquidity as a purchaser of the securities in the event there are no buyers in the market for the City's VRDB, and secondly, as guarantor for the VRDB were the City unable to make payments for the debt service on the VRDB. The City entered into a LOC with Dexia Credit Local Bank (Dexia) at the time the VRDB was issued, which expired in June 2011. On June 21, 2011, the City entered into a new LOC with a team of three banks (JP Morgan, KBC Bank and Royal Bank of Canada) for a period of 3 years with an expiration date of June 21, 2014.

The interest rate on the Series 2005 Bonds is a variable rate that resets weekly. Investors in these types of bonds require a letter of credit or other facility to be in place to provide liquidity support, which is provided by a large commercial bank or other financial institution. Investors in these types of bonds have the opportunity to keep the bonds or to tender them for purchase, in which event the tendered bonds are remarketed to new investors, and the funds received from the new investors are used to pay the purchase price of the tendered bonds. In the event the tendered bonds are not repurchased by a new investor, the purchase price for the tendered bonds is paid via a draw made on a letter of credit. Thus, the provision of a letter of credit (liquidity support) allows for a smooth transition from one investor to another for these types of bonds, and is an element of the financing structure for these types of bonds that is required by the rating agencies.

The letter of credit being provided for the Series 2005 Bonds also provides credit support, meaning, the principal and interest payments on the bonds are made on a timely basis directly by the letter of credit bank, which are in turn reimbursed by the City. Thus, the letter of credit is important to the investors not only because of the liquidity support it provides, but also because investors look first to the letter of credit to pay the principal and interest on the bonds.

The bank issuing the letter of credit must be acceptable to the investors that purchase this type of security. The universe of banks that participate in the letter of credit market consists of large U.S. and foreign banks. This group of banks is further reduced because of the high bank credit ratings required to issue a letter of credit and meet investor requirements. The bond ordinance that governs the Series 2005 Bonds contains provisions requiring a minimum credit rating of A-1 by Standard & Poor's for any letter of credit bank. One result of the economic turmoil in 2008 and the resulting huge credit crunch, was that liquidity facility providers were forced to actually perform the function for which they were intended for – that is to step up when there is no demand for the variable rate debt that was being remarketed. Even at the credit crunch eased, many banks quit participating in these types of agreements, due to a lack of capital and/or credit rating downgrades,

On December 8, 2011, Standard and Poor's downgraded KBC Bank to an 'A-' long-term rating and 'A-2' short-term rating. The 'A-2' short-term rating reduces the number of investors available to purchase the VRDB, therefore increasing the borrowing cost associated with the KBC Bank supported portion of the outstanding VRDB. In order to lower the borrowing cost State Street has been selected to replace KBC Bank. State Street has an 'A-1' short-term rating by Standard and Poor's. The replacement will reduce the borrowing cost. JP Morgan and Royal Bank of Canada maintain an 'A-1' short-term rating by Standard and Poor's.

This action to replace KBC with State Street affects Series 3 of the City of Austin Airport System Variable Rate Revenue Refunding Bonds, Series 2005 (\$59,100,000 of the \$236,300,000 currently outstanding). The rate for the State Street LOC is 100 basis points with an expiration date of June 21, 2014.

In addition to the ongoing LOC fees, there will be certain one-time cost of issuance fees associated with execution of this transaction. The estimated total for these fees is \$125,000 and will be paid to the following entities acting in the capacity noted:

Public Financial Management – Financial Advisor

Bracewell & Giuliani LLP – Bond Counsel

McCall, Parkhurst & Horton – Disclosure Counsel

Andrews Kurth – Bank Counsel

Winston & Strawn – Bank Counsel

Standard & Poor's – Rating Agency

State of Texas Attorney General