

STATE OF ARIZONA

Joint Committee on Capital Review

STATE
SENATE

DON SHOOTER
CHAIRMAN 2013
OLIVIA CAJERO BEDFORD
GAIL GRIFFIN
JOHN McCOMISH
AL MELVIN
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HOUSE OF
REPRESENTATIVES

JOHN KAVANAGH
CHAIRMAN 2014
LELA ALSTON
CHAD CAMPBELL
TOM FORESE
DAVID GOWAN, SR.
RICK GRAY
ANDREW C. SHERWOOD

JOINT COMMITTEE ON CAPITAL REVIEW

Thursday, April 10, 2014

9:15 A.M. or upon adjournment of JLBC

Senate Appropriations, Room 109

MEETING NOTICE

- Call to Order
- DIRECTOR'S REPORT (if necessary).
- 1. [SCHOOL FACILITIES BOARD - Review of Lease-Purchase Refinancing.](#)

The Chairman reserves the right to set the order of the agenda.

4/9/14

lm

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DATE: April 9, 2014
TO: Representative John Kavanagh, Chairman
Members, Joint Committee on Capital Review
THRU: Richard Stavneak, Director *RS*
FROM: Ben Henderson, Fiscal Analyst *BH*
SUBJECT: School Facilities Board - Review of Lease-Purchase Refinancing

Request

The FY 2014 K-12 Education Budget Reconciliation Bill (BRB) (Laws 2013, 1st Special Session, Chapter 3) authorizes the School Facilities Board (SFB) to enter into a refinancing agreement that reduces the board's lease-purchase payments in FY 2014 and FY 2015 by a combined total of at least \$4.0 million, but will not increase or decrease the total amount of lease-purchase payments in any other fiscal year by more than \$100,000.

The FY 2014 K-12 Education BRB requires that, before entering into a refinancing agreement, the agreement's proposed terms must be submitted for review by the Joint Committee on Capital Review. The Committee already reviewed a refinancing proposal by SFB in October 2013 to reduce its debt service payments by \$5.2 million. SFB is now proposing to use the same statutory authority for a 2nd refinancing proposal with debt service savings of \$8.4 million.

Recommendation

The Committee has at least the following 2 options:

1. A favorable review of the refinancing agreement.
2. An unfavorable review of the refinancing agreement.

Under either option, the JLBC Staff recommends that SFB submit a final debt service schedule associated with the refinancing agreement.

(Continued)

Analysis

In FY 2003 - FY 2005, FY 2008, FY 2009, and FY 2011, SFB entered into lease-purchase agreements to finance the costs of new school construction. For each agreement, SFB issued Certificates of Participation (COPs) that are typically repaid over a period of 15 years. In October 2013, JCCR favorably reviewed a proposed refinancing agreement which achieved non-recurring savings of \$1.4 million in FY 2014 and \$3.8 million in FY 2015.

SFB has proposed executing a second refinancing agreement under the same statutory authority provided in the FY 2014 K-12 Education BRB. Under this second proposed refinancing agreement, there would be additional one-time savings, which are estimated to total \$8.4 million. The one-time savings would mostly occur in FY 2015, along with minor amounts between FY 2016 and FY 2020.

The current outstanding amount of the 2005 lease-purchase agreements is \$209 million. In this new proposed transaction, SFB would immediately issue \$226 million of new financing at an average interest rate of 1.5%, which would then be used to retire the \$209 million of current outstanding COPs with an interest rate of 5%. This retirement would occur in early FY 2016, when the 2005 issuance becomes "callable."

The excess proceeds above \$209 million would be used to pay for \$10.4 million of existing debt service in FY 2015, thereby reducing the General Fund requirement. In FY 2015, the state would then begin to make new debt service payments on the new \$226 million issuance at a cost of \$2.5 million. With the \$10.4 million reduction in the General Fund debt issuance, offset by a new payment of \$2.5 million, the net result is \$7.9 million of General Fund savings in FY 2015 in relation to the existing SFB debt service requirements, as shown in *Table 1*.

The excess proceeds would also pay for \$5.2 million of the FY 2016 debt service on the 2005 issuance before it is "called" in September 2015. The excess proceeds would also be used for approximately \$1.0 million of transaction costs. The transaction would not change the length of the term of the 2005 issuance, which is currently scheduled to expire in FY 2020. Almost all of the refinancing savings are generated in FY 2015, with only minimal changes in debt service payments after that time.

SFB expects the refinancing issuance to occur by the end of FY 2014, since the current statutory authority to proceed expires at that time. If the refinance were instead authorized in FY 2015, SFB's ability to generate a comparable level of savings would depend on whether interest rates remain stable.

Table 1 below outlines the changes to SFB's current overall debt service schedule.

Table 1

Changes to General Fund Debt Service Schedule Due To Refinancing 1/

<u>Fiscal Year</u>	<u>Current Debt Schedule 2/</u>	<u>Updated Debt Schedule</u>	<u>Difference</u>
FY 2014	172,719,800	172,719,800	0
FY 2015	170,155,200	162,232,500	(7,922,700)
FY 2016	173,734,900	173,636,600	(98,300)
FY 2017	173,509,600	173,411,600	(98,000)
FY 2018	173,267,600	173,168,200	(99,400)
FY 2019	137,790,200	137,690,300	(99,900)
FY 2020	134,528,400	134,428,900	(99,500)
FY 2021	69,835,600	69,835,600	-
FY 2022	69,835,000	69,835,000	-
FY 2023	69,835,100	69,835,100	-
FY 2024	69,834,900	69,834,900	-
FY 2025	11,187,300	11,187,300	-
FY 2026	11,187,300	11,187,300	-
FY 2027	11,187,300	11,187,300	-
FY 2028	<u>8,447,600</u>	<u>8,447,600</u>	-
Total	\$1,457,055,800	\$1,448,638,000	(\$8,417,800)

1/ Reflects total SFB debt service across all issuances. Only the 2005 series is actually being refinanced.

2/ Reflects prior FY 2014 refinancing agreement entered into by SFB.

RS/BHe:lm



STATE OF ARIZONA
SCHOOL FACILITIES BOARD

Governor of Arizona
Janice K. Brewer

Executive Director
Dean T. Gray

April 2, 2014

The Honorable John Kavanagh, Chairman
Joint Committee on Capital Review
1716 West Adams
Phoenix, Arizona 85007

Dear Representative Kavanagh:

Laws 2013, First Special Session, Chapter 3, Section 48 authorizes the School Facilities Board (SFB) to enter into a refinancing or refunding agreement in FY 2013-14 to reduce the FY 2013-14 and 2014-15 Certificate of Participation (COP) program lease purchase payments. Under the law, the transaction is required to generate a combined total of at least \$4 million savings in the two fiscal years in order to be executed. Additionally, the law requires that annual lease purchase payments in each of the other fiscal years not be increased or decreased by more than \$100,000. Subject to review and upon execution, this will be the second transaction entered into pursuant to the 2013 Legislative authorization.

Prior to entering into the agreement, the proposed terms are required to be submitted for review to the Joint Committee on Capital Review (JCCR). As such, please accept this letter and updated presentation from Stifel Nicolaus as the SFB request for JCCR review at its next meeting.

As brief background, the general fund annually appropriated lease purchase payments are debt service for the outstanding State COP obligations for new school facilities funding through the SFB. Under current conditions in the government bond market we believe the proposed refunding transaction (consisting of Refunding Series 2005A-1, 2005A-2, and 2005A-3) is poised to meet the savings requirement stated in the law. As of February 27, 2014, the following savings estimates, by maturity, were prepared by our financial team:

Maturity Date – Fiscal Year Ending	Par Amount Being Refunded	Net Estimated Savings*
6-30-14	\$0	\$0
6-30-15	\$0	\$6,500,000 - \$8,400,000
6-30-16	\$0	\$98,000
6-30-17	\$67,695,000	\$98,000
6-30-18	\$86,835,000	\$99,000
6-30-19	\$36,590,000	\$99,000
6-30-20	\$17,800,000	\$99,000

*All savings estimates are subject to market conditions and subject to change.

In sum, it is currently anticipated that the transaction will refund approximately \$208.9 million COPs. Depending on market conditions at time of sale, the total lease purchase savings is estimated to be in the range of \$6.5 – 8.4 million, virtually all of which will be realized in fiscal year 2015. These savings accrue to the state general fund. In addition, due to the structuring requirements of the legislation, the transaction is expected to also deposit \$1.3 million to the debt service fund, which is available for use in FY 2015 to offset the otherwise required general fund appropriation for the COP principal and interest payments in that year. In total, the general fund savings associated with the transaction is approximately \$6.5 – 8.4 million in FY 2015. The expected present value savings associated with the transaction is 4.0% of the par certificates being refunded. Additionally, the required payments in each of fiscal years 2016 through 2020 will change by less than \$100,000. All other basic terms (such as timing of principal payments and length of maturity) remain the same. Additional detail regarding the proposed refunding is enclosed for your review.

Finally, as required by law, this transaction will not be executed by the SFB if we are not able to meet the stated general fund savings criteria. Entering into the transaction is also subject to authorization by the SFB Board. We appreciate your review of the information. Please contact me at 602-542-6143 if you have any questions.

Sincerely,



Dean T. Gray
Executive Director

Enclosure

cc: The Honorable Don Shooter, Arizona State Senate
John Arnold, OSPB
Richard Stavneak, JLBC
Jack Brown, JLBC
Ben Henderson, JLBC
Phil Williams, SFB

State of Arizona School Facilities Board

- **Outstanding Debt Overview**
- **Legislative Criteria**
- **Certificates of Participation Taxable Refunding Opportunity**
- **Timetable of Key Steps**

April 2, 2014

Presented By Stifel:

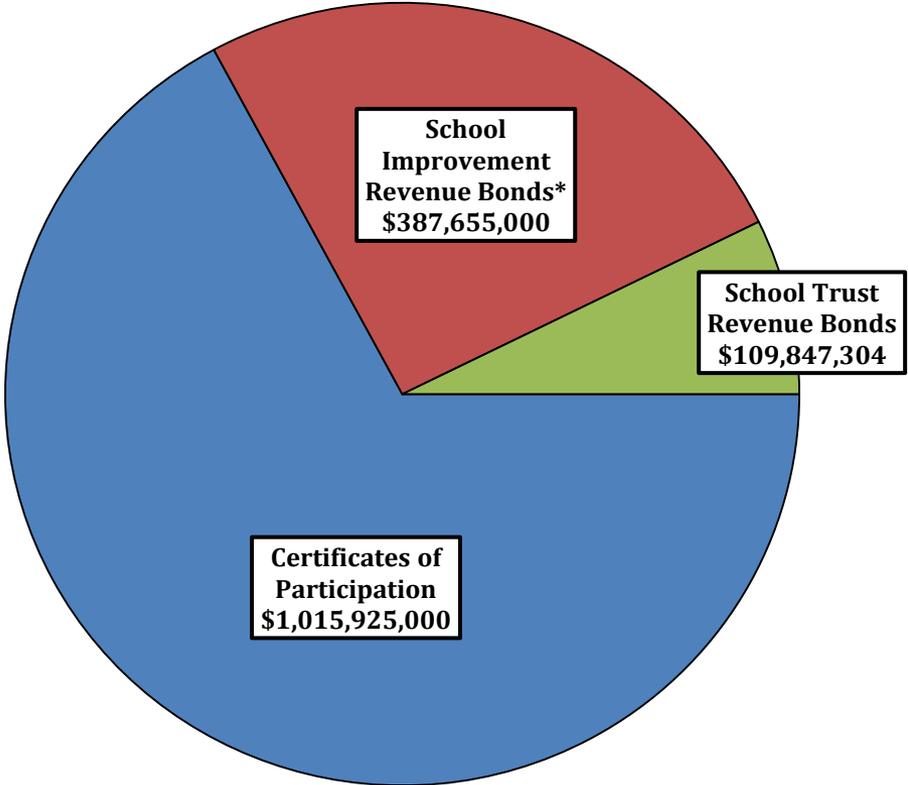
Grant Hamill, Managing Director

Randie Stein, Director

OUTSTANDING DEBT OVERVIEW

SFB Outstanding Obligations (as of March 1, 2014)

SFB Obligations Outstanding
as of March 1, 2014
\$1,513,427,304

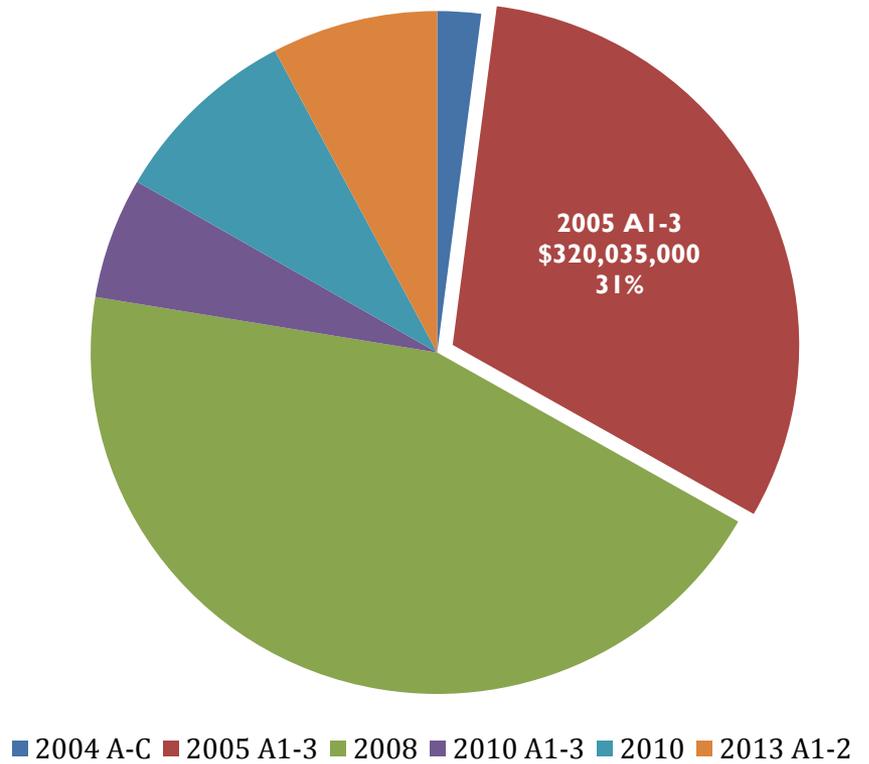


*Excludes outstanding QZAB (\$6,350,000) - all sinking fund payments have been made.

Outstanding COP Obligations

Series	Outstanding	As % of COP
2004A	\$3,585,000	0.35%
2004B	\$13,680,000	1.33%
2004C	\$3,600,000	0.35%
2005 A-1 (Ref)	\$194,590,000	18.98%
2005 A-2 (Ref)	\$73,875,000	7.20%
2005 A-3 (Ref)	\$51,570,000	5.03%
2008	\$454,870,000	44.36%
2010 A-1 (Ref)	\$11,100,000	1.08%
2010 A-2 (Ref)	\$10,000,000	0.98%
2010 A-3 (Ref)	\$37,685,000	3.68%
2010	\$81,820,000	8.91%
2013 A-1 (Ref)	\$29,945,000	2.92%
2013 A-2 (Ref)	\$49,605,000	4.84%
	\$1,015,925,000	100.00%

Taxable Refunding Opportunity



LEGISLATIVE CRITERIA

- Laws 2013, First Special Session, Chapter 3, Section 48
 - Authorization to enter into refunding agreement in fiscal year 2013-2014
 - Required to reduce SFB FY 2013-14 and FY 2014-15 lease-purchase payments, combined, by at least \$4,000,000
 - Change in lease-purchase payments in other years limited to \$100,000

TAXABLE REFUNDING OPPORTUNITY

Series 2005 A1-3 Refunding Analysis

Summary of Certificates Being Refunded*

SERIES	MATURITY	INTEREST RATE	PAR AMOUNT	CALL DATE
2005 A-1	9-1-16	5.0%	\$49,700,000	9-1-15
2005 A-1	9-1-17	5.0%	\$52,005,000	9-1-15
2005 A-2	9-1-16	5.0%	\$17,765,000	9-1-15
2005 A-2	9-1-17	5.0%	\$18,680,000	9-1-15
2005 A-2	9-1-18	5.0%	\$19,635,000	9-1-15
2005 A-3	9-1-16	3.7%	\$230,000	9-1-15
2005 A-3	9-1-17	5.0%	\$16,150,000	9-1-15
2005 A-3	9-1-18	5.0%	\$16,955,000	9-1-15
2005 A-3	9-1-19	5.0%	\$17,800,000	9-1-15

*Subject to change.

Upfront Savings meeting Legislative Criteria (as of 2-27-14)*

Estimated Debt Service Savings by Fiscal Year

	Series A-1	Series A-2	Series A-3	Total
FY 2014	\$0	\$0	\$0	\$0
FY 2015	4,079,963	2,116,881	1,725,855	7,922,698
FY 2016	(167,473)	95,798	169,954	98,278
FY 2017	2,678	2,479	92,826	97,982
FY 2018	4,604	4,397	90,422	99,422
FY 2019		2,988	96,877	99,865
FY 2020			99,465	99,465
Total	\$3,919,771	\$2,222,542	\$2,275,397	\$8,417,710

*Subject to change. Estimated savings are based on interest rates and other factors that are subject to change based on market conditions at the time of sale.

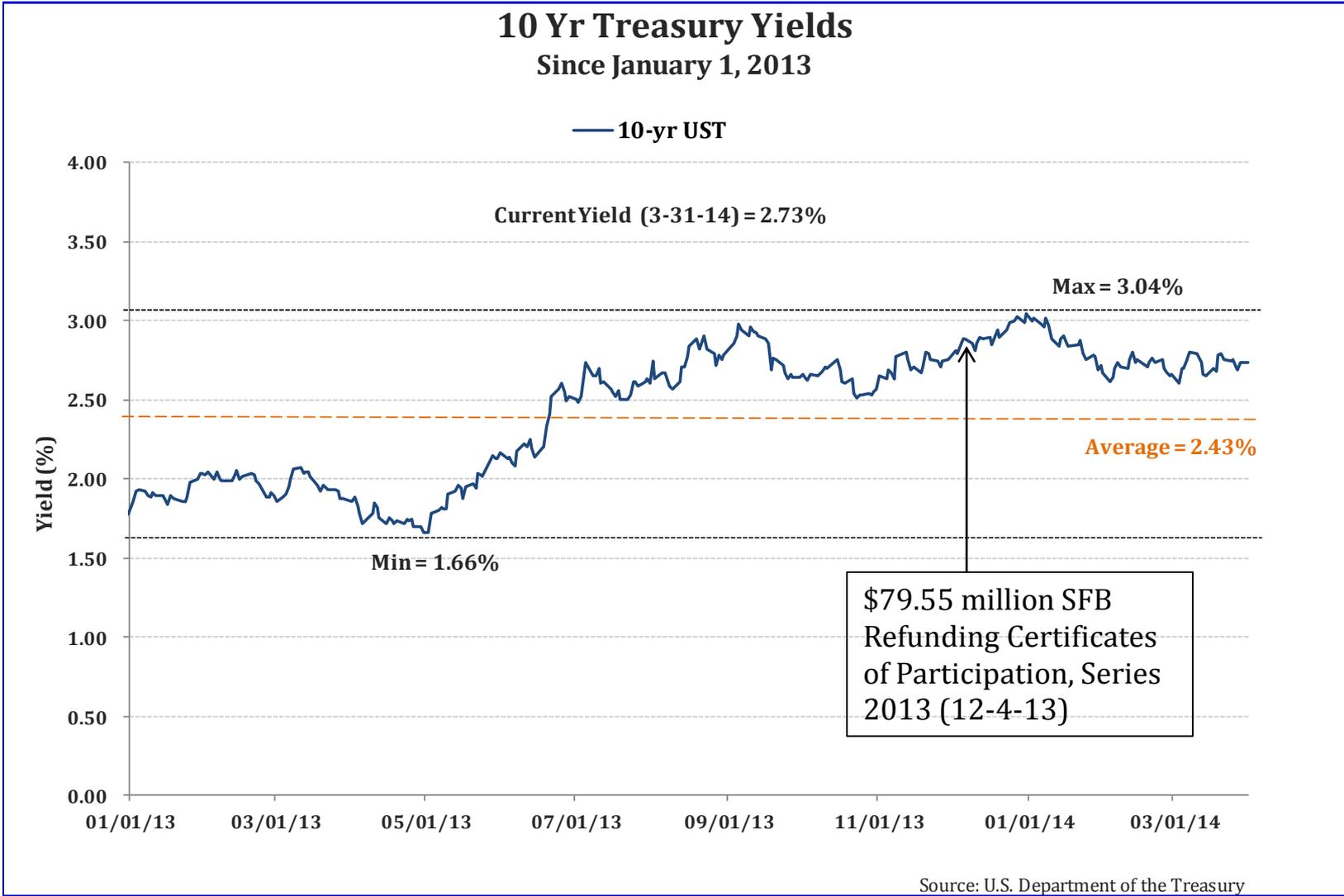
Summary of Up-Front Savings Scenario*

Dated Date	5-1-14
Refunded Certificates	\$208,920,000
Refunding Certificates	\$226,430,000
All-In True Interest Cost	1.595194%
Estimated FY 2014 and FY 2015 Debt Service Savings	\$7,922,698
Total Estimated Debt Service Savings	\$8,417,710
Estimated Savings on Present Value (PV) Basis	\$9,611,073
% Savings of Refunded Certificates	4.600360%
Negative Arbitrage**	\$3,776,454
Negative Arbitrage as % of Estimated PV Savings	39.29%

*Assumptions and market conditions are subject to change. Debt service savings are estimated and subject to change based on market conditions and other factors at the time of pricing.

**Negative Arbitrage represents the lost opportunity from funding an escrow to retire the prior bonds or certificates at a yield that is less than the maximum allowable arbitrage yield.

Benchmark Yield



Transaction Challenges

- Legislative criteria for FY 2013-14/FY 2014/15 savings
 - FY 2013-14 payment dates have passed, no savings can be realized
 - Majority of savings to be realized in FY 2014-15
- Legislative requirement to execute transaction by June 30, 2014
- Taxable Refunding Certificates
 - Refunding of a tax-exempt refunding
 - Certificates to be refunded are not callable until 9-1-15

TIMELINE OF KEY STEPS

Preliminary Financing Timeline – subject to change

March 2014						
S	M	T	W	TH	F	S
						1
2	3	4	5	6	7	8
9	10	11	12	13	14	15
16	17	18	19	20	21	22
23	24	25	26	27	28	29
30	31					

April 2014						
S	M	T	W	TH	F	S
		1	2	3	4	5
6	7	8	9	10	11	12
13	14	15	16	17	18	19
20	21	22	23	24	25	26
27	28	29	30			

May 2014						
S	M	T	W	TH	F	S
				1	2	3
4	5	6	7	8	9	10
11	12	13	14	15	16	17
18	19	20	21	22	23	24
25	26	27	28	29	30	31

June 2014						
S	M	T	W	TH	F	S
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30					

Key Financing Step	TARGET DATE
Distribute RFI to State Underwriting Pool	March 26
Governing Board Consideration of Refunding Resolution	April 2
RFI Proposals Due from Underwriting Firms	April 8
Review by Legislative Joint Committee on Capital Review	TBD
Team Distribution of Draft Preliminary Official Statement	April 11
Select Underwriting Team	April 11
Applications/Materials Submitted to Rating Agencies	April 21
Governing Board Distribution of Preliminary Official Statement	April 21
Governing Board Review of Preliminary Official Statement	May 7
Receive Ratings	May 9
Certificate Pricing	May 20/21
Certificate Closing	June 11

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