



City of Palo Alto City Manager's Summary Report

TO: HONORABLE CITY COUNCIL

FROM: CITY MANAGER

**DEPARTMENT: ADMINISTRATIVE
SERVICES**

DATE: OCTOBER 20, 2008

CMR: 420:08

REPORT TYPE: INFORMATIONAL

SUBJECT: Response to Frequently Asked Questions (FAQ) About Issuance and Administration of Measure N Library General Obligation Bonds

This is an informational report and no Council action is required.

BACKGROUND

In the November 2008 General Election, Palo Alto voters are being asked to vote on Measure N which would give the City authority to issue up to \$76 million in General Obligation Bonds. Proceeds from the issue would be used for capital improvements to the Mitchell Park Library and Community Center as well as the Main and Downtown libraries. A number of frequently asked technical and strategic questions have been raised about this potential bond issue and responses are presented below for public information. Several of these questions are a consequence of recent turmoil in the financial markets.

DISCUSSION

Q. What is the maximum amount the City can issue in bonds for Measure N?

A. The City can issue, at once or over time, a maximum of \$76 million in bonds, the amount cited in Measure N.

Q. How is annual debt service determined?

A. There are 3 factors which determine annual debt service: the amount borrowed, the amortization period for bond repayment, and the interest rate. Two of the three variables have been decided: a maximum of \$76 million in borrowing and a 30 year amortization period for the projects. When the interest rate is determined at the time bonds are sold, an annual debt service schedule will be established.

Q. What is the estimated annual debt service based on the 3 factors cited in the previous question and response?

A. The estimated, average annual debt service based on the 3 factors is \$5.1 million.

Q. How is the annual tax rate per \$100,000 of assessed value determined?

A. Prior to the beginning of each fiscal year, the County will be sent the annual debt service amount for the General Obligation bonds. This amount will be divided by the cumulative assessed value for the City of Palo Alto and a rate per \$100,000 of assessed value is calculated. This rate is then applied to each parcel's assessed roll value and a tax is determined and placed on each property tax bill. Each year this calculation will be done anew, so as assessed values for the City and for individual parcels change so will the rate per \$100,000 and the tax for each individual property.

The tax rate cited in ballot information, \$27 per \$100,000, was an estimate based on all of the factors cited above and on available assessed value information from the county. The interest rate assumed in this calculation was 5.43 percent which the City's Financial Advisor identified as a conservative rate. This rate is still slightly below current market rates based on a triple A credit rating.

Q. What is the estimated share of annual debt service that will be paid by residents and businesses?

A. The estimated share is 60 percent for residents and 40 percent for businesses.

Q. What flexibility does the City have in issuing General Obligation (GO) bonds in terms of timing and project needs?

A. There is no required timeline for issuing GO bonds once issuance is approved. The City would have the flexibility and discretion to issue bonds when cash is needed for projects and/or when interest rates are favorable.

Q. Can the City issue one or more bonds so as to time funding with project timelines?

A. The City can implement one or more bond issues or series to match the funding requirements and timing for each project. With each bond issue, however, the City incurs issuance costs for legal, trustee, and financial adviser fees for example. These costs are can range from \$125,000 to \$200,000.

Q. If the City issues 2 series of bonds, will the interest rate for the first series be the same as the second series?

A. No. Interest rates are determined on the date of sale of each series of bonds.

Q. What is the timeframe for issuing the first set of bonds?

A. At this time, the anticipated construction dates are Spring 2010 for the Mitchell Park Library and Community Center, and for the Downtown Library. Main Library construction is to start in early 2012. The first series of bonds would be issued just prior to construction in Spring 2010 and the second series just prior to construction in early 2012.

Q. How will current market and financial conditions affect the interest rate?

A. Current market conditions are extremely volatile and interest rates are highly variable given credit and liquidity concerns. This is not a "normal" market to issue bonds. The City and its Financial Advisor continue to monitor the bond issuance market and, at this time, believe it is responsible to wait until more favorable bond market conditions emerge.

Q. Since Palo Alto is one of a handful of cities with a triple A credit rating and minimal debt, is it likely to get the lowest rates in the market?

A. With each new bond issue, the City's financial status is evaluated by the credit rating agencies. The City currently has a triple A underlying credit rating for General Obligation bonds. While the City has low debt levels, solid demographics, diverse revenue sources, and strong reserves, rating agencies such as Standard and Poor's will take a critical look at General Fund finances, particularly in the current debt market. Historically, however, City debt has been viewed favorably by investors resulting in comparatively low interest rates.

Q. In January 2009, funding will be required to complete design for the proposed projects and in order to move the projects forward. Since these funds will be needed before the City issues bonds, where will the money come from?

A. The City will advance these funds from its General Fund Infrastructure Reserve. This advance will be repaid after the GO bonds are issued so other critical General Fund infrastructure projects can be implemented.

Q. What assurance does the public have that money raised through the bond issue will be spent appropriately and efficiently?

A. There are a number of mechanisms designed to allay this concern. A bond oversight committee that consists of residents will be appointed by the City Council. In addition, the City Auditor will perform audits of the bond issuance and how bond funds are spent. Finally, each bond issue's documentation will contain specific and clear requirements as to how bond proceeds can be used and these are strictly followed by City staff and monitored by outside agencies and bondholders.

Q. Should final construction costs be lower than estimated, how will remaining project funds be used?

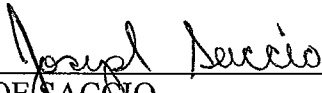
A. If there are remaining project funds once the projects are complete, those monies can be used to offset annual debt payments and lower the annual assessment to property owners. If significant funds remain, the City may be able to redeem bonds and lower the annual

assessment over the life of the bonds. If remaining funds are not significant, then assessments could be reduced for one or perhaps two years.

Q. Can the City refinance the General Obligation bonds if interest rates decline in the future?

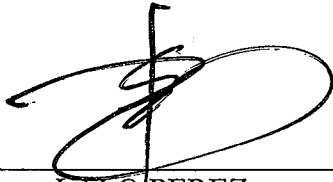
A. Provided certain pledges to bondholders are met, the City has the option to refinance these bonds in the future. The City and its financial advisor frequently review outstanding bonds to determine whether savings can be realized from refinancing. A net present value calculation is performed and if it demonstrates material savings a refinancing will be considered.

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