REDEVELOPMENT AGENCY
AND THE CITY OF OAKLAND
AGENDA REPORT

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TO: Office of the City Administrator/
Executive Director of the Oakland Joint Powers Financing Authority
ATTN: Deborah A. Edgerly
FROM: Finance and Management Agency
DATE: March 18, 2008

RE: **Supplemental Report To Approving The Issuance And Sale Of Refunding Revenue Bonds To Refund The Authority's Outstanding Refunding Lease Revenue Bonds (Oakland Administration Buildings) In One Or More Series To Refund The Authority's Outstanding Refunding Lease Revenue Bonds, 2004 Series A-1 (Auction Rate Securities) (Tax-Exempt Bonds), And 2004 Series A-2 (Auction Rate Securities) (Tax-Exempt Bonds)**

SUMMARY

This supplemental report responds to the Finance and Management Committee's request on March 11, 2008, for staff to explain the fiscal impact associated with refunding the 2004 Auction Rate Securities (ARS).

FISCAL IMPACT

Over the past several weeks, the underlying 2004 ARS rates have reset at the maximum rate of approximately 6%. This resulted in the City experiencing an interest rate differential, which is costing the City over **$60,000 each week** in additional borrowing costs. This increased interest cost was not anticipated in 2004 when the City entered into an interest rate swap agreement.

While this additional interest cost could decrease at some point, there is no certainty of this occurring (and to what extent) given the volatility in the market place. The City made a solid financing decision back in 2004 when it entered into a swap agreement and sold ARS. None of the recent market developments could have been anticipated. Nonetheless, the current ARS/swap structure exposes the City to ongoing variable rate and derivative risks, and most importantly, budgetary uncertainty.

By refunding the ARS (and terminating the swap) with fixed rate bonds, the City achieves <u>complete</u> interest rate cost certainty and eliminates all financial risks. Based on current insured market conditions, the City could potentially lock in interest rates at near historic 25-year lows. More importantly, a fixed rate refunding would relieve the City of the high maximum interest rates currently paid if the ARS continue to fail in the market.

As a final observation, staff compared the cost had the City issued fixed rate bonds in 2004 with the costs to issue variable rate bonds, hedged by a swap, and reissuing fixed rate bonds in 2008. The proposed solution (terminating 2004 swap and issuing fixed rate refunding bonds in 2008), would generate $4.7 million in lower debt service, when compared to issuing fixed rate bonds in 2004.

These debt service payments will continue to be paid by the City's general fund. Other costs related to the financing will be paid by costs of issuance upon closing.

Respectfully submitted,

WILLIAM E. NOLAND
Director, Finance and Management Agency/
Treasurer

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APPROVED AND FORWARDED TO THE
CITY COUNCIL:

Office of the City Administrator/
Executive Director of the Oakland JPFA