

Metropolitan Water District of Salt Lake & Sandy
Board Packet Information
Last Update: August 5, 2011

Agenda Item: Consider approval of resolution authorizing the issuance of up to \$15 million of water revenue bonds; and related matters.

Objective: Seek board authorization of the bond parameters resolution.

Background: The enclosed analysis by Zions Bank Public Finance and the related bond parameters resolution were discussed at the Finance Committee meeting held on August 4, 2011. The recommended action was to proceed with a new revenue bond in February 2012 pending the favorable results of the bid process of the Terminal Reservoir Project (bid opening is scheduled for September 14). The process for the new bond will be coupled with a refunding of one or more existing bonds.

Committee Activity: The Finance Committee has reviewed the enclosed information and recommended that the resolution be forwarded to the full board for consideration.

Recommendation: Approval.

Included in this packet of information are four items of discussion.

1. Bond now or later for Terminal Reservoir
2. Bond refunding
3. Fix variable rates or let them float
4. Swap options

To Bond Now or Later?

It is contemplated that Metropolitan Water District of Salt Lake & Sandy will construct the Terminal Reservoir. If construction bids come in as expected, project costs will be significantly lower than the costs estimated for a later construction commencement. The District has cash available to cover some of the costs associated with the project, and it is advisable to use a combination of cash and debt to maintain the strong bond ratings of the District.

Currently, Standard and Poor's rates the District AA+ and Fitch Ratings rates the District AA. It is anticipated that approximately \$6.6 million of cash reserves could be utilized for the project with such action reducing Days Cash on Hand (a key rating ratio) from about 740 days to about 570 days. Both very strong and both well above the medians for AA rated issuers (365 days in 2010). The rating analysts are used to seeing the District average about 600 days which has in the past offset narrow projected coverage ratios of as low as 1.26 times. In 2010, the coverage was 1.5 times. As discussed previously, the project timeline is about 7 years. Due to IRS regulations, bond proceeds must be spent within a three-year window from the bond closing. This analysis assumes two bond issues spread out over three years with the first commencing in either November 2011 or February 2012 (see below for further discussion), or November 2012. The issue dates are flexible.

The decision to utilize cash now or later has been analyzed based upon your earning power now and the earning potential over the course of the project (about 7 years), and the current and estimated cost of borrowing in the future. Cash now or later means the District spends cash over the next year or waits until the end of the project life (about 7 years) and spends the cash then.

Your cash today earns about .5%. Your borrowing costs today are estimated to be about 3.8%, meaning the District incurs negative arbitrage of 3.3% (3.8% minus .5%) for one year. Assuming a bond issue of \$12.055 million the negative arbitrage costs the District \$397,815, which is one year of interest on the full amount borrowed. This amount could have been avoided had the District waited a year to issue bonds and used its cash for the first year of projects.

Another considerations include the earning potential of the cash while it is held over until the end of the construction term. As illustrated on the handout, if the earning rate stays at about .5%, over the almost 7 years the cash is invested, the District generates approximately \$220,000. If the average rate over the next 7 years climbs to 1%, the cumulative earnings would be \$452,000. The 20-year average interest rate at the Public Treasurer's Investment Fund is 3.91%.

Yet another consideration is whether borrowing rates today will be the same a year from now. If borrowing rates increase by .25% over the course of the next year, the District would avoid the \$397,815 negative arbitrage, but pay \$802,000 more over the life of the financing as illustrated on the handout. If rates remain the same over the course of the next year, just due to the timing of project costs, the financing cost about \$6,000 more than financing today.

The question of whether to use cash now versus later is answered by our prediction of interest rates in the future. As illustrated on the handout, we're still at historically low levels. It is not hard to envision rates going up.

To issue bonds in November 2011 as opposed to February 2012 is simply a matter of interest rate expectations. To issue in February, assuming rates today prevail through February would save the District approximately \$174,000, or about four months of interest expense. If rates in February go up about 5.5 basis points or .055%, we break even.

As shown on the attached handout, if rates increase by .25%, our \$174,000 savings generated by waiting goes away and we end up paying about \$600,000 over the life of the bonds.

Bond Refunding

Also of interest is that the District has two series of bonds that are eligible for refunding today. Eligibility is based upon an industry standard that net present value savings (after costs, transfers from reserves, etc.) total at a minimum 3% of the new bond amount. As illustrated, the 2003 and 2004 bonds are just above that threshold and have been for a few months. The District's 2002B bonds are considerably higher at 10% NPV savings, but cannot be refunded until 2012 because they were already refunded once back in 2002. The IRS only allows one refunding opportunity in advance of the call date.

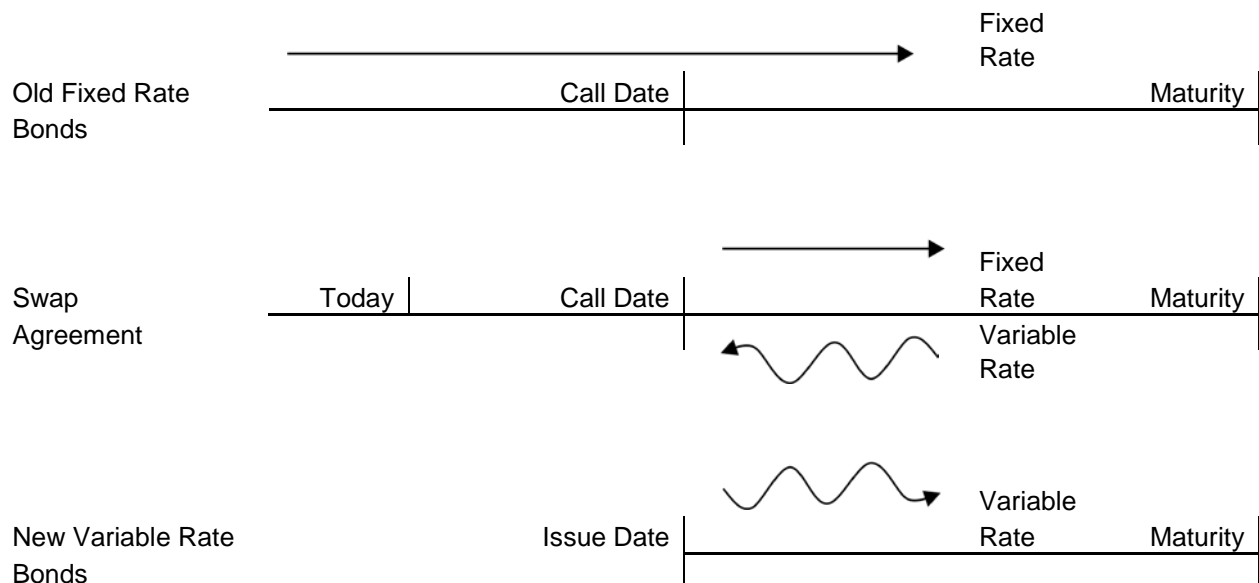
Although the 2002B bonds are not callable until July 1, 2012, it is possible to close within 90 days prior to the call date and sell bonds, locking in rates about 45 days prior to that. This would presume we are selling bonds around February 15, 2012. Based upon the significant savings associated with the 2002B bonds, we'd anticipate a bond issue in February regardless of other decisions made.

The only other ways to skirt the "one-time" advance refunding rule is to sell bonds on a taxable basis, that later convert to tax exempt bonds on a specific date in the future. Not coincidentally, these bonds are called Cinderella Bonds.

We contemplate including the refunding bonds with the Terminal Reservoir bonds, presuming they are issued. So doing saves upfront costs and the time and effort of District staff wading through the process.

Alternatively, Wells Fargo has proffered a "synthetic advance refunding," which involves the use of a forward starting swap. We set the interest rates on a swap today. On the call date of each series of bonds to be refunded (2012, perhaps 2013, and 2014), we issue variable rate debt that is used to pay off the old bonds and is swapped to a fixed rate determined today.

Synthetic Advanced Refunding



The benefits of so doing include:

- No negative arbitrage on a refunding escrow (currently over \$1 million on the 2003 and 2004 bonds)
- Wells Fargo documents used on prior transaction would be very similar going forward

The risks are the same on this swap as any other swap and include the following:

- Counterparty risk to Wells Fargo as a swap provider
- Tax risks due to changes in tax law, audit requirements, etc.
- Termination / Market risk
- Basis risk
- Systemic risk
- Remarketing / Liquidity risk associated with the underlying variable issue

To Fix or Float?

There is the discussion of fixing a portion of the outstanding, true variable rate bonds. The District has approximately \$35 million of true variable rate bonds outstanding. Variable rates are at historic lows. However, by the time the interest rates on variable rate obligations move up, the long term, fixed rates will have increased commensurately. By splitting the true variable rate issues into two parts and selling at separate times, we hedge our bet that rates will go up. We fix a portion at historically low long-term rates and leave a portion outstanding at historically low variable rates. Current economic projections suggest interest rates will remain constant through 2011 with increases commencing the middle part of 2012 . . . debt ceiling issue and potential US default excluded.

The District has about \$58 million of its variable rate debt swapped to fixed interest rates. As the value of the District's swaps improves, we will be able to terminate those swaps and expose true variable rate bonds at that time. The termination payment made to the District could be utilized to pay a portion of the additional interest expense that then would be present on variable rate obligations. Currently the true variable rate debt amounts to about 13% of the District's outstanding debt.

Swap Options

For our benefit, Wells Fargo has also presented to the District the concept of entering into an agreement called a Swaption. This is an agreement providing Wells Fargo or other provider with the option to terminate the District's existing swaps on a specific date in time. The Swaption provider receives any benefit derived by the termination in exchange for an up front payment to the District.

The value of the Swaption is based upon the provider's expectations that interest rates will rise, the swaps will be terminated and they will make more money than they pay the District to enter into the agreement. If they are wrong, they will not exercise their option and the swaps stay intact.

They have also offered to restructure our current swaps, roll the termination fees into a new swap rate and perhaps still provide a better, fixed rate swap.

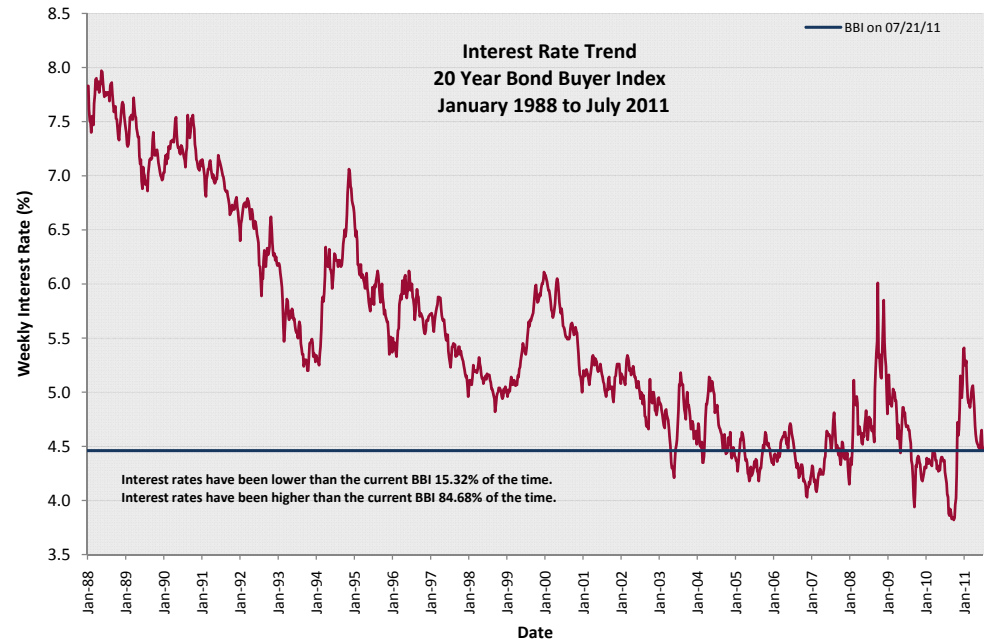
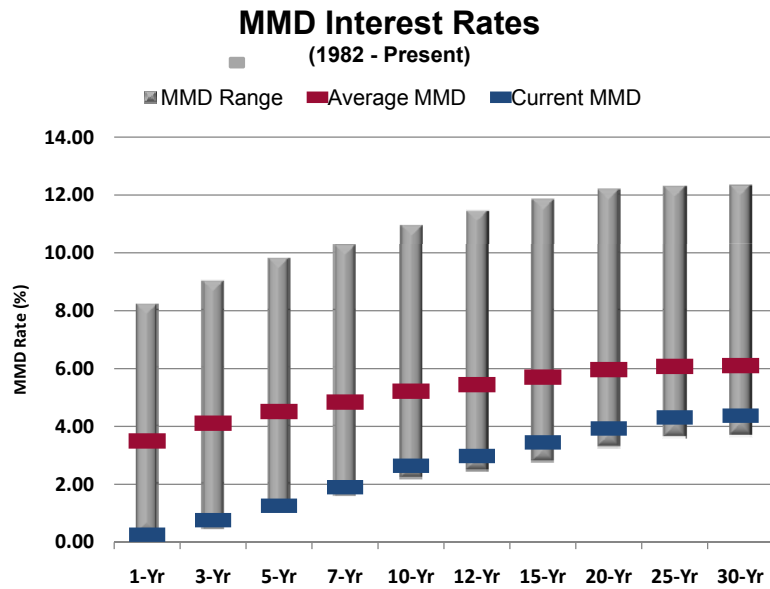
Metropolitan Water District of Salt Lake & Sandy

Financing Analysis

Option 1: Issue Now, Use Cash Later	Issue Month	Average AIC	Total P+I	Total P+I Difference with Base Case	Average DS
	Series 2011B and Series 2014 (Base Case)	Nov	3.812%	36,067,376	-
Series 2012 and Series 2014	Feb	3.826%	35,893,051	(174,325)	1,560,567
Break Even at +5bps	Feb	3.829%	36,049,292	(18,084)	1,567,361
Break Even at +6bps	Feb	3.887%	36,080,569	13,193	1,568,720
+25bps	Feb	4.081%	36,667,828	600,452	1,594,253
+50bps	Feb	4.338%	37,462,537	1,395,161	1,628,806
+75bps	Feb	4.595%	38,257,182	2,189,806	1,663,356
+100bps	Feb	4.723%	38,626,309	2,558,932	1,679,405
Option 2: Use Cash Now, Issue Later					
Series 2012 and Series 2015	Nov	3.819%	36,073,435	6,058	1,503,060
+25bps	Nov	4.075%	36,869,745	802,369	1,536,239
+50bps	Nov	4.332%	37,681,798	1,614,422	1,570,075
+75bps	Nov	4.588%	38,502,733	2,435,357	1,604,281
+100bps	Nov	4.845%	39,322,629	3,255,252	1,638,443

Earning Potential on \$6,599,382 Cash		
Interest Rate	First Year Earnings	6.5 Years Cumulative Earnings
0.50%	32,997	223,139
1.00%	65,994	452,697
2.00%	131,988	931,687
3.00%	197,981	1,438,225
4.00%	263,975	1,973,617
5.00%	329,969	2,539,214
6.00%	395,963	3,136,421

Potential Refunding Summary						
Issues Refunded	Par Amt	AIC	TIC	NPV Savings %	NPV Savings \$	Avg Savings
Series 2003 and Series 2004	24,495,000	3.017%	2.912%	3.168%	708,002	67,322
Series 2002B	14,140,000	2.975%	2.733%	10.726%	1,494,626	145,979



RESOLUTION NO. 1852

A RESOLUTION AUTHORIZING THE ISSUANCE OF UP TO \$15,000,000 AGGREGATE PRINCIPAL AMOUNT OF WATER REVENUE BONDS OF THE METROPOLITAN WATER DISTRICT OF SALT LAKE & SANDY, FIXING THE MAXIMUM AGGREGATE PRINCIPAL AMOUNT OF THE BONDS, THE MAXIMUM NUMBER OF YEARS OVER WHICH THE BONDS MAY MATURE, THE MAXIMUM INTEREST RATE WHICH THE BONDS MAY BEAR AND THE MAXIMUM DISCOUNT FROM PAR AT WHICH THE BONDS MAY BE SOLD; AUTHORIZING THE PUBLICATION OF A NOTICE OF BONDS TO BE ISSUED, AUTHORIZING THE PUBLICATION OF A NOTICE OF PUBLIC HEARING AND THE HOLDING OF A PUBLIC HEARING; AND RELATED MATTERS

WHEREAS, the Board of Trustees (the “*Board*”) of the Metropolitan Water District of Salt Lake & Sandy (the “*District*”) considers it desirable and necessary and for the benefit of the District to issue its water revenue bonds (the “*Bonds*”) for the purpose of financing the costs of acquisition and construction of reservoirs, pipelines, pump stations, water tanks, treatment facilities, and related improvements (the “*Project*”), providing any necessary reserves, and paying costs of issuing the Bonds, pursuant to authority contained in Title 17B, Chapter 1, Part 11, Utah Code Annotated 1953, as amended; Title 17B, Chapter 2a, Part 6, Utah Code Annotated 1953, as amended; and the Local Government Bonding Act, Title 11, Chapter 14, Utah Code Annotated 1953, as amended (collectively, the “*Act*”);

WHEREAS, the Board now desires to (a) publish a Notice of Bonds to Be Issued pursuant to Section 11-14-316 of the Act; (b) provide for the holding of a public hearing pursuant to Section 11-14-318 of the Act, and (c) direct the publication of a Notice of Public Hearing (the “*Notice of Public Hearing*”); and

WHEREAS, expenditures relating to the Project (the “*Expenditures*”) have been paid from District funds within 60 days prior to the passage of this resolution (the “*Resolution*”) or will be paid from such funds on or after the passage of this Resolution and prior to the issuance of the Bonds;

NOW, THEREFORE, Be It Resolved by the Board of Trustees of the Metropolitan Water District of Salt Lake & Sandy, as follows:

Section 1. Bonds to Be Issued. The Board hereby finds and determines that it is desirable and necessary and for the benefit of the District for it to issue, in one or more series, for the purpose of financing the costs of the Project, providing any necessary reserves, and paying costs of issuing the Bonds, not more than \$15,000,000 aggregate principal amount of its water revenue bonds, to mature in not more than 30 years from their date or dates, to bear interest at a

rate or rates not to exceed 6% per annum, and to be sold at a discount from par, expressed as a percentage of principal amount, of not to exceed 3%, all in accordance with and pursuant to the provisions of (1) a Master Resolution Providing for the Issuance of Water Revenue Bonds, adopted April 29, 2002, as amended and supplemented (the “*Master Resolution*”), a copy of which is attached as *Annex 1*, and (2) one or more Supplemental Resolutions (collectively, the “*Supplemental Resolution*”) supplementing the Master Resolution, to be adopted at a future date, a draft of which is attached as *Annex 2*, and the Board hereby declares its intention to issue the Bonds according to the provisions of this section.

Section 2. Authorization. The Board hereby authorizes and approves the issuance of the Bonds for the purpose of financing the costs of the Project, providing any necessary reserves, and paying costs of issuing the Bonds, pursuant to the provisions of this Resolution, the Master Resolution and the Supplemental Resolution; *provided* that the principal amount, interest rate or rates, maturity or maturities, and discount shall not exceed the maximums set forth in Section 1 hereof.

Section 3. Publication of Notice of Bonds to Be Issued. In accordance with the provisions of Section 11-14-316 of the Act, the Clerk of the District (the “*Clerk*”) shall cause the following Notice of Bonds to Be Issued to be published one time in the *Deseret News* and *The Salt Lake Tribune*, newspapers of general circulation in the District, and shall cause a copy of this Resolution, together with the annexes thereto, to be kept on file in the office of the Clerk for public examination during the regular business hours of the Clerk for at least 30 days after the date of such publication. The Notice of Bonds to Be Issued shall be in substantially the following form:

NOTICE OF BONDS TO BE ISSUED

NOTICE IS HEREBY GIVEN pursuant to the provisions of Section 11-14-316, Utah Code Annotated 1953, as amended, that on August 15, 2011, the Board of Trustees (the “*Board*”) of the Metropolitan Water District of Salt Lake & Sandy (the “*District*”) adopted a resolution (the “*Resolution*”) in which it authorized the issuance of one or more series of the District’s water revenue bonds (the “*Bonds*”) in an aggregate principal amount of not to exceed \$15,000,000, to mature in not more than 30 years from their date or dates, to bear interest at a rate or rates not to exceed 6% per annum, and to be sold at a discount from par, expressed as a percentage of principal amount, of not to exceed 3%.

The Bonds are to be issued and sold by the District pursuant to (1) the Resolution, (2) a Master Resolution Providing for the Issuance of Water Revenue Bonds, adopted April 29, 2002, as amended and supplemented (the “*Master Resolution*”), and (3) one or more Supplemental Resolutions supplementing the Master Resolution, to be adopted at a future date (collectively, the “*Supplemental Resolution*”). The form of the Supplemental Resolution, in substantially final form, and a copy of the Master Resolution were attached to the Resolution at the time of the adoption of the Resolution. The Supplemental Resolution will be adopted by the Board at a future date prior to the issuance of the Bonds in substantially the form attached to the Resolution, with such changes thereto as shall be approved by the Board upon the adoption of the

Supplemental Resolution, *provided* that the principal amount, interest rate or rates, maturity or maturities and discount will not exceed the maximums set forth above.

The Bonds are to be issued for the purpose of financing the costs of acquisition and construction of reservoirs, pipelines, pump stations, water tanks, treatment facilities, and related improvements (the "*Project*"), providing any necessary reserves, and paying costs of issuing the Bonds, all as set forth in the Resolution, the Supplemental Resolution, and the Master Resolution.

A copy of the Resolution (including the Master Resolution and a draft of the Supplemental Resolution) is on file in the office of the Clerk of the District, located at 3430 East Danish Road, Cottonwood Heights, Utah, where it may be examined during regular business hours of the Clerk from 8:00 a.m. to 4:00 p.m., Monday through Thursday. The Resolution (including the Master Resolution and a draft of the Supplemental Resolution) shall be so available for inspection for a period of at least 30 days from and after the date of the publication of this notice.

NOTICE IS FURTHER GIVEN that pursuant to law for a period of 30 days from and after the date of the publication of this notice, any person in interest shall have the right to contest the legality of the above-described Resolution (including the Supplemental Resolution) of the Board, or the Bonds or any provisions made for the security and payment of the Bonds, and that after such time, no one shall have any cause of action to contest the regularity, formality or legality thereof for any cause.

DATED this 15th day of August, 2011.

METROPOLITAN WATER DISTRICT OF SALT
LAKE & SANDY

By _____
Clerk

Section 4. Contestability. For a period of 30 days after publication of the Notice of Bonds to Be Issued, any person in interest shall have the right to contest the legality of the resolutions pursuant to which the Bonds are to be issued, or of the Bonds thereby authorized or any provisions made for the security and payment of the Bonds. After such time, no person shall have any cause of action to contest the regularity, formality or legality of the resolutions or the Bonds for any cause whatsoever.

Section 5. Public Hearing. In satisfaction of the requirements of Section 11-14-318, Utah Code Annotated, as amended, a public hearing shall be held by the Board at its regular meeting that begins at 4:30 p.m. on September 19, 2011, at the regular meeting place of the Board, located at 3430 East Danish Road, Cottonwood Heights, Utah, with respect to (i) the

issuance by the District of the Bonds for the purpose of financing certain costs of the Project and (ii) the potential economic impact of the Project.

Section 6. Publication of Notice of Public Hearing. The District Clerk shall cause the Notice of Public Hearing, in substantially the following form, to be published once each week for two consecutive weeks in the *Deseret News* and *The Salt Lake Tribune*, newspapers of general circulation in the District, with the first publication being at least 14 days prior to the date set for the public hearing:

**NOTICE OF PUBLIC HEARING
METROPOLITAN WATER DISTRICT OF SALT LAKE & SANDY**

PUBLIC NOTICE IS HEREBY GIVEN pursuant to Section 11-14-318, Utah Code Annotated 1953, as amended, that, on August 15, 2011, the Board of Trustees (the “*Board*”) of the Metropolitan Water District of Salt Lake & Sandy (the “*District*”) adopted a resolution providing for the issuance of up to \$15,000,000 of water revenue bonds (the “*Bonds*”) of the District and calling a public hearing to receive input from the public with respect to the issuance of the Bonds and the potential economic impact that the improvements, facilities, or properties to be financed in whole or in part by the Bonds will have on the private sector.

The District intends to issue the Bonds for the purpose of financing the costs of acquisition and construction of reservoirs, pipelines, pump stations, water tanks, treatment facilities, and related improvements (the “*Project*”), providing any necessary reserves, and paying costs of issuing the Bonds. The District intends to issue the Bonds in an amount not to exceed \$15,000,000.

The District will not pledge any taxes of the District for the payment of the Bonds. Instead, the District will pledge, pursuant to that certain Master Resolution Providing for the Issuance of Water Revenue Bonds, adopted April 29, 2002, as amended and supplemented, the revenues attributable to the District’s water system for the payment of the Bonds.

The Board will hold a public hearing at its regular meeting that begins at 4:30 p.m. on September 19, 2011. The public hearing will be held at the regular meeting place of the Board, located at 3430 East Danish Road, Cottonwood Heights, Utah. All members of the public are invited to attend and participate in the public hearing. Prior to the public hearing, written comments may be submitted to the District, to the attention of the Clerk of the District, at 3430 East Danish Road, Cottonwood Heights, Utah.

The purpose of the hearing is to receive input from the public with respect to the issuance of the Bonds for the purpose of financing or refinancing all or part of the cost of the Project and the potential economic impact that the Project will have on the private sector.

DATED this 15th day of August, 2011.

METROPOLITAN WATER DISTRICT OF SALT
LAKE & SANDY

By _____
Clerk

Section 7. Ratification. All proceedings, resolutions and actions of the District and its officers taken in connection with the sale and issuance of the Bonds are hereby ratified, confirmed and approved.

Section 8. Severability. It is hereby declared that all parts of this Resolution are severable, and if any section, paragraph, clause or provision of this Resolution shall for any reason be held to be invalid or unenforceable, the invalidity or unenforceability of any such section, paragraph, clause or provision shall not affect the remaining provisions, paragraphs, clauses or provisions of this Resolution.

Section 9. Conflict. All resolutions, orders and regulations or parts thereof heretofore adopted or passed that are in conflict with any of the provisions of this Resolution are, to the extent of such conflict, hereby repealed.

Section 10. Captions. The captions or headings herein are for convenience of reference only and in no way define, limit or describe the scope or intent of any provisions or sections of this Resolution.

Section 11. Effective Date. This Resolution shall be in full force and effect immediately upon its adoption.

PASSED and APPROVED by the Board of Trustees of the Metropolitan Water District of Salt Lake & Sandy, this 15th day of August, 2011.

METROPOLITAN WATER DISTRICT OF SALT
LAKE & SANDY

By _____
Chair, Board of Trustees

ATTEST:

By _____
Clerk

[SEAL]

BOARD MEMBER	VOTE
John S. Kirkham	_____
Tom Godfrey	_____
Lee Kapaloski	_____
Donald Y. Milne	_____
Kathy W. Loveless	_____
David L. Buhler	_____
Patricia Comarell	_____

ANNEX 1

[MASTER RESOLUTION]

ANNEX 2

[SUPPLEMENTAL RESOLUTION]