

BOARD LETTER APPROVAL

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Ann M. Santilli (Feb 2, 2024 09:41 PST)

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DATE: January 31, 2024

SUBJECT: Authorization to Issue up to \$1.10 Billion of Power System Revenue Bonds Under Resolution Nos. 5049 and 5050

SUMMARY

Proposed Resolution Nos. 5049 and 5050 will authorize the issuance of up to \$1.10 billion of fixed-rate, tax-exempt Power System Revenue Bonds, in two separate series. The first series of Power System Revenue Bonds, 2024 Series A (Power 2024A Refunding Bonds) will refinance certain outstanding Power System Revenue Bonds, 2014 Series C (Power 2014C Bonds), 2014 Series D (Power 2014D Bonds), and 2014 Series E (Power 2014E Bonds) (together, the "Series A Refunded Bonds"), and to pay the related costs of the debt issuance. The second series of Power System Revenue Bonds, 2024 Series B (Power 2024B Refunding Bonds) will refinance certain outstanding Power System Revenue Bonds, 2010 Series A, Federally Taxable Build America Bonds (Power 2010A Bonds) and pay the related costs of the debt issuance. Depending on market conditions, two other smaller series of outstanding Power System Revenue Bonds, 2012 Series A (Power 2012A Bonds) and 2014 Series B (Power 2014B Bonds) (together, the "Low Coupon Refunded Bonds") totaling \$7.1 million may be refunded by either the Power 2024A Refunding Bonds or the Power 2024B Refunding Bonds.

The Power 2024A Refunding Bonds will primarily refund approximately half of the Series A Refunded Bonds that are callable on July 1, 2024, in order to manage market supply and establish appropriate pricing levels. The Power 2024A Refunding Bonds will replace higher interest debt from the Series A Refunded Bonds with lower debt service, which is estimated to provide an aggregate gross debt service savings of approximately \$76.97 million or approximately \$57.93 million in present value terms to the Power System over a period of twenty years or approximately average \$3.84 million annually based on interest rates for tax-exempt bonds as of January 23, 2024.

The Power 2024B Refunding Bonds will be issued to refinance the Power 2010A Bonds to remove the regulatory risks, provide new optionality for future refinancing, and provide actual cash flow and present value savings.

Resolution No. 5049 is a supplemental resolution to Resolution No. 4996. Resolution No. 4996 is the Initial Refunding Authorization to Issue up to \$2.20 billion of Power System Refunding Bonds, which was adopted by the Board of Water and Power Commissioners (Board) on November 16, 2021, and subsequently approved by the City Council.

Resolution No. 5050, if adopted, approves certain actions in connection with the issuance of the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds.

City Council approval is not required.

RECOMMENDATION

It is recommended that the Board adopt Resolution Nos. 5049 and 5050 authorizing the refinancing and issuance of up to \$1.10 billion of Power 2024A Refunding Bonds and Power 2024B Refunding Bonds.

ALTERNATIVES CONSIDERED

For the Power 2024A Refunding Bonds, LADWP can either continue to pay higher debt service and forego this refinancing opportunity to save approximately \$76.97 million over twenty years or wait for interest rates to potentially fall further from current levels.

For the Power 2024B Refunding Bonds, LADWP can continue to pay higher debt service, bear the regulatory risks associated with the Power 2010A Bonds and forego the optionality of future refinancing, and capture actual savings or wait until the regulatory risks outweigh the potential costs of a refunding.

FINANCIAL INFORMATION

Refunding of Series A Refunded Bonds

The proposed Power 2024A Refunding Bonds will be structured to allow LADWP maximum flexibility in refunding the Series A Refunded Bonds. LADWP intends to refund approximately half of the Series A Refunded Bonds and refund the remaining refunding candidates in the next refunding transaction during Fiscal Year 2024. Under favorable market conditions and sufficient investor demand, LADWP may refund entire maturities of the refunding candidates, which range from \$12 to 109 million, but would primarily target approximately \$400 million in refunding candidates for this transaction. If investor demand is weak, LADWP may refund fewer bonds and retain the option to

refund with the next refunding transaction. As of January 23, 2024, the total debt service cost of the Power 2024A Refunding Bonds for the Series A Refunded Bonds, including principal and interest, is estimated at \$543.55 million. This compares to the total refunded principal and interest costs of \$620.51 million. This refunding is expected to provide approximately \$76.97 million in gross savings, which is approximately \$57.93 million on a net present value basis, as shown in the table below. The amount of the savings depends on market conditions, and may vary up or down depending on interest rates as of the date of pricing tentatively slated in March 2024.

	Series A Refunded Bonds^{(1) (2) (3)} (\$ in million)	Power 2024A Refunding Bonds^{(1) (2)} (\$ in million)
Principal	\$400.31	\$352.71
Interest	220.20	190.84
Total Cash Flows	620.51	543.55
Cash Flow Savings	n/a	76.97
Present Value Savings (\$)	n/a	57.93
Present Value Savings (%)	n/a	14.47%

⁽¹⁾ subject to change based on market conditions at time of pricing

⁽²⁾ sized to refund approximately half of the Series A Refunded Bonds

⁽³⁾ does not include the Low Coupon Refunded Bonds

Total debt issuance costs are estimated at \$1.20 million, equivalent to 0.34 percent of the \$352.71 million estimated bond issue, which includes underwriters' discount, bond counsel, disclosure counsel, escrow, municipal advisor, and rating agencies fees.

CA Senate Bill 450

California Senate Bill 450, signed into law by Governor Brown on October 9, 2017, requires local issuers to obtain and disclose, prior to authorization of the bond issuance with a term greater than 13 months, good faith estimates of the following information as it relates to the Power 2024A Refunding Bonds:

- 1. True interest cost ^(a) 3.41%
- 2. Cost of Issuance ^(b) \$1,204,200
- 3. Bond proceeds ^(c) \$399,827,248
- 4. Total payment amount ^(d) \$543,867,314

^(a) the rate necessary to discount the amounts payable on the respective principal and interest payment dates to the purchase price received.
^(b) the sum of all fees and charges paid to third parties.
^(c) bond proceeds net of fees and charges paid to third parties.
^(d) the sum total of all debt service payments plus fees and charges paid to third parties not paid with bond proceeds and may not match Total Cash Flows

Refunding of Power 2010A Bonds

The Power 2010A Bonds are a federally taxable bond issue and are immediately callable under a “Make-Whole Premium.” This Make-Whole Premium determines a redemption price that is essentially equal to the discounted cash flows of the bonds, discounted by Treasury yields plus a spread. Over the last year, as treasury yields have increased, the discounted cash flows of the Power 2010A Bonds has decreased. In addition, as the ratio of tax-exempt yields to treasuries yields has decreased, replacing taxable bonds with tax-exempt bonds becomes more attractive. As of January 26, 2024, it is estimated that a reduction of tax-exempt yields by six basis points or a similar six basis points increase in Treasury yields, will allow for an economic refunding of the Power 2010A Bonds at a three percent net present value savings. Under current market conditions, the proposed refunding would result in 2.46 percent net present value savings. However, as discussed in the Background, by refunding the Power 2010A Bonds, LADWP will remove the regulatory risk related to the sequestration of interest rate subsidy payments and structure optionality through par call features. If there are any savings, LADWP plans to execute the refunding transaction to remove the regulatory risk and improve future restructuring optionality. As of January 26, 2024, the total debt service cost of the Power 2024B Refunding Bonds for the Power 2010A Bonds, including principal and interest, is estimated at \$460.78 million. This compares to the total refunded outstanding principal and interest costs of \$476.58 million. This refunding is expected to provide approximately \$15.80 million in gross savings, which is approximately \$7.77 million on a net present value basis, as shown in the table below. The amount of the savings depends on market conditions, and may vary up or down depending on interest rates as of the date of pricing tentatively slated in March/April 2024.

	Power 2010A Bonds^{(1) (2)} (\$ in million)	Power 2024B Refunding Bonds^{(1) (2)} (\$ in million)
Principal	\$316.00	\$275.25
Interest	160.58	185.53
Total Cash Flows	476.58	460.78
Cash Flow Savings	n/a	15.80
Present Value Savings (\$)	n/a	7.77
Present Value Savings (%)	n/a	2.46%

⁽¹⁾ subject to change based on market conditions at time of pricing

⁽²⁾ net of Internal Revenue Service Subsidies and anticipated sequestration rates

Total debt issuance costs are estimated at \$0.87 million, equivalent to 0.31 percent of the \$275.25 million estimated bond issue, which includes underwriters’ discount, bond counsel, disclosure counsel, escrow, municipal advisor, and rating agencies fees.

CA Senate Bill 450

California Senate Bill 450, signed into law by Governor Brown on October 9, 2017, requires local issuers to obtain and disclose, prior to authorization of the bond issuance with a term greater than 13 months, good faith estimates of the following information as it relates to the Power 2024B Refunding Bonds:

1. True interest cost ^(a)	3.22%
2. Cost of Issuance ^(b)	\$865,600
3. Bond proceeds ^(c)	\$328,956,572
4. Total payment amount ^(d)	\$461,028,791

^(a) the rate necessary to discount the amounts payable on the respective principal and interest payment dates to the purchase price received.

^(b) the sum of all fees and charges paid to third parties.

^(c) bond proceeds net of fees and charges paid to third parties.

^(d) the sum total of all debt service payments plus fees and charges paid to third parties not paid with bond proceeds and may not match Total Cash Flows

BACKGROUND

The Board adopted Resolution No. 4996, the Initial Refunding Authorization which authorizes the issuance and private sale of a maximum of \$2.20 billion of Power System Refunding Revenue Bonds, on November 16, 2021, and subsequently approved by City Council. Of this amount, \$970.00 million has been used to refund certain Power System Revenue Bonds, leaving a balance of \$1.23 billion. At this time, the Financial Services Organization (FSO) is recommending the use of up to \$1.10 billion of the refunding authorization balance of \$1.23 billion to refinance the Series A Refunded Bonds and Power 2010A Bonds.

The Initial Refunding Authorization provides FSO with the flexibility to execute several and multiple refunding transactions for the Power System whenever it determines such to be necessary and/or market conditions become favorable for refinancing. When issued, the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds will be payable from the Power Revenue Fund and will be issued under the Power System Master Bond Resolution.

LADWP's Debt Management Policy for refunding stipulates a threshold of three percent net present value savings prior to the scheduled call date before a refunding transaction can be pursued or if that threshold is not met, a refunding may be completed to reduce risk and for the restructuring of the debt repayment schedule. At this time, the Power 2024A Refunding Bonds are expected to produce present value savings of approximately 14.47 percent of the refunded par amount and the Power 2024B Refunding Bonds are expected to produce present value savings of approximately 2.46 percent of the refunded par amount. The Power 2024B Bonds will be refunded if there are any net present value savings, to eliminate regulatory risk and restructure the debt to gain refinancing optionality.

Based on interest rates for tax-exempt bonds as of January 23, 2024, FSO has determined that LADWP can refinance the Series A Refunded Bonds at an all-in true interest cost of approximately 3.41 percent. The Power 2024A Refunding Bonds are structured to achieve an aggregate average net cash flow savings of approximately \$76.96 million (\$57.93 million in present value terms) or average \$3.84 million annually over the next twenty years.

Based on interest rates for tax-exempt bonds as of January 26, 2024, FSO has determined that LADWP can refinance the Power 2010A Bonds at an all-in true interest cost of approximately 3.21 percent. The Power 2024B Refunding Bonds are structured to achieve an aggregate average net cash flow savings of approximately \$15.80 million or \$7.77 million in present value terms over the next fifteen years.

The proceeds of the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds will be deposited into an Escrow Account to fund the debt service of the Refunded Bonds.

Power 2010A Bonds

The Power 2024B Refunding Bonds are planned to price separately from the Power 2024A Refunding Bonds. The intention of the separation is to reduce the complexity of applying Internal Revenue Service's regulations from the comingling of the refunding of the Series A Refunded Bonds and the Power 2010A Bonds. In addition, by separating the pricing will allow LADWP to manage the supply of bonds in the market and isolate the market conditions that will affect the pricing of the Power 2024B Refunding Bonds.

The Power 2010A Bonds were issued as Federally Taxable Build America Bonds with a direct payment subsidy to the Power System, which lowered the overall interest costs of the bonds. The Power 2010A Bonds were to receive a subsidy from the federal government in the amount of approximately 35 percent of the interest payments. However, in 2011, the Budget Control Act of 2011 imposed automatic spending reductions, or "sequestration" beginning in 2013. The sequestration reduction rate has ranged from 5.7 percent to 8.7 percent, and currently stands at 5.7 percent through 2031. In 2022, as a result of COVID-19 relief legislation and mandatory spending cuts related to increases in the federal deficit, there was a possibility of a 100 percent reduction in subsidy payments. Currently, there is no permanent solution to eliminating sequestration and there continues to be a risk of 100 percent sequestration, until legislation guarantees the original federal subsidies. By refunding the Power 2010A Bonds now, LADWP will remove the risks of the subsidies being further reduced or eliminated in the future, and gain refinancing optionality in the future, while capturing known savings now.

The structure of Build America Bonds utilized a "Make-Whole Call" and Extraordinary Redemption Provision (ERP). Currently, it is understood that the ERP is exercisable as a result of the official sequestration of subsidies. LADWP is pursuing the proposed

refunding exercising the ERP with guidance from its bond counsel. Unlike typical tax-exempt bonds, that would be callable at par, the Make-Whole Call would require a calculation of the “Make-Whole Premium,” which essentially is a discounted premium based on Treasuries plus a spread of 100 basis points under the ERP. As the relative difference between tax-exempt yields increase versus Treasuries yields, the refunding economics are increasingly improved, as the relative cost of the Make-Whole Premium reduces and investors are willing to pay a relative higher price for replacement tax-exempt bonds. As of January 2024, 10-year tax-exempt yields versus Treasury yields is approximately 59.1 percent, which would result in close to three percent net present value savings from refunding the Power 2010A Bonds. However, most importantly as these low ratios are not typical, the resulting Make-Whole Premium under historical market conditions would be expensive and these bonds could not be refunded to generate savings. Refunding the Power 2010A Bonds at current yields and spreads will produce economical savings, while also introducing future optionality. By refunding the bonds with market standard five percent coupons and 10 year at par call provisions, LADWP can increase the Power 2010A Bonds optionality, allowing for a refunding in the future that will produce additional savings. By refunding the Power 2010A Bonds now, LADWP will capture current savings near LADWP’s target thresholds, while improving the optionality in the future to increase savings, whereas under typical market conditions, these savings could not be captured.

Transaction Approval and Details

Resolution No. 5049, the Sixty-First Supplemental Bond Resolution to the Power System Master Bond Resolution, if adopted, authorizes LADWP to issue up to \$1.10 billion of fixed-rate, tax-exempt Power 2024A Refunding Bonds and Power 2024B Refunding Bonds, outlines the terms and conditions for the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds, and authorizes the payment of the related costs of issuance.

Resolution No. 5049 is also a supplemental resolution to the Initial Refunding Authorization under Resolution No. 4996 adopted by the Board on November 16, 2021, and subsequently approved by the City Council.

Resolution No. 5050, if adopted, approves certain actions and agreements in connection with the issuance of the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds, including the sale of the bonds pursuant to the Contracts of Purchase with the underwriters named therein that were selected from LADWP’s investment banking team, the form of the Escrow Agreements relating to the period from the time of the issuance of the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds

to the redemption date of the bonds refunded whereby U.S. Bank Trust Company, National Association may perform certain actions as Escrow Agent, and the form of the Preliminary Official Statement to be used in connection with the sale of the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds.

Siebert Williams Shank & Co., LLC (Minority Business Enterprise and Women Business Enterprise) has been selected as senior book-running manager and BofA Securities, Inc. (Local Business Enterprise), as co-senior manager for the Power 2024A Refunding Bonds transaction. BofA Securities, Inc. (Local Business Enterprise) has been selected as senior book-running manager and Siebert Williams Shank & Co., LLC (Minority Business Enterprise and Women Business Enterprise) as co-senior manager for the Power 2024B Refunding Bonds transaction. Alamo Capital (Women Business Enterprise), Cabrera Capital Markets, LLC (Minority Business Enterprise), Morgan Stanley & Co. LLC (Local Business Enterprise), Stern Brothers & Co. LLC (Women Business Enterprise), and TD Securities (USA) LLC, as co-managers, will provide support to the senior managers for both transactions.

Senior and co-managers for bond transactions are selected from the current underwriting pool based on Request for Proposal (RFP) for investment banking services, past underwriting performance, continual coverage provided to LADWP, retail and institutional bond distribution capabilities, as well as bank credit extended to LADWP. The current underwriting pool was established through a RFP process and approved by the Board on July 20, 2021.

ENVIRONMENTAL DETERMINATION

Determine item is exempt pursuant to California Environmental Quality Act (CEQA) Guidelines Section 15060(c)(3). In accordance with this section, an activity is not subject to CEQA if it does not meet the definition of a project. Section 15378(b)(4) states that government fiscal activities which do not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment do not meet that definition. Therefore, the issuance of up to \$1.10 billion of Power System Revenue Bonds is not subject to CEQA.

CITY ATTORNEY

The Office of the City Attorney reviewed and approved as to form and legality the attached Resolution Nos. 5049 and 5050, the Contracts of Purchase, and the Escrow Agreements under the Power 2024A Refunding Bonds and Power 2024B Refunding Bonds.

ATTACHMENTS

- Resolutions
- Contracts of Purchase
- Escrow Agreements
- Preliminary Official Statement