Valley Water

File No.: 20-0924 **Agenda Date:** 10/13/2020
Item No.: *2.7

SUPPLEMENTAL BOARD AGENDA MEMORANDUM

SUBJECT:
Receive Information and Authorize Staff to Proceed with Execution of Bank Line(s) of Credit with Aggregate Stated Amount Not to Exceed $200 Million.

REASON FOR SUPPLEMENTAL MEMORANDUM:
This report conveys additional information received after the initial report was released, consistent with Executive Limitations Policy EL-7-10-5.

RECOMMENDATION:
A. Receive information regarding bank line(s) of credit solicitation;
B. Authorize staff to proceed with execution of bank line of credit with aggregate stated amount not to exceed $200 Million;
C. * Authorize a deposit of up to $14 million in a Certificate of Deposit Account Registry Service (CDAR) account with Bank of San Francisco, earning 0.45% per year for three-years; and
D. * Authorize staff to offer special incentives to California based small community banks

SUMMARY:
On April 28, 2020, the Santa Clara Valley Water District's (Valley Water) Board of Directors authorized the solicitation, negotiation and execution for bank line(s) of credit up to $200 million to provide backup liquidity for Valley Water's capital improvement program and general financing needs in light of the ongoing economic uncertainties related to the COVID19 pandemic (Resolution 20-11). The results of the solicitation were presented to the Board at its meeting on June 9, 2020 where the Board directed staff to conduct additional research regarding the environmental, social and governance (ESG) policies of each of the five banks (MUFG Union Bank, JPMorgan Chase, US Bank, UBS and Bank of America) who responded to the solicitation. On August 11, 2020, the Board authorized staff to proceed with negotiations with the banks to ensure Valley Water achieves the most favorable business terms and pricing, provided that the banks meet a minimum of "Average or Medium" ESG ranking by an ESG research firm (per Executive Limitation 4.7.7). The Board also directed staff to reserve $20 million of the credit capacity for small local banks located within the nine Bay Area counties with total assets of under $10 billion.

Staff proceeded to contact the top three ranked banks (MUFG, JP Morgan, and US Bank), and negotiated for the best and final offers from each of the banks. Each bank offered various degrees of changes to their respective proposals, as summarized in Attachment 1.

Based on the banks' best and final offers, staff recommends that the Board authorize the execution of the bank agreement with US Bank to act as the sole lead bank for $150 million line of credit and the agent for the small/local bank syndicate of up to $20 million (Attachment 2). Staff recommends proceeding with US Bank due to the following factors:

- US Bank increased the credit capacity to $150 million (previously $75 million);
- US Bank reduced the fee structure which resulted in the lowest overall financing rates among the competing offers; for comparison, the estimated bank fees offered by US Bank for the three-year term is approximately $2.4 million to $5.3 million lower than JP Morgan and MUFG respectively (assuming $170 million tax-exempt draw);
- US Bank increased the term to three years (previously 2.5 years) and agreed to various other amendments to key business terms; and
- US Bank agreed to act as the lead bank and agent to administer the syndicated small local bank credit capacity of up to $20 million, for a total combined revolving line of credit capacity of $170 million.

US Bank marketed the local bank syndicated loan to 24 local banks located within the Bay Area as well as across California to maximize interest levels (Attachment 3). To-date, US Bank received preliminary commitments from the following local banks:

- Community Bank of the Bay, headquartered in Alameda County, has received bank credit approval to commit $5 million, subject to Valley Water Board approval of the pricing, terms and conditions of the US Bank agreement.

- Bank of San Francisco, headquartered in the City and County of San Francisco, has conditionally committed up to $7 million, subject to the following conditions:

    (i) Valley Water Board approval of the pricing, terms and conditions of the US Bank agreement;

    (ii) Bank of San Francisco Board approval; and

    (ii) Valley Water Board approval of placing up to $14 million in a CDAR deposit account with the Bank of San Francisco earning an annual interest rate of 0.45% for the three-year term. Bank of San Francisco stated that the deposit is necessary to meet the bank's capital funding requirements pursuant to federal banking laws. The funds placed in the CDAR account would be secured by the Federal Deposit Insurance Corporation (FDIC). For comparison, Valley Water current holds $75 million in deposits in the Local Area Investment Fund (LAIF) administered by the State Controller's Office, earning 0.78% as of August 2020. Should the Board approve Bank of San Francisco's deposit requirement, staff would withdraw $14 million from LAIF and transfer the funds to the Bank of San Francisco to be invested in the CDAR account. The potential reduction in investment income for the $14 million CDAR deposit is estimated at approximately $47 thousand per year or $140 thousand for the three-year term.

- First Foundation Bank, headquartered in Irvine, Orange County but has Bay area branch locations in Burlingame (San Mateo County) and the City and County of San Francisco, has conditionally committed up to $10 million, subject to Valley Water Board approval of the pricing, terms and conditions of the US Bank agreement as well as bank credit approval.

Community Bank Special Incentives

The $20 million small local bank credit capacity may potentially be fully subscribed if the Board approves the three banks described above and each of the banks can complete its own credit approval process to close on the syndicated loan. In the event that any of the small banks are unable to close on the syndicated loan, staff recommends that the Board authorize staff to continue to work with US Bank to offer special incentives to California based community banks and/or minority owned banks with under $10 billion in total assets to fully subscribe the $20 million capacity reserved for community banks. Although the prior Board direction was to solicit participation from banks headquartered within the nine Bay Area counties, due to lack of interest from the local Bay area banks, staff recommends expanding the eligibility criteria to California based small banks. The special incentives may include the following, but may be amended to meet the needs of the community banks:

- Offer a one-time upfront fee equal to a percentage of the commitment amount (e.g. 0.50%);

- Offer a deposit amount up to two times the commitment amount; subject to the legal requirements per California Government Code 53600 et. al. for a securitized deposit account (via FHLB Letter of Credit equal to 105% of the deposit amount) or place the funds in FDIC insured CDs through the CDAR program.

US Bank, as the provider for up to $150 million line of credit, requires that the ongoing commitment and draw fees for the entire syndicated loan be the same, and if Valley Water enters into any future credit agreement that offers terms and conditions to other lenders with provisions more favorable to such lender, then US Bank will receive the same. Given this requirement, Valley Water is not able to offer different commitment and draw fees or better terms and conditions to the community banks, whether through a syndicate with US Bank or other separate bank agreements, other than the one-time upfront fee, as well as offering other incentives such as establishing a deposit account as discussed above. Staff has also previously received guidance from MUFG that the bank's interpretation of Municipal Securities Rulemaking Board (MSRB) Rule G-38 Solicitation of Municipal Securities Business, prohibits different pricing among syndicated loan members (<http://www.msrb.org/Rules-and-Interpretations/MSRB-Rules/General/Rule-G-38.aspx>).

FINANCIAL IMPACT:

Good Faith Estimate of Costs

Pursuant to Government Code 5852.1, the good faith estimate of costs for the three-year term of the bank agreement are calculated to show a range of costs, depending on the timing, amount and tax status of the draws against the line of credit. The low end of the range assumes costs based on limited draws to meet specific business needs, and the high end assumes costs based on fully drawing $170 million line of credit on a tax-exempt basis.

(1) The true interest cost is currently estimated to be 0.574% - 1.557%;
(2) The finance charge (which means the sum of all fees and charges paid to third parties) is estimated to be $367,780;
(3) The amount of debt proceeds received by Valley Water (which is net of the finance charge) is estimated to range from $60 million to $170 million per year; and
(4) The total payment amount during the three-year term is estimated to be $2.7 - $7.3 million in interest and finance charge, and principal amount ranging from $60 million to $170 million per year to be repaid through long-term bond issuances over time.

The above good faith estimates of costs are based on market conditions as of September 30, 2020. Actual results will differ depending on market conditions, fluctuations in the benchmark rate for the draw fees, Valley Water's future business needs which will impact the timing, amount and tax status of the draws, among other factors, that may impact the actual costs in the future.

CEQA:
The recommended action does not constitute a project under CEQA because it does not have the potential for resulting in direct or reasonably foreseeable indirect physical change in the environment.

ATTACHMENTS:
Supplemental Attachment 1: Best/Final Bank Proposals
Supplemental Attachment 2: Certificate Purchase/Reimbursement Agreement
Supplemental Attachment 3: Small Banks Outreach

UNCLASSIFIED MANAGER:
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