

# Minutes

Sacramento Suburban Water District  
**Board Workshop**  
Monday, January 9, 2012

## Call to Order

President Fellenz called the meeting to order at 6:03 p.m.

## Roll Call

Directors Present: Thomas Fellenz, Frederick Gayle, Todd Robison, Neil Schild and Kevin Thomas.

Directors Absent: None.

Staff Present: General Manager Roscoe, Dan Bills, Ed Formosa, Jan Gentry, Warren Jung, John Valdes and Legal Counsel Joshua Horowitz.

Public Present: William Eubanks and Peter Shapiro.

## Public Comment

None.

## Items for Discussion and Action

1. **Resolution 12-01 Authorizing an Application for Funding Assistance Through the Reclamation's WaterSMART and Energy Efficiency Grant Program**

General Manager Roscoe presented the staff report. In November 2011, the Bureau of Reclamation released a Grant Funding Opportunity Announcement (FOA) under the cost-share funding for water and energy-efficient projects.

The District can submit a funding request under one of two FOA funding groups. Staff is proposing to apply for funding in both categories. For the smaller on the ground projects, staff proposes a \$300,000 grant for accelerating meter retrofits and for a larger project staff is looking at a \$300,000 for energy conservation projects such as a possible in-conduit hydroelectric project. The applications are due January 19, 2012.

Director Schild asked if District staff talked with Bureau staff. Warren Jung stated that Brown and Caldwell spoke with the Bureau regarding the application.

MSC<sup>1</sup> (Thomas/Gayle) that the Board of Directors adopt Resolution 12-01 Authorizing an Application for Funding Assistance Through the Reclamation's WaterSMART and Energy Efficiency Grant Program, by unanimous vote.

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<sup>1</sup>Motion, Second, Carried.

## 2. **Interest Rate Swap Agreement**

General Manager Roscoe and Dan Bills presented the staff report. The District is exploring a potential counterparty substitution (“novation”) and restructuring of the interest rate swap agreement (“the Swap”) entered into between itself and Citibank, N.A. (“Citibank”) which currently hedges the Series 2008A2 bonds (the “2008A2 Bonds”) and Series 2009A bonds (the “2009A Bonds”). Staff wishes to narrow the options to allow further development of those specific options.

Mr. Bills gave a PowerPoint presentation. Discussion ensued and included:

- A change would likely better the stance with the District’s debt.
- The District’s current debt is approximately 70% variable and 30% fixed, with the Swap hedging some of the variable debt.
- How a swap structure works.
- Credit risk is reduced if the District changed from Citibank to a different counterparty with a better credit rating.
- The District’s credit rating is very important for many reasons, including debt issuance, market trading, LOC renewal and collateral posting requirements.
- Over the past 7 years, \$10.56 million was saved due to the District issuing variable debt and managing its risk versus issuing fixed-rate debt.
- There are six main risks inherent in issuing variable rate debt. The primary risk is market risk which is mitigated by issuance of a swap.

Mr. Peter Shapiro, Managing Director, Swap Financial Group, LLC was contacted for purposes of obtaining a list of alternatives and pricing information that might be available to the District on its Swap. Swap Financial Group served as the District’s advisor on the Swap when it was originally purchased in 2005 and again in 2008 when the Swap was amended as part of the 2008 debt refinancing.

Mr. Shapiro gave a PowerPoint presentation which included:

- Swap Financial Group serves as an independent advisory firm.
- Background on swap markets.
- A swap is used for hedging purposes.
- Interest expense savings are not always realized with a swap.
- An entity can take advantage of market opportunities more quickly with a swap.
- When originally issued, SSWD could have issued a fixed rate bond at 4.3% or variable rate debt with a swap rate at 3.283% (about 100 basis points difference).
- California bonds trade better than national bonds due to the state tax exemption in addition to the federal tax exemption.
- Risk requires the variable rate debt be managed actively.
- Current issues for SSWD include counterparty risk and swap structure (the total variable debt and the Swap are mismatched).
- Citibank’s credit has declined.
- Citibank is looking to reduce its swap positions and is willing to pay the cost for SSWD to replace it.

- Most cost-effective approach: combine Citibank novation with swap restructuring or termination.
- Three general options for the District to consider include: 1) upgrade swap credit by novation and leave existing mismatch in place; 2) upgrade swap credit by novation and restructure the 2009A portion to eliminate mismatch; and 3) novate only the 2008 A2 portion and terminate the 2009 A portion.

Mr. Bills continued with his PowerPoint presentation. Discussion ensued and included:

- All costs presented are estimates only as market conditions constantly change. Final costs will not be known until closing.
- Reviewed Citibank's proposal.
- Wells Fargo and Bank of New York are two possible counterparties for the novation.
- Graphs of the 2008A-2, 2009A bonds payment schedule and the total variable rate versus current Swap were reviewed.
- Five alternatives were presented. Swap alternatives include novation, novation and restructure, novation and partial termination and novation, partial termination and restructure or refinancing.
- If the District restructured the swap to match the terms of both 2008A2 and 2009A debt, it would receive roughly \$4.7 million. The District does not wish to borrow money, so it can either choose to lower the swap fixed rate to break even or it can restructure the swap to match only a selected portion of the 2009A bond, for example one-half (\$21 million).
- Novation and partial termination by retaining one-half of the current swap. Cost would be roughly \$4.8 million to the District.
- Novation, partial termination and restructure could be done at no cost to the District. Keeping the 3.283% current fixed rate intact, \$12.3 million, notional, of the swap could be terminated with the term extended by one year.
- Novation, partial termination and refinance. This option would novate and restructure the swap to equal a portion of both 2008A2 and 2009A bonds absent the amortizations that occur through 2020 (approximately \$32.4 million). The cost to terminate this portion of the swap would be approximately \$3.3 million. The current amortizations would be reissued as fixed-rate debt.

Mr. Shapiro stated the District should remove variable-debt and swap related risks when at no or a low cost. Citibank may decide to withdraw the current novation offer at any time. The District should act before this window of opportunity closes, preferably in January, no later than February 2012. He suggested that the combination of novating and partially terminating the swap and issuing fixed-rate debt was a good option for the District to pursue. Mr. Shapiro stated the novation, partial termination and restructure is a good plan B.

William Eubanks encouraged the Board to give staff direction tonight and make a final decision at the January 23, 2012 meeting.

General Manager Roscoe asked the Board to provide staff guidance with respect to their comfort level on how much should be hedged with the Swap agreement and how much variable rate exposure should be hedged with District reserves also invested at variable rates. Plan A takes a portion fixed, reducing variable rate risk and may be accomplished at relatively low cost. This option would cost the District roughly \$3.3 million up front, but the pay back would be certain as rates would be fixed.

MSC (Robison/Gayle) that the Board of Directors direct staff to proceed with Plan A (novation, partial termination and refinance) and Plan B (novation, partial termination and restructure) for consideration at the January 23, 2012 regular Board meeting, by unanimous vote.

### **Adjournment**

President Fellenz adjourned the meeting at 8:46 p.m.

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Robert S. Roscoe  
General Manager/Secretary