COUNCIL OF THE CITY OF PHILADELPHIA
PUBLIC HEARING AND PUBLIC MEETING

BEFORE THE COUNCIL COMMITTEE ON FINANCE

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Room 400, City Hall
Philadelphia, Pennsylvania
Thursday, November 12, 1998
10:00 a.m.

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Bill No. 980790 - An ordinance authorizing the issuance of general obligation bonds to provide funds to refund certain outstanding general obligation bonds of the City of Philadelphia; authorizing the Mayor, City Controller, and City Solicitor, or a majority of them, to sell the bonds at public or private negotiated sale; setting forth the purposes and amounts for which the proceeds of the bonds will be expended; providing for the maturities and for other terms and conditions and for the form of the bonds; providing that bonds may be redeemable prior to maturity; providing sinking funds for the bonds and for appropriations to the Sinking Fund Commission for the payment thereof; authorizing agreements to provide credit enhancement or payment or liquidity sources for the bonds and certain other actions.

PRESENT: COUNCILWOMAN ANNA CIBOTTA VERNA
COUNCILWOMAN JANNIE BLACKWELL
COUNCILMAN JAMES F. KENNEY
COUNCILWOMAN MARIAN B. TASCO
COUNCILMAN W. THACHER LONGSTRETH

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VINCENT VARALLO ASSOCIATES, INC.
Registered Professional Reporters
Eleven Penn Center, Suite 600
Philadelphia, PA 19103
(215) 561-2220

11/12/98 FINANCE COMMITTEE - Bill No. 980790

I N D E X

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P R O C E E D I N G S

COUNCILWOMAN VERNA: Good morning. This is the public hearing of the Committee of Finance.

I would ask the clerk to please read the title of Bill No. 980790.

THE CLERK: Bill No. 980790 - An ordinance authorizing the issuance of general obligation bonds to provide funds to refund certain outstanding general obligation bonds of the City of Philadelphia; authorizing the Mayor, City Controller, and City Solicitor, or a majority of them, to sell the bonds at public or private negotiated sale; setting forth the purposes and the amounts for which the proceeds of the bonds will be expended; providing for the maturities and for other terms and conditions and for the form of the bonds; providing that bonds may be redeemable prior to maturity; providing sinking funds for the bonds and for appropriations to the Sinking Fund Commission for the payment thereof; authorizing agreements to provide credit enhancement or payment or liquidity sources for the bonds and certain other actions.

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(Thomas Queenan comes forward.)

COUNCILWOMAN VERNA: Good morning. Please identify yourself for the record and proceed with your testimony.

MR. QUEENAN: Yes, good morning. My name is Thomas Queenan, I'm the Treasurer for the City of Philadelphia.

At this time slight, I have some amendments to the ordinance as presented to Council. May I offer them to you and read the changes into the record please.

COUNCILWOMAN VERNA: Do you have copies?

MR. QUEENAN: Yes.

COUNCILWOMAN VERNA: Thank you.

(Mr. Queenan distributes copies of amendment.)

MR. QUEENAN: It's a very minor change. It falls under Section 3, the very, very last sentence of Section 3 of the ordinance. And that is ordinance Bill No. 980790, and the change would be: We have less than ten number of days. I'll read the entire sentence.

"Bonds that the owner addresses on the

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registry of the fiscal agent not less than 10. . ." It should be 30 instead of 10 days, 30 days.

"No more than 45 days" should be "60 days prior to the date of the fix for redemption." This just represents how much notification time you need to contact the bondholders in the event of a redemption of the bonds. We're just making it a longer period of time. This is too short. There was an oversight.

I have provided testimony to the committee for your review, and I will read it into the record. I will note also that I did notice two typing errors as well as in this particular item, and I will note them when I get to that portion of the testimony.

But I'm here to testify in support of Bill No. 980790, an ordinance authorizing the issuance of the Series 1998 refunding general obligation bonds to provide funds to refund certain outstanding obligation bonds of the City of Philadelphia; further authorizing the Mayor, City Controller, and City Solicitor, or a majority of them, to borrow by issuance of and sale of

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general obligation refunding bonds of the City in a sum, or sums that do not exceed $250 million at a public or private negotiated sale.

The proceeds of the bonds will be used to provide bonds for the refunding of the principal amount outstanding of the Series 1990 general obligation bonds, and the refunding of all or a portion of the Series 1973 A's, Series 1973 B, Series 1993 A, Series 1994 B, and Series 1995 general obligation bonds. In.

1990, the City issued 148 million of variable-rate general obligation bonds. The Series 1990 bonds also include a fixed interest rate swap that is secured by a Fuji Bank letter of credit. Both the swap and the Fuji LOC expire August 2,000. Final maturity of the Series 1990 bond is 2020.

A key feature of the proposed series 1998 -- that's the typo, I have "1989", that should be "1998" -- refunding bonds is determination of the interest rate swap agreement and the conversion of the variable-rate interest rate bonds to a fixed interest rate bond.

Termination of the swap and current

market conditions will allow the City to take advantage of low rates by converting the variable rate interest to a fixed interest rate for savings.

If the City were not to terminate the swap or convert to a fixed interest rate while rates are at a historic low and wait until August 2000, it is likely that interest rates will be higher at that time. The City is then at risk of paying a higher fixed beginning in August 2,000 -- that's the other typo, instead of "August 200, it should be "August 2000" -- through to the year 2020, a rate that may be significantly higher than what can be received day of the variable rate debt is converted to fixed-rate debt.

As you all know, and I testified just two days ago, rates are very, very low, mortgage rates for houses are very, very low. So because rates are low, it's a good time to convert from a variable rate to fixed rate.

For example, the recent PGW bond sale had a fixed rate of 5.23, the airport bonds had a fixed rate of 5.29. Both these deals, by the way, were financed in July of this year, the PGW deal and the airport deal.

An insured General Fund bond with a Baa2/BBB credit rating in the current market would have a rate of about 5.25 percent. The existing all in cost of the Series 1990 variable rate bonds is about 7.25 a percent. If we are convert to a fixed rate today, the City will have a lower annual debt service cost of about 2 percent.

If we wait until the swap terminates and the fixed rate rise to a 5.75, for example in the year 2,000, the additional cost in debt service is about $6.5 million over the remaining life of the bonds out to the year 2020. The additional cost increases to about 13 million if rates rise to 6.25 percent and approximately -- approximately $19.5 million if rates were to rise to a 6.75 percent. Therefore, the economic benefit of terminating the swap today is greater than the transaction costs plus the termination fee of about $8 million.

An elimination of the Fuji LOC converting the variable rate Series 1990 bonds to a fixed rate and refunding of certain outstanding bonds can save the City about $2.5 million or 5.3

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percent of the debt service cost, plus between about $6.5 and $19.5 million, or for a total of $9 million to $22 million. Minus the termination fee of $8 million, the savings to the City will be between 1 million and $14 million.

Some portion of the termination fee can be recovered in the refunded escrow. The amount is yet to be determined; although estimate may be as high as about $3.5 million. So the savings estimates could increase by this amount of money.

The Series 1998 refunding bonds issued will be fixed rate, in denominations of $5,000. Interest will be payable semiannually. All the debt service will be issued as general obligation bond debt of the City. The full-faith credit and taxing power of the City are pledged for the payment of principal and interest and premium, if any on the Series 1998 refunding bonds and all other general obligation bonds of the City. We expect to pursue the provision of bond insurance for all the Series 1998 refunding bonds.

The sale of the bonds is tentatively skilled late November in an amount not to exceed $250 million. Settlement of the bonds is scheduled for late December. Attached is the financing team.

Right now, the size of the refunding is actually about $190 million, so we can refund up to 250 but the refunding amount based on where interest rates right now is about 190, $192 million.

That concludes my testimony. If you have any questions, I'd be happy to answer them.

COUNCILWOMAN VERNA: Mr. Queenan, according to your testimony, there is an $8 million termination fee?

MR. QUEENAN: Yes.

COUNCILWOMAN VERNA: For refunding these bonds prior to August 2,000?

MR. QUEENAN: Yes.

COUNCILWOMAN VERNA: Who receives that termination fee?

MR. QUEENAN: Well, the City has entered into a swap agreement with the investment banker, who was the investment banker at the time, the senior manager, which was Merrill Lynch.

And so there's a contract between the City and Merrill Lynch when we entered into the swap. So the payment will be made to Merrill Lynch.

COUNCILWOMAN VERNA: The bill states that you can refinance up to $250 million in bonds. What is the actual amount that you intend to refund?

MR. QUEENAN: Right now, the amount of the refunding is about 190, $192 million.

As interest rates change, some bonds will be refundable. If interest rates go up, for example, some of those bonds go away as refundable candidates. If interest rates drop a little bit between now and the time we do the pricing, then the amount could rise because other bonds are in the money.

COUNCILWOMAN VERNA: Well, if you do not refund that entire amount, does this bill give you the authorization to refund other bonds without coming back to City Council?

MR. QUEENAN: Let me check with counsel on that.

(Mr. Queenan briefly confers with counsel.)

(City Council President Street enters

chambers.)

PRESIDENT STREET: Can we have your attention, please.

I would like to announce that the City Council session today, which was scheduled for -- which is routinely scheduled to start at 10 o'clock, will not start at 10 o'clock, in case no one noticed.

We will start the Council session as quickly as we can at the termination of this Finance Committee meeting. There will be a brief caucus, and then we will convene the Council session.

We hope this has not inconvenienced anyone. We appreciate very much your being here, but we must do this business.

Thank you, Councilwoman Verna.

COUNCILWOMAN VERNA: Thank you.

MR. QUEENAN: To answer your question, in a conversation with Paul Rucci, from the City Law Department, my understanding is that under Section 2 of the ordinance, that we would have authorization to refinance the balance of what is not refunded under the series of bonds that are noted here in Section 2 of the ordinance.

So when we have the series '73 A's, the Series '73 B's, the Series 1993 A's, the Series 1994 B's, and any 1995 bonds that are not refunded when we do the sale, if we're approved, we would be able to refund the rest of those bonds without returning to Council, up to $250 million.

COUNCILWOMAN VERNA: Thank you.

Your testimony the other day referenced the RFQ process that the Finance Department has in place to select financing teams. Could you provide the committee with a list of all the banks that have participated in these financings since 1992, and how many financings they have participated in.

MR. QUEENAN: Yes, I can, I can provide that to you. I'll have it to you by Monday.

COUNCILWOMAN VERNA: Thank you.

Are there any questions from members of the committee?

The Chair recognizes Councilwoman Tasco.

COUNCILWOMAN TASCO: Would you explain to me what a swap is?

MR. QUEENAN: (Sighs.) There --

COUNCILWOMAN TASCO: I remember this. I was here in 1990 when this Fuji issue came up.

MR. QUEENAN: You were here in 1990? Essentially -- well, a swap is, you basically swap interest payments.

In 1990 -- I wasn't here then -- but apparently, the City was not able to actually issue bonds for a fixed rate at the time because of the credit rating of the City. In fact, if you recall the handout that I gave you on Tuesday -- it was Tuesday -- the City's credit rating was almost down to a CCC.

So in order for the City to get a synthetic fixed rate, we entered into a swap with a swap provider where they would pay us in a variable interest rate, and we would pay them a synthetic fixed interest rate.

So to allow the City to control its interest cost on an annual basis, if you had a mortgage, for example, right now and you had a variable rate mortgage, the payment would fluctuate, based on what the market is.

And from a budgetary perspective, if

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you had a fixed income and you were trying to budget what your payments would be every payments every month going forward, it could be a little tough to do because you never know what the variable rate would do.

So what you're able to do is actually swap these payments with someone else and get a synthetically-fixed interest rate. So from a budgetary perspective, you would know that your interest rate is the same amount every month going forward.

So a swap agreement, whether you're doing it for a home mortgage or whether you're doing it for City bonds is pretty much the same thing. And we swapped our interest payments to a fixed rate because we were not able to get a fixed rate on our own.

COUNCILWOMAN TASCO: Okay. The other question I have: Where is your WBE/MBE participation on this deal?

MR. QUEENAN: As you noted, the last sheet of the paper actually does have a listing of the team. I would offer that this is not the completed team yet and that I suspect that the team will actually be completed before we actually move further ahead with the transaction.

COUNCILWOMAN TASCO: Let us know, I would be interested in knowing who the minority participants are.

MR. QUEENAN: Okay.

COUNCILWOMAN TASCO: The other question I have: The other day, you asked us to approve the bonds for private sale. And I noticed in here, you say -- you request that these could be sold public or private.

Why couldn't you have done the same thing with the other bonds the other day, the other bonds requests? You came in and asked to sell those bonds at a private sale.

Here in this testimony, it says that you want a public or a private negotiated sale. Well, I mean, what's the difference?

MR. QUEENAN: That's a good question.

COUNCILWOMAN TASCO: Could we have done the other bond -- the other ordinance public our private and you had the same flexibility?

MR. QUEENAN: Well, I would say that -- before I let the other person testify -- is that the difference between the request the other day was to do a competitive or to do a privately negotiated sale. You're absolutely right.

And so the question is, we're going to still do a negotiated sale, but your question is, What is the distinction between a public or private negotiated sale?

I'll let Paul Rucci answer that.

MR. RUCCI: I'm not sure I'm answering the question that's in your mind, but --

MR. QUEENAN: Introduce yourself for the record.

MR. RUCCI: I'm Paul Rucci from the City Solicitor'S Office.

COUNCILWOMAN TASCO: Speak into the mike.

MR. RUCCI: The ordinance that you were working with the other day --.

COUNCILWOMAN VERNA: It was a resolution.

MR. RUCCI: -- was drafted and enacted long before any deal was contemplated. It was simply an authorization when the time was right to borrow the money.

COUNCILWOMAN VERNA: I'm sorry, we can't hear you.

MR. RUCCI: I'm sorry.

COUNCILWOMAN TASCO: Is the mike on? You have to speak up. We can't hear you.

MR. RUCCI: The authorization that you were looking at the other day was adopted and put into place long before any deliberate decision to sell bonds was made. It was for future use, and it was customary to require the Treasurer to come back to Council for the decision on a private-versus-negotiated sale.

This ordinance was prepared kind of for a specific deal right from the start. The Treasurer knew that he wanted to do a negotiated sale and so he was going to make his case here.

(Mr. Queenan asks Mr. Rucci a question off mike.)

MR. RUCCI: In the past, we would accept bids for general obligation bonds. I believe that that is the essence of a public sale. There may well have been some negotiation that would go on after the bid was opened and the successful bidder was selected.

We haven't done that in such a long time, I don't want to go back and -- I don't want to speculate right now about what that might entail.

But a private negotiated sale would be the sort of thing that's going on now, where negotiations begin with the underwriters, and there's no thought given to a bid.

MR. QUEENAN: My understanding of the distinction is this: Tuesday, I talked about a competitive versus a private negotiated. This is still going to be as a negotiated sale.

The testimony that I provided for the new money on Tuesday was for a negotiated sale, and I made the distinction between negotiated or a competitive sale.

This is still a negotiated sale. The distinction between a private negotiated sale and a public negotiated sale is that in this case, we have selected the investment banker now based on a proposal that was submitted. And in the last couple months, we've been negotiating the process of doing the sale, and we will sell the bonds.

I believe a public negotiated sale,

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which we are not going to do, is where we would actually, I suppose, put out bids for people to respond to, to enter into a private negotiation with the City of Philadelphia.

So when we do the RFQ process and we select a whole list of investment banking firms that the City will prequalify to do bond deals with, that kind of negates the public negotiated sale aspect because we already have defined who we can work with. We select from that group of people we've already selected, and then we have private negotiated sale discussions and sell the bonds.

So this bond sale will actually sell the same way as the new money. They're both negotiated sales. This is not a competitive sale. The one that we talked about on Tuesday for the new money is not a competitive sale. This committee approved for a negotiated sale. The request today is also for approval of a negotiated sale.

MR. RUCCI: I continue to believe that the timing is important to that. We submit and usually secure passage of an authorization to sell general obligation bonds each year with the adoption of the capital budget, but often those authorizations are not used for a very long time.

And so it's appropriate for the administration to come back to the Council with its plans for a negotiated sale when the deal is actually ready to go. I think we're already at that stage in this transaction.

COUNCILWOMAN TASCO: Thank you. Let me ask you, how large is your pool of investors, your investment --

MR. QUEENAN: Banks?

COUNCILWOMAN TASCO: -- banks that you deal with?

MR. QUEENAN: I believe we have about 63 investment banks.

COUNCILWOMAN TASCO: How many?

MR. QUEENAN: 63, 6-3.

COUNCILWOMAN TASCO: 63.

MR. QUEENAN: Right, 63 investment banks have been qualified to provide for investment banking services for the City of Philadelphia. And I can provide you with a list of those banks, by the way.

COUNCILWOMAN TASCO: Mm-hmm, I'd like see that.

MR. QUEENAN: Okay.

COUNCILWOMAN TASCO: Thank you.

COUNCILWOMAN VERNA: Are there any other questions from members of the committee?

(No questions.)

COUNCILWOMAN VERNA: Do we have any anyone else to testify on this bill?

(No response.)

COUNCILWOMAN VERNA: Is a suspension being requested? Or isn't it necessary?

MR. RUCCI: No. Councilwoman, because elements of this loan are incurring debt without the consent of the electors on a ballot question, there is a certain amount of advertising that has to be completed five times at intervals of not less than three days before the Council can finally adopt the ordinance. That's a summary of this ordinance that's being published, and so suspending the rules will not help us.

COUNCILWOMAN VERNA: Be necessary. Thank you.

Do we have anyone else here to testify

on this bill?

(No response.)

COUNCILWOMAN VERNA: Seeing none, this will conclude the public hearing.

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COUNCILWOMAN VERNA: We will now go into our public meeting.

The Chair recognizes Councilwoman Blackwell.

COUNCILWOMAN BLACKWELL: Madame Chair, I move the approval of the amendments.

(Duly seconded.)

COUNCILWOMAN VERNA: All those in favor will signify by saying aye.

Those proposed?

The amendments will be adopted.

The Chair recognizes Councilwoman Blackwell.

COUNCILWOMAN BLACKWELL: Madame Chair, I move that Bill No. 980790 be reported out of committee, as amended, with a favorable recommendation.

(Duly seconded.)

COUNCILWOMAN VERNA: It's been properly moved and seconded that Bill No. 980790 be reported out of committee with a favorable recommendation, as amended.

All in favor will signify by saying aye.

Those opposed?

The ayes have. The motion is carried.

This concludes the public meeting of the Committee on Finance. Thank you all very much.

(Adjourned at 10:28 a.m.)

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C E R T I F I C A T E

I HEREBY CERTIFY that the foregoing proceedings of the Council of the City of Philadelphia of Thursday, November 12, 1998, were reported and accurately by me, and that this is a correct transcript of same.

RE: COUNCIL COMMITTEE ON FINANCE
BILL NO. 980790

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JOSEPHINE CARDILLO,
Registered Professional Reporter