



ARLINGTON COUNTY, VIRGINIA

<p>County Board Agenda Item Meeting of January 26, 2008</p>
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DATE: January 9, 2008

SUBJECT: Authorize the interest rate conversion of the Industrial Development Authority Taxable Economic Development Revenue Bonds (Skating Facility Project), Series 2005.

C. M. RECOMMENDATION:

Adopt the attached resolution requesting the Industrial Development Authority to change the Bonds' interest rate mode, pursuant to the terms of the Indenture, to reduce the County's potential interest rate risk on the Bonds, if determined to be advantageous by the County Manager or the Director of the Department of Management and Finance.

ISSUES: This action reduces interest rates exposure; no issues on this project.

SUMMARY: In May 2005, the Arlington County Industrial Development Authority ("IDA") issued \$35.7 million of Taxable Variable Rate Economic Development Revenue Bonds (Skating Facility Project), Series 2005 (the "Series 2005 Bonds") to finance a portion of the cost of construction of an ice skating facility on top of the Ballston Commons Parking Garage, including the construction of two NHL sized ice skating facility sheets, corporate office space for the Washington Capitals Hockey Club, locker rooms and training facility, and approximately 192 public parking spaces.

Under a Cooperation Agreement between the County and the IDA, the County Board agreed to undertake in each fiscal year to consider appropriations of the full amount necessary (i) to pay the scheduled debt service on the Series 2005 Bonds, (ii) to replenish any shortfalls in the Debt Service Reserve Fund, and (iii) to pay all other amounts required to be paid by the IDA on the bonds in each fiscal year. The obligation of the County to make payments on the Series 2005 Bonds is subject to and conditioned upon annual appropriation by the County Board. This annual appropriation is offset by fixed annual lease payments from the Lincoln Ballston, LLC (the "Capitals") of \$2.4 million, approximating the debt service on the Series 2005 Bonds. However, due to the variable nature of the debt service on the bonds, such revenue may be more or less than debt service on the bonds.

<p>County Manager: _____</p>

<p>County Attorney: _____</p>

<p>Staff: Mark Schwartz; Director DMF, Gus Vega; Sr. Financial Analyst DMF</p>
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Since the Capitals lease payment is fixed, the County is exposed to the risk of changing interest rates and debt service on the Series 2005 Bonds. The interest rates on the bonds have fluctuated between a low of 3.06 percent in May, 2005 to a high of 5.95 percent in September 2007; the rate as of December 31, 2007 was 4.95 percent. When the Series 2005 Bonds were issued, the IDA purchased interest rate protection which limits the County's interest rate risk to a 6 percent rate. This interest rate protection expires in May 2008. County staff and its financial advisor are carefully monitoring the market for opportunities to limit the County's interest rate exposure. One way this may be achieved is by changing the interest rate mode on the bonds from a rate that resets every week to a longer term rate.

BACKGROUND: The purpose of the Skating Facility Project is to promote the economic development of the Ballston Commons Mall and the relocation of jobs to the County. Further the direct and indirect economic benefits and the cultural and recreational benefits of the project are manifestly in the public interest. The two ice rinks opened in November 2006 and four months later the Capitals moved its corporate headquarters to the newly built office space at Ballston.

The total cost of the project was approximately \$42.8 million; the sources of funding included \$35.7 million in revenue bonds, \$6 million County paygo contribution, and approximately \$1.2 million in equity from the Capitals. Proceeds from the Series 2005 Bonds were spent on project construction costs, capitalized interest during the construction, a debt service reserve fund, and an operating reserve fund. The Series 2005 Bonds are currently outstanding in the principal amount of \$35.7 million with a final maturity in 2031. Annual principal repayments are scheduled to begin in Fiscal Year 2009.

The Capitals, for so long as the Series 2005 Bonds remain outstanding, shall pay to the IDA as basic rent for the Skating Facility a fixed amount approximately equal to the total debt service on the Series 2005 Bonds. Since the bonds were sold as variable rate bonds, debt service will fluctuate based on variable interest rates on the bonds. The lease payments made by the Caps were calculated at the closing of the bonds based on the actual amount borrowed, estimated expenses on the bonds, and a historical average of short-term taxable interest rates. Based on these estimates, the annual debt service and lease payments from the Capitals were fixed at \$2.4 million. Consequently, depending on interest rate market conditions, the Capitals lease payment may be more or less than the actual debt service on the bonds.

To the extent that the lease payments from the Capitals would be insufficient to cover debt service (due to high interest rates or failure of the Capitals to make the payment), the County would need to appropriate the shortfall. To meet any shortfalls, the County would have access to any surplus from operation of the facility, a \$1 million Operating Reserve, and Debt Service Reserve Fund. In addition, the 192 parking spaces built with this project generate annual net income estimated at \$175,000 that could be used to mitigate any gap in the rent paid by the Capitals. Moreover, the skating facility and the parking garage paid real estate taxes of \$294,336.84 in 2007.

The initial debt service on the Series 2005 Bonds was paid from the capitalized interest fund, which was funded with the initial bond proceeds and interest earned on available project funds. The Capitals started paying the annual rent on July 1, 2007; the payment has been used by IDA to

pay the monthly debt service on the bonds. To date, capitalized interest funds, interest earned, and rental payments from the Capitals have fully covered debt service on the bonds.

The interest rate on the Series 2005 Bonds is currently reset weekly and approximates the 1-month London Interbank Offering Rate (“LIBOR”). The rates have fluctuated from a low of 3.06 percent in May 2005 to a high of 5.95 percent in September 2007; as of December 31, 2007, the rate was 4.95 percent. At the time of the closing of the bond sale in May 2005, the IDA negotiated with Lehman Brothers an agreement that established a maximum interest rate of 6 percent; this agreement expires in May 2008.

The Indenture governing the Series 2005 Bonds allows the interest rate on the bonds to be set for different periods of time. When the bonds were initially issued, they were issued in “Weekly Mode,” in which the interest rate on the bonds is reset each week. The interest rate on the bonds has reset each week since the initial issuance. The Indenture permits the interest rate on the bonds to reset in a number of different frequencies. These include another short-term mode in which the interest rate is reset every 1 to 360 days, and two longer-term modes, in which the interest rate may be fixed up to the final maturity of the bonds. Fluctuations in market conditions may make alternative modes more attractive at various times.

County staff and its financial advisor track market rates and monitor opportunities to lower the overall debt service on the bonds. The authorization requested of the Board in this report will allow the County Manager or the Director of the Department of Finance to act as soon as an opportunity arises to change the interest rate reset period from a weekly period to a longer term mode period, taking into consideration the fixed commitment from the Capitals to pay \$2.4 million in annual rent. The goal of this approach will be to lower the anticipated debt service on the bonds to limit the County’s interest rate exposure on the bonds.

DISCUSSION: County staff and its financial advisor have followed the market in search of opportunities to minimize the County’s interest rate exposure on the Series 2005 Bonds. As the Federal Open Market Committee (“FOMC”) has cut the Federal Reserve target rate, short-term interest rates have declined. The market generally expects the FOMC to continue to cut rates in 2008. Future reductions in interest rates may allow the County to convert the interest rate mode on the Series 2005 Bonds and lock in interest rates that will eliminate or reduce the current risk the County’s Board has to appropriate funds to cover any debt service shortfall.

FISCAL IMPACT: If the Series 2005 Bonds are converted to an alternative interest rate mode, it would reduce the County’s interest rate exposure on the bonds, which would create a positive fiscal impact for the County.

A RESOLUTION OF THE COUNTY BOARD OF
ARLINGTON COUNTY, VIRGINIA
AUTHORIZING THE INTEREST RATE COVERSION OF THE INDUSTRIAL
DEVELOPMENT AUTHORITY OF ARLINGTON COUNTY, VIRGINIA'S TAXABLE
ECONOMIC DEVELOPMENT REVENUE BONDS
(SKATING FACILITY PROJECT), SERIES 2005

WHEREAS, the Industrial Development Authority of Arlington County, Virginia (the "Authority") issued its Taxable Economic Development Revenues Bonds (Skating Facility Project), Series 2005 (the "Bonds") for the purpose of financing a portion of the cost of construction of certain ice skating facilities on top of the Ballston Commons Parking Garage, including the construction of an eighth level slab and parking facilities (the "Project");

WHEREAS, the Bonds were issued as variable rate bonds pursuant to an Indenture of Trust dated as of May 1, 2005 (the "Indenture"), between the Authority and Wells Fargo Bank, N.A., as trustee;

WHEREAS, Arlington County, Virginia (the "County") is, subject to appropriation, obligated to make payment to the Authority sufficient in timing and amount to pay the debt service on the Bonds, pursuant to a Cooperation Agreement dated as of May 1, 2005 (the "Cooperation Agreement"); and

WHEREAS, the County Board (the "County Board") of the County has determined that it may be necessary to change the interest rate mode on the Bonds pursuant to the terms of the Indenture, to minimize the County's interest rate exposure on the Bonds.

NOW, THEREFORE, BE IT RESOLVED BY THE COUNTY BOARD OF ARLINGTON COUNTY, VIRGINIA:

1. County Consent to Change the Interest Rate Mode. The County Board requests the Authority to change the Bond's interest rate mode, pursuant to the terms of the Indenture, to minimize the County's interest rate mode exposure on the Bonds, if determined to be advantageous by the County Manager or the Director of the Department of Management and Finance.
2. Disclosure Documents. The County Manager and the Director of the Department of Management and Finance, or either of them, and such officers and agents of the County as either of them may designate, are hereby authorized and directed to prepare, execute, if required, and deliver appropriate disclosure relating to the County prepare, execute, if required, and deliver appropriate disclosure relating to the County and the Project as may be required for any official statement, reoffering document or other offering or disclosure document to expedite the remarketing of the Bonds. The County Manager, or such other officer or agent of the County as he may designate, is authorized and directed to deem the official statement "final" with respect to such disclosure for purposes of Securities and Exchange Commission Rule 15c2-12.

3. Continuing Disclosure. The County Manager is authorized and directed to enter into a Continuing Disclosure Agreement for the benefit of the owners of the Bonds to assist the Authority and the underwriter for the Bonds in complying with the provisions of Section (b)(5) of Securities and Exchange Commission Rule 15c2-12.

4. Further Actions. The County Manager and the Director of the Department of Management and Finance, or either of them, and such officers and agents of the County as either of them may designate, are authorized and directed to take such further action as they deem necessary or appropriate in furtherance of the transactions contemplated by this Resolution and all actions taken by such officers and agents in connection with any of the foregoing are ratified and confirmed.

5. Effective Date. This Resolution shall take effect immediately.

CERTIFICATE OF THE CLERK
OF THE COUNTY BOARD OF
ARLINGTON COUNTY, VIRGINIA

At a regular meeting of the County Board of Arlington County, Virginia, held on the ____ day of _____, 2008, the following County Board members were recorded as present:

PRESENT:

On motion by _____, seconded by _____, the foregoing Resolution was adopted by a majority of the members of the County Board recorded as follows:

MEMBER

VOTE

Dated: _____, 2008

CLERK, ARLINGTON COUNTY BOARD