OFFICE OF THE CONTROLLER
CITY AND COUNTY OF SAN FRANCISCO

Ben Rosenfield
Controller

Todd Rydstrom
Deputy Controller

Anna Van Degna
Director of Public Finance

MEMORANDUM

TO: Honorable Members, Board of Supervisors

FROM: Anna Van Degna, Director of the Controller's Office of Public Finance
Luke Brewer, Controller's Office of Public Finance
Bob Beck, Director of the Treasure Island Development Authority

DATE: **Tuesday, October 5, 2021**

SUBJECT: Resolution Authorizing the Issuance of Improvement Area No. 2 of the City and County of San Francisco Community Facilities District No. 2016-1 (Treasure Island) Special Tax Bonds, Series 2021 Not to Exceed $25,130,000; and

Ordinance Appropriating proceeds from the issuance of Special Tax Bonds of the City's Improvement Area No. 2 of the CFD No. 2016-1 (Treasure Island)

Recommended Actions

We respectfully request that the Board of Supervisors ("Board") consider for review and approval the resolution (the "Bond Resolution") which authorizes the issuance of, in one or more series, not to exceed $25,130,000 aggregate principal amount of Improvement Area No. 2 of the City and County of San Francisco Community Facilities District No. 2016-1 (Treasure Island) Special Tax Bonds, Series 2021 (the "Bonds").

A supplemental ordinance appropriating (the "Ordinance") the proceeds of the Bonds will be also introduced. The Bond Resolution and the Ordinance are anticipated to be heard at the Budget & Finance Committee meetings on October 20, 2021 and November 10, 2021 respectively.

Background

Since 1997, the City and County of San Francisco ("City") and the Treasure Island Development Authority ("TIDA") have worked together on the Treasure Island/Yerba Buena Island Development Project ("Project") in order to redevelop the former Treasure Island Naval Station ("NSTI") in connection with the conveyance of the Navy-owned lands to TIDA. In early 2003, TIDA and the Treasure Island Community Development, LLC [1] ("TICD" or the "Developer") entered into an Exclusive Negotiating Agreement and began work on a Development Plan.

1. The existing members of TICD are (1) Treasure Island Holdings, LLC, a joint venture comprised of a subsidiary of Lennar Corporation and a non-managing third-party investor member, (2) TICD Hold Co., LLC, an indirect subsidiary of Lennar, (3) KSWM Treasure Island, LLC, a joint venture comprised of affiliates of Stockbridge Capital Group, LLC, Kenwood Investments, and Wilson Meany, LP, and (4) Stockbridge TI Co-Investors, LLC, an affiliate of Stockbridge.

In 2011, TICD and TIDA entered into the Disposition and Development Agreement ("DDA") and TICD and the City entered into the Development Agreement ("DA") to deliver the Project. The Financing Plan attached to the DDA and DA contemplates reimbursement to the Developer for costs incurred to construct public infrastructure through the issuance of special tax bonds issued under the Mello-Roos Community Facilities Act of 1982 and tax increment bonds issued by the City and County of San Francisco Infrastructure and Revitalization Financing District No. 1 (Treasure Island).

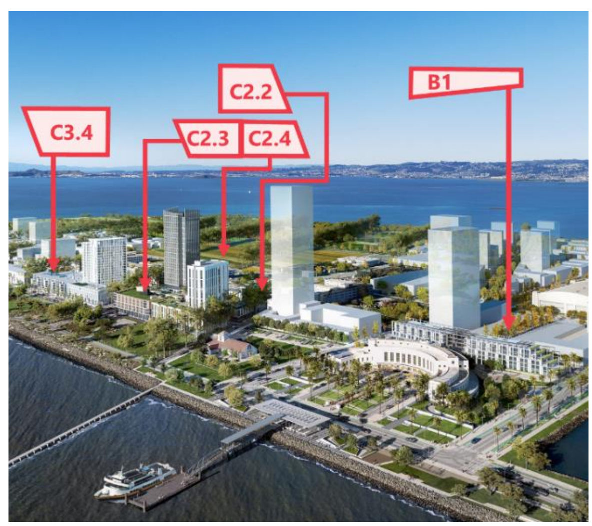
The development plan for the Project anticipates a new San Francisco neighborhood consisting of up to 8,000 new residential housing units, as well as new commercial and retail space, a hotel, and 290 acres of parks and public open space, including shoreline access and cultural uses. Transportation amenities being built for the project will enhance mobility on the Yerba Buena Island and Treasure Island as well as link the islands to mainland San Francisco. Some amenities include a combined police/fire emergency services building; utility improvements including new water, sewer, storm, gas, electrical and communications infrastructure with new water storage reservoirs and a wastewater treatment plant; new and upgraded streets, public byways, bicycle, transit, and pedestrian facilities; and a new ferry terminal.

The Treasure Island CFD

The Treasure Island CFD was formed to provide funding for certain public infrastructure to be built as a result of the Project and certain ongoing public services. On January 24, 2017, following a public hearing and landowner vote, the Board adopted Resolution No. 8-17 ("Resolution of Formation") establishing the Treasure Island CFD, an initial improvement area in the Treasure Island CFD entitled "Improvement Area No. 1 of the City and County of San Francisco Community Facilities District No. 2016-1 (Treasure Island)" ("Improvement Area No. 1"), and a Future Annexation Area for the Treasure Island CFD, which was established to provide for streamlined annexations of future phases of the Project into the CFD.

<u>Improvement Area No. 2</u>

Improvement Area No. 2 (or "IA No. 2") consists of up to five development parcels (B1, C2.2, C2.3, C2.4 and C3.4) located on Treasure Island, which are expected to include 777 residential units at buildout, as depicted in the rendering the right.



In April 2020 the development parcels were annexed into the Treasure Island CFD as IA No. 2 through Unanimous Approval by the property owners, based in compliance with the Annexation Approval Procedures established by on the Board Approved Annexation Procedures in the Resolution of Formation. In September 2020 the Board of Supervisors adopted Resolution No. 410-20 to confirm the annexation of property and confirm that the maximum aggregate principal amount of special tax bonds and other debt to be issued by IA No. 2 is $278,200,000.

The proposed Bond Resolution authorizes the sale of an aggregate principal amount not to exceed $25,130,000 and approves related financing documents. If the full not to exceed amount of Bonds are issued, the remaining bond authority for Improvement Area No. 2 would be $253,070,000.

The Special Tax Bonds of Improvement Area No. 2

The proposed Bonds will be secured by a pledge of special taxes levied on taxable property in Improvement Area No. 2. In accordance with Ordinance No. 22-17 and the Rate and Method of Apportionment of Special Tax for Improvement Area No. 2 (the "RMA") approved by Unanimous Approval at annexation and confirmed by the Board in Resolution No. 410-20, the City has the authority to begin levying special taxes on all taxable property within IA No. 2. There was no special tax levied for FY 2021-22 as there were no special tax bonds issued and outstanding at that time, and no development parcel had received a final building permit required for vertical development ("Building Permit") as of June 30, 2021. As a result of issuing the proposed Bonds and expectations of certain development parcels receiving building permits by June 30, 2022, the City anticipates levying special taxes in IA No. 2 in FY 2022-23.

Current Plan of Finance

The proposed Bonds will be sold without a rating ("Non-Rated"), given the risks associated with this land secured financing, which is secured by property in an early stage of development. Thus, these Bonds would not receive an investment grade rating. Non-Rated special tax bonds (or "Land Secured bonds") have unique credit considerations and risk factors for investors which are discussed in the Official Statement, including:

- Until fully built-out, all Land-Secured bonds bear some degree of development risk. In troubled real estate markets, projects can struggle and may be abandoned by developers and/or homebuilders potentially leading to their inability or refusal to pay special taxes when due.
- Taxpayer concentration risk, as the Bonds are secured by only the vertical developers at this time.

All of the property in IA No. is owned by merchant builders. Three of the landowners are affiliates of the Developer. One of the landowner/merchant builders is Poly (USA) Real Estate Development Corporation. It is not an affiliated entity with the Developer and its parent company is a relatively new entity, having been formed in 2016 according to information on its website. It owns property entitled for 200 units, more than 25% of the total entitled units for IA No. 2.

The Bonds are limited obligations of the City, secured by and payable solely from the special taxes levied in Improvement Area No. 2.

The General Fund of the City is not liable for the payment of principal or interest on the Bonds, and the credit of the City is not pledged to the payment of the Bonds.

While the General Fund of the City is not liable for the payment of the debt, the Bonds still carry the "City and County of San Francisco" issuer name and market recognition, and as such the City is subject to reputational risk.

Under the Fiscal Agent Agreement, the City, on behalf of the District, has covenanted for the benefit of the owners of the Bonds that, under certain circumstances, the City will commence judicial foreclosure proceedings with respect to delinquent special taxes on property within IA No. 2, and will diligently pursue such proceedings to completion.

The proposed Bonds will be secured by a pledge of special taxes levied on all of the taxable property in IA No. 2 pursuant to the RMA, and at current projected interest rates produce approximately 256% debt service coverage on the proposed Bonds when compared to maximum projected special tax revenues from all development parcels at buildout. Debt service on the Bonds escalates at approximately 2% per year, in accordance with the 2% per year escalation of the special taxes, per the RMA.

Value-to-Lien Ratio

Under the City's *Local Goals and Policies – Community Facilities Districts and Special Tax Districts*, the City is required to have a minimum a value-to-lien ratio ("VTL") of 3-to-1 at issuance based on (i) an appraised value (in this case) or assessed value and (ii) special tax and assessment debt encumbering the taxable property. The estimated value-to-lien ratio based on the proposed not to exceed par amount of $25,130,000 and the current appraised value (as of August 1, 2021) of the property in IA No. 2 of $75,400,000 is 3-to-1.

Integra Realty Resources, Inc. (the "Appraiser") has prepared an Appraisal Report dated September 16, 2021 with a valuation date of August 1, 2021, estimating the market value of the fee simple interest in the five development parcels within IA No. 2 currently subject to the special taxes. The Appraiser concluded in the Appraisal Report that the market value of the fee simple interest of these parcels is $75,400,000, subject to certain assumptions and limiting conditions set forth therein. The value of individual parcels in Improvement Area No. 2 may vary significantly, and no assurance can be given that should Special Taxes levied on one or more of the parcels become delinquent, and should the delinquent parcels be offered for sale at a judicial foreclosure sale, that any bid would be received for the property or, if a bid is received, that such bid would be sufficient to pay such parcel's delinquent Special Taxes. Land values for properties that are not yet fully developed can be extremely volatile, which is why the City and its financing team are currently evaluating whether to issue fewer bonds than the not to exceed principal amount of $25,130,000.

Use of Proceeds

The proceeds of the Bonds will (i) finance or reimburse expenditures on public improvements for the Project, (ii) fund a debt service reserve fund for the Bonds, (iii) fund capitalized interest on the Bonds, if any, (iv) fund administrative expenses, and (v) finance costs of issuance. More specifically, the proceeds of the proposed Bonds are expected to reimburse the Developer for developer qualified costs, such as on-site infrastructure costs, including utility improvements, street improvements, curb, gutter and sidewalk improvements, streetlights, and traffic signals, and related pre-development costs.

Table 1 below outlines anticipated sources and uses for the Bonds, based on current market conditions, at the not to exceed par amount of $25,130,000.

Table 1: Estimated Not to Exceed Sources & Uses of the Special Tax Bonds, Series 2021

Sources:	
Bond Proceeds	
Not to Exceed Par Amount	$25,130,000
Premium	910,000
Total Sources	**$26,040,000**
Uses:	
Improvement Fund	$22,275,000
Debt Service Reserve Fund	1,920,000
Capitalized Interest Fund	720,000
Delivery Date Expenses	
Cost of Issuance	$750,000
Underwriter's Discount	$375,000
Total Uses	**$26,040,000**

Source: Stifel and CSG Advisors Inc.

The City, in consultation with its legal counsel, underwriting team and municipal advisor will evaluate the feasibility of an early stage bond issuance at minimum industry standard level value to line of 3-to-1. Given underwriting criteria and risks associated with early stage developments, the Bond size may be smaller than the not-to-exceed amount of $25,130,000 or the Bonds may be issued in multiple series over time as development milestones occur. Additionally, the City's Municipal Advisor and Underwriter may determine that higher minimum denominations should be used or limit the bond offering in order to meet investor suitability requirements. Conditions that could result in a change in the anticipated par amount include accelerated or delayed development, a delayed issuance of the Bonds, increases in the Appraised Value, fluctuations in market interest rates between the date of authorization by the Board and the sale of the Bonds, changes in required deposits for reserves or in estimated delivery date expenses, or market response to the early stage of development in IA No. 2.

The difference between the not to exceed principal amount of $25,130,000 and the not to exceed amount of $31,630,000 in the appropriation ordinance is to provide for budgetary flexibility in the case where the City potentially receives additional proceeds resulting from bond premium, which is a common phenomenon in tax-exempt bonds due to the very low interest rate environment and investor preferences. The lower interest rates get, the higher the bond premiums investors must pay to the City in order to buy the bonds.

<u>Interest Rate; Projected Debt Service</u>

Based upon current market conditions, a 30-year term and a true interest cost of 3.84%, which assumes the issuance up to the not to exceed amount of the Bonds on a tax-exempt basis, the Office of Public Finance estimates average annual debt service to be approximately $1.54 million. The not to exceed total par amount of $25.13 million is estimated to result in approximately $20.54 million in interest payments over the life of the Bonds. The total debt service over the life of the Bonds is estimated at approximately $45.67 million.

<u>Negotiated Sale of the Bonds; Underwriters</u>

A negotiated sale is planned in connection with this transaction. The Bonds are repaid from special tax revenues from taxable property within Improvement Area No. 2 and are outside of the City's customary credit profile. Through a competitive Request for Proposals ("RFP") process, Stifel, Nicolaus & Company, Incorporated ("Stifel") was selected to serve as Senior Underwriter and RBC Capital Markets, LLC, ("RBC") was selected to serve as Co-underwriter (together, "Underwriters"). The Underwriters were selected via the RFP process to the City's Underwriter Pool, which was also established via a competitive process. The proposed Bond Resolution approves the form of the Bond Purchase Agreement (described further below) which provides the terms of sale of the Bonds by the City to the Underwriters.

<u>The Capital Plan</u>

The Bonds are limited obligations of the City payable solely from the special tax revenues within Improvement Area No. 2 and therefore are not subject to policy constraints of the Ten-Year Capital Plan.

Additional Information

The Bond Resolution is expected to be introduced at the Board of Supervisors meeting on Tuesday, October 5, 2021. The forms of the financing documents related to the Special Tax Bonds—including the

Bond Purchase Agreement, Fiscal Agent Agreement, Preliminary Official Statement, the Continuing Disclosure Certificate and related documents—will also be submitted.

Bond Purchase Agreement: The City intends to issue the Bonds on a fixed rate basis through a negotiated sale with the Underwriters. The Bond Purchase Agreement sets forth the terms, covenants, and conditions for the sale of the Bonds with the Underwriters, as well as agreements regarding expenses, closing and disclosure documents.

Fiscal Agent Agreement: The proposed Bond Resolution also approves the form of the Fiscal Agent Agreement pursuant to which the Fiscal Agent administers and disburses bond payments. The Fiscal Agent Agreement provides for the terms of the bond redemption, prepayment provisions, and other related administrative provisions. The Fiscal Agent holds the Treasure Island CFD special taxes and the bonds proceeds derived from the sale of the Bonds and will disburse the proceeds as directed by authorized City representatives.

Official Statement: The Official Statement provides all material information for investors in connection with the public offering by the City of the Bonds. The Official Statement describes the Bonds, the Project, including sources and uses of funds; security for the Bonds; development conditions in IA No. 2; the developers' financing plans; risk factors; an appraisal of the property and tax and other legal matters, among other material information.

A *Preliminary Official Statement* is distributed to investors prior to the sale of the Bonds and, within seven days of the public offering, the *Final Official Statement* (adding certain sale results including the offering prices, interest rates, selling compensation, principal amounts, and aggregate principal amounts) is distributed to the prospective purchasers of the Bonds.

The antifraud provisions of the federal securities laws require that offering documents prepared by issuers of municipal securities, like the special tax bonds here, that the document be accurate and complete in all material respects. This obligation applies to the individual members of the governing bodies approving the document as well as City staff charged with preparing the document. Much of the information in the Official Statement was provided by the Developer and the landowner/merchant builders, and those entities will certify in writing that the information provided by the Developer is accurate and complete in all material respects. The draft Preliminary Official Statement, which has been critically reviewed by the City's staff and outside financial professionals, has been submitted for your review prior to its publication.

The Board of Supervisors and the Mayor, in adopting and approving the Bond Resolution, approve and authorize the use and distribution of the Preliminary and Final Official Statements by the Underwriters and co-financial advisors with respect to the Bonds. For purposes of the Securities and Exchange Act of 1934, the Controller will certify, on behalf of the City and the District, that the Preliminary and Final Official Statements are final as of their dates.

Continuing Disclosure Certificate: The City covenants, on behalf of the District, to provide certain financial information and operating data relating to the Bonds (the "Annual Report") not later than 270 days after the end of the fiscal year and to provide notices of the occurrence of certain enumerated events, if material. The Continuing Disclosure Certificate describes the nature of the information to be contained in the Annual Report or the notices of material enumerated events. These covenants have been made in order to assist the Underwriters of the Bonds in complying with the Securities and Exchange Commission Rule 15c2-12(b)(5).

Anticipated Financing Timeline

Milestones	Dates*
• Introduction of the Resolution and the Ordinance to the Board	October 5, 2021
• Presentation to Capital Planning Committee	October 18, 2021
• Budget & Finance Committee Hearing (Resolution)	October 20, 2021
• Board Approval of the Resolution	October 26, 2021
• Budget & Finance Committee Hearing (Ordinance)	November 10, 2021
• Board Considers Approval of the Ordinance (1st Reading)	November 16, 2021
• Final Board Approval of the Ordinance (2nd Reading)	November 30, 2021
• Sale and Closing of the Bonds	December 2021

*Please note that dates are estimated unless otherwise noted.

Your consideration of this matter is greatly appreciated. Please contact Anna Van Degna (anna.vandegna@sfgov.org) or Luke Brewer (luke.brewer@sfgov.org), if you have any questions.

cc: Angela Calvillo, Clerk of the Board of Supervisors
Andres Powers, Mayor's Office
Ashley Groffenberger, Mayor's Budget Director
Ben Rosenfield, Controller
Carmen Chu, City Administrator
Ken Bukowski, Deputy City Administrator
Harvey Rose, Budget & Legislative Analyst
Severin Campbell, Budget & Legislative Analyst
Mark Blake, Deputy City Attorney
Kenneth Roux, Deputy City Attorney

Attachment 1

GOOD FAITH ESTIMATES

For purposes of compliance with Section 5852.1 of the California Government Code, the following information are good faith estimates provided by the City's Underwriters, and the City's Municipal Advisor CSG Advisors Incorporated assuming the maximum bond authorization of $25,130,000:

1. True interest cost of the Bonds: 3.84%

2. Finance charge for the Bonds, including all fees and charges for third parties (including underwriter's compensation, municipal advisory fees, co-bond counsel fees, disclosure counsel fees, trustee fees and other payments to third parties): $1,125,000.

3. Amount of Bond proceeds expected to be received by the City, net of payments identified in 2 above and any reserve fund or capitalized interest funded with proceeds of the Bonds: $22,275,000.

4. Total payment amount for the Bonds, being the sum of (a) debt service on the Bonds to final maturity, and (b) any financing costs not paid from proceeds of the Bonds: $45,670,000.

The information set forth above is based up estimates of prevailing market conditions. Actual results may differ if assumed market conditions change.