ITEM NO.: 7a

DATE OF MEETING: 10/05/2010

Commercial Paper Letter of Credit Extension

October 5, 2010

Port of Seattle

Introduction

- Bank of American Letter of Credit (LOC) for $100 million commercial paper (CP) expires in November, 2010
- Port has negotiated an extension of the LOC
- Due to numerous changes since 1997, the LOC agreement will be amended and restated
  - Pursuant to Resolution No. 3456, authority to extend the letter is delegated to the Port's CFO
- This briefing will highlight key changes included in this extension
  - Impact of financial crisis
  - Negative and positive changes
- Update on the next LOC expiration in January, 2011

Introduction – Variable Rate Debt

The Port uses LOCs to provide liquidity and credit support to its variable rate debt

- The Port uses two types of variable rate debt
  - Long-term bonds with floating interest rates
  - Short – term commercial paper
- Variable rate debt is a useful component of the Port's debt portfolio
  - Low cost - short term rates are lower than long term rates
    - Currently – about 30 – 50 basis points
    - Average since 1997 – approximately 2.5%
  - Risk management - variable rates on debt off-set variable rates on investments

Background – Commercial Paper

- 1997 Port instituted a CP program for $100 million
  - Issued on the Port's Subordinate Lien, secured by operating revenues after payment of prior lien debt service
  - Short-term borrowing – maturities less than 270 days
  - Can "roll over" multiple times (revolving credit)
  - Used as bridge financing in anticipation of grant receipts or long-term debt issuance
  - Initial program backed by an LOC from Bank of America
- 2001 Port increased the program to $250 million
  - Added an LOC for $150 million with Bayerische Landesbank (BLB)

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Letter of Credit function

- A direct pay LOC provides immediate liquidity support
  - When the Port rolls-over maturing CP, if there are no investors the LOC bank will buy and hold the CP until
    - 1. an investor is found
    - 2. the Port pays off the CP
  - If repayment has not occurred after 6 months (liquidity period), the Port begins repayment to the bank over an extended time period. This feature of the LOC is referred to as “term out” or “term out loan”.
    - Port LOCs typically provide for a 5-year “term-out” or 5 years to repay the CP held by the bank
  - While the bank holds CP, the Port pays the bank an interest rate to the bank established in the LOC documents

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2008 Financial Crisis

- The financial crisis resulted in significant constraints on credit and therefore, the LOC market
  - Fewer LOC providers
  - Providers are more selective – prefer existing clients or clients with whom they have more extensive relationships
  - Credit approvals are slower and often involve bank staff who are not familiar with municipal credits

- More cost and risk have shifted to the borrower
  - Fees have increased significantly
  - LOCs are typically now 1-3 years in term rather than 3-7 years
  - Liquidity periods (period bonds or notes are held by the bank prior to term-out) and term-out periods are shorter
  - Covenants have become more restrictive and there are more Events of Default

Bank of America LOC - Changes

Consistent with the current LOC market this LOC extension includes several changes adverse to the Port

- <u>LOC fee</u> – increases from 20 basis points to 140 basis points
- <u>Early termination</u> – Port can terminate at any time, but fee is paid for first 3 years instead of first 1 year (unless the banks credit is downgraded)
- <u>Bank rate</u> – the interest rate the Port pays if CP is held by the bank is a minimum 7.5% rather than Fed Funds + 50-150 basis points
- <u>Downgrade</u> – A below investment grade rating on the Port's Subordinate Lien is an Event of Default

Bank of America LOC - Changes

There are several provisions that are better than the Port's current agreement and lower the Port's risk

- The Port was able to preserve
  - Expiration – LOC is issued for 5 years
  - Liquidity period – 6 months
  - Term out - 5 years
- Port was able to improve
  - Set-off - re-written with appropriate restrictions and clarifications to protect the Port and maintain the integrity of existing liens
  - Cure periods – extended for certain Events of Default
  - Lower risk of triggering a default
    - Higher threshold for certain problems to become a default
    - Fewer repetitive representations that could trigger a default

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Schedule

- Bank of America LOC for CP
  - Extension and amendments will take effect in November upon expiration of the current LOC

- New LOC for Seaport Variable Rate bonds
  - Existing LOC expires January, 2011
    - provider is not longer offering LOCs
  - Per FT-01 policy – competitive solicitation for a new LOC
    - Only 3 responses
    - Best offer from Bank of America
  - Resolution No. 3238 delegates authority to the CFO to negotiate and execute the LOC agreement

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