

- Water Revenue Refunding Bonds,
2008 Series A1-A2 Issue

Summary

On March 25, 2008, Metropolitan closed a \$501.6 million variable rate Water Revenue Refunding Bond issue to refund \$500.3 million of water revenue bonds (Auction Rate Securities).

Detailed Report

Metropolitan priced the \$501,575,000 Water Revenue Refunding Bonds, 2008 Series A-1 and Series A-2 issue (the "2008 Series A bonds") as variable rate demand bonds on March 24, 2008, at an initial interest rate of 1.85 percent. The transaction closed on March 25, 2008. The 2008 Series A bonds will initially bear interest in a weekly mode. The 2008 Series A bonds were issued for the purpose of refunding all of Metropolitan's \$500.3 million of outstanding Auction Rate Securities (ARS).

As discussed in the March 11, 2008 Board Letter No. 7-2, and at the Business and Finance Committee meeting of March 10, 2008, the ARS market has undergone severe and well-publicized dislocations. The recent turmoil in the ARS market due to the fallout from the credit downgrades of the municipal bond insurers and the continuing liquidity crisis caused auction rate programs throughout the country to experience higher interest costs and failed auctions. The problems that have developed in the ARS market are systemic, and have affected all municipal governments that have issued ARS. Metropolitan had six series of ARS totaling \$500.3 million, all insured by XLCA. Since the onset of the breakdown in the ARS market in February 2008 and the credit downgrade of XLCA, interest rates on Metropolitan's ARS were resetting at 250 to 700 basis points higher than Metropolitan's variable rate demand bonds which have reset at one percent to two percent over the past month. There was, and continues to be, no evidence that the ARS market will stabilize, and that interest rates will return to normal market levels. Approximately 70 percent of all auctions failed over the past month. Metropolitan staff analyzed the potential financing options available, and determined that the most cost-effective way to exit the ARS market was to refund Metropolitan's outstanding ARS with variable rate water revenue refunding bonds. Given Metropolitan's strong credit rating, the variable rate demand bonds are supported with standby bond purchase agreements and are uninsured.

An appropriation for the cost of issuance of the refunding bonds was approved by the Board at the March 2008 Board meeting. The 2008 Series A Bond refunding transaction is anticipated to save Metropolitan approximately \$4.4 million per year through final maturity of the refunding bonds in July 2037, or approximately \$89.2 million on a net present value basis, assuming that the VRDOs trade about 1.50 percent lower than insured ARS. The average life of the refunding bonds is approximately 17.3 years.

Metropolitan has two underwriters on the transaction, Banc of America Securities LLC which will serve as remarketing agent for the \$250.94 million 2008 Series A-1 bonds, and Citigroup Global Markets Inc. which will serve as remarketing agent for the \$250.64 million 2008 Series A-2 bonds. Bank of America, N.A. will provide liquidity for the 2008 Series A-1 bonds, and Landesbank Baden-Wurtemberg (LBBW) will provide liquidity for the 2008 Series A-2 bonds. Public Resources Advisory Group served as financial advisor. Fulbright & Jaworski L.L.P. and Alexis S.M. Chiu, Esq., served as co-bond counsel. Wells Fargo Bank, N.A. will serve as paying agent and escrow agent, and Grant Thornton LLP served as verification agent.

The estimated costs and expenses associated with the 2008 Series A bonds are as follows:

Board Report (Water Revenue Refunding Bonds, 2008 Series A1-A2 Issue)

Estimated Costs:

	<u>Amount</u>	<u>\$/1,000 Bond</u>
Rating Agencies	\$ 240,000	\$ 0.48
Co-Bond Counsel	\$ 90,000	0.18
Financial Advisor	\$ 65,000	0.13
Liquidity Bank Counsel	\$ 63,000	0.13
Printing/Mailing	\$ 20,000	0.04
Paying/Escrow Agent	\$ 10,500	0.02
Other/Contingency	<u>\$ 11,500</u>	<u>0.02</u>
Total	<u>\$ 500,000</u>	<u>\$ 1.00</u>

Underwriter's Discount:

	<u>Amount</u>	<u>\$/1,000 Bond</u>
Takedown (sales fees)	\$ 752,363	\$ 1.50
Expenses		
- Underwriters Counsel	\$ 25,000	0.05
- Other (e.g. CDIAC, SIFMA Fees, etc.)	<u>\$ 43,411</u>	<u>0.09</u>
Subtotal	<u>\$ 820,774</u>	<u>\$ 1.64</u>
Total Costs of Issuance	<u>\$1,320,744</u>	<u>\$ 2.64</u>

Savings from Bond Refundings

Since February 2001, Metropolitan has issued over \$2.42 billion of water revenue refunding bonds, savings are anticipated to be over \$191 million on a present value basis and at least \$11.8 million per year (on average) over the next 20 years. This equates to approximately \$6 per acre-foot of savings on future water rates. The following table summarizes each of the transactions, along with the net present value savings, the average annual savings, true interest cost, and the average maturity of the refunding bond issues:

<u>Revenue Refunding Bond Issue</u>		<u>NPV Savings</u>	<u>Average Annual Savings</u>	<u>True Interest Cost</u>	<u>Average Maturity</u>
2001 Series A	\$195.7M	\$ 9.6 million	\$.7 million	4.50%	12.7 years
2001 Series B1-B2	\$224.8M	\$15.0 million	\$1.0 million	4.22%	15.2 years
2002 Series A&B	\$132.2M	\$ 9.7 million	\$.7 million	3.30%	18.1 years
2003 Series A	\$ 36.2M	\$ 3.0 million	\$.1 million	3.34%	9.1 years
2003 Series C1-C3	\$338.2M	\$21.1 million	\$1.3 million	3.26%	20.8 years
2004 Series A1-A2	\$162.5M	\$11.4 million	\$1.1 million	2.92%	15.4 years
2004 Series B	\$274.4M	\$12.2 million	\$1.1 million	3.14%	8.3 years
2004 Series C	\$136.1M	\$11.0 million	\$.6 million	3.23%	14.9 years
2006 Series A1-A2	\$ 74.1M	\$ 6.4 million	\$.7 million	3.22%	11.3 years
2006 Series B	\$ 45.9M	\$ 2.0 million	\$.1 million	4.48%	16.4 years
2007 Series A1-A2	\$218.4M	NA (a)	NA (a)	NA (a)	9.6 years
2007 Series B	\$ 81.9M	NA (a)	NA (a)	NA (a)	26.8 years
2008 Series A1-A2	\$501.6M	\$89.2 million (b)	\$4.4 million	3.47% (b)	17.3 years

(a) The 2007 Series A1-A2 and 2007 Series B variable rate water revenue refunding bonds were Auction Rate Securities, and were refunded by the 2008 Series A1-A2 variable rate water revenue refunding bonds, anticipated savings reflected in projected savings for the 2008 Series A1-A2 issue.

(b) Variable rate bonds, initial weekly interest rate of 1.85%, weekly interest rates will vary over time. Savings calculations based on an average interest rate of 3.43% on the 2008 Series A1-A2 issue, and an average interest rate of 5.00% on the refunded ARS.

Board Report (Water Revenue Refunding Bonds, 2008 Series A1-A2
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