

October 26, 2015

Marin Emergency Radio Authority  
Finance Committee  
Vice Chair Gaffney and Executive Officer Cassingham.  
Via Email: [tegaffney1@gmail.com](mailto:tegaffney1@gmail.com); [mlc1948@aol.com](mailto:mlc1948@aol.com)

Re: Financial Advisor Scope of Service

Dear Tom and Maureen,

Reflecting our discussion at the organizational meeting in our offices on October 14, 2015 and subsequent exchanges, this letter sets out our understanding of the scope of advisory services to be completed by Sperry Capital Inc. ("Sperry") leading up to the financing of the Next Gen II project.

## **Project Schedule and Cost**

Pending revised information from Federal Engineering, we will use the AECOM System Design Report dated April 29, 2010 as a source of assumptions on cost and schedule. We assume that the project will cost \$40 million and will require 16 months to complete. With the understanding that Federal Engineering has commenced preparation of the bid requirements, we assume that the procurement contract will be awarded with Notice to Proceed in August 2016. We assume that the acquisition will be made with equal monthly payments of \$2.5 million from August 2016 to December 2017.

## **Financing Strategy**

We are planning the Next Gen II financing in a period of historically low long term interest rates, very low rates of return on invested construction funds, expectations that interest rates will rise, but significant uncertainty about the timing of any interest rate changes stemming either from central bank action or market dynamics. There are, then, a number of questions we will address to inform MERA's decisions on what financing alternatives to employ and when to employ them relative to the project acquisition schedule. These questions include but are not necessarily limited to:

1. **What are the pros and cons of getting into the market as soon as possible, given that interest rates may rise?**
  - a. *Scenario 1A* - Sell \$40 M bonds Jan 1, 2016 and invest proceeds until August 2016, when construction starts, and through the 16 month draw period. We will use current market values for the average long term bond rate and the rate of return on bond proceeds. This is meant to represent the strategy of capturing today's historically low long term rates.
  - b. *Scenario 1B* - Wait to sell \$40 M bonds until August 2016, at the time construction will begin. We will calculate the added cost of selling bonds before construction begins

(January 2016) and the amount that rates on the August 2016 bonds can increase before tipping the scales in favor of selling in January.

2. **Since the rate of return on invested bond proceeds is so low relative to the interest cost of fixed rate bonds (negative arbitrage), can we save money by using a commercial construction loan that can be drawn upon as construction progresses and take it out with a bond issue when the project is complete in December 2017?** We will calculate how much interest expense can be saved by drawing down a construction line instead of selling the full \$40 million in bonds in August 2016. Once again we will determine the breakeven rate for the December 2017 sale that would make selling in August 2016 advantageous. We will assume that today's rates exist in August 2016.
3. **Can we reduce negative arbitrage and improve the probability of securing low long term rates by selling \$10 million bonds every four months during the 16 month construction schedule rather than selling the entire amount in August 2016?**
4. **Is the Barclays' incremental issuance program better than 1 through 3?** Barclays has developed a program that "issues" the long term bonds at today's rates in small amounts as needed to fund construction. Interest accrues only on the aggregate amount drawn. Sounds very clever. We are awaiting sample terms.
5. **What financing terms do the vendors of equipment offer?** Are they beneficial?
6. **Will a refinancing of the 2007 New Project Note create a net financial benefit?** We will incorporate the refinancing as an additional option in our analysis.
7. **What market conditions in 2020 will yield refunding savings of at least 3% of the refunded principal?**

Here are the basic debt assumptions we will use:

Bonds:	Construction Loan:
Bond amortization period: 20 years	Origination Fee: 0.5% up front
Underwriter's discount: \$5 per \$1,000	Availability Fee: 0.15% per annum?
Cost of issuance: \$250,000 each issue	Use Fee: 0.25% per annum?
Level debt service	
No debt service reserve	
Yield scale: AAA MMD with premium coupons	

### System Financial Forecast and Analysis

We will prepare an annual revenue and expense projection based on the selected project debt strategy and the following considerations:

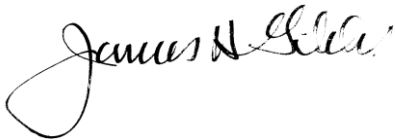
1. O&M projections as they become available and are updated

2. Staging of the procurement process to defer borrowing
3. Alternative strategies of building a Gen III Reserve
4. Financing the System Upgrade Agreement

We are prepared to adjust our scope to reflect new information and decisions as they unfold in coming months. We will first address Question 1 with Scenarios 1A and 1B and once we have reviewed the results with you and the Finance Committee, will, subject to your direction, proceed to analyze the remaining questions.

We are very pleased to begin work and look forward to our continued collaboration.

Best Regards,



James H. Gibbs

Principal