



Regular Meeting

Item Number 4 – Open Session

Subject: Headquarters Expansion Bond Financing Education and Authorization for Issuance of Bonds for Additional Funding

Presenter(s): Julie Underwood/Kevin Civalo, Stradling Yocca Carlson & Rauth/Michael Kremer, Montague DeRose and Associates, LLC

Item Type: Action

Date & Time: November 2, 2022 – 30 minutes

Attachment(s):

Attachment 1 – Bond Resolution – Approval of Financing of Completion Costs of the Headquarters Expansion Project

Attachment 2 – Preliminary Official Statement for The California Infrastructure and Economic Development Bank Lease Revenue Bonds (California State Teachers’ Retirement System Headquarters Expansion) Series 2022 (Green Bonds – Climate Bond Certified)

PowerPoint(s): None

Item Purpose

The purpose of this item is to provide the Teachers’ Retirement Board (board) with a review of the transaction to finance the additional funding approved by the board in January 2022 for the completion of the Headquarters Expansion Project (HQE project) utilizing tax-exempt lease revenue bonds, seek formal authorization to issue the additional bonds, and request approval to deposit with the bond Trustee at the time of issuance, the debt service payments that will be due on August 1, 2023.

Recommendation

Staff recommends the board review the preliminary official statement, Attachment 2, and authorize the issuance of the additional bonds (Series 2022 Bonds) in an amount not to exceed \$19 million, which includes up to \$18.5 million for the completion of the HQE project and approximately \$0.5 million for estimated costs of issuance, by adopting a formal resolution, Attachment 2, authorizing and directing the CalSTRS Chief Executive Officer (or designee) to prepare, approve, execute and deliver (as applicable) all documents necessary to complete the process for the issuance of the additional bonds as tax-exempt lease revenue bonds (Series 2022

Bonds). In addition, staff recommends approval of a not to exceed \$13 million deposit, payable to the bond Trustee at the time of issuance of the Series 2022 Bonds, for the August 1, 2023 debt service payment that will be due for the Series 2019 Bonds and Series 2022 Bonds, to address debt service payments that continue to be due regardless of substantial completion of the HQE project.

Executive Summary

At the November 2018 meeting, the board approved the construction of an expansion structure for CalSTRS headquarters at a cost not to exceed \$300 million utilizing tax-exempt lease revenue bond financing, and those bonds were issued in December 2019 (Series 2019 Bonds). Due to extended HQE project schedules related to permitting issues, cost escalations associated with supply chain shortages and safety measures associated with the prolonged COVID-19 pandemic, additional time and funding was required to complete the HQE project. In January 2022, the board approved additional funding, in the amount of \$18.5 million, utilizing tax-exempt lease revenue bonds (Series 2022 Bonds), as bond financing would be the most cost-effective means to finance the additional costs of the HQE project. At the time, staff recommended, after consultation with our financing team, that CalSTRS issue the bonds after substantial completion of the HQE project.

Since the January 2022 board meeting, the financing team met monthly to monitor bond market conditions, discuss the structure of the financing transaction and determine the optimal time to issue the bonds. Although staff initially recommended to issue the bonds upon substantial completion of the HQE project, which is projected to be late March 2023, the financing team is now recommending issuance of the bonds as soon as practical. The Series 2022 Bonds can be issued as soon as December 2022. The recommendation to move forward with issuance of the Series 2022 Bonds prior to completion of the HQE project results from staff's increased confidence in the final cost to complete the headquarters expansion and the likelihood of continued increases by the Federal Reserve of interest rates to address inflation. It should be noted, by issuing the Series 2022 Bonds prior to completion of the HQE project, interim funding from the State Teachers' Retirement Plan would not be needed to cover any budget shortages, which was originally contemplated.

Board approval of the bond offering

The board is required to authorize the issuance of the Series 2022 Bonds, which is accomplished by adopting the Bond Resolution (see Attachment 1). The board is also required to ensure there is a robust disclosure process in place with the appropriate level of staff involved in the preparation and review of the bond disclosures. To ensure compliance with all disclosure requirements, the financing team includes senior members of CalSTRS staff from the Financial Services, Investments, Administrative and Legal branches that are deeply involved in the preparation and review of the principal bond documents and the preliminary official statement (the offering document that will be provided to prospective purchasers of the Series 2022 bonds).

The draft preliminary official statement (see Attachment 2), which provides many critical disclosures, is provided for board review and any input is requested at the meeting.

The Bond Resolution includes information on the bond financing transaction and requires the issuance of the bonds to be subject to certain parameters, including not to exceed amounts for the par amount of the bonds, true interest cost, annual lease payments, term of the bonds/lease and the underwriters' discount, if applicable. It also authorizes the Chief Executive Officer (or designee) to prepare, approve, execute, and deliver (as applicable) all documents necessary to complete the process for the issuance of the Series 2022 Bonds. In addition, the Bond Resolution authorizes the Chief Executive Officer (or designee) to deposit up to \$13 million with the bond Trustee at the time of issuance of the Series 2022 Bonds, for the amount of the debt service payments that will be due on the Series 2019 Bonds and Series 2022 Bonds on August 1, 2023 (capitalized interest payments on deposit for the Series 2019 Bonds currently only extend through February 1, 2023). Since the HQE project will not be substantially completed on February 1, 2023, we need to provide the Bondholders assurance that the scheduled debt service payments will be made as scheduled, as CalSTRS technically does not have a legal obligation to make debt service payments until substantial completion of the HQE project. Therefore, we need to ensure the bond Trustee has sufficient funds on deposit to pay the debt service payments that will be due on August 1, 2023 (see *Deposit of Debt Service Payments* section below).

Background

Staff has been working with its professional bond advisors to develop a plan with the steps necessary to successfully issue the Series 2022 bonds as follows:

Financing Team

As a reminder, the Financing Team is responsible for the successful issuance of the bonds. The team's primary responsibilities are to finalize the financing plan, prepare and finalize legal documents, develop offering documents, prepare for any rating agency and investor presentations, market the bond offering to investors, price the bonds and close the transaction. To minimize costs, we have retained the same financing team that assisted with the issuance of the Series 2019 Bonds, except for bond counsel, as Stradling Yocca Carlson & Rauth, who served only as disclosure counsel for the Series 2019 Bonds, has the experience to serve a dual role, including bond counsel, which assists CalSTRS in minimizing the overall financing costs. In addition to senior CalSTRS staff, the financing team is as follows:

Bond Issuer/Lessor:	California Infrastructure and Economic Development Bank
Agent for Sale:	CA State Treasurer
Bond and Disclosure Counsel:	Stradling Yocca Carlson & Rauth
Municipal Advisor:	Montague DeRose and Associates, LLC
Trustee:	BNY Mellon Corporate Trust

The Bond Financing Transaction

The bond financing transaction will have a similar structure to the Series 2019 Bonds, which were titled, California Infrastructure and Economic Development Bank Lease Revenue Bonds (California State Teachers' Retirement System Headquarters Expansion) Series 2019 (Green Bonds – Climate Bond Certified) (the “Series 2019 Bonds”). The new issuance, which will officially be named similarly as, “California Infrastructure and Economic Development Bank Lease Revenue Bonds (California State Teachers' Retirement System Headquarters Expansion) Series 2022 (Green Bonds – Climate Bond Certified) (the “Series 2022 Bonds”), will require approval by the California Infrastructure and Economic Development Bank (IBank or the issuer) board.

The IBank is a public instrumentality of the State of California organized and existing pursuant to the Bergeson-Peace Infrastructure and Economic Development Bank Act. IBank has broad authority to issue tax-exempt and taxable revenue bonds, provide financing to public agencies, provide credit enhancements, acquire, or lease facilities, and leverage state and federal funds.

The Series 2022 Bond issuance is facilitated through the amendment of the lease-leaseback arrangement executed upon issuance of the Series 2019 Bonds. Under that arrangement, CalSTRS leased the HQE project site to the IBank and contemporaneously, the IBank leased the HQE project site (land) and the HQE project (building) back to CalSTRS. The proceeds from the bonds issued by the IBank were received by the bond Trustee, The Bank of New York Mellon Trust Company, N.A. through a Trust Agreement. The proceeds of the Series 2019 Bonds have been used, upon requisition by CalSTRS, for the construction of the HQE project, payment of financing costs and interest on the bonds during the capitalized interest period.

Likewise, the Series 2022 Bonds proceeds will be placed in trust with the bond Trustee and utilized to pay for the costs necessary to complete the HQE project upon the exhaustion of the proceeds from the Series 2019 Bonds and based on current assumptions approximately \$2 million in excess interest earnings from the Series 2019 Bonds.

The terms of the amended leases and the Series 2022 Bonds will be aligned with the terms of the Series 2019 Bonds and will not exceed 30 years from the date of issuance of the Series 2019 Bonds. Principal will amortize annually to produce level annual debt service payments, commencing on August 1, 2023 (see *Deposit of Debt Service Payments* section below). CalSTRS will have the ongoing option to prepay the balance of the lease/outstanding bonds without penalty beginning August 2029 (the same call date as the Series 2019 Bonds). Staff will provide the board with recommendations as we near the redemption period and thereafter until the bonds are paid in full.

Another important consideration is whether to use a competitive or negotiated method to sale the Series 2022 Bonds.

- Competitive Sale – The bonds are advertised for sale and any broker dealer or dealer bank may bid on the bonds at the designated date and time. The bonds are awarded to the bidder offering the lowest true interest cost in compliance with the terms of the Notice of Sale. The bidder sells the bonds to investors.
- Negotiated Sale – An underwriter is selected to purchase the bonds. The underwriter, in turn, sells the bonds to its investor customers. The terms of the sale are negotiated by the issuer and the bond purchaser.

Each of these methods has its advantages and disadvantages. Since the State Treasurer’s Office is our agent for sale, the STO will determine the method of sale, in consultation with CalSTRS and the rest of the financing team. Note: CalSTRS used negotiated sale for the Series 2019 Bonds.

Based on current assumptions, we estimate that approximately \$2 million will be available from the excess interest earnings on the Series 2019 Bonds to offset the \$18.5 million needed to complete the project. Therefore, the par amount of the bonds is estimated to be around \$17 million, including \$0.5 million for costs of issuance. The bonds are anticipated to sell at a premium. If that occurs, the premium amount would be used to offset some or all of the financing costs.

Although staff anticipates the overall issuance to be less than the additional funding requested, since the foregoing amounts are preliminary estimates and are subject to change based on modified assumptions and market conditions at the time of the bond sale, staff is asking the board to approve a not to exceed par amount of \$19 million. This includes the \$18.5 million approved for additional funding and \$0.5 million for costs of issuance. This will allow staff the flexibility needed at the time of sale. The table on the next page summarizes the current estimated bond sizing based on current assumptions, as well as the maximum bond sizing reflected in the Bond Resolution.

	Current Estimated Sizing of the Bonds*	Sizing of the Bonds for the Bond Resolution
Credit Ratings	S&P: A+; Fitch: AA	
Interest Rates	As of Oct 14, 2022	As of Oct 14, 2022, plus 0.75%
Par Amount	\$16,135,000	\$18,310,000
Original Issue Premium	<u>824,260</u>	<u>663,589</u>
Total Bond Proceeds	16,959,260	18,973,589
Rounded	<i>N/A</i>	19,000,000
Project Fund	16,500,000	18,500,000
Capitalized Interest	0	0
Financing Costs	<u>459,260</u>	<u>473,589</u>
Total Bond Uses	\$16,959,260	\$18,973,589
True Interest Cost	4.58%	5.20%
Rounded	<i>N/A</i>	5.25%
Annual Debt Service	\$1,081,000	\$1,290,500
Rounded	<i>N/A</i>	\$1,300,000
Total Debt Service	\$29,192,236	\$34,842,939

* Preliminary, subject to change.

Deposit of Debt Service Payments

Pursuant to the abatement provisions of the Facility Lease (described below), CalSTRS’ legal obligation to pay rent under the Facility Lease, with respect to the HQE project (which in turn would be used to pay debt service on the Series 2019 Bonds and Series 2022 Bonds) does not arise until substantial completion of the HQE project. To address this, in connection with the issuance of the Series 2019 Bonds, capitalized interest was funded in an amount sufficient to pay semi-annual interest payments on the Series 2019 Bonds through and including February 1, 2023 (at the time of issuance of the Series 2019 Bonds, this amount was considered to be sufficient because it provided seven months “cushion” against delays in the then-projected July 2022 completion date and then assuming the HQE project was completed prior to February 1, 2023, semi-annual principal and interest payments (“rent”) would commence beginning on August 1, 2023.) Since the HQE project will not be substantially completed on February 1, 2023, CalSTRS’ obligation to pay rent will not arise as of the February 1, 2023 interest payment date, and the Trustee will not have sufficient funds on deposit to make the August 1, 2023 payment of debt service due on the Series 2019 Bonds (and the Series 2022 Bonds). In order to address this shortfall, facilitate the successful sale of the Series 2022 Bonds, and provide assurances to Bondholders that the August 1, 2023 debt service payments on the Series 2019 Bonds and the Series 2022 Bonds will be made as scheduled (regardless of substantial completion of the HQE project), staff recommends that CalSTRS deposit with the bond Trustee at the time of issuance of the Series 2022 Bonds, from legally available funds, an amount equal to debt service that will be

payable on the Series 2019 Bonds and Series 2022 Bonds on August 1, 2023, in an amount not to exceed \$13 million (\$12 million due for the Series 2019 Bonds and \$1 million due for the Series 2022 Bonds). This deposit with the bond Trustee is projected to earn approximately 4.3% until August 1, 2023, costing roughly \$195 thousand compared to the assumed earnings rate of 7% if the funds remained in the investment portfolio.

Tentative Timeline

Provided below is a summary of the anticipated timeline for the bond financing.

Week of	Financing Activity*
Oct-31	Board authorizes bonds (Nov-02)
Nov-7	Rating agency meetings
Nov-14	IBank board authorizes issuance of bonds (Nov-16)/Method of sale finalized
Nov-21	Credit ratings received
Nov-28	Preliminary Official Statement (POS) posted for sale
Dec-5	Sale of the bonds
Dec-12	Official Statement posted; Bond documents finalized
Dec-19	Bond closing; Delivery of bond proceeds to Trustee

* Preliminary, subject to change.

Green Bonds

CalSTRS vision includes advancing sustainability practices that promote long-term value creation and stewardship of our natural resources. Our guiding beliefs also support sustainability programs that build environmental, social and governance principles into our core business and investment practices. With our vision and guiding beliefs in mind, the HQE project is being designed to support green building practices, including green technologies, sustainable construction, energy conservation and whole-building integrated energy efficiency measures as well as employee wellness goals.

The Series 2019 Bonds were designated as “Climate Bond Certified” by the Climate Bonds Initiative (CBI). CBI is an independent not-for-profit organization that works solely on mobilizing the bond market for climate change solutions. Green Bonds identify to investors that the bond proceeds will be used specifically for sustainable projects that will have a positive impact on the environment.

CalSTRS will seek the Climate Bond Certified designation for the Series 2022 Bonds and anticipates certification prior to the issuance of the bonds.

Principal Bond Documents – Definitions

The bond issuance is executed through various legal documents that are defined as follows:

First Amendment to Facility Lease

The amended Facility Lease sets forth the terms under which IBank will lease the HQE project, and the real property on which the HQE project will be located, back to CalSTRS. This agreement contains provisions relating to the lease term, payment or abatement of rent, maintenance, insurance, defaults, and remedies. The First Amendment to Facility Lease sets forth the increased lease payments necessary to support payment of debt service on the Series 2022 Bonds. The document will be executed by IBank and CalSTRS.

First Supplement to Trust Agreement

The First Supplement to the Trust Agreement sets forth the terms of the Series 2022 Bonds, the application of the proceeds thereof, the nature and extent of security for the Series 2022 Bonds, the rights of the bondholders and the responsibilities and duties of the Trustee. The agreement will be executed by the IBank and the Trustee, The Bank of New York Mellon Trust Company, N.A. Note: The CalSTRS financing team will have the opportunity to review and approve the trust agreement before it's completed.

Bond Purchase Agreement

For a negotiated sale, where a bond underwriter is selected prior to the sale of the Series 2022 Bonds, the Bond Purchase Agreement sets forth the terms of the bond sale and will be executed by CalSTRS, IBank, the California State Treasurer, as agent for sale for the Series 2022 Bonds, and the representative for the selected underwriter. The agreement specifies the Series 2022 Bonds' closing date, purchase price, interest rates, maturity dates, principal amounts, and redemption provisions. It also contains the parties' rights and representations, and the conditions precedent for the representative for the underwriters to purchase the Series 2022 Bonds.

Notice of Sale

For a competitive sale, where the underwriter is selected through a competitive process on the day the Series 2022 Bonds will be sold, a Notice of Sale is distributed to potential investors with the Preliminary Official Statement. The Notice of Sale describes the terms on which the IBank and CalSTRS are willing to sell the Series 2022 Bonds and solicits competitive bids from financial institutions to purchase the Series 2022 Bonds.

Preliminary Official Statement/Official Statement

The Official Statement (OS) provides information to prospective investors and bondholders about CalSTRS and the Series 2022 Bonds. The OS typically includes information regarding the purposes of the bond issue, how the Series 2022 Bonds will be repaid and the financial and economic characteristics of the conduit borrower (CalSTRS). Investors and market intermediaries use this information to evaluate the credit quality of the securities and potential risks of the bond offering. The offering and sale of the Series 2022 Bonds through the OS is

subject to certain provisions of state and federal securities laws. The Preliminary Official Statement (POS) is a preliminary version of the OS prepared for potential investors prior to the sale of the Series 2022 Bonds.

Continuing Disclosure Certificate

The Continuing Disclosure Certificate contains the required obligations of CalSTRS and the Trustee to provide ongoing disclosure in the form of annual reports and event notices for the life of the Series 2022 Bonds. This certification will be executed and delivered by CalSTRS.

Strategic Plan Linkage: Goal 3: Sustainable organization-*Fully integrate a unified environmental, social and governance ethos in all we do*: Objective C. Complete headquarters expansion and transition activities.

Board Policy Linkage: Pursuant to [Appendix I of the Teachers' Retirement Board Governance Manual](#), the board may delegate authority to the Chief Executive Officer to perform any act within the power of the Board itself to perform.
