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August 26, 2013

Brian Fahnstock, Chair
Oversight Board Members
c/o Brian Bosse, Waterfront Business Manager
123A Harbor Way
Santa Barbara, California 93109

Re: Use of Remaining Bond Proceed

Dear Mr. Fahnstock and Board Members:

The City of Santa Barbara (the "City") serving as Successor Agency (the Successor Agency") to the former Santa Barbara Redevelopment Agency (the "RDA") has asked us to review and advise the Successor Agency regarding the permissible expenditure of remaining bond proceeds ("Remaining Bond Proceeds") derived from certain tax allocation bonds (the "Bonds") issued by the RDA on or before December 31, 2010, and to communicate our conclusions to the members of the Santa Barbara Successor Agency Oversight Board (the "Oversight Board"). As a preliminary matter, Orrick has been the City's bond counsel and advisor on public finance matters for many years, including with respect to the bond issues discussed herein. In that regard, our experience in public finance is quite substantial. For example, in 2012 Orrick was bond counsel to issuers in the State of California on 146 bond issues totaling approximately \$20.3 billion in principal amount and representing a 49.1% market share as bond counsel for issuers in the State.

The Bonds giving rise to the Remaining Bond Proceeds are the RDA's Central City Redevelopment Project Tax Allocation Bonds, Series 2001A (the "Series 2001 Bonds") and the RDA's Central City Redevelopment Project Tax Allocation Bonds, Series 2003A (the "Series 2003 Bonds"). Specifically, we have been asked whether Remaining Bond Proceeds can be spent on several proposed projects "in a manner consistent with the original bond covenants," within the meaning of Health and Safety Code Section 34191.4(c)(2)(A). In that regard, we understand that the Oversight Board asserts that if the projects were not specifically identified in the Official Statements through which the Bonds were sold, remaining Bond Proceeds cannot be expended on the projects in a manner consistent with the original bond



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covenants. I also understand that the Oversight Board has not raised any other legal issues which might restrict the expenditure of Remaining Bond Proceeds on these projects.

As a general matter, official statements are disclosure documents and do not themselves create binding contractual covenants. For example, if an official statement incorrectly described a financial covenant contained in an indenture pursuant to which bonds were issued, the indenture covenant would control, not the official statement; though there might well be a securities laws question for the issuer of such bonds. The covenants in indentures pursuant to which tax allocation bonds are issued do not typically include provisions specifically limiting the use of bond proceeds to specific projects. Rather, it was often the case that uses were described as capital projects in accordance with the redevelopment plan for a project area. For example, the Third Supplemental Indenture of Trust authorizing the 2001 financing creates the Redevelopment Account for the Series 2001 Bonds and provides that “[s]uch moneys transferred to the Agency shall be used by the Agency to pay for costs of the Redevelopment Project in accordance with the Law.” The term “Redevelopment Project” is defined in the preambles to the Third Supplemental Indenture of Trust and simply equates the term with the Redevelopment Plan for the Central City Redevelopment Project. Accordingly, there is no original bond covenant limiting the expenditure of Remaining Bond Proceeds to specific projects. The same indenture language is used in connection with the issuance of the Series 2003 Bonds and the language for both series of Bonds is attached.

The principal reason that financial covenants for tax allocation bond financings typically provide so much flexibility is that the security for the bonds is tax increment generated by the project area, not the projects to be financed themselves. In fact, usually the projects are some sort of public improvement which would not generate any new property tax dollars. The larger picture and financial assumption, of course, is that blight removal in general increases property values in general in a given project area. Official statements for tax allocation bond issues may include more or less information regarding proposed redevelopment project expenditures. And such information may or may not be considered important as it is understood that specific projects may change, and furthermore that blight removal may or may not increase property values in a given project area. What is always material to a bondholder is the amount of increment generated, presently, historically and as projected, and the potential for future growth in assessed value through infill. Other material factors would include the size and diversity of the project area and the concentration of ownership.

The language in the indenture sections creating the redevelopment project accounts stating that bond proceeds are to be used “to pay for costs of the Redevelopment Project in accordance with



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the Law” simply means that the proposed projects are generically identified in the redevelopment plan as well as the relevant implementation plan and are otherwise financed in compliance with the relevant redevelopment law. For example, Health and Safety Code Section 33445, 33445.1 and 33679 apply to these projects, and require certain findings be made in connection with publicly owned facilities.

Health and Safety Code Section 34191.4(c) mandates a specific order and use of Remaining Bond Proceeds following receipt of a finding of completion by the Department of Finance. In general, Remaining Bond Proceeds must be used for the purpose for which the Bonds were sold. Indeed, to do otherwise would likely violate bond covenants. Only if Remaining Bond Proceeds “cannot be expended in a manner consistent with the bond covenants..., the [Remaining Bond Proceeds] shall be used to defease the bonds or to purchase those same outstanding bonds on the open market for cancellation.” In this regard, representatives of the Successor Agency have indicated their opinion that tax increment could have been used to finance both of the proposed projects, as they are identified in the Redevelopment Plan and are otherwise costs of the Redevelopment Project which the Successor Agency can pay in accordance with the law.

Very truly yours,

William W. Bothwell

cc: Mark S. Manion, Esq.
Sarah Knecht, Assistant City Attorney

Provisions of the Third and Fourth Supplements to Indenture of Trust

Section 14.05 of the Third Supplement to Indenture of Trust authorizing the Redevelopment Agency of the City of Santa Barbara Central City Redevelopment Project Tax Allocation Bonds, Series 2003A reads as follows (underscore added):

Section 14.05. Redevelopment Project Fund (Series 2001 A). The Trustee shall establish and maintain a separate fund designated the “Redevelopment Project Fund (Series 2001 A).” On the date of issuance of the Series 2001 A Bonds, there shall be deposited in the Redevelopment Project Fund (Series 2001 A) the amount specified in Section 14.07(b) hereof. The moneys in the Redevelopment Project Fund (Series 2001A) shall be withdrawn by the Trustee and transferred to the Agency from time to time upon submission of a Written Request of the Agency requesting such transfer. Such moneys transferred to the Agency shall be used by the Agency to pay for costs of the Redevelopment Project in accordance with the Law. The provisions of Section 6.07 hereof shall be applicable to the investment of moneys in the Redevelopment Project fund (Series 2001 A); provided, however, that all interest or gain derived from the investment of amounts in the Redevelopment Project Fund (Series 2001 A) shall be retained therein.

Section 15.05 of the Fourth Supplement to Indenture of Trust authorizing the Redevelopment Agency of the City of Santa Barbara Central City Redevelopment Project Tax Allocation Bonds, Series 2003A reads as follows (underscore added):

Section 15.05. Redevelopment Project Fund (Series 2003A). The Trustee shall establish and maintain a separate fund designated the “Redevelopment Project Fund (Series 2003A).” On the date of issuance of the Series 2003A Bonds, there shall be deposited in the Redevelopment Project Fund (Series 2003A) the amount specified in Section 15.08(c) hereof. The moneys in the Redevelopment Project Fund (Series 2003A) shall be withdrawn by the Trustee and transferred to the Agency from time to time upon submission of a Written Request of the Agency requesting such transfer. Each such Written Request of the Agency shall be sufficient evidence to the Trustee of the facts stated therein and the Trustee shall have no duty to confirm the accuracy of such facts. Such moneys transferred to the Agency shall be used by the Agency to pay for costs of the Redevelopment Project in accordance with the Law. The provisions of Section 6.07 hereof shall be applicable to the investment of moneys in the Redevelopment Project Fund (Series 2003A); provided, however, that all interest or gain derived from the investment of amounts in the Redevelopment Project Fund (Series 2003A) shall be retained therein.

Both the Third and Fourth Supplements to Indenture of Trust define Redevelopment Project in the preambles in the same manner:

WHEREAS, a redevelopment plan for the Central City Redevelopment Project in the City of Santa Barbara (the “Redevelopment Project”) has been adopted in compliance with all requirements of the Law;