Capital Markets Finance Newsletter

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Welcome to CMF New Addition!

John Nguyen, the new Senior Finance Officer in Capital Markets Finance. He graduated from UC Berkeley, where he actively participated in the campus community as a Cal Student Orientation counselor, Resident Assistant and tutor at the Student Learning Center.

NEW AND NOTEWORTHY

Private Use Module
The Private Use Training and Tutorial is now available for use. Please submit user requests to Timothy Loving at timothy.loving@ucop.edu. Each user will have a unique username and password.

Permitted Use of Excess Bond Proceeds

At times, campuses are confronted with unspent excess bond proceeds when an externally financed capital project is nearing/at completion. This may occur for several reasons: timing of project expenditures and unexpected cost savings. Excess bond proceeds may be defined as proceeds no longer needed to pay for more capital costs towards a project. The question then arises as to what may be the legally permitted uses of these excess proceeds that were not expected when the bonds were first issued.

Tax law specifies that tax exempt bond proceeds should generally be spent on capital costs (either acquisition or construction). Any cost that is not a capital cost is a working capital cost. Tax rules limit what type of working capital may be paid with bond proceeds to only those identified here. In fact, taxable Build America Bonds (BABs) limit expenditures to only capital costs, and are not eligible for these exceptions, except for capitalized interest. So, the permitted uses for tax exempt bonds are: (a) costs of issuance, (b) fees for qualified guarantees of the issue (such as insurance premiums, letter of credit fees), (c) interest on the issue for a period commencing on the issue date and ending on the date that is the later of three years from the issue date or one year after the date on which the project is placed in service. This is the 'capitalized interest' rule, (d) rebate payments to the IRS, (e) a very small amount of working capital expenses directly related to the project being financed (e.g., initial operating expenses for a new capital project), and (f) debt service on that issue if there are unexpected excess proceeds.

Issuers of taxable Build America Bonds (BABs) must comply with the same requirements as tax-exempt bonds and certain additional requirements: (a) all excess available project proceeds are used only for capital expenditures, such as costs incurred to acquire, construct, or improve buildings, equipment, and land; (b) in addition to new money capital expenditures, all excess proceeds may be also used to reimburse prior capital expenditures incurred after February 17, 2009; (c) additionally, any interest earnings on the investment of BAB proceeds may be used only for capital expenditures; and, (d) finally, BAB proceeds may not be used for operating expenses or other "working capital" costs.

To sum up, tax exempt bond proceeds should be used primarily for capital expenditures related to the construction, acquisition and renovation of capital facilities, equipment and land. Tax law is specific and provides limited permitted uses if there are excess bond proceeds from tax exempt bonds and taxable Build America Bonds.

Rating Update

The University of California *General Revenue Bond* ratings were affirmed in August by the three major credit agencies that rate the University. They include the following:

Rating Agency	Rating	Outlook
Moody's	Aa1	Stable
S & P	AA	Stable
Fitch	AA+	Stable

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"Character is what emerges from all the little things you were too busy to do yesterday, but did anyway."

~Mignon McLaughlin

Commercial Paper Program Update

Despite Money Market Fund Assets Outflows

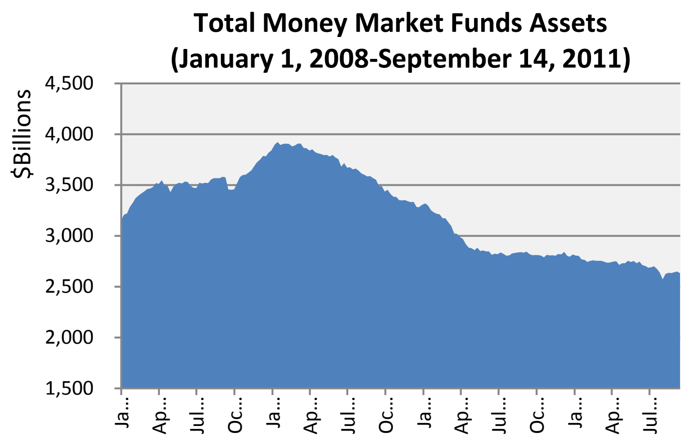
Since the beginning of 2011, U.S. money market funds have lost over $172.8 billion dollars in assets. While fund outflows have slowed over the past few months, the current money market fund level of $2.633 trillion dollars is substantially less than the $3.923 trillion that was held in money market funds in January 2009.

The drastic decline in money market fund assets is reflective of extremely low interest rates which have driven retail, price-sensitive investors out of the municipal bond market. On Monday September 12th, the benchmark 10-year Municipal Market Data (MMD) yield dropped to 2.07% -- an all-time low, while the 30-year MMD yield dropped to 3.66%, the lowest yield in 30 years.

Money market funds are pertinent because they are the largest investors of the University's Commercial Paper Program. In adherence to SEC Rule 2a-7, money market funds invest in the highest-rated, most liquid debt maturing in less than 397 calendar days.

Despite money market fund outflows, the University continues to borrow at attractive rates for its commercial paper program. Recent commercial paper has been sold at rates competitive with prior levels going back to 2008 when the University expanded its program.

The University's borrowing rates have remained attractive because of its strong underlying credit quality. It possesses the highest short-term ratings available: "A-1+" from Standard and Poor's and "P-1" from Moody's Investor Service. The recent downgrade of the United States caused some concern amongst commercial paper dealers; however the demand for the University's commercial paper has remained strong given the University's outstanding credit and liquidity positions.



UC Attains Significant Cashflow Savings

Tax-exempt and Taxable Fixed Income Rates at Historic Lows

The University of California successfully issued General Revenue Bonds ("GRB") Series AB (tax-exempt) & AC (taxable) on September 9th, funding several new money capital projects, capturing savings through a fixed rate refunding, converting internal loans to long term debt, and restructuring certain May 15, 2011 principal and interest payments. All campuses, including the Office of the President, participated in the transaction through one or a combination of the components.

Market conditions proved to be extremely favorable for the University's previous transaction, GRB Series Y Z AA, which helped fund a portion of the University's fiscal year 2011-12 pension annually required contribution and helped bridge a portion of the state's delayed appropriation. Continuing market volatility resulted in providing additional low financing costs for the University's most recent Series AB & AC. Significant savings will be realized for GRB Series 2005C, 2005D, 2005G, 2005H and MPP Series Q as a result of the favorable municipal fixed income market rates. The University was able to generate $17.2 million in cashflow savings through fiscal year 2027-28, or $15.2 million in present value savings. If your campus has projects in the bonds mentioned you can look for project specific savings in the Debt Information System within the next few weeks!

Highlights to the recent financings in addition to the savings from the refunding include the complete defeasance of all bonds outstanding on the Multiple Purpose Projects ("MPP") credit. A portion of MPP Series Q was cash defeased and the remainder refunded under the GRB credit.

The University's credit portfolio is now narrowed to General Revenue Bonds, Limited Project Revenue Bonds, Medical Center Pooled Revenue Bonds, and Hospital Revenue Bonds (HRB), are also being phased out. Additionally, the University has exhausted the whole alphabet in naming our GRB bonds and has restarted at series AA (with the most recent issue at AC). Please look to our public official statements to review the alphabet with your toddlers!