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Investors Hire Counsel to Challenge $1 Billion University Bond.

- **Holders are represented by Kramer Levin in the challenge**
- **University of California sold refunding debt earlier in March**

A group of investors has hired law firm Kramer Levin to challenge a $1 billion refunding deal by the Regents of the University of California, according to a letter seen by Bloomberg and people familiar with the situation.
The letter, dated March 20, was sent by Amy Caton, a partner at Kramer Levin, to the University of California officials disputing the Build America Bond refinancing transaction. The firm said it was representing investors that hold or manage "hundreds of millions of dollars" of the debt that is being refunded by the new issue sale.

At the crux of the debate is whether the taxable debt can be replaced by lower-cost tax-exempt bonds under a call provision that may be invoked in the occurrence of an extraordinary event.

The letter did not name the investors that the firm is representing. It was sent to Nathan Brostrom, chief financial officer for the University of California, and Charles Robinson, the school's general counsel.

"Our group asks the Regents to reconsider their proposed course of action, and avoid litigation, by either canceling the proposed redemption, or by moving forward with a redemption that is legally appropriate by paying holders the make-whole premium to which any current redemption entitles them," Kramer Levin's letter said.

Representatives for the University of California did not respond to a request for comment, sent after the close of business hours on Wednesday.

Under a make-whole call, an issuer provides a lump sum payment to investors, so the buyers avoid facing losses on an earlier call, according to the Municipal Securities Rulemaking Board. That scenario would cost the university at least $120 million more than the extraordinary redemption, Kramer Levin's letter said.

The challenge is rare in the municipal-bond market, and escalates a simmering feud between investors and issuers over a call mechanism in Build America Bonds. The securities were sold through a debt-issuing program instituted to spur economic growth by infrastructure spending after the Great Recession.

A number of Build America Bonds refinancing deals are already underway, spurred by the recent outperformance in the tax-exempt debt market — which has pushed those yields well below those on taxable securities. At least two investors have pushed back against a planned sale by the state of Washington scheduled for next week.

Extraordinary Redemption

States and municipalities are seeking to call the bonds back under what's known as an extraordinary redemption provision because of the federal government's cut to the subsidies paid to municipalities that sold BABs. Through the program, the federal government was supposed to cover 35% of the interest paid to investors. That subsidy had been slightly reduced through sequestration.

Nearly all of the $100 billion in outstanding Build America Bonds include an extraordinary call provision.

The letter sent by Kramer Levin states that the change in subsidy hasn't been material. On the Series R bonds being refunded, the reduction amounts to an estimated $872,000 a year, a small fraction of the regents' budget, the law firm said.

The letter called for the University of California's regents to scrap the transaction or for holders to be paid the make-whole redemption amount. The deal is expected to close on March 27.

"Should the Regents fail to cancel the redemption or pay the make-whole redemption amount, the holders we represent reserve their right to pursue an action for breach of contract, breach of the implied duty of good faith and fair dealing, and unjust enrichment, at a minimum," the letter said.

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