



City of Rialto

Legislation Text

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For City Council Meeting [November 14, 2017]

TO: Honorable Mayor and City Council

APPROVAL: Michael Story, City Administrator

FROM: Misty Cheng, Contract Financial Officer

Request City Council Adopt **Resolution No. 7219** Approving Financing Contracts related to the Solar CREB Lease Financing, in the amount of \$6,854,652.88, with Holman Capital and Mega Bank and the Service Contract with Alliance Building Solutions, Inc., supplementing Resolution No. 7122 adopted on May 9, 2017 and Adopt **Budget Resolution No. 7220**.

(ACTION)

BACKGROUND:

California Government Code Section 4217 authorizes California municipalities to repair and replace aging and dilapidated equipment by entering into energy contracts on terms that are found to be "in the best interests" of the agency "notwithstanding any other provision of law." In essence, this law allows a city to single source an energy contract so long as the energy cost savings to be derived from those services exceed the anticipated cost for the energy project. Energy Service Companies (ESCO's) that pursue single source contracts with local government agencies commonly cite Government Code Section 4217. On May 9, 2017, the City adopted Resolution No. 7122 and approved a contract with Alliance Building Systems, Inc. (Alliance) for the installation of certain solar equipment on City facilities, among other equipment (the "Installation Agreement"), and authorized the City to execute agreements with Holman Capital Corporation and other parties related to the financings. Certain circumstances have changed since the May 9, 2017 approval and Staff desires to bring the item back to the Council for a supplemental approval of the documentation. On October 24, 2017, the City Council reviewed the revised transaction and asked for more information.

ANALYSIS/DISCUSSION:

The May 9, 2017 City Council action contemplated two separate financings: (1) a Clean Renewable Energy Bond financing for the \$6,854,653 solar improvements at 2.1% over 20 years and, (2) a tax exempt capital lease structure for the \$2,455,000 energy efficiency improvements at 3.6% over 15 years. This report only addresses the terms of the Clean Renewable Energy Bond (CREB) financing.

The City's lease obligation with respect to the Solar Project is part of a financing known as a Clean Renewable Energy Bond, which allows for a lower interest rate as the buyer of the obligation can obtain federal tax credits. The limitations of the financing, certain software items, the software maintenance contract, and the equipment maintenance contract, which lasts 10 years, cannot be financed through the CREB. Therefore, Alliance will finance these excluded items under its service contract, with the City's obligation to pay for the items over a period of 5 years with no interest charge in equal annual payments. The total amount of the Solar Project does not change. However, the

CREB financing has been reduced to a lower amount.

Solar Project Financing	\$6,104,652.88
Alliance Service Contract	<u>\$750,000.00</u>
Total	\$6,854,652.88

The CREB financing structure was originally presented as a sinking fund to the City staff by Holman Capital. The debt service payments made by the City on a semi-annual basis would have been sent to a bank located in Arizona. Furthermore, the payments made by the City would not have reduced our outstanding loan balance until the end of the life of the loan financing (20 years). In addition, the escrow deposit account holding the funds to be paid to Alliance for progress payments for work performed would also have been held at the same out of state bank in Arizona. To comply with the State of California's government code, Holman has since changed the escrow deposit institution to Mega Bank located in San Gabriel, CA. Mega Bank is also a party to the Assignment Agreement instead of the Arizona Bank, and thus, is essentially the Bank providing the funds for the lease financings. In addition, there is no longer a sinking fund structure, but rather a traditional amortized loan structure whereby each debt service payment will be reducing the outstanding loan balance. As a result, the contemplated interest rate on the financing be around 3.43% (as of October 11, 2017), but the interest rate may change subject to the 4.5% maximum.

The new amortized loan structure saves the City an estimated \$3.8 million over the life of the combined energy efficiency and solar projects. For the first 3 years of the projects, the City will see a reduction in energy costs and by the year 4, there will be no energy costs incurred by the City as a result of these projects, only the debt service payment for the loans. At the end of 20 years, the loan will be paid off and the savings will be realized in the last five years of useful life. The annual expected savings from the finance contract and the service contract are shown on Exhibit A. These items reflect an overall savings over 25 years and an annual break even, except for the first few years.

In addition to the changes mentioned above, there was some concern regarding whether Holman Capital needed to be registered with the California Department of Business Oversight and to have their company registered with the California Secretary of State. With respect to registering the company with the Secretary of State, Holman Capital has done so and the City is resolved with that issue. With respect to the registration with the California Department of Business Oversight, Holman Capital is a public finance firm that originates and assigns loans over to partner banks, who ultimately loan out the proceeds. As such, both the legal counsel of Holman Capital and the City Attorney concur that Holman Capital does not need to register with the agency.

The controlling document for the financing is a Master Lease Agreement (Lease Agreement), whereby the lessee (City of Rialto) is responsible for lease payments and all costs of operation, maintenance, and insurance for the financed facilities. The City will make the payments by annual appropriations from the General Fund, but where appropriate, the City may make payments from other funds, whereby assets held receive benefit from the improvements, i.e. the Rialto Utility Authority fund will fund lease payments for improvements at Water and Wastewater facilities. The pertinent documents being approved are all attached to the staff report.

Resolution No. 7122 granted certain Designated Officers the authority to negotiate and approve the various Transaction Documents (as defined), including the financing documents - provided the terms remain consistent with the original approval. The final financing documents attached hereto contain certain provisions that the City Attorney and staff have determined the Council approve.

Recently, the House of Representatives introduced the Tax Cut and Jobs Act, which is now a bill pending in the House. The provisions of the bill would affect the City's transaction in the following ways if a law with similar provisions were to be enacted:

1. The bill eliminates the ability to do tax credit bonds like this CREB for the solar financing as of December 31. Therefore, if the City does not close the transaction by the end of the year, it would lose the ability to do a CREB.
2. The bill would cut the corporate tax rate to 20%. Under the City's energy efficiency financing, which was completed in May, a change like this would cause the interest rate on that financing to increase to provide the equivalent return on the transaction to the investor. There is a maximum of 4% interest rate permitted under the transaction. Such an increase could cause a difference in the savings analysis for the 15 years the energy efficiency financing is outstanding and hence affect overall savings on both the energy efficiency financing and the solar financing.

ENVIRONMENTAL IMPACT:

The requested action is not a "Project" as defined by the California Environmental Quality Act (CEQA). Pursuant to Section 15378(a), a "Project" means the whole of an action, which has a potential for resulting in either a direct physical change in the environment, or a reasonably foreseeable indirect physical change in the environment. According to Section 15378(b), a Project does not include: (5) Organizational or administrative activities of governments that will not result in direct or indirect physical changes in the environment.

GENERAL PLAN CONSISTENCY:

Approval of this action complies with the City of Rialto General Plan Goals and Policies:

Goal 2-30: Incorporate green building and other sustainable building practices into development projects.

Policy 2.30.1: Explore and adopt the use of green building standards and Leadership in Energy and Environmental Design (LEED) or similar in both private and public projects.

Policy 2-30.2: Promote sustainable building practices that go beyond the requirements of Title 24 of the California Administrative Code, and encourage energy-efficient design elements, as appropriate.

Policy 2-30.3: Support sustainable building practices that integrate building materials and methods that promote environmental quality, economic vitality, and social benefit through the design, construction, and operation of the built environment.

Goal 3-11: Provide community facilities that adequately support established programs, can accommodate future needs, and are accessible to all members of the community.

Policy 3-11.1: Allocate resources for the maintenance and operations of City facilities; explore alternative funding options for maintenance and operational costs of new facilities.

LEGAL REVIEW:

The City Attorney has reviewed and approved the staff report, Contracts with ABS and Resolutions.

FINANCIAL IMPACT:

The solar improvements will be financed by the lease and the service contract: Solar Project Financing, Service Contract \$6,854,652.88. The City Treasurer has reviewed and concurred with compliance with the applicable California Government Code as to keeping the monies on deposit in the State of California.

The payments will be made by annual appropriations from the General Fund, and all other funds, whereby assets held receive benefit from the improvements, i.e. the Rialto Utility Authority fund will fund lease payments for improvements at Water and Wastewater facilities.

The use of proceeds for the Solar project financing has been described as follows by the vendor (some of which are included in the Service Contract and some in the Lease Agreement):

Description	Cost
Solar System	\$ 5,576,846.00
Building VUE	\$ 494,569.00
Total Project Cost	\$ 6,071,415.00
(+) HCC Cost of Issuance	\$ 68,164.88
Cost of Issuance Received	\$ (30,000.00)
Solar Project Financing - CREB	\$ 6,109,579.88
ABS Operations and Maintenance	
EM Software	\$ 369,534.00
Monitoring PV Assist	\$ 219,943.00
Engineering and Commissioning	\$ 23,986.00
Labor	\$ 50,000.00
Labor & Overhead PV Assist	\$ 81,610.00
ABS Financing	\$ 745,073.00
Total	\$ 6,854,652.88

*This proposal is subject to final credit approval by the Credit/Investment Committee of Holman Capital Corporation's sole discretion. To render a credit decision, Lessee shall provide HCC with necessary underwriting information.

The cost of financing proposal is as follows:

Financing Amount	Interest Rate	Term	Payments	Total Payments
\$6,109,579.88	3.43%	20 Years	Semi-Annual	\$8,909,471

Annual Budget Preparation - As illustrated in the table below, the lease payments will end in 20 years for the Solar project and 5 years (equal payments each year) for the service contract. The cash flows reflect near breakeven annually until the lease payments are completed. In year 21, the City will begin to truly benefit from the costs savings. It is important to note no significant savings will result from this project until the lease payments are completed in year 21. It is also important to note the estimate of program savings are subject to change based on usage, utility rate structures, and the effectiveness of the improvements being made. However, the lease payments are fixed obligations that must be appropriated annually. **RISK - If the savings do not exceed the cost of the lease payments the City's total costs will increase, conversely, if the savings exceed expectations then the City will realize greater than expected cumulative savings.**

The City has prepaid \$30,000 of the costs of issuance and this amount is not included in the financing. It is reflected in the table below as a payment by the City in Year 1 of the transaction, in addition to the required lease payment.

The combined cost of capital for the CREB's financing and the Alliance loan is 3.32%. The net present value of the investment at a 5% discount rate is approximately \$1.2 million over a 25 year assumed project term. As noted above, most of the present value savings derive from the later years of the project and those years are the most difficult to predict with any certainty.

	Solar Project				Combined Energy			
	CREB		Debt Repayment		Solar		Solar	
Years	Savings	Lease	Pay	Mean	Debt	Cash	Cash	Flow
0	0	0	0	0	0	0	0	0
1	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
2	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
3	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
4	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
5	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
6	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
7	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
8	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
9	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
10	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
11	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
12	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
13	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
14	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
15	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
16	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
17	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
18	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
19	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
20	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
21	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
22	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
23	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
24	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
25	224,400	6,109,579	109,748	073	854,653	1,061,061	1,061,061	1,061,061
Total	5,677,999	152,950	2,950	938	76,388	1,231	1,231	1,231
NPV at 5%	3.43%	0.00%	3.32%	1,183,993				

Notes:

1. Includes \$30,000 advance for issuance costs

Staff recommends City Council increase estimated revenues in Capital Projects Fund Account No. 300-400-7302-7721-170006-01 in the amount of \$6,109,579.88 for loan proceeds and increase estimated revenues in Building Maintenance Fund Account No. 770-400-7302-9010 in the amount of \$750,000 for the ABS service contract. Staff also recommends increasing appropriations in Capital Projects Fund Account No. 300-500-7302-3001-170006-07 in the amount of \$6,109,579.88 for the capital project costs, and increasing appropriations in Building Maintenance Fund Account No. 770-500-7302-4001 and 770-500-7302-4010 in the amounts of \$150,858.70 and \$209,551.30, respectively, for principal and interest payments for FY 18.

Staff recommends council un-designate fund balance from General Fund Account No. Reserve for Contingencies 010-310-0710-0000 in the amount of \$750,000 and increase appropriations in General Fund Account No. 010-500-0001-5060.

RECOMMENDATION:

Staff recommends the City Council:

1. Adopt the Resolution approving the financing Contracts related to the Solar CREB Lease

Financing with Holman Capital and Mega Bank and the service contract with Alliance Building Solutions, Inc.; and

2. Adopt the Budget Resolution.