



REPORT TO CITY COUNCIL

Approved by:

Aurds Rodriguez

Department Director

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City Manager

Council Meeting of: December 4, 2019

Agenda Number: E-1

SUBJECT:

Seek City Council Direction Regarding Term and Amortization to Secure Funding for Energy Improvements (e.g. ENGIE Project)

RECOMMENDATION:

Staff recommends a 20-year level debt service amortization with either the California Bank and Trust option or the Bank of America option. The decision very much depends on whether the City can tolerate the final five maturities resetting in interest rate every five years.

SUMMARY:

Staff and the City's financing team secured term sheet proposals from lenders interested in financing the various energy improvements. Each lender was asked to provide 15 and 20-year escalating and level debt service options. The City received responses from seven (7) different lenders. The purpose of this staff report is to discuss the results of the responses and receive direction from the City Council (Council) as to the term and structure of the amortization.

DISCUSSION:

On August 21, 2019, the Council approved a Resolution appointing Del Rio Advisors, LLC as Municipal Advisor. On September 18, 2019, the City Council approved a Resolution appointing Jones Hall as Bond Counsel and Brandis Tallman LLC as Placement Agent.

On October 24, 2019, the Placement Agent circulated a term sheet to 25 different lenders known to finance energy improvements as an equipment lease. An equipment lease means that only the assets placed in service are the subject of the lease. The City is not required to lease an essential asset as required for a standard lease revenue bond.

Table 1 summarizes the results of the qualifying term sheet responses. A much more detailed description of all the responses is included as Attachment 1 of this report.

Table 1: Comparison of Term Sheet Responses (Level and Escalating Debt Service Options)						
<i>Lender</i>	<i>Term</i>	<i>Structure</i>	<i>Interest Rate</i>	<i>Principal Amount</i> ⁽²⁾	<i>Total Net Interest</i> ⁽³⁾	<i>Net Energy Savings</i> ⁽⁴⁾
Cal Bank and Trust	15yr	Level DS	2.51%	\$19,693,000	\$3,908,346	\$31,554,375
Cal Bank and Trust	15yr	Escalating DS	2.55%	\$19,701,000	\$4,170,908	\$31,283,813
Cal Bank and Trust	20yr	Level DS	2.36% ⁽⁵⁾	\$19,667,000	\$4,830,093	\$30,658,627
Cal Bank and Trust	20yr	Escalating DS	2.34% ⁽⁶⁾	\$19,665,000	\$5,261,904	\$30,228,819
Bank of America	20yr	Level DS	2.77%	\$19,743,000	\$5,921,152	\$29,491,568
Bank of America	20yr	Escalating DS	2.79%	\$19,747,000	\$6,576,421	\$28,832,300

(1) *DS: Debt Service*
 (2) *Assumes funding \$19,123,000 of energy improvements, one year of capitalized interest and costs of issuance*
 (3) *Net of one year of capitalized interest while the improvements are installed*
 (4) *Assumes cash flows provided by ENGIE showing energy savings over a 30-year period*
 (5) *First 15 years are at a fixed 2.52% and the final 5 years are variable at 2.05% and resets every five years*
 (6) *First 15 years are at a fixed 2.56% and the final 5 years are variable at 2.05% and resets every five years*

Worth noting is that in the staff report to the Council on November 6, 2019, staff noted various assumptions. At that meeting, based on the current financial market conditions, the following assumptions were made for the purposes of calculating estimated savings from the proposed energy saving improvements:

Table 2: Financing Assumptions from Nov. 6, 2019 Council meeting	
A. Finance term	20 years
B. Annual interest rate on the loan	2.85%
C. Annual escalation of electricity cost	4.3%
D. Annual escalation of operating and maintenance cost	3%

FINANCING OVERVIEW

The following provides an overview of the proposals from both lenders, plus a third summary that is non-callable.

1. Cal Bank and Trust Proposal

15-year Option

If the City chooses either of the 15-year options, the most attractive offer came from California Bank and Trust. The following is a summary of this option:

- The interest rate is locked for 60-days which should cover the period through closing.
- The loan is callable in whole or in part on any date with no prepayment penalty.
- The bank would require the City to keep the project funds with the bank and they would disburse the funds as escrow agent.
- They do not require fees for either bank counsel or a lender representative.

20-year Option

Cal Bank and Trust also presented a 20-year option that has a fixed rate of 2.52% on the level debt service option and 2.56% of the escalating debt service option. Under both scenarios, the first 15 maturities would be at the respective fixed interest rate, but the last 5 maturities would be at a variable interest rate that resets every five years. A few items worth highlighting:

- Currently the variable rate on the final 5 maturities would be set for the first five years at 2.05%.
- While this would be the lowest 20-year option in terms of interest cost, the City would need to decide if it can tolerate the variable rate risk on approximately 30-40% of the loan as the rate resets every five years.
- The interest rate is locked for 60-days which should cover the period through closing.
- The loan is callable in whole or in part on any date with no prepayment penalty.
- The bank would require the City to keep the project funds with the bank and they would disburse the funds as escrow agent.
- They do not require fees for either bank counsel or a lender representative.

One thing to consider on this option is that the loan is callable in whole or in part on any date with no prepayment penalty. Should the opportunity arise at some future date or should the variable rate increase significantly, the option to refund the obligation will always be available

2. Bank of America Proposal

If the City wishes to choose either of the 20-year options and desires that the interest rates remain fixed for the entire term, the most attractive offer came from Bank of America. Some highlights:

- The interest rate is locked through December 31, 2019.
- The loan would be callable on any payment date in whole only at 102%.
- This would not allow the City to prepay portions of the loan over time.
- They do not require fees for either bank counsel or a lender representative.

3. Municipal Finance Corporation Proposal (Non-Callable Option)

One last proposal to note was received from Municipal Finance Corporation. They would have the lowest fixed rate interest rates for the entire term on both the 15-year (2.39% and 2.42%) and 20-year (2.60% and 2.66%) options but the loans would be non-callable. The concern regarding non-callable is the loans would not have the ability to be restructured or refinanced at some future date. This is particularly true given that the estimated energy savings are just that, an estimate, and the flexibility to restructure the obligation could be important if the savings do not materialize as planned.

ESTIMATED ENERGY SAVINGS

From Table 1 above, the level debt service option, whether a 15 or 20-year term, a few items to note:

- Either option clearly provides the most net energy savings as compared to its' escalating counterpart.
- It is also important to analyze the cash flow based on the estimated energy savings versus the proposed annual debt service on the lease obligation.

The estimated energy savings were provided by Engie for 30 years, but for purposes of this report, the focus is simply the 15 to 20-year time horizon of any proposed loan. Table 3 shows the net annual energy savings on a cash flow basis for each scenario:

Table 3: Estimated Net Annual Energy Savings/(Cost)

FY	Cal Bank and Trust 15yr Level	Cal Bank and Trust 15yr Escalating	Cal Bank and Trust 20yr Level	Cal Bank and Trust 20yr Escalating	Bank of America 20yr Level	Bank of America 20yr Escalating
2021	(247,147)	(251,188)	(233,542)	(232,130)	(273,440)	(275,470)
2022	(197,426)	(229,950)	194,194	275,170	134,159	210,049
2023	(263,662)	(219,049)	127,667	263,223	68,195	200,165
2024	(208,171)	(228,562)	182,642	273,595	123,816	208,660
2025	(506,063)	(182,053)	(115,002)	217,732	(174,086)	165,610
2026	(459,319)	(188,746)	(68,259)	226,489	(127,491)	171,854
2027	(368,636)	(203,625)	22,175	243,186	(37,092)	185,301
2028	(317,175)	(210,736)	74,126	252,741	14,938	192,878
2029	(263,828)	(219,482)	126,701	262,889	67,707	200,287
2030	(208,492)	(227,655)	182,005	272,801	123,324	207,720
2031	(151,056)	(237,044)	240,121	283,649	180,885	216,359
2032	(91,412)	(246,424)	300,148	295,596	240,503	225,386
2033	(29,443)	(256,565)	362,201	306,833	302,297	234,017
2034	34,969	(266,233)	426,398	318,569	367,372	243,470
2035	102,932	(277,178)	493,849	331,991	433,854	252,969
2036	1,840,376	1,840,376	562,903	344,815	503,871	262,753
2037	1,912,904	1,912,904	635,559	357,960	576,542	273,065
2038	1,988,293	1,988,293	711,569	372,803	652,002	283,170
2039	2,066,658	2,066,658	790,056	386,547	730,394	295,318
2040	2,148,115	2,148,115	871,159	402,403	811,861	306,782
Totals	\$6,782,417	\$6,511,856	\$5,886,670	\$5,456,862	\$4,719,611	\$4,060,343
		\$270,562		\$429,809		\$659,268
	Difference		Difference		Difference	
					\$1,167,060	
			Difference			

From the above estimate of energy savings:

- Staff would recommend either of the 20-year scenarios, leaning towards the level debt service option.
- While there are a few years of a net energy cost, the overall savings are between \$430,000 and \$660,000 over time.
- If the City can tolerate some portion of the loan being variable, the 20-year Cal Bank and Trust option could provide significantly more savings (currently estimated at \$1.17 million) as compared to the Bank of America 20-year option. However, actual savings are very dependent on where the interest rate would reset every five years

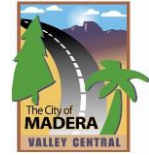
FINANCIAL IMPACT:

It is estimated that a portion of the proposed payments on the loan can be allocated to the City’s Water Enterprise Fund, a portion to the City’s Wastewater Enterprise Fund and the balance to the City’s General Fund.

ATTACHMENT:

1. Summary of Term Sheet Responses

**City of Madera
2019 Solar Lease Financing
Summary of Proposals Received
November 8, 2019**



	<u>Academy Bank [2]</u>	<u>BBVA Compass</u>	<u>Bank of America</u>	<u>Cal Bank & Trust</u>	<u>Municipal Finance Corp</u>	<u>Pinnacle Public Finance</u>	<u>Sterling National Bank</u>
Interest Rate:					<u>Callable</u>	<u>Non-Callable</u>	
15-Year Term, Level DS			2.569%	2.51%	2.67%	2.39%	2.800%
15-Year Term, Escalating DS			2.586%	2.55%	2.72%	2.42%	2.810%
20-Year Term, Level DS	3.57%	2.84%	2.770%	Variable, See Footnote [3]	2.92%	2.60%	2.935%
20-Year Term, Escalating DS		2.88%	2.790%	Variable, See Footnote [4]	2.96%	2.66%	2.940%
Rate Lock Terms:		Upon credit approval, rate is locked 60 days (subject to breakage fees)	Rate locked through December 31, 2019	Rate locked up to 60 days	Rate locked up to 60 days	Rate locked through December 8, 2019	Rate locked through December 18, 2019
Prepayment Terms:							
15-Year Term			Callable any payment date, in whole only, at 102%	Callable in whole or in part, anytime at par	Callable on any payment date commencing December 1, 2024 at par	Callable any payment date at 102%	Callable in whole but not in part on any payment date, year 4-6 at 102%, year 7-9 at 101%, year 10+ at 100%
20-Year Term	Callable anytime in whole or in part without penalty	Callable after the 10th anniversary at par, however earlier calls are available upon request, at a premium to the proposed interest rate	Callable any payment date, in whole only, at 102%	Callable in whole or in part, anytime at par	Callable on any payment date commencing December 1, 2026 at par	Callable any payment date at 102%	Callable in whole but not in part on any payment date, year 4-6 at 102%, year 7-9 at 101%, year 10+ at 100%
Costs: [1]							
Bank Counsel	\$10,000	\$17,500	\$0	\$0	\$10,000	\$0	\$0
Escrow Agent	\$0	\$0	\$0	\$1,500	\$0	\$750	\$0
Lender Rep.	\$0	\$0	\$0	\$0	\$5,000	\$0	\$0
Proposal Expiration:		November 22, 2019	November 22, 2019		November 13, 2019		November 15, 2019

[1] Additionally, bond counsel, municipal advisor, placement agent and miscellaneous fees may apply to all proposals.

[2] Academy Bank can only loan up to \$5,000,000 on this transaction.

[3] Maturities 12/1/2021 through 12/1/2034 will have a fixed rate of 2.52%. The maturities 12/1/2035 through 12/1/2039 will have an initial rate of 2.05%, and will reset every 5-years based on the 5-year Federal Home Loan Bank Des Moines Regular Fixed Advance Rate Index.

[4] Maturities 12/1/2021 through 12/1/2034 will have a fixed rate of 2.56%. The maturities 12/1/2035 through 12/1/2039 will have an initial rate of 2.05%, and will reset every 5-years based on the 5-year Federal Home Loan Bank Des Moines Regular Fixed Advance Rate Index.

The following banks declined to submit a proposal:

Banc of California	Capital One	First Internet Bank	Orix Bank	Westamerica Bank
BB&T Governmental Finance	CoBiz Public Finance	Flagstar Bank	Pacific Western Bank	Western Alliance Bank
Banner Bank	Five Star Bank	Key Bank	River City Bank	
BCI Capital Management	First Foundation	Opus Bank	Signature Bank	

Estimated Closing Date: December 18, 2019
Approximate Principal Amount: \$19.9 Million
Final Maturity: Dec. 1, 2034 or Dec. 1, 2039