AGENCY:	**City Council**
MEETING DATE:	**July 22, 2024**
DEPARTMENT:	**City Manager**
PRESENTED BY:	**I. Whippy/Consultants**
EMAIL ADDRESS:	**iwhippy@fortbragg.com**

AGENDA ITEM SUMMARY

TITLE:
Consider adoption of City Council Resolution No. ____ authorizing the execution and delivery of an Equipment Lease/Purchase Agreement and Escrow Agreement with Bank of America, National Association relating to the financing of energy efficiency projects to be undertaken pursuant to an agreement with Syserco Energy Solutions, Inc., and approving related documents and actions.

ISSUE:
On June 10, 2024, the City Council approved entering into an Energy Services Agreement with Syserco Energy Solutions, Inc. ("SES"), which authorized SES to proceed with solar photovoltaic ("PV") implementation at the following six City sites:

1. City Hall (416 North Franklin St.)
2. Corp Yard / Water Treatment Plant (31301 Cedar St.)
3. CV Starr Center (300 South Lincoln St.)
4. Fire Department (141 North Main St.)
5. Police Station (250 East Cypress St.)
6. Wastewater Treatment Plant (100 W Cypress St.)

In addition to the solar PV improvements at the six City sites above, the roof of the Police Station will be replaced before the solar panels are installed. The total cost of these projects is $7,501,224. The total project cost will be financed with proceeds from a tax-exempt municipal equipment lease.

There are two project incentives available from the federal government under the Inflation Reduction Act ("IRA") that can potentially reduce the net cost to the City. The first project incentive under the IRA is the "direct-pay" project incentive, valued at 25.5% of solar project costs, or approximately $1,811,389, which is available in the form of a refundable tax credit at the conclusion of the project (once permission to operate has been granted by PG&E). All eligible projects nationwide can receive this direct-pay incentive, without regard to volume cap limitations. The second, more competitive, project incentive is the low-income communities bonus credit incentive valued at 8.5% of solar project costs (or approximately $603,796). Unlike the direct-pay incentive, the low-income bonus incentive requires an application and has a volume cap limitation. More information on how these two project incentives will be used to reduce the overall cost to the City is included in the Discussion/Analysis section below.

DISCUSSION/ANALYSIS:

To assist with (1) reviewing the financial feasibility of the energy efficiency projects process and (2) executing a tax-exempt municipal equipment lease, City staff engaged NHA Advisors ("NHA"), a municipal advisor, in September 2023. NHA has worked with City staff to review the feasibility of the proposed projects and projected energy savings, manage the financing process, and assist in structuring the tax-exempt municipal equipment lease payments.

Due to the relatively small size of the tax-exempt municipal equipment lease and the equipment lease structure, NHA and City staff decided to utilize a private placement process (direct loan with a bank), rather than a public offering (bond issued to investors). The City therefore engaged Oppenheimer & Co. Inc. ("Oppenheimer") as the placement agent for the transaction. Oppenheimer has a 10+ year history with the City, having previously served as underwriter on the City's 2021 Lease Revenue Bonds and 2015 Tax Allocation Bonds, and as placement agent on the 2014 Water Revenue Refinancing. Oppenheimer contacted 12 banks in a formalized lender RFP process, requesting interest rates for a 20-year tax-exempt lease. Five banks responded to the lender RFP, with interest rates ranging from 4.46% to 5.59%.

The 4.46% interest rate, proposed by Bank of America, National Association ("BANA"), was the lowest bid, and the only bid under 4.50%. BANA's bid also offered a beneficial financing structure for the City, including no capitalized interest requirement and favorable terms for extraordinary prepayment from the IRA incentives. The City Manager signed BANA's term sheet on July 3, 2024, to lock in the terms of BANA's proposal, subject to City Council's final approval. Accordingly, City staff are now recommending that the City enter into a 2024 Equipment Lease/Purchase Agreement ("2024 Lease") with BANA.

The 2024 Lease will have a 20-year term, maturing August 1, 2044, with annual debt service payments escalating at approximately 5.3% to align with the escalation of projected energy savings. BANA has provided a fixed 4.46% interest rate for the 2024 Lease. This interest rate is locked through August 27, 2024, which removes the risk that interest rates rise before the 2024 Lease closes and funds on August 1, 2024. The City's first payment on the 2024 Lease is scheduled for August 1, 2026.

As noted above, there are two project incentives available from the federal government under the IRA that can potentially reduce the net cost to the City: the direct-pay incentive and the low-income communities bonus credit incentive, available in a combined estimated amount of $2,415,186. The direct-pay incentive is available to all eligible projects, while the low-income bonus incentive is subject to a nationwide competition, for which the City has applied. Instead of front loading the City's repayment and assuming the IRA incentives will be available to pay the large upfront payments, the plan is to prepay a portion of the 2024 Lease with the IRA incentives once one or both incentives become available to the City. Front loading the repayment of the 2024 Lease potentially exposes the City to an excessive debt service payment in the event one or both of the IRA incentives arrives late or does not arrive at all. BANA's proposal features an extraordinary optional prepayment provision that allows for partial prepayment of the 2024 Lease using the IRA incentives. There will be a 0.5% premium associated with an extraordinary optional prepayment.

Due to the competitiveness and uncertainty of the low-income bonus, the analysis below considers two prepayment scenarios. In Scenario #1, only the direct-pay IRA incentive, in the amount of $1,811,389, is available in time for partial prepayment on August 1, 2026. In Scenario #2, the direct-pay IRA incentive and the low-income bonus, in the aggregate amount of $2,415,186, is available in time for a partial prepayment on August 1, 2026; however, this may not be the case.

The 2024 Lease is estimated to have a par amount of $7,606,000, which will cover the solar PV and roof replacement costs ($7,501,224) and the financing costs relating to the 2024 Lease ($104,776).

Based upon the energy savings pro-forma prepared by SES, implementing the energy efficiency projects is estimated to generate energy savings of approximately $20.6 million for the City through 2055. Once the debt service cost of the 2024 Lease is factored in, as well as the costs associated with operation, maintenance, and management of the solar PV improvements, the net savings through 2055 is estimated to be approximately $10.4 million on a cumulative basis and $3.6 million on a present value basis under Scenario #1, and approximately $11.4 million on a cumulative basis and $4.2 million on a present value basis under Scenario #2.

Next Steps & Timeline:

For the City to enter into the 2024 Lease, City Council will need to approve the 2024 Lease documents and a related Escrow and Account Control Agreement (the "Escrow Agreement") and authorize City staff to sign the documents and take other necessary actions. Once City staff have City Council approval and authorization, they expect to finalize and sign the 2024 Lease documents and close the financing on or about August 7, 2024.

Discussion of Lease Documents:

- **Equipment Lease/Purchase Agreement:** The Equipment Lease/Purchase Agreement ("ELPA") outlines the terms governing the 2024 Lease. The ELPA also identifies the location of the energy improvements and that the security for the 2024 Lease is a lien on the equipment. This lien will be in place until the 2024 Lease matures in August 2044 or is otherwise prepaid in accordance with the 2024 Lease terms. The ELPA also contains the payment details, prepayment provisions, and other covenants of the City. As an appropriation lease, the City will, as part of the annual budget process, appropriate sufficient amounts each fiscal year to make payments on the ELPA and, if an appropriation is not made, the sole remedy is for the bank to re-possess the equipment that was financed.

- **Escrow and Account Control Agreement:** The Escrow Agreement is among BANA, the City, and Wilmington Trust, National Association, as escrow agent (the "Escrow Agent"). Under the Escrow Agreement, the proceeds of the 2024 Lease will be held by the Escrow Agent and disbursed to pay costs of the energy efficiency projects based on requisitions filed by the City with the Escrow Agent.

2024 Lease Financing Team:

As part of City Council Resolution No. ____, the Special Legal Counsel (Jones Hall), the Municipal Advisor (NHA Advisors), and the Placement Agent (Oppenheimer & Co. Inc.) will be formally engaged. Fees and expenses of the financing team members are payable from a portion of the proceeds of the 2024 Lease, not any other City funds. BANA does not charge any upfront fees. All participants of the 2024 Lease financing team are listed below.

- **Special Legal Counsel:** Jones Hall
- **Energy Solutions Company:** Syserco Energy Solutions
- **Escrow Agent:** Wilmington Trust
- **Lessee:** City of Fort Bragg
- **Lessor:** Bank of America, National Association
- **Lessor's Counsel:** Chapman and Cutler LLP
- **Municipal Advisor:** NHA Advisors
- **Placement Agent:** Oppenheimer & Co. Inc.

Good Faith Estimates:

NHA Advisors (the City's municipal advisor) and Oppenheimer (the City's placement agent) have provided good faith estimates on the cost of the 2024 Lease, as required by California Government Code Section 5852.1. All amounts and percentages are estimates and are made in good faith based on current information available.

1. True Interest Cost of the 2024 Lease: 4.434%.

2. Finance charge of the 2024 Lease, being the sum of all fees and charges paid to third parties in the amount of $104,776.

3. Amount of proceeds of the 2024 Lease expected to be received by the City, net of proceeds for Costs of Issuance in (2) above and net of capitalized interest (if any) and reserves (if any) paid or funded with the proceeds of the 2024 Lease: $7,501,224.

4. Total payment amount for the 2024 Lease, being the sum of (a) debt service to be paid to final maturity, plus (b) any financing costs not paid from proceeds of the 2024 Lease: $12,586,225.

RECOMMENDED ACTION:

Consider adoption of City Council Resolution No. ____ authorizing the execution and delivery of an Equipment Lease/Purchase Agreement and Escrow Agreement with Bank of America, National Association relating to the financing of energy efficiency projects to be undertaken pursuant to an agreement with Syserco Energy Solutions, Inc., and approving related documents and actions.

ALTERNATIVE ACTION(S):

An alternative action is to not proceed with adoption of City Council Resolution No. ____ authorizing the execution and delivery of an Equipment Lease/Purchase Agreement and Escrow Agreement. This alternative action means the City will need to find financing from another source, at potentially a higher interest rate or a less favorable financing structure.

FISCAL IMPACT:
The 2024 Lease has ascending debt service payments. Under Scenario #1, where partial prepayment of the 2024 Lease occurs on August 1, 2026 from the direct-pay IRA incentive, the City's debt service payments range from $331,000 in 2027 to $812,000 in 2042. Under Scenario #2, where partial prepayment of the 2024 Lease occurs on August 1, 2026 from both the direct-pay and low-income bonus IRA incentives, the City's debt service payments range from $305,000 in 2027 to $740,000 in 2041. The costs associated with issuing the 2024 Lease will be paid out of the proceeds of the 2024 Lease (no direct budgetary impact).

GREENHOUSE GAS EMISSIONS IMPACT:
The projects to be implemented by SES are estimated to reduce the City's greenhouse gas emissions by 882 metric tons of Carbon Dioxide per year. This is roughly equivalent to 210 gas-powered vehicles driven for one year or 971,558 pounds of coal burned.

CONSISTENCY:
N/A

ATTACHMENTS:
1. City Council Resolution No. ____
2. Equipment Lease/Purchase Agreement
3. Escrow and Account Control Agreement

NOTIFICATION:
N/A