RESOLUTION NO. 2015-97

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF MARINA ACCEPTING INFORMATION REGARDING LOAN OPTIONS TO CONSIDER FOR THE ACQUISITION OF PRESTON PARK AND PROVIDING FURTHER DIRECTION TO THE CITY MANAGER

WHEREAS, The City of Marina and the Fort Ord Reuse Authority (FORA) have executed a Settlement Agreement and a Purchase and Sale Agreement whereby the City would purchase Preston Park from FORA. Under the terms of the Agreements, the City will purchase FORA's one-half interest in Preston Park for a purchase price of $35 million dollars and escrow must close by no later than September 15, 2015; and

WHEREAS, following direction received by the City Council on March 3, 2015, City staff have been actively engaged in working with Berkeley Point Capital to secure a $35 million, 10-year fixed rate, interest only loan to be insured by Fannie Mae. This loan option was preferred by the City Council because the long-term interest only feature protects the revenue stream that the City is currently receiving from the property and provides the City with the most flexibility; and

WHEREAS, the underwriting process was progressing smoothly until Fannie Mae determined that repairs to the siding of Preston Park buildings, which FORA had intended to undertake in FY 2015/16 and FY 2016/17, would need to be undertaken immediately and completed prior to loan approval and closure. To address this issue, FORA agreed to amend the Settlement and Purchase and Sale Agreements to provide for a September 15, 2015 closing date; and

WHEREAS, the attached **("EXHIBIT A")** prepared by Keyser Marston and Fieldman Rolapp summarizes the key aspects of four of the five options that we are requesting the City Council to consider:

Option 1: 10-year fixed rate, interest only Fannie Mae loan;

Option 2: 10-year fixed rate loan with Rabobank with 2 years of interest only payments;

Option 3: 10-year fixed rate loan with Western Alliance with 5 years of interest only payments;

Option 4: 15-year variable rate loan with Western Alliance with 5 years of interest only payments

WHEREAS, Staff requests guidance regarding these loan options to fund the acquisition of Preston Park; and

NOW, THEREFORE BE IT RESOLVED, by the City Council of the City of Marina does hereby:

1. Adopt Resolution Nos. 2015-, accepting information regarding loan options to consider for the acquisition of Preston Park; and
2. Directs the City Manager to proceeds with Option(s) 1 and Option 4

PASSED AND ADOPTED, by the City Council of the City of Marina at a City Council meeting duly held on this 5th day of August, 2015 by the following vote:

AYES, COUNCIL MEMBERS: Amadeo, Brown, Morton, Delgado
NOES, COUNCIL MEMBERS: None
ABSTAIN, COUNCIL MEMBERS: None
ABSENT, COUNCIL MEMBERS: O'Connell

Bruce C. Delgado, Mayor

ATTEST:

Anita Sharp, Deputy City Clerk

EXHIBIT A

Acquisition Financing Options - Preston Park

	Option 1: Fannie Mae/BPC	Option 2: Rabobank –	Option 3: Western Alliance – Fixed Rate	Option 4: Western Alliance – Variable Rate
Loan term	10 years	10 years (amortized over 30 years)	10 years (amortized over 30 years)	15 years (amortized over 30 years)
Fixed or Variable	Fixed	Fixed	Fixed	Variable
Interest Rate	10-year treasury + margin Current est.: 2.26% +1.92 % = **4.18%**	10-year treas. + margin Current est.: 2.26%+2.25% =**4.51%**	1 month libor + margin Current Est. = **4.25%**	68% of 1-month libor + margin Current est.: .129%+ 3.75%. = **3.88%**
Interest Only or Amortizing	10 yrs - interest only	2 yrs – interest only and 8 yrs. Amortizing	5 yrs. Interest only and 5 yrs. Amortizing	5 yrs. interest only and 10 yrs. Amortizing
Estimated Loan Amount	$35,370,000	$35,370,000	$35,370,000	$35,370,000
Debt Service	Interest only = $1,478,000 P+ I = NA	Interest only = $1,593,000 P+ I = $2,225,000	Interest only = $1,503,000 P+I = $2,299,000	Interest only = $1,372,000 P+I = $2,212,000
Impact to Marina's Cash Flow (interest only pmts.)	Positive $265,000	Positive $151,000	Positive $241,000	Positive $372,000
Impact to Marina's Cash Flow (amortizing pmts.)	Not applicable	Negative $481,000	Negative $555,000	Negative $468,000
Impact to Marina's Cash Flow over 10 years	Positive $2.65 million	Negative $3.55 million	Negative $1.57 million	Negative $482,000
Principal reduction over 10 years	$0	$6.07 million	$4.43 million	$4.63 million
Financing Fees	0.5%; Est. 1% total or $370,000	0.5%; Est. 1% total or $370,000	.2% Est. 1.0% total or $370,000	.2% Est. 1.0% total or $370,000
Security	Non-recourse, loan secured solely by Preston Park	Full recourse to borrow. Effectively minimal as borrower is Preston Park (not the City).	Non-recourse, loan secured solely by Preston Park	Non-recourse, loan secured solely by Preston Park
Prepayment Penalty	Greater of 1% or 9.5 years of yield maintenance (YM declines if interest rates rise)	Similar to yield maintenance. Penalty will exist if interest rates decline. May not have any penalty or unlikely possibility of positive cash flow	100% during 1st 5 years	No penalty. Pre-payable at any time at 100% with 30 day notice

	Option 1: Fannie Mae/BPC	Option 2: Rabobank –	Option 3: Western Alliance – Fixed Rate	Option 4: Western Alliance – Variable Rate
Assumable Loan	Yes	No	No	No
Risk Factors	Moisture repairs and mold testing must be complete with favorable results prior to loan approval. Repairs are scheduled to be complete by Sept. 5th, which results in insufficient time to complete FNMAE underwriting to close by Sept. 15th. Lender indicates Sept. 30th closing would be achievable.	After 2 years, debt service would increase to $2.2 million per year, which would reduce the City's current cash flow by $481,000 per year	There may not be sufficient time to complete the bond documents to close by September 15th. Tax exempt status not yet approved. After 5th year, payments would increase to $2.3 million per year, which would reduce City's current cash flow by $555,000 per year. Will know by 8/7 if closing is conditioned on completion of moisture repairs. Requires City to sign commitment/exclusive negotiation agreement at some point prior to closing	There may not be sufficient time to complete the bond documents to close by Sept. 15th. Tax exempt status not yet approved. Variable Rate Loan subject to changes in 1-month libor. After 5th year, payments would increase to $2.2 million, which would reduce City's current cash flow by $468,000 per year Will know by 8/7 if closing is conditioned on completion of moisture repairs. Requires City to sign commitment/exclusive negotiation agreement at some point prior to closing
Positive Features	10 years of interest only payments, at an attractive fixed rate.	Option with highest degree of certainty. Moisture repairs are not a condition for closing.	5 years of interest only payments at a relatively attractive fixed rate.	Low initial interest only rate and can be paid off at 100% at any time in the future.

Prepared by: Keyser Marston Associates, Inc. and Fieldman, Rolapp & Associates, Inc.; 7/31/2015

EXHIBIT B

History of One-Month Libor
Federal Reserve Economic Data
Federal Reserve Bank of St. Louis

Frequency: Annual

observation_date	USD1MTD156N	
1986-01-01	6.91	6.91%
1987-01-01	7.00	7.00%
1988-01-01	7.81	7.81%
1989-01-01	9.27	9.27%
1990-01-01	8.25	8.25%
1991-01-01	5.93	5.93%
1992-01-01	3.74	3.74%
1993-01-01	3.19	3.19%
1994-01-01	4.47	4.47%
1995-01-01	5.97	5.97%
1996-01-01	5.45	5.45%
1997-01-01	5.67	5.67%
1998-01-01	5.57	5.57%
1999-01-01	5.25	5.25%
2000-01-01	6.41	6.41%
2001-01-01	3.88	3.88%
2002-01-01	1.77	1.77%
2003-01-01	1.21	1.21%
2004-01-01	1.50	1.50%
2005-01-01	3.39	3.39%
2006-01-01	5.10	5.10%
2007-01-01	5.25	5.25%
2008-01-01	2.68	2.68%
2009-01-01	0.33	0.33%
2010-01-01	0.27	0.27%
2011-01-01	0.23	0.23%
2012-01-01	0.24	0.24%
2013-01-01	0.19	0.19%
2014-01-01	0.16	0.16%
Avg., 1986 - 2014	4.04	4.04%
Avg. 1995 - 2014	3.03	3.03%
Avg. 2000 - 2014	2.17	2.17%
Avg. 2005 - 2014	1.78	1.78%
Avg. 2010 - 2014	0.22	0.22%

July 27, 2015 Item No: **11c**

Honorable Mayor and Members
of the Marina City Council

City Council Meeting
of August 5, 2015

CITY COUNCIL CONSIDER ADOPTING RESOLUTION NO. 2015-, ACCEPTING INFORMATION REGARDING LOAN OPTIONS TO CONSIDER FOR THE ACQUISITION OF PRESTON PARK AND PROVIDING FURTHER DIRECTION TO THE CITY MANAGER

REQUEST:
It is requested that the City Council consider:

1. Adopting Resolution Nos. 2015-, accepting information regarding loan options to consider for the acquisition of Preston Park; and
2. Provide further direction to the City Manager

BACKGROUND:
The City of Marina and the Fort Ord Reuse Authority (FORA) have executed a Settlement Agreement and a Purchase and Sale Agreement whereby the City would purchase Preston Park from FORA. Under the terms of the Agreements, the City will purchase FORA's one-half interest in Preston Park for a purchase price of $35 million dollars and escrow must close by no later than September 15, 2015[1].

Following direction received by the City Council on March 3, 2015, City staff have been actively engaged in working with Berkeley Point Capital to secure a $35 million, 10-year fixed rate, interest only loan to be insured by Fannie Mae. This loan option was preferred by the City Council because the long-term interest only feature protects the revenue stream that the City is currently receiving from the property and provides the City with the most flexibility.

The underwriting process was progressing smoothly until Fannie Mae determined that repairs to the siding of Preston Park buildings, which FORA had intended to undertake in FY 2015/16 and FY 2016/17, would need to be undertaken immediately and completed prior to loan approval and closure. To address this issue, FORA agreed to amend the Settlement and Purchase and Sale Agreements to provide for a September 15, 2015 closing date. On June 26, 2015, FORA executed an agreement with Hometech Remodeling Inc. to undertake the needed repairs. Work commenced during the last week of June 2015 and the repairs (including new stucco and paint) are scheduled to be complete by September 5, 2015.

Fannie Mae's requirement to complete the repairs within this abbreviated time period and obtain environmental test results demonstrating that mold is not present in any of the units significantly increased the level of uncertainty about being able to close a Fannie Mae loan by the September 15, 2015 deadline. To reduce the level of risk, City staff have expanded the search for financing options, including:

- obtaining a loan from Rabobank, which is the current lender on the property; and
- obtaining a loan funded by a private placement revenue bond.

1 Closure date was originally July 15, 2015, but was extended to September 15, 2015 as a result of Fannie Mae's requirement that repairs to the property be completed prior to the issuance of financing.

ANALYSIS:

The attached **("EXHIBIT A")** prepared by Keyser Marston and Fieldman Rolapp summarizes the key aspects of four of the four options that we are requesting the City Council to consider:

Option 1: 10-year fixed rate, interest only Fannie Mae loan;
Option 2: 10-year fixed rate loan with Rabobank with 2 years of interest only payments;
Option 3: 10-year fixed rate loan with Western Alliance with 5 years of interest only payments;
Option 4: 15-year variable rate loan with Western Alliance with 5 years of interest only payments

As shown in the chart, Option 1 is superior with respect to maximizing cash flow to the City. Over the 10-year loan term, the City would retain approximately $2.65 million more revenue from the property than it currently receives. In comparison, the other three loan alternatives will reduce the City's cash flow over the 10-year period because each of them converts from an interest-only loan to an amortizing loan during the 10-year period. When a loan is an amortizing loan, monthly payments include pay-down of the outstanding principal as well as the interest expense. However, the City[2] would enhance its net equity in the property through making payments on the outstanding loan principal. The benefits of reducing the outstanding principal of the loan would be realized if the City upon refinancing or selling the property.

Option 1 – Fannie Mae 10 year, fixed rate interest only loan

This option would generate approximately $265,000 of additional net cash flow per year, or $2.65 million over the 10-year term, assuming current expense and revenue amounts. The positive cash flow could be set aside in a reserve fund to pay down the principal at the end of the 10-year loan, or could be used to fund capital improvements at Preston Park, subsidize future Preston Park rent increases, or provide additional revenue to the General Fund. At the end of the 10-year loan, if interest rates have increased and money has not been set aside to pay down the loan principal, there is a possibility that the City would either have to divert a portion of the cash flow that it currently receives from the property to fund debt service on a new $35 million loan, or the City would need to sell the property.

While the stucco work and painting following the siding repairs are not anticipated to be complete until September 5, 2015, the environmental testing of all units is anticipated to be complete by August 7, 2015. Berkeley Point is cautiously optimistic that Fannie Mae will proceed with underwriting the loan upon receipt of the favorable environmental report. If this is acceptable to Fannie Mae, it may be possible to close the loan by September 15, 2015.

Option 2 – Rabobank 10-year fixed rate loan with 2-years of interest only payments

This loan option has the greatest certainty of closing since Rabobank is the current lender on the property and desires to loan the City $35 million to acquire FORA's interest. Completion of the siding repairs is not a condition for closing the Rabobank loan. Based on current interest rate levels, the interest rate would be approximately 4.51%, which is higher than any of the other loans being considered. As of today, the bank is only offering two years of interest only. During the two years of interest only, the City's cash flow would increase by approximately $151,000 per year. Once amortizing provisions apply, cash flow to the City would decline by approximately $481,000 per year. Rabobank is considering offering 5 years of interest only payments, but has not yet approved

2 For convenience purposes, this staff report references the City of Marina as being the future owner of Preston Park and the borrower. The future ownership structure has not yet been finalized, but it is contemplated that the nonprofit corporation "Preston Park Sustainable Community Nonprofit Corporation" will either lease the property from the City or own the property. The nonprofit will be the borrower.

making that offer and has indicated that the interest rate would be higher with a 5-year interest only option.

If the City were to go forward with the Rabobank loan but desired to refinance in the future, it is possible that the City could refinance without any financial penalty if the market interest rate at the time of refinance is higher than the loan's interest rate. While unlikely, if interest rates decline, the City would incur a prepayment penalty.

Option 3 – Western Alliance 10-year fixed rate loan with 5 years of interest only payments

Both Western Alliance loan options (Options 3 and 4) would be funded by Western Alliance's purchase of revenue bonds to be issued by the Marina Financing Authority, which issued the bonds for the Abrams B transaction. Repayment of the bonds would be secured solely by rental income from Preston Park. Based on current interest rates, the interest rate would be fixed at approximately 4.25% throughout the 10-year term. This rate is only slightly higher than the Fannie Mae option, but the interest-only period is limited to 5 years. During the first five years of interest only payments, the City's cash flow would increase by approximately $241,000 per year. During the 6th through the 10th years when amortizing provisions would apply, the City's cash flow would decrease by approximately $555,000 per year. There is a restriction on the prepayment of the bonds for the first 5 years. They could, however, be refunded at no cost after 5 years, when the amortization period commences.

Western Alliance would also be willing to provide a fixed rate loan in which the interest only term would be three years instead of five years. The interest rate for that loan based on current market conditions would approximate 4.12% per year, compared to 4.25% for the fixed rate loan with five years of interest only payments.

There are a number of uncertainties associated with the Western Alliance loan option. First, the preparation of bond documents has not yet commenced and it is not certain that the documents can be finalized and terms accepted by Western Alliance to permit a September 15th closing. Western Alliance has not yet determined if closing will be conditioned upon completing the repairs. It will make that determination after it visits the property next week. Additionally, the tax exempt status has not yet been approved by Western Alliance. If it is determined that the bonds are taxable, the interest rate would be higher than a tax exempt rate. And, Western Alliance has indicated that it wants the City to execute a commitment letter, which would prohibit the City from negotiating with any other lenders. The bank has indicated that it is willing to wait until after the August 18, 2015 City Council meeting to receive the commitment letter, by which time all of the open issues related to tax-exemption, type of legal documents required and whether completion of the moisture repairs will be a condition to closing the loan will be known. However, the need for a commitment letter could be a critical issue because the City needs to be certain that it can close on an acquisition loan by September 15th and needs to preserve flexibility in the event that it is not possible to finalize a loan with Western Alliance.

Option 4 – Western Alliance 15-year variable rate loan with 5 years of interest only payments

This loan option is similar to Option 3 except that the interest rate would be a variable rate, tied to the one-month libor rate. The one-month libor rate is currently 19 basis points, or .19%. Including the margin, the current rate for the Preston Park loan would approximate 3.88%, which is the lowest rate of the options being considered. At a rate of 3.88%, the loan would increase the City's annual cash flow by $372,000 per year. The rate would be revised monthly. The attached **("EXHIBIT B")** provides some historical data on the one-month libor rate. As shown, the current rate is at or near historic lows. Over the past five years, the average rate has been .22%. Over the past ten years, the rate has averaged 1.78%, over the past fifteen years, the rate has averaged 2.17% and over the past twenty years, the rate has averaged 3.03%. In 2007, the one-month libor averaged 5.25%. If the libor rate were to increase to the average of the past 10 years (1.78%), the Preston Park rate would be 4.96%, which would result in an interest-only payment of $1,755,000 per year, which slightly exceeds the City's current cash flow from the property. Obviously, the index would need to move significantly to reach 1.78% given its current level of 0.19%.

In addition to the current low interest rate, another benefit of this option is that there is no prepayment penalty throughout the term of the loan. Therefore, if the City desired, the loan could be refinanced or the property sold at the end of the interest-only period.

REQUEST

Staff requests guidance regarding these loan options to fund the acquisition of Preston Park. Based on the objectives expressed by City Council on March 3, 2015 and the assessment of each option as summarized on Exhibit A, staff would rank the options as follows:

1st choice: Option 1;
2nd choice: Option 4;
3rd choice: Option 3;
4th choice: Option 2.

Given the need to close on a loan by September 15, 2015 and the desirability but uncertainties associated with Options 1, 3, and 4, staff recommends that the City proceed with processing all of the options. The financial cost of proceeding with all four options will be mitigated by the following considerations:

1) The City has already funded Berkeley Point's and Rabobank's 3rd party costs for Options 1 and 2;
2) Future city staff/consultant expenses, such as establishing a legal parcel and finalizing flood insurance, will in many instances serve all 4 options;
3) For underwriting a document processing, Options 3 and 4 are effectively one option.

City staff estimates that the cost to prepare the documents for Options 3 and 4 will be approximately $75,000. While the City will need to advance funds for these services, the costs will be reimbursed through loan proceeds.

Staff anticipates returning to the Council on August 18, 2015 to request selection of a preferred loan option.

REVIEWED/CONCUR:

____

Layne P. Long
City Manager
City of Marina