



# Memorandum

**TO:** HONORABLE MAYOR  
AND CITY COUNCIL

**FROM:** John Stufflean

**SUBJECT:** SEE BELOW

**DATE:** 11-22-10

Approved

Date

12/1/10

**COUNCIL DISTRICT:** 3

**SUBJECT: AGREEMENT WITH THE NATIONAL DEVELOPMENT COUNCIL FOR  
FEDERAL NEW MARKETS TAX CREDIT FINANCING CONSULTING  
SERVICES**

## RECOMMENDATION

Authorize the City Manager to negotiate and execute an agreement with the National Development Council for New Markets Tax Credit consulting services with an initial term from December 15, 2010 through January 31, 2012, and an option to extend up to seven years for compliance and asset management services; for compensation to be contingent on closing of the transaction in an amount not to exceed \$177,500 for the initial term, and \$70,000 for services during the optional period.

## OUTCOME

Approval of this agreement would enable the City to retain consultant support for a complicated financing mechanism involving federal New Market Tax Credits (NMTC). The proceeds from the sale of NMTC would assist with the cost of the construction of the San José Environmental Innovation Center (EIC). Securing the construction funds promptly for the EIC would allow the City to take advantage of the favorable construction bidding environment. The EIC is a critical component of the City's Economic Development Strategy, advances the City's Green Vision goals, and positions the City to attract more federal and state funding and private sector investment. If successful, the experience gained from this transaction could facilitate development of other capital projects through NMTC financing.

## **BACKGROUND**

### **Environmental Innovation Center Construction Status**

In June 2010, the Administration informed the Transportation and Environment Committee of the status on the site development and programming options for the EIC. The Administration identified several funding opportunities to assist with the construction of the EIC. One of the options identified is to secure a grant from the U.S. Department of Commerce's Economic Development Administration (EDA) through the American Recovery Program. The City had submitted a proposal to the EDA in Fall 2009 for \$4 million, but the decision for award is still pending.

The construction bid documents for the EIC are complete; however, the City must secure additional construction funds in order to complete the second phase of the project. Funds identified to date include:

<b>Source of Funding</b>	<b>Amount</b>
Reserve for EIC (Adopted 2010-2011 Operating Budget—Fund 423)	\$6,635,000
ESD Funding for HHW Facility (Adopted 2010-2011 Operating Budget )	\$3,500,000
Pending EDA Funding Assistance	\$4,000,000
<b>Total Required for Base-Level EIC Construction</b>	<b>\$14,135,000</b>

The \$4 million could fund base construction and related soft-costs and/or add alternates identified in the construction bid documents, bringing the facility closer to achieving a Leadership in Energy and Environmental Design (LEED) Platinum certification. The proposed add alternates include:

- 40-foot monument tower with Solar Photovoltaic (PV) panels and wind turbines;
- freestanding canopy at the main entrance plaza with the facility name;
- rooftop and carport PV panel systems for energy production;
- painting the exposed interior structure (i.e. ceiling, columns) of the warehouse; and
- repaving Nipper Avenue.

The Administration must also identify approximately \$700,000 to fund the City's Master Agreement with Group 4 Architecture Research + Planning, Inc (Group 4). Group 4's services would assist the City through the bid and award process and construction administration for the EIC.

### **New Markets Tax Credit Program**

The NMTC program, administered by the U.S. Department of the Treasury (Treasury), was created by the Community Renewal Tax Relief Act of 2000 to promote economic development in distressed areas. The program increases the amount of investment capital available to businesses and economic development programs through federal income tax credits. Each year, credits from the Treasury's Community Development Financial Institutions (CDFI) Fund are competitively allocated for distribution to certain qualifying entities, known as Community Development Entities (CDEs). In turn, a CDE solicits private equity investments in exchange for

a federal income tax credit totaling 39% of the amount invested that the investor claims over seven years. The investments are then provided to a Qualified Active Low-Income Community Business (QALICB), a corporation or partnership that sponsors projects within the economically disadvantaged area it is located in. A city or other governmental agency project would not qualify as a QALICB to receive revenue from the sale of the tax credits. But it may be possible for a transaction to be structured so that this project would qualify for NMTC. A seven-year compliance period follows the closing wherein all investments in the project are frozen and cannot be redeemed.

The NMTC funding mechanism is more common in the East Coast and Midwest, but increasingly more West Coast entities are seeking NMTC to help close project development funding gaps. The San Francisco Bay Area government agencies which have utilized or are pursuing NMTC to fund capital projects include the cities of Berkeley, Richmond, and the County and City of San Francisco. The financing structures for these projects vary, and have involved private developers.

For example, the Oxford Plaza and David Brower Center in Berkeley—a \$75 million mixed-use development with affordable housing, ground floor retail, underground parking, and offices of non-profit environmental organizations—incorporated NMTC into the project's financing structure. Richmond's Community Redevelopment Agency sought \$7 million in NMTC to rehabilitate the Oil House in the historic Ford Richmond Plant completed in 2008.

More recently, in September 2009, the San Francisco Redevelopment Agency sought consultant services to assist with an application for their own NMTC allocation from the Treasury. If allotted the requested NMTC amount, San Francisco plans to distribute the funds across several projects, including a \$30-\$40 million phased clean tech, and research and development corridor at Hunters Point Shipyard.

The EIC project is located in a qualifying census tract for the NMTC program. Assuming a qualifying QALICB can be established, the EIC project, valued at approximately \$29 million, would be eligible for NMTC that if purchased by investors, could generate approximately \$4 million in net revenue. This is revenue that would be sufficient to fund outstanding soft costs, add alternates, any remaining items for the base bid construction, and/or future project phases. Further analysis by the consultant is necessary to determine if this financing mechanism would be feasible for the EIC project. If successful, the experience gained from this project could support future capital project opportunities by the City and Redevelopment Agency.

## **ANALYSIS**

### **Scope of Work**

The proposed consultant would assist the City in establishing a QALICB, obtain NMTC, and close a NMTC transaction for the EIC. Specifically, the consultant would:

- evaluate the feasibility of a NMTC financing structure and its benefits for the EIC;

- provide legal services for the structuring of a QALICB;
- secure NMTC from a CDE(s) with sufficient credits from a previous Treasury allocation cycle;
- market to and place credits with investors;
- negotiate CDE fees and terms as well as the investors' pricing;
- assist with the preparation, review, and execution of the NMTC financial structure; and
- coordinate documentation for all requisite transactions.

The City would have the option to extend the contract for seven additional years to secure compliance and asset management services, for a compensation not to exceed \$70,000 through the term of the agreement.

Since, a city or other governmental agency project would not qualify as a QALICB to receive revenue from the sale of the tax credits, the City must determine if a transaction could be structured so that a qualifying QALICB would receive the investment which in turn, would be used for the EIC project. The consultant would assist the City to determine if a QALICB could be established that complies with the federal Internal Revenue Code and NMTC regulations. The consultant would also assist with the preparation of documentation necessary to create this QALICB. Since the investment must be held by the QALICB, which is not the City, for a period of seven years, the consultant would advise the City as to how the City can best maintain its short and long-term interest in the EIC, and the programs and operations on-site. The consultant would also advise staff on how to mitigate potential risks, liabilities, and responsibilities associated with the proposed QALICB. The Administration would return to Council to seek approval of the final QALICB and NMTC financing structure prior to execution of the underlying transactions.

#### **Selection Process**

In October 2010, the Environmental Services Department (ESD) released a Request for Proposal (RFP) for a NMTC consultant to assist the City with the range of NMTC activities, as described in the Scope of Work above. The RFP was posted on ESD's Request for Proposals page and the City's Internet Bid Line. ESD received proposals from the following four qualified firms:

1. CBO Financial, Inc.
2. Equity Community Builders, LLC
3. National Development Council
4. United Fund Advisors, LLC

All firms have provided consulting services to government or public sector agencies. Three of the firms proposed to work with specialized outside legal counsel to assist with the formation of a QALICB and accomplish the scope of work described in the RFP.

The following table is a summary of the four firms' proposed not-to-exceed maximum compensation amounts.

<b>Firm Names</b>	<b>Consultant Fee</b>	<b>QALICB Attorney Fee</b>	<b>Agreement Not To Exceed Amount</b>
CBO Financial, Inc.	\$85,000	\$5,000	\$90,000
Equity Community Builders, LLC	\$175,000	\$125,000	\$300,000
National Development Council	\$97,500	\$80,000	\$177,500
United Fund Advisors, LLC	\$475,000	\$75,000	\$550,000

A panel comprised of three representatives from ESD and the Finance Department reviewed the proposals, with the exception of the fee structures which were scored separately. Each panel member independently rated each proposal and scored them using the following criteria: adequacy and responsiveness, NMTC project experience, past project performance, and project approach for the EIC project, including schedule and staffing. The review panel ranked the National Development Council (NDC) highest among the four proposals.

### **Selected Consultant**

Staff recommends awarding this agreement to NDC for best meeting the criteria described in the RFP's scope of work. NDC was established in 1969 and has offices in Los Angeles and Napa, California. Since its inception, NDC has been engaged in economic and community development with more than 100 communities across the country. NDC provides financial analysis skills, development expertise, access to public and private sector financing, and training to their clients. Clients include units of government, public agencies, and other non-profit organizations. They are a non-profit organization that solely represents the interests of public agencies and other non-profit organizations, and they do not represent private developers or interests. NDC will subcontract with the Los Angeles-based legal firm Bocarsly, Emden, Cowan, Esmail, & Arndt, LLP, to provide QALICB legal representation and services for structuring the NMTC financing.

NDC has been the recipient of five NMTC allocations and has successfully structured, underwritten, and closed more NMTC transactions than nearly any other CDE in the country. NDC has been awarded \$486 million in total NMTC allocation and closed \$444 million in qualified equity investments in 55 projects and 22 states. Their investments have helped create nearly 5,000 jobs.

Some of their NMTC-financed projects include: the David Brower Center and Ed Roberts Campus in Berkeley; a 245kW solar system in San Bernardino; a 100kW solar system in Napa; and several projects in Washington State, including hotel construction, acquisition of a passenger ferry and shore facilities, and rehabilitation of a mixed-use building.

### **EVALUATION AND FOLLOW-UP**

Prior to the completion of the NMTC transaction, it is projected that staff will present the final NMTC structure and related agreements for Council consideration in 2011.

### **PUBLIC OUTREACH/INTEREST**

- Criteria 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criteria 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- Criteria 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

This recommendation does not meet any of the criteria listed above. This memorandum will be posted on the City's Internet website for the December 14, 2010, Council agenda.

### **COORDINATION**

This memorandum has been coordinated with the Offices of Economic Development and the City Attorney, City Manager's Budget Office, and the Departments of Finance and Public Works.

### **COST SUMMARY/IMPLICATIONS**

The cost for the initial term of the agreement with the consultant will be \$177,500, and an additional \$70,000 for the optional seven-year compliance period. This compensation includes legal services to advise the consultant on the formation of a QALICB. Any payment pursuant to this recommendation would be contingent on a successful closing of the transaction. The funding for these services would be derived from the proceeds on the sale of the NMTC. The 2011 Council memo recommending the final NMTC structure will provide detailed analysis of closing costs and proceeds, including investor fees, CDE fees, accountant fees, taxes and audits.

The timeline to establish the financing structure is anticipated to be one year. The estimated cost for staff and non-personnel services expenses for ESD during this period is \$75,000. These costs will be absorbed in ESD's existing Personal and Non-Personal/Equipment funding in the Integrated Waste Management Fund and will not impact the current service delivery levels.

This project will be the City's first experience with NMTC financing. Due to the complexity of a NMTC transaction, the City must also retain assistance of outside legal counsel to conduct peer review. The cost for outside legal counsel however has not been determined. Additional workload assessment must also be performed to determine if it would be possible for the Office

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of the City Attorney to coordinate legal review for this project with its existing staffing. The source of funding for outside legal counsel, and commensurate supervision from the City Attorney's Office would be from AB939 and late fees in the Integrated Waste Management Fund. It is estimated that these costs be \$150,000 but this amount may change once the Administration has more information about the funding structure and the extent of legal review required. These costs may be reimbursable from NMTC closing proceeds.

**CEQA**

A CEQA Negative Declaration for the renovation of the EIC was adopted on December 1, 2009 (PP09-138).

/s/

JOHN STUFFLEBEAN

Director, Environmental Services

For questions please contact Jo Zientek, Deputy Director, Integrated Waste Management Division, at (408) 535-8557.