COUNCIL AGENDA: 10-21-03
ITEM: 3.6

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM Scott P. Johnson

SUBJECT: TRANSITION PLAN FOR THE THE HAYES MANSION

DATE: October 16, 2003

Approved Kay Winer

Date 10/17/03

Council District: City-Wide
SNI: NA

SUPPLEMENTAL REPORT

Reason for Supplemental

Since issuance of the staff report on October 9, 2003 relating to the transition plan for the Hayes Mansion, staff has been working with Comerica Bank on the terms and conditions of the proposed line of credit with the City. The negotiated proposed changes to the terms are outlined below.

The primary change in the terms is to break up the $7 million line of credit into two separate credit facilities. The first credit facility proposed is a $5 million revolving line of credit and the second credit facility proposed is a $2 million term note amortized fully (principal and interest) over a 48 month period. The purpose of the term note would be to fund the assumption of HRLP's Comerica line of credit and their Greater Bay Bank loan (per the proposed transition agreement). The remaining amount (approximately $150 thousand) would be available for operating cash flow needs of the Hayes Mansion. The $5 million revolving line of credit would be used to fund any Hayes Mansion operating cash flow needs and the City's Hayes debt service costs if operating profits are not sufficient.

Staff recommends Council authorize the City Manager to negotiate and execute the Line of Credit and the Term Loan with Comerica including the following changes in the terms:

- Credit Facility: Original term was for a $7,000,000 revolving line of credit. The revised terms propose two separate credit facilities. The first credit facility is proposed to be a $5 million revolving line of credit and the second credit facility proposed is a $2 million term note amortized fully (principal and interest) over a 48 month period.

Rate: No changes to the rates for the revolving line of credit. The rate on the term note would be the same floating rate. However the term loan's options on the fixed Libor rate would be limited to revolving terms of 90, 180 or 360 days.
Amortization/Repayment: The revolving line of credit would not require any principal payments until maturity. Principal payments made prior to maturity would be at the option of the City. The term note would have fixed monthly principal payments of $41,666.67 per month with interest added (at the rate terms noted above.)

Default provisions: Each credit facility would be cross defaulted (if there is a default on one credit facility, a default on the other would be automatic.)

Subordination: Payments made by City on the proposed Devcon loan would be subordinated to all payments made to the bank on the term loan.

Collateral: The Bank to retain its UCC filing on the fixed assets located at the Hayes Mansion until the term loan is paid in full.
City's Hayes Reserve: The proposed $5 million reserve would be limited to securing the line of credit facility. The reserve would not apply to the term loan.

- Covenant to keep Hayes open: This commitment would not apply to the line of credit facility assuming the Council approves the proposed $5 million reserve that would "collateralize" the line of credit facility. However, this requirement would be a condition on the term note credit facility since the only means of repayment to the loan is the net operating revenues of the Hayes Mansion (and any draws from the line of credit facility).

Projected Draws from Comerica revolving Line of Credit

It should be noted, per the related Council item agendized for October 21st on the Hayes RFP process, assuming Council approves the recommended management agreement with Dolce, that the cash flow needs (including the City's Hayes debt service) would require draws of approximately $1.2 million in the first year of the operating agreement period (based on Dolce's five year financial proforma projections.) The repayment of these draws could be repaid as early as year three (2006) (based on Dolce's five year financial proforma projections.)

Although the projected cash flow needs from the Comerica line of credit is significantly less that the line of credit amount recommended ($5 million), staff suggests that the City enter into the line of credit agreement at $5 million to provide a long-term approach of having a Hayes Mansion operating cash flow "cushion" available until such time that the City is able to accumulate sufficient Hayes operating reserves to mitigate financial risks due to economic uncertainties in the economy. Therefore, this line of credit will protect the City's General Fund and mitigate the City's risk of potential Hayes Mansion cash flow shortfalls that could potentially result in the City's General Fund subsidizing the Hayes operations or to pay the City's Hayes Mansion debt service costs.

City to Enter into Covenant that the Hayes Mansion will Remain Open During the Term of the Comerica Loan

In negotiating the terms of the line of credit with Comerica, it was necessary that the City agree to enter into an affirmative covenant that the Hayes Mansion will remain in operation for the term of the line of credit. Comerica had concerns given the repayment to the line of credit being strictly limited to the net operating revenues of the Hayes (net of the City's Hayes debt costs) and any draws the City made on the line of credit facility. If the City agrees to encumber a $5 million Hayes Mansion Special Reserve dedicated for the $5 million Comerica line of credit, it is not necessary to have this provision for the line of credit. However, since the repayment of the term loan of $2 million is restricted to the net revenues of the Hayes Mansion (and any draws on the line of credit), Comerica requires that the City agree to keep the Hayes in operation until the term loan is paid off.

COORDINATION

This memo has been prepared by the Finance Department in coordination with the City Manager's Office and the City Attorney's Office.

SCOTT P. JOHNSON
Director of Finance