COUNCIL AGENDA: 04/30/19
FILE: 19-282
ITEM: 7.1

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Julia H. Cooper
Lori Mitchell
Margaret McCahan

SUBJECT: SEE BELOW

DATE: April 17, 2019

Approved D. DSyL Date 4/18/19

SUBJECT: FIRST AMENDMENT TO THE REVOLVING CREDIT AGREEMENT AND 2018-2019 BUDGET ADJUSTMENTS

RECOMMENDATION

It is recommended that the City Council take the following actions:

(a) Adopt a resolution (the "First Amendment Approving Resolution") authorizing the City Manager, the Director of Finance, the Assistant Director of Finance or their authorized designees to negotiate, execute and deliver the First Amendment to the Revolving Credit Agreement with Barclays Bank PLC to increase the-sublimit for the line of credit facility thereunder from an aggregate principal amount not to exceed $20,000,000 to $30,000,000, increase the sublimit for the standby letter of credit facility thereunder from an aggregate principal amount not to exceed $35,000,000 to $65,000,000, increase the aggregate commitment to issue revolving loans and standby letters of credit from an aggregate principal amount not to exceed $50,000,000 to $80,000,000 outstanding at any one time, and increase certain fees payable by the City to Barclays Bank PLC in connection with the credit facilities under the revolving credit agreement to finance start-up cost of the City of San José's Community Energy Program, purchase power, and secure payments under power purchase agreements, and other costs associated and consistent with the Community Energy Implementation Plan, and to take other related actions in connection therewith.

(b) Adopt the following Fiscal Year 2018-2019 Appropriation Ordinance amendments in the San José Clean Energy Fund:

(1) Increase the Cost of Energy appropriation to the Community Energy Department in the amount of $23,000,000;

(2) Decrease the Debt Service – Principal – Revolver appropriation to the Finance Department in the amount of $20,000,000; and

(3) Decrease the Ending Fund Balance – Community Energy Rate Stabilization Reserve in the amount of $3,000,000.

OUTCOME

Approval of the First Amendment Approving Resolution will authorize the City Manager, the Director of Finance, the Assistant Director of Finance or their authorized designees to negotiate, execute and deliver the First Amendment (the "First Amendment") to the Revolving Credit Agreement ("Credit Agreement") by and between the City of San José (the "City") and Barclays Bank PLC (the "Bank"), and a promissory note (the "Note") evidencing the City's obligations thereunder. The Credit Agreement, as amended by the First Amendment, will provide for a credit facility (the "Credit Facility") consisting of a revolving line of credit facility (the "Revolving Line of Credit Facility") and a standby letter of credit facility (the "Standby Letter of Credit Facility"). Under the terms of the Credit Agreement, as amended by the First Amendment, the Bank will commit to (i) make loans on a revolving basis under the Revolving Line of Credit Facility to the City in the aggregate principal amount of not to exceed $30 million outstanding for a period commencing on the effective date of the First Amendment and ending on November 27, 2021, and (ii) issue standby letters of credit under the Standby Letter of Credit Facility for the account of the City in an aggregate principal amount not to exceed $65 million outstanding for a period commencing on the effective date of the First Amended Credit Agreement and ending on October 27, 2023, provided that the aggregate principal amount outstanding under the Revolving Line of Credit Facility and amounts available to be drawn under Standby Letter of Credit Facility shall not exceed $80,000,000 at any one time.

Additionally, approval of the Appropriation Ordinance Amendments will (i) increase the Cost of Energy appropriation for 2018-2019 to enable SJCE to pay for increased power supply cost associated with higher than forecasted load, higher than forecasted energy costs, and a potential increase in Resource Adequacy ("RA") costs and (ii) approve decreases in the Debt Service – Principal – Revolver appropriation and the Community Energy Rate Stabilization Reserve that will offset the higher energy costs and more closely align the budget with year-end projections.

BACKGROUND

On February 27, 2017, the City Council approved the San José Clean Energy Community Choice Aggregate Business Plan, which concluded that San Jose Clean Energy ("SJCE"), under a single-jurisdiction model, is financially viable and can yield a variety of benefits including cost savings, economic growth, greenhouse gas reductions, and enhanced program offerings.

On May 17, 2018, the Finance Department issued a request for proposals ("RFP") to qualified lenders and/or financial institutions seeking proposals to provide a credit facility supported solely by SJCE revenues to secure initial power contracts and to support longer term operations (i.e., working capital). The City received responses from three (3) banks: the Bank; JP Morgan and River City Bank. Only the Bank and JP Morgan provided proposals to the City for credit facilities and the flexibility to provide loans and issue letters of credit simultaneously for the account of the City, as requested in the RFP.

Based on the analyses and evaluations of the proposals by Finance staff and the City's municipal advisor, including financing costs and the City's preferred terms, City staff recommended that the Bank be selected to provide the Credit Facility as the most responsive and cost-effective credit facility provider.

On September 25, 2018, City Council adopted a resolution authorizing the City Manager, the Director of Finance, the Assistant Director of Finance or their authorized designees to negotiate, execute, and deliver a revolving credit agreement with the Bank providing for a commitment to issue revolving loans and standby letters of credit in an aggregate principal amount not to exceed $50,000,000 total outstanding to finance start-up costs of the SJCE Program, purchase power, and, in the case of standby letters of credit, secure payments under power purchase agreements and other costs associated and consistent with the Community Energy Implementation Plan, and to take other related actions in connection therewith.

Effective on November 27, 2018, the Bank and the City entered into the Credit Agreement. The Credit Agreement currently provides a credit facility in the form of a commitment by the Bank to issue revolving loans to the City under the Revolving Line of Credit Facility in an aggregate principal amount not to exceed $20,000,000 (the "Revolving Line of Credit Facility Sublimit") and standby letters of credit for the account of the City under the Standby Letter of Credit Facility in an aggregate principal amount not to exceed $35,000,000 (the "Standby Letter of Credit Facility Sublimit"), provided, however, that the aggregate principal amount outstanding under the Revolving Line of Credit Facility and the Standby Letter of Credit Facility shall not to exceed $50,000,000 at any one time (the "Aggregate Commitment"). The City's obligations under the Credit Agreement were secured solely by a pledge and lien on revenues of SJCE, including revenues deposited in an operating reserve account held by the City pursuant to the Credit Agreement, as described below.

Under the terms of the Credit Agreement, the City agreed, among other things, that, so long as the Bank has any commitment thereunder or any amount payable thereunder remains unpaid from and including: (a) August 31, 2019, to but excluding November 15, 2019, to maintain not less than $10,000,000 in an operating reserve account held by the City established pursuant to and identified under the Credit Agreement (the "Operating Reserve Account") at all times during such period; (b) November 15, 2019, to but excluding December 31, 2019, to maintain not less than $15,000,000 in the Operating Reserve Account at all times during such period; and (c) the December 31, 2019 and thereafter, to maintain at all times $20,000,000 in the Operating Reserve Account (collectively, the "Operating Reserve Requirement").

SJCE now desires to amend the Credit Agreement pursuant to the First Amendment to, among other items: (i) increase the Revolving Line of Credit Facility Sublimit from an aggregate principal amount not to exceed $20,000,000 to $30,000,000; (ii) increase the Standby Letter of Credit Facility Sublimit from an aggregate principal amount not to exceed $35,000,000 to $65,000,000; (iii) increase the Aggregate Commitment from an aggregate principal amount not to exceed $50,000,000 to $80,000,000 total outstanding at any one time; and (iv) increase certain fees payable by the City to the Bank under the Credit Agreement in connection with the credit facilities thereunder.

SJCE determined that the increases to the Revolving Line of Credit Facility Sublimit, the Standby Letter of Credit Facility Sublimit and the Aggregate Commitment are necessary as a result of several changes in the operations of SJCE that have occurred since the execution and delivery of the Credit Agreement. Such changes include increases in the Power Charge Indifference Adjustment ("PCIA"), volatility in the power supply market and possible disruptions in revenue related to the bankruptcy filings of Pacific Gas & Electric ("PG&E") in January 2019. In addition, as part of the operations of SJCE, the City entered into certain power purchase agreements with power providers and the City is required to make payments to such providers in exchange for electrical power for SJCE. The City anticipates entering into additional power purchase agreements in the future under which the City will be required to make payments to such providers in exchange for electrical power for SJCE and, in some instances, may also be required to secure the City's performance of its obligations thereunder. To the extent the City is required to secure its performance, the City anticipates causing the Bank to deliver Standby Letters of Credit to counterparties of the power purchase agreements. In February 2019, the City Council authorized SJCE to enter into medium-term power purchase agreements through 2022. Because such power purchase agreements are medium-term and have higher notional amounts, an increase in the Standby Letter of Credit Facility Sublimit may be necessary to increase the City's capacity to secure its obligations to counterparties under such power purchase agreements.

The 2018-2019 SJCE budget was approved by the City Council on June 19, 2018 as part of the 2018-2019 Adopted Budget. On November 6, 2018, City Council approved budget adjustments to align the budget with revised projections for 2018-2019.

ANALYSIS

First Amendment to the Revolving Credit Agreement with Barclays Bank PLC

Since the execution and delivery of the Credit Agreement on November 27, 2018, SJCE has encountered various factors that require the City to amend the Credit Agreement to increase the Revolving Line of Credit Facility Sublimit, the Standby Letter of Credit Facility Sublimit and the Aggregate Commitment, and to amend the 2018-2019 Operating Budget as described in this memorandum. Factors include: uncertainty related to PCIA and PG&E rate changes; increased power supply costs; an update in load data; and the City's desire to procure energy under

medium-term power purchase agreements with higher notional amounts requiring the City to secure its performance with standby letters of credit.

If approved, the First Amendment would primarily: (i) increase the Revolving Line of Credit Facility Sublimit from an aggregate principal amount not to exceed $20,000,000 to $30,000,000; (ii) increase the Standby Letter of Credit Facility Sublimit from an aggregate principal amount not to exceed $35,000,000 to $65,000,000; (iii) increase the Aggregate Commitment from an aggregate principal amount not to exceed $50,000,000 to $80,000,000 total outstanding at any one time; and (iv) increase certain fees payable by the City to the Bank under the Credit Agreement in connection with the credit facilities thereunder. Such amendments will permit SJCE to enter into power contracts and provide collateral for power purchase agreements during the ramp-up phases of the SJCE. Advances under the Revolving Line of Credit will also be used to fund start-up and long-term costs for working capital associated with the operation of the Program, including the purchase of electrical power. Additionally, draws can be made on the Revolving Line of Credit to meet the Operating Reserve Requirement to the extent there is insufficient cash to meet the reserve requirement. A summary of the business terms of the Agreement and First Amendment are provided in Appendix A.

Revised 2018-2019 Budget Projections and Recommended Budget Actions

SJCE's 2018-2019 Adopted Operating Budget was based on preliminary forecasts of SJCE's load, PG&E's rates, and the PCIA that were incorporated into a preliminary version of SJCE's financial model to estimate the power costs and associated revenue for SJCE. In November, budget adjustments were approved to bring the budget in line with the latest proforma before the launch of the program to non-municipal customers.

Additional budget adjustments are now necessary after launching operations, entering into power purchase agreements, and further refining the financial modeling tool to reflect actual operations of SJCE. In addition, SJCE is required to meet the Operating Reserve Requirement as specified under the terms of the Credit Agreement of $10 million by August 31, 2019, $15 million by November 15, 2019, and $20 million by December 31, 2019. Based on updated projections, the required reserve levels are anticipated to be met next fiscal year. SJCE does not anticipate it will have sufficient net revenue in 2018-2019 to fund the Debt Service – Principal – Revolver payment to pay debt service and to maintain the Community Energy Rate Stabilization Reserve at $4.9 million in 2018-2019 after adjustments to the Cost of Energy appropriation (power supply cost) are made. It is also likely the O&M reserve will not be fully funded by the end of this fiscal year.

An increase to the Cost of Energy appropriation (power supply cost) in the amount of $23 million is recommended in 2018-2019. This increase is primarily due to an increase in load and potentially higher than expected RA costs as described below.

1) SJCE's current actual load is approximately 15% higher than was forecasted based on early metering results for February 2019. SJCE is still evaluating its current actual load

and associated revenues, and it is unclear whether this increase will continue throughout 2019. It is possible that this increase was weather-related and will only impact the month of February. It will take SJCE several months to evaluate and analyze this trend. However, SJCE recommends increasing the Cost of Energy appropriation (power supply cost), assuming this increase will continue throughout 2018-2019, to ensure adequate funding is available, if needed. This change will allow SJCE to pay for the additional power supply that may be required to serve its load if the increased load trend continues. This results in a potential increase of $6.7 million in power costs for 2018-2019.

2) SJCE's potentially higher than expected RA and other power costs results in an estimated cost increase of $16.3 million for 2018-2019. Some of the main factors contributing to the increased costs include power prices increasing in mid-October due to natural gas supply issues and lower storage availability; and the California Public Utilities Commission's requirement of SJCE to procure excess RA in early 2019; and the payment of a potential penalty.

The $23.0 million increase to the Cost of Energy appropriation is recommended to be offset by a decrease to the Debt Service – Principal – Revolver appropriation ($20.0 million) and the Community Energy Rate Stabilization Reserve ($3.0 million). Typically, an increase in the cost of energy would be offset by an increase in the revenue estimate. However, this adjustment is not recommended because the current revenue estimate is overstated in relation to the cost based on actual performance. As shown in the table below, the 15% load increase is needed to meet the current revenue estimate of $114.6 million, but does not allow for additional revenue over that amount. The revenue will fall below the budgeted estimate if this load increase is not realized.

2018-2019 Community Energy Major Budget Components

	2018-2019 Modified Budget	2018-2019 Revised Estimate (No Increase in Load)	March-June 2019 15% Load Increase	Recommended 2018-2019 Modified Budget
Fees, Rates, and Charges - Energy Sales	$114,616,000	$101,338,000	$114,616,000	$114,616,000
Cost of Energy	$82,000,000	$98,303,000	$105,000,000	$105,000,000
Other Operating Costs	$13,732,568	$13,732,568	$13,732,568	$13,732,568

EVALUATION AND FOLLOW-UP

No additional follow-up is anticipated.

PUBLIC OUTREACH

The proposed First Amendment (together with a form of Note appended thereto), in substantially final form, will be posted to the City's Council Agenda webpage for the April 30, 2019 Council Meeting.

COORDINATION

This report has been coordinated with the City Attorney's Office.

COMMISSION RECOMMENDATION/INPUT

There is no commission recommendation or input associated with this action.

FISCAL/POLICY ALIGNMENT

The proposed financing plan is also consistent with the City's Debt Management Policy which establishes objectives in order to obtain cost-effective access to the capital markets, which includes minimizing debt service and issuance costs; maintaining access to cost-effective borrowing; and ensuring compliance with applicable State and Federal laws.

COST IMPLICATIONS

The net financial impact of the new fees and rates associated with the First Amendment to the Credit Agreement are estimated at $25,000 in 2018-2019 and a cost range of approximately $2.3 million to $2.4 million for the remaining term of the Credit Agreement, as amended. The 2018-2019 costs are anticipated to be funded by the current year allocation. Costs for future years will be included as part of the budget development process and subject to the appropriation of funds. The lower amount assumes minimal amounts of the Credit Facility have been drawn or utilized and the higher amount assumes full use of the Credit Facility's $80 million limit. In addition, costs for professional services, such as bank expenses, bank counsel, and borrower's counsel fees are estimated at $45,000 as well as an amendment fee of $5,000 to amend the current contract will be funded by estimated savings the Community Energy Non-personal/equipment appropriation.

As described above, the increase to the Cost of Energy appropriation of $23.0 million is recommended to be offset by decreases to the Debt Service – Principal – Revolver ($20.0 million) appropriation that was budgeted to pay debt service and to the Community Energy Rate Stabilization Reserve ($3.0 million). No adjustment to the revenue estimate is recommended based on actual performance. After launching operations, entering into power purchase

agreements, and further refinement of the financial modeling tool, SJCE discovered that the 2018-2019 estimated revenue was set too high relative to the cost of energy.

BUDGET REFERENCE

The table below identifies the funding source and the appropriation adjustments recommended in this memorandum.

Fund #	Appn #	Appn. Name	Current Appn.	Recommended Budget Action	2018-2019 Operating Budget Page	Last Budget Action (Date, Ord. No.)
501	202V	Cost of Energy	$82,000,000	$23,000,000	X-76	11/6/2018, 30182
501	204F	Debt Service – Principal - Revolver	$20,000,000	($20,000,000)	X-76	10/16/2018, 30172
501	8530	Ending Fund Balance – Community Energy Rate Stabilization Reserve	$4,939,000	($3,000,000)	X-76	6/19/2018, 30124

CEQA

Not a Project, File No. PP17-003, Agreements/Contracts (New or Amended) resulting in no physical changes to the environment.

/s/
JULIA H. COOPER
Director of Finance

/s/
LORI MITCHELL
Director of Community Energy

Margaret McCahan
MARGARET MCCAHAN
Budget Director

For questions, please contact Lisa C. Taitano, Assistant Director of Finance, at (408) 535-7041 or Lori Mitchell, Director of Community Energy, at (408) 535-4880.

Attachment: Appendix A: Summary of Amended Business Terms with Barclays

APPENDIX A

SUMMARY OF AMENDED BUSINESS TERMS WITH BARCLAYS

Under the terms of the Credit Agreement, as amended by the First Amendment, the Aggregate Commitment will be increased from an aggregate principal amount of not to exceed $50,000,000 to $80,000,000 to support SJCE. A Commitment Fee will be charged by the Bank on the undrawn amount of the Line of Credit Facility Sublimit and the Letter of Credit Facility Sublimit available for issuances, or amendments to, letters of credit at the "Commitment Fee Rate" corresponding with the table below. The "Letter of Credit Fee Rate" is charged on the stated amount of each letter of credit (i.e. the amount the purchase power provider requires the City to make available for draw by the provider under the letter of credit as security for the City's obligations under a power purchase agreement). The "Drawn Fee Rate" at any given time, as set forth in the following table, is determined based on the current LIBOR rate plus the "Applicable Spread" for the line of credit and the letter of credit. The City is allowed to draw on the Revolving Line of Credit to meet the Operating Reserve Requirement if needed.

Revolving Line of Credit			
Term	Commitment Fee Rate		Drawn Fee Rate
3 Year	Increase from 0.65% to 1.00%		Increase from 1-month LIBOR + 2.10 to 1-month LIBOR + 2.90%
Standby Letter of Credit			
	Commitment Fee Rate	Letter of Credit Fee Rate	Unreimbursed Draw Fee Rate
5 Year	Decrease from 1.05% to 1.00%	Increase from 1.75% to 1.95%	Increase from 1-month LIBOR + 2.10 to 1-month LIBOR + 2.90%

Each issuance of a Standby Letter of Credit is subject to a $600 application fee.

The Bank's commitment to make advances under the Revolving Line of Credit is scheduled to terminate on November 27, 2021.

The Bank's commitment to issue Standby Letters of Credit for the account of the City is scheduled to terminate on October 27, 2023 .

Letter of Credit Issuance Fee 1.95%

Default Rate: Prime Rate + 4.00%. This is the interest rate charged to the City upon the occurrence of certain enumerated events (defined in the Credit Agreement as "Events of Default") and during the period such events continue.

Prime Rate: For any day, the rate of interest in effect for such day as publicly announced from time to time by the Bank as its "prime rate." The "prime rate" is a rate set by the Bank based upon various factors including the Bank's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans, which may be priced at, above, or below such announced rate. Any change in such rate announced by the Bank shall take effect at the opening of business on the day specified in the public announcement of such change.