THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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Proposed Financing Plan for Plaza de Panama Project in Balboa Park

OVERVIEW

On October 27, 2016, the Infrastructure Committee received information regarding a proposed Financing Plan for the Plaza de Panama Project ("Project") in Balboa Park. The Project involves construction of a below-grade paid parking garage, a ground-level rooftop park on top of the garage, a bypass bridge for vehicles, roadway improvements leading to the garage, and other improvements to the Alcazar parking lot and specific Park plazas. The total cost of the Project is currently estimated to be approximately $78.1 million.

A public-private partnership between the City and the Plaza de Panama Committee ("Committee") is proposed for the Project. Terms of the partnership are specified within a Cooperation Agreement ("Agreement") between the City and the Committee. The Agreement requires the City to contribute $49 million to the Project. The Committee is required to contribute up to $29.1 million and cover cost overruns, if any, encountered during Project construction after a $6.1 million Construction Contingency Reserve has been exhausted.

If the City Council elects to approve the Agreement and requested financial authorizations for the Project on November 14th, it will be initiating one of the largest public-private partnerships for the construction of public infrastructure the City has ever undertaken. Public-private partnerships provide unique opportunities to raise private capital to help fund the construction of public projects that otherwise might not be fiscally viable. The Agreement before the Council stipulates Project roles, fiscal responsibilities, and rights for both the City and the Committee.

The proposed Project Financing Plan indicates the City will use a combination of bond financing and cash to meet its $49 million funding obligation. This report discusses the current Financing Plan, contrasts it with key elements of the 2012 plan, and highlights important provisions within the Agreement that may have fiscal implications for the Financing Plan.

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FISCAL/POLICY DISCUSSION

The Proposed Financing Plan

The proposed Agreement requires the City to contribute $45 million for Project construction and $4 million for City staff costs related to the Project. Approximately $3.75 million of the $4 million in anticipated City staff costs (shown in Exhibit A of the Agreement) are for Program and Construction Management expenses incurred by the Engineering branch of the Public Works Department. The remaining $250,000 is attributable to Project related fees for the Development Services Department. The City's total contribution to the Project in accordance with the Agreement is therefore expected to be capped at $49 million. This amount excludes the interest the City will pay on the bonds over thirty years.

As discussed in the staff report, the Financing Plan calls for $39 million of the $49 million to be financed with bonds and the remaining $10 million to come from City funds that would otherwise be available for other major capital projects. The following sections provide key elements of the Project Financing Plan in 2012 as compared to 2016, discuss the proposed lease revenue bond issuance, and identify the $10 million of existing City funds being used to satisfy the $49 million contribution requirement.

Comparison of the 2012 and 2016 Financing Plans

The table below illustrates key elements of the Plaza de Panama Project Financing Plan in 2012 as compared to the current plan. A number of factors have contributed to increased Project costs since 2012. These factors are discussed in IBA Report No. 16-40 entitled "Plaza de Panama Project and Proposed Cooperation Agreement", which focuses on the Project and the Agreement.

Plaza de Panama: Comparison of 2012 and 2016 Project Financing Plans		
	2012	**2016**
Total Project Cost	$45.3 million	$78.1 million
City Contribution / Private Contribution ($)	$14 million / $31.3 million	$49 million / $29.1 million
City Contribution / Private Contribution (%)	31% / 69%	63% / 37%
Cost of Parking Garage*	$17 million	$33.3 million
Proposed Parking Rates	$5 for 5 Hours	Weekday: $2/$4/$8 Weekend/Holiday: $3/$6/$12 (0-1 hour/1-2 hours/Over 2 hours)
Projected Net Revenue from Garage Operations**	$1.3 million	$3.3 million
Lease Revenue Bonds for Project	$14 million	$39 million
City Cash Contribution for Project	$0	$10 million
Annual Lease Payment/Debt Service	$1.1 million	$2.7 million
Use of Bonds	Garage only	Entire project***

* Excludes rooftop park.

** Projected Net Revenue from Garage Operations does not include the annual debt service.

*** The Project involves construction of a below-grade paid parking garage, a ground-level rooftop park on top of the garage, a bypass bridge for vehicles, roadway improvements leading to the garage, and other improvements to the Alcazar parking lot and specific Park plazas.

Proposed Lease Revenue Bonds

Staff is requesting the Council authorize the issuance of up to $50 million of lease revenue bonds ("Bonds"). The financing structure of the Bonds is similar to the CIP infrastructure bonds the City has issued in recent years and the bonds previously proposed for the Project in 2012. The bond financing structure necessitates the creation of a lease between the City and its Public Facilities Finance Authority ("Authority"). The City would first lease the site of the Project's parking garage to the Authority for a nominal annual lease payment and the Authority would subsequently lease the completed parking garage back to the City for annual lease payments that are sufficient to cover annual debt service payment on the Bonds. The Bonds would be issued by the Authority, and the City's General Fund would be responsible for making the annual lease payments to the Authority.

The Financing Plan estimates Bonds will be issued in August or September of 2017. In requesting authorization to sell up to $50 million of Bonds, staff is conservatively requesting authority to sell more bonds than they currently expect to need in order to accommodate potential changes in interest rates, market conditions, or unanticipated changes in the Project timeline. Based on an assumed interest rate of 4.25% for the Bonds, the goal is to receive approximately $44.5 million of bond proceeds to provide $39 million to the Project Construction Fund, $4.9 million to the Capitalized Interest Fund which will make lease payments to the Authority for 2.5 years while the parking garage is being constructed, and $600,000 to cover other necessary costs associated with issuing the bonds. If these estimates are accurate, the City's annual lease payment to the Authority would be approximately $2.7 million over the 30-year life of the bonds.

If the Bonds were to be issued today, staff indicates they would receive an interest rate of approximately 3.6%. The Financing Plan conservatively uses a 4.25% interest rate because Bonds are not expected to be issued until September 2017 and interest rates could rise in that time. If, however, interest rates were to remain unchanged at 3.6%, the Bonds could be issued to yield approximately $43.4 million for the Project Construction Fund (as opposed to $39 million) without increasing the $2.7 million annual lease payment. If this were to be the case, staff has indicated the City would be able to proportionally reduce its $10 million cash contribution to the Project by the additional $4.4 million of bond proceeds. Conversely, if interest rates were to rise above 4.25% when the Bonds are issued, the City would need to increase its planned $10 million cash contribution in order to maintain the annual $2.7 million lease payment to the Authority.

The City hired the same parking consultant it hired in 2012 (Parking Concepts Inc. or "PCI") to utilize limited parking data gathered by City staff to reassess demand for paid parking, develop a proposed parking fee model, and estimate reasonable operating costs for the Project's parking garage. Based on PCI's estimates, total annual revenue from parking garage operations in the first year is projected to be approximately $4 million. After deducting $683,000 for annual operating and maintenance expenses and $2.7 million for the annual lease payment due to the Authority, the paid parking garage is projected to generate net revenue of approximately $630,000.

If these projections are correct, net parking garage revenue would be used to fully offset the General Fund's annual lease payment obligation to the Authority. To the extent net annual revenue exceeds the estimated $2.7 million annual lease payment, excess revenue would become unrestricted General Fund revenue that could be appropriated for any general purpose through the annual budget process. Alternatively, if net annual parking revenue were to fall significantly short of projections and be less than the $2.7 million annual lease payment, the General Fund will be required to cover the shortfall as a priority expense.

Assuming estimated debt service on the Bonds and PCI revenue/expense estimates are accurate, the following table projects net revenue, on a bi-annual basis, that would be unrestricted and available for other General Fund purposes beginning in calendar year 2020 when the parking garage is expected to become operational.

Estimated Net Revenue from Paid Parking Garage Operations					
	2020	**2022**	**2024**	**2026**	**2028**
Revenue					
General Visitor Parking	$ 3,792,720	$ 4,045,694	$ 4,045,694	$ 4,315,542	$ 4,603,389
Monthly Permits/Users	$ 45,000	$ 48,002	$ 48,002	$ 51,203	$ 54,618
Valet Parking	$ 175,200	$ 186,886	$ 186,886	$ 199,351	$ 212,648
Total Revenue	**$ 4,012,920**	**$ 4,280,582**	**$ 4,280,582**	**$ 4,566,097**	**$ 4,870,655**
Operating Costs	$ 682,530	$ 755,611	$ 800,832	$ 835,722	$ 872,281
Revenue Net of Operating Costs	**$ 3,330,390**	**$ 3,524,970**	**$ 3,479,750**	**$ 3,730,375**	**$ 3,998,374**
Estimated Lease Payment to Authority	$ 2,700,000	$ 2,700,000	$ 2,700,000	$ 2,700,000	$ 2,700,000
Estimated Net Revenue	**$ 630,390**	**$ 824,970**	**$ 779,750**	**$ 1,030,375**	**$ 1,298,374**

Note: Assumes parking garage opens January 1, 2020. Parking garage revenue and operating costs are based on Parking Concepts Inc. (PCI) projections. Total Revenue is assumed by PCI to increase 6.66% every third year.

While these net revenue projections represent the best current estimates of City consultants and staff, they are based on estimates of future demand for paid parking and bond market conditions which can change due to a variety of factors. There may not be any net revenue in any given year or there could be a net loss which would result in an added expense for the City's General Fund. For example, there wouldn't be any net revenue in 2020 if demand for General Visitor Parking were to be 17% less than the PCI projections. There would be a net loss to be covered by the General Fund if demand for parking were to be more than 17% below PCI projections.

The Project also involves one-time costs (e.g., $320,000 for a parking management plan in fiscal years 2018 and 2019) and ongoing costs (e.g., $366,000 annually for four additional Park & Recreation Department staff to maintain new Project improvements - this annual expense was not included in costs to be addressed with parking garage revenues). As these will be new Project-related General Fund costs that are not included in the recently released Five-Year Financial Outlook, they should be considered when evaluating the potential for future net revenue attributable to paid parking in the new garage.

Additionally, the Financing Plan requires the first $2.7 million (or an amount equal to the actual annual lease payment) of net revenue be deposited into an Internal Safety Fund. The Internal Safety Fund is being established to buffer the General Fund from any parking revenue volatility that may be encountered over the 30-year term of the Bonds. If current projections were to be accurate, the resulting net revenue from parking garage operations over the first three to four years would be deposited into the Internal Safety Fund and not be available for other General Fund uses.

Proposed City Cash Contributions to the Project

Assuming bonds are issued to finance $39 million of the City's $49 million commitment to the Project, the Financing Plan envisions the remaining $10 million will come from City funds that would otherwise be available for other major capital projects. As noted in the previous section of this report, if bond interest rates remain low resulting in additional available proceeds for the Project, the City's cash contribution could be reduced by an equivalent amount.

On September 19, 2016, the City Council approved the establishment of the Plaza de Panama CIP and authorized the CFO to appropriate and expend up to $1 million for the purpose of: finalizing the design; ensuring compliance with all applicable regulations; and calculating a revised cost estimate for the Balboa Park Plaza de Panama Project. The $1 million appropriation was comprised of approximately $603,000 in idle funds for other Balboa Park CIPs and $397,000 from the Capital Outlay-Sales Tax Fund.

The Financing Plan indicates the remaining $9 million cash contribution to the Project will come from two funding sources. The longstanding Capital Outlay-Sales Tax Fund has unallocated fund balance that would be used to provide $1 million to the Project. The final $8 million would come from the City's Capital Outlay-Miscellaneous Revenue Fund which has available proceeds from the sale of City properties.

Important Financial Provisions within the Proposed Cooperative Agreement

On November 8, 2016, the City Attorney issued a memorandum explaining some of the stipulated responsibilities for the City and the Committee in the Agreement. As noted in the City Attorney's memorandum, the Agreement is unique and represents a negotiated arrangement where both the City and the Committee have roles in delivering the Project. This section highlights key financial provisions of the Agreement that relate to the City's financial obligations and proposed Financing Plan.

Section 1.8: This is an important section because it specifies: 1) the City's responsibility to contribute $45 million for Project construction and $4 million for City staff charges, permits, inspections or other City costs; and 2) the Committee's responsibility to cover all Project costs [excluding City staff charges, City permit fees, and costs tied to City negligence] above the City's $49 million contribution irrespective of whether those costs were anticipated or attributable to differing site conditions, delays, etc.

Section 1.4: Specifies that the City and Committee must jointly agree on any design changes or change orders during construction. City and Committee approval of design changes or change orders is not to be unreasonably withheld and dispute appeal processes are provided. It should be noted that any design changes, and/or change orders, could result in cost overruns that would be the responsibility of the Committee. Additional time could be required to achieve agreement on needed changes during construction, which could in turn impact the Project timeline. It will be important for the City and the Committee to have Project leads, designated in advance, to expeditiously work through any necessary changes.

Section 1.13: The Committee warrants to the City that the Project design will be of good quality and free of defects. If notified by the City within one year of Project completion, the Committee must correct any portion of the Project for which the design was not in conformance with this warranty at its own cost and expense. The Committee's consultants are required to adhere to the insurance requirements set forth in Exhibit C of the Agreement.

Section 1.14 and 1.17: Requires the Project to be designed in compliance with the Americans with Disabilities Act (ADA). In accordance with the City Municipal Code, all of the work on the Project that is covered by the Agreement is subject to State prevailing wage laws.

Section 2.1: States that revenue generated from the operation of the paid parking garage is to be used to cover all bond related expenses including debt service and costs of issuance. Additionally, this revenue is expected to cover operation and maintenance expenses for the parking structure. It should be noted that this section does not provide that certain one-time or ongoing expenses related to the Project (e.g., the interim Parking Management Plan or additional Park & Recreation staff to maintain Project improvements) are to be covered by garage revenues.

Section 3.4: This section describes circumstances that would allow the Committee to terminate the Agreement for its convenience. Prior to the award of the construction contract, the Committee can elect to terminate the Agreement if: 1) the City does not approve its $45 million funding commitment for construction by June 1, 2017 or 2) the low-bid for the construction contract were to exceed the $60 million estimate in Exhibit A of the Agreement by approximately $1.5 million. At this point, the City would have already incurred some costs related to the Project but not have initiated construction. Once the construction contract has been awarded, neither the City nor the Committee may terminate the Agreement for convenience.

Section 3.6: This section provides a joint right to terminate the Agreement if the low-bid for the construction contract exceeds the $60 million estimate in Exhibit A by any amount. It requires the City and the Committee to discuss the higher than expected bid and determine whether to proceed and how the additional Project costs will be funded. If the parties cannot reach agreement, either party may terminate the Agreement for convenience. The Project timeline calls for the construction contract to be awarded at the end of August 2017.

CONCLUSION

On November 14th, the City Council will be asked to approve a Cooperation Agreement and authorize a Financing Plan for the proposed Plaza de Panama Project. If approved, the Council will be initiating one of the largest public-private partnerships for the construction of public infrastructure the City has ever undertaken. This report reviews the Financing Plan and highlights key provisions of the proposed Agreement.

The Financing Plan calls for the issuance of up to $50 million of lease revenue bonds to provide $39 million of the City's $49 million contribution commitment to the Project in accordance with the Agreement. The City would provide the remaining $10 million from City funds that would otherwise be available for other major capital projects. Based on current projections, annual debt service on the Bonds would be approximately $2.7 million for 30 years.

The City's General Fund would be responsible for debt service payments on the Bonds. However, the Project's paid parking garage is projected to generate approximately $3.3 million of net revenue in the first full year of operation (2020) which would more than offset the General Fund debt service payment. If, however, the City's parking consultant (PCI) has significantly overestimated demand for public parking, the City's General Fund will be required to cover the resulting revenue shortfall as a priority expense.

There are three Bond features that provide limited protection to the General Fund. There is a Capitalized Interest Fund to pay debt service on the Bonds while the Project is being constructed. The Bonds have been structured so that projected net parking garage revenues exceed debt service by approximately 20%. Additionally, the Financing Plan requires that approximately $2.7 million of net revenue from parking garage operations (after debt service has been paid) be deposited into an Internal Safety Fund. If parking demand projections are accurate, it would take approximately 4 years to accumulate $2.7 million for the Fund which could then be utilized as a reserve to buffer the General Fund from any parking revenue volatility that may be encountered over the 30-year term of the Bonds.

This report summarizes key financial provisions in the Agreement relating to the City's financial obligations and the proposed Financing Plan. Some of these provisions protect the City's financial exposure on this Project. For example, the Committee must cover cost overruns once construction begins and additionally agrees to correct any design-related Project defects. Other provisions stress the importance of working well with the Committee as our Project partner (to process design changes or change orders during construction) to avoid disputes and project delays. Provisions allowing either party to terminate the Agreement (prior to the award of the construction contract) highlight the importance of accurate Project cost estimates in Exhibit A of the Agreement, and could test the Committee's willingness to commit additional funds to the Project should the low bid exceed current estimates.

This public-private partnership provides an opportunity to pursue a unique infrastructure project with the added benefit of private sector capital. It also raises a policy question about prioritization of City infrastructure projects as this Project was not initially prioritized by City staff. Project prioritization is particularly important given that the City's infrastructure needs exceed our limited capital and human resources to address those needs. The Council may want to confirm that this Project will not adversely impact staff capacity to complete other projects, hinder the City's ability to complete other prioritized infrastructure projects for which bonds have already been issued, or delay the next planned issuance of deferred capital bonds.

The IBA is not recommending the Council support or oppose this Project as we believe it is a policy call for the Council that must balance this unique public project opportunity against the City's capacity to address other high-priority infrastructure needs. We have reviewed the Project Financing Plan and believe it to be reasonable, noting the inclusion of conservative provisions for the planned issuance of Bonds. It is important to note that this is a large public-private partnership and, like all public infrastructure projects, it is not without some limited financial risk. Future parking demand can be difficult to project for the year 2020 and beyond considering other parking and travel options. The accuracy of PCI's parking demand projections will ultimately determine whether this is a financially self-sufficient project, or a project that will potentially require contributions from the City's General Fund in the future.

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