



The State Bar of California

OPEN SESSION AGENDA ITEM JULY 2020 FINANCE COMMITTEE III.A

DATE: July 6, 2020

TO: Members, Finance Committee

FROM: John Adams, Chief Financial Officer

SUBJECT: Real Estate Analysis and Strategy Development – Loan Refinancing

EXECUTIVE SUMMARY

As part of its analysis of options to identify sufficient funding to implement the State Bar's Five Year Capital Improvement Plan, or relieve the State Bar of its obligations as an owner of its San Francisco building, staff conducted an analysis of the debt service on the loan related to the Los Angeles building. While the impacts of COVID-19 have led to additional expenditures for the State Bar in certain circumstances, it has also created a situation that may allow the State Bar to save money and reduce annual outlays for repayment of the Los Angeles loan. This agenda item is requesting that the Finance Committee of the Board of Trustees authorize staff to proceed with exploring refinancing of the 2012 Loan with Bank of America that was used to purchase the State Bar's building in Los Angeles.

BACKGROUND

The State Bar has approximately \$21 million in outstanding real estate loans. There are two loans outstanding, one for the purchase of the Los Angeles property and the other for improvements at the San Francisco Building. On November 1, 2012, the State Bar entered into a Real Estate Loan Agreement in the amount of \$25,500,000 with Bank of America, N.A., for the purpose of financing the costs of purchasing real property located at 845 South Figueroa Street, Los Angeles. The loan bears a tax-exempt fixed rate of 4.26 percent per year and is due on November 1, 2027, with a monthly payment of \$191,802. The total annual debt service payment is \$2,301,600. The loan agreement also contains certain covenants including the requirement of a \$4.6 million debt service reserve fund with Bank of America. As of June 30, 2020, the outstanding loan balance for the 2012 Los Angeles Building Loan was \$14,614,532. The 2016 Loan used for the San Francisco building has an outstanding balance of \$6,387,277.

DISCUSSION

As part of the 2020 Budget approval on January 24, 2020, the Board of Trustees provided direction that staff in the Office of Finance and the Office of General Services work with the Finance Committee to do a comprehensive analysis of alternatives and funding options for the State Bar's 5 Year Capital Project Plan, including tenant improvements.

The comprehensive analysis would include the following components with regard to State Bar property located at 180 Howard Street in San Francisco:

1. Review of the scope and costs of the Five-Year Capital Improvement Plan
2. Space Utilization Study for 180 Howard Street
3. Building Occupancy and Market Analysis for 180 Howard Street
4. Debt Analysis and Funding Options

During the first quarter of 2020, staff completed the review and cost analysis of the five-year capital plan. But with a world-wide pandemic, COVID-19 has impacted both the space utilization and market analysis. Although a space utilization study was completed prior to the pandemic, the need to provide a safe work environment by ensuring proper social distancing make the plan to condense the staff into a smaller space, with more cubicles added on certain floors, problematic. At the same time, the experience with telecommuting could result in a work environment in which a substantial amount of staff work from home full time on a permanent basis, and other staff only requiring hoteling space for limited in office presence. Until the future of the State Bar work environment is decided, efforts to revise the space utilization study will need to be put on hold. COVID-19 has also impacted the office rental market as businesses expand telecommuting and are not looking to rent more office space. Similarly, the amount of space the State Bar would need in a sales/lease back or for rental space in another building is in flux pending settling down of the pandemic and decisions about how we will conduct our work in the future.

Debt Analysis and Funding Options

COVID-19 has also impacted interest rates due to actions by the Federal Reserve, with the 10 Year Treasury going from 1.88 percent on January 1st to 0.68 percent as of July 1st, representing a decline of 64 percent since the beginning of the year. This change in the market has provided an opportunity to refinance existing loans at a lower rate and extend the remaining term to provide a substantial savings and cash flow relief to the State Bar, especially with the loss of revenue from investment earnings.

New Loan Analysis – It is anticipated that the current financial market will continue to provide very favorable interest rates, with the short to medium term remaining very attractive to investors, especially banks. The 2012 Loan can be refinanced to provide savings to the State Bar. The table on the following page shows a comparison of the current loan with what is estimated for the refinance based on current market rates.

	<u>Estimated</u>	<u>Estimated</u>	<u>Current</u>
Refinancing Term	10 Years	20 Years	15 Years (11/2027)
Interest Rate	2.4%	3.0%	4.26%
Annual Debt Service	\$1,245,000	\$765,000	\$2,301,600
Net Present Savings (\$)	\$770,000	\$454,000	-
Net Present Value Savings (%)	5.4%	3.2%	-

Debt Structure – Staff, in consultation with its Municipal Advisor, recommends proceeding with a tax-exempt private placement with a term between 10 and 20 years. Advantages of a private placement compared to a public sale include limited annual disclosure governed by the U.S. Securities and Exchange Commission Rule 15c2-12 since the debt will not be traded in the secondary market and no requirement for a credit rating from a rating agency like Fitch or Moody’s. The Los Angeles Building would be security for the loan and a 1-year debt service reserve would be anticipated. The refinancing would be a competitive bid process, where a request for proposal and term sheet will be distributed to potential lenders. Staff will request proposals for a 10, 15, and 20-year loan.

Sample 10 Year Loan – Depending on the length and terms of the loan, it is anticipated that the new loan amount will be between \$11 and \$12 million, as compared to the current outstanding balance of \$14 million. Below is a sample of the Sources and Uses on the new loan.

Application of Existing Reserve Fund	\$ (4,600,592)
Escrow Deposit	14,220,152
Reserve Fund	1,245,440
Cost of Issuance	<u>200,000</u>
Total Loan Amount	\$ 11,065,000

Financing Team – In addition to key State Bar staff from the Office of Finance and Office of General Counsel, the refinancing requires certain outside professionals with expertise in tax-exempt financing for public agencies. As its Municipal Advisor, the State Bar has engaged James Fabian, of Fieldman, Rolapp & Associates, to assist in the formulation and execution of the financing plan. The municipal advisor serves as a fiduciary licensed by the U.S. Securities and Exchange Commission. In addition, the State Bar will engage outside bond counsel and a placement agent to assist in the refinancing. Cost of issuance is estimated at \$200,000 and is contingent on a completed transaction.

Tentative Schedule – The schedule on the following page provides a reasonable timeline should the Finance Committee approve staff proceeding with the refinancing of the 2012 Loan. Once proposals are received and evaluated, the recommended bid will be brought back to the Finance Committee in early September for recommendation to the Board on September 24, 2020. Closing is anticipated in early October.

<u>Description</u>	<u>Timeline</u>
1. Finance Committee Meeting	July 6, 2020
2. Selection of Consultants	July 13 – 24, 2020
3. Development of Documents	July 27 to August 14, 2020
4. RFP & Term Sheet to Banks	August 17, 2020
5. Proposals Due	September 1, 2020
6. Finance Committee Meeting	September 8, 2020
7. Board Approval	September 24, 2020
8. Close	October 1, 2020

FISCAL/PERSONNEL IMPACT

Refinancing and restructuring the 2012 Loan could reduce the annual debt service by more than \$1 million annually and would provide at least \$450,000 in savings over the term of the new loan.

STRATEGIC PLAN GOALS & OBJECTIVES

Goal: 3. Improve the fiscal and operational management of the State Bar, emphasizing integrity, transparency, accountability, and excellence.

Objective: (k) In conjunction with annual budgets, ensure maintenance and use of the Bar's Los Angeles and San Francisco buildings to maximize benefit to the Bar and the people of California.

RECOMMENDATIONS

Should the Finance Committee concur in the proposed action, passage of the following resolution is recommended:

RESOLVED, that the Finance Committee recommends and authorizes staff to proceed with refinancing the 2012 Loan with Bank of America, including hiring outside consultants, preparing legal and financing documents, and soliciting proposals from lenders, and it is

FURTHER RESOLVED, that staff will return to the Finance Committee in September with the recommended bid so the Finance Committee can make a recommendation to the Board of Trustees for its meeting on September 24, 2020.