

## MEMO

TO: City Council, City of Northfield, Minnesota;  
Board of Commissioners, Economic Development Authority in and for the City of  
Northfield, Minnesota

FROM: Jenny Boulton, Kennedy & Graven, Chartered

DATE: September 23, 2024

RE: Summary of Documents Related to EDA's Lease Revenue Bonds (Municipal Ice  
Arena Project)

### Background

The City of Northfield, Minnesota (the "City") is authorized by Minnesota Statutes, Section 465.71, as amended, to acquire real and personal property under lease-purchase agreements. The Northfield Economic Development Authority (the "EDA") is authorized by Minnesota Statutes, Sections 469.090 to 469.1082 (the "Act"), and specifically Section 469.103 thereof, to issue revenue bonds for any of its corporate purposes, and to pledge thereto income and revenues of the EDA, including without limitation revenues received under a lease with the City. The City proposes to enter into a lease with the EDA pursuant to which the City will make rental payments in an amount sufficient to pay all of the principal of and interest on revenue bonds issued by the EDA to finance the construction and equipping of a new municipal ice arena to replace the existing ice arena in the City (the "Ice Arena"). The City will also pay the operating, maintenance, insurance and all other expenses of the Ice Arena. As revenue bonds, only specific revenues of the facility are pledged toward repayment of the bonds. This limited revenue pledge means that the EDA will not be required to contribute any funds or its levy authority to provide for repayment of the bonds or operation of the Ice Arena. The bondholders have recourse only to the bond financed facility. EDA lease revenue bonds (also known as public project revenue bonds) are a recognized tool used by many communities in Minnesota to finance public building projects.

This memo is intended to provide the City and the EDA with brief descriptions of the various documents the City and/or EDA will execute as a part of the EDA issuing its Lease Revenue Bonds (Municipal Ice Arena Project), Series 2025A (the "Bonds").

### Documents

In issuing the Bonds, the following documents will be executed: (1) a Ground Lease, (2) a Lease-Purchase Agreement, (3) a Trust Indenture, (4), a Cost Share Agreement, (6) an Ice Rental Agreement, and (7) an Assignment of Rents.

The **Ground Lease (the "Ground Lease")** is between the City, as landlord and owner of the land on which the Ice Arena will be built (the "Site"), and the EDA, as tenant. Pursuant to the Ground Lease the EDA will lease the Site from the City. The term of the Ground Lease (the "Term of the Ground Lease") runs longer than the term of the Bonds. The reason the Ground Lease is longer

than the term of the Bonds is so that if the City ever stops paying rent under the Lease described below, the EDA's rights to the property would continue longer to build in a cushion to find another user of the Ice Arena. The rent for the entire Term of the Ground Lease is One Dollar (\$1.00) payable in advance on the date the Bonds are issued.

The **Lease-Purchase Agreement (the "Lease")** is between the EDA, as landlord, and the City, as tenant of the Ice Arena and subtenant of the Site, Pursuant to the Lease, the City will lease, with the option to purchase, the EDA's interest in the Ice Arena from the EDA. The Lease details the timing and amount of Lease Payments (rent) the City pays to the EDA which will be equal to the payments of principal and interest on the Bonds. The term of the Lease (the "Term of the Lease") runs concurrent to the term of the Bonds. However, the Lease may be terminated early because of (a) non-appropriation by the City; (b) the payment by the City of the Purchase Price (i.e. prepayment of the Bonds), (c) the discharge by the City of its obligation to pay the Lease Payments and Additional Lease Payments (as defined in the Lease) required to be paid by it; or (d) a default by the City and the EDA's election to terminate the Lease.

Pursuant to the Lease, the EDA appoints the City as its agent to construct the Ice Arena. The City will have full authority under the Lease to supervise and control all aspects of the construction of the Ice Arena. The Bond Trustee will disburse Bond proceeds to the City to pay project costs as they are incurred.

Except to the extent specifically provided in the Lease, the City is not obligated to appropriate or otherwise provide moneys for the payment of the Lease Payments or any other amounts coming due; and in the event of non-appropriation or non-renewal by the City, the City will not be liable for general, special, incidental, consequential or other damages resulting therefrom. The Lease does not constitute a general obligation of the City, and the full faith and credit and taxing powers of the City are not pledged for the payment of the Lease Payments or other amounts coming due, or other actions required to be performed, thereunder. While the City has the legal right to non-appropriate lease payments and terminate the Lease, the City will likely face a market reaction based on its unwillingness to pay for a government facility. That will likely make the City's borrowing costs higher for all other governmental purposes for an extended period of time. Therefore, it would be inadvisable for the City to enter into the Lease unless it has the expectation that it will want to use and pay for the Ice Arena until the Bonds are fully paid.

The Lease also contains certain covenants and agreements related to the City's use of the Ice Arena and the Site, Lease Payments and other payments, non-appropriation and requirements to maintain the tax-exempt status of the Bonds. Including, but not limited to, the following covenants of the City:

- A. Use of Facility. Subject to the City's rights to non-appropriate lease payments, the Ice Arena and the Site will be used, until the Bonds have all been paid primarily, to carry out the governmental or proprietary purposes of the City.
- B. Annual Budget. Subject to the City's rights to non-appropriate lease payments, the City administration will include in the annual budget of the City submitted to the City Council, for each Fiscal Year during the Lease Term, moneys sufficient to pay and for the purpose of paying all Lease Payments and Additional Lease Payments and other obligations of the City under the Lease.

- C. Maintenance. During the Term of the Lease the City will, at its own expense, maintain, preserve and keep the Ice Arena and the Site in good repair, working order and condition, and will from time to time make all repairs, replacements and improvements necessary to keep the Ice Arena and the Site in such condition. The EDA will have no responsibility for any of these repairs, replacements or improvements.
- D. “Additional Lease Payments”. During the Term of the Lease the City will also pay or cause to be paid when due all gas, water, steam, electricity, heat, power and other charges incurred in the operation, maintenance, use, occupancy and upkeep of the Ice Arena and the Site. The City will also pay all property and excise taxes and governmental charges of any kind whatsoever which may at any time be lawfully assessed or levied against or with respect to the Ice Arena and the Site or any part thereof or the Lease Payments, and which become due during the Term of the Lease with respect thereto; and all special assessments and charges lawfully made by any governmental body for public improvements that may be secured by a lien on the Ice Arena or the Site; provided that with respect to special assessments or other governmental charges that may lawfully be paid in installments over a period of years, the City will be obligated to pay only such installments as are required to be paid during the Term of the Lease as and when the same become due. The City may, at the City’s expense and in the City’s name, in good faith contest any such taxes, assessments, utility and other charges.
- E. Insurance. During the Term of the Lease, the City will procure and maintain continuously in effect with respect to the Ice Arena and the Site, insurance against liability for injuries to or death of any person or damage to or loss of property arising out of or in any way relating to the maintenance, use or operation of the Ice Arena and the Site. The City will also procure and maintain continuously in effect, to the extent of the full replacement value of the Facilities, other than building foundations, insurance against loss from or damage by vandalism and fire, with a uniform standard extended coverage endorsement limited only as may be provided in the standard form of extended coverage endorsement at the time in use in the State of Minnesota, in such amount as will be at least sufficient so that a claim may be made for the full replacement cost of any part thereof damaged or destroyed.
- F. Damage, Destruction and Condemnation. If the Ice Arena or any portion thereof is destroyed (in whole or in part) or is damaged by fire or other casualty or title to or the temporary use of the Ice Arena or any part thereof, or the interest of the City or the EDA in the Ice Arena and the Site or any part thereof is taken under the exercise of the power of eminent domain by any governmental body or by any person, firm or corporation acting under governmental authority, the City will have the rights with respect to the Net Proceeds of any insurance or condemnation award specified in Section 7.7 of the Lease, but the City will be obligated to continue to pay the Lease Payments and Additional Lease Payments due with respect to the Ice Arena. All Net Proceeds will be applied to the prompt repair, restoration, modification, improvement or replacement of the Ice Arena by the City, or, if the City elects not to repair or rebuild, all Net Proceeds will be applied to prepay the Lease Payments and Additional Lease Payments; in either event all Net Proceeds not needed for the purpose will belong to the City. In the event Net Proceeds exceed \$100,000, they will be held by the Trustee (as hereinafter defined) and disbursed in payment of costs of repair, restoration, modification, improvement or replacement substantially in accordance with the procedure for disbursement of Bond proceeds from the Project Fund in Article IV of the Indenture.

- G. Assignment and Subleasing by the City. Other than use by the School District and other ice time users in the ordinary course, the rights and obligations of the City under the Lease may not be assigned by the City without the written consent of the EDA and the Trustee. The City may also sublease the Project, or any portion thereof, to any other entity, provided that the City furnishes to the EDA and the Trustee an Opinion of Counsel, who is nationally recognized bond counsel, that such sublease will not adversely affect the validity of the Outstanding Bonds or the exemption of the interest thereon from federal income taxation.

The **Trust Indenture (the “Indenture”)** is a document by and between the EDA and [TRUSTEE], [a national banking association], as trustee (the “Trustee”), pursuant to which the EDA employs the Trustee, on behalf of bondholders, to receive, hold, invest, and disburse moneys for the payment and security of the Bonds; to prepare, execute, deliver and deal with the Bonds; and to apply and disburse the Lease Payments received from the City to the owners of the Bonds; and to perform certain other functions; all as provided in the Indenture and subject to the terms and conditions of the Indenture. Pursuant to the Indenture, all Lease Payments will be paid directly to the Trustee and will be deposited in the Bond Fund (as defined in the Indenture) and applied by the Trustee solely for the benefit of registered owners of the Bonds.

The Indenture establishes a Project Fund (as defined in the Indenture) and a Bond Fund and allows for certain investments of funds in the Project Fund and the Bond Fund by the Trustee, as allowable under the Internal Revenue Code.

The **Cost Share Agreement (the “Cost Share Agreement”)** is a document by and between the City and the City of Dundas, Minnesota, a municipal corporation under the laws of the State of Minnesota (“Dundas”), pursuant to which Dundas agrees to financially assist the City in funding the construction and equipping of the Ice Arena on the Site. Dundas will contribute capital by making annual payments to the City in an amount equal to the annual debt service on the Bonds multiplied by a percentage equal to the ratio of Dundas’s net tax capacity for taxes payable in the year of the issuance of the Bonds to the combined net tax capacity of Dundas and City in such year (the “Dundas Percentage”). The Dundas annual capital contribution for the estimated amount of the Bonds is estimated to be approximately \$151,963 per year. The term of the Cost Share Agreement runs concurrent to the term of the Bonds.

The **Ice Rental Agreement (the “Rental Agreement”)** is a document by and between the City and Independent School District 659, a body corporate and politic existing under the laws of the State of Minnesota (the “School District”), pursuant to which the District agrees to rent the Ice Arena from the City during certain dates and times. The School District will pay the City (A) for the rented time at the hourly rate set forth in an Addendum B attached to the Rental Agreement (as adjusted from time to time, the “Hourly Rent”) and (B) as part of its rent, the amount of \$200,000 per year for the District’s share of the costs of the Ice Arena (the “Improvement Rent”). The term of the Rental Agreement runs concurrent to the term of the Bonds.

The **Assignment of Rents (the “Assignment”)** is a document by and among the City, the EDA and the District, pursuant to which the City assigns and grants to the EDA a security interest in all of City’s right, title and interest in and to the Improvement Rent payable under the Rental Agreement. The term of the Assignment runs concurrent to the term of the Bonds.

## **Conclusion**

These documents are currently being negotiated and drafted. They will be executed by the parties on or prior to the date of the closing on the Bonds (the “Closing Date”), currently anticipated to be in early 2025. Please do not hesitate to reach out if you have any questions on these documents or the Bond structure.

## MEMORANDUM

**TO:** Ben Martig, City of Northfield  
**FROM:** Nick Anhut, Ehlers  
**DATE:** April 17, 2024  
**SUBJECT:** EDA and HRA Public Project Revenue Bonds (Lease Revenue Bonds)

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This memo has been prepared to discuss in general terms the issues involved with various types of bonds used to finance a new ice arena facility within the City of Northfield.

### General Legal Authority; Financing Options for a Public Recreational Facility

The ability to undertake projects, issue bonds and levy taxes is governed by state law. The City of Northfield is exploring building a new ice arena facility within the community. Although user fees will be used to support operations of the arena, they are not expected to generate sufficient revenue necessary to finance the cost of the new facility's construction. The City will plan to rely on property taxes to provide the primary source of repayment.

A city debt obligation for public recreational facilities supported primarily by property taxes may be issued after approval of the majority of electors voting on the question of each project. However, cities have additional options within the state statutes to issue debt outside of holding a referendum. These options are discussed below.

### Lease Revenue Bonds

An option under consideration is the issuance of revenue bonds through an Economic Development Authority (EDA) or Housing and Redevelopment Authority (HRA) pursuant to their statutory powers in Minnesota Statutes, Chapter 469 and the city's ability to enter into a lease purchase agreement pursuant to Minnesota Statutes, Section 465.71.

The concept behind lease revenue bonds, also referred to as public project revenue bonds, is that the EDA (or HRA) would exercise its statutory and local enabling powers to acquire real property and issue revenue bonds to renovate and equip a proposed facility for lease to a user. As issuer, the EDA would own the proposed facility for the term of the bonds and pledge to the bondholders the revenues made available by the facility project. The EDA and city would enter into a corresponding long-term lease purchase agreement relating to the facility and payment of debt service on the bonds. The lease will require the city make rental payments that cover the full debt service costs on the Bonds. The lease would allow the city to operate the facility, including the cost of maintenance, insurance, and all other expenses. The EDA may also designate the City as its agent to oversee construction, thereby alleviating the EDA of any associated costs, time and effort. Once all payments on the bonds have been made and the bondholders interests released, the city would then gain title to the facility.

As revenue bonds, only specific revenues of the facility are pledged toward the repayment. This limited revenue pledge allows that the EDA will not be required to contribute any funds or its levy authority to provide for the bonds' repayment, nor any liability for operations. The bondholders

interests are typically managed within a Trust Indenture with a designated trustee establishing the account for the project and debt service on their behalf. The EDA would be a party to the indenture assigning all of its rights to the city lease agreement and ownership of the facility to the Trustee as security for the bonds. In some instances, lease revenue bonds also include a set-aside debt service reserve fund pledged as a back-stop in case of insufficient funds.

### **Northfield EDA Public Project Revenue Bonds, Series 2006A**

The City of Northfield and the EDA have utilized this bonding approach for the original construction of the Memorial Pool in 2006. Through a cooperative agreement, the EDA issued \$3,210,000 Public Project Revenue Bonds, Series 2006A. The 2006A Bonds were successfully sold and the swimming facility constructed. The City operates the swimming pool and made all ongoing payments on the 2006A bonds until the City exercised its purchase option to acquire the facility and terminate the lease through a refinancing in 2014.

### **Lease Revenue Bonds - Considerations**

The city, in any one year, could technically choose to not continue the facility lease, leaving bond holders Trustee the choice to foreclose on the mortgage against the facility. The Trustee could then choose to operate the facility or sell it in order to recover the outstanding bond amount. In this unlikely event, the city would relinquish all purchase rights and built up equity from its payments, and the EDA would not be obligated to step in to remedy. This very event did occur in the City of Vadnais Heights in 2012, who chose to non-appropriate the general tax funds necessary to cover user fee revenue shortfalls it was depending on. The resulting bond default caused the City's own credit rating to be downgraded dramatically, twelve notches from "AA" to "B." The rating did not recover and the facility was ultimately sold by the bondholders to Ramsey County who operates it to this day.

Due to the annual appropriation risk, Lease Revenue Bonds typically carry a lower bond rating and higher interest cost than a general obligation bond. However, the impact generally only carries an impact on the interest rates of 30 to 50 basis points (0.30-0.50%) and the rating agencies usually give a bond rating which is one or two steps lower than the G.O. rating ("AA-" or "A+" instead of the city's "AA" G.O. rating). At the end of this memo, we have included an estimate of the pricing and debt service associated with a 20-year generic \$10,000,000 Public Project Revenue Bond in today's market.

### **General Obligation Tax Abatement Bonds**

Tax abatement is a tool a local government can use to finance public improvements or public facilities, as well as a form of assistance for new development or redevelopment. An abatement allocates the city's taxes derived from specified property toward certain public purposes like financing public facilities. The City can issue bonds without a referendum if a tax abatement is established in an amount to cover at least the principal amount required. As far as limitations, repayment of the bonds is limited to 20-years, and the sum total of all existing abatements granted within the city for any year is limited to 10% of its current net tax capacity. For the pay 2024 tax year the City of Northfield's annual abatement levy limit is \$2,431,860, of which approximately \$360,307 has been pledged or planned for other existing Abatement Obligations. It is anticipated that a significant portion of the remaining capacity would need to be set aside for the Ice Arena if abatement bonds are considered.

The city has used tax abatement bonds to finance street improvements, trails, and recreational facilities. It is expected to rely on abatement bonds for future park and infrastructure needs as well. As mentioned, tax abatement bonds can carry the City's General Obligation pledge and "AA" credit rating. For interest cost comparison purposes, at the end of this memo we have also included an estimate of the pricing and debt service associated with a 20-year \$10,000,000 General Obligation Tax Abatement Bond in today's market.

## Conclusion

While this list of financing tools is not exhaustive, they (and any combination thereof) are meant to provide the groundwork for current discussions as the city's ice arena project needs are refined. Ultimately, Lease Revenue Bonds should be expected to carry a higher interest and transactional cost when compared to a similarly sized General Obligation Bond. However, we believe that either approach would prove suitable to meet the project's funding needs. The city should weigh the anticipated cost differences against the General Obligation capacity limitations to determine its preferred fit. We at Ehlers look forward to continuing to help the city review its financing options and agreements for this important objective.

## Bond Interest Comparison:

|                              | <u>Election –<br/>G.O. Bond</u> | <u>Tax Abatement –<br/>G.O. Bond</u> | <u>Lease Revenue Bond</u> |
|------------------------------|---------------------------------|--------------------------------------|---------------------------|
| Repayment Source:            | City Tax Levy                   | City Tax Levy                        | City Tax Levy             |
| Rating:                      | AA                              | AA                                   | AA-                       |
| Principal Amount:            | \$10,000,000                    | \$10,000,000                         | \$10,000,000*             |
| Term of Debt:                | 20 years                        | 20 years                             | 20 years                  |
| Estimated Interest Rate:     | 4.0269%                         | 4.0269%                              | 4.5531%                   |
| Average Annual Payment:      | \$733,139                       | \$733,139                            | \$763,111*                |
| Cumulative Interest Expense: | \$4,662,778                     | \$4,662,778                          | \$5,262,213*              |

\* For interest cost comparison purposes, the sizing and payment estimates do not contemplate potential additional \$30,000 to \$50,000 in transactional costs, nor debt service reserve requirements that can vary widely based on the nature of the Lease Revenue terms and bond placement.