CITY OF LONGMONT
PRIVATE ACTIVITY BONDS
PROCEDURES AND GUIDELINES

The City of Longmont encourages private sector investment in our community with the use of Private Activity Bonds pursuant to the State of Colorado's Private Activity Bond (PAB) allocation program, established by state statute (CRS 24-32-1701). The State of Colorado allocates 50% of state PAB ceiling to local governments on a per capita basis and the remaining 50% to statewide authorities (i.e., Colorado Housing and Finance Authority, CollegeInvest, Colorado Agricultural Development Authority). If a local government does not issue bonds or assign the bond cap to an entity for a local project, the cap reverts to the state's pool. The state makes the unused bond cap available to (1) local issuers not receiving a direct allocation or (2) statewide authorities and designated local governments that need additional allocation.

Because Longmont is precluded from issuing such bonds by its Home Rule Charter without a vote of the citizens, Longmont will choose another governmental or appropriate entity (e.g., Boulder County, Colorado Housing Finance Agency, Colorado Department of Local Affairs, etc.) hereafter "Inducement Entity", to be the formal entity responsible for inducing the bonds. The City of Longmont issues an endorsement of the proposed project and allows its PAB allocation to be used by an Inducement Entity or the State of Colorado for distribution under the statewide allocation.

<u>What are Private Activity Bonds?</u>

Private Activity Bonds (PAB) are tax-exempt bonds that can be issued for specific purposes for **privately** developed projects. PABs are designed to offer low-cost financing that encourages private sector investment in communities throughout the country, specifically projects that increase the tax base of a local community, including: (1) affordable housing, (2) economic development/manufacturing, (3) infrastructure, and (4) environmental projects. They are bonds issued by a municipality (any city, town or county) for the purpose of financing land, buildings and/or equipment for manufacturing, industrial, commercial, agricultural or business enterprises. This financing technique may also be used for low and moderate-income housing projects, hospital facilities or other critical community needs projects.

PABs are not an obligation of the municipality; state law prohibits the municipality from making debt service payments or from incurring any other pecuniary liability in connection with the bond issue. The principal and interest on the bonds are paid by the benefiting private company pursuant to a "financing agreement": (e.g. a lease, installment sale or loan agreement) between the Inducement Entity and the company. Therefore, it is essential that the company have sufficient financial means to assure prompt payment of the bonds over the life of the bond issue. Since the interest on the bonds is exempt from Federal income taxes, the interest rate is lower than traditional corporate forms of financing. This form of bond financing can provide 100% financing of land, building, equipment and machinery, as well as project development costs, financing costs and other costs incidental to the issuance of bonds.

Program Purposes

The primary purpose of the PAB program is to meet federal requirements in the Tax Reform Act of 1986. The program is designed to accomplish the following:

1. Establish an orderly and equitable process of allocating tax-exempt PAB's.

2. Encourage private investment in creating and sustaining affordable housing, higher education, jobs, solid and hazardous waste treatment, and water and sewer facilities.

3. Encourage development in areas of the state where housing, higher education, jobs, and certain infrastructure improvements are most needed.

4. Encourage the increase or maintenance of the local tax base.

5. Maximize the use of the state's tax exempt PAB ceiling allocation.

Selected Eligible Uses of the PAB Program within the City Allocation

Eligible uses of the PAB program are wide ranging and include:

Qualified residential rental projects[1] – Bond proceeds are used to finance new construction or acquisition/rehabilitation of housing for persons with low and moderate incomes.

Single-family mortgage revenue bonds (SFMRB) – Bonds sold by local and state agencies, to be used for mortgages for persons with low and moderate incomes.

Mortgage Credit Certificates (MCC) – Local issuers can elect to use a bond allocation as mortgage credit certificates for income-qualified homebuyers.

Student loans – Proceeds are used to provide low interest loans to eligible students at institutions of higher education.

Manufacturing "small issue" industrial development bonds (not to exceed $10,000,000) – Bonds sold for construction of manufacturing facilities that cause a change in the condition of goods or products.

Qualified redevelopment bonds – Bonds sold to acquire property in blighted areas; prepare land for redevelopment; and relocate occupants of structures on the acquired property.

Exempt facility bonds – Hazardous waste facilities, solid waste disposal facilities, water and sewer

1 Rental housing projects are also eligible for Low Income Housing Tax Credits under Section 42 of the Internal Revenue Code. The Colorado Housing and Finance Authority (CHFA) administers the tax credit program in Colorado. Developers of rental housing projects must contact CHFA prior to application for PAB and inquire about applying for 4% tax credits. CHFA requires a market study completed under their guidelines. For further information, call CHFA at (800) 877-2432.

facilities, mass commuting facilities, local district heating and cooling facilities, local electric energy or gas facilities, and multifamily housing bonds.

The City strongly suggests that any project developer considering using PABs seek advice of bond counsel prior to submitting an application to determine project eligibility under federal definitions of PABs.

Structure of Private Activity Bond Issues

The principal documents generally involved in a PAB bond issue are the bonds, financing agreement, trust indenture, and official statement.

A. The Bonds--The bonds may be issued on a serial, term or a combination serial-term basis. Debt retirement schedules on the bonds can be tailored to suit the company although it is common to structure the repayment schedule so that the annual debt service payments are level. The maximum maturity of the bonds is 30 or 40 years, depending upon the applicable state statute. The state statutes do not contain maximum interest rate limitations, and the bonds are not required to be sold at a public, advertised sale.

B. The Financing Agreement--The basic instrument securing the bond issue is the financing agreement between the company and the Inducement Entity. This may take the form of a lease agreement, installment sale agreement or, in some states, a loan agreement.

Under a lease agreement or an installment sale agreement, title to the project is held by the Inducement Entity and either leased or sold on an installment basis to the company. The company acquires title to the project when the bonds are retired. Under the loan agreement, title to the project is held by the company throughout the life of the bond issue. There is, however, no property tax exemption if the title is held by the local government (i.e., City of Longmont). The tax benefits to the company (i.e., depreciation, investment tax credit, etc.) with respect to the project are the same regardless of which type of financing agreement is used.

Under all forms of financing agreements, payments are structured to retire the bonds, fund any reserve accounts, and pay any trustee or municipal/county handling charges. The company is responsible for any maintenance costs, taxes, insurance premiums and any other costs incurred with respect to the project. Other matters generally contained in a financing agreement include (1) control and authority of the company in constructing the project; (2) operational control of the project by the company; (3) maintenance and insuring of the project by the company; (4) assignment and leasing or subleasing by the company; (5) consequences or condemnation or destruction of the project; (6) criteria and remedies in the event of default; and (7) prepayment of the bonds by the company.

C. The Trust Indenture--The trust indenture is a contract between the Inducement Entity and a trust company acting as trustee for the bondholders. The trust indenture sets forth the details of the bonds, including interest rates and maturity dates, and provides for the administration of all financial aspects of the bond issue. The trustee is responsible for, among other things, disbursement of bonds proceeds, investment of idle construction funds and reserve account moneys (at the direction of the company), receipt of financing agreement payments made by the company and the payment of principal and interest on the bonds. The trustee's fees are paid by the company.

D. The Official Statement--The official statement is a document describing in detail the bond issue prepared by the investment banker, the company and bond counsel. The official statement generally conforms to the disclosure requirements of the Securities and Exchange Commission with respect to corporate securities issues, although it does not have to be registered with the Securities and Exchange Commission or any other federal agency. The official statement summarizes the financing agreement, trust indenture, and the project, and contains a description of the company including its financial statements. The official statement is distributed to potential bond purchasers, state agencies and other interested parties.

Longmont PAB Procedures

1. The Longmont City Charter does not allow the City Council to induce Private Activity Bonds without a general election vote on the issue. The City will allocate the funds via an endorsement resolution to the appropriate Inducement Entity; therefore, the applicant is required to apply to the City and receive a resolution of endorsement from the City Council as the first step towards receiving an inducement resolution.

2. After the stated due date for PAB applications, City staff evaluates PAB applications for conformance to its land use and municipal development goals and policies, as well as to evaluation criteria.

3. City staff prepares a summary report of the applications, including preliminary ranking based on the evaluation criteria, and presents the report to City Council at one of its regular meetings, which are usually the second and fourth Tuesday of each month.

4. City Council reviews the application reports and provides a recommendation for approval of PAB requests based on the evaluation of applications and funding available. One or more applicants may receive PAB funding.

5. A resolution of endorsement does not have to be provided by the applicant. The City will provide the resolution in its own format.

6. The resolution of endorsement is forwarded to the appropriate Inducement Entity as part of the City's PAB review process.

7. The Inducement Entity is responsible for issuing an "inducement resolution" prior to the company purchasing, contracting or acquiring any part of the project. An inducement resolution states, among other things, that the company is being induced to locate, expand, or remain within the municipality by the local government's willingness to issue Private Activity Bonds in connection with

the specific project. To ensure that the inducement resolution satisfies certain legal requirements, it should be drafted by bond counsel.

8. A financial plan is developed by the company and the investment banker, and bond counsel prepares the financing agreement and the trust indenture. The company, bond counsel and the investment banker prepare the official statement. The contents of these documents must be mutually acceptable to all parties.

9. Upon finalization of the above documents, the Inducement Entity adopts a resolution or ordinance authorizing the issuance of the bonds.

10. The various documents are then executed and the investment banker makes payment for the bonds. The bond proceeds are delivered by the Inducement Entity to the trustee.

If you have any questions regarding this information, please contact:
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