
SALT LAKE CITY COUNCIL STAFF REPORT

DATE: August 2, 2002

SUBJECT: **INDUSTRIAL REVENUE BOND APPLICATION FROM
BASIC RESEARCH, LLC**

STAFF REPORT BY: Gary Mumford

CC: Rocky Fluhart, David Nimkin, Margaret Hunt, David Dobbins, LuAnn Clark, Bob Gore,
Dan Mulé

Document Type	Budget-Related Facts	Policy-Related Facts	Miscellaneous Facts
Resolution	The City charges an application fee of \$1,000 and an additional fee if the bonds are sold (\$16,000 in this case) to cover administrative costs for acting as a conduit issuer.	Allowing a private entity to use the City's name for securing tax-exempt bonds is a form of development subsidy.	The City requires a direct-pay letter-of-credit to insure and guarantee repayment of the bonds. Industrial revenue bonds are not considered obligations of the City.

ACTION REQUESTED:

Basic Research, LLC is requesting that the City issue industrial revenue bonds to help the company finance a \$7 million move and expansion of its manufacturing facility from Utah County to the International Center in Salt Lake City. The repayment of industrial revenue bonds relies upon revenue generated by the private entity and is not considered an obligation of the issuing local governmental entity. Basic Research, founded in 1992, currently employs 170 people and plans to increase the number of employees to 218 within one year. The company projects that it will employ about 480 within five years and over 1000 in ten years.

POTENTIAL MOTION:

On June 21, 2002, Basic Research purchased a vacant facility at the International Center and would like to use part of the bond proceeds to reimburse itself for the purchase. For this to occur, the Council would need to adopt a reimbursement resolution within 60 days of the date of purchase. The reimbursement resolution does not commit the City since a public hearing is required and because the company needs to obtain a direct-pay letter-of-credit prior to the Council's approval of the bonds. Following the briefing, the Council may wish to schedule consideration of a reimbursement resolution for the Council's August 13th meeting, which is probably the Council's last opportunity for consideration of the resolution within the 60-day limitation.

The Council may wish to consider the following motion: [I move that the Council] **Adopt a resolution expressing an intent to reimburse certain qualified expenditures with proceeds of an issue of revenue bonds to finance the acquisition, rehabilitation, construction and equipping of manufacturing facilities for Basic Research, LLC.**

MATTERS AT ISSUE:

Salt Lake City requires applicants to secure a direct pay letter-of-credit from a financial institution with at least an AA rating. Under a direct pay letter-of-credit, a financial institution guarantees payments to the bondholders regardless of whether the conduit borrower makes payments to the bank. Basic Research is still in the process of obtaining a direct pay letter-of-credit for the bond issue. If Basic Research is not able to qualify for a direct pay letter-of-credit, it will withdraw its application and the City Council will not be requested to take any additional bond action on behalf of Basic Research. *At the briefing, the Council may wish to ask about the status of the company's efforts to obtain a direct pay letter-of-credit.*

Nonprofit organizations are allowed by IRS regulations to apply directly to a local government, to act as a conduit issuer, for bonding relating to health care or educational purposes. The IRS has set a "volume cap" for each state (\$150 million per year for Utah) for entities other than health care or education that are seeking to finance facilities or equipment through industrial revenue bonds. The Utah Legislature has established priorities for allocating the volume cap with most going to the Utah Housing Finance Agency for first-time single-family homeowners or to college student loan programs. On July 10, 2002, the Utah Private Activity Bond Authority authorized up to \$7 million for industrial revenue bonds subject to City Council approval and issuance.

Resolution 91 of 2001 establishes review criteria for private activity bonds. In addition to the direct-pay letter-of-credit, the applicant is to respond to the follow:

- Will the project have a positive economic impact on the community?
- What social and physical benefits will be realized by the City?
- How many new jobs to be created, at what levels, and at what percentage of the applicant's total payroll will they comprise?
- Does the project contribute to the development of underutilized property in the City?
- Does the project serve unmet needs of City residents?
- Does the project generate synergies for the development of surrounding properties?
- What is the current vitality of the proposed applicant and what impact will the proposed expansion have in the applicant?
- Does the direct pay letter-of-credit ensure terms and conditions that are acceptable to the City?
- Has the applicant's financial performance remained relatively stable for the past three years?
- Has the applicant clearly identified the sources and uses of funds?
- Does the applicant's finance plan identify how the bonds will be repaid?

Basic Research did not address these questions in a concise approach, but answers were found in various sections of the company's application material. Council staff has

summarized the answers beginning on the following page. The City’s application form is being revised so that future applicants will know to address each of these questions.

If the City Council decides to issue industrial revenue bonds, the Council would need to adopt a reimbursement resolution, conduct a hearing under the Tax Equality and Fiscal Responsibility Act (TEFRA), and authorize issuance of the bonds.

ANALYSIS/BACKGROUND:

Industrial revenue bonds (also referred to as private activity bonds) are bonds issued by government and backed solely by the private entity for which the bonds are issued. No real or implied guarantee or obligation is assumed by the City for payment of the bonds. In 2001, the City Council adopted a resolution establishing review criteria for private activity bonds. The one absolute criterion is the guarantee of the bond repayment by a direct-pay letter-of-credit issued by a financial institution with at least an AA rating. The resolution also requested that the applicant respond to the following questions: (Council staff has summarized answers from the applicant’s application in italics following each question.)

- Will the project have a positive economic impact on the community? *Greater tax base since property values will increase. A large portion of the company’s products are manufactured under contract with out-of-state subcontractors. Basic Research plans to bring all of the manufacturing to the Salt Lake City facility. The company projects that purchases from Utah suppliers will increase from \$27 million to \$34 million in one year and to \$77 million in five years.*
- What social and physical benefits will be realized by the City? *Provides local jobs; vacant facility will be occupied*
- How many new jobs to be created, at what levels, and at what percentage of the applicant’s total payroll will they comprise? *Additional permanent jobs as follows:*

<i>Additional Permanent Jobs</i>				
	<i>Current Jobs</i>	<i>Additional Jobs in One Year</i>	<i>Additional Jobs in Five Years</i>	<i>Current Average Annual Pay</i>
<i>Executives</i>	3		1	\$80,000
<i>Professionals</i>	5	12	25	\$60,000
<i>Skilled craftsmen</i>	111	32	142	\$35,000
<i>Unskilled laborers</i>	48		134	\$25,000
<i>Clerical</i>	1	2	4	\$36,000
<i>Services/sales</i>	2	2	10	\$45,000
<i>Total jobs</i>	170	48	316	
<i>Average wage</i>	\$33,572	\$35,250	\$42,850	

- Does the project contribute to the development of underutilized property in the City? *The facility is now vacant.*
- Does the project serve unmet needs of City residents? *Provides additional local jobs.*

- Does the project generate synergies for the development of surrounding properties? *Some of the company's suppliers are also located in the International Center.*
- What is the current vitality of the proposed applicant and what impact will the proposed expansion have in the applicant? *The company estimates that current sales of \$40 million will increase to \$50 million in one year and to \$112 million in five years.*
- Does the direct pay letter-of-credit ensure terms and conditions that are acceptable to the City? *A direct pay letter-of-credit has not be finalized. The company will need to be meet this requirement before the Council will be asked to consider issuing the bonds.*
- Has the applicant's financial performance remained relatively stable for the past three years? *Basic Research has almost doubled revenue in each of the last three years.*
- Has the applicant clearly identified the sources and uses of funds? *The company proposes that the expansion will be financed by the bond proceeds and approximately \$2,500,000 over the next five years from its own resources. The proposed use of funds are: acquisition of building \$4,220,000; renovation costs \$350,000; new equipment \$2,150,000, architect and engineering costs \$30,000; permits \$5,000; bond expenses \$245,000; additional equipment within five years \$2,500,000.*
- Does the applicant's finance plan identify how the bonds will be repaid? *Cash flow projections show significant amounts of net income in excess of bond debt service requirements.*

CHRONOLOGY:

- June 21, 2002** – Basic Research purchased vacant manufacturing facility in Salt Lake City's Industrial Center (5742 W Harold Gatty Drive).
- July 10, 2002** – The Utah Private Activity Bond Authority authorized up to \$7 million for industrial revenue bonds subject to approval and issuance by a local government.
- July 16, 2002** – Basic Research submitted an application requesting Salt Lake City to act as a conduit issuer of industrial revenue bonds.