



City Council Memorandum

City of Arts & Innovation

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TO: HONORABLE MAYOR AND CITY COUNCIL DATE: OCTOBER 3, 2023

FROM: FINANCE DEPARTMENT WARDS: ALL

SUBJECT: SUPPLEMENTAL AGREEMENT TO MASTER PROFESSIONAL CONSULTANT SERVICES AGREEMENT WITH OMNICAP GROUP, LLC FOR ARBITRAGE REBATE AND SWAP REPORTING SERVICES FOR A TERM OF FIVE YEARS – SUPPLEMENTAL APPROPRIATION

ISSUES:

Approve a Supplemental Agreement to the Master Professional Consultant Services Agreement with Omnicap Group, LLC of Delaware, for a term of five years, for arbitrage rebate and swap reporting services for a total amount of \$280,950.

RECOMMENDATIONS:

That the City Council:

1. Approve a Supplemental Agreement to the Master Professional Consultant Services Agreement with Omnicap Group, LLC of Delaware, for an amount of \$280,950 with a 15% change order authority and an expiration date of June 30, 2028;
2. With at least five affirmative votes, authorize the Chief Financial Officer, or designee, to record an increase in revenues and a supplemental appropriation in the General Fund, Debt and Treasury Administration, in the amount of \$14,070 for ad-hoc services.
3. Authorize the City Manager, or designee, to execute the Supplemental Agreement with Omnicap Group, LLC, including making minor and non-substantive changes.

BACKGROUND:

The City of Riverside frequently issues tax-exempt bonds to finance public projects, infrastructure development, and other initiatives. To preserve the tax-exempt status of these bonds, the City must adhere to strict regulations outlined in the Internal Revenue Code (IRC) Section 148, which governs arbitrage rebate compliance. Arbitrage rebate refers to the process by which a municipality or other tax-exempt entity calculates and pays any taxes that may be owed to the U.S. Internal Revenue Service (IRS) on investment earnings generated from the temporary investment or proceeds from tax-exempt bonds.

The arbitrage rebate requirement exists to prevent tax-exempt entities from benefiting excessively from the difference between the interest rates they pay on tax-exempt bonds and the interest rates they earn on their temporary investments of the bond proceeds. If the tax-exempt entity earns more from its temporary investments than it pays in interest on its bonds, it is said to have “arbitrated” the difference, potentially leading to unfair tax advantages. To prevent this, the IRS sets regulations that require tax-exempt entities to calculate whether they have earned more investment income than the amount they would have paid in interest on their bonds. If they have, they must pay the excess amount as a rebate to the IRS. This process ensures that the tax benefits granted to tax-exempt entities are used for their intended purposes and not abused for investment gains.

Arbitrage rebate calculations can be complex, involving factors such as the yield on the investments, bond issuance dates, and the use of bond proceeds. The entity responsible for the bonds must typically perform these calculations periodically, often at five-year intervals, over the life of the bonds. If the entity finds that it owes a rebate, it must make the payment to the IRS. Since the regulations surrounding arbitrage rebate can be intricate, tax-exempt entities often seek the assistance of financial professionals with expertise in this area to ensure proper compliance with the rules.

Additionally, the City uses interest swaps to manage its variable rate debt, requiring diligent reporting under the Dodd-Frank Act and Commodity Future Trading Commission (CFTC) rules. An interest rate swap is a financial derivative contract between two parties who agree to exchange interest payments based on a notional principal amount for a set period of time. The primary purpose of an interest rate swap is to manage or hedge interest rate risk, to reduce borrowing costs, or to achieve a desired interest rate exposure. Interest swap reporting involves providing detailed information about these swap transactions to regulatory authorities or other relevant entities.

DISCUSSION:

To ensure compliance with these complex regulations, it is necessary for the City to engage with a professional consultant who specializes in arbitrage rebate and swap reporting services. As such, on June 27, 2023, the City Council approved Professional Consultant Services Agreements with seven (7) municipal financial advisors to assist with various debt and financial related matters for a term of five years with an option to extend for two additional two-year terms, in accordance with Request for Proposal No. 2261. Omnicap Group, LLC, who currently serves as the City’s Swap and Arbitrage advisor, was the firm awarded to continue providing these services. The current Master Agreement is valid through June 30, 2028, with the option to extend for two additional two-year terms. Within the scope of services of the Master Agreement, Supplemental Agreements are utilized to assign specific projects as needed. At the end of the five-year term staff will bring back to City Council for consideration the optional extensions for the master and supplemental agreements if so desired by all parties.

The City currently has several arbitrage analysis reports due over the next five-years. As new debt is issued, additional arbitrage reports will need to be completed by the financial advisor as well. Additionally, because interest rate swaps are derivative instruments used by the City, the City’s Finance Department Accounting Division and Riverside Public Utilities rely on information from the annual valuation reports to comply with Governmental Accounting Standards Board Statement No. 53 (GASB 53). The report contains information that is used to post journal entries and adjust deferred swaps which are reflected in the City’s annual financial statements. Thus, the City will require assistance with fulfilling its arbitrage rebate and swap reporting obligations to relevant regulatory authorities and stakeholders.

To ensure proper and timely reporting, staff recommends approving the first Supplemental Agreement allowing the City to engage Omnicap's services through June 30, 2028. The scope of services will include the preparation of arbitrage calculations on all necessary bond issuances to determine any rebate liability that may be due to the IRS, monthly updates on mark to market swap valuation reports on all swap agreements, preparation of the annual valuation report, and ad-hoc advisory services.

The Purchasing Manager concurs that this request is in compliance with Purchasing Resolution No. 23914.

STRATEGIC PLAN ALIGNMENT:

This item contributes to **Strategic Priority 5 – High Performing Government**, and **Goal 5.3 – Enhance communication and collaboration with community members, to improve transparency, build public trust, and encourage shared decision-making.**

This item aligns with each of the five Cross-Cutting Threads as follows:

1. **Community Trust** – As one of the City of Riverside's Financial Advisors, Omnicap serves as a fiduciary, providing a specialized, certified level of knowledge and skillset to ensure that the City is aware of all the risks and benefits related to various financing strategies to choose the most financially advantageous course of action for our residents, taxpayers, and ratepayers.
2. **Equity** – Competitive procurement was achieved through RFP 2261, issued January 4, 2023. Of the nine qualified firms who submitted proposals, Omnicap was the only responsive bidder in the Arbitrage and Swap category.
3. **Fiscal Responsibility** – Through the RFP process, the City was able to lock in the rates with Omnicap Group throughout the entire term of the contract. This allows the City to achieve pre-determined rates, regardless of inflation or economic uncertainties.
4. **Innovation** – Utilizing a team of financial advisors is an innovative way for the City to stay on top of current laws and best practices in government finance. The City can rely upon experts in their field to ensure that the City is following various reporting and legislative requirements.
5. **Sustainability & Resiliency** – The City benefits from having a history with Omnicap who has become familiar with the City's large and complex debt portfolio. The historical knowledge of the City's swap agreements and arbitrage requirements is valuable in a portfolio the size of Riverside's.

FISCAL IMPACT:

The total fiscal impact of this action is anticipated to be \$280,950 over the five-year period. Arbitrage rebate and swap reporting services total \$146,000 and \$62,500, respectively and are budgeted as administration costs within the funds of the related bond issuances that have swap and arbitrage reporting requirements. Ad-hoc services are expected to total \$72,450 for the full five-year term. The total for Fiscal Year 2023/24 is \$14,070 and there are sufficient funds available in the Special Deposit Fund – Debt Service Administration Fees account number 0000720-

225087. Appropriations for future fiscal years will be included in the Debt and Treasury Administration, Professional Services account during the budget process.

Source of Funds

Fund	Program	Account	Amount
Special Deposits Fund	Debt Service Administration Fees	0000720-225087	\$14,070

Revenues & Appropriations

Fund	Program	Account	Amount
Revenue			
General Fund	Finance-Debt & Treasury Admin	2302000-374200	\$14,070
Expenditures			
General Fund	Finance-Debt & Treasury Admin	2302000-421000	\$14,070

Prepared by: Karen Hessell, Interim Debt and Treasury Manager
 Certified as to availability of funds: Kristie Thomas, Finance Director/Assistant Chief Financial Officer
 Approved by: Edward Enriquez, Assistant City Manager/Chief Financial Officer/City Treasurer
 Approved as to form: Phaedra A. Norton, City Attorney

Attachment: Supplemental Agreement with Omnicap Group, LLC