

RECOMMENDATION APPROVED;
RESOLUTION 17-8179 ADOPTED; AND
AGREEMENT 17-3354-D APPROVED;
BY THE BOARD OF HARBOR COMMISSIONERS

October 19, 2017

Amber M. Klesges

AMBER M. KLESGES
Board Secretary



Executive Director's
Report to the

Board of Harbor Commissioners

DATE: OCTOBER 13, 2017

FROM: CARGO & INDUSTRIAL REAL ESTATE

SUBJECT: RESOLUTION NO. 17-8179 - APPROVE FOURTH
AMENDMENT TO OPERATING AGREEMENT NO. 15-3354 WITH
HECATE ENERGY HARBORSIDE LLC

SUMMARY:

Staff requests approval of the Fourth Amendment to Operating Agreement No. 15-3354 (Operating Agreement) with Hecate Energy Harborside LLC (Hecate).

Hecate is responsible for financing, developing, constructing, installing, operating, managing, and maintaining photovoltaic solar power systems (PV Systems) for the City of Los Angeles (Harbor Department). Hecate will build the PV Systems on twelve (12) specific site locations (Site Locations) located throughout the Port of Los Angeles (Port) and deliver the power from these sites to the Los Angeles Department of Water and Power (LADWP) pursuant to the terms of certain Power Purchase Agreements (PPAs) between Hecate and LADWP.

Hecate requested the Harbor Department consider various modifications to the Operating Agreement as a result of the development and finance challenges Hecate encountered as part of its planning and financing process. The proposed Fourth Amendment addresses these issues, including but not limited to: redefining "Pre-commercial Operations" as "Substantial Completion" and extending the Substantial Completion milestone date; allows for a one-time series of transfers and delegations, including change of ownership of Hecate, and sub-contracting to two (2) sub-operators controlled by Hecate; provisions delineating "material interference" by City; and other modifications necessary to further align the Operating Agreement with the terms of the PPAs. Further, this Amendment will facilitate the Harbor Department's fulfillment of its obligations under the Agreement with the California State Attorney General.

In addition to the amendment to the Operating Agreement, Hecate requested the consent to a restructure of the ownership of Hecate to facilitate financing of the development from other tax equity partners. The proposed consent addresses this issue.

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RECOMMENDATION:

It is recommended that the Board of Harbor Commissioners (Board):

1. Find that the proposed action is administratively exempt from the requirements of the California Environmental Quality Act (CEQA) under Article II Section 2(f) of the Los Angeles City CEQA Guidelines as determined by the Director of Environmental Management;
2. Approve the Fourth Amendment to Operating Agreement No. 15-3354 with Hecate Energy Harborside LLC and the Consent;
3. Direct the Board Secretary to transmit the Fourth Amendment to Operating Agreement No. 15-3554 and the Consent to City Council for approval pursuant to Charter Section 606 of the City Charter;
4. Authorize the Executive Director to execute and the Board Secretary to attest to the Fourth Amendment and the Consent upon approval by City Council; and
5. Adopt Resolution No. 17-879

DISCUSSION:

Background - On October 15, 2015, the Board approved the Operating Agreement between Hecate and the Harbor Department. The Operating Agreement provides for each PV System to be in service for a term of 20 years on Site Locations that include roofs, parking lots, and other available areas. Under the Operating Agreement, Hecate would procure, install, operate, and maintain PV Systems at up to 12 Site Locations within the Port, which would generate at least 10 MW of clean renewable energy. At this time, Hecate has submitted all design drawings and requested permits from Building & Safety for the installation of six rooftop PV Systems.

In order to fund the installation of the PV systems, Hecate entered into negotiations with True Green Capital Management, LLC, an investment management firm headquartered in Westport, CT (True Green). True Green specializes in funding and financial structuring of alternative energy projects around the U.S. including through the use of self-managed investment funds and so-called "tax equity" investors – investors who can take advantage of Federal tax credits offered to incentivize solar and other alternative energy development. Both Hecate and True Green have placed large sums of money on deposit with LADWP that are at risk of forfeit if the PV Systems are not constructed.

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Due to delays in permitting and complications in obtaining and structuring the tax equity financing related to the terms of the Operating Agreement, Hecate has been delayed in commencing construction. These delays have led to Hecate being in technical default of the Operating Agreement since July 1, 2017. However, since early in 2017, staff has been working closely with Hecate and True Green to work out the terms that will allow financing to close and construction to begin. Both Hecate and True Green have indicated that they will be able to begin construction activity upon approval of this Amendment.

On or prior to signing of the Fourth Amendment, Hecate's parent entity, Hecate Energy LLC intends to transfer one hundred percent of its membership interest in Hecate to USPS LA Solar Holdings, LLC, a subsidiary of investment funds managed by True Green Capital Management LLC.

Summary of Significant Provisions:

The Fourth Amendment will implement the following significant changes to the Operating Agreement:

1. Milestone Extension – The Operating Agreement requires the PV Systems achieve Commercial Operation whereby the PV System is in full operation with Hecate transacting the sale of energy to LADWP by June 2017. The Fourth Amendment modifies this milestone and allows Hecate to achieve Pre-Commercial Operation by the Substantial Completion Date of December 31, 2017. Pre-Commercial Operation is defined as construction of the PV System in accordance with specific conditions, including but not limited to requirements set forth by LADWP and third-party permitting agencies. However, under this revision, Hecate will no longer be required to transact the sale of energy. This modification replicates the Pre-Commercial Operation definition stated in the PPAs and allows for consistency between the departments and their respective contractual terms. The extension also ensures that the Harbor Department remain on track with its commitment to the Attorney General to provide 6.7 megawatts by March 2018.
2. Transfer – Section 9 of the Operating Agreement currently provides that Hecate cannot assign, transfer, or delegate any of its rights, duties, or obligations under the Operating Agreement without the prior written consent of the City but is silent as to change of control. The Fourth Amendment provides the City with more control over who ultimately controls Hecate by requiring Hecate to seek the City's prior written consent if there is a change of 49 percent or more of the ownership interests in Hecate.

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3. Consent – Following the execution of the Fourth Amendment, Section 9 of the Operating Agreement (as amended) will provide that any transfer of 49 percent or more of the membership units of Hecate shall require the prior written consent of the City. Following USPS LA Solar Holdings, LLC's acquisition of all of the membership units in Hecate as outlined above, USPS LA Solar Holdings, LLC proposes to transfer all of the membership interests in Hecate to USPS LA Solar Investment, LLC. USPS LA Solar Investments, LLC is owned by a tax equity partner, G-1 Energy, LLC and investment funds managed by True Green. The City has been advised that the purpose of the transfer of Hecate from USPS LA Solar Holdings, LLC to USPS LA Solar Investment, LLC is to allow the Hecate to access funding from G-1 Energy LLC to finance the development. However, True Green has yet to determine exactly when such transfer will take place. The Consent provides for City's consent to the transfer of Hecate from USPS LA Solar Holdings, LLC to USPS LA Solar Investment, LLC on the following terms and conditions:
 - a. the transfer takes place within 90 days of the date of the Consent;
 - b. Hecate to notify the City in writing within 3 business days of the transfer taking place; and
 - c. if the transfer does not take place within 90 days of the date of the Consent, Hecate is required to seek new written consent from the City for the transfer through action in open public session.
4. Sub-Operating Agreement – The Fourth Amendment grants to Hecate the right to delegate certain of its duties and obligations under the Operating Agreement to two sub-operators, USPS LA Solar FiT "A", LLC ("USPS A") and USPS LA Solar FiT "B", LLC ("USPS B") (collectively referred to as "Sub-Operators"). The Sub-Operators are owned and controlled by USPS LA Holdings, LLC and the delegation is reflected in sub-operating agreements between the Sub-Operators and Hecate and which is attached to the Fourth Amendment as an exhibit. Hecate requested this sub-operating agreement due to a requirement under the PPA's, which also are sub-contracted to these two entities, that the solar energy provider have demonstrated site access and control.

The sub-operating agreement may not be changed without prior Executive Director consent and substantial changes to the Sub-Operating Agreement require prior Board consent. Any future delegation to a new sub-operator is not permitted without prior consent of the Board through action in open public session. Additionally, the sub-operating agreement does not release Hecate from requirements under the Operating Agreement and Hecate remains responsible for performance.
5. City Notice – The Fourth Amendment requires the Harbor Department to provide notice to its tenants, as provided for in standard Harbor Department lease reservation provisions, of Hecate's plans to install, operate and maintain the PV Systems within a respective tenant's premise area.

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6. Best Efforts to not Materially Interfere – The Fourth Amendment requires that the Harbor Department use its “best efforts” to not materially interfere with the PV Systems, i.e., creating or allowing the obstruction of sunlight from Harbor Department-controlled property. Material Interference does not mean the actions of the Harbor Department’s tenants or third-parties, Force Majeure events, projects as a result of CEQA/NEPA, mitigation measures, master plan amendments, court imposed rulings, local, state and federal law, and does not limit the Board’s ability to control or manage the Harbor Departments assets as granted by the Los Angeles City Charter. In the event of a demonstrated material interference whereby the respective PV System is producing less than fifty percent (50%), the Department is required to cure such interference and if the Department fails to cure such interference within three months, the Department and Operator will work to find and relocate the Operator to substitute sites. Such relocation will be seen as a temporary removal and the Harbor Department is required to compensate Hecate, but in no event will such compensation exceed the revenue received by the Department from that specifically impacted PV System over the previous twelve-month period.

Design and Building Status:

All permit requests for the rooftop PV Systems have been submitted by Hecate and have undergone Harbor Department engineering review. Upon approval of this Fourth Amendment, Hecate and True Green are confident they can commence installation on three of the rooftop PV Systems with the remainder to commence as soon as final roofing repairs are completed. Parking lot canopy PV Systems are still under design and review with other permitting agencies and will commence as approval of all necessary permits are obtained.

CONCLUSION:

Approval of this Fourth Amendment to Operating Agreement 15-3354 will allow for financial close with appropriate tax equity investors which is necessary to fund the installation of the PV systems contemplated under the Agreement. Failure to do so will result in the potential cancellation of the Operating Agreement and will further jeopardize the deadlines set forth in the Agreement between the Harbor Department and the State’s Attorney General.

ENVIRONMENTAL ASSESSMENT:

The proposed action is approval of a Fourth Amendment to Operating Agreement No. 15-3354 with Hecate to adjust certain terms and conditions of the Operating Agreement. In accordance with the requirements of the Operating Agreement, environmental review pursuant to CEQA is required for each PV System Site Location at the time the Operator submits an application for Port Project and prior to obtaining all necessary approvals. Therefore, as an administrative activity involving an Amendment to an Operating Agreement, the Director of Environmental Management has determined that the proposed action is exempt from the requirements of CEQA in accordance with Article II Section 2(f) of the Los Angeles City CEQA Guidelines.

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FINANCIAL IMPACT:

The Fourth Amendment will not have any effect on compensation to the Harbor Department. This action only changes the start date of commercial operation. Each PV System will be in operation for a term of 20 years commencing on each Site Location's commercial operation date. As previously disclosed to the Board, annual revenue to the Harbor Department is estimated to be \$146,090, with total revenue over the term being approximately \$2,931,800 for 10 MW.

CITY ATTORNEY:

The Fourth Amendment to Operating Agreement No. 15-3354 and Consent (Transmittal 1) has been reviewed and approved as to form and legality by the Office of the City Attorney.



TRANSMITTAL:

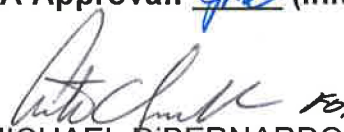
1. Fourth Amendment


JACK C. HEDGE
Director of Cargo & Industrial Real Estate

APPROVED:

 FOR
EUGENE D. SEROKA
Executive Director

FIS Approval:  (initials)
CA Approval:  (initials)

 FOR
MICHAEL DiBERNARDO
Deputy Executive Director

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