

STAFF REPORT

TO: Union Corners Committee

FROM: Union Corners Staff Team (Aaron Olver, Don Marx, Joe Gromacki, Dan Rolfs)

DATE: November 1, 2012

SUBJECT: Union Corners Proposals Staff Report

BACKGROUND

The Union Corners RFP was issued on June 15, 2012, with responses due on July 27, 2012. The City received 5 responses. On August 29, 2012, the Committee placed Gorman & Co. and Livesey / Stonehouse on a short list and directed City Staff to conduct a brief, preliminary financial analysis of the two proposals. City Staff subsequently scheduled face-to-face meetings with both development teams. On September 21, 2012 City Staff sent an e-mail to both development teams asking them to be prepared to discuss the following items:

1. Financing – be prepared to discuss your sources of funding and any contingency plans, should various funding sources such as tax credits fall through;
2. Uses – be prepared to discuss your construction cost estimates, especially for Phase I;
3. TIF Policy – be prepared to discuss applicable TIF policies related to your project (City TIF Policy can be found here:
 - a) <http://www.cityofmadison.com/planning/tidmaps/TIFPOLICY.pdf>)
4. Phase I – Be prepared to discuss in more detail your plans for Phase I, including the sources and uses of funds and any other items that you view as critical.
5. TIF Financing – Be prepared to discuss your team’s TIF request, including a breakdown of how these funds will be applied across phases, why the funds would be needed, value assumptions, rents, expenses, and project costs that impact your TIF request.

Additionally, the RFP states that the Union Corners Committee “will be responsible for evaluating the proposal based on the following criteria.... Economic feasibility of the proposed development”.

The basic financial aspects of each proposal are summarized in the spreadsheet below. City Staff has outlined the Advantages and Disadvantages of both proposals below.

Gorman & Co.

- **Gorman – Advantages**
 1. Experienced Developer
 2. UW Clinic selected Gorman
 3. Not relying on New Market Tax Credits (NMTC)
 4. Investing more cash / equity
 5. Experience with WHEDA Low Income Housing Tax Credits (LIHTC)

- **Gorman – Disadvantages**
 1. **TIF**
 - a) **50% Rule** – City TIF Policy 4.1(8) states that “no more than 50% of the net present value of the tax increment generated by a private development project shall be made available to that project as gap financing”. As shown in the attached spreadsheet, City Staff estimates that Gorman’s request for TIF assistance for the clinic will exceed 100% of the TIF generated. The total TIF request is estimated to be 182% of the TIF generated.

 - b) **Personal guaranty** –City TIF Policy 4.1(12) states that the “City will require a personal guaranty for TIF assistance...” In City Staff’s meeting with Gorman & Co. on Oct 11, 2012, Gorman stated that he is unwilling to provide a personal guaranty as part of a TIF loan. This is a major exception to TIF policy. In the past, the City has rejected requests for TIF assistance that required this exception to policy.

 - c) **Non-recourse Debt** – In City Staff’s meeting with Gorman & Co. on Oct 11, 2012, Gorman stated that he will require non-recourse debt for any TIF assistance that the City may provide. In the past, the City has rejected requests for TIF assistance that required this exception.

 - d) **TID Status** – Union Corners sits in TID #37. The TID does not have excess increment to contribute to any project, including projects that require more incremental revenue than they generate. The TID has expended \$6.2 million on various projects. To retire the \$6.2 million debt will require new developments that create new (incremental) value.

 - e) **Use of Increment from housing to guarantee clinic loan** – Any TIF loan will require that the entire phase (both the clinic and housing) to guaranty the loan. It would be very unlikely for the investors of one project to guaranty the increment from another project.

 2. **Low Income Housing Tax Credits (LIHTC)** – LIHTCs are awarded annually on a competitive basis. If a project does not get LIHTCs, it must either find another source of equity or wait until the next annual round of

funding. It should be noted that LIHTCs are only being proposed for later phases of the project.

3. **Low cap rate** – Gorman used a cap rate of 7.00% in their estimates. A cap rate is a simple way to measure risk. A lower cap rate indicates lower risk, and leads to a higher estimated value. In this case, City Staff believes that a more realistic cap rate would be around 9.00%. This higher cap rate would lead to a lower value and less increment available for a TIF loan.
4. **City to buy grey-box for branch library (vs. land donation)** – Gorman’s proposal provides the City the opportunity to purchase a grey-box condo for a branch library for \$2.1 million. This sets the City on a course to build a branch library facility at this location.
5. **Phased takedown of land** – Gorman & Co is proposing a phased purchase of the land. This keeps the property off of the tax rolls for a longer period of time and eliminates an incentive for the developer to move expeditiously to develop the site.

Livesey / Stonehouse

- Livesey / Stonehouse – Advantages

1. Experienced developer
2. Buying all land (no phasing)
3. Stonehouse's experience with WHEDA's LIHTC
4. Donation of branch library site to the City

- Livesey / Stonehouse – Disadvantages

1. TIF

- a) **50% Rule** – City TIF Policy 4.1(8) states that “no more than 50% of the net present value of the tax increment generated by a private development project shall be made available to that project as gap financing”. As shown in the attached spreadsheet, City Staff estimates that Livesey / Stonehouse's request for TIF assistance for the clinic will exceed 100% of the TIF generated. The total TIF request is estimated to be 67% of the TIF generated.
- b) **TID Status** – Union Corners sits in TID #37. The TID does not have excess increment to contribute to any project, including projects that require more incremental revenue than they generate. The TID has expended \$6.2 million on various projects. To retire the \$6.2 million debt will require new developments that create new (incremental) value.
- c) **Equity investment less than TIF request** – TIF Policy 4.1(7) states, “TIF assistance shall not exceed the amount of equity provided by the Developer. Equity is defined as cash or un-leveraged value in land or prepaid costs attributable to the project.” As shown in the attached spreadsheet, the Livesey / Stonehouse proposal for Phase I does not conform to this policy.
- d) **TIF allocation to housing is not based upon need** – TIF Policy 4.1(6) states, “Each project must demonstrate sufficient need for the City's financial assistance, so that without that assistance, the proposed project would not occur. Every other financial alternative is to be exhausted prior to the use of TIF, including equity participation, other federal and state funds, bonds, tax credits, loans, etc. TIF assistance will be utilized as gap financing. Each project must demonstrate probability of economic success.” Simply allocating a portion of the TIF request to the housing does not conform to this policy.
- e) **Use of increment from grocery to guarantee clinic TIF loan** - Any TIF loan will require that the entire phase (both the clinic and grocery) to guarantee the TIF loan. It is would be very unlikely for the investors of one project to guaranty the increment from another project.

1. **UW Clinic** - Livesey / Stonehouse has not provided strong evidence that UW Clinic will locate at Union Corners should they be selected.
2. **New Market Tax Credits (NMTC)** – The Livesey / Stonehouse proposal includes \$10,450,000 in NMTC financing over the entire project, with Phase I including \$6.75mm for the clinic and \$1.5 mm for the grocery. NMTCs are awarded on an annual competitive basis. If Livesey / Stonehouse is unable to secure the required NMTCs, they will have to find an alternate source of capital. NMTCs are awarded to projects in qualified Census tracts, such as Union Corners. It should be noted that Union Corners is in a qualified, but not highly distressed, Census tract.
3. **LIHTC** - LIHTCs are awarded annually on a competitive basis. If a project does not get LIHTCs, it must either find another source of equity or wait until the next annual round of funding. It should be noted that LIHTCs are only being proposed for later phases of the project.
4. **Low cap rate** – Livesey / Stonehouse used a cap rate of 7.75 – 8.00% in their estimates. A cap rate is a simple way to measure risk. A lower cap rate indicates lower risk, and leads to a higher estimated value. In this case, City Staff believes that a more realistic cap rate would be around 9.00%. This higher cap rate would lead to a lower estimated value, and less increment available for a TIF loan.
5. **Land Price** – The proposed Livesey / Stonehouse land price of \$4.5 mm is low. It should be noted that Livesey / Stonehouse is proposing to donate a site for a branch library back to the City.

Union Corners Staff Report

	Livesey / Stonehouse				Gorman & Co.			
	Total Project	Phase I (Projected Assessor's Value)			Total Project	Phase I (Projected Assessor's Value)		
		Clinic	Clinic Grocery**	Clinic Grocery*		Clinic	Clinic Housing*	Clinic Housing*
Baseline								
- purchase price	\$ 4,500,000	\$ 2,000,000	\$ 3,500,000	\$ 3,500,000	\$ 7,808,400	\$ 1,796,382	\$ 2,796,382	\$ 2,796,382
- TIF request	\$ 5,000,000	\$ 4,000,000	\$ 4,000,000	\$ 4,000,000	\$ 14,800,000	\$ 4,356,000	\$ 4,356,000	\$ 4,356,000
- Cap Rate	7.75% - 8.00%	7.75%	7.75%	9.00%		7.00%	7.00%	9.00%
- Estimated Final Value* (provided by Developer)	\$ 49,577,500	\$ 19,596,774	\$ 26,079,870	\$ 22,458,333	\$ 54,135,270	\$ 25,271,000	\$ 42,138,650	\$ 29,394,478
Est. TIF Increment Revenue	\$ 7,436,625	\$ 2,939,516	\$ 3,911,981	\$ 3,368,750	\$ 8,120,291	\$ 3,790,650	\$ 6,320,798	\$ 4,409,172
50% of Est TIF Increment Revenue	\$ 3,718,313	\$ 1,469,758	\$ 1,955,990	\$ 1,684,375	\$ 4,060,145	\$ 1,895,325	\$ 3,160,399	\$ 2,204,586
% of Available TIF Requested by Developer	67.23%	136.08%	102.25%	118.74%	182.26%	114.91%	68.92%	98.79%

Uses of Funds

- Land	\$ 4,250,000	\$ 2,000,000	\$ 3,500,000	\$ 7,808,400	\$ 1,796,382	\$ 2,796,382
- Construction Costs	\$28,454,000	\$17,685,000	\$ 21,488,000	\$ 55,157,980	\$ 16,768,432	\$ 30,151,658
- Structured / Underground Parking	\$ 6,500,000	\$ 5,740,000	\$ 6,500,000		\$ 5,310,760	\$ 5,310,760
- Permits, Fees, Commission	\$ 1,366,000	\$ 500,000	\$ 900,000		\$ 3,097,078	\$ 4,078,178
- Union Corners Site	\$ 700,000	\$ 375,000	\$ 525,000			
- Overhead / Profit	\$ 1,660,000	\$ 1,000,000	\$ 1,300,000			\$ 1,435,854
- Contingency	\$ 525,000	\$ 250,000	\$ 350,000		\$ 1,992,508	\$ 2,990,014
TOTAL	\$ 43,455,000	\$ 27,550,000	\$ 34,563,000	\$ 62,966,380	\$ 28,965,160	\$ 46,762,846

Sources of Funds

- Developer Equity	\$ 2,050,000	\$ 1,200,000	\$ 1,600,000	\$ -	\$ 4,400,000	\$ 6,228,528
- Tax Credits (NMTC and LIHTC)	\$ 10,450,000	\$ 6,750,000	\$ 8,250,000	\$ 18,067,771	\$ -	\$ -
- Sale of Library Land	\$ -	\$ -	\$ -	\$ 2,124,500	\$ -	\$ -
- Reserves						\$ 997,506
- Deferred Developer Fees	\$ -	\$ -	\$ -	\$ 1,841,455	\$ -	\$ -
- Builder & Sponsor Profit & Risk						\$ 1,435,854
Allowance						
- TIF	\$ 4,000,000	\$ 4,000,000	\$ 4,000,000	\$ 14,817,404	\$ 4,365,160	\$ 4,365,160
- Bank Loan	\$ 26,955,000	\$ 15,600,000	\$ 20,713,000	\$ 47,015,574	\$ 20,200,000	\$ 33,735,798
TOTAL	\$ 43,455,000	\$ 27,550,000	\$ 34,563,000	\$ 83,866,704	\$ 28,965,160	\$ 46,762,846

NOTE: Livesey / Stonehouse numbers do not include Sources and Uses for residential portion of project

*NOTE: Any TIF loan will be based upon increment guaranties

**NOTE: Livesey / Stonehouse may commence housing as part of Phase I. This would have a positive impact on value and potentially decrease their TIF request. At this time, however, staff have no preliminary numbers on a potential housing phase.

		Clinic	Clinic Grocery*
Total Cost		\$ 27,550,000	\$ 34,563,000
Livesey Adjusted Phase I (No NMTCs)	80% LTV 1st Mort	\$ 22,040,000	\$ 27,650,400
	TIF request	\$ 4,000,000	\$ 4,000,000
	Equity	\$ 1,510,000	\$ 2,912,600
	Total	\$ 27,550,000	\$ 34,563,000