DRAFT Minutes

City of Lawrence
Public Incentives Review Committee
November 1, 2016 minutes

MEMBERS PRESENT:	Mayor Mike Amyx, Vice Mayor Leslie Soden Linda Jalenak, Aron Cromwell, Bradley Burnside, and Kris Adair
MEMBERS ABSENT:	County Commissioner Mike Gaughan, Brian Iverson
STAFF PRESENT:	Tom Markus, Diane Stoddard, Britt Crum-Cano
PUBLIC PRESENT:	Several other interested citizens

Mayor Amyx called the meeting to order at approximately 3:00 pm.

The minutes were reviewed. Ms. Jalenak made a motion to approve the minutes from the August 22, 2016 meeting; Mr. Cromwell seconded the motion. The motion was unanimously approved.

Matt Gough, representing the 826 Pennsylvania Street Project, provided details about the project.

Britt Crum-Cano summarized the request for a 10-year, 85% NRA and Industrial Revenue Bond financing in order to access a sales tax exemption on construction materials. She mentioned that the project also included two affordable housing units as part of the project. She coordinated assumptions on the analysis with Tom Jackson from National Development Council (NDC) who worked on the gap analysis. She reported that the current base property tax is approximately $11,000 per year. The cost benefit results were 1.36 for the City, 2.05 for the County and 10.17 for the School District. She did mention that the model likely over inflated the school district return due to the way the state funding formula for schools works. During the NRA period, the improved property would generate 1.88 times the property tax revenues over the current base and this amount grows to 8.26 times the current base once the NRA expires (average over years 11-15).

Mr. Jackson (NDC), briefed the group on the National Development Council, its mission, and explained NDC's approach in evaluating gap financing need for a project. The financing gap is the total project costs minus equity and debt. In cases where project costs are greater than fair market value, it may be a project that justifies the use of incentives. He stated that often the public will question the gap if a developer has cash that could be put into a project. He said that the following questions should be asked 1) Does the developer and partnered investors have the necessary resources to close the gap? 2) Is it reasonable for the Developer to invest enough to close the gap? In the second question, developers must look at cash flow, tax benefits and appreciation while taking into account risk, inflation and opportunity costs. A developer identifies a desired Internal Rate of Return (IRR) and if the projected IRR of the project is less than the desired rate, a gap is created. A gap can be closed through value engineering, public assumption of some project costs (infrastructure, etc.), or other incentives. For the 826 Pennsylvania Project, Mr. Jackson projected an IRR of 9.85% with both NRA and IRB incentives, 8.51% with just NRA incentives, 7.99% with just IRB incentives and 6.98% with no incentives.

Vice Mayor Soden asked about the 6.98% return with no incentives and asked whether that is a reasonable return. Mr. Jackson responded that for some investors, a 6.98% return is acceptable, as in the case with non-profits with certain missions, etc. He stated that he had estimated that now the bank loan is 4%+ and that is projected to increase in the future based on his assumptions. In the future, this makes the return to the developer less. He said that in this case, the property is not in the main part of downtown and based on his review of the real estate in the area, a 10%-12% rate for developers for at-risk capital is not an unreasonable return. Again, the risk associated with the project is key. He stated that there is a reasonableness related to the incentives being requested. Vice Mayor Soden asked when is there a point at which the City does not provide incentives for these projects. Mr. Jackson responded that he imagined there will be projects that will be built without incentives, with those being projects that don't respond as carefully with the built environment and untested product types. He stated that when affordability requirements are added to a project, they can increase the gap, but also meet a community goal.

Mayor Amyx clarified that Mr. Jackson only looked at the 85% level that was in the request. Mr. Jackson confirmed that is what he looked at. He later clarified that he also looked at 50% in his report. He also added that the bank terms were very favorable. He stated that he did a lot of modeling on the project.

Ms. Crum-Cano added several other project considerations that are difficult to quantify in the models. These include the fact that the project provides an opportunity to redevelop an unproductive, dilapidated structure with productive space and infill development. She also mentioned that the Affordable Housing Advisory Board unanimously recommended favorable approval related to the affordable housing units that the project would add.

Mr. Jackson added that a 50% would be 9.03% IRR.

Vice Mayor Soden asked about the 11 full-time positions to be created with the project and whether they would have coverage. Matt Gough responded that a bit over 40% would have benefits. She also asked about the future standards for the affordable units. Mr. Gough responded that the State has a low income tax credit program and their numbers would be utilized to determine annual affordability. He stated that low income housing tax credit reporting could be assisted by a non-profit.

Chuck Magerl, owner of Free State Brewing Company, and Wheatfields Bakery, spoke to the policy issue of whether the project would diversify the economic base or attract unique retail operation and whether the project competes with existing businesses.

Mr Burnside asked if the competing business question was considered on past projects. Cromwell mentioned that was part of the review when the Olive Garden project was being considered. Ms. Stoddard also responded that many of the past projects approved for incentives that included retail were also mixed use and including housing, etc.

There was a question about the internal rate of return of other projects that had been approved for NRAs and if they were around 8%?Crum-Cano mentioned she would need to reference the pro forma analysis for those projects to check the return rate. She stated that for those projects, a return threshold test was applied of two times the risk free rate (10 year Treasury Bonds). Over the past year, the City has subscribed to the quarterly Price Waterhouse Cooper Real Estate Investor Survey and that data was also referenced for return rates other investors were demanding for similar types of projects. Ms. Adair stated she thought that the state's share of the school district's levy can't be overlooked. Ms. Crum-Cano stated that gets to the "but-for test" because it is only if the project proceeds that the revenues and rebates come into play. Mr. Cromwell mentioned that if the project doesn't proceed, both the State and School District continue to get very small tax revenues. Developed, the State and School District will both realize greater tax revenues compared to what the property is currently producing.

Vice Mayor Soden asked what the internal rate of return would be at the 50% level. Mr Jackson stated that gap analysis showed a 9.03% return at the 50% level.

Mayor Amyx stated that he thought that the project brought more than double the existing tax base than the current situation and also provided affordable housing in the area.

Mr. Cromwell stated that the returns need to be considered in terms of the risk associated with getting that return. He stated that investment in an infill project in this manner has risk associated with it and needed to be taken into consideration. Mr. Cromwell stated that the project does meet the policy parameters based on the numbers of the project.

Ms. Jalenak stated that the affordable housing and mixed use aspects of the project were in line and desirable.

Mr. Magerl asked for clarification about the criteria. It was stated in the Technical Report that staff believed that the eligibility criteria was met but that these items were open for some amount of interpretation.

Mr. Gough stated that the project does create mixed use development, will add to the economic climate and enhance the neighborhood as outlined in the policy.

Raymond Hall, 800 New York Street, Apartment 1, suggested offering homeless people a free Greyhound bus ticket to any destination.

Mr. Cromwell made a motion to recommend a 10 year 85% NRA and IRB financing for the 826 Pennsylvania Project and stated that it meets eligibility as outlined in city policy and the staff report. Ms. Jalenak seconded the motion. The motion was approved 4-2, with Kris Adair and Vice Mayor Soden voting against. Vice Mayor Soden wished to add to the minutes that her vote was due to it being more than 50% on the NRA.

Bob Schumm presented his project, Vermont Place, on behalf of himself and his wife Sandra, the applicants. He stated that the project would be on a lot that had been vacant for a long time. It will be a mixed unit project, which has been a goal of the downtown area. He also stated that a goal going back to the 1980s was to add housing units in the downtown area as well. He stated that the project provides for 30 new high tech office spaces, commercial space, residential units, and parking. The project would include one affordable unit. It would be built to a LEED certified silver level. This project will encourage attraction of entrepreneurs and provide justification for a downtown grocery store project.

Ms. Crum-Cano added remarks about the project. The request, based on the gap analysis is for a 75% NRA for 10 years and IRB financing for a sales tax exemption. Staff does believe that the project meets both NRA and IRB eligibility. The current base property taxes are a bit over $7,000 per year. Over the NRA rebate period, the improved property would result in over 6 times that property tax base amount. After the rebate period, the taxing revenues would be greater than 27 times the base amount (average over years 11-15). The City would realize a 1.78 cost-benefit analysis, the County a 2.56 cost-benefit ratio and the school district and the state ratios were not calculated in this case due to no anticipation that the project will result in new students to the community.

Mr. Jackson presented the gap analysis. The projected internal rate of return with NRA and IRB incentives is at 7.94%, with just NRA incentives at 7.23%, with just IRB incentives at 6.36%, and with no incentives at 5.78%. 7.39% would be the internal rate of return for the NRA and IRB incentives at the 50% NRA level. He added that the County appraiser did a very good job to ensure properties are close to market value. He stated that office space brings a good lease rate return to the project and adds to the returns to the developer. He stated that in this area based on his review of vacancy rates, etc. that he would expect a return of 8-10% for a project of this type.

Ms. Crum-Cano added that the project would redevelop long-time vacant lots to productive use, promote density and vibrancy in the downtown, provide an opportunity to support infill development, and add to property tax generation.

Mayor Amyx stated that an important consideration was parking under the building as part of the project. He stated that currently parking is not required at that location. He stated that based on these items, he would look favorably on the project.

Mr. Cromwell stated that designing to LEED silver level is much more expensive and is an important policy goal. He stated that with the incentives there will be a much better project than without the incentives to include the parking. He stated that an 8% return sounded reasonable. He also mentioned the downtown goals this project supports.

Vice Mayor Soden thanked Bob Schumm for looking at the affordable housing and stated that when she votes it will be related to the 50% rebate level but she believes that everything else is great. Bob Schumm added that the 75% rate was determined by the consultant because it makes the project work from a return standpoint.

Mr. Burnside made a motion to recommend the City Commission authorize a 10-year, 75% NRA and IRB financing. Jalenak seconded the motion. The motion passed 4-2 (Adair and Soden against.)

Motion was made to adjourn by Vice Mayor Soden and seconded by Ms. Jalenak. Meeting adjourned at 5:01 pm.