MORAN BLUE RIBBON COMMITTEE

FINAL REPORT TO BURLINGTON CITY COUNCIL

JULY 12, 2010

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Overview of Work Performed

On April 26, 2010 the Burlington City Council passed a resolution to appoint a Moran Blue Ribbon Committee (MBRC or Committee) and gave it the following charge:

1) Review the proposed financing structure of Moran and assess it in terms of:

    A. How it protects and insulates the taxpayer in the event of an unexpected downturn or development.

    B. What other financing alternatives are available and if all options have been evaluated and assessed to see if there is a more appropriate model.

    C. Assess any financial risks associated with the project.

2) Discuss and evaluate the need to review the proforma, business plan and model, projections, feasibility study (if applicable) marketing plan and other financial data of the proposed tenants to assess:

    A. The potential for success for fundraising, if applicable, and other methods of raising capital in the private sector.

    B. Whether the business plan and other data is realistic and what the data relies on or is dependent upon.

3) The members of the Committee shall work in a prudent, careful and expeditious manner, while maintaining confidentiality of any proprietary information of the prospective tenants, as well as any information related to tenant negotiations.

It was not the task of the MBRC to evaluate the overall concept for redevelopment of the Moran plant. The Committee's main focus was the current financial structure of the existing project. Whether or not this is the only viable option for the redevelopment of Moran was not within the Committee's scope or responsibilities.

The Committee convened its first meeting on May 25, 2010 and has met formally as a committee six times. Those meetings were as follows:

May 25- One-hour and forty-minute meeting to review the Council's Charge and an overview of the current project.

June 1- Two hour and twenty minute meeting to review the Sources and Uses of Funds, Construction estimates, Tax Increment Financing and the Risk and Mitigation report.

June 8- Two hour and forty minute meeting to review financial structure utilizing Historic Tax Credits and New Market Tax Credits.

June 15- Two hour and forty-five minute meeting to review operating pro forma, components of projected Development Agreements, and to discuss information required from prospective tenants.

June 22- Two-hour and forty five-minute meeting to review the updated Sources and Uses budget, Project Labor Agreement status, TIF district debt capacity, negotiations with tenants, and preliminary list of risks, mitigations and benefits discussed to date, and the potential cost to tear down the Moran plant as opposed to its development.

June 29- Two-hour and forty-minute meeting to discuss the project's risk, potential mitigations and potential benefits. The formal meeting was followed by a discussion among the Committees members regarding the preparation of the final report to be submitted to the City Council on July 12, 2010.

City Council President, William Keogh, encouraged the Committee to complete its deliberations within a five-week timeframe. This precluded the committee from hiring outside firms to assist in the evaluation of the work done by the City's Community and Economic Development Office. We did utilize the expertise of the real estate investment advisory firm, White + Burke Real Estate Investment Advisors, Inc. retained by the city to assist in the development of the project. Every effort was made to challenge the assumptions imbedded in the information we received and to objectively review the project's risk to the City of Burlington taxpayers.

Acknowledgement

The Chair would like to thank the members of the committee for their tireless efforts, their attendance and participation at each meeting and the objectivity, which they displayed throughout the process; if they were for or against the Moran project, the Chair never detected it.

The Committee would like to thank CEDO, City staff and consultants for their responsiveness to our need for information, their frank comments to tough questions and their overall balanced presentation of the facts, risk and benefits of this very complex project.

The Committee further wishes to thank the super-human effort of David G. White of White + Burke Real Estate Investment Advisors, Inc. In six weeks he tried his best to make us experts on the Moran redevelopment. His responses to our need for information were timely and complete.

To all who took their time to sit through this process with us, we thank you.

Executive Summary

The following report attempts to respond to each of the City Council directives outlined in the resolution passed at their April 26, 2010 meeting. The Committee focused its work on the identification of the major risk areas and possible mitigation of each risk. In some cases sufficient information was not available to ascertain the level of risk. In these cases the Committee makes recommendations as to what information should be obtained before moving forward.

The Moran project is best described as a community development as opposed to a commercial development. A similar size commercial development is often financed through infusions of owner's equity and a reasonable amount of debt from a financial institution. A community development project normally is not financed through traditional means relying instead on a myriad of grants, government bonds or other government debt instruments, tax credits and fund raising activities. The Moran Redevelopment Project must use all of these non-traditional vehicles to successfully finish the project. We conclude that traditional financing would not be a viable method to redevelop the property as it is currently designed. The Committee focused its attention on the inherent risk within the project's scope. A summary of the major risks are:

- **Environmental Contamination Risk:** The Moran Plant is a brownfield site. Phase I and II environmental assessments have been completed. Remediation and clean-up are ongoing and receive direct oversight from Vermont DEC and the USEPA. Storm water controls are incorporated into the current project plan. The committee did not look at source documents (many of which are on the CEDO website) but relied on representations made by the City's employees, attorneys and consultants. We believe the City has addressed the environmental contamination risks. We would not recommend closing on the proposed financial structure however, until the City's attorney is satisfied that all remediation plans have the appropriate state/federal approvals.

- **Permit Risk:** The Moran plant is in the Public Trust Special Overlay District, which limits its use. The building is a "grandfathered" non-conforming structure, and, due to its height, size and proximity to the waterfront, will require a Major Impact Review and, specific permits from various City, State and Federal jurisdictions. The Committee recommends that construction contracts and financial closing commitments not be executed until all zoning, environmental and land use permits have been secured.

- **Construction Risk:** As with any project, there are financial risks associated with the redevelopment of the Moran Plant, including potential cost overruns due to inadequate budgeting, scope, and/or quality changes and hidden conditions, and the failure of the contractor(s) to complete the project. The Committee reviewed the design development construction cost estimates, and proposed increases in several reserve categories, which have been incorporated into the financial plan. A new design development construction cost estimate is in process, based on the most recent revised plans. The Committee recommends that a second cost estimate be independently prepared based on the same plans and any significant differences between the two be reconciled before moving forward with the final construction plans. To reduce the financial exposure during construction all contractors must be bonded.

- **Financing Risk:** The Committee focused a majority of its attention on the complex financial structure of the proposed Redevelopment. We did not look at conventional financing options, recognizing that this project would not work utilizing traditional commercial financing alternatives. There are four major financial components of the proposed plan:

  -The City will use incremental tax revenues from the Waterfront **Tax Increment Financing** district (TIF) to pay the debt service on a $2.1MM loan from Housing and Urban Development under their section 108 program. The repayment of this debt will not come from the project, but will be paid out of projected excess revenues within the TIF. The Committee reviewed several income and expense projections for the TIF and concluded that the TIF, once the Marriot expansion and the new hotel on Cherry St. are complete, could generate sufficient excess tax revenues to service this debt.

  -The project will require **additional debt to be paid from TIF revenues** of up to $6.6MM to complete the redevelopment as proposed. The TIF district (the City) will borrow the money. Repayment of the loan will be the responsibility of the TIF district, not the project. Analysis of the existing borrowing capacity of the TIF district indicates that the TIF district will support this additional debt at current interest rates. The amount of additional borrowing by the TIF district could be reduced to $4.9MM if the tenants fully participate in two other major sources of funding: Historic Tax Credits (HTC) and New Market Tax Credits (NMTC). The Committee determined that the total current borrowing capacity of the TIF (once the Marriott expansion and the new Cherry St. hotel have been fully taxed) could support the additional borrowings. We support the City's recommendation that the project will close on all major components of the financial funding concurrently to insure that adequate funding is available before moving forward with the development.

  It should be noted that the "city" takes on this additional TIF financed debt, and hence the taxpayer is ultimately responsible should the TIF district not achieve the projected level of revenues. While conservative assumptions were used in the TIF projections and any potential shortfalls are mitigated by projected surpluses from the Moran project itself, it can't be made risk-free. Unless further development occurs in the TIF district, the city will be using most of the district's projected incremental property tax surplus revenues in order to service the new debt. Although most of the incremental tax funds being used to service the debt will be monies that would otherwise have gone to the State, the City and its taxpayers should recognize that they will be forgoing potential use of the City's portion of these funds for other purposes.

-A third source of funds is the sale of **Historic Tax Credits** (HTC). The project will be applying for Federal Rehabilitation Investment Tax Credits valued at $1.3MM based on qualified rehabilitation expenses of $6.6MM. These credits will be sold to private investors and the proceeds used to fund a portion of the development cost. The project will be applying for state historic tax credits, but the proceeds from their sale, should it occur, have not been included in the budget. Should the federal tax credit program not be available to Moran, the project would have to obtain alternative funding sources. We reiterate that the project should close on all major components of the financial funding at once to insure that adequate funding is available before moving forward with the development.

-The final major component of the funding is the issuance of federal **New Market Tax Credit** (NMTC). This is a relatively new tax credit program, which was passed by Congress to encourage economic development. It is a very complex program administered by the Department of the Treasury. Similar to HTCs, investors in eligible tax credit projects receive a federal tax credit equal to 39% of a project's total eligible cost. Unlike HTCs the transaction cost are extraordinarily high due to the complexity of the program. If the tenants agree to include their fit-up cost in the total eligible project cost it could generate $5.8MM in NMTC net of transaction cost. This is a critical piece of the financing and as mentioned above the City should close on this transaction at the same time the other major financing components are secured. If NMTCs are not available to the City the project should not move forward. Replacing this part of the financial package with debt is not advised.

-There are a myriad of other **smaller funding sources**-third party grants and project subsidies exceeding $1.5MM that have been awarded to date. We did not verify the existence of these sources, but based our analysis on assurances from City employees that they are available. The combination of all these funding sources, assuming they are all available to the project, would more than cover the projected development cost. The City provided us with several financing scenarios that combine some but not all of the above funding sources. In the worst case scenario the project, based on projected development cost of $16.2MM would have a shortfall in funding of $344,000. The Committee recommends that even in this case alternative funding be obtained to cover this shortfall before moving forward with the project.

- **Tenant Performance Risk**: The area that is the most tenuous is the projected performance of the tenants. Although the Committee met in executive session to determine the viability of the proposed tenants, we could not determine the tenants' ability to raise adequate capital to meet their obligations for startup and fit-up expenses based on the information we reviewed.

The two non-profits' ability to meet the financial requirements are subject to the completion of successful fund raising capital campaigns. The City should monitor the two non-profits' fundraising goals and performance of the fundraising campaigns to gauge their ability to raise the required capital for their portions of the project. Furthermore, the City should continue to review and evaluate the reasonableness of the non-profits' business plans for their operations at Moran.

The major tenant, a private commercial enterprise based in Europe, has not provided any meaningful financial information to the City. A major development of this size would normally attract a "credit" tenant, such as a publicly traded company whose financials are readily available to the landlord. The Committee can appreciate the prospective tenant's reluctance to share private information, but we would not recommend moving forward without the City adequately reviewing their financial records. In the event the information provided is not sufficient for the City to be confident in the capacity of the tenant to raise the capital necessary for their startup and fit-up costs and the reasonableness of their business plan, we recommend that the City require a Letter of Credit from qualified financial institution or other financial surety sufficient to guarantee financial performance of the tenant during the redevelopment/construction phase of the project.

The City has structured this project so that the tenants' success is not critical to the project's success. As mentioned above the TIF and not the tenants will pay the project's debt. Tax credits from the project will continue to flow to the investors should one or more of the tenants fail, so long as the City does not violate the terms of the tax credit agreements. That said, the Committee feels strongly that every effort should be made to insure that financially viable tenants occupy the building at the outset of the project. We recommend that the City complete its due diligence on the tenants before entering into lease agreements. We further recommend that the City not close on the major components of the financing, nor commit to the construction until such time that this work is complete.

- **Operating Proforma:** The committee reviewed several operating pro-formas, including a breakeven analysis of the Moran plant once the construction is completed and the tenants have occupied their space. The information was reviewed in an Executive Session of the board. Premature disclosure of that information could affect the lease negotiations with the tenants. The operating expenses seemed reasonable for this size building. The lease income required to reach breakeven seemed reasonable for the available leased square footage of the building. In conclusion the Committee is confident that the building can generate sufficient revenue to cover its expenses provided that the tenants have the capacity to meet their lease obligations.

As mentioned above, the Committee did not have sufficient financial information from the tenants to determine if they, collectively, have the capacity to meet their lease obligations. The Committee recommends that the City complete a financial analysis of the major tenant to determine its ability to fund operating losses during their initial start-up sufficient to meet its lease obligations. The Committee did review pro-forma financial information on the operating plans of the major tenant. This alone is not sufficient information to ascertain where resources could be procured should the major tenant experience losses during the start-up period. Lacking adequate financial information we recommend that the major tenant provide a letter of credit, or other adequate financial surety which could be drawn on by the City in the event the major tenant does not meet their lease obligations during the first two-years of operations.

- **Risk of Inaction:** The Committee realizes that certain funding opportunities may be lost if we don't proceed with Moran since these funding mechanisms are not easily used for other city projects (New Market and Historical Tax Credits, the HUD loan, and certain grants the project have already received). If a suitable redevelopment of Moran does not happen the City will be faced with the demolition of the structure, which we were informed will cost several million dollars. The TIF district has been given a five year extension by the State with regard to the use, by the district, of the additional taxes generated within the TIF district. Recognizing the redevelopment of Moran has been in the works for over twenty years, there is some question as to whether or not the City can develop a new alternative plan within the next five years.

  The redevelopment of the northern part of the Waterfront for both economic and community development purposes is an important source of future tax revenues for the City and its taxpayers. An important first step will be the development of the adjacent project referred to as Waterfront North-an asset that will enhance the Moran redevelopment. We hope our findings assist the City in helping Moran become a viable community asset.

Moran Plant Ownership

The voters in Burlington made it clear in a number of referenda that the Moran Plant property was an asset to the city and that the city should retain ownership and not sell to a private developer. The basis of the subsequent proposals for the site all have been with the goal of the city retaining ownership and the property becoming an asset to the Waterfront and to the City as a whole.

That said, due to the structure of the financing with regard to the New Market Tax Credits, the building must be held by a non-municipal entity for the duration of the holding period. This is explained in greater detail in the section of this report explaining New Market Tax Credits and quoted here:

"Within this scenario, the City council should understand that the property must be held by an arms-length holding company that is established to own the building for the 7 year period in which tax credits are generated to investors. The City will relinquish ownership of the building during this period (while retaining ownership of the underlying land). NMTC could allow this to be either a non-profit or a for profit corporation with an independent board of governance but the use of the historic preservation tax credits… will require it to be structured as a for-profit corporation".

During this time, Moran will generate property taxes on the entirety of the building. When the New Market Tax Credit holding period has expired, the property will revert back to the city and will continue to generate taxes on the for-profit portions of the building.

During all this time the City will be responsible either through the Parks and Recreation Department or some other City Department for the upkeep and maintenance of the building and the grounds.

The risks to the taxpayer at every point in the ownership of the building seem to remain the same regardless of the actual ownership of the building. The revenues generated by the tenants will pay for maintenance of the property.

Environmental Risks to the Moran and surrounding area:

As part of the "MBRC" work over the last several weeks the one area that appears to have the least amount of realistic concern or risk is the environmental issues that surround the proposed Moran Redevelopment project. One could easily surmise that while a power plant facility in operation until it is was decommissioned in 1986 could and would pose many challenges and obstacles environmentally the City and CEDO has done its due diligence and ensured that the site poses little risk at this current time. For over two decades the building has largely been dormant aside from the use of a small portion of the building on the North West side by the sailing center.

The Moran building is a steel frame and masonry structure constructed in 1954 by the Burlington Electric Department. It is built on fill that was placed between the 1850s and 1950s, and was previously used as a rail yard and, before that, for lumber processing and storage

In 2005 The Phase II Environmental Site Assessment was done and elements of that test include the following : 1) installation of six soil borings/groundwater monitoring wells surrounding the existing building and on the grounds; 2) surveying of the soil boring and well locations; 3) an interior building survey to assess the presence of asbestos containing materials and lead paint; 4) sampling of the soil from two different intervals for analysis of several contaminants; 5) sampling of the groundwater for analysis of several contaminants; 6) validation of the soil and groundwater analytical data; and 7) reporting.

This report concluded that with new or redevelopment construction most issues would be addressed or remedied in the work that followed or levels of lead paint and asbestos were well within acceptable levels for a Power station located at the site.

In 2006 Waite Environmental Management (WEM) conducted more Brownfield's testing of the Soil Quality and Ground Water Quality. This test concluded that there are no significant contaminant concerns in the deeper soil (5'- 44' depth) under the Site aside from the "Hot Spots" where coal had been stored for a great number of years. The City took steps to cover and fill these spots where over time this area's coal concentration would dissipate and pose no further risk to the soil or Lake Champlain.

The City has been awarded a $1 million BEDI grant through the U.S. Department of Housing and Urban Development (HUD) one of just seven projects chosen nationally under this highly competitive program that promotes the redevelopment of abandoned industrial sites. BEDI grant funds must be used in conjunction with a HUD "Section 108" federally-guaranteed loan, which is a financing tool for cities to invest in economic development projects. HUD has preliminarily approved a $2 million Section 108 loan for Moran, to be paid back with proceeds from the Tax Increment Financing district. Much of these funds have been used to ready the Moran Structure for future re-development or at the very least allow for the building to be left dormant without posing any significant risk to the surrounding waterfront and Lake Champlain itself.

In closing The City and CEDO has done its work to remedy any environmental concerns that resulted from the operation of a Power Plant on this site. Since its decommissioning and over the last decade the Risk to future generations has been minimal at best.

Construction

The relative risk exposure for the proposed project, while not substantial, is not low. There is a potential for hidden, or as yet unidentified, conditions to emerge during the demolition, environmental review and renovation processes. The proposed project consists of renovations within the former Moran Power Plant, which is located on a former industrial site which was originally created by filling in a portion of Lake Champlain. The site is considered a "Brownfield" site, and is known to contain what is currently considered to be manageable levels of hazardous material contamination.

The scope of the project according to the most recent plans available, prepared by Freeman-French- Freeman Architects, dated May 13, 2010, consists of interior renovations, "core and shell" improvements and newly constructed additions to the Moran Plant to create "shell space" earmarked to house several tenants. The tenants will be responsible for their own fit-up. A small portion of the facility will be occupied by Burlington's Parks department. The project also includes site improvements associated with a skate park and public space immediately north of the Moran Plant, as well as a new public entrance addition and related work immediately to the east of the Moran Plant. Other improvements related to the project include the construction of new surface parking lots and road relocations which will be handled as a separate project by the Burlington Department of Public Works. The Sailing

Center is planning to directly fund and construct a new building north of the Moran Plant which will house training and boat storage facilities.

The most recent revised design development plans, dated June 4, 2010 total approximately 43,528 gross square feet of space to be renovated and constructed to yield the following gross usable spaces:

- Ice Factor: 16,154 SF
- Parks and Recreation and Community Rooms: 4,319 SF
- Lake Champlain Community Sailing Center: 7,408 SF
- Lake Champlain Maritime Museum: 3,226 SF
- Public Circulation and Service Space: 12,421 SF

To date, design development level documents have been completed. Design development cost estimates were prepared by DEW Construction Corp., dated January 11, 2010. Pizzagalli Construction Company is in the process of completing a new design development construction cost estimate based on the June 4, 2010 plans.

Several studies have been undertaken to evaluate the existing building's structure and site and to validate suitability for the proposed adaptive reuse of the building. Other studies have been completed to evaluate the site's geotechnical features and assess environmental and hazardous materials conditions. None of the studies completed to date have identified any unmanageable risk. The building's structure, dating to 1954, will require some upgrades and retrofitting to meet current building code requirements with respect to structural and seismic standards.

Risk Analysis:

As with any project, there is some financial risk exposure associated with the renovations of the Moran Plant, including potential cost overruns due to inadequate budgeting, scope and or quality changes and hidden conditions.

Budget- The budget prepared to date estimates the total cost of the project for design and construction to be $15,871,124 excluding tenant fit-up, and other construction to be performed by the Department of Public Works.

- The budget includes contingencies for design evolution, bidding errors and hidden conditions. Specifically there are several contingencies in the budget:
    - 5% (of the construction estimate) for a design contingency intended to reflect the potential of minor scope and quality changes during the design evolution and estimating corrections as more detailed design information is made available;
    - 7.5% (of the construction estimate) to deal with potential hidden conditions identified during construction; and
    - 10% (of project costs) to cover any changes or additions to the project as design and construction are completed – otherwise referred to as an owner's contingency.

It is recommended that an escalation allowance be established at 2% of construction costs to compensate for any price increases for commodities, such as steel, copper and other price sensitive construction materials, which may occur prior to securing construction contracts.

The budget for soft costs appears adequate but the budgets for owner testing and inspections are contained within the construction budget. The amounts specified may not fully reflect the needed testing and inspection requirements. These expenses should be included in the owner's budget.

- Construction Cost Estimate– The largest cost risk to the project, other than outright scope changes, hidden conditions, or commodity cost increases as discussed above – relates to how accurately and completely the construction documents reflect the scope of work. Proper document coordination between the core and shell design team is essential as well as coordination with the tenant's fit-up scope of work. The cost estimators and eventually the bidding contractor will only estimate what is on the drawings, so if scope is missing or unclear, change orders and claims could result.

  The construction cost estimates prepared by DEW were performed using a typical and industry standard format and methodology. The estimates were based on drawing prepared by Freeman-French-Freeman, dated December 2, 2009. The construction cost estimate includes a number of lump sum estimates and allowances for miscellaneous site scope, demolition and building repairs. In addition, there is an assumption that "winter conditions" will not be required. To the extent that these cost assumptions are not refined and validated during design development they could pose some moderate cost risk.

  It is unclear if the estimates to date contain any assumption about the project's expected labor components. Typically, a cost estimator will factor in an expected labor rate assumption. There has been some discussion about the use of a "Project Labor Agreement" (PLA) for the project. While a competitive bidding environment may mitigate any cost impacts associated with a PLA, cost estimates at the design development phase should reflect this labor rate assumption which could be impact construction costs by approximately 5%.

- Hidden Conditions- the Moran Plant and site do present a potential for discovery of hidden conditions that may be revealed as construction and building structural upgrades and repairs are executed. Reasonable due-diligence has been completed to indentify potential risks. But given the nature of the site, building and structure all potential risks cannot be eliminated.

Risk Mitigation and Recommendations:

- Cost Estimates: It is recommended that the cost estimates completed to date be reconciled. This typically occurs at various stages of a project's design and most importantly at the conclusion of the design development phase of design. The process consists of having two estimators (typically construction or professional estimating firms) complete separate cost estimates using the same design development documents.

They then compare and reconcile the differences between the two estimates. This is useful in clarifying design intent and for identifying missing or unclear scope as well as variances in materials quantities and unit costs. Ideally, a target of reconciling the estimates within a 5% difference between the estimates is established. Any variances between the two estimates are evaluated and reconciled.

- Construction Manager: It is recommended that a qualified Construction Manger (CM) be retained for "pre-construction services" prior to the completion of the construction documents and final cost estimates. They can assist with the final site and building analysis and scope definition, prepare cost estimates and render valuable advice as to how to approach and complete the construction and renovations.

- Design Completeness and Coordination: It is recommended that a process be put in place to review and manage document coordination within the construction documents. This process typically involves the design team and the CM, as a pre-construction service, prior to the issuance of bidding documents with the goal of ensuring the drawings are complete, coordinated and that the contractor can construct the project in conformance to the architect's design intent. This process should be extended to evaluate the coordination between the "core and shell" and tenant fit-up documents.

- Bid Acceptance Contingency: It is recommended that construction contract award(s) be contingent upon bids coming in within budget. However, if for some reason the project does not move forward it is likely the City would need to reimburse the CM for pre-construction services rendered to date.

- Bidding Coordination: As a part of the Construction Management Contract it is recommended that the CM assume all risk associated with coordinating bid documents. They will likely be developing independent bid packages for different trades and therefore must assume the responsibility and liability for scope coordination during the bidding process.

- CM and Major Sub-Contractor Bonding: It is recommended that the CM and major sub-contractors procure performance and completion bonds for the total construction value of the contract.

The greatest risks to the project will be the emergence of hidden conditions due to the site and buildings structure and the coordination of the tenant's fit-up with the core and shell design.

The project team has completed substantial pre-project due-diligence. The site is easily accessible and has adequate areas to stage for construction activities, which will ease contractor mobilization concerns. The project has a strong and experienced design team in place and the design development documents appear comprehensive and complete, not withstanding the lack of tenant fit-up information. These factors taken together with the recommendations above will reduce overall financial risk associated with the project's construction.

Permitting

With respect to environmental and land use permits the relative risk exposure to the proposed project is low. Pre-permit due-diligence undertaken by the project team has thoroughly examined permitting requirements. City Staff and the project's consultants have complete relevant project reviews and have maintained ongoing dialog with the various permitting agencies during the planning and design development process to date.

- The project site resides within the Downtown-Public Trust district. The proposed uses of the Moran Plant conform to allowable uses permitted within the Public Trust district.

- The Moran Plant is a "non-conforming" structure as defined by the current zoning ordinance; however it is expected that that the building with the proposed improvements will be "grandfathered". The project will require to be viewed under the "Major Impact Review Criteria" as mandated by the existing Zoning Ordinance. The Development Review Board must be satisfied that the project meets statutory criteria for a conditional use within the district.

- The project will require a permit from the US Army Corp of Engineers for waterfront improvements associated with the Sailing Center's docking and hoisting operations. Permitting will also be required due the filling of about 12,000 square feet of wetlands to the north of the Moran Plant that were created when the former tank farm ceased operations and was decommissioned. It is possible the project may be required to undertake offsetting improvements to restore or improve water quality protective features on or near the site.

- The project will require a state-issued Storm Water permit as well as approval of a storm water and erosion management plan detailing pollution control and management measures to be taken during and after construction to mitigate potential storm water run off and soils erosion from the site.

- The project has been preliminarily reviewed and endorsed by the Vermont Division for Historic Preservation. The design team has also worked throughout the design process with the National Park Service office, which is required to approve the designs as being in conformance with the Secretary of the Interiors Standards for Historic Rehabilitation in order for the project to qualify for historic preservation tax credits. The plans were submitted and City staff has received verbal notification that the design has been approved.

- The project has been reviewed by the District 4 Environmental Commission's Coordinator with a finding that no Act 250 Land Use permit will be required for the proposed project.

The project team has worked with the City's Zoning and Planning staff throughout the planning process to ensure the project addresses and meets current City permitting requirements. Initial and required project reviews have been completed or are underway by the City's Technical Advisory Committee, Design Review Board, and the Conservation Review Board in preparation for consideration of the project by the Development Review Board which begin in early August of 2010. While the project will undergo continued permit reviews, no major permitting issues have been identified to date and the remainder of the permitting process should proceed and be concluded in a typical manner without any anticipated complications. However it is recommended that construction contracting and financing closing commitments not be executed until all zoning and related permits have been secured.

Project Labor Agreement

A Project Labor Agreement is a common document used in large construction projects around the country and specifically with publicly funded projects. A PLA is a set of standards most commonly set around labor and working conditions issues that often require contractors who bid on the project to use of local workers, set certain minimum wage standards, and abide by other working conditions that benefit the public interest. PLAs can be designed based on the specific needs of a project, such as Moran. To date, one private PLA has been used in Vermont for the Champlain Bridge (2010), which will include the use of local labor.

In December of 2009, the City Council passed a resolution encouraging the city to abide by responsible contractor provisions (such as a PLA) when financially possible with the Moran Project in order to support our local workforce and provide additional economic development in area. In order to determine if a Moran Project PLA is financially feasible and in the public's interest, it is recommended to conduct a feasibility study based on the use of local labor and other minimum working conditions, such as contracts who work with affiliated apprenticeship training programs. Once completed, it can be determined if there are significant additional costs associated with using a PLA and whether it is prudent to use a PLA on the project.

Tax Credit Mechanisms

A critical factor in the assessment of the financial viability of the Moran Redevelopment plan is evaluating the relative risks of the various sources of funds to support redevelopment. Current project estimates including contingencies estimate total uses of $16.215M to redevelop the building. These estimates are inclusive of the building construction and surrounding park but do not include tenant fit up the access road or and parking facility development. Sources of funds projected total $15.871 M and do not require tenant participation.

The sources of funds are comprised of 4 basic categories:

- Third party government grants and subsidies. These include EPA and Vermont Brownfields remediation programs and CDBG grants totaling a projected 1.5M in funding. There is relatively no risk associated with these instruments as they have been awarded and are available to the project.
- City of Burlington funds. These include the existing sunk costs of acquisition from many years ago, and a mix of allocated capital and general funds totaling just under $700K. There is no risk in these funding sources.
- Tax Credit Equity instruments. The two instruments considered for funding are New Market Tax Credit Equity and Historic Preservation Tax Credit Equity. Both of these instruments have administrative costs and mandate holding periods- 7 years and 5 years, respectively- where funds must remain in the project and not be used to repay debt. These sources total $4.9m in a fully funded scenario. While not determined to present high levels of risk, they are complex and critical to the success of the funding formula.
- Debt incurred by the City of Burlington. There are two instruments: an already approved HUD section 108 Loan for $2M and additional borrowing within the existing Tax Increment Finance district (TIF) contemplated as $6.6M. The section 108 loan was part of an approved BEDI (Brownfields Economic development Initiative) grant and repayment has been authorized by the City. The TIF borrowing history and the City's ability to support additional borrowing is explored below.

There is a potential shortfall between sources and uses of $344K over the life of the project. This is not judged to be a significant gap as it could be absorbed by various identified sources, including an applied for and not yet awarded State of Vermont Historic preservation tax credits of up to $510,000.

It should be noted that with the passage of legislation at the state level in the 2010 session that authorized the City to incur new debt in the TIF district, the need for tenants to participate in the redevelopment of the shell of the building and be "quasi partners" in development was removed, a very positive development for the project. This opportunity to pursue TIF borrowing is a game changer that makes the funding formula viable as TIF borrowing will represent close to 42% of the financing package.

One of the essential questions to be answered in this funding scenario is: but for the existence of this financing plan as contemplated, could the redevelopment of the Moran Plant proceed or would it proceed in a less desirable and materially different manner? And, what risk could this present to the taxpayers of the City?

The ability for the City to incur additional TIF debt within the 5 year period beginning January 1, 2010 combined with existing and projected surpluses of incremental tax revenues within the district creates a unique set of circumstances for funding to support this project. This set of conditions may not exist at any time in the future and is time sensitive, as there is a window for borrowing. Hence, but for this set of conditions, this redevelopment as contemplated may not occur.

As to the risk of the financing mechanisms and their combination to the taxpayers, it should be known that the financing formula involves multiple sources that must align in order for the package to come together. While none of the sources can be judged as "risky" unto itself it is this sequential complexity that must be considered and carefully monitored by the entities that will eventually control the redevelopment project. As is also stated, there are risks inherent in the escalation of costs, as there may be with any project of this nature.

Every effort should be made to identify risk at all times and develop mitigating strategies in order to protect the taxpayer from impact over the life of this project.

What follows is a summary of the Tax Credit Equity and TIF instruments as they are relatively challenging to understand and create a level of sequential complexity for the project.

New Market Tax Credits

This should be recognized as the predominant go/no go factor for the project. This is the first sequential step in the financing formula that must be met in order for the project to go forward.

The New Markets Tax Credits (NMTC) program was established by the US Congress to attract debt and equity investors to invest capital in qualified projects in eligible low income areas. The Moran Plant falls into one of the designated census tract areas. The types of business investments eligible under the NMTC program are very broad, and the currently proposed uses at the Moran plant are eligible. Projects can be undertaken by either for profit or not for profit organizations.
Criteria and components of a model NMTC project include:

- Capital requirement of $2- $30M, met by Moran
- Strong economic development and/or community impact such as the project acts as a catalyst for larger or additional development; met by Moran
- Environmental sustainability and beneficial impacts, such as the reuse of existing or historic structures; met by Moran
- The deal must allow for "substantially all" (85%) of the capital to stay invested in the project for the entire 7 year tax credit period. This is met, although debt service is taking place for the project during this period and is funded through other sources than the equity generated by these credits.

The tax credit program provides an incentive to investors in the form of a 39% federal income tax credit for investing their capital. Essentially, the financial mechanism allows for the aggregation of all project funding sources into a large "bucket" that is run through the tax credit program. In the case of Moran, it is contemplated that $21- $30M will be aggregated. The sources are:

- $16.2M from project sources (see sources and uses). This is inclusive all 4 categories mentioned above, with the net of the TIF and net equity generated by this program in the bucket.

- $3.5M from the Waterfront north roadway and parking improvements project. These developments are adjacent to Moran and have secured funding sources; they can be included because of their existence within this census tract and close association with the Moran project.
- $2.1M of transaction costs for NMTC are included, which although a portion of this is paid out later in the 7 year cycle can be used to contribute to the whole during the tax credit period.
- Possibly, $9M in tenant fit up funding is included; this is the variance between $21M and $30M running through this program. Should the tenants be able to complete capital campaigns and meet closing deadlines, there is a means that exists to later credit a reduction in their rent basis which repays their participation.

It is the participation of the tenants in the aggregating stream that later determines the total TIF borrowing requirements. If they participate, TIF borrowings could be $4.5M; if not, they would be targeted at $6.6M. This is relevant in that the City Council should consider the total amount of forgone revenues by the taxpayers.

In very simplified terms, what transpires in the NMTC vehicle is:

- Funds are aggregated to a lump sum
- Tax credits are offered by the federal government to investors
- Investors participate, purchasing those credits typically at a range of 67 to 72 cents on the dollar on the face value of the credits
- A federal tax credit of 39% is generated to the investor over a 7 year period
- The property must be held by a holding company during the 7 year life of the tax credits.
- Administrative fees are collected by the sponsoring entities, the federally appointed “allocatees” which are typically non profit agencies.

It should be noted that transaction fees are relatively high at an estimated $2M to participate in this vehicle. These are paid for through the life of credit by the investor’s funds.

Within this scenario, the City council should understand that the property must be held by an arms-length holding company that is established to own the building for the 7 year period in which tax credits are generated to investors. The City will relinquish ownership of the building during this period (while retaining ownership of the underlying land). NMTC could allow this to be either a non-profit or a for profit corporation with an independent board of governance but the use of the historic preservation tax credits (discussed below) will require it to be structured as a for-profit corporation.

The overall transaction will generate a targeted $3.9M in equity for the project if the tenants do not run their startup and fit-up costs through the structure and up to $6M if the do.

The program became available in 2003 and has two typical beneficiaries:

1. the projects that get funded through the equity produced by investors in these credits
2. The non profit organizations that are the “allocatees” or federally appointed sponsors of these projects.

Factors that could affect the value if the tax equity generated that should be taken into consideration:

- Could be affected by the rate that investors want to pay, in terms of the total value of the credit that can be generated. Should the rate be below the 67% threshold, it might not generate the necessary equity and could be a non starter for the project.
- At the very least, $20M needs to run through this facility in order for the rest of the formula to work, in particular to not exceed the ceiling for TIF borrowing.
- Should this facility not be used, there is no identified replacement and either the project would not go forward or would need to go forward in a materially different way that reduced the overall refurbishment costs.

And in general, while this is a federally supported program it is somewhat complex to understand.

The risk of participation in the facility would be deemed low, the complexity considerable.

Historic Preservation Tax Credits

Historic preservation tax credits are much easier to understand and fairly straight forward. There is little risk associated with these other than a required 5 year compliance period which may run concurrent with the 7 year NMTC holding period. The project is pursuing both a federal and state historic tax credit but relies only on the federal in the funding model.

The requirements for federal historic tax credits are:

- The project must be on the national register. The Moran plant has applied and expects to be approved.
- Tax credits are given for up to 20% of qualified rehabilitation expenses of a building. The estimate for these qualified expenses is $6-7M yielding an estimate $960K in net tax equity to the project after transaction costs. Unlike NMTC, there is no aggregating- simply, what you spend on rehab can be considered for credit factoring.
- Since tax credits are available to investors in the first year, they typically pay an estimated 90% to 95% of the face value of the tax credits. This is favorable for the project, as it generates a relatively high return quickly.
- The building cannot be sold during the 5 year payout and compliance period.
- At minimum, 50% of the leasable space must be occupied by for profit enterprises. As this is determined by square footage occupancy, the project qualifies. A risk factor could be the permanency of the tenancy of the Ice Factor. Should they not be a tenant at any time during the 5 year period, the space would need to be released or held for releasing only to for-profit tenant There are limiting factors on the type of business being operated by a for profit tenant determined by the Public Trust doctrine.

Together, these credits are fundamental to the project and do present some cash flow timing issues where there are possible projected shortfalls from the project in years 6 – 8. These have been mitigated through other strategies, one of which is establishing a robust reserve fund to cover these costs.

Burlington's Waterfront TIF District

The essential nature of a TIF is:

- Infrastructure improvement is desired within a district, with the belief that when the infrastructure improvement takes place private development will follow. This will allow for increased assessment and valuation of the property.
- A base level of value is established, on which the City will continue to generate and collect property and education tax revenues that will flow to the City and state.
- The incremental value of the property created an increment of tax revenues, and those revenues are dedicated to the repayment of the debt incurred to fund the infrastructure improvement. Following repayment of debt, the total tax proceeds of the property revert to the City and state.
- During the debt repayment period, City and state taxpayers forgo these revenues for other purposes as they are dedicated to repayment.
- It should be noted however, that as with any TIF district, the ultimate responsibility for repayment of debt should the district not be able to generate all funds reverts to the City and thus, the taxpayer. The scenario contemplated has been vetted using conservative assumptions.

Established by the City Council in January of 1996, 58% of City voters ratified a referendum that authorized the City to borrow for infrastructure development projects in March of 1996. The City Council and voters should refer to maps that outline this area which is accessible on the CEDO website.
To date, $16.8M has been borrowed to complete projects such as:

- Lake Street reconstruction, which leveraged the re-development of the Hilton Hotel, the construction of the Marriott Hotel and a planned and approved development at 41 Cherry Street.
- Acquisition of the Urban Reserve
- Lakeview parking garage construction, which leveraged re-development of the Burlington Town Center
- And others

There was a resolution by the City Council in April of 2010 that directed CEDO to consider TIF financing as a part of the Moran Redevelopment project.

It is estimated that the valuation of all properties within the TIF district have increased from a base assessment of $42.4M in 1996 to more than $119.5 M today. A key factor in the Moran Redevelopment financing is that the current properties within the district are creating a surplus of incremental tax revenues which will be dedicated to repayment of Moran debt. This does represent potential revenue that could revert back to the City and State after current debt repayment is satisfied, and prior to incurring new debt. The City Council should recognize this as foregone revenues.

Extensive financial analysis was performed to test the capacity of the Waterfront TIF district to support new debt with the following key variables taken into account:

- The amount of municipal property taxes retained by the district, currently .4415 cents within this district, and an allowable possible approved increment of .712. This establishes that the current retained increment rate is substantial enough and there is potentially additional available increment in the rate calculation.
- Assumptions were made regarding background growth of this tract and municipal and educational tax rate growth. All three of these will contribute to revenues generated. Background growth is conservatively estimated at .2% annual. The relationship for the education and municipal rates is relatively simple: as they increase, more property tax is generated. Education tax rates increases in the City are factored at 3% versus the experienced 7.5 % (homestead) and 5.8% (non homestead) over the past 5 years. The municipal rate was factored at .75% growth versus actual of 1.57%.
- Planned additional developments within the district include the addition of rooms at the Marriott, and the build out of a hotel property at 41 Cherry Street which will both contribute to increased valuation and therefore, more incremental TIF revenues. Assumptions here are about the completion plan dates which in the conservative estimates bring these properties as tax producing entities on line starting in 2010 through 2013. Moran Plan completion and increased valuations would be on line and complete by 2013.
- The post development value of the Moran Plant was also taken into account, increasing from roughly 900K to 4M at completion. There is a timing nuance to the generation of tax revenues, as property taxes are collectable in the first 7 years of the life of the building (due to NMTC for profit holding company) and thereafter, property tax revenues are paid by the for profit tenants only for the life of their tenancy.

Based on the above variables, it is calculated that the TIF district could sustain and carry $7.5M more debt over the course of its debt repayment schedule through 2025. Incremental property tax revenues from Moran plus current and projected surplus property tax revenues would be used to pay off both the Section 108 Loan ($2M borrowed) and the new TIF borrowings with a range of $4.5M to $6.6M, for a total of $8.691M in additional debt and $16.6M in repayment on a 15 year schedule.

A summary of current+ future revenues and obligations is as follows:

	Revenues	Debt
Current	30M	17.4M
New Marriott	1.3M	
New 41 Cherry	4.4M	
New Moran	962K	
Background	290K	
New 108 loan repayment		3.4M
TIF 6.6M repayment		13.2M
TOTAL	37.2M	34M
Variance + possible		3M

The analysis does demonstrate that the revenues possible can exceed debt payments.

It is important to iterate several items:

- TIF borrowing could range from a low of $4.5 M to a high of $6.6M based on the participation of tenants in the NMTC aggregating facility. The assumptions for the model are conservatively that the tenants do not participate and $20M runs through the NMTC facility, generating $3.9M in tax equity to the project, which would require $6.6M TIF debt. This is demonstrated to be feasible by this model.
- The change by the legislature is a "ticking clock" and new TIF debt must be incurred within the 5 year period starting January 1, 2010. Should delays to the project extend beyond the 5 year window, TIF would not be available.
- Taxpayers and the City must accept that these are forgone revenues. Should there be additional pressures on the city for funding of various other priorities, these incremental new and incremental surplus funds will have already been committed to retire debt to support the redevelopment of Moran.

Tenant Risk

Every landlord wants good, solid, financially stable tenants for their rental property. The City of Burlington wants no less of its tenants at the new Moran Center. The principal partners with the city in this venture, after some reshuffling, are The Ice Factor, the Lake Champlain Maritime Museum and the Community Sailing Center.

The Ice Factor is the anchor tenant of the venture. The company is a Scottish based company founded in 2002. Although the company appears to be successful based upon its European facilities already in operation, the Committee, because of the condensed period of Committee review and the non-public nature of the company, was unable to obtain financial statements showing a current balance sheet or income statement. The city will need to obtain additional financial information and suitable financial guarantees on The Ice Factor to ensure that the company is stable and can viably take on the fit-up of the Moran space. Because of the significant cost of the fit-up and the necessity of payment of funds in advance of construction to maximize tax credits, third party guarantees, e.g. Letters of Credit or similar guarantees, need to be obtained by the city when entering into final contracts. Letters of Credit are perhaps more common in commercial trade situations where parties are unknown to each other, or where one party has poor or unverifiable credit, requests the purchaser to provide a guarantee to the seller that the necessary funds for the transaction will be coming forthwith. Under the circumstances, without verifiable financial information or a significant outlay of cash as a down payment from The Ice Factor, the city would be well advised to obtain a Letter of Credit to ensure that the company fulfills its commitment.

After the Green Mountain Children's Museum decided not to continue discussions for space in the center, the space was allocated to the Lake Champlain Maritime Museum. The museum, which was founded in 1985, is currently located in Basin Harbor in Vergennes, VT. The museum is widely known for its Nautical Archaeology Center.

The third and final tenant is the Community Sailing Center. The Center provides educational and recreational access to Lake Champlain through camps, sailing instruction, boat rentals and storage, and a variety of social activities. In addition to the occupying and fit-up of the Moran plant building, the Sailing Center has embarked on another simultaneous, separately funded project, a new free-standing storage and classroom building. The projected cost of the new storage and classroom building is $1,330,000, with another $400,000 for dock and waterfront improvements.

The Lake Champlain Maritime Museum and Community Sailing Center will both require significant fund raising campaigns to raise funds for their respective fit-up and separate construction expenses. Both organizations have expressed that they are fully capable of raising the needed funds to meet their commitments and are in the process of engaging well-known fundraisers to assist in their campaigns. The City Council will have to monitor the activities of the Maritime Museum and the Sailing Center as their fund raising activities proceed. The city should set benchmarks and specific crucial reporting dates to ascertain if sufficient progress is being made for the non-profits to meet their commitments.

The city estimates that the Ice Factor will need to commit some $4 million dollars, the Maritime Museum $2.4 million and the Sailing Center $2.3 million. Although the project has the ability to continue if all the tenants do not fully participate in New Market Tax Credits it would require additional borrowing on the part of the city. The City Council will be required to evaluate the progress of the fund raising campaigns and the guarantees of The Ice Factor before construction begins.