EHLERS
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Memo

To: Ryan Schroeder, City Manager
Jim Hartshorn, Community Development Director

From: Stacie Kvilvang and Keith Dahl, Ehlers

Date: December 4, 2019

Subject: Kmart Redevelopment Project – Analysis of TIF Request

The EDA received an application for public financial assistance from Dominium requesting approximately $6.5 million of Tax Increment Financing (TIF) assistance in the form of a pay-as-you-go (PAYGO) TIF Note over a 20-year term. Dominium has proposed to construct a 232-unit affordable senior apartment and a 137-unit, non-age restricted affordable apartment at 50 Signal Hill Center, West St. Paul, MN (the "Project"). Construction would begin in the spring of 2020 with an anticipated project cost of approximately $99.4 million (taxable value of $46.125 million).

We conducted a review of the Project, specifically Dominium's budget and pro forma based on industry standards for construction, land acquisition, and project costs; as well as ensured all revenues, and expenditures have been appropriately accounted for and considered.

A TIF estimate was prepared to determine the potential amount of increment that could be generated from the Project. Based upon an estimated market value of $125,000 per unit provided by the County Assessor's office, the Project would generate a total present value (principal amount) of approximately $6.1 million. This figure assumes a financing rate of 5%.

Based on our review, the Developer's requested financial assistance is more than what is necessary for the Project to become "financially feasible". We've concluded that the Project would only require 12 years of assistance totaling $3.282 million.

The tables below provide a synopsis of the sources and uses associated with the Project:

SOURCES	Amount	Pct.	Per Unit
First Mortgage	54,837,027	55%	148,610
TIF Mortgage	3,282,000	3%	8,894
Tax Credits	33,078,914	33%	89,645
Deferred Developer Fee (100% of Total Fee)	8,160,856	8%	22,116
TOTAL SOURCES	**99,358,797**	**100%**	**269,265**

USES	Amount	Pct.	Per Unit
Acquisition Costs	6,365,000	6%	17,249
Construction Costs	69,221,820	70%	187,593
Professional Services	2,758,800	3%	7,476
Financing Costs	1,925,455	2%	5,218
Developer Fee	8,160,856	8%	22,116
Cash Accounts/Escrows/Reserves	10,926,866	11%	29,612
TOTAL USES	**99,358,797**	**100%**	**269,265**

Pro Forma Analysis:

Overall, the information contained in the development pro forma generally meets the expectations of a rental housing project utilizing 4% low-income housing tax credits (LIHTC) and other sources of public financial assistance.

1. **Acquisition Costs** – The proposed land acquisition cost of the Project is approximately $17,250 per unit. This figure is higher than what we expected to see for this area. We would expect to see a market range of $8,000 to $12,000 per unit for similar development projects of its type in this area. However, this is the negotiated price with the current property owner. The City and Dominium met with them to request a reduction in the price which they were not willing to do.

2. **Total Development Costs (the "TDC")** – The TDC is approximately $99.4 million or $269,000 per unit. Multi-family apartments in this market generally range between $225,000 and $275,000 per unit so this Project is within the market range even though it is pushing the upper limits.

3. **Developer Fee** – The proposed developer fee is approximately 8% of the TDC, which is within the typical industry range of 8-10% for LIHTC projects. Dominium is limiting its fee and deferring 100% of it to close the financial gap. Instead of Dominium being compensated upfront for the time and resources spent to develop the Project, they will be paid out of available cash flow. **Currently, it is anticipated to be repaid within 11 years. After its repaid, the Project is expected to have a net cash flow of over $1.4 million. This is one of the main reasons why we recommend limiting public assistance to 12 years.**

4. **Rents** – All of the units will be affordable to households at or below 60% of the area median income (AMI). The 2019 rent limits are noted in the table below. The rent and income limits are derived by the United States Department of Housing and Urban Development (HUD) on an annual basis, and the 2020 rent limits will not be released until April of next year.

Maximum Gross Monthly Rent

Bedroom Size	60% AMI
One Bedroom	$ 1,125
Two Bedrooom	$ 1,350
Three Bedroom	$ 1,560

5. **Operating Expenses** – The operating expenses on a per unit basis for the Project is approximately $3,500, which is in the middle of the typical market range of $3,000 to $4,000 per unit per year. Please note that this per unit expense is before management fees, property taxes, and replacement reserves.

6. **Management Fee** – The proposed management fee is 2.0% of the effective gross income of the Project. This is lower than the typical range of 3% to 5%.

7. **Reserves** – The annual deposit to replacement reserves is $300 per unit per year, which is typical for LIHTC projects.

8. **Financing** – The Developer has maximized the First Mortgage for the Project. The mortgages require debt coverage of 115% to ensure that revenues generated will be adequate to repay them. In review of Dominium's debt coverage, they will achieve a 118% with TIF assistance in year 2.

9. **Low-income Housing Tax Credits (LIHTC)** – The Project anticipates tax credit pricing of $0.95 for every $1.00 of available tax credit, which generates approximately $33 million of proceeds for the Project. Tax credit pricing on many current projects is between $0.85 and $0.95. Based on current conditions, the assumed tax credit equity is within expectations.

Recommendation:

Based on our review of Dominium's pro forma and under current market conditions, the proposed development may not reasonably be expected to occur solely through private investment within the near future. The cost associated with development of the Project is only feasible through public financial assistance from the City. We conclude that TIF assistance in the amount of $3.282 million over a term of 12 years is supportable for this Project.

It should be noted that Dominium disagrees with our recommendation and is requesting the EDA to consider providing 15 years of assistance totaling $3.98 million. As mentioned above, after the deferred developer fee is paid off in year 11, the net cash flow is expected to be over $1.4 million. If the additional 3 years of assistance is provided, Dominium's net cash flow in each subsequent year will be in excess of approximately $2 million per year. **For this reason, we maintain our recommendation of 12 years totaling $3.282 million.**

Please contact either of us at 651-697-8500 with any questions.