



Office of the Comptroller

June 23, 2005

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Alderman Michael S. D'Amato
Chair, Zoning, Neighborhoods & Development Committee
City Hall Room 205
Milwaukee, WI 53202

RE: PabstCity - Questions

Alderman D'Amato:

In a recent meeting to discuss the proposed PabstCity Project, you raised a number of questions for which a written response was requested from our Office. Enclosed is our response to these questions.

Should you have any follow-up questions on this matter, please contact me.

Sincerely,

W. Martin Morics
Comptroller

Cc Members of the Zoning, Neighborhoods & Development Committee
Commissioner Richard Marcoux
Joel Brennan
James Scherer

Alderman D'Amato Questions Re PabstCity Project

1. Question: "Economic forces including Park East development are likely to increase the value of the current PabstCity site even without PabstCity. Given this assumption, what compound growth rate for the current PabstCity property would have to occur to equal the projected property value of the PabstCity development in the projected year of the PabstCity TID's retirement?"

Response: Given the projected PabstCity taxable value of \$241,530,000 in the year 2027 (projected year of TID closure for a \$41 million TID) compared to a base TID value of \$9,833,000, the **property within the proposed TID 58 boundaries would have to increase at an annualized rate of 15.7% to reach the same property value by 2027.**

2. Question: "Assuming CHJC's report is correct, about 50% of the aggregate retail sales generated by PabstCity will be sales new to the area. The remainder will result from a shift in sales demand from existing area retailers to PabstCity. Assuming only new sales are counted at property tax increments, how many years would be required to successfully retire the TID issued for the PabstCity Project?"

Response: Capitalizing (or valuing) the PabstCity retail development based on a net income approach, a linear relationship between tax increments generated and sales is assumed. In turn, about 50% of the development is retail (the remainder being office and residential). Given the above, about a 25% reduction in tax increments (50% of 50%) would result for the entire PabstCity development if the CHJC Report regarding retail sales is correct and only *new* retail sales generate property tax increment.

Given this assumption, the proposed TID would generate annual property tax increments averaging about \$1 million below the projected \$3.1 million - \$4.6 million annual projections in the TID S.B. Friedman Feasibility Study. **With this reduced property tax increment as a result of counting only retail sales new to the area, the TID would not be able to successfully retire the \$47 million debt obligation within the 30 year maximum legal time limit.**

3. Question: "Using an average of the last five years as a limit for future TID spending over the next five years, how many years would a competing TID project using City General Obligation (GO) borrowing have to be deferred in order to accommodate the PabstCity Project?"

Response: During the period 2000 through 2004, \$75.0 million of General Obligation TID borrowing authority was adopted, for an average annual TID GO borrowing of \$15 million. Including capitalized interest, the TID GO borrowing for the PabstCity Project will total about \$47 million. Therefore, using the past five years as a guide, the PabstCity Project consumes just over three years of City TID GO borrowing capacity. **If the City set a policy to not exceed its past average of \$15 million in annual TID GO borrowing over the next five years, no other City GO financed TID projects would be able to be started for three years.**

4. Question: “What is the expected internal rate of return (IRR) to PabstCity investors based on the City providing the requested \$39 million grant? How does this return compare to similar projects the City has supported?”

Response: The S.B. Friedman Feasibility Study identifies two sets of private investors, each with its own set of cashflows and expected returns. These are Juneau Avenue Partners, LLC (the Developer) and “Outside Investors”. The Friedman Study (page 4) projects the returns to each set of PabstCity investors for a 10 year investment period, assuming the development is sold in year 11. Both the Developer and Outside Investors are also projected to receive 10% “cash-on-cash” returns for the first six years of the Project, then increasing from years 7-10. This means that investors are expecting to get a strong, immediate year payback on their investment, without having to wait years before a return is realized. The projected 10 year (IRR) returns are as follows:

- **Developer 20.3%-23.1%**
- **Outside Investors....14.2%.**

Friedman indicates that the 23.1% IRR and 10% cash-on-cash returns “... appear to be at the aggressive (insert high) end of the spectrum, particularly in terms of early year cashflows...”. However, Friedman adds that “...the overall returns indicated by the developer fall within ranges that have been observed in the market.”

Regarding projected returns for similar City TID projects, there really isn’t a development project which was closely comparable to PabstCity. However, here is a sample of projected internal rates of return for other City TID projects having some similar components:

- TID 37 Grand Avenue – Marshall Fields Renovation
 1. Office Tower/Suites.....15.7%-18.9%
 2. Retail.....20.4%
- TID 37 Grand Avenue – Boston Store Renovation
 1. Retail(Bostco/Wispark return).....4%¹
- TID 42 Midtown Phase I..... 7%-9%²
- TID 51 Granville Station.....10% cash-on-cash

Juneau Avenue Partners, LLC, the developer for PabstCity, derives a higher return than its outside investors, but the vast majority of equity investment (\$51 million) is intended to come from outside investors. **Based on the above imperfect comparisons, the proposed 10% cash-on-cash return and the 14.2% ten year returns to the outside investors seem reasonable. The 20%-23% ten year returns to the developer are on the high side according to S.B. Friedman, but relate to a much smaller investment (about \$5 million) and reflect the substantial risks associated with this Project.**

¹ Wispark was willing to accept a below market return in order to complete the project financing.

² Development fees for Phases I (\$1million) and II (\$1.7 million) as well as the proceeds from the sale of the development would supplement this projected return.

5. Question: "What are the specific purposes for which the proposed \$41 million TID is to spent?" "How large would the PabstCity TID be if it only included City infrastructure improvements?"

Response: From the draft PabstCity Term sheet 5/4/05:

Public infrastructure improvements	
streets, sidewalks, lighting, sewer, water, etc.....	\$16 million
Site remediation and preparation; interior demolition.....	\$14 million
Rehabilitation of existing historic structures.....	\$ 9 million
City administered job training & RACM administration.....	\$ 2 million
TOTAL.....	<u>\$41 million.</u>

6. Question: "It is my understanding that the proposed PabstCity Block 2 parking garage is being financed independent of the City's TID financing. It is also my understanding that New Markets Tax Credits which could be allocated to the City portion of PabstCity to lower the City's required contribution were instead allocated to the Block 2 parking garage. Please confirm."

Response: As shown on page nine of the S.B. Friedman Feasibility Study, New Markets Tax Credits were allocated to the Block 2 parking garage. **As of 4/29/05, the amount of New Markets tax credits allocated to this garage is \$1.95 million.**

7. Question: "What are the five largest active TIDs the City has approved up to this point?"

Response: Based on our brief review, here are the five largest active TIDs approved by the City of Milwaukee:

1. **TID 49 - Cathedral Place \$23.3 million (financed City owned parking structure)**
2. **TID 48 - Park East III \$20.0 million (public improvements, freeway demolition cost overruns)**
3. **TID 5 - Theatre District \$20.0 million (Milwaukee Center)**
4. **TID 37 - Grand Avenue \$19.3 million (multiple projects)**
5. **TID 22 - Beerline "B" \$16.7 million (multiple projects).**