CITY OF BLOOMINGTON MINNESOTA

Request for Council Action

Originator	Item
Port Authority	**South Loop Waterpark - Progress Update**
Agenda Section	Date
	Thursday, January 31, 2019

Requested Action

City Council motion made by ____________, seconded by ______________ to direct staff to continue to analyze and perform due diligence for the waterpark ownership and financing model outlined herein and bring a Development Services Contract for consideration of approval

Port Authority motion made by ____________, seconded by ______________ to direct staff to continue to analyze and perform due diligence for the waterpark ownership and financing model outlined herein and bring a Development Services Contract for consideration of approval

Item created by: Schane Rudlang, Port Authority Administrator

Presenter: Schane Rudlang, Port Authority Administrator

Description

Summary

On March 6, 2018 City Staff and representatives from Triple 5 (T5), owners of Mall of America (MOA), updated the City Council and Port Authority on the status of development for future phases of MOA. The focus of that meeting was on the potential to develop and construct a large indoor waterpark, which would be connected to Mall of America. At that time, Staff and T5 were exploring a number of different ownership and financing structures for the waterpark, including one where the City would own and issue debt for the project, and use revenues from the waterpark to pay for the waterpark's debt payments. In the aforementioned financing model, which is not currently being studied, Bloomington residents would not have been at financial risk for the project. Work continued in the summer and fall of 2018 to find an ownership and financing model where the City and Port are not the owners during the financing period; this included numerous staff and developer meetings, and extensive legal analysis. On November 1, 2018 staff presented a proposed waterpark ownership model utilizing a nonprofit owner that is not the City or Port; the Council and Port directed staff to continue studying the ownership model outlined. On January 31, 2019 staff will present a further refined version of the nonprofit model.

Quick Facts about the Waterpark Project

1. Bloomington property taxes are not put at risk with this project.
2. The City will not own, operate or finance the project at the time of construction. Ownership would transfer to the City after 30 years, or sooner if the debt is paid off earlier.
3. Estimates of benefit to the community include an additional $1M in admissions taxes, as well as an incremental increase in lodging tax revenue.
4. Mall of America is not enriched in this project structure. The waterpark will be owned by a non-profit entity not related to Triple 5. Excess revenues flow to pay off the project debt, not to the nonprofit ownership nor the waterpark manager.
5. Poor performance by the waterpark (lower attendance than projected) would not create direct financial exposure for the City. The financial performance is back-stopped by ARBLs (alternative revenues by legislation; admissions, food/beverage, lodging and sales taxes that get turned on) that are limited to Mall of America property and would be paid by MOA visitors.

Background

The original construction of the 4.2 million sf Mall of America in 1992 was modeled in some ways after the 5.3 million sf West Edmonton Mall (WEM) in Canada, which was built starting in 1981 with three subsequent phases that were completed in 1998. WEM has an amusement park and a 215,000 sf indoor waterpark. In many ways, T5 and the City learned what worked well and what could be improved upon from the earlier construction of WEM. The same is true with MOA expansion – we can learn what works for future phases of MOA, including learning from their waterpark experience at WEM. While WEM is sprawling and has dead ends reminiscent of Southdale's corridors, MOA was built as a circle with the amusement park in the middle. One major component of WEM that brings vibrancy and attracts around 500,000 people annually is a waterpark. In the continually evolving retail environment, diversification of the mall/retail experience is necessary to continue to keep malls economically healthy; this diversification can take many forms, but largely it is the addition of entertainment options. A waterpark connected to MOA would be a big draw and amenity, not only to Bloomington, but to the region.

MOA is important to the City of Bloomington in many direct and indirect ways. Directly, MOA is about 10% of the City's property tax base, creates admissions taxes that are deposited into the City's General Fund, and also accounts for about a third of hotel room nights booked in the City, which translates into lodging taxes that are deposited in the City's general fund; these revenues directly lower property taxes. The City would benefit by collecting existing and in place admissions taxes from the new waterpark in an amount estimated to be about $1 million annually, and new lodging taxes created by the room nights generated from the waterpark (through new or extended hotel bookings) estimated to be $200,000 to $400,000 annually; these new general fund revenues would more than offset the $150,000 to 200,000 in City property taxes that would not be collected since the project would be exempt from paying them due to the ownership and use status. The City stands to benefit from the project during the first 30 years through the collection of these added lodging and admissions taxes, and then once the debt is paid off in year 31 the City would benefit by receiving the excess revenues from the waterpark directly.

A waterpark has been part of the expansion plans for MOA for many years. Where and how to build the waterpark has evolved. The current plan is to construct the waterpark directly north of MOA, attached to MOA's north front door, and in the space east of IKEA in what is now a parking lot (see attached layout map). The building footprint would be around 250,000 sf, the main pool hall being 215,000 sf, and the total area around 335,000 sf. These dimensions will fluctuate depending on the budget, and the budget is dependent on projected revenues – so the design of the size, amenities, and rides/slides is an iterative process. However, an indoor waterpark of this size would be the largest or second largest indoor waterpark in North America.

The displaced parking would be moved into a parking structure. The parking structure would be built in such a way to allow the conversion of the structure into another use (e.g., office, residential, etc.) should parking ratios decrease in the future due to autonomous vehicles, increased transit use, and/or continued growth of ride sharing services (e.g., Uber, Lyft).

Funding and Ownership Model

Currently, Staff is studying a funding and ownership model that utilizes a nonprofit entity (NPE) to own and be the borrower for the waterpark, on land that is leased by the City from T5 (see attached outline for more detail). The debt for the project would be issued by a conduit issuer (not the City), and underwritten by one or more investment banks or underwriters. Structuring the project like this allows the project to obtain a much lower interest rate than private, for-profit financing, and the City has very limited financial exposure. This tax-exempt financing, combined with the nonprofit regulations, provides many checks and balances on the profits and operations of the project that work in the City's favor. This nonprofit ownership model is done for commercial real estate projects when the borrowing interest rate is a barrier and/or when private profits are not a primary objective. For this project the primary objective is to add an amenity to South Loop and the region, and to diversify MOA. Many NPEs exist that would serve as the owner, some of which are very experienced in this model. The NPE receives a fee for doing so for their board members to manage the NPE, which is relatively low given the size of the project. In the model currently being studied, the NPE would be the owner through the 30-year financing period, and as such would be the borrower of the debt. During the financing period, the City would pledge sales and use taxes that are allowed through special legislation which is an existing part of

MN Statute. These taxes include admissions, food/beverage, lodging, and sales taxes (aka ARBLs for additional revenues by legislation – the legislation that was adopted in 2008 and revised in 2010) that would be applied solely at MOA and most importantly <u>only if</u> the project revenues do not meet projections. The City would become the owner once the debt is paid off in year 31, through year 50 when the risk of the debt service payments are gone. It should be noted that substantial capital expense reserves are planned so that the waterpark can be updated and maintained at the highest level. The City would receive the excess revenues from the project starting in year 31. Additional detail and proposed terms of the key agreements for the project is included in the attached outline.

Two main factors allow the project to cash flow: the NPE ownership allows for tax exempt financing at a lower interest rate and exemption from property taxes, and the ARBL tax pledge provides additional security for the financing, additionally lowering the interest rate and debt service coverage ratios. Neither of these key factors exist for a traditional, for-profit, real estate development.

<u>Development Services Contract</u>
Development of the project would be led by T5 and the Port Authority. In order to bring the project to a state of design where costs can be accurately determined, the Guaranteed Maximum Price (GMP) stage, about 6-9 months of work by architects, suppliers, and engineers needs to take place. Management, hiring and coordination of these tasks is a large endeavor. Staff proposes to engage MOA-WP Development for the design/development GMP work through the execution of a Development Services Contract (DSC). The City and MOA-WP Development are proposing to share in the cost of the DSC as detailed in the attached outline, with 75% of the cost being born by the City (SLDF) and 25% by MOA-WP Development. The DSC is estimated to cost $10M (with a more detailed estimate coming in the next few weeks).

The special legislation that created the South Loop Development Fund (SLDF) allows this type of expenditure. Funds from the SLDF cannot be spent outside of South Loop and it exists to create and promote real estate development in South Loop. Funding for the DSC would be provided by a Grant Agreement whereby the City grants revenue to the Port Authority from the SLDF. Revenues in the SLDF are derived from liquor and lodging taxes in the City, and the lodging industry would be a beneficiary of the waterpark. Consideration of the Development Services Contract would occur at a future joint meeting of the City Council and Port Authority, likely in February. Both the City and MOA-WP Development would be reimbursed for the cost of the DSC if and when the waterpark project financing closes.

<u>Schedule</u>
February 2019 (estimated) - Consideration of the Development Services Contract, Grant Agreement and Master Contract Notice Provision Amendment
Q3/Q4 2019 – Consideration of some ancillary agreements (e.g., nonprofit and underwriter determination)
Q3/Q4 2019 - GMP Determination
Q1 2020 – Consideration of approval of all documents, financial closing, start of construction
Q1 2022 – Construction completion and grand opening

<u>Management</u>
Management of the park for the first 30 years would be performed by MOA-WP Management, an entity specifically created to manage the waterpark. After the first 30 years, the City would hire a management company, which could be a different management company, or MOA-WP Management again. Due to the nonprofit and tax exempt statutes, management contracts cannot be for more than 30 years and must be at industry standard compensation rates.

<u>2016 MOA Master Redevelopment Contract Notice Provision</u>
A term has been added to the attached outline that modifies the notice provision if there are changes to ownership entities of MOA.

<u>Project Risks</u>
While early indications are that the project will be very successful, no project is without risk. The City and Port's investment in the design/development GMP phase via the DSC is at risk if the project does not move forward (should the bodies approve that contract). Construction risks including increased costs are always a potential issue. Legal risks exist, but Staff believes they are manageable. The biggest risk is probably the waterpark not meeting revenue expectations.

In that case, the ARBLs would be enacted to cover any shortfalls, and do not directly impact the City's finances. There is also reputation risk; although the City and Port would not be waterpark owners or issuers of the debt, the bodies are still a party to the various agreements.

From the perspective of the MOA, the two largest risks it has are the opportunity cost of the land for development (and the potential subordination of ground rent for the project), and the fact that ARBLs could be enacted at MOA if the project does not perform. They also have another risk given that if the project does not perform to expectations, they have attached their valuable mall to an underperforming asset.

<u>T5 Concurrence</u>

Triple 5 concurs with moving forward with the project as outlined, and will be present at the meeting to answer any questions.

Attachments:

Waterpark Overview and Agreement Outline
Preliminary Plan Layout and Renderings