



**Request for City Council Committee Action
from the Department of Community Planning & Economic
Development – CPED and the
Finance & Property Services Department**

Date: February 25, 2014

To: Council Member Lisa Goodman, Chair, Community Development & Regulatory Services Committee and MCDA Operating Committee

Referral to: MCDA Board of Commissioners

Subject: Block E Redevelopment Project (Mayo Clinic Square) - Amendments to Redevelopment Contract and Related Documents

Recommendation: Approve amendments to the applicable Block E documents, subject to the terms and conditions described in this report.

Previous Directives:

- 1) July 8, 2010, the City approved the assignment of the Block E redevelopment contract, ground lease and related agreements for the theatre/retail portion of the block to Camelot LLC, an affiliate of Alatus LLC.
- 2) May 5, 2004, the City approved the assignment of the Block E hotel lease and transfer of the hotel portion of the block from Block E Hotel Capital, LLC to Block E Hotel Capital II, LLC.
- 3) April 2003, MCDA Board approved amendments to the hotel lease to facilitate additional financing.
- 4) March 3, 2000 – City Council approved revised project finance plan and MCDA Board of Commissioners approved terms for, and authorized execution of, amended redevelopment contract.
- 5) There were many other actions dating back to December 1997.

Department Information

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Approved by:

Charles T. Lutz, Interim Director CPED

Kevin Carpenter, City Finance Officer

Presenter in Committee: Mark Winkelhake

Financial Impact

- X Action is within the Business Plan

Staff believes that the proposed Block E redevelopment project will produce substantial benefits to the City, and will (1) add significantly to the taxable property value on the block, (2) generate additional tax increment and holding rent revenue in upcoming years, (3) allow for the early retirement of the TIF bonds issued for the project seven years ahead of schedule (March 1, 2020), and (4) allow for early decertification of the Block E TIF district so that all of the property value in the district can be returned to the City's general tax base.

The amendments, terms and conditions outlined in this report will have a positive financial impact to the City in 2014 and beyond. The City will receive \$250,000 in cash at closing from Camelot LLC. Additionally, staff is recommending that \$950,000 in current City cash associated with this project be used for other purposes. Staff will return to the City Council with recommendations regarding use of these funds.

Community Impact

- Neighborhood Notification – Not applicable
- City Goals – Jobs & Economic Vitality; Many People, One Minneapolis; A City that Works
- Comprehensive Plan – Policy 4.1: Support private sector growth to maintain a healthy, diverse economy; Policy 4.12: Downtown will continue to be the economic engine of the Upper Midwest region by strengthening its employment core.
- Zoning Code – The proposed project is currently in compliance with zoning code and will follow all required City processes for building improvements.
- Sustainability Targets: Not applicable
- Living Wage/Business Subsidy Agreement – Yes ___ No X .
- Job Linkage - Yes ___ No X .

Brief History

Block E is located in downtown Minneapolis and is bounded by Hennepin Avenue, 1st Avenue North, 6th Street North and 7th Street North. The current development on this block was constructed in 2001, and consists of two parcels of property.

The theatre/retail/parking (TRP) parcel contains a three-story building with approximately 261,300 square feet and a 455-space underground parking garage. This building was developed by Block E Interests LLC (an affiliate of McCaffrey Interests LLC), and originally contained retail and restaurant space on the ground and skyway levels and a multi-screen movie theatre on the third floor. The TRP building went into voluntary foreclosure in late 2009, and was purchased in 2010 by the current owner, Camelot LLC (an affiliate of Alatus LLC). Camelot assumed all of the rights and responsibilities of the former owner. The TRP building is largely vacant at the moment, but will be redeveloped as described below.

The hotel parcel contains a 255-room luxury hotel named the Graves 601, which is owned by Block E Hotel Capital II LLC. The proposed Block E redevelopment project described in this report does not include the hotel parcel or building. All of the land on Block E is currently owned by the Minneapolis Community Development Agency and is leased to the two building owners

under separate ground leases through December 31, 2028. At the termination of each ground lease each owner is entitled to purchase their respective parcel for \$1.00.

Proposed Redevelopment Project

Camelot is planning to reconfigure the entire Block E TRP building into a unique, sports facility, office, and retail/entertainment destination. It will be rebranded as Mayo Clinic Square. The total investment by Camelot is projected to be \$50 million, consisting entirely of private sources. This major investment will not only revitalize the block itself, but will further enhance the economic vitality of the surrounding entertainment district.

The entire building will be redesigned and will include high-ceilings and open, sunlit public spaces. The interior will be reconfigured to create better pedestrian flow, highlighted by a ground level corridor connecting Hennepin and 1st Avenues. Furthermore, the entire TRP building shell (excluding the hotel) will be remodeled to incorporate a more modern design (see attached renderings at the end of this report). Updated digital media and billboards will be added as well as new sidewalks, seat walls and planters.

The Timberwolves/Lynx and Mayo Clinic will occupy the building's third floor (former theater space), which will contain a new practice facility for the teams as well as Mayo Clinic's new sports medicine facility. The facility will provide such services as physical rehabilitation and sports-specific skills programs to the teams and the public. It is anticipated that the second floor will consist of new office space with some service-oriented retail. The Timberwolves and Lynx also plan to add a team store on the second level. The first floor will include retail, restaurant and entertainment businesses that will promote night and weekend activity at the street-level. The current ground floor tenants, which include Jimmy Johns, Starbucks, Kieran's Irish Pub and the Shout House Dueling Piano Bar will remain; and additional tenants will be sought to fill the rest of the leasable space.

Past City Financial Assistance

The City provided financial assistance to the original development predominantly through the issuance in late 2000 of \$29M in general obligation tax increment bonds (the TIF bonds). Bond proceeds were used to pay for a portion of the underground parking garage which is open to the public, as well as the skyways and public areas in and around the TRP building and hotel. Prior to construction on the block, the City established a tax increment financing (TIF) district that included both parcels on Block E and one adjacent parcel located across 7th Street.

The TIF bonds are payable semi-annually and were originally scheduled to be fully retired on March 1, 2027. It was originally anticipated that repayment of the TIF bonds was to be made from tax increment revenues collected from the TIF district and entertainment taxes generated by the hotel and various tenants in the TRP building. Additionally, it is required that if tax increment revenue generated by the two Block E parcels does not meet minimum levels each year, the owners of the TRP and hotel buildings have to make annual "holding rent" payments to make up any tax increment revenue shortfalls.

Due to legislative changes in the property tax system in 2001, the TRP and hotel parcels have never generated the minimum tax increment levels required, and the two building owners have been making annual holding rent payments since 2003. The total of these two payments have ranged from approximately \$328K in 2003 to \$1.0M in 2008, and were approximately \$788K in 2013.

Over the years the TIF bonds have been refinanced several times, and interest costs have been significantly reduced. Therefore, no entertainment taxes generated by the two Block E parcels have ever been needed to pay debt service on the TIF bonds. All of the entertainment taxes collected from this block have gone to the City's General Fund. Additionally, tax increment and holding rent payments have been sufficient to prepay the bonds ahead of schedule. Assuming the terms, conditions and amendments contained in this report are approved and executed, it is projected that the TIF bonds will be fully retired on March 1, 2020 (seven years ahead of schedule).

Proposed Amendments

In order for Camelot to obtain financing for their proposed redevelopment project, a number of amendments need to be made to several of the Block E documents that were signed between Block E Interests LLC and the Minneapolis Community Development Agency, and assigned to Camelot LLC upon their purchase of the property. These amendments include the following:

- 1) Eliminate provisions in the Redevelopment Contract relating to the Stipulated and Accrued Amounts. Since entertainments taxes from the block have never been used to pay bond debt service on the bonds, City staff and Camelot agree that these provisions are not relevant, but do present an obstacle to the financing of the project and should be deleted.
- 2) Cap Camelot's annual Holding Rent obligation at \$535,332 per year.
- 3) Terminate Camelot's ground lease and Holding Rent obligations to the City upon the earlier of the date on which Camelot makes the payment for calendar year 2018 and the date the TIF bonds are fully retired.
- 4) A commitment by the City to utilize Holding Rent paid by Camelot, for calendar years 2014 and beyond, solely for the payment of debt service on the TIF bonds until they are fully retired.
- 5) Replace the old Block E project name with the new project name.
- 6) Potential minor changes to the Lease of Public Elements, regarding such items as the location and use of escalators and elevators, provided they are consistent with the original bond financing requirements.

Terms and Conditions

In consideration for approval of the requested amendments, Camelot will agree to the following terms and conditions related to the TRP parcel and building:

- 1) Camelot will construct a ground level interior public corridor connecting Hennepin Avenue and 1st Avenue North in the TRP building. This should provide more activity and better pedestrian flow on the ground level of the building.
- 2) Until termination of the ground lease, Camelot will lease and market a minimum of 80% of the net rentable area of the TRP building's ground floor (including the space located at Hennepin Avenue and 7th Street North) for restaurant, retail and entertainment uses that have weekend and evening hours. The remaining net rentable area may be used for other purposes. Camelot must annually demonstrate to the City's satisfaction that it is

making significant efforts to lease vacant ground floor space for restaurant, retail and entertainment purposes. Failure to demonstrate such efforts will result in the ground lease continuing until December 31, 2028. The CPED Director and City Finance Officer will have joint authority to (a) determine on an annual basis if significant efforts to lease ground floor space have been made, and (b) administratively adjust the 80% benchmark downward if appropriate.

- 3) After renovation, any ground floor tenant space with exterior walls must have an entrance from the outside of the TRP building, as well as significant square footage of windows in the exterior walls. The CPED Director and City Finance Officer will have joint authority to waive this requirement for selected spaces and tenants if appropriate.
- 4) After renovation, any vacant ground floor tenant space must contain a “pop-up” shop or other temporary use such as art exhibits or displays.
- 5) For each of the calendar years 2014-2018, Camelot will pay the Holding Rent calculated as currently provided in the ground lease, plus “Additional Holding Rent” equal to \$535,332 minus the normal Holding Rent amount calculated for that year. Cumulative Additional Holding Rent payments during this time period shall not exceed \$500,000.
- 6) Camelot will pay the City \$250,000 on the day when the document amendments are executed by the MCDA and Camelot.

The City will also utilize \$950,000 in cumulative Holding Rent on hand, from calendar years 2012 and 2013, for purposes other than debt service on the TIF bonds. The City will utilize all remaining Holding Rent after the TIF bonds are fully retired for purposes to be determined by the City Council at that time.

Use of Funds

This report does not make any recommendations as to the use of the \$1.2M in funds noted above. Staff will return at a later date with specific recommendations regarding use of these funds.

Recommended Hotel Parcel Amendments

If the requested amendments are approved for Camelot, staff also recommends that, for consistency sake, the following amendments also be made to those documents affecting Block E Hotel Capital II LLC, the hotel owner. The hotel owner is agreeable to these amendments.

- 1) Holding Rent paid by the hotel owner to the City, for calendar years 2014 and beyond, will be used solely for the payment of debt service on the TIF bonds until they are fully retired.
- 2) The hotel owner’s Holding Rent obligation will terminate when the TIF bonds are fully retired.
- 3) The hotel ground lease will terminate when the TIF bonds are fully retired.