Request for City Council Committee Action from the Department of Community Planning & Economic Development

Date: December 12, 2006

To: Council Member Lisa Goodman, Community Development Committee
Council Member Paul Ostrow, Ways and Means/Budget Committee

Subject: Request for approval of amendment to terms of $1.25 million loan to 2700 East Lake LLC (Coliseum Building).

Recommendation: **Recommendation: The CPED Director recommends that the City Council approve the amendment to the terms of the loan deferring the principal and interest payments until January, 2008 and then interest only payments be made for twelve months to accommodate a lower than projected building cash flow.**

Previous Directives: May 2006, City Council approval of a Loan Modification Agreement deferring Principal and interest payment for four months and then interest only payments for one year. November 1999, City Council approval of $625,000 Commercial Corridor Loan. June 2000, City Council approval of the Redevelopment Plan and Tax Increment Plan for 2700 East Lake Street. October 2000, City Council approval of the Coliseum Financing Plan including Empowerment Zone funds. August 2001, approval of sewer access payment. November 2001, City Council approval of an additional $250,000 Commercial Corridor Loan. March 2003, MCDA Executive Director approval of loan subordination to accommodate new, higher first mortgage amount and reduction in the TIF note interest rate from 10% to 5%.

Prepared by: Kris Maritz, Business Finance
Approved by: Charles T. Lutz, Deputy Director CPED ________________
Presenters in Committee: Kris Maritz

Reviews

- Permanent Review Committee (PRC): Approval _N.A.__ Date ________________

Financial Impact

- Other financial impact: The payment deferral will allow the project to stay in a positive cash flow position and therefore, increase the success of the project and the repayment of the City's loan.

Community Impact

- Neighborhood Notification: N.A. The original project and financing was approved by the Longfellow Community Council.
- City Goals: The project supports the City goal of a mix of unique businesses that give Minneapolis' neighborhoods unique identities and character. The project also supports entrepreneurial opportunities for residents by enabling financing for the ownership of buildings and businesses.
- Sustainability Targets: N.A.
- Comprehensive Plan: Project is in compliance.
- Zoning Code: Project is in compliance.
- Living Wage/Business Subsidy/Job Linkage: N.A.
- Other: N.A.

Supporting Information

The Coliseum Building, at 2700 East Lake Street was purchased by Fred Lehmann, 2700 East Lake Street LLC, in December 2000. The building is a three-story, 77,000 square foot brick structure built in 1917. The total project cost of acquisition and rehab exceeded $5 million. Current tenants include Denny's Restaurant, Hennepin County Medical Center, several small professional services offices and two small restaurants. Originally, the Minneapolis Police Department was a tenant in the basement but canceled it's lease in 2001 shortly after they moved in due to a moisture problem. Since then no other tenant has leased space in the basement due in part to the impending construction of the areaway.

Financing Overview

Original financing terms, originated in **December, 2001:**

First Mortgage:	$2,321,627	(To be taken out by CRF upon construction completion)
TIF Note:	920,000	($1.1 million placed with a consortium of 5 area banks, 10%)
Commercial Corridors (CPED):	625,000	(4%, 20 years, no payments for 5 years, interest accrued)
Longfellow NRP:	325,000	(4%, 20 years, no payments for 5 years, interest accrued)
Empowerment Zone:	300,000	(4%, 20 years, no payments for 5 years, interest accrued)
Total:	$4,466,627	

Refinance in **April, 2003**:

The project ran into significant cost over runs, partly due to the areaways under Lake Street. Originally, the Police Department occupied the basement level. However, the areaway caused a moisture leak into the basement and the Department complained of mold and climate issues. Lehmann tried to remedy the problem through several construction amendments but, in the end, the problem could not be remedied to the Police Department's satisfaction and they cancelled their lease. This loss of rental income (projected to be

$90K+ in year one) and other cost over runs prevented the Community Reinvestment Fund from taking out the construction financing as planned and prompted Lehmann to seek alternative first mortgage financing. Lehmann refinanced with American Bank and CPED subordinated to the new first mortgage of $3,470,000. In addition, as an acknowledgment of lower property tax revenue due to property tax compression, the City reduced the TIF note interest rate from 10% to 5%. All other loan terms remained the same and repayments on the public financing were set to begin in June, 2006.

Extension in **May, 2006:**

When the developer began negotiations with American Bank for an extension or renewal of the first mortgage loan, the Bank was unwilling to do so without some forbearance on the CPED loan, due to pending lease renewals and the Lake Street reconstruction. After reviewing several cash flow scenarios and participation in negotiations with the bank, developer, leasing agent (Master Development), the property management company (Facility Management Partners, McGough Construction's property management division) and CPED, the bank agreed to a six month loan extension (October 15th) contingent on an amendment to CPED's loan terms: Principal and Interest deferral for four months (June – September) to coincide with the Bank extension, interest continues to accrue, and interest only for a period of 12 months. Full principal and interest payments would begin in October, 2007.

Current Financial Status:

The building is projecting a slight ($1,000) operating profit for 2006. But the projected cash flow position for the year is a negative $61,000.

This is due to the following:

- Two major tenants, La Clinica and CLUES (Chicano Latinos Unidos in Service), have leases that expired on August 31st. HCMC leased 13,363 square feet of space. The occupancy rate is currently 41.8%.
- A commission owed to the management company for recruiting HCMC.
- The areaway construction (which affects the ability to lease the basement) has not yet been awarded to a contractor thus the space cannot be leased.

The building is current on its debt obligations to the bank and on its TIF note. In October, the bank agreed to another extension until December 15, 2006. The interest only payments to CPED which were to have begun in October, 2006 have not as yet started.

The projected cash flow for 2007 is a negative $310,000 for the year. This is a result of the following:

- The area way construction (which affects the ability to lease the basement) has been delayed. As of November 9, 2006, public works opened bids with the intent of having the construction completed by mid summer. This is a best case scenario. There is a possibility that construction could be delayed as long as 2008. The streetscape construction cannot be done until the areaway is completed. However, the streetscape construction should not be a leasing impediment.
- The current vacancy rate is 58.2%.

The extension and deferral until January, 2008 allows the developer to potentially get the area way construction completed (this is dependent on public works timeline) and begin leasing the basement space. The interest only provision should see the project through to the completion of all construction projects, removing barriers to the marketability of the basement spaces. In addition, it will provide them with a small capital reserve which will be needed to do some tenant improvements to attract new leaseholders. It will also allow a small buildup of cash that will be needed to begin paying the construction assessments which could total $54,000 per year by 2009.

The building was appraised at approximately $4.55 million at the time of closing in 2000, assuming the income approach, which included approximately $100,000/year from the Police Department. The current tax assessed value is $2,975,000. Because the building is not currently fully leased and the street will be torn up again in both the front and side to do the areaway, there is reason to believe that the current value is less than the original appraised value. The CPED loan to value ratio based on the assessors “market value” and including the senior debt ($3.2 million American Bank, $1.054K Associated Bank/TIF and $1.5 million CPED/NRP/EZ) is 193%.

Conclusion:

Overall, the finance plan is dependent on fully leasing the building. The payment deferral and interest only payments will allow the project to stay in a positive cash flow position and therefore, increase the success of the project. There is both a professional leasing company and property management company in place. The professional management should increase the chance of success as well. If they are unsuccessful leasing and default on the first mortgage, there is not enough value at this time to be paid in full from the sale of the building. Therefore, we recommend the changes to the repayment schedule.

Coliseum Report December 12, 2006

November 16, 2006

MEMO TO: Chuck Lutz, Deputy Director

FROM: Jack Kryst, Chair, Development Finance Committee

SUBJECT: Development Finance Committee Recommendation Regarding Amendment of Loan Terms for 2700 East Lake (Coliseum Building)

On November 16, 2006, the Development Finance Committee considered a staff report regarding the proposed amendment of terms for a $1.25 million loan to 2700 East Lake LLC for the Coliseum Building.

The Committee concurs with the staff recommendation that principal and interest payments be deferred until January 2008, and then interest only payments be made for 12 months.

One Committee member abstained from discussion and voting due to a conflict of interest.

cc: Kris Maritz

Tom Daniel

Mike Christenson

Lee Sheehy

November 16, 2006

MEMO TO: Chuck Lutz, Deputy Director

FROM: Jack Kryst, Chair, Development Finance Committee

SUBJECT: Development Finance Committee Recommendation Regarding Amendment of Loan Terms for 2700 East Lake (Coliseum Building)

On November 16, 2006, the Development Finance Committee considered a staff report regarding the proposed amendment of terms for a $1.25 million loan to 2700 East Lake LLC for the Coliseum Building.

The Committee concurs with the staff recommendation that principal and interest payments be deferred until January 2008, and then interest only payments be made for 12 months.

One Committee member abstained from discussion and voting due to a conflict of interest.

cc: Kris Maritz
Tom Daniel
Mike Christenson
Lee Sheehy