



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

Date: June 12, 2006

To: Council Member Paul Ostrow, Ways & Means Budget/Committee

Subject: Amendment to the Target Center Arena Lease, Operating, Management, Use and Assurances Agreement and to the Basketball Playing Agreement

Recommendation: 1. Approve the terms of an Amendment to the Target Center Arena Lease, Operating, Management, Use and Assurances Agreement and Basketball Playing Agreement; 2. Authorize the proper City and MCDA officials to execute this Amendment; 3. Amend the 2006 Operating Budget to increase the appropriation in CPED Fund ERZO – GARFS (890-8490) by \$1,200,000 from fund balance for transfer to CPED Fund CPOO - Capital Projects; 4. Amend the 2006 Operating Budget to increase the appropriation in CPED Fund CPOO – Capital Projects (890-8933) by \$1,200,000.;5. Refer this report to the MCDA Board of Commissioners for its concurrence and approval.

Previous Directives: On March 10, 1995, the City Council and MCDA Board of Commissioners approved the terms and authorized the execution of the Target Center Purchase Agreement, related Lease and financing documents, and the issuance of \$84,650,000 in bonds.

On May 19, 2000, the MCDA Board of Commissioners authorized the issuance of a Notice of Termination to Ogden Entertainment, Inc. and the execution of an Assignment and Assumption Agreement with SFX Entertainment Corporation and amendments to related Target Center documents for SFX to assume the duties and obligations of Operator.

On April 2, 2004, the City Council and MCDA Board of Commissioners approved principal terms and authorized the execution of an Agreement Regarding Assignment and Assumption of Arena Lease, Operating, Management, Use and Assurances Agreement by and among the Minneapolis Community Development Agency, Clear Channel Target Center Arena Mgmt LLC, and Midwest Entertainment Group LLC (MEG) for MEG to assume the duties and obligations of Operator.

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Approved by: Patrick Born, Finance Officer _____

Lee Sheehy, CPED Director _____

Permanent Review Committee (PRC) Approval Not Applicable

Note: To determine if applicable see <http://insite/finance/purchasing/permanent-review-committee-overview.asp>

Presenter in Committee: Patrick Born

Financial Impact (Check those that apply)

- No financial impact (If checked, go directly to Background/Supporting Information).
- Action requires an appropriation increase to the Capital Budget or Operating Budget.
- Action provides increased revenue for appropriation increase.
- Action requires use of contingency or reserves.
- Business Plan: Action is within the plan. Action requires a change to plan.
- Other financial impact (Explain):.
- Request provided to department's finance contact when provided to the Committee Coordinator.

Community Impact (use any categories that apply)

Neighborhood Notification: Not applicable

City Goals: Create an environment that maximizes economic development opportunities within Minneapolis by focusing on the City's physical and human assets.

Comprehensive Plan: Not applicable

Zoning Code: Not applicable

Other:

Background/Supporting Information:

There are three key agreements explaining the rights and obligations of the three primary stakeholders at the Arena portion of Target Center:

- The Arena Lease, Operating, Management, Use and Assurances Agreement ("Operating Agreement") between MCDA and Operator;
- The Arena Use Agreement between Taylor Partnership (Team) and Operator; and
- The Basketball Playing Agreement ("Playing Agreement") between MCDA and Taylor Partnership.

Through the Operating Agreement, the MCDA contracted with Ogden Entertainment, Inc., as part of the Target Center purchase in 1995, to be the Operator of the Arena for a term that ends on June 30, 2025. Ogden had been the Operator for the previous Arena ownership.

The Arena Use Agreement allocates Arena use rights and the rights to certain Arena revenues between the Taylor Partnership and the Operator. Because of this critical partnership between the Taylor Partnership and the Operator, the Playing Agreement between MCDA and the Taylor Partnership provides that the Taylor Partnership has the right to assume the rights and obligations of the Operator under the Operating Agreement or to subcontract with a third party, acceptable to the MCDA, to assume and perform the Operating Agreement in the event that the Operator is ever anyone other than Ogden. Any such assignment and assumption would bind the new Operator to existing contracts and agreements, such as collective bargaining agreements.

In 2000, Ogden announced the pending sale of its Entertainment Division to Aramark Corporation. Due to the uncertainty of the timing and effect of the pending sale to Aramark, the Taylor Partnership requested that MCDA terminate the Operating Agreement with Ogden and assign the Operating Agreement to SFX Entertainment Corporation. SFX agreed to pay the required termination payment to Ogden and to give a Guaranty to MCDA equivalent to the Guaranty given by Ogden. Shortly after assuming the Operating Agreement, SFX was acquired by Clear Channel Entertainment (CCE).

On January 30, 2004, MCDA received a request and proposal from representatives of the Taylor Partnership and Nederlander Company to consent to the assignment of the Operating Agreement from CCE to Midwest Entertainment Group LLC ("MEG"), a Minnesota limited liability company formed for the specific purpose of managing and promoting Target Center for the remaining term of the Operating Agreement (June 30, 2025). MEG ownership was comprised 50 percent by an entity comprised of members of the Taylor Partnership (TC Arena Group LLC), and 50 percent by an entity comprised of James M. Nederlander and other Nederlander Company owners (Nederlander West Coast). In lieu of a Guaranty Agreement, MEG was required to include a liquidity covenant in the Assignment and Assumption Agreement obligating MEG to maintain minimum operating capital of \$1,500,000, throughout the term of the Operating Agreement. Unlike previous operators which were shell corporations, MEG would have assets. This fact, plus the vested interests of Glen Taylor and his companies, resulted in the liquidity covenant provision. The assignment had the support of CCE, and MEG assumed the duties and obligations of Operator on May 1, 2004.

On January 4, 2006, MCDA received notice from MEG that on December 31, 2005, it met the liquidity covenant and was in compliance with the Assignment and Assumption Agreement. MEG further notified MCDA that it might not be able to meet the liquidity covenant in the future due to losses.

Target Center's Impact

Target Center is a significant asset to the entire state. The MCDA acquired the facility in 1995 in order to preserve the asset and to keep the Timberwolves playing basketball in Minnesota. In addition to being the home of the NBA's Timberwolves and WNBA's Lynx, Target Center hosts dozens of first class events each year—from family shows like Sesame Street Live to big name concerts like Elton John, Coldplay, and U2. Every year, more than one million people attend over 200 events at Target Center. These events generate in excess of \$3.7 million in sales and liquor tax revenue to the State of Minnesota and \$2.0 million in sales, restaurant, liquor, and entertainment tax revenue to the City of Minneapolis as well as parking revenue to the City's parking fund.

In addition to attending Target Center's events, many guests enjoy an afternoon or evening in downtown Minneapolis and frequent restaurants, shops, and hotels. Their impact is felt in terms of street life and at the cash register—local restaurateurs, for instance, often speak of the robust business they do when there is an event in the Arena. Target Center is clearly a vibrant facility and has a vital role to the City, region, and State.

Industry Dynamics and Financial Performance

The Arena Operator's financial performance is being affected by a significant change in the national concert industry and national facility competition. Artists and their promoters are demanding greater economic returns and now access revenue streams (such as concessions) that formerly flowed to the operators. In order to book certain events, the Arena Operator has given up revenues and as a result has experienced losses.

Another factor that affects the Operator's financial performance is the reduction of revenue-share as a consequence of existing contractual arrangements that over time have worked to the Operator's disadvantage.

As a result of these market changes and contractual agreements, the operation has seen profitability decline since 2000 and has operated at a loss which is not projected to improve under the currently operating structure.

It is important to note that the Target Center situation is not unique. Within the past 12 months, building operators, NBA teams, and government officials in Portland, Seattle, and Milwaukee have been addressing similar financial issues in their facilities.

In March of 2006, the Nederlander half of MEG informed the MCDA that they no longer desired to serve within the operating partnership. At the same time, TC Arena Group LLC (the Taylor half of MEG) indicated its intent to acquire Nederlander's 50% share in MEG and work in close partnership with the City to improve the performance and competitiveness of the arena, although they also indicated that it was not their current intention to continue long-term as the operator of the facility.

Principal Terms of the Amendment to the Operating Agreement and the Basketball Playing Agreement

In May of 2006, TC Arena Group LLC completed its acquisition of the Nederlander interest and is now the 100 percent owner of MEG. MEG will continue to manage the Arena on an interim basis, provided MCDA participates in stabilizing operations. The principal terms of this proposal, which are incorporated into an Amendment to the Operating Agreement and to the Basketball Playing Agreement (see Attachment A) are as follows:

- On a monthly basis commencing on June 1, 2006, if Monthly Arena Operating Expenses exceed Monthly Arena Revenue, MCDA will reimburse MEG the lesser of \$200,000 or 50 percent of the difference between Monthly Arena Revenue and Monthly Arena Operating Expenses.
- Unless terminated earlier, the Amendment will expire on the earlier of June 1, 2007 or the exhaustion by MCDA of reimbursement funds.
- On or before April 1, 2007, MCDA and MEG will discuss whether and under what conditions the parties will continue to collaborate regarding Target Center.
- Right to terminate Operating Agreement: After August 1, 2006, MEG may provide notice to MCDA of its intention to discontinue as Operator of Target Center. Between August 1, 2006 and June 1, 2007, MEG must provide 90-day notice; between June 2, 2007 and December 31, 2007, MEG must provide 120-day notice; between January 1, 2008 and July 1, 2008, MEG must provide 150-day notice; and from July 2, 2008 through the end of the term, MEG must provide 180-day notice. MCDA and MEG are discussing a parallel termination right and notice provision for MCDA.
- MEG agrees to provide MCDA with the opportunity to review all information regarding Target Center operations.
- As a condition of the MCDA sharing in future operating losses, Taylor Partnership waives its right to assume the rights and obligations of MEG under the Operating Agreement pursuant to the Basketball Playing Agreement.

During this interim period, MCDA and MEG will collaborate in pursuing the best model for long term management. This may lead to an RFP process to retain a new manager for Target Center and would not exclude examining regional approaches to public venue management. By August 15, 2006, MCDA will finalize a process for identifying the new Operator and will provide an update to the City Council.

Staff recommends approval of this amendment in order to ensure the continued smooth operation of the facility. By investing in the operations for an interim period, MCDA will stabilize the current facility operations and provide the opportunity to develop a long-term approach to preserve this important City and State asset.