CITY COMMISSION WORK SESSION
December 6, 2010

The work session was called to order by Mayor Bradley at 5:06 p.m. in the Commission Chambers, 401 Park Avenue South, Winter Park, Florida.

Members present:	Also present:
Mayor Kenneth Bradley	City Manager Randy Knight
Commissioner Tom McMacken	Deputy City Clerk Michelle Bernstein
Commissioner Beth Dillaha	City Attorney Usher Brown
Commissioner Carolyn Cooper	CRA Director, Dori DeBord
Commissioner Anderson	Assistant CRA Director, Peter Moore
	Real Estate Research Consultant, Dr. Owen Beitsch

This meeting was a work session with no public input.

State Office Building

Mayor Bradley mentioned the reason for this meeting is for staff to enlighten the Commission on the current status which will help them make a clear decision on this item at the next Commission meeting scheduled for December 13, 2010. CRA Director Dori DeBord introduced Dr. Owen Beitsch, a consultant helping the City work through the process. She explained that Dr. Beitsch has a background in real estate throughout the Central Florida area and has been doing this type of work for the past 30 years. Ms. DeBord recapped the RFI process and provided a brief summary regarding the status of the current negotiations.

Dr. Beitsch explained that he has been working with the CRA Department for several months and has reviewed the development proposal submitted by Concord Eastridge and prepared a memo dated July 19, 2010 with his comments (attached). He mentioned there are 3 major items that it comes down to:

1. What really is the underlying value of the property;
2. What might be the role of RLF in implementing any kind of development on this site;
3. How do they best implement some kind of lease hold arrangement on this property

He spoke about a memorandum he prepared dated December 6, 2010 (attached) which highlights 8 major points that the Commission and City must consider and briefly addressed each item.

1. The appraisal and the appraisal process;
2. Use of the site;
3. Lease rate and term;
4. Economic development issues;
5. Negotiations to date
6. Risks and perceptions
7. Options (reasons to do this deal or not);
8. Recommendations

Dr. Beitsch concluded by saying there are 4 fundamental options and he thinks they can be treated as rather individualized or discrete. He explained each of the options:

1. Accept the deal as it is now;
2. Reject it;
3. Modify the offer (the basic structure) and push it closer to what they perceive is market value.
4. Separate RLF and CEI

In summary, he stated that the bottom line has merit on a policy basis but the Commission is the one that needs to decide if it is a policy they want. He thinks what they should do as a leadership body is to come up with a threshold value they want to achieve. He said once they do that, they would have to provide a reasonable amount of time for CEI to finalize any arrangements that they have with RLF. He also suggested that they place much less emphasis on CPI as the cost of doing business and instead deal directly with the costs of this deal.

Mayor Bradley asked if staff would be making a recommendation at the next Commission meeting. Ms. DeBord stated no. She explained that staff would be expecting the Commission to provide them with an official direction on where they want to go with this deal and to let staff know what the threshold value is that they want to achieve. She suggested another option for the Commission to provide staff with direction this evening so they can move forward to the next step.

There was a lengthy discussion regarding the key threshold value whereby each Commissioner provided input. They also shared their concerns regarding the value and the current use of the property, along with discussing the various potential land uses, the options available that would help generate property tax revenue for the City, the length of the lease term and the due diligence period. Ms. DeBord provided a summary and said they are going to look at some terms that are based on somewhere between \$3.2 to \$4.0 million, with a discount rate and those terms may include a partnership agreement either in a lease partnership or an equity partnership down the road in order to get to that bottom line.

She noted that they will look at more of a bottom line number to deliver to them rather than an annual number because she thinks it will be easier to understand and it will also help provide CEI with the traction they may need to use to work out their performance as well. She said they will discuss this with CEI prior to this coming Monday's Commission meeting so they will keep the item on the agenda to update them on the progress and to also give CEI the opportunity to share their findings. This will also allow the Commission to provide staff with further direction. There was a consensus for this to occur.

<u>Five Goals from City Manager's Evaluation</u>

Mr. Knight stated that he will email the five goals to the Commissioners for their review and input since there was not enough time this evening to discuss this item.

The meeting was adjourned at 6:59 p.m.

Michelle Bernstein

Deputy City Clerk Michelle Bernstein

MEMORANDUM

TO: Dori DeBord, AICP
Economic Development/CRA Director

FROM: Owen Beitsch, PhD, FAICP, CRE

DATE: July 19, 2010

RE: **Comments on Concord Eastridge proposal**
(RERC 10-108)

Hard copy will not follow unless requested

At your request, we have reviewed the development proposal submitted by Concord Eastridge for the former state occupied office building on Morse, vacated now for several years.

Understanding there has been limited time available to confirm many of the underlying considerations that generated the proposal, we think the offer is below what the market should be capable of supporting if the property were developed to its maximum intensity. We cannot really evaluate the full impact of the proposal because we do not have the financial analysis which presumably is the basis for Concord's offer. That said, based on a cursory financial analysis we completed, the sum and terms may not be *grossly* out of line *if a smaller building* is all that is developed. Still, the imputed value appears to be at the lowest end of the potential range. Consequently, the merit of the offer must be evaluated on the quality and investment in the smaller structure relative to expectations or criteria imposed by the City.

From the material we have available, the representations are that the building would be improved to Class A quality, necessitating material outlay. Such investment is not really described but, in effect, it is difficult to understand the proposer's interest in saving the structure and then providing the capital required to enhance its condition as outlined. These strategies seem irreconcilable based on the observed physical configuration and age of the building.

Of there are reasons to maintain the tree canopy, as described in the proposal, there are designs and solutions that could enable more intense development such that the site's allowable FAR and value are maximized. If, for example, the City is willing to concede the discounted value some of that savings could be directed to a parking garage should that be a crucial goal. In our opinion, the most obvious issues relate to the City's envisioned strategy and uses for the site relative to the concept advanced by the respondent.

Over the next four years the City and/or CRA will have received about $400,000 in revenues from the development itself as well as some assumed level of ad valorem. The potential future value needs to be evaluated relative to this sum which, *if not received* by the City, is properly viewed as the opportunity cost of postponing any action. In our mind, the opportunity cost is extremely low.

Given the state of the larger real estate market, the location, and the potential to replace the existing structure with others more in keeping with the City's vision, this sum seems to be a relatively modest level of financial exposure should the City still wish to explore other options.

In the event the City wishes to proceed, there are many issues to address in the basic lease, primarily those associated with allowing Concord to control the remainder of the property without added financial consideration and under general terms more beneficial to the City.

The appraisal process

Implicit in the appraisal process is that the property targeted for valuation is being deployed for its highest and best use, that which is physically possible, legally permissible, market supportable and yields the highest return to the land. In this case, the appraiser has treated the site as a vacant parcel or has attributed no material value to the building occupying the site.

The inference in the logic of appraisal is that any commercial structure erected under the conditions of highest and best use would generate rents enabling a certain land value to be supported. In other words, even though the parcel is vacant, the inherent assumption is that the prices of the comparable vacant properties were negotiated with the expectation that rents (income) of a certain level would enable the land to support a value commensurate with the related income stream. Multiple properties sold at similar values tends to confirm the conclusion

Though useful for defining value at a specific point in time, an appraisal is silent about future conditions and rarely addressees adequately the broader market dynamics affecting the conclusion in question. When a property is used for something which is other than the assumed highest and best use, there is naturally a variance between the appraised value and that estimated using different conditions.

In this case, the highest and best use purports to be a commercial venture, more specifically an office building. An appraiser is not a developer and cannot fully evaluate all the risk issues involved in reaching decisions about the best means to proceed. He certainly cannot consider all options. Nonetheless, the reported value of the land should still broadly reflect what multiple interests, looking to realize an expected income stream, would willingly pay for a particular parcel at single point in time.

In theoretical terms, the developer's proposal should not be impossible to reconcile to the appraisal unless there are gross deviations in assumptions or procedures. What seems apparent in this case are major differences in the developer's approach (a smaller, renovated building), the cost to demolish (material whatever the sum), presumptions about the near term state of the market (diminished and highly competitive) and likely expectations imposed by the City. The implications of these differences are discussed briefly in the next few pages.

Indicated value

The substance of the proposal is associated with the perceived value of the underlying property. As you are likely aware, finding meaningful transactions for purposes of benchmarking in today's market context is difficult but not impossible. Nonetheless, the outcome of such an analysis is reasonably considered in the context of obvious influences that cause a change in that value.

The City's appraisal places that value at about $6,000,000, but draws upon some older transactions. Many current listings, without consideration to their comparability, suggest a lower value as do other transactions of properties intended for office development and also comparable in size. These other examples are much more recent reference points.

Current commercial listings (Loopnet, July 15, 2010)								
Location/ Address	Descprtion	Size (AC)	Size (SF)		List		$/SF	
521 N Cenrtal blvd	commercial	5.45	237402	$	7,122,000	$	30.00
Onco Dr	commercial	4.98	216058	$	3,000,000	$	13.89
9588 SOBT	commercial	2.57	111949	$	1,570,000	$	14.02
Lee Road	commercial	1.5	65340	$	550,000	$	8.42
425 Sybella Pkwy	commercial	2.62	114127	$	2,950,000	$	25.85
415 Kennedy Blvd	commercial	0.13	5663	$	99,500	$	17.57
2301 Opak ridge	commercial	6.42	279655	$	2,600,000	$	9.30
4426 S Conway	commercial	1.69	73616	$	1,150,000	$	15.62
1705 Lee Rd	commercial	1.49	64904	$	950,000	$	14.64
9036 Tueky Lake	commercial	3.10	135036	$	1,850,000	$	13.70
					Average	$	16.75

Other recent sales								
Location/ Address	Date	Descprtion	Size (AC)	Size (SF)		Price		$/SF
Lake Mary	2008	PUD	5.25	227819	$	2,032,143	$	8.92
Lakemont/Orlando	2009	PD	1.99	86641	$	1,000,000	$	11.54
Lake Mary	2009	PUD	1.75	76255	$	875,999	$	11.49
Doulas Rd/Altamonte	2009	MOC	1.21	52754	$	550,000	$	10.43
Lake Nona	2010	PD	4.00	174,240	$	2,000,000	$	11.48
						Average	$	10.45

Appraisal (Bledsoe)								
Location/ Address	Date	Descprtion	Size (SF)	Size (SF)		Price		$/SF
Orange/Denning	2008	Retail	217,800	244434	$	6,400,000	$	26.18
600 Concourse Pkwy	2008	Church	217,800	226076	$	3,923,400	$	17.35
80 West Michigan	2009	Office	217,800	46358	$	1,250,000	$	26.96
901 N Orlando	2006	Retail	217,800	84,972	$	4,350,000	$	51.19
						Average	$	26.46

Except as noted in the accompanying table, we really cannot opine on the physical or legal comparability of these other examples but clearly they are intended for office development. Given the suburban locations common to the other transactions, they may reflect a lower intensity of potential development than the property on Morse suggesting they *should* have a lower price per square foot. While we can speculate about their physical condition, none of these other properties seem to have demolition associated costs involved. Without suggesting that we are offering an opinion of value there is a well established range with about $16 per SF anchoring the mid range of value.

Potential indiucated value				
Location/ Address	$/SF	Size (SF)		Estimated value
Appraisal	27	217,800	$	5,880,600
Listings	17	217,800	$	3,702,600
Other transactions	11	217,800	$	2,395,800
Imputed proposal (7%)	7	217,800	$	1,475,000

The proposal places an imputed value of $1,475,000 on the property for the concept proposed, a discount from the other transactions of almost $1,000,000, a discount of about $2,000,000 from the midrange value. The discounts are sufficient in magnitude to question the reasonableness of the proposed leasehold sum. The difference logically considers at least the costs of demolition, which might be justified were Concord intending to raze the existing structure, and /or the form of the deal being offered to RLF as the anchor tenant.

A very crude financial analysis - based on the outlined cost of development at about $7,100,000 or $133/SF - indicates the low land value results almost exclusively from the reduced building size and possibly from lower rents that may be dictated by the concept and the anchor. Expectedly, the same analysis completed for 98,000 SF seems to suggest a land value closer to the appraised value. Because no income data for the project was provided, we can only speculate on these conclusions but they do raise questions, possibly easily documented, about the underlying assumptions. If there is a risk premium reducing the offer, it is not evident nor warranted in our opinion. The proposer already claims to have secured the anchor tenant. Effectively, the building is almost fully leased from the beginning so many risks are fully mitigated.

The building's size and lease may be all the market can support. If so, the proposal is silent on these points. Still, the remainder of the site is held by the developer virtually for free to accommodate activity that might occur in the future under terms stipulated by the developer. Again, if there is an anchor tenant, the proposer's risk in proceeding with a larger or more aggressive concept seems nominal.

Leasehold

As with transactions involving full fee interests, those that are not adversely affected by the current market are hard to find, but not impossible. Virtually every commercial outparcel involves a net lease arrangement.

The City's appraisal references leases executed by the airport. In our opinion these reflect unique circumstances and must meet criteria imposed by the FAA. As a practical matter, while some leases do achieve 10% of value as described in the appraisal, it is not the norm. The added considerations at the airport and on any other piece of publicly owned property impose constraints to a lease or involve unrelated goals that raise questions about the use of properties owned or placed into service by public agencies as a meaningful reference point.

Neither the basic financial dimensions of any future changes in lease payments – now tied to 7% of value - or the developer's request for a 60 year lease are unreasonable in our opinion. The basis for renewal beyond that point are worth reexamining as are the market indicators provided by the proposer as criteria for intensifying the site.

Leases, by their vary nature are complex and can be problematic. With the proper lender, they may also reduce the amount of cash necessary initially which may be the part of the developer's strategy although the City may find it attractive to retain the site long term, just as the proposal describes.

In any case, the lease itself is a subject that merits a separate and much more substantive discussion about the key business points. The most effective lease will have safeguards to assure it is equitable and beneficial for both the developer and the City. In general, it has been our experience that parties to a ground lease fail to recognize *both* the complexities and compromises that may be necessary to structure a sound lease. From the background materials in the proposal, there is at least an indication that this subject has been addressed by the team in other public settings. Nonetheless, we are not satisfied that the City's interests are properly protected, especially given the low land value.

Concept and design

Design, and representations about it, open subjective debate. While it is compelling to contemplate a remodeled building, upgraded to LEEDS standards, as a Class A office structure, this outcome is not likely. Though not impossible that this building *could* ultimately command rents comparable to the market's conventional Class A structures, *rarely* has any remodeled or renovated building been successfully positioned to compete with this tier of properties. The typical Class A building, aside from its upgraded features, must have efficiencies, extensive amenities, and finishes that offer reasonable alternatives to the region's newest facilities.

Such upgrades and features are not at all apparent in the current proposal. The characterization of the building and proposal as something *unusual* or *special* serves only to overstate the value of the concept being advanced. To the degree the remodeled structure could be considered a Class A building, it is reasonable to posit that it would generate higher rents or possibly have higher costs of development but neither is obvious in the proposal.

There may be *merit* or *purpose* in saving the existing structure but the criteria in awarding this opportunity, along with the financial implications, should not focus on the building's designation as a Class A facility but rather the value gained (lost) with implementing a renovation scheme. At the moment, we can only assume that the primary economic advantage results from demolition but, as noted, that is not apparent in the land value.

Policy considerations and goals

It is worth noting that Concord will relocate and accommodate a major Winter Park employer, a reasonable economic development goal in the currently challenging job market. If that is the purpose of the proposal, however, there may be more effective ways of achieving that result, including use of other programs intended for job creation. When a developer is provided discounts or incentives to construct a facility, while making representations about the nature of the anchor tenant, the City indirectly becomes a party to that agreement and should be assured that the goal intended is achieved. If the prospective tenant is conditionally tied to this *specific proposal*, then the relationship should be transparent to the City so its value to the proposal can be properly vetted.

Intuitively, it is more meaningful to provide the incentives *to the end users*, not the developer unless there is evidence that a lease rate appropriate to the inducement has been provided. In any case, the developer will benefit over the *entire* ground lease term and the employer, unless seeking a commensurate lease term, receives benefit for a much reduced time period.

In effect, the support for the employer, if that is a key goal, will expire well before the financial commitment to the developer of record.

CRA

Chapter 163.380 (2), FS, addresses the public purpose associated with the sale of properties acquired by the CRA. Without implying there are possible legal issues to consider in the planned transaction – we know nothing about the actual ownership, the flow of funds, or other matters - the references in 163.380 are instructive because they speak specifically to the public benefit stemming from a transaction at less than *fair* [market] *value*. The idea, of course, is simply to evaluate the quid pro quo realized by the broader community as the result of the transaction. The seemingly low value, while not necessarily at conflict with the provisions of Chapter 163, is a *reminder* that the City and its agency have plans, a mission, and possibly a vision that were contemplated as part of the property's acquisition from the state and the redevelopment effort.

Conclusion

The value of the property in question is such that the developer's offer, though not unreasonably related to the size of the *existing* building, represents at best a minimal sum and the City may be advised to consider what opportunity costs are incurred by renegotiating, postponing, or abandoning the transaction. We believe these costs are very low given what could happen at some future date or under more favorable financial terms. Whatever may happen in the market, of course, is speculative but the low value seems to remove much of the risk in pursuing a strategy which postpones the transaction or seeks to enhance the value or conditions of the current offer.

At the very least, the city should consider revising the manner in which the remainder of the site of the site is available for the developer's use. The terms of the agreement should speak to an improved form of control that does not deter the developer's interest in the property, perhaps a significantly reduced option period with additional performance criteria. As for the main ground lease, we would suggest that the key business points be drafted in a term sheet and accepted prior to approving the general development approach.

Other issues are likely to emerge that are beyond the scope of this brief assessment. The comments here should be viewed in that context. RERC's information and comments should be relied upon only to aid your continued discussions with the proposer and to support your own planning efforts.

Real Estate RESEARCH
CONSULTANTS

MEMORANDUM

DATE: December 6, 2010

TO: Winter Park City Commission

FROM: Owen Beitsch, PhD, AICP, CRE
REAL ESTATE RESEARCH CONSULTANTS
14 East Washington Street, Suite 500
Orlando, FL 32801

PH (407) 843-5635 FAX (407) 839-6197

RE: Continued Review of CEI Proposal

Based on my review of the original proposal submitted by CEI and the subsequent discussions I have had with staff and CEI, I have prepared this brief memorandum covering what, I think are the major points that the commission and City must consider. Several of the points are laid out in more detail in my correspondence to Dori Debord dated July 2010 and distributed to you over the course of the last week.

- **The appraisal and the appraisal process**
  - Normally, there is the expectation that value reflects highest and best use but even so that use or activity has variants and some subjectivity. Certainly, the appraisal did not explicitly recognize reuse of the office building.
  - The appraisal indicated a value of approximately $5,800,000 drawing upon relatively older comparables and assuming only limited constraints on use and market.
  - The presence and siting of the existing office building hold the overall value below what the appraisal suggests might be realized.
  - RERC's analysis indicates for a lower density office use, the value of the property recognized in the proposal is not unreasonable. It is probably at the lower end of the value range for such a use but still within that range. I can't reconcile to a value today of much more than some $3,400,000 but costs to implement the project affect this value.
  - Regardless of the ostensible differences in valuations, land value is a function of the use placed on the property.
  - Could other uses support a higher value? Possibly, but the value for an office use at the density represented by the existing building is not unreasonable.

- **Use of the site**
  - Because the proposal does not anticipate maximum use of the site, there is no inherent value in allowing the developer to use the entire site.

- **Lease rate and term**

  - Too lengthy for the nature of the simple development concept proposed which has limited risk with a key tenant already identified.
  - Instead, a lease of 40-50 years is not unreasonable with provisions made for extensions reasonable.
  - The proposed percentage arrangement is not unreasonable for a land lease. The sum could be higher but not materially and then it would be dependent upon the other terms and conditions of the lease itself.
  - A form of lease escalation is appropriate but setting the target is difficult because provisions for increases in the base rent may not match to the timing of increases in the rents negotiated with individual tenants. Both the amount of an increase and the uncertainty of the increases will make it difficult to negotiate financing and individual leases with tenants.

- **Economic development issues**

  - The transaction, at what might be a value set by less than highest and best use, sets into motion a discussion about who benefits from the lease. CEI and RLF are two distinct entities. CEI benefits from the full term of the lease while RLF will benefit only from the terms of the lease the firm executes with CEI. The City might consider ways to bifurcate the benefits of the lease.

- **Negotiations to date**

  Given these various issues and the City's directions to negotiate with CEI, the following points have emerged:

  - Raise the annual rent for the basic lease beyond that offered.
  - Offer various alternatives to fixed increases based on CPI.
  - Limit the size of the parcel that could be the subject of the lease...effectively preserve entitlements for some future use or action controlled by the City.
  - Consider a stepped increase in ground rent that follows CEI's lease term.

- **Risks and perceptions**

  Reasons *to do* this deal

  - Recognition that the City plays a part in economic development that may be difficult to value and there is an obvious corporate citizen that could benefit.
  - Though difficult to value, the economic considerations of the current offer are not entirely at odds with market value...buildings are being sold and leased at values that would suggest the actual cost of replacement would be higher.
  - The parcel has remained vacant for some time and there is no ostensible interest from other parties to activate the site.
  - Any consideration about a valuation recovery is largely speculative.
  - An unsubordinated land lease, properly done, exposes the City to only modest risk.

Reasons *not* to do this deal

- Based on the original offer, the opportunity cost to wait a few years seems modest. There may, for example, be an inherent benefit in creating park land or open space that benefits other development.
- Even though the City retains control of some part of the site, there are more limitations on the remainder than might be if the site were fully utilized from the outset.
- As this specific corporate citizen is enabled, an alternate space will be vacated.
- The most challenging aspect is avoiding a financial position for either party that creates too much risk and/or subsequent potential criticism.
- The opportunity has not been adequately exposed to the broader market.
- The City has not, at this point in time, actually seen the terms of the agreement between CEI and RLF.

- **Options**

  - Accept deal fundamentally as submitted, recognizing that it is largely below market value. The premise for accepting this option is that the City has to be aggressive in its economic development role.
  - Reject it as being excessively generous. The premise to rejecting the proposal is to explore other options while also understanding that the proposer has made it relatively clear that the offer has little, if any, room for modification.
  - Modify the offer to push it closer to perceived market value:
    - Within the basic structure already on the table....this means only a handful of terms would be modified so as not to change the fundamental dynamics of the offer
    - Participate in the rental stream to assure common objectives
    - Participate in the equity on some preferred basis
  - Separate RLF and CEI

- **Recommendations**

  - If committed to RLF, the deal may have merit.
  - Target value threshold for entering into negotiation and allowing CEI to accept or reject
  - Provide a reasonable period for CEI to reach agreement with RLF
  - Place less emphasis on CPI
  - Instead accept deal fundamentally as it has emerged so far but focus on safeguards to modify costs that impact value...if within 10%, adopt shared rental streams going forward against a modestly increasing base rent....if greater than 10%, assume equity participation in addition to shared gross rents
  - Recognize time necessary to finalize deal
  - Recognize need for some flexibility in terms
  - Recognize obligations imposed by *participating* in the financial arrangement