



But-For Determination Report

Parkville, Missouri

First Amendment to the Parkville Market Place Tax Increment Financing Redevelopment Plan

November 7, 2017

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Mission Statement

Springsted provides high quality, independent financial and management advisory services to public and non-profit organizations, and works with them in the long-term process of building their communities on a fiscally sound and well-managed basis.

1. Purpose

The City of Parkville has retained Springsted to review the proposed First Amendment to the Parkville Market Place Tax Increment Financing Redevelopment Plan. The First Amendment proposes the expansion of the of the Redevelopment Area to include a new redevelopment project area (“Redevelopment Project Area 2”), which is an approximately 6.41 acre of land north of Redevelopment Project Area 1, on the north side of Missouri Highway 45 west of Melody Lane. The Developer is proposing the development of approximately 33,400 square feet of retail, restaurant, and/or other commercial facilities. Additionally, the Developer will be undertaking necessary onsite and public infrastructure improvements.

The City has requested this analysis to determine the need for the requested assistance, based on the cost and operating pro forma information provided by the Developer. The analysis that follows examines whether the proposed redevelopment scenario would reasonably be anticipated to be developed without adoption of the requested financial assistance.

The report that follows is pursuant to Missouri Statutes 99.800 et seq. relative to a determination that the proposed TIF Redevelopment Plan would not reasonably be anticipated to be developed without the adoption of the Plan.

We have approached this determination based on the proposed plans regarding redevelopment costs, outcomes, financing sources, and timing to develop a measure of the Developer’s expected return when compared to the amount of risk. If a development is owned and operated as an investment, a measure of return is calculated considering the time value of money and involves an assumed sale of the property at a price appropriate in the market place. This analysis is termed the Internal Rate of Return (“IRR”). The final determination is based on whether or not a potential IRR is reasonable without the requested subsidy, within the current marketplace and at the present time.

The Developer (CBC Parkville LLC) has requested assistance in the following forms:

-Statutory TIF – One hundred percent of the incremental increase in ad valorem property taxes revenues (“PILOTS”) along with 50% of the incremental increase in economic activity tax revenues (“EATS”) which will be captured and re-directed to pay for new eligible reimbursable project costs incurred by the Developer.

-Community Improvement District (CID) Sales Tax – The Developer is proposing the creation of a 1% Community Improvement Sales Tax which will be applied to all properties within the CID Area which is coterminous with the

TIF District. The CID is anticipated to have a lifetime of twenty-three years from the creation of the District.

-Community Improvement District #2 (CID) Sales Tax – The Developer is also proposing the creation of a second Community Improvement District that would apply a second 1% sales tax. This second CID Area would also be coterminous with the TIF District, and would be created for the purpose of funding potential future improvements to Melody Lane and Hwy 45. Additionally, funds from the second CID area may be used for repayment of eligible TIF/CID expenses within the current budget amounts which would result in a reduction in the term of the District if funds were utilized in this manner. The second CID would have a different board with a majority City representation. This CID is anticipated to have a lifetime of twenty-three years from the creation of the District.

2. Executive Summary

Shown in the tables below are the calculated internal rates of return with and without the subsidy request, based on the project costs and operating revenues of the proposed project. Determining if a project would occur without subsidy requires the testing of various assumptions which have a material effect on a project's feasibility. We have tested the sensitivity of the return without assistance by varying the cost and the revenue assumptions, each independently and then collectively. The reason for testing sensitivity is to illustrate the magnitude with which project assumptions would have to change in order for the project to be considered feasible without assistance. Table A, below, details the significant findings of the sensitivity analysis:

Table A

Without Assistance Sensitivity Analysis	Change Necessary to be Feasible	Rate of Return without Assistance
Decreased Costs	40% Decrease	7.41%
Increased Revenue	50% Increase	7.34%
Combined Cost and Revenue Changes	23% Decreased Costs 23% Increase Rev	7.40%

The table above indicates the magnitude at which project assumptions would have to change for the project to have a feasible rate of return without assistance. Based on the *Korpacz/Price Waterhouse Cooper Real Estate Investor Survey* the current range of unleveraged market returns for a project of this nature is 5.50% to 10.50%, with an average of 7.32% which we used as our feasibility benchmark. Absent the changes outlined above, the projects would not attract a return sufficient to exceed the industry's threshold for investment and would not likely be completed through private enterprise alone.

Table B, below, illustrates the Developer's projected rates of return with and without assistance:

Table B

Combined Projects Pro Forma	With Full Assistance Request	Without Assistance
Unleveraged	7.65%	0.45%

3. The Project

The Developer is proposing the redevelopment of Project Area 2 into a commercial development containing approximately 33,400 square feet of retail and restaurant uses. Project Area 2 is an approximately 6.41 acre property located generally at the northwest corner of Missouri Highway 45 and North Melody Lane. The Developer of the project is CBC Parkville LLC. Construction of the development is projected to be commenced in the fourth quarter of 2017 or the first quarter of 2018 and is expected to be completed by the end of 2019.

The development will be undertaken in part by the Developer and in part by third-parties which will purchase pad ready sites from the Developer. The Developer is anticipated to own and operate a 15,000 square foot retail building on Lot 1 and an 8,400 square foot retail building on Lot 4.

The Developer will construct two pad-ready sites, which will be sold to third-party developers who are anticipated to construct an approximately 4,000 square foot retail/restaurant building on Lot 2 and an approximately 6,000 square foot retail/restaurant building on Lot 3.

The total cost of the project is detailed in Table C, below.

Table C

Costs Category	Total Project Cost	% of Total Costs	Developer* Costs	TIF Eligible Costs	CID Eligible Costs
Land Acquisition	\$1,960,000	22.12%	\$1,116,878	\$843,122	-
Public Roadway	180,000	2.03%	-	-	\$180,000
Storm Water Detention	220,066	2.48%	-	57,566	162,500
Utilities	358,725	4.05%	-	358,725	-
On Site Improvements	1,250,200	14.11%	-	1,250,200	-
Building Costs	3,069,000	34.64%	3,069,000	-	-
Soft Costs	1,125,500	12.70%	429,500	696,000	-
Financing Costs	96,500	1.09%	96,500	-	-
Miscellaneous Costs	600,000	6.77%	600,000	-	-
Total Project	\$8,859,991	100%	\$5,311,878	\$3,205,616	\$342,500
Percentage of Total Cost:			59.95%	36.18%	3.87%

*Project Cost are net of third-party expenses for the development of lots 2 & 3.

Acquisition

The Developer identified the total cost of acquiring the site as \$1,960,000. The cost estimate is based on the Developer's cost of acquiring the site which they have under contract to purchase. The Developer is seeking TIF reimbursement for \$843,122 of the total acquisition cost.

The purchase price of \$1,960,000 equates to approximately 22.12% of the total project costs and equates to a per acre price of \$305,772 or approximately \$7 per land square foot.

Hard Costs

We have taken the project cost information submitted by the Developer and grouped the following line-items together under the hard cost heading, which are outlined in Table D below.

Table D

		Developer Costs	TIF Reimbursed	CID Reimbursed	% of Total Project Costs
Net Developer Hard Costs	Total Cost				
Building Construction (Developer Portion)	\$3,069,000	\$3,069,000	-	-	34.64%
Public Roadway					
Improvement on 45 Highway	30,000	-	-	30,000	0.34%
Improvement on Melody Lane	65,000	-	-	65,000	0.73%
Turn Lane on 45 Highway	85,000	-	-	85,000	0.96%
Utilities					
Storm Water Detention	220,066	-	57,566	162,500	2.48%
Storm Sewer/Sanitary/Water	358,725	-	358,725	-	4.05%
Other Site Improvements					
Demo, Grading, Retaining Walls	662,526	-	662,526	-	7.48%
Parking Lots/Drives/Sidewalks/Lighting	407,674	-	407,674	-	4.60%
Electric/Gas/Phone	75,000	-	75,000	-	0.85%
Landscape/Signage	105,000	-	105,000	-	1.19%
Total Hard Costs	\$5,077,991	\$3,069,000	\$1,666,491	\$342,500	57.31%

The Developer incurred costs categorized together under the hard cost heading total \$5,077,991 which equates to approximately 57.31% of the total project cost.

The Developer is anticipating constructing two retail buildings of 15,000 square feet and 8,400 square feet respectively; for a total of 23,400 square feet. The Developer's projected cost of constructing these buildings is \$3,069,000 which equates to a per square foot cost of \$113.15 per square foot.

To provide a comparison, we compared the cost estimates to the *RSMMeans Square Foot Cost Estimator* for estimated construction costs for a retail building in Kansas City. The *RSMMeans* data provides a range of cost estimates for the construction of vertical building improvements. The *RSMMeans* estimate range for this type of building ranges from \$101.31 to \$138.01 depending on construction type, with an average of \$119.35. The Developer's estimate of \$113.15 appears reasonable based on this comparison.

The remaining Hard Costs include expenses related to improvement of the site, the extension of public utilities and street improvements adjacent to the site. These costs total \$2,008,991 and represent approximately 22.67% of the total project cost. The Developer is seeking the reimbursement for 100% of these costs from TIF and CID sources.

In total, the construction cost category is the largest segment of the development costs, accounting for 57.31% of the total project costs. Consequently, this is a segment where project costs savings could have a positive effect on the rate of return realized by the Developer, while higher than estimated costs would have the converse effect. In the return analysis section of the report, we discuss the sensitivity of the rate of return to changes in the project costs and the effect on the return without assistance of a decrease in project costs.

Soft Costs

For purposes of this review, we have grouped the cost categories in Table F below as Soft Costs:

Table F

Total Soft Costs	Total Cost	Developer Cost	TIF Reimbursed	% of Total Project Costs
Legal/Consulting/Accounting	\$125,000	\$125,000	-	1.41%
Architectural/Engineering/Surveying	261,000	-	261,000	2.95%
Geotechnical Studies/Environmental	67,500	-	67,500	0.76%
Professional Services	292,500	-	292,500	3.30%
Commission on Pad Sales/Leases	304,500	304,500	-	3.44%
Bond/Permits/Fees	75,000		75,000	0.85%
Financing Fees	96,500	96,500	-	1.09%
Developer's Fee	350,000	350,000		3.95%
Contingency	250,000	250,000		2.82%
Total	\$1,822,000	\$1,126,000	\$696,000	20.56%

The total amount of the costs categories grouped under the soft cost heading totals \$1,822,000, which equates to approximately 20.56% of the total development costs. The Developer is seeking reimbursement from TIF for a portion of the soft costs in an amount of \$696,000. The Developer is not seeking reimbursement from the CID for soft costs.

Reviewing the soft cost categories for largest percentage of the total project costs to smallest, the largest soft cost line-item is the Development fee of \$350,000. This cost estimate equates to approximately 3.95% of the Developer's portion of the total project cost, which is a reasonable basis for the Development fee.

The next largest soft cost line-item is the Commission expense of \$304,500. This cost estimate is based on an upfront expense related to the sale of the pad

sites and the leasing of the Developer owned retail buildings. The cost estimate equates to approximately 6.8% of the total lease and pad sales amounts, which is a reasonable estimate.

The third largest soft cost line-item is Professional Services at \$292,500, for which the Developer is seeking full reimbursement from TIF. This cost equates to 2.95% of the Developer's total cost estimate. A basis for this cost estimate was not provided.

The Architectural/Engineering/Surveying line-item is the next largest at \$261,000, for which the Developer is seeking full reimbursement from TIF. This line-item equates to approximately 8.5% of the vertical building improvement costs, which is a reasonable estimate.

The Developer identified a contingency line-item of \$250,000 which equates to 2.82% of the total project cost, which is a reasonable estimate if not a touch conservative.

The Developer identified a legal/consulting/accounting line-item of \$125,000 which includes the City's legal expenses. In total, this line-item equates to approximately 1.41% of the total project cost. A basis for how the cost estimate was derived was not provided.

The remaining soft cost line-item greater than 1.0% of the total project cost is the Financing Fee estimate of \$96,500. No basis for how this cost estimate was derived was provided. However, this estimate equates to approximately 1.3% of the anticipated borrowing amount, which is a reasonable amount.

The other remaining soft cost categories are all less than 1.0% of the total budget and, combined, equate to \$142,500 or 1.61% of the total project cost. The Developer is seeking TIF reimbursement for both of these remaining line-items; Geotechnical Services/Environmental and Bonds/Permits/Fees.

In the "Return Analysis" section of the report we discuss the sensitivity of the rate of return to changes in the project costs and the effect on the return of a decrease in project costs.

4. Assistance Request

The Developer is requesting assistance from the following sources:

-Statutory TIF – One hundred percent of the incremental increase in ad valorem property taxes revenues (“PILOTS”) along with 50% of the incremental increase in economic activity tax revenues (“EATS”) which will be captured and re-directed to pay for new eligible reimbursable project costs incurred by the Developer.

-Community Improvement District (CID) Sales Tax – The Developer is proposing the creation of a 1% Community Improvement Sales Tax which will be applied to all properties within the CID Area. The CID is anticipated to have a lifetime of twenty-three years from the commencement of the District.

-Community Improvement District #2 (CID) Sales Tax – The Developer is also proposing the creation of a second Community Improvement District that would apply a second 1% sales tax. This second CID Area would also be coterminous with the TIF District, and would be created for the purpose of funding potential future improvements to Melody Land and Hwy 45. Additionally, funds from the second CID area may be used for repayment of eligible TIF/CID expenses within the current budget amounts which would result in a reduction in the term of the District if funds were utilized in this manner. The second CID would have a different board with a majority City representation. This CID is anticipated to have a lifetime of twenty-three years from the creation of the District.

For both of the CID sales taxes, the first 50% of the receipts under these sales taxes will be captured as TIF revenue and redirected to reimburse TIF eligible improvements. The remaining 50% of the CID sales tax revenue will be used to reimburse the CID budget costs as identified earlier in the report. The remaining 50% of the second CID sales tax revenue will be used by the CID and the City to fund Melody Lane/Hwy 45 intersection improvements, which are in addition to what was previously described in the project budget. Additionally, funds from the second CID maybe used by the CID to reimburse the Developer for eligible project costs included within their current budget, resulting in the TIF District satisfying its obligation over a potentially shorter period.

The requested assistance will be on a pay-as-you-go basis with the Developer initially funding all redevelopment project costs and receiving reimbursement for eligible redevelopment project costs as the TIF and CID revenues are captured and re-directed. The Developer is seeking reimbursement from in an amount of \$3,205,613 from TIF sources and \$342,500 from CID sources, plus interest at an estimated rate of 5.50%.

The net present value of the TIF revenue stream, when calculated at a 5.50% discount rate is approximately \$2,883,480. As a result, the Developer is not anticipating being fully reimbursed for their TIF budgeted amounts of \$3,205,613, plus interest. Since the Return Analysis is based on the actual level of TIF revenue projections and not the budget amount, the TIF reimbursement agreement should be capped to reflect the revenue capacity of the revenue streams as currently projected. In the case of the TIF reimbursement, the Developer should be reimbursed for their principal request of \$3,205,613, but with a cap on the maximum amount of interest reimbursement set at \$2,711,280; for a total reimbursement of principal and interest of \$5,916,893. The cap on the total amount of interest reimbursement will result in the Developer receiving interest at an effective rate closer to 4.5%, as opposed to their requested 5.5%.

The Developer will be funding their portion of the Project costs through a mix of Developer equity, private debt, and pad sale proceeds from the sale of pad ready sites. The pro forma estimated an equity contribution of 20% of project cost with the remaining 80% of project costs to be financed by permanent debt. The Developer projected private financing terms of 5.5% interest over a term of 25 years. The Developer will be responsible for initially privately financing the \$3,548,113 of TIF/CID redevelopment project costs that are anticipated to be reimbursed through future TIF/CID revenues.

Table G provides the anticipated sources that will be utilized to fund the redevelopment project. The TIF and CID revenues will be provided on a pay-as-you-go basis, with revenues received used to offset the private equity and debt of the Developer.

Table G

Sources:	
Developer Equity	\$1,771,998
Pad Sale Proceeds	\$1,600,000
Developer Private Debt	\$5,487,993
Total Sources	\$8,859,991

5. Return Analysis

Utilizing the operating pro forma prepared by the Developer we evaluated the need for assistance for the proposed development by comparing the potential return with and without assistance. The Developer provided a 10-year operating pro forma for the development based on a two-year build-out and lease up period, and operating revenue and expense assumptions. The Developer's pro forma calculated a leveraged internal rate of return (IRR) calculation after the 10-years of the pro forma. We utilized their submitted pro forma as our baseline to estimate the potential return with and without the requested forms of assistance. The return realized by the Developer is a result of the assumptions used in the creation of the operating pro forma, therefore a number of steps must be performed to analyze the reasonableness of the assumptions used.

Step One – Evaluate Project Costs:

The first step in analyzing the return to the Developer is to determine if the costs presented are reasonable. We have discussed a portion of the costs above and have commented on the mechanics whereby cost savings on the private side could occur. If cost savings for the Developer's share occur absent any other changes, the Developer would realize a greater return than projected. In the following sensitivity analysis we examine the impact of cost savings on the projected rate of return without assistance.

Step Two – Evaluate Operating Pro Forma Assumptions:

The second step in calculating the return to the Developer is to determine if the operating revenues and expenses of the proposed development are reasonable. The Developer projected average lease rates for the retail components that will be constructed, and average pad sale prices for the components that will be sold.

- The Developer has assumed a lease rate of \$13.00 per square foot for the retail with the lease rate to escalate to \$14.30 in Year 7.
- The Developer has assumed a 1.5% vacancy/unreimbursable expense allowance upon occupancy in Year 3.
- The Developer has estimate the total pad sale proceeds for the sale of the two pads of \$1,600,000.

We reviewed third-party market information to evaluate the projected lease rate. The market information indicated average neighborhood retail space, in Kansas City, leases for an average rate of \$13.25.

The Developer's pad sale assumption also appears reasonable.

Step Three – Evaluate Hypothetical Sale Assumptions:

The third step in analyzing the return to the Developer is to determine if the assumptions for the hypothetical sale of the asset are reasonable. The calculation of an internal rate of return requires the assumption of a hypothetical

sale of the asset in the final year of the operating pro forma. The inclusion of this hypothetical sale is used purely for purposes of evaluating the return on the Developer's investment. The determination of the potential market value of the project through a hypothetical sale is necessary as it allows for inclusion of the value of the asset into the rate of return calculation. The calculation of an IRR without the hypothetical sale would result in an understated return, as the return would not take into account the value of the real estate asset. The use of a hypothetical sale assumption is not indicative of the Developer's intention to sell the development in the final year.

The critical assumption when valuing the asset at the time of the hypothetical sale is the capitalization rate. The available net operating income divided by the capitalization rate results in the assumed fair market value of the asset. The Developer has used a capitalization rate of 7.00% for the project to calculate the hypothetical sale value. In reviewing historical cap rate trends for retail developments, we feel that 7.00% is a reasonable assumption.

Developer – Baseline Leveraged Return Analysis:

Table H below, shows the Developer's calculation for their base pro forma rate of return without assistance, and with the full assistance request of TIF and CID Sales Tax. Their return was calculated on a leveraged basis.

Table H

Developer Pro Forma	Leveraged IRR
Without Assistance	-17.44%
With Assistance	10.69%

Springsted – Adjusted Unleveraged Return Analysis:

Table I below, shows the Springsted adjusted rate of return analysis to be based on an unleveraged basis.

Table I

Springsted Unleveraged Pro Forma	Unleveraged IRR
Without Assistance	0.45%
With Assistance	7.66%

Market Return Benchmark:

The Developer's return was modified to be measured on an unleveraged IRR calculation in order to compare the potential return to the Developer to a third-party market source in the *Korpacz/Price Waterhouse Cooper Real Estate Investor Survey* prepared for the second quarter of 2017. The *Korpacz/Price Waterhouse Survey* provides a market comparison on which project feasibility can be judged.

To evaluate the rate of return a project of this nature would require to be considered "feasible" we consulted this survey as a resource to compare the Developer's rate of return to a market benchmark to help determine feasibility. According to the developers surveyed, the typical unleveraged market return necessary to pursue a project of this nature falls in a range from 5.50% to 10.50%; with an average return of 7.32%.

Additionally, we consulted the *IRR Viewpoint Online – Kansas City Market Data* resource for the second quarter of 2017, which identified a target unleveraged rate of return of 8.0% for a community retail development.

Sensitivity Analysis

In order to answer the question "is the development likely to occur without public assistance" we analyzed the without incentive scenarios, using the Springsted Adjusted Unleveraged Return Analysis Pro Forma without assistance as the basis for the sensitivity analysis. The sensitivity analysis is performed in order to understand the magnitude at which project costs would have to decrease, or conversely project revenues would have to increase, for the project to be considered feasible. For this sensitivity analysis we use the average return of 7.32% from the *Korpacz/Price WaterHouse Cooper Real Estate Investor Survey, Second Quarter 2017* as the benchmark for performing our sensitivity analysis.

To understand the impact of the project cost assumptions, we performed a cost sensitivity analysis to determine the rate at which project costs would have to be reduced for the projected rate of return to be in excess of our feasibility benchmark without assistance. Table J illustrates the development would need to realize a 40% reduction in project costs in order to be feasible without assistance. Given a 40% reduction in costs the project would have a rate of return of 7.40%.

Table J

Project Costs Sensitivity	Reduction in Project Costs	Rate of Return without assistance
	40%	7.40%

To understand the impact of increased revenues, we have performed a sensitivity analysis to determine the rate at which project revenues, both lease

rates and pad sale prices, would have to increase for the projected rate of return to be in excess of our feasibility benchmark without assistance. Table K illustrates the development would need to realize a 50% increase in project revenues for the project to be feasible without assistance. Given a 50% increase in project revenues, the project would have a rate of return of 7.34% which falls into the reasonable range.

Table K

Project Revenue Sensitivity	Increase in Project Revenue	Rate of Return without assistance
	50%	7.34%

As a final step in the sensitivity analysis, and to understand the impact of a combined change in project costs and project revenues, we have performed a sensitivity analysis to determine the rate at which these areas would have to change for the projected rate of return to be in excess of our feasibility benchmark without assistance. Table L illustrates the development would need to realize a combined 23% decrease in project costs and a 23% increase in project revenues for the project to be feasible without assistance. Given these changes in assumptions the project would have a rate of return of 7.40%.

Table L

Combined Sensitivity	Reduction in Project Costs	Increased Project Revenues	Rate of Return without assistance
	23%	23%	7.40%

The three tables above (Tables J, K, and L) indicate the magnitude at which project assumptions would have to change for the project as a whole to have a rate of return in excess of the 7.32% feasibility benchmark used in the sensitivity analysis. Absent changes of the magnitude outlined above, the project would not have a sufficient return to draw market investment. Only by assuming either increases in project revenues, decreases in project costs, or a combination of the two does the return increase to a feasible level without public assistance. However, we project changes of the magnitude outlined above are unlikely to be realized, which indicates the proposed project, when viewed as a whole, would not likely be completed through private enterprise alone.

6. "But For" Conclusion

The proposed development contemplates the construction of a 33,400 square foot commercial development including retail and restaurant uses. In addition, the Developer will undertake both onsite and offsite improvements necessary to redevelop the site. The Developer will bear all the risk until project completion and permanent financing is in place and continued operating risk thereafter. This level of risk demands a positive return with a comparable national market range of 5.50% to 10.50%, with an average of 7.32% as indicated in the *Korpacz/Price Waterhouse Cooper* study. As detailed above, the projected IRR to the Developer without assistance falls outside of the low-end of the range expected within the marketplace and significantly below the average return used as our feasibility benchmark. In comparison, the return with assistance is consistent with the average return used in our analysis.

A Blight Study prepared by JLL Valuation & Advisory Services dated July 12, 2017, and an affidavit signed by the Developer dated October 17, 2017 state that the redevelopment area is a blighted area and has not been subject to growth and development through investment by private enterprise and would not reasonably be anticipated to be developed without the adoption of tax increment financing. Based upon the Blight Study, Developer affidavit, and upon our analysis, Springsted concludes that the proposed Project, without assistance, would not likely be undertaken at this time without the requested assistance