



MEMORANDUM

To: City of Princeton
From: Tammy Omdal
Date: September 16, 2020
Re: Tax Increment Financing Assistance for Housing Project

The City of Princeton (the “City”) received an application from the Briggs Companies (the “Developer”) for public financial assistance to assist with the development and financing of certain project costs for the construction of two apartment buildings, constructed in phases, include approximately 49 rental units in each of the two buildings (the “Project”). The Proposed is proposed to be market rate with an affordable component.

The first building of the Project will be located along First Street and the second building will be located just behind the first building, on a site that is owned by the Developer. The first building is proposed to be completed and at 50% occupancy by 2022 and full occupancy by 2023. The second building is proposed to be completed and at 50% occupancy by 2024 and full occupancy by 2025. The Developer’s plan and timing is contingent on receiving public financial assistance to assist with the affordable component of the market rate building, among other items.

The cost for the Project (inclusive of 98 units, both buildings) is estimated at approximately \$15.4 million in today’s dollars. See Exhibit A for more information on the estimated Project cost, based on the Developer’s pro forma. The Developer’s request for public financial assistance is to assist with the extraordinary costs, including public improvements, and the cost to be provide the affordable housing units. The Developer has represented that it will not undertake the Project as proposed without public financial assistance. The timing of commencement of the Project has not been confirmed, but for planning purposes is anticipated to begin in 2021.

This memorandum provides a review of the request based on Northland’s analysis of the Developer’s application for assistance, including sources and uses of funds and operating pro forma for the Project. It is Northland’s opinion that the Project as proposed, which includes indoor parking, is unlikely to occur but for the proposed public financial assistance, inclusive of the tax increment financing. Without the assistance, the Project is not expected to achieve the level of debt service coverage and returns needed to secure the necessary private financing and equity.

The present value of the tax increment revenue available to reimburse the Developer for project costs on a pay-go basis over a 15-year term is approximately \$2.8 million. The future value of the total payments to the Developer, with interest at 3.0%, is estimated at \$3.6 million. The Developer requested a 25-year term. The additional 10 years would provide approximately \$1.6 million of additional tax increment revenues to reimburse project costs. Based on Northland’s analysis, the additional 10 years of assistance may not be necessary for the project based on current assumptions. This conclusion may change as the assumption for project costs are refined and updated by the Developer, including estimates for public improvements and development fees, for example.

The Developer's anticipated source of funds for the Project (as shown in the application) includes a combination of mortgage, contribution of the land, and deferral of the general contracting and development fees.

Public Financial Assistance

Due to the extraordinary costs associated with acquisition and development of the Project, the Developer is seeking public financial assistance from the City in the form of pay-go tax increment financing assistance. The tax increment revenue is proposed to come from the establishment of Tax Increment Financing District No. 9-2 (the "TIF District") within the existing Development District No. 9. The City plans to consider approval of the establishment of the TIF District, following a public hearing on September 24, 2020. The City will not consider approval of an agreement with the Developer for the financial assistance until a later date. Proposed terms for assistance have not been presented or agreed to by the Developer. The specifics for the Projects are subject to change.

The proposed plan for the TIF District is for the City to retain 100% of the increased net tax capacity from the Project to pay certain eligible project costs. The City may retain up to 10% of the tax increment derived from the Property to reimburse the City for the cost of administering the TIF District. The City may determine to use tax increments to pay for City costs incurred that are directly related to the housing project and/or to reimburse the Developer for eligible project costs. Eligible project costs may include land acquisition (the Developer is planning to establish a separate legal entity to own and manage the Project), costs of site preparation, street and utility improvements directly related to the housing.

Exhibit B provides a summary of the estimated potential tax increment cash flow from the TIF District, based on certain assumptions. State law provides that the increase in property taxes from the captured tax capacity (from the increase in market value) applied against the local tax capacity rates may be captured to assist the Project. Referendum market value taxes and the State of Minnesota property tax for commercial property (not applicable for residential property) are not captured for tax increment financing.

To reimburse the eligible costs incurred by the Developer, the City may determine to issue, and the Developer may purchase a Tax Increment Financing Revenue Note (the "TIF Note") in a maximum principal amount. Based on a 15-year term for the assistance, the maximum estimated principal amount is \$2.8 million. The TIF Note will be payable solely from net available semi-annual tax increments. Net available semi-annual tax increments is estimated to be based on 90% of the tax increment collected from the Project within the TIF District, subject to final negotiation and agreement with the Developer. The TIF Note is assumed to bear simple, non-compounding interest from the date that the City determines paid invoices, as paid by the Developer, in compliance with the terms of an agreement, at an estimated 3.0%, from the date of issue per annum. As noted, the terms for the TIF Note are preliminary for planning purposes and have not been negotiated with the Developer.

Review of Need for Assistance

Northland conducted a review of the Developer's application for financial assistance and pro forma as submitted to the City. Northland reviewed project cost estimates to ensure all anticipated sources and uses for the Project were properly included. Exhibit A provides information on the sources and uses of funds for the Project. Based on our review of the pro forma and under current market conditions, we find that the Project, as proposed, may not reasonably be expected to occur solely through private investment within the reasonably near future. Due to the costs associated with construction of the affordable housing units (among other extraordinary costs), the Project as proposed is feasible only through assistance, in part, from tax increment financing. This conclusion is supported by the following:

- The Developer plans for the estimated \$15.4 million cost for the Project to be funded from a combination of debt \$13.1 million (85.0%), and equity and deferred construction management and developer fees of \$2.3 million (15.0%). The present value of the estimated future tax increment revenue from the TIF Note payments to the Developer reduces the effective cost of the Project by \$2.8 million. Based on estimated net operating income, the effective return without the public financial assistance is not at a level the Project, as proposed, would proceed.
- The total average cost per housing unit is estimated at approximately \$157,000 (in today's dollars) for the construction of the 98 units, including the cost of the parking. Each building for the Project will include 13 studio units, 22 one-bedroom units, and 14 two-bedroom units. Based on Northland's experience with similar projects and given the location of the Project, we would expect total development costs to range between \$97,000 and \$160,000 per unit. The total per unit project cost is generally within this range.
- The estimated average gross monthly rent per unit for the first building, in the first stabilized year of the Project, is estimated at approximately \$1,054 per month (in year 2023). The Project is estimated to include three stories, with indoor and surface parking. Monthly average gross rents are estimated at \$636-\$950 for the studios, \$1,075 for a one-bedroom unit to \$1,200 for a two-bedroom unit. A minimum of 20% of the units are planned to be affordable at 50% of the average median income (AMI) for Mille Lacs County as of fiscal year 2020 is \$72,600). The annual total gross rental income for the first building is estimated at approximately \$620,000 in the first year of stabilized occupancy, before adjusting for estimated apartment vacancy and rental loss of 5%.
- The total annual expense, operating and non-operating, is estimated at \$5,125 per unit (after completion of both buildings). This includes a 5% management fee and approximately \$265 per unit (2%) for replacement reserve. This includes an estimated average \$3,091 per unit for real estate taxes. The contribution to reserves is reasonable and the projected total annual expense is within industry standards.
- The estimated average debt service coverage with tax increment financing is estimated to average 1.19X during the first five years of stabilized operations, and without tax increment assistance the average is 0.95X. The coverage for the mortgage without the tax increment is not at a level that we would expect the Project, as proposed, to proceed. The financing of this type of project would be expected to be at a minimum of approximately 1.2X coverage.
- The deferred construction fee and developer fee is projected to paid within the first ten years of operations. The beginning balance is estimated at \$1,025,000, and the pro forma assumes this balance will be repaid with interest at 3.0% rate.
- The estimated annual cash on cash return (net annual operating income divided by total development project costs) with tax increment financing is estimated to average 5.4% during the first five years of stabilized operations and 4.2% without tax increment assistance. The cash on cash return is reasonable for this type of project and the proposed source of financing.

Process for Approval

The first step in creating the TIF District is the adoption of a Tax Increment Financing Plan for the TIF District (the "TIF Plan"). The TIF Plan provides information about the Project to be funded with tax increment from the TIF district and authorizes the use of tax increment from the district to pay TIF-eligible project costs, among other items.

A tax increment financing district established by the City must be established within the boundaries of a Development District. The Development District is sometimes commonly referred to as a "Project Area". The City has previously established Development District No. 9. The boundaries of the Development District are proposed to be set to be contiguous with the boundaries of the City. When a new tax increment financing district is established by the City, the Development Program for the Development District, may be amended and supplemented from time to time. The Development Program is a written plan that contains the statement of objectives for the Development District and contains the information set forth in Minnesota Statutes. The Development Program may be included in the same document that contains the TIF Plan, but the two plans are separate and must comply with respective statutory requirements.

After the TIF District is established (TIF Plan adopted), the City may consider entering into a development (TIF) agreement with the Developer for tax increment financing assistance at a future date. The City plans for this to occur at a date following the public hearing date. The proposed terms of the agreement and project specifics are still under discussion between the City and the Developer.

Notice to County and School District

Before the public hearing and the establishment of a TIF district, the City must provide certain notices to the county and the school district, including providing a copy of a draft TIF plan. The county and school district may comment on the proposed TIF district but cannot prevent the creation of the TIF district. On behalf of the City, Northland submitted a letter and a draft copy of the TIF Plan for the TIF District to Mille Lacs County and Independent School District No. 477 on August 25, 2020 asking to receive written comments. As of the date of this memorandum no comments, written or oral, have been received by Northland.

Adoption of Modified Development Program and TIF Plan

Following the public hearing, the City Council may consider a resolution approving the modification to the Development Program for Development District No. 9 and the establishment of the TIF District within the Development District and the adoption of the TIF Plan relating thereto (the "Resolution"). The City Council may consider adoption of the Resolution on the same date of the public hearing (after closing the hearing) or a date following.

EXHIBIT A

**City of Princeton
Briggs Company Affordable Housing Project
Developer Sources and Uses of Funds for Construction**

	Total	% of Total	Per Unit
Sources of Funds			
First Mortgage	\$13,106,685	85.0%	\$133,742
Other Private Funds (Cash/General Contracting)	\$1,312,945	8.5%	\$13,397
Developer Equity	\$1,000,000	6.5%	\$10,204
Total Sources of Funds	\$15,419,630	100.0%	\$157,343

Uses of Funds			
Land Acquisition and Site Work	\$1,920,000	12.5%	\$19,592
Construction	\$10,939,970	70.9%	\$111,632
General Contracting	\$625,000	4.1%	\$6,378
Development Fee	\$400,000	2.6%	\$4,082
WAC and SAC	\$669,790	4.3%	\$6,835
Financing and Other Soft Costs	\$389,870	2.5%	\$3,978
Contingency	\$475,000	3.1%	\$4,847
Total Uses of Funds	\$15,419,630	100.0%	\$157,343

Number of Units 98

EXHIBIT B
City of Princeton
Tax Increment Financing District No. TIF District No. 9-2 (Housing)
Projected Tax Increment Cash Flow
Briggs Apartment Project

TIF District Year	PHASE I			PHASE II			TOTAL			Less Base Tax Capacity ⁴	Captured Tax Capacity ³	Original Tax Rate ²	Total Available TIF ⁷	Present Value of Total Available TIF ⁵	TIF Retained by City	PV of TIF Retained by City ⁵	TIF to Developer	PV of TIF to Developer ⁵
	Taxes Payable Value ^{1,6}	Market Value (TMV) ^{1,6}	Taxable Market Value (TMV) ^{1,7}	Taxes Payable Value ^{1,6}	Market Value (TMV) ^{1,6}	Taxable Market Value (TMV) ^{1,7}	Taxes Payable Value ^{1,6}	Market Value (TMV) ^{1,6}	Taxable Market Value (TMV) ^{1,8}									
1	2023	3,185,000				3,185,000	39,813	(1,229)	38,584	174.09%	66,930	65,292	6,693	6,529	60,237	58,762		
2	2024	6,433,700		-		6,433,700	80,421	(1,229)	79,193	174.09%	137,373	195,370	13,737	19,537	123,635	175,833		
3	2025	6,498,037		3,249,019		9,747,056	121,838	(1,229)	120,609	174.09%	209,217	387,665	20,922	38,766	188,295	348,898		
4	2026	6,563,017		6,563,017		13,126,035	164,075	(1,229)	162,847	174.09%	282,484	639,684	28,248	63,968	254,236	575,715		
5	2027	6,628,648		6,628,648		13,257,295	165,716	(1,229)	164,487	174.09%	285,330	886,773	28,533	88,677	256,797	798,096		
6	2028	6,694,934		6,694,934		13,389,868	167,373	(1,229)	166,145	174.09%	288,205	1,129,030	28,820	112,903	259,384	1,016,127		
7	2029	6,761,883		6,761,883		13,523,767	169,047	(1,229)	167,818	174.09%	291,108	1,366,549	29,111	136,655	261,997	1,229,894		
8	2030	6,829,502		6,829,502		13,659,004	170,738	(1,229)	169,509	174.09%	294,041	1,599,421	29,404	159,942	264,637	1,439,479		
9	2031	6,897,797		6,897,797		13,795,594	172,445	(1,229)	171,216	174.09%	297,002	1,827,738	29,700	182,774	267,302	1,644,964		
10	2032	6,966,775		6,966,775		13,933,550	174,169	(1,229)	172,941	174.09%	299,994	2,051,589	29,999	205,159	269,995	1,846,430		
11	2033	7,036,443		7,036,443		14,072,886	175,911	(1,229)	174,682	174.09%	303,015	2,271,061	30,302	227,106	272,714	2,043,955		
12	2034	7,106,807		7,106,807		14,213,615	177,670	(1,229)	176,441	174.09%	306,066	2,486,239	30,607	248,624	275,460	2,237,615		
13	2035	7,177,875		7,177,875		14,355,751	179,447	(1,229)	178,218	174.09%	309,148	2,697,207	30,915	269,721	278,233	2,427,486		
14	2036	7,249,654		7,249,654		14,499,308	181,241	(1,229)	180,013	174.09%	312,261	2,904,047	31,226	290,405	281,035	2,613,643		
15	2037	7,322,151		7,322,151		14,644,301	183,054	(1,229)	181,825	174.09%	315,405	3,106,841	31,541	310,684	289,841	2,800,000		
16	2038	7,395,372		7,395,372		14,790,744	184,884	(1,229)	183,656	174.09%	318,580	3,305,667	31,858	330,510				
17	2039	7,469,326		7,469,326		14,938,652	186,733	(1,229)	185,504	174.09%	321,787	3,500,603	32,178	350,603				
18	2040	7,544,019		7,544,019		15,088,038	188,600	(1,229)	187,372	174.09%	325,027	3,691,724	32,507	369,174				
19	2041	7,619,459		7,619,459		15,238,919	190,486	(1,229)	189,258	174.09%	328,298	3,879,105	32,828	387,910				
20	2042	7,695,654		7,695,654		15,391,308	192,391	(1,229)	191,163	174.09%	331,603	4,062,820	33,163	4,062,820				
21	2043	7,772,611		7,772,611		15,545,221	194,315	(1,229)	193,087	174.09%	334,940	4,242,939	33,490	4,242,939				
22	2044	7,850,337		7,850,337		15,700,673	196,258	(1,229)	195,030	174.09%	338,311	4,419,534	33,811	4,419,534				
23	2045	7,928,840		7,928,840		15,857,680	198,221	(1,229)	196,992	174.09%	341,715	4,592,672	34,175	4,592,672				
24	2046	8,008,128		8,008,128		16,016,257	200,203	(1,229)	198,974	174.09%	345,154	4,762,422	34,514	4,762,422				
25	2047	8,088,210		8,088,210		16,176,419	202,205	(1,229)	200,976	174.09%	348,626	4,928,850	34,826	4,928,850				
26	2048	8,169,092		8,169,092		16,338,184	204,227	(1,229)	202,999	174.09%	352,134	5,092,020	35,134	5,092,020				
						TOTAL =					7,683,755	5,092,020	4,085,933	2,295,863	3,603,798	2,800,000		

Key Assumptions for Cash Flow:

- 1 Taxable market value (TMV) annual growth assumption = 1.00%
- 2 Original Tax Capacity Rate estimated based on Taxes Payable Year 2020.
- 3 Election for captured tax capacity is 100.00%
- 4 Captured Tax Capacity is net of Base Tax Capacity calculated based on TMV = \$98,300.
- 5 Present value (PV) is calculated based on semi-annual payments, 3.0%, and date of 1/1/2023.
- 6 TMV calculated based on 49 units in Phase I and 49 units in Phase II for total of 98 housing units at an estimated average value of \$130,000 per unit
- 7 Total Available TIF (Tax Increment Financing) is net of State Auditor Fee of 0.36%.

EXHIBIT C
City of Princeton
Briggs Company Affordable Housing Project
Review of Developer Pro Forma
Summary of Pro Forma

Year of TIF District	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Gross Income (before TIF)	284,808	592,628	906,720	1,209,344	1,233,531	1,258,202	1,283,366	1,309,033	1,335,214	1,361,918	1,389,156	1,416,940	1,445,278	1,474,184	1,503,668
Less Expenses before real estate taxes	(75,996)	(123,036)	(171,170)	(195,456)	(199,365)	(203,352)	(207,419)	(211,568)	(215,799)	(220,115)	(224,518)	(229,008)	(233,588)	(238,260)	(243,025)
Less real estate taxes	-	(73,504)	(148,477)	(224,943)	(302,923)	(305,952)	(309,012)	(312,102)	(315,223)	(318,375)	(321,559)	(324,774)	(328,022)	(331,302)	(334,615)
Net Operating Income (NOI)	208,812	396,088	587,074	788,946	731,243	748,897	766,935	785,363	804,192	823,428	843,080	863,157	883,668	904,622	926,027
Plus TIF Revenue	-	60,237	123,635	188,295	254,236	256,797	259,384	261,997	264,637	267,302	269,995	272,714	275,460	278,233	281,035
NOI with TIF	208,812	456,325	710,709	977,241	985,479	1,005,694	1,026,319	1,047,361	1,068,828	1,090,730	1,113,075	1,135,871	1,159,128	1,182,855	1,207,062
Debt Service	150,000	415,091	565,091	830,183	830,183	830,183	830,183	830,183	830,183	830,183	830,183	830,183	830,183	830,183	830,183
Net Cash Flow before Payment on Deferred Developer Fee	58,812	41,234	145,618	147,058	155,296	175,511	196,136	217,178	238,645	260,547	282,892	305,688	328,945	352,672	376,879
Payment on Deferred Fees ²	58,812	41,234	145,618	147,058	155,296	175,511	196,136	217,178	238,645	260,547	282,892	305,688	328,945	352,672	376,879
Net Cash Flow after Payment on Deferred Developer Fee	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Cash Flow after Payment on Deferred Developer Fee	-	-	-	-	-	-	-	-	169,169	260,547	282,892	305,688	328,945	352,672	376,879
Cash on cost with TIF (NOI/TDC) ¹	1.4%	3.0%	4.6%	6.3%	6.4%	6.5%	6.7%	6.8%	6.9%	7.1%	7.2%	7.4%	7.5%	7.7%	7.8%
Cash on cost without TIF ¹	1.4%	2.6%	3.8%	5.1%	4.7%	4.9%	5.0%	5.1%	5.2%	5.3%	5.5%	5.6%	5.7%	5.9%	6.0%
Debt coverage with TIF ³	1.39	1.10	1.26	1.18	1.19	1.21	1.24	1.26	1.29	1.31	1.34	1.37	1.40	1.42	1.45
Debt coverage without TIF ³	1.39	0.95	1.04	0.95	0.88	0.90	0.92	0.95	0.97	0.99	1.02	1.04	1.06	1.09	1.12

Notes:
1/ Total Development Cost (TDC): \$15,419,630
2/ Assumes construction/development fee deferred. Pro forma assumes no construction management fee paid at closing. The pro forma above assumes the deferred fee is payable with 3.0% interest.
3/ Par amount of TIF note for Phase I is estimated at \$1.5M, 15 year term, 3.0% rate. Par amount of TIF Note for Phase II is estimated at \$1.3M, 15 year term, 3.0% rate. The source of funds does not assume a mortgage of the TIF note.