

# Mercantile Ground Lease Parcel Acquisition

Briefing to the Economic Development and  
Housing Committee

June 27, 2006

## Purpose

- Describe the provisions of the development agreement with Forest City ("FC Merc") for the Mercantile project as it pertains to the ground lease parcel under the Dallas Building.
- Describe how the actual acquisition of the ground lease parcel occurred.
- Detail staff's recommendation on amending the development agreement.

## The Development Agreement (“DA”)

- The main focus of the DA was the acquisition and development of the entire Mercantile Block into 375 multifamily units, 30,000 sq. ft. of ground floor retail and 375 parking spaces.
- The Mercantile Block was subject to a 99-year ground lease covering a 10,000 square ft parcel located at the southeast corner (the “Ground Lease Parcel” or “GLP”) of the Mercantile Block.

## The Development Agreement ("DA")

- Pursuant to the DA, FC Merc acquired the entire Mercantile Block and purchased the lessee's interest under the GLP.
- It was not financially feasible for FC Merc to develop the Mercantile Block with the ground lease in place.



## DA Provisions Concerning Acquisition of the GLP

- Section 1.02 of the DA provided that the costs to acquire the GLP by condemnation or deed in lieu of condemnation (the “Condemnation Costs”) would be shared by FC Merc and the City as follows:
  - FC Merc would advance the first \$3,500,000
  - City would pay the next \$2,500,000
  - FC Merc and City would share on a 50%-50% basis if the costs to acquire the GLP exceeded \$6,000,000

## DA Provisions Concerning Acquisition of the GLP

- Section 1.02 of the DA further provided that following acquisition of the GLP, the City would take fee title interest to the GLP but grant FC Merc an easement for an underground parking facility extending beneath the GLP.

## DA Provisions Concerning Acquisition of the GLP

- In March, 2006, the City sold Bonds as contemplated by, and provided for in, Section 6.02 of the DA.
- Such Bonds allocated \$2,500,000 to the possible future payment by City of Condemnation Costs in excess of the first \$3,500,000 of Condemnation Costs to be paid by FC Merc, as contemplated by, and provided for in, Section 1.02 of the DA.



## Settlement in lieu of Condemnation

- On November 2, 2005, the City Council authorized acquisition, including the use of eminent domain if necessary, of the GLP as contemplated by, and provided for in, Section 1.02 of the DA.
- In lieu of condemnation, FC Merc negotiated a settlement with the GLP owners and entered into a purchase agreement dated March 7, 2006, directly with them to acquire the fee simple interest in the GLP for \$4,000,000 in cash.

## Valuation of Ground Lease

Annual Ground Lease Payment	\$ 156,080
Discount Rate	4.00%
Net Present Value of Ground Lease	\$ 3,330,975
Residual Value of Land (2006 dollars)	\$ 1,000,000
Total Value of Ground Lease	\$ 4,330,975

Valuation reflects a guaranteed income stream through 2053.

## Settlement in lieu of Condemnation

- FC Merc is requesting that the City consent to FC Merc's acquisition of the fee simple interest in the GLP and amend Section 1.02 of the DA to conform to how the acquisition of the GLP actually occurred.
- As a result of this amendment the City is relieved of its obligation to pay any portion of the Condemnation Costs, and the City/DDDA may now reprogram \$2,500,000 of the proceeds of the Bonds for other projects in the DC TIF District.

## Acquisition of the ground lease parcel

- FC Merc consulted with OED, and received assurances that OED staff would recommend an amendment to the Mercantile DA allowing FC to acquire the fee simple interest in the ground lease parcel.
- FC Merc closed on the purchase of the ground lease parcel in May 2006.
- The amendment to the DA is scheduled for Council consideration on June 28, 2006.

## Purchase was preferable to condemnation

- The time required to conclude condemnation proceedings was unknown.
- Legal challenges were a possibility if the leasehold owners claimed the taking was illegal under state law.
  - State law is only one-year old.
  - No case law exists.
- Development of the entire block could have been delayed because of these uncertainties.

<b>Planned Acquisition</b>	<b>Actual Acquisition</b>
FC required to pay first \$3.5 million in condemnation costs and 50% additional above \$6 million.	FC paid \$4 million plus \$47,500 for initial City condemnation costs to acquire fee simple interest.
City required to pay next \$2.5 million in condemnation costs and 50% additional above \$6 million.	The City saved approximately \$547,500 in condemnation costs above first FC requirement of \$3.5 million.

<b>Planned Acquisition</b>	<b>Actual Acquisition</b>
City was to take fee simple interest in the parcel.	FC acquired fee simple interest in the parcel.
There was no limit to the liability of the City and FC for condemnation costs (both the cost of the parcel and the cost of litigation, including likely appeals).	City has spent no money on acquisition. City's liability capped at \$0 and \$2,500,000 of the bond proceeds of the bonds are now available for other projects in the DC TIF District.

<b>Planned Acquisition</b>	<b>Actual Acquisition</b>
<p>City would have granted a below-ground easement to FC for use as a private parking garage.</p>	<p>FC will construct an underground parking structure on its own property.</p>
<p>In the worst case, the owners could have prevailed in litigation and voided the City's taking of the property by eminent domain. This could have prevented completion of the project or delayed new construction.</p>	<p>All risk was eliminated and construction is proceeding as planned on the major economic development project in the core of downtown.</p>



## Option of Not Authorizing Development Agreement Amendment

- The recommended amendment to the DA simply revises Section 1.02 of the DA to conform to what actually occurred when FC Merc acquired the GLP.
- The amendment does not transfer the GLP from the City to FC Merc since the City never owned any portion of the Mercantile Block.
- If the City Council chooses not to authorize the amendment to the DA, the City would then request that FC Merc transfer the fee interest to the City pursuant to the original provisions of the DA.

## Option of Not Authorizing Development Agreement Amendment

- The City would have the additional time, expense and uncertainty of negotiating the conveyance of the GLP to the City reserving a mutually satisfactory underground parking easement.
- With title to the GLP in the City, only the underground parking easement would be on the tax rolls after the tax abatement expires.

## Recommendation

- It is recommended that the Economic Development and Housing Committee recommend to the full Council that it approve an amendment to the Mercantile development agreement to allow Forest City to acquire fee simple interest in the ground lease parcel.