DATE: November 5, 2015

SUBJECT: Approval of Non-Binding Letter of Intent between the County Board of Arlington County, Virginia and FC Ballston Common, LLC Related to a Potential Public-Private Partnership for the Ballston Quarter Redevelopment Project

C. M. RECOMMENDATION:

1. Approve the attached non-binding Letter of Intent (“LOI”) between the County Board of Arlington County, Virginia (the “County”) and FC Ballston Common, LLC (“Forest City”) that sets forth the proposed terms and conditions for a future development agreement detailing a public-private partnership for the Ballston Quarter redevelopment project and the County’s financial participation in its implementation.
2. Authorize the County Manager to execute the LOI, subject to approval as to form by the County Attorney.

ISSUES: Should the County Board approve the non-binding LOI as a next step in negotiating a development agreement for the implementation of a public-private partnership to facilitate redevelopment of the Ballston Common Mall and the broader Ballston area?

SUMMARY: The proposed non-binding LOI lays out the primary terms and conditions of a future development agreement that details a public-private partnership between the County and Forest City for the proposed Ballston Quarter redevelopment project, and which will be presented to the County Board for its consideration at a later date. The project’s transformative vision and scale are consistent with the County’s historic plans and future vision for Ballston where this retail and commercial development serves as a cornerstone for planning and development in the Ballston area as set forth in County planning policies, and a key economic anchor, both stabilizing the economic base but also spurring additional development and generating additional tax revenues. Given the magnitude of the public improvements needed to achieve this vision, as well as the complex, costly development and construction techniques associated with a redevelopment, there is a financial gap (currently estimated at approximately $55.5 million) that cannot be fully supported by private investment. Without the County’s
financial participation, the County would not realize the additional tax revenues and positive fiscal impact resulting from the project, and could also lose a fundamental element of the planning vision for Ballston.

The LOI lays out the tools the County intends to use for its financial participation in the project, including funding for garage and transportation improvements and the issuance of bonds through a community development authority (to be created by the County Board) that will be repaid by incremental tax revenues generated by the project. Additional terms of the LOI are focused on risk mitigation in the event of revenue shortfalls, the County’s financial participation in better than expected project performance, and responsibilities of each party in development of the project. More specific terms will be laid out in a development agreement that would require separate approval by the County Board in first quarter calendar year 2016. Additional approvals by the County Board will be required to create the community development authority and for issuance of bonds.

BACKGROUND: The Ballston Common Mall has historically been one of the cornerstones of commercial development in Ballston, and as such, has been the focus of significant County investment. In the mid 1980’s, the County completed its first public-private partnership at the current Ballston site that transformed the Parkington Shopping Center into a regional mall. Subsequent land use changes include expansions of both retail and office in the area. Finally, in 2006, the County completed its second public-private partnership for the Kettler Iceplex.

Over the last decade, the retail market has evolved significantly, driven by changing demographics (particularly millennials) and demand for mixed use, entertainment-oriented developments that are very different than the current Ballston format. Increased regional competition from the Mosaic District in Fairfax and the Southwest Waterfront and other areas in the District have further deteriorated Ballston’s position, especially in light of the significant public subsidies provided to these developments. Finally, the Ballston market faces very specific challenges due to the pending move of the National Science Foundation and the U.S. Fish and Wildlife Service to other jurisdictions. The combination of these factors and the resulting impact on the County’s economic and fiscal position have driven Forest City and the County to pursue a transformative redevelopment project that will be catalytic to Ballston and the broader County. The County Board first considered this proposed partnership at two separate meetings in June and July 2015.

DISCUSSION: The proposed redevelopment would transition the existing largely retail development into a mixed use project that includes a total retail square footage of approximately 621,000 square feet and provides a new 406 unit residential development (the redevelopment proposal is the subject of three site plan amendments also under consideration by the County Board). Because of the complex and costly development and construction requirements and the significant public infrastructure improvements needed, the project has a current estimated financing gap of $55.5 million, or 17.5 percent of total development costs. It should be noted that this estimate will change based on final design drawings, final construction costs, financing structure and interest rates.
The LOI describes the types of project costs associated with the financing gap that the public-private partnership could fund. These include improvements to the Ballston Public Parking Garage; transportation infrastructure along Wilson, Randolph and Glebe; plaza and pedestrian connections; and internal circulation with public access and vertical improvements such as facades. (Additional detail on potential partnership investments is found on page 3 of the attached LOI.)

The LOI provides a framework for the financing tools the County will consider using in the public-private partnership:

**Direct Public Funding** – The County will consider providing direct capital funding in three categories: 1) garage improvements (approximately $4 million) with funds derived from garage revenues and / or amounts previously allocated to garage improvements. Many of the proposed garage improvements were already anticipated in the County’s CIP; 2) transportation improvements (approximately $6 million) such as the Wilson Boulevard reconfiguration and pedestrian bridge replacement; and 3) public art elements for the pedestrian bridge (approximately $0.2 million).

**Community Development Authority Bonds** – Other improvements are expected to be funded through bonds issued by a community development authority (CDA). Debt service on the bonds would be repaid with incremental tax revenues generated by the redevelopment (tax increment financing, or TIF). A CDA is a development tool authorized by state statute that has certain powers that can help facilitate redevelopment projects or public-private partnerships; in particular, the CDA, if established by the County Board, has the ability to issue bonds to finance certain public improvements of the type anticipated in the Ballston Quarter project. The CDA also the ability to assess a special assessment or a special tax within the CDA boundaries in the event of a default on bonds backed by TIF revenues. The CDA would be established by the County Board at the request of the landowners, and the powers of the CDA would be limited to those authorized specifically by the County Board.

Under the proposed LOI, the CDA bonds would be repaid through incremental real property, sales and meal taxes generated by the redevelopment, specifically the properties owned by Forest City. As the County and Forest City negotiate the development agreement, the County may consider the addition of other nearby parcels to support the CDA bonds. To the degree TIF revenues are insufficient to pay debt service on the CDA bonds, a back-up special assessment and / or special tax would be imposed on the Forest City parcels to ensure bond repayment.

Under the County’s TIF policy, the amount of TIF within in a TIF area cannot exceed 40 percent (the remaining 60 percent would be retained in the General Fund). The County’s financial participation will be structured to meet this policy.

Based on current project and financing estimates, the proposed LOI anticipates that approximately $45-46 million in net project costs would be financed with CDA bonds. It should be noted that the actual size of the CDA bond issue will be larger than this amount due to bondholder-required reserve requirements, capitalized interest and issuance costs. Additionally, the estimated CDA amount will change based on final design and construction bids.
amortization structure, term, tax status, and other bond features will be determined through the development agreement and bond structuring process. The final interest rate and debt service schedule will be determined once the bonds have been sold, anticipated in late spring 2016.

The CDA bonds would not be considered debt of the County and would not be recorded on the County’s balance sheet; bondholders will rely solely on incremental tax revenues from the project and the back-up special assessment / special tax. In a severe downside scenario, failure of the developer to pay the back up special assessment could result in a lien being placed on the developer’s property for the benefit of bondholders. The CDA bonds will be unrated. The CDA bonds will not negatively impact the County’s bond ratings.

While the CDA / TIF approach has not been used before in the County, they have been used widely across the Commonwealth. Most recently, a CDA / TIF bond structure was used for the Mosaic redevelopment project in Fairfax County; the CDA bond issue totaled approximately $66 million. Fairfax County also accelerated and reprioritized various transportation projects to support the redevelopment; the total amount of public contribution approximated 21 percent of the overall Mosaic development costs. Henrico County has used a CDA structure for the Short Pump retail development (developed by Forest City) and two other retail / mixed use developments. Triple-A rated counties in Virginia using CDAs have included Prince William, Loudoun, Henrico, Hanover, Chesterfield, and Stafford for various projects including commercial and residential developments.

Other LOI Terms -- The LOI also includes preliminary terms related to Forest City and the County’s responsibilities for development of the project improvements and phasing. It notes that provisions related to performance thresholds for financing, tenanting and leasing will be developed as part of the development agreement. Finally, it includes a framework for the development of a lookback model so that to the degree the development exceeds its projected financial performance or that the project is sold, retirement of the CDA bonds may be accelerated.

FISCAL IMPACT: Net of current projections of CDA debt service, the proposed parcels in the redevelopment are estimated to generate additional incremental property, sales and meals taxes ranging from $152 - 167 million through 2045. In addition to those specific taxes, the redevelopment will generate additional BPOL, business tangible, and other revenues that go to the General Fund; similarly, incremental taxes associated with the commercial & industrial real property tax (dedicated to transportation) and the sanitary district tax (dedicated to stormwater) will accrue to those funds. If the County were to forgo the proposed public-private partnership, it is likely that Forest City would pursue a significantly more modest redevelopment with resulting lower incremental tax revenues. The projected difference in incremental tax revenues to the County if it pursues the proposed public-private partnership (vs. a significantly more modest redevelopment scenario) is $52 - $67 million.
NON-BINDING LETTER OF INTENT
Identifying Terms and Conditions
for Arlington County’s Potential Financial Participation in the
Ballston Quarter Redevelopment Project

This Letter of Intent (“LOI”), dated ____, 2015, between the County Board of Arlington County, Virginia (“Board” or “County”) and FC Ballston Common, LLC (“FCB”), the owner of the enclosed retail shopping center currently known as Ballston Common Mall and Ballston Acquisition Company, LLC, (“BAC”), the owner of the former Macy’s Furniture Site (FCB and BAC are together collectively referred to as “Forest City” or “Developer”), sets forth the terms and conditions upon which the County and Developer intend to enter into a Development Agreement related to the County’s financial participation in the implementation of the Ballston Quarter Redevelopment Project (as fully detailed in two currently pending amendment applications to Site Plan No. 193 filed by Developer (“Ballston Quarter” or “Project”). For the avoidance of doubt, the Project shall not include the minor site plan submission filed by [Ballston Air Rights Acquisition Company, LLC] with respect to the air rights office parcel located above the Macy’s Department Store that is adjacent to the enclosed mall.

BACKGROUND AND PURPOSE

Forest City is pursuing the redevelopment of its privately held sites currently consisting of the Ballston Common Mall (“BCM,” RPC# 14-059-035, RPC# 14-059-036) and the adjacent Macy’s Furniture Site (“MFS,” RPC#14-059-028). These three parcels comprise the defined Taxable Properties.

As proposed in its minor site plan submission, FCB would redevelop and reposition the existing BCM structure, with only a nominal increase of approximately 11,854 square feet, and BAC, in accordance with its major site plan submission, would redevelop the MFS with approximately 406 residential units and approximately 66,475 square feet of retail. This LOI does not presuppose, and is contingent upon, Board approval of the special exception site plan amendments required to realize this proposal.

At a public meeting of the County Board on June 16, 2015, Forest City presented the proposed Project to the Board as an informational item and requested that the County consider public financial participation through a form of public-private partnership. At that time the Board directed the County Manager to study the issue and report back at the July County Board meeting. On July 21, 2015, during the County Manager’s report, the County Manager reported back his findings and recommended to the Board that the public-private partnership warranted more detailed analysis. At that time the Board directed the County Manager to work with Forest City on a public-private partnership structure that could be considered by the Board at a later date.

This LOI affirms the following findings:

- The proposed Ballston Quarter requires significant public infrastructure improvements and complicated and challenging development techniques, in order to achieve the transformative vision that is proposed and is regarded as in the best interest of the County to facilitate.
- The cost of the public infrastructure improvements and complicated development techniques result in a financial gap in the return on private investment necessary to develop the transformative and impactful Project that is proposed, and thus cannot be fully supported by private sector investment.
• The scale and transformative vision of the proposed Ballston Quarter is consistent with the vision for development in the Ballston area as set forth in the County’s planning policies, and will provide substantial public benefits to stabilize the broader economic base of the Ballston neighborhood as well as act as a catalyst for future dynamic growth to the Ballston fiscal base.

• It will ensure that, as articulated in County planning policies, the area will avoid future economic distress and promote continued redevelopment and growth in the Ballston area.

• The incremental tax revenue expected to be generated directly by the Project justifies public participation in this Project, specifically the leveraging of tax revenues that would not be available “but for” the undertakings made by the County to realize the full vision of the Project.

• The County has public finance tools available at its disposal which allow the County to effectively and efficiently participate in the Project.

• A public-private partnership structure can be established that limits direct risk to the County’s General Fund while also allowing for participation in the Project’s financial upside.

• Financial participation by the County in the Project is in the near and long-term fiscal interests of the County.

The purpose of this LOI is to summarize the significant terms and conditions of a future Development Agreement between the County and Forest City for the proposed development of the Ballston Quarter. This LOI is non-binding and contingent upon further negotiation and Board approval of such Development Agreement. The Development Agreement will reflect more refined construction costs, and will provide a more refined level of detail related to all aspects of a potential public-private partnership. The LOI is not intended to limit the scope or provisions of the Development Agreement and, thus, terms and conditions other than those set forth herein may be agreed upon in the final Development Agreement.

POTENTIAL PUBLICLY FUNDED IMPROVEMENTS IN THE PROJECT

Table 1 below outlines the types of publicly funded improvements that are considered appropriate and necessary to achieve the transformative vision and catalytic impact of Ballston Quarter.

The size of the private development gap upon which the scale of County’s potential participation has been based was determined through a detailed analysis of the Project economics by County staff and its consultants. The financial gap for the Project was determined based upon a pro forma analysis of the Project’s estimated costs and revenues with a target return on cost of 6.3%, based on the projected first year stabilized net operating income (NOI) in relation to total net project cost. The financial model incorporated both new Project Costs and incremental NOI and excluded the current NOI of the Developer’s assets. The Project costs included all estimated private and public infrastructure costs associated with the Project. The County and Developer have agreed that this method for determining the Project’s economic feasibility, including the determination of the target return on cost, is valid and appropriate. The Developer commits to provide updated cost, revenue, and financing assumptions, when such updated information is available, resulting in a change in the size of the gap before final approval of a Development Agreement.

Based upon this financial analysis, the private development gap for the project was calculated at approximately $55.5M, or 17.5% of total project costs.

Table 1. Potential Publicly Funded Improvements in the Project
<table>
<thead>
<tr>
<th>Type of Publicly Funded Improvement</th>
<th>Description</th>
<th>Approximate Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>County-Owned Assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Garage Improvements</td>
<td>Elevator replacements, lobby upgrades, wayfinding &amp; traffic control, Glebe Rd façade (false face to conceal existing bridges)</td>
<td>$8.9M</td>
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<tr>
<td>Public Infrastructure</td>
<td></td>
<td></td>
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<tr>
<td>Wilson Boulevard Streetwork &amp; Streetscapes</td>
<td>Narrowing of Wilson Boulevard, removal of median, associated streetscape work</td>
<td>$3.6M</td>
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<tr>
<td>Streetscapes</td>
<td>Sidewalk and transit facility upgrades on Wilson, Randolph and Glebe</td>
<td>$1.1M</td>
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<tr>
<td>Pedestrian Bridge</td>
<td>Removal of existing bridge structure and construction of new above-grade bridge connecting Ballston Quarter and Stafford I</td>
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</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td></td>
<td>$7.4M</td>
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<tr>
<td>Publicly Accessible Elements</td>
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<td></td>
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<tr>
<td>Plaza/Mews</td>
<td>Hardscaping and design elements for plaza and mews; façade demolition</td>
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<tr>
<td>Circulation/Connections</td>
<td>“Blade” vertical circulation and Randolph pedestrian connection</td>
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<tr>
<td><strong>Subtotal</strong></td>
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<td>$9.4M</td>
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<tr>
<td>Buildings/Development</td>
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<tr>
<td>Vertical Improvements incidental to public improvements</td>
<td>Façade remodeling &amp; façade demolition/construction incidental to public improvements</td>
<td>$14.8M</td>
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<tr>
<td>Internal Circulation</td>
<td>Internal pathways and related vertical circulation that will have public access easements</td>
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<td><strong>Subtotal</strong></td>
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<td>$29.8M</td>
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<tr>
<td><strong>TOTAL</strong></td>
<td></td>
<td><strong>$55.5M</strong></td>
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</table>

PUBLIC FINANCE TOOLS

The County Manager will present to the Board for its consideration the following public-private partnership utilizing two sources of public financing, as outlined below:

*Direct Public Funding: Approximately $10M*

The Board shall consider the appropriation of available funds for specific capital improvement projects in two areas: 1) improvements to the County-owned parking garage (~$4M) utilizing existing and future garage improvement funds derived from garage revenues and amounts previously allocated for garage improvements; 2) transportation capital projects (~$6M), such as the Wilson Boulevard rebuild, the removal and reconstruction of the Wilson Boulevard pedestrian bridge, and public streetscape elements funded through available transportation capital funds; and 3) public art elements and design
enhancements to the pedestrian bridge (~$200k) utilizing existing and future funds (including the $75k contribution through the residential building site plan) in the public art trust and agency account designated for use in the Ballston area. To the extent such funds are not available, the associated cost of investments would be covered through a larger than currently anticipated bond issuance described below.

Community Development Authority Bond Issue: Approximately $45.5M

The remainder of the publicly funded improvements plus related costs of issuance and required reserves is expected to be funded through bonds issued by a Community Development Authority (CDA) that the Board will consider establishing at the time the Development Agreement is considered for a district that encompasses the Taxable Properties. The expected public improvements and any improvements necessary and incidental to the public improvements to be funded through the CDA are currently estimated at $45.5M, although the actual size of the bond issuance(s) will be determined by the more refined costs of these improvements as well as associated costs of issuing the bonds, any required reserves and capitalized interest on the bonds. The Development Agreement shall detail the governance, structure and purposes of the CDA, the size of future bond issuances, the term and amortization structure of the bond, and expected use of tax-exempt versus taxable bonds.

The CDA bond will be repaid primarily through three sources of incremental tax revenues: 1) real property tax; 2) sales and use tax; and 3) meals tax. The incremental tax revenues will be associated with the defined Taxable Properties, but may also include additional parcels such as the Macy’s and the office buildings as part of the overall source of incremental tax revenues (any such additional parcels, together with the Taxable Properties, the “TIF Area”). Should TIF revenue be insufficient, the bonds would be paid by a back-up special assessment or special tax levied against the Developer owned Taxable Properties, as more fully discussed below.

The specific blend of incremental tax revenues used to repay the CDA bond will be set forth in Development Agreement. Per the County Board approved Tax Increment Finance Policy, the incremental taxes pledged to repay the CDA bond cannot exceed 40% of total incremental taxes, including the sources identified above but also including other tax revenues associated with the Project or the TIF Area that are not expected to be pledged for repayment of the CDA bond.

FURTHER TERMS AND CONDITIONS

The County and the Developer agree that the following terms and conditions will be included, as such may be further refined, in the Development Agreement.

1. CDA SPECIAL ASSESSMENT/SPECIAL TAX BACKSTOP

A special assessment or a special tax may be imposed on the Developer-owned Taxable Properties as necessary. The special assessment/special tax would be levied and/or collected only in the event that incremental tax revenues are insufficient to meet annual CDA bond payment obligations. The amount of the special assessment/special tax will be determined on any given year by the necessary revenue required to meet all CDA bond obligations. The Developer acknowledges that the County may exercise its full rights and remedies in collecting delinquent special assessments/special taxes and to enforce any special assessment/special tax liens that are in arrears. The potential for a special assessment/special tax will stay in place until all CDA bond debt is retired.

Further, as long as there is the potential for a special assessment/special tax on the identified properties:
• The new construction residential building proposed as part of Ballston Quarter will not be allowed to create residential condominium units. The commercial component of the residential tower will be eligible for conversion to a condominium unit.

• The Developer, or any future landlord, must include in all residential and commercial leases a clause that limits the amount of Special Assessment taxes in any year that can be passed on to the tenants. The specific limits on special assessment/special tax pass-throughs will be detailed in the Development Agreement.

2. ALTERNATIVE FINANCING MECHANISMS

The Developer and County shall continue to explore alternative financing mechanisms to the currently proposed CDA structure. These mechanisms may include (but not be limited to) Developer financing secured with the incremental taxes described above as well as the Developer purchase of the CDA bonds. Considerations for alternative financing mechanisms include transparency, efficiency, cost and risk.

3. LOOKBACK MODEL

A Lookback Model is wholly appropriate and necessary given the significant public participation in the Project. Such Lookback Model shall recognize that the Developer should benefit from better than estimated market performance, given the risk associated with the private capital investments. Accordingly, the Lookback Model will set financial terms which, if exceeded by the Project, returns an agreed upon proportionate share of the excess return to the County to accelerate the retirement of the outstanding CDA debt or, as may be agreed upon, serve as reimbursement for County directly funded improvements related to the Project. The Lookback Model shall coincide with the term of the CDA bonds and shall include a provision that evaluates both excess return on an annual basis and excess return in the event of a sale or transfer of ownership.

3. DEVELOPMENT OF IMPROVEMENTS

The Developer is responsible for constructing (design, contracting, project management and physical construction) all of the improvements outlined as part of this public-private partnership, based upon an approved set of plans, project budget and appropriate reserves for cost overruns, unless the County agrees in writing to be responsible for such construction. The Developer will be reimbursed for the costs related to its construction of the County funded improvements, including related soft costs, fees and overhead expenses. The County and the Developer will develop a process for monitoring the costs of the improvements from design to completion that the County is funding and that are designed and or constructed by the Developer.

CDA bond proceeds may not be used to pay for infrastructure improvements or private development costs not explicitly outlined as part of the future Development Agreement.

4. PHASING OF DIRECTLY FUNDED IMPROVEMENTS BY THE COUNTY

The County and the Developer will develop a phasing plan to ensure that any directly funded improvements by the County in County owned assets will occur in concurrence with or after milestone investments by the Developer. The phasing plan shall be structured to avoid negatively impacting the commencement of construction (projected to be May 15, 2017) and the opening date of the Project (projected to be April, 2018) or its post occupancy market performance.
If directly funded improvements are made by the County in accordance with plans and budget approved by Developer, but the Project ultimately is not delivered in its approved form or is significantly delayed, then the Developer shall fully reimburse the County for the full capital expenditure associated with such improvements. The detailed terms of the timing and amount of such reimbursements will be addressed in the Development Agreement.

5. DEVELOPER COMMITMENT TO DELIVERING COMPLETE PROJECT

The Developer commits to using commercially reasonable efforts to develop the Project simultaneously. The Development Agreement will lay out conditions upon which County and CDA investments are predicated upon development and financial milestones.

6. PERFORMANCE HURDLES – TENANTING & LEASING

The realization of the proposed tenant mix is critical to the County’s participation in the Project. The Developer and County shall develop a commercially reasonable leasing strategy, with defined tenant mix and targets and key performance metrics and hurdles. County funding and issuance of CDA bonds shall be dependent upon meeting hurdles outlined in this leasing plan.

7. PERFORMANCE HURDLES – FINANCING

The Developer and County shall set commercially reasonable performance hurdles and metrics relative to the private financing of the Project, including but not limited to, the relationship of private equity to public debt in the public private partnership. County funding and issuance of CDA bonds shall be dependent upon meeting the defined private financing performance hurdles, unless otherwise amended by the County.

{signatures on the following page}
IN WITNESS WHEREOF, the County Board and Forest City have executed this Letter of Intent as of the date set forth below:

County Board of Arlington County

FC Ballston Common, LLC

Ballston Acquisition Company, LLC