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MEMORADUM

To: Marti Praschan, Chief Financial Officer, City of Ann Arbor
John Fournier, Deputy City Manager, City of Ann Arbor

From: Kevin Plenzler, Director

RE: Oxford – Southside Development – Work Statement 3

The City of Ann Arbor, MI ("City") engaged PFM Group Consulting LLC ("PFM") via Work Statement No. 3 ("WS3") regarding the Oxford Companies, LLC of Ann Arbor's ("Oxford" or "Developer") multi-use development project ("Southside Redevelopment") within the Transit Corridor District ("TC1 District"). Oxford has requested City participation in funding and operating multiple parking structures in support of the project. Parking structure financing program options were proposed to the City including utilizing the Brownfield Program. PFM provided an initial analysis of the Oxford project as part of Work Statement No. 1 ("WS1") in October 2023 and an updated study in April 2024.

Per the City's WS3, the Developer of the Southside Redevelopment has requested City participation in funding and operating multiple parking structures in support of the project with the City wanting to evaluate a privately owned and operated facility, which would receive tax increment financing reimbursement from the project ("TIF Reimbursement Scenario"). The City requested PFM to examine the most recent Developer financial model for the proposed Southside Redevelopment. The scope of services associated with WS3 is provided below:

1. Preliminary review of the Developer-owned reimbursement scenario using the initial development pro forma and phasing schedule.
2. This initial analysis will quantify the estimate net operating income associated with the three proposed parking decks; as well as the estimate amount of real estate revenue from the parking decks assuming they are owned and operated by the Developer.
3. Participation in the Arbor South Work Session of City Council
4. Complete a full economic/financial analysis of a Parking Deck Reimbursement scenario to ascertain viability.
5. Meet with Development and City teams to gather the necessary data to complete an in depth financial and economic analysis of the alternative scenario.
6. Analysis shall include an estimate of the developer's return on investment in this alternative scenario
7. Determine the amount of the subsidy the city would be providing in this alternative scenario
8. Ascertain pros and cons of both the original proposal and the alternative scenario

The City quotes an industry standard of 10% ROI for developers, which is not necessarily defined as there are multiple measures that benchmark a developer or investors ROI. In this case, PFM focused on the internal rate of return ("IRR") for comparative purposes. PFM's experience suggests that a typical developer/investor involved with a real estate project of this complexity is typically looking for an internal rate of return ("IRR") of 15% to 25% to compensate for the relative risk of the investment compared with other investment alternatives. In addition, PFM compared the average annual Return on Equity (ROE) of the TIF Reimbursement Scenario.

In November 2024, PFM provided preliminary analysis using the April 2024 model and data to evaluate the potential viability of a privately owned and operated facility, which would receive tax increment financing reimbursement. This initial research was inconclusive at the time given that an updated model had not yet been provided in advance of the November 12, 2024, City Council Work Session. Since then, an updated Developer pro forma (December 2024) model was provided and analyzed.

CONCLUSIONS

The most recent analysis of the Developer's December 2024 pro forma model indicates that the alternative TIF Reimbursement Scenario for a privately owned and operated project resulted in an IRR of 10.38% and a ROE of 7.20% which fall short of typical investment hurdles.

The most recent analysis of the Developer's December 2024 pro forma model indicates that the Developer's request of the City's participation via the financing of the structured parking elements of the proposed Southside Redevelopment by the City is necessary to meet the typical investment hurdle for a multi-phases mixed-use project. The proposed City-financed option results in an IRR of 16.06% compared to the IRR when purely privately financed at 6.22%. Also, per the most recent analysis and review of the Developer's pro forma model, the Developer's request of the City's participation in the Southside Redevelopment meets the general guidelines of the City's ROI policy.

I. Developer's Estimated ROI – Internal Rate of Return (IRR)

The financial pro forma model provided by the Developer is a dynamic model allowing for estimates of IRR and ROE with and without the private financing of the structured parking elements. Since the modeling in April 2024, the development plan has been modified with the inclusion of an additional 188 structured parking spaces as well as 88 residential multi-family units. With respect to the IRR detailed herein, it is a levered IRR assuming capital events, the majority of which occur in Year 10. The IRR and ROE results are as follows when answering Yes or NO to both of the following questions embedded in the financial pro forma model:

- Garage cost included in Private Cost?
- Garage NOI allocated to Private Cost?

Table 1 summarizes the results with respect to IRR and ROE when modeling the following: 1) City financed structured parking, 2) Privately funded structured parking and 3) privately funded structured parking with 100% TIF reimbursement.

Table 1. Estimated Project IRR

	Apr-24	Jan-25
IRR (10-Year)		
Garages City Financed	14.26%	16.06%
Garages Privately Financed	4.24%	6.22%
Garages Privately Financed - Reimbursed	9.48%	10.38%
Avg Annual ROE (10-Year)		
Garages Privately Financed - Reimbursed	6.35%	7.20%

Source: Developer

With respect to the latest model, the modeling indicates that when including the associated costs and resulting garage NOI via Developer financing, the resulting 10-Year IRR is 6.22%. Alternatively, if the garage costs and associated garage NOI are excluded, the resulting IRR is 16.06%. This data suggests that the requested City participation benefits the project and results in achieving the respective market IRR hurdle rate. When assuming a privately funded project with TIF reimbursement, the resulting 10-Year IRR is 10.38% with average annual ROE of 7.20%.

II. Estimated Garage NOI and Real Estate Taxes

Applying the latest development program, net operating revenues and real estate taxes were estimated for the structure parking garages (see Table 2). The Developer financial pro forma includes the following development volumes based on the most recent revised development program (Figure 1 and Figure 2).

Table 2. Estimated Project Land Value

	Total NOI*	Total RE Taxes	Time Period
Garage A	$29,804,022	$17,659,614	2028-2057
Garage B	$33,989,248	$18,654,526	2028-2057
Garage C	$26,313,166	$19,838,982	2032-2061
TOTAL	**$90,106,437**	**$56,153,122**	

*NOI excludes RE Taxes

Source: Developer

Figure 1. Southside Redevelopment Volumes

Southside Redevelopment- Ann Arbor, MI							
Programming							
Phase	Building	Use	MF Units	Square Feet	Keys	Spaces	For Sale Units
Phase 3	A1	Hotel		97,434 SF	150 Keys		
Phase 3	A3	Multifamily	121 Units	115,619 SF			
Phase 3	A3	Commercial		4,981 SF			
Phase 3	A2	Garage		254,296 SF		778 Spaces	
Phase 3	A6	Retail		9,810 SF			
Phase 3	A6	Condo/ For-Sale		60,853 SF			30 Units
Phase 4	A4	Commercial		3,244 SF			
Phase 4	A5	Commercial		3,124 SF			
Phase 2	B1	Multifamily	188 Units	194,635 SF			
Phase 2	B1	Commercial		41,292 SF			
Phase 2	B2	Garage		287,700 SF		876 Spaces	
Phase 4	B3	Multifamily	152 Units	156,600 SF			
Phase 4	B3	Commercial		11,522 SF			
Phase 5	C1	Multifamily	109 Units	121,288 SF			
Phase 5	C1	Commercial		8,234 SF			
Phase 5	C4	Commercial		3,906 SF			
Phase 6	C3	Multifamily	239 Units	222,664 SF			
Phase 6	C3	Retail		11,551 SF			
Phase 6	C2	Garage		250,502 SF		822 Spaces	
Phase 6	D2	Multifamily	94 Units	88,400 SF			
Phase 1	D1	Multifamily (Affordable)	210 Units	134,004 SF			
			1,113	**2,081,659**	**150**	**2,476**	**30**

Source: Developer

Figure 2. Southside Redevelopment Project Map

Source: Developer

III. Estimated Project Cash Flow and Garage Costs

Based on the latest information provided in the Developer financial pro forma, the total cost of the three structured parking decks (totaling 2,476 spaces) is $130.6 million, which is inclusive of land, hard costs and soft costs. A review of the latest modeling indicates that once each of the structured parking decks are built, the combined average annual facility and operation costs to run all three is approximately $1.9 million and the total estimated facility and operation costs through 2058 is $57.1 million.

When looking at the impact to the overall project cash flow, by either excluding (or including) the structured parking in the model, the net result is an estimated $130.6 million (Table 3).

Table 3. Estimated Project Cash Flow (Total)

	Apr-24	Jan-25	Difference
Project Cash Flow (2026-2039)			
NO (garages excluded)	$175,177,342	$281,380,567	
YES (garages included) - Reimbursement	$71,820,000	$152,117,268	
Difference	$103,357,342	$129,263,299	$25,905,957
Est. Garage Costs	$104,309,734	$130,609,655	$26,299,921

Source: Developer and PFM Group Consulting LLC

As the data above indicate, project cash flows have changed dramatically over the last year. Per discussions with Developer, more detailed and market specific information has been gathered resulting in adjustments to the forecast revenues while also adjusting for site-specific and local development costs. In addition to the forecast revenues and expenses, as described above, there was also a net increase in development volumes with respect to the addition of 88 multi-family units as well as an addition of 188 additional structured parking spaces.

As part of its analysis, PFM reviewed and compared the total garage costs as provided in the Developer financial model and compared those to another recognized structured parking development cost source. Table 4 summarizes the resulting comparative estimates. As the data shows, the current total cost estimates per space are comparatively high and represent a potential area for savings. Note that the comparative costs do not fully incorporate new requirements with respect to sprinklers and EV charging which results in increased development costs. It’s understood that the Developer is continuing to review and revise its construction cost estimates as it discusses the project with contractors.

Table 4. Garage Cost Estimates

	Developer	WGI Outlook (2025)*		
	Jan-25	Detroit	Median	High
Total Garages (A2-B2-C2)	$130,609,655	$75,786,200	$76,014,243	$92,792,194
Spaces	2,476	2,476	2,476	2,476
Hard Costs$/space	$37,088	$30,608	$30,700	$37,477
Total Costs$/space	$52,750	$39,791	$39,911	$48,720

*WGI Outlook 2023 with 2.9% CPI annual inflator; however, the costs do not fully incorporate new requirements with respect to sprinklers and EV charging

Source: Developer and PFM Group Consulting LLC

IV. TIF Reimbursement Scenario and Subsidy Estimates

The TIF Reimbursement Scenario represents an alternative to the proposed City financing of the structured parking as currently proposed by the Developer. In the TIF Reimbursement Scenario, the Developer would privately develop, own, and operate the Southside Redevelopment with the City committing all future TIF revenue resulting from the project improvements to the Developer (Property Owner).

When the garage cost(s) (land, hard costs, and consultant fees) get incorporated into the private building proforma the financing cost increases along with the construction management fee, development fee, insurance (% of cost estimate) and contingency. The net result is an increase in $6.6 million in garage costs (see Table 5).

Table 5. Additional Costs Associated with Private Garage Financing

Garage Included – Yes (Private)	$605,861,188
Garage Included – No (Public)	$468,694,935
Delta	$137,166,252
Garage Costs	$130,609,655
Difference (private financing costs)	$6,556,597

Source: Developer

The financing of the structured parking is reliant on two revenues sources: 1) parking garage NOI and 2) TIF revenues. PFM estimates that the Southside Redevelopment net present value of the future Parking Garage NOI is $46.6M (assuming a 4.25% discount rate through 2058). PFM estimates that the Southside Redevelopment net present value of the future TIF revenue to be $162.1M (assuming a 4.25% discount rate through 2058).

Table 6. Parking Garage NOI and TIF Revenues Estimates (Total and NPV)

	Est. Parking NOI			
	PH 1	PH 2	PH 3	TOTAL
Total	$29,804,022	$33,989,248	$26,313,166	$90,106,437
NPV	$15,364,052	$17,345,126	$13,846,838	$46,556,016
	Estimated TIF			
TIF	PH 1	PH 2	PH 3	TOTAL
Total	$108,445,421	$94,434,448	$120,218,243	$323,098,113
NPV	$54,740,992	$49,757,366	$57,624,161	$162,122,520
TOTAL NPV	$70,105,044	$67,102,492	$71,471,000	$208,678,536

Source: Developer and PFM Group Consulting LLC

The TIF Reimbursement Scenario assumes a privately owned and operated Southside Redevelopment with the forecasted Parking Garage NOI is retained by the Developer as well as the future TIF being retained by the Developer and that the TIF Reimbursement Scenario commits the future project TIF increment to the Southside Redevelopment.

The proposed City financing of the Southside Redevelopment structured parking assumed a total commitment of $146M in bonds across three issuances (final sources and uses still to be determined). Based on the information in Table 6, the debt service on the bonds is secured by the Parking Garage NOI and TIF revenues. Using these estimates, PFM estimates that the resulting subsidy provided via the TIF Reimbursement Scenario is $62.6M. The TIF Remaining represents the estimated present value of future project revenues foregone.

Table 7. TIF Reimbursement Subsidy Estimate

City Financing of Garage (Total Par)	$146,090,000
Parking NOI	$46,556,016
Remaining	$99,533,984
Southside Redevelopment PV of TIF	$162,122,520
TIF to Service City Bonds	$99,533,984
TIF Remaining	$62,588,536

Source: Developer and PFM Group Consulting LLC

V. City-Financed Structured Parking vs. TIF Reimbursement Scenario

A City-financed structured parking facility as initially proposed provides the project the lowest cost of capital and reduces the net operating costs of the structured parking by eliminating property taxes on the structured parking. However, in the City-financed option, the City is taking on the project risk such that if the parking garage NOI and TIF revenue is not sufficient to cover the debt service, the City's general fund represents the source of payment for the shortfall.

In addition, the City-financed option will require the City to operate and manage the structured parking or enter into an operating agreement with the Developer to operate the garages and remit the parking revenues back to the Developer. Also, with respect to the City-financed structured parking, while the City takes on the risk of the project not performing, conversely, if the project does perform and generates Parking Garage NOI and TIF revenues more than the project debt service, it can use those funds to finance other City infrastructure priorities.

The main benefits to the City regarding the TIF Reimbursement Scenario is that it does not use the City's bonding capacity and reserves that capacity for other City initiatives, and it removes the risk of the potential Southside Redevelopment's non-performance and the associated responsibility of servicing the future debt service of the project. As illustrated above, the estimated cost to insulating the City from that project risk is estimated at $62.6M.