

PORT OF PORT TOWNSEND AGENDA COVER SHEET

MEETING DATE	April 11, 2018
AGENDA ITEM	<input type="checkbox"/> First Reading <input type="checkbox"/> Second Reading <input checked="" type="checkbox"/> Regular Business
AGENDA TITLE	VII. C) Northwest Maritime Center Point Hudson Proposal Analysis
STAFF LEAD	Sam Gibboney
REQUESTED	<input type="checkbox"/> Motion <input checked="" type="checkbox"/> Possible Action <input type="checkbox"/> Discussion
ATTACHMENTS	A. Info Memo B. ECONorthwest Point Hudson Analysis C. RedFern Consultants

PORT OF PORT TOWNSEND

INFORMATIONAL MEMO

DATE: 4/11/2018
TO: Commission
FROM: Sam Gibboney, Executive Director
SUBJECT: Analysis of offer from Northwest Maritime Center

ISSUE

The Northwest Maritime Center (NWMC) has presented a proposal for the lease and operation of Point Hudson. The purpose of this memo is to provide a framework for discussion in open session of the issues that might affect the minimum price at which this property might be leased. Each factor must first be discussed in open session without reference to the specific dollar impact on the bottom line price. After this public discussion has occurred, the Commission may go into executive session to discuss how this factor will impact the bottom-line price, without making those factors the focus of discussion. The final decision regarding the leasing of this public property must be taken in a meeting open to the public.

BACKGROUND

The Port and the NWMC (along with participation by the City of Port Townsend) has met for many months to discuss various options for partnership regarding Point Hudson. The NWMC presented a proposal dated January 26, 2018. The Commission has previously received a copy of the proposal. A copy of the proposal is not attached in hard copy to this memo. A link to it will be provided on the Port's website.

At the Port special meeting on March 20, 2018, the Commission directed staff to develop a counter proposal.

Two other analyses have been provided to the Commission: *A Financial Assessment of the Port Hudson Proposal* by ECONorthwest, and *An Analysis of the Various Outcomes of a Lease between the Port of Port Townsend and NWMC* by Red Fern Consulting. Both documents are attached to this memo.

DISCUSSION

The factors that affect the future of Point Hudson are complex, and this memo does not seek to present either a comprehensive evaluation or scenario analysis. Rather, the intention is to present a framework for discussion that can inform and educate the Commission as it faces the fundamental question: to lease or not to lease? And more specifically, should the Commission lease to the NWMC given the proposed terms?

To answer this question, the Commission should consider the following factors:

- **Debt Service.** The question that will affect the minimum acceptable price is: should the NWMC lease provide the financial resources to cover the debt service associated with Point Hudson?
 - The existing debt on the property was incurred to rehabilitate the marina and two of the historic buildings on the property. The principal and interest due from 2019 onward totals \$3,847,000.
 - Additionally, the Port has prepared an amortization schedule for a bond that would be used to fund the construction of the south jetty. The principal and interest due from 2019 onward equals \$5,517,519.
 - In total the Port will be obligated to service a debt of \$9,364,519 in the next twenty-five years.
- **North Jetty Cost.** The most current engineer's cost estimate for the north jetty is approximately \$2,700,000. If the Port bonds for the south jetty, the organization will lack the bonding capacity to complete the north jetty.

The question to consider is: should the NWMC proposal provide a sufficient capital contribution to cover the construction of the north jetty? If so, what is a reasonable timeframe for such a contribution?

- In both scenarios presented in the NWMC proposal, the Port would be obligated to replace both jetties.
- **Capital Contribution(s)** Both scenarios presented by the NWMC include a capital contribution of \$3,500,000. The timing of such contributions varies under the two scenarios presented. A fundamental question of interest to both the Port and the NWMC is whether such a contribution would be subject to leasehold tax. While that question would ultimately be answered by the WA Department of Revenue, for the purpose of analysis the Port has assumed that the stated payment would be received in full by the Port. Any tax obligation from such a payment would need to be considered separately.
- To answer the question "Would the Port be in a better or worse financial position under the terms of the NWMC proposal?", some financial forecasting must be done. The Port has analyzed the past 9 years of revenues and costs Port-wide. Revenues have grown on average at a rate of 4.0%. Expenses have grown on average at 4.9%. These represent more conservative numbers than those seen in the actual trends at Point Hudson. Still, they were determined to be appropriate for modeling purposes.
- **Annual Lease Payment.** The annual lease payment varies under the two scenarios presented by the NWMC. The phased approach offers an initial lease payment of \$100,000 per year for three years and then an annual lease payment of \$150,000 through 2024 with the annual lease again increasing to \$350,000 annually. (This is Port

staff's best interpretation as the NWMC proposal is sometimes not internally consistent in its presentation.) The non-phased proposal offers a lease of payment of \$200,000 per year for three years and then an annual lease payment of \$350,000 thereafter. Neither approach appears to account for inflation after the initial period.

Leases may include an initial "break in" period with a lower initial lease payment so long as the total life of the lease does not result in a gifting of public funds.

- **Net Income Sharing.** The NWMC proposes a share of net income after a base amount, i.e. a percentage of net on net. While this attempt to align interests and offer a share of improvement to the public good is noted and appreciated, a percentage of net income is not a common real estate term. More common is a percentage of gross receipts, which is far easier to administer.

The question for the Commission is: to what extent should a revenue (or income) share be considered as part of the overall consideration of the property?

- **Term.** The term of the lease is one of the basic aspects of any agreement. The NWMC proposes a lease term of 50 years under both scenarios presented. In general, Ports are authorized to lease properties for a maximum term of 50 years. In practice, the term of the lease must be of such duration to protect the public interest over a reasonable period. Leases for a shorter duration with option(s) to renew give both the Port and the tenant the flexibility to adjust to changing conditions.

The question for the Commission to consider is: what is a reasonable lease term?

- **Security.** RCW 53.08.085 requires some form of security for the lease payment. State law further stipulates that any security offered should be of not less than one year's value and no more than three year's value.

The NWMC proposal does not specify what type of security would be offered.

The question for Commission consideration is: what amount and type of security should be required to protect the public's interest in the event of non-performance?

- **Lease Option Payment.** The Port currently has two buildings vacant that are part of either scenario presented by the NWMC. The Port has not actively marketed either building for a variety of reasons, not the least of which is the uncertainty regarding an agreement with the NWMC.

Should the Port and the NWMC come to an agreement that would lead to a letter of intent, the question is: should a lease payment to purchase an option to lease be required to hold the vacant properties for future NWMC use. If so, what is an appropriate payment?

- **Building Repair.** Much is known about the current condition of the historic buildings at Point Hudson. Still, when it comes to repair or restoration of any historic building, any reasonable owner or tenant must be prepared for surprises.

The two scenarios presented by the NWMC offer two different levels of commitment for both the Port and the tenant. Both are difficult to quantify given the nature of estimating with historic structures.

Further complicating the issue is whether improvements undertaken by the NWMC would be considered public works and subject to state and federal standards for procurement.

Still, the Port does have an assessment of the repairs and rehabilitations that would be required to keep the structures weather tight and to address life and safety issues.

- **Infrastructure Management & Maintenance.** Both scenarios presented by the NWMC stipulate that the Port would be required to maintain “below grade utility function such as water, sewer, power, power and data.”

Continued operation, let alone any type of upgrade, presents considerable risk. In addition, the NWMC proposal states in its vision that there would be “improved electrical and wireless infrastructure.” It is unclear in the proposal which entity would pay for such improvements.

The question before the Commission is: what type of consideration should this long-term management obligation be given in the lease terms to offset the risk to the Port?

- **Compatibility of Proposed Uses with Zoning, Shoreline and other Regulations**
Port staff recognizes that the document presented is in some respects aspirational. Potential uses mentioned include: venues for theater or music/dancing, additional eateries (or restaurant spaces), grocery sales, a seafood market and relocation of RV spaces. Some of these uses appear to be incompatible with existing regulations. All would require careful planning and development.

The question for the Commission to consider is: does the NWMC have the demonstrated experience to develop and manage the variety of uses presented?

- **Experience and Credit-Worthiness.** To the extent that the experience and credit-worthiness of a potential tenant affects the risk to the Port, both factors should be considered in developing the terms of a potential agreement. Risk can be mitigated by measures such as security deposits.

Credit-worthiness is somewhat easier to assess. A credit check for timely payments, contract compliance, etc. is fairly easy to obtain.

Experience is somewhat more difficult to analyze. Does the NWMC have experience demonstrating the capacity to manage a property of this nature and complexity? Does the NWMC have the experience to manage a property with underlying public ownership?

FISCAL IMPACT

To be determined.

RECOMMENDATIONS

Discuss the above factors, and any other related issues and factors in open session. Then adjourn to executive session to discuss the minimum acceptable price.

ATTACHMENTS

1. *A Financial Assessment of the Port Hudson Proposal* by ECONorthwest
2. *An Analysis of the Various Outcomes of a Lease between the Port of Port Townsend and NWMC* by Red Fern Consulting