May 22, 2023

Michael Lambert
Preservation Planner
City of Geneva
22 South First Street
Geneva, IL 60134

Dear Mr. Lambert:

Teska Associates, Inc. and The Planera Group were retained by the City of Geneva to review the pro forma and economic feasibility analysis presented in the Application for Demolition of a Designated Property at 4 East State Street, City of Geneva.

Our assignment was to investigate whether the pro forma analysis in the Application meets the requirements that, according to Ordinance 10-6-10, the "demolition shall be considered only when all other redevelopment options for a building, structure, object, improvement, or site have been exhausted."

Teska submitted an initial report as testimony to the City of Geneva Historic Preservation Commission on April 18, 2023.

As part of our scope of work, we analyzed the pro forma submitted by the Applicant. We also developed a series of alternative approaches that would include renovation and reuse of the historic building in the context of the entire site. We evaluated public funding sources to support the renovation of the historic building and enhance the project's financial feasibility.

On May 2nd, the Applicant provided comments on our analysis. This report provides updated findings and addresses comments from the Applicant.

A summary of key findings include:

1) A stand-alone renovation of the historic building would be revenue neutral earning a 1.3% Return On Investment (ROI). Earning a market-based, 10% ROI would require a public private partnership in which eligible expenses are supported through public incentives such as Tax Increment Financing (TIF) and possibly, Federal Historic Tax Credits and other historic preservation grants. A Preservation Easement may also be used as a source of revenue for a private developer who would donate the unused portion of the development rights of the property to an eligible non-profit organization.
2) Teska/Planera have updated the financial analyses of two additional scenarios, comparing the projected returns <u>with</u> the historic building versus <u>without</u> the historic building.
3) We have found very similar annual returns of approximately 3.4%-3.6% Return on Investment (ROI) for a Four-Story Development with the Historic Building and without the Historic Building. The Internal Rate of Return (IRR), a common measure of determining financial feasibility of real estate projects, would be 11%-12% for the two options. Public incentives such as TIF and Federal Historic Tax Credits would increase the ROI.

4) Similarly, we found similar annual returns of approximately 3.6%-4% ROI for a Four-Story Building with Partial Fifth Floor for a development that would include the historic building renovation versus not including it. The IRR for these scenarios would range from 12%-13%. Public incentives such as TIF and Federal Historic Tax Credits would increase the ROI for this scenario as well.

The analysis which follows responds to the comments from the Applicant and the Commissioners, a summary of the alternatives analysis, additional information on public incentives, our assumptions, and limitations of the report.

Sincerely,

Scott Goldstein FAICP LEED AP
Principal
Teska Associates, Inc.

Terri Haymaker
Principal
The Planera Group

1 RESPONSE TO APPLICANT COMMENTS

Comment #1: Analysis of Alternative Uses of the Site

The Teska/Planera alternatives analysis considers stand-alone scenarios as well as development of the full parcel. The Applicant questioned whether alternative analyses should consider the building only versus the full parcel in which the building occupies a portion of the site.

The Ordinance states: "demolition shall be considered only when all other redevelopment options for a building, structure, object, improvement, or site have been exhausted."

As stated at the May 2nd Public Hearing by the City's Attorney, the analysis can include all options for the building and the site. The historic structure sits on a larger site identified in County records with a single parcel identifier number (PIN) that should be considered for alternative development scenarios. The area under the historic structure has not been subdivided from this larger site. The corner site (12 E. State Street) was included in the analysis as that property was also incorporated in the 2019 Charrette (which the Applicant participated in) and the Applicant currently has site control of the corner property, as confirmed at the May 2nd Public Hearing. An alternative analysis that did not consider a larger project would ignore the redevelopment potential of the historic building.

Comment #2: Land Costs of Historic Site (page 10 of Teska/Planera Report)

Teska/Planera did <u>not</u> find that there was any real or perceived taking of the property. In fact, historic designation of the property is an example of a regulation, similar to zoning, that provides parameters regarding the use of property based on existing ordinances.

Teska/Planera determined the value of land for the historic designated property based on the land assessed value of four nearby vacant commercial properties. These properties include 12 East State St., 22 Chrissey Avenue, 34 N. Bennett St. and 102 E. State St., all properties that were included in the Applicant's Demolition Application. We determined market value of the land based on three times the assessed land value of each property. Based on this analysis, we estimated a land value of $50,000 for the property including, and immediately surrounding the historic building.

Comment #3: Leasing Fees (page 10 of Teska/Planera Report)

Our analysis of the Applicant's pro forma questioned whether a commercial broker leasing fee would typically be required in a market transaction for a property such as leasing this building. Since the Foundation currently owns the property and was cited in the Applicant's submission as the occupant, we questioned this charge back to the property owner as an assumption in the Applicant's development pro forma.

Comment #4: Federal Historic Tax Credits (page 11 of Teska/Planera Report)

Teska/Planera tested various assumptions in our analysis of the Applicant's pro forma submission.

Teska/Planera are not making any assumption regarding potential eligibility for the National Register of Historic Places, especially as there has been no application for such listing. Our assignment included investigating potential funding sources for the restoration of the locally designated historic property. This included the possible use of Federal Historic Tax Credits, which first require the property owner to apply and receive National Register designation. Some of the alternatives we investigated included the use of Historic Tax Credits, while others did not.

Comment #5: Return on Investment (page 11 of Teska/Planera Report)

There are several measures that the real estate industry employs to determine Return on Investment (ROI). The Applicant has used only one method – one year of Net Operating Income at Stabilization over Equity. While this is one measure, it does not include the gain in the owner's equity over time.

We have added Internal Rate of Return (IRR) estimates for the full-site scenarios. IRR includes the return on equity over a period of years, including the change in value of the property over a given period of time, in this case ten years. IRR calculations are often used by developers and the public sector in evaluating investment opportunities. IRR standards for a stabilized public private partnership project are typically approximately 10-15%.

The estimated value of land for the full site was based on market listings for nearby commercial properties that have similar development potential: 402 W. State St., 206 E. State St. and 302 N. River Lane. The average listing price of these properties is $51.84 per sq. ft. or $3,251,613 for the full site including the 12 E. State St. property. The cost of demolition and environmental work is assumed to be part of the total development cost estimated during the 2019 Public Charrette that we used as a basis for the cost analysis and brought up to current dollars.

Comment #6: Analysis of Stand-Alone Scenarios 1)A and 1)B (pages 12-13 of Teska/Planera Report)

Our analysis of the Applicant's pro forma resulted in two stand-alone scenarios. Both scenarios include the renovation of the historic building separate from any new development proposed for the remainder of the larger site.

Scenario 1)A Stand-Alone without TIF and Historic Tax Credits (similar to the Applicant's pro forma application) would provide approximately 1.3% ROI, measured by annual Net Operating Income over Equity. In addition, the developer would earn 10% Developer's Fee according to the Applicant's submittal. This would essentially be a "break even" scenario.

Scenario 1)B Stand-Alone with TIF Increment, with approximately $1.5-$1.7 million of public funds (with or without Federal Historic Tax Credits), the project would have 10% ROI plus the 10% Developer's Fee.

Note that if TIF were used to cover eligible expenses, this public investment would be approximately 3.75% of the estimated Total Development Cost of full-site redevelopment, well within established norms for the City of Geneva TIF program.

At the Public Hearing, the Applicant agreed with one of Teska/Planera's key findings that 10% ROI on a public private partnership project meets market expectations and standards in the industry. Whether public sources include TIF and/or Federal Historic Tax Credits, this alternative could be financially viable with approximately $1.7 million in City and other public funds or tax credits.

Furthermore, as stated in the Teska/Planera report, there are additional possible incentives available to support the historic building renovation. One source is two historic preservation grants offered by Landmarks Illinois which can be used for the application for the National Register of Historic Places, among other eligible costs.

Specifically, the Application did not consider a significant possible public source – a Preservation Easement.

Preservation Easement programs allow for owners of historic buildings to gain the federal income tax benefits derived from a donation equal to the easement value to a qualified nonprofit entity. The exact financial benefit of this donation, which is based on an appraised value of the easement, has not been determined and therefore, is not included in our analysis. Yet, it is a possible additional revenue source that could make renovation and preservation of the building a more viable financial option.

At the May 2nd Public Hearing, Historic Preservation Commissioners inquired whether there could be additional alternative uses of the historic property.

Teska/Planera have investigated other uses and have determined that the $20 rent per sq. ft. in the Applicant's pro forma equates to market rent for the existing interior footprint. This rent assumption would apply to other commercial and retail uses which could occupy the building. However, depending on how the project is designed, there could be additional sources of revenue from using the indoor and outdoor space for meetings and events, especially considering the potential for space overlooking the Fox River and as a complement to nearby event spaces on the west side of the river.

While Teska/Planera investigated several possibilities for the reuse of the historic property, there could be other alternatives in which the historic property is reused as a part of a larger redevelopment project. The building could become retail or amenity space as part of other alternative redevelopments. Similar to the findings in the development concepts we analyzed below, the market fundamentals would be driven primarily by the larger site redevelopment, in which the $1.5 - $2.0 million cost for the historic property is a largely revenue neutral portion of the overall development cost and return for the larger project.

Comment #7: Analysis of 4-Story As-of-Right Scenarios (pages 14-15 of Teska/Planera Report)

The Applicant questioned the Teska/Planera estimates of ROI in these two scenarios. We have updated our analysis to correct annual debt service payments, which had previously been calculated based on monthly estimates. We have also updated market assumptions for rent and operating expenses at the time of the application. We applied the loan "Stress Test" and used the lowest risk loan value calculation based on the Debt Service Coverage Ratio (DSCR).

Based on these revisions, we estimate that the annual ROI would be approximately 3.41% for a 4-Story As-of-Right Development with the Historic Building versus 3.62% ROI for the same development without the Historic Building. Note that this doesn't include any public incentives such as TIF, Federal Historic Tax Credits or Preservation Easements that could be used to increase the ROI.

The IRR for Scenario 2)A with the Historic Building would be 11.1% versus 12% for Scenario 2)B without the Historic Building.

A combination of TIF, Federal Historic Tax Credits and other alternatives such as a Preservation Easement, would increase the financial viability for these development options proportionately.

Comment #8: Analysis of 4-Story Building with Partial 5th Floor Scenarios (pages 14-15 of Teska/Planera Report)

Similar to the changes discussed under Comment #7, we have updated the analyses of these scenarios using annual debt service, rent and operating costs, and lower-risk DSCR loans to the lender.

As a result of these changes, annual ROI would be 3.58% for Scenario 3)A with the Historic Building versus 4.02% without the Historic Building. Both scenario options do not include public incentives such as TIF, Federal Historic Tax Credits or a Preservation Easement, which would increase the ROIs.

The IRR for Scenario 3)A with the Historic Building would be 11.8% versus 13.0% for Scenario 3)B without the Historic Building.

Similar to our response to Comment #7, we calculated these annual ROIs without any public incentives. A combination of TIF, Federal Historic Tax Credits and other alternatives such as a Preservation Easement, would increase the financial viability for these development options proportionately.

Our conclusion that the Historic Building is essentially revenue neutral remains unchanged. There is very little difference between the ROI's with the Historic Building versus without it, assuming the same footprint and number of units in both scenarios, and the IRRs for both scenarios are within an acceptable range.

2 SUMMARY OF ALTERNATIVES ANALYSIS

	1)A Teska/Planera Review of Applicant Pro Forma	1)B Stand-Alone with TIF
Total Development Cost	$1,918,250	$1,918,250
Net Operating Income (NOI)	$20,259	$20,259
Loan	0	0
Equity	$1,525,981	$202,670
Public Incentives (TIF, Federal Historic Tax Credits)	$392,269	$1,715,580
Developer Fee	$169,299	$169,841
Annual Debt Payment	$0	$0
Return On Investment (ROI)	**1.3%**	**10%**

	2)A Four Story with Historic Building	2)B Four Story without Historic Building
Total Development Cost	$38,445,107	$37,054,613
NOI	$2,459,619	$2,439,360
LTV (75%) Loan	$33,540,258	$33,264,000
LTC (75%) Loan	$28,833,830	$27,790,960
DSCR (1.25) Selected Loan	$24,001,703	$23,804,010
Equity	$14,443,404	$13,250,603
Public Incentives (TIF, Federal Historic Tax Credits)	Not Included in Calculation	Not Included in Calculation
Annual Debt Payment	-$1,967,695	-$1,951,488
ROI at Stabilization	**3.41%**	**3.62%**
Future Value (Year 10)	$54,972,721	$54,519,932
Less Closing Costs	-1,099,454	-$1,090,399
Less Outstanding Loan	-18,605,701	-$18,452,453
Net Sale Proceeds	$35,267,566	$34,977,081
IRR (10 Year)	**11.1%**	**12.0%**

	3)A Four Story with Partial Fifth Floor with Historic Building	3)A Four Story with Partial Fifth Floor without Historic Building
Total Development Cost	$40,739,041	$39,043,613
NOI	$2,670,819	$2,650,560
LTV (75%) Loan	$36,420,258	$36,144,000
LTC (75%) Loan	$30,554,281	$29,282,710
DSCR(1.25) Selected Loan	$26,062,656	$25,864,963
Equity	$14,676,385	$13,178,650
Public Incentives (TIF, Federal Historic Tax Credits)	Not Included in Calculation	Not Included in Calculation
Annual Debt Payment	-$2,136,655	-$2,120,448
ROI at Stabilization	**3.58%**	**4.02%**
Future Value (Year 10)	$59,693,061	$59,240,273
Less Closing Costs	-$1,193,861	-$1,184,805
Less Outstanding Loan	-$20,203,316	-$20,050,068
Net Sale Proceeds	$38,295,884	$38,005,399
IRR (10 Year)	**11.8%**	**13.0%**

3 Public Incentives

Our analysis evaluated the Applicant's pro forma and the possibility of public incentives in alternative scenarios. Two sources highlighted in Scenario 1)B are Tax Increment Financing and Federal Historic Tax Credits. Other sources can augment or be substitutes for these, pending further investigation. These two sources were used to serve as an example of forming a public private partnership to preserve the historic building and to cover a portion of the higher renovation cost.

The subject property is within an existing Tax Increment Financing District. The Tax Increment Financing (TIF) is a commonly used tool to support community redevelopment projects. Through the use of TIF, municipalities capture future property tax revenue increases from a defined area or district to use toward an economic development project or public improvement project. The possible TIF subsidy for a project is based on the amount of expected growth in property tax revenue as a result of the proposed new development. For the purposes of the Scenario 1)B pro forma, the assumed TIF subsidy equals $1,525,000, which would be equivalent to approximately three to four percent of the full site Total Development Cost. This does not presume the applicant will be submitting a TIF request nor does it assume any approval of the City's consideration of a possible TIF application.

Federal Historic Tax Credits are a tool for supporting the restoration of historic buildings. The level of available tax credits for a project is based on the costs incurred for the building restoration. The income tax credit is equal to 20% of the qualifying rehabilitation expenditures in the project. The tax credits are typically syndicated to tax credit investors at a rate of $0.80 per $1.00 of tax credit. This was the calculation used to determine the amount of federal historic tax credits to be included in the 1)B pro forma.

In order to be eligible for historic tax credits, buildings must be listed on the National Register of Historic Places. Within the scope of work for this report, we did not conduct any evaluation of the building's eligibility for the National Register nor are we aware of any analysis or application prepared to date for National Register consideration.

Not included in the 1)B pro forma are several other historic preservation funding sources.

The State of Illinois Historic Tax Credits are available; however, they were not considered in the pro forma as they are competitive with limited awards offered to projects who meet more of the program's criteria than this proposed project. There is a $15 million program cap to be used for all projects that apply for the State Tax Credits, which makes the awarding of funds very competitive. The competitive nature of this subsidy is the reason it was excluded from this project's potential public subsidy options.

Landmarks Illinois offers two grants which were not factored into this pro forma's funding sources as the amount of funding available would be based on more detailed eligible costs than currently known and will determined through the application process. The two grants are the Preservation Heritage Fund Grant and the Barbara C. and Thomas E. Donnelley II Preservation Fund Grant. They are designed to preserve and protect significant sites and structures, especially those under threat of demolition and in need of stabilization. Eligible costs are planning, design, engineering, feasibility studies and other pre-development expenses. Non-profits or governmental agencies may apply for the purposes of supporting specific historic buildings.

Preservation Easement programs facilitate the permanent protection of historic structures. They enable owners of historic buildings to gain the federal income tax benefits derived from a donation to a qualifying nonprofit based on the undevelopable value of their property. This donation grants the qualifying nonprofit authority over any future changes proposed to the building's historic features. Landmarks Illinois has a formal preservation easement donation program. The financial benefit of this donation is based on the appraised value of the easement, which has not been determined and therefore, is not included in pro forma analyses.

4 ASSUMPTIONS

Total Development Costs -

Historic Building Costs: AltusWorks Building Assessment Report, August 17, 2022

Residential Building: Proportionate share based on 2019 Charrette estimates + 17% inflationary factor

Loan Terms -

6.5% interest rate (at time of demolition application)

25-year amortization

Loan "Stress Test"

Teska/Planera analyzed the following methods for each scenario:

Loan to Cost – 75%

Loan to Value – 75%

DSCR 1.25 Loans (in all cases, this was the lowest loan value of the three-part test)

Closing Costs – 2%

Return On Investment - Annual Net Operating Income at Stabilization divided by Equity

Internal Rate of Return (IRR) - Ten Year Cash Flow Analysis with two-year construction, 60% occupancy in Year 3 and full stabilization in year 4. Future value in Year 10 shown in tables above determined by NOI in year 10 divided by cap rate.

Commercial Cap Rate: 7.5%

Residential Cap Rate: 5.5%

Information on Financial Assumptions:

Tax Increment Financing – Illinois Department of Commerce and Economic Opportunity

Financial Resources for Historic Places - Landmarks Illinois

Easements - Preservation Leadership Forum - A Program of the National Trust for Historic Preservation (savingplaces.org)

Commercial Property Assessed Clean Energy - Illinois Finance Authority

Kane County GIS

Kane County Assessment

5 REPORT LIMITATIONS

The assumptions in the report are based on industry standards, results of interviews, and market information. The sources of the assumptions are delineated in the report. While these assumptions are based on industry standards, they present scenarios representing a range of reasonable forecasts. The analysis in this report is intended for use by review of local government reviewing the project and should not be used for any other purposes.

---End of Report---