CITY OF WORCESTER, MASSACHUSETTS

Auditing Department

Robert V. Stearns, CPA
City Auditor

June 4, 2019

TO THE WORCESTER CITY COUNCIL

RE: Request City Auditor provide City Council with a report reviewing whether the passage of time taken to develop the Madison Properties will have an impact on the solvency in terms of any payment on any loans or bonds.

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The passage of time taken to develop the Madison Properties would affect the timing of the receipt of revenues required to service Series A bonds. The $70M Series A bonds are to be repaid from new city revenue generated mainly from the Madison property developments in the ballpark district. Development is in two phases with several of the phase 1 developments expected to be completed prior to the opening of the ballpark in 2021. The original proforma assumed that the debt service not including capitalized interest on the Series A bonds would begin in fiscal 2022, thereby requiring that the revenues be available at that time to pay the debt. However, the debt strategy as it relates to the Series A bonds was changed and provides the city with flexibility as to when the Series A bonds are issued and when the first bond payment becomes due.

The letter of intent between the city and Madison is non-binding and to serve as a guideline for the negotiations to the final agreement between the parties in the "Development Agreement", currently in progress. The letter of intent set a schedule for several of the properties with an occupancy date of not later than January 1, 2021. This date is relevant because it is when the Assessor will determine the taxable assessed value for fiscal 2022. The parties however acknowledge that this schedule represents a reasonable expectation and the scope and timing is subject to market forces and general economic conditions. If the project falls behind and the properties are not completed by January 1, 2021 an assessment on the partial construction would be assessed including development from January 2nd through June 30th.

The original proforma assumed the Series A bonds would be issued in November 2018 with fiscal 2022 as the first year debt service would be paid using the new city revenue. Debt service due in fiscal 2022 was projected to total $2.8M on the Series A bonds. The new revenue that year is projected to total $3.7M with approximately $2.8M attributable to Madison developments including real estate tax net of exemptions, revenue for use of the city-owned garage and local option excise tax from Madison restaurants and hotels. Other revenue that have been identified to service Series A bonds total $0.9M including event parking, city share of advertising, personal property taxes and meals taxes at the ballpark. It is also assumed there will be $1M revenue from real estate taxes on the assessment of partially constructed properties from fiscal 2021 carried forward to be available in fiscal 2022.

A surplus of $741K is expected in fiscal 2022 of the revenues mentioned above over the Series A debt service less certain operating expenses and a 5% contingency. Surpluses are expected each year thereafter with a cumulative net surplus projected of $22M at the end of thirty years. Cumulative revenues over the thirty years are projected to total $157M, and the gross debt service on Series A is $128M. This excludes any revenue generated from the planned developments in phase 2.

As mentioned the proforma originally assumed that the Series A debt would be issued in its entirety in November 2018. This is based in part on the language in the letter of intent between the city and the team requiring simultaneous issuance of Series A and B bonds as soon as practicable. The team and city have since amended the language and agreed that the Series B bonds would be issued as soon as practicable which was done in November 2018, and that Series A would be issued in accordance with the City's debt strategy which includes issuing a series of short-term notes from time to time in anticipation of the Series A bonds.

The change in the debt strategy with respect to Series A bonds will provide the city with some flexibility when the first bond payment would be due, likely extending it out one year to fiscal 2023. There will likely be lower capitalized interest costs as the full $70M would not be accruing interest from the pre-construction period but rather interest would accrue on the bond anticipation notes (BANS) as issued which would be based on when the funds are needed and generally at a lower rate.

There is $26M of Series B proceeds remaining for project costs including $2M for its capitalized interest costs. This should finance all of the land acquisition and the beginning construction work prior to any draws on Series A BANs. The first of the Series A BANs to be issued is expected in fiscal 2020 with draws of $28M as reflected in the capital improvement plan. The remainder of the Series A BANs would be issued in fiscal 2021.

Interest on the BANs would be accrued and part of the capital project costs. The BANS would be permanently financed with bonds likely within two years after first series of BANs were issued. This has basically given the city an additional year to pay the first Series A bond payment and a hedge should the Madison developments are not fully assessed by January 1, 2021. The city in keeping within the objective of providing sufficient funds to complete the ballpark on time while using the lowest possible cost of capital will monitor the debt strategy as market conditions may change.

Should the passage of time taken to develop the Madison Properties extend beyond a year would not necessarily mean the debt service fund would be insolvent to make debt payments in fiscal 2023 as there would be taxes assessed on the fully and partially constructed properties at that time. Other ancillary revenues from ballpark operations are expected such as personal property taxes, event revenue, event parking, advertising, and excise from ballpark meals.

However, the 30 year debt schedule will have increasing payments to coincide with assumed increases in tax and other revenues. It is in the city's interest that the parties stay within schedule as a delay may not necessarily jeopardize the solvency of the Series A debt service fund but would be a loss of revenue which may be needed for future needs and contingencies.

The loan payments for the Series B bonds are not dependent upon the development of the Madison Properties and are to be paid from the new city revenues generated by team rent pursuant to a ballpark lease that is in the process of being finalized.

Respectfully Submitted,

Robert V. Stearns

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City Auditor