Appendix B

Brownfield Redevelopment Incentive Program
Reasonable and Appropriate Return on Investment

Introduction

As with its predecessor real estate development incentive, the Economic Redevelopment and Growth Program (ERG), a key statutory requirement within the Economic Recovery Act of 2020 (ERA) enacted real estate development incentives is that without the incentive award, the redevelopment project is not economically feasible. As such the applicant must demonstrate that a project financing gap exists, which requires that redevelopment project will generate a below market rate of return.

This appendix outlines the Authority's history with such analyses and present policy recommendations for administering related provisions such as determining the reasonable and appropriate rate of return on investment for the project.

Authority History with Gap Financing Programs and Hurdle Rate Determinations

As noted previously the Authority has experience administering gap financing real estate development incentives through the ERG program dating back to its establishment in 2012. In November of 2012 the Authority Board approved the use of a financial model developed by real estate services firm Jones Lang Lasalle (JLL) for the purpose of determining market returns that would be required for prospective real estate projects in the State to be considered economically viable, i.e., a hurdle rate. This model was subsequently modified in December of 2012 to add functionality and allow for its use more efficiently across the State. A "Modification to the Hurdle Rate Model" memorandum is being proposed concurrently to the Board on October 12, 2022, which specifically addresses the Brownfield Redevelopment Incentive, and the Historic Property Reinvestment Program. The model arrives at a project specific hurdle rate based upon three factors including the projects proposed zip code, industry class, and if it would be located in area of the state exhibiting economic distress.

The model is updated semi-annually to reflect current market realities.

In the event of a large, unique, and/or complex project, which could include complex projects utilizing LIHTC but having a significant commercial component, the Authority has commissioned a proposed project-specific third-party analysis performed by a real estate services firm to determine a project specific hurdle rate. As provided in the Aspire rules, the cost of these services is charged to the applicant.

Policy within ERA enacted real estate development incentives for Determining Reasonable and Appropriate Return on Investment

Staff is proposing the use of the JLL hurdle rate model, with the modifications proposed in the October 12, 2022 memorandum, for purposes of determining the reasonable and appropriate return on investment

that projects will be evaluated upon for program eligibility and award sizing. The modifications in the October 12, 2022 memorandum, reflect nuances related to capital financing strategies and market return expectations that may exist within the relevant sub-category.

Although redevelopment projects in the Brownfield Redevelopment Incentive Program include projects that are only remediation as well as projects that also include construction, the Brownfield Redevelopment Incentive Act provides that the project financing gap is based on remediation only. Thus, the project finance gap will only consider the total cost of remediation, and the equity required will be calculated on the total cost of remediation.

As stated in the rules, if the developer sells, leases, or subleases the site of the redevelopment project within four years after the completion of the redevelopment project, the developer is subject to a re-evaluation of the rate of return. Staff will compare the sale price or the net present value of the entire lease or sublease against the appraisal, submitted by the developer at application, which indicated the “as is” value of the site if remediated. If the sale price is greater than the appraised value (regardless of the reason), the rate of return will be re-evaluated using the sale price, which may include an increase in value attributed to additional construction or other post-remediation work that the developer may have undertaken. While the rules do not prescribe a threshold for an increase in the rate of return that requires the re-payment of 20% of the excess, Staff proposes using 15%, consistent with the Aspire statute and rules. Thus, the developer shall pay 20% of the excess only if the developer's re-evaluated rate of return exceeds the Board approved rate of return by 15%.

Staff proposes continuing to use a third-party consultant to perform project-specific analysis for large and highly specific projects. In these circumstances, the Authority staff will continue to rely upon real estate advisory services providers on an as needed basis to determine project specific reasonable and appropriate return on investment for large, unique, and/or highly complex projects. As previously noted, it is likely that some of the product specific programs within the ERA may result in particularly unique projects as it relates to the product and the financing that may be utilized. In these events the authority may rely upon a third-party to complete certain aspects of the return analysis as needed.