

## MEMORANDUM

TO: Courtney Kramlinger, Economic Development Coordinator

FROM: Stacie Kvilvang, Ehlers

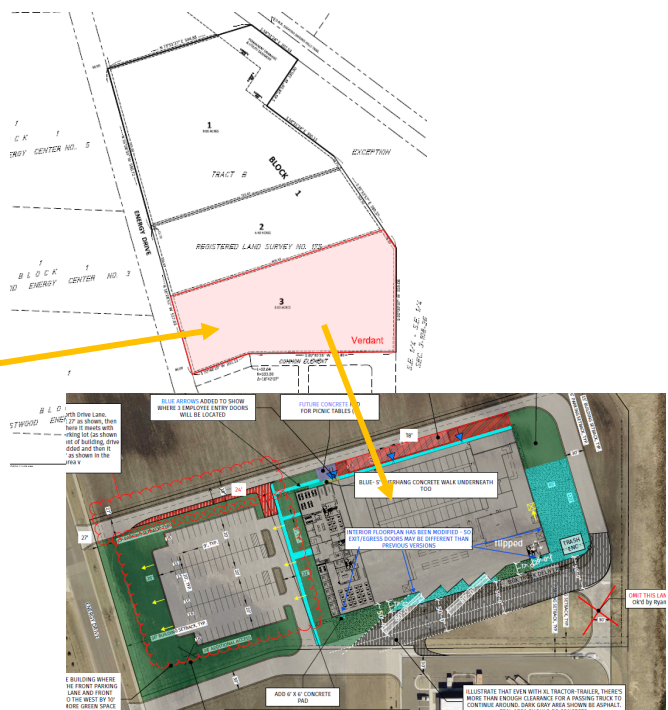
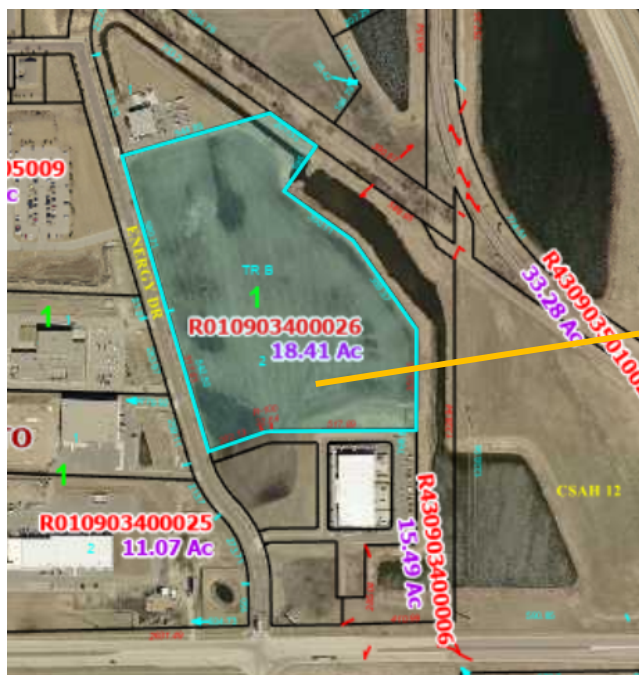
DATE: August 28, 2026

SUBJECT: Old Town Properties, LLC.

### Project Background

The City of Mankato (the “City”) received a request for \$1,890,000 in Tax Abatement Financing (“Abatement”) from Old Town Properties, LLC (the “Developer”) for the construction of a 63,000 sq. ft. office and indoor organic production and processing facility for cultivation, processing, packaging and distribution of mushrooms and microgreens (the “Project”). They requested a 15-year term with annual abatement of \$126,000. The Developer would own the facility and lease it to Verdant Organics (the “Tenant”).

The Developer originally purchased the existing site in 2022, which included the southern parcels that have been replatted (total of 26.53 acres) for \$1.849M, or \$1.60 sq. ft. In 2023, they replatted and sold the parcel located at 1021 Elevate Lane for \$600,000 (\$8.35 sq. ft. sq. ft.) and currently own and lease that space to tenants. The remaining 18.41-acre site noted below (PID : R01.09.03.400.026) would be replatted into 3 lots, with the proposed Project being developed on approximately 6 acres located on the southern end of the existing parcel.



## Tax Abatement

MN Statutes 469.1813 allows a political subdivision (city, county or school district) to grant an abatement of all or a portion of their share of the taxes to a business or development if they deem that in doing so is in the public's interest because it will meet at least one (1) of ten (10) reasons. For purposes of this discussion, the project in question would meet the following two (2) benefits:

1. Increase or preserve tax base; and
2. Provide employment opportunities in the political subdivision;

Each political subdivision has a say in the abatement of their portion of taxes, and the City can only agree to abate their share. In addition, if a city awards more than \$150,000 in assistance to a commercial business (housing is exempt from this requirement), the City is required to hold a public hearing on the abatement and enter into a formal agreement with the business that outlines job and wage goals attributable to the project.

Cities typically treat tax abatement like tax increment financing (TIF). The value that the City abates is only the new increased value of the property created by construction of building (so land value taxes still go to the City). Based upon the projected valuation of the Project upon completion by the County Assessor (\$5.046M), the overall taxes to be paid by the Project is approximately \$141,000/year. Of this, the City's portion is approximately \$31,000/year or 22% of the overall taxes.

The Abatement agreement is with the property owner, since they are ultimately responsible for payment of the property taxes and the Abatement note is issued and paid to them. The Tenant is not entitled to the Abatement unless there is a formal agreement with the Developer, of which the agreement is a private agreement between the parties.

## Financial Analysis

The Developer submitted financial information ("Proforma") for the Project to the City. Ehlers conducted a review of the Developer's current Proforma based on industry standards for construction costs, land costs, rental rates, developer fee, available funding sources, underwriting criteria, and project cash flow. Based on the results of the pro forma analysis, we conclude the project requires approximately \$178,000 in Abatement. This assistance would be provided in the form of a pay-as-you-go (PAYGO) note paid with 90% of the City's portion of the increased taxes (Abatement) generated annually from the Project over a 7-year period (the "City Assistance"). This equates to approximately \$28,000/per year when the project is fully valued in year two (2).

1. **Total Development Costs (TDC):** The TDC of the project is approximately \$13.56 million as noted in the table below. The per sq. ft. cost at \$215 is higher than what we typically see of \$120 to \$150. The increased cost is attributable to the higher land purchase price and possibly the cost of tenant build out.

| First Mortgage       | 10,850,499        | 80.00%         |  |
|----------------------|-------------------|----------------|--|
| Developer Equity     | 2,712,625         | 20.00%         |  |
| <b>TOTAL SOURCES</b> | <b>13,563,124</b> | <b>100.00%</b> |  |

| Acquisition Costs     | 1,568,160         | 11.56%         | 24.89         |
|-----------------------|-------------------|----------------|---------------|
| Construction Costs    | 10,559,848        | 77.86%         | 167.62        |
| Professional Services | 1,144,116         | 8.44%          | 18.16         |
| Financing Costs       | 291,000           | 2.15%          | 4.62          |
| Developer Fee         | 0                 | 0.00%          | 0.00          |
| <b>TOTAL USES</b>     | <b>13,563,124</b> | <b>100.00%</b> | <b>215.29</b> |

2. **Project Financing:** The Developer proposes to finance the Project with a combination of debt and equity. The Developer anticipates securing a first mortgage in the amount of \$10.850 million to finance 80% of TDC. The Developer will be providing \$2.712 million in equity, which is 20% of TDC and in line with typical development projects which range from 20% to 50%. The equity is comprised of land acquisition (\$1.568M) and future cash infusion at closing (\$1.144M).
3. **Land Acquisition Costs:** As discussed earlier, the Developer owns the land and has sold a portion already. The sale of land as proposed would likely reimburse the Developer for their original purchase price plus holding costs to date (taxes, etc.). Sale of the remaining 18.88 acres after this transaction would provide the Developer approximately \$4.9M in gross profit, if sold at the same anticipated \$6.00 sq. ft. We view that the purchase price of the land exceeds what we typically see for bulk manufacturing and contributes to the overall gap in the project.
4. **Developer Fee:** A developer fee compensates a developer for the staff time, effort and resources required to complete the steps necessary to bring a project to the development stage. This fee is typically 3% to 5% of TDC. The proposed developer fee is \$0 since the developer is the builder and will receive compensation as part of that contract. Overall, charging no developer fee makes the financing of the project more feasible.
5. **Rent:** For commercial projects we look at rents on a triple net (NNN) basis, meaning taxes, insurance and operating costs/CAM are netted out. The Developer has a 10-year lease with the tenant, with two 5-year renewals. The proposed rent for the tenant is \$15.72 sq. ft., and inflates annually, which is typical of the tenant profile for this type of facility.
6. **Financial Performance.** The Developer would like to attain an Yield on Cost (YOC) of 9% to 11%. This is higher than what we see for this type of build-to-suit and would expect that a YOC of 7.5% to 9%, depending on the tenant and proposed lease terms, etc.. Based upon our review, the YOC is 7.75% with tax abatement and 7.52% without tax abatement.

The other financial metric we review is when the project can meet a likely 120% debt service coverage for it bank financing. Based upon our review, by year seven (7) the project would meet this requirement.

## **Recommendation:**

If the EDA agrees that \$6 sq. ft. for the land is a fair market price for the land, based on our review of the Developer's Proforma and under current market conditions, the proposed Project isn't feasible without the City Assistance outlined (7-year PAYGO Abatement note of \$178,700). If the EDA deems that the land value is excessive, if we reduced the land to \$4.50 sq. ft. (where County has value on smaller lots), they would still require 5 years of Abatement (\$122,400).

We recommend inclusion of a three-prong 'lookback' provision in the Abatement agreement. This provision will allow for review of (i) actual project costs when project construction is completed (since everything is just estimates at this time); (ii) project performance and returns on investment against initial projections at stabilization; and (iii) review at sale. If project costs are lower when (i) is completed we typically see a reduction in Abatement on a \$1 for \$1 basis. For the other return metrics we typically see a sharing factor so only a 50% reduction in the Abatement needed to make the project financially feasible.

Please contact me at 651-697-8506 if you have any questions or comments.