

Memo

To: Sean Sullivan, Economic Development Manager
From: Jason Aarsvold, Ehlers
Date: 5-30-19
Subject: Delta ModTech TIF request

The City of Ramsey requested that Ehlers review the Tax Increment Financing (TIF) request from Delta ModTech for their proposal to construct an approximately 210,000 square foot manufacturing facility along Bunker Lake Blvd. just east of Puma Street. If approved, the project is expected to commence in 2019 and be complete in 2020.

Delta ModTech is requesting \$1.5 million in tax increment assistance. The project meets the requirements necessary for the City to establish a 9-year Economic Development TIF district. Based on our estimates, the project is expected to generate a total of approximately \$972,000 in tax increment over the 9-year life of the district. Therefore, the maximum amount of any TIF assistance should be limited to the \$972,000 projected.

The purpose of this memorandum is to evaluate whether the available assistance for Delta ModTech's project is necessary for financial feasibility in comparison to typical market-based expectations and alternative investment options available to the company. This is commonly referred to as meeting the "but for" test, which means the project would not occur on this site "but for" the public assistance being provided.

"But For" Test

As the company evaluated potential locations to invest in this new facility, it was considering alternative investment options outside Ramsey. The business indicated that local assistance was necessary to make investment at this location financially feasible. Based on our discussions with the company, we were able to conclude that Delta ModTech was not likely to make this current investment at the City's location without some outside assistance.

While this conclusion generally meets the "but for" test, we believe it's good policy to subject these requests to a more rigorous analysis to determine whether the level assistance is necessary for financial feasibility. For this reason, we took a second approach to analyzing the request.

The second approach to the "but for" analysis treats this project as an independent income producing real estate venture that might be built by a third party (developer) and leased back to Delta ModTech. In this scenario, we explored whether the project costs

and end sources of funds (rent paid by the business) would meet typical market returns to attract private equity financing.

Summary of Analysis

For purposes of this analysis, we assumed the project receives the full 9 years of tax increment totaling an estimated \$972,000. Based on the anticipated development costs and potential rental income, the projected cash-on-cost return on investment to a potential developer would be 8.1% without TIF assistance and 8.42% with TIF assistance. Cash-on-cost return is simply the annual income from the property divided by the total development cost. Industrial developers typically need a cash-on-cost return of between 7% and 9% to attract private financing. With the requested TIF assistance, the projected returns are still within this range.

Recommendations

Based on our review of the project and market trends, we conclude that the proposed development would not reasonably be expected to occur solely through private investment within the reasonably foreseeable future. Therefore, if the City chooses to provide assistance, Ehlers concludes it will help facilitate the project and not unduly enrich the company.

TIF assistance could be provided on a “pay-as-you-go” basis in an amount up to \$972,000. With “pay-as-you-go” TIF assistance, the City does not provide any funding up-front. Instead, the City enters into an agreement to provide tax increment payments that are generated **solely** from the project’s actual increased property taxes for up to nine years. The applicant uses those future tax increment payments to obtain additional debt and/or support returns on investment. If the tax increment is insufficient to pay the \$972,000 TIF note in nine years, the City does **not** make up the shortfall.

Please contact me at 651-697-8512 with any questions.