

Agenda Report

TO: CITY COUNCIL
THROUGH: FINANCE COMMITTEE

DATE: JULY 13, 2009

FROM: CITY MANAGER

SUBJECT: PROPOSED ICE RINK FACILITY

RECOMMENDATION

It is recommended that the City Council:

1. Find that the project was subject to adequate environmental review in the Initial Study approved and the Mitigated Negative Declaration adopted by the City Council for the Pasadena Ice Skating Facility on August 8, 2005 and that there are no changed circumstances or new information which would require further environmental review;
2. Approve the proposed Management Agreement between the City and Polar Ice Enterprises Pasadena for the management of a new ice rink facility in substantially the form attached and authorize the City Manager to execute the Management Agreement;
3. Adopt a Resolution declaring the City's intention to reimburse itself from the proceeds of one or more tax-exempt financings for certain expenditures made and/or to be made in connection with the Pasadena Ice Skating Rink Facility;
4. Accept the bid dated April 1, 2009, submitted by Mallcraft, Inc., in response to the specifications for the construction of the Pasadena Ice Skating Facility, reject all other bids received, and authorize the City Manager to enter into a contract in an amount not to exceed \$19,633,900, which includes the base bid of \$17,849,000 plus an allowance of 10% to accommodate any contingencies;
5. Authorize the City Manager to approve any other documents related to the construction of the new ice rink facility with the exception of any financing documents.

Alternatively, if the City Council elects to not move forward with the project, staff recommends that the City Council:

1. Reject all bids received in response to the Request for Bids for construction of the Pasadena Ice Skating Facility;

2. Direct staff to terminate discussion with Polar Ice Ventures,
3. Direct staff to return to the City Council with an operations and revitalization plan for the ice skating facility at the Convention Center.

EXECUTIVE SUMMARY

Since 1976 the Pasadena Ice Skating Facility has occupied space at the Pasadena Center, formerly used as a ballroom. However, the current facility is substandard and not in keeping with the quality of recreational facilities appropriate for a community such as Pasadena.

In August 2005, the City Council approved a capital improvement project for the relocation of the facility, thereby clearing the way for renovation of the historic ballroom. Under this plan, the ice rink is to be relocated to a new facility to be constructed on approximately four acres of City-owned parkland located between Orange Grove Boulevard and Foothill Boulevard.

In conformance with this plan, the proposed new facility has been designed, bids have been received and a management agreement for operation of the facility has been negotiated. Given a low bid of \$17.85 million, plus a 10% construction contingency for total construction cost of \$19,633,000, the estimated total development cost of the project is slightly more than \$24 million. There are several ways to finance the cost of the facility as described later in this report.

Economic conditions have change dramatically since this process was initiated resulting in significant new factors, both positive and negative, that must be considered in determining whether or not to proceed with the project at this time. Proceeding with the facility at this time would accomplish a stated City Council objective of retaining ice skating as a recreational amenity in Pasadena while returning the historic ballroom back to the control of the Pasadena Center Operating Company (PCOC). Given the climate of the construction industry the current bid price is likely to be the lowest possible. The project has received its design review and entitlement and is ready for building permits and a management agreement has been negotiated with an experienced operator. In sum, the project is ready to construct.

Based on the cash flow projections contained in the pro forma the project pays for itself over a 30 year period, however, during the first 10 years of operation there is a cumulative loss of \$3.06 million, which could rise higher if revenues fall below projections and/or expenses exceed estimates. Consequently, some form of subsidy, either annually or an upfront contribution to 'buy down' the debt service will be necessary to cover the first 10 years of operation.

This occurs at a time of fiscal uncertainty when the State of California is considering budget balancing options that may impact the City's revenues and overall the economy remains weak. Moreover, the addition of debt to the City's

balance sheet combined with these factors may likely have a negative affect on the City's bond rating which, if it occurs would impact future borrowing costs.

Given these considerations, the City Council could choose not to proceed with the project. If the Council decides not to proceed with the new facility, it is recommended that the ice skating facility at the Convention Center be retained and improved. Staff would work with the Convention Center staff and Board to develop a rehabilitation plan for the facility and evaluate options for managing the facility as the current lease terminates in November 2011. This action would preclude the rehabilitation of the facility as a ballroom. However, at this time, the PCOC does not have the funds necessary for this investment.

BACKGROUND

Construction Cost and Bid Award

In August 2005, the City Council amended the Capital Improvement Program Budget to include a new project in the Municipal Buildings and Facilities section titled, Pasadena Ice Skating Facility. This project was approved by the City Council to assist the Pasadena Ice Skating Center (PISC) in finding a new location for the ice skating facility that is currently located in the ballroom at the Convention Center. It has been the desire of the PCOC to relocate the ice rink and restore the historic ballroom as part of the conference center expansion. Subsequently, The Albert Group Architects was hired by the City for design of the new ice skating facility.

The scope of the work for the project includes construction of an approximately 65,000 square foot commercial recreational ice skating facility (containing two NHL-sized rinks) and surface parking for approximately 143 parking spaces. Other amenities include spectator seating, food preparation and eating area, small retail shop, skate rental, locker rooms, restrooms, lobby and waiting area.

The project was put out for competitive bid and the apparent low bid came in at nearly \$22 million, considerably higher than estimated. The primary factors for this situation were construction cost inflation for specialty public works facilities, and additional structural requirements due to site conditions.

City Council rejected all bids on March 10, 2008 and directed staff to value engineer the project and rebid. Staff analyzed various options in an effort to more closely align the project costs and the project budget including a redesign which was completed in 2009.

The redesign of the project was advertised in the Pasadena Star News on March 3, 2009. In addition, the Notice Inviting Bids was published on the City's bidding website, Reed Construction Data, McGraw-Hill Construction News, and Santa Clarita Builders Exchange in order to solicit qualified bidders for the project. On

March 10, 2009 a mandatory job walk was held at the project site, with 27 prospective general contractors in attendance.

A total of seven bids were received at the bid opening of April 1, 2009, as follows:

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| 1. Mallcraft, Inc. | \$17,849,000 |
| 2. Sinanian Development Inc. | \$18,688,000 |
| 3. Howard S. Wright Constructors, L.P. | \$19,228,000 |
| 4. Bernards Bros. Inc. | \$19,709,000 |
| 5. Morillo Construction | \$19,879,000 |
| 6. DJM Construction | \$20,175,000 |
| 7. Pinner Construction | \$21,053,000 |

Subsequent to the bid opening staff performed a reference check on the ostensible low bidder, Mallcraft Inc., reviewed their business practice history with the Department of Industrial Relations and conducted a litigation search. Based on the information received, Mallcraft, Inc., has been determined to be the lowest responsive and responsible bidder. The proposed contract amount of \$19,633,900 includes the base bid plus an amount equal to 10% of the bid to accommodate any necessary change orders. The total project cost is slightly greater than \$24 million as illustrated below:

Ice Rink Project Costs	
Underground of Utilities	\$910,000
Pre-entitlement consulting cost	\$160,000
Project Design and Construction Management Costs	\$3,320,864
Construction Cost	\$17,849,000
Construct Contingency	\$1,784,900
Total	\$24,024,764

Management Negotiations

Prior to October 2007 and with City Council authorization, staff had been negotiating a proposed management agreement for operation of the new ice skating facility with Pasadena Ice Skating Center (PISC), the leasehold operators of the existing facility.

In October 2007, staff was contacted by representatives of the Los Angeles Kings Hockey Team who indicated an interest in managing the new facility though an associated entity, Polar Ice Ventures (PIV). The Kings/PIV were invited to submit an operating pro forma and PISC was invited to update its prior analysis for the purpose of determining which potential operator could best operate the facility and maximize revenue needed to service the associated debt.

A comparison of the two pro formas indicated that the Kings/PIV proposal would result in higher net income for the facility/City. As a result in August, 2008 the City Council agreed to terminate negotiations with PISC and authorized staff to enter negotiations with the Kings/PIV to complete a management agreement for the operation of the proposed ice rink facility. Subsequently, the Kings informed the City that their relationship with PIV is such that any agreement for operation and management of the facility would be between the City and PIV exclusively and that the Kings would enter into a separate agreement with PIV to provide naming rights, advertising and sponsorship sales similar to the arrangement they have for operation of the Toyota Ice Skating Center in El Segundo.

Staff has completed negotiations with PIV, which is proposing to form Polar Ice Enterprises Pasadena (PIEP) to manage the City's new facility, on the proposed management agreement, the key terms of which are outlined in Attachment A and include:

1. Term of the Management Agreement
2. Management Fee
3. Naming rights and Participation in Gross Sponsorship Revenue
4. Public Benefit Program
5. Local Hiring Program
6. Marketing Program
7. Community Outreach
8. Annual Budget Review

Proposed Project Financing

As indicated above the total project cost is slightly more than \$24 million. Of this amount \$3 million has already been funded by the Pasadena Center Operating Company. The \$21 million balance is to be funded either by bond proceeds, or a combination of bond proceeds and General Fund contribution.

Staff proposes issuing bonds that will generate a net \$21 million to complete the funding of the project. The bonds would be structured to have level debt service with interest only payments during the first two years of operation of the ice rink. In this scenario, the annual debt service is estimated at \$1.84 million. The projected net operating income (NOI) of the project is estimated at \$914,746 for the first year of operation and increases to \$1,996,706 by the 11th year of operation, when it turns profitable based on the pro forma. Therefore, during the first ten years of operation, the project will require annual subsidies to cover its revenue shortfall which is the difference between the annual net operating income and annual debt service. In this case, it is estimated that the cumulative subsidy for the first ten years will total \$3.06 million.

A sensitivity analysis indicates that if the actual NOI falls 10% below the projected NOI in the pro forma, the amount of the cumulative cash shortfall during the first ten years increases to \$4.5 million. Additionally, if the NOI drops

20% below projections, the required cumulative subsidy grows to \$6.4 million. Conversely, if the facility exceeds expectations for NOI the amount of cumulative subsidy would be reduced accordingly.

The recommended financial approach is based on the following reasoning: 1) Today's interest rates are at historic low levels and liquidity in the municipal bond market has significantly improved as compared to several months ago, therefore issuing bonds in today's market is preferred rather than taking future interest rate risk. 2) The proposed approach does not require any upfront contribution from the General Fund, consequently will not reduce the General Fund's fund balance, a factor that is closely watched by the municipal bond rating agencies. Nevertheless, it is important to understand that ratings are required on any bond the City may issue and this exposes the City to the potential risk of a ratings downgrade. 3) The projected revenue shortfalls will take place over several years and by making annual contributions to the project the City can properly match the liability.

Staff evaluated several other options as follows:

Financing Option #2

A bond sizing based on the pro forma and the projected net operating income using the fifth year of operation as the stabilized year, with a level debt service structure at a 120% debt service coverage ratio would generate a bond in the amount of \$13.8 million with net bond proceeds of \$11,075,000. This would require an upfront contribution from the City in the amount of \$9.925 million to reach the necessary construction funding level for the project. This analysis also indicates that if the revenues and expenses anticipated by the pro forma are achieved, over the next 30 years, the surplus revenues (the difference between the net operating income and debt service) will generate to the City a net present value of \$16.2 million. Similarly, at 115% coverage ratio, the required upfront City contribution will drop to \$7.6 million and the present value of the surplus would net the City \$13.4 million.

Financing Option #3

The City could structure a bond with debt service payments that match expected net cash flows in the pro forma. Although this approach mitigates the need to invest upfront cash into the project or cover annual shortfalls, it backloads the debt service payments and the principal payments on the bonds to later years. In addition to increasing the total interest costs, this would create additional risks and would not be viewed favorably by the rating agencies.

Financing Option #4

Internally fund the \$21 million required amount by using available cash in the City's pooled investment portfolio until such time the City issues a bond and reimburses itself from the bond proceeds. This could be ideal if there still exists a liquidity crisis in the market and the City is unable to issue bonds because of lack of investor demand. This could also reduce the bond size by eliminating the requirement for a large capitalized interest amount. However, this approach exposes the City to future interest rate risk and in all likelihood interest rates will rise in the next few years.

Project Access

To achieve access to the site of the proposed ice rink the City will need to enter into agreements with Pasadena City College (PCC) as well as Southern California Edison (SCE). These agreements have not been concluded.

The agreement with PCC would cover a driveway located on PCC property that serves as entry to the student parking area. The student parking area itself is on SCE property. Staff has prepared a Memorandum of Understanding between the City and PCC that sets forth the business terms that the City is required to meet in order to use the PCC driveway for access to the ice rink site. These terms entail removing the island medians along Foothill Boulevard, installing a traffic light at the driveway entry, and completing improvements to the student parking area. These capital costs are included in the project costs and financing plan.

In regard to SCE owned land adjacent to the ice rink site needed for access, staff is seeking to enter into a long term lease for the use of the property. SCE has expressed a willingness to accommodate such under certain conditions. Specifically, SCE has requested the City provide a concept plan with an alternative emergency access route to the ice rink site. Staff has had several reviews with SCE representatives and will be submitting these final plans to SCE by July 16, 2009. Additionally, the City may need to pay the market rate for the use of the property and staff is awaiting the results of an appraisal commissioned by SCE.

Additional Questions Raised By City Council

In June 2009 the City Council requested that staff provide certain information and address a number of questions related to the proposed management agreement between the City and PIEP. Attached F is a consolidated response to this request.

FISCAL IMPACT

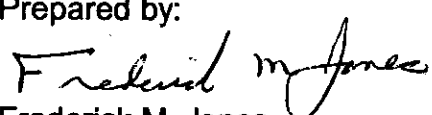
The total estimated project cost is approximately \$24,024,764. Staff is proposing to issue tax-exempt certificates of participation to generate the funds to cover the construction and related project costs. The interest rate on the bonds is estimated at 5.5%. Should the actual rate vary the debt service expense will also vary correspondingly.

Using a traditional level-debt service approach and based on the current pro forma the net revenue from the operation of the project will not be sufficient to cover the debt service for the first 10 years of operation, thus necessitating an annual subsidy from the General Fund. These same projections indicate that over the lifetime of the bonds the project is expected to fully recover its development cost.

Respectfully submitted,


Michael J. Beck
City Manager

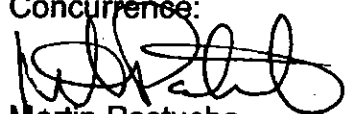
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Attachments:

- Attachment A – Key Term of Proposed Management Agreement
- Attachment B – 30 year pro forma with 4% growth in revenue and 3% in expenses
- Attachment C – 30 year pro forma with 3% growth in revenue and 3% in expenses
- Attachment D – Bond sizing based on Year 5 stabilized revenues
- Attachment E – Reimbursement Resolution
- Attachment F – Responses to questions from City Council
- Attachment G - Management and License Agreement