

SEP 13 2012

September 13, 2012

**By Hand Delivery**

Ms. Laura Neumann  
City of Colorado Springs Chief of Staff  
30 S. Nevada Ave., Suite 601  
P.O. Box 1575, Mail Code 601  
Colorado Springs, CO 80901-1575

**Re: Colorado Springs Urban Renewal Authority Best Practices**

Dear Ms. Neumann:

At your request, we have prepared this letter which reflects recommended topics for discussion regarding the Colorado Springs Urban Renewal Authority ("CSURA"). This firm was charged with the responsibility of completing a review of CSURA records, coupled with interviews on selected topics pursuant to Section 1.2.308 of the City Code. A. Marvin Strait, CPA/ABV, CVA, CFF, also assisted in this review, with a particular emphasis on the University Village, as referred to below.

I invite your attention to the following:

**I. UNIVERSITY VILLAGE:** On February 1, 2008, CSURA issued two categories of bonds: (1) \$47,125,000 Senior Tax Increment Special Revenue Bonds, Series 2008A, ("Series A Bonds") and (2) \$7,505,000 Subordinate Tax Increment Special Revenue Bonds, Series 2008B ("Series B Bonds") (collectively, the "Bonds"). The Bonds were issued for the purpose of financing a portion of the public improvement costs and other costs associated with the construction of the University Village Shopping Center, to provide capitalized interest, to provide a reserve fund, and to pay the costs of issuing the Bonds. The Bonds are solely secured and payable from "Pledged Revenues", which consist of monies resulting from Incremental Property Tax Revenues, Incremental Sales Tax Revenues, and all income from investment and reinvestment of the trust funds. The bondholders are sophisticated institutional investors.

Pursuant to Section 2.04 of the Indenture of Trust ("Indenture"), interest on the Series A Bonds is calculated at 7.00% per annum, payable in semi-annual payments on June 1 and December 1 of each year, commencing with the first payment on June 1, 2008. The Series A Bonds mature on December 1, 2029. Interest on the Series B Bonds is calculated at 7.50% per annum, payable in annual payments on December 15 of each year, commencing with the first payment on December 15, 2008. The Series B Bonds mature on December 1, 2029.

CSURA advised the Colorado Springs City Council ("City Council") that there was a \$50,000 default in December 2011 ("December 2011 Default"). The December 2011 Default occurred when the Pledged Revenues were insufficient to pay the amounts due on the Series B Bonds.

Pursuant to Section 5.03 of the Indenture Agreement, a reserve fund was established for both the Series A Bonds and the Series B Bonds. Originally, the Series A Bonds had a reserve fund (identified in the bond documents as the "Senior Account") of \$4,712,500. The Series B Bonds had a reserve fund (identified in the documents as the "Subordinate Account") of \$750,500. The December 2011 Default occurred when the Pledged Revenues (as defined in § 1.01 of the Indenture) to pay the bonds were insufficient to make the required payments of \$2,494,375 due on December 1, 2011 for the Series A Bonds and \$687,875 due on December 15, 2011 for the Series B Bonds. In order to meet the 2011 payments to the bondholders, the sum of \$913,124.58 from the Senior Account was utilized to make the payment on the Series A Bonds. However, when the funds were utilized in the Subordinate Account to make payment on the Series B Bonds, there were insufficient funds available to make full payment. The Subordinate Account had already been previously exhausted meeting prior obligations on the Series B Bonds. In summary, there is no longer any reserve available for the Series B Bonds that previously was \$750,500.

As a result, on December 15, 2011, the Series B Bonds could not be fully funded and therefore, the December 2011 Default occurred. For further detailed information on the bonds, please review the bond documents and also the 2011 CSURA independent auditor's report.

We have been informed by CSURA's CPA, CliftonLarsonAllen, that it is expected that the balance of the Senior Account for payment of the Series A Bonds will be exhausted to meet payment obligations for this December 2012.

In summary, there will no longer be any reserve for the Series A Bonds that previously was \$4,712,500. We do not know if the Series A Bonds will be in default. There will also be a further default on the Series B Bonds.

It does not appear the depletion of the reserves was identified to the City Council or the City Administration at the time the December 2011 Default was disclosed.

CSURA's position is that no one could have reasonably predicted the financial collapse in the United States which occurred in approximately September-October 2008. As a result, the leasing of the University Village Shopping Center is well behind the forecasting provided in the limited offering memorandum that went to the institutional investors for this project.

One issue that has been raised is the inability of CSURA to review the Sales Tax Revenues for those businesses that would be subject to the Tax Incremental Financing ("TIF") to insure all TIF revenue is received. City Attorney Chris Melcher has correctly concluded that the City is unable to provide that information voluntarily. Denver Urban Renewal Authority ("DURA") attempts to include a provision in its redevelopment agreements requiring the developer and its tenants to provide this information to it on a confidential basis. This should be implemented to avoid this problem in the future.

**II. COPPER RIDGE:** An issue was raised as to what, if any, of the TIF revenue for the Copper Ridge Project had been spent. This is a project that did not have a development agreement in 2011. The CSURA determined to charge \$20,000 for 2012 for administrative expenses. Jim Rees at CSURA advises that none of the Copper Ridge TIF revenue went for the payment of any other projects. Other projects are also charged annual fees for contributing to the overall administrative cost to operate the CSURA.

**III. IVYWILD SCHOOL:** A number of issues were raised by the developers of the Ivywild School project ("Ivywild"):

- The Ivywild developers were initially provided with a spreadsheet that included a total of \$1,250,000 in fees.
- There appeared to be a lack of organization with the CSURA, as there was no standard packet of information, no apparent benchmarks for the project, and no standard fee structure.
- The Ivywild developers were advised very late in the process that an analysis needed to be done as to the tax exempt status of the lender. A \$20,000 cost was assessed for the Kutak Rock law firm. The Ivywild developers were advised that this is a "standard fee". The Ivywild developers' view was that if it was a "standard fee", they should not have been advised so late in the process.
- The Ivywild developers stated there was a \$5,000 fee for sales forecasts that also came very late in the process.
- It did not appear that the services that were charged to the Ivywild developers were done on a competitive bid basis. The Ivywild developers were advised by CSURA to simply let the CSURA go forward with their process.
- At a meeting on December 11, 2011, the Ivywild developers advised that they were being charged an additional fee of \$100,000. CSURA was asked what the \$100,000 was for, and the Ivywild developers never received a satisfactory answer.
- There was considerable discussion about the negotiation of fees, and ultimately an acceptable fee was reached from the Ivywild developers' perspective. It was the perception of the developers that the CSURA was simply trying to generate funds for a purported significant CSURA budget shortfall.

Per Chuck Miller of CSURA, these developers had not been involved in an urban renewal project before and were generally not real estate developers by background. Mr. Miller acknowledges that these matters could have been explained more fully and completely to the Ivywild developers. As to the specifics, Mr. Miller stated the following:

The spreadsheet that stated the fees of \$1,250,000 was just part of a process of testing the revenues that would be available to pay off the loan. This figure was plugged in from other project proformas. It was never the intention of CSURA to charge \$1,250,000 in fees on a project that would cost less than half that amount to develop. In any event, CSURA could have better handled the process with respect to communicating to the Ivywild developers what was being generated.

CSURA advises that each transaction stands on its own, including the fee structure. Therefore, there is not complete standardization of the process.

While the Ivywild developers view that the charging of fees to examine the tax exempt status for the lender and the fees for sales forecasts were raised late in the process, per Mr. Miller, to those experienced in the urban renewal process, that would not have been unusual. Nonetheless, Mr. Miller emphasized that they could have better explained the process.

CSURA has vendors that they generally rely upon and have used in the past. Therefore, absent something extraordinary, CSURA does not specifically put out to bid legal services, blight studies, or other services when they have used reliable vendors in the past.

With respect to fees, CSURA states that every deal stands on its own as a negotiation. CSURA does negotiate these fees with an eye toward generating additional revenue for CSURA for operating expenses. This is not an unusual part of the process and is generally accepted in the industry.

**IV. PREPARATION OF A CITY-SANCTIONED REDEVELOPMENT PLAN:** Consideration should be given to incorporating into the City's comprehensive plan ("Comprehensive Plan") goals and objectives that would include redevelopment projects that can be directed by the CSURA. Apparently, urban renewal plans were part of the City's Comprehensive Plan many years ago. Carl Schueler is the City's Comprehensive Planning Lead. Mr. Schueler has, in the draft stages, the City of Colorado Springs' Infill and Redevelopment White Paper ("White Paper"). The White Paper is a work in progress at this point in time. However, Mr. Schueler was kind enough to highlight a few of the sections related to his views regarding urban renewal. One proposed recommendation is that any infill strategy be aligned with an agreed-upon written City Economic Development policy (coordinated with the Chamber/EDC) and a companion policy for use of the CSURA. Although we would defer to a full reading of the White Paper, it fairly supports having a global coordinated policy for infill, economic development, and urban renewal.

**V. URBAN LAND INSTITUTE ("ULI"):** The ULI and the International Downtown Association presented an Advisory Services Panel in Colorado Springs in June 2012. The presentation was entitled "An Era of a New Renaissance for Colorado Springs".

A PowerPoint presentation was made at this meeting, and a written report of recommendations will be forthcoming. The ULI report should be reviewed and considered as part of the overall economic development effort referred to herein.

**VI. COORDINATION OF VARIOUS RELATED ENTITIES:** There are multiple entities that should be coordinated moving forward in the best interests of economic development for Colorado Springs. They include the Colorado Springs Downtown Development Authority ("CSDDA"), the Downtown Partnership of Colorado Springs ("DPCS"), Colorado Springs Community Ventures Inc. ("CSCV"), the Greater Colorado Springs Chamber/Economic Development Corporation ("C-EDC"), the Downtown Renaissance Solutions Team, the Streetscapes Solutions Team, and the Transit Solutions Team (collectively, "CS Solutions Teams"). The City should consider a process to coordinate the various efforts of all of these entities or at least regular periodic meetings of the organizations. This would include evaluating the possibility of shared expenses, joint staff, and other synergistic opportunities. Ultimately, one person could be appointed to continue this coordinated effort in the best interests of Colorado Springs economic development.

**VII. DEVELOPMENT COMMUNITY CONCERNS:** Some of the concerns raised from the development community include the following:

- Possible favored utility rates
- Favored entitlement requirements
- Expediting the entitlement process

Some determination needs to be made as to whether any of those issues can be addressed to the mutual satisfaction of the CSURA, the City, and the development community.

**VIII. PROACTIVE APPROACH TO PROJECTS:** The CSURA could be proactive in identifying projects that would be appealing to a developer utilizing the CSURA process. If the CSURA were to take a more proactive approach and was required to advance any initial cost, one way to reduce expenses would be to have blight studies and proposed urban renewal plans completed by City Planning staff (subject to an appropriate defined separate legal relationship with the CSURA). Outside consultants typically cost \$10,000 - \$15,000 for a blight study, and as much as \$25,000 for an urban renewal plan.

**IX. CSURA REVENUE:** A consistent game plan needs to be developed with respect to revenue to be generated for the CSURA's operations, balanced with reasonable fees for the developer. This issue is of considerable concern. On one hand, the CSURA needs funds to be able to operate. On the other hand, the development community wants to have reasonable fees in order to be able to move forward. In the typical case, both with CSURA and elsewhere, there is a separate fee negotiation for each project. DURA typically charges a 1% "origination" fee which is based upon the maximum reimbursable amount the developer is entitled to receive. DURA also typically charges a 1% annual "priority" fee, which is also based upon the same calculation. Finally, DURA requires the redeveloper to reimburse DURA for all third-party fees and expenses, including attorneys' fees. CSURA needs to explore all reasonable avenues that strike the appropriate balance regarding fees.

The most recent method of charging fees is a "Predevelopment Retainer Agreement". The first is being used on the Copper Ridge Project. In summary, the developer pays a retainer deposit which is utilized by the CSURA to pay costs that are incurred which include, but are not limited to, economic impact reports, market feasibility studies, legal fees, CSURA staff time billed per hour, other third party consultant fees and expenses, and any other reasonable costs and expenses.

Additional ways should be explored regarding the most appropriate method for developing a fee structure that is adequate to fund CSURA operations, and is a fair and reasonable fee for developers.

**X. ATTORNEYS:** There are attorneys who specialize exclusively in Urban Renewal Authority matters that are available at reasonable rates.

**XI. ADMINISTRATIVE SUPPORT:** The CSURA and the City should jointly determine whether it would be most cost efficient and effective to utilize (with an appropriate separate legal relationship) City employees who are contractually "loaned" to the CSURA for various tasks, including

administrative support. Administrative operations are currently handled by an independent contractor.

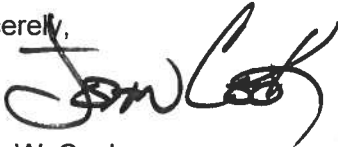
**XII. CONSULTANTS:** Presently, there are two independent contractor and consulting agreements with urban renewal specialists. One such agreement is with Mr. Miller, who concludes his contract this September 2012. Jim Rees is under a contract which provides for a payment of \$10,000 per month plus reimbursable expenses. Mr. Rees' agreement can be terminated on 90 days written notice. Mr. Rees' agreement also provides that he can work for other companies or employers so long as there is no conflict of interest with his work with CSURA. Neither one of the contracts provide for any benefits.

Like any other expense, there should be an on-going evaluation of performance and compensation for the independent contractors.

**XIII. POSSIBLE COST SAVINGS CONSIDERATIONS – CSURA FACILITIES:** A business lease agreement was entered into between the CSURA and Michael H. Collins, d/b/a The Van Dyke Lofts. The lease expires on November 15, 2012. The rental is \$1,113 per month. This is presumably a market rental. Consideration should be given as to whether the CSURA could rent City office space at a nominal cost, subject to a written lease agreement that clearly delineates the separation of the City (as Lessor) and CSURA (as Lessee).

Please let me know if you have any questions, concerns or comments.

Sincerely,



John W. Cook

Partner  
john.cook@hoganlovells.com  
D 719 448 5912

cc: Chris Melcher, City Attorney (*via hand delivery*)