

Request for City Council Committee Action from the Department of Finance

Date: June 24, 2008
To: Community Development Committee
Referral to: Ways & Means/Budget Committee

Subject Green Institute Loan Status and Recommended Action

Recommendation

The Finance Department is providing details below regarding the current status of the Green Institute's Section 108 HUD loan and the Delinquency Loan entered into on May 1st, 2007 and now recommends approval of a plan to hire a professional leasing agent/property management firm to manage the Green Institute facility.

Previous Directives

11/14/05 Green Institute Loan Update
3/27/06 Green Institute Section 108 HUD Loan Update
11/27/06 Green Institute Loan Update – forwarded to
the Community Development Committee
4/17/07 Green Institute Loan Update – Delinquency Loan approval
8/21/07 Green Institute Section 108 and Delinquency Loan Update

Prepared or Submitted by: Michael Abeln
Director, Capital & Debt Management
673-3496

Approved by: Patrick Born, City Finance Officer _____

Steven Bosacker, City Coordinator _____

Presenters in Committee: Michael Abeln, Director, Capital & Debt Management and
Patrick Born, City Finance Officer

Financial Impact (Check those that apply)

- No financial impact - or - Action is within current department budget.
(If checked, go directly to Background/Supporting Information)
- Action requires an appropriation increase to the Capital Budget
- Action requires an appropriation increase to the Operating Budget
- Action provides increased revenue for appropriation increase
- Action requires use of contingency or reserves
- Other financial impact (Explain):
- Request provided to the Budget Office when provided to the Committee Coordinator

Community Impact (use any categories that apply)

- Neighborhood Notification
- City Goals
- Comprehensive Plan
- Zoning Code
- Other
- Not applicable

Background/Supporting Information

This letter is an update to the August 21, 2007 letter regarding financial details about the Green Institute's Section 108 Loan and Delinquency Loan repayment history. The Delinquency Loan became effective May 1st, 2007 and contained a provision for the Finance Department to provide a quarterly receive and file update on the status of these loans.

All scheduled Delinquency Loan payments were timely in 2007 and the November 1, 2007 Section 108 Loan interest payment was made timely, so no update was prepared for November 2007.

Current Financial Status as of 6/12/08:

Section 108 Loan – Initial amount was \$3,500,000 and the current outstanding principal balance is \$3,048,000.

As mentioned in the last update, the Green Institute was unable to pay the full August 1, 2007 principal and interest payment of \$167,082.08 on the Section 108 Loan on the due date but the entire amount was paid by August 21, 2007. Part of the capacity to pay the August debt service was provided by a \$100,000 loan from the Minnesota Non-Profit Assistance Fund which operates out of the Green Institute building.

The February 1, 2008 quarterly interest payment on the Section 108 loan was \$44,356.80. The Green Institute has paid \$9,500.00 toward this bill and \$34,856.80 remains outstanding. This loan is a variable rate loan and has benefited from the interest rate cuts initiated by the Federal Reserve. The May 1, 2008 interest amount due was \$24,580.50. There have been no payments received against this bill bringing the total currently delinquent amount on the Section 108 loan to \$59,437.30. On August 1, 2008 there will be quarterly interest due and an additional principal amount due of \$128,000. The City has continued to make all payments to HUD (the loan originator) on a timely basis despite any delinquencies from the Green Institute.

As a result of the delinquency described above, the Finance Department has been in contact and discussions with the Green Institute since early February. By early April, it became apparent that the delinquency was more than a simple matter of being tardy.

Delinquency Loan – Initial amount was \$216,188.66 and the current outstanding principal balance is \$184,826.82.

In 2008, payments of \$2,374.04 per month were received for January through June but the May and June payments were received together on June 11th. This loan is now current.

Economic Health of the Green Institute -

Finance staff met with Green Institute management and the president of the Green Institute Board of Directors on 4/18/08. Interim financial statements for 2007 and early 2008 were reviewed and the slowing business environment was discussed. While business was generally strong during most of 2007, it began to deteriorate in November and December. Several factors negatively impacting business at the Reuse Center and its satellite stores included the cold winter, deteriorating housing values, tighter credit conditions and other economic ills for developers and individuals. The Osseo store which had been operating with a small margin will be closing within 60 days due to the slow conditions.

Green Institute management indicated that lack of working capital has made it difficult to get their message out at a time when more advertising is needed. Lack of sufficient cash flow is causing management to spend more time managing operating costs and debt payments and less time growing the business. To reduce salary costs, the Executive Director and Operations Manager jobs have been combined into one position which saves money but reduces time for doing strategic planning to develop the various lines of business. Leases are also being renewed at higher rates and the Green Institute building is 100% occupied which is helping revenues. However, the Reuse Center and Green Institute offices utilize approximately 35% of the total space in the building for which they do not pay rent.

The Green Institute is currently one month behind on their loan payments to Western Bank, the 1st mortgage holder. The outstanding principal balance with Western Bank is approximately \$507,000 and is subject to a full balloon payment and/or refinancing in February 2009.

The Finance Department has been working with the Green Institute on its financial challenges for several years. While there have been triumphs and setbacks along the way, the financial statements indicate that the debt burden is not manageable under the current business model for the Green Institute. We therefore recommend the following options for consideration to minimize financial risk to the City.

Option 1: Hire Lease Agent/Property Management Firm: (Recommended Option)

Hire a professional lease agent/property management firm to manage the Green Institute facility to maximize financial results in the short-term and allow time for the best long-term strategy to develop for the City. This recommendation would allow for the facility to continue operating as an Eco-Enterprise Center to ensure grant agreement provisions are met and would include the Green Institute vacating and/or leasing their space at market rates.

Pros:

- Professional management of leasing arrangements/rates, receipts and payments properly directed to building obligations (loan payments/utility bills, etc.) rather than to Green Institute operational expenses.
- Provides Green Institute with an avenue to continue as a going concern, albeit possibly in a much diminished capacity.

- All current loan arrangements and building ownership remains intact.

Cons:

- Net Lease revenues and Green Institute profits may not cover debt obligations/operating expenses on the building.
- Cost of professional services creates additional burden on building finances.
- City retains second mortgage position behind Western Bank limiting flexibility.
- Additional administrative burden on City to manage contractor, accounting issues, etc.

Option 2: Payoff Western Bank and foreclose on mortgages with the Green Institute.

As building owner, the City would have control over the leasing, sale, reuse and/or timing of the disposition of the facility. However, long-term operation of a facility of this type is not an activity typically undertaken by the City.

Pros:

- City has greater capacity to act on a timely basis with decisions regarding what to do with the building and when.
- May allow for lower cost financing thereby minimizing loss or maximizing gain to the City upon disposition of building.
- City may recover upfront losses, financing costs through ultimate sale of building.

Cons:

- City has to commit funds to payoff Western Bank ~ \$500,000.
- City may take a financial loss for foreclosed loans with Green Institute.
- City still needs to hire a leasing agent to manage facility.
- Additional management burden involved with building ownership.