IV. IMPLEMENTATION

Investment decisions made today will affect Alexandria's prosperity for decades to come

I. Overview

Alexandria's growth in the past decade is partially the result of planning and infrastructure investments such as the Eisenhower and King Street Metrorail stations, the urban street grid, and that were the result of both public and private investment. Through the build-out of the plan area, the future Potomac Yard Metrorail station, land uses, street grid and associated infrastructure will enable long-term redevelopment for the City, similar to infrastructure investments in the City decades ago. If the City implements all of the recommendations of the Plan, the City could capture a significant share of the projected regional growth. The Plan lays out an ambitious twenty- to thirty-year vision for Alexandria's North Potomac Yard.

It is important to understand the degree to which the implementation and infrastructure components of the Plan are interrelated and depend on one another for their success. In addition, implementing the required infrastructure and development must be carefully phased. The transportation and circulation through the site are based on the provision of a Metrorail station and dedicated transit. Without a Metrorail station, this Plan does not work and is not feasible. The success of the residential neighborhoods will depend on the viable retail and commercial uses which will provide convenient access to goods and services. Open space and design excellence add value but will also add amenities for the workers, residents, and visitors. Without all of the necessary infrastructure improvements and amenities working together and phased appropriately potential tenants, residents and retail patrons will go someplace that does provide the necessary level of infrastructure improvements and amenities.

This implementation chapter reflects the proposed land use and density, as well as the current analysis related to elements of the Plan such as infrastructure, transportation, community facilities, phasing and fiscal impacts, among others. The implementation chapter serves several purposes that include:

- Evaluate the overall financial feasibility of the land use plan;
- Understand and describe the project economics and general financing concepts;
- Understand and describe the basic financial transaction structure between the City and developers proffers;
- Ensure that private development provides funding for public improvements and their on-going maintenance; and
- Finding the right balance of private and public funding that is needed to construct the Metrorail station.

II. Infrastructure, Amenities, and Phasing

The necessary cost to construct a new WMATA Metrorail station is approximately $210 to $250 million (2015 dollars) for the northern Metrorail station options discussed within the Plan. In addition, $16 million dollars in construction costs are anticipated for the dedicated transitway, with an additional $5 million anticipated for other transportation improvements, including a future east-west connection to Commonwealth Avenue and intersection improvements at E. Glebe Road and Route 1. Transportation is not the only needed infrastructure given the number of employees, residents, visitors and students which will eventually reside, work or visit North Potomac Yard. Significant additional investment in sewer and water distribution and management are needed to accommodate the basic needs generated by the proposed amount of development. It is projected that the basic amount of sanitary sewer and stormwater infrastructure will be $__________. In addition, necessary services such as police, fire and schools will require services from the proposed development which are anticipated to be $____________.

The discussion of sources, uses and revenues below provides a static summary of total project financing, total project costs and total revenues. In actuality, these costs and revenues are incurred over time from the inception of development through the buildout of the project and the impacts of these timing issues have an enormous impact on the overall financial feasibility of the project. As is often the case with large, complex, urban infill redevelopment efforts, in the initial years of planning and constructing a large proportion of overall costs must be incurred and revenues follow much later. At North Potomac Yard this is particularly true as a result of the significant infrastructure improvements that must be made in the early phases in order to support development. The lists in Section III of this chapter provide for the major transportation and infrastructure projects proposed in this Plan. Note that most costs of the Metrorail station and infrastructure are "front loaded" – as by far the largest expenses occur in early years of redevelopment.

III. Zoning and Developer Proffers

The City's Zoning Ordinance is its key regulatory tool, and is used to direct the size, character, use, and location of development throughout the City. A new Coordinated Development District is planned for Landbay F and require a rezoning process for the plan area.

The proposed increase in allowable development from 600,000 square feet to approximately 7.5 million square feet will require significant investment from the developer for infrastructure and public benefits. The following are standard site plan requirements for the City, which are generally included in the development special use permit process:

- Street and Street Improvements – Sidewalks – Street right-of-way (necessary to serve the needs of the site)

- Applicable Utilities such as Sanitary and Storm Sewer – Water – Electric (necessary to serve the needs of the site)
- Parks – Open Space (necessary to serve the site)
- Voluntary Affordable Housing Contribution
- Voluntary Public Art Contribution (policy under development)
- High Quality Architecture and Streetscape
- Underground Parking
- Sanitary Sewer and Stormwater

In addition, in order for the development proposed in this Plan to be implemented, the following major transportation infrastructure improvements will be required:

- WMATA Metrorail Station
- Dedicated High-Capacity Transitway

This Plan recommends a number of other desired community benefits that are desired by the City to be at additional cost to the developer but where negotiations are ongoing, which includes the following:

- Site for future school
- Civic Uses – Performing Arts Theater, etc.
- Green – Sustainable Building Elements
- Sanitary Sewer and Stormwater

The developer's ability to invest in community benefits is driven by the strength of the market (i.e. achievable rents and revenues) and development costs. Although Potomac Yard is in a relatively strong market, there will be costs associated with infrastructure development. The developer must obtain enough income from a project to pay development costs and achieve an adequate investment return. When the developer obtains a return exceeding the return-on-cost threshold there is an opportunity for the developer to invest in public amenities.

The proposed rezoning would significantly increase the amount of density and associated value that could be provided as proffers to the City. The presence of a Metrorail station significantly increases proffer potential by creating market value (higher rents) and reducing development cost (less parking required). (See Figure 1). In addition, all other things being equal, absorption (the amount and pace of development) near Metrorail stations is faster than non-Metro locations. Office rents at Metrorail station in Alexandria are almost one and a half times to comparable non-Metrorail locations. (See Figure II). As such, the ability for the developer to contribute significantly toward public benefits increases significantly, almost ten fold, if a Metrorail station is constructed.

Figure I

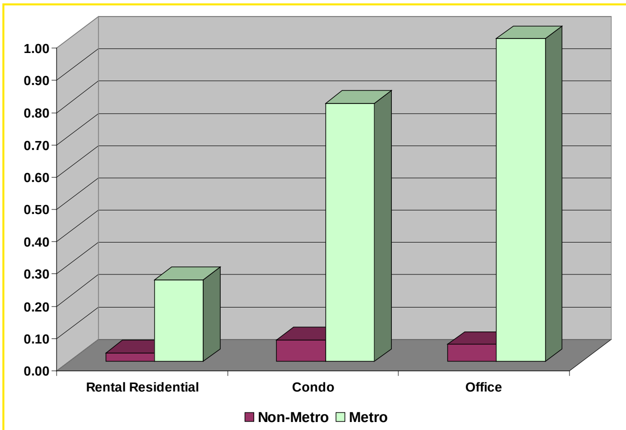
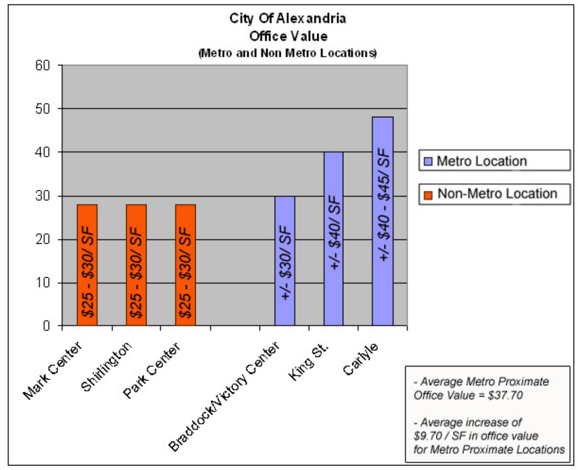


Figure II



While the current economic state of commercial real estate development makes a calculation speculative, accounting for developer cost and profit margin, by one conclusion, the proposed increase in allowable development on the property with the construction of a new Metrorail station will increase the value of the land by as much as $240 million, creating value that can be spent toward community benefits. (See Figure III). The proffer amount will have to be refined as part of the implementation phase of the project.

Figure III

2.5 FAR, Metro
Office/Retail Mix
Potomac Yard Retail Center

	Existing Zoning		2.5 FAR		
Land Area (Sq Ft)	3,008,589		3,008,589		
FAR			2.5		
FAR Feet	600,000		7,521,473		
Retail	*600,000*	*20%*	*1,504,295*		
Office	*0*	*80%*	*6,017,178*		
Retail					
Land Value	$90,000,000		$60,171,800		
Value /FAR Ft			$40.00		
Office					
Land Value	$0		$270,773,000		
Value /FAR Ft			$45.00		
					Difference
Total Value	$90,000,000		$330,944,800		$240,944,800
Discount for Profit				10.00%	$216,850,300
Proffer /FAR Ft					$28.83

Source: City of Alexandria; W-ZHA

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IV. Overview of Financing the Potomac Yard Metrorail Station

This Implementation Plan is provided for discussion and planning purposes in connection with anticipated proffers for the proposed rezoning of Landbay F at Potomac Yard, and in connection with anticipated development activities for other landbays at Potomac Yard where developer contributions to construct a Metrorail station have long been contemplated. The proposed rezoning of Landbay F increases the development on that landbay from 600,000 square feet of "big box" retail to 6,395,000 square feet of residential or office, an additional 245,000 square feet of retail, and 170,000 square feet of hotel. Indisputably, according to traffic studies already provided, the transportation network in this area of the City of Alexandria will not support this development, and thus the rezoning cannot be approved, in the absence of the construction of a new Metrorail station.

In contemplating this and developing this implementation plan, this Plan supports the recommendations of the Metrorail Station Feasibility Work group (see final report Potomac Yard Metrorail Station Concept Development Study). In addition, the following fundamental principles should guide the City of Alexandria, its political decision makers, and staff:

- The City is supportive of the type of long-term, quality mixed-use development contemplated at Potomac Yards, and plans to provide the bond financing of the Metrorail station, but the financial risk to the City must be carefully structured and managed.
- The City plans to enact a special tax district on Landbays F, G, H, I, and J as well as Potomac Greens and Old Town Greens, that will help pay for a portion of the cost of the Metrorail station, and to issue general obligation or other types of municipal bonds for such construction, most likely backed by the full faith and credit of the City of Alexandria, or a similar pledge.
- The special tax district could be implemented as early as 2011 to help finance pre-construction and environmental study costs. At this time the needed tax rate and geographic applicability has not been determined.
- No negative cash impact on the City's General Fund in any given year. The projected "gap" between the anticipated tax revenues from the special tax district, per square foot developer contributions, plus additional incremental net new revenues generated by the project, will need to be "bridged" in the early years of the bond financing by firm and sufficient upfront Landbay F payments, so there will be no negative cash impact on the City's General Fund in any given year.
- Any proposed financing must be conservative with a sound financing structure and shared risk. The proposed financing must not put at risk the City's AAA/Aaa bond ratings, as well as projections used for the Metrorail station construction costs, as well as the project build-out timetable and resultant projected tax revenues need to utilize conservative assumptions, so that the downside risks can be minimized. Some of the downside risks also need to be shared by the participating parties.

- The final financing plan when approved by City must be based on final plans approved by the Washington Metropolitan Area Transit Authority and the City, and a guaranteed maximum or other fixed price construction contract for construction approved by WMATA must be in place for the station to be constructed and must be structured to minimize the possibility of cost overruns.
- Even with a combination of special tax district, proffered contributions, other contributions, and increased taxes, it is likely that if projections are not met, the City will have to pay any net shortfalls, and this risk and the impact on the City's ability to do other projects must be factored in to all proffer negotiations to result in a conservative, sound financing structure with shared risk.

A. Discussion

A plan of finance and agreement with the owner of North Potomac Yard (Landbay F) in regard to funding the $240 million (assumes for financing modeling purposes the midpoint of a $210 million to $270 million construction range which is the B options with a 2015 construction midpoint and is also the highest cost of the three options A, B1 and B2 under consideration) Metrorail station to serve Potomac Yard and adjacent neighborhoods is a necessary precedent to any rezoning of Landbay F. Since the additional 7.5 million square feet of additional density of all types contemplated for Landbay F can only occur if the necessary transportation infrastructure (including a new Metrorail station) is provided, it must be certain that the station can be financed, constructed and put into operation.

Financing a $240 million project is an exceedingly difficult challenge given the enormity of this cost. In perspective, $240 million is nominally about two and one-half times the cost of the new T.C. Williams High School recently constructed in the City. Proof of the difficulty of this is that there has been only one new Metrorail station (New York Avenue) constructed and added to the existing 103-mile Metrorail system that serves the entire Washington, D.C. area since the system was constructed starting in the 1970's. This is in large part due to the cost of such station additions, as well as the lack of significant federal and state funding opportunities for adding stations to existing subway systems. Also since individual stations largely benefit individual localities, the Washington Metropolitan Transit Authority (WMATA) does not spend its limited capital dollars on adding Metrorail stations to its system. In Virginia, where State transportation capital funding assistance to localities has collapsed, as the State's transportation tax revenues have fallen sharply and not kept up with demand, there also is no current significant new funding for mass transit capital projects such as a new Metrorail station. The absence of state and federal funding opportunities, leads to the conclusion that any Metrorail station to serve Potomac Yard must be planned to be locally funded and financed, with any state and/or federal funding that might occur reducing that local funding burden.

B. Modeling of Financial Feasibility

In order to determine the financial feasibility of funding a Metrorail station, the City retained the transportation consulting firm of PB Consulting to undertake calculation of tax revenues potentially generated by the development of Potomac Yard, as well as modeling how City-issued general obligation bonds could raise the funds necessary to fund the construction of the station. These bonds would be serviced and repaid by a combination of developer contributions, net new taxes, as well as special tax district revenues.

The PB modeling made the following key revenue assumptions:

1. Tax rates assumed at 2009 levels and policies,
2. Special Tax District at 20-cents per $100 of valuation,
3. As contemplated by the original Potomac Yard CDD approval, all of Potomac Yard (except the most southern Landbay L) including Potomac, Greens and Old Town Greens would be included in the Special Tax District and all net new tax revenues from those landbays (including already zoned Landbays G and H) counted as available revenues,
4. No current tax revenues generated by any Potomac Yard landbays would be counted as available for a Metrorail station financing,
5. Real Estate unit values (i.e., per unit or per square foot values) at 2009 values,
6. 10% value increase assumed for properties within ¼ mile of the Metrorail station entrance, with two entrances to the Metrorail station provided,
7. 6.5% (hotel) to 59.8% (residential) of new tax revenues (not including the $.20 per $100 special tax district revenues) would be assumed to be used to finance City and School services and capital costs to serve Potomac Yard and thus would not be available to assist in the Metrorail station financing.
8. 25-year straight-line build out of planned development starting in 2017, and
9. No federal or state aid.

At the City's direction, PB consulting used the following key bond financing assumptions:

1. 30-year amortization of the bonds, commencing in 2014;
2. Use of AAA/Aaa rated general obligation bonds issued by the City,
3. Capitalized construction period interest, during the first three years;
4. A $275 million bond issuance ($240 million for construction, $30 million for capitalized interest during construction, and $5 million in related bond issuance costs);
5. Interest only repayment in years four, five and six; and
6. Gradual build-up of principal repayment in years seven through seventeen, and then level principal and interest through year thirty.

The results of the PB analysis shows that while there are sufficient net new tax revenues after 2024 to cover the debt service obligation of the Metrorail station bond financing, there is a significant up front gap from 2014 to 2024 (years 1 to eleven). This is because the net new tax revenues generated from development are projected not to grow sufficiently in the first eleven years after the bonds are issued (in part because the buildout of this order of magnitude of new development will be phased over the long term because of the limitations of market absorption). These projections are subject to many variables (actual station construction costs, land valuations, buildout timetable, interest costs, etc) and would need to be rerun and any financing plan adjusted accordingly to the realities of the time in which the decisions of going forward or not going forward with a Metrorail station would need to be made. For this reason, the final underwriting and construction contracting decisions must be based on final approved plans, not to exceed a construction contract price acceptable to the City and its advisors, as well as a sound and predictable financing plan.

C. Developer Contributions

In order to finance a portion of the Metrorail station ($475 million in total debt service over the 30-year period including $275 million in bonds and $200 million in interest) and to close the aforementioned funding gap, it will be necessary for the developers to proffer to pay for a significant portion of the Metrorail station development that will benefit them by increasing the value of their property as well as accelerating when the market will facilitate the development of the property. Without such proffers, including a written agreement about such proffers and other related matters executed with the City by each of the three sets of owners (PYD, RREEF's institutional client, and MRP) their successors, no Metrorail station can or will be built at Potomac Yard. In addition, the proposed density increase in North Potomac Yard/Landbay F of some 7.5 million square feet would not be able to be constructed, as the Metrorail station is precedent for any new development density in Landbay F as it is the only way that such density can receive adequate transportation capacity to function.

Any developer agreements with the City need to recognize the different land use status of the various Landbays at Potomac Yard. For already developed property (Potomac Greens, Old Town Greens, Slaters Lane retail and the Station at Potomac Yard) there would be no developer proffer expected as development has already taken place. Those properties are proposed to be subject, however, (as was originally contemplated in the original Potomac Yard CDD approved by the City in 1999) to the special tax district levy (20-cents per $100 of valuation is currently contemplated).

For the properties within a quarter of a mile of the entrance to the proposed Metrorail station and where the allowed density is already in place (Landbays G and H) but there has not been development, there would be a proposed $10 per square foot contribution (in 2010 dollars and to be adjusted annually for inflation and paid at the time of each building's issuance of a certificate of occupancy) to assist paying for a Metrorail station. There is approximately 2.2 million square feet of development within a quarter mile of the Metrorail station in Landbays G and H. This $10 per square foot would raise about $22 million (in 2009 dollars) which is the approximate cost of adding the second southern entrance to the proposed Metrorail station.

This $10 per square foot contribution can be justified as reasonable in that research has shown that the value of buildings within ¼ mile of a Metrorail station increase in value (i.e., in rents achieved) in comparison with similar properties not that close to a Metrorail station. If a property increases by 10% in long term value or about $40 per square foot, due to the presence of a Metrorail station within a quarter mile, it would be reasonable for the developers to pay $10 of that towards the costs of the Metrorail station. As of the time of the issuance of this chapter (02/03/10), the owners of Landbays G and H have rejected the concept or specific structure of such a contribution.

For the owner of Landbay F, where any upzoning does not currently exist, and would only be approved as Metrorail station dependent, the proffer for the Metro station and for other public amenities should be significantly more than $10 per square foot, as the contemplated possible increase in approved overall density is upwards of 7.5 million square feet. As indicated earlier in this Implementation section of this North Potomac Yard Plan, the potential public increment of value through a rezoning alone (i.e, not including any long term value added from actual construction of higher density improvements) may be as much as $100 million to over $200 million. Given today's unsettled commercial real estate markets, the determination of the value of a rezoning is challenging. A large portion of this public creation of private value should be allocated and proffered towards the new Metrorail station upon which any rezoning would be dependent.

The timing of a proffer payment would need to be negotiated and structured to fit the financing needs of the Metrorail station, and would have to be able to be financed by the developer in the commercial lending marketplace. Some of these funds should be paid upfront and be sufficient to cover the estimated current minimum $32 million gap between projected revenues and projected debt service costs, and some of the funds paid at the time of the development. While paying upfront for infrastructure puts a burden on the development project to be financed, it is a common real estate development practice. For example, PYD paid in 2010 dollars more than $40 million upfront in anticipation of future development to construct the new Monroe Avenue Bridge, as well as tens of millions in already invested, or to-be-invested public infrastructure which will serve their future project.

It would not be unreasonable for the developer of North Potomac Yard/Landbay F to also proffer a significant upfront contribution for the transportation infrastructure – in this case a portion of the costs of the Metrorail station, as well as other public infrastructure. As of the time of the issuance of this chapter (02/03/10), the owners of North Potomac Yard/Landbay F have tentatively agreed to an upfront guarantee in an amount that would be sufficient to close the projected funding gap. Negotiations with the City are active and ongoing on this issue as well as that of other proffers with many details to be worked out.

In addition to the cash proffers, there will have to be negotiations of the allocation of risk, and contingency plans and protections structured to cover circumstances that could arise prior to, during and after the Metrorail Station is constructed. Without such an executed agreement between the City and the owner of North Potomac Yard/Landbay F, on funding and related conditions, no new density authorization can be legally assumed to have been granted by the City through the development and approval of this North Potomac Yard Plan, and therefore no new development could be initiated in Landbay F without a formal executed agreement and an actual rezoning (which is a distinct and separate action from an adoption of a North Potomac Yard Plan).

D. City Risks and Debt Policy Implications

While the financial model's projections and potential future agreements with developers in regard to their contributions could result in a plan of finance for the Metrorail station that is self-financing from developer contributions and net new tax revenues generated by that development, such projections are just projections and reality may be very different. Also City issuance of $275 million in bonds would represent a major, significant change in City debt policies and practices.

First, with regard to the model's projections and eventual reality, it is very difficult to predict real estate development. While real estate development is cyclical in nature, predicting the cycles is difficult. While many real estate pro forma projections proved correct, many real estate pro forma projections prove materially incorrect. The current commercial real estate market place contains many examples of highly inaccurate projections and failed real estate ventures (such as development related local government issued "dirt bonds" that are now in default). While the use of general obligation financing would avoid a default situation, there is the real possibility that once the station was constructed that it would take far more time than the model projects for net new tax revenues to cover bond debt service obligations. This means that there is a risk that a deficit would occur and need to have a funding source. While some of this down side risk to the City and its General Fund may be able to be shared with the developer of Landbay F, in the end of the day it will be the City that is standing behind any bonds issued and would be the City's responsibility as the final backstop and ultimate obligator to pay debt service as it becomes due. Failure to repay the bonds is not a realistic, pragmatic option as it would result in a downgrading of the City's top AAA/Aaa bond ratings and the raising of future borrowing costs (if not an actual inability to access the bond markets to raise capital for City needs some time period).

A second set of major issues for the City are the debt policy implications of the City issuing $275 million in new bonds to finance this new Metrorail station. For several decades the City has had in place very conservative debt policy guidelines with specific numerical targets and limits. This has resulted in the City's debt being considered low in comparison with other jurisdictions by the New York bond rating agencies. If the City issued $275 million in additional bonds it would increase the City's debt burdens in year 2015 and beyond by about 64% (from a projected $433 million in 2015 to $708 million). This would raise the City's primary measure of debt capacity (debt as a percent of property value) from a projected 1.18% in 2015 to 1.93%. In comparison with other AAA/Aaa rated localities in Virginia and Maryland this would shift the City's debt burdens from being on the low end when compared to those localities to the high end when compared to these peer localities.

While this represents a significant, material increase, according to the City's independent financial advisors, it would not in and of itself jeopardize the City's top AAA/Aaa bond ratings. In particular, the rating agencies recognize that the investment in heavy or light rail transit systems is an investment with multi-generational benefit if coupled with new transit-oriented development. This view and bond rating agency acceptance is highly likely to hold in the future, but cannot be guaranteed to not change in the future.

The issuance of $275 million in new debt will have the implication of potentially limiting future major public projects that the City may want to consider funding. For example, if federal, state or other funds are not substantially available to upgrade the planned Potomac Yard high-capacity transitway from a Bus Rapid Transit (BRT) to a street car system, then that upgrade may have to be delayed until such time as a large portion of the Metrorail station bonds have been repaid. The Metrorail and the high-capacity transitway are required to accommodate the traffic associated with the proposed development.