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Inter-Departmental Memo

To: Hon. Norma Gonsalves, Presiding Officer
Hon. Kevan Abrahams, Minority Leader
All Members of the Nassau County Legislature

From: Maurice Chalmers, Director
Office of Legislative Budget Review

Date: September 20, 2013

Re: Review of the Nassau County Veterans' Memorial Coliseum Lease

The County's current lease agreement with the New York Islanders through the Spectacore Management Group (SMG) will expire on July 31, 2015. Prior efforts to redevelop the site using public funds failed; therefore, any revitalization plans would have to be privately funded. Last October, the Islanders announced their intention to move to the Barclays Center in Brooklyn for the fall of 2015. The County faced the prospect of owning an empty and aging facility. The County Executive issued a Request for Proposals (RFP) to redevelop the Coliseum and the surrounding grounds. A selection committee, comprised of County employees was assembled by the Administration to review submitted proposals. The selection committee was advised by the County Executive's Business Advisory Council. The Madison Square Garden Company (MSG) and Bruce Ratner's Nassau Events Center LLC, (NEC) were chosen as the two finalists for the Coliseum's redevelopment.

In mid-August, the County Executive awarded the Coliseum redevelopment lease to NEC. NEC's proposal requires no public financing. The Office of Legislative Budget Review (OLBR) has prepared this memo to provide a financial and economic overview of the NEC proposal. Our analysis relies on the MSG and NEC leases, as well as reports from Public Financial Management (PFM) and KPMG, two consultants whose reports reviewed each proposals.

Current SMG Lease

Under the County's current agreement with SMG, the Islanders are required to make payments to the County for rent, utilities, concessions and parking. The rental amount paid by SMG/the Islanders is fixed at a base rate and increases by an annual Consumer Price Index (CPI) adjustment. The expenses for electric and chilled & hot water are paid by the County and then reimbursed by SMG/the Islanders. In addition, the County is responsible for some capital improvements. An average of roughly $2.5 million in revenue has been collected yearly from 2010-2012.

Proposed NEC Lease

The proposed lease is between Nassau Events Center LLC and the County of Nassau. The initial term of the lease is 34 years. The lease grants NEC three additional five year extensions. NEC will spend approximately $229.0 million to renovate the Coliseum and improve the Plaza. This is based on the $98.5 million estimated for the Coliseum renovation and an estimated $130.5 million for the Plaza.

The Coliseum will be renovated to 13,000 fixed seats. Additional floor seating for events such as concerts would allow the Coliseum to accommodate up to 14,500 patrons. Seating could be adjusted down (to approximately 4,000) in order to suit events demanding less space. Parking spaces would number about 6,500 spots. The Town of Hempstead (TOH) has the final say to determine the zoning for parking spaces at the renovated Coliseum site.

An American Hockey League (AHL) team would serve as the Coliseum's anchor tenant. The renovated Coliseum will host one Brooklyn Nets' preseason game, and the Islanders will return for four regular season home games and two preseason games each season. This arrangement is subject to all applicable NHL approvals. The annual minimum rent would be enhanced by $1.0 million per lease year for 10 years if the Islanders do not return to the Coliseum (i.e. NHL owners reject plan, NHL labor strike, etc).

According to the lease agreement, a number of other sports and entertainment events are scheduled to take place. The New York Yankees would hold a coaches' clinic each season at the Coliseum. A college basketball program will be implemented to promote college basketball games involving NCAA Division I institutions. Golden Boy Promotions, LLC, will organize, stage, and promote periodic multi-card boxing events at the Coliseum. A Grammy award winning artist with regional and national appeal would play a so-called "closing concert" before the renovation process begins. The same artist would perform an opening concert at the renovated coliseum. The Disney Institute will train Coliseum employees.

The lease proposes a 145,000 square foot dining and entertainment complex in the Coliseum plaza. According to Schedule G of the lease agreement, a 10-12 screen movie theater would account for 60,000 square feet of the complex, and another 60,000 square feet of the complex would be devoted to a variety of dining options. The remaining 25,000 square feet in the complex would be dedicated to a recreational anchor (bowling, bocce, dining, etc.). Schedule G notes roughly a 2,500+/- seat theater based on the House of Blues or Fillmore Theater concept to host regional, national, and international musical acts. A space would serve as an ice rink in the winter and a performance lawn for cultural and musical events in the summer.

Highlights

The tables below highlight aspects of the NEC and MSG proposals. Included are summaries of proposed investment levels, comparisons of guaranteed revenue and general lease terms. Discussions of each section follow these tables.

NEC			MSG		
Arena Investment:	$ 67,498,653	Hard costs	**Arena Investment:**	$ 67,920,000	Hard costs
	$ 23,114,496	Soft costs		$ 5,795,000	Soft costs
	$ 7,905,590	Contigency		$ 17,285,000	Contingency
Arena Investment Total:	**$ 98,518,739**		**Arena Investment Total:**	**$ 91,000,000**	
Plaza Investment::	$ 69,206,600	Hard costs	**Plaza Investment:**	$ 70,000,000	Hard and Soft costs
	$ 25,527,485	Soft costs		$ 40,000,000	Interior and Leasing Fit Out
	$ 8,619,344	Contigency		$ 15,000,000	Contingency
	$ 27,165,000	Additional Tenant Fit-Out*	**Plaza Investment Total:**	**$125,000,000**	
Plaza Investment Total:	**$ 130,518,429**				
Total Investment:	**$ 229,037,168**		**Total Investment:**	**$216,000,000**	*
Capital Expenditures	NEC assumes all capital expenses.		Capital Expenditures	$34.0 million to cover capital expenses.	
Total After Captial Investment:	**$ 229,037,168**		**Total After Capital Investment:**	**$250,000,000**	
***To be paid by NEC's tenants at Plaza**			*** The breakdown of MSG's investment figures are based on KPMG's Report.**		

Minimum Guarantee by NEC			Minimum Guarantee by MSG		
Coliseum Revenue	$ 4,000,000	Annually	Coliseum Revenue	$ 3,000,000	Annually
	10%	Growth Percent		5%	Growth Percent
	5	Growth Period		5	Growth Period
Years 1-34	$ 194,522,894		Years 1-34	$ 112,109,840	
Years 35-49	$ 139,325,478		Years 35-49	$ 65,904,564	
Total Revenue Years 1-49	**$ 333,848,371**		**Total Revenue Years 1-49**	**$ 178,014,403**	
Plaza Base Revenue	$ 400,000	Annually	Plaza Guaranteed Total Sales Tax for first 5 Years.	$ 2,125,000	
**Grows with the same escalators above.					
Capital Expenditures	NEC Assumes All Capital Expenses.		Capital Expenditures	MSG assumes all capital expenses for first 30 years & not required after to make any capital investment if MSG deems it is not commercially viable.	
Fixed Seats	13,000		Fixed Seats	14,500	
Parking Spots	6,500		Parking Spots	4,900	
Term	34 year lease, 3 separate 5 year options		Term	40 year lease, 4 separate 5 year options	
Pre-Construction Revenue	$50,000/ Calendar Month		**Pre-Construction Revenue**	$1,500,000 One Time Payment Credited Against Next Payable Installment of Annual Rent	
Approvals (if any)	5% of gross coliseum revenue				
Construction- Coliseum	$90,000/ Calendar Month				
Construction- Plaza	$10,000/ Calendar Month				

Investment

NEC proposes an initial investment of $98.5 million for the Coliseum renovation and $130.5 for the Plaza improvement, while MSG proposes $91.0 million for the Coliseum and $125.0 million for the Plaza. MSG does budget an additional $34.0 million for any ongoing capital expenditures required during the term of the lease. PFM comments on MSG's additional $34.0 million, "if this money is held separately in escrow, there would be less credit and market risks as the funds would be readily available for capital expenditure without the need to acquire further financing sources. However both proposers have committed to assume full responsibility for capital expenditure during the lease term. Therefore we do not consider this amount as a separate or additional investment unique to MSG's proposal." NEC did not quantify a figure for capital expenses but assumes all expenditures for the term of the lease without condition.

After factoring in the capital expenditures, MSG's investment is roughly $250.0 million compared to NEC's investment of $229.0 million. The MSG contract does explicitly state that the actual costs may be greater or less than the estimated project cost. The NEC lease states that the investment can't be less than $229.0 million.

It would be possible for MSG to self-fund the project with cash and cash equivalent. According to the Administration, MSG expressed an interest in financing part of their proposals. NEC is planning to finance their investment with debt and debt equity. Per the KPMG report, Goldman Sachs expressed confidence NEC can achieve debt proceeds of $60.0 million; Guggenheim Partners issued a letter of support indicating interest to provide debt and equity financing up to $65.0 million and NEC partners will provide $32.0 million.

Fiscal Impact of Proposals

Revenue

In order to determine the fiscal impact, OLBR has reviewed the leases and compared the projections to the two consultants' reports prepared by Public Financial Management Inc. (PFM) and KPMG, LLP. Our results are very similar.

Under the NEC proposed lease, Nassau County will receive the greater of:

- A minimum of $4.0 million annually from the Coliseum or 8% of all gross revenue, 12.75% of parking revenue, plus $1.50 per ticket entertainment tax surcharge. The Coliseum minimum is subject to 10% escalators every five years. At the Plaza, NEC will pay the County a minimum of $400,000 annually, or 8% of all gross Plaza revenue. The Plaza minimum is also subject to 10% escalators every five years. The initial annual minimum guarantee is $4.4 million.

Under the MSG proposed lease, Nassau County will receive the greater of:

- A minimum of $3.0 million annually from the Coliseum, escalating every five years by 5% and no additional proceeds from the plaza; or revenues based on ticket sales plus $1.50 per ticket entertainment tax.

The chart below depicts the projected revenue from the Coliseum and the Plaza based on the minimum guarantee over the initial 34 year term of the lease and if the lease is extended to 49 years:

Projected Revenue Based on the Minimum Guarantee

NEC	Years 1-34	Through Year 49
Coliseum	177.1	303.7
Plaza	17.5	30.1
NEC Total:	**194.5**	**333.8**

MSG	Years 1-34	Through Year 49
Coliseum	112.1	178.0
Plaza	0.0	0.0
MSG Total:	**112.1**	**178.0**

As reflected above, the County is projected to collect $194.5 million over the 34 year term. If NEC chooses to renew the lease for the three additional five year periods, the projected revenue will be roughly $333.8 million in contrast to $178.0 million by MSG over the same period. The figures in the chart above include discounted annual revenues during the planning and construction period. Given the larger NEC escalation coupled with additional funds from the Plaza, the NEC lease is projected to generate greater cash flow to the County.

PFM performed an analysis to project the amount of revenue that would need to be generated by MSG to break-even with the NEC proposal. PFM made spending and attendance assumptions to compare the two proposals. Based on their scenario of 1.4 million ticket sales, MSG will generate $232.2 million in rental payments in comparison to NEC's $239.6 million over 49 years. The 1.4 million is an optimistic figure since it is greater than the historical average of Coliseum ticket sales. If the average attendance were lowered to less than 1.4 million, the revenue gap would widen further in NEC's favor. In addition, the revenues generated in this scenario are still less than the NEC minimum guarantee.

The revenue figures include the $1.50 entertainment surcharge tax on each ticket sold, which is imposed by Local Law 28-2000. In the event that the Entertainment Tax was to lapse or be discontinued, NEC has agreed to collect and remit to the County a payment in lieu of Entertainment Tax ("PILOET"). The PILOET is designed to protect the County in the event the Entertainment Tax is no longer in place. If the Entertainment Tax is no longer in place, NEC will collect and remit to the County an amount equal to the Entertainment Tax that existed immediately before it lapsed or was discontinued. The MSG proposal does not include a similar provision.

In addition, the County will also continue to collect revenue from sales tax. The County currently collects sales tax revenues from all events held at the Coliseum. OLBR estimates that the County has historically been collecting close to $2.0 – 3.0 million annually. At a minimum, it is fair to assume that similar revenue will be collected from the new lease. Furthermore, there is an opportunity to generate newfound sales tax revenue for the County from Plaza activities.

IDA Pilot

Both MSG and NEC indicate that they require Industrial Development Agency (IDA) assistance. According to the MSG proposal, they are seeking full exemption for the Coliseum and Plaza; whereas, the NEC lease seeks an exemption solely on the Coliseum. NEC seeks to negotiate a phased in real estate Payment in Lieu of Tax (PILOT) for the Plaza development. Based on conversations with the Administration, OLBR understands that the Plaza will end up on the tax roll once the PILOT expires. When the Plaza lands on the tax roll, the tax base would widen and the County could realize a revenue opportunity. If the PILOT is not granted, the project may not move forward.

Expenditures

Based on the proposed lease, NEC has agreed to accept all costs and responsibilities for operating, insuring, maintaining and providing utilities for the Coliseum. Under the current lease with SMG, the County is responsible for some repairs, maintenance and capital expenditures. With the NEC lease, the County will shed these costs as the tenant will assume that responsibility. This provision of the lease represents an opportunity to the County.

Under the County's current agreement with SMG and the Islanders, the County pays the electric and chilled & hot water and then is reimbursed by SMG / the Islanders for these expenses. This arrangement has long been a source of dispute resulting in deductions to revenue and numerous reconciliations. NEC's agreeing to accept all utility costs up front may allow for cleaner and more accurate accounting records.

Economic Benefits

NEC's plan to spend $229.0 million to redevelop the Coliseum site will have wider economic benefit for Nassau's economy. These benefits may be measured with the use of an economic input-output model. OLBR used U.S. Bureau of Economic Analysis RIMS II multipliers to quantify these benefits. The results of this model are shown in Table 1.

Table 1

Economic Impact of the Construction Spending Output and Earning			
Industry	**Increased Output**	**Increased Earnings**	**New Employment**
Agriculture, forestry, fishing, and hunting	256,480	18,320	$1.2
Utilities	2,253,360	164,880	2
Construction	184,024,400	41,439,840	924
Manufacturing	12,347,680	1,667,120	33
Wholesale trade	9,709,600	1,941,920	31
Retail trade	18,832,960	4,012,080	162
Transportation and warehousing	3,151,040	732,800	18
Information	7,914,240	677,840	11
Finance and insurance	11,028,640	1,832,000	26
Real estate and rental and leasing	15,388,800	916,000	35
Professional, scientific, and technical services	10,314,160	2,967,840	46
Management of companies and enterprises	1,630,480	146,560	1
Administrative and waste management services	4,964,720	1,209,120	43
Educational services	1,117,520	348,080	13
Health care and social assistance	9,434,800	2,949,520	72
Arts, entertainment, and recreation	1,062,560	311,440	14
Accommodation and food services	3,334,240	622,880	38
Other services	4,030,400	916,000	33
Labor earnings	-	36,640	3
Total	**$300,796,080**	**$62,910,880**	**1,505**
Sources: RIMS II Multipliers and US Bureau of Economic Analysis. Discounted by 20% to reflect instances outside Nassau County.			

It was found that introducing the investment discounted by 20% into the local economy will generate 1,505 jobs, $62.9 million in earnings and $300.8 million in output.

Risks and Concerns

- Each proposal would, in the Plaza, create an entertainment district with a variety of bars, restaurants, and other amusements. The increase in activity at the Plaza could translate into additional policing costs to the County. The Administration is of the opinion that the County will not experience an increase in policing costs for the Coliseum, as the County already maintains the areas outside the Coliseum on event and non-event days. Given the current Police staffing levels, it is a concern.

- According to the NEC lease, "the tenant shall have received binding commitments in form reasonably satisfactory to the tenant and landlord for all benefits required by the tenant and all financing deemed necessary." Some concerns were raised by the Legislature as to what may be deemed to the tenant as "reasonably satisfied." According to the County's outside counsel, this language is a standard business term in commercial real estate agreements and in the unlikely event NEC was unable to obtain satisfactory financing the determination as to whether such financing is reasonably satisfactory would be based on an objective reasonableness standard.

- According to the lease, if any of the approval conditions have not been met and the construction commencement date has not occurred before the second anniversary of the lease effective date (on which the County Executive executes the lease and following all necessary approvals), the County and tenant can both terminate the lease. However, in the event of a Force Majeure, the 2 year period may extend for the duration of the delay up to 5 years. This raised the concern that the potential inability to obtain financing by NEC would constitute an event of a Force Majeure.

  NEC has stated that they are confident that they will obtain the appropriate financing prior to the expiration of 2 years. To respond to the Legislature's concerns, NEC has provided a letter as commitment that if they are unable to obtain the necessary financing it will not constitute as an event of Force Majeure.

- At the August 16, 2013 press conference to unveil NEC's redevelopment plan, Bruce Ratner announced that the AHL's Bridgeport Sound Tigers would serve as the Coliseum's new anchor tenant.[1] The Sound Tigers are the Islanders' top affiliate, so the Nassau County market would be a natural fit for the team. Certain contractual and logistical hurdles must be negotiated first before the Sound Tigers can replace their parent club. According to Team President Howard Saffan, the Sound Tigers and their parent company Harbor Yard Sports and Entertainment have 8 years remaining on their lease at Webster Bank Arena[2].

Conclusion

With the looming expiration of the current SMG/Islanders lease, the County needs to make a decision which ultimately determines whether the site is redeveloped or not, while ensuring the best possible financial return to the County. To tackle this task, a selection committee, comprised of County employees, and advised by the County Executive's Business Advisory Council, was assembled by the Administration to review submitted proposals. Two financial consultants were hired to evaluate the soundness of each proposal and make their recommendation to the Administration. The law firm of Pannone Lopes Devereaux & West LLC served as the County's outside counsel on the procurement process and lease negotiations.

MSG's strengths are its ability to self-finance the project and its lengthy experience in sports and entertainment programming. MSG would have likely financed the project but does have the capability to self-fund it with cash and borrowing available under its existing revolving credit facility. NEC is planning to finance their investment with debt and equity.

Although NEC does include a financing contingency, they offer a percentage of all gross revenue and a higher minimum revenue guarantee to the County. By offering the County

[1] John Callegari, "Ratner touts winning Coliseum Plan," Long Island Business News, August 16, 2013.
[2]Michael Fornabaio, "Despite relocation speculation, Sound Tigers remain committed to Bridgeport," August 15, 2013.

protections and assurances its competitor would not, NEC surpasses MSG on nearly every other front. NEC assumes all expenses at the end of the SMG/Islanders lease, including all capital expenses for the life of the agreement. The County retains development rights over any excess land in the NEC proposal. MSG does not allow for such a provision in its proposal; MSG required control over all future development. NEC also proposes a steady stream of revenue for the Coliseum Plaza, whereas MSG does not. In addition, NEC seeks to negotiate a phased in PILOT for the Plaza development; the County's tax base would widen once the PILOT expires. If the entertainment tax were to expire, NEC has agreed to remit a PILOET to the County. Forest City Enterprises, NEC's parent company, has had great success at the Barclays Center. In its first year of operation, the Barclays Center was the nation's top selling venue.[3] Additionally, major sports and entertainment brands, such as the New York Yankees, the NHL, Live Nation, and NCAA Division I basketball institutions, have expressed great interest in NEC's plan for the Coliseum.

Risk and reward decisions are policy choices. Based on OLBR's review, it is apparent that NEC was chosen because it offers greater financial benefits that outweigh those offered by MSG in addition to other protections. Several challenges still lie ahead for NEC and the County such as securing an anchor tenant as well as Legislative, NIFA, and Town of Hempstead approvals.

cc: Tim Sullivan, Deputy County Executive
Gregory May, Director of Legislative Affairs
Chris Ostuni, Majority Counsel
Dan McCloy, Director of Law, Finance & Operations
David Gugerty, Minority Chief of Staff
Peter Clines, Minority Counsel
Aline Khatchadourian, Minority Finance Director

[3] Matthew J. Perlman and Larry McShane, "Barclays Center ranked No. 1 venue in U.S. in ticket sales, raking in $46.9 million in its first year," NY Daily News, July 23, 2013.