



Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873
Email: fiscal.bureau@legis.wisconsin.gov • Website: <http://legis.wisconsin.gov/lfb>

October 15, 2015

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Section 13.10 Request for Sale of State Land at Hill Farms and Badger Road in the City of Madison

REQUEST

The Department of Administration (DOA) is requesting Joint Finance Committee approval of the proposed sale of approximately 13.87 acres of underutilized land at the Hill Farms state office building site in the City of Madison to the Smith Gilbane Company for \$12,084,000. The state and Smith Gilbane would then enter in a development agreement to develop a replacement state office building and a parking ramp on the remaining seven acres at the Hill Farms site. The state would also enter into a purchase agreement with Smith Gilbane to purchase the replacement office facility and ramp on the remaining seven acres at the Hill Farms site. In addition, DOA requests the Committee's approval of the related sale of 4.35 acres of state-owned property at 801 W. Badger Road in the City of Madison for \$1,000,000. This property currently houses the state Department of Employee Trust Funds (ETF), which will be moving into the new Department of Transportation (DOT) Hill Farms development.

BACKGROUND

2013 Act 20 provided DOA and the Building Commission broad authority to sell state properties. The Act also specified that DOA or the Building Commission could not sell or lease state-owned property, unless such a transaction was approved by the Joint Committee on Finance. In addition, the Act requires DOA or the Commission to submit the following information to the Joint Finance Committee as part of any request for approval of a sale or lease: (a) the estimated value of the facility as determined by DOA and at least one qualified privately-owned assessor; (b) the full cost of retiring remaining debt for the facility; (c) a cost benefit analysis that considers the short-term and long-term costs and benefits to the state of selling or leasing the property; (d) the length and conditions of any proposed sale or lease between the state and a proposed purchaser or lessee; (e) the estimated budgetary impact for affected state agencies for at least the current and

following biennium; and (f) any other information requested by the Committee.

DOA or the Building Commission are first required to use the proceeds from the sale of state assets to retire any outstanding principal, interest, or premium due on debt used to finance the acquisition, construction, or improvement of the property. Under Act 20, after the outstanding debt and all other obligations related to property are met, the DOA or the Building Commission are required to use the remaining proceeds to pay principal and interest on other outstanding public debt. To the extent practical the DOA Secretary or the Building Commission are to consider all of the following in determining which public debt to redeem: (a) the extent to which the debt service on the property being sold or leased was paid from a segregated fund, other outstanding debt related to that fund should be redeemed; (b) the extent to which general obligation debt was issued to acquire, build, or improve the property is subject to current optional redemption, would require the establishment of an escrow, or could be assigned for accounting purposes to a statutory bond purpose; (c) the fiscal benefit of redeeming outstanding debt with higher interest costs; and (d) the costs of maintaining federal tax law compliance in the selection of general obligation debt to be redeemed.

JFC APPROVAL

2013 Act 20 also modified the 2007-09 state building program to increase the State Department of Transportation Building replacement project at the Hill Farms site in Madison by \$146,615,000 for a total project cost of \$196,615,000, to be entirely funded with program revenue-supported bonding. The program revenue debt service payments on the bonds would be made from DOA's space rental account, which receives revenues associated with rental charges from state agencies that are housed in general office facilities owned and operated by the state. Agency rental payments are generally made from agency funding sources in proportion to the percentage each funding source makes up of total agency operations funding. For example, rents paid by DOT to the space rental account are made from the segregated transportation fund, which funds all the Department's program operations.

The proposed 600,000 gross square foot state office building at Hill Farms and the adjacent parking facility would use approximately seven acres of the existing 20.75 acre Hill Farms site, and would house staff from the following seven state agencies.

<u>Tenant</u>	<u>Approximate Gross Square Feet</u>
DOT (Central Office)	340,000
ETF	80,000
Public Service Commission	35,000
Office of Commissioner of Insurance	55,000
Department of Financial Institutions	45,000
Wisconsin Economic Development Corporation	35,000
DOA (Division of Hearings and Appeals)	10,000

In October, 2014, DOA initiated a request for proposal process (RFP) to select a developer

for the replacement Hill Farms state office facility project. The RFP was issued for potential qualified development teams or joint ventures to:

- a. design and construct a turn-key, 600,000 gross square foot office building on state-owned land at the Hill Farms site;
- b. address the state's parking needs with a new parking structure and surface lots at the Hill Farms site;
- c. purchase the remaining underutilized land and the existing office building that will be vacated at the Hill Farms site; and
- d. purchase the Badger Road State Office Building that will be vacated as a result of this initiative.

DOA reviewed and scored five independent offers under the RFP process. On February 2, 2015, DOA issued a notice of intent to award a contract resulting from the RFP to Smith Gilbane. On July 20, 2015, a final agreement between DOA and Smith Gilbane was reached.

The Building Commission approved DOA's request to proceed with the project, including the proposed sale of the state land at the Hill Farms site and the Badger Road site in Madison at its August, 12, 2015, meeting. The request was approved on an 8-0 vote.

Estimated Value of the State Land

DOA hired an independent appraiser to complete a valuation report on each property in the City of Madison. The same appraiser also conducted an evaluation report for the both properties in 2014.

Hill Farms Site. At the Hill Farms property the evaluation looked at the Hill Farms Building A, the nine story DOT building, and Building B, the two story adjacent building and a connector, and the 20.95 acres of land. These buildings entail 377,661 square feet of gross building area. While the appraiser evaluation report indicates that while the existing buildings were well-maintained and capable of continuing operational functions, the majority of the facility is considered outdated by many. The appraisal attempted to derive a market value for the property that reflects the "as is" condition of the property. However, the appraiser indicated that the highest and best use would be to raze the existing facilities and redevelop the property. Therefore, the appraiser concluded that a buyer would likely base the acquisition of the property on the land value without any material contribution to the existing improvements.

Using a sales comparison approach, the appraiser reached an estimated market value of \$20 per square foot or \$18,250,000 (\$871,121 per acre) for the 20.95 acre site. Based on the selected developer's proposal, 13.87 acres would not be needed for the DOT replacement building and parking structure. Therefore, using the same \$20 per square foot appraised value amount, the sale of 13.87 acres would result in an estimated value of \$12,083,544, which equals the sale amount for this property included in the DOA request.

Smith Gilbane's offer included the highest amount of land at Hill Farms to be sold (13.87 acres) among the five offers reviewed under the RFP process. Despite Smith Gilbane's offer to purchase the Hill Farms property for \$8,537,760, or \$615,556 per acre, DOA indicates that negotiations with the developer resulted in a total purchase price of \$12,084,000 for 13.87 acres. This purchase price, which is contained in the development agreement essentially equals the appraised value on the property.

Badger Road Site. The same appraiser completed a valuation report for the state's Badger Road property using a sales comparison approach. Based on this analysis, the appraiser found the fair market value of the property to reasonably estimated at \$2,845,000.

The five offers included in the RFP process included purchase prices for the Badger Road property ranging from \$500,000 to \$1,000,000, which are well below the appraised value of the property. Smith Gilbane's purchase price offer was at \$522,700. After their selection, DOA indicates that through negotiations Smith Gilbane increased its purchase price to \$1,000,000, which is the purchase price for the property included in the development agreement with DOA, as well as in the request before the Committee.

Full Cost of Retiring Remaining Debt for the Facilities

DOA indicates that the \$2,054,000 is still owed on the Hill Farms and Badger Road properties. DOA indicates that the remaining proceeds after this debt is retired would be used to reduce the amount of debt issued to purchase the new Hill Farms state office facility and parking structure from the project developer, rather than to retire other outstanding debt obligations of the state.

Cost-Benefit Analysis

In carrying out the Act 20 authority relating to the sale of state assets, in March, 2014, DOA, using a competitive selection process, contracted with Robert W. Baird and Co. (Baird) to be its financial consultant to review, assess, and consider the sale, lease, or other disposition of certain state-owned assets and the impact on public debt of the state. Baird conducted a cost-benefit analysis on the long-term impact to the state of two separate alternatives: (a) the proposed sale of the Hill Farms and Badger Road land in the City of Madison and developing a state office facility and an adjacent parking structure on the remaining seven acres of land at the Hill Farms site; or (b) retaining the 50-year old DOT building structures at Hill Farms as well as the Badger Road office facility and addressing the critical maintenance needs at the two sites, and then replacing the DOT facility in 2035 when that facility would be 70 years old. Baird's cost-benefit analysis is not specific to the land being sold under DOA's request in that it primarily analyzes the DOT replacement structure and an alternative to that structure. However, the sale of the land is dependent on that Hill Farms development project taking place and the property sales are included in the analysis.

The cost-benefit analysis looked at the 50-year cost to the state under the two alternatives. Under both alternatives, the analysis looks at the 50-year rental revenues to be assessed by DOA and deposited to the state's space rental account under each alternative. Those revenues would be

used to retire the debt associated with each alternative and to maintain and operate each facility being analyzed. Therefore, the consultant's analysis also compares the costs that would be incurred by the state to develop, maintain, and operate the proposed Hill Farms state office facility with those same costs under an alternative scenario whereby the state occupies the existing DOT facility for 20 years and then has to replace the DOT facility.

The cost-benefit analysis essentially reviewed the impact of the two alternative on the state's space rental account, where revenues to the account are rents paid by state agencies and monthly parking charges paid by state agency staff. The costs paid from that account are annual debt service payments on bonds issued under each alternative as well as the costs to clean, maintain, and operate the facilities.

The consultant's analysis indicates that the primary costs associated with the proposed Hill Farms state office facility includes the costs to retire the \$179.3 million in bonds issued to finance the development of the facility and parking garage. Similarly, the primary costs associated with the alternative scenario, whereby the state continues to occupy the existing DOT facility and then replaces that facility in 2035, are the costs related to: (a) retiring the estimated \$34.1 million in bonding assumed to be issued in 2015 and needed to make immediate, necessary improvements to the existing facility; and (b) retiring the estimated \$400.7 million in bonding the analysis indicates would be needed for the eventual development of a new state office facility at Hill Farms in 2035.

Under the analysis, two primary differences between the two sites are identified. Under the alternative to the proposed Hill Farms state office facility, the costs of replacing the DOT office facility in 2035 would inflate to an estimated net cost, after the sale of lands, of \$400.7 million, compared to the \$179.3 million in estimated costs for the facility in 2015 under the proposed site. Secondly, one of the primary difference in revenues between two alternatives involves the difference in parking revenue at the Hill Farms site under each alternative. The analysis projects that the new Hill Farms state office facility would have 1,700 stalls, with parking tenants paying a monthly rate of \$100 per stall for total annual revenue of \$2,040,000. Comparatively, it is projected that the existing DOT facility surface lot structure would generate only around \$50,000 per year in the early years of the analysis and would grow to only \$116,000 by 2035, the year in which the existing facility is to be replaced under that alternative.

Overall, over the 50-year period, the consultant's analysis indicates that the proposed Hill Farms state office facility development would generate sufficient rents to cover annual debt service costs on bonds issued for the facility. The analysis also indicates that the development would have a higher benefit to the state than the alternative scenario whereby the state remains in the existing DOT facility for 20 years and then replaces that facility.

Conditions of the Proposed Sale

No specific conditions are placed on the state or the developer as part of the proposed sale of state lands at the Hill Farms and Badger Road sites. However, as mentioned earlier, Smith Gilbane, Inc., the project developer, would be subject to the requirements outlined in DOA's RFP, which were factored into the developer's bid to develop a replacement state office facility and parking garage at the Hill Farms site. DOA and the developer would enter into a developers

agreement and a purchase agreement for the purchase of the state office facility and parking structure at Hill Farms. In addition, these agreements would stipulate that the existing DOT building be demolished within a specified time after the new facility is completed and that the new parking structure be built within a specified period as stipulated in an agreement with the developer.

Budgetary Impact for Affected State Agencies

In reviewing the budgetary impact on affected state agencies, DOA and the consultant analyzed the annual impact on the each agency's rent costs. The attachment compares the annual and total rents to be charged the seven state agencies under the proposed Hill Farms state office facility and the rents paid by those agencies at their existing sites. As shown in the attachment, the proposed Hill Farms state office facility would involve a more efficient use of space by several state agencies, which would reduce the net square footage needed for several of agencies involved, including DOT. As a result, total net square footage (compared to 600,000 in gross square footage) among all state agencies would be reduced by 54,274 square feet. As a result, the total annual cost of rented space under the proposed Hill Farms project would be reduced by an estimated \$604,844 compared to the prospective tenant agencies' existing sites.

In addition, the DOA analysis indicates that the proposed Hill Farms state office facility would provide heating, ventilation and air conditioning, and other operational savings totaling over \$1 million per year compared to the existing facility.

If the Committee approves the proposed sale of the state lands at the Hill Farms and Badger Road sites in Madison, the development of the Hill Farms state office facility would move forward using the funding provided in the 2013-15 budget.

If the Committee does not approve the proposed sale of state lands related to the Hill Farms project, the development of the Hill Farms state office facility, as well as the private development on the remainder of the site, would not be able to move forward at this time. Consequently, the bonding authorized for the project, to be paid back with rents from agencies occupying all state general office facilities, would not be issued until it is resolved as to how DOA will proceed with the existing, or planned, Hill Farms state office facility. However, DOA indicates that if the Hill Farms project is not approved, the Department may have to consider requesting \$35 million in bonding to carry out needed critical improvements to the existing 50-year old building, including needed heating, ventilation and air conditioning work.

The Department also notes that if the requested land sales are not approved, it is unlikely the Department could move ahead with the existing developer on a more narrowly scoped project to just develop a replacement facility on the site. The RFP specifically requested that each bidder incorporate in their offers the purchase from the state of underutilized land at the existing Hill Farms that is not needed for their development proposal, as well as the purchase of land at the Badger Road site. Therefore, DOA indicates that the Department would not be able to legally move forward on the just the Hill Farms state office facility portion of Smith Gilbane's offer. Further, given that these land purchases, and the private development of those lands were to be incorporated in the RFP offers, as well as the work completed with the City of Madison on the

potential development, it is unclear whether Smith Gilbane would be willing to move forward with just the state office facility portion of their offer and not the private development portion. Therefore, DOA would have to start over with the RFP process that would narrow the scope of the development to just a new state office facility at the Hill Farms site. Finally, any delay in the eventual construction of the state office facility would likely result in a higher cost for the development of a state office facility.

In relation to the existing project plan, DOA indicates that the existing project development plan would have the developer completing project site work later this year, as well as some preliminary work related to the parking facility, which is to be constructed in advance of the state office facility. Failure to gain Committee approval for the land sale portion of the development would likely mean that this work would not get completed until the spring of 2016, which would delay the project delivery.

ALTERNATIVES

1. Approve DOA's request to sell 13.87 acres of state land at the Hill Farms site in the City of Madison for \$12,084,000 and 4.35 acres of state land at 801 W. Badger Road in the City of Madison for \$1,000,000.
2. Deny the request.

Prepared by: Al Runde
Attachment

ATTACHMENT

Comparison of Square Footage and Costs of Proposed Hill Farms State Office Facility and the Existing Agency Sites

<u>Agency</u>	<u>Net Square Feet</u>	<u>Rent/ Sq.Ft.</u>	<u>Annual Rent</u>
Proposed Hill Farms Facility			
Department of Transportation	241,227	\$24.98	\$6,025,840
Employee Trust Funds	68,763	24.98	1,717,696
Public Service Commission	28,600	24.98	714,428
Office of the Commissioner of Insurance	51,693	24.98	1,291,303
Department of Financial Institutions	29,215	24.98	729,803
Wisconsin Economic Development Corporation	27,829	24.98	695,169
Department of Administration	<u>18,373</u>	24.98	<u>458,946</u>
 Total	 465,700		 \$11,633,185
 Existing Agency Sites			
Department of Transportation	287,519	\$24.98	\$7,182,225
Employee Trust Funds	71,731	24.98	1,791,800
Public Service Commission	41,689	17.82	742,912
Office of the Commissioner of Insurance	46,024	24.98	1,149,680
Department of Financial Institutions	32,510	18.70	607,825
Wisconsin Economic Development Corporation	23,446	18.70	438,328
Department of Administration			
Hill Farms and Badger Rd	4,925	24.98	123,027
5005 University Ave	<u>12,130</u>	16.67	<u>202,232</u>
 Total	 519,974		 \$12,238,029
 Difference in Rent and Rental Costs			
Department of Transportation	-46,292	\$0.00	-\$1,156,384
Employee Trust Funds	-2,968	0.00	-74,144
Public Service Commission	-13,089	7.16	-28,484
Office of the Commissioner of Insurance	5,669	0.00	141,623
Department of Financial Institutions	-3,295	6.28	121,978
Wisconsin Economic Development Corporation	4,383	6.28	256,841
Department of Administration	<u>1,318</u>	5.91*	<u>133,687</u>
 Total Rental Costs	 -54,274		 -\$604,844

*Average change in rental rate for two existing sites.