Brinn Consulting, 9 Birch Knolls, Cape Elizabeth, Me. 04107 712-8237

Mr. Thomas Hall
Scarborough Town Manager
259 US Route One
Scarborough Me 04074

October 26, 2018

Dear Mr. Hall;

As you requested, I have reviewed the Financial Analysis completed by Karen Martin of SEDCO which compares two Development Scenarios regarding the Scarborough Downs site in Scarborough, Maine.
My assignment is summarized as follows:

A). To meet with Karen Martin of SEDCO and thoroughly review their financial analysis focusing on the methodology employed and the consistency of assumptions between the two scenarios. Scenario One, which assumes a town partnership with Crossroads Holdings, LLC and the creation of a Credit Enhancement Agreement (CEA) has more aggressive and quicker to fruition growth assumptions than Scenario 2, which assumes that Crossroads Holdings, LLC develops the property without the Town as a partner, with a slower to build and less significant footprint.

B). To evaluate the results and determine if they follow logically from sound methodology and assumptions, and are based on a true incremental analysis. Please note that all growth assumptions were provided by the developer to SEDCO.

C). To complete an Executive Opinion Letter which summarizes the results of A&B above.

This letter as outlined below, represents Step C above.

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Background

My focus in this evaluation was to look at the methodology and resulting conclusions of the financial analysis, which was done on an annual basis for all 30 years of the project for both Scenario 1 and 2.

Because Scenario 2 can be considered the Status Quo, ie; what happens at the Scarborough Downs site without the Town being an active partner, the analysis completed compares Scenario 2 to Scenario 1 on an incremental basis. It determines the impact of the Town becoming a partner in the development and creating the CEA, which enables the developer to share in the increased revenue that accrues to the town from the larger and more rapid development in Scenario 1.

The CEA caps this sharing amount at $55 million plus a potential bonus of $26 million capped at $2 million per year starting in year 17, which means that of the assumed increase in incremental revenue to the town in Scenario 1 of $229 million dollars over the 30 year life of the project, that the town will forego $55-$81 million of the $229 million and provide it to the developer(if the developer achieves certain agreed upon milestones) to help reimburse costs of development including infrastructure costs borne by the developer. In both scenarios, there is no assumed Capital outlay by the Town, as all capital costs are the responsibility of the developer. It is also assumed that current and future impact fees will cover the cost of any future infrastructure needs caused specifically by this development that was not already being paid for by the developer directly. Evaluating impact fees was beyond the scope of my assignment.

- The Financial Analysis was done two ways for both Scenarios. First it was done with un-inflated revenues and costs meaning on the revenue side that property tax rates do not change, that revaluations do not occur, and that there is no inflation to revenue from excise taxes; and on the expense side meaning that there is no increase in the costs of services that the town provides due to inflation. Conversely, it was also evaluated assuming that both costs and revenues will experience inflation, with annual cost inflation of 2.7% (based on the American City and County's Municipal Cost index July 1988 to July 2018), and with a property tax rate increase of 3% annually, property tax valuation increases of 20% every ten years, and excise tax increases of 3% per year. Again, both scenarios were treated the same way in regard to these assumptions.

- Both Scenarios result in a positive result for the town if the growth assumptions from the developers are enacted, with Scenario 1 resulting in $346 million in net revenues (after expenses are subtracted but before subtracting the $55 million that the CEA would provide the developer) and Scenario 2 resulting in $117 million in net revenues (after expenses are subtracted.) It is worth noting that the $346 million in Scenario 1 and the $117 million in Scenario 2 are provided in future dollars, and would be considerably less in today's dollars if a discount rate were applied.

Findings

- Based on my discussions with Karen Martin and the review of her analysis, the analysis is very thorough in its methodology, its focus to detailed assumptions and the scope of its inclusion of costs that will impact the Town. I believe the work done represents an accurate projection of the revenues and costs associated with both scenarios being considered by the Town and the results presented are based on appropriate methodology and assumptions.

- Because the Town has no capital outlay assumed nor any ownership in the proposed development, it is appropriate that the Financial Analysis excludes a Net Present Value component. That methodology would be more appropriate for the developer to undertake, as they will have a large capital outlay and maintain ownership of the assets in many cases.

- Regardless of the way costs and revenues were considered (in 2018 dollars or in inflated dollars) the results are favorable for both scenarios. The results improve dramatically in both Scenarios when costs and revenues are projected to increase over time and the resulting ratio of incremental costs to revenues drops from 58% in Scenario 1, when costs and revenues are in constant 2018 dollars, to 40% when the increases in costs and revenues noted above, are in effect. It seems appropriate to include the assumptions that costs will grow over time as well as revenues due to revaluations and tax rate increases.

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Suggestions and Considerations

- While the hundreds of assumptions that went into the analysis appear to be well reasoned and extremely well researched and I have no reason to think they are anything but accurate, my expertise is not in municipal costs and the impact development has on them. It would be prudent of the town to also have an outside person with demonstrated expertise in municipal and school department costs and revenues, review the assumptions made in regard to incremental cost impacts for town services such as police, fire, public works, school, public safety, library, etc, caused by the scope of development assumed to occur in both scenarios.

  Because the analysis is done incrementally comparing one scenario to another, and because the assumptions are consistent between the two scenarios, the impact of changing a cost assumption won't dramatically impact the difference in results between the two scenarios. Nonetheless, it would be useful to have a municipal financial expert focus in on the incremental cost aspects of doing either scenario

- It is also worth noting that the build out timelines provided by the developer vary by ten years, with Scenario 1 becoming 100% developed in 20 years with a total of 1986 housing units of diverse types, along with 1,156,000 sq feet of office/retail, 775,000 sq ft of manufacturing, and an assumed increase of 350 students within the school district.
  On the other hand, Scenario 2 is assumed to take 30 years to become 100% developed and it includes a total of 1077 housing units, the majority of which are single family units, and also includes 300,000 sq ft of office/retail, 400,000 sq ft of Manufacturing, and assumes the addition of 305 new students within the school district.
  If Scenario 2 occurred on the same timeline as Scenario 1 it would generate additional revenue and costs. The assumption underlying Scenario 1 is that the CEA will accelerate development.

This time horizon difference lessens the revenue that Scenario 2 results in compared to Scenario 1 particularly when costs and revenues are inflated. As an example, in Year 19 with both costs and revenues inflated, the spread between revenues and costs is approx $9.2 million in favor of Scenario 1. In year 20, when the 20% revaluation kicks in, the spread grows to approx $12 million mainly because all the development build out is in place in Scenario 1, but only 60% of the non residential development is in place in Scenario 2 by year 20 and only 69% of the residential development is in place by year 20.

- Additionally, in both scenarios, a significant amount of the cumulative net revenue increase over and above costs, occurs from year 20 onward. In Scenario 1, this amounts to $218 million of the $346.7 million or 62.9%, and in Scenario 2, this amounts to $91 million of $117 million, or 77.8%. Because risk increases as time goes on, and assumptions are less likely to be accurate, the Town should be aware that a significant amount of the benefit the analysis results in occurs in the years 20 to 30.

- There are assumptions regarding incremental new students and incremental new cars attributed to the development of Scarborough Downs which do not appear to take into account that a portion of the students and cars due to the project development will result from existing Scarborough residents.
  In the case of students, this assumption overstates costs and in the case of cars, it overstates revenues. But it does so in both scenarios to a similar extent and impact.

- However another assumption relating to the number of incremental new students may understate the Scenario 2 costs as there are assumed to be 45 fewer students in the development in Scenario 2 compared to Scenario 1. While that may be true based upon the ratios of students per HH and is appropriately based upon the type of housing units constructed, if there is demand in town for the amount of housing units assumed in Scenario 1, they will probably get built elsewhere in town, if not built as part of scenario 2, resulting in the same number of new students (350) in either scenario, practically speaking.

In either case, it appears that the number of incremental 350 new students assumed to move into Scarborough can be absorbed within the current system wide physical structure of the school department based upon the Classroom Capacity Analysis completed by SEDCO, which shows additional capacity for 669 students in K-12.

Conclusions

My review of the Financial Analysis completed by SEDCO indicates that the methodology employed was appropriate and that the assumptions utilized were consistently applied to both Scenarios. The version of both Scenarios that assumes that costs increase over time and that revenues will also increase due to revaluations and tax rate increases, appears to be the more realistic of the two versions I reviewed, and also results in the higher incremental increase in revenues versus costs over time. Scenario 1, which assumes the CEA, results in considerably higher net revenues (after costs and reimbursement to the developers) than does Scenario 2, but both Scenarios have favorable results.

With the suggestions noted in the section above, I believe the work done represents an accurate projection of the revenues and costs associated with both Scenarios being considered by the Town and the results presented are based on appropriate methodology and assumptions.