

City of San José

*Financial Feasibility Study
of the
Ice Centre Expansion Project*

*City Council Meeting
December 10, 2019
Item 4.2*

Presenters:

Julia Cooper, Director of Finance

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Background

Ice Centre – Current Facility

- Constructed 1994 with three project expansions
- Four sheets of ice; approximately 177,000 square feet

Ice Centre – Proposed Expansion

- Two additional sheets of ice; 200,000 square feet; 2 years to complete
- One ice sheet will be a competition rink for the San Jose Barracuda
- Medical Office Space (20,000 square feet for lease by Sharks)

Feasibility Study

Requirement of City's Debt Policy

- City debt financing paid solely from Project Revenues requires:
 - Feasibility Study to determine revenue volatility; sensitivity analysis; worst/best case scenarios; and impact(s) on repayment source(s) identified as backstop to project revenues; and
 - Two-thirds Council approval to proceed with project financing

Feasibility Consultant Procurement

- RFP issued in December 2018
- January 2019 - Six responses received
- February 2019 – City selects Strategic Venue Studies/Sports Synergy as the Feasibility Consultant
- Sharks Ice, LLC providing funding for contract



Financial Feasibility Report

Solar4America Ice Centre Expansion San José, California

Strategic Venue Studies
and
Sport Synergy, LLC

December 10, 2019

Study Methodology

Market Analysis

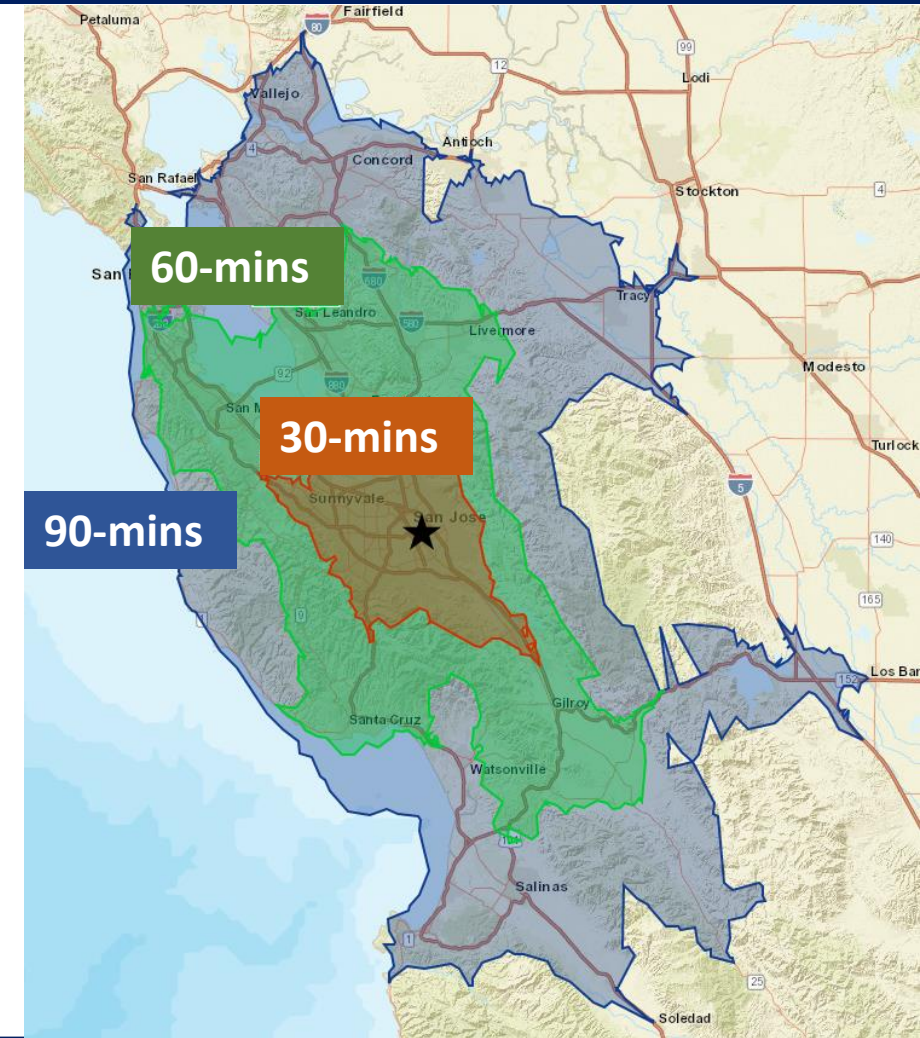
- Field Work/ Interviews
- Market Analysis
- Participation Trends
- Competitive/Peer Venue Analysis

Feasibility Analysis

- Historical Operations Review
- Plan Review
- Operating Projections
- Recession Scenarios & Project Risks

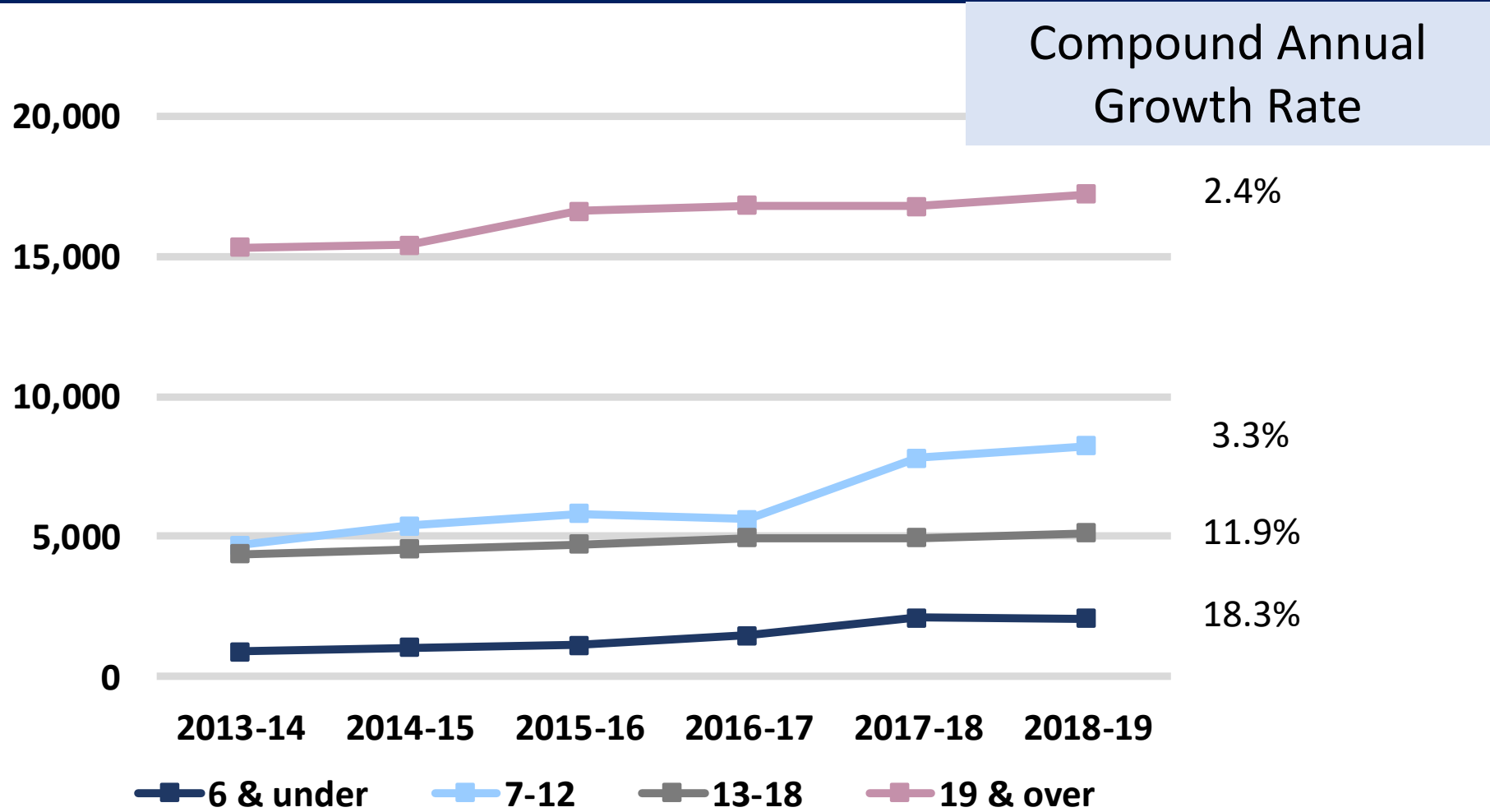
Market Demographics

- Large population base
- Well-educated and affluent
- Low unemployment
- Diversified corporate base
- Spending on recreation and sports is 1.5 to 2 times the national average



Participation Trends

California
Ice Hockey
Participation



Competitive Venues

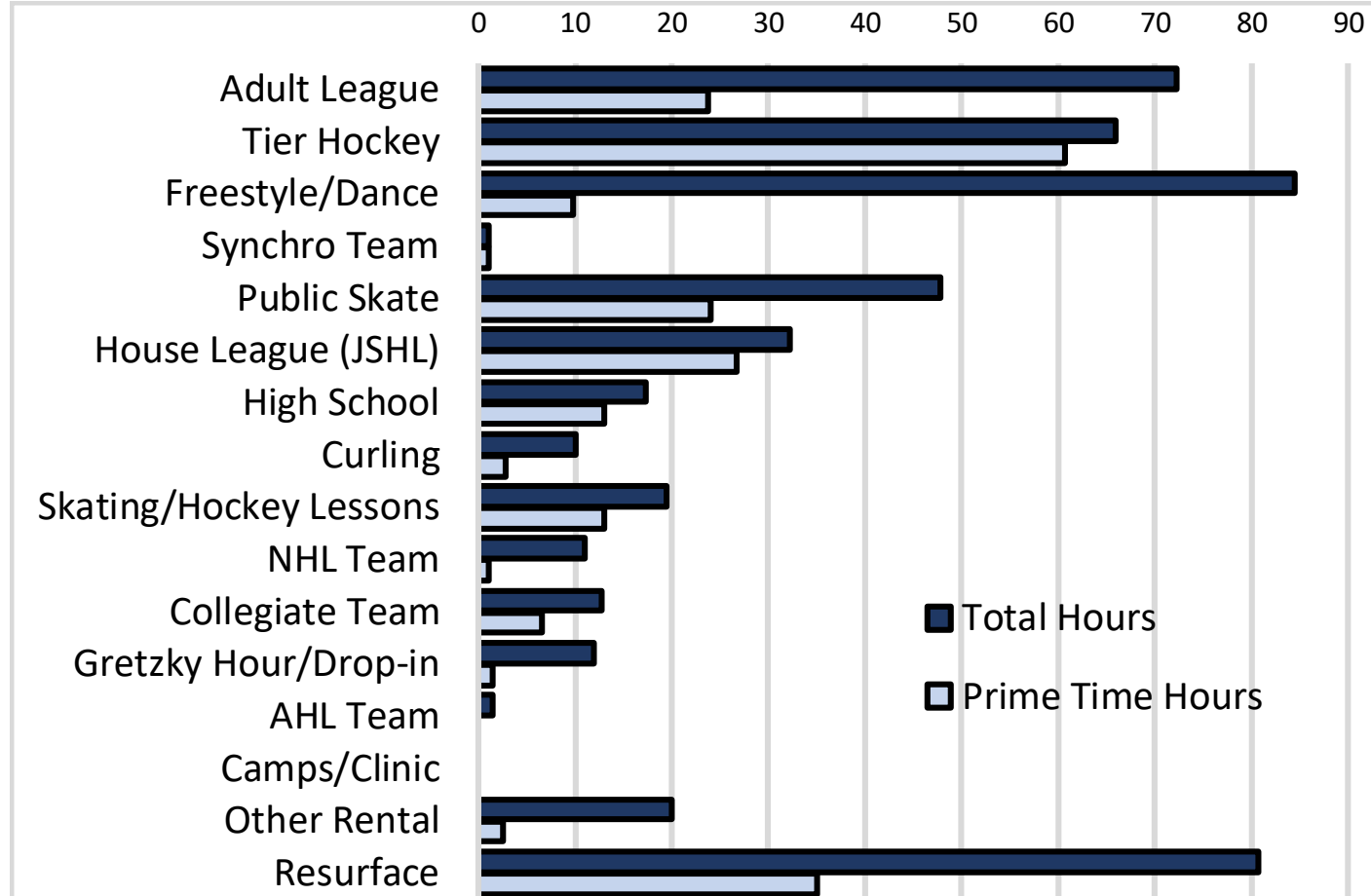
Venue	City	Rinks
Solar 4 America Ice Centre *	San Jose	4
Oakland Ice Center *	Oakland	2
Vacaville Ice Sports	Vacaville	2
Tri-Valley Ice	Livermore	2
Ice Center at Cupertino	Cupertino	1
Dublin Iceland	Dublin	1
Solar4America Fremont *	Fremont	1
Gateway Ice Center	Fresno	1
Winter Lodge **	Palo Alto	1
Nazareth Redwood City	Redwood City	1
Skatetown Roseville	Roseville	1
Sacramento Iceland **	Sacramento	1
Yerba Buena Ice Skating Center	San Francisco	1
Nazareth San Mateo	San Mateo	1
Redwood Empire Ice Arena	Santa Rosa	1
South Lake Tahoe Ice Arena	South Lake Tahoe	1
Oak Park Skating Arena	Stockton	1

* Operated by Sharks Ice ** Outdoor Venue (winter use)

- The Bay Area has the highest concentration of rinks in California.
- Compared to other states with an NHL team, CA has significantly lower rink to population ratio.

Historical Ice Centre Use

Typical Winter Week



Occupancy Rate: 84-88%

Prime Time Ice:
Weekdays 4:00pm to 10:00pm

Expanded Use Projections (hours)

	Expansion Projected		Historical	
Facility Hockey Programs	12,499	40.7%	6,280	31.6%
Classes & Lessons	2,581	8.4%	1,436	7.2%
General Admission	7,898	25.7%	7,268	36.6%
Tier/Travel Hockey	3,441	11.2%	2,651	13.4%
Contracted Ice & Events	4,316	14.0%	2,211	11.1%
ANNUAL TOTAL HOURS	30,734	100.0%	19,845	100.0%

Financial Operations

Operating Revenues

Hockey Programs
Classes & Lessons
General Admission
Facility Rental
Contracted Ice
Tier 1 & Travel Hockey
Sponsorships
Food & Beverage Sales
Merchandise Sales
AHL Net Income
Miscellaneous Income

Operating Expenses

Hockey Programs
Classes & Lessons
General Admission
Facility Rental
Contracted Ice
Tier 1 & Travel Hockey
Sales & Marketing
Food & Beverage
Merchandise Sales
Administration
Building Operations
Utilities
Engineering

Financial Operations

Non-Operating Revenues

Leases and Long-Term
Contracts
Incremental Naming Rights

Indirect Expenses

Parking Access Fee
Other Related Payments
Possessory Interest Fee

Expected Case Projection (in 000s)

Fiscal Year	Stabilization Period				Stabilized Operations
	2022	2023	2024	2025	2026
OPERATING REVENUE					
Total Operating Revenue	\$17,200	\$23,493	\$24,626	\$25,702	\$26,888
OPERATING EXPENSES					
Total Operating Expenses	\$10,842	\$13,745	\$14,317	\$14,800	\$15,353
OPERATING INCOME (LOSS)	\$6,357	\$9,748	\$10,309	\$10,902	\$11,535
NON-OPERATING REVENUE					
Total Non-Operating Revenue	\$1,047	\$3,260	\$3,349	\$3,440	\$3,535
INDIRECT EXPENSE					
Parking Access Fee	\$50	\$151	\$152	\$153	\$154
Other Related Payments	100	103	106	109	113
Possessory Interest Fee	561	571	581	591	601
Total Indirect Expense	\$711	\$825	\$839	\$853	\$868
NET INCOME AVAILABLE FOR LEASE PAYMENTS	\$6,694	\$12,183	\$12,819	\$13,489	\$14,202

Conservative Projection (in 000s)

Fiscal Year	Stabilization Period				Stabilized Operations
	2022	2023	2024	2025	2026
OPERATING REVENUE					
Total Operating Revenue	\$16,026	\$21,637	\$22,670	\$23,676	\$24,782
OPERATING EXPENSES					
Total Operating Expenses	\$9,830	\$12,799	\$13,314	\$13,771	\$14,290
OPERATING INCOME (LOSS)	\$6,196	\$8,838	\$9,356	\$9,905	\$10,492
NON-OPERATING REVENUE					
Total Non-Operating Revenue	\$1,047	\$3,260	\$3,349	\$3,440	\$3,535
INDIRECT EXPENSE					
Total Indirect Expense	\$711	\$825	\$839	\$853	\$868
NET INCOME AVAILABLE FOR LEASE PAYMENTS	\$6,533	\$11,273	\$11,866	\$12,492	\$13,159

Aggressive Projection (in 000s)

Fiscal Year	Stabilization Period				Stabilized Operations
	2022	2023	2024	2025	2026
OPERATING REVENUE					
Total Operating Revenue	\$18,742	\$26,090	\$27,364	\$28,547	\$29,849
OPERATING EXPENSES					
Total Operating Expenses	\$11,304	\$14,917	\$15,567	\$16,091	\$16,689
OPERATING INCOME (LOSS)	\$7,438	\$11,173	\$11,798	\$12,457	\$13,159
NON-OPERATING REVENUE					
Total Non-Operating Revenue	\$1,047	\$3,260	\$3,349	\$3,440	\$3,535
INDIRECT EXPENSE					
Total Indirect Expense	\$711	\$825	\$839	\$853	\$868
NET INCOME AVAILABLE FOR LEASE PAYMENTS	\$7,775	\$13,608	\$14,308	\$15,044	\$15,826

Net Income Scenarios - 2026

Based on Expected Operation

	Stabilized Operations			Recession Scenarios		
	Expected	Conservative	Aggressive	10% Rev Decline	20% Rev Decline	30% Rev Decline
OPERATING REVENUE						
Total Operating Revenue	\$26,888	\$24,782	\$29,849	\$24,199	\$21,510	\$18,822
OPERATING EXPENSES						
Total Operating Expenses	\$15,353	\$14,290	\$16,689	\$14,098	\$12,843	\$11,588
OPERATING INCOME (LOSS)	\$11,535	\$10,492	\$13,159	\$10,101	\$8,668	\$7,234
NON-OPERATING REVENUE						
Total Non-Operating Revenue ¹	\$3,535	\$3,535	\$3,535	\$3,535	\$3,535	\$3,535
INDIRECT EXPENSE						
Total Indirect Expense ¹	\$868	\$868	\$868	\$868	\$868	\$868
NET INCOME AVAILABLE FOR LEASE PAYMENTS	\$14,202	\$13,159	\$15,826	\$12,768	\$11,335	\$9,901

¹ Long-term contracts, such as leases and naming rights agreements and indirect expenses would not be impacted by short-term economic downturn

Operating Challenges & Risks

Challenges

- As a national competitor, ice rental rates are high compared to other markets
- High market hotel rates
- Relatively small seating capacity for AHL arena

Risks

- Multiple renewals of third-party contracts over the term of the agreement
- Reduced enthusiasm for the sports of ice hockey due to removal of team(s) or league-related stoppage (strike, lockout)

Conclusions

- The market analysis indicates there is unaccommodated demand for ice time from multiple sources.
- Increased ice supply will allow expanded use by the facility hockey programs and contracted ice that earn the greatest revenue per hour of ice use.
- The ability to utilize the established ice operation and incrementally expanded ice programming benefits from economies of scale.
- With the addition of AHL income, 57% of the projected operating income can be attributed to the addition of 2 new ice sheets.

Ability to Support Debt Service Payments

- Annual Debt Service Payments estimated at approximately \$8 million per year after 2 year construction period and 3-year “ramp up” period
- Conservative Scenario assumes \$10.5 million per year in operating income at beginning of stabilization period (FY 2026) producing debt service coverage of 1.33 x

<u>Scenario</u>	<u>FY 2022</u>	<u>FY 2023</u>	<u>FY 2024</u>	<u>FY 2025</u>	<u>FY 2026</u>
Conservative	\$6.196	\$8.838	\$9.356	\$9.905	\$10.492
<i>Debt Service Coverage</i>	n/a	1.26	1.25	1.25	1.33
Expected	\$6.357	\$9.748	\$10.309	\$10.902	\$11.535
<i>Debt Service Coverage</i>	n/a	1.39	1.38	1.38	1.46
Aggressive	\$7.438	\$11.173	\$11.798	\$12.457	\$13.159
<i>Debt Service Coverage</i>	n/a	1.60	1.57	1.58	1.66

Proposed Bond Financing Structure

- Taxable Lease Revenue Bonds issued by City of San Jose Financing Authority

Projected Use of Bond Proceeds (Series 2020 Bonds)

Construction Fund Deposit ¹	\$112,100,000
Refund CSJFA Series 2008E Bonds	13,050,000
Liquidation of Series 2008 Debt Service Reserve	(2,840,000)
Bond Issuance Cost	1,710,000
Capitalized Interest	10,900,000
Debt Service Reserve – Series 2020 Bonds	8,680,000
Total	<hr/> \$143,600,000

¹ \$1.9 million in interest earnings assumed during construction period for \$114.0 million available for project construction costs

Key Business Terms – Amended/Restated Lease and Management Agreement

- **Term**

- Initial period of 30 years to coincide with the issuance of 2020 bonds with option to extend up to an additional 25 years; for a total maximum Term of 55 years

- **Rent**

- Reduced Base Rent during construction period for FY 2020-21 and FY 2021-22
- Base Rent during FY 2022-23; FY 2023-24; and FY 2024-25 will reflect gradual increased payments through the stabilization period (ramp up)
- Base Rent, beginning in FY 2025-26, after the stabilization period, will be flat until bonds are fully amortized and set at City borrowing costs plus 50 basis points (1/2%)

Key Business Terms – Amended/Restated Lease and Management Agreement

▪ Capital Reserves

- Sharks Ice responsible for making all Capital Repairs and Replacements
- Capital Reserve established in the Ice Centre Revenue Fund (Fund 432) to be used solely as a source of funds to pay for any Extraordinary Repair Work or uninsured casualty loss
- Capital Reserve is funded by excess base rent payments above the amounts required for annual debt service and City administrative expenses
- Capital Reserve will receive an estimated \$21 million over the 30-year term

▪ Substitutions

In the event that either the Barracuda or San Jose Sharks would relocate to another venue, Sharks Ice, LLC would continue to pay all amounts due under their sub-lease until an acceptable substitute subtenant was found

Key Business Terms – Amended/Restated Lease and Management Agreement

▪ Letter of Credit (LOC)

- Sharks to maintain a LOC equal to **two years** of debt service payments
- Can be reduced to **one year** of debt service payments after one of the two conditions are met:
 - Debt Service Coverage Ratio for prior three fiscal years is 1.50 times operating income
 - San Jose Arena Management, LLC agrees that the Arena Management Agreement is extended to June 30, 2040, without right of early termination
- LOC requirement can be **eliminated** after both conditions are met
- City maintains the ability to **reinstate** the LOC (or cash security deposit) equal to one year of debt service payments, if the Debt Service Coverage Ratio for the prior consecutive three fiscal years has not be maintained at least 1.50 times operating income

▪ Long-Term Leases

- The Barracuda will sign a 30-year sublease for the Barracuda's occupancy of the AHL training facility, the San Jose Sharks will sign a 30-year sublease for the NHL training facility

Key Business Terms – Amended/Restated Lease and Management Agreement

▪ Parking

- In addition to roughly 435 on-site parking spaces available onsite, Sharks Ice will enter into a Parking Agreement with SJSU for parking
- Parking Agreement must align with the term of the Agreement and allow the Parking Agreement to be assigned to the City or other operator of the Ice Centre

▪ Arena Authority

- Sharks Ice currently contributes annual payment budgeted at \$49,955 which beginning in FY 2020-21 increases to \$100,000 and escalates with inflation

▪ Ticket Distribution Program

- Sharks Ice will provide the City with up to 20 complimentary club-level seat tickets to Barracuda home games

Key Milestones

- **January 2020**
 - Council approval of the Ice Centre Construction Project

- **March 2020**
 - Council approval of
 - Amended and Restated Lease and Management Agreement
 - Issuance of taxable lease revenue bonds and related documents (2/3 Council approval)

- **April 2020**
 - Bond sale and closing
 - Funds provided by bond trustee to fund Ice Centre expansion improvements
 - Commence Construction

- **April 2022**
 - Project Completion

Conclusion

- City staff recommends approval of the Financial Feasibility Report
 - Report satisfies the requirements of the City's Debt Management Policy
 - Provides support of project revenues sufficient to solely support the proposed leased revenue financing (of the Ice Centre Expansion Project)
- Council approval of recommendations will provide direction to develop a bond financing plan (and associated documents) and negotiate the new Agreement with Sharks Ice, LLC

Recommendation

1. Accept Feasibility Study on the financial feasibility of financing the proposed expansion of the Solar4America Ice Centre with the lease payments from Sharks Ice, LLC
2. Direct staff to develop a bond financing structure and prepare the necessary documents for consideration by the City of San Jose Financing Authority Board and City Council
3. Direct staff to negotiate an Amended and Restated Lease and Management Agreement with Sharks Ice, LLC for the City Council's consideration

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