



Date: December 6, 2023, 2023

To: Christine Taylor, Assistant City Manager, City of Denton
Ralph Bishop, Fine Arts Theater of Denton, LLC.

Re: **Final** Revised Underwriting Report 3 incentive options – Fine Arts Theater of Denton, LLC.

From: Grow America, formerly National Development Council
Underwriter: Sheldon Bartel, CEcD, EDFP, HDFP

STATUS: The City of Denton (“City”) and Fine Arts Theater of Denton, LLC (“Developer”) retained Grow America to underwrite Fine Arts Theater of Denton, LLC request for a \$2,000,000 City economic development incentive. A final underwriting report was delivered (8/16/23) as a guide to assist the City in determining the type(s), timing, and amount(s) of incentives to commit, if any.

The requested incentives will support the development of 113-115 N. Elm Street, Denton TX (“Project”). The expected outcome is a rehabilitated historic theater with approximately 200 seats and V.I.P. mezzanine (25-30 seats), a smaller movie theater on the second level with approximately 50 seats, and a new concession area at the entrance with a bar that overlooks the downtown courthouse open to theater patrons and casual visitors alike. The developer believes the Project will contribute to the City as follows:

- Generate new revenue (sales and mixed beverage as well as property taxes) and drive tourism and visits to Denton Square and the City.
- Increase Denton Square’s value as a unique business and promote investment in other non-competing businesses due to increased visits.
- Enhance the creative arts culture of Denton.
- Provide new jobs and training in the theater arts with plans to partner with UNT’s media arts and hospitality management departments.
- Continue to revitalize Denton Square by bringing another newly rehabilitated building up to code.

The City provided a term sheet to the Developer post underwriting report. Following a meeting between the City and Developer where the Developer provided revised project financial information including:

- A revised operating model including proposed sales tax and property rebates,
- Updated Project development costs, sources and uses, based on the 8/31 balance sheet,
- corrections to the lender’s cash reserve requirement for debt service coverage after clarifying our projections of operating losses during the first few years, as well as the interest calculation.

Developer finds that because of the above changes and the assumption that the Project is approved for property and sales tax rebate incentives for 10 years:

- the initial cash needed at the opening, (year 1) is reduced to \$193,107.
- additional cash of \$121,371 to cover losses in years 2-4.
- The total cash requirement for working capital and debt service coverage is \$314,478.



With this information the Developer presented to the City three (3) incentive options as follows:

1. Option 1 - \$1,076,366 City of Denton incentive at CO, this can be a grant for 5 to 7 years . No tax rebates. An additional \$544,782 City of Denton incentive funded at opening or annually as needed, as a grant for 5 to 7 years s.
2. Option 2 - \$1,076,366 City of Denton incentive at CO, this can be a grant or forgivable loan over 10 years. Annual rebates for property, sales, and beverage taxes for 10 years. An additional \$314,478 City of Denton incentive funded at opening or annually as needed, as a grant or forgivable loan over 10 years.
3. Option 3 – Developer is not eligible for Option 3. Only non-profits are eligible for HOT funds. Developer pointed out that options 1 and 2 will require an additional capital contribution from its ownership group of approximately \$555,000, bringing their total investment to approximately \$1,837,000.

On 10/16/23 the City asked Grow America to review the new information and 3 incentive options for the Project provided by the Developer.

REVIEW OF PROJECT COSTS: Developer is proposing the rehabilitation of a Historic Theater into a multi-use entertainment facility. Existing 9,900 sqft structure is situated on 6,000 sqft footprint located at 113-115 N. Elm in the Denton Square. This is in a 2023 Qualified Census tract. Developer has site control via fee simple ownership of the property since 2018.

The building was originally constructed as a furniture store in the 1890’s and converted to a movie theater in 1935. The building ceased operation as a movie theater in 1982. From 1982 to 2014 the space was utilized as a church and performance space. It has been vacant since 2014 and sustained considerable interior damage due to a small fire and weather-related issues due to a faulty roof. The Developer acquired the Project site in 2018 has restored the building to shell condition which included replacing the roof, asbestos removal and abatement, and demolition of the damaged areas along with architectural services at a cost of approximately \$2,146,714.

The ownership intends to completely renovate the building and convert it into a multi-use entertainment facility. Examples of its activity will involve assorted options including movies, film festivals, concerts, live performance, and rentals such as receptions, seminars, and worship services, as well as various community-based rentals. The renovated facility will have three interior levels and includes a restored main theater with approximately 200 seats and V.I.P. mezzanine (25-30 seats), a smaller movie theater on the second level with approximately 50 seats, a new concession area at the entrance and a bar that overlooks the downtown courthouse open to theater patrons and the public.

The table below shows the total rehabilitation budget, sources and uses of funds, and permanent financing for Fine Arts Theater at 3/21/23 (application) and 8/31/23. The table includes post construction proposed investments by Developer and City (Option 1).



Uses:		3/21/2023		8/31/2023	Difference
Building Purchase (at actual)		\$769,442		\$769,442	(0)
Pre-development Costs (at actual)		\$1,377,272		\$1,440,025	62,753
Total Pre-Development Costs		\$2,146,714		\$2,209,467	62,753
Rehabilitation Costs (projected)					
Rehabilitation costs & Contingency		\$5,185,490		\$5,186,074	584
Furniture & fixtures		\$629,985		\$629,985	0
Soft costs		\$410,000		\$410,000	0
Interest & related costs		\$672,409		\$684,096	11,687
Cash Reserve to meet OWC/DSCR Requirement		\$924,634		\$0	(924,634)
Total Projected Rehabilitation costs		\$7,822,518		\$6,910,155	(912,363)
Total Projected Project Costs		\$9,969,232		\$9,119,623	(849,609)
Funding Sources:					
Cash equity already invested		\$1,152,260		\$1,282,041	129,781
Deferred developer fee		\$250,000		\$250,000	0
Construction Loan Proceeds:					
Appraised Value - As Complete 75%LTV	\$3,195,000		\$3,195,000		0
Loan on Historic Tax Credits 75% LTV	\$2,000,000		\$2,033,217		33,217
Pledged collateral 75% LTV	\$744,918		\$2,359,365		1,614,447
Funding GAP	\$2,627,054		\$0		(2,627,054)
Construction Loan Amount	\$8,566,972	\$8,566,972	\$7,587,582	\$7,587,582	(979,390)
Total Funding Sources		\$9,969,232		\$9,119,623	(849,609)
Post Construction Loan Paydown					
Construction Loan		\$ 5,939,918		\$ 7,587,582	1,647,664
Historic Tax credits (Estimated)		\$ (2,694,918)		\$ (2,710,956)	(16,038)
Denton Downtown Econ Façade Grant (Estimated)		\$ (50,000)		\$ (50,000)	0
COD Rehab Cash Incentive		\$ -		\$ (1,076,366)	(1,076,366)
Funding Gap funded by partners		\$ -		\$ (555,260)	(555,260)
Loan Balance		\$ 3,195,000		\$ 3,195,000	(0)

Notes:

Rehabilitation/Construction.

- The 8/31/23 projected total rehabilitation/construction cost is reasonable. Total cost per square foot is \$921.
- Total pre-development costs increased \$62,753. These have been funded by a combination of \$1.2 million Developer cash and \$1.0 million loan.
- Total Rehabilitation costs (uses of funds) are \$9,119,623 – a decrease of \$849,609. This is primarily due to removal of cash reserve to meet Lender OWC/DSR requirement. This is a post rehabilitation cash need.
- Total Funding sources are \$9,119,623 – a decrease of \$849,609. Expected proceeds from sale of Project Historic Tax Credits increased \$33,217, proceeds from Developer pledged collateral



increased \$1,614,447, and the rehabilitation funding gap decreased \$2,627,054. The Developer is filling the gap.

Post Construction

The City will only be involved post construction. Lender requires the Developer pay down the construction loan to 75% of “as completed” appraised value of \$4,260,000 = \$3,195,000. Sources of funding to pay down the Lender are sale of Project Historic Tax Credits, proposed City Rehabilitation Cash Incentive (\$1,076,366), Denton Downtown Reinvestment Grant (\$50,000), and \$555,260 additional Developer cash. Discussion of City post construction incentives follows.

Option 1

Post Construction Permanent Financing (Spreadsheet Option 1 Project Cost Worksheet and Sources of Funds tabs)

- The City will only be involved post construction.
- Project Development Budget is a breakdown of the rehabilitation/construction costs.
- Source of Funds is the breakdown of post construction permanent financing including the Lender loan (\$3,195,000), the City’s proposed Rehab Cash Incentive (\$1,076,366), Downtown Reinvestment grant (\$50,000), Historic Tax Credit equity (calculated by Project consultants Architexas @ \$2,710,685), and Developer equity investment (\$1,837,041) into the Project as well as Developer Deferred Loan (\$250,000).
 - Sources of funds exceed uses of funds by \$529 (insignificant).

Operating and Debt Service Reserve Needs (Spreadsheet Option 1 Proforma tab)

The Proforma shows the projected revenues and expenses for 10 years for the Project. Revenues and expenses were provided by Project Consultant ACI North LLC who has operated the Texas Theater in Dallas since 2010. Add backs to Net Profit include:

- Proposed/requested City Operating and Debt Reserve Grants totaling \$544,503 that includes:
 - \$465,701 over 7 years to cover projected shortfall between project Net Profit and Debt Service that results in required debt service coverage ratio of 1:1. These funds are included in the Add Backs to Cash Flow section of the Option 1 Proforma.
 - The Lender requires an additional \$0.25 of cash flow for debt service be maintained in a reserve account at the lending bank. This amounts to \$78,802 and is identified as Bank Required DSC Reserve (0.25%) on the Proforma. The source of the \$78,802 is the proposed City operating reserve incentive. The funds will only be drawn down should they be needed, that is, actual operations demonstrate cash flow for debt service is lower than projected. These funds are included in the Bank Required DSC Reserve line on the Option 1 Proforma.
- In summary, the projected total value of City operating and debt reserve incentives under Option 1 is \$544,503. When the City Rehab Cash (\$1,076,366) and City Downtown Reinvestment grant (\$50,000) incentives are added to the operating and debt reserves (\$544,503) incentives the total City incentive package totals \$1,670,869.

Option 2

Post Construction Permanent Financing (Spreadsheet Option 2 Project Cost Worksheet and Sources of Funds tabs).

The City will only be involved post construction.

- Project Development Budget is a breakdown of the rehabilitation/construction costs.



- Source of Funds is the breakdown of post construction permanent financing including the Lender loan (\$3,195,000), the City’s proposed Rehab Cash Incentive (\$1,076,366), Downtown Reinvestment grant (\$50,000), Historic Tax Credit equity (calculated by Project consultants Architexas @ \$2,710,685), and Developer equity investment (\$1,837,041) into the Project as well as Developer Deferred Loan (\$250,000).
 - Sources of funds exceed uses of funds by \$529 (insignificant).

Operating and Debt Service Reserve Needs (Spreadsheet Option 2 Proforma tab)

Add backs to Net Profit include:

- Proposed/requested City Operating and Debt Reserve Grants totaling \$301,947.
 - \$223,145 over 4 years to cover projected shortfall between project Net Profit and Debt Service that results in required debt service coverage ratio of 1:1. These funds are included in the Add Backs to Cash Flow section of the Option 2 Proforma.
 - The Lender requires an additional \$0.25 of cash flow for debt service be maintained in a reserve account at the lending bank. This amounts to \$78,802 and is identified as Bank Required DSC Reserve (0.25%) on the Proforma. The source of the \$78,802 is the proposed City operating reserve incentive. The funds will only be drawn down should they be needed, that is, actual operations demonstrate cash flow for debt service is lower than projected. These funds are included in the Bank Required DSC Reserve line on the Option 2 Proforma.
- Proposed City real estate tax rebate equal to 100% of the estimated property taxes of the Project
 - This is calculated on an estimated assessed value of \$3,195,000 (75% of the “As completed” appraised value of \$4,260,000) increasing 3% per year over 10 years. Total property tax rebate over 10 years = \$205,362 These funds are included in the Add Backs to Cash Flow section of Option 2 Proforma along with the following:
- Proposed City Sales Tax rebate 1.5% of total revenues over 10 years. Total sales tax rebate over 10 years = \$225,837.
- Proposed City Mixed Beverage Gross Receipts Tax over 10 years calculated using 50% of projected concession revenue. Total MBGRT tax rebate over 10 years = \$24,626
- Proposed City Mixed Beverage Sales Tax over 10 years calculated using 50% of projected concession revenue. Total MBST rebate over 10 years = \$30,322

In summary, the projected total value of City operating and debt reserve incentives under Option 2 is \$788,094. When the City Rehab Cash (\$1,076,366) and City Downtown Reinvestment grant (\$50,000) incentives are added to the operating and debt reserves (\$788,094) incentives the total City incentive package totals \$1,914,460.

Option 3

Developer is not eligible for HOT Funds.

ANALYSIS OF DEVELOPER PROPOSED INCENTIVES

The Table highlights the 2 Options of incentives proposed for the Project.

COD \$	Option 1	Option 2
Rehab Cash	\$1,076,366	\$1,076,366
Downtown Reinvestment Grant	\$50,000	\$50,000
Operating Reserve	\$465,701	\$223,145



Debt Service Reserve	\$78,802	\$78,802
Cash Rebates*	N/A	\$486,147
Hot Funds	N/A	N/A
Total	\$1,670,869	\$1,914,460
Developer Equity	\$1,837,041	\$1,837,041

- Property, Sales, MBGRT, & MBST Rebates

Option 1: \$1,076,366 City of Denton Rehab Cash incentive at CO, this can be a grant for 5-7 years. No tax rebates. An additional \$544,782 City of Denton incentive funded at opening or annually as needed, as a grant over 10 years. This includes \$465,701 City operating incentive over 7 years and \$78,802 debt service reserve. This is sufficient to produce cash flow sufficient to repay Lender loan at 1:1 ratio as well as fund the Lender required 0.25:1 debt service coverage reserve.

When the City Rehab Cash (\$1,076,366) and City Downtown Reinvestment (\$50,000) incentives are added to the operating and debt reserves (\$544,782) incentives the total City incentive package totals \$1,670,869. This option is the least expensive option.

Under Option 1, the Developer begins to receive a cash-on-cash return on \$1,837,041 equity (Cash Flow Available for Distribution divided by equity investment) starting in year 8. There is no return on the Deferred Developer loan until year 11.

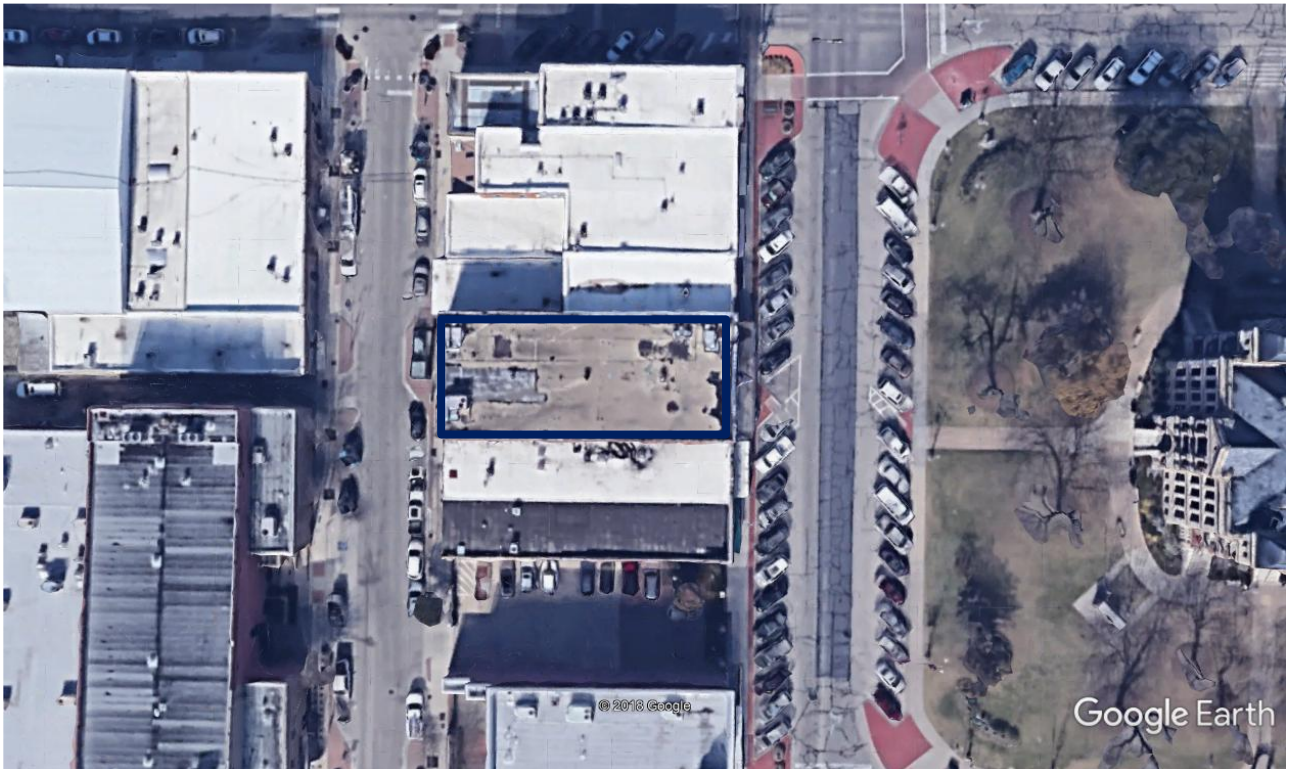
Option 2: \$1,076,366 City of Denton incentive at CO, this can be a grant over 10 years. An additional \$709,292 City of Denton incentive funded at opening or spread annually as needed, as a grant over 10 years. This includes \$223,145 City operating incentive over 4 years and \$78,802 debt service reserve. This is sufficient to produce cash flow sufficient to repay Lender loan at 1:1 ratio as well as fund the Lender required 0.25:1 debt service coverage reserve. In addition, the City provides \$486,147 real estate, sales, and beverage taxes rebates over 10 years.

When the City Rehab Cash (\$1,076,366) and City Downtown Reinvestment (\$50,000) incentives are added to the operating (\$223,145) and debt reserves (\$78,802) as well as property, sales, MBGRT, and MBST rebates (\$486,147) incentives the total City incentive package totals \$1,914,460.

Under this Option, the Developer only receives a cash-on-cash return on \$1,837,041 equity (Cash Flow Available for Distribution divided by equity investment) starting in year 5. There is no return on the Deferred Developer loan until year 11.



Exterior View: Front



Location



Interior View

