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MEMORANDUM

Date: April 21, 2006

From: George Sweeting

To: Council Member David I. Weprin and the City Council Finance Committee
Council Member Hiram Monserrate

Subject : Financing Plan for the Proposed Stadium for the Mets **(Revised)**

As you requested at the April 10, 2006 Finance Committee hearing, IBO has reviewed and analyzed the financing terms of the proposed stadium for the New York Mets. We have followed the same general outline used in the testimony we presented on the stadium proposed for the Yankees.

The plan for financing a new stadium for the Mets includes direct subsidies and exemptions from state and local taxes as well as access to tax-exempt bonds for building the stadium. Over a 40-year period, these subsidies and exemptions would cost the city $155 million (present value) and the state an additional $89 million. For the Mets, these benefits, including savings that result from the use of tax exempt bond financing, add up to $276 million over 40 years (present value).

The tax exempt bond financing is the largest of the benefits offered to the Mets, saving the team $105 million over 40 years. These bonds depend upon an unusual arrangement for repayment and the city is awaiting word on whether it complies with federal tax rules.

The following paragraphs briefly review each of the benefits and exemptions being offered, followed by a more detailed discussion of the tax-exempt financing subsidy.

Capital Investments. The city expects to spend $105 million over the next three years for infrastructure and other improvements around the new stadium, including preparing the site, demolition of the old stadium, and paving of parking lots. The state would also contribute $70 million for infrastructure.

The city's spending for infrastructure and other improvements will be financed by issuing bonds through the city's regular capital program, with the principal and interest payments funded with general city revenues. The projects are already included in the current Capital Commitment Plan, with commitments scheduled for 2007 and 2008. The present value of the city's debt service obligations for these projects is $98 million.[1] Similarly, assuming the state uses Empire State Development Corporation bond financing for its $70 million contribution, the present value of the state's debt service cost is $73 million.[2]

Property Tax Exemption. The new stadium will be exempt from New York City's property tax because it will sit on public land and will be legally owned by a subsidiary of the city's Industrial Development Agency (IDA); the subsidiary will lease the stadium to the Mets. The Mets will make a payment in lieu of taxes, or PILOT, but it will be used to pay debt service on the construction financing rather than flow into the city's coffers in place of the foregone property tax. IBO's estimated value of the exemption is based on a 2010 market value of $543 million ($444 million cost of construction plus $99 million land value).[3] IBO estimates that this exemption generates savings to the Mets of $72 million (present value) over 40 years. These savings are net of the tax breaks under the Industrial and Commercial Incentive Program that would automatically apply if the stadium were taxable. The property tax exemption does not reduce the city's current revenues because there is no property tax today from the existing stadium. Because there is no loss of current revenue, IBO does not include the value of the exemption as a cost to the city.

Sales Tax Exemption. The project will be exempt from city, state, and Metropolitan Transportation Authority (MTA) sales tax on purchases of construction material, equipment and fixtures installed in the stadium. This benefit is granted at the discretion of the Industrial Development Agency. IBO estimates the 40-year cost of the exemption for the city will be $8.7 million and $9.5 million for the state and MTA combined. The exemption results in an equal amount of savings for the Mets.

Foregone Parking Revenues. Under the current lease, the city gets about half of the parking revenues from the city-owned parking lots around the stadium. In recent years this has brought in about $3.7 million per year. Under the new lease, the Mets will keep the first $7 million of annual parking revenues and then split the remainder with the city. (The $7 million figure will be adjusted for inflation each year.) IBO estimates that with the new terms in place, the city will a lose $57 million (present value) over 40 years, compared with what it would receive if the current arrangement remained in place at the new facility.

Rent Credits. Under the current lease between the Mets and the city, the team has been allowed a rent credit of up to $5 million each year from 2001 through 2005 for costs associated with planning and designing the new stadium. Under the June 23, 2005 memorandum of understanding between the city and Mets, the team will be entitled to an additional $5 million in annual rent credits for 2006, 2007, and 2008 as well, although with construction expected to be underway by then, most of the planning costs for the new stadium will have already been incurred.

Capital Replacement/Operation Reserves. When the new stadium is completed, the city and state will each make one-time, $4.7 million payments into reserve funds for the stadium. Thirty years after the stadium opens the city will make an additional $8.5 million payment for the same purpose. The city's contribution to these reserves will total $6.3 million in present value terms.

Mortgage Recording Tax Exemption. Like the sales tax exemption, this benefit is also granted at the discretion of the Industrial Development Agency and it has been made available for the project. However, because this project uses bond financing rather than mortgage financing, the exemption is unlikely to result in significant costs for the city or savings for the Mets.

Rent and Maintenance. The Mets will pay no rent for the use of the new stadium. This is in contrast with the current lease under which the Mets owe annual rent payments based on a percentage of ticket sales, advertising and other revenues. Under the current lease the city is responsible for the costs of maintenance expenses and upkeep, including capital improvements. In recent years, as a result of large capital expenditures at Shea, the city has been losing money on its lease with the Mets. Under the proposed lease for the new stadium the Mets would pay for maintenance and upkeep. The city will also be spared the expense of making major repairs in the old stadium in the coming decades. Estimating the value of the foregone rent and the averted city spending on maintenance and repairs is quite speculative, but projecting from actual results in recent years, IBO estimates that under the new stadium lease, the city would have a net savings of $31 million (present value) compared with having the Mets remain in the current stadium with the current lease in place.

Access to Tax Exempt Bond Financing. The largest benefit for the Mets comes from the tax-exempt financing. Tax-exempt bonds lower the project financing costs for a developer because investors are willing to accept a lower interest rate since their interest income is not subject to income tax. IBO assumes that the difference in interest rates between taxable and tax-exempt bonds is 1.5 percentage points. This means that the Mets can save about $6.9 million annually. The present value of the savings for the team over the 40-year financing period is $105 million.

The cost of this subsidy falls largely on the federal government. IBO estimates that the annual cost in federal tax revenues will be about $2.1 million, or $32 million over 40 years (present value). The impacts on the city and state budgets depend on how many of the investors who buy the bonds are New York residents. It is likely that a significant share would be residents, given the triple tax-free nature of these bonds and the existence of municipal bond mutual funds targeted for New York investors. Assuming that half of the buyers reside in the city, the cost to the city budget is about $1.6 million over 40 years and the cost to the state budget is roughly $2.9 million.

In order to make the savings for the Mets possible, the proposed financing plan relies on an aggressive interpretation of what investments that largely benefit private entities are eligible for the tax exemption. The Bloomberg Administration has asked the Internal Revenue Service (IRS) for a letter ruling on the matter. It is not clear whether a ruling will be made before the Council currently plans to vote on the use of PILOTs later this month.

The tax-exempt status of bonds for federal income tax purposes is governed by the federal internal revenue code (IRC). Exemption from city and state income tax is determined by city and state laws, which closely parallel federal provisions. In general, the IRC limits tax exempt status to projects with a governmental or public purpose, although bonds for some private activities can qualify. In 1986 an amendment sponsored by Senator Daniel Patrick Moynihan—who had long sought to ban the use of tax-exempt bonds for sports facilities—was enacted specifically excluding sports facilities from projects eligible to use tax-exempt private activity bonds. The

IRC permits some private projects that are not eligible to use private activity bonds to qualify for government purpose bonds by satisfying several tests spelled out in the revenue code.

In the case of the Mets' stadium, the important eligibility test to qualify as public purpose in the IRC is known as the "private payment test." A project is disqualified under this test if more than 10 percent of the revenue used to pay the debt service on the bonds is generated directly from the project itself—by rental payments, for example. (This test is one reason why the project does not include rent paid from the team to the city.) Viewed from the opposite perspective, at least 90 percent of the revenue paying the debt service must come from broader sources such as general taxes or fees that apply to the whole city or other broad geographic area.

Although the Mets—rather than the government —are in fact paying for construction of the stadium, their intention is to maximize the use of cheaper tax-exempt financing. This makes it necessary to structure the agreement so that the money pledged for debt service on the bonds bears enough resemblance to a regular city tax that the deal can get past the private payment test.

The solution developed by the project's planners is a payment in lieu of taxes, which according to the Industrial Development Agency documents will be calculated in a manner similar to the city's regular property tax. (As discussed above, the stadium will actually be exempt from property tax because it will be publicly owned and leased to the Mets, in part to help qualify the deal for tax-exempt financing.)

Given the large annual payments needed to service the $528 million of tax-exempt bonds proposed in the financing plan, it is not clear that a property tax-based PILOT would be sufficient. Assuming an interest rate of 6.5 percent, annual debt service payments for 40 years on level payment bonds would be about $37.3 million.[4] Based on the $444 million estimated construction cost for the new stadium plus the value of the land as currently recorded on the city's assessment roll, IBO estimates that a regular property tax bill in 2010 would be about $27.6 million (before exemptions)—considerably below the annual debt service payments. The gap between IBO's projected PILOT and the necessary debt service would change under different financing terms. For example, if the interest rate were 5.5 percent then 40-year bonds would require an annual payment of $32.9 million. Alternatively, shortening the term of the bonds to a more conventional 30 years would result in higher annual payments: at 5.5 percent they would be $36.3 million and at 6.5 percent they would be $40.4 million.

Costs and Benefits. In total, the bond financing, direct subsidies and exemptions will save the Mets $276 million and cost the city $155 million in forgone revenue and the state $89 million. However, these costs should not be viewed as the total fiscal impact for the city of the stadium project; such an estimate would also include the impact on city revenues of any additional economic activity associated with the new facility. Because of the short time available to prepare this review, we are not able to undertake a complete fiscal analysis.

Nevertheless, we can make a few observations about the stadium's likely broader economic effects. The incremental job and revenue claims made by the stadium's planners are relatively modest. In the IDA Project Cost/Benefit Analysis, the 40 year present value of incremental city tax revenues from construction and operation of the stadium is estimated at $61 million. There is no detail provided, but the three-year construction period, when the employment effect is much greater than during the actual use of the stadium, likely accounts for a disproportionate share of the new revenue.

It is not surprising that IDA's estimate is relatively low given that this project replaces a facility that has been operating in recent years at about 60 percent of its full capacity with a significantly smaller facility. (The capacity will drop from 56,000 at the existing Shea Stadium to 44,100 at the new facility.) There is little reason to expect a large gain in local economic activity beyond the three-year construction period since most of the spending at the new stadium will directly replace spending that would have occurred at the existing stadium.

Attendance is expected to increase in the first few years after the new stadium opens and prices for tickets and other items at the stadium will probably be higher than at the current stadium, yielding higher revenues for the Mets. However, because a large share of sports business income flows to a relatively small number of players and owners—few of whom reside in the city— much of these earnings will be spent elsewhere with only a small effect on the local economy.

IDA's cost/benefit analysis finds a net fiscal benefit for the city of $48 million in present value terms. But their calculation ignores several items that IBO would include in such a calculation, most notably the foregone parking revenues, which IBO estimates have a present value of $57 million. Simply including that item in the IDA calculation would switch the fiscal impact from a net positive to a net negative.

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1 Based on the projected long-term general obligation bond rate for the first half of fiscal year 2007 of 5.5 percent in the Mayor's Office of Management and Budget Debt Service back-up from the January 2006 Financial Plan.

2 Based on 30-year bonds paying 6.5 percent. The higher rate reflects an assumed premium for Empire State Development Corporation debt.

3 IBO's market value assumes no change in the current value of the land under the stadium as recorded on the city's 2007 property tax assessment roll, other than modest baseline appreciation. Given that the project is essentially swapping the current sites of the stadium and the parking lots within the same parcel of land there is no change in land use to produce a significant change in value. In addition, IBO's estimate of the land value did not reflect the cost of driving pilings into the ground in order to support the new stadium and other site preparation covered by the city's capital contribution. Presumably a private developer purchasing this land for commercial development would face similar costs which would be capitalized in the sales price.

4 IBO's interest rate assumption is based on the city's current projection of a 5.5 percent interest rate for new general obligation bonds issued during the first half of fiscal year 2007 plus a 1 percentage point premium given the sole reliance on project revenues to service the debt.

(Costs)/Savings From Exemptions and Subsidies for New Mets Stadium
Present value (millions of dollars)[a]

	City (Costs)/Savings	State/MTA (Costs)/Savings	Mets' Savings
Infrastructure Contributions	($98.4)	($72.7)	$0.0
Foregone Parking Revenue	(57.4)	0.0	80.0
Property Tax Exemption	0.0	0.0	71.8
Sales Tax Exemption	(8.7)	(9.5)	18.2
Tax Exempt Financing	(1.6)	(2.9)	104.9
Maintenance Savings Net of Foregone[b]	31.0	0.0	n.a.
Rent Credits 2006-2008	(13.4)	0.0	13.4
Capital Replacement Reserves	(6.3)	(3.9)	10.2
TOTAL	**($154.7)**	**($89.0)**	**$275.8**

SOURCES: IBO; January 2006 Capital Commitment Plan; New York City Industrial Development Agency
NOTES:
a) Present value computed using discount rate of 6 percent over 40 years.
b) The cost or savings to the Mets over 40 years will depend on factors such as future team revenues, wear and tear on the stadium, and future repair costs.