FINANCE COMMITTEE MEETING

The Finance Committee of the City of Norfolk, Nebraska met in the City's Conference Room, 309 West Madison Avenue, Norfolk, Nebraska, on Monday, October 16, 2006, beginning at 7:00 a.m.

Mayor Gordon D. Adams called the meeting to order.

Roll call found the following Committee members present: Mayor Gordon Adams and Councilpersons Kaspar-Beckman, Brenneman, Fauss, Lange, Saunders, Stauffer, Van Dyke and Wilson. Absent: None.

Staff members present were City Administrator Mike Nolan, Public Works Director Dennis Smith, City Attorney Clint Schukei, City Clerk Beth Deck, and Finance Officer Randy Gates.

The media was represented by Jim Curry, WJAG/KEXL; Greg Wees, Norfolk Daily News; and Brian Masters, US92.

Notice of the meeting was given in advance by publication in the Norfolk Daily News, and notice of the meeting was given to the Mayor and all members of the Council prior to the meeting.

The Mayor presided and the City Clerk recorded the proceedings.

The Mayor informed the public about the location of the current copy of the Open Meetings Act posted in the meeting room and accessible to members of the public.

Items listed on the agenda for discussion were:

1. Letter dated October 11, 2006 to the Mayor and City Council from Phil Perry.
2. Loan modification agreement and related allonge with Meadow Ridge Partners, LLC, forgiving accrued interest on the $935,000 HOME loan to Meadow Ridge Partners, LLC, and reducing the interest rate from 7.88% to 0%.
3. Subordination agreement subordinating the City's $935,000 HOME loan to Meadow Ridge Partners, LLC, to a loan from JP Morgan Chase Bank.
4. Authorization for the Mayor to sign a letter to the Nebraska Department of Economic Development requesting an amendment to Grant Contract M94-SG-3101-13 to reduce the number of HOME assisted units from 42 to 19.
5. Memorandum of Understanding (MOU) with Meadow Ridge Partners, LLC, requiring Meadow Ridge Partners to comply with HOME Program requirements and limiting distributions to the Managing Members to $30,000 annually.

City Administrator Mike Nolan disclosed to the Mayor and City Council that the City's server was down last night but Nolan received an audited financial statement from Phil Perry at 11:03 p.m. on Sunday, October 15, 2006, and it was emailed at 10:35 a.m. that morning. Nolan stated all of the elected officials were copied in on the email. The document is entitled, "Meadow Ridge Audited Statements for 2000-2001 and 2001-2002". Another email was sent at 10:35 a.m. and Nolan received it at 12:25 p.m. yesterday. The email was with regard to a written response from Angie Maurer, Comptroller for Perry Reid Properties, regarding information received

regarding the Public Meeting Laws that was presented at the City Council meeting on October 11, 2006. Nolan wanted elected officials to know the effort was made to get the information sent out in time for this meeting.

Councilperson Fauss said there wasn't any use to send it on Sunday when the information was requested last Wednesday.

Nolan just wanted elected officials to know the information was emailed to each of them.

Mayor Adams received the emails and didn't think it was new information since it was copies of the financial statements that Finance Officer Randy Gates has received.

Attorney Jan Einsphar was present at the meeting representing Meadow Ridge Partners.

Councilperson Fauss feels Perry has received documents requested from the City, but elected officials have not received all of the documentation requested from Perry.

Mayor Adams questioned what specific documents Fauss is requesting.

Fauss requested copies of all of the financial records for Meadow Ridge Partners LLC. Perry supplied copies of only two years worth of financial statements.

Councilperson Van Dyke had a lot of questions regarding the issue. Van Dyke had questions on the following:

(1) The original NDED contract expiration date in Section 1.05, Time of Performance. It said, "The period covered under this Contract will be 24 months from March 14, 1995. The termination date of this Contract will be March 14, 1997." Van Dyke questioned whether the City still has a contract with NDED.

Finance Officer Randy Gates stated the regulatory agreement is in place with NDED for twenty (20) years. Gates stated the 1997 contract was in place to get the funds spent but the City still needs to comply with the regulations for twenty years.

(2) Van Dyke questioned where the $397,220 in Section 3.01, Project Description, came from. Van Dyke said the fee increases over the years and the higher fee generates more money from the administration of the grant.

Gates said the amount includes a developer's fee of $300,000 and the $97,220 was advanced by the partners. Gates said the preferential cash flow is a percentage of the $397,220. Therefore, the partners could take $60,000 but have only been taking $30,000 annually.

(3) Tax credit investors – Van Dyke has concerns because it sounds like the only way the tax credit partners can withdraw from the project is if the City of Norfolk forgives the accrued interest. However, the "Fact Sheet" states, "The tax credit partners have received more tax credits than promised on this project."

Gates explained the operating agreement specifies when the tax credit partners can take out the tax liability. The project is generating big losses every year, a large part of which is the interest on the note.

Van Dyke said the tax credit partners aren't paying the interest and, therefore, should not be deducting the expense. Van Dyke also questioned how residual receipts are figured. The note said residual receipts shall be paid for from surplus cash and residual receipts which are defined as those funds left over after vacancy costs, operating expenses, superior lien debt service, and preferential cash flow are subtracted. Van Dyke was referring to a Statement of Loss. Van Dyke said the reason there is a loss is because "they are saying they are paying the interest but they aren't."

Gates said the deductions can be made because of accrual accounting. Once an expense is booked, the deduction can be made on a tax return by the tax credit partners. The tax credit partners get this benefit for putting money up front for the project.

Einsphar said accrual accounting shows expenses that can be deducted for tax purposes. One of the biggest expenses that can't be deducted for tax purposes is the principal payment being made to the first lien holder. There isn't any extra cash available at the end of the year.

General discussion was had regarding Van Dyke's question about accounting.

Gates said the way the original documents are written, the City will never see any preferential cash flow. The proposed Memorandum of Understanding defines the preferential cash flow computations as not being cumulative. The Memorandum of Understanding also limits the amount of distribution to $30,000 annually to the Partners.

Van Dyke doesn't feel the interest should be deducted as a loss since it isn't paid out.

(4) Subordination Agreement – Van Dyke has concerns with the agreement because the City isn't able to condemn the property, if necessary. Van Dyke stated the City won't even have a lien under Section 8(c) of the agreement and the City isn't able to foreclose on the property. Section 9 also says the City will be agreeing "to almost everything the Senior Lender wants to do." Van Dyke feels everything in the Agreement is set up for the first mortgage holder and the City doesn't have any rights left.

Gates agrees that the Subordination Agreement is a standstill agreement and basically the City can't take any action under the agreement. Gates doesn't like the agreement but the City doesn't have any other option. If Meadow Ridge Partners is going to refinance with JP Morgan it will be packaged together with other loans and sold. This is a standard subordination agreement required by JP Morgan to sell these types of loans as a package.

Gates also said the City won't see a lot of money repaid to the City, if any, on the loan. However, in most years the City should get some money back if the new documents are approved.

Schukei stated City staff had the same concerns as Van Dyke and raised the same questions when presented with the Subordination Agreement. Schukei stated JP Morgan Chase Bank is the entity requiring the Subordination Agreement.

Gates stated the proposed refinancing allows the City the opportunity to receive money and provides Meadow Ridge Partners with money to be able to lower rents. There may be approximately $9,000 available annually to pay back to the City.

Mayor Adams asked whether the City has any assurances that the actual result will be an increase in the number of low rent housing units available.

Gates stated the MOU outlines that Meadow Ridge Partners will comply with HOME loan requirements and the letter to DED will modify the City's contract to reflect that change.

Mayor Adams stated the original concept of the project was for the City of Norfolk to provide low rent housing. If elected officials agree with the changes, the City will have at least as much or more low rent housing available, and that is a significant economic development issue. The availability of low rent housing is a major factor in the attractiveness of a community.

Van Dyke questioned why the original grant was changed into a loan.

Einsphar stated the grant was structured as a loan to benefit the tax credit partners.

Councilperson Fauss questioned why all of the financial statements for all of the years have not been provided to elected officials. Fauss doesn't want the audited financial statements. Fauss wants the actual spreadsheets showing expenses. Fauss doesn't trust Phil Perry.

Einsphar said the City has received the financial statements every year. Einsphar said Meadow Ridge rents have not been raised to keep up with the rate of inflation, which means rents have not been raised enough to keep up with the costs of operation. Einsphar said the Partners have not taken money out of the project other than the $30,000 annually plus the management fee.

Van Dyke said the statements show $800,000+ paid to the City of Norfolk that hasn't been done. Van Dyke questions where the money went.

Fauss wants more information to clarify what Perry previously said about rents, etc. Fauss is skeptical of what is going on and frustrated because Perry won't provide the requested information. Fauss wants to know where the $800,000 is going and the statements show $70,000 at the end of the every year but "it disappears and starts over with zero in January."

Gates said the biggest difference in what Fauss is looking at and the real cash flow is the $30,000 being paid down on the developers' fee which isn't shown in the budget. That brings it down to about $40,000 cash flow each year. What they actually had in 2001 instead of a $70,000 plus $30,000 cash flow was a $369 decrease in cash. Although a lot of numbers in the budget are similar to what the actual numbers are, they are not exactly the same. There's enough of a difference in those numbers to make up the $40,000.

Einsphar said the $800,000+ is interest on a loan that should never have been a loan.

Fauss said, "That's not my problem." The Meadow Ridge project should probably have waited then until NeighborWorks received a 501(c)(3) designation.

Wilson questioned the need for a contract if the City isn't going to follow through with the terms.

Kaspar-Beckman said the biggest problem is that elected officials need to explain to the public why the interest is being forgiven "when you didn't forgive the last one."

Stauffer said elected officials need to answer to the citizens why elected officials forgave almost $1,000,000 in interest. Elected officials need to understand the reasoning first before being able to explain it to the public, if that is the final outcome.

Einsphar agrees that the biggest problem is the public feels it was City of Norfolk tax dollars that went to build the apartments. Citizens don't understand that the money came from the Federal government and the grant was structured as a loan to benefit the tax credit partners.

Wilson said the tax credit partners don't take cash from the project but it was almost as good as cash in hand because it was used against a tax liability.

Einsphar said that, looking forward, if Meadow Ridge LLC isn't able to refinance, the City of Norfolk will never receive an interest payment or repayment of the loan. Meadow Ridge LLC can't pay back the interest or the loan and is in financial difficulty because of the interest accruing on the loan. Einsphar said there are really only two options: (a) leave the documents the same as it but the City will never receive an interest or principal payment on the loan, or (b) refinance the loan and the City has the possibility of receiving some payments on the loan.

Van Dyke has problems with the scenario. Van Dyke said Meadow Ridge LLC will only gain about $9,000 per year if the Council agrees to the refinancing. Therefore, the $935,000 will probably never be repaid to the City. The problem is how elected officials explain the issue to the general public.

Mayor said that the problem is answering to the general public even if elected officials do understand the request to refinance. However, Mayor said leadership sometimes requires elected officials to make tough decisions.

Stauffer said elected officials can probably be convinced but "now you only have 23,000 more to go."

Wilson left the meeting at 7:53 a.m.

Kaspar-Beckman said it has been said the City "may" get money in the future if the refinancing is approved. It doesn't say the City will receive money for certain.

Fauss questioned who will end up with the property if "this doesn't go through." Should the City file a lien on the property to get "our money and give it to NeighborWorks to manage".

J Paul McIntosh is involved with 168 of these types of units and, without exception, every one of them have gone bankrupt. McIntosh was reluctant to "participate in the project because of suspicions of Federal government help."

Einsphar said, however, those bankruptcies aren't a result of developers like Phil Perry but because of the government housing requirements.

Mike Renken, Board President of NeighborWorks, stated the tax partners will end up owning the property and then it will probably end up in bankruptcy. The second mortgage holder, the City of Norfolk, will then need to decide about forgiving the second mortgage, write off the $935,000 plus interest, or pay off the first mortgage. It will come to foreclosure if the interest isn't

forgiven by the City because at the end of 15 years, the managing partners have the right to pay off the tax partners but that bill is what their equity account. If the City doesn't forgive the interest, the General Partners could pay off the tax partners so NeighborWorks could own the property. However, that isn't going to happen when there is a first and second mortgage that is having difficulty with operating expenses. The City may receive the property by foreclosure, but until that time, the tax partners will get it. Renken stated, if the City approves the documents, the tax partners are giving up income—giving back their tax benefit—but they are willing to do so. Renken stated that using the cash flow statement to try to justify what payments should be made to the City is incorrect. An income statement and a cash flow statement are two completely different documents. The cash flow statement is not valid to determine what should be paid back to the City. Renken said the City has received the information through the audited financial statement that a major accounting firm has said is valid and correct.

Van Dyke said it seems that if the City would pay off the first mortgage of $2,000,000, the City would have $3,000,000 worth of property free and clear.

Nolan said the real question is where the City would get $2,000,000. Nolan said the Norfolk Area Chamber of Commerce was insistent that this project be completed in 1995 to create affordable housing. After about six months of looking for investors, the City asked J Paul McIntosh to organize a group of investors. Perry and McIntosh came up with a "mixed use" concept for the project. The initial proforma assumed build outs by the end of seven years and the developers would have their return. That was at least 11-12 years ago and less than half of the apartments are constructed because a proforma only makes assumptions of what the future is going to be. Those assumptions didn't all happen. The rest of the property can now be used for affordable single-family housing units. Nolan said the goal of providing affordable housing was accomplished and the project has benefited the community. The tax partners received a few fees but J Paul McIntosh has yet to make a profit on the project. Affordable housing is vital to the community to bring jobs to Norfolk and the surrounding area.

McIntosh said the Federal housing regulations are very complicated and, therefore, many of the housing complexes built with Federal dollars are now being demolished. McIntosh said people living in the Meadow Ridge development take pride in the area. McIntosh would hate to see the apartment complexes fall into disrepair.

Mayor Adams said the money wasn't City money and it could not have been used for any other project.

Nolan suggested the Meadow Ridge items be taken off the October 16, 2006 City Council meeting. Nolan suggested elected officials meet to discuss the audited financial statements. Nolan suggested Gates compile the information in a spreadsheet for elected officials.

Mayor Adams questioned whether the suggestion is agreeable with Fauss.

Fauss agreed with the suggestion.

Renken said Meadow Ridge LLC would like a decision by the end of October.

Saunders moved to go ahead as suggested and put a group together to look at all of the information and advise the other City Council members.

Fauss said a subcommittee needs to report back to all elected officials.

Nolan feels the discussion should be in a public meeting with all elected officials participating.

The motion died for lack of a second.

Mayor Adams suggested Finance Officer Randy Gates put a spreadsheet together so elected officials can meet in a Finance Committee meeting to review the information.

Gates said Perry indicated it will take about one week to get all the audited information together.

Saunders moved, seconded by Kaspar-Beckman to remove the Meadow Ridge items from the October 16, 2006 City Council meeting and have Finance Officer Randy Gates spread the audited financial statements and that the spreadsheet, based on the audited financial statements, is what will be brought back to the next Finance Committee meeting.

Some additional discussion occurred regarding the subject.

Saunders left the meeting at 8:24 a.m.

Gates said a simple way to look at this is that the City received the money from DED and DED recommends the City sign the documents to refinance the loan.

Kaspar-Beckman said that isn't very easy to explain to the public.

Lange said that elected officials need to make tough decisions some times. What worries Lange is that this will be drawn out enough that it will come too late and result in the apartments going into disrepair. The City "won't then have the low income housing necessary to a community". The money originally was a grant and the City was never intended to receive money back.

Roll call on the motion: Ayes: Kaspar-Beckman, Brenneman, Fauss, Lange, Stauffer, Van Dyke and Mayor. Nays: None. Absent: Saunders and Wilson. Motion carried.

Einsphar talked to Tom Huston who wants to clarify that City staff supported approval of the form of the agreement presented to the Council. Huston didn't mean to imply that staff approved the agreement itself.

Fauss said both Huston and Perry are saying contradictory statements and elected officials "get more confused".

Councilperson Fauss moved, seconded by Councilperson Stauffer to adjourn the meeting at 8:29 a.m. Roll call: Ayes: Council members Kaspar-Beckman, Brenneman, Fauss, Lange, Stauffer, Van Dyke, and Mayor Adams. Nays: None. Absent: Saunders and Wilson. Motion carried.

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Elizabeth A. Deck
City Clerk