

EXAMINATION OF THE (COSTLY) PURCHASE OF THE PROPERTY FOR THE HERNDON ART CENTER

by
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A. INTRODUCTION

Cultural Art Center is at the left, center and right of Herndon politics for more than a decade. Its idea was conceived and promoted by a former Mayor. He did not get to see his vision come true. He led the effort to purchase a site for the Center, though. A councilmember from his team took over the cause and became the Mayor. He reached a Memorandum of Understanding with a nonprofit group to help finance and build the Center by 2010, but then he lost in the next election. The next Mayor did not move the goal posts for the next six year. The current Mayor won her election with a considerable support from the Art community.

All along, a large segment of the community has felt that the concept of Art Center was forced upon them, that it would raise their taxes unnecessarily and that they would not gain much if anything from it. The business community, on the other hand, believes that an Art Center would benefit the downtown. It has now been 14 years since the property for the Center was purchased. The question many have asked is, "Why it is taking so long?" To answer this question, one must start at the very beginning.

1. Putting The Cart Before The Horse

Almost 40 years ago, a friend enquired about joining my fledging consulting company as a partner. He said that he wanted us to relocate into a higher-class building, and invest about \$35,000 in two private offices and a reception area for him. But, when we enquired about his client base, his plans for getting contracts, or about the length of time before he could start giving our investment back, he said he was not ready to answer our questions. In fact, he just wanted us to spend our money even though he was not ready to develop his consulting business.

The case of a Cultural Art Center in Herndon appears to be no different. In 2001, the then Mayor Tom Rust appointed Rick Thoesen as the Chairman of the Cultural Arts Advisory Committee II whose purpose was, in Mr. Thoesen's words, "...to create greater specificity in terms of finding a site, deliver a governance model and provide a functional analysis for a cultural arts center..." It is not clear what the underlined phrases had meant to the Committee, but one would think that the committee's first task would be to answer questions such as the following:

- What kind of art would make use of the Center?
- Were there enough artists in Town to warrant building an Art Center?

- What kind of out-of-Town artists would be invited?
- Would Elden Street Players and their Industrial Strength Theater make the Art Center their home?
- Would other Art groups in Fairfax, Loudoun and other counties use the Art Center?
- What should be the target audience for the Arts in Herndon? Will it focus on children in the community?
- Were there successful models of small town Art Centers? Could they be adapted to Herndon?
- What would be the likely capital and operating costs?
- How should the needed capital be raised?
- If the Town were to provide assistance, how should the founders of the Art Center obtain community backing?

As the following sequence of actions shows such questions had not been asked before the Town purchased the current site (called Art Spaces and located at 750 Center Street) for the Art Center in 2002; the founders did not starting asking such questions until 2005 and most issues still need to be resolved.

Late 2002 The Town purchases the property at a premium price of \$1.5 million, leases the property back to the seller for \$1 per year for a period of two years.

Mid 2003 A Town-retained architectural firm estimates that the capital costs of a cultural art center (containing a 275-seat theater) would be about \$8 million and its operating costs would be about \$250,000 per year. The firm does not mention much about parking for the patrons, but 200 parking spaces would add another \$4 million to the capital costs.¹

Oct 2004 The Town and the Foundation for the Cultural Arts negotiated a memorandum of Understanding (MOU), which contemplated the following:

- *Subject to Town appropriations* (Emphasis Added), the Town and Foundation shall provide necessary funds to complete the construction of a shell arts center from 2006 to 2008, and Town and Foundation would fund finishing out of the arts center during and after 2008 to 2010.²

¹ This estimate is at least an order of magnitude greater than the cost of the facilities used by the Elder Street Players and the Industrial Strength Theater.

² There is widespread confusion in the community about who was supposed to raise the capital necessary to build an Art Center. This paragraph is at best very confusing, because it does not set out the responsibility of the Foundation. Many believe that the Foundation was supposed to raise the funds from private sources; they often complain that its leaders have done practically nothing to raise the necessary capital. They could not possibly have raised any money. They had no product, no ideas, no artists and no plan to sell to potential donors. Folks on the conservative side believe that the Art Center should be funded strictly with private funds.

- The Foundation would manage and operate the Arts Center with a yearly financial subsidy from the Town
- The term of this MOU shall run to December 31 2014. In the absence of a negotiated renewal by a date one year prior to the scheduled expiration date this agreement will automatically be renewed for one two-year period.³

2005 *The Foundation Develops the First (Bare-Bones) “Strategic Plan”*

2008 The Foundation renovates the building and starts showing exhibits.

2009 *The Foundation Develops the Second “Strategic Plan”*

2008-Present The Foundation experiments with different types of art exhibits and performances to develop a financially viable business model for the art center. *The Foundation is currently in the process of revising the Strategic Plan.*

The emphasis is on bringing outside artists to Herndon. Very few, if any, notable artists from Herndon itself have displayed their art or participated in the programs. There aren’t too many of them in the Town. The experimentation, that is still being done today, should have been done decades ago – perhaps at a location other than the Art Spaces building. Then, and only then, the founders of the Center could have developed a clear idea about the kind of art center that could possibly be successful in Herndon. In 2002, however, the Town decided to purchase the property without first asking the kind of questions given above, and, in the process of doing so, it “put the cart before the horse”.

This is not the end of this story, however. The Town was so intent on purchasing the specific property right then and there that it exposed itself to “exploitation” (or, “price-gouging”) by the owner of the property. The report shows how the Town paid a premium price for the property.

The phrase, “*Subject to Appropriations*”, in the MOU suggests that the Art Center was going to be built primarily with Town appropriations. The then Mayor, O’Reilly, appeared to reinforce this belief during the 2004 public hearings for the MOU by remarking, “...*there is new money coming into Town that may be available to help with funding of the arts center...*” How else could the shell (of the Art Center) be constructed by 2008 and construction of the Center be completed by 2010 (as contemplated by the MOU)? During the 2004 hearings, none of the councilmembers even made a mention of the \$12 million that would be needed to construct the Center, much less address how the funds would be raised. Ten years later, the funding of the Art Center, along with many other issues remain unresolved.

³ This means the agreement shall run through December 31, 2016, unless either the Town or the Foundation terminates it by giving a 90-day notice.

2. Organization Of The Report

Section B discusses how the price was negotiated and how the Town ended up paying almost twice as much as the value estimated by the Town's appraiser and more than 3 times the Fairfax County's 2002 assessment. Among other things, it discusses the role played by the town staff in facilitating the purchase. In Section 3, the report presents selected comments to show how councilmembers supportive of the purchase justified the premium price. The section also questions the assumptions that underlie the councilmembers' comments. The lone dissenter on the council asserted that the premium price would hinder the development of the downtown. Her comments were probably politically incorrect, but in hindsight, she appears to be prophetic. In many ways, the purchase appears to have hindered the development of the downtown. Sections 4 & 5 present the past costs that the Town has incurred so far and future costs that it can expect to spend. Finally, it poses three basic questions that badly need to be asked before spending any more money.

B. BRIEF DISCUSSION OF THE PRICE NEGOTIATIONS

1. Consequences of Selecting a Single Site for the Art Center

By the end of 2001, the Town's Cultural Arts Advisory Committee had decided that the Art Center would be located at 750 Center Street even though a print shop was still operating at this location. By fixing the location, the Advisory Committee had inevitably weakened the Town's power to negotiate a lower price. The owner of the property would reject whatever offer was put on the table, take unreasonable positions, use any technique possible to force the other side to increase its offer. The Town's negotiating stance would be further compromised if it could not walk away from the purchase. The following sections show that this is exactly what happened. With the able help of an Attorney, who knew all the players well, the seller extracted a high price from the Town.

2. Initial Appraisal By The Town's Assessor

The Town retained an appraiser who had been in the business of doing real estate appraisals at the Federal, State and local level for more than 30 years. What was even better was that he had grown up in Herndon and knew the landscape well. He had easy access to people and could get the reliable information quickly.

In any appraisal, three issues are of utmost importance – the determination of the highest and best use of the property in question, selection of properties for purposes of comparison and selection of the most appropriate subset for determining the value of the subject property. Highest and best use can be defined as that use that is physically possible, appropriately supported, financially feasible, and which results in the highest land value.

Mr. Thomas Reed, the appraiser, submitted his report to the Town on May 16th, 2002. In it he stated the following:

a. Highest And Best Use

A part of the challenge for the appraiser was to determine whether the property would be developed under the CCD zoning or under the available PD-MU Zoning. Mr. Reed opined that (1) the continuation of the print shop use is acceptable for the foreseeable future, and (2) a 20,000 sq. ft. building (under the CCD zoning) along with the required 66 parking spaces represented the highest and best use of this site. He was aware of the availability of the PD-MU zoning under which, theoretically speaking, a 100,000 square foot building could be built, but chose not to mention it. Obviously, he did not think a development using the PD-MU zoning would represent the “highest and best use” of the property.

b. The First Appraised Value

Mr. Reed determined the value by comparing the sales of five real estate properties and price of a “for sale” property. Three of these properties were located in (downtown) areas with the same zoning as the subject property. He summarized his opinion as follows:

“After all necessary adjustments and considerations, it is my opinion that the subject property should fall into a value range of *something more than \$15 .00/sf up to about \$18.00/sf (emphasis added)*. I think that the land value estimate should reflect the upper limit, but if this analysis is assumed, then the building has only depreciated contributory value. My estimate is about \$20.00/sf of the base area of 6,000 sf or about \$120,000.” Accordingly, his estimate was as follows:

Land: 40,430 sf @ \$18.00/sf	= \$727,740
Estimated Contributory Value of Improvements:	= <u>\$120,000</u>
Total:	= \$847,740
Say	= \$850,000

Mr. Reed did not explain why he used the upper limit of \$18/sq. ft., but if he had used the lower limit, the land value estimate would have reduced by \$121,290 to \$606,450. Accordingly, he would have valued the property for \$726,450.

Mr. Reed also noted that Mr. Wyzkoski had purchased the subject property for a total purchase price of \$327,250 in 1994. Thus, the assessment of \$850,000 meant that the value of the property had increased at a rate of about 12.5% per year for about 8 years. A review of the selected properties suggests that property values in Herndon downtown area increased at a rate of, at best, 8% per year. Therefore, it appears that Mr. Reed should have used a figure lower than the \$18/sq. ft. for the price of land. It should also be noted that the Fairfax County had appraised the property at less than \$500,000.

Nonetheless, based on Mr. Reed's appraisal, the town made an offer of \$850,000 to Mr. Wyzkoski on July 1, 2002.

3. Seller's Response To Mr. Reed's Appraisal

In two separate letters in July 2002, the seller through his attorney, Grayson Hanes, questioned almost everything in Mr. Reed's appraisal. He took issue with Mr. Reed's determination that development under CCD zoning would represent the highest and best use of the property. He could not understand why Mr. Reed had given not even scant consideration to the PD-MU zoning. He vehemently objected to the rejection of the Closet as a comparable, because, according to him, if Mr. Reed had not done so (*and used Mr. Hanes methodology*), the subject property would be valued at \$1.8 million. Similarly, Mr. Hanes claimed that if Mr. Reed had used the Scagg's property (located next to the Closet at 847 Station Street), the subject property would have been valued at \$2.5 million. Mr. Hanes seemed to imply that large valuations were due to the availability of PD-MU zoning and that values of structures located on them should be totally ignored. Accordingly, Mr. Hanes, an attorney by trade, asserted that Mr. Reed's method for finding the appraised value was wrong. He also complained that the Town's delay in making definitive decisions about the purchase was harming his client. And, he claimed that his client had wanted to develop his property, but had put his plans on hold because he wanted to accommodate the Town.⁴ Subsequently, by a letter dated August 16, 2002, Mr. Hanes suggested that the Town had not made a bona fide offer since the offer did not reflect the best and highest use of the property, ripped apart the Town's appraisal item by item and asserted that the effect of the PD-MU zoning had to be considered. Nonetheless, Mr. Hanes made an offer of \$1.7 million.

In an earlier letter, he had offered to continue to negotiate provided two conditions were met. He asked that, "...I must have some commitment from you on behalf of the town within the next ten days that this will be done with the understanding that it is an attempt to compromise and settle a disputed matter and will not be used in any litigation between the town and my client..." (emphasis added) The second condition was particularly important because he could use any methodology and data in the negotiation and never worry about anybody cross examining his experts for the contents' validity.

It is at this stage, given wide differences between their negotiating positions, the Town could have either stopped the entire process of purchasing the property or asked the seller to submit his own appraisal.

After the Town received Mr. Hanes's letter, it asked Mr. Reed to reconsider and respond to Mr. Hanes criticism. It is not clear why the Town did not walk away from the property, because the tone of the letter suggested that the negotiations were going to be very tough.

⁴ It is worth noting that Mr. Wyzkoski was operating a printing business that may not have survived for long due to the rapidly increasing technological sophistication and consolidation in the industry. Mr. Wyzkoski probably recognized the changes and was thrilled to sell the property to the Town at a high premium. Unconfirmed reports suggest that he retired to Florida soon after selling his property.

4. Revised Appraisal By The Town's Appraiser, And Town's 2nd Offer

In response, Mr. Reed largely held his ground. He argued that:

- The market for PD-MU Zoning was very weak and supported his conclusion by giving specific examples.
- In the case of the Closet property, the building played a sizeable part in the overall transaction since it filled an immediate need by a special user.

He had not been able to get the necessary information about CITGO property earlier. After considering the new information, he was not inclined to make much adjustment, because its parking had been heavily subsidized under the Town's Shared Parking program. Nonetheless, I believe that my appraisal estimate should be adjusted as follows:

Land: 40,430 sf@ \$20.00/sf	\$808,600
Estimated Contributory Value of Improvements:	\$120,000
Total:	\$928,600

Based on this revised appraisal, the Town makes an offer of \$928,600 on September 11, 2002.

5. Seller Conducts Its Own Appraisal

There was no easy way to bridge the gap between respecting demands. The seller had confused the issue by raising as many objections as possible, but had not succeeded. As a final resort, he ordered an appraisal of his own.

It was hardly an appraisal, because it used a methodology that did not make sense. It did nothing but to reiterate what Mr. Hanes had already claimed in previous letters to the Town. It used the same two rather unusual, inapplicable and invalid criteria that Mr. Hanes had been mentioning in his letters – per square foot dirt price and per square foot FAR price - both of which gave internally inconsistent and ridiculous results for the value of the Art Space property when different properties were used as comparables.⁵ (See Section D of the Appendix) The consultant claimed that the minimum market value of the property under the CCD zoning was \$1.8 million and maximum value was \$2.5 million.

Notwithstanding all of the weaknesses in the appraisal, on Oct. 21, 2002, Mr. Hanes offers to settle for \$1.8 million. Note that Mr. Hanes increased his offer from the August 26th demand of \$1.7 million. In addition, he now asked that (1) his client be allowed to continue operating his business at the current location at for \$1 per year for 2 years and (2) the Town provide his client a letter indicating that the Town was proceeding with this purchase under its Eminent Domain

⁵ It is worth noting that Mr. Hanes had asserted (and the Town had agreed) that the appraisal could not be used in any future litigation. This means the faulty analysis could not be subject to interrogation in a court of law.

powers. By submitting his appraisal, the seller (and his attorney) had dug their heels in the negotiations and dared the Town to make a counteroffer.

6. Town Staff Gives A Strong Criticism Of Seller's Appraisal and Its Own Idea Of The Property Value

Immediately upon receiving Mr. Hanes' counter offer of \$1.8 million, the staff began to prepare a counter offer. On Oct 24th, Mr. Bibber, Director, Community Development provided a strong criticism of the seller's appraisal but he also provided what the staff thought might be supportable values.⁶ The staff indicated that the following values could be supported.

Max Value	\$1.5 million
Min Value	\$1.2 million

All the staff had done was to tweak the seller's approach for determining the assessed value. It is not clear whether the Mayor or the Council used the staff's analysis in making its next offer.

7. Town's Counteroffer, Its Acceptance By The Seller

On October 28th, the deadline set by Mr. Hanes, the Mayor, after discussing the matter with the Town Council sent a letter containing a counteroffer to Mr. Hanes. It contained the following provisions:

- A proposed contract of sale with a purchase price of \$1.5 million.
- A letter from the Town Attorney to Mr. Wyzkoski that would recite the Town's power of eminent domain, its ability to use this power to acquire land for recreational purposes, and indicate that the Town was proceeding under those powers.
- The \$1.5 million sale price includes the value for relocation expenses for Mr. Wyzkoski's business and the business of any existing or future tenants on the site. The Town will agree to a 2-year rent-back provision for \$1.00 per annum.

On November 26th, the Town Council approves the contract in a public hearing. Mr. Hanes had done a masterful job of negotiating for his client. He took full advantage of the desire on the part of the Town Council to move forward with the purchase.

C. TOWN COUNCIL'S VOTE AND COMMENTS

Before the Council voted on the resolution to approve the purchase, it asked for comments from the public. As usual, only a few people, out of the total population of about 21,000 turned out to share their thoughts with the council. The vast majority of people in the Town probably did not even know that the Art Center was on the TC's agenda. Those who knew, most likely believed

⁶ It is reasonable to assume that the staff had been given the task to develop a counter offer. One way or the other, it had to come up with something. Notice that no one on the staff was and is a professional appraiser of real estate properties.

that the purchase was going to be approved. The record suggests that it was not until Oct 2014, when the Memorandum of Understanding between the Foundation for Cultural Arts and the Town was approved, that some of the citizens spoke against the Art Center. However, on this day, no member of the public dissented during the public hearings.⁷ After hearing public comments, the Council approved the purchase of the subject property by a vote of 6-1. **The following paragraphs discuss comments of the councilmembers.**

Councilmember Hutchison was the lone dissenter. She stated that she supports the cultural arts center project and believes the property at 750 Center Street will be of benefit to the project; however, she expressed concern regarding the purchase price. She stated that the purchase price is 50 percent more than the appraised value stated in the Town's professional appraisal. She stated the inflated price "...will stifle any future development of other undeveloped parcels in the downtown, because it will raise the asking price for other properties to unrealistic levels..." *(Emphasis Added)*

Given the expectation of the approval, Ms. Hutchison's comments were probably very disappointing for many. In hindsight, however, they turned out to be true. It did not take long for downtown property owners to take notice of the high price. They started to expect far more for their properties and developer had to pay more in order to buy them. In turn, they proposed denser developments than they have would otherwise. In 2005 and 2006, the Town rejected two proposals partly because the developers and at least one property owner made excessive demands.⁸ Consequently, little or no development has taken place during the last 12 years in the downtown.

Mayor Thoesen reportedly had conceived of an art center for the Town. For him, the purchase was a small personal triumph. He hoped that, "...this is another step towards the Cultural Arts Center, which will help the Town maintain its sense of uniqueness. He seemed to genuinely believe in the Town's distinctiveness. It is reasonable to assume that he had done his best in negotiating the purchase price. Still, he felt that the Town had paid a high price and he expressed his feelings by saying, "...he wishes he could have brought the community a lower price."

Councilmember De Noyer recalled some of the past struggles and stated that "...it has been a long steady fight", and that "... this is the next big step that the Town must take in the Downtown." It is not clear what he meant by "long steady fight", but he was probably referring to the resistance from some in the community to the idea of an Art Center. Or, he may have been

⁷ Mr. Les Zidel, Kingsvale Circle, Herndon; Ms. Stacey Sinclair, VP, the Council for the Arts of Herndon, 763 Monroe Street, Herndon; Mr. Richard Schneider, 510 Alabama Drive, Herndon; Mr. Richard Downer, 609 Center Street Herndon; and Ms. Betty Hatfield, 414 Madison Forest Drive, Herndon spoke in favor of the resolution. Mr. Jim Deuel, President, Herndon Dulles Chamber of Commerce submitted a letter of support. **No one raised any questions about the high purchase price.**

⁸ The Town also bought additional properties at high prices. Lot 23C, across the street from the subject property and to the South, for example, was bought at a price of \$25/sq. ft (or about \$5/sq. ft. higher than the subject property) only 4 months after the purchase of the subject property. In other words, the town paid at least \$100,000 more than it should have.

referring to the long fight the Town had fought in developing the downtown. If he had any concerns about the high price of the purchase, he did not share them.

Councilmember O'Reilly stated he received an email from Ms Kathy East dated November 26, 2002 expressing concerns about purchasing the property and moving forward with the Cultural Arts Center at this time. Mr. O'Reilly did not explain the specific comment Ms. Kathy had made, but he expressed support for moving forward and acquiring the site. Ms. Kathy's comment, like that of Councilmember Hutchinson, in hindsight, appears to be prophetic. Given the lack of a specific business model or even a marketable "product", the purchase of the Art Center, as explained throughout this report was like putting the cart before the horse. Mr. O'Reilly, however, dismissed Ms. Kathy's comment by stating that "*he believes the cultural arts center will benefit the downtown, and will come to fruition soon...*" (Emphasis Added) We now know that the Art Center is nowhere near fruition. And, it remains to be seen whether it will benefit the Town, that is, if it comes to realization.⁹

Mr. O'Reilly also remarked that the proposed purchase price represented "fair market value" for the property. As this report shows, the purchase price represented "fair market value" only because the Town was in a hurry to buy the property – even though it was hardly prepared to use it for six more years. Therefore, the Town Council's actions, not the market, gave the property its stated value. If the Council had walked away, or pretended to do so, or had asked the seller to submit an appraisal that could be defended in court, the fair market value would have been substantially different.

In the course of commenting, Mr. O'Reilly said, "...members of Council were very concerned for weeks hoping that the negotiations would be fruitful..." The seller had sensed the Town's urgency and grabbed the opportunity to make almost \$1 million in profits and keep his businesses operating for two more years. For all his pretensions, he had no intentions of redeveloping the site under the PD-MU zoning. Had he been more daring in taking his negotiating positions, who knows how much more he may have walked away with.

It is also worth noting that Mr. O'Reilly had requested and received on June 17, 2002, a copy of the contract between the Fairfax County Redevelopment and Housing Authority and Carrhomes, Inc. under which Carrhomes, Inc. had purchased 110,673 square feet of land in the Fortnightly development for \$1.57 million, or for \$14.19/sq. ft. in Dec 2000. Fortnightly development, only a few yards away from the subject property was also zoned PD-MU. He made no mention of this low price in his comments or explained why the Town should pay such a high premium for the subject property.

⁹ It has also been asserted by many in the Town that Art Centers generate economic growth and contribute to the success of the downtown. **This assertion needs to be examined in detail.**

Discussions with some developers suggest that Art Centers generally have not been successful from a business perspective. More often than not, they need public money to survive. The Lorton Art Center in Fairfax, for example, has reportedly lost about \$16 million and the County has agreed to assume its \$30 million debt. The 2003 report for an Art Center showed that the Town would have to cover about 50% of the yearly deficit and would probably be on the hook for about \$12 millions (in 2003 dollars) in capital costs.

Councilmember Husch made a very lengthy statement and said, "...he would support the motion to procure the property, because of the guidance and direction the Town had received from its consultants and community leaders and the impact the acquisition would have on future development of the Herndon core business district..." He also did not make any comment about the price. If he thought it was unfair, he did not say. His comments seemed to suggest that he believed that the purchase was going to help downtown businesses; *however, according to some old timers in the town, it did not hurt that the seller was his friend.*

Councilmember Reece stated that the council is taking a bold step and not every resident of Herndon supports the purchase of the property, but he did not mention any specific reservations the residents had about the property. Instead, he relied on the wishes of "...most of the residents he has talked to during the past few years, support the purchase..." It should be noted that no one is against an Art Center-as-a-concept, but most people would want to know the details, including its costs and strategic plans, before giving definitive opinions.

None of the councilmembers made any comments about the timing of the construction of the Art Center, its capital & operating costs, or the startup costs. The record shows that the Foundation for the Cultural Arts was not established until 2003, the Memorandum of Understanding that put the Foundation in charge was not signed until October 2004 and strategic planning activities did not begin until 2005. Eight or so years after the first strategic plan was prepared, there is still no viable "product". Given this schedule, councilmembers couldn't have even imagined what the startup costs would be. They could have made a good faith effort though.

D. THE PAST COSTS

The Art Center related activities impose both indirect and direct costs. Direct costs are those that the Art Center imposes on the Town directly. These include utility costs and annual cultural arts grants, if any. Indirect costs are largely "invisible" costs. They include lost rent, taxes, town staff time and interest on the contributed capital. Table 1 shows that since 2002, the Town has incurred about \$5 million in start-up costs for the Art Center. They can be explained as follows:

- 1. Capital Costs:** The Town paid a total of \$1.5 million at the end of 2002 and the first quarter of 2003. In 2014 dollars, this sums amounts to about \$2.6 million. If a developer were to buy the property for redevelopment, most likely he will ask for the demolition cost of the existing building. In order words, he would pay less than the value of the land only. Fairfax county assessment records suggest that the sale should not yield more than \$1.2 million dollars in the absence of any unusual concessions by the Town. **This implies that as a result of premium price paid by the Town, it has incurred a capital loss of \$1.4 million.**
- 2. Rental Costs:** It is reported that the Foundation pays a significant amount of rent. In fact, it does not. A lease market analysis prepared for the Town in 2004 recommended that Market Lease rate should be \$12.75 per sq. ft. net. The town could have rented the

Table 1. PAST AND FUTURE COSTS OF AN ART CENTER

A. PAST COSTS

Year	Capital Costs	Over-payment for other proprietiess	Lost Rent	Lost Taxes,	Operating Costs and Grant Funds	Staff Time	Total	Present(2014) Value of Money
2002						\$75,000	\$75,000	\$134,689
2003	\$1,500,000	\$200,000	\$76,500		\$10,000	\$20,000	\$1,806,500	\$3,089,728
2004			\$78,030		\$10,200	\$20,400	\$108,630	\$176,947
2005			\$79,591		\$10,404	\$20,808	\$110,803	\$171,891
2006			\$81,182	\$5,000	\$10,612	\$21,224	\$118,019	\$174,367
2007			\$82,806	\$5,150	\$10,824	\$21,649	\$120,429	\$169,456
2008			\$84,462	\$5,305	\$11,041	\$22,082	\$122,889	\$164,683
2009			\$86,151	\$5,464	\$11,262	\$22,523	\$125,400	\$160,046
2010			\$87,874	\$5,628	\$11,487	\$22,974	\$127,963	\$155,539
2011			\$89,632	\$5,796	\$11,717	\$23,433	\$130,578	\$151,160
2012			\$91,425	\$5,970	\$11,951	\$23,902	\$133,248	\$146,906
2013			\$93,253	\$6,149	\$12,190	\$24,380	\$135,972	\$142,771
2014			\$95,118	\$6,334	\$12,434	\$24,867	\$138,753	\$138,753
TOTAL (Past Costs)								\$4,976,936
B. Future Costs								
1. Yearly Costs If Operations do not change (No Town Subsidy)							\$140,000	
2. Operating Deficits (if \$8 million Art Center is Constructed and Operating)							\$410,481	
3. Yearly debt service on the capital costs (assuming 5% interest and 20 year term)							-\$1,375,587	
4. Capital Costs, if 2003 Art Center is built								
	Building (based on 2003 Estimates)					\$13,682,715		
	Parking (say 200 Parking Spaces)					\$4,000,000		
						\$17,682,715		
4. Revenues (If Town were to sell the property to a developer) in 2014 \$s, based on FC assessment records								-\$1,200,000

One Way Forward: There are some who say that this property can be exchanged in a Public Private Partnership for an Art Center. A builder will never give the Town more than the value of the land, that is, if he is given the land free. Under these circumstances, a builder might build a 5,000 to 6,000 sf Art Center for the Town. If so, it would still need at least 20 parking spaces. The structured cost of such spaces would be about \$400,000.

space to some other tenant and realized a rent of about \$76,500 in 2002. Thus, the town bears the cost of lost rent. And, the town has lost this much rent every year since the purchase of the property.

- 3. Operating Costs and Grant Funds:** Under the 2010 lease, the Tenant (presumably the Foundation) shall maintain and pay the cost of all utilities (including telecommunications) on the leased premises. The Landlord (presumably the Town) shall equitably prorate these costs based on building square footage except (telecommunications) and then settle up fairly with the Tenant on the cost of these utilities, which Tenant shall pay on demand to Landlord. The intent of this paragraph is not clear at all.

In another clause, the Landlord shall be responsible for roof, structural integrity of the building, and replacement and repair of the utility systems related to the leased premises.

The Foundation, for the first time, applied for and received a small grant from the Town in 2012. In 2013, it received another grant believed to be \$5,000.

- 4. Lost Taxes:** The Foundation pays no taxes to the Town; if a profit making entity were to lease the space, it would pay at least professional license taxes. This report estimates that the Town has lost at least \$5,000 per year in occupational taxes alone. This sum does not include the taxes lost due to the delayed development of the downtown. It is difficult to estimate the foregone taxes, but they are likely to run into millions of dollars in some development scenario.
- 5. Staff Time:** The Town Attorney, the Town Manager, the Director of Community Development, the Community Development Staff and the administrative staff worked on this one issue over 9 or so months. If it is assumed that only one senior person worked during this period, the Town should have spent about \$75,000 in 2002.

And, the staff did not stop spending time on the Art Center matters after 2002. In 2003, it worked on issuing a contract for developing a conceptual design of an Art Center and worked closely with the selected Architect to articulate the Town's vision, develop a design and the associated operating and maintenance costs. In 2004, the staff worked on developing the Memorandum of Understanding between the Foundation and the Town and helped to get it approved by the Town Council. In 2005, the staff was bound to be busy with Art Center matters as the Foundation prepared and presented the first strategic plan to the Town Council. In 2008, the Art Spaces building was renovated and the Art Center formally opened for the public. In 2009, the strategic plan was revised and presented to the Town Council again. In 2010 the Town undertook the development and approval of the Downtown Master Plan. Once again the Town staff and its consultants spent considerable time on the Art Center and the garage. The downtown master plan matters continued to consume substantial staff time during 2011 and 2012. And, it is still on the TC agenda in 2014. Conservatively speaking, the cost of the staff consulting time was at least \$20,000 per year.

E. FUTURE COSTS

Future costs depend on our assumptions about what actions are taken in the forthcoming years. The scenarios can be summarized as follows:

- If the Cultural Arts Center remains where it is today, the Town will continue to incur about \$140,000 in direct and indirect costs plus interest costs of about \$75,000 (on the initial purchase of \$1.5 million) for a total of \$215,000.
- Finally, if an Art Center is built in accordance with the 2003 conceptual design and is able to operate in conformance with 2003 operating plan, then it will incur a yearly operating deficit of about \$400,000 and pay a yearly debt service of about \$1.38 million provided it can finance the construction. If the Town pays for the construction of the center and its parking then the deficit of \$400,000 would still need to be covered.
- If a builder develops the property, and builds a 5,000 or 6,000 sq. ft. and if we forget about the original investment and other indirect costs, and assume that the Art Center can operate without grants and/or subsidies, then the Art Center can be considered to be self supporting. The key question is, can it operate without any subsidies and can it pay back some of the original investment?

In summary, the Town has spent about \$5 million already on numerous experiments the Foundation has conducted to develop a product(s). Even though the recent management changes are encouraging, it is not certain that a definitive plan for sustainable operations can be developed in the near future. Regardless of the scenario chosen, the Town should ask the following three questions before any more money is spent or any new approach is undertaken,

1. What is the marketable product?
2. What are the milestones for attaining sustainable operations?
3. How much more money would be spent before achieving financially sustainable operations?