FINANCIAL FEASIBILITY REVIEW OF YAKIMA CONVENTION CENTER EXPANSION

Prepared for:

Washington State Department of Commerce

November 2019

E. D. Hovee & Company, LLC

Economic and Development Services

Financial Feasibility Review of Yakima Convention Center Expansion

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Note: Cover exterior rendering is courtesy of the Yakima Regional Public Facilities District.

AT-A-GLANCE SUMMARY

The Yakima Regional Public Facilities District (District) is planning to construct an 18,500+ square foot expansion to the Yakima Convention Center (YCC) and refund existing debt – funded by issuance of $16 million in new bonded indebtedness. In accordance with state statute, the economic and development consulting firm E. D. Hovee & Company, LLC has prepared this independent feasibility review for the Washington Department of Commerce on behalf of the District. Key findings of this report follow.

YCC Expansion Capital Cost & Funding. Based on cost estimates provided by the District, the expansion cost involves hard construction cost of $9.3 million together with $3.2 million in associated soft costs – for a total maximum allowable construction cost of $12.5 million. A limited tax general obligation (LTGO) bond is anticipated to be issued in the amount of $16.0 million – to cover construction cost plus the refunding of $3.5 million in remaining indebtedness from a prior 2007 bond issue.

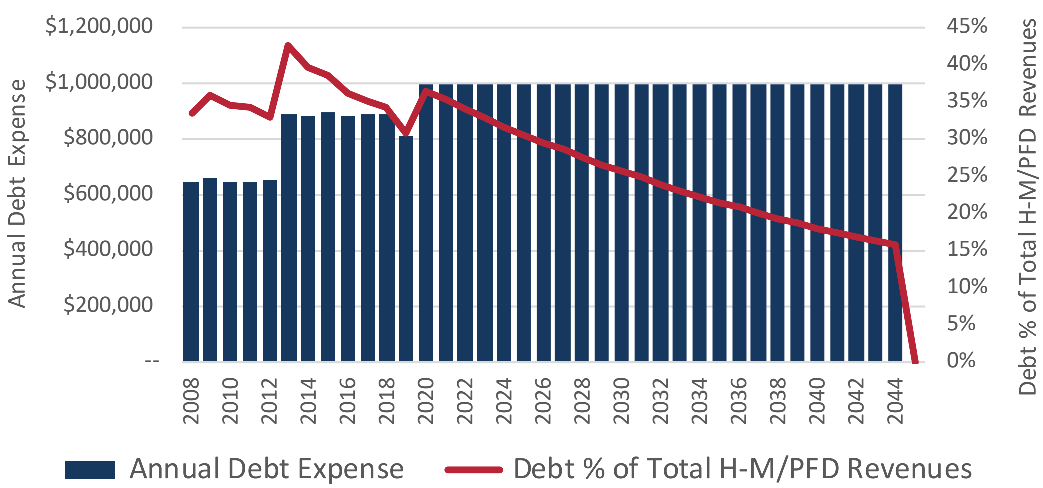
Bond payments are preliminarily estimated at $991,973 per year, assuming repayment over 25 years at an annual interest rate of 3.7%. While the project schedule is not fully determined, it is anticipated that construction may begin as early as spring 2020 with completion targeted for 12 months thereafter.

Feasibility of Issuing New Debt. Two sources of revenue allocated, in part, to repay debt are the City of Yakima Hotel-Motel (H-M) tax and PFD sales tax credit receipts – together totaling about $2.579 million as of 2018. These revenues are currently allocated to pay existing bonded indebtedness at an amount of $883,360 as of 2018 – albeit with some year-to-year variation. Debt payments will increase by close to an added $110,000 per year with the new debt schedule, replacing current bond payments.

In addition to paying debt, a combination of H-M and PFD funds are also allocated to pay for support of convention center and Capitol Theater operations, tourism promotion and on-going YCC capital improvements. As of 2018, H-M/PFD revenues exceeded all allocated expenses by close to $213,000, allowing management flexibility or discretion in application of surplus funds. From 2002-18, combined revenues have increased at an average rate of 3.6% per year. The combination of H-M and PFD funding has provided a more stable revenue flow than would be the case with reliance on just a single source.

New bonding would increase debt service payments to 36% of combined H-M and PFD revenues initially, then drop back to 16% of combined revenues just before debt retirement, as shown by the graph below.

Historic & Forecast Debt Service vis-à-vis H-M/PFD Revenues (2008-45)



Bottom line, this review demonstrates that, with *base case* conditions, there should be more than ample lodging and PFD tax revenue available over a planned 25-year repayment schedule, assuming that debt payments take first priority with the allocation of these revenues. Also assumed is that, even with ups and downs of the business cycle, economic conditions supporting these revenues streams do not materially change from what has been historically experienced.

The District forecasts that with the planned addition, H-M/PFD tax revenues will increase to just over $3 million after completion (by about 2022-23) – termed for this report as *base case* conditions. With more conservative *stress test* conditions, annual revenues could decline to about $2.4 million. This would reduce but not eliminate the current surplus assuming continuation of existing commitments that include debt payments together with convention center/Capitol Theater operations, tourism promotion and on-going capital improvements funding support. However, projected revenues in a stress test scenario likely would not be adequate to also fund anticipated debt coverage or reserves.

Operating Sustainability. The District projects that *base case* revenues and expenses will both increase with the Addition, resulting in a break-even operating position. Under *stress test* conditions, an annual deficit in the range of $100,000 - $200,000+ could materialize. Unless facility revenues were increased or expenses curtailed, on-going deficits could require added funds from H-M/PFD sources, reducing what is available for debt service/coverage, promotion and/or capital improvements.

Project Risks & Mitigation. As illustrated by the following chart, four potential categories of project risk are identified with this review – construction, debt financing, operating and institutional risk. Also listed are potential options that might be considered to mitigate these risks.

Type of Risk	Potential Sources	Options for Mitigation
Construction risk – if YCC expansion project costs increase above the $12.5 million budget	• Unforeseen cost • Inflation • Construction disruption and/or delay • Post-construction issues	• Warranty coverage • Value engineering • Added bonded debt • PFD reserves • Yakima General Fund financial backstop
Debt risk – as with increased cost, economic downturn, and/or debt coverage requirement	• Increased cost of debt service • Economic downturn • Debt coverage requirement	• Set funding priorities pre- debt issuance • H-M/PFD 1st priority to repay debt • City of Yakima credit enhancement • Reduced bond amount • Added up-front reserve set-aside
Operating risk – as with weak facility use and/or greater than anticipated expense	• Weak facility utilization • Greater-than-expected operating cost	• Grow out of deficit w/interim funding • Reduce YCC/Theater operating support • Reduce tourism/capital fund support
Institutional risk – with multiple cities in the PFD & need to update interjurisdictional roles	• Extension of YCC lease • Unclear priorities to remedy potential funding shortfalls	• Extend lease to cover term of new debt • New intergovernmental agreement with mutually agreed H-M/PFD fund priorities

These risks are addressable with PFD/City of Yakima action. Most important is the need for a clear policy of H-M/PFD revenue allocation in the event of shortfall, *first* to debt repayment and coverage, *second* to YCC operating cost, *third* to tourism/Capitol Theater and capital expense.

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I. INTRODUCTION

The Yakima Regional Public Facilities District (YRPFD or District) is planning to construct an 18,500+ square foot expansion to the Yakima Convention Center (YCC) at a total cost estimated at $12.5 million. Combined with refunding of $3.5 million of 2007 bonds, the District is proposing to issue $16 million of new bonded indebtedness.

PURPOSE OF INDEPENDENT FEASIBILITY REVIEW

The economic and development consulting firm E. D. Hovee & Company, LLC has been retained by the Washington State Department of Commerce (Commerce) to conduct an "independent feasibility review" for Commerce on behalf of the District, pursuant to RCW 35.57.025.

The purpose of the review is to examine the potential costs and the adequacy of revenues or expected revenues to meet the costs to be incurred by the District. As directed by state statute, the preparer of this report is to exercise independent professional judgment in conducting the financial feasibility review.

STATE OF WASHINGTON ROLE & STATUTORY AUTHORITY

As enacted by the 2012 Washington State Legislature, RCW 35.57.025 requires that:

> (1) An independent financial feasibility review under this section is required to be performed prior to any of the following events:
>
> > (a) The formation of a public facilities district under this chapter;
> > (b) The issuance of any indebtedness, excluding the issuance of obligations to refund or replace such indebtedness, by a public facilities district under this chapter; or
> > (c) The long-term lease, purchase, or development of a facility under RCW 35.57.020.
>
> (2) The independent financial feasibility review required by this section must be conducted by the department of commerce through the municipal research and services center under RCW 43.110.030 or under a contract with another entity under the authority of RCW 43.110.080. The review must examine the potential costs to be incurred by the public facility [facilities] district and the adequacy of revenues or expected revenues to meet those costs. The cost of the independent financial feasibility review must be borne by the public facility [facilities] district or the local government proposing to form a public facility [facilities] district.
>
> (3) The independent financial feasibility review, upon completion, must be a public document and must be submitted to the governor, the state treasurer, the state auditor, the public facility [facilities] district and participating local political subdivisions, and appropriate committees of the legislature.

This evaluation is being prepared pursuant to sections (1)(b)-(c) of the above noted statute.

DISTRICT HISTORY & AUTHORITY

The Yakima Regional Public Facilities District was formed in 2001 for the immediate purpose of an estimated $10 million expansion of the Yakima Convention Center. District formation was put in place via an Interlocal Cooperation Agreement established between the cities of Yakima, Selah and Union Gap in 2001. Limited Tax General Obligation (LTGO) bonds were issued by the City of Yakima in 2002 for Phase III of a Convention Center expansion and remodel – with work completed over the 2002-03 time period. This $6.7 million project effectively doubled the size of the convention center.[1]

In 2004, bonds were issued in the amount of $4.175 million to refund initial 1996 YCC bonding. In 2007, the City approved issuance of added LTGO bonds – of which $4.91 million was allocated to the convention center for refunding of the 2002 issue.[2]

Based on a credit review by the rating firm Standard and Poor's, the city received an "A" credit rating with a stable outlook. An additional tax rebate was awarded to the District in 2008 to fund the 4th Street Theatre addition to the Capitol Theatre.

Documents important to understanding the relationship between the regional PFD and the three cities as PFD participants include the initial 2001 interlocal agreement and subsequent City of Yakima resolution detailing PFD involvement in expansion funding for the city-owned convention center. Each of these is briefly summarized, in turn.

Interlocal Agreement

The 2001 Interlocal Cooperation Agreement between the Cities of Yakima, Selah and Union Gap to form a multi-city public facilities district occurred for the purposes of assisting in the:

> … financing, development, and operation of, regional convention center facilities; stimulating economic development by creating jobs, realizing additional sales tax and lodging tax revenues and attracting commercial business and tourism; and providing facilities for community events including public meetings and performing arts events.

The immediate purpose was to finance an expansion of the Yakima Convention Center. The City transferred a leasehold interest in the convention center and underlying site to the District. In return, the newly created District agreed to sublease the Convention Center and underlying site to the City of Yakima, with the City of Yakima taking responsibility to design, develop, construct, operate and maintain the facility. The City of Yakima reserved the right retain all revenues of the convention center. Other provisions of the interlocal agreement included:

- Authorization for the City of Yakima to issue bonds for convention center expansion.
- Agreement for the District to have powers typically available to a PFD by state statute as for taxing authority including sales tax credit from the state for the convention center or other Regional Center projects (subject to City of Yakima approval) and to issue District general obligation or revenue bonds.

- Agreement for the City of Yakima to contribute lodging taxes for convention center operations/maintenance and make up any shortfall in the event of a PFD Sales Tax shortfall – coupled with the understanding that the Cities of Union Gap and Selah have no responsibility to the District in the event of a Sales Tax shortfall.
- Provisions for potential future dissolution of the District once there is no longer bonded indebtedness, with all assets or property of the District vesting with the City of Yakima.

City of Yakima Resolution

Also in 2001 and subsequent to the Interlocal Agreement, the City of Yakima (by Resolution 2001-102) approved a 25-year lease of the convention center to the Yakima Regional PFD and approved an agreement between the City and PFD for the purpose of financing, operating and maintaining the convention center. Key provisions of these agreements included:

- The District's pledge of sales tax receipts to the City to "pay debt service on the bonds and other Project costs."
- City pledge to contribute lodging taxes to the District in amounts annually determined to the Convention Center including revenues in the event of a Sales Tax shortfall.
- Authorizing a 25-year lease of the convention center to the PFD, assigning the responsibility for design, development and construction of YCC expansion to the City, and establishing a sublease of the center from the PFD to the City with City responsibility for operation and maintenance.

Also noted at the time with the City Council Agenda Statement of June 19, 2001 was recognition that "to make the financing plan work, the Convention Center may have to temporarily reduce operating expenditures and/or non-operating expenditures such as promotional expenses." This confirms the implied if not explicit priority that debt repayment would have over other uses of City hotel-motel tax and PFD sales tax funding allocations – a matter of significance for this independent feasibility review.

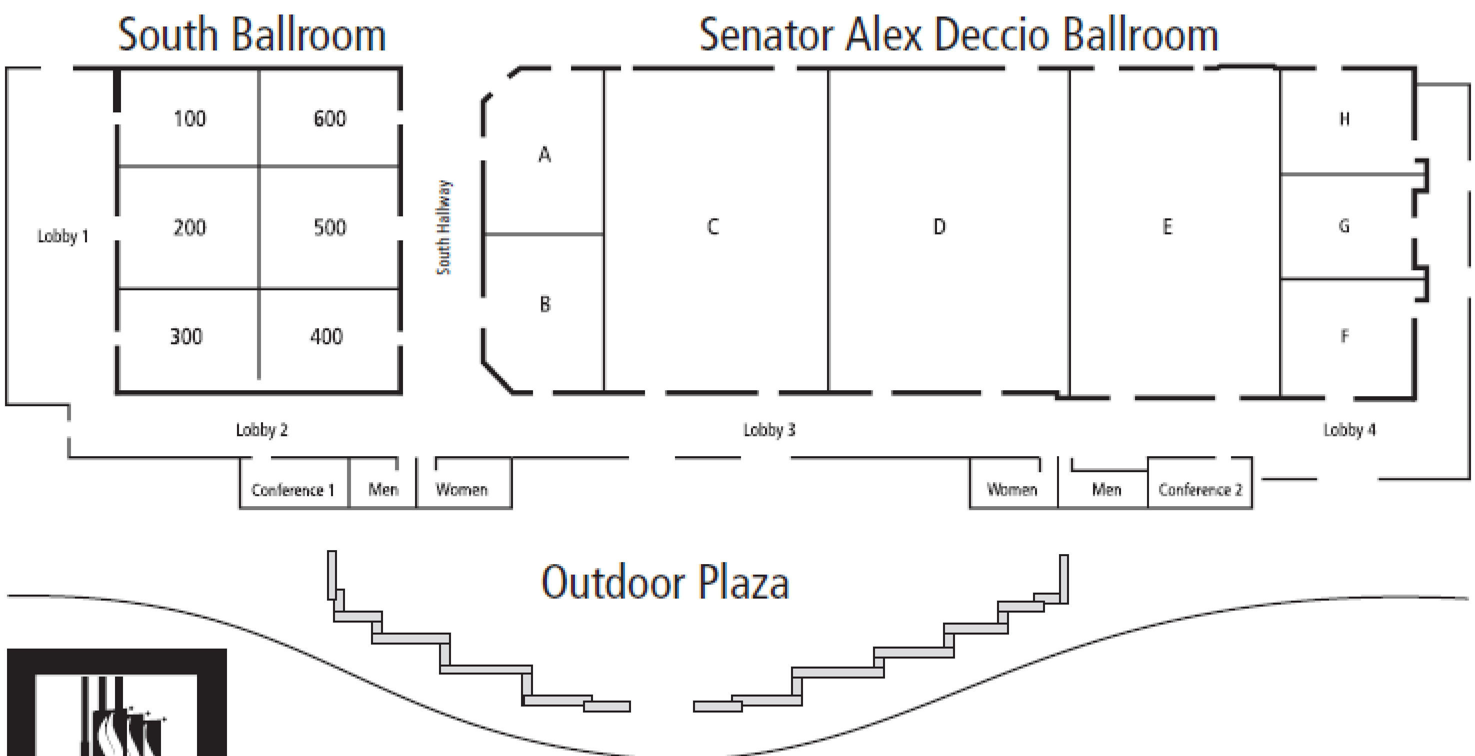
THE YAKIMA CONVENTION CENTER & PLANNED EXPANSION

As described by its web site and illustrated by the current floor plan on the following page, the Yakima Convention Center features an estimated 41,000 square feet of versatile, column-free space plus a 7,000 square foot outdoor plaza.[3] The facility is designed as multi-purpose space with the ballrooms serving meal, meeting and/or exhibit functions as the occasion requires.

Expansion Plan

With expansion, spaces shown as F, G and H on the current floor plan will be replaced by a combined designation F of approximately 5,163 square feet. A new mirror G space of 5,055 square feet will be extended out from the existing reconfigured F space. Three meeting rooms will also be added as rooms H, I and J with 1,130, 1,144 and 1,129 square feet respectively – together with an extended lobby.

Current Yakima Convention Center Floor Plan



YAKIMA CONVENTION CENTER

10 North 8th Street
Yakima, WA 98901

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800.221.0751

YakimaCenter.com
meetings@yakimacenter.com

Capacity

Suite/Room	Square Footage	Dimensions	Theater Seating	Class Seating	Banquet Seating	Standing Reception	Exhibits
South Ballroom (Suites 100-600)	6,000	90x66	400	220	360	600	36
100 - 300 (Each)	900	29x31	70	32	50	100	6
400 - 600 (Each)	1,080	30x36	85	40	50	125	6
Conference Room 1	340	20x17x10		Boardroom seating for 10			
Lobby 1 and 2	5,600						18

	Square Footage	Dimensions	Theater Seating	Class Seating	Banquet Seating	Standing Reception	Exhibits
Deccio Ballroom (Rooms A–H)	23,568	23x90x259	2,250	925	1,600	3,300	157
A and B (Each)	1,575	45x35x15	150	60	90	225	8
C	5,580	90x62x15	545	220	360	800	38
D	5,850	90x65x15	545	220	360	800	38
E	5,612	92x61x23	545	220	360	800	38
F–H (Each)	1,080	30x36x23	100	45	70	150	6
Conference Room 2	459	27x17x10		Boardroom Seating for 12			
Lobby 3 and 4	6,000						28
Outdoor Plaza	7,000				360	500	

The combined effect of the expansion will be to maintain the existing functional and flexible space configuration of the convention center by extending the existing structure – as depicted by the following illustrative.

Bird's Eye View of Existing & Expanded Yakima Convention Center

Source: Yakima Regional Public Facilities District. Rose colored shading indicates the proposed addition.

The expansion will comprise an estimated 18,566 square feet of gross building area. Rentable ballroom and meeting space affected (including renovated space) is estimated at 15,436 square feet – including 1,815 square feet provided by converting three existing meeting rooms to a single larger ballroom/meeting space (with existing corridor removed). Net added rentable space is estimated at 10,273 square feet.

Expansion Purposes

As stated in public information provided by the convention center, YCC serves as a place for convening by local groups and visitors – also supporting jobs, added spending and tax revenue community-wide.[4] A major reason for the expansion is that the center has lost conferences to other cities due to increasingly insufficient convention meeting space and availability. An expanded center is expected to increase utilization and community benefits in the years ahead.

ANALYSIS APPROACH

This analysis has been prepared for Commerce by the independent economic and development consulting firm E. D. Hovee & Company, LLC (E. D. Hovee).[5] A brief profile of the firm as report preparer is provided by Appendix A.

Documents Reviewed

A listing of documents reviewed as part of this independent feasibility study is provided by Appendix B to this report. Included are documents as initially provided by Commerce and YRPFD at the outset of this assignment together with other materials obtained during the course of this review.

No additional independent document research has been conducted for this assignment, outside of materials provided via Commerce, information already available to E. D. Hovee, and any added information provided as a result of follow-up with Commerce and the YRPFD. The assistance of Commerce and the District with provision of background information, follow-up to questions, and review of draft report documentation is greatly appreciated.

Methodology Overview

A major focus of this report is to review the project's capital cost and related documentation. This is followed by a review of the sources and adequacy of revenues to meet debt service requirements – including a baseline scenario consistent with District provided projections followed by stress test scenarios to assess potential vulnerability to weaker-than-expected facility financial performance and/or slower local/regional economic growth.

Also reviewed is the adequacy of existing agreements related to capital and operating funding between the YRPFD and its funding and operating partners. Both the debt financing and overall feasibility reviews are accompanied by consideration of project and operating risks including measures that might be considered for mitigation or added financial backstop, as appropriate.

The Yakima Regional PFD has stated that it does not have a municipal advisor so no letter from an Independent Registered Municipal Advisor (IRMA) is indicated at this time.

Report Organization

The remainder of this report is organized to cover the following topics:

- **YCC expansion capital cost and funding** – including a review of the expansion budget, project management and capital funding
- **Feasibility of issuing new indebtedness** – addressing lodging tax and PFD revenue resources and capacity to support new debt
- **Operating sustainability** – focused on base case and stress test operating scenarios for YCC and associated implications for debt funding capacity
- **Project risks & mitigation** – addressing construction, debt and operating risks

Included with the report are two appendices – providing a profile of E. D. Hovee & Company, LLC as project preparer and listing of documents reviewed.

II. YCC EXPANSION CAPITAL COST & FUNDING

As stipulated by RCW 36.100.025 (2), the independent financial feasibility review must examine the potential costs to be incurred by the public facilities district. This section of the report addresses:

- **Expansion budget** – including hard construction costs and associated soft costs for the project as estimated for the District and City of Yakima by ALSC Architects, P.S.
- **Project management** – addressing responsibilities to completion of the expansion project including scheduling and addressing potential disruption during construction.
- **Capital funding** – considering sources and uses of funds for the expansion project together with refunding of outstanding bonded indebtedness.

Each of these topics is considered, in turn.

EXPANSION BUDGET

As prepared, the budget for the YCC expansion project has two parts:

- **Hard construction costs** – including building and site costs for an estimated maximum allowable construction cost of $9.3 million.
- **Associated soft costs** – including furniture, fixtures and equipment (FF&E), fees, miscellaneous project costs and architect/engineering fees (A&E) which together total approximately $3.2 million.

Detailed cost estimating information is provided on the following two pages. Taken together, total cost associated with convention center expansion as currently proposed is $12.5 million.

The hard construction budget is quite recent – estimated as of June 26, 2019. The soft cost budget is more dated, having been prepared in June 2018.

The hard construction cost budget includes design contingencies of 8%. The soft cost budget includes a general owner contingency of 5%. Alternative improvements are also included as part of the $9.3 million MACC – allowing for lobby enclosure, additional audio-visual equipment, an additional operable partition, and additional overhead door. It is assumed that these alternates could be excluded if other project costs prove to be higher than expected.

While both the hard and soft cost schedules are quite detailed, it is not clear to what extent the estimates account for inflation extending from the date of estimate preparation to the date when construction starts and then to project completion.

YCC Expansion Hard Construction Cost Budget

#	Description	Cost/SF	Cost Allocation	
A10	Foundations	$14.92		
	Slab on Grade	$7.64	$141,844	
	Footings/Foundations	$7.28	$135,160	
A20	Basement Construction	$0.30	$5,570	
810	Superstructure	$28.00	$519,848	
820	Exterior Enclosure	$42.74		
	Studs		$62,900	
	CMU @ Storage		$85,800	
	Insulation		$34,600	
	Skylights		$29,260	
	Storefront		$180,000	
	Retractable Entrance Doors		$80,000	
	Brick Veneer		$123,000	
	Stucco		$115,000	
	Gabian Blocks		$8,000	
	Flag Poles relocate, trellis, soffit		$25,000	
	Sheathing, flashing. Coping, joints		$45,000	
	HM Man Doors		$5,000	
830	Roofing	$7.95	$145,469	
C10	Interior construction	$20.33		
	Stud Walls		$78,000	
	CMU @ Storage/3-hr		$95,000	
	GWB		$37,600	
	Man doors		$28,500	
	Storefront Glass Inside Vestibule		$11,100	
	Ceilings-ACP		$15,400	
	Cei1ings-GWB		$15,200	
	Ceilinos - Wood Slat		$45,000	
	Wall Sound Attenuation		$29,600	
	Signate		$10,000	
	Misc: CG's, transitions, chairrails		$12,000	
C20	Stairs	--	--	
C30	Interior finishes	$46.20		
	Replace Carpet in Existing Building		$440,000	
	VWC		$50,000	
	Thin Brick Veneer		$12,300	
	Wall Paint		$8,600	
	Wall Tiles - Feature		$45,000	
	Wall Tile - Restrooms		$30,600	
	New Carpet in Addition		$215,000	
	Entry Mats		$15,000	

YCC Expansion Hard Construction Cost Budget (continued)

#	Description	Cost/SF	Cost Allocation	
	Floor Tile		$15,500	
	Sealed Concrete Slab		$5,000	
	Wall Base		$3,000	
	Ceiling Paint		$17,800	
010	Conveving Svs terns	--	--	
020	Plumbing	$10.55	$195,782	
	Toilet Room Accessories		$35,000	
030	HVAC	$39.45	$732,429	
040	Fire Protection	$5.00	$92,830	
050	Electrical	$43.50	$807,621	
F20	Building Demolition	allowance	$80,000	
E20	Casework	$0.27	$5,000	
F10	Speciall Construction	$56.86		
	3-hr Wall in Existing Building		$165,000	
	3-hr doors		$70,000	
	Movable Partitions		$241,200	
	Glass Partitions		$188,500	
	OH Doors		$45,920	
	A/V Systems		$345,008	
	Subtotal: Building		**$5,980,941**	
	Design Contingency 8%		$478,475	
	Total : Building	**$347.92**		**$6,459,416**
F20	Demo/Temporary Relocation Costs		$30,000	
G10	Site Preparation		$73,000	
G20	Site Improvements		$135,000	
G30	Site Civil/ Mech Utilities		$125,000	
G40	Site Electrical Utilities		--	
G50	Other Site costs		$160,000	
	Sub-Total: Site Design Contingency 8% Total-Site			
	Design Contingency 8%		$523,000	
	Design Contingency 8%		$41,840	
	Total - Site			**$564,840**
210	General requirements 10%		$930,000	
	GC Overhead/Profit 15%		$1,036,641	
	MACC Total	**$484.27**		**$8,990,897**
MACC Budget:			**$9,300,000**	
Possible Alternates				
Lobby enclosure			--	
Additional AV Equipment		allowance	$100,000	
Additional Operable Partition@ G			$100,800	
Additional OH Door West Wall			$15,680	
Subtotal Alternates:			$216,480	
Total MACC + Alternates:				**$9,207,377**

Source: ALSC Architects, P. S., as of June 26, 2019.

YCC Expansion Associated Soft Cost & Total Budget

Description		Estimate
Other Fees		
	Predesign Fee	$25,000
	Commissioning Agent	$30,000
	Construction Management	$50,000
	Reimbursable Expenses	$10,000
	Construction Testing & Special Insptections	$37,768
	Site Surveys	$15,000
	Soils Analysis	$9,000
	Air Barrier Leakage Testing	$7,000
FF&E		
	Furniture & Furnishings	$219,000
	Major Equipment	$151,071
	IT Equipment	$150,000
	IT Cabling	$32,375
	Audio Visual	$600,000
	Security Access Control	$80,000
	Washington State Sales Tax (8.2%)	$101,061
Contingencies:		
	General Owner Contingency (5%)	$377,677
Miscellaneous Project Costs		
	Plan Review Fee	$13,516
	Building Permits	--
	Land Use Application Supmbittal Fee	$1,200
	Zoning Approvals	$10,000
	Utility Fees - Cit Connections	$10,000
	Utility Fees - Power	$15,000
	Utility Fees - Natural Gas	$5,000
	Legal & Accountying Fees	--
	Insurance	$15,107
	Signage & Graphics	$10,000
Maximum A&E Fees (Per State Fee Schedule)		$1,221,000
Total Soft Costs		**$3,195,775**
	Rounded to	**$3,200,000**
Total Hard Cost (MACC)		**$9,300,000**
Total Expansion Project Cost Estimate		**$12,500,000**

Source: ALSC Architects, P. S., from KDF Feasibility Study, as of July 2018.

Project Management

Questions of project schedule and associated potential for disruption during construction represent key underpinnings of the project and appropriate mitigation with risk management.

Expansion Schedule

As of August 2019, the project schedule is not fully determined. Architectural and engineering design has been underway starting in April 2019 with schematic design, moving to design development, with construction documentation indicated as being prepared over the summer of this year.

Based on the project going to bid in late September and with bid opening scheduled for October, the PFD and City of Yakima have anticipated awarding a construction bid in November 2019. Once the general contractor is selected, a more precise construction time frame will be determined.

Some utility work will need to be completed prior to actual construction. Weather permitting, it is understood that the contractor might choose to do this portion of the work prior to actual ground-breaking in early spring 2020 for construction.

The duration of construction is expected to take approximately 12 months – with an expanded convention center opening in the spring of 2021.

Disruption During Construction

The Yakima Convention Center will continue operations through the approximate 12-month duration of construction – accommodating on-going convention activity as booked for the center. The most pronounced area of potential impact will be at the north end of the building – in rooms now referred to as F, G, and H (see earlier floor plan).

While there is potential for groups to cancel meetings and other events due to construction, facility management will be working closely with clients and local partners to minimize this potential risk.

Construction and equipment staging will occur on existing city-owned land. Consequently, little to no direct adverse impact is expected to neighboring properties. Potential impact to facility parking over the duration of construction is less clear based on information received.

YCC notes that the center has already expanded three times over the last 23 years. Past construction activities have been viewed by the center as successful at mitigating interruptions for guests and clients. Existing staff has been through previous expansions, providing knowledge as to potential impacts and how they were addressed in the past – allowing for "successful events throughout construction."

Capital Funding

This discussion begins by summarizing sources and uses of anticipated project funding. This is followed by review of anticipated repayment of existing bonded debt.

Sources & Uses

As shown by the chart to the right, the sole **source of funds** is anticipated be $16 million of new bonded indebtedness issued by the City of Yakima.

Sources & Uses of YCC Expansion Funding

Description	Amount	Comments
Sources of Funds		
Total Bond Amount	$16,000,000	City issued LTGO bonds
Uses of Funds		
Hard Cost Budget	$9,300,000	MACC Budget 6-26-19
Expansion Soft Cost	$3,200,000	As estimated July 2018
Refunding of 2007 Bonds	$3,500,000	Remaining principal & interest
Total Uses	$16,000,000	

Note: Schedule is preliminary and subject to change.

Source: YRPFD.

Uses of funds are proposed to include the $12.5 million cost of the expansion as the sum of $9.3 million maximum allowable construction cost (MACC) and $3.2 million estimated soft cost – plus refunding of existing indebtedness from a 2007 bond issue (for an estimated $3.5 million). While not fully determined, the PFD indicates that a debt service coverage ratio in the range of 1.25-1.50 could be required with this debt issue – a topic discussed further with Sections III and V to this report.

Repayment of Existing Bonded Indebtedness

The City of Yakima has issued limited tax general obligation (LTGO) bonds for the Yakima Convention Center dating back to original facility construction in 1996. Over time, earlier debt issues have been replaced as the result of bond re-funding. Currently two convention center related bonds are outstanding:

- **A 2004 LTGO bond in the amount of $4.175 million to refund 1996 convention center bonds.** Recent debt service payments have been in the range of $425,000 - $440,000 per year. Repayment funding is from the City of Yakima H-M tax; a last payment of $349,070 is scheduled for November 1, 2019, effectively retiring this debt.
- **A 2007 LTGO bond in the amount of $4.910 million with refunding of an earlier 2002 issue for convention center expansion in 2002-03.** Repayment funding is from the PFD. Debt service payments vary from about $455,000 - $462,000 per year. The scheduled 2019 payment is just under $460,000, with final annual payment set for 2026.

With the recent May 1, 2019 principal payment, the remaining balance on existing 2007 LTGO debt would be $2.77 million. The next scheduled date for a principal (and interest) payment would be May 1, 2020 – when the remaining payment including accrued interest (if calculated to May 1, 2020) would be less than $2.9 million. This would appear to provide room to support some or all of the bond issuance costs that may also be covered within the $3.5 million figure currently budgeted (although specific estimates of issuance costs have not been provided).

Convention Center Expansion Debt Scenario

Depicted by the following chart is a potential debt scenario for amortizing $16 million in new bonded indebtedness.

YCC Expansion Debt Scenario

Year	Beginning Balance	Payment	Interest	Principal	Ending Balance
1	$16,000,000	($991,973)	($592,000)	($399,973)	$15,600,027
2	$15,600,027	($991,973)	($577,201)	($414,772)	$15,185,254
3	$15,185,254	($991,973)	($561,854)	($430,119)	$14,755,135
4	$14,755,135	($991,973)	($545,940)	($446,033)	$14,309,102
5	$14,309,102	($991,973)	($529,437)	($462,537)	$13,846,565
6	$13,846,565	($991,973)	($512,323)	($479,651)	$13,366,915
7	$13,366,915	($991,973)	($494,576)	($497,398)	$12,869,517
8	$12,869,517	($991,973)	($476,172)	($515,801)	$12,353,716
9	$12,353,716	($991,973)	($457,087)	($534,886)	$11,818,830
10	$11,818,830	($991,973)	($437,297)	($554,677)	$11,264,153
11	$11,264,153	($991,973)	($416,774)	($575,200)	$10,688,953
12	$10,688,953	($991,973)	($395,491)	($596,482)	$10,092,471
13	$10,092,471	($991,973)	($373,421)	($618,552)	$9,473,919
14	$9,473,919	($991,973)	($350,535)	($641,438)	$8,832,481
15	$8,832,481	($991,973)	($326,802)	($665,172)	$8,167,309
16	$8,167,309	($991,973)	($302,190)	($689,783)	$7,477,526
17	$7,477,526	($991,973)	($276,668)	($715,305)	$6,762,221
18	$6,762,221	($991,973)	($250,202)	($741,771)	$6,020,450
19	$6,020,450	($991,973)	($222,757)	($769,217)	$5,251,233
20	$5,251,233	($991,973)	($194,296)	($797,678)	$4,453,556
21	$4,453,556	($991,973)	($164,782)	($827,192)	$3,626,364
22	$3,626,364	($991,973)	($134,175)	($857,798)	$2,768,566
23	$2,768,566	($991,973)	($102,437)	($889,536)	$1,879,029
24	$1,879,029	($991,973)	($69,524)	($922,449)	$956,580
25	$956,580	($991,973)	($35,393)	($956,580)	$0
Total				**($16,000,000)**	

Source: YRPFD, as of August 2019

As noted, this schedule assumes equal annual payments of just under $992,000 per year over 25 years at an assumed annual interest rate of 3.70%. These estimates are subject to refinement based on underwriting and market conditions up to the date of issuance.

III. FEASIBILITY OF ISSUING NEW INDEBTEDNESS

The feasibility of issuing new bonded debt is dependent on demonstrating adequacy of resources to replace the existing debt and also to finance convention center expansion. As has been historically the case for the Yakima Convention Center, sources of debt repayment have been limited to hotel-motel tax revenues received by the City of Yakima and sales tax credit revenue received by the Yakima Regional Public Facilities District.

The key question addressed with this review is: **Will lodging tax and PFD tax revenues prove adequate to pay the new debt plus other on-going uses to which these tax revenues are allocated?**

This review starts with a history of these two tax revenue sources together with other uses to which the revenues are allocated. This is followed by consideration of repayment capacity under base case and stress test conditions of current and on-going tax revenue resources.

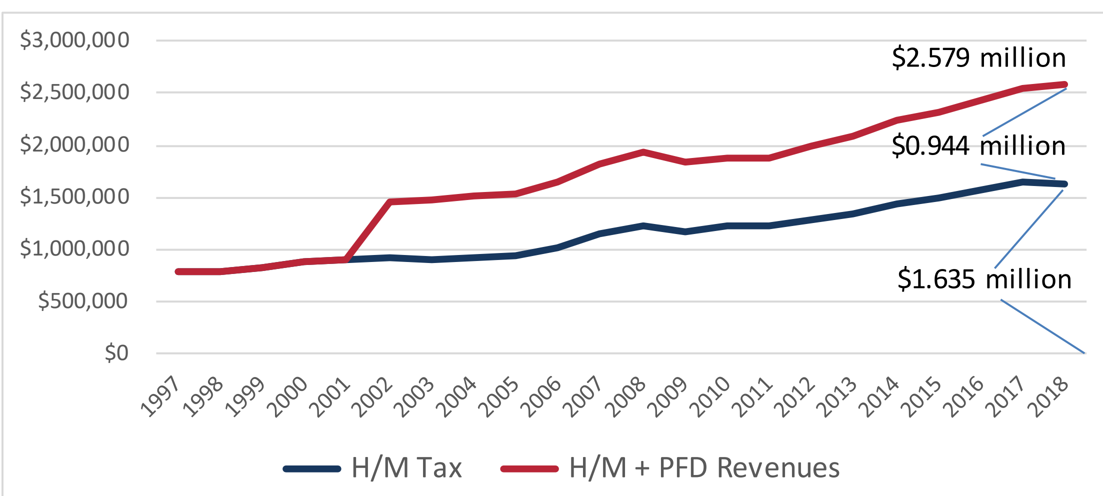
Lodging Tax & PFD Revenue Resources

The two revenue resources that have been available for convention center debt funding are:

- **City of Yakima hotel/motel tax revenues** – at 5% total including 2% state credit against the state retail sales tax and 3% local option lodging tax revenues.
- **Yakima Regional Public Facilities District sales tax credit** – available to eligible PFDs at a rate of 0.033% credit against the Washington State sales tax from within the District.

As shown, combined revenues have reached a total of $2.579 million as of 2018, with $1.635 million from hotel/motel and $0.944 million from PFD sales tax credit revenues.

Yakima Lodging Tax and PFD Revenue History (1977 – 2018)



Source: YRPFD.

As illustrated by the foregoing chart, PFD sales tax credit revenues did not become available to the Yakima Regional PFD until 2002. From 2002-18, combined revenues have increased at a compound annual growth rate of 3.6% - with a slightly higher growth rate for hotel/motel than PFD revenues. Hotel/motel revenues tend to fluctuate more than PFD sales tax revenues, but together provide a more stable revenue flow than would otherwise be the case.

Over this time frame, there has been only one year of declining revenues – from 2008-09 with a combined drop of just over $91,500. This demonstrates relative stability of underlying funding capacity from the two revenue sources on a sustained basis. Over this full 16-year time frame, combined revenues have increased by an average of nearly $70,000 per year.

Revenue gains were well below average in the recessionary period experienced from 2008-11. From 2012-17, revenues increased by an average of over $110,000 per year – but then increased by less than $40,000 in the most recent year from 2017-18. Whether this is an early sign of potential economic slowdown or a one-year deviation is uncertain at present.

Lodging Tax & PFD Revenue Capacity to Support Debt

With a new $16 million bond issue, annual debt payments can be expected to increase by about 11-13% -- from a range of $880,000 - $890,000 per year paid from 2014-18 to just under $992,000 annually over a future 25-year repayment period. This equates to a debt service increase of over $100,000 per year.

The question of whether and to what degree existing lodging tax and PFD revenues will prove adequate to support the added debt is addressed in three steps:

- Comparison of debt service to annual lodging tax and PFD revenues – both currently and in the future.
- More detailed consideration of other uses for which lodging tax and PFD revenues are currently allocated.
- Stress test evaluation of conditions that conceivably might affect repayment capacity – both short- and long-term.

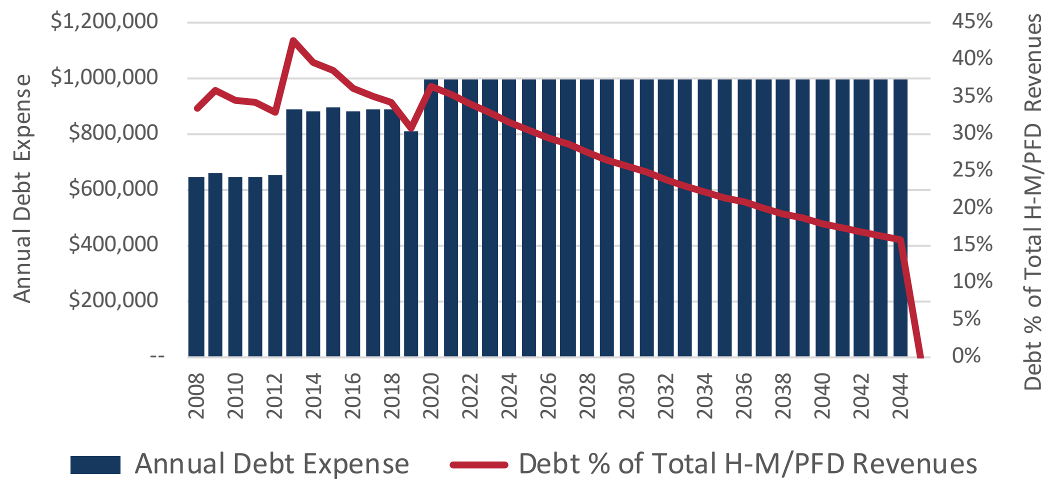
Debt Service as a Share of Lodging Tax & PFD Revenue

Based on current and projected debt and as illustrated by the graph on the following page:

- Scheduled debt service payments (shown by the solid bars) went from about $646,000 per year in 2008 to the $880,000 - $890,000 range in recent years. Debt service will increase further to nearly $992,000 per year with the proposed bond refunding and new issue.
- As a share of all hotel-motel and PFD revenue (shown by the line), debt service peaked at about 43% of combined lodging/PFD tax revenues in 2013, dropping to 31% as of 2019.

- Going forward, the new debt issue can be expected to increase debt service payments initially to about 36% of combined lodging and PFD tax revenues in 2020. However, if these revenue sources continue to increase at historic rates, debt service would drop back to 16% of combined total H-M tax/PFD revenue capacity just before debt retirement in 25 years (or by 2044-45 depending on when new debt is issued).

Historic & Forecast Debt Service vis-à-vis H-M/PFD Revenues (2008-45)



Notes: Historic scheduled debt payments as provided by the YRPFD (and shown above) do not fully coincide with budgeted bond funding allocations. Additional payment may be paid so as to build reserves. From 2010-18, annual payments of $428,000 have been budgeted and shown as expenditures annually, although bond scheduled payments have varied from year-to-year.

With payment on a new $16 million, 25-year bond assumed to occur first in 2020, the subsequent decline in bond payments as a share of available revenues assumes continued average annual growth in combined H-M/PFD revenues to occur at a combined rate of 3.61% per year per base case conditions.

Source: YRPFD.

In effect, discretionary income can be expected to increase in the latter years of debt repayment. This should provide flexibility for added capital improvements, convention center operating or tourism promotion funding support, even before the new indebtedness is fully repaid.

Bottom line, this review demonstrates that there should be more than ample lodging and PFD tax revenue available over a planned 25-year repayment schedule assuming that debt payments take first priority with the allocation of these revenues as are currently made. This assumes that, even with ups and downs of the business cycle, economic conditions supporting these revenues streams do not materially change from what has been historically experienced.

H/M & PFD Funding Allocations

The full range of uses for which hotel-motel and PFD fund allocations are currently made (per Yakima City/PFD funds) involve:

- Fund 170 – City allocation to Tourist Promotion Operations (including both operation of the Yakima Convention Center and general tourism promotion)
- Fund 171 – City allocation to Capitol Theater Operations
- Fund 287 – City allocation for its share of debt repayment with the initial 1996 bond as refinanced in 2004 and with payments extending through 2019
- Fund 370 – City allocation to Convention Center capital expense
- Fund 172 – with PFD payments for debt service per a 2007 LTGO bond issue and miscellaneous operating expense as well as for transfers to the City/YCC for convention center operating and capital accounts.

DEBT FUNDING CAPACITY WITH BASE CASE & ALTERNATIVE SCENARIOS

This independent feasibility report involves review of debt funding capacity pursuant to:

- **Base Case Scenario** – utilizing revenue-expense projections as provided by the District.
- **Two Alternative Stress Test Scenarios** – with both Stress Tests 1 and 2 reflecting more conservative projections of H-M and PFD sales tax growth than with the base case and with Stress Test 2 also reflecting higher expenditure levels than Stress Test 1.

Line item results associated with base and stress test scenarios are shown by the chart on the following page.

Base Case & Stress Test H-M/PFD Allocation Scenarios with YCC Addition

Description	2018 Actuals	2022 w/Addition		
		Base Case	Stress Test 1	Stress Test 2
H-M Tax & PFD Revenues				
H-M Tax Revenue	$1,635,225	$1,919,216	$1,528,401	$1,528,401
PFD Sales Tax Credit	$943,863	$1,107,784	$892,844	$892,844
Total Revenues	**$2,579,088**	**$3,027,000**	**$2,421,245**	**$2,421,245**
Allocation by Fund				
H-M Fund Allocations:				
170 Tourist Promo/Ops from H-M	$745,000	$930,996	$755,000	$930,996
171 Capitol Theatre Operations	$205,570	$205,570	$205,570	$205,570
287 Debt Service	$428,000	$485,973	$485,973	$485,973
370 Convention Center Capital	$256,655	$296,677	$81,858	($94,137)
Subtotal H-M Fund Allocations	$1,635,225	$1,919,216	$1,528,401	$1,528,401
172 PFD Fund Allocations:				
Convention Center Operating	$100,000	$161,612	$100,000	$161,612
Convention Center Debt	$463,213	$506,000	$506,000	$506,000
Convention Center Capital	$155,000	$155,000	$155,000	$155,000
Miscellaneous Expense	$13,583	$15,000	$15,000	$15,000
PFD Net Income/Surplus	$212,067	$270,172	$116,844	$55,232
Subtotal PFD Fund Allocations	$943,863	$1,107,784	$892,844	$892,844
Total Allocations	**$2,579,088**	**$3,027,000**	**$2,421,245**	**$2,421,245**
Debt Coverage				
H-M Plus PFD Debt Service	$891,213	$991,973	$991,973	$991,973
H-M Plus PFD Revenue/Debt Ratio	2.89	3.05	2.44	2.44
Uncommited Revenue/Debt Ratio	1.24	1.27	1.12	1.06

Notes: Base case scenario is based on City and PFD budgeted amounts and assumes that stabilized utilization with YCC expansion may be achieved within about two years after completion (or by 2022-23). Stress Tests 1 and 2 both assume lower revenue growth than the base case; Stress Test 2 also assumes higher end expenses.
In the event of temporary account shortfalls, funding could be drawn from existing reserves (with a balance in excess of $1 million as of year-end 2018). This indicates ability to draw from the fund balance should revenues drop and capital expenditures still be required over and above debt service and operations.
Source: YRPFD and E. D. Hovee. Scenarios are for illustrative purposes only.

Base Case Review

With the base case scenario, total lodging and PFD revenues would increase by approximately 17% from 2018-22 (with 2022 or 2023 as a potential target stabilized year after opening of the expanded convention center). Key allocation items reflect the PFD-prepared "Addition" scenario – one of two primary scenarios provided by the District. This scenario is based largely on expense and income adjustments consistent with proportionate expansion of the convention center (as further described in the operating sustainability section of this report).

This base case scenario indicates that even with projected increases in debt service and tourist promotion/YCC operations funding that there should be a surplus of funds if not otherwise expended. If this turns out to be the case, it could provide opportunity to increase support for the 171 Capitol Theater funds that are otherwise expected to be held constant at historically experience levels. Alternatively, excess funding could be applied to on-going annual capital improvements and/or to build reserves for future facility improvements.

With base case conditions, the annual PFD net surplus as of 2022 would be about $58,000 more than realized in 2018. It is also noted that much of the impetus for healthy financial outcomes is linked to an assumption of continued H-M tax and PFD sales tax credit revenues increasing at rates experienced historically. "With addition" revenues (as of about 2022-23) could be nearly $450,000 more than in 2018. In effect, this revenue growth makes possible a projected 2022 net City/PFD funding surplus – consistent with current fund accounting.

When viewed as the ratio of all hotel-motel (H-M) plus PFD sales tax credit receipts *divided by* projected debt service with a new bond issue, the resulting debt service coverage ratio (DSCR) would increase from 2.89 (as of 2018) to 3.05 by about 2022. However, when viewed from the standpoint of revenue not committed for other purposes (including support of convention center and theater operations, on-going YCC capital improvements, and PFD miscellaneous expense), debt coverage appears far less favorable – increasing somewhat from 1.24 times *free revenues* as of 2018 to 1.27 by 2022.

While a specific DSCR formula has yet to be determined, financial input to District staff indicates that required coverage is likely to be in the range of 1.25-1.50. The uncommitted revenue DSCR calculation is above the 1.25 threshold but well below a 1.50 ratio – though this might still prove adequate if all non-debt uses of H-M and PFD funds are subordinated to debt payment. In effect, the precise determination and application of a DSCR mechanism may prove pivotal even with base case expectations as currently projected by the District.

Base case financial outcomes also depend on positive economic growth regionally – especially over about the next five years. In the event of a significant recession, this apparent financial surplus could disappear quickly. The facility is more vulnerable to this type of downturn near term than in the later years of debt repayment. Continued economic and associated revenue growth through the mid-2020s would provide a more solid *cushion* to lessen the impact of a recession that occurred later rather than sooner in the coming decade.

Alternative Stress Test Scenarios

Two stress test scenarios are aimed to identify conditions that might reasonably occur in the event of less favorable economic and facility utilization circumstances:

- **Stress Test 1** assumes flat revenues through 2021 followed by a severe recession in 2022 (with percentage declines in H-M and PFD revenues as experienced in 2009 – followed by subsequent recovery). This stress test also assumes that tourist promotion, convention center and Capitol Theater operations support are held to 2018 levels rather than increased as with the base case. Convention center capital allocations are calculated as a residual (i.e., as the different between H-M tax revenue *minus* the sum of H-M allocations for promotion/YCC operations, Capitol Theater operations and debt service).

The result is that the overall H-M plus PFD revenue to debt ratio falls from 3.05 with the base case to 2.44 with this first stress test. However, when considered in terms of revenues already committed for non-debt purposes, the unencumbered coverage factor drops from 1.27 with base case conditions to 1.12 (below anticipated coverage requirements).

- **Stress Test 2** is predicated on the same H-M and PDF revenue assumptions as Stress Test 1 but also assumes that that tourist promotion, convention center and Capitol Theater operations funding support increases to the same levels as with the base case. This could occur if operating support proves difficult to be curtailed, at least in the near term. This stress test is no different from the first stress scenario when the coverage factor is measured based on total H-M plus PFD sales tax credit revenue divided by debt service.

  However, when calculated after deducting for non-debt fund uses, unencumbered revenue available for debt service drops to a DSCR of just 1.06. When adjusted for negative convention center capital contribution (i.e., requiring some withdrawal of reserve funds), effective coverage drops to 0.96 meaning that planned allocations cannot be fully covered by available 2022 revenues. This potentially results in a negative H-M cash flow in the range of $100,000 per year as of stabilized utilization.

Both stress tests indicate that while the capacity of the PFD and City of Yakima to fund debt may be challenged under adverse conditions, payment capacity should remain intact provided that reserves or other funding resources prove adequate to offset what would most likely prove to be a short-term deficit. As noted, convention center reserves show a balance in excess of $1 million as of year-end 2018, providing capacity to fund at least temporary funding shortfalls.

For repayment capacity to be more seriously challenged, an economic downturn more serious than that of the Great Recession of the last decade would be required. Alternatively, repayment capacity also could be challenged if other allocations – as for tourism promotion, convention center and Capitol Theater operations – increase by more than currently projected.

The size of the financial gap to be addressed could further increase if operating expenses outpace revenues – as described with discussion of Section IV Operating Sustainability which now follows.

IV. OPERATING SUSTAINABILITY

Preceding sections of this independent feasibility review have focused on the financial feasibility of the District issuing new indebtedness. This section broadens the scope to cover potential effects of convention center expansion on operating income and expense together with resulting implications for capacity to support debt repayment. As with debt capacity, this operating review includes consideration of base case and alternative operating scenarios.

BASE CASE & ALTERNATIVE OPERATING SCENARIOS

This independent feasibility report involves review of income-expense impacts pursuant to:

- **Base Case Scenario** – utilizing YCC revenue-expense projections as provided by the District covering the time just prior and then subsequent to completion of the Addition.
- **Two Alternative Stress Test Scenarios** – with Stress Test 1 reflecting a conservative YCRPFD projection to 2022 consistent with prior YCC expansion experience and Stress Test 2 also adding in the higher operating expense projections of the base case.

Line item results associated with base and stress test scenarios are shown by the chart below.

Base Case & Stress Test Operating Scenarios with YCC Addition

Description	2018 Actual	2022 w/Addition		
		Base Case	Stress Test 1	Stress Test 2
Revenue				
Meeting Room Rent	$305,990	$497,761	$422,042	$422,042
Miscellaneous	$202,611	$201,334	$267,404	$267,404
Catering	$326,632	$369,549	$420,000	$420,000
PFD Transfer	$100,000	$161,612	$80,000	$80,000
Interest	$50	$97	$50	$50
Hotel/Motel Tax	$730,392	$930,996	$755,000	$755,000
Subtotal	$1,665,675	$2,161,349	$1,944,496	$1,944,496
Beginning Balance	$418,410	$557,061	$557,065	$557,065
Total Revenues	**$2,084,085**	**$2,718,410**	**$2,501,561**	**$2,501,561**
Expenses				
Tourist Promotion Fund	$444,098	$523,801	$468,000	$523,801
Center Management	$1,230,544	$1,634,891	$1,567,227	$1,634,891
Total	**$1,674,642**	**$2,158,692**	**$2,035,227**	**$2,158,692**
Net Income	**$409,443**	**$559,718**	**$466,334**	**$342,869**
Net w/o Beginning Balance	($8,967)	$2,657	($90,731)	($214,196)

Note: Net income is shown with and without the beginning balance included, as detailed below.

Source: YRPFD for Base Case and Stress Test 1, E. D. Hovee for Stress Test 2.
Scenarios are for illustrative purposes only.

Base Case Operating Scenario

A preliminary operating pro forma has been provided as one possible scenario by the District (termed for purposes of this review as a base case operating scenario). The chart on the previous page compares 2018 experience with what is assumed to be a stabilized year of operations post-expansion (assumed to occur by about 2022 or 2023).

With the base case scenario, total revenues increase by a projected 30% with the Addition. Expenses are projected to increase by about 29% - with net income (including the effects of the beginning balance) increased by over $150,000 in this five-year period.

There are two primary drivers of this base case operating scenario:

- A key assumption is that operating income and expenses will increase in line with the increase in key portions of newly constructed net rentable space within the expanded facility.
- This percentage increase is applied to the average of revenue/expenditures (by line item) as experienced over the five years of 2013-2017.

The City/PFD accounting is somewhat unusual in that a beginning balance (based on prior year results) is included in the calculation of annual income rather than being shown as a change in net position.

By including the beginning balance, net income is shown as an estimated $409,000+ for 2018, increasing to a figure approaching $560,000 with stabilized annual use of the facility with completion of the new addition. If the effects of beginning balance are excluded, the resulting net operating income figure for 2018 is reduced from positive net income over $409,000 to an annualized deficit of about $9,000. The *with addition* base case result goes from a positive net income of $560,000 to less than $3,000 as of 2022.

In effect, the YCC net profit margin has been extremely narrow in recent years (with some years showing a small operating loss). In the absence of a strong reserve balance to carry forward, there would be years where the convention center could readily slip from small surplus to operating deficit.

Alternative Stress Test Scenarios

The District also prepared an alternative scenario for 2022 (the year after opening), based on different operating assumptions. With this approach, the years 2019-2021 are lumped into one category with the YRPFD projection. Anticipated is that during these years of construction activity, operating income and expenses likely will remain relatively flat.

In projecting numbers for 2022, a couple of different approaches were considered. The PFD looked at the past 21 years of operation, then at the years following each expansion. For example:

- With the initial 1996-97 expansion – the years 1998-2001 were looked at for percentage of increases/trends, etc.
- With the more recent 2002-03 expansion – the years 2004-07 were looked at separately for the percentage of increases/trends, etc.

The PFD then took some averages of those four years and applied this average experience to projections of future revenue growth, adding in some adjustments based on past experience. A similar approach was then applied to projection of expenses.

The result of this forecast approach (indicated as **Stress Test 1**) is weaker financial performance post-expansion. Year 2022 revenue would be forecast at $2.502 million and expenses projected at $2.035 million – for net income of about $466,000.

If the beginning balance figure of $557,000 is excluded from the actual annual operating income, the 2022 result calculates out to a loss of $91,000 for 2022. If this pattern of operating loss were extrapolated forward, the result would be a negative balance within about 6-7 years.

The conclusion of the PFD is that this scenario "did not calculate out in a reasonable manner."[6] It was largely for this reason that the District went with the base case approach described above, based on square footage coupled with the more recent 5-year history of YCC operations.

An even more conservative approach would be to replace the somewhat lower expense projections of Stress Test 1 with the higher expense forecast associated with the District's base case scenario. The result (with what is termed as **Stress Test 2**) is that net income would be reduced by another $123,000. If the beginning balance is not included, this means that the Year 2022 operating deficit is potentially increased from just over $90,000 with Stress Test 1 to a deficit of $214,000 with Stress Test 2.

IMPLICATIONS FOR SUSTAINABLE OPERATIONS & DEBT REPAYMENT

On balance, the District's selection of the square footage approach appears reasonable as a base case scenario. However, this review also indicates a very real risk or potential downside associated with more conservative stress test scenarios:

- With the **base case scenario,** the expanded facility would be operating at about break-even – assuming continued H-M tax and PFD support as currently projected by the District. There is not much margin for error though financial results could improve post-2022 if the expansion continues to gain traction with added convention activity.
- With the **stress test scenarios,** YCC could be in a deficit position by 2022 of $100,000 - $200,000 or more per year. If not remedied via stronger revenue increases and/or expense reductions, higher levels of H-M and/or PFD funding support for YCC operations could be required, reducing funds available for tourism and Capitol Theater operations, capital improvements, and/or debt service (including debt coverage). Potential risks and options for mitigation are considered with the next (final) section to this report.

V. PROJECT RISKS & MITIGATION

Reviewed with this final section of the financial feasibility report are risks related to construction and related expense, debt financing and repayment, expanded facility operations, and institutional arrangements. Each of these potential risks is considered, in turn, together with potential options for risk mitigation.

CONSTRUCTION RISK

Risks potentially associated with project construction primarily involve the potential for the construction cost to exceed the project budget – from any or some combination of several possible sources.

As in any construction project, there is some risk that project costs could exceed the current budget. This risk is mitigated by a detailed construction and soft cost budget including a maximum allowable construction cost (MACC) budget of $9.3 million together with line item detail of $3.2 million in soft costs – leading to a $12.5 million total project cost estimate (increased by $3.5 million to $16.0 million with bond refunding).

The construction budget includes contingency allocations – including 8% design and total site contingencies, together with 5% general owner contingency. All-inclusive project costs of $12.5 million averaged over 18,566 square feet of expansion area works out to a figure of $673 per square foot. This compares to an approximately $650 - $660 per square foot figure for the Spokane Convention Center expansion completed in 2015 and an estimate of close to $1,000 per square foot figure for the Washington State Convention Center expansion project currently under construction in Seattle. [7]

Nonetheless, construction cost could end up exceeding current budget, particularly due to factors such as:

- **Unforeseen costs becoming apparent during the course of construction** – which could require change orders.
- **Inflation increasing beyond what is built into the cost estimate** – by the time of actual construction; somewhat unclear is if the current cost estimate has been escalated through the duration of construction (as part of the June 2019 estimate).
- **Construction disruption or delay –** that could extend the project timeline or require mitigation to address needs of on-going meeting and convention activity.
- **Post-construction issues** – if needed to remedy design or construction flaws.

Options for Mitigation. The District and City of Yakima have multiple options that might be considered in the event of construction costs substantially exceeding current estimates. These include any or some combination of measures such as:

- Assuring adequate contractor and vendor warranty coverage – to the extent available and as negotiated with construction contract(s).
- Value engineering to scale back and delete or defer some project items, for example, approximately $216,480 of identified alternates as for additional audio-visual equipment, operable partition and overhead door.
- Increasing the size of the bond issue (if not already completed) and/or issue supplemental debt – to the extent supported by anticipated revenues for debt repayment and associated coverage requirements.
- Using available PFD reserves estimated at a 2018 year ending balance of over $1 million – to the extent that reserve funds are not otherwise encumbered.
- If needed, drawing on City general fund resources as a last-resort backstop to fund construction cost overruns.

DEBT FINANCING RISK

Debt financing risks that conceivably could affect project feasibility and/or debt repayment capacity include:

- **Impaired capacity or increased cost of debt financing** – as could occur if bonds prove less marketable or affected by higher interest rates, a shorter term and less favorable payment structure, or higher debt service coverage ratios than currently expected.

  An item of potential concern is with the downgrading of the Standard & Poor's (S&P) LTGO bond rating to A+ from AA- in 2017. The rating could be improved in the future should "recent economic development in the city contribute to increasing income levels, and should the city strengthen its ending reserve to levels we (S&P) consider at least strong."[8]
- **Economic downturn** – would have the most adverse effect on debt service funding capacity if a significant recession were to unfold in the near-term (between about 2020 and 2025). The risk is not so much with making annual debt payments as scheduled but of covering this responsibility plus added debt service coverage together with other on-going uses of City H-M tax and PFD sales tax revenues.
- **Debt coverage management** – could prove problematic even if the City and PFD has adequate funding to make debt and other existing payments from H-M/PFD resources but if determined to be not adequate to also cover the anticipated DSCR anticipated to be in the range of 1.25-1.50 times actual debt service. Depending on bond covenants associated with debt issuance, the City and PFD could be put in the position of having to divert resources to maintain adequate reserves before funding non-debt related uses of H-M/PFD revenues. This could result in reduced funding available for tourist promotion, YCC and Capitol Theater operating support, and/or on-going capital improvements.

Options for Mitigation. Options associated with debt financing risk might be addressed or otherwise mitigated through such measures as:

- Clear specification of City/PFD funding mechanisms, accounting and monitoring for debt service coverage prior to debt issuance.
- Binding agreements or covenants to prioritize debt and associated debt reserves or coverage requirements ahead of other uses of H-M/PFD funding, i.e., ahead of tourism promotion, convention center and Capitol Theater operations, and on-going convention center capital improvements funding.
- Reduced impact of debt coverage requirements if coverage or reserves are not limited to H-M/PFD sources but can be otherwise addressed as by City credit enhancements allowing for reduced/eliminated H-M/PFD coverage.
- Reducing the size of the currently planned $16 million bond issue at time of underwriting if terms of financing prove to be less favorable than currently anticipated.
- Potential set aside of additional temporary up-front reserves adequate to meet bond requirements and/or withstand a recession event through at least 2025.

OPERATING RISK

Operation risks of potential consequence are essentially two-fold:

- **Weak facility utilization** – as might happen if facility use and associated revenues do not increase to the extent anticipated with base case conditions (which assume that revenues increase roughly proportional to the net added rentable ballroom and meeting space). Marketability may be influenced by off- as well as on-site factors such as a relatively older supporting hotel inventory than is the case with other comparable convention center facilities regionally – a condition that may change with addition of two new hotels providing added room inventory.[9] As with funding capacity to repay debt, operating revenues may also be affected by changing economic conditions, particularly with potential for economic recession between now and 2025.
- **Greater than anticipated operating expense** – which could occur if on-going expenses increase more than currently projected (indicated with base case conditions as increasing in proportion with net building space added). Consistent with experience of prior YCC expansions, there can be a tendency for convention facilities to ramp up expenses in anticipation of more convention activity than actually materializes, leading to a need for subsequent expense reduction or right-sizing.

As an alternative scenario, the District forecasts year 2022 revenues and expenses consistent with experience after earlier 1996-97 and 2002-03 YCC expansions. What is termed as Stress Test 1 results in the convention center going from break-even with base case conditions to a 2022 operating deficit of $90,000+. If expenses associated with the base case also increase (as with Stress Test 2), the 2022 projected deficit would more than double to over $214,000. Based on experience with expansions of other convention centers, it is possible that deficits could build even more quickly – if expenses are not better matched to realized revenue growth.[10]

If not curtailed, future year operating deficits in the range of $100,000 - $200,000+ per year would affect not only operating sustainability – but also potentially affect debt repayment and reserves as less funding might become available for other uses of H-M/PFD funds including on-going promotion/YCC and Capitol Theater operations, and YCC capital improvement funding.

Options for Mitigation. Options potentially available for consideration to assure operating sustainability without impairing debt repayment include the following:

- Grow out of any substantial financial issue even if YCC operations require higher levels of operating support from H-M tax and PFD revenues initially as the expanded facility transitions to fully stabilized performance. This might occur, for example, if H-M tax and PFD revenues increase more rapidly (for example at the 4.3% rate per year experienced from 2013-18) versus YCC expenditures which have been increasing at the slower rate of 3.2% per year over this same recent time period.
- Right-size YCC and/or Capitol Theater incremental operating expenses to a level that can be sustainably supported by incremental revenues received – in the event that incremental H-M tax and/or PFD support is not achievable to the level anticipated to fully support facility operations.
- In the event that neither of the two above approaches prove to be adequate to offset facility deficits, make added reductions to other discretionary uses of H-M tax and PFD revenues – notably tourism promotion and/or capital improvement allocations in a manner that does not impair debt repayment capacity.

In any event, it may be appropriate for the District and City to consider formalizing a clear *waterfall* or prioritization of H-M tax and PFD revenue allocations – as with first priority to debt repayment and associated coverage requirements, second priority to covering YCC operating support, and third priority to tourism promotion and on-going support for Capitol Theater operating plus YCC on-going capital improvements funding.

INSTITUTIONAL RISK

As described at the outset of this report, the joint relationship and responsibilities among the District and the Cities of Yakima, Selah and Union Gap were established by an Interlocal Cooperation Agreement dating to 2001. As the principal parties to PFD funding and operations, the relationship between the City of Yakima and the District was further articulated by City of Yakima Resolution (2001-102), also implemented in 2001 following approval of the initial Interlocal Cooperation Agreement.

While the creation of this institutional relationship was occasioned by the need to proceed with near-term (2002-03) financing and construction, these two documents also set in place the framework for subsequent funding, construction/expansion, operation and maintenance of the Yakima Convention Center – including the two most recent bond issues of 2004 and 2007.

There is no specific time limit set for the duration over which these arrangements will be maintained as originally agreed. However, the interlocal agreement does provide for termination prior to repayment of bonds by action of the Yakima City Council.

At such time as there is no remaining bonded indebtedness, the District might be terminated by mutual agreement of the City Councils of the three founding cities. Alternatively and after bonds have been repaid, one or two of the parties may withdraw from the 2001 agreement. Dissolution is not to occur until "proper provision has been made for disposition of all District assets."

However, the City of Yakima lease of the Convention Center authorized by 2001 resolution was for a 25-year term, assumed to expire about 2026. The most recent 2007 financing provided for bond repayment over a 20-year time frame, with final bond payments to be made in 2026. The current proposed bond issue for $16 million is planned to be for 25 years – which could carry to about 2044-45 (depending on when the debt is issued).

Public agencies pivotal to successful debt financing, project expansion, and on-going operations are the District and the City of Yakima. Even in a two-party arrangement, misunderstandings may arise that adversely affect on-going project sustainability. Reliance on older agreements that have not been updated to reflect current and prospective conditions poses two risks of potential significance to the three forming cities (particularly Yakima) and the District:

- **Provision to extend the existing lease of the YCC facility** – from the City to the District beyond what appears to be the current 2026 expiration date. From a financing perspective and consistent with the interests of all parties, it would appear that the lease would need to be extended for a term that is equal to or greater than the 25-year term of planned new LTGO bonding.
- **Unclear interjurisdictional priorities and responsibilities to remedy any potential YCC weak financial performance** – that could jeopardize bond repayment, coverage and/or operating sustainability. The PFD remains as a three-city entity for purposes of PFD sales tax revenues but with facility ownership and management a responsibility of the City of Yakima. Also unclear is the question of whether and how future dissolution of the District might occur – once all bonded indebtedness is repaid.

  Legal documents associated with a 2001 City of Yakima resolution do articulate a City responsibility to make up any deficiency in funding to repay bonded indebtedness. The existing interlocal agreement states that "the City of Yakima will also be solely responsible to contribute revenues in the case of a Sales Tax shortfall." However, the existing documentation does not appear to clearly outline mutually agreed priorities for spending of Yakima's H-M tax and PFD revenue in the event that revenues do not prove adequate to fund all current and anticipated uses of these funds, whether short- or long-term.

Options for Mitigation. Steps to take to address these risks in advance rather than when a major issue emerges could include the creation of new or amended agreements to:

- Extend the facility lease term to cover at least the full period of anticipated additional bonding for YCC expansion.
- Provide a clear statement of funding priorities and responsibilities in the application of City of Yakima H-M taxes and PFD revenues – with *first priority* to debt repayment and coverage requirements (as applicable), *second priority* to fully funding YCC operating expense, *third priority* to tourism promotion, on-going Capitol Theater operating support, and YCC capital improvements, and possible *fourth priority* to other as yet unfunded eligible uses to the extent that excess revenues may be available now or in the future.

Ideally, these additional provisions could be made via a new or supplemental interlocal agreement prior to issuance of additional debt.

APPENDIX A. PREPARER PROFILE

This independent feasibility review has been conducted on behalf of the Washington State Department of Commerce for the Yakima Public Facilities District by the economic and development consulting firm E. D. Hovee & Company, LLC (E. D. Hovee).

Since 1984, E. D. Hovee has provided consulting services for a wide range of public agency, non-profit and private clients primarily, though not exclusively, in the Pacific Northwest states of Washington, Oregon and Idaho. Assignments conducted have included market and feasibility studies, economic impact analyses, due diligence reviews, and strategic business development planning – covering a diverse set of industrial, commercial, residential, tourism-destination and related major capital investment projects.

E. D. Hovee has extensive experience working for Washington State-based PFDs, together with specific experience in evaluating convention, arts, sports and related event facilities both in and outside the state of Washington. Representative project assignments have included:

- October 2017 submittal of a *Spokane Public Facilities District INB Performing Arts Center Independent Financial Feasibility Review* for a $22 million renovation, since completed.
- Prior completion of the February 2013 Spokane *Public Facilities District Independent Financial Review* on behalf of the Washington State Department of Commerce for capital funding of then planned Spokane Convention Center (SCC) expansion, followed by May 2013 submittal of an operating budget review for the SCC.
- November 2015 review of land acquisition and financing feasibility for expansion of the Washington State Convention Center in Seattle on behalf of the state's Department of Commerce, followed by a 2018 Phase 2 review evaluation of facility build-out.
- Other assignments on behalf of Washington State PFDs including potential regional center projects for the Tri-Cities (two-county) PFD, economic restructuring of the Wenatchee hotel-motel tourism funding for marketing and event/conference facilities, Vancouver Hilton Hotel and conference center, Clark County amphitheater, and Cowlitz County expo/conference center, and lease extension for the Seattle Mariners stadium.
- Non-PFD related event facility assessments for the Oregon Convention Center, Portland Expo Center, Walla Walla Marcus Whitman Hotel feasibility, Skamania Lodge market analysis and development proposal, Oregon Trail Interpretive Center, Portland Center Stage/Armory Theater due diligence review, and Eola Hills Conference Center market feasibility (Salem, OR).
- Other related market and financial due diligence assignments including WSU campus building reuse and North Foothills brownfield site redevelopment (Spokane), business case for the 2016 USATF/IAAF indoor world track and field championships in Portland, feasibility evaluation for a Vancouver/Clark County minor league and multi-use baseball stadium, and transit oriented development impact analyses (Portland, SeaTac, Boise, Reno, Santa Ana, Anaheim, San Antonio and Oklahoma City).

APPENDIX B. DOCUMENTS REVIEWED

Documents reviewed as part of this independent feasibility evaluation of the Convention Center expansion project for the Washington State Department of Commerce and Yakima Public Facilities District (YRPFD) have included the following:

Cities of Yakima, Selah and Union Gap, *Interlocal Cooperation Agreement to Form a Public Facilities District,* 2001.

E. D. Hovee & Company, LLC, *Washington State Convention Center Expansion: Build-Out & Operating Feasibility,* as prepared for the Washington State Department of Commerce, May 24, 2018.

S&P Global Ratings, *Summary: Yakima, Washington; General Obligation*, March 21, 2017.

Yakima Convention Center, web site: www.yakimacenter.com

YRPFD, *Annual Tax Revenue, Five Year Historical Data.*

YRPFD, *Current Bond-Related Documentation* (including existing bond resolution and most recent bond rating).

YRPFD, *Construction Schedule, Potential Disruption.*

YRPFD, *Convention Center PFD 10-Year Fund 172 Revenue-Expenditure History.*

YRPFD, *Debt Financing Schedule.*

YRPFD, *Estimated Construction Costs.*

YRPFD, *Operating Income-Expense Projections.*

YRPFD, *1997 to Current HMT Tax Revenues* (spreadsheet file).

YRPFD and ALSC Architects, *Exterior Renderings*.

YRPFD, *3-5 Years Historical Data, Line-Item Financial Report*.

END NOTES

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1 David McFadden, Yakima County Development Association, "Yakima Valley real estate heats up," December 11, 2003 per https://www.djc.com/news/re/11151820.html (as of September 2019).

2 Convention Center refunding appears to have been one purpose of 2007 Limited Tax General Obligation and Refunding Bonds in the aggregate principal amount of $8,980,000 for purposes of refunding a 2002 LTGO (convention-center related) issue and to finance other projects including fire station remodel, modifications to River Road and financing for a Downtown Futures Initiative.

3 Floor plan and other facilities information for the Yakima Convention Center is provided by the web site: https://yakimacenter.com/

4 Information on the planned Yakima Convention Center Addition is provided by the web site: https://www.yccaddition.com.

5 Information for this independent financial review has been obtained from sources generally deemed to be reliable. However, E. D. Hovee does not guarantee the accuracy of information provided by third party sources, and information is subject to change without notice. Observations and findings made with this report are those of E. D. Hovee. They should not be construed as representing the opinion of other parties prior to express approval, whether in whole or in part.

6 As an added note, the Yakima Regional PFD was working with the knowledge that there are some expense items for which relatively flat fees are involved. Some of those expenses reflect very little if any change through the years. So, these expenses might be expected to remain basically the same over time.

7 Per an independent feasibility review conducted for the Spokane Convention Center expansion by E. D. Hovee, the initial project estimate was at about $710 per square foot. The project came in under budget at between $650 - $660 per square foot of added building area.

The Washington State Convention Center estimate of nearly $1,000 per square foot includes both added convention and structured parking area but excludes the cost of site acquisition, as reported via an independent feasibility review by E. D. Hovee completed in 2018.

8 As stated by S&P: "The downgrade reflects our opinion of weakening economic factors in the city, particularly income levels, as well as the recent use of general fund reserves, which has lowered the city's financial flexibility, in our view." While S&P considers the city and region's economy as "weak", counterbalancing factors include reviews of city management, budgetary performance and budgetary flexibility as "adequate". Liquidity and debt/contingency liability profile is viewed as "very strong." Source is S&P Global Ratings, *Summary: Yakima, Washington; General Obligation*, March 21, 2017.

9 Information regarding new hotels is as provided by Yakima Center personnel, October 2018.

10 As part of the Washington State Convention Center Expansion: Build-Out & Operating Feasibility Study prepared by E. D. Hovee for the Washington State Department of Commerce, May 24, 2018, a review was conducted of year-to-year operating income-expense experience pre- and post-expansion for selected western North American facilities. Experience was profiled for major convention facilities in Seattle, Spokane, Portland, Vancouver BC, Denver, and San Francisco. As noted by the report, over a period extending from two years before to three years after expansion, "expenses for these facilities have tended to increase by more than revenues." While detailed comparable data is not available for facilities comparable to YCC, this experience appears to be similar to what has been noted for Yakima with its prior facility expansions.