

CDA Act. A contract may have the effect of limiting a CDA's ability to act, but no contract may increase a CDA's powers beyond those authorized by the CDA Act.

The CDA Act and an ordinance creating a CDA, like all state laws, must be in conformance with the Constitution of Virginia. Article X, Section 3 of the Virginia Constitution requires that taxes or assessments (including special assessments) be levied or imposed only to pay for "local public improvements." Article X, Section 8 limits taxes, assessments or revenues only to the amount required to pay necessary expenses of government. There are no direct Virginia Supreme Court cases providing guidance on whether "local public improvements" is synonymous with public ownership. But decisions in other related areas suggest they are synonymous and we and other experienced practitioners in this area have concluded that public ownership of CDA financed improvements is the most sound approach in applying the provisions of the CDA Act.

While public ownership is necessary to meet state law requirements, such ownership need not be perpetual. Public ownership is required only for the period assessments are being imposed. Once bonds are paid and assessments no longer imposed, ownership of improvements may reside in a private entity.

Specifics of Park Center CDA. Section 15.1-5158A.1 of the CDA Act authorizes the Authority to "finance, fund, establish, acquire, construct, equip, operate and maintain" various infrastructure set forth in the City's Ordinance forming the Authority. This infrastructure, which was defined in the Ordinance as "Public Improvements," are listed in Attachment A to this memorandum. They include road improvements, sidewalks, landscape, signage, pedestrian bridge, public utilities, public park land and related soft costs, estimated to cost \$18,000,000 in total and allocated by cost category, and expressly subject to reallocation and to be undertaken in phases.

The Authority and the Developer entered into several agreements by which the Authority has agreed to finance, and the Developer has agreed to build, the Public Improvements authorized by the Ordinance. In accordance with the Ordinance, the Authority and the Developer entered into a Development/Acquisition Agreement pursuant to which the Developer would undertake the acquisition, construction and equipping of certain of the Public Improvements on the Authority's behalf. Defined under the Development Agreement as "Facilities," these improvements are set forth in Attachment B to this memorandum.

In the Development/Acquisition Agreement, the Authority represented that it was in the best interest of the Authority to acquire from the Developer or cause the Developer to convey certain Facilities at closing and to provide for the completion of certain other Facilities and, upon such completion, to acquire for itself or cause such Facilities to be acquired by another public entity. In all cases, however, public ownership of the Facilities was contemplated, was a fundamental component of the bond transaction and was critical to our analysis in delivering our opinion confirming the validity and enforceability of the Bonds. If any of the Facilities financed with the proceeds of the Bonds were not to be owned by the Authority or another public entity, there may well be an adverse affect on the validity of the Bonds.

Qualification of Park Center Costs for Federal Income Tax Purposes

Generally. CDA financed costs may be undertaken on both a taxable and tax-exempt basis or a combination of both. Tax-exemption is determined by whether property financed by the Bonds is used for governmental purposes or private purposes. Federal tax law distinguishes between these two purposes by focusing on whether any private person or entity has rights of use that are different and greater than the rights of use a member of the general public would have in the financed property. Ownership, long-term leases or licenses and similar contractual arrangements with private entities are deemed to be uses that are fundamentally private.

Recognizing that all property may be subject to inadvertent private use, federal tax law imposes a mathematical test to determine whether private uses preclude eligibility for tax-exempt financing. In rough terms, the test is applied on a 90% / 10% basis, with private use rights not to exceed the 10% threshold. There are various means to compute the 10% test, but in its simplest form, it is a computation that focuses on the percentage of bond proceeds for improvements subject to private use in relation to the overall proceeds of a bond issue (amounts received from the sale of the bonds plus investment proceeds on such sale proceeds). For example, if bond proceeds to build a government office building are \$1,000,000 and the government leases 15% of the building to a law firm, then the bonds would be “private activity bonds” and the government could not finance the building on a tax-exempt basis. However, if the law firm lease were only for 3% of the space, then all of the building could be financed on a tax-exempt basis.

Specifics of Park Center CDA. The Authority’s Bonds were issued as tax-exempt bonds on the basis that all improvements to be paid with the proceeds of the Bonds were to be owned by the Authority or another public entity. No private ownership or other private benefits/entitlements were contemplated either during the time the Bonds are outstanding or thereafter.

With that said, it is possible for a portion of the Facilities to be subject to some private use rights (e.g., reversionary interest or de minimis purchase option right following the payment of the Bonds) without adversely affecting the tax-exempt status of the Bonds. Any such arrangement would need to be small in amount, in my judgment materially less than 10%, to avoid any mistakes in how costs are determined and the math applied. And, as discussed above, no private ownership could exist during the time the Bonds were outstanding to avoid the Bonds being declared invalid under state law.

Current Discussions

Representatives of the City, the Authority and the Developer have been discussing the application of the remaining Bond proceeds as the completion of the Facilities nears. These discussions have arisen, at least in part, because the original budgeted amounts for the Facilities have not held true as the actual construction has taken place. In some instances, the costs of Facilities have been less than budgeted, while the costs of other Facilities have been more than budgeted. Because Bond proceeds for both state and federal law purposes must be expended on costs authorized by the CDA Act and the

Ordinance, the parties have been reviewing alternative Public Improvement costs to fully utilize the Bond proceeds.

In the most recent discussions to which I have been privy, the parties have focused on the land underlying the travelways and in particular whether such land could be acquired by the Authority in the same manner as the improvement (i.e., the road) is being acquired (by purchase or gift). The Ordinance authorized road improvements (with a preliminary cost allocation of \$7,500,000). The CDA Act defines "cost of improvements" to mean "the cost of constructing improvements and includes the cost of all labor and material; the cost of land, property . . . which are deemed necessary for such construction." Taken together, these provisions authorize the Authority to acquire the land under the newly constructed travelways and to use Bond proceeds to pay the cost of such acquisition.

Related to this discussion is the fact that the Authority must possess some property interest in the land on which the travelways and other Public Improvements are located. It cannot own the improvements unless it has some underlying property right without running the risk that the owner of the land will assert a claim of ownership on the improvements. At present, the City enjoys an easement right giving it access to the travelways but the Authority does not. A purchase of the land would address this dilemma. It also would allow the Authority and the Developer to meet their collective responsibility to spend all Bond proceeds on "costs of improvements" authorized by both the CDA Act and the Ordinance. Satisfying this obligation to spend the Bond proceeds will ensure that the validity and tax-exempt status of the Bonds is not jeopardized.

Please note that this memorandum summarizes only the relevant legal issues regarding the validity and tax-exempt status of the Bonds arising out of the current discussions. But should there be alternative approaches, the rules I describe will apply with equal effect. I would be happy to answer any questions you may have.

JDO/tv

EXHIBIT C

DESCRIPTION OF PROPOSED PUBLIC IMPROVEMENTS*

Road Improvements	\$7,500,000
Sidewalks, Hardscape, Signage and Pedestrian Bridge	3,000,000
Public Utilities including Storm Water Management	4,500,000
Public Park Facilities including Land	2,000,000
Engineering, Design and Permits	<u>1,000,000</u>
Total	<u>\$18,000,000</u>

* Costs are estimates, are subject to reallocation among the cost categories and will be undertaken in phases.

EXHIBIT A
To
Development/Acquisition Agreement
DESCRIPTION OF FACILITIES

<u>CDA - Qualified Costs</u>	<u>Sub-Total</u>	<u>Total</u>
<u>Milesson Park</u>		
Land/Closing Costs/Real Estate Taxes	1,421,833	
Landscaping/Hardscape	<u>50,000</u>	
Total		1,471,933
<u>Manassas Drive</u>		
Design/Submission Fees:	48,000	
Dry Utility Relocation and New Service:	80,000	
Bonds, Fees and Permits	50,690	
Hard Costs	<u>1,139,112</u>	
Total		1,315,803
<u>Traffic Signal</u>		
Design/Submission Fees:	19,700	
Bonds, Fees, Permits	5,000	
Hard Costs	<u>213,484</u>	
Total		238,184
SWM Pond Design and Pro-Rata Contribution		60,000
<u>Public Utilities, Travelways and City Parking</u>		
Design/Submission Fees	173,208	
Bonds, Fees, Permits	50,000	
Hard Costs	<u>3,610,849</u>	
Total		3,834,056
Contingency		250,000
Developer Fee and Overhead		230,024
<u>Finance Costs</u>		
Issuance Costs (Legal and Consulting)	350,000	
3 Years of CDA Admin Expenses	60,000	
Lehman Take Down Fee	51,737	
Duxbury Financial Fee	340,000	
Capitalized Interest (24 Months)	1,325,044	
Debt Service Reserve Fund	<u>875,000</u>	
Total		3,011,781
Total CDA Qualified Costs		10,411,781