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June 19, 2008

The Hon. Jacquelyn Brechtel Clarkson
Councilmember-at-Large
New Orleans City Council
1300 Perdido St., Room 2W50
New Orleans, LA 70112

Re: World Trade Center Transaction

Dear Councilmember Clarkson:

We are writing to express BGR's concerns with certain aspects of the proposed lease of the World Trade Center to the World Trade Center of New Orleans, Inc. (WTC). Our understanding of the transaction is based on a review of the following documents, as well as conversations and correspondence with representatives of New Orleans Building Corporation (NOBC) and WTC: the draft lease among NOBC, WTC, and the City of New Orleans as Intervenor (Draft Lease); the draft transfer, assignment, assumption and quit-claim agreement among WTC, Full Spectrum and NOBC as Intervenor (Draft Assignment Agreement); and a memorandum of understanding between NOBC and WTC dated January 31, 2007 (MOU).

<u>Background</u>

The Draft Lease would replace a lease currently in place between NOBC and WTC. Twelve years remain under that lease.

Under the Draft Lease, NOBC will lease the World Trade Center property to WTC, a nonprofit organization, for 99 years. WTC is permitted to assign all its rights in and to the Improvements, and under the lease, to Full Spectrum of NY, LLC, or its designee. Improvements are defined as the tower building and parking garage (the "Buildings") and any other structures and improvements permitted to be located on the Leased Premises.

The Draft Assignment Agreement assigns all of WTC's rights in the Draft Lease to Full Spectrum. The assignment calls for Full Spectrum to pay $30 million to WTC. NOBC will receive $24.25 million of this amount as pre-paid rent (Base Rent) up front. WTC will keep $5.75 million as reimbursement for demolition and legal and other expenses that NOBC owes from earlier transactions. WTC will also retain floors 29 and 30 and receive an annual rent payment. The rent begins at $350,000 and is adjusted upward for inflation every five years.

The Draft Lease requires Full Spectrum to develop an urban mixed-use project on the leased property. It requires the project to include at least 100 residential units, at least 100 hotel rooms, a "cultural attraction consistent with the established themes and traditions of the City of New Orleans," and specialized retail, together with "all necessary streetscape, landscape and hardscape" on or adjoining the property.

Failure to comply with the covenants would be a default under the Draft Lease. However, the Draft Lease specifically states that because the Base Rent is prepaid, NOBC has no right to terminate the lease.

The Draft Lease provides that the property is taxable to the extent provided by law. According to NOBC, new improvements (which will be owned by Full Spectrum and condominium owners) will go on the tax rolls. However, under Louisiana law, because the land and the existing Buildings are publicly owned, they will remain tax exempt even though they are being converted to a private development. To compensate partially for that defect in Louisiana law, the Draft Lease stipulates that, so long as the existing property is off the tax roll, WTC will pay NOBC Additional Rent equal to 60% of the taxes that would otherwise be payable on the land and existing Buildings. NOBC commits to spending the Additional Rent to make riverfront improvements in the area proximate to the World Trade Center building.

We are advised by NOBC that the payment was set at 60%, rather than 100% of taxes, because WTC and the developers are giving up their rights to build on part of the land. NOBC sought the no-build area to protect the line of sight to the river. The no-build area consists of an 8,409 square foot strip, about 70 feet wide, running along the left side of the building from Canal Street toward Spanish Plaza. Approximately half of the area appears to be subject to a Public Belt Railroad right-of-way, which would limit (if not prevent) the tenant's ability to build there.

<u>BGR's Concerns</u>

Our major concerns with the Draft Lease relate to an implicit tax break for the property owners, the retention of rent payments by NOBC, inadequate remedies, ambiguities in the document as to the payment of the up-front rent, and an unusual auction provision. To address them, we recommend the following:

Eliminate the tax break by requiring a full tax-equivalent payment.

Although the transaction is structured as a lease, it is the functional equivalent of a sale of the World Trade Center property. For that reason, the Draft Lease should require a tax-equivalent payment equal to 100% of the taxes that would be payable if the land and existing buildings were not exempt. This can be accomplished by raising the Additional Rent to 100% of the taxes that would otherwise be payable on the land and existing buildings.

We are advised that more than half of the development would consist of high-end condominiums. Under the terms of the Draft Lease, these properties would not be fully taxable unless NOBC sold the building outright. Until then, the condominium owners, like Full Spectrum, would pay full taxes only on the build-out. They would get a pro-rata share of the tax break for the existing land and Buildings. Immediately before Hurricane Katrina, BGR took a stand against tax breaks for high-end condominium developments. It reiterates that position here.

The World Trade Center property enjoys one of the most attractive locations in New Orleans. It is hard to believe that it cannot be developed in a way that protects riverfront views without a tax break. If indeed it cannot, the City should consider holding the property until the market improves.

Direct Additional Rent to tax-recipient bodies and Base Rent to the City.

Under the Draft Lease, the Additional Rent is retained by NOBC and reinvested in the riverfront around the development. We strongly believe that proceeds from the Additional Rent, which functions as a payment in lieu of taxes, should be directed to the appropriate tax recipient bodies. The proceeds of the Base Rent should be transferred to the City for use in accordance with priorities established through its capital planning process.

Require a performance bond or add termination rights for nonperformance.

As noted above, the Draft Lease contains the Tenant's commitment to develop the property, but it does not provide any deadline for doing so. Failure to do so constitutes an event of default. NOBC can exercise various remedies in the case of a default. However, one critical remedy – the ability to terminate the Lease – is specifically excluded on the grounds that the rent (other than the Additional Rent) has been paid for the entire lease term. In other words, NOBC cannot reclaim the property if the tenant fails to develop it.

Having opted for a lease transaction, NOBC should address this weakness. This can be done either by requiring the developer to post a performance bond in favor of NOBC or by adding termination provisions to the Draft Lease. The termination provision should stipulate that the Draft Lease will terminate if either of the following occurs: the up-front rent is not paid by a specific date, or the development described in the Draft Lease is not completed by a specific date.

The lack of protection for the City stands in marked contrast to the protection afforded WTC. The Draft Assignment Agreement requires Full Spectrum to obtain a $5 million line of credit to assure that it meets its financial obligations to WTC.

Clarify the terms for payment of up-front rent.

Section 3 of the Draft Lease requires the tenant to exercise its "best efforts" to execute the Lease and pay NOBC the Base Rent of $24.25 million by certain dates. The section is ambiguous. It should be revised to eliminate the "best efforts" language and provide instead a clear deadline for payment. It should also make clear that the agreement terminates if the payment is not received by that deadline.

Explain and evaluate the auction provision.

The Draft Lease states that the tenant (which after the assignment would be Full Spectrum) has the right to demand that NOBC sell the property, subject to the lease, through a public auction. On its face, this is an extraordinary provision to include in a commercial real estate transaction. It should be thoroughly explained and evaluated in light of the explanation.

The effective sale of one of New Orleans' most valuable public assets is a matter that should receive careful scrutiny. We hope that you will seriously consider our comments and demand changes before you vote on the ordinance to approve the Draft Lease and other documents.

Sincerely yours,

Janet R. Howard
President

cc: Sean Cummings