AGENDA

Cambridge City Council Committee
Cambridge Boys & Girls Club Board

Issues of Concern:

1. Current financial status of the Boys & Girls Club, affecting joint program of Club and City in Cambridge Enterprise Collaborative.

2. Bridge loan to Club for general operating expenses, to allow for continued participation by the Club in Collaborative program, not to exceed $60,000.

Appended:

a. Press Release, 5/5/86, describing Club financial situation

b. Memorandum, 4/31/86, describing Collaborative opportunities

c. Memorandum, 4/17/86, describing Club opportunities with Collaborative.

FOR IMMEDIATE RELEASE 9:00 A.M. 5/06/86

CAMBRIDGE BOYS & GIRLS CLUB FACES EARLY CLOSING

The Boys & Girls Club of Cambridge, with ten years of programs for low and moderate income Cambridge youths, may be forced to close by the summer. Part of the national Boys Club of America movement, the Club offers recreational, employment readiness, and organizational experience to Cambridge young people, 7 to 17 years of age. Members pay a flat $2 membership fee to receive all member services including photo identification cards and access to all club activities. This makes the Club one of the few economically desegregated programs for youth in the city.

Founded ten years ago in East Cambridge, the Club was one of the first in the nation to integrate boys and girls programming. This year, funded by E.R.I. its partner in the Cambridge Enterprise Collaborative, the Club is planning an extensive summer recreational program which may be threatened by its current financial situation.

Delays in development, rentals, and sales have stalled income from the Club's project, the Cambridge Enterprise Collaborative. This has led to severe cutbacks in services at the Cambridge Boys and Girls Club on Prospect Street. Funded in 1982, the Collaborative was planned as an economic development program to finance a Boys & Girls Clubhouse for low and moderate income Cambridge youths, 7 to 17 years old.

The Collaborative purchased the Hyde Shoe Company building for industrial development a year ago this month. Consultants and developers hoped to finance Club activities by November, 1985. This allowed the Club to move to the former St. Mary's Gym on Prospect Street near Central Square. The Collaborative now awaits lease up, refinancing, and corporate condominium sales, without which the Club cannot continue at its current deficit at St. Mary's.

According to the Club's Executive Director, Jack Litwinsky, "There's been good faith on all sides, but we simply can't put off bills with Collaborative promises. We have to ask for help from our neighbors to get us through this next six months."

The Club has at least one-third interest in the Collaborative, which received $1 million three years ago to purchase a clubhouse and develop new business opportunities for Cambridge residents. Along with E.R.I. and the City of Cambridge, the Club is now offering "incubator space" to new and developing Cambridge employers at below market rentals. When the Collaborative is fully developed, market rents will subsidize these rentals as well as Club activities and a revolving loan fund for these and other community based ventures. Until then, however, the Club does not have enough money to operate.

Juan Everteze, the Club's Finance Chairman, was asked by the Board to raise funds to bridge the gap until Collaborative income is stable, now planned for late Fall, 1986. The Club's immediate debts are about $15,000, and longer term debts of $20,000. "This is not very much in the hole, given the Club's equity in the Collaborative," according to Joe Beckmann, a development volunteer. "Yet the Club can't expect the I.R.S., the Commonwealth, and individual vendors to wait forever until that equity begins to earn income," Beckmann continued.

Cambridge Police Lieutenant Richard Ring, who founded the Club ten years ago and is also on the Finance Committee, added that, "We can't expect all our vendors to become our lenders, and the public can help."

The Club is now asking for short term loans or grants enough to cover immediate debts, and can pledge up to $50,000 of its equity in the Collaborative to guarantee repayment or services to Cambridge youths. The City Council recently appointed a Special Committee of Councillors Velucchi, Graham, and Walsh, to review the city's role in the Collaborative and examine the 1982 commitment of a $2 million guarantee of construction loans. In the interim, the Club is seeking immediate financial aid from area businesses and donors. Interested donors, lenders, or investors should contact the Finance Committee care of the Club's Executive Director, Mr. Litwinsky, at the Clubhouse, 120 Prospect Street, Cambridge, 547-2319.

MEMORANDUM

TO : Finance Committee, Board of Directors
FROM : Jack Litwinsky
RE : Financing Plan
4/31/86

In my experience there are several sources available for short term $50,000 loans, most of which we have already contacted. We have received $3,000 from the Cambridge Foundation, the use of a Digital computer and supplies for a photo identification program from Polaroid. In each of these gifts the donors explicitly stated their concern that such contributions be used specifically for the purposes stated in our proposals.

As per your request of 4/16, the Collaborative Board approved the guarantee of up to $50,000 to the Club at its last meeting, 4/22. You may use that guarantee with anyone who respects the asset value of the Collaborative - banks, the city, the state, or private investors. The Collaborative Board expected that the city would refinance the Collaborative, and were disappointed.

Community Development Block Grant funds already guarantee the Collaborative funding and the Collaborative's guarantee may be enough to secure a city sponsored advance for a specified period.

If the Collaborative is not available as a direct source of funds for the foreseeable future the Club should move from St. Mary's as soon as the summer program is over. There is no way Beano and ad hoc fund raising can carry the overhead and provide services to children. You will note I made this same recommendation in December, January, and March.

This leaves two options: to close at St. Mary's or to market Collaborative assets and earn a developer's fee. There are several conditions by which the Collaborative can save the Club by August. Some are a result of the City Council intervention.

On 4/28, the Council's consultant cast the entire project at incubator rates. The Collaborative building can be developed and marketed **either** as unimproved warehouse/incubator space **or** as first class office space. In either case the Club makes the same amount of money:

Without major improvements, and with $700,000 for construction to bring the exterior up to Class B standards and seal the interior space for tenant improvements, the building will have cost less than $3 million for over 100,000 square feet of rentable space. At $4/square foot, 75% rented represents break even, and 100% provides over $250,000/year to the Club.

With major improvements, and $3 million in construction, the building will have cost about $5 million. At triple net sales of

100,000 square feet, $75/foot including commissions will break even at 75% sold. As additional units are sold, the Club takes a greater net capital gain.

Whether the development is high ball or low ball **is not our decision.** The City Council may decide, or some outside developer partner may generate a high ball option. **In either case the Club makes about the same amount of money.**

Regarding the Collaborative, therefore, the question faced by your committee is (a) Will the project pay off; and (b) if so, when?

If you determine that the Collaborative is still a worthy investment, it will only be worth while if we can market the space (in either high or low ball formula). For the past year we have relied on refinancing as the means of delivering a developer fee. This has not worked.

A better plan, in the words of the bank, of private developers and even of our own consultants at GBCDC, is to sell or rent space in the building as fast as possible. For this I need your authority.

The CEC proposal specified that the Boys & Girls Club should broker its own space for profit. The Collaborative Board directed negotiations with Russell Hill, the broker, to guarantee that he charge no more than 50% of his normal brokerage when clients are identified by the city, GBCDC or the Club. With your approval I will hire several unlicensed brokers, and the Club can collect 50% brokerage on tenants or owners generated and developed by these staff people, who will work for a percentage of the Club's commission.

With $350,000 budgeted for "high ball brokerage", 50% of this brokerage earned for generating initial contacts represents at least $100,000 to the Club by September, by which the building must be sold or the project dies. The only cost of this activity is a percentage of profit, for salaries to the in-house representatives. That should not exceed $30,000 for four months, for a net to the Club of at least $60,000.

That net is in addition to whatever developer fees or management services might be negotiated with the Collaborative.

MEMORANDUM

TO : Executive Committee, B & G Club
FROM : Joe Beckmann
RE : Alternative Pro forma projections
4/17/86

The financial formulas for the Enterprise Collaborative involve recycling debt commitments already made. The initial Collaborative proposal, submitted by the City of Cambridge and therefore binding the city by contract, commit $2 million in loan guarantees for incubator space and Boys & Girls Club space acquisition.

These commitments are not appended or referred to in the mortgage documents signed for the Hyde Shoe Company purchase, and are even by implication a part of that financial transaction.

Davis-Bacon wage rates are avoidable only if those commitments are not used as direct city loans. There is no reason for them to be used if sales are as they are now projected.

Given this outstanding commitment, a $600,000 direct guarantee - and not a loan - would be useful only to start construction to be followed, within weeks, by bank financing.

I suggest several strategies:

1. Leases with options to purchase at the rates already signed by Hill, in order to achieve the 35% lease-up initially required by the banks.

2. Large scale promotion, among non-profits and business community that we have achieved 25% lease up in three to four weeks.

3. A series of specified goals for brokers, with brokerage fees sliding in accord with goal achievements (essentially commissions with overrides on volume) to move as many small (1,500 to 2,500 square foot) units in as short a time as possible.

4. No exclusives, but commissions at 6% of sale price, 10% of lease total value, and overrides for sales or leases in excess of 15% of the total available space.

5. A direct promotion by the Club to small business in Cambridge for incubator tenancies. There is no reason why rates as low as $4.50 triple net do not move quickly, if only people know about them. A corollary is to open more than basement space to incubator tenants. Perhaps with options to other space for additional fees.

6. Three year leases to the city, for particular agencies to "anchor" the development. If one-third of the building is leased this way, or 30,000 square feet, the $2 million commitment is met without cost to the city or the city's credit, **even if that space**

includes basement at $3.50! After those leases expire the city can collect at market price for any leasehold improvements, and that delays our marketing period for three more years.

These strategies are based on my perception that the core of the problem with the Collaborative has been its marketing. If you accept this perception, the Collaborative has spent almost $100,000 in the past year, in interest payments, due to inept marketing. No one is to blame, but solutions are available only if they address what was initially at fault.

A second fault, again of no individual or firm, has been in financing the initial purchase and now the acquisition. The city guarantee exceeded, by a large margin, all costs to date, and yet the Collaborative has paid interest at market rates, and the next round of financing seems even higher, with two points above best rate and an additional point as a bonus. There are several financing strategies which come to mind, which obviously have not been used.

1. Private placement to limited partners of the incubator and publicly tenanted shares, allowing private investors to write off the interest and depreciation, and collect a second position on an income stream and first position on later sale of public tenant space.

2. Sale of warrants, in effect industrial development bonds, which include rehab and final fitting up of incubator tenant space, for later sale or market rental. Such warrants should include Investment Tax Credits on all non-condominium space in the building, as well as any historical designation credit or residual C.A.R.D. benefits. They may be highly speculative, but they are useless to the Club and not very useful to the Collaborative.

3. L.I.S.C. support to supplement or overlap any direct city guarantees. The last attempt was in the context of a one-time development, but L.I.S.C. has not been contacted since condominium development has emerged as the primary means of financing. Condo sales will generate a capital fund for the Boys & Girls Club which must be re-invested before the Church gets its hands on it. That reinvestment can be in L.I.S.C. supported investments anywhere, thus opening discussions in a most untraditional vein, asking for loan guarantees for bridge funding and offering investment capital when that space is sold.

These are neither exhaustive nor necessarily good strategies, but they do suggest that we have yet to use up ideas which may pay.

Finally, the pro forma drafts circulated at our 4/16 meeting merit some consideration, in the context of these suggestions. Their assumptions differed significantly from Zimlicki's, and, even in error, offer more hope to the Club's financial viability.

1. Phase I has begun, and began upon purchase of the building. Therefore Phase I funds to the Club are earned income, at least in part, before further construction. To make such funds contingent upon separate loans only diminishes the unclear equity of the Club in the Collaborative, and requires a legal opinion whether such loans are necessary or appropriate or in conflict with the Club's trustee role to the Collaborative.

2. Other payees are paid on the basis of the entire budget of the program, from acquisition through construction, but the base for the Club, in Zimlicki's projection, is only on construction. This is neither equitable nor appropriate, and, basing 1.5% on the whole budget increases the amount from $55,000 to well over $75,000, or what it was initially supposed to be.

3. Splitting payments between Phase I and Phase II may be appropriate, but not 50/50, for, most notably, GBCDC is paid $50,000 and then $20,000 as a consultant. A more equitable formula, used in my projection, is a proportion which reflects the actual expenditures in Phase I and Phase II and final Tenant Set Up. Depending on how those numbers run through, this ranges from 65% to 72% for the initial payment of the total of 1.5% of the entire deal. There are plenty of precedents for such a formula, not the least of which is GBCDC itself, or the role in the initial proposal of a General Manager, which is devolving on the Club in lieu of a personal position.

4. Interest rates are poigniantly fuzzy in these projections as well as in Zimlicki's. Reserve requirements of condo fees are also very fuzzy. When purchase and sale agreements are signed, many of the loans projected for Phases I and II will be paid well before they come due, and may, in fact, be avoided with a 90 day float from the bank and contractor. Such a float is, again, well below the city's extant $2 million commitment. Saving $200 to $400,000 in interest the first year represents a net direct profit to the Club as well as the Collaborative, unless the Collaborative draws in private investors who could use the deduction. This sounds like a snake eating its tail, but it means that private loan guarantors could stand to make up to $400,000 in a secure tax deduction for a risk guaranteed by the City of Cambridge, against a payment guaranteed by rapid sale or easy lease up at 20% to 40% below market value. The point of so many different financial projections was to see how different interest rates play through such a large number of variable budget costs. Saving on interest saves almost twice as much than saving on any other cost. And that saving is directly to the benefit of the Developer (including GBCDC).

5. The payout to GBCDC and other vendors of services which might be considered contingent upon success (eg., legal) is on the basis of 20%, 20%, and 60% upon completion. Surely this can be adjusted, but there is no reason why some fees cannot be contingent. Legal, accounting, and consulting are often formulated with a bonus for timely performance, and we have plenty of room to ne-

gotiate. Realize that, although GBCDC has done reasonably well on behalf of the Collaborative, there are other developers who would do better on a straight percentage with a contingency bonus. The time it takes to bring them in and brief them adequately is the primary argument against change, and a financial argument is not valid. (I've talked with two such developers who would be happy to bid 20% to 30% less than GBCDC for the right to 10% commissions on all private investment and legal and/or accounting contracts.) The $.58/foot rate in this budget is far less than GBCDC should make when all is said and done.

6. The largest difference in these projections is a result of how much is actually in the construction loans. Zimlicki's pro forma includes the complete refinancing of purchase as well as of direct construction expenses. Even at that, however, I don't see how he derived .0079 as a unit when there are at least eight months (or .75) of a year. I'm sure that footnotes would resolve this kind of confusion, and that the entire financial pro forma package has more information than is included in the package we saw. However, that makes me even more uncomfortable.

It only took an afternoon to derive these numbers, and this itself shows why we must get some additional computer support as soon as possible. A few hours as a group manipulating these variables should produce financial arguments at least as strong as those presented in the package.

5-320

Comm. from the Cambridge Boys & Girls Club Re: issues of concern on their financial status affecting the joint program of the Club & the City in Cambridge Enterprise Collaborative & a bridge loan to the Club for general operating expenses.

In City Council,

May 5, 1986