# Lot D Waterfront
# Roadmap to Redevelopment

*Prepared for:*
The City of Duluth

*Prepared by:*
Council of Development Finance Agencies

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# Contents

# About the Roadmap to Redevelopment

The *Roadmap to Redevelopment* is a product of the CDFA Brownfields Technical Assistance Program, which is funded through a grant from the U.S. Environmental Protection Agency (EPA). The program provides technical assistance to brownfields communities on redevelopment finance. For communities that require detailed, hands-on assistance for their redevelopment efforts, CDFA Brownfields Project Response Teams comprised of CDFA staff and technical assistance partners are available to conduct site visits and offer financing strategies. The goal of these visits is to provide communities with specific, actionable steps that can transform brownfields into economically-productive sites in accordance with the goals and plans of the community. CDFA will coordinate 36 Brownfields Project Response Teams over the life of the program.

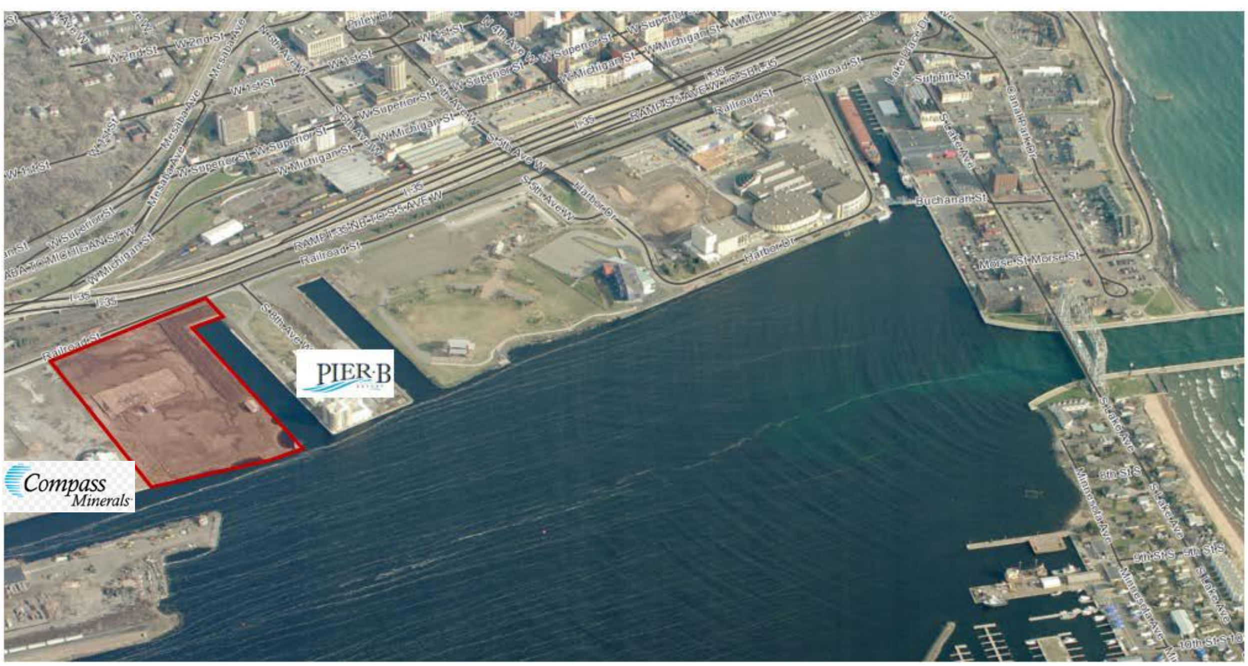
The *Roadmap to Redevelopment* was developed through a multi-day process that included interviews with numerous stakeholders from the government, business, and non-profit sectors. The strategies provided are based on the input of development finance experts, CDFA staff, and the interests of stakeholder groups gathered during the Project Response Team site visit. This report provides a framework for financing the cleanup and redevelopment of Lot D along the Duluth waterfront.

# Background & History

The City of Duluth is known for its 26-mile-long coast along the western shore of Lake Superior and the St. Louis River. Founded on industry, Duluth became a major exporter of iron ore, lumber, and other natural resources. In the 1900s, its port handled more tons yearly than New York City. With access to the St. Lawrence Seaway[1], and the ability to accommodate large ocean vessels in its large inland harbor, Duluth's industries flourished in manufacturing plants and warehouses along the waterfront. When large steel companies closed in the 1970s, many neighboring corporations also closed, leaving vacant warehouses and junkyards dotting the coast. In the decades that followed, Duluth's recovery efforts focused on improving the aesthetics of the waterfront to attract tourism.[2] Duluth has become known as the gateway to Minnesota's North Shore. Today, historic warehouses are inhabited by shops and restaurants catering to visitors in what is known as the Canal Park District. While several industries still thrive nearby, the City has cleaned up much of the waterfront and diversified the land use to include retail, hotels, and housing.

The Lot D site in Duluth is the last mixed-use (non-industrial) zoned parcel to be redeveloped along the downtown waterfront. The property was manmade in the 1880s. Former users on the site include the Cold Storage Company and Western Electric Company. More recently, the City has used the site for overflow parking for large events hosted at Bayfront Festival Park or at the nearby convention center. The site is also used for snow storage and laydown space as needed.

Selective remediation has already taken place on the site. The major redevelopment challenges are due to geotechnical issues caused by a shallow water table, poor soil bearing capacity, and a deteriorating seawall. Improvements to the site will require foundation piling systems, seawall repairs, and possible




[1]A system of channels connecting the Great Lakes to the Atlantic Ocean

[2] Duluth Chamber of Commerce. (n.d.) History & Area Information. Retrieved from: https://duluthchamber.com/local-living/history-area-information/

removal of a 1-acre of thick concrete foundations in the center of the site. Public infrastructure improvements to roadways will also be required to improve connectivity to the downtown and Canal Park District; Interstate 35 severs the site from other desirable nodes, preventing convenient multimodal travel options.

**Opportunity**

As the last mixed-use waterfront parcel with views of Duluth's iconic Aerial Lift Bridge, Lot D has potential to offer a unique high-end housing option along with commercial and retail opportunities. The site has long been underutilized and yet, the site work required to get the property development-ready is a daunting challenge.

*The Duluth Aerial Lift Bridge was originally constructed in 1905 resembling a ferry bridge in Rouen, France- the only other one of its kind in the world. The lift was added in 1930.*

In 2016, the City issued a Request for Proposals for the redevelopment of Lot D. The Developer selected for the project has proposed 300 units of high-end housing with commercial, retail, and restaurants on the site. The property will also provide up to 1000 parking stalls to accommodate residents and businesses, but also to be used as event parking on evenings and weekends. Total project cost is estimated at $133M, of which the Developer expects the Public to absorb $20M. At this time, there is no cost breakout to demonstrate how much of the $20M is for off-sites, additional parking, or other line items.

In preparation for gap financing, the City has been pursuing a special TIF District designation. Minnesota law reserves TIF for use as a redevelopment tool and requires that a site must have an existing "substandard" structure in order to be eligible. Although the Lot D project fits within the goals and purpose of TIF funding, it does not legally qualify because there is no longer a structure on the property. Other communities in Minnesota with similar challenges have been granted special TIF legislation to allow for use of the tool. Preliminary analysis demonstrates that TIF would contribute $10-$12M of the total project cost. In May 2018, the City requested designation for a Lot D Special Legislative District, based on the grounds that the blighted property formerly housed a structure that was later removed for safety reasons, and the redevelopment otherwise fits the TIF criteria; unfortunately, the request was not granted. City Administration intends to renew this legislative request in 2019.

Additionally, the City is hoping to utilize Minnesota's Redevelopment Grant Program offered through the state's Department of Employment and Economic Development (DEED) to fund a portion of the project. This program was not funded in the 2017 or 2018 legislative sessions; as of the writing of this report, there is no certainty as to whether or not these grant funds will be made available in time to fund the Lot D project. The strategies below offer supporting suggestions and ideas for alternative funding sources.

# Strategies

## Part I: Pursuing Sources of Local Funding

As mentioned previously, the total project cost is currently estimated at $133M. This includes predevelopment costs, geotechnical work to prepare the site, infrastructure required for the development, and vertical construction. Despite the extraordinary costs of this project (due primarily to the geotechnical work and public infrastructure requirements), the City can justify the financing assistance if the financing gap can be validated and economic benefits of the project can be demonstrated. The following suggestions support the City's efforts to identify sources for local gap financing.

i. Define the Public Realm within Project Scope

The City should work with the Developer to determine which aspects of the redevelopment are within the Public realm of the project. For instance, the infrastructure and parking are currently included in the Developer's total project costs; if the City had an option of issuing a General Obligation Bond for infrastructure, costs to the developer for that component of the project could be reduced, which may then reduce the financing ask from the City.

ii. Renew Request for Special Legislation for Tax Increment Financing (TIF)

As previously mentioned, the City requested designation for a Lot D Special Legislative District in May 2018, based on the grounds that the blighted property formerly housed a structure that was later removed for safety reasons, and the redevelopment otherwise fits the TIF criteria. The request was denied. It is recommended that the City work with its legal counsel to renew this request in 2019. To show good faith in the meantime, the City should enter into a memorandum of understanding with the Developer outlining the expectations and commitments related to the future of Lot D redevelopment.

iii. Expand Special Service District (SSD) Boundaries

Duluth's downtown and Canal District were designated as a Special Service District (SSD). SSDs, (the Minnesota version of Business Improvement Districts (BIDs)), are organizations formed by local businesses and property owners that offer services beyond what the local government offers in the area. In Minnesota, SSDs have commonly been used for expenses like street and sidewalk cleaning, snow and ice removal, lighting, signage, parking, parking enforcement, marketing and promotion, landscaping, and security. They may also include capital improvements as authorized in the special assessment statute.[3] The City could consider extending the BID along the waterfront to include the Lot D site, which could offset some of the improvements. An additional, or premium sales tax could be imposed on consumers (a large portion of whom are tourists) to pay any loan or debt service payments for the project.

iv. Evaluate Potential for Tourism Tax Bond to Fund Redevelopment Projects

The City collects a significant amount of revenue from tourism activities each year and these funds are used for a variety of projects. It may be worth considering whether a portion of these funds could be directed to a fund to support redevelopment projects.

v. Levy Economic Development Authorities (EDA) Tax

Minnesota statute permits a city to levy taxes for the Economic Development Authority as a "special taxing district".[4] The tax is limited to .0185 percent of the estimated market value on property. Although modest, this appropriation could be used to fund pre-development activities including required studies, design, and site prep.

## Part II: Pursuing Grant and Loan Opportunities

Several grant and loan opportunities exist at the state and federal level that can support various aspects of the project. Combining two or more of the following resources would make a significant contribution to the development gap.

i. Minnesota Department of Employment and Economic Development (DEED) Grants

The City is aware that the Lot D project is a great fit for DEED's Redevelopment Grant Program. The program pays up to 50 percent of infrastructure improvements, soil stabilization and other environmental infrastructure costs with a 50 percent local match.[5] The City will continue to request the refunding of this program.

Other DEED Grants that may be able to offer financial assistance to the project include:

*Contamination Cleanup Grant Program*
Although selective remediation has already been completed on the site, some unknowns may still exist. If additional cleanup funding is needed, DEED's Contamination Cleanup Grant Program can cover up to 75 percent of the cost to investigate and clean up sites for redevelopment purposes. The program requires a 25 percent local match.

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[3] Minnesota House of Representatives. (October 2014). City Special Service Districts. Retrieved from: http://www.house.leg.state.mn.us/hrd/pubs/cityssd.pdf
[4] The Office of the Revisor of Statutes. (n.d.) 2017 Minnesota Statues. Retrieved from: https://www.revisor.mn.gov/statutes/cite/275.066
[5] Minnesota Employment and Economic Development. (n.d.) Redevelopment Grant Program. Retrieved from: https://mn.gov/deed/government/financial-assistance/cleanup/redevelopmentgrantprogram.jsp

*Innovative Business Development Public Infrastructure (BDPI) Grant*
The BDPI program focuses on job creation and retention of innovative businesses such as "using proprietary technology to add value to a product, process, or service in a high technology field; researching or developing a proprietary product, process or service in a high technology field; researching, developing, or producing a new proprietary technology for use in the fields of tourism, forestry, mining, transportation, or green manufacturing." Like the Redevelopment Grant program, the BDPI program provides grants to local governments for up to 50 percent of the capital cost of public infrastructure with a 50 percent match.[6]

ii. Economic Development Administration (EDA) Public Works Program

EDA's Public Works program helps distressed communities revitalize, expand, and upgrade their physical infrastructure. EDA grant funding is targeted for distressed areas and is tied to job creation, so it would be necessary to demonstrate that end uses of the Lot D redevelopment would result in some permanent jobs. If awarded, grants could cover some of the site costs and possibly connectivity enhancements. The City should reach out to the regional EDA office to inquire about specific eligibility criteria.

iii. Better Utilizing Investments to Leverage Development (BUILD) Grants

Previously known as Transportation Investment Generating Economic Recovery, or TIGER Discretionary Grants, Congress has dedicated nearly $5.6 billion for nine rounds of National Infrastructure Investments to fund projects that have a significant local or regional impact.[7] The BUILD program is administered through the Department of Transportation and grants are highly competitive. Projects with multi-modal and multi-jurisdictional components are given special consideration. Although not appropriate for the Lot D redevelopment, the BUILD grant may be an option for the larger connectivity issues to and from the site: improvements to Railroad Street, de-tangling of the "can of worms" caused by multiple on/off ramps to Highway 35 near the site and connecting Lot D via streets and pedestrian trails to the Canal Park District.

*Aerial view of the "can of worms" interchange along Interstate 35 in Duluth. Photo courtesy of Duluth News Tribune / 2017 file*

[6] Minnesota Employment and Economic Development. (n.d.) Innovative Business Development Public Infrastructure Program Overview. Retrieved from: https://mn.gov/deed/government/financial-assistance/business-funding/innovative/
[7] U.S. Department of Transportation. (2018). About BUILD Grants. Retrieved from: https://www.transportation.gov/BUILDgrants/about

iv. Transportation Infrastructure Finance and Innovation Act (TIFIA)

TIFIA provides Federal credit assistance in the form of direct loans, loan guarantees, and standby lines of credit. Key objectives of the program include facilitation of projects with significant public benefit and encouragement of new revenue streams and private participation. Typically, TIFIA requires large surface transportation projects with costs of over $50M and covers less than 33 percent of eligible project costs. State and local governments, as well as private firms, are eligible to apply. Public or private highway, transit, rail and port projects are eligible to apply for TIFIA assistance.[8]

## Part III: Incentivizing Private Investment

Lot D may be eligible for certain federal incentive programs that have various qualifying factors including project location, end use, and jobs created. While the investment tools discussed in this section have very specific eligibility and qualification criteria, they should be considered by the development team if a fitting project or tenant is identified.

i. Market Lot D as Qualified Opportunity Zone

The Tax Cuts and Jobs Act (HR 1) that was signed into law late in 2017 creates a new tax incentive to attract capital to low-income census tract areas, allowing investors to defer tax on capital gains if the proceeds are invested in a qualified Opportunity Fund which is used to support new or existing business activities within the zone. The capital gains invested in a Qualified Opportunity Fund are eligible for partial tax forgiveness if the investment is held in a Qualified Opportunity Fund for at least 5 years, and if an investment is held for 10 years, any tax on the appreciation of that investment is forgiven. Many investors are willing to provide capital to projects but lack the wherewithal to locate and follow through on opportunities in needy communities. The new Opportunity Funds will democratize economic development by allowing a broad array of investors throughout the county to pool resources and mitigate risk, increasing the scale of investments going into underserved areas. However, when funds will be organized and begin investment is uncertain. The IRS has not yet issued regulations and, while investment houses and some community economic development organizations like LISC are exploring creating funds, such funds do not yet exist. If the project is delayed until such time as funds have been set up, it may be a source.

ii. Utilize New Markets Tax Credits (NMTC)

Lot D is located in a NMTC eligible census tract. The NMTC program incentivizes economic growth through the use of tax credits that attract private investment to distressed communities that provides significant direct benefit to low income people. The NMTC Program can potentially generate a substantial amount of private equity (approximately 20-25 percent of project costs) for eligible projects depending on the fee structures of the CDE providing the credits and investors.

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[8]TIFIA Credit Program Overview (2015). Retrieved from: http://www.transportation.gov/tifia/tifia-credit-program-overview.

However, to be competitive projects must have a strong commercial or retail component providing direct benefit to low income persons. Incubators that assist low income entrepreneurs and essential retail services like grocery stores in food deserts may garner credits. A museum or other civic facility providing special educational programs and employment benefiting low income individuals may be competition. Market rate housing is not an eligible use although some mixed-use structures can qualify. If housing is part of the project and even on overall site, 20 percent of the units may need to be affordable even if the housing is not directly assisted. NMTC is intended to fill financing gaps on a project and requires that 80 percent of the total project cost be funded through other sources, including conventional lending or certain bond financing, equity from the project owner or investors, other government or public subsidy (grants/loans, etc.), and private donations and/or fundraising. The common minimum size of most NMTC projects is around $8 million (generating under $2 million in actual funds) and over $10 million may require multiple sources of allocation. The tax credits are highly competitive and awards are made through certified Community Development Entities (CDEs). If the commercial component of the Lot D redevelopment, such as a possible museum or other project has significant direct benefit to low income people and is within the mission of a CDE, NMTC may be an option.

iii. EB-5

The EB-5 program is a federally-authorized visa category created by Congress in 1990. The primary concept is to encourage foreign investment in job-creating U.S. economic development projects or companies in return for a U.S. green card. These projects or companies must create or retain 10 full-time jobs, and a minimum investment of $1M is required. This investment can be reduced to $500K if the investment is made in a high unemployment or rural area. EB-5 projects are typically financed through Regional Centers, which can accept the investment from the green card-seeking investor. The U.S. government sets aside 10K green cards each year for foreign investors participating through designated Regional Centers. The centers invest in projects that meet all of the program criteria. Like NMTC, EB-5 is a complex tool, and there are significant investment and timing rules that must be followed. Consult and work only with reputable and qualified Regional Centers, immigration lawyers, and project finance experts.[9] Due to the jobs requirement, EB-5 would be appropriate for the commercial components of the project. The North Dakota/Minnesota Regional Center (http://ndmneb5.com/) has been very active in both states and is a reputable regional center.

[9] Council of Development Finance Agencies. (n.d.) EB-5 Resource Center. Retrieved from: https://www.cdfa.net/cdfa/cdfaweb.nsf/resourcecenters/eb5.html

## Part IV: Maximizing Opportunity for Growth along Waterfront

Duluth's location on Lake Superior places a natural constraint on the city's development opportunities between downtown and the waterfront. The City has indicated that they will be conducting a reassessment of the waterfront parking and development opportunities that will inform future development decisions in the Canal District and Bayfront. Such a study should include an in-depth analysis of market opportunities. The suggestions below will assist the City in identifying their best opportunities and assets related to attracting new businesses, increased visitors, and improved experiences.

i. Complete a Market Study to Identify Retail Opportunities

   The Developer for Lot D has indicated a certain amount of retail on the site, but the specifics are unknown. For years, the strongest concentration of retail near downtown and waterfront has been located in the Canal District. A market study would indicate the likelihood of successful retail business at Lot D and identify what types of retailers might be targeted. Although the Developer has likely completed some of this research already, the City should complete its own study for the site and/or the entire district.

ii. Complete a Parking Study for Downtown and Waterfront

   One of the major challenges for Duluth is to provide enough parking throughout the City, particularly along the waterfront and in the Canal District. Major events and tourism attract approximately 6.5 million visitors each year. Much of the parking that is currently available consists of surface parking lots, many of which are located in heart of the Canal District. As the City strives to maintain the waterfront overflow parking that has historically been accommodated at Lot D, it should investigate more permanent and convenient parking opportunities that might allow for existing surface lots in the Canal District to be redeveloped into more aesthetic and higher revenue-generating uses. A well-designed parking garage (with associated shuttle service for waterfront events) would relieve parking demand while opening up new development opportunities in the thriving tourist area. An in-depth parking study completed by a third party would indicate projected demand, evaluate parking management and governance structure, and identify practical strategies to address parking needs.

# Additional Resources

CDFA Brownfields Financing Toolkit |
http://www.cdfa.net/cdfa/cdfaweb.nsf/ord/201502_BF_Toolkit/$file/CDFA%20Brownfields%20Financing%20Toolkit%2002.02.15.pdf

CDFA Online Resource Database |
http://www.cdfa.net/cdfa/cdfaweb.nsf/ordsearch.html

CDFA Advanced Bond Finance Reference Guide |
https://www.cdfa.net/cdfa/store2.nsf/browse.html?open&so=popularity

Economic Development Administration Funding Opportunities |
https://www.eda.gov/funding-opportunities/index.htm

BUILD Grants |
https://www.transportation.gov/BUILDgrants/about

Transportation Infrastructure Finance and Innovation Act |
https://www.transportation.gov/buildamerica/programs-services/tifia

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