

 <p style="text-align: center;"><b>Council Communication</b> Office of the City Manager</p>	<b>Date:</b> October 10, 2011
	<b>Agenda Item No.</b> 24 <b>Roll Call No.</b> <u>11-1714</u> <b>Communication No.</b> <u>11-640</u> <b>Submitted by:</b> Don Smithey, Aviation Director and Allen McKinley, Deputy City Manager

**AGENDA HEADING:**

Recommend Approval of Termination Agreement For United Parcel Service, Inc. Leases

**SYNOPSIS:**

On September 14, 1999, by Resolution No. A99-317, the Airport Board recommended to the City Council, approval of a Land Lease Agreement with United Parcel Services, Inc. (UPS) for 30.74 acres of Airport property on which UPS was to construct a new sort and distribution facility. On October 18, 1999, by Roll Call No. 99-3257, the Des Moines City Council approved the lease.

Due to changes in their business model, UPS has requested a negotiated termination of this lease. As the overnight shipping market decreased significantly over the last decade, UPS has focused their efforts on development of markets in Asia. The company’s strategic plan no longer includes construction of the sort facility on this leasehold.

**FISCAL IMPACT:**

Amount: A cash payment of \$12,330,000 would be made by UPS no later than October 30, 2011, of which \$7,330,000 would go to the operating fund of the Airport and \$5,000,000 would go to the City of Des Moines. UPS will continue to lease space in Buildings 31 and 32 and, combined with landing and apron fees, will pay the airport approximately \$1,571,000 annually

Funding Source: Airport Enterprise Fund and City Fund(s) to be determined

**ADDITIONAL INFORMATION:**

The main provisions of the lease include:

- The lease requires UPS to construct a new sort and distribution facility of at least 250,000 square feet with a construction cost of not less than \$12,000,000 with a deadline for construction of the new facility of December 31, 2003. (The new facility is to remain under the ownership of UPS throughout the lease term thereby requiring the payment of ad valorem taxes by UPS. The City is to provide a 10-year partial declining exemption from taxation on the facility and improvements.) Although UPS has not constructed the sort facility, a payment in lieu of taxes (PILOT) provision requires UPS to pay the City an amount equal to the taxes it would have paid had they built the building in 2003.
- The Lease has a term of thirty (30) years beginning on January 1, 2000, and expiring on December 31, 2029, with two additional option periods if exercised by UPS. The first option period is

for a term of twelve (12) years and six (6) months. The second option period is for a term of ten (10) years.

- The initial leasehold was for 30.74 acres of land, including a portion of “old” Army Post Road. By amendment, additional land has since been added to the leasehold bringing the total to approximately 43.5 acres.
- The Lease obligates the Airport to install a traffic signal at SW 28th Street and Relocated Army Post Road, and install water, telephone, and sanitary sewer to the site.
- Ownership of all buildings and improvements constructed on the leasehold revert to the Airport upon termination of the Lease. The fifth amendment to the lease imposes a \$2 million payment if the facility is not completed by December 31, 2014.

The lease agreement has been amended five times for various reasons, such as adding optional land to the lease, extending the deadline for completion of the facility, and adjusting the monthly land lease rental rate. The current monthly rent amounts to \$42,161.71. Due to changes in their business model, UPS has requested a negotiated termination of this lease. As the overnight shipping market decreased significantly over the last decade, UPS has focused their efforts on development of markets in Asia. The company’s strategic plan no longer includes construction the sort facility on this leasehold.

Negotiation of a settlement began in May 2011 and both sides have come to a tentative agreement subject to final approval by both parties. The two primary elements considered in the settlement were (1) the value of future lease payments and construction to the Airport and (2) the PILOT due the City of Des Moines. The proposed settlement amount is \$12,330,000.

In consideration of the value of future payments and construction to the Airport, staff completed a net present value calculation of the land lease payments to be made by UPS between October 2011 and December 2029. At a discount rate of 3%, the calculation amounts to a net present value of \$7,121,344. Current leases on buildings 35 and 48 extending through 2014 are also included in the termination agreement. As consideration for lease payments not received on these two buildings, estimated demolition and refurbishment costs of approximately \$208,000 have been added to the settlement, bringing the total amount to \$7,330,000.

Two other elements of the existing lease include the \$2 million payment for not completing the building by December 31, 2014, and the fact that the Airport would take possession of the building at the end of the lease. For purposes of settlement, both of these items were given minimal consideration because: 1) the sort facility would have limited, if any, salvage value at the end of the lease, and 2) if the agreement is terminated prior to December 2014, there would be no claim to the \$2 million.

In consideration of the value of future payments related to the PILOT/property tax payments (including the impact of tax abatement) through December, 2029, staff also completed a net present value calculation. Utilizing a 3% discount rate the NPV was computed to be \$4.3 million. The \$5 million payment will need to be incorporated into this year’s budget process and should be used in conformance with Council’s guiding principles that includes not using one-time revenues to balance the budget. In receiving this payment of \$5 million the City will be losing an annual revenue of approximately \$400,000. Thus, staff will be looking for a method to hold all or a portion of this payment in a manner that can release at least the equivalent amount annually to fund the operating budget for a significant length of time.

#### **PREVIOUS COUNCIL ACTION(S):**

Date: October 18, 1999

Roll Call Number: 99-3257

Action: On a Lease Agreement with United Parcel Service, Inc., for the leasing of 2401 Army Post Road for the construction of a parcel sort center and other facilities. (Council Communication No. 99-470). **Moved by Hensley to adopt. Motion Carried 6-1. Pass: Flagg.**

**BOARD/COMMISSION ACTION(S): NONE**

**ANTICIPATED ACTIONS AND FUTURE COMMITMENTS: NONE**

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