

## Eisenhower Golf Course Assumption Overview

### Comments and Observations

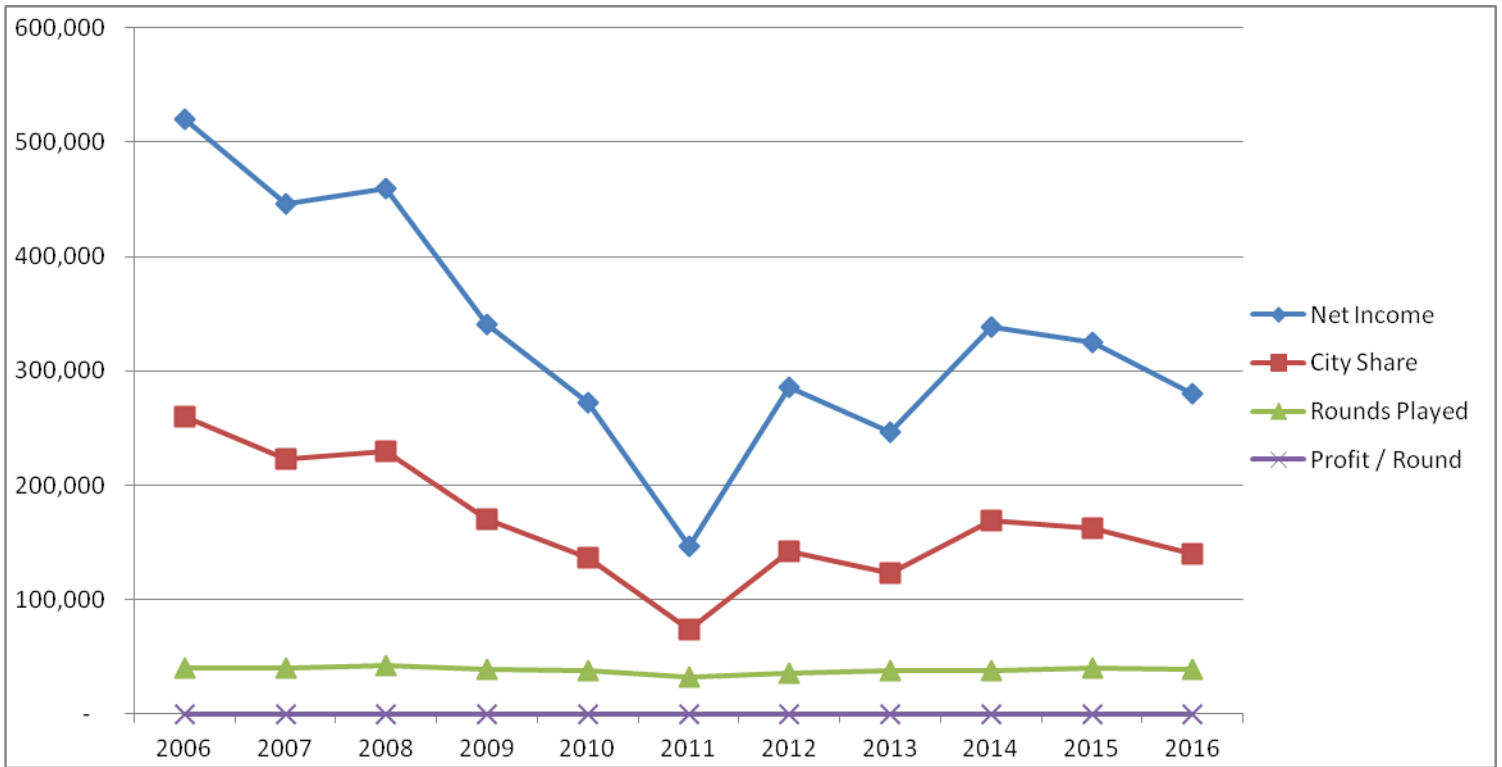
#### *Requests for Proposals/Bids:*

In July 2013, the City issued a RFP to sell the Eisenhower Golf Course and received three proposals: Friend Brothers, Erickson Living Properties and Caruso Homes. The City rejected these proposals in the best interest of the City. Only one proposal would continue operating the golf course, while the other two were contingent on the ability to re-zone and develop property zoned open space which is unlikely.

In October 2017, the City contacted parties that had previously expressed interest in the Eisenhower Golf Course, including Mr. Jeffery Rice, Fort Meade and Mr. Friend. No party was willing to match the County's offer.

#### *Historically, what does golf course make on an annual basis*

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Net Income	520,042	445,474	458,960	340,836	272,586	146,761	285,398	246,701	338,215	325,476	279,791
City Share	260,021	222,737	229,480	170,418	136,293	73,381	142,699	123,351	169,108	162,738	139,896
Rounds Played	40,512	39,950	42,248	39,458	38,109	32,945	36,278	38,377	38,352	40,092	39,098
Profit / Round	12.84	11.15	10.86	8.64	7.15	4.45	7.87	6.43	8.82	8.12	7.16



*Change in revenues, rounds and profit per round- FY 2006 compared to FY 2016*

Net Income	-46.20%
City Share	-46.20%
Rounds Played	-3.49%
Profit / Round	-44.25%

**Year to Date Activity**

The County reported year to date net income through September 2016 of approximately \$130,000 as compared to budget of \$151,000.

**Why the rush?**

From the City’s perspective, the option of selling the Eisenhower Golf Course has been evaluated since 2013. Acknowledging that the County lease would be terminating, the City’s administration looked at different options, including extending the current lease with similar terms and conditions, assuming the operational responsibilities of the golf course, and selling the property while retaining open space and recreational uses in order to protect the City’s water supply aquifer. The City evaluated these different options over a long period of time which by virtue of taking a prudent approach may result in the City recognizing a much higher return on investment than if it had accepted one of the earlier offers- over two times the proposed offer. Simply put, the City is not/ did not rush to reach this conclusion.

**Financial Analysis**

**Recapitalization Costs**

	County Estimate	3rd Party Estimates	
Clubhouse (10K sq. ft.)	1,806,000	2,600,000	Two local firms estimates range \$200 - 325 / sq. ft.: midpoint \$260
Bunker/Green Renovations	1,500,000	1,800,000	GCBAAs estimate
Tree Pruning	100,000		County estimate:
Tee/Fairway Renovations	120,000	859,281	GCBAAs estimate
Irrigation Renovations	725,000	2,561,286	GCBAAs estimate
Cart Path	200,000	200,000	County estimate:
Permits	250,000	250,000	County estimate:
Subtotal	<u>4,701,000</u>	<u>8,270,567</u>	
Other costs			
Drainage- pond	500,000	500,000	County estimate:
Subtotal	<u>500,000</u>	<u>500,000</u>	
Full 18 Hole Renovation	<u>5,201,000</u>	<u>8,770,567</u>	

### *Revenue and Expense Projections*

Based on the current business projections of the Golf Course industry, player rounds have decreased sharply over recent years and future industry projections do not show significant growth. Although the City's Eisenhower Golf Course player rounds do not reflect significant decreases year over year, profit per round has decreased significantly by over 44% during the last 10 years. Similarly, net income has decreased by over 46% during the same time period.

Furthermore, annual debt service payments ranging between \$282,000 and \$471,000, depending upon final re-capitalization costs, would need to be included in future projections. Arguably, revenues would also increase because of improved and/or expanded facilities; however, assuming rounds would/could not increase materially because they are at near maximum levels, then fees and other revenue sources would need to increase accordingly. This leads to a fundamental question- why should the City want to assume the business risk of this enterprise?

By example, if improvements are made and debt service incurred without appreciable new revenue, the City could be exposed to losses ranging between \$1,700 and \$475,000.

### *Net Present Value of Cash Flows*

One of the financial evaluation tools commonly used to assess an investment is the net present value (NPV) of cash flows. Simply put, this tool discounts the value of a series of payments (net income) that is received over a period of years at a given interest rate which can then be compared to the sales proceeds one would receive at time of sale. Another way of thinking about it is; how much money needs to be invested today at a given interest rate to reach the sales price. Given this relationship, if the NPV of cash flows is greater than the sales price then the sale should not be recommended because the investment will yield a higher rate of return and is therefore is a better financial option. However, conversely if the NPV of cash flows is less than the sales price then the sales should be recommended because the sales price exceeds the expected rate of return for the same investment.

A break even scenario whereby the sales price, approximately \$3.1million, essentially equals the net present value of cash flows over a period of 30 years, includes using the following assumptions: because the golf course is anticipated to be closed for year one and two for construction and rehabilitation, no revenues would be factored for these two years; in year three net revenues start at \$200,000 and grow at 3% annually over the next 30 years reaching \$345,000; and interest rates increase incrementally over the next 10 years and plateau to 5.5% for the remaining 20 years.

Because of business and economic risks, there is no guarantee that any of the above assumptions would hold, and most likely the assumptions would not. As a consequence it would be necessary for the City to assume the associated risks and realize the outcomes if it does not sell the golf course.

For example, how likely is the potential that the golf course will earn \$400,000 the first year it re-opens? Based on the current agreement whereby the City shares 50% of net income/loss, in order for the City to receive that payment, operations would need to net \$400,000.

The interest rate which is another component of the analysis can be volatile and hard to predict. Although interest rates have been somewhat constant over recent years, there have been economic cycles that are quite the opposite. If the interest rate assumption changed slightly whereby it increased .025% each year starting in year two, the net present value of cash flows would decrease by approximately \$500,000. Simple changes in interest rates may have material impacts on net present value results.

Recognizing that there are uncertainties in future revenue and expense forecasting, interest rate and other business assumptions, simply put, if the City wants to maintain ownership of the Eisenhower Golf Course it needs to develop a business model that has sufficient certainty to achieve NPV exceeding \$3,100,000, otherwise, the City should consider the County's offer.

*Revenue and Expense by year*

	<i>Fiscal Year</i>				4 Year Average	With Bond Amortization
	2016	2015	2014	2013		
<b>Revenues</b>						
Green Fees	664,281.00	734,080.00	695,535.00	672,742.58	691,659.65	664,281.00
Cart Fees	301,110.00	326,927.00	310,349.00	300,281.06	309,666.77	301,110.00
Driving Range	38,976.00	41,852.00	41,647.00	39,405.56	40,470.14	38,976.00
Golf Cards	54,300.00	61,560.00	59,425.00	59,732.00	58,754.25	54,300.00
Pro Shop	98,899.00	110,921.00	122,945.00	121,855.80	113,655.20	98,899.00
Food	83,592.00	110,619.00	110,437.00	100,694.22	101,335.56	83,592.00
Beverages	90,753.00	91,987.00	86,921.00	81,799.91	87,865.23	90,753.00
Rentals	10,421.00	8,426.00	6,771.00	1,371.08	6,747.27	10,421.00
Clinic	29,201.00	27,892.00	31,371.00	20,160.28	27,156.07	29,201.00
Monthly Dues	56,799.00	65,201.00	71,975.00	55,450.00	62,356.25	56,799.00
Miscellaneous	2,814.00	11,181.00	32,427.00	11,775.50	14,549.38	2,814.00
	<u>1,431,146.00</u>	<u>1,590,646.00</u>	<u>1,569,803.00</u>	<u>1,465,267.99</u>	<u>1,514,215.75</u>	<u>1,431,146.00</u>
<b>Expenses</b>						
Cost of Goods Sold	123,204.00	144,155.00	137,265.00	135,082.94	134,926.74	123,204.00
	70.67%	71.15%	69.55%	74.02%	71.31%	70.67%
Labor						-
Golf Operations	129,726.00	120,922.00	120,328.00	123,511.28	123,621.82	129,726.00
General / Admin	82,304.00	95,958.00	83,473.00	60,919.22	80,663.56	82,304.00
Maintenance	192,734.00	208,611.00	175,646.00	168,121.24	186,278.06	192,734.00
F&B	41,710.00	50,908.00	45,598.00	39,732.17	44,487.04	41,710.00
Subtotal	<u>446,474.00</u>	<u>476,399.00</u>	<u>425,045.00</u>	<u>392,283.91</u>	<u>435,050.48</u>	<u>446,474.00</u>
Benefits						
Taxes	40,098.00	42,715.00	37,850.00	39,654.88	40,079.47	40,098.00
Health	22,889.00	23,059.00	22,670.00	23,006.22	22,906.06	22,889.00
Workers Comp	7,875.00	8,470.00	10,687.00	1,127.40	7,039.85	7,875.00
Subtotal	<u>70,862.00</u>	<u>74,244.00</u>	<u>71,207.00</u>	<u>63,788.50</u>	<u>70,025.38</u>	<u>70,862.00</u>
Total Labor	<u>517,336.00</u>	<u>550,643.00</u>	<u>496,252.00</u>	<u>456,072.41</u>	<u>505,075.85</u>	<u>517,336.00</u>
<b>Operating Expenses</b>						
Golf Ops	37,325.00	34,410.00	33,406.00	45,423.56	37,641.14	37,325.00
G&A	193,335.00	223,497.00	261,681.00	230,092.38	227,151.35	193,335.00
Maintenance	152,544.00	161,922.00	134,996.00	137,860.49	146,830.62	152,544.00
F&B	9,979.00	16,333.00	13,013.00	13,081.27	13,101.57	9,979.00
Sales and Marketing	14,072.00	13,676.00	12,663.00	10,989.99	12,850.25	14,072.00
Golf Cart Leases	42,180.00	60,278.00	52,351.00	65,824.51	55,158.38	42,180.00
Equipment Leases	29,857.00	25,446.00	50,846.00	57,674.63	40,955.91	29,857.00

PP Taxes	2,199.00	5,879.00	5,210.00	8,380.83	5,417.21	2,199.00
P&C Insurance	29,324.00	28,806.00	33,903.00	29,138.45	30,292.86	29,324.00
Debt Service						281,410.00
Subtotal	510,815.00	570,247.00	598,069.00	598,466.11	569,399.28	792,225.00
Total Expenses	1,151,355.00	1,265,045.00	1,231,586.00	1,189,621.46	1,209,401.87	1,432,765.00
Net Income	279,791.00	325,601.00	338,217.00	275,646.53	304,813.88	(1,619.00)
	279,791.00	325,601.00	338,215.00	275,646.53		
	-	-	2.00	-		
Rounds Played	39,098	40,090	38,350	38,377	38,980	38,980
Net income / round	7.16	8.12	8.82	7.18	7.82	7.82

### ***Condition of Course/Facilities***

In May of 2016 the United States Golf Association issued an "On-Site Visit Report." The report is a very extensive third party analysis of the City asset. In summary, the report finds the asset to be in very poor condition while noting that a "significant investment will be needed...."

Similarly, when comparing the life expectancy of assets located at Eisenhower Golf Course as provided by the Golf Course Superintendents Association of America, GCSAA, the golf course current capitalized assets far exceed the projected years.

### ***Incremental Improvements***

Because of the scope and materiality of the improvements outlined above, it will be necessary to close the golf course for a period of time- estimated up to 24 months. Arguably, this could be done over phases, such as 9 holes at a time; however, this approach would elongate the improvement cycle and would only increase financial constraints.

### ***Open Space funds for improvements***

Over 75% of the Open Space funds that the County has allotted to the City can only be used to acquire property and cannot be used to make physical improvements. The approximate 23% of the City's Open Space funds that can be used for improvements have been earmarked by the City's Park and Recreation Department for City park improvements.

### ***Management Agreement w/ County***

Currently, the City has an operating lease agreement with the County whereby each has a 50%-50% participation in operating net revenues. Although the City does not maximize revenues under this arrangement, the benefit is that the City minimizes risks and eliminates the debt associated with capitalization costs from the City's financial statements.

### ***Maintaining Open Space Protection***

The Administration is very concerned about ensuring that this property be maintained as open space, especially as it has an inherent interest in safeguarding the City's water supply. Accordingly, the City expects to include "belts and suspenders" to insure that the property remains open space via deed restrictions and conditions of any purchase and sale agreement.

### *Public Policy Considerations*

- ***Risk***

An important component providing City services is a risk assessment. This should include a comparison between community and personal benefit; e.g., do residents and tax-payers of the City benefit from the risk/reward relationship or do other entities/individuals? If there are underlying risks, can the City effectively control potential outcomes and is service essential for the welfare of the community? Also, to what degree should the City assume operating and business risks for non-essential services?

- ***Opportunity loss***

The City should assess the opportunity loss that is presented by not pursuing this transaction. For example, the City continues to discuss using pay-go for capital improvements and other opportunities that have overall community benefits. Therefore, if the City does not accept this proposal it will not have additional pay-go funds to facilitate potential projects, and it will potentially have to increase borrowing to make golf course improvements while decreasing net revenues and increasing the amount of debt on the City's balance sheet- all having negative fiscal impact.

- ***Community maintains access to Golf Course/open space***

As noted above, in order to protect its water supply, it is imperative that the City protect the Eisenhower Golf Course property as recreational open space. As such, the residents of the City of Annapolis will not lose access to Eisenhower Golf Course.