Robert J. Long
Village Attorney

Memo

To: Mayor Hanson, Trustees, Staff, Interested Parties

From: Robert J. Long

Date: 10/21/2015

Re: Deercrest, Clublands, SSA-1 and SSA-2

As you are aware, the Board was approached about a year and a half ago by Troy Mertz, who proposed that the Village refinance Neumann's SSA bonds and thereby assist him in re-starting development in the Clublands and Deercrest subdivisions with the additional benefit of lowering the tax burden on existing homeowners. The special meeting of October 28th will introduce the final product of the last 18 months of discussions to the board and public. This memo is intended to give some history and background to this proposal and to Staff's recommendations.

Background

The two Neumann Homes developments were born out of the settlement of a multi-party lawsuit. The main issues were the density of housing proposed on the two properties and on the sewer connection. Facing a difficult time in court, the Village and County opted to work out an agreement to allow Clublands and Deercrest to have certain maximum densities and to fund part of their roads, water lines, sewers and the deep well along with a host of other qualifying improvement costs with the proceeds of special tax bonds. There was to be one bond for Deercrest (SSA-1), an initial one for Clublands (SSA-2) and a third one for Clublands coming sometime later on once development moved into the southern half of that property. Both SSA-1 and SSA-2 were approved by the Village Board, the bonds were sold to institutional investors and the proceeds were used on the public improvements in both subdivisions.

Home sales were initially brisk, but the economy cooled, and Neumann showed signs of financial weakness. Ultimately, the company collapsed, the Village declared it in default and it ended up filing bankruptcy, leaving a chain of incomplete subdivisions in about 5 states stretching from Michigan to Colorado.

In both Deercrest and Clublands, Neumann's demise meant that there were incomplete roads and sewer lines. Raccoons moved into half-completed houses. Properties intended for public or subdivision parks were left with huge piles of dirt. Residents were extremely worried about losing the entire value of their investments.

Additionally, Neumann hadn't paid all of its contractors and lien claims against the Village started to pile up.

At the direction of the Mayor and Board, Staff enlisted the assistance of outside attorneys and acted to lay claims on the surety bonds that secured Neumann's obligations to the public. This took nearly 7 years of very complicated and difficult litigation and negotiations, with one case going all the way to the Illinois Supreme Court. But, the end result was that the surety companies paid for the pavement, the curbs and gutters, the completion of the sewer and water lines, some of the costs of the deep well and many park improvements. This includes the wonderful public space at Sprenger Park. The lien claims have also been fully resolved.

While this was going on, Neumann's banks foreclosed on the remaining vacant lots and unplatted land in the two subdivisions. They sat on that land for a long time, and were unable to sell them due to the global recession we're still working our way out of. Some of the banks went into receivership, evidence of the difficult financial environment.

The remaining bright spot was that the work and effort of the Village through the Mayor, the Board, Staff and attorneys had stabilized the two subdivisions, had gotten the infrastructure working and the land was ready for a new developer to come in and resume building homes once the economy improved. If that work had not been done, we would be facing a much different picture today.

Over several years, the banks brought a number of would-be developers in to talk to Village Staff and one, the Walton Group came forward with a formal proposal to revive the Clublands a couple of years ago, but they eventually pulled out. Shortly afterward, the Village was informed that Troy Mertz had bought all of the undeveloped property from the banks and was intending on moving forward with a redevelopment and refinancing proposal.

Staff's Marching Orders

The basic proposition Mr. Mertz made was to refinance both of the SSA-1 and SSA-2 bonds at today's much lower interest rates, reducing the amount needed to service that debt annually. He said the difference would reduce the burden shouldered by the homeowners and restart development. He came before the Village Board in the summer of 2014 and the Mayor and Board directed Staff to work with him to come up with a concrete proposal for their consideration.

From this directive, Staff and the undersigned have engaged in months-long discussions, analysis and negotiations. During this time, we have tried to examine every possible scenario and financial projection available. We have secured the services of a financial planner knowledgeable in the world of municipal bonds. We hired an outside bond attorney. We have asked for, received and reviewed confidential financial information from Mr. Mertz. We have had numerous live and telephone conferences with all our team, with Mr. Mertz and his counsel and the proposed bonding company. To the best of our ability, our research and analysis has been thorough and careful.

The proposals themselves started with a basic idea composed of three primary parts:

1. Arrange refinancing ("refunding") of the SSA-Bonds;
2. Secure a waiver ("abatement") of some unpaid taxes on the vacant land;
3. Restart development in both subdivisions.

Our marching orders were to examine the proposals with the following cardinal rules in mind:

1. Protect the current landowners in Deercrest and Clublands;
2. Protect the Village as a whole;
3. Allow Mr. Mertz to resume development at current market conditions once the first two objectives are met.

We have never wavered from those marching orders. We believe that Staff support for the current proposal is based on sound application of those rules, understanding the reasonable ability of Staff and the undersigned to guard against future events which may be unpredictable and chaotic.

The Financial Proposal

It took a substantial amount of time and effort to bring the current proposal into a concrete form. This is because of the complexity of the financial mess left behind by Neumann's bankruptcy and the foreclosures, compounded by the collapsing and then recovering national economy. Rather than recite how the proposal moved through the negotiation process, we will outline and explain what it ended up being.

1. The two SSA bonds will be collapsed and merged into a new, single bond, although the two SSAs themselves will remain intact.
2. The County will be asked to abate unpaid SSA taxes on the vacant lands.
3. The Village will enter into a new redevelopment agreement with Mr. Mertz relating to Clublands.
4. The Village will entertain Mr. Mertz's current petition to resubdivide part of Deercrest, by reducing the number of townhomes to a smaller number of age-targeted single family homes.

There are many details involved in this proposal, of course. Looking at the big picture first, joining the SSA bonds into one issuance will allow there to be two series ("tranches") of bonds. The first series will qualify for insurance coverage, and will be mainly secured by current homes which have a history of paying the SSA taxes. This produces a significantly lower interest rate. The second series is at a little less favorable rate because it's secured by the development potential of the vacant land and will be targeted at larger investors willing to take that risk.

The overall plan will allow the SSA bonds to be refinanced now at a much lower interest rate than was available 13 years ago. Individual property owners should see lower taxes in the future. There is no risk that the taxes will increase over the maximum rates established before the owners bought their homes from Neumann. There is no risk that the taxes will burden properties longer than with the existing bonds.

Risk Factors and Analysis

There are still risks of course. At present, there's the potential for either or both of the SSA bonds to go into default, which would negatively affect the Village's bond rating and increase the cost of municipal borrowing. It would likely halt the potential for any future redevelopment of the two subdivisions for an extended period of time. The Village would also have to shoulder continuing administrative expenses. While the individual homeowners' responsibilities would not continue past the 2033 maturity dates, the vacant land would remain burdened by debt and there is the potential for foreclosure or bankruptcy proceedings resulting in unpredictable rulings and burdens.

One of the biggest risks the Village and the homeowners currently face is that if nothing is done to stabilize the SSA bond situation and restart development, the approximately 800 vacant lots and parcels could be sold for unpaid taxes to a large number of individual investors. That would mean that no one entity or person would ever be identified as a subsequent "developer". That would also mean no clubhouse in Clublands, no storm sewer improvements along Miller Road and incomplete raw lands in phases 3 East and 4 of Clublands sitting vacant for many years to come. It could have a much less negative effect in Deercrest, however.

Balanced against this is a diminished risk that the proposed new bonds (particularly the more risky second series) could fall into default. While this is not a good thing, at least the amount of the default would be greatly diminished and the way the proposal works, the Village wouldn't be burdened to the same extent with administrative expenses. The individual homeowners would still remain fully protected with each owners' responsibilities ending not later than the 2033 maturity.

The Redevelopment Proposal

With the property tax abatement and the refinancing of the bonds burdening the vacant land, Mr. Mertz proposes to engage one of the national homebuilders he's been in contact with to start marketing and building homes in both Clublands and Deercrest. There are about 56 lots in Clublands and around 38 in Deercrest which are eligible for building permits presently, provided that the proposed houses meet platted guidelines and village codes.

In Deercrest, Mr. Mertz has already started the replatting process. The Board is encouraged to let the matter work its way through the PZB and avoid prejudging any aspect of this proposal. It is fair to state that there have been positive comments to date on this proposed replatting, but also an objection that may be worked out in coming weeks. Whether the replatting is ultimately approved does not seem to be a highly material impediment to the financial proposal's success, however.

In Clublands, Mr. Mertz has come forward with a proposal similar to that negotiated with Walton a couple of years ago. He has expressed confidence that he will secure reasonable buy-in from the Clublands HOA on it. Basically, he would abide by all existing platted rules and regulations, ranging from required best management practices on White Lake to the building of a clubhouse. The expense of the clubhouse was a major reason other developers weren't interested in Clublands over the past 8 years. Mr. Mertz has offered to build a somewhat smaller clubhouse with related downsized amenities with construction to start in about two years, if and when some houses are sold and the pace of development starts to pick up.

An additional big-ticket item in Clublands is the Miller Road stormwater system. This plan entails the construction of a drainage basin in the southeastern part of the subdivision with an overflow leading to Old Mill Creek and downstream to the DesPlaines River. Mr. Mertz will have to fund that improvement before he can obtain building permits for any lots in Clublands beyond the 56 mentioned above.

Among Mr. Mertz's ideas is age-targeted development. That is one of the issues he's brought forth in the Deercrest replatting proposal, and it's one which he's mentioned that he may bring up later on when he is in a position to resume development in phases 3 East and 4 in Clublands. There is no formal request for that currently pending, but it could be forthcoming if the housing market turns the way he expects it to.

Finally, the proposal kills the idea of a second bond issue on Clublands for all purposes.

Conclusion

Staff recommends approval of this proposal in concept, with bond ordinances and appropriate adopting resolutions to follow.

Respectfully submitted,

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Individually and for Staff
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