Dennison Building's low appraisals didn't sink sale-leaseback deal

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Photo credit: Ed Betz | The H. Lee Dennison Building in Hauppauge. (Oct. 8, 2013)

When the H. Lee Dennison Building was dedicated in 1973, Suffolk's first county executive, after whom the $16 million building was named, jokingly predicted that "this building is going to sink" because it was built over swampland.

Still mired after four decades, the Hauppauge building last week brought in $70 million in cash from a sale-leaseback deal even though two appraisers in September valued Dennison at one-third that price -- between $22.8 million and $24 million.

The deal, the product of special state legislation, allowed the Suffolk Judicial Facilities Agency to buy the building from the county and pay for it by selling bonds to investors. The agency then will pay off the bonds through rental payments from the county, which still occupies the building and will regain ownership in 2033.

"My personal feeling was how do we do this and sell something when the value comes in at $24 million?" said agency board member Michael O'Donohoe, county commissioner of jurors and a former Conservative county lawmaker. "But we were assured by everyone involved it was going to be OK."

"We were all surprised" by the appraisals, said Martin Cantor, the agency's chair. "But no one thought it would kill the deal."

He added that there was wide interest in the bond, which sold out in three hours. That's because the deal carried a higher interest rate -- an average 4.63 percent or about $26 million in all. That compares to 3.47 percent rate the county earlier paid in a $60 million fall borrowing for capital projects.

While the cash infusion will get the county through the end of this year, County Executive Steve Bellone is going to have to find a way to replace the one-shot revenue next year. In addition, the $4.8 million in annual rental payments over the next 20 years only widens, not narrows, the county structural deficit.

Because of the low appraisals, bond prospectuses clearly warned investors the $70 million price "is significantly greater than the appraised value of the facility" and warned in case of a default that "the sale price . . . may be significantly less than the amount due." It also warned that should an investor try to sell their bonds early, they could face a loss.

"We wanted every wart and risk factor to be plainly noted so the investor knows what they were buying," said Cantor.

Jon Schneider, deputy county executive, said the administration never considered backing away, despite the low appraisals, because the deal was always driven by the rental payments the county would make. "The most relevant number is the cost of new replacement construction would be $97 million," he said. "There's no thought we are leaving Dennison and leaving the JFA holding the bag. That ain't going to happen."

After years in which numerous one-shots were used up, Schneider said few options were left except Dennison, after Bellone took steps such as shrinking the payroll by 1,000 and closing the county nursing home. "You would need draconian cuts and the impact would have been devastating," Schneider said.

But others say the deal inflated Dennison's sale price and only exacerbates the county's fiscal woes. "This is one-shot revenues on steroids and contradicts every other claim in the Bellone narrative," said Paul Sabatino, former chief deputy county executive under Steve Levy.

O'Donohoe acknowledged the sale-leaseback is not a perfect solution. "The deal is expensive, but when you're in a hole, sometimes it costs you more to get out of it," he said.

Schneider said the public works department is studying if there are departments that qualify for federal aid for rent that can be moved into Dennison to lower costs, a review that should be finished by year's end. Cantor said the agency also hopes to save by retiring bonds early, perhaps within a decade.