

# Arena Review Panel

Report to City of Seattle Mayor and King County Executive

April 4, 2012

## **Executive Summary**

The City of Seattle and King County received a proposal from Chris Hansen to construct a sports and entertainment arena in SODO and bring NBA and NHL teams to Seattle. Before advancing the proposal to the City and County Councils for their consideration, the Mayor and County Executive named an Arena Review Panel to evaluate the proposal for three criteria:

- **Existing General Fund resources are protected;**
- **The City and County should be significantly protected from any financial risks; and**
- **The partnership should result in an investment into the community and region.**

The Panel consists of community members with extensive experience in finance, development, community services, and the sports industry. These community leaders reviewed financial information, spoke with experts, and heard from the public.

**Based on their review, the Panel believes that the proposal is favorable, has promise, and is generally consistent with the principles set forth by the Mayor and County Executive; however, there are many important issues to be worked through to ensure these principles are met and to address other issues of importance to the community. The proposal warrants the serious consideration of the City and County policy makers.**

The Panel recommends that the City and County continue to work with Chris Hansen to further refine details for the potential public/private partnership, begin the processes that are required to address the multitude of issues at play with a project of this nature, and begin to engage with other community members to broaden the perspectives on the proposal and work through issues identified.

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## **Section 1: Introduction**

On February 16<sup>th</sup>, 2012, the Mayor and County Executive received a proposal from an investor outlining the development of a multisport and cultural event arena in Seattle's SODO neighborhood. The proposal requested a public investment of \$200 million and included a number of provisions to ensure repayment of the public funds.

Following receipt of the proposal, the Mayor and County Executive named an Arena Review Panel and charged them with ensuring that the City and County General Funds were protected, that the public faced no significant financial risk, and that City and County participation would leverage an investment into the community.

The Arena Panel includes members with a broad background, including experts in finance, development, public services, employment, and the sports industry.

Panel members include:

<b>Jan Drago</b>	Former City and County Councilwoman – Co-Chair
<b>Lenny Wilkens</b>	Former NBA player and Coach – Co-Chair
<b>David Freiboth</b>	Executive Secretary, ML King County Labor Council
<b>Doris Koo</b>	Former President & CEO, Enterprise Community Partners
<b>Karen Lee</b>	CEO, Pioneer Human Services
<b>Estela Ortega</b>	Executive Director, El Centro de la Raza
<b>Greg Smith</b>	CEO, Urban Visions
<b>Dr. Jill Wakefield</b>	Chancellor, Seattle Community Colleges

Financial Adviser to the Panel:

<b>Maud Daudon</b>	President & CEO, Seattle Northwest Securities, & Interim President & CEO, Seattle Metropolitan Chamber of Commerce
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The Panel convened on February 29, 2012, and held several public meetings. The Panel considered information from City and County staff and experts with a variety of relevant background, heard from Chris Hansen, and also received public comments and questions submitted both in writing and verbally.

Video archives of these meetings can be found here:

- [February 29, 2012](#)
- [March 8, 2012](#)
- [March 12, 2012](#)
- [April 4, 2012\\*](#)

\* Link to be added once available



**Materials considered by the Panel can be found online at:  
[www.seattle.gov/arena/materials.htm](http://www.seattle.gov/arena/materials.htm)**

The Panel's short time frame for review limited their scope to the specific areas described in the subsequent sections of this report. Additional issues which arose during the Panel's review have been noted in the report for further consideration by the City and County.

## **Section 2: Proposal**

This section provides a high-level summary of the proposal from Chris Hansen. The Panel recognizes that the proposal received by the City and County on February 16<sup>th</sup>, 2012, was at a high level, with many details that still need to be worked through.

The proposal requests up to \$200 million in public funds (combined from the City of Seattle and King County) towards the development of an approximately \$500 million multipurpose arena (sports and cultural events) to be located in Seattle's SODO neighborhood. The investor group would also be responsible for acquiring NHL and NBA franchises.

The public investment would be repaid by team rent and tax revenue directly attributable to the arena. No new taxes would be created or levied for the development of the arena. In addition, the proposal includes a number of provisions that are intended to provide financial security and mitigate risk for the City and County, as further discussed below.

The site for the proposed arena is directly south of Safeco Field in an area zoned for sports facilities. Chris Hansen's proposal is for his investor group to acquire all property required for the project through market transactions, which the Panel understands has largely occurred already. Beyond the public investment described above, all other arena costs, including potential construction cost overruns, are a responsibility of the investor group.

The investor group would construct the facility, built to pre-determined and agreed upon standards.

As proposed, there are two points in time at which public funds would be contributed to the project. *Prior* to the first contribution, several things need to have occurred, including:

- All land use processes are successfully completed;
- Both NBA and NHL teams are secured, with 30-year non-relocation agreements;
- Initial investor group financial obligations satisfied, including private funding of a security reserve; and
- Disclosure of members of the investor group and appropriate due diligence on their financial wherewithal would be completed.

With the above conditions and other requirements met, the first investment of public funds would occur and be used to purchase land for the arena site from the investment group at the properties' appraised value. At that point, the land becomes public.

Following this, the investor group would lease the site and begin constructing the arena facility. A rough estimate for this process is two years of construction. No additional public funding is required during construction of the facility.

Upon completion of the facility, including final permits, and satisfaction of pre-agreed upon construction standards and other conditions, the City and County would purchase the facility. The amount of this investment, combined with the prior land purchase, would not exceed \$200 million.

With the land and facility publically owned, the teams would enter into a 30-year lease to use the facility. The proposal includes a binding non-relocation clause that would be linked to term of the lease and guaranteed by a monetary damages provision. The NBA and NHL would recognize these agreements as well.

The investor group would operate the arena at their sole cost. Operating costs would include payments to the City and County of base rent, ensuring sufficient funding of the security reserve, annual contributions to a capital account, and payments to the City and County to cover any shortfalls in tax revenues. Visual depictions of these flows can be found online at: [www.seattle.gov/arena/materials.htm](http://www.seattle.gov/arena/materials.htm)

### **Section 3: Evaluation of Panel Charge**

The Mayor and County Executive charged the Arena Review Panel with evaluating the proposal in relation to three specific criteria. The specific criteria are:

- **Existing General Fund resources are protected.**
- **The City and County should be significantly protected from any financial risks.**
- **The partnership should result in an investment into the community and region.**

For each criterion, the Panel identified the aspects of the proposal that related directly to that criterion, and also concepts or issues that require additional consideration or investigation.

#### ***A - Existing General Fund resources are protected.***

*The City and the County provide critical public safety, health, educational, human services and other quality of life core services to the public. Any public-private partnership should not impair the provision of those services directly or indirectly, by creating financial pressure on general resources.*

#### **Arena Panel Findings**

The Arena Review Panel found that the intent of Chris Hansen’s proposal is to provide financial protections for both the County and City’s General Fund resources. Some of these protections include limiting the public’s obligation to rent from the arena and taxes derived from arena activity, as well as eliminating the public risk of cost overruns during construction. The proposal also puts the burden to cover revenue shortfalls on the investor group. Ultimately, the public investment will likely involve General Obligation bonds; in the event that all other protections are insufficient, the City and County are pledging General Fund resources and the full faith and credit of taxpayers to repay the City and County portion of any debt issued for the project.

#### **Responsive Components of Proposal**

- **Direct and Incremental Taxes Only.** Public dollars are invested based only on incremental existing taxes directly attributable to the new arena and rent directly from the investor group. Identified taxes include property tax, admissions tax, sales tax, business and occupation tax, and leasehold excise tax.
- **Agreement of Intent to Protect General Resources.** The terms of the proposal make clear that the intent is to protect the City and County general funds – this is an important common understanding in the partnership. As discussions continue, it will be important for all parties to continue working collaboratively to keep this key principle at the forefront and to memorialize it as irrevocably as legally possible in the detail documents.

### Additional Considerations

- **General Obligations.** Repayment of public investment is ultimately a liability against the City's and County's general funds, should all other recourses be exhausted. The proposal includes several financial protections for the City and County as described under the next principle to mitigate this risk.
- **Unknown Costs.** There may be additional capital and operating costs required in the area or costs for the City and County in oversight of the project. These costs and the source of funding should be examined and considered as they become known. The Panel understands that the investment group is proposing to cover direct operational costs, but as specific cost drivers are identified through the various review processes that lay ahead, it will be important to be clear about specific funding sources and expectations around these costs. Examples of such costs would be traffic and transportation improvements and mitigation, transit improvements, etc.
- **Substitution.** It is likely there will be some substitution effect with existing tax dollars, although this impact is likely to be modest. Substitution occurs when spending and resulting tax revenues that would have occurred elsewhere in the City and/or County occur instead at the arena. Shifting of spending would also occur should an arena be developed elsewhere in the region. This is something to continue to examine.
- **Key Arena.** Key Arena will need to adapt as additional entertainment venues come into existence in the region. While the solution for Key Arena has not yet been identified, all parties involved have committed to work together to explore potential options and find the best path ahead. This is demonstrated in part through Chris Hansen's proposal to fund a study that examines potential options moving ahead. As these options are considered, the City will need to evaluate the impact to Seattle Center's operations and its financial sustainability, and also any potential impacts on the City's General Fund.
- **Debt Rating.** City and County officials should evaluate potential impacts on municipal debt ratings given overall bonding plans. This evaluation was beyond the scope of the Panel. Changes in ratings could have an impact of the cost of borrowing for both entities.

### ***B - The City and County should be significantly protected from any financial risks.***

*The public should not bear any significant financial risk from the public-private partnership.*

### Arena Panel Findings

The Arena Review Panel found that the intent of Chris Hansen's proposal is to provide substantial safeguards and protections for the City and County from financial risk. Based on the review, many of the safeguards are unprecedented in arena public – private partnerships or are in sharp contrast to the arrangement between the City of Seattle and the Sonics. Some of these

protections include a multi-year security reserve, additional rent in the event of tax shortfalls, a non-relocation agreement covering the full term of any public financing, and capital expenditure reserves. The impact of many of these provisions is to shift risk from the City and County to the private investors. One primary area that needs additional scrutiny and attention is “What would happen in the case of bankruptcy or default by the investment group?”.

### **Responsive Components of Proposal**

- **Additional Rent.** The proposal includes an “Additional Rent” guarantee to cover any potential gaps between City and County annual financial obligations and the revenues received from base rent and direct taxes. This aspect of the proposal shifts forecast error risk from the public to private investors.
- **Security Reserve.** The proposal includes a “Security Reserve” that would initially provide a full year coverage for city and county financial obligations. The reserve grows by year 10 to reach 3 years annual average debt service. This reserve provides immediate cash flow for the City and County to pay financial obligations should the teams be delinquent in any payments. This cash flow will supplement continued tax revenues that are collected from activities that continue to occur in the arena during any financial challenges. Any excess funds in the security reserve will be used to prepay the public investment in the arena.
- **First Tier Lender.** The investors have offered the City and County a “First Tier” lender position. A “First Tier” lending position is meant to give the City and County first priority, ahead of other potential financial lenders, to take position of assets or revenues in the event of a default. The specific details of this still need to be determined. The panel understands that this may include first rights to assets and/or revenue streams. The City and County will want to ensure that these resources are sufficient to cover the public financial obligations should they be needed.
- **Non-Relocation Agreement.** The proposal states that the investors/team owners will sign a binding non-relocation agreement, ensuring the teams will not leave during the term of the facility lease. Should an ownership transfer of the teams occur, this agreement would be assigned to the new ownership group. This agreement would also be acknowledged by the NBA and NHL.
- **Conservative Financial Projections.** According to consultant Carl Hirsh and research conducted independently by staff, assumptions incorporated into the financial model are conservative and reasonable. The financial models allow for sensitivity testing to these inputs. Given the terms of the proposal, any shortfall in revenues relative to projections will be covered by the private investor group (the importance of assessing the financial strength of the group and its business model is discussed in later sections of this report).

## Additional Considerations

- **Unknown Team Operational Costs.** As the proposal shifts risk from the public to the private investors, there is an increased reliance on the financial performance of the teams and the leagues. City and County officials have not reviewed the overall business plan for the teams or leagues, and this creates uncertainty around the ability of the teams to meet obligations without risking financial hardship. This risk can be mitigated through strong security provisions and a financially strong ownership group.
- **Ramp Up of Security Reserve.** It would be prudent to include specific and regular “Security Reserve” minimum target levels to provide a regular ramp up of this reserve, avoiding the need for a larger lump sum payment in year 10. Clarity about the disposition of the security reserve at the end of the 30 years is also important.
- **Team Retention.** “Liquidated damages” is a financial penalty that is paid by the teams to the City and County in the event that the 30-year lease is prematurely terminated by a judge for some unforeseen reason. As proposed, the liquidated damages for noncompliance with the lease (such as team relocation) are sufficient to cover the outstanding public debt on the arena. Consequently, in later years of the lease, the amount of the liquidated damages declines and will prove a smaller disincentive to relocation. The City and County may consider an approach to liquidated damages that results in additional financial incentive for the teams to remain in Seattle, particularly towards the end of the end of the lease term. Considerations here could include payments for adverse impacts to the local community and businesses resulting from a premature departure of the teams.
- **Casualty Insurance.** The City and County are making a considerable investment in a valuable long term asset. It should be insured to the highest level, including broad casualty insurance as well as business interruption insurance. This should be a cost of the investor group.
- **Evaluate Strength of Ownership Group.** Much of the financial security of the proposal is tied to the performance of the arena. However, in the event that the arena does not perform as well as expected, the ownership group may be forced to contribute funds towards the additional rent payment. To ensure that the investors are able to meet this responsibility the City/County should ask Chris Hansen and the ownership group to agree to a third party evaluation of the financial strength of the ownership group.
- **Review Investor Business Model.** Similar to the above, the ability for the City and County to meet their debt obligations is ultimately dependent on the success of the arena and the NBA and NHL franchises. The City/County should ask Chris Hansen to agree to a third party evaluation of the investors’ business model to ensure that there will be sufficient revenue for the investors to meet their public obligations.



- **Strengthen Security to Backstop Rent Guarantee.** The proposal states that the investors will make additional rent payments equal to any shortfall in tax revenue sufficient to pay the City/County debt obligations. Security for this additional rent includes security reserve (equal to up to three years average debt service) as well as a first priority position on revenues from the arena. The City and County should consider other forms of additional security, including for example:
  - Pledged stake in specific assets, such as local TV revenues,
  - Letters of credit or collateral in allowable investments from the investors (investments that could be legally held by Washington cities and counties),
  - The right to the leasehold improvements in the event of bankruptcy, and
  - Define the role of the NBA and NHL in the event of team bankruptcy.
  
- **Consider Whether Local Market is Large Enough to Support Additional Teams.** Repayment of the public funds is largely dependent on the performance of the arena and teams (excluding security provisions). The City and County are likely unable to determine the extent to which the local market can support additional professional sports franchises. Ultimately, the NBA and NHL will provide their opinion on this through approval (or not) of locating franchises here for a minimum of 30 years. Regardless, accurately foreseeing the future over 30 years is impossible for any party, so the City and County should ensure that the final detailed form of security and risk mitigation provisions continue to protect both public partners.
  
- **Ensure that Investors will not Return to City/County for Additional Funds in the Future.** The public is making a large one time investment in the new arena based on assurances by the investors that there will be no additional public financing required in the future. The City and County should consider including in the transaction documents a covenant by the investors stating they will not request additional public financing in the future.
  
- **Potential for Risk Reduction in Later Years.** As the details on the disposition of surplus revenues are refined, consider opportunities to reduce public risk in later years, through pledging a portion of surplus revenues to additional security mechanisms or pre-payment of debt.

***C - The partnership should result in an investment into the community and region.***

*The City and County each target its limited resources on providing core public services. The arena proposal should offer the City and County with a potential opportunity to leverage outside resources to further enhance the community and region, by creating a new entertainment venue and spurring job growth and economic activity in the process.*

**Arena Panel Findings**

The Arena Review Panel found that Chris Hansen’s proposal offers a significant investment in



the community and the region. Bringing NBA and NHL franchises to the region have significant intangible benefits that make the region more vibrant and attractive. Thousands of jobs will be created in the construction and operation of the facility that might not otherwise happen. Unlike many development projects, this proposal's financing does not rely on economic multipliers or other external impacts (such as those that may result from induced or indirect job creation).

This type of project will have externalities associated with it, bringing both opportunities and challenges. Traffic and parking issues, particularly as they impact existing businesses and industry, will need to be carefully examined. The panel recognizes the proposal as an opportunity for both the community and the existing maritime and industrial uses to benefit from the arena and for a renewed focus on development in the area. The City and County have a variety of processes ahead to further evaluate the potential need for mitigation to protect existing investment in the area, and also should consider opportunities to bolster other important objectives including equity and social justice. The Panel felt that this proposal, in the context of a collaborative approach with stakeholders through future processes, could result in a best-practice example for the development of public/private partnerships and new sports facilities.

#### **Responsive Components of the Proposal**

- **Intangible Benefits.** Bringing NBA and NHL teams to the region represent an intangible benefit. Sports teams can bring communities together, add cultural vibrancy, and can make the region more attractive for people to live, work and visit. These benefits are not easily quantifiable, but do have a value.
- **Counter-Cyclical with MLB.** Significant activity related to Safeco field primarily occurs between April and October, depending on playoff status of the Mariners. NBA and NHL seasons offer regular activity during the other half of the year, typically between October and April. Having said this, there is some potential for overlapping schedules should the teams continue into playoff seasons, and with other major events, so careful coordination with existing teams will be critical to achieving the community benefit.
- **Other Tax Revenues.** While City and County general tax revenues generated directly as a result of this project are utilized for financing, tax revenues restricted for specific purposes and all tax revenues for other jurisdictions will accrue to support those purposes and jurisdictions. This includes the State of Washington, Seattle Public Schools, Port of Seattle, Sound Transit, King County Flood and Ferry Districts, as well as specific taxes received by the County and City for specific purposes including Metro Transit, Automated Fingerprint Identification Systems (AFIS), King County Parks, Seattle Emergency Medical Services, and County and City criminal justice and mental health programs.

### Additional Considerations

- **Jobs.** Construction and operation of the arena will create jobs locally. Consideration should be given to the kind of jobs that will be created both directly and indirectly as a result of the project, and also potential impacts to existing employment in the area.
- **Social Justice and Equity.** Opportunities for incorporating social justice and equity issues should be embraced, as well as opportunities for apprenticeships and job training that lead to family wage jobs.
- **Community Benefits.** The City and the County have an opportunity to guide additional benefits to achieve important objectives including equity and social justice. Consideration of these issues should be given in defining both how the arena will be constructed and operated, as well as how the arena will impact the local community.
- **Protection and Enhancement of Maritime and Industrial Activities.** Further study and assessment of State and City transportation infrastructure and parking availability is necessary to determine the ability of the system to adequately support both maritime/industrial uses and the new arena. Future studies should identify improvements to transportation infrastructure that could enhance access and operation of the Port of Seattle's cargo operations and other maritime and industrial uses.
- **Land Use Regulation.** Further study and assessment is needed of effective buffers and other regulatory tools to protect and enhance industrial uses on adjacent land.
- **Recognition of Pending Transit Investments.** Consideration should be given to pending improvements to the light rail system, including connection to Northgate and the eastside. There may be some disconnect between the opening of the arena and the completion of this linkage, so that will need to be considered as well in the traffic and parking analysis.
- **Impact to Local Community.** Development in any area results in changes. It is important to work collaboratively with the local community to evaluate and guide those changes in a positive way. This includes stakeholders in Chinatown/International District, SODO, Pioneer Square, the Port, the other two stadiums, and other neighbors.
- **Collaboration with Other Teams.** In order to foster a successful long-term working relationship, it will be important for the new teams to interact cooperatively with the existing teams, particularly when it comes to scheduling events, but also to ensure that all parties contribute constructively to making the area more vibrant over time. Some initial thinking on a longer-term vision for the area has been done by the two existing

public oversight boards for the stadium districts, and can be found online here:  
[www.stadiumdistrict.org](http://www.stadiumdistrict.org)

#### **Section 4: Due Diligence Checklist**

The following checklist summarizes the issues identified during the Panel's review that have arisen and warrant additional consideration by the City and County. Some of these include:

- Continued work to identify **unknown costs** such as impact on police or fire services
- Additional research on the **substitution effect**
- Review **investor business model**
- Review **financial strength of investor group**
- Increase **security reserve** deposits in earlier years to avoid large deposit at Year 10
- Include a **supplemental amount in the liquidated damages** provision to ensure lease compliance in later years
- Include the **disposition of tenant improvements** in the event of a default
- Provide broad range of **casualty insurance**
- Evaluate **Key Arena** operations to ensure long term viability
- Strengthen **security that serves as backstop to rent guarantee**
- Ensure City and County **retain first tier lending position** as investment group finalizes private lending agreements
- Be specific about **to which assets and revenues the first tier status applies**
- Seek investor assurance to **not request additional public funds** in the future
- **Evaluate the impact on Port activities**, traffic in particular
- Evaluate impact of additional **parking demand and traffic** in the vicinity
- Develop an approach to governance and decision-making that **encourages continued cooperation** between all parties, especially in later years when individuals involved on all sides may be different than those currently involved
- The City and County will need to evaluate their respective **capacities to issue councilmanic debt** for the project and **appropriately structure intergovernmental agreements**, should revenue be transferred from one jurisdiction to the other.

## **Section 5: Future Public Review Processes**

In addition to the work of the Panel, the arena proposal will go through the following public processes:

1. **Memorandum of Understanding (MOU) Consideration:** The Mayor and County Executive anticipate transmitting a nonbinding agreement between the City, County and Investor group providing a more detailed outline of the arena proposal and the public/private partnership. The MOU will be considered by both the City and County Councils and would be endorsed by resolution.
2. **Master Use Permit (MUP):** The land use permit process including State Environmental Policy Act (SEPA) review of the proposal for construction of an arena at the proposed site. The SEPA review will include an analysis of all environmental impacts of the arena, including impacts on traffic and parking. The MUP process also includes Design Review.
3. **Building Permits:** City review of the arena plans and construction, ensuring that construction complies with all building codes.
4. **Street Vacation:** A process ensuring the public receives adequate benefit when a street or alley is lost due to development. The proposed arena would result in the permanent closure of Occidental Ave S between Massachusetts St. and S Holgate St. This must be approved by City Council ordinance.
5. **Transaction Agreements:** The detailed documents outlining the public investment in the arena and the security and other guarantees provided by the investor. The agreements will need to be approved by City and County Councils.
6. **Land Acquisition and Initial Debt Issuance:** The City and County Councils would approve the public acquisition of the land for the arena site. The Councils must also approve issuing debt for the acquisition.
7. **Final Debt Issuance:** The City and County Councils would approve issuance of debt for the acquisition of the completed arena. Under the proposal the City and County would purchase the arena from the investor once the building is complete.

## **Section 6: Conclusions**

**Based on their review, the Panel believes that the proposal is favorable, has promise and is generally consistent with the principles set forth by the Mayor and County Executive; however, there are many important elements to be worked through to ensure these principles are met and to address other issues of importance to the community. The proposal warrants the serious consideration of the City and County policy makers.**

The Panel recommends that the City and County continue to work with Chris Hansen to further refine details for the potential public-private partnership, begin the processes that are required to address the multitude of issues at play with a project of this nature, and begin to engage with other community members to broaden the perspectives on the proposal and work through issues identified.

Based on information presented to the Panel during its review, there are additional considerations that will increase the chance of a successful outcome of the proposed public-private partnership.

A key determinant of success is that all parties continue to approach the partnership through trust and cooperation. The initial proposal embraced key principles for the City and County and as details get worked through, all parties will be well served to ensure open and honest communication. This becomes important also down the road when unanticipated issues arise, as they always do.

Another recommendation is to finalize as many details as possible well in advance of final deadlines. This lesson-learned applies in particular to major deadlines, where expectations are high. Sorting through details and issues in advance where possible can serve to improve outcomes.

***Additional information can be found online at: [www.seattle.gov/arena/](http://www.seattle.gov/arena/)***

The first step in the process of identifying the needs of the community is to conduct a needs assessment. This involves gathering information about the community's current situation and identifying the gaps between the current situation and the desired situation. The information gathered during the needs assessment can be used to develop a plan of action to address the community's needs.

The second step in the process of identifying the needs of the community is to develop a plan of action. This involves identifying the specific actions that need to be taken to address the community's needs. The plan of action should be based on the information gathered during the needs assessment and should be realistic and achievable.

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The third step in the process of identifying the needs of the community is to implement the plan of action. This involves carrying out the specific actions that have been identified in the plan of action. It is important to monitor the progress of the implementation and to make adjustments as needed.

The fourth step in the process of identifying the needs of the community is to evaluate the results of the implementation. This involves assessing the extent to which the community's needs have been met and the impact of the implementation on the community. The results of the evaluation can be used to inform future efforts to address the community's needs.