SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

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DEVELOP DON'T DESTROY (BROOKLYN), INC., et al.,

Petitioners,

-against-

EMPIRE STATE DEVELOPMENT CORPORATION and FOREST CITY RATNER COMPANIES, LLC,

Respondents.

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**AFFIDAVIT OF JOSHUA KAHR**

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JOSHUA KAHR, being first duly sworn, deposes and states as follows:

1. I am a principal in Kahr Real Estate Services, a real estate analysis and investment firm. My curriculum vitae is attached as Exhibit A.

2. My firm was retained by the Council of Brooklyn Neighborhoods to review certain aspects of the proposed Atlantic Yards Project, specifically to review whether it was financially feasible for the Project to be completed within 10 years. We were also retained to review the December 2006 report by KPMG prepared for ESDC which reviewed the financial feasibility of the Project.

3. On August 31, 2009 we submitted comments on the proposed MGPP which included a detailed analysis of the current market including projected growth in supply and demand, vacancy rates, the state of the capital markets and an analysis of the expected return on investment and concluded that:

> It is extremely unlikely that the full project can be financed and completed within 10 years at a profit by a private sector developer without substantial subsidies in excess of what has already been currently proposed. Based on the state of the market, the current plan, and the collective experiences of other large scale projects, it

> is much more likely that the development will take at least 20 years to complete.

(Kahr Report p. 2)

4. Our analysis also took into account the renegotiated terms in 2009 between FCRC and the MTA and we concluded that our projections were borne out by the actions of FCRC and we stated:

> Most important of all, the likelihood of this time frame has been essentially acknowledged by the developer; when they restructured their original 2006 agreement to purchase property rights from the MTA, they built in the ability to exit from the purchase of the Phase II properties for either no breakup fee or a minimal breakup fee depending on when they choose to exit the transaction. In addition, the timing of the payments has now been stretched out to 2030 – the new timing of the payments clearly indicates that the developer expects the timeframe of the development to stretch beyond ten years.

5. Recently, our client CBN, provided us a copy of a September 16, 2009 report prepared by KPMG LLP for ESDC entitled “Review of the Development Model and Absorption Period for the Residential Components of the Atlantic Yards Land Use Improvement and Civic Project”, and asked us to review it for its accuracy. KPMG concluded that FCRC’s market absorption data for the residential uses was consistent with market data. It is my understanding that ESDC relied upon the KPMG report to determine that a 2019 project completion date was not unreasonable.

6. In my opinion the KPMG report does not provide a reasonable basis to arrive at that conclusion.

7. Overall, the analysis prepared by KPMG fails on a number of fronts in addressing the outstanding challenges facing the Project. While the report does provide a relatively detailed long term demographic analysis of Brooklyn, it does not deal directly with any specific supply or

demand issues a development of this size and scope will face. In a number of areas, the degree of analysis employed to justify major development decisions is severely lacking.

8. KPMG uses Forest City assumptions as a base to determine project viability, as opposed to performing an independent analysis of the area's viability for development. A case in point is the demand analysis, in which a blanket statement about the site's proximity to transportation, building amenities, proposed retail corridor, attractiveness of new buildings, and high end nature will stimulate demand and result in faster occupancy than other buildings of comparable quality. This is something of a logical stretch, especially when one takes into account the number of units being proposed and the fact that there are currently a large number of high end luxury buildings that are currently operating at high vacancy rates.

9. While we do not dispute the long term projections for population growth, the timeline for the growth deviates significantly from the projected development timing of the planned development process. Furthermore, this projection is inconsistent with the conclusion reached by KPMG that most of the development will have been completed by 2015 and absorbed within the following 12 months. Using the projected population data over a 20-year period to support a development project over a 6-year time horizon is simply not a sound basis for analysis.

10. The KPMG report further states that the timing of the buildings' entry into the market will ensure that the units will be absorbed. As the nation continues to work through its second worst recession in the last 100 years, KPMG apparently believes that a market opportunity will emerge for the development of the largest concentration of high end residential units in the borough's history. In reality, the more likely scenario is that of a slow recovery that will take a number of years, as was the case in the years following the Great Depression.

11. The KPMG report further asserts that all units within the development will be absorbed by 2016. This assertion is far too aggressive for a number of reasons. First, this assumes that development will begin within a relatively short time period and continue unabated for about 5 years. This can be reasonably challenged from a number of different directions. From a supply standpoint, a development of this scope cannot be reasonably expected to be completed within such a small window of time. A normal development process more often than not includes delays and encounters unforeseen problems. To assume that this would be any different, especially given its large scope, is inconsistent with other large scale development projects in New York City, such as Forest City's own Metrotech project or other projects such as Battery Park City, (the proposed) Hudson Yards, World Trade Center (both the first and the proposed second), AOL Time Warner Center, or Queens West.

12. As outlined in our August 31, 2009 feasibility analysis comments, there is a substantial amount of development glut that will require an additional 4 years to be fully absorbed. Essentially, this development project alone will add thousands of new high end condo and rental buildings into a small subsection of Brooklyn. To put the proposed Atlantic Yards development in perspective, its nearly 6,500 units represents almost the entire number of units that were brought to market during the booming construction years of the early and mid 2000's throughout all of Brooklyn. In other words, the proposed 6,500 units represent an enormous infusion of new housing into an already saturated market. When adding in the fact that much more than the majority of the units are targeted to upper income consumers, it is inconceivable that the absorption will be anything close to what KPMG projects. In addition, based on measures of affordability and what the average Brooklyn resident can afford, the vast demand for new housing in Brooklyn is from low to moderate income families. Even if one takes an

optimistic view of the economic recovery and assumes that the existing glut of housing is absorbed, it still seems highly unlikely that the proposed Atlantic Yards project will absorb all of the demand for high end units from the rest of the established market. This development represents a serious departure from the traditional Brooklyn housing stock, which in and of itself is a questionable premise in a relatively weak market with weak projection for future growth.

13. In order for the project to achieve the level of success that is projected by the KPMG analysis, a number of critical demand and supply side factors would have to be perfectly aligned. On the supply side, there is an enormous amount of glut on the market. As stated in our August 31, 2009 comments, Brooklyn has traditionally operated at a vacancy rate of about 2%. The current vacancy rate is over 3% and this represents a significant departure from long term occupancy levels. While that may not sound like a large difference, in a market as large as Brooklyn, 1% of existing housing stock is substantial. What is required now in the market is a cooling down period for development in order for existing and recently created stock to be reabsorbed.

14. Furthermore, housing growth is fueled by solid economic fundamentals. Despite the potential for economic recovery over the next few years, the unemployment rate is projected to remain high for a prolonged period of time. Most economists seem to believe that it is likely that this recovery will be marked by a “jobless recovery”. As a general rule, without the creation of new jobs, it is difficult to justify the construction of new housing.

15. Moreover, the success of the proposed project is largely contingent on the sale and rental of high end units. In our previous analysis, we determined that prices have fallen by as much as 25%-30% in the high end market. Forest City’s initial projections had assumed an already low 9% IRR (“internal rate of return”) for the development.

16. The projected sales prices for the residential condominium units are not realistic given recent market conditions. In our report we noted:

> Sale prices PSF for the proposed Atlantic Yards project were underwritten at $850 PSF (2006 dollars). The market correction has resulted in a significant reduction in residential prices. Conservatively, if prices sell for 15%-20% less than projected, this would severely impact the financial viability of the project, and force a longer unit delivery period.

(Kahr Report p. 23)

According to data that we obtained from Miller and Samuel, a leading source of market data for residential condominium sales, in no quarter from 4th quarter 2006 to 2nd quarter 2009 did the average $/SF price for residential condominium units in Brooklyn exceed $600/SF. This is substantially lower than the projected $/SF sales prices of $850/SF (2006 dollars). Moreover, it is completely unrealistic to assume that prices will increase to $1,220/SF within five years as relied upon by KPMG.

17. With the further downward adjustment in rental and sale prices, the 2006 projected IRR will decrease substantially. Even if Forest City is willing to accept essentially no profit on its investment, which is an unlikely proposition, it is unlikely that investors and debt providers will accept an investment that does not make economic sense. To be specific, the KPMG report fails to address how Forest City will succeed in funding the development in an economic environment where it is difficult to obtain commercial real estate financing for almost any construction project, much less one of this size. When the original plan was proposed, financing was widely available for a project of this size. Today, and into the foreseeable future, it is simply not available. This will result in one of two situations. Either the developer will need to use less debt financing and will have to invest more equity which will substantially damage the

financial returns to investors, or the development will need to substantially delay the development until the financing becomes available.

18. It is notable that the KPMG report does not make any reference to the renegotiated terms between FCRC and the MTA which extended the payment for Phase II. Such a major restructuring of the terms is a material fact which should have been identified and considered. As we noted in our August comments, that restructuring is the clearest evidence that the FCRC itself knew the project could not be financially feasible to complete in 10 years.

19. In summary, KPMG did not undertake an independent analysis of the absorption projections for Atlantic Yards and did not evaluate the financial feasibility of the project or update its 2006 report. KPMG's report does not provide a reasonable basis to disagree with our August comments nor does it support a determination that the project will be completed in 2019.

Dated: October ___, 2009

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JOSHUA KAHR