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Memorandum

UNIVERSITY of ALASKA
Many Traditions One Alaska

To: Dr. Ashok Roy

Thru: Kit Duke

From: Robert McMaster

Date: 5-13-2013

Re: Bragaw Office Complex and Diplomacy Building Asset Repositioning – An Update

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Below, I have summarized a number of the key "Deal Points" associated with the sale of the Diplomacy building and acquisition of the Bragaw Office Complex ("BOC"), also presented are the three requested financing structures including Facilities and Land Management's (FLM) recommended course of action.

1915 Bragaw – to be demolished

The BOC located at 1815–1901 Bragaw Street in Anchorage currently consists of four buildings, including a functionally obsolete, one story building (1915 Bragaw) consisting of approximately 3,000 sf. This building does not meet numerous building, seismic and handicap codes. The cost to bring this building into compliance cannot be justified in the current market, as potential Net Operating Income (N.O.I) would not support the cost of renovation. In addition, the demolition of this building will provide additional parking and allow for reconfiguring the parking lot serving 1901 Bragaw. Post-closing the complex will consist of the following three buildings:

Name:	**"1815"**	**"1835"**	**"1901"**	**Total**
Address:	1815 Bragaw	1835 Bragaw	1901 Bragaw	
Gross Sq. Ft.:	27,239	77,891	67,779	168,927
Rentable Sq. Ft.:	25,346	72,929	64,451	159,787
# of Floors:	Two	Five	Four	
Parking Spaces:	100	153	278	545
Year Built	1971	1974	1978	
Recent Remodel:	2007	2004 & 2010	2003 & 2012	
Zoning:	RO	RO	RO	(Residential / Office)

FLM has completed extensive financial modeling on current and future BOC operations that include Operational Pro-Forma(s), Break-Even Analysis, Return on Investment, Internal Rates of Return (IRR), Current and Future Valuation, Capital/Debt Requirements and Management structures.

We have also stressed the various financing options to determine which option presents the least risk relative to any advantages flowing to the University. The model currently assumes that both UAA and the Land Grant Trust Fund ("LGTF") will sell the Diplomacy building and reinvest all of the net equity proceeds from that sale into the BOC. Using both tax-exempt and taxable bonds to leverage the Diplomacy proceeds delivers a conventional commercial real estate financing structure.

FLM presents the following three financing scenarios in order to demonstrate that the optimum structure tracks the financing strategy noted above.

General Assumptions Common to all Three Financing Options –

- **Sell the Diplomacy building to ANTHC for at least $16,500,000**
- Net Proceeds of Diplomacy Sale:

Net Proceeds of Diplomacy Sale:	Sales Price	$16,500,000
	Less Transaction Costs	($ 43,500)
	Gross Sale Proceeds	$16,456,500

LGTF's Inflation Proofing Fund (IPF) – Net Proceeds (39%)	**$6,418,035**
UAA Portion of Gross Sale Proceeds (61%)	$10,038,465
Sinking Fund to Pay Existing "Series P" Debt Service Schedule	($1,692,800)
UAA Net Proceeds	**$8,345,665**

Approximate BOC Purchase Price :	$31,000,000
BOC Transactions Costs: (Points, Due Diligence, Closing Costs, Escrows, etc.)	$ 861,000
Tenant Improvements in 1901 Bragaw:	$ 1,750,000
Total Cost to Acquire BOC	**$33,361,000**

Financing Option #1 (FLM's Recommendation) -

BOC Acquisition Cost:	$33,361,000
Use 100% of Diplomacy Proceeds as "Equity":	$14,763,700
Amount to be Financed by Bonds	**$18,597,300**

- Amount of Bonds $18,597,300

Underwriting Assumptions:

Net Operating Income: (Based Upon Current Leases @ 1835 & 1815)		$1,414,013
Debt Service Coverage Ratio:		1.20
Amortization:		25 yr.
Blended Interest Rate: (Tax-Exempt & Taxable Bonds)		4%
Approximate Post-Debt Service/AMF* Cash Flow:		$200,000
Internal Rate of Return: (IRR)	10 year	13.8%
	15 year	11.6%
	25 year	9.7%

**AMF – Asset Management Fee*

Financing Option #2

- BOC Acquisition Cost: $33,361,000
- Use 61% of Diplomacy Proceeds as "Equity": ($ 8,345,665)

Amount to be Financed by Bonds $25,015,335

- Amount of Bonds $25,015,335

Underwriting Assumptions:

Net Operating Income: (Based Upon Current Leases @ 1835 & 1815)	$1,414,013
Debt Service Coverage Ratio:	1.00
Amortization:	25 yr.
Blended Interest Rate: (Tax-Exempt & Taxable Bonds)	4%

Approximate Post-Debt Service/AMF Cash Flow: $0

Additional Debt Service Needed Over N.O.I.: $ 172,980

Internal Rate of Return: (IRR)	10 year	0%
	15 year	0%
	25 year	0%

The IRR is zero since there is no Cash Flow available to serve as the "return instrument" and because the IPF would have fund the Additional Debt Service … of $172,980 every year.

FLM would caution against this approach to financing the BOC purchase, as it provides zero IRR on a project basis, requires the University to fund approximately $172,980 per year for 25 years or $4,324,575 and would require the University to fund any operational deficits for the next 25 years.

However, the IPF would receive $6,418,035 that it could invest. Comparing the IPF's 20-yr. historical return average of 7.8% to Option #1's projected 25-yr. IRR of 9.6%, indicates that all things being equal, including risk profiles, the IPF would extract a higher net return using the Diplomacy equity to finance the BOC purchase.

We have illustrated this difference for IPF returns below using a simple interest approach for ease of calculation and understanding.

IPF Investment Amount:	$6,418,035
IPF's Historical Return Average:	7.8%
Approximated Annual Return Amount:	$500,600 *(not necessarily liquid)*
Less Additional Debt Service:	$172,980 *(must be liquid)*
Adjusted Net Annual Return Amount:	$327,620

BOC 25-yr. IRR:	9.6%
Less Adjusted IPF Return %:	5.1%
Option #1 provides a Higher Return of:	4.5%

Financing Option #3

- BOC Acquisition Cost: $33,361,000
- Use 10% of Diplomacy Proceeds as "Equity": $ 1,476,370

Amount to be Financed by Bonds **$31,884,630**

- Amount of Bonds $31,884,630

Underwriting Assumptions:

Net Operating Income: (Based Upon Current Leases @ 1835 & 1815)	$1,414,013
Debt Service Coverage Ratio:	1.00
Amortization:	25 yr.
Blended Interest Rate: (Tax-Exempt & Taxable Bonds)	4%

Approximate Post-Debt Service/AMF Cash Flow: $0

Additional Debt Service Needed Over N.O.I.: $ 608,887

Internal Rate of Return: (IRR)	10 year	0%
	15 year	0%
	25 year	0%

The IRR is zero since there is no Cash Flow available to serve as the "return instrument" and because the IPF would have fund the Additional Debt Service ... of $608,887 every year.

This financing structure for the BOC purchase provides the worst net return to the IPF of the three financing options explored. Like Option #2 above, this Option requires the University to fund approximately $608,887 per year for 25 years or $15,222,175 and would require the University to fund any operational deficits for the next 25 years.

However, the IPF would receive $13,287,330 that it could invest. Comparing the IPF's 20-yr. historical return average of 7.8% to Option #1's projected 25-yr. IRR of 9.6%, indicates that all things being equal, including risk profiles, the IPF would extract a higher net return using the Diplomacy equity to finance the BOC purchase.

We have illustrated this difference below using a simple interest calculation for ease calculation and understanding.

IPF Investment Amount:	$13,287,330
IPF's Historical Return Average:	7.8%
Approximated Annual Return Amount:	$1,036,400 *(not necessarily liquid)*
Less Additional Debt Service:	$608,887 (must be liquid)
Adjusted Net Annual Return Amount:	$427,513

BOC 25-yr. IRR:	9.6%
Less Adjusted IPF Return %:	3.2%
Option #1 provides a Higher Return of:	6.4%

Upon review, Option #1 provides the best financing solution to purchasing the BOC. FLM is proceeding with contract negotiations assuming Option #1 will be the path of choice for financing this acquisition.