Trust

Alaska Mental Health Trust Authority

Resource Management Committee
Special Meeting
April 29, 2016
PUBLIC PACKET

Protecting and enhancing the value of Alaska Mental Health Trust Lands while maximizing revenues from those lands over time.

ALASKA MENTAL HEALTH TRUST AUTHORITY
RESOURCE MANAGEMENT COMMITTEE MEETING
DRAFT AGENDA
APRIL 29, 2016
10:00 a.m. - 10:45 a.m.

<u>Teleconference Information</u>
Call in Number: (866) 469-3239
Meeting/Session Number: 921 183 69 #
Attendee Number: #

Call to Order (Chair Larry Norene)
Committee Members (Voting):
- Laraine Derr
- Paula Easley
- Russ Webb
- Mary Jane Michael
- Carlton Smith
- Jerome Selby
- John Morrison, Staff

Announcements
Approval of Agenda

1. Consultation

2. Approvals
   a) Texas Building Acquisition (Item 1)
   b) WA JV Building Development (Item 2)

3. Executive Session will be conducted

4. Other

5. Adjourn

2600 Cordova Street
Anchorage, Alaska 99503
Phone: 907-269-8658
Fax: 907-269-8605

To: Larry Norene, Chair
Resource Management Committee
From: John Morrison
Date: 4/29/2016
Re: Item 1 – PUBLIC - Texas Building Acquisition - Project #2016-130
Fiscal Year: 2016

Approval

Proposed RMC Motion:

Proposed Motion One: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees approve the action as described herein wherein the Trust Land Office (TLO) forms and manages a Single Purpose Entity (SPE) Limited Liability Corporation (LLC) owned in full by the Trust for the purpose of acquiring, owning, and operating the proposed property."*

Proposed Motion Two: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees approve the proposed action to fund the newly formed LLC with principal from the Trust Authority Development Account (TADA) fund code 3320, to acquire the property, up to $9,500,000. This funding will include purchase price net of loan acquired, entity formation expenses, legal review, closing, and due diligence costs as necessary to complete the transaction, as presented."*

Proposed Motion Three: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees concur with the proposed action to complete the financing of the proposed property."*

Proposed Motion Four: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees approve an increase to the property budget appropriation in the amount of $2,128,725."*

Proposed Motion Five: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees delegate to the Executive Director of the TLO the authority to determine if it is necessary to modify or cancel this transaction."*

Background:

Transaction/Resource: Form and fund a SPE LLC, operated and managed by the TLO, to purchase and finance land and improvements, the Real Property.

Property Description/Acreage/MH Parcel(s): The parcel of land located in, Austin, TX , consisting of 8.81 acres +/-, together with the building erected thereon containing an approximate total of 106,000 square feet. Additional improvements include parking lots and landscaping.

Proposed Actions: There are four proposed actions:

1. Formation of a SPE LLC to acquire the proposed property.
2. Approve funding the SPE LLC for:
   a. Entity organizational costs
   b. Due Diligence period costs
   c. Acquisition of the property under consideration
3. Acquire financing.
4. Approve an incremental increase of $2,128,725 to the property budget. The incremental costs are attributable to the purchase and operation of this property. This property will be among those managed by a third party property manager. Revenue from this property will be collected and then used to pay expenses for the property, by the property manager. The net funds, which are Trust funds, would then be distributed to the Trust as Income Revenue. Finally, a journal entry would be made in order to capture all of the activity on the state accounting system. This new budget appropriation is necessary because it was not previously known the TLO would acquire this facility.

General Background: Through approval of the Real Estate Management Plan (REMP), the Trustees have directed the TLO to invest in quality income properties that produce predictable market rate returns. Most recently the TLO has been instructed to develop a plan to greatly increase its income revenue to match the annual distribution provided by the cash assets. Acquisitions such as this are integral to the success of that plan. The REMP contemplates various ways to increase long term benefit to the Trust through investments in income producing real property. The TLO, in accordance with the plan, has focused on ways to diversify the holdings of the Trust. Specifically, it discussed and approved the process and results of using leverage to increase returns and reduce risk to the Trust. In addition, the TLO has sought assets outside of the Trust's current geographical holdings.

This property is being presented with financing placed at acquisition. This financing proposal meets the REMP business model for three reasons. First, this asset will be owned by a title holding entity. This is an important consideration because the legal entity offers several protections for the Trust. The most important protection, as it relates to financing, is that the LLC provides a buffer between the lender and the Trust. In other words, because the Trust is not the owner of the property and will not be a signatory on the note, the liability related to the property and specifically the loan, cannot reach the Trust. In addition, the completion of the financing will provide cash for additional Trust investment. Finally, as shown below in the anticipated benefit section, the proposed financing will increase the return potential of this asset.

Purchase Considerations

Tenant and Lease: The facilities are currently 91 percent leased to a diverse blend of 12 tenants. The remaining lease terms range from one to seven years and the expirations are appropriately staggered. There is currently one vacancy representing 4.29% of the building. Total vacancy of 8.62% of the building consists of one vacancy of 4,572 square feet (4.29% of the building) and non-revenue generating spaces of 3,143 square feet occupied by the business park management (2.95%) and a fitness center space of 1,462 square feet (1.38%). There is as strong possibility of monetizing these spaces in the near future. All leases are triple net, meaning the tenants pay base rent plus all operating expenses related to the property.

Facility: The property was constructed in 2001 as part of a larger business park. The building is a two story 106,000 Class B+ office with a very attractive 4.8 per thousand square feet parking ratio. The site is 8.81 acres and is located in Austin with easy access to several regional arterial roads. The central location, ease of employee access, and substantial parking are all unique attributes that would be difficult to replicate. In addition the facility is currently leased at a 20% discount to similar buildings in the immediate submarket, providing the opportunity to increase revenue with future tenant rollovers and renewals.

Market/Tenants: The facility is located in Austin, TX, in Williamson County just a few miles north of downtown in a burgeoning technology corridor. The northwest submarket is one of the fastest growing areas both in Texas and nationally. There has been a 19% rent growth in the area since 2012. In addition the area has continued to absorb newly delivered space over the last several years.

Interesting market facts:

- Austin was the fastest growing city in the country in 2015, as ranked by Forbes.
- Austin has created 31,000 new jobs in the past 12 months.
- Recent Northwest submarket announcements from Corporations
  - Apple 3600 new jobs
  - Ebay 1000 new jobs
  - Charles Schwab 820 new jobs
  - Websense 470 new jobs
  - Home Away 300 new jobs
  - Amazon 240 new jobs
- The Austin MSA has a population of 1.9 million.
- The workforce is concentrated in education, medical, technology, and governmental.
- Austin is experiencing growth at twice the national rate and has unemployment of 3.3%.

Anticipated Revenues/Benefits: The key anticipated benefits that result from pursuing the transaction are as follows:

1. Provide a significant source of spendable Income Revenue to the Trust;
2. Increase cash available for investment in other opportunities;
3. Increase the return metrics of this property;
4. Reduce risk; and
5. Diversify Trust holdings.

First, this property will provide an average of approximately $588,000 of predictable spendable Income Revenue per year, over a 20 year hold period, when leveraged as proposed. The most important aspect of this stream of cash is the predictability. The cash may be used to supplant unexpected changes in other cash sources.

Second, financing will allow the Trust to increase the power of its capital. It is important to have a ready supply of cash for active projects and those not yet identified.

The third benefit is apparent within the economics of financing this property. Without financing, the property will outperform the Permanent Fund's long term 6.9 percent projected return on assets that consists of a 4.4 percent projected real return plus an assumed inflation rate of 2.5 percent. The project as proposed increases all of the key metrics the TLO uses to evaluate the merits of an investment. Potential modifications to the financing would further increase the return on investment.

Fourth, the use of financing has the potential to reduce risk in two ways. Foremost, it reduces Trust equity[i] committed to an individual asset. If an asset is destroyed or otherwise rendered worthless, the Trust's exposure to loss is reduced dollar for dollar by the amount of non-recourse financing on the investment. The Trust's financial exposure to the destruction or other risk associated with the property valuation is minimal in this instance and insurance is carried to cover the full value of the building. In the unlikely event the asset is compromised, the insurance proceeds will cover the loss to the owner, and will pay the loan balance in full.

The other way that financing reduces risk is by allowing an equity pool of a certain amount to be invested across a greater variety of assets. For arguments sake, an unleveraged $50 Million investment in one property would be the definition of putting all the Trust's eggs in one basket - generally, not considered wise financial planning. A more diversified unleveraged fund might buy a certain group of five properties across geographic regions, business types, and property types. If that same $50 Million was leveraged at 50 percent it would produce $100 Million of buying power. This would allow the purchase of ten properties under a similar scenario. Potential risk to the Trust is reduced by doubling the number of cash flow streams, diverse geographic locations, and diversity of tenants among other benefits. This approach is consistent with the Resource Management Strategy and Real Estate Management Plan.

The fifth benefit of this proposal is that this asset diversifies the Trust's holdings in several ways. First, the Trust is heavily invested in Alaska land and more specifically, its natural resources therein. The proposed asset is not in the same geographic or economic trade region as other Trust land. Second, the tenants are not associated with the natural resource industry, and third, the property is developed and located within a commercial district, both of which are unique attributes when compared to Trust holdings in general.

In summary, it is in the best interest of the Trust to pursue the acquisition and financing on its own merit and as part of the overall plan to invest in property producing income revenue.

Anticipated Risks/Concerns: There are two types of risk associated with this proposal. The first is the direct risk of nonperformance by the title holding entity. This specifically is the ability of the entity to pay the mortgage payments or the mortgage in full. Financing for this property only adds direct risk to the extent that the Trust, through the entity, would not have cash to pay the loan payment or the loan in full. This risk is quantified and limited to the equity in the property. In other words, the risk upon acquisition is capped at $9.5 million. For all these reasons the direct risk is minimal and not increased by the proposed financing.

The second type of risk is indirect, specifically the risk that the Trust is not able to use financing due to some outside objection. This is specifically associated with precedent and procedure. Objections may come from an interested party in the government bureaucracy, a member of the public, or a Trust beneficiary. The concept of acquiring and mortgaging the Trust's property has been analyzed and discussed with the Attorney General and has been reviewed by the outside counsel to the Trust. Further discussion can be found under "Applicable Authority" (below). The Trust has completed other large purchases and subsequent financing without comment; the indirect risk is considered low.

Due Diligence: The terms of the purchase contract include a 35-day due diligence period, beginning the day the contract is executed. During that time the TLO will perform many tasks. In addition, the TLO will direct third party contractors to perform many important functions to study the asset. Some of the due diligence items are as follows:

- Appraisal – is performed by a Certified Real Estate Appraiser with any acquisition as part of the REMP plan.
- ALTA Survey – is a specific kind of survey that goes beyond locating the parcel and any structures. The ALTA Survey also notes any items related to title such as trespass and easements. ALTA surveys are also performed to a more exacting standard.
- Title Review – is performed early in the due diligence period by an attorney to ensure that the seller has the rights to the property they have presented.
- Phase 1 Environmental – is a review of the structures, grounds, and all the business processes performed there in. It is performed by an environmental engineer and provides information as to the possible presence of contaminates.
- ADA inspection – ensures that the building is up to proper code with regard to the Americans with Disabilities Act.
- Structural Inspection – provides an analysis of the structure as a whole as to the suitability of its current use, and an estimate of useful life.
- Geotechnical Inspection – specifically inspects the structure to ensure it meets seismic standards.

- Roof Inspection – provides a report on the condition and useful life of the roof. In addition, it will recommend a maintenance schedule to maximize the useful life.
- HVAC Inspection – provides a report on the condition and useful life of the HVAC system. In addition, it will recommend a maintenance schedule to maximize the useful life.
- Capital Project Review – is an analysis of projects performed over the life of the building so that any of the other inspections may pay close attention to the subject area. It is also used as part of the financial analysis to determine the capital budget.
- Financial Review – is an analysis of the operations of the property for the last several years to determine if they are as presented in the sale.
- Tenant Communications – the TLO will continue communications with the tenants to discuss their use and plans for the facility.
- Vetting of Seller – the overall analysis that the seller has the authority to sell their interest in the property as negotiated.

The TLO will amass and study all the information produced as well as make physical inspections of the property. The information will be taken as a whole to determine if the transaction will be completed. If a concern is uncovered during the process there are various ways to negotiate and mitigate the effects. If a concern is found that is unacceptable to the TLO, the transaction may be cancelled at any time before the end of the due diligence period without penalty.

Consistency with the Resource Management Strategy: The proposal is consistent with the long term "Resource Management Strategy for Trust Land" (RMS) which was adopted January 2016 in consultation with the Trust and provides for the TLO to focus on generating long term cash flow through asset acquisition and diversification.

Trust Land Office Recommendation: Proceed with the formation and funding of the SPE LLC, operated and managed by the TLO, for the acquisition, operation and financing of the proposed property, as described herein.

Applicable Authority: State and federal authority supporting this proposed action can be found in public law, and state statutes and regulations. Primarily, the Alaska Mental Health Enabling Act of 1956 - Section 202 of P.L. 84-530, authorized the Trust to mortgage its lands.

> *"Such lands together with any property acquired in exchange therefore or acquired out of the income or proceeds therefrom, may be sold, leased, **mortgaged**, exchanged or otherwise **disposed** of in such manner as the Legislature of Alaska may provide…"*

By including the action of mortgage in the above authorized actions, Congress implied the mortgage of Trust lands was a disposal of a Trust interest. The State Legislature enacted laws providing Trust lands be managed by the Department of Natural Resources (AS 37.14.009(b)) and that the management of Trust lands be consistent with the federal enabling act (AS 38.05.801(a)). In the adoption of regulations for the Trust Land Office, the TLO Executive Director's duties and authority provides that he/she shall manage Trust lands consistent with other provisions of law as "implemented by this chapter" (11 AAC 99.010(a) Authority and duties of executive director.) Actions authorized by chapter

99 of the Alaska Administrative Code include “management, sale, lease, conveyance, permitting, licensing, dedication, and other management and disposal of trust land…” (11 AAC 99.010(b)).

In addition, the Asset Management Policy Statement (AMPS), which has been adopted by reference (20 AAC 40.600), provides guidance consistent with this proposed action (page 9, revised January 28, 2015.)

> *“Lands, structures and resources may be acquired when the acquisition will add value to The Trust’s non-cash asset portfolio or will contribute to the mission of The Trust in some other way.”*

Other applicable authorities include Alaska Statutes 36.30.850(b)15(B), 37.14.009, 38.05.801, 11 AAC 99.010(b), 11 AAC 99.020(b), 11 AAC 99.090(a), 11 AAC 99.090(e), 11 AAC 99.030(e), 20 AAC 40.700.

Trust Authority Consultation: This briefing document fulfills the consultation requirements that are applicable to the transaction.

---

[i] **Equity** is the difference between the market value of an asset and the mortgage thereon if any.

2600 Cordova Street
Anchorage, Alaska 99503
Phone: 907-269-8658
Fax: 907-269-8605

To:	Larry Norene, Chair Resource Management Committee
From:	John Morrison
Date:	4/29/2016
Re:	Item 2 – PUBLIC – WA JV Building Development – #2016-131
Fiscal Year:	2016

Approval

Proposed RMC Motion:

Proposed Motion One: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees approve the action as described herein wherein the Trust Land Office (TLO) forms a Single Purpose Entity (SPE) joint venture (JV) Limited Liability Company (LLC) with Panattoni Development Company for the purpose of acquiring, owning, developing and operating the proposed property."*

Proposed Motion Two: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees authorize the Executive Director of the TLO to represent the Trust's interests in the transaction by working with the development partner to ensure a successful project, including but not limited to decisions about modifications to the project plan, leasing, tenant improvements, financing, and buying out Panattoni at project stabilization."*

Proposed Motion Three: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees approve the proposed action to fund the newly formed LLC with principal from the Trust Authority Development Account (TADA) fund code 3320, to complete the proposed action, up to $11,000,000. This funding will include payments to be made as part of the development process, the eventual purchase price net of loan acquired, entity formation expenses, legal review, closing, and due diligence costs as necessary to complete the transaction, as presented."*

Proposed Motion Four: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees concur with the proposed action to complete the financing and subsequent purchase or sale of the proposed property."*

Proposed Motion Five: *"The Resource Management Committee recommends the Alaska Mental Health Trust board of trustees delegate to the Executive Director of the TLO the authority to determine if it is necessary to modify or cancel this transaction."*

Background:

Transaction/Resource: Form and fund a SPE JV LLC with Panattoni for the purposes of acquiring a site and developing a Class A industrial facility in Everett, Washington. During the JV period the entity will be managed by Panattoni with close interaction, participation and monitoring by the TLO of all substantive business decisions. After the proposed buyout of Panattoni by the Trust, the entity would continue to exist and would then be operated and managed by the TLO.

Property Description/Acreage/MH Parcel(s): The parcel of land located in, Everett, WA consisting of 9.7 acres +/-, together with the building to be erected thereon containing an approximate total of 208,000 square feet of shell space and a 3,000 square foot mezzanine. Additional improvements will include parking lots and landscaping.

Proposed Actions: The following are the proposed actions:

1. Formation of a SPE JV LLC to:
    a. Acquire the proposed property
    b. Develop the proposed property
    c. Lease out the proposed property
    d. Acquire interim construction financing
2. Approve funding the SPE JV LLC for:
    a. Entity organizational costs
    b. Due Diligence period costs
    c. Financing costs
    d. Legal costs
    e. Acquisition of the property under consideration upon stabilization by buyout of JV partner; or alternatively, sale of the property to a third party if deemed to be in the Trust's best interest
3. Acquire financing:
    a. Construction financing
    b. Long-term financing for buyout

General Background: Through approval of the Real Estate Management Plan (REMP), the Trustees have directed the TLO to invest in quality income properties that produce market rate returns. Most recently the TLO has been instructed to develop a plan to greatly increase its income revenue to match the annual distribution provided by the cash assets. Transactions such as this, which leverage the skills and opportunities of JV partners, are integral to the success of that plan. The REMP contemplates various ways to increase long term benefit to the Trust through investments in income producing real property. The TLO, in accordance with the plan, has focused on ways to diversify the holdings of the Trust. Specifically, it discussed and approved the process and results of using leverage and joint venture partnerships to increase returns and reduce risk to the Trust. In addition, the TLO has sought assets outside of the Trust's current geographical holdings.

This property is being presented as a joint venture development with financing placed during construction and at acquisition. This financing proposal meets the REMP business model for three reasons. First, this asset will be owned by a title holding entity. This is an important consideration because the legal entity offers several protections for the Trust. The most important protection, as it relates to financing, is that the LLC provides a buffer between the lender and the Trust. In other words, because the Trust is not the owner of the property and will not be a signatory on the note, the liability related to the property and specifically the loan, cannot reach the Trust. In addition, the completion of the financing will provide cash for additional Trust investment. Finally, as shown below in the anticipated benefit section, the proposed financing will increase the return potential of this asset.

Project Considerations

Tenant and Lease: The facilities are not yet under construction and have already received Letters of Intent from 4 reputable tenants seeking space ranging from 60,000 square feet to the entire facility. All conceptual leases would be triple net.

Facility/ Site: The property is located in a business park +/- 30 miles from Downtown Seattle. The proposed building is a single story, 211,000 square foot, Class A, cross dock industrial warehouse with very attractive state of the art features such as:

- 30’ clear height
- 480 volt 3-phase electrical service
- Divisibility to 20,000 sf
- T5 energy efficient lighting
- 50’ x 50’ column spacing
- 6” reinforced slab
- Dock height and grade level loading

The site is 9.7 acres located in Everett with easy access to several regional arterial roads. Access to the site is primarily comprised of a two lane bridge that the Port of Everett constructed in 2006, and is built to the same specifications as the bridges on I-5. The ease of access, utility availability, zoning, and proximity to sea ports, rail lines, and Boeing’s primary assembly plant at Paine field are all unique attributes that would be difficult to replicate. The opportunity exists to deliver a Class A product at below market rents.

Partner: Panattoni
LOCAL MARKET EXPERIENCE

Panattoni Development Company, Inc. is one of the largest privately held, full-service real estate development companies in the world. Founded in 1986, Panattoni operates from 24 offices in the United States, Canada and Europe. Since inception, Panattoni has developed more than 200 million SF of space. Locally, Panattoni Seattle has developed more than 11.8 million square feet of industrial, office and build-to-suit projects in the Pacific Northwest, and is proud to be the most active industrial developer in Washington State.

Panattoni’ s Seattle team has a long history and an impressive track record of successful industrial development projects in the north end market including Everett, Monroe and Burlington. Panattoni has 16 buildings totaling over 1,800,000 SF in this local Everett / North End market. No other developer has built, leased or sold more industrial buildings in this market.

Market/Tenants: The facility is located in Everett, WA, in Snohomish. The Everett market has historically been characterized by steady smaller deals in the 20,000 to 50,000 sf range due to the dynamic between Boeing and its vendors. Panattoni has experienced positive absorption trends with much larger tenants in its recent developments such as its Powder Mill Business Center, which is a 372,000 sf facility that was completed in March of 2016 that is now 100% leased to a diverse blend of tenants. The Powder Mill facility was 90% leased before completion. The subject property, has already received four letters of intent (LOI) for space from 60,000 sf to the entire property.

The industrial and warehousing market in Everett is benefitting from the traffic congestion in Seattle along the I-5 corridor. Traditionally developments of this type were located south of Downtown near the sea port or the airport. Distributors have realized that they are no longer able to serve the areas north of downtown in a timely and efficient manner, leading to strong interest in a market that has limited space available.

Anticipated Revenues/Benefits: The key anticipated benefits that result from pursuing the transaction are as follows:

1. Provide a significant source of spendable Income Revenue to the Trust;
2. Increase cash available for investment in other opportunities;
3. Increase the return metrics of this property;
4. Reduce risk; and
5. Diversify Trust holdings.

First, this property will, upon stabilization, provide an average of approximately $725,000 of predictable spendable Income Revenue per year when leveraged as proposed. The most important aspect of this stream of cash is the predictability. The cash may be used to supplant unexpected changes in other cash sources.

Second, financing will allow the Trust to increase the power of its capital. It is important to have a ready supply of cash for active projects and those not yet identified.

The third benefit is apparent within the economics of financing this property. Without financing, the property will outperform the Permanent Fund's long term 6.9 percent projected return on assets that consists of a 4.4 percent projected real return plus an assumed inflation rate of 2.5 percent. The project as proposed increases all of the key metrics the TLO uses to evaluate the merits of an investment. Potential modifications to the financing would further increase the return on investment.

Fourth, the use of financing has the potential to reduce risk in two ways. Foremost, it reduces Trust equity[i] committed to an individual asset. If an asset is destroyed or otherwise rendered worthless, the Trust's exposure to loss is reduced dollar for dollar by the amount of non-recourse financing on the investment. The Trust's financial exposure to the destruction or other risk associated with the property valuation is minimal and in this instance insurance is carried to cover the full value of the building. In the unlikely event the asset is compromised, the insurance proceeds will cover the loss to the owner, and will pay the loan balance in full.

The other way that financing reduces risk is by allowing an equity pool of a certain amount to be invested across a greater variety of assets. For arguments sake, an unleveraged $50 Million investment in one property would be the definition of putting all the Trust's eggs in one basket - generally, not considered wise financial planning. A more diversified unleveraged fund might buy a certain group of five properties across geographic regions, business types, and property types. If that same $50 Million was leveraged at 50 percent it would produce $100 Million of buying power. This would allow the purchase of ten properties under a similar scenario. Potential risk to the Trust is reduced by doubling the number of cash flow streams, diverse geographic locations, and diversity of tenants among other benefits. This approach is consistent with the Resource Management Strategy and Real Estate Management Plan.

The fifth benefit of this proposal is that this asset diversifies the Trust's holdings in several ways. First, the Trust is heavily invested in Alaska land and more specifically, its natural resources therein. The proposed asset is not in the same geographic or economic trade region as other Trust land. Second, the tenants are not associated with the natural resource industry, and third, the property is developed and located within a commercial district, both of which are unique attributes when compared to Trust holdings in general. In addition this particular transaction allows the Trust to acquire a facility in a targeted geographical area at well below market cost. A completed and stabilized product such as this on the open market would not meet the Trust's return hurdles.

In summary, it is in the best interest of the Trust to pursue the acquisition and financing on its own merit and as part of the overall plan to invest in property producing income revenue.

Anticipated Risks/Concerns: There are three types of risk associated with this proposal. The first risk is market risk. In a speculative development there is a chance that the product will be delivered and not meet the expectations or needs of the market for any number of reasons. In this instance we have selected a partner who is well versed in the market, has recent success in this market and is currently receiving positive feedback on market demand. This risk is also mitigated by timing. It is likely that the property will be ready for occupancy within 9 months, reducing the risk of a significant market shift. The Trust is compensated for this market risk by sharing in the value add nature of the development through what is known as a promote with the JV partner. In this instance the promote divides income from the development, which is the difference between cost and stabilized market value, between the partners at ratios that begin with more income going to the Trust and at each of several return hurdles the split shifts to the benefit of the developer. This arrangement protects the Trust and entices the partner to perform by aligning our interests in a successful project.

The second type of risk is the direct risk of nonperformance by the title holding entity. The first risk is the ability of the entity to deliver a Class A facility as proposed. This is always a risk in development and construction, but Panattoni has a proven track record of delivering millions of square feet of this exact product type in this market. In addition the JV structure is designed to incentivize Panattoni to deliver a successful product. The more successful the project, the greater the returns for both partners. The second risk is the ability of the entity to pay the mortgage payments or the mortgage in full. Financing for this property only adds direct risk to the extent that the Trust, through the entity, would not have cash to pay the loan payment or the loan in full. This risk is quantified and limited to the equity in the property. In other words, the risk upon acquisition is capped at $11 million. For all these reasons the direct risk is minimal and not increased by the proposed financing.

The third type of risk is indirect, specifically the risk that the Trust is not able to participate in a joint venture or use financing due to some outside objection. This is specifically associated with precedent and procedure. Objections may come from an interested party in the government bureaucracy, a member of the public, or a Trust beneficiary. The concept of acquiring and mortgaging the Trust's property has been analyzed and discussed with the Attorney General and has been reviewed by the outside counsel to the Trust. Further discussion can be found under "Applicable Authority" (below). The Trust has completed other large purchases and subsequent financing without comment; the indirect risk is considered low.

Due Diligence: The terms of the purchase contract include a due diligence period which the TLO has already begun. The TLO will direct third party contractors to perform many important functions to study the asset. Some of the due diligence items are as follows:

- Appraisal – is performed by a Certified Real Estate Appraiser with any acquisition as part of the REMP plan.
- ALTA Survey – is a specific kind of survey that goes beyond locating the parcel and any structures. The ALTA Survey also notes any items related to title such as trespass and easements. ALTA surveys are also performed to a more exacting standard.
- Title Review – is performed early in the due diligence period by an attorney to ensure that the seller has the rights to the property they have presented.
- Development Feasibility Review – analyses of market conditions, supply/demand projections, vacancy rates, market rent studies, etc.
- Design Feasibility Review – continual monitoring of design components, changes to design throughout construction, and finally, design considerations for specific tenant finishes.
- Phase 1 Environmental – is a review of the structures, grounds, and all the business processes performed there in. It is performed by an environmental engineer and provides information as to the possible presence of contaminates.
- ADA inspection – ensures that the building is up to proper code with regard to the Americans with Disabilities Act.
- Structural Inspection – provides an analysis of the structure as a whole as to the suitability of its current use, and an estimate of useful life.
- Geotechnical Inspection – specifically inspects the structure to ensure it meets seismic standards.
- Roof Inspection – provides a report on the condition and useful life of the roof. In addition, it will recommend a maintenance schedule to maximize the useful life.
- HVAC Inspection – provides a report on the condition and useful life of the HVAC system. In addition, it will recommend a maintenance schedule to maximize the useful life.
- Capital Project Review – is an analysis of projects performed over the life of the building so that any of the other inspections may pay close attention to the subject area. It is also used as part of the financial analysis to determine the capital budget.

- Financial Review – is an analysis of the operations of the property for the last several years to determine if they are as presented in the sale.
- Tenant Communications – the TLO will continue communications with the tenants to discuss their use and plans for the facility.
- Vetting of Seller – the overall analysis that the seller has the authority to sell their interest in the property as negotiated.

The TLO will amass and study all the information produced as well as make physical inspections of the property and thorough review of the design. The information will be taken as a whole to determine if the transaction will be completed. If a concern is uncovered during the process there are various ways to negotiate and mitigate the effects. If a concern is found that is unacceptable to the TLO, the transaction may be cancelled at any time before the end of the due diligence period without penalty.

In addition for this particular transaction the TLO will closely monitor the construction of the facility through on-site inspections, and regular communication with the contractor, our partner, local officials who inspect the property, and the bank providing the construction loan.

Consistency with the Resource Management Strategy: The proposal is consistent with the long term "Resource Management Strategy for Trust Land" (RMS) which was adopted January 2016 in consultation with the Trust and provides for the TLO to focus on generating long term cash flow through asset acquisition and diversification.

Trust Land Office Recommendation: Proceed with the formation and funding of the SPE JV LLC, with Panattoni as our partner. The SPE JV LLC will construct the facility as proposed. Upon completion of the facility, the TLO intends to purchase the facility through a buy-out of Panattoni at or below market rate. Once fully owned by the Trust, the SPE JV LLC will be operated and managed by the TLO. It may also be deemed to be in the Trust's interest to allow the property to be sold on the open market to a third party at or above market rate.

Applicable Authority: State and federal authority supporting this proposed action can be found in public law, and state statutes and regulations. Primarily, the Alaska Mental Health Enabling Act of 1956 - Section 202 of P.L. 84-530, authorized the Trust to mortgage its lands.

> *"Such lands together with any property acquired in exchange therefore or acquired out of the income or proceeds therefrom, may be sold, leased, **mortgaged**, exchanged or otherwise **disposed** of in such manner as the Legislature of Alaska may provide…"*

By including the action of mortgage in the above authorized actions, Congress implied the mortgage of Trust lands was a disposal of a Trust interest. The State Legislature enacted laws providing Trust lands be managed by the Department of Natural Resources (AS 37.14.009(b)) and that the management of Trust lands be consistent with the federal enabling act (AS 38.05.801(a)). In the adoption of regulations for the Trust Land Office, the TLO Executive Director's duties and authority provides that he/she shall manage Trust lands consistent with other provisions of law as "implemented by this chapter" (11 AAC 99.010(a) Authority and duties of executive director.) Actions authorized by chapter

99 of the Alaska Administrative Code include "management, sale, lease, conveyance, permitting, licensing, dedication, and other management and disposal of trust land…" (11 AAC 99.010(b)).

In addition, the Asset Management Policy Statement (AMPS), which has been adopted by reference (20 AAC 40.600), provides guidance consistent with this proposed action (page 9, revised January 28, 2015.)

> *"Lands, structures and resources may be acquired when the acquisition will add value to The Trust's non-cash asset portfolio or will contribute to the mission of The Trust in some other way."*

Other applicable authorities include Alaska Statutes 36.30.850(b)15(B), 37.14.009, 38.05.801, 11 AAC 99.010(b), 11 AAC 99.020(b), 11 AAC 99.090(a), 11 AAC 99.090(e), 11 AAC 99.030(e), 20 AAC 40.700.

Trust Authority Consultation: This briefing document fulfills the consultation requirements that are applicable to the transaction.

---

[i] **Equity** is the difference between the market value of an asset and the mortgage thereon if any.