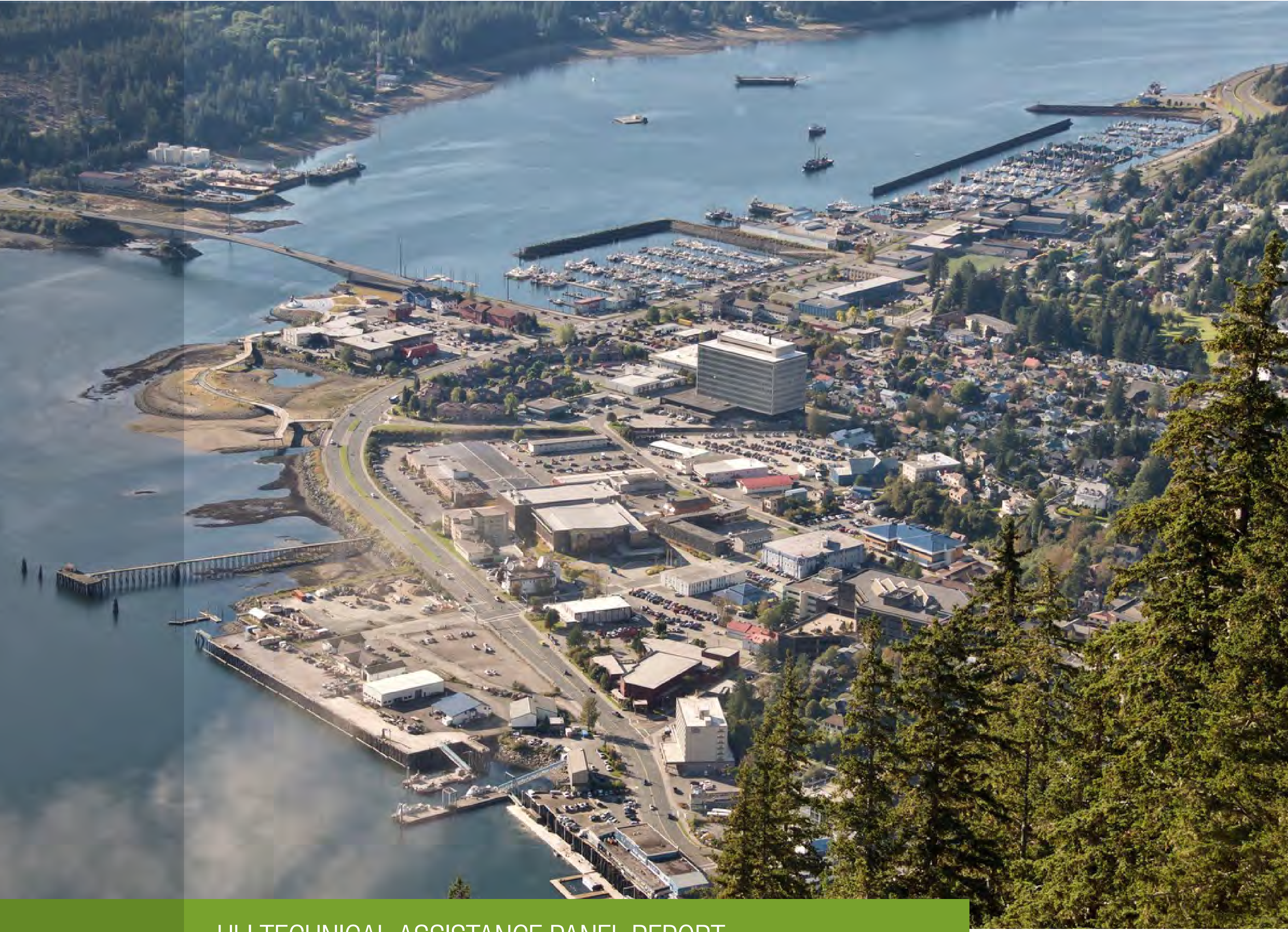

ULI TECHNICAL ASSISTANCE PANEL REPORT

JUNEAU SUBPORT DEVELOPMENT

Alaska Mental Health Trust Authority

SPONSORED BY:

Trust Land Office

Urban Land Institute Northwest

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ABOUT ULI NORTHWEST

ULI Northwest is a District Council of the Urban Land Institute (ULI), a non-profit education and research organization supported by its members. Founded in 1936, the Institute today has more than 44,000 members worldwide. ULI members represent the full spectrum of land use planning and real estate development disciplines working in the private, public, and non-profit sectors.

ULI's mission is to provide leadership in the responsible use of land and in creating and sustaining thriving communities worldwide. ULI Northwest carries out the ULI mission locally by serving as the preeminent real estate forum in the Pacific Northwest, facilitating the open exchange of ideas, information, and experiences among local, national, and international industry leaders and policy makers.

Our mission is to:

- Build a regional vision of the Northwest that embraces and acts upon quality growth principles.
- Encourage collaboration among all domains—public and private—of the real estate industry.
- Build consensus among industry and public leaders who influence land use, transportation, environmental, and economic development policies.

Contact Us

ULI Urban Land Institute Northwest

ULI Northwest
107 Spring Street
Seattle, WA 98104
206.224.4500
northwest@uli.org
northwest.uli.org

Cover photo: Subport site can be seen on left side of frame, along the water

ABOUT THE TECHNICAL ASSISTANCE PANEL (TAP) PROGRAM

The objective of ULI Northwest's Technical Assistance Panel (TAP) Program is to provide expert, multidisciplinary, and non-partisan advice on land use and real estate issues facing public agencies and nonprofit organizations in the Pacific Northwest. Drawing from its extensive membership base, ULI Northwest conducts multi-day panels offering objective and pragmatic advice to local decision makers on a variety of land use and real estate issues, ranging from site-specific projects to public policy questions. The TAP Program is intentionally flexible to provide a customized approach to specific land use and real estate issues.

Learn more at: **https://northwest.uli.org**

Table of Contents

Panel representatives for the Juneau TAP

Panelists

H. Pike Oliver,
Panel Chair
Founder, URBANEXUS

Craig Johnson
Project Manager, Heartland LLC

Kaitlin Boyce
Development Manager, Spectrum Development Solutions

Nathan Korpela
Vice President, Washington Holdings

J. Jay Brooks
Principal, Brooks Ventures LLC

Daniel P. Meyers
Senior Vice President, Madison Marquette

Rita Greene
Principal, Magnusson Klemencic Associates (MKA)

Walt Niehoff
Partner, LMN Architects

Dennis Haskell
Principal, SRG Partnership

Sarah Zahn
Director of Development, ZRZ Realty

Stakeholders & Project Staff

STAKEHOLDERS

Mike Abbott, Alaska Mental Health Trust Authority

Dan Blanchard, Uncruise

Scott Ciambor, City and Borough of Juneau

Laraine Derr, Alaska Mental Health Trust Trustee

Tracy LaBarge, Tracy's Crab Shack

Geoff Larson, Alaskan Brewing Company

Jill Maclean, City and Borough of Juneau

Joe Nelson, Sealaska Corporation

Liz Perry, Travel Juneau

McHugh Pierre, Goldbelt, Inc.

Tracey Ricker, Ricker Real Estate

Scott Shapiro, Eagle Rock Ventures

Carlton Smith, Alaska Mental Health Trust Trustee

Tom Sullivan, First National Bank of Alaska

Doug Trucano, Trucano Construction

Carl Uchytil, Port of Juneau

Paul Voelckers, MRV Architects

PROJECT STAFF

ULI Northwest

Kelly Mann, ULI Northwest

Victoria Oestreich, ULI Northwest

REPORT AUTHOR

Clair Enlow

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ULI Northwest is grateful to the Trust Land Office for its commitment to make this TAP a productive experience and owes special thanks to Aaron O'Quinn, Wyn Menefee, and Jusdi Doucet for managing program logistics and coordinating with local stakeholders and staff. The engagement and desire for development that benefits the Trust's beneficiaries and the Juneau community is reflected in this report. ULI would like to acknowledge former Alaska Mental Health Trust trustee Greg Jones and current trustee Carlton Smith, and Craig Driver, who originally recommended that the Trust Land Office work with ULI on this project. Finally, ULI thanks the stakeholders, staff, and trustees who provided valuable input for this report.

Local stakeholders share their thoughts with the Trust Land Office and TAP Panelists

Executive Summary

The Juneau Subport Subdivision (Subport) is positioned to contribute to the vibrancy of the city and the health of the local economy while the city continues to develop as a center for employment in Southeast Alaska, a cruise destination and a base for adventure tourists. It is located on the projected path of the city's signature Seawalk along the waterfront, as called for in the city's comprehensive plan. The site is also near important government, cultural and civic centers. With good design decisions and an optimum mix of uses, the 1.9-acre parcel can become an important asset to the region.

The Subport is owned by the Alaska Mental Health Trust Authority (the Trust). The Trust is charged with optimizing revenue from this property, because the primary mission of the Trust is to generate revenue on behalf of its beneficiaries. Funding is derived from land sales and leases as well as other investments owned by the Trust, with proceeds used directly for beneficiary programs or invested in the Alaskan Permanent Fund.

The Trust Land Office (TLO) is a unit of the State of Alaska Department of Natural Resources, responsible for managing and disposing of the Trust's real estate, including the Subport. With its advantageous geographical position along the city's primary shoreline, the Subport now provides short-term revenue and it is likely appreciating in value. At the same time, the TLO faces decisions about the Subport: whether to sell the property outright or seek a developer who will enter into a long-term ground lease with the TLO.

At the request of the TLO, ULI Northwest convened a volunteer Technical Assistance Panel in Juneau for a two-day intensive study of the site. The Panel considered implications of the land sale and ground lease alternatives.

The Panel concluded that, considering investment return assumptions described in this report, the TLO's least risky option is to sell the parcel. This option would likely result in similar financial returns for the beneficiaries of the Trust over a 50-year period when compared to the ground lease option. In addition, the sell option minimizes the opportunity cost of TLO staff time and management focus on the Subport.

The riskier choice, which may yield more spendable income in the midterm (5 to 30 years) as well as sale or financing options over the long term, is to seek a development partner who would be willing and able to enter into a long-term ground lease and pursue the highest and best use for the site. Panel recommendations include a conceptual site plan that outlines potential land uses that are consistent with site conditions and perceived market demand. Those uses include mixed-use residential, boutique hotel and ground-floor commercial containing retail or food and beverage.

Development of the proposed marina adjacent to the site to accommodate small to medium-size boats and smaller ships for adventure cruises could help support mixed-use residential, boutique hotel, retail, and food and beverage uses on the site.

A museum or research facility along the tidelands adjacent to the parcel would also be compatible with such a marina.

Therefore, it is in the best long-term interest of the Trust and the community for the proposed marina project to go forward in the short term, and the TLO should be ready to negotiate a right-of-way easement through the site to accommodate it.

> **“The waterfront is sacred—it’s important that whatever happens here must be good for the long term.”**

A view of the Subport looking southeast across Gastineau Channel

Background

The City and Borough of Juneau is the capitol city of the state of Alaska, located along Gastineau Channel in the panhandle. Its US Census population of 32,406 makes Juneau one of the three largest cities in the state. Drivers of Juneau's economy include government, tourism (especially the cruise ship industry) and healthcare. Historic industries include mining and logging. Commercial fishing is still a major economic sector in Juneau and Southeast Alaska. The population of Juneau can fluctuate over 100 percent with the seasonal docking of cruise ships. Much of the central business district is dominated by retail and food and beverage outlets that cater to tourists who are in the city for less than a day during the summer, from May to September. The state legislature convenes from January through April, which provides a countercyclical season, especially during weekdays.

Whale statue and fountain at the northeast terminus of the Seawalk

The undeveloped subject area, called the Juneau Subport Subdivision, lies along the shore between Egan Drive, the main thoroughfare through Juneau, and the water. It is in the projected path of the Seawalk, a unifying pedestrian corridor and main promenade along the shoreline. The Seawalk is fully built out at the cruise ship docking area and it continues to the northeast of the Juneau Subport to the destination dominated by public art. The Subport area itself lies along the shore near government office buildings and also near the Willoughby District, Juneau's civic, arts and cultural district. It does not yet support the Seawalk, and users must traverse the gap by walking along busy Egan Drive.

The owner is the Alaska Mental Health Trust Authority, a public corporation within the state of Alaska. The Trust is primarily a grant-making organization, which funds beneficiary-serving organizations who provide everything from direct services to the mentally ill to adaptive sport and safety training to employment transition service. Since 2015, it was the source of nearly $3.8 million in grants to Juneau organizations, including the Juneau Alliance for Mental Health Inc (JAHMI), Aiding Women in Abuse and Rape Emergencies (AWARE), and Southeast Alaska Independent Living, Inc. Grants are often keystone grants that make other funding possible for programs.

In an effort to geographically diversify its real estate holdings, the TLO sold many high value Alaska parcels in recent years. Proceeds of these sales were used to purchase seven investment properties in the lower 48 states. The findings of a recent legislative audit have caused the TLO to pause the use of sale proceeds (which is categorically Trust principal) to purchase investment property. This pause has necessarily caused the TLO to consider and often prioritize diversifying its income streams by other means, including more long-term ground leases of its valuable commercial properties in Alaska.

Along with first hand observations and interviews with a broad sample of stakeholders, the Panel was informed by various civic documents, including a Juneau Assembly resolution supporting the disposal of the Subport land, a vision for the Juneau Ocean Center, a marina development plan and a concept statement for Juneau District Heating. The panel reviewed the Juneau conceptual master plan for waterfront development, a due diligence report for the land, and a 1982 geotechnical investigation for the Gold Creek Reclamation Project by Dames & Moore. Additionally, the panel viewed a 2007 subdivision survey for the property and the Southeast Alaska Business Climate and Private Investment Survey of 2018. Other documents made available to the Panel were the Juneau planning documents, the Southeast Alaska 2020 Economic Plan, and the Willoughby District Land Use Plan.

With the benefit of these sources and experiences, the panel addressed the following questions from the Trust:

- For maximizing long-term revenue for the Trust, is it better to treat the parcel as a whole or should the parcel be subdivided in order to facilitate multiple uses?
- Considering the real estate market, community trends, probability of successful project, structure of real estate transaction, maximizing long-term revenues for the Trust, or any other factors applicable to the best interest of the Trust, what is the highest and best commercial real estate development use for the parcel, or what are the most ideal types of development and transactions for this parcel?
- Considering the City and Borough of Juneau's conceptual master plan for waterfront development, is there a way to maximize long-term revenue for the Trust while being consistent with the intent of the plan?
- Can the Trust do anything to this parcel or in preparation that will help the Trust Land Office better market this parcel to potential developers?
- Are there any timing considerations that may influence whether a long-term action should be taken on this parcel now or later?

TAP Panelists at Tracy's King Crab Shack, which currently sits on the site

Recommendations

The Trust faces a basic, binary decision about disposing of its Juneau Subport site. Put simply, it must answer the following question: Should the Trust sell the site outright, or should it seek a development partner under a long-term lease? A sale would be the simpler option. A long-term lease allows more flexibility and control of use, and also potentially more revenue. But it also brings more risk. As described below and in graphic analyses on pages 12-13, projected financial returns in the two scenarios are close.

The Panel noted that there is local interest in purchasing the Subport site and developing a marina on tidelands adjacent to the site, and there is community support for such a project. There is also considerable local support for a proposal called The Juneau Ocean Center—a research, exhibit and meeting facility that could complement the other civic arts and cultural facilities in the neighboring Willoughby District.

As the Panel set out to offer advice to the Trust, members sought answers to two overarching questions. One is about highest and best use: What kind of development brings the most value to the owner and to the community? The answer to this question informs the second one, which is financial: What is the best way to dispose of the land in light of risks and potential returns?

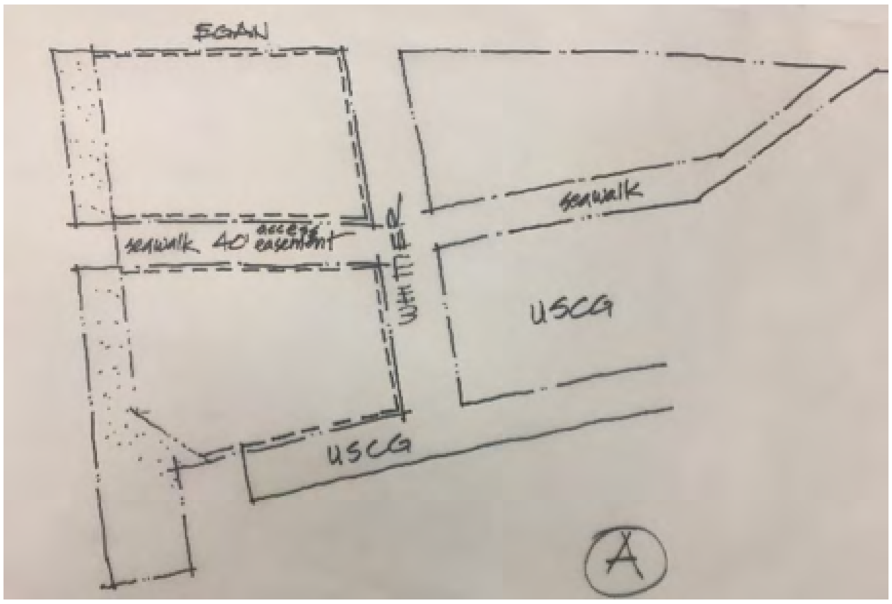
Highest and best use

Recommendations include conceptual site sketches on page 11, which show a suggested division of uses and an ideal level of development intensity. Optimum use of the land is likely to be achieved by dividing the existing parcel into smaller parcels around key rights-of-way in preparation for sale or lease. No specific improvements other than subdivision and dedication of key rights-of-way need to be made prior to disposal.

Parcelization would enhance value to the public by accommodating extension of the Seawalk in an alignment that is consistent with the City's long-term waterfront planning. At the same time, dividing the site may enhance developer interest by allowing for smaller acquisition or ground lease opportunities and by connecting the property with future development (the marina) while allowing flexibility for future uses on the site.

“It doesn't work as a single site.”

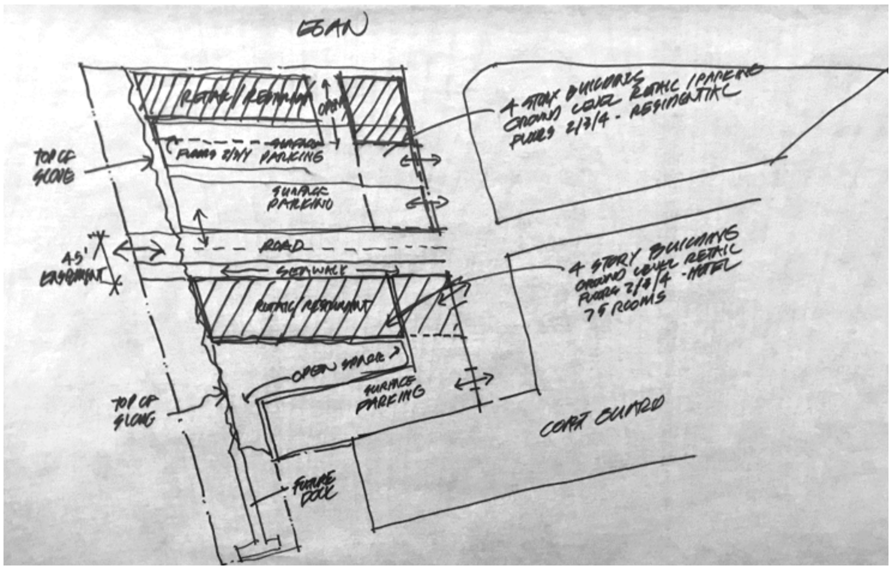
Divisions. The optimum division or parcelization would begin with a continuation of Whittier Street alignment into the Subport in a new right-of-way perpendicular to Egan Drive. This street would become the essential landside access for a marina nearby, through an easement or dedicated right-of-way through the Subport. It would contain continuing utilities that now run along Whittier Street. It may have the character of a community street similar to Pike Place in Seattle, wherein pedestrians share the roadway with slow vehicular traffic. The division should accommodate a second pedestrian street or wide walkway through the center of the site that is roughly parallel to Egan Drive. This walkway would be a continuation of the Seawalk, connecting other sections on either side of the site.



Sketch showing a potential easement parallel to Egan Drive

Uses. The best mix of uses would build upon the potential moorage adjacent to the site and the anticipated growth in adventure cruising. It may include a mix of housing (apartments and/or condos), food and beverage, retail and hospitality. A boutique hotel would complement the value of the marina and support adventure cruising, which brings an estimated $2,100 per visitor into the economy, in contrast to $300 per visitor for the traditional cruise industry. While surface parking does not optimize the use of the site, it may be necessary to comply with zoning, and it can be accommodated with low-rise (four-story) buildings. The city may be willing to significantly reduce parking requirements based on proposed uses. Feasibility of any use is subject to market conditions. While there is proven demand for apartments, condos and retail within the Juneau market and a need for additional hotel rooms, the boutique hotel would be a new class of high-end product within the market and would require average daily rates that greatly exceed the current stock of hotel rooms.

> “Have people come in and see how to fillet a fish.”



Sketch showing a scenario in which mixed-use developments front Egan Drive and Seawalk

Intensity. Market demand and site conditions are such that exceeding the intensity called for in the city's development plans and regulations is not warranted. The site can support only low-to-medium intensity development. This would mean four-story-high buildings, at 45 feet in height, with floor-to-ceiling heights of 15 feet for ground floor retail and 10 feet on upper floors. Such a scheme would yield about 76 apartments, 17,800 square feet of retail space and a 75-room boutique hotel, along with 130 stalls of surface parking and a small amount of open space.

> "How much meeting space does the town need?"

Financial assumptions and projections

Cashflow projections, as shown in analyses on pages 12-13 are based on the following general assumptions:

- The value for developable land is $40 per square foot.
- There is a one percent transaction cost.
- The cash flow duration is 50 years.

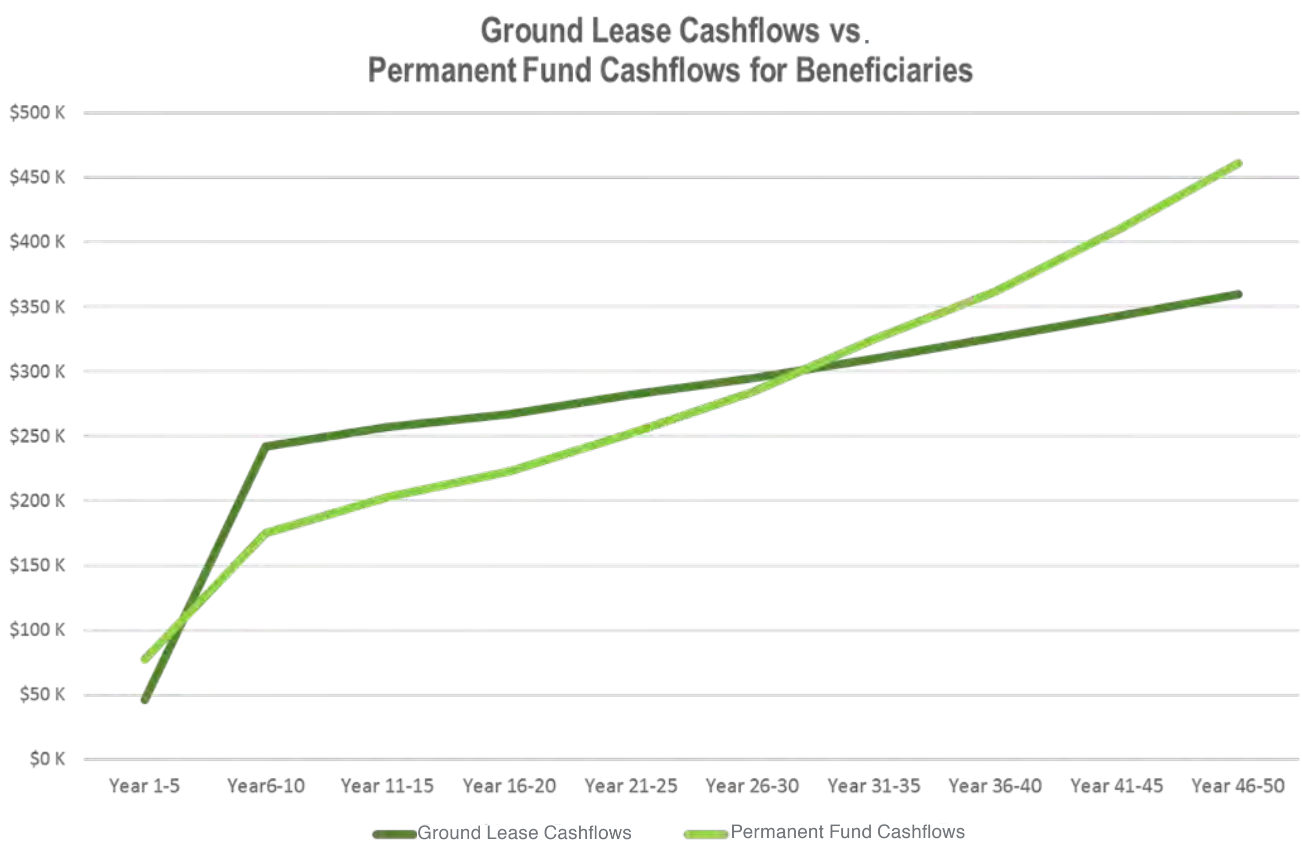
A discount rate of 6.55 percent determines the present value of future cash flows. It is estimated that a fee simple sale would net $3.0 million in principal funds to the Trust. Principal funds are statutorily required to be placed in a trust fund managed by the Alaska Permanent Fund Corporation. Trust policy currently dictates that the Trust may draw 4.25 percent of its trust fund balance yearly. Returns for the first five years would average $78,000 annually and grow to an estimated $483,000 in year 50 for a total net present value (NPV) of $2.75 million.

The fee simple sale option is based on the following assumptions:

- The land sale would take place in 2019.
- Annual Permanent Fund returns will average 6.55 percent.
- The annual payout from the trust fund remains 4.25 percent of the balance.

For the sake of comparison, the ground lease option is based on the following cash flow assumptions:

- Ground lease payments are set at seven percent of total value.
- Values step up by 5.1 percent every five years (assuming the value of land appreciates at one percent per annum).
- Ground lease begins when construction is complete (1/1/2022).
- Income from existing leases at the Subport continues for the next two years.
- $300,000 is expended on preparing site information required to secure ground lease bids.
- There is no sale of underlying land after 50 years.



Graph comparing ground lease cashflows and Permanent Fund cashflows over a 50-year period

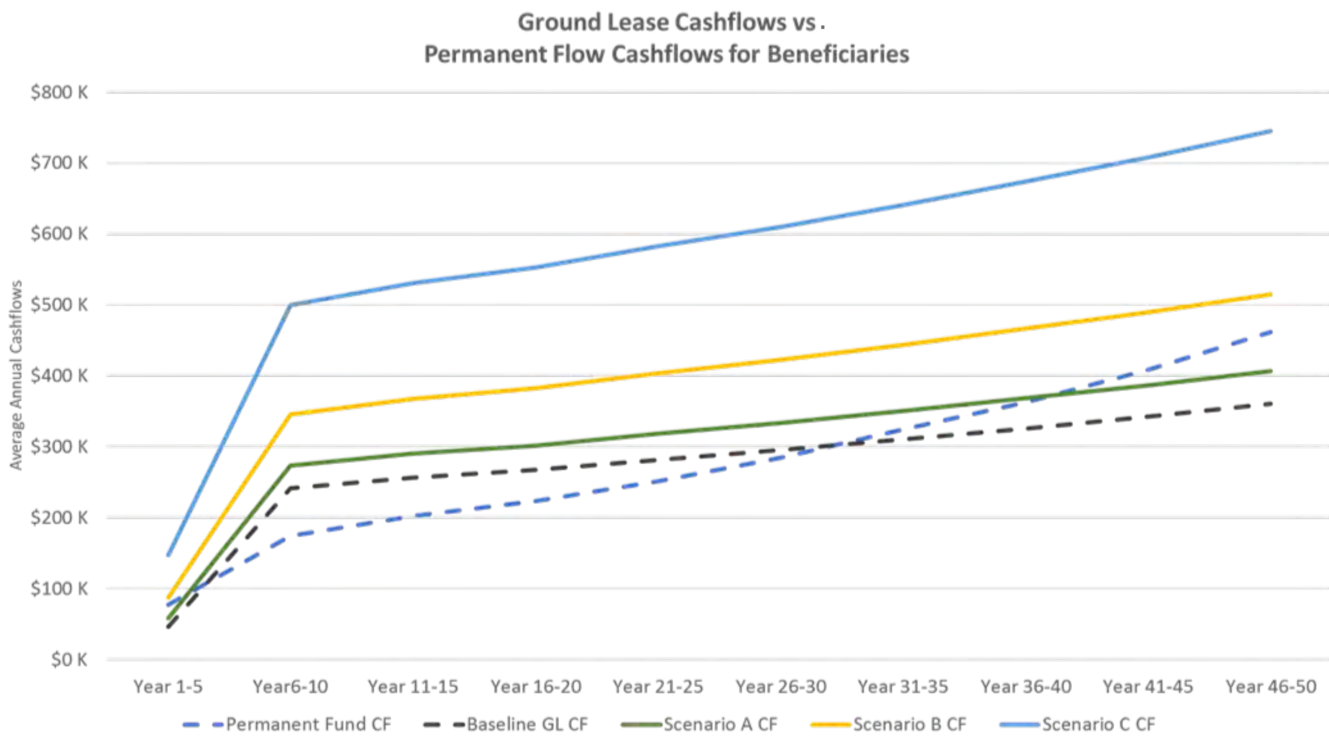
	Years 1-5	Years 6-10	Years 11-15	Years 16-20	Years 21-25	Years 26-30	Years 31-35	Years 36-40	Years 41-45	Years 46-50	NPV@ 6.55%
Ground Lease Cashflows for Beneficiaries	$46 K	$242 K	$257 K	$267 K	$282 K	$295 K	$310 K	$326 K	$343 K	$360 K	**$2.95M**
Permanent Fund Cashflows for Beneficiaries	$78 K	$175 K	$203 K	$223 K	$252 K	$284 K	$325 K	$362 K	$409 K	$461 K	**$2.75M**

Ground lease and Permanent Fund cashflows (5-year averages)

	Program	Overall Cost	Target Return on Cost	Estimated Ground Lease Payment	Comments
Scenario A: Mixed-Use Lower Density	48 units rental apartments 17,800 sf retail 60 room boutique hotel	$31.6M	8%	$315k (year 1)	Parking requirements on site
Scenario B: Mixed-Use Maximize Capacity	77 units rental apartments 17,800 sf retail 75 room boutique hotel	$42.6M	8%	$240k (year 1)	With fee-in-lieu parking
Scenario C: Mixed-Use Max w/condos	77 units for sale condos 17,800 sf retail 75 room boutique hotel	$44.0M	8%	$490k (year 1)	Challenging to find sophisticated developer With fee-in-lieu parking Complex structure (condos on ground lease)

Chart comparing three ground lease scenarios

TAP panelists review potential ground lease scenarios



Graph comparing ground lease cashflows in the three scenarios and Permanent Fund cashflows over a 50-year period

A ground lease, based on these assumptions, would generate $46,000 in the same five-year period. It would then surpass the returns of the sale scenario for the following 25 years but would be less than the sale scenario after year 25. The total NPV of just the ground-lease payments would be slightly higher than the sale scenario at $2.95 million (see two tables: Ground Lease Cashflows versus Permanent Fund Cashflows for Beneficiaries).

In addition, unlike the sale scenario, the TLO would be able to capitalize the principal (i.e. the underlying land asset) during the lease term. The value of the land is likely to appreciate one percent per annum based on the TLO estimate. Assuming the TLO held the land for a full 50-year lease term with an estimated worth of $3 million now, in year 50 the land value would be $4.99 million. Discounting this future value back to the present at a 6.55 percent rate (the discount rate given by the TLO) would result in an NPV of the underlying land asset of $220,000 and increase the total present value of the ground lease option from $2.95 million to $3.15 million.

There may be strategic financial reasons an owner may choose to generate cash flow through a long-term lease, such as the desire to enhance operating capital over time. Also, an owner could potentially sell or borrow against the land with a ground lease in place. The land could be sold at the end of the lease period, although the value of improvements is typically nil at that time.

In conservative cash flow projections for a long-term (50-year) lease, the lease option is roughly similar to the sale option in returns. There is an upside potential for a long period of robust returns on a ground lease, but it comes with high risks. Exposure to these risks begin in the months of preparation for marketing the land to potential lessors with desire and capacity to develop the parcel. This preparation typically involves a request for proposal (RFP) and an information packet that reflects due diligence. The ground lease scenario is subject to the following risks and uncertainties:

Panelists review potential site designs

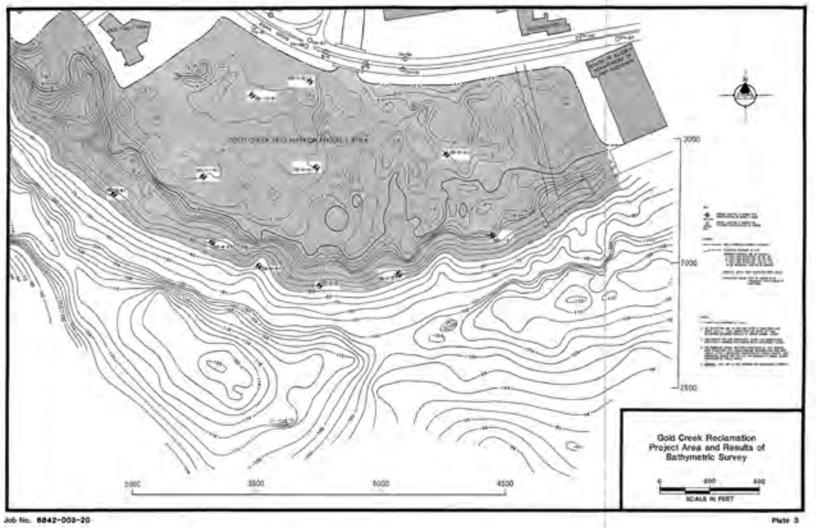
Lack of local market. There is little evidence of Juneau-based demand for a ground lease. In general, ground leases are less attractive to institutional capital. Though ground leases are common in other parts of Alaska, long term lease between owner and developer are unknown in the region, which means the land may need to be marketed to an outside developer who is comfortable with it. The Trust would need to develop a request-for-proposal, accompanied by a geotechnical analysis, a bulkhead concept, sea level rise projections (FEMA data), an environmental soil study, and market data. In addition, there is risk that if the Trust “stays in the deal” via a ground lease, there could be negative public perception if the lessor’s project fails to materialize or runs into significant challenges.

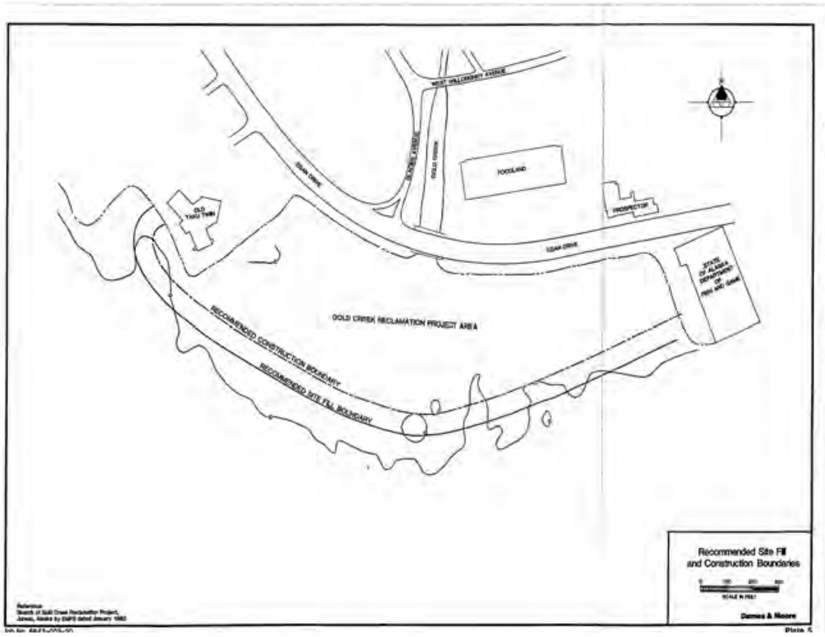
Ongoing community and organization challenges. As it grapples with decisions about the site, the TLO faces challenges from the local community. These include:

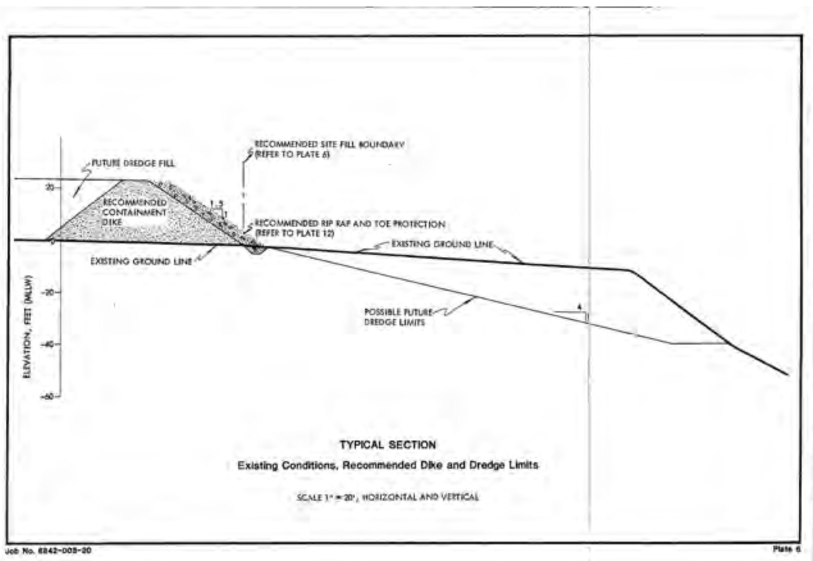
- Opaque goals. The Trust has been reviewing options for this site for a number of years without visible progress.

- Need for a local champion. The Trust has lacked a local advocate with the ability to connect with stakeholders and interact with those interested in acquiring the site.
- Limited community understanding of the Trust's primary mission. The Trust desires a favorable outcome for the community, but this is secondary to its fiduciary responsibility to its beneficiaries.
- Lack of transactional connections locally and nationally. Given the complexity of disposing of this site and the need to attract investors from outside the region, a broker may be appropriate.
- Diversion from focus on the Trust's other assets. With finite management and staff time, the Trust may be best served by refocusing on its broader portfolio.

Geotechnical complications. A Geotechnical analysis for a site directly north of the Subport, prepared by Dames and Moore in 1982, was reviewed. It involved 11 borings to 20 feet, supplemented with data from the geotechnical investigation for the Juneau-Douglas Bridge, and showed a silty fine to medium sand layer likely to extend 150 to 170 feet below grade. Below the sand layer, a dense layer of glacial till is expected, with bedrock at about 170 to 210 feet below grade. Although not addressed in this report, soils of this type typically do not have high bearing capacities. Construction of multistory structures may require a deep foundation, but lighter buildings may require only shallow foundations. Soil improvements may be required to mitigate liquefaction. The Dames and Moore analysis also addressed stability of a submerged slope to the south of the site. The slope appears to align with the current bulkhead at the site and is expected to extend the length of the site boundary. The report recommended a fill and setback for the adjacent site to limit damage during the analyzed seismic event. In order to determine requirements specific to the Subport site, a new geotechnical investigation is called for.







Images from Dames and Moore Geotechnical report, 1982

Conclusion

It is clear that the Trust's highest priority is the welfare of its beneficiaries and the return on investment that supports those beneficiaries. The Juneau Subport Subdivision is one of its better-quality developable assets.

With the future of this extraordinary site at stake, it is also appropriate for the Trust to proceed carefully in its disposal, and to consider the consequences of its decisions about how and when to proceed in a sale or lease. Part of that care is to determine the likely uses and best direction for development.

Based narrowly on investment risks and returns, and according to assumptions described in this report, the Trust's best option is to sell the parcel outright. This option is preferred by a slight margin over a long-term lease, only because it is relatively risk free and it is also projected to lead to slightly better financial returns for the Trust, both in the short and in the long terms. A sale converts a risky investment into a more predictable and steady income stream for beneficiaries.

The Panel recommends the following simultaneous actions based upon this conclusion:

- Seek a buyer based on a general estimate of value of $40 per square foot of usable land.
- Work with the owner-developer of the proposed marina to guarantee an access easement through the Subport land so that marina construction can proceed in advance of overall Subport development, if such an arrangement is advantageous to the Trust as well as other parties. This access should be compatible with parcelization of the site.

The Trust is to be commended for placing the highest priority on its fiduciary role toward Trust beneficiaries, but also for its desire to optimize the development of the Subport site. The sooner the shoreline and related urban developments are completed, the better for the city and for the region.

Panelists tour the Willoughby District

Urban Land Institute
Northwest

ULI Northwest
107 Spring Street
Seattle WA 98104
206.224.4500
northwest@uli.org
northwest.uli.org