Innovative Property Financing Tools and Methods

PANELISTS
JOE EUPHRAT, CLEANFUND
MATT SUTHERLAND, CEC-X
DEAN BRITTON, AIA TERRA

MODERATOR
JOHN COE, COE ENTERPRISES

SEPTEMBER 20, 2019
Company Info

- CleanFund- Leading provider of Commercial PACE Financing
- CEC-X- First marketplace to hedge credit risk for commercial real estate loans
- AIA Terra- Bifurcating fee simple estates into leased fee and leasehold estates
- Coe Enterprises- Providing real estate capital markets and strategic advice
Base Financing Case

Situation: Client is developing a 250,000 s.f. speculative office building in Washington DC CBD. Total Project Costs are $100,000,000. Client is seeking at least the following structure:

- Construction Loan of $65,000,000 (65% Loan to Cost)
- Institutional JV Equity of $31,500,000 (90% of Total Equity)
- Sponsor Equity of $3,500,000 (10% of Total Equity)
CleanFund
CleanFund

Joe Euphrat, Managing Director

WHO IS CLEANFUND?

✦ Leading national provider of Commercial PACE (C-PACE) financing
✦ PACE originations platform - focus is on C-PACE only
✦ Proven execution
✦ Direct Lender of C-PACE capital (not brokers)
✦ $1B+ in lending capacity
✦ Vertically integrated platform with originations, credit, underwriting and government affairs
✦ Relationships with select lenders that are open to C-PACE
✦ CleanFund is backed by Starwood Sustainable Credit, a subsidiary of Starwood Capital Group and Vulcan Capital, the investment arm of the late Microsoft co-founder, Paul Allen.
## CleanFund C-PACE Financing Terms

<table>
<thead>
<tr>
<th><strong>Financing Amounts:</strong></th>
<th>$1,000,000 to over $100MM</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Term:</strong></td>
<td>Up to 30 years, with interest rate fixed at the time of commitment letter</td>
</tr>
<tr>
<td><strong>Recourse:</strong></td>
<td>None. The financing is non-recourse to the property owner or sponsor</td>
</tr>
<tr>
<td><strong>Rate:</strong></td>
<td>300+ basis points above like-term US Treasuries (high 5% to mid 6%)</td>
</tr>
<tr>
<td><strong>Property Types:</strong></td>
<td>Commercial, Hospitality, Healthcare, Industrial, Multifamily, Non-profit and certain specialty property types</td>
</tr>
<tr>
<td><strong>Eligible Improvements:</strong></td>
<td>Renovations, retrofits or new construction related to energy efficiency, water conservation, renewable energy and/or seismic strengthening.</td>
</tr>
<tr>
<td><strong>Type of Financing:</strong></td>
<td>Special assessment recorded on the subject property, paid back via property taxes, and runs with the property in a transfer. No assignment and assumption req’d.</td>
</tr>
<tr>
<td><strong>Loan to Value:</strong></td>
<td>Up to 20% As Completed value subject to identifying qualified costs</td>
</tr>
<tr>
<td><strong>Prepayment:</strong></td>
<td>At anytime subject to a negotiable fee</td>
</tr>
<tr>
<td><strong>Funding:</strong></td>
<td>Within 45-60 days from signed Term Sheet</td>
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**With CPACE**

- 3.5% Sponsor Equity
- 10% CPACE
- 21.5% Sponsor Equity
- 65% Debt

CPACE reduces JV Equity by 10%

**Without CPACE**

- 3.5% Sponsor Equity
- 31.5% JV/LP Equity
- 65% Debt
CEC-X Inc.

Matthew Sutherland, CEO

- CEC-X is the first marketplace to hedge credit risk for lenders making quality CRE loans.

- CEC language is standardized to offer lenders an unconditional “Eligible Guarantee”.

- CECs reduce the risk of CRE lending and save borrowers millions in loan interest.

- Quick stats on CEC-X financings:
  
  $1.5+ Billion of CECs Scheduled for 2020
CEC-X Inc.

Virtually Every Market

*(Except Commercial Real Estate)*

has an Efficient Way to Hedge Credit Risk

through Insurance, CDS or Derivatives…
CEC Marketplace

**CRE Borrowers**
- Credit Enhancement
- Higher IRRs
- Better Loan Terms
- Better Loan Servicing

**CRE Lenders**
- Credit Protection
- Broader Market for Distribution
- Lower Cost of Capital

**CEC Writers**
- Low Cost Origination
- Diversification
- Superior IRRs
- Path to Collateral

**CEC Clearing**
- Capital-Lite Exposure
- Superior, Non-Correlated Revenue
- Low Attachment Point

**CEC-X**

Supply of CRE Loans

Demand to Write CECs
Adding a CEC to the Capital Stack saves this Borrower >$1M per year and makes the loan safer for the Senior Lender.

**BASE CASE**

Cost of Capital = $9.9M @ 65% LTC

- $31.5M @ 20% IRR
  - = $6.3M per year
- $65M @ 5.57% Interest Rate
  - = $3.6M Interest Cost per year

**WITH CEC**

Cost of Capital = $8.8M @70% LTC

- $26.5M @ 20% IRR
  - = $5.3M per year
- $70M Senior Debt @ 4.25% Interest Rate
- $70M of CEC Protection @ 0.70% Interest Rate
  - = $3.5M Interest Cost per year
Adding a CEC with CPACE to the Capital Stack saves this Borrower >$1.5M per year and keeps the loan safer for the Senior Lender.

<table>
<thead>
<tr>
<th></th>
<th>BASE CASE</th>
<th>WITH CEC</th>
<th>WITH CEC AND CPACE</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cost of Capital</strong></td>
<td>$9.9M</td>
<td>$8.8M</td>
<td>$8.3M</td>
</tr>
<tr>
<td><strong>$3.5M</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>$31.5M @ 20% IRR</strong></td>
<td></td>
<td>$26.5M @ 20% IRR</td>
<td>$16.5M @ 20% IRR</td>
</tr>
<tr>
<td><strong>= $6.3M per year</strong></td>
<td></td>
<td><strong>= $5.3M per year</strong></td>
<td><strong>= $4.3M per year</strong></td>
</tr>
<tr>
<td><strong>65% LTC</strong></td>
<td></td>
<td><strong>70% LTC</strong></td>
<td></td>
</tr>
<tr>
<td><strong>$65M @ 5.57% IR</strong></td>
<td></td>
<td><strong>$70M @ 4.25% IR</strong></td>
<td><strong>$60M @ 4.25% IR</strong></td>
</tr>
<tr>
<td><strong>= $3.6M Interest Cost per year</strong></td>
<td></td>
<td><strong>= $3.5M Interest Cost per year</strong></td>
<td><strong>= $4.0M Interest Cost per year</strong></td>
</tr>
<tr>
<td><strong>Sponsor Equity</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Debt</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>JV/LP Equity</strong></td>
<td></td>
<td></td>
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AIA Terra
“Lease Monkeys”… specializing in bifurcating Fee Simple Estates into:

* Ground (or “Leased Fee Estate”) and
* Improvements (the “Leasehold Estate”)

PURCHASER of smaller ground leases
LENDER (with LifeCo partners) on mid-sized deals
ADVISOR to Sponsors on very large ($100M+) bifurcations

AIA partners, Dean Britton, Barry Funt and Grant Rogers, have over 60 years of shared RE capital markets experience.
What is a Ground Lease… *Legally?*

### One Fee Simple Estate becomes Two Separate Estates

- **Fee Simple Estate**
- **Leased Fee Estate (Ground)**
- **Leasehold Estate**

### Ground Lease Terms

- 99 year term is typical, but can be shorter
- Ground lease payments are an *unsubordinated* claim in the property.
- Effectively a second tier of RE tax
- Building reverts to land owner at expiration or earlier upon default. In such event, any Leasehold debt on property is extinguished if payment default uncured.
- Leasehold lender has cure rights if Ground Lessee defaults.
- Ground lease not subject to early termination except in the case of condemnation.
“A Third of Value for a Quarter of Cashflow”

- **Cash flow**
  Ground rent typically 20-35% of Property CF (3-5x coverage)

- **Cap Rates**
  3.5% - 5% (varies by market, property type, quality, and leverage)

- **Value**
  Typically 35% of fee simple value (40-45% in prime markets)

- **Rent Growth**
  2%-2.5% per annum, with CPI catch-up in later years (if CPI > bumps)

- **Property Expenses**
  Ground Lessee responsible for all property expenses (triple net)
**What is a Ground Lease…**

*Functionally?*

<table>
<thead>
<tr>
<th><strong>Four Quadrants” Groundlease Matrix</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Stabilized</strong></td>
</tr>
<tr>
<td><strong>Purchase</strong></td>
</tr>
<tr>
<td>40% of Property Value</td>
</tr>
<tr>
<td>3.0X coverage</td>
</tr>
<tr>
<td>2% growth with inflation</td>
</tr>
<tr>
<td>3.5-4.5% cap rate</td>
</tr>
<tr>
<td><strong>Lending</strong></td>
</tr>
<tr>
<td>20-40 year term</td>
</tr>
<tr>
<td>80-95% leverage</td>
</tr>
<tr>
<td>UST + 175-225</td>
</tr>
</tbody>
</table>
Why the Great (GL) Revival? *Interest Rates!*

- Two bites at the Mortgage Apple...
- Repurchase Rights let Owners view Ground Leases as Long-Term Financing
Why the Great Revival? *Buyers/Recaps...Leverage!*

- Leverage - Reduces equity requirement & Increases investment yield
- Non-Callable Long-term Leverage with Repurchase Right
- Base Case $100M Purchase, 6% Cap Rate (NOI: $6,000,000)

<table>
<thead>
<tr>
<th>NCF:</th>
<th>$2,048,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity:</td>
<td>$35MM</td>
</tr>
<tr>
<td>Initial Yield:</td>
<td>5.85%</td>
</tr>
<tr>
<td>Loan:</td>
<td>$65M (65% LTV)</td>
</tr>
<tr>
<td>Loan Rate:</td>
<td>4.5%, 10 on 30</td>
</tr>
<tr>
<td>Debt Service:</td>
<td>$3,952,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>NCF:</th>
<th>$1,955,250</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity:</td>
<td>$22.75MM</td>
</tr>
<tr>
<td>Initial Yield:</td>
<td>8.6%</td>
</tr>
<tr>
<td>Leasehold Loan:</td>
<td>$42.75 (65% LTV)</td>
</tr>
<tr>
<td>Loan Rate:</td>
<td>4.75% 10 on 30</td>
</tr>
<tr>
<td>Debt Service:</td>
<td>$2,644,750</td>
</tr>
<tr>
<td>Ground Price:</td>
<td>$35M</td>
</tr>
<tr>
<td>Ground Rent:</td>
<td>$1,400,000</td>
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<tr>
<td>Ground Cap:</td>
<td>4%</td>
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Think Like Your Own Family Office:
Sell the building...HOLD YOUR GROUND

• Reduce taxable gain?
your 1031 Exchange is IN YOUR OWN GROUND

• Long term income with *de minimus* operations

• Estate Value appreciates generationally

• PRITZKERS, HELMESLEYS, ZECKENDORFS etc
Why the Great Revival?  *Developers...Basis!*

- Reduction in Equity Requirement
- Ability to get CREDIT for VALUE of SITE ENHANCEMENTS
- Opportunity to develop asset without “LP” partners, gives
- Option to HOLD the improvements upon stabilization
Proposed Questions

- PACE Financing is a viable alternative to mezzanine financing and preferred equity due to attractive relative pricing. However, first trust lenders perceive PACE as an encumbrance to securing their first lien rights in the event of default. How has CleanFund addressed this concern with lenders?

- CEC-X is a new phenomenon in the market. How has its technology been accepted by both the investor/enhancement provider market as well as the real estate lending market? What will be its tipping point for success?

- Bifurcation financing offers higher leverage with offsetting risks providing a sponsor/borrower an overall lower cost of capital, yet with perhaps a more challenging recapitalization or exit strategy. What are the ideal circumstances for considering this type of financing?

- If the capital markets become less “fluid” and providers become more conservative in their underwriting and approvals how will each of these alternatives provide either more stability or liquidity to a tightening market?

- What obstacles have each of these alternatives faced in reaching their market potential? How will these challenges be overcome?
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