

FCR 8

Office of the President
February 21, 2012

Members, Board of Trustees:

AUTHORIZATION OF GROUND LEASE FOR STUDENT HOUSING

Recommendation: that the Board of Trustees authorize the President, or his designee, to enter into a long-term ground lease with an affiliate of Education Realty Trust, Inc. (“EdR”) guaranteed by Education Realty Operations Partnership, LLC for purposes of development and potential management of a student housing project.

Background: At the Board of Trustees retreat on October 1 and 2, 2011, the Board identified the need to expand and improve student housing facilities as a primary strategic priority. On October 26, 2011, the University issued a Request for Proposal seeking developers with the capacity and interest in partnering with the University to complete a long-term housing plan. On December 13, 2011, the University announced that it would negotiate with EdR, a third-party developer, to improve, expand, and potentially manage student housing beginning with construction of two new buildings on Haggin Field.

According to Moody’s Investment Service, universities have been utilizing public-private partnerships (P3) for student housing for nearly two decades. Such a strategy is appropriate for UK given the advanced age of the student housing stock and the University’s desire to modernize and expand it quickly while reserving debt capacity for other capital projects. The University will maintain control over the Resident Life programs.

EdR is a publicly traded real estate investment trust headquartered in Memphis, Tennessee, with more than 50 years of student housing experience. Since 2000, EdR has completed more than \$2.3 billion in collegiate housing transactions, including investing \$1.3 billion in private equity. EdR currently owns or manages 57 student housing properties with approximately 34,000 beds in 23 states, including four facilities at the University of Louisville. EdR has proposed to provide a 100 percent equity investment in UK’s student housing.

This project is the development of two buildings with a total of 601 undergraduate beds at Haggin Field. The P3 arrangement will include a ground lease of Haggin Field to EdR for an initial term of 50 years with two renewal options of 10 years and 15 years, respectively. The ground lease will include maintenance standards for the facilities and parameters for the room rental rates for the duration of the lease. In addition to receiving funds for the Resident Life programs in the facilities, the University will receive a percentage of gross revenues and, after EdR achieves a minimum internal rate of return, a share of net income.

The University's housing stock currently includes 5,154 undergraduate beds and 816 efficiency, one- and two-bedroom apartments for graduate students and family housing. The average age of the residence halls and apartments is 44 years and 48 years, respectively.

A summary of the terms of the draft ground lease is attached. The draft agreement can be viewed at http://www.uky.edu/Housing/facilities_documents.html. The draft agreement may be modified prior to execution, if necessary. Any substantive modifications will be reported to the Board. If the Board authorizes the President to enter into this long-term ground lease, an affiliation agreement between the University and EdR outlining how the housing facility would be operated and maintained will also be executed.

This project represents the first step in the transformation of student housing. The total development is anticipated to include up to 9,000 replacement and expansion beds and be completed within seven years.

Action taken: Approved Disapproved Other _____

University of Kentucky and Education Realty Trust, Inc.
Draft Ground Lease
Summary of Terms

- Project:
 - Lease of Haggin Field to EDR Lexington LLC 1 (EdR), guaranteed by Education Realty Trust Operating Partnership, LP, for development, leasehold ownership, and management of an undergraduate student housing facility
 - Estimated development cost: \$25.8 million (100% equity funded by EdR)
 - University shall approve any material changes to plans and specifications
 - Occupancy: August 2013
 - Facilities:
 - 2 buildings
 - 601 double occupancy rooms
 - Offices for University's Honors Program and Resident Life staff
 - Three 'smart' classrooms
 - EdR will seek LEED-Silver certification

- Term:
 - Original Term: 50 years
 - First Renewal Term: 10 years
 - Second Renewal Term: 15 years
 - Both parties must agree to extension(s) of the original term
 - University shall have option to terminate lease upon the 20th, 30th, and 40th anniversary dates upon payment of an early termination fee
 - Expiration of Term:
 - At expiration of original term or first renewal term, University shall purchase facilities at their appraised value or
 - At expiration of second renewal term, University shall purchase facilities at the greater of:
 - Depreciated value or
 - \$10.00

- Residential rental rates:
 - 2013-14 Not to exceed \$3,490 per bed per semester
 - 2014-15 to 2016-17 Annual rate increase limited to the greater of:
 - (3-years) a) 3% or
 - b) percentage rate increase of university-owned housing
 - Effective 2017-18 Annual rate increase limited to the greater of:
 - a) 4% or
 - b) 2-yr rolling average increase in consumer price index or
 - c) percentage rate increase of university-owned housing

- EdR Financial requirements:
 - EdR shall not mortgage, pledge, or encumber the facilities or property
 - Allocate \$260 per bed per year for Replacement Reserve; allocation to increase over time by an amount sufficient to ensure the facilities are maintained in a first class manner
 - Provide the University \$639 per bed per year for Resident Life; rate may increase annually by the greater of:
 - 3% or
 - University's salary increase pool
 However, annual rate increase may not exceed the percentage increase in rental rates

- Financial return:
 - Education Realty Trust
 - 4% management fee based on gross revenues; reduced to 2% upon execution of contract to construct 2,500 beds (including 601 beds for this project) or manage university-owned housing
 - Minimum 9% internal rate of return (IRR)
 - University of Kentucky
 - 10% of gross revenues; increased by 2 points to 12% upon execution of contract for EdR to construct at least 2,500 beds (including 601 beds for this project) or manage university-owned housing
 - 25% of net income in each year in which EdR achieves 9% IRR

- Rights, Risk and Other Requirements:
 - EdR assumes construction and operating risks
 - EdR must comply with University's existing vendor contracts
 - University may audit EdR's financial records
 - EdR shall pay prevailing hourly rates for the construction
 - Dispute resolution shall proceed as follows:
 - Good faith negotiation
 - Private mediation
 - Legal action
 - University retains all naming rights

- Responsibilities:
 - EdR responsible for maintenance, operation, and taxes related to the facilities, except lawn care and snow removal
 - EdR responsible for insuring premises at replacement value
 - University responsible for Residence Life Programming including the hiring of residence advisors and resident hall director

- Tenant Default:
 - If Tenant defaults, the University has a number of remedies, including: pursuing legal action for damages, specific performance, terminate lease (upon payment to EdR of the appraised value of the facilities, less damages), require EdR to market and sell the lease to a third party
 - Tenant defaults include: failure to pay rent; failure to observe and perform terms; bankruptcy; abandonment; failure to discharge liens; assignment of lease in violation of terms

- Change of Control and University's Right of First Refusal:
 - Established requirements for Qualified Assignee and terms of a Permitted Assignment
 - University has right of first refusal at a price:
 - During the original term, price contained in Bona Fide offer
 - During the renewal term, the price shall be the lesser of:
 - Bona Fide offer or
 - Appraised value
 - During the second term, the price shall be the greater of:
 - Depreciated value or
 - \$10.00
 - Under certain circumstances, EdR's public company parent may undergo a change of control without triggering University's right of first refusal