

**STATE UNIVERSITY SYSTEM OF FLORIDA
BOARD OF GOVERNORS
Project Summary
Florida Polytechnic University
Student Housing Project Phase II**

Project Description: The proposed project (the “Project”), includes the construction of a 543 bed, 131,695 gross square-foot, five-story student residence facility, and associated infrastructure and amenities, such as an outdoor pool and volleyball courts. The Project will be owned by VC FPU Housing II, Ltd, (the “Owner”), a partnership owned by Vestcor Communities, Inc. The Florida Polytechnic University (“FPU” or the “University”) will enter into an Operating Agreement and a Ground Lease with the Owner to design, construct, finance, operate and maintain the Project on the FPU campus. Consent to enter into the Ground Lease as provided in F.S. 1013.171 is not required, as the University holds title to the property rather than the Board of Trustees for the Internal Improvement Trust Fund. The Owner will enter into a separate Management Agreement with Ambling Student Housing (the “Manager”) to operate the Project.

The Project is included in the campus master plan.

Project Site Location: The Project will be located on FPU’s campus in Lakeland, adjacent to the existing student housing facility.

Projected Start and Completion Date: It is anticipated that construction will commence in March 2015 with design creation, and is expected to be completed by August 15, 2016, with occupancy beginning Fall 2016. Should the Project fail to open by August 15, 2016, the Owner is responsible for providing temporary housing and transportation costs for residents until completion of the Project.

In the event the Project completion deadline extends beyond August 15, 2016, as a result of delays caused by FPU, FPU shall reimburse the Owner for temporary housing and transportation costs. FPU does not anticipate any Project delays and has not identified an account from which such a reimbursement could be made.

Project Cost:

The total cost of the Project is estimated at \$22 million, which includes construction costs of approximately \$17.8 million (including a contingency budget of \$400,000), with planning, equipment and other estimated soft costs of \$4.2 million (including capitalized interest of \$304,000). The total cost per bed is approximately \$40,500. The Owner has represented that the relatively low cost would have been higher if the Owner were not receiving all annual net cash flow profits of the Project during the first 39 years of operations under the terms of the operating lease (see "Financing Structure" below).

(See estimated Sources and Uses of funds.)

Financing Structure:

FPU has chosen to utilize a public-private partnership ("P3") to construct, finance, operate and maintain the Project. The primary benefit of a P3 is the transfer much of the risk for construction, operation, and demand to the Owner. There is no specific statutory framework authorizing universities to use public-private partnerships to finance university facilities, but the Board of Governors has begun developing P3 guidelines under which to evaluate P3 projects to finance university facilities. FPU is seeking permission from the Board of Governors to use the authority provided in s. 1013.171, Fla. Stat., which authorizes university boards of trustees to enter into lease agreements with private entities for the purpose of constructing a facility that meets the needs and purposes of the university, to enter into the necessary lease arrangements for the property. FPU has represented that it is utilizing a P3 because a university-owned financing structure was not a viable and cost-effective option for the Project due to the credit challenges resulting from a lack of demonstrated enrollment trends, demand for housing, and lack of accreditation (which is expected to be received in 2016).

The Project will be initially financed using an interim bank loan in the amount of \$13,200,000 and an equity investment of \$8,800,000 by the Owner. The interim loan is anticipated to be for a period of 6 years, the first year of which is during the construction period, or until FPU admission and occupancy rates have stabilized and accreditation has been achieved. At that time, the Owner intends to obtain a 30-year bank loan to refinance both the interim loan and the \$8,800,000 of equity funding provided by the Owner, at which point the Owner will not have any equity at risk. The financing will not be tax exempt.

The Owner will be the borrower and obligor for the loan payments. FPU has no legal liability for the Project or repayment of the debt. The Project has a 36-year financing structure, with ascending debt service

for the first five years of operation during the interim financing when there is little or no amortization. After 6 years, the Owner intends to obtain a long-term bank loan with a level debt payment structure; however, it is possible that this option will not be available to the Owner at that time. Interest rate risk, while solely the responsibility of the Owner, has not been hedged and could represent a significant risk to the long-term success of the Project.

FPU and the Owner will enter into a 40-year ground lease and operating agreement, which may be extended upon mutual agreement of FPU and the Owner. All net revenues of the Project after payment of expenses, required deposits to the Repair and Replacement Fund, and payments on the debt, will be retained by the Owner as profit. The total cash-flow profits to the Owner over the 40-year lease term are projected to be \$59.4 million or \$18.8 million on a present value basis, based upon assumptions of occupancy, rental rates, interest rates, and operating expenses.

This financing structure differs from a traditional University-owned and financed facility where the University retains all annual net cash flows after repayment of the associated debt. The annual net cash flows could be used by the University to maintain system facilities, offset future rate increases, or as a down-payment towards future system capital projects. The University has represented that it forwent the right to receive any future net cash flows of the Project, unlike Phase I where the University receives 10%, in an effort to keep the rental rates to students as low as possible.

Under the lease, FPU retains an option to purchase the Project based on a set lease termination value schedule. For the first year of operation, the \$22 million facility may be purchased for \$26 million, increasing slightly each year to a maximum price of \$28 million in year 5, and then declining thereafter throughout the term of the lease. At the end of the lease term, FPU will own the Project.

The Board of Governors' Debt Guidelines recommend, as a general guideline, maturities of no more than 30 years and debt service payments which, as nearly as practicable, are the same each year. Total financing costs under a 36-year repayment period with ascending debt service in the first five years are an estimated \$4,500,000 more over the life of the loan than under a 30-year, level debt service structure. The Owner has represented that financing over 36 years is necessary to keep rental rates low and obtain an adequate return on its investment.

Security/Lien Structure: The repayment of the construction loans will be an obligation of the Owner secured by net Project revenues and will be paid prior to any equity investment return or other cash flow profit to the Owner. There is no other debt outstanding with a lien on the Project. The debt associated with the Project will have no lien on any revenues or resources of FPU.

Quantitative Demand for Project:

There is currently one on-campus student housing facility with a capacity of 241 beds ("Phase I"). The Phase I facility opened in Fall 2014 and was also constructed, financed, and operated using a P3 arrangement with the Owner. The initial design capacity for Phase I was 219 beds; however, in an effort to respond to additional demand from students, the Owner increased capacity by 22 beds by converting some single occupancy rooms to double occupancy.

The University has represented that they have a need for additional on-campus housing beginning Fall 2015 resulting from the projected doubling of enrollment as the University enrolls its second class of students. Since additional on-campus housing could not be built in time to meet that demand, the University issued an ITN to identify existing rental units in the surrounding community that could be leased by the University for at least one year until the Project is completed. As of March 5, 2015, the University has narrowed its review to responses received from one apartment complex and a Quality Inn hotel.

Projected total on-campus housing capacity for Fall 2016, when the proposed Project would open, is 784 beds, which represents 48% of the projected total undergraduate student enrollment at that time, or 66% of the projected freshmen and sophomore students.

In 2014, FPU commissioned B&D to conduct a student housing demand analysis. B&D used university enrollment projections, student surveys and its proprietary methodology to project demand. According to the study, B&D projects student demand for on-campus housing in Fall 2016, when the Project is scheduled to open, will be 915 beds, which exceeds projected capacity of 784. FPU has an enrollment goal of 1,224 FTE by Fall 2016 built into its enabling legislation. The projections indicate FPU is on track to exceed that goal with projected enrollment of 1,715 in 2016-17, and FPU believes availability of student housing is integral to attracting and retaining students. The majority of the students surveyed said that

convenience, the ability to be engaged in university life, and a lack of suitable options off-campus was the main reason for the decision to live on campus.

(See attached Student Housing Demand Analysis prepared by B&D)

The study by B&D found that the rental market in the surrounding area is “immature” and does not offer many options within a 10-minute drive of campus given the comparatively rural nature of the area. While there are private off-campus housing alternatives currently meeting demand and FPU provides some shuttle services from certain off-campus facilities, there are indicators that as enrollment increases, the student demand for housing will exceed what is provided by the rental market. For example, a student survey was conducted in October 2014 of students in the Phase I residence hall to determine the interest level in on-campus housing for the next year. 241 residents, or 74% responded to the survey. 145 of the residents said they would like to stay in their current room next year. Other students indicated a desire to stay in the on-campus housing but desired to switch roommates or room, etc. Also, in addition to receiving approximately 20 applications a week, FPU has received over 200 completed housing applications from incoming freshman who would like to live in the residence hall.

To provide a level of commitment to the developers of Phase I, FPU adopted an on-campus residency requirement in 2014. The policy, with some exceptions, requires all full-time undergraduate students entering the University with less than 30 college credits to reside in an on-campus housing facility for the first two semesters of enrollment, subject to space availability. FPU has stated they did not have to enforce the residency requirement in Fall 2014 since demand exceeded the number of on-campus rooms available.

In the event that all available beds are not rented by students, the lease permits full-time faculty and visiting faculty to rent the unfilled beds. In addition, FPU may provide additional project support by filling unrented beds with groups participating in activities sponsored by FPU. However, the Owner represents the Project breaks even if 68% occupancy is maintained.

Project Rental Rates:

Based on the survey of data, B&D estimates that the rental rates for the Project will average \$5,791 per bed per academic year for the first year of operation, or \$643 per month (for 9 months), compared to an average annual cost for off-campus housing of \$7,476 per bed, or

\$623 per month (for 12 months). Initial rental rates have been set by the Owner and the University and will be reviewed annually as part of its Project budget by the Advisory Management Committee comprised of one representative from FPU, a representative of the Owner and a third representative from the Management Company. The Advisory Management Committee will only render non-binding advice to the Owner, but the Owner and FPU must agree on the annual budget, and disagreement will be resolved through a dispute resolution process involving mediation or binding arbitration. Annual rental rate increases that exceed 2.5% require approval of the University Board of Trustees, pursuant to the terms of the ground lease, but there is no hard limit on rental rate increases to students. The Owner built in projected annual rate increases of 2.25% to generate the cash flow profits it needs, resulting in a total rental rate increase to students of 12% after 5 years when the higher debt associated with the long-term bank loan are projected to start. If rates continue to grow by 2.25% per year over the lease term, rental rates will double in 32 years and will increase by 213% by the time the bank loans are paid off after 35 years of operations. Deferring the debt over 36 years with little to no amortization at the beginning of the term will drive rental rates higher for future students to generate sufficient amounts to cover debt service and profit for the Owner.

**Study of Private Sector
Alternatives:**

FPU is located in a sparsely-developed area, adjacent to 2,479 acres of undeveloped land owned by the private developer that donated the 171-acre campus. The existing private apartments nearby range from 6 to 19 miles from the FPU campus. The University has spoken with representatives of the adjacent landowner and also to developers who are planning to build apartment complexes within a few miles of campus. Based on those conversations, it is the University's understanding that there is a desire to build apartment units but the timing of such projects is uncertain. It is the University's belief that such future developments will not be completed soon enough to address the University's need for housing by Fall 2016.

**Pledged Revenues and
Debt Service Coverage:**

Projected net revenues of the Project for the first 5 years of operation and for the duration of the interim financing are expected to grow from \$1,721,316 in 2016-17 with debt service coverage of 4.48x to \$1,889,392 in 2020-21 with debt service coverage of 2.18x. After the

interim financing and equity investment are refinanced into a long-term permanent bank loan, projected to occur in 2021-22, the Owner expects annual loan payments to increase from approximately \$867,000 to \$1.5 million. Based on the increased debt costs and projected net revenues of \$1,933,976 in 2021-22, debt service coverage would be reduced to 1.28x at that time. The projected net revenues are based upon annual rental rate increases of 2.25%, estimated occupancy of 95% during the Fall and Spring semesters, and 10% during the Summer semesters, and 2% annual increases in operating expenses.

The debt will be repaid 36 years after funding the Project, which exceeds the limits imposed by the Debt Guidelines by 6 years. If the debt were issued on a 30-year basis using level debt service and the same interest rate (6%) assumed for the long-term bank loan portion of the proposed financing, projected debt service coverage during the first five years of operations would fall below the 1.20x coverage required by the Debt Guidelines, ranging from 1.08x in Fiscal Year 2016-17 to 1.18x in Fiscal Year 2020-21. Coverage noted for 30-year debt already takes into account annual rental rate increases of 2.25%.

(See Historical and Projected Debt Service Coverage, and estimated net cash flow profits to Owner)

Taxable Debt:

This Project will be financed by the Owner, a for-profit entity, with a combination of equity contribution and taxable bank debt. Only governmental entities such as universities and their direct support organizations or not-for-profit 501(c)(3) organizations may use tax exempt financing. To use tax exempt financing, the university would have to enter into a ground lease with a 501(c)(3) organization and finance the Project with all debt financing, which is not the financing model chosen by the Owner.

University Support of Project:

The debt will not be a legal obligation of FPU or any of its Direct Support Organizations, and FPU has not pledged its credit toward the Project. In addition to providing the land for the ground lease free of charge to the Owner, FPU is responsible for providing an addition to its existing chilled water system for the Project at an approximate cost of \$500,000, half of which will be reimbursed by the Owner. FPU will expand its parking system to accommodate the student housing facility at a total cost that has yet to be determined.

The Owner is contributing \$1,240,000 toward the parking expansion, which covers the cost of parking spaces for 57% of the beds in the Project.

FPU will provide information on its website to students regarding the housing available through the Project. FPU has also agreed to take the Project and its occupancy into account in planning any future student housing projects and to treat the Project at all times as a part of FPU's student housing program on an equal basis. In addition, FPU will provide security to the Project and data and phone services at a set cost. Chilled water and potable water will be provided by FPU and billed monthly to the Owner.

FPU is not legally obligated to pay debt service or maintain the Project. However, given the location of the Project on the FPU campus and the strategic importance of student housing, FPU may feel obligated to take over the Project or provide some other form of project support.

Return on Investment:

Based on projections provided by FPU, the Owner expects to receive annual cash flow profits from the Project totaling \$59.4 million over the 39-years of operations during the lease term, which equates to an IRR of 18% based on its \$8.8 million initial equity investment during the interim financing period. The cash flow profits to the Owner and IRR are based on assumptions of occupancy (95% during Fall and Spring semesters and 10% during summer), rental rate increase of 2.25% per year, and 2% increases in operating expenses per year and a refinance in year 6 that returns the equity principal to the Owner's equity. Actual profits to the Owner will be more or less than projected based upon actual operating results, but there is no limit on the amount of profit the Owner may receive from the Project.

In addition to the annual operating cash flow profits from the Project, the Owner will receive a management fee equal to 4% of rental revenues received, retaining 1%, which is estimated to be \$1.7 million over the term of the lease, and paying 3% to the Manager. It also anticipates receiving an upfront \$600,000 developer fee from the Project. The estimated total cash flow to the Owner from both Project net revenues and the 1% management fee average \$1.1 million during the first five years of operations during the interim financing and then range from \$450,000 to \$4.3 million throughout the remainder of the lease term. The IRR to the Owner increases to

approximately 20% when including the 1% management fee and upfront developer fees.

**Analysis and
Conclusion:**

Staff of the Board of Governors and the Division of Bond Finance has reviewed the information provided by Florida Polytechnic University with respect to the request for Board of Governors approval for the Project. The demand for the Project appears to be adequate given the results of the studies performed by B&D, enrollment expectations, and the immature nature of the off-campus housing market. Insufficient demand could result in the Owner's inability to operate and maintain the Project. Should the Owner be unable to operate the Project or pay debt service, FPU may feel obligated to pay these expenses due to the Project's location on the main campus and the strategic importance of student housing to the FPU. In addition, although projections provided by FPU indicate that sufficient revenues will be generated to pay debt service on the debt, the projections are predicated on 36-year debt with ascending payments for the first six years, which is inconsistent with the Debt Guidelines. The University has limited ability to control rental rate increases, projections provide a return on investment of 18% to the Owner, and there is no hard limit on the amount the Owner can earn from Project.