STATE UNIVERSITY SYSTEM OF FLORIDA
BOARD OF GOVERNORS
November 5, 2015

SUBJECT: A Resolution of the Board of Governors Approving the University of South Florida entering into a Ground Sub-Lease and a Management Agreement with HSRE-Capstone Tampa, LLC for the demolition of existing student housing and adjacent buildings and the construction, financing, and maintenance of a new student village complex comprised of housing, parking and dining facilities, a fitness center and pool, and retail space (the "Project").

PROPOSED BOARD ACTION

Adoption of a resolution approving the ***University of South Florida ("USF" or "University") entering into a 51-year Ground Sub-Lease with HSRE-Capstone Tampa, LLC (the "Owner") to construct, finance, and maintain the Project.*** If approved, ***the Owner will engage USF for the operation and custodial maintenance of the housing facility under a 51-year Management Agreement*** that overlaps the term of the ground lease.

Staff of the Board of Governors, State University System of Florida, and the Division of Bond Finance, State Board of Administration of Florida, has reviewed this resolution and all supporting documentation for compliance with Florida law and both the Board of Governor's Debt Management Guidelines, as well as the P3 Guidelines. USF is seeking permission from the Board of Governors to use the authority provided in s. 1013.171, which authorizes university boards of trustees to enter into lease agreements with private entities for the purpose of constructing a facility and enter into the necessary lease and lease arrangements for the proposed Project.

The proposed Project appears to be in compliance with applicable Florida law but as proposed, is not in compliance with the P3 Guidelines in several respects. However, the BOG should consider the following information in determining whether to approve the Project as proposed:

- ***The term of the Ground Sub-Lease is 51 years, 11 years longer than the 40-year term recommended in the P3 Guidelines.*** USF's justification for the longer term is the Owner's ability to set initial rates lower than under a 30 or 40-year agreement.
- The Project is financed with debt and equity. ***The 35-year repayment term of the equity and deferral of cumulative preferred equity distributions to year 11 of the agreement effectively violates the principles contained within the BOG Debt***

Guidelines and the P3 Guidelines as to deferring payments. ***Deferring payments*** extends the duration and increases the interest cost of the obligations.

- ***Taxable debt, the longer repayment period, and 7.0% interest rate on the cumulative preferred equity increases the total interest costs of the financing over traditional tax-exempt debt by an estimated $55 million.***
- ***The Project pro-forma shows the Owner receiving cash distributions of $410 million while USF is projected to receive $273 million***, of which $140 million (51%) is expected to be received in years 41 through 51 of the agreement.
- ***USF's purchase option is cost prohibitive*** with estimates indicating that after 15 years, the University could purchase the Project from the Owner for $431.5 million.
- ***Rental rates are 5% higher than existing housing rates*** even though the duration of the Ground Sub-Lease is longer than recommended by the P3 Guidelines.
- ***The financing includes costs associated with ancillary facilities*** (i.e. parking and dining facilities, a fitness center and pool, and retail space).

AUTHORITY FOR BOARD OF GOVERNORS ACTION

Article IX, Section 7, Florida Constitution; Section 1013.171, Florida Statutes

BACKGROUND INFORMATION

The University of South Florida Board of Trustees has reviewed a proposal and adopted a resolution authorizing the President to execute a Ground Sub-Lease and Management Agreement with HSRE-Capstone Tampa, LLC for the construction and operation of a student village complex comprised of a housing facility with 2,165 beds (1,039 replacement and 1,125 new), parking and dining facilities, a fitness center and pool, and retail space utilizing a public-private partnership arrangement. The Project will be approximately 578,000 gross square feet, be located on the University's main campus in Tampa and supports USF's belief that living on-campus is integral to student success.

The Project cost of approximately $133.0 million will be financed by the Owner, using a taxable loan and equity contribution which will be repaid with net housing revenues. USF is not legally obligated to pay debt service or maintain the Project. ***However, the rating agencies will consider the obligations associated with the proposed Project in evaluating USF's debt profile.*** The 35-year repayment term of the equity exceeds the limits imposed by the P3 Guidelines and Debt Guidelines by 5 years and defers the principal repayment of the equity until year 11 of the agreement. The equity is analyzed as subordinate debt because repayment is required under the terms of the Ground Sub-Lease and if Project cash flow is insufficient to make the required 7.0% preferred return on equity payment, the obligation is carried forward and paid in future years (i.e. the preferred return is cumulative).

USF asserts it would take eight years to deliver the Project using traditional procurement and financing methods as the existing housing system lacks sufficient debt capacity to finance the Project as proposed. However, in reaching this conclusion, ***the University did not consider a phased approach to replacing and financing student housing.*** Brailsford & Dunlavey estimates traditional procurement and delivery would cost approximately $15 million to $25 million more than the P3 model. However, these estimates are not supported by any analysis and have not been validated. Although development costs are estimated to be more than the P3 model, ***this P3 arrangement requires the University to share 60% of any excess cash flow after payment of operations, debt service and the preferred equity return with the Owner (about $410 million) while USF receives 40% (about $273 million)*** until the Owner achieves an internal rate of return ("IRR") of 11.50%. Over the term of the agreement, the Project's pro-forma indicates the Owner will not achieve its 11.50% IRR hurdle.

Supporting Documentation Included:	Information located in the Finance Committee materials