

9. Disposition of Real Property by Lease - WCUJonathan Womer

Situation: Western Carolina University has requested approval to lease its Millennial Campus to its Endowment Fund for 65 years in order to speed development of the property. The Endowment Fund anticipates entering into individual subleases to develop the property. Once the property is leased to the Endowment Fund, the fund would have the ability to enter into subleases without further statutory, policy, or regulatory approval.

Background: Western Carolina University purchased 344 acres southwest of campus in 2004 with about 90 acres developable. In 2006 the Board of Governors approved the Millennial Campus designation of the property. Millennial Campus development is intended to facilitate activities that enhance regional economic development beyond WCU’s traditional educational mission. Given its location and the nature of the development opportunities available, WCU has determined that it requires the ability to move quickly whenever new development partners are identified, particularly with respect to opportunities that involve significant construction projects. The ground lease would be executed in accordance with the existing statutory authority for disposition of property by lease at Millennial Campuses. The Endowment Fund would be able to enter into subleases without first seeking approval from the Office of State Property, UNC General Administration, Board of Governors, Council of State, or the Governor, absent additional requirements from the Board.

Assessment: The proposed ground lease has the effect of delegating certain approval authority of the Board of Governors to the WCU Endowment Fund for 65 years, at greater independence from oversight than delegated campuses. Accordingly, the Board’s approval should be conditioned on including terms in the Master Lease (between WCU and the Endowment Fund) that require the Endowment Fund to seek and receive approvals by the campus, the President and the Board of Governors for subleases. In addition, the Master Lease Agreement should include provisions to protect the interests of WCU and the University and provide WCU with additional expertise for property review.

Action: This item requires a vote.

Disposition of Real Property by Lease - WCU

Western Carolina University purchased 344 acres southwest of campus in 2004. The purchase price of the property was \$2,870,458; the 2000 Higher Education Improvement Bonds, specifically allocated for land acquisition, were used for the purchase. About 90 acres of the land is developable. In 2006, the Board of Governors approved the Millennial Campus designation of the property. Millennial Campus development is intended to facilitate activities that enhance regional economic development beyond WCU's traditional educational mission. To date, the only significant development has been the Health and Human Sciences Building that opened in 2013. It is 160,000 square feet and features telehealth facilities, laboratory spaces, offices, and meeting areas for the College of Health and Human Sciences and is directly owned by WCU. It also has a limited amount of clinic space available for use by private entities under separate space use agreements, in accordance with IRS regulations pertaining to the private use of bond financed facilities.

WCU anticipates a development trajectory characterized by relatively few and sporadic opportunities extending over a long period of time. Development of WCU's Millennial Campus presents certain challenges because: (i) WCU is a regional comprehensive university, with an emphasis on undergraduate research, not a high level research university; and (ii) WCU's Millennial Campus is located in a rural area, without the advantages attendant to being close to the Research Triangle Community or similar research parks, or the major industries and commercial activity of a large city. Consequently, as WCU pursues economic development opportunities and partnerships with private businesses, it is incumbent upon the university to be able to work with potential partners with agility and at the pace of their business activities. It is also vital to be able to offer the security of long-term sub-ground leases to business

partners so that they may realize the full financial benefit of their substantial contribution to the Millennial Campus infrastructure.

The Board of Governors possesses the authority, by statute, to approve the disposition of property by lease, up to 65 years, without the approval of the Governor and the Council of State. This authority is scheduled to sunset on June 30, 2015. WCU requests approval to enter into a 65-year ground lease whereby the State of North Carolina will lease the Millennial Campus property, excluding the Health and Human Sciences Building and the ground on which the building is situated, to the WCU Endowment Fund.¹ If the transaction is approved, WCU anticipates that the development of the Millennial Campus may involve the following:

- In the near future, the WCU Endowment Fund expects to enter into sub-ground lease(s) with private developer(s) to finance and construct buildings and other improvements on the Millennial Campus that align with programs and activities in the new Health and Human Sciences Building; and
- Over the long term the WCU Endowment Fund may enter into sub-ground lease(s) and other agreements with the WCU Research and Development Corporation, a tax-exempt organization described in Section 501(c)(3) of the IRC and a UNC associated entity, or its wholly-owned subsidiaries (tax-exempt LLC's) as part of joint ventures or other collaborations with third-parties, including for-profit entities.

The long-term ground lease will permit the WCU Endowment Fund to enter into sub-ground leases with developers as opportunities arise. Without this flexibility, WCU would have

¹ The Board of Trustees of the WCU Endowment Fund is comprised of the following members: the Chair of the WCU Board of Trustees (the "Board"); the Vice Chair of the Board, who is also the Chair of the Board's Finance and Audit Committee; the Secretary of the Board; the Chair of the Board's Academic Affairs and Personnel Committee; the Chair of the Board's Administration, Governance, and Trusteeship Committee; and the Chancellor.

to pursue individual ground leases with private developers in piecemeal and lengthy processes. The WCU Endowment Fund's long-term interest in the Millennial Campus property would permit the pursuit of private and joint development in the most expeditious manner and speed development.

Under current law, the Department of Administration's Office of State Property need not review the lease, subleases, or sub-subleases. However, the Office of State Construction will still be required to approve transactions that contemplate construction, to ensure the buildings meet code. The level of review will depend on the degree of State use (e.g. faculty offices) and the likelihood that the building will return to the State (instead of being torn down) after the ground lease expires.

The proposed ground lease, depending on its terms, would have the effect of leaving decisions concerning the leased property in the hands of the WCU Endowment Fund for 65 years at greater independence from Board of Governors oversight than delegated campuses.² WCU has not received delegated authority from the Board of Governors for lease transactions pursuant to UNC Policy 600.1.3.1. A delegated campus is required to have certain organizational or professional capacity for property matters. As such, WCU should be required to include certain terms in the ground lease to preserve the continuing interests of the Board of Governors in the overall development of the property. The recommended conditions and terms are listed below.

Recommended Board of Governors Approval Language

The Board should approve Western Carolina University's request to lease its Millennial Campus property of 344 acres, excluding the Health and Human Sciences Building and the

² The process of review for delegated campuses is outlined in Board policy 600.1.3.1 and in regulation 600.1.3.1 [R].

ground on which the building is situated, to the WCU endowment for 65 years under the following conditions:

- Subleases shall be treated as if the leases were undertaken directly by a delegated campus under regulation 600.1.3.1 [R] and will require the approval from the campus property committee, the Chancellor, the Board of Trustees, the President, and the Board of Governors as required by the thresholds in 600.1.3.1 [R] but shall not require State level approvals. Such terms shall be incorporated into the lease in detail, rather than simply by reference to the current regulation. The President or the Board of Governors may place conditions on the sub-subleases as determined by the review of the sublease.
- A financial feasibility and business plan from each proposed sublessee shall be submitted to UNC General Administration when the President or Board of Governors is required to approve the sublease or sub-sublease.
- WCU shall engage at its cost expert financial, property or other appropriate advice prior to completing the ground lease to the endowment by: (i) engaging qualified professional financial/property advisors through an agreement with the advisor(s), which is reviewed by UNC General Administration; or (ii) entering into a Memorandum of Understanding with a delegated campus and UNC General Administration. The agreement or MOU shall provide for review of all subleases and sub-subleases and provide feedback on the leases to UNC GA and WCU.
- With the assistance of its advisors, WCU shall develop and require the use of standard forms of sub-subleases for review and approval by the President, and once forms are approved no material term of any sub-sublease shall be modified, amended, deleted or abrogated, nor shall any material term be added to the forms. Failure to comply with this provision shall be deemed a default under the ground lease.
- Upon expiration of the ground lease term, ownership of any improvements constructed by or on behalf of the WCU Endowment Fund or its sublessees or sub-sublessees shall reside with the State.
- Rental for the term of the ground lease will be \$1.00.
- The property shall be developed and used in furtherance of WCU's teaching, research, and service mission as well as the economic development of the Western North Carolina region.
- The WCU Endowment Fund or its sublessees shall only enter into subleases or sub-subleases with unrelated third parties at or above fair market rental rate unless the process from 600.1.3.1 [R] is followed.
- The WCU Endowment Fund or its subleases, sub-sublessees or assigns may finance, construct, and operate improvements on the property that align with WCU's mission and strategic plan.
- The WCU Endowment Fund or its subleases, sub-sublessees or assigns may make annual payments to WCU for their proportionate costs for Millennial Campus common area maintenance.
- The WCU Endowment Fund or its sublessees, sub-sublessees or assigns may not encumber the State's fee simple interest in the property.

- The WCU Endowment Fund or its sublessees, sub-sublessees or assigns shall comply with applicable ordinances, regulations, and laws, including requirements pertaining to minority business participation.
- The ground lease shall terminate upon the happening of any of these events:
 - 1) Expiration of the term;
 - 2) WCU Endowment Fund default, defined as the failure to perform or comply with any material agreements, terms or covenants under the ground lease that have not been cured; or
- Subleases or sub-subleases will terminate upon default, defined as the failure to perform or comply with any material agreements, terms or covenants under the sub-lease or sub-sublease that have not been cured by the sublessee, sub-sublessee or, at its election, the WCU Endowment Fund or its permitted assigns.
- The WCU Endowment Fund shall require the inclusion of the following terms in subleases or sub-subleases:
 - 1) Subleases and sub-subleases shall be at all times subject and subordinate to the ground lease.
 - 2) Terms of the subleases or sub-subleases shall expire prior to or contemporaneously with the expiration of the ground lease.
 - 3) During the term of the ground lease, ownership of all improvements constructed by the WCU Endowment Fund or its sublessees or sub-sublessees shall be in the WCU Endowment Fund or its sublessees or sub-sublessees, as the case may be.
 - 4) Throughout the term of the ground lease, any liens, encumbrances, mortgages or claims of third parties, including construction lenders and permanent lenders, with respect to the property or improvements that may be deemed owned by the WCU Endowment Fund or its sublessees or sub-sublessees shall be expressly subordinate and subject to the rights of the State.
 - 5) Upon the expiration of the term of the ground lease, ownership of all improvements constructed on behalf of the WCU Endowment Fund or its sublessees or sub-sublessees shall reside with the State.
- The ground lease shall reference and be made contemporaneous with an operating agreement between the WCU Endowment Fund and WCU that sets forth additional understandings and obligations, including the following:
 - 1) WCU Endowment Fund's delegation to WCU of responsibility for the management of the Millennial Campus property, specifically including performance of the WCU Endowment Fund's various obligations and agreements under the ground lease and any subleases.
 - 2) The requirement that rental and other Millennial Campus operating revenues paid to the WCU Endowment Fund will be transferred to the WCU Millennial Campus Trust Account.
- Quarterly financial and accountability reports to WCU's Board and Chancellor concerning Millennial Campus development projects, which shall be provided to UNC General Administration and the President.