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TO: City of Milwaukie

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SUBJECT: DRAFT MILWAUKIE PRO FORMA GLOSSARY

This document provides a glossary of key terms found in the financial pro formas for the Moving Forward Milwaukie opportunity site development concepts. This document is organized according to the title of the tabs of the pro forma spreadsheets where these terms appear.

1. Operating Pro Forma

Potential Gross Revenue: The income that would be collected on the development assuming every square foot of leasable space was fully (100%) leased on an annualized basis.

Vacancy Loss: The Potential Gross Revenue that is not projected to be collected due to vacant space. Vacancy assumptions in our analysis are based on interviews with private developers, and generally begin at 25% in Year 1, and stabilize at 5% in Year 3.

Effective Gross Revenue: The Potential Gross Revenue minus Vacancy Loss.

Total Operating Expenses: This is the annual cost for the property owner to operate the property. These costs do not include debt service, which is shown in its own line items in each pro forma. Total Operating Expenses also does not include expenses paid by tenants (either outright or via "pass-throughs"). For triple-net tenants, Total Operating Expenses includes: management fees, marketing, landscaping, leasing and other miscellaneous expenses. For full-service tenants, Total Operating Expenses also include property taxes, utilities, insurance, and maintenance. Assumptions for Total Operating Expenses are shown on the "Pro Forma Assumptions" tab and are based on interviews with private developers.

Net Operating Income: Calculated as Effective Gross Revenue less Total Operating Expenses.

Debt Service: Amount owed—including principal and interest—to service traditional bank loans, construction loans and other types of development loans. Debt Service is calculated by the total project cost minus total equity, factoring in the loan term and interest rate.

EBITDA: "Earnings before interest, taxes, depreciation, and amortization." Calculated as Net Operating Income minus Debt Service.

Cash on Cash Return: Ratio of EBITDA to Total Equity. Also known as Return on Equity, Cash on Cash Return is a measure of annual return that excludes Debt Service.

Cash on Cost Return: Ratio of EBITDA to total project cost, including both equity and financing.

Cap Rate: Ratio between the Net Operating Income of the property and its assumed Resale Value. The cap rate is usually between 6.0% and 10.0%. A property's Resale Value can be estimated by dividing Net Operating Income by the assumed Cap Rate, which is dependent on the strength of the local economy among other factors. The Moving Forward Milwaukie pro formas show Resale Value at three different potential cap rates: 7.5%, 8.0%, and 8.5%. These cap rate assumptions were based on interviews with private developers.

Leveraged Internal Rate of Return (IRR): The expected investment return over a period of time (usually five or ten years). The Leveraged IRR represents the average rate of return on investors' equity over the term of the project from construction to sale. Leveraged IRR accounts for the time-value of money, cost of capital, and investment risk. Leveraged IRR is calculated using initial Total Equity, EBITDA (earnings before interest, taxes, depreciation, and amortization), and Resale Value (being the ratio of Net Operating Income in the resale year to an assumed Cap Rate) less the remaining principal balance of the project loan at sale. Leveraged IRR is commonly calculated using pre-tax cash flows because future tax liabilities may be unpredictable.

Unleveraged Internal Rate of Return (IRR): Unleveraged IRR is a measure of the expected investment return over a period of time, similar to leveraged IRR, with a few key differences in how it is calculated. Unleveraged IRR is calculated using the Total Project Cost (instead of Total Equity), Net Operating Income (instead of EBITDA), and total Resale Value (instead of Resale Value less the remaining principal balance of the project loan at sale).

2. Uses

Note that all assumptions for construction costs (except where otherwise noted) come from the range of cost estimates provided by the JE Dunn Construction Cost Matrix, with specific assumptions based on interviews with developers.

Site Acquisition: The price the developer pays to obtain the land.

Construction Costs: The Moving Forward Milwaukie pro formas show different line items for construction costs for the different uses within a building (e.g., residential, office, retail/commercial, etc.). Each use has a different construction cost per SF, based on the type of construction. Note that residential construction costs include the cost for interior finishes, whereas cost estimates for other uses assume shell buildings with no interior-buildout.

Type V Construction: Type V Construction is refers to a structure classification used by the National Fire Protection Association that measures fire risk for firefighting purposes. Structures are classified into five types—from I to V—based upon the combustibility of the construction materials. Type V accounts for wood framed construction and therefore represents the most combustible classification. Since Type V is most combustible, buildings that fall within this classification must be limited to at most four stories. Typical Type V uses are single-family residences, townhomes, and low-density apartments and condos.

Podium Construction: A type of construction whereby residential and commercial uses are raised—usually above street-level or above grade—on a platform using supporting columns, and are usually rested above structured or tuck-under parking.

Site Work: Work performed on the project at its physical location to prep the site for construction such as grading (leveling), demolition, tree clearing, and platting lot lines before the foundation is installed.

Building Skin: The exterior surface area of a building that will receive additional treatment to make it more aesthetically pleasing. Examples include stucco, curtain wall, window wall, etc.

Tenant Improvement (TI) Allowance: An estimate of the portion of costs paid by the property owner for tenant improvements to office or retail / commercial space. Typically, total TI costs exceed the TI allowance, and thus a portion of these costs are paid by the tenant as well.

Parking: Number of spaces for motor vehicles (referred to as "stalls"), which may be constructed as one of three types: structured, tuck-under, and surface. Structured parking refers to multi-story parking, and may be above or below grade. Structured parking is commonly mixed with commercial and residential uses. Tuck-under parking is generally found at street-level underneath podium construction that supports a platform that other uses rest upon. Surface parking is at grade, usually an asphalt surface with no other mixed-uses.

Frontage Improvements / Public Area Requirements (PARs): The frontage is the length of the site that is directly adjacent to the road it faces. Frontage Improvements are commonly stipulated in development contracts and hold the project accountable for elements such as curbs, sidewalks, and landscaping. Public Area Requirements also stipulate certain design elements for public areas—such as roadways, parking lots, and sidewalks—directly adjacent to the development within the downtown zones. Source: Cost estimates for frontage improvements / PARs were provided by City staff.

Hard Cost Contingency: An assumed hard cost that accounts for possible construction cost overruns due to project delays, and other unforeseen obstacles. The Moving Forward Milwaukie pro formas assume a Hard Cost Contingency of 7.5% of all other hard costs, except Site Acquisition.

Architecture and Engineering: The chief component of soft costs is design work known as architecture and engineering.

General Soft Costs: Development costs not directly associated with construction. In our pro forma, this category accounts for legal fees, and other consultants (for example soil and water testing, transportation analysis, etc.)

Financing Fees: Bank and lender fees associated with the origination of the construction loan and other development loans.

City Fees & Permits: Includes building permits, planning and building department staff time, land use applications and review, and other fees associated with the due diligence required for approval or denial of a project. Source: City Fee and Permit cost estimates provided by City staff.

FF&E: Furniture, Fixtures, and Equipment. Accounts for the non-permanent items that will be associated with the project. In the development phase, FF&E costs are generally associated with the common areas and can include chairs, desks, light fixtures, and electrical equipment.

Systems Development Charges (SDCs): Costs the developer pays to the City and other local governments in order to mitigate increased demand for infrastructure generated by the project including transportation, parks, water, waste water, and storm water. These are separate from City Fees and Permits. Source: SDC cost estimates were provided by City staff.

Soft Cost Contingency: An assumption that accounts for possible cost overruns due to project delays, and other unforeseen obstacles. The Moving Forward Milwaukie pro formas assume a Soft Cost Contingency of 7.5% of all other soft costs.

3. Sources

Equity: The amount of capital a developer contributes to the project before loans and other financing mechanisms. Equity is also funds contributed by other investors, such as EB-5 investors.

EB-5: EB-5 is a visa program specifically for immigrants to invest within the United States. It is an incentive program meant to create economic and employment opportunities in exchange for a path to permanent residency. Program participants must invest at least $1.0 million—or $0.5 million if it's in a designated high unemployment or rural area—and demonstrate the creation and preservation of 10 jobs for US workers. Investment in development projects, which can be managed by a third party and approved by the United State Citizenship and Immigration Services, is one method immigrant investors can become eligible for the EB-5 program benefits.

Loan to Value Ratio: Total Equity divided by Total Financing. It is a measure of the value of funds being personally invested by the developer and project investors versus the total value of the bank loan servicing the project.

Debt: Total Financing is the total project cost minus Total Equity; the amount of money that has been borrowed to finance the construction and operations phases of the project.

Debt Service Coverage Ratio: The ratio of Net Operating Income to annual payments owed on the project Debt (known as Debt Service).

Refinance: Replacement of an existing loan obligation with a new loan under a different set of terms: usually at a lower interest rate and/or different payoff period.

4. Other key terms

Triple Net (NNN): NNN denotes a lease that stipulates the lessee (the tenant) must pay insurance, property taxes, and maintenance and utilities associated with the leased space, in addition to the agreed upon base lease amount. The NNN portion of the lease generally varies from month to month; the base lease amount does not. A NNN Lease is generally associated with retail/commercial properties.

Full Service: A full service lease stipulates that the lessor (the landlord) must pay for all costs associated with building operations, including maintenance and upkeep, utilities, insurance, and property taxes. The lessee is only responsible for the agreed-upon base lease amount. A Full Service Lease is generally associated with office and residential rental properties.