

\$147M Lease Fuels Build, Shows Lending Shift

By Bob Howard



Project Rendering

SANTA MONICA, CA-UCLA has signed a \$147 million lease for a 50,000-square-foot medical facility here that is being built with a \$28.5 million construction loan that is a sure sign of a distinct shift in the capital markets over the past year, according to the George Smith Partners team that arranged the financing. SVP Steve Orchard of Century City-based GSP tells GlobeSt.com that developer Randall Miller, who is building a three-story outpatient surgery facility that is 100% leased to UCLA, had five solid offers to choose from prospective lenders on his construction loan, three of them offering a firm commitment on take-out financing. The UCLA lease is for 30 years, according to principal Gary Weiss of Madison Partners, which represented the developer.

The five construction loan offers that Miller received stand in sharp contrast to the reception that GSP got when it first took the loan to market a year ago, in February 2009: The loan got hardly a nibble from lenders.

Orchard tells GlobeSt.com that conventional lenders were so cool to the deal then that GSP decided that the best route would be bond financing. The Century City-based firm hired a bond consultant and began a months-long "lengthy and involved process" to not only define what the bond markets would require for the financing but also to renegotiate lease terms with UCLA to meet some of the conditions required by the bond financing.

In July, the GSP team was getting close to an agreement on the bond placement—except for one or two key issues—but those were sticking points for UCLA, which was going to want some concessions on the lease if the university agreed to those points. "Right about that time, we began to see a mild shift in the more traditional side of the lending market, so we put the bond financing on hold," Orchard says.

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GSP then took the deal back to the traditional market, where "90% of the people still said no," Orchard tells GlobeSt.com. But 10 different lenders showed serious interest, and five of them ultimately "came out with strong offers," the GSP senior vice president says.

The five qualified offers included two from banks that offered construction loans, one from a pension fund that offered a construction-to-permanent loan, one from a life insurance company that offered a construction-to-

permanent and one from a pension fund adviser—syndicating two union pension funds—that offered a forward permanent.

Ultimately, there were two competing quotes, one from US Bank and one from a pension fund offering a construction-to-perm loan, Orchard says. The offers also included personal guarantee requirements that were more reasonable than those that lenders wanted a year ago when, Orchard says, "The types of guarantees that the lenders wanted for traditional construction financing were Draconian."

The developer chose the offer from US Bank, a subsidiary of Minneapolis-based US Bancorp, which is underwriting the entire loan with no syndication. The loan starts at a 5.25% interest rate, floating over Libor, with a 5.25% floor.

Underwriting is still conservative, Orchard says, and lenders are still requiring considerably more equity from borrowers. He points out that, before the downturn, the project would have likely had offers approaching 100% of cost with cash-out to the sponsor at closing based on re-entitled land value.

The US Bank loan does not include a commitment for take-out financing, but the developer chose it instead of a loan with pre-committed take-out financing because he feels that he will be able to get better terms on permanent financing when the building is completed, according to Orchard. Construction of the new UCLA medical facility is expected to begin in the middle of this month, upon closing of the loan. The surgery center, which is scheduled to open in 2011 and is being designed for LEED Gold certification, is being developed at 1217-1233 16th St., across the street from the Santa Monica-UCLA Medical Center.

The borrower's qualifications, the 100% lease and the healthcare tenant were all keys to making the deal work, Orchard points out. Quality cash flow is critically important in securing financing today, he says, with lenders "emphasizing sectors that are considered more predictable, such as multifamily, investment grade credit leases and need-based services such as healthcare and grocery-anchored retail." In addition to Orchard, the George Smith Partners team included Jay J. Brooks, Gary E. Mozer and Josh Roseman.

Weiss of Madison Partners points out that Miller acquired the land two years ago and that the UCLA lease was first negotiated a year ago, contingent upon the completion of the entitlements and building design. Miller is principal of Nautilus Group Inc., and the development partnership/owner of the project is Sixteenth Street Medical Center LP.

Brad Erickson, UCLA's director of Campus Services Enterprises, assisted in-house with the negotiations, and attorney Brian Kang of the Los Angeles law firm Greenberg Glusker also was instrumental in the negotiations. The project is being designed by the Santa Monica firm of Michael W. Folanis, Architects.