SB 159 cont/..

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COMMENTS AND SUGGESTIONS OF THE
ALASKA INDUSTRIAL SUBDIVISION LEASEHOLDERS
ON SB 159

By virtue of the fact that the leaseholders of state lands within the Anchorage area designated as the Alaska Industrial Subdivision have a great deal, if not everything, to lose if remedial legislation is not forth coming which would (in some manner) alleviate the untenable situation they presently face, it would seem only befitting that they offer their comments on SB 159 which was introduced in the Legislacure on February 15, 1977.

Prior to undertaking a section-by-section analysis or critique of SB 159, the state leaseholders think it may be beneficial to submit a brief outline of the pertinent facts which surround this controversy. Specifically, the purpose of this background material is twofold: first, to familiarize the reader with the dramatic changes which have occurred recently in state land leasing policy and to emphasize how those harsh changes now threaten the economic survival of the state leaseholders in Alaska; second, such facts establish and support the leaseholders' contentions brought out later in the discussion of SB 159.

1. In 1958 the territorial government of Alaska made the policy determination that an area of government-owned land located east of and nearly inaccesible to Anchorage be leased for commercial and industrial purposes. This area of Anchorage was then leased to the highest bidder at public auction for a term of 55 years. The area in question was designated the Alaska Industrial Subdivision, and during subsequent years other lands in it were leased under terms comprable to those written into the initial leases. One of the basic provisions of these leases, and the one bringing this controversy into existence, was codified

into state law in 1959 (§7, art. V, Ch. 169, SLA 1959). This statute (AS 38.05.105) reads in part:

> Each lease shall stipulate that the annual rental payment is subject to adjustment at five-year intervals and charges or adjustments shall be based primarily on a reappraised rental value . . .

2. Upon statehood, the Department of Natural Resources, Division of Lands for the State of Alaska, officially reaffirmed the prior land lease policy mentioned in number 1 above, in adopting its administrative regulations on July 1, 1960. The regulation which set fort' the intent behind adopting the "Surface Leasing Regulations" read in part:

> . . . The intent of this chapter is to insure the equitable leasing of Alaska land <u>in a manner that will encourage development for its highest and best use</u>. (Emphasis added)(11 AAC 58.900)

This regulation and its intent still remain on the books, and the state has never changed or attempted to change the highest and best use classification of the Alaska Industrial Subdivision from its original designation as commercial industrial lands.

3. During the period of 1958 through the spring of 1976 the leaseholders in the Alaska Industrial Subdivision developed their lands and established business enterprises at a considerable expense in both money (substantial portions being borrowed) and time. The state Division of Lands during this same period had followed rather consistent and tolerable annual rental readjustment practices under the authority of AS 38.05.105. Annual rentals were adjusted upward from 40% to 100% during this period without undue protest from the leaseholders.

4. In the spring of 1976 numerous leaseholders holding state leases in the Alaska Industrial Subdivision were given notice that their leases were to be reappraised and five-year annual rental readjustments made. Such notice caused no particular concern among the leaseholders because of past state policy.

5. In May and June of 1976 the state Division of Lands advised the leaseholders whose lease rentals had come up for readjustment that their new annual rental payments had increased anywhere from 700% to 800%, and in some cases even more. To say the least, this came as an overwhelming shock to the leaseholders and they immediately registered protests with the Division of Lands. These same protests for an independent appraisal or some form of compromise, however, fell upon deaf ears with the Division of Lands, and the leaseholders in the Alaska Industrial Subdivision were thereby faced with exceedingly harsh possibilities of (a) abandoning all the work, time and money they had devoted to the economic endeavors and have their leases forfeited to the state; (b) trying to salvage what they could from their ongoing businesses and attempt, at great personal and monetary sacrifice, to re-establish their business interests on fee simple land in other parts of Anchorage; or (c) try and have the impossible situation remedied in a fair and equitable manner through the proper judicial and legislative channels. The leaseholders in this case chose the latter option as the only one realistically open to them.

6. The leaseholders of the Alaska Industrial Subdivision demanded and were afforded an administrative hearing (held the 14th, 15th, 20th and 21st of December 1976) before a hearing panel consisting of George Hollett from the state Division of Lands; Kenneth Zamzou, an appraiser with the state Division of Petroleum Revenue; and Timothy G. Middleton, an attorney in private practice in Anchorage. During the four days of administrative hearings tremendous amounts of testimony and other evidence were elicited from both the state and the leaseholders. The Hearing Panel's Proposed Decision and Recommendations in this matter are attached hereto and marked as Attachment "A". While there is no need here to summarize this decision or the recommen-

dation, special attention is directed to the Summary and Findings of Facts (p. 15), Conclusions of Law (p. 17), and Recommendations (p. 18) found therein.

7. By virtue of the fact that the Hearing Panel's decision submitted January 20, 1977 so strongly supported the leaseholders' position, and because of their own personal feelings of indignation, the leaseholders have now decided to bring their case before the members of the First Session of the Tenth Alaska Legislature.

CRITIQUE OF SB 159

While the leaseholders of state land in the Alaska Industrial Subdivision believe the basic format of SB 159 offers a good solid foundation upon which equitable relief could be structured, it contains, in its present form, a number of serious deficiencies which must be changed or altered if the impossible situation being faced by state leaseholders is to be resolved with any degree of certainty.

The specific points of contention and the resolution of them can be basically set forth as follows:

1. *Section 1 of SB 159 provides in AS 38.05.085(a)(1) [p. 1, line 12] that the parties shall agree on a fixed base annual rental to run for an initial ten-year period. While the leaseholders realize and appreciate that this new lease period is double the existing length, it nevertheless completely fails the test of economic reality. What is meant by this is that with a short initial period of ten years before the state can readjust the fixed base annual rental, the financial institutions of this and other states will not loan money to leaseholders to develop and improve their leased property. During the administrative hearing held on this matter the testimony of John Kemper, an Anchorage banker, and Andrew Hoge, an Anchorage attorney having done considerable work in this field, brought out the fact that lending institutions require a high degree of certainty that the

borrower will be able to repay a loan under the terms of a ground lease. It was well established that, under normal economic circumstances, to expect a borrower to lease land, develop commercial establishments and be able to repay the borrowed money with interest within a period of ten years is totally unrealistic. In effect whet lenders require is that before loans can be made on unsubordinated ground leases the rental to be paid annually must be either a level term or a rent which is ascertainable for a period of ten to fifteen (or in some cases even more) years after the term of the loan. Because this is a rather complicated matter, a full and thoughtful discussion is left to pages 5 through 7 of the transcribed testimony of Andrew Hoge which is affixed hereto as Attachment "B". For further discussion on this point, also see pages 12 through 15 and 24 through 29 of the Hoge transcript. From this discussion, which reveals the generally accepted practices of the lenders in this state and elsewhere and the testimony of a practicing attorney who is well versed in the field of ground lease financing, it becomes apparent that a short ten-year initial fixed rental will prohibit the leaseholders from acquiring the financing necessary for developing and improving the leasehold property. In light of these circumstances, the leaseholders cannot see any other answer to their economic plight but to have their fixed base annual rental increased from ten years to at least 25 years during the initial period.

2. *Section 1 of SB 159 further provides in AS 38.05.085 (a)(1) [p. 1, line 15] that the initial fixed base annual rental may not exceed 8% of the fair market value of the property. To demonstrate that this percentage figure is much too high, one only has to consult the Hearing Panel's discussion of the appraisal techniques (see Rental Rate, pages 12 through 14 of Attachment "A") and its Findings No. 5, which states:

> The rental rate of 8% is excessive, considering the private lease market and the disadvantageous provisions in the State lease,

including: (a) no subordination of fee, (b) no rent ceilings, (c) unilateral adjustment with no arbitration, (d) floating easements, (e) lack of option to purchase. Specifically, the private leases examined contained one or more of the following advantageous conditions: (a) subordination, (b) an option to purchase, (c) rent ceilings, (d) arbitration; and none contained floating easements provisions.

3. Section 1 of SB 159 provides in AS 38.05.085(a)(2) and (3)[p. 1, lines 17-24] that once the initial lease period has expired, the annual rental is to be readjusted every five years thereafter, so long as the new rental does not exceed 8% of the fair market value of the property or 50% more than the amount paid the preceeding period, whichever is higher. These provisions represent a number of major points of contention and disagreement which the leaseholders have with SB 159.

First, the requirement that the annual rental payments be readjusted every five years after the short ten-year initial period has run only compounds many times over the critical problem which has been discussed in number 1 above with regard to obtaining any financing for developing or making improvements on the land. With a statutory provision requiring the rentals to be paid be readjusted eight times after the initial period gives the leaseholders and their potential lenders absolutely no way to estimate the intermediate or ultimate rental payments to be required. As already noted in number 1 above, the lending institutions making development or improvement loans would not do so where the potential rental liability is so uncertain and unascertainable.

Second, the requirement in this provision of SB 159 that the leaseholder pay a readjusted rental every five years after the initial ten-year period which is the higher of 8% of the reappraised fair market value of the property or no more than 50% of the rental he has paid the preceding period not only further contributes to the problem of making the state lease unbankable because the future rental payments cannot be ascertained with any degree of certainty, but it also penalizes the

state leaseholder over lessees of privately-owned land throughout the lease period to a point which is nearly beyond comprehension. Just how the state leaseholders would be so severely penalized under this "higher" of two limits or ceiling can be fully appreciated from the computations made in Attachment "C" which is attached hereto.

Third, the leaseholders further contend that the 8% figure used in this portion of SB 159 also is unrealistically high considering the unfavorable aspects of state leases in comparison to private commercial leases (see p. 16, Finding No. 5, Attachment "A").

4. Subsection (b) of AS 38.05.085 as proposed in Section 1 of SB 159 (p. 1, line 25 through p. 2, line 10) establishes what the leaseholders believe to be an excellent procedure for appraising state lease land in a fair and certain manner. Further, this provision corresponds with the Hearing Panel's Recommendation No. 4 (see p. 19 of Attachment "A"). The only difficulty the leaseholders have with this proposal is that, because of the frequency of appraisals needed under Section 1 of the bill, they think that the sharing of appraisal costs (p. 2, line 10) would be a highly expen ve proposition.

5. The leaseholders earnestly believe that a new section should be inserted between *Section 1 and *Sec. 2 of SB 159. This new section would repeal and reenact AS 38.05.090 and would read as follows:

> Sec. 38.05.090. REIMBURSEMENT FOR FIXTURES AND IMPROVEMENTS. (a) A lessee of state land shall be reimbursed by a succeeding lessee or purchaser for fixtures constructed and installed on the land and improvements made to the land. If the retiring lessee and the new lessee or purchaser do not agree on the fair market value of the fixtures or improvements, or both, then such value shall be determined as provided in (b) of this section.
>
> (b) When it is necessary to determine the fair market value of the property under

> the provisions of (a) of this section, the lessee shall appoint an M.A.I. appraiser and the new lessee or purchaser shall appoint an M.A.I. appraiser. The two appraisers so appointed shall, within a specified period of time agreed upon by the parties, make their appraisals of the property in question. If the two appraisers agree upon the fair market value then that determination is absolutely binding on the parties. In the event that the two appraisers are not able to agree, then they shall together appoint a third M.A.I. appraiser and he shall then make his appraisal of the property in question. When the third appraisal is completed, the two of the three appraisals which are nearest each other in their determination of the fair market value shall be averaged and the resulting sum shall be the fair market value of the the matter in question and absolutely binding on the parties. The cost incurred in making the appraisals provided for in this subsection shall be borne by the parties equally.

The reason that this repeal and reenactment of AS 38.05.090 is necessary is that much of the existing provisions of this section are antiquated and internally inconsistent. This present state of affairs subjects the leaseholders to a great deal of unnecessary uncertainty with regard to their rights (or lack thereof) for reimbursement for improvements made to the state land if they must give up their leases. The amendatory language would eliminate any such problems.

6. The only other modification which the leaseholders believe necessary in SB 159 relates to *Sec. 3 (p. 3, lines 16-20). By virtue of what the leaseholders have suggested in numbers 1 and 3 above, the provision should naturally be redrafted to change the initial lease period to 25 years and readjustments to be made at intervals of ten years or more.

In conclusion, it may be fairly stated that the leaseholders sincerely believe that, in order for them to economically survive in the Alaska Industrial Subdivision, the changes to SB 159 stated herein are essential and not merely wishful thinking.

BEFORE A HEARING PANEL OF
THE ALASKA DIVISION OF LANDS

In the Matter of Protests)
of Various Leaseholders in)
ALASKA INDUSTRIAL SUBDIVISION)

HEARING PANEL PROPOSED DECISION AND RECOMMENDATION

I

INTRODUCTION

Pursuant to a letter of November 2, 1976, written by Michael Smith, Director, Division of Lands, to lessees holding leases in the Alaska Industrial Subdivision, an administrative hearing was held December 14, 15, 20 and 21, 1976. The hearing was called to give the lessees an opportunity to protest the five-year reappraisal of certain state leases within the Alaska Industrial Subdivision, said reappraisal resulting in substantially higher annual rental payments. The hearing panel consisted of George Hollett from the Division of Lands; Kenneth Zamzow, an appraiser with the State Division of Petroleum Revenue; and Timothy G. Middleton, an attorney in private practice.

The Division of Lands (Division) was represented at the hearing by John Gissberg from the Attorney General's Office. Representing various leaseholders was Douglas Daily, and representing leaseholder Groh & Benkert, a partnership, was Clifford Groh.

Testifying as witnesses for the Division were Ronald Bunn, an appraiser with the Division; Robert Kesling, a forester with the Division; and Eugene Harp with the Department of Highways.

ATTACHMENT "A"

Testifying as witnesses for the lessees were Leon Brown, Jim Cristopher, Joe Wilhour, lessees; Fred Ferrara, and Erroll Simmons, appraisers; John Kamper, a banker; Andrew Hoge, an attorney; and Paul Kimball from Lynden Transport, a lessee.

The relevant provisions of the lease form, regulations and statute are set out as follows:

(1) State lease provision calling for reappraisal:

> "[S]uch payments to be subject to adjustment at each five-year interval from the effective date hereof, if the lease term hereof exceeds five years, such adjustment to be based primarily upon a reappraised annual rental value of land in a state of improvement similar to that of the land described herein at the time this lease was entered into.

(2) Regulations governing rental: 11 AAC 58.520 and 11 AAC 58.410:

> 11 AAC 58.520. ADJUSTMENT OF RENTAL. All leases shall stipulate that the annual rental payment shall be subject to adjustment by the director at five-year intervals and any changes or adjustments shall be based primarily upon the reappraised annual rental value. The director shall take into consideration the following factors in reappraising the annual rental value: the value of comparable lands in the same or similar areas, exclusive of buildings, structures, appurtenances, equipment, land fill, clearing, leveling or roads owned by the lessee. The commissioner may waive one or more of the periodic rental adjustments or lengthen the reappraisal period, when a lessee who has acquired a tract of land for multiple unit housing, commercial, or industrial development can demonstrate to the satisfaction of the commissioner that such action is essential in order to obtain the primary long-term financing or loan insurance required for development of the leased land. In order to qualify, applicants must furnish written evidence that, in requiring a waiver of rental adjustment, the lending or insuring agency is applying a generally applicable rule. Waivers shall remain in effect only during the term of the loan but shall not exceed 40 years.
>
> 11 AAC 58.410. ANNUAL RENTAL. Annual minimum rentals shall be computed from the approved appraised market value, except in the case of a preference right grazing lease, and shall be the lowest acceptable bid in the event of an auction. Annual rental shall be the basis of bidding for

all surface leases, except as provided in sec. 440 of this chapter. Annual rentals in amounts up to and including $250.00 shall be paid on an annual basis. Annual rentals in amounts above $250.00 shall be paid either annually or in quarterly installments, at the discretion of the lessee. All rentals shall be paid in advance.

11 AAC 58.900. SHORT TITLE. This chapter pertains to the leasing of land of the State of Alaska and to the jurisdiction of the Division of Lands, Department of Natural Resources and related matters. The intent of this chapter is to insure the equitable leasing of Alaska land in a manner that will encourage development for its highest and best use. This chapter may be referred to as the "Surface Leasing Regulations."

(3) Statutory provision dealing with rental adjustments in effect as of May 1, 1976:[1]

AS 38.05.105. PERIODIC RENTAL ADJUSTMENTS. Each lease shall stipulate that the annual rental payment is subject to adjustment at five-year intervals and charges or adjustments shall be based primarily on a reappraised annual rental value. However, when development of the land is not otherwise possible due to special conditions, the reappraisal period may be lengthened or waived under regulations adopted by the commissioner.

Because the hearing panel is composed of an appraiser, lawyer and a representative of the Division of Lands, it is considered appropriate in formulating recommendations to the Director that the panel exercise independent judgment based on expert testimony presented and exhibits offered. Accordingly, we do not accord the Division's position any special deference which might be applied in an administrative appeal in the judicial process.

The basic question to be resolved in this hearing is the determination of a fair rental for certain lots within the Alaska Industrial Subdivision. This fair rental is to be determined for the five-year period May 2, 1976, through May 1, 1981, the third rental adjustment period since the leases

[1] This section has since been amended, §1, Ch. 267 SLA 1976.

commenced on May 2, 1961. The Division had adjusted the annual rental of the leases in question as of May 1, 1976. This adjustment had been based on a reappraised fair market value and an increase in the rental rate from 6% to 8%. The reappraisal and adjustment were based on the relevant provision of the statute and regulations quoted above. Additionally, the term "fair market value" is defined in 11 AAC 58.910(11) as:

> "Fair market value" means the highest price, estimated in terms of money, which the property would bring if exposed for sale for a reasonable time in the open market, with a seller, willing but not forced to sell, and a buyer, willing but not forced to buy, both being fully informed of all the purposes for which the property is best adapted or could be used.

II

ISSUES

The issues appear to be the following:

(1) An interpretation of the lease, regulatory and statutory provisions, as to the nature of improvements to be included in the appraised value.

(2) Whether or not the term "primarily" as used in the lease, regulations and statute means that the Division should consider other factors in arriving at a reappraised annual rental value.

(3) Whether the Division's appraisal was in accord with the law and consistent with the relevant market conditions, particularly as to (a) use of comparables and (b) determination of original condition.

(4) Whether the 8% rental rate is appropriate in view of market conditions, the provisions of the state lease not found in private leases.

III

DISCUSSION

A. State of Improvements

The lessees represented at this hearing interpret the term "state of improvement" to mean the state of improvement of the entire Alaska Industrial Subdivision. Specifically, the lessees interpret this to mean that any improvements made outside of lot boundaries since 1961, such as roads and utilities, are to be excluded from consideration in the fair market value of the subject lots. The appraisals conducted by Messrs. Ferrara and Simmons for the lessees and presented at the hearing reflected adjustments in value to account for the cost of those improvements, particularly cost of access. This was based on language in the lease indicating value should be based on land in a similar state of improvement as land described in the lease at the time the lease was entered into; thus, the reference to "original condition." The regulations, however, are more explicit in determining what improvements are to be excluded. The Panel believes it would be inappropriate, in view of regulations and principles of equity, to exclude from the value of the leased property improvements off the property, especially when such improvements were paid for by the lessor. When a lessee can demonstrate that such off property improvement was paid for by him or his predecessor in interest, a different approach should be used. Both the State and the lessees agree that any improvements made within lot boundaries by lessees are to be disregarded in the valuation. The Panel finds in favor of the State in interpreting this phrase "state of improvement" to mean only the condition within the subject lots and that all improvements made since the leases were entered into which lie outside of the lot boundaries, specifically roads, water, sewer, power, and any other amenities

which affect the value of the subject lots are to be included in the fair market value of those lots.

A further disagreement among the parties involving the "state of improvement" is that of the original condition of the lots before any tenant improvements were made. The State's appraisal witness, Mr. Bunn, testified that as far as he could determine after reference to soil maps, aerial photos and consultation with various knowledgeable individuals, that the soils were basically adequate for building development with a minimum of site preparation required for any development, that no substantial amount of overburden needed to be removed. Mr. Bunn admitted his findings in this regard were based largely on the lack of evidence to the contrary. He did not, apparently, attempt to gather evidence from individuals who developed the leased land. Several other witnesses testified as to moderate to severe conditions of peat and unstable soil conditions at the time the leases were originally entered into. The lessees' appraisers, Mr. Simmons and Mr. Ferrara, after thoroughly investigating the original soil conditions with various knowledgeable people indicated that it was still not clear exactly what the soil conditions were on each parcel. There was adequate testimony given that most, if not all, of the subject lots had conditions of unstable peat soils in depths ranging from one to four feet, with testimony given concerning individual spots where the depth of peat extended 14 feet. In Mr. Ferrara's appraisal of Lot 4, Block 2; Lot 12, Block 10; Lot 10, Block 9; Alaska Industrial Subdivision, he stated that soil conditions probably varied from two to three feet of overburden along Commercial Drive on the north with overburden deepening in the area of Rampart Drive and reaching depths of two to three feet

again along Mt. View Drive. Mr. Ferrara testified that although he was uncertain as to the actual soil conditions at the time the leases were entered into, he felt a realistic condition was that approximately two feet of fill was required on the average for development of those lots which he estimated would cost, at the time of reappraisal, $.50 per square foot. Mr. Simmons' appraisal report and testimony regarding soil conditions were similar to those of Mr. Ferrara. In Mr. Simmons' appraisal of Lots 8 and 30, Block 10, he estimated a current cost of surcharging the peat with gravel in an amount adequate to support parking and storage yards was $40,000, which divided by total site area of 46,021 square feet equals $.87 per square foot. In the Panel's opinion, the investigation and analysis by the lessees' two appraisers were reasonably well supported and much more creditable than the investigation, analysis and testimony given by the Division.

B. Meaning of Primarily

The lessees contended that because the lease, regulation and statute all use the adverb "primarily" to modify the verb in, "such adjustment to be based primarily upon a reappraised annual rental value," that the State should consider other factors in arriving at an annual rental value. The lessees point to 11 AAC 58.900 wherein the intent of the regulations is spelled out, i.e., to "insure equitable leasing" to "encourage development." Accordingly, the lessees presented evidence, unrefuted by the Division, of the difficulty in obtaining financing for development of the leaseholds.

The Division's position was that the word meant nothing now with respect to the leases under question, but that it referred to the since repealed provisions for waiver

of five-year adjustments in cases where such a waiver is necessary to obtain long-term financing. The Division stressed the point that the lessees never attempted to obtain the waiver. The Panel finds the Division's argument to be without merit. First of all, the word "primarily" applies, if at all, to the reappraisal. The waiver would mean there would be no reappraisal at all. The suggestion that the lessees should have attempted to get the waiver is also without merit. The date of the reappraisal was May 1, 1976; the date the waiver repeal became effective was June 22, 1976. Assuming that the lessees had notice of the reappraisal simultaneously with the reappraisal, there would be only six weeks in which to get the waiver after reappraisal. The lessees indicated such actual notice of reappraisal came much later, in June and July; this was not rebutted. It is also unrealistic to believe that the State would have agreed to such a waiver.

The word "primarily", taken along with 11 AAC 58.900, is not without meaning. The Panel believes that the Division should consider other factors besides a determination of open market rent. The present state of the lease and regulations makes it difficult to arrive at a readily ascertainable meaning, especially in view of the duty owed to the people of Alaska by its government to obtain a good return from the State land. While principles of legislative interpretation dictate that the word be given meaning, the Panel finds it difficult to do so. Because nothing was presented to resolve this dilemma, the Panel refrains from attempting a definition beyond suggesting that doubts or ambiguities be resolved in favor of the lessee.

C. Appraisal.

11 AAC 58.410 states that annual minimum rentals shall be computed from the approved appraised market value. Rent paid for land in the open market place is typically determined by, and expressed as, a percentage of the market value of the land. Therefore, a reasonable estimate of the fair market value of the land in question must first be made before a market rent can be derived. The generally accepted method of appraising vacant land, and that which was used by all three appraisal witnesses, is the direct market comparison approach. All three of the appraisal witnesses utilized definitions in 11 AAC 59.810(11), and 11 AAC 58.520 regarding the use of comparable land sales. All three appraisers used the same basic techniques in adjusting comparable land sales for differences in comparison with the subject lots. The major factors for which adjustments were made were for increase in price levels between the dates of sale and the date of appraisal, neighborhood location, specific location (corner or inside lot, street improvements, utilities available, zoning, etc.), and physical characteristics of the comparables, including such things as soils, topography, shape and easements. As the panel finds that offsite improvements made since 1961, specifically water, sewer, power and road improvements are to be included in arriving at the fee market value of the land, the Panel addressed itself to the major points of disagreement between the State and the lessees' appraisers which are adjustments for time increment, neighborhood and an electrical transmission line easement.

(1) Time Adjustment

All three appraisal witnesses agreed that a rapidly rising trend of price levels for industrial land was evident

during the two-year period prior to the appraisal date of May 2, 1976. Mr. Bunn testified his conclusion was that a time increment of 3.5% per month was appropriate; both Mr. Ferrara and Mr. Simmons concluded a time increment of 2% per month was appropriate. Mr. Bunn used 10 comparable sales which indicated a range of time increment from 2.8% per month to 4% per month. One example which tended to limit Mr. Bunn's testimony in this regard was where he compared the sale of one parcel with a later sale of another parcel to arrive at an indication of time trend. Mr. Bunn did not adjust for other factors but compared the two sites as equal in value when actually one of the sale sites had much less utility than the other due to its very odd shape. Also, Mr. Bunn utilized sales in a faster growing area of Anchorage (South Anchorage) in arriving at a time adjustment. The Panel believes a reasonable upward adjustment for time increment to be 2% per month. This belief is based on the fact that Ferrara and Simmons used sales of property more likely to reflect accurately the increase in value in the Mountain View area. The Panel finds the lessees' appraisers more persuasive on this point.

(2) Neighborhood Locations.

Mr. Bunn used 18 comparable land sales with two from the immediate Mountain View area, two from the Anchorage Industrial Park in the Ship Creek area and 14 in the South Anchorage area in the vicinity of International Airport Road. Mr. Bunn's testimony was that the Alaska Industrial Subdivision is comparable in location to the other industrial areas of Anchorage, that price levels for industrial land was similar and that no adjustments were required for

neighborhood location to the comparable sales used. Mr. Simmons and Mr. Ferrara both agreed that the Alaska Industrial Subdivision neighborhood was inferior in price levels to either of the Ship Creek or South Anchorage Industrial area. Testimony was given and agreed by all parties that the Alaska Industrial Subdivision is well located in proximity to the downtown business center of Anchorage, is close to transportation facilities, and has good arterial access. However, testimony was given that the type and intensity of uses, as well as the rate of development within the Alaska Industrial Subdivision are inferior to the Ship Creek and South Anchorage Industrial areas. The Panel agrees with the lessees' appraisers in this regard and finds that the prices of comparable land sales from the Ship Creek and South Anchorage Industrial areas should be adjusted downward before arriving at a comparable market value for subject lots in the Alaska Industrial Subdivision.

(3) Electrical Transmission Line Easement.

Testimony was given and evidence presented concerning an electrical transmission line easement 45 feet in width which crosses diagonally through the Alaska Industrial Subdivision. According to testimony, no permanent structures may be built within the easement right-of-way and no structures may be placed closer than 10 feet vertically and horizontally from the electrical wires or supports. Mr. Bunn testified that the transmission line easement was not important and would not result in any loss in value to those lots crossed by the easement.

Mr. Ferrara testified that there is a loss of value in varying degrees caused by the easement, depending upon its location within each affected lot. Although Mr. Ferrara said he did not have time to investigate the effect

on value to a sufficient degree to estimate what loss in value would be involved for specific lots, he said one measure of the loss in value would be the cost of relocating the easement either within the public street right-of-way or along the property boundaries.

Mr. Leon Brown, a lessee in the Alaska Industrial Subdivision since May, 1958, to the present, testified as to the problems encountered in developing four lots which were affected by this transmission line easement. The Panel notes here that Mr. Wilhour said he complained to Peanuts Main on the staff of the Division of Lands with a resultant rent reduction because of the effect of the easement.

The Panel believes that the evidence is conclusive, and common sense dictates, that the electrical transmission line easement has an adverse effect on value. The Panel suggests that the testimony of Mr. Ferrara as to the cost to cure method, that is the cost of relocating the transmission line, is only one way of measuring this loss in value and that other appropriate means of estimating loss of value may be used. Before Mr. Ferrara's method is used, an investigation of the feasibility and likelihood of moving the line should be made. The Panel notes that the transmission line affects in a substantial way four of the reappraised lots. One method might be an actual computation of the value of the lost area.

(4) Rental Rate.

The May 1, 1976, adjustment, in addition to using a higher fair market value as a basis for computing the annual rent, also increases the rental rate from 6% to 8%. This, Mr. Buma testified, was done because his review and analysis of private leases in the community indicated that 8% was the more appropriate rate.

The lessees protested that this increase was unwarranted. They argue that various provisions of the State lease make it less desirable than a private lease and that therefore the rental rate should be lower. The major differences which made the state lease less desirable were asserted as follows:

(a) Lack of subordination. Many private leases allow for subordination of the fee to any encumbrance placed on the property to secure debt financing. The state lease does not provide for this, it only allows the financing agency to step into the shoes of the lessee by way of a "collateral assignment of interest." Mr. Bunn testified that this provision was substantially the same as subordination; thus, no downward adjustment should be made in the rental rates to allow for this. The testimony of Andy Hoge, an attorney heavily involved in lease financing, and John Kamper of Peoples Bank persuade the Panel that Mr. Bunn's perception of subordination is simply wrong. The lack of subordination in the State lease is a very significant factor for which adjustment in rental rate should be made.

(b) Lack of arbitration and rent ceiling. Many private leases provide for arbitration of disputes over rent or rent ceilings or rent payments adjusted in accordance with the cost of living index. The State's lease contains none of these provisions. Mr. Bunn made no attempt to adjust for these provisions. The lessees argue, with considerable merit, that provisions such as rent ceilings, linking adjustments to the consumer price index, and arbitration provisions provide some degree of predictability as to what the rent will be in the future. This predictability is absent in the State leases, which provide for a unilateral adjustment

of rentals by the lessor.

(c) Option to purchase. Many private leases also provide an option to purchase. The State's lease contains no such provision.

(d) Floating easement. The State's lease contains a floating easement giving the lessor the right to grant easements or rights-of way across the leased land with compensation for improvements damaged or destroyed, but does not provide for consequential damage. The private leases do not reserve this kind of easement.

Most private leases contain one or more provisions which make them more advantageous to the lessee than the State's lease. Contrary to testimony of Mr. Bunn, the State's lease contains no provisions more advantageous to the lessees. Given the long term of the State lease, the Panel does not believe the right to renew is of significant benefit to the lessee. The evidence is overwhelming on this point. The banker, attorney, and lessee's appraisers all testified to the more noxious State lease. Thus, the Panel believes the increase in rental rate to 8% is unjustified. The general market rate for private leases is no doubt in the 8% range; however, some allowance should be made for the less desirable features of the State lease. For the above reasons, the Panel believes a return to the 6% rate would accurately reflect the market rental value for a State lease.

IV

SUMMARY AND FINDINGS OF FACT

In summary, the Panel makes the following findings:

1. The Division incorrectly made no allowance for site preparation to arrive at a fair market value in accord with the lease. The evidence was overwhelming that there was substantial overburden to remove, from one to four feet with some fill required perhaps on most lots.

2. The Division's appraiser incorrectly arrived at a time increment to use for upward adjustment of comparable sales. The Panel finds that the 2% per month time adjustment suggested by the lessees' appraisers to be well founded and the correct one to apply in the appraisal of the subject lots.

3. The Division's appraiser used some 14 sales from the South Anchorage area as comparables in his reappraisal. Only four comparable sales were taken from an area near the subject property. The Panel is cognizant that Mr. Bunn was attempting to find land of the same zoning classification as the subject lots to use as comparables. However, the Panel finds that the rate of development is higher in South Anchorage and that the type and intensity of uses is greater. Some appropriate downward adjustment should be made before arriving at an appraised value of subject lots from these South Anchorage sales. Additionally, the Division's appraiser should consider the comparable sales used by the lessees' appraisers, even though they were of differing zoning classifications.

4. The Division's appraiser should have, but did not, adjust downward the value of the lots which have an electrical transmission line running through them. The Panel finds from the map submitted by the Division that this line has caused a

substantial diminution in the value of at least four of the reappraised lots. Additionally, the Panel finds that the adjustment suggested by Mr. Ferrara to be appropriate only if it were economically feasible to move the line, and likely that such a cure could be consummated.

5. The rental rate of 8% is excessive, considering the private lease market and the disadvantageous provisions in the State lease, including: (a) no subordination of fee, (b) no rent ceilings, (c) unilateral adjustment with no arbitration, (d) floating easements, (e) lack of option to purchase. Specifically, the private leases examined contained one or more of the following advantageous conditions: (a) subordination, (b) an option to purchase, (c) rent ceilings, (d) arbitration; and none contained floating easements provisions.

6. The Panel finds that subordination and collateral assignment are not the same as suggested by the Division's appraiser. The evidence on this point is overwhelming, consisting of the testimony of a disinterested expert, Mr. Hoge, that financing of a leasehold interest is typically much more favorable to a lessee when the land lease contains a subordination agreement. Mr. Kamper, Mr. Simmons and Mr. Ferrara agreed with this assertion.

7. The advantages alleged to be present in the State lease are more illusory than real. Any advantages to the right to renew the 55-year State lease and removing improvements is insignificant in relation to the disadvantageous features described in Finding No. 5. This is supported by weight of the testimony of expert witnesses.

8. The lessees had no real opportunity after they had received notice of the reappraisal and before the effective

date of the repeal of the waiver of adjustment to seek such a waiver. It was unrealistic to think they might have reason to seek such a waiver prior to receiving notice of the reappraisal.

9. The effect of the adjusted rentals is to discourage development of the subject area rather than to further the objective of encouraging development, which is the intent of the leasing regulations (11 AAC 58.900).

10. A new reappraisal by the Division should be conducted.

V

CONCLUSIONS OF LAW

The Panel having heard legal argument and read the memoranda submitted makes the following conclusions of law:

1. The lease and regulations read together require that the Division include in its appraisal of subject lots the increment of value generated by offsite improvements, such as installation of roads and utilities into the subdivision, with the provision that any utility hook-up to a main trunk line which was paid for by the lessee or a predecessor not be included, even if it is off the subject property.

2. The terms "such adjustment to be based primarily upon a reappraised annual rental value of land" and "any changes or adjustments shall be based primarily upon the reappraised rental value" found in the State's lease and 11 AAC 58.520 mean that the Division should consider other factors besides a reappraised annual rental value in arriving at an adjusted rental. This is so because of the use of the adverb "primarily" to modify the verb "based." The principles of interpretation dictate it be given meaning; without the presence of this word the Division would be able to consider only the reappraised annual rental value.

3. The reappraisal of May 1, 1976, the subject of this hearing, was not done consistent with the provisions of 11 AAC 58.900, which expresses the intent of the leasing chapter of the Administrative Code.

4. Subordination of the fee and collateral assignment are substantially different as a matter of law. Subordination of the fee means the fee can be encumbered to secure debt financing for the lessee. The holder of a collateral assignment merely steps into the shoes of the lessee.

VI

RECOMMENDATIONS

Implicit in the above discussion and findings is that the Panel finds the Division's reappraisal unacceptably high. Therefore, the Panel recommends that the subject lots in the Alaska Industrial Subdivison be reappraised by the Division in a manner consistent with the above discussion, findings and conclusions.

In addition, the Panel believes further recommendations are appropriate. The present lease and the present leasing policy should be modified. These modifications should be designed to put the State on a competitive footing to the degree possible with private lessors and are as follows:

1. In accord with the provisions of the lease, the lessees should be encouraged to record expenses incurred in site preparation so that the "original condition" can be more adequately ascertained.

2. The lease language should be clarified to remove any possible inconsistencies with 11 AAC 58.520.

3. To insure some predictability, place some control over the size of the rental increase through utilization of a ceiling

on the size of the increase in rental every five years.

4. Provide for arbitration of disputes over the annual rental arrived at after a reappraisal process and overinterpretation of other sections of the lease. This would ameliorate the current unilateral nature of rent adjustments.

5. Eliminate the floating easement. The State could exercise the right of eminent domain to condemn. The condemnation would result probably in greater compensation for damages to the lessee, especially in view of the Supreme Court decision in State v. Hammer, 550 P.2d 820, thus the lease would be more attractive to the leasing market. Additionally, the language in the current lease is ambiguous as to damages compensable. This ambiguity only encourages litigation.

6. These above recommendations, if adopted, would assure the State a competitive position in the lease market, encourage development of the leaseholds consistent with the intent of the leasing regulations, and be equitable to the lessee. The Panel also believes the State should be able to obtain a good return on its land. Accordingly, if the recommendations as to the lease are adopted, the rental rate should be changed to reflect the removal of the undesirable aspects of the State lease.

7. Suggest an amendment as to AS 38.05.105 to eliminate the term "primarily" from the statute, and also eliminate this term from the regulation and the lease. This is ambiguous, and assuming it has meaning, it may encourage individual accommodation of lessees by the Division. This, the Panel believes, is not in the State's best interest in that it could encourage political maneuvering to attempt to obtain this accommodation, and may well mean uses other than the highest and best use would be perpetuated. Also, the presence of such an ambiguity

could lead to an excess of administrative discretion.

8. Finally, should some or all of the above general recommendations be ultimately adopted, then legislation should be suggested for enactment providing all present lessees the opportunity to negotiate modifications consistent with the changes adopted.

RESPECTFULLY SUBMITTED at Anchorage, Alaska, this 20th day of January, 1977.

TIMOTHY G. MIDDLETON
Hearing Panel Member

KENNETH E. ZANZOW
Hearing Panel Member

GEORGE K. HOLLETT
Hearing Panel Member

TESTIMONY OF

ANDREW HOGE

before the

Division of Lands Hearing Panel
meeting to consider various appeals of the
reappraisals of leases in the
ALASKA INDUSTRIAL SUBDIVISION

Hearing convened 10:00 A.M., December 14, 1976.

ATTACHMENT "B"

ANDREW HOGE

Anchorage attorney

BY TIMOTHY MIDDLETON, HEARING OFFICER:

Q: Do you want to state your name for the record?

A: Andrew Hoge.

Q: And your address?

A: My work address is 3201 "C" Street, Suite 706, Anchorage 99503. My home address is 1370 Bennington Drive, Anchorage, 99504.

Q: Okay, thank you. Mr. Baily.

BY DOUGLAS BAILY, ATTORNEY REPRESENTING LEASEHOLDERS

Q: Will you tell us what your business or profession is?

A: I'm an attorney at law.

Q: And you're in private practice?

A: In private practice.

Q: And to take one of the risks that lawyers shouldn't take, I'm going to ask you some questions that I haven't discussed with you. You have been asked to come down here today to testify by myself on behalf of the leaseholders?

A: Yes.

Q: And it is correct, is it not, that you and I have not discussed in any detail your testimony?

A: Yes.

Q: And is it also correct to say I believe that the that the position, the opinions that you will express today were not prepared or derived at my request or in conjunction with any preparation for this hearing?

A: No.

Q: Do you represent any of the leaseholders in Alaska Industrial Subdivision to your knowledge?

A: To the best of my knowledge, I do not. I used to represent Inside Alaska Tours, but they have sold their property, so ... And I still represent them. They hold the second mortgage. Other than that, I don't know of anybody. Our firm might, but ...

Q: The point is, that it is correct ...

A: But I don't, ah, I mean I don't know of it. There's a likelihood we do have some ...

Q: But is it your understanding that I contacted you concerning your testifying here because I had heard that you have prepared a position, independently of this hearing, for presentation to the Governor's Task Force?

A: Yes. (Inaudible)in the state lease programs.

Q: It is also my understanding that I have been advised by Mr. Rasmussen that you are, have been authorized by

National Bank of Alaska to state what the position of NBA would be with respect to commercial lending on state leases in Alaska Industrial Subdivision?

A: Yes.

Q: I wonder if you would relate them to the hearing panel, and I ask, Mr. Hoge, that you give this presentation in comparative summary with respect to the (inaudible) knowledge of the lease terms contained in the standard state lease forms which are utilized in Alaska Industrial Subdivision and some of the difficulties which he sees with respect to financing institutions participating in real estate loans and commercial loans in Alaska Industrial Subdivision (inaudible).

BY MR. MIDDLETON

Q: Is this his position, or NBA's?

BY MR. BAILY

Andy represents NBA.

BY MR. HOGE

I represent NBA on a case-by-case basis, and I've dealt with one loan at Henlin Subdivision for NBA most recently on an interim loan; and I've dealt with ground leases, in fact representing the developer on a parking garage over here which is similar to the state ground lease. And I've dealt with other

ground leases, both subordinated and unsubordinated, for National Bank of Alaska, Washington Mortgage. I represent several lenders outside and in the state, and I gather I'm reflecting what conclusions I've drawn from that experience as to what lenders generally require of loans of this nature. The state has a policy, which I understand, of leasing its lands. However leasing its lands has several provisions which cause concern to lenders and really affect the possibility of financing the project. Maybe in narrative form I could ... I've got a pad here, just to keep track of the main headings and then maybe after I've testified I can give some ranking to what I think are the more important ones. The obviously most important one is that the state will not subordinate. And that really is the most crucial one, because when that occurs that means that the lender must, if he forecloses his security instrument, which usually is a deed of trust, must come in and assume the responsibilities of the lessee. Now, that may not sound like much, but you've got to realize in the lending business that the lender, when he does come in for foreclosure, means that his borrower's gotten into trouble. And, usually, if he's gotten into trouble on the loan--the real estate project--there are a whole number of defaults which the lender then must of necessity cure to protect his security. And, obviously, if his borrower is in trouble, he can't go against his borrower--his borrower is probably bankrupt or nearly so--so he's got to look to his security, which is the project, to protect

himself. Now, that is a risk in the lending business. I think most lenders accept that. But, when they in addition have to deal with a third party, the State of Alaska in this case--but anybody else, it could be the City of Anchorage, or that--who are sitting there with a defaulting borrower ... I mean, a defaulting lessee ... the pressure is on the lender to cure all these defaults and try to make something rational out of really a messed up situation. So that's why subordination is just very important. It makes another difference, too, in evaluating the project, because if there is subordination it means that the lender can come in and take the fee. It also means that fee is available as security for the loan. If it's just a ground lease that can go up every five years, or whenever your reappraisal increments are stated for in the lease, then that lease really has very little security, you know, towards your project. You really are looking to the commercial project then to carry one of the loans. So, subordination is a very critical thing. Now, the state is taking the position that it will not or cannot subordinate. So, the things then that lenders look to when they make what we call unsubordinated ground lease loans become even more critical, and those things--again, not in terms of importance, but all of them, I think have some value--are first, what happens to the rent? In other words, if you're making a loan, and you make the evaluation of the project--and, again, I'm talking about how lenders evaluate it, maybe not like a real estate appraiser,

although there's a similarity--you've got to say, "Can this project bear the costs associated with that, and pay back the loan?" I mean, that's ultimately what it has to do. If one of those factors, which is usually a major factor in the ground rent, can dramatically increase, then you get into a very critical situation as to whether there's enough money coming back to pay off the loan. So, generally, lenders request that there either be a level term rent or that the rent be ascertainable. And in fact for at least savings and loans, by federal law, that's a regulation that is required, and the regulation when I last looked at it a couple years ago provided that the rent has to be ascertainable for a term of at least ten years after the term of the loan. And I'll explain why that's required. That also, while not necessarily a legal requirement, is generally followed by most banks in Alaska, and some insurance companies, depending on whether they're what we call an eastern life insurance company out of New York, have other terms, like 80 per cent of the loan term. Now the reason for that is that if the lender has to come in on an unsubordinated loan, he can extend the terms of payment to eventually recapture his loan. In other words, he can push the payments out for five years if there's a default. Five years to go. Then you can push them out to fifteen and presumably recapture your loan. I might add I made a comment to the Governor's Committee on that, that while regulations now provide for level term, I mean they provide for level term payments during the term

of the loan, it ought to be the term of the loan and up to ten years. So, the rent is very important.

The next item that causes real difficulty is that the regulations are totally inadequate to cure defaults. The regulation says that if the ground lease is forfeited, then the state will recognize the lienholder, presumably the mortgagee or the lender. But this is only after the lease is terminated. That is not of m. ch help to anybody, because that procedure can take a certain amount of time because of the requirement, as I understand in the McCarrey case, that any lessee who is being defaulted can get a hearing... I mean, that can drag on forever. And you need, you know, if you've got problems--I can tell you in the lending business, I've been in some loans that haven't always worked out as well as the lender planned--you've got to get in there and solve the problems now. The problems only compound themselves if you're forced to wait. So, your default provisions in the present state ground lease are totally inadequate. And I gave the illustration to the Governor's Committee, and I've given it to you here, because I think there's some importance to it. The assignment lease form that you are required to use and analyze it has about two sentences. And I brought along, just to show you what it looks like. This is a copy of the ground lease with the City of Anchorage for the parking garage. And most of those provisions govern the type of construction, the type of the project, curing of defaults, what happens in the event of condem-

nation, what happens in the event of casualty. Yet the state really never addresses any of these really critical problems in their ground lease assignment forms. So, one of the things we've attempted to do ... I know in the first Penny loan, when this whole general problem started coming up ... was we drafted our own assignment. We finally agreed to that with the state, and I think it's four legal pages of single-typed space, it was, every word was negotiated. Not necessarily the most satisfactory thing, but acceptable to the lender. I'm not abdicating either that you have to have big ground leases like this, but there certainly ... there should be discretion, and it should be recognized that various projects require various loan conditions. And then I think you've got to address that, and the fact that you don't have it makes it very risky. Really, what is happening, I think you will find, is the projects that are being and will be developed until these areas are resolved or there's some reasonable policy on some of these things, is the lenders will make some loans--I'm not saying they will never make a loan--but they'll make them on the credit of the borrower, and not on the project. In other words, obviously if you're dealing with General Motors Corporation they can sign a note and, you know, they're not going to be as concerned. But, when you talk about the kinds of people that deal in Alaska who are not of the financial caliber of General Motors, then the lender is going to be looking to that project to make those payments, and not to the particular lender.

So, I think it's just going to cut off and has to have an adverse effect on financing, especially, I think, with some of the dramatic rent increases. You just wouldn't, as a lender, be too enthusiastic about making a loan if you know that rent can jump that dramatically every five years. It just, you know, that's ... to me that's just common sense.

Another area that becomes important, I think, is in these ground leases--and they've ... there's a little variety in them, the aviation lease is, I think, a little different than the Division of Lands, but it's the same problem. One, a condemnation and putting through public roads and improvements. I know in the Penney ground lease they tried to negotiate some of those points. In other words, the reason why you do that is you, when you get a state ground lease or make a development, you're planning to put "X" building here, "Y" building there, "Z" building here. If you were building a shopping center, it's critical that you have certain tenants--what they call "anchor tenants", "national tenants", "regional tenants". If the state can come through and build a road and say--I guess in some of the aviation leases they only have to pay you for the land--but, if they can just go through and, without any regard to your planning, take condemnation, that's another risk that the lender's gotta' take. While true, there's the right of private condemnation in any project, but the prevailing thing of that is, at least the little experience I had with the Department of Highways, both as an attorney general

and outside of it, is obviously the state's going to look to use state lands before it condemns private lands. I mean, that's logical, 'cause it costs the state something. (inaudible). You've got to recognize some of those protections. I don't know that casualty insurance becomes significant to the state, but obviously on the parking garage here that's very significant, I mean casualty insurance. So, those are what I call normal lease provisions that really aren't adequately provided for under the state regulations, and I've advocated to the Governor's Committee that, to the extent possible, there ought to be given discretion to the Director or someone in his office that these things can be negotiated. The state, of course, is ultimately protected because it never subordinates. And by never subordinating it will always have the land and the improvements on it. So, those are the ... I think ... the main areas I address myself to. I made comments to the Committee on some of the things that are involved. You get different problems, of course, with residential housing, FHA requirements ... but I think that general category of things that the general problem areas there's different solutions, of course. So, those generally would be the considerations that I think any lender is looking at in determining whether to make a loan; and, obviously, a lender is going to ... y'know, if you've got a good project on fee land or subordinated lease land versus a project on state land ... y'know, a comparable project, you've just ... the lender's got to be looking at the fee land. I mean, there's

just too much uncertainty in this area, and I really think the state needs to address those questions. And I hope they will. I mean, I think it's important if you're going to have state land and you're going to hold on to it and lease it, then you ought to provide the means to develop it. You know, unless you want to leave it as park land, but then if you want to leave it as park land, which may be a legitimate choice by the state, then you shouldn't be forced to lease it, and it should have never been given (inaudible). That's really the object of this (inaudible). That really is the areas that I would stress to this committee.

MR. BAILY

Your honor, I have nothing ... no further questions.

MR. MIDDLETON

Mr. Gissberg.

JOHN GISSBERG, ASSISTANT ATTORNEY GENERAL

Q: Right. Mr. Hoge, how long have you been in the Anchorage area?

A: Anchorage, Alaska? I've lived in Anchorage since 1965.

Q: And have you been familiar with the Alaska Industrial Subdivision?

A: I've served it, yes.

Q: You have, reviewed (inaudible) lease agreements for that particular area ...

A: In connection with this comments before the Committee I looked at a lease. I can't tell you for this hearing today I intimately reviewed it.

Q: The provisions that you mentioned, though, were from a state lease and they were applicable, of course (inaudible).

A: Yes, I think so.

Q: As far as (inaudible).

A: I mean, I think they're pretty standard provisions.

Q: Now, until ... you talked about this ten years' security period past the normal time of the loan. What's the normal term of a loan that your bank has been involved in?

A: Well, let me give you ... there's been a little change in that, and that's because of our inflation which we don't seem to be able to control. It used to be lenders would loan --and again--a variety of terms on ground lease loans. But say you're looking at a 20-year term, maybe a 25-year term of a loan. But what the lenders do now is make the payments amortize on either a 20-year basis, 25, 28, I've seen 29. But they have a balloon at the end of 15 years, and the balloon is there so that if the money market--in other words, the lenders traditionally got caught in four per cent when money rates are at ten. Now they could never get out of the loan for thirty years. So, as a compromise, they're looking at ten years, 15 years, a balloon, so

that at least they can look at the loan again. And then the nature of the provisions, at least I have written for National Bank of Alaska, Washington Mortage Savings and Loan in Washington, are that then they have an option to continue the payout over the next 20 years or 25 years. It varies, but that's one thing that's ... I've got to qualify my remark on. But, assuming you're dealing with a 20 or 25-year term, then the ten years you would add to the maximum term of the loan. But, as I stated, some of the New York life insurance companies, I may even have a letter on this, we have a ... when we were doing the parking garage, we had to put in a provision because our long-term commitment wasn't fully committed at that point to get enough term so we could make the loan to whoever came along, and I think it's 80 per cent--there may even be a few that are 75 per cent. So, if you have a 20-year term, you take in effect 20 per cent of the 20, which would be four additional years.

Q: Okay.

A: If you're an 80 per cent lender. If you're a 25 per cent lender, they want five additional years. If you're a 30 year loan, you'd have six years, if you're a 75 per cent lender you're, well, you're adding about eight years. If you're dealing with an S&L--savings and loan, federal--you're adding ten years. If you're doing with NBA, generally, obviously every lender where he's got discretion makes exceptions. I think they generally talk about ten years. They generally follow ten years. That's

been my experience.

Q: That's very complicated and interesting. I don't know it very well. If the state could ... if you got an application for somebody with one of these state leases, and, I mean, you looked at it on the basis of what you have said very possibly they might say no, we can't lend on this because we don't know what that rate is going to be in 15 years from now. It will have changed three times by then. The rental rate may have gone up quite high, so we ...

A: Yeh.

Q: You'd say, in light of the fact that there's no subordination, why, it would be difficult for us to loan on that. If your loan was for 20 years and if you were able to give them testimony, the lender, the person who wanted the money, evidence that no, we can't loan on this unless we know that that rate is going to be fixed for ten years beyond the term of our loan, and they came back with a statement from the Division of Lands that we will fix it at this rate for the length of your loan plus 20 years, then you would be able to lend on it, because you would know the rate. If that were possible.

A: Yes, that would eliminate that problem on rent.

Q: I presume you are familiar enough with what happens in the (inaudible) office lending at that, that it was possible to get waivers, like thru June 22 of this last year, when it became only possible to get waivers on residential property.

A: Yes. But that was PET land.

Q: That's exactly right.

A: (Inaudible) is maybe a good example, but before that statute was passed I can assure you it was not that easy to get the waiver. I think ...

Q: Do you know if anybody ever got one of those in those particular cases.

A: I don't know.

Q: Do you know of anybody in your experience in the bank that applied for one?

A: No.

Q: Can the loans that the bank made that you're aware of (inaudible).

A: The loans I was involved in, no. I don't think.

Q: How many loans, approximately, have you been involved in on state leases that don't provide for subordination?

A: On state leases, I've been involved with, directly involved with two on PET land and I'm familiar with three or four over there. I was involved in Inside Alaska Tours' loan on their building, and that to me wasn't on commercial real estate, it was on the strength of the borrower, Mr. Kniesol, who was very well-to-do by himself. I have been involved with other ground leases, unsubordinated ground leases, but I think those are the ones that you could call my most direct experience with the state. I've been involved in the City of Kenai, the City of Anchorage, private

parties.

Q: The loss of this opportunity for a commercial developer to get a waiver is to make them more risky for your loan?

A: Yes, it does.

Q: Now you also mention, I think you were referring to a (inaudible) lease, the need for what you call "anchor" tenants?

A: Well, I ... what I was trying to mention there was that the condemnation provision which gives just the state the right to build a road or use (inaudible) right-of-ways is too broad, just by itself. In other words, you have to make some agreement that can be exercised rationally, and I gave you an example of ... say you made a little shopping center--or a big shopping center--on state land. And you have Safeway and Pay'N Save or LaMonts and Pay'N Save as your anchor tenants. If the state should just decide that it wanted to put a road through there, you know, then that's a negative factor in deciding to make the loan, because it's more likely that the state will use free right-of-way than right-of-way it has to pay for. Based on my experience, and I think just common sense ...

Q: Okay. But now you would have loaned from the bank that amount of money you will (inaudible), or somewhat close to that, I mean, if we ...

A: Yeh. Well, I think the appraisers can tell you it

doesn't quite work that way. I'm talking about commercial real estate. You figure the income from the building or the project. Okay. You deduct the expenses, then you use a capitalization rate to get the amount that that project is worth in terms of income. Now it may cost you more to build it than it's worth in income, so you wouldn't build it. But assuming that the income producing ability of that building equals its construction cost, or nearly that, then you've got the discount that you make in a ground lease loan. You have the loan, the value ratio, and ...

Q: What is the discount because you're making a ground lease loan?

A: Well, because ...

Q: What is the (inaudible).

A: Well, because on a ground lease loan you can never get the appreciation of the land.

Q: You have a fixed discount?

A: Well, I ... it varies again by lender. But I've seen sixty-five to seventy per cent--this is on unsubordinated ground lease loans.

Q: What would be the range?

A: Sixty-five to seventy. Some may even go as high as seventy-five -- it depends on the quality of your project, what kind of income it's turning out. Whereas on a fee loan you might go as high as eighty. In fact under, I think, the state banking laws you can go up to eighty under the law. I mean,

that's ... you know, when you're looking at construction, that's pretty dramatic. That ten per cent is, y'know ... that may be what you need to make the project go. So, it, ah ... and when you're looking at multi-million dollar projects, which in Alaska more and more you look at, that stuff is very important.

Q: So you're looking carefully at the income producing aspect of it (inaudible)?

A: Right.

Q: Would it be unusual to loan more than the improvements cost?

A: Ah, that gets involved again. When you say what the improvements cost, okay. It's a mistake to have what they call "hard cost" -- that's the contract cost. Okay. And I won't name the project, but I'll give you -- this is a realistically -- this is a true example. On a project in this town that's going to cost -- construction cost -- seven million dollars, the loan has to be nine million dollars to take care of what we call "soft cost". Architects, loan fees, special utilities, fixtures, other improvements, attorneys' fees. So, to answer your question, you have to loan ... you have to meet all these costs. I mean, the buyer has to meet all these costs.

Q: So, in the event that ... let's say that this was a true example and that, okay, nine million dollars was lent, and it's a seven million dollar structure on fee land which the state came in and ...

A: Right.

Q: ... and condemned it. Now the state would pay for the cost ... the seven million dollars that the lender ...

A: Well, hopefully, the state'll pay for the nine million dollars. Because these soft costs are costs you can say go into the improvement ... are part of the improvement. But the state could go down to seven million dollars. They could say ...

Q: How much does it cost you to build that building?

A: The contract says seven million dollars.

Q: It might take litigation to decide it?

A: It would probably take litigation in proving that.

Q: How often (inaudible). Let's say you were able to get the nine million.

A: Okay.

Q: Well, let's say you only lent the loan for seven million.

A: Okay.

Q: Why ... Why is the subordination of the fee so important if you get it back from the improvements when that easement went through?

A: Well, okay. This is a changing area of law. Until -- and we ran into this on the parking garage -- until this past summer our supreme court had not ruled as to what extent if any they were gonna' recognize lessees. Ah, there's better recent supreme court where they'll ... decision recognizing lost

profits. But we don't know how far that's going to go.

Q: (inaudible)

A: I can't tell you the name of it, it was out of Fairbanks, it was on a bar. The guy had a bar and they started to recognize lost profits in the decision. But there is such a decision. And up till then negotiating with the city, they didn't want to recognize those values in a ground lease, and after we had a supreme court decision it was easier to negotiate on that. But, we don't know. I mean, we really don't know what recognition is going to be given to those values.

Q: (Inaudible)

A: I had understood up to that time they left that to be part of the award and then whatever agreement the parties made with the Division and so forth.

Q: So, it would be incorporated from the state, but the city ... as far as the city was concerned, what ... ?

A: Well, no ...

Q: I mean, it's a supreme court decision.

A: No, I'm just saying as I understood the state's past practice it determined what the value of the land or the building they were taking and that was their award. Now if that building was leased, the state said, "Here's the fair market value, that's all I'm required to give to you. Now you people fight." And I'm sure any of your appraisers who've been involved in that kind of litigation will tell you how interesting it gets,

ah ...

Q: Now we're talking ... I'd like to think about the case where the state is the ...

A: Right.

Q: ... lessor. Then if there's a multiple ... if there's multiple lessees ...

A: Division.

Q: ... then, of course, they would have to fight it out. That would depend on their subleases, and whatever they ...

A: Right. All I'm trying to point out is that that's an area of law that is changing, that there's really no definite policy on it, and obviously the state -- you can expect them to take this position -- is going to take the hardest position they can to protect the state. I ... I don't have any problem with that. But, in some of these areas there are ... in other words, you go to the California law ... they have gone through some of this litigation -- there are some set rules that you can agree to that at least are acceptable to the financial community. We really don't have those rules set up in Alaska.

Q: In California would they be more likely to lend on the ... with the use of improvements as security rather than requiring the subordination of the lease?

A: I ... I can't tell you what California lending practices ... California is unique in a lot of respects.

Q: I guess what I really don't understand -- and I

think you did explain it to, ah, me -- is if we ... if a lender can get seven million dollars out of improved ... the state is going to pay you ... compensate for those improvements. Why is the subordination ... (inaudible)?

A: I don't know how much the state's going to ... y'know, is the state gonna' pay the severance damages? You take the corner off of Safeway's building, and they lose the value there; and you take fifty per cent. You know, it's the severance damages to the whole project. Or, you build a planned-unit development -- a nice housing project -- you run a highway through the middle of it. Y'know. That ....

Q: So then what you really need is ...

A: ... dimishes. Well, sure, sure. I would stress ... my solution is better planning before you start so that will never happen.

Q: You plan it better.

A: Right. And then as a second resort have a fair ... And, I'm not saying the state should get cheated or anything. I'm saying a fair division of compensation. And that's all I advocate. And so everybody's treated fairly, that's all. Y'know.

Q: Thank you. And on the ... on this point about the state being treated fairly ... I think that's obviously what they ... the best interests of the state certainly ... the state is going to have to be served or we're not going to be involved in leases if we didn't think it was. What ... I mean, a lawyer

plays many roles, as you have in your long term of service in Anchorage. Could you assume now the role of a private attorney and I'm a person ready to, ah ... I come in and I have some property that I invested some money in, and I don't see much of an income from that property and I don't need ... I want to set it aside, and, in fact, I think I want to set it aside for a long term -- say a hundred years.

A: Okay.

Q: And, further, let's assume that we're talking about forty years ago. And, I'm going to rent it now -- I'm going to rent it to somebody for a hundred year term at three per cent. But in the year 2000 if the common rental rate in Anchorage is fifteen per cent, I'd like to make sure that whoever's going to benefit from that income is getting better than three per cent or four percent, whatever I said, of the fair market value. Now, you indicated the example of the bank, which is quite interesting, where they may on a long-term loan lend at a low -- at the going rate -- I say, four per cent, and have a balloon payment at a certain period of time. I think you said fifteen years would be a common one. And that doesn't necessarily mean that the guy has to pay it all, but then that part of the loan is renegotiated at the going rate at that time. Now, if the state was going to get involved, if a person was going to get involved in a long-term lease like this, what could they do that would be desirable concerning the lease rate, so that there would not be such a

windfall benefit to the person that picked up the lease in the beginning?

A: Well, one of the things I've told many ... I mean, you're going to back the value of the loan, but ... the Governor's Committee has put a lid on the rent. Obviously, it's one ... y'know, you can't have 300 and 400 and 600 per cent increases, but it would never go up by more than, say, 25 per cent.

Q: Put a lid on the per cent increase.

A: Yeah. Because that ... it's either a fixed rental or ascertainable rental. Then it would be up to lenders to decide whether even that's acceptable. In the Penland thing -- because I was dealing with the mobile home space -- and we had to show this to the state. Mr. Penney, I think, went to something like 25 lenders before he found one, and that lender was only going to go on a level term. And that was over a period of, y'know, four, five or six years. So, ah, y'know, that ascertainable rent, putting the lid, may work -- hopefully will work -- for most, but not all.

Q: Well, what do you think if you're in a, ah, property value situation where the market value of a piece of property could double in even as much as three months? I mean, would a 25 per cent lid every five years seem reasonable as a maximum?

A: Well, to me it does. Y'know, I'm trying to be impartial a little bit here. Y'know, I can see the state's point

of view to say, "Boy, we want what every per cent that value goes up we want some money for it." Okay.

Q: I'm trying to think ... and you said this is what the bank does, too.

A: Well, I mean, they consider ... you know ... they're trying to look at that. But, let's look at the other coin. If any leaseholder developed on fee land. Okay? Presumably he's paid at today's prices and the land appreciates. By upping the rent he never gets any benefit of the appreciation. And appreciation, of course, provides security for lenders, so the lender gets no benefit from that appreciation. In other words, I suppose you get philosophical then about market value. You ... a year ago, you were doing ... or maybe two years ago ... a subdivision, and there was a great demand for housing. Okay? You're just going like gangbusters. But, if you have a subdivision today, you don't have it sold, you've probably been talking to your banker. So the vagueries of market value ... trying to be ... trying to answer your question ... are maybe not that kind of concept you can pinpoint every second of the day. True, you know, I can understand that these -- especially in the last few years -- we've had some tremendous increases in market value of land. But, alot of people too, you've got to look at their use of the property. They build buildings for themselves -- for their companies. And those companies sometimes just can't respond to the inflation like the state can if it can just raise its

rent, or maybe an attorney can--he can raise his fees. Y'know. But they can't. They're selling a product; they've got a lot of competition; and, y'know, all of those things go into figuring market value. And, again, what's in the public interest? You know, it's kinda' like taxes--everything that you put against a person he's gotta' try to pass on to the consumer and go out of business.

Q: When you talk about the benefit of appreciation, do you see as a philosophy of the private leases you look at the fact that they start out at what the market will bear the first year and then thereafter it's ... it'll be below what (inaudible) were offering at that point?

A: I think it's been ... the lender's gotta' be looking at them as a definite (inaudible) at maturity. Maybe ... let me ... take the disaster situation. Y'know, you can say ... Take the Calais office building--that's where I have my office--okay. That's a great project right now. It's full, good tenants, you know. First-class tenant oil companies, title companies and Alyeska. But two years from now, okay, when Alyeska's done, they've got three or four floors they've gotta' rent out. And when the federal office building opens up that changes your whole market immediately, overnight. And I don't know what's going to happen. And is that building then worth, in terms of let's say--and I have no reason to believe this and I probably shouldn't use it as an example--but, let's say they had to going into Chapter

XI or something. Is that building now worth what it's worth today? The answer is no. Because the market value concept changes. Ah, and what is market value? Are you talking about terms, are you talking about wholesale market value, or are you talking about retail market value? Those are different. Market value to a developer is different that what you and I expect to pay for one lot in the subdivision. So, maybe that word market value gets elusive both in a disaster situation and what level are you talking about? At the development level? Or are you talking at the retail level?

Q: On this benefit of appreciation where the lease is renegotiated every five years to take it back into what the lease market will bear, wouldn't the lessee have the benefit of appreciation as soon as the market started going up and land developers in three months can start getting some benefit from (inaudible)?

A: For how long? For four years, three years?

Q: Well, wouldn't he have it ... wouldn't he have it until the next adjustment to take it back to market value?

A: Well, generally not, because his people that lease from him ... Let's say he builds a building to lease. Okay? They want their fixed rent as long as they can have it. You know.

Q: But what he would give is not the same curve, I suppose he would change his...

A: He would try... obviously he would try to pass

through the increases that he could.

Q: If he did have anybody on the property he would be getting the benefit of leasing land at less than the actual leasehold interest for at least four years, I presume.

A: He, he might. He might, if he could. It depends on his terms. You know, a person in 1970, 71 or 74 could have made terms for a ten-year lease, not thinking there was going to be a big increase in rental. And he's locked in. I mean, he's dead.

Q: Well, let's say it's, ah, let's...

A: And he can't renegotiate these.

Q: Let's look at the state lease. Would, wouldn't there be for every five years ... it's a 55-year lease, and every five years it comes into the market (inaudible).

A: Right.

Q: Then, if the market continues to go up as it has, would he be renting for at least four years below the market rate; and, so, wouldn't that be a favorable deal for him?

A: No. No, no. Oh, I don't think so necessarily. In other words, let's say he made a lease in '74 for ten years. He agreed to.

Q: But let's say it's (inaudible), and every five years...

A: Well, no. I'm talkin' about the owner of the building. In other words, one measure of market value to him is

what can he rent the building out at. Okay? Or rent out part of it. He rents it out. He agrees for ten years to a certain term. The state comes in and with this rather huge increase. It's something he can't pass on. So what... I mean, what's the market value to him? Y'know, he might have a ... I heard testimony in one of the governor's ad hoc committee work ... somebody had, ah ... they were makin' money on a lease. You know, it didn't sound like an outrageous profit from land. And because of the rent increase they're losing money. And they're ... they're tied into a big term.

Q: Well, for example, you probably do...

A: So, if you were gonna' say, "What's the market value of your lease, Mr. Jones?", and he says, "Well, it's a great deal, I'm only losing $12,000 a year." What are you gonna' pay him for it? What are you going to pay for a $12,000-a-year loss? Y'know, the state doesn't reflect those things in its appraisals, I don't think.

Q: Sounds to me like what you might be saying is that, not only would you find it difficult to loan on such a lease that the state has, but you would ... you would probably not be inclined to enter into such a lease agreement yourself.

A: I would find that difficult, yes. I mean, realistically, you know, if yo re talking about big projects--multi-million dollar project boy, you know the lender's gotta' look at those things.

Q: I sure appreciate your testimony on this. I'm gonna have to point away (inaudible).

A: Okay, John.

Q: And, ah, I'm sure that it's also been very valuable to the ad hoc committee. We've been... Some of the things we've been talking about have hit specific words and I want to make sure that I know you meant in the beginning of your narrative you indicated that the regulations are inadequate defaults, and then later on you mentioned provisions. Alright. Were you talking about the paragraph in the lease when you stated ... when you said that? I believe you said that.

A: I'm referring to the regulations.

Q: Alright. Which one are you specifically talking about?

A: Let me see what we've got in here. I at one point had these regulations in this file, but if you have them I can point them out to you. Yeah, I've got it. Not necessarily readily. Okay, ah, when you talk about defaults, if you look at 11 AAC 58.540, that's what I call the DL-50 form, which is this two sentence form that is supposed to protect these somewhat large loans. Maybe it's right that the bank accuses me of writing too much, so they like to keep it concise. So maybe they like that form, I don't know. But, anyhow, you look at the assignment provision. You have to use that form. And that form to me, representing lenders, is adequate. Okay? I mean, I can say that

unqualifiably, and I'll show you ... I gave some sources to the committee that (inaudible). I referred them to ... there's about three good books on ground lease practice, that I thought he should look at. Then look at the rights of mortgagee or lien-holder, 11 AAC 58.590. Okay? And notice of default, 11 AAC 58.570.

Q: What specifically about .590, would you make reference to?

A: Well, in .590 it says that in the event of cancellation or forfeiture of the lease, okay?

Q: Um-hum.

A: The holder of a suborted mortgage, conditional assignment--I haven't figured out what that is--or a collateral assignment--well, the collateral means more to me--will have the option to acquire the lease or the unexpired terms thereof, subject to the same terms and conditions as the original lease. Okay. Number one. And some of these leases have some peculiar conditions in 'em. I don't know whether they do in the Industrial Subdivision, but the lender comes in, and a lender really can cure things with money. I mean, you know, that's one thing generally a lender has, is money. But, if the lessee was supposed to do something that has to be cured, ah, then... Let's say he does. In other words, he has to assume the obligations of the lessee. That's difficult, number one. What I call "non-monetary defaults."

Q: If the obligations are more than paying money.

A: Right.

Q: If, for example, you're thinking of something specific.

A: Well, let's make it like if you had to put in sewers, and you hadn't put in sewers. Or, he was supposed to build something for the state or put in a beacon. He hasn't done those things. And, you know, one, can he do them? Is he capable of doing them? I gather some of the--I'm not talking about the Industrial Subdivision, but some other leases that I've heard about--have some peculiar provisions. I mean they're peculiar in the sense that they're particular to a certain project but not generally applicable. So, you've gotta' comply with those. So, anyhow--and I'm not sure how the state does all this, I've never... I don't think they've really thought it through. But, you go back to 11 AAC 58.560, you can cancel it, basically, on 30 days' notice. Okay? And let's say one of the things that you're cancelling for is the input into sewers. Well...

Q: But does it say mutual ... doesn't it say mutual in this agreement? It can't be unilateral then at all, can it?

A: Well, for a default--I'm talking about a default--the guy is defaulted. He was supposed to put in sewers by July 1, 1976 and didn't put it in; we got the loan; you try to cancel it. Okay. You cancel it in the middle of the winter; he says, "Well, I had trouble with the borough, etc., give me some more

time." You give him some more time. The lender doesn't know. I mean, he can't come in to really take over if you read literally .590. "Cause you can ... the lender can only come in and assume that lease if you cancel it. You never cancel, that creates an ambiguity that I think is unnecessary. So, what I try to write into my assignment forms is a provision talking about what happens if we take over by reason of foreclosure, judicial or non-judicial. Okay? In other words, the reality of the lending industry is we come in on foreclosure, not when you cancel the lease. And you don't--I'm saying you, but I mean the State of Alaska--never dresses that question.

Q: Is forfeiture ... it says forfeiture, too ... is that closer to default than ...

A: What does forfeiture mean? I mean, I don't know what... The word cancellation I understand. But, if you cancelled and forfeited the lease, how can you tell me to assume a lease that's not in existence? I mean that ... it's ... the language isn't even accurate. How can you assume you cancelled ...

Q: Well you have acquired. Let's say you've acquired the lease, so you acquired... I mean, whatever happens that lease goes back to the state, wouldn't you think that then you have a right to acquire that lease. Doesn't that... Who has it, then? Doesn't... It says you have the right to acquire... (Inaudible.)

A: I think we could agree that the words could be

more precise, without arguing the point.

Q: As far as curing the default, one of the things that is required of all leases in .510--58.510?

A: Um-hum.

Q: Is on use utilization. And, there it says that failure to make substantial use of the land (inaudible) within five years shall, on discretion, constitute cancellation.

A: Um-hum.

Q: I presume if you lose ... if you did lend money, though, you would make sure that there was ... it was going to be used for the purpose that it was applied so that, at least as far as Alaska Industrial Subdivision is concerned here, have you ever been concerned with anything other than payment of money for a ...

A: Yes, in fact we were concerned with that with the Penland development, and I was supposed to ...

Q: Well, I know that, but I was just wanting to talk about Alaska Industrial Subdivision.

A: No. Okay, well I...

Q: You have been concerned about...

A: It's the same kind of problem. Let me explain the problem. Ah, the land out there might have certain zoning restrictions or utilization restrictions. In other words, apart from the state there might be some zoning or some other restrictions placed on the land. Another problem we've had, like with the

Penland lease ... there's no provision for the ground lessor to file an estoppel agreement, although I always require it. I write it into the ground lease. I said in granting and approving this assignment the State of Alaska says there are no known defaults. You know, that's the only prudent thing to do, is make them commit themselves in writing that there aren't any. And I tell 'em to go ahead and check it, too. 'Cause we don't wanta' make the loan if there's defaults. And obviously we don't want the state, the day we fund a two or three million dollar loan, to come back and say, "We're cancelling the lease." Y'know.

Q: Are you aware at this time of any permanent action required of any lessee on a parcel of Alaska Industrial Subdivision lease (inaudible).

A: I'm not aware of any. I'm just suggesting that that's a problem and can be a problem. In other words, when I get a loan package from the bank, the bank says, "We're going to make X loan on this property, you put the paperwork together." So I, y'know, I'll go over to the state lease file and read it and talk to the state lease people, y'know the administrators of the program and say, "Do you know of anything wrong," and "What's your view of the project?" and, y'know, check with the borough, or the municipality, now.

Q: I really didn't understand that when you first explained, I think I do now.

A: Okay.

Q: One other thing related to that which you mentioned is preference and assignment lease form that is required to be used ... and you used the words required to use ... and then looking at .540, it does say that application for assignment shall be made in writing to the director on forms with the assignment of lease or attach a copy thereof. Now you have indicated that you have prepared a better assignment and have had that approved...

A: I'm not saying it's better, but at least...

Q: No, no, well I mean longer...

A: It was longer.

Q: It was more satisfactory to you?

A: Yes. More confortable, at least...

Q: Doesn't that seem to indicate that this DL-50, although it's called an assignment of lease is an application for the assignment; and, if it's approved it should reference something else, such as you or a private attorney might prepare to make it a better collateral assignment for that...

A: If you'd review the files that the lenders have filed you'd find a variety of attempts to solve this problem. And they vary. I mean, each bank has been different. All I'm trying to point out you is that that--if you read that regulation literally I suppose you could read that's all you could ever have in there. I've read it and add things that aren't otherwise covered in here. And, all I've advocated to the Governor's

Committee, and maybe even this panel, is that there has to be some flexibility in there to make what we call in lending make the lease bankable.

Q: There was... At least you were able to persuade ... corrected there was enough flexibility to make your (inaudible).

A: Well they, y'know, you give 'em to them, you don't argue with them. You say, "This is what we need to make the loan, you sign it." If they sign it I figure they're bound by it. But, you know, I recognize and advise the clients, well, they can argue the other way. The big thing in any real estate transaction--I think any attorney who does a lot of it will tell you--and this has been a big problem in Alaska. We have absolutely no certainty in our law or our procedures or our practices. You know. And that's what hurts Alaskans. We pay an extra penny, I mean an extra point in interest--not solely because of that, part of it is our isolation. But lenders have told me outside of this state. "Lookit. We're fifteen hundred miles away from you, we're based in Seattle--I'm talking about some of these big ones--and you people have no certainty in your law. Absolutely no certainty in your law or your procedures."

Q: And because of that it should be defined more specifically?

A: Yes. Yes, uh-huh. Sure. If the lender comes in and he feels comfortable with your procedures and practices, y'know. Then that's gonna' allow development. And if he doesn't feel comfortable, then I think it's going to be charged to him.

BY MR. MIDDLETON

Q: It's past noon already, and I'd like to complete Mr. Hoge's examination. I just really have one question. Ah, with respect to, ah, the rental provisions in the state leases. Ah, let's... And more particularly the one's that resulted from the reappraisal ... let's kind of draw, ah, make a hypothetical here. Ah, y'know, assume that there perhaps had been an under-valuation for the purpose of this question. That in fact the rental payments were lower than they should have been considering the standards that have been set up.

A: Um-hum.

Q: i.e., appraised value based on the fair market value, or appraised rental based on fair market value. Ah, and, then assume that there was ... there was what you might refer to as a correction of that, coupled with a tremendous jump in real estate values generally in a certain period of four or five years. Ah, would the bank be quite so concerned by the dramatic increase?

A: The answer is that they would always be concerned. Now, how adverse that would be would depend upon, ah, what the particular loan transaction was. If the transaction were one that, say there couldn't be a dramatic increase in rent necessarily... In other words, it depends on your lease. Some of these leases, ah, like a Safeway lease or that. The ones I've seen, they've got a base rent and they go on profits. Okay. I ... I mean

percentage of sales and volume. That, coupled with a dramatic increase of the underlying ground lease--and that is also reflective of another thing that's going up, is that the real property taxes presumably are going up. This is, I understand, although I got into this again with the parking garage. The municipality has a variety ... has used a variety of methods ... it's not legally committed to one over the other ... of evaluating these ground lease projects. Y'know. And that's a whole 'nuther area. But, to answer your question directly, Mr. Middleton, I think one, yes, it is of concern. Two, it depends on the project--how big a factor that would be.

Q: Well, what I'm... What I'm getting at is they all, look, they jumped this rental payment six, seven hundred per cent and, and, God knows, they're gonna' do it every five years. Y'know. When the truth of the matter may be, Gentlemen, that this is a one-time thing, resulting from, y'know, these two or three factors. Specifically a possible undervaluation. A tremendous jump in real estate prices, y'know. In other words, an increase in ... of the market value. And that in five years you may see ... you may see a reversion to the trend that--you weren't here-but the earlier trend in the rental adjustments was ... was substantial, but not in the neighborhood of six or seven hundred per cent. It was maybe fifty per cent over five years or something like that. People felt they could live with it.

A: Obviously that's a judgment thing, but I just

remember reading in the Alaska Land Lines, put out by the Division of Lands--a very good publication, I recommend that everybody get it--but, they were talking about the speech of the governor gave recently. And, I don't have the correct figures, but he was pointing out that of all the land in Alaska maybe one per cent is in private ownership. And then, I don't know what small per cent is in Anchorage. You know. And the trend that I see in Anchorage is everybody wants to live in Anchorage. Maybe people want to live in the capitol and the valley. Obviously, there's more development in that area. But, I don't ... I guess I don't see the trend that you might see, but you may be right, y'know. That it may normalize out. Maybe people will move to the other side of the inlet and develop their warehouses in other places. But I don't know that.

Q: Well, I'm just concerned that maybe the bank and the lenders ... the banks and the lenders are saying ... are getting nervous about a six or seven hundred per cent increase that may not be really something that can be projected as a trend. And they may get all nervous about this. Obviously, y'know, the provisions of the lease are there.

A: Yeah.

Q: And they're concerned about that. But, is it simply because this one time, you know, we've seen a really very, very dramatic increase?

A: Well, that could obviously be. But it is, y'know,

part of all of this is in Alaska--and I think this may have come out at the governor's committee the day I was there--y'know we accepted ... I'm sure banks made loans on these ground leases and never questioned them. They just ... things went along. The rental increases were always moderate, and you just accepted that as a way of life. Now, I think with the Penney matter, the Teamsters matter, this matter, and the general increased value, y'know, you've awakened the lenders and say, "Oh, we're not gonna' get in that." Y'know, whether itis gonna' go up or not, because you've gotta' say, "God, it went up six hundred per cent this time, is it gonna' go six hundred per cent again?" And I've, y'know ... I don't know that that's gonna' always happen. God, I hope not. I really do. But, ah, y'know the lenders gotta be saying, "What kind of people are we dealing with?" Y'know. If they can always change the rules, then you've taken out of lending--at least on state ground land--the certainty that you need. Especially when it's unsubordinated. That's what really hurts the lenders. If it was subordinated, then, y'know, the lender... The lender will always know he'll get his project back if the state ever pushes too hard on the rents. But, when he doesn't have that subordination, that ... that's where he's gotta' really have certainty. He's gotta' know what his relationship is.

Q: Alright, I don't have any more questions.

BY CLIFFORD GROH, ATTORNEY REPRESENTING INDIVIDUAL LEASEHOLDER

Q: Very, very quickly I would like (inaudible). But, Mr. Hoge, there's some discussion by the Attorney General about the benefit of the appreciation the lessee has because there's been an appraisal and then there's not another reappraisal for five years, there's a benefit to the lessee in some f shion. But there's really nothing the lessee can do with that appreciation, is there?

A: No, I ... I... In terms of a five-year term, there's not enough ... there's not enough time to get any benefit out of it.

Q: Well, he can't sell it. He can't buy it. He can endeavor to renegotiate his lease, if he's successful in doing so, but as you and I know it's a very difficult proposition.

A: It is difficult.

Q: Okay. Now, there has been some confusion in this hearing among some of us about the basic difference between a subordination and a so-called collateral assignment. And let's you and I see if we can straighten this up. Okay. In a subordination, what really happens is the lessor agrees that the lender may have the fee if the lessee defaults. Is that correct?

A: That's right.

Q: Okay. Now in an assignment, or a so-called "collateral" assignment, all that really happens is that the lessee assigns to his lender his ... gives the lender the right to cure

the default if there's a default?

A: That's true.

Q: And that is the basic difference?

A: Yeah. It's more dramatically. In one case on subordination the lender's getting the asset, and on an assignment he's really getting a liability, potentially.

Q: Right.

A: In other words, the potential liability is he'd have to cure the defaults, assume ... pay the rent on the ground lease.

Q: And any suggestion that the two things are equivalent just isn't, ah, legally correct?

A: No. No, they ... both in lending and law, they're about 180 degrees apart ... maybe not quite that.

BY MR. GISSBERG:

Q: Well, would you take one that had no subordination and no collateral assignment?

A: Well, you wouldn't ... I mean, you wouldn't be... Well, I'm sure the Controller of the Currency would be putting you in jail if you ever made a loan like that. I mean, you've gotta' have at least the assignment of the ground lease, unless you're a charitable institution, and banks, believe me, are not. I don't say that facetiously, they've gotta' make a profit. You don't... What you would be doing is saying, here, I'm gonna'

lend five million dollars. Build a building on this property. The state comes along and cancels the gound lease, gets the property. Even though they've got this permission that you can move the improvement in 30 days, but you're not gonna' remove a parking garage. You're not gonna' remove any kind of five million dollar building. So, in effect, the lender's made a charitable contribution, because he'll never get his building back, and he'll never get his security. He's gotta have at the minimal the collateral assignment, and much preferred is lease subordination. Much, much preferred.

Q: Could you have a subordination on the leasehold interest. That's the collateral assignment?

A: No, that's meaningless, because you'd still have the fee interest. I mean, that... You can have-there's another word for it that doesn't come to mind--a partial subordination thing, but it wouldn't be realistic, nor, I don't think, applicable in terms of what you're dealing with in state ground leases. In other words, the state either, y'know, the state probably is at this point not going to subordinate; and, if it's not going to subordinate, then it has to take care of these other problems.

Q: Is subordination always included in collateral assignments?

A: Ah, yeah, I've done one like that. "A" owns the fee. "A" leases to "B", a developer. Ah, developer "B" leases to "C". Well, you wouldn't have it in terms of the state ground

lease, but in that situation the developer will assign his tenant leases to the bank as security for the loan. Ah, the ground lessor may subordinate to the loan. Y'know, "A" will subordinate to the lender, and "B" will also be assigning his leases, but you wouldn't have it on the same lease, you'd have different leases in order to accomplish it.

MR. MIDDLETON:

Q: Okay, anything further? Thank you, Mr. Hoge.

A: Okay, thank you.

END OF TESTIMONY

ALASKA INDUSTRIAL SUBDIVISION LEASEHOLDERS ASSOCIATION

EFFECT OF SENATE BILL #159 ON MY PROPERTY LOCATED BLOCK 3, LOT 7A, ALASKA INDUSTRIAL SUBDIVISION. LOT SIZE APPROXIMATELY 64,000 SQ. FT. APPRAISED AT $65,640.00 TO BE REAPPRAISED 1978.

TERM	% INC TERM	% ORIG VALUE	NEW APPRAISED VALUE	LEASE PAYMENTS	ACCUMULATED COST TO LEASEE
1-10	0%	100%	$ 65,640.00	$ 52,512.00	$ 52,512.00
10-15	50%	150%	98,460.00	39,384.00	91,896.00
15-20	50%	225%	147,690,00	59,076.00	150,972.00
20-25	50%	337.5%	221,535.00	88,614.00	239,586.00
25-30	50%	506.25%	332,302.00	132,920.80	372,506.80
30-35	50%	759.38%	498,454.00	199,381.60	571,888.40
35-40	50%	1,139.07%	747,686.00	299.074.40	870,962.80
40-45	50%	1,708.61%	1,121,531.00	448,612.64	1,319,575.44
45-50	50%	2,562.92%	1,682,301.00	672,920.28	1,992,495.72
50-55	50%	3,844.38%	2,523,451.00	1,009,380.40	3,001,876.12

1. Above is MINIMUM
2. Rates are compounded
3. When lease finished, leasee will have paid 45.73 times value (3,001,876 ÷ 65,640)

ATTACHMENT "C"

BEFORE A HEARING PANEL OF
THE ALASKA DIVISION OF LANDS

In the Matter of Protests)
of Various Leaseholders in)
ALASKA INDUSTRIAL SUBDIVISION)

HEARING PANEL PROPOSED DECISION AND RECOMMENDATION

I

INTRODUCTION

Pursuant to a letter of November 2, 1976, written by Michael Smith, Director, Division of Lands, to lessees holding leases in the Alaska Industrial Subdivision, an administrative hearing was held December 14, 15, 20 and 21, 1976. The hearing was called to give the lessees an opportunity to protest the five-year reappraisal of certain state leases within the Alaska Industrial Subdivision, said reappraisal resulting in substantially higher annual rental payments. The hearing panel consisted of George Hollett from the Division of Lands; Kenneth Zamzow, an appraiser with the State Division of Petroleum Revenue; and Timothy G. Middleton, an attorney in private practice.

The Division of Lands (Division) was represented at the hearing by John Gissberg from the Attorney General's Office. Representing various leaseholders was Douglas Baily, and representing leaseholder Groh & Bankert, a partnership, was Clifford Groh.

Testifying as witnesses for the Division were Ronald Bunn, an appraiser with the Division; Robert Kesling, a forester with the Division; and Eugene Harp with the Department of Highways.

Testifying as witnesses for the lessees were Leon Brown, Jim Cristopher, Joe Wilhour, lessees; Fred Ferrara, and Errol Simmons, appraisers; John Kemper, a banker; Andrew Hoge, an attorney; and Paul Kimball from Lynden Transport, a lessee.

The relevant provisions of the lease form, regulations and statute are set out as follows:

(1) State lease provision calling for reappraisal:

> "[S]uch payments to be subject to adjustment at each five-year interval from the effective date hereof, if the lease term hereof exceeds five years, such adjustment to be based primarily upon a reappraised annual rental value of land in a state of improvement similar to that of the land described herein at the time this lease was entered into.

(2) Regulations governing rental: 11 AAC 58.520 and 11 AAC 58.410:

> 11 AAC 58.520. ADJUSTMENT OF RENTAL. All leases shall stipulate that the annual rental payment shall be subject to adjustment by the director at five-year intervals and any changes or adjustments shall be based primarily upon the reappraised annual rental value. The director shall take into consideration the following factors in reappraising the annual rental value: the value of comparable lands in the same or similar areas, exclusive of buildings, structures, appurtenances, equipment, land fill, clearing, leveling or roads owned by the lessee. The commissioner may waive one or more of the periodic rental adjustments or lengthen the reappraisal period, when a lessee who has acquired a tract of land for multiple unit housing, commercial, or industrial development can demonstrate to the satisfaction of the commissioner that such action is essential in order to obtain the primary long-term financing or loan insurance required for development of the leased land. In order to qualify, applicants must furnish written evidence that, in requiring a waiver of rental adjustment, the lending or insuring agency is applying a generally applicable rule. Waivers shall remain in effect only during the term of the loan but shall not exceed 40 years.
>
> 11 AAC 58.410. ANNUAL RENTAL. Annual minimum rentals shall be computed from the approved appraised market value, except in the case of a preference right grazing lease, and shall be the lowest acceptable bid in the event of an auction. Annual rental shall be the basis of bidding for

all surface leases, except as provided in sec. 440 of this chapter. Annual rentals in amounts up to and including $250.00 shall be paid on an annual basis. Annual rentals in amounts above $250.00 shall be paid either annually or in quarterly installments, at the discretion of the lessee. All rentals shall be paid in advance.

11 AAC 58.900. SHORT TITLE. This chapter pertains to the leasing of land of the State of Alaska and to the jurisdiction of the Division of Lands, Department of Natural Resources and related matters. The intent of this chapter is to insure the equitable leasing of Alaska land in a manner that will encourage development for its highest and best use. This chapter may be referred to as the "Surface Leasing Regulations."

(3) Statutory provision dealing with rental adjustments in effect as of May 1, 1976:[1]

AS 38.05.105. PERIODIC RENTAL ADJUSTMENTS. Each lease shall stipulate that the annual rental payment is subject to adjustment at five-year intervals and charges or adjustments shall be based primarily on a reappraised annual rental value. However, when development of the land is not otherwise possible due to special conditions, the reappraisal period may be lengthened or waived under regulations adopted by the commissioner.

Because the hearing panel is composed of an appraiser, lawyer and a representative of the Division of Lands, it is considered appropriate in formulating recommendations to the Director that the panel exercise independent judgment based on expert testimony presented and exhibits offered. Accordingly, we do not accord the Division's position any special deference which might be applied in an administrative appeal in the judicial process.

The basic question to be resolved in this hearing is the determination of a fair rental for certain lots within the Alaska Industrial Subdivision. This fair rental is to be determined for the five-year period May 2, 1976, through May 1, 1981, the third rental adjustment period since the leases

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[1]This section has since been amended, §1, Ch. 267 SLA 1976.

commenced on May 2, 1961. The Division had adjusted the annual rental of the leases in question as of May 1, 1976. This adjustment had been based on a reappraised fair market value and an increase in the rental rate from 6% to 8%. The reappraisal and adjustment were based on the relevant provision of the statute and regulations quoted above. Additionally, the term "fair market value" is defined in 11 AAC 58.910(11) as:

> "Fair market value" means the highest price, estimated in terms of money, which the property would bring if exposed for sale for a reasonable time in the open market, with a seller, willing but not forced to sell, and a buyer, willing but not forced to buy, both being fully informed of all the purposes for which the property is best adapted or could be used.

II

ISSUES

The issues appear to be the following:

(1) An interpretation of the lease, regulatory and statutory provisions, as to the nature of improvements to be included in the appraised value.

(2) Whether or not the term "primarily" as used in the lease, regulations and statute means that the Division should consider other factors in arriving at a reappraised annual rental value.

(3) Whether the Division's appraisal was in accord with the law and consistent with the relevant market conditions, particularly as to (a) use of comparables and (b) determination of original condition.

(4) Whether the 8% rental rate is appropriate in view of market conditions, the provisions of the state lease not found in private leases.

III

DISCUSSION

A. State of Improvements

The lessees represented at this hearing interpret the term "state of improvement" to mean the state of improvement of the entire Alaska Industrial Subdivision. Specifically, the lessees interpret this to mean that any improvements made outside of lot boundaries since 1961, such as roads and utilities, are to be excluded from consideration in the fair market value of the subject lots. The appraisals conducted by Messrs. Ferraro and Simmons for the lessees and presented at the hearing reflected adjustments in value to account for the cost of those improvements, particularly cost of access. This was based on language in the lease indicating value should be based on land in a similar state of improvement as land described in the lease at the time the lease was entered into; thus, the reference to "original condition." The regulations, however, are more explicit in determining what improvements are to be excluded. The Panel believes it would be inappropriate, in view of regulations and principles of equity, to exclude from the value of the leased property improvements off the property, especially when such improvements were paid for by the lessor. When a lessee can demonstrate that such off property improvement was paid for by him or his predecessor in interest, a different approach should be used. Both the State and the lessees agree that any improvements made within lot boundaries by lessees are to be disregarded in the valuation. The Panel finds in favor of the State in interpreting this phrase "state of improvement" to mean only the condition within the subject lots and that all improvements made since the leases were entered into which lie outside of the lot boundaries, specifically roads, water, sewer, power, and any other amenities

which affect the value of the subject lots are to be included in the fair market value of those lots.

A further disagreement among the parties involving the "state of improvement" is that of the original condition of the lots before any tenant improvements were made. The State's appraisal witness, Mr. Bunn, testified that as far as he could determine after reference to soil maps, aerial photos and consultation with various knowledgeable individuals, that the soils were basically adequate for building development with a minimum of site preparation required for any development, that no substantial amount of overburden needed to be removed. Mr. Bunn admitted his findings in this regard were based largely on the lack of evidence to the contrary. He did not, apparently, attempt to gather evidence from individuals who developed the leased land. Several other witnesses testified as to moderate to severe conditions of peat and unstable soil conditions at the time the leases were originally entered into. The lessees' appraisers, Mr. Simmons and Mr. Ferrara, after thoroughly investigating the original soil conditions with various knowledgeable people indicated that it was still not clear exactly what the soil conditions were on each parcel. There was adequate testimony given that most, if not all, of the subject lots had conditions of unstable peat soils in depths ranging from one to four feet, with testimony given concerning individual spots where the depth of peat extended 14 feet. In Mr. Ferrara's appraisal of Lot 4, Block 2; Lot 12, Block 10; Lot 10, Block 9; Alaska Industrial Subdivision, he stated that soil conditions probably varied from two to three feet of overburden along Commercial Drive on the north with overburden deepening in the area of Rampart Drive and reaching depths of two to three feet

again along Mt. View Drive. Mr. Ferrara testified that although he was uncertain as to the actual soil conditions at the time the leases were entered into, he felt a realistic condition was that approximately two feet of fill was required on the average for development of those lots which he estimated would cost, at the time of reappraisal, $.50 per square foot. Mr. Simmons' appraisal report and testimony regarding soil conditions were similar to those of Mr. Ferrara. In Mr. Simmons' appraisal of Lots 8 and 30, Block 10, he estimated a current cost of surcharging the peat with gravel in an amount adequate to support parking and storage yards was $40,000, which divided by total site area of 46,021 square feet equals $.87 per square foot. In the Panel's opinion, the investigation and analysis by the lessees' two appraisers were reasonably well supported and much more creditable than the investigation, analysis and testimony given by the Division.

B. Meaning of Primarily

The lessees contended that because the lease, regulation and statute all use the adverb "primarily" to modify the verb in, "such adjustment to be based primarily upon a reappraised annual rental value," that the State should consider other factors in arriving at an annual rental value. The lessees point to 11 AAC 58.900 wherein the intent of the regulations is spelled out, i.e., to "insure equitable leasing" to "encourage development." Accordingly, the lessees presented evidence, unrefuted by the Division, of the difficulty in obtaining financing for development of the leaseholds.

The Division's position was that the word meant nothing now with respect to the leases under question, but that it referred to the since repealed provisions for waiver

of five-year adjustments in cases where such a waiver is necessary to obtain long-term financing. The Division stressed the point that the lessees never attempted to obtain the waiver. The Panel finds the Division's argument to be without merit. First of all, the word "primarily" applies, if at all, to the reappraisal. The waiver would mean there would be no reappraisal at all. The suggestion that the lessees should have attempted to get the waiver is also without merit. The date of the reappraisal was May 1, 1976; the date the waiver repeal became effective was June 22, 1976. Assuming that the lessees had notice of the reappraisal simultaneously with the reappraisal, there would be only six weeks in which to get the waiver after reappraisal. The lessees indicated such actual notice of reappraisal came much later, in June and July; this was not rebutted. It is also unrealistic to believe that the State would have agreed to such a waiver.

The word "primarily", taken along with 11 AAC 58.900, is not without meaning. The Panel believes that the Division should consider other factors besides a determination of open market rent. The present state of the lease and regulations makes it difficult to arrive at a readily ascertainable meaning, especially in view of the duty owed to the people of Alaska by its government to obtain a good return from the State land. While principles of legislative interpretation dictate that the word be given meaning, the Panel finds it difficult to do so. Because nothing was presented to resolve this dilemma, the Panel refrains from attempting a definition beyond suggesting that doubts or ambiguities be resolved in favor of the lessee.

C. Appraisal.

11 AAC 58.410 states that annual minimum rentals shall be computed from the approved appraised market value. Rent paid for land in the open market place is typically determined by, and expressed as, a percentage of the market value of the land. Therefore, a reasonable estimate of the fair market value of the land in question must first be made before a market rent can be derived. The generally accepted method of appraising vacant land, and that which was used by all three appraisal witnesses, is the direct market comparison approach. All three of the appraisal witnesses utilized definitions in 11 AAC 58.810(11), and 11 AAC 58.520 regarding the use of comparable land sales. All three appraisers used the same basic techniques in adjusting comparable land sales for differences in comparison with the subject lots. The major factors for which adjustments were made were for increase in price levels between the dates of sale and the date of appraisal, neighborhood location, specific location (corner or inside lot, street improvements, utilities available, zoning, etc.), and physical characteristics of the comparables, including such things as soils, topography, shape and easements. As the panel finds that offsite improvements made since 1961, specifically water, sewer, power and road improvements are to be included in arriving at the fee market value of the land, the Panel addressed itself to the major points of disagreement between the State and the lessees' appraisers which are adjustments for time increment, neighborhood and an electrical transmission line easement.

(1) Time Adjustment

All three appraisal witnesses agreed that a rapidly rising trend of price levels for industrial land was evident

during the two-year period prior to the appraisal date of May 2, 1976. Mr. Bunn testified his conclusion was that a time increment of 3.5% per month was appropriate; both Mr. Ferrara and Mr. Simmons concluded a time increment of 2% per month was appropriate. Mr. Bunn used 10 comparable sales which indicated a range of time increment from 2.8% per month to 4% per month. One example which tended to limit Mr. Bunn's testimony in this regard was where he compared the sale of one parcel with a later sale of another parcel to arrive at an indication of time trend. Mr. Bunn did not adjust for other factors but compared the two sites as equal in value when actually one of the sale sites had much less utility than the other due to its very odd shape. Also, Mr. Bunn utilized sales in a faster growing area of Anchorage (South Anchorage) in arriving at a time adjustment. The Panel believes a reasonable upward adjustment for time increment to be 2% per month. This belief is based on the fact that Ferrara and Simmons used sales of property more likely to reflect accurately the increase in value in the Mountain View area. The Panel finds the lessees' appraisers more persuasive on this point.

(2) Neighborhood Locations.

Mr. Bunn used 18 comparable land sales with two from the immediate Mountain View area, two from the Anchorage Industrial Park in the Ship Creek area and 14 in the South Anchorage area in the vicinity of International Airport Road. Mr. Bunn's testimony was that the Alaska Industrial Subdivision is comparable in location to the other industrial areas of Anchorage, that price levels for industrial land was similar and that no adjustments were required for