One Lincoln Street (A)

After more than six months of seemingly daily e-mails, conference calls, and presentations, John Hynes still couldn't believe what he was hearing on the other end of the phone from Frank Mattson, a Real Estate Investment Officer for Midwest State Teachers Retirement System ("STRS").

> "Wait a minute. I *know* it looks like a good deal. But John, I've tried to be clear from the start: we're a public pension fund. Our policies are we only invest in fully entitled land and, even then, we don't build on spec. We need at least 25% pre-leasing. And I still want to talk to you about that residual profit split.
>
> All I can say right now is get me those revised unlevered cash flows and maybe I can bring the issues up at the Investment Committee meeting this week. But don't get too optimistic – we learned our lesson the last go-round, and it wasn't pretty.
>
> I've got to get home for dinner or my kids are going to forget my name. I'll be in early tomorrow. Thanks, partner."
>
> "O.K. then, Frank, I guess we'll talk in the morning. Bye."

As he released the call from his speaker phone, John Hynes muttered angrily:

> "Spare me that partner crap, please! *Partners* take *risks.*"

John knew his discussions with Frank needed to evolve. He just worried that he didn't have much time.

Context

John B. Hynes, III was the Senior Vice President and Principal in charge of the Boston office for Gale & Wentworth LLC ("G&W"), a diversified real estate investment and services firm. Gale & Wentworth owned approximately 12 million square feet of suburban office properties and provided fee-based services to another 17.5 million square feet of such product. Gale & Wentworth had offices in seven states and the United Kingdom, employing over 350 people.

This case was prepared by W. Tod McGrath for the purpose of class discussion. The case describes an actual situation, but in the interests of confidentiality, certain names and other identifying information have been changed. The situation described herein is not intended to illustrate either effective of ineffective handling of a fiduciary situation. Revised October 2003.

John Hynes was G&W's newest addition to its senior management team. A lifelong Bostonian and real estate professional, John was transitioning from a successful career in commercial brokerage back to one centered on real estate investment, development, and management. John had been there before. From 1983 to 1992, he directed Lincoln Property Company's Boston office as its Operating Partner and developed approximately 850,000 square feet of office space in Boston and Chelsea, Massachusetts.

John's primary responsibility at G&W was to use its resources and network of relationships to expand its presence in the Boston office market. John knew that the principal resource available to him was the $50 million in capital that had recently been raised in MSGW III, G&W's latest opportunity fund co-sponsored with Morgan Stanley Real Estate. Similar to its two predecessor funds, MSGW III had been launched to acquire (with leverage) about $200 million of "value added" real estate (i.e., largely empty buildings in improving markets). Levered investment returns were targeted at about 25%, down considerably from the 40%+ returns achieved in MSGW's first fund.

G&W had recently finished investing MSGW II, the second opportunity fund it co-sponsored with Morgan Stanley. This fund was subscribed in 1997 with $50 million of equity and, somewhat unexpectedly, became fully invested in a single transaction with the levered acquisition of a national portfolio of office properties known as the Chubb Portfolio.

John was well aware that it had become increasingly difficult to find existing investment opportunities that both matched MSGW III's investment objectives and could deliver the targeted level of investment returns. In many respects, the Boston market as of mid 1999 didn't seem to offer a great deal of promise in terms of opportunistic investing. Over the past 5 years, the vacancy rate for Class A & B space in the City of Boston had dropped from 13% to less than 4% and asking rental rates had more than doubled (Exhibit 1). John knew he was late to the party, but also felt that a dynamic metro area such as Boston would continue to offer smart investment opportunities over time.

Others thought so, too. That's how John came to meet Frank Mattson.

STRS

From the standpoint of commercial real estate investment, STRS was one of the most progressive public pension plan sponsors in the country. Unlike most of its peers, STRS had made a conscious decision to internally staff its real estate investment function as opposed to outsourcing such responsibilities to third-party pension investment managers. More significantly, perhaps, STRS was willing to venture a little further out on the risk/reward frontier than most other plan sponsors.

But STRS appetite for risk was buffered by a strategic decision to concentrate their investment in only about 10 MSAs nationwide. The rationale for such concentration stemmed from the practical requirements of both internal management efficiency and depth of external investment resources (i.e., joint venture partners) in the private property markets.

To be blunt, in order not to be preyed upon in the quirky and inefficient private real estate equity markets, STRS Real Estate Investment Committee wanted to make sure they were aligning themselves only with the most reputable partners and only in those markets with the most depth, stability, and transparency. STRS had come to regard Boston as one of those markets.

As of mid 1999, STRS commercial real estate portfolio had a market value in excess of $5.5 billion and funding commitments for another $700 million. Although the portfolio was generally well diversified across property types, geographic regions, and investment structures, Frank Mattson believed that additional investment exposure to the higher cost, supply-constrained Northeast property markets was desirable. As he continued to follow the rapid escalation of rents and asset values in the Northeast, he began to more formally explore investment opportunities in Boston, both for STRS on its own and with selected joint-venture partners. Early in 1999, G&W had been recommended to him as a possible source for investment opportunities by his contacts at Morgan Stanley Real Estate, with whom STRS had previous investment experience. Frank Mattson wasted no time in calling for a meeting with John Hynes, and soon the two were scavenging the Boston metro area looking for deals.

Unfortunately, after many months of search and due diligence, neither had identified a prospective investment that met their objectives. For John, "opportunistic" acquisitions seemed to be ancient history; for Frank, "core" investments in fully-leased office buildings were generating initial unlevered cash returns of only about 7.0% to 7.5% (Exhibit 2) and expected unlevered IRRs in the 9.0% to 9.5% range. Frank was more than a little dismayed to find that even 30 year old buildings (with a host of issues related to functional obsolescence) were trading at cap rates in the 7.50% to 7.75% range.

A strong appetite to invest, enthusiasm for the Boston market, and an underwhelming array of acquisition opportunities: it was no surprise that Frank and John's discussions quickly turned to development.

The 4% vacancy rate in Boston's downtown office market had prompted five new office developments totaling approximately 2.7 million square feet to break ground in time for tenants to take occupancy between 2000 and 2002 (Exhibit 3). These five developments included:

- World Trade Center East
- World Trade Center West
- 10 Saint James Avenue
- 470 Atlantic Avenue
- 111 Huntington Avenue

Across these five developments, approximately 1.7 million square feet (60%) had been pre-leased and the remainder was in high demand by a dozen or so legal, financial services, and professional services firms which were strapped for available expansion space. Recently signed leases were generally in the $50.00 to $60.00 per rentable square foot range. Based on the nature of development timelines in Boston, it was pretty clear that the next wave of available supply couldn't be delivered until 2003 or 2004. What seemed to be holding the other proposed developments back from a groundbreaking was a combination of inadequate entitlements and pre-leasing commitments.

John believed that the next building to break ground would have a first-mover advantage that would effectively cause the remaining proposed developments to stop and watch. While Frank certainly wasn't prepared to base his investment strategy on that premise, he did feel strongly that each of the other proposed developments would need significant amounts of equity capital to move forward and, in some cases, additional development expertise. After carefully reviewing the location, development program, and sponsorship of each of the remaining development opportunities, One Lincoln Street quickly emerged as the front runner in terms of a realistic investment opportunity.

One Lincoln Street

One Lincoln Street was a proposed 36-storey office development located in the Financial District of downtown Boston on a site bordered by Lincoln, Bedford, Kingston, and Essex Streets. The development program consisted of approximately 1 million rentable square feet of office space, 15,000 rentable square feet of retail space, some below-grade storage space, and a five-level underground parking garage totaling 345,000 square feet with 725 parking spaces (parking for 900 cars with valet service). The development was projected to cost approximately $330 million if built on an "all cash" basis (Exhibit 4).

The development was ostensibly controlled by Columbia Plaza Associates ("CPA"), a minority-owned development consortium which had originally received developer designation for the project by the Boston Redevelopment Authority ("BRA") back in the late '80's. More specifically, the BRA had awarded CPA the right to acquire two parcels of land owned by the City of Boston. The first parcel was the 27,000 square foot site of the nearly condemned Kingston-Bedford Public Parking Garage located on the northern half of the block bounded by Bedford, Kingston, Essex and Columbia Streets. The second parcel was an adjacent 20,000 square foot surface parking lot. The acquisition of two other privately-owned parcels of land totaling approximately 16,000 square feet was needed to complete the development plan.

But all of that was supposed to have happened a decade ago. The city was now growing increasingly frustrated, and it had conveyed its frustration to CPA. Understanding the political realities of the need to show progress and, perhaps more importantly, as a condition to the extension of CPA's designation as developer, CPA had recently entered into a preliminary joint-venture agreement with a local Boston developer who was responsible for arranging the debt and equity financing for the project as well as the acquisition of the privately-owned land parcels. But none of those development milestones had been achieved and John had just been able to confirm with city officials that the preliminary joint-venture agreement previously approved by the BRA was set to expire within 30 days. That's all he needed to hear.

John immediately called the managing partner of CPA and asked if they could meet. Unfortunately, he was rather clinically informed that, under the terms of its existing joint-venture agreement, CPA was precluded from discussing any aspect of ownership in the proposed development with any other party. John wasn't exactly sure what that meant − and he wasn't exactly sure that he cared. Within 72 hours of his phone call with CPA, he had flown to New York and put the two privately-owned parcels under agreement for $22 million. The terms of sale were simple: $2 million upon execution of the purchase and sale agreement (which was fully refundable within the negotiated 30-day "due diligence" period) and the remaining $20 million at closing, which was also scheduled to occur in 30 days.

John knew that control of the privately-owned land parcels was essential to the proposed development becoming a reality. Without that site area, the land assemblage was inadequate for large-scale development. No one knew that better than CPA. John also knew that the BRA would be hesitant to even threaten to use its power of eminent domain in order to complete the assemblage for CPA. They'd had that chance for over a decade, and never bit.

As the purchase and sale agreement was being executed, John placed his second call to CPA, this time introducing himself as their new partner. He followed that call with one to Frank Mattson, suggesting that he may have found what they were looking for.

A few weeks passed and the preliminary joint-venture agreement between CPA and their local development partner expired. It was August of 1999. Within a matter of days, John had reached agreement with both CPA and his money source, MSGW III, to conditionally move forward with the project subject to the approval of the Mayor of Boston and the BRA Board.

<u>Morgan Stanley</u>

Investment approvals from MSGW were ultimately granted by Morgan Stanley Real Estate − guys who liked to ask a lot of questions. Question number one to John was something like:

> "You don't really think we're going to go hard on a dollar without all the approvals, do you?"

John smiled nervously but assured them that he fully understood the investment objectives of MSGW III and that the necessary approvals would be in place before the due diligence period expired. Another phone call was quickly placed; this time to the mayor's office. John needed a meeting, and fast.

Two weeks remained before the due diligence period expired. Everything seemed to be moving forward (as well as could be expected) until John received a call from the Mayor's office informing him that, while the Mayor would support the project moving ahead, the Director of the BRA had suddenly resigned and the BRA Board meeting scheduled for later that week would need to be postponed for at least another two weeks. Breathing somewhat anxiously into his cell phone, John placed a call to the owner of the private land parcels. Twenty minutes later, he had negotiated both an extension of the due diligence period until the day after the rescheduled BRA Board meeting and an extension of the closing date until the end of the year. Price tag: $500,000 plus a $2 million contingent purchase payment if lease commitments for 250,000 square feet of space in the new development were executed within 12 months of the closing. Simple enough.

His next call was to his partners at Morgan Stanley. He updated them on his various discussions and politely reminded them that G&W had invested 10% of the capital ($5 million) into MSGW III and that there was no way they could realistically move forward on the deal without going hard on the $2 million deposit after the BRA Board vote. As John had painfully become aware, the venture still needed a handful of miscellaneous city (and state) permits in order to break ground. The good news was that the Mayor had agreed to try to expedite the issuance of all remaining permits by the closing of the purchase and sale agreement. The mayor had an obvious incentive to cooperate; the acquisition of the city-owned parcels had been negotiated to occur on the same day. Price tag: $15 million, half payable at closing, half payable approximately three years thereafter upon certificate of occupancy for the first tenant.

After listening to John's pitch, reviewing the pro forma financial information relating to the operations of the development (Exhibit 5), and reflecting on the real estate investment climate in downtown Boston, Morgan Stanley not only signed on to going hard on the $2 million deposit, but funding for an additional $5 million of required design, professional, and permitting costs as well. And all by years end. John ended the call feeling a strange mix of elation and dread. Although he got the green light to proceed, Morgan Stanley not-so-politely reminded him that no more than 50% of the equity raised in their fund could be invested in any one asset.

John immediately thought of his new buddy Frank.

Venture Structure

After a few perfunctory meetings and conference calls, John cut to the chase and proposed the following deal structure to Frank for his review and recommendation to STRS Real Estate Investment Committee.

- A new joint-venture between MSGW, STRS and CPA would be formed to undertake the development. The venture would initially fund equity capital in an amount equal to the greater of $175 million or 50% of the total development cost. The remaining capital required to complete construction and lease-up would be borrowed under a construction loan with a commercial lender. Upon maturity of the construction loan, the venture would likely (although not necessarily) redeem it with additional equity.

- Of the equity capital required, MSGW would contribute 10% and STRS would contribute 90%. CPA had no obligation (or desire or ability) to contribute additional capital to the venture. In fact, as part of its understanding with John, CPA was entitled to a $5 million reimbursement at closing for previous expenditures made and services performed since the late '80's.

- MSGW and STRS would each receive an annually compounded 11% cumulative preferred return[1] on their invested equity capital. Once such preferred returns were paid, MSGW, STRS, and CPA would receive 34%, 51%, and 15%, respectively, of any remaining cash flows. STRS would control a majority of the voting interests in the venture.

- Construction and permanent financing commitments would be approved by STRS in its sole discretion.

The bottom line was that Frank liked what he heard, both from a financial and managerial (control) standpoint. Frank had previously stressed to John the importance that STRS placed, for example, on the monitoring role an experienced construction lender performed during the construction period. He was pleased that John had wisely offered up − without posturing or pretense − exclusive approval rights to STRS on all project financings. After all, STRS was putting up 90% of the equity.

With regard to requiring the use of a construction lender during the construction stage, Frank realized he would have to review the cash flow impact of such use on the development and operating budgets. He also knew from recent experience that the venture would be required to expend available equity capital on project expenditures prior to draws being approved by the construction lender under the construction loan. The venture would also have to guarantee completion of the development to the construction lender.

Frank conservatively expected to be able to negotiate a construction loan with a term-to-maturity of up to four years, quarterly interest-only payments, and a fixed interest rate no higher than 8%, compounded quarterly. He estimated that the construction lender would charge $2 million in fees at closing and would require an additional $200,000 per year of direct expense reimbursement for inspections during the three-year base building construction period. John had previously provided Frank with an annual and quarterly breakdown of expected construction period expenditures on hard construction and soft development costs (<u>Exhibit 6</u>), which Frank assumed would occur ratably throughout each quarter. With that information in hand, Frank prepared a pro forma construction loan disbursement and interest schedule (<u>Exhibit 7</u>).

That essentially left Frank needing to do what he liked to do best: calculating and evaluating the expected cash flows and investment returns from the venture to each venturer in accordance with the proposed distribution priorities. Although Frank already felt comfortable with the development and operating budgets John had prepared for the property, he knew he

[1] Cumulative preferred returns, in this context, are calculated similar to the way cumulative preferred dividends are paid on preferred stock. Specifically, MSGW and STRS must each be paid 100% of the 11% preferred return payable on their respective equity investments before any return (cash distribution) is paid to CPA; in addition, MSGW and STRS are each entitled to receive the full repayment of their cumulative equity investment (including any earned but unpaid preferred return thereon) from the proceeds of the sale of the development before any payment is made to CPA. MSGW and STRS are entitled to such return preferences on a *pari passu* basis.

would need to make a few assumptions regarding capital events and related market-based investment parameters. In particular, Frank assumed that

- The property could be sold at the end of its tenth year of stabilized operations for a price equal to its then current net operating income capitalized at 7.5%. Frank reasoned that in Year 10 (not unlike in the Boston market at the time), the owner of the property would likely be on the verge of receiving significant increases in base rental revenues through lease renewals at market rental rates. Using a 7.5% capitalization rate to arrive at an expected sale price for the property seemed to be as good a guess as any, particularly in light of current market conditions.

- Transaction costs for an asset this size would be no more than 1.25%.

Frank understood that, for presentation purposes to STRS Real Estate Investment Committee, he would principally focus on the expected unlevered cash flows and investment returns (IRRs) both to the venture as a whole and to STRS individually. Analyses of potential levered investment returns would not be presented because he was uncomfortable trying to forecast permanent financing rates four years into the future. Moreover, one of the committee members was a real estate academic who undoubtedly would feel the need to comment on both the appropriateness of investing on a levered basis and any estimation of future interest rates. Frank was aware that permanent financing rates for current 10-year fundings to properties that meet conventional loan underwriting criteria were in the 7.5% range, about 200 basis points over 10-year Treasury Bonds and about 300 basis points over 90-day Treasury Bills.

But Frank also understood that the proposed investment in One Lincoln Street was more than just a little different than what STRS had seen in a while. Even for an institution that prided itself on taking the long view of real estate investment, four years of consecutive cash outflows was a long time indeed. He mused that, for any number of reasons, he might not even be around to see it completed.

But that got Frank thinking, from a practical standpoint, about when and how STRS could get out of the deal and what the project might be worth upon construction completion and lease-up. He figured he should be prepared to discuss those issues since they seemed particularly relevant for this investment. He also knew that if he were inclined to recommend the investment for approval, he would have to step off the curb and justify it from the standpoint of it adequately compensating STRS for bearing the risks associated with both construction and lease-up.

Even though he knew the venture would obtain a guaranteed maximum price contract from their chosen general contractor, their construction lender would require a completion guarantee that would, in all likelihood, devolve into negotiations over the venturers guaranteeing individual line item costs in the development budget. Frank knew that based on the magnitude of the overall construction budget, STRS would have to be the front line guarantor on the construction loan. Frank also knew that STRS would require significant backup guarantees from Morgan Stanley (corporately) for certain budgeted line items, and that Morgan Stanley would in turn require Gale & Wentworth to provide certain backup guarantees. After all, it was G&W who sourced the deal and who had presumably vetted the thousands of assumptions that went into it. John had already informed Frank that $5 million of G&W's $9 million share of the budgeted development fees were being proposed to be deposited into escrow accounts to ensure performance under its guarantees. Frank wondered whether or not Morgan Stanley would feel that was enough.

Regardless, he knew he needed to give the issue of risk-adjusted investment returns a lot more thought in order to formalize his analyses and recommendations. He needed to think hard about how to price construction and lease-up risk in real estate development.

Update

It was September 1999. In the afternoon before the regularly scheduled monthly Real Estate Investment Committee meeting, Frank's assistant pulled him out of a staff meeting and informed him that John Hynes was on the phone and needed to talk.

John had just gotten off the phone with Morgan Stanley and Morgan Stanley had given him an ultimatum of sorts. It seemed that Morgan Stanley was getting a bit uncomfortable with the thought of carrying through with the development phase. By their calculations, they would need to invest in excess of $40 million over the next few months in order to close on the City-owned and privately-owned land parcels and to pay CPA and the venture's permitting, design, and legal consultants. In the context of managing MSGW III in the near term, that was becoming a problem.

But the guys at Morgan were smart, although maybe too smart from John's perspective. Their message to John was simple: get STRS, or someone else, on board right now to fund 90% of the equity requirements of the development or the day after the closing on the land parcels they were going to flip the site with its as-is entitlements to a large Boston-based REIT they had recently done some investment banking work for. Price tag: $60 million. Morgan told John – unequivocally − that they were prepared to execute such an agreement within 60 days. They also gratuitously reminded John that, as their partner, G&W could pocket their share of the profits if they did decide to sell. John wasn't interested in selling.

So John's message to Frank was equally simple: STRS had 15 days to get investment committee approval for the deal and 45 days to completely document the transaction. In addition, assuming that all of the entitlements were in place at the time of the land closings, there would be no pre-leasing contingencies or other thresholds to be met that would permit STRS to defer funding its 90% equity share. They didn't have time for that. STRS was either in or out. Welcome to the real world of high stakes real estate development.

Crunch Time

Frank had personally invested a lot of time looking at this deal. And he realized that even if his analyses supported a recommendation to pursue it, he would still have to be particularly persuasive to gain Investment Committee approval the following day. They hadn't even considered a deal like this for over a decade.

The thought of having to prepare both his analyses and remarks in one evening started to make him feel a bit anxious. And it really didn't help to have John jump off the call saying,

> "I've got to get home for dinner or my kids are going to forget my name. Get back to me tomorrow as soon as you can and tell me how the meeting went. And, Frank, I wouldn't even think about coming back to me on that residual profit split. It is what it is.
>
> Hey, partner, remember: pre-leasing is for sissies."

Exhibit 1

Boston Office Market: Statistical Overview

		Annual Change			Annual Change			Annual Change			Annual Change			Class A	Class B
Year	Class A Supply	Sq.Ft.	%	Class B Supply	Sq.Ft.	%	Total Supply	Sq.Ft.	%	Occupied Space	Sq.Ft.	%	Vacancy Rate	Asking Rents PSF	Asking Rents PSF
1975	14,166,000	3,813,000	36.8%	380,000	15,000	4.1%	14,546,000	15,000	0.1%	12,328,000	15,000	0.1%	15.2%	$14.00	$6.50
1976	15,406,000	1,240,000	8.8%	753,000	373,000	98.2%	16,159,000	1,613,000	11.1%	13,816,000	1,488,000	12.1%	14.5%	$12.00	$6.50
1977	16,465,000	1,059,000	6.9%	847,000	94,000	12.5%	17,312,000	1,153,000	7.1%	15,105,000	1,289,000	9.3%	12.7%	$12.00	$6.50
1978	16,465,000	0	0.0%	1,388,000	541,000	63.9%	17,853,000	541,000	3.1%	16,157,000	1,052,000	7.0%	9.5%	$14.00	$6.50
1979	16,465,000	0	0.0%	1,766,000	378,000	27.2%	18,231,000	378,000	2.1%	17,092,000	935,000	5.8%	6.2%	$16.00	$8.00
1980	16,465,000	0	0.0%	2,590,000	824,000	46.7%	19,055,000	824,000	4.5%	18,388,000	1,296,000	7.6%	3.5%	$20.00	$10.00
1981	17,475,000	1,010,000	6.1%	3,914,000	1,324,000	51.1%	21,389,000	2,334,000	12.2%	20,373,000	1,985,000	10.8%	4.8%	$22.00	$12.00
1982	17,612,000	137,000	0.8%	5,506,000	1,592,000	40.7%	23,118,000	1,729,000	8.1%	22,309,000	1,936,000	9.5%	3.5%	$25.00	$16.00
1983	17,812,000	200,000	1.1%	6,493,000	987,000	17.9%	24,305,000	1,187,000	5.1%	23,394,000	1,085,000	4.9%	3.7%	$30.00	$22.00
1984	21,722,000	3,910,000	22.0%	7,884,000	1,391,000	21.4%	29,606,000	5,301,000	21.8%	26,201,000	2,807,000	12.0%	11.5%	$35.00	$24.00
1985	22,491,000	769,000	3.5%	8,825,000	941,000	11.9%	31,316,000	1,710,000	5.8%	28,341,000	2,140,000	8.2%	9.5%	$38.00	$26.00
1986	22,641,000	150,000	0.7%	12,154,000	3,329,000	37.7%	34,795,000	3,479,000	11.1%	31,316,000	2,975,000	10.5%	10.0%	$42.00	$26.00
1987	24,280,000	1,639,000	7.2%	13,187,000	1,033,000	8.5%	37,467,000	2,672,000	7.7%	33,720,000	2,404,000	7.7%	10.0%	$44.00	$28.00
1988	27,510,000	3,230,000	13.3%	14,577,000	1,390,000	10.5%	42,087,000	4,620,000	12.3%	36,195,000	2,475,000	7.3%	14.0%	$50.00	$30.00
1989	28,220,000	710,000	2.6%	15,091,000	514,000	3.5%	43,311,000	1,224,000	2.9%	36,381,000	186,000	0.5%	16.0%	$55.00	$30.00
1990	30,085,000	1,865,000	6.6%	15,894,000	803,000	5.3%	45,979,000	2,668,000	6.2%	38,048,000	1,667,000	4.6%	17.2%	$40.00	$25.00
1991	30,335,000	250,000	0.8%	16,022,000	128,000	0.8%	46,357,000	378,000	0.8%	37,549,000	(499,000)	-1.3%	19.0%	$30.00	$20.00
1992	30,835,000	500,000	1.6%	16,077,000	55,000	0.3%	46,912,000	555,000	1.2%	38,937,000	1,388,000	3.7%	17.0%	$25.00	$18.00
1993	31,585,000	750,000	2.4%	16,077,000	0	0.0%	47,662,000	750,000	1.6%	40,465,000	1,528,000	3.9%	15.1%	$26.00	$18.00
1994	31,585,000	0	0.0%	16,077,000	0	0.0%	47,662,000	0	0.0%	41,466,000	1,001,000	2.5%	13.0%	$27.00	$20.00
1995	31,005,000	(580,000)	-1.8%	16,172,000	95,000	0.6%	47,177,000	(485,000)	-1.0%	42,223,000	757,000	1.8%	10.5%	$30.00	$24.00
1996	31,005,000	0	0.0%	16,422,000	250,000	1.5%	47,427,000	250,000	0.5%	43,870,000	1,647,000	3.9%	7.5%	$34.00	$26.00
1997	31,585,000	580,000	1.9%	16,305,000	(117,000)	-0.7%	47,890,000	463,000	1.0%	45,017,000	1,147,000	2.6%	6.0%	$40.00	$30.00
1998	31,585,000	0	0.0%	16,305,000	0	0.0%	47,890,000	0	0.0%	45,903,000	886,000	2.0%	4.1%	$50.00	$34.00
1999	32,185,000	600,000	1.9%	16,595,000	290,000	1.8%	48,780,000	890,000	1.9%	46,951,000	1,048,000	2.3%	3.7%	$60.00	$35.00

Exhibit 2

Boston Office Market: Recent Building Sales

Building	Year Built/ Rehabbed	Floors	Net Rentable Area	Sale Date	% Leased	Buyer	Seller	Price	Price/SF	Cap Rate
One Boston Place	1970	41	779,000	Dec-99	95%	Gerald Hines Interests	Lend Lease	$200,000,000	$257	7.75%
99 High Street	1971	32	731,000	Dec-99	99%	Boston Capital	Keystone-Centrose Associates	168,500,000	231	7.71%
75 State Street	1988	31	770,000	Oct-98	100%	World Financial Properties	Lend Lease	311,000,000	404	7.40%
745 Atlantic Atlantic	1987	11	168,000	Oct-99	100%	Lend Lease	Tishman Speyer	39,500,000	235	7.00%
399 Boylston Street	1983	13	255,000	Nov-98	90%	CentreMark	Met Life	52,000,000	204	7.50%
265 Franklin Street	1985	20	329,000	Apr-99	100%	Westbrook Ptrs / Divco West	Shuwa Investments	70,000,000	213	7.70%
260 Franklin Street	1985	23	349,000	Jan-00	100%	Heitman / State of Florida	JMB / TIAA	76,000,000	218	7.00%
125 High Street (1)	1990	30	1,438,000	May-99	100%	Jamestown	Tishman Speyer	496,600,000	345	7.75%
116 Huntington Avenue	1990	15	261,000	Jun-99	100%	IDX Partners	IDX	55,200,000	211	6.95%
100 Summer Street	1974	32	1,020,000	Mar-98	80%	Equity Office Properties	Blue Cross Blue Shield / Emerik	225,000,000	221	7.50%
Totals / Averages			6,100,000					$1,693,800,000	$278	7.43%

Note: (1) 76% ownership interest.

Exhibit 3

Boston Office Market: Development Pipeline

Building	District	Developer	Net Rentable Area	Status	Leased Space	Completion Date	Delivery of New Supply 1999	2000	2001	2002	2003	2004	2005
Lafayette Corporate Center	Financial	Amerimar	600,000	Under Constr.	600,000	1999	600,000						
Landmark Center	Fenway	Abbey Group	950,000	Under Constr.	750,000	1999	950,000						
World Trade Center East	Seaport	Drew / Fidelity	500,000	Under Constr.	500,000	2000		500,000					
10 Saint James	Back Bay	Millenium	585,000	Under Constr.	450,000	2001			585,000				
470 Atlantic Avenue	Financial	Modern Cont.	335,000	Under Constr.	0	2001			335,000				
111 Huntington Avenue	Back Bay	Boston Properties	850,000	Under Constr.	550,000	2001			850,000				
World Trade Center West	Seaport	Drew / Fidelity	500,000	Under Constr.	175,000	2002				500,000			
One Lincoln Street	**Financial**	**Gale & Wentworth**	**1,000,000**	**Proposed**	**0**	**2003**					**1,000,000**		
Seaport Center	Seaport	Chiofaro	500,000	Proposed	500,000	2003					500,000		
Two Financial Center	Financial	Rose Associates	250,000	Proposed	0	2003					250,000		
131 Dartmouth Street	Back Bay	Sullivan & Assoc.	350,000	Proposed	0	2003					350,000		
33 Arch Street	Financial	Krulewich	600,000	Proposed	0	2004						600,000	
700 Boyston Street	Back Bay	Boston Properties	150,000	Proposed	0	2004						150,000	
650 Atlantic Avenue	Financial	Hines / Tufts	1,250,000	Proposed	0	2005							1,250,000
One Fan Pier	Seaport	Pritzger / S&S	750,000	Proposed	0	2005							750,000
Total New Supply			9,170,000		3,525,000		1,550,000	500,000	1,770,000	500,000	2,100,000	750,000	2,000,000
Preleased							1,350,000	500,000	1,000,000	175,000	500,000	0	0
% Preleased							87%	100%	56%	35%	24%	0%	0%

Exhibit 4

ONE LINCOLN STREET

DEVELOPMENT BUDGET

	Line Item Cost	Cost Per Sq.Ft. of GBA	Cost Per Sq.Ft. of NRA	% of Total Cost
SITE ACQUISITION:				
BRA Parcel	$15,000,000	$13.95	$14.79	4.5%
O'Connor Parcel	24,500,000	22.79	24.16	7.4%
CPA Entitlement Cost Reimbursement	5,000,000	4.65	4.93	1.5%
Legal (Due Diligence)	250,000	0.23	0.25	0.1%
Legal (Closing, Title Insurance, Misc.)	600,000	0.56	0.59	0.2%
Total Site Acquisition	**45,350,000**	**42.19**	**44.72**	**13.7%**
HARD CONSTRUCTION COSTS:				
Base Building: Guaranteed Maximum Price	162,975,000	151.60	160.70	49.3%
Tenant Improvements	55,335,000	51.47	54.56	16.7%
Window Coverings	250,000	0.23	0.25	0.1%
Allowance for Common Corridors	1,000,000	0.93	0.99	0.3%
Parking Garage Equipment	100,000	0.09	0.10	0.0%
Abutter Improvement Allowance	500,000	0.47	0.49	0.2%
Bell Atlantic Conduit Relocation	1,700,000	1.58	1.68	0.5%
Building Security Equipment	250,000	0.23	0.25	0.1%
FF&E / Interior Artwork	500,000	0.47	0.49	0.2%
Landscaping	500,000	0.47	0.49	0.2%
Total Hard Construction Costs	**223,110,000**	**207.54**	**219.99**	**67.5%**
SOFT DEVELOPMENT COSTS:				
Architectural & Engineering	7,200,000	6.70	7.10	2.2%
Space Planning	300,000	0.28	0.30	0.1%
Construction Coordination Website	270,000	0.25	0.27	0.1%
Building Permit	1,600,000	1.49	1.58	0.5%
Other Permits	100,000	0.09	0.10	0.0%
MEPA EIR, Consulting Fees	200,000	0.19	0.20	0.1%
Builder's Risk Insurance	525,000	0.49	0.52	0.2%
Bonds to City	250,000	0.23	0.25	0.1%
Testing & Inspections	800,000	0.74	0.79	0.2%
Legal (Contracts)	75,000	0.07	0.07	0.0%
Legal (Approvals)	350,000	0.33	0.35	0.1%
Legal (Leasing)	1,000,000	0.93	0.99	0.3%
Leasing Commissions	8,113,000	7.55	8.00	2.5%
Real Estate Taxes During Construction	2,500,000	2.33	2.47	0.8%
Advertising & Marketing	1,000,000	0.93	0.99	0.3%
Linkage & Public Benefits:				
Neighborhood Housing Trust	1,900,000	1.77	1.87	0.6%
Neighborhood Jobs Trust	852,000	0.79	0.84	0.3%
Chinatown Childcare	1,250,000	1.16	1.23	0.4%
Dudley Street Initiative	50,000	0.05	0.05	0.0%
Community Development Fund	10,000,000	9.30	9.86	3.0%
Owners's Representative	200,000	0.19	0.20	0.1%
Development Fee: CPA	1,500,000	1.40	1.48	0.5%
Development Fee: G&W	9,000,000	8.37	8.87	2.7%
Contingency	13,000,000	12.09	12.82	3.9%
Total Soft Development Costs	**62,035,000**	**57.71**	**61.17**	**18.8%**
TOTAL DEVELOPMENT COSTS	**$330,495,000**	**$307.44**	**$325.87**	**100.0%**

Exhibit 5

ONE LINCOLN STREET

PROJECTED NET OPERATING INCOME AND CASH FLOW FROM OPERATIONS

($ in Thousands)

Calendar Years Ending:	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Base Rental Revenue	$53,141	$53,141	$53,141	$53,141	$53,141	$54,435	$56,008	$58,012	$60,425	$60,425	$66,309
Absorption and Turnover Vacancy	(21,736)	0	0	0	0	(3,477)	0	(3,939)	0	0	(3,568)
Scheduled Base Rental Revenue	31,405	53,141	53,141	53,141	53,141	50,958	56,008	54,073	60,425	60,425	62,741
Operating Expense Reimbursement	120	434	716	1,007	1,306	1,399	1,468	1,461	1,419	1,766	1,151
Real Estate Tax Reimbursement	120	434	716	1,007	1,306	1,399	1,468	1,461	1,419	1,766	1,151
Parking Garage Revenue (net)	4,000	5,000	5,150	5,305	5,464	5,628	5,796	5,970	6,149	6,334	6,524
General Vacancy	0	(2,950)	(2,986)	(3,023)	(3,061)	(3,143)	(3,237)	(3,345)	(3,471)	(3,514)	(3,757)
Effective Gross Income	35,645	56,059	56,737	57,437	58,156	56,241	61,503	59,620	65,941	66,777	67,810
Operating Expenses	(9,128)	(9,401)	(9,683)	(9,974)	(10,273)	(10,582)	(10,899)	(11,226)	(11,563)	(11,910)	(12,267)
Real Estate Taxes	(9,128)	(9,401)	(9,683)	(9,974)	(10,273)	(10,582)	(10,899)	(11,226)	(11,563)	(11,910)	(12,267)
NET OPERATING INCOME	**17,389**	**37,257**	**37,371**	**37,489**	**37,610**	**35,077**	**39,705**	**37,168**	**42,815**	**42,957**	**43,276**
Tenant Improvements	(55,335)	0	0	0	0	(7,496)	0	(8,478)	0	0	(9,096)
Leasing Commissions	(4,057)	0	0	0	0	(1,874)	0	(2,119)	0	0	(2,326)
Capital Reserve	(152)	(157)	(161)	(166)	(171)	(176)	(182)	(187)	(193)	(198)	(204)
PROPERTY BEFORE-TAX CASH FLOW	**($42,155)**	**$37,100**	**$37,210**	**$37,323**	**$37,439**	**$25,531**	**$39,523**	**$26,384**	**$42,622**	**$42,759**	**$31,650**

Exhibit 6

ONE LINCOLN STREET

CONSTRUCTION PERIOD FUNDING SCHEDULE

	2000	2001	2002	2003	Totals
Base Building Costs	$14,430,000	$79,200,000	$65,350,000	$3,995,000	$162,975,000
Tenant Improvements				55,335,000	55,335,000
Other Hard Construction Costs	2,200,000			2,600,000	4,800,000
Linkage & Public Benefits	4,326,000	426,000		9,300,000	14,052,000
Leasing Commissions		4,056,000		4,057,000	8,113,000
Developer Fees	2,140,000	2,188,000	2,203,000	3,969,000	10,500,000
Other Soft Development Costs	13,684,000	6,996,000	5,725,000	2,965,000	29,370,000
Total Funding Requirements	**$36,780,000**	**$92,866,000**	**$73,278,000**	**$82,221,000**	**$285,145,000**

SUPPORTING QUARTERLY DETAIL

Quarter	Base Building	Tenant Improvements	Other Hard Construction	Linkage & Public Benefits	Leasing Commissions	Developer Fees	Other Soft Development
2000.1							4,983,000
2000.2	2,030,000			3,150,000		525,000	3,574,000
2000.3	3,146,000		500,000	1,126,000		525,000	3,106,000
2000.4	9,254,000		1,700,000	50,000		1,090,000	2,021,000
2001.1	16,005,000				1,014,000	525,000	1,478,000
2001.2	18,047,000				1,014,000	525,000	1,623,000
2001.3	19,424,000			426,000	1,014,000	525,000	1,816,000
2001.4	25,724,000				1,014,000	613,000	2,079,000
2002.1	19,912,000					525,000	1,734,000
2002.2	20,223,000					525,000	1,398,000
2002.3	14,851,000					525,000	1,467,000
2002.4	10,365,000					628,000	1,126,000
2003.1	1,701,000	32,960,000	1,623,000		1,014,000	525,000	896,000
2003.2	1,134,000	4,421,000	457,000	6,800,000	1,014,000	525,000	734,000
2003.3	673,000	5,181,000	386,000	1,500,000	1,014,000	525,000	691,000
2003.4	486,000	12,773,000	134,000	1,000,000	1,015,000	2,394,000	644,000
Totals	**$162,975,000**	**$55,335,000**	**$4,800,000**	**$14,052,000**	**$8,113,000**	**$10,500,000**	**$29,370,000**

Exhibit 7

ONE LINCOLN STREET

CONSTRUCTION PERIOD INTEREST SCHEDULE

Gross Construction Period Equity Funding	$175,000,000
Less Site Acquisition	(45,350,000)
Less Financing & Inspection Fees	(2,600,000)
Less Construction Loan Interest	(16,312,000)
Net Construction Period Equity Funding	110,738,000

Annual Construction Interest Rate	8.00%
(compounded quarterly)	

Quarter	Beginning Debt Balance	Required Funding	Equity Funding	Debt Funding *	Interest Expense	Interest Paid	Ending Debt Balance
2000.1	$0	$4,983,000	$4,983,000	$0	$0	$0	$0
2000.2	0	9,279,000	9,279,000	0	0	0	0
2000.3	0	8,403,000	8,403,000	0	0	0	0
2000.4	0	14,115,000	14,115,000	0	0	0	0
2001.1	0	19,022,000	19,022,000	0	0	0	0
2001.2	0	21,209,000	21,209,000	0	0	0	0
2001.3	0	23,205,000	23,205,000	0	0	0	0
2001.4	0	29,430,000	10,522,000	18,908,000	189,000	(189,000)	18,908,000
2002.1	18,908,000	22,171,000	0	22,171,000	600,000	(600,000)	41,079,000
2002.2	41,079,000	22,146,000	0	22,146,000	1,043,000	(1,043,000)	63,225,000
2002.3	63,225,000	16,843,000	0	16,843,000	1,433,000	(1,433,000)	80,068,000
2002.4	80,068,000	12,119,000	0	12,119,000	1,723,000	(1,723,000)	92,187,000
2003.1	92,187,000	38,719,000	0	38,719,000	2,231,000	(2,231,000)	130,906,000
2003.2	130,906,000	15,085,000	0	15,085,000	2,769,000	(2,769,000)	145,991,000
2003.3	145,991,000	9,970,000	0	9,970,000	3,020,000	(3,020,000)	155,961,000
2003.4	155,961,000	18,446,000	0	18,446,000	3,304,000	(3,304,000)	174,407,000
		$285,145,000	$110,738,000	$174,407,000	$16,312,000	($16,312,000)	

* Assumed To Occur Ratably Throughout the Quarter.