

Bald Head Island Transportation Authority

Responses to LGC Staff Review of NKF's valuation for Deep Point Terminal dated 7-26-2021

- 1) NKF appears to review slightly different set of parcels than the Worsley report. NKF report page 41 lists total of 54.6 acres for Deep Point and Worsley report page 1 lists 52.6 acres. At \$1.35 per sq. ft., 2 acres would have a value of \$117,612. At \$15 per sq. ft for "usable land" classification, 2 acres would have a value of \$1,307,000.

Response: NKF was instructed to include 2.2 acres of additional land in the parking area. At the time of the Worsley report, this additional acreage was not contemplated to be part of the proposed transaction. However, subsequent to the Worsley report, the Authority negotiated with the Seller and obtained Seller's agreement to include this additional acreage in the proposed transaction at no additional cost to the Authority.

- 2) NKF Cost approach numbers on the various schedules do not tie (pgs. 59-61). There appears to be missing items, possibly for Site Improvements (bulkhead items), when compared to the listing of "Improvements to Land" as found on page 62 of the Worsley report. The table at the top of page 61 in the NKF report does not total to the number at the bottom of the column.

Response: In response to inquiries from the Authority regarding the tables contained on pages 59-61 of the Deep Point report, NKF informed the Authority that pages 59-61 of the report contained tables with old data which mistakenly had not updated at the time the report was finalized. NKF explained that the sources of the data in those tables (i.e., within the underlying Excel spreadsheets) had been updated at the time of the final report, and therefore the "Cost Approach Conclusion" table at the bottom of page 61 is accurate and properly reflects the appraiser's conclusion. However, the inadvertent failure to incorporate the updated tables into the final report caused confusion.

NKF has now provided the Authority, and the Authority has provided LGC staff and the public, a corrected appraisal report dated August 31, 2021. This report updates the data in the tables on pages 59-61 which, in turn, form the basis for the data in the "Cost Approach Conclusion" table at the bottom of page 61. But, as noted by NKF, the "Cost Approach Conclusion" table itself, and the opinions evidenced by it, remain unchanged.

The Authority hopes that these revisions to the tables on pages 59-61 will address the questions raised above.

- 3) When comparing numbers that were provided in answer to question 2 in the Responses to Questions document (7/6/2021) provided by the Authority with the numbers in the NKF valuation (pgs. 59-61), the difference is approx. \$8 million. See below for the Revision to table from page 3 of the Responses document. Note this assumes the same valuation for the Bulkhead improvements.

Response. See the "Table Comparing Book Value, Worsley Appraised Value and NKF Appraised Value" below for an updated table with revised numbers from the NKF appraisal.

In assisting the Authority with this table, the NKF appraiser noted that while it recognizes that the LGC asked for the comparison to book value, the book value of the assets on the books of the current owner is not relevant to an appraisal, as the appraiser is charged with looking at the current value. In that process, the appraiser evaluates the replacement cost of the assets and

estimates depreciation based on both the actual age of the improvements as well as its observations regarding the current condition of those improvements.

- 4) Answer to Question 3 in the Responses document is “See New Appraisal”. Under Assumptions and Limiting Conditions section (p. 71) in the NKF report, Item #4 has the same assumption that was the basis for Question 3. Question remains unanswered.

Response. In response to this question, NKF noted that it not an auditor or a forensic accountant. Instead, in accordance with the standards set out in the Uniform Standards of Professional Appraisal Practice (“USPAP”), it relies on information provided to it in the normal course of an appraisal. The assumptions and limiting conditions contained in its appraisal, as in the Worsley appraisal, are based on and consistent with the USPAP.

- 5) Answer to Question 4 in the Responses document is “See New Appraisal”. New appraisal uses the same 15% mark-up for Entrepreneurial Profit with no explanation of the concept or the basis. In the Worsley valuation, the mark-up under the cost approach was 10% for indirect and 15% for Developer’s profit. In NKF, the mark-ups were 20% and 15%, indirect costs and entrepreneurial profit, respectively. A 10% difference for the indirect costs translates to an 11.5% compounded increase. On a total of \$14,369,518 for replacement costs before indirect and profit factors, the difference translates to \$1,652,494 in additional estimated replacement cost.

Response. The NKF appraiser pointed out that under the USPAP, in performing the cost approach, the appraiser is charged with determining the current cost of reproducing or replacing the asset, minus an estimate for depreciation, plus the value of the land, plus an entrepreneurial profit if the appraiser believes it appropriate. In this instance, the NKF appraiser indicated that in determining the replacement cost of the assets, based on his experience with other projects, he included the indirect costs necessary to shepherd a project through the development process. NKF’s estimate is based on likely higher costs for obtaining the necessary permits and developing a waterfront project which would exceed those of an inland project. Similarly, the estimate of the entrepreneurial profit as part of the total cost was based on its experience with build-to-suit projects regionally as well as discussions with developers.

The Authority notes that both appraisers included entrepreneurial profit in the calculation of the replacement cost of the assets. This was not an instruction given by the Authority, but rather the determination by both appraisers that inclusion of a profit component was appropriate in determining the replacement cost of these assets, consistent with the USPAP standards. The appraisers were not asked to determine what the purchase price of these assets should be when sold from this seller to this buyer, but rather, what the market value of this real property would be if sold in an arms-length transaction in the marketplace.

- 6) Answer to questions 6, 7, 8 & 24 in the Responses document is “See New Appraisal” – NKF valuation uses a new set of comparables and makes various adjustments for location, size, etc. but does not provide specific details as to why those adjustments were made. General comments on the adjustments can be found on page 58 of the NKF report.

Response. First, NKF did provide details as to why it made various adjustments to the comparables in the appraisals – in the Deep Point appraisal, on page 54 relating to the parking, and on page 57 relating to the Terminal and Barge, and in the Bald Head Island terminal appraisal, on pages 51-52. Additionally, NKF has stated that the adjustments used in the values are based on the appraiser’s experience and expertise as well as a comparison of the individual

comparables to the extent that different elements of comparison can be isolated and an adjustment can be extracted. The appraiser noted that in a pure sense, if there are two properties that were otherwise identical with the exception of the element the appraiser is trying to isolate, then the difference between the two unit values would be the magnitude of the adjustment. For example, if one parcel were 5 acres and sold for \$36,000 per acre and a 10 acre parcel sold for \$30,000 per acre, the difference for size would reflect a 20% premium for a 5 acre parcel over an otherwise similar 10 acre parcel.

NKF stated that, given the multitude of differences between each of the comparables, it reviewed the data and extracted reasonable estimates of the impact of the various elements of comparison.

- 7) In the NKF valuation using the Income Capitalization approach, the computation of the market rent is based on a depreciated cost plus land (excluding profit and capex) of \$30,900,000 (p.63). Where does this number come from? It does not tie to the Replacement Cost Approach numbers on pages 59-61 Those numbers conclude a cost of \$33,900,000. This starting number is crucial as it estimates the "Market Rent"/"Return on Cost number" that is then termed the Newmark Projection (p.64) for Net Operating income. The NOI estimate divided by the capitalization rate of 7.25% results in the \$31,800,000 valuation. This valuation appears to be directly a result of the initial estimate of cost.

Response. NKF informed the Authority that the \$30,900,000 is derived by taking the total Depreciated Replacement Cost of the assets other than the land (\$23,964,416) on page 61, backing out the 15% profit (which results in depreciated cost of \$20,818,860) and then adding the value of the Land (\$10,080,000), for a total cost of **\$30,898,860**, which it rounded up to **\$30,900,000**.

- 8) The LGC asked the Authority to update the table provided by the Authority in its initial response to question number 2 of the LGC's questions about the Worsley appraisal – that is, Worsley's appraisal valuation compared to the book value, depreciated based on useful life of the assets.

Response: The Authority has updated the table previously provided to the LGC to include information from the NKF appraisals. The table on the following page provides a list of the buildings and other improvements at Deep Point and at the Bald Head Island Terminal, including cost and depreciated value in 2020, which information was provided by the Seller, and the values on a building by building basis from the Worsley appraisals in 2019. The assessed value was derived from the 2021 tax bills, which were based on the values determined in the 2019 assessment. The values for the NKF column were derived by taking the Replacement Cost New information on page 59 of the NKF report for Deep Point (before indirect cost or entrepreneurial profit) and subtracting the percentage depreciation for those assets from page 61; a similar methodology was used for the Bald Head terminal property, using information from pages 53 and 54 of the Bald Head terminal report.

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Table Comparing Book Value, Worsley Appraised Value and NKF Appraised Value

<u>Asset Description</u>	<u>Seller's Cost</u>	<u>Seller's Book Value¹</u>	<u>Worsley Value²</u>	<u>Brunswick County Assessed value</u>	<u>NKF Value³</u>
DP Maintenance Building	\$ 775,836	\$ 464,081	\$ 375,196		\$ 182,314
DP Main Ferry Terminal Building	\$ 8,261,654	\$ 5,152,506	\$ 7,408,260		\$ 7,128,249
DP IT Server Room Building	\$ 88,051	\$ 66,508	\$ 41,138		\$ 36,803
DP Warehouse/shipping and receiving	\$ 1,271,645	\$ 775,258	\$ 425,840		\$ 341,947
Parking Booths	\$ 67,372	\$ 11,351	\$ 12,516		\$ 5,501
Deep Point - All Buildings	\$ 10,464,558	\$ 6,469,704	\$ 8,262,950	\$ 2,060,640	\$ 7,684,814
DP Docks, Piers and Bulkheads ⁴	\$ 3,025,310	\$ 349,650	\$ 2,338,750		\$ [see total below]
DP Site Improvements	\$ 4,364,988	\$ 1,410,535	\$ 7,670,833		\$ [see total below]
DP Site Total Site Improvements including Bulkheads, Docks and Piers	\$ 7,390,298	\$ 1,760,185	\$ 10,009,583	\$ 1,101,210	\$ 9,670,841
Deep Point - Land	\$ 299,022	\$ 299,022	\$ 10,520,000	\$ 7,101,380	\$ 10,080,000
Deep Point Total (Buildings, Total Site Improvements and Land)	\$ 18,153,878	\$ 8,528,911	\$ 28,792,533	\$ 10,263,230	\$ 27,445,655
Bald Head Island Docks, Piers and Bulkheads ⁴	\$ 1,887,676	\$ 226,998	\$ 687,500		\$ [see total below]
Bald Head Island Site Improvements	\$ 423,199	\$ 163,467	\$ 150,625	\$ 39,870	\$ [see total below]
BH Island Total Site Improvements including Bulkheads, Docks and Piers	\$ 2,310,875	\$ 390,465	\$ 838,125	\$ 39,870	\$ 491,537
Bald Head Island Terminal Land⁵	\$ 175,383	\$ 48,085	\$ 234,208	\$ 170,420	\$ 466,778
(Less required Deferred Maintenance and External obsolescence (NKF only))					\$ (1,122,815)
BH Island Terminal Total (Terminal, Total Site Improvements and Land)	\$ 2,486,258	\$ 438,550	\$ 4,802,333	\$ 3,710,630	\$ 6,135,500

¹ The book value column reflects cost less depreciation, including accelerated depreciation on some assets, as permitted under applicable accounting treatment. The placed in-service dates for various assets that makeup these categories date back as far as the late 1980s.

² The Worsley value column uses cost less assumed depreciation as shown in the Worsley appraisals, and does not include the 10% for indirect costs or 15% for developer's profit that Worsley included in his overall cost model.

³ The NKF values were calculated by taking the Replacement Cost New (before indirect cost or entrepreneurial profit) and subtracting the assumed depreciation percentage contained in the NKF appraisal for those assets.

⁴ The Worsley appraisal and the NKF appraisal included different assets in these two categories; the NKF appraisal includes docks, piers and bulkheads in "site improvements." Therefore, only a total of all assets other than land and terminal buildings were included for the NKF appraisal column.

⁵ The Bald Head Island Terminal numbers (Cost and Book) do not include a value for land.