**MINUTES**
**SPECIAL COMMISSION MEETING**
**THE PORT OF PORTLAND**
**March 22, 2007**

In response to due notice, the special meeting of the Commissioners of the Port of Portland was held at 12:00 p.m. in the St. Helens Conference Room at Portland International Airport.

**<u>QUORUM</u>**

Commissioners present were Jay Waldron, President, presiding; Ken Allen; Steve Corey; Bruce Holte; Judi Johansen; Mary Olson; Bill Thorndike; Junki Yoshida and Grant Zadow. Also present were Bill Wyatt, Executive Director; participating staff members; members of the public; representatives from Zimmer Gunsul Frasca (ZGF) Partnership; Grubb & Ellis; Cost Technology and Hoffman Construction.

**<u>ACTION ITEM</u>**

<u>Agenda Item No. 1</u>

GROUND LEASE – THE BOEING COMPANY

This agenda item requested approval to enter into a new lease and ramp management agreement with The Boeing Company. The initial term of the new lease will begin April 1, 2007, and expire March 30, 2022, unless terminated earlier, with an option to extend for an additional eight years.

Ken Anderton presented the Executive Director's recommendations as follows:

> BE IT RESOLVED, That approval is given to enter into a new lease and ramp management agreement with The Boeing Company, on the terms and conditions described herein; and
>
> BE IT FURTHER RESOLVED, That the Executive Director or his designee is authorized to execute the necessary documents on behalf of the Port of Portland Commission in a form approved by counsel.

Commissioner Johansen commended everyone involved for a job well done; she said it is wonderful the way this agreement came about.

Mr. Wyatt acknowledged the extraordinary work by Port staff, outside counsel Barbara Jacobson and our soon-to-be new partners and tenants at Boeing. He said this came together very quickly; it is an immensely complex proposition because we were negotiating a long-term lease for a facility we did not actually own, but is on our property.

Commissioner Waldron echoed Commissioner Johansen and Mr. Wyatt's comments. He said in his eight years on the Commission, this is by far the finest example of Port staff making lemonade out of lemons.

Commissioner Johansen moved that the Executive Director's recommendations be approved. Commissioner Allen seconded the motion, which was put to a voice vote; Commissioners Allen, Corey, Holte, Johansen, Olson, Thorndike, Waldron, Yoshida and Zadow voted in favor of the motion.

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## HQP2 COMMISSION WORKSHOP

Mr. Wyatt said we began talking about the headquarters (HQ) and second parking garage (P2) project a year ago. He said there is a strong business case to build the second parking garage, which has been included in the PDX Master Plan for quite some time.

Mr. Wyatt said with respect to a new headquarters building, it is important to understand the primary motivation for putting this on the table. In 2004, both K-Line and Hyundai discontinued their container service in Portland. Because containers play such a significant role in our general fund revenues, the loss of the two carriers had a profound and immediate impact on the general fund. The decision was made to address this forthrightly by eliminating 81 positions in the administrative staff. The net effect was close to an $8-million reduction in expenses in the General Fund.

Mr. Wyatt said it was this traumatic experience that started him and Steve Schreiber thinking about a better way to handle revenue losses in the future, and they came up with the idea of consolidating the administrative organization. Mr. Wyatt said over the past decade, the Port has experienced phenomenal growth in the commercial aviation side of its operations. This shift is evident in the Port's operating revenues, assets, capital spending and staffing levels.

Mr. Wyatt noted this is not a commentary on our marine franchise, which is very strong. Because we are the operators of the airport, the people who are most directly involved with airport operations need to be on-site at PDX, and if we are going to combine the administrative offices, it has to be at the airport. Mr. Wyatt said the only way he felt he could justify a consolidation was to demonstrate that, at the end of the day, the Port as an institution would be better off financially than if we did not make the decision.

Mr. Wyatt said when we conclude today, he would put together a final recommendation to be presented at the April Commission meeting. He said he would be meeting with Port staff on March 25 to let them know what his recommendation is going to be. He said this is both an important decision for the Port and a very personal decision for our employees.

### Business Case Review

Steve Schreiber discussed the key business drivers for the HQP2 project, including: insufficient general fund resources to fund business needs and long-term liabilities; opportunity to reduce or stabilize operating expenses to maintain competitiveness and long-term financial viability; opportunity to gain efficiencies and improve the effectiveness of Port staff through consolidation; significant growth in PDX business activity; and insufficient office space at PDX that will require the construction of new space in approximately five to seven years.

Mr. Schreiber provided an overview of the Port's financial structure and the differences between the airport funds and the General Fund. He also reviewed the working capital balance forecast, operating revenue, capital expenditures, capital assets and FTEs.

Commissioner Waldron asked about the utilization of the current headquarters in terms of space and employees. Mr. Schreiber said the building is under-utilized and if we could move people around, one floor would be vacant.

Mr. Schreiber discussed the key financial factors of the project, including: sale value of current headquarters and reinvestment earnings, cost of building additional space at PDX for Aviation-related growth, operational savings and cost of new headquarters building.

**Real Estate Analysis**

David Squire, Grubb & Ellis Senior Vice President, and David Hill, Grubb & Ellis Vice President, led a discussion of the evaluation of the current Port headquarters building.

Mr. Squire provided an overview of the current downtown office market, which he said is very competitive. He said it is a strong sellers market; there is a limited supply of office space and the demand should push vacancy further. He also said rental rates will likely spike over the next two years.

Mr. Hill said investor demand is at an all-time high; whether it is small investment properties or large institutional properties, there has been a shift of interest in buying real estate. He noted that Class A office buildings are highly sought after and the prices per square foot are at historical highs.

Mr. Hill said they looked at four options the Port could undertake: sell the building vacant to an owner/user in 2010; sell the vacant building to an investor; retain the property as an investment; or sell the property to an investor in 2008 with a Port leaseback. Mr. Squire discussed the pros and cons, pricing and risks associated with the four options. He said the option to sell the building to an owner/occupant when the Port vacates is the best possible scenario. The building is set up to be a single-tenant building and an owner/user could potentially pay a premium because they do not have to pay real estate commissions, and assuming the building suits them, they do not have to spend as much money adapting the building and they do not have the risk of finding tenants. Mr. Hill said the challenge is that the buyer pool is limited. He did a search of sales of 50,000 square feet and larger since 2003, and there were only two that went to owner/users.

The recommendation from Grubb & Ellis is to see if the Port can capture the user market and see if there is a tenant out there willing to pay a premium. Mr. Hill recommended a two-phase approach. Phase I would be to market the property to an owner/user. Grubb & Ellis would prepare an offering package, identify and vigorously pursue all owner/users of 50,000-100,000 square feet and determine viability within 120 days. Phase II would be to market the property to an investor with a Port sale/leaseback. Grubb & Ellis would prepare an investment-offering package and then launch a city, regional and national marketing campaign.

Commissioner Johansen asked why we would not pursue Phase I and II at the same time. Mr. Bach said the Phase II interested parties are already here; they are already calling. We know they are out there but if we can get a higher price from a user, we need to pursue that.

**PDX Space Requirements and Uses**

Mary Maxwell, Aviation Director, provided an overview of PDX office space and the additional space needed within five to seven years. She discussed the estimated future cost to construct space in the terminal, which would be approximately $37.6 million in 2014 ($19.6 million in today's dollars). Ms. Maxwell also discussed options to reuse the current administrative office space, should the Commission decided to move forward with HQP2. She said the federal government or a federal agency could use some of the space. Ms. Maxwell said the Transportation Security Administration (TSA) has an office building outside of the airport, and we would like them to have better access to the terminal. Ms. Maxwell said another use for some of the space is a fitness center, which they have always wanted for the airport, but for which they never had enough space. She said this would be an important amenity for employees, passengers and the public.

Ms. Maxwell said since 9/11, TSA continues to tighten down employee access to the secured areas, so there is greater demand for space pre-security where employees do not have to go through screening. With a reasonable lease-up time, she is confident they would be able to lease all the space, primarily to current tenants. Ms. Maxwell said that currently the Port does not pay rent to the airlines for our occupancy, so any revenue generated from the space will go to the airline cost center and help offset their costs of occupancy.

Commissioner Waldron asked Ms. Maxwell for her best guess as to what the odds are that we would be able to lease all the space in some manner similar to what she just described. Ms. Maxwell said within five years the space would be absorbed.

**Operational Analysis**

Mr. Schreiber said our original projections estimated a $3-million annual cost savings as a result of consolidation. Given that this is one of the key financial factors, we wanted an independent verification of our estimates and asked Peter Turney, President of Cost Technology, to assist us with this evaluation. Cost Technology works with a wide variety of organizations to help identify and capture costs savings. Mr. Schreiber said we have used Cost Technology on other projects at the Port and have actually been able to capture those savings based on the work that was done.

Mr. Schreiber said we did not have the time or resources to evaluate every area of the Port, so we selected representative processes to test whether or not savings could be achieved with consolidation.

Mr. Schreiber said we do have experience in this regard and referenced the reduction in force in 2004, which was business driven and done in a relatively short period of time. He said the reduction was an indication that we do have the ability as an organization to focus, create a plan and actually execute it. Mr. Wyatt said we do not intend to initiate any layoffs associated with the consolidation of the headquarters. The plan is to identify areas for savings and then capture them as opportunities develop to do so.

Peter Turney, President of Cost Technology, provided a brief overview of StorySolve, the method used as a way of understanding, evaluating and measuring processes so they can calculate the potential impact of consolidating the Port. Cost Technology evaluated two areas: records files management and project management.

Mr. Turney reviewed the key cost drivers for the two areas evaluated. The financial impact for records files managements, in terms of the process, is calculated to be $302,000 annually as a result of the consolidation. If you include the impact of the process improvements, the savings would go up to $477,000. The savings calculation from the project management evaluation was $307,000. Mr. Turney also discussed his findings relative to organizational overlap. Cost Technology identified four areas of overlap, including: administrative support, other support (primarily telephones), fleet management and security for the front desk. The savings associated with consolidating the four areas is approximately $340,000 annually. The total annual savings identified as a result of consolidation, including the extrapolated savings of $1.83 million, is $2.8 million. Mr. Turney said these savings are on the low end of the range; if they had not discounted the extrapolations, the savings would be $4.6 million.

Commissioner Waldron asked Mr. Turney how confident he is that the Port would save at least $3 million annually. Mr. Turney said he would bet his business and company reputation that the analysis is solid.

Mr. Turney said the consolidation is not about eliminating jobs; it is about making jobs better with less confusion and better transfer of knowledge, all through better-defined processes. He also said achieving these savings would require a commitment by all levels of management. Management must be committed, expectations must be communicated and performance must be tracked.

## Design and Cost Estimates

Doug Sams from ZGF reviewed the guiding principles used as benchmarks for the project, which are: create at least 3,000 public parking spaces and 500 rental car spaces; create a positive financial impact for both the Port's general fund and aviation; design and build a corporate headquarters that creates a positive image of the Port to the public, our customers and employees; create a consolidated office that supports a "one Port" environment; and provide close access to the PDX terminal building for employees.

Mr. Sams presented the HQP2 preliminary design. The total gross square footage of the new headquarters building will be roughly 171,000, or 155,000 net. Mr. Sams said the building would also allow for future growth of approximately 24,000-square-feet gross or 21,000-square-feet net.

Dan Brame, HQP2 Project Manager, discussed the current parking situation at PDX and the need for additional parking, as well as the plan to manage the parking demand during construction. Mr. Brame noted that HQ and P2 are two structures, and Hoffman Construction has come up with an idea to recover some of the parking spaces while still under construction by allowing cars in the north half of the structure as early as November 2008.

Mr. Brame noted there is a line item in the project budget for sustainability. He said a lot of thought was given to what type of sustainability features should be incorporated in the project. Tanya Starr led a team to come up with a program that is consistent with the Port's environmental goals. Mr. Brame said the major items include a renewable energy partnering program for a photo voltaic system, an automatic parking guidance system in P2, a living machine and geothermal heating and cool system with radiant ceiling panels.

Mr. Brame led a discussion of the preliminary cost estimates. He said we are at 30-percent design, so we know a lot more about what the project will look like. He said ZGF and Hoffman Construction reviewed the estimates independently. We also hired a third-party estimating firm, Rider Hunt, whose only involvement in the project was to review the ZGF plans and offer an independent estimate. Mr. Brame discussed the individual line items and noted the total project costs is $231 million. He said staff met with an independent review panel to gain insights on how we would compare our costs to a private development downtown. What they determined is that we pay a 15-percent premium. This is because of the significant foundations needed due to poor soil conditions at PDX; the regulatory oversight from the Federal Aviation Administration and TSA; the complexity of phasing/staging due to size, access and proximity to roads, parking and the air traffic control tower; as well as the additional costs of the atrium and elevated decks.

## Financial Analysis

Mr. Schreiber reviewed the key financial factors, the financial analysis and the financing plan. He said we will use a combination of cash on hand and debt to finance the project and noted that no state or local tax money will be used on this project. Mr. Schreiber reviewed the balance sheet impacts and said the General Fund and PDX balance sheets remain strong. He discussed the NPV financial impact over 20 years. Mr. Schreiber concluded with a summary of the financial benefits and other benefits.

Commissioner Johansen said there are two issues with the assumptions of the efficiency savings and the NPV of $30 million. She said this is difficult to grasp in a confident way. She said it is important for the Commission to understand that they are assuming that the savings will really materialize and it will not evaporate into something else. The other issue is the 15-percent premium for building at PDX versus downtown, combined with the aesthetics of the building; she believes people may not agree with the Commission's decision if we proceed.

Commissioner Waldron said the cynical view is that the new headquarters building is a wash, but we are moving $25 million into the General Fund by selling the downtown property. He also said this would allow Mr. Wyatt and the directors to better manage the Port, which is hard to quantify.

Commissioner Johansen said we have to ask ourselves why we are doing this; is it because we want a nice, new building and we want everyone together, or is it because we want to significantly improve the General Fund. She said we need to be clear that we are not doing this just for the $18 million NPV benefit.

Commissioner Olson said it is difficult to explain to the average person the restricted fund issue of the airport versus the General Fund. She said as Commissioners, they need to be cognizant of the fact that they are taking an asset in the General Fund and liquefying it for cash. Commissioner Olson said this would bring challenges to us because we will need to figure out how to leverage that for the items that are going to be necessary to take this Port to the next level. She said from a logical perspective, we are able to take cash that is sitting in a savings account at PDX and use it to help the General Fund, while in no way affecting the viability of the operations at PDX.

Commissioner Waldron said the upside of the consolidation is clear. He said the potential downsides would be employee acceptance, public acceptance and the risk of construction. Mr. Schreiber agreed that the area with the most risk is on the construction side. He said the Port has done a good job over time bringing projects in on budget and on schedule, so big projects are something with which we have a fair amount of experience. He also said he has never been involved with a project that has been reviewed as thoroughly as this one.

Commissioner Allen said while he is concerned about public perception, he is mostly concerned about the business community, political leaders and our stakeholders, and he believes they will look at the project and think it makes a lot of sense.

Mr. Wyatt outlined the next steps, including his recommendation on whether to proceed or not, which will be presented at the April Commission meeting, and the best way to proceed with the current headquarters building.

Commissioner Waldron said this is a creative idea and it has been a thoughtful process. The Commission has been provided with enough information to make an informative decision in April.

The meeting adjourned at 4:50 p.m.

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President

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Assistant Secretary

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Date Signed

A complete audio recording of these proceedings is available at the Port of Portland administrative offices, 121 N.W. Everett Street, Portland, Oregon 97209.

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